

UNCLASSIFIED
SAVING TELEGRAM

FROM BONN
FRAME ECONOMIC

TO FCU TELNO 27 SAVING OF 22 OCTOBER 1984. Info all EC Posts, UKDel OECD, UKMis Geneva, all Consulates-General in the Federal Republic, Washington, Tokyo, Vienna.

Prime Minister
I suggest page I
only, as useful
background to your
visit to Bonn on
Friday.

CDP

29/11

THE FIVE INSTITUTES' AUTUMN REPORT

Summary

1. The five major economic institutes published their forecasts and recommendations today. They forecast an increase in real GNP of 2.5% in 1984 and 2% in 1985. Unemployment is expected to increase slightly from 2.27 million in 1984 to 2.28 million in 1985: inflation, cost of living index, will be 2.5% in 1984 falling to 2% in 1985 while the current account surplus will be around DM 10 billion in 1984 and DM 20 billion in 1985. Growth in 1985 will be export-led supported by some pick-up in investment. A cyclical downturn will begin in the second half of 1985 with the institutes forecasting only 1.5% real GNP growth in the second half of the year.

2. The forecast for 1984 is in line with the Government's own annual economic report published in January. The figures for 1985 are more pessimistic: the range of other forecasts for 1985 is between 1.5% and 3%. Bangemann, Minister of the Economy, has said that 2.5% real GNP growth in 1985 is possible.

3. The institutes are critical of some aspects of Government policy. They say again, as they have in their last two reports, that the Government has not been determined enough in its attack on structural problems. And while they praise the Government's efforts in reducing the budget deficit they say that consolidation has been achieved too much by increased taxes and levies with the effect that tax legislation has become over complicated. The institutes recommend that the Government's planned two-stage income tax reform in 1986 and 1988 should be brought in in one stage in 1986 in order to obtain the maximum economic benefit. The report also calls for more privatisation and, in order to achieve higher employment, real wage increases kept below productivity growth rates.

4. Initial business reactions to the report have agreed with its general tenor. The business daily "Handelsblatt", sums it up "The economy is already past its peak". The institutes' recommendation that income tax reform should be in one stage will help fuel the continuing debate on this. Stoltenberg remains committed to the Government's announced plan of a two-stage reform (he argues one large step is incompatible with the Government's policy of reducing the budget deficit), but Franz Josef Strauß, with some support from Bangemann, is pressing for a one-stage reform. Lambsdorff, as economic spokesman of the FDP, agrees.

Detail

5. The five major economic institutes (Hamburg, Essen, Munich (IFO), Berlin and Kiel) produced the second of their half-yearly reports today. They forecast real GNP growth of 2.5% in 1984 and 2% in 1985. This forecast is based on the assumption that real GNP in western industrial countries will grow by 5% on average in 1984 declining to 3% in 1985. Real world trade will increase by between 8% and 9% in 1984, declining to around 4% next year. Real GNP in the USA will grow by 7% in 1984 and by 3.5% in 1985. Unemployment in the USA will increase but only slightly while consumer inflation (assuming no strong increase in the value of the dollar) will rise to 5% in 1985 after about 4.5% in 1984. Real GNP in Japan will increase by 5.5% this year followed by 4% next with consumer prices growing by around 2.5% in 1985 - only slightly up on 1984. Western Europe economies are expected to grow by about 2% in 1985 after 2.2% in 1984: unemployment will increase slightly, while inflation will fall to around 5% after 6% this year.

FRG Economy: Assumptions

6. The Five Institutes' forecast for the West German economy in 1985 is based on the following assumptions:

a) world trade will expand by about 4%;

b) the US\$ will remain high in relation to the Deutschemark and will record the same annual average in 1985 as in 1984. The Deutschemark will strengthen within the EMS;

c) no significant change in world market prices for industrial raw materials. The dollar price of oil will ease slightly;

d) the Federal Government's financial policies to remain on course - expenditure increases will continue to be low and the budget deficit will be reduced further;

e) the Bundesbank's Central Bank Money monetary growth targets will be in the range of 4% - 6%;

f) wage costs will increase more strongly in 1985 than 1984 because of the cut in working time. Additional costs will be incurred as a result of early retirement schemes.

7. Details of the forecast are as follows:

Exports

The current upturn in industrial economies has improved foreign demand and on annual average FRG's exports are expected to grow this year by 8% on a year ago - without the metal workers' strike the increase would have been higher. The Dollar-Deutschemark relationship during 1984 has improved West German competitiveness resulting in an increase in market shares. In 1985 a further increase of 6.5% in exports will occur, despite the slowing down in world trade (the slow down is thought likely to occur in areas which will not affect German exporters).

Investment

Investment in capital goods has increased sharply following the conclusion of the metal workers' strike. It has now reached the high point of the end of 1983/beginning of 1984. Investment in 1985 will be stronger than this year increasing by 5% (real) encouraged by higher profits and a downturn in interest rates. Investment in modernisation will increase, but following the agreement on a shorter working week, the proportion of investment in rationalisation will rise in 1985.

Construction

With the expiry of government incentives for the residential construction sector at the end of 1984, the construction sector will register a real increase of 3.5%. However, the incentives have had the effect of bringing forward demand in housing and despite the possibility of a slight increase in local authority construction, the construction sector as a whole is forecast to decline by 0.5% in 1985.

Private Consumption

Private consumption will increase only moderately (up 1.5%) in 1985. While the upwards development of incomes of private households will no longer be dampened by government savings measures, the improvement will be limited as a result of the agreements on shorter working time.

Disposable income will increase by 3.5% (nominal) in 1985 - the same rate as in 1984. The savings ratio will remain unchanged at 11.5%.

Production

Capacity utilisation is not expected to change. Manufacturing output is expected to increase somewhat more strongly than real GNP while construction output will fall. The relatively constant growth in the tertiary sector will continue.

Employment

The number of employed will increase slightly in the services sector but at best stagnate in the manufacturing sector and fall markedly in the construction sector. On the other hand the potential labour force will increase by an approximate 30,000 - 40,000. The latent reserve will grow further. All in all the number of registered unemployed, despite the return home of some gastarbeiter, will increase by about 10,000 in 1985.

Current Account

With the strong increase in exports and only relatively small growth in imports the real visible trade surplus will increase considerably. Although the deficits on services and transfer payments will also increase, the current account surplus will be around DM 10 billion in 1984 and about DM 20 billion in 1985.

Prices

Although import prices will fall in 1985, unit wage costs will increase leading to a less favourable price position than towards the end of 1984 (inflation in September was rising at 1.5%) thus producing an increase of 2% on annual average.

Policy Considerations

The institutes concentrated on three aspects of policy

- a) General Economic
- b) Monetary Policy
- c) Wage Policy

a) General Economic

The institutes argue that the success in reducing the budget deficit has failed to eliminate the weakness in investment although it has had positive effects on confidence. Budgetary consolidation has been achieved by increasing taxes and levies with the result that tax legislation has become even more complicated. And further consolidation could have been possible had subsidies to the sunset industries been reduced.

The legislation proposed by the Cabinet on employment promotion and income tax reform are a step in the right direction but they do not go far enough to provide lasting growth. The institutes criticise the make up of the planned tax reform, calling for more emphasis on the need to promote initiative rather than on family considerations. They make a plea for a full introduction of the income tax package in 1986.

The institutes also recommend further deregulation and privatisation together with less government intervention.

b) Monetary Policy

It is recommended that monetary growth should take medium term (rather than short term) growth potential, currently 2.5%, as a yardstick. In the light of the fact that the reduced level of inflation is being offset by cost incentive wage agreements, growth of Central Bank Money should be around 5%. The institutes also recommend that the Bundesbank should be encouraged to announce its growth targets for the following years in advance.

c) Wage Policy

There are indications that wage decisions in the course of 1984 are constraining growth and preventing any improvement in employment. In order to achieve higher employment, real wage increases must remain consistently below productivity growth rates.

The cost effects of the shorter working week are hard to gauge but represent a massive increase in supplementary wage costs. The institutes therefore recommend that more market orientated flexibility is required.

8. The Munich and Berlin institutes dissent from criticism of this year's wage round. They argue that the flexibility created will allow for increased productivity. The Berlin Institute (Keynesian) dissents from the views expressed in the report on privatisation, tax reform and government intervention.

9. Detailed forecast overleaf.

BULLARD

FRAME ECONOMIC

ECD (1)

NATIONAL ACCOUNTS
ESTIMATE 1984/85

DIE WICHTIGSTEN DATEN DER VOLKSWIRTSCHAFTLICHEN GESAMTRECHNUNG
Vorausschätzung für die Jahre 1984 und 1985

	1983 ¹	1984 ²	1985 ²	1984		1985	
	Jahre			1. HJ. ¹	2. HJ. ²	1. HJ. ²	2. HJ. ²

ORIGIN OF GNP

1. Entstehung des Sozialprodukts
Veränderung in vH gegenüber dem Vorjahr **CHANGES ON PREVIOUS YEAR**

Zahl der Erwerbstätigen LABOUR FORCE	-1,7	-0,5	0	-0,5	0	0	0
Arbeitszeit (arbeitstäglich) HOURS WORKED (per working day)	-0,1	0	-0,5	-0,3	0,5	0,5	-1
Arbeitstage ³ WORKING DAYS	0	0	-0,5	0,4	-1	-1	0,5
Arbeitsvolumen (kalendermonatlich) HOURS WORKED (MONTHLY)	-1,8	-0,5	-1	-0,4	-0,5	-0,5	-1
Produktivität ⁴ PRODUCTIVITY	2,8	3	3	2,6	3,5	3	2,5
Bruttoinlandsprodukt in Preisen von 1976 GDP	1,0	2,5	2	2,2	3	2,5	1,5

2. Verwendung des Sozialprodukts in jeweiligen Preisen

USE OF GNP a) Mrd. DM **IN CURRENT PRICES**

Privater Verbrauch PRIVATE CONSUMPTION	347,2	982,5	1018,5	475,5	507	492	526,5
Staatsverbrauch GOVERNMENT CONSUMPTION	334,2	344,5	357,5	159,7	184,5	166	191,5
Anlageinvestitionen FIXED CAPITAL FORMATION	346,5	363,5	377,5	162,4	201	173	204,5
Ausrüstungen MACHINERY AND EQUIPMENT	137,6	142,5	153	62,5	80	69,5	83,5
Bauten BUILDINGS	209,0	221	224,5	99,9	121,5	103,5	120,5
Vorratsveränderung CHANGE IN STOCKS	4,9	14,5	12,5	13,1	1,5	9,5	3
Außenbeitrag NET EXPORTS OF GOODS AND SERVICES	38,8	44	61	15,0	29	26	35
Ausfuhr EXPORTS	540,0	597,5	650	285,4	312	316	334
Einfuhr IMPORTS	501,3	553,5	589	270,5	283	290	299
Bruttosozialprodukt GNP	1671,6	1748,5	1826,5	825,7	923	866,5	960

b) Veränderung in vH gegenüber dem Vorjahr

% CHANGE ON PREVIOUS YEAR

Privater Verbrauch	4,1	3,5	3,5	3,7	4	3,5	4
Staatsverbrauch	2,7	3	4	3,4	3	4	3,5
Anlageinvestitionen	4,8	5	4	4,1	5,5	6,5	1,5
Ausrüstungen	8,3	3,3	7,5	0,5	8	11	5
Bauten	2,5	6	1,5	6,4	5,5	4	-0,5
Ausfuhr	0,2	10,5	9	8,5	12,5	11	7
Einfuhr	0,1	10,5	6,5	11,5	9,5	7,5	5,5
Bruttosozialprodukt	4,5	4,5	4,5	4,2	5	5	4

3. Verwendung des Sozialprodukts in Preisen von 1976

USE OF GNP a) Mrd. DM **AT 1976 PRICES**

Privater Verbrauch	706,1	714,5	724,5	347,6	367	352,5	372
Staatsverbrauch	248,7	250	252	122,6	127,5	123,5	128
Anlageinvestitionen	256,5	263	267,5	118,0	145	123,5	144
Ausrüstungen	109,5	111	116	49,1	61,5	53	63
Bauten	147,0	152	151,5	69,0	83	70	81
Vorratsveränderung	3,8	13,5	11,5	10,1	3,5	7	4,5
Außenbeitrag	50,1	58	70	24,1	34	32,5	37,5
Ausfuhr	417,3	446,5	474	216,1	230,5	232	242
Einfuhr	367,2	388,5	404	192,0	196,5	199,5	204,5
Bruttosozialprodukt	1265,1	1299	1325,5	622,4	677	639	685,5

b) Veränderung in vH gegenüber dem Vorjahr

% CHANGE ON PREVIOUS YEAR

Privater Verbrauch	1,1	1	1,5	0,6	2	1,5	1,5
Staatsverbrauch	0	0,5	0,5	0,6	0,5	1	0,5
Anlageinvestitionen	3,1	2,5	2	1,4	3,5	4,5	-0,5
Ausrüstungen	6,1	1	5	-1,5	3,5	8,5	3
Bauten	0,9	3,5	-0,5	3,5	3,5	1,5	-2,5
Ausfuhr	-1,3	7	6	5,5	8,5	7,5	5
Einfuhr	0,5	6	4	7,0	4,5	4	4
Bruttosozialprodukt	1,3	2,5	2	2,2	3	2,5	1,5

noch: Die wichtigsten Daten der volkswirtschaftlichen Gesamtrechnung

	1983 ¹	1984 ²	1985 ²	1984		1985	
	Jahre			1. Hj. ¹	2. Hj. ²	1. Hj. ²	2. Hj. ²
GNP DEFLATOR							
4. Preisniveau der Verwendungsseite des Sozialprodukts (1976 = 100)							
Veränderung in vH gegenüber dem Vorjahr							
Privater Verbrauch PRIVATE CONSUMPTION	2,9	2,5	2	3,0	2	2	2,5
Staatsverbrauch GOVERNMENT CONSUMPTION	2,7	2,5	3	2,8	2	3	3
Anlageinvestitionen FIXED CAPITAL FORMATION	1,7	2,5	2	2,6	2	2	2
Ausrüstungen MACHINERY AND EQUIPMENT	2,3	2	2,5	2,0	2,5	2,5	3
Bauten BUILDINGS	1,6	2,5	2	2,8	2	2	2
Ausfuhr EXPORTS	1,5	3,5	2,5	2,8	4	3	2
Einfuhr IMPORTS	-0,4	4,5	2	4,2	4,5	3	1,5
Bruttosozialprodukt GNP	3,2	2	2,5	2,0	2	2,5	2,5

5. Einkommensentstehung und -verteilung

a) Mrd. DM

ORIGIN AND DISTRIBUTION OF INCOME

	1983	1984	1985	1984	1985	1984	1985
Bruttoeinkommen aus unselbständiger Arbeit WAGE AND SALARY INCOME	915,4	946,5	980,5	443,6	503	460	520,5
Bruttolohn- und -gehaltssumme GROSS	742,3	766,5	794,5	359,4	407	373	421,5
Nettolohn- und -gehaltssumme NET	510,2	520,5	535	246,7	274	254	281
Bruttoeinkommen aus Unternehmertätigkeit und Vermögen NET ENTREPRENEURIAL + PROPERTY INCOME	362,0	388	412	180,1	208	195	217
Nettoeinkommen aus Unternehmertätigkeit und Vermögen NET ENTREPRENEURIAL + PROPERTY INCOME	297,9	320,5	342,5	147,4	173	161,5	181
Entnommene Gewinne und Vermögenseinkommen DISTRIBUTED PROFITS + PROPERTY INCOME	280,9	306	326	148,2	157,5	157	169
Nichtentnommene Gewinne UNDISTRIBUTED PROFITS	17,1	14,5	16,5	-0,8	15,5	4,5	12
Volkseinkommen NATIONAL INCOME	1277,5	1334,5	1392,5	623,7	711	655	737,5
Abschreibungen DEPRECIATION	210,6	222	234,5	109,5	112,5	115,5	119
Indirekte Steuern abzüglich Subventionen INDIRECT TAXES - SUBSIDIES	183,5	192	199,5	92,5	99,5	96	103,5
Bruttosozialprodukt GNP	1671,6	1748,5	1826,5	825,7	923	866,5	960

b) Veränderung in vH gegenüber dem Vorjahr

	1983	1984	1985	1984	1985	1984	1985
Bruttoeinkommen aus unselbständiger Arbeit	1,7	3,5	3,5	2,9	4	3,5	3,5
Bruttolohn- und -gehaltssumme	1,4	3,5	3,5	2,9	3,5	3,5	3,5
Nettolohn- und -gehaltssumme	0,4	2	3	1,6	2,5	3	2,5
nachrichtlich: PER EMPLOYED PERSON							
Bruttolohn- und -gehaltssumme je Beschäftigten	3,4	4	4	3,6	4	4	3,5
Nettolohn- und -gehaltssumme je Beschäftigten	2,3	2,5	3	2,2	3	3	2,5
Bruttoeinkommen aus Unternehmertätigkeit und Vermögen	11,2	7	6	5,3	9	8,5	4,5
Nettoeinkommen aus Unternehmertätigkeit und Vermögen	12,9	7,5	7	4,6	10	9,5	4,5
Entnommene Gewinne und Vermögenseinkommen ⁵	3,4	9	6,5	6,4	11,5	6	7
Volkseinkommen	4,2	4,5	4,5	3,5	5,5	5	3,5
Abschreibungen	5,1	5,5	5,5	5,5	5,5	5,5	5,5
Indirekte Steuern abzüglich Subventionen	6,4	4,5	4	7,2	2,5	3,5	4,5
Bruttosozialprodukt	4,5	4,5	4,5	4,2	5	5	4

6. Einkommen und Einkommensverwendung der privaten Haushalte

a) Mrd. DM

INCOME AND USE OF INCOME OF HOUSEHOLDS

	1983	1984	1985	1984	1985	1984	1985
Nettolohn- und -gehaltssumme NET WAGES + SALARIES	510,2	520,5	535	246,7	274	254	281
Empfangene laufende Übertragungen OFFICIAL CURRENT TRANSFERS	290,2	293,5	300,5	146,3	147	149,5	151
Entnommene Gewinne und Vermögenseinkommen	319,7	346,5	367	169,6	177	178,5	188,5
Abzüge: Zinsen auf Konsumentenschulden INTEREST	18,5	17,5	17,5	8,9	9	8,5	9
DEDUCTIONS: Geleistete laufende Übertragungen OUTGOING TRANSFERS	32,5	34,5	36	16,1	18	17	19
Verfügbares Einkommen DISPOSABLE INCOME	1069,2	1108,5	1149	537,6	571	556,5	592,5
Privater Verbrauch PRIVATE CONSUMPTION	947,2	982,5	1018,5	475,5	507	492	526,5
Ersparnis SAVINGS	121,9	126	130,5	62,1	64	64,5	66
Ersparnis in vH des verfügbaren Einkommens (Sparquote)	11,4	11,5	11,5	11,5	11	11,5	11

b) Veränderung in vH gegenüber dem Vorjahr

	1983	1984	1985	1984	1985	1984	1985
Nettolohn- und -gehaltssumme	0,4	2	3	1,6	2,5	3	2,5
Empfangene laufende Übertragungen	2,6	1	2,5	1,1	1	2	3
Entnommene Gewinne und Vermögenseinkommen	4,6	8,5	6	8,8	8	5,5	6,5
Verfügbares Einkommen	2,3	3,5	3,5	3,6	4	3,5	4
Privater Verbrauch	4,1	3,5	3,5	3,7	4	3,5	4
Ersparnis	-9,5	3,5	3,5	3,0	3,5	3,5	3,5

noch: Die wichtigsten Daten der volkswirtschaftlichen Gesamtrechnung

	1983 ¹	1984 ²	1985 ³	1984		1985	
	Jahre			1.Hj. ⁴	2.Hj. ⁵	1.Hj. ⁶	2.Hj. ⁷
STATE REVENUE + EXPENDITURE							
7. Einnahmen und Ausgaben des Staates⁷							
a) Mrd. DM							
Einnahmen REVENUE							
Steuern TAXES	414,7	439,5	459	206,5	233	216	243
Sozialbeiträge SOCIAL SECURITY CONTRIBUTIONS	290,3	303,5	315	142,2	161	148	167
Erwerbseinkünfte GOV'T BUSINESS REVENUE	29,7	30	32	15,8	14	17	15
Sonstige laufende Übertragungen CURRENT TRANSFERS	19,8	21,5	22	9,9	11,5	10	12
Empfangene Vermögensübertragungen PROPERTY	6,4	6,5	6,5	2,9	3,5	3	3,5
Einnahmen insgesamt TOTAL REVENUE	760,9	801	834,5	377,4	423,5	394	440,5
Ausgaben EXPENDITURE							
Staatsverbrauch INVESTMENT CONSUMPTION	334,2	344,5	357,5	159,7	184,5	166	191,5
Zinsen INTEREST	50,1	53	55,5	28,3	24,5	29,5	25,5
Laufende Übertragungen an CURRENT TRANSFERS TO:	356,8	367,5	376,5	182,4	185	187	139,5
Private Haushalte HOUSEHOLDS	296,1	300,5	307,5	150,6	150	153,5	154
Unternehmen ENTERPRISES	34,6	38,5	39,5	17,2	21,5	18,5	21
Ausland ABROAD	26,1	28	30	14,6	13,5	15,5	14,5
Geleistete Vermögensübertragungen PROPERTY TRANSFERS	32,5	34	31,5	15,3	19	13,5	18,5
Nettoinvestitionen NET INVESTMENT	32,9	32,5	33,5	12,5	20	13	20,5
Ausgaben insgesamt TOTAL EXPENDITURE	806,4	831,5	854,5	398	433	409	445
Finanzierungssaldo BALANCE	-45,5	-30,5	-20	-20,9	-9,5	-15,5	-4,5

b) Veränderung in vH gegenüber dem Vorjahr
% CHANGE ON PREVIOUS YEAR

Einnahmen							
Steuern	4,9	6	4,5	8,1	4	4,5	4,5
Sozialbeiträge	2,0	4,5	4	3,1	5,5	4	3,5
Erwerbseinkünfte	0,1	1	7	-22,3	51	8	6
Sonstige laufende Übertragungen	20,6	9	1,5	6,4	11,5	1	1,5
Empfangene Vermögensübertragungen	1,3	1,5	0	3,5	-0,5	-0,5	0,5
Einnahmen insgesamt	3,9	5,5	4,5	4,4	6	4,5	4
Ausgaben							
Staatsverbrauch	2,7	3	4	3,4	3	4	3,5
Zinsen	14,1	6	4,5	2,9	9,5	5	3,5
Laufende Übertragungen an	2,1	3	2,5	3,3	2,5	2,5	2,5
Private Haushalte	1,5	1,5	2,5	1,5	1,5	2	2,5
Unternehmen	4,7	11,5	1,5	13,0	10,5	6	-2
Ausland	5,6	8	5,5	12,1	4	5,5	6
Geleistete Vermögensübertragungen	3,1	4	-7,5	6,5	2	-13	-2,5
Nettoinvestitionen	-11,1	-0,5	3	-5,2	3	5	2
Ausgaben insgesamt	2,5	3	3	3,1	3	3	3

1) Nach Angaben des Statistischen Bundesamtes (vgl. Wirtschaft und Statistik, Heft 9/1984) sowie eigene Berechnungen der Arbeitszeit und der Produktivität; Abweichungen in den Summen durch Rundung der Angaben in Mrd. DM bedingt. - 2) Vorausschätzungen der beteiligten Institute; Angaben gerundet. - 3) Veränderung der Zahl der Arbeitstage nur zur Hälfte berücksichtigt. - 4) Bruttoinlandsprodukt in Preisen von 1976 je Erwerbstätigenstunde. - 5) Nach Abzug der Zinsen auf Konsumentenschulden. - 6) Nicht zurechenbare Steuern, freiwillige Sozialbeiträge der Selbständigen, Hausfrauen u.ä., Rückerstattungen und sonstige laufende Übertragungen an den Staat, Nettoprämien für Schadenversicherungen abzüglich Schadenversicherungsleistungen, internationale private Übertragungen. - 7) Gebietskörperschaften, ZRP, Lastenausgleichsfonds und Sozialversicherung.