UNCLASSIFIED
SAVING TELEGRAM

Prime Minister
This explains Kohl's jubilation.
CDP

BY BAG
FROM BONN
FRAME ECONOMIC
TO FCO TELNO 33 SAVING OF 30 NOVEMBER 1984. Info all EC Posts, UKDel OECD, UKMis Geneva, all Consulates-General in the Federal Republic, Washington, Tokyo, Vienna.

FEDERAL GERMAN ECONOMY

Summary

1. A good month highlighted by a very optimistic report from the Five Wise Men, forecasting investment and export led growth of 3% GNP next year; supported by an IFO survey projecting a 10% increase in investment in 1985, and also by the trade figures for October showing an increase in exports of 27% on a year earlier. West Germany is now heading for a record trade year.

2. Other good news included a 3.2% settlement on public sector pay, an increase in private consumption, a slight fall in the number of unemployed (seasonally adjusted) and a relatively smooth ride for the Government in the second reading of the Federal Budget.

3. The only shadow in this bright picture was a decision by the courts to declare the investment loan unconstitutional. This, together with a downward revision of tax estimates will cause a slight hiccough in PSBR.

Detail

4. The Five Wise Men's annual report published on 23 November (Bonn telno 32 saving of 27 November) was very optimistic, forecasting real GNP growth of "a good 3%" based on investment and exports. It has been enthusiastically received by trade and industry. The Five Wise Men expect investment in 1985 to grow by 4% (real): within this overall figure machinery and equipment will go up 10% with construction registering zero. World trade will increase by 5.5% and German exports by around 7%. Private consumption will also increase in real terms by 2.5% after 1% this year. The report praises the Government's economic record to date although it is critical of continued subsidies to ailing

/industries.

industries. However, both the opposition and the trades unions criticise the fact that no solution to unemployment has been offered - the Five Wise Men forecast that unemployment will fall by 100,000 but remain above 2 million.

5. The IFO Institute's six monthly survey on investment prospects supports the Five Wise Men's optimism. Investment in production will rise by 8% (real) next year with expectations of continued growth in exports. The weakness in domestic demand has yet to be overcome. Over 50% of the 2,800 firms surveyed intend to invest more. There will however be sectoral variations eg. electrical engineering up 15% and construction stagnating around this year's low level. Investment in rationalisation will predominate but there will be some increase in capacity in all sectors with the exception of construction.

6. The latest trade figures also support the Five Wise Men's optimism. A record monthly trade surplus of DM 8.8 billion was recorded in October and exports for the month were up 27% on the high level of a year ago. The trade performance will have a healthy impact on current account, which even though now showing a surplus of DM 6 billion, was in the red for the first nine months. A current account surplus of DM 10 billion or more for the year as a whole is now likely.

7. Retail trade turnover figures for July and August have been revised sharply upwards showing that private consumption has made a bigger contribution to GNP than expected. From the second to the third quarter, retail turnover rose by 1%, above the already high level attained in the first quarter. This is all the more surprising as first quarter private consumption had been influenced positively by special factors such as premature payment of holiday and Christmas bonuses. The signs are favourable that the current strength of private consumption will continue, following a further improvement in the consumer climate index in October.

8. Other good news for the Government included a surprisingly quick conclusion to the public services wage agreement. From

/1 January

1 January 1985 public service pay will increase by 3.2% which is about the going rate for settlements in the private sector and 1.2% above the current rate of inflation. On shorter working time, it has been agreed that two extra paid holidays will be granted to those aged 58 and above and this arrangement will be extended to those aged 50 from 1 January 1986 and to all members from 1 January 1987. The agreement applies not only to the 2.7 million workers represented by the public services trades union (ÖTV) but also to the Post Office, the railways, established civil servants (Beamte) and to the armed forces. The cost to the Government is estimated at around DM 8.5 billion in 1985. The settlement has been favourably received mainly because it removes any threat of industrial action by the public services in the coming year. Nevertheless, it is advantageous to the unions as the Government's "nil round" was scheduled to preclude any increase before 1 April 1985. The settlement means an increase in real wages for the public services for the first time in three years. The terms of the agreement suggest that the Government was not interested in further industrial relations strife, following the long drawn out and unexpectedly bitter metal workers' strike. More good news on the labour front included a slight fall in the seasonally adjusted number of unemployed (down 24,000).

9. The Government will also be pleased with its performance during the second reading of the Federal Budget debate which began on 28 November. Chancellor Kohl was able to deliver a confident speech listing a number of the coalition's economic achievements including stable prices, real wage increases, lower interest rates, the falling financial deficit and even some progress on the unemployment front. The Government came under criticism from the opposition on the parlous state of the pension funds but Blüm, the Minister of Labour, was able to give assurances that there was no cause for alarm.

10. The only shadows to this generally bright picture were the decision by the Federal Constitutional Court instructing the Government to repay the special income tax surcharge (known as the

/investment

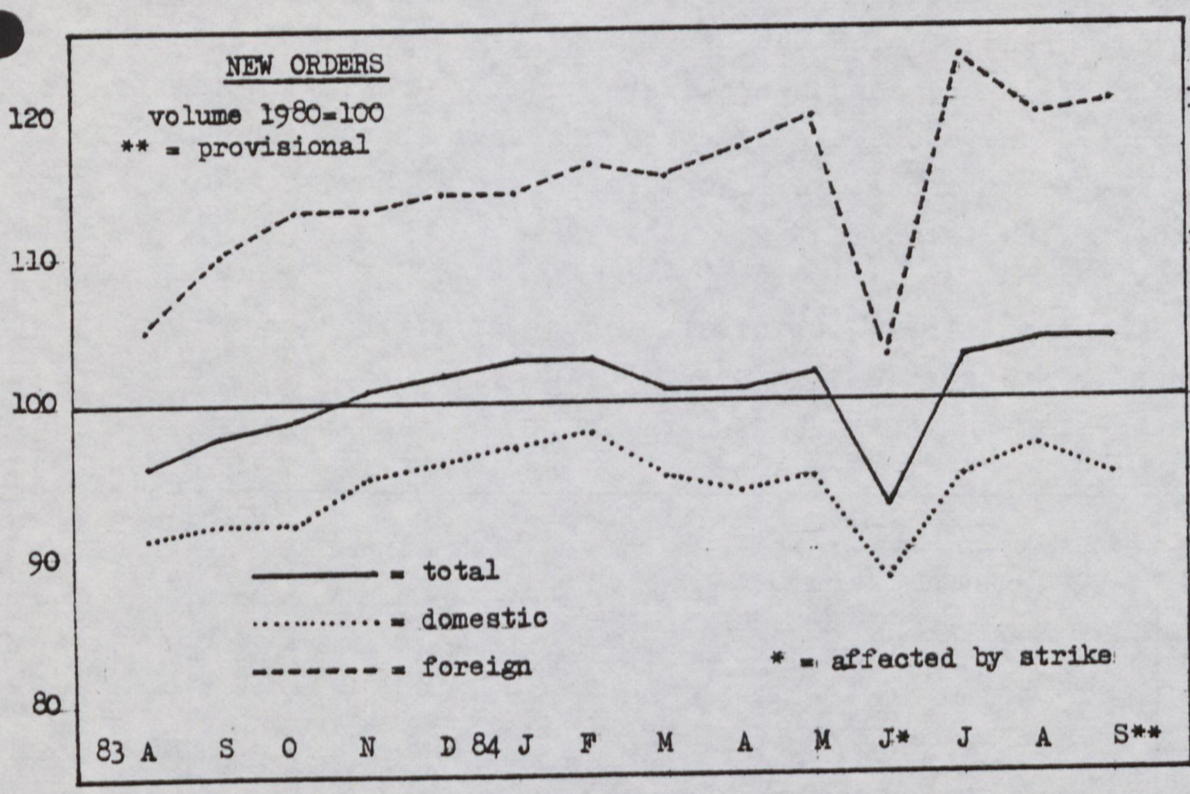
investment levy) imposed in 1983 and the downward revision of revenue estimates (Forbes-Meyler's letter of 14 November to Graham, Treasury). Both developments will affect the Federal Borrowing Requirement. The investment levy was imposed on higher tax payers in 1983 and was the equivalent of 5% of income tax. It was to be repaid between 1990 and 1993 without interest. The Government is now refunding the levy which will amount to about DM 2 billion. The coalition are now considering a substitute measure although initial calls for a surtax have been rejected.

11. According to tax estimates released in mid-month, federal revenue will fall short of earlier estimates by DM 2.8 billion in 1984 and DM 4 billion in 1985. The loss of revenue in 1984 results from the effects of the metal workers' strike and the introduction of early retirement schemes; and in 1985 lower revenue is due to the downward revision of nominal GNP growth estimates. The negative effect of these developments on PSBR will however be offset to some extent by the fact that the 1984 Bundesbank windfall profit, payable in 1985, will increase from the present estimate of DM 10.5 billion to "at least" DM 12-13 billion. Thus, although Federal PSBR will be slightly higher than originally targetted, it will remain within the planned figure of "under DM 30 billion" in 1984 and around DM 25 billion, rather than earlier estimates of DM 24 billion, in 1985.

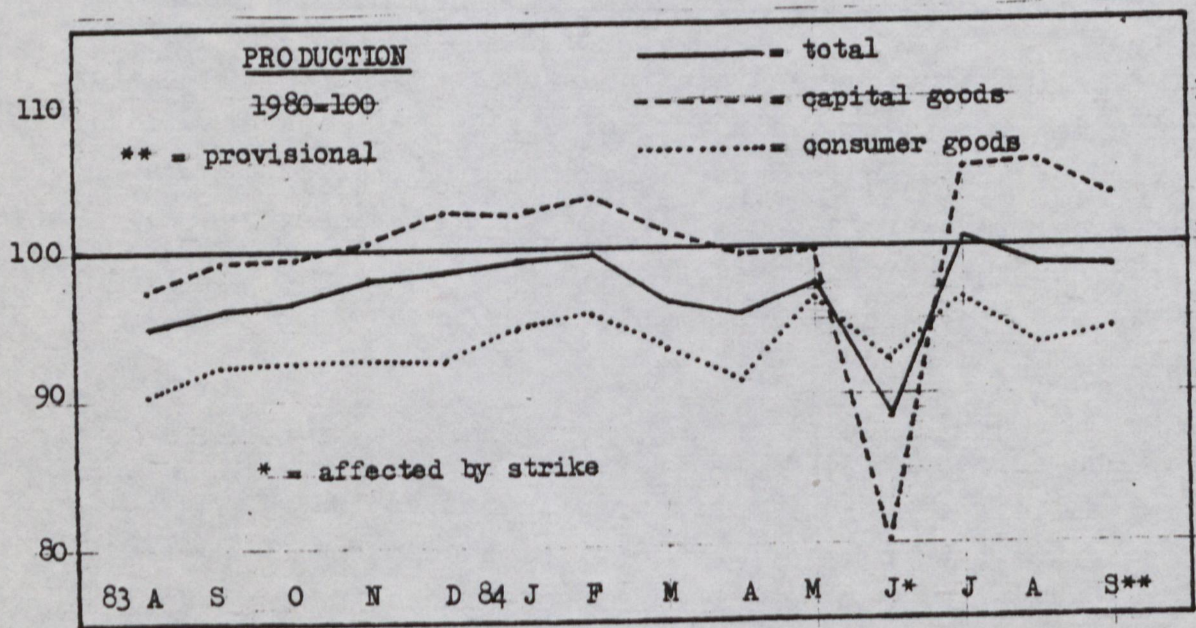
Prospects and Indicators

12. September's provisional new orders figures show that the high level attained in August was maintained. Although domestic orders fell by 2%, export orders rose by 1%. The two monthly comparison August/September on a year ago shows that overall demand in real terms was 4% higher with domestic demand up by 2.5% and export orders by 7.5%. Provisional Q3 figures underline the strength of the recovery in demand following the strike with the total volume of new orders exceeding the level reached in the first quarter.

/NEW ORDERS



13. The overall level of production in September was virtually unchanged on the preceeding two months and continues to register a strong recovery after the metal workers' strike in the summer. The two monthly comparison August/September on a year earlier shows that overall production was up by 1.5%: manufacturing by 2%; capital goods by 4% and consumer goods by 1%. Construction activity continues to remain disappointing, down 6.5%. Provisional Q3 figures show that all major sectors, with the exception of construction, have reverted to the high level of output registered in Q1.



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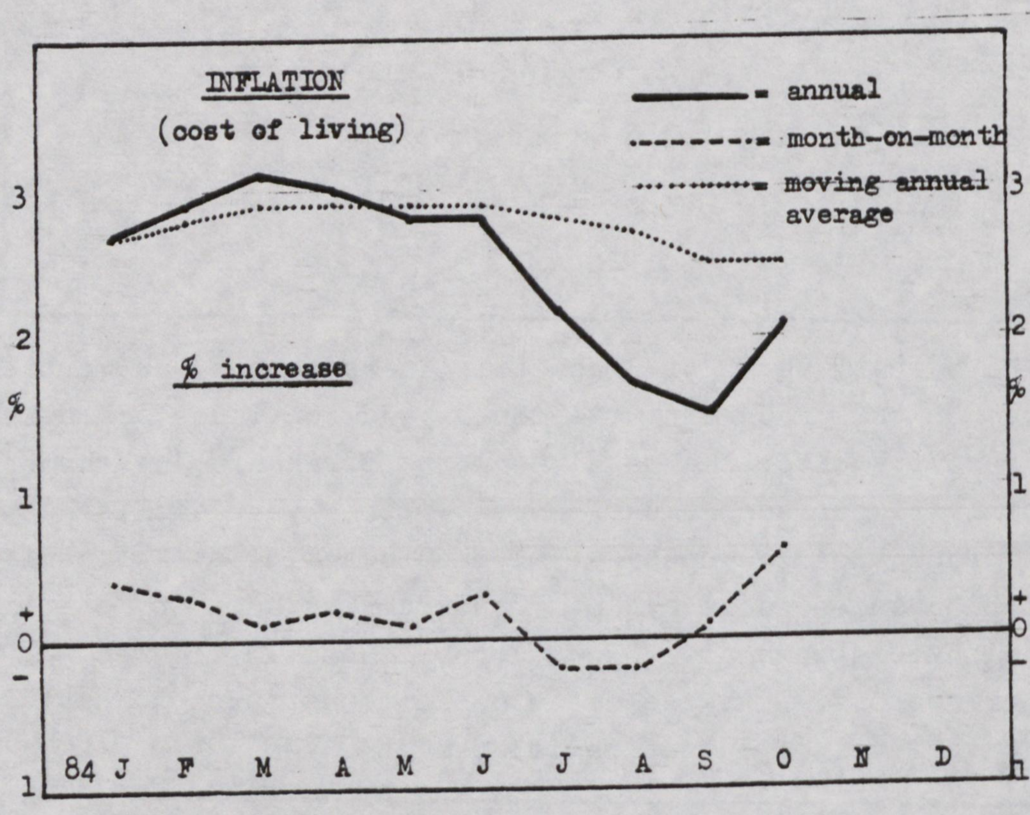
14. Private consumption as measured by retail trade turnover has improved markedly. The October IFO survey also registered a furth[er] improvement in the consumer climate index. Growth in private consumption therefore has been given a spur which, according to the Five Wise Men's report, will continue into 1985 with the expected growth of 2.5% (real) after 1% this year.

15. The annual rate of inflation cost of living index rose in October to stand at 2.1% after 1.5% in September. The moving annual average now stands at 2.5%.



16. A slight improvement continues on the labour front. For the first time since 1980 the number of employed in the manufacturing industry recorded an increase, while short-time working in October registered a slower rate of increase than in recent years. However, it is clear that given the depressed state of the construction sector, coupled with the approach of winter, the labour market will be exposed to additional pressure.

17. The current account in September finished in balance compared with a deficit of DM 1.5 billion in August but the figures for October show a surplus of DM 6.5 billion compared to DM 3.8 billion in October 1983. This was a result of a huge improvement in export performance (up 27%) on a year earlier with imports increasing by 17%.

/The

The net foreign assets of the Bundesbank fell in September by DM 4.2 billion as a result of Bundesbank intervention. In the face of the strong dollar in October they fell by a further DM 1 billion.

28. Leading interest rates remain unchanged with Discount at 4.5% and Lombard at 5.5%. Market rates, yield on bonds outstanding, fell to 7.4% in October after 7.7% in September and 7.9% in August. Central Bank Money figures for October indicate a growth rate on the final quarter of 1983 of 5% exactly in the middle of this year's target corridor of 4-6%.

BULLARD

| NEW ORDERS

New orders

29. Provisional new order figures for September indicate that the high level attained in August was maintained. Although domestic orders fell by 2 per cent, foreign demand rose by 1 per cent. The two-monthly comparison, August/September on June/July, is distorted by the effects of the strike in June and the resulting increase of 6 per cent gives a rather too positive picture of the development in demand. Compared to the corresponding two-month period a year earlier, however, overall demand in real terms was 4 per cent higher with domestic demand up by 2.5 per cent and export orders by 7.5 per cent. Provisional figures for the third quarter underline the recovery in demand following the strike with the total volume of new orders exceeding the level reached in the first quarter.

NEW ORDERS

1980=100

	Total		Domestic		Foreign	
	Value	Volume*	Value	Volume	Value	Volume
1983						
April	103	93	99	89	110	100
May	103	93	100	90	112	101
June	106	95	103	92	113	102
July	105	94	98	88	118	106
August	108	96	102	91	118	105
September	110	98	104	93	123	109
1984						
April	115	101	106	94	134	117
May	117	102	109	95	137	119
June	107	93	101	88	119	103
July	119	103	109	95	142	123
August	121	104	112	97	138	119
Septemb(p)	121	104	111	95	140	120
Quarterly						
1984 Q1	117	102	110	97	132	115
Q2	113	99	105	92	129	112
Q3(p)	121	104	111	96	140	121

* = at constant prices
(p)= provisional

/Production

Production

30. The overall level of production in September was practically unchanged on the preceding two months having recovered strongly after the strike. Between August and September manufacturing output recorded a small decline (- 0.5 per cent), while construction output was 1.5 per cent below the heavily revised August result. As with new orders the two-monthly comparison, August/September on June/July, is distorted by the strike-induced output losses in June and the 6 per cent upturn in manufacturing output paints a too positive picture. Compared to the corresponding two-month period a year earlier overall production was 1.5 per cent higher. Maufacturing outurn was 2 per cent up on a year earlier, the field being led by capital goods (+ 4 per cent), followed by consumer goods (+ 1 per cent) and basic and producer goods (+ 0.5 per cent). Construction activity remained disappointing, down 6.5 per cent. Provisional quarterly figures show all major sectors having reverted to a level of output higher than in the first quarter following the set-back in the second quarter, with the exception of construction.

PRODUCTION

1980=100

	Total	Basic & producer goods	Capital goods	Consumer goods	Construction
1983					
April	93.5	91.6	97.7	90.2	79.8
May	93.9	92.0	98.0	90.5	83.8
June	97.7	94.3	100.9	96.7	87.9
July	94.8	93.0	96.9	90.7	88.0
August	95.2	93.9	97.1	90.4	90.5
September	96.4	96.0	99.8	91.7	88.4
1984					
April	95.6	96.5	99.7	91.0	76.5
May	97.7	97.0	99.9	96.5	86.0
June	88.3	93.0	80.1	92.2	81.7
July	100.5	99.1	105.1	96.4	90.9
August	98.7	95.9	105.7	93.2	84.7
Septemb*	98.5	96.8	103.2	94.3	83.3
Quarterly					
1984 Q1	98.5	98.6	102.3	94.4	88.1
Q2	93.8	95.5	92.6	93.0	81.6
Q3*	99.3	97.2	105.1	94.8	86.3

* = provisional

/Private Consumption

Private consumption

31. Retail trade turnover figures for July and August have been revised sharply upwards; in the light of the new statistics, private consumption made a more marked contribution towards GNP growth than originally thought. From the second to the third quarter retail turnover rose by 1 per cent, thus taking it above the already high level attained in the first quarter. This is all the more surprising as first quarter private consumption had been influenced by special factors such as premature payments of holiday and Christmas bonusses. The signs are favourable that the current strength of private consumption will continue, with a further improvement in the consumer climate index recorded in October.

Prices

32. As expected, the rate of inflation, cost of living index, rose again in October to stand at 2.1 per cent after 1.5 per cent in September.Month-on-month prices rose by 0.6 per cent. The moving annual average now stands at 2.5 per cent. Food prices in October remained only 0.5 per cent higher than a year earlier.

33. Retail prices in October rose by 0.4 per cent month-on-month with the annual rate rising to 1.8 per cent after 1.5 per cent in September. Industrial producer prices rose by 0.5 per cent month-on-month with the annual rate edging up to 3.1 per cent from 2.7 per cent. Wholesale prices were 2.1 per cent higher than a year earlier. Other indicators are for September. Agricultural producer prices stood 2.6 per cent below their level a year earlier. Doubtless affected by the strong dollar, import prices jumped 1.2 per cent month-on-month, with the annual rate moving up from 4.7 per cent in August to 5.4 per cent in September. Export prices showed an annual increase of 3.4 per cent after 3.2 per cent in August. Latest Terms of Trade figures for September show a further worsening on August to stand 1.6 per cent down on a year ago.

Prices
1980=100

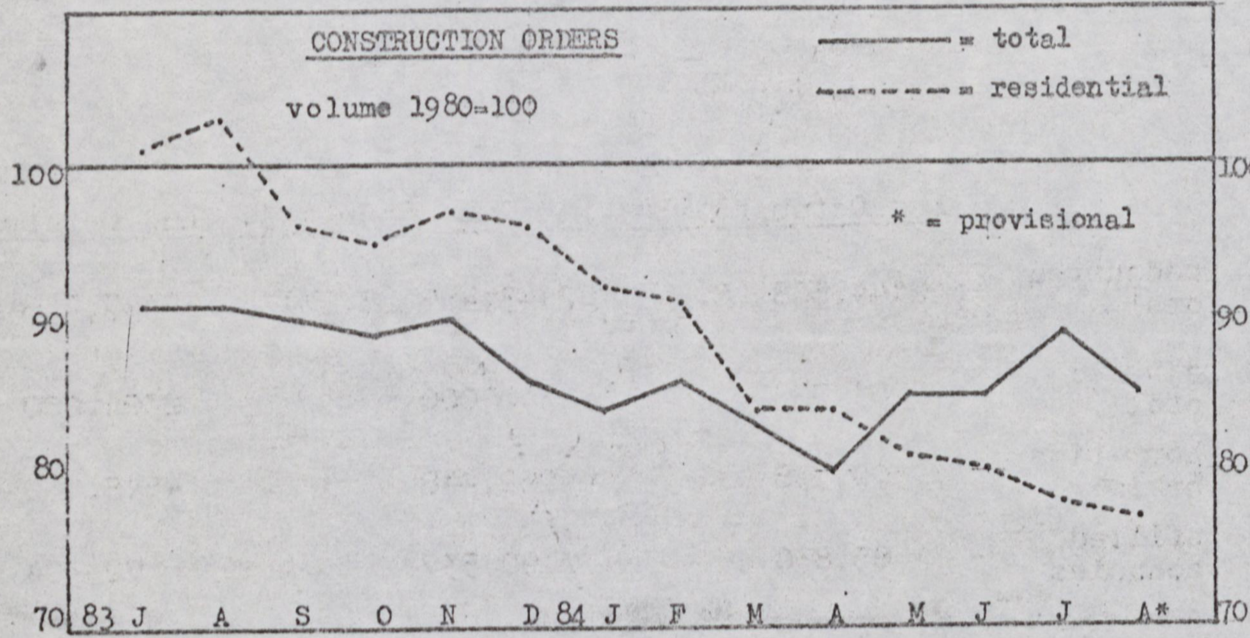
	Cost of living	Industrial producer prices	Agricultural producer prices	Retail prices 1976=100	Import prices	Export prices
1983						
July	115.8	115.6	103.8	132.0	115.5	112.4
August	116.2	116.3	105.3	131.9	117.7	112.9
September	116.5	116.6	107.3	132.2	118.3	113.3
October	116.5	116.7	107.2	132.3	117.3	113.2
1984						
July	118.4	119.3	108.2	134.8	122.5	116.2
August	118.2	119.3	106.4*	134.2	123.2	116.5
September	118.3	119.7	107.0*	134.2	124.7	117.1
October	119.0	120.3		134.7		

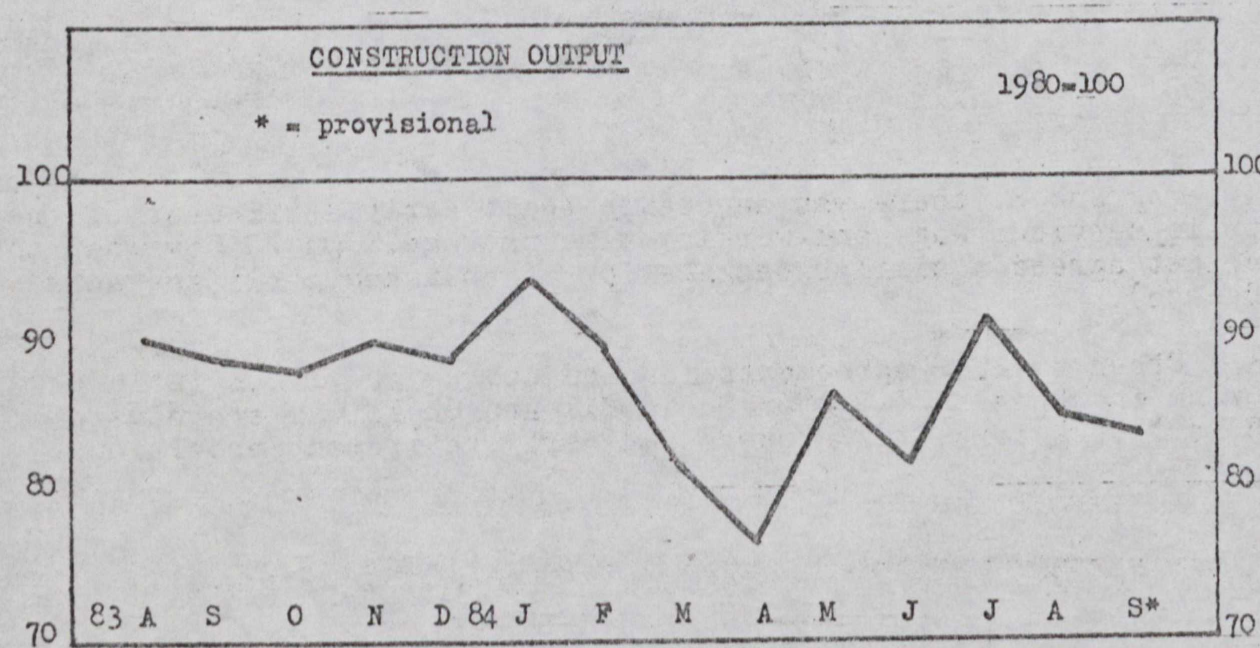
* = provisional

/Construction

Construction

34. Construction output fell further in September, down 1.5 per cent on the heavily revised August figure, and in the two-month period August/September showed a 6.5 per cent decline on the corresponding two month period a year earlier. Figures for the third quarter show a 6 per cent improvement on the low level of the second quarter but this was insufficient to reattain the first quarter level. The trend now seems to be firmly downwards with capacity utilisation in the third quarter also falling. The picture for new orders improved, if only marginally. Latest figures for July/August show an upturn in total orders of 2.5 per cent over the previous two-months although the weakness of the residential sector persisted.





/Labour Affairs

Labour Affairs

35. The labour market has recorded a better result in October than at the same time in previous years. This is reflected in the decrease in the seasonally adjusted number of unemployed ie. down by about 30,000 on September and by 20,000 on October 1983. More jobs are being created in the automobile industry as well as in manufacturing, particularly in engineering and electrical engineering. Nevertheless the depressed state of the construction industry and the approach of winter will produce a negative effect on the labour market.

36. Youth unemployment (especially those under 20 years of age) fell by 14,300 at the end of October ie. by 8% on September and by 5% on a year earlier. The detailed figures are as follows:

	End October 1984	End September 1984	End October 1983
a) Unadjusted total	2144,508 (8.6%)	2143,486 (8.6%)	2147,756 (8.7%)
b) Adjusted total	2281,000	2310,000	2301,000
c) Short-time working	300,538	262,448	548,532
d) Unfilled vacancies	85,830	90,537	72,304
e) Total men in a)	1154,969	1154,782	1153,035
f) Total women in a)	989,539	988,704	994,721

37. There were no industrial disputes of note. However, as reported in paragraph 8, there was an unexpectedly early settlement of the public services wage and working time package. On 20 November the Cabinet agreed a similar package for established civil servants (Beamte).

38. Other smaller agreements reached during the month included a wage increase of 3.2% for Mobil Oil and Shell workers plus a 35 hour week for older workers and early retirement provisions.

/Balance of Payments

Balance of payments

39. Current account in September finished in balance compared with a deficit of DM 1.5 billion in August and DM 0.7 billion a year earlier. In the first nine months of the year the current account shows a small deficit of DM 0.3 billion compared to a surplus of DM 0.5 billion in the corresponding period 1983. In seasonally adjusted terms the current account in September recorded a surplus for the third consecutive month. Decisive for the favourable development was a surge in the visible trade surplus from DM 3.8 billion in August to DM 5.3 billion in September. A year earlier the surplus had been only DM 3.6 billion. Exports were 7 per cent up on a year ago while imports grew by 3 per cent. In the first nine months of the year the visible trade surplus stood at DM 32.1 billion compared with DM 30.4 billion between January and September 1983. On services account the deficit was practically unchanged on the preceding month (DM 2.3 billion) although the negative tourist expenditure balance fell to DM 2.6 billion. Outgoing transfer payments were also unchanged at DM 2.6 billion. On long-term capital account outflows of DM 3 billion were recorded after small inflows in August. On short-term capital account there were also renewed outflows (DM 1.8 billion).

40. Figures for October indicate that foreign trade reached record levels. Exports were 27 per cent higher than a year earlier and imports 17 per cent, with the visibile trade balance reaching DM 8.8 billion. The surplus on current account was DM 6.5 billion, compared to only DM 3.8 billion in October 1983. The surplus for the year so far now stands at DM 6 billion with an annual surplus of DM 10 billion or over now likely.

41. The net foreign assets of the Bundesbank fell in September by DM 4.2 billion as a result of Bundesbank intervention in the face of the strong dollar. In October they fell by a further DM 1 billion. After a brief period below DM 3, the dollar in late November has again moved above the DM 3 barrier.

Monetary

42. Leading interest rates remained unchanged with Discount at 4.5 per cent and Lombard at 5.5 per cent. Market rates, yield on bonds outstanding, fell to 7.4 per cent in October after 7.7 per cent in September.

43. Private sector credit, which had expanded strongly in August and September, weakened slightly in October. Over the last three months and at a seasonally adjusted annual rate private sector credit has risen by 6.5 per cent with the emphasis on short-term loans. Monetary capital formation was stronger in October than in September. In total monetary growth was thus weaker in October. M3 over the last three months has expanded at a seasonally adjusted annual rate of 6 per cent, exceeding its corresponding 1983 level at the end of October by 4 per cent. Both M2 and M1 expanded at an annual rate of 7 per cent. Central Bank Money figures for October indicate a growth rate on the final quarter 1983 of 5 per cent, exactly in the middle of this year's target corridor of 4-6 per cent.

/FRG/UK Trade

FRG/UK Trade

30.11.84: £ = DM 3.71

44. In the twelve months to the end of September 1984 FRG imports from the UK totalled DM 31.4 billion, 7.4 per cent of total FRG imports. A year earlier the UK market share stood at 6.9 per cent. While total FRG imports rose by 12.3 per cent at an annual rate, imports from the UK increased by 19.8 per cent. Excluding oil, total FRG imports rose by 13.3 per cent, while imports from the UK rose by 18.7 per cent with the UK share of the non-oil import market climbing to 5.5 per cent from 5.3 per cent a year earlier. The graph clearly illustrates the rising market share for both total and non-oil imports.

45. FRG exports to the UK over the period were up 12.9 per cent year-on-year against an increase of 10.5 per cent in total FRG exports. The proportion of FRG exports destined for the UK rose from 8.1 per cent to 8.2 per cent.

46. The trade gap in favour of the FRG declined to DM 7.4 billion after DM 8.1 billion a year earlier

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ECD (1)

/FRG MAIN

FRG: Main economic statistics

	Q2 83	Q1 84	Q2 84	q/month	year
1.Expenditure on GNP (current prices)		DM bn			
a) Gross National Product	414.8	433.9	425.2	-2.0	2.5
b) Private consumption	236.6	243.4	244.6	0.5	3.4
c) Government consumption	82.7	84.1	86.1	2.4	4.1
d) Fixed capital formation	85.8	89.5	86.4	-3.5	0.7
e) Exports of goods & services	132.5	146.3	142.2	-2.8	7.3
f) Imports of goods & services	122.5	137.7	135.0	-2.0	10.2
g) Net exports	10.0	8.6	7.2		
2.Expenditure on GNP (constant prices)					
a) Gross National Product	316.1	324.5	317.7	-2.1	0.5
b) Private consumption	177.5	178.2	178.2	0.0	0.4
c) Government consumption	62.1	61.8	62.7	1.5	1.0
d) Fixed capital formation	63.8	65.1	62.6	-3.8	-1.9
e) Exports of goods & services	103.3	111.0	107.4	-3.2	4.0
f) Imports of goods & services	91.2	97.4	95.7	-1.7	4.9
g) Net exports	12.1	13.6	11.7		
3.Income of households					
a) Gross wages & salaries	189.0	199.2	190.3	-4.5	0.7
b) Disposable income	269.7	281.0	276.5	-1.6	2.5
c) Savings as a % of b)	12.3	13.4	11.5		
		1976=100			
4.Productivity					
a) In the economy as a whole					
i) GNP per working person (1976 prices)	114.4	117.8	115.5	-2.0	1.0
ii) wage and salary costs per production unit	124.9	128.1	125.6	-2.0	0.6
		1980=100			
	Aug 83	Jul 84	Aug 84		
b) In industry					
i) output per employed person	106.0	114.0	112.0	-1.8	5.7
ii) wage and salary costs per production unit	109.0	103.0	106.0	2.9	-2.8
	Sep 83	Aug 84	Sep 84		
5.Industrial production					
a) Total	96.1	98.7	98.5	-0.2	2.5
b) Manufacturing industry	97.1	100.4	99.8	-0.6	2.8
c) Construction	88.4	84.7	83.3	-1.7	-5.8
6.New orders					
a) Total	98.0	104.0	104.0	0.0	6.1
b) Domestic	92.0	97.0	95.0	-2.1	3.3
c) Foreign	110.0	119.0	120.0	0.8	9.1

/7.

FRG: Main economic statistics

	Oct 83	Sep 84	Oct 84	q/month	year
		in 1000's			
7. Unemployment					
a) i) unemployed	2,147.7	2,143.5	2,144.5	0.0	-0.1
ii) as a % of the working population	8.7	8.6	8.6		
b) Short-time workers	548.5	262.4	300.5	14.5	-45.2
c) Vacancies	72.3	90.5	85.8	-5.2	18.7
		1980=100			
8. Prices					
a) Cost of living of all private households	116.5	118.3	119.0	0.6	2.1
b) Retail prices (1976=100)	132.3	134.2	134.7	0.4	1.8
c) Producer prices of industrial products	116.7	119.7	120.3	0.5	3.1

	Sep 83	Aug 84	Sep 84		
d) Export prices	113.3	116.5	117.1	0.5	3.4
e) Import prices	118.3	123.2	124.7	1.2	5.4
Terms of Trade	97.6	96.2	96.0	-0.2	-1.6
		DM bn			
9. Balance of payments					
a) Visible trade					
i) exports	37.8	37.9	40.5		
ii) imports	34.2	34.1	35.2		
iii) balance	3.6	3.8	5.3		
b) Supplementary trade items	0.3	-0.5	-0.4		
c) Services	-2.5	-2.2	-2.3		
d) Transfers	-2.0	-2.6	-2.6		
e) Current account	-0.6	-1.5	0.0		
10. Net foreign reserves	69.4	73.9	69.7		

Seasonally adjusted

	Oct 83	Sep 84	Oct 84
11. Money stock			
M1	1.9	3.9	0.8
M2	2.8	4.6	0.7
M3	4.2	6.4	2.5

Unadjusted

12. Monetary capital formation	7.0	1.8	4.9

Bank rates:

Since 29.6.84 Discount rate: 4.5%
Since 9.9.83 Lombard rate: 5.5%

Sources: Federal Statistical Office, Wiesbaden;
Deutsche Bundesbank, Frankfurt
Discrepancies in totals due to rounding (65)(20)

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