

II

(Acts whose publication is not obligatory)

COUNCIL

COUNCIL DECISION

of 21 December 1988

adopting the annual report on the economic situation in the Community and laying down economic policy guidelines for 1989

(88/655/EEC)

THE COUNCIL OF THE EUROPEAN COMMUNITIES,

HAS ADOPTED THIS DECISION:

Having regard to the Treaty establishing the European Economic Community,

Having regard to Council Decision 74/120/EEC of 18 February 1974 on the attainment of a high degree of convergence of the economic policies of the Member States of the European Economic Community ⁽¹⁾, as amended by Decisions 75/787/EEC ⁽²⁾ and 79/136/EEC ⁽³⁾, and in particular Article 4 thereof,

Having regard to the proposal from the Commission,

Having regard to the opinion of the European Parliament ⁽⁴⁾,

Having regard to the opinion of the Economic and Social Committee ⁽⁵⁾.

Article 1

The Council hereby adopts the annual report on the economic situation in, and economic policy guidelines to be followed by the Community, which are contained in Parts A to C of the report attached to this Decision and lays down the economic policy guidelines to be followed by the Member States, contained in Part D of the said report.

Article 2

This Decision is addressed to the Member States.

Done at Brussels, 21 December 1988.

For the Council

The President

V. PAPANDREOU

⁽¹⁾ OJ No L 63, 5. 3. 1974, p. 16.

⁽²⁾ OJ No L 330, 24. 12. 1975, p. 52.

⁽³⁾ OJ No L 35, 9. 2. 1979, p. 8.

⁽⁴⁾ OJ No C 326, 19. 12. 1988.

⁽⁵⁾ Opinion delivered on 23 November 1988 (not yet published in the Official Journal).

ANNUAL ECONOMIC REPORT 1988 to 1989

PREPARING FOR 1992

ANNUAL ECONOMIC REPORT 1988 to 1989

Preparing for 1992

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ANNUAL ECONOMIC REPORT 1988 to 1989

PREPARING FOR 1992

SUMMARY AND CONCLUSIONS

Favourable economic prospects for the Community and world economy

1. The economic prospects for the Community have significantly improved in recent months. In 1988 the Community benefited from an unexpected dynamism of its own, in the whole Organization for Economic Cooperation and Development (OECD) area and from world trade. In the Community, growth (1988: 3 1/2 % on average) is likely to be the strongest since the end of the 1970s; the increase in investment (7%) the highest for over two decades; the inflation rate (3 1/2 %) should be about that of the 1960s. Despite some moderation in economic growth in the rest of the world, growth is likely to be strong in 1989 (about 2 3/4 %). The inflation trend should only increase slightly. The rate of unemployment has started to decrease but it is still at too high a level.

2. The international framework for the conduct of monetary policy in the Community has changed significantly. With an improvement in the United States trade deficit early in the year and an increase in interest rates in spring the exchange rate of the dollar against European currencies had by autumn almost reached its level of January 1987, just before the Louvre accord. Partly to control the rise in the dollar and partly in response to the exigencies of internal stability European central banks were led, to different degrees, to tighten conditions on their own money markets.

3. International cooperation allowed significant progress to be made towards greater stability in the world economy. But it needs to be pursued with determination because important risks remain: (a) in 1989, the reduction in balances of payments disequilibria is likely to lose some of its vigour at a time when the accumulation of United States foreign debt is continuing; (b) the persistence of the disequilibria continues to create risks for the stability of the international monetary system; (c) the situation in developing countries is not improving and is affected by the recent rise in interest rates.

Encouraging elements and some matters of concern

4. Three aspects of the economic situation are encouraging:

- The dynamism of the economies of Spain, Portugal, Italy and the United Kingdom is now spreading to their partners whose exports, and also investment, are more buoyant. Thus, for example, in France and Germany growth should be about 3 % in 1988 and should only dip slightly in 1989 (compared with 2 % in 1987).

- Growth is more and more being led by investment. Many factors are contributing to this: greater profitability, a historically high level of capacity utilization, a favourable international environment and preparation by private firms for 1992.

- The Community has achieved a degree of stability and convergence of inflation rates unequalled since the 1960s. However, progress is still necessary, especially in Portugal and Greece.

5. Despite these satisfactory trends there are four areas of concern: (a) the risk of renewed inflation; (b) excessive budgetary deficits in some countries; (c) an increase in the intra-Community disequilibria in external balances; (d) an unemployment rate that is still on average in the Community more than 11 % of the active population.

6. The strengthening of potential growth must remain a priority for all Member States. However, the consolidation of the current good growth performances may require, over the coming months, different actions in different Member States. As growth in the more dynamic countries is expected to slow down as a result of inflationary pressures and/or a deterioration of external accounts, economic policies in the other countries should accentuate the shift to domestic growth by a strengthening of supply and demand conditions.

Realizing the medium-term objectives

7. Faster growth is now giving the Community the chance to realize in the best conditions its major objectives: to benefit from the completion of the internal market, strengthen economic and social cohesion and reduce unemployment.

8. The irreversible character of the completion of the internal market in 1992 was confirmed by the Council of Hanover. Significant progress has already been realized. In recent months, public opinion and enterprises have become more and more aware of the opportunities offered by this project. It is essential that these hopes are not disappointed when the decisions implementing the important measures of the White Paper are taken during the coming years.

9. To produce its full effects, the completion of the internal market needs to be accompanied by appropriate

structural policies, including an effective competition policy, also necessary in their own right.

10. The success of the internal market will also have significant macroeconomic effects. Studies by the Commission services indicate that the completion of the internal market will in the medium term improve significantly growth, budgetary and external positions and will have favourable effects on inflation. So that the productivity gains which will be realized are rapidly transformed into higher growth and employment, it will be important to fully benefit from the alleviation of constraints by reducing domestic disequilibria and actively strengthening the conditions of supply and demand.

11. With the reform and the increase of the Structural Funds, already under way, and the increased activity of the Community financial instruments, the Community has acquired the means to strengthen economic and social cohesion. A new model of 'partnership' between the Community and the beneficiary countries must be created. Not only is the efficient utilization and additionality of these resources at programme level essential but economic policies in the countries concerned must ensure that the overall supply conditions improve and especially that the efficiency and the share of productive investment relative to GDP are increased.

12. Even if the completion of the internal market in the last analysis results in significant gains in welfare and employment, the restructuring which it will imply during the transition phase gives rise to certain anxieties. The social dimension of the internal market needs to be given attention, in particular: (i) the implementation of policies to facilitate re-employment; (ii) the convergence towards the higher social standards, for instance, by minimum security and health regulations at the work place; (iii) the strengthening of the social dialogue at Community level.

13. The reduction in unemployment remains the priority task common to all Member States. Already employment is increasing at a historically high rate. This trend needs to be reinforced. In many countries there are signs of greater labour market adaptability, especially in the form of part-time work. The direction of the cooperative growth strategy for more employment remains valid: it involves, at the macroeconomic level further improvement in the profitability of capacity increasing and employment creating investment. Continued moderation in wage costs, in conjunction with the new favourable demand prospects would contribute to this. It also involves concentrating attention on the elimination of unnecessary administrative obstacles which hinder employment creation and on greater mobility and skill improvements, particularly by sustained training efforts.

The narrow path towards a consolidation of growth

14. The potential for non-inflationary growth can be strengthened by making European economies even more adaptable. Greater flexibility of markets and their positive effect on the behaviour and initiative of entrepreneurs is in itself a source of progress. In a situation where on the one hand it is necessary to avoid excessive pressures on productive capacity and on the other to further improve employment performances, structural policies are still very important.

15. The stabilization, and then the appreciation of the dollar on the foreign exchanges, led the monetary authorities to give more attention to the objectives of domestic stability. Recent increase in money market interest rates in the Community has strengthened the credibility of monetary authorities. To the extent that longer-term expectations of inflation and/or depreciation of the currencies have been reduced, long-term interest rates could be stabilized or decrease on a sound basis; some evidence of this emerged in some countries in early autumn.

In the countries participating in the exchange rate mechanism domestic inflationary pressures generally remain under control and further tightening of monetary policy does not seem necessary in the immediate future. Yet, the risk and main challenge to monetary policy could arise from renewed instability of the dollar.

16. For budgetary policies, medium-term objectives continue to be of primary importance. In the context of the achievement of the internal market discussions concerning the approximation of indirect taxes and taxation of capital income must be pursued so as to reach rapid agreement on these subjects. Other medium-term objectives include the convergence of general government balances, still excessive in some Member States, and the need to use budgetary policy to improve the conditions of supply and demand.

17. The increasing interdependence between Member States makes greater coordination of economic policy even more important. Furthermore, an increasingly high degree of stability in exchange rates related to converging underlying economic fundamentals would improve the functioning of the internal market. Monetary cohesion would be strengthened by an enlargement of the exchange rate mechanism at the appropriate time to those countries not yet participating, management of monetary policies in greater cooperation and strengthening the role of the ecu. However monetary cohesion in the Community cannot be permanently ensured unless Member States follow compatible policies in other areas, particularly budgetary policy. In this context it is important to strengthen the consensus on the principal economic policy objectives: (a) stable prices and downward convergence of inflation rates; (b) medium term compatibility of payments balances; and (c) the contribution of internal and external stability to the growth and employment objectives of the Community and its Member States.

Main economic indicators 1985 to 1989 — Community countries, USA and Japan

(a) GDP ⁽¹⁾ at constant prices
(% change on previous year)

	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	1,4	2,3	1,8	3	2 1/4
DK	4,2	3,4	-1,0	0	1 3/4
D	2,1	2,6	1,9	3 1/4	2 1/2
GR	3,0	1,3	-0,4	2 3/4	2
E	2,3	3,3	5,2	4 3/4	4
F	1,7	2,1	2,3	3	2 3/4
IRL	1,1	-0,3	4,1	3	3 1/4
I	2,7	2,7	3,1	4	3 1/4
L	3,8	2,9	2,4	2 3/4	2 1/2
NL	2,3	2,4	1,5	2 1/4	2 1/4
P	3,3	4,3	4,6	4	3 1/2
UK	3,7	2,9	4,3	3 3/4	2 1/2
EUR 12	2,5	2,6	2,9	3 1/2	2 3/4
USA	3,1	3,0	3,4	4	2 1/4
JAP	4,5	2,4	4,2	5 1/2	3 3/4

(b) Domestic demand at constant prices
(% change on previous year)

	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	1,3	3,2	2,4	3	2 1/4
DK	5,7	5,7	-3,2	-1 1/2	3/4
D	1,0	3,7	3,1	3 1/2	2 1/2
GR	6,1	-0,5	0,2	3 1/2	3
E	2,9	5,9	8,0	6 1/4	5 1/4
F	2,2	3,7	3,3	3	2 3/4
IRL	-1,3	0,8	-1,5	-1/4	1 1/2
I	3,2	3,6	4,6	4 1/2	3 1/2
L	0,7	-0,9	6,1	1/2	2 1/2
NL	2,5	3,9	2,2	1 3/4	2
P	0,8	8,4	9,5	6 1/2	5 1/2
UK	2,9	3,8	4,3	5 1/4	3 1/2
EUR 12	2,4	3,9	3,9	4	3 1/4
USA	3,5	3,8	3,0	2 3/4	2
JAP	3,8	4,0	5,1	7 1/4	4 1/4

(c) Deflator of private consumption
(% change on previous year)

	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	5,2	0,8	1,6	1 1/4	2 1/2
DK	4,9	3,6	4,1	4 3/4	3 3/4
D	2,1	-0,2	0,5	1 1/4	2 1/2
GR	18,7	22,2	15,8	13 1/4	12 3/4
E	8,3	8,7	5,3	4 3/4	4 1/4
F	5,7	2,5	3,2	2 3/4	2 3/4
IRL	4,5	3,6	3,1	2	2 3/4
I	9,3	6,1	4,8	5	4 1/2
L	5,2	0,6	0,6	1 1/2	2 1/4
NL	2,5	0,2	-0,4	3/4	1 1/4
P	19,0	12,0	10,2	9 1/2	7
UK	5,2	3,6	3,8	4 1/2	4 3/4
EUR 12	5,9	3,6	3,3	3 1/2	3 3/4
USA	3,1	2,1	4,5	4 1/4	5
JAP	2,1	0,6	-0,2	1	2

(d) Balance on current transactions
(% of GDP) ⁽¹⁾

	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	0,7	2,6	1,9	1 3/4	1 3/4
DK	-4,7	-5,1	-3,0	-2 1/2	-2 1/4
D	2,4	4,2	4,0	4	4 1/4
GR	-8,2	-5,4	-3,4	-2 3/4	-3 1/2
E	1,6	1,7	0,1	-3/4	-2
F	0,1	0,6	-0,3	0	1/4
IRL	-3,8	-2,4	1,3	2 1/2	3 1/2
I	-0,9	0,8	-0,1	-1/2	-1/2
L	43,3	46,1	38,0	38 1/2	36 1/2
NL	4,3	2,8	1,7	1 1/2	1 3/4
P	1,7	3,9	1,8	0	-1 3/4
UK	0,5	-0,8	-0,6	-3	-3 1/4
EUR 12	0,7	1,3	0,8	1/2	1/4
USA	-2,9	-3,4	-3,6	-2 3/4	-2 1/2
JAP	3,7	4,3	3,6	2 3/4	3

(e) Number of unemployed as % of the civilian labour force ⁽³⁾

	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	13,6	12,6	12,3	11½	11
DK	8,7	7,4	7,6	8½	9
D	8,4	8,1	8,1	8	8¼
GR	7,8	7,4	7,4	7½	7½
E	21,4	21,0	20,5	20	19½
F	10,5	10,7	10,8	10¾	10¾
IRL	17,9	18,2	19,2	18¾	18¼
I	12,9	13,7	14,0	15	14½
L	1,7	1,4	1,6	1½	1¼
NL	13,3	12,1	11,5	11¼	11
P	8,7	8,7	7,2	6½	6½
UK	12,0	12,0	10,6	8½	7¼
EUR 12	11,8	11,9	11,6	11¼	11
USA	7,2	7,0	6,2	5½	5½
JAP	2,6	2,8	2,8	2½	2½

(f) General government lending and borrowing ⁽⁴⁾
(% of GDP)

	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	-8,3	-8,9	-7,2	-7¼	-6½
DK	-2,0	3,1	-2,1	1	1¼
D	-1,1	-1,3	-1,8	-2¼	-1¼
GR	-13,6	-10,8	-9,5	-12	-13¼
E	-7,0	-5,7	-3,6	-3	-3
F	-2,8	-2,9	-2,5	-2	-1¾
IRL	-11,1	-10,6	-9,1	-6½	-6
I	-12,5	-11,4	-10,5	-10	-10
L	5,8	6,0	5,2	5¼	6¼
NL	-4,7	-6,0	-6,3	-5¼	-4½
P	-10,1	-7,8	-8,4	-8	-7¾
UK	-2,7	-2,4	-1,4	-¼	0
EUR 12	-5,2	-4,8	-4,2	-3¾	-3½
USA	-4,3	-3,5	-2,3	-1¾	-1¾
JAP	-0,8	-1,5	-0,3	-¼	¼

(g) Total employment
(annual % change)

	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	0,8	1,0	0,3	1¼	¾
DK	2,9	2,3	1,1	-¼	¼
D	0,7	1,0	0,7	½	¾
GR	1,0	0,1	-0,1	1	¾
E	-1,4	1,9	3,0	2½	2
F	-0,4	0,3	0,1	½	½
IRL	-2,2	-0,4	-0,1	0	½
I	1,4	0,8	-0,1	½	½
L	1,4	2,6	2,7	2	1½
NL	1,3	1,8	1,2	¾	1
P	-0,3	0,0	2,7	1¾	1
UK	1,6	0,4	1,7	2	1
EUR 12	0,6	0,8	0,9	1	1
USA	2,4	1,7	2,6	2¼	1½
JAP	0,7	0,9	1,0	1½	¾

(h) Real compensation of employees per head ⁽⁵⁾
(annual % change)

	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	-0,4	3,0	1,6	1	1¼
DK	-0,3	1,0	4,0	-½	-1
D	0,9	4,1	2,4	1¾	0
GR	3,3	-5,4	-2,9	3¼	1
E	1,7	-0,4	2,1	1¾	1¾
F	0,9	1,5	0,1	1	1
IRL	1,8	1,5	1,9	1¼	1
I	0,8	1,5	3,8	2	2¾
L	-1,4	4,3	3,3	2	2¾
NL	-1,1	1,4	1,6	1	-¼
P	2,8	4,5	3,3	1½	2¾
UK	1,4	3,6	3,0	3	3
EUR 12	0,9	2,3	2,1	1¾	1½
USA	1,1	1,6	-0,4	1	-¼
JAP	1,3	3,1	3,3	3¼	2½

⁽¹⁾ GNP for USA and Japan from 1987 onwards.⁽²⁾ Forecasts September to October 1988.⁽³⁾ EUR 9: Registered unemployed; GR, E, P: labour force sample survey.⁽⁴⁾ ESA definition of general government which includes social security funds.⁽⁵⁾ Deflated by the price deflator of private consumption.

Source: Commission services.

A. THE ECONOMIC SITUATION AND OUTLOOK

1. The external environment

The international economic environment and the economic situation in the European Community are characterized by a buoyancy in production activity and trade coupled with low recorded inflation rates that have not been seen for a long time. The years of structural adjustments in most industrial economies have made them more resilient. Despite the October 1987 stock-market crash and continuing concern about the international payments imbalances growth in industrial countries is strong (3,9 % in 1988). The delayed favourable effects of the oil price fall in 1986 and the rapid growth of monetary liquidity in 1987 (first through foreign exchange intervention and later in the year to assist financial institutions after October 1987) are all reflected in a growth performance which is better than that expected at the beginning of the year and is even accompanied by evidence of overheating in some countries. Despite some moderation, GDP growth in the OECD area should still be close to 3 % in 1989, the seventh year of continuing expansion in activity.

This favourable development has been common to all major industrialized countries. The American economy has been growing very strongly — though unevenly — since 1983. Capacity limits are now being reached in some industries and the unemployment rate is only slightly higher than during the 1960s. Yet, despite this and the massive dollar devaluation for over three years (March 1985 to March 1988: 38 % in effective terms), the rate of inflation in 1988 has remained at

about 4½ %. Monetary policy was tightened in early summer, following first signs of overheating of the economy. Some slowing down is likely to occur in 1989, given the somewhat less pronounced growth of both domestic demand and exports.

In Japan, domestic demand growth during the past 12 months has averaged almost 7½ % in real terms. At the same time, the Japanese economy seems to have adjusted to the considerable yen appreciation (March 1985 to March 1988), 60 % in effective terms) of the last three years and export prospects have improved. Thus, despite an expected deceleration of domestic demand growth in 1989, the Japanese economic performance will remain very strong.

Economic growth in the developing countries is likely on average to be in the range of 3,5 to 4 % in both 1988 and 1989. However, this average conceals great diversity. The Asian newly industrialized economies (NIEs), major exporters of manufactured products, continue to enjoy growth rates of GNP exceeding 7 %. Oil-exporting countries are only now recovering from the loss in export revenues in the wake of the oil price collapse of 1986. GDP growth of exporters of raw materials does not seem to have accelerated very markedly, despite the strength of activity in industrial countries and the substantial rise in non-oil commodity prices which increased at an annual rate of 17 % in the last six months of 1987 and 27 % in the first six months of 1988. This has brought a welcome improvement in the terms of trade of these countries.

TABLE 1

Real GDP, domestic demand and world trade

(annual percentage changes)

	I-1987	II-1987	I-1988	1987	1988 (¹)	1989 (¹)
(a) GDP						
EUR 12	2,5	3,5	3,8	2,9	3,5	2,8
USA	3,9	5,0	4,0	3,4	3,9	2,3
Japan	3,7	6,0	6,4	4,2	5,6	3,8
OPEC				0,0	1,1	2,6
Asian NIEs				11,8	8,5	7,5
Other NIEs				2,8	1,3	3,4
Other LDCs				4,0	5,0	4,6
(b) Domestic demand						
EUR 12	3,6	4,3	4,1	3,8	4,0	3,2
USA	2,8	4,8	2,5	3,0	2,8	2,0
Japan	3,9	7,7	8,9	5,1	7,4	4,2

(¹) September to October 1988 forecasts of the Commission services.

	I-1987	II-1987	I-1988	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
(c) <i>World trade</i>						
World imports (excluding EC)	0,6	11,6	7,0	5,0	7,6	5,7
EUR 12 export markets				6,2	8,2	6,1

⁽¹⁾ September to October 1988 forecasts of the Commission services.

For the European Community, the vigorous performance of the world economy represents a welcome stimulus to its own exports, which is reinforcing its own domestic-demand led economic growth. In fact, world imports (excluding the Community's export markets. Because of a faster expansion in 1988, which implies a considerable growth of the Community's export markets. Because of a faster expansion in imports net external trade will however continue to contribute negatively to GDP growth in the Community (for the third year in a row). Thus the international adjustment process will continue to take place at a relatively high level of growth in both trade and GDP.

The above developments have important consequences for the conduct of economic policy, particularly monetary policy. From 1985 up to early 1988, monetary authorities in the main industrial countries had generally attached a high priority to external goals in support of the international adjustment process. Exchange rate considerations therefore played an important role in the management of interest rates and of foreign exchange reserves. The climate changed in mid-1988. The dollar exchange rate stabilized when it became clear that the world economy had robustly resisted the impact of the stock-market crash and the international adjustment process was finally reducing the nominal United States trade deficit. (During the first eight months of 1988, the deficit ran at approximately US \$18 billion less than in the same period of 1987.) Markets eventually revised their appreciation of the economic climate, showing concern about higher price pressures. As the danger of a revival of inflation became apparent, domestic goals gained importance and monetary policy was somewhat tightened, at first in the United States. The restructuring of financial portfolios together with higher interest rates eventually triggered a recovery of the dollar in the second quarter of 1988.

By late September the dollar exchange rate was more than 10% higher than at the end of last year in effective terms (18% higher with respect to the deutschmark and 10% higher in relation to the yen) a little lower than the rate prevailing on average in the second and third quarters of 1987. In fact the dollar exchange rate *vis-à-vis* the main European currencies was at the beginning of autumn close to that prevailing at the time of the Louvre agreement of February 1987.

Central banks have reacted to the change of market sentiment about the US dollar and the more restrictive

United States monetary policy by selling dollars on the foreign exchanges and by raising short-term interest rates. In the context of faster-than-expected growth as well as a perceptible deterioration in the terms of trade, authorities in Germany and the United Kingdom considered this desirable for domestic reasons. But, in other Member States, fears have been manifested that the induced rise in interest rates could have a negative impact on growth (see C.2).

TABLE 2

Nominal short-term interest rates

(three month money market rates)

	End January 1988	End April 1988	End September 1988
Average EMS	5,7	5,7	6,8
D	3,3	3,4	5,3
UK	8,7	8,5	12,3
USA	5,8	6,1	7,5
Japan	3,9	3,9	4,1

The reduction of international current account imbalances is making progress, not only in real but also in nominal terms. Trade flows are adjusting to the new configuration of exchange rates and the resulting recovery in United States competitiveness. But the pace of the adjustment is slow. Moreover, up to now the geographical counterpart of the improvement in the United States deficit has largely not been located in the main surplus countries (Japan, Germany, and the Asian NIEs) but in other OECD or less-developed countries (LDCs). Certainly the bilateral positions of the first group of countries *vis-à-vis* the United States are deteriorating. But this is being compensated by an improvement of the trade balances in relation to their other trading partners as a whole. In the Community, in particular, the reduction in the overall surplus with the rest of the world therefore reflects rapidly deteriorating current account positions by Member States other than Germany, particularly those with faster domestic demand growth than the Community average.

TABLE 3

Current account balances

	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
(a) billion US\$					
EUR 12	18,4	50,4	42,4	24	16
USA	-116,4	-141,4	-154,0	-135	-131
Japan	49,2	85,8	87,1	79	86
OPEC	3,7	-26,4	-9,5	-21	-22
Asian NIEs	10,1	22,8	29,1	34	33
Other LDCs	-34,5	-32,4	-22,9	-27	-32
(b) as % of GDP ⁽²⁾					
EUR 12	0,7	1,3	0,8	1/2	1/4
USA	-2,9	-3,4	-3,4	-2 3/4	-2 1/2
Japan	3,7	4,3	3,6	2 3/4	3

⁽¹⁾ September to October 1988 forecasts of the Commission services.

⁽²⁾ GNP in USA and Japan.

Furthermore, on the assumption of current or forecast output trends, current policy and current real exchange rates, the adjustment process in the industrialized countries, particularly between the United States and Japan, could lose much of its impetus in late 1989 and beyond. The question thus arises of whether, on the basis of the forecast net export performance, the United States trade deficit is indeed being reduced at a pace sufficient to signal to markets that the current account imbalances will eventually be resolved without disruption.

In this regard, the continuing build-up of United States external indebtedness is of particular concern as a significant debt servicing cost will be added to the required United States payments adjustment. The longer the current account imbalance is maintained, the larger will be the improvement needed in the merchandise trade balance to compensate for the deterioration in the invisible account.

Economic policy in all major countries is therefore facing the well-known twin goals. The speed of international adjustment has to be sufficient to preserve confidence in the final outcome and thus maintain stability in foreign exchange and securities markets. From an international standpoint as well as from the Community's point of view a period of stability for the dollar at prevailing rates would be desirable. A renewed depreciation of the dollar will prevent the adjustment of real trade flows, which is currently under way, being reflected fully in further reduction of the nominal United States trade deficit because of higher import prices

(J-curve effect). Furthermore this would increase the inflationary risk in the United States which could also result in higher interest rates. On the other hand a further appreciation of the dollar would increase inflationary pressures in the economies of the trading partners of the United States and would threaten the continuation of the real adjustment process of the world economy. In order to support the adjustment process, the reduction in the United States current account deficit should go hand in hand with a reduction in the federal budget deficit. At the same time, monetary policy can no longer give exclusive priority to the international adjustment process, since, in the United States and several other countries, anxieties concerning inflation are gaining ground.

Furthermore, adjustment policies have to be accompanied by determined efforts to resist protectionist pressures and to promote world trade. The Uruguay round of multilateral trade negotiations provides the opportunity for such efforts. The ministerial meeting in Montreal in December must give political impetus to the negotiating process so that the Uruguay round can achieve effective liberalization of trade in goods and services. At the same time, all participants must continue to respect the standstill commitments entered into at the launching of the round; recent United States trade legislation causes concern in this respect.

With respect to the second major imbalance facing the world economy, the debt problem of the developing countries, the debt service/export ratio will probably increase in 1988,

particularly due to the recent rise in interest rates. Furthermore, the situation of the highly indebted Latin American and of some middle income African countries as well as the poorest African countries is still difficult and is likely to remain so, even in the medium term. These countries therefore continue to be vulnerable.

A medium-term solution to the debt problem of middle income countries continues to require adequate adjustment policies in the debtor countries, sufficient external financing as a complement to domestic resources, a continued favourable international growth environment and forms of debt reduction on a voluntary basis. For some of the poorest developing countries, the implementation of the Toronto summit's decision within the framework of the Paris Club and as a complement the conversion of official development assistance loans into grants as well as the result of the annual meeting of the IMF and World Bank in Berlin are encouraging.

2. The Community economy in 1988 and 1989

Like other major industrial countries, the economy of the European Community has shown a remarkable dynamism since the second half of 1987. This dynamism has been fuelled by a significant acceleration in investment. In 1988, average growth will be almost 3 1/2 %, the best performance since 1978/79: yet at that time inflation was on average three

times today's level. One has to go back more than two decades to find a combination of output growth and low recorded inflation as desirable as today. This performance is all the more remarkable in that it is following a steady and exceptionally long, though moderate, expansionary phase. Since 1981, average growth of real output in the Community has continued to accelerate and, since 1984, it has equalled or been above 2,5 %.

Prospects for 1989, on the whole, remain favourable. Growth could slow down slightly (from 3 1/2 % to 2 3/4 %) as the exceptionally favourable factors, particularly the mild winter of 1987/88, cannot be expected to recur. Furthermore the international environment is expected to be somewhat less favourable; private consumption could increase less rapidly due to a deterioration in the terms of trade; in some countries monetary policy and/or budgetary policy will have moderating effects. Yet the improvement in supply conditions and demand prospects will once again favour investment. Growth could slow down in countries like Spain, Italy and the United Kingdom who up to now have been the driving force of intra-Community trade. This should result in an alleviation of balance of payments and inflationary pressures. The impetus which these countries have given to economic activity is benefiting their Community partners, who are now picking up some momentum. In these circumstances, it should be possible to avoid a cyclical downturn, which would put a brake on investment, and an acceleration in inflation, equally prejudicial to the maintenance of sustained growth.

TABLE 4

Determinants of GDP growth in the Community of 12 (at constant prices)

	1984	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
— GDP growth at constant prices	2,4	2,5	2,6	2,9	3 1/2	2 3/4
— Contribution to growth of ⁽²⁾ :						
— net exports	+0,5	+0,1	-1,2	-1,2	-1	-1/2
— domestic demand (including stocks)	+1,9	+2,4	+3,8	+3,9	+4	+3 1/4
— Exports of goods and services (annual % change)	7,7	4,7	1,5	3,7	5 1/4	5 1/4
— Private consumption (annual % change)	1,4	2,5	3,9	3,8	3 1/2	3
— Gross fixed capital form. (annual % change)	1,3	2,1	3,1	4,6	7	5 1/4

⁽¹⁾ September to October 1988 forecasts of the Commission services.

⁽²⁾ Change as % of GDP of the preceeding year.

The structure of demand has changed over the recent past. In 1984 and 1985 growth was primarily led by exports. In 1986, this momentum came from an increase in private consumption following the improvement in the terms

of trade as a consequence of (i) the fall in oil prices and (ii) the appreciation of European currencies with respect to the US dollar. Since 1987, and to a greater extent in 1988, investment, whose rate of growth up to

now in the recovery has been relatively moderate, is tending to be the most dynamic component of domestic demand. It is equally important that the upturn in investment is occurring in all Community countries.

Many factors explain this upturn in business capital formation:

- (a) The economies of the industrialized countries are beginning to reap the benefits of structural policies and of greater adaptability of markets. The significant improvement in the profitability of capital and self-financing of enterprises, first induced by moderate wage developments, was accelerated in 1986 and 1987 by the reduction in energy prices as well as by the pick-up of sales.
- (b) Demand has been, and is expected to remain strong. In manufacturing industry the rate of capacity utilization is now reaching record levels in many countries. With capacity utilization higher than any time since the previous cyclical peak (1979), and the improved profitability, there is now evidence of a strengthening of capital formation and apparently a progressive and welcome shift from labour-saving to capacity-augmenting investment.
- (c) It is also possible that rising expectations in the business sector in relation to 1992 may be beginning to have a positive influence on investment trends. There has, in the course of 1988, emerged clear signs of a '1992 effect' in merger and take-over activity in the Community, and there are some tendencies for multinational companies to redirect investment location strategies in favour of the Community.
- (d) The improvement in the international environment and the acceleration in world trade have both helped to improve the business climate.

In general, inflation in the Community remains under control (+ 3 1/2 % in 1987 and 1988). It did, however, undergo an acceleration, partly due to exceptional or technical factors in some countries in recent months, notably the United Kingdom and Spain. Some pick up of inflationary expectations was noticed by the authorities in Germany, although from a very low level of recorded inflation. In addition, the disinflation process in Italy, after years of good results seems to be slowing down.

The perception of greater inflationary risks has a number of origins, but on the whole, the risk of renewed inflation in the Community in the months ahead should not be overestimated. This notwithstanding, vigilance is necessary, to different degrees in different countries, because the

sustained increase in spending and the higher rates of capacity utilization may combine elements of demand-pull and cost-push price pressure.

- (a) In the Community domestic prices are no longer benefiting from an improvement in the terms of trade, as was the case in recent years. The terms of trade have already deteriorated due to the effect of the recent appreciation of the dollar and the increase in raw material prices (excluding oil). Furthermore, average prices of non-oil raw materials, though only representing about 7% of Community imports, have undergone significant increases during the first half of 1988 (about + 27% in dollar terms). Yet, the recent new reduction in oil prices has to a large extent compensated for the increases in other raw material prices. According to forecasts the terms of trade will remain stable on average in the Community. The risk of a further deterioration will remain limited as long as exchange rates remain stable and there is no new significant increase in raw material prices.
- (b) The growth acceleration is accentuating the domestic price pressures, especially in those countries where the rate of capacity utilization has been quite high for some time (United Kingdom, Italy and Spain). In these countries, there is a risk that wage cost developments will contribute to additional cost pressures. Yet on average, in the Community, the increase in nominal unit labour costs should remain moderate throughout the forecast period.
- (c) During 1987, developments in world exchange markets and the large interventions employed to at least partly finance the United States current account deficit were accompanied by strong monetary expansion in Europe and Japan while monetary growth in the United States was very restrained. This move towards a more expansionary stance in Europe and Japan helped stabilize exchange rates and, after the October 1987 crash, the financial markets; to a certain extent it responded to an increase in desired liquidity holdings in a period of financial innovation, deregulation and decelerating inflation and it helped maintain growth. This effectiveness of the monetary policy measures was in no small part due to the credibility that the monetary authorities had built up over a number of years. The recent increases in short-term rates should moreover allow this credibility to improve further and show the determination of the monetary authorities to preserve their stability achievements. In addition these increases should bring a deceleration in the growth of the monetary aggregates.

The unemployment rate, which has fallen slightly since the middle of the decade still remains around 11 % of the active population. The faster rate of job creation has thus not been

fully reflected in a reduction in unemployment ⁽¹⁾. This is for several reasons — firstly the jobs created are not always suitable for the registered unemployed and secondly, since 1986, the participation rate has increased. Due to both these circumstances, despite more favourable

employment performances, the share of the long-term unemployed in the total number of unemployed continues to increase while youth unemployment still remains too high. Overall, despite the better growth dynamics in the Community unemployment remains the major problem confronting the European economy.

TABLE 5
Unemployment rate

	1973	1979	1982	1985	1988 ⁽¹⁾	1989 ⁽¹⁾
EUR 9 ⁽²⁾	2,4	5,2	9,3	11,1	10,5	10,1
EUR 12	:	:	9,4	11,8	11,3	10,9
USA	4,9	5,8	9,7	7,2	5,5	5,5
Japan	1,3	2,1	2,4	2,6	2,5	2,6

⁽¹⁾ September to October 1988 forecasts of the Commission services.

⁽²⁾ The Community excluding Greece, Spain and Portugal.

3. Convergence, stability and growth

The average Community increase in growth since the beginning of this decade has been accompanied by greater convergence towards lower inflation rates. But significant divergences are persisting with respect to budgetary positions. New ones are developing in the field of external balances of Member States.

As expected, the convergence of inflation rates of those countries participating in the EMS exchange rate mechanism is particularly significant. No country participating in the exchange rate mechanism has an inflation rate above 5 %. This is also true for Spain and the United Kingdom, so that the major gap between the participating and non participating countries has closed significantly. Portugal and Greece however continue to experience inflation rates sharply in excess of the Community average.

TABLE 6
Convergence of inflation rates

	1980	1984	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
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(a) *Weighted average*

EUR 12	13,5	7,1	3,6	3,3	3,5	3,7
ERM ⁽²⁾	12,0	6,5	2,4	2,5	2,7	3,1
Non-ERM ⁽²⁾	17,0	8,5	6,6	5,2	5,2	5,1

(b) *Maximum and minimum inflation rates within the ERM ⁽²⁾*

Maximum	19,6	11,4	6,1	4,8	4,9	4,6
Minimum	6,0	2,0	-0,2	-0,4	0,9	1,3
Difference	13,6	9,4	6,3	5,2	4,0	3,3

⁽¹⁾ September to October 1988 forecasts of the Commission services.

⁽²⁾ Countries participating/non-participating in the exchange rate mechanism of the EMS.

⁽¹⁾ See Chapter B.3.

This convergence of inflation rates has allowed monetary cohesion in the Community to strengthen. Bilateral parity adjustments in the EMS have become less frequent. No realignment has taken place since January 1987. The greater convergence first created a solid base for the strengthening of the EMS mechanism with the Basle/Nyborg accords; since then, the agreement itself has strengthened the EMS. This makes new advances in the monetary area possible. An enlargement of the number of countries participating in the exchange rate mechanism is desirable, at the appropriate time.

Up to 1985 this convergence was achieved in spite of the strong revaluation of the dollar. Since 1986 it was assisted by the oil price fall and the devaluation of the dollar. This development has been rapidly internalized in a slower increase in internal costs. However, the downward convergence in inflation fundamentally reflects the greater consensus in the European economies regarding the objective of stability. The concentration on this objective has made monetary policies more and more compatible with each other. In addition, nominal wage developments have supported the disinflation process. Even if the convergence of budget deficits remains insufficient, their increasingly non-monetary financing has largely contributed to the process of disinflation. However, this has been achieved at the price of a rapid increase in public debt and very high interest rates in high deficit countries.

The downward convergence of inflation rates has not been fully reflected in a downward convergence of nominal

interest rates. Among the countries participating in the exchange rate mechanism, for example, the average money market rate in Germany for the first nine months of 1988 was 2,6 points lower than in Belgium, 4 points lower than in France and 7,3 points lower than in Italy, even though the rates of inflation in Belgium and France are almost equal to that of Germany, and in Italy it is only about 2,5 points above. Similar differences exist with respect to the long-term interest rates in the different countries.

This can have several origins: (a) a more or less longstanding tradition of stability which goes hand in hand with a more or less rapid reduction of medium-term inflationary expectations; (b) a differential evolution of fundamentals notably budget and external balances which nourish expectations of inflation or exchange rate changes.

In fact, in these two areas, budget deficits and external balances, important divergences persist or are developing. These divergences are a potential source of instability for exchange rates, even if, in the short term, it is always possible to compensate for these effects by intervention and by appropriate interest rate differentials. They increase the risk of conflict between the domestic objectives of monetary policy and the exchange rate discipline of the EMS. In addition, the divergent external balances could make it more difficult to define a common position *vis-à-vis* third currencies, notably the dollar.

TABLE 7

Convergence of net general government borrowing (–) or lending (+)

	1980	1984	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
	(% of GDP)					

(a) *Weighted average*

EUR 12	—	– 5,3	– 4,8	– 4,2	– 3,8	– 3,4
ERM ⁽²⁾	– 4,0	– 5,4	– 5,0	– 4,8	– 4,5	– 4,1
Non-ERM ⁽²⁾	—	– 5,1	– 4,1	– 2,9	– 2,1	– 2,1

(b) *Maximum and minimum within the ERM*

Maximum	– 8,5	– 11,5	– 11,4	– 10,5	– 10,0	– 10,0
Minimum	– 0,8	– 1,9	+ 3,1	+ 2,1	+ 0,9	+ 1,4
Difference	7,7	9,6	14,5	12,6	10,9	11,4

⁽¹⁾ September to October 1988 forecasts of the Commission services.

⁽²⁾ Countries participating / non-participating in the exchange rate mechanism of the EMS.

The significant differences in the budgetary positions of Member States are being reduced only slowly in 1988. Even if these differences in the level of budget deficits are

accompanied by different household saving behaviour, they nevertheless complicate the task of monetary policy in the pursuit of the objectives of internal and external stability.

TABLE 8

Gross household saving and net borrowing (–) or lending (+) of general government in 1987

(% of GDP)

	B	DK	D	GR	E	F	IRL	I	L	NL	P	UK
— Saving	9,8	11,1	7,8	12,9	8,0	8,3	13,6	20,1	9,0	9,0	22,8	3,5
— Net borrowing of general government	–7,2	+2,1	–1,8	–9,5	–3,6	–2,5	–9,1	–10,5	+5,2	–6,3	–8,4	–1,4
— Difference	2,6	13,2	6,0	3,4	4,4	5,8	4,5	9,6	14,2	2,7	14,4	2,1

Excessive public debt as a percentage of GDP also carries with it serious drawbacks and is creating problems for monetary cohesion and the conduct of monetary policy. (a) It is contributing to the maintenance of high real interest rates prejudicial to productive investment and the pursuit of sustained growth. (b) The share of irreducible interest repayments in public expenditure is increasing and is reducing the room for manoeuvre for the necessary restructuring in favour of productive expenditure and a reduction in direct tax rates. (c) The credibility of stabilization policies may eventually be affected, this is also increasing the risk premium on long-term interest rates. It is therefore essential for those countries where the budget deficit is still excessive that they follow medium-term strategies to allow them to regain sustainable budgetary positions.

The evolution of external balances presents both a positive and a disquieting aspect. All of those countries, with

the exception of Greece, who in recent years had worrying external positions, as at the beginning of this decade did Belgium, Ireland, Portugal and, more recently Denmark, have experienced a significant improvement.

But a significant divergence between the external balances of the countries participating in the EMS exchange rate mechanism and the others is developing; furthermore, within the exchange rate mechanism, the gap between the surplus and deficit countries is growing particularly as the German surplus is not yet declining. Simultaneously, intra-Community trade imbalances are widening. In particular, between 1985 and 1987 the intra-Community trade surplus (excluding energy) of Germany increased by about ECU 10 billion and the intra-Community trade deficit of France deteriorated by about ECU 3,8 billion.

TABLE 9

Convergence of external balances of current transactions

(% of GDP)

	1980	1984	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
(a) <i>Weighted average</i>						
EUR 12	–1,2	0,3	1,3	0,8	0,5	0,3
ERM ⁽²⁾	–1,7	0,5	2,0	1,5	1,5	1,6
Non-ERM ⁽²⁾	0,2	–0,2	–0,2	–0,4	–2,3	–3,0
(b) <i>Maximum and minimum within the ERM ⁽²⁾</i>						
Maximum	–1,3	4,2	4,4	4,0	4,0	4,2
Minimum	–11,8	–6,0	–5,2	–3,0	–2,5	–2,3
Difference	10,5	10,2	9,6	7,0	6,5	6,5

⁽¹⁾ September to October 1988 forecasts of the Commission services.

⁽²⁾ Countries participating / non-participating in the exchange rate mechanism of the EMS.

	1980	1984	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
(c) Average of ERM ⁽²⁾ surplus and deficit countries in 1988						
Surplus countries ⁽³⁾	—	—	4,0	3,6	3,6	3,8
Deficit countries ⁽³⁾	—	—	0,0	-0,4	-0,3	-0,4
Difference	—	—	4,0	4,0	3,9	4,2

⁽¹⁾ September to October 1988 forecasts of the Commission services.

⁽²⁾ Countries participating / non-participating in the exchange rate mechanism of the EMS.

⁽³⁾ Surplus countries: B, D, IRL, L, NL; deficit countries: F, I, DK.

The existence of such imbalances in the medium term is partly the corollary of the catching-up process of the poorest countries, where the need for and the capacity of investment are relatively stronger. Deficits in these countries are sustainable in the medium term on condition that the deterioration of the current balance corresponds on the domestic plane to a strengthening of productive investment and goes hand in hand with sound external financing. This for example is the case in Spain and Portugal where the

deterioration in current transactions has accompanied a strong uptake in productive investment financed by private capital inflows. Hence, the level of deficits in these two countries remains sustainable. Furthermore, it is normal and even desirable that countries with a higher level of development experience surpluses on their current accounts and export capital to the less prosperous countries in which investment will be fostered and the catching-up process assisted.

TABLE 10

Growth in GDP and domestic demand

	(% of GDP)				
	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
(a) GDP growth					
EUR 12	2,5	2,6	2,9	3½	2¾
ERM ⁽²⁾	2,2	2,5	2,2	3¼	2¾
Non-ERM ⁽²⁾	3,2	3,0	4,3	4	3
(b) Growth in domestic demand					
EUR 12	2,3	3,8	3,8	4	3½
ERM ⁽²⁾	2,1	3,7	3,3	3¼	2¾
Non-ERM ⁽²⁾	3,0	4,3	5,8	6½	4

⁽¹⁾ September to October 1988 forecasts of the Commission services.

⁽²⁾ Countries participating / non-participating in the exchange rate mechanism of the EMS.

Since 1984, the evolution of the relative external positions between the exchange rate mechanism participating countries and those not participating appears mainly to be associated with growth differentials. On average for the four countries not participating in the exchange rate mechanism, domestic demand will have risen by about 21% between 1984 and 1988 as against 13% for their partners in the exchange rate mechanism.

On current trends, the growth dynamic as it is now taking shape in the different countries in 1989 is a first step towards renewed equilibrium. The growth differentials between those countries participating in the exchange rate mechanism and those not participating are narrowing. However, for the latter group of countries, the growth of domestic demand remains significantly above that of GDP, which indicates that the external balance will continue to deteriorate in terms of

constant prices. On the other hand, the external balances (in constant prices) of those countries participating in the exchange rate mechanism, with the exception of Italy, will scarcely deteriorate or may slightly improve. Two factors help to explain this contrasting evolution: (a) The EMS countries are continuing to benefit from a sustained expansion of imports of their partners where domestic supply is beginning to be constrained by a relatively higher rate of capacity utilization. (b) The acceleration in productive investment throughout the Community and the world is particularly profitable for countries like Germany who are traditional exporters of equipment goods.

Between the countries participating in the exchange rate mechanism, the evolution of domestic demand generally played a less important role. The increase in domestic demand in four countries, Belgium, France, Germany and the Netherlands, between 1984 and 1988 was between 10,5 and 13 %. It was stronger in Italy (about 17 %). In Ireland and Denmark, domestic demand needed to be controlled in order to improve the serious external position. During this period, the evolution of real effective exchange

rates of the different countries *vis-à-vis* their EMS partners remained more or less stable, or, in particular with the effective appreciation in the exchange rate of the Deutschmark, they played a role in the direction of reestablishing equilibrium in external positions.

Despite the marked differences in current account positions of ERM countries, the EMS exchange rate mechanism has remained relatively stable due to capital flows and better monetary policy coordination but this could change depending on market expectations and reactions to increasing imbalances. But in order to maintain the current growth dynamic in the Community and at the same time reduce these imbalances it is necessary that the growth process in the EMS surplus countries and particularly in Germany remains or becomes increasingly led by domestic demand. Recent economic developments in Germany suggest that this is already under way. In addition to contributing to a reduction in payments imbalances it would also assist the growth and investment process in these countries and increase stability within the EMS. Furthermore it would allow the Community to make a greater contribution to the international adjustment process.

B. PROBLEMS, OPPORTUNITIES AND CHALLENGES IN THE COMMUNITY ECONOMY

The economic situation has improved considerably. This situation, the most favourable for a long time, is giving the Community the chance to realize to a greater extent and more quickly its fundamental objectives: preparing for 1992, strengthening economic and social cohesion and reducing unemployment.

The internal market programme will in itself give or is even already giving a strong impetus to productivity and growth. But as enterprises prepare themselves to face new realities, output patterns, geographical location and the utilization of factors of production will change. Therefore, while the ultimate benefits of 1992 in terms of growth and employment have been estimated to be significantly positive, there is some concern, especially about the transition towards the completion of the internal market. These uncertainties will be better overcome the more that the achievement of the internal market is accompanied by policies resolutely oriented towards growth and employment as well as towards a reinforcement of economic and social cohesion in the Community.

1. Exploiting the potential of the internal market

In the course of the last year, the programme to complete the internal market by 1992 made considerable progress in relation to (i) the understanding of the size and nature of the potential economic gains that it offers as well as to (ii) the

legislative actions needed for its implementation. Both are reflected in the heightened awareness and expectations of the private sector.

The legislative actions have been numerous. In the area of finance, the Council has agreed on a timetable and procedure for eliminating capital controls in all Member States. Agreements were also reached on opening the non-life insurance market for larger risks. Commission proposals for the banking sector have been tabled and proposals for securities markets are under preparation. Progress has been made in the areas of public procurement, transport services and technical norms. Measures for the approximation of indirect taxes are under discussion.

Completion of the large internal market is first and foremost a huge programme for improving supply-side conditions, whose success will be effected by markets and firms, that is at the microeconomic level. Studies completed in the last few months show that the realization of the internal market will result in considerable gains for the Community in terms of potential GDP growth⁽¹⁾. These gains will arise from a number of sources: reduced production costs following the abolition of barriers affecting trade; better exploitation of economies of scale due to the increased market size which will also facilitate the development of larger and therefore

⁽¹⁾ Notably 'The Costs of Non-Europe', researches published in *European Economy* No 35, March 1988, under the title 'The Economics of 1992'.

more competitive European firms; greater efficiency within firms; reduced monopoly power and more dynamic investment and innovations as a result of increased competition and budgetary savings resulting from the opening of public markets.

These potential benefits can only accrue if a rigorous competition policy is implemented to ensure (i) that the positive effects of greater competition are not diminished by State aids and subsidies and (ii) that the free movement of goods and services is not impeded by individual firms in a dominant market position or by groups of firms acting in concert to restrict such competition.

Due to their size, the microeconomic gains will have significant macroeconomic consequences, which in particular depend on the reaction of firms and consumers. For example, faced with cheaper inputs and factor productivity gains, firms could reduce prices to their customers (consumers, firms or public administrations) or increase wages. They could use their additional profits to reduce their indebtedness more quickly or to self-finance their investments. Consumers could react to a higher level of real income by raising the savings ratio or by increasing consumption.

The studies mentioned above confirm that the reactions of the private sector to the completion of the internal market notably by an increase in investment will, in the medium term, allow the achievement of a significantly higher level of GDP and employment and lower inflation. But much depends on the way in which the public authorities react to the easing of the macroeconomic constraints, notably the reduction of the budget deficit, the improvement in the external position and a slowdown in inflation. It seems essential in this respect that the budgetary room for manoeuvre created by the internal market will be used (i) in those countries where the budgetary situation remains difficult, to reduce more rapidly the budget deficit and (ii) in the other countries it should be actively used to improve the conditions of supply and demand by reducing the tax burden and increasing economically profitable public investment.

In this way, the productivity gains resulting from the completion of the internal market, at the macroeconomic level, can be accompanied by an even greater acceleration in GDP growth so that a favourable development in employment can take place. In such a context the increase in total demand can remain sufficiently dynamic and profitability of investment sufficiently high. Better macroeconomic conditions for growth and the completion of the internal market will thus reinforce each other.

It would not, however, be opportune to wait for the 1992 deadline to strengthen the consensus on the macroeconomic policies required for the European economies to increase potential output and sustain growth. In fact:

- Firms are already incorporating the 'internal market' factor into their strategies. The more that they can rely on macroeconomic policies being defined in clear and credible terms, the more energetic they will be in doing so.
- Restructuring at firm, sectoral and market level, already underway, is necessary if the productivity gains expected from the internal market are to be achieved. In the context of slow growth, it is possible that this could lead to job losses initially. This risk could be avoided and new jobs could more than compensate for the job losses due to restructuring by maintaining the Community economy on a sufficiently dynamic growth path. The inertia and opposition to the necessary restructuring will be easier to overcome the more the realization of the 1992 objective results in an increase in employment and a reduction in unemployment. The acceleration of growth and employment observed in 1988 puts this problem in a favourable light — a growth dynamic that needs to be maintained and strengthened over the medium term.

These various movements in the public and private sectors confirm that the 1992 programme has achieved, in the words of the European Council of Hanover, the stage of irreversibility. The rising awareness of the private sector still, however, must continue to be translated into even-stronger growth of investment and thence the capacity for faster non-inflationary growth. It may be expected that this will follow, on condition that the public authorities ratify these expectations with (i) further agreements in the next 12 months on several important outstanding proposals in the 1992 programme, (ii) complementary actions in several associated domains, such as structural, social and external trade policies, and (iii) support for a consistent, growth-oriented macroeconomic policy.

2. Towards greater economic and social cohesion

The strengthening of economic and social cohesion in the Community as well as the improvement in living and working conditions of the workforce are objectives of the Community as confirmed by the Single European Act (Articles 130 A and 117). This is why particular attention should be accorded to the regional and social dimension in the face of the changes which will occur in the European economies in the coming years.

2.1. Narrowing income gaps within the Community

The income gap between citizens from the various countries and regions of the Community is a complex and pressing issue. This catching-up process is, in its own right, one of the more fundamental economic and social objectives of the Community. Historical experience shows that it is possible to reduce in a significant way the per capita GDP disparities, measured in purchasing power standards (PPS), which exist between the different regions and countries. For example, between 1960 and 1973, the gap between the four poorest countries of the current Community of Twelve and the four

richest narrowed by about one-third. It widened again following the first oil shock. But since mid-1980, this gap has again tended to narrow, in particular because of good growth performances in Spain and Portugal. Moreover, the disparities in GDP per head between the different regions within countries are very large. Such disparities exist in all countries. For example in Italy, the GDP per head is almost equal to the Community average, but that of the southern regions is 30 % below while that of the north-western regions is 30 % above. In these conditions, the strengthening of economic and social cohesion of the Community also necessitates a convergence towards the higher levels of GDP per head between regions within countries.

TABLE 11
Ratios of per capita GDP (PPS) in the Community ⁽¹⁾

	1960	1975	1985	1987	1988 ⁽²⁾	1989 ⁽²⁾
Four poorest countries ⁽³⁾ over four richest countries ⁽⁴⁾	0,41	0,64	0,58	0,60	0,61	0,61
Four poorest countries over average for EUR 12	0,52	0,71	0,66	0,67	0,67	0,68
Eight richest countries over average for EUR 12	1,10	1,06	1,08	1,08	1,08	1,08
Index of GDP per head at constant prices (EUR 12)	100	166	200	210	217	223

⁽¹⁾ All statistics have been calculated on the basis of the current 12 Member States.

⁽²⁾ September to October 1988 forecasts by the Commission services.

⁽³⁾ Greece, Spain, Ireland, Portugal.

⁽⁴⁾ The composition of this group is variable and depends on the level of per capita GDP (PPS) in the year indicated.

The trend differences in GDP and population growth imply that in the period immediately ahead no more than a small reduction in the disparity of average *per capita* incomes can be envisaged. An extrapolation of the trends of recent years, not taking into account the effect of the doubling of the Structural Funds, suggests that in 1992, average *per capita* GDP in the four poorest countries will still represent only some 65 % of average *per capita* GDP in the four richest countries (against 60 % in 1987).

The average GDP per head is not the only criterion by which the degree of economic and social cohesion can be measured,

even if it is the main one. In the area of unemployment, significant disparities exist not only between Community countries but also between regions. In Spain and Ireland, for example, unemployment stands at around 20 % of the active population compared to a Community average of 11 %. Furthermore, certain regions in southern Italy as well as in central and northern Europe are particularly affected by unemployment. It is also clear that high levels of underemployment of the workforce are often related to, if not the cause, of lower per capita GDP. The catching-up process should therefore be accompanied by a downward convergence of unemployment rates.

TABLE 12

Macroeconomic adjustment indicators in the poorest countries

	Inflation rate (Private consumption)		Balance of current transactions with the rest of the world as % of GDP		Real unit labour costs (Index)	
	1981	1988 ⁽¹⁾	1981	1988 ⁽¹⁾	1981	1988 ⁽¹⁾
GR	23,4	13 ¹ / ₄	- 0,7	- 2 ³ / ₄	100	100,0
E	14,3	4 ³ / ₄	- 2,7	- ³ / ₄	100	86,0
IRL	19,6	2	- 14,7	2 ¹ / ₂	100	90,5
P	23,3	9 ¹ / ₂	- 12,2	0	100	83,8
EUR 4	16,8	6 ¹ / ₄	- 4,3	- ³ / ₄	100	88,0
EUR 8	11,4	3	- 0,4	¹ / ₂	100	94,0
EUR 12	12,1	3 ¹ / ₂	- 0,7	¹ / ₂	100	93,2

⁽¹⁾ September to October 1988 forecasts of Commission services.

The less-favoured countries, in particular Spain, Portugal and Ireland, have in recent years made major strides in adjustment and consolidation: a fact which in itself should accelerate the narrowing of the gap. In Greece also some favourable developments have taken place but to a lesser extent. Inflation in Ireland (2 % in 1988), for example, is now less than the Community average and in Spain (4¹/₂ %) it is just one percentage point above. Taking the four countries together: the inflation rate has declined by 11 percentage points since 1981; the balance of current transactions is now close to equilibrium (- ¹/₂ % of GDP) after having been well in deficit (- 4,3 % of GDP) in 1981; the adjustment of real unit labour costs has been particularly large, falling by about 12 % since 1981 compared to some 6 % on average in the Community.

The Decision of the European Council held in Brussel on 11 to 12 February 1988 to double the budgetary commitments of the Structural Funds between 1987 and 1993 show the Community's determination to make an active contribution to the catching-up process of the less-favoured countries and regions. The subsequent adoption by the Council of a framework Regulation on the tasks of the funds and their effectiveness and cooperation with the operations of the European Investment Bank establishes the main operating principles (Regulation (EEC) No 2052/88) ⁽¹⁾. This Regulation sets out in particular a new model for the 'partnership' between the Community and Member States intended to ensure that the funds contribute effectively to the objectives of economic and social cohesion.

The Community resources together with appropriate structural and macroeconomic policies can make an

important contribution to the acceleration of the catching-up process. In fact, the increased Structural Funds and financial instruments could represent in Greece, Portugal and Ireland 4 to 5 % or even more of GDP. In Spain and Italy, they would represent a smaller percentage of national GDP, but concentrated on the poorest regions they will represent a similar percentage of the GDP of these regions. This opportunity must be seized by the beneficiary countries. In this regard, paying due attention to the effective use and additionality at programme level in the allocation of these resources to priority development needs is necessary but insufficient.

At the macroeconomic level the community support alleviates the balance of payments constraint of the recipient countries. The overall influence on medium-term economic growth essentially depends on the capacity of the recipient countries to attract private capital by credible management of economic policy and greater returns on investment and on the domestic counterpart to the easing of the external constraint. If this counterpart is found in an increase in the share of consumption in GDP in the countries concerned, the overall effect will be limited and the chance to fully exploit the opportunities offered will be missed. If, on the other hand, the macroeconomic counterpart of the increase in these Community resources is an equivalent increase in the investment share and an improvement in the efficiency of investment, the doubling of the Structural Funds will deliver its full benefits. In reality, micro- and macroeconomic behaviours are interdependent. There is no incentive for firms to invest more, unless profitability (and therefore also productivity) is high; otherwise the increased transfers would mainly lead to a substitution of sources of finance. Similarly, a dynamic environment broadens the range of opportunities available for more productive investment and better returns.

⁽¹⁾ OJ No L 185, 15. 7. 1988, p. 9.

By easing the resource constraint both internal and external, the doubling of the Structural Funds creates the initial condition for a sustainable resumption of the catching-up process. It is therefore necessary that the less-favoured countries continue with and strengthen the implementation of bold adjustment policies so as to gain the maximum benefit from the resources assigned to them to reduce economic disparities.

2.2. *The social dimension of the internal market*

Catching-up in economic terms must go hand in hand with catching-up in social terms, while maintaining basic social standards in the more advanced countries. Thus, apart from its regional aspects, the social dimension of the internal market is essential. Three elements are important in this respect: (i) the social effects of the completion of the internal market; (ii) the convergence in the improvement of living and working conditions of the workforce (Article 117 of the EEC Treaty); and (iii), social dialogue.

The productivity gains which will flow from completion of the internal market will also entail structural changes in markets and firms. Policies must be implemented which take account of the social effects of this restructuring. In this respect investment in the best resource available to the Community, its people, is essential. A greater emphasis on vocational and in service training will make it easier for the employed to meet these changes and for the unemployed to re-enter working life.

The completion of the internal market will intensify competition between firms of countries with quite different working and social conditions. These differences largely correspond to levels of productivity and capital efficiency which vary just as widely. In these circumstances, it is essential first to create economic conditions which will engender an upward convergence of social standards. The lower real wage levels and less onerous social regulations in the less advanced countries are comparative advantages which enable them to make progress in the catching-up process. In addition, minimum health and safety standards at work and the pursuit by Member States according to Article 118 A of the EEC Treaty of the objective of harmonizing conditions in this area, while maintaining the improvements already made, will contribute to better working and living conditions as well as to the avoidance of distortions in competition between the firms of different Member States. In this context, greater job mobility with maintenance of benefits when changing jobs as well as other guaranteed rights should also be sought.

Strengthening the social contract at the enterprise level could include rights for workers to be involved in the running of their companies and in sharing the benefits arising from higher productivity, broader-based management and a better climate at the work place. In this regard, attention should be given to the advantages that could arise from the adoption by firms on a voluntary basis of a European company statute, allowing companies to operate across the frontiers without violating existing corporate laws and which foresees the implementation of worker participation schemes in the countries concerned.

In the framework of the social dialogue at Community level the social partners have on several occasions in the last few years expressed their support for the general thrust of economic policy of the Community. This agreement represents a precious achievement. This consensus must now be strengthened if the remaining tasks are to be accomplished successfully. As provided for in Article 3 of Council Directive 74/121/EEC of 18 February 1974 on stability, growth and full employment in the Community ⁽¹⁾, the Governments of the Member States, according to their own arrangements, should confer with the representatives of the main economic and social groups on the broad lines of economic policy. The contribution of the social partners in the area for which they are competent is vital to the shaping of the social dimension of the internal market. For its part, the Commission will continue to contribute to the development of Community level dialogue between management and labour which, according to Article 118 B of the Treaty establishing the European Economic Community as amended by the Single European Act, could lead to relations based on agreement, if the two sides consider it desirable. In this respect the development of closer cooperation between the social partners of different Member States in bordering regions could be an encouraging first step towards an awareness of the European dimension in industrial relations.

3. Towards higher employment growth

Unemployment remains the major challenge for the Community. It more than doubled during the 1970s, from 2,8 million in 1973 to 7,1 million people in 1979 (from 2,4% of the labour force to 5,2%). It has doubled once again between 1979 and 1985, now extending, despite a slight fall in 1988, to 15,4 million people or 11,3% of the labour force (see Table 5 in A. 2). Furthermore long-term unemployment continues to grow and already exceeds 50% of total unemployment. The rate of youth unemployment, on average in the Community, is still over 20%. Thanks to the stronger net supply of jobs, the trend of unemployment which has been rising for over two decades gradually started to be reversed in 1987, although experience differs quite markedly among Member States.

Since 1985 the annual rate of employment creation in the Community on a per capita basis reached a historically high level (close to 1%). The volume of employment has

⁽¹⁾ OJ No L 63, 5. 3. 1974, p. 19.

increased less, however, since much of the increase has taken the form of part-time employment. In 1988 employment creation remains above the Community average in countries such as Spain (2,6%), the United Kingdom (1,9%),

Luxembourg (1,7%) and Portugal (1,7%). Longer-lasting and more sustainable growth (than that experienced in the 1970s) is thus also becoming even more employment-creating.

TABLE 13

Economic growth and employment

(annual average rates of change, in %)									
	$\frac{1973}{1960}$	$\frac{1975}{1973}$	$\frac{1979}{1975}$	$\frac{1984}{1979}$	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
<i>EUR 12</i>									
GDP	4,8	0,4	3,4	1,2	2,5	2,6	2,9	3,4	2,8
employment	0,3	-0,4	0,3	-0,5	0,6	0,8	0,9	1,1	0,9
<i>USA</i>									
GDP	4,0	-0,9	4,1	2,4	3,1	3,0	3,4	3,9	2,3
employment	1,9	-0,5	3,6	1,3	2,4	1,7	2,6	2,3	1,6
<i>Japan</i>									
GDP	9,6	0,7	5,1	3,9	4,5	2,4	4,2	5,6	3,8
employment	1,3	-0,1	1,0	0,9	0,7	0,9	1,0	1,0	0,8

⁽¹⁾ September to October 1988 forecasts of Commission services.

This performance is nonetheless still unsatisfactory in at least two respects (i) when compared with that of other industrialized countries and (ii) when compared to Europe's own post-war history. For example in the United States and Japan, the rate of job creation has been adequate to restore or to maintain an unemployment rate very close to the one prevailing a decade ago, before the second oil shock. Therefore, by international standards, Europe has a long way to go.

While other industrialized countries are approaching full employment, a mechanical extrapolation of the growth trend of the years prior to 1988 suggests that the unemployment rate in 1992 in the Community would not be much below one-tenth of the labour force. Unemployment represents an under-utilization of the labour resource. This resource must be transformed into a basis for growth as it was in the post-war period. About 15 to 18 million people engaged in agriculture with low marginal productivity and low incomes moved into industry and services where pay was better. Thanks to the realized rapid growth of income and to the strong development of trade and innovation, the resulting capital accumulation turned into jobs, demand and even faster growth.

The development of unemployment has been affected by changes in demography and participation rates. These two factors have moved in opposite directions. The annual increase in the population of working age (15 to 64) in the

Community on the one hand has certainly slowed down from 1% at the beginning of the 1980s to 1/4% today, but it will still contribute to a growing labour supply in the near future. Overall participation rates of the population of working age in the Community on the other hand declined between 1975 and 1985 from 64,4% to 63,3%, due to a marked decline in male participation from 87,5 to 80,8%, which outweighed the steady increase in female participation from 45,3 to 49,0%. Thus the overall decline in participation has slowed down somewhat the increase in unemployment. In recent years, however, male participation appears to have stabilized while female participation seems to continue its upward trend. Therefore overall participation is now recovering. This is a positive phenomenon, but it renders the reduction of unemployment in the Community more difficult.

Differences between participation rates in Member States are vast; they range from 53% in the Netherlands to more than 83% in Denmark. This is to a large extent due to wide discrepancies in female participation, where Spain with only 34% and Denmark with more than 78% (in 1986) provide the extreme cases. Furthermore, the estimated overall Community participation rate of 64 1/4% in 1988 is significantly lower than in other industrialized countries (e. g. 72 1/2% in Japan, 76% in the USA, 82 1/4% in Sweden and 70 1/4% in the OECD average ⁽¹⁾).

All this indicates that with regard to labour supply there is a significant potential for stronger and sustained economic growth in the Community. The increase in employment in general and in particular the growing willingness of women to seek employment could also provide a broader basis for the sharing of the burdens of taxation and social security, which will become more and more important in the medium and longer term to compensate for the ageing of the Community's population. To take full advantage of this potential, employment growth must be centre stage in the Community's economic policy.

In order to appreciate recent developments in the Community's labour market three points deserve particular attention.

First, the process of sectoral change continues. Employment in agriculture is declining further; it now provides only 8 % of total Community employment. Industry has also continuously shed employment for more than a decade. Today, with higher overall growth rates, this seems to have come to an end. The current expansion of net employment is, however, still provided virtually by the service sector alone.

TABLE 14

Employment creation by sector in the Community

	1974 ⁽¹⁾ 1958	1986 1974	1987	1988 ⁽²⁾	1989 ⁽²⁾	Shares in total employment in		
						1958	1974	1986
Agriculture	-4,4	-3,0	-2,0	:	:	22,8	11,5	8,1
Industry	0,5	-1,7	-0,0	0,2	0,2	39,1	39,5	32,5
Services	1,7	1,6	2,1	:	:	38,1	49,0	59,4
Total	0,2	-0,1	0,9	1,1	0,9	100	100	100

⁽¹⁾ EUR 5: Belgium, Germany, France, Ireland, Italy.

⁽²⁾ September to October 1988 forecasts of Commission services.

Second, part-time work has increased considerably and continues to do so. On average, for the Community, part-time employment as a proportion of total employment has increased to about 14%. In the past few years three-quarters of the net employment created in the Community has been part-time. Recent information concerning Spain confirms that an even higher proportion of new jobs created since early 1987 have been part-time in nature. The increase in part-time employment, to the extent that it is voluntary, is a sign of a healthy labour market. To the extent, however, that it is involuntary (13 % of all

part-time employed, according to the 1986 Community labour force survey) it indicates a degree of under-employment.

Third, an indicator of progress made in the Community towards achieving healthier labour markets is the relative evolution of real per capita labour costs and productivity (real unit labour costs). On average, this ratio has fallen in the Community, by over 6 % since 1981. This fall has been particularly large in the poorest countries (except for Greece, see B.2.1).

TABLE 15

Real unit labour costs ⁽¹⁾

(index 100 in 1981)

	1960	1973	1981	1988 ⁽²⁾	1989 ⁽²⁾
EUR 12	96,0	97,0	100	93,2	92,8
EUR 4 ⁽³⁾	92,5	94,3	100	88,0	87,7
EUR 8 ⁽³⁾	95,5	97,1	100	94,0	93,5

⁽¹⁾ Real per capita labour costs divided by productivity (GDP over total employment).

⁽²⁾ September to October 1988 forecasts of Commission services.

⁽³⁾ EUR 4: Greece, Spain, Ireland, Portugal; EUR 8: other Member States.

⁽¹⁾ OECD, Economic Outlook, June 1988.

This trend in real unit labour costs is favourable for a variety of reasons. First, it helps to boost profitability of fixed capital and hence to set an important precondition for a higher propensity to invest. The decline in real unit labour costs indicated in Table 15 also implies that the share of profits in value added has developed very favourably which does, however, not represent a proportionate increase in profitability. Because today a larger amount of capital is required per person employed, profitability of capital has not yet regained the level of the 1960s, a period of almost full employment in the Community.

Secondly, the income of capital relative to that of labour is moving in a direction which slows down the tendency for labour to be substituted by means of capital-deepening investment. Whereas, for example, between 1960 and 1974 an annual average growth of the capital stock of more than 5% accompanied a rate of net employment creation of 0,3%, this ratio was 3% to -0,3% between 1974 and 1983 and 2,3% to 0,7% after 1983. The moderate real wage growth of the 1980s thus shows significant effects. In order to further accelerate employment creation it has to be continued to an extent which may differ between Member States.

The employment content of investment could also be improved by broader efforts to stimulate higher capital productivity along with lower capital/labour ratios. Higher capital productivity would help to avoid capacity constraints in sectors where demand is already strong. It would also improve the competitiveness of European firms and thus create additional demand. In sectors and enterprises where demand is particularly strong this could, for example, be achieved by longer operating hours of equipment, which would allow the employment of more labour per unit of capital. Today's restrictions on operating and opening hours both by law and collective agreements should give way to a more flexible approach. The appropriate implementation would have to be determined by pragmatic decentralized negotiations between the social partners. The cost reductions resulting from longer operating hours of equipment could in part be used to compensate employees for less attractive working hours with additional reductions of individual working time, which would then still be neutral to the level of total costs. This would further increase the employment content of economic growth.

The basic direction of policy to successfully tackle the Community's large-scale unemployment remains uncontroversial. At present the more favourable economic performance provides a good opportunity for the adjustment necessary to sustain the higher growth path and to make it more resistant to possible shocks. But the conditions for more employment-creating growth and investment have to be further improved along the lines of the Community's cooperative growth strategy for more employment ⁽¹⁾.

At the macroeconomic level, the conditions for a further rise in profitability and sustained trend of job-creating investment must continue to be strengthened. In this connection, moderate increases in real wages coupled with the now more favourable outlook for demand remains indispensable. At the microeconomic level, structural policies have an essential role to play in increasing the adaptability of the markets in goods, services, capital and labour, in encouraging entrepreneurial initiative and thus in improving the efficiency of the Community economies. The lifting of unnecessary administrative barriers, notably where these stand in the way of a major improvement in the employment situation, has a high priority. In order not to call into question fundamental rights in the fields of social security, of social protection and of working conditions, appropriate regard must be given to the social dimension and the process of structural adjustment must be accompanied by a wide social dialogue (see B.2.2). Furthermore, with some parts of the unemployed in danger of losing contact with the labour market and with structural change continuing a special need has developed to focus on employability (see C.1).

With the full implementation of the macro- and microeconomic policies outlined above and the completion of the internal market, the Community would have the chance to transform its 1988 growth rate of about 3 1/2% into a lasting medium-term growth path of this order of magnitude or even better. If this could be realized, employment could expand at a rate of about 1 1/2% per year in the Community. Such an increase of employment would — in spite of a still growing labour supply due to demographic factors and increasing participation rates — be sufficient to reduce the Community unemployment rate by about 1 percentage point per year.

C. POLICY FOR GROWTH AND GREATER CONFIDENCE

The renewed investment, which is underway, increases the chances of realizing the objective of sustained, durable and non-inflationary employment-creating growth. The current favourable trend needs to be reinforced over the coming months. However, some aspects of the problem are different in the various countries. In some countries external demand

has outstripped domestic supply, giving rise to inflationary pressures and/or a deterioration in the external account. In these circumstances it is important that growth is restored to

⁽¹⁾ See annual economic reports 1985/86, 1986/87 and 1987/88 published in *European Economy* Nos 26, 30 and 34.

more sustainable rates. The running should now be taken up by those countries where growth has been slower and weaker and who now have better conditions for internal growth. This will also contribute to a renewed equilibrium in the external accounts of the different countries.

1. Structural and labour market policies

Structural policies are required in their own right to improve the adaptability and efficiency of the Community economies and thus to make a non-inflationary rise in output and employment sustainable, while simultaneously pursuing the objective behind efforts to increase flexibility is not to destroy social achievements but to create even more employment. Furthermore structural policies must accompany the completion of the internal market in order to ensure that its full benefits are actually forthcoming.

Competition policy must be stringently enforced by rigorous application of the legislation, by the introduction of a control of concentration with a Community dimension and by strict control of State aids. Moreover, the public and private sectors should be treated in a non-discriminatory manner. In this context it is desirable that complete transparency is assured in the relations between public enterprises and the State.

Emphasis must continue to be placed on research and development and on improving the technological competitiveness of European firms. Here the Community has a particular role to play as it encourages and coordinates national research efforts and develops a genuine European approach to research and technology by supporting Community-wide collaboration projects in a variety of sectors, *inter alia* information and communications technology (Esprit II and RACE). It aims in particular at a strengthening of the technological foundation of the internal market. In this respect the framework programme for research (1987 to 1991) adopted in September 1987 is a success. One year after the adoption of this programme, it is clear that a new impetus has been given to Community research and technological development. In financial terms more than 90% of the specific implementing programmes have already been submitted to the Council and more than 50% have been adopted.

The Commission also intends to pursue its policy in favour of small and medium-sized enterprises (SME), as defined in its action programme, approved by the Council in November 1986. To further improve the information for SMEs on European affairs (regulation, norms, tender offers, research projects) the Commission together with the Member State is pursuing an extension of the successful project of 'EC

infocentres'. A computerized information network (BCNet) to support cross border cooperation between SMEs has been installed.

With the completion of the internal market, a significant increase of demand for transport services is to be expected. The exchange of goods must not be impeded by lack of transport and communication facilities within the Community. In addition, the links between the peripheral regions and the centre of the Community have to be improved. The Commission is therefore focusing its efforts to support the medium-term improvement of Community infrastructure⁽¹⁾ on projects which are of particular importance to the process of the completion of the internal market and has submitted a draft Regulation to the Council on an 'Action programme in the area of infrastructure financing with regard to the completion of the internal market'. The Commission also intends to introduce a 'declaration of Community interest' for transport infrastructure programmes. This would give priority to these programmes with regard to the Community's financial instruments and would facilitate the attraction of private capital.

The 'declaration of Community interest' is also a major element of the Commission proposals for the development of new financing instruments. In order to help major European infrastructure projects to become a reality and to do this by stimulating the markets to offer the required finance, it has submitted a revised proposal for a 'Decision on the financing of major infrastructure projects of European interest'⁽²⁾, which has been given approval by the European Parliament and the Economic and Social Committee and is now under further discussion by the Council.

These intentions are complemented by an increased willingness of the European Investment Bank (EIB) to use its means to the full to encourage major European infrastructure investment. A striking example was the agreement of the EIB in September 1987 to make loans of some ECU 1,4 billion for the Channel tunnel project.

In the longer run the hope for Europe lies in the intellectual and technical potential of its population and notably the younger generation. Investment in human capital in general and in education and training in particular must, therefore, be high on the agenda of all Member States. Training for work is one of the sources of strength of the German economy; the United Kingdom and France have committed themselves to important efforts in this field. It is essential that in all other Member States as well substantial efforts be deployed in this field in the next few years, to the largest possible extent with the assistance of the Community.

⁽¹⁾ Basic principles have been put forward in the proposal for a 'Medium-term programme for transport infrastructure', Doc. COM(86) 340.

⁽²⁾ Doc. COM(88) 340.

⁽³⁾ Doc. COM(87) 724.

The very special attention which labour markets have received in a number of Member States in the 1980s, together with the improved overall economic climate, have borne fruit. Labour markets throughout Europe are generally showing signs of greater adaptability (see B.3). Yet unemployment persists, with continuing increases in the average period of unemployment. Hence the need to improve the integration and re-integration into working life of the unemployed by a full range of measures, encompassing counselling and guidance, job search assistance, recruitment assistance and appropriate vocational training. All Member States have followed various specific labour market policies to address this problem, in particular for the young and long-term unemployed. A comprehensive overview of these policies is regularly provided by the Commission in its semi-annual follow-up on the Council resolution of 22 December 1986 ⁽¹⁾. The necessity of the measures designed in the Commission's 'Memorandum on long-term unemployment' ⁽²⁾ and the special priority for the use of the growing Community Structural Funds to combat long-term unemployment are underlined by these developments in the labour market. Based on the Council decision on 'Action to combat long-term unemployment' ⁽³⁾, the Commission started an 'Action programme to assist the long-term unemployed' in summer 1988.

2. Monetary policy

The framework for conducting monetary policies in the Community in 1988 has continued to be strongly influenced by international monetary developments:

- (a) in 1987 monetary policies in Europe were geared to preventing an undershooting of the dollar, involving official financing of the United States external deficit and implying reduced interest rates and fast growth of the monetary aggregates in Europe;
- (b) the appreciation of the dollar during 1988 alleviated this external constraint and allowed the European authorities to give greater weight to domestic objectives.

The greater freedom for manoeuvre in monetary policy, most evident in recent months, has been directed to damping or reversing the upturn in inflation expectations that appeared to have occurred during the summer as a result of a number of factors:

- higher import costs, in dollar terms, in the first half of the year, aggravated by the dollar's appreciation,
- fears of overheating in some Community countries and stronger-than-expected growth in the context of high capacity utilization in all of them,

- continuing concern in some countries about above-target growth of the monetary aggregates and their possible detrimental effect on future wage and price-setting behaviour.

The combination of these factors, weighted in different ways in different Member States, thus led the monetary authorities, notably in the Federal Republic of Germany and the United Kingdom, to increase short-term interest rates. The actions taken appear to have had the desired effect of damping longer-term inflation expectations, as evidenced by the considerable flattening of yield curves since the summer. To the extent that longer-term expectations of inflation and/or depreciation of the currencies have been reduced, long-term interest rates could be stabilized or decrease on a sound basis; some evidence of this emerged in some countries in early autumn.

Among ERM participants, short-term interest rates have risen most in Germany. The rise started on the money market during the second quarter of 1988 and since June the Bundesbank has on several occasions raised its key rates. These movements initially marked a reversal of previous tendencies essentially imposed by external constraints but later reflected a fear that further deutschmark weakness could increase inflationary expectations via rising import prices, as well as a desire to rein back above-target growth of money supply. Some deceleration of M3 in Germany is already in evidence: the latest figures show growth only just above the top of the 3 to 6% target range.

In other countries belonging to the exchange rate mechanism the increases in short-term interest rates have been somewhat smaller than in Germany. In these countries, the compatibility of domestic economic policies with final objectives has important repercussions on the conduct of monetary policy. In Italy, the budget situation is a serious problem for monetary policy: high short-term interest rates, which are required to stabilize the lira exchange rate, affect the fiscal budget consolidation via higher debt servicing costs. Without significant progress in the budgetary field the difficulties of the policy-mix could become even more obvious, further complicating the task of monetary policy. Other countries with budgetary problems might be faced with a similar, although probably less acute, dilemma.

In the United Kingdom, the authorities have reacted to ensure that the downward pressure on inflation is maintained by increasing rates on several occasions. The recent monetary tightening is consistent with the need to cool the very rapid growth of domestic demand.

⁽¹⁾ 'An action programme on employment growth'.

⁽²⁾ Doc. COM(87) 231.

⁽³⁾ OJ No C 335, 1. 12. 1987.

Internally-generated inflationary pressures, at least in the countries participating in the exchange-rate mechanism of the EMS, seem at the moment to be contained: monetary growth is under control; the composition of overall growth has favoured investment, holding out the prospect of an increase in supply capacity; and unit labour costs are increasing only slightly. Moreover, non-oil commodity prices have stabilized since the summer and oil prices have slumped. Further, the tightening of monetary policies in these countries in recent months has already dampened expectations of inflation.

The risk to the outlook and the potential challenge to monetary policy could come from a renewed instability of the dollar. In such circumstances, the monetary authorities will have to coordinate their efforts. Active foreign exchange intervention has recently proved its effectiveness in calming wilder oscillations in market expectations of the dollar's exchange rate, and the importance of this monetary tool may need to be put further to the test should major exchange rate pressures develop. The exchange rate mechanism of the EMS has well withstood recent dollar gyrations, mainly because of the coordination of interventions and the active management of interest rate differentials following from the Basle/Nyborg agreement.

3. Budgetary policies

For budgetary policies, the medium-term objectives remain paramount. Their realization should allow expectations to stabilize and the efficiency of public finances to improve so as to contain the growth in public debt.

The first set of objectives is connected with the actual attainment of the large internal market. There is wide

support for the point of view that the approximation of indirect taxation is a precondition for the full abolition of barriers to the free movement of goods and services. In some cases this is seen as conflicting with the domestic priorities of budgetary policies. It is important that the current discussions on this topic advance rapidly in order to confirm once more the irreversible nature of the completion of the internal market.

In addition, in a situation of complete freedom, tax considerations could have a greater influence on capital movements. When the new directive liberalizing capital movements was adopted, it was thus agreed that the period adopted for its implementation should be put to good use in order to define, within the Council, measures intended to abolish or reduce the risks of distortion, evasion and tax fraud related to the diversity of national systems concerning the taxation of savings and the control of their application.

Another medium-term objective assigned to budgetary policies, essential for a strengthening of the economic and monetary cohesion of the Community, is the need for increased convergence of budget balances by a reduction of deficits in those countries where they are largest. The need for better balance between investment and domestic saving must also be taken into account. In these respects the progress which could be made in 1988 seems too small or non-existent. In two countries, Italy and Greece, the budget deficit should remain at or above 10% of GDP, which represents a difference of over 6 percentage points with the Community average. In these two countries, as well as in Belgium, Ireland, the Netherlands and Portugal, the already high level of public debt and the high burden of interest payments require persistent efforts to reduce budget deficits.

TABLE 16

General government borrowing requirement

(% of GDP)

	B	DK	D	GR	E	F	IRL	I	L	NL	P	UK	EUR 12
1987	-7,2	2,1	-1,8	-9,5	-3,6	-2,5	-9,1	-10,5	5,2	-6,3	-8,4	-1,4	-4,2
1988 ⁽¹⁾	-7 1/4	1	-2 1/4	-12	-3	-2	-6 1/2	-10	5 1/4	-5 1/4	-8 1/4	-1/4	-3 3/4
1989 ⁽¹⁾	-6 1/2	1 1/4	-1 1/4	-13 1/4	-3	-1 3/4	-6	-10	6 1/4	-4 1/2	-7 3/4	0	-3 1/2

⁽¹⁾ September to October 1988 forecasts of Commission services.

TABLE 17

Public debt ⁽¹⁾

(% of GDP)

	B	DK	D	GR	E	F	IRL	I	L	NL	P	UK	EUR 12
1980	75,7	33,5	32,7	28,8	18,2	24,6	76,8	58,5	13,8	46,0	46,4 ⁽³⁾	52,2	42,6 ⁽³⁾
1984	110,7	67,0	41,4	53,2	41,2	31,8	102,1	77,1	14,8	66,1	61,4	58,4	54,0
1988 ⁽²⁾	127,4	57,8	45,0	69,4	48,0	37,2	123,3	96,6	14,7	79,4	78,8	49,3	60,0

⁽¹⁾ General government; for Belgium and the Netherlands excluding social security funds; for Greece and Ireland central government only.

⁽²⁾ September to October 1988 forecasts of Commission services.

⁽³⁾ 1981.

The developments in budget deficits forecast for 1989 give rise to some concerns of another nature: on current trends, budgetary policies do not appear to be contributing to a reduction in the divergent external balances.

Among the surplus countries the budget deficit in Germany should decrease by $1\frac{1}{2}$, to 1 percentage point in 1989. In a

medium-term perspective, German management of public finances should continue to contribute to a strengthening of supply and demand conditions, but domestic demand should continue to rise faster than potential output so as to achieve a further shift to domestic-demand-led growth. In these conditions, the implementation of the final stage of the tax reform in January 1990 is welcome for its impact on business motivations as well as for its effect on demand.

TABLE 18
Net borrowing of general government in ERM countries

	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
ERM countries	- 5,0	- 4,8	- 4 $\frac{1}{2}$	- 4
— Above average current balance ⁽²⁾	- 2,8	- 3,0	- 3 $\frac{1}{4}$	- 2 $\frac{1}{4}$
— Below average current balance ⁽³⁾	- 6,3	- 5,7	- 5 $\frac{1}{4}$	- 5 $\frac{1}{4}$

⁽¹⁾ September to October 1988 forecasts of Commission services.

⁽²⁾ Belgium, Germany, Netherlands, Ireland, Luxembourg.

⁽³⁾ Denmark, France, Italy.

A further objective of budgetary policies is the simultaneous strengthening of the conditions governing supply and demand. This is not only a question of the level of budget deficits but also of the efforts still necessary in several Member States to reorientate public expenditures to the benefit of a strengthening of the productive system by profitable public investment and reductions and reform in taxation and parafiscal charges. The faster-than-expected growth and the room for manoeuvre created by unexpectedly

higher revenue should be put to good use by bold action in this area. Especially, in practically all Member States, the system of subsidies will need to be thoroughly reconsidered, not least with a view to minimizing tensions with respect to competition policy as the Community proceeds towards the completion of the internal market. The re-examination of subsidies and tax exemptions for housing and of rent controls that has started in several Member States should be generalized.

TABLE 19
Indicators of budgetary policy (EUR 12)

	1983	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
Taxes	24,8	25,2	25,6	25,8	25,8
Social security receipts	14,7	14,5	14,6	14,5	14,4
Other receipts	3,8	3,8	3,5	3,4	3,4
Total receipts	43,3	43,6	43,7	43,6	43,6
Current expenditure	44,9	44,7	44,4	43,9	43,5
of which:					
— Government consumption ⁽²⁾	18,9	18,4	18,5	18,3	18,1
— Transferred to households	17,7	17,3	17,1	17,1	17,0
— Interest payments	4,4	5,1	4,9	4,8	4,8
— Other ⁽³⁾	3,9	3,9	3,9	3,7	3,6
Gross capital formation	2,9	2,8	2,7	2,8	2,8
Other capital expenditure	0,9	0,9	0,8	0,8	0,8
Total expenditure	48,6	48,4	47,9	47,4	47,1
Net borrowing requirement of general government ⁽²⁾	- 5,3	- 4,8	- 4,2	- 3,8	- 3,5

⁽¹⁾ Sum of transfers to enterprises, transfers to the rest of world and other transfers.

⁽²⁾ September to October 1988 forecasts of Commission services.

⁽³⁾ General government: ESA definition which includes social security funds.

The current public expenditures as a percentage of GDP are expected only to diminish slightly in 1988 and 1989 on average in the Community. In some countries, notably in Greece, Italy and Portugal and to some extent in Belgium and the Netherlands, the control of the spontaneous rise of public expenditures remains a problem.

Rationalization of tax systems and lowering of rates of direct taxation have been high on the agenda in many Member States and important results have already been achieved. Despite these efforts tax and parafiscal receipts as a percentage of GDP are not expected to diminish on average in the Community. The United Kingdom has moved ahead of other Member States in the area of tax reform; important reforms have also been implemented or will be implemented in the near future in Belgium, Denmark, Germany, Italy and the Netherlands. A lowering of income taxes was introduced in France in 1987 and 1988 and the system of taxes on economic activity has been simplified. Some Member States, moreover, have taken steps to change indirect taxes and taxes on capital income in ways which should facilitate fiscal harmonization in the Community although much remains to be done in this area. In addition, several Member States, notably Greece and Italy, appear to be in need of a modernization of the system of tax collection to counter tax evasion and broaden the base of taxation of non-wage incomes. Where tax reforms are undertaken in countries with serious budgetary positions, efforts must be deployed to ensure that the systemic changes do not lead to a shortfall of tax receipts; Belgium is a case in point here.

The currently more favourable performances should not mask the fact that in the budgetary area major structural problems persist. The solution which will be found for them will determine the Community's capacity to attain stronger growth and better employment performances and to derive all the benefits from the completion of the internal market.

4. The need for increased policy coordination

The need for coordination within the Community stems from the existence of several centres of major economic policy decision-making and from its already very high degree of economic interdependence. Today nearly 60% of total visible Community trade is conducted between Member States. This interdependence will be further increased by the completion of the internal market and the integration of the financial markets of the Community. In addition the strengthening of the social and economic cohesion of the Community will also put specific demands on the conduct of economic policies of the Member States as required by Article 130 B.

Coordination is not only necessary to make progress towards the achievement of the internal goals of the Community. This

is also necessary so that it can throw its considerable weight behind international cooperation in order to contribute to the necessary adjustments in the world economy. The Community is in fact the largest economic area in the industrialized world with a population of over 320 million but also provides roughly one-quarter of world production (as compared to just over one-fifth by the United States and one-tenth by Japan). It also has a greater share of world trade than any other economy in the world.

An increasingly high degree of stability in exchange rates between Member States would improve the functioning of the internal market. Uncertain developments in exchange rates unrelated to changes in underlying economic fundamentals, which distort competitive conditions, can affect trade and the regional allocation of investment. The current monetary framework of the Community is characterized by an exchange rate mechanism which — even if it has to date succeeded in ensuring a satisfactory level of stability in exchange rates — only includes eight of the 12 European currencies. Monetary cohesion would be further strengthened by an enlargement of the exchange rate mechanism at the appropriate time to countries not yet participating and as a corollary by the participation of all currencies in the definition of the ecu. The strengthening of the role of the ecu will also make a welcome contribution to monetary cohesion in the Community. (i) An increasing role for the ecu as a reserve currency would lead to a more even distribution between Community currencies of capital movements to and from the rest of the world. It would help to stabilize exchange rates within the Community and in particular the countries participating in the exchange rate mechanism. (ii) An increased role for the ecu in intra-Community trade could reduce transaction costs as does the abolition of other barriers and thus contribute to the realization of the single market. (iii) Greater ecu borrowing by Member States and Community institutions would add to the breadth and depth of the market.

Close monetary cooperation is essential to ensure that realignments are less frequent and correspond to the changes in economic fundamentals. For the most part, such coordination already exists between the countries participating in the European monetary system (EMS) exchange rate mechanism. In recent years, significant progress has been made. There is a stronger consensus between Member States on the objective of domestic stability. The convergence of inflation rates between EMS countries is high by historical standards. In addition, the Basle/Nyborg agreements have improved the mechanisms of the system. They also represent a step towards a more cooperative conception of the management of monetary and exchange rate policies.

Such cooperative management is necessary. Certainly, each country participating in the exchange rate mechanism is benefiting from external stability. But this participation involves a certain loss of autonomy in the conduct of

monetary policy. The success of the EMS creates the conditions in which further progress can be made towards integration and at the same time poses the challenge of closer coordination. The Community cannot ignore this movement without undermining the whole of the edifice which is already standing. The full liberalization of capital movements within the Community ⁽¹⁾ between now and 1 July 1990, to which they have committed themselves, will further reduce the autonomy and increase the need for discipline in the conduct of monetary policy. Therefore greater cooperation is necessary. This could manifest itself in two ways: (i) by further strengthening the convergence of monetary policies taking account of the interests of all participants. In this context, especially for currencies participating in the exchange rate mechanism, the implementation of a coherent exchange rate policy *vis-à-vis* the rest of the world is also necessary.

Greater discipline and better convergence in other domains of economic policy, especially in the domain of public finance, is also necessary to attenuate the risk of conflict between exchange rate stability and the domestic goals of monetary policy. As long as the health of public sector finances remains as disparate as at present (with deficits and surpluses ranging from - 13 to + 1 % and gross public debt between 15 and 140 % of GDP), the market will still worry that the convergence towards price stability, towards more stable exchange rates and towards a constellation of sustainable interest rates can be reversed. The risk premiums they will charge on the financial activities of the poorly performing countries will eventually create tension and undermine the stability which has been recorded of late in the Community.

For coordination to be efficient and credible, it is not only a question of procedure but also of a consensus on the main objectives:

- Price stability and the downward convergence of inflation rates. Achievements in this area represent a precious asset which must not be squandered as they provide a prerequisite for the other economic objectives.
- The medium-term compatibility of balances of payments. In this area the problems are more complex. It is normal for countries which have a greater need to catch up and/or greater investment opportunities to be in deficit with the rest of the world over a longer period.

But it is essential for the Community's medium-term cohesion that these countries' deficits be financed by private capital movements, attracted by adequate remuneration and supplemented, where appropriate, by Community resources. In addition, the conditions must be created which enable the external debt to be serviced thereafter by additional exports. If these conditions are not met, exchange rate and monetary policy will be to the forefront in ensuring exchange rate stability. And if tensions persist they cannot do this for long without the risk, in the surplus countries, of conflicting with the objective of domestic stability or, in the deficit countries, of imposing an excessive level of interest rates.

Hence a stronger consensus is also necessary on the broad lines of all economic policies, so as to ensure that domestic and external monetary stability contribute fully to the objectives of growth and employment in the Community and the Member States. The annual economic report and the Community economic policy strategy developed here should be seen as an attempt to foster this general economic policy consensus.

D. COUNTRY SITUATIONS, PROSPECTS AND POLICIES

BELGIUM

Financial imbalances are being reduced but further progress is needed

The restoration of financial balance in the Belgian economy has proceeded albeit gradually in recent years. Between 1981 and 1987 the general government borrowing requirement has been reduced substantially and the external balance has shifted from a large deficit to a comfortable surplus. Despite

the lowering of the nominal budget deficit, the rise in public debt as a proportion of GDP has nevertheless remained strong while, at the same time, the rise in debt servicing has substantially reduced the scope for an increase in non-interest expenditure. The Government has succeeded in keeping the evolution of the deficit broadly on track in 1988, partly due to higher-than-expected fiscal receipts.

A significant feature of economic policy, in recent years, has been a series of measures aimed at keeping the level of wage costs constant relative to that of competitors and thereby stimulating employment in the private sector. The flexibility of the labour market has been improved through the use of measures to amend the generous system of unemployment allowances and through various schemes for training, etc., while the adaptation of working hours has facilitated growth in employment.

⁽¹⁾ Except for Spain, Ireland, Portugal and Greece, which between now and the end of 1992 will be covered by transitional arrangements, and Belgium and Luxembourg, which until that date will be allowed to retain the dual exchange market.

The revival of economic activity at the world level in 1988 has been particularly beneficial to Belgium: the growth of output this year is likely to be the highest recorded since 1980 and unemployment should show a strong decline. As in other Member States, the cyclical upturn has been broadly based, as illustrated by a significant improvement in the investment climate.

The upturn in activity is, on present trends and prospects, likely to continue well into 1989 with a further expansion of output and employment and a lowering of unemployment. Inflation should rise somewhat but remain below the Community average and the surplus on the current external account is unlikely to fall.

Stabilization of the public debt/GDP ratio will require further strong budgetary consolidation

Even though growth prospects appear favourable, any reduction in the government budget deficit in 1989 will require that a careful watch be kept on expenditure especially in view of a rising trend in interest rates in recent months. A

further significant rise in the public debt/GDP ratio is to be envisaged. In order to stabilize this ratio in subsequent years, a further substantial reduction of the general government borrowing requirement will be needed. In this regard, the objectives announced in the Government's declaration for the period after 1989, i. e. no increase of non-interest expenditure in real terms and no increase in the deficit in nominal absolute terms should progressively restrain the spiralling costs of debt-servicing.

Hence, the stance of budgetary policy must remain restrictive for some time and the fiscal reform to be introduced should on no account lead to an increase in the budget deficit. The rate of economic growth, therefore, will be determined principally by the vitality of the private sector and notably by its readiness to increase productive capacity and employment. The Council's decisions to proceed with the completion of the internal market have clearly opened new favourable prospects for the Belgian business environment.

In order to fully benefit from the new opportunities, structural adjustment, greater flexibility and mobility in the labour market, training and education should have a high place on the political agenda for the coming years.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

BELGIUM

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	9,2	9,3	8,8	6,0	7,3	7,0	6,0	3,5	4,6	5,0
— at constant prices	4,9	2,0	1,5	0,1	2,1	1,4	2,3	1,8	2,9	2,2
— price deflator	4,1	7,1	7,1	5,9	5,0	5,5	3,7	1,6	1,6	2,8
2. Gross fixed capital formation ⁽²⁾										
— total	5,1	-0,6	-1,7	-4,2	2,1	1,0	6,5	5,2	7,3	2,7
— construction	:	-1,2	-5,6	-6,3	-5,9	-0,3	2,0	3,0	7,1	0,8
— equipment	:	2,1	6,0	-2,8	13,4	-0,7	10,8	7,9	7,6	5,0
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	21,8	21,3	17,3	16,3	16,1	15,7	16,1	16,6	17,6	17,8
— general government	:	3,7	3,4	3,0	2,6	2,2	1,9	1,9	1,8	1,7
— other sectors	:	17,6	13,9	13,3	13,5	13,5	14,1	14,7	15,8	16,1
4. Final national uses including stocks:										
— at constant prices	4,8	1,7	0,9	-2,3	2,1	1,3	3,2	2,4	3,1	2,1
— relative against 19 competitors	-0,1	-0,1	0,6	-4,0	-0,7	-1,3	-0,7	-0,9	-0,7	-0,5
— relative against other Member States	0,0	0,1	0,3	-3,6	0,3	-0,9	-0,7	-0,9	-0,7	-0,6
5. Inflation (price deflator private consumption)	3,7	7,8	7,6	6,8	5,8	5,2	0,8	1,6	1,3	2,4
6. Compensation per employee:										
— nominal	8,9	11,0	7,9	6,0	6,1	4,8	3,8	3,3	2,2	3,8
— real, deflator private consumption	5,1	3,0	0,3	-0,8	0,3	-0,4	3,0	1,6	0,9	1,3
— real, deflator GDP	4,6	3,6	0,8	0,1	1,0	-0,7	0,2	1,6	0,6	0,9
7. Productivity ⁽⁴⁾	4,3	2,2	2,9	1,2	2,1	0,6	1,3	1,6	1,7	1,4
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	111,5	112,5	111,2	110,0	108,6	107,3	107,4	106,2	105,8
— annual percentage change	0,3	1,4	-2,1	-1,1	-1,1	-1,3	-1,1	0,1	-1,1	-0,5
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	112,9	91,9	89,6	88,3	89,5	93,9	97,0	94,0	:
— annual percentage change	-0,3	0,3	-11,4	-2,5	-1,5	1,3	4,9	3,3	-3,1	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	109,8	91,6	90,6	91,2	92,7	94,9	96,3	93,9	:
— annual percentage change	-0,7	0,3	-9,9	-1,0	0,7	1,6	2,4	1,4	-2,4	:
11. Employment	0,6	-0,2	-1,3	-1,1	0,0	0,8	1,0	0,3	1,2	0,7
12. Unemployment rate ⁽⁶⁾	2,2	7,4	13,0	14,3	14,4	13,6	12,6	12,3	11,5	11,0
13. Current balance ⁽⁷⁾	1,1	-1,6	-3,5	-0,5	-0,2	0,7	2,6	1,9	1,8	1,9
14. Net lending of general government ⁽⁷⁾	:	-6,6	-10,9	-11,2	-9,3	-8,3	-8,9	-7,2	-7,1	-6,5
15. Gross debt of general government ⁽⁷⁾	:	67,5	95,3	105,0	110,7	117,2	120,1	125,0	127,4	129,8
16. Interest payments by general government ⁽⁷⁾	:	4,8	9,2	9,4	9,9	10,5	11,0	10,6	10,5	10,8
17. Money supply (end of year) ⁽⁸⁾	10,1	11,1	7,5	7,1	6,2	6,7	10,7	9,9	:	:
18. Long-term interest rate ⁽⁹⁾	6,5	9,9	13,4	11,8	12,0	10,6	7,9	7,8	7,9	:

(1) 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

(2) At constant prices.

(3) At current prices.

(4) GDP at constant market prices per person employed.

(5) Deflator GDP.

(6) Percentage of civilian labour force.

(7) Percentage of GDP.

(8) M 2 N.

(9) Levels.

DENMARK

Gradual return to more stable conditions but at the cost of a large loss of output

After a phase of serious deterioration in the external balance which reached its worst point in 1986, the Danish economy in 1987 and 1988 has moved gradually back towards a more sustainable position. Thanks to a considerable discretionary tightening of budgetary policy and of measures to boost household saving, real domestic demand fell strongly both in 1987 and 1988 and the current external deficit was reduced from 5,2 % of GDP in 1986 to some 2,4 % in 1988.

The adjustment process was rendered more difficult, however, by the 1987 wage settlements which not only provided for large increases in hourly wage costs but also for cuts in working hours which added to the cost push and led to a significant deterioration in the competitiveness of Danish enterprises. Cost-reducing fiscal measures subsequently adopted have compensated exporters, to some extent, for the rise in wage costs but the capacity of the Danish economy to pursue the employment creating growth seen in the period 1982 to 1985 clearly suffered and unemployment is again on the rise.

Against this background the external constraint will again necessitate a tight control on the growth of domestic demand in 1989. Although the external balance may improve somewhat further, both in volume and in value terms. GDP is unlikely to grow by more than some 1½ %. The number of persons employed may rise only a little, mainly as a result of shorter working hours. The rate of unemployment is, therefore, likely to show a further rise.

The diminishing scope for using macroeconomic policy in demand management: a policy dilemma

Although the general government budget balance has deteriorated somewhat since 1986 it is still (despite the fact

that GDP in real terms will be no higher than three years earlier) likely to show a surplus of some 1 % of GDP in 1989. Thus, the external deficit is the counterpart of a savings deficit in the private sector, notably the low level of household savings. While strict limits on public expenditure will remain necessary, it is politically and economically difficult to raise the budget surplus much further and it would, therefore, be desirable to rely on other policy instruments: monetary policy and microeconomic policies to bring about a reduction of the external deficit to a sustainable level. The scope for using monetary policy in stabilization policy is, however, restricted by the EMS commitments and the large scope for off-setting capital movements. Interest rate increases (aimed at stimulating domestic saving) could (and would most probably) trigger capital imports and upward pressure on the Danish krone.

Given the limited scope for using monetary and budgetary policy for balance of payments purposes (which is indeed a normal consequence of the ongoing monetary integration), the labour market to an increasing extent will have to take the brunt of the adjustment. The need to keep wage settlements at a level compatible with external balance and a continued rise in employment is, therefore, larger than ever before.

Given this change in the general macroeconomic framework, microeconomic policies appear to have an increasing role to play. Therefore, further steps to remove the incentives to take up debt, to stimulate saving of wage incomes (for example through some version of profit-sharing), to render wage settlements more responsive to regional and corporate conditions and to stimulate labour market flexibility in general, appear even more urgent in Denmark than in many other Member States.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

DENMARK

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	11,7	11,3	13,9	10,4	9,4	9,7	8,4	3,9	4,3	4,8
— at constant prices	4,3	1,2	3,0	2,5	3,5	4,2	3,4	-1,0	0,0	1,7
— price deflator	7,0	10,0	10,6	7,6	5,7	5,3	4,9	5,0	4,3	3,1
2. Gross fixed capital formation ⁽²⁾										
— total	6,5	-5,3	7,1	1,9	10,5	11,9	16,8	-8,9	-4,1	0,1
— construction	:	-6,6	-1,3	1,9	7,7	7,7	19,3	-1,0	-4,4	-3,1
— equipment	:	-0,6	19,8	2,3	14,3	15,4	14,8	-18,0	-3,4	4,5
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	24,0	20,9	16,1	16,0	17,1	18,5	20,4	18,5	17,7	17,3
— general government	:	3,6	2,8	2,3	1,9	2,2	1,7	2,1	2,3	1,9
— other sectors	:	17,3	13,2	13,7	15,2	16,3	18,7	16,4	15,3	15,4
4. Final national uses including stocks:										
— at constant prices	4,6	0,0	3,5	1,4	4,1	5,7	5,7	-3,2	-1,4	0,7
— relative against 19 competitors	0,1	-1,7	3,2	-0,6	0,5	2,9	1,8	-6,5	-5,1	-1,9
— relative against other Member States	0,2	-1,4	3,1	-0,1	2,0	3,6	1,9	-6,7	-5,2	-2,1
5. Inflation (price deflator private consumption)	6,6	11,0	10,2	6,8	6,5	4,9	3,6	4,1	4,8	3,7
6. Compensation per employee:										
— nominal	10,7	11,4	11,9	8,2	5,1	4,5	4,7	8,2	4,5	2,5
— real, deflator private consumption	3,8	0,4	1,5	1,3	-1,3	-0,3	1,0	4,0	-0,4	-1,1
— real, deflator GDP	3,4	1,3	1,2	0,5	-0,6	-0,7	-0,2	3,0	0,1	-0,5
7. Productivity ⁽⁴⁾	3,2	1,1	2,6	2,2	1,7	1,2	1,0	-2,2	0,3	1,5
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	101,9	99,2	97,5	95,3	93,5	92,4	97,3	97,1	95,1
— annual percentage change	0,2	0,3	-1,3	-1,7	-2,3	-1,9	-1,2	5,3	-0,2	-2,0
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	116,7	99,6	100,6	97,0	97,8	103,7	116,0	115,6	:
— annual percentage change	2,2	-1,2	-2,5	1,0	-3,5	0,8	6,1	11,9	-0,4	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	113,1	98,6	100,9	100,7	102,0	104,5	113,8	114,8	:
— annual percentage change	1,7	-1,2	-0,9	2,3	-0,2	1,3	2,4	9,0	0,9	:
11. Employment	1,1	0,2	0,4	0,3	1,7	2,9	2,3	1,1	-0,3	0,2
12. Unemployment rate ⁽⁶⁾	1,1	5,9	9,3	10,1	9,9	8,7	7,4	7,6	8,5	9,0
13. Current balance ⁽⁷⁾	-2,0	-3,5	-4,2	-2,6	-3,3	-4,7	-5,1	-3,0	-2,5	-2,3
14. Net lending of general government ⁽⁷⁾	:	-1,4	-9,1	-7,2	-4,1	-2,0	3,1	2,1	0,9	1,4
15. Gross debt of general government ⁽⁷⁾	:	22,3	53,1	62,6	67,0	65,3	59,8	58,4	57,8	56,4
16. Interest payments by general government ⁽⁷⁾	:	2,6	6,0	8,1	9,6	9,8	8,8	8,3	7,9	7,4
17. Money supply (end of year) ⁽⁸⁾	10,6	11,4	11,4	25,4	17,8	15,8	8,4	4,4	:	:
18. Long-term interest rate ⁽⁹⁾	9,0	16,4	20,5	14,4	14,0	11,6	10,5	11,9	10,8	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ M 2.

⁽⁹⁾ Levels.

FEDERAL REPUBLIC OF GERMANY

After adjustment to a lower dollar the German economy has entered a new phase of faster growth in output and employment

After a difficult period of adjustment to the effects of the steep decline in the dollar with, notably, a 24-months-long stagnation of the volume of exports the German economy at the beginning of 1988 entered a phase of strong recovery in activity and in the business climate. In fact, some strengthening had occurred already in the course of 1987 but investment remained hesitant up to the end of the year influenced in part by the stock market crash and the rapid decline of the dollar rate. Since the first half of 1988, however, all leading indicators turned sharply upwards.

The strengthening of activity in 1988 is attributable both to domestic demand as supported by economic policy (tax cuts implemented at the beginning of the year, the special multi-year investment credit programme for municipalities and a relatively accommodating monetary policy) and to a marked increase in orders from abroad supported by a more favourable investment climate in other countries. In turn, this has entailed a considerable strengthening of private investment and of imports. For the year 1988 as a whole, GDP is now estimated to show a rise of some 3 $\frac{1}{4}$ %, about 1 point more than forecast only six months ago and about 1 $\frac{1}{4}$ points faster than in 1987.

On the whole, the prospects for continuation of the present investment-led upturn in Germany appear to be favourable: the growth of gross fixed capital formation is likely to be boosted by the rise in capacity utilization and by a further improvement in profitability. Moreover, growth is now becoming more employment intensive as the share of the rationalization motive has been reduced and as the need for expansion of productive capacity is becoming larger. The growth of private consumption will, on the other hand, be hampered somewhat by the increases of indirect taxes to be implemented from 1 January 1989. Nevertheless, the rate of expansion of output appears likely to slow down by only about $\frac{3}{4}$ of a point from 1988 to 1989. Although the growth of employment in 1989 may be quite fast the rate of unemployment may not decline much as the growth of the labour force will be boosted both by a rise in the activity rate and by immigration from eastern Europe.

Given that the present recovery to a considerable extent has been induced by foreign demand (in particular by the growth of investment in other Member States) the German trade surplus albeit reduced in real terms has remained high in nominal terms in 1988 and is unlikely to fall in 1989. However, the German external surplus, to a large extent, serves to finance investment abroad and, therefore, as long as the capital outflow can be maintained, does not cause an immediate concern for the international adjustment process. On the other hand, while the overall current external account of the Community is likely to show a small deficit for 1989 as

a whole, surpluses and deficits will be unevenly spread among Member States. This pattern is unlikely to be sustainable in the longer run as some Member States will aim at limiting the increase in their external liabilities. A major task for German economic policy in a medium-term perspective will be, therefore, to prepare for a return to a more sustainable external balance by maintaining the momentum of growth in the domestic economy in the face of a potential slowdown of the growth of foreign demand.

Economic policy issues: prepare for the medium term by strengthening the domestic growth factors

Although exports have been a driving force behind the 1988 upturn, net exports can hardly be counted upon to provide a positive contribution to growth in 1990 and beyond. Most likely, therefore, the degree of buoyancy of domestic demand will be decisive for the growth of GDP and for the capacity of the German economy to continue the favourable employment performance seen in the last couple of years.

The objective of the German tax reform is to strengthen the market forces in the economy by improving the tax structure and by bringing down the tax burden in terms of GNP. It now appears that the tax reduction in 1990, the next phase of the reform, is also a welcome measure ensuring continued momentum of domestic demand at a point in time where the present upturn in exports may have passed its peak. In total, it involves tax cuts amounting to some 1 % of GDP and may result in an increase in the general government borrowing requirement of some 0,7 points or to about 2 $\frac{1}{4}$ % of GDP. This level would be broadly compatible with stability of the ratio of public debt to GDP, particularly since a lowering of this level is envisaged for the following years.

The stance of monetary policy, which had been adapted to the relatively weak business climate (implying, notably, a considerable widening of the spread between long-term and short-term interest rates), was tightened significantly in June to August of 1988 in response to the strengthening of the dollar in exchange markets. The development of monetary policy over the last few years clearly reveals a certain flexibility in the face of, notably, turbulences in the exchange markets without endangering its medium-term credibility. Pending unforeseen turbulences in the exchange markets, monetary policy should now be in a position to focus more than in 1986 and 1987 on the stabilization of the macroeconomic conditions in the German economy and reaffirm its role as the anchor of the EMS.

For the time being the budgetary and monetary policy stance in 1989/90 appears to be broadly set to ensure a continued

stable, non-inflationary growth in the German economy. However, a considerable growth potential still remains to be exploited, notably in view of the fact that the demographically determined fall in the labour force envisaged for the years after 1990 seems likely, for some time ahead, to be compensated through immigration. This will require a continuation of the strong growth of investment, further improvement of profitability and moderate growth of

real wages. In addition, the scope for measures aimed at improving the adaptability of the economy including, notably, a lowering of subsidies remains considerable. With the external aspects in mind, it would not appear inappropriate for Germany to take an early lead in the process of reducing subsidies and streamlining regulations, notably in the perspective of the completion of the internal market.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

FEDERAL REPUBLIC OF GERMANY

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	8,9	6,7	3,7	4,8	4,8	4,3	5,7	4,0	5,1	4,8
— at constant prices	4,4	1,9	-0,6	1,5	2,8	2,1	2,6	1,9	3,2	2,5
— price deflator	4,3	4,7	4,4	3,3	2,0	2,2	3,1	2,0	1,8	2,3
2. Gross fixed capital formation ⁽²⁾										
— total	4,0	0,1	-5,3	3,2	0,8	0,1	3,1	1,8	6,2	3,7
— construction	:	-0,8	-4,3	1,8	1,5	-5,7	2,5	0,2	6,7	2,6
— equipment	:	2,3	-7,0	5,6	-0,2	10,0	4,3	4,0	5,5	5,2
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	24,9	21,2	20,5	20,5	20,2	19,7	19,5	19,3	19,8	20,0
— general government	:	3,5	2,8	2,5	2,4	2,3	2,4	2,4	2,4	2,4
— other sectors	:	17,6	17,6	18,0	17,8	17,4	17,0	16,9	17,4	17,6
4. Final national uses including stocks:										
— at constant prices	4,5	1,7	-2,0	2,3	2,0	1,0	3,7	3,1	3,5	2,4
— relative against 19 competitors	-0,5	-0,2	-2,7	0,7	-1,5	-1,9	-0,2	-0,5	-0,2	-0,2
— relative against other Member States	-0,4	0,1	-3,5	1,7	0,0	-1,6	-0,1	-0,5	-0,4	-0,5
5. Inflation (price deflator private consumption)	3,6	5,0	4,7	3,2	2,4	2,1	-0,2	0,5	1,3	2,5
6. Compensation per employee:										
— nominal	9,2	7,1	4,2	3,7	3,5	3,0	3,9	2,9	3,0	2,5
— real, deflator private consumption	5,4	2,0	-0,5	0,5	1,0	0,9	4,1	2,4	1,7	0,0
— real, deflator GDP	4,6	2,3	-0,2	0,4	1,5	0,8	0,8	0,9	1,2	0,2
7. Productivity ⁽⁴⁾	4,1	2,3	1,1	3,1	2,7	1,4	1,6	1,2	2,7	1,7
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	103,7	102,2	99,6	98,4	97,8	97,1	96,7	95,3	93,9
— annual percentage change	0,5	0,0	-1,2	-2,5	-1,2	-0,6	-0,8	-0,3	-1,5	-1,5
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	111,9	98,6	97,8	93,5	91,6	100,0	105,6	101,8	:
— annual percentage change	2,3	-2,5	-0,1	-0,8	-4,5	-2,0	9,2	5,6	-3,5	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	110,6	99,6	101,1	99,4	97,4	103,2	106,2	103,1	:
— annual percentage change	2,2	-2,8	2,8	1,5	-1,6	-2,0	6,0	2,9	-2,9	:
11. Employment	0,2	-0,4	-1,7	-1,5	0,1	0,7	1,0	0,7	0,5	0,8
12. Unemployment rate ⁽⁶⁾	0,8	3,7	6,9	8,4	8,4	8,4	8,1	8,1	8,1	8,2
13. Current balance ⁽⁷⁾	0,7	0,5	0,5	0,7	1,3	2,4	4,2	4,0	4,0	4,2
14. Net lending of general government ⁽⁷⁾	:	-3,0	-3,3	-2,5	-1,9	-1,1	-1,3	-1,8	-2,3	-1,3
15. Gross debt of general government ⁽⁷⁾	:	28,8	39,3	40,9	41,8	42,5	42,7	43,9	45,0	45,3
16. Interest payments by general government ⁽⁷⁾	:	1,7	2,8	3,0	3,0	3,0	3,0	2,9	2,8	2,7
17. Money supply (end of year) ⁽⁸⁾	10,9	8,1	7,1	5,3	4,7	5,0	6,6	5,9	:	:
18. Long-term interest rate ⁽⁹⁾	7,2	8,1	9,0	7,9	7,8	6,9	5,9	5,8	6,3	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services.
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ M 3.

⁽⁹⁾ Levels.

GREECE

Resumption of growth as incomes and investment recover

During the two-year stabilization programme applied in Greece from the end of 1985, a strict incomes policy led to substantial real wage reductions which depressed domestic demand and helped to achieve a slowing in the inflation rate and an improvement in the current account of the balance of payments. In 1988, domestic demand has been strengthened by a more flexible wage policy and a revival in private investment. Despite some deterioration in the real foreign balance, real GDP growth is expected to be over 2½ % this year and could continue at a similar pace in 1989. Faster wage increases this year have meant relatively small further gains in inflation, with the average annual rate falling to about 13 % from 16 % in 1987 and 22 % in 1986. Despite some widening of the trade deficit, strong invisible receipts have maintained the improvement in the current account where all of the deficit is being covered by private capital inflows.

Weak economic performance since entry into the Community but progress since 1985

From the point of view of convergence with Community partners, Greek economic performance during the 1980s has been weak. On the real side, the ratio of GDP per head to the Community average has fallen back since 1980. The Greek inflation rate, despite the slowing since 1986, is still a matter of concern and makes necessary a continuous gradual depreciation of the drachma. Although there was some improvement in 1986 and 1987, insufficient progress has been made so far in correcting the imbalance in the public finances, and the general government deficit is still substantial.

Nonetheless, important advances have been made since the end of 1985 both from the point of view of structures and of stabilization. Labour cost increases have been moderated and, combined with the deregulation of goods markets, this has allowed a substantial recovery in profits, leading to a strengthening of business investment. Progress has also been

made towards the rationalization and simplification of the financial system by unifying interest rates and turning them positive in real terms; moreover, a large part of the PSBR has been financed through sales of debt to the non-bank private sector, thus facilitating monetary control. These positive developments have, however, made the servicing of the public debt more expensive and the reduction of the fiscal deficit even more difficult.

Need for further structural change and the continued pursuit of stability

Faster development and greater stability in the Greek economy will depend on tackling structural problems with an appropriate involvement of both the private and the public sectors. The start made in deregulating markets needs to be continued, with further emphasis on competition in financial and goods markets. The productive base needs to be strengthened through further encouragement of private investment, so as to improve competitiveness and trade performance. Priority must be given to reducing the public finance deficits, which pre-empt so much of the saving in the Greek economy. It is particularly the current budget deficit which must be limited, through restraint on government consumption and transfers and through spreading the tax burden more widely and fairly. Room must thus be created for both private investment and public infra-structure investment, notably in the context of the considerable expansion of Community interventions through the structural funds and lending. For the desired effects to be achieved, this must not be allowed to have a harmful effect on costs and prices. A phased reduction in the PSBR of at least 6 % of GDP is desirable over the next four to five years, and the Government has announced its intention to implement the policies required to reach such an objective and, notably, to reduce the budget deficit by 2 % of GDP already in 1989. Further progress on disinflation will also involve keeping a tight rein on wage developments, with real wage increases kept below productivity growth, and the maintenance of a tight monetary policy.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

GREECE

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	12,5	19,8	25,4	19,5	23,6	21,3	20,6	13,8	17,4	15,4
— at constant prices	7,7	3,0	0,4	0,4	2,8	3,0	1,3	-0,4	2,8	2,1
— price deflator	4,5	16,3	25,1	19,1	20,3	17,8	19,0	14,3	14,3	13,0
2. Gross fixed capital formation ⁽²⁾ :										
— total	10,0	-1,9	-1,9	-1,3	-5,7	5,1	-4,8	-3,2	8,8	8,0
— construction	:	-2,0	-13,2	5,4	-6,9	2,9	-3,3	-5,0	9,0	8,0
— equipment	:	0,5	14,1	-8,6	-4,1	7,6	-6,5	-0,9	8,5	8,0
3. Share of gross fixed capital formation in GDP ⁽³⁾ :										
— total	22,7	22,9	19,9	20,3	18,5	19,1	18,5	17,6	18,2	19,2
— general government	:	0,5	2,9	3,3	4,1	4,4	4,1	3,4	3,4	3,5
— other sectors	:	22,4	17,0	16,9	14,3	14,7	14,4	14,2	14,8	15,7
4. Final national uses including stocks:										
— at constant prices	8,2	2,1	3,5	0,8	-0,4	6,1	-0,5	0,2	3,5	3,0
— relative against 19 competitors	3,1	0,2	3,6	-1,0	-3,8	3,3	-4,1	-3,1	0,0	0,5
— relative against other Member States	3,3	0,4	3,2	-0,3	-2,6	3,8	-4,1	-3,1	0,0	0,4
5. Inflation (price deflator private consumption)	3,5	16,9	21,2	18,2	18,3	18,7	22,2	15,8	13,3	12,8
6. Compensation per employee:										
— nominal	10,2	21,2	27,8	21,3	22,3	22,6	15,7	12,5	17,0	14,0
— real, deflator private consumption	6,5	3,7	5,4	2,6	3,4	3,3	-5,4	-2,9	3,2	1,1
— real, deflator GDP	5,5	4,2	2,2	1,9	1,7	4,1	-2,8	-1,6	2,4	0,9
7. Productivity ⁽⁴⁾	8,2	1,7	1,2	-0,6	2,4	1,9	1,3	-0,3	1,7	1,3
8. Real unit labour costs ⁽⁵⁾ :										
— index: 1961 to 1973 = 100	100,0	96,3	105,8	108,5	107,7	109,9	105,5	104,1	104,7	104,3
— annual percentage change	-2,5	2,5	1,0	2,5	-0,7	2,1	-4,1	-1,3	0,6	-0,4
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	78,7	86,7	82,7	81,9	80,0	69,6	68,9	72,0	:
— annual percentage change	-4,2	1,0	8,3	-4,7	-0,9	-2,3	-12,9	-1,0	4,5	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	75,9	87,3	84,8	86,4	84,5	71,4	69,1	72,8	:
— annual percentage change	-4,6	1,2	11,2	-2,9	1,8	-2,1	-15,5	-3,2	5,4	:
11. Employment	-0,5	1,3	-0,8	1,0	0,3	1,0	0,1	-0,1	1,0	0,7
12. Unemployment rate ⁽⁶⁾	0,0	0,5	5,8	7,8	8,1	7,8	7,4	7,4	7,4	7,6
13. Current balance ⁽⁷⁾	-2,9	-1,7	-4,4	-5,0	-4,0	-8,2	-5,4	-3,4	-2,8	-3,7
14. Net lending of general government ⁽⁷⁾	:	-1,4	-7,7	-8,3	-10,0	-13,6	-10,8	-9,5	-12,1	-13,3
15. Gross debt of general government ⁽⁷⁾	:	26,8	38,7	44,3	53,2	62,6	64,6	66,7	69,4	73,9
16. Interest payments by general government ⁽⁷⁾	:	1,9	2,6	3,7	4,6	5,4	5,7	7,3	8,1	9,3
17. Money supply (end of year) ⁽⁸⁾	18,2	25,1	29,0	20,3	29,4	26,8	19,0	24,8	:	:
18. Long-term interest rate ⁽⁹⁾	0,7	11,9	15,4	18,2	18,5	15,8	15,8	17,2	18,0	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ M 3.

⁽⁹⁾ Levels.

SPAIN

Vigorous growth continues but inflation and competitiveness outlook is uncertain

Following the 1975 to 1985 recession, during which investment marked time and unemployment rose by 20 percentage points (from 2 to 22 %), Spain has been enjoying vigorous growth over the last three years. This renewed buoyancy is largely attributable to the beneficial effects of Community membership on the economic climate. Nonetheless, other factors have made a major contribution, viz. the decline in oil prices, the slower rate of increase in wage costs, and budgetary consolidation.

The progressive stabilization of the economy has produced a substantial fall in inflation, with the rise in the private consumption deflator slowing from some 15 % on annual average for the period 1975 to 1985 to 5 % in 1987. The growth rate of GDP is estimated to have been one of the highest in the Community and the prospects for continuing expansion in 1989 are favourable.

Domestic demand is expected to continue to expand rapidly, mainly in response to the buoyancy of investment. However, a large proportion of demand is spilling over into imports, which will probably show a further brisk rise. Since exports are now expanding at a more modest rate, the real external balance is once again likely to deteriorate. As a result, the growth rate of GDP is expected to be much lower than that of domestic demand but, even so, will probably be around 4 %. The growth in output should permit a further rapid rise (some 2 %) in the employed population. Nevertheless, since the labour force is expected to expand almost in step with employment, the unemployment rate will probably decline only marginally (from 20,1 % in 1988 to 19,8 % in 1989).

The current account, which dipped slightly into the red in 1988, is set to deteriorate further, with the deficit possibly widening to 2 % of GDP in 1989. A deficit of this magnitude would just about be covered by long-term capital inflows with the result that, given buoyant investment, it would constitute neither a problem nor a constraint for economic policy. With the introduction of tight budgetary controls and the rapid increase in tax revenue, the Spanish Government has, in recent years, carried through an almost exemplary policy of budget consolidation, including a substantial

reduction in net borrowing by general government. In 1989, the deficit will probably be roughly the same as in 1988 (equivalent to some 3 % of GDP).

Main economic policy tasks: closer convergence and further integration of Spain into the Community

The Government has set as its priority target rapid integration of the Spanish economy into the monetary cooperation arrangements within the EMS and participation at the earliest possible opportunity in the process of liberalizing capital movements. It is particularly important, therefore, to keep the Spanish economy on the path leading to convergence with the Community and, at the same time, to press ahead with efforts to narrow the gap between per capita GDP in Spain and the Community average. This necessitates the maintenance of a favourable climate for investment. A continuing process of disinflation, containment of wage costs, and competitiveness are key aspects of this strategy and, if they are to be achieved, the increase in nominal per capita wages must be severely curbed. This is all the more important in that the peseta's appreciation in recent years has already led to a substantial deterioration in the cost competitiveness of Spanish firms.

Growth in productive investment is a necessary condition for rapid, non-inflationary and job-creating growth in the years ahead. It will require the mobilization of substantial financial resources, and so the expansion of the structural funds and EIB lending answers a genuine need in the Spanish economy. The fact remains though that the objective of stepping up Community support for the Spanish economy can be achieved only if the extra resources available are reflected in a higher share of investment in GDP and do not cause costs and prices to rise. Macroeconomic policy will, therefore, have a prime role to play in guaranteeing successful implementation of the decisions taken by the Brussels European Council. This is because, with the availability of Community resources, continuation of the budgetary consolidation process would be welcome and feasible. A further reduction in the budget deficit would make it possible for monetary policy to contribute further to stabilizing the macroeconomic framework, notably through a reduction in monetary financing.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

SPAIN

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	14,8	19,1	15,2	13,6	12,9	11,2	14,6	11,3	10,2	8,4
— at constant prices	7,2	1,8	1,2	1,8	1,8	2,3	3,3	5,2	4,7	3,9
— price deflator	7,1	17,0	13,8	11,6	10,9	8,7	10,9	5,7	5,2	4,3
2. Gross fixed capital formation ⁽²⁾										
— total	10,4	-1,3	0,5	-2,5	-5,8	3,8	7,9	13,0	13,0	10,0
— construction	:	-1,5	0,1	-2,0	-5,3	2,0	6,6	10,5	12,0	8,6
— equipment	:	-0,4	2,2	-4,8	-7,3	8,5	10,4	19,0	14,3	11,9
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	24,2	23,9	21,3	20,6	18,8	18,9	18,7	20,1	21,5	22,7
— general government	:	2,2	3,1	2,8	3,0	3,7	3,5	3,6	3,8	3,9
— other sectors	:	21,7	18,2	17,7	15,7	15,1	15,2	16,5	17,8	18,8
4. Final national uses including stocks:										
— at constant prices	7,7	1,4	1,1	-0,1	-0,7	2,9	5,9	8,0	6,3	5,2
— relative against 19 competitors	2,7	-0,5	0,7	-1,9	-3,9	0,2	2,0	4,3	2,4	2,4
— relative against other Member States	2,9	-0,3	0,2	-1,1	-2,5	0,7	2,0	4,4	2,4	2,3
5. Inflation (price deflator private consumption)	6,6	17,5	14,5	12,3	11,0	8,3	8,7	5,3	4,7	4,3
6. Compensation per employee:										
— nominal	14,6	21,2	13,7	13,8	10,0	10,1	8,3	7,5	6,5	6,1
— real, deflator private consumption	7,5	3,2	-0,7	1,3	-0,9	1,7	-0,4	2,1	1,7	1,7
— real, deflator GDP	7,1	3,6	-0,1	1,9	-0,9	1,3	-2,3	1,7	1,2	1,7
7. Productivity ⁽⁴⁾	6,5	3,3	2,2	2,3	4,3	3,7	1,4	2,2	2,1	1,8
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	104,9	102,4	102,1	97,1	94,8	91,3	90,9	90,2	90,0
— annual percentage change	0,6	0,3	-2,2	-0,3	-4,9	-2,4	-3,7	-0,5	-0,8	-0,1
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	121,6	118,9	104,4	103,9	103,7	105,6	108,2	113,2	:
— annual percentage change	1,8	1,5	-3,1	-12,2	-0,5	-0,1	1,8	2,5	4,6	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	115,3	117,6	105,7	108,5	108,8	106,5	106,2	112,1	:
— annual percentage change	1,3	1,5	-0,4	-10,2	2,7	0,2	-2,1	-0,3	5,5	:
11. Employment	0,7	-1,5	-0,9	-0,5	-2,4	-1,4	1,9	3,0	2,6	2,1
12. Unemployment rate ⁽⁶⁾	0,4	6,3	16,2	17,7	20,1	21,4	21,0	20,5	20,0	19,6
13. Current balance ⁽⁷⁾	-0,2	-2,0	-2,5	-1,5	1,4	1,6	1,7	0,1	-0,8	-2,1
14. Net lending of general government ⁽⁷⁾	:	-1,3	-5,6	-4,8	-5,5	-7,0	-5,7	-3,6	-3,0	-2,9
15. Gross debt of general government ⁽⁷⁾	:	15,5	27,9	34,5	41,2	46,4	47,4	48,1	48,0	48,7
16. Interest payments by general government ⁽⁷⁾	:	0,6	1,0	1,3	2,0	3,2	3,9	3,6	3,5	3,3
17. Money supply (end of year) ⁽⁸⁾	6,8	18,6	16,6	15,9	13,1	12,8	12,6	13,9	:	:
18. Long-term interest rate ⁽⁹⁾	0,0	5,6	16,0	16,9	16,5	13,4	11,4	12,8	12,0	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ ALP.

⁽⁹⁾ Levels.

FRANCE

Following a period of adjustment in the productive system, the French economy is showing signs of increased dynamism

Since 1983, the French economy has been experiencing a difficult period of adjustment in the structures of the productive system and in the behaviour of economic agents. During this time, markets have become more flexible and freer (especially under the impact of price deregulation). The financial position of firms has recovered and the return on investment has improved. Moreover, a budgetary and monetary policy geared essentially to currency stability and budget consolidation has made a major contribution to curbing inflation and to significantly dampening down inflationary expectations.

As expected, the effects of this gradual improvement in the basic conditions for balanced, non-inflationary growth have taken some time to work through. However, since the beginning of the year, the economic climate has picked up appreciably; the share of investment designed to increase productive capacity is rising sharply and the net loss of jobs is giving way to some increase in the number of those gainfully employed. On the back of buoyant growth in investment and exports, GDP rose by over 3 % in 1988. Unlike in 1982 the revival in activity has taken place without jeopardizing either economic stability or the improvement in international competitiveness, as witnessed by the slight improvement in the current external balance and by the continuing slowdown in price increases.

All in all, the conditions for continuing, fairly rapid growth in 1989 are favourable. Higher investment will probably lead to an expansion in productive capacity and be accompanied by a gradual improvement in the situation on the labour market. The buoyancy of exports will probably make it possible to accommodate the fairly rapid increase in imports (notably capital goods) without any deterioration in the external balance. With activity picking up in the course of 1988, net borrowing by general government now seems likely to fall significantly between 1987 and 1988 and is expected to show a further, slight decline in 1989, as certain additional expenditure will be financed largely through higher tax revenue accruing from the new wealth tax in particular.

Main economic policy objective: to establish the basic conditions for stronger growth in the medium term

Even if the economic outturn in 1988 and in 1989 is much better than anticipated at the beginning of 1988, unemployment will continue to pose an acute problem and one of the main tasks of economic policy will be to reduce it. Given the prospect of a continuing, relatively rapid expansion in the labour force (due largely to the higher female participation rate), even growth of 3 % a year would

be insufficient to permit a reduction in unemployment unless employment responded more than in the past to the growth in output. It is essential, therefore, that new resources should be mobilized in support of investment aimed at creating extra capacity and harnessing new technologies. An increase in the share of investment in GDP will doubtlessly also be necessary if France is to exploit fully the extra growth potential created by completion of the internal market. Continuing wage restraint and a higher return on investment would seem, therefore, to be key elements of the medium-term economic strategy.

The continuing recovery in investment would be even more stimulated if the Government managed to bring long-term interest rates in France more closely into line with those in Germany. The differential that exists at the moment reflects in part expectations that exchange rates may be adjusted. It can, therefore, be eliminated only if financial markets and economic agents are more confident that the commitment to maintain a stable link between the French franc and the deutschmark is definitive and irrevocable.

Such greater confidence in the stability of the macroeconomic framework cannot be brought about by monetary policy alone. The thrust and implementation of budgetary policy, the functioning of the labour market and wage formation will all have a prime role to play in this respect. For its part, budgetary policy will need to take account of the general financial equilibrium and, more particularly, of the personal savings ratio, the decline of which in recent years may have helped to keep real interest rates high. If this ratio continued to fall at the rate observed over the last few years, this would, of course, contribute to the resurgence in domestic demand but would create a more precarious balance-of-payments situation and would bolster the arguments in favour of a cautious budgetary policy.

The budget strategy being pursued by the Government, even though it involves a different set of priorities for expenditure and tax cuts, follows on from previous governments' strategies regarding reduction of the deficit as a proportion of GDP and the trend of public debt. Since this strategy of budget consolidation is based on the assumption of buoyant business growth, its credibility would be enhanced if the policy on the structural adjustment of the economy were continued and strengthened. The lifting of the remaining restrictions on capital movements, decided recently by the Council, further accentuates the need for a budgetary policy and an adjustment policy that could facilitate the tasks of monetary policy.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

FRANCE

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	10,7	13,7	14,6	10,5	8,9	7,5	6,9	4,9	5,9	5,3
— at constant prices	5,6	2,6	2,5	0,7	1,4	1,7	2,1	2,3	3,1	2,8
— price deflator	4,9	10,8	11,7	9,7	7,5	5,7	4,7	2,5	2,7	2,5
2. Gross fixed capital formation ⁽²⁾ :										
— total	7,6	0,8	-1,4	-3,6	-2,3	1,1	3,0	3,4	6,9	5,4
— construction	:	0,1	-2,4	-3,6	-3,1	-0,9	1,9	2,2	4,5	3,4
— equipment	:	1,9	1,5	-3,4	0,2	4,6	3,8	4,4	8,8	6,8
3. Share of gross fixed capital formation in GDP ⁽³⁾ :										
— total	23,7	23,2	21,4	20,2	19,3	19,0	18,8	19,0	19,6	20,1
— general government	:	3,4	3,4	3,3	3,0	3,2	3,2	3,4	3,4	3,4
— other sectors	:	19,8	17,9	17,0	16,3	15,8	15,6	15,6	16,2	16,7
4. Final national uses including stocks:										
— at constant prices	5,8	2,3	3,5	-0,7	0,5	2,2	3,7	3,3	3,0	2,7
— relative against 19 competitors	0,9	0,5	3,8	-2,6	-3,1	-0,5	-0,1	-0,4	-1,0	-0,1
— relative against other Member States	1,1	0,8	3,5	-2,0	-1,8	0,1	-0,1	-0,3	-1,0	-0,2
5. Inflation (price deflator private consumption)	4,7	11,2	11,5	9,7	7,5	5,7	2,5	3,2	2,7	2,7
6. Compensation per employee:										
— nominal	9,9	14,8	14,1	10,1	8,6	6,6	4,0	3,3	3,8	3,8
— real, deflator private consumption	5,1	3,2	2,3	0,4	1,0	0,9	1,5	0,1	1,0	1,0
— real, deflator GDP	4,8	3,6	2,1	0,4	1,1	0,8	-0,7	0,7	1,0	1,3
7. Productivity ⁽⁴⁾	4,9	2,4	2,4	1,1	2,3	2,1	1,8	2,2	2,5	2,3
8. Real unit labour costs ⁽⁵⁾ :										
— index: 1961 to 1973 = 100	100,0	106,2	108,3	107,5	106,2	104,9	102,3	100,9	99,4	98,4
— annual percentage change	0,0	1,1	-0,3	-0,7	-1,2	-1,2	-2,5	-1,5	-1,4	-1,0
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	92,9	87,4	84,6	83,0	84,4	86,9	86,1	83,2	:
— annual percentage change	-0,9	0,1	-4,8	-3,2	-2,0	1,8	2,9	-0,9	-3,4	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	90,4	88,4	87,5	88,5	90,4	89,9	86,6	84,2	:
— annual percentage change	-1,3	0,2	-2,4	-1,0	1,1	2,2	-0,6	-3,7	-2,7	:
11. Employment	0,7	0,2	0,2	-0,4	-0,9	-0,4	0,3	0,1	0,6	0,5
12. Unemployment rate ⁽⁶⁾	1,1	5,1	8,7	8,9	10,0	10,5	10,7	10,8	10,7	10,8
13. Current balance ⁽⁷⁾	0,2	-0,4	-2,1	-0,8	0,0	0,1	0,6	-0,3	0,1	0,1
14. Net lending of general government ⁽⁷⁾	:	-1,0	-2,8	-3,2	-2,8	-2,8	-2,9	-2,5	-1,9	-1,8
15. Gross debt of general government ⁽⁷⁾	:	23,6	27,9	29,5	31,8	33,8	35,1	36,7	37,2	37,8
16. Interest payments by general government ⁽⁷⁾	:	1,3	2,0	2,6	2,7	2,9	2,9	2,8	2,9	2,9
17. Money supply (end of year) ⁽⁸⁾	13,7	13,4	11,4	11,5	9,5	6,8	6,3	7,3	:	:
18. Long-term interest rate ⁽⁹⁾	6,9	11,7	15,6	13,6	12,5	10,9	8,4	9,4	9,2	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ M 3 R.

⁽⁹⁾ Levels.

IRELAND

Great strides towards sustainability but growth is not yet sufficiently employment-creating

The Irish economy, which in the early 1980s had one of the highest inflation rates in the Community, a huge external deficit and spiralling public debt, has in the course of the last few years made great strides towards stability. In 1987, consumer price inflation was close to the Community average and the current external account was in surplus for the first time since 1967. Moreover, strong measures were initiated, backed by a broad political consensus, to rein in public expenditure and reduce the government budget deficit. Domestic demand declined in 1987 and has stagnated in 1988, in part reflecting the necessary stabilization policies. However, helped by the buoyancy of world trade and improvements in Irish competitiveness, export growth has been exceptionally strong, leading to GDP growth of 4 % in 1987 and near 3 % in 1988. The pattern of growth in 1989 is likely to be more broadly based and could lead to a further small increase in employment but, despite high emigration, the very high unemployment rate is likely to decline only marginally.

Achieving faster and more employment-creating growth remains a major challenge for the Irish economy

The medium-term challenge for the authorities is to further restore the conditions necessary to sustain a high rate of economic growth while maximizing the employment potential of such growth. Given the need to pursue the policy of fiscal consolidation for some time ahead, growth and employment will rely even more than in most other Member States on a supply-side response to a more favourable economic environment. The recent substantial decline in

nominal interest rates is an important first condition for such a response but other measures influencing the supply-side performance of the economy would seem appropriate. The efficient operation of markets is crucial to prospects for sustained growth and job creation. It is of even greater importance in the context of the completion of the internal market where flexibility in response to increased competition and changing market conditions will be essential. In the labour market, the provision of higher quality training, the encouragement of more flexible working patterns and some limited deregulation would help to convert improvements in output into higher employment. Deregulation should not, however, be confined to the labour market.

Consolidation of budgetary achievements the priority for 1989

Although the prospects for growth are brighter than for some years, the process of budgetary adjustment must continue to take precedence over other considerations to meet the Government's target of stabilizing the national debt/GDP ratio by 1990 (at about 120 % still one of the highest levels in the Community). A continuing reduction in the underlying exchequer borrowing requirement in terms of GDP is, therefore, desirable. This should once again be achieved by cuts in public expenditure, but with greater emphasis on restraining current rather than capital expenditure. The restructuring of taxation continues to be desirable and must be financed within the constraint of the necessary budgetary adjustment. Restraints on current expenditure will be all the more necessary, over the next few years, in view of the need to step up infrastructural investment in the context of the large increase in interventions through the Community's structural funds.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

IRELAND

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	11,8	19,7	17,8	9,7	11,1	6,1	5,3	6,6	5,2	6,5
— at constant prices	4,4	4,3	2,3	-0,6	3,2	1,1	-0,3	4,1	2,9	3,2
— price deflator	7,1	14,8	15,2	10,4	7,7	5,0	5,6	2,5	2,3	3,2
2. Gross fixed capital formation ⁽²⁾										
— total	10,0	4,6	-3,4	-9,3	-2,4	-4,4	-3,5	-1,0	0,4	3,6
— construction	:	4,3	-4,8	-12,2	-13,5	-7,5	-5,3	-6,5	-6,9	1,0
— equipment	:	5,6	-5,8	-5,0	9,2	4,9	0,3	3,6	6,0	5,4
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	21,2	26,7	26,5	23,3	21,7	20,4	18,7	17,5	17,2	17,4
— general government	:	5,3	5,1	4,5	3,9	4,0	3,7	2,9	2,3	1,9
— other sectors	:	21,4	21,4	18,7	17,8	16,4	15,0	14,6	14,9	15,5
4. Final national uses including stocks:										
— at constant prices	5,4	3,5	-2,1	-2,9	0,2	-1,3	0,8	-1,5	-0,2	1,5
— relative against 19 competitors	1,4	2,1	-2,6	-5,2	-3,1	-4,0	-2,9	-5,1	-4,2	-1,2
— relative against other Member States	1,5	2,4	-3,0	-4,7	-1,9	-3,6	-2,9	-5,1	-4,3	-1,4
5. Inflation (price deflator private consumption)	6,0	16,6	15,3	8,6	9,4	4,5	3,6	3,1	2,1	2,8
6. Compensation per employee:										
— nominal	11,3	19,3	14,4	12,0	11,7	6,4	5,1	5,1	3,5	3,9
— real, deflator private consumption	5,0	2,3	-0,8	3,2	2,1	1,8	1,5	1,9	1,3	1,1
— real, deflator GDP	3,9	3,9	-0,7	1,5	3,8	1,3	-0,5	2,6	1,1	0,8
7. Productivity ⁽⁴⁾	4,3	3,3	2,3	1,3	5,2	3,3	0,1	4,2	2,9	2,8
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	101,4	98,0	98,1	96,8	94,9	94,4	92,9	91,3	89,5
— annual percentage change	-0,4	0,6	-2,9	0,2	-1,3	-1,9	-0,6	-1,5	-1,7	-2,0
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	95,8	100,9	102,9	101,3	101,7	107,0	102,6	98,9	:
— annual percentage change	0,3	-0,5	3,3	1,9	-1,5	0,4	5,2	-4,0	-3,7	:
— against other Member States										
— index: 1961 to 1973 = 100	100,0	93,0	100,5	104,4	105,5	106,2	108,2	101,3	98,1	:
— annual percentage change	0,1	-0,6	5,7	3,9	1,1	0,6	1,9	-6,3	-3,2	:
11. Employment	0,1	0,9	0,0	-1,9	-1,9	-2,2	-0,4	-0,1	0,0	0,4
12. Unemployment rate ⁽⁶⁾	4,8	8,4	12,3	14,9	16,6	17,9	18,2	19,2	18,7	18,2
13. Current balance ⁽⁷⁾	-2,5	-8,6	-10,6	-6,9	-6,0	-3,8	-2,4	1,3	2,6	3,5
14. Net lending of general government ⁽⁷⁾	:	-10,5	-13,7	-11,6	-9,6	-11,1	-11,0	-9,1	-6,5	-6,1
15. Gross debt of general government ⁽⁷⁾	:	70,9	87,2	97,3	102,1	105,0	116,5	119,8	123,3	124,9
16. Interest payments by general government ⁽⁷⁾	:	5,6	9,0	9,3	9,4	10,4	9,8	9,9	9,7	9,4
17. Money supply (end of year) ⁽⁸⁾	12,1	19,2	13,0	5,6	10,1	5,3	-1,0	10,9	:	:
18. Long-term interest rate ⁽⁹⁾	2,2	14,6	17,0	13,9	14,6	12,7	11,1	11,3	9,7	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ M 3.

⁽⁹⁾ Levels.

ITALY

Strong growth supported by productivity gains but difficult to sustain

Economic activity has expanded more rapidly in the past five years as a strict stance has been maintained on monetary policy and applied since 1983 on wages. In 1988, there has been a sharp acceleration in growth mainly because of the generalized recovery in economic activity within the Community. Real GDP could increase by nearly 4 %, which would be the highest growth rate since 1979. So far this development has had only a limited impact on employment as firms have been protecting their export competitiveness and preparing for the 1992 internal market by rationalizing their workforce. Consequently, demographic factors have continued to push up the unemployment rate.

The success in reducing inflation after the 1986 counter oil shock has gone no further in 1988, with the inflation rate stabilizing at 5 % from the end of 1987. Recently, substantial wage increases in some parts of the public sector have shown up the absolute necessity of keeping unit labour costs to the Community average and of finding an appropriate solution to the problem of the public sector deficit, which is among the highest in the Community. The pressure placed on the capital market by renewal of public debt increases the vulnerability of the economy to external influences, despite a very good export performance which should keep the external deficit within reasonable limits in 1988 (0,4 % of GDP) and in 1989 (0,6 %). However, the outlook is highly dependent upon the effective implementation of the medium-term plan to stabilize the public finances, which will probably imply a slight slowdown in activity in 1989.

A need to improve structural and financial balance

Recent economic performance has only slightly diminished the scale of the adjustments which are still necessary in both private and public sectors.

In 1987, the marked slowing in the price of capital goods helped to stimulate demand; this shift in relative prices has intensified the process of factor substitution. Thus, any strengthening of employment demand has been delayed and import penetration has increased as production of certain highly specialized capital goods has been abandoned where importing has become more attractive. Moreover, the prospect of the internal market and the competitive imbalances at international level reflecting real exchange rate differentials have intensified innovation and reorganization within the enterprise sector, which are now bringing some

benefits but which, in the absence of a stricter wage policy, could lead in due course to a narrowing of the productive base.

Moreover, the public debt (which exceeded 90 % of GDP in 1987) represents an element of instability because of its size and composition. Indeed, the average maturity of the debt is among the shortest in the Community, with renewal dates concentrated into the next two years; debt servicing will reach 8 % of GDP this year out of a borrowing requirement which can probably be limited to 11 % of GDP. So far, this situation has not proved totally unsustainable due essentially to the high savings rate of households and the rise in real interest rates.

Wage restraint and budgetary control necessary to lower interest rates

The medium-term outlook would suggest that all efforts should be made such that the rapidly approaching deadlines can be faced under less tight monetary conditions. Such an easing can only occur if there is stricter control of inflation and public sector borrowing. Against the background of a much wider opening of markets for goods and capital, it will be essential to keep nominal wages in line with those elsewhere in the Community, and future wage negotiations must take this into account. Indeed, relative production costs will prove a decisive factor in the distribution of the benefits offered by the 1992 internal market.

A good performance in a unified internal market will largely depend on budgetary policy and on the effective implementation of the medium-term stabilization plan which the Government presented to parliament at the end of May. The effort to control the level of public debt must be accompanied by a parallel improvement in the quality of public services, which determine the efficiency and competitiveness of the entire economic system. It is evident that countries which continue having pronounced structural disequilibria in a unified internal market will be forced to adjust very quickly and at a high cost. The Government's programme and the 1989 Finance Law clearly aim at avoiding such difficulties. The action under way is of particular importance in order to ensure that completion of the internal market provides a room for manoeuvre that can be fully used for the development of productive capacity and employment.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

ITALY

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	11,0	20,8	16,5	15,9	14,1	11,8	11,0	8,7	8,7	7,5
— at constant prices	5,3	2,6	0,2	0,5	3,5	2,7	2,7	3,1	3,9	3,2
— price deflator	5,4	17,7	16,2	15,3	10,2	8,8	8,0	5,4	4,6	4,1
2. Gross fixed capital formation ⁽²⁾										
— total	4,3	0,5	-5,7	-1,6	4,4	3,3	1,2	5,2	4,9	3,8
— construction	:	-0,3	-6,7	0,9	0,5	-0,4	-0,6	-1,3	1,2	1,7
— equipment	:	3,0	-6,8	-5,7	15,1	11,4	5,0	11,5	8,0	5,5
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	25,9	24,4	22,3	21,3	21,2	21,2	20,1	20,0	20,1	20,1
— general government	:	3,0	3,7	3,7	3,6	3,8	3,6	3,5	3,6	3,6
— other sectors	:	21,4	18,6	17,5	17,6	17,4	16,6	16,5	16,5	16,5
4. Final national uses including stocks:										
— at constant prices	5,5	2,0	0,3	-0,5	4,5	3,2	3,6	4,6	4,4	3,5
— relative against 19 competitors	0,6	0,2	0,1	-2,5	1,2	0,5	-0,2	1,2	0,7	0,8
— relative against other Member States	0,7	0,5	-0,4	-1,8	2,9	1,1	-0,2	1,3	0,7	0,7
5. Inflation (price deflator private consumption)	4,8	17,6	15,9	14,8	11,4	9,3	6,1	4,8	4,9	4,6
6. Compensation per employee:										
— nominal	11,6	20,5	16,2	16,0	11,4	10,2	7,7	8,7	7,0	7,5
— real, deflator private consumption	6,5	2,5	0,2	1,0	0,0	0,8	1,5	3,8	1,9	2,7
— real, deflator GDP	5,9	2,4	0,0	0,6	1,1	1,3	-0,3	3,1	2,2	3,2
7. Productivity ⁽⁴⁾	5,7	1,9	-0,3	0,0	2,7	1,3	1,9	3,2	3,4	2,6
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	107,5	107,8	108,5	106,8	106,7	104,3	104,3	103,1	103,7
— annual percentage change	0,2	0,5	0,3	0,6	-1,6	-0,1	-2,2	-0,1	-1,1	0,6
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	89,2	92,8	99,9	99,2	99,0	105,2	109,4	106,5	:
— annual percentage change	-0,3	-0,3	1,4	7,6	-0,7	-0,2	6,3	3,9	-2,6	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	85,8	93,6	103,6	106,4	106,6	109,0	110,0	108,0	:
— annual percentage change	-0,8	-0,2	4,4	10,7	2,7	0,1	2,3	0,9	-1,8	:
11. Employment	-0,4	0,7	0,6	0,5	0,8	1,4	0,8	-0,1	0,5	0,6
12. Unemployment rate ⁽⁶⁾	5,2	6,2	9,7	11,0	12,0	12,9	13,7	14,0	15,0	14,5
13. Current balance ⁽⁷⁾	1,5	-0,7	-1,6	0,3	-0,6	-0,9	0,8	-0,1	-0,4	-0,6
14. Net lending of general government ⁽⁷⁾	:	-8,4	-11,3	-10,6	-11,5	-12,5	-11,4	-10,5	-10,0	-10,0
15. Gross debt of general government ⁽⁷⁾	:	58,7	66,3	71,9	77,1	83,7	87,9	92,6	96,6	101,4
16. Interest payments by general government ⁽⁷⁾	:	4,5	7,1	7,5	8,0	8,0	8,5	8,2	8,4	8,9
17. Money supply (end of year) ⁽⁸⁾	15,4	18,5	18,0	12,3	12,1	11,1	9,4	8,3	:	:
18. Long-term interest rate ⁽⁹⁾	7,0	14,2	20,9	18,0	15,0	14,3	11,7	11,3	12,1	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ M 2 N.

⁽⁹⁾ Levels.

LUXEMBOURG

The restructuring of the Luxembourg economy has slightly reduced its dependence on international market conditions for steel, but nevertheless economic policy still has limited room for manoeuvre

The restructuring of the Luxembourg economy which began some 10 years ago has reduced the steel industry's relative importance; it has permitted the diversification of the economic structure by means of the more rapid establishment of foreign firms and the development of financial and other services.

The increase in economic activity, underpinned by the buoyancy of exports, remained in 1988 close to the Community average, despite a certain slowdown in domestic demand. The pace of growth of GDP should decline only marginally in 1989: the increase of exports, in particular of steel, should slow down but private consumption, sustained by a significant rise in wages will probably be rather buoyant.

The absence of a domestic market of any size makes the Luxembourg economy heavily dependent on developments in the international environment. Overall growth and the increase in employment will therefore hinge on the way in which activity develops in the neighbouring countries. The pursuit of a prudent economic policy, with the aim of diversifying structures and safeguarding the competitiveness, should enable Luxembourg to maintain a growth rate close to that of the Community as a whole without disturbing existing equilibria.

A continuing policy of diversification of economic structures should also prevent the replacement of the steel industry by the financial sector as the dominant one. Because of the importance of small and medium-sized enterprises, it is difficult to intensify scientific research activities on an individual basis; this is why a development of centres of technology, as provided for by a recent law, is very important. The introduction of new technologies as part of the restructuring process, will require increased efforts to improve the skills and vocational training.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

LUXEMBOURG

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	8,7	8,0	12,1	10,0	12,5	7,3	5,5	3,5	5,1	5,2
— at constant prices	4,2	1,2	1,5	3,0	6,5	3,8	2,9	2,4	2,9	2,4
— price deflator	4,3	6,7	10,4	6,9	5,6	3,4	2,6	1,1	2,2	2,7
2. Gross fixed capital formation ⁽²⁾										
— total	5,1	-1,1	0,4	-10,9	-2,3	-3,7	15,8	16,4	-6,3	1,7
— construction	:	-1,4	-1,3	-12,9	-5,3	0,0	7,7	4,6	5,2	1,9
— equipment	:	1,3	0,6	-9,2	0,8	0,0	7,9	3,9	-1,4	1,5
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	26,4	25,4	25,2	21,6	19,6	18,1	20,7	23,8	21,8	21,8
— general government	:	6,4	6,7	6,0	4,9	4,7	4,9	5,0	4,9	5,0
— other sectors	:	19,0	18,5	15,6	14,7	13,4	15,8	18,9	16,9	16,8
4. Final national uses including stocks:										
— at constant prices	4,2	1,8	0,7	0,3	4,1	0,7	-0,9	6,1	0,6	2,5
— relative against 19 competitors	:	:	:	:	:	:	:	:	:	:
— relative against other Member States	:	:	:	:	:	:	:	:	:	:
5. Inflation (price deflator private consumption)	3,0	7,5	10,8	8,9	5,5	5,2	0,6	0,6	1,4	2,2
6. Compensation per employee:										
— nominal	7,4	10,7	6,9	6,9	7,1	3,8	5,0	3,9	3,4	5,0
— real, deflator private consumption	4,2	2,9	-3,5	-1,9	1,5	-1,4	4,3	3,3	1,9	2,8
— real, deflator GDP	2,9	3,7	-3,1	0,1	1,4	0,3	2,4	2,8	1,2	2,2
7. Productivity ⁽⁴⁾	3,1	0,6	1,8	3,3	5,9	2,4	0,3	-0,4	0,9	0,9
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	117,4	115,7	112,1	107,4	105,2	107,5	110,9	111,2	112,7
— annual percentage change	-0,2	3,1	-4,8	-3,1	-4,2	-2,0	2,1	3,2	0,3	1,3
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:	:	:	:	:	:	:	:	:	:	:
— against other Member States:	:	:	:	:	:	:	:	:	:	:
11. Employment	1,1	0,6	-0,3	-0,3	0,6	1,4	2,6	2,7	1,9	1,6
12. Unemployment rate ⁽⁶⁾	0,0	0,5	1,3	1,6	1,8	1,7	1,4	1,6	1,4	1,3
13. Current balance ⁽⁷⁾	6,8	21,4	35,2	39,6	39,5	43,3	46,1	38,0	38,6	36,4
14. Net lending of general government ⁽⁷⁾	:	1,4	-1,2	1,6	2,9	5,8	6,0	5,2	5,3	6,2
15. Gross debt of general government ⁽⁷⁾	:	15,7	14,5	14,8	14,8	14,4	14,7	14,9	14,7	13,0
16. Interest payments by general government ⁽⁷⁾	:	0,9	1,0	1,1	1,2	1,3	1,3	1,4	1,2	1,1
17. Money supply (end of year) ⁽⁸⁾	:	:	:	:	:	:	:	:	:	:
18. Long-term interest rate ⁽⁹⁾	0,5	7,2	10,3	9,8	10,3	9,5	8,7	8,0	0,0	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ Levels.

THE NETHERLANDS

The adjustment of economic structures is continuing and growth is again approaching the Community average

As a result of the shift in economic policy since the autumn of 1982, a number of imbalances (including the imbalance in the public finance situation) have gradually been reduced, the level of investment and employment has been raised and the GDP growth rate is again approaching that of the Community partner countries.

During 1988 and 1989 the Dutch economy is continuing the restructuring process while taking full advantage of the renewed buoyancy of the world economy in general and of intra-Community trade in particular. In 1988, the acceleration of export demand and the large increase in investment are compensating for a slowdown in private consumption, which is partly due to the effects of a more moderate growth of real disposable income. The GDP growth rate could exceed 2% in real terms, and should accelerate slightly in 1989.

The central government budget deficit is being reduced in line with the forecasts of the government programme and the borrowing requirement will fall to 6,7% of NNI (net national income) in 1988 and to 6,0% in 1989 ⁽¹⁾. Due to higher-than-expected tax revenues, the Government is able to reduce tax rates in 1988 and 1989 despite the fact that the level of expenditure forecast in the multiannual programme will somewhat overshoot. The target set in the government declaration with respect to the overall tax burden is, therefore, likely to be achieved. However, the progress made on the unemployment rate is distinctly, less rapid than forecast, despite sustained employment growth.

The emphasis on consolidation should continue beyond 1989 in order to guarantee balanced growth in the medium term

Efforts to reduce rigidities in the operation of the labour market and to make the system of production more flexible will have to be continued beyond 1989, in order to make it easier to adjust to the new conditions of competition in the context of the single European market. This presupposes, *inter alia*, that the budget deficit will be further reduced, a condition necessary to stop the growth of the public debt as a proportion of GDP, and that tax rates will be brought more into line with those of other Member States.

Better control of budget expenditure by limiting government intervention and its cost should open the way to tax reform which, from 1990, should considerably simplify the taxation system. In the meantime, care must be taken to ensure that the higher-than-expected tax revenues now being recorded do not give rise to excessive overshooting of the expenditure forecast in the multiannual programme. In this respect, the reduction of VAT rates whose purpose it is to maintain purchasing power and to contribute to the harmonization of taxation envisaged in connection with the establishment of the internal market at the end of 1992 can be seen as a positive measure. Certain other measures are also positive, in particular those which aim to reduce public authority spending on sickness and invalidity insurance and the housing market.

Already some success has been achieved in reducing unemployment: the fight against unemployment will have to be continued chiefly by raising the investment rate, maintaining wage moderation and by selective measures to bring certain categories of unemployed persons back into the productive process more quickly.

⁽¹⁾ 6,1% and 5,4% of GDP, respectively.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

NETHERLANDS

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	11,2	9,1	4,5	3,3	5,0	4,1	3,1	0,4	2,4	3,8
— at constant prices	4,8	2,0	-1,4	1,4	3,2	2,3	2,4	1,5	2,2	2,3
— price deflator	6,0	6,9	6,0	1,9	1,8	1,7	0,7	-1,0	0,3	1,5
2. Gross fixed capital formation ⁽²⁾										
— total	5,3	-1,6	-4,1	2,1	5,4	5,2	7,2	1,6	3,3	2,9
— construction	:	-1,9	-6,6	-3,4	4,1	-3,5	4,1	2,9	4,9	0,3
— equipment	:	-0,2	-0,1	10,1	9,4	17,4	9,8	0,1	1,4	6,1
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	25,1	20,8	18,2	18,2	18,6	19,0	19,6	19,8	20,3	20,4
— general government	:	3,4	2,9	2,7	2,8	2,6	2,4	2,3	2,3	2,2
— other sectors	:	17,3	15,3	15,6	15,8	16,3	17,2	17,4	18,0	18,2
4. Final national uses including stocks:										
— at constant prices	4,9	1,5	-0,9	1,5	1,7	2,5	3,9	2,2	1,9	1,9
— relative against 19 competitors	0,1	-0,2	-1,0	0,0	-1,2	0,1	0,2	-1,3	-1,9	-0,7
— relative against other Member States	0,2	-0,1	-1,3	0,4	-0,3	0,5	0,2	-1,3	-1,9	-0,8
5. Inflation (price deflator private consumption)	5,0	7,1	5,3	2,7	2,0	2,5	0,2	-0,4	0,9	1,4
6. Compensation per employee:										
— nominal	11,4	8,7	5,8	3,2	0,2	1,4	1,6	1,3	1,9	1,0
— real, deflator private consumption	6,0	1,6	0,5	0,4	-1,7	-1,1	1,4	1,6	1,0	-0,3
— real, deflator GDP	5,0	1,7	-0,3	1,3	-1,6	-0,3	0,8	2,3	1,6	-0,4
7. Productivity ⁽⁴⁾	3,9	1,9	1,1	3,4	3,2	1,0	0,6	0,3	1,3	1,4
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	105,4	101,1	99,1	94,5	93,3	93,5	95,4	95,7	94,0
— annual percentage change	1,0	-0,2	-1,3	-2,0	-4,6	-1,3	0,2	2,0	0,3	-1,8
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	122,7	113,7	110,7	102,3	99,3	104,4	107,8	105,4	:
— annual percentage change	2,9	-0,7	2,8	-2,6	-7,6	-3,0	5,2	3,2	-2,2	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	120,5	114,4	112,8	106,2	103,3	106,1	107,6	105,9	:
— annual percentage change	2,7	-0,6	4,5	-1,4	-5,8	-2,8	2,7	1,4	-1,6	:
11. Employment	0,9	0,1	-2,5	-1,9	-0,1	1,3	1,8	1,2	0,9	0,9
12. Unemployment rate ⁽⁶⁾	1,3	5,7	11,8	14,2	14,5	13,3	12,1	11,5	11,3	10,9
13. Current balance ⁽⁷⁾	0,5	1,0	3,2	3,1	4,2	4,3	2,8	1,7	1,6	1,8
14. Net lending of general government ⁽⁷⁾	:	-2,9	-7,0	-6,3	-6,2	-4,7	-6,0	-6,3	-5,2	-4,6
15. Gross debt of general government ⁽⁷⁾	:	42,8	55,6	62,0	66,1	69,6	71,1	75,0	79,4	82,2
16. Interest payments by general government ⁽⁷⁾	:	3,3	5,2	5,7	6,0	6,3	6,4	6,4	6,6	6,5
17. Money supply (end of year) ⁽⁸⁾	10,3	9,1	7,6	10,4	7,6	11,1	5,1	5,4	:	:
18. Long-term interest rate ⁽⁹⁾	5,9	9,7	10,5	8,8	8,6	7,3	6,4	6,4	6,5	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ M 2 N.

⁽⁹⁾ Levels.

PORTUGAL

Strong improvement in the macroeconomic performance but insufficient budgetary consolidation

After the phase of strong adjustment from 1982 to 1985 (during which the current external account shifted from a huge deficit to a surplus), the Portuguese economy has been expanding at a faster rate than recorded by other Member States. The growth of real per capita income has resumed, not least due to the substantial terms-of-trade gains resulting from the oil price decline, and business investment has staged a strong recovery, stimulated by the improvement of business sentiment and economic prospects following adhesion to the Community and a more stability-oriented economic policy. Moreover, the rate of increase in consumer prices which, as late as 1984, reached almost 30 % has been brought into single-digit figures. However, the consolidation of the public finances has been insufficient to halt the rise in the public debt/GDP ratio, and the further slowdown of inflation, aimed at by the authorities, has proved difficult to achieve.

The expansion of activity would seem likely to slow down by only a little in 1989: domestic demand is set to grow at a fast rate and while imports will rise strongly in response, the increase in domestic output is expected to remain high. There may be a further rise in employment but hardly more than necessary to absorb the rise in the labour force. Unemployment may show a small decline. The current external account is expected to fall into deficit to the tune of some 1½ % of GDP.

The main task: further budget consolidation and disinflation

The current rate of increase in consumer prices is considerably above the Community average and a

pronounced slowdown during the remainder of 1988 and 1989 is a high priority target of the Government. Such a slowdown is all the more important since a significant reduction of the inflation differential is to be seen as the main condition for a successful completion of the integration of Portugal into the Community and notably its eventual participation in the EMS.

For the rate of inflation to slow down in line with official intentions, a deceleration of the still excessively high increases in per capita wages is clearly necessary. It would, however, also seem essential that budgetary and monetary policy be used more actively to fight against inflation. A significant reduction of the general government borrowing requirement would, in fact, serve not only to dampen the rise in public debt but also to reduce the level of monetary financing thereby helping to keep real interest rates down. A resumption of the process of budget consolidation is also required to make room for the rise in budgetary resources needed to match the substantial increase in transfers from the Community's structural funds over the next few years. In this way, the additional financial resources would not cause new inflationary pressures in the economy.

However, the acceleration of the catching-up process will also depend strongly upon the ability of the Portuguese economy to adapt its structures and institutions to the changing conditions within the internal market. This will require not only further progress with respect to privatization and implementation of the already approved tax reform but also strong measures to improve the quality, skills and education of the labour force and to increase the flexibility of the labour market.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

PORTUGAL

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	11,1	23,2	23,3	24,4	21,9	25,7	23,0	17,3	15,0	11,8
— at constant prices	6,9	3,0	2,4	-0,3	-1,6	3,3	4,3	4,6	4,0	3,6
— price deflator	4,0	19,6	20,4	24,8	23,9	21,7	17,9	12,1	10,5	8,0
2. Gross fixed capital formation ⁽²⁾										
— total	7,8	1,4	2,9	-7,5	-18,0	-3,0	9,5	19,6	12,8	11,0
— construction	:	0,0	0,0	0,0	0,0	0,0	0,0	10,5	10,0	10,0
— equipment	:	0,0	0,0	0,0	0,0	0,0	16,0	30,0	15,5	12,0
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	24,1	27,2	31,1	29,2	23,9	21,7	21,6	24,3	26,4	28,2
— general government	:	1,0	3,4	3,1	2,6	2,5	2,6	2,7	2,7	2,9
— other sectors	:	26,1	27,7	26,1	21,3	19,3	19,0	21,6	23,6	25,2
4. Final national uses including stocks:										
— at constant prices	7,5	2,8	2,7	-7,4	-6,6	0,8	8,4	9,5	6,3	5,5
— relative against 19 competitors	2,7	1,1	2,3	-9,1	-9,5	-1,9	4,3	6,9	2,9	3,1
— relative against other Member States	2,9	1,4	2,0	-8,6	-8,4	-1,4	4,4	6,9	2,9	3,0
5. Inflation (price deflator private consumption)	3,4	21,9	20,6	25,3	27,8	19,0	12,0	10,2	9,4	7,0
6. Compensation per employee:										
— nominal	12,0	24,5	19,8	18,7	18,9	22,4	17,0	13,9	11,0	10,0
— real, deflator private consumption	8,3	2,2	-0,6	-5,2	-7,0	2,8	4,5	3,3	1,5	2,8
— real, deflator GDP	0,7	4,1	-0,5	-4,8	-4,0	0,6	-0,7	1,6	0,5	1,8
7. Productivity ⁽⁴⁾	7,4	2,7	2,8	-4,4	-0,1	3,6	4,3	1,8	2,3	2,7
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	123,9	112,6	112,0	107,7	104,5	99,5	99,3	97,5	96,7
— annual percentage change	0,3	1,4	-3,2	-0,5	-3,9	-2,9	-4,8	-0,2	-1,8	-0,8
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency										
— against 19 competitors										
— index: 1961 to 1973 = 100	100,0	108,3	89,1	83,3	79,3	80,0	80,0	80,8	81,4	:
— annual percentage change	-0,3	-1,1	-5,5	-6,5	-4,8	0,9	0,0	1,0	0,8	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	104,9	88,1	83,6	81,7	82,7	80,4	79,5	80,7	:
— annual percentage change	-0,8	-1,1	-3,6	-5,1	-2,4	1,3	-2,8	-1,0	1,5	:
11. Employment	-0,5	0,4	-0,4	4,3	-1,5	-0,3	0,0	2,7	1,7	0,9
12. Unemployment rate ⁽⁶⁾	0,0	5,1	5,7	5,6	8,6	8,7	8,7	7,2	6,5	6,4
13. Current balance ⁽⁷⁾	0,4	-6,8	-13,5	-8,3	-3,0	1,7	3,9	1,8	-0,1	-1,7
14. Net lending of general government ⁽⁷⁾	:	-0,4	-10,4	-9,1	-12,0	-10,1	-7,8	-8,4	-8,1	-7,8
15. Gross debt of general government ⁽⁷⁾	:	10,4	50,0	56,0	61,4	60,7	63,6	67,6	78,5	83,5
16. Interest payments by general government ⁽⁷⁾	:	1,0	5,5	6,4	7,1	7,9	9,3	8,0	8,2	7,9
17. Money supply (end of year) ⁽⁸⁾	9,9	21,6	24,6	16,3	24,5	29,8	25,8	16,8	:	:
18. Long-term interest rate ⁽⁹⁾	0,0	0,0	0,0	0,0	0,0	25,4	17,9	15,4	14,0	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services; ...
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ L.

⁽⁹⁾ Levels.

UNITED KINGDOM

Continued strong growth but signs of overheating

The United Kingdom economy has been growing at an annual rate of over 3 % for seven consecutive years. Its recent performance has exceeded expectations, with real GDP growth of almost 4 % likely this year. Unemployment, now at a rate close to 8½ %, has declined continuously since mid-1986 and labour market conditions have tightened appreciably. The construction sector is booming. Business investment has picked up sharply, in a lagged response to the steep increase in profitability.

However, the pace of growth has caused fears of overheating. Capacity utilization has reached a high level. The fast rate of growth reflects the coincidence of an investment surge with continuing buoyancy of private consumption, which has been fuelled by strong growth in real earnings and a rapid expansion in credit. The 12-month rate of increase in the retail prices index has edged upwards from its 3 to 4 % range in 1987 towards 6 % in the latter part of 1988, partly because of the impact of higher mortgage payments. Demand has outstripped the economy's immediate capacity to respond and has increasingly spilled over into imports, the growth of exports has slowed this year and the deficit on the current account of the balance of payments has widened rapidly.

An improving supply-side performance but little progress on disinflation

Although growth has been unsustainably fast over the past year or so, the underlying economic performance of the UK in many respects now compares favourably both with earlier experience and with other Member States. That structural adjustment policies have progressed much further in the UK is evident not only in the rapid catch-up in manufacturing productivity towards best Community levels but also in the job-creating capacity of the economy. Since 1983 employment has increased by over 1½ % per year, though appreciable regional disparities still persist. Corporate profitability has steadily improved. Moreover, through effective control of expenditure the public accounts have moved into surplus and a good deal of progress has been made in the field of tax reform. In particular, there has been a considerable simplification of the personal income tax system, with now only two much-reduced tax rates of 25 % and 40 %.

The fast growth of demand has meant that little further progress has been made on limiting inflation recently. Annual growth in average earnings, having remained stubbornly close to 7½ % since 1983, accelerated to 9 % by mid-1988 (explained partly by more overtime working, bonus payments and a catching-up in public sector wages). Productivity gains have so far offset the effects of earnings

growth, especially in manufacturing; but these gains are partly cyclically related and will thus taper off when output growth slows, so that unless wage increases slow correspondingly they will increasingly spill over into costs and prices. The rigidity of the wage formation process, with its implications for inflation and competitiveness, remains one of the key problems for the UK economy.

Will the present policy mix put sufficient downward pressure on inflation?

Over the medium term some of the imbalances in the economy will be self-righting. The sharp pick-up in business investment implies a considerable increase in the supply potential of the economy. As economic growth slows and corporate profits rise less quickly, firms may no longer be prepared to concede such high wage increases. In addition, personal saving can be expected to recover as higher interest rates and a cooling in financial and real asset markets lessen the willingness to take on additional debt. Nevertheless, it remains to be seen how strong an effect these factors will have on inflation and the current account deficit.

This raises the question of how best to use any margin available for fiscal manoeuvre. In particular, caution is desirable in phasing in the further reductions in the basic rate of income tax to which the Government is committed. To avoid too rapid an expansion of demand and to contain inflationary pressures it may be necessary to continue a public sector surplus for several years. Part of any fiscal margin could be used in ways which would further improve supply-side potential but with less direct impact on private consumption and imports, for example by reducing the cost to employers of taking on additional labour and increasing the post-tax return on investment.

Although there was some overall tightening of monetary policy in the early part of 1988, interest rates were reduced as sterling was subject to strong upward pressure, partly speculative. Since June, interest rates have risen by 4½ percentage points in total, marking a further substantial tightening of policy. This will help keep inflationary pressures in check. The recent rises in interest rates have been accompanied by relative stability in sterling though at higher rates against other European currencies than at the beginning of the year. Over the medium term, a tight fiscal policy stance should enable monetary growth to be restrained without the use of very high interest rates, the persistence of which could affect investment. Monetary policy should also be consistent with the aim of greater exchange rate stability.

Main economic aggregates, 1961 to 1989 ⁽¹⁾

UNITED KINGDOM

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	8,4	16,7	8,7	8,9	6,4	9,9	6,6	9,4	9,7	8,4
— at constant prices	3,1	0,7	1,1	3,5	2,0	3,0	2,9	4,3	3,8	2,6
— price deflator	5,1	15,9	7,6	5,2	4,2	6,0	3,5	4,9	5,6	5,7
2. Gross fixed capital formation ⁽²⁾										
— total	4,6	-1,8	5,2	5,2	8,2	3,1	0,3	5,5	9,6	6,3
— construction	:	-3,2	8,3	5,3	7,0	-2,9	4,4	4,2	9,8	5,8
— equipment	:	0,1	1,5	4,9	9,6	9,9	-3,9	6,9	9,3	6,9
3. Share of gross fixed capital formation in GDP ⁽³⁾										
— total	18,5	18,8	16,2	16,2	17,3	17,2	17,2	17,4	18,4	19,1
— general government	:	3,4	1,6	2,0	2,1	2,0	1,8	1,5	1,6	1,6
— other sectors	:	15,4	14,6	14,2	15,2	15,3	15,4	15,9	16,8	17,5
4. Final national uses including stocks:										
— at constant prices	3,2	0,1	2,2	4,5	2,7	2,9	3,8	4,3	5,3	3,5
— relative against 19 competitors	-2,0	-1,9	2,4	2,7	-0,9	0,2	0,0	1,5	3,0	0,9
— relative against other Member States	-1,9	-1,7	2,0	4,1	0,9	0,9	0,0	1,7	3,3	0,8
5. Inflation (price deflator private consumption)	4,8	15,1	8,6	5,0	4,8	5,2	3,6	3,8	4,4	4,7
6. Compensation per employee:										
— nominal	8,3	17,1	8,4	8,7	5,3	6,7	7,3	7,0	7,5	7,8
— real, deflator private consumption	3,3	1,7	-0,2	3,5	0,5	1,4	3,6	3,0	3,0	2,9
— real, deflator GDP	3,0	1,0	0,8	3,3	1,1	0,7	3,7	2,0	1,9	2,0
7. Productivity ⁽⁴⁾	2,9	1,1	2,9	4,8	0,1	2,1	2,5	2,6	1,9	1,6
8. Real unit labour costs ⁽⁵⁾										
— index: 1961 to 1973 = 100	100,0	103,0	99,0	97,6	98,5	97,1	98,2	97,6	97,6	98,0
— annual percentage change	0,2	-0,1	-2,1	-1,4	0,9	-1,4	-1,1	-0,6	0,0	0,4
9. Profitability (index: 1961 to 1973 = 100)	:	:	:	:	:	:	:	:	:	:
10. Relative unit labour costs in common currency:										
— against 19 competitors:										
— index: 1961 to 1973 = 100	100,0	90,3	105,5	97,5	95,0	95,7	90,0	90,5	98,1	:
— annual percentage change	-1,9	3,8	-6,5	-7,6	-2,6	0,8	-6,0	0,5	8,5	:
— against other Member States:										
— index: 1961 to 1973 = 100	100,0	83,7	105,3	99,3	100,7	102,0	89,8	86,6	95,8	:
— annual percentage change	-2,9	4,3	-3,6	-5,7	1,4	1,3	-12,0	-3,6	10,7	:
11. Employment	0,3	-0,4	-1,8	-1,2	1,9	1,6	0,4	1,7	1,9	1,0
12. Unemployment rate ⁽⁶⁾	2,1	5,1	10,6	11,6	11,8	12,0	12,0	10,6	8,6	7,2
13. Current balance ⁽⁷⁾	-0,1	-0,5	1,3	0,8	-0,3	0,5	-0,8	-0,6	-3,1	-3,3
14. Net lending of general government ⁽⁷⁾	:	-3,7	-2,5	-3,3	-3,9	-2,7	-2,4	-1,4	-0,3	-0,1
15. Gross debt of general government ⁽⁷⁾	:	55,8	57,4	57,1	58,4	57,2	56,1	53,2	49,3	46,1
16. Interest payments by general government ⁽⁷⁾	:	4,4	5,0	4,7	4,9	4,9	4,6	4,3	3,9	3,6
17. Money supply (end of year) ⁽⁸⁾	9,5	12,1	8,9	10,4	10,0	13,4	18,9	22,5	:	:
18. Long-term interest rate ⁽⁹⁾	7,6	13,9	12,7	10,8	10,7	10,6	9,8	9,5	9,5	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ At current prices.

⁽⁴⁾ GDP at constant market prices per person employed.

⁽⁵⁾ Deflator GDP.

⁽⁶⁾ Percentage of civilian labour force.

⁽⁷⁾ Percentage of GDP.

⁽⁸⁾ M 3.

⁽⁹⁾ Levels.

ANNUAL ECONOMIC REPORT 1988 TO 1989

Preparing for 1992

— STATISTICAL ANNEX —

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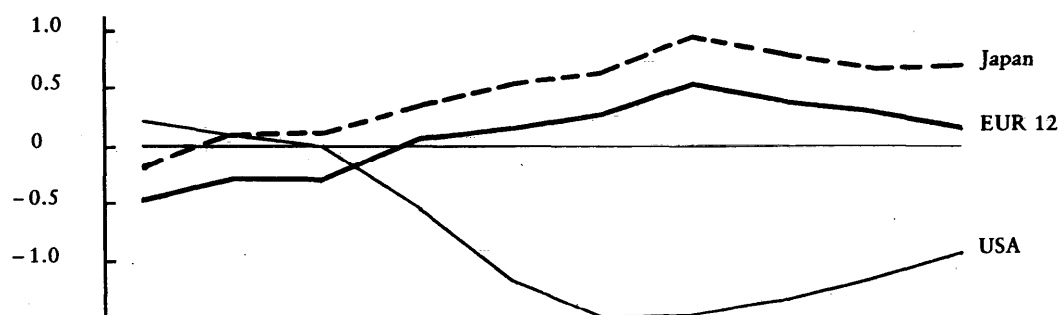
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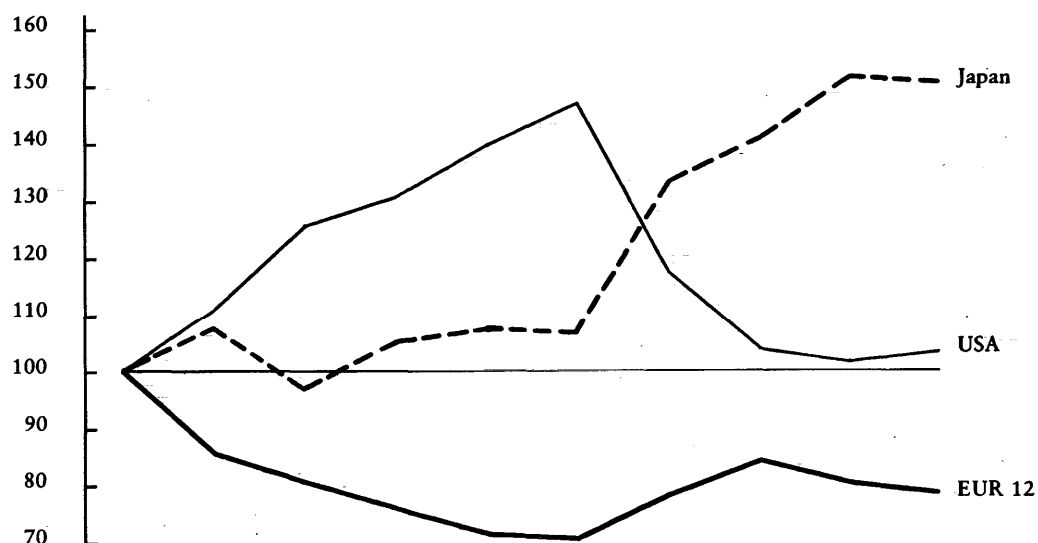
⁽¹⁾ 1988 to 1989: Economic forecasts, September to October 1988.

GRAPH A1
Current balances and determinants

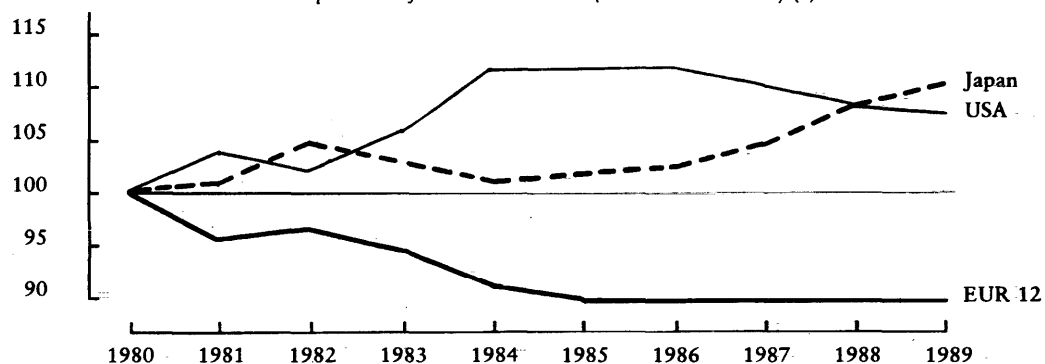
Balance on current transactions as % of total GDP of the three main economic zones



Real effective exchange rates (index 1980 = 100)



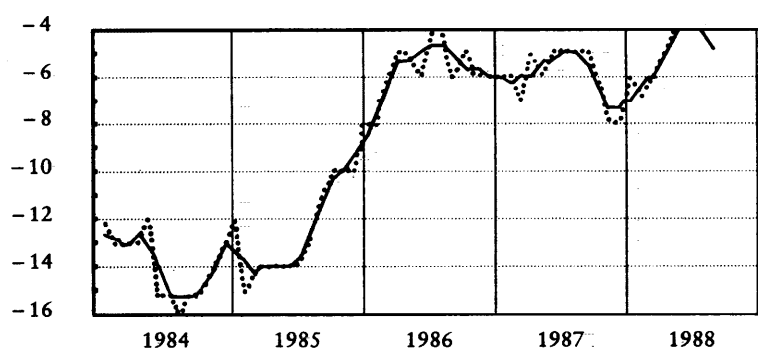
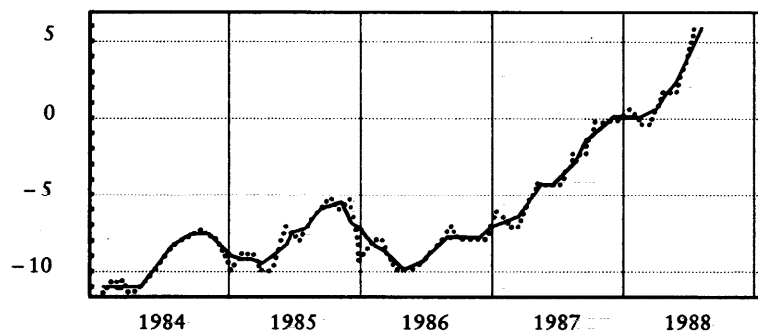
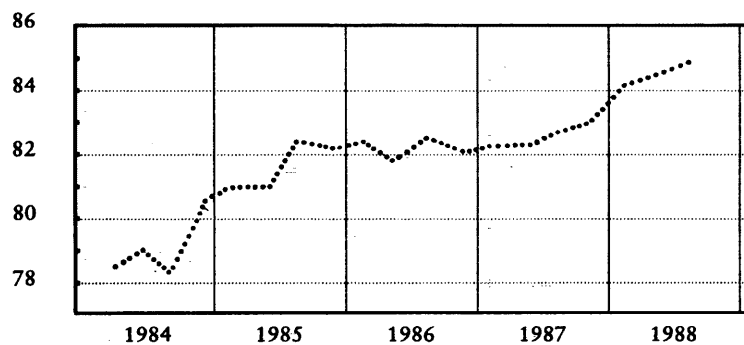
Relative position of domestic demand (index 1980 = 100) ⁽¹⁾



⁽¹⁾ Index of domestic demand of the country or economic zone concerned in relation to those of its trading partners.

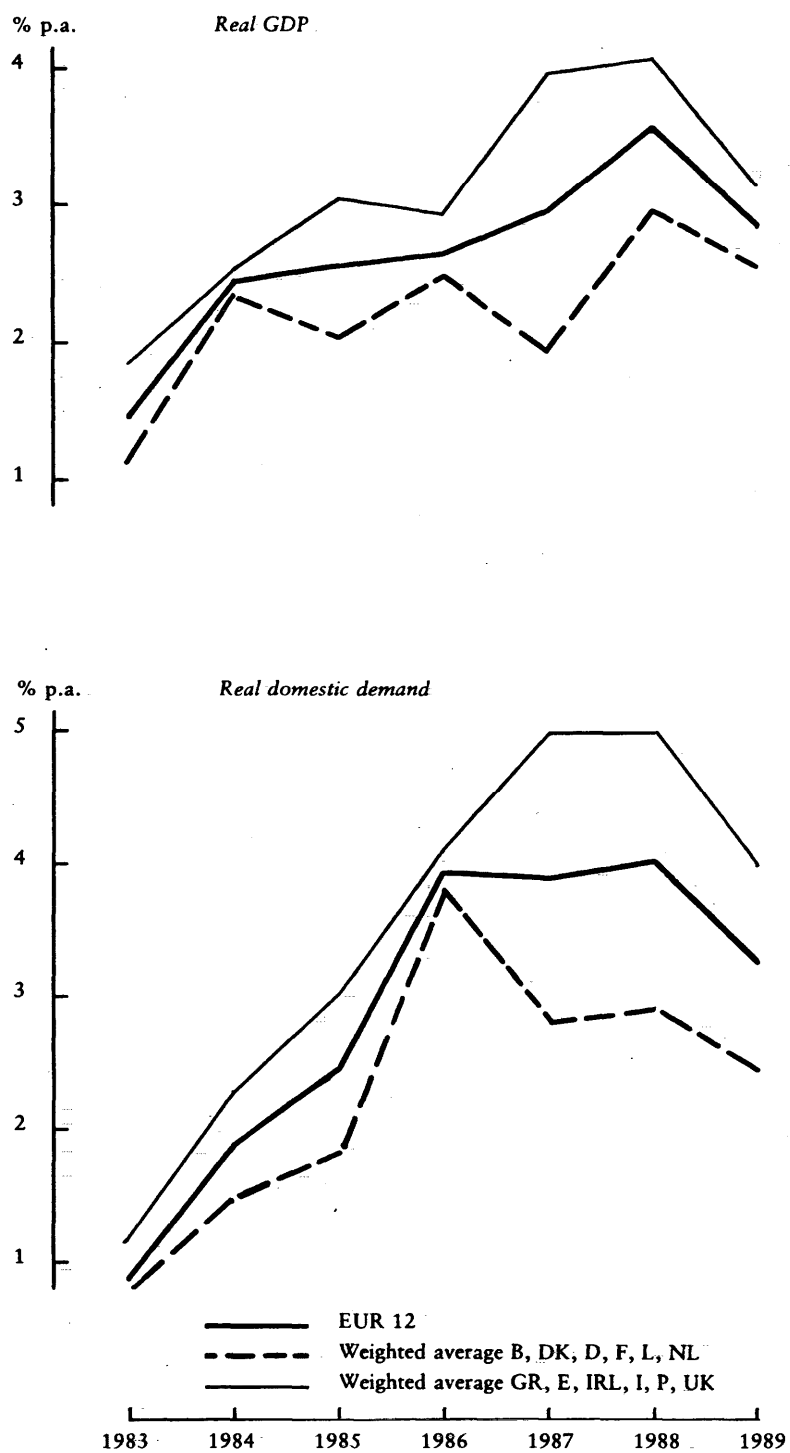
GRAPH A2

Principal results of Community business and consumer surveys (EUR 12)

Consumer confidence indicator (balance) (three-month moving average)*Industrial confidence indicator (balance, s.a.) (three-month moving average)**Capacity utilization in manufacturing (degree in %)*

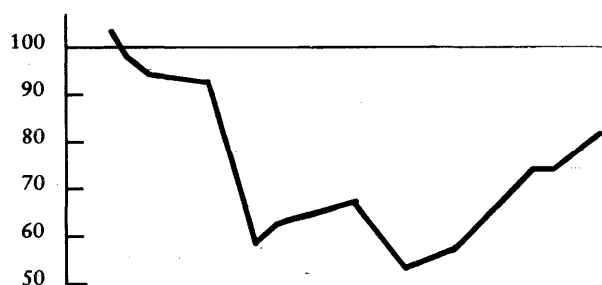
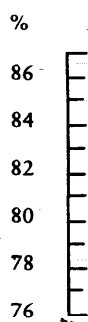
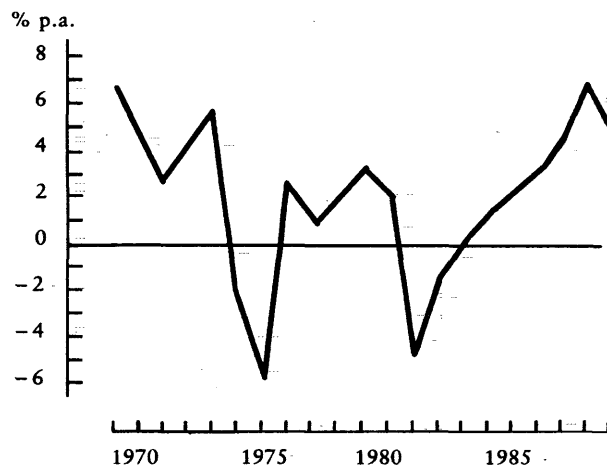
GRAPH A3

Growth of real GDP and domestic demand



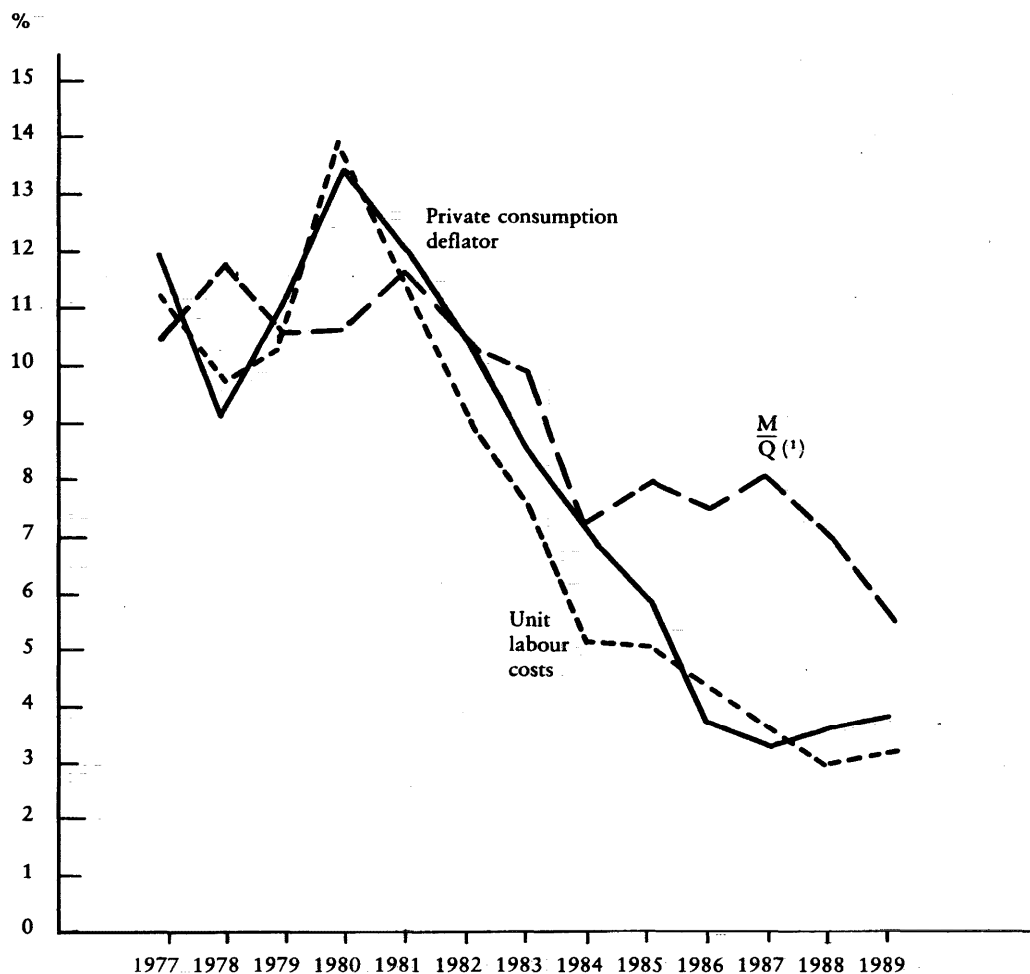
GRAPH A4

Profitability, capacity utilization and investment (EUR 12)

Profitability of fixed capital in the whole economy (index 1960 = 100)*Capacity utilization in manufacturing industry ⁽¹⁾**GFCF in volume, annual % change in the whole economy*⁽¹⁾ Business surveys.

GRAPH A5

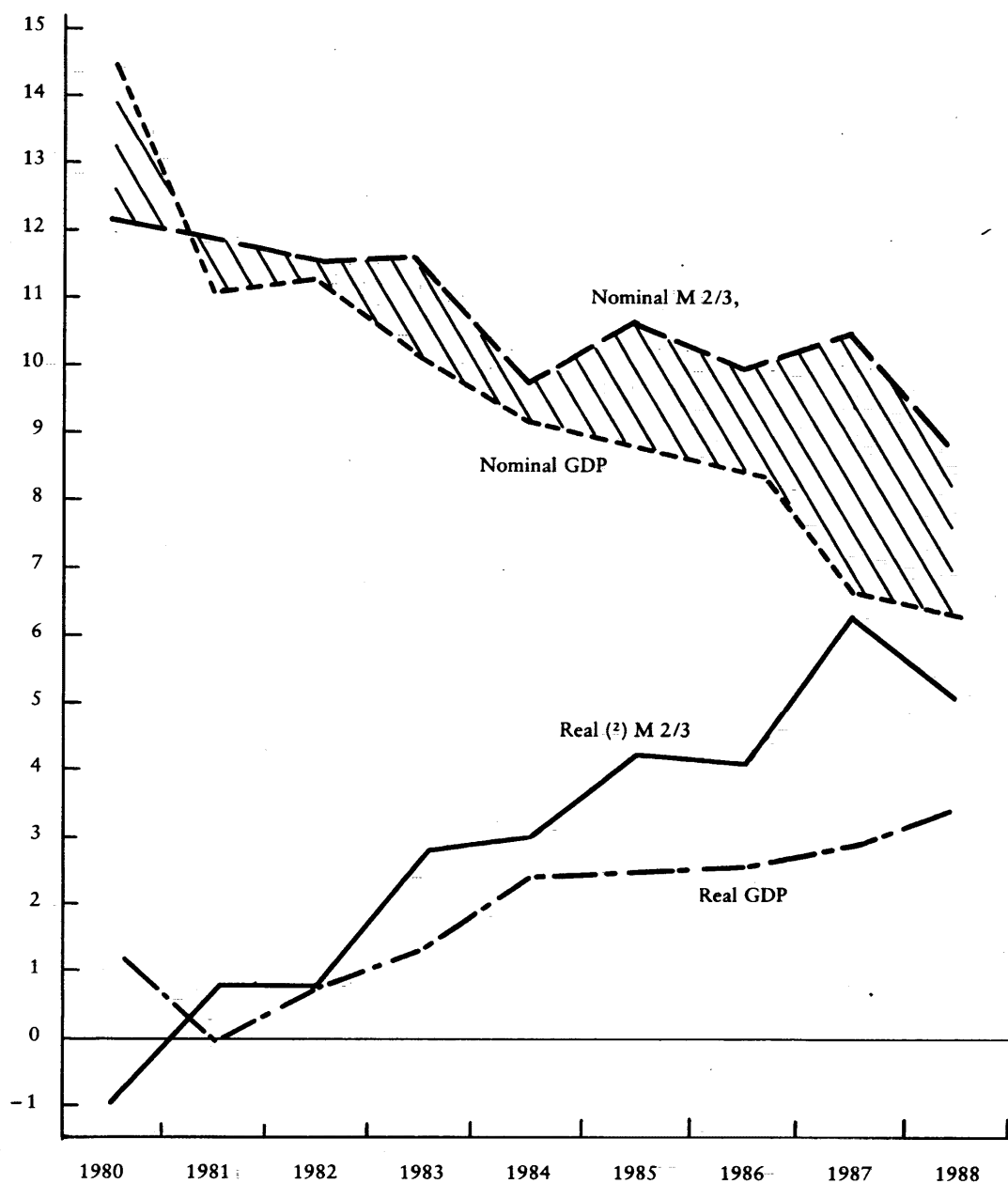
Private consumption deflator, unit labour costs and growth of money stock per unit of output
(weighted average percentage change EUR 12)




(1) Broad money supply (M 2/3) divided by real GDP.

GRAPH A6

Growth of money supply ⁽¹⁾ M 2/3 and GDP, EUR 12
(average annual % change)

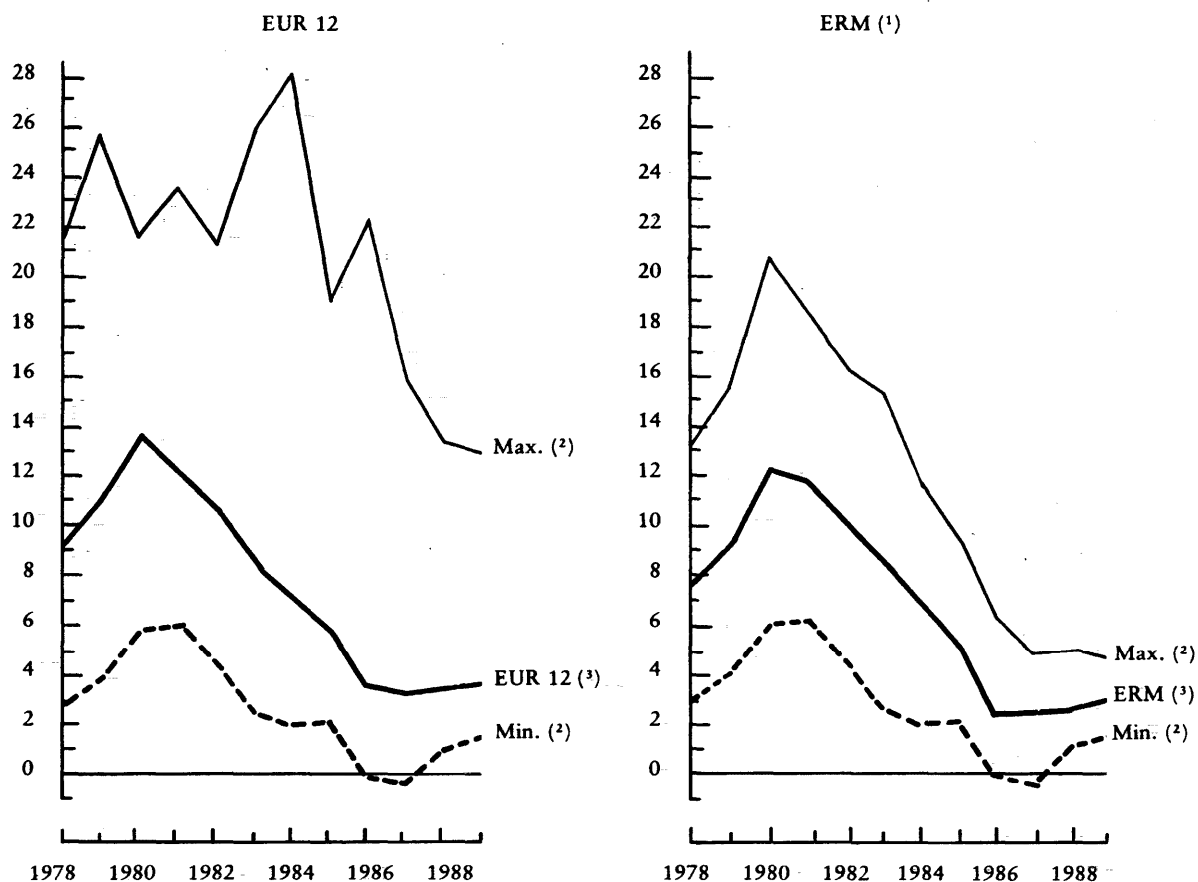


 = Change in liquidity ratio

⁽¹⁾ EUR 12 average of broad money supply M 2/3, weighted by GDP.
⁽²⁾ Nominal money supply (M 2/3) adjusted by the GDP deflator.

GRAPH A7

Convergence of inflation rates in the Community and in the ERM-countries ⁽¹⁾
(private consumption deflator)

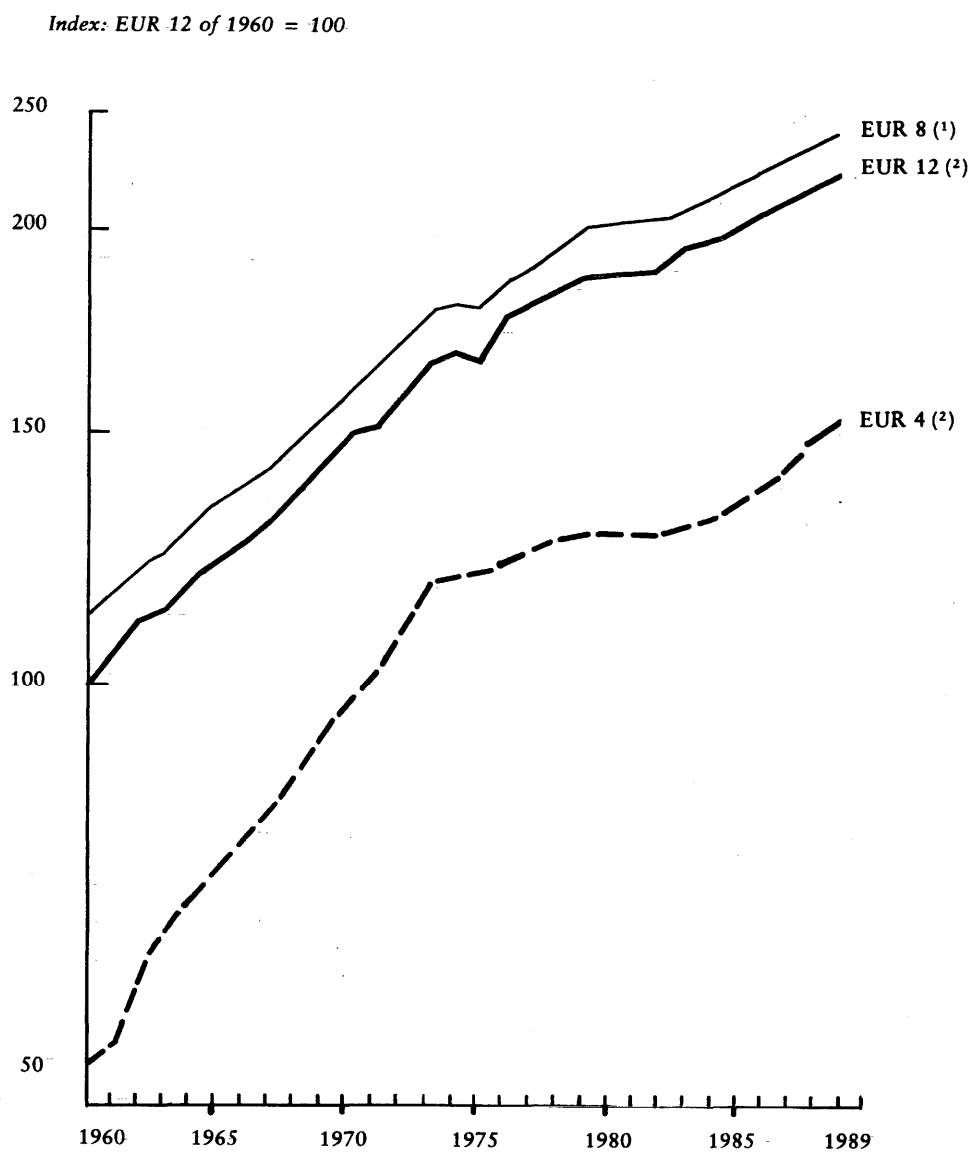


⁽¹⁾ Countries participating in the exchange rate mechanism of the EMS.

⁽²⁾ Maximum/minimum rate of inflation in the Community/ERM-countries.

⁽³⁾ Weighted average rate of inflation in the Community/ERM-countries.

GRAPH A8
GDP per capita at constant prices and PPS

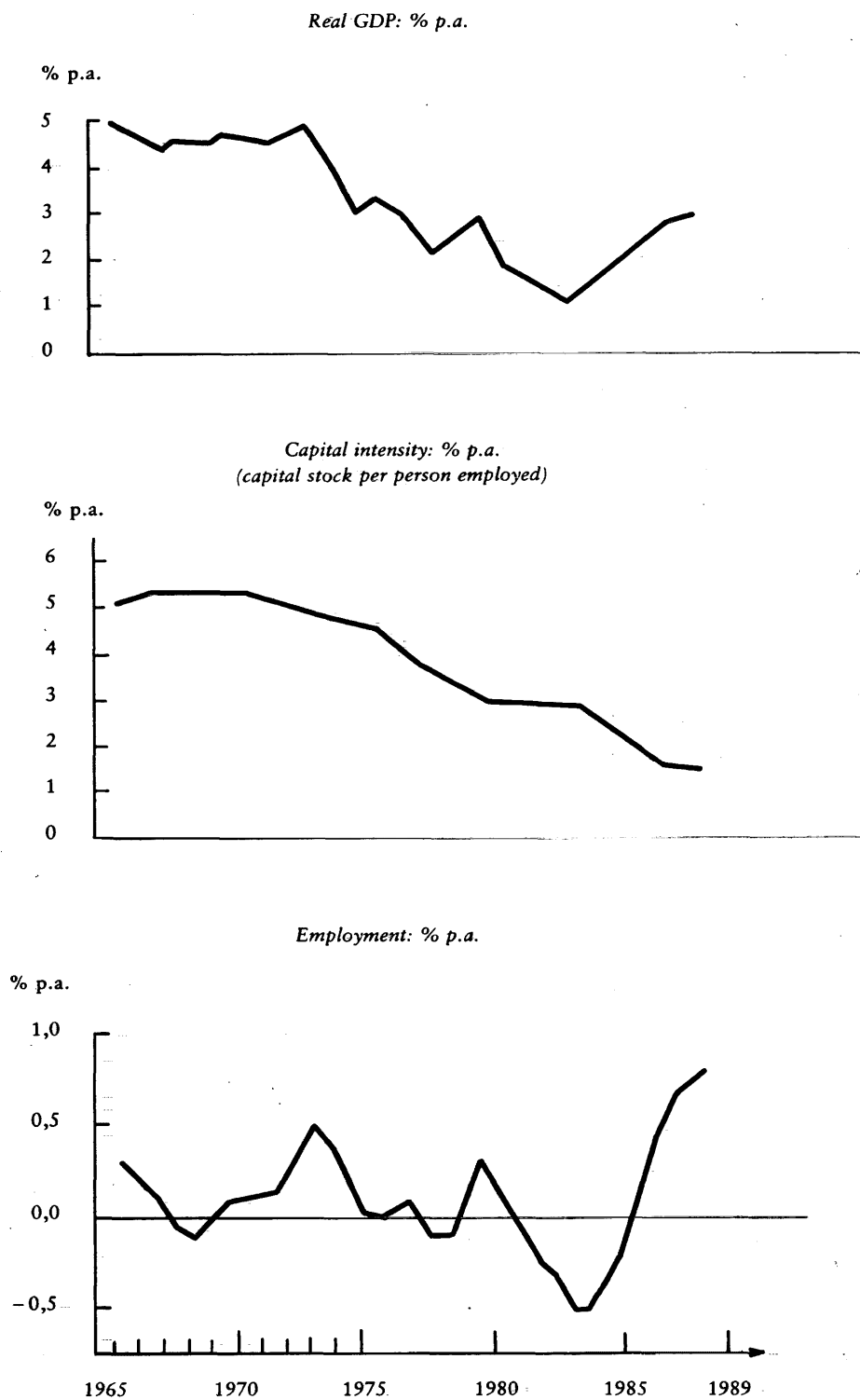


⁽¹⁾ EUR 8: Weighted average of B, DK, D, F, I, L, NL, UK.

⁽²⁾ EUR 4: Weighted average of GR, E, IRL, P.

GRAPH A9

Real GDP, capital intensity and employment, EUR 12
(five-year moving average of annual growth rates ⁽¹⁾)



(¹) Five-year period ending in indicated year.

GRAPH A10

Real unit labour costs, profitability, real long-term interest rate and investment (EUR 12)

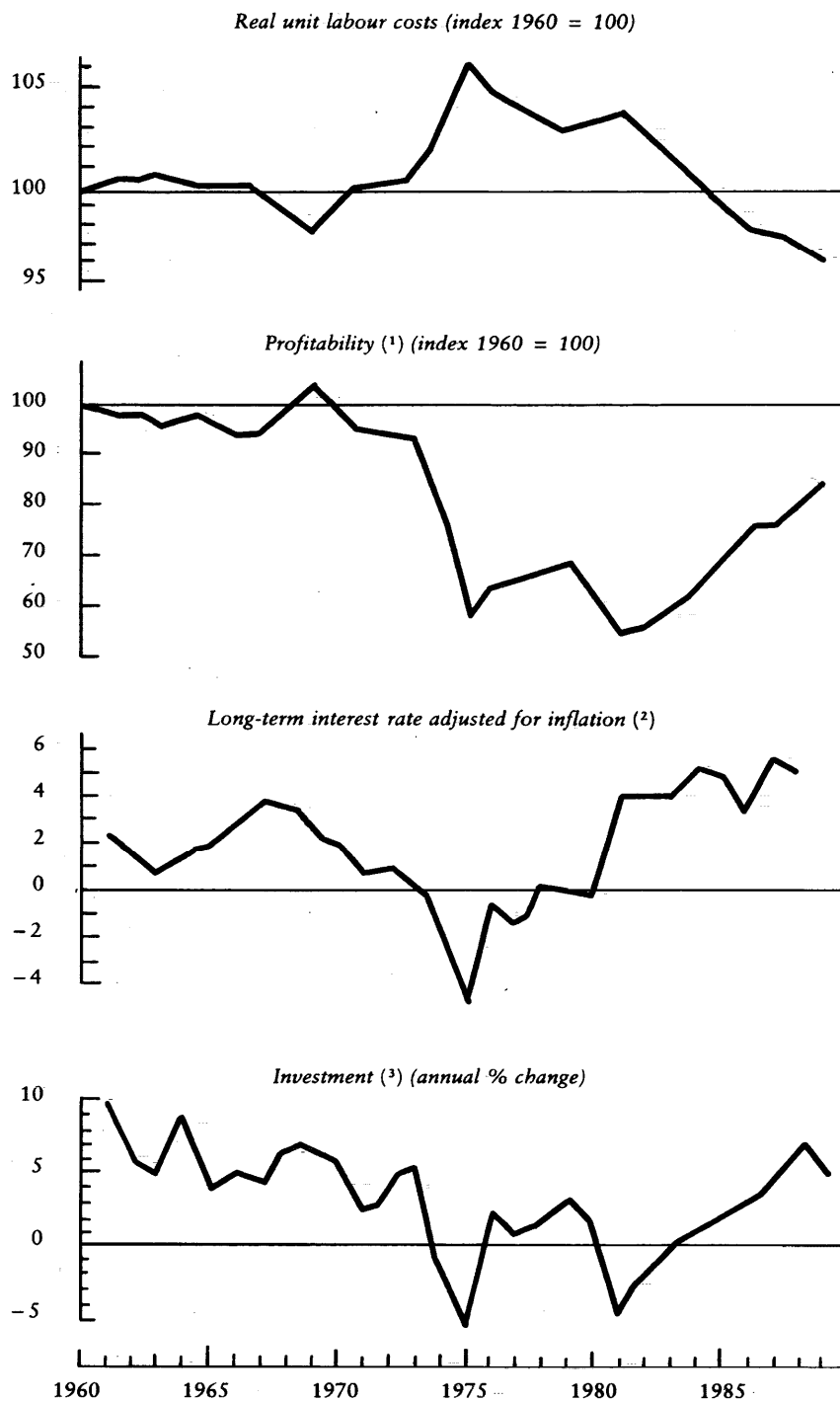
⁽¹⁾ Compact Databank.⁽²⁾ Long-term interest rates deflated by GDP deflator.⁽³⁾ Gross fixed capital formation at constant 1980 prices.

TABLE A 11

Main economic aggregates of EUR 12 (1961 to 1989) ⁽¹⁾

(Annual percentage change; unless otherwise stated)

	1961 to 1973	1974 to 1981	1982	1983	1984	1985	1986	1987	1988	1989
1. Gross domestic product:										
— at current prices	10,2	14,4	11,2	10,1	9,1	8,7	8,3	6,9	7,4	6,7
— at constant prices	4,8	2,0	0,8	1,4	2,4	2,5	2,6	2,9	3,5	2,8
— price deflator	5,1	12,1	10,3	8,5	6,6	6,1	5,5	3,9	3,8	3,7
2. Gross fixed capital formation ⁽²⁾ :										
— total	5,6	-0,3	-2,0	-0,1	1,3	2,1	3,1	4,6	7,1	5,2
— construction ⁽³⁾	:	-1,2	-2,4	0,6	1,2	-2,4	2,4	2,2	6,2	3,8
— equipment ⁽³⁾	:	1,8	-1,9	0,1	6,6	9,1	3,3	7,2	8,1	6,7
3. Share of gross fixed capital formation in GDP ⁽⁴⁾ :										
— total	23,3	22,1	20,2	19,7	19,3	19,2	18,9	19,1	19,7	20,1
— general government	:	3,3	3,0	2,9	2,8	2,9	2,8	2,7	2,8	2,8
— other sectors	:	18,8	17,3	16,8	16,5	16,3	16,1	16,3	16,9	17,3
4. Final national uses including stocks ⁽²⁾ :										
— EUR 12	4,9	1,6	0,8	1,1	1,9	2,3	3,8	3,8	4,1	3,0
— EUR 12 against nine other OECD countries	-0,5	-0,7	1,0	-2,0	-3,4	-1,4	-0,1	-0,2	0,0	0,3
5. Inflation (price deflator private consumption)	4,6	12,3	10,5	8,5	7,1	5,9	3,6	3,3	3,5	3,7
6. Compensation per employee:										
— nominal	10,0	14,9	11,0	9,7	7,4	6,9	6,1	5,5	5,3	5,2
— real, deflator private consumption	5,1	2,3	0,4	1,1	0,3	0,9	2,3	2,1	1,8	1,5
— real, deflator GDP	4,6	2,4	0,6	1,1	0,8	0,8	0,5	1,6	1,4	1,4
7. Productivity ⁽⁵⁾	4,5	2,1	1,6	2,0	2,3	1,8	1,8	2,0	2,4	2,0
8. Real unit labour costs ⁽⁶⁾ :										
— index: 1961 to 1973 = 100	100,0	104,3	103,1	102,2	100,7	99,7	98,4	98,0	97,2	96,7
— annual percentage change	0,1	0,4	-1,0	-0,9	-1,4	-1,0	-1,3	-0,3	-0,9	-0,5
9. Profitability (index: 1961 to 1973 = 100)	100,0	65,7	59,0	61,1	68,2	72,5	77,6	78,7	82,1	83,0
10. Relative unit labour costs in common currency against nine other OECD countries:										
— index: 1961 to 1973 = 100	100,0	107,6	98,2	92,8	85,9	85,4	93,8	100,8	98,0	:
— annual percentage change	1,0	-0,2	-6,1	-5,6	-7,4	-0,6	9,7	7,5	-2,8	:
11. Employment	0,3	-0,1	-0,8	-0,5	0,1	0,6	0,8	0,9	1,1	0,9
12. Unemployment rate ⁽⁷⁾	2,2	5,1	9,4	10,6	11,4	11,8	11,9	11,6	11,3	10,9
13. Current balance ⁽⁸⁾	0,4	-0,6	-0,9	-0,1	0,3	0,7	1,3	0,8	0,3	0,1
14. Net lending of general government ⁽⁸⁾ ⁽⁹⁾	:	-3,7	-5,5	-5,3	-5,3	-5,2	-4,8	-4,2	-3,8	-3,5
15. Gross debt of general government ⁽⁸⁾ ⁽⁹⁾	:	39,4	47,6	50,8	54,0	56,6	57,8	59,2	60,0	60,7
16. Interest payments by general government ⁽⁸⁾ ⁽⁹⁾	:	2,8	4,1	4,4	4,7	5,0	5,0	4,9	4,8	4,8
17. Money supply (end of year) ⁽¹⁰⁾	11,9	13,4	11,9	10,7	9,9	9,9	10,4	11,0	:	:
18. Long-term interest rate ⁽¹¹⁾	7,1	11,7	14,3	12,7	11,8	10,9	9,2	9,3	9,3	:

⁽¹⁾ 1961 to 1986: Eurostat and Commission services;
1987 to 1989: economic forecasts, September to October 1988.

⁽²⁾ At constant prices.

⁽³⁾ Until 1986: EUR 12 without Spain and Portugal.

⁽⁴⁾ At current prices.

⁽⁵⁾ GDP at constant market prices per person employed.

⁽⁶⁾ Deflator GDP.

⁽⁷⁾ Percentage of civilian labour force (1961 to 1973: EUR 12 without Greece, Spain and Portugal).

⁽⁸⁾ Percentage of GDP.

⁽⁹⁾ 1974 to 1981: EUR 12 without Greece and Portugal.

⁽¹⁰⁾ Broad money supply, M 2 or M 3, according to State.

⁽¹¹⁾ Levels; 1988: January to August average.

TABLE A 12

Convergence of price development (private consumption deflator, annual % change)

	1969 1960	1977 1969	1981 1977	1982	1984	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
B	3,2	7,4	5,6	7,6	5,8	5,2	0,8	1,6	1,3	2,4
DK	5,7	10,0	10,6	10,2	6,5	4,9	3,6	4,1	4,8	3,7
D	2,7	5,5	4,7	4,7	2,4	2,1	-0,2	0,5	1,3	2,5
GR	2,4	10,5	18,5	21,2	18,3	18,7	22,2	15,8	13,3	12,8
E	5,9	13,2	16,6	14,5	11,0	8,3	8,7	5,3	4,7	4,3
F	4,2	8,3	11,5	11,5	7,5	5,7	2,5	3,2	2,7	2,7
IRL	4,5	13,8	15,2	15,3	9,4	4,5	3,6	3,1	2,1	2,8
I	3,7	12,9	16,5	15,9	11,4	9,3	6,1	4,8	4,9	4,6
L	2,3	6,8	6,2	10,8	5,5	5,2	0,6	0,6	1,4	2,2
NL	4,0	8,0	5,5	5,3	2,0	2,5	0,2	-0,4	0,9	1,4
P	2,6	13,1	22,4	20,6	27,8	19,0	12,0	10,2	9,4	7,0
UK	3,7	12,4	12,6	8,6	4,8	5,2	3,6	3,8	4,4	4,7

Weighted average

EUR 12	3,7	9,9	11,4	10,5	7,1	5,9	3,6	3,3	3,5	3,7
EMS	3,6	8,6	10,0	9,9	6,5	5,2	2,4	2,5	2,7	3,1

Measures of dispersion related to average ⁽²⁾

EUR 12	0,9	2,5	4,8	4,4	4,9	3,6	4,1	3,0	2,7	1,9
EMS	0,8	2,2	4,0	3,3	2,4	1,4	1,8	1,6	1,4	0,8

Measures of dispersion related to lowest ⁽²⁾

EUR 12	1,4	4,7	7,5	7,5	7,4	5,5	5,5	4,8	3,4	2,9
EMS	1,5	3,6	4,8	5,5	4,3	2,8	2,4	2,6	1,5	1,4

⁽¹⁾ Forecasts September to October 1988.⁽²⁾ The dispersion index is an unweighted arithmetic mean of each country's absolute deviation from the respective reference value (e.g. weighted average or lowest rate).

Source: Eurostat and Commission services.

TABLE A 13

Nominal unit labour costs (annual % change)

	1969 1960	1977 1969	1981 1977	1982	1984	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
B	3,4	9,5	5,0	4,8	3,9	4,1	2,5	1,7	0,5	2,3
DK	6,7	10,2	8,6	9,1	3,4	3,3	3,6	10,6	4,1	1,0
D	3,3	6,8	4,3	3,1	0,7	1,6	2,3	1,7	0,3	0,7
GR	0,8	11,3	19,6	26,3	19,4	20,2	14,2	12,8	15,0	12,5
E	7,1	14,0	15,7	11,3	5,5	6,1	6,8	5,2	4,4	4,1
F	4,2	9,6	11,2	11,4	6,1	4,5	2,1	1,0	1,3	1,4
IRL	4,6	13,6	15,3	11,8	6,2	2,9	5,0	0,9	0,6	1,1
I	3,7	14,8	16,8	16,5	8,5	8,7	5,7	5,4	3,5	4,7
L	2,4	11,2	5,8	5,1	1,2	1,4	4,7	4,3	2,5	4,1
NL	6,4	8,9	4,5	4,6	-2,9	0,4	1,0	1,0	0,6	-0,3
P	2,2	17,4	16,7	16,5	19,0	18,1	12,2	11,9	8,6	7,1
UK	3,7	13,1	14,3	5,3	5,2	4,5	4,7	4,2	5,6	6,1

Weighted average

EUR 12	3,9	11,1	11,3	9,2	5,1	5,0	4,2	3,5	2,9	3,2
EMS	3,9	10,0	9,7	9,3	4,2	4,3	3,1	2,6	1,5	1,9

Measures of dispersion related to average ⁽²⁾

EUR 12	1,4	2,4	4,9	5,2	4,5	4,2	2,8	3,4	3,0	2,7
EMS	1,1	1,9	4,3	4,0	2,9	2,1	1,4	2,4	1,2	1,4

Measures of dispersion related to lowest ⁽²⁾

EUR 12	1,9	4,9	7,2	7,4	9,3	5,9	4,4	4,2	3,6	4,0
EMS	1,9	3,8	4,6	5,2	6,3	3,0	2,4	2,3	1,4	2,2

⁽¹⁾ Forecasts September to October 1988.⁽²⁾ The dispersion index is an unweighted arithmetic mean of each country's absolute deviation from the respective reference value (e.g. weighted average or lowest rate).

Source: Eurostat and Commission services.

TABLE A 14

Gross domestic product per capita at current market prices and purchasing power standards (EUR 12 = 100)

	B	DK	D	GR	E	F	IRL	I	L	NL	P	UK	EUR 4 (¹)	EUR 8 (²)	EUR 12	WMAD (³)	Ratio (⁴)
1960	95,6	119,6	117,9	38,7	59,1	101,6	61,9	91,3	137,0	118,6	38,4	128,3	52,4	110,4	100,0	20,4	41,5
1961	95,5	120,9	116,4	40,8	62,6	101,4	62,3	93,8	134,7	115,3	38,7	125,7	55,0	109,8	100,0	18,6	45,4
1962	96,4	122,3	116,3	39,7	65,4	102,5	62,0	95,4	130,1	114,0	39,9	121,5	56,7	109,4	100,0	17,2	47,7
1963	96,4	117,8	114,2	42,0	68,1	102,4	62,3	96,6	128,6	112,5	40,5	121,4	58,9	108,9	100,0	16,0	50,0
1964	97,5	121,9	115,0	43,3	68,3	103,0	61,6	93,9	130,8	114,6	41,0	121,0	59,3	108,8	100,0	16,7	50,2
1965	96,8	122,3	116,1	45,5	69,5	103,4	60,5	93,0	127,5	115,1	42,6	119,0	60,7	108,5	100,0	16,6	51,5
1966	96,2	120,8	114,8	46,5	71,3	104,6	59,1	94,9	124,1	113,2	43,1	116,9	62,0	108,2	100,0	15,5	53,4
1967	96,6	120,3	111,2	47,1	71,4	105,6	60,1	98,1	120,5	114,5	45,1	116,2	62,6	108,1	100,0	14,4	53,8
1968	95,8	118,8	111,7	47,9	72,0	104,4	61,8	99,2	119,6	115,2	46,8	115,0	63,5	108,0	100,0	13,6	55,0
1969	97,0	119,7	113,1	49,9	73,9	105,5	62,1	99,6	124,5	115,3	45,6	110,3	64,9	107,6	100,0	12,8	56,9
1970	99,0	116,5	113,3	51,7	73,3	106,3	61,2	100,3	123,1	115,8	48,1	108,2	65,2	107,6	100,0	12,4	57,2
1971	99,5	115,7	112,4	53,7	73,9	108,1	61,1	98,9	122,0	116,1	50,3	107,7	66,3	107,3	100,0	12,3	58,5
1972	100,6	116,7	112,2	55,9	76,2	109,4	61,7	97,8	123,8	114,4	52,4	105,7	68,5	106,8	100,0	11,9	60,7
1973	100,6	113,8	110,7	56,6	77,1	108,2	60,2	98,4	125,9	112,5	55,2	107,5	69,5	106,6	100,0	11,3	62,5
1974	102,9	110,7	109,2	53,6	79,1	109,4	60,9	100,4	127,7	114,4	54,3	105,0	70,2	106,5	100,0	10,5	63,5
1975	102,6	111,2	109,5	57,1	79,9	110,8	63,0	97,6	120,1	115,0	51,2	105,9	70,9	106,5	100,0	11,3	63,5
1976	103,4	113,0	110,9	57,3	77,9	111,0	60,1	98,3	117,1	114,7	51,1	105,1	69,4	106,9	100,0	11,6	62,1
1977	101,8	112,2	112,2	57,2	77,9	111,6	62,9	97,8	116,7	114,3	52,3	104,1	69,8	106,9	100,0	11,8	62,0
1978	101,8	110,6	112,5	58,7	76,4	111,9	64,9	97,5	117,9	113,4	52,3	105,1	69,2	107,1	100,0	12,3	61,6
1979	101,0	111,1	113,9	58,5	73,8	111,8	64,0	99,1	117,4	112,1	53,5	104,2	67,6	107,5	100,0	12,4	59,9
1980	104,3	109,4	114,0	58,4	73,7	112,0	64,7	101,9	117,2	111,2	54,9	100,9	67,8	107,5	100,0	12,1	60,0
1981	103,0	108,7	114,2	58,0	72,9	112,9	66,2	103,1	116,9	109,8	55,3	99,8	67,4	107,6	100,0	12,3	59,5
1982	104,0	111,5	113,0	57,6	73,0	114,6	66,6	102,6	118,0	107,2	55,9	100,5	67,5	107,6	100,0	12,3	59,4
1983	102,9	113,0	113,7	56,8	73,0	113,4	64,9	101,5	120,0	107,0	54,7	102,7	67,1	107,8	100,0	12,9	59,1
1984	102,8	114,4	114,8	56,8	72,4	112,1	65,1	102,5	125,0	107,6	52,2	102,3	66,3	108,0	100,0	12,8	58,4
1985	101,9	116,5	114,9	57,0	72,1	111,0	64,2	102,7	126,5	107,2	52,4	103,5	66,1	108,0	100,0	12,9	58,4
1986	101,8	117,6	115,1	56,2	72,5	110,3	62,6	102,9	126,6	106,6	53,0	103,8	66,2	108,0	100,0	12,9	58,6
1987	100,8	112,7	114,1	53,8	73,9	108,9	62,9	103,4	125,6	105,4	53,5	106,2	66,8	107,9	100,0	12,6	59,8
1988 ⁽⁵⁾	99,9	109,1	113,8	52,8	74,6	108,4	62,4	103,2	124,6	103,6	54,8	107,5	67,3	107,8	100,0	12,3	60,5
1989 ⁽⁵⁾	100,3	107,1	113,5	51,1	75,6	108,4	63,1	102,7	124,9	102,6	55,5	108,2	67,8	107,7	100,0	12,2	61,1

⁽¹⁾ EUR 4: GR, E, IRL, P.⁽²⁾ EUR 8: B, DK, D, F, I, L, NL, UK.⁽³⁾ WMAD = Weighted mean absolute deviation.⁽⁴⁾ Relationship between GDP per capita in the four poorest countries and the four richest countries in the Community.⁽⁵⁾ 1987 to 1989: Economic forecasts, May to June 1988.

Source: Eurostat and Commission services.

TABLE A 15

Compensation per employee (annual % change)

	Selected periods				Change on previous year				
	1973 1960	1979 1973	1984 1979	1989 1984	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
B	8,9	11,9	7,2	3,6	4,8	3,8	3,3	2,2	3,8
DK	10,7	12,0	8,9	4,9	4,5	4,7	8,2	4,5	2,5
D	9,2	7,4	4,7	3,1	3,0	3,9	2,9	3,0	2,5
GR	10,2	22,0	21,8	16,3	22,6	15,7	12,5	17,0	14,0
E	14,6	22,9	14,0	7,7	10,1	8,3	7,5	6,5	6,1
F	9,9	14,7	12,5	4,3	6,6	4,0	3,3	3,8	3,8
IRL	11,3	19,2	15,4	4,8	6,4	5,1	5,1	3,5	3,9
I	11,6	19,9	17,7	8,2	10,2	7,7	8,7	7,0	7,5
L	7,4	11,3	7,7	4,2	3,8	5,0	3,9	3,4	5,0
NL	11,4	10,2	3,6	1,4	1,4	1,6	1,3	1,9	1,0
P	12,0	25,8	19,8	14,8	22,4	17,0	13,9	11,0	10,0
UK	8,3	17,2	11,1	7,3	6,7	7,3	7,0	7,5	7,8
EUR 12	10,0	15,1	11,2	5,8	6,9	6,1	5,5	5,3	5,2
USA	5,7	8,2	7,2	4,4	4,3	3,7	4,1	5,3	4,8
JAP	14,0	12,6	4,8	3,9	3,4	3,7	3,1	4,4	4,7

⁽¹⁾ Forecasts September to October 1988.

Source: Commission services.

TABLE A 16

Real compensation per employee ⁽¹⁾ (annual % change)

	Selected periods				Change on previous year				
	1973 1960	1979 1973	1984 1979	1989 1984	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	4,6	3,6	1,8	0,5	-0,7	0,2	1,6	0,6	0,9
DK	3,4	1,6	0,4	0,3	-0,7	-0,2	3,0	0,1	-0,5
D	4,6	2,5	1,0	0,8	0,8	0,8	0,9	1,2	0,2
GR	5,5	5,6	1,2	0,5	4,1	-2,8	-1,6	2,4	0,9
E	7,1	3,9	1,3	0,7	1,3	-2,3	1,7	1,2	1,7
F	4,8	3,8	1,9	0,6	0,8	-0,7	0,7	1,0	1,3
IRL	3,9	4,2	2,1	1,0	1,3	-0,5	2,6	1,1	0,8
I	5,9	2,4	1,3	1,9	1,3	-0,3	3,1	2,2	3,2
L	2,9	4,5	0,2	1,8	0,3	2,4	2,8	1,2	2,2
NL	5,0	2,6	-0,5	0,8	-0,3	0,8	2,3	1,6	-0,4
P	7,7	5,1	-1,4	0,7	0,6	-0,7	1,6	0,5	1,8
UK	3,0	1,0	1,5	2,0	0,7	3,7	2,0	1,9	2,0
EUR 12	4,6	2,6	1,3	1,2	0,8	0,5	1,6	1,4	1,4
USA	2,0	0,2	1,1	1,0	1,1	1,0	0,7	1,9	0,2
JAP	7,6	4,2	2,6	2,5	1,9	1,9	2,9	3,5	2,3

⁽¹⁾ From the point of view of costs: compensation of employees per wage and salary earner deflated by the GDP deflator.⁽²⁾ Forecasts September to October 1988.

Source: Commission services.

TABLE A 17

Labour productivity (GDP at constant prices per person employed, annual % change)

	Selected periods				Change on previous year				
	1973 1960	1979 1973	1984 1979	1989 1984	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
B	4,3	2,1	2,2	1,3	0,6	1,3	1,6	1,7	1,4
DK	3,2	1,3	1,4	0,4	1,2	1,0	-2,2	0,3	1,5
D	4,1	2,9	1,6	1,7	1,4	1,6	1,2	2,7	1,7
GR	8,2	3,0	-0,3	1,2	1,9	1,3	-0,3	1,7	1,3
E	6,5	3,2	3,1	2,2	3,7	1,4	2,2	2,1	1,8
F	4,9	2,7	1,8	2,2	2,1	1,8	2,2	2,5	2,3
IRL	4,3	3,4	3,0	2,6	3,3	0,1	4,2	2,9	2,8
I	5,7	1,8	1,3	2,5	1,3	1,9	3,2	3,4	2,6
L	3,1	0,8	2,2	0,8	2,4	0,3	-0,4	0,9	0,9
NL	3,9	2,4	1,7	0,9	1,0	0,6	0,3	1,3	1,4
P	7,4	3,1	0,2	2,9	3,6	4,3	1,8	2,3	2,7
UK	2,9	1,3	1,7	2,1	2,1	2,5	2,6	1,9	1,6
EUR 12	4,5	2,3	1,7	2,0	1,8	1,8	2,0	2,4	2,0
USA	2,0	0,1	1,3	1,0	0,7	1,2	0,6	1,8	0,9
JAP	8,2	3,0	2,9	3,1	3,8	1,6	3,2	4,0	3,0

⁽¹⁾ Forecasts September to October 1988.

Source: Commission services.

TABLE A 18

Real unit labour costs ⁽¹⁾ (1961 to 1969 = 100)

	1961 to 1969	1975	1979	1981	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	100,0	110,4	112,7	115,4	109,0	107,8	107,9	106,7	106,2
DK	100,0	104,6	100,2	100,6	93,6	92,5	97,4	97,2	95,3
D	100,0	107,0	102,5	104,5	98,8	98,0	97,7	96,3	94,8
GR	100,0	87,2	96,7	101,0	106,0	101,7	100,4	101,0	100,6
E	100,0	105,5	106,7	105,6	95,5	92,0	91,5	90,8	90,7
F	100,0	105,6	105,4	108,3	104,6	102,1	100,6	99,1	98,2
IRL	100,0	104,3	100,5	100,3	94,3	93,7	92,3	90,7	88,9
I	100,0	111,7	107,5	108,2	107,4	105,1	105,0	103,8	104,5
L	100,0	119,7	117,0	120,5	104,3	106,5	109,9	110,3	111,8
NL	100,0	110,5	107,3	104,1	94,7	95,0	96,9	97,2	95,5
P	100,0	143,3	119,9	119,7	107,6	102,4	102,2	100,4	99,6
UK	100,0	110,2	100,1	101,3	97,4	98,5	97,9	97,8	98,2
EUR 12	100,0	107,3	103,1	104,4	99,9	98,6	98,2	97,3	96,8
USA	100,0	101,7	102,5	102,2	101,8	101,7	101,8	102,0	101,3
JAP	100,0	110,6	107,5	106,5	103,8	104,1	103,8	103,3	102,5

⁽¹⁾ Compensation of employees per wage and salary earner deflated by the GDP deflator and divided by real GDP per head of occupied population.⁽²⁾ Forecasts September to October 1988.

Source: Eurostat and Commission services.

TABLE A 19

Gross fixed investment as % of GDP

	Selected periods				1979	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
	1960 to 1973	1974 to 1979	1980 to 1984	1985 to 1989					
B	21,6	21,9	17,7	16,8	20,7	16,1	16,6	17,6	17,8
DK	23,8	22,1	16,7	18,5	20,9	20,4	18,5	17,7	17,3
D	24,9	20,8	21,1	19,6	21,8	19,5	19,3	19,8	20,0
GR	22,4	22,8	21,0	18,5	25,8	18,5	17,6	18,2	19,2
E	24,0	24,6	20,9	20,4	21,6	18,7	20,1	21,5	22,7
F	23,5	23,4	21,2	19,3	22,4	18,8	19,0	19,6	20,1
IRL	20,7	25,9	26,0	18,2	30,5	18,7	17,5	17,2	17,4
I	26,0	24,6	22,6	20,3	23,1	20,1	20,0	20,1	20,1
L	26,0	25,1	23,8	21,2	24,4	20,7	23,8	21,8	21,8
NL	25,0	21,0	19,0	19,8	21,0	19,6	19,8	20,3	20,4
P	24,0	26,3	28,7	24,4	26,6	21,6	24,3	26,4	28,2
UK	18,3	19,3	16,8	17,9	18,8	17,2	17,4	18,4	19,1
EUR 12	23,2	22,2	20,5	19,4	21,7	18,9	19,1	19,7	20,1
USA	18,2	18,7	18,0	17,5	20,4	17,8	17,3	17,2	17,2
JAP	32,7	31,8	29,6	29,2	31,7	27,8	29,4	30,5	30,8

⁽¹⁾ Forecast September to October 1988.

Source: Commission services.

TABLE A 20

Investment in equipment, annual % change in volume

	<u>1973</u> 1970	<u>1979</u> 1973	<u>1984</u> 1979	<u>1989</u> 1984	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
B	3,2	1,2	5,0	6,1	-0,7	10,8	7,9	7,6	5,0
DK	3,7	2,7	1,5	1,9	15,4	14,8	-18,0	-3,4	4,5
D	0,3	2,9	-0,5	5,8	10,0	4,3	4,0	5,5	5,2
GR	11,8	1,4	-1,5	3,2	7,6	-6,5	-0,9	8,5	8,0
E	10,9	-0,7	-2,0	12,8	8,5	10,4	19,0	14,5	11,9
F	9,0	1,7	0,4	5,7	4,6	3,8	4,4	8,8	6,8
IRL	13,8	6,8	-0,4	4,0	4,9	0,3	3,6	6,0	5,4
I	5,9	0,6	3,6	8,2	11,4	5,0	11,5	8,0	5,5
L	5,4	-1,4	-0,2	4,2	4,0	7,9	3,9	-1,4	1,5
NL	2,2	2,0	0,4	6,8	17,4	9,8	0,1	1,4	6,1
P	—	—	—	14,2	-0,5	16,0	30,0	15,5	12,0
UK	3,5	2,6	-0,2	5,7	9,9	-3,9	6,9	9,3	6,9
EUR 12	5,4 ⁽²⁾	1,7 ⁽²⁾	0,8 ⁽²⁾	6,9	9,1	3,3	7,2	8,1	6,7

⁽¹⁾ Forecasts September to October 1988.⁽²⁾ EUR 12 excluding Portugal.

Source: Commission services.

TABLE A 21

Nominal short-term interest rates ⁽¹⁾

	1961 to 1969	1970 to 1977	1978 to 1981	1982	1983	1984	1985	1986	1987	1988 ⁽²⁾
B	4,9	7,4	12,0	14,1	10,5	11,5	9,5	8,1	7,0	6,4
DK	6,6	9,1	14,9	16,4	12,0	11,5	10,0	9,1	9,9	8,6
D	4,5	7,2	8,1	8,8	5,8	6,0	5,4	4,6	4,0	3,9
GR	—	—	4,2	18,9	16,6	15,7	17,0	19,8	15,6	16,5
E	—	1,9	16,5	16,3	20,1	14,9	12,2	11,7	15,8	11,2
F	5,0	8,4	11,2	14,6	12,5	11,7	9,9	7,7	8,3	7,8
IRL	—	8,9	14,7	17,5	14,0	13,2	12,0	12,4	11,0	8,2
I	3,5	9,8	14,9	19,9	18,3	17,3	15,0	12,8	11,4	11,1
NL	3,6	6,1	9,7	8,2	5,7	6,1	6,3	5,7	5,4	4,5
P	1,4	6,1	16,0	16,8	20,9	22,5	21,0	15,6	13,9	13,1
UK	6,1	9,6	13,6	12,2	10,1	10,0	12,2	10,9	9,7	9,3
EUR 12	4,8	8,5	12,2	13,8	12,1	11,3	10,6	9,1	8,9	8,2
USA	4,1	5,7	10,8	10,6	8,7	9,5	7,5	6,0	5,9	6,3
JAP	—	7,3	7,3	6,8	6,5	6,3	6,5	5,0	3,9	3,8

⁽¹⁾ Three-month interbank rate, except: Belgium: yield on issue of four-month *Fonds des Rentes* certificates; Denmark: daily money market rate (annual average); Portugal: six-month deposits; from 1986, three-month treasury bills.

⁽²⁾ January to August average.

Source: Commission services.

TABLE A 22

Nominal long-term interest rates ⁽¹⁾

	1961 to 1969	1970 to 1977	1978 to 1981	1982	1983	1984	1985	1986	1987	1988 ⁽²⁾
B	6,1	8,1	11,0	13,4	11,8	12,0	10,6	7,9	7,8	7,8
DK	7,9	13,2	17,9	20,5	14,4	14,0	11,6	10,5	11,9	10,8
D	6,6	8,3	8,0	9,0	7,9	7,8	6,9	5,9	5,8	6,0
GR	:	6,1	14,0	15,4	18,2	18,5	15,8	15,8	17,2	17,8
E	:	:	11,3	16,0	16,9	16,5	13,4	11,4	12,8	11,6
F	6,2	9,6	12,6	15,6	13,6	12,5	10,9	8,4	9,4	9,2
IRL	:	10,6	15,1	17,0	13,9	14,6	12,7	11,1	11,3	9,9
I	6,5	10,2	16,1	20,9	18,0	15,0	14,3	11,7	11,3	12,1
NL	5,3	8,3	10,1	10,5	8,8	8,6	7,3	6,4	6,4	6,3
P	:	:	:	:	:	:	25,4	17,9	15,4	14,3
UK	6,7	11,8	13,6	12,7	10,8	10,7	10,6	9,8	9,5	9,3
EUR 12	6,5	9,8	12,4	14,3	12,7	11,8	10,9	9,2	9,3	9,4
USA	4,6	6,5	10,1	12,2	10,8	12,0	10,8	8,1	8,7	8,9
JAP	:	5,8	8,0	8,3	7,8	7,3	6,5	5,2	5,0	4,6

⁽¹⁾ Yield on public sector bonds.

⁽²⁾ January to August average.

Source: Commission services.

TABLE A 23

Total government receipts ⁽¹⁾ (% of GDP)

	1973	1981	1983	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	38,2	45,0	46,1	47,3	46,0	46,2	45,5	45,1
DK	47,3	52,9	54,4	56,9	58,9	59,9	60,8	61,1
D	42,9	45,6	45,8	46,4	45,6	45,1	44,5	45,2
GR	25,1	28,9	33,2	34,5	35,3	37,6	36,3	36,5
E	23,8	31,7	34,0	35,1	36,5	37,9	38,6	39,0
F	39,4	46,7	48,2	49,3	48,8	49,3	48,9	48,6
IRL	32,2	38,4	42,0	41,9	42,1	42,3	42,1	40,0
I	26,7	34,1	37,9	38,1	39,0	39,6	40,5	40,7
L	39,3	55,0	57,2	55,6	55,7	56,0	55,9	56,2
NL	46,4	53,8	55,7	54,9	53,6	54,6	54,5	52,9
P	:	32,3	37,0	33,4	37,5	35,0	35,1	35,0
UK	35,4	41,7	41,5	41,6	40,6	39,8	39,5	38,8
EUR 12	35,9 ⁽³⁾	41,8	43,3	43,8	43,6	43,7	43,6	43,6

⁽¹⁾ ESA definition of general government, which includes social security funds.⁽²⁾ Forecasts September to October 1988.⁽³⁾ EUR 12 without Portugal.

Source: Commission services.

TABLE A 24

Total government expenditure ⁽¹⁾ (% of GDP)

	1973	1981	1983	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	41,5	57,8	57,2	55,6	54,8	53,4	52,7	51,6
DK	42,1	59,8	61,6	58,9	55,8	57,8	59,9	59,8
D	41,7	49,2	48,4	47,5	46,9	46,9	46,7	46,5
GR	:	39,9	41,5	48,1	46,1	47,1	48,4	49,8
E	22,7	35,6	38,8	42,1	42,2	41,5	41,6	41,9
F	38,5	48,6	51,4	52,1	51,7	51,8	50,8	50,4
IRL	36,8	51,8	53,7	53,0	53,0	51,4	48,8	46,2
I	32,8	45,4	48,5	50,6	50,5	50,1	50,4	50,7
L	36,1	58,5	55,6	49,8	49,7	50,8	50,6	50,1
NL	45,7	59,2	62,0	59,6	59,6	60,8	59,6	57,4
P	:	41,5	46,1	43,5	45,3	43,4	43,3	42,7
UK	38,1	44,3	44,9	44,3	43,0	41,3	39,8	39,0
EUR 12	37,2 ⁽³⁾	47,1	48,6	49,0	48,4	47,9	47,4	47,1

⁽¹⁾ ESA definition of general government, which includes social security funds.⁽²⁾ Forecasts September to October 1988.⁽³⁾ EUR 12 without Greece and Portugal.

Source: Commission services.

TABLE A 25

Net government lending (+) or borrowing (-) ⁽¹⁾ (% of GDP)

	1973	1981	1983	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	-3,3	-12,7	-11,2	-8,3	-8,9	-7,2	-7,1	-6,5
DK	5,2	-6,9	-7,2	-2,0	3,1	2,1	0,9	1,4
D	1,2	-3,7	-2,5	-1,1	-1,3	-1,8	-2,3	-1,3
GR	:	-11,0	-8,3	-13,6	-10,8	-9,5	-12,1	-13,3
E	1,1	-3,9	-4,8	-7,0	-5,7	-3,6	-3,0	-2,9
F	0,9	-1,9	-3,2	-2,8	-2,9	-2,5	-1,9	-1,8
IRL	-4,6	-13,4	-11,6	-11,1	-11,0	-9,1	-6,5	-6,1
I	-6,1	-11,3	-10,6	-12,5	-11,4	-10,5	-10,0	-10,0
L	3,3	-3,6	1,6	5,8	6,0	5,2	5,3	6,1
NL	0,8	-5,4	-6,3	-4,7	-6,0	-6,3	-5,2	-4,6
P	:	-9,2	-9,1	-10,1	-7,8	-8,4	-8,1	-7,8
UK	-2,7	-2,6	-3,3	-2,7	-2,4	-1,4	-0,3	-0,1
EUR 12	-1,1 ⁽³⁾	-5,3	-5,3	-5,2	-4,8	-4,2	-3,8	-3,5

⁽¹⁾ ESA definition of general government, which includes social security funds.⁽²⁾ Forecasts September to October 1988.⁽³⁾ EUR 12 without Greece and Portugal.

Source: Commission services.

TABLE A 26 (a)

Interest payments on public debt (% of GDP)

	1973	1981	1983	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
B	3,3	7,9	9,4	10,5	11,0	10,6	10,5	10,8
DK	1,3	5,3	8,1	9,8	8,8	8,3	7,9	7,4
D	1,1	2,3	3,0	3,0	3,0	2,9	2,8	2,7
GR	1,0	3,2	3,7	5,4	5,7	7,3	8,1	9,3
E	0,6	0,8	1,3	3,2	3,9	3,6	3,5	3,3
F	0,8	2,0	2,6	2,9	2,9	2,8	2,9	2,9
IRL	3,6	7,4	9,3	10,4	9,8	9,9	9,7	9,4
I	2,2	6,1	7,5	8,0	8,5	8,2	8,4	8,9
L	0,9	0,9	1,1	1,3	1,3	1,4	1,2	1,1
NL	2,8	4,4	5,7	6,3	6,4	6,4	6,6	6,5
P	:	5,1	6,4	7,9	9,3	8,0	8,2	7,9
UK	3,6	5,0	4,7	4,9	4,6	4,3	3,9	3,6
EUR 12	1,9 ⁽²⁾	3,7	4,4	5,0	5,1	4,9	4,8	4,8

⁽¹⁾ Forecasts September to October 1988.⁽²⁾ EUR 12 without Portugal.

Source: Commission services.

TABLE A 26 (b)

Interest payments on public debt (% of total government expenditure)

	1973	1981	1983	1985	1986	1987	1988 ⁽¹⁾	1989 ⁽¹⁾
B	8,0	13,7	16,4	18,9	20,1	19,9	20,0	20,9
DK	3,0	8,8	13,1	16,6	15,8	14,4	13,3	12,5
D	2,7	4,7	6,2	6,4	6,3	6,2	6,0	5,9
GR	:	8,0	8,9	11,1	12,4	15,5	16,7	18,7
E	2,7	2,2	3,4	7,7	9,2	8,6	8,4	7,9
F	2,2	4,1	5,0	5,5	5,6	5,4	5,6	5,7
IRL	9,7	14,3	17,3	19,5	18,5	19,2	20,0	20,4
I	6,7	13,5	15,4	15,9	16,8	16,3	16,6	17,5
L	2,6	1,5	1,9	2,6	2,6	2,7	2,4	2,1
NL	6,0	7,5	9,2	10,5	10,8	10,4	11,0	11,3
P	:	12,3	13,9	18,1	20,5	18,4	18,9	18,6
UK	9,5	11,3	10,4	11,1	10,6	10,3	9,7	9,1
EUR 12	5,1 ⁽²⁾	7,9	9,1	10,2	10,4	10,2	10,2	10,3

⁽¹⁾ Forecasts September to October 1988.⁽²⁾ EUR 12 without Greece and Portugal.

Source: Commission services.

TABLE A 27

Gross public debt ⁽¹⁾ in Community countries (% of GDP)

	1973	1981	1983	1985	1986	1987	1988 ⁽²⁾	1989 ⁽²⁾
B	63,2	87,7	105,0	117,2	120,1	125,0	127,4	129,8
DK	5,0	43,7	62,6	65,3	59,8	58,4	57,8	56,4
D	18,6	36,3	40,9	42,5	42,7	43,9	45,0	45,3
GR	19,5	34,3	44,3	62,6	64,6	66,7	69,4	73,9
E	12,8	22,7	34,5	46,4	47,4	48,1	48,0	48,7
F	22,7	23,9	29,5	33,8	35,1	36,7	37,2	37,8
IRL	54,7	81,7	97,3	105,0	116,5	119,8	123,3	124,9
I	54,2	60,5	71,9	83,7	87,9	92,6	96,6	101,4
L	20,4	14,4	14,8	14,4	14,7	14,9	14,7	13,0
NL	43,4	50,4	62,0	69,6	71,1	75,0	79,4	82,2
P	:	46,4	56,0	60,7	63,6	67,6	78,8	83,5
UK	63,2	50,7	57,1	57,2	56,1	53,2	49,3	46,1
EUR 12	36,9 ⁽³⁾	42,6	50,8	56,6	57,8	59,2	60,0	60,7

⁽¹⁾ General government; for Belgium and the Netherlands: excludes social security funds; for Greece and Ireland: central government only.⁽²⁾ Forecasts May to June 1988.⁽³⁾ Excludes Portugal.

Source: Commission services.

TABLE A 28

Nominal effective exchange rates (1980 = 100) ⁽¹⁾

	B/L	DK	D	GR	E	F	IRL	I	NL	P	UK	EUR 12	USA	J
1960	82,6	104,1	52,8	192,6	150,4	117,1	149,7	196,9	74,8	214,5	158,6	98,4	125,0	71,8
1961	81,7	103,1	54,7	191,1	149,6	116,1	149,4	195,2	77,1	213,4	157,8	99,9	125,3	71,4
1962	81,7	103,1	54,9	190,9	150,0	116,1	149,8	195,0	77,6	213,8	158,3	100,5	126,3	71,5
1963	81,5	103,2	55,2	191,0	150,1	116,2	149,7	194,8	77,7	213,4	158,0	100,6	126,6	71,5
1964	81,7	103,0	55,3	191,0	150,1	116,2	149,5	193,9	77,5	212,9	157,5	100,5	126,7	71,4
1965	82,0	103,1	55,1	191,2	150,2	116,2	149,6	193,9	77,7	213,1	157,8	100,4	126,7	71,5
1966	81,9	103,3	55,1	191,4	150,2	116,1	149,6	194,3	77,4	213,3	157,8	100,3	126,8	71,4
1967	82,1	102,6	55,4	191,8	147,9	116,2	148,6	194,8	77,9	214,1	155,3	100,1	127,2	71,6
1968	82,9	99,0	56,4	195,1	132,2	117,9	139,5	198,7	79,1	222,8	137,1	96,5	130,0	73,1
1969	83,1	98,6	57,9	195,4	132,3	112,1	139,6	198,3	79,2	224,6	137,2	96,2	130,2	73,7
1970	83,2	97,8	62,8	192,6	131,8	103,1	139,4	196,1	78,0	223,4	136,7	97,5	128,5	73,3
1971	83,1	96,9	64,7	188,2	130,2	100,8	139,5	194,3	78,7	222,0	136,7	98,3	125,1	74,5
1972	85,5	97,6	66,4	176,2	132,6	103,2	136,7	193,0	79,8	219,6	131,8	100,3	116,7	82,8
1973	86,7	103,6	73,4	162,2	134,7	106,7	127,3	173,3	82,4	223,5	118,0	103,0	107,4	87,4
1974	87,9	104,0	77,4	162,6	138,7	99,5	124,1	156,4	86,7	220,5	113,9	101,1	109,6	81,6
1975	89,2	107,6	78,6	146,7	135,2	109,3	117,0	149,9	88,8	213,9	104,8	102,5	108,7	79,3
1976	91,3	110,0	83,1	138,7	124,2	105,2	105,1	124,3	91,2	195,4	89,7	92,8	114,4	83,3
1977	96,5	109,4	89,7	134,7	108,7	100,2	101,5	114,4	96,0	153,1	85,5	91,9	113,6	92,4
1978	99,3	109,4	95,0	122,4	98,3	98,9	102,0	107,3	98,3	121,9	85,7	92,4	103,1	112,5
1979	100,5	108,5	99,6	115,5	107,4	99,6	102,2	103,7	99,8	103,3	90,9	98,4	100,2	104,2
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	100,0	100,0
1981	94,2	92,5	94,4	89,8	90,4	91,2	91,3	87,6	95,7	96,2	100,2	83,9	112,8	113,6
1982	85,5	88,4	99,1	82,7	84,9	83,6	90,3	81,6	100,5	83,8	95,8	78,0	126,3	107,9
1983	83,1	87,9	103,1	67,7	70,3	77,6	86,6	78,5	102,6	66,1	89,1	71,4	133,6	119,7
1984	81,3	84,7	101,4	58,0	68,6	73,9	82,9	73,9	101,0	54,6	84,9	64,8	144,0	126,6
1985	82,0	85,7	101,7	48,8	67,1	74,7	83,9	70,1	101,2	48,3	84,8	63,5	149,9	130,5
1986	86,5	91,1	112,6	38,4	66,0	78,0	87,0	72,7	109,0	44,6	78,6	69,7	121,3	166,0
1987	90,0	95,0	120,4	34,6	66,2	78,9	85,2	73,5	114,6	41,4	77,8	74,5	106,7	179,7
1988	88,7	93,3	119,1	32,1	68,0	77,1	84,0	70,8	113,8	39,4	81,7	72,9	101,2	196,9

⁽¹⁾ The nominal effective exchange rate is the weighted average (double export weights) of the exchange rate of a currency with respect to the main nine (EUR 12) or 19 competing countries.

Source: Commission services.

TABLE A 29

Real effective exchange rates (1980 = 100) ⁽¹⁾

	B/L	DK	D	GR	E	F	IRL	I	NL	P	UK	EUR 12	USA	J
1960	93,8	77,4	81,9	168,5	65,7	105,1	94,3	104,8	65,4	120,3	97,1	76,3	167,3	69,7
1961	88,5	79,8	88,4	152,7	64,0	106,2	93,7	100,6	68,9	116,7	98,6	79,8	162,8	68,1
1962	88,0	81,8	89,0	152,0	65,6	106,9	95,1	102,2	69,8	111,7	99,5	81,3	159,6	71,8
1963	87,7	83,3	88,3	141,3	70,8	109,8	94,1	110,2	71,9	110,4	96,7	82,8	155,0	73,2
1964	88,2	83,3	86,4	141,4	73,9	109,9	100,0	115,8	76,2	108,4	96,0	83,9	151,9	71,4
1965	89,9	88,6	86,0	138,2	77,7	107,5	98,4	114,0	78,5	107,9	97,5	84,6	146,6	74,8
1966	91,0	91,4	85,9	139,5	82,8	104,2	100,7	109,6	81,8	109,2	98,3	84,6	147,6	72,8
1967	91,4	94,0	83,3	139,2	87,7	103,6	99,3	109,2	83,1	111,8	94,8	82,2	149,1	72,7
1968	91,0	93,6	82,8	139,9	77,8	109,2	92,6	108,5	84,5	106,3	83,3	78,1	156,8	73,3
1969	89,5	94,2	84,1	133,2	76,8	104,9	94,6	105,2	87,7	109,4	84,3	77,6	160,5	72,8
1970	85,0	95,2	95,5	122,3	74,9	94,5	97,1	106,0	85,8	117,1	85,8	81,0	157,6	72,6
1971	85,6	95,6	99,7	112,1	75,3	90,5	100,3	108,6	87,9	117,6	85,8	82,9	147,1	77,4
1972	89,7	94,5	101,0	103,4	79,0	91,0	99,5	108,1	90,9	116,7	86,2	85,4	135,0	86,0
1973	90,2	102,3	110,2	97,1	82,8	93,5	98,5	100,6	95,3	115,0	76,0	87,4	120,6	96,2
1974	92,9	107,0	110,5	106,3	86,1	87,5	94,8	94,9	98,0	131,3	77,0	85,9	115,9	100,3
1975	96,9	108,3	102,2	96,3	87,9	98,3	92,5	101,3	99,2	153,1	82,5	91,3	107,5	97,6
1976	101,1	109,0	100,4	99,0	88,6	96,8	89,9	90,5	100,3	150,3	71,8	82,6	110,9	102,1
1977	107,0	108,9	102,7	106,6	88,0	93,7	86,4	93,3	104,2	127,7	69,6	83,8	108,5	111,1
1978	107,4	110,4	104,0	105,0	89,7	94,5	89,0	93,5	105,3	106,8	72,0	85,9	99,7	130,4
1979	105,7	109,2	103,6	110,4	106,3	96,8	97,1	95,7	104,5	96,6	81,6	93,9	99,6	112,8
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	100,0	100,0
1981	92,2	92,5	89,7	105,4	93,3	94,0	95,0	98,5	90,4	105,7	102,6	86,2	110,4	108,2
1982	81,7	90,2	89,6	114,2	90,4	89,5	98,1	99,9	92,9	99,9	95,9	81,0	125,6	97,0
1983	79,7	91,1	88,8	108,9	79,4	86,7	100,0	107,5	90,5	93,4	88,7	76,5	130,7	105,1
1984	78,5	87,9	84,9	107,9	79,0	85,0	98,5	106,7	83,6	89,0	86,4	70,8	140,3	107,7
1985	79,5	88,6	83,2	105,3	78,9	86,5	98,8	106,5	81,1	89,7	87,1	70,4	146,9	106,4
1986	83,5	93,9	90,8	91,7	80,3	89,0	104,0	113,2	85,3	89,7	81,9	77,3	118,1	134,0
1987	86,2	105,1	95,9	90,8	82,4	88,2	99,8	117,7	88,1	90,6	82,3	83,1	105,0	140,4
1988	83,6	104,7	92,5	94,9	86,1	85,2	96,1	114,6	86,1	91,4	89,3	80,8	100,8	149,7

⁽¹⁾ The index of the real effective exchange rate is derived by multiplying the index of the nominal effective exchange rate by a similarly calculated index of the relative change in unit labour costs in the total economy.

Source: Commission services.