

RESTRICTED

FM BONN

TO PRIORITY FCO

TELNO 168

OF 121003Z FEBRUARY 90

INFO SAVING CGS IN THE FRG AND BERLIN, BMG BERLIN, EAST BERLIN

FRAME ECONOMIC

FRG ECONOMY 

SUMMARY

1. A CONFIDENT START TO THE YEAR, THOUGH SOME CONCERN ON THE LABOUR FRONT AND RESIDUAL WORRIES ABOUT INFLATION. A DEBATE HAS BEGUN ABOUT THE EXPECTED COSTS, BOTH SOCIAL AND FINANCIAL, OF ECONOMIC AND MONETARY UNION WITH THE GDR.

DETAIL

2. REAL GNP GROWTH OF 4 PER CENT LAST YEAR HAS SET THE TONE FOR 1990. THE GOVERNMENT'S ANNUAL ECONOMIC REPORT, RELEASED ON 22 JANUARY, FORECAST GROWTH THIS YEAR OF 3 PER CENT. ALTHOUGH EXPORTS ARE EXPECTED TO EASE BACK, INVESTMENT WILL REMAIN LIVELY AND THE JANUARY CUTS IN INCOME TAX SHOULD STIMULATE PRIVATE CONSUMPTION. IMPORTS WILL ALSO INCREASE, THOUGH NOT ENOUGH TO REDUCE THE TRADE SURPLUS MUCH. IT SEEMS LIKELY TO HAVE REACHED DM135 BILLION LAST YEAR.

3. EVENTS IN THE GDR ARE NOW DOMINATING THE ECONOMIC AGENDA. POLICY HAS BEEN ACCELERATED BY THE CONTINUING STREAM OF RESETTLERS (OVER 60,000 FROM THE GDR ALONE SINCE 1 JANUARY) PLUS WARNINGS OF THE IMMINENT ECONOMIC COLLAPSE OF THE GDR. THE DEBATE IS NOW OVER HOW AND WHEN MONETARY UNION WILL HAPPEN. FEW DOUBT THE LONG-TERM ECONOMIC BENEFITS OF UNION FOR THE FRG AS WELL AS FOR THE GDR. BUT THE IMMEDIATE PRICE WOULD BE HIGH FOR BOTH, AND MUCH WOULD DEPEND ON TIMING AND THE SPEED OF ACCOMPANYING ECONOMIC REFORM.

4. INFLATION - 2.8 PER CENT LAST YEAR AND 2.6 PER CENT IN JANUARY - WAS ALREADY A PREOCCUPATION EVEN WITHOUT THE PROSPECT OF MONETARY UNION WITH THE GDR. MONETARY POLICY IS STILL TIGHT, WITH INTEREST RATES AT 6 PER CENT, THE HIGHEST SINCE THE EARLY 1980S. THE BUNDESBANK WILL NO DOUBT REMAIN CAUTIOUS UNTIL THE SITUATION ON MONETARY UNION AND THE TRENDS IN THE CURRENT WAGE ROUND BECOME CLEAR. TRADES UNIONS, INCLUDING THE POWERFUL METALWORKERS, ARE NEGOTIATING CLAIMS OF 8.5 PER CENT OR MORE, COMBINED WITH FURTHER

MOVES TOWARDS A 35 HOUR WORKING WEEK.

5. THE EFFECTS OF EVENTS IN THE GDR ARE BEING FELT IN INCREASED SOCIAL SPENDING, A TIGHT HOUSING MARKET AND HIGHER UNEMPLOYMENT. ALTHOUGH RESETTLERS DO NOT FEATURE ON THE REGISTER FOR THE FIRST TWO MONTHS OF THEIR STAY, UNEMPLOYMENT HAS RISEN STEADILY SINCE NOVEMBER AND NOW STANDS ABOVE 2 MILLION AGAIN. THE FEDERAL FINANCE MINISTER HAS PUT FORWARD A SUPPLEMENTARY BUDGET OF SOME DM 6.9 BILLION NET WHICH WILL BE PAID FOR BY ADDITIONAL BORROWING. LITTLE OF THE MONEY - SOME DM 860 MILLION - IS SPECIFICALLY EARMARKED FOR ASSISTANCE MEASURES WITHIN THE GDR. MOST IS TO FUND THE EFFECTS OF RESETTLEMENT IN THE FRG. THE SPD HAVE ALREADY PICKED UP THIS POINT.

COMMENT

6. THE STRENGTH OF THE FRG ECONOMY REMAINS BEYOND DOUBT. CONFIDENCE HAS NOT BEEN DENTED BY THE UNCERTAINTIES SURROUNDING DEVELOPMENTS IN THE GDR, BUT A DEBATE HAS BEGUN ABOUT THE ULTIMATE COST OF UNITY. THE OFFER OF TALKS ON MONETARY UNION WITH THE GDR IS INTENDED TO BUILD CONFIDENCE THERE AND HENCE RESTRAIN EMIGRATION. BUT THE CONSEQUENCES OF MONETARY UNION, ASSUMING IT COMES ABOUT, COULD BE DIFFICULT FOR BOTH SIDES. WHILE THE BUNDESBANK ACQUIESCED IN THE DECISION TO OFFER THE GDR MONETARY UNION, POEHL HAS POINTED OUT THAT MUCH WORK REMAINS TO BE DONE BEFORE IT CAN BE EFFECTED. CHALLENGED IN A TV INTERVIEW ON THE COSTS INVOLVED, HE SAID THAT GERMANY SHOULD BE PREPARED TO PAY THE PRICE OF UNITY.

NEVILLE-JONES

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ADDITIONAL 1

FRAME

SAVING 1

EAST BERLIN

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