

UNCLASSIFIED
SAVING TELEGRAM

FROM BONN

FRAME ECONOMIC

TO PCO TELNO 8 SAVING OF 30 JUNE 1986. Info all EC Posts,
UKDel OECD, UKMis Geneva, all Consulates-General
in the Federal Republic, Washington, Tokyo, Vienna.

FEDERAL GERMAN ECONOMY

Summary

1. Economic growth slowed in the first quarter. Real GNP grew by only 1.6% on Q1 1985 and actually fell by 1% on Q4. Reactions to this development and its effects on growth prospects this year are mixed. The government blame the economic slowdown on the cold winter weather and early Easter holidays. They highlight a rise of 3.5% in private consumption and predict even stronger growth in this component in the second half of the year. A number of other positive factors support their optimism: export demand is not falling dramatically; inflation has remained negative for the last three months; April's figures are good and the business climate improved in April for the first time since October 1985. However, other commentators are not so sanguine about the future outlook. Two of the leading economic institutes have revised their forecasts for 1986 downwards to 2.5%-3%. The Berlin Institute have recommended the introduction of reflationary policies - a recommendation that Bangemann has declined unequivocally.

2. During the month the Bundesbank rejected demands to reduce interest rates, arguing that monetary targets were overshooting and that West German rates were already low by international standards.

3. On 25 June Stoltenberg gave his Cabinet colleagues the 1987 draft Federal Budget for their consideration on 1 July: expenditure is planned to rise by 2.9% (which includes provision for the new Ministry of the Environment) but, due to problems on the revenue side, the financial deficit will increase slightly. Privatisation proposals expected to produce DM 3 billion form part of the budget package.

4. Earlier in the month Stoltenberg announced that, as a result of additional subsidies to farmers following EC agreements on agricultural prices and compensation for damage to crops in the wake of the Chernobyl accident, some DM 1 billion of expenditure in the 1986 Federal Budget will be blocked.

5. Unemployment dropped further to reach the lowest monthly level since late 1982; the number of vacancies increased by nearly 50%.

6. The Federal Constitutional Court ruled that the system of Länder equalisation payments was unreasonable; a new system must be introduced by 1988.

Detail

7. In the second week of June the Federal Statistical Office announced that in the first three months of 1986 real GNP had grown by only 1.6% on a year earlier and fallen by 1% on Q4 1985. Seasonally adjusted the statistics leave room for a wide margin of speculation as to the causes of lower growth and the underlying structure of the decline therefore remains unclear. With the exception of private consumption, all other components of demand were weak but as yet there is no evidence either to identify the particular component or components responsible for the decline or to point to a trend.