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Annual Economic Report 1985-86

A cooperative growth strategy for more employment

Annual Economic Review 1985-86

No 26 November 1985

'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 September, '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 July issue presents a report on the Community's borrowing and lending activities in the preceding year.

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

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

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Contents

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
EUR	Total of the Member States of the European Community
EUR 4	Federal Republic of Germany, France, Italy, United Kingdom
EUR 9	Community without Greece

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
YEN	Yen
CAD	Canadian dollar
ÖS	Austrian schilling

Other abbreviations

ACP	African, Caribbean and Pacific countries
ECSC	European Coal and Steel Community
EDF	European Development Fund
EIB	European Investment Bank
EMCF	European Monetary Cooperation Fund
EMS	European Monetary System
ERDF	European Regional Development Fund
Euratom	European Atomic Energy Community
Eurostat	Statistical Office of the European Communities
GDP (GNP)	Gross domestic (national) product
GFCF	Gross fixed capital formation
mio	Million
NCI	New Community Instrument
OCTs	Overseas Countries and Territories
OECD	Organization for Economic Cooperation and Development
OPEC	Organization of Petroleum Exporting Countries
SMEs	Small and medium-sized enterprises
SOEC	Statistical Office of the European Communities
toe	Tonnes of oil equivalent

Annual Economic Report 1984-85

'A cooperative growth strategy for more employment'

(Communication from the Commission to the Council)

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Part I — The Community economy

Introduction and summary

1. The present *Annual Economic Report* for 1985-86, here submitted to the Community institutions in accordance with regular procedures,[1] builds on the report which the Council adopted last year, the principal theme of which was the need to achieve a substantial and durable improvement in the employment situation. Its potential is increased by proposals for a cooperative strategy calling for balanced contributions from the Community, governments of Member States as well as from the social partners. This strategy will be even more effective if it can rely on international cooperation.

2. In 1984/85 the Community countries have achieved some progress in respect of economic policy:

(i) The moderate economic recovery, which has been under way for 2 ½ years, is continuing.

(ii) Considerable progress has been made towards restoring price stability.

(iii) There has been further improvement with respect to the budgetary and external imbalances.

3. These successes are grounds neither for complacency nor for hoping that the major problem of the Community — unemployment — will be resolved if current trends continue. Indeed, all medium- and long-term forecasts of growth and employment agree that, on the basis of present policies and behaviour, there is no prospect in the medium term of raising the growth rate in the Community above some 2 ½ %. This would not lead to a significant decline in unemployment in this decade. A disorderly adjustment process in the USA, a further rise in real interest rates and a worsening of the debt problem in developing countries could make the outlook even more gloomy.

The apparent inevitability of the prospect of persistently high unemployment has led to widespread pessimism with regard to economic policy. If the relationship between growth and employment observed in the 1960s still applied, medium-term growth rates above 6 % would be necessary to achieve the increase in employment (1-1 ½ % per year) that is needed in order to bring down unemployment gradually but significantly. Such rates of growth are at present quite unattainable. Consequently, the unemployment problem can only be solved if there is a distinct improvement in the relationship between growth and employment.

4. We should not, however, ignore the fact that the process of moderation of real wage increases established since the end of the 1970s has already helped to make growth potentially more employment-creating. The growth rates of recent years, however, were not sufficient to permit the necessary rise in employment. It is therefore necessary to strengthen growth in Europe further and to make it more employment-creating.

5. In order to achieve this objective, a series of macroeconomic and microeconomic conditions need to be fulfilled to the greatest possible extent.

5.1 At the macroeconomic level, it depends in particular on a higher level of job-creating investment in the coming years. This is first of all the task of entrepreneurs. It is, however, also necessary that the profitability of job-creating investment should continue to improve, and that there is a sufficiently strong outlook for demand. Job-creating investment is mostly capital-widening investment, requiring favourable prospects for demand and the continuation for a certain period of moderation of real wage increases at a rate lagging behind productivity growth. If wages were to rise too fast, profitability would suffer and rationalization (capital-deepening investment), which destroys jobs, would be unnecessarily encouraged. Avoiding such an eventuality in no way implies that technological progress should be relinquished; job-creating investment also incorporates technological progress. But because of the inadequate capital stock and the high unemployment rate, Europe needs for some years a new balance between capital-widening and capital-deepening investment.

5.2 The combination of moderate real wage increases and safeguarding an appropriate development of demand is also an important element in improving profitability, strengthening growth and making it more employment-creating. Wage moderation alone would not, or only very slowly, lead to the required employment effects. Simply expanding demand would, given the inadequate level of productive capacity, run the risk of producing higher inflation and/or public debt without having the desired effect on employment. A combination of both is therefore necessary.

[1] The Commission's proposed *Annual Economic Report* is submitted to Community institutions in accordance with the Council's 1974 Decision for attainment of a high degree of convergence of economic policies of Member States (Article 4 of Decision 74/120/EEC of 18.2.1974, amended by Decision 75/787/EEC of 18.12.1975). The Council is required in the fourth quarter of each year — on proposal of the Commission and after consulting Parliament and the Economic and Social Committee — to adopt an annual report on the economic situation in the Community and to set economic policy guidelines to be followed by each Member State. As in previous years, the services of the Commission are preparing, as a separate background document, an *Annual Economic Review* which contains a more detailed factual analysis of economic trends and the outlook for the year ahead. This second document is for the information of the Council, Parliament and the Economic and Social Committee.

5.3 With respect to the maintenance of moderate real wage increases, which has been achieved in many countries in recent years, the cooperation of the social partners, and in particular of the unions, is required. Moderate wage development should continue until there is a clear and lasting fall in the unemployment rate, after which real wage increases could again become close to productivity growth.

5.4 The safeguarding of an adequate level of demand is the task of government, to be carried out until the process becomes self-sustaining by means of strong investment and an appropriate rise in private consumption.

5.5 What Europe needs is a dual strategy of moderation of real wage increases and support for demand. Indeed, the accompanying measures to underpin demand hold the key to the success of the strategy and social acceptance of wage moderation. This is, at any event, true in a transitional phase during which consumer purchasing power will, to begin with, inevitably grow more slowly and aggregate demand will not rise at a sufficiently rapid pace as a result of extra business investment to expand capacity.

Only if wage moderation is accompanied by a sufficient level of aggregate demand can one have confidence that the process of improving profitability and restructuring demand (relatively more investment and relatively less consumption) will be rapid enough and not involve drastic deflation that would place social consensus under considerable strain. Only in this way can wage moderation fulfil its employment function.

5.6 As a result, the long-term tendency for capital productivity to decline would also be arrested. Together with rising employment, growing demand and mounting confidence in future trends, this would provide the most effective stimulus to the propensity to invest. As investment rises, more rapid technological progress would at the same time be incorporated into the productive apparatus, and this would in turn have a beneficial effect on the productivity of labour and capital. Profitability and the propensity to invest would therefore continue to increase. This would create a 'virtuous circle' of technological progress, capital productivity, profitability, investment and renewed embodiment of technological progress.

6. The strategy proposed in this *Annual Economic Report*, however, consists not only of macroeconomic elements. Employment-creating growth also depends upon important microeconomic conditions. Action, with the aim of improving the adaptability of markets, and not only the labour market, should be reinforced. With regard to the labour market, the extent to which greater wage differentiation and reorganization and reductions of working time, without raising costs, could benefit employment should be studied in the light of results already achieved. The national governments and the Community should also examine whether existing rules and regulations impede the functioning of markets and the setting up of new, and in particular small and medium-sized businesses.

The spirit in which the debate about market adaptability is held is important for its success. The objective behind efforts to increase flexibility is not to destroy achievements made on the social front but to create more jobs. As far as at all possible, therefore, economic efficiency should be reconciled with the maintenance and further development of social achievements.

7. The central strategy of moderate growth of real wages accompanied by the maintenance of an adequate level of demand requires the monetary and budgetary policies of the Member States to be based on the following principles:

7.1 *Monetary policy* must continue to provide the framework for stability. The proposed dual strategy must thus not lead to an acceleration of inflation. On the contrary, in most Community countries, the rates of inflation need to be brought down further. Monetary policy can best safeguard this, within the EMS framework, by continuing to set a nominal framework which is oriented towards economic stability. Such a monetary policy offers considerable potential for cuts in interest rates in the Community on a sound basis, particularly if the dollar falls further. If this could be achieved, with the necessary caution and coordinated within the EMS framework, it would add an additional, not inconsiderable stimulus to business investment and significantly reduce pressure on government budgets. This is a positive effect benefiting all countries.

7.2 *Budgetary policy* must underpin the strategy of employment-creating growth in the following ways:

Macroeconomically, it must continue to safeguard the consolidation objective, i.e. deficits must be further reduced in those countries which still have a level of indebtedness which is either excessive or rising too fast. At the same time, it must sustain demand where there is room for manoeuvre, the more so since wage moderation leads temporarily to a fall-off in demand. In addition, budgetary policy should continue to restructure the expenditure side of the public budgets to reduce subsidies more strongly and in a selective way and to increase public investment; particularly in respect of infrastructure, environmental protection and urban

renewal, a considerable backlog of needs has built up in recent years, which could be met with the spare capacity in the construction sector.

Budgetary policy should also provide for further measures to strengthen supply, which generally have an impact on demand at the same time, and safeguard the improvement in relative factor prices by reducing taxes and social security contributions — wherever possible, at the expense of the central government budget. In addition, microeconomic measures to promote employment (job-creation schemes and promotion of vocational training) should be taken wherever possible.

8. The success of the proposed strategy depends on a coordinated application of policies between Member States within a Community framework.

The economic potential of the Community will be considerably reinforced by the accelerated completion of the large internal market including the liberalization of national financial markets and by the promotion of technical progress, as the Commission has proposed. The completion of the internal market lies at the heart of the Community; by generating supply dynamism and by permitting, at the same time, a more sustained growth in demand, it ties in directly to the cooperative macroeconomic strategy. The promotion of technical progress is essential to safeguard and promote the Community's position among the most developed economies of the world. In addition, in those sectors for which the Community is directly responsible, a greater weight should be given to the operation of the market. In all these areas, the social dimension should be taken fully into account.

The realization of major infrastructure projects in the transport, telecommunications and environmental fields, as well as exploitation of technological potential, would substantially improve the functioning of the internal market. The accelerated implementation of numerous projects, which are already available and have an adequate social rate of return, would reinforce economic dynamism and contribute to the success of the proposed strategy.

Finally, given the importance of a favourable international environment for growth and employment, the Community should at the same time continue its efforts to improve the international trading and monetary systems. It should also, together with other countries, attempt to mitigate the debt problem of developing countries, and to work towards maintaining the growth in world trade as the inevitable adjustments in the USA are made.

The contributions of the Community referred to here correspond to numerous resolutions of the European Parliament.

9. Whatever the international environment, the policies set out above are necessary. It is evident that the international environment would be considerably reinforced by the success of the Community strategy. Given a plausible margin of uncertainty as far as world developments are concerned, such a policy should make possible the achievement of an increase in the economic growth rate in the Community from its present level of 2 ½ % to an average of 3-3 ½ % over the next few years, and at the same time make growth much more employment-creating. This would produce an average annual increase of 1-1 ½ % in employment, opening up the prospect of unemployment being brought down to around 7 % by 1990.

10. Such a development is only possible, however, when all concerned — the Community, national governments, employers and unions — work fully together to implement the proposed strategy.

10.1 This overall strategy 'offers' governments and the social partners an opportunity to achieve a joint solution to the major problem confronting the Community, namely unemployment. However, the strategy provides only a general framework within which much of the debate should be held with the governments and with and between the social partners. This general framework should also incite those concerned at least to reflect upon their respective positions. For the present, there is no political approach in sight other than this strategy providing any prospect of significantly reducing unemployment by the end of the decade. It is therefore an urgent task to proceed via a wide debate to the implementation of this cooperative strategy.

10.2 Exploratory discussions which the Commission has had with the European Trade Union Confederation (ETUC) and with the Union of Industries of the European Community (Unice) have been encouraging. They have shown that there is interest and a willingness to talk about such an approach. This dialogue should be continued.[1] It is evident that social dialogue should also be reinforced at national level. The more progress is made in such dialogue at all levels, the easier it will be for the national governments and the Community itself to make their own contributions.

[1] The Commission will thus ask the ETUC and Unice for written opinions on the draft *Annual Economic Report*. These opinions will be transmitted to the Council, Parliament and the Economic and Social Committee so that they can be borne in mind in the future discussion.

10.3 The strategy should gradually be transformed into reality. This applies to the cooperation in each country between governments, unions and employers. Each should make their contribution and at yearly intervals the progress should be examined in order to determine the next steps. This approach should continue over several years. This also applies, however, to cooperation between the Community countries and at an international level. Each partner should act according to their available room for manoeuvre.

11. The coordinated application of the strategy in the Member States should engage and foster a mutually reinforcing process of supply, demand and employment. In this respect an analysis of developments forecast for Germany in 1986 are of considerable interest. Economic growth could exceed 3 % and employment could rise by more than 1 %, so that unemployment declines, albeit slowly at first. The price outlook continues to be favourable. A considerable current account surplus and, despite the tax reform, a further significant decline in the government deficit is expected. Thus, a positive chain reaction is developing between price stability, more growth and employment and more room for manoeuvre in the fiscal and external fields. This room should be used for higher public investment in 1986 and bringing forward to 1987 the tax reform planned for 1988. This appears necessary so that the favourable economic development continues in and beyond 1987.

Even in Germany it is necessary to have a growth rate of some 3,5 % and a rise in employment of about 1,5 % per annum for several years in order to achieve a lasting decline in unemployment. This is in both the national and the Community interest.

11.1 In the other countries such room for manoeuvre is not yet available. In some of the countries, however, it is possible that, with a certain time-lag as compared to Germany, a similar positive chain reaction could develop from more growth and employment to greater room for manoeuvre on the fiscal and external fronts. Such a development seems possible in Denmark, the Netherlands, the United Kingdom and France. Its speed will depend upon how favourably developments proceed in Germany and upon appropriate behaviour of the social partners in relation to the requirements of the strategy. Every effort should be made to extend the positive chain reaction as quickly as possible to this group of countries. This would also considerably improve the situation in the third group of countries where room for manoeuvre is not yet in view.

11.2 The differing situations in the Member States naturally restrict a rapid implementation of the proposed cooperative strategy. In this respect, the Community's contribution could provide a certain compensating factor. This refers not only to the accelerated completion of the internal market but above all to the large projects of the Community interest in the fields of transport and telecommunications infrastructure and of environmental protection. The stronger the commitment of governments and the social partners to the implementation of the overall strategy, the greater the chance that the Community's contribution will succeed in being of significant macroeconomic importance.

1. Evolution of the economy and convergence

1.1. The current situation and outlook for Europe

The present European recovery so far has lasted about 2 ½ years. From a starting point dominated by structural imbalances accumulated over a long period as evidenced by large budget deficits, high and continuing inflation, poor growth performance and a highly unsatisfactory labour market situation, policy management has relied heavily on supply-side considerations. Moreover, the degree of imbalance as between member countries has varied greatly across the Community.

By mid-1985 gross domestic product in the EC had risen to nearly 5 percentage points above the previous cyclical peak of 1980. Industrial production, which suffered a deeper recession than the rest of the economy, also returned to the 1980 peak level in June 1985. The Commission's recent forecasts[1] point to a continuation of this trend, with a growth rate of about 2 ½ % for the Community as a whole being forecast for 1986, which is marginally more than that expected for 1985.

The outlook for growth, therefore, remains one of modest proportions. Even so, in a number of respects, there have been positive signs of progress in some areas. There has been a general awareness that, starting from a position of acute imbalance coupled with a world recession, the adjustment necessary would be a slow one. Moreover, the degree of imbalance in Member States is by no means the same. The fundamental approach suggested by the Commission in the last two annual reports has been to stress the need for improvements to supply conditions in member countries set within a framework of control over national budgets. A component judged necessary in this approach has been to ensure that the evolution of real employment costs continues to be maintained below the growth of productivity.

Experience across Member States has varied a good deal but looking at average Community performance over the past year, there are some encouraging signs. To a degree, there has been real wage moderation. Of significance is the fact that after a decade in which the creation of new jobs has been negative, the Community is beginning to experience some growth in employment. Table 1 shows that for 1985 employment growth is estimated to be 0,4 % with an increase to 0,5 % for 1986.

[1] Commission of the EC, *European Economy*, Supplement A, October 1985.

Table 1

Main economic aggregates, EC,[2] 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current account of balance of payments	General government net lending or borrowing	Money supply (M2/3)[3]	Unemployment (% of labour force)	Employment
	%change	% change	% change	% change	% change	% of GDP	% of GDP	% change	%	% change
1961-70	9,0	4,6	4,2	3,7	8,8	0,4	−0,4	10,2	2,1	0,2
1971-80	13,4	2,9	10,2	10,1	13,6	−0,1	−2,8	14,4	4,2	0,2
1981	10,4	−0,2	10,6	11,7	12,6	−0,5	−5,4	10,9	7,6	−1,3
1982	10,7	0,5	10,1	9,8	10,6	−0,6	−5,6	10,7	9,2	−1,4
1983	8,9	1,0	7,8	7,6	8,7	0,1	−5,5	9,7	10,3	−0,5
1984	8,0	2,2	5,7	6,2	6,7	0,1	−5,4	8,7	10,8	0,2
1985										
Last report	(7,5)	(2,3)	(5,0)	(5,2)	(6,7)	(0,3)	(−4,8)	(7,2)	(11,5)	(0,0)
This report[1]	7,6	2,3	5,1	5,2	6,3	0,5	−5,2	8,4	11,1	0,4
1986[1]	6,7	2,5	4,1	3,9	5,4	0,6	−4,8	6,7	11,1	0,5

[1] Forecast of the Commission services, on the basis of present policies, September 1985.
[2] EC average calculated with current GDP weights at purchasing power parities.
[3] End of year (annual growth rate).

Note: Percentage changes are given as annual rates.

Table 2

World imports of goods

(% increase in volume)

	1981	1982	1983	1984	1985	1986
EUR	−2,9	2,4	2,3	7,1	5,0	5,3
US	6,6	0,1	11,8	29,9	10,0	6,6
Japan	−2,4	−0,6	0,3	10,7	3,0	4,7
OPEC	27,4	5,5	−8,2	−9,0	−10,9	−4,0
Other developing countries	3,5	−5,2	−1,2	6,0	4,0	4,5
World	2,5	−0,1	2,2	9,3	4,8	4,8

Source: Commission services.

By far the greater part of this growth, however, has come from increases in activity rates, particularly of women, and new entrants to the labour force. To begin to have an effect on the current and widespread unemployment problem therefore, it is necessary that this progress be improved upon and continued into the medium term. When appraised in such terms, it is clear that the situation reached remains fragile and this report acknowledges that future progress will be difficult if both policy and behaviour are not changed.

Table 3

Rate of change of demand components, EC

	1982	1983	1984	1985	1986
Private consumption	0,5	1,1	1,0	1,7	2,7
Public consumption	1,1	1,6	1,2	1,2	1,1
Fixed investment	−1,6	0,0	2,3	1,6	3,7
Contribution to change in GDP of:					
Final domestic demand[1, 2]	0,2	1,0	1,3	1,6	2,5
change in stocks[1]	0,5	−0,2	0,5	0,2	0,1
foreign balance[1]	−0,3	0,1	0,2	0,4	−0,2
GDP	0,5	1,0	2,2	2,3	2,5
Exports	1,5	1,9	7,2	6,4	4,6
Imports	2,6	1,5	6,6	5,0	5,3

[1] Change as percentage of GDP of preceding period.
[2] Excluding change in stocks.
Source: Commission services.

In some contrast to the relatively subdued growth in Europe, the international economy has been undergoing a much more marked cyclical development. For the United States, 1984 was a year of exceptionally strong output growth (+6,8 %) and even more so of imports (+30 %). With Japanese imports also growing fast in that year (+10,7 %), total world trade grew by as much as 9,3 %. For 1985 world trade growth is estimated to slow to a more normal rate (4,8 %) and on present forecasts a similar result is expected in 1986. This is subject, however, to a number of uncertainties which are discussed briefly in a later section. The forecast includes a more moderate but still positive rate of output growth in the United States economy (+2,3 % in 1985, +2,5 % in 1986) and a sustained growth rate of 4 -5 % in Japan in both years.

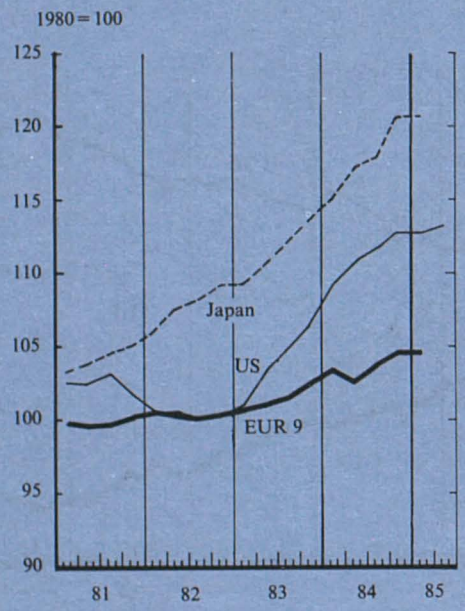
It may be questioned why the European economy did not respond more strongly to the acceleration of world trade that occurred in 1984. It is indeed striking that while Community exports grew by 7,7 % in 1984, imports grew almost as much by 7,1 % compared to the modest 2 % growth of domestic demand. As a result, the net impact of export and import trade volume growth was negligible. However, special factors such as strikes in the UK coal industry and German metal industries, together with a relatively high rate of stockbuilding of high import content help to explain why this happened. For 1986 the forecasts suggest a continued gradual strengthening of domestic demand.

This view is supported by evidence from surveys of both business and consumer opinion. The industrial confidence indicator for the EC as a whole has improved only very slightly over the 12 months to September 1985. Confidence in the construction sector remains very depressed. Consumer confidence recovered only a little in 1983 measured from the low-points reached in preceding recession years but since then has remained stable. The remaining component of the Commission's composite economic sentiment indicator, and the only one to have risen at all significantly over the last year, is the share price index.

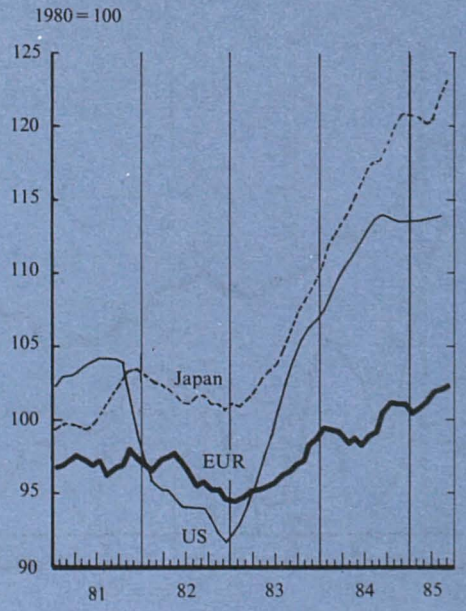
The rise in the share price index may be associated with the welcome rise in private industrial investment, which in Europe as a whole is now the fastest growing demand component. After three years of decline in 1981 to 1983 a recovery began in 1984, with a 7 % volume rise in industrial investment. First indications for 1985 from business survey sources pointed to a 9 % volume rise, and more recent surveys have revised this up to 11 %. Within these EC average figures there are some examples of a much stronger private industrial investment upswing. In Denmark, for example, the growth rate is estimated to be nearly 40 % and for the Netherlands over 20 % in both 1984 and 1985. In

GRAPHS 1 to 4: **Comparative evolution of the EC, US and Japanese economies, 1980-85**

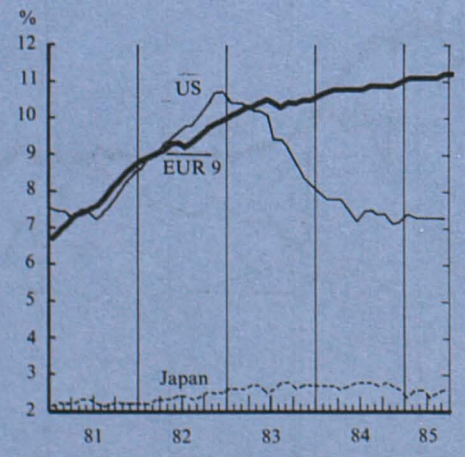
1. Gross domestic product, s.a.



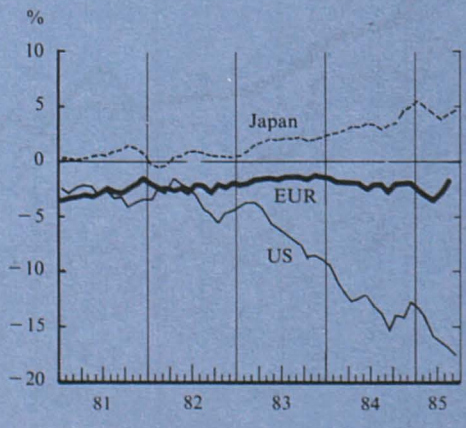
2. Industrial production
3-month moving average, s.a.



3. Unemployment rate

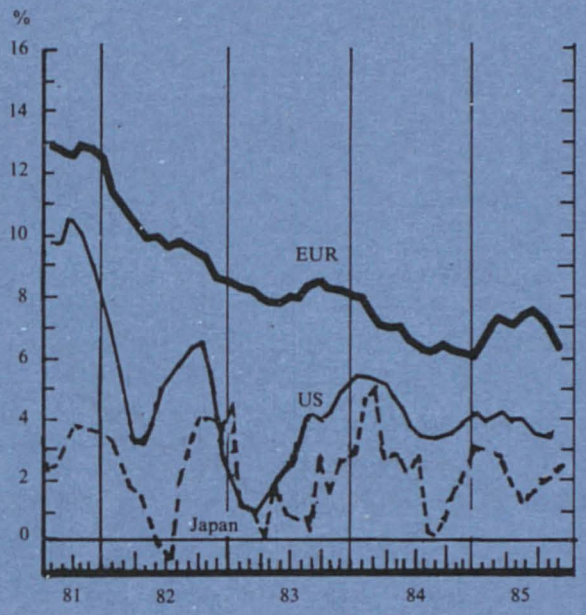


4. Trade balance
fob/cif, '000 million ECU
3-month moving average, s.a.

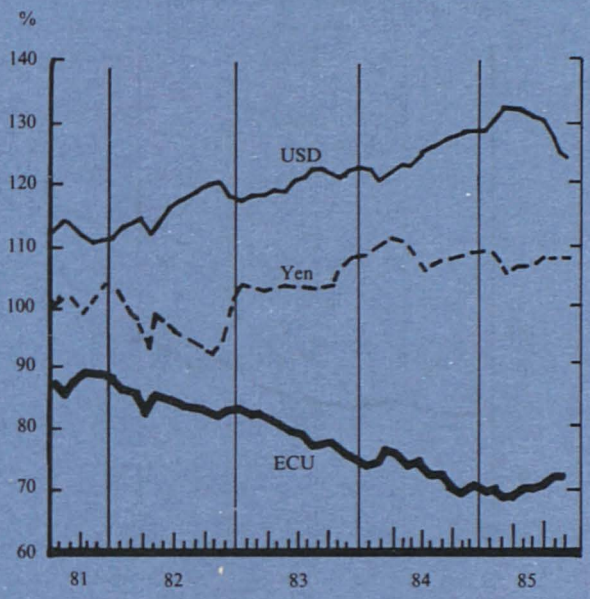


GRAPHS 5 to 8: **Comparative evolution of the EC, US and Japanese economies, 1980-85**

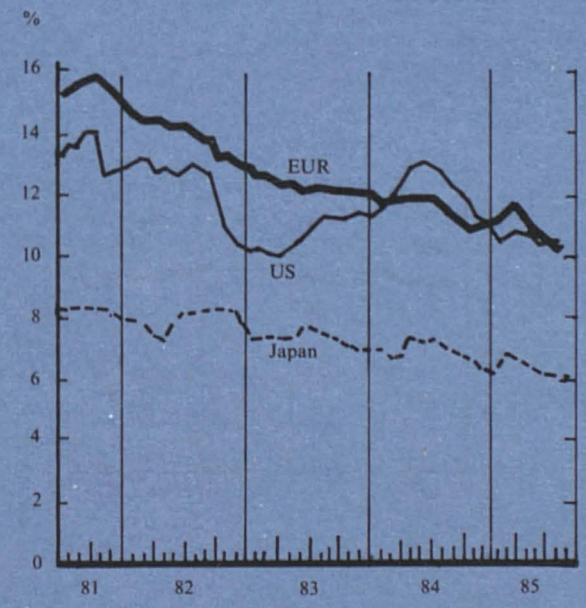
5. Consumer prices
6-month change, s.a., annual rates



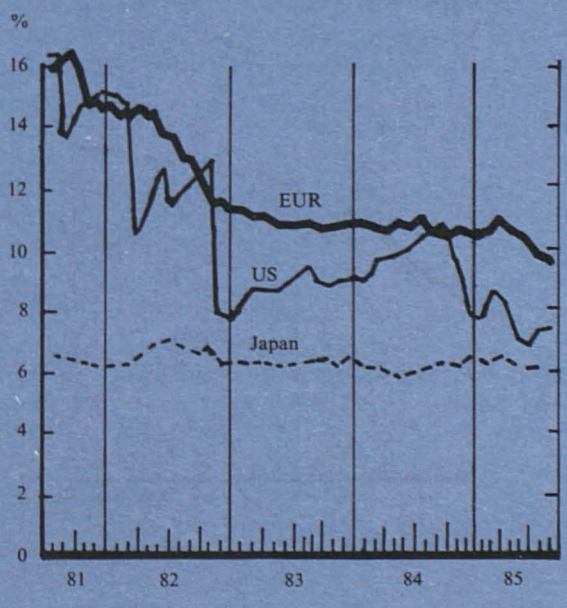
6. Exchange rates
Index of SDRs per currency unit
March 1979 = 100



7. Long-term interest rates



8. Short-term interest rates



1985 German industrial investment is expected to rise by 13 % in volume.

Of considerable significance, however, is the fact that the level of investment is still low. In 1985 the volume of investment is only that attained in 1980. It is still some 14 % below the level in 1973. Sustained and substantial rises in investment are now required if the economy's potential growth rate is to be improved. Additional evidence is provided by the behaviour of capacity utilization. Despite slow output growth, capacity utilization in industry rose to 82 % in July 1985, which is close to the 84 % level recorded at the cyclical peak in 1979-80. Thus in spite of the existence of high unemployment, the European economy is already beginning to experience production capacity constraints.

As already noted, in the meantime, total employment has increased modestly. Indeed, employment growth of over 1 % is expected in 1985 in Denmark and the United Kingdom, but even this is clearly insufficient given the growth of labour supply and the high unemployment level at the beginning of the recovery.

After a long period in which Europe has demonstrated a remarkable incapacity to create new jobs, these signs are indeed welcome. They do, however, underline the need to strengthen further those conditions necessary to secure sustained growth embodying employment creation.

The present European recovery, so far of two-and-a-half years duration, is expected to continue through 1986 at a growth rate around 2 ½ %. Although private industrial investment is showing a significant upturn, this is from a very low base. More recently employment has also begun to increase. However, there are indications that in some countries, despite the presence of continuing, unacceptably high unemployment, the economy is beginning to experience capacity constraints. This emphasises the need for sustained growth of investment in new capacity.

Table 4

Forecast increase in gross domestic product in 1985 and 1986

(%)

	1985			1986		
	Nominal GDP	GDP output volume	GDP price deflator	Nominal GDP	GDP output volume	GDP price deflator
B	6,7	1,9	4,7	6,2	1,7	4,4
DK	6,3	2,3	3,9	5,4	3,2	2,2
D	4,4	2,3	2,1	5,4	3,5	1,9
GR	19,3	1,9	17,1	16,8	1,0	15,7
F	7,0	1,2	5,7	5,8	1,9	3,9
IRL	8,7	2,5	6,1	7,5	2,3	5,0
I	11,0	2,7	8,1	9,5	2,7	6,6
L	6,0	1,7	4,2	6,4	1,3	5,0
NL	4,5	2,1	2,3	3,0	2,0	1,0
UK	9,1	3,4	5,5	7,0	2,0	4,8
EUR	7,6	2,3	5,1	6,7	2,5	4,1

Source: Commission services.

1.2. Imbalances and convergence in the EC economy

The situation in 1985 may be compared with that in 1980, a period which conveniently spans a business cycle. In 1980 as in 1985, a moderate economic recovery had been under way for about two-and-a-half years, and capacity utilization rates in industry were similar. Some of the more important macroeconomic indicators are set out in Table 5.

In the labour market, the four larger Member States have experienced a rise in the rate of unemployment of between 4 and 6 percentage points. Among the smaller countries Belgium, the Netherlands and Ireland have suffered higher than average increases. In so far as a convergence process is at work here the similarity of the growth in unemployment is striking and this development remains wholly unacceptable.

Although employment growth has become positive in the last year, in no country except Denmark is the level of employment currently higher than it was at the beginning of the decade. Thus virtually the whole of the Community is facing a labour market problem of comparable gravity.

As regards price stabilization, on the whole there has been a striking and positive convergence process. Germany and the Netherlands have reduced their already below-average inflation rates to a very low level. The United Kingdom, Ireland and Italy have reduced their inflation rates from 1980 to 1985 by well over 10 percentage points, and France by over 6 points. Denmark has also made notable progress in achieving a measure of price stabilization. Greece has not progressed in this respect.

On the balance of payments the Community as a whole has moved from substantial current account deficit in 1980 to a surplus in 1985, but divergences in individual performance remain considerable. In addition, when seen against the very large current account deficit of the United States, the Community retains a degree of vulnerability in this respect. The most impressive adjustments have been those of Belgium and Ireland which improved their current account positions by 5 % and 9 % of GDP respectively over the five-year period, thus eliminating or very much reducing their previously alarming deficit levels. France and Italy have also made substantial progress in reducing their deficits, even if more recently in the Italian case the deficit has begun to grow again. Germany and the Netherlands on the other hand have moved into situations of widening surplus.

Table 5

Indicators of disequilibria and divergence, 1980 and 1985

	Unemployment %		GDP deflator %		Current account % of GDP		Budget deficit % of GDP		Gross public debt % of GDP	
	1980	1985	1980	1985	1980	1985	1980	1985	1980	1985
B	9,1	13,8	3,9	4,7	−4,5	0,6	−9,9	−8,6	76,1	116,0
DK	6,7	9,1	8,2	3,9	−3,7	−3,4	−3,3	−2,9	33,5	68,6
D	3,3	8,4	4,3	2,1	−1,8	2,1	−3,1	−1,2	32,6	42,6
GR	:	8,3	17,7	17,1	0,3	−5,2	−5,4	−12,5	27,7	54,5
F	6,4	10,7	12,2	5,7	−1,4	−0,5	0,3	−3,2	25,0	35,9
IRL	8,2	17,1	14,2	6,1	−12,0	−3,3	−11,8	−11,5	85,9	124,3
I	7,1	12,6	20,6	8,1	−2,5	−1,7	−8,4	−13,6	93,9	120,4
L	0,7	1,7	7,8	4,2	"	"	−0,8	2,1	13,6	15,6
NL	6,2	13,2	5,7	2,3	−1,5	4,5	−4,0	−5,9	45,9	72,3
UK	6,0	12,0	19,8	5,5	1,8	1,1	−3,4	−3,3	59,7	59,7
EUR 10	5,8	11,2	12,6	5,1	−1,3	0,5	−3,5	−5,2	50,5	64,3

Source: Commission services.

In spite of the severity of budget consolidation efforts, EC government deficits in 1985 are, on average, significantly higher than in 1980 (5,2 % of GDP versus 3,5 %). Moreover, in this area also the degree of divergence continues to be relatively wide. Four countries (Belgium, Greece, Ireland and Italy) have deficits of nearly 10 % of GDP or more. Belgium and Ireland despite considerable efforts have not been able to reduce substantially the deficit level over the five-year period, even if over a more recent period some improvement has been made. The Greek and Italian deficits have become more serious still. Germany has reduced its deficit to 1,2 % of GDP, whilst Luxembourg has moved into surplus. France, the UK and Denmark are now in an intermediary category with deficits of around 3 % of GDP.

Over the five-year period, virtually all countries have seen a substantial build up in their stock of public debt. The levels however are very different. The gross stock of public debt in Germany, France and the UK appears to be of relatively moderate size (40 %, 30 % and 60 % of GDP respectively). The debt levels of Belgium, Ireland and Italy are much larger (well over 100 % of GDP), and the interest rate burden in these countries is now in the region of 20-25 % of total current public expenditure and some 10 % of GDP.

Virtually no country has avoided a very large rise in unemployment, which has thus become the most serious imbalance in the European economy. As regards the other imbalances:

(i) Germany has achieved a broadly satisfactory position, but is accumulating an increasing current account surplus;

(ii) France and the United Kingdom have succeeded in reducing these imbalances to more moderate proportions;

(iii) Italy has made considerable progress on inflation and until recently on the balance of payments, but still has a grave public finance problem to overcome;

(iv) the other countries are mostly in rather hetereogeneous situations, with success on some scores but problems on others. Denmark has the most generally improved situation. Greece has problems on most accounts.

1.3. Some risk factors in the medium-term outlook

Under the assumption of an approximately stable influence from the rest of the world on the European economy, and with broadly unchanged policies and economic behaviour in the Community, the Commission would expect a rather steady medium-term economic growth rate of about 2 ½ % per annum in the EC, on average, for the rest of the present decade. Inflation might stablize at around 4 % on average, with nominal GDP therefore growing by nearly 7 % per annum. Unemployment would not fall significantly, and thus the central employment problem internal to the European economy would remain. There is little hope that it could be alleviated by the end of the decade.

However the assumption of a stable international economy may well not hold and before turning to the Community's domestic objectives and policies it is necessary to consider the sensitivity of the European economy to possible international events. Indeed the past decade has seen a sequence of massive world economic shocks: oil price rises, large exchange and interest rate movements, debt crises. For the next few years potential external sources of disturbance would lie primarily in the manner in which the process of correction of the US external deficit and related budget deficit and exchange rate imbalance takes place, and a resurgence of the debt crisis. A large fall in the price of oil would have positive and negative effects.

Some very approximate orders of magnitude are given in Table 6. It should be stressed, however, that in principle, a wide range of different estimates could be discussed, de-

Table 6

Sensitivity of the EC economy to changes in the world economic environment

(%)

	Impact on EC, cumulative total for three years on levels of:		
	output	prices	nominal GDP
US budget restriction in three successive years of 1% of GDP per annum, cumulatively	− ¾	− ½	− 1 ¼
US exchange rate depreciation of 20%[1]	− 1 ¼	− 2 ½	− 3 ¾
US budget restriction and exchange rate depreciation combined	−2	−3	−5
Monetary conditions permitting a 2% fall in European real interest rates	+ ⅔	—	+ ⅔
Fall in oil price of 20% with respect to the 1985 level	+ ⅔	− 1	− ⅓

[1] With respect to the ECU and yen.

Source: Estimates of the Commission services.

pending on assumptions about particular circumstances and on different reactions in private markets as well as official policies.

The broad picture which emerges is that, as regards the level of output in the EC, there are both negative and positive risks inherent in the potential disturbances considered, although the negative risks look on balance to be greater. As regards the rate of inflation there are possibilities for significant disinflationary impacts but none that appear likely to increase inflation significantly.

The actual position in the United States and what developments are likely over the medium term remain debatable. On this score it must be admitted that the degree of uncertainty on such matters as future US growth, its budget and external deficits, and the behaviour of interest rates and the dollar exchange rate is large. In the absence of any firm view, one can only resort to some stylized assumptions. Thus for illustrative purposes, what might be judged to be a substantial budgetary contraction, or a substantial exchange rate depreciation would (in the amounts specified in Table 6) lower the level of output in the EC by amounts in the range of ¾ to 1 ¼ percentage points for three years taken cumulatively.

Each element on its own would therefore represent a small but not trivial set-back to the European recovery. Taken together, however, the impact becomes considerable.

These estimates already take into account some decoupling of European interest rates from those in the United States (in the sense of relatively lower European rates). The magnitude of such changes is hard to judge. However, if one supposed that an extra margin of 2 percentage points reduction in European interest rates became possible, for example as a reaction to a very sharp weakening of the dollar, there might be a compensating boost to activity in Europe of around two-thirds of a percentage point cumulatively over three years.

A substantial fall (20 %) in the price of oil would have a beneficial impact on conjunctural trends in the EC. (The fiscal aspects of such a development are treated in section III.1.2.) This is estimated at cumulating to two-thirds of 1 % of GDP over three years, but the margin of uncertainty here is wide. Real incomes of companies and households would gain on the terms of trade, which would stimulate investment and consumption. However, oil and gas producers would lose incomes. Western Europe produces a substantial part of its own oil and gas (taking production of the UK, the Netherlands and Norway as a share of EC and EFTA demand). Exports to OPEC countries would surely weaken.

The disinflationary impact would be considerable in the event of a substantial dollar exchange rate fall (2 ½ % off the EC price level after three years with a 20 % depreciation against the ECU). The 20 % fall in the price of oil would also have a significant but smaller disinflationary impact.

One of the main issues arising from these scenarios is how to judge reactions to a simultaneous weakening in the EC of both output and inflation. In some of the hypotheses discussed there would remain a significant reduction in aggregate nominal demand. Compensatory policy reactions would then need to be considered, especially in countries which have already made good progress in reducing inflation (see further below in relevant policy sections of this report).

Potential disturbances in the international economy over the foreseeable future (adjustments in the US, a possible fall in the price of oil) point to the possibility of further reductions in inflation in the EC. As regards the level of output there are different risks arising from negative and positive impacts from the rest of the world; the negative risks seem to be greater. In the event of external conditions transmitting disinflation and real contractionary influences to the EC at the same time, the question of the adequacy of nominal demand would arise.

2. A cooperative strategy for more employment-creating growth

2.1. The background and orders of magnitude

The principal theme of this report is focused on the prime necessity of renewed economic growth but of a character which will begin to create a significant number of new jobs and thus represent a step towards solving the problem of unemployment.[1] Initially therefore, it is useful to outline the medium-term prospect for Europe in the absence of any significant changes to international trends and to existing policy and behaviour. In other words how might the output, employment and unemployment situations in Europe unfold if, at the broad macroeconomic level, recent trends were maintained. Projections of this nature, whilst difficult to make, nevertheless are necessary as a means of assisting in the policy judgement process.

Recognizing the well-known limitations of model-based scenarios, present policies and trends are represented in the

[1] Apart from the programme for European economic recovery, adopted in March 1984, the European Parliament has advocated on many occasions an employment-generating investment effort (see Resolution, OJ C 122/57, 16.4.1985, point 4).

first column of Table 7 by a 'baseline assumption'. In this initial entirely illustrative case GDP growth in the EC as a whole is seen to be stabilizing at around 2 ½ % until the end of the decade, with inflation decelerating further to a little over 4 % and nominal GDP thus growing between 6 ½ % and 7 % a year. Budget deficits would be further reduced, and money supply kept to near its present growth rate. Labour productivity might increase by about as much as that observed during the last decade, at a little over 2 % per year. Real wages might grow a little below 2 %, thus allowing for some modest improvement in the share of profits in national income. Investment would be growing faster than GDP, perhaps 5 % per year, reflecting some response to the more recent slowdown in the rate of technological advance and to the restructuring needs of the economy.

In these conditions the rate of return on invested capital would not increase very substantially. In particular the cost of labour relative to the rate of return on fixed capital would not change markedly. Employment growth would be quite modest, perhaps not quite 0,5 % per year, albeit better, however, than the recent record of stagnant or declining employment. Unemployment might then decline only very slightly, maybe to 10 ½ % by 1990.

The characteristics of this assumed baseline projection, although disappointing, are not unreasonable given the fact that currently in Europe it remains questionable as to whether the unemployment level has stabilized when the economic growth rate is around 2 ½ %. What the baseline projection underlines is the strong likelihood that it will require a set of policy changes and behavioural changes to be introduced and maintained if the growth path for output and employment is to be improved in a significant way.

Given the improved situation with respect to budget deficits shown in the baseline projection, a more obvious suggestion might be to adopt a policy of pronounced budgetary expansion. Although this particular course is not the

Table 7

Some illustrative orders of magnitude in a baseline scenario and in an employment growth scenario, EC, 1986-90

(annual average growth rates)

	Baseline scenario	Fiscal reflation scenario	Cooperative growth scenario	(EC scenario without international cooperation)
GDP, volume growth	2,5	3,4	3,5	(3,2)
GDP deflator	4,2	5,4	3,7	(4,0)
GDP, nominal	6,7	8,8	7,2	(7,2)
Investment	5,0	5,1	6,6	(5,9)
Employment	0,4	0,8	1,1	(1,0)
Unemployment rate[1]	10,4	8,5	7,0	(7,4)
Labour productivity	2,2	2,6	2,4	(2,2)
Real wage cost	1,7	2,5	1,0	(1,0)
Profit share in national income	1,1	−0,8	3,8	(3,3)
Budget balance[2]	−3,8	−7,1	−4,0	(−4,4)
Rate of interest[3]	10,9	12,5	8,3	(9,4)

[1] Percentage of total labour force at end of period.
[2] Percentage of GDP at end of period.
[3] Long term rate of interest at end of period.

Source: Estimates of the Commission services.

Note

(i) The 'baseline scenario' supposes the maintenance of present budgetary and monetary policies in the Community, the absence of budgetary adjustment in the United States and normal growth of world trade

(ii) The 'fiscal reflation scenario' sees the budget deficit in the EC increased by as much as is necessary to reach 8 ½ % unemployment by 1990, other variables reacting endogenously; the international environment is the same as in the 'baseline scenario'.

(iii) The 'cooperative growth scenario' comprises, for the Community, a moderate growth in real wages until there is a significant fall in the unemployment rate (1988-89). The development of real wages then moves gradually towards that of productivity per person occupied. Budgetary and monetary policies maintain GDP at a level close to the baseline scenario; while, outside the EC, the US reduces its budget deficit, offset by expansionary action in Japan and some other countries, the dollar depreciates against the ECU and, more substantially, against the yen. This scenario is explained in Section II.5 below.

(iv) The 'EC scenario without international cooperation' assumes the same economic policy measures in the Community as the 'cooperative growth scenario'. On the other hand, the international environment remains the same as in the 'baseline scenario'.

judgement of the Commission or the Council, it is nevertheless useful to outline what this kind of policy might imply over the medium term.

The second column of Table 7 illustrates the economic effects of a straightforward 'fiscal reflation' option in which the target for a significant reduction in the level of unemployment is set at 8 ½ % by 1990. In this simple case, the instrument for achieving this is assumed to be a fiscal expansion with no other constraints observed and the international environment as in the baseline projection.

What the projection shows is that to realize the employment target (8 ½ % unemployment), the European economy would experience a continuously mounting increase in the budget deficit, which, for the EC as a whole, rises from 4,8 % of GDP in 1985 to 7,1 % in 1990. Growth is increased, but so also is inflation which accelerates from 4,5 % in 1985 to 7,1 % in 1990. The projection period ends therefore with a combination of accelerating inflation and public debt burdens, after only a rather moderate reduction in unemployment. The momentum of accelerating inflation and public debt burdens at the end of the period points to the prospect of further harmful interaction between the two. In short the policy would be unsustainable and have to be reversed. The introduction of an accompanying and unavoidable stabilization policy would result in a renewed rise in the rate of unemployment.

These two scenarios can be interpreted as useful reference points in the development of a feasible strategy. Neither a continuation of the existing state of affairs nor an isolated demand-based reflationary policy embody the ingredients necessary to secure the improvement in economic performance desired.

Model-based simulations for the medium term confirm that neither a scenario based on unchanged policies and behaviour nor a simple fiscal reflation will lead to a sustainable acceleration of output growth and job creation. They corroborate the results of other analyses which show that neither a spontaneous development nor budgetary reflation would resolve the problem.

2.2. The need for more employment-creating growth

Current demographic trends and participation rates demonstrate that in order to bring the unemployment rate down from its present level of around 11 % to a level of some 7 % of the labour force between now and 1990, employment growth rates of between 1 and 1,5 % a year would be necessary.

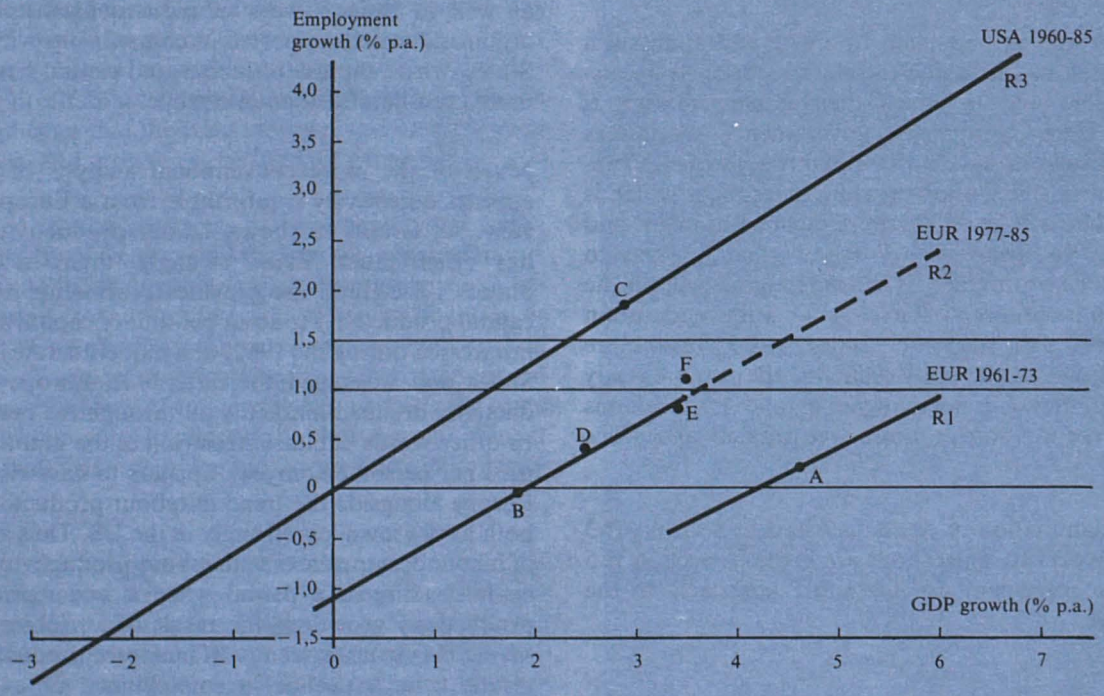
Graph 9 provides a simple illustration of the relation between the growth rates of employment and output in the Community and the United States.

The relationship observed in the Community over the period 1961-73 (R1) shows that despite rapid economic growth averaging 4,6 % per annum, the rise in employment was very modest (an average increase of 0,2 %). If the relation established for this period were still valid at the present time, growth rates averaging over 6 % a year would be needed in order to achieve the desired increase in employment. Such a growth rate would appear to be quite out of reach in present circumstances. It should be noted, however, that the capital-intensive type of growth of the 1960s suggested by the graph was perfectly compatible with the very modest growth in the labour force at that time and permitted the maintenance of a very low unemployment rate (2 to 2,5 % of the labour force).

After the crisis years of 1974-75 and the recovery in 1976 — years which were excluded from the estimating periods because of the extreme instability which they introduced into the results — a new relation was established over the period 1977-85 (R2). This shows a shift of the curve towards the left, i.e. a given economic growth rate is paralleled by a larger increase in employment. However, because economic growth remained low during this period (increasing by an average of 1,8 % a year), no growth in employment resulted. The increase in the labour force was therefore reflected in an increase in unemployment. If the new relation established between growth and employment were to prove stable, growth rates of 3,5 to 4,5 % a year would be sufficient to obtain the increase in employment necessary to reduce unemployment.

Graph 9 also illustrates the relation between employment and growth resulting from the three scenarios presented in Table 7. Thus, annual average growth rates of GDP and employment over the period 1986-90 are in the case of the basic scenario situated virtually on the straight line R2. This means that, with no change in policies and behaviour, the low economic growth rate associated with a fairly modest rate of increase in employment (point D) would be entirely consistent with the relation recorded in the last few years. The isolated fiscal reflation scenario would be reflected in faster economic growth and employment would increase more or less according to the relation R 2 (point E). Lastly the point corresponding to the cooperative growth scenario (point F) would be situated above the present relation: it would clearly represent growth which was faster and which is more employment creating. This third case is treated in more detail in Section II.5.

GRAPH 9: **Relationships between growth and employment**[1]



[1] The lines R1, R2 and R3 summarise the observed association between the growth of employment and the growth of real output. The length of each line is restricted to the extreme observations. R2 only has been extended as a dotted line in order to indicate how, on the basis of more recent experience, employment in the European economy might evolve if growth performance were to improve.

A = Average of 1961-1973	:	+ 4,6% GDP;	+ 0,2% Employment
B = Average of 1977-1985	:	+ 1,8% GDP;	− 0,03% Employment
C = Average of 1966-1985	:	+ 2,9% GDP;	+ 1,9% Employment
D = Basic scenario	:	+ 2,5% GDP;	+ 0,4% Employment
E = Fiscal reflation scenario	:	+ 3,4% GDP;	+ 0,8% Employment
F = Cooperative growth scenario	:	+ 3,5% GDP;	+ 1,1% Employment

The coordinates of points D, E and F are taken from Table 7.

For the United States the apparently favourable positioning of the line R3 is influenced by specific demographic considerations. The active population has been growing at a rate of more than 2% per annum. Between 1960-1970, however, the unemployment rate was always higher than in Europe. It is only since 1980 that unemployment in Europe has constantly exceeded that in the United States.

Several elements can contribute to the achievement of growth which creates more jobs :

(i) a slower increase in real per capita labour costs associated with an appropriate growth in demand;

(ii) a continuing effort to improve the adaptability of all markets (labour, goods and services, capital);

(iii) on the labour market, changes in working time and arrangements for introducing shorter working hours which have no effect on production costs;

(iv) wage differentials which give a more appropriate picture of the requirements for labour in different industries and regions, and with different skills.

An adjustment process guided by these principles is capable both of permitting growth which creates more jobs, but also of laying the foundations for a more satisfactory growth dynamic for the future, to the extent that it restores the economic conditions of supply.

Here it should be stressed that another essential feature is markedly more sustained investment growth. The report has shown that, while growth performance remained modest, the economy was already beginning to run into capacity constraints. Irrespective of the inadequacy of the level of investment (the investment share fell by 5 percentage points between 1970 and 1985), it is probable that, following the shocks caused by energy prices, part of the existing stock is obsolete and less efficient. Hence, if the adjustment process

is to create new jobs, it must be based on conditions propitious to new investment expenditure.

Lastly, it is at least as important to create and maintain a social framework within which the changes deemed necessary are accepted and in which their implementation is encouraged. Here, companies, governments, employees and their trade unions have an essential role to play. Companies must carry out the job-creating investment which is necessary. They will be all the more inclined to invest and more generally to spend if they expect their markets to expand and to be profitable. The trade unions will on the whole be much more receptive to calls for wage moderation if they consider that such moderation will permit more growth and employment. Governments will be more ready to cut taxes if they can see companies and trade unions working together to improve productive capacity and hence the tax base.

After the re-examination of these questions in Sections II.3 and II.4 of this report, suggestions are made in Section II.5 as to how to implement an integrated approach to the problems posed.

Performance in creating jobs in the Community has been generally poor for 25 years. However the model of capital-intensive growth developed in the 1960s was appropriate for that period, because the low increase in employment was paralleled by the small growth of the labour force, so that unemployment could be kept at a low level. Times have changed and in response to the poor growth outlook, it is urgent for the unemployment curve to be reversed. The problem is to achieve economic growth which is both faster and also creates more jobs. The main points of the economic policy to be implemented in order to attain this objective have been clearly identified. Essentially they combine a moderate growth of wages with the right degree of support for demand and must be accompanied by improved adaptability on all markets. It is therefore the conditions for the cooperative implementation of this policy which must now be considered.

2.3. Labour, capital and technology

There is now a strong suspicion that the mix of capital and labour used in the European productive process has become biased too much against the use of labour. The stagnation of employment as we have observed is an uncontested fact. Evidence has also built up showing an increasingly distorted use of capital for labour-saving rather than for capacity expansion. Whilst there are many data problems, it is worth noting that there is a corroboration of evidence from statistical estimates for the industrial and manufacturing sectors, as well as from surveys of industrialists' opinions. The argument is also supported in comparisons with the United States, where the use of labour and capital has been rather more even-handed than in Europe.

Much of the more conventional analysis of productivity appears deceptively comfortable from a European point of view. As Graph 10 shows, labour productivity in Europe has risen much more strongly than in the United States. The graph also provides information on the trend in capital productivity (output per unit of capital stock). This progressed during the 1960s at a moderate rate in the United States and weakened thereafter. In Europe capital productivity declined markedly all through the period 1960-85. In other words capital intensity (i.e. the amount of capital used per person employed), appears to have risen steeply in Europe alongside the trend in labour productivity, whereas both have grown less strongly in the US. Thus a comparison of labour cost increases with labour productivity growth will be misleading in a period when a major part of labour productivity growth is the result of an increasing labour-saving bias in investment. If increased productivity growth results from a decline in employment, or an insufficient increase in employment with respect to the growth of the labour force, the labour force as a whole is not reaping the benefits of these apparent productivity gains.

Increases in capital per employee are regarded naturally as a desirable thing and experience through the 1960s suggests that the growth of capital per employee did yield a reasonably acceptable growth of GDP and output per employee. A question which arises,therefore, is why capital accumulation in Europe, particularly from the 1970s onwards, has not generated more employment. There is little doubt that energy price increases reduced the net worth of the existing capital stock. Action by governments to control inflation with restrictive policies also led to under-utilization of capacity. Looked at over the longer term, however, another important part of the answer is that these trends have been accompanied by a sustained deterioration in the profitability of or return to investment and,related to this, a marked increase in the real reward to labour relative to that of capital (see Graph 11).

Three other factors which may help in an explanation are, firstly, the existence of labour market rigidities which may have impeded the effective working of the labour market in the face of rising employment costs. Secondly, the conscious policy on the part of governments to increase taxes on labour, particularly social security contributions. Non-wage costs in the Community have risen by around one half

of a percentage point per annum over the past two decades. Thirdly, the need to exercise control over inflation and the necessary non-monetary financing of budget deficits has led to a high real interest rate in the Community. Taken together, these factors have produced a sustained deterioration in the profitability of investment. Reference to Graphs 11 and 12 indicates that there is a strong association between rates of return and growth of the stock of capital.

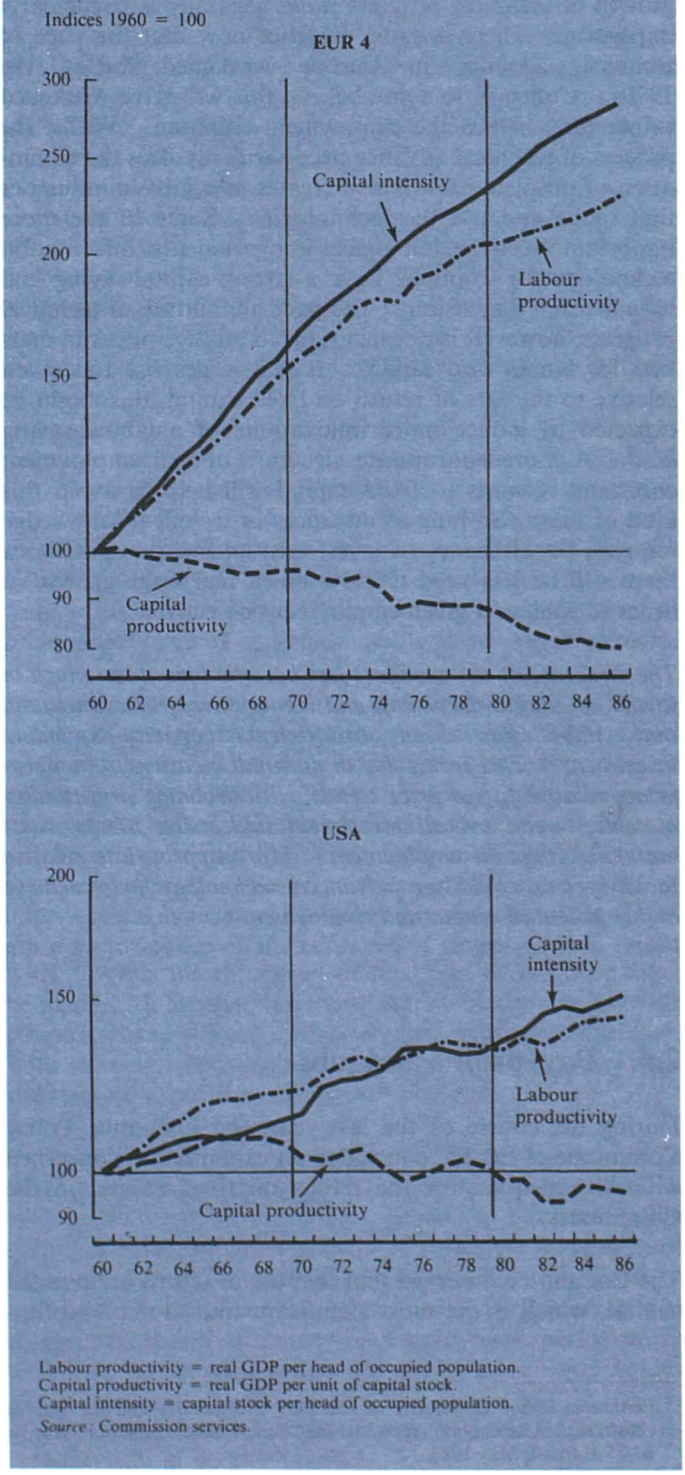
The increased relative real costs of employment and weakened profitability of fixed capital has tended to make labour-using or capital-widening investment increasingly less attractive relative to the more capital intensive methods of production. Overall, the decline in capital productivity and fall in rates of return in Europe points to a pronounced decline in the efficiency of its investment, perhaps for some considerable time. The implication is that new investment has not provided the contribution to production capacity needed.

In summary, the position reached in Europe, therefore, is one where there has been too much emphasis on labour-saving investment; but induced by poor profitability, the economy is faced with a shortage of investment for new capacity. In the low efficiency situation, the gap between the marginal product of capital and the real interest rate is too large.

Since the early 1980s there has been some correction of these trends. The trend growth of real wage costs has moderated to 1,0 % per annum over the period 1983-85 compared to 2,1 % for 1974-82 and 4,4 % for 1961-73. The rate of return on the gross capital stock is estimated to have increased somewhat from its low point at the beginning of the 1980s following the second oil shock, but this is still a long way below the level observed in the 1960s when there was a faster rate of growth of the capital stock (see Graph 12).

Investment has begun to pick up in 1984 and 1985, but from a very low base. As noted, however, the increase in the rate of capacity utilization in industry has continued through the last 12 months, rising from 79 % in the middle of 1984 to 82 % in 1985. Given this supply constraint, if the potential rate of growth of the European economy is to be significantly increased, there will have to be a major investment effort and one oriented away from labour saving and more towards capacity extension. This in turn implies that the recent improvement in the relative reward to capital as compared to labour will have to be continued for a considerable number of years. Such a trend would, of course, be more readily accepted as part of a social consensus if the economy was seen to be moving onto a more favourable growth path and at the same time creating more

GRAPH 10: **Labour productivity, capital productivity and capital intensity in the four main Member States and the United States, 1960-85**



Labour productivity = real GDP per head of occupied population.
Capital productivity = real GDP per unit of capital stock.
Capital intensity = capital stock per head of occupied population.
Source: Commission services.

employment. This raises a question of an appropriate demand development which must go on in parallel with small increases in real wages.

In this context, the role of technological innovation and the growth of technical progress more generally is particularly important. There is some evidence now that the pace of technical advance in Europe weakened during the 1970s. Contrary to some beliefs, this will have weakened rather than helped the employment situation. Whilst the process of technical advance necessarily involves the elimination of obsolete jobs, it also creates new jobs in industries that make and use the technologies. Some of the more important recent technological improvements, information technology for example, have a strong capital-saving and labour-using dimension. The pace and nature of technical progress, however, is not invariant to relative prices in markets for labour and capital. If real wages rise too much relative to the rate of return on fixed capital, this might be expected to induce more innovations of a labour-saving kind. A more appropriate structure of real employment costs and rewards to fixed capital will help to avoid this kind of bias. So long as advances in technical knowledge improve the efficiency of investment and working methods there will be less need to slow down real wage growth in order to achieve a given employment objective.

The structure of the economy has become biased too much in favour of capital-deepening and labour-saving investment, so that there has been insufficient capacity-expanding investment. This seems due in no small measure to inappropriate relative factor price trends, with declining profitability matching weak overall investment and rising labour costs matching stagnant employment. More appropriate relative factor prices could see advanced technology help achieve higher potential output and employment growth.

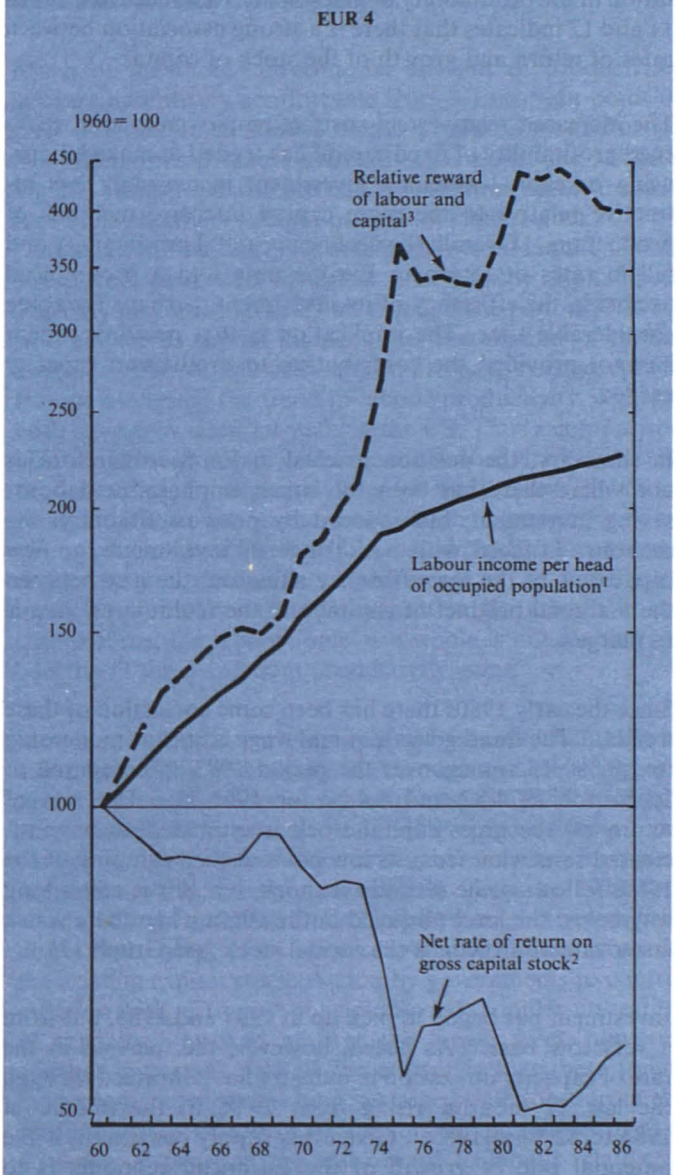
2.4. Pay, profits and jobs

During the course of the last year, the Economic Policy Committee of the EC concluded an examination concerned with the adequacy of the return on fixed capital in the Community.[1]

The Committee observed that the rate of return on invested capital, which is the most significant indicator of profita-

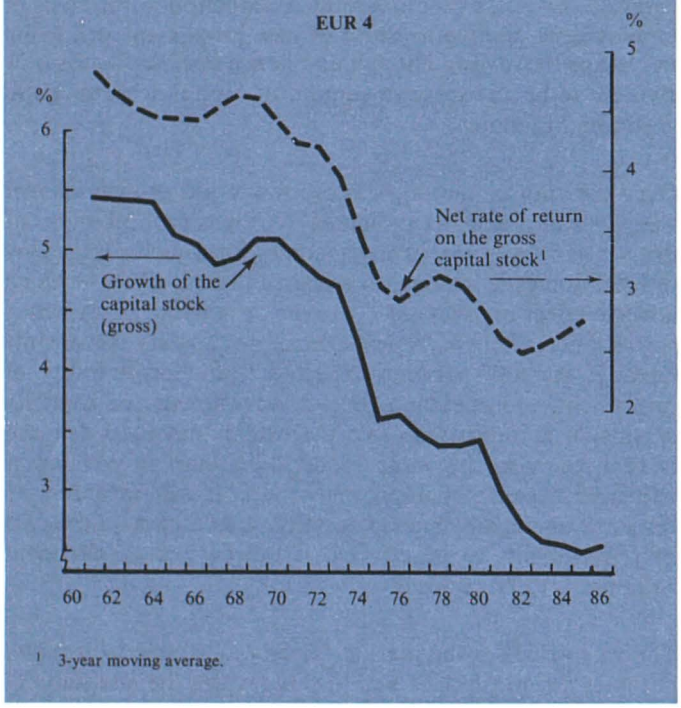
[1] Economic Policy Committee of the EC, 'Profitability and the rate of return in the Community', report to the Council and Commission, (doc.II/02/85-E final), May 1985.

GRAPH 11: **Relative rewards of labour and capital**
Constant prices: indices 1960 = 100



[1] Compensation of employees per wage and salary earner, including an estimated labour income of the self-employed, assumed to be equal to the compensation of employees per wage and salary earner.
[2] Net operating surplus, excluding estimated labour income of the self-employed, as a % of the gross capital stock.
[3] Relative reward of labour and capital = labour income per head of the occupied population/Net rate of return on the gross capital stock.

GRAPH 12: **Rates of return and growth of the capital stock**
Constant prices



[1] 3-year moving average.

bility, declined in the 1960s and the 1970s in the Community. In 1984 the net rate of return on the net capital stock in the EC is estimated on average to have been 4,2 % (see Graph 14), which compares with 11 % in the 1960s (on the basis of the definitions used in Graph 14). This decline in the rate of return however appears to have been arrested in the more recent past, as the rate of increase of real wages moderated to an annual average growth of 1 % in the period 1983-85 (compared with 2,1 % in the period 1974-82 and 4,4 % in the period 1961-73). Nonetheless the recovery of the rate of return, while variable across countries, has on average been very modest when compared with the levels observed during periods of faster growth in Europe.

The wage share in national income in Europe has fallen back closer to the levels observed at the beginning of the 1970s, and the profits share has increased correspondingly. However, this change in income distribution has merely matched the change in capital-labour mix. This explains why the rate of return on fixed capital has hardly increased, and why therefore there remains a problem of insufficient profitability in Europe.

While there are serious statistical difficulties in the measurement of profitability of fixed capital, there exist also other criteria for judging the level of profits and wages, notably in the investment and employment performance of the economy. High real wage growth through the 1970s has contributed to a weak investment performance accompanied by an unfavourable investment mix.

In the judgement of the Economic Policy Committee, the great majority of Member States do still experience a level of profitability on fixed capital that is, in most sectors, probably too low from the standpoint of fostering sufficient investment and employment growth. Sustained moderate increases in real wages coupled to adequate demand growth would, of course, lead to the desired overall increase in the rate of profitability of fixed capital. An example of the very positive response of employment and investment to real wage moderation and improved profitability is being seen currently in Denmark where, in a small open economy, the increase in exports has provided the necessary demand stimulus.

The case exists therefore for an adjustment to be sustained for several years. Indeed, it may well be necessary for real wage growth to remain very modest and below the growth of labour productivity, as long as unemployment has not fallen significantly. However, this would need to be accompanied by an appropriate evolution of demand sustained progressively in part by spending on new private investment.

The issue of wage differentials, and flexibility in real wage evolution is also relevant in the pursuit of a higher level of employment. This issue of course poses considerable problems in the context of centralized wage bargaining; the appropriate balance between centralized versus decentralized negotiation is an important topic of dialogue between the social partners. Some evidence on the significance of inter-sectoral real wage flexibility for the employment-creating performance of the economy is suggested in a recent work.[1] While interpretation of this kind of evidence must be made with caution, it does appear to be the case that EC countries have shown a relatively low real wage flexibility, both inter-sectorally and at the macroeconomic level, this running alongside increasing unemployment.

It is of crucial importance that a greater consensus be reached over how these several difficult issues of pay, profits and employment performance should be handled in the Community in the years ahead. European countries must no doubt find solutions which can be adapted to the particular political and social traditions, whilst taking full notice of the ingredients of successful employment performance elsewhere. In this connection the role of more novel modes

[1] OECD, 'Labour market flexibility and external price shocks', ESD Working Paper No 24, September 1985.

of pay determination could be examined, including for example a larger component of profit, bonus or performance-related pay. In pay systems which embody some of these characteristics, employees could have some measure of guarantee against excessive swings of the pendulum in favour of returns to share-holders. Moreover, the employer would be more prepared to recruit extra staff in the knowledge that labour costs were more flexible. In view of the need for a period of faster investment and higher profitability, it could also be helpful to foster a climate of wider participation on the part of employees in schemes for capital accumulation.

Wage moderation in recent years has allowed the decline in profitability of fixed capital to be arrested. However, profitability is still too low for the purpose of achieving higher investment and employment growth. Real wage flexibility in the EC, both at macroeconomic and sectoral levels, is also rather low and apparently related to the weak employment propensity in the European economy. Therefore real wage moderation, of a kind actually witnessed in most Member States in the last four years or so, needs to be sustained for a period of years ahead until a substantial and continuing reduction of unemployment is achieved. Employers for their part must ensure that the necessary investment is forthcoming. Within a broad framework of concertation between the social partners there are three particular areas of concern: (i) how governments might formulate the necessary demand policies to accompany wage moderation agreements; (ii) the adjustment of relative factor prices and attainment of employment objectives; (iii) the scope for new modes of wage determination designed to attain more readily the objectives of high employment.

2.5 A cooperative medium-term growth strategy

The earlier parts of this section of the report have attempted to provide what are in effect building blocks for a suggested strategy aimed at securing a substantial and employment-creating growth. Given this earlier discussion, the judgement in this report is that the possibility of realizing such an outcome will depend heavily on a small number of particularly important conditions but set within a cooperative framework. Particular emphasis is placed on the contribution required from the different actors for the purposes of improving the profitability of capital, providing aggregate demand support and thus generating the investment necessary for growth of a more employment-creating kind.

Within this cooperative framework, the recent moderation in most countries in the rise of real employment costs, after a period of strong increases, must be maintained. It is clear that those countries which have not yet achieved the degree of moderation required must make efforts to do so. Associated with this is the need to encourage a more even-handed evolution of the relative rewards to labour and capital. Over the medium term, a reduction in the costs of employment relative to those of new investment will begin to change the investment mix and hence reverse what is now thought to be an excessive amount of capital deepening and shedding of labour.

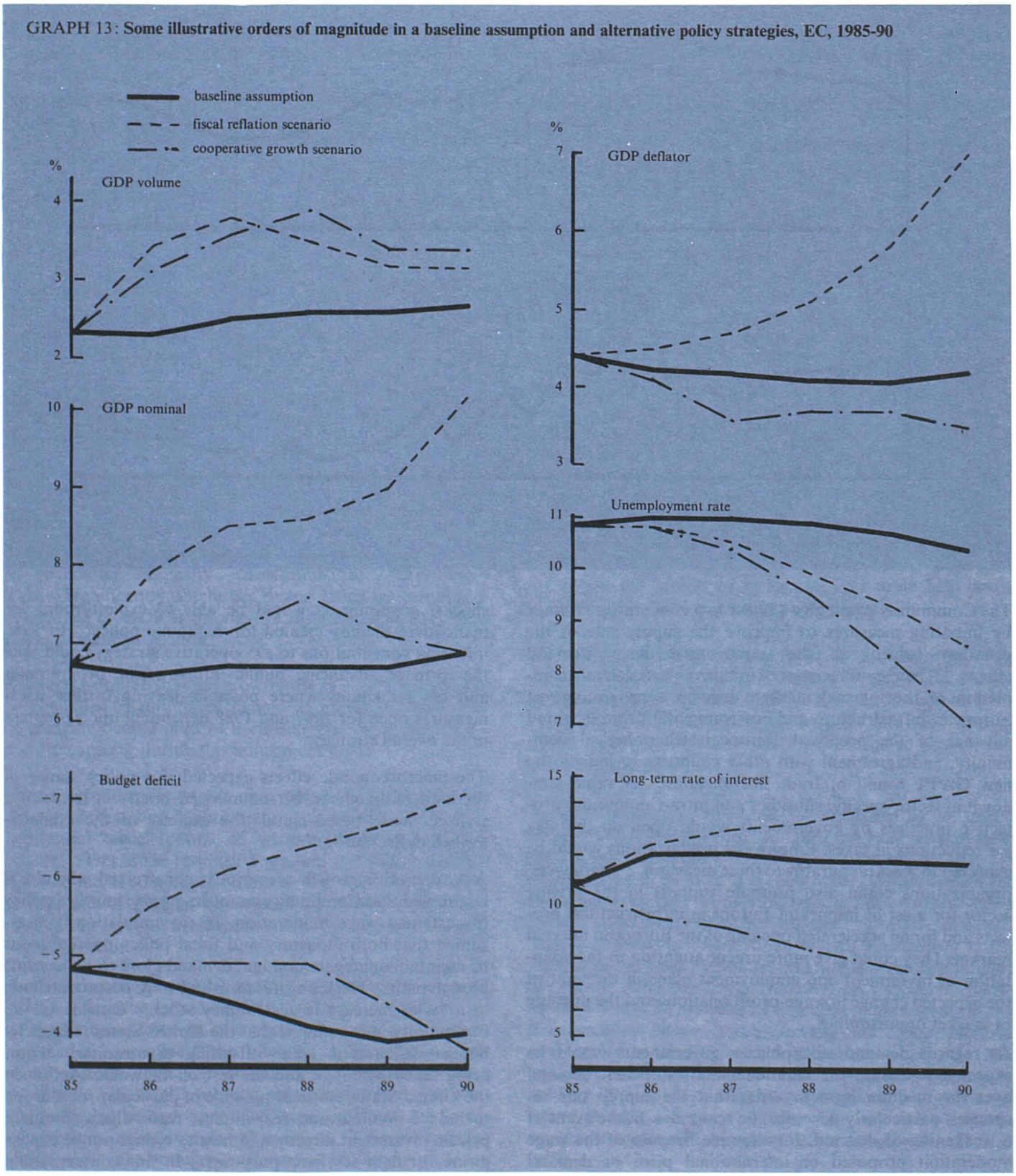
Over the shorter period, a more moderate growth of real wages will tend to increase the profitability of firms. However, since wage incomes form such a large part of total domestic income, to a degree there is likely to be an adverse effect on demand. Given the starting point which is one where there is some evidence of capacity constraints already, the link between expected future profitability of investment and spending on new investment for capacity expansion is important. To the extent that total demand is reduced more by wage moderation than investment is increased because of improved profits, it will be necessary for some aggregate demand sustaining measures on the part of governments to be effected if the desired employment response is to be realized.

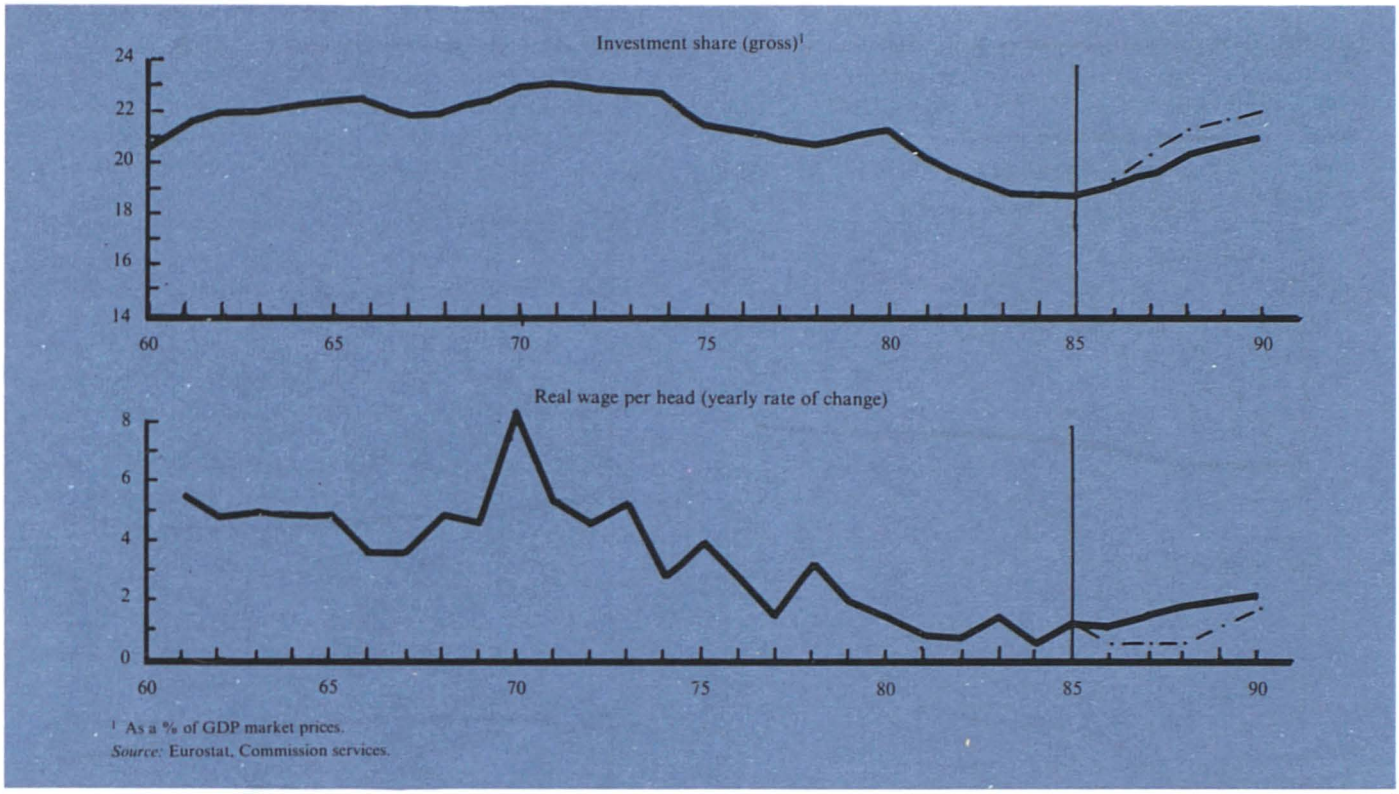
The way in which the market for labour is able to respond occupies a central place and in this respect the adaptability and functioning of labour markets has been identified as a problem area in Europe. Factors such as job tenure and severance conditions, more flexible use of working time, the adequacy of professional training, the relation of wage differentials to labour needs in different sectors, regions and skills and the growth of non-wage costs should be re-examined in order to improve market efficiency without jeopardizing social protection.

The elements noted above constitute the essential core of the approach, a characteristic of which is that total demand has an important supporting role rather than one of leading in the growth process.

It is envisaged that the implementation of a growth strategy of the above kind would require an undertaking by both employers and trade unions to hold the evolution of real wages to the course of moderation witnessed in recent years for a further period until a sufficient reduction in unemployment is achieved. It should be examined in the wage-profit-investment-employment nexus whether there could be a role for wages having a larger flexible and more profit-related component. This could help boost employment by making labour less of a fixed cost. In present conditions, such an initiative would serve also to assist an investment upswing, by enabling companies to rely less on external sources of finance.

GRAPH 13: **Some illustrative orders of magnitude in a baseline assumption and alternative policy strategies, EC, 1985-90**





[1] As a % of GDP market prices.
Source: Eurostat, Commission services.

The Community could give a boost to a cooperative strategy by initiating measures to improve the supply side of the economy which at the same time have demand effects. These could consist of initiatives to accelerate completion of the internal market, develop a programme of European infrastructure and environmental projects, rapid advance of the proposed European technological community, and agreement with other countries to launch the new GATT round of trade liberalization. A rapid rundown in sector-specific subsidies and intra-Community protective practices by governments would open up the way for reductions in taxes. Employers' organizations would be expected to react favourably to these measures. Employers' organizations could also promote support in the private sector for a set of important European infrastructural projects and for an accelerated opening of the European internal market. They could give more urgent attention to the adaptation of investment and employment plans in the light of the expected change in wage-profit relations and the opening of market opportunities.

As regards demand side policies governments would be expected to ensure the maintenance of sufficient demand over the medium term in order that the supply side responses, particularly new jobs, be realized. In the event of a weakening of demand, for example because of the wage moderation proposed or international price or demand shocks, governments would be able to exploit room for manoeuvre thereby created for economic policy. In 1986 initiating contributions to a cooperative strategy could take the form of advancing public infrastructure programmes and tax reductions where possible, leaving further fiscal measures open for 1987 and 1988 depending upon progress in the overall strategy.

The macroeconomic effects expected if a policy stance of the kind outlined can be summarized briefly in terms of a stylized model-based simulation exercise of the kind described in Section II.1.

A 'cooperative growth scenario' is constructed whereby it is assumed that Community countries pursue jointly a policy of sustained wage moderation. In the simulation it is assumed that both monetary and fiscal policy operate so as to maintain aggregate nominal demand close to its baseline growth path. Declining inflation and wage costs contribute to a faster increase in real money stock. Outside of the Community, it is assumed that the United States reduces its budget deficit with some offsetting expansionary action being taken by Japan and the rest of the world. Action in the United States makes it possible in particular for Europe to reduce nominal and real interest rates which stimulate private investment directly and help to reduce public expenditure for debt servicing purposes. In this context, some

moderate expansion of public investment and reductions in taxation are compatible with the desired control of budget deficits, largely because of the impact of higher growth on budget revenues and the lower interest rates. In the case of a less favourable assumption about the international environment some additional demand support would be necessary to obtain the desired reduction in unemployment.

The results of a simulation of a cooperative strategy of this kind, on an internal and international level, are illustrated in the third column of Table 7, and Graph 13.

The major feature is that the initiatives proposed, if implemented, offer the prospect of a growth rate of 3,5 % between 1986 and 1990 being associated with an average employment growth of 1,1 %. Indeed, in the final year of the projection, output grows by 3 ½ % and employment increases by 1 ½ %. This reduces the unemployment rate in 1990 to 7 %. This development could be sustained after 1990 and therefore opens up the perspective of a further substantial reduction in unemployment.

The assumed policy of wage moderation with demand support reduces the rate of inflation and increases company profitability. This induces a rise in private investment of over 6,5 % which, over the simulation period, is sufficient to overcome capacity constraints at the macro level. Significantly, the public sector deficit measured as a percentage of GDP is on average little different from that in the baseline projection.

It should be noted that the growth rate of 3 ½ % on average as simulated is not to be judged as excessive when seen against the background of a considerable increase in productive capacity during this adjustment phase.

Labour productivity grows on average only a little faster than in the baseline assumption in spite of the much more substantial acceleration of growth from 2 ½ % to 3 ½ %. This is the result of a gradual but widely diffused shift in the labour-capital mix in the economy. Faster growth and a gradual change in the labour-capital mix combine to give the favourable results for employment and unemployment.

The macroeconomic model simulation cannot take account of, or describe, the detailed sectoral evolution of productivity. However, such productivity growth might be expected to have some of the following characteristics. For those who are already in employment, one can assume a reasonable high skill level, that their productivity performance will also be high and, when combined with the anticipated new investment, may well increase. Of those entering employment, the younger entrants will be largely unskilled and require a period of training. Over this time, their productivity contribution will certainly be low. The same will be true for people who have been unemployed for a long time.

In summary, the simulation as constructed implies that a fulfillment of the conditions outlined could lead the European economy on to a growth path which has some characteristics of a 'virtuous circle'. Higher profitability and demand support generate the investment and output growth sufficient to absorb new jobs on a scale which reduces the pool of unemployed. Stronger growth, increased employment and lower unemployment in turn, improve public sector deficits by more revenues and less crisis-related expenditure, and this contributes, with increased self-financing of enterprises, to produce lower interest rates.

Even so, there are some factors which are not modelled in the scenario and which could generate further improvements in the economy's performance. These include various supply side improving measures that have been taken in recent years in many countries, but which take a long time to bear fruit. Improved market adaptability with cost neutral reorganization and reduction of working time and the accelerated realization of the EC internal market, as now proposed, would add to growth and employment. Lower oil prices also (as mentioned in Section I.3.) could help boost activity in the world economy more generally.

The strategy thus depends heavily on the mutual supporting action of the major partners — employers, trade unions and governments. There must be a conscious will to both ensure the desired supply response on the one hand, and to ensure that the nominal demand is sufficient to absorb this supply on the other.

A policy strategy is suggested, for discussion by the social partners and governments, designed to raise employment growth and reduce unemployment very substantially over the medium term. If pursued, it is conceivable that unemployment could fall to about 7 % by 1990 and, in this event, the gains to real output would also be significant. The core elements, namely a temporary moderation of real employment costs, relative factor price flexibility, and nominal demand support are highly interdependent. However, an important contribution will also be provided by extensive improvements in the functioning of labour, goods, services and capital markets and notably in the EC internal market in many fields. The implementation, success and credibility of the adjustment strategy rests, however, on a joint willingness by all parties to ensure that the necessary conditions are met with a step-by-step implementation starting in 1986, extending over several years.

3. Economic policy in the framework of a cooperative growth strategy

3.1 Public finances

3.1.1 The public sector

Last year's annual report advocated a reversal of the mounting share of public expenditure and taxation in the gross domestic product of the European Community. Recent estimates by the Commission suggest that the previous trend is now being checked if not reversed. The volume of public expenditure is expected to grow by under 1 % in 1986. Total public expenditure in the EC as a share of GDP is estimated to decline slightly from 51,9 % in 1984 to 51,5 % in 1985, and then more substantially to 50,8 % in 1986. Similarly, the total tax burden is estimated to be declining, although by a somewhat smaller margin, because of budgetary consolidation. Total taxes amounted to 46.4 % in 1984, are expected to be 46,3 % in 1985 and 46,0 % in 1986.

Given institutional differences in the organization and extent of the public sector, such highly aggregated data must be used with caution, especially in inter-country comparisons. Some summary comparisons between the EC and US are shown in Table 8 which point to similarities as well as differences between the two economies. Government consumption expenditures, for example, stand in both cases at about 19 % of GDP, and the weight of direct income taxation is also similar at about 13 ½ % of GDP. The higher level of government capital formation in Europe no doubt reflects the wider extent of public intervention in certain services, for example transport and health. Striking differences arise in the magnitude of government current transfer payments which reflects the greater involvement of government in the provision of health and social security. Social security contributions in Europe as a percentage of GDP are correspondingly higher than those in the US. The EC average tax and social security burden however covers a considerable range; in 1985 for example, from around 55 % in Denmark and the Netherlands to 41 % in the United Kingdom and 35 % in Greece.

The reasons why the scale of both public expenditure and taxation can influence economic growth and employment over the longer term are extremely complex. However, three channels of influence can be identified which create the possibility of risks to the achievement of an efficient economic performance.

As the taxation on labour income rises, so also does the difference or 'wedge' between what an employee costs to the employer, and what the employee receives as net-of-tax income. Higher labour costs tend to reduce the demand for labour and therefore private employment. Further, in so far as lower net-of-tax incomes induce wage-earners to claim higher wages in compensation, this will create inflationary pressure and worsen employment prospects again when this inflation has to be reversed. Higher taxation on wage income helps also to account for the increase in the price of labour relative to capital and hence the increase in the capital-labour ratio observed in the 1970s, and noted earlier in this report. The increase in this taxation 'wedge' has been pronounced in most European countries over the last two decades, as compared with experience in the United States and Japan. For example between 1960 and 1983, the difference between gross and net wages expressed as a percentage of net wages grew on average in the four larger EC countries from 36 to 60 %. In the United States over this same period, the increase was from 29 to 37 %.

A second channel concerns the efficiency and value of public services. If wage-earners perceive public services and transfers to be giving good and fair value, there will be a more ready consensus over accepting the tax burden implied. Inefficient and unduly extensive transfer payment systems on the other hand will tend to undermine such a consensus and thus lead to higher wage pressure with detrimental effects on growth and employment.

A third channel of influence occurs when public borrowing rather than taxation is used to finance current public expenditure. Here, given the need to pursue anti-inflationary policies the deficits should not be financed by money creation. The impact on performance will thus operate primarily through a higher rate of interest. Insofar as this reduces private investment it will harm the growth of productive potential.

Although the timing and nature of the final incidence of these effects on economic performance are highly uncertain, there is a presumption that in Europe the rapid growth of public expenditure and changes in its composition together with the evolution of the tax burden has had detrimental effects on economic performance when measured over the longer term. The fact that the Community is beginning to reverse some of the trends observed indicates an awareness of these possibilities and this is to be encouraged.

It is highly unlikely that economic performance is invariant to both the weight and shape of the public sector. Undesirable consequences can follow from the difference between gross and net incomes, a weakening of social acceptance of the tax burden and the effects of public debt on capital formation. There are signs of increasing awareness in the Community that these are real problems and the observed tendency to begin a reversal of earlier trends is to be welcomed.

3.1.2 Taxation policy for economic growth

There are a number of ways in which taxation policy can contribute to a strategy aimed at higher growth of a more employment-creating nature.

One question is whether such a strategy could be furthered by means of increased incentives and subsidies for investment. This has been discussed extensively in the relevant Community bodies during the last year. The predominant judgement is that the experience of trying to stimulate growth through increased specific investment subsidies has been rather disappointing. Although a sustained increase in investment spending is needed now as part of a growth strategy, it is felt that inducement of this through the introduction of specific investment incentives creates the risk of worsening any trend in the direction of capital-deepening and labour-saving activities. Given the present condition of the European economy, with its notably poor employment record, it may be desirable to create conditions which are more even-handed with respect to business expansion. Any feasible tax concessions should therefore be used primarily to cut labour costs, so improving the profitability of private enterprise in order to initiate a more balanced mix of labour-using and labour-saving investment.

A related issue is whether public deficit considerations permitting faster progress in the reduction of both subsidies and taxes in various sectors of the economy could be made. There are some persuasive reasons for doing this. Notably it will help to reallocate resources from the more stagnant or declining sectors to the more productive and growing sectors of the economy. This is an area of policy where the responsibilities of the European Community itself are considerable, in competition policy in general and in some specific sectors (see further below on agriculture, steel, and shipbuilding). A mutually reinforcing action by the Community and Member States is needed to effect a more rapid series of tax cuts and of subsidies, so adding a further dynamic element to the economic strategy.

In the same class of ideas, but this is clearly a matter of national competences, is a detectable notion of tax reform. Examples are seen currently in the United Kingdom, Denmark and other countries. What is envisaged is that a simplification of existing tax systems, through the elimination of the numerous tax offsets and advantages for special purposes especially in the income taxation of persons and companies, will enable basic rates of taxation to be reduced within existing revenue constraints. This encourages the market to allocate resources in response to more appropriate price signals and thus helps to avoid the kind of bias which have become all too obvious over the past decade.

Finally, the possibility of a substantial fall in the price of oil raises issues concerned with the taxation of energy, labour and capital. The objective of a more employment-creating growth is easier to attain in the presence of reductions in the taxation of employment income. A pronounced fall in the price of oil over a few years could endanger progress being made towards securing a situation whereby the economy is less vulnerable to imported price or supply shocks. It is, of course, difficult to judge what the long-term equilibrium price of energy might be. Nevertheless, the raising of duties or taxes on oil products would contribute to budget flexibility and thus provide more room for manoeuvre in the job creation, investment strategy proposed here.

There are several ways in which taxation policy can contribute to a strategy for higher growth and more employment-creating growth: (i) a switch in emphasis away from specific fiscal incentives for investment, which will help to foster employment and enterprise profitability; (ii) reduction of industry-specific subsidies coupled with general tax reductions; (iii) reduction of other specific tax offsets accompanied by lower tax rates; and (iv) in the event of an energy price fall, the raising of duties or taxes on energy could provide room for manoeuvre for employment creation.

3.1.3 The role of public debt

Fluctuations in budget deficits and public debt can have important effects on both supply and demand conditions in the economy. However, these are not easy to define in a simple way. Rising public debt burdens tend to increase the rate of interest and, other things being equal, depress private capital formation. This interest rate effect, however, need not necessarily be a dominant factor since, under certain conditions, budget deficit movements can contribute positively to economic growth. If an appropriate policy succeeds in raising the potential output of the economy, a temporary rise in borrowing may increase demand, in a way which matches broadly the increased potential tax base of the economy. The structural public debt burden, as measured, for example, by the medium-term value of public debt as a percentage of GDP, may then not rise.

What level of the public debt burden might be judged appropriate depends very much on specific economic circumstances. However, at very high levels of the public debt burden, such as around 100 % of GDP or more, as currently is the case in Belgium, Ireland and Italy, the serious economic problems caused by excessive borrowing and the resulting debt burden become quite obvious. Interest payments on the public debt can reach 10 % or more of GDP, and account for 20 to 25 % of public expenditure. The rate

Table 8

Level and structure of public expenditure, receipts and public debt in the US and the EC

(% or % of GDP)

	US		EUR		
	1970	1982	1970	1982	1985
A. *General government expenditure, total*	32,8	37,6	37,9	51,2	**51,5**
1. General government capital formation	2,5	1,5	4,2	3,0	**2,8**
2. Net capital transfers	−0,5	−0,3	0,8	1,0	**1,1**
3. Government final consumption expenditure, total	19,2	18,7	15,3	19,3	**19,2**
4. Subsidies	0,5	0,5	1,8	2,3	**2,4**
5. Interest payments	2,3	4,5	2,0	4,7	5,3
6. Current transfers	8,3	12,4	13,8	20,9	23,1
B. *General government receipts, total*	31,0	33,6	38,2	45,8	46,3
1. Indirect taxes	9,5	8,5	13,9	13,5	**13,8**
2. Direct taxes	13,9	13,6	10,3	13,0	**13,2**
3. Social security contributions	4,7	6,8	11,0	15,4	**15,5**
4. Other current receipts	2,9	4,7	2,9	3,8	**3,8**
	1971	1982	1971	1982	1985
C. *Public debt*					
1. Gross public debt	26,1[1]	28,5[1]	47,8	57,5	64,3
2. Net public debt	:	:	14,7[2]	26,3[2]	33,4
D. *General government share in total employment, %*	18,1	16,7	13,7	17,5	:
E. *General government financial balance (in % of GDP)*[3]	−1,8	−3,9	0,3	−5,6	−5,2

[1] Federal government.
[2] Average for EUR 5 (D, F, I, UK, DK).
[3] Projected financial balance for 1985 for the US: −3,7% of GDP.

of interest itself is, under conditions of non-inflationary monetary policy, subject to strong upward pressure. If the risk associated with a rise in the debt burden becomes important, a country's domestic interest rate eventually will incorporate a substantial risk premium. This is a direct reflection of markets' view of the financial problem. There may also develop income distribution problems between bond-holders and salary-earners. A combination of arguments, concerned with economic growth, monetary stability and income distribution therefore, all plead in favour of action to reverse what can easily become an unsustainable trend situation.

As for the adjustment process required, examples show that comprehensive stabilization programmes need not necessarily be excessively costly or disruptive even in the short term. Denmark, in particular, has been reducing its government borrowing requirement massively, from 9 % of GDP as recently as 1982 (which is comparable or lower than the present deficits of Belgium, Greece, Ireland and Italy) to under 2 % of GDP forecast for 1986. In the meantime, the Danish economy will have grown by 15 % (from 1981 to 1986), whereas in the same period the EC on average grew only by 8 %. Danish employment growth was also much faster than in any other EC economy during this period.

In other EC countries the debt burden currently is not so great. The gross public debt burden in Germany presently appears to be stabilizing at around 42 ½ % of GDP. That of France is currently rising but remains at a lower level of 36 % of GDP. That of the United Kingdom is higher, at 60 % of GDP in 1985, but has been decreasing since 1983. Thus these countries perhaps have some margin within which the evolution of the public debt burden as a share of GDP could vary, depending upon their economic policy strategy. If some temporary rise in the public debt burden were to be accepted in the next few years, great care should be taken to ensure that (a) this formed part of a combined supply and demand strategy that effectively raised the profile of actual and potential production; and (b) remained within the constraints of a sound medium-term financial strategy. These conditions should be easier to satisfy if the following criteria are observed:

(i) On the supply side, the counterpart to increased public debt where possible, should represent investment in pro-

ductive potential, either in the form of public investments offering acceptable social rates of return, or, in the case of tax reductions, in a stimulation of private investment which will lead to a widening of the future tax base of the economy. Such tax reductions might be expected to have beneficial incentive effects in the markets for labour and capital. In this way a virtuous circle of interrelated movements can be possible. With enhanced productive capacity the tax base is increased; thus tax rates can be reduced which further stimulates growth, even within the constraint of given budget deficit levels.

(ii) On the demand side, expansionary measures in the budget should be justified by the need to correct any inadequacy in the growth of demand. In the event of further disinflationary effects on the European economy resulting from dollar depreciation or falls in commodity prices, it may be desirable to sustain demand, in particular to prevent excessive deflation of the tax base. In these conditions it makes little sense to raise taxes or cut expenditure to offset such shortfalls.

(iii) The evolution of wage incomes has important implications for both supply and demand sides of the economy. Starting from a situation of inadequate profitability and high unemployment, wage moderation helps create and increase profitable productive capacity. It increases the potential tax base, and in a situation where public finances are in reasonable balance, justifies tax rate reductions. Wage moderation itself, however, may create a transitional problem of demand weakness, and this is another case where accompanying support from demand policy is desirable.

Public debt strategy is an important ingredient of both supply and demand policy. Such a strategy cannot always be defined in simple terms. There are cases in the Community where the growth of the public debt burden is clearly alarming and must now be put onto a corrected trend (Italy, Belgium, Ireland). Elsewhere public debt burdens are generally lower and, in some cases, approximately stabilized. Whether there is a sound case for using room for manoeuvre here for some increase in the public debt burden during an adjustment period to help the economy onto a higher growth trajectory, depends upon a specific set of supply and demand conditions. If supply potential is improved by wage moderation and microeconomic policies to improve markets, and if demand is temporarily weak because of, for example, wage moderation or international influences, then some transitory increase in the public debt may contribute a valuable element to the wider growth strategy.

3.1.4 The European Community budget

An additional level of public finance is developing in Europe. With a revenue or expenditure volume of around 1 % of Community GDP the Community budget, admittedly, has not a major macroeconomic impact but is playing a greater role in structural adaptation. With the enlargement of the Community the total own resources of the budget are being increased, as from 1986, with revision in the maximum rate of value-added tax call from 1,0 % to 1,4 %. At the same time, an increased effort is being made to contain the large share of agricultural price support expenditure in the Community budget.

The policy priorities for the enlarged Community budget are to facilitate the structural improvement and convergence of the Community economy. This comes out clearly in Table 9. The 1986 figures are taken from the preliminary draft budget. In several of its faster growing functions, the budget is contributing aids to compensate for the effects of the opening of the Community's markets and help to restructure regions or sectors in difficulty.

The increase in expenditure in 1986 is partly due to the accession of Spain and Portugal, but also reflects an increase in respect of the other Member States. This is particularly true of the Regional Fund which, under the new Regulation applicable from 1985, increases the share of expenditure going to more selectively defined regions with the most severe problems.

Expenditure on integrated Mediterranean programmes, aimed at helping Mediterranean regions adapt to the consequences of the Community's enlargement, becomes significant for the first time in 1986. Expenditure on transport infrastructure projects, the Social Fund (retraining and job-creation projects), and R&D and innovation and development aid also becomes more important in 1986. About 50 % of new expenditure in 1986 can be attributed to the accession of Spain and Portugal. This part, however, will be covered by own resources paid in by the new members. The remaining part of the increase takes place because of the substantial rise in payments to finance commitments incurred before 1986 and also because of new commitments.

Priorities for the Community budget, endowed from 1986 with increased own resources are (i) to contain agricultural expenditures more effectively; and (ii) to devote increasing resources to structural improvement and convergence of the Community economy.

3.2 Monetary policy and the European Monetary System

In recent years, a consensus has gradually emerged on the need to create a stable monetary environment and on the

contributory role of monetary policy. This consensus contrasts with the marked differences in the management of national monetary policies in the 1970s. By imposing exchange rate discipline on the participating countries, the European Monetary System has shown itself to be an essential factor in the cohesion of monetary policies with a common objective of stability. Such consensus is an important achievement which must be preserved: monetary stability must, for several reasons, be an essential part of any strategy which aims at restoring lasting growth, capable of creating more jobs.

First of all, monetary stability creates an environment which encourages those involved in the economic process to cooperate with each other and in particular reduces the justification for indexation mechanisms. Some of these mechanisms, a relic of periods of high inflation, both obscured and held back the necessary adjustment of relative prices and costs and so contributed to present macroeconomic imbalances.

Secondly, expectations of a permanently low inflation rate enable interest rates to play more efficiently their role in

Table 9

European Community budget, 1984-86: Preliminary draft proposed by the Commission

(million ECU)

Expenditure	1984 EUR 10	1985 EUR 10	1986 EUR 12
Policy functions			
Agriculture — Guarantee Section	18 126	19 691	20 688
Agriculture — 'structural' Funds	667	687	946
Fisheries	87	105	236
Social Fund	1 212	1 410	2 399
Regional Fund	1 413	1 610	2 600
Integrated Mediterranean programmes	10	10	151
Transport	505[1]	36	74
Energy and industry	659[2]	130	105
Research and innovation	533	570	673
Food aid	737	772	954
Development aid	527	531	697
Other expenditures including refunds to Member States	2 733	2 881	5 527
Total	27 208	28 433	35 050

Revenue	1984 EUR 10	1985 EUR 10	1986 EUR 12
Agriculture levies	2 435	2 106	2 699
Customs duties	7 961	8 596	9 700
Value-added tax (VAT)	14 594	15 1981	22 184
Special contributions	596	2 247	204
Miscellaneous	466	286	263
Total	26 052	28 433	35 050
p.m.			
Maximum rate of VAT	1.00	1.00	1.4
Effective rate of VAT	1.00	1.00	1.34[3]
Budget total as share of GDP	0.94	0.85	1.10

[1] Includes 471 million ECU of special measures in the UK and Germany.
[2] Includes 456 million ECU of special measures in the UK and Germany.
[3] Except for Germany 1.31 and UK 0.82.

Source: 1984: Management accounts; 1985 86: Preliminary draft budget 1986 adopted by the Commission on 14 June 1985.

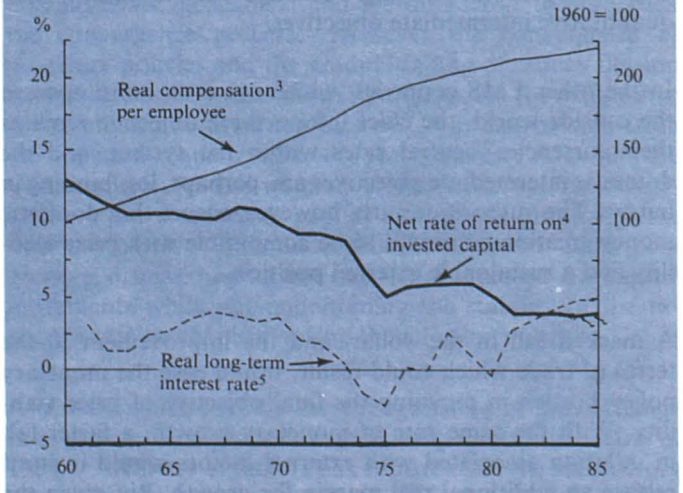
establishing the balance between supply and demand on the capital market. An artificially low or even negative real cost of capital, such as that which obtained in certain countries in the 1970s, gives a distorted indication of the scarcity of capital, encourages the waste of scarce resources formed from savings and leads to a pattern of growth which creates fewer jobs. Of course, excessive real interest rates (for example, greater than the underlying growth rate of the economy) accompanying budget deficits which are too high, have considerable structural consequences. But now the level of real interest rates must make it possible to attract the funds needed to finance not only public deficits, still excessive in certain cases inside and outside the Community, but also to finance the required investment drive. Furthermore, an essential justification for the policy indicated for certain countries of a continued reduction in the public deficit is that it contributes to lower real interest rates in the medium term.

Finally, the level of the real return on capital is a key factor in the investment decision. Present distortions between the cost of capital and the profitability of productive fixed capital originate, as illustrated in Graph 14, in the decline in profitability which occurred in the 1970s, rather than in the more recent rise in real interest rates. Thus, whilst a fall in real interest rates of, say, 1 or 2 percentage points from their present level would certainly help to stimulate investment, it would come nowhere near to restoring the differential which prevailed between real interest rates and the profitability of productive capital in the 1960s, a period of full employment, and which existed again during part of the second half of the 1970s.

As is evidenced by the downward convergence of inflation rates in the Community, considerable progress has been made towards the creation in Europe of an internal and external zone of monetary stability (see Table 5 of this report). Since March 1983 there has been no change in the central rates of almost all the currencies participating in the EMS. The adjustment of the Italian lira's parity, which took place in July 1985 by unanimous decision of the partner countries, remained limited in scale. The stability of nominal and real exchange rates between the currencies participating in the EMS exchange rate mechanism provides a striking contrast with the often sharp variations recorded before the establishment of the EMS and those which are today still affecting other currencies. This stability is naturally reflected in small exchange rate variations between the ECU and its chief component currencies. It satisfies a need felt by private operators, as can be seen from the development of the private ECU as a borrowing and investment currency and its growing use for commercial transactions. Monetary policies, pursuing the common objective of stability, but which have to be differently framed to take account of the progress still necessary in each country, are a guarantee that these achievements will be consolidated and improved.

A number of countries — in particular the Federal Republic of Germany, France, Italy and the United Kingdom — are pursuing normative targets for the growth of monetary aggregates or domestic credit expansion. For countries where the inflation rate is still too high, the aim should continue to be a progressive reduction in the growth rates of monetary aggregates or domestic credit expansion, so as to underpin the stabilization process. Where the rate of inflation and inflationary expectations are sufficiently low, monetary growth should release a margin for real growth in line with the medium-term trend of productive capacity while preserving what has been achieved in terms of stability. This would provide lasting support for economic activity.

GRAPH 14: Rewards of labour, fixed capital and financial capital in the Community[1,2]



1 The above graph has been taken from the report of the Economic Policy Committee concerning 'Profitability and the rate of return in the Community'(2). The graph provides an illustration, on the basis of different definitions, of the development of profitability as presented in Graphs 11 and 12 above.
2 Community average weighted with GDP of 1975 and 1975 purchasing power parities.
3 Deflated by GDP-prices.
4 Net operating surplus of enterprises (excluding housing) as % of corresponding net capital stock (left-hand scale). Because of well known statistical problems, the level of this curve has to be interpreted with caution and it is its evolution which is of greater relevance.
Source: Deutsches Institut für Wirtschaftsforschung (Berlin) on behalf of the Bundesministerium für Wirtschaft (Bonn). Recent years and the Community average have been calculated by the Commission services.
5 Interest rate on government bond yields. Deflated by consumer price index (left-hand scale).

In these countries the setting of the target for monetary growth must, however, be largely influenced by the judgement made on the growth of productive potential, notably with regard to the effects of supply policies carried out in other areas and the increase in capacity utilization rates which can be achieved without creating inflationary strains. To the extent that supply side policies speed the growth of the productive potential, such a strategy goes hand in hand with the sound financing of the increase in demand which then becomes desirable.

It is true that the present changes on financial markets, especially the spread of financial innovations which are tending to make the demand for money more unstable, sometimes complicate the implementation of policies based on monetary aggregates or credit targets. But experience has shown that, where the authorities of the EMS countries are determined to pursue a policy which conforms with guidelines based on the above criteria, the exchange rate mechanism is stabilized and its macroeconomic effects reinforced. For EMS countries, the quantitative intermediate objectives of monetary policy and the exchange rate objective thus mutually reinforce one another. Furthermore, the United Kingdom authorities are tending to attribute more importance to the sterling exchange rate alongside their quantitative intermediate objectives.

In the other EMS countries, which are even more open to the outside world, the chief intermediate objective remains their currencies' central rates within the system, and the domestic intermediate objectives are, perhaps, less binding in nature. The authorities must, however, ensure that domestic money creation continues to be compatible with price stability and a sustainable external position.

A marked fall in the dollar, and the improvement in the terms of trade which could result, would ease the monetary policy burden in pursuing the final objective of price stability. With the same rate of monetary growth, a faster fall in inflation associated with external factors would in itself release an additional real margin for growth. But given the present instability of the international monetary system, lasting stability can be guaranteed only by the continuing control of monetary growth. However, following the recent declaration by the Ministers for Finance of the five major industrialized countries, it is to be hoped that a solution to this instability will be found which, at the same time, will help to relax even further the external constraints which may stop interest rates from falling in Europe.

In the convergence process, the stability of bilateral exchange rates within the EMS is of prime importance. For one thing, in the countries where inflation is highest, such stability reinforces internal efforts to bring down inflation. In these countries, because of the greater convergence of inflation rates and allowing for the lira parity adjustment in July 1985, the rise in nominal effective exchange rates weighted by inflation differentials against partner countries (real exchange rates) is still moderate, but nevertheless illustrates the stabilizing effect of an exchange rate mechanism which provides for fixed but adjustable parities. Secondly, the competitiveness gains obtained by the more stable countries help them to acquire a comfortable external position and contribute to the release of a real margin for growth. But these considerations do not exclude a realignment of central rates in the event of fundamental disequilibria.

In the last few years, the internal cohesiveness of the EMS, which admittedly has at certain times also benefited from favourable external factors, has above all been guaranteed by the stronger consensus on the priorities to be adopted and the methods to be used in all areas of economic policy, the increased convergence of performances and the close coordination of monetary policies both internal and external. However, major progress is still necessary to achieve a satisfying degree of convergence. In this respect, some countries must, in any event, still make substantial efforts with regard to budgets and incomes so as to reduce the sometimes excessive burden borne by monetary policy in the stabilization process. The greater growth is in the Community, the more rapidly will these efforts be crowned with success.

The room for manoeuvre available to the authorities for influencing interest rates is largely determined by interest rate levels on international markets and by the pursuit of the intermediate and final objectives of monetary policy. As regards the external constraint, European short-term interest rates did not completely follow the upward movement of United States short-term rates in the first six months of 1984, and then their marked fall in the following 12 months. As an average for the Community countries, the fall in short-term rates between December 1983 and July 1985 was steadier but slightly less marked than in the United States (1.1 percentage points for Europe compared with 1.7 percentage points in the US). The prudent management of short-term interest rates in Europe, tailored to the needs which still exist as regards internal stabilization and to the severity of the external constraint, and a more favourable trend of fundamentals (external and budget deficits) reinforces, on this side of the Atlantic, the credibility of the policies implemented. This has contributed to a notable fall in nominal long-term rates (1.7 percentage points) which, between December 1983 and July 1985, was more marked in Europe than in the United States.

Until March 1985, the strength of the dollar impeded the fall of short-term interest rates in Europe, but the situation has since changed, and some room for manoeuvre has appeared. It is already being utilized in the Community countries with the lowest inflation rates. In Germany, the money market rate has thus been cut by around 1,6 percentage points since March 1985 and now stands at 4,5 %, its lowest level since the end of 1978. A favourable international context would make it possible to make even more use of this margin. In countries where there is still a major need for stabilization, and where monetary policy must go on contributing to the convergence process, nominal interest rates could, however, continue to fall in line with the reduction in the inflation rate. To the extent that this difference in managing interest rates, in line with the internal monetary policy objectives in the different countries, leads to the maintenance of the right interest rate differential within the EMS, it also reinforces the stability of the exchange rate mechanism and its internal cohesiveness in response to external shocks, despite the divergences which still exist in certain fundamentals.

In the Community countries real long-term interest rates, measured as a first approximation by the differential between nominal interest rates and the rate of increase in consumer prices, rose by an average of 4,5 percentage points between 1981 and 1984. The rise was particularly marked in countries where they had been close to zero or even negative at the start of the 1980s, while the rise was only some 2 percentage points in the more stable countries. When disinflation is rapid or when the inflation rate is historically low, the real interest rate, measured by the differential between the nominal interest rate and the current rate of price increase, is probably overestimated in relation to a measure which would take account of the inflation rate expected in the medium term, which is probably then higher than current inflation. Conversely, in countries where the inflation rate is still high but where the disinflation process is well under way and credible, the real interest rate expected in the medium term is higher than that measured by the current inflation rate. In any event, inflationary expectations play a key role in the formation of nominal interest rates which increases the importance which should be attached to the conduct of monetary policies with the lasting and credible aim of price stability. Such policies help to bring the current inflation rate and the expected inflation rate closer to one another and to stabilize them at the lowest level and this makes the formation of nominal interest rates more rational and creates a suitable environment for their steady and lasting reduction.

Within the Community, the upward convergence of real interest rates is evidence of the now common course of monetary policies in a context of generally high public deficits and severe strains on international capital markets, particularly in the United States. Their progressive fall, which is desirable, will have to be soundly based and will depend mainly on both the satisfactory progress and the credibility of the disinflation process and on the absorption of financial imbalances, particularly of the public deficits inside and outside the Community.

The effective liberalization of capital movements inside the Community and, at the same time, efforts towards a greater convergence of economic policies for higher growth, will make possible the completion of the European Monetary System, which is necessary in order to create a European monetary and financial area. Liberalization would favour the development in Europe of a dynamic and attractive financial market and would thus contribute to the better allocation of savings.

Since the establishment of the EMS in March 1979, the objective of liberalizing capital movements has become even more important. To the extent that the restrictions placed on capital movements artificially increase the autonomy of monetary policies, they reduce the disciplinary effect of the exchange rate mechanism and are thus liable to hold back the convergence process. However the convergence of monetary policies and the gradual fading of money illusion among economic agents mean that this room for manoeuvre is not utilized or even non-existent — as can be seen from the upward equalization of real interest rates in the Community. As and when divergences narrow, the restrictions on the freedom of capital movements gradually lose their usefulness. This underpins the argument for a progressive dismantling of the restrictions placed on capital movements while not undermining the stability of the exchange rate mechanism during the adjustment phase.

A climate which favours the strengthening of the exchange rate system has gradually grown up since the start of 1984. A variety of factors has contributed: the satisfactory convergence of monetary policies, the credibility gained by the general process of bringing down inflation, a more open and more evenly spread attitude as to the advisability of resuming the liberalization of capital movements in the interests of the EMS itself and the strength of the parity grid agreed in March 1983 in withstanding external currency movements. This state of mind was demonstrated by the adoption in 1985, by the Council and by the central banks of the Community, of preliminary technical measures which will slightly widen the use of the ECU in the effective operation of the exchange rate system. The possibility has even been mentioned of giving third country holders access to the ECU in the European Monetary Cooperation Fund.

The Community bodies concerned have agreed to keep under review the possibilities of fresh progress in the monetary area, and the conditions for achieving this. The Council of Finance Ministers has confirmed the ultimate objective of economic and monetary union. The development of the EMS, reinforcement of which is doubtless an objective in itself, must also be seen in this perspective. Of special interest here are questions relating to the expansion of the international role of the ECU, both in its public and private uses, and to the participation, on an equal footing, of the component currencies in the exchange rate mechanism.

The creation of a zone of monetary stability is an integral part of the strategy for lasting growth, capable of creating more jobs. By reducing uncertainties as to the future real value of the currency, an environment is created which encourages those involved in the economic process to cooperate with each other. The stabilization of inflation expectations also makes the determination of interest rates on capital markets, which have an essential role in the optimal allocation of the scarce resources formed by savings, more rational. As regards stability, achievements in recent years have been encouraging. Monetary policies, designed to achieve the common objective of stability, but framed accordingly to take account of the progress still necessary, are the guarantee that these achievements will be consolidated. In some countries monetary policy must still underpin the stabilization process, by reducing the rate of monetary growth and by lowering short-term interest rates in line with the progress made in bringing down inflation. The internal cohesiveness of the European Monetary System should, however, be strengthened by additional progress in all areas of economic policy in order to reduce the, sometimes still excessive, burden borne by monetary policy in the stabilization process. In other countries, monetary policy should continue to use the margin available for bringing down interest rates and, while preserving what has been achieved in terms of stability, provide the liquidity necessary for the establishment of a growth rate in line with the medium-term improvement in productive capacity. Here it is to be hoped that recent progress in international monetary cooperation will further relax the external constraints and thus make a fall in real interest rates possible. This would encourage investment in fixed capital rather than in financial assets. Within Europe the adoption of the above-mentioned monetary policy guidelines would, in addition to reinforcing the Community's internal monetary cohesiveness, increase interest in further progress in the construction of the EMS, and in particular in measures to liberalize capital movements and to develop the role of the ECU.

3.3 Market and sectoral policies

3.3.1 Improving the internal market

The completion of a large internal market, as has been proposed by the Commission in its White Paper of June 1985, provides strong support for the successful achievement of a cooperative growth strategy for more employment in so far as it supports a growth in supply, which is both profitable and efficient. A wider market provides the opportunity for firms to expand production and exploit economies of scale. The resulting cost reductions lead to lower prices and hence demand will be strengthened. A faster growth of both demand and output will be reflected in productivity growth and this in turn will feed into the exploitation of new investment opportunities and employment creation. The benefits of improved efficiency and competitivity will be affected also through an increase in the economy's longer-term equilibrium exchange rate and more beneficial terms of trade. A lower trend evolution of both domestic and import prices will in turn mean that a given expansion of nominal demand will result in a higher real demand. Again, there will be beneficial effects on output and employment. Thus, the economy enters what can be called a virtuous circle of economic growth which is not unlike Community experience in the 1960s.

At the same time promoting better competition on markets would be ineffective if structural and social inequalities prevented the completion of the internal market. If the internal market is realized in the context of more dynamic and harmonious growth, imbalances at the regional and sectoral level will be more easily overcome. This is also the best way to take account of the Community 'social dimension' and structural problems. In addition, this requires the development of more coherent European-wide social policies and the strengthening of existing national and Community instruments, the European Social Fund and the European Regional Development Fund for example. Success in overcoming adjustment problems and in achieving the full employment and social benefits of improvement of the internal market will require considerable cooperation between the social partners and governments in the development of these actions and in encouraging the attitudes consistent with the growing integration of the European economy.

Consensus on the importance of improving the Community's internal market has strengthened greatly at the political level and amongst industrialists and trade unionists. At its meeting in Brussels in March 1985 the European Council called for 'action to achieve a single large market by 1992

thereby creating a more favourable environment for stimulating enterprise, competition and trade'. The Commission responded to this call with publication of a White Paper addressed to the European Council meeting in Milan in June 1985, entitled 'Completing the internal market'.[1] The White Paper sets out a detailed programme, calling for over 300 legislative acts, most of them before 1990.

Given the extremely complex and extensive nature of the proposals in total, the Commission has given particular attention to ways to lighten the administrative and legislative burdens of achieving the objective. An integrated and balanced set of proposals made to this end are (i) to maximize use of the principle of mutual recognition of national technical standards and minimize the amount of harmonization legislation at the EC level; (ii) to maximize the off-loading of technical matters from the Council, by making more use of the institutional powers of delegation that exist and; (iii) to increase recourse to majority voting in Community decision-making processes concerning the internal market. Although the various elements interact and should be considered as a whole, some individual examples serve to illustrate the substance of the proposals.

As regards technical standards for industrial goods, food products and construction, it is proposed that legislative harmonization (Council directives based on Article 100 of the Treaty of Rome) will in future be restricted to essential health and safety requirements.

Public procurement competition will be enhanced for sectors already covered by EC directives by more prior information and publication of contracts. Existing restrictions on public procurement of services, compared to goods, should be removed. Four major sectors — energy, transport, water and telecommunications — not yet covered by public procurement directives are to be made the subject of further proposals.

In the transport sector important actions to ensure the freedom to provide transport services are proposed.

Service branches of the more conventional kind such as banking and insurance together with newer forms such as information and data processing, computerized marketing and distribution services, audio-visual services including broadcasting by satellite are undergoing unprecedented technological development. Many of these fastest growing branches of the economy have little chance of being internationally competitive without being given a large open market in which to develop.

Turning to financial markets, the improvement of the internal market for financial services links directly to the policy objectives of improving the functioning of domestic financial markets, the convergence of macroeconomic policies and strengthening of the European Monetary System. In this context, in April 1983 the Commission submitted to the Council a communication on financial integration[2] which stressed the need for more freedom of capital movements between the Member States and for the creation of a unified network of financial services in the areas of credit, insurance, and stock exchanges.

Such integration gives rise to direct and indirect benefits. The direct advantages come through a reduction in financial costs for borrowers and through helping assure access for savers to higher yielding investments. An increase in the effective size of the market induced by financial integration encourages financial institutions to specialize more, creates additional competition and effects a more efficient transfer of savings into real investment.

As regards indirect benefits, the greater liberalization of financial markets enhances discipline in the conduct of economic policies and thus contributes to price stability and to the strengthening of the EMS. A second indirect benefit would relate to reducing dependence of European economies on the US dollar, which is likely to occur if European capital markets become more integrated. This would insulate Europe to some extent from external shocks. Thirdly, controls on capital flows interfere to some extent with the free movement of goods, services and persons, by increasing the cost of related financial transfers whose legality has to be checked. Fourthly, the utility of capital controls in terms of greater independence of monetary policy has been greatly reduced through commitments to monetary policy coordination implicit in EMS membership.

Financial integration should be sought in a balanced way on four fronts: (i) gradual removal of the remaining capital controls; (ii) free flow of financial services; (iii) rationalization of domestic financial markets; and (iv) the promotion of the ECU in the credit and capital markets.

At present two Council directives classify capital flows in four lists (A to D). Member States are obliged unconditionally to free transactions contained in list A (including

[1] Commission of the EC, 'Completing the internal market', (COM(85) 310), June 1985.

[2] Commission of the EC, 'Communication of 20 April 1983 on financial integration', *European Economy*, No 18, November 1983.

direct and real estate investment) and in list B (operations in listed securities). Transactions in list C (including other types of portfolio investments and long-term credits) are conditionally liberalized. There is no obligation to free transactions in list D (deposits with financial intermediaries and other short-term monetary operations). The actual degree of capital freedom varies considerably in the Community. A number of Member States have liberalized virtually all transactions contained in lists C and D. On the other hand, three Member States (France, Italy and Ireland) have had to make use of the protective clauses provided for in the Treaty in order to apply restrictions on transactions which are unconditionally liberalized. In December 1984 the Commission reviewed these derogations and renewed them for a limited scope and period (OJ L 8, 10 January 1985). In addition, the Commission is studying proposals with the Monetary Committee for a new directive which would extend the obligations of Member States to liberalize certain transactions contained at present in list C.

The creation of an efficient network of financial services in the areas of credit, non-life insurance, and stock exchange services can be aided through assuring the right of establishment and the provision of financial services on a non-discriminatory basis across frontiers.

The rationalization of domestic financial markets should go in parallel with the removal of controls on the circulation of capital and services. Although there has been some action towards harmonizing national provisions governing the activities of financial intermediaries, the regulatory and allocative aspects of the domestic financial markets should be given more attention.

Community companies and institutions have used the Euromarkets in order to avoid the disadvantages of narrow national markets. More recently, as the risk in the use of the dollar has become large, the market has increasingly turned to the use of the ECU which exhibits small variability *vis-à-vis* member currencies and is free of purely national controls. It is, therefore, well placed to be a vehicle for capital transfers within the Community.

The Milan European Council in June 1985 welcomed the Commission's White Paper for improving the internal market, and charged the Council to elaborate a work programme to achieve the single market objective by 1992. Ways of achieving this objective are identified as (i) suppression of physical barriers; (ii) the removal of fiscal frontiers; (iii) suppression of technical barriers (especially for new technologies); (iv) creation of a free market in financial and transport services; (v) complete freedom of establishment for the professions; and (vi) liberalization of capital movements. The integration and modernization of European financial markets should be pursued further through rationalization of domestic financial markets and promotion of the ECU in credit and capital markets. This process will be facilitated by the more dynamic growth fostered by the overall economic strategy, and thus enhance with other more specific measures the social dimension.

3.3.2 Infrastructure projects of European interest and infrastructure financing

Improving the internal market needs also the provision of an adequate infrastructure. In the programme for 1985, the Commission identified the benefits to be obtained from a coordinated infrastructure strategy. Such an approach would contribute significantly to the aim of unifying the internal market, strengthening industrial competitiveness, integration of the peripheral regions and stimulating new technologies.[1] It could also become, progressively, an important element in the development of demand and economic activity.

In the area of telecommunications, concertation mechanisms have been set up between the Commission, Member States, industry, and national telecommunications administrations. The work and reflection carried out so far have identified the common prospects for the evolution of telecommunications networks and services and the strategic objectives upon which a consensus at Community level could be reached, in order to define infrastructure projects of European interest in this field.

This is in particular the case for the establishment of a telecommunication transborder backbone network which could set up the base of future integrated broadband (IBC) communications to be operational by 1995.

According to available estimates, the total investment related to the project could amount to some 3 000 million ECU. Currently, studies are carried out to specify the project further. The project will, however, depend on prior agreement between the public authorities and the telecommunications administrations concerned.

The Commission will make proposals on the use of the ERDF to help improve modernization of telecommunications networks in the less favoured regions of the Community.

[1] The necessity for investment in employment-creating infrastructural projects in transport, telecommunications and environmental protection was stressed in Parliamentary resolutions (OJ C 122 59, 20.5.1985, point f and Doc. B 2-103/85, point 1a).

In the area of transport, the Commission's proposed medium-term infrastructure programme already provides a framework for the development of three linking networks of Community interest: road, rail and inland waterways. The investment in question would exceed 20 000 million ECU. This programme contains a range of small and medium-sized projects some of which have already been started and receive Community finance from the ERDF and the EIB and specific credits for the support of transport infrastructure of Community interest (line 581) as well as some major projects. The financing of these projects will naturally differ according to their relative size and character. A large number of smaller projects will have been included already in national public investment programmes and will have received Community financial support. However, the financing of the larger projects has yet to be arranged.

Two major projects should be added, the Paris-Cologne high speed rail link, the cost of which has been put at some 3 000 million ECU. An 'intergovernmental group' has been set up to work out the general specification of requirements, each party's responsibilities and the possible financial package. The final report is expected in March 1986. Also the fixed Channel link which, depending on the type of link, varies widely in cost from 3 000 to 9 000 million ECU. In April 1985 the French and United Kingdom Governments published the guidelines enabling those promoters interested to prepare by 31 October 1985 a proposal for financing, executing and exploiting the project. Work could thus start by the end of 1986, completion being planned for 1992-93.

In the longer term other projects are envisaged in the area of road and rail transport, in particular the motorway link with the Scandinavian countries through Denmark and the Baltic straits, the Venice-Munich link with its passages through the Alps, etc.

In the area of environmental protection, a programme of investment is necessary to improve the quality of life and protect the basis for future economic growth. The damage caused by air pollution can only be reversed by investment in large combustion installations, while in many Member States investment in effluent treatment is essential to improve water quality. The treatment of waste and its recycling would both improve environmental quality and reduce the Community's raw material dependence. Such investment, leading to the development of new products, will not only improve the quality of life but also create markets for new products in third countries.

Thus all in all, the infrastructure programme which can be envisaged in the medium term would represent an investment volume of 30 to 45 000 million ECU over a period of five to seven years.

All these infrastructure projects are not, of course, at the same stage of development. The Community can facilitate the advancement of the larger projects in several different ways; by giving its support to the proposals already made, easing administration and fiscal conditions, taking the initiative in bringing together interested parties, and by financing the necessary feasibility studies.

At the same time the Commission has undertaken to study the scope for using or adapting the range of financial instruments at its disposal as well as ways in which the Community could improve and simplify the administrative and legal framework in which infrastructure projects can be carried out.

Apart from continuing with the traditional types of infrastructure financing, the use of new financing formulae can be envisaged, which aim in particular to reduce the guarantees required from the promoters or to base these guarantees on the assets of the project rather than on those of the promoter (formula of the project financing type or preferential claim on receipts). Because the financial package required for this type of investment needs to combine in variable proportions, capital formation, bond market flotations and bank loans, Community intervention should bring together new and traditional financing techniques.

There exists a considerable economic potential in a number of large infrastructure projects of Community interest, notably in the areas of cross-frontier transport, telecommunications and environmental protection. At the macroeconomic level these would make a modest but nevertheless useful contribution to growth. The Community should facilitate the advancement of the projects, inter alia *through the easing of administrative and fiscal conditions, through the development of its own financial instruments, and thus contribute over the next five years a useful dynamic element in the Community's economic development.*

3.3.3 Adaptability of the labour market

Given the urgent need to improve the conditions for employment growth in the economy, increasing attention is being given currently by governments and the social partners to the task of making the labour market work more efficiently. This involves improving the adaptability of the European labour market to structural change, especially to the introduction of new technologies and to competition from the United States and Japan as well as the newly-industrialized countries.

Table 10

European Community investment financing through capital market borrowing and on-lending

(million ECU)

	1983	1984	(1985) estimate
Lending by institution or mechanism:			
European Investment Bank	4 256	5 013	:
Commission			
European Coal and Steel Community	778	825	:
Euratom	366	186	:
New Community Instrument	1 212	1 181	:
Total	6 612	7 206	7 400-7 700
Lending by sector or policy objective:			
Private industrial sector	1 938	2 850	2 700-2 900
of which: global loans to small and medium enterprises	1 263	1 860	1 900-2 100
Infrastructure	2 241	2 344	2 250-2 300
Energy	2 433	2 012	2 450-2 500
Total	6 612	7 206	7 400-7 700

Source: Commission of the EC, 'Report of the Commission to the Council and the European Parliament on the borrowing and lending activities of the Community in 1984' (COM(85) 213 final).

In the last *Annual Economic Report*, the Commission identified examples of labour market regulations which had turned out to be designed inefficiently or in ways that serve to deter employment. It called for a re-examination of labour market regulations in order to ensure both greater equality of access to employment and greater efficiency in the use of labour within enterprises.

The Economic Policy Committee is in the process of examining this question in relation to labour and other markets. In addition to the question of wages and non-wage labour costs discussed above, the Committee has paid attention also to the question of labour market regulations, mobility, training and more flexible use of working time.

In conjunction with the Member States and the social partners, the Commission is currently carrying out a comprehensive review of the legislation and collective agreements in these fields. A group of experts is studying also the attitudes of social partners and governments to the problem of labour market flexibility. A communication will be sent to the Council.

The social partners are principally responsible for the adaptability of the labour market. Where government regulations are important, any specific proposals to change them — particularly those concerning job tenure or dismissals — should be fully discussed with the social partners. Governments should also review to what extent they themselves are inhibiting the workings of the labour market by the complexity of administrative regulations they impose on employers.

Some actions have recently been taken by member governments with the intention of improving the adaptability of the labour market. For example, in Germany, new measures allow limited term employment contracts and promote part-time employment. In France, regulations governing fixed-term contracts have been relaxed to promote the recruitment of the long-term unemployed, and measures have been taken to promote part-time employment. In Italy rules restricting the choice of employers on whom to recruit have been relaxed.

Another important factor inhibiting adaptability of the labour market are weaknesses in employment and training services geared to current and future labour market needs. To make good these weaknesses will require the cooperation of representatives of governments, and social partners at local, regional and national levels. The Commission is currently pursuing a programme of consultations designed to promote this kind of forward-looking labour market management in the Community.

For their part, governments should continue to examine whether the structure and organization of their employment services are adequate to meet the demands of a rapidly-changing market.

Improving the adaptability of the labour market also encompasses the need to reorganize existing work patterns, and in particular working time but in ways which would be broadly neutral with respect to costs. The reorganization and reduction of working hours can be designed to maximize employment effects while maintaining competitiveness and the basic social rights of the employees. Collectively-agreed working time reductions in France, Belgium, Netherlands and the Federal Republic of Germany have often been accompanied by a rearrangement of working hours so that productive equipment, especially advanced machinery in high growth markets, is utilized more efficiently. Traditional barriers between daily full-time work, shift work in its various forms, part-time work over periods of time, overtime working, etc., have become less pronounced. The traditional full-time work in a standard working week, which continues to apply to the majority of those in work, coexists with an increasing number of more differentiated work contracts which can meet both the aspirations of the employees and the requirements of production. Such measures in the industrial sector have helped to save jobs which would otherwise have been lost. In the service sector an increase in employment has been reinforced by these measures. In some branches, for example the retail trade, the number of employees may rise despite a declining volume of work, due to the growing importance of part-time work.

Within the framework of the collective agreement in the German metal-working industry which reduced average weekly working hours from 40 to 38,5, about 70 % of the companies have reached agreements to maintain operation time. The company agreements take various forms. In France more than 500 enterprises, usually in the context of solidarity contracts, have reorganized working and production time in agreement with the unions. These have often led to a substantial increase in the utilization of capital equipment. In Belgium and the Netherlands innovations in working time arrangements have also been numerous. A recent survey carried out for the Commission indicated that a large proportion of the labour force would be prepared to consider the possibility of new working time arrangements.

Improved adaptability of the labour market is an important component of a strategy for more employment-creating growth. This broad concept has in practice many detailed aspects, including the various conditions of employment in addition to pay, the organization and reduction of working time and the adaptation of working skills and patterns to new technologies. These, however, should be appraised within the general constraint of avoiding cost increases. While governments have to consider whether legal regulations inhibit the workings of the labour market, the social partners have often the major role in negotiating together conditions that will be helpful for an employment-creating growth strategy. The general objective must be to seek improvements to the functioning of the labour market that reconcile to the maximum degree the objectives of economic efficiency and an enhanced employment propensity with social values of equity and security.

3.3.4 Specific employment programmes

The process of reducing unemployment by means of macroeconomic policy measures will take several years. Thus, in the meantime, specific employment measures will still be required. The high level of unemployment is particularly serious in old industrialized areas of declining employment and the under-developed areas which had never achieved self-sustaining industrialization. Its effects can also be seen in the very high rates of youth unemployment (three times the adult rate) and in the increasing number of long-term unemployed (39 % of the total unemployed have been unemployed for more than one year).

The Commission proposed guidelines for temporary work measures already in its communication on long-term unemployment in 1984.[1] At that time, it stressed the need for temporary work programmes to be prepared in collaboration with local and regional governments, and so be suitably adapted to local needs. Temporary work measures of this kind need to be publicly funded but often involve the voluntary sector or non-profit enterprises as well. The net financial costs to public budgets is generally small since a high proportion of the unemployed who would be engaged on temporary employment programmes are already in receipt of unemployment benefit or other forms of social support.

Many Member States have been developing such temporary work schemes specifically aimed at particular groups of unemployed. For example, in Germany, the public interest jobs (ABM —*Arbeitsbeschaffungsmaßnahmen*) for up to one year are aimed at 'difficult to place' unemployed who are in receipt of unemployment benefit. The government pays 60-100 % of the cost. In France, young people aged 18-21 can be given jobs in the 'TUC' schemes (*Travaux d'Utilité Collective* — jobs of benefit to the Community) and through 'solidarity contracts' between local authorities and non-

[1] Commission of the EC, 'Action to combat long-term unemployment', (COM(84) 484 final), 1984.

profit organizations. The jobs include vocational training, and the government contributes to the cost. In the United Kingdom, the Community programme is aimed at adult long-term unemployed. The government pays a wage subsidy. These various schemes are in 1985 reaching around 100 000 people in each of the three countries mentioned.

In general, these types of programmes have several advantages over alternative public job-creation schemes (limited substitution effects, more precise demographic and geographical targeting, lower budgetary costs). Nevertheless, as a solution to the problem of unemployment, they can only play a relatively minor role. The productivity of these jobs may be relatively low, and the slight amount of associated training does little to enhance the long-term job prospects of participants.

Another specific measure adopted by a number of Member States is the provision of assistance to help the unemployed set up their own business. In general, such measures allow the unemployed, under certain conditions, to capitalize their unemployment benefit into a lump sum, or to continue receiving unemployment benefit at the same time as they are self-employed, or a combination of the two. In France, for example, the government gives a subsidy to unemployed people who set up their own business. In the UK and Ireland, a weekly allowance is granted to unemployed persons who can also put up a certain amount of their own resources. In the Netherlands, people can receive a loan and an income supplement up to the level of social assistance during the start-up period. In most cases, eligibility for the allowance is conditional upon having been unemployed for a certain period or is limited to the maximum period of qualification for unemployment benefit (usually 12 months).

The role of local government and non-government organizations in the development of small local-level enterprises is crucial. In a recent communication,[1] the Commission highlights the key role of local support structures which are able to offer encouragement, information, guidance and assistance to those involved in enterprise and employment creation.

While fundamental solutions to the unemployment problem will take many years, quicker solutions have to be found to alleviate the heaviest concentrations of unemployment, for example among young people and depressed regions. Several countries have developed schemes for relatively low-cost employment on activities of public interest, targeted on such groups and areas. There are also examples of incentive schemes for unemployed persons to set up their own businesses. Rapid experimentation and development of such schemes is called for, drawing on local organizations in both public and private (profit and non-profit) sectors.

3.3.5 Education, training and technology

The speed and scale of technological change is creating new and urgent needs, particularly for considerable numbers of technical specialists, and for the retraining of adults whose jobs are affected by technological change. These pressures, combined with the demographic bulge in the numbers of young people, persistent high unemployment and the continuing restructuring of industry in the Community, are leading already to major changes in the education and training policies of the Member States.

For example, a striking development has been the rapid expansion in youth training provision in recent years. Some 700 000 apprentice places are now available annually under the German 'Dualsystem'; the United Kingdom's Youth Training Scheme has over 300 000 participants at any one time; and in France the number of training places supported under the government's special measures is approaching 500 000. Member States are also making major efforts to ensure that young people acquire a basic understanding of the new information technologies before they leave school, and to improve the vocational relevance of the curriculum — even in non-technical subjects. Policies on the youth employment and training problems have been recently reviewed in a Commission memorandum.[2]

Through its work programme on 'New information technologies and the school systems'[3] the Commission is offering technical support in the areas of new information technologies and the school curriculum, the training of teachers, and educational software and hardware.

A parallel programme is under way in the field of vocational training.[4] Under the new guidelines for the management of

[1] Commission of the EC, 'Community action to combat unemployment — the contribution of local employment initiatives', (COM(83) 662 final), 1983.

[2] Commission of the EC, 'International Youth Year', (COM(85) 247 final), July 1985.

[3] Commission of the EC, 'New information technologies and the school systems in the EC', (COM(84) 722 final), June 1984.

[4] Commission of the EC 'Vocational training and the new information technology', (COM(85) 167 final), April 1985.

the European Social Fund issued in April, the Commission is giving priority to training programmes linked with the introduction of new technologies.

In July 1985 the Commission published proposals for a new Community programme in education and training for technology (Comett).[1] This is designed to encourage university-industry cooperation, within a Community framework, on advanced training in the new technologies. It will help ensure that the competitiveness of the Community's industries is not inhibited by shortages of highly skilled manpower, and encourage economies of scale by facilitating joint training programmes in specialist skills. The programme, which is due to start in 1986, includes: (i) funding for a Community network of university-industry training partnerships; (ii) grants to enable students, academics, managers, trade unionists and others to be seconded to universities or enterprises in other Member States; (iii) joint training projects involving enterprises and universities from different Member States, designed to meet specific manpower shortages; (iv) the feasibility of establishing a European technological open university system will also be examined. The Commission intends to submit a communication, before the end of 1985, proposing Community action in the field of education technology (especially through the use of information technology) in order to improve the access and the cost-efficiency of education and training.

The speed and scale of technological change is creating new and urgent needs to develop a technological awareness among the working population at all levels. Combined with the problem of high unemployment, especially among young people, major changes are being made in the education and training policies of the Member States. The Community can add to this process, as illustrated by recent Commission proposals for giving a Community dimension to university-industry cooperation on training in new technologies.

3.3.6 Sectoral policies, technology and enterprise

The adjustment and improvement of industrial structures, technological development and the creation of new enterprises constitute some of the main objectives of Community policies. With regard to sectors suffering from excess capacity, the Commission has adopted policy proposals in several areas.

Agriculture: the problems which occurred in the markets of certain agricultural products — especially the problem of surplus production — have led to substantial changes of the mechanisms of the common agricultural policy (CAP) in recent years.

'Guarantee thresholds' were introduced for main agricultural commodities together with quotas in the milk sector, thereby limiting the previously open-ended support guarantees. In so far as the decisions on agriculture prices for 1985-86 are concerned, the Commission proposed a continuation of its restrictive price policy; to a large extent the Council did not follow these proposals, in particular for cereals and rapeseed. The Commission proposed a reduction in prices of 3,6 % but the Council did not reach an agreement. As a result the Commission has been obliged to take special measures for this product under its own authority. The new structural policy, which was decided upon in 1984 and 1985, avoids encouraging the production of surplus products. In line with these measures to adjust supply to demand for agricultural goods, the Commission has recently published a Green Paper on the perspectives for the CAP[2] in which it proposes various options and insists on the need for a price policy which is more related to market conditions. The income-support function which has so far been ensured by the price policy could in future be met increasingly by production-neutral income aids.

To support the necessary adaptation of the European agricultural sector, the Green Paper opts for measures to facilitate structural adjustments, to change to efficient alternative productions and to create additional income, or alternative employment for farmers.

Steel, shipbuilding and energy policies: Community policy for steel and shipbuilding is aimed at restructuring in line with a more market-oriented approach, together with concern for the social consequences of the rapid decline in size that these industries have been experiencing.

The Commission's recent decisions bearing on the steel industry clearly illustrate this general approach.[3] Their aim is to achieve further cuts in capacity within a much more market-oriented framework while increasing the provision to handle the social effects of restructuring. Thus all investment and operating aids are to be suspended after the end of 1985, the present minimum price system for steel products

[1] Commission of the EC, 'Community programme in education and training for technology', (COM(85) 431 final), July 1985.

[2] Commission of the EC, 'Perspectives for the common agricultural policy', (COM(85) 333 final), July 1985.

[3] Commission of the EC, 'The organization of the steel market after 1985', (COM(85) 382 final), July 1985.

will be ended, and production quotas will be phased out over a three-year period. Special State subsidies will continue to be permitted only for environmental protection programmes, research and development and plant closures.

At the same time, increased and better coordinated spending on regional and social programmes in areas affected by the continued rundown of the industry are envisaged.

In 1985 the Commission published a study of energy prospects to the end of the century, and then followed this by proposing new Community energy objectives for the year 1995.[1] These objectives are designed to ensure that the Community's economic performance is not undermined by renewed energy problems in the longer term. The Commission also published an analysis of restructuring in the Community's oil refining sector which paid particular attention to the impact of exports of refined products from the Middle East and North Africa.

Technology: Europe has traditionally looked to knowledge-intensive, high value-added industry as the basis for its economic prosperity. But Europe's leadership in many fields of technology has been increasingly eroded as new competitors have managed to diffuse many significant innovations faster. The share of the Community of Ten in total industrial world (OECD) high-tech manufactured exports fell from 58 % in 1963 to 43 % in 1983; those of the US from 27 % to 21 %, while those in Japan rose from 5 % to 23 % during this period.

The organization of a European effort to reverse these trends has in the last year been progressively taking shape, especially through the definition and implementation of Community strategic R&D programmes such as Esprit or Brite. In the sector of telecommunications, which is to play a major role in the reinforcement of the competitivity in the world economy, the Council has approved in July 1985 the definition phase of the RACE programme (Research in advanced communication for Europe).

The actions undertaken in the technology field are complemented by measures aimed at creating the European-wide market necessary to recoup the R&D and production investments required by the high-technology products and services (common standards, opening of public procurement, etc.).

The European Council, meeting in Milan in June 1985, gave a new impulse to these efforts, approving a communication of the Commission on the strengthening of technological cooperation[2] and supporting the Eureka initiative proposed by the French Government.

The Commission's communication to the European Council 'Towards a European technological community' sketches out the range of organizational techniques, as well as the possible substantive domains of technological advances, that the Community should now pursue. The general objectives are to (a) exploit to the maximum the Community dimension of a continental market and network of research institutes and facilities; (b) promote the greatest possible synergetic effects from the interactions of national and Community efforts, possibly with an additional Community contribution and participation of non-member countries.

Creation of new enterprises and simplification of existing regulations: A number of measures have recently been proposed or adopted in several countries of the Community with the intention of reducing regulation and thereby the costs imposed on small companies, particularly in their creation. It is to be noted that the biggest increases in employment in the Community in recent years have occurred in new enterprises. Small and medium-sized enterprises are thus seen to be an important source of new employment creation for the future.

The examination of existing regulations does not mean that all rules should necessarily be called into question. It is more a question of simplifying existing regulations and ensuring that the manner in which they are applied does not constitute a handicap for employment.

At a Community level, the Economic Policy Committee, in parallel with its work on flexibility in the labour market, is examining the flexibility of product markets, including the impact of regulations on companies as well as other aspects of government intervention. The Commission intends to submit a communication before the end of 1985 on the reform of business regulation and the promotion of a dynamic small and medium-sized enterprise sector.

Small and medium-sized enterprises are dependent to an important extent on the general conditions in which they operate, in particular those relating to taxes and social security contributions. For such enterprises the access to capital markets is generally narrower than for large public companies; their investment plans therefore depend particularly on their capacity for self-financing. In most member

[1] Commission of the EC, 'Energy policy objectives for 1995', (COM(85) 245), 1985.

[2] Commission of the EC, 'Towards a European technological community', (COM(85) 350 final), June 1985.

countries the characteristics of small and medium-sized enterprises are not given due consideration in income tax legislation, which thus tends to impede the setting up of new enterprises and to slow the growth of existing enterprises. It is therefore appropriate to examine income tax legislation in the Member States for its effects on small and medium-sized enterprises, and if necessary change the provisions relating to the definition of taxable income and the structure of tax rates in order to strengthen the employment potential of such enterprises.

As regards the frontiers between private and public sectors, one of the interesting consequences of technological advance is that, in some sectors, traditional 'natural' monopolies may no longer exist. One example is in telecommunications networks, where privatization and deregulation have taken place in the UK (with parallel or similar developments in the USA and Japan) and where discussion is also underway on the role of the Bundespost in the telecommunications market in Germany.

The Commission has adopted specific proposals either to reduce production capacity in sectors such as steel and shipbuilding, or to reinforce control on production in agriculture. It also made proposals for the organization of a 'technological community'. Allied to these sectoral objectives are the many detailed initiatives which are being undertaken to make the European business environment more conducive to the creation and expansion of enterprises.

4. European interests in the international economy

4.1. The world trading system

The prosperity of the European economy depends greatly upon an open world trading system. There is strong evidence, in economic theory and practice, to show that protectionism does not pay as an instrument of general economic policy. The protection of limited producer interest groups does provide income and employment protection to those groups in the short term. However, other adverse effects of protectionism are present even in the short term, while the negative long-term effects are even more disadvantageous. Protection has the effect of increasing consumer prices, cutting real incomes and real consumer demand and hence output and employment in the economy as a whole. Where the protected goods or services are inputs into the production of other branches of the economy, as is often the case, then those branches themselves lose in competitiveness in world markets. They then lose orders and have to cut employment, unless the exchange rate is devalued to compensate. With devaluation standards of living are reduced and the problem of inflation is worsened. Macroeconomic policy has to become more restrictive, thus again weakening real demand and output. Alternatively, branches of industry faced with uncompetitive inputs from protected sectors are forced to try to evade this disadvantage by substituting these inputs with alternatives (e.g. plastic for steel components), or by relocating their investments in other countries where the inputs are competitive (e.g. some EC biotechnology firms are investing outside the EC to gain access to cheaper agriculture inputs). These general arguments have been set out in greater detail in official documents of the EC,[1] as well as elsewhere such as the OECD.[2]

For these reasons the EC is in favour of a new round of multilateral trade negotiations. Preliminary discussions have been under way in the course of 1985, and the decision in principle to begin the negotiation process is expected to be taken shortly.

Trade liberalization and the unwinding of protectionism can of course be a difficult process for the industries concerned, and for working people when their existing jobs may be threatened in the absence of encouraging prospects of alternative jobs. Therefore there has to be agreement over a balanced set of trade liberalizing measures, otherwise the adjustment costs may be unfairly distributed across the world trading community.

The Community's attitude towards a new GATT multilateral trade round is expressed in the Council's declaration on 19 March 1985; and it has subsequently set out its ideas on the subject matter of such a negotiation and the Community's principal objectives in a written submission to GATT on 8 July. Commitments undertaken in the OECD and GATT to halt protectionism and roll back protectionist measures should be implemented, without waiting for the new round. In this regard it is important to note that some protectionist measures (e.g. steel products) were taken by the United States after the Williamsburg Summit. In addition, some disquieting protectionist trends have appeared in Congress, although these have in general been opposed by the Administration. Japan could be supportive in helping to alleviate protectionist pressures in both the US and the EC by rapidly and substantially giving effect to its

[1] Economic Policy Committee of the EC, 'Opinion on protectionism', *European Economy*, No 19, March 1984.
[2] OECD, 'Costs of Protectionism', 1985.

declared objective of facilitating access for imports, especially of manufactured goods. The US deficit and Japanese surplus cannot, however, be sufficiently rectified by trade policy measures alone, which is why the Community argues in favour of a more concerted approach to exchange rate and macroeconomic policy internationally. This point of view is reinforced by the outcome of the September 1985 meeting of the Group of Five ministers for finance and central bank governors which underlined the importance of maintaining an adequate level of world demand and the joint responsibility to reduce world current account imbalances and resist protectionist pressures.

The Community also favours the participation in a new GATT round of the largest possible number of newly-industrialized countries. Several of these countries have achieved impressive penetration of export markets while maintaining extremely high protective barriers to their own markets. Further liberalization by these countries is a necessary counterpart to their expressed desire to see their own conditions of access to world markets improved in a new round. Finally the EC has indicated its willingness to include trade in services in a new round, and is actively seeking a basis for agreement on this point with developing countries, some of whom remain sceptical or even opposed to negotiations in GATT on this subject.

The Community is strongly in favour of a new round of multilateral trade negotiations. This, together with improvements in the functioning of the international monetary system, will offer the most appropriate framework for a global review of trade policy options which must be addressed if the threats confronting the multilateral trading system are to be averted.

4.2 Improving the international monetary system

The international monetary scene has continued to be characterized by a high degree of exchange rate instability. Both the US dollar and the pound sterling have recorded very sharp fluctuations during the first half of this year in both nominal and real terms. However, what is probably more damaging to the performance of the world economy as a whole is the tendency for the exchange rates of major currencies to move progressively further out of line from what might be considered their 'equilibrium' levels over long periods of time. Over the six years from the first quarter of 1979 to the first quarter of 1985 the US dollar appreciated in real terms on a trade weighted basis by 63 %, admittedly from an under-valued starting position.

These prolonged shifts have produced a pattern of exchange rates which is incompatible with a stable structure of international trade and capital flows and thus is clearly unsustainable over the medium or longer term. Moreover, import penetration in the United States, resulting from the overvaluation of the dollar, is producing a formidable accumulation of protectionist pressure, which now threatens seriously to undermine the liberal system of international trade that was established under the GATT and promoted further over the post-War period.

Against a background such as this it is regrettable that the Group of Ten (leading industrialized countries), which received a mandate from the Williamsburg Summit in 1983 to examine ways of improving the working of the international monetary system, has been unable to reach agreement on a concrete and more comprehensive programme of action designed effectively to tackle the problem of exchange rate instability. However, following the agreement of 22 September between the Group of Five countries, there now appears to be some measure of accord concerning both the dampening effects of currency misalignments and the scope for concerted action to influence exchange rates and other key economic variables with a view to correcting major imbalances in the world economy.

The main focus of the Group of Ten's report, published in April,[1] has been on the need to improve multilateral surveillance procedures, with a view to achieving better coordination and mutual consistency between the policies of the major industrial countries. Whether the procedural changes recommended in the group's report will lead to significant improvement in this respect remains to be seen. The time may not be ripe to establish a regime of target zones for exchange rates, entailing an obligation to intervene when the limits of such zones are attained. It might nevetheless be fruitful to examine seriously the possibility of an intermediate stage, involving indicative zones, whereby consultation, rather than central bank intervention, would be triggered when the limits were breached. The meeting of the Group of Five in September 1985 marked a certain advance with agreement for the first time in recent years on the desirable direction of movement of the dollar's exchange rate and readiness to cooperate to this end when this would be helpful.

The Community for its part has found that the existence of an exchange rate constraint, as embodied within the EMS rules, has undoubtedly contributed to the achievement of

[1] International Monetary Fund, Supplement on the Group of Ten Deputies Report 'The Functioning of the International Monetary System', *IMF Survey*, July 1985.

more convergent policies and performance among its members. The institutions which are appropriate and effective within a closely integrated economic region such as the European Community are not necessarily applicable to a wider and more diversified group of countries. However, the Community would welcome more effective multilateral surveillance of the exchange rate and of monetary and economic policies of major countries such as the United States and Japan (as well as the Community's own Member States) with a view to achieving more compatible policies. As noted, there are serious problems created for the world trading system due to a major misalignment of exchange rates which in turn result from poor internal and international coordination of monetary and fiscal policies.

International exchange rate instability and misalignment has led to a clearly unsustainable pattern of trade and capital flows. The Group of Ten has so far only been able to agree on modest procedural proposals improving the system. It is extremely difficult for trade policy alone to absorb the problems caused by exchange rate disorders. This is why the Community is pressing for parallel progress in improving the international monetary system alongside the new GATT round. The September 1985 meeting of the Group of Five represents a certain advance in the approach to exchange rate and macroeconomic policy coordination.

4.3 European economic space

The EC exports more to the rest of Western Europe (26 % of total EC exports, excluding intra-EC trade) than it does to any other region of the world. At the beginning of 1984 the EC and EFTA completed the removal of all tariffs and quantitative restrictions between the two blocs. In April of last year they followed this up with a joint declaration expressing the political will to extend Community-EFTA cooperation 'with the aim of creating a dynamic European economic space'. In 1985 a joint communiqué of the Commission and EFTA countries set out the domains of policy which should in the future contribute to developing this relationship. The Commission for its part published a communication detailing how, in its view, this might be done.[1]

First priority should be given to abolishing a series of technical and administrative obstacles to deepen trade relations through simplification of border facilities and origin rules, reciprocal cooperation in technical standards and rules, mutual recognition of test results and certificates.

Other areas where cooperation should be enhanced are in research and development, trade in processed agricultural products, public procurement, border controls on travellers, transport projects and policies, environmental policy and economic and monetary consultations. On several of these topics the Community has recently taken initiatives. It has, for example, been suggested that new programmes to create a European technological community should be open for other Western European countries to participate. The Council is in the process of authorizing the European Monetary Cooperation Fund to designate certain non-Community central banks to become holders of official ECU reserves, and this arrangement could be used by some EFTA countries. Already some of these countries have begun to hold privately traded ECU assets as part of their foreign exchange reserves.

Good progress has been made in opening trade between the EC and EFTA countries. On both sides it is now agreed to build further on these achievements. The Community is seeking, in the light of its own efforts to complete the internal market and deepen economic cooperation, to make it possible for EFTA countries to participate closely in the European economy's integration process. These efforts should of course continue to respect the distinct institutional identities and objectives of the EC and EFTA. The EFTA countries could be invited to contribute to the implementation of the cooperative growth strategy. Current negotations to adapt the existing free trade arrangements between the Community and EFTA countries, necessary because of the accession of Spain and Portugal, aim at a further consolidation and extension of the free trade system in Western Europe.

4.4. International cooperation for world economic adjustments

As already noted, in the medium term the United States economy must move into a phase of major correction of its still mounting external current account deficit. What is still uncertain is the timing and amplitude of this correction, and how it will be induced. Contributing to the adjustment process there will no doubt be elements of both budgetary restriction and cyclical slowdown and of dollar exchange rate depreciation.

The prospect of some adjustment by the United States and its possible effects poses important issues for international economic cooperation. The objective would clearly be to achieve the necessary adjustments with the smallest possible cyclical reverse in the United States itself (obviously the United States' own interest) and, equally also, in the growth of the world economy as a whole. A disorderly adjustment

[1] Commission of the EC, 'The Community and EFTA countries', (COM(85) 206 final), May 1985.

entailing trade restrictions would, of course, be very damaging to the world economy.

From the United States' point of view a given balance of payments correction can be achieved at a higher level of internal economic activity, the higher the level of activity in the rest of the world economy. For the Community it is necessary to achieve more dynamic economic growth and the question arises of how to maintain this in the case of an adjustment to growth in the United States. If such were the case there would also be the question of whether the EC would be acting on its own or in concert with a larger number of countries.

In the hypothesis that the European Community alone tried to sustain its growth trajectory, while other regions in the world passively allowed a US slowdown to depress their growth rates, the EC could move into substantial current account deficit. To a certain extent the Community can afford a reduction in its surplus and even a temporary current account deficit. But it cannot aim to have a deficit on the scale of that in the US. The US's massive external deficit is not an example for the EC to copy.

There would, on the other hand, be a case for the EC to urge that the largest possible number of countries participate in a world economic adjustment. In this context Japan is in a position of particular importance. It has the largest single counterpart to the US deficit, as well as serious problems of an unbalanced trade structure in relation to the EC. An international cooperative action to sustain the world business cycle should see an above average contribution by Japan as regards both exchange rate appreciation and domestic demand expansion. If this contribution were assured, then it might well be possible to extend further a world cooperative action. The European Community could suggest to EFTA countries that they join the EC's initiative. Japan and the newly-industrializing countries of the Pacific region could contribute a useful counterpart to the reduction of the US external deficit. The United States could most usefully help by actions to lower its interest rates, which are a particularly heavy constraint on the growth possibilities of the heavily indebted developing countries, especially in Latin America.

Avoiding a situation where the US economic adjustment process leads to a pronounced and generalized slowdown in world trade is essential to the continuation of an orderly adjustment process in the indebted developing countries, as pointed out by the IBRD in its recent *World Development Report*.[1]

[1] IBRD, *World Development Report 1985*, July 1985.

The IBRD sets out in particular 'High' and 'Low' case scenarios for the developing and industrialized countries which are quite in line with the conclusions drawn above (in Section II.2) about the potential gains from a cooperative growth strategy. Depending upon whether developing countries find themselves operating in favourable or unfavourable conditions as regards the growth of world trade, the terms of trade and the level of interest rates, their capacity to import is substantially affected. For the years 1985 to 1990 the annual average growth rate of developing countries' imports is projected to range from 9,3 % in the 'High' case to 2,5 % in the 'Low' case. The debt service burden of developing countries would rise in the 'Low' case to 28 %; thus the range here is between the debt problem being brought under control to it being aggravated to even more acute crisis proportions than so far experienced. In the latter case the threat to world economic stability would be considerable.

The prospect of an important internal and external adjustment by the United States economy for a period of years ahead poses the question of how the rest of the world's economy will be kept on an adequate growth path. The European Community should be prepared to take up its responsibilities as a large economic region to sustain its own internally generated growth during this period. However, it is equally important that Japan lends its support to a wide-scale international adjustment of this kind, without which the EC might face unacceptable risks as regards its own external account. Without an adequate global cooperation the risks of upsetting the fragile recovery of the indebted developing countries would be very great.

5. Conclusions: Objective, instruments and method

In the present report, the Commission offers to the Council, Parliament and social partners the outline of a cooperative growth strategy which aims at a decisive improvement in the Community's economic performance between now and 1990. The application of this strategy is necessary if a reduction in unemployment, without a rekindling of inflation, is desired. It will produce positive results irrespective of the international environment. Clearly, a favourable environment will facilitate a successful outcome. However, in the uncertain conditions which exist today for the world economy because of the persistent financial imbalances in the United States and the critical problem in some large and highly indebted developing countries, the signal which would emerge from the Community embarking on a cooperative growth strategy would be far reaching. The proposals may be summarized as follows:

Objective: The Community should set clear aims for economic policy. In this report, the Commission proposes a cooperative strategy designed to realize a sustainable growth rate of 3 ½ % over the period 1986-90. This will make possible a growth of employment rising to 1,5 % per annum and will provide the means by which unemployment can be reduced to 7 % by the final year. The pattern of growth will thus become more employment-creating and can take place within a framework consistent with stability of national budgets and the reduction of inflation. Such results will only be possible if all participants furnish the contribution required from them by the strategy and if international cooperation progresses satisfactorily.

Instruments: No single instrument suffices to achieve this objective. However, a number of recent policy initiatives fit well into the cooperative growth strategy, but their implementation needs to be accelerated and accompanied by a further dynamic element in order to secure a sufficient change in the economy's growth trajectory. The main elements may be itemized as follows:

(i) Monetary policy implemented so as to continue further the progress made already in reducing inflation but also allowing room for faster real growth. Faster growth will be possible also by exploiting opportunities which are likely to arise as international monetary conditions serve to accentuate the reduction of European interest rates.

(ii) Budgetary policies which, at a microeconomic level, favour more employment-creating growth. At the macroeconomic level a first aim would be to correct present imbalances but at the same time exploiting, where room exists, opportunities for improving supply and demand together and moving the European economy on to a 'virtuous circle' of investment, output growth and new job creation and thereby to a better equilibrium of public finance. Within the framework of the cooperative growth strategy, tax-cuts and increased infrastructural investment would be some of the principal measures envisaged.

(iii) A moderate increase in real wages to increase the profitability of fixed capital. Together with demand support, this will create a climate at the macro level favourable to fostering an upsurge in investment which at the same time will be more employment-creating.

(iv) Initiatives designed to improve labour market adaptability, the reorganization and reduction of working time, under cost-neutral conditions, should also contribute to making growth richer in terms of employment.

(v) Improved and integrated market policies designed to open up the Community's internal market; liberalize domestic financial markets, and to give a better market orientation to interventionist policies of the Community with due regard to the 'social dimension'.

(vi) Greater investment in Europe's economic potential in the widest sense, ranging from major transport and communication projects of Community interest, through environmental investment, to the better use of Europe's technological potential.

(vii) International policies whereby the Community strives to improve continually the GATT trade system and international monetary system, and, with other countries, acting so as to sustain the growth of world trade and to mitigate the LDC debt problem while inevitable adjustments occur in the US.

Method: A step-by-step method is proposed, so as to assure sufficiently clear initial commitments to give a credible launch to the strategy and establish dialogue between the parties involved, while allowing for later steps to be adapted in view of an assessment of the results, the evolution of economic events and the validity of each parties' contribution.

Step 1: Before the end of 1985 Community institutions and the social partners will seek to achieve consensus on the objectives of the cooperative growth strategy and initiating action judged to be necessary.

Step 2: A first set of actions will be put into operation in 1986, including in particular macroeconomic policy measures, pledges by the social partners on incomes and labour market adjustments, expanded public investment at national and EC level, and proposals for international coordinated action in order to reinforce the dynamics of the movement. In addition, significant progress in the implementation of Commission proposals, contained in its White Paper on the internal market, is necessary.

Step 3: After an appraisal of the results of Step 2, a second set of actions will be implemented in 1987 to confirm and deepen the employment-creating growth movement. Some of these actions will be contingent, however, upon evolution of the EC and international economy, and the adequacy of contributions on the part of all concerned to the cooperative growth strategy. The 1986-87 *Annual Economic Report* will contain an evaluation of progress in this respect.

This outline has been deliberately set out in a very schematic form and much must remain for discussion between the parties involved. However, the principal point is that this should provide a basis for reflection on their own positions of each of the major actors concerned — governments, employers and trade unions. Each actor is, in particular,

invited to consider how his existing position might evolve in the direction of the common interest if it was evident that the other actors were prepared also to adapt their positions.

The second part of this report contains specific guidelines for economic policy in the Member States. As emphasized earlier, the strategy cannot be implemented at a stroke but should be introduced gradually. To achieve this, close cooperation between governments, unions and employers will be necessary.

As far as the demand side aspect of the strategy is concerned, the room for manoeuvre in the two main areas of macroeconomic policy differs considerably. The situation regarding monetary policy is relatively satisfactory. Within the context of a monetary policy geared towards stability, which is largely determined by the EMS, significant potential exists for bringing down interest rates, particularly if the dollar continues to weaken against the ECU.

As far as a possible demand support through government budgets is concerned, implementing the strategy of employment-creating growth presents specific problems in individual Member States. Since the strategy cannot be implemented at a stroke, the recommendations addressed to the various countries must remain realistic and capable of being coordinated. Simultaneously with the moderate increase in wages and the widening room for manoeuvre in fiscal policy — more growth and employment boosts revenue, while expenditure caused by the crisis is reduced - demand support should occur step by step, until the process becomes self-sustaining through private investment and an appropriate development of private consumption.

In some Community countries (Italy, Belgium, Ireland and Greece), the relative level, or the growth, of public debt is such that the consolidation process must be continued at all events. Elsewhere, the German case is particularly interesting. As is indicated in the forecast presented below in the German chapter, growth of 3 ½ % and an increase in employment of 1,3 % are expected in 1986. The price outlook continues to be favourable. The surplus on the balance of payments current account should remain very high (2 % of GDP). The budgetary deficit will decline more strongly than was earlier expected (from 1,2 % of GDP in 1985 to 0,8 % of GDP in 1986). In Germany, therefore, a positive chain reaction is developing between price stability, more growth and employment and expansion of room for manoeuvre in the fiscal and external fields. This room for manoeuvre should be exploited in order to ensure beyond 1986 the steady growth (annual average increase of some 3 ½ %) necessary for a continuing reduction in unemployment. Such a development is in the interests both of Germany and the Community. By acting in this way, Germany would not repeat the 'locomotive policy' experience of 1978. Monetary policy would remain geared to stability; the cooperative dimension of the strategy between governments and social partners, applied in the Community, would facilitate the transposition of the positive chain reaction to other Member States.

In the other Member States budgetary and/or external room for manoeuvre has not yet been re-established. In some of these countries (Denmark, France, the Netherlands and the United Kingdom) it is possible that a similar positive chain reaction to that being experienced in Germany will arise in the near future. Such a progress will appear all the more rapidly in so far as there is a positive contribution from the social partners to the realization of the strategy and as developments proceed favourably in Germany.

Part II — Economic policy in the Member States

Belgium

In *Belgium*, despite the fairly weak private consumption, economic activity accelerated slightly in 1985 because of the vigorous growth of investment and the greater contribution of foreign trade to growth. Inflation continued to slacken. The unemployment rate fell somewhat in the course of the year and the general government borrowing requirement was cut by slightly over one percentage point of gross domestic product. The Belgian franc remained firm even though interest rates fell more sharply than in the other EMS countries.

In 1986, growth is again likely to be modest. The current account surplus will probably grow rapidly, mainly because of the improvement in the terms of trade but the gain in competitivity experienced after the 1982 devaluation will continue to diminish. Consumer price rises will again slow down under the moderating effect of world prices. In view of these prospects, an improvement in unemployment will be difficult to achieve.

Although expansion remains moderate in 1985 and 1986, it is encouraging to note that it is based primarily on exports and investment: this proves that the two priority objectives attained after the first phase of the economic recovery policy (the restoration of the economy's competitiveness and of company finances) are bearing fruit in terms of growth. Nevertheless, given the scale of the imbalances which were created in the 1970s, the recovery remains incomplete and fragile; efforts cannot be relaxed if existing achievements are to be consolidated.

In the 1970s, a gap between the growth rate of labour costs and productivity was accompanied by an important destruction of jobs in manufacturing industry. At the end of the period, in 1981, the rate of return had plummeted from the early 1970s level, the remuneration of capital in comparison with that of labour had deteriorated appreciably and investment activity had dropped. Since then certain profitability indicators point to a recovery, but the remuneration of capital relative to labour has scarcely improved, apart from a revival in 1982 and 1983.

Therefore the conditions underlying a lasting expansion of capital-widening investment are not sufficiently satisfied, whereas the capacity utilization rate is approaching the maximum value of the previous cycle. This is the background against which government efforts to increase competitive capacity should be assessed. In the social recovery law of 22 January 1985, the government set a norm, valid for 1985 and 1986, designed to maintain competitiveness at the 1982-84 average level. This norm is based on the remuneration per head in a common currency relative to the weighted average for Belgium's seven main trading partners. After assessing the statutory norm for the first time early in July, the government concluded that it was being respected in 1985.

Although the merit of setting a norm for the maintenance of competitiveness is that an economic policy priority is clearly defined, the fact should not be overlooked that this reduces the problem of competitiveness to a single measure with all its limitations and imperfections. Other approaches, which place greater emphasis on the 1985-86 collective agreements or on other indicators, tend to suggest that the competitive advantage achieved in 1982 and 1983 began to be eroded in 1984. When the statutory norm is assessed for the second time early in 1986, the situation ought to be re-examined with all the requisite caution, and taking account of the progress relating to elements other than the trend of compensation per employee achieved or planned by competing countries, such as the evolution of labour productivity and effective exchange rates.

It is especially important to safeguard competitiveness because the improvement of employment and public finance hinges on this in the immediate future. The new collective wage agreements covering 1985 and 1986 were signed in the spring. Because the social recovery law, by prohibiting all new advantages, has obliged management and labour to translate productivity gains into work sharing, these agreements open up the prospect that jobs will be created equivalent to some 1,5 % of the number of wage- and salary-earners concerned by the agreements. The scope within the country for underpinning activity is limited by the constraints imposed by the still precarious public finance situation and current efforts to improve it are closely bound up with the measures designed to maintain competitiveness. The decisions of March 1984, imposing a three-year moderation of disposable incomes by requiring a 2 % slice of wages to be paid to the Treasury, introduce a wider split between the growth of wages as costs and wages as income without alleviating the former. A correction of indirect labour costs, which is likely to prove necessary in order to restore competitiveness, would immediately interfere with the programme of improving the public finance situation or would have a moderating effect on domestic demand because of the budget spending cuts necessary to prevent a widening of the deficit. Yet, even though the general government net borrowing has already been pruned by almost 4 percentage points of gross domestic product, from 12,8 % of gross domestic product in 1981 to 8,9 % in 1985, it is still too high. To measure the fragility of what has been achieved, suffice it to say that although non-interest expenditure was markedly reduced, it was barely possible to stabilize total expenditure because of the debt interest burden which climbed from 7,3 % to 10,9 % of gross domestic product in the

same period. It should be stressed that the increase in revenue includes a greater yield from company taxation, although from 1982 on, companies benefited from a variety of tax cuts (the top rate of tax on company profits was brought down from 48 % to 45 %, the additional 'solidarity' tax was abolished, tax exemptions were introduced in exchange for investment).

Despite the efforts made, the vicious circle of deficit-interest payments—larger deficit means that the borrowing requirement is still too high. Therefore for 1986 the last section of the 15 March 1984 programme must be implemented in full and all overspending and any fall in revenue, notably as a result of the programme for cutting taxation from 1986 to 1989 which was voted in July, must be offset within the budgetary ceiling. If all these conditions are met, and given the automatic growth of revenue, the central government Treasury financing requirement should be limited to 9,6 % of gross domestic product in 1986 compared with 10,4 % in 1985. Because of the tax cuts voted, from which disposable income will, from 1989, benefit by the equivalent of 1,5 %, even tighter management of public finance will be required. However, the structure of revenue, and notably the high level of social security charges compared with an average level of indirect taxation, gives some margin for cutting the cost of labour, provided that the effect of this change in structure is not wiped out by the indexation mechanism. On the expenditure side, virtually the only stimulus which the public sector can provide in the short term is to shift expenditure more firmly into areas which favour employment.

Until now, the chief weapon in the fight against unemployment has been wage moderation as a means of improving the economy's competitiveness and company profitability and financial structure. It has been supplemented by a revival, from 1984 on, of public-sector programmes to absorb unemployment — programmes which employ 2,1 % of the labour force in 1985 compared with 1,4 % in 1983 — and by measures to help people to be taken on in their first job, to encourage the unemployed to start their own businesses, and to promote work sharing.

Given the existing measures to reduce taxation and to support employment directly, and the need to go on trimming the public deficit, external trade must provide most opportunities for raising the growth rate and expanding the volume of employment. Here, the economic policy priority must continue to be the maintenance of the right level of competitiveness. Cooperative action at Community level would also help to cut the public sector deficit more quickly and would allow the more rapid creation of the room for manoeuvre which is now missing.

Table 11

Belgium: main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current transactions account	General government net lending or borrowing	Money supply M2[3]	Unemployment in labour force[4]	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	8,5	4,9	3,4	3,1	7,8	0,6	−1,5	8,6	2,2	0,6
1971-80	10,5	3,1	7,1	7,1	11,9	−0,2	−5,0	10,3	5,5	0,3
1981	4,2	−1,2	5,4	8,6	7,7	−4,5	−12,8	5,8	11,2 (10,3)	−2,0
1982	8,3	1,1	7,1	7,6	7,9	−3,4	−11,0	5,7	13,1 (12,1)	−1,3
1983	6,3	0,4	5,9	7,5	6,7	−0,7	−11,7	7,0	14,4 (13,3)	−1,6
1984[1]	7,0	1,7	5,3	6,2	6,2	−0,3	−9,9	6,1	14,5 (13,3)	0,4
1985[2]	6,7	1,9	4,7	4,9	5,7	0,6	−8,6	6,0	13,8 (12,4)	0,4
1986[2]	6,2	1,7	4,4	3,2	4,2	2,0	−7,4	5,5	13,4 (12,2)	0,3

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] End of the year.
[4] Eurostat concept; between parentheses: national concept.

Denmark

In *Denmark* economic activity continued to expand during 1985; estimated real GDP growth was close to 2 1/2 %, down from the almost 4 % recorded the year before, but corresponding to the average annual medium-term trend. Whereas the excellent harvest bolstered total output in 1984 a number of factors combined to slow the rate of increase during 1985. In particular, domestic demand was less buoyant with the sluggish development of private consumption and residential construction offsetting the continued rapid rise in private business investment. Imports of capital investment goods as well as specific consumer items remained strong. Despite the reinforced industrial competitiveness resulting from tight incomes policies, exports, which triggered the present phase of economic expansion, performed less strongly against the background of slower growth in the country's markets. Consequently, the deficit on the current balance of payments, which includes a large amount of interest payments abroad, remained large. More positively, however, inflation continued to level off as domestic costs declined, while private sector employment rose faster than total labour force growth so that the unemployment rate fell by almost 1 percentage point. In addition, the general government deficit narrowed to some 3 % of GDP as real expenditure remained unchanged with current receipts growing in line with GDP.

In 1986, gross domestic product is expected to grow by more than 3 %. Although domestic demand is due to rise at a rate close to that for 1985, changes in the structure of demand reinforced by import substitution are likely to produce a smaller increase in imports. Private consumption should grow, underpinned particularly by a rise in employment, but public consumption will reflect the tight budgetary stance pursued by the authorities. The cyclically sensitive investment categories should benefit from lower financial costs and improved profitability, while discretionary components, particularly in the energy area, are expected to begin to wind down. The relative fall in domestic costs, reflected in lower inflation, should contribute to a further gain in market shares for manufactured goods. Unemployment should show a further improvement compared with the year before.

External constraints and tight budgetary management may mean that realized growth in the period 1984-86 will emerge at slightly below potential. The economic policy pursued by the authorities since 1982 aims at a return to external balance and equilibrium on the central government budget by 1988 and 1990 respectively, and, though the achievement of these objectives also depends to a considerable extent on the continuation of sufficiently vigorous growth in world demand, appreciable progress has been made. The wage restraint pursued in recent years has altered the relative costs of labour and capital and strengthened profitability. At the same time, tight budgetary control has reduced the general government borrowing requirement. Lower inflationary expectations helped to bring down nominal interest rates. Against this background, improved business confidence favoured a rise in the stock of productive capital with private employment growing simultaneously. The result has been the achievement of a much improved equilibirum in domestic macroeconomic conditions with the external balance still lagging however behind the desired objective.

The incomes policy measures adopted in March imply a rise in nominal wages of the order of 2 % per annum. Together with a cut in indirect labour costs equivalent to 1½% of the wage bill as from October 1985 and limitations on other forms of income increase this should bring about a slowdown in inflation and improve profitability. There will also be a favourable impact on employment not only as a result of greater potential output due to higher industrial investment, but also due to an improved mix of capital and labour inputs. However, relatively rapid changes in the product mix and market conditions require a high degree of adaptability in the labour market. It has become increasingly important to update skills acquired in the past in view of current technological progress and to review labour market regulations in order to remove possible obstacles to the potential of the economy to generate jobs. Various measures have been taken to reintegrate long-term unemployed and other groups hit by unemployment.

The pressing need for further improvement in the balance of payments remains a decisive element for the stance of monetary and budgetary policy. Adjustments might be necessary if domestic demand, particularly private consumption, should deviate from the trend compatible with improved external equilibirum. Restoration of external equilibrium must remain an essential policy objective but the authorities' room for manoeuvre in this respect would be enlarged if foreign demand was supported through cooperative Community action.

The growth in money supply fell during 1984 and continued to level off in 1985 as did bank lending. Interest rates declined considerably in response both to the anticipated slowdown in inflation and to a rise in private capital inflows. The differential between domestic and foreign interest rates narrowed consequently; this should reduce the propensity of industry to contract foreign debt. In order to allow a more market-oriented control of domestic liquidity, the National Bank modified at mid-year the domestic credit monitoring system by establishing a new system of marginal

reserve requirement. A more flexible management of liquidity and short-term interest rates based on short-term deposit certificates issued by the National Bank and traded only among banks was implemented in August replacing the existing tranche division of banks' borrowing facilities with the National Bank.

A lower share of public expenditure in gross domestic product would help alleviate monetary constraints and stimulate the growth potential of the economy. The draft budget for 1986 remains in line with the medium term strategy adopted by the government and corresponds to what appears to be an appropriate guideline from the Community point of view. The level of expenditure will stabilize at the ceiling fixed for 1985, whereby it declines as percentage of GDP, whereas taxation should grow more or less in proportion to nominal GDP. The outcome will therefore be a further reduction in the central government deficit to some 3 % of GDP and 1 % for general government. The relative cutback in total expenditure, in terms of GDP, necessitates a continuous reappraisal of existing schemes with a view to reallocating resources on a priority basis among various expenditure categories. It is of particular importance to favour public investment and expenditure which fosters economic development. Total taxation will remain approximately unchanged in relative terms as the cut in indirect labour costs is financed by a rise in corporate taxes, which, due to improved competitiveness, should leave profitability unaffected. In addition, a reform of income tax is planned for 1987. Its aim is to discourage tax-induced dis-economies as marginal rates are reduced and the fiscal disincentives to save are diminished. In budgetary terms the envisaged changes in taxation should balance, but they may very well have an expansionary impact on domestic demand. It will be necessary not to lose sight of such likely effects.

Table 12

Denmark: main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current transactions account	General government net lending or borrowing	Money supply M2[2]	Unemployment in labour force[3]	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	11,2	4,5	6,4	5,8	10,6	−2,2	1,3	10,2	1,1	1,1
1971-80	12,2	2,3	9,6	10,1	11,5	−2,9	0,9	11,3	3,8	0,7
1981	9,1	−0,9	10,1	12,0	9,2	−3,0	−6,9	9,6	9,2	−1,3
1982	14,6	3,0	11,3	11,0	11,5	−4,1	−9,3	11,8	9,8	0,3
1983	10,3	2,0	8,1	7,1	6,4	−2,2	−7,4	25,5	10,4	0,5
1984	9,9	3,9	5,8	6,6	4,9	−3,2	−4,6	17,0	10,0	2,2
1985[1]	6,4	2,3	3,9	4,2	3,7	−3,4	−2,9	11,0	9,1	2,0
1986[1]	5,4	3,2	2,2	1,7	2,4	−2,7	−0,7	7,5	8,6	1,6

[1] Forecast of the Commission services, October 1985, on the basis of present policies.
[2] End of the year.
[3] National concept.

Federal Republic of Germany

Economic conditions in the *Federal Republic of Germany* have improved significantly during 1985: economic growth strengthened through the year, the rise in consumer prices slowed further and employment rose more strongly than was generally expected. There was another considerable reduction in the financial deficit of the territorial authorities while the surplus on the current account of the balance of payments, however, has reached a new record level.

The rate of growth of gross domestic product in 1985 is likely to be only 2¼ %, remaining therefore slightly below the rate of growth forecast by the government in its latest annual economic report (2½ %). This must be seen, however, in the light of the fall in output in the first quarter, mainly due to the effect of extremely harsh weather conditions on construction activity. From the second quarter onwards, real GDP has risen appreciably. External demand has continued to provide expansionary pressure but domestic demand, especially for capital goods, has increasingly contributed to growth. The expansion in the economy has been reflected in the labour market. According to the latest employment data, which incorporate substantial upward revisions, aggregate employment rose in the year to mid-1985 by about 155 000. The reductions in working time contributed somewhat to this rise. The increase in employment in industry and services has thus more than compensated for redundancies in the construction sector. Unemployment, however, rose over the same period by 55 000, reflecting demographic factors and, above all, a renewed rise in participation rates; the unemployment rate in 1985 is thus at the same high level as in 1984 (8,4 %).

The slowdown in inflation was due to competition and, to a considerable extent, to a favourable development of unit labour costs; the moderate increase more than offset the inflationary pressure resulting from higher import prices in the opening months of the year. The rise in consumer prices in 1985 (annual average) is expected to measure some 2 %, compared to 2,5 % in 1984.

The surplus on the current account of the balance of payments in 1985 is estimated at 2,1 % of GDP, more than twice as high as in 1984, reflecting a much higher trade surplus and a broadly unchanged deficit on services and transfers.

In 1986 the momentum of economic expansion should continue and real GDP growth is expected to reach 3½ %. This year-on-year growth rate — relatively high by European standards — is, however, strongly influenced by the expected rapid recovery in activity during the second half of 1985. Indeed, GDP growth between the fourth quarters of 1985 and 1986 is not expected to be more than 2½ %.

Growth in 1986 will result mainly from the increase in domestic demand, where private consumption will play an essential role. Real disposable income is expected to rise appreciably in 1986 in view of a further reduction in inflation due principally to falling DM import prices. Moreover, the introduction on 1 January 1986 of the first stage of the tax cuts, which should benefit families with children in particular, will contribute substantially to improving the financial position of households. Finally, disposable income is expected to be boosted by a rise in employment in 1986, estimated at 330 000 persons, compared with the average for 1985. Nevertheless, the unemployment rate will fall only slightly, from 8,4 % to 8,0 %.

Investment in equipment in 1986 is likely to lose only a little of its momentum (growing by almost 9 %, as compared to 11 % in 1985). After the downturn in housing in 1985, investment in construction should again show a slight real increase in 1986. Total fixed investment is thus expected to rise by almost 5 %, following a decline by more than 1 % in 1985.

The growth of exports is expected to slow down in 1986. On account of the present favourable competitive position, in terms of prices and technology, the volume of German exports is nevertheless expected to continue rising somewhat faster than the increase in world trade. Imports, however, are likely to rise much more strongly. The faster economic growth rate expected in the Federal Republic indicates that there is a widening difference in the relative cyclical position as compared to other Member States, and to the USA. Experience from earlier cycles suggests that, with a relatively short lag, this will lead to a strong upturn in German imports. The Federal Republic would thus also provide an appreciable contribution to growth in other countries. Nevertheless, the current account surplus will remain almost unchanged, at around 2 % of GDP.

During the last three years, considerable progress has been made in the consolidation of the public finances. The deficit of the territorial authorities, which amounted to about DM 60 000 million in 1982 (on national accounts definitions), will probably be less than half that figure in 1985. It is true that, initially, consolidation had a negative impact on demand; expectations were stabilized, however, and the positive effects of the strategy have subsequently come to the fore. Restraint on public expenditure and borrowing has opened up wider scope for reducing taxes and interest rates than would otherwise have been the case. This room for manoeuvre should now be used. The introduction in 1986

of the first stage of the tax reductions, corresponding to about 0,5 % of GDP, is thus to be welcomed. Despite these tax cuts, the increase in tax revenue in 1986 is expected to be only marginally slower than in 1985. Total revenue of general government will grow even somewhat faster than in 1985 because of a significant rise in social security contributions resulting mainly from the increase in employment. The government deficit is thus falling more quickly than was earlier expected. In the Commission's current forecast the budget deficit is estimated to narrow, despite the tax reform, from 1,2 % of GDP in 1985 to 0,8 % in 1986. In the absence of additional expenditure, the outturn for the central government (federation and *Länder*) deficit in 1986 is likely to be several thousand million marks below the level of some DM 40 000 million considered to be appropriate by the Commission.

The stronger growth and rising employment are opening up room for manoeuvre at the level of general government which in 1986 should be used essentially to raise public investment. The improved depreciation provisions for industrial buildings already decided upon by the government represents an initial step in this direction. In addition, the urban renewal programme, for which federal assistance has already been increased from DM 300 million to DM 1 000 million in both 1986 and 1987, might be further extended. *Länder* and local authorities should also increase their financial contributions to this programme. There is evidence that there are a large number of worthwhile projects in the field of environmental improvement and urban renewal on which decisions could now be taken. As such funds are provided in the form of partial grants, their overall effect is considerably greater. There is also scope for graduating the grants from the point of view of structural and regional policy (e.g. according to regional unemployment rates) so as to achieve greater employment effects in problem areas. A further increase in ERP funds in order to encourage investment in environmental protection (e.g. sewage works) also seems advisable in 1987. These specific measures to create employment and to support the building industry seem appropriate in a wider macroeconomic context, since they would help to meet needs which have been neglected in recent years, but which are important both for the present and for the future. Because of existing spare capacity in the building industry, there is no danger that such measures would impede the process of structural adjustment in this industry. A restructuring of resources away from the declining sector of new house-building into the direction indicated above therefore also appears justified from a medium-term viewpoint.

In addition, already in 1986, supply conditions should be improved through specific changes in the tax system. This should also cover taxes which, while contributing insignificantly to total government revenue, restrict the efficiency of the capital market, such as taxes relating to share transactions and issues (*Börsenumsatzsteuer* and *Gesellschaftssteuer* — together contributing barely 0,5 % of the federation's total tax revenue). The Commission has already submitted proposals in this respect.

The increasing room for manoeuvre also permits the second stage of the tax reform to be brought forward from 1988 to 1987, without endangering the consolidation process. It appears necessary to relax taxation sooner than originally planned in order to sustain growth and provide the basis for a significant decline in unemployment in the medium term.

Supply conditions could furthermore be improved, and the fiscal room for manoeuvre could simultaneously be widened, if selected subsidies were to be reduced more quickly and fairly. A start on reducing certain forms of savings promotion could be made already in 1986, since this measure no longer appears necessary.

Finally, the major programme of tax reform planned for the next legislative period should be presented in outline in 1986 with a view to a binding decision on its implementation in 1989. This would also help to underpin expectations of enterprises and consumers.

The development of the public finances is an impressive example of a positive chain reaction resulting from more growth and employment. The interlocking effects of faster growth and greater room for manoeuvre for financial policy provide the basis for a virtuous circle which will eventually bring the economy on to a steady growth path with rising employment.

Over the last three years monetary policy has managed to achieve a marked reduction in the inflation rate and — what is equally important — in inflationary expectations. The confidence which this has created in the German mark has made it possible to decouple interest rates to a considerable extent from US levels. Since the spring of 1985, the room for manoeuvre in monetary policy has grown even further, since the dollar has been falling since then, albeit irregularly. Monetary policy should continue to exploit fully the developing potential for interest rate reductions in the framework of the price stability objective. To the extent that growth potential rises as a result of higher investment and more flexible use of the capital stock, additional scope will develop for monetary growth which is still consistent with price stability.

The dynamic recovery in investment must continue. As the capital stock in many areas is obsolete, gross fixed invest-

ment must expand appreciably in real terms for a number of years in order to permit both adequate modernization and the extension of the capital stock necessary to generate additional jobs. The growing need for capital-widening investment is demonstrated by the high level of capacity utilization recorded in mid-1985; the level of utilization in industry was only one percentage point lower than at the previous cyclical peak at the beginning of 1980.

In recent years wage moderation has made a considerable contribution to the recovery of companies' financial situation. While the profit share in value-added has again reached the level of the early 1970s, the yield on physical capital in many areas is, however, still too low. This underlines the need to use the capital stock more efficiently and in such a way as to generate more employment.

Now that productivity is again rising more strongly, real wage increases are clearly possible in 1986. The increase in real per capita incomes should however continue to lie below overall productivity growth. Thanks to the first stage of the tax reform and to the further success in combating inflation (achieved mainly through a fall in import prices in 1985), there will be a further appreciable improvement in real incomes despite a moderate wage round. Given the economic situation in 1986, a rise in real per capita income is not only possible but within limits also desirable, since private consumption should compensate for the slow growth of exports in order to support the overall level of activity, as long as it does not impede investment growth.

In negotiations between employers and unions in 1986 it might be considered whether, as a direct counterpart to continued moderation of wage settlements, additional jobs could be created. This form of arrangement could signal an increase in employment.

More employment-creating growth could also be promoted if working hours were made more flexible than is currently the case in most firms. This would also facilitate reductions in working hours. The experience gained so far in the metal and printing industries, where employers and unions last year agreed on a cut in working time combined with more flexible arrangement of the hours worked, is certainly encouraging. A recent survey carried out on behalf of the Commission among a representative cross-section of European employees has shown that there is a high degree of readiness in the Federal Republic of Germany (and in most other member countries) to accept new working time arrangements. For example, a third of the employees surveyed favour working irregular and, in some cases, inconvenient hours (e.g. in the evening until 22.00 and once a month on a Saturday) if this is matched by a reduction of some 5 % in annual working hours. Furthermore, approximately one in every six of those currently employed on a full-time basis would welcome a working week reduced to some 30 hours on the same hourly wage. These preferences regarding working hours can generally be reconciled with business reality only if the whole pattern of working is made more flexible. Only in this way could shorter working hours for the individual be consistent with the current length, or even an extension, of operating hours, while at the same time creating additional employment opportunities. The new legislation governing limited-period contracts and part-time working should be used more actively by employers and workers so that the evident large potential for flexibility among workers can be better exploited for the benefit of both sides. In the services sector in particular, a considerable increase in employment might be achieved if more flexible working hours were accompanied by changes in operating hours. Such measures are no less appropriate for the fact that more attractive working hours have the effect of bringing persons from outside the labour force onto the labour market and that the number of registered unemployed falls less sharply as a result.

A particularly important task in the next few years is to further improve the vocational training opportunities for school-leavers and to guarantee them employment after their training, even if this initially has to be in some form of part-time working. One way of doing this is to make early retirement more attractive financially — at least for a limited period up to 1988 — in order to boost the numbers opting for early retirement during the next few years, which will still see an appreciable increase in the potential labour force.

The economic outlook for 1986 is generally favourable. Nevertheless, there are still two appreciable imbalances, the current account surplus and, above all, unemployment. The regained room for manoeuvre for financial policy should be fully used, not only to counteract in time a possible cyclical weakening of the economy in 1987, but also to maintain the momentum of the positive chain reaction between growth, employment and the room for manoeuvre. A medium-term growth rate similar to that expected for 1986 and an increase in employment of about 1½% per year are preconditions for a significant reduction in unemployment. Because of the resulting higher import requirement, the Federal Republic would also help to ease the employment problem in its partner countries.

Table 13

FR of Germany: main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current balance	General government net lending or borrowing	Money supply M3[3]	Unemployment in labour force	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	**8,4**	4,5	3,7	2,7	8,5	0,7	0,4	10,4	0,8	0,2
1971-80	**8,2**	2,7	5,3	5,1	8,5	0,6	2,0	9,8	2,7	−0,1
1981	**4,2**	0,2	4,0	6,2	5,2	−1,0	−3,7	5,0	4,7	−0,7
1982	**3,7**	−0,6	4,4	4,8	4,2	0,5	−3,3	7,1	6,8	−1,7
1983	**4,6**	1,2	3,3	3,2	3,9	0,7	−2,5	5,3	8,4	−1,5
1984	**4,5**	2,6	1,9	2,5	3,2	1,0	−1,9	4,7	8,4	0,0
1985[1]	**4,4**	2,3	2,1	2,1	3,2	2,1	−1,2	5,0	8,4	0,6
1986[2]	5,4	3,5	1,9	1,5	3,8	2,0	−0,8	4,8	8,0	1,3

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] End of the year.

Greece

In *Greece* domestic demand in 1985 has continued to be sustained by the still vigorous expansion of public expenditure and by a further increase in the number of tourists. However, the contribution of the real foreign trade balance has deteriorated sharply due to the combined effects of a marked slowdown in the rate of growth of exports (exceptionally high in 1984) and an appreciable upturn in imports. The growth rate for 1985 is thus likely to fall to around 2 %. Moreover, major disequilibria have continued to affect the economy. The rise in consumer prices has slowed down only temporarily and, on a year-on-year basis, could climb to over 19 % again. Business investment has continued at a very low level, showing no tendency to recover. Lastly, the sharp increase in the tourism surplus has not been sufficient to offset the deterioration in other current account items; the deficit on current account (on Bank of Greece definitions) could be as much as 8,5 % of gross domestic product.

Faced by these developments, which represented a lasting change in the competitiveness of the economy, the authorities decided on 11 October 1985 to devalue the drachma by 15 % and to introduce a compulsory deposit on a large proportion of imports. At the same time a series of complementary measures was announced, which demonstrates a will to get the economy onto the adjustment path necessary for the recovery of growth on a sounder basis. The fact that external indebtedness was continuing to increase rapidly, whereas the share of business investment in domestic demand was declining steadily, was, among other factors, particularly disturbing. The economy was in effect tending to become trapped in a vicious circle, so that it was liable to become increasingly difficult to restore external equilibrium as a result of inadequate investment to increase production capacity and to improve competitiveness. The priority aim of economic policy had therefore to be to break this circle as soon as possible. This means not only gradually adjusting domestic demand as a whole to the external constraint, but also increasing as rapidly as possible the share of productive investment in domestic demand, in order to bring it to the level required to ensure growth in the future.

The precondition for attaining these results was to bring about as quickly as possible a disinflation of the economy. The lasting re-establishment of competitiveness depends on this, and so does the return to normal of investment and savings behaviour. Fulfilling this objective implied major efforts — on which the authorities have now decided as shown by the measures announced — to curb spiralling costs and the public deficit, the two essential factors which perpetuate inflation.

The first step was to seek to obtain a substantial moderation in the nominal increase in earnings, as compared with the rate of 20 % or so still evident in 1985. This aim was not compatible with the continuation of the old system of indexation, which had the disadvantages not only of feeding automatically into costs, whether directly or indirectly, a large proportion of earlier price rises and of thus permitting only very slow disinflation, but also of making wage adjustment too independent of changes in productivity in the various sectors of the economy. It has been decided to make a fundamental change to this system, by linking wage increases from now on to the targetted, rather than the observed, rate of inflation, excluding the impact of import price rises. It has also been decided to freeze incomes above a certain level for a period of four months. These decisions should make possible a faster deceleration of prices, as well as a start in the process of improving the substantially deteriorated financial position of enterprises. The reduction in inflation and the recovery of business profitability aimed for by these measures are an essential condition for the re-establishment of balanced growth.

A start should also be made on reducing the public deficit, which, partly because of the insufficient yield from the tax system, will in 1985 again have overshot the very high level of previous years. The effort to be made should help, in 1986, to reduce public sector net borrowing by 4 % of GDP and to bring the central government budget deficit down to 9-10 % of GDP. Given the momentum of interest charges — which will however be held back by the decline in inflation — and the need to maintain adequate investment in the public sector, these aims imply very rigorous management of administrative expenditure, including wages, and a considerable reduction in the burden of subsidies. This reduction, among other things, will require an appropriate adjustment of public utility charges and other administered prices, which have been kept at artificially low levels relative to the rise in the general price level. To this end, an initial series of measures has already been taken. It will be no less necessary, as foreseen in the Government programme, to increase the pressure of taxation not only, by means of the steps taken to intensify the fight against evasion, but also by deliberate tax increases, which appear unavoidable.

This two-pronged effort to reduce inflation should considerably reduce the pace at which the demand for credit increases; yet, monetary policy will still have to exercise restrictive action, confirming the current trend for positive real interest rates, with a view to encouraging the development of a stable pattern of saving and, in particular, to extend the public placement of government securities which was started in 1985.

These measures should make it possible to point the economy more resolutely in the direction of sounder management which is essential for its subsequent recovery. It will nevertheless be necessary to supplement them by new measures designed to hasten the recovery of business investment. *Inter alia*, prices policy will have to contribute by becoming more flexible, provided that there is no danger of vigilance being relaxed with regard to dominant positions.

As early as 1986, the policy described above could begin to bear fruit. Domestic demand should slow down to the advantage of the external account but, on balance, it will not be possible to avoid an appreciable check on in growth. Private investment should also pick up; this is likely to be reflected in a gradual climb in the share of investment in domestic demand. The year-on-year increase in consumer prices could be around 21 %, which would mean a rate through the year much lower than this figure. Lastly, given favourable prospects for the international environment, the balance of payments on current account, expressed as a percentage of gross domestic product, should show a marked recovery. These results however are merely a first step towards the necessary adjustments. They will imply the maintenance of a policy of consolidation for several years, which should contribute after an unavoidable phase of slower growth to more rapid expansion.

This outlook does not hold out any hope of a rapid improvement in the employment situation. Long-term recovery on this front will depend on the gradual strengthening of the upturn in investment, the primary condition for which is the maintenance of the policy of consolidation.

Table 14

Greece: main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current transactions account	General government net lending or borrowng	Money supply M2[3]	Unemployment in labour force	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	**11,0**	7,6	3,1	2,5	9,8	−3,1	:	17,6	:	−0,7
1971-80	**19,1**	4,7	13,8	13,6	18,3	−2,7	:	23,8	:	0,6
1981	**18,9**	−0,3	19,3	23,4	21,8	−0,2	−11,1	34,3	4,1	4,8
1982	**24,4**	−0,1	24,6	20,5	26,8	−3,9	−8,5	29,1	5,8	−1,0
1983	**20,2**	0,3	19,8	19,5	19,7	−4,7	−8,9	20,3	7,9	−1,0
1984	**23,0**	2,6	19,9	18,1	21,3	−4,0	−9,9	29,4	8,1	−0,2
1985[1]	**20,9**	1,7	18,9	19,1	20,0	−6,6	−13,4	27,0	8,3	0,8
1986[2]	18,1	0,1	18,0	21,5	13,8	−4,5	−11,0	20,0	9,3	−0,1

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] End of the year. Up to 1980: M2.

France

In *France*, domestic demand has been kept under strict control in 1985; even though it has accelerated slightly during the year, it will have grown nearly as slowly as in 1984. Private consumption has been slightly more buoyant overall, while there has been evidence of a vigorous upturn in industrial investment, which after several years of uninterrupted decline, has been sufficient to bring about a positive, though tiny, change in aggregate investment. Export growth remains buoyant, though distinctly slower than in 1984 because of the less strong expansion of world trade, while imports remain on a very moderate upward trend. This has produced a further slight improvement in the real foreign trade balance and gross domestic product growth in the region of 1 %, despite a zero, or even slightly negative, contribution from agricultural production. The trade deficit is likely to narrow further helped by the weakness of energy and imported raw material prices and the reversal of the upward trend of the dollar from the second quarter on. The current account should thus be roughly in balance, despite the smaller surplus on invisible transactions. Lastly, the rise in consumer prices has started to slow again after an interruption in the early part of the year, and the annual average should be under 6 %.

Thanks to the pursuit since 1983 of efforts to achieve sounder economic management, the economy has made further progress in returning to balance. This progress, however, still needs to be consolidated. It is indeed necessary to go further than simply eliminating the inflation differential between France and the average of her trading partners, which is about to be achieved, and to obtain a lasting significant current account surplus which allow the gradual reduction of external indebtedness. Moreover, in the case of manufactures, the rapid rise in import penetration and the renewed contraction in export market shares, after the improvement of 1983-84, are indeed clear signs that the economy's competitive position is still weak. Restraint must therefore continue to be the watchword of economic policy. It is also the prerequisite for a return to the more sustained growth rate which is the aim of the Community strategy, since the effort now being made to improve the health of the economy is also directed towards the lasting improvement of its competitiveness by stimulating the recovery of investment through a return to profitability. This is a long-term strategy, in which economic policy has been involved since 1983. It implies not only appropriate wage developments, but also sometimes major adjustments in manning levels. Nevertheless, as the rate of capital formation gradually becomes more sustained again, the time is probably approaching when a reversal of the downward trend of employment will begin. The strategy has in any case already brought some results in that a significant recovery in the trend of investment has occurred right in the crucial area of competitive industry. Under the strategy, any stimulation of private consumer demand is of course out of the question so long as production capacity has not been reinforced to the point of being able to cope with this acceleration without damaging the balance of payments. Caution is all the more essential here because the upturn in industrial investment is liable to boost import penetration, at least temporarily.

Persistence with a pay policy based both on economic stability and on employment creation is therefore the first requirement of the continued emphasis on restraint. This means that the increase in per capita earnings must still not exceed the target inflation rate by the end of the year, and must therefore be well below 1 % a quarter. Based on the experience of the last two years, this norm will probably be respected in both the public and private sectors. Such moderation seems all the more reasonable because price rises will have decelerated sharply by the time the 1986 pay round opens at the end of 1985. As the pressure of costs, and with it inflationary expectations, gradually slackens, it should also be possible to contemplate further relaxation of the prices code, but without jeopardizing the objective of reducing inflation. Relaxation could go at least as far as the complete de-control of industrial prices, which are sufficiently constrained by external competition for them to be in no danger of moving out of line.

Public finance will have to be kept within the strict framework laid down in 1983 in order to avoid excess pressure from the deficit on the financial markets. As provided in the draft budget for 1986, adopted on 18 September 1985, the net balance to be financed in the central government budget and the general government net borrowing must still be kept very close to 3 % of gross domestic product. The danger is, however, that there will be some difficulty in combining this constraint of keeping borrowing stable with the reduction, however limited, in the level of tax and social security deductions implied by the newly announced cuts in personal income tax. There is an essential need for balance in the social security system, in which certain schemes, particularly for retirement and unemployment insurance, are affected by the progressive change in the ratio of beneficiaries to contributors. It is therefore not certain that social security contributions will not have to be increased sooner or later to prevent these schemes from again moving into deficit. In any event, extremely tight control of expenditure must be continued at all levels in order to keep the volume increase of total expenditure slightly below the real growth rate, even though interest charges and the cost of social transfer payments are bound to increase much more sharply. Consequently, the management of central government spending

must leave no room for a real increase in expenditure exclusive of debt interest. This means that the growth margin required in order to press ahead with the priority measures in the fields of security, employment, training and research must be obtained by diminishing the real burden of the other spending areas. It also means that overall public service manning levels should stop rising and that, taking all the components of increases together, pay rises cannot accommodate any improvement in purchasing power.

Lastly, if the rise in earnings and the public sector deficit are kept within the projected limits, monetary policy can continue to reinforce the reduction of inflation in the economy by lowering interest rates as progress is achieved and by aiming at an increase in the money supply M2 in 1986 below that of 1985.

In these circumstances, domestic demand might well be able to grow slightly more, pushing the growth of gross domestic product above 1,5 %, despite the expected smaller contribution of the real foreign balance resulting from the probable acceleration of imports. The terms of trade should, however, move favourably, so that the trade balance is likely to return to equilibrium and the current account should remain roughly in balance. At the same time, consumer price increases are again likely to slow down, helped by the weakening of the dollar exchange rate, and should average slightly over 4 % for the year.

The inevitable counterpart of this effort to achieve sounder economic management is the temporary persistence of a downward trend in employment and of an accompanying slight increase in unemployment. This problem could, however, start to ease in 1986 with the completion of the principal industrial restructuring operations, the progress achieved in real wage adjustment, the upturn in investment and the simultaneous slowdown in the increase in the labour force. In fact, the rate of increase in unemployment has already fallen significantly in 1985, for reasons due partly, it is true, to the success encountered by the part-time work programme mounted by the local authorities and other public agencies, as part of the public authority drive to promote employment, notably among young people. The introduction of community work schemes marks the last stage in this drive and might also be the starting point for a more general trend towards the easing of conditions for integrating the young into working life. More generally still, employment as a whole should benefit from the new initiatives agreed in the area of training as well as from certain proposed changes in labour legislation and working hours.

Economic policy must continue to give priority to restoring the conditions making for balanced growth, and endeavour to mitigate, by specific measures, the temporarily adverse consequences for employment of this necessary approach; in so doing it will best be able to fulfil the objectives of the cooperative strategy for growth devised for the Community as a whole. If the international environment continues to develop favourably domestic demand should again be given a larger margin for growth from 1987 on. Nevertheless the bulk of this margin should be utilized by corporate investment, which still has much ground to make up.

Table 15

France: main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current transactions account	General government net lending or borrowing	Money supply M2[3]	Unemployment in labour force[4]	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	10,2	5,6	4,4	4,3	9,4	0,2	0,4	12,7	0,9	0,6
1971-80	13,4	3,6	9,5	9,5	13,8	−0,4	−0,1	14,8	3,8	0,4
1981	12,1	0,2	11,9	12,9	14,5	−1,4	−1,8	11,4	7,8	−0,7
1982	14,8	1,8	12,8	10,9	14,5	−2,9	−2,7	10,8	8,7 (8,8)	−0,8
1983	10,9	1,0	9,8	9,4	10,9	−1,7	−3,1	11,2	8,8 (9,0)	−0,6
1984	8,7	1,6	7,0	7,3	8,1	−0,7	−2,8	8,3	9,9 (9,9)	−1,0
1985[1]	7,0	1,2	5,7	5,8	5,9	−0,5	−3,2	5,8	10,7 (10,7)	−1,0
1986[2]	5,8	1,9	3,9	4,0	4,5	−0,3	−3,3	4,9	11,0 (10,9)	−0,7

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] End of the year. Up to 1980: M2.
[4] Eurostat definition in parentheses.

Ireland

In *Ireland* the pattern of vivid contrasts, which has characterized macroeconomic performance since recovery began in 1983, remained marked in 1985. Exports continued to expand vigorously despite slower growth in external markets; domestic demand, on the other hand, remained at a low level, reflecting factors whose cumulative influence is likely to dampen aggregate activity for some time to come — in particular, a still relatively modest amount of domestic sourcing for important export categories, the implications of further fiscal adjustment, and the impact on global investment as work on major projects in the public sector comes to an end, offsetting the strong resurgence in private investment in capital goods. The benefits of rapid export expansion are also weakened by the high level of net factor income outflows, 11 % of GDP in 1985, mainly attributable to interest charges on the external public debt and profit repatriations by Irish branches of foreign-owned firms. As a consequence, growth in real GNP, the appropriate measure of the resources actually available to the economy, is a full percentage point below the comparative GDP figure, estimated at about 2½%. Against this background, unemployment continued to rise during the year to the unprecedented rate of 17 %. In other respects however, adjustment has proceeded much faster. A significant degree of wage moderation has been achieved. The rate of inflation (CPI), as high as 20 % in 1981, is expected to come down to almost 5 % in 1985. The deficit on the current account of the balance of payments as a percentage of GDP has also been reduced dramatically by an estimated 11 percentage points in the same period. Indeed, the trade balance has moved into modest surplus for the first time in many years. The small overrun expected on the planned budgetary target of 11½% of GDP for the Exchequer Borrowing Requirement (EBR) should be seen in the light of the approximately equivalent saving recorded in the previous year. However, fiscal adjustment has effectively marked time for the past two years so that the size of the national debt continues to grow by further substantial annual increments and may indeed approach 120 % of GDP by end-year of which close to half will be owed abroad. Moreover, the deficit on the current balance of payments is still rather high in view of the relatively low level of domestic demand.

Growth prospects for 1986, with real GDP expected to rise by nearly 2½% on the assumption that progress in fiscal adjustment will resume as provided for in the government's medium-term economic plan 'Building on Reality', are similar to those in the current year although the balance of growth should shift somewhat towards stronger domestic demand. Nonetheless, some further reduction is likely in the deficit on the current balance of payments while the underlying rate of inflation should continue to improve. Employment is likely to grow at a modest pace but unemployment will probably remain at around 17 % during the year.

The considerable success achieved by the authorities in some areas of the economy throws into sharper focus the relatively slow progress being made in improving labour market conditions. In Ireland, particular demographic influences have been superimposed on more commonly experienced cyclical and structural factors. The labour supply is likely to increase by about 1 % per annum in the next few years even allowing for significant net emigration. The problem therefore, if any inroad into the level of unemployment is to be made, is to raise employment by a much faster rate each year. To this effect, the authorities should endeavour to make simultaneous progress in three areas, namely, restoring order to the public finances, improving labour market management and making industrial policy more effective in terms of retaining more value-added in the economy and generating more employment.

The persistence of high public deficits entailed not only a rapid accumulation of external debt (almost 50 % of GDP at end-1984) and resultant interest charges (1981, 2 % of GDP; 1985, 4½%) but also, bearing in mind the relatively narrow tax base, exceptionally high levels of personal taxation. Over 40 % of income tax payers fall into the two higher tax bands (48 % and 60 %). 'Building on Reality' proposes to reduce the EBR and current budget deficit (CBD) to 9,8 % and 5 % of GNP respectively by 1987 (that is, a reduction of over 3 percentage points in each relative to 1985) while holding taxation constant as a percentage of GNP, at the 1984 level. Substantial imbalances will thus persist in the period after 1987.

These targets must be regarded as a minimum. Consequently, in 1986 the authorities should reduce the EBR and CBD by at least 1,5 percentage points of GDP respectively, by reference to the probable outturn for 1985, constituting a half-way step towards 1987. While the expected moderation of international interest rates and the dollar exchange rate will ease the debt interest burden somewhat in 1986, this order of reduction in the deficits will be feasible only if there is severe restraint on non-interest expenditure including the maintenance of strict limits on the rise in public service pay and the second and final phase of the abolition of consumer subsidies. It would be appropriate to continue the reform of the tax system initiated in the January 1985 budget with a view to promoting incentive and enterprise. While more emphasis on reducing the income tax burden would appear desirable, progress in this direction must depend on how far expenditure can be reduced. Resources

could be freed by restructuring the system of transfers to households so as to reflect priorities and direct expenditure to areas of real need. It is questionable, in the context of overall budgetary targets, whether the real value of social transfers can be maintained — these have risen by as much as 4 percentage points since 1981 to an estimated 19 % of GNP in 1985.

Monetary policy will have to mitigate the strains arising from the pressures exerted by large public deficits. The improvement in the external current account deficit is reducing the role played by external financing of the public sector. Despite subdued demand for private sector credit, which has facilitated the recent reduction in the role of quantitative credit controls, the continuance of Exchequer external borrowing at the high level of 1985 could contribute to excessively fast growth in the money supply. In regard to interest rate policy, the authorities must strike a balance between ensuring that the economy benefits proportionately from the easing in international rates and maintaining a strong flow of savings from the non-bank public to the Exchequer. Avoidance of short-run volatility in domestic interest rates is obviously essential.

The prospect of high levels of unemployment over the medium term has been the main stimulus behind initiatives taken by the authorities in labour market management. Training schemes, particularly for young people, are now being greatly expanded. A social employment scheme has been introduced, offering 10 000 longer-term unemployed part-time work for one year mainly on local authority projects. The scope for this type of scheme is limited however, both by the cost, and by the rather slow take-up of job opportunities linked partly to limited trade union acceptance. However, the Enterprise Allowance Scheme, designed to help unemployed persons start their own business, has been much more successful in terms of demand for the scheme combined with a relatively low degree of initial failure. The Employment Incentive Scheme, which subsidizes incremental employment, is also attracting growing demand, but to evaluate its success is more difficult because some employers may have hired more labour anyway. Overall, there is now need for greater coordination in administering manpower policy, given the recent rapid expansion of schemes and the number of bodies involved.

An important development to date in promoting labour market adaptability has been the increasing dispersion, in terms of timing and size, of wage settlements. In regard to the replacement ratio (level of unemployment benefit relative to net income after tax), a more emphatic stress on reducing personal taxation, particularly for those on lower incomes, could encourage a greater take-up of less well paid job opportunities especially since there is little scope for increasing the value of social transfers. The correction of the longer-term trend towards excessive capital deepening is more problematic but there is evidence that generous levels of investment incentives, which have attracted many capital intensive production operations, have had an important effect. Since Ireland is likely to require foreign inward investment for some time to come, it may be difficult to reduce the level of these incentives, but, in line with the White Paper on industrial policy, they can be used more selectively to ensure the creation of more jobs. At present, it makes sense to put a strong emphasis in industrial policy on improving supply linkages between the foreign and domestic sectors in manufacturing. Ultimately however, the best prospects for a wider basis of output and employment growth in manufacturing lie with the recovery and expansion of domestic firms; this will not come about in the absence of sustained wage moderation, to generate profits and investment and protect competitiveness, and of an appropriate business climate in terms of taxation and interest rate levels. Wage moderation, in combination with budgetary restraint, is not only imperative solely from the point of view of Ireland, but would be in harmony with a consistent, more employment intensive, growth strategy in the Community as a whole.

Table 16

Ireland: main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current balance	General government net lending or borrowing	Money supply M3[3]	Unemployment in labour force	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	**9,9**	4,2	5,5	4,6	9,9	−2,3	−2,7	10,4	4,5	0,0
1971-80	**19,5**	4,6	14,2	13,8	18,0	−4,6	−8,1	18,5	7,4	1,0
1981	**21,2**	2,6	18,2	21,2	19,6	−14,1	−13,2	21,5	10,6	−0,9
1982	**16,9**	0,0	15,9	15,9	15,7	−9,9	−13,8	13,5	12,8	0,2
1983	**10,4**	0,8	10,4	8,3	9,3	−6,3	−11,8	5,6	14,6	−2,0
1984	**11,3**	4,4	6,6	8,5	9,6	−5,1	−10,1	10,1	16,1	−0,9
1985[1]	**8,7**	2,5	6,1	5,7	7,0	−3,3	−11,5	6,6	17,1	−0,3
1986[2]	7,5	2,3	5,0	5,3	5,7	−2,0	−10,4	9,8	17,4	0,6

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] End of the year.

Italy

In *Italy*, the absence of arrangements for containing the in-built momentum of earnings, the insufficient control of the public deficit and the consequent accelerated growth in the monetary aggregates in the early part of the year have provided a further boost to private consumer demand in 1985 while business demand, still stimulated by the favourable trend of profits in 1984, has remained very buoyant. This momentum, coupled with worsening competitiveness, has tended to pull in appreciably more imports and to curb the rise in exports, which has nevertheless remained strong. Despite the strongly negative influence of the real balance of foreign trade, the growth of gross domestic product will, however, be similar to that in 1984. But the pressure of demand on domestic supply and the rise in the dollar in the first half of the year temporarily interrupted the slowdown in the inflation rate, which should settle at about 9% on average in 1985. Above all, no favourable factor reduced the impact on the current account of the deterioration in the real external balance: the current account deficit for the year is therefore likely to reach 1,7 % of GDP. Following two successive slides in the exchange rate of the lira, in February-March, and again in July, the new downward adjustment of its central rate within the European Monetary System on 20 July was the consequence of these major imbalances.

However, the tendency for the balance of payments to deteriorate will not be lastingly reversed as a result of Italy's improved competitiveness *vis-à-vis* the countries of the European Monetary System, and the simultaneous improvement in her terms of trade linked with the decline of both the dollar and the oil price, unless the causes of the present disequilibrium are corrected rapidly. There is even the danger that the persistence of relatively high inflation will wipe out the exchange rate advantage obtained before it can be fully exploited in respect of real flows. Fundamental measures must therefore be taken not only to curb domestic demand to the appropriate extent but also to break the inflationary spiral itself, which tends to perpetuate economic instability and, by so doing, impede the expansion of productive capacity. Over and above the chronic precariousness of external equilibrium, the most serious consequence of this situation has been the decline in the rate of formation of productive capital connected with the fall in its profitability and the resultant severe crowding out of labour in the sectors exposed to competition. It is therefore essential for economic policy to attack the very roots of this problem by calling into question certain automatic institutional procedures which deprive labour costs and public expenditure of the flexibility needed to restore the key equilibria on a lasting basis. Unless there is resolute action along these lines, the monetary authorities will inevitably be faced with contradictory policy options, permitting neither the necessary progress towards re-establishing equilibrium, nor a lasting return of productive investment to a level compatible with a gradual reduction in unemployment.

In this context, the revision of wage adjustment procedures is of key importance: on it depends the control not only of the evolution of costs in the competitive sector but also to a large extent that of public expenditure. Even when it was alleviated down in 1983, the undifferentiated indexation system introduced in 1975 retained most of its disadvantages: it impedes disinflation by automatically feeding into the wage bill much of the impact of any past rise in prices; its effects of squeezing wage differentials is bound to be offset by differentiated pay increases, the addition of which is incompatible with the desirable slowing down of nominal pay rises; and in the end it implies a trend of real wage increases which is higher than that of productivity growth.

Management and unions seem to be working out an agreement to abandon this mechanism, already rejected by private industry employers, with effect from the start of 1986, although there is no question of abandoning all idea of automatically protecting wages against the decline in the value of money. It might thus be possible to move towards a method of wage-fixing which would retain some indexation, but in the diluted form of a half-yearly adjustment of an amount of salary limited to a level far lower than the current rate of coverage, with the other elements of the increase being no longer determined at branch and company level three years at a time, but for shorter periods. This might go a long way towards reducing the rigidities of the former system and should do away with most of its disadvantages. As a result, it should be possible to make much faster progress in reducing inflation and also to remove, by negotiation, the possibility of rises in real wages beyond the increase of productivity. The system might be used to make appropriate corrections to the distortions which occurred in the past.

But the expected results will not be achieved unless the shift in the system of wage formation is matched by an extremely energetic effort to reduce, and not just contain, the enormous inflationary pressure emanating from public finance. Contrary to the initial forecasts, the Treasury deficit shows no sign of falling in 1985. Its underlying trend is even tending to rise from levels which already imply a rapid increase in the burden of indebtedness, already close to 100 % of GNP.The strategy necessary has been outlined in a plan for the reform of public finance to 1990 published by the Minister for the Treasury on 22 May 1985. The twin objectives, justified by the need for the gradual reduction of the public

finance burden on the productive system, are to stabilize overall government receipts as a percentage of GDP as well as the real share of current expenditure, excluding debt interest, at levels very close to their present ones. If these two objectives were achieved, and assuming that growth averages close on 3 % a year until the end of the decade, and that inflation tends rapidly towards an annual rate of 4 %, general government net borrowing, expressed as a proportion of gross domestic product, could be cut from 13,5 % in 1985 to around 7 % in 1990.

The major difficulty of this strategy is the stabilization of the growth in real terms of current expenditure excluding debt interest, especially since much of this expenditure is controlled by decentralized departments. The objective means that the volume of total public service pay must be lastingly stabilized, i.e. that the mechanism for its adjustment — notably indexation and automatic career increases — be amended accordingly, and that the numbers employed in government and public departments should only be increased when strictly necessary. It also means that in order to compensate for the inevitable increase in the real cost of pensions, the costs to the budget of public services must be reduced by an appropriate increase in the user contribution to their operating costs. Lastly it requires the introduction of provisions designed to limit the increase in the burden of pensions as much as possible. The 1986 budget proposal, presented to the parliament on 30 September 1985, includes a collection of fundamental changes which already seem to meet some of these requirements and to move towards the goal of stabilizing real non-interest expenditure, but without being able to achieve this by 1986.

The revenue measures adopted in the budget proposal provide for a reduction in personal income tax, adjusting the tax bands so as to neutralize inflation effects, for the reduction with effect from 1987 of the tax on invested profits, and also a reduction in the taxation of inheritances. They also comprise, on the other hand, substantial increases in social security contributions. In total, revenue as a percentage of GDP should be broadly maintained at its 1985 level, which is unlikely to be sufficient to keep the Treasury deficit for 1986 within the limit set earlier of LIT 110 million million (14,8 % of GDP). This target figure, which shows an improvement of 1 percentage point compared to the probable 1985 outturn, should be considered as a ceiling, taking into account the absolute need to stabilize the relative level of the debt by 1990. It is essential, in these circumstances, to ensure that it is not exceeded, either by making additional cuts in spending or, unless there is a spontaneous rise in tax yields, by appropriate tax increases.

These guidelines with respect to pay and fiscal policy should be coupled with a monetary policy strict enough to stabilize the economy's M2 liquidity ratio by the end of 1986, after its rise in 1985. This measure would produce some slowdown in domestic demand, which should bear more heavily on consumption than on investment. The continuation of the real external balance would become positive again permitting gross domestic product growth for the year of the order of 2,5 %, and the current account could begin to improve helped by the favourable movement of the terms of trade. At the same time, the rise in consumer prices should slow down very sharply to settle at an annual average of around 6,5 %, approaching the Community average by the end of the year.

If pursued with sufficient vigour, the twofold drive to control costs and the public deficit, on which substantially depends the ultimate return to more stable growth, leading to an expansion of productive capacity which would allow employment to increase, is likely to be fully in keeping with a cooperative strategy for growth. In order to fulfil its objectives completely, this drive must nevertheless, and as far as possible, be supplemented by direct and immediate measures to bring down unemployment. Even if the problem is today no longer growing appreciably worse, because the increase in the labour force is tending to slow down, it is sufficiently worrying to require intensification in scale of the specific efforts undertaken to reduce it, be they to increase labour market adaptability, to adjust vocational training and retraining schemes, or to promote directly jobs in the southern regions. As far as budgetary constraints permit, these efforts must also be extended to include measures to stimulate research, technological advance and the redeployment of energy so as to improve production structures and consequently growth and employment prospects in the medium term.

Table 17

Italy: main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current transactions account	General government net lending or borrowing	Money supply M2[3]	Unemployment in labour force[4]	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	10,5	5,7	4,5	3,8	10,7	1,8	−2,3	13,3	5,2	−0,4
1971-80	18,3	3,1	14,7	14,6	18,4	−0,2	−8,0	19,5	6,0	0,5
1981	18,5	0,2	18,3	19,2	21,9	−2,3	−11,7	10,0	8,8	0,5
1982	17,2	−0,5	17,8	17,1	17,3	−1,6	−12,7	18,0	8,7 (10,5)	−0,2
1983	13,6	−1,2	15,0	14,9	16,0	0,2	−12,4	12,3	9,9 (10,8)	0,1
1984	13,6	2,6	10,7	11,1	12,1	−0,9	−13,5	12,1	10,4 (12,0)	0,4
1985[1]	11,0	2,7	8,1	8,6	10,2	−1,7	−13,6	12,1	10,9 (12,6)	0,2
1986[2]	9,5	2,7	6,6	6,5	7,6	−1,1	−12,8	8,5	11,2 (13,1)	0,3

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] End of the year.
[4] Eurostat definition in parentheses.

Luxembourg

In *Luxembourg*, economic activity contracted in 1985, because of the slowdown of steel production after the very sharp increase recorded last year. Nevertheless, because demand for other products remained buoyant, total exports again advanced slightly. Domestic demand improved markedly as a result of the upturn in private consumption and business investment, but investment by the public sector and in housing fell in real terms. Overall, gross domestic product will grow by around 1,7 %. The rise in consumer prices (of 3,2 % on average) weakened perceptibly.

In 1986, the growth of gross domestic product is likely to remain fairly modest and should not go much above 1,5 %. A stabilization of activity in the steel industry is likely to be more than offset by the continuing vigorous advance in the other sectors. The greater dynamism of private consumption and the continuing buoyancy of investment, mainly by companies, is likely to underpin domestic demand so that its growth rate will compare with this year's. The rate of increase of consumer prices is likely to weaken further during the year.

The financial position of steel enterprises has improved at the end of three years of considerable efforts. Consolidation of profitability in this sector is likely to involve further substantial costs for the central government budget in 1986, but this is not likely to hold back efforts to diversify the Luxembourg economy by developing and modernizing existing enterprises and introducing new industries.

Restructuring must take place in an economic climate which favours investment, and this implies adequate corporate profitability. In this context, the wages trend plays a key role. The ending of specific measures to hold down wages in the steel industry, the restoration of indexation and the granting of benefits outside the collective agreements could have an effect in other sectors very sensitive to international competition, reducing the country's attractiveness for new enterprises and impeding industrial diversification, especially since wage moderation will continue in the neighbouring countries. If the efforts made so far in the Grand Duchy were relaxed, the competitive position of companies would suffer. Participation in a cooperative strategy for growth and income moderation would, by contrast, have favourable effects on export prospects.

In comparison with the other Community countries, unemployment has remained relatively limited owing among other things to specific programmes to provide employment for workers in the steel industry. However, imbalances persist in relation to the qualifications of manual workers, and these could be remedied by looking for suitable methods of youth guidance and vocational training. By increasing the attractiveness of various training arrangements in industry and by making working hours more flexible, company requirements could also be better served.

As a result of the spontaneous increase in revenue, combined with a continuing strict hold on central government expenditure, it should be possible to keep the 1986 net budget surplus at the 1985 level (2 % of GDP). If this budget guideline is respected in 1986, it will again give some room for manoeuvre which would permit the rebuilding of investment fund reserves and, over the next few years, a further reduction in the burden of taxation and parafiscal charges on top of those proposed in the draft budget for 1986. It would also immediately give the authorities the finance needed for the planned capital expenditure, notably on roads and telecommunications infrastructure. Apart from the intrinsic advantages of such investment, in particular for the industrial restructuring policy, execution of these programmes would give appreciable support to the construction industry which is now facing a contraction in demand.

Table 18

Luxembourg: Main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current transactions account	General government net lending or borrowing	Money supply M2[3]	Unemployment in labour force[4]	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	**7,6**	3,6	3,8	2,5	6,7	7,4	1,8	:	**0,1**	0,6
1971-80	**9,6**	3,1	6,3	6,7	10,5	21,5	2,2	:	**0,3**	1,3
1981	**4,2**	−2,6	7,0	7,8	9,0	32,0	−2,3	:	1,0	−0,6
1982	**9,9**	0,3	9,6	10,5	6,0	40,8	−1,4	:	1,2	0,6
1983	**6,1**	−2,2	8,5	9,1	6,6	31,0	0,0	:	1,5	−0,3
1984[1]	**9,2**	3,2	5,8	6,7	4,2	33,2	1,5	:	1,7	0,5
1985[2]	6,0	1,7	4,2	3,7	4,9	32,1	2,1	:	1,7	0,6
1986[2]	6,4	1,3	5,0	3,5	5,6	30,8	1,9	:	1,6	0,4

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] End of the year.
[4] Eurostat concept.

The Netherlands

In the *Netherlands*, the rate of increase of economic activity in 1985 was comparable with that in 1984. Real gross domestic product grew by around 2 %, mainly due to the fairly buoyant expansion of exports. However, despite the upturn in private consumption, domestic demand grew less sharply, mainly because of the weakness of demand for housing and the decline in public-sector investment. The moderation of labour costs in earlier years made it possible to improve the level of corporate profits. This was a favourable influence on the sharp upturn in corporate investment in plant and machinery, which started early in 1984; but the increase in building investment is still small. Overall, corporate investment remains below the late 1970s level, expressed as a percentage of gross domestic product (10,0 % in 1983-85 compared with 11,3 % in 1977-79). The number of unemployed fell, as an annual average, and the unemployment rate declined from 14,2 % of the labour force in 1984 to 13,5 %. Consumer price rises remained very moderate. The current account surplus increased further, to 4,4 % of gross domestic product. The resultant increase in the liquidity ratio has not been entirely offset by monetary policy, given the low inflation rate, and the still high general government borrowing requirement — 8 % of net national income.

In 1986, the rate of increase of gross domestic product is not likely to accelerate greatly and will probably reach almost 2 %. Exports will go on expanding but at a somewhat lower rate. Domestic demand will, on the whole, become more buoyant. Private consumption will be boosted slightly by the rise in wages resulting from the new collective agreements and the increase in employment. The improvement in company profitability and the higher capacity utilization are likely to favour the expansion of capital widening investment, particularly by companies in the exporting industries. But residential construction and public investment will again dip slightly. Inflation will fall to a very low rate, with lower import prices largely offsetting the effect of the somewhat faster rise in unit labour costs. The favourable movement of the terms of trade will produce a sharp rise in the current account surplus which could exceed 5 % of gross domestic product in 1986. Employment in manufacturing industry could well increase slightly for the second year in succession.

In recent years, economic policy has chiefly concentrated on reducing the budget deficit and the level of taxation and social security contributions, improving company profitability and making changes in working hours and employment opportunities; but the results obtained so far are still insufficient in view of the seriousness of the problems.

Industrial companies have been able to increase their profitability appreciably, and subsequently, their investment. Company finances and competitiveness were improved by holding down the rise in labour costs, partly as a result of a cut in social security contributions. However, the level of profitability now reached is still an argument in favour of a moderate increase in real wages.

The prospects for 1986 are fairly encouraging in this respect. The 1982 agreements between labour and management severely limited the rise in earnings, but the current decentralized negotiations at industry and company level will bring about a more substantial rise in wages overall. A general consensus should be sought and maintained on the priorities of collective agreements, in order to prevent them from deviating too sharply from productivity gains and so becoming incompatible with the maintenance of competitiveness.

The result of decentralizing wage negotiations is likely to be greater pay differentiation between sectors, and this could promote greater labour mobility, which would favour even more the wages structure and would curb the tendency for excessive rationalization investment. In the 1980s, many selective measures have been taken with the view to hold back the rise in unemployment: lower minimum wages, reduced parafiscal pressure, restricted unemployment compensation, more part-time jobs, shorter working hours, and compensatory recruitment with no increase in labour costs. The greater flexibility of demand on the labour market, and the wage differentiation which may become possible under negotiations at industry and company level, are further improving the favourable recruitment climate. Until recently this policy had not had the expected effects on the level of employment, but there are signs of an improvement in 1985. Because of the upturn in activity and all the measures mentioned, employment has risen sufficiently to reduce unemployment in 1985 somewhat. However, programmes to provide employment for young people should be expanded so as to give them easier access to the labour market from which they are often debarred by inadequate vocational training.

Progress has been made in achieving a healthier public finance situation: the size of the public sector has been reduced markedly between 1982 and 1985 and the general government net cash deficit was cut from 10 % to 8 % of net national income. In the same period the burden of taxes and social security contributions was reduced by some 1 % of net national income. The reduction of the deficit is not only due to the major effort in controlling expenditure, partly nullified, moreover, by overshoots on social security costs and debt interest charges but it stems also from the

rise in natural gas revenue. The marked drop forecast in gas revenue from 1986 on is likely to make it even more difficult to trim the budget deficit. So even by making the savings provided for by the government agreement, there is limited room in the draft 1986 budget for any further appreciable reduction in the borrowing requirement, although, care should be taken to bring the general government cash deficit down to under 8 % of net national income in 1986. Nevertheless, a temporary slowdown in the rate of reducing the general government borrowing requirement, is in present circumstances advisable in order to avoid the necessity of a deliberate increase in the tax burden or the introduction of additional measures which might hamper the recovery of corporate investment and private consumption. Faster growth stemming from the improved investment and export performance appears to be a necessary condition to create the financial room for manoeuvre so that purchasing power of the private households could be increased, notably by reducing social security contributions or direct taxes, without in the long run jeopardizing the desirable stabilization of the rapidly increasing debt interest charges. This could provide a solution to the external surplus dilemma which cannot be solved in the present circumstances by simply relaxing the management of public finance.

Table 19

The Netherlands: main economic aggregates, 1961-86

	GDP current prices	GDP real terms	GDP deflator	Private consumption deflator	Compensation per employee	Current transactions account	General government net lending or borrowing	Money supply M2[3]	Unemployment in labour force[4]	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	10,6	5,2	5,2	4,1	10,6	0,0	−0,8	9,1	1,0	1,2
1971-80	10,8	2,9	7,7	7,8	10,7	1,3	−1,5	10,8	4,5	0,2
1981	4,8	−0,6	5,4	6,3	3,6	2,1	−5,5	5,3	8,8	−1,5
1982	4,5	−1,8	6,5	5,3	5,6	2,8	−7,1	7,6	11,7	−2,5
1983	2,5	0,6	1,9	2,8	3,4	2,9	−6,5	10,5	14,0	−2,0
1984[1]	4,3	1,7	2,6	2,6	0,6	4,1	−6,3	7,7	14,2	−0,5
1985[2]	4,5	2,1	2,3	2,4	1,4	4,5	−5,9	8,0	13,2	0,4
1986[2]	3,0	2,0	1,0	1,1	2,5	4,5	−6,5	6,5	13,0	0,6

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] End of the year.
[4] Eurostat concept.

United Kingdom

The upturn in the *United Kingdom* economy, which started in 1981, has lasted longer and been somewhat stronger than in the rest of the Community. Economic expansion has been accompanied since early 1983 by a rise in employment, but this has not been sufficient to allow any decline in the number of unemployed. The annual inflation rate appeared to have stabilized at around 5 % in 1983 and 1984, but inflation performance was threatened at the beginning of 1985 by a steep depreciation in the sterling exchange rate (caused mainly by worries about the miners' strike, about oil prices and about the government's resolve to contain public spending and borrowing). The authorities reacted by raising interest rates sharply and by reaffirming a tight budgetary stance. Sterling subsequently strengthened, and the outlook for inflation over the next year is now improved. The higher sterling exchange rate, however, especially against other European currencies, together with unit wage costs rising noticeably faster in the United Kingdom than in the main competitor countries, has led to a deterioration in the international competitiveness of UK manufacturers, worsening prospects for exports in 1986. This factor contributes to the slower growth in real GDP expected for 1986, when the pattern of growth is likely to be strongly weighted towards private consumption.

A rise in real GDP of almost 3½% is likely to be recorded for 1985, but adjusted for the distortions caused by the coal strike, which ended in March of this year, the growth rate is close to 2½%. Fuel imports have fallen back since the end of the strike and other imports have also grown at a slower rate than in 1984, while exports have gained market share in buoyant world trade, so that the external balance has contributed strongly to GDP growth. While real disposable incomes have been growing fairly fast, as a result of a sustained increase in average earnings and boosted by tax cuts in the March 1985 budget and the recovery of miners' earnings, growth of private consumption has been moderated by a higher saving ratio probably induced by somewhat faster inflation and higher interest rates. In spite of continued strength in investment by the enterprise sector (particularly in the first quarter, as some expenditure was brought forward to take advantage of tax arrangements), lower capital expenditure by the public sector and for residential purposes is likely to result in the slowest expansion of total fixed investment since the 1980-81 recession. Employment has continued to rise, but this has led only to a slowing in the increase of unemployment, because many of those entering new jobs were not previously recorded as unemployed.

In 1986 there is likely to be a significant shift in the pattern of demand from net exports towards private consumption. With average earnings in nominal terms likely to continue rising appreciably (by some 7 %), the slowing expected in consumer prices, mainly as a result of weak import prices following the appreciation this year of the sterling exchange rate, will boost real household incomes and, together with a possible fall in the saving ratio, will lead to faster growth of private consumers' expenditure in real terms. This could be further reinforced by a cut in personal taxation, as the outlook for the public finances suggests that, on the basis of the latest version of the medium-term financial strategy (MTFS), there will be some room for easing of taxation or increase in public expenditure ('fiscal adjustment'). Stronger consumer demand is likely to be offset, however, by weak public consumption and slower growth of exports resulting from the loss of competitiveness. Overall real GDP growth is expected to slow to a rate of about 2 %. There may be some slight improvement in the outlook for the unemployment count, particularly in view of measures already announced in the 1985 budget to extend youth training and community work for the long-term unemployed.

Budgetary policy is aiming to bring general government expenditure and the public sector borrowing requirement (PSBR) back on to declining paths in relation to GDP, after the overshooting in 1984/85 mainly caused by the extra costs associated with the miners' strike. There are certain risks to the MTFS objectives in the form of upward pressure on spending from public sector pay awards and from increases in social security benefits and of a possible shortfall on revenue associated with North Sea oil output. These risks appear at present, however, to be largely covered for the current and next financial years by the contingency reserves, the level of which was increased in the 1985 budget. On balance it is still expected that the official projection for the PSBR of UKL 7 500 million in 1986/87 will allow some room for a fiscal adjustment to be introduced in the budget next spring, though the size of this adjustment is uncertain and could be well below the latest official estimate of UKL 3 500 million.

In view of the emerging weaker export and investment trends, which may well be prolonged, particularly if expansion of the world economy slows down, there is a danger that slower growth could persist in the UK for two or three years, making any significant reduction of unemployment unlikely. In these circumstances, any margin of manoeuvre for supporting the economy via fiscal and interest rate policy should be fully used. In this respect it is important to note that the overall budgetary and public debt position of the UK now appears to be very robust. However, the extent to which fiscal policy can be used to strengthen activity depends

also on inflation performance. The acceleration of retail prices in the early months of this year was a temporary movement, resulting from a weakening of the exchange rate and the associated rise of interest rates, and has since been clearly reversed. Although the outlook is for an improved inflation performance in 1986, helped by falling import prices, domestic cost pressures are such that, in the absence of wage moderation bringing the increase in average earnings down from its present rate of 7-8 %, it will be difficult to bring the annual inflation rate below 5 % (the average rate since 1983) on a lasting basis.

In using the available room for manoeuvre afforded for fiscal policy, priority should be given to those measures which are most beneficial to the supply side of the economy and the creation of employment. The main emphasis of the present government in respect of fiscal changes has been to lower the burden of personal income tax in order to increase incentives to work and for enterprise. While reflecting a long-term approach, this may already be in part responsible for the increase in employment since 1983, much of which has been accounted for by people newly entering or re-entering the labour force. A further easing of income tax would be welcome, particularly if it were again used to raise substantially the tax threshold, since the provisions of the tax and social security systems still combine in some circumstances to set high effective marginal tax rates for those on low incomes. It is to be hoped that such anomalies will be eliminated in the reform of the social security system which is under discussion. Proposals for wide-ranging reform, published in a Green Paper in June this year, emphasized the need to integrate the different social benefits and to concentrate benefits on those most in need.

In 1986, when private consumption is in any case likely to be growing at a rapid rate (3-4 %), it would as usual be appropriate to consider other ways, in addition to income tax reduction, of using the fiscal room for manoeuvre. For instance, there would also be direct benefits to employment and inflation from reducing the cost of employment to enterprises, by lowering social contributions. There is also increasing evidence to support the argument that some of the room for manoeuvre should be used to finance public sector infrastructure investment, which is relatively labour-intensive. The state of some of the infrastructure was described earlier this year in a series of reports submitted by government departments for discussion in the framework of the National Economic Development Council. In view of these apparent deficiencies the situation should be carefully reviewed when spending plans are reformulated.

Monetary developments over the last year have been a source of some concern. The various indicators of monetary conditions, in particular the monetary aggregates and the exchange rate have often provided divergent information. In January, at a time when monetary growth was largely satisfactory, the sterling exchange rate came under considerable pressure and bank base rates which had fallen to below 10 % in late 1984 were raised to 14 %. In recent months, however, despite high (nominal and real) interest rates, the rate of growth of the broad measure of money supply, sterling M3, has been well above the 5-9 % target range for 1985/86 set out in the latest MTFS. Since March interest rates have declined slightly, but it is to be hoped that further reductions consistent with the monetary targets can be achieved in order to give support to economic activity.

In spite of the downward movement in interest rates during 1985, differentials with other countries have remained high and movements in sterling have at times been volatile. Within a period of 12 months from July 1984, the composite sterling exchange rate index first fell by more than 10 % and subsequently appreciated by more than 15 %. Such movements can have undesirable effects on prices and resource allocation and generate uncertainties. In both the previous and current financial years, this has been particularly evident with respect to the level of tax revenue linked to oil output, which depends upon both the dollar price of oil and the sterling-dollar exchange rate. Such experience illustrates the potential benefits of avoiding exchange rate overshooting that might be gained from full participation in the EMS. Given the greater convergence now existing in the economic policies of member countries, such a step should be given renewed consideration.

1985 and 1986 are thought to be the years of peak output of North Sea oil and gas, this sector accounting for some 6-7 % of total GDP and more than 20 % of visible exports. Even though the decline of oil output will occur at a much slower pace than its expansion (10 years ago, output was negligible), the economy will have to adapt to this important change. The most direct impact on economic policy may be with respect to tax revenue associated with oil, which is estimated to account for 9 % of general government receipts in the present financial year. Offical projections indicate that this share will be roughly halved by 1988/89. The decline of the oil surplus in the balance of payments will also need to be offset by improvements in other areas. The continuing strengthening of the invisible account will contribute towards this, but any further worsening of the non-oil trade account (which has moved from small surplus in 1981 to sizeable deficit in 1985, estimated at almost 3 % of GDP) could lead to considerable imbalance. It is therefore essential that the performance of the non-oil economy, which has been growing since the recovery began in 1981 by less than 2½ % per annum on average, should strengthen.

An improvement in the relations between the social partners could open the way to a significant reduction in the unemployment level in the medium-term. The series of supply side measures taken in recent years, such as the changes relating to personal taxation have, together with the improved growth performance, contributed to the substantial increase in the employed labour force (by more than 600 000, or almost 3 %, from the first quarter of 1983 to the first quarter of 1985). Further measures with regard to the labour market are being prepared. It is to be hoped that, if employment growth can be maintained, jobs will be filled increasingly from the pool of unemployed and to a lesser extent than has so far been the case from new entrants to the labour force.

The substantial productivity gains of the early 1980s have now slowed down, leading to an acceleration of unit labour costs, which is weakening the international competitive position of enterprises and threatening to reverse the improving trend of company profitability. In order to sustain the growth of investment and thus expand the capacity of the economy (particularly as the role of oil declines), and hence potential employment, a further shift in relative factor remuneration towards returns on capital is needed. In consequence, the growth of real wages, which for several years has been notably stronger than in other Member States, now needs to become much slower.

Table 20

United Kingdom: main economic aggregates, 1961-86

	GDP current prices[1]	GDP real terms[1]	GDP deflator	Private consumption deflator	Compensation per employee	Current balance	General government net lending or borrowing	Money supply[4]	Unemployment in labour force[5]	Employment
	% change	% change	% change	% change	% change	% GDP	% GDP	% change	%	% change
1961-70	7,1	2,8	4,2	3,9	7,1	0,0	−0,6	5,9	1,9	0,2
1971-80	16,2	1,9	14,0	13,3	16,0	−0,6	−3,1	14,5	4,0	0,2
1981	10,4	−1,1	11,7	11,2	13,5	2,7	−3,1	14,6	9,2	−3,9
1982	9,1	1,9	7,1	8,3	8,8	1,7	−2,3	10,6	10,6	−1,4
1983	8,6	3,3	5,1	5,1	8,8	1,1	−3,6	10,3	11,6	−0,8
1984	6,2	1,8	4,4	5,1	5,5	0,3	−3,8	9,6	11,8	1,5
1985[1]	9,1	3,4	5,5	5,3	7,7	1,1	−3,3	11,3	12,0	1,1
1986[2]	7,0	2,0	4,8	4,3	7,1	0,9	−2,8	8,6	11,7	0,9

[1] Estimates of the Commission services, October 1985.
[2] Forecast of the Commission services, October 1985, on the basis of present policies.
[3] Expenditure measure at market prices.
[4] Sterling M3, end of the year.
[5] Eurostat definition.

Annual Economic Review 1985-86

(Submitted for information to the Council, the Economic and Social Committee and the Parliament together with the proposed 'Annual Economic Report 1985-86)

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1. The economic situation and short-term prospects

1985 saw a marked slowdown in world economic activity as the expansion decelerated in the USA and the recovery in other parts of the world was not strong enough to maintain the rate of growth of world trade achieved in 1984. Growth in industrial countries outside the USA as well as in developing countries was fairly stable and is forecast to remain so in 1986. World trade is therefore expected to expand at approximately the same pace next year. In the Community a fall in the contribution to growth from external demand is likely to be compensated by a strengthening of domestic demand in 1986. The world recovery of the last few years has been accompanied by drastic changes in the balance of payments positions of important countries or regions, as well as by a further reduction of world inflation. Convergence of inflation rates in the Community has been further improved.

1.1. Economic growth and the business cycle

In 1985 growth has been regionally more even although weaker than the year before. Following the boom of 1984 economic activity slowed down in the USA, as generally expected, whereas it remained rather buoyant in other industrialized countries. At the same time, developing countries as a whole have managed to pursue their recovery. The expansion of world trade, while significantly slower than in 1984, has been sustained by developments outside the USA. Similarly, the decline in interest rates has tended to mitigate the effects of the slowdown in the USA.

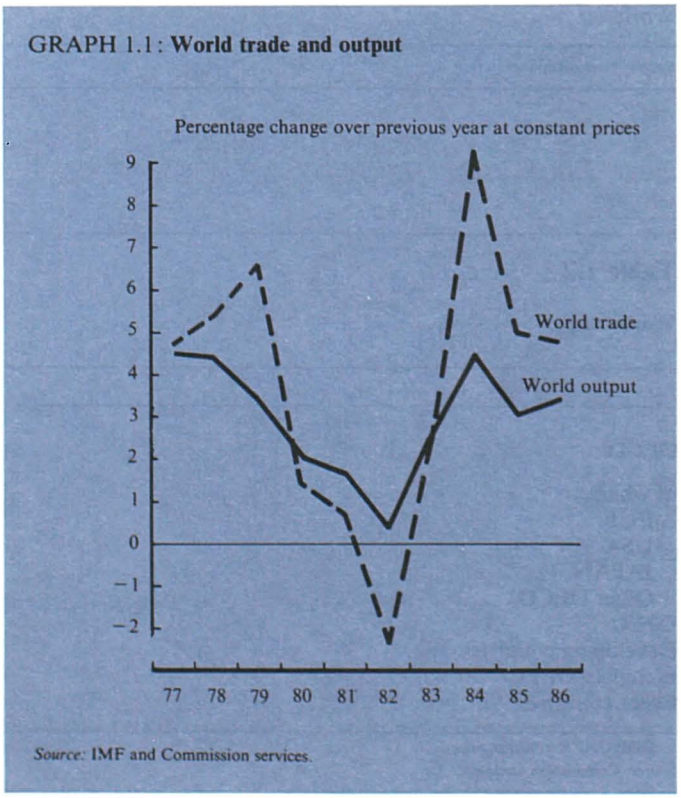
The changes in the growth rate of world output over the last business cycle have been accompanied by significantly stronger fluctuations in world trade (Graph 1.1). The volume of world trade actually declined in 1982, recovered sharply afterwards and slowed down again in 1985, when it is likely to have grown by 4 ¾ %. A similar rate of expansion is forecast for 1986 (Table 1.1).

The gross national product of the industrialized countries including the Community is estimated to have grown in real terms by 4 ½ % in 1984 (Table 1.2). This performance — the most favourable since 1978 — is in part a reflection of the boom in economic activity in the USA and the related export-led expansion in Japan and in Canada. Not surprisingly, growth in the industrialized world dropped in 1985. For the group as a whole however this deceleration was not very substantial, being of the order of 1 ½ percentage points.

In the USA, the upswing which had started in late 1982 peaked in the first half of 1984. In the second half of that year output growth decelerated to 3 ½ % measured at an annual rate and slowed down further to about 1,5 % in the first half of 1985. For the whole year 1985 therefore, a growth rate of slightly above 2 % seems realistic, which implies some strengthening of economic activity in the second half of 1985. This trend is expected to continue in 1986 and if realized, would result in an average GDP increase of 2 ½ % next year.

The deceleration of US growth is a reflection of the lessening strength of the factors on which the strong upturn was built. The effect of expansionary fiscal policy on domestic demand has increasingly leaked into imports, especially as a restrictive monetary policy through most of 1984 helped push the

GRAPH 1.1: **World trade and output**



Source: IMF and Commission services.

dollar to a very high value. The effect of the 1981 tax cuts on investment, which were largely delayed until 1984, when real business fixed investment grew 20 %, left little room in 1985 for further substantial increases. The effects of earlier cuts in marginal tax rates on personal incomes are unlikely to provide an acceleration of the growth rate in 1985.

Worries about the economic effects of the federal budget deficit have given rise to a Congressional budget resolution that is expected to reduce it by about 1 % of GNP in fiscal 1986. Fiscal policy will be less expansionary. In a reversal of the situation in the last few years, monetary policy has become cautiously expansionary and the narrower measures of money supply have recently increased beyond the upper limit of their target zones. This change of policy has led to lower interest rates and a weakening of the dollar exchange rate.

In Japan the export-led recovery registered in 1984 is likely to persist in 1985. In 1986, the appreciation of the yen

Table 1.1

World imports of goods

(percentage change over previous year at constant prices)

	1981	1982	1983	1984	1985	1986
OECD	−1,2	—0,4	4,1	12,9	6,4	5,4
of which						
EUR	−2,9	2,4	2,2	7,1	5,0	5,3
USA	2,5	−5,0	11,8	29,9	10,0	6,6
JAPAN	−2,2	−0,5	0,3	10,7	3,0	4,7
Other OECD	−0,2	1,1	−0,1	7,2	6,3	4,2
OPEC	27,4	5,5	−8,2	−9,0	−10,9	−4,0
Developing countries excluding OPEC	4,3	−6,1	−0,3	6,0	4,0	4,5
World	1,8	−1,0	2,2	9,3	4,8	4,8

Source: Commission services.

Table 1.2

World output[1]

(percentage change over previous year at constant prices)

	1981	1982	1983	1984	1985	1986
OECD	1,6	−0,2	2,6	4,5	2,8	2,7
of which						
EUR	−0,2	0,5	1,0	2,2	2,3	2,5
USA	3,4	−3,0	2,9	6,8	2,3	2,5
JAPAN	4,2	3,0	3,0	5,7	5,0	4,2
Other OECD	1,6	0,9	1,6	3,3	2,6	2,5
OPEC	−3,5	−4,0	−2,5	1,4	2,0	2,0
Developing countries excluding OPEC	3,0	0,9	0,8	3,9	2,9	3,8
Other countries	2,3	2,2	3,1	3,9	3,6	3,7

[1] GDP/GNP at constant prices.

Source: Commission services.

underway at the moment will probably reduce the competitivity of Japanese exports. In spite of a significant expansion of private investment since 1983, the growth rate of internal demand was modest in 1985 and will remain so in 1986. This is partly a result of the strict fiscal policy stance adopted by the Japanese authorities in order to reduce, in the medium term, an already high level of indebtedness; at the same time private consumption has not accelerated and will probably remain sluggish with no significant reduction of the savings ratio. Recently the Japanese Government has adopted a number of measures to sustain internal demand; but this programme will not be sufficient to reduce significantly the surplus on the current balance of payments. This surplus which amounted to USD 35 000 million in 1984 and is expected to reach almost USD 50 000 million in 1985 could grow to approximatively USD 60 000 million in 1986.

The output of the developing countries (excluding OPEC) is forecast to grow by 3 % in 1985 and by 3 ¾ % in 1986. Although still modest by historical standards — their growth rate averaged around 5 ½ % from the middle of the 1960s to the end of the 1970s — developing countries as a whole seem to have overcome the difficult period of the early 1980s, when output per head was declining. They are now benefiting from the recovery in the industrialized countries, as well as from an improved financial position after severe internal adjustments. The acceleration of output growth is concentrated in regions where the crisis was deepest, namely Africa and Latin America. At the same time, the newly industrialized countries of South-East Asia will continue to enjoy distinctly faster growth than the rest, even allowing for the fact that their exports are particularly sensitive to the less bright prospects on the US market.

In the Community, real gross domestic product has been growing since the first half of 1984 at an annual underlying rate of between 2 % and 2 ½ %, and is not forecast to move in a more expansionary way throughout 1986 (Table 1.3).

These prospects for 1986 imply an acceleration of private consumption (+2,7 %), which should benefit from faster growth of real disposable income of households (+2,3 % as against +1,5 % in 1985). The slowdown of inflation is a major factor here, but substantial tax cuts announced in some countries will also tend to stimulate household spending in 1986. Real fixed investment as a whole is likely to accelerate (+3 ¾ % after 1 ½ % in 1985), mainly because construction activity is likely to stabilize after the decline in 1985, even though the prospects in the construction sector remain gloomy. It is expected that those factors which have stimulated investment in equipment since the start of the recovery should continue to operate much as before.

Table 1.3

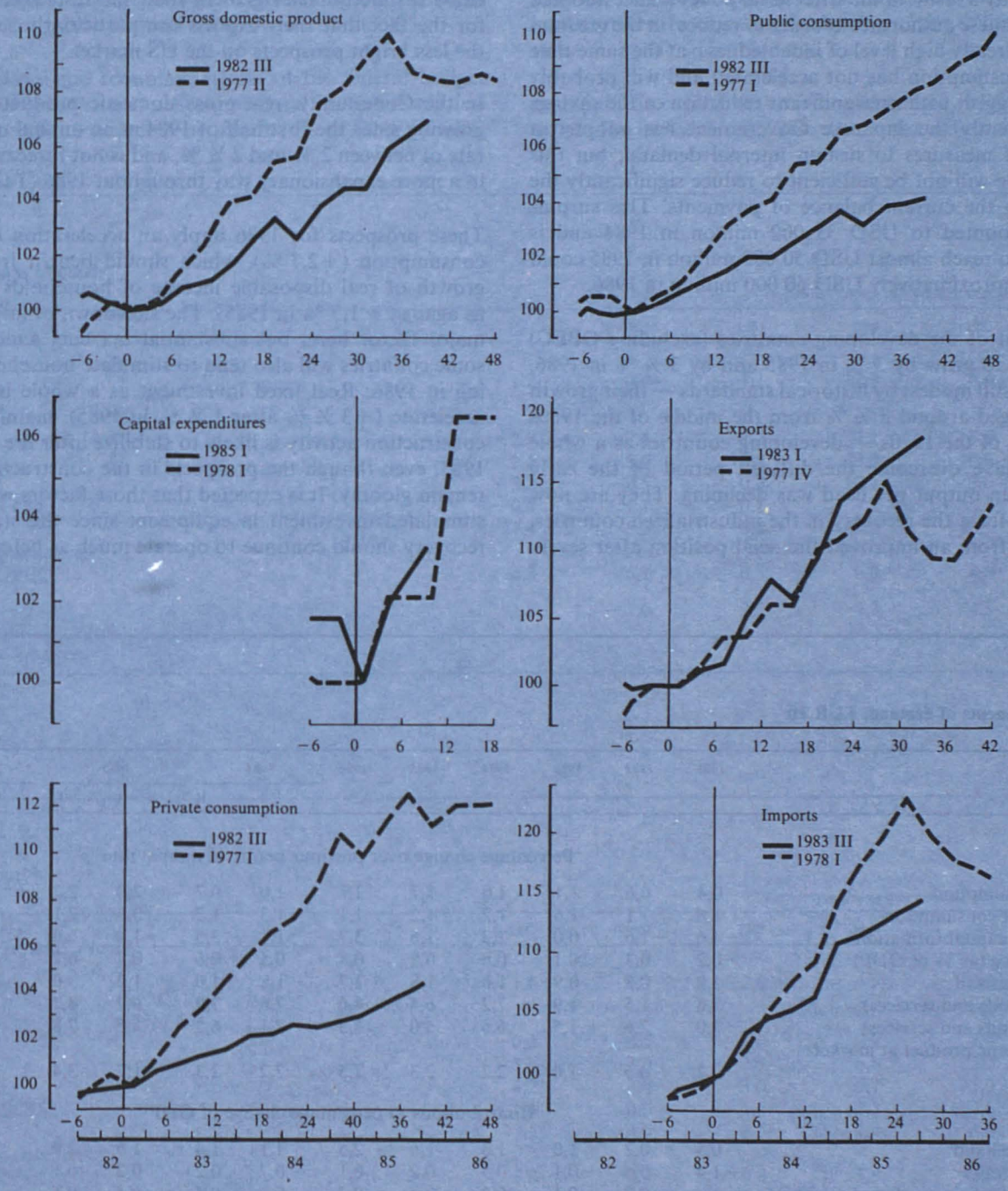
Main components of demand, EUR 10

	1981	1982	1983	1984	1985	1986	1984		1985		1986	
							I	II	I	II	I	II
	Percentage change over previous period at annual rate											
Private consumption	0,4	0,6	1,1	1,0	1,7	2,7	1,0	0,7	2,0	2,2	2,9	2,6
Government consumption	1,6	1,1	1,6	1,2	1,2	1,1	1,3	1,7	0,6	2,1	0,8	0,7
Gross fixed capital formation	−4,6	−1,6	0,0	2,3	1,6	3,7	1,1	3,5	−1,4	6,0	3,0	2,7
Stockbuilding (as % of GDP)	−0,2	0,3	0,1	0,6	0,8	0,8	0,5	0,6	0,7	0,7	0,8	0,9
Domestic demand	−1,8	0,8	0,9	1,8	1,8	2,7	1,8	1,6	1,2	3,0	2,6	2,6
Exports (goods and services)	3,8	1,5	1,9	7,2	6,4	4,6	7,6	7,9	6,7	4,2	4,8	4,6
Imports (goods and services)	−2,0	2,6	1,5	6,6	5,0	5,3	7,1	6,2	5,5	2,8	6,1	6,1
Gross domestic product at market prices	−0,2	0,5	1,0	2,2	2,3	2,5	2,2	2,3	1,7	3,4	2,2	2,0
	Contributions to percentage change of GDP[1]											
Domestic demand	−0,5	0,2	1,0	1,3	1,6	2,5	1,1	1,4	1,0	2,9	2,5	2,3
Change in stocks	−1,4	0,6	−0,1	0,5	0,2	0,1	0,7	0,2	0,2	0,1	0,0	0,3
Balance of trades in goods and services	1,7	−0,3	0,1	0,2	0,4	−0,2	0,1	0,5	0,4	0,5	−0,3	−0,4

[1] Does not necessarily add up to GDP growth due to aggregation of national data with different base years.

Source: Commission services.

GRAPH 1.2: **Comparison of recent recovery (—) with previous one (- -)**



The charts show how the current recovery, dated from the 3rd quarter 1982 (GDP) compares with the previous recovery (dated from the 2nd quarter 1977, GDP) over the same length of time. All figures in volume terms.

Source: Commission services.

With export performance of the Community probably declining and with stronger domestic demand inducing more imports, only a slight contribution to growth is to be expected from the net foreign balance in 1986. In total, growth in the EC is forecast to shift from external sources to internal demand in 1986.

This is confirmed by the latest consumer and business survey results. Consumer confidence improved in most member countries after a rather subdued development in the first half of the year. In industry the assessment of total orderbooks continued to improve while the export expectations deteriorated somewhat. The recent survey results in construction also draw a less gloomy picture.

This recovery in the Community has been lasting for nearly three years and in terms of previous experience the cycle would appear to have reached a mature stage. This raises the question of how long it is likely to continue.

The present economic upturn in real gross domestic product until now has been significantly less buoyant than the previous one which began in the first quarter of 1977 (Graph 1.2). On the other hand, several arguments support the view that the present upswing will go on longer than its predecessor, which was heavily influenced by the second oil shock.

In the early quarters of the present upswing in total economic activity, the investment trend was still downwards. A continued decrease in real capital expenditure for more than two years, as has been the case in 1982 and 1983, is something which has never been observed in previous business cycles in the post-war period. In 1984 this downward trend finally came to a halt. Investment recovered further in 1985; its rate of growth of about 3 % has been rather modest, however, mainly because of the structural weakness of demand in the construction sector.

This positive trend in total investment is likely to continue in 1986 and could also be a feature of the remaining years of the 1980s. Many of the basic conditions for a long-lasting expansionary phase of investment, particularly investment in equipment, are more favourable than they have been for a long time.

First, inflationary tensions are not expected to increase in the near future; raw material and crude oil prices will probably be fairly weak, and the dollar less firm, thus dampening the trend of import prices. This environment will offer scope for bringing interest rates down further. Central banks in most Member States will not be confronted with increasing inflationary pressures — as had been the case in the third year of the previous two upswings — and will thus not be inclined to tighten monetary policy on this count.

Second, profits have increased in most European companies in the course of the past couple of years. This positive trend is likely to continue because of relatively low cost pressures — thanks to the moderate wage increases and weak raw material prices which are expected.

Third, the economic confidence of the business sector could thus further improve, which reinforces the argument for a continuation of an induced investment growth process.

Fourth, there are also signs that new technologies (e.g. telecommunications, robotics, microelectronics, etc.) are increasingly providing a stimulus to growth. A growing number of companies in Europe are perceiving the need to step up investment in these new technologies if they are not to run the risk of losing market shares. The increasing proportion of this type of investment is a main feature of the latest investment survey results in European industry.

All these considerations point to a phase of cyclical recovery in real investment which will be significantly longer-lasting than in the two previous upswings, particularly the one starting in 1977. The performance of investment is more likely to resemble that in the recovery period at the beginning of the 1970s, provided that the expected strength of private investment is not accompanied by a decrease in real public investment.

Real private consumption at present remains below the level that would have been implied if the path of previous cyclical upswings had been reproduced. The weak but accelerating increase in real disposable income will possibly give some boost to consumption beyond 1986. The current and expected improvement in real income, unlike that in the 1970s, is being brought about mainly by a decrease in the inflation rate and by tax cuts, rather than increases in wages and social transfers. As pointed out above, this implies that the upswing phase will not need to be cut short by a more restrictive future turn of economic policy. Even though private consumption will probably not pick up as strongly as in the 1977-79 upswing period, the cyclical pattern of previous upturns points to a significantly more buoyant development of private consumption in the next two years than in 1984 and 1985.

Real exports are the only demand component which have so far increased more strongly in the present upswing than in the previous recovery. Even if export performance becomes somewhat weaker in 1986 it will still contribute to overall growth and should remain above the cyclical trend of the

previous recovery. This forecast relies on the assumption, however, that growth continues in the United States at a rate close to 2,5 % in real terms.

The cyclical development of real public consumption has until now been significantly less strong than in the period 1978/79; this will continue to be the case throughout 1986, according to Commission forecasts.

To sum up, the present recovery has, in terms of the increase in aggregate economic activity, been less dynamic than the previous one. This gap will continue in 1986, but will narrow. However, the expected contribution of private investment as well as a more solid base for private consumption could help to extend the length of the present economic upswing beyond that of the previous recovery.

A stable growth rate for the Community as a whole seems to be one of the characteristics of present trends. It is in fact difficult to find in the Community's history a three-year period with a comparable constancy of growth rates. The lack of marked fluctuations raises the question of how these actual growth rates compare to potential growth. Estimates of long-term potential growth in the Community indeed point to a rate of no more than 2 ½ % and possibly even less than that. Moreover, the rate of capacity utilization in industry is very close to the peak reached during the previous upswing (82,5 % in June compared with 84 % at the cyclical peak of 1979/80). This reinforces the argument that moderation of the growth of real labour costs per capita and a strong increase in investment over a number of years are necessary if there is to be sufficient capacity for the Community economy to grow for a time at a rate substantially above the long-term potential rate so as to reduce unemployment significantly.

1.2. Changing pattern of external balances

The recovery in world activity after the recession of the early 1980s has been accompanied by — and was in fact to a large extent dependent on — unprecedented changes in balance of payments positions throughout the world.

The accumulation of current account deficits or the disappearance of surpluses in the first half of the 1980s was concentrated on the USA and the OPEC countries (Table 1.4) The corresponding improvements are mainly reflected in the balances of Japan, the non-oil developing countries and the Community.

Various factors have been at the root of the newly emerging world balance of payments structure. They are related to long-term economic trends, cyclical developments, economic policy and developments in individual markets. They may be summarized as follows.

(i) The assessment of prospects for economic growth in different parts of the world has been changing, inducing a stronger demand for investment in physical assets in some parts than in others. This is possibly one of the factors behind the growth of the US external deficit.

(ii) The enormous increase in the US budget deficit had to be financed mainly by external resources — which up to a point proved to be rather easy, given the confidence of foreign investors in the US dollar and interest differentials favourable to the dollar.

(iii) Differences in the timing of the growth cycle among industrialized countries have tended to raise external deficits

Table 1.4

World current external balances (including official transfers)

(in USD '000 million)

	1980	1981	1982	1983	1984	1985	1986
Industrial countries	−39	3	1	2	−65	−70	−55
of which							
EUR	−36	−12	−9	2	3	12	18
USA	7	11	−4	−36	−102	−126	−131
Japan	−10	6	8	22	35	49	59
OPEC	100	35	−23	−17	−6	−12	−27
Developing countries excluding OPEC	23	−91	−76	−54	−20	−25	−30
Errors and omissions	−19	−56	−96	−64	−66	−78	−81

Source: IMF and estimates of Commission services.

in the leading countries and to create surpluses in the lagging ones. This effect has also contributed to the US deficit.

(iv) Related to this, desynchronized adjustment policies have enforced improvements of the balance of payments in some parts of the world, while necessarily affecting the rest inversely. This factor played a major role in the improvement of developing countries' external accounts. It has also been at the root of the swing in the Community's balance from an important deficit in the early 1980s to a moderate surplus.

(v) Changes in relative prices and shifts in demand — notably for oil — have particularly worsened the external position of OPEC countries, with corresponding improvements in the position of Japan, Europe and the non-oil developing countries.

A major part of the shifts in the external balances called for by the factors listed above has been achieved through changes in exchange rates, which in turn led to substantial modifications in the price competitiveness of individual countries or groups of countries. The pattern of external balances which has emerged from these trends presents the following picture for the various countries.

The US deficit on current account is likely to be about USD 126 000 million in 1985 and will not decline in 1986 according to the forecast (USD 130 000 million). The appreciation of the US dollar in real terms against the yen, the ECU and other currencies since 1980 has led to a sharp deterioration in US price competitiveness. As a consequence, the export performance of the USA has been poor. In 1984 and 1985 taken together, American exports of goods probably grew by 10 percentage points less than average imports of US customers (weighted by their shares in US exports, Table 1.5). In 1986, when the competitive position of the USA will start to improve somewhat on given exchange rate assumptions, the USA may start to regain some of the lost market share. The geographical pattern of US export markets has also been detrimental to US exports. A large part — about 20 % — of US exports is directed towards Latin America, which suffered from the rigorous policies of retrenchment being applied in a number of countries in that region. Apart from the weak export performance, American import volumes have increased roughly three times as fast as real domestic demand both in 1984 and 1985.

The swing in the OPEC current account of over USD 100 000 million since 1980, producing a deficit, resulted from a decline of a roughly comparable magnitude in these countries' oil export earnings. This large drop in oil revenues was due not only to the fall in world oil consumption and the associated downward adjustment in oil prices but also to continued increases in the market shares of other oil exporting countries.

A salient feature of balance of payments developments in the past three years has been the marked improvement in the current account position of the developing countries excluding OPEC. Over a period of only four years (1981-84) the three largest debtor countries — Brazil, Argentina, Mexico — succeeded in reducing their combined current account deficit by USD 30 000 million. This adjustment was mainly achieved by a substantial reduction of imports. Also important, however, is the fact that non-oil developing countries taken as a group managed to strengthen their export earnings. Indeed, the combination of expanding import demand in industrial countries — in particular in the USA — and the temporary upward movement in non-oil commodity prices resulted in a significant increase in their earnings. All in all, non-oil developing countries thus succeeded in reducing their current account deficit as a percentage of gross national product (GNP) from a peak of 5,1 % in 1981 to 2,2 % in 1984 (World Bank figures). However, the differences between individual countries and regions remain substantial, and the corresponding figure for Africa is as high as 9,4 % for 1984.

The reduction of the current account deficits of developing countries has eased the debt crisis, but not prevented a further, albeit slower, rise of overall external debt, which amounted to almost USD 900 000 million or 34 % of GNP in 1984 for all developing countries taken together. On average, about 20 % of export earnings have been used for debt servicing in the period 1982 to 1984 — significantly more than in the 1970s. The recent decline of US interest rates is likely to have lowered this ratio somewhat.

The Community's current account, which was practically balanced in 1983 and 1984, is forecast to show a surplus of around USD 12 000 million in 1985 and to improve further next year.

The improvement of the Community's current balance is attributable in part to the slow growth of import volume and the fall in the dollar price of oil (Graph 1.3). The quantity of imported oil fell by around 20 %, and the oil import bill from around USD 120 000 million in 1980 to USD 80 000 million in 1985 (in ECU terms the oil bill actually showed a rise over this period).

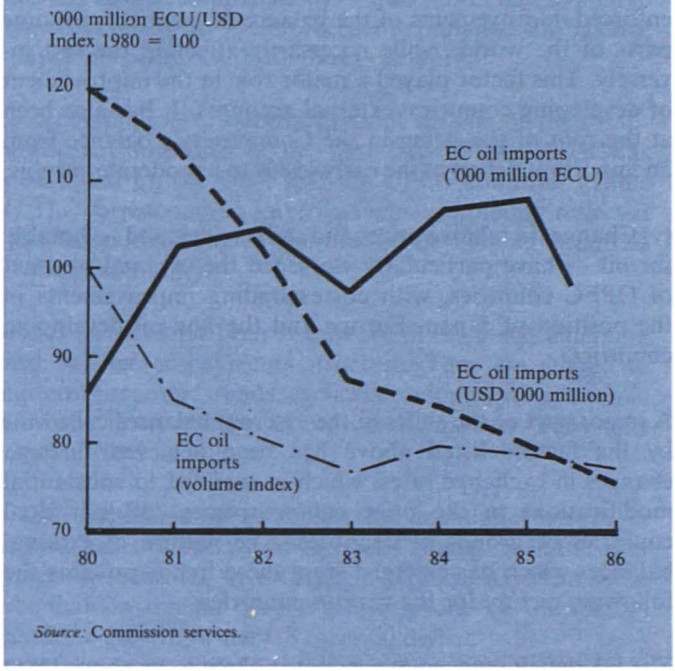
The Community's overall export performance presents a mixed picture. The gains in market share seem modest compared with the favourable price situation for the Community's exports. In fact, between 1981 and 1984 the Community's average index of producer and wholesale prices,

expressed in a common currency, rose by 4 percentage points per year less than the average of the corresponding price index of the Community's competitors on world markets and some further improvement has occurred in 1985. Yet gains in market share were limited to around 1 % in 1984 and 1985 (Table 1.5). One reason behind this relatively poor performance may be the pricing policies of European exporters when competitiveness was improving. The available evidence — *inter alia* relatively strong rises in export prices in ECU terms — suggests that exporters rather than expanding their sales in volume terms preferred to restore their profit margins, perhaps partly because they did not expect the favourable situation to last long enough to justify the efforts associated with the establishment of a durable increase in market shares.

The relative weights of the factors which have contributed to the improvement of the Community's external balance over the last couple of years are now likely to change. The cyclical impact of slow growth in Europe compared with North America and Japan, which was particularly important in 1983 and 1984, is weakening. As a result, for the first time since 1982 the volume changes of exports and imports will in 1986 probably make no positive contribution to the overall balance. The expected further increase in the surplus will instead be accounted for by improving terms of trade, reflecting partly both a decline in oil prices in dollar terms and the assumed decline of the dollar exchange rate against the ECU.

All in all, the Community's overall external balance has improved significantly during the recovery and is likely to continue to do so in 1986. However, the position of some individual member countries remains vulnerable.

GRAPH 1.3: Oil imports of the Community



Source: Commission services.

1.3. Continuing disinflation

The recovery of the world economy in the last couple of years has been accompanied by a general process of disinflation in the industrialized countries. The fact that price increases are continuing to slow down even after the recovery has been

Table 1.5

Export markets and exports of goods

(percentage change over previous year at constant prices)

	export markets			exports		
	1984	1985	1986	1984	1985	1986
EUR[1]	6,8	5,0	5,1	7,7	6,4	4,8
USA	8,1	4,9	5,2	5,2	−1,9	8,6
Japan	12,8	7,7	6,0	15,4	7,5	5,1
OPEC	5,2	1,0	2,8	1,9	−8,9	−6,1
Developing countries excluding OPEC	9,9	4,7	5,1	11,3	5,5	4,5

[1] Intra and extra EC.

Source: Commission services.

underway for nearly three years is one of the characteristics of the present business cycle. Average inflation, as measured by the deflator of private consumption, has fallen in the industrialized countries from 12 % in 1980, the previous peak, to around 4 % in 1985. By contrast, the general price level is still rising fast in developing countries as a group. Due to hyperinflation in some Latin American countries the average annual rate even increased, from 27 % to 35 % in this period, according to IMF sources.

The fall in inflation since 1980 is common to all the major industrial countries. The extent of this slowdown, expressed as the reduction in inflation in percentage points, was greatest in the countries with the highest inflation five years ago. Consequently, convergence has improved not only within the Community, but also worldwide. Two principal common factors may be identified behind this parallelism: oil prices expressed in USD have dropped substantially since 1981, and, more fundamentally, monetary policy in industrialized countries has followed a course orientated towards price stability.

Consumer price inflation in the USA declined from 10,3 % to 3 ¼ % between 1980 and 1985, and in the Community from 12,8 % to 5,2 % (Table 1.6). While this is a decline of similar size, the circumstances in which it has been achieved differ in one important respect: European currencies depreciated effectively by 8 % per annum over this period, while the dollar's effective exchange rate rose by the same average annual rate. The EC thus managed to reduce inflation despite continuous upward pressure on import prices. This aspect will be further discussed later.

The rate of consumer price increases in the USA stabilized at some 3 % in 1984; it is expected to accelerate somewhat in 1986. In the Community the slowdown is still going on this year and probably next, when the rate of increase is forecast to be 3,9 %. In each of the six years from 1981 to 1986 the average inflation rate in the Community will thus have fallen by between one and two percentage points and is expected to be lower in 1986 than the US rate.

The basic factor behind this achievement, as mentioned, has to be seen in the stance of monetary policies. The increase in the money supply on the wider definition slowed down from an annual average of 12 ½ % in 1975/80 to 9 % in 1980/85, and is decelerating further. The decline of oil prices has to some extent to be attributed to microeconomic factors like the dismantling of monopolistic power on the supply side or to the efforts of consumers to economize in oil

Table 1.6

Consumer prices[1]

(percentage change over previous year)

	1973/60	1981/73	1982	1983	1984	1985	1986
B	3,7	7,8	7,5	7,0	6,2	4,9	3,2
DK	6,1	10,7	11,0	7,2	6,6	4,2	1,7
D	3,6	5,0	4,8	2,9	2,5	2,1	1,5
GR	3,5	16,8	21,1	19,5	18,1	18,0	16,0
F	4,7	11,1	11,2	9,4	7,3	5,8	4,0
IRL	6,3	16,1	16,0	9,7	8,5	5,7	5,3
I	4,8	17,8	17,1	14,9	11,1	8,6	6,5
L	3,0	7,5	9,7	8,4	6,7	3,7	3,5
NL	5,8	6,3	5,4	2,9	2,6	2,4	1,1
UK	4,8	15,1	8,3	5,1	5,1	5,3	4,3
EUR	4,5	11,3	9,8	7,6	6,2	5,2	3,9
Memo:							
EUR-standard deviation[2]	1,3	4,4	4,6	4,6	3,4	2,8	2,5
USA	3,1	8,0	5,9	3,7	3,2	3,2	4,4
Japan[3]	5,9	8,5	2,8	1,6	2,1	1,9	1,4

[1] Deflator of private consumption.
[2] Weighted.
[3] 1973/65.

Source: Commission services.

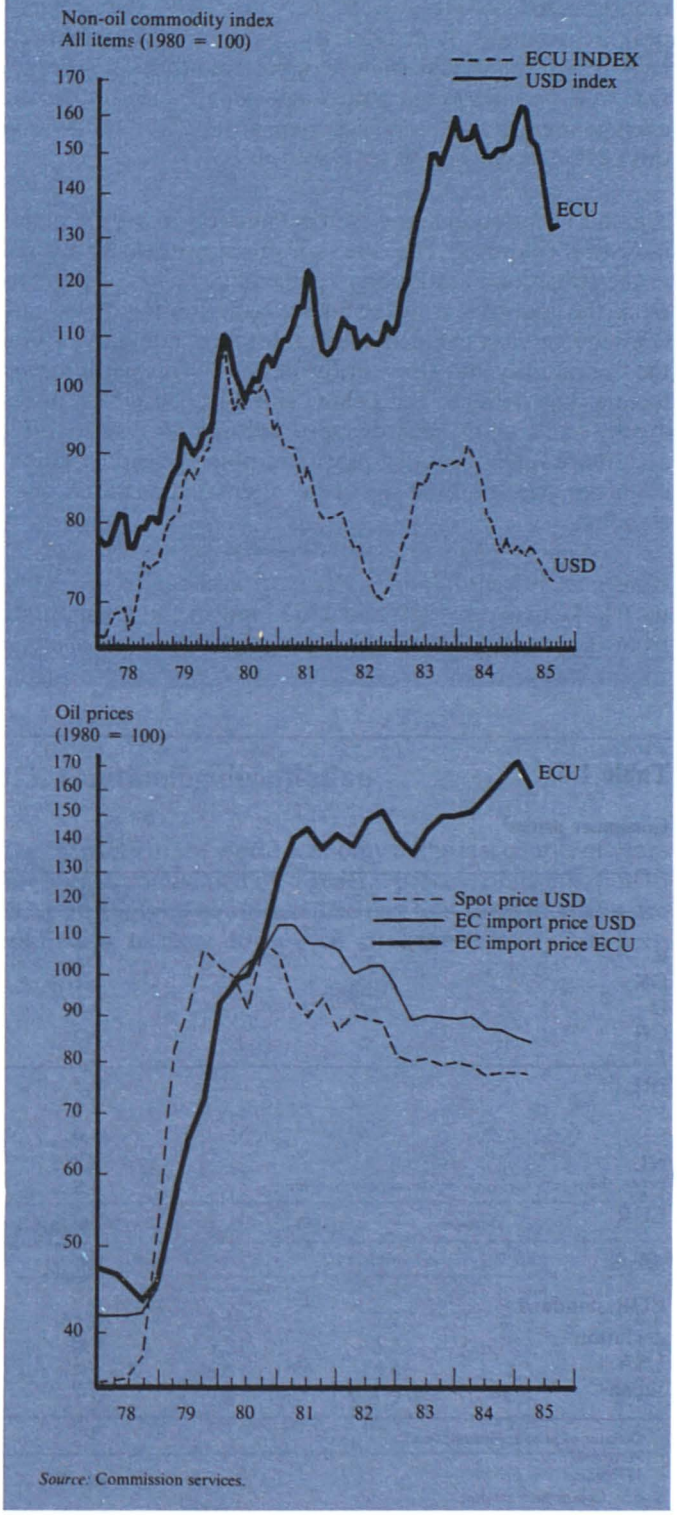
consumption; however, these structural changes on the oil markets would probably not have been brought about without adequate macroeconomic policies.

Most of the decline of oil prices from the peak reached in 1980/81 has taken place in several steps of sharp falls within a few months; the last of these steps can be located in the summer of 1985, with the oil import prices paid by the Community reaching less than USD 27 in the autumn of 1985 (Graph 1.4). Prices on the spot market, although undergoing stronger fluctuations, show a similar trend. Given the appreciation of the US dollar *vis-à-vis* the Community currencies, oil has nevertheless become considerably more expensive in Europe over the last two years. The Community's import price in ECU has risen at an annual rate of 9 % between the summer of 1983 and the autumn of 1985. This compares to an annual increase in ECU of Community export prices of manufactures over the same period of approximately 6 ½ %, which implies a significant terms-of-trade improvement for oil producers in their trade with Europe. Non-oil commodity prices in USD rose throughout 1983, but much of this increase was later reversed in 1984 and 1985. However, the annual increase of non-oil commodity prices in ECU between end 1982 and the autumn of 1985 — some 8 % — is similar to the increase in oil-prices.

Even in 1984 when world economic activity was buoyant, oil consumption increased very moderately. Given that economic growth in the industrialized countries will be lower in 1985 and 1986 and assuming that the trend towards a decreasing proportion of oil consumption to GDP continues, world oil demand is expected to decline further this year and next. With monopolistic quantity restrictions on the supply side possibly further weakening, oil prices in USD are likely to decline further. By contrast, non-oil commodity prices in USD may show some hardening next year, partly due to foreseeable reductions in supplies of some agricultural commodities, but also as a reaction to the assumed weakening of the US dollar.

Significant changes in relative prices were not confined to the prices of oil or other raw materials but have been a general feature of the disinflation process, affecting not only markets for goods and services but also those for labour and capital. Domestically, the relative prices of the productive services supplied by the different factors of production have undergone noticeable changes, entailing important adjustments in the distribution of incomes. In fact, the deflator of GDP, which measures the price of total value-added in the economy, has, in every year since 1980, risen more strongly than unit labour costs (Table 1.7). This process will probably continue next year. Domestic cost pressures thus are unlikely to stop the disinflation process in the Community in the near future.

GRAPH 1.4: Commodity prices



Source: Commission services.

Table 1.7

Deflator of GDP, of imports and unit labour costs

(% change on previous year, EUR, 1973-86)

	1981	1982	1983	1984	1985	1986
Deflator of GDP	10,6	10,1	7,8	5,7	5,1	4,1
Deflator of Imports (G + S)	15,5	7,8	4,8	8,4	4,9	−0,4
Unit Labour Costs (whole economy)	11.3	9,0	7,1	4,7	4,2	3,4

Source: Commission services.

Table 1.8

Origin of increases in final expenditure prices, EUR and USA

(Contribution in percentage points to total increase)

	Imports[1]				Unit labour costs	Indirect taxes	Other factors	Total	
	Total	*of which*[2]		*of which*					*of which*
		export prices of suppliers	nominal effective exchange rate	real exchange rate					domestic factors[3]
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
					EUR-10				
1981-83	0,9	−0,3	1,2	1,1	3,6	0,9	2,5	7,9	7,1
1984	1,1	0,0	1,1	0,9	1,6	0,5	2,1	5,3	4,4
1985	0,6	0,3	0,3	0,3	1,6	0,4	1,9	4,5	3,9
1986	−0,3	0,6	−0,9	−0,8	1,2	0,5	1,2	2,5	2,7
					USA				
1981-83	−0,3	0,6	−0,9	−0,9	3,5	0,5	2,1	5,8	6,1
1984	−0,2	0,4	−0,7	−0,6	1,2	0,1	2,1	2,6	2,8
1985	0,5	−0,1	−0,5	−0,5	2,3	0,4	0,8	2,6	3,2
1986	0,5	−0,4	0,9	0,9	1,9	0,4	1,6	4,1	3,6

[1] Excluding intra-Community trade.
[2] The breakdown of the total import price into its components is based on geometric rather than arithmetic weights. The elements therefore do not exactly sum to the total import contribution.
[3] Total, excluding the effect of export prices of suppliers and real exchange rate changes. The factors were regarded as additive.

Sources: Eurostat and Commission services. For methods used, see technical annex of *European Economy*, No 18, November 1983.

On the external side, the prospects for a reduction in inflation are improving. Community import prices for goods and services are forecast to decline by ½ % in ECU terms in 1986. This outlook is based on the assumption of a weakening US dollar and on the development of oil markets described above.

The relative inflation performance of the Community and the USA in recent years can to a large extent be ascribed to movements of exchange rates. To analyse in more detail the origins of price increases, it is convenient to concentrate on the deflator of total final expenditure at market prices (the sum of GDP at market prices and imports of goods and services). This deflator is estimated to have risen by 4,5 % in 1985 for the Community as a whole (Table 1.8, column 8). Of this increase, 0,6 percentage points are accounted for by increases in import prices (column 1), and the rest by the internal cost elements which are reflected in the GDP deflator: unit labour costs contributed 1,6 points, indirect taxes 0,4 points, and other factors, including profits and income from property, 1,9 points. In contrast to the USA, the contribution to price increases from imports has been positive in the Community in every year since 1981.

A change in import prices is either due to higher export prices of suppliers at given exchange rates, or to a change in the exchange rate at given export prices, or to a combination of both. The relevant point in the present context is the contribution to price increases from movements in real-exchange rates, which for the Community on average added about 1 percentage point per year to the increase in the total final expenditure deflator in the first half of the 1980s (column 4). The reverse holds for the USA. The change in the total final expenditure deflator less the estimated impact of the change in the real effective exchange rate yields the 'true' impact from domestic cost factors. The latter has, in fact, been much more similar for the EC and the USA than has the change in the total expenditure deflator (column 9).

2. The labour market

A favourable characteristic of the Community labour market in 1985 has been the increase, albeit modest, in the demand for labour. However, the accompanying increase in the supply of labour has prevented any substantial improvement in the unemployment rate, which has again increased slightly and is unlikely to stabilize until next year. The position of young people and women appears to have deteriorated further, and long-term unemployment seems to be on the increase. The recent slowdown in real wages growth has been maintained and is likely to continue in 1986. As a result, wages and salaries have again fallen slightly as a proportion of GDP. If a longer-term view is taken, however, the improvement in the profits trend seems to be due to the capital-deepening process brought about by distortions in factor prices. A number of factors suggest that unemployment in Europe is to a large extent the result of an excessive increase in real wages and salaries and has been aggravated by a lack of adaptability on the labour market. As the process of reducing unemployment is necessarily long, governments are compelled to pursue a two-pronged strategy: wage moderation and the pursuit of greater flexibility accompanied by special shorter-term measures aimed at specific categories of the unemployed.

2.1. Labour-market trends and prospects

The employment trend in 1984 and 1985 has exceeded the estimates given in the last annual economic review: demand for labour increased by 0,3 % in 1984 and should increase by 0,4 % this year (Table 2.1). An even greater improvement is likely in 1986, when employment is expected to increase by 0,5 %. This improvement contrasts with the job losses recorded during the period from 1973 to 1983 (0,2 % on average per year), and in particular at the beginning of this decade, although it still reflects a low elasticity of employment with respect to GDP. Most member countries have experienced a better than expected employment trend in 1984 and 1985, although only Denmark and the United Kingdom have recorded an appreciable growth in employment, which is likely to continue in 1986. In most Member States, the improvement is reflected mainly in a reversal of trend, with the losses of recent years giving way to moderate growth. In 1986, only France is likely to see a further contraction of employment.

The upturn in economic activity has led to a rise in the labour force, which has also exceeded the estimates made a year ago (Table 2.2). The labour supply has shown a relatively high cyclical elasticity: while, at the beginning of this decade, the combined effect of 'discouraged workers' and policies for regulating supply brought about a decline in the labour force and a fall in activity rates, the economic upturn seems to have put an end to that process. In 1985 the labour force should increase at a slightly faster rate than the population of working age at Community level. A particularly marked rise in the activity rate is expected in Denmark and the United Kingdom; France should be the only country in which the activity rate will continue to fall.

As a result of the simultaneous upturn in demand for and the supply of labour, the unemployment rate is not showing any real improvement (Table 2.3). Despite a fall in the level due mainly to revised statistical data (in Belgium, the Netherlands, Italy and France), the unemployment rate is

Table 2.1

Employment in the Community

	Occupied population Change as %			
	1983/73 (average)	1984	1985[1]	1986[2]
B	−0,4	0,4	0,4	0,3
DK	0,2	2,2	2,0	1,6
D	−0,7	0,0	0,6	1,3
GR	0,3	−0,2	0,8	0,1
F	0,0	−1,0	−1,0	−0,7
IRL	0,6	−0,9	−0,3	0,6
I	0,6	0,4	0,2	0,3
L	0,5	0,5	0,6	0,4
NL	−0,4	−0,5	0,4	0,6
UK	−0,5	1,5	1,1	0,9
EUR 10	−0,2	0,3	0,4	0,5

[1] Estimates.
[2] Forecasts.

Sources: Eurostat and Commission services.

Table 2.2

Labour force and population of working age in the Community

(Change as %)

	Civilian labour force				Population of working age			
	1983/1973	1984	1985[1]	1986[2]	1983/1973	1984	1985[1]	1986[2]
B	**0,7**	0,2	0,4	0,3	**0,6**	0,2	0,2	0,2
DK[3]	**1,2**	1,9	1,0	1,0	**0,5**	0,4	0,4	0,4
D	**0,1**	−0,1	0,7	0,8	**0,7**	0,6	0,5	0,5
GR	**1,6**	0,1	1,0	0,9	**1,1**	1,2	0,8	0,8
F	**0,8**	0,6	−0,1	−0,3	**0,9**	1,0	0,7	0,4
IRL	**1,5**	0,4	1,0	1,0	**(1,6)**	:	:	:
I	**1,1**	0,9	0,8	0,8	**0,7**	1,4	0,8	**0,6**
L	**0,6**	0,5	0,6	0,3	**0,5**	0,0	0,0	**0,0**
NL	**1,7**	0,8	0,1	**1,2**	**1,3**	1,2	1,0	**0,7**
UK	**0,4**	1,6	1,4	**0,6**	**0,5**	0,5	0,0	**0,1**
EUR 10	0,7	0,7	0,7	0,5	0,7	0,9	0,5	0,4

[1] Estimates.
[2] Forecasts.
[3] Total labour force.
Source: Eurostat and Commission services.

likely to increase further between 1984 and 1985, from 10,9 % to 11,1 %. It should then stabilize at that level and remain unchanged in 1986. As in recent years, the relative position of the less-favoured categories has again deteriorated. According to the latest estimates, the unemployment rate for women in 1985 will have increased more rapidly than that for men and is likely to exceed 12 % on average for the year. Similarly, the gap between the unemployment rate for the young and that for adults is likely to continue to widen. Finally, long-term unemployment is continuing to increase as a proportion of total unemployment. Although the data on this subject are not recent, they indicate a trend which will be very difficult to reverse. Between 1981 and 1983, the number of persons out of work for more than a year increased from 33 % to 47 % of the total, while more recent information covering a number of countries confirms that this trend is intensifying.

Denmark is the only member country likely to see a fall in its unemployment rate in 1985. In Belgium and the Netherlands the unemployment rate should also drop, but changes in statistics make comparisons with previous years difficult. In the other countries the improved economic climate will be reflected in 1985 in a slowdown—varying from one country to another—in the rise in unemployment. In 1986, however, unemployment is likely to fall in Denmark, Belgium, Germany, Luxembourg, the Netherlands and the United Kingdom.

Table 2.3

Unemployment rates[3]

	1973	1983	1984	1985[1]	1986[2]
B	(2,8)	14,3	14,5	13,8[4]	13,4
DK	(0,8)	10,2	9,8	9,1	8,6
D	1,0	8,4	8,4	8,4	8,0
GR	:	7,9	8,1	8,3	9,0
F	1,8	8,8	9,9	10,7	10,9
IRL	5,6	14,9	16,3	17,1	17,4
I	4,9	10,9	11,9	12,6	13,1
L	0,0	1,6	1,7	1,7	1,6
NL	3,1	14,3	14,2	13,2[4]	13,0
UK	(2,2)	11,6	11,8	12,0	11,7
EUR 10	2,4	10,4	10,9	11,1	11,1

[1] Estimates.
[2] Forecasts.
[3] Unemployed population as % of civilian labour force: Eurostat definition (for Greece, national definition and Commission staff estimates).
[4] Owing to a change in the definition of registered unemployed, 1985 and 1984 figures are not comparable.
Source: Eurostat and Commission services.

2.2. Wage costs and income distribution

The wage moderation already observed during 1984 should continue in 1985 and 1986 (Table 2.4). Thus, as was the case in 1984, a growth in real wages less than that of productivity should result in a slight reduction in the wage share in GDP; thus bringing it down to a level close to that of 1973. Developments estimated for 1985, as well as those expected for 1986, show several positive signs: a certain amount of wage moderation, a slight increase in employment and in the share of profits in GDP. Nevertheless this progress is quite modest when compared with the opposite movements registered during the previous decade.

As is shown in Table 2.4 the period which followed the first oil crisis showed the following trends: a rise in labour productivity somewhat below the growth in real wages, a slight slide in the share of profits in GDP, and a reduction in employment. Studies have additionally shown that these trends have been accompanied by increases in the capital/labour ratio in the production process.[1] The interconnection of these elements reveals the underlying process: a too rapid development of real wages has encouraged investment in rationalization. Thus the stock of capital per person has grown, as well as labour productivity, but the gains in productivity have been obtained from the suppression of jobs. At the same time profitability has declined, influencing negatively the rate of investment and growth. In this context the modest nature of the fall in the share of profits in GDP was mainly due to greater capital productivity and went hand in hand with a substantial fall in the rate of return on investment.

Table 2.4

Wage costs, productivity and income distribution[1]

Change as %

	1983/1973[2]				1984				1985				1986			
	S	W	Q	E	S	W	Q	E	S	W	Q	E	S	W	Q	E
B	0,9	3,0	2,1	−0,4	−0,4	0,9	1,3	0,4	−0,5	1,0	1,5	0,4	−1,6	−0,2	1,4	0,3
DK	−0,3	1,0	1,4	0,2	−2,4	−0,8	1,6	2,2	−0,6	−0,2	0,3	2,0	−1,3	0,2	1,6	1,6
D	−0,4	1,9	2,3	−0,7	−1,2	1,3	2,6	0,0	−0,6	1,1	1,6	0,6	−0,2	1,9	2,1	1,3
GR	1,5	3,5	2,0	0,3	−1,6	1,2	2,9	−0,2	0,5	1,6	1,1	0,8	−3,5	−2,7	0,8	0,1
F	0,7	3,0	2,3	0,0	−1,5	1,0	2,6	−1,0	−2,0	0,1	2,2	−1,0	−1,9	0,6	2,6	−0,7
IRL	0,1	3,0	3,0	0,6	−2,4	2,8	5,3	−0,9	−1,8	0,9	2,7	−0,3	−1,0	0,6	1,7	0,6
I	0,7	1,9	1,2	0,6	−0,8	1,3	2,1	0,4	−0,6	1,9	2,4	0,2	−1,5	0,9	2,4	0,3
L	2,0	2,0	−0,1	0,5	−4,1	−1,5	2,7	0,5	−0,5	0,5	1,0	0,6	−0,3	0,7	1,0	0,4
NL	−0,5	1,4	1,8	−0,4	−4,1	−1,9	2,3	−0,5	−2,6	−0,9	1,7	0,4	0,1	1,4	1,3	0,6
UK	−0,4	1,2	1,6	−0,5	0,7	1,0	0,3	1,5	−0,1	2,1	2,2	1,1	1,0	2,1	1,1	0,9
EUR 10	0,1	2,0	1,9	−0,2	−1,0	0,9	1,9	0,3	−0,9	1,0	1,9	0,4	−0,7	1,2	1,9	0,5

[1] Key:
S = adjusted share of labour income
W = real wages (deflator: GDP prices)
Q = labour productivity (GDP at constant market prices per person employed)
E = employment.

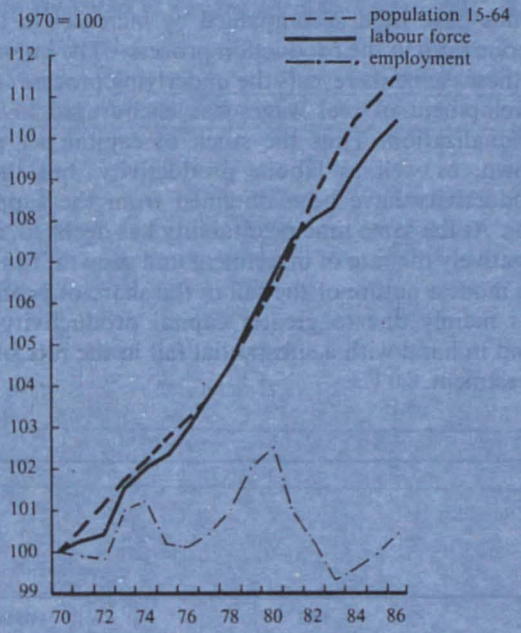
[2] Average annual change.

Source: Commission services.

However, a reversal of this trend seems to have begun since 1982 principally due to the wage moderation shown since then. Job losses were first limited and have been replaced, in 1984 and 1985 by a slight increase in employment, productivity has grown faster than real wages, the share of profits has increased in parallel with a recovery, albeit very modest, in the rate of return. There is reason to believe that this development is common to all Community countries, although with certain time-lags, in particular insofar as commitment to the adjustment process is concerned. Thus in 1985 two countries — France and Ireland — should still register a fall in employment and obtain thereby an *ex post* increase in productivity and the majority of other Member States will only record very limited rises in employment. Indeed, only in Denmark have wage developments been such

[1] See *European Economy* No 20, July 1984.

GRAPH 2.1: **Population of working age, labour force and employment in the Community**



as to permit, in the context of the recovery in activity, the achievement of an appreciable and simultaneous increase in the share of profits, of productivity and employment. It appears in consequence that in the other countries the adjustment which has begun should be continued and intensified for several years.

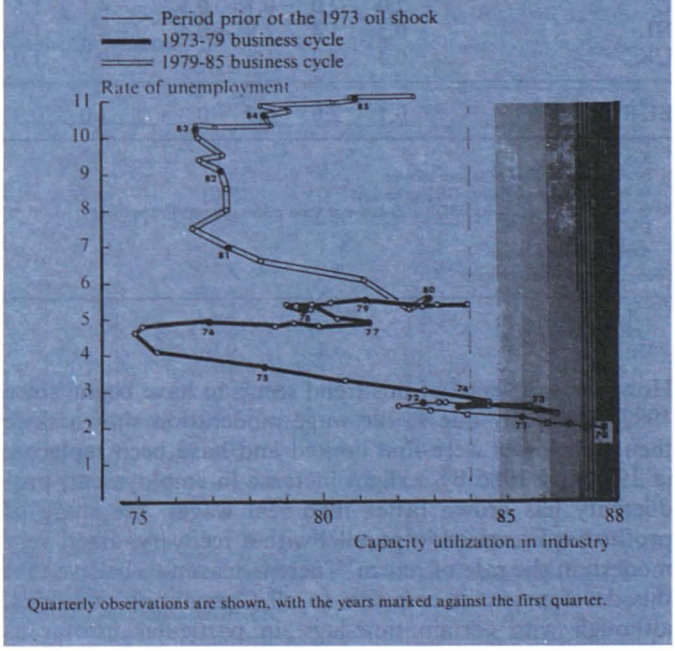
2.3. The nature of the disequilibrium on the labour market

The rise in the capital/labour ratio in conjunction with a fall in employment has made it necessary to look at the trend of relative factor prices and its role in the disequilibrium on the labour market. Although the data in this field should be interpreted with some caution, existing studies are unanimous in recording an increase in the relative price of labour in a number of European countries during the 1970s. Even on the basis of the most conservative hypotheses concerning the elasticity of substitution, there would seem to be no doubt that such a trend has contributed to the process of factor substitution by promoting rationalization.

This is confirmed by the strains affecting production capacity. As Graph 2.2 shows, despite the high and growing rate of unemployment and a still modest economic upturn, the level of capacity utilization in manufacturing industry is continuing to rise and to approach the maximum rate of operation currently possible. This may of course be explained partly by the rapid retirement of capital stock, but it is also due to types of investment which are increasing capital intensity at the expense of an expansion of production capactiy.

While the divergence of factor costs has been accentuated by the fairly widespread post-war tendency to subsidize investment, a growth in wages and salaries which has been too rapid has undoubtedly played a part too. Graph 2.3 seems to suggest that those Member States which have been most successful in controlling the rise in real wages are also those which have recorded the lowest rise in unemployment. There seems to be a close correlation between the growth in the average rate of unemployment between 1973 and 1985 (shown along the x axis) and the slowdown in the rise in real wages per employee during the same period (shown along the y axis and defined as the difference in their average growth in the periods 1960-73 and 1974-85). Clearly, this approach may have limited validity owing to its partial nature, and final conclusions cannot therefore be drawn from it. Nevertheless, it makes it possible to build up a

GRAPH 2.2: **Rate of unemployment and capacity utilization in industry in the Community**



Quarterly observations are shown, with the years marked against the first quarter.

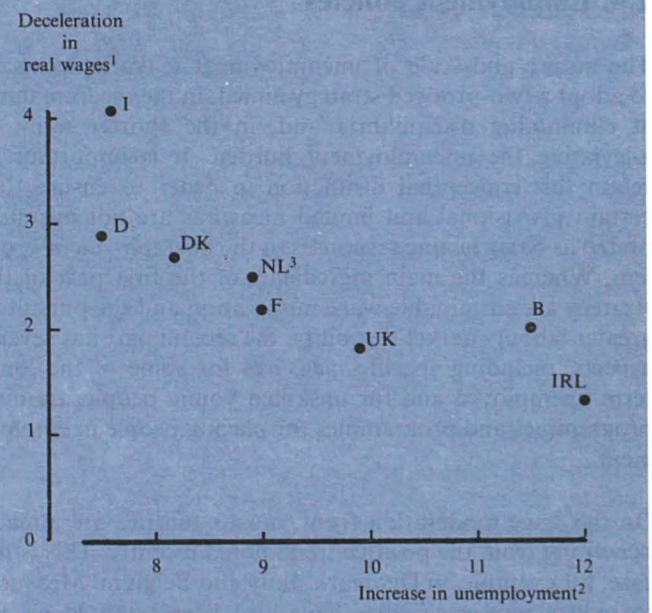
picture in which the various elements form a coherent whole. It is also interesting to note that the relative positions of the countries in the graph correspond very largely to the findings of a number of empirical studies on the rigidity of real wages in Europe and the United States.[2]

It should be added that other research carrried out by the Commission staff with a view to establishing a model for economic relationships (Compact model, see Chapter 6) seems to confirm that a major component of unemployment in Europe is due to the real wage gap. This modelling exercise introduces the concept of potential employment, which is defined as the maximum level of employment which firms are prepared to absorb assuming full use of existing capacity at the given relative factor prices. The model estimates show a considerable widening since 1973 in the gap between the labour force and potential employment and, therefore, an appreciable increase in the proportion of unemployment which is likely to persist even under boom conditions. (This category of unemployment is frequently referred to as 'classical' unemployment as opposed to cyclical or 'Keynesian' unemployment, which reflects the difference between potential and actual employment).[3]

A number of studies in this field all conclude that a substantial proportion of European unemployment is due to a too rapid growth in real wages and salaries, to reduced capital accumulation caused by the fall in profitability and to greater capital intensity. While the recent and anticipated trend in real wages, as shown in Table 2.4, points to an improved outlook, it would seem clear that wage moderation must be maintained for a number of years if the trend which has persisted for a decade is to be reversed.

A final point should be made concerning real wages and salaries. This relates to the impact of non-wage labour costs, which have tended to increase in practically all Member States and which now stand at between 20 % and 40 % of gross wage costs: This trend, like the taxation of income from employment, has created a growing gap between gross and net wages and is making wage negotiations more difficult.

GRAPH 2.3: **Unemployment and real wages**



[1] Difference between the annual average growth rate in the periods 1961-73 and 1974-85.
[2] Increase in the unemployment rate between 1973 and 1985.
[3] 1974-82. The deflator does not take account of the price of energy products.

The strictly macroeconomic view, which describes unemployment as 'classical' and/or 'Keynesian', does not, however, provide an explanation for certain aspects of the phenomenon which are not connected with real wages or with the trend of demand. The steady and uninterrupted increase in unemployment since the first oil shock, which contrasts sharply with the relative stability of the previous decade, also reflects the difficulty encountered by the European labour market in adapting, at microeconomic level, to the changes required by technological progress, to change in the demographic profile of labour supply and to the constraints imposed by slackening growth on State action in the social field. Over the last 10 years, the rise in unemployment has thus been reinforced by other factors, such as deficiencies in respect of training and conversion, lack of mobility, the existence of barriers to entry, limitations on part-time working, the bureaucratization of business management, obstacles to self-employment and the creation of new firms, excessive administrative rules and regulations (particularly in the service sector), rigidities in the organiza-

[2] See, for example, J. Sachs, *A Report on Real Wages and Unemployment in the OECD*, Brookings Paper on Economic Activity, 1, 1983; J.R. Artus, *An Empirical Evaluation of the Disequilibrium Real Wage Hypothesis*, IMF Staff Papers, 12, 1984.

[3] The results of the Compact model on the extension of Keynesian and classical unemployment are as follows:

Unemployment rate % of the civilian labour force

	73	74	75	76	77	78	79	80	81	82	83	84	85
Classical unemployment (including frictional)	2,3	2,6	3,4	4,4	4,5	4,8	5,3	5,8	6,0	7,4	8,1	8,5	9,0
Keynesian unemployment	0,1	0,3	0,9	0,5	0,8	0,6	0,2	0,3	1,9	2,2	2,2	2,3	2,1

Source: Commission Services.

tion of labour. These rigidities have generally added to the frictional/structural component of unemployment. Although it is difficult to quantify their impact, it would be wrong to underestimate their role when considering macroeconomic policies.

2.4. Employment policies

The nature and scale of unemployment make it necessary to adopt a two-pronged strategy aimed, in the medium term, at eliminating disequilibria and, in the shorter term, at alleviating the unemployment burden. It is important to retain this conceptual distinction in order to ensure that certain provisional and limited measures are not misinterpreted as being lasting responses to the unemployment problem. Whereas the main ingredients of the first part of the strategy are sustainable wage moderation and the pursuit of greater labour-market flexibility, the second part has several aspects, including specific measures for some of the long-term unemployed and for unskilled young people, training programmes and programmes for placing people in employment.

On the wage moderation front, most countries are already benefiting from the positive trend noted recently. This is the case, for example, in Denmark, Italy and Belgium. Measures to reduce non-wage costs have also been adopted or are envisaged, for example in the United Kingdom and Denmark, but the acute financial position of social security systems is at the moment restricting the scope for action in this field.

As wage trends are brought more tightly under control, greater flexibility in the wage-determination process also seems desirable. This would be facilitated if, for example, arrangements for remunerating workers which were better tailored to the situation of individual firms were devised, notably schemes for linking remuneration to a firm's results or profit-sharing schemes. Such models are not new in Europe but they centred on the ideas of worker participation in management (industrial democracy) and promotion of asset ownership for workers. Their scope has remained limited. While firms generally regarded them as a means of avoiding tax, workers did not show a particular interest in them.

The idea of profit sharing would be revived in a quite different form. The model taken is the system in Japan, where workers receive two or three times a year a bonus that may make up a significant portion of their total earnings. While being an important factor in wage bargaining, the bonus is still the most immediate and most effective way of alleviating the pressure of wage costs when this proves necessary. At the beginning of the 1980s, profit-sharing schemes were introduced in the United States in industries particularly exposed to competition and these were even granted preferential tax treatment in some states. There is no denying that such institutional innovations call for a joint effort by the two sides of industry, and especially a consensus on the need for greater flexibility.

Turning to another aspect of flexibility, the reorganization of working time, discussions between the two sides of industry are already at an advanced stage, particularly in certain Member States such as France, the Netherlands and Germany. The progress made in this connection should be emphasized. First, a growing number of workers are displaying a willingness to work shorter hours, even without any wage compensation or with only partial compensation. This is one of the initial findings of a survey carried out by the Commission departments.[4] Second, the rather simplistic assumption that a reduction in working time and a rise in employment are two sides of the same coin is now increasingly jettisoned in favour of a more rigorous approach that also looks at the period of capital utilization. The process of capital-deepening has brought about a fall in the productivity of capital. Now a reduction in working time that further undermines capital productivity will clearly be damaging to employment, investment and growth. It will provide a boost to employment only if the existing capital stock is used more intensively or its productivity increases. In other words, a reduction in working time must be accompanied by its reorganization, the aim being a longer period of utilization of plant and machinery. Consequently, over and above a national agreement, it is at the level of the individual firm that the two sides of industry must devise ways and means of ensuring that a reduction in working time has a beneficial impact on employment.

In tandem with the efforts of the two sides of industry, government action is needed to enhance flexibility by ridding legislation of a number of anachronisms and constraints hampering job creation. Not only should rules and regulations that discourage recruitment be revised, but steps should also be taken to encourage the formation of businesses, to streamline procedures and to reduce the administrative burden on firms. Several governments have already set about tackling these problems but results remain limited up to now.

Since wage moderation, a more smoothly functioning labour market, institutional innovations and greater dynamism will probably make for a lasting recovery in employment only

[4] See Supplement B — No 10 of *European Economy*, October 1985.

in the medium term, Member States are faced with the immediate need to devise measures to help employment directly. Moreover, technological progress and lengthening periods of unemployment may exclude some older workers from the employment market once and for all. Most Member States have already shown themselves to be very active on this front, bringing into effect a whole array of measures. These include, in particular, early retirement schemes, which make for a temporary contraction in the supply of labour and one way of resolving the problem posed by the lack of skills on the part of older workers. They may, however, have to be refashioned in the future to take account of the constraints that an ageing population will impose on retirement schemes.

Second, in virtually all Member States, vocational training has attracted special attention. While not disregarding workers who need to be taught new skills, it has generally focused on school-leavers and on preparing them for an occupation. It transpired that the difficulties they encountered on entering the labour market also had to do with the mismatch between the education received by them and technological change and with the fact that a 'gap' of a sort needed to be filled between the classroom and the factory. As a result, a number of countries have rightly come up with combined study-at-school/in-firm training schemes in which, in recognition of the part the private sector has to play in this field, they have asked firms to participate. Insofar as the task of vocational training is, at the moment, to rectify the mismatch between the supply of and the demand for different skills, a more thorough reform of education system is clearly needed, possibly extending down as far as primary eduction in some cases.

Lastly, programmes to assist disadvantaged categories of unemployed people, especially the long-term unemployed, have been drawn up or are being studied in a number of Member States. They provide employment, in the form of community work, for a limited period. The work schemes are identified by intermediary agencies which, in return for subsidies, take on unemployed individuals and remain responsible for the work to be carried out. Although the private sector has been asked to participate, most of the agencies are public-sector agencies. Programmes of this kind have already been launched in the United Kingdom (Community programmes), Germany ('Arbeitsbeschaffungsmaßnahmen'—ABM) and France ('Travail d'utilité collective') and are being studied in Italy.

These measures are of indisputable interest from several points of view: the target group can be clearly defined; the substitution effects can be limited provided the schemes involve work that would not otherwise be carried out; the range of goods and services available to the community can be diversified; more generally, finding employment for people who have been out of work for a long time corresponds to a fundamental social priority. It would though be a mistake to exaggerate the usefulness of such measures. This is because, by their very nature, the jobs created do not substantially improve the prospects of those concerned and are unlikely to make it easier for them to take up normal employment. The longer-term effect on unemployment may, therefore, be fairly weak, not to mention the fact that, from a strictly economic viewpoint, the value of their output is probably lower than if those same individuals were employed in the private sector. It is important to stress the temporary nature of such measures, at least where the most 'usable' individuals, notably young people, are concerned. However, even with a less depressed employment market, these measures would still be important if they were confined to particularly disadvantaged groups such as the handicapped and those in poor health.

3. Investment in the Community

The recovery in investment in the Community beginning in 1984 has continued through 1985 and should result in capital formation attaining its 1980 level during 1986. The long-term trend in investment nevertheless, gives cause for concern, with investment as a proportion of GDP declining by some four to five percentage points over the period 1970-85. More particularly the considerable decline in capital formation during 1980-83 has led to a situation in 1985 where increased output has quickly resulted in capacity utilization returning to the level of its last peak of 1979. Although the share of profits in output has recovered and wage moderation has taken place in the last three years, the rate of return on invested capital still remains low. In addition policy measures towards investment have tended to encourage the process of capital-deepening, labour-saving investment and have accentuated the decline in profitability. There is also cause for concern at a sectoral level. The investment performance in industries which have experienced relatively strong demand over the 1970-85 period (and which are more technologically orientated) has been particularly poor in the Community compared to the USA and Japan.

3.1. Investment trends

The recovery in investment which started at a Community level in 1984 has continued through 1985 at a slightly faster rate. According to the investment survey carried out in the spring of 1985 (see Table 3.1), industrial investment is expected to increase in 1985 in the Community as a whole by 16 % in current prices, corresponding to some 11 % in real terms. This is an improvement over the estimate for 1984 which indicated a rise of 7 % in real terms (12 % nominally). The strongest performers in the industrial surveys in 1984 were Denmark and the Netherlands and this has largely continued into 1985. Industrial investment was also consistently above the Community average in 1984 in the UK and to some extent Belgium while latterly, survey data indicate significant recoveries in Greece and Italy. Such

Table 3.1

Industrial investment survey — all branches

(% change in value in relation to preceding year)

Year to which data relate	1981		1982		1983		1984		1985
Date of survey	March/ April 1981	Oct Nov 1981	March/ April 1982	Oct/ Nov 1982	March April 1983	Oct/ Nov 1983	March/ April 1984	Oct/ Nov 1984	March/ April 1985
B(a)	+8	+4	−3	+10	−9	−2	+15	+13	12
DK(a)	:	:	:	+11	+11	+18	+60	+54	+40
D	+2	0	0	−2	+2	+2	+5	+4	+14
GR(a)	:	+38	−6	−19	−35	−49	+23	−1	+82
F	+5	−1	+5	+4	+6	+6	+20	+18	+13
IRL(a)	−22	−16	+54	0	−18	−24	+13	−31	+9
I	+17	+14	+6	+8	+7	+3	+11	+6	+14
L(b)	−8	+17	+24	+1	−39	+13	−22	+4	+4
NL	−2	−6	+6	−1	+11	+6	+29	+27	+24
UK(a)	−6	−11	+5	−4	+2	+2	+16	+16	+15
EUR 10(c)	+3	−1	+3	+1	+4	+3	+13	+12	+16

(a) Excluding the extractive industries.
(b) Excluding the extractive, including energy and water.
(c) Weighted total of the above (not given when data are substantially incomplete).

Source European Community business surveys

a trend in investment would mean that gross fixed capital formation (for the whole economy) in the Community would return to its 1980 level during 1986 (see Graph 3.1).

Although investment is presently increasing, the considerable drop in capital formation in the period 1980-83 (see Graph 3.1) has meant that capacity utilization is already, in the third quarter of 1985, back to the level of the last peak in 1979 (82,5 % in the Community), see Table 3.2. Evidence suggests that capacity utilization is particularly high relative to normal levels in Denmark and the Netherlands, and this despite fairly substantial investment growth in these countries, of late. The poor investment performance in the early 1980s would not be quite so alarming particularly for employment prospects if it reflected the choice by firms of less capital intensive technology, a partial undoing of the earlier period of capital deepening. The fact that capacity utilization levels have recently become quite high lends support to the hypothesis that not only has capital decumulation taken place but that there has been no real reversal of the capital-deepening process. Graph 3.1 shows, for example that despite the recovery in GDP from 1983 and investment from 1984 onwards, the number of employees in manufacturing continues to decline and is only expected to stabilize in 1986.

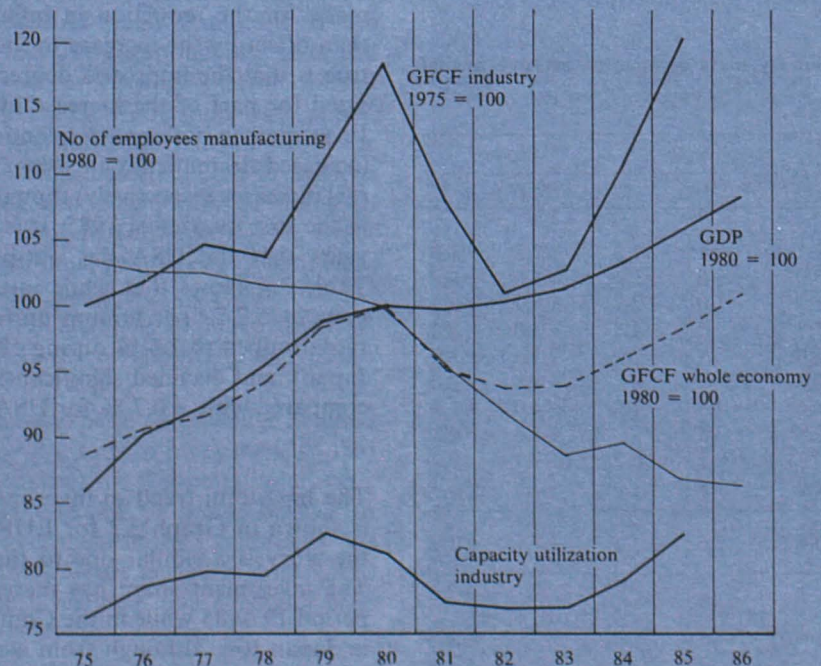
Table 3.2

Capacity utilization

	Capacity utilization rates as %				1984/83 growth rates
	Last high point 1979-80	1983	1984	July 1985	Industrial output
B	79,1	75,7	76,1	78,2	5,3
D	86,0	77,0	80,3	85,0	3,0
F	85,3	81,6	81,9	83,1	3,1
IRL	68,1	58,1	61,5	72,7	13,1
I	77,3	70,1	71,9	74,3	3,1
L	83,0	70,7	77,7	82,6	—
NL	83,0	79,5	82,4	84,0	5,2
UK	87,6	76,7	82,4	87,4	0,9
EUR 8	83,9	77,2	79,9	82,5	2,8

Source: European Economy, Supplement B, No 8/9, August/September 1985, and Commission departments.

GRAPH 3.1: **Trend in industrial investment—European Community**



A breakdown between investment in plant and machinery, and construction is given in Table 3.3. The decline in equipment (− 1,6 % annual average) and construction (− 3,7 %) capital formation during the period 1980-83 has been followed by respective recoveries of 4,1 % and 0,9 % for 1983 through 1985. The increase in equipment investment is particularly marked in Denmark (+ 15,0 %), Belgium (+ 9,5 %) and the Netherlands (+ 7,3 %) while substantial improvements have taken place in the UK (+ 5,5 %) and Germany (+ 5,2 %). With respect to the UK it is possible that measures announced in the March 1984 budget involving a gradual decline in investment depreciation allowances (see section 3.3) over a three-year period has led to a bringing forward of investment plans. UK survey data indicate that investment in the financial year 1984/85 was higher than expected from the April 1984 survey, but clearly this is not necessarily attributable to the budget measures.

Both Denmark (+ 8,9 %) and the UK (+ 5,4 %) have also experienced substantial increases in construction while some countries have merely seen an ending of the considerable decline in this sector during the 1980-83 period. For example Belgium, as a result of fiscal incentives, has experienced a turnaround from − 11,3 % (1980-83 annual average) to + 1,0 % (1983-85 annual average) while the decline in the Netherlands has similarly been arrested (from − 6,7 % to 0 %).

Table 3.3

Gross fixed capital formation by main component average annual growth rates

	1980/70		1983/80		1985/83	
	PM[1]	C[1]	PM[1]	C[1]	PM[1]	C[1]
B	+ 2,1	+ 2,1	− 1,1	− 11,3	+ 9,5	+ 1,0
DK	+ 2,2	− 2,0	+ 3,0	− 7,6	+ 15,0	+ 8,9
D	+ 2,5	+ 1,1	− 1,0	− 2,7	+ 5,2	+ 0,2
GR	+ 4,2	+ 1,3	− 2,3	− 4,8	+ 3,0	− 2,4
F	+ 4,9	+ 1,0	− 0,1	− 2,0	+ 1,4	− 3,9
IRL	+ 6,4	+ 5,3	—	—	+ 1,8	− 2,6
I	+ 3,8	− 0,6	− 4,6	− 1,5	+ 4,0	+ 1,5
L	+ 3,1	+ 2,8	—	—	+ 3,8	− 2,1
NL	+ 1,3	0	− 1,5	− 6,7	+ 7,3	0
UK	+ 2,2	− 1,2	− 1,6	+ 1,6	+ 5,5	+ 5,4
EUR 10	+ 3,1	+ 0,4	− 1,6	− 3,7	+ 4,1	+ 0,9

[1] PM = plant and machinery
C = construction.

Note: Share in gross fixed capital formation is as follows:
1970 PM 36.5% C 61.2%
1985 PM 44.3% C 50.2%

Source: Eurostat + Commission services.

Despite the recent improved investment situation in the Community the performance over the last 15 years is rather depressing. For many Community countries investment as a proportion of GDP reached an historical low-point in 1983, although for some (France, Ireland and Greece) this ratio still appears to be declining. Only in countries where the investment performance has been reasonably strong of late (e.g. Denmark, the UK, Germany) has this investment ratio remained on a par with that in 1980, and is even here still significantly below that of 1970. This apparent long-term decline in the investment ratio (all economic sectors) for Community countries is demonstrated in Table 3.4 which shows that the Community average has dropped from 24,0 % to 19,5 %. In Japan the investment share has fallen from 34,5 % (1970) to an estimated 30,6 % in 1985. In the USA where the investment performance has been particularly strong since 1983 the ratio for 1985 (20,7 %) stands above that for 1970 (19,5 %). Capital formation in the USA is estimated to have increased at an impressive 12,2 % in annual terms over the period 1983-85 and while the generous depreciation allowances instituted in 1980 have contributed to this rise another major reason has been the sizeable growth in output. It is clearly not too easy to distinguish between the effect on investment due to investment incentives and that due to output or accelerator effects (see also later for a discussion of profitability). The improved investment depreciation allowances instituted in the USA in 1982 and rescinded slightly in 1983 lowered user cost by about 1 ½ percentage points for equipment and about two-thirds of a point for structures, although if allowance is made for the reduction in inflation this lowering is more than offset by the increase in the real cost of debt. What is true is that the improved depreciation allowances compensated for part of the increase in interest rates in the USA. Investment in both non-residential structures and equipment increased dramatically in 1984 (15,6 % and 21,5 % annual real increases respectively) though the latter began to decline in the first quarter of 1985. It is not just over the last three years that the USA has out-performed the Community. Table 3.4 shows that while investment in the Community grew at 5,7 % per annum during the period 1960-70, the rate dropped to 1,6 % during 1970-80 (below the USA and Japan), and declined significantly during 1980-83, − 2,0 % compared with + 0,7 % for USA and + 1,9 % for Japan.

The long-term trend in investment share for industry only is shown in Graph 3.2 for EUR 7, USA and Japan. Here the story is a similar one to that for the whole economy. The investment share has increased in the USA over the period 1970-85 while in the Community it has declined, and in Japan too, although from a much higher level. A more structural analysis of investment demonstrates that industrial sectors have not been equally affected by this slowdown

Table 3.4

Investment trends by country[1]

	Investment as % of GDP			Rate of change of investment			
	1970	1980	1985	1970/60	1980/70	1983/80	1985/83
B	23,4	21,3	17,3	5,8	2,2	−8,1	4,4
DK	25,4	18,8	18,5	7,0	−0,7	−4,2	11,7
D	25,7	22,8	21,1	4,5	1,6	−2,0	1,6
GR	29,2	24,2	19,6	9,3	2,8	−3,6	−2,9
F	23,5	21,9	19,5	7,8	2,9	−1,2	−1,1
IRL	25,8	28,7	23,6	9,8	5,6	−2,3	−0,4
I	24,1	19,8	18,7	5,1	1,1	−3,3	4,0
L	27,0	26,2	21,4	3,5	2,8	−7,1	0,0
NL	26,9	21,0	18,8	6,8	0,4	−4,9	2,9
UK	21,0	18,0	18,7	5,1	0,4	0,6	5,2
EUR 10	24,0	21,0	19,5	5,7	1,6	−2,0	2,2
USA	19,5	18,5	20,7	4,1	2,4	0,7	12,2
Japan	34,5	32,0	30,6	15,5	4,1	1,9	5,4

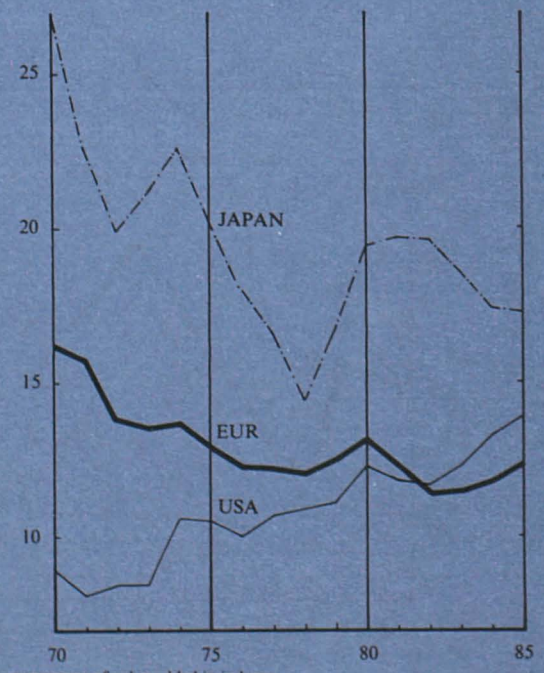
[1] Total economy.
Source: Commission services.

in investment. Graph 3.3 shows the evolution of investment in the Community for sectors which have globally (i.e. for the US, Japanese and Community economies combined) experienced strong, medium and weak demand over the period 1973-82.[1] The first sectoral group includes electrical goods and electronics, data processing, pharmaceutical products and chemicals, the second, food industries, paper, transport, rubber, plastic and industrial machines and the third textiles, steel, and building materials. It is in the first sectoral group, where there is generally a high technological content in goods, that the poor performance of the Community is most marked. The annual growth of capital formation for the whole of industry was 4,5 % points below that of the USA and 3,7 points less than Japan but for the high demand sector the shortfall was 6,6 points and 6 points respectively.

The group of sectors that have experienced average demand have followed a similar growth path of investment to that of the USA and Japan except that the Community has been more adversely affected by the second oil shock. Finally for the weak demand sectors investment in the Community has declined continually over the 1973-82 period in contrast to the USA and Japan where investment has generally been maintained.

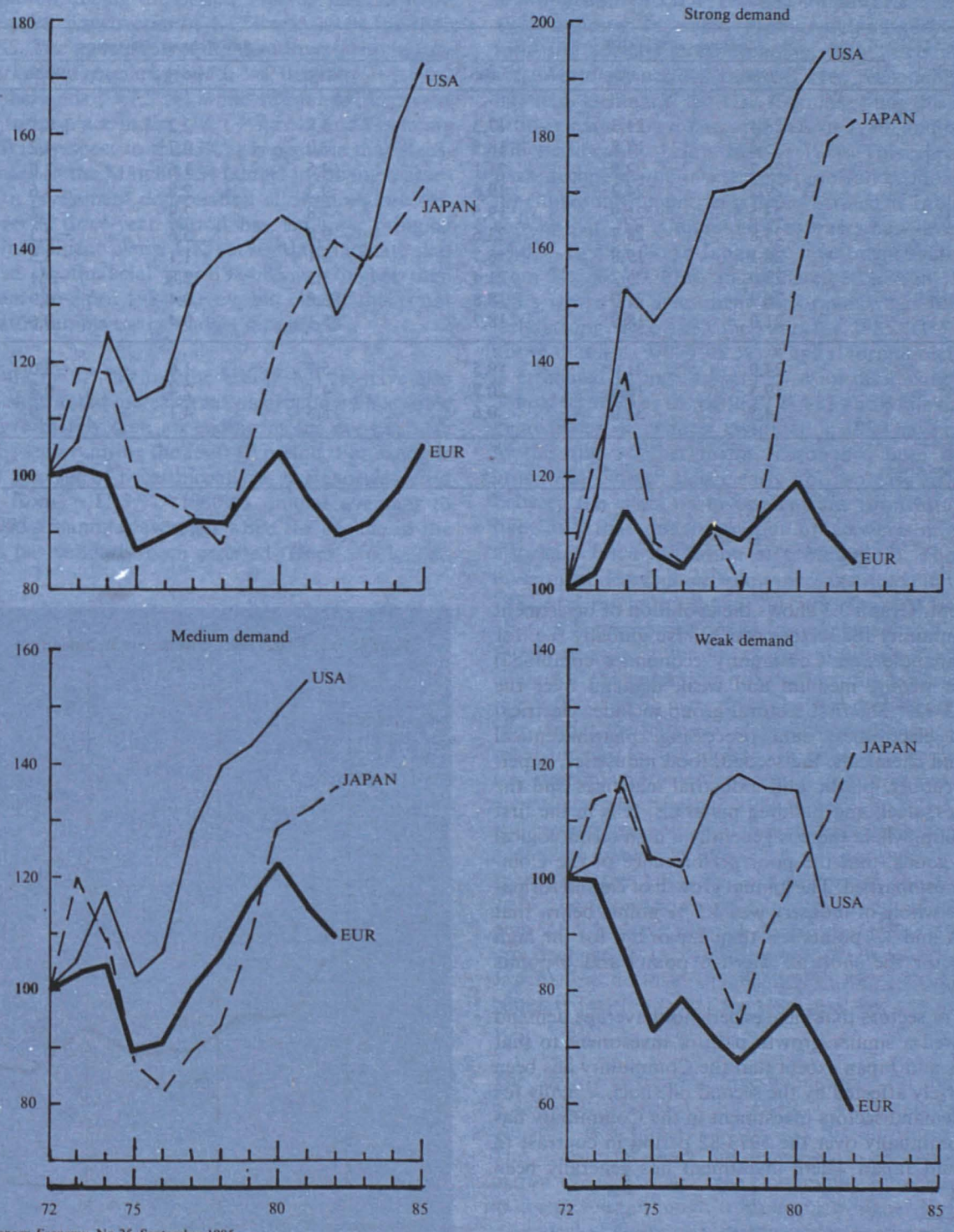
[1] A more detailed analysis is contained in Chapter 2 of *European Economy* No 25, September 1985.

GRAPH 3.2: **Gross fixed investment in industry** [1]



[1] As a percentage of value added in industry.
Source: European Economy No 25, September 1985.

GRAPH 3.3: **Trend in gross fixed capital formation for industry (1975 prices)**



Source: European Economy, No 25, September 1985.

The level of investment, therefore, in the Community seems not only insufficient but gives cause for concern at a sectoral level. The sectors benefiting from a fast growth of demand represent 40 % of value-added by industry in Japan and 31 % in the USA, in contrast to only 26 % in the Community, and it is these sectors in particular in the Community which have experienced a high rate of import penetration during the period 1973-82. Insufficient investment has therefore created a situation where capacity has become inadequate to respond to internal and external demand.

3.2. Investment, wages and profits

There are a number of factors that affect aggregate investment performance, the most important being changes in demand or output and expectations about future demand, changes in profits or company liquidity and interest rates, and lastly tax changes in the corporate sector. These factors link together to influence expected future profitability and in turn investment affects output.

Tables 3.5 and 3.6 demonstrate the long-term decline in the rate of return on invested capital in the Community. The gross rate of return (see table for definition) averaged nearly 11 % in the period 1960-73 but has subsequently declined to about 6 ½ %. A sharp fall occurred between 1973 and 1975 and although a recovery of profitability took place in the second half of the 1970s, the second oil shock precipitated a further decline. A similar profile has occurred in the USA but there the decline has been less severe.

Although the gross operating surplus of the business sector fell sharply in relation to gross value-added in the mid-1970s, the steady subsequent recovery has resulted in the share of gross profit in value added returning to its 1960 level. With the profit share remaining fairly stable but the rate of return falling, the implication is that the capital output ratio has increased and the efficiency of capital declined. There are clearly problems associated with working with capital stock and profitability data but evidence suggests that capital intensity has increased much more in Europe than the USA and this is an important reason for the divergence of rates of return (see Graph 10 of the report).

While the return on capital tended to fall appreciably from 1960 to 1985 in the Community, real wage costs (compensation per employee deflated by the GDP deflator) increased on average by 4,4 % per year from 1960 to 1973 and by a further 2,3 % per year on average from 1974 to 1981. Since 1982, the rate of increase has moderated somewhat to less than 1 % on average (see Table 3.7 and Graph 11/12 of the report). The variation between Member States in recent years has been quite strong; the rise in real wage costs between 1981 and 1985 ranged from −0,4 % in the Netherlands to +2,2 % in the United Kingdom, the latter being the only country where the average rate of increase for 1981 to 1985 was higher than that for the period 1973 to 1981.

Table 3.5

Gross rate of return on invested capital enterprises excluding housing[1] — (capital stock at replacement cost)

	B	D	F	I	NL	UK	EUR 10[2]	USA
1960-73	10,6	11,6	13,1	8,3	11,6	9,2	10,8	10,2
1974	10,3	9,1	11,4	6,5	10,1	5,9	8,6	8,6
1975	8,6	8,6	9,6	4,2	8,7	5,0	7,3	8,4
1976	8,1	9,6	9,0	4,9	10,1	6,3	7,8	8,8
1977	7,7	9,6	8,8	4,3	9,8	6,9	7,9	9,3
1978	7,5	10,0	8,7	4,5	9,6	7,1	8,0	9,1
1979	7,5	10,3	8,4	5,7	9,0	6,2	8,0	9,1
1980	6,9	9,4	7,3	6,2	8,6	5,3	7,3	8,3
1981	6,0	8,8	6,2	4,3	8,9	4,9	6,5	8,3
1982	6,1	9,1	6,1	4,0	8,7	5,0	6,5	7,4
1983	6,4	9,3	6,2	3,7	8,7	5,3	6,6	7,5
1984	6,5	9,3	6,3	3,8	9,3	5,0	6,6	7,8

[1] Gross operating surplus as % of gross capital stock, adjusted for the imputed labour income of employees.
[2] Weighted with GDP at 1975 purchasing power parities.

Source: DIW on behalf of the Ministry of Economic Affairs (EC average and estimates for 1983 and 1984 Commission services).

Table 3.6

Net rate of return on the gross capital stock[1]

	B	D	F	I	NL	UK	EUR 6[2]	USA
1960-73	6,7	7,4	9,9	4,8	6,5	5,2	6,9	6,2
1974	6,5	4,7	7,4	2,5	5,0	1,4	4,3	4,6
1975	4,7	4,4	6,3	0,2	3,6	0,9	3,3	4,4
1976	4,5	5,1	5,1	0,9	5,0	2,2	3,7	4,8
1977	4,0	5,4	4,9	0,3	6,6	2,7	3,8	5,3
1978	4,0	5,6	4,6	0,5	6,4	2,7	3,8	5,2
1979	3,7	6,0	4,4	1,8	5,7	1,5	3,8	4,8
1980	2,2	5,3	3,1	2,2	4,8	0,4	3,0	4,2
1981	1,7	4,9	3,3	0,5	4,2	0,1	2,5	4,1
1982	2,1	4,6	2,1	0,2	4,7	1,0	2,3	3,4
1983	2,4	4,7	2,1	−0,1	4,8	1,1	2,4	3,6
1984	2,4	4,8	2,2	0	5,4	1,0	2,4	3,7

[1] Net operating surplus, excluding estimated labour income of the self-employed as a percentage of the gross capital stock.
[2] Weighted with GDP at 1975 purchasing power parities.
Source: DIW on behalf of the Ministry of Economic Affairs (EC average and estimates for 1983 and 1984 Commission services).

Furthermore, throughout the period 1960 to 1981, the rise in real per capita wage costs in the Community exceeded the increase in labour productivity adjusted for rationalization effects.[2] The difference between the rise in wage costs and adjusted labour productivity was 0,9 percentage points on average for the period 1961-73 and 1,1 percentage points for the period 1974-81 (see Table 3.6). Only since 1982 has the increase in real wage costs (0,9 %) been slightly less than that of adjusted labour productivity (estimated to be 1,2 %). The divergence between wage costs and productivity during the period 1961-73 and the lack of adjustment after the first oil shock, which resulted in a worsening of the gap between wages and productivity, served to encourage the increase in the capital-labour ratio at a rate which was greater than its normal trend increase. This has meant that capital intensity has increased, that profitability has declined and that the lack of real wage adjustment has intensified the unemployment problem.

Developments since 1981 with respect to wages represent a major change of trend, and one which is likely to have its first effects on employment in the Community from 1985 (when total employment should increase, for the first time since 1980, and by 0,2 %). As real wages have increased less rapidly than the estimated rate of increase in adjusted labour productivity, firms are less compelled now to rationalize production and may allocate a greater proportion of investment to increase capacity (and employment), provided that demand expectations are also favourable.

However, despite the rise in the share of profits in national income, the rate of return on invested capital is still low and

[2] Labour productivity less the estimated impact of the increase in the capital stock per employee due to the rationalization of production, particularly through the elimination of the least productive firms and jobs.

Table 3.7

Change in real wage costs and in labour productivity adjusted for the effects of rationalization

(% change)

	1961-73	1974-81	1982-85
European Community			
Real per capital compensation of employees[1]	4,4	2,3	0,9
Adjusted labour productivity[2]	3,5	1,2	1,2
Wage costs/productivity gap[3]	0,9	1,1	−0,3
United States			
Real per capital compensation of employees[1]	2,1	0,5	1,6
Adjusted labour productivity[2]	1,8	0,5	1,3
Wage costs/productivity gap[3]	0,3	0,0	0,3

[1] Deflated by GDP deflator.
[2] Change in output per person employed less impact of the change in per capita capital stock.
[3] Difference between the growth of real per capita compensation and the growth of adjusted labour productivity. Since under certain assumptions the rise in per capita compensation may exceed the growth of adjusted labour productivity this figure should only be considered as a broad indicator of the trend.
Source: Eurostat and Commission services.

indeed, inadequate to bring about a satisfactory growth of employment in the Community. The problem of uncertainty over expected future profitability in Community economies is further exacerbated by the level of interest rates. Since 1979, there has been a sharp rise in real interest rates affecting not only the general changeover to more stability-orientated monetary policies but also the impact of very high interest rate levels in the US. This has imposed a considerable burden on the structure of firms' balance sheets and may have led, in particular, to cuts in programmes to extend capacity, in order to restrict the use of borrowed capital — net borrowing by enterprises has declined substantially since 1980. Thus, despite the relatively marked increase in gross operating surplus in relation to the gross value added of companies in recent years, the level of investment in relation to value-added, even in 1985 will remain below that recorded during the last cyclical upturn in 1979-80.

In conclusion, therefore, the outlook for investment and consequently output and employment is disquieting. Although profitability has improved, wage moderation has occurred in a number of countries and capacity utilization has risen markedly, rates of return are still low, particularly relative to real interest rates. Other demand components have contributed to low aggregate demand and uncertainty about future growth. Private consumption has temporarily grown very modestly following the effects of wage moderation and the growth of public consumption has been halted by budgetary consolidation policies. Finally, while exports have received a significant stimulus in the last two years from high US growth, uncertainty about the continuing strength of the dollar and the US recovery have made investors in Europe more cautious about expanding capacity.

3.3. Policy towards investment

All Member States have to varying extents in the past attempted to encourage investment. If anything, these attempts have multiplied in the recent five to 10-year period, and certainly the means used to encourage investment have become more elaborate. Direct grants and subsidized loans have been increasingly supplemented with a mixture of loan guarantees, participation schemes, depreciation allowances and other tax measures. Some of the traditional types of investment incentive, such as support for research and development or regional policy, have been justified in the past by externality considerations and by market imperfections (such as the immobility of labour). More recently, the desire to protect or to ease the adjustment of industries (such as steel, coal, shipbuilding) which have been faced with low demand and/or increased competition from newly industrialising countries has led to further subsidies both to these sectors and to ones which will hopefully provide future employment growth.

Why is it, therefore, that the investment incentives used have not only failed substantially to create employment but have not even had the desired effect on either the size or type of investment itself. Firstly, it is important to recall the factors which influence investment (mentioned already in section 3.2) and which include both price and income (or output) effects. Investment incentives clearly, *a priori*, lower the price of capital (and therefore both encourage the formation of capital and its substitution for labour), but other factors also influence the expected user cost of capital, including expected interest and inflation rates and taxation. Furthermore, capital formation is strongly influenced by expected demand which has hardly been helped by two oil shocks, inflation and more recently policies to control the latter.

While investment incentives may, therefore, have helped to offset the negative influences on capital formation caused by weak demand expectations and high interest rates, by reducing the cost of capital they have further aggravated the distortion in relative factor prices (between labour and capital) and contributed to the decline in profitability discussed in section 3.2. The implication, therefore, is that the capital-labour ratio has risen above its long-run evolutionary path with respect to output per employee. The fact that three European countries, the UK, France and the Netherlands, plus the USA are in the process of substituting lower corporate tax rates for accelerated depreciation allowances seems to be indicative of the desire to adopt a more neutral[3] approach and reduce the subsidy to capital which has existed. In the UK, the accelerated depreciation allowances for equipment (100 % first year plus interest allowance) were reformed in the 1984 budget and replaced by a 25 % reducing balance method, introduced gradually so as to come into force in 1986/87, (see Table 3.9 for details). At the same time corporation tax is being reduced in stages from 52 % to 30 %. In France, where the tax allowance or credit (10 % of investment up to 1981 and 15 % in 1982) was replaced in 1983 by a special depreciation allowance, similar changes have recently been announced. After 1985, when the present system ends, the extra first year depreciation allowances (which have been up to 70 %) will be replaced by a corporate tax cut from 50 % to 45 %. Finally, in the USA, where 'accelerated cost recovery' was introduced

[3] Neutrality requires that the economic depreciation of fixed assets is tax deductible, interest costs likewise (alternatively, there may be 100 % immediate depreciation and no allowance for interest payments), that capital gains are taxed at the same rate as income and that allowance is made for inflation.

in 1981 by reducing writing-off times for assets, certain reforms have already been proposed. This package of proposals includes the repeal of investment credit (5 or 10 % of new investment can at present be set against tax), the reduction of the corporate tax rate from 46 % to 33 %, interest deductibility only for the 'real' part of interest costs and a change to a 'real recovery cost system' where depreciation periods correspond more closely to economic lifetimes and where account is also taken of the inflation rate.

Although a reassessment of special depreciation allowances is taking place, the process has not yet substantially begun for more direct forms of investment incentive. Of the other two main types of incentive, interest rate subsidies and grants, the former appear to be much more widespread in France, Belgium and Italy, while the latter are more common in the UK, Ireland and to some extent Germany. In the Netherlands the situation is rather particular and is governed by the Investment Account Act (WIR) of 1978 which instituted a system of investment subsidies based on tax credits, and which may involve a negative tax if the credit is greater than the tax due (the latter is to be abolished according to the 1986 budget proposal). The subsidy is based on the value of investment beyond a certain floor and the allowable subsidy may be extended for small companies or for energy and environment projects. This type of discrimination is a trait which exists in many Member States. In Italy special funds are allocated to small companies, innovation and restructuring, while France gives interest subsidies for certain activities such as innovation, exports and energy projects. In Belgium there have been special tax measures for research and development and energy projects, while Germany accords extra accelerated depreciation allowances for environment and energy, small companies and special regions, particularly West Berlin. The UK has likewise given grants for a series of innovation fields and also for energy conversion. Small companies have been encouraged through tax measures.

Table 3.8 lists some of the more important grant and interest rate subsidy measures in Community countries as well as the structure of corporate tax and depreciation measures.

Table 3.8

Corporate taxes, tax depreciation allowances and investment grants in Member States

	Corporate tax rates	Tax depreciation allowance system		Carry-forward and carry-back of losses		Other principle financial incentives to investment
		Equipment and plant	Buildings	Carry-forward	Carry-back	
B	— standard rate = 45% — progressive rates of 31-45% for profits up to BFR 14.4 million — double taxation of dividends reduced to half the standard rate through tax credit	— straight-line or declining balance (multiplier = 2) — 1982 basic investment allowance 13% (25 or 18% in some cases)	— straight line 5% p.a.	5	0	— interest-rate subsidies — guaranteed loans — grants — temporary tax deductions for certain investment
DK	— standard rate = 40% moving to 50% in 1986/87 — for cooperatives: 16% at present will be raised to 20% — existing double taxation of dividends will be abolished from 1990 — tax-free investment reserves of up to 25% of annual taxable profits equivalent to an advance allowance for investment before purchase	— 30% of aggregate book value	— industrial buildings: — straight line rate 6% p.a. for 10 years then 2% p.a. — other buildings: straight line rate 4% p.a. for 10 years then 1% p.a. — no allowance for office space and housing	5	0	— investment grants — soft loans — regional aid for purchase of industrial land and building

Table 3.8 *(continued)*

Corporate taxes, tax depreciation allowances and investment grants in Member States

	Corporate tax rates	Tax depreciation allowance system		Carry-forward and carry-back of losses		Other principle financial incentives to investment
		Equipment and plant	Buildings	Carry-forward	Carry-back	
D	— standard rate = 56% distributed profits = 36%	— straight-line or — declining balance multiplier 3 with maximum rates of 30%, average life-times 4-10 years — special allowances for small companies	— old buildings, straight-line 2% p.a. or declining balance 12 × 3,5%, 20 × 2%, 18 × 1% — new buildings, straight-line 4% p.a. or declining balance 4 × 10%, 3 × 5%, 18 × 2,5%	5	2	— investment grants — special depreciation allowances for certain sectors and regions
F	— standard rate 50%; no reduced rates for SME — double taxation of dividends reduced to half the standard rate through tax credit — carry back of losses instituted in 1985 — tax credit for the take-over of enterprises by employees	— up to 75% allowance in first year for 1984 and 1985 — this higher depreciation rate (usually 40%) will be abolished at end of 1985 and corporate tax rate will be reduced to 45%	— straight line 5% p.a.	5	3	— subsidised loans — grants — extra depreciation allowances
IRL	— standard rate = 50% — reduced rate of 10% for manufacturing, replacing former system of tax exemptions for export profits — reduced rate of 40% to 5p% for profits up to IRL 35 000 — double taxation of dividends reduced to less than half the standard rate through tax credit	— free depreciation allowance up to 100% in the first year, since 1972	— free depreciation allowance up to 100% in the first year since 1978 — no allowances for office space and dwellings		0	— investment grants — tax relief — grants for product development and feasibility studies
I	— standard rates state 36% + local = 16.2% = effective rate 46%, lower rates for profits reinvested in the Mezzogiorno — no reduced rates for SME, but reductions for certain categories, eg cooperatives — no double taxation of dividends	— straight-line, but advance allowances of 3 × 15% in addition to normal rates	— normal straight-line rates 3.8% p.a. — same advance allowances as for equipment	5	0	— subsidized loans SME — repayable grants and subsidized loans for innovation — subsidies for restructuring

Table 3.8 *(continued)*

Corporate taxes, tax depreciation allowances and investment grants in Member States

	Corporate tax rates	Tax depreciation allowance system		Carry-forward and carry-back of losses		Other principle financial incentives to investment
		Equipment and plant	Buildings	Carry-forward	Carry-back	
L	— standard rate = 40% — full double taxation of dividends	— straight-line or — declining balance multiplier = 2	— straight-line 3% p.a.	5	0	— investment grants
NL	— standard rate 43%, (42% in 1986) — full double taxation of distributed profits	— straight line or — declining balance multiplier (2-2,5), max. rate 25% — 1978 WIR scheme	— straight-line 2 to 4% p.a.	8	2	— Investment grants and tax credits through Investment Account Act 1978
UK	— standard rate progressively reduced 1983/84 = 50%, 1984/85 = 45%, 1985/85 = 40%, 1986/87 = 35% — reduced rate of 30% for profits less than UKL 100 000 (in 1983/84) progressive rates for profits between UKL 100 000 and UKL 500 000	— first year allowances 1984/85 75%, 1985/86 50%, 1986/87 reverts to 25% declining balance	— normal straight-line rate 4% p.a. first year allowance 1984/85 50%, 1985/86 25%, 1986/87 reverts to 4%		1	— investment grants, regional, discretionary and for certain sectors — tax allowances for expansion of companies

Corporate tax rates vary between 35 % (the UK from 1986/87 onwards) and 56 % (for Germany, although distributed profits are taxed at 36 %). Several countries have reduced tax rates for small companies (Belgium, Ireland, Luxembourg, the Netherlands and the UK). Most countries have accelerated depreciation schemes for plant and equipment but only a few (Germany and Ireland) for buildings. There are a mixture of carry-back, carry-forward arrangements for losses, with the most common being five years carry-forward and no carry-back.[4]

Table 3.9 shows the evolution of central government investment grants in the Community, as defined by the European System of Accounts. Investment grants consist of unrequited transfers by general government for the purpose of financing, in whole or in part, specific items of gross fixed capital formation by other institutions. The definition includes all sectors of the economy, but does not include tax relief measures to encourage investment, nor does it include grants for interest relief. Statistics in the table, therefore, omit two of the important measures which are used to stimulate investment.

This omission makes any inter-country comparison very difficult. For example France has a much lower level of investment grants relative to Germany or the UK because a much higher proportion of investment stimulation is accorded via interest rate subsidies. Interpretation is also difficult because any change in balance between the three main policy measures effects the evolution of investment grants relative to GDP for any particular country. The significant fall in investment grants in the UK from 1972 onwards was in a large part due to the introduction and substitution of 100 % first year depreciation allowances for other more direct policy measures.

Nevertheless the table shows the significant subsidy that investment grants have made towards gross fixed capital

[4] A proposition concerning the harmonization of Member State legislation regarding the carry-over of losses is being considered by the Council, COM(84) 405. It consists of a system of two years carry-back and unlimited carrying-forward of losses.

formation. For Belgium, Germany, Italy and the UK, grants as a percentage of capital formation were in the range 5,7 % to 6,9 % in 1982, but for Ireland, the Netherlands and Luxembourg the proportion is much higher. Tentative estimates for France, Germany and the UK indicate that the budgetary cost of grants, interest-rate subsidies and accelerated depreciation allowances in the industry and service sector as a proportion of GDP was as high as 1,9 %, 1,4 % and 2,3 % respectively in 1983.

In conclusion, therefore, investment incentives do not appear to have been particularly successful in offsetting, in aggregate terms, the negative influences on capital formation caused by poor demand expectations. Furthermore, they have contributed to the distortion of factor prices (and therefore artificially increased the capital intensity of net investment) with the result that profitability and employment creation has been poor.

Table 3.9

General government investment grants to other resident sectors

	B	DK	D	F	IRL	I	L	NL	UK
					as % of GDP				
1970	0,5	0,4	0,5	0,6	2,5	1,4	2,0	0,8	1,5
1974	1,0	0,3	1,1	0,5	2,0	0,8	1,8	0,7	1,2
1975	0,9	0,5	1,1	0,7	2,0	1,0	2,6	0,8	1,2
1976	1,0	0,5	1,15	1,1	2,1	1,0	2,3	0,9	1,2
1977	1.0	0,5	1,4	0,5	2,1	1,2	2,0	0,8	1,1
1978	1,1	0,5	1,3	0,4	2,2	1,1	1,7	0,9	1,2
1979	1,1	0,4	1,4	0,4	2,4	1,0	2,3	1,5	1,0
1980	1,2	0,5	1,4	0,4	2,9	1,0	2,7	2,3	1,0
1981	1,4	0,6	1,4	0,4	2,7	1,1	4,2	2,6	1,0
1982	1,1		1,4	0,4		1,1	—	2,6	1,0
					as % of gross fixed capital formation				
1970	2,0	1,7	3,0	2,3	11,4	6,5	8,4	3,2	8,2
1974	4,4	1,4	5,2	1,9	7,8	3,7	7,4	3,1	6,0
1975	4,2	2,3	5,2	2,8	8,3	4,9	9,3	3,9	5,6
1976	4,3	2,4	6,7	4,6	8,7	4,8	9,3	4,5	5,8
1977	4,6	2,3	6,5	2,5	8,2	6,3	8,0	4,0	6,0
1978	5,3	2,1	6,2	1,9	7,7	5,9	7,2	4,3	6,8
1979	5,3	2,1	6,4	2,0	7,6	5,5	9,2	7,1	5,1
1980	5,9	2,4	6,0	1,9	10,0	4,8	10,4	11,1	5,4
1981	7,7	3,8	6,3	2,0	9,2	5,2	18,1	13,6	6,0
1982	6,2		6,9	2,0		5,7	—	14,1	6,2

Sources: Eurostat, 'General government accounts and statistics', and national sources.

4. Monetary policy and the European Monetary System

In 1984, the monetary policies conducted in the Community contributed satisfactorily to convergence. This stabilized the European Monetary System. The stance adopted in 1985 is generally in line with last year's trends. However, financial innovations are changing the conditions in which the authority of the central banks is exercised, and several of them have been led to modify their instruments. The fall in nominal interest rates generally continued and in Europe was more marked on long-term than on short-term rates. Among the EMS countries, the fall was more marked in the countries where rates remain relatively high and which were able to take advantage of disinflation than in the countries with lower interest rates which suffered substantial exports of capital to the United States. However, in the latter countries the movement of the dollar exchange rate on the foreign exchange market after March 1985 opened up some scope for reducing interest rates, and this has already been used. The upward convergence of real interest rates is indicative of the common stance of monetary policies against a background of substantial public sector deficits. The stability of exchange rate relationships within the EMS provided a contrast with the wide swings in the exchange rate of the ECU against other currencies. The adjustment of the lira's official exchange rate on 21 July 1985 will not be fully vindicated unless the Italian economy converges more rapidly with those of her partners. New vigour was given to the process of financial and monetary integration in the field of the freedom of capital movements. Basing themselves on the progress made in this area and in the area of convergence, the competent Community authorities strengthened the exchange rate mechanism of the EMS.

4.1. Contribution of monetary policies to convergence

As demonstrated by the changes in a number of indicators analysed below, monetary policies generally made a substantial contribution in 1984 to the convergence process. This stabilized the European Monetary System. The objective of creating an internal and external zone of monetary stability is now common ground, but, given the uneven results in the fight against inflation, the stance to be taken by monetary policy is bound to vary from country to country. In the countries where the inflation rate is still high, the monetary authorities seek a progressive reduction of monetary growth. In the countries where the inflation rate is sufficiently low, monetary policy seeks to provide the liquidity necessary for real, lasting growth in line with the growth of potential output while preserving the stability already achieved.

These policies were reflected in 1984 in a fresh deceleration of monetary growth both as an average for the Community countries and as an average for the countries participating in the EMS exchange rate mechanism. Further, the summary indicators of convergence, such as the average absolute difference between national rates of monetary growth and the Community average, or in between them and the lowest in the Community, stabilized at a level much closer to that of the 1960s, a period of internal and external monetary stability, than to the level which prevailed when the EMS was established.

A country-by-country analysis of two additional indicators of the stance of monetary policy confirms this general impression. First, the development of the liquidity ratio, which measures the difference between the expansion of the broad measure of money supply and the growth of nominal GDP gives an initial impression of the degree of constraint exercised by monetary policy.

In the Federal Republic of Germany, the fall (−0.7 %) follows three consecutive years of increase at an average rate of 2.4 % a year. These trends remain in line with the Bundesbank's medium term strategy which gears monetary growth to the growth of potential output. In a period of cyclical catching-up such as characterized 1984, the liquidity ratio therefore tends to fall, in contrast to periods during which actual growth is lower than potential growth.

In Italy, France and Ireland the fall in the liquidity ratio, which has been in progress for several years, corresponds to the need to bring inflation down towards the lowest rates in the Community and to reform financing structures. Denmark and the Netherlands have for some years recorded a marked rise in the liquidity ratio. The monetary authorities have indicated that they are watching these developments carefully; these developments have not, however, affected their principal intermediate objective, the exchange rate parity of their currencies within the EMS.

In the United Kingdom the liquidity ratio, measured by reference to the broad measure of money supply (sterling

Table 4.1

Convergence and deceleration of growth rates of the money stock (yearly averages)

		1970/60	1975/70	1980/75	1980	1981	1982	1983	1984	1985	Change 1981-85
B	M2H	8,3	14,4	10,8	7,4	7,8	9,7	5,4	8,8	6,0	−1,8
DK	M2H	10,3	11,2	12,0	9,4	5,2	11,0	19,5	19,2	13,0	+7,8
D	M3	10,1	10,8	8,8	5,3	6,3	6,5	6,6	3,8	5,2	−1,1
GR	M3	17,7	20,8	22,9	19,8	30,4	32,9	21,7	25,8	29,8	−0,6
F	M2R	12,7	16,8	13,4	11,0	10,7	11,2	9,3	8,5	7,3	−3,4
IRL	M3	10,0	17,8	19,1	14,5	20,6	13,7	9,3	8,2	8,3	−12,3
I	M2	13,2	18,5	22,8	19,9	17,1	16,2	15,4	12,5	12,0	−5,1
NL	M2	9,1	14,0	8,8	8,0	4,3	7,4	9,5	6,9	8,3	+4,0
UK	UKLM3	5,3	17,0	11,7	15,2	16,9	11,5	10,9	9,7	11,4	−5,5
EUR		10,0	15,3	13,4	11,9	11,8	11,2	10,4	8,7	9,0	−2,8
Weighted dispersion within the EC in relation to:											
(i) the mean		2,9	3,7	4,4	4,6	4,8	2,9	2,9	2,8	3,0	−1,8
(ii) the lowest		5,0	6,3	7,4	6,6	7,6	4,7	5,0	5,0	3,8	−3,8
EMS		11,3	14,7	13,6	10,8	10,1	10,5	9,9	8,1	7,9	−2,2
Weighted dispersion within the EMS in relation to:											
(i) the mean		1,9	3,4	4,5	4,4	3,8	3,2	3,1	3,0	2,3	−1,5
(ii) the lowest		4,4	5,7	6,9	5,5	5,8	4,0	4,6	4,3	2,7	−3,1

Source: Commission departments.

Table 4.2

Monetary and credit targets

		1980		1981		1982		1983		1984			1985	
		Target	Out-turn	Target	Out-turn	Target	Out-turn	Target	Out-turn	Target	Out-turn	Target	Out-turn	
													over 12 months	in relation to the base Annualized rate season-ally adj.
D	MZ[1]	5-8	4,8	4-7	3,5	4-7	6,0	4-7	7,0	4-6	4,6	3-5	4,3 (August)	4,7
F	M2[2]	11,0	9,8	10,0	11,4	12,5-13,5	11,5	9,0	10,2	5,5-6,5	7,6[4]	4-6	8,0 (July)	6,3[8]
I	TDCE[3]	17,5	18,4	16,0	18,2	15,5	20,8	18,2	20,6	17,4	19,3	16,8	18,3 (August)	—
UK[5]	UKL M3	7-11	18,6	6-10	13,8	8-12	10,8	7-11	9,4	6-10	11,9	5-9	13,6 (August)	13,6
	M0									4-8	5,7	3-7	4,5 (August)	4,5
USA[6]	M1	4,5-6	7,3	3,5-6	2,3	2,5-5,5	8,5	4-8	9,6	4-8	6,0	3-8	10,4 (August)	13,2
	M2	6-9	8,4	6-9	9,2	6-9	9,9	7-10[7]	7,8[7]	6-9	8,0	6-9	9,6 (August)	9,3
	TDCE[3]							8,5-11,5	10,6	8-11	13,6	9-12	12,8 (July)	12,8

[1] Central bank money stock.
[2] For 1984 and 1985: M2R (residents' M2).
[3] TDCE (total domestic credit expansion).
[4] Change between three-month averages centred on December.
[5] Targets were also set for M1 and PSL2 (liquidity broadly defined) in 1982 and 1983. Up to 1985: annual rates for the period from February to April of the following year; from 1985: 12 month rates.
[6] The USA also has an M3 target.
[7] For the period from February/March 1983 to the fourth quarter of 1983; annualized rates.
[8] Following the definition of the target, the difference between the quarterly average centred on June and the quarterly average centred on December.

M3), rose sharply in 1984 for the fourth year in succession. This development can however be partly explained by the greater role of certain time deposits as an investment asset. The United Kingdom authorities had indeed taken account of this element of uncertainty in setting their target for the growth of money supply (sterling M3), which was nevertheless overshot by 1,9 percentage points during the 1984-85 budgetary year.

Lastly in Greece, the rapid growth of the liquidity of the economy means there is no real hope of a significant slowdown in the immediate future of the inflation rate which is now still close to 18 %.

The development of the sources of money creation is another important indicator of the stance of monetary policies (see Table 4.4). First, a significant restoration of balance between internal and external counterparts took place in Denmark, France and Ireland, countries in which the destruction of liquidity by the external sector was still marked in 1983. This trend, which became apparent in 1984, should continue in 1985. It demonstrates that the monetary policy followed in these three countries supports the process of restoring balance to the external accounts by moderating money creation through the domestic sectors. In Belgium, a substantial improvement in the current account balance which started in 1983 did not suffice to prevent a substantial destruction of liquidity by the external sector, because of the persistence of net exports of capital by the non-bank private sector. In that country this situation nevertheless seems to have been reversed in the early months of 1985.

With regard to the domestic counterparts, greater recourse to non-monetary resources by the Treasury or the banking system is evidence of the efforts made to reform financing structures. In their turn these efforts are largely the result of the movement of real interest rates (Table 4.5) and in certain cases were accompanied by the appearance of new

Table 4.3

Indicators of the liquidity of the economy

	(a) liquidity ratio (M : GDP) (annual % changes)							(b) real money supply (M : GDP prices) (annual % change)						
	1970/60	1980/70	1981	1982	1983	1984	1985	1970/60	1980/70	1981	1982	1983	1984	1985
B	−0,2	1,9	3,7	1,3	−0,9	1,6	−0,7	4,7	5,1	2,4	2,4	−0,5	3,3	1,3
DK	−0,7	−0,5	−3,5	−3,1	8,5	8,5	6,2	3,8	1,8	−4,4	−0,3	10,6	12,7	8,7
D	1,6	1,5	2,0	2,8	2,3	−0,7	0,7	6,3	4,4	2,1	1,8	3,2	1,9	3,0
GR	6,0	2,3	9,7	6,8	1,3	2,2	8,8	14,1	7,2	9,3	6,7	1,6	4,9	10,9
F	2,3	1,4	−1,5	−3,0	−1,4	−0,2	0,3	8,0	5,1	−1,3	−1,1	−0,4	1,4	1,5
IRL	0,1	−0,4	0,1	−3,2	−1,8	−2,7	−0,4	4,4	4,1	3,0	−1,3	−1,2	1,5	2,1
I	2,5	1,9	−1,2	−1,0	1,5	−0,9	0,9	8,3	5,1	−1,0	−1,5	0,3	1,6	3,6
NL	−1,3	0,5	−0,5	2,8	6,7	2,5	3,6	3,8	3,4	−1,2	1,3	7,7	4,2	5,8
UK	−1,7	−1,6	5,9	2,3	2,1	3,2	2,1	1,1	0,3	4,7	4,2	5,5	5,0	5,6
EUR	0,9	0,8	1,3	0,5	1,4	0,7	1,3	5,5	3,8	1,1	1,0	2,4	2,8	3,7
EMS	1,6	1,4	−0,1	−0,1	1,3	−0,0	0,9	6,8	4,6	−0,0	0,1	1,7	2,2	3,0
	(c) ratio of money supply to real GDP (annual % changes)							(d) money supply deflated by unit labour costs (annual % changes)						
B	3,2	9,2	9,2	8,5	5,0	7,0	4,0	4,8	3,5	0,9	4,2	0,2	3,7	1,8
DK	5,6	9,0	6,2	7,8	17,3	14,7	10,4	3,2	1,7	−3,2	2,2	14,1	15,4	9,3
D	5,3	6,8	6,1	7,5	5,6	1,2	2,9	5,9	4,2	1,9	3,1	5,6	3,1	3,6
GR	9,3	16,4	30,8	33,1	21,3	22,6	27,4	16,1	7,3	4,0	5,8	3,0	6,7	10,3
F	6,7	11,0	10,4	9,1	8,3	6,8	6,0	8,1	4,4	−2,2	−0,6	0,1	3,0	3,6
IRL	5,5	13,3	17,3	11,5	8,6	3,6	5,7	4,4	3,5	7,0	1,1	1,5	4,0	3,9
I	7,1	16,9	16,9	16,7	16,8	9,7	9,1	8,6	4,4	−4,2	−1,1	−1,8	2,5	4,1
NL	3,8	8,2	5,0	9,0	8,5	5,1	6,0	2,6	3,3	1,5	2,9	9,2	8,6	8,6
UK	2,4	12,2	18,3	9,5	7,4	7,8	7,7	0,9	0,3	6,0	5,9	6,1	4,3	5,7
EUR	5,1	11,1	12,1	10,6	9,3	6,4	6,5	5,6	3,4	0,5	2,0	3,0	3,9	4,6
EMS	5,9	10,7	10,1	10,3	9,5	5,7	5,7	6,7	4,1	−0,9	1,0	2,3	3,7	4,1

Source: Commission departments.

financial products, made attractive by a high level of both liquidity and yield. Greater recourse to these non-monetary resources does of course help to contain the inflationary impact of high public sector deficits; but it also involves substantial financial costs for public finances, seen in the increase in debt servicing costs, and it puts pressure on the private sector whose share in domestic credit in Belgium, Greece, Ireland, Italy and the Netherlands remains lower than or just about equal to the public sector share. In these countries, this development merely reinforces the need for a much quicker reduction of public sector deficits.

In the light of the objectives set, where appropriate, for monetary aggregates and credit, the stance adopted in 1985 for monetary policies is in line with last year's developments (see Table 4.2). In the Federal Republic of Germany the 1 percentage point reduction in the target range for the growth of central bank money stock (MZ 3 % to 5 % in 1985) takes account of the fall in the inflation rate to a level close to 2 %. If MZ were to grow at a rate close to the upper limit of this range, as it did in the early months of 1985, this would provide sufficient liquidity for real growth of over 2,5 %.

In France and Italy, the targets set are well down on last year's out-turns. This is in line with the need for stabilization which still exists in the two countries. Developments at the start of the year in both cases indicate that the targets set have been overshot. This is chiefly due to public monetary financing requirements which were higher than forecast. In France, the Treasury expressed, at the end of June 1985, its intention of resorting to a greater extent to non-monetary resources while the Banque de France tightened its rules for controlling lending to the private sector; such lending was

Table 4.4

Counterparts of money creation

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

	(1) Money creation = rate of growth[1] of M2/3 (1 = 2 + 3 + 4)			(2) Domestic money creation (2 = 5 = 6 + 7 − 8)			(3) External creation (+) or destruction (−) of liquidity			(4) Other		
	1983	1984	1985	1983	1984	1985	1983	1984	1985	1983	1984	1985
B	7,0	6,1	6,0	13,9	10,7	9,7	−5,9	−5,3	−3,1	−1,0	0,7	−0,5
DK	25,5	17,0	11,0	27,6	12,7	9,5	−4,1	0,8	0,0	2,0	3,5	1,5
D	5,3	4,7	5,0	5,1	3,2	3,5	0,7	0,8	1,7	−0,5	0,7	−0,3
GR	20,3	29,4	29,3	23,6	33,0	31,4	−3,6	−4,6	−2,0	0,3	1,0	0,0
F	11,2	8,3	5,8	11,6	7,0	5,2	−1,9	−0,1	0,1	1,5	1,4	0,5
IRL	5,6	10,1	16,6	9,5	15,2	3,9	−3,9	−5,1	2,7	0,0	0,0	0,0
I	13,2	11,8	12,1	13,2	15,1	16,3	0,9	0,1	−1,2	−0,9	−3,3	−2,9
NL	10,5	7,7	8,0	9,8	4,9	2,8	2,3	5,2	6,9	−1,7	−2,5	−1,8
UK	10,3	9,6	11,3	10,0	8,6	8,0	1,2	−2,4	0,6	−0,9	3,5	−2,7

	(5) Domestic money creation (5 = 2 = 6 + 7 − 8)			(6) Lending to the public sector			(7) Lending to the private sector			(8) Non-monetary liabilities		
B	13,9	10,7	9,7	17,7	14,0	11,7	3,1	1,2	2,7	6,9	4,5	4,7
DK	27,6	12,7	9,5	17,4	0,8	0,7	17,2	14,3	11,5	7,0	2,4	2,7
D	5,1	3,2	3,6	2,5	2,6	2,1	11,0	10,0	10,6	8,4	9,4	9,1
GR	23,6	33,0	31,4	13,1	18,7	17,8	11,9	14,0	12,5	1,4	−0,4	−1,1
F	11,6	7,0	5,2	3,5	1,0	2,0	12,1	10,4	7,3	4,0	4,4	4,1
IRL	9,5	15,2	3,9	7,7	10,0	3,3	6,3	5,7	2,4	4,5	0,5	1,8
I	13,2	15,1	16,3	8,4	8,6	9,6	8,6	11,2	7,1	3,8	4,7	0,4
NL	9,8	4,9	2,8	4,8	5,3	2,8	6,9	7,3	8,1	1,9	7,6	8,0
UK	10,0	8,6	8,0	0,0	−1,3	−2,7	13,9	16,2	16,9	3,9	6,3	6,2

[1] Money supply broadly defined. The figures for the counterparts are difficult to compare between one country and another.
Source: Commission departments.

also tending to exceed a rate compatible with the target for the growth of the M2R money supply (4 %-6 %). In Italy, the targets set for total domestic credit, an aggregate which largely depends on the size of the budget deficit, and for the growth of the M2 money supply, which is more directly under the control of the central bank, were largely overshot in the early months of 1985. If this excessive money creation is to be offset in the next few months, the measures adopted to check and to reverse the tendency for the public deficit to increase must be effectively implemented and the monetary authorities must display great rigour.

In the United Kingdom the target adopted was to keep the 12-month growth rate during 1985-86 within the ranges 3-7 % for M0 and 5-9 % for sterling M3. In accordance with the government's medium-term financial strategy, these targets are 1 percentage point lower than in the preceding year. However, as a result of the difficulties associated with the interpretation of sterling M3, the growth of which has remained very strong, the United Kingdom authorities have gradually given special importance to the narrower aggregate, M0, and greater attention has been given to the movement of the sterling exchange rate as an indicator of the course of monetary policy.

4.2. Financial innovations and the operation of monetary policies

For some years monetary policies have been operated against the background of changing financial markets. It is still too soon to draw any final conclusions on the consequences of the changes which are taking place almost day by day on the money and capital markets, but some remarks must be made. There are two reasons for the emergence of new financial products: the attempt to find protection against variations in interest rates and exchange rates, and greater competition in the collection of savings against a background of high real interest rates. There are numerous examples, which include variable or indexed interest rates, zero coupon bonds which reduce taxation or at least defer it until the redemption date, interest rate and currency swaps. These new financial products come both from private debtors and financial intermediaries and from Treasuries, which seek in this way to reduce the financial cost of their indebtedness against a background of a policy of monetary stabilization. The result of the keener competition on the financial markets has been to widen the range of activities undertaken by intermediaries, within the limits set by present law, and to decompartmentalize the money and capital markets both nationally and internationally.

The long run consequences of these developments on the stability of financial systems will depend on the speed of the innovation process, on the capacity of banks to act in a more turbulent situation and the appropriate reactions of the banking supervisory authorities. Further, problems will also result for the operation of monetary policy itself.

The choice of an intermediate objective in the form of a monetary aggregate becomes more difficult. The difficulties are associated more particularly with the appearance of new financial products which serve as substitutes for the assets traditionally included in the definition of the money supply. For example, in France, the creation of unit trusts holding of bonds close to maturity has provided the public with a high yield asset which can be easily realized and for which the variation in prices are not very sensitive to variations in interest rates. The funds collected for this type of investment have risen to 4.2 % of the money supply. In Italy, the issue of treasury bills at indexed interest rates, which combine the advantages of high yield and a high degree of liquidity, has also helped in the last two years to moderate the growth of money supply. Conversely, in Denmark the extremely rapid expansion of the money stock in the last two years is attributable to the greater competition between banks for time deposits (included in the definition of M2), the return on which is now close to the return on bonds maturing within a similar period. These examples call for three comments.

First, it is probable that after an adjustment period the money demand function will gradually stabilize. It is therefore fundamentally no less relevant to pursue a target for a monetary aggregate, even though this policy becomes more complicated.

Second, even though they offer significant advantages in terms of liquidity, the new financial products are not without cost to the debtor. On the contrary their appearance has been accompanied by a rise in short-term real interest rates. This has the welcome effect of rationalizing the allocation of resources obtained from financial savings.

Lastly, the fact that assets which are liquid but earn a high rate of interest occupy a position between the capital markets and the segment of the money market more directly under the control of the central bank weakens the transmission mechanism of monetary policy: the actions of a central bank are primarily reflected in changes in the relative level of interest rates on short-term and liquid assets and only reach the capital market late and in a diluted form. This strengthens the arguments in favour of a monetary policy which consistently aims for stability. By limiting inflationary expectations, such a policy makes market forces more rational, and these in any event remain the chief determinant of long-term rates.

The greater role played by the markets in determining short-term rates also has its consequences for the management of monetary policy. In recent months several Community central banks have thus had to modify their instruments to a greater or lesser extent so as to strengthen the role of interest rates in controlling the monetary aggregates and credit, or so as to be able to react more flexibly to changes in money market rates. Thus Belgium's Banque Nationale, stating that monetary policy had to face up to changes which were far more rapid and more intense than before, decided in May 1985 to amend the procedures for fixing official rates in order to make them more flexible. With effect from 1 June 1985 the Danish national bank replaced a quantitative ceiling on credit by compulsory reserves on bank deposits in order to have a control mechanism more oriented to the market, and with effect from 1 August modified its money market intervention instruments in order to achieve more flexible management of liquidity and short-term rates. In the first half of 1985, the Bundesbank strengthened the role played by open market operations thus enabling a more flexible management of the money market. There is also the problem of reforming the system of compulsory reserves in the Federal Republic. The present system's effectiveness is liable to be jeopardized by the growth of marketable instruments on both the asset and the liability side. In particular, the growth of certificates of deposit, which are negotiable short or medium-term securities, and are not subject to compulsory reserves, could call into question the significance of the intermediate objective, which is directly linked to conventional bank deposits. With effect from 1 January 1985, the Banque de France abolished the system of quantitative ceilings on credit and replaced it by arrangements based on compulsory reserves on lending net of non-monetary resources. The reserve ratio is progressive and can be modified every quarter. These arrangements should give the banks greater discretion in their operations and stimulate competition between institutions. They could mark a stage in a gradual development which will result in more room being given to the use of interest rates.

4.3. Interest rates

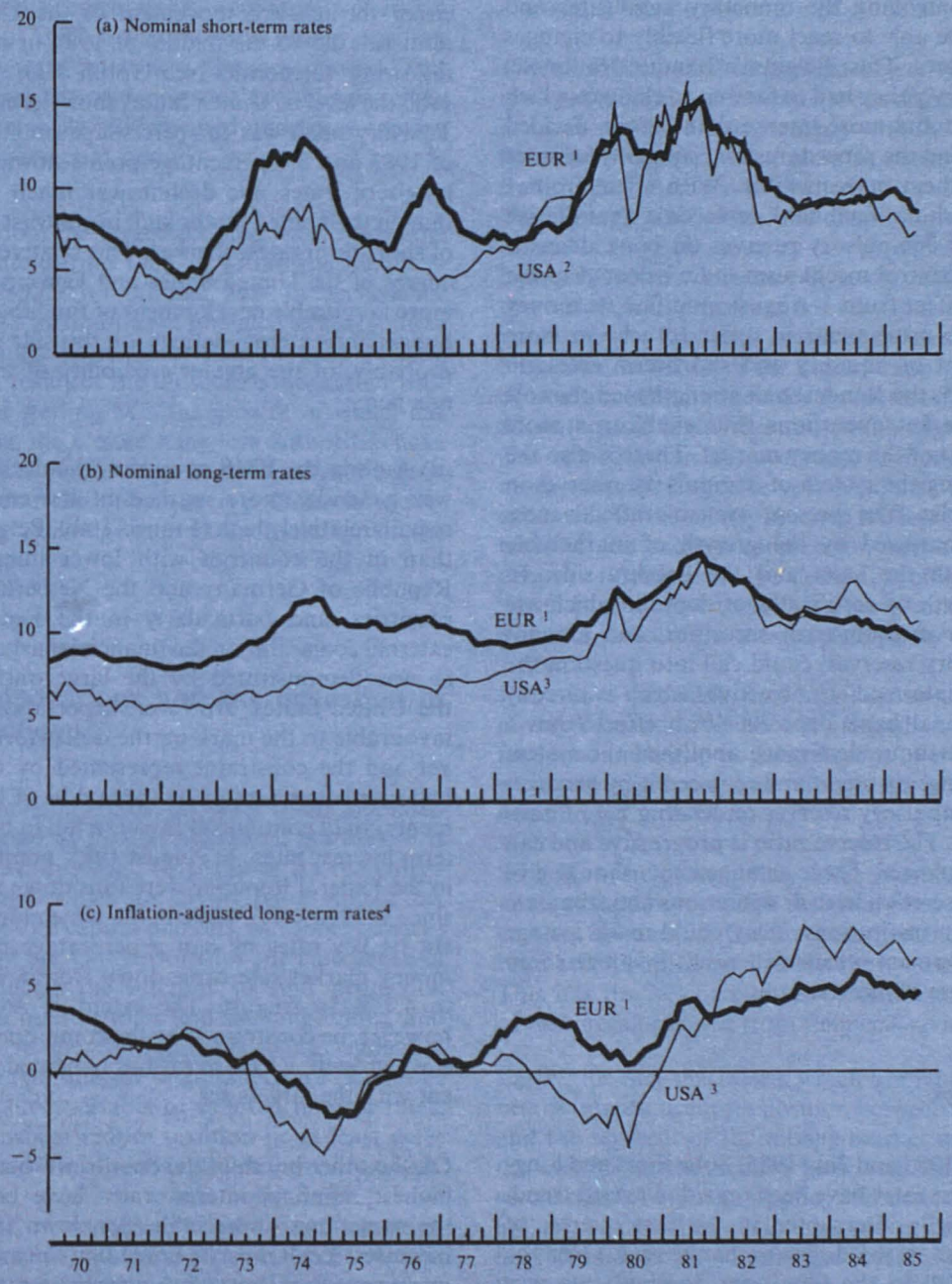
Between the end of 1983 and July 1985, both short and long-term nominal interest rates have been on a downward trend, which was temporarily interrupted in the first quarter of 1985 following a rise in the dollar exchange rate. Over the whole period the fall in the long-term nominal rate was sharper than the fall in the short-term rate: in terms of Community averages the long-term rate fell 1,7 percentage points between the end of December 1983 and July 1985, while the short-term rate fell 1,2 points. Among the countries participating in the EMS exchange rate mechanism the fall over the same period was 1,9 percentage points for long-term rates and 1,7 percentage points for short-term rates. Three additional comments are called for.

(i) European short-term interest rates did not fully match either the upward movement of the United States short-term rate up to the middle of 1984 or its sharp fall in the following 12 months (see Graph 4.1). At the end of July 1985 the level of United States short-term rates (three-month Treasury bills) was 1,7 percentage points down on the end of 1983 and 3,1 percentage points down on July 1984. For long-term rates, the decline was much steadier in Europe than in the United States and, in contrast to the performance of short-term rates, sharper. This relative change in the yield curves of the United States and Europe is indicative of the more favourable development of fundamentals, in particular budget and external deficits, on this side of the Atlantic and, probably, of the greater credibility of the economic policy mix here.

(ii) Among the EMS countries, the decline in interest rates was generally more marked in the countries where they remain relatively high (France, Italy, Belgium and Denmark) than in the countries with lower interest rates (Federal Republic of Germany and the Netherlands). In the latter countries, and particularly in the Federal Republic, the external constraint on the financial markets remained severe, as was demonstrated by the large outflows of capital to the United States. However, expectations now seem more favourable to the mark on the dollar foreign exchange market and the constraint represented by outflows of capital had eased considerably by the middle of 1985; these developments could continue to favour a fall in both long and short-term interest rates. In August 1985, nominal long-term rates in the Federal Republic were thus down to their lowest level since 1979 (6,4 %), while in the same month the Bundesbank cut its key rates by half a percentage point. The German money market rate came down from 6,3 % in March 1985 to 4,7 % in August. The extent of any further fall will, however, be constrained by the commitment to control monetary growth, which so far has remained completely consistent with the targets set.

On the other hand, in the countries where inflation remains highest, nominal interest rates have been able to follow the sometimes appreciable slowdown in the rate of price increases. Yet it must be noted that the monetary authorities' management of short-term rates has remained very cautious, and this is desirable from the point of view of the external and internal stabilization of their currencies. The central banks have in general avoided reducing short-term rates more rapidly and more sharply than the fall in the inflation rate even though the external situation as revealed by con-

GRAPH 4.1 : **Interest rates in the Community and in the USA (end of month)**



[1] Averages of representative money-market rates (short term) and capital market rates (long term) weighted by the contribution of each currency to the ECU.
[2] Yield at issue of 13-week Treasury bills.
[3] Federal government bonds over 10 years.
[4] Rate of inflation over 12 months preceding each observation. Further details are given in the technical annex.

ditions within the EMS seemed to leave them some room for manoeuvre.

In the United Kingdom the pressures on sterling at the start of this year meant that short-term interest rates had to be raised by some 4 percentage points, and this was reflected in a 5 percentage point rise in the banks' base rates. Although they have since fallen, short-term rates in the United Kingdom are still some 2,5 percentage points higher than at the end of 1984. Given some revival of inflation and the very rapid growth of money and credit in the last few months, this movement of rates is also justified by a domestic need for stabilization.

(iii) In the Commmunity, in the last few years, 'real long-term interest rates', measured as a first approximation by the difference between the nominal interest rate and the rate of increase of consumer prices, converged upwards (see Table 4.5). However, the rise of real interest rates on average in the Community (by 4,5 percentage points between 1981 and 1984) remained well below the increase in the United States (9,9 percentage points between the same two years). In all the Community countries except Greece the difference between the nominal long-term interest rate and the inflation rate is now in the range 3,5 % to 6,5 %, whereas a far wider range still existed at the start of the 1980s.

Methodological difficulties exist in measuring real interest rates. If disinflation is rapid or the inflation rate is historically low, the real interest rate, as measured by the difference between the nominal interest rate and the actual rate of price increase can in certain cases be an overestimate as compared to a measure taking account of the inflation rate expected in the medium-term, which is probably higher than the current rate of inflation at such a time. Conversely, in countries where the inflation rate is still high but where the disinflation process has clearly begun and carries conviction, the real interest rate expected in the medium-term is higher than the rate measured with the current inflation rate. Inflationary expectations play a key role in the formation of nominal interest rates. This fact certainly increases the importance that should be attributed to the pursuit of monetary policies which aim at lasting price stability in a manner which carries conviction. Such policies help to bring the current and the expected inflation rates closer to one another and to stabilize them at the lowest level. This puts the formation of nominal interest rates on a more rational basis and creates a situation favourable to their progressive and lasting decline.

Nevertheless, the persistence of a wide gap between the long-term nominal interest rate and the current inflation rate may be seen as the expected consequence of a disinflation strategy which includes a tight monetary policy, especially since such policies are applied in most instances in situations characterized by large public sector deficits. This strategy has been applied in some Community countries and its effects in these countries have been accentuated by developments in the

Table 4.5

Development and convergence of real long-term interest rates[1]

	1971-80	1980	1981	1982	1983	1984	Change 1980-84	Aug. 1985
B	1,3	5,2	5,7	**4,3**	**3,8**	**5,3**	+0,1	**5,6**
DK	4,4	5,7	6,8	**9,4**	**7,0**	**7,3**	+1,6	**6,1**
D	2,7	2,8	4,2	**3,5**	**4,2**	**5,2**	+2,4	**4,2**
NL	1,1	3,5	5,0	**4,3**	**5,9**	**5,3**	+1,8	**4,9**
F	1,0	0,1	2,6	**3,6**	**4,5**	**5,3**	+5,2	**6,0**
IRL	−0,7	−2,5	−2,4	**−0,3**	**3,1**	**5,5**	+8,0	**5,7**
I	−2,1	−4,3	0,9	**3,8**	**2,9**	**3,7**	+8,0	**4,0**
GR	−5,3	−6,2	−5,5	**−4,6**	**−1,9**	**0,1**	+6,3	**−3,2**
UK	−1,1	−3,5	2,6	**3,7**	**5,9**	**5,5**	+9,0	**4,0**
EUR average	1,4	0,6	3,2	3,7	4,5	5,1	+4,5	4,7
USA	−0,5	−2,4	2,3	5,7	7,4	7,5	+9,9	6,8
Range								
EMS	6,5	10,0	9,2	9,7	**4,1**	**3,6**	−6,4	**2,1**
EUR	9,7	11,9	12,3	14,0	**8,9**	**7,2**	−4,7	**9,3**

[1] Adjusted on the basis of the consumer price index.

USA, where a combination of tight monetary policy has resulted in other countries being crowded out of the international capital markets.

Almost all Community countries are now pursuing monetary policies based on the progressive reduction of the rates of growth of money and credit and on subsequently holding them to a path compatible with the objective of stability. In most cases these policies include participation in the European Monetary System. In these circumstances, the management of short-term interest rates by the monetary authorities is subject to the constraints represented by the growth of money and credit and by the exchange rate discipline; and the room for manoeuvre in this area is limited. Market forces are becoming, perhaps for the first time, the chief determinant of interest rates. In particular, the monetary authorities are virtually unable to exercise direct control over long-term nominal (and, *a fortiori*, real) interest rates without a danger of coming into conflict with the other intermediate objectives of monetary policy. Further, full participation in the EMS stabilizes expectations about the long-term development of exchange rates and thus increases the degree of substitutability between financial assets denominated in the different currencies. To that extent the links between the interest rates ruling on the different national capital markets are made stronger.

The continuation of restrictions on capital movements does of course introduce distortions into the formation of interest rates within the EMS. Such restrictions can give the authorities an enlarged room for manoeuvre in the execution of monetary policy. It may, however, be noted that the existence of very different systems regulating the movement of capital has not prevented an upward convergence of real long-term interest rates in the Community (see Table 4.5). That is to say, since the aims of stability and convergence are common ground, the room for manoeuvre made available by capital controls has been used only to a limited extent.

While it may appear that the persistence of high real long-term interest rates may raise problems, notably for public finance, and may more generally have an impact on the growth process, the scope for individual, or even for concerted, action on long-term interest rates is very limited. A sustained reduction will be dependent essentially on the orderly continuation of the disinflation process in a manner which carries conviction, and on the elimination of financial disequilibria, in the first place those affecting the public finances.

4.4. Exchange market developments

The exchange rates of the principal non-Community currencies have, as in other recent years, been subject to very wide changes. Over the period from December 1983 to July 1985 the gap between the highest monthly average value of the US dollar against the ECU, which occurred in March 1985, and the lowest, which occurred in March 1984, was 27 ½ %. By July 1985 the monthly average value of the US dollar had fallen 12,4 % against the ECU since March 1985. The yen also underwent wide variations against the ECU: its range over the same period and on the same basis was 11,4 % and it fell against the ECU by 7,3 % between March and July 1985. It should be remembered that the dollar's movements in both directions have been accompanied since July 1984 by a fall of short-term interest rates in the USA which has been much more rapid than that occurring in Europe, while the differential between long-term interest rates has been virtually unchanged (see 4.3). The relationship between interest rate differentials and exchange rates has been extremely unstable in this period, and is evidence of the uncertainty felt in the markets as to the future value of the US dollar.

These developments must be seen in the context of the stance of monetary policy in Europe. In 1983 and 1984 monetary authorities in Europe could accept a rise in the exchange value of the US dollar without a substantial or prolonged tightening of policy. As a result of the substantial steps taken in other areas of economic policy, it was possible to make great progress towards domestic stabilization in spite of the fall in the external value of European currencies. The stabilization process was, however, interrupted, if not reversed, in the early months of 1985, to some extent precisely because of the sharp rise of the US dollar between November 1984 and March 1985. The fall of the US dollar which is occurring at present should certainly reduce the burden falling on monetary policy in the pursuit of the final objective of price stability. The stabilization which would be the mechanical result of a slow-down of the rise of import prices will of itself open up greater scope for real growth for any given rate of expansion of nominal quantities. Nevertheless, quite independently of the US dollar exchange rate, lasting success in the struggle against inflation can only be obtained by the pursuit of the medium-term strategy currently being given effect, which aims at moderate money growth over the long term and which is dealing with the structural causes of inflation, in particular by dismantling systems of income indexation. The stabilization of the international monetary system is desirable, but, pending substantial progress in this field, monetary and financial discipline remains the option taken by Europe as a whole as a matter of domestic policy.

The exchange rate mechanism of the European Monetary System has demonstrated a remarkable degree of stability since the realignment in March 1983, even if one takes account of the realignment of 20 July 1985 which resulted

in a depreciation of 7,8 % in the lira's central rate against the other currencies, but left all other bilateral rates unchanged.

If one excludes the case of the lira, it would appear that the maintenance of the bilateral parities within the EMS since March 1983 has not required the monetary authorities to react with substantial and long lasting changes in interest rates. The one exception to be noted is the Belgian franc which came under pressure at the beginning of 1984. The increase in the rates decided at that time by the authorities has since then been reversed.

The absence of significant pressures within the exchange rate mechanism is well illustrated by the relative position of currencies within their margins for fluctuations (see Graph 4.3). The currencies of the countries having the lowest rates of inflation and in addition an external surplus retained a margin for appreciation within the existing constraints of the system. However the stabilization programmes undertaken by the least well balanced countries in the EMS were and will remain decisive; these efforts have already been crowned with a certain success and the external accounts have been brought back into balance.

For all that, the convergence of policy has proven insufficient in itself and, given the continued disparities in performances, has necessitated the maintenance of large interest differentials between the currencies of the EMS. By not fully exploiting the margin of manoeuvre in the short term to reduce their interest rates whilst still maintaining a reasonable situation with the EMS, the central banks of the high-inflation countries have reinforced both the credibility of their policies aimed at internal stabilization and of the parity grid itself.

The effect of the interest differentials on the stability of the EMS has also been reinforced by the burden carried by

Table 4.6

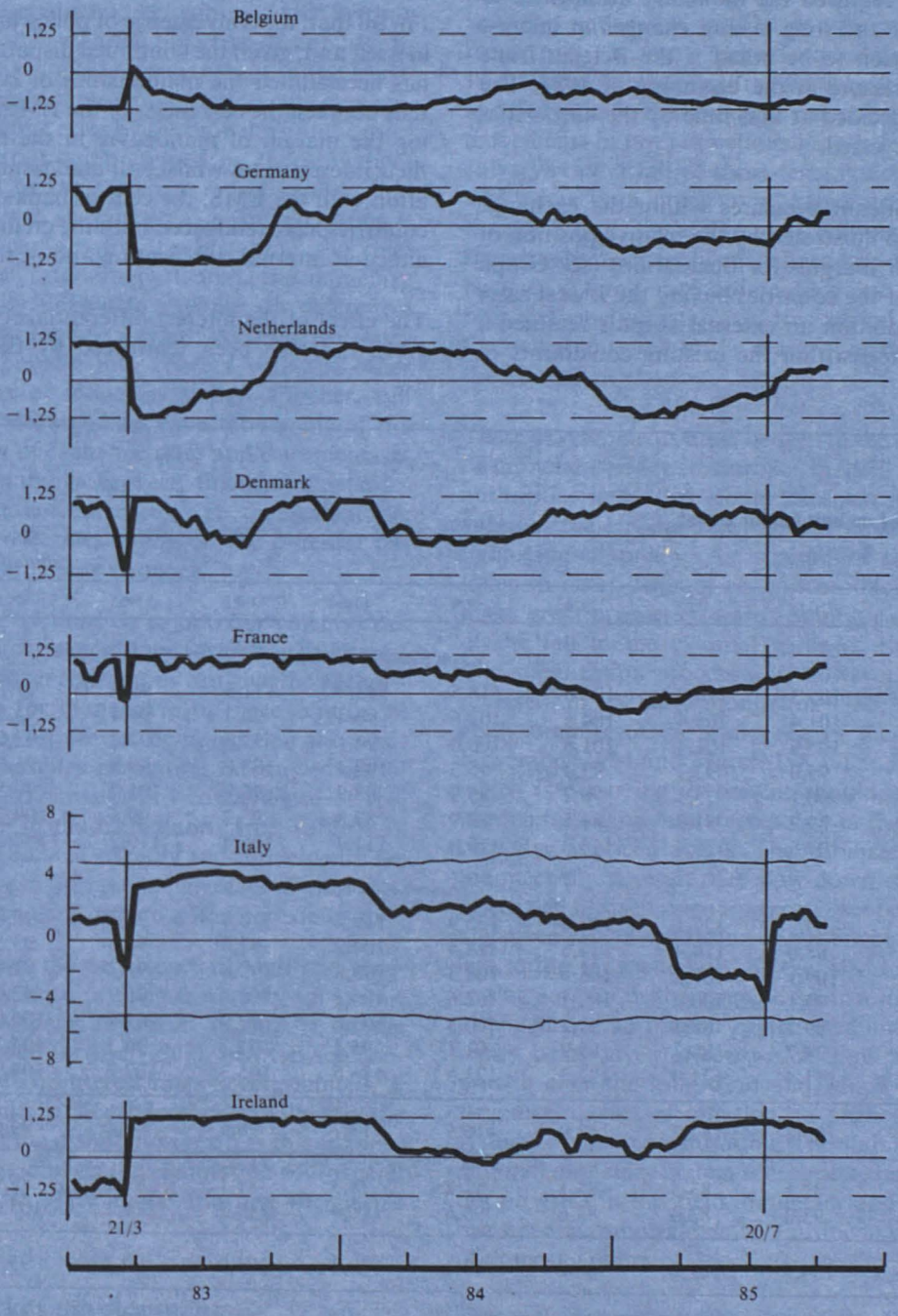
Real exchange rates based on unit labour costs[1]

(annual averages, 1970 = 100)

	1961-70	1971-76	1977	1978	1979	1980	1981	1982	1983	1984	1985[2]
						Against EMS partners only					
B	105,3	105,3	120,8	120,6	118,5	113,8	111,5	99,9	97,7	99,6	102,6
DK	98,6	101,4	105,4	104,6	102,6	96,4	96,7	94,4	93,5	93,5	95,8
D	90,9	105,9	101,4	101,8	100,0	96,1	92,3	94,3	93,5	92,0	90,8
F	115,3	95,0	93,7	93,4	95,3	100,4	103,0	99,8	96,5	96,9	99,1
IRL	105,4	90,1	75,3	76,7	85,9	93,9	96,8	101,4	99,5	98,9	102,0
I	103,1	89,2	81,9	81,5	82,9	87,8	95,2	99,6	109,7	114,9	113,8
NL	92,0	107,6	115,4	116,0	115,0	111,7	106,4	110,2	107,2	102,5	99,4
						Against 19 partners					
B	103,8	109,2	127,1	127,6	125,9	119,2	110,4	98,1	95,8	95,3	96,7
DK	94,9	108,0	114,4	115,6	114,4	104,9	97,0	94,0	93,5	90,3	90,6
D	90,9	109,1	107,5	108,6	108,3	103,8	92,8	92,7	91,8	87,6	85,2
F	111,6	99,1	100,0	100,1	102,6	106,3	100,7	95,9	92,6	90,0	90,1
IRL	99,1	99,3	88,8	91,3	100,3	103,6	97,9	101,4	100,0	96,4	97,3
I	100,7	94,7	88,7	88,9	91,1	95,4	94,7	96,5	104,7	105,6	103,0
NL	90,9	111,4	121,0	122,3	121,5	116,5	105,3	107,7	104,9	98,3	94,2
EMS	96,2	109,2	112,2	113,9	116,1	113,7	98,5	95,4	94,6	89,1	86,3
GR	112,1	82,1	83,5	83,1	87,2	78,3	81,1	87,1	79,9	78,3	77,8
UK	108,0	93,0	82,0	84,6	95,6	116,9	119,2	111,1	103,0	100,3	102,2
EUR	100,4	104,9	102,2	105,2	113,1	120,3	105,0	99,2	95,2	88,5	86,3
USA	97,3	76,4	67,1	61,8	61,3	61,8	68,6	78,2	82,3	88,5	93,6

[1] Calculated using double export weights variable from year to year until 1983.
[2] October 1985 economic forecasts of the Commission departments.

GRAPH 4.2: **Position of EMS currencies in the band**



Germany in financing the external deficit of the USA, given the position of the mark as a reserve currency and the freedom of capital movements in Germany.

The stability of bilateral exchange rates within the EMS has led to certain divergences in real exchange rates (see Table 4.6). On the basis of unit labour costs in the whole economy as compared to their partners in the EMS, these divergences remain in all cases, except Italy, moderate and less than those experienced during the first of the prolonged periods of stability within the EMS (1979-81). These divergences remain in the spirit of an exchange rate mechanism with fixed but adjustable parities and provide support to the domestic stabilization policy actions in the countries where inflation is still too high. For these countries the rise in the US dollar up to March 1985 has attenuated the impact of these divergences on their overall level of competitivity against their industrialized partners. On the other hand the gains in competitivity made by the more stable countries should allow them, everything else being equal, to permit a faster rate of real growth without prejudicing their external balance.

The adjustment of the lira's parity, carried out at the end of July 1985, can be accounted for by fundamental and by circumstantial factors.

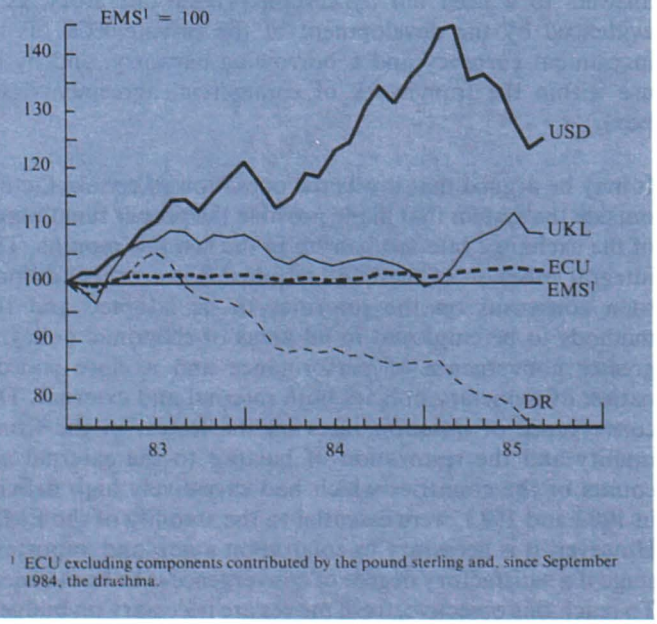
The rapidity with which this operation was conducted after the disorder in the lira exchange market on the previous day — with the unanimity of the participants in the EMS — bears witness to the orderly functioning of the exchange rate mechanism. Because of a growth rate which was in excess of its partners, Italy experienced a sharp deterioration in its external balance at the end of 1984 and the beginning of 1985. In spite of the progress already achieved, Italy retained an inflation rate some 4,5 percentage points above its EMS partners and consequently experienced a loss of competitivity against them. The Treasury deficit threatened in the first quarter of 1985 to exceed 16 % of GDP for the whole year — 1 % more than in 1984 — whilst the system of automatic wage indexation known as the *scala mobile* would, in contrast to the previous year, have its full impact on wage and salary developments. The burden placed on monetary and exchange rate policy in the stabilization process was made significantly heavier.

Following the realignment of July 1985, the situation within the EMS remained calm. The currencies other than the lira returned more or less to the same positions within their margins of fluctuation. Compared with the market rate on the Thursday preceding the realignment, the effective rate of the lira, which at present is the strongest currency in the EMS, depreciated by only 3 %. However, this currency adjustment will not be fully vindicated unless, as soon as possible, significant measures, some of which had already been decided on at the time of the July realignment, are put into effect so as to permit the Italian economy to return this year and next to the path of convergence.

In recent months sterling has fluctuated sharply (see Graph 4.3). At the end of 1984, and even more in January 1985, this currency was under severe pressure on the foreign exchange markets. Between September 1984 and January 1985 it depreciated by 5,3 % against the ECU and 11 % against the dollar. Since then the rise in short-term interest rates which occurred at the end of January 1985 (see 4.3) has reversed and sterling has tended to rise both against the dollar (by 13,5 % between January and June 1985) and against the ECU (by 8,7 % over the same period). The instability of the sterling exchange rate against the ECU and the size of the changes in interest rates necessary to stabilize the currency's external value have contrasted sharply in recent months with the more placid course taken by the currencies participating in the EMS exchange rate mechanism.

In 1985 the drachma continued to depreciate against the ECU. This movement became more pronounced following the fall of the dollar after March 1985. However, the sharp deterioration of the Greek current account balance in the

GRAPH 4.3: **Exchange rates of the pound sterling, the drachma and the US dollar relative to the EMS**



[1] ECU excluding components contributed by the pound sterling and, since September 1984, the drachma.

first nine months of 1985 led the Greek authorities to devalue the drachma by 15 % on 11 October 1985. This devaluation is part of an economic stabilization programme which led the Commission to put into effect the provisions of Article 108 of the EEC Treaty. On this basis, the Commission addressed an economic policy recommendation to the Greek Government covering monetary policy as well as public finance and incomes. The Commission also authorized Greece to maintain temporarily certain protective measures affecting external trade and capital transactions undertaken by Greek residents. At the same time Greece benefited from a Community balance of payments support loan of 175 million ECU.

4.5. European Monetary System and financial integration

Several facts make it incontrovertibly clear that the monetary and financial component of the Community's internal market has been strengthened, while remaining incomplete, and that some progress has been made towards the financial integration of the Community countries.

First of all, the stability of exchange rates between the currencies of the countries participating in the EMS exchange rate mechanism and the generally orderly way in which the necessary adjustments are made contrast sharply with the often erratic shifts which occurred in the past, and which still affect other currencies. This stability is also reflected in the limited nature of exchange rate variations between the ECU and its chief component currencies. It answers to a need felt by certain private operators, as is evidenced by the development of the private ECU as an investment currency and a borrowing currency, and by its use within the framework of commercial agreements (see box).

It may be argued that it was the operation of certain factors outside the system that made possible the proper functioning of the exchange rate mechanism in the last few months. The integral cohesion of the EMS required however, in addition to a consensus on the priorities to be adopted and the methods to be employed in all areas of economic policy, a greater convergence of performance and a close coordination of monetary policies both internal and external. The convergence of inflation rates on the lowest in the Community and the restoration of balance to the external accounts of the countries which had excessively high deficits in 1982 and 1983, were essential to the stability of the EMS. However, it is necessary to enter upon a new and important stage if a satisfactory degree of convergence is to be attained. To reach this objective, fresh moves are necessary on budgets and on wages. The size of these moves will determine the burden which monetary policies will have to bear in the convergence process in the months ahead. In any event, coherent monetary policies which contribute to convergence remain a factor of the utmost importance for the internal cohesion of the EMS and for its capacity to withstand external monetary shocks in an orderly fashion.

If the stability of the Community currencies — both internal stability and, within the framework of the EMS, external stability — is an essential economic foundation for the greater strength of the European monetary area, the freedom of capital movements within the Community is another essential component of that area. The principle of this freedom is written into the Treaty of Rome and, by contributing to the creation of the internal market, its attainment would favour a better allocation of the resources represented by savings.

Since the establishment of the EMS in March 1979, the objective of liberalizing capital movements has become even more important. For, to the extent that the restrictions on capital movements artificially increase the autonomy of monetary policies, they reduce the disciplinary effect of the exchange rate mechanism and are thus liable to hold back the convergence process. This argument is particularly relevant when external monetary shocks have a differential effect on the balances of payments as a result, partly of the varying degree of freedom enjoyed by capital movements. If the countries are to react smoothly to such shocks, the rules governing movements of capital must be brought closer together and their implementation must be properly coordinated. Indeed, in 1972 the Council adopted a Directive, which is still in force, requiring the Member States to provide themselves with certain instruments by which they can protect themselves against capital flows from third countries and their effects on domestic liquidity, and to coordinate, where necessary, the use of these instruments.

Since March 1979, some countries have maintained restrictions on capital movements which should otherwise have been freed under the Council Directive of 1960 implementing Article 67 of the EEC Treaty on the freedom of capital movements. In accordance with Article 108 of the EEC Treaty, these restrictions were authorized by the Commission because of the balance of payments problems which the countries in question were experiencing at the time. In the early days of the EMS they could be justified by the scale of the differences then existing in the performances of the European economies. However, as these differences narrow and policies focus more resolutely on the common objective of stability, restrictions lose their point and it becomes more and more easy to do away with them.

In the last few months, a new impetus has been given to the process of financial integration (see box). The Commission has repealed a decision which authorized Denmark to apply certain protective measures to capital movements. In addition, earlier decisions authorizing three other Member States — France, Ireland and Italy — to maintain certain restrictions on capital movements were reviewed at the end of last year. They are now limited in time and have been made less restrictive in some respects. Some countries have also relaxed their exchange control regulations to an extent which goes beyond their strict obligations to the Community. In this area, much progress still needs to be made in France, Italy and Ireland. In Belgium the abolition of the dual foreign exchange market would serve to complete the full liberalization of the money and capital markets.

The increased convergence of economic performances and the measures increasing somewhat the freedom of capital movements provide a basis on which the Committee of Central Bank Governors and the Council have been able to strengthen the exchange rate mechanism of the EMS. The yield of official ECU positions held by the central banks is now linked to the actual conditions prevailing on the money markets of the member countries. In addition, the rules governing recourse to official ECU holdings within the exchange rate mechanism have been made more flexible, and third country central banks and certain international financial institutions have been given the possibility of holding official ECU. The growing use of the ECU as a vehicle for financial and commercial transactions, and the development of a huge financial market, which is dynamic and attractive to international investors, are likely to reduce the cost to Europe of external monetary shocks (see box on the private ECU).

Greater convergence of performance, an effective coordination of monetary policies, progress towards the freedom of capital movements, and the strengthening of the exchange rate mechanism together bear witness to a significant achievement over the last twelve months in the area of monetary and financial integration.

Exchange control measures
Commission Decisions under Article 108 of the Treaty

At its meeting on 19 December 1984 the Commission adopted four Decisions (OJ L 8 of 10 January 1985, pp. 29-37) concerning the application of the safeguard clause in Article 108 (3) of the Treaty. These Decisions were addressed to the four Member States (France, Italy, Ireland and Denmark) which had previously been authorized by the Commission to maintain restrictions on capital movements which would otherwise have been liberalized under the Council Directive of 11 May 1960 (First Directive for the implementation of Article 67 of the EEC Treaty), as amended by the Directive of 18 December 1962.

In the case of Denmark, the Commission repealed its Decision of 22 December 1977, since the protective measures authorized by that Decision had been withdrawn.

The other Member States concerned are still authorized to continue to apply certain protective measures with regard to capital movements which would otherwise have been liberalized.

In the case of Ireland, the authorized restrictions relate to the acquisition by residents of foreign securities dealt in on a stock exchange other than securities issued by Community institutions and the EIB.

In the case of France and Italy, the Commission Decisions feature new measures which relax earlier restrictions:

France

The requirement that direct investments of more than FF 2 million must be financed with foreign currency now applies only to 50 % of the operation (instead of 75 %). The requirement that residents acquiring foreign securities denominated in foreign currency must do so through the investment currency market no longer applies to the acquisition of securities denominated in ECU and issued by Community institutions and the EIB on the French market.

The limit on the personal transfers which residents may make abroad without justification has been increased to FF 1 500 a month per person. The construction or purchase of real property abroad by residents for second homes, gifts to non-residents and transfers abroad of the assets of French emigrants remain subject to authorization.

Italy

The relaxation affects the non-interest bearing deposit which residents wishing to effect certain investments abroad must lodge with the Bank of Italy: this has been reduced and the rules have been modified.

For investments in real estate, the deposit has been cut from 50 % to 40 % of the value of the property;

For investments in foreign securities dealt in on a stock exchange:

the deposit is reduced from 50 % to 40 % for the acquisition of securities which the resident undertakes to hold for more than a year;

it is cut to 30 % for the acquisition of securities issued by the Community institutions and the EIB, held for more than a year;

collective investment undertakings for transferable securities may put up to 10 % of their resources into foreign securities without making the deposit.

The Commission has fixed a period after which the Decisions should in principle expire (after two years in the case of France and three years in the case of Italy and Ireland). Beyond those periods, the authorization to maintain all or part of the protective measures in force may be extended only if those countries' balances of payments are still in difficulties or are seriously threatened with difficulties.

Main measures taken by the Member States

Independently of the Community requirements laid down in the above mentioned 1960 Directive, a number of Member States have taken steps to relax their exchange controls.

In Denmark, with effect from 1 July 1985, the authorities reduced from five years to one year the minimum period for which Danish enterprises other than financial institutions may contract loans abroad. The acquisition of unlisted foreign securities has also been authorized.

In France, the declaration formalities relating to direct investment were relaxed in November 1984. In March 1985 French importers were authorized to make forward foreign exchange purchases for a maximum period of six months with a view to paying for goods invoiced in ECU.

In Italy, the amount of loans which residents may contract abroad without prior authorization was increased in June 1985 to LIT 500 million for loans not exceeding five years and to LIT 3 000 million for loans of less than five years but with an average maturity of more than two years.

Tourism and other forms of travel

The Commission has informed those Member States which maintain exchange controls of the conclusions it has drawn from the judgment delivered by the Court of Justice on 31 January 1984 concerning transfers relating to tourism and other forms of travel (Joined Cases 286/82 and 26 83, Luisi-Carbone). The Commission's position is, in brief, that residents of the Member States must be put in a position to cover expenditure incurred abroad, whether this involves transfers through approved inter-

mediaries, the granting of flat-rate foreign currency allowances on departure (which may be exceeded subject to proof and possible *post facto* justification), or the local use of appropriate means of payment.

Major liberalizing measures were taken in this field in 1984 in France (permission to use credit cards and similar instruments abroad was restored) and in Italy (increase in the flat-rate allowance, residents being able to take with them without justification the equivalent of LIT 2 million per person and per trip; permission for credit cards and similar instruments to be used abroad). The Irish authorities have clarified their rules concerning the possibility of exceeding the flat-rate allowance and the use of credit cards beyond that limit.

The ECU market: developments and characteristics

The banking market

Using information provided by reporting European banks, the Bank for International Settlements now produces quarterly statistics[1] for the ECU banking market similar to those which it has compiled for a long time for the main currencies. After setting out below the ECU liabilities and assets of the banking system — in aggregate and broken down by activity sector — this section examines a number of the market's salient features.

Overall growth of ECU (in '000 million)

	Liabilities	Assets
December 1982	5,68	6,72
December 1983	12,09	14,38
March 1984	17,09	20,70
June 1984	20,52	25,99
September 1984	25,44	32,34
December 1984	31,45	39,49

Breakdown between the two sectors of banking activity (in '000 million ECU)

	Liabilities *vis-à-vis*:		Assets *vis-à-vis*:	
	Banking sector[1]	Non-banking sector	Banking sector	Non-banking sector
End December 1983	10,76	1,33	9,67	4,71
End March 1984	15,35	1,74	14,19	6,51
End June 1984	18,41	2,11	18,16	7,83
End September 1984	23,41	2,03	23,27	9,07
End December 1984	28,63	2,82	28,35	11,14

[1] The figures for the banking sector are obtained by deducting those recorded for non-banks from the totals in the first table above.

Source: Commission of the European Communities, based on dollar figures from the BIS and converted into ECU using the dollar ECU rates for the last working day of the month concerned.

Four characteristics of the market emerge from these statistics, from the study devoted to the ECU in the BIS annual report[2] and from observation of banking activity in this field.

The ECU is now well placed among the currencies used on the international banking market. Whereas European banks' assets and liabilities in other currencies are marking time or even falling, ECU business has been expanding considerably, particularly since the beginning of 1984 — the year in which ECU liabilities and assets overtook those denominated in pounds sterling, guilders and French francs; if, as is probable, they overtake those denominated in yen during the course of 1985, the ECU will then rank after the dollar, the German mark and the Swiss franc.

The breakdown between interbank operations and those with non-banks (depositors and borrowers) shows that the former take by far the larger share, with the interbank market accounting for more than 70 % of the total. This proportion — much greater, according to the BIS, than that recorded for other currencies except the yen — is due to the wide variety of operators on this market. The fact that borrowers are concentrated mainly in Italy and in France and depositors principally in Belgium and that only a few banks are feeding the market by putting together ECUs from the component currencies has necessitated the setting-up of a major interbank transfer system between the different banking centres active in the field of ECU operations.

The geographical enlargement of the ECU banking market beyond its present Belgian, Italian and French 'sanctuaries' which is regarded as one of the conditions of its further development, now appears to be developing progressively, both on the deposit and on the lending side. Deposits by Belgian residents are now down to 25 % of the total, while in the field of syndicated medium-term credits, the summer of 1985 saw such operations in some 15 countries, including the USSR, Hungary, India and Brazil. The formula increasingly proposed for syndicated bank loans is one in which the ECU is offered jointly or alternately with the dollar and is thus promoted on the international monetary scene.

[1] Quarterly bulletin of the Bank for International Settlements, Monetary and Economic Department: 'International banking activity, fourth quarter of 1984', April 1985.

[2] 55th annual report of the Bank for International Settlements (BIS) (Basle, 10 June 1985) pp. 148 to 155.

The ECU banking market is a net borrower: deposits are not growing sufficiently fast (a total of less than 3 000 million ECU at the end of 1984) to cover the rapid growth in lending (more than 11 000 million ECU at the same time). The shortfall has had to be made up by putting together ECUs from liabilities denominated in component currencies. This gap, which is continually widening and which currently represents almost three quarters of the loans granted, is filled by a few banks (notably those participating in the present clearing arrangements, which thus maintain the balance of the system).

Since it is always possible to switch between the ECU and its component currencies, the short-term ECU interest rates paid to and by major operators remain constantly close to the theoretical rates calculated on the basis of the rates for the component currencies.

2. Bond issues

From a total of 190 million ECU in five issues in 1981, ECU-denominated bond issues increased to 722 million ECU in 1982, to 1 935 million ECU in 1983, to 3 444,2 million ECU in 1984 and to 6 568 million for the first nine months of this year (including 4 290 million ECU for the first six months). The amount placed during the first three quarters is already twice the amount issued during the whole of the previous year. On the Euro-issue market, the ECU ranks third after the dollar and the German mark, while on the international market generally (which also includes issues of non-residents on domestic markets) it ranks fifth after the two currencies previously mentioned — the Swiss franc and the yen.

ECU bond issues on the international market
(by issuer group, in millions of ECU)

	1981	1982	1983	1984	1985 1
EEC	150	572	1 330	2 004	2 833
Rest of Europe	—	85	285	634	250
Rest of the world	40	65	320	806	1 207
Total:	190	722	1 935	3 444	4 290

Source: Commission of the European Communities

With regard to the structure of the market, the statistics show that, while Community issuers still account for the bulk of all operations, there has been a gradual widening of the circle of borrowers since 1984: issuers of ECU-denominated bonds number approximately 100 from 23 countries. The newcomers to this market include operators from New Zealand and Korea and the Inter-American Development Bank.

For the first nine months of 1985, Japanese issuers, either directly or through their subsidiaries, led the way in terms of number of issues, with 16 issues out of 80. Some of these issues were launched not on the international market but on the domestic financial markets in New York, Copenhagen, Amsterdam (bankbrieven) and Tokyo (private EEC placement).

Although no statistics are available, it is estimated that since the beginning of 1985, 75 % of issues have been placed outside Belgium and that 50 % have been placed with institutional investors, mainly from Switzerland, Japan, Scandinavia and the United States.

Interest rates fell to such an extent during the first half of the year (from just above 10 % to 8 ⅝ %) that they went below the short-term three-month rates. Since then, the situation has normalized: short-term rates have fallen, long-term rates have recovered and the most recent issues have been placed at rates which are more in line with the maturity profile. Although, at the long end, it is difficult to make any meaningful comparison between the actual yield and the theoretical yield computed from that of issues in each of the component currencies, certain statistics indicate that the premium which the observed rate has regularly shown over the calculated rate, narrowed in the early part of 1985, eventually giving way to a discount. This comparison between long-term market rates, observed short-term rates and long-term computed rates illustrates the actual autonomy of the rates at which ECU issues are floated.

3. Conclusions

Parallel with this growth in its market, the ECU has become more institutionalized since 1984: the ECU is now officially fixed on the foreign exchange markets of all the Member States (except for Germany) which have a fixing procedure, and also in Portugal. ECU issues, still very small in number, are quoted on all Community stock exchanges except for those in Germany, Ireland and Greece. The issues floated at the beginning of the year in the United States and the private placement made in Tokyo in June 1985 by the European Economic Community are probably forerunners of new developments on these markets. Both financial and commercial transactions can be carried out in almost all Member States, in many other European countries and in the United States, Canada, Japan and India. The fact that the ECU is beginning to be used for invoicing or paying for raw materials, for gas within the Community and for coal and paper pulp from the United States, demonstrates that the commercial use of the ECU is beginning to take off — a process which should be helped by the introduction of this currency unit on the financial futures markets.

5. Budgetary policy

In 1985, the budget deficit expressed as a proportion of GDP again fell slightly in the Community as a whole, because of the strict control of budget volumes, which for the first time in a long period was translated into a slight decrease in the weight of public expenditure in GDP. This trend, of which there were signs a year ago, has therefore been confirmed. The stance of budgetary policies has remained very cautious even if the slight increase in activity and the slowdown in inflation have slightly diminished their restrictive character. For the longer term, most Member States today have a dual ambition: to continue to limit budget deficits and to bring down, by stages, rates of taxation. In these circumstances we can expect, as a Community average, a gradual moderation in the increase in the weight of public debt in GDP. Although some Member States are in a position to stabilize fairly rapidly their public debt as a proportion of GDP, others will probably require far more time and effort to do so; they would be greatly helped if interest rates go on falling.

5.1. Budgetary trends and policies

The main feature of 1985 is that it continues to follow the trends of earlier years as regards the control of budget volumes and balances rather than steering a new course. The restoration of balance to public accounts is a long-term endeavour, so that the national authorities have directed their efforts at keeping the implementation of budgets within the limits set by the finance laws for 1985 and have been fairly successful in doing so, given the huge scale of expenditure resulting automatically from existing legislation. The maintenance of a strict control on public spending and budget deficits governs the success or implementation of plans to bring taxation down by stages, which are increasingly becoming the objectives of medium-term budget strategies in the Community. Reduction of the central government's weight in the economy, and more precisely of the proportion of resources which it collects and redistributes, is an element in the improvement of the Community's capacity for growth; but this is made more difficult to achieve because of the persistence of moderate growth which, if policies remain unchanged, is unlikely to increase significantly in 1986.

The slowdown in the advance of budget revenue and expenditure continued in 1985 (see Table 5.1) in parallel with the reduction in the rate of inflation and nominal growth. On the whole, and except for income from direct taxes and public debt interest charges, revenue and expenditure increased slightly less than the value of GDP. So, the proportion of current revenue in GDP, which had again increased in 1984, diminished slightly in 1985 as did the proportion of current expenditure and total expenditure (see Table 5.3). The Community's net borrowing fell by two-tenths of a percentage point of GDP in 1985 to stand at 5.2 %. This general trend of budget volumes is likely to continue in 1986 and to give rise to a further reduction in the share of budget expenditure and revenue in activity and to a further fall in net borrowing as a proportion of GDP.

The change, of which there were signs a year ago (see Chapter 6 of the 1984-85 Review, *European Economy* No 22) in the trend of public finance as a proportion of activity in the Community, is therefore being confirmed. But the final out-turn for 1984 is slightly down on that suggested last year by the preliminary estimates; in comparison with 1983, current revenue increased by a half a percentage point of GDP and total expenditure by three-tenths of a point, whereas a year ago these magnitudes were expected to remain virtually stable. However, average net borrowing did improve as forecast by one-tenth of a point in 1984. The fall in budget revenue and expenditure as a proportion of GDP, which last year was expected for 1985, has taken place: three-tenths of a point of GDP for current revenue and expenditure and one half of a point for total expenditure; similarly the budget balance has improved by two-tenths of a point compared with the six-tenths expected a year ago.

If we examine the same trends for each of the Member States, we see that the large majority of them in 1985 did indeed succeed in slightly reducing the share of public expenditure in GDP: only in Greece, Ireland and Italy did changes in the opposite direction occur. As regards receipts, however, the need to reduce structural deficits has caused six of the 10 Member States to go on increasing the burden of taxation. On the other hand, France, the Netherlands and the United Kingdom have purposely reduced the proportion of public revenue in GDP at the same time as that of public expenditure. In Ireland, the reduction in the weight of public revenue as a proportion of GDP observed in 1985 resulted from a more substantial than expected slowdown in the rhythm of tax receipts while expenditure continued to grow. Germany stabilized the burden of taxation in 1985 at the same time reducing the weight of her budget expenditure.

Table 5.1

General government revenue and expenditure,[1] EUR 10

	'000 million ECU	% change					% of GDP					
	1985[2]	1982	1983	1984	1985[2]	1986[3]	1975[4]	1980[4]	1983	1984	1985[2]	1986[3]
Indirect taxes	409.6	11.9	10.8	9.3	6.0	6.7	12.3	13.4	13.8	13.9	13.7	13.7
Direct taxes	391.7	14.2	10.1	9.3	8.0	5.9	11.5	12.3	13.0	13.2	13.2	13.1
Social security contributions received	461.6	14.5	11.2	8.3	6.7	7.0	13.5	14.5	15.5	15.6	15.5	15.5
Total taxes and social security contributions	1 262.9	13.6	10.7	8.9	6.9	6.6	37.3	40.2	42.3	42.7	42.4	42.3
Other current revenue	115.7	14.9	6.3	9.5	8.5	4.1	3.0	3.5	3.7	3.8	3.8	3.7
Total current revenue	1 378.6	13.7	10.3	9.0	7.0	6.4	40.3	43.7	46.0	46.5	46.2	46.0
Current transfers paid	687.8	14.9	9.8	8.3	6.6	5.1	20.0	21.0	23.2	23.3	23.1	22.7
Actual interest payments	152.3	22.8	15.4	14.5	9.8	6.6	2.6	3.6	4.9	5.2	5.3	5.3
Government consumption	568.9	10.9	9.4	7.6	6.5	5.5	18.2	18.5	19.4	19.3	19.1	18.9
Total current expenditure	1 409.1	14.0	10.2	8.6	6.9	5.4	40.8	43.1	47.5	47.8	47.5	46.9
Gross saving	− 30.5	—	—	—	—	—	− 0.5	0.6	− 1.5	− 1.3	− 1.3	− 0.9
Net capital transfers	32.5	13.2	22.6	22.9	− 4.4	2.8	0.9	1.1	1.1	1.3	1.1	1.1
Gross capital formation	81.0	7.5	5.6	5.3	5.2	6.7	4.0	3.2	2.9	2.8	2.8	2.8
Net lending (+) or borrowing (−)	− 144.0	—	—	—	—	—	− 5.4	− 3.7	− 5.5	− 5.4	− 5.2	− 4.8
Memorandum: nominal GDP	—	10.7	8.9	8.0	7.6	6.7						

[1] National accounts definition, exluding loans, advances and participations.
[2] Estimates.
[3] Forecasts.
[4] EUR 10, excluding Greece and Ireland.
Source: Commission services.

With regard to budget balances, the two-tenths of a point GDP reduction in the level of Community countries' net borrowing, as compared with 1984, conceals an improvement in the balance expressed as a percentage of GDP in six Member States and a deterioration in the other four (Greece, France, Ireland and Italy, see Table 5.4, section (a)). If we compare the trend of budget balances in the Member States since 1982 we see that Denmark has managed to cut its net borrowing substantially, from 9.3 % of GDP in 1982 to 2.9 % in 1985, by stabilizing expenditure as a proportion of activity but chiefly by raising the rate of tax and social security contributions. Germany, Luxembourg and the Netherlands have steadily improved their budget balance. Belgium did not really start to reduce its net borrowing until 1984 and in Ireland, the underlying fall in the deficit was interrupted in 1985. France, like the United Kingdom, shows no falling trend over these years, while Greece and Italy are not succeeding in checking the growth in net borrowing as a proportion of GDP. The scale of the deficits also differs sharply from one Member State to another, with Luxembourg, Germany, Denmark, France and the United Kingdom in the most favourable positions in 1985.

In order to refine slightly the assessment of budget trends, Table 5.4 also evaluates structural budget balances, using the method described in the last Annual Review (see *European*

Table 5.2

Member States' general government revenue and expenditure,[1] % change, 1984-86

	Total current revenue			Indirect taxes			Direct taxes			Social security contributions received			Other current revenue		
	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]
B	9,6	9,0	6,9	3,4	5,1	5,3	10,7	9,4	6,6	13,9	12,3	10,8	9,4	4,9	−8,3
DK	13,3	7,8	6,6	11,3	6,5	3,9	12,8	9,2	9,9	10,1	8,6	−7,3	22,0	5,4	5,8
D	5,3	4,6	4,9	5,4	3,7	5,2	6,3	6,1	3,6	4,8	4,3	6,0	3,8	4,5	3,2
GR	28,0	21,4	21,1	26,5	20,3	20,9	34,5	24,4	27,5	28,1	23,0	17,9	17,9	8,2	20,4
F	10,5	5,0	5,9	11,5	5,3	6,1	11,2	3,1	5,5	9,4	5,9	5,5	11,0	2,6	8,1
IRL	11,2	7,3	5,7	11,1	5,0	6,1	17,7	6,4	6,0	10,5	8,0	6,5	−4,7	17,7	2,7
I	13,5	11,6	10,2	15,0	10,0	10,0	12,7	12,0	9,3	13,1	10,0	11,5	14,4	28,9	8,2
L	6,5	6,2	5,5	7,9	8,0	5,4	5,0	5,7	4,6	5,8	5,2	5,5	9,0	5,2	8,0
NL	3,0	3,2	1,1	6,5	3,6	2,8	−1,6	3,2	4,0	−0,4	1,6	−1,0	14,3	6,1	−0,7
UK	7,3	7,5	5,2	6,9	5,7	6,7	8,0	9,3	4,1	8,7	7,4	7,0	4,1	8,0	−0,6
EUR 10	9,0	7,0	6,4	9,3	6,0	6,7	9,3	8,0	5,9	8,3	6,7	7,0	9,5	8,5	4,1

	Total expenditure			Current transfers paid			Actual interest payments			Government consumption			Net capital transfers and gross capital formation		
	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]
B	5,8	6,2	4,6	4,9	3,9	3,6	14,2	15,1	8,7	4,5	5,2	3,6	−2,1	2,7	4,5
DK	8,0	4,7	2,5	6,1	4,2	3,3	30,8	7,4	0,2	4,7	3,7	2,6	−7,0	8,8	2,3
D	4,1	3,0	4,1	3,6	2,7	3,3	5,1	5,5	4,5	4,1	4,0	4,6	6,6	−2,0	5,0
GR	29,9	27,9	15,0	24,6	22,6	15,9	57,3	49,3	19,8	24,7	26,7	14,0	53,2	30,4	11,5
F	9,8	5,9	5,9	10,8	6,8	5,9	16,2	8,1	8,7	9,1	5,3	5,9	0,0	−0,7	4,1
IRL	7,8	10,5	3,8	9,7	8,4	3,6	13,0	21,7	3,4	7,5	7,0	3,4	−8,3	10,7	7,7
I	15,8	11,7	8,5	11,9	13,5	7,4	21,3	10,9	9,5	14,6	11,0	7,5	26,6	8,5	13,5
L	3,7	5,0	5,8	5,1	5,5	5,2	24,8	18,4	14,1	6,4	5,1	7,3	−7,3	1,3	3,2
NL	2,7	2,6	2,3	2,3	2,0	2,9	10,5	9,2	5,9	−0,9	1,6	0,3	11,1	1,9	0,9
UK	7,8	6,2	4,2	9,9	6,1	3,6	10,2	9,8	4,7	6,0	6,7	5,8	6,1	−3,4	−7,1
EUR 10	8,8	6,6	5,4	8,3	6,6	5,1	14,5	9,8	6,6	7,6	6,5	5,5	10,2	2,3	5,6

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

Source: Commission services.

Economy No 22, section 6.2). The cyclical component of the Community's budget deficit (Table 5.4, section (b)), calculated in relation to the average growth trend over the economic cycle, became slightly positive in 1985, thus indicating that the current recovery has spontaneously contributed to an 0,2 point of GDP improvement in the budget deficit. Consequently, the autonomous component of the deficit (section (c)) was slightly magnified to 5,4 % of GDP for the Community as a whole in 1985 compared with 5,1 % in 1984. Over the same year, only Belgium, Denmark and Germany have, according to these calculations, cut their autonomous deficit. Debt interest charges (section (d)) went on increasing in 1985 but markedly more slowly than in earlier years and represented 4,4 % of GDP compared with 4,3 % the year before; Denmark and the United Kingdom did, however, register a fall in their interest charges as a proportion of activity. If we take account of the inflation adjustment corresponding to the inflation tax to which holders of public-sector assets are subject (here calculated as the difference between the nominal debt interest charge (section (d)) and the real charge established on the basis of a real medium-term interest rate (section (e)), the budget

Table 5.3

Member States' general government revenue and expenditure,[1] as % of GDP, 1984-86

	Total current revenue			Indirect taxes			Direct taxes			Social security contributions received			Other current revenue		
	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]
B	47,3	48,4	48,7	11,6	11,5	11,4	19,3	19,8	19,9	14,2	14,9	15,5	2,2	2,2	1,9
DK	55,9	56,6	57,2	18,0	18,0	17,7	27,3	28,0	29,2	2,9	3,0	2,6	7,7	7,7	7,7
D	46,4	46,5	46,2	13,0	12,9	12,8	12,2	12,4	12,2	17,5	17,5	17,6	3,7	3,7	3,6
GR	33,2	33,7	35,0	15,5	15,7	16,2	6,0	6,2	6,8	10,3	10,7	10,8	1,3	1,2	1,2
F	49,8	48,9	48,9	15,1	14,8	14,9	9,4	9,1	9,0	21,6	21,4	21,4	3,7	3,6	3,6
IRL	42,5	41,9	41,2	17,6	17,0	16,8	14,8	14,5	14,2	5,7	5,7	5,6	4,4	4,7	4,5
I	45,1	45,4	45,7	11,3	11,2	11,3	15,3	15,4	15,4	16,2	16,1	16,4	2,3	2,6	2,6
L	56,6	56,7	56,2	15,7	16,0	15,9	19,2	19,2	18,8	14,6	14,5	14,4	7,1	7,1	7,2
NL	55,3	54,6	53,5	12,0	11,9	11,8	12,9	12,8	12,9	21,0	20,4	19,6	9,4	9,5	9,2
UK	42,0	41,4	40,7	16,5	16,0	15,9	14,6	14,6	14,3	7,0	6,9	6,9	3,9	3,9	3,6
EUR 10	46,5	46,2	46,0	13,9	13,7	13,7	13,2	13,2	13,1	15,6	15,5	15,5	3,8	3,8	3,7

	Total expenditure			Current transfers paid			Actual interest payments			Government consumption			Net capital transfers and gross capital formation		
	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]	1984	1985[2]	1986[3]
B	57,2	57,0	56,1	26,0	25,3	24,7	10,1	10,9	11,1	17,9	17,6	17,2	3,3	3,2	3,1
DK	60,5	59,6	57,9	22,2	21,7	21,3	9,5	9,6	9,1	25,9	25,3	24,6	2,8	2,9	2,8
D	48,3	47,7	47,0	21,2	20,8	20,4	3,0	3,0	3,0	20,1	20,0	19,8	4,1	3,8	3,8
GR	43,1	46,2	45,5	15,2	15,7	15,5	4,3	5,4	5,5	19,0	20,2	19,7	4,6	5,0	4,8
F	52,6	52,1	52,2	30,2	30,2	30,2	2,8	2,8	2,9	16,4	16,2	16,2	3,2	2,9	2,9
IRL	52,6	53,4	51,6	19,9	19,8	19,1	9,5	10,7	10,3	18,9	18,6	17,9	4,1	4,3	4,3
I	58,7	59,0	58,5	22,9	23,4	23,0	9,6	9,6	9,6	19,4	19,5	19,1	6,6	6,5	6,8
L	55,2	54,6	54,3	29,8	29,6	29,3	1,1	1,2	1,3	16,1	16,0	16,1	8,2	7,9	7,7
NL	61,6	60,5	60,1	33,5	32,7	32,6	6,1	6,3	6,5	16,8	16,3	15,9	5,4	5,2	5,1
UK	45,9	44,7	43,5	16,5	16,0	15,5	4,9	4,9	4,8	21,8	21,3	21,1	2,7	2,4	2,1
EUR 10	51,9	51,4	50,8	23,3	23,1	22,7	5,2	5,3	5,3	19,3	19,1	18,9	4,1	3,9	3,9

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

Source: Commission services.

deficit adjusted both for the cycle and for inflation (section (f)) increased slightly in 1985 to 2,3 % of GDP in 1985 compared with 2,0 % in 1984. In contrast to this general trend, the structural deficit, measured similarly, fell in Belgium and Denmark and the structural surplus increased in Luxembourg.

All in all, this evaluation of structural budget balances shows that the strengthening of the economic recovery in the Community and the slowdown of inflation have slightly relaxed the restrictiveness of budgetary policies and slightly improved their contribution to growth.

The medium-term budget guidelines set by most of the Member States and which generally define the indicative framework for the desired trend of public finances have not been greatly changed in comparison with 1984, even though the target dates are sometimes slightly longer.

This is particularly the case for Belgium and Ireland, where the targets for the reduction of budget deficits set for 1987 have been postponed or relaxed. Italy intends to eliminate the current Treasury deficit and to stabilize Treasury debt as a percentage of GDP by 1990. Denmark hopes to present a balanced central government account by the end of the

Table 5.4

General government structural budget balances

(% of GDP)

	(a) Net lending (+) or borrowing (−)					(b) Cyclical impact on the budget balance					(c) Budget balance adjusted for effects of the cycle (c = a − b)				
	1982	1983	1984	1985[1]	1986[2]	1982	1983	1984	1985[1]	1986[2]	1982	1983	1984	1985[1]	1986[2]
B	−11,1	−11,7	−9,9	−8,6	−7,4	0,3	−0,6	−0,2	0,1	0,4	−10,8	−11,1	−9,7	−8,7	−7,8
DK	−9,3	−7,4	−4,6	−2,9	−0,7	−0,9	−1,0	0,0	0,5	1,0	−8,4	−6,4	−4,6	−3,4	−1,7
D	−3,4	−2,5	−1,9	−1,2	−0,8	−0,7	−1,0	−0,5	0,1	0,9	−2,7	−1,5	−1,4	−1,3	−1,7
GR	−9,4	−8,9	−9,9	−12,5	−10,5	−0,4	−0,7	−0,2	0,2	0,5	−9,0	−8,2	−9,7	−12,7	−11,0
F	−2,5	−3,1	−2,8	−3,2	−3,3	0,1	−0,1	0,0	−0,1	0,2	−2,6	−3,0	−2,8	−3,1	−3,4
IRL	−14,2	−11,8	−10,1	−11,5	−10,4	0,2	−0,6	−0,1	0,1	0,2	−14,4	−11,2	−10,0	−11,6	−10,6
I	−12,7	−12,4	−13,5	−13,6	−12,8	0,1	−1,1	−0,6	0,0	0,5	−12,8	−11,2	−13,0	−13,6	−13,3
L	−1,3	0,0	1,5	2,1	1,9	−0,3	−1,8	−0,5	0,2	1,0	−1,0	1,8	1,9	1,9	0,9
NL	−7,1	−6,5	−6,3	−5,9	−6,5	−1,3	−1,3	−0,5	0,4	1,2	−5,8	−5,2	−5,8	−6,3	−7,7
UK	−2,4	−3,6	−3,8	−3,3	−2,8	−1,3	−0,4	−0,4	0,6	1,0	−1,1	−3,2	−3,4	−3,9	−3,8
EUR 10	−5,6	−5,5	−5,4	−5,2	−4,8	−0,5	−0,7	−0,3	0,2	0,7	−5,1	−4,8	−5,1	−5,4	−5,5

	(d) Net interest payments (interest paid less interest received)[3]					(e) Theoretical real charge on public debt[4]					(f) Budget balance adjusted for effects of the cycle and inflation (f = c + d − e)				
	1982	1983	1984	1985[1]	1986[2]	1982	1983	1984	1985[1]	1986[2]	1982	1983	1984	1985[1]	1986[2]
B	9,3	9,4	10,1	10,9	11,1	3,1	3,4	3,7	3,9	4,1	−4,6	−5,1	−3,3	−1,7	−0,8
DK	2,6	4,3	5,8	5,6	5,4	1,0	1,6	2,0	2,2	2,3	−6,8	−3,6	−0,9	0,0	1,4
D	2,0	2,3	2,3	2,3	2,4	0,6	0,7	0,7	0,8	0,8	−1,3	0,1	0,2	0,2	−0,1
GR	2,6	3,4	4,3	5,4	5,5	1,2	1,3	1,4	1,7	1,9	−7,6	−6,1	−6,8	−9,0	−7,4
F	1,3	1,8	2,0	2,1	2,1	0,2	0,3	0,3	0,4	0,5	−1,5	−1,5	−1,2	−1,4	−1,8
IRL	9,1	9,4	9,5	10,7	10,3	3,2	3,4	3,8	4,1	4,3	−8,5	−5,2	−4,3	−5,0	−4,6
I	7,7	8,4	9,1	9,2	9,4	1,9	2,0	2,0	2,5	2,7	−7,0	−4,8	−5,9	−6,9	−6,6
L	0,9	0,9	1,1	1,2	1,3	0,5	0,6	0,6	0,6	0,7	−0,6	2,1	2,4	2,5	1,5
NL	5,1	5,7	6,1	6,3	6,5	1,8	2,0	2,2	2,4	2,5	−2,5	−1,5	−1,9	−2,4	−3,7
UK	3,3	3,2	3,5	3,4	3,2	0,8	1,0	1,2	1,2	1,2	1,4	−1,0	−1,1	−1,7	−1,8
EUR 10	3,7	4,0	4,3	4,4	4,5	1,0	1,1	1,2	1,3	1,4	−2,4	−1,9	−2,0	−2,3	−2,4

[1] Estimates.
[2] Forecasts.
[3] B, GR, IRL, L, NL: interest paid.
[4] B, GR, IRL, L, NL: real charge on gross debt; DK, D, F, I, UK: real charge on net debt.

Sources: Commission services.

decade. The United Kingdom, in its Medium-Term Financial Strategy, has adopted a target of around UKL 7 000 million until 1988-89 for the public sector borrowing requirement, reflecting a relative fall as a percentage of GDP. Germany and the Netherlands also wish to go on reducing their budget deficits as a percentage of GDP while France has kept its target of a deficit limited to 3 % of GDP. Greece has decided to reduce its total public sector deficit by 4 percentage points of GDP in 1986 on the 1985 level. Lastly, Luxembourg intends to use her budget surplus to rebuild the budget reserves intended for investment.

This framework for the evolution of budget deficits over the next few years is strengthened by the desire to keep the rate of increase in public expenditure below the nominal growth rate. In Denmark and the United Kingdom, the aim is actually to keep public expenditure constant in volume terms, while in Germany the nominal growth of public expenditure is to be limited to a maximum of 3 %.

Thus although 1985 overall confirms in general the change noted last year for the budget outturn and trends, certain new elements seem to be appearing on the horizon — cer-

tainly as regards intentions concerning, in particular, the taxation component of budgetary policies. The Commission's annual economic report 1984-85, adopted by the Council in December 1984, recommended that the total public authority tax burden should fall by one percentage point of GDP a year from 1985 to 1987. The idea of the interest of tax-cutting plans is also gaining ground among the Member States. France, which in 1985 reduced taxation and social security contributions by the equivalent of 1 % of GDP, is preparing to cut the taxation of personal incomes in 1986. The draft Netherlands budget for 1986 provides for a one percentage point cut in the rate of company taxation. On 1 January 1986 Germany will apply the first part of her tax-cutting plan which was decided in 1984. Several other Member States have stated their intention of reducing taxes in the more or less immediate future: Belgium adopted in summer 1985 a multiannual plan for reducing taxation over the period 1986-89; the Danish Government is proposing a major tax reform to take effect from January 1987 which would reduce the pressure of taxation on households but would increase it on companies, and Luxembourg is also planning to reduce taxation in 1987. The United Kingdom Government is also considering a tax-cutting programme spread over several years and starting with the next budget. These proposals are in keeping with the strategies for coherence in the medium term presented above: they therefore imply a package of measures on the expenditure side which has not yet been defined in great detail in every case.

On 1 July 1985 the Commission adopted a communication to the Council on the budgetary policies of Member States[1] in which it examined the policies pursued and considered the possible role of budgetary policy in the implementation of a more employment-creating growth strategy. This would mean a shift in the structure of budget revenue and expenditure and direct measures to promote employment, while respecting the particular situation of each country. Within the framework of an overall macroeconomic strategy, a policy of wage moderation coupled with a temporary budgetary policy contribution to demand, where the margin exists, would enable the Community to increase its growth potential. For it to bear fruit, this change in budgetary policies should be accompanied by a stability-oriented monetary policy and backed by a constructive dialogue between the two sides of industry.

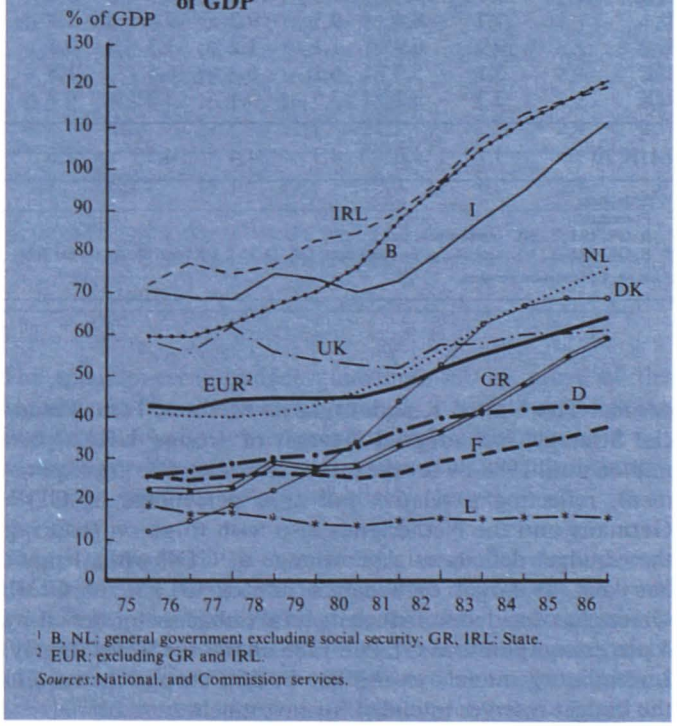
5.2. Trends in public debt

The outturn and guidelines of budgetary policies must also be assessed in the light of the trends of stock variables. It must be possible for economic systems to finance, in an orderly fashion, the repetition of budget deficits and therefore the constitution of public debt if they are not to suffer imbalances, particularly in the form of high interest rates which hamper growth. If the scale of budget deficits is such that the constitution of new debt as a percentage of GDP is greater than the (inverse) influence of economic growth on the share of public debt in GDP, the result is an increase in public debt as a proportion of GDP. The danger is that this increase in the proportion of debt, if it applies to an already high level of debt, will require the mobilization of excessive resources for use by government, thus diverting finance from the productive sector of the economy, and will induce excessively high external indebtedness and real interest rates.

Section 6.3 of the annual economic review 1984-85 (*European Economy* No 22, page 133) presented an appraisal of the extent to which budget deficits could be sustained in the light of the trend of public debt. The analysis showed that three Member States — Belgium, Ireland and Italy — were, on a 1985 horizon, the most inclined, given the high level of, and the increase in, their public debt, to experience financing imbalances which would harm their capacity for growth.

Projections of the weight of public debt in 1986 presented in Graphs 5.1 and 5.2 have been established on the basis of

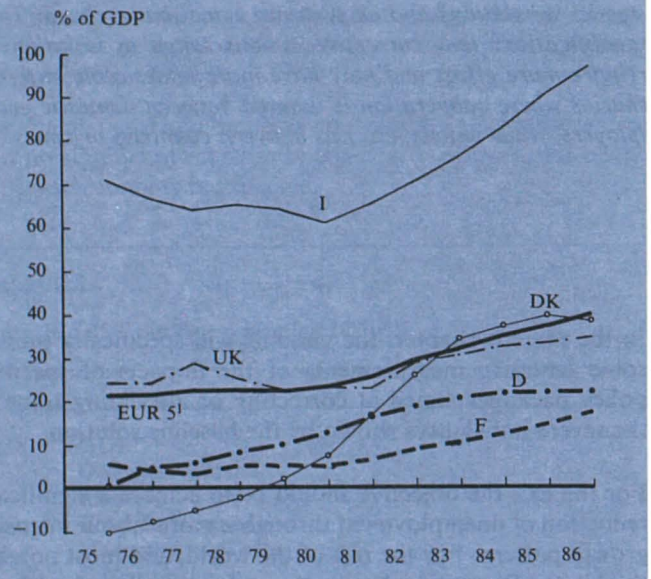
GRAPH 5.1: **Trend in general government gross debt[1] as % of GDP**



[1] B, NL: general government excluding social security; GR, IRL: State.
[2] EUR: excluding GR and IRL.
Sources: National, and Commission services.

[1] The economic outlook for 1986 and the Member States' fiscal policies, COM(85) 336 final of 1 July 1985.

GRAPH 5.2: **Trend in general government net debt as % of GDP**



[1] EUR 5: DK, D, F, I, UK.
Sources: National, and Commission services.

budgetary forecasts. They confirm the extent of the problem in the three Member States mentioned above: their gross public debt[2] could still grow as a proportion of GDP in 1986. The reduction expected in net borrowing as a percentage of GDP could still be insufficient, taking into account the nominal growth expected, to stabilize the weight of public debt. The Netherlands could also see an increase in public debt as a percentage of GDP and Greece has registered a substantial increase in public debt for several years and the level could reach 60 % of GDP in 1986. The other Member States are in a relatively more favourable position: Denmark, Germany and Luxembourg could stabilize or even reduce their public debt burdens in 1986, which for Denmark represents a considerable turnaround from the trend at the beginning of the 1980s. France could register an increase in the weight of public debt in 1986 which would bring this closer to that of Germany. In the United Kingdom the increase in the debt/GDP ratio should continue at the modest rate of previous years. Graph 5.2, which contains net public debt[3] for the Member States publishing such series, shows similar trends to those in Graph 5.1.

From this comparison of positions on public debt, it is the countries with the greatest proportion of debt which meet with the most difficulties in stabilizing it. These countries have for a long time tolerated budget deficits on a far larger scale than that which, given the economic growth rate to be expected, would, in the relatively near future, have stabilized the ratio of public debt to GDP. The effort to be made in respect of expenditure, excluding interest payments, should be particularly vigorous given the scale of debt interest charges. The prospects for interest rates are at this level a strategic variable: if rates were to fall, the process of adjustment towards the stabilization of the weight of debt could be accelerated. Several Member States have already been able to consolidate their debt at reduced interest rates as a result of the fall in long term rates which took place in the first half of 1985: this has been the case in Belgium, Denmark and France, in particular as regards the foreign currency component of their public debt. If rates were to go on falling, the weight of debt interest charges could be reduced and at the same time the Community economies' capacity for growth would be reinforced. It is, however, evident that the principal condition to be fulfilled in order to arrive at a more satisfactory situation lies in a substantial reduction in existing deficits.

[2] Gross debt of general government except for GR and IRL (State), B and NL (general government excluding social security). *Source:* Financial accounts, amounts outstanding D, F, I, UK; Central Bank for DK, public accounts for B, GR, IRL, L, NL.

[3] Net debt of general government: net debt is defined as the difference between monetary and financial liabilities and assets of general government. *Source:* Financial accounts, amounts outstanding D, F, I, UK; Central Bank for DK.

6. The medium term: central projection and policy scenarios

The world economy shows at present serious disequilibria in the main trading zones or countries: the EC has a very high unemployment rate, the US considerable internal and external deficits, Japan a very large trade balance surplus. This chapter sets out some scenarios starting from a baseline projection in which these disequilibria are not corrected. These scenarios are based on model simulations and as such are somewhat stylized. They show, however, with all due qualifications that corrective actions taken in isolation by individual zones or countries require more effort and may have more undesirable external spillovers than cooperative scenarios where cooperation is assured between domestic economic agents (governments, employers, trade unions, etc.) as between countries or zones.

6.1. Introduction

Medium-term projections may be made along two different lines of approach. The first approach may be called 'normative' in the sense that it defines target values for some economic and/or social aggregates and describes explicitly those policy actions deemed essential for reaching the targets. Medium-term plans or programmes typically follow this approach.

The second approach, to which the baseline projection in this chapter belongs, may be called 'descriptive' since it analyses a possible evolution of a given economic system, should the behaviour of economic agents and the stance of economic policy remain broadly the same in the future as in the recent past. Such projections are therefore sometimes called 'constant-policy' scenarios.

Normative and descriptive projections are both surrounded with considerable uncertainty. In the former, the political will and social consensus needed to implement the required policy measures may in reality not be forthcoming. As to the latter, behaviour and policy stances may in fact change. Furthermore, both are subject to external, non-controllable conditions that may not turn out as expected.

It is therefore hardly possible or at least extremely difficult to produce reliable forecasts for the medium term that could truly be considered as *the* most probable outcome. A more modest approach is to start from a baseline scenario which is not a forecast but a technical extrapolation of past trends and present economic policy settings. From the baseline may then be derived alternative scenarios showing the implications for a given country or zone of:

(a) domestic policy adjustment;
(b) changes in the international environment;
(c) any combination of (a) and (b).

In the present chapter, the variants will specifically present some tentative measurements of the impacts of specified policy packages aimed at correcting or alleviating some of the severe imbalances shown by the baseline solution.

For the EC, the objective should be to achieve a significant reduction of unemployment through a more labour intensive growth pattern. For the rest of the world, and most notably the United States and Japan, the variants will explore some of the ways and means of providing a reduction of excessive balance of payments surpluses or deficits.

Both baseline and variants are based on macroeconometric model simulations.[1] Given space limitations, the analysis will present only aggregate EC results, completed by the most relevant US, Japan and rest of world macroeconomic indicators when and where needed.

6.2. Baseline projection, 1986-90

The main assumptions underlying the baseline projection may be summarized as follows:

In the EC, fiscal policies remain restrictive in order to reduce or stabilize public budget deficits during the projection period. In real terms, public current and capital expenditures are therefore growing at about 1 % per year on average between 1986 and 1990. There is no reduction in average taxes and social contribution rates. Monetary policy stays on a stability-oriented path with no substantial reduction in interest rates and money supply growing at about the same rate as nominal GDP. Finally, the demographic projections show a significant reduction in the growth rate of population in working-age group from an average of 0,9 % 1985/80 to 0,15 % 1990/86.

[1] A short description of the model used is given in the appended box.

For the US, the assumption is made that no strong corrective action is taken at the level of the Federal budget deficit, contributing to the maintenance of high nominal and real interest rates. Similarly, no loss of confidence in the dollar is assumed and exchange rates vary little, showing an average devaluation in the dollar effective exchange rate by about 1,6 % per year 1990/86.

For Japan, fiscal and monetary policies are also conservative and no significant increase in the degree of openness of the Japanese economy is expected.

In the rest of the world, the real price of oil (in dollar terms) is supposed to stabilize to zero growth after 1985. Similarly, no major debt crisis or protectionist upsurge is assumed, keeping the non-EC world import demand on a trend rate of growth of 5 % 1990/86.

As might be expected, these assumptions lead to a world picture for 1986-90 which poses serious questions of its sustainability (see Table 6.1)

Table 6.1

Scenario 6.0 — Baseline projection 1986-90

		1985	1986	1987	1988	1989	1990
EUR	GDP	2,3	2,3	2,5	2,6	2,6	2,7
	Domestic demand	1,7	2,1	2,3	2,5	2,5	2,6
	Inflation	4,5	4,4	4,3	4,2	4,2	4,3
	Total employment	0,0	0,1	0,3	0,5	0,5	0,4
	Unemployment rate	18,8	11,0	11,0	10,9	10,7	10,4
	Current balance	0,4	0,5	0,5	0,6	0,5	0,5
	Budget balance	−4,8	−4,7	−4,4	−4,1	−3,9	−3,8
	Exchange rate (ECU/USD)	3,5	−1,6	−1,6	−1,5	−1,5	−1,5
	Interest rate (long)	10,8	11,0	11,0	10,8	10,8	10,7
USA	GDP	3,0	2,5	3,0	3,1	3,2	3,1
	Domestic demand	3,5	2,8	3,2	3,2	3,1	3,1
	Inflation	5,2	5,1	5,3	5,4	5,5	5,6
	Unemployment rate	7,2	7,3	7,1	6,6	6,5	6,3
	Current balance	−3,6	−3,7	−3,8	−4,0	−4,1	−4,0
	Budget balance	−5,1	−5,0	−5,0	−4,9	−4,9	−4,8
	Exchange rate index	−4,8	1,6	1,6	1,6	1,6	1,6
	Interest rate (long)	12,5	12,0	11,9	12,0	12,1	12,1
Japan	GDP	4,6	4,2	4,2	4,4	4,3	4,4
	Domestic demand	3,9	4,0	3,6	4,0	3,9	4,0
	Inflation	3,0	2,7	3,2	3,1	3,0	3,1
	Unemployment rate	2,1	2,2	1,9	1,0	1,7	1,7
	Current balance	2,7	3,0	3,1	3,2	3,3	3,2
	Budget balance	−3,5	−3,1	−3,1	−3,0	−2,9	−2,7
	Exchange rate (Yen/USD)	4,6	−3,5	−3,5	−3,5	−3,5	−3,5
	Interest rate (long)	6,9	6,7	6,7	6,8	6,8	6,9

Rate of growth, except interest rate, unemployment rate (% level) and balances (% GDP).

In the EC, the growth of real GDP stabilizes around its post-1973 trend, i.e. 2,5 % per year 1990/86. Inflation remains under control at 4,3 %. The public sector borrowing requirement decreases regularly from 4,7 % of GDP in 1986 to 3,8 % in 1990 and the current balance is kept in slight surplus.

However, this leaves the major disequilibrium in the EC unchanged. Given the moderate average growth rate, and assuming no change in wage behaviour, labour demand increases by only 0,4 % on annual average from 1986 to 1990. The unemployment rate therefore stays above 10 % of the active population over the whole period. In fact, the slight decrease registered in 1990 (10,4 % versus 11 % in 1986) results mostly from the easing of demographic pressures in labour supply and might be wiped out by any unexpected increase in participation rate.

For the US, GDP growth averages 3 % 1990/86 and the unemployment rate remains significantly lower than Europe

(6,3 % in 1990). However, in line with the assumptions, the Federal budget deficit is hardly reduced and the current account deficit continues to grow as a share of GDP from −3,7 % in 1986 to −4,0 % in 1990, despite the fact that real exports are growing faster than real imports from 1986 to 1990. The critical factor here is in the conversion of the net creditor position of the US into a net debtor: given the continuous accumulation of outstanding foreign liabilities in order to finance the current account deficits, the stock of external debt reaches USD 1 200 000 million in 1990 (i.e. 21 % of GDP) and net external interest payments grow from negligible amounts in 1985-86 to more than 100 000 million dollars in 1990, i.e. 20 % of nominal export receipts.

Japan continues to register rates of growth larger than 4 % (4,3 % 1990/86) together with low inflation and unemployment rates. The current balance surplus, however, remains very large at +3,2 % of GDP.

Finally, the rest of the world also benefits from net interest outflows from the US and is able to convert its 1986 current balance deficit into a slight surplus (0,4 % of GDP) at the end of the period.

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These current balance figures continue the present statistical discrepancy in the aggregated world current balance (about −USD 100 000 million) which is left unallocated. Thus all regions together must in reality be in a better current account position than indicated but of course it is impossible to distribute these credits by country or region.

6.3. US adjustment alone

The scenarios proposed in this section present the implications of the US making adjustments in the absence of any explicit accompanying actions in the non-US world. For clarity, these policy shocks will first be presented in isolation and may seem somewhat unlikely. A more plausible composite scenario will therefore be described later. In order to avoid a somewhat fastidious enumeration of figures, results are presented in graph form for the EC and the US, the text keeping to the main comments (see Graph 6.1).

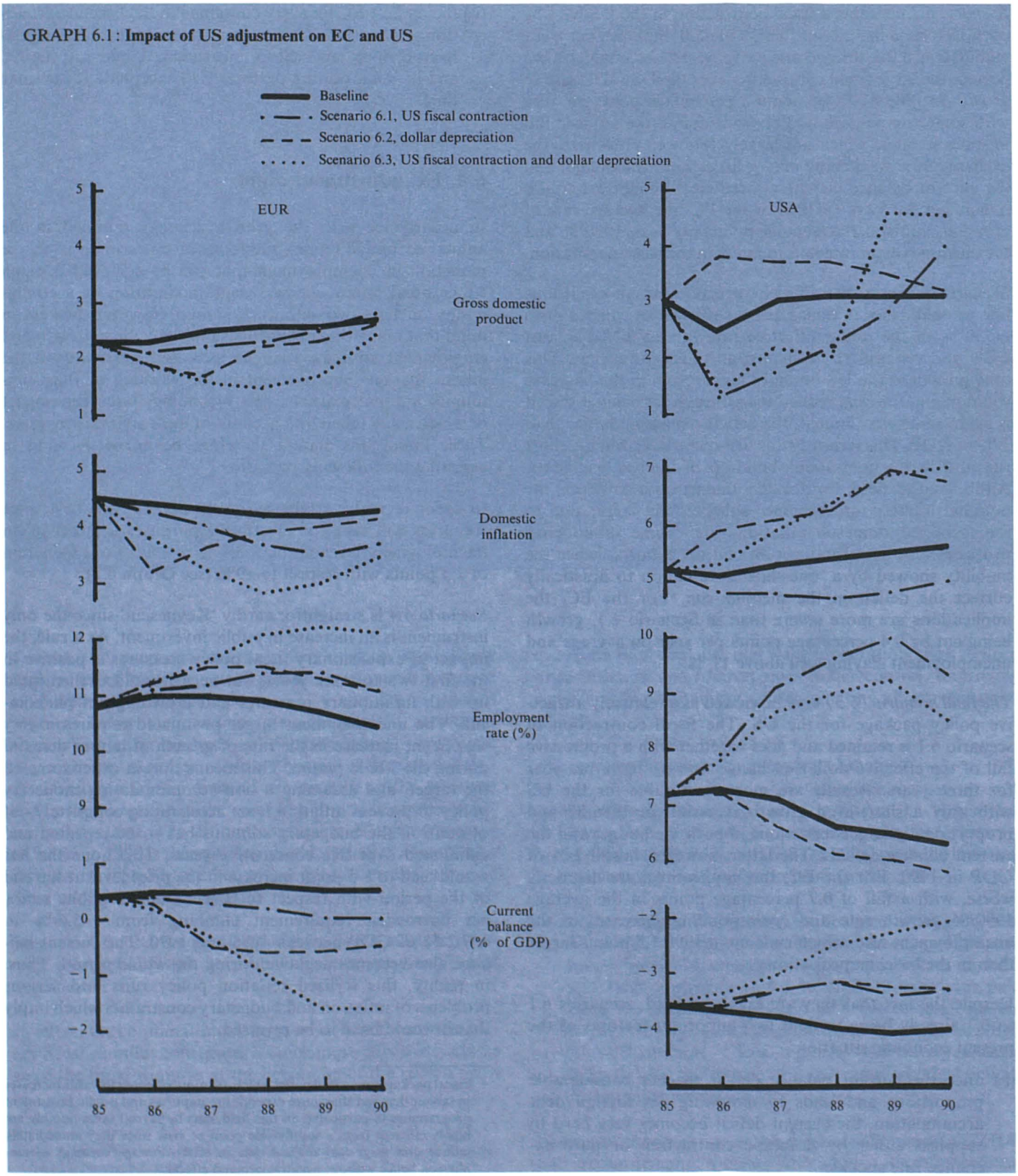
Table 6.2

Scenario 6.8 — World composite scenario

		1985	1986	1987	1988	1989	1990
EUR	GDP	2,3	3,1	3,6	3,9	3,4	3,4
	Domestic demand	1,7	3,2	3,9	4,1	3,4	3,4
	Inflation	4,5	4,1	3,6	3,7	3,7	3,5
	Total employment	0,0	0,3	0,8	1,3	1,7	1,5
	Unemployment rate	10,8	10,8	10,4	9,5	8,3	7,0
	Current balance	0,4	0,4	−0,2	−0,6	−1,0	−0,9
	Budget balance	−4,8	−4,9	−4,9	−4,9	−4,4	−4,0
	Exchange rate (ECU/USD)	3,5	−9,5	−9,7	−9,6	−0,2	0,1
	Interest rate (long)	10,8	9,5	9,1	8,3	7,7	7,0
USA	GDP	3,0	2,7	3,0	3,3	4,3	3,8
	Domestic demand	3,5	2,4	2,6	3,9	3,9	3,8
	Inflation	5,2	5,2	6,0	6,6	7,0	7,1
	Unemployment rate	7,2	7,4	7,1	6,5	5,8	5,0
	Current balance	−3,6	−3,4	−2,6	−2,2	−1,4	−1,3
	Budget balance	−5,1	−4,5	−3,9	−3,2	−3,0	−2,9
	Exchange rate index	−4,8	8,9	8,8	8,8	1,3	1,3
	Interest rate (long)	12,5	10,5	10,1	9,5	9,0	9,1
Japan	GDP	4,6	4,9	4,9	5,3	4,5	4,0
	Domestic demand	3,9	5,2	4,4	5,0	4,3	4,1
	Inflation	3,0	2,6	3,0	3,3	3,3	3,3
	Unemployment rate	2,1	2,0	1,7	1,7	1,6	1,5
	Current balance	2,7	2,5	2,4	1,1	0,8	0,8
	Budget balance	−3,5	−4,0	−4,8	−5,1	−4,9	−4,4
	Exchange rate (Yen/USD)	4,6	−18,5	−18,4	−18,6	−3,6	−3,7
	Interest rate (long)	6,9	6,0	5,8	5,0	4,4	4,9

Rate of growth, except interest rate, unemployment rate (% level) and balances (% GDP).
For policy setting, see section 6.5.

GRAPH 6.1: Impact of US adjustment on EC and US



Scenario 6.1 contains a fiscal contraction in the US by 1 % of GDP *ex ante* (about USD 50 000 million) per year cumulatively for three consecutive years. As could be expected, the large fiscal contraction cuts the US GDP rate of growth in 1986-87-88 by about 1 percentage point per year with some compensation afterwards due to the induced fall in interest rates, which are largely followed elsewhere, the exchange rate weakening only a little. Both the budget and the current balance deficits are reduced, but the latter still remains at 3,3 % of GDP. For the EC, the average rate of growth is cut by 0,2 percentage points per year, 1990/86 and the unemployment rate fails to fall as in the baseline solution.

Scenario 6.2 assumes no fiscal correction but an exogenous loss of confidence in dollar assets sufficient to cause a drop of 20 % in the dollar effective rate (about 30 % against ECU and yen and 10 % against all other currencies). This time growth in the US becomes higher than in the basecase solution, but the final reduction in the current balance deficit is again somewhat limited, the deficit remaining larger than 3 % of GDP. This is mostly due to J-curve effects in the short run and to the continuous build-up of interest payments. Although the need for foreign financing is lowered, the nominal interest rate becomes substantially larger due to the increased domestic inflation rate. These inflationary processes also act negatively on real net exports, hence the inability showed by a 'one-shot' devaluation to drastically correct the deficit in the medium-run. For the EC, the implications are more severe than in Scenario 6.1, growth being cut by 0,4 percentage points per year on average and unemployment staying well above 11 %.

The final scenario (6.3) may be viewed as a relatively attractive policy package for the US. The fiscal contraction of scenario 6.1 is retained and goes together with a progressive fall of the effective dollar exchange rate by 10 % per year for three years. Results are more favourable for the US with only a short-lived growth recession in 1986-87 and proportionally larger reductions in both the budget and the current balance deficits. The latter, however, is still 2 % of GDP in 1990. For the EC, the implications are distinctly worse, with a fall of 0,7 percentage points in the average 1990/86 growth rate and corresponding increases in the unemployment rate, which ends up in 1990 1,5 points larger than in the baseline projection.

Despite the fact that they are highly stylized, scenarios 6.1 to 6.3 already bring to light two important features of the present economic situation:

(a) once the current balance deficit reaches considerable proportions and leads to mounting net foreign debt accumulation, the current deficit becomes very hard to suppress either by domestic contraction or pure exchange rate shocks;

(b) the modest EC recovery contained in the baseline projection is vulnerable to any strong and sustained US adjustment if no compensatory measures are taken in the EC and its main trading partners (US excepted) at the same time.

6.4. EC adjustment alone

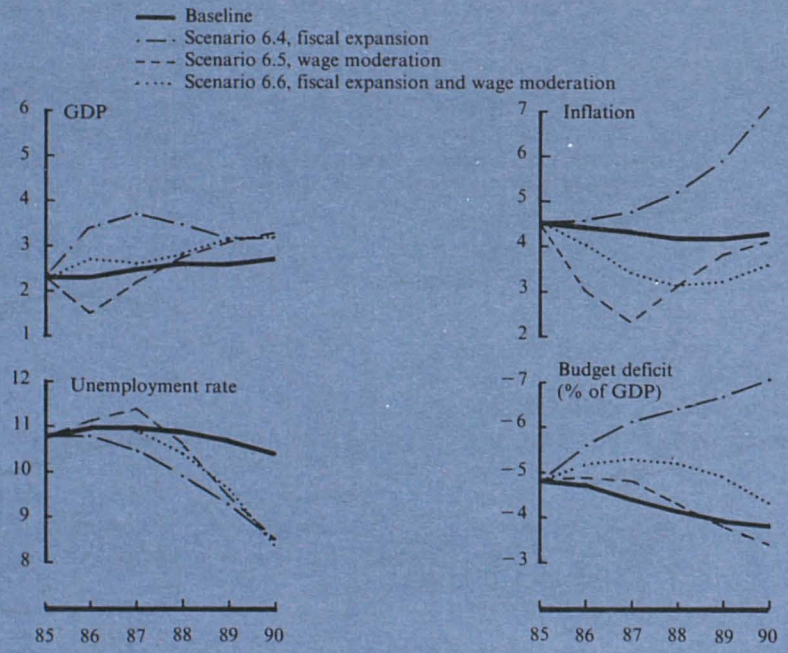
In accordance with the growth strategy outlined in the annual economic report, the focus of this section is on the reduction in unemployment that can be achieved through either fiscal policy actions, wage moderation or a combination of these two actions. It should, however, be kept in mind that many other elements should play in a growth and employment strategy, such as increased flexibility on the labour market, improvement in the working of the Community internal markets, new technology, etc., the impact of which is *not* taken into account in these stylized scenarios. These limitations should therefore be borne in mind in assessing the following scenario.

In order to make results more comparable, the first three scenarios will take for illustrative purposes a target of an unemployment level of about 8,5 % in 1990, i.e. a reduction of 2,5 points with respect to 1986 (see Graph 6.2).

Scenario 6.4 is straightforwardly 'Keynesian' since the only instrument is an increase in public investment. As a rule, the impact of expansionary fiscal policy measures is positive in the first two to three years, but negative effects then build up with inflationary pressures and crowding-out phenomena. The unemployment target postulated requires a very significant increase in the rate of growth of labour demand during the whole period. This means that in order to reach the target, and assuming a non-accommodating monetary policy to prevent inflation from accelerating completely out of control, the budgetary stimulus has to be repeated and cumulated over five consecutive years. This none the less would lead to a 5 point increase in the price level at the end of the period with respect to baseline and a public sector net borrowing requirement climbing from −5,6 % to −7,2 % of GDP between 1986 and 1990. The current balance also becomes negative during the whole period. Thus, in reality, this stylized reflation policy runs into serious problems of inflation and budgetary constraints which imply that it would have to be reversed.[2]

[2] Fiscal packages may be devised which are more oriented towards increases in labour demand than pure expenditure impulses and public investment programmes in particular. In this field, cuts in payroll taxes notably are highly efficient from a supply-side point of view since they immediately reduce unit wage-cost *without* cuts in effective wage earnings of employees, hence without negative demand effects.

GRAPH 6.2: **Impact of EC adjustment policies on EC variables**



Scenario 6.5 proposes, on the other hand, a pure supply impulse in which the rates of increase in nominal wages in 1987 and 1988 are changed to 3,5 % and 3,8 %, that is 2 points below the baseline rates, the rate of growth of nominal wages going back to its baseline level afterwards. As in similar exercises made with quite different models,[3] the effects on labour demand are positive in the medium-run but are negative in the short-run due to the induced fall in final demand. The ultimate reduction of unemployment to 8,5 % in 1990 is therefore only achieved after a temporary increase in 1986-87 together with a growth recession during these two years (see Graph 6.2).

Scenario 6.6 tests the possibility of finding a more satisfactory solution through a combined action on supply and demand.

In effect, the combination of wage moderation with temporary fiscal stimulus constitutes a much more effective package since the fiscal stimulus at the beginning of the period helps to sustain final demand, and wage moderation helps to keep price inflation and interest rates under control, improving considerably profitability and eliminating all crowding-out effects.

The scenario includes the following elements:

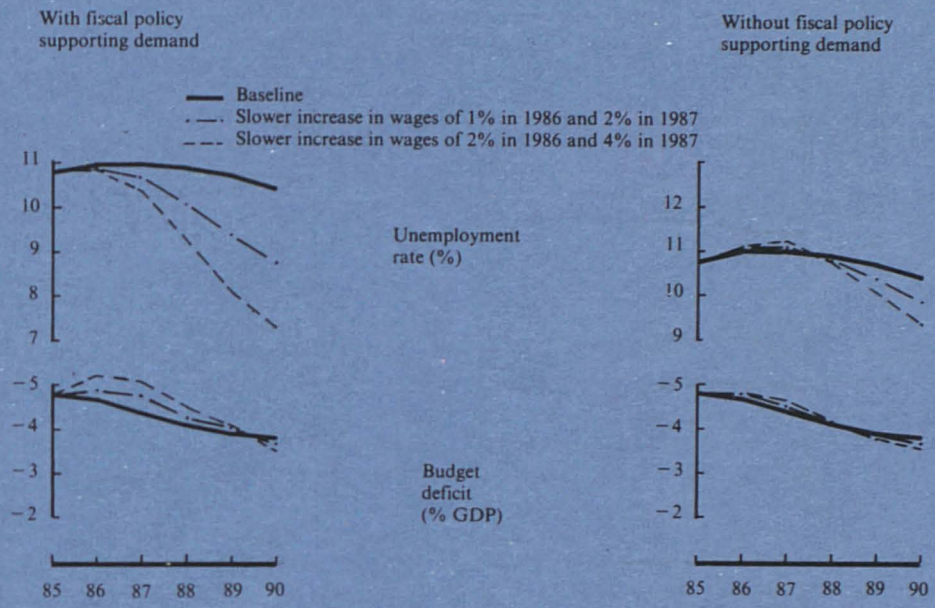
(a) real wage increases are kept at a rate of 0,5 % per year during two years, wage growth returning progressively to productivity growth (1,9 % in 1990) once the lowering of unemployment begins to be apparent;

(b) negative demand effects are alleviated through a sustained 0,5 % increase in public investment in 1986, followed by two successive cuts in payroll taxes in 1987 and 1988 equivalent to 0,5 % of GDP each year paid from the government budget in order to reinforce the impact of wage moderation without affecting earnings. This distribution of fiscal impulses over three years also helps to keep the unavoidable increases in budget deficits within more moderate limits.

The result shown in scenario 6.6 is a steady increase in GDP and labour demand, together with a fall in the inflation rate.

[3] see Annual Economic Review 1984-85, Chapter 9, *European Economy* No 22; November 1984.

GRAPH 6.3: **Wage moderation with and without nominal GDP target**



The current balance surplus is lowered but remains positive. Finally, the budget deficits remain more or less constant at − 5,2 % during the first three years and decrease afterwards. In 1990, an unemployment rate of 8,5 % is achieved and this should continue to diminish further in as much as the rate of growth of GDP (3,5 %) is sustainable.

It is of course difficult to know what degree of wage moderation might prove acceptable to the social partners, or under what conditions such policies might prove feasible. A final set of simulations tries therefore to illustrate some of the central issues that are posed here. Two variables are tested together: first, the extent of wage moderation (a slower increase in wages of the order of 1 % or 2 % compared to the baseline for each of two years cumulatively), and secondly, the presence or absence of fiscal policy adjustments (in the case of fiscal adjustments these are calculated to compensate the effects of wage moderation on nominal demand).

The wage moderation policy, accompanied by the fiscal policy adjustment, produces much sharper reductions in unemployment, as Graph 6.3 shows. The 2 % wage moderation case leads to a 7,2 % unemployment rate by 1990, compared to 8,9 % unemployment with the 1 % wage moderation example. Budget deficits are somewhat higher for the first few years, but by 1990 they fall felow the baseline level. In the case of inactive fiscal policy, the same wage moderation policies lead to reductions in unemployment which are about three times weaker.

6.5. Composite world scenario

Scenario 6.3 showed clearly the negative implications of adjustment policies taken by the US when other zones react passively to the US action. More cooperative scenarios may, however, be envisaged: given international interdependence,

coordinated expansion in the non-US world would make the US adjustment easier through increased demand for US exports, while the rest of the world would itself reduce its growth recession.

A composite scenario 6.8 was therefore constructed in which the US fiscal adjustment is halved with respect to scenario 6.3 (three times −0,5 % of GDP). Japan, on the other hand, applies a fiscal expansion equal to the former US contraction (three times 1 % of GDP). The rest of the world is also able to expand its overall import demand by 1 % per year through a combination of circumstances: improved balance of payments situations and domestic policies, lower interest payment on external debts and the beneficial impact of higher growth in the EC, US and Japan from 1986/87 on.

In the EC, the policy package includes a wage moderation keeping the rate of growth of real wage-cost per capita to 0,5 % per year during three years (1986-88) with progressive return to a rate of growth equal to real labour productivity growth afterwards. The wage moderation goes together with fiscal expansion calculated so as to prevent the wage policy from depressing nominal GDP. The income and fiscal actions are completed by some relaxation of monetary policy targets leading to a fall of 2 percentage points in the short-term interest rate.

Besides these fiscal packages, exchange rate changes are also modulated with a 9 % revaluation of the ECU against the dollar in 1986, 1987 and 1988, a revaluation by 15 % of the yen and revaluation by 5 % on average of all other currencies during the same period, corresponding to about 7,5 % devaluations of the effective rate of the dollar during each of these three years, cumulatively.

The results are more favourable for the EC than any of the preceding scenarios, GDP growth reaching 3,5 % on average between 1986 and 1990. Combined with wage moderation, this achieves a larger reduction of unemployment than in scenarios 6.4 to 6.6. The budget deficit is larger in 1986-88 by 0,8 percentage points of GDP with respect to the baseline but falls back thereafter. The current balance becomes negative but remains on average below −1 % of GDP.

These good results come mostly from internal factors, helped by increased demand from the non-US world. A strong growth of private investment is induced by increased profitability, supported by the fact that the sustained nominal GDP growth eliminates the usual negative demand side effects of wage cuts in the short run. In the medium term, the corresponding expansion of productive capacity enables also the EC economy to avoid bottlenecks, or demand-induced inflationary pressures. Also the large fall in the number of unemployed leads to an increase in the total wage bill, despite the initial cuts in wages per capita. In short, the impressive increase in labour demand comes from the cumulation of two positive factors: a 'Keynesian' effect linked to demand expansion and a classical effect linked to the fall in wage-cost and the expansion of productive capacity.

For the US and Japan, the results are also better. Growth in both countries is stronger than in the baseline projection, and in addition, the balance of payments disequilibria are much reduced. The Japanese current account surplus is brought down to +0,8 % of GDP and the US deficit reduced to −1,3 % of GDP.[4]

6.6. Conclusions

Although model results should always be taken with caution, the various scenarios put forward in the former sections seem to show that it should be possible to specify both international and domestic policy packages that give good or at least adequate results for all parties concerned, together with adjustment of the major disequilibria on the labour market or international trade and capital flows. These results, however, need strong and coordinated actions by all participants both on the domestic (governments, employers, employees) and the international (EC, US, Japan, rest of world) markets.

[4] The world scenario has been composed by retaining the hypotheses relative to the EC and assuming an unchanged international environment compared to the baseline in terms of policy.
The results for the EC are as follows:

	1985	1986	1987	1988	1989	1990
GDP	2,3	3,2	3,8	3,6	2,9	2,7
Domestic demand	1,7	3,0	3,8	4,0	3,1	3,0
Inflation	4,5	4,3	4,0	4,1	4,1	4,2
Total employment	0,0	0,3	0,9	1,2	1,5	1,2
Unemployment rate	10,8	10,8	10,3	9,6	8,5	7,4
Current balance	0,4	0,4	0,0	−0,2	−0,4	−0,4
Budget balance	−4,8	−5,0	−5,2	−5,3	−4,9	−4,4
Exchange rate (ECU USA)	3,5	−1,6	−1,5	−1,5	−1,5	−1,5
Interest rate (long)	10,8	10,5	9,9	9,2	8,9	8,7

Brief description of the Compact model of the European Community in the world economy.

The Compact model is a relatively small macro-econometric model. It has been developed within the Directorate General for Economic and Financial Affairs for the purpose of analysing the effect of economic policy measures, taking account of interactions between the main economic variables while keeping the overall structure relatively small.

Leaving aside the trade and capital flow linkage part (the block which links the EC model to models for the US and Japan and for the rest of world) the Compact model includes 50 endogenous variables which are determined within the model by 28 behavioural equations and 22 identities. The EC module is a completely new system based on EC-10 aggregated stock and flow yearly data in ECU as published and constructed by Eurostat and DG II services. It includes all the basic blocks of an operational macroeconomic model, i.e. final demand, production and factor supply and demands, wages and prices, public sector receipts and expenditures, monetary and financial relations, balance of payments and international trade linkages.

The models for the US and Japan have been derived from a simplification of these components of the world model built by the Economic Planning Agency of the Japanese Government. The rest of the world module at present includes only international trade and capital movements variables plus an estimate of GDP, but will be extended to endogenize commodity price movements (drawing here on IMF and OECD work).

The main features of the Compact model, and notably as regards its EC module, are:

(a) the attention paid to both stock and flow equilibrium in the flow of funds matrix of transactions between economic agents, namely, households, enterprises, government and the foreign sector;

(b) the inclusion of wealth effects in consumers' demand;

(c) the disaggregation of total unemployment into classical, Keynesian and frictional shares using a labour market disequilibrium approach;

(d) the integration of the distinction between Keynesian and classical unemployment into the wage determination process and, via wages, into the inflation process;

(e) the integration of the balance of payments item with the determination of public sector borrowing requirement and the money supply;

(f) the exchange rate is determined by the outcome for the current and capital accounts and floats with exchange reserves held constant in relation to imports (alternative exchange rate policies can be envisaged).

On the whole, the Compact model proves to be capable of simulating economic developments in the EC quite well over the period 1973 to 1982. The principal source of more serious deviations in the model simulations appears to originate in the difficulty in simulating exchange rate developments correctly. The directions of change in the ECU/USD rate are normally correctly indicated but their amplitude is under-represented at present, and this point is receiving further attention. A simulation covering the period 1983-85 also gives a broadly satisfactory reproduction of the Commission's estimates and forecasts for this period.

Technical annex

Basic concepts and forecasting techniques

Aggregation in Community data

In general, national accounts variables in national currencies for the Member States are aggregated using purchasing power standards (PPS) for domestic variables and market exchange rates (ECU) for foreign trade variables. Volume series (constant price series) are aggregated on the basis of 1975 prices and 1975 PPS/exchange rates. Value series (current price series) are aggregated on the basis of current prices and current PPS/exchange rates. National accounts implicit price deflators are obtained by dividing current price series by the corresponding constant price series.

Money supply indices for the Community are derived from harmonically-weighted indices for the Member States, the weights being the share of each country in total Community GDP at current prices and current PPS in the year in question. Long-term and short-term interest rates for the Community are similarly derived as a harmonically-weighted average of rates in the Member States, the weights being the same as for the money supply calculations.

Forecasting procedures

Short-term forecasts are prepared by the Directorate-General for Economic and Financial Affairs twice a year, in May-June and September-October. The time horizon of these forecasts is to the end of the following year. The forecasts contained in this review are those given by the September-October 1985 exercise. The forecasts are built up separately for each of the 10 member countries of the Community, but within a framework of common assumptions about the external environment, exchange rates and interest rates, and subject to controls and checks on the consistency of foreign trade forecasts. The forecasts are made on the basis of the assumption of unchanged government policies.

The forecasts for each Community country cover the main components of gross domestic product in volume, price and value terms; the income and expenditure accounts of households and of general government; the current account of the balance of payments; saving, investment and the financial balance of the main institutional sectors; employment and unemployment; and domestic money supply and its counterparts. Figures are mainly compiled on an annual basis, but half-yearly estimates are made for gross domestic product and its components in volume terms and for certain other key indicators such as industrial production, unemployment, and the current account balance. Quarterly profiles for gross domestic product are also made for the whole forecast period.

Although in principle the definitions used are those of the ESA, in practice national definitions and sources are used in some cases because the statistics become available more quickly, and in order to facilitate discussion of the forecasts with national authorities.

The forecasting round starts with the setting of assumptions about exchange rates, interest rates, and demand and prices in the rest of the world. These initial assumptions may be amended as the round progresses in the light of new information and of the emerging forecast for the Community countries.

(i) Exchange rate forecasts are normally based on the rates implied by the forward exchange markets, modified to take account of the EMS and other considerations. In the present forecast the forecast rates took into account forward rates prevailing at the beginning of September 1985.

(ii) Short-term interest rate assumptions are set for the USA and for each of the Community countries taking account of exchange rate developments, domestic monetary policies, etc.

(iii) Forecasts are made for the growth of real GDP and its components for the USA, Canada and Japan, and in a more summary form for each of the other non-EC member countries of the OECD. In the light of output growth and other considerations, forecasts of the change in the volume of total imports of goods are made for each of these countries, and for three other world zones—OPEC, non-oil developing countries, and other countries (consisting principally of the centrally planned economies, South Africa, and Yugoslavia). An assumption is made, having regard to oil market conditions and recent OPEC decisions, about the export price of oil, and forecasts are also made for the world export prices of the main groups of non-oil primary commodities (based on UN indices) and for the export prices of manufactured goods of the major non-EC developed countries.

The forecasts of the change in import volumes for the non-EC countries and zones, together with initial import forecasts for each of the Community countries, are weighted together according to the structure of exports to provide estimates of 'export market growth' for each country. Similarly, the forecasts of rest-of-the-world export prices for primary commodities and manufactures, together with initial forecasts of total export prices of goods for each of the

Community countries and with the necessary exchange rate adjustments, are weighted together according to the structure of imports to provide estimates of 'import costs' for each country. On the basis of this and other information the country desks make their first forecasts of export volumes and import prices and, if necessary, revise their forecasts of import volumes and export prices, with in all cases a split between trade within the Community (intra-EC) and trade with non-EC countries (extra-EC). Particular attention is paid to ensuring that the changes in total intra-EC imports and exports should be close in both volume and price terms. Checks are also made at world level to make sure that world exports and imports are in line with each other. In order to reach this desired convergence and in response to the country desks' forecasts which are being developed at the same time, this procedure for achieving trade consistency is reiterated several times.

Balance of payments and exchange rates

Sources of balance of payments and related data

Data on current balances (Table 1.4) are taken from the IMF publication *World Economic Outlook* and from the forecasts of the services of the Commission. Current balances have been defined as inclusive of official transfers.

Effective exchange rates

Changes in the effective exchange rate of a currency *i* measure the average change in the exchange rates between currency *i* and a representative sample or 'basket' of other currencies between two points in time in order to express in a single figure the average direction and magnitude of change over the period in question. The model used in the Commission to calculate these average exchange rate changes involves 20 countries—the members of the Community (with Belgium and Luxembourg treated as a single entity), the two candidates for membership (Spain and Portugal), and the nine other countries with the greatest importance in world trade. An effective exchange rate change for currency *i* is obtained by multiplying the percentage change against each of the other 19 currencies in the model by that currency's weight and summing the results.

The weights attributed to each currency reflect the importance of the currency concerned, both as a bilateral trading partner for country *i* and as a competitor against exports from country *i* in third markets. For this reason the term 'trade-weighted exchange-rate changes' is sometimes used in place of the term 'effective exchange rate changes'. The weights used are based on trade data for the year in question up to and including 1980. For subsequent years, the weights are based on 1980 trade data.

For certain purposes it may be useful to use a more restricted sample of currencies. For example, following a realignment within the EMS it is possible to calculate the effective exchange rate of each EMS currency against all other EMS currencies taken together using the same technique as described above, but using a 'basket' composed of EMS currencies only.

The ECU and measures used in the European Monetary System[1]

The ECU

The ECU is at the centre of the European Monetary System. Central rates are declared in terms of the ECU and bilateral central rates are derived from them. A proportion of member countries' reserves is held in ECU in the form of claims on the European Monetary Cooperation Fund and settlement of certain debts arising thereunder may be made in ECU. The ECU is also central to the functioning of the Community institutions, being the unit in which all receipts and expenditures are expressed, as well as having a growing role in the private markets. It is defined as a basket of the currencies of EC member countries, the quantity of each being based on fundamental economic criteria. Its composition had been determined before the inception of the EMS and was revised on 15 September 1984:

	13 March 1979	*15 September 1984*
BFR	3,660	3,710
DKR	0,217	0,219
DM	0,828	0,719
DR	—	1,150
FF	1,150	1,310
IRL	0,00759	0,00871
LIT	109	140
LFR	0,140	0,140
HFL	0,286	0,256
UKL	0,0885	0,0878

[1] For a detailed explanation of the EMS, see *European Economy* No 3, July 1979.

Bilateral divergence between currencies of the European Monetary System (EMS)

The width of the EMS band depends on the positions of the two currencies that diverge most in relation to their bilateral central rate. The maximum divergence allowed between two currencies is 2,25%, although the lira may diverge by up to 6%; sterling is not in the exchange mechanism.

The average point in the band is determined by half the bilateral divergence of the two currencies with the widest divergence (not counting the lira).

Divergence indicator

The divergence indicator (DI) measures the degree of movement of a specific currency against its maximum divergence spread (MDS), which differs for each currency as a function of its weight in the ECU basket. The formula for the divergence indicator is:

$\pm 2{,}25 \times (1 - p_i)$, where p_i is the weight of the currency in the ECU basket.

For a given currency, the divergence indicator is obtained:

(i) first by calculating the premium (P) or discount (D) shown by the market rate of the ECU in terms of that currency against its ECU central rate;

(ii) and then by comparing the result obtained with the maximum divergence spread.

In order to permit a comparison of movements in the divergence indicators for each of the EMS currencies, the maximum divergence spread for each currency is assigned an index of 100. The indicator will therefore be expressed as a figure from 0 to 100. A currency reaches its divergence threshold when the indicator stands at 75.

Expressed as a formula, calculation of the indicator is as follows:

$$\text{P or D} = \frac{\text{ECU market-ECU central}}{\text{ECU central}} \times 100$$

$$\text{DI} = \frac{\text{P or D}}{\text{MDS}} \times 100$$

The result is adjusted to ensure that the indicator for currencies observing narrow margins of 2,25% against one another is not distorted by exchange rate movements in the lira and the pound sterling outside those margins (which are not, of course, operationally compulsory for Italy and the UK).

Monetary concepts and definitions

Money supply

Each country uses several definitions of money supply, which do not coincide with those of other countries since financial structures and behaviour mean not only that some assets are regarded as money in one country but not in another, but also that definitions in the same country may change as structures and behaviour evolve.

The basic elements for defining the money supply are:

(a) the characteristics of monetary assets;

(b) the holders of monetary assets;

(c) the issuers of monetary assets.

There are two main definitions of money supply: money supply narrowly defined (M1), comprising circulating coins and notes and current bank accounts; money supply broadly defined (M2 or M3), comprising M1 and various assets with banks and other financial institutions in the form of deposit accounts, savings accounts or short-term notes. The principal components of money supply broadly defined (M2 or M3) for each country are described below.

Belgium: Money supply broadly defined (M2).

(a) *Monetary assets:* Coins and notes, current bank accounts and all other assets with a maximum maturity of one year in national or foreign currency.

(b) *Holders:* Resident households and private firms.

(c) *Issuers:* Central bank, commercial banks and other financial intermediaries; the figures from 1982 onwards include monetary claims on the external sector.

Denmark: Money supply broadly defined (M2: new definition from 1975).

(a) *Monetary assets:* Coins and notes, current bank accounts, deposit accounts, foreign currency deposits, Treasury bills.

(b) *Holders:* Resident households and firms, non-monetary financial institutions, local authorities.

(c) *Issuers:* Central bank, commercial banks, main savings banks, postal service.

FR of Germany: Money supply broadly defined (M3).

(a) *Monetary assets:* Coins and notes, current bank accounts except those of the authorities with the central bank, deposit accounts, banking liabilities up to four

years, savings accounts with a legal period of notice, foreign currency deposits.

(b) *Holders:* Resident households and firms, local authorities.

(c) *Issuers:* Central bank, commercial banks, savings, co-operative and mortgage banks.

Greece: Money supply broadly defined (M3).

(a) *Monetary assets:* Coins and notes, sight savings and time deposits.

(b) *Holders:* Resident households and firms, including public authorities, sight accounts.

(c) *Issuers:* Central bank, commercial banks and special credit institutions.

France: Residents' holdings of money broadly defined (M2R).

(a) *Monetary assets:* Coins and notes, sight deposits, current bank books, five year home-purchase saving plans, time deposits (all maturities), bank tap notes up to five years, foreign currency accounts.

(b) *Holders:* Resident households and firms, certain central government agencies, local authorities, social security funds.

(c) *Issuers:* Central bank, commercial banks and, for sight deposits, postal cheque office, *banques populaires*, co-operative banks, savings banks and Treasury.

Ireland: Money supply broadly defined (M3).

(a) *Monetary assets:* Coins and notes, current and deposit accounts.

(b) *Holders:* Resident households and firms, including government and local authority deposits with licensed banks.

(c) *Issuers:* Central bank and licensed banks.

Italy: Money supply broadly defined (M3).

(a) *Monetary assets:* Coins and notes, current and deposit accounts, current accounts in foreign currency, savings accounts, postal savings certificates, Treasury bills up to 12 months, foreign currency deposits.

(b) *Holders:* Resident households and firms, local authorities, social security funds.

(c) *Issuers:* Central bank, commercial banks, savings banks, Treasury postal service.

The Netherlands: Money supply broadly defined (M2).

(a) *Monetary assets:* Coins and notes, current bank and post office accounts, bank and post office time deposits up to two years, foreign currency deposits, savings accounts with high velocity of circulation, Treasury liabilities in the form of bonds, certificates and loans or deposits, and liabilities up to two years of the *Bank voor Nederlandse Gemeenten* and the *Nederlandse Waterschapbank*.

(b) *Holders:* Resident households and firms, local authorities.

(c) *Issuers:* Central bank, Treasury, local authorities, commercial banks, giro services and savings banks.

United Kingdom: Money supply in national currency broadly defined (sterling M3).

(a) *Monetary assets:* Coins and notes, all types of sterling bank deposits including certificates of deposit.

(b) *Holders:* Resident households and private firms.

(c) *Issuers:* Central bank, commercial banks, discount houses.

Monetary targets

At present, monetary targets are set in Germany, France, Italy, the United Kingdom, Ireland and Greece.

The aggregates used are as follows:

FR of Germany: Central bank money (MZ), comprising notes in circulation and compulsory reserves of banks calculated as a constant fraction of residents' claims on banks: 16,6% on current accounts, 12,4% on deposit accounts, 8,1% on savings accounts.

Greece: Private sector bank credit (PSCE), notes in circulation (MO) and M3.

France: Residents' holdings of money broadly defined (M2R).

Ireland: Private sector credit (PSCE): lending by licensed banks in Irish pounds and foreign currency to households, private firms and State-sponsored bodies.

Italy: Total domestic credit (TDCE), including bank loans and loans from special credit institutions, bonds issued by firms and local authorities, and the public sector

borrowing requirement (Treasury, Cassa Depositi e Prestiti, Cassa del Mezzogiorno and public utilities, except Treasury financing of financial intermediaries).

United Kingdom: Broadly defined money supply, in national currency (£ M3) and, from March 1984, MO, i.e. notes and coin plus the small working balances maintained by the commercial banks with the Bank of England.

Counterparts of the money supply

The money supply and its counterparts are analysed on the basis of a consolidation of the transactions of money-creating financial institutions which are analysed into:

(a) *public sector credit;*

(b) *private sector credit;*

(c) *miscellaneous items,* covering residual items which vary from country to country;

(d) *external contribution,* the balance of financial institutions' external liabilities and claims;

(e) *non-monetary liabilities,* covering medium-term and long-term liabilities and, for some countries, proprietors' funds.

Domestic money creation is the sum of aggregates (a), (b), (c) minus the amount of aggregate (e).

In countries where the Treasury and other public institutions have monetary liabilities (coinage, short-term Treasury bonds, etc.), these are included as liabilities in the consolidate account of financial institutions, an equivalent amount being included under the heading for public sector credit.

National monetary analyses also differ according to the definitions of the three sectors: public sector, private sector, foreign sector. For example, loans to public corporations may be included either in public sector or in private sector credit. For some countries, the external counterpart is distorted by valuation changes.

In the following descriptions, the financial institutions are those described as issuers of the money supply in the Section 'Money supply'.

Belgium:

(a) *Public sector credit:* Net claims (loans and purchases of securities) of financial institutions on general government (except social security funds) and net foreign borrowing by general government.

(b) *Private sector credit:* Claims of financial institutions on households and firms.

(c) *Miscellaneous:* Capital and own resources, items in transit, statistical residuals, social security debt.

(d) *External contribution:* Net external position of financial institutions plus net foreign borrowing by general government.

(e) *Non-monetary commitments:* Claims, with maturities of more than one year by firms and households on the financial institutions.

Denmark:

(a) *Public sector credit:* Net claims (loans and purchases of securities) of financial institutions on central government (including public borrowing abroad sterilized in the central bank).

(b) *Private sector credit:* Claims of financial institutions on households and firms, local authorities, public sector undertakings and non-money-creating financial institutions.

(c) *Miscellaneous:* Capital and own resources, items in transit, statistical residuals.

(d) *External contribution:* Surplus on current external payments, net borrowing abroad by business, local government authorities, etc. and net sales of krone-denominated bonds to non-residents.

(e) *Non-monetary liabilities:* Some categories of time deposits of over one year.

FR of Germany:

(a) *Public sector credit:* Claims (loans and purchases of securities at issue) of financial institutions on general government.

(b) *Private sector credit:* Claims (loans and purchases of securities) of financial institutions on household and firms, the railways, federal postal services, State corporations and home-savings institutions.

(c) *Miscellaneous:* Items in transit, statistical residuals, authorities' deposits with the central bank.

(d) *External contribution:* Net external position of financial institutions, including balance on financial institutions' dealings in foreign securities.

(e) *Non-monetary liabilities:* Liabilities of financial institutions other than M3 held by households, firms and authorities.

Greece:

(a) *Public sector credit:* Claims (loans and purchases of securities) of financial institutions on central government, local authorities, social security and public corporations.

(b) *Private sector credit:* Claims (loans and purchases of securities) of financial institutions on households and private firms.

(c) *Miscellaneous:* None.

(d) *External contribution:* Net external position of financial institutions.

(e) *Non-monetary liabilities:* Private blocked deposits, deposits, other than sight deposits, of authorities, securities issued by financial institutions, items in transit, capital and reserves.

France:

(a) *Public sector credit:* Claims (loans and purchases of Treasury bonds) of financial institutions on the Treasury; State financing through postal cheque deposits and deposits with Treasury branches.

(b) *Private sector credit:* Loans to households, private firms and public corporations, excluding loans to non-resident households and firms.

(c) *Miscellaneous:* Items in transit.

(d) *External contribution:* Net external position of money creating banks.

(e) *Non-monetary liabilities:* The balance between certain liabilities of financial institutions (capital, reserves, securities issued) and certain assets (buildings and securities portfolio); net liabilities towards other financial intermediaries.

Ireland:

(a) *Public sector credit:* Loans by financial institutions to central government, local authorities and State-sponsored bodies (net of central government deposits with the central bank), plus government bond issues to finance the purchase of agricultural products on behalf of the EEC.

(b) *Private sector credit:* Loans by financial institutions to households and private firms.

(c) *Miscellaneous:* None.

(d) *External contribution:* Net external position of licensed banks, official external reserves.

(e) *Non-monetary liabilities:* Items in transit, capital and reserves.

Italy: Balance sheet of financial institutions consolidated with supply and demand in the securities market.

(a) *Public sector credit:* Borrowing requirement of Treasury and other government agencies, excluding public financing of the private sector and foreign borrowing.

(b) *Private sector credit:* Claims of financial institutions and special credit institutions on households, firms, local authorities and social security funds; net issue of private bonds not held by financial institutions.

(c) *Miscellaneous:* Capital and own resources, items in transit.

(d) *External contribution:* Net external position of financial institutions.

(e) *Non-monetary liabilities:* Assets of households and firms consisting of: deposits with special credit institutions (ICS), bank acceptances, bonds issued by firms and ICS, public securities and shares.

The Netherlands:

(a) *Public sector credit:* Loans by financial institutions to central government and local authorities.

(b) *Private sector credit:* Loans to households, firms in the private and public sectors and institutional investors, as well as investments on the capital market.

(c) *Miscellaneous:* Items in transit and statistical adjustment.

(d) *External contribution:* Net external position of financial institutions and Treasury.

(e) *Non-monetary liabilities:* Liabilities of financial institutions other than M2 held by households, firms, institutional investors and the authorities, and the capital and own resources of financial institutions.

United Kingdom:

(a) *Public sector credit:* Net claims of commercial banks, the Banking and Issue Departments of the Bank of England and the Exchange Equalization Account on general government and public corporations.

(b) *Private sector credit:* Loans by banks to the private sector and commercial bills held by the Issue Department of the Bank of England.

(c) *Miscellaneous:* Net claims by banks on residents in foreign currency.

(d) *External contribution:* Net short-term external position of commercial banks; official reserves net of liabilities to IMF.

(e) *Non-monetary liabilities:* Liabilities of financial institutions other than sterling M3 including capital and reserves; includes some external items.

Labour market definitions

Labour force, employment, unemployment and hours worked definitions

The civilian labour force in the Community and Member States comprises all persons employed (including self-employed and family workers but excluding the armed forces) plus the unemployed. The national concept is used: all employed or unemployed persons resident in the territory of the country in question are included.

Total employment in the Community and Member States includes all persons in employment or self-employment, as well as family workers. The domestic concept is used: all persons employed or self-employed within the territory of the country in question whether or not they are resident, are included.

The *unemployment* rate in the Community and Member States is defined as the number unemployed as a percentage of the civilian labour force; data for numbers unemployed and the labour force relate to the same year, i.e. the 1981 unemployment rate is the average number unemployed in 1981 as a percentage of the 1981 labour force. Rates for 1970-84 are historical data supplied by Eurostat; 1985-86 rates are estimates using Eurostat definitions based on forecasts, prepared by the Commission departments, for numbers unemployed and the labour force. Data for *unemployed persons* are derived from statistics of registered unemployed supplied to Eurostat by national agencies in accordance with standardized procedures: in principle, the definition of unemployed persons covers persons without a job, seeking employment as an employee and immediately available for work. For more specific detail on the individual series for Member States, see *Employment and Unemployment* (Eurostat, 1984).

Statistical annex

Notes on the statistical annex

General remarks

This year's November edition of *European Economy* again gives in its statistical annex updated time series of annual data.

Unless otherwise specified, aggregates up to 1983 are defined for member countries as in the ESA (European System of Economic Accounts), and for the USA and Japan as in the SNA (UN-OECD System of National Accounts). National accounts figures for 1984, 1985 and 1986 are estimates and forecasts made by Commission staff using the definitions and latest figures available from national sources, and so they are not fully comparable with the corresponding figures for earlier years. However, in Tables 1, 2, 4 to 8, 10 to 15, 17 to 27, 30 and 31 discontinuities have been eliminated.

Community totals are for EUR 10 unless otherwise stated. Community totals for national accounts data are aggregated using purchasing power parities, except in Tables 6, 28, 29, 32 to 36 and 45 to 47, where current exchange rates have been used.

List of tables

The public sector

Table 1

Population; total

('000 persons)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	9 119	4 581	55 433	8 327	45 684	2 832	50 198	314	11 483	52 372	240 343	179 979	93 260
1961	9 166	4 617	56 175	8 398	46 163	2 818	50 523	317	11 637	52 807	242 621	182 992	94 090
1962	9 218	4 647	56 837	8 448	46 998	2 830	50 843	321	11 801	53 292	245 235	185 771	94 980
1963	9 283	4 684	57 389	8 480	47 816	2 850	51 198	324	11 964	53 625	247 613	188 483	95 900
1964	9 367	4 720	57 971	8 510	48 310	2 864	51 600	328	12 125	53 991	249 786	191 141	96 890
1965	9 448	4 758	58 619	8 550	48 758	2 876	51 988	331	12 293	54 350	251 972	193 526	97 950
1966	9 508	4 797	59 148	8 612	49 164	2 884	52 332	334	12 455	54 643	253 877	195 576	98 860
1967	9 556	4 839	59 286	8 716	49 548	2 900	52 667	335	12 597	54 959	255 403	197 457	99 920
1968	9 590	4 867	59 500	8 741	49 914	2 913	52 987	336	12 726	55 214	256 788	199 399	101 070
1969	9 613	4 891	60 067	8 773	50 318	2 929	53 317	338	12 873	55 461	258 579	201 385	102 320
1970	9 638	4 929	60 651	8 793	50 772	2 950	53 661	339	13 032	55 632	260 397	203 984	103 403
1971	9 672	4 963	61 284	8 831	51 251	2 978	54 005	342	13 194	55 907	262 428	206 827	105 687
1972	9 709	4 992	61 672	8 889	51 701	3 024	54 400	347	13 330	56 079	264 143	209 284	107 178
1973	9 738	5 022	61 976	8 929	52 118	3 073	54 779	350	13 438	56 210	265 634	211 357	108 702
1974	9 768	5 045	62 054	8 962	52 460	3 124	55 130	355	13 543	56 224	266 665	213 342	110 158
1975	9 795	5 060	61 829	9 047	52 705	3 177	55 441	359	13 660	56 215	267 288	215 465	111 520
1976	9 811	5 073	61 531	9 167	52 891	3 228	55 701	361	13 773	56 206	267 742	217 563	112 768
1977	9 822	5 088	61 400	9 308	53 077	3 272	55 930	361	13 856	56 179	268 293	219 760	113 860
1978	9 830	5 104	61 327	9 430	53 277	3 314	56 127	362	13 939	56 167	268 877	222 095	114 920
1979	9 837	5 117	61 359	9 548	53 480	3 368	56 292	363	14 034	56 227	269 625	224 567	115 880
1980	9 847	5 123	61 566	9 642	53 714	3 401	56 416	364	14 148	56 314	270 535	227 202	116 800
1981	9 852	5 122	61 682	9 729	53 966	3 443	56 502	366	14 247	56 379	271 288	229 348	117 660
1982	9 856	5 118	61 638	9 790	54 218	3 483	56 639	366	14 312	56 335	271 755	231 786	118 440
1983	9 855	5 114	61 426	9 850	54 441	3 508	56 837	366	14 365	56 377	272 139	233 981	119 259
1984	9 853	5 111	61 178	9 913	54 713	3 535	56 954	366	14 422	56 397	272 443	236 204	120 094
1985	9 852	5 111	60 933	9 992	54 968	3 560	57 012	366	14 478	56 437	272 710	238 448	120 934
1986	9 852	5 111	60 763	10 072	55 260	3 581	57 066	366	14 533	56 506	273 111	240 713	121 781

Table 2

Employment; total economy

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	0,8	1,5	1,4	1,1	0,1	−0,2	0,2	1,1	1,5	1,2	0,8	−0,4	1,4
1962	1,6	1,5	0,4	−0,8	0,2	0,7	−1,1	0,3	2,0	0,7	0,2	2,0	1,3
1963	0,7	1,2	0,2	−0,9	1,0	0,6	−1,5	−0,4	1,4	0,1	0,1	0,8	0,9
1964	1,3	2,1	0,1	−0,9	1,1	0,5	−0,6	1,7	1,8	1,1	0,5	1,8	1,3
1965	0,2	1,8	0,6	−0,8	0,4	−0,2	−1,7	0,9	0,9	0,9	0,2	3,3	1,6
1966	0,5	0,5	−0,3	−0,8	0,8	−0,3	−1,5	0,5	0,8	0,6	−0,0	4,5	2,1
1967	−0,3	−0,6	−3,3	−0,9	0,3	−0,6	1,1	−1,1	−0,3	−1,5	−1,0	2,5	1,9
1968	−0,1	1,1	0,1	−0,9	−0,1	0,3	−0,0	−0,4	0,9	−0,7	−0,1	2,4	1,7
1969	1,7	0,9	1,6	−0,8	1,7	0,3	0,5	1,4	1,7	0,1	1,0	2,5	0,8
1970	−0,5	0,7	1,3	−0,8	1,0	−1,2	−0,0	1,8	1,2	−0,5	0,4	−0,8	1,1
1961-70	0,6	1,1	0,2	−0,7	0,6	−0,0	−0,5	0,6	1,2	0,2	0,2	1,9	1,4
1971	1,0	0,6	0,3	−0,9	0,4	0,2	−0,1	3,1	0,6	−1,0	−0,1	−0,4	0,5
1972	−0,1	2,1	0,1	0,4	0,5	−0,5	−1,1	2,6	−0,9	−0,2	−0,1	2,4	0,1
1973	1,3	1,2	0,7	0,5	1,3	0,7	0,8	1,9	0,0	2,3	1,2	4,0	1,9
1974	1,4	−0,3	−1,3	−0,1	0,7	1,1	1,5	2,5	0,0	0,3	0,2	1,5	−0,4
1975	−1,4	−1,2	−2,8	0,6	−1,0	0,4	0,2	1,6	−0,7	−0,4	−1,0	−2,5	−0,3
1976	−0,6	1,8	−0,8	1,3	0,7	−0,8	0,8	−0,6	−0,2	−0,9	−0,1	2,7	0,9
1977	−0,2	0,8	−0,2	−0,9	0,8	1,8	0,6	0,3	0,2	0,1	0,3	3,4	1,3
1978	0,0	1,0	0,6	1,6	0,4	2,5	0,6	0,0	0,7	0,6	0,6	5,1	1,2
1979	1,2	1,2	1,3	1,5	−0,1	3,2	1,0	1,0	1,3	1,5	1,0	3,3	1,3
1980	−0,0	−0,4	1,0	1,7	−0,0	1,0	0,9	1,1	0,7	−0,3	0,4	0,3	1,0
1971-80	0,3	0,7	−0,1	0,6	0,4	0,9	0,5	1,3	0,2	0,2	0,2	2,0	0,8
1981	−2,0	−1,3	−0,8	0,1	−0,7	−0,9	0,5	−0,6	−1,5	−3,9	−1,3	0,9	0,8
1982	−1,3	0,3	−1,8	−1,3	0,1	0,2	−0,1	0,0	−2,5	−1,4	−0,9	−1,8	1,0
1983	−1,1	0,5	−1,7	−1,0	−0,6	−2,0	0,1	−0,3	−2,0	−0,8	−0,9	0,7	1,7
1984	0,4	2,2	−0,0	−0,2	−1,0	−0,9	0,4	0,5	−0,5	1,5	0,3	4,1	0,6
1985	0,4	2,0	0,6	0,8	−1,0	−0,3	0,2	0,6	0,4	1,1	0,4	2,0	1,5
1986	0,3	1,6	1,3	0,1	−0,7	0,6	0,3	0,4	0,6	0,9	0,5	1,7	1,2

Table 3

Unemployment rate

(as percentage of civilian labour force)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 9	US	JA
1960	3,1	1,6	1,0	:	0,7	4,7	7,2	0,1	0,7	1,6	2,5	5,5	1,7
1961	2,5	1,2	0,7	:	0,6	4,3	6,6	0,1	0,5	1,4	2,2	6,7	1,5
1962	2,0	1,1	0,6	:	0,7	4,2	5,5	0,1	0,5	1,9	2,0	5,5	1,3
1963	1,5	1,5	0,7	:	0,7	4,5	5,1	0,2	0,6	2,3	2,1	5,7	1,3
1964	1,5	0,9	0,6	:	0,6	4,3	5,2	0,0	0,5	1,6	1,9	5,2	1,1
1965	1,8	0,7	0,6	:	0,7	4,5	5,7	0,0	0,6	1,4	1,9	4,5	1,2
1966	2,0	0,8	0,6	:	0,7	4,3	5,5	0,0	0,8	1,4	1,9	3,8	1,3
1967	2,6	1,0	1,8	:	1,0	4,5	5,0	0,1	1,7	2,2	2,4	3,8	1,3
1968	3,1	1,7	1,2	:	1,3	4,8	4,7	0,1	1,5	2,3	2,3	3,6	1,2
1969	2,3	1,4	0,7	:	1,1	4,6	4,4	0,0	1,1	2,3	2,0	3,5	1,1
1970	2,1	1,1	0,6	:	1,3	5,3	4,4	0,0	1,3	2,5	2,0	4,9	1,1
1961-70	2,1	1,1	0,8	:	0,9	4,5	5,2	0,1	0,9	1,9	2,1	4,7	1,2
1971	2,1	1,3	0,7	:	1,6	5,2	5,1	0,0	1,8	2,9	2,4	5,9	1,2
1972	2,7	1,3	0,9	:	1,8	6,0	5,2	0,0	3,0	3,2	2,7	5,6	1,4
1973	2,8	0,8	1,1	:	1,8	5,5	4,9	0,0	3,1	2,2	2,4	4,9	1,3
1974	3,1	2,1	2,3	:	2,3	5,9	4,9	0,0	3,7	2,2	2,9	5,6	1,4
1975	5,1	5,0	4,1	:	3,9	8,4	5,3	0,2	5,3	3,6	4,3	8,5	1,9
1976	6,5	5,2	4,0	:	4,2	9,3	5,6	0,3	5,6	4,9	4,8	7,7	2,0
1977	7,5	6,3	4,0	:	4,8	9,1	5,4	0,5	5,4	5,3	5,0	7,1	2,0
1978	8,1	7,1	3,8	:	5,2	8,3	6,1	0,7	5,4	5,1	5,2	6,0	2,2
1979	8,4	5,8	3,3	:	5,9	7,4	6,7	0,7	5,5	4,7	5,2	5,8	2,1
1980	9,1	6,7	3,4	:	6,4	8,2	7,2	0,7	6,2	6,0	5,8	7,1	2,0
1971-80	5,5	4,2	2,8	:	3,8	7,3	5,6	0,3	4,5	4,0	4,1	6,4	1,7
1981	11,1	8,9	4,8	:	7,7	10,2	8,0	1,0	8,8	9,2	7,7	7,6	2,2
1982	13,0	9,5	6,9	:	8,7	12,2	9,7	1,3	11,8	10,6	9,3	9,7	2,4
1983	14,3	10,2	8,4	7,9	8,8	14,9	10,9	1,6	14,3	11,6	10,4	9,6	2,7
1984	14,5	9,8	8,4	8,1	9,9	16,3	11,9	1,7	14,2	11,8	10,9	7,5	2,7
1985	13,8	9,1	8,4	8,3	10,7	17,1	12,6	1,7	13,2	12,0	11,2	7,3	2,5
1986	13,4	8,6	8,0	9,0	10,9	17,4	13,1	1,6	13,0	11,7	11,1	7,7	2,6

Table 4

Gross domestic product at current market prices

(national currency; '000 million)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	557,0	41,15	302,7	105,2	296,5	0,631	23 207	26,03	44,00	25,73	261,4	505,4	15 841
1961	592,4	45,66	331,7	118,6	323,5	0,680	25 810	27,27	46,46	27,46	284,7	523,4	19 579
1962	633,7	51,45	360,8	126,0	361,2	0,736	28 998	27,37	50,01	28,76	309,8	563,6	21 715
1963	681,3	54,76	382,4	140,7	404,9	0,791	33 215	29,48	54,26	30,56	337,3	595,0	25 076
1964	762,5	62,60	420,2	158,0	449,2	0,901	36 360	33,41	63,85	33,33	372,4	635,8	29 646
1965	830,0	70,32	459,2	179,8	483,5	0,959	39 124	35,14	71,31	35,80	403,7	689,0	32 750
1966	892,1	77,18	488,2	200,0	523,4	1,010	42 391	36,80	77,65	38,14	433,6	754,2	38 029
1967	955,3	84,81	494,4	216,1	565,4	1,104	46 695	37,77	85,19	40,36	460,1	797,9	44 567
1968	1 022,3	94,36	533,3	234,5	614,5	1,245	50 614	41,37	94,46	43,79	500,6	871,0	52 853
1969	1 134,2	107,32	596,9	266,5	700,7	1,438	55 876	47,57	106,98	46,78	556,5	941,4	62 181
1970	1 262,1	118,63	675,3	298,9	782,6	1,620	62 883	54,04	120,50	51,31	625,1	989,5	73 285
1971	1 382,0	131,12	750,6	330,3	872,4	1,853	68 510	55,97	136,36	57,64	695,1	1 074,2	80 632
1972	1 545,4	150,73	823,7	377,7	981,1	2,238	75 124	62,41	154,32	63,82	772,2	1 181,3	92 306
1973	1 755,0	172,86	917,3	484,2	1 114,2	2,701	89 746	76,41	176,80	73,78	888,0	1 317,1	112 420
1974	2 056,8	193,63	984,6	564,2	1 278,3	2,988	110 719	93,24	200,13	83,90	1 007,0	1 423,4	134 169
1975	2 271,1	216,26	1 026,5	672,2	1 452,3	3,789	125 378	86,63	220,25	105,96	1 130,0	1 542,2	148 031
1976	2 571,6	251,21	1 119,7	824,9	1 678,0	4,621	156 657	99,50	252,59	126,45	1 295,8	1 709,9	165 851
1977	2 774,1	279,31	1 196,1	963,7	1 884,6	5,642	190 083	101,87	274,93	145,43	1 439,9	1 907,5	184 460
1978	2 979,2	311,38	1 285,1	1 161,4	2 141,1	6,684	222 254	112,08	297,01	167,49	1 598,1	2 145,7	202 638
1979	3 180,1	346,89	1 392,5	1 428,8	2 442,3	7,783	270 198	123,32	315,96	195,92	1 799,0	2 388,4	218 616
1980	3 419,6	373,79	1 481,4	1 710,9	2 769,3	9,178	338 743	135,20	336,74	229,56	2 026,9	2 606,6	235 912
1981	3 554,4	407,79	1 544,1	2 034,8	3 111,4	11,058	401 579	143,20	352,85	253,45	2 222,7	2 934,9	252 546
1982	3 849,5	467,30	1 600,3	2 531,7	3 569,3	12,989	471 390	153,73	368,86	276,42	2 423,4	3 045,3	264 707
1983	4 095,0	515,40	1 667,5	3 040,7	3 957,0	14,452	535 904	163,20	378,44	300,23	2 592,7	3 275,7	274 568
1984	4 382,7	566,13	1 742,0	3 741,5	4 301,1	16,078	608 598	178,20	394,94	319,00	2 775,2	3 640,6	292 206
1985	4 677,5	602,15	1 819,3	4 464,2	4 600,4	17,475	675 596	188,90	412,64	347,87	2 965,1	3 865,8	309 917
1986	4 967,4	634,77	1 918,1	5 213,0	4 868,1	18,787	739 842	201,04	424,94	372,14	3 140,0	4 128,9	326 504

Table 5

Gross domestic product at current market prices

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	6,4	11,0	9,6	12,8	9,1	7,7	11,2	4,8	5,6	6,7	8,7	3,6	23,6
1962	7,0	12,7	8,8	6,2	11,7	8,3	12,4	0,4	7,7	4,7	8,8	7,7	10,9
1963	7,5	6,4	6,0	11,7	12,1	7,5	14,5	7,7	8,5	6,2	9,0	5,6	15,5
1964	11,9	14,3	9,9	12,3	10,9	13,8	9,5	13,3	17,7	9,1	10,4	6,9	18,2
1965	8,8	12,3	9,3	13,8	7,6	6,5	7,6	5,2	11,7	7,4	8,4	8,4	10,5
1966	7,5	9,8	6,3	11,2	8,3	5,4	8,4	4,7	8,9	6,5	7,4	9,5	16,1
1967	7,1	9,9	1,3	8,1	8,0	9,2	10,2	2,6	9,7	5,8	6,2	5,8	17,2
1968	7,0	11,3	7,9	8,5	8,7	12,8	8,4	9,5	10,9	8,5	8,5	9,2	18,6
1969	10,9	13,7	11,9	13,6	14,0	15,5	10,4	15,0	13,3	6,8	11,0	8,1	17,6
1970	11,3	10,5	13,1	12,2	11,7	12,6	12,5	13,6	12,6	9,7	11,8	5,1	17,9
1961-70	8,5	11,2	8,4	11,0	10,2	9,9	10,5	7,6	10,6	7,1	9,0	7,0	16,6
1971	9,5	10,5	11,1	10,5	11,5	14,4	8,9	3,6	13,2	12,3	11,1	8,6	10,0
1972	11,8	15,0	9,8	14,4	12,5	20,7	9,7	11,5	13,2	10,7	11,1	10,0	14,5
1973	13,6	14,7	11,4	28,2	13,6	20,7	19,5	22,4	14,6	15,6	14,9	11,5	21,8
1974	17,2	12,0	7,3	16,5	14,7	10,6	23,4	22,0	13,2	13,7	14,1	8,1	19,3
1975	10,4	11,7	4,3	19,1	13,6	26,8	13,2	−7,1	10,1	26,3	13,6	8,3	10,3
1976	13,2	16,2	9,1	22,7	15,5	22,0	24,9	14,9	14,7	19,3	16,4	10,9	12,0
1977	7,9	11,2	6,8	16,8	12,3	22,1	21,3	2,4	8,8	15,0	12,9	11,6	11,2
1978	7,4	11,5	7,4	20,5	13,6	18,5	16,9	10,0	8,0	15,2	12,5	12,5	9,9
1979	6,7	11,4	8,4	23,0	14,1	16,4	21,6	10,0	6,4	17,0	14,0	11,3	7,9
1980	7,5	7,8	6,4	19,7	13,4	17,9	25,4	9,6	6,6	17,2	14,0	9,1	7,9
1971-80	10,5	12,2	8,2	19,1	13,5	18,9	18,3	9,6	10,8	16,2	13,4	10,2	12,4
1981	3,9	9,1	4,2	18,9	12,4	20,5	18,5	5,9	4,8	10,4	10,4	12,6	7,1
1982	8,3	14,6	3,6	24,4	14,7	17,5	17,4	7,4	4,5	9,1	10,6	3,8	4,8
1983	6,4	10,3	4,2	20,1	10,9	11,3	13,7	6,2	2,6	8,6	8,8	7,6	3,7
1984	7,0	9,8	4,5	23,0	8,7	11,3	13,6	9,2	4,4	6,3	8,0	11,1	6,4
1985	6,7	6,4	4,4	19,3	7,0	8,7	11,0	6,0	4,5	9,0	7,6	6,2	6,1
1986	6,2	5,4	5,4	16,8	5,8	7,5	9,5	6,4	3,0	7,0	6,7	6,8	5,4

Table 6

Gross domestic product at current market prices

('000 million ECU)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	10,5	5,6	68,2	3,3	56,9	1,7	35,2	0,5	11,0	68,2	261,4	478,5	41,7
1961	11,1	6,2	77,0	3,7	61,4	1,8	38,7	0,5	11,9	72,0	284,7	490,4	51,0
1962	11,8	7,0	84,3	3,9	68,4	1,9	43,4	0,5	12,9	75,3	309,8	526,9	56,4
1963	12,7	7,4	89,4	4,4	76,7	2,1	49,7	0,6	14,0	80,0	337,3	556,1	65,1
1964	14,3	8,5	98,2	4,9	85,0	2,4	54,4	0,6	16,5	87,2	372,4	594,3	77,0
1965	15,5	9,5	107,3	5,6	91,5	2,5	58,5	0,7	18,4	93,7	403,7	644,0	85,0
1966	16,7	10,4	114,1	6,2	99,1	2,6	63,4	0,7	20,1	99,8	433,6	705,0	98,7
1967	17,9	11,4	116,1	6,8	107,5	2,8	70,2	0,7	22,1	104,1	460,1	749,3	116,3
1968	19,9	12,2	129,6	7,6	121,0	2,9	78,7	0,8	25,4	102,2	500,6	846,6	142,7
1969	22,2	14,0	148,3	8,7	132,4	3,4	87,5	0,9	28,9	109,8	556,5	920,9	169,0
1970	24,7	15,5	180,5	9,7	137,8	3,8	98,4	1,1	32,6	120,5	625,1	968,0	199,1
1971	27,2	16,9	205,9	10,5	151,1	4,3	105,8	1,1	37,3	134,5	695,1	1 025,2	221,6
1972	31,3	19,4	230,3	11,2	173,4	5,0	114,8	1,3	42,9	142,2	772,2	1 053,0	271,7
1973	36,7	23,3	280,0	13,1	203,8	5,4	125,3	1,6	51,6	146,9	888,0	1 069,3	337,4
1974	44,3	26,7	319,3	15,8	222,9	5,9	142,7	2,0	62,5	164,6	1 007,0	1 193,4	386,1
1975	49,8	30,4	336,6	16,8	273,0	6,8	154,9	1,9	70,3	189,2	1 130,0	1 242,9	402,6
1976	59,6	37,2	397,7	20,2	313,9	7,4	168,4	2,3	85,5	203,4	1 295,8	1 529,4	500,7
1977	67,9	40,7	451,7	22,9	336,2	8,6	188,8	2,5	98,2	222,5	1 439,9	1 671,6	603,2
1978	74,4	44,4	502,8	24,8	373,0	10,1	205,7	2,8	107,8	252,3	1 598,1	1 684,1	758,7
1979	79,2	48,1	554,6	28,1	419,0	11,6	237,3	3,1	115,0	303,1	1 799,0	1 742,5	727,6
1980	84,2	47,8	586,9	28,8	471,9	13,6	284,8	3,3	122,0	383,6	2 026,9	1 872,1	748,8
1981	86,1	51,5	614,2	33,0	515,1	16,0	317,9	3,5	127,1	458,2	2 222,7	2 628,8	1 029,2
1982	86,1	57,3	673,5	38,7	555,0	18,8	356,1	3,4	141,1	493,2	2 423,4	3 108,3	1 086,9
1983	90,1	63,4	734,4	38,9	584,4	20,2	397,0	3,6	149,2	511,4	2 592,7	3 679,7	1 299,1
1984	96,4	69,5	778,4	42,3	625,6	22,1	440,4	3,9	156,5	540,0	2 775,2	4 621,5	1 562,4
1985	104,2	75,0	815,1	44,3	675,0	24,4	463,4	4,2	163,8	595,8	2 965,1	5 170,2	1 710,3
1986	111,4	78,8	874,1	43,4	713,6	26,1	475,7	4,5	171,9	640,4	3 140,0	4 845,2	1 710,0

Table 7

Gross domestic product at current market prices per head of population

(ECU)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	1 157	1 231	1 231	399	1 245	591	700	1 570	955	1 303	1 088	2 658	447
1961	1 211	1 341	1 371	441	1 330	633	766	1 613	1 024	1 364	1 173	2 680	542
1962	1 285	1 498	1 483	465	1 455	680	853	1 595	1 094	1 413	1 263	2 836	594
1963	1 372	1 582	1 557	517	1 603	727	970	1 701	1 171	1 492	1 362	2 951	679
1964	1 522	1 795	1 694	578	1 760	823	1 054	1 905	1 360	1 616	1 491	3 109	794
1965	1 642	2 000	1 831	655	1 877	873	1 126	1 982	1 498	1 724	1 602	3 328	868
1966	1 754	2 177	1 929	724	2 016	917	1 212	2 060	1 610	1 827	1 708	3 605	999
1967	1 878	2 361	1 958	776	2 171	982	1 332	2 118	1 754	1 894	1 802	3 795	1 164
1968	2 072	2 512	2 178	869	2 424	997	1 485	2 394	1 993	1 850	1 950	4 246	1 412
1969	2 309	2 862	2 468	990	2 632	1 153	1 640	2 758	2 246	1 980	2 152	4 573	1 651
1970	2 562	3 139	2 976	1 109	2 715	1 289	1 834	3 117	2 499	2 166	2 400	4 745	1 926
1971	2 809	3 408	3 359	1 190	2 949	1 452	1 959	3 214	2 826	2 406	2 649	4 957	2 097
1972	3 225	3 876	3 734	1 263	3 354	1 648	2 111	3 648	3 216	2 535	2 923	5 032	2 535
1973	3 770	4 641	4 517	1 467	3 910	1 750	2 287	4 560	3 838	2 613	3 343	5 059	3 104
1974	4 538	5 287	5 146	1 759	4 250	1 876	2 589	5 659	4 615	2 927	3 776	5 594	3 505
1975	5 088	6 000	5 444	1 858	5 180	2 130	2 794	5 296	5 143	3 366	4 228	5 769	3 610
1976	6 072	7 324	6 463	2 201	5 936	2 303	3 024	6 389	6 206	3 620	4 840	7 030	4 440
1977	6 909	8 007	7 356	2 463	6 334	2 638	3 376	6 893	7 086	3 960	5 367	7 607	5 298
1978	7 565	8 691	8 198	2 633	7 002	3 038	3 666	7 727	7 737	4 492	5 944	7 583	6 602
1979	8 049	9 404	9 038	2 947	7 834	3 452	4 216	8 458	8 191	5 391	6 672	7 760	6 279
1980	8 554	9 321	9 532	2 991	8 785	3 992	5 049	9 139	8 623	6 811	7 492	8 240	6 411
1981	8 736	10 049	9 958	3 394	9 546	4 648	5 627	9 483	8 925	8 128	8 193	11 462	8 747
1982	8 735	11 194	10 927	3 958	10 237	5 408	6 287	9 404	9 860	8 755	8 917	13 410	9 177
1983	9 144	12 393	11 956	3 953	10 735	5 762	6 985	9 821	10 383	9 072	9 527	15 726	10 893
1984	9 787	13 596	12 723	4 268	11 434	6 263	7 733	10 722	10 853	9 576	10 187	19 566	13 010
1985	10 574	14 676	13 376	4 435	12 279	6 861	8 128	11 505	11 314	10 557	10 873	21 683	14 142
1986	11 310	15 421	14 385	4 312	12 914	7 296	8 336	12 335	11 827	11 334	11 497	20 129	14 041

Table 8

Gross domestic product at constant market prices

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	5,0	6,4	5,2	11,1	5,5	4,7	8,2	4,4	3,1	3,3	5,2	2,6	14,6
1962	5,2	5,7	4,5	1,5	6,7	3,7	6,2	1,4	4,0	1,1	4,3	5,7	7,1
1963	4,4	0,6	3,2	10,1	5,3	4,8	5,6	2,6	3,6	4,2	4,4	4,0	10,5
1964	7,0	9,3	6,7	8,3	6,5	4,2	2,8	7,5	8,3	5,2	5,8	5,0	13,2
1965	3,6	4,6	5,5	9,4	4,8	2,0	3,3	1,7	5,2	2,3	4,1	6,2	5,1
1966	3,2	2,7	2,7	6,1	5,2	1,0	6,0	1,7	2,7	1,9	3,6	5,8	10,6
1967	3,9	3,7	0,0	5,5	4,7	5,1	7,2	1,6	5,3	2,8	3,4	2,8	10,8
1968	4,2	3,8	5,7	6,7	4,3	8,1	6,5	4,2	6,4	4,2	5,2	4,0	12,8
1969	6,6	6,5	7,4	9,9	7,0	6,1	6,1	8,9	6,4	1,3	5,6	2,9	12,3
1970	6,4	2,3	5,2	8,0	5,7	3,5	5,3	2,2	6,7	2,2	4,8	−0,2	9,8
1961-70	4,9	4,5	4,6	7,6	5,6	4,3	5,7	3,6	5,2	2,8	4,6	3,9	10,6
1971	3,7	2,4	3,3	7,1	5,4	3,4	1,6	4,3	4,3	2,7	3,4	3,1	4,6
1972	5,3	5,4	4,2	8,9	5,9	6,4	3,2	6,2	3,4	2,3	4,1	5,4	8,8
1973	5,9	3,8	4,5	7,3	5,4	4,7	7,0	10,8	5,7	7,9	6,0	5,7	8,8
1974	4,1	−0,7	0,7	−3,6	3,2	4,3	4,1	3,6	3,5	−1,1	1,7	−0,9	−1,0
1975	−1,5	−1,0	−1,6	6,1	0,2	3,7	−3,6	−6,1	−1,0	−0,7	−1,2	−0,8	2,3
1976	5,2	6,5	5,4	6,4	5,2	1,4	5,9	1,9	5,3	3,8	5,1	4,7	5,3
1977	0,4	2,3	3,1	3,4	3,1	8,2	1,9	0,6	2,4	1,0	2,3	5,5	5,3
1978	3,0	1,8	3,1	6,7	3,8	7,2	2,7	4,5	2,5	3,6	3,3	4,7	5,0
1979	2,0	3,5	4,1	3,7	3,3	2,8	4,9	4,0	2,4	2,1	3,5	2,6	5,1
1980	3,5	−0,4	2,0	1,8	1,1	3,3	3,9	1,7	0,9	−2,2	1,2	−0,4	4,9
1971-80	3,1	2,3	2,8	4,7	3,6	4,5	3,1	3,1	2,9	1,9	2,9	2,9	4,9
1981	−1,3	−0,9	0,1	−0,3	0,2	2,9	0,2	−1,8	−0,7	−1,1	−0,2	3,4	4,2
1982	1,1	3,0	−0,9	−0,1	2,0	1,9	−0,4	−1,1	−1,4	1,9	0,5	−3,0	3,0
1983	0,4	2,0	0,9	0,3	1,0	0,6	−1,2	−2,4	0,9	3,3	1,0	2,9	3,0
1984	1,7	3,9	2,6	2,6	1,6	4,4	2,6	3,2	1,7	1,8	2,2	7,1	5,8
1985	1,9	2,3	2,3	1,9	1,2	2,5	2,7	1,7	2,1	3,4	2,3	2,3	4,7
1986	1,7	3,2	3,5	1,0	1,9	2,3	2,7	1,3	1,9	2,0	2,5	2,5	4,0

Table 9

Industrial production

(annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	6,8	8,7	11,7	:	8,9	6,9	15,7	9,0	10,0	6,8	10,6	2,2	24,4
1961	6,2	5,1	6,1	:	5,5	8,6	10,8	2,9	3,6	0,0	5,5	0,7	19,4
1962	5,7	8,9	9,2	:	5,1	7,1	9,6	−4,2	3,5	1,1	5,1	8,3	7,9
1963	7,4	1,3	3,5	10,4	7,1	5,8	8,9	1,0	5,1	4,0	5,7	6,0	11,4
1964	6,5	11,7	7,7	10,9	6,1	7,7	1,2	9,2	9,7	7,9	6,2	6,7	15,6
1965	2,5	6,6	5,3	8,5	1,9	4,2	4,6	0,8	4,4	3,3	4,0	10,0	4,0
1966	2,0	2,9	1,3	16,0	5,4	3,0	11,4	−3,2	4,2	1,4	4,4	8,8	13,0
1967	1,8	3,9	−2,5	4,6	2,5	8,1	8,3	−0,6	2,7	0,2	1,8	2,3	19,2
1968	5,5	7,4	9,7	7,8	3,5	10,4	6,4	6,0	9,2	6,7	7,0	6,4	15,2
1969	9,7	12,4	12,7	11,8	10,4	7,1	3,7	12,8	10,8	3,3	8,3	4,5	15,9
1970	3,1	2,5	6,1	10,5	5,3	4,4	6,5	0,5	8,7	0,5	4,9	−3,0	13,7
1961-70	5,0	6,2	5,8	:	5,3	6,6	7,1	2,4	6,2	2,8	5,3	5,0	13,4
1971	1,7	2,4	1,4	11,3	4,8	3,7	−0,6	−1,1	5,5	−0,2	1,7	1,8	2,7
1972	7,5	4,4	4,2	14,1	6,7	4,3	4,9	4,2	5,1	2,2	4,7	9,2	7,3
1973	6,2	3,4	7,2	15,3	6,7	9,8	9,7	11,9	7,7	8,7	8,0	8,4	14,9
1974	4,0	−0,8	−1,1	−1,5	2,3	3,0	4,0	3,5	4,7	−2,4	0,8	−0,4	−3,9
1975	−9,8	−6,0	−6,2	4,3	−7,4	−6,1	−8,9	−21,9	−5,1	−4,7	−6,6	−8,9	−10,5
1976	7,8	9,6	7,4	10,6	8,6	8,7	11,6	3,8	7,7	2,7	7,6	10,8	11,0
1977	0,5	0,8	2,1	1,5	1,9	8,0	0,0	0,5	0,5	4,7	2,0	5,9	4,1
1978	2,4	2,3	3,0	7,5	2,3	7,9	2,1	3,2	0,8	3,9	2,8	5,8	6,1
1979	4,5	3,6	5,1	6,0	4,0	7,7	6,7	3,4	3,1	3,8	4,8	4,4	7,1
1980	−1,3	0,2	0,2	0,9	−0,5	−0,8	5,0	−3,3	−0,1	−6,7	−0,5	−3,6	4,6
1971-80	2,2	1,9	2,3	6,9	2,8	4,5	3,3	0,0	2,9	1,1	2,4	3,2	4,1
1981	−2,7	0,0	−1,9	−0,6	−2,3	2,2	−2,2	−5,7	−2,2	−3,5	−2,3	2,7	1,0
1982	0,0	2,7	−2,9	−4,2	−1,2	0,3	−3,1	0,9	−3,7	2,1	−1,5	−8,2	0,4
1983	2,0	3,2	0,6	−0,7	1,1	6,5	−2,4	5,4	2,1	3,4	0,8	6,5	3,6
1984	2,6	9,7	3,0	3,5	2,4	12,9	3,0	13,3	5,0	1,0	2,8	10,7	10,9
1985	3,3	4,3	4,5	0,5	1,5	5,5	3,1	3,0	3,5	4,6	3,4	:	:
1986	3,6	5,0	4,0	0,5	2,4	5,0	3,3	2,3	4,0	2,6	3,2	:	:

Table 10

Private consumption at current prices

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	69,2	62,0	59,4	80,3	61,9	76,6	62,7	55,2	58,2	66,3	62,9	63,8	58,9
1961	67,9	62,1	59,5	76,8	62,1	75,0	61,7	55,5	59,4	65,3	62,5	63,6	54,5
1962	66,6	61,9	59,5	76,4	62,1	74,7	62,0	58,4	60,1	66,1	62,7	62,7	57,2
1963	67,1	61,4	59,6	74,3	62,6	74,1	63,3	58,3	61,5	66,1	63,1	62,7	58,0
1964	64,1	60,3	58,4	73,6	61,6	72,6	62,7	57,5	59,1	64,7	61,9	62,8	57,2
1965	64,3	58,9	59,2	72,8	61,1	71,7	62,3	58,6	59,2	64,2	61,7	62,2	58,4
1966	63,9	59,6	59,7	72,3	61,0	71,8	63,4	58,8	59,1	63,7	61,9	61,4	57,9
1967	62,9	59,9	60,8	72,4	61,2	70,1	63,7	58,3	58,5	63,3	62,1	61,3	56,6
1968	63,7	58,8	60,1	71,9	61,4	71,0	62,8	56,9	57,7	62,7	61,7	61,6	54,6
1969	62,2	57,5	59,1	69,2	61,2	69,8	62,3	52,9	58,3	62,3	61,1	61,8	53,5
1970	59,8	57,4	58,4	69,2	60,0	68,9	62,6	51,3	58,1	61,7	60,4	62,8	52,2
1961-70	64,3	59,8	59,4	72,9	61,4	72,0	62,7	56,6	59,1	64,0	61,9	62,3	56,0
1971	60,3	55,8	58,7	68,0	60,5	68,0	62,4	54,9	57,3	61,5	60,5	62,8	53,5
1972	60,2	53,4	59,3	65,7	60,4	65,0	62,6	54,0	56,9	62,8	60,8	62,6	54,0
1973	60,6	54,5	58,8	63,4	60,0	64,4	62,5	48,8	56,4	61,9	60,3	61,9	53,6
1974	59,8	54,3	59,6	67,7	61,1	68,4	62,8	46,2	56,3	62,9	61,1	62,6	54,3
1975	61,2	55,5	63,2	67,5	61,9	64,2	64,3	57,5	58,5	61,1	62,3	63,5	57,1
1976	61,0	56,6	62,8	65,8	62,1	64,3	62,8	56,5	58,8	59,4	61,6	63,8	57,4
1977	61,9	56,9	63,0	65,9	62,2	63,8	62,1	59,8	59,8	59,0	61,5	63,5	57,4
1978	61,6	56,2	62,5	65,2	62,0	63,2	61,6	57,9	60,3	59,0	61,3	62,9	57,2
1979	62,6	56,4	62,0	63,3	62,1	64,8	61,1	57,7	60,9	59,8	61,3	63,2	58,1
1980	63,5	55,9	62,6	64,0	63,0	65,2	61,5	58,5	61,1	59,2	61,7	64,3	58,3
1971-80	61,3	55,5	61,3	65,6	61,5	65,1	62,4	55,2	58,6	60,7	61,2	63,1	56,1
1981	65,5	56,0	63,4	67,0	64,6	66,1	62,3	60,5	60,4	59,6	62,6	63,5	57,5
1982	65,4	55,1	63,3	66,6	64,6	62,1	62,3	61,0	60,1	59,8	62,5	65,6	58,7
1983	65,2	54,5	63,2	66,6	64,2	59,0	62,5	61,4	60,5	60,3	62,5	66,2	59,4
1984	65,0	54,3	62,3	65,3	63,8	57,3	62,3	59,2	59,2	60,6	62,1	64,7	58,5
1985	63,9	54,2	61,7	65,7	64,1	56,3	62,3	59,1	59,0	59,9	61,8	65,3	57,9
1986	62,4	53,6	61,5	65,4	64,2	55,9	61,9	58,6	59,3	60,6	61,8	65,1	57,9

Table 11

Private consumption at constant prices

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	1,6	7,3	5,9	6,8	5,9	2,8	7,5	4,9	5,2	2,2	5,0	2,1	8,4
1962	3,9	5,9	5,5	4,3	7,1	3,6	7,1	4,5	6,1	2,2	5,2	4,5	9,5
1963	4,4	0,0	3,0	5,1	6,9	4,1	9,3	4,5	7,0	4,6	5,4	3,8	9,6
1964	2,6	7,8	5,3	8,8	5,6	4,3	3,3	8,5	5,9	3,0	4,5	5,5	11,6
1965	4,3	3,4	7,0	7,7	4,0	0,4	3,3	3,9	7,5	1,5	4,2	5,6	5,6
1966	2,7	4,3	3,7	6,8	4,8	1,6	7,2	1,5	3,2	1,7	4,0	5,1	9,7
1967	2,8	3,6	1,5	6,2	5,1	3,4	7,4	−0,5	5,4	2,4	3,8	3,1	9,5
1968	5,3	1,4	4,9	6,9	4,0	8,5	5,2	4,3	6,6	2,8	4,3	5,4	8,3
1969	5,4	6,2	7,5	6,2	6,0	5,7	6,6	5,0	7,9	0,6	5,3	3,7	10,1
1970	4,4	3,0	7,4	8,8	4,3	2,9	7,6	5,9	7,7	2,7	5,6	2,3	6,9
1961-70	3,7	4,3	5,2	6,7	5,4	3,7	6,4	4,2	6,2	2,3	4,7	4,1	8,9
1971	4,8	−0,6	5,6	5,6	6,6	3,2	2,9	5,8	3,0	3,1	4,4	3,7	5,9
1972	6,0	1,6	5,0	7,0	6,1	5,1	3,4	4,3	3,2	6,1	5,1	5,7	9,5
1973	7,7	5,7	3,0	7,6	5,8	7,2	5,9	5,4	3,9	5,1	5,0	4,0	9,3
1974	2,6	−2,5	1,1	0,7	2,9	1,6	2,6	5,0	2,7	−1,4	1,3	−0,7	−0,7
1975	0,6	3,6	4,2	5,5	3,4	−2,7	−1,6	5,1	3,4	−0,7	1,7	2,1	4,1
1976	4,6	7,9	4,0	5,3	5,6	2,8	3,4	3,0	5,7	0,3	3,7	5,6	3,4
1977	2,3	2,0	3,5	4,6	3,1	6,8	1,4	2,4	4,4	−0,5	2,3	4,8	3,8
1978	2,6	1,0	3,7	5,7	4,2	9,0	2,7	3,0	4,3	5,5	4,0	4,2	4,7
1979	4,4	1,4	3,1	2,7	3,5	4,3	4,9	3,6	3,0	4,5	3,8	2,7	5,9
1980	2,3	−3,7	1,7	−0,2	1,5	1,5	4,8	3,2	0,0	−0,4	1,6	0,6	1,3
1971-80	3,8	1,6	3,5	4,4	4,3	3,8	3,0	4,1	3,4	2,1	3,3	3,2	4,7
1981	−1,2	−2,3	−0,2	1,0	2,1	2,1	0,8	1,7	−2,5	−0,0	0,4	2,0	0,8
1982	0,7	1,5	−1,4	2,1	3,2	−4,9	0,2	−1,7	−1,2	1,0	0,6	1,2	4,2
1983	−0,9	1,7	1,1	0,6	0,7	−3,5	−0,6	−1,2	0,4	4,2	1,1	4,5	3,3
1984	0,5	2,8	0,6	2,1	0,7	−0,5	1,8	−1,2	−0,6	1,7	1,0	5,3	2,8
1985	0,0	1,7	1,3	1,7	1,5	1,1	2,4	1,9	1,8	2,3	1,7	3,9	3,0
1986	0,5	2,6	3,6	0,2	1,9	1,2	2,2	2,0	2,3	3,7	2,7	2,0	3,1

Table 12

Public consumption at current prices

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	12,4	13,3	10,7	11,7	13,0	12,5	12,8	9,8	12,8	16,4	13,2	16,9	8,0
1961	11,9	14,4	11,1	11,3	13,1	12,4	12,7	9,5	13,4	16,6	13,4	17,8	7,5
1962	12,3	15,2	11,9	11,6	13,3	12,5	13,1	10,9	13,9	17,0	13,8	18,0	7,8
1963	13,0	15,4	12,6	11,3	13,4	12,7	13,9	12,2	14,7	16,8	14,2	17,8	8,0
1964	12,5	15,6	11,9	11,7	13,3	13,3	14,3	10,8	14,8	16,4	13,9	17,5	7,9
1965	12,8	16,3	12,1	11,7	13,1	13,6	15,1	10,9	14,8	16,8	14,2	17,1	8,2
1966	13,1	17,1	12,1	11,8	13,0	13,6	14,9	11,4	15,2	17,1	14,2	18,1	8,0
1967	13,5	17,8	12,6	13,0	13,0	13,4	14,4	11,9	15,5	17,9	14,5	19,4	7,7
1968	13,6	18,6	11,8	12,9	13,5	13,4	14,5	11,8	15,2	17,5	14,4	19,2	7,4
1969	13,6	18,9	11,9	12,7	13,3	13,5	14,2	10,9	15,3	17,1	14,2	18,9	7,3
1970	13,4	20,0	12,0	12,6	13,4	14,6	13,8	10,7	15,6	17,6	14,3	19,2	7,4
1961-70	13,0	16,9	12,0	12,1	13,3	13,3	14,1	11,1	14,8	17,1	14,1	18,3	7,7
1971	14,1	21,3	12,7	12,5	13,4	15,2	15,5	11,7	16,0	17,8	14,9	18,5	8,0
1972	14,5	21,3	12,7	12,2	13,2	15,3	16,1	11,9	15,9	18,4	15,0	18,4	8,2
1973	14,5	21,3	13,0	11,5	13,2	15,7	15,5	11,3	15,6	18,2	15,0	17,8	8,3
1974	14,7	23,4	13,9	13,8	13,6	17,2	15,1	11,5	16,3	19,9	15,7	18,5	9,1
1975	16,4	24,6	14,4	15,2	14,4	18,6	15,4	14,9	17,4	21,8	16,6	19,1	10,1
1976	16,5	24,1	13,7	15,1	14,6	18,2	14,8	14,8	17,2	21,4	16,3	18,7	9,9
1977	16,8	23,9	13,5	16,0	14,7	17,2	15,3	16,0	17,4	20,3	16,1	18,2	9,9
1978	17,5	24,5	13,6	15,9	15,0	17,3	15,9	15,6	17,7	19,9	16,3	17,7	9,7
1979	17,6	25,0	13,6	16,3	14,9	18,4	16,2	15,8	18,1	19,8	16,3	17,6	9,8
1980	18,0	26,7	13,9	16,4	15,2	20,3	16,4	16,7	17,9	21,3	16,8	18,3	10,0
1971-80	16,1	23,6	13,5	14,5	14,2	17,4	15,6	14,0	17,0	19,9	15,9	18,3	9,3
1981	18,8	27,8	14,1	18,1	15,8	20,5	18,3	17,5	17,8	21,9	17,5	18,2	10,1
1982	18,4	28,0	13,9	18,6	16,2	20,3	18,6	17,2	17,7	21,8	17,6	19,2	10,2
1983	17,7	27,2	13,7	18,8	16,3	20,2	19,5	17,3	17,6	22,0	17,8	18,9	10,2
1984	17,3	25,9	13,6	19,0	16,3	19,5	19,7	16,9	16,8	21,9	17,7	18,5	10,0
1985	17,0	25,3	13,6	20,2	16,2	19,2	19,7	16,7	16,3	21,4	17,6	:	:
1986	16,6	24,6	13,5	19,7	16,1	18,5	19,3	16,8	15,9	21,2	17,3	:	:

Table 13

Public consumption at constant prices

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	1,9	5,3	6,7	4,4	4,8	2,9	4,4	1,3	2,8	3,5	4,5	6,1	6,1
1962	8,6	9,9	10,4	6,7	4,7	2,9	3,9	2,4	3,3	3,1	5,5	5,3	8,4
1963	11,6	2,9	6,3	4,2	3,4	4,2	4,3	5,8	4,7	1,8	4,1	1,5	8,7
1964	4,2	7,3	0,6	9,3	4,2	3,0	4,2	−0,8	1,7	1,6	2,6	2,5	6,0
1965	5,5	3,4	4,0	9,0	3,2	3,6	4,0	2,5	1,5	2,6	3,4	2,8	6,3
1966	4,7	5,8	1,0	6,3	2,7	1,1	4,0	5,8	1,7	2,7	2,6	10,2	5,8
1967	5,7	7,6	2,9	8,5	4,3	5,3	4,4	4,2	2,4	5,7	4,5	8,0	4,7
1968	3,5	4,7	−1,4	1,3	5,6	4,9	5,2	5,6	2,2	0,4	2,2	3,0	5,7
1969	6,3	6,8	4,6	7,7	4,1	6,7	2,8	3,3	4,5	−1,9	2,6	0,5	5,1
1970	3,1	6,9	4,4	5,9	4,2	7,5	2,6	4,1	6,0	1,6	3,4	−1,2	5,7
1961-70	5,5	6,0	3,9	6,3	4,1	4,2	4,0	3,4	3,1	2,1	3,5	3,8	6,2
1971	5,5	5,5	3,9	4,9	3,5	8,7	5,7	3,8	3,3	3,1	4,0	−2,1	5,4
1972	5,9	5,7	2,3	5,7	2,7	7,5	5,3	4,0	1,8	4,2	3,7	2,5	5,2
1973	5,3	4,0	3,7	6,8	3,2	6,8	2,4	3,3	0,7	4,9	3,6	0,6	5,0
1974	3,4	3,5	2,5	12,1	1,2	7,6	2,8	4,8	2,0	1,5	2,3	3,3	3,5
1975	4,5	2,0	1,1	11,9	4,7	6,5	3,2	6,6	3,9	5,5	3,9	2,2	6,8
1976	3,7	4,5	0,0	5,1	6,2	2,6	2,2	1,9	4,0	1,3	2,5	1,9	4,1
1977	2,3	2,4	1,2	6,5	1,4	2,1	2,8	3,0	3,2	−1,6	1,1	1,9	3,9
1978	6,0	6,2	3,8	3,5	4,3	8,2	2,3	2,0	3,9	2,3	3,4	2,1	5,0
1979	2,5	5,9	3,8	5,8	1,8	6,8	1,6	4,7	2,8	2,1	2,6	2,5	4,3
1980	1,5	4,3	2,2	0,2	1,8	7,0	2,1	4,6	0,6	1,5	1,9	2,6	2,9
1971-80	4,1	4,4	2,4	6,2	3,1	6,4	3,0	3,8	2,6	2,5	2,9	1,7	4,6
1981	1,2	2,6	0,8	6,8	2,3	2,0	3,3	2,1	2,0	0,0	1,6	2,4	5,2
1982	−1,2	2,8	−0,9	1,9	2,5	4,0	2,3	0,3	0,7	0,9	1,1	2,8	2,3
1983	0,3	−0,0	−0,2	2,4	1,9	0,1	2,7	0,0	1,5	2,6	1,6	0,6	2,4
1984	−0,2	−0,0	2,4	3,9	0,3	−1,2	2,7	−1,3	−1,6	1,0	1,2	2,9	2,3
1985	0,4	0,2	1,5	4,3	1,0	0,5	1,9	0,7	0,5	1,0	1,2	4,1	2,5
1986	−0,0	0,0	2,0	0,7	0,9	−0,5	1,5	0,0	0,3	0,8	1,1	1,5	1,9

Table 14

Gross fixed investment at current prices; total economy

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	19,3	21,6	24,3	19,0	20,1	14,4	22,6	21,0	24,1	16,4	20,8	17,9	29,5
1961	20,7	23,2	25,2	18,2	21,2	16,3	23,2	23,2	24,8	17,3	21,7	17,4	32,6
1962	21,3	23,1	25,7	20,1	21,4	17,9	23,7	26,1	24,5	17,0	22,0	17,6	32,9
1963	20,7	22,0	25,6	19,2	22,1	19,5	24,0	29,9	23,8	16,8	22,0	17,9	31,5
1964	22,4	24,5	26,6	21,0	22,9	20,5	22,2	33,5	25,5	18,4	22,8	18,1	31,7
1965	22,4	24,1	26,1	21,6	23,3	21,4	19,3	28,0	25,1	18,5	22,3	18,7	29,9
1966	22,9	24,1	25,4	21,7	23,7	19,8	18,8	26,6	26,2	18,5	22,1	18,5	30,4
1967	22,9	24,2	23,1	20,3	23,8	20,1	19,5	23,3	26,3	19,1	21,8	17,9	32,1
1968	21,5	23,4	22,4	23,2	23,3	20,9	20,3	21,4	26,9	19,4	21,7	18,1	33,2
1969	21,3	24,6	23,3	24,6	23,4	23,3	21,0	21,7	24,6	18,9	22,0	18,2	34,5
1970	22,7	24,7	25,5	23,6	23,4	22,7	21,4	23,5	25,8	19,0	22,7	17,6	35,5
1961-70	21,9	23,8	24,9	21,4	22,9	20,2	21,3	25,7	25,3	18,3	22,1	18,0	32,4
1971	22,1	24,2	26,1	25,2	23,6	23,6	20,4	28,4	25,9	18,9	22,8	18,1	34,3
1972	21,3	24,6	25,4	27,8	23,7	23,7	19,8	28,2	23,7	18,7	22,4	18,7	34,2
1973	21,4	24,8	23,9	28,0	23,8	25,3	20,8	27,4	23,1	20,1	22,5	19,1	36,4
1974	22,7	24,0	21,6	22,2	24,3	24,6	22,4	24,7	21,8	20,6	22,3	18,4	34,8
1975	22,5	21,1	20,4	20,8	23,3	22,6	20,6	27,8	20,9	20,1	21,2	17,0	32,4
1976	22,1	23,0	20,2	21,2	23,3	25,2	20,0	24,5	19,3	19,5	20,9	17,1	31,3
1977	21,7	22,1	20,3	23,0	22,3	25,0	19,6	25,3	21,1	18,6	20,5	18,3	30,5
1978	21,7	21,7	20,8	23,9	21,4	28,0	18,7	23,9	21,3	18,6	20,3	19,5	30,8
1979	20,8	20,9	21,9	25,8	21,5	31,1	18,8	24,6	21,0	18,8	20,7	19,8	32,1
1980	21,3	18,8	22,8	24,2	21,9	28,7	19,8	26,2	21,0	18,1	21,0	18,5	32,0
1971-80	21,8	22,5	22,3	24,2	22,9	25,8	20,1	26,1	21,9	19,2	21,4	18,4	32,9
1981	18,1	15,6	21,9	22,3	21,4	29,5	20,2	23,3	19,2	16,5	20,1	17,8	31,0
1982	17,5	16,1	20,7	20,2	20,5	25,8	19,0	24,1	18,2	16,6	19,2	16,5	29,9
1983	16,1	16,3	20,8	20,5	19,6	22,6	18,0	23,1	18,1	16,5	18,8	16,8	28,4
1984	16,2	17,6	20,5	18,8	18,7	21,0	17,9	22,2	18,4	17,5	18,7	17,8	27,9
1985	16,6	19,0	19,7	19,0	18,4	21,0	18,2	21,8	18,4	17,5	18,5	18,1	27,5
1986	16,7	19,9	19,9	19,2	18,2	20,9	18,4	21,3	18,6	17,5	18,6	18,7	27,2

Table 15

Gross fixed investment at constant prices; total economy

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	12,4	13,9	6,8	8,1	10,9	15,9	11,6	9,1	6,0	9,8	9,4	1,6	27,8
1962	5,9	6,7	4,1	8,4	8,5	14,8	9,8	7,8	3,4	0,7	5,5	7,4	11,3
1963	0,1	−2,4	1,3	5,5	8,8	12,0	8,1	14,2	1,1	1,4	4,0	7,4	10,4
1964	14,7	23,5	11,2	20,7	10,5	11,6	−5,8	21,0	19,2	16,6	9,4	6,6	16,7
1965	4,1	4,7	4,8	12,8	7,0	10,0	−8,4	−13,1	5,3	4,8	2,9	10,3	3,2
1966	6,8	4,3	1,2	3,2	7,3	−3,0	4,3	−5,1	8,0	2,5	3,7	5,0	13,4
1967	2,9	5,5	−6,9	−1,6	6,0	6,5	11,7	−9,0	8,5	8,8	3,5	−1,3	18,2
1968	−1,3	1,8	3,6	21,4	5,5	13,1	10,8	−4,1	11,2	6,2	6,4	6,1	20,0
1969	5,3	12,1	10,5	18,6	9,2	18,3	7,8	10,2	−2,2	−0,7	6,7	2,4	18,9
1970	8,4	2,4	9,9	−1,4	4,6	0,3	3,0	9,2	9,5	2,6	5,5	−3,6	16,9
1961-70	5,8	7,0	4,5	9,3	7,8	9,8	5,1	3,5	6,8	5,1	5,7	4,1	15,5
1971	−1,9	1,7	6,2	14,0	7,1	8,8	−3,2	15,1	3,4	1,9	3,5	5,4	4,3
1972	3,4	8,6	2,6	15,4	7,2	7,4	0,9	6,0	−2,8	−0,3	2,9	8,5	10,4
1973	7,0	4,3	−0,2	7,7	6,1	16,2	7,7	11,4	4,5	7,2	4,8	7,3	13,7
1974	6,9	−9,0	−9,5	−25,6	0,9	−11,6	3,3	−5,2	−3,8	−4,1	−3,5	−6,8	−9,1
1975	−1,9	−12,2	−4,9	0,2	−3,2	−2,6	−12,7	−7,1	−4,9	0,2	−4,9	−11,2	−1,1
1976	4,0	17,4	4,6	6,8	3,7	13,6	2,3	−5,2	−2,8	1,5	3,4	6,3	3,0
1977	0,0	−2,3	3,8	7,8	−0,8	4,1	−0,4	1,8	11,7	−2,6	1,0	10,5	4,8
1978	2,8	1,4	4,9	6,0	1,5	18,9	−0,1	0,3	2,5	3,9	2,9	9,5	9,4
1979	−2,7	−0,4	7,2	8,8	3,7	13,4	5,8	7,0	−1,7	2,3	4,3	3,1	6,3
1980	4,6	−12,6	3,2	−6,5	3,2	−6,9	9,4	5,9	−0,9	−5,2	1,8	−6,1	1,1
1971-80	2,2	−0,7	1,6	2,8	2,9	5,6	1,1	2,8	0,4	0,4	1,6	2,4	4,1
1981	−16,3	−19,2	−4,2	−7,8	−1,6	8,0	0,6	−13,4	−10,4	−8,5	−4,6	1,1	3,6
1982	−0,9	5,4	−4,7	−1,5	−0,6	−6,2	−5,2	−2,1	−4,1	6,7	−1,6	−6,6	1,8
1983	−6,4	3,2	3,0	−1,4	−1,4	−7,9	−5,3	−5,4	0,4	4,2	0,0	8,1	0,2
1984	2,3	12,8	0,8	−4,7	−2,3	−1,8	4,1	−1,3	4,3	8,4	2,3	16,6	5,7
1985	5,2	10,2	−1,2	2,3	−0,2	2,5	4,9	0,0	2,5	3,1	1,6	6,1	5,1
1986	3,0	8,6	4,9	1,1	1,9	2,3	5,6	0,8	2,5	2,6	3,7	6,7	4,1

Table 16

Net stockbuilding at current prices

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	−0,1	4,4	3,0	−0,4	3,0	2,0	2,1	1,0	3,3	2,2	2,5	0,7	3,6
1961	0,5	1,9	2,0	1,8	1,7	1,4	2,3	5,3	2,7	1,0	1,7	0,4	7,2
1962	−0,0	2,9	1,6	1,1	2,3	1,6	1,7	4,0	1,5	−0,0	1,3	1,2	2,2
1963	0,4	0,8	0,7	2,1	1,5	0,9	1,0	−0,2	1,1	0,5	0,9	0,9	3,6
1964	1,5	1,7	1,5	4,7	2,4	1,2	0,5	−1,9	3,0	2,1	1,8	0,7	3,7
1965	0,8	2,3	2,3	4,7	1,6	2,3	0,7	1,1	1,9	1,3	1,6	1,3	2,1
1966	1,0	0,8	1,1	0,6	2,0	0,8	0,8	0,6	1,3	0,8	1,1	1,5	2,1
1967	0,4	0,0	−0,1	2,0	1,8	−0,4	1,1	−1,6	0,9	0,7	0,8	1,2	3,4
1968	0,9	0,6	2,1	−0,1	1,8	1,1	0,0	−0,2	0,6	1,0	1,2	1,1	3,6
1969	1,9	1,3	2,9	1,3	2,6	2,4	0,7	−0,1	2,4	1,1	1,9	1,1	3,1
1970	1,6	1,0	2,1	4,5	2,7	1,7	1,7	2,1	2,5	0,7	1,9	0,2	3,5
1961-70	0,9	1,3	1,6	2,3	2,0	1,3	1,1	0,9	1,8	0,9	1,4	1,0	3,5
1971	1,4	0,6	0,6	2,7	1,5	0,3	0,6	2,6	1,4	0,2	0,8	0,8	1,5
1972	0,5	0,2	0,6	1,8	1,9	1,4	0,6	1,3	0,7	0,0	0,8	0,7	1,4
1973	1,3	1,3	1,4	7,8	2,4	1,6	3,4	0,9	1,8	2,1	2,2	1,2	1,7
1974	2,2	1,2	0,5	7,1	2,4	4,4	4,2	−2,1	2,9	1,5	2,1	0,8	2,5
1975	−0,6	−0,2	−0,6	6,2	−0,3	0,6	−0,3	−3,3	−0,2	−1,4	−0,5	−0,4	0,3
1976	0,2	1,0	1,1	5,1	1,2	0,3	3,6	−0,0	1,3	0,6	1,5	0,7	0,6
1977	0,3	0,8	0,7	3,5	1,1	3,2	1,8	−3,1	0,6	1,2	1,2	1,4	0,7
1978	0,2	−0,2	0,6	3,7	0,6	1,5	1,3	3,2	0,6	1,0	0,9	1,3	0,5
1979	0,7	0,5	1,9	4,3	1,4	2,4	2,4	−0,1	0,5	1,1	1,6	0,6	0,8
1980	−0,0	−0,3	1,3	4,4	1,7	−0,6	5,2	1,6	0,5	−1,3	1,5	−0,3	0,7
1971-80	0,6	0,5	0,8	4,6	1,4	1,5	2,3	0,1	1,0	0,5	1,2	0,7	1,1
1981	−0,0	−0,2	−0,3	3,2	−0,2	−1,4	1,1	3,8	−0,9	−1,2	−0,1	1,2	0,5
1982	−0,4	0,3	−0,3	2,0	1,1	−0,6	1,1	1,9	−0,3	−0,5	0,3	−0,5	0,5
1983	−0,4	−0,1	0,3	1,0	0,5	0,6	−0,6	2,0	−0,2	0,1	0,1	−0,1	0,1
1984	−0,0	1,1	0,6	6,7	0,3	2,2	0,7	1,6	0,5	−0,1	0,6	1,5	0,6
1985	0,1	0,7	1,0	5,7	0,4	0,8	1,1	1,7	0,8	0,2	0,7	:	:
1986	0,4	0,5	1,2	5,4	0,6	0,4	1,0	1,7	0,7	0,2	0,8	:	:

Table 17

Price deflator GDP at market prices

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	1,3	4,3	4,2	1,5	3,4	2,8	2,8	0,4	2,4	3,3	3,3	1,0	7,9
1962	1,7	6,6	4,1	4,6	4,7	4,4	5,8	−1,0	3,5	3,7	4,3	1,9	3,6
1963	3,0	5,8	2,7	1,4	6,4	2,6	8,5	5,0	4,7	2,0	4,4	1,5	4,5
1964	4,6	4,6	3,0	3,7	4,1	9,2	6,5	5,4	8,7	3,7	4,4	1,7	4,4
1965	5,1	7,4	3,6	4,0	2,7	4,4	4,2	3,4	6,1	5,1	4,2	2,0	5,1
1966	4,2	6,8	3,5	4,9	2,9	4,3	2,2	3,0	6,0	4,6	3,7	3,5	5,0
1967	3,1	6,0	1,2	2,4	3,2	3,9	2,8	1,0	4,2	3,0	2,7	2,9	5,8
1968	2,7	7,2	2,0	1,7	4,2	4,4	1,7	5,1	4,2	4,1	3,2	5,0	5,2
1969	4,0	6,8	4,2	3,4	6,6	8,9	4,1	5,5	6,4	5,4	5,1	5,1	4,8
1970	4,6	8,1	7,5	3,9	5,6	8,9	6,9	11,1	5,6	7,3	6,7	5,3	7,3
1961-70	3,4	6,4	3,6	3,1	4,4	5,4	4,5	3,8	5,2	4,2	4,2	3,0	5,3
1971	5,6	7,9	7,6	3,2	5,8	10,6	7,2	−0,7	8,5	9,4	7,4	5,3	5,2
1972	6,2	9,0	5,4	5,0	6,2	13,5	6,3	5,0	9,4	8,3	6,7	4,4	5,2
1973	7,2	10,5	6,6	19,4	7,8	15,3	11,6	10,5	8,4	7,1	8,4	5,5	11,9
1974	12,6	12,8	6,6	20,9	11,1	6,1	18,5	17,8	9,3	14,9	12,3	9,0	20,6
1975	12,1	12,8	5,9	12,3	13,4	22,3	17,5	−1,1	11,2	27,2	14,9	9,2	7,8
1976	7,6	9,0	3,5	15,4	9,9	20,3	18,0	12,7	8,9	14,9	10,8	5,9	6,4
1977	7,4	8,7	3,6	13,0	9,0	12,9	19,1	1,7	6,3	13,9	10,3	5,7	5,7
1978	4,3	9,5	4,2	12,9	9,5	10,5	13,9	5,3	5,4	11,1	8,9	7,4	4,6
1979	4,6	7,6	4,1	18,6	10,4	13,2	15,9	5,8	3,9	14,5	10,2	8,5	2,6
1980	3,9	8,2	4,3	17,7	12,2	14,2	20,6	7,8	5,7	19,8	12,6	9,6	2,8
1971-80	7,1	9,6	5,2	13,7	9,5	13,8	14,8	6,3	7,7	14,0	10,2	7,0	7,2
1981	5,3	10,1	4,1	19,3	12,1	17,1	18,3	7,9	5,5	11,7	10,6	8,9	2,7
1982	7,1	11,3	4,6	24,6	12,5	15,2	17,9	8,5	6,0	7,1	10,1	6,9	1,7
1983	5,9	8,1	3,2	19,8	9,8	10,6	15,0	8,8	1,6	5,1	7,8	4,5	0,7
1984	5,3	5,8	1,9	19,9	7,0	6,6	10,7	5,8	2,6	4,4	5,8	3,8	0,6
1985	4,7	3,9	2,1	17,1	5,7	6,1	8,1	4,3	2,3	5,5	5,1	3,8	1,3
1986	4,4	2,2	1,9	15,7	3,9	5,0	6,6	5,0	1,0	4,8	4,1	4,2	1,3

Table 18

Price deflator private consumption

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	2,7	3,5	3,6	1,1	3,3	2,6	1,7	0,5	2,4	2,9	2,9	1,1	5,6
1962	1,1	6,2	3,2	1,3	4,4	4,0	5,3	0,9	2,6	3,7	3,8	1,7	6,1
1963	3,7	5,6	3,1	3,4	5,7	2,5	7,0	2,9	3,8	1,7	4,0	1,6	6,9
1964	4,2	4,0	2,3	2,2	3,4	6,9	4,9	3,1	6,8	3,6	3,7	1,4	4,4
1965	4,6	6,1	3,4	4,6	2,6	4,8	3,6	3,2	4,0	4,9	3,8	1,7	6,8
1966	4,1	6,5	3,5	3,5	3,2	3,8	2,9	3,5	5,4	4,0	3,6	2,8	4,8
1967	2,5	6,8	1,6	1,9	3,0	3,1	3,2	2,3	3,0	2,6	2,6	2,4	4,8
1968	2,9	7,7	1,7	0,7	5,0	5,2	1,5	2,5	2,6	4,6	3,2	4,1	5,5
1969	2,8	4,7	2,5	3,0	7,1	7,4	2,9	1,8	6,1	5,5	4,4	4,5	4,7
1970	2,5	7,1	3,9	3,1	5,0	8,1	5,0	4,0	4,4	5,9	4,8	4,5	7,6
1961-70	3,1	5,8	2,9	2,5	4,3	4,8	3,8	2,5	4,1	3,9	3,7	2,6	5,7
1971	5,3	8,2	5,9	2,9	5,5	9,4	5,5	4,7	8,3	8,6	6,5	4,6	6,5
1972	5,4	8,2	5,6	3,3	5,8	9,7	6,4	5,2	8,8	6,6	6,2	3,8	5,4
1973	6,1	10,8	7,1	15,0	6,8	11,6	12,5	5,0	9,3	8,3	8,6	5,9	10,6
1974	12,7	14,5	7,6	23,5	13,5	15,7	20,9	9,9	10,1	17,1	14,1	10,1	21,8
1975	12,3	10,0	6,0	12,7	11,3	22,3	17,7	10,2	10,7	23,7	13,8	7,7	11,6
1976	7,8	9,8	4,2	13,4	9,8	18,8	18,1	9,5	8,8	15,7	11,0	5,4	8,9
1977	7,1	9,6	3,7	11,9	9,0	13,3	18,2	5,8	6,0	14,9	10,3	5,9	7,1
1978	4,1	9,0	2,9	12,8	8,7	7,8	12,9	3,5	4,5	9,0	7,7	6,9	4,6
1979	4,0	10,4	4,2	16,4	10,4	14,4	15,1	5,8	4,3	13,6	9,9	9,0	3,5
1980	6,6	10,7	5,5	21,4	13,2	17,0	20,2	7,7	6,9	16,4	12,8	10,3	6,8
1971-80	7,1	10,1	5,3	13,2	9,4	13,9	14,6	6,7	7,8	13,3	10,1	6,9	8,6
1981	8,5	12,0	6,0	23,3	12,8	19,5	19,2	7,7	6,3	11,2	11,7	9,0	4,8
1982	7,5	11,0	4,8	20,9	11,2	16,0	17,0	10,0	5,3	8,3	9,8	5,9	2,7
1983	7,0	7,2	2,9	19,5	9,4	9,7	14,9	8,2	2,8	5,1	7,6	3,8	1,5
1984	6,2	6,6	2,5	18,1	7,3	8,5	11,1	6,7	2,6	5,1	6,2	3,2	2,1
1985	4,9	4,2	2,1	18,0	5,8	5,7	8,6	3,8	2,3	5,3	5,2	3,2	1,8
1986	3,2	1,7	1,5	16,0	4,0	5,3	6,5	3,4	1,1	4,3	3,9	4,4	2,2

Table 19

Price deflator of exports of goods and services

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	0,6	−1,2	0,2	0,2	0,3	−0,1	−0,8	−3,1	−1,7	1,3	0,2	1,1	−2,1
1962	1,0	2,5	0,5	1,1	1,2	1,5	0,8	−1,7	−0,1	0,8	1,0	−0,3	−1,3
1963	2,1	2,8	0,9	8,0	2,8	2,0	3,3	−0,0	2,6	0,9	2,2	0,1	2,2
1964	4,2	3,4	2,6	0,9	4,4	4,9	4,1	2,3	2,5	2,2	2,9	0,5	2,0
1965	1,4	2,2	2,5	−1,1	1,1	1,8	−0,0	1,4	2,3	2,4	1,6	3,4	0,5
1966	3,7	3,0	2,5	3,9	2,0	1,8	0,2	0,7	0,7	3,0	1,8	2,9	1,2
1967	0,5	1,7	0,3	−2,7	−0,4	0,7	1,1	0,3	−0,0	2,4	0,7	1,8	1,2
1968	0,2	2,6	−0,1	−1,3	−0,4	6,5	0,3	1,2	−0,5	8,4	1,9	2,2	0,8
1969	4,6	7,2	4,2	0,5	4,8	6,1	2,7	6,7	2,2	2,5	3,6	3,1	2,5
1970	5,7	7,0	4,4	3,1	7,8	6,8	6,1	12,8	5,1	8,8	6,6	5,1	3,5
1961-70	2,4	3,1	1,8	1,2	2,3	3,2	1,8	2,0	1,3	3,2	2,2	2,0	1,0
1971	2,1	4,0	4,2	1,7	4,8	7,3	4,3	−2,9	3,1	5,0	4,1	4,3	2,1
1972	1,7	6,8	2,1	5,7	0,7	11,5	2,8	1,2	1,3	4,3	2,4	3,0	−1,7
1973	8,3	12,2	6,4	26,1	7,4	19,7	15,2	15,5	6,9	12,6	10,0	13,0	7,7
1974	24,5	19,4	15,1	31,6	22,7	23,0	34,9	23,8	25,8	25,1	24,0	22,1	31,8
1975	5,5	7,7	4,3	12,9	4,7	18,8	11,3	−1,5	5,0	20,4	9,5	10,9	−0,0
1976	5,8	6,9	3,4	10,0	7,8	23,0	20,4	7,7	6,6	19,7	11,2	3,6	−0,2
1977	3,7	5,9	1,8	9,9	9,0	14,8	19,2	−1,2	3,6	15,6	9,7	4,1	−4,1
1978	1,1	5,4	1,7	8,2	6,3	6,6	8,2	2,0	−1,3	7,5	5,0	6,9	−6,5
1979	9,1	8,2	4,4	14,5	10,0	9,4	15,6	8,7	8,3	11,3	10,1	13,4	8,4
1980	9,3	14,6	6,4	34,2	12,4	10,7	18,2	5,7	12,3	14,6	13,1	10,9	8,2
1971-80	6,9	9,0	4,9	15,0	8,4	14,3	14,7	5,6	6,9	13,4	9,8	9,1	4,1
1981	9,5	12,7	6,0	21,1	13,6	16,6	21,1	1,7	14,0	9,5	12,7	8,4	0,7
1982	13,1	10,6	4,2	22,4	14,1	10,8	15,1	15,5	3,9	6,4	9,9	1,3	2,5
1983	7,4	6,9	1,4	16,7	8,8	8,5	8,0	5,1	−0,4	8,1	6,3	1,4	−6,8
1984	7,0	7,8	3,4	21,5	9,2	7,6	10,0	7,7	6,1	7,3	7,5	3,3	−2,6
1985	3,0	3,0	2,9	16,8	4,3	5,9	8,3	3,6	2,5	5,0	4,9	0,2	1,1
1986	0,0	0,0	−0,7	14,3	1,6	3,5	4,4	0,2	−3,3	−0,2	0,9	7,8	6,0

Table 20

Price deflator of imports of goods and services

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	2,6	0,1	−2,6	−1,7	0,1	0,9	−2,2	1,1	−1,9	0,0	−0,7	−0,9	0,6
1962	0,8	−0,1	−0,3	−0,7	2,8	0,5	0,4	0,7	−0,9	−0,2	0,4	−2,1	−2,6
1963	4,0	1,9	2,4	3,0	1,1	1,8	1,5	1,0	1,4	2,4	2,2	1,4	3,1
1964	3,2	1,3	1,8	3,0	0,9	1,3	3,4	1,9	2,4	2,6	2,5	2,1	1,3
1965	0,2	1,6	2,8	0,3	1,4	2,5	0,6	1,5	0,5	1,5	1,2	1,0	−2,1
1966	3,2	1,6	1,8	3,3	3,2	0,2	1,9	1,3	0,7	1,6	1,5	2,1	2,1
1967	0,5	1,7	−1,5	−3,0	−1,3	−0,3	0,7	−0,9	−0,9	1,2	−0,5	0,5	−1,5
1968	0,6	5,0	0,5	0,2	−1,1	7,9	0,7	−0,0	−2,9	11,3	2,7	1,3	2,0
1969	3,2	3,4	2,4	0,0	4,9	4,2	1,4	3,0	3,3	2,8	2,6	2,4	3,8
1970	5,1	6,5	−0,4	4,0	9,7	6,9	3,7	11,0	6,5	7,1	4,9	6,6	2,9
1961-70	2,3	2,3	0,7	0,8	2,1	2,6	1,2	1,9	0,8	3,0	1,6	1,4	0,9
1971	3,4	5,8	1,6	2,9	3,7	5,4	5,3	4,9	4,5	3,9	3,6	5,4	−0,8
1972	0,4	2,5	1,7	7,7	−1,8	5,7	3,9	0,2	−0,5	2,8	1,3	7,3	−4,1
1973	7,5	14,4	8,3	21,9	6,8	13,9	26,1	9,7	7,6	23,3	14,3	17,5	18,9
1974	27,5	32,4	24,0	41,6	42,0	44,4	56,2	21,7	32,7	41,9	37,9	44,1	62,8
1975	6,7	4,4	1,9	17,4	−0,2	20,5	6,4	10,5	4,3	13,7	5,6	9,6	8,6
1976	6,3	7,2	5,5	11,2	8,6	19,0	24,1	5,6	6,5	21,8	12,6	2,8	5,4
1977	3,1	7,6	2,0	5,8	10,7	16,8	17,1	2,3	3,3	14,1	9,1	10,5	−4,7
1978	1,1	2,3	−1,7	9,7	1,2	4,7	4,7	0,7	−1,6	3,0	1,7	4,6	−15,9
1979	8,9	13,7	8,4	17,7	10,3	13,5	17,4	6,6	10,9	8,6	11,4	17,2	27,5
1980	13,6	21,7	12,6	34,1	16,8	18,2	21,9	9,0	14,5	9,9	1,62	20,0	36,1
1971-80	7,6	10,8	6,2	16,4	9,2	15,7	17,4	7,0	7,8	13,8	10,9	13,4	11,4
1981	13,8	17,7	10,2	15,3	15,9	17,9	27,6	4,0	14,3	8,1	15,5	0,9	1,1
1982	13,0	11,0	2,2	26,1	9,6	7,5	10,9	15,3	1,3	7,5	7,8	−6,3	2,8
1983	7,2	4,9	−0,7	21,6	6,3	4,8	4,8	5,4	0,7	8,3	4,9	−4,5	−5,3
1984	7,6	8,0	4,7	22,9	9,7	9,4	10,7	8,2	5,6	8,9	8,3	−2,6	−3,7
1985	3,0	3,0	2,9	18,2	4,5	5,7	9,2	2,6	2,0	4,7	4,9	−5,5	−3,0
1986	−1,4	−0,6	−1,7	13,4	0,7	3,1	1,8	−1,4	−3,8	−1,6	−0,4	5,6	3,0

Table 21

Terms of trade, goods and services; including intra-Community trade

(1980 = 100)

	B	DK	D	GR	F	IRL	I	L	NL	UK	US	JA
1960	106,0	109,2	101,1	108,8	105,7	106,5	120,1	113,1	103,8	100,4	139,5	194,4
1961	103,9	107,8	104,0	110,9	105,9	105,5	121,8	108,4	104,1	101,7	142,3	189,2
1962	104,1	110,5	104,9	112,9	104,2	106,6	122,4	105,7	104,9	102,7	145,0	191,8
1963	102,2	111,5	103,3	118,4	105,9	106,8	124,5	104,7	106,1	101,2	143,1	190,0
1964	103,2	113,8	104,1	116,0	109,6	110,6	125,3	106,0	106,2	100,9	140,8	191,4
1965	104,4	114,5	103,8	114,4	109,2	109,8	124,5	105,9	108,0	101,7	144,1	196,5
1966	105,0	116,0	104,5	115,0	107,9	111,6	122,5	105,2	108,0	103,1	145,2	194,6
1967	105,0	116,0	106,4	115,4	109,0	112,7	123,0	106,4	108,9	104,3	147,0	199,8
1968	104,5	113,3	105,8	113,6	109,7	111,2	122,5	107,7	111,5	101,6	148,4	197,4
1969	106,0	117,5	107,7	114,2	109,6	113,2	124,1	111,7	110,3	101,3	149,3	195,0
1970	106,6	118,1	112,9	113,1	107,6	113,2	126,9	113,5	108,8	102,9	147,2	196,1
1971	105,3	116,0	115,8	111,7	108,7	115,2	125,7	105,0	107,4	104,1	145,8	201,7
1972	106,7	120,9	116,2	109,6	111,4	121,5	124,4	106,0	109,3	105,7	139,9	206,9
1973	107,5	118,5	114,2	113,4	112,0	127,7	113,6	111,7	108,6	96,4	134,5	187,5
1974	104,9	106,9	105,9	105,4	96,8	108,8	98,1	113,6	103,0	85,0	113,9	151,8
1975	103,8	110,2	108,5	101,3	101,6	107,2	102,7	101,3	103,6	90,0	115,3	139,8
1976	103,2	109,9	106,3	100,3	100,8	110,8	99,6	103,3	103,7	88,4	116,2	132,3
1977	103,8	108,2	106,2	104,2	99,3	108,9	101,4	99,7	104,1	89,6	109,4	133,0
1978	103,8	111,5	109,8	102,7	104,2	110,9	104,8	101,1	104,4	93,6	111,8	148,0
1979	104,0	106,2	105,9	99,9	104,0	106,8	103,1	103,1	101,9	95,9	108,2	125,8
1980	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0
1981	96,2	95,7	96,2	105,0	98,1	98,9	94,9	97,8	99,7	101,3	107,4	99,6
1982	96,3	95,3	98,1	101,9	102,1	101,9	98,4	97,9	102,3	100,2	116,2	99,3
1983	96,5	97,2	100,2	97,8	104,6	105,5	101,5	97,7	101,2	100,1	123,4	97,8
1984	96,0	97,0	98,9	96,6	104.1	103,7	100,8	97,2	101,7	98,6	130,9	98,9
1985	96,0	97,0	98,9	95,5	103,9	103,9	99,9	98,2	102,2	98,9	138,8	100,8
1986	97,4	97,6	99,9	96,2	104,9	104,3	102,5	99,7	102,7	100,3	141,7	103,8

Table 22

Compensation per employee; total economy

(national currency, annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	3,2	12,9	10,2	6,5	10,6	9,5	8,2	2,8	7,4	6,8	8,5	3,2	13,4
1962	7,2	11,1	9,1	6,9	11,6	9,3	13,5	4,8	6,8	4,7	8,7	4,4	14,0
1963	8,0	4,6	6,1	7,5	11,4	6,1	19,7	8,1	9,3	5,0	9,1	4,0	14,2
1964	9,7	10,7	8,2	13,1	9,2	14,2	12,3	13,3	16,5	7,1	9,4	5,1	11,9
1965	9,5	13,8	9,5	12,6	6,5	3,2	7,7	4,2	11,7	6,8	8,0	3,7	11,5
1966	8,6	10,2	7,6	12,7	6,0	8,5	7,9	5,0	11,1	6,4	7,3	5,1	9,9
1967	7,4	10,9	3,3	9,2	6,9	8,0	8,4	2,8	9,3	6,2	6,2	4,3	12,2
1968	6,3	9,6	6,7	9,6	11,2	10,6	7,4	5,9	8,6	7,8	8,1	7,4	15,0
1969	8,4	11,4	9,5	10,2	11,1	13,9	7,6	5,6	13,2	7,1	9,1	7,4	14,1
1970	9,4	11,0	16,0	9,6	9,8	16,8	15,7	14,8	12,6	13,0	13,4	7,6	18,1
1961-70	7,8	10,6	8,6	9,8	9,4	9,9	10,8	6,7	10,6	7,1	8,8	5,2	13,4
1971	11,7	11,7	12,6	9,2	11,5	14,0	13,1	9,3	13,4	11,4	12,1	7,2	15,1
1972	14,0	7,9	9,1	12,4	10,3	16,9	11,1	8,8	12,9	13,2	11,0	7,4	14,2
1973	13,0	13,1	12,1	17,6	12,8	19,8	19,6	12,8	15,1	13,2	14,2	7,0	21,3
1974	18,2	18,4	11,5	18,7	17,6	18,6	22,1	21,3	15,8	18,9	17,2	8,1	25,7
1975	16,5	14,0	7,2	19,7	18,6	26,8	21,0	11,3	13,3	31,3	18,2	9,2	16,1
1976	16,0	11,7	7,9	23,9	14,7	19,8	20,9	13,2	10,9	14,9	14,1	8,0	11,3
1977	8,7	9,7	6,6	22,3	12,6	13,8	21,4	9,4	8,1	10,6	11,8	7,5	10,0
1978	7,5	9,2	5,6	23,1	12,5	15,3	16,2	5,6	7,2	13,5	11,2	7,6	7,0
1979	5,6	9,4	5,9	22,0	13,3	19,2	17,9	6,0	6,0	14,9	11,9	8,5	6,0
1980	8,7	10,0	6,8	14,4	14,9	21,5	22,5	7,8	5,4	19,1	14,3	9,9	6,4
1971-80	11,9	11,5	8,5	18,2	13,9	18,5	18,5	10,5	10,7	16,0	13,6	8,0	13,2
1981	7,6	9,2	5,2	24,8	14,2	17,0	21,9	7,8	3,6	13,5	12,6	9,5	6,5
1982	7,9	11,5	4,3	27,2	14,1	14,4	17,0	6,9	5,6	8,8	10,6	8,0	4,4
1983	6,7	6,4	3,7	19,7	10,9	10,5	16,0	6,6	3,3	8,8	9,1	6,0	2,9
1984	6,2	4,9	3,2	21,3	8,1	9,6	12,1	4,2	0,6	5,5	6,7	5,2	4,9
1985	5,7	3,7	3,2	19,0	5,9	7,0	10,2	4,8	1,4	7,7	6,3	4,4	4,9
1986	4,2	2,4	3,8	12,6	4,5	5,7	7,6	5,7	2,5	7,1	5,4	4,2	5,4

Table 23

Real compensation per employee; total economy

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	0,6	9,0	6,4	5,4	7,0	6,7	6,4	2,3	4,9	3,7	5,4	2,1	7,4
1962	6,1	4,7	5,7	5,5	7,0	5,1	7,8	3,9	4,1	0,9	4,7	2,7	7,4
1963	4,2	−0,9	2,9	4,0	5,4	3,5	11,8	5,0	5,3	3,2	4,9	2,4	6,8
1964	5,3	6,4	5,8	10,7	5,6	6,8	7,1	9,9	9,1	3,3	5,5	3,6	7,2
1965	4,7	7,3	5,9	7,7	3,9	−1,5	4,0	0,9	7,4	1,8	4,1	1,9	4,4
1966	4,3	3,4	4,0	8,9	2,8	4,6	4,8	1,5	5,4	2,3	3,5	2,2	4,8
1967	4,7	3,9	1,7	7,2	3,7	4,7	5,1	0,5	6,1	3,5	3,5	1,9	7,0
1968	3,3	1,8	5,0	8,8	5,9	5,1	5,8	3,3	5,9	3,1	4,8	3,2	9,0
1969	5,4	6,3	6,9	6,9	3,8	6,1	4,5	3,7	6,7	1,6	4,5	2,7	8,9
1970	6,7	3,6	11,6	6,3	4,5	8,1	10,1	10,5	7,9	6,7	8,2	3,0	9,7
1961-70	4,5	4,5	5,6	7,1	4,9	4,9	6,7	4,1	6,3	3,0	4,9	2,6	7,2
1971	6,0	3,2	6,3	6,1	5,7	4,2	7,2	4,4	4,7	2,5	5,3	2,5	8,1
1972	8,2	−0,3	3,2	8,8	4,3	6,6	4,4	3,5	3,8	6,2	4,5	3,5	8,4
1973	6,5	2,1	4,7	2,2	5,6	7,4	6,3	7,5	5,3	4,5	5,2	1,0	9,7
1974	4,9	3,4	3,6	−3,9	3,6	2,5	1,0	10,3	5,2	1,5	2,7	−1,9	3,2
1975	3,8	3,6	1,1	6,2	6,6	3,6	2,8	1,0	2,3	6,1	3,9	1,4	4,1
1976	7,6	1,7	3,6	9,2	4,5	0,8	2,4	3,4	1,9	−0,7	2,7	2,5	2,3
1977	1,5	0,1	2,8	9,3	3,3	0,4	2,7	3,4	2,0	−3,7	1,4	1,5	2,7
1978	3,3	0,1	2,6	9,1	3,5	7,0	2,9	2,0	2,5	4,1	3,2	0,6	2,3
1979	1,5	−0,9	1,6	4,9	2,6	4,2	2,4	0,1	1,7	1,2	1,9	−0,4	2,4
1980	2,0	−0,6	1,2	−5,7	1,5	3,8	1,9	0,1	−1,4	2,3	1,4	−0,4	−0,5
1971-80	4,5	1,2	3,1	4,5	4,1	4,0	3,4	3,5	2,8	2,4	3,2	1,0	4,2
1981	−0,9	−2,5	−0,7	1,2	1,2	−2,1	2,3	0,1	−2,6	2,0	0,8	0,4	1,6
1982	0,4	0,5	−0,5	5,1	2,6	−1,4	0,0	−2,9	0,3	0,5	0,7	1,9	1,6
1983	−0,2	−0,7	0,8	0,2	1,3	0,7	1,0	−1,4	0,4	3,6	1,4	2,1	1,4
1984	0,0	−1,6	0,7	2,8	0,7	1,0	1,0	−2,4	−1,9	0,3	0,4	1,9	2,7
1985	0,7	−0,5	1,1	0,8	0,1	1,3	1,5	1,0	−0,9	2,3	1,0	1,2	3,1
1986	1,0	0,7	2,3	−2,9	0,5	0,4	1,0	2,2	1,4	2,6	1,5	−0,2	3,2

Table 24

Adjusted share of labour income; total economy

(percent of GDP at current factor cost)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	69,2	71,4	70,5	102,8	72,6	86,5	80,8	66,4	64,2	71,6	74,3	73,6	81,9
1961	68,3	72,4	72,1	98,4	73,5	87,0	79,0	65,6	66,5	72,3	74,8	73,1	75,9
1962	69,6	73,0	72,5	98,6	73,5	88,1	78,7	68,7	67,3	72,9	74,9	72,2	78,8
1963	70,4	73,4	72,6	94,4	74,0	88,0	80,9	68,4	68,8	72,1	75,0	71,8	78,4
1964	69,9	72,6	71,4	94,3	73,9	89,2	82,4	69,1	69,3	71,9	74,8	71,9	74,8
1965	70,1	75,4	71,6	92,5	73,2	86,5	80,9	69,3	70,0	72,6	74,6	70,9	76,6
1966	71,8	76,6	72,2	93,3	72,2	89,9	79,2	69,7	72,2	73,4	74,6	70,8	73,7
1967	72,2	77,4	71,5	93,8	71,2	87,9	79,3	69,0	71,8	72,6	74,0	71,7	71,8
1968	71,3	77,9	70,0	94,7	72,1	86,4	78,1	66,4	71,4	72,1	73,3	72,4	70,6
1969	70,7	77,1	70,5	91,6	71,8	86,2	76,1	62,1	71,9	73,5	73,3	73,8	68,8
1970	68,9	78,1	72,1	88,3	70,8	88,6	78,2	64,0	73,1	75,3	74,2	75,3	69,9
1961-70	70,3	75,4	71,6	94,0	72,6	87,8	79,3	67,2	70,2	72,9	74,3	72,4	73,9
1971	70,8	79,4	73,2	85,8	70,9	88,6	80,7	70,5	74,2	73,0	74,5	74,1	73,4
1972	71,3	76,0	72,8	84,3	69,9	85,0	79,9	71,2	73,4	73,8	74,1	73,9	73,3
1973	71,5	75,2	73,6	76,7	70,1	84,5	80,4	66,4	73,3	73,2	74,2	73,7	74,4
1974	73,3	78,0	75,1	76,9	72,1	90,3	81,0	66,7	74,5	75,4	75,8	74,9	77,5
1975	75,9	79,0	75,0	79,2	74,2	88,2	84,9	83,2	76,3	77,9	77,7	73,6	81,2
1976	77,4	77,6	73,5	80,9	74,4	88,5	83,7	80,1	73,6	74,6	76,3	73,5	81.6
1977	77,8	78,0	73,2	84,5	74,6	80,8	84,8	86,6	73,8	72,8	76,1	73,0	82,1
1978	78,0	77,9	72,4	87,8	74,6	78,7	84,5	83,3	73,9	72,2	75,7	73,1	80,9
1979	77,9	78,3	71,9	88,8	74,5	82,7	82,2	80,7	74,2	73,2	75,4	73,3	81,0
1980	78,9	79,3	73,0	84,5	75,6	88,2	81,7	81,1	73,9	74,7	76,1	74,2	80,6
1971-80	75,3	77,9	73,4	82,9	73,1	85,5	82,4	77,0	74,1	74,1	75,6	73,7	78,6
1981	80,0	78,3	73,1	86,7	76,0	86,8	84,0	82,5	71,9	74,5	76,6	73,1	80,8
1982	78,9	75,4	72,1	88,3	75,9	85,7	83,5	82,8	70,5	73,9	76,0	74,6	81,6
1983	78,0	73,2	70,6	88,3	75,3	83,9	86,7	84,5	69,5	73,0	75,7	73,9	82,0
1984	77,4	71,7	69,8	87,1	74,2	82,3	86,0	81,8	66,7	73,4	75,0	72,7	81,4
1985	76,9	71,4	69,3	87,8	72,6	80,3	85,5	81,8	64,8	73,1	74,2	73,0	82,0
1986	75,7	70,2	69,2	85,4	71,3	80,1	84,3	81,5	64,9	74,2	73,8	72,5	83,3

Table 25

Relative unit labour costs; manufacturing industry (calculated in a common currency: US dollars against 19 countries)

(1972 = 100)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10	US	JA
1960	110,5	93,6	76,4	119,7	125,0	75,8	85,9	74,8	107,0	85,8	133,3	85,2
1961	106,3	94,6	81,5	122,1	124,9	75,6	82,6	80,6	111,1	90,8	129,8	82,8
1962	104,8	95,0	83,9	124,9	126,2	79,4	84,4	81,0	110,8	93,1	125,8	88,7
1963	104,7	98,1	83,0	118,7	128,0	81,8	96,7	85,0	107,6	95,9	117,5	92,1
1964	106,3	97,0	81,4	122,5	127,3	86,5	100,4	90,3	105,7	96,1	116,1	91,0
1965	109,8	99,5	81,4	123,7	124,1	82,6	94,0	94,3	110,1	97,0	110,5	97,0
1966	109,3	104,1	82,7	120,5	117,3	85,2	88,6	97,6	111,6	96,0	111,3	93,6
1967	109,5	103,2	79,7	128,6	115,0	83,8	90,4	102,6	107,4	93,1	115,2	88,4
1968	106,6	99,6	79,7	129,4	119,9	81,7	89,7	104,2	93,1	88,3	120,9	91,3
1969	103,1	103,9	81,6	129,2	113,6	88,1	91,6	100,4	95,7	88,4	124,0	90,2
1970	94,4	101,9	94,6	118,9	101,8	91,8	95,2	95,2	99,5	93,7	122,4	83,9
1971	95,9	101,5	98,0	112,4	98,4	95,3	99,0	96,4	103,0	97,6	111,4	89,1
1972	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0
1973	100,8	110,3	110,1	89,5	102,0	96,6	95,5	103,4	87,9	102,8	87,1	111,8
1974	106,0	113,1	110,0	103,9	90,0	98,9	90,3	106,9	87,2	97,6	86,1	117,2
1975	107,5	106,9	99,7	94,1	106,4	97,4	101,4	108,9	94,9	105,4	78,7	111,5
1976	109,8	110,6	99,7	102,8	104,7	91,1	88,6	106,4	85,9	97,0	81,4	108,3
1977	111,6	111,3	105,3	113,8	100,4	89,4	89,9	109,2	84,3	99,8	79,8	114,6
1978	109,4	118,6	109,4	115,4	100,6	92,4	88,0	107,0	90,5	104,3	73,8	127,5
1979	104,2	116,7	110,5	120,2	102,0	97,7	88,3	106,2	106,0	112,4	74,4	107,5
1980	102,2	101,6	107,7	119,1	106,9	109,4	87,0	100,5	129,2	120,1	76,0	90,6
1981	92,8	91,5	98,7	126,0	101,0	103,0	84,0	90,0	130,4	104,3	84,4	97,3
1982	81,0	90,6	99,6	148,9	99,3	105,1	85,1	92,0	121,4	100,5	94,2	83,0
1983	79,6	89,4	99,0	140,0	95,1	98,3	93,3	91,0	112,2	96,8	96,7	90,1
1984	80,1	87,2	95,0	146,3	91,1	89,2	90,9	84,2	108,9	88,8	107,0	90,9
1985	81,7	87,9	92,3	148,0	90,7	86,5	88,4	81,1	112,4	86,8	112,3	90,2
1986	83,4	87,5	96,4	145,0	90,9	87,6	86,4	83,1	121,4	92,3	101,4	90,5

Table 26

Exports of goods and services at current prices

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	38,4	32,2	18,8	9,1	15,0	31,8	14,1	85,1	48,1	21,1	20,5	5,1	10,8
1961	39,6	29,9	17,9	9,3	14,5	34,6	14,4	81,2	45,8	20,6	20,0	5,0	9,2
1962	41,2	28,5	17,3	9,7	13,4	32,3	14,2	78,0	45,2	20,2	19,4	4,9	9,5
1963	42,4	30,3	17,7	10,0	13,1	33,6	13,7	74,9	45,2	20,1	19,4	4,9	9,0
1964	43,2	29,7	17,9	9,2	13,2	33,4	14,4	76,8	43,8	19,5	19,4	5,2	9,4
1965	42,6	29,2	17,9	9,0	13,8	34,8	16,1	78,6	43,2	19,4	19,7	5,1	10,5
1966	44,3	28,4	19,0	11,3	13,8	37,2	16,5	75,3	42,0	19,5	20,1	5,1	10,6
1967	43,4	27,2	20,3	10,7	13,7	37,8	16,3	75,1	40,8	19,2	20,2	5,2	9,7
1968	45,5	27,5	21,2	9,6	13,7	38,8	17,1	76,9	41,3	21,5	21,2	5,2	10,1
1969	49,5	27,4	21,6	9,7	14,6	37,3	17,8	81,2	42,8	22,5	22,0	5,2	10,5
1970	51,9	27,9	21,0	10,0	16,3	37,0	17,8	86,9	44,9	23,4	22,7	5,7	10,8
1961-70	44,4	28,6	19,2	9,8	14,0	35,7	15,8	78,5	43,5	20,6	20,4	5,2	9,9
1971	50,6	27,6	20,9	10,3	17,1	36,1	18,2	84,2	45,4	23,3	22,8	5,5	11,7
1972	51,1	27,1	20,8	11,7	17,2	34,6	18,9	79,5	45,0	22,1	22,7	5,7	10,6
1973	55,6	28,5	22,0	14,2	18,2	38,0	18,8	85,9	47,2	24,0	24,0	6,9	10,0
1974	61,3	31,8	26,0	16,1	21,5	42,6	22,3	99,3	53,7	28,2	28,0	8,4	13,6
1975	53,7	30,1	24,5	16,9	19,5	42,7	22,8	88,3	49,7	26,2	26,3	8,5	12,8
1976	57,0	28,8	25,9	17,6	20,2	46,6	24,6	84,2	50,9	28,5	27,8	8,3	13,6
1977	55,9	28,8	25,7	16,8	21,3	49,9	26,3	82,4	47,6	30,4	28,4	7,9	13,2
1978	54,0	27,8	25,2	17,6	21,3	50,5	26,8	79,1	44,9	28,9	27,8	8,2	11,2
1979	59,5	29,2	25,4	17,5	21,9	50,6	27,9	85,4	49,1	28,5	28,5	9,1	11,7
1980	62,9	32,7	26,7	20,9	22,2	50,5	25,1	81,4	52,5	27,8	28,8	10,2	13,9
1971-80	56,2	29,2	24,3	16,0	20,1	44,2	23,2	85,0	48,6	26,8	26,5	7,9	12,2
1981	68,5	36,5	29,4	20,4	23,6	49,8	26,7	79,4	58,0	27,1	30,5	9,7	15,0
1982	73,7	36,2	30,9	18,2	23,1	49,5	26,5	85,6	57,6	26,7	30,7	8,6	14,9
1983	74,4	36,3	29,7	19,4	23,5	53,4	26,2	83,7	58,0	26,8	30,5	7,7	14,0
1984	78,2	36,8	31,6	21,1	25,2	60,3	27,2	92,7	63,1	28,9	32,5	7,5	15,1
1985	78,6	37,6	33,9	21,8	25,4	63,8	28,1	93,1	64,6	30,1	33,7	6,9	15,2
1986	77,4	37,4	33,9	22,6	25,2	65,9	28,5	89,0	63,2	28,6	33,4	7,4	16,3

Table 27

Exports of goods and services at constant prices

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	9,2	4,3	3,8	14,5	5,1	17,2	14,8	3,2	2,3	3,1	5,4	0,6	6,9
1962	10,1	4,9	4,9	10,0	1,8	−0,7	10,4	−1,9	6,2	1,8	4,7	5,3	16,8
1963	8,2	10,0	7,2	6,7	7,1	9,7	6,5	3,5	6,0	4,5	6,4	6,7	7,3
1964	9,4	8,5	8,4	1,7	6,7	7,9	10,8	13,4	11,3	3,8	7,6	12,1	21,0
1965	6,1	7,9	6,6	12,7	11,5	9,0	20,0	6,2	7,6	4,5	8,5	2,4	22,6
1966	7,7	3,9	10,1	34,4	6,6	10,7	11,2	−0,3	5,2	4,0	7,5	7,2	15,5
1967	4,3	3,4	7,7	5,1	7,3	10,2	7,2	2,1	6,6	1,6	5,6	4,3	5,7
1968	12,2	9,8	13,0	−1,0	9,4	8,8	13,9	10,7	12,8	12,0	12,1	7,8	23,1
1969	15,3	5,7	9,4	14,6	15,7	4,6	11,8	13,8	14,9	9,0	11,4	4,8	19,6
1970	10,2	5,2	5,3	12,4	16,1	4,4	5,8	7,8	12,3	4,9	7,9	9,5	16,8
1961-70	9,2	6,3	7,6	10,7	8,6	8,1	11,1	5,7	8,5	4,9	7,7	6,0	15,4
1971	4,5	5,1	6,3	11,9	11,0	4,1	7,0	3,4	11,0	6,7	7,5	0,9	16,9
1972	11,1	5,7	6,9	22,9	12,9	3,6	10,6	4,0	10,8	0,7	7,8	9,4	5,2
1973	14,2	7,7	10,6	23,4	11,8	10,9	3,3	14,5	12,4	11,5	10,5	19,5	7,2
1974	3,8	4,4	10,4	0,1	10,4	0,7	8,5	14,1	2,5	6,8	7,5	8,9	22,7
1975	−8,2	−1,7	−5,7	10,6	−1,5	7,2	3,8	−16,1	−3,0	−2,7	−2,7	−1,3	4,0
1976	13,6	4,2	11,2	16,4	10,6	8,1	12,4	1,7	10,1	8,6	10,7	3,9	19,2
1977	1,9	4,8	4,3	1,8	9,0	14,0	8,5	1,4	−1,8	6,1	5,3	2,1	12,3
1978	2,6	2,0	3,5	16,4	6,6	12,3	10,2	3,5	3,3	1,7	4,8	9,4	0,0
1979	7,9	8,4	4,5	6,7	6,9	6,7	9,5	9,3	7,4	3,8	6,3	8,7	4,1
1980	4,1	5,2	5,1	6,6	2,4	6,5	−4,6	−1,1	1,5	−0,3	1,5	10,1	18,6
1971-80	5,4	4,5	5,6	11,4	7,9	7,3	6,8	3,1	5,3	4,2	5,8	7,0	10,8
1981	3,3	8,2	8,4	−4,1	5,1	1,8	4,1	1,6	1,5	−1,9	3,8	−1,1	14,7
1982	3,1	2,6	4,2	−9,0	−1,7	5,5	1,6	0,2	−0,0	1,0	1,5	−8,8	1,2
1983	0,0	3,4	−1,3	9,7	3,4	10,6	4,0	−1,3	3,6	0,9	1,7	−5,2	4,8
1984	5,1	3,5	7,8	9,7	6,8	16,9	7,0	12,3	6,9	6,9	7,1	4,7	18,1
1985	4,2	5,5	8,8	5,7	3,3	8,5	6,1	2,7	4,4	8,2	6,4	−1,8	7,7
1986	4,5	4,8	6,2	5,8	3,4	7,4	6,2	1,6	4,2	1,8	4,6	6,2	6,3

Table 28

Intra-Community exports of goods at current prices

(as percent of GDP at current market prices)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10
1960	20,2	14,8	6,4	2,6	4,4	20,6	4,0	23,3	3,3	6,3
1961	20,8	13,4	6,7	2,3	4,8	23,0	4,4	23,2	3,6	6,6
1962	22,6	12,7	6,7	3,0	4,7	20,2	4,7	23,6	3,9	6,8
1963	25,1	13,4	7,4	2,7	4,8	21,4	4,4	24,5	4,2	7,1
1964	26,3	12,9	7,5	2,8	4,9	22,0	5,1	25,1	4,1	7,4
1965	27,3	12,1	7,3	2,7	5,2	20,4	5,9	24,6	4,0	7,5
1966	27,4	11,3	7,8	2,7	5,4	20,9	6,1	23,5	3,9	7,7
1967	26,3	10,3	8,4	3,3	5,1	22,8	5,8	22,9	3,7	7,6
1968	27,8	9,7	8,7	3,2	5,2	22,2	6,1	23,6	4,2	8,0
1969	32,0	9,3	9,3	3,2	6,1	20,8	6,5	24,0	4,6	8,9
1970	33,3	9,2	9,0	3,4	7,1	21,7	6,6	25,6	4,8	9,2
1961-70	26,9	11,4	7,9	2,9	5,3	21,5	5,6	24,1	4,1	7,7
1971	31,8	8,7	9,1	3,2	7,3	21,9	7,0	26,5	4,7	9,4
1972	32,9	8,7	8,7	3,6	7,6	22,6	7,5	26,2	4,7	9,5
1973	35,1	10,1	9,4	4,9	8,1	24,5	7,5	27,8	5,6	10,4
1974	36,0	10,6	10,7	5,4	9,3	28,3	8,4	31,7	6,7	11,9
1975	31,9	10,5	9,7	5,5	7,7	30,4	8,5	29,2	6,1	10,8
1976	35,2	10,1	10,7	5,7	8,2	30,6	9,8	30,8	7,4	12,0
1977	33,5	9,7	10,5	5,0	8,5	34,3	10,1	27,7	8,4	12,0
1978	32,9	10,1	10,4	5,4	8,6	34,5	10,6	26,0	8,5	11,9
1979	36,5	11,1	11,2	5,0	9,2	35,0	11,3	29,6	9,2	12,8
1980	38,1	12,9	11,6	6,2	8,8	33,6	9,7	31,5	9,1	12,7
1971-80	34,4	10,2	10,2	5,0	8,3	29,6	9,0	28,7	7,1	11,3
1981	39,0	13,2	12,0	5,1	8,5	30,6	9,3	34,5	8,5	12,5
1982	42,2	13,5	12,9	5,2	8,3	30,8	9,7	34,7	8,5	12,8
1983	43,6	13,9	12,5	6,8	8,6	33,1	9,5	35,8	8,9	13,0
1984	44,8	12,9	13,3	7,8	9,2	38,0	9,6	39,3	9,9	13,9

Table 29

Extra-Community exports of goods at current prices

(as percent of GDP at current market prices)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10
1960	13,8	11,4	10,2	3,5	7,6	3,2	6,2	14,9	11,9	9,8
1961	12,9	11,2	9,8	3,7	7,0	3,4	6,2	14,3	11,3	9,3
1962	12,1	11,0	9,0	3,4	6,1	3,5	5,8	13,2	10,8	8,6
1963	11,1	11,9	8,9	3,9	5,8	3,7	5,6	12,2	10,7	8,3
1964	11,0	11,8	9,0	3,4	5,6	3,1	5,7	11,4	10,5	8,2
1965	11,9	11,9	9,3	3,2	5,7	2,9	6,2	11,5	10,7	8,5
1966	11,7	11,7	9,8	3,8	5,6	3,9	6,3	11,5	10,8	8,6
1967	11,2	11,4	10,3	4,0	5,4	5,9	6,5	11,3	10,0	8,5
1968	11,4	11,5	10,4	3,0	5,3	6,3	6,7	10,5	10,9	8,6
1969	11,3	11,8	10,2	3,2	5,2	6,6	6,8	9,8	11,3	8,6
1970	11,5	12,1	9,9	3,1	5,8	6,4	6,7	9,9	11,2	8,7
1961-70	11,6	11,6	9,6	3,5	5,8	4,6	6,3	11,6	10,8	8,6
1971	11,1	11,5	9,9	2,8	5,7	6,0	6,6	9,1	11,1	8,6
1972	11,1	11,3	9,3	3,3	5,7	5,4	6,8	8,5	10,5	8,3
1973	12,2	11,6	10,0	4,0	6,1	7,3	6,8	9,7	11,2	8,9
1974	14,8	13,6	12,6	5,4	7,9	9,3	9,2	11,9	12,9	11,1
1975	12,5	12,6	11,9	5,5	7,7	7,3	9,5	10,6	12,5	10,5
1976	11,9	11,8	12,1	5,7	7,7	9,1	9,8	10,7	12,9	10,7
1977	12,8	12,0	12,3	5,5	8,1	9,8	10,7	10,4	14,1	11,1
1978	12,4	10,7	11,7	5,2	7,5	9,4	10,5	9,7	13,6	10,6
1979	13,0	11,3	11,3	5,1	7,9	9,4	10,6	10,1	12,5	10,5
1980	14,6	12,6	11,9	6,9	8,1	10,8	9,8	11,2	12,2	10,8
1971-80	12,6	11,9	11,3	4,9	7,2	8,4	9,0	10,2	12,3	10,1
1981	16,2	15,0	13,5	6,6	9,2	12,6	11,9	12,8	12,2	12,0
1982	17,0	14,2	13,8	6,1	8,7	12,3	11,1	12,4	12,2	11,8
1983	18,2	14,9	13,4	6,1	8,9	14,2	10,9	12,9	11,5	11,7
1984	19,9	16,7	14,5	6,6	9,6	16,6	11,3	14,2	12,4	12,6

Table 30

Imports of goods and services at current prices

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1960	39,3	33,4	16,3	16,7	12,9	37,3	14,3	72,1	46,2	22,4	19,9	4,4	10,4
1961	40,6	31,5	15,6	16,4	12,6	39,8	14,3	74,8	45,7	20,9	19,3	4,2	10,7
1962	41,4	31,6	16,0	16,9	12,4	38,9	14,6	77,4	44,8	20,3	19,2	4,3	9,3
1963	43,5	30,0	16,1	18,0	12,8	40,8	15,9	75,2	45,9	20,4	19,6	4,2	9,9
1964	43,7	31,8	16,3	19,0	13,4	41,0	14,1	76,7	45,9	21,2	19,8	4,3	9,6
1965	42,9	30,7	17,6	20,3	12,9	43,9	13,4	77,2	43,9	20,1	19,5	4,4	9,1
1966	45,2	30,0	17,3	18,8	13,6	43,2	14,4	72,8	43,4	19,6	19,6	4,8	9,0
1967	43,1	29,2	16,6	18,0	13,4	40,9	15,0	66,9	41,7	20,1	19,4	4,8	9,4
1968	45,3	28,9	17,6	18,4	13,8	45,2	14,7	66,8	41,3	22,2	20,2	5,2	9,0
1969	48,6	29,6	18,8	18,7	15,2	46,3	16,1	66,5	43,0	21,9	21,2	5,2	9,0
1970	49,4	30,9	19,0	18,4	15,8	45,0	17,2	74,5	46,6	22,4	22,0	5,5	9,5
1961-70	44,4	30,4	17,1	18,3	13,6	42,5	15,0	72,9	44,2	20,9	20,0	4,7	9,5
1971	48,4	29,4	19,1	18,4	16,1	43,4	17,1	81,8	45,7	21,8	21,8	5,7	9,0
1972	47,6	26,5	18,8	20,0	16,3	39,9	18,0	74,9	42,2	22,1	21,7	6,1	8,3
1973	53,4	30,4	19,1	25,2	17,6	44,8	20,9	74,3	44,0	26,3	24,0	6,8	10,0
1974	60,7	34,7	21,7	25,6	23,0	57,2	26,8	79,6	51,0	33,2	29,2	8,8	14,4
1975	53,3	31,0	21,9	26,9	18,8	48,8	22,7	85,3	46,4	27,8	25,8	7,8	12,8
1976	56,7	33,5	23,6	25,8	21,3	54,6	25,9	79,9	47,5	29,5	28,0	8,6	12,8
1977	56,7	32,5	23,4	25,2	21,6	59,1	25,0	80,3	46,3	29,5	27,7	9,3	11,5
1978	54,9	29,9	22,7	24,6	20,3	60,5	24,2	79,8	44,9	27,4	26,5	9,6	9,5
1979	61,2	32,1	24,8	25,3	21,8	67,3	26,5	83,4	49,6	28,1	28,5	10,3	12,6
1980	65,7	33,8	27,2	26,4	24,0	64,3	28,0	84,4	53,0	25,2	29,7	11,0	14,9
1971-80	55,9	31,4	22,2	24,4	20,1	54,0	23,5	80,4	47,1	27,1	26,3	8,4	11,6
1981	70,8	35,8	28,5	26,5	25,2	64,4	28,6	84,4	54,5	23,8	30,4	10,4	14,2
1982	74,7	35,7	28,4	28,2	25,5	57,1	27,6	89,8	53,4	24,4	30,4	9,5	14,1
1983	73,1	34,2	27,6	29,3	24,1	55,9	25,6	87,5	54,1	25,6	29,7	9,4	12,1
1984	76,8	35,8	29,2	29,4	24,8	60,1	27,4	93,3	58,0	28,7	31,7	10,4	12,3
1985	76,4	36,7	30,4	30,8	25,0	61,0	29,1	93,1	59,0	28,8	32,4	10,2	11,7
1986	73,6	36,1	30,5	30,6	24,7	61,5	28,7	88,1	57,5	27,7	31,9	10,8	12,0

Table 31

Imports of goods and services at constant prices

(national currency; annual percentage change)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 10	US	JA
1961	7,2	4,5	7,8	12,7	6,9	13,9	13,7	7,4	6,4	−0,7	5,8	0,2	27,2
1962	8,2	13,4	12,0	10,1	6,7	5,4	14,9	3,2	6,5	2,1	8,0	12,2	−0,7
1963	8,6	−1,1	4,0	15,4	14,1	10,8	22,5	3,6	9,8	4,1	8,9	2,9	18,0
1964	8,9	19,6	9,3	15,2	15,1	12,9	−6,1	14,4	14,9	10,3	8,7	5,5	14,1
1965	6,6	6,9	14,5	21,2	2,2	11,1	2,0	4,3	6,1	0,8	5,8	11,1	7,1
1966	9,9	5,4	2,6	−0,5	10,6	3,5	14,0	−2,5	7,0	2,1	6,1	15,3	12,4
1967	1,6	5,3	−1,2	7,1	8,3	3,8	13,5	−4,8	6,3	7,4	5,7	7,0	24,5
1968	11,7	4,9	13,5	10,3	12,9	15,6	5,9	9,3	13,0	7,3	10,2	15,4	10,8
1969	15,5	12,6	16,8	15,5	19,5	13,5	19,3	11,3	14,1	2,6	13,6	5,9	12,8
1970	7,6	8,4	14,6	6,2	6,3	2,3	16,0	14,6	14,5	4,7	10,4	3,8	21,9
1961-70	8,5	7,8	9,3	11,2	10,2	9,2	11,3	5,9	9,8	4,0	8,3	7,8	14,5
1971	3,6	−0,5	10,2	7,6	9,1	4,7	2,6	8,4	6,1	5,3	6,3	6,4	4,7
1972	9,6	0,9	6,3	15,4	16,0	5,1	11,0	1,9	5,2	9,3	9,1	11,1	9,9
1973	18,5	15,1	4,2	32,2	15,2	19,0	10,3	10,9	10,9	11,8	11,3	4,7	23,9
1974	4,4	−3,5	−1,6	−16,3	5,2	−2,3	1,2	7,4	−1,1	0,9	0,6	−3,1	5,1
1975	−9,0	−4,3	3,3	6,3	−6,6	−10,2	−9,7	−9,9	−4,1	−7,1	−4,8	−12,3	−9,5
1976	13,3	17,0	11,5	6,1	20,3	14,7	14,7	2,0	10,3	4,1	12,0	20,1	6,5
1977	4,5	0,2	3,7	8,0	2,9	13,3	−0,0	0,5	2,9	0,9	2,5	8,6	5,0
1978	2,9	0,6	6,2	7,2	5,4	15,7	8,1	8,5	6,3	3,7	5,7	11,1	7,3
1979	9,3	5,0	9,3	7,2	11,1	14,1	13,5	8,0	6,0	10,4	10,1	1,6	13,1
1980	1,5	−6,8	3,6	−6,6	6,9	−4,7	8,4	1,8	−0,4	−4,3	2,3	−3,2	−6,8
1971-80	5,6	2,1	5,6	6,0	8,3	6,5	5,8	3,8	4,1	3,3	5,4	4,1	5,5
1981	−1,4	−1,7	−0,8	3,4	1,8	2,3	−5,1	1,8	−5,9	−3,5	−2,0	6,1	1,5
1982	1,1	2,9	1,0	5,1	5,8	−3,1	2,1	−0,9	1,1	4,0	2,6	1,6	1,1
1983	−2,9	0,7	1,8	2,6	−1,5	3,9	0,8	−1,9	3,3	5,4	1,4	11,1	−6,2
1984	4,6	6,5	5,6	0,7	2,3	9,5	9,6	7,6	5,9	9,4	6,3	26,6	12,5
1985	3,0	5,8	5,5	5,7	3,0	4,3	8,0	3,1	4,3	4,6	5,0	9,6	4,1
1986	3,8	4,2	7,6	2,0	4,0	5,0	6,1	2,1	4,4	4,7	5,3	6,9	5,0

Table 32

Intra-Community imports of goods at current prices

(as percent of GDP at current market prices)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10
1960	20,0	17,1	5,6	9,4	3,7	24,0	4,7	23,2	3,8	6,3
1961	21,3	16,3	5,6	9,5	4,0	26,7	4,9	25,8	3,8	6,5
1962	22,0	15,9	5,9	10,1	4,3	26,4	5,4	25,4	3,8	6,8
1963	23,6	14,5	6,0	9,4	4,9	28,1	6,2	26,8	3,8	7,1
1964	24,5	15,3	6,3	9,7	5,2	27,9	5,3	27,1	4,2	7,4
1965	24,8	14,5	7,4	10,4	5,1	27,8	4,7	26,0	4,1	7,6
1966	26,5	13,8	7,2	10,2	5,6	26,2	5,2	25,7	4,2	7,8
1967	24,5	12,8	6,9	9,6	5,7	25,2	5,7	24,2	4,5	7,7
1968	25,5	12,3	7,4	9,9	6,1	28,3	5,5	23,8	4,9	8,1
1969	28,2	12,9	8,4	9,5	7,3	29,2	6,3	23,8	4,7	9,0
1970	28,9	13,4	8,3	10,0	7,5	29,6	7,0	25,6	4,9	9,3
1961-70	25,0	14,2	6,9	9,9	5,6	27,5	5,6	25,4	4,3	7,7
1971	30,6	11,7	8,8	9,6	7,4	27,3	6,8	24,0	5,1	9,4
1972	30,2	10,7	8,5	10,2	7,7	26,1	7,5	22,6	5,5	9,5
1973	33,1	12,5	8,4	10,6	8,2	30,3	8,9	23,6	7,1	10,4
1974	35,8	14,3	8,9	10,1	10,0	37,3	10,3	25,7	8,4	11,9
1975	32,3	12,7	9,1	10,9	7,9	31,2	8,8	23,1	7,4	10,7
1976	34,8	14,1	9,7	10,7	9,2	35,2	10,3	23,4	8,0	11,8
1977	34,1	13,6	9,8	11,1	9,1	37,4	9,7	22,5	9,7	12,0
1978	34,2	12,8	9,7	10,7	8,9	39,0	9,8	22,2	9,3	11,8
1979	34,5	14,3	10,5	10,9	9,7	44,3	10,7	24,2	10,1	12,6
1980	35,7	14,5	11,0	10,6	10,0	43,9	11,2	24,3	8,6	12,5
1971-80	33,5	13,1	9,4	10,5	8,8	35,2	9,4	23,6	7,9	11,2
1981	36,8	14,8	11,5	12,1	10,1	44,3	10,5	24,4	8,2	12,5
1982	40,3	14,9	11,5	12,2	10,8	38,6	10,3	24,5	8,8	12,7
1983	42,9	14,2	11,8	13,4	10,7	36,7	9,7	24,8	9,6	12,9
1984	44,5	14,5	12,4	13,6	11,3	38,8	10,5	26,7	10,6	13,7

Table 33

Extra-Community imports of goods at current prices

(as percent of GDP at current market prices)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10
1960	15,9	14,9	9,2	11,7	7,3	12,6	8,7	20,2	14,8	11,1
1961	15,0	14,0	8,6	9,7	6,9	13,0	8,6	19,2	13,3	10,3
1962	14,9	14,8	8,7	7,8	6,7	12,1	8,5	18,1	12,9	10,0
1963	14,9	14,2	8,6	8,9	6,5	12,3	9,0	18,0	13,0	10,0
1964	15,3	15,7	8,5	8,3	6,7	12,5	8,0	17,9	14,1	10,2
1965	14,6	15,1	8,9	9,8	6,2	12,7	7,9	16,6	13,1	9,9
1966	14,8	14,8	8,6	9,4	6,4	12,5	8,3	16,4	12,4	9,7
1967	13,9	14,6	8,0	7,9	5,8	12,4	8,3	15,4	12,4	9,3
1968	14,8	14,1	8,1	8,4	5,4	12,6	7,5	14,7	13,7	9,3
1969	15,0	14,3	8,4	8,8	5,7	12,6	7,9	13,8	13,4	9,4
1970	15,2	15,0	8,2	10,1	6,3	11,6	8,2	15,3	13,1	9,6
1961-70	14,8	14,7	8,5	8,9	6,3	12,4	8,2	16,6	13,1	9,8
1971	13,0	14,0	7,9	9,3	6,0	12,2	7,6	15,2	11,9	9,0
1972	12,1	12,6	7,1	8,4	6,0	10,8	7,5	13,5	11,9	8,5
1973	13,6	14,7	7,4	10,6	6,5	11,3	9,1	14,9	14,4	9,6
1974	18,2	17,0	9,3	13,3	9,9	16,5	13,8	18,9	18,8	12,9
1975	15,6	14,9	8,9	14,7	8,1	13,3	11,3	17,3	14,9	11,1
1976	16,5	15,7	10,1	16,2	9,2	14,8	13,1	18,7	16,1	12,4
1977	16,2	14,9	9,8	15,0	9,2	16,6	12,6	18,2	15,0	12,0
1978	15,2	12,9	9,3	14,1	8,3	15,9	11,8	16,3	15,1	11,2
1979	19,0	14,1	10,4	14,1	8,8	16,9	13,2	18,4	14,5	12,2
1980	23,2	15,0	12,0	16,0	10,5	14,7	14,0	21,0	13,7	13,4
1971-80	16,3	14,6	9,2	13,2	8,2	14,3	11,4	17,2	14,6	11,2
1981	25,3	16,1	12,4	12,1	10,9	14,7	15,3	22,2	12,6	13,7
1982	25,7	15,6	12,0	14,1	10,4	13,4	14,3	20,9	12,7	13,3
1983	23,8	15,0	11,6	14,5	9,5	14,0	13,0	21,7	12,7	12,7
1984	25.2	16,1	12,4	15,3	9,7	16,3	13,7	24,9	14,4	13,7

Table 34

Current account of balance of payments

(as percent of GDP at current market prices)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10	US	JA
1960	0,7	−1,6	1,6	−2,9	1,5	−0,1	0,8	3,0	−1,0	0,7	0,6	0,3
1961	0,3	−2,0	1,0	−2,2	1,1	0,2	1,2	1,4	0,0	0,7	0,7	1,8
1962	0,7	−3,4	−0,1	−1,6	1,0	−1,8	0,6	1,0	0,4	0,4	0,6	−0,1
1963	−0,4	0,1	0,2	−2,2	0,3	−2,8	−1,4	0,7	0,3	−0,0	0,7	1,1
1964	0,2	−2,4	0,2	−4,3	−0,3	−3,5	1,1	−1,1	−1,3	−0,3	1,1	−0,6
1965	0,6	−1,8	−1,3	−5,8	0,8	−4,4	3,6	0,1	−0,2	0,2	0,8	1,1
1966	−0,1	−1,9	0,2	−2,0	0,1	−1,6	3,2	−1,0	0,1	0,4	0,4	1,3
1967	1,2	−2,4	2,2	−2,2	0,0	1,4	2,2	−0,3	−0,9	0,7	0,3	−0,1
1968	1,4	−1,7	2,3	−3,6	−0,5	−1,3	3,3	0,3	−0,8	0,8	0,1	0,8
1969	1,8	−2,8	1,4	−4,0	−1,1	−4,8	2,7	0,3	0,7	0,6	0,0	1,3
1970	3,2	−3,9	0,6	−3,1	0,1	−4,0	1,2	−1,4	1,3	0,5	0,2	1,0
1961-70	0,9	−2,2	0,7	−3,1	0,2	−2,3	1,8	0,0	−0,0	0,4	0,5	0,8
1971	2,3	−2,4	0,4	−1,5	0,6	−3,8	1,8	−0,3	1,8	0,8	−0,1	2,5
1972	3,9	−0,3	0,4	−1,2	0,5	−2,2	1,6	2,8	0,2	0,8	−0,5	2,2
1973	2,8	−1,7	1,3	−3,8	−0,2	−3,5	−1,7	3,8	−1,9	0,0	0,5	0,0
1974	1,7	−3,1	2,7	−3,3	−2,3	−9,9	−4,6	3,0	−4,6	−1,0	0,3	−1,0
1975	0,7	−1,5	1,0	−4,2	−0,0	−1,5	−0,2	2,4	−2,0	0,0	1,2	−0,1
1976	1,1	−4,9	0,9	−2,6	−1,5	−5,3	−1,5	3,0	−1,6	−0,5	0,3	0,7
1977	−0,3	−4,0	0,8	−1,9	−0,7	−5,5	1,2	0,7	0,0	0,1	−0,7	1,6
1978	−0,5	−2,7	1,4	−1,3	0,6	−6,9	2,4	−0,8	0,6	0,8	−0,7	1,7
1979	−1,6	−4,7	−0,8	−1,9	−0,0	−13,6	1,7	−1,1	0,1	−0,4	−0,1	−0,9
1980	−3,5	−3,7	−1,8	−0,3	−1,4	−12,0	−2,5	−1,5	1,8	−1,3	0,2	1,1
1971-80	0,6	−2,9	0,6	−2,2	−0,4	−6,4	−0,2	1,2	−0,6	−0,1	−0,0	0,6
1981	−3,2	−3,0	−0,8	−0,2	−1,4	−15,1	−2,3	2,1	2,7	−0,5	0,2	0,5
1982	−2,0	−4,1	0,6	−3,9	−3,0	−10,9	−1,6	2,8	1,7	−0,6	−0,2	0,7
1983	0,5	−2,2	0,7	−4,7	−1,7	−6,3	0,2	2,9	1,1	0,1	−1,0	1,9
1984	1,1	−3,2	1,0	−4,0	−0,7	−5,1	−0,9	4,1	0,3	0,1	−2.8	2,8
1985	1,9	−3,4	2,1	−5,2	−0,5	−3,3	−1,7	4,5	1,1	0,5	−3,4	3,5
1986	3,2	−2,7	2,0	−4,1	−0,3	−2,0	−1,1	4,5	0,9	0,6	−3,8	3,8

Table 35

Structure of EC exports by country and region, 1958 and 1984

(as % of total exports)

Exports of	BLEU		DK		D		GR		F		IRL		I		NL		UK		EUR 10	
	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984
BLEU	—	—	1,2	1,8	6,6	7,0	1,0	1,8	6,3	8,6	0,8	4,3	2,3	2,9	15,0	14,3	1,9	4,3	4,9	6,3
DK	1,6	0,9	—	—	3,0	2,1	0,2	0,7	0,8	0,8	0,1	0,8	0,8	0,8	2,6	1,4	2,4	1,7	2,0	1,4
D	11,6	19,7	20,1	16,3	—	—	20,5	19,6	10,4	14,7	2,2	10,2	14,3	16,1	19,0	29,7	4,2	10,5	7,4	12,0
GR	0,7	0,5	0,4	0,7	1,4	1,0	—	—	0,7	0,9	0,1	0,4	2,1	1,7	0,9	0,9	0,7	0,5	1,0	0,9
F	10,6	18,4	3,0	4,4	7,6	12,6	12,9	8,6	—	—	0,8	8,4	5,3	14,0	4,9	10,3	2,4	10,1	4,6	10,3
IRL	0,4	0,4	0,3	0,5	0,3	0,4	0,4	0,2	0,2	0,5	—	—	0,1	0,3	0,5	0,5	3,5	4,8	1,1	1,1
I	2,3	5,1	5,3	3,8	5,0	7,7	6,0	13,5	3,4	10,9	0,4	3,1	—	—	2,7	5,6	2,1	4,1	3,1	6,1
NL	20,7	13,9	2,2	3,4	8,1	8,5	2,0	3,4	2,0	4,7	0,5	7,0	2,1	2,9	—	—	3,1	8,6	5,4	6,5
UK	5,7	9,9	25,9	12,7	4,0	8,3	7,6	6,3	4,9	7,9	78,8	34,4	6,8	6,8	11,9	9,6	—	—	5,5	7,5
Total intra-Community trade	53,5	68,7	58,3	43,6	35,9	47,7	50,5	54,1	28,6	48,9	83,6	68,6	33,8	45,5	57,5	72,3	20,3	44,5	34,9	52,1
Other European OECD countries	10,4	7,9	17,2	25,6	23,7	19,2	6,7	6,4	10,5	11,9	1,8	6,1	16,6	12,9	12,3	7,6	9,6	12,4	16,4	13,6
USA	9,4	6,1	9,3	9,7	7,3	9,6	13,6	8,3	8,1	8,1	5,9	9,7	8,1	10,9	5,6	5,0	8,8	14,6	7,8	9,5
Canada	1,1	0,6	0,7	0,9	1,2	0,9	0,3	0,6	0,8	1,1	0,7	1,7	1,2	1,1	0,8	0,5	5,8	1,7	2,3	1,0
Japan	0,6	0,8	0,2	2,8	1,0	1,4	1,4	1,1	0,3	1,1	0,1	1,7	0,3	1,1	0,4	0,6	0,6	1,3	0,6	1,2
Australia	0,6	0,3	0,3	0,7	1,0	0,8	0,1	0,6	0,4	0,5	0,1	1,2	1,0	0,9	0,7	0,4	7,1	1,7	2,5	0,8
Developing countries of which:	18,8	11,9	9,7	13,7	22,3	13,8	7,2	22,1	48,4	24,0	1,6	8,1	27,9	21,8	18,1	9,8	33,8	19,1	27,9	16,1
OPEC	3,3	3,9	2,3	4,7	4,8	5,7	0,1	11,9	21,3	9,8	1,3	3,7	7,5	11,7	4,5	3,8	7,0	7,3	7,8	7,0
Other developing countries	15,5	8,0	7,3	9,0	17,5	8,1	7,1	10,2	27,1	14,2	1,3	4,4	20,4	10,1	13,7	6,0	26,8	11,8	20,1	9,1
Centrally-planned economies	3,8	2,4	3,8	2,4	5,0	4,8	16,3	6,4	3,7	3,7	0,2	0,8	4,7	4,1	2,0	1,6	3,1	2,4	3,9	3,4
Rest of world and unspecified	1,9	1,2	0,5	0,6	2,6	1,8	4,0	0,4	1,3	0,6	6,2	2,1	5,1	1,7	2,6	2,2	10,8	2,2	3,8	2,3
World (excl. EC)	46,4	31,3	41,7	56,4	64,1	52,3	49,5	45,9	71,4	51,1	16,4	31,4	66,2	54,5	42,5	27,7	79,7	55,5	65,1	47,9
World (incl. EC)	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Table 36

Structure of EC imports by country and region, 1958 and 1984

(as % of total imports)

Imports of	BLEU		DK		D		GR		F		IRL		I		NL		UK		EUR 10	
	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984	1958	1984
BLEU	—	—	3,8	3,0	4,5	7,1	3,3	2,5	5,4	9,6	1,8	2,1	2,0	3,7	17,9	10,8	1,6	4,3	4,4	6,0
DK	0,5	0,5	—	—	3,4	1,7	0,7	0,9	0,6	0,7	0,7	0,9	2,2	0,8	0,7	0,8	3,1	2,1	2,0	1,2
D	17,2	19,6	19,8	21,0	—	—	20,3	16,6	11,6	17,2	4,0	7,5	12,1	15,9	19,5	21,4	3,6	13,6	8,2	12,7
GR	0,1	0,2	0,0	0,2	1,7	0,7	—	—	0,6	0,4	0,2	0,1	0,5	1,0	0,1	0,2	0,2	0,4	0,4	0,5
F	11,6	14,5	3,4	4,2	7,6	10,6	5,4	6,9	—	—	1,6	4,5	4,9	12,4	2,8	6,3	2,7	7,4	4,2	8,0
IRL	0,1	0,4	0,0	0,4	0,1	0,6	0,0	0,4	0,1	0,8	—	—	0,1	0,3	0,1	0,8	2,9	3,3	0,9	1,1
I	2,1	3,6	1,7	3,3	5,5	7,8	8,8	9,6	2,4	9,7	0,9	2,0	—	—	1,8	2,8	2,0	4,8	2,5	5,4
NL	15,7	18,3	7,3	6,1	8,0	14,1	4,8	6,1	2,5	7,1	2,9	4,6	2,6	4,9	—	—	4,2	6,5	6,4	8,6
UK	7,4	6,5	22,8	9,1	4,4	7,4	9,9	3,9	3,6	8,2	56,4	48,1	5,5	4,3	7,4	8,5	—	—	5,0	6,5
Total intra-Community trade	54,7	63,5	59,0	47,3	35,2	50,0	53,3	47,0	26,7	53,7	68,4	69,8	29,8	43,3	50,1	51,7	20,3	42,3	34,0	50,0
Other European OECD countries	8,1	7,0	19,5	27,6	15,8	16,2	9,5	7,6	8,0	10,6	4,3	5,5	12,0	11,9	7,7	8,9	13,9	16,6	12,0	13,1
USA	9,9	6,4	9,1	4,7	13,6	6,6	13,7	2,9	10,0	6,5	7,0	14,2	16,2	6,1	11,3	9,2	9,3	14,0	11,4	8,1
Canada	1,4	0,6	0,2	0,5	3,1	0,9	0,8	0,3	1,0	0,7	3,0	1,0	1,4	0,7	1,5	0,7	8,2	2,0	3,7	1,0
Japan	0,6	2,2	1,5	3,5	0,6	4,0	2,0	7,6	0,2	2,2	1,1	2,8	0,4	1,6	0,8	2,5	0,9	4,9	0,7	3,2
Australia	1,7	0,3	0,0	0,5	1,2	0,4	0,3	0,3	2,4	0,6	1,2	0,0	3,0	0,7	0,2	0,4	5,4	0,9	2,7	0,6
Developing countries of which:	19,7	11,6	6,1	9,6	24,4	15,2	9,6	24,8	46,7	21,1	9,7	4,3	31,2	25,6	25,0	20,7	35,0	14,6	30,3	17,6
OPEC	5,9	4,2	0,3	3,3	6,7	5,9	1,7	19,6	19,7	11,5	0,7	0,3	13,9	15,7	11,5	9,9	11,3	3,4	10,9	8,1
Other developing countries	13,8	7,4	5,8	6,3	17,7	9,3	7,8	5,2	27,0	9,6	9,0	4,0	17,3	9,9	13,5	10,8	23,7	11,2	19,4	9,5
Centrally-planned economies	2,0	4,5	4,6	5,5	5,3	5,9	8,1	8,8	3,3	3,7	1,2	1,5	3,6	7,8	2,6	5,5	3,2	2,8	3,5	5,0
Rest of world and unspecified	1,9	3,9	0,0	0,8	0,8	0,8	2,9	0,7	1,6	0,8	4,2	0,9	2,3	2,3	0,8	0,4	3,8	1,9	1,5	1,4
World (excl. EC)	45,3	36,5	41,0	52,7	64,8	50,0	46,7	53,0	73,3	46,3	31,6	30,2	70,2	46,7	49,9	48,3	79,7	57,7	66,0	50,0
World (incl. EC)	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100

Table 37

Money supply (M2/M3)

(annual percentage change)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10	US	JAP
1960	4,3	8,0	11,1	20,2	16,7	5,5	19,6	7,0	0,9	10,5	4,9	20,1
1961	9,9	9,8	12,9	17,0	17,2	7,3	14,9	5,4	2,3	10,7	7,4	20,2
1962	7,4	8,5	10,4	21,5	18,7	9,6	17,0	6,6	2,6	10,9	8,1	20,3
1963	10,3	12,5	9,9	21,4	14,1	5,8	13,5	9,8	7,8	11,0	8,4	24,0
1964	7,6	11,1	9,4	16,1	9,8	9,4	8,8	10,4	5,8	8,6	8,1	18,7
1965	9,6	9,7	10,6	12,9	10,9	6,7	15,4	6,2	7,6	10,4	8,1	18,0
1966	8,2	12,8	8,3	18,2	10,6	10,6	13,8	5,9	3,4	8,6	4,5	16,3
1967	7,1	9,8	12,0	16,1	13,1	12,7	13,3	10,9	9,6	11,6	9,1	15,5
1968	8,6	14,5	11,8	17,8	11,6	16,9	11,6	14,8	7,3	10,9	7,9	14,8
1969	7,0	10,2	9,4	16,2	6,1	11,2	11,4	10,2	2,0	7,5	4,0	18,5
1970	10,0	3,3	9,1	19,3	15,4	14,0	13,6	11,0	9,6	11,5	6,2	16,9
1961-70	8,6	10,2	10,4	17,6	12,7	10,4	13,3	9,1	5,7	10,2	7,2	17,9
1971	12,9	8,5	13,5	22,4	17,8	12,9	17,1	9,0	14,1	14,9	13,4	24,3
1972	17,0	15,0	14,4	23,6	18,5	14,2	18,3	11,9	24,6	18,3	13,0	24,7
1973	15,4	12,6	10,1	14,5	15,0	26,0	23,2	21,9	27,0	18,1	7,0	16,8
1974	14,0	8,9	8,5	20,9	15,9	20,6	15,5	20,0	10,7	13,0	5,5	11,5
1975	15,1	25,1	8,6	26,5	18,2	18,9	23,5	5,7	6,3	13,7	12,6	16,5
1976	14,3	10,9	8,4	26,7	12,8	14,5	22,8	22,7	9,7	13,7	13,7	15,4
1977	10,3	9,9	11,2	22,7	13,9	17,1	23,8	3,6	9,4	13,4	10,6	13,4
1978	10,2	8,7	11,0	26,0	12,2	29,0	24,2	4,2	15,3	14,5	8,0	14,0
1979	8,2	10,8	6,0	18,4	14,0	18,7	23,2	6,9	13,2	12,9	7,9	10,8
1980	6,5	8,1	6,2	24,7	8,4	17,7	17,3	4,4	18,5	11,6	8,9	9,5
1971-80	12,4	11,7	9,8	22,6	14,7	18,9	20,8	10,8	14,7	14,4	10,0	15,6
1981	10,0	9,1	5,0	34,7	10,4	17,4	15,9	5,3	13,7	10,9	10,0	11,2
1982	7,5	11,4	7,1	29,0	10,8	13,0	17,2	7,6	8,9	10,7	9,0	9,1
1983	7,1	25,4	5,3	20,3	11,2	5,6	14,7	10,4	10,4	10,4	12,0	8,3
1984	5,7	17,8	4,7	29,4	8,3	10,1	13,9	7,7	10,0	9,2	8,3	8,1

Table 38

Short-term interest rates

(%)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10	US	JA
1960	:	:	5,1	8,0	4,1	:	3,5	2,1	:	:	:	:
1961	4,6	6,3	3,6	8,0	3,7	6,2	3,5	1,1	5,2	3,9	2,4	8,5
1962	3,4	6,5	3,4	8,0	3,6	5,0	3,5	1,9	4,1	3,6	2,8	9,0
1963	3,6	6,1	4,0	7,9	4,0	4,3	3,5	2,0	3,7	3,7	3,2	7,4
1964	4,9	6,2	4,1	7,8	4,7	5,5	3,5	3,5	5,0	4,4	3,6	10,0
1965	5,0	6,5	5,1	7,8	4,2	6,8	3,5	4,0	6,8	5,0	4,0	7,0
1966	5,6	6,5	6,6	8,0	4,8	7,0	3,5	4,9	7,0	5,6	4,9	5,6
1967	5,5	6,6	4,3	8,5	4,8	6,3	3,5	4,7	6,3	4,9	4,3	6,2
1968	4,5	6,6	3,8	8,3	6,2	7,9	3,5	4,6	7,9	5,3	5,4	7,6
1969	7,3	8,2	5,8	8,0	9,3	9,2	3,7	5,7	9,2	7,1	6,7	7,6
1970	8,1	9,0	9,4	8,0	8,6	7,0	5,3	6,2	8,1	7,9	6,3	8,0
1961-70	5,2	6,8	5,0	8,0	5,3	6,5	3,8	3,8	6,6	5,1	4,3	7,7
1971	5,4	7,6	7,1	8,0	6,0	6,6	5,7	4,5	6,2	6,1	4,3	6,4
1972	4,2	6,3	5,7	8,0	5,3	7,1	5,2	2,7	6,8	5,4	4,2	4,7
1973	6,6	8,1	12,2	9,0	9,3	12,2	7,0	7,5	11,8	9,7	7,2	7,2
1974	10,6	13,3	9,8	11,8	13,0	14,5	14,9	10,4	13,4	12,0	7,9	12,5
1975	7,0	6,5	4,9	11,9	7,6	10,9	10,4	5,4	10,6	7,5	5,8	10,7
1976	10,1	10,3	4,3	11,5	8,7	11,7	16,0	7,4	11,6	8,6	5,0	7,0
1977	7,3	14,5	4,3	12,0	9,1	8,4	14,0	4,8	8,0	7,5	5,3	5,7
1978	7,3	15,4	3,7	13,5	7,8	9,9	11,5	7,0	9,4	7,1	7,4	4,4
1979	10,9	12,5	6,9	16,7	9,7	16,0	12,0	9,6	13,9	9,8	10,1	6,3
1980	14,2	16,9	9,5	21,0	12,0	16,2	16,9	10,6	16,8	12,6	11,6	10,9
1971-80	8,3	11,1	6,8	12,3	8,8	11,3	11,3	6,9	10,8	8,6	6,8	7,5
1981	15,6	14,9	12,4	21,0	15,3	16,7	19,3	11,8	14,1	14,1	14,0	7,4
1982	14,1	16,4	8,8	20,0	14,6	17,5	19,9	8,2	12,2	11,9	10,6	6,9
1983	10,5	12,0	5,8	20,0	12,4	14,0	18,3	5,7	10,1	9,1	8,7	6,4
1984	11,5	11,5	6,0	20,0	11,6	13,2	17,3	6,1	10,0	9,2	9,5	6,1

Table 39

Long-term interest rates

(%)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10	US	JA
1960	:	:	6,3	:	5,7	5,4	5,3	4,2	5,4	:	:	:
1961	5,9	6,6	5,9	:	5,5	6,2	5,2	3,9	6,3	5,7	3,9	6,4
1962	5,2	6,6	5,9	:	5,4	6,0	5,8	4,2	5,9	5,6	3,9	6,4
1963	5,0	6,5	6,1	:	5,3	5,6	6,1	4,2	5,4	5,6	4,0	6,4
1964	5,6	7,1	6,2	:	5,5	6,0	7,4	4,9	6,0	6,1	4,1	6,4
1965	6,4	8,6	7,1	6,2	6,2	6,4	6,9	5,2	6,6	6,6	4,2	6,4
1966	6,7	8,7	8,1	7,4	6,6	6,8	6,5	6,2	6,9	7,0	4,7	6,8
1967	6,7	9,1	7,0	7,4	6,7	6,7	6,6	6,0	6,8	6,8	4,9	6,8
1968	6,5	8,7	6,5	7,3	7,0	6,5	6,7	6,2	7,6	6,9	5,3	6,8
1969	7,3	9,7	6,8	7,1	7,9	7,3	6,9	7,0	9,1	7,7	6,2	6,8
1970	7,8	11,1	8,3	7,4	8,6	7,8	9,0	7,8	9,3	8,7	6,6	7,1
1961-70	6,3	8,3	6,8	7,1	6,5	6,5	6,7	5,6	7,0	6,7	4,8	6,7
1971	7,3	11,0	8,0	7,5	8,4	9,2	8,3	7,1	8,9	8,3	5,7	7,0
1972	7,0	11,0	7,9	7,8	8,0	9,1	7,5	6,7	9,0	8,0	5,6	6,9
1973	7,5	12,6	9,3	10,4	9,0	10,7	7,4	7,3	10,8	9,0	6,3	7,0
1974	8,8	15,9	10,4	9,6	11,0	14,6	9,9	10,7	15,0	11,3	7,0	8,1
1975	8,5	12,7	8,5	9,0	10,3	14,0	11,5	9,2	14,5	10,5	7,0	8,4
1976	9,1	14,9	7,8	10,0	10,5	14,6	13,1	9,2	14,6	10,5	6,8	8,2
1977	8,8	16,2	6,2	9,2	11,0	12,9	14,6	8,5	12,5	9,8	7,1	8,2
1978	8,5	16,8	5,7	9,3	10,6	12,8	13,7	8,1	12,6	9,3	7,9	6,3
1979	9,7	16,7	7,4	13,3	10,9	15,1	14,1	9,2	13,0	10,2	8,7	7,3
1980	12,2	18,7	8,5	18,8	13,7	15,4	16,1	10,7	13,9	11,9	10,8	8,5
1971-80	8,7	14,6	8,0	10,4	10,3	12,8	11,6	8,6	12,5	9,9	7,3	7,5
1981	13,8	19,3	10,4	17,7	16,3	17,3	20,6	12,2	14,8	13,9	12,9	8,2
1982	13,5	20,5	9,0	15,4	16,0	17,0	20,9	10,5	12,7	12,7	12,2	8,0
1983	11,8	14,4	7,9	18,2	14,4	13,9	18,0	8,8	10,8	10,9	10,8	7,8
1984	12,0	14,0	7,8	18,5	13,4	14,6	15,0	8,6	10,7	10,5	12,0	7,4

Table 40

Gross official reserves

(end year, '000 million ECU)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10
1960	1,43	0,27	6,66	0,23	2,15	0,31	3,08	1,76	3,52	19,41
1961	1,70	0,26	6,70	0,25	3,15	0,32	3,55	1,83	3,10	20,86
1962	1,64	0,24	6,50	0,27	3,79	0,34	3,80	1,82	3,09	21,49
1963	1,84	0,44	7,15	0,27	4,59	0,38	3,38	1,96	2,94	22,95
1964	2,08	0,60	7,37	0,26	5,35	0,42	3,57	2,19	2,16	24,00
1965	2,18	0,55	6,95	0,23	5,93	0,38	4,49	2,26	2,81	25,78
1966	2,20	0,56	7,51	0,26	6,29	0,46	4,59	2,29	2,90	27,06
1967	2,52	0,52	7,92	0,28	6,80	0,43	5,31	2,55	2,62	28,95
1968	2,33	0,45	10,28	0,33	4,60	0,54	5,58	2,62	2,55	29,28
1969	2,53	0,45	7,49	0,33	4,19	0,68	5,31	2,69	2,66	26,33
1970	2,82	0,48	13,42	0,31	4,95	0,68	5,31	3,22	2,80	33,98
1971	3,25	0,66	17,17	0,48	7,72	0,90	6,38	3,57	8,04	48,18
1972	4,30	0,81	23,73	1,00	10,93	1,03	7,03	5,33	5,51	59,65
1973	6,22	1,20	34,03	1,05	12,15	0,72	8,96	7,50	5,53	77,37
1974	8,61	0,92	40,16	1,08	16,50	0,78	12,02	10,91	6,47	97,46
1975	9,57	0,94	40,49	1,17	21,19	0,95	12,31	11,80	5,63	104,05
1976	8,34	0,95	43,90	1,09	16,12	0,90	10,81	11,13	4,01	97,25
1977	8,64	1,53	50,61	1,15	17,07	1,08	13,97	12,18	13,24	119,47
1978	8,18	2,55	52,84	1,25	21,03	2,00	19,70	11,11	13,90	132,57
1979	10,41	2,59	57,59	1,47	29,44	1,62	26,69	14,52	17,39	161,72
1980	20,54	3,28	76,56	2,49	57,10	2,25	45,94	27,50	23,69	259,34
1981	18,28	3,01	79,81	2,19	52,52	2,59	45,48	26,26	22,13	252,28
1982	16,24	2,94	82,14	2,31	46,30	2,84	39,02	26,52	19,71	238,01
1983	20,94	5,17	98,20	2,95	63,69	3,33	56,31	33,25	23,17	307,01
1984	22,03	4,99	100,90	3,21	66,18	3,03	59,67	32,89	22,51	315,41

Table 41

ECU exchange rates

(national units per ECU; annual average)

	BL	DK	D	GR	F	IRL	I	NL	UK	US	JA
1960	52,810	7,2953	4,4360	31,686	5,2145	0,37721	660,1	4,0136	0,37721	1,0562	380,23
1961	53,367	7,3722	4,3074	32,020	5,2695	0,38119	667,1	3,8985	0,38119	1,0673	384,24
1962	53,490	7,3893	4,2792	32,094	5,2817	0,38207	668,6	3,8727	0,38207	1,0698	385,13
1963	53,490	7,3893	4,2792	32,094	5,2817	0,38207	668,6	3,8727	0,38207	1,0698	385,13
1964	53,490	7,3893	4,2792	32,094	5,2817	0,38207	668,6	3,8727	0,38207	1,0698	385,13
1965	53,490	7,3893	4,2792	32,094	5,2817	0,38207	668,6	3,8727	0,38207	1,0698	385,13
1966	53,490	7,3893	4,2792	32,094	5,2817	0,38207	668,6	3,8727	0,38207	1,0698	385,13
1967	53,240	7,4229	4,2592	31,945	5,2570	0,38765	665,5	3,8546	0,38765	1,0648	383,33
1968	51,444	7,7166	4,1155	30,867	5,0797	0,42870	643,1	3,7246	0,42870	1,0289	370,40
1969	51,109	7,6664	4,0262	30,666	5,2903	0,42591	638,9	3,7003	0,42591	1,0222	367,99
1970	51,112	7,6667	3,7414	30,667	5,6777	0,42593	638,9	3,7005	0,42593	1,0222	368,00
1971	50,866	7,7526	3,6457	31,433	5,7721	0,42858	647,4	3,6575	0,42858	1,0478	363,83
1972	49,361	7,7891	3,5768	33,653	5,6572	0,44894	654,3	3,5999	0,44894	1,1218	339,72
1973	47,801	7,4160	3,2764	36,952	5,4677	0,50232	716,5	3,4285	0,50232	1,2317	333,17
1974	46,399	7,2593	3,0835	35,781	5,7339	0,50980	775,7	3,2022	0,50980	1,1927	347,47
1975	45,569	7,1227	3,0494	39,994	5,3192	0,56003	809,5	3,1349	0,56003	1,2408	367,68
1976	43,165	6,7618	2,8154	40,884	5,3449	0,62158	930,1	2,9551	0,62158	1,1181	331,21
1977	40,883	6,8557	2,6483	42,035	5,6061	0,65370	1 006,8	2,8001	0,65370	1,1411	305,81
1978	40,061	7,0194	2,5561	46,783	5,7398	0,66389	1 080,2	2,7541	0,66391	1,2741	267,08
1979	40,165	7,2091	2,5109	50,774	5,8295	0,66948	1 138,5	2,7486	0,64639	1,3706	300,47
1980	40,598	7,8274	2,5242	59,323	5,8690	0,67600	1 189,2	2,7603	0,59849	1,3923	315,04
1981	41,295	7,9225	2,5139	61,624	6,0399	0,69102	1 263,2	2,7751	0,55311	1,1164	245,38
1982	44,711	8,1569	2,3760	65,342	6,4312	0,68960	1 323,8	2,6139	0,56045	0,9797	243,54
1983	45,438	8,1319	2,2705	78,088	6,7708	0,71496	1 349,9	2,5372	0,58701	0,8902	211,35
1984	45,448	8,1477	2,2381	88,425	6,8750	0,72619	1 381,8	2,5233	0,59072	0,7877	187,02
1985	44,899	8,0283	2,2320	100,739	6,8158	0,71548	1 458,0	2,5192	0,58387	0,7477	181,21
1986	44,578	8,0537	2,1944	120,026	6,8216	0,71904	1 555,2	2,4723	0,58108	0,8522	190,94

Table 42

Central rates against the ECU

(national currency per ECU)

Date	BLUE	DK	D	GR[1]	F	IRL	I	NL	UK[1]
13. 3.1979	39,4582	7,08592	2,51064	:	5,79831	0,662638	1 148,15	2,72077	(0,663247)
24. 9.1979	39,8456	7,36594	2,48557	:	5,85522	0,669141	1 159,42	2,74748	(0,649821)
30.11.1979	39,7897	7,72336	2,48208	:	5,84700	0,668201	1 157,79	2,74362	(0,648910)
23. 3.1981	40,7985	7,91917	2,54502	:	5,99526	0,685145	1 262,92	2,81318	(0,542122)
5.10.1981	40,7572	7,91117	2,40989	:	6,17443	0,684452	1 300,67	2,66382	(0,601048)
22. 2.1982	44,6963	8,18382	2,41815	:	6,19564	0,686799	1 305,13	2,67296	(0,557037)
14. 6.1982	44,9704	8,2340	2,33379	:	6,61387	0,691011	1 350,27	2,57971	(0,560453)
21. 3.1983	44,3662	8,04412	2,21515	:	6,79271	0,717050	1 386,78	2,49587	(0,629848)
18. 5.1983	44,9008	8,14104	2,24184	:	6,87456	0,725690	1 403,49	2,52595	(0,587087)
17. 9.1984	44,9008	8,14104	2,24184	87,4813	6,87456	0,725690	1 403,49	2,52595	(0,585992)
22. 7.1985	44,832	8,12857	2,2384	100,719	6,86402	0,724578	1 520,6	2,52208	(0,555312)

[1] The pound sterling and, since 19 September 1984, the drachma are represented in the ECU, but do not participate in the EMS exchange rate mechanism.

Table 43

Bilateral central rates since 22 July 1985

		BFR/LFR (Bruxelles)	DKR (København)	DM (Frankfurt)	FF (Paris)	IRL (Dublin)	LIT (Roma)	HFL (Amsterdam)	UKL[1] (London)
BFR/LFR 100	± 2,25	100	18,1312	4,99288	15,3106	1,61621	3 391,77	5,62561	—
DKR 100	± 2,25	551,536	100	27,5375	84,4432	8,91396	18 706,9	31,0273	—
DM 100	± 2,25	2 002,85	363,141	100	306,648	32,3703	67 932,5	112,673	—
FF 100	± 2,25	653,144	118,423	32,6107	100	10,5562	22 153,2	36,7434	—
IRL 100	± 2,25	61,8732	11,2184	3,08925	9,47313	1	2 098,6	3,48075	—
LIT 1 000	± 6,00	29,4831	5,34563	1,47205	4,51402	0,476508	1 000	1,65861	—
HFL 100	± 2,25	1 777,58	322,297	88,7526	272,158	28,7295	60 291,5	100	—
(UKL 1)	—	—	—	—	—	—	—	—	

[1] The pound sterling does not participate in the EMS exchange rate mechanism.

Table 44

Effective exchange rates against 19 countries

(1972 = 100)

	BL	DK	D	GR	F	IRL	I	NL	UK	EUR 10	US	JA
1960	96,7	106,6	79,4	109,3	113,4	109,5	102,0	93,7	120,4	97,4	107,1	86,7
1961	95,5	105,6	82,3	108,4	112,5	109,4	101,1	96,6	119,8	98,9	107,3	86,3
1962	95,6	105,6	82,7	108,3	112,5	109,6	101,1	97,2	120,1	99,4	108,2	86,4
1963	95,4	105,7	83,0	108,4	112,5	109,5	101,0	97,3	119,9	99,5	108,5	86,4
1964	95,6	105,5	83,3	108,4	112,5	109,4	100,5	97,1	119,6	99,4	108,5	86,3
1965	95,9	105,6	82,9	108,5	112,6	109,5	100,5	97,4	119,8	99,3	108,5	86,4
1966	95,8	105,8	82,9	108,6	112,4	109,5	100,7	97,0	119,8	99,2	108,6	86,2
1967	96,0	105,1	83,4	108,8	112,5	108,7	100,9	97,6	117,8	99,1	109,0	86,5
1968	97,0	101,4	84,9	110,7	114,2	102,1	103,0	99,1	104,1	96,3	111,4	88,4
1969	97,2	101,0	87,2	110,9	108,6	102,2	102,7	99,2	104,2	95,9	111,5	89,0
1970	97,3	100,2	94,5	109,3	99,9	102,0	101,7	97,7	103,7	97,3	110,1	88,6
1971	97,2	99,3	97,4	106,8	97,6	102,1	100,7	98,6	103,8	98,2	107,1	90,0
1972	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0
1973	101,4	106,1	110,5	92,0	103,3	93,1	89,8	103,2	89,6	102,5	92,0	105,6
1974	102,8	106,6	116,4	92,3	96,4	90,8	81,1	108,6	86,5	100,4	93,9	98,7
1975	104,4	110,2	118,3	83,2	105,8	85,6	77,7	111,2	79,5	102,0	93,1	95,8
1976	106,8	112,7	125,0	78,7	101,9	76,9	64,4	114,3	68,1	93,5	98,0	100,7
1977	112,9	112,1	135,1	76,4	97,0	75,2	59,3	120,3	64,9	94,2	97,3	111,6
1978	116,2	112,0	143,1	69,4	95,8	74,6	55,6	123,2	65,0	95,9	88,3	136,0
1979	117,6	111,2	149,9	65,5	96,4	74,8	53,7	125,0	69,0	101,5	85,8	125,9
1980	117,0	102,4	150,5	56,7	96,9	73,2	51,8	125,3	75,9	103,8	85,7	120,8
1981	110,2	94,7	142,1	51,0	88,3	66,8	45,4	119,8	76,0	88,6	96,6	137,3
1982	100,0	90,6	149,1	46,9	81,0	66,1	42,3	125,9	72,7	83,4	108,2	130,4
1983	97,3	90,1	155,1	38,4	75,2	63,4	40,7	128,6	67,7	78,6	114,4	144,6
1984	95,3	87,1	153,1	33,0	71,7	60,8	38,5	126,8	64,6	72,3	123,6	153,5
1985	96,0	87,9	152,8	28,9	72,1	61,2	36,1	126,5	64,7	70,7	129,6	155,7
1986	98,6	90,1	160,9	25,0	74,6	62,4	34,8	131,4	67,6	75,5	117,3	157,7

Table 45

Current receipts of general government

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 8
1960	27,5	27,3	35,1	21,1	34,9	24,8	28,8	32,5	33,9	30,1	32,2
1961	28,4	26,6	36,3	22,0	36,2	25,7	28,2	34,1	34,9	31,3	33,0
1962	29,2	28,2	36,6	23,2	36,3	25,2	29,1	33,5	34,4	32,9	33,7
1963	29,4	29,9	36,9	23,2	37,1	26,1	29,5	33,6	35,6	31,5	33,8
1964	30,0	29,7	36,4	24,0	38,0	26,9	30,6	33,5	35,7	31,5	34,1
1965	30,7	31,2	35,7	23,7	38,4	27,9	30,1	35,2	37,3	33,2	34,5
1966	32,4	33,5	36,2	25,3	38,4	30,0	30,1	35,8	39,2	34,4	35,1
1967	33,2	34,1	36,9	26,2	38,2	30,6	31,0	35,7	40,6	36,3	35,9
1968	33,8	36,9	38,0	27,3	38,8	31,0	31,6	34,5	42,4	37,7	36,9
1969	34,3	37,2	39,4	27,2	39,8	31,6	30,7	34,3	43,2	39,6	37,9
1970	35,2	41,7	38,3	26,8	39,0	35,3	30,4	35,0	44,5	40,5	37,8
1961-70	31,7	32,9	37,1	24,9	38,0	29,0	30,1	34,5	38,8	34,9	35,3
1970	36,5	46,2	38,9	26,5	39,8	:	30,7	36,4	44,8	39,9	38,2
1971	37,1	46,9	40,0	26,3	39,1	:	31,4	39,2	46,8	38,0	38,2
1972	37,6	46,5	40,4	26,3	39,0	:	31,2	39,6	47,9	36,4	38,0
1973	38,2	47,3	42,9	25,1	39,4	:	30,8	39,5	49,2	35,5	38,5
1974	39,2	49,1	43,4	26,7	40,3	34,3	30,9	40,5	50,4	39,1	39,8
1975	42,3	46,8	43,3	27,1	41,2	33,7	31,6	50,0	51,9	39,7	40,4
1976	41,8	47,6	44,6	29,2	43,5	36,9	33,2	51,3	52,5	38,8	41,4
1977	43,5	48,3	45,7	29,6	43,4	35,5	34,5	55,8	50,9	38,4	41,9
1978	44,2	50,3	45,3	29,9	43,3	34,3	36,3	56,5	50,9	37,1	41,9
1979	44,8	51,5	45,0	30,4	44,8	35,0	35,9	52,7	52,4	38,0	42,4
1980	44,6	52,9	45,3	30,2	46,6	37,7	38,1	52,7	53,6	39,5	43,7
1971-80	41,3	48,7	43,6	28,1	42,1	:	33,4	47,8	50,6	38,1	40,6
1981	45,3	52,9	45,4	29,0	47,4	38,4	39,6	53,8	53,8	41,3	44,6
1982	47,0	51,6	46,0	31,5	48,3	40,7	42,2	55,7	54,2	42,5	45,8
1983	46,2	54,1	46,0	31,9	48,9	42,5	45,1	58,1	56,3	41,6	46,4
1984	47,3	55,9	46,4	33,2	49,8	42,5	45,1	56,6	55,3	42,0	46,8
1985	48,4	56,6	46,5	33,7	48,9	41,9	45,4	56,7	54,6	41,4	46,5
1986	48,7	57,2	46,2	35,0	48,9	41,2	45,7	56,2	53,5	40,7	46,3

Table 46

Total expenditure of general government

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 8
1960	30,3	24,8	32,5	:	34,6	28,0	30,1	30,5	33,7	32,4	32,3
1961	29,8	27,1	33,8	:	35,7	29,7	29,4	30,3	35,4	33,1	33,0
1962	30,5	28,1	35,6	:	37,0	29,5	30,5	32,2	35,6	34,0	34,2
1963	31,5	28,6	36,4	:	37,8	30,5	31,1	32,1	37,6	35,4	35,2
1964	30,8	28,4	36,1	:	38,0	31,8	31,8	32,3	37,8	33,7	34,8
1965	32,3	29,9	36,7	:	38,4	33,1	34,3	33,3	38,7	36,2	36,3
1966	33,5	31,7	36,9	:	38,5	33,6	34,3	35,0	40,7	35,4	36,3
1967	34,5	34,3	38,8	:	39,0	34,8	33,7	37,5	42,5	38,3	37,7
1968	36,3	36,3	39,2	:	40,3	35,2	34,7	37,3	43,9	39,3	38,7
1969	36,1	36,3	38,8	:	39,6	36,6	34,2	34,1	44,4	41,3	38,8
1970	36.5	40,2	38,6	:	38,9	39,6	34,2	33,1	46,0	39,2	38,3
1961-70	33,2	32,1	37,1	:	38,3	33,5	32,8	33,7	40,3	36,6	36,3
1970	38,6	42,1	38,7	:	38,9	:	34,2	33,7	44,7	37,0	37,9
1971	40,3	43,0	40,2	:	38,3	:	36,6	36,9	46,6	36,6	38,8
1972	41,3	42,6	40,9	:	38,3	:	38,6	37,6	47,1	37,7	39,6
1973	41,5	42,1	41,7	:	38,5	:	37,8	36,3	47,5	38,2	39,8
1974	41,8	45,9	44,7	:	39,7	42,5	37,9	35,8	49,5	43,0	42,1
1975	46,7	48,2	49,0	:	43,5	46,3	43,2	48,9	54,1	44,2	45,9
1976	47,3	47,8	48,1	:	44,0	45,5	42,2	49,7	54,8	43,7	45,5
1977	49,1	48,8	48,1	:	44,2	43,1	42,5	52,7	52,4	41,7	45,2
1978	50,2	50,6	47,8	:	45,2	44,0	46,1	51,8	54,5	41,5	46,1
1979	51,9	53,2	47,7	:	45,5	46,4	45,5	52,1	57,0	41,4	46,3
1980	53,7	56,2	48,4	:	46,4	50,4	46,1	54,4	57,8	43,2	47,4
1971-80	46,4	47,8	45,7	:	42,3	:	41,6	45,6	52,2	41,1	43,7
1981	58,0	59,8	49,3	40,9	49,1	51,6	51,4	56,6	59,2	44,4	49,8
1982	58,1	60,9	49,5	40,9	51,1	54,5	54,8	57,0	61,2	44,8	51,2
1983	57,9	61,5	48,5	40,8	52,0	54,3	57,5	58,1	62,7	45,2	51,8
1984	57,2	60,5	48,3	43,1	52,6	52,6	58,7	55,2	61,6	45,9	52,1
1985	57,0	59,6	47,7	46,2	52,1	53,4	59,0	54,6	60,5	44,7	51,5
1986	56,1	57,9	47,0	45,5	52,2	51,6	58,5	54,3	60,1	43,5	50,9

Table 47

Net lending or net borrowing of general government

(as percent of GDP at current market prices)

	B	DK	D	GR	F	IRL	I	L	NL	UK	EUR 8
1960	−2,8	3,1	3,0	:	0,9	−2,4	−0,9	3,1	0,8	−1,0	0,6
1961	−1,3	0,1	2,8	:	1,0	−3,2	−0,8	4,8	0,1	−0,7	0,6
1962	−1,3	0,6	1,4	:	−0,1	−3,6	−1,0	2,3	−0,6	−0,0	0,1
1963	−2,1	1,9	0,9	:	−0,1	−3,6	−1,2	2,6	−1,3	−2,8	−0,8
1964	−0,8	1,8	0,7	:	0,7	−4,1	−0,8	2,2	−1,5	−1,1	−0,1
1965	−1,6	1,8	−0,6	:	0,7	−4,3	−3,8	2,9	−0,8	−2,0	−1,2
1966	−1,0	2,3	−0,2	:	0,6	−2,8	−3,8	1,9	−0,9	−0,0	−0,6
1967	−1,3	0,4	−1,4	:	0,0	−3,3	−2,2	−0,7	−1,3	−1,0	−1,1
1968	−2,5	1,1	−0,8	:	−0,8	−3,3	−2,8	−1,7	−0,9	−0,5	−1,1
1969	−1,8	1,4	1,1	:	0,9	−4,2	−3,1	1,2	−0,5	−0,6	−0,3
1970	−1,3	2,1	0,2	:	0,9	−3,7	−3,5	2,8	−0,8	2,5	0,1
1961-70	−1,5	1,3	0,4	:	0,4	−3,6	−2,3	1,8	−0,8	−0,6	−0,5
1970	−2,2	4,1	0,2	:	0,9	:	−3,5	2,7	0,1	2,9	0,3
1971	−3,2	3,9	−0,2	:	0,7	:	−5,2	2,2	0,2	1,4	−0,6
1972	−3,7	3,9	−0,5	:	0,8	:	−7,5	2,0	0,7	−1,3	−1,6
1973	−3,3	5,2	1,2	:	0,9	:	−7,0	3,3	1,7	−2,7	−1,3
1974	−2,6	3,1	−1,3	:	0,6	−8,2	−7,0	4,7	0,9	−3,8	−2,3
1975	−4,4	−1,4	−5,7	:	−2,2	−12,5	−11,7	1,1	−2,2	−4,6	−5,4
1976	−5,5	−0,2	−3,5	:	−0,5	−8,6	−9,0	1,6	−2,4	−4,9	−4,1
1977	−5,5	−0,5	−2,4	:	−0,8	−7,6	−8,0	3,1	−1,5	−3,3	−3,3
1978	−6,0	−0,3	−2,5	:	−1,9	−9,7	−9,7	4,6	−3,7	−4,4	−4,2
1979	−7,1	−1,7	−2,7	:	−0,7	−11,4	−9,5	0,6	−4,6	−3,3	−3,9
1980	−9,0	−3,3	−3,1	:	0,2	−12,7	−8,0	−1,6	−4,2	−3,7	−3,7
1971-80	−5,0	0,9	−2,1	:	−0,3	:	−8,3	2,2	−1,5	−3,1	−3,0
1981	−12,8	−6,9	−3,9	−11,9	−1,8	−13,2	−11,9	−2,3	−5,4	−3,1	−5,3
1982	−11,1	−9,3	−3,4	−9,7	−2,7	−13,8	−12,6	−1,4	−7,0	−2,3	−5,4
1983	−11,7	−7,4	−2,5	−8,9	−3,1	−11,8	−12,4	−0,1	−6,4	−3,6	−5,4
1984	−9,9	−4,6	−1,9	−9,9	−2,8	−10,1	−13,5	1,4	−6,3	−3,9	−5,3
1985	−8,6	−2,9	−1,2	−12,5	−3,2	−11,5	−13,6	2,1	−5,9	−3,2	−5,0
1986	−7,4	−0,6	−0,8	−10,5	−3,3	−10,4	−12,8	1,9	−6,5	−2,8	−4,6

Table 48

Budgetary expenditure of the European Communities (a)

(million ua/EUA/ECU)

	ECSC operational budget	European Development Fund	Euratom (b)	EC general budget						Total
				EAGGF (c)	Social Fund	Regional Fund	Industry, Energy, Research	Adm. and others (d)	Total EC	
1958	21,7	—	7,9	—	—	—	—	5,9	5,9	35,5
1959	30,7	51,2	39,1	—	—	—	—	25,2	25,2	146,2
1960	23,5	63,2	20,0	—	—	—	—	28,3	28,3	135,0
1961	26,5	172,0	72,5	—	8,6	—	—	25,4	34,0	305,0
1962	13,6	162,3	88,6	—	11,3	—	—	81,0	92,3	356,8
1963	21,9	55,5	106,4	—	4,6	—	—	79,5	84,1	267,9
1964	18,7	35,0	124,4	—	7,2	—	—	85,9	93,1	271,1
1965	37,3	248,8	120,0	102,7	42,9	—	—	55,5	201,1	607,2
1966	28,1	157,8	129,2	310,3	26,2	—	—	65,8	402,2	717,3
1967	10,4	105,8	158,5	562,0	35,6	—	—	77,5	675,1	949,8
1968	21,2	121,0	73,4	2 250,4	43,0	—	—	115,3	2 408,6	2 624,2
1969	40,7	104,8	59,2	3 818,0	50,5	—	—	182,7	4 051,2	4 255,9
1970	56,2	10,5	63,4	5 228,3	64,0	—	—	156,1	5 448,4	5 578,5
1971	37,4	236,1	—	1 883,6	56,5	—	65,0	284,3	2 289,3	2 562,8
1972	43,7	212,7	—	2 477,6	97,5	—	75,1	424,3	3 074,5	3 330,9
1973	86,9	210,0	—	3 768,8	269,2	—	69,1	533,8	4 641,0	4 937,9
1974	92,0	157,0	—	3 651,3	292,1	—	82,8	1 011,9	5 038,2	5 287,2
1975	127,4	71,0	—	4 586,6	360,2	150,0	99,0	1 017,8	6 213,6	6 412,0
1976	94,0	320,0	—	6 033,3	176,7	300,0	113,3	1 329,2	7 952,6	8 366,6
1977 (e)	93,0	800,0	—	6 667,6	55,3	400,0	167,0	1 303,9	8 483,2	9 376,2
1978	159,1	394,5	—	9 552,3	256,5	254,9	266,8	1 430,8	11 884,2	12 190,8
1979	173,9	480,0	—	10 765,0	527,0	499,0	288,0	2 368,0	14 602,5	15 256,4
1980	175,7	508,5	—	11 596,1	502,0	751,8	212,8	2 994,9(f)	16 057,5	16 741,7
1981	261,0	658,0	—	11 443,0	547,0	547,0	232,0	4 060,0	18 546,0(g)	19 465,0
1982	243,0	750,0	—	12 792,0	910,0	2 766,0(h)	346,0	4 613,0	21 427,0(i)	22 420,0
1983	300,0	752,0	—	16 331,3	801,0	2 265,5	1 216,2	4 151,5	24 765,5(j)	25 817,5
1984	408,0	810,0	—	18 985,8	1 116,4	1 283,3	1 346,4	3 387,4	26 119,3(k)	27 337,3
1985	453,0	—	—	20 483,0	1 410,0	1 620,0	736,0	4 184,0	28 433,0(l)	—
1986 (m)	439,0	—	—	21 870,0	2 399,0	2 751,0	852,0	7 178,0	35 050,0	—

Table 49

Budgetary receipts of the European Communities (a)

(million ua/EUA/ECU)

	ECSC levies and other	European Dev. Fund contributions	Euratom contributions (research only)	EC budget						Total
				Miscellan. and contributions under special keys	Own resources				Total EC	
					Miscellaneous	Agricultural levies	Import duties	GNP contributions or VAT (b) (c)		
1958	44,0	116,0	7,9	0,02	—	—	—	5,9	5,9	173,8
1959	49,6	116,0	39,1	0,1	—	—	—	25,1	25,2	229,9
1960	53,3	116,0	20,0	0,2	—	—	—	28,1	28,3	217,6
1961	53,1	116,0	72,5	2,8	—	—	—	31,2	34,0	275,6
1962	45,3	116,0	88,6	2,1	—	—	—	90,2	92,3	342,2
1963	47,1	—	106,4	6,7	—	—	—	77,4	84,1	237,5
1964	61,3	—	124,4	2,9	—	—	—	90,1	93,1	278,7
1965	66,1	—	98,8	3,5	—	—	—	197,6	201,1	366,0
1966	71,2	—	116,5	3,9	—	—	—	398,3	402,2	590,0
1967	40,3	40,0	158,5	4,2	—	—	—	670,9	675,1	913,9
1968	85,4	90,0	82,0	—	—	—	—	—	2 408,6	2 666,0
1969	106,8	110,0	62,7	78,6	—	—	—	3 972,6	4 051,2	4 330,7
1970	100,0	130,0	67,7	121,1	—	—	—	5 327,3	5 448,4	5 746,1
1971	57,9	170,0	—	—	69,5	713,8	582,2	923,8	2 289,3	2 517,2
1972	61,1	170,0	—	—	80,9	799,6	957,4	1 236,6	3 074,5	3 305,6
1973	120,3	150,0	—	—	511,0	478,0	1 564,7	2 087,3	4 641,0	4 911,3
1974	124,6	150,0	—	—	65,3	323,6	2 684,4	1 964,8	5 038,2	5 312,8
1975	189,5	220,0	—	—	320,5	590,0	3 151,0	2 152,0	6 213,6	6 623,1
1976 (d)	129,6	311,0	—	—	282,8	1 163,7	4 064,6	2 482,1	7 993,1	8 433,7
1977	123,0	410,0	—	—	283,0	1 778,5	3 927,2	2 494,5	8 483,2	9 016,2
1978	164,9	147,5	—	—	217,2	2 283,3	4 407,9	4 975,8	11 884,2	12 196,6
1979	168,4	480,0	—	—	230,3	2 143,4	5 189,1	7 039,8	14 602,5	15 251,0
1980	226,2	555,0	—	—	1 055,9(e)	2 002,3	5 905,8	7 093,5	16 057,5(f)	16 838,7
1981	264,0	658,0	—	—	1 219,0	1 747,0	6 392,0	9 188,0	18 546,0(g)	19 468,0
1982	243,0	750,0	—	—	187,0	2 228,0	6 815,0	12 197,0	21 427,0	22 420,0
1983	300,0	700,0	—	—	1 565,0	2 295,0	6 988,7	13 916,8	24 765,5(h)	25 765,5
1984	408,0	810,0	—	—	1 060,7(i)	2 436,3	7 960,8	14 594,6	26 052,4(j)	—
1985	453,0	—	—	—	2 269,1(l)	2 106,5	8 596,1	15 461,5	28 433,2(k)	—
1986(m)	439,0	—	—	—	263,5	2 698,7	9 700,5	22 388,0	35 050,7	—

Table 50

Borrowing operations of the European Communities and of the European Investment Bank

(million ua/EUA/ECU) (a)

	ECSC	EIB	Euratom	EEC(b)	EEC-NCI(c)	Total
1958	50	—	—	—	—	50
1959	—	—	—	—	—	—
1960	35	—	—	—	—	35
1961	23	21	—	—	—	44
1962	70	32	—	—	—	102
1963	33	35	5(d)	—	—	73
1964	128	67	8(d)	—	—	203
1965	54	65	11(d)	—	—	130
1966	103	139	14(d)	—	—	256
1967	58	195	3(d)	—	—	256
1968	108	213	—	—	—	321
1969	52	146	—	—	—	198
1970	60	169	—	—	—	229
1971	102	413	1(d)	—	—	516
1972	230	462	—	—	—	692
1973	263	608	—	—	—	871
1974	528	826	—	—	—	1 354
1975	731	814	—	—	—	1 545
1976	956	732	—	1 249	—	2 937
1977	729	1 030	99	571	—	2 429
1978	981	1 863	72	—	—	2 916
1979	837	2 437	153	—	178	3 605
1980	1 004	2 384	181	—	305	3 874
1981	325	2 243	373	—	339	3 280
1982	712	3 146	363	—	773	4 994
1983	750	3 508	369	—	1 617	6 244
1984	822	4 050	214	—	967	6 053

Table 51

Net outstanding borrowing of the European Communities and of the European Investment Bank

(million ua/EUA/ECU) (a)

	ECSC	BEI	Euratom	EEC(b)	EEC-NCI(c)	Total
1958	212	—	—	—	—	212
1959	209	—	—	—	—	209
1960	236	—	—	—	—	236
1961	248	21	—	—	—	269
1962	304	54	—	—	—	358
1963	322	88	—	—	—	410
1964	436	154	—	—	—	590
1965	475	217	—	—	—	692
1966	560	355	—	—	—	915
1967	601	548	—	—	—	1 149
1968	686	737	—	—	—	1 423
1969	719	883	—	—	—	1 602
1970	741	1 020	—	—	—	1 761
1971	802	1 423	—	—	—	2 225
1972	963	1 784	—	—	—	2 747
1973	1 157	2 287	—	—	—	3 444
1974	1 615	3 124	—	—	—	4 739
1975	2 391	3 926	—	—	—	6 317
1976	3 478	4 732	—	1 161	—	9 371
1977	3 955	5 421	99	1 500	—	10 975
1978	4 416	6 715	172	1 361	—	12 664
1979	4 675	8 541	323	965	178	14 682
1980	5 406	10 604	502	1 016	402	18 019
1981	5 884	13 482	902	1 062	894	22 224
1982	6 178	16 570	1 272	591	1 747	26 358
1983	6 539	20 749	1 680	4 610	3 269	36 847
1984	7 119	25 007	1 892	4 932	4 432	43 382

Notes on the tables

Table 1

Source: EC: Eurostat, Cronos data bank, USA: Department of Commerce, Bureau of the Census, series p-25; Japan: OECD, National accounts, Volume I.

Table 2

Definition: NL: full-time equivalent; USA: persons engaged.

Source: EC: as Table 1; USA: by Department of Commerce, Survey of Current Business; Japan: national publications.

Table 3

Definition: EC: SOEC; USA, Japan: OECD.

Source: Eurostat, Cronos data bank;

Belgium: For certain categories of unemployed the obligation to register was ended with effect from 1 April 1985.

The Netherlands: For those unemployed aged 57 1/2 years or over, the obligation to register was ended with effect from 1 January 1984.

Tables 4 to 8, 10 to 22, 26 and 27, 30 and 31

Source: EC: Eurostat, Cronos data bank; USA, Japan: OECD, National accounts, Volume I.

Table 9

Coverage: Construction excluded.

Source: Eurostat, Cronos data bank.

Table 23

Definition: Compensation per employee deflated by the price index of private consumption.

Table 24

Definition: Compensation of employees adjusted for the share of self-employed in total employment, as per cent of GDP at current factor cost.

Table 25 and 44

For a detailed commentary on the method used see *European Economy* No 8, March 1981.

EUR 10: against 11 non-member countries (Australia, Austria, Canada, Finland, Japan, Norway, Portugal, Spain, Sweden, Switzerland, USA).

Table 28 and 29; 32 to 33; 35 and 36

Source: Eurostat, Cronos data bank.

Table 34

Definition: Net lending or borrowing of the nation minus net capital transfers to the rest of the world.

Source: Eurostat, Cronos data bank.

Table 37

Definition: B up to 1969, monetary claims on the main monetary institutions; from 1969, M2. DK: M2; new definitions from 1975. D: M3. GR: M3; F: up to 1978, total M2; from 1978 residents M2. IRL: M3; breaks in series 1971 and 1983. I: up to 1975 and from 1982 M2; otherwise M3. NL: M2; breaks in series 1976, 1977 and 1978. UK: sterling M3. EC: rate of growth of the harmonic mean, weighted by GDP at current prices and purchasing power parities of the money stock indices of the countries (1975 = 100). The weight of Luxembourg has been added to that of Belgium.

Table 38

Definition: DK: Discount rate until 1976, day-to-day rate since 1977. D: 3-month inter-bank rate. GR: interest rates on credit for working capital to industry until 1980; from 1981, rate on large time deposits. F: Day-to-day rate until 1968, 1-month commercial paper rate since 1969. IRL: up to 1970: 3-month inter-bank loans in London; from 1971: 3-month inter-bank loans in Dublin. I: 12-month Treasury bill rate until 1970, inter-bank call money rate since 1971. NL: Treasury bill 3-months up to 1972; inter-bank loans 3-months from 1973. B: rate 4-month certificates of Fonds des Rentes. UK: 3-month Treasury bill rate until September 1964, 3-month inter-bank rate since October 1964. EC: geometrically weighted average with weights based on 1975 GDP at 1975 prices and purchasing power parities. The weight of Luxembourg has been added to that of Belgium.

Table 39

Definition: DK: yield on first-class mortgage loans. D: average yield on all public sector bonds. GR: weighted average yield of government bonds. F: yield on public sector bonds. IRL: up to 1970: yield on government securities with maturity 20 years in London; from 1971: yield on government securities with maturity 15 years in Dublin. I: yield on Crediop public bonds. NL: yield of 3,25% government bonds up to 1973. Private loan to public utilities from 1974. B: yield on 5-year government bonds. UK: yield on 20-year government securities. EC: as for Table 38.

Table 40

Source: IMF: International Financial Statistics and Commission departments. Gold is valued at market-related prices.

Table 41

Source: Eurostat and Commission departments.

Tables 42 to 44

Source: Commission departments.

Tables 45 to 47

Source: EC: 1960-70 OECD, 1970-85 member countries national accounts and Commission departments; USA, Japan: OECD. EUR 8: Community excluding Greece and Ireland.

Table 48

Source: 1958-84: Management accounts. (a) u.a. until 1977, EUA/ECU 1978 onwards. (b) Incorporated in the EC budget from 1971. (c) This column includes, for the years to 1970, substantial amounts carried forward to following years. (d) Including the European Parliament, the Council, the Court of Justice, the Court of Auditors and the administrative part of the ECSC budget. (e) In 1977 appropriations for the Social Fund carried forward from 1976 and subsequently cancelled amounted to 227 716 611 u.a., while total expenditure for 1977 amounted to only 172 439 999 u.a. giving the net figure shown here. (f) Including surplus of 82,4 million ECU carried forward to 1981. (g) Including 1 173 ECU carried forward to 1982. (h) Including 1 819 million ECU UK special measures. (i) Including 2 211 million ECU carried forward to 1983. (j) Including 1 707 million ECU carried forward to 1984. (k) There was a small deficit in 1984 in respect of EC budget due largely to late payment of advances by some Member States. (l) 1985 general budget adopted in June 1985. (m) Preliminary draft general budget for 1986 prepared by the Commission in July 1985.

Table 49

Source: 1958-84: Management accounts. (a) u.a. until 1977, EUA/ECU 1978 onwards. (b) GNP until 1978, VAT from 1979 onward. (c) This column includes for the years to 1970 surplus revenue from previous years carried forward to following years. (d) As a result of the calculations to establish the relative shares of the Member States in the 1976 budget, an excess of revenue over expenditure occurred amounting to 40 543 573 u.a. This was carried forward to 1977. (e) Including surplus brought forward from 1979 and balance of 1979 VAT and financial contributions. (f) Including surplus of 82,4 million ECU carried forward to 1981. (g) Including surplus of 661 million ECU. (h) Includes surplus of 307 million ECU. (i) Includes 593 million ECU of repayable advances by Member States. (j) See note (k) to Table 48. (k) 1985 general budget adopted in June 1985. (l) Includes non-repayable advances by Member States of 1981, 6 mio ECU. (m) Preliminary draft general budget for 1986 prepared by the Commission in July 1985.

Tables 50 and 51

Source: European Economy No 6; 'Borrowing and lending instruments looked at in the context of the Community's financial instruments', No 8, 'The Community's borrowing and lending operations: recent developments affecting certain instruments', and No 13, September 1982, 'The borrowing and lending activities of the Community'. (a) ECSC: 1958-74, u.a.; 1975-82. EUA/ECU, EIB: 1961-73, u.a.; 1974-82, EUA/ECU. Euratom: 1963-71 u.a.; 1977-84, EUA/ECU. (b) EEC balance of payments financing. (c) EEC New Community Instrument (for investment). (d) Drawings under credit lines opened with Eximbank (USA).

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