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Recent Economic Developments in the Netherlands, September-December, 1964

32 pages

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Summary

Towards the end of 1964 it became increasingly clear that earlier indications that the Dutch economy had begun to move towards greater equilibrium were materializing.[1/] Year-end estimates indicate that the economy probably expanded at a somewhat faster rate than anticipated with GNP, in real terms, rising by about 6.5 per cent. As a result of the greater supply elasticity, pressures on the price level (stemming from the 17 per cent wage increase which had to be absorbed during 1964 and the attendant expansion of demand) were translated into price increases no greater, and possibly somewhat more moderate, than expected. Consumer prices, for example, averaged 5.5 per cent above the preceding year's level in 1964, slightly less than the 6 per cent forecast by the Central Planning Bureau at the beginning of the year.

The year 1964 had begun with fears that inflationary pressures developing during the course of the year might prove uncontrollable; but it ended with the Ministry of Economic Affairs being able to state that they anticipated for 1965 "quiet economic development with the vigorous economic upswing under control."

Much of this improvement in the economic situation was owing to external developments. Despite large increases in labor and raw material costs, exports expanded by 17 per cent over their 1963 level,

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1/ See "Recent Economic Developments in the Netherlands, July-September, 1964" dated November 10, 1964.

more than twice as fast than had been anticipated. Dutch exporters apparently kept their prices competitive and probably were helped in doing so by the fact that prices elsewhere in Europe, particularly in Germany, also rose appreciably during the year. The large increase in exports partly offset the upsurge in imports--which increased by 18 per cent--so that the current account deficit for 1964 at less than fl 900 million ($249 million) was fl 350 million ($97 million) below official estimates made as late as September 1964. This basic improvement has led the authorities to believe that the deficit can be reduced to a manageable amount during the course of 1965 and that perhaps by year-end a surplus may re-emerge. However, this would still be some way off the fl 600 - 700 million ($166 - 193 million) current account surplus which the authorities seek to attain as a basis for a sustained rate of balanced growth.

The fact that the Government was able to work out an acceptable compromise in the crucial end-of-year wage negotiations, which once again had threatened the collapse of the existing collective bargaining machinery, was a further ground for the cautious official optimism about prospects for 1965. The agreement concluded will raise contract wages by 5 per cent and is estimated to raise over-all wage costs by around 8 per cent. This is well above the 3 per cent increase originally offered by employers, which was consistent with the official view that inflationary dangers precluded any increase in real wages in 1965; but it also is well below earlier union requests. The agreed figure remains within the 6 - 8 per cent limits which private observers had anticipated and had thought could be tolerated, particularly with the improved external payments position.

Despite inflationary risks, the Government decided to advance the effective date of part of the scheduled tax cut to July 1, 1965. The hope of influencing the wage negotiations, the better-than-expected outturn for 1964 and political pressures contributed to this decision. Accordingly, in early December the Lower House was asked to, and did, approve a bill lowering income and wage taxes by fl 1 billion (annual rate), half of the cut to become effective July 1, 1965 and the other half as soon as possible, but no later than January 1, 1967.

The combined effect of the tax cut and the proposed wage increases will undoubtedly be a stimulus to consumer demand. But aggregate disposable income is expected to rise less in 1965 than in 1964 and price increases will continue to cut into real demand; as a result, the rate of growth in real consumption demand is expected to slow down appreciably. Fixed investment demand also should grow less rapidly than the 15 per cent annual rate achieved in 1964: financing will be more difficult with profit margins caught between wage increases and the Government's policy not to allow them to be passed on as price increases. In addition, the restrictive monetary policy has brought about an appreciable tightening of domestic liquidity and credit availability. Finally, large once-for-all spending in connection with the exploitation of the natural gas deposits is expected to taper off.

On the external side, demand should continue to rise but hardly at the high rate achieved in 1964. Import demand will be cut in the United Kingdom and somewhat lower over-all growth rates are expected elsewhere. On the other hand, imports should also rise at a slower rate particularly with the inventory build-up tapering off. The EEC Commission estimates that, on balance, real demand should rise by 3.5 per cent in 1965 over 1964 as compared with an increase of 6.5 per cent in 1964 over 1963. With the continued tension on the labor market, a faster rate of growth is thought to be unattainable within a stabilization program.

Up to the end of 1964, however, there have been no noticeable effects of the restrictive monetary policies on investment demand. Credit extensions have continually exceeded the limits agreed upon between the banks and the authorities. As a result, banks had to maintain an average of fl 200 million in interest-free penalty deposits with the Netherlands Bank during the last quarter of 1964 and the first six weeks of 1965. From mid-February to mid-March, however, the level of penalty deposits fell back to fl 134 million.

The main effect of the tightening of monetary conditions, thus far, has been an appreciable flow of funds across the international exchanges into the Netherlands during the second half of 1964. Commercial banks repatriated considerable amounts: between the end of 1963 and November, 1964 they reduced their foreign exchange balances by about fl 435 million ($120 million) and increased their foreign short-term liabilities by about an equal amount. In addition, the increase in the Dutch interest rate level has produced a foreign investment flow into Dutch fixed interest securities.

These inflows helped the Dutch capital market to achieve a substantial increase in private activity during 1964. Because of tightening monetary conditions and the restrictions on local authority borrowing, the Dutch capital market remained closed to private foreign borrowers throughout 1964. However, ample funds have been available to maintain the current issue levels of 5-1/2 per cent to 5-3/4 per cent at par; recently, perhaps partly because of seasonal ease, loans floated by the Netherlands Gas Union and the Bank for Dutch Municipalities were heavily oversubscribed. In January, market yields on long-term government bonds were around 5 per cent compared with 4.92 per cent in November, 4.78 per cent in September and 4.83 per cent in January 1964.

Pressures on capacity lessen

Industrial output in the fourth quarter of 1964 appears to have expanded at a somewhat faster rate than during the summer and early fall. On a year-to-year basis, industrial production advanced by over 7 per cent during the last three months of 1964 as compared with an increase of about 6 per cent in the preceding six months. (See Table 1.) Increases in productivity apparently were greater than anticipated and provided a greater elasticity of output in the absence of any easing in the labor situation.

The increases in output per man-hour (estimated at 5 - 6 per cent in 1964 as compared with about 3.5 per cent in 1963) reflect the efforts of Dutch industry to achieve greater efficiency, spurred by the scarcity of labor and increased competition, particularly from Common Market countries, at home and abroad. These efforts have taken

Table 1. Netherlands: Industrial Production, 1963-1964 a/
(Index numbers, 1958=100 and percentage changes)

Year		Index	Percentage change from preceding year	Year		Index	Percentage change from preceding year
1963		139	+4.5	1963	November	153	+7.0
1964 e/		150	+8.0		December	150	+7.1
1963	Jan.-March	132	+1.5	1964	Jan.-March	146	+10.6
	April-June	142	+6.0		April-June	151	+6.3
	July-Sept.	134	+4.7		July-Sept.	142	+6.0
	Oct.-Dec.	151	+6.9		a/Sept.-Dec.	162	+7.3
	September	140	+3.7		September	151	+7.9
	October	149	+6.4		October	163	+9.4
					November	164	+7.2

a/ Adjusted for number of working days; seasonally adjusted data are being revised and are not yet available.
e/ Estimated.
Source: Centraal Bureau voor de Statistiek.

Table 2. Netherlands: Order Backlog, 1962-November 1964
(Orders in terms of months of production, end-January 1963=100)

End of Month	All industries 1/			Consumer goods sector			Investment goods and all others		
	1962	1963	1964	1962	1963	1964	1962	1963	1964
January	109	100	96	106	100	107	110	100	94
March	105	97	100	100	98	108	106	97	98
May	104	98	98	102	104	109	105	97	96
July	101	100	96	100	101	104	101	100	94
September	100	95	96	100	100	104	100	94	94
October	104	96	97	101	103	107	105	95	95
November	103	96	96	105	108	105	102	94	94
December	100	98		101	109		100	96	

1/ Excluding chemical industry.
Source: Centraal Bureau voor de Statistiek.

the form of large increases in investment in labor saving equipment and a continuing trend towards concentration of enterprises. During 1964 about 90 mergers were reported. Two mergers in the banking sector received the greatest public attention; but there were numerous mergers of industrial enterprises attempting to achieve economies of scale and thus to improve their competitive position. Most of these mergers took place in the chemical, metal and textile industries. The latter industry, which has been operating in a situation of stable or falling world market prices and has been facing sharp competition from foreign sources both at home and abroad, is particularly hard pressed to achieve greater efficiency.

The somewhat accelerated growth in output of the past months has outpaced the continuing rise in order inflows. Consequently, order backlogs, according to a survey conducted by the Central Bureau of Statistics, have been reduced towards the end of the year and further reductions were anticipated for the beginning of 1965. (See Table 2.) The reduction in order backlogs was mainly concentrated in the consumer goods industries, while those for investment and other goods remained comparatively stable at about the preceding year's level. Order inflows in general were judged satisfactory by industry, with 80 per cent of the respondents considering their order position to be normal, 10 per cent judged it large and 10 per cent small. This was a slightly less favorable assessment than that given towards the end of 1963, when 15 per cent judged their position to be large and 75 per cent thought it was normal; this change may be an indication of a lessening of pressures on productive capacity.

Labor situation easing?

With the lessening of demand pressures, there appeared some signs that the very tight labor situation may be easing slightly. Unemployment, which (after seasonal adjustment) had been rising fractionally since the first quarter of 1964, moved slightly above the preceding year's level in the fourth quarter of 1964. (See Table 3.) Although job vacancies continued to increase, the ratio of vacancies to number of unemployed was reduced slightly. January (1965) estimates indicate a probable continued movement towards some relaxation of tension. In view of the severity of the labor market tension, however, these indications of easing so far are so slight that they can have little or no effect on the over-all situation. Thus, by the end of 1964, the substantial lessening of labor market tightness--which the Government at the beginning of the year had expected would result from the effects of the large wage increases and the authorities' restrictive credit policy--had not materialized; over-all conditions can be described as little changed from those prevailing at the end of 1963.

Table 3. Netherlands: Labor Market 1963-1964
(in thousands, monthly averages, seasonally adjusted)

		Unemployment	Vacancies	Ratio of Vacancies to Unemployment
1963	I	37	115	3.1
	II	31	121	3.9
	III	30	123	4.1
	IV	28	126	4.5
1964	I	27	128	4.7
	II	28	130	4.6
	III	29	132	4.6
	IV	30	135	4.5

Source: OECD

Wage guidelines set for 1965

The continuing labor shortage and the negative attitude of labor leaders towards the Government's view that inflationary dangers precluded any increase in real wages in 1965 started the crucial year-end wage negotiations off on a rather unpromising note. The unions asked for a 7 per cent increase in contract rates: 2 - 3 per cent to become effective in a general wage round on January 1, 1965 and the remainder on the date of effectiveness of the new contracts (generally also in January 1965). The unions also asked for greater possibilities of wage differentiation between individual firms and for an increase in the minimum weekly wage from fl 100 to fl 110 and equal pay for women; but they dropped earlier demands for a reduction in the 45 hour work-week.

The employers originally offered a 3 per cent wage increase (which would have been more or less compatible with the Government's view of wage increases limited to the expected increase in the general price level), but expressed willingness at first to go beyond this percentage if unions would agree to a maximum percentage and forego any wage differentiation whatsoever. At a later stage, employers indicated that they would be willing to raise their offer more nearly to the 7 per cent level if the Government would relax its price policy. After the Government rejected this proposal, employers virtually withdrew from the negotiations, saying that they would be willing to go along with any settlement the Government found acceptable as they were quite aware that the Government would represent their interests in holding down wage increases to a minimum more forcefully than they themselves could hope to do.

On December 9, 1964, a compromise agreement was finally reached which, although satisfying neither side, proved to be acceptable to both. It provides for:

a) a 5 per cent increase in contract rates;

b) a 10 per cent increase in minimum weekly wages to fl 110;

c) an increase in children's allowances for large families effective July 1, 1965;

d) a mid-year lump sum payment to improve vacation allowances if economic conditions permit; and

e) continuation of present possibilities of wage differentiation between individual firms and between industry branches.

On the basis of this compromise, it was agreed that a general wage increase of 2 per cent would become effective January 1, 1965. The remaining 3 per cent are to be settled with the renewal of individual wage contracts. These have begun to be worked out within the Labor Foundation.[1/] By the end of January, contracts had been approved for the mining and baking industries providing for a 5 per cent increase and an interim agreement was accepted for the important metal industry. The metal industry settlement, which will be operative until a new formal agreement becomes effective in July 1965, provides for a 5 per cent increase plus an industry-wide application of the possible 4 per cent inter-firm differential which had been part of the 1964 contract.

1/ The Labor Foundation is a non-governmental body representing labor and management charged with the approval of individual wage contracts. For a detailed description of the Dutch wage-setting machinery see "Recent Economic Developments in the Netherlands, October 1962-January 1963" dated February 26, 1963, page 6.

The wage settlement thus remains within the 6 - 8 per cent limits which private observers had anticipated and had thought could be tolerated without putting undue pressure on the Dutch cost level.

On basis of the recent agreements, Mr. de Pous, Chairman of the Social and Economic Council, estimated that over-all wage costs would rise by 8 - 9 per cent in 1965 and that the price level would go up by about 5 per cent. The latter percentage would be at the upper limit of the price rise unions said would be acceptable on the basis of the percentage increases of wages agreed upon.

Moderate price rises

With ampler supply availabilities and with foreign competition in home and export markets, price developments have been more moderate than expected earlier. After the initial impact of the wage increases and the temporary relaxation of the Government's price policy had worked themselves out early in 1964, most price series exhibited relative stability through the third quarter of 1964. (See Table 4.) Towards the end of the year there again appeared to be a slightly stronger upward tendency; but this upward movement was very moderate when compared with price developments in neighboring countries.

Consumer prices remained stable throughout the last three quarters of 1964 as price increases for services (the most important of which was a rent increase which became effective in July 1964) were offset by declines in food and clothing prices. Between the end of 1963 and the end of 1964, consumer prices rose by 5.5 per cent or slightly less than the official forecast of 6 per cent.

Table 4. Netherlands: Selected Price and Wage Indicators, 1963-December 1964
(Index numbers, 1958=100, monthly averages and month)

	Hourly Wage Rates	Wholesale Prices	Manufactured Product Prices	Cost of Living	Export Prices	Import Prices
1963						
I	137	100	102	109	100	94
II	138	99	102	111	99	95
III	139	100	103	108	99	96
IV	140	104	105	110	99	96
1964						
I	153	106	108	113	101	99
II	162	107	109	117	102	99
III	165	107	109	116	102	99
IV 1/	165	109	110	117	105	98
October	165	108	110	117	104	98
November	165	109	110	117	105	98
December	n.a.	n.a.	n.a.	117	n.a.	n.a.

1/ Partly estimated.
n.a. Not available.
Source: Centraal Bureau voor de Statistiek; OECD.

Wholesale prices rose by approximately 2 per cent in the fourth quarter of 1964, after having remained stable during the preceding two quarters. The fourth quarter upward pressure came primarily from price increases for foodstuffs and raw materials; manufactured product prices remained at their September level.

The most pronounced tendency for a somewhat faster upward movement was exhibited by export prices. Dutch exporters, through the third quarter of 1964, had managed to keep their price rises below those recorded in the domestic price indexes. But in the fourth quarter export prices rose by 3 per cent, the same rise as in the preceding nine months combined. However, this recent acceleration in the rise of Dutch export prices was paralleled by movements in export prices of competing European countries; thus, it would appear that Dutch exporters are continuing to price as competitively as they did earlier in the year.

Favorable trade returns

The continued competitiveness of Dutch exporters in foreign markets, despite rising labor and raw material costs, is demonstrated by the much-better-than-expected trade returns of recent months. (See Table 5.) During the second half of 1964, a continuing expansion of exports was accompanied by a slowdown in the growth of imports. As a result, the trade gap has been narrowing steadily; the percentage of imports covered by exports has risen from a 1964 second quarter low of 80.3 per cent to 85.2 per cent in the fourth quarter. The 85 per cent level represents about the minimum coverage considered adequate by the authorities for the achievement of a satisfactory payments balance.

Table 5. Netherlands: Merchandise Trade, 1962-1964
(Millions of U.S. dollars, monthly averages, seasonally adjusted)

Year		Exports f.o.b.	Imports c.i.f.	Balance	Exports as % of Imports
1963		414	497	-83	83.3
1964		484	588	-104	82.3
1963					
	I	389	462	- 73	84.2
	II	432	492	- 60	87.8
	III	424	508	- 84	83.5
	IV	420	537	-117	78.2
1964					
	I	453	563	-110	80.5
	II	478	595	-117	80.3
	III	486	585	- 99	83.1
	IV 1/	519	609	- 90	85.2

1/ Estimated.
Source: OECD.

The export results for 1964 as compared with 1963 were very much more satisfactory than had been anticipated: export values rose by 17 per cent and export volumes by 13-14 per cent, or about twice the rate officially estimated at the beginning of the year. Since the increase in the value of imports (18 per cent) was only moderately larger than anticipated, the trade deficit widened considerably less than expected.

Balance of payments in surplus in third quarter

The trend towards a more favorable trade balance and large private capital inflows were the major factors leading to an improvement of over fl 1 billion ($276 million) between the second and third quarters of 1964 in the Dutch balance of payments. (See Table 6.) The third quarter over-all balance showed a surplus for the first time since the end of 1963; in addition, the surplus at fl 563 million ($156 million) was even slightly larger than that recorded in the third quarter of 1963. The cumulative deficit, which in the first half of 1964 had exceeded fl 1 billion, was thus cut back to fl 519 million ($143 million) for the January-September period.

The current account swung from a fl 596 million deficit in the second quarter of 1964 to a small surplus (fl 26 million) in the third quarter. Although the third quarter trade deficit was twice as large as in the preceding year, it was about fl 200 million smaller than in the preceding quarter. In addition, there was the usual seasonal improvement in the investment income account amounting to a swing of fl 425 million. Even with the improvement in the current account

Table 6. Netherlands: Balance of Payments, 1963 to Third Quarter 1964 1/
(in millions of Dutch guilders)

	Jan.-Sept.		1963		1964		
	1963	1964 a/	III	IV	I	II	III a/
Goods and Services							
Merchandise	- 880	-2,373	-339	-389	-792	-898	-683
Investment income	295	350	251	338	195	-135	290
Other services	1,128	1,154	463	430	298	437	419
Total	543	- 869	375	379	-299	-596	26
Private Capital							
Transactions in domestic securities	556	172	163	- 40	- 62	44	190
Transactions in foreign securities	- 125	52	- 74	- 73	- 36	16	72
Direct investment	- 145	- 215	- 8	- 91	-139	- 32	- 44
Long-term credits	- 81	267	-118	- 26	158	67	42
Other	236	65	57	-160	14	- 94	145
Total	441	341	20	-390	- 65	1	405
Commercial Banks Capital							
Long-term	- 51	- 55	6	32	- 18	28	- 65
Short-term	- 294	102	81	165	- 92	18	176
Total	- 345	47	87	197	-110	46	111
Official Payments							
Debt repayments	- 29	- 21	- 1	- 20	- 1	- 20	--
Other	13	- 17	63	- 32	- 8	- 30	21
Total	- 16	- 38	62	- 52	- 9	- 50	21
Surplus or Deficit (-)	623	- 519	544	134	-483	-599	563
Financed by:							
Special transactions							
Debt prepayments	- 253	--	-253	--	--	--	--
Commercial banks							
Foreign exchange, net (increase-)	- 14	816	-247	114	261	495	60
Central bank							
Drawing rights on IMF (increase-)	--	- 163	- 18	--	- 72	--	- 91
Consolidated credits (receipts-)	10	8	5	2	2	2	4
Gold & foreign exchange (increase-)	- 366	- 142	- 31	-250	292	102	-536
Total	- 356	- 297	- 44	-248	223	104	623
Total financing	- 623	519	-544	-134	483	599	-563

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.

balance, the cumulative deficit for January-September 1964 at fl 869 million ($240 million) showed a deterioration of fl 1.4 billion ($390 million) from the position recorded for the corresponding period of 1963.

Private capital transactions were the main factor in producing a substantial surplus of fl 537 million ($148 million) on capital account in the third quarter. Considerable inflows of short-term money (amounting to fl 321 million) and foreign purchases of Dutch securities accounted for the bulk of the inflows. In addition, net sales by Dutch investors of foreign securities amounted to fl 72 million. These sales reportedly consisted mainly of movements out of German fixed interest securities when it had become clear that the German Parliament would pass a bill providing for a withholding tax on income accruing to foreigners from such securities. Government transactions produced a small capital inflow as a second payment of fl 81 million was made by Germany under the terms of the financial agreement of April 1960.

For the first nine months of 1964, private capital inflows amounted to fl 388 million ($107 million) as compared with fl 96 million ($27 million) over the corresponding period of 1963. The major difference arose from commercial banks' short-term transactions, which in 1963 had resulted in substantial outflows and in 1964 resulted in money inflows produced by the tightening of domestic liquidity.

With the improvement in the trade balance, the Finance Ministry recently announced that the 1964 deficit on current account would probably total slightly under fl 900 million ($249 million), which is considerably below the September 1964 official estimate of a fl 1,250 million ($345 million) deficit. Still, this result would represent a deterioration of fl 1.8 billion ($0.5 billion) from the 1963 payments position.

With the inflow of private capital continuing through the fourth quarter of 1964, the over-all balance for the year is estimated to have been in deficit to the approximate amount of fl 350 million ($97 million). This compares with a surplus of fl 757 million ($209 million) recorded in 1963.

Official reserves rise

The third quarter balance of payments surplus was reflected in an increase of $174 million in the foreign exchange holdings of the Netherlands Bank and a $25 million increase in drawing rights on the International Monetary Fund. (See Table 7.) During the fourth quarter, there was a further flow of reserves to the Netherlands Bank, which increased its gold holdings by $87 million and its foreign exchange holdings by $37 million. The IMF position was increased by $17 million as some repayments of guilder drawings partly offset the $40 million made available to the Fund under the General Agreements to Borrow in connection with the United Kingdom's drawing on the Fund.

For the year as a whole, foreign exchange holdings of the Netherlands Bank increased by $98 million, and gold holdings by $87 million. This brought the total official holdings of gold and foreign exchange to $2,084 billion, 81 per cent of which was held in gold, as compared with $1,899 million, 84 per cent of which was held in gold, at the end of 1963. The IMF position increased by $62 million, bringing the total rise in the official reserve position for 1964 to $247 million.

This substantial inflow into official reserves, despite the large balance of payments deficit, reflected the tightening of domestic

Table 7. Netherlands: Changes in Official Reserves
1962-January 1965
(in millions of U.S. dollars, end of period figures)

		Gold	Foreign Exchange	Total	IMF	Total
Annual Change:						
1962		--	28	28	-40	-12
1963		20	136	156	--	156
1964		87	98	185	62	247
Quarterly Change:						
1963	I	--	7	7	--	7
	II	--	88	88	- 5	83
	III	--	15	15	5	20
	IV	20	26	46	--	46
1964	I	--	--66	- 66	20	-46
	II	--	- 47	- 47	--	-47
	III	--	174	174	25	199
	IV	87	37	124	17	141
Monthly Change:						
1964	October	10	- 5	5	-10	- 5
	November	10	94	104	- 7	97
	December	67	- 52	15	34	49
1965	January 1/	--	- 9	- 9	a/	a/

1/ Estimated.
a/ Not available.
Source: International Financial Statistics; Netherlands Bank.

financial markets which caused an appreciable inflow of funds across the international exchanges into the Netherlands. Commercial banks, in response to the restrictive measures of the monetary authorities, repatriated considerable amounts: between the end of 1963 and November 1964 they reduced their foreign exchange assets by about fl 435 million ($120 million) and increased their foreign short-term liabilities by about an equal amount. In addition, the rise in the Dutch interest rate level has attracted a flow of foreign funds into Dutch fixed interest securities.

These developments, added to the seasonal year-end demand, were reflected in a steady strengthening of guilder quotations in foreign exchange markets. (See Table 8.) A further factor, adding to the active demand for guilders, was an intermittent withdrawal of Dutch funds from the London market in connection with the weakness of the pound sterling. As a result of these movements, the Dutch guilder rate rose from 27.772 U.S. cents in October to 27.831 U.S. cents in December. Since then, the rate has remained at around 27.83 U.S. cents, just 0.01 cent below the level at which the Netherlands Bank is committed to intervene.

Financial markets ease

General stringency in Dutch financial markets was eased by the inflow of foreign exchange (which resulted from the swing in the balance of payments), by the continuing reduction in foreign balances of commercial banks and, in December, by a considerable repatriation by Dutch enterprises of maturing investment funds from London which were not reinvested because of doubts about the stability of the pound sterling.

Table 8. Netherlands: Exchange Rate in U.S. Cents per Guilder 1/
January 1964 - February 1965

Par Value	27.624
Lower Limit	27.42
Upper Limit	27.84

Monthly Average

1964	January	27.753
	April	27.711
	July	27.657
	August	27.674
	September	27.712
	October	27.772
	November	27.824
	December	27.831
1965	January	27.827

End of Week

1964	October	16	27.786
		30	27.794
	November	13	27.832
		20	27.832
	December	4	27.832
		18	27.832
		31	27.832
1965	January	15	27.831
		29	27.827
	February	5	27.829

1/ Noon buying rates.
Source: Federal Reserve Board.

Despite the large demands for liquid funds stemming from the general growth in economic activity and year-end seasonal factors, there appeared to be ample supplies. Except for momentary tightness in the second half of November, which forced banks to obtain some expensive funds from the Netherlands Bank, the money market remained unusually easy through year-end. This ease was reflected in the relative stability of call money rates, which remained at around 2 - 2-1/2 per cent throughout December and most of January 1965. (See Table 9.) Banks even increased their holdings of Treasury paper toward the end of the year.

In January, when the reflow of bank notes brought further ease to the money market, the Treasury was able to place additional large amounts of paper at declining rates. Three-months bill rates thus moved down from 3.94 per cent in mid-November to 3.25 per cent in the third week of January 1965.

With the general ease, the Netherlands Bank, by intervening in the forward exchange market, encouraged commercial banks to undertake swaps--i.e., to buy spot dollars and to sell them back forward to the Netherlands Bank--thereby lessening the inflow of spot dollars into Dutch official reserves. Commercial banks are estimated to have availed themselves of this opportunity to very substantial amounts.

But by the end of January money market conditions again tightened somewhat and by February 5, call money was up to 4 per cent and the three-months Treasury bill rate to 3.38 per cent. Part of this tightening may possibly be attributed to the new practice of the

Table 9. Netherlands: Selected Interest Rates, September 1963 - February 1965
(per cent per year)

Monthly Average			Official Call Money Rate	Three Month Treasury Bill Rate	Government Bond Yield
1963	September		1.24	1.89	4.33
	December		1.56	2.25	4.77
1964	January		1.67	2.31	4.83
	June		2.05	3.81	4.87
	September		2.09	3.70	4.78
	October		3.14	3.80	4.84
	November		2.79	3.84	4.92
Week Ending					
	November	6	2.50	3.69	4.93
		13	2.00	3.81	4.92
		20	3.50	3.94	4.92
		27	3.00	3.88	4.92
	December	4	2.00	3.81	4.94
		11	2.00	3.75	4.98
		18	2.50	3.75	4.99
		25	2.00	3.44	5.00
1965	January	1	2.00	3.44	5.00
		8	2.00	3.38	4.93
		15	2.00	3.25	4.98
		23	2.50	3.19	5.03
		30	3.50	3.38	4.98
	February	5	4.00	3.38	4.91

Source: Netherlands Bank.

Treasury in making its payments to the local and communal governments on a monthly rather than a quarterly basis. This would smooth out monthly fluctuations in the money market, but reduce the availability of funds at the end of January, and on the other three quarterly payment dates.

The inflow of funds across the foreign exchanges also added to ease conditions in the Dutch capital market when large demands were made upon it during 1964. Although public authorities reduced their demands upon the capital market somewhat, private borrowing is thought to have increased substantially. Apparently the restrictive monetary policy of the Netherlands Bank so far has had no appreciable effect on the demand for investment funds: capital market funds have been ample, although at higher issue rates, and banks have continually exceeded the limits put on their credit extensions. Consequently, they had to maintain an average of over fl 200 million in interest-free penalty deposits with the Netherlands Bank during the last quarter of 1964 and in January 1965. In February, however, there was an appreciable reduction in the deposits to be maintained, indicating that banks had exceeded their limits by smaller margins than in previous months. For the January-April, 1965 period these limits were fixed at 4 per cent above the January-June, 1963 level.

Because of the tightening of monetary conditions and the restrictions on local authority borrowing, the Dutch capital market remained closed to private foreign borrowers throughout 1964. However, there were successful issues by the European Investment Bank and the Coal and Steel Community of fl 30 million and fl 25 million, respectively, which were welcomed by the Netherlands Bank because they helped to absorb liquidity.

With the recent relative ease in the financial markets, loans floated by the Netherlands Gas Union, with a 5-3/4 per cent coupon at par, and by the Bank for Netherlands Municipalities with a 5-1/2 per cent coupon at par, were highly successful. But it appears that the higher interest rate level reached last year is being maintained despite the somewhat easier tone of the market. Government bond yields remained at around 5 per cent throughout December 1964 and January 1965: they were at 4.78 per cent in September and 4.83 per cent in January 1964.

Further progress towards more stable growth foreseen

With results for 1964 turning out to be much more favorable than expected, particularly on external balance, and with the general wage agreement for 1965 providing for more moderate increases than feared, the Ministry of Economic Affairs was able to anticipate in a year-end assessment for 1965 "quiet economic development with the vigorous economic upswing under control."

The progress made towards greater economic stability, together with some hope perhaps to influence the wage negotiations, and strong political pressures led the Government to decide in December 1964 to advance the effective date of the scheduled income tax cut to July 1, 1965. The Lower House, accordingly, approved a bill lowering income and wage taxes by about fl 1 billion (annual rate) with half the cut becoming effective July 1, 1965 and the other half as soon as economic conditions allowed, but no later than January 1, 1967.

Although the tax cut undoubtedly will add to demand, real consumption demand is expected to grow at an appreciably slower rate than in 1964 (3.5 per cent as compared with 6.5 per cent). Disposable incomes are expected to rise less than in 1964, when the wage bill per worker increased by 17 per cent; furthermore, the price level is expected to continue to rise appreciably, in part because of scheduled administrative price increases such as higher rates for postal, telephone and telegraph services and increases in railroad tariffs, and these price increases will cut into real demand.

Fixed investment demand is also expected to grow much more slowly than in 1964, when an estimated record rate of increase of 15 per cent (in real terms) was achieved. The E.E.C. Commission estimates that the rate of increase will fall back to 3 per cent. Two factors contribute to this reduction: (a) the Government's policies of holding the price line, combined with restricted credit availabilities, will make financing increasingly difficult; and (b) large nonrecurrent investments in connection with the exploitation of the natural gas deposits should taper off.

With growth of both exports and imports also moderating somewhat, the outlook for over-all growth in real demand is for an appreciably slower rate than that achieved in 1964. The EEC Commission estimates that GNP in 1965 will grow by about 3.5 per cent over 1964 as compared with a 6.5 per cent increase in 1964 over 1963. In view of the continued tight labor situation, such a cutback in the rate of growth would appear to be in line with the Ministry of Economic Affairs view that 1965 will show "quiet economic development."

The major problem still remaining is the continued tendency towards labor unrest. The labor unions have been increasingly unhappy with the current system of wage negotiation, in particular with the dominant role conceded to the Government by the employers. The general dissatisfaction has been aggravated by the feeling on labor's part that the Government deliberately presented a more pessimistic picture of the economic situation than necessary in order to exercise moral pressure on the unions during the recent wage negotiations. As a result of the growing discontent, the unions have appointed a special inter-union committee to work out specific recommendations aimed at achieving less centralized bargaining procedures.

APPENDIX

Netherlands: Chronology of Economic and Financial Events - 1964

January 6

Discount rate is raised from 3.5 to 4 per cent; previous change was a cut from 4 to 3.5 per cent on January 8, 1963. Credit ceiling agreement of banks with Netherlands bank which was re-instituted in October 1963, is extended to April 1964, ceiling is set at 5 per cent over January-June 1963 average.

January 9

Banks which have exceeded the credit ceiling have to make interest free penalty deposits of fl 40 million with the Netherlands Bank for excess credit extensions in November, fl 100 million for December, 1963 and about fl 80 million for January 1964.

January 31

Government announces decision not to intervene in the wage contract approval powers of the Labor Foundation (non-Governmental body, representing labor and management, charged with the review of all wage contracts).

February 1

A series of limited anti-inflationary measures become effective:

(a) investment tax credit for construction is suspended

(b) accelerated depreciation allowances for all private industry are suspended

(c) the 5 per cent cut in government investment expenditures which first became effective in October 1963 is extended by six months (to October 1964)

(d) personal loans are included in the general scheme of credit restriction

(e) minimum down payments for instalment credit purchases are increased by 5 per cent

(f) collective fair trade agreements and certain individual retail price maintenance agreements are abolished

(g) a bill is 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)

February 13

The Bank for Netherlands Municipalities launches a fl 100 million 25 year 5 per cent loan at 99 per cent of par. Previous loan was floated September, 1963 for fl 100 million at 99-1/4 with a 4-1/4 per cent coupon and was heavily oversubscribed.

March 1

Railway tariffs for passengers and goods are raised by an average of 6 - 8 per cent.

March 6

Turnover tax on cigarettes and special import duty on gasoline is to be increased. Retail prices of cigarettes and gasoline are to increase by about 25 per cent and 15 per cent, respectively.

March 12

Wage contract for construction industry is signed providing for a 16 per cent increase in contract rates, differential increases of up to 5 per cent for individual firms, productivity bonuses of up to 35 per cent and several fringe benefits.

March 19

A bill is presented to Parliament providing for a rent increase for dwellings built before July 1, 1957 of 10-12-1/2 per cent to be effective July 1, 1964.

April 1

Tax increase on cigarettes and gasoline becomes effective.

April 24

The Labor Foundation approves a 1.3 per cent increase in wage rates to offset the 10-12-1/2 rent increase which is to become effective July 1, 1964.

June 14

Discount rate is increased from 4 to 4.5 per cent after having been increased from 3.5 to 4 per cent on January 6, 1964. The Netherlands Bank stated that this action is prompted by the repeated failure of commercial banks to keep credit expansion within the credit ceiling limitations.

June 5

The Social and Economic Council receives the Government's proposals for social-economic policy for the next two years:

(a) Old age pensions are to be raised from fl 2,754 to fl 3,540 (married couples) effective January 1, 1965. Social insurance premiums are to be increased from 6.8 per cent to 8.7 per cent of incomes, the increase to be equally divided between employers and employees. The Government will absorb part of the additional cost.

(b) Income taxes are to be reduced by about fl 1 billion (annual rate) in two stages, the first to become effective July 1, 1965 and the second on January 1, 1967 at the latest.

June 15

Abolition of all forms of collective resale price maintenance becomes effective. This includes agreements price reductions, trade-ins and profit margins.

July 1

Rent increase of 10-12 per cent for dwellings built before 1957 becomes effective.

July 16

A 25-year 5-1/4 per cent Government loan for fl 200 million issued at 99 per cent of par is not fully subscribed. The effective yield of 5.36 per cent was the highest of any State loan issued since 1924, when a 6 per cent loan was floated at par.

July 24

The Netherlands Bank moves to limit increases in foreign indebtedness of commercial banks. After July 31, 1964 any individual bank may not allow its foreign short-term liabilities to exceed its foreign assets by more than fl 5 million without the express approval of the Netherlands Bank. This measure is designed to prevent banks from financing domestic activities with borrowed foreign funds.

August 21

The Government introduces a bill providing for a tax cut of about 20 per cent in income tax; this would amount to a reduction in the over-all tax burden of approximately 7 per cent. The tax cut is to become effective in two steps on January 1, 1966 and on January 1, 1967; if inflationary pressures ease the date of the first step will be advanced to July 1, 1965. The tax cut is designed to bring the income tax burden down to about the level prevailing in July 1962; it had risen considerably because of the progressive scale.

September 4

The Netherlands Bank announces that the credit expansion permitted for the period September-December, 1964 is set at 5 per cent above the average level in the first half of 1963. During the May-August, 1964 period no credit expansion was allowed.

September 10

The Government introduces a bill providing for an increase in old-age pensions of 20 per cent effective January 1, 1965. The maximum income covered by the scheme is to be raised from fl 10,900 to fl 12,000 per annum. The increase in benefits is to be financed by a Treasury contribution of fl 150 million per annum and an increase in premiums from 6.8 per cent to 9.5 per cent to be paid jointly be employers and employees.

September 11

Individual resale price maintenance is abolished for 5 important categories of consumer durables effective December 1, 1964.

September 15

Budget proposals and macro-economic estimates of the Central Planning Bureau are submitted to Parliament. Budget reiterates necessity for continuation of basically restrictive policies. "Net impulse" emanating from government expenditure is estimated at 3.2 per cent over against an expected increase in nominal national income of 6.5 per cent.

Estimates of Central Planning Bureau foresee a growth of 2.5 per cent in real GNP for 1965 as compared with 1964 (1964 increase currently estimated at 6.5 per cent) under the assumption that wage rates will increase by no more than 2 per cent.

October 15

Government floats a 20-year 5-1/4 per cent loan for fl 200 million at 98.5 per cent of par; this is slightly above market rates and also in excess of Treasury financing requirements for

1964; the flotation of this loan under these terms is interpreted as an effort to absorb liquidity arising from capital inflows into the Netherlands. Substantial foreign interest in the issue was reported.

December 2

The Government amends its tax bill to advance the effective date of the first step of the proposed tax cut to July 1, 1965, the second step to become effective as soon as economic conditions allow, but no later than January 1, 1967. The bill is approved by the Lower House.

December 9

Government proposes a compromise agreement for wage settlements for 1965. It provides for:

(a) a 5 per cent increase in contract rates, 2 per cent effective January 1, 1965 as compensation for the increase in social insurance premiums, the remaining 3 per cent to become effective on contract renewal dates.

(b) a 10 per cent increase in weekly minimum wage to fl 110;

(c) an increase in children's allowances for large families to become effective July 1, 1965;

(d) a mid-year lump sum payment to improve vacation allowances if economic conditions permit;

(e) continuation of present possibilities of wage differentation between individual firms and between branches of industry.

This compromise is accepted by labor and management.

1965

January 3

Railway tariffs for passengers are raised by 6-1/2 - 9-1/2 per cent, for goods by 10 per cent.

January 14

The Netherlands Bank announces that the credit expansion permitted for the period January - April, 1965 is set at 4 per cent above the average level in the first half of 1963.