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FRG ECONOMY: MARCH REPORT

SUMMARY

1. SPECULATION ABOUT A GOVERNMENT RESHUFFLE HAS PUSHED ECONOMIC ISSUES INTO THE BACKGROUND. BUT PRESSURES ON PUBLIC SPENDING AND FOR TAX REFORM REMAIN. INFLATION GIVING CAUSE FOR CONCERN.
2. REPORTS FROM INDUSTRY INDICATE CONTINUING STRONG ECONOMIC ACTIVITY, PARTICULARLY INVESTMENT. INDICATORS OF FOREIGN DEMAND REMAIN HEALTHY. LESS OPTIMISM FOR PRIVATE CONSUMPTION.
3. MONETARY GROWTH (M3) REMAINS STRONG. PRESSURES ON INTEREST RATES HAVE EASED.

DETAIL

4. ECONOMIC ISSUES HAVE TEMPORARILY RETREATED TO THE BACKGROUND OF THE POLITICAL DEBATE BUT FISCAL POLICY AND PUBLIC EXPENDITURE REMAIN CONTENTIOUS ISSUES. A REPORT BY ONE FISCAL INSTITUTE HIGHLIGHTED THE SIZE OF FEDERAL BORROWING, PARTICULARLY THE COST OF DEBT SERVICING WHICH THE INSTITUTE ESTIMATED AT 11.9 PER CENT OF THE 1988 FEDERAL BUDGET. SUCH CONCERNS MAKE VERY DIFFICULT CURRENT NEGOTIATIONS OVER THE 1990 BUDGET AND DECISIONS ABOUT ADDITIONAL SPENDING ON HOUSING AND IN OTHER AREAS OF SOCIAL CARE. IN ADDITION, THE DEBATE ABOUT THE REFORM OF CORPORATE TAXATION IN THE 1990S CONTINUES TO SIMMER. THE FEDERAL ECONOMICS MINISTER, HAUSSMANN, HAS NAILED HIS COLOURS TO THE MAST OF THOSE WHO WOULD LIKE TO SEE SUCH A REFORM SELF-FINANCING.

PRICES

5. INFLATION CONTINUES TO BE A SOURCE OF CONCERN FOR THE AUTHORITIES. PROVISIONAL MARCH COST OF LIVING FIGURES INDICATE AN INCREASE OF 2.7 PER CENT - 0.2 PER CENT MONTH ON MONTH - THE HIGHEST SINCE JUNE 1984. THIS FOLLOWS 2.6 PER CENT IN JANUARY AND FEBRUARY. IMPORT PRICES IN FEBRUARY WERE 5.9 PER CENT HIGHER THAN A YEAR

EARLIER - 0.3 PER CENT MONTH ON MONTH - WHILE EXPORT PRICES ROSE BY 4.2 PER CENT. A LEADING ESSEN-BASED ECONOMIC INSTITUTE FORECAST 3 PER CENT INFLATION ON AVERAGE THIS YEAR, BLAMING THE INCREASE ON HIGHER CONSUMER TAXES AND HIGH CAPACITY UTILISATION IN INDUSTRY.

ECONOMIC ACTIVITY

6. ECONOMIC ACTIVITY APPEARS TO HAVE REMAINED STRONG. THE CONSTRUCTION ASSOCIATION REPORTED THAT SO FAR THIS YEAR THE NUMBER OF BUILDING PERMITS IN THE RESIDENTIAL SECTOR IS UP 25.4 PER CENT AND 17.5 PER CENT IN THE NON-RESIDENTIAL SECTOR. THE VOLUME OF CONSTRUCTION ORDERS AT THE END OF LAST YEAR WAS DM 6.5 BILLION, 5.6 PER CENT HIGHER THAN A YEAR EARLIER. NEW ORDERS FOR MACHINERY AND CAPITAL EQUIPMENT IN FEBRUARY ROSE BY 10 PER CENT IN REAL TERMS, WITH DOMESTIC DEMAND INCREASING BY 11 PER CENT AND FOREIGN ORDERS RISING BY 9 PER CENT. THE AUTOMOBILE INDUSTRY REPORTED THAT CAR AND COMMERCIAL VEHICLE OUTPUT WAS 4 PER CENT HIGHER IN FEBRUARY AND THAT AUTOMOBILE EXPORTS INCREASED BY 7 PER CENT. THE REGULAR BUSINESS CLIMATE SURVEY CONDUCTED BY THE MUNICH-BASED IFO INSTITUTE SHOWED THAT IN FEBRUARY THE INDEX ROSE AGAIN TO 114 FROM 113.6 IN JANUARY. FIRMS INDICATED THAT PRODUCTION WOULD EXPAND OVER THE NEXT THREE MONTHS.

7. IN ITS MARCH MONTHLY REPORT, THE BUNDESBANK COMMENTED THAT THE HIGH LEVEL OF INVESTMENT ACTIVITY IN INDUSTRY, WHICH ACCOUNTED FOR MUCH OF THE INCREASED GROWTH LAST YEAR, APPEARS TO HAVE CONTINUED INTO 1989. BUT WHILE INDUSTRIAL ACTIVITY CONTINUES AT A HIGH LEVEL, INDICATORS FOR PRIVATE CONSUMPTION ARE NOT GOOD. RETAIL TURNOVER IN JANUARY REACHED DM 40.3 BILLION, A RISE IN REAL TERMS OF 4.2 PER CENT. HOWEVER, WHEN ADJUSTMENT IS MADE FOR WORKING DAYS THE INCREASE WAS ONLY 1.8 PER CENT. THE CONSUMER CLIMATE INDEX FOR JANUARY ROSE BY ONLY 0.7 PER CENT.

MONEY AND EQUITY MARKETS

8. THE BUNDESBANK REPORTED THAT MONETARY GROWTH CONTINUED STRONGLY BOOSTED BY INCREASED PRIVATE SECTOR CREDIT. M3 CLIMBED IN FEBRUARY BY 7.3 PER CENT. PRESSURES ON INTEREST RATES EASED AS THE BUNDESBANK CONTINUED TO SUPPLY THE MONEY MARKETS WITH FUNDS AT A FIXED INTEREST RATE OF 5.8 PER CENT. LONG AND SHORT-TERM INTEREST RATES FELL AS A RESULT. YIELDS ON BONDS OUTSTANDING FELL BACK BELOW 7 PER CENT AS DID THREE MONTH FIBOR WHILE CALL MONEY ENDED THE MONTH BELOW 4.5 PER CENT. ON THE FRANKFURT FOREIGN EXCHANGE, ATTENTION FOCUSSED ON THE US DOLLAR, WHICH BRIEFLY CLIMBED ABOVE DM 1.90, AND STERLING WHICH DESPITE A WEAK MID-MONTH RALLY, CONTINUED TO DEPRECIATE AGAINST THE D-MARK. DESPITE SOME MID-MONTH NERVOUSNESS, THERE WAS

LITTLE EXCITEMENT ON GERMAN STOCK EXCHANGES. ALL THE MAJOR INDICATORS HOVERED AROUND OR JUST BELOW AVERAGE LEVELS FOR THE YEAR. COMPANY RESULTS NOW BEING ANNOUNCED SHOW GENERALLY INCREASED PROFITS ACROSS ALL MAJOR SECTORS, PARTICULARLY BANKING.

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