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FRAME ECONOMIC

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UKDel OECD, UKMis Geneva, all Consulates-General
in the Federal Republic, Washington, Tokyo, Vienna.

THE FIVE INSTITUTES' SPRING REPORT

Summary

1. The Five major economic institutes published their forecasts and recommendations yesterday. They forecast an increase in real GNP of 3.5% in 1986. The number of employed is expected to rise by about 300,000 while the number of unemployed is forecast to fall by 70,000 to 2.23 million; inflation, cost of living index, will be 0.5% while the current account surplus will be around DM 60 billion compared to DM 38.6 billion in 1985. Growth in 1986 will stem from domestic demand, investment and exports. Broadening and strengthening economic activity will produce an even higher GNP outturn in 1987.

2. The report supports the main thrust of the Government's economic policy but is mildly critical about the lack of progress on privatisation and on reducing subsidies and about the disappointing progress recorded on deregulation and deburocratisation. The Five Institutes warn the Government that a further fall in interest rates will result in increased capital intensive investment and will consequently adversely affect the labour market.

3. The report has been welcomed by the Government as a vindication of its economic policies.

Detail

4. The five leading economic institutes (Berlin, Hamburg, Munich, Kiel and Essen) produced their latest half-yearly report yesterday. They forecast real GNP growth of 3.5% in 1986 based on the following assumptions:

- a) world trade will expand by 4%;
- b) mineral oil prices will average about 15 US\$ per barrel;
- c) the US\$ will average about DM 2.30 over the year.
There will be no further revaluation of the DM against most EMS currencies;
- d) financial policy will adhere to the course laid down in the 1986 draft budget;
- e) the present expansive course of monetary growth will cease and lead later in the year to growth in the upper band of the Bundesbank's CBM target range;
- f) wage agreements will be about 1 percentage point higher on average than last year.

Details of the forecast are as follows:-

Private Consumption

5. Private consumption will increase strongly in 1986 as a result of higher wages, an increase in the number of employed persons and tax relief in the wake of the introduction of the first stage of income tax reform on 1 January. Gross incomes will increase by 5.5% nominal ie. a good two percentage points more than 1985. These factors plus an improvement in profits will lead to an increase of 5.5% (nominal) in disposable incomes. Given virtual price stability, the real increase will be only slightly lower than the nominal.

6. As a result of falling interest rates the savings ratio is forecast to increase by between half and one percentage point. Therefore real private consumption will grow by 4.5% during the course of the year, the highest rate of increase for 10 years. Demand for consumer goods is expected to be strong especially for electrical appliances and cars, while expenditure on services, particularly travel, will also be high.

/Machinery and Equipment