

24/10/66

AN ADDRESS BY PAUL VAN DEN BEMPT, HEAD OF THE DIVISION FOR ECONOMIC TRENDS, DIRECTORATE GENERAL FOR ECONOMIC AND FINANCIAL AFFAIRS, COMMISSION OF THE EUROPEAN ECONOMIC COMMUNITY, BEFORE THE LUNCHEON MEETING CO-SPONSORED BY THE CENTRAL NATIONAL BANK OF CLEVELAND AND THE CLEVELAND COUNCIL ON WORLD AFFAIRS AT THE STATLER-HILTON HOTEL, NOON, THURSDAY, OCTOBER 20, 1966

I thought it would be useful for you to be informed about the Commission's most recent views on the short-term and medium-term economic development in the EEC, a market which, as we know, is the first importer in the free world.

During the first five years of this decade the EEC has known a strong and uninterrupted expansion. Its gross domestic product increased, in real terms, by almost 5% per annum. This strong expansion, given the fact that full employment had been attained in all member countries in 1960, has, however, made it very difficult to maintain internal balances, so that the six member countries were submitted to heavy inflationary pressures; and their governments were obliged to take steps to curb the expansion of overall demand.

Such steps were taken in Italy and France by the end of 1963 and the beginning of 1964, and produced satisfactory results during 1964 and 1965, although they inevitably led to some slowing-down of economic activity. Germany and the Benelux Countries, although they had taken anti-inflationary measures in 1964, following a recommendation addressed to all member countries by the Council of Ministers of the EEC, found themselves in 1965 in a similar though perhaps not so critical position as France and Italy had been at the end of 1963. As a result, restrictive policies had to be applied in these countries, too. Therefore, economic expansion also tended to slow down in this area as from the second half of 1965 onward, whereas in France and Italy, after a short pause in 1964, expansion was resumed at a rapid pace. Thanks to this upturn in several member countries and because restrictive measures were effected so as to moderate demand to a degree which did not exceed the requirement necessary for a return of

relative price stability, the economic expansion of the Community has, on the whole, remained appreciable after having increased by almost 6% in 1964. The gross domestic product of the Community still expanded by 4% in real terms in 1965, and according to our latest estimates the rate of increase will have risen to 4.5% in 1966.

How do prospects for next year look? Let me point out immediately that, according to our present news, there will be no marked slowing-down of economic expansion in 1967 in the Community as a whole. Gross domestic product is expected to increase by 4.5%, the same ratio as in 1966. Our forecasts with regard to our own exports necessitate, of course, an appraisal of world economic activity and trade. In this respect, we are certainly not pessimistic although it seems probable that our exports to other industrial countries will slow down in 1967, after an exceptionally rapid increase in 1966 (our exports to the U.S.A., e.g., will have increased by almost 20% in 1966). Indeed, the anti-inflationary measures taken in the U.K. in July are likely to reduce the expansion of our exports to this country and perhaps to cause a temporary decline. We expect also that anti-inflationary action undertaken and possibly to be undertaken in the U.S.A. and Canada will slow down the growth of our foreign sales to North America. Some other industrialized countries may be affected by these trends, and consequently take measures to curb the growth of their internal demand thereby limiting considerably the flow of their imports from the EEC. As a favorable factor we may mention that the evolution of world market prices for the major raw materials, the probable growth of imports of these raw materials by industrialized countries from developing countries, as well as the reserve position of the latter countries supports the view that the buying of manufactures by these countries will be a dynamic element in world trade in 1967.

On the whole on account of a slower development of sales, exports by the Community to the rest of the world may, therefore, slow down in 1967 but we do not expect that this movement will have a marked effect on economic activity within the Community. To this must be added the expectation that internal demand will also expand appreciably in the Community in 1967. We expect, indeed, that on a year to year basis its expansion will still accelerate in France and Italy where consumption and investment demands will be particularly strong. It should be more or less the same as last year in West Germany and perhaps somewhat slower in Belgium and the Netherlands. As a result of this, it would be obvious to conclude that EEC merchandise imports (excluding trade among member countries) should increase at almost the same rate as in 1966, when, according to present estimates they might rise by some 8 to 9%. However, due to the fact that following the decline in world market prices of some raw materials, the inventory building of these materials tends to slow down markedly and it is, therefore, expected that in 1967 imports of these raw materials will be at a relatively low level. Consumer and investment goods will, however, remain in high demand, following mainly the strong expansion of economic activity in Italy and France and progress to be observed among other member countries. Given the already described evolution of exports, the trade balance of the EEC should not change very much compared to 1966, though a slight improvement seems probable.

What are the Community's forecasts with regard to a longer term period? We find certain indications on the subject in the draft of the first medium-term economic policy program which contains projections of the economic development in EEC countries during the years 1966-1970. It is important to explain, first of all, that these projections are not of the same character as the short-term forecasts. The latter attempt to describe the most probable evolution of the EEC economy, given certain economic policy decisions. The former are above all an

explanation of growth possibilities of the EEC economies under the proviso that these growth possibilities will only be realized if economic resources are adequately used, and if appropriate policies designed to keep the economy in balance are followed.

The medium-term economic projections are, therefore, much more conditional than short-term ones. Despite these unavoidable drawbacks it is interesting to have some indications on how the Community could develop in the next five years if appropriate policies were followed.

It is shown, in the first place, by these projections that some reduction of the growth of the Community's gross domestic product cannot be avoided; and that for the years 1966-1970 an average increase in real terms of 4.3% is foreseen compared with an annual average increase of 4.9% between 1960 and 1965. This slowing down is mainly the consequence of developments in West Germany, where it is expected that the total labor force will decline substantially between 1966 and 1970, despite reinforced immigration efforts. This is seen clearly in the following table comparing growth rates country by country:

RATES OF GROWTH OF GROSS DOMESTIC PRODUCT

	<u>1960/1965</u>	<u>1966/1970</u>
West Germany . . . . .	5.1	3.5
France . . . . .	4.8	4.3
Italy . . . . .	5.1	5.0
Netherlands . . . . .	4.7	4.6
Belgium . . . . .	4.5	4.1
Luxembourg . . . . .	2.9	3.2

In order to achieve these rates of growth it will be necessary to realize a substantial increase in productivity, since the increase in the labor force appears to be slower than during the period 1960-1965 (and this last point is probably the most certain part of these projections). Therefore, all countries will have to maintain a high rate of investment in plant and equipment. Residential construction, on the other hand, is not likely to grow as rapidly as between 1960 and 1965, when substantial backlogs due to the rapid population increase

combined with the replacement of houses destroyed during the War existed in several countries. According to the views expressed by government experts and incorporated in the projections, public investment should increase at a rate almost double of that of total gross domestic product. This very rapid progression appears to be necessary if the ever-increasing collective requirements (roads, schools, etc.) are to be met, and also a substantial backlog incurred in this field is to be eliminated. These projections show that a very heavy pressure on resources by public and private investment is to be expected in years to come. If the EEC economies are to be kept in balance this would mean that private consumption could not increase in real terms by more than 4.1%, a substantial rise but a less rapid one than during the years 1960-1965 when it was, on the average, 5.3%.

This is precisely the crucial point in the projections. If consumer demand increased in fact more quickly -- and given conditions of full employment -- we have every reason to believe that it will grow at a very substantial rate. Then either the share of investment in total expenditures would have to decline and this would certainly be detrimental to our longer term growth, or the increase of monetary demand would substantially exceed the increase in domestic production causing price increases and balance of payments deficits. A very important task rests, therefore, on those responsible for economic policies in the short-term in the Community if these projections in the longer term are to be realized.

At any rate, it appears that in all probability and barring extraordinary political events which would affect the world economy, during the period 1966-1970 EEC imports, particularly of manufactures, will increase at a rate not much less than that obtained during the period 1960-1965 when it amounted in volume to some 10% per annum for all imports from third countries. Higher figures would be obtained, of course, if inflationary pressures were stronger than what we expect, but we hope that this will not be the case and that our economic policies will be efficient.

I may perhaps summarize and conclude this talk by saying that for the immediate future, and particularly the year 1967, prospects with regard to the development of economic activity of the Community and its imports from third countries look more than satisfactory, and that in the longer term, given appropriate short-term economic policies, a steady and firm improvement of its import demand may be expected.

10/20/66