

Princeton Economic's The World Capital Market Review



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214 Carnegie Center, Princeton NJ 08540 609-987-9522 Annual Subscription US\$49.95

The New \$100 Bill Conspiracy or Honest Reform?

by **Martin Armstrong**

The new US \$100 bill is causing quite a stir not merely inside the United States but also around the world. Full scale currency panics are under way in a number of countries with particular significance in Russia where over \$20 billion of US currency circulates freely as part of the money supply.

Jumping on an international flight from the US these days brings this issue of a panic to light. The US Treasury has been launching a massive advertising campaign trying to reassure the world public that the old \$100 is still legal tender and will continue to be so in the future. Not mere do these advertisements appear on the movie screen of on international flights, but the Secretary of the Treasury has become a familiar face on Russian TV.

Exchanging old \$100 bills for the new version has become such a big business overseas that up to 5% is being charged by Banks just to swap the notes. Even the Russian government has jumped into the scam by imposing a tax on the exchange of the notes.

So what is going on? Is there a hidden agenda that the US government is not admitting to? Or is there a real reform going on to stamp out counterfeiting?

There is little doubt that the counterfeiting of US currency has reached huge proportions outside the US. While it is an issue that remains largely undiscussed, the truth of the matter is quite concerning. The largest counterfeiting ring is actually in Asia and this is a front for the Chinese military. The surprising aspect here is that the \$50 bill is not being replaced. The counterfeits of this note are excellent and are widely known in Asia as "Hong Kong Fifties." Stopping this type of counterfeiting is going to be impossible. The new \$100 note will at least make things more difficult for the counterfeiting rings but by no means will it come to an end.

International concerns have risen to such a height over the issue of cancellation largely because this is routine practices throughout Europe. Most European nations cancel their currency right down to large denomination coins about every 10 years. This is a tactic that is used largely for the purposes of taxation. Cancelling the currency once every 10 years forces the public to redeem their notes thus

thwarting the efforts of tax evaders who stockpile cash in their safety-deposit boxes. This, at least, does not appear to be the purpose of the Treasury at this time. Nonetheless, it is an option that they are very much aware of and can become reality perhaps by the turn of the century.

Domestic concerns are centered around the presence of a strip inside the paper that can be read by a scanner. With the proper equipment, it will be possible to determine how much cash someone has on his person. This, however, does not appear to be a major risk of privacy at this time. Nonetheless, it is a valid concern for the future when budget get tight and government is desperate for revenue. Part of the penalty for not declaring the amount of cash on your person at customs includes the government's right to confiscate the funds entirely. That does offer a big advantage over merely taxation.

The question of conspiracy seems to be the hot topic on talk shows around the nation. Is this a conspiracy to expand the powers of big government? The answer to this is perhaps. The more important issue is that government has been routinely starving the public from a money supply perspective. Even



\$5,000. F.R.N. Series 1934 Block K--A



during the 1930s, the Treasury issued \$500, \$1,000, \$5,000 and \$10,000 bills for general circulation. If you can imagine that an automobile sold for only \$600 at that time, a 1,000 bill was indeed a lot of money. You would think that given the massive level of inflation since World War II, \$1,000 bills should be part of the normal money supply today. The reason that large denominations are NOT in circulation is due solely to the government's policy of trying to starve the underground economy.

This starvation of cash on the part of government has nothing to do with the drug trade since the last \$1,000 bill issued was back in 1934. The real conspiracy here, if you must use that word, is the fact that government is attempting to allow inflation to naturally reduce the importance of cash within our society. The goal is clear. If the majority are forced into the electronic system of banking, then the government will be able to more

efficiently collect its share of revenue. Large denomination notes were withdrawn from circulation at the same time when the majority of citizens found themselves subject to income tax following World War II. This also coincided with the introduction of the payroll tax system. The issue is not so much scanning people at airports - it is a definitive

attempt by government to reduce the importance of cash within our economy to further enhance tax collection efforts.

In the final analysis, the introduction of the new \$100 bill may have something to do with counterfeiting. However, the risk is clear that at some point in the future the government could very well demonize the old \$100 note as we enter the century.



Mad Cows to Revolution

The PEI UK & Middle East Update

by: **Bruce Allen**
Executive Director
PEI UK & Middle East

Official figures released last month on the UK's balance of payments show the current account moving further into deficit last year. The 1995 figures was BP6.7 billion in the red, three times the size of the 1994 deficit, confirming the extent that UK exports of goods and services have been hit by declining European markets, particularly Germany. GDP grew by 2.5%, a downward revision of earlier estimates and investments, estimated as 2% growth actually fell by 0.5% in the fourth quarter as public sector investment was reduced sharply. Personal savings as a percentage of disposable income increased to the highest level since 1993 but in contrast companies recorded a financial deficit for the first time in three years largely due to higher dividend payments. Direct investment overseas by UK companies rose to a record high of BP24 billion in 1995. Direct investment by overseas companies into the UK also rose to a record level with a sharp increase in the 4th quarter reflecting overseas company takeovers of UK companies.

The "Mad Cow Disease" panic, (Bovine Spongiform Encephalitis) has vindicated those critics of the food rendering industry who have forecast such a crisis for many years. The impact on dairy and beef farmers, processors and equipment supplies will be quite severe at a time when this sector of farming was already seeing returns lowered by between 10% and 25%. However, the crops

sector of farming saw a 32% increase in income last year and higher cereal prices are likely to improve returns this year again. The governments handling of the crisis was rightly criticised severely but it also highlighted the increasing public opinion against EEC control of UK affairs following the beef and beef products export ban imposed by Brussels.

A new political grouping, the "Referendum Party", partly financed by the Anglo-French based financier Sir James Goldsmith, is gaining momentum in its attempt to contest every seat in the next UK general elections. Although pressure is mounting on Prime Minister Major to hold a referendum on the common European currency, the Referendum Party is tapping into the mounting feeling of fear that British sovereignty will be lost to faceless bureaucrats in Brussels and national self-determination will be a thing of the past.

Not only is public opinion in existing EEC countries challenging political ideals to understand the rationale for convergence of economies in Europe, countries waiting in the wings for admission such as Cyprus are pressing politicians harder for information on practical rather than emotional advantages. There is a growing awareness that a united European economy, even if it is possible, would benefit Germany and France more than the smaller economies. A central European finance authority is unlikely in their view to make their currency and industry more competitive against the needs of the major economies at a time when they foresee a reduction in EEC commitments to provide financial investment and subsidies.

Money for old "notes"

The redesigned \$100 banknote hit the streets of Russia last month with a \$1 million publicity campaign by the US government which has made a television start out of Mr. Robert Rubin in an effort to convince Russians you can still trust Uncle Sam. Russians are the largest foreign holders of US banknotes to the tune of some \$20 billion in circulation. While the minimum 2% replacement fee charged by Russian banks perhaps dampened enthusiasm for the new notes, the Russian state customs had no hesitation in cashing in. They announced a 0.1% levy on banks shipping the old notes out. The government already charges 0.15% of face value on all foreign currency imports.

Middle East

While the Israeli-Palestine problems continue to command attention, the instability of the Persian Gulf countries and their impact on the Kingdom of Saudi Arabia should not be overlooked. Oil was first discovered in the region on the Island of Bahrain in 1938 and whilst production of the onshore fields is not minimal, Bahrain draws heavily on revenues from a 50:50 sharing arrangement with Saudi Arabia from an offshore field situated on their mutual border. Like Saudi Arabia, the majority of Bahrainis are Shi'a Muslims including a smaller number of Iranian Shi'as who have lived in Bahrain for several generations but whose ties are more with Iran than the ruling Sunni minority.

A form of democracy existed after independence from Britain in 1971 until the National Assembly was dissolved in 1975. An armed rebellion was put down within hours in 1981 but the frustration of the majority has fermented and led to the beginning of the current agitation 18 months ago to reinstate a more democratic government. Riots in the last few months have met with a hardline response by police and military. The Saudi government's concern that a domino effect would increase their own problems is such that they have reportedly agreed to give Bahrain up to 100% of the shared oil field revenues in return for a continuing hard line response. The ruling Al Khalifa family in Bahrain appears to consider no alternative but to resist charge, a strategy that history would book long odds on success.

Elections In Israel

The next tinder box to keep an eye on will be the elections coming up in Israel during the last week of May. The opposition, if successful, intends to put the breaks on the land for peace process. Needless to say, these elections will become critical to market behaviour particularly around late May to early June when our Economic Confidence Model calls for a major change in the world capital markets.

The fact that this election in particular is lining up with our Economic Confidence Model is not a good sign for the peace process. There is definitely a risk that a serious directional change is coming in the Middle East.

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Chicken Kiev - Russian Style

by **Dana Schneider**
director of Russian
Studies, PEI

Most restaurants that endeavor to offer a taste of Russian dining will invariably include on their menus borscht, pirozhki, blini, beluga caviar, and chicken Kiev. Granted, Kiev is in the Ukraine but taking this dish off the Russian menu would mean many disappointed diners. Translate this into Russian politics and you end up with the outlandish Parliamentary vote by the communist majority on March 15th that declared the dissolution of the Soviet Union in 1991 to be unconstitutional and invalid. President Yeltsin condemned this resolution as scandalous while Georgia, Kazakhstan, and indeed the West, were quick to express their outrage at such a proposition. If the communist sweep of the December Parliamentary elections added uneasiness to the state of Russian affairs, the past six weeks have certainly given a sense of schizophrenia. The shifting financial market, the domestic presidential politicking, and the international posturing makes the coming presidential elections in June anyone's guess.

Russia Tells Clinton to Keep his Chicken in Arkansas

A recent dispute over US chicken exports underscores the influence that the revived communist party is affecting on foreign policy and reflects the creeping desire of the Russian people to slip into economic and political protectionism. A \$10 billion IMF loan was

recently secured by Russia to be paid out over three years. Certain economic objectives and trade stipulations were negotiated. However, Russia remains unwilling to disabuse herself from super power stature abroad or at home.

In early February, Russia announced that it would halt US chicken imports by mid-March under the guise of health safety and regulations. The choice of banning this commodity carried some political irritation since the largest US poultry producer is located in President Clinton's home state. In 1995, 85% of Russian poultry came from the US, constituted 20% of US poultry, and totaled approximately \$600 million. By early April, the issue had made a lot of noise but was basically waffled and moot. In the end, both countries are negotiating over tariffs while exports continue to be shipped. The nature and content of this trade dispute revealed two distinct political camps competing for influence in Russia. For Yeltsin, he accomplished two politically important tasks: publicizing the ability and duty of the President to pursue economic policies that heed the social and economic concerns of the people; cultivating an image of the necessity of Russia to be consulted in economic and political negotiations if her markets are to be accessed. For the Communist Party and their candidate Zyuganov, they achieved a domestic image of a strong, protectionist position against the devastating capitalist policies of the West.

NATO expansion is still a volatile issue and has gained even more prominence through presidential campaigning. Communist Party candidate Zyuganov has vowed to oppose any expansion. Yeltsin has taken to vehemently campaigning against it at home and abroad - most recently in Norway.

However, diplomatic liaisons have made signals that compromise on NATO is feasible if expansion is limited to political concerns and military guarantees without the hardware or troops. Again, what is being sounded out domestically and on the campaign trail is more closely related to domestic political posturing than any coherent foreign policy direction. Expect the months preceding the June elections to be marked by shifting and contradictory positions.

Don't Count Your Chickens Before They're Hatched

Russia's trade shenanigans and parliamentary votes have put world lending institutions on edge. Although Yeltsin parleyed the IMF loan as a sign of international support for his leadership, the opposition has also played the issue to the populist notion that Russia is selling out to the West. The IMF has warned that the loan may be suspended if the communist party candidate Zyuganov wins the June election and then pursues any contradictory policies. Similar to the preceding \$6.5 billion loan, the new loan contains several stipulations: monthly auditing for the first year, targets of 1.9% monthly retail inflation rate declining to 1% within a year, 3.85% of GDP budget deficit, removal of all export tariffs by April 1 with energy tariffs by July 1, 1996, and continued progress on financial legislation and monetary mechanisms. The first tranche of the \$10 billion IMF loan has been disbursed but Russia has yet to lift the export tariffs (\$4 billion will be delivered in the first year). Facing a revenue short-fall but committed to cutting energy tariffs as prescribed under the IMF loan, Russia

is seeking to raise excise taxes. Analysts warn that this will increase domestic energy prices and drive up inflation while still falling short of needed revenue.

The EU, Russia's largest trading partner, extended a \$1.2 billion grant to Russia. The grant comes from the Tacis program which promotes the transfer of information and experience to aid development in various sectors ranging from government administration to agriculture. However, Russia is making waves by insisting on protectionist tariffs of up to 20% on EU imports. EU representatives are miffed as general guidelines and policies had just been negotiated at the end of February that provide for consultation before such moves are employed.

The London Club renegotiated Vnesheconombank defaulted Soviet loans and received \$170 million in payment. The Paris Club deferred a \$34 billion debt payment. In doing so, the group of western creditor nations took a major step to providing Russia with a credit rating for the first time since the breakup of the Soviet Union. In the meantime, Germany and France have provided billions of dollars in loans to help Yeltsin solidify support against the communist opposition and to meet his campaign spending promises.

The new loan and debt agreements are not a sure bet on Russia's financial and political solvency, particularly in light of the Duma's vote to annul the 1991 accord that dissolved the Soviet Union. Adding to creditors discomfort is the campaign rhetoric of Zyuganov who consistently leads Yeltsin in opinion polls by a minimum of 8 points. As part of his platform, the Communist Party has endorsed reconstituting the Soviet Union, renationalizing banks and industries, and setting price controls for certain retail and food products. Several resolutions to come out of the Duma are raising eyebrows also. A presidential decree allowing for private ownership of land was attacked as unconstitu-

tional and against the interest of farmers. The order included directives to issue deeds and allows for purchases and sales. The fact that a fundamental premise of a free market - private property - is facing new attacks in one of Russia's legislative bodies highlights the stakes at risk in the coming presidential elections.

Game of Chicken Anyone?

For investors and fund managers, involvement in Russia's markets has been a high risk climate balanced with high returns. Rapid privatization and developing market institutions have opened up vast investment opportunities. But the high risk/high return climate has edged closer to a game of chicken. The unabated growth in organized crime and the high stakes of the presidential election has left many players lining up on the sidelines until June 16th. Still, positive economic indicators and continued development of market mechanisms keeps Russia one of the most intensely watched of the emerging markets.

The trading band set a year ago for the ruble has been maintained at 4,650 to 5,150. However, the steady decline of the ruble has prompted the central bank to intervene by selling hard currency reserves on 3/04 for \$13 million, \$8 million on 3/14, and most recently on April 11. Although the ruble has continued to decline in trading to 4,901 on 4/11, it has appreciated in real terms, regaining 71% in purchasing power in the past year. Demonstrating the government's growing confidence in the economic reforms, Yeltsin revealed a large package of tax and currency exchange proposals that would make the ruble fully convertible for trading transactions.

Data suggests that Russia's economy may be stabilizing as declines slow. The GDP for the first

quarter of 1996 was down 3% from last year while industrial output declined 4%. The Ministry of Finance reports a 1995 budget deficit of 2.9% of GDP which was 20% lower than anticipated. The peak of monthly CPI was 18% in 1995 and successfully brought down to 3% by year's end. Recent figures released from the State Statistics Committee reported that in February the CPI had its smallest weekly increase (.4%) since prices were freed in January of 1992. Consumer price inflation stood at 2.8% in mid-March indicating that last years tight monetary policies were beginning to bear fruit.

The Finance Ministry reported the possibility of tapping into precious stone and metals reserves in light of wage shortfalls. However, the central bank made known its desire to see more effective tax collection as the means for revenue as hard currency reserves have been depleted. The Russian State Tax service reported collecting only 43% of budgeted tax revenue totaling 150.2 trillion rubles (\$32 billion). These figures, however, are a post-inflation increase of 230% over 1994. In terms of GDP, 1995 tax revenue equaled 9.1% while 1994 produced 7.9%.

The central bank, chaired by Dubinin, has taken several encouraging steps in the development of the Russian market system. A Lombard rate (on par with the Fed Funds rate) has been introduced in an attempt to attach interest rates with a market mechanism. Beginning the first of May, the hard currency deposit reserve rates will be cut from 1.5% to 1.25%. The reserve requirement on bank deposits will be reduced to 18% from 20% for deposits up to 30 days. The non-market refinancing rate to commercial banks has been cut from 160% to 120%. The reduction of reserve requirements were aimed at helping several commercial banks facing insolvency. Still, the market continues to face problems with liquidity despite intervention by the central bank and large debt auctions.

In other developments, Micex - The Moscow Interbank Currency Exchange - is on track to begin trading futures contracts in the DM, the USD, and GKO (t-bills). The establishment of these instruments is pending on current talks with the central bank to allow GKO and OFZs (t-notes) to be used as deposits for trading. The last government debt auctions sold 2.8 trillion rubles (\$570 million) of GKOs. GKO yields were at 112% after rising 5.8 percentage points. Last months yields were peaking at 120% with several different issues maturing within a short period of time. 49-day bill auctions produced yields of 61.9% in comparison to last week's 50-day bill yield of 71.8%. Approximately 4% of Russia's gross domestic product is dedicated to the GKO market.

Why Did The Chicken Cross the Road?

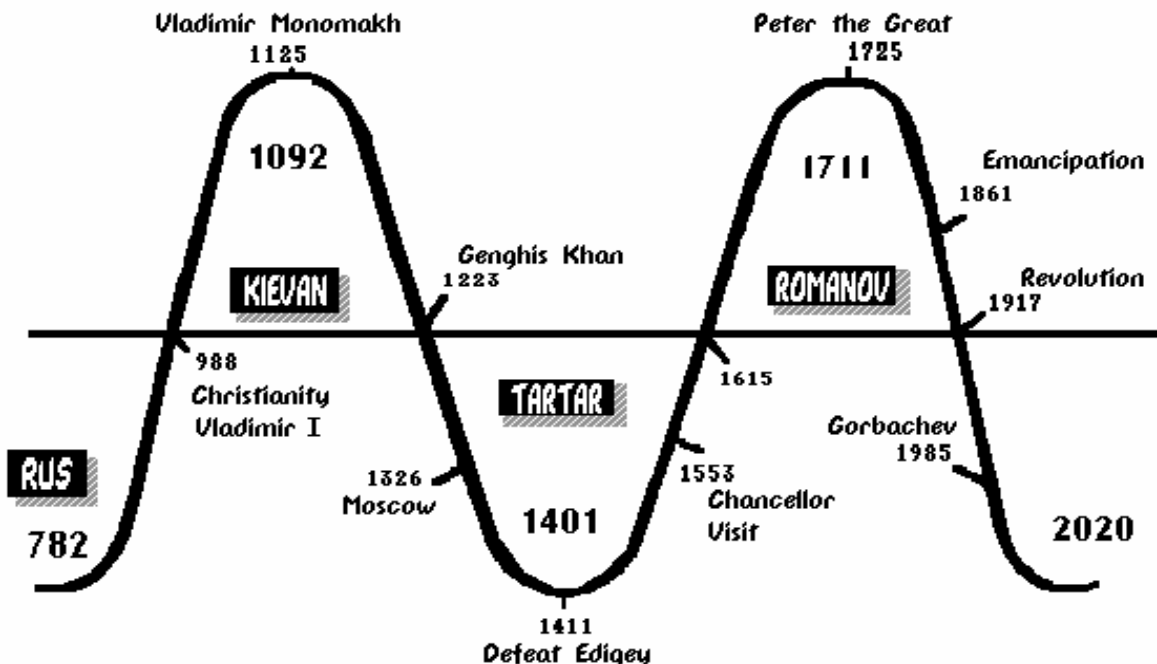
By any measure, 1996 is shaping up to be a critical juncture in the political and economic evolution of the former Soviet Union. After muddling through five years of political uncertainty and economic decline, Russia is approaching another test of democratic and free market resolve. Yeltsin must not only persuade the electorate to cross the road, but he must convince them that getting to the other side is an end unto itself and that once there, the reasons will be clear and the benefits felt by all. But the Russian people have grown impatient with free-market riddles and rhetoric as evidenced by the communist victory in December and the tight presidential race between Zyuganov and Yeltsin.

Yeltsin has realized this and begun to aggressively campaign - building on themes of "social and economic rights", raising living standards, fighting crime, and stimulating domestic production and job growth. He has made over \$14 billion worth of spending com-

mitments. A presidential reserve fund was set up in early February holding over \$6 billion to ensure prompt payment of wages and salaries. An additional \$4 billion has been dedicated to pensioners and the mining industry. Yeltsin promised a 40% increase (\$630 million) in funding to coal miners in order to end a strike. In 1991, this influential group helped sweep Yeltsin to power but now stands ready to cast their vote with the opposition. These spending commitments have some officials and creditors warning that it may double the budget deficit, increase inflation, and put economic reforms at risk. Nevertheless, recent polls indicate that this strategy is working as Yeltsin edges closer to Zyuganov.

Yeltsin has also incorporated the end of the Chechnyan War as a campaign promise. Over \$4 billion dollars for reconstruction in this devastated region has been committed. The President had offered a peace plan and cease fire at the

Long Wave Cycles of Russia



end of March but the implementation never left the paper. Russian soldiers continue to demolish villages, engage in sniper warfare, and even bombed a civilian building. Defense Minister Pavel Grachev has cited the Chechen rebels as "cancerous tumors" that must be cut out. Complete cessation of hostilities is a viable campaign promise to the voters but an unrealistic proposition to the military establishment. Yeltsin will need the support of the military not only to win but to keep control if he does. The Russian Interior Minister underscored this situation when he called for renationalizing several commercial banks to address the critical circumstances of the military caused by a "drastic shortage of budget financing." Kulikov warned that the rapid deterioration of the armed forces as well as the spiraling crime rate could lead to a crisis equivalent to that of the 1917 Bolshevik revolution. Yeltsin has now promised increased funding for recruiting, procurement, and salaries during his speeches.

The polls have consistently tracked Yeltsin behind Zyuganov - both of whom are formally registered presidential candidates in addition to nationalist Zhirinovsky. One million signatures from 15 regions of Russia are required for formal entry. {However, for a mere 1.6 billion rubles (\$318,000) one may purchase a dubious list. The Central Electoral Commission has refused to hear a filing regarding the legality of this entrepreneurial activity.} After the December Parliamentary elections, Yeltsin's popularity could easily be found around 4-7% while Zyuganov enjoyed ratings in the high teens to mid-twenties. However, Yeltsin has slowly been gaining to trim the gap to 14 points in January, 12 at the end of February, 10 points by the end of March, and latest indicators track him at 8 points behind and gaining. Russian equity and security markets have rallied in response to Yeltsin's growing support.

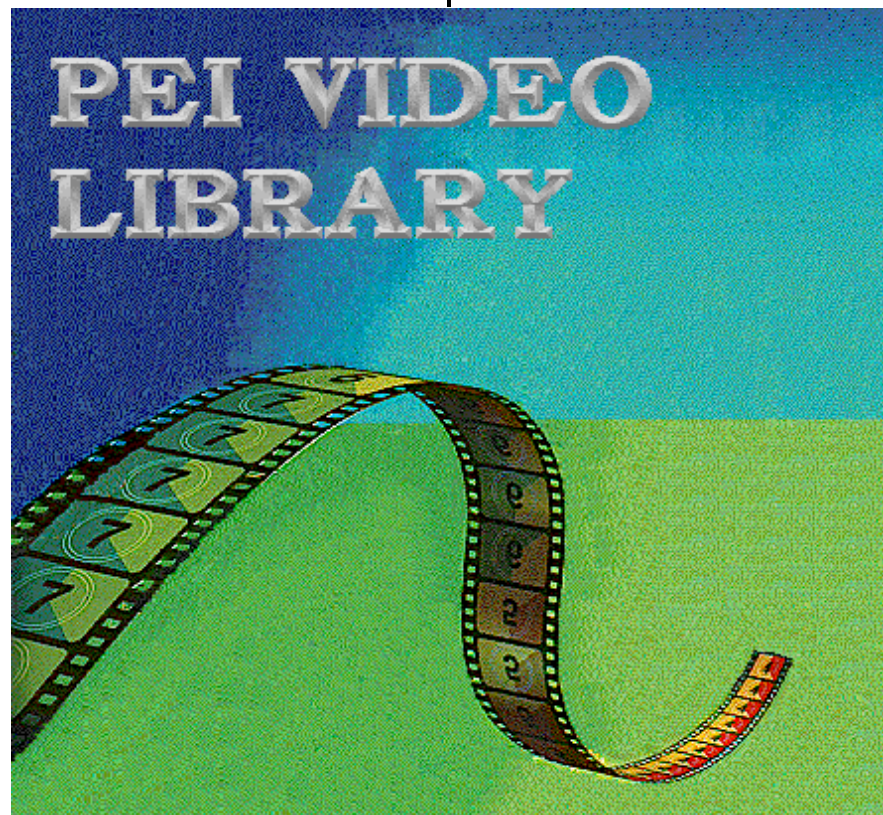
Several pro-reform and centrist groups have been approached by

Yeltsin's campaign staff in an effort to consolidate their support. Our Home is Russia (Chernomyrdin) has already stepped up to support Yeltsin. The most popular reform party, Yabloko (Yavlinsky), has not yet endorsed Yeltsin. The surprising appearance of Gorbachev as a presidential candidate (although not yet formalized) has had no visible affect and his press coverage is non-existent. Zhirinovsky has formally entered the race but is in a distant third place behind Zyuganov and Yeltsin. It is likely that the elections will go to a second round between the top two vote getters.

Chicken Little or Cyclical Trend?

As the elections draw closer, it becomes increasingly tempting for politicians and analysts alike to em-

brace long-term outcomes based on short-term events. Such doomsday predictions or rose-colored speculations often fail to consider the underlying cyclical nature of history. It is important to note that every major long-term trend contains within it several short-term reactions. Our computer models continue to identify a long-term bearish trend for Russia until 2020 when the overall cycle turns bullish. Within this long-term cycle, our models show May of 1996 as a turning point when the economic decline begins to slow. This stabilization should continue until 1998 when volatility increases and the slow decline begins to rapidly accelerate until it peaks in 2003. A Yeltsin victory should continue the short-term stabilization of the economic decline. On the other hand, a Zyuganov victory and its associated policy reversals are unlikely to receive immediate implementation nor would the cumulative effects be suffered immediately either.



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A Change in Government A View of Australia

by Nigel Kirwan
Executive Director
PEI Australia

The March 2nd election victory of the conservative Liberal/National Party coalition led by Prime Minister-elect John Howard could have significant implications for Australian society and capital markets. For business, and particularly small business, the coalition has promised to get rid of red-tape, free up the labour market, do away with so-called unfair dismissal laws which have been an impediment to employment, and deal with a series of imposts on business from provisional taxation, fringe benefit taxes and compulsory worker superannuation mandated by the former Hawke/Keating Labor governments. Pastoralists and mining companies should see some changes to the existing native title legislation which casts doubt on their ability to operate in vast inland and northern areas of the continent as well as a redefinition of restrictions placed on mining and agriculture in some areas proposed for World Heritage listing or as National Parks & Wilderness.

Probably the greatest area for essential change is the nation's costly and inefficient, but nonetheless popular, Medicare program. Healthcare consumes 11.5% of federal government outlays and this is rising fast, while the participation rate of individuals taking private health insurance has fallen below 25%. A reversal of these two trends and genuine reform of the system has been promised by the coalition - although they have had to avoid being too specific about

their plans in this area - and savings in government expenditure in this area could be significant. The other major area of federal government expenditure and responsibility, which the coalition promises to deal with, is the relationship with the states and territories. The problems are associated with duplication of service delivery and vertical fiscal imbalance where the states provide most of the services but the Commonwealth collects the major part of the tax take.

From a foreign perspective, there would appear to be no change in foreign investment rules, possibly little change in Australian interest rates, regardless of the coalitions desire to see them lower,

and conditions ripe for the stock market (which lags behind the underlying value in most commodities) to exude a greater confidence although local institutional buying generally lags behind offshore institutions in this respect.

The 40 seat majority obtained by the new government in the House of Representatives should provide a powerful mandate for change. This will be important for the government in its dealings with a potentially hostile Senate where a combination of far-left Greens and Democrats will hold the balance of power between Labor and Liberal/National.

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World Capital-Economic Review

by Hal Ludwig
Director PEI United States

UNITED STATES

PRODUCER PRICE INDEX: US wholesale prices fell in February for the first time since last June, indicating that inflation remains subdued in spite of recent evidence of faster economic growth. The Labor Department said the producer price index for finished goods fell 0.2%, partially reversing a gain of 0.3% in January. The annual rate of producer price inflation dropped to 2% from 2.3%. The drop reflected falls in food and energy prices. However, even excluding these volatile components, the "core" index rose by only a marginal 0.1%, after a 0.1% decline in January.

The price data showed little evidence of inflationary pressures at earlier stages of production than finished goods. The price indices for intermediate and crude goods fell 0.4% and 0.7% respectively.

INDUSTRIAL PRODUCTION: US industrial production showed its largest monthly gain in eight years in February. The Federal Reserve said production rose 1.2% after a revised decline of 0.4% in January, when activity was depressed by cold weather. Most analysts had expected an increase of about 0.9%.

The Fed said the production gain was partly a rebound from disruptions caused by severe weather. A recovery in aircraft production after the strike at Boeing last year ac-

counted for nearly a third of the total rise in output since December.

But there were production gains in nearly all industrial sectors. Output of consumer goods, business equipment and construction supplies were up 1.2% and 2.3% respectively from January. Overall production was 1.6% higher than in February last year.

RETAIL SALES: The US Commerce Department said American consumers boosted motor sales in February by 2% and helping lifting overall retail sales by 0.8%, signaling a continued moderate growth in the US economy.

In February, new car sales, which comprise about one quarter of total retail sales, were the strongest in six months. Sales of durable goods rebounded by 1.4%. The department also revised January's 0.3% drop in sales to a 0.1% decline.

Sales by general merchandise stores rose by 2.3%, the strongest pace in more than a year. but food store sales declined by 0.8% and furniture and appliances, up 0.3%, were relatively weak.

CONSUMER PRICES: The consumer price index rose 0.2% in February and by 2.7% on an annual basis - in line with expectations. Core consumer prices - which exclude the volatile components of food and energy - also rose 0.2%

EXISTING HOME SALES: US sales of existing homes rose strongly in February, despite higher mortgage rates, according to the National Association of Realtors, as the housing industry shook off the impact of bad weather. Total

sales of existing homes climbed 6.5% to a seasonally adjusted annual rate of 3.96 million, following a revised January decline of 3.9% to 3.72 million. The rebound was significantly stronger than Wall Street forecasts of an annual rate of 3.82 million.

NEW HOME STARTS: Construction starts on new homes and apartments increased in February to their highest rate in more than a year, according to the US Commerce Department. Despite bad weather and higher interest rates, total starts rose 3% to a seasonally adjusted annual rate of 1.49 million in February - the strongest building pace since December 1994, when they were running at 1.51 million.

The February pick-up in starts was sharply against Wall Street expectations of a decline to 1.42 million a year. The increase followed a 1.5% rise in January starts to a rate of 1.45 million units and a decline in December of 2.3% to a revised 1.43 million units a year.

The department sharply revised up its estimate of the level of December starts from a previously reported 1.39 million units, indicating the housing industry finished 1995 on a stronger note than thought earlier.

FACTORY ORDERS: The Commerce Department said new orders for manufactured goods rose 0.5% in January, reflecting strength in the technology sector. Officials also released revised figures for December, showing a gain of 1.7% rather than a 1.3% as previously reported.

The figures were considerably stronger than expected, where

analysts had predicted a fall in orders of 0.3%.

Orders rose despite weakness in the volatile transport sector, which were pulled down by an erratic 11.8% decline in aircraft orders. Excluding transport, orders rose 1.5% in January. The strongest sector - industrial machinery and equipment - registered a gain of 5.7% from December.

The orders figures showed encouraging strength in capital goods. Excluding aircraft and defense industries, new orders for capital goods - a guide to civilian investment trends - rose 3.3% in January, reversing falls in preceding months. The harsh winter weather in January mainly affected shipment orders, which fell 0.9% following a 0.7% gain in December.

DEFENSE SPENDING: The Clinton Administration unveiled a 1997 military budget, continuing a long-term trend of declining defense spending. Procurement of new weapons would take the biggest cut out of the Pentagon budget. Last year, the Pentagon had said such spending would increase this year, but those increases have been delayed by a year, because of pressure to reduce the federal deficit.

The Pentagon said its spending as a share of GDP would drop to 3.2% in this budget, the lowest since 1938. As recently as the 1980s, this figure was 6%. Although procurement spending would fall in 1997 to \$38.9 billion from this year's \$42.3 billion, the decline would only be temporary. By 2001 - the year before the President and Congress have agreed to balance the federal budget - it would have jumped 40% from current levels, to \$a60 billion. Senior military officials say such spending is essential to keep US forces up to date.

OUTPUT GROWTH: The US economy grew modestly in January and February without putting upward pressure on inflation, according to the Federal Reserve in its

"beige book" analysis of regional trends.

The report said, "Over half the districts cite moderate economic growth or continuing solid levels of economic activity. Most of the others mention recent improvements, largely reflecting rebounds from weather related slowdowns earlier in the year".

However, the Fed's regional banks saw little evidence of inflationary pressures. Retail prices were rising slightly if at all. Commodity prices were "steady, stabilizing, or increasing very little. wages were "increasing at a modest pace". Retail sales were weak nearly everywhere in January but most areas said activity picked up last month.

Manufacturing was mixed but "fairly flat on average". More than half the districts reported gains in some industries or sub-regions, but the Boston, St. Louis, Minneapolis, Kansas City and Dallas districts said output was either flat or growing more slowly than last year.

LEADING INDICATORS: Severe winter weather contributed to a 0.5% fall in the US index of leading indicators in January to its lowest level in more than two years. The Conference Board, the New York business analysis group that compiles the figures, said the decline largely reflected a sharp fall in the average factory working week, owing to blizzard on the east coast.

Other sources of weakness included declining building permits, a fall in consumer confidence and higher claims for state unemployment insurance.

The January drop followed a gain of 0.2% in December and a decline of 0.2% in November. The index is meant to predict economic trends six to nine months in advance, but many analysts regard it as a indicator of current conditions.. The index has fallen in four of the past six months.

CONSUMER CONFIDENCE: The Conference Board, a New York business analysis group said US consumer confidence held steady in March, after a sharp improvement in February. The index fell marginally to 97.7% from 98 in February. This was in line with readings late last year and well above the trough of 88.4% in January when severe weather and other distortions depressed other economic activity. Confidence readings of about 100 typically indicate solid economic growth.

The survey indicated consumers were generally "quite positive" about business conditions. However, Mr. Edgar Fielder, economic counselor to the board, said there was evidence of "uneasiness about the job market".

UNITED KINGDOM

TRADE SURPLUS: Britain recorded its first trade surplus for two and a half years with the rest of the European Union in December after imports from the Continent fell sharply. The surprise improvement came amid fresh signs that demand is faltering on both sides of the Channel, because of lower than expected growth in Europe.

Imports of consumer goods and cars have risen slightly in recent months. However, manufacturing confidence may be weakening, with imports of investment goods used by manufacturers falling. These types of imports showed the sharpest quarterly fall in the last three months of 1995 for five years. Imports of German goods seem to be particularly affected.

The value of exports in December was a seasonally adjusted 0.5% lower than in November, according to the CSO office. Measured on a three monthly basis, in volume terms - a better guide to trend - exports were 1.5% lower in between the third and fourth quarters.

The weakness was not spread equally: sales to Germany fell

3.3%, while exports to Belgium, Holland and Luxembourg are running at record levels. This patchy performance left exports falling more slowly than imports, resulting in a BP56 million surplus in Trade with European countries, against a BP118 million deficit in November.

This surplus helped bring the overall trade deficit with the whole world to BP557 million in December, unchanged from November.

INFLATION: The annual rate of inflation, which excludes mortgage interest payments, rose to 2.9% in February, from 2.8% in January. This occurred even though the "headline" rate - which includes all items - fell to its lowest level for 15 months because of lower mortgage costs and sharp falls in petrol and tobacco prices. However, a Confederation of British Industry survey showed that demand for manufacturing goods was at its weakest level for more than two years.

The CBI warned that although factories are still increasing output, it fears some companies may be excessively optimistic - particularly since export markets are weakening.

BALANCE OF PAYMENTS: Britain's balance of payments swung further into deficit in the final quarter of last year as transfer payments to European Union institutions reached record levels, according to official figures.

The current account was in deficit by BP1.8 billion in the fourth quarter of last year, according to the CSO. This was less than the BP2.1 billion deficit recorded in the third quarter, because of a recovery in income from UK companies' investments overseas, which recorded its highest surplus for a year and a half.

But the figure took the deficit for 1995 as a whole to BP6.7 billion. This was more than three times as big as the deficit in 1994 - but still little more than half the size of the BP11 billion deficit recorded in 1993. Revisions to earlier data also

provided a gloomier quarterly picture of the balance of payments throughout 1995 than earlier figures had suggested.

The CSO increased its estimate of the deficit in both the second and third quarters of last year by about a third because of lower investment income from abroad and higher transfer to the EU. The UK's payments to the EU institutions - such as the agricultural fund, social fund and regional development fund - far exceeded receipts from the EUY last year. The payments deficit almost doubled from BP2.1 billion in 1994 to BP4.1 billion in 1995.

The deterioration in the visible trade balance reflected the sharp slowdown abroad which hit exports. Services income bucked the trend, however. Net income from services rose from BP4.8 billion in 1994 to a surplus of BP% .7 billion last year, the highest since 1987.

The total invisible balance - which includes services, investment income and transfers - slipped from BP1.4 billion in the third quarter to BP0.9 billion in the fourth quarter, its lowest for two years.

Direct investment overseas by UK companies rose to a record BP24 billion in 1995. Direct investment in the UK by overseas companies also rose to record levels. It tripled between the third and fourth quarters of the year - largely reflecting overseas company takeovers of UK companies.

MONEY SUPPLY: According to official figures, growth in money supply eased in February for the first time since last autumn, but lending by banks and building societies rose at its fastest rate for almost five years.

The Bank of England (the UK central bank) said that M\$, the broad measure of the amount of money circulating in the economy, grew at an annual rate of 9.9% in February, down from 10.3% in January. Growth in the money supply has accelerated rapidly since

the beginning of last year to exceed the government's monitoring range of 3-9%. Lending by banks and building societies grew by 9.5% in the 12 months to February.

MANUFACTURING INVESTMENT: Fears for the long-term health of manufacturing industry were eased when official figures confirmed that the drop in factory investment last year was not as great as suspected. Higher than expected spending on engineering machinery and on investment in the chemical sector meant that government statisticians revised down estimates of the overall decline in investment in the fourth quarter of last year. Seasonally adjusted manufacturing investment in the fourth quarter was 5% lower than in the third quarter at constant prices, the Central Statistical Office (CSO) said. This was better than the picture presented by earlier figures which had startled City of London economists by showing a 9% drop in investment.

TOURIST INDUSTRY: A weak pound and the Northern Ireland cease-fire helped the British tourist industry notch up a record year in 1995, with visitor spending up by about 18%. Mrs. Virginia Bottomly hailed the figures as evidence that tourism is now more important than North Sea oil and the financial services industry to the UK economy.

But many in the tourist industry remain concerned that Britain is failing to increase its market share of world tourism, as they believe more government sounding overseas is vital. Figures from the CSO show that visitor spending in the UK in 1995 was about BP11.8 billion (\$18.2 billion) up from BP10 billion in 1994.

The annual figures also show an increase of some 12% in the number of visitors to Britain - the largest jump in recent years. The total number of visitors was about 23.5 million, up from 21 million.

NORTH SEA OUTPUT: The annual industry review by Wood

Mackenzie, the Edinburgh based energy-consultants says UK oil production is on track to set a record of 2.71 million barrels a day this year.

The forecast represents a 5% increase on last year's average output of 2.58 million b/d, which in turn amounted to a 3% increase over 1994. The upward trend in North Sea production is set to continue for some years, says Wood Mackenzie, with output of as much as 3 million b/d towards the end of the decade.

The growth in UK production is part of a general rise in North Sea output. Total production from Norway, the UK, Denmark and the Netherlands this year is expected to average around 6 million B/d, a 9% rise over 1995.

The Norwegian government will be the largest producer, accounting for about a third of total North Sea production. Statoil, the Norwegian state oil company will be the second largest North Sea producer this year, followed by British Petroleum.

The consultants say the expected rise in 1996 production in the UK will be the result of a less extensive offshore maintenance session this year and the start-up of 15 new fields.

JAPAN

GDP: The government's economic planning agency said stronger than expected consumer spending lifted Japan's gross domestic product by an annualized 3.6% in the final quarter of 1995, the fastest growth for five years. The result confirms the government's assessment that Japan is recovering from there longest recession since the 1930s.

GDP rose 0.9% in the final quarter from the three months to September, an acceleration on 1.6% growth in the second and third quarters. But even after a better than expected final three months,

the Japanese economy grew by just 0.9% last calendar year, the third year in which it has grown less than 1%.

Mr. Makato Koayshi, the agency's vice-minister, said the economy was now on track to achieve its official target of 1.2% growth in the fiscal year ending in March.

Domestic demand rose by 1.5% from the third to the final quarter, by far the largest contributor to the 0.9% GDP growth over that period. Within this, private consumption rose by 0.4% quarter on quarter, led by spending on car and, personal computers.

Government spending from a record Y14,220 billion (\$135 billion) public works package announced last September underpinned much of the growth in the final quarter. Public investment contributed 0.6% to quarter on quarter growth.

IMPORT GROWTH CUTS TRADE SURPLUS: Formerly export-obsessed Japan reported a gap of just \$6.1 billion in February, slightly above the market estimates and sharply down on the \$11.3 billion of the same month last year. Imports grew 16.8%, according to preliminary figures from the finance ministry. It was the 36th consecutive month of increased imports and took place despite the weakness of consumer demand for most of that period.

Exports dropped by 3.3% in the 12 months to February, the first fall in three years, attributable to a one-off correction from unusually high overseas sales in February last year. This was when Japanese exporters were rushing to catch up on deliveries delayed by the January Kobe earthquake.

But compared with January this year, overseas sales rose by the same amount, 3.3%, a pace of growth which reflects weakness of demand in the US and Europe.

Japan's surplus with the US dropped 30% to \$3.4 billion. The surplus with other Asian countries, on a long-term rising trend, also dropped by almost 39% to \$3.8 billion, the second monthly decline.

CORPORATE SPENDING: Capital spending by Japanese companies increased for the third successive quarter in the last three months of 1995, providing further evidence of the country's gradual economic recovery.. Corporate investment rose 5.7% compared with the same period a year earlier, according to a survey published by the ministry of finance, with the increase especially marked among manufacturers.

A survey by the Japan Development Bank suggested that corporate spending plans for 1996 point to continued recovery in investment. Private sector capital formation in the financial year beginning in March is expected to rise by 0.7%, the second successive year of growth.' The figure is lower than the current year's 5.7% projected increase, but a bank official said the forecast for next year reflected a familiar caution on the part of companies.

HOUSEHOLD DEBT: The average salaried worker's household borrowed 11.4% more in 1995 than the previous year, the third year it has risen by more than 10%, according to the government's Management and Coordination Agency. Nearly all these loans - 93% - were taken out to buy property rather than consumer goods. The average household had Y12.6 million (\$120,000) savings - a record high - and Y4.5 million of borrowings .

Japan's salaried workers preferred to save rather than spend most of their spare cash. Their average savings last year rose by 2.2%, faster than the 1.6% average rise in income.

Savings had dropped in 1994 for the first time in three decades, holding out hopes for a recovery in con-

sumer spending, but this has yet to gain impetus.

INDUSTRIAL OUTPUT: The Ministry of International Trade and Industry (MITI) reduced its January production estimate to zero, from 0.5% month-on-month growth. It said corporate shipments fell 0.9% in January, instead of 0.7% as earlier estimated, while stocks of unsold goods and materials rose by 0.8% instead of the preliminary 0.6% increase.

MITI did not change its forecast that industrial output would rise by 1.5% in February and then fall back sharply by 5.3% in March, as companies sought to trim stocks after overproducing early in the year.

The forecast decline would eliminate four months of output increase and bring production volumes back to the level of last September. For the first quarter to March, MITI expects a marginal 0.2% rise in output compared with the previous quarter.

SURVEY REAFFIRMS SLOW RECOVERY: The "tankan" survey, which forecasts Japan's short-term economic outlook based on responses from some 9,000 companies, reaffirmed forecasts for a sluggish rebound from four years of slow economic growth and lessened expectations of higher interest rates. The survey is conducted by the Bank of Japan.

The manufacturing business conditions index, the leading indicator that reflects the general sentiment of Japan's major producers, was minus 12. That was up from minus 14 recorded in the last survey in November, but below expectations of minus seven. The non-manufacturing sector data improved to minus 18 from minus 22.

The survey portrayed an economy in transition, as long-term corporate overhaul continues to damp consumer spending. Profits for the year ending March 31, are expected to rise by 11% and 3.2% among manufacturers and non-manufacturers, respectively, in part

because the yen's relative decline against the dollar. But the survey suggested that Japanese workers aren't getting higher wages. Instead, the survey showed, companies are continuing to invest in new plants and equipment overseas.

The outlook for the retail industry deteriorated, as that sector's index slipped to minus 16 from minus 14 in November. The lingering recession has forced the industry into aggressive sales and cost cutting, which have proved especially painful for the country's department stores.

Sluggish retail sales have resulted in persistently high inventories, according to the tankan.

EASING OF CURRENCY CURBS: Japan's finance ministry intends by the end of March to ease some curbs on currency transactions by security houses and other companies with foreign businesses. Senior officials said they accepted in principle proposals by a working party of the ruling coalition to allow companies to "net out" foreign exchange transactions between different subsidiaries, to reduce the number of transactions necessary with authorized foreign exchange banks.

The coalition called for an end to the present ceiling of Y100 million allowed for such offset deals and an end to the present requirement that companies must set official approval for foreign exchange transactions carried out two years after the original deal was struck.

Economists in Tokyo said these were minor technical changes but nevertheless significant as the latest in a series of steps to encourage freer trade in the yen.

MONEY SUPPLY: Japan's Broad M2 money supply rose 2.8% in February from a year earlier, after expanding 3.1% the previous month, according to the Bank of Japan. M2 is the broadest measure of total money supply, comprising cash in circulation, deposits in bank accounts as well as quasi-money,

including time deposits and treasury bills.

M1 or cash in circulation rose 16% in February after a revised 14.7% in January. Preliminary data had shown a 14.8% rise in M1 for January.

GERMANY

HEALTH INSURANCE SYSTEM: Germany's health insurance system ended last year with a DM2.4 billion surplus in 1994, prompting fears that contributions may have to rise unless savings are made. Mr. Horst Seehofer, the health minister, warned that contributions, divided equally between employers and employees, could jump by one percentage point to 14.4% of earnings unless agreement is reached between the federal government and the Lander (states) on disputed plans to limit the costs of hospital care.

Last year's deficit was lower than the DM10 billion-12 billion recently forecast by health insurance officials. Mr. Seehofer said the move into deficit slowed markedly in the final three months, with the 1995 shortfall in western Germany dropping to DM4.15 billion from DM5.8 billion at the end of September. However, the deficit in eastern Germany grew to DM2.85 billion from DM1.7 billion in the first three quarters.

GROSS DOMESTIC PRODUCT: German GDP contracted by 0.5% during the fourth quarter last year according to figures from the Federal Statistics Office. The German economy grew 1.9% last year. Output rose 1.6% in west Germany and 5.6% in the east, a significant slowdown.

The output data were widely discounted in financial markets, although several GDP components appeared to cause some surprise. These included the strong fall in inventory accumulation and a rise in private consumption. Some

economists were puzzled by the 3.4% rise in exports from the previous quarter, and the 5.5% rise year-on-year.

UNEMPLOYMENT - ONE IN NINE OUT OF WORK: Germany's unemployment rate in February soared to 11.1% of the work force from 10.8% in January, logging a post World War II record for the second month in a row. The jobless total rose to seasonally adjusted 4.27 million from 4.16 million; the seasonally adjusted increase was 107,000, almost double the 56,000 rise in January. The government

said unusually cold weather and a stagnant economy spurred the increase, but it predicted improvement by midyear.

Eastern Germany was especially hard hit, with 1.31 million people or 17.5% of the labor force out of work. In western Germany, where 2.96 million were jobless, the unemployment rate was 9.6%. Mr. Bernhard Jagoda, the labor office president, said this year's record unemployment reflected the loss of 262,000 construction jobs in January and February. Although the hard winter was partly to blame,

companies were also reacting to a lack of orders.

GOVERNMENT SPENDING CAP: Forecasts that the German budget deficit this year - predicted at DM60 billion - would in fact be DM20 billion higher have prompted fears that Mr. Theo Waigel, the finance minister, will have to announce a cap on government spending because of lower tax revenues.

Press reports suggested the spending restrictions would only be introduced after three state elec-

The German Finance Minister

by Harry Groenert

Executive Director, PEI Continental Europe

When Theo Waigel took over from Gerhard Stoltenberg as Finance Minister in April 1989 even the opposition named him an "intelligent guy." Today, seven years later the picture has changed. He has managed to break several records as far as the budget is concerned. Even the BDI-President, Mr. Hans-O. Henkel expressed that Mr. Waigel's activities had been inadequate.

What did he do? He reduced taxes on Salt and chewing tobacco, however, since 1991 he has increased other taxes seventeen times:

1/1/91 Fuel tax	1/7/93 Withholding tax on deposits
1/7/91 Solidaritätszuschlag (till 30/6/92)	1/1/94 Insurance tax
1/7/91 Fuel tax	1/1/94 Car tax for diesel cars
1/7/91 Fuel tax on heating oil	1/1/94 Fuel tax
1/7/91 Fuel tax on natural gas	1/1/94 Coal Pfenning
1/7/91 Insurance tax	1/95 Solidaritätszuschlag
1/3/92 Car tax	1/95 Insurance tax
1/1/93 Tax on tobacco	1/1/95 Wealth tax
1/1/93 Value added tax	

During his period in office he has accumulated almost as much on debt as his twelve predecessors combined. He has increased the public debt by nearly 100%, from DM491 billion to DM822 billion. The interest payments have increased from formerly DM32 billion to DM99 billion as of today. Currently, about 21% of the tax income has to be spent on interest payments.

To summarize the political achievements so far:

Highest tax burden ever
Almost highest unemployment
Companies are moving offshore
Maastricht shall help?

Recently asked on his politics, Waigel said about Waigel, "I could say good-bye anytime and start as a lawyer.."
Good for him.

tions had taken place on March 24, the next important date in Germany's political calendar. However, the finance ministry insisted that no decision had been taken and that the final decision had "nothing to do with the elections".

Fears about lower tax revenues caused Mr. Waigel to demand last October that all government expenditure over DM1 million be cleared with his ministry. That spending cap, however, ran out on December 31.

TRADE SURPLUS: According to the federal statistics office, visible exports fell to DM61.6 billion in December last year from DM65.5 billion in November and were 2.7% below the DM63.3 billion of December 1994.

Imports declined to DM54.6 billion in December, from DM55.3 billion the previous month and were 6.9% lower than the DM58.6 billion of December 1994. As a result, December's trade surplus was lower than November's DM10.2 billion but higher than the DM4.7 billion of the previous December.

Germany's visible trade surplus increased to DM93.4 billion last year from DM73.3 billion in 1994 as exports rose 5.4% to DM727.6 billion from DM690.6 billion and imports advanced 2.7% to DM634.2 billion from DM617.3 billion.

After deducting net investment income together with the balance of trade in services and net transfers, Germany's current account balance of payments recorded a provisional DM3.5 billion deficit in December after a DM4 billion deficit in December 1994. For last year as a whole, the current account deficit fell to DM24.8 billion from DM34.7 billion in 1994.

Statistics office officials said the export downturn was a delayed response to last year's sharp increase in the value of the D-Mark. It cast doubt on government hopes that exports would support German economic activity this year at a time

of weak consumer demand and investment.

PRODUCER PRICES: German producer prices rose 0.1% in February from January, but were down 0.2% year-on-year.

NEW ORDERS: New orders for plant and machinery in Germany fell 6% in price-adjusted terms in February from a year earlier, said the VDMA industry association. It blamed weakness in domestic investment.

INFLATION: Germany's consumer price inflation crept up to an annual 1.5% in March from 1.4% in February, the German federal statistics office said. Prices in western Germany rose 0.1%, after a 0.5% rise in February. The office also released final data for February inflation showing prices across the whole country rose 0.5% from January and 1.6% from a year earlier.

FRANCE

INTEREST RATES: The Bank of France trimmed its two key interest rates by 0.10 of a percentage point, in a furthering of softening of monetary policy induced by the slowdown in the economy. The reductions, which bring the central banks intervention base rate to 3.8% and its repurchase rate to 5.5%, may increase the government's impatience to see the commercial banks pass on the benefit of the Bank of France cuts in lower lending rates to their own customers. The banks have proved reluctant to do this, claiming the need for higher lending margins to improve their poor profitability. Some French MPs have criticized the government as well as the Bank of France, for slow, piecemeal action to revive the economy.

CONSUMER PRICES: France's consumer price index in February provisionally rose 0.4% from the previous month, and 2% from a year earlier, according to the national statistics institute. Excluding energy prices, which rose 0.7%

from January and 1.9% from a year earlier.

The prices of manufactured products rose 0.5% from the previous month due to the 1.5% increase in clothing and shoe prices. Services sector prices rose 0.2%, and 3.2% year-on-year.

PUBLIC SPENDING FREEZE: The French government announced a FF20 billion (\$4 billion) freeze in budgets allocated across all ministries for 1996 as part of its plan to maintain public spending targets. Mr. Jean Arthuis, economics minister, said the freeze would cover all departments but would not affect civil servants' salaries, social expenditure or debt payments. He said it was imposed to maintain the budget deficit for 1996 at below FF287 billion. The government also indicated that tax receipts for 1995 would fall by 0.4% from the level FF296 billion collected in 1994. It said this reflected a substantial increase in tax deductions, including those for professional expenses and household help. By contrast, value-added tax receipts rose by 2.6% last year before the effects of the 2% increase in the tax.

INDUSTRIAL PRODUCTION: French industrial production fell 0.7% in December after rising a revised 0.5% in November.

The decline in French industrial activity has stopped in recent months and a pick up in production can be expected in the second quarter, but prices should remain on a downward trend, according to the statistics office, Insee. The balance between the number of industrialists reporting a decline in output and those experiencing an increase during the previous three months narrowed 10 percentage points in March from 11 the month before. The difference between those expecting a decline in output and those expecting an increase fell to 23 points from 32.

CONSUMER SPENDING: French consumer spending was unchanged in February, after a re-

vised 5.0% rise in January compared with December, according to France's national statistics institute, Insee. The February figures are encouraging and suggest then French economy will avoid a recession.

RETAIL SALES: French retail sales fell a provisional 4.7% in December, following a rise of 4.4% in November, according to figures from Insee. December sales were flat compared with the average of the previous three months.

CURRENT ACCOUNT: France virtually doubled its current account surplus last year to reach FF84.5 billion, an increase of nearly FF40 billion on 1994, according to the finance ministry. The trade surplus in goods rose to more than FF50 billion, while that of services stayed steady at around FF74 billion.

The balance on investment income was reduced to a deficit of FF31 billion, though French companies, anxious to reduce their debt, cut their direct investment abroad from FF106 billion in 1994 to FF92.5 billion last year, while at the same time selling off foreign companies worth FF44.6 billion. However, foreign investors maintained their investments in France at around FF60 billion last year.

Public financial transfers, traditionally in deficit because France is a net contributor to the European Union budget and a large provider of foreign development aid, remained in deficit at FF32.5 billion, but this was FF12 billion smaller than in 1994.

CANADA

BORROWING CUTS: Canada's borrowing requirement for the 1997-98 fiscal year will be the smallest in almost three decades and the lowest among the Group of Seven leading industrial countries relative to gross domestic product, according to finance minister Paul Martin in his annual budget speech.

The budget contained only a handful of minor tax changes. But Mr. Martin launched an overhaul of Canada's social security system, notably the scheme that has guaranteed generous pensions for every Canadian over 65. The pension reforms, in the face of an aging population, mean high income retirees - or about 9% of the total - will no longer be eligible for government pensions after 2001.

Mr. Martin predicted he could easily meet his target of bringing the budget deficit down to C\$24.3 billion (\$US17.7 billion) or 3% of GDP, in the fiscal year to the end of March 1997. The deficit would shrink further to C\$17 billion, or 2% of GDP, in 1997-98. The minister pledged to keep moving towards a balanced budget, but said that "we will do so in a way that is measured, deliberate and responsible."

The borrowing requirement is expected to fall to C\$6 billion, or 0.7% of GDP, in 1997-98 from C\$30 billion, or 4.2% of GDP, in 1993-94. Aside from borrowing, the rest of the budget deficit is to be met by non-budgetary transactions, including use of pension fund surpluses. The deficit will be brought down in the coming fiscal year mainly by a cut in transfer payments to the ten provinces for health, education and social security, lower business subsidies, and defense cuts.

AUSTRALIA

BUDGET DEFICIT: Australia aims at fiscal balance by 1997-98, a year later than planned under the ousted Labor government, after figures released by the new Liberal-National ruling coalition showed it faced an underlying federal budget deficit of A\$7.64 billion in the 1996-97 year.

The treasury estimate of the deficit is struck before asset sale proceeds, and before spending pledges made during the election campaign. The figures contrast

sharply with small surplus predicted by Mr. Ralph Willis, then federal treasurer, in last May's budget speech. Mr. Peter Costello, his successor, said the government planned to redress the balance by taking A\$4 billion out of the budget in 1996-97 and a similar amount in the next year, "overwhelmingly through expenditure reductions".

ECONOMIC GROWTH: Australia's economy continued to grow at around 0.5%, seasonally adjusted, during the final quarter of 1995, bringing the annualized growth for the year to about 3.1%. The final quarter result marks a considerable slowdown from the 1.65 rise in real gross domestic product seen during the September quarter, when year-on-year growth rate was 3.3%.

But it was still a slightly stronger performance than private-sector economists had been expecting, with some cautioning the annual growth rate could slip below 3%.

BUSINESS CONFIDENCE POLL: According to the latest quarterly industrial trends survey by the Australian Chamber of Commerce and Industry and Westpac bank. The ACCI-Westpac survey is one of the first pieces of statistical data since the change of government on March 2, which brought to an end 13 years of Labor rule. It found that manufacturing activity remained weak in the first quarter, with industry reporting falling output and lower orders. Capacity utilization also declined.

By contrast, most manufacturers said they were expecting improved conditions over the next six months, and expected to see new orders and output rise in the second quarter. In the first quarter, some 34a5 of the respondents predicted improved business in six months, compared with only 8% in the final quarter of 1995.