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PP CANBE
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FM FCO
TO PRIORITY WASHINGTON
TELNO 2210
OF 191500Z DECEMBER 86

AND TO PRIORITY CANBERRA, VIENNA, BRUSSELS, OTTAWA, COPENHAGEN
AND TO PRIORITY HELSINKI, PARIS, BONN, ATHENS, REYKJAVIK, DUBLIN
AND TO PRIORITY ROME, TOKYO, LUXEMBOURG, AMSTERDAM, WELLINGTON
AND TO PRIORITY OSLO, LISBON, MADRID, STOCKHOLM, BERNE, ANKARA
AND TO PRIORITY BIS NEW YORK, UKDEL OECD
AND TO PRIORITY UKMIS GENEVA, UKREP BRUSSELS

OECD ECONOMIC OUTLOOK

1. THE LATEST EDITION OF THE SIX-MONTHLY OECD ECONOMIC OUTLOOK WAS PUBLISHED ON 18 DECEMBER. THE GENERAL THRUST OF THE REPORT IS THAT COUNTRIES SHOULD PROMOTE THE CORRECTION OF INTERNATIONAL IMBALANCES WHILE MAINTAINING LOW INFLATION AND STRENGTHENING OUTPUT AND EMPLOYMENT GROWTH. SPECIFIC RECOMMENDATIONS INCLUDE
(A) A LARGE AND SUSTAINED REDUCTION IN THE US BUDGET DEFICIT
(B) DOMESTIC DEMAND IN JAPAN TO GROW FASTER THAN PRODUCTIVE POTENTIAL
(C) INCREASED EFFORTS TO REDUCE STRUCTURAL RIGIDITIES IN EUROPE.
2. THE REPORT'S MORE PESSIMISTIC FORECASTS ON UK ECONOMIC

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PERFORMANCE, AND ITS CLAIM TO SEE A SHIFT TOWARDS EXPANSION IN UK FISCAL AND MONETARY POLICY, HAVE BEEN PROMINENTLY REPORTED BY TODAY'S (19 DECEMBER) UK PRESS: THE FINANCIAL TIMES HIGHLIGHTS THE OECD MEDIUM-TERM FORECAST OF A WORSENING UK TRADE POSITION AND STEADILY RISING INFLATION.

LINE TO TAKE

3. THE OECD ASSESSMENT SUPPORTS OUR VIEW THAT SUSTAINABLE WORLD GROWTH OF AROUND 3 PER CENT SHOULD BE ACHIEVED IN 1987 WITHOUT INFLATION PICKING UP FROM PRESENT LOW LEVEL. WE AGREE WITH THE OECD'S SPECIFIC RECOMMENDATIONS ON THE WORLD ECONOMY, AND WE WELCOME CONTINUED OECD SUPPORT FOR PRUDENT FISCAL AND MONETARY POLICIES, AND FOR EFFORTS TO REDUCE STRUCTURAL RIGIDITIES. ADDITIONAL POINTS ON UK ECONOMY (IF ASKED) -

4. OECD FORECASTS CORRECT OF CURRENT ACCOUNT DEFICIT OF POUNDS 3 AND HALF BILLION FOR 1987, POUNDS 3 BILLION FOR FIRST HALF OF 1988?

DIFFERING FORECASTS ARE THE RESULT OF DIFFERING VIEWS ON TERMS OF TRADE. BUT OECD FORECAST FOR 1987 CLOSE TO INDUSTRY ACT FORECAST FOR INVISIBLES AND FOR IMPORT AND EXPORT VOLUME GROWTH.

5. INFLATION ACCELERATING?

MAY RISE IN MIDDLE OF NEXT YEAR BUT WILL ASSUME DOWNWARD PATH TOWARDS END OF 1987. UNDERLYING INFLATION (EXCLUDING MORTGAGE INTEREST COMPONENT) UNLIKELY TO BE VERY DIFFERENT IN 1987 Q4 FROM WHAT IT IS NOW.

6. CHANGE IN EMPHASIS IN MONETARY POLICY?

NO CHANGE IN VIEW THAT MONETARY POLICY IS KEY TO CONTROLLING INFLATION AND THAT INTEREST RATES ARE THE ESSENTIAL INSTRUMENT OF THAT POLICY. SOME CHANGE IN BEGIN UNDERLINING IMPLEMENTATION CEASE UNDERLINING OF POLICY OVER TIME.

7. OVERALL STANCE OF FISCAL POLICY EASING?

NO. CHANCELLOR HAS REAFFIRMED THAT PSBR FOR 1987-88 WILL BE HELD TO ONE AND THREE QUARTERS PER CENT GDP AS IN 1986 MEDIUM TERM FINANCIAL STRATEGY, DESPITE IMPACT OF OIL PRICE FALL ON NORTH SEA REVENUE.

8. STATUS OF REPORT?

OECD AN INDEPENDENT BODY, CARRYING OUT ITS OWN FORECASTS AND

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ANALYSIS.

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