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REF 470

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Division of International Finance

REVIEW OF FOREIGN DEVELOPMENTS

February 26, 1964

Recent Economic Developments in the Netherlands
October 1963 - January 1964

16 pages

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Recent Economic Developments in the Netherlands
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Economic developments in the Netherlands during the past three months have been dominated by growing concern over the inflationary pressures emanating from the wage and price agreements concluded in October 1963 and the Government's attempts to bring them under control.^{1/} Both the wage and price situation are in flux. The 10 per cent increase in wages authorized last fall is being taken as a minimum and actual agreements seem to be averaging around 15 per cent. The labor market remains tight and employers appear to be willing to give increases well in excess of the 10 per cent to retain their working force, particularly since they can pass some part of the wage increase on in higher prices.

Prices have been moving up on a broad front. Several factors are contributing to this trend: higher wage costs; rising raw material prices in world markets; higher agricultural prices in accordance with EEC-sponsored farm policies; and the deliberate Government effort to use higher prices to curtail consumer incomes. This, however, has caused unions to declare that they cannot abide by the October 1963 agreement on wage increases, if the larger part of additional income is swallowed up by price increases, and that they would feel justified in reopening negotiations later in the year if such proved to be the case.

To keep the process of wage-price adjustment under control, the Dutch authorities have taken a series of limited measures in the period under review. Some price increases in excess of the authorized 5 per cent limit have been rolled back. In the fiscal field, remaining tax advantages on private investment have been revoked and the curb on government investment spending has been extended an additional

^{1/} See "Recent Economic Developments in the Netherlands, May-October 1963" dated December 6, 1963.

six months to October 1964. In the monetary field, credit ceilings which were reimposed in October were extended, the discount rate was raised from 3-1/2 to 4 per cent in early January, and restrictions on personal loans and installment credit were announced in early February. The rise in discount rate merely confirmed market trends toward higher rates apparent since last September. Fair trade practices in retail trade were also abolished.

Thus far, the central bank has refrained from raising the minimum cash reserve requirement (which was reduced to zero in September), presumably because the commercial banks could bring back portions of their money-market assets abroad if domestic credit availabilities tightened. This is exactly what the monetary authorities wish to avoid. In practice, the credit ceiling system works to encourage Dutch banks to put more money abroad because funds placed outside the Netherlands are not counted in the total of permissible credit extensions. This policy has so far been successful; Dutch banks are reported to be investing considerable amounts in the Euro-dollar market. In fact, these outflows in January, together with heavier imports, underlie a recent easing of the spot guilder in the foreign-exchange market and a reduction in official reserves estimated at about \$40 million in January.

Because of the wage and price adjustments now in progress, some changes are being made in official Dutch estimates for major economic sectors for 1964. The current account is expected to shift into substantial deficit for 1964 (fl 1 billion or \$276 million) compared with a surplus (fl 450 million or \$124 million) in 1963. The rate of increase in exports of goods and services is expected to decline from 7 per cent in 1963 to 5 per cent in 1964 and imports are expected to rise further during the year. The outlook for 1964 is for a modest over-all balance of payments deficit, probably financed by a drawing down of official reserves (in the light of the central bank policy of not encouraging commercial banks to repatriate foreign balances) and in this way withdrawing liquidity from the domestic economy.

However, the vigorous domestic expansion underway in 1963 is expected to be maintained during the current year. In fact, the EEC estimates that real GNP will rise even faster in 1964 than it did in 1963: by 4.5 per cent compared with 4 per cent. Considering the strains on Dutch labor and plant resources, the projected advance in output seems to imply an optimistic judgment about the ability of the Dutch authorities to keep well in hand the substantial price-wage adjustments presently underway.

Industrial output continues to expand

Despite inflationary pressures within the Dutch economy, industrial production, which had been stagnating at a high level during the second and third quarters of 1963, rose considerably in October and is reported to have risen further in subsequent months. (See Table 1). For 1963 as a whole industrial output rose by 4 per cent, as compared with 3.8 per cent in 1962.

Table 1. Netherlands: Industrial Production 1962 - October 1963^{1/}
(index numbers 1953=100, seasonally adjusted, monthly average or month)

1962	I	167	June	173
	II	166	July	172
	III	164	August	171
	IV	169	September	169
1963	I	170	October	175
	II	172		
	III	171		

1/ Excludes building

Source: OECD

This increase in output was achieved despite a further tightening of the labor market and the virtual nonexistence of further labor reserves. (See Table 2). Employment in industry has been virtually unchanged since mid-1962 and increases in output

have been due to increases in productivity. In the third quarter of 1963 output was 5.8 per cent above the third quarter 1962 level.

Table 2. Netherlands: Labor Market 1962 - December 1963
(in thousands, monthly averages or month, seasonally adjusted)

1962			1963		
	<u>Unemployment</u>	<u>Vacancies</u>		<u>Unemployment</u>	<u>Vacancies</u>
I	28	123	June	30	125
II	30	125	July	31	125
III	33	121	August	31	123
IV	32	117	September	30	120
1963			October	28	123
I	38	114	November	28	124
II	30	121	December	27	128
III	30	124			
IV	28	125			

Source: OECD

The continuing productivity gains explain why increases in demand could be accommodated with only moderate price advances. These gains also contributed to an acceleration of investment demand which became apparent in the second quarter of 1963. The inflow of orders to the consumer goods and the investment goods sectors from both foreign and domestic sources increased during the last quarter of 1963 according to a survey conducted by the Central Bureau of Statistics. (See Table 3). By December the industrial order backlog was rising again.

Table 3. Netherlands: Order backlog 1961 - December 1963 ^{1/}
(Orders in terms of months of production, January 1961=100)

<u>End of Month</u>	<u>All industries excl. chemical industry</u>			<u>Consumer goods sector</u>			<u>Investment goods sector and all others</u>		
	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>
March	96	95	88	94	93	91	97	95	88
June	100	92	87	99	95	97	101	92	86
September	98	89	85	93	93	93	99	88	84
December	97	90	89	99	95	103	96	89	86

^{1/} Based on a sample survey.

Source: Centraal Bureau voor de Statistiek

The wage rate index, pending the wage increases slated for the beginning of 1964, remained stable during the second half of 1963. (See Table 4). However, prices began to climb in the fourth quarter. Wholesale prices, unchanged during the first nine months of 1963, rose by 3 per cent in October; prices of manufactured goods were up 2 per cent. Consumer prices, on the other hand, were virtually stable with seasonal declines in food prices offsetting increases in other sectors. Through October, both export and import prices also remained relatively stable.

Table 4. Netherlands: Selected Wage and Price Indices, 1962 - Dec. 1963
(Index numbers 1958=100, monthly averages and month)

		<u>Hourly Wage Rates</u>	<u>Wholesale Prices</u>	<u>Manufactured Products Prices</u>	<u>Cost of Living</u>	<u>Export Prices</u>	<u>Import Prices</u>
1962	I	125	98	100	107	98	95
	II	128	101	100	109	100	95
	III	130	98	100	109	96	94
	IV	133	98	102	109	98	94
1963	I	137	100	102	112	100	96
	II	138	99	102	114	98	97
	III	140	100	103	112	99	97
	Oct.	140	103	105	113	99	96
	Nov.	140	<u>a/</u>	<u>a/</u>	113	<u>a/</u>	<u>a/</u>
	Dec.	140	<u>a/</u>	<u>a/</u>	114	<u>a/</u>	<u>a/</u>

a/ Not available.

Source: International Financial Statistics, Centraal Bureau voor de Statistiek.

Trade balance deteriorates as exports decline

During the second half of the year, exports dropped from the second-quarter peak. (See Table 5). Fourth-quarter exports, on a seasonally adjusted basis, were 4.5 per cent below the third quarter and 7.1 per cent below the second quarter level.

Table 5. Netherlands: Merchandise Trade, 1962 - December 1963
(Million U. S. dollars, monthly averages, seasonally adjusted)

		<u>Exports, f.o.b.</u>	<u>Imports, c.i.f.</u>	<u>Balance</u>	<u>Exports as % of Imports</u>
1962	I	375	450	- 75	83.3
	II	389	443	- 54	87.8
	III	381	448	- 67	85.0
	IV	386	444	- 58	86.9
1963	I	386	461	- 75	83.7
	II	438	496	- 59	88.3
	III	426	502	- 76	84.9
	IV	407	532	-125	76.5
	Oct.	422	540	-118	78.1
	Nov.	417	537	-120	77.7
	Dec.	382	519	-137	73.6

Source: OECD

At the same time, imports continued to rise, even at an accelerated rate: they were up 6.0 per cent in the fourth quarter. Growing imports of investment goods following the revival in investment demand, expanding raw materials imports at rising prices, and higher inventory demand on the expectation of further price increases contributed to the fourth-quarter jump in imports.

With imports rising and exports declining, the trade deficit increased from a monthly average of fl 76 million in the third quarter to fl 125 million in the fourth quarter of 1963. The percentage of imports covered by exports declined from 84.9 per cent in the third quarter to 76.5 per cent in the fourth quarter.

Trade results for 1963 as a whole were, nevertheless, relatively satisfactory. Exports rose by 8.4 per cent as compared with a 6.4 per cent increase registered in 1962. But imports rose even faster, by 11.4 per cent, while they had increased by only 4.7 per cent in 1962. As a result of the fourth quarter deterioration in trade, it is expected that balance of payments results for 1963 will be somewhat less favorable than projected earlier.

Third-quarter balance of payments in substantial surplus

The third-quarter balance of payments results were very favorable as a substantial (fl 292 million) surplus was recorded. In 1962 the third quarter surplus had been a negligible fl 15 million. (See Table 6). Almost the entire 1963 improvement came from substantial gains in earnings on invisibles and a slight reduction in the trade deficit.

Table 6. Netherlands: Balance of Payments 1962 - Third Quarter 1963 ^{1/}
(million Dutch guilders)

	<u>Jan.--Sept.</u>		<u>1963</u> ^{a/}		
	<u>1962</u>	<u>1963</u>	<u>I</u>	<u>II</u>	<u>III</u>
<u>1. Goods and Services</u>					
Merchandise	-1,113	-576	-85	-213	-278
Investment income	162	290	214	-155	231
Other services	<u>1,004</u>	<u>1,038</u>	<u>189</u>	<u>398</u>	<u>451</u>
Total	53	752	318	30	404
<u>2. Private Capital</u>					
Transactions in domestic securities	647	556	198	195	163
Transactions in foreign securities	-261	-125	8	-59	-74
Direct investment	-22	-154	-159	22	-17
Long-term credits	-200	-279	-141	--	-138
Other	<u>42</u>	<u>235</u>	<u>141</u>	<u>41</u>	<u>53</u>
Total	206	233	47	199	-13
<u>3. Commercial Banks Capital</u>					
Long-term	-105	-45	-6	-51	12
Short-term	-90	-301	-304	-76	79
Total	<u>-195</u>	<u>-346</u>	<u>-310</u>	<u>-127</u>	<u>91</u>
<u>4. Official Payments</u>					
Debt repayments	-68	-282	-2	-26	-254
Other	-69	14	-30	-20	64
Total	<u>-137</u>	<u>-268</u>	<u>-32</u>	<u>-46</u>	<u>-190</u>
<u>Surplus or Deficit (-)</u>	<u>-73</u>	<u>371</u>	<u>23</u>	<u>56</u>	<u>292</u>
Financed by:					
Change in IMF position (increase-)	145	--	--	18	-18
Former EPU credits, etc. (receipts-)	17	10	4	1	5
Increase or decrease (+)					
gold stock	-1	-11	-2	-6	-3
foreign exchange, central bank	-244	-356	-50	-277	-29
foreign exchange, commercial banks	<u>156</u>	<u>-14</u>	<u>25</u>	<u>208</u>	<u>-247</u>
Total	<u>73</u>	<u>-371</u>	<u>-23</u>	<u>-56</u>	<u>-292</u>

^{1/} Data are shown on a cash rather than a transactions basis. This affects primarily the current account balance and the commercial banks' capital flows.

a/ Preliminary

SOURCE: Netherlands Ministry of Finance.

Even though the Dutch government made a substantial advance payment on debt owing to the United States the capital balance was only slightly less favorable in 1963 than in the third quarter of 1962. The heavier government payments abroad were partially offset by the receipt of the first installment of fl 90 million from January as part of the German-Dutch Financial Agreement of April 1960 and by an inflow of commercial bank funds.

For the first nine months of 1963, an over-all surplus of fl 371 million was achieved compared with a deficit of fl 73 million for the corresponding period of 1962. The major factor in this improvement was an increase in the current account surplus from fl 53 million to fl 752 million.

Because of the fourth-quarter trade deterioration, the Central Planning Bureau now estimates that the current account surplus for 1963 as a whole will amount to fl 450 million rather than the fl 650 million expected earlier. However, a further inflow of private capital during the fourth quarter, (partly in response to revaluation rumors and partly because commercial banks brought back funds for year-end requirements and to make payments on a government loan floated unexpectedly in November) probably means that the over-all balance for the year was in moderate surplus. Last year, there was a fl 121 million deficit.

Official reserves rise

The favorable balance of payments developments during 1963 are reflected in a rise in the gold and foreign exchange holdings of the Netherlands Bank. For 1963 as a whole official reserves increased by \$156 million. (See Table 7). Gold holdings rose by \$20 million,^{1/} and foreign exchange holdings rose by \$136 million. At the end of the year, official reserves reached almost \$1,900 million with additional drawing rights on the IMF of \$615 million.

^{1/} The press reported that the gold acquired in the fourth quarter represented the Netherlands' share of the gold pool's purchases of Russian gold during the fall months, rather than direct Dutch purchases on their own initiative.

Table 7. Netherlands: Changes in Official Reserve Position
1962 - December 1963

(in millions of U. S. dollars, end of period figures)

	<u>Gold</u>	<u>Foreign Exchange</u>	<u>Total</u>
Dec. 1961 - Dec. 1962	--	28	28
Dec. 1962 - Dec. 1963	20	136	156
Dec. 1962 - March 1963	--	7	7
March 1963 - June 1963	--	88	88
June 1963 - Sept. 1963	--	15	15
Sept. 1963 - Dec. 1963	20	26	46
Dec. 1963 - Jan. 1964	--	-40e	-40e
Actual amounts Jan. 1964	1,601	258e	1,859e

e. Estimate

Source: International Financial Statistics

In January official reserves declined approximately \$40 million. Commercial banks started to put short-term funds abroad again and the speculative inflow of funds halted after the discount rate increase announced in early January.

Demand for guilders moderates

With the end of speculative and seasonal inflows of funds, demand for the guilder became somewhat less active in foreign exchange markets. Guilder quotations, which had been rising steadily since August, reached 27.790 U. S. cents (only 5 basis points under the upper intervention level to which the central bank is committed) on January 6, 1964, the date on which the discount rate increase became effective. Since then, the rate has been declining. (See Table 8). On February 7 the guilder was traded at 27.728 cents, well below the early January level, but still considerably above the par value of 27.624 cents. With the decline in the spot rate, the forward premium on the guilder rose from 0.2 per cent on January 6 to 0.9 per cent on February 7.

Table 8. Netherlands: Exchange Rate in U.S. cents per guilder ^{1/}
July 1963 - February 1964

Par Value	27.624
Lower Limit	27.42
Upper Limit	27.84

		<u>Monthly Average</u>			<u>End of Week</u>
1963	July	27.755	November	22	27.780
	August	27.712		29	27.770
	September	27.721	December	6	27.753
	October	27.749		13	27.763
	November	27.765		20	27.780
	December	27.765		27	27.778
	1964	January	27.753	1964 January	3
				10	27.770
				17	27.743
				24	27.735
				31	27.737
			February	7	27.728

1/ Noon buying rates.

Source: Federal Reserve Board

Satisfactory economic performance for 1963

For the year as a whole the Dutch economy seems to have fared well. For example, the Netherlands was the only Common Market country to register a larger increase in real output in 1963 than in the preceding year: 4 per cent as compared with 2.7 per cent. (See Table 9). Among major economic sectors, only public consumption and exports showed smaller increases in 1963 than in the preceding year.

Table 9. Netherlands: Changes in Gross National Product and Selected Components,
1962 - 1964

(In real terms, per cent change from preceding year)

	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1964</u>
			<u>Estimate A</u>	<u>Estimate B</u>
Private consumption	4.2	5.0	4.5	6.0
Public consumption	6.3	3.0	1.5	1.5
Gross fixed investment	4.2	5.0	a/	7.0
Exports of goods and services	6.6	7.0	.9	5.0
Imports of goods and services	6.6	8.0	.8	8.5
Total GNP	2.7	4.0	5.5	4.5

Estimate A - Central Planning Bureau, September, 1963.

Estimate B - E.E.C., December, 1963

a/ Not available

Source: Miljoenennota 1964; EEC: La Situation Economique de la Communauté,
 December, 1963.

The external position improved, despite a deterioration in the trade balance; the balance of payments moved again into surplus after deficits in 1961 and 1962. However, part of the improvement was due to the fact that the authorities closed the Dutch capital market to foreign issues in 1963, primarily because of budget financing considerations.

Total wages and salaries are estimated to have risen by 10 per cent in 1963 (11 per cent in 1962) according to the EEC. An increase in industrial production of 4 per cent, primarily because of productivity increases, and an increase in the volume of imports of 8 per cent, helped to keep prices from rising much more rapidly than in 1962 despite the strong expansion of demand. Consumer prices rose by about 3 per cent (same as in 1962); however, industrial prices were up 1.5 per cent, after being unchanged in 1962. Prices for services also rose more rapidly than during the preceding year: 4 per cent as over against 3.5 per cent.

Inflationary pressures mounting

Even though the 1963 performance was encouraging, wage and price developments during the second half of the year raised doubts about a smooth continuation of these

trends into 1964.^{1/} The big uncertainties have related to how the substantial wage increases agreed in late October would work out.

The most recent developments confirm these uncertainties. Following the October agreement for increases of 10 per cent in two steps (half of which were allowed to be passed on in price increases), a stream of new labor contracts has been submitted to the Labor Foundation.^{2/} It now appears that the 10 per cent figure is being taken as a minimum from which bargaining is begun. Average increases including fringe benefits, compensation for wage lag in some industries and adjustments in occupational relationships, are running at about 15 per cent rather than the 12 per cent estimated earlier.

Concern about this pace of wage increases is being voiced not only by government officials but also by management and labor representatives. Union leaders apparently are noting, with some surprise, that employers in their wish to hold labor are in no way resisting demands for large increases and some offers are reported to even exceed union demands. The temporary suspension of the Government's tight price policy probably plays a major role in the employers' acquiescence to union demands.

At the same time the Government itself is in a rather difficult position to criticize since wage rises of 10.6 per cent were granted to civil servants (with the assurance that there will be make-up increases if the general wage level should go up by more), 17 per cent to railroad employees and 18.5 per cent to municipal bus drivers.

The major area of concern is the building industry; after the government had announced that building workers should be given exceptional treatment in wage determinations, construction workers asked for increases of 18 - 20 per cent. Negotiations

^{1/} See "Recent Economic Developments in the Netherlands, May - October 1963."

^{2/} See footnote 1, page 13.

were broken off recently because no agreement could be reached on whether the percentage increases would be applied to official wage rates or to the black wage level. A major concern is that, if construction workers succeed in obtaining increases in excess of those granted in other economic sectors, this may lead to a continuation of the practice of the payment of black wages.

Recent wage developments led the Government's Board of Mediators in early January to write a letter to the Labor Foundation^{1/} expressing its concern over these trends. This was followed by a number of discussions between Cabinet Ministers and the Labor Foundation; during those conversations apparently the shift of power to approve wage contracts from the Labor Foundation (temporarily) to the Board of Mediators was considered. On January 31, however, the Government announced the decision not to intervene in the approval powers of the Foundation.

Instead, the authorities stated that, after April 1, the date on which negotiations are slated to be completed, the Government will seek the advice of the Social-Economic Council with regard to its social-economic policy.

At the same time, a series of limited anti-inflationary measures were announced effective February 1:

- a) suspension of investment credit for construction;
- b) suspension of accelerated depreciation allowances for all private industry;
- c) extension by six months (to October 1964) of the 5 per cent cut in government investment expenditures which first became effective in October, 1963;
- d) inclusion of personal loans in the general scheme of credit restrictions;
- e) an increase of 5 per cent in the minimum downpayment for instalment purchases;
- f) abolition of collective fair trade agreements and abolition of certain individual retail price maintenance agreements; and
- g) a bill is being introduced to give the government authority to decree price ceilings for individual firms (in addition to existing authority to establish general price ceilings for individual industries).

^{1/} The Labor Foundation is a non-Governmental body, representing labor and management charged with the review of all wage contracts. For further details see "Recent Economic Developments in the Netherlands, October 1962 - January 1963" dated February 26, 1963, p. 6.

In the meantime, prices at the consumer or retail level have been moving up on a broad front. Increases have been announced for bread, coal, rail fares, hospital rates, milk, sugar, coffee and a number of other items. On the other hand, the Minister of Economics has been successful in achieving a partial roll-back of price increases for a number of goods and services in cases where the authorized 5 per cent increase has been exceeded. However, external factors as well as the internal pressures are making it extremely difficult to hold price increases down to an acceptable level: raw material prices are moving up, agricultural prices are increasing because of agricultural policy decisions taken within the EEC framework, the low Dutch rates may have to be raised under the EEC transportation policy, and the recent increase in communal steel tariffs decreed by the High Authority may increase the cost of steel products.

Discount rate raised last month

In early January, as a further measure within the monetary field, the Netherlands Bank moved to supplement the measures announced in October, 1963 when the ceiling on credit extensions was reimposed. Effective January 6, 1964, the discount rate was raised from 3-1/2 to 4 per cent. The reason given for this move was the fact that the reinstatement of the credit ceiling in October, 1963 had not been sufficient to slow down the rate of credit expansion, since the permissible amount had been exceeded in December. Actually, the discount rate rise followed the upward trends in interest rates which had been apparent since October, 1963. (See Table 10). In November a Government issue at a 4.5 per cent rate had not been successful and a recent issue of the Gas-Union (a part-Government, part-private natural gas corporation) was placed at 5 per cent, as have been industrial bonds for some time now.

Table 10. Netherlands: Selected Interest Rates, July 1963 - February 1964
(per cent per year)

<u>Monthly average</u>		<u>Official Call</u> <u>Money Rate</u>	<u>Three Month</u> <u>Treasury Bill Rate</u>	<u>Government</u> <u>Bond Yield</u>
1963	July	1.92	2.07	4.32
	August	1.06	1.78	4.32
	September	1.24	1.89	4.33
	October	1.11	1.95	4.43
	November	1.14	2.10	4.61
<u>Week ending</u>				
	December 6	1.00	2.25	4.78
	13	1.00	2.25	4.79
	20	2.00	2.25	4.75
	27	3.00	2.25	4.75
1964	January 3	3.00	2.25	4.79
	10	2.00	2.38	4.92
	17	1.25	2.38	4.90
	24	1.25	2.19	4.80
	31	1.75	2.31	4.78
	February 7	1.75	2.31	4.77

Source: Netherlands Bank

At the same time, the Netherlands Bank also announced the extension, through April, of the credit ceiling, which was fixed at 5 per cent above the January - June, 1963 average. Apparently there had been some speculation that the Bank might also increase the required cash reserve ratio (reduced to zero since September, 1963), but this might only induce banks to repatriate some of their considerable funds employed abroad, defeating the Bank's policy to encourage commercial banks to put funds abroad and thus reduce domestic liquidity.

The Central Planning Bureau, which is currently attempting to estimate the effects of the current price and wage developments, is forecasting a considerable deterioration in the Netherlands current account balance: from a surplus of fl 450

million to a deficit of fl 1 billion in 1964. Given the Central Bank's policy of encouragement to commercial banks to put funds abroad, the resulting balance of payments deficit would presumably be financed by a drawing down of official reserves. This would have the effect of curtailing domestic liquidity, in contrast to 1963, when Central Bank purchases of foreign exchange injected a considerable amount into the domestic economy.

An optimistic appraisal of the ability of the Dutch Government to cope with its current economic difficulties is apparent in the latest estimates of the EEC. In these studies, the expected rate of increase in real output for 1964 for Holland is placed at 4.5 per cent, compared with 4 per cent for 1963 and a 1964 estimate prepared by the Dutch Central Planning Bureau before the wage-explosion of 5.5 per cent. As expected, exports are estimated to grow more slowly than in 1963 (5 per cent as compared with 7 per cent), but imports are estimated to grow only fractionally faster than in 1963 (8.5 per cent as compared with 8 per cent). The EEC Commission expects that productivity will continue to grow, perhaps even faster than in 1963, and that the Government's measures will be successful in using available labor more effectively and bringing all available manpower into the labor force.