

UNCLASSIFIED  
SAVING TELEGRAM

BY BAG  
FROM BONN

FRAME ECONOMIC

TO PCO TELNO 10 SAVING OF 31 JULY 1986. Info all EC Posts,  
UKDel OECD, UKMis Geneva, all Consulates-General  
in the Federal Republic, Washington, Tokyo, Vienna.

FEDERAL GERMAN ECONOMY

Summary

1. The West German economy is on the move again. But no agreement amongst economic experts on the size and shape of growth this year.
2. Current account surplus reaches a new record high level. Renewed appeals from abroad for reflationary policies are resisted by the Government who point to evidence which suggests the beginning of a slowdown in German exports.
3. Unemployment down again in June and now stands at 8.4%.
4. The Bundesbank left its key interest rates unchanged as well as its Central Bank monetary target for the rest of 1986.

Detail

5. Following the frisson caused by the poor outturn in the first four months of the year, the economy is now picking up again. New orders, production and private consumption have all recorded improvements. The latest IFO test on the business climate reinforces this mood as well as confirming a more confident outlook for the next six months. However, a round of summer forecasts proved that there is no consensus among the leading economic institutes about the speed of economic growth this year nor indeed about the relative strengths of the components of demand.
6. On 10 July the Council of Economic Advisers (the Five Wise Men) met Chancellor Kohl, Stoltenberg, Bangemann and Pöhl, the President of the Bundesbank, for an informal discussion about the

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economy. The Five Wise Men said that they estimated real GNP growth this year would be around 3% and thus unchanged on their November forecast. They noted however that the relative weighting of the components of demand had changed. Their original forecast had predicted export growth of 4.5% (real) which they have now revised downwards to 1.5% - 2.5%. At the same time, private consumption has been revised upwards from 3% to 4% - 4.5%.

7. Four of the five main economic institutes have also undertaken individual revisions of their unanimous, collective Spring forecast of 3.5% real GNP growth (Bonn telno 5 Saving of 29 April). All agree that the events which led to a downturn in the first four months of the year were due to special, short term factors: poor winter weather and its adverse effect on the construction sector, doubts about the future development of the US dollar and oil prices, and the lower than usual number of days worked. All are also agreed that the conditions exist for increased growth in the second half of 1986: wages and income taxes have been cut; mineral oil price falls have produced an added bonus to real wages; monetary policy is less restrictive; interest rates are low and inflation is negative. But here the consensus ends.

8. Of the four institutes who have published summer forecasts (Kiel, IFO (Munich), Berlin and Hamburg), three have revised their forecast downwards from 3.5% to 2.5% - 3% real GNP growth. The components of demand affected by the downward revision are private consumption (down from 4.5% to 4%), investment in machinery and equipment (down from 8% to 7.5%) and exports (down from 3% to 2.5%). The exception to this downward reappraisal is the Kiel Institute which sticks to the original forecast of 3.5% real GNP growth this year and predicts even stronger growth (4%) in 1987. Kiel's optimism is based upon the evidence that the fundamental factors exist for a strong pick-up in domestic demand led particularly by private consumption and investment.