'Sick Men' Of Europe Revived But Not Cured

During the past two months, the economies of Britain, Italy, and France — widely known as the "sick men" of Western Europe — have shown a significant *short-term* improvement, indicated by the surprising stability of their respective currencies. Although most U.S. financial press commentators have attributed this development to the alleged success of domestic austerity programs (e.g., the "Barre Plan" in France), the actual determining factor has been political rapprochement with the Arab oil-producing nations and, to a lesser extent, with the Soviet sector.

The immediate fruit of this European-Arab dialogue have been substantial OPEC investment in all three European economies, (including, in the case of Britain, the informal commitment of the Saudis and other OPEC investors to assist in stabilizing the troublesome sterling balances), and a sudden flood of oil-for-technology trade arrangements. This has coincided with a major shift in government economic recovery strategies, not only of Britain, Italy, and France but of West Germany as well, with primary emphasis now being placed on the opening of new markets for high-technology European industry in the Middle East oil-producing, Soviet, and Third World sectors. Accordingly, government exports credits guarantee policies have been upgraded and expanded, including a 37 percent hike in credits available for the British program and a 100 percent increase for West Germany's Hermes export credit program announced during January.

Although this shift in European government strategies has given a temporary boost to business confidence, the lack of an adequate *international* credit mechanism with which to finance large-scale North-South and East-West projects, means that the European upswing will soon run up against its inherent limits. European-Arab rapprochement has brought Western Europe a breathing space, but not economic recovery.

Italy, the country which has recently been in the forefront of European efforts to transform East-West credit practices, including a proposal for European-wide discounting of the Comecon transfer ruble, has just suffered a major setback in its Soviet trade. A number of Italian companies have complained that they are losing several hundred million dollars' worth of Soviet orders due to prohibitive credit requirements imposed by the Italian government. Under heavy pressure from the International Monetary Fund to impose new austerity so as to qualify for bailout funds, the Andreotti government has reached a stalemate in its negotiations with the Soviets concerning an estimated $7 billion worth of prospective trade.

Similarly, Soviet officials last week notified the British government that one billion pounds in Soviet orders were available to British industry *dependent upon* the working out of appropriate financial arrangements.

In actuality, the Italian government's own "Ratti Plan", providing for European-wide pooling of reserves in an East-West Bank which would finance trade through the discounting of Soviet commercial paper, has all the ingredients of a solution to this dilemma. The only obstacles are *political* — most notably the opposition of the U.S. Carter Administration

The problems in the lack of such an international mechanism are most evident in the heavy industry-based, export-oriented economy of West Germany, Western Europe's industrial linchpin. The West German government has reported a 10.6 per cent plunge in the

Overall Industrial Production Indices

(1970=100)

	W.GERMANY	FRANCE	U.K.	ITALY
1973	113.2	120	110.2	114.5
1974	111.9	123	106.3	119.0
1975	105.0	112	101.0	108.5
1976				
JAN	103.8	125	101.0	110.5
FEB	113.0	128	101.9	120.7
MAR	110.1	129	101.7	121.9
APR	118.0	128	102.0	124.3
MAY	116.6	126	103.9	129.7
JUN	118.6	129	100.2	128.5
JUL	99.1	110	101.8	123.1
AUG	98.1	77	100.8	68.9
SEP	113.7	129	100.8	136.6
OCT	120.7	123	100.8	135.1
NOV	122.8	126	102.4	130.6
DEC	109.7		102.5	132.0

preliminary (unadjusted) industrial production index in December and a 14 per cent jump in January unemployment. The production and employment cuts occurred primarily in the deeply depressed steel and machinery industries — precisely those European sectors which have yet to benefit from trade deals in a major way. With a worldwide "glut" of steel emerging, an estimated 200,000 workers have been or are about to be placed on short-time or laid off throughout Europe.

Unemployment

(IN THOUSANDS AND IN % OF LABOR FORCE)

	W. GERMANY		FRANCE	U.K.		ITALY	
	TOTAL	%	TOTAL	TOTAL	%	TOTAL	%
1973	274	1.3	394	618.8	2.7	669	3.7
1974	583	2.6	494	614.9	2.6	560	2.9
1975	1,074	4.7	840	977.6	4.2	654	3.3
1976							
JAN	1,351	5.9	1,017	1,303.1	5.5	681	3.5
FEB	1,347	5.9	978	1,304.4	5.5		
MAR	1,190	5.2	938	1,284.9	5.5		
APR	1,094	4.8	897	1,281.1	5.4	693	3.5
MAY	954	4.2	848	1,271.8	5.4		
JUN	921	4.0	813	1,331.8	5.6		
JUL	945	4.1	809	1,463.5	6.2	776	3.8
AUG	940	4.1	842	1,502.0	6.4		
SEP	899	3.9	955	1,455.7	6.2		
OCT	944	4.1	1,025	1,377.1	5.8	777	4.0
NOV	985	4.3	1,041	N.A.	-		
DEC	1,090	4.8	1,037	1,371.0	-		
1977							
JAN	1,240						

A related problem is the fact that, in every country, industrialists are short of funds for necessary capital investment programs, at the same time that trade unions are demanding pay hikes to compenstate for two years of declining real incomes. In West Germany a modest 6.9 percent metalworkers' wage boost last week evoked a wave of protest from employers' associations and economic institutes, who labeled the increase a precedent-setting "threat" to the economy.

Throughout Europe, previous government-employer ability victories to limit wage increases has eaten heavily into retail sales, eliminating the possibility of any internally based recovery and threatening the decimation of the skilled labor. Given this predicament, the continuing failure of European governments to take swift action to revamp the world monetary system will undoubtedly lead to serious economic deteoriation and renewed currency turmoil during 1977.

Consumer Prices

(% CHANGE FROM PREVIOUS MONTH)

	BRD	FRANCE	UK	ITALY
JAN	+0.8	+1.1	+1.3	+1.2
FEB	+0.7	+0.7	+1.3	+2.2
MAR	+0.4	+1.0	+0.5	+2.0
APR	+0.6	+0.9	+1.9	+2.6
MAY	+0.4	+0.7	+1.1	+2.0
JUNE	+0.3	+0.4	+0.5	+0.5
JULY	-0.4	+1.0	+0.2	+0.6
AUG	+0.4	+0.7	+1.4	+0.9
SEP	+0.0	+1.1	+1.3	+1.8
OCT	+0.1	+0.9	+1.8	+2.9
NOV	+0.4	+0.8	+1.4	+2.2
DEC	+0.5	+0.3	+1.3	+1.2
1975-76 % CHANGE	+ 3.7	+9.8	+15.1	+ 22.0

Investment Squeeze Hurting Callaghan Industrial Strategy

BRITAIN

The recent inklings of an industrial recovery for Britain, largely the result of the Callaghan government's attempts to shape the political climate for industrial growth, is in danger of disintegrating before it has had a chance to fully take hold.

The reason is the lack of investment funds available to industry. The government's willingness to make short-term compromises over sterling and credit policies to meet the conditions of the IMF loan announced in December could mean the failure of its positive industrial strategy — without an immediate move toward long-term investment credits for industry as outlined in the Ratti Export-Import bank proposal for Europe.

Following Prime Minister Callaghan's decision to take