

UNCLASSIFIED
SAVING TELEGRAM

FROM BONN
FRAME ECONOMIC

TO FCO TELNO 12 SAVING OF 17 NOVEMBER 1988. Info. Brussels, Luxembourg, The Hague, Paris, Rome, UKRep Brussels, UKDEL OECD, UKMis Geneva, all Consulates-General in the Federal Republic and West Berlin, Washington, Tokyo, Vienna.

FRG ECONOMY

SUMMARY

1. Broad based growth continues. Federal Finance Minister forecast nominal GNP growth of 5.3% this year and 4.2% in 1989. Consensus of most other analysts is for 3% real growth this year falling to 1.5% to 2% in 1989. Unemployment expected to rise slightly next year. (Para. 9)

2. 1989 budget approved in the Committee stage in Parliament allowing a 5.4% increase in expenditure to DM 290.3bn. Final reading in the lower house later this month and in the upper house on 16 December. Tax revenue estimates for this year and next year revised upwards to DM 488.1bn and DM 512.7bn respectively. But confusion remains about tax increases and the introduction of new taxes next year. (Paras. 10 to 12)

3. Unemployment in October fell by 25,000 to 2.07 million (8%). Employment in September rose to 26.44 million. Seasonally adjusted unemployment has now fallen for four consecutive months. (Para. 13)

4. Business climate now reported to be higher than at any time since 1973. Manufacturing sector reports demand outpacing production. Capacity utilisation for the quarter ending September estimated at 87.4%. New orders rose by 4% in August/September on a two month comparison, with foreign orders alone up 5.5%. On the same basis, production grew by 3.5% and construction sector output rose by 2.5%. (Paras. 14 to 17)

5. Private consumption remains buoyant with retail trade turnover up 5.4% in real terms in September. Inflation, cost of living index, slowed to 1.3% in October but the moving annual average edged up to 1.1%. (Paras. 18 to 20)

6. Stronger activity on German stock markets. In Frankfurt the Commerzbank index reached the year's high point of 1641.6 before falling back in the wake of the US elections. Capital outflows appear to have been reversed. On the money markets, short term interest rates moved higher as the Bundesbank adjusted its monetary policy. Long term interest rates eased to 6.1%. The money supply expanded strongly once again in September with M3 growing by 6.6%. (Paras. 21 to 24)

7. The D-Mark continued to fall against the Yen having fallen some 9% since the end of 1987. Against the dollar the D-Mark has continued to appreciate. Pressures have eased within the EMS.
(Para. 25)

8. The visible trade surplus in September climbed to DM 11.3bn and the current account surplus to DM 6.1bn. Imports from the UK in the 12 months to June, the latest month for which details are available, reached DM 29.4bn, and the trade surplus in favour of the FRG rose to DM 19.5bn. (Paras. 26 to 28)

DETAIL

THE ECONOMY

9. The strength of the economy continues to be a source of satisfaction to the Government. In its October monthly report, the Federal Economics Ministry stressed the broad base of the domestic recovery with higher demand, production, orders and investment all contributing to industrial confidence. The Federal Finance Minister later revealed that he expected nominal growth of GNP of 5.3% (almost 3% real) to DM 2.127bn this year and 4.2% (around 2% real) to DM 2.217bn in 1989. The Dresdner Bank in its latest report forecast real GNP growth of 3.5% this year, based on continuing strong private consumption (3%), the return of high fixed capital investment (6.5%) and modest inflation. The bank noted that this strength was likely to continue into next year though at a lower level: real GNP growth of 2%; private consumption to rise by 2%; and capital investment to grow by 3.5%. This view was supported by the Commerzbank which in its October report forecast 3% real GNP growth this year and 1.5% to 2% in 1989. For the economic institutes, the DIW in Berlin confirmed the strong recovery and stressed that it was due as much to domestic consumption as to foreign demand. The trades union-funded WSI institute also forecast 3% real growth in GNP this year falling to 1.5% in 1989. But the bullish mood does not extend to the labour market with all sources echoing the WSI's prediction that, while numbers in employment will continue to grow, unemployment will average around 2.25 million (8.1%) this year and rise to 2.28 million (9.1%) next year.

1989 BUDGET

10. The Budget Committee of the Bundestag passed the draft 1989 budget on 10 November. The draft allows a 5.4% increase in expenditure to DM 290.3bn. The main change made by the Committee to the draft put forward by the Government was an increase of DM 839 million in allocations for capital investment which now total DM 37.4bn. The draft foresees tax revenue of DM 240.3bn and Bundesbank profits of DM 5bn. With only one privatisation planned - the Bonn-based DSL Bank - privatisation proceeds will amount to only DM 300 million, of which DM 100 million will have been spent to increase the bank's capital. The Federal budget deficit is planned to be DM 27.9bn. The draft will now go forward for the final readings in the Bundestag on 22 to 24 November and to the upper house, the Bundesrat, on 16 December.