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

A Look Ahead

At The Year Of Change

by Martin A. Armstrong

If there ever will be the year of all years, 1996 is shaping up to be just that. Virtually every market around the globe from commodities to bonds and stocks is poised to make some sort of very important turning point. Our volatility models are building and the second-half of 1996 appears to be unfolding as if it were an 8.0 earthquake.

In part, 1996 is simply the year from Political Hell. With major elections running from Israel, Europe, Russia, UK, US, Canada, Australia and Japan followed by the Hong Kong turnover in July 1997, there is little doubt that the market will have a lot to worry about. Particularly when you take into consideration the fact that the polls are in favor of the opposition in many cases or at the very least they are going to be a tight race - like in the US.

To make matters even more confusing, it appears as though we are headed to a major turning point in the bond markets with the final stages of Germany being forced into rate cuts. Japan may reach the culmination of a banking crisis as early as March but there is hope that the Great Depression in Japan may also come to an end by May. German, on the other hand, appears poised to slide into the depths of recession as its economic growth turns downward following May.

To add chaos to this mayhem, we will see the beginning of the debt crisis in the second half of the year for Canada and Russia with continued concerns for Belgium, Italy and Sweden. The Russian situation has grown beyond all proportions like a newly formed virus. The debt owed to the West has mushroomed from practically **ZERO** to $85 billion+ and growing. Russia has already failed to make interest payments and the bankers, who never seem to learn, are increasing their loans just so the Russians can make interest payment on what they already owe. Our concern is that a swing back toward a nationalistic party will also greatly raise the risk of Russia defaulting on its debt by 1998.

The key focal point that needs to be watched is May 25th, 1996. This is the next turning point on our Economic Confidence Model. This turning point is the equivalent match to that of the previous 8.6 year business cycle which produced the 1987 Crash. The one thing to be careful of here is a continued rally in the Dow that would take the index up to the 5800-6000 range going into late May. If you see that unfold, run for the hills! A mini-crash cannot be easily discounted at that time. Preferably, we would like to see the market reach a new **LOW** and then consolidate with a broader correction that establishes a **LOW** during the May time period. This type of pattern would speak very well for the future of the US market pointing to a final high in the 7000+ zone for 1998.

We do see the possibility of a minor recession for the US following the May time period that would continue for 6 to 12 months perhaps leading to another turning point in 1997. In any event, 1998 certainly looms on the horizon as the grand old big bang of capital markets. The 1998-2003 time period does **NOT** look to be a lot of fun according to our long-range computer models. The Russian economy will implode leading to a final bottom in 2003 **- AND NOT BEFORE!** The risk of a renewed cold war will never be greater and we cannot discount geopolitical instability either for the 1998-2003 period. We expect these concerns to rise to the surface in both China as well as Russia.

The bond markets are in the final stages of a rather unique event - a market induced inverted yield curve! Most people believe that an inverted yield curve is something that is created solely by the central bank to fight inflation. However, the Fed, as well as all central banks, have been circumvented by their ruling political leaders. Bill Clinton began this trend when he cut the 30 year bond auctions in half and shifted the funding of the national debt to 33% 1 year or less. This debt shift took place when short-term rates where half that of long-term. This savings in interest expenditures was what attracted Clinton and enabled him to claim that he reduced the deficit by $500 billion - the biggest cut in history. What really happened was that Clinton added a new tax bracket to raise $250 billion in revenue and the debt shift from long to short-term saved $50 billion annually. Over 5 years, the interest savings projected by Clinton was therefore $250 billion. Adding this to the tax increase and you came up to the $500 billion number. Of course, not one cent of spending was actually reduced.

The Clinton debt sham was then used by most countries. The result is that our politicians have just made the same mistake that the Japanese did when they were buying up all the real estate and funding long-term purchases with short-term money. The inverted yield curve that developed by default in Japan was astonishing - almost a 5% move in one year. The market place is already creating the same effect worldwide. In the US, 2 through 10 year paper is trading below Fed Funds Rate. The Fed will undoubtedly cut the rate, but still the marketplace has long-term rates falling faster than short-term. We suspect that after May, long-term rates will rise, but not nearly as fast as short- term. Look for a market induced inverted yield curve doing to government exactly the same thing it did to the Japanese investors. Eventually, government deficits could rise far faster than they have at anytime in the past since the national debts are much more sensitive to short-term changes in interest rates today.

Amid all this chaos will be the drive for tax reform in the US. The flat tax is something that appears to be headed toward a slow death. Of course Steve Forbes has built his whole strategy upon the flat tax, but even Jack Kemp will fall victim to this trend. The long awaited Kemp Commission on tax reform will release its findings January 9th. Our sources say that Kemp has backed away from the flat tax and the report will end up to be more of a review of why we need tax reform without strongly endorsing the flat tax. This miracle of miracles was accomplished by Dole twisting Kemp's arm to back-off. What is gaining rather significant momentum is the retail sales tax and the repeal of the 16th Amendment. Depending upon the primaries, there should be some big bucks coming out in advertising to push Dole in that direction. Dole himself will swing in the direction of the polls since he is not very committed one way or the other.

1996 Global Capital Market Conference

April 18-19th Princeton, New Jersey

Keynote Speaker Lady Thatcher

Come join us for one of the most important conferences ever held. Our list of guest speakers will include some of the most important political leaders that will help shed some light upon what we see as the driving forces behind capital and the geopolitical future that lies ahead for all of us going into the next century.

Thursday, April 18th will be a solid day of reviewing our forecasts for the future as we approach the next turning point on our Economic Confidence Model. Friday, we will have special technical training sessions for those who would like to continue their education process of understanding market behaviour. Friday night, we will have a banquet with Lady Thatcher delivering her view of our geopolitical future. Other guests will include William Kristol, former Chief of Staff and driving force behind the Contract With America, Steve Moore of the Cato Institute and more.

Seats are $295.00 reservations mandatory

In the final analysis, 1996 is indeed shaping up to be a year that will not be soon forgotten. It may even prove to be the year where gold and silver at last complete their reaction lows and begin a new age of a bull market into 1998. Look for a low for these two slackers in Feb/Mar of May/June followed by a nice rally during the second-half of the year.

Russian Dec 17th Elections

Brief on the State of Russian Parliamentary Elections for the lower house Duma to be Contested 12-17-95

by Dana Schneider

The Russian Parliamentary elections are less than two weeks away. Already, optimistic speculation as to the direction of the elections has given way to the reality that Russia's hard fought reforms may be stopped short of affecting substantial long-term results. Evidence of the reformers losing ground in the current Parliament is visible and the likelihood that they will lose even more ground with the elections on December 17 is inevitable.

Opinion polls show the public leaning more and more toward "reformed" communists and nationalists. Already back in August, the Financial Times summed up the situation that has become progressively worse as the elections near. Of 1,943 Russians polled, nearly one-third said they would *not both*er voting, another one-third was *undecided*, and the remaining one-third voiced their support for 14 different political groups. Currently, there are some 43 different groups contesting approximately 450 seats. To complicate matters, 5% of the vote is needed in order for a party to occupy a seat in the Parliament. Questions and accusations abound as to the validity of the 200,000 signatures required by each party to contest the elections, campaign finance violations, access to polling booths, and widespread corruption of party and government officials. Worse still, the possibility of having the elections made null and void and subject to judicial review is growing.

While the lower house - State Duma - is legally obliged to hold elections in December, the fate of the upper house - Federation Council - is not so sure. The Federation Council was appointed by President Boris Yeltsin after his election without provisions being made for re-elections. Currently, the Council's legislative session is slated to expire on December 12 leaving it to be disbanded or continued by Presidential decree. Earlier in November, the Duma passed legislation calling for regional representative elections for the upper house but that was rejected by the Federation Council along with Yeltsin's backing. Delaying and/or keeping the Parliament insolvent would be a great advantage to the presidential hopefuls for next June's elections. Keep in mind that this is the first time that Russia has attempted to sequentially hold a free second national election - ever. There have been first elections but every time they have remained just that.

It is unlikely that President Boris Yeltsin and the remaining reformers of his administration will be able to influence the direction of the national election. President Yeltsin has persistently received single digit approval ratings and has missed many PR opportunities while recovering from the second bout of heart failure in four months. Anatoly Chubais, the engineer of Yeltsin's budget and the First Vice Premier, has taken heated attacks from the communists and nationalist for the social crisis and economic hardships so visible today. The loss of Chubais' power to pressure reform was evidenced when Parliament forced the return of 4.5 trillion rubles ($1 billion) to the budget as a condition for passage after 3 previous failures. The additional money is to be used for pensioners, subsidies to state industry and social programs, as well as to the agricultural and military sectors. These budgetary categories lie at the heart of the Communists and Nationalists constituency. The first budget to be in place by the new year since the breakup of the Soviet Union is in jeopardy since only 11 votes secured its simple majority passage. The foundation for apathy and desire for a communist/nationalist parliamentary rule is steadfastly in place.

The signs are there that Russia is in for economic and political instability on the level it experienced in the attempted August 1991 coup and possibly worse. Political pressure and corrupt lobbying groups succeeded in pressuring the Elections and Campaign Committee in annulling the validity of one of Russia's most popular reform parties-Yabloko - to contest the elections. However, with some maneuvering, the Constitutional Court surprised many participants by overturning that decision. Yabloko will be allowed to compete and it is not expected that the committee will appeal the ruling. Meanwhile, the Federation Council Chairman, Vladimir Shumeiko, has launched a political party that is based on Russians "different genetic make-up, arising from our Orthodox past." His party is planning to contest the Presidential elections in June. Considering the declining influence the reformers and centrists have been able to exercise in the current Parliament where they occupy nearly 48% of the vote, the likelihood that next Parliament will move at all toward expanded reform is unlikely.

Another sign that the reformers are losing was seen with the the current Parliament's unwillingness to confirm Yeltsin's appointee to head the Central Bank - Tatayana Paramonova. Paramonova is credited with creating the ruble trading band, slowing down the growth of money supply to below 3%, stabilizing inflation around 6.7 percent , and establishing stricter rules to govern banking exchange, lending and ruble-denominated reserve requirements. The banking crisis witnessed in mid-summer was the weeding out of the weaker institutions that survived by feeding off interest and exchange rate volatility. Paramonova viewed this as necessary in order to get on the path of economic stability and growth as well as a means of promoting banking/financing legitimacy. The State Duma passed legislation requiring banks to allocate 3 percent of their liabilities for a general deposit insurance fund, further inhibiting profits of speculative bankers.

The policies that were put in place were vital to the restructuring of Russia's debt with international creditors and well as securing loans from the IMF and the World Bank. At risk is a tentative 3-year loan of up to $18 billion contingent upon a 1.2 percent inflation projection by the government (which was compromised to 1.9 percent in order to pass the budget through the Duma). Unfortunately, Paramonova has been replaced by Sergei Dubinin who is not known for tight monetary policies or sympathy with the reformers. His interests lie in placating the demands of the communists and nationalists to continue subsidies while at the same time satisfying the big banking and natural resource interests. As of the week of December 6th, the ruble trading range of 4,300 to 4,900 to the US. dollar was eased to 4,550 to 5,150 for the first half of next year and the refinancing rate for loans to commercial banks was cut from 170% to 160%. At the same time, the government is planning to go ahead with its dubious loans-for-shares privatization program in which several of Russia's largest banks will bid to make loans to the government in exchange for a high percentage share of stocks in some of the nation's most vital and valuable natural resource industries.

This scenario does not bode well for Russia or investors. For those who have invested in Russia, they may soon find import tariffs rising as dramatically as the value added taxes and bureaucratic licensing fees. The agreements for developing new office space or renovating an old hotel may be shelved. The stock that you just bought on the assurances of the recently inaugurated Exchange and Securities Commissions will somehow be lost on the books and the Russian debt you just financed with the go-ahead from the IMF, World Bank and London Club may have to undergo entirely new negotiations after the elections. If the elections shake investor confidence, it could deliver a serious economic blow to Russia whose restructured debt agreements rely on funding 37% of its $19.2 (3.8% of the GDP) billion budget deficit through international capital markets in 1996. On the other hand, investors may be encouraged by the fact that companies in which the State owns less than 25% of the shares increased output by 2.3% while state-owned industries continued to decline by an average of 12%. Employees in non-state plants enjoyed a 9.8% increase in wage while their state-employed counterparts suffered a 6.6% wage decrease in real terms. These figures were published in Izvestiya at the end of November via the Russian Marketing Association from results of a survey of 300 companies in 13 regions considering 8 sectors of production. As bankers are being poisoned and "small" hand-made time bombs explode in the office of a member of the lower house of Parliament, one cannot be overly cautious.

by Harold Ludwig

UNITED STATES

HOME SALES: Sales of existing homes in the US fell for the first time in six months in October despite lower mortgage rates, according to the National Association of Realtors. Sales fell 1.9% to a seasonally adjusted annual rate of 4.07 million in September. The last monthly decline in sales was in April, which saw a sharp fall of 6%. The drop occurred even though average rates for 30-year mortgages eased down to 7.48% in October, from 7.64% in September. October rates were below last year's 8.93% average.

HOUSING STARTS: The Commerce Department said housing starts fell 2.7% in October to a seasonally adjusted annual rate of 1.34 million, the lowest levels since June. For the year to date, starts are down 8% from the same period last year.

The decline in housing starts was concentrated in the mid-west where starts fell 8.9% in October. However building permits - a guide to future construction trends - rose 5% in the region, indicating softness in starts may be short-lived.

PURCHASING MANAGERS" INDEX: Purchasing manages reported an unexpected decline in their index of manufacturing activity to 46.8% against 48.3% in September, well below the 50% threshold for expansion in the sector.

The purchasing index has moved up and down erratically since the spring, but has generally been much weaker than last year. The index has been below the 50% threshold for growth in five of the past six months , reflecting manufacturers' efforts to curb production and reduce excessive levels of inventories.

LEADING INDICATORS: The official index of leading indicators - designed to provide advance warning of recessions - was reported down 0.1% in September. The drop reflected falls in commodity prices, consumer sentiment, and higher claims for unemployment insurance. It followed a revised increase of 0.1% in August band a decline of 0.2% in July.

"BEIGE BOOK": The Federal Reserve published an assessment of lackluster growth prospects in its latest "beige book" on regional economic trends. It said retail sales were soft and below expectations in may area in October.

The beige book indicated the economy was still growing at a "moderate" pace, but probably slower than during the summer. Consumer spending reports indicated a "possible slowing of demand." However, it noted an offsetting pickup in exports and demand for some business equipment

CONSUMER CONFIDENCE: The Conference Board, a New York business analysis group, said its confidence index rose to 101.4% against 96.3% in October. Readings above 100 have historically been associated with vigorous economic growth.

The consumer confidence survey indicated that US consumers expected economic conditions to improve following a pause in growth earlier this year: the proportion saying business conditions looked good rose to nearly 27% from 24% in September.

TRADE DEFICIT: The US trade deficit was lower than expected for the second month running in September, reflecting sluggish domestic demand. The Commerce Department said the deficit fell to $8.3 billion against Wall Street expectations of a shortfall of about $9.5 billion. Figures for August were revised down to show a deficit of $8.4 billion, rather than $8.8 billion as previously reported.

The bilateral deficit with Japan fell from $5.1 billion to $4.3 billion, its lowest level in more than two years. The decline in the overall deficit from a monthly average this year of about $10 billion partly reflected corporate efforts to bring inventories of unsold goods into line with likely consumer demand. The "inventory correction" has helped to improve the trade figures because many capital goods are imported.

Exports rose 1.6% between August and September to $67.2 billion, more than offsetting a 1.4% increase in imports to $67.2 billion. Exports were 10.3% higher than in September last year. Imports were up 8.6% over the same period. The deficit for the first nine months was $90 billion against $78.7 billion for the same period last year. A deficit of $136.8 billion in goods was partially offset by a $46.8 billion surplus in services.

INDUSTRIAL PRODUCTION: US industrial production fell in October, providing fresh evidence that economic growth is slowing. The Federal Reserve said output dropped .3% in its first decline in six months. The fall partly reflected a strike at Boeing, the aircraft maker, which cut factory output by about 0.2%. But even allowing for the strike, most sectors were down or flat.

Industrial production showed across-the-board weakness last month. Output of consumer goods, business equipment and construction supplies were down 0.5%, 0.8%, and 0.6% respectively. The rate of industrial capacity utilization fell sharply to 83.6% from a revised 84.1% in September, indicating little risk of factory sector pressures on prices.

CONSUMER PRICES: The Labour Department released figures showing an unexpected upward move in inflation in October. Consumer prices rose 0.3% from September and by 2.8% on an annual basis. The 0.3% rise in consumer prices reflected larger than expected increases in the cost of housing, energy and clothing. Excluding food and energy, the "core" consumer price index also rose by 0.3%, following a string of moderate 0.2% increases.

RETAIL SALES: The Commerce Department said retail sales fell 0.2% in October, following a revised 0.1% gain in September. Wall Street expected sales would decline by about 0.1%. The sluggish retail spending has raised doubts about the strength of the Christmas sales season.

Sales of cars rose 0.7% in October, following a dip in September. But nearly all other sectors were weak. Sales of building materials fell 0.4% from September in spite of an upturn in the housing market. Sales of clothing fell 2.4% from September. Excluding cars, overall sales were down 0.5%.

CONSUMER CONFIDENCE: According to a report from the Conference Board, a New York business analysis group, US consumer confidence remain "reassuringly strong". Its confidence index fell slightly to 97 in October against 97.3% i September. However the index was eight points higher than in the same period last year when the economy was growing robustly.

Separate data indicated employment costs remain unusually subdued. The employment cost index - a broad measure including fringe benefits as well as wages - rose 0.6% in the third quarter. The annual increase of 2.6% was one of the lowest on record.

GDP: Gross Domestic product pointed to growth but at a more moderate pace than in the third quarter. GDP grew at an annualized rate of 4.2%.

GERMANY

MONEY SUPPLY: The Bundesbank said money supply growth in October remained well below the target range and bank lending had weakened. M3 rose at an annualized rate of 1.8% against 1.6% in September. The 1995 target range is 4-6%.

INFLATION: The cost of living in western Germany held unchanged between October and November, largely as a result of falling prices for imports, according to the Federal Statistics Office. Preliminary figures, based on returns from four states, showed that the annual rate of inflation fell to 1.5% in November from 1.6% in October and September. Western Germany's year-on-year inflation rate last touched 1.5% in August. Imported goods prices in October were 0.2% below those of October of last year after modest year-on-year increases of 0.5% in September and August respectively.

GERMAN GROWTH: The DIHT, the Bonn based umbrella organization for Germany's chambers of industry and commerce, said that its latest half yearly survey of companies and industry, construction and services had uncovered growing skepticism and uncertainty about economic prospects. Weak business investment will condemn Germany to slower growth and rising unemployment next year, according to the survey of 25,000 companies.

The poll, which covered companies employing about half the labor force, is the most comprehensive carried out on a regular basis in Germany. It reported a sharp increase in the number of businesses planning to reduce staff, with the share of companies planning to cut employment in the next 12 months exceeding the number planning to take on staff by 23 percentage points.

Although the survey did not point to a recession next year, the chambers expect growth to slow to 2% in 1996 from the 2.5% now forecast by the government for 1995. Although export growth would continue to support activity, it would slow, largely as a result of the D-Mark's strength.

UNEMPLOYMENT: Figures from the federal labor office showed the jobless total increased by 4,800 in October to 3,525,800, and was 78,500 higher than at the end of last October. However, Germany's unemployment rates stayed unchanged. The all-German jobless rate was 9.2% of the labor force at the end of October, with unemployment in western Germany at 8.1% and in eastern Germany at 13.8%

Unemployment rose in October on a seasonally adjusted basis for the third month in succession. However, the rise of 4,000 was lower than the 44,000 increase reported in September and August's 26,000 rise.

The German government promised to draw up a comprehensive program to boost growth and employment for presentation in January next year. The economics minister, Mr. Gunter Rexrodt, said unemployment was the biggest challenge facing the government. In contrast to previous periods of economic growth, there had been no improvement in the German labor market in the 2 1/2 years since the economy started to recover from a recession. The government is expected to seek ways of reducing the cost of labor in Germany by attacking non-wage labor costs such as social security contributions.

SHOPS TO OPEN FOR LONGER: The German government agreed to let shops open until 8pm on weekdays and 4pm on Saturdays, marking a victory for consumers by some of the world's most restrictive shopping hours. At present, under a 1956 law, German shops must close at 6:30pm on weekdays, other than on Thursdays, when they can stay open till 8:30pm. Closing time on Saturdays is 2pm, with longer opening on the first Saturday of each month.

The issue has been hotly debated for years and drew criticism from the HBV union, which claims to represent 300,00 retail workers. The HBV union says the result will be fewer jobs with less protection and more pressure to perform.

The Economics minister, Mr. Gunter Rexrodt, who has been pushing for the liberalization of shopping hours, described the agreement as a "giant step forward". The agreement is expected to come into force in the second half of next year.

MONEY SUPPLY: German M3 money supply grew at an annualized rate of 1.6% in September and at a non-annualized rate of 1.6% from the fourth quarter of 1994, according to the Bundesbank. Provisional September figures released in October had shown 1.5% and 1.3% respectively.

INDUSTRIAL ORDERS: New orders for German industry rose in volume terms by a seasonally adjusted 0.2% in September compared with August, providing a further indication that economic growth is slowing. The Economics Ministry said orders for manufacturers in western Germany rose by 1.6%, partly reversing a fall in August of 4%. Foreign demand for west German goods rose 3.1% in September, while domestic orders rose by only 0.8%. In eastern Germany, new orders fell in September by 13.2% in reaction to an exceptional 22.8% jump in August when a number of large contracts were agreed. Taking the most recent two months together, pan- German orders declined by 1.5% compared with June and July and were 3.9% lower than in August and September last year.

UNITED KINGDOM

PURCHASING MANAGER'S INDEX: Britain's manufacturers shed more jobs than they created for the first time in more than two years in October, according to the latest survey of purchasing managers.

The purchasing managers' index, which tracks business activity in manufacturing, rose slightly in October, but pointed to continued slow growth of factory output. The survey also revealed a further weakening of upward pressure on prices as demand for goods continued to decline and companies found it easier to meet that demand. Prices of raw materials and other inputs rose in October at the slowest rate since November 1993.

TRADE DEFICIT: Britain recorded its biggest underlying monthly trade deficit so far this year in August. The headline visible trade gap rose by BP120 million to BP1.265 billion, according to the Central Statistical Office. Imports rose by 2% in August and exports rose by 1%.

GROWTH FIGURES: The Central Statistical Office said the economy, excluding oil and gas extraction, grew by only a seasonally adjusted 0.3% between the second and third quarters of this year. This is the lowest quarterly rate of growth since the final three months of 1992 and down from the original estimates of 0.5% growth in the third quarter.

Weakness in the building industry accounted for most of the downward revision in GDP; construction industry output fell by 1.4% between the second and third quarters.

New home loans made by building societies reached their lowest level for more than 15 years while mortgage lending by banks, whose market share has been increasing, also fell.

CONSUMER CONFIDENCE: A survey, conducted by the research group GfK for the European Commission suggests their has been barely any change in consumer sentiment over the past six months.

Comparing this confidence level with earlier periods is difficult because GfK took over running the survey (previously conducted by market research organization Gallup) in the summer, resulting in a break in the data. But rough comparisons suggests that confidence is better than it was during much of last year - albeit still down from the levels of previous recoveries.

Slightly more of the 2,000-odd households surveyed in November expect their financial situation to deteriorate over the next year or more. 56% of the households believe their finances will remain unchanged - the same proportion as in October. However, 16% expect them to get a little worse - the highest proportion for six months.

The proportion of households expecting to make a major purchase has also deteriorated slightly - 32% of people think now is a bad time to buy a large item, the highest level for six months.

The amount of money people plan to spend over the next 12 months has barely changed, with only 12% anticipating higher expenditure.

LIVING STANDARDS: Average earnings rose by an underlying 3.25% in the year to September, according to the CSO. Over that period, the average household needed a 4.3% rise in income simply to compensate for the higher prices and taxes. The resulting drop in real average earnings was the largest since March 1982.

UK BUDGET: Mr. John Major's government sought to revive its fortunes with a Budget proposing a modest ($4.8 billion) cut in taxes, paid for in planned public spending.

The centerpiece of the budget, presented by Mr. Kenneth Clarkie, chancellor of the Exchequer, was a widely expected cut in the basic rate of income tax from 25 to 24%, the first reduction since 1988. Mr. Clark also announced changes to allowances and thresholds which will reduce the numbers of people paying income tax at all and those paying at the higher 40% rate.

Mr. Clarke's other giveaways included a cut in tax on savings income, a series of tax cuts for businesses and measures to help people cope with the cost of long-term care in their old age. He also increased the threshold at which people have to pay inheritance tax by a third.

Mr. Clarke paid for these tax cuts by reducing the planned "control total" for the bulk of government spending next year by BP3.2 billion to BP260.2 billion.

NON-EU TRADE GAP: Britain's trade deficit with countries outside the EU deteriorated sharply in October to its widest level since records began more than seven years ago, according to official figures. The CSO blamed record levels of imports and a sharp fall in exports as activity in some of the UK's main trading partners remained weak. The surge in exports to North America, which caused a narrowing of the deficit in September, was reversed in October. Exports to North America fell by 12% in October.

The value of exports was BP5.3 billion in October, a fall of 7% from September. This was due to a fall i exports of oil, precious stones, cars and capital goods, according to the CSO. Imports, on the other hand, were a record BP6.5 billion, 1.5% more than the previous month.

The Treasury said, however, that the upward trend in exports was continuing. In the three months to October exports rose 4.5%, while imports rose 7.5%. Officials said the growth in imports was due largely to semi-manufactured and capital goods rather than consumer goods, which suggested that companies were importing goods to increase their investment.

MANUFACTURING INVESTMENT: Manufacturing investment in the third quarter of the year was the highest for more than 4 years, according to official figures. But the rise in manufacturer's unsold stocks in the third quarter was the largest for almost 19 years. Unexpected heavy stockpiling of computers in the run up to Christmas and a rise in the amount of finished goods held by the chemicals industry were mainly responsible for the rise. Manufacturing investment was 2% higher in the third quarter than in the second quarter of the year and 12% higher on a year earlier.

MANUFACTURER'S COSTS: Manufacturers' fuel and raw material costs fell back in October for the first time since January 1994, providing strong evidence that inflationary pressures are easing. The decline in industrial input costs was coupled with signs that manufacturers have also begun to rein in price rises at the factory gate - the annual rate of increase in the cost of basic goods declined in October for the first time since June 1994.

The figures were also in line with recent business survey evidence which had pointed to moderating price pressures in industry. The CSO said the cost of raw materials and fuels purchased by industry fell by a seasonally adjusted 0.3% in October. On a seasonally adjusted basis, the cost of raw material and fuels fell by 0.7% in October. The decline reflected falls in the prices of crude oil and imported metals and chemicals, the CSO said.

FACTORY OUTPUT: Manufacturing output fell by 0.6% in September, the largest one-month fall since January, said the CSO The data conflicted with City of London expectations of further slow growth in manufacturing. Economists had expected output to grow by 0.2% in September.

The CSO believes factory output is now rising by only 1/2 per cent on an underlying basis. This is the lowest growth rate for almost three years, down from a peak of 5.5% last autumn.

But a rebound in North Sea oil and gas extraction and a rise in energy output meant that industrial production overall grew by 0.5% in September despite the drop in manufacturing.

The Treasury said the industrial production figure was close to the CSO's original forecasts, so it would probably not revise down its original estimate of 0.5% growth in total gross domestic product in the third quarter of the year.

CAR SALES: Registrations of new cars rose sharply in Britain in October for the first time this year. Statistics from the Society of Motor Manufacturers and Traders showed that registrations of new cars totalled 136,605 in October, arise of 11.5% on October last year.

This lifted registrations for the first 10 months of this year to 1,730,771, up 1.16% on the comparable period of 1994. Even if the improvement were sustained in the final two months of the year, it is likely that 1995's total would still fall short about 50,000 cars short of the million which the industry had been hoping this time last year.

Imports took a 57.48% share of October's market, up from the previous October's 56.77%. Their share for the first 10 months reached 59.62 % compared with 57.39% at the same time a year ago.

JAPAN

TRADE SURPLUS: Japan's trade surplus registered one of its sharpest ever monthly falls i October, the strongest evidence that the country's chronic external surpluses have at last begun to shrink.

The customs cleared surplus fell by 42.4% in October from a year earlier to a seasonally adjusted $4.8 billion, helped lower by a surge in imports, which grew by 17.8%. The decline was the largest since April 1990, excluding a 51% fall in January this year - an exceptional figure caused by the disruption of the Kobe earthquake. Exports crept up by just 1.7% with a sharp fall in sales to the US and Europe offset by a continuing strong demand in Asia.

The main reason for the fall was a sharp rise in the value of the yen in the two years to this April, when the currency rose in value by more than 25%, raising the prices of exports and making imports cheaper.

A big increase in car imports from the US was one of the principle factors in October's steep fall. The Japanese bought 122% more imported vehicles from the US in October than in the same month a year earlier. There were also big increases in purchases of semiconductors and computers. Overall, imports from the US grew 21.4%.

At the same time, weakening demand in North America depressed Japanese exports there. Car sales dropped by 22%, producing an overall drop in exports to the US in volume terms of 14.7%. Japan's total trade surplus with the US fell by 44.2% to $2.7 billion.

ECONOMIC RECOVERY WEAK: Japan's economy remained weak in the five months to September, but recovery is expected early next year. The latest leading indicator issued by the Economic Planning Agency, pointed to business conditions in the near future, stood at 36.4 in September, having languished below 50, the dividing line between growth and decline since May.

However, Mr. Isamu Miyazaki, the EPA's director General, said he could detect signs of business recovery, such as a rise in corporate investment and public spending, partly in response to the Y14,220 billion fiscal stimulus package adopted by the government in late September.

The leading indicator, a basket of 11 indices, showed a slight pickup from 33.3 in August. Of its components, four showed an improvement, most notably housing starts. Among the other seven, stocks of unsold goods rose slightly, a reminder of Japan's overcapacity, while sales of consumer durables declined. The labor market also weakened.

MACHINERY ORDERS: The EPA reported that Japanese companies spent less on machinery from August to September, but that the three month trend continues to rise.

Machinery orders fell by 3.9% to Y903.6 billion from August to September, or by 0.9% by comparison with September of last year. However this indicator tends to be volatile. Taken over the three months to September, a better guide to the trend, Japanese companies spent 2.4% more on machinery than the same period in 1994.

BAD BANK LOANS: According to Japan's finance ministry, Japanese banks' problem loans totalled Y37,390 billion at the end of September, more than 5% of their total lending. The figure represents the most detailed yet of the bad debt problem at Japanese banks.

The report showed that after subtracting loan loss provisions and the likely value of collateral, total bad loans at present provided for was Y18,290 billion, a figure equal to nearly four times banks' recent average annual operating profits.

Among the various categories of financial institutions, the trust banks were revealed to have the biggest problems. Over 11% of their total loans are now designated Non-performing. For leading commercial banks, the figure is just under 5%.

ORGANIZATION TO RESCUE BANKS: Japan is to set up a special organization to rescue the country's collapsing banks, according to the finance ministry. The body is to modelled on the US Resolution Trust Corporation which disposed of bankrupt savings and loans institutions in the early 1990's, will take over the operations of banks that fail within the next five years.

The decision was prompted by the discovery of far greater losses than previously estimated at one of the institutions that has already collapsed this year.

HIGH CORPORATE TAXES: Mr. Tomichi Murayama, the Japanese prime minister said that the country's high corporate taxes were hindering its economic recovery. Mr. Murayama said the three party coalition government would make a policy decision on its response to mounting business pressure for a cut in corporate tax by the end of the year. Mr. Murayama was replying to a list of demands for tax cuts and further economic deregulation presented by Japan's four leading lobby groups. They called for cuts in land and income taxes and more aggressive economic deregulation than achieved so far.

A tax commission panel has been considering an overhaul of the entire tax system, the first since 1988, for the past year and the process faces intricate political and financial difficulties.

Japanese corporate taxes average nearly 50%, nearly 10 percentage points higher than the US but slightly lower than Germany's 52%, according to the finance ministry.

UNEMPLOYMENT: Japan's unemployment rate remained at the record high of 3.2% in September, according to the government. The jobless rate coincides with the weakest labor market in 9 years. The number of jobs available per 100 workers fell from 61 in August to 60 in September, the worst since 1986. Previous falls have warned of a rise in unemployment.

Employment overall rose by 0.7%, or 450,000 jobs, to 65.3 million in the year to September. The number of people seeking work grew much faster, so the total unemployed rose by 9%, or 180,000 people to a six month high of 2.2 million, the management and coordination agency said. Manufacturers shed jobs through early retirement and recruitment freeze, cutting 320,000 posts in the year to September, down on the 500,000 lost in the year to August.

FRANCE

UNEMPLOYMENT: French unemployment rose sharply in September. Unemployment increased 28,200 from the August level to 2.95 million. September's rise in unemployment, the second successive monthly increase, took the jobless rate from 11.4% to 11.5%, and confirmed that an underlying improving trend has halted. Several factors were blamed - ranging from a bigger-than-usual impact of school-leavers on the labor market and the increased volatility of the French labor market after the rise in part-time and short- term contracts.

CPI: France's consumer price index rose 0.1% in October compared with September, taking the year-on-year inflation rate down to 1.8%, according to the government.

INDUSTRIAL OUTPUT: French industrial output fell in September by 1.8% from its July-August level, according to the Insee statistics agency, providing further evidence of the slowdown in French economic growth. In the same month, manufacturing output, as lightly narrower measure which excludes energy and food, dropped by 2% over its July-August level. The September decline was broadly based, affecting intermediate industrial inputs as well as finished consumer goods.

KEY INTEREST RATE REDUCTION: The Bank of France responded to President Jacques Chirac's tougher line on tackling public sector deficits and the rebound in the French franc by cutting one of its main interest rates. The central bank reduced the 24-hour lending rate from 7% to 6.6%. The move was in response to calls from the conservative government of Mr. Alain Juppe, prime minister, and French employers for a sustained reduction in interest rates to help stimulate the slowing economy.

The cut reflected improved confidence in financial markets after Mr. Chirac's call for budgetary rigor and his backing for two years of austerity to enable France to satisfy the criteria for European monetary union. The criteria require a maximum public sector deficit of 3% of GDP compared with a forecast ratio of 5% in France this year.

INDUSTRIAL PRODUCTION: French industrial production saw a modest recovery in October in most sectors, but not in semi-finished goods, which declined further, according to a survey of business leaders by the Bank of France.

Overall demand improved mostly due to orders from abroad, notably from the US and Asian countries. The performance of European countries continued to be mediocre. The survey found that economic activity is likely to remain stable in the months ahead, with progress expected in the capital goods, vehicle and agricultural industries.

AUSTRALIA

ECONOMIC GROWTH: Australian Treasurer Ralph Willis said September quarter growth is consistent with the government's estimate for the economy to grow by 3.75% in the year to June 30, 1996. Figures released showed the Australian economy expanded by 1.6% in the September quarter, for an annual growth rate of 3.3%. That's down 3.8% in the year to June 30.

Willis said the date indicated there have been strong productivity gains, which in turn may take some of the heat off wages growth and inflation. He said the major sources of growth in the quarter were net exports, non-farm inventories and a rebound in the farm sector following the breaking of the drought.

UNEMPLOYMENT: Australia's unemployment rate increased for the third consecutive month, to 8.7%, in October, while the estimate of total employment fell by 33,700. The data was significantly weaker than expected. Market estimates had been for modest growth in jobs during the month and small decline or, at worst, a static unemployment rate. The unemployment rate, at 8.5% in September, has now risen for three consecutive months, something which last happened in mid-1992.

RETAIL SALES: Australian retail spending in October rose 0.5% as expected, underpinning expectations that the economy is slowing, although not enough to warrant any immediate cut in interest rates.

Retail spending in October increased A$9.89 billion (US$7.35 billion) from A$9.85 billion in September, according to the Bureau of Statistics. The rise followed the first decline in a year in September, by 1.6%. In the current year, sales were up 7.1%

NET FOREIGN DEBT: Australian net foreign debt in the September quarter fell 0.3% to A$180.723 billion (US134.386 billion), according to the Bureau of Statistics. That compares with a record revised A181.228 billion in the previous 3-month period. Net foreign debt includes government and corporate borrowing overseas, foreign investment in Australia and Australian investment abroad. On the year it rose 10.9%.

As a percentage of GDP, the bureau said net foreign debt fell to 39.3% from 39.9% in the June quarter.

BUDGET DEFICIT: The Australian government's budget deficit in July-October, the first four months of its current financial year, fell to $4.374 billion (US$3.2 billion) from $7.224 billion in the same period last year.

According to a government statement issued by Finance Minister Kim Beazley, the lower deficit partly reflected the timing of spending by the government and of the receipt of proceeds from the sale of its 75% stake in Quantas Airways Ltd.

BUILDING APPROVALS: Building approvals in October dropped 8% to 10,035 for a value of A$2.161 billion (US$1.616 billion), the Bureau of Statistics said. In the year they were down 37.5%.

CURRENT ACCOUNT: The government released the October balance of payments report, which showed the current account deficit widened 8% to A$1.60 billion, in line with expectations. The September deficit was revised down to A$1.48 billion from the original estimate of A$1.57 billion.

WESTPAC LEADING INDEX: The most widely watched leading indicator on the Australian economy rose just 0.2% in September, underscoring expectations that the pace of Australia's economic activity is easing. Te Westpac-Melbourne Institute monthly index measures where the economy is likely to be in six months.

MANUFACTURING INPUT PRICES: The prices of materials used by Australian manufacturing industry in September fell 0.9% from August, according to the Bureau of Statistics. In the year, prices were up 5.2%. The seasonally adjusted fall follows a 1.3% decline in August. The prices of imported materials used by manufacturing industry fell 0.6% in September from August. They rose 8.9% on the year.

INFLATION EXPECTATIONS: Australian expectations for the nation's annual inflation rate fell to 4.6% in November from 4.8% in October, according to a survey by Westpac Bank and the Melbourne Institute Centre for Business Cycle Analysis. It was as high as 5.2% in August and as low as 4.3% in September. The measure is a median rate of price rises expected by consumers in the next 12 months. Consumer price inflation in Australia was running at 5.1% in the year to September 30, up from 4.5% in the year to June 30. It was the highest consumer price inflation in almost five years.

HOUSING FINANCE APPROVALS: Approvals for housing financing in Australia in September rose 10.1% from August, according to the Bureau of Statistics. That followed a 10.6% decline a month earlier. The bureau said housing approvals in September fell 10.9% on the year, seasonally adjusted.

In the month, 38,116 home loans were approved. That's down from August's 34,604 approvals. The bureau said housing financing was valued at A$3.63 billion (US$2.67 billion), compared with A$3.30 billion in August.

PRIVATE SECTOR WAGES: Australian average weekly wages in the private sector rose 1.3% in the three months to August 31, the government reported. In the year, private sector wages were up 6.1%. The central bank and the government have repeatedly warned that such strong wages growth will sound alarm bells about the pace of inflation.

The latest figures compare with 1.9% in private sector wages in the three months to May 31. In the year to May, wages grew by 5.8%.

MERCHANDISE IMPORTS: Australian merchandise imports in October were little changed, underpinning perceptions the economy is slowing and the worst of the nation's troublesome current account deficits is over.

Imports in October rose 0.2% to A$6.08 billion (US$4.51 billion) according to the Bureau of Statistics. That compares with an 11- month low of A$6.06 billion in September. Forecasts were for an increase of about 2.5%

CANADA

CURRENT ACCOUNT: Canada's current account deficit narrowed to an eight year low of C$3.39 billion (US$2.5 billion) in the third quarter, according to StatsCan. The second-quarter gap was revised down to C$4.744 billion from the originally reported C$5.512 billion. All figures are seasonally adjusted.

Then current account deficit was made up of a surplus of C$7.036 billion on merchandise trade, up from C$10.426 billion in the second quarter, and a deficit of C$10.426 billion on non- merchandise transactions, which increased from the second quarter gap of C$10.322 billion, according to StatsCan. It was the lowest quarterly current account gap since 1987.

The merchandise trade surplus in the July-September period set a new record high, up 26% from the previous benchmark of C$5.89 billion in the first quarter of 1995.

GDP: Strong exports to the US helped offset slow domestic demand in the third quarter as Canada's economy pulled out of its second-quarter contraction, according to StatsCan.

Gross domestic product at 1986 prices expanded in the July- September period to C$613.628 billion (US$452.2 billion), which was up 0.5% from the previous quarter and 1.9% from the year- earlier quarter. At a compounded, annualized rate, StatsCan said the output of goods and services expanded at a 2.1% rate - the strongest quarterly pace this year - as an export surge compensated lagging construction and business capital spending.

The GDP deflator - the overall inflation measure covering all price changes in the economy and not just at the consumer level - rose 0.4% in the third quarter to 128. The deflator, or implicit price index, stood at 127.5 in the second quarter. The deflator's base year of 100 was in 1986.

1997 BUDGET: The Ontario government said it will cut up to C$3.5 billion (US$2.59 billion) from its budget in fiscal 1997 as part of a plan to rein in its deficit. The announced cuts will take effect in the fiscal year ending March 31, 1997, and are in addition to C$1.9 billion of cuts announced in July for the current fiscal year.

On an annualized basis, the series of cuts will save the government between C$4.5 billion and C$5.5 billion during the next two years. The budget deficit for the year ending March 31, 1996, was revised to C$9.3 billion from C$8.7 billion because of the changes in the way the province reports its revenues and expenses.

JOBLESS CLAIMS: The number of people receiving unemployment insurance in Canada rose 1.1% in September from August, according to StatsCan. Some 734,000 Canadians received benefits in September, up from 726,000 in August. In September, the number of Canadians filing new claims fell 3.9% to 256,000 from August's 266,000. All figures are seasonally adjusted.

INDUSTRIAL PRICES: Canada's industrial product price index fell 0.5% in October from September because of cheaper metal and lumber prices, according to StatsCan. October's decrease was greater than economist's expectations of a 0.3% decline. The index stood at 100 in 1986.

A 2.5% decrease in metal prices helped account for the lower trend; nonferrous metal prices alone dropped 5.45. Prices for lumber and wood products fell 2.3% on the month, StatsCan said.

Excluding petroleum and coal products, the producer price index fell 0.4% in October to 131.5% and was up 6.6% fro the year- earlier month.

M1 MONEY SUPPLY: Canada's M1 money supply rose C$653 million (US$476.7 million) to C$60.972 billion in October from September, the Bank of Canada said. M1, which includes currency in circulation and demand deposits, totalled C$60.319 billion in September, revised from an originally reported C$60.064 billion.

M2 money supply, which consists of M1 as well as savings and deposits, rose C$1.2 billion to C$379.857 billion from a revised C$378.659 billion.

Canada's M3 money supply in October totaled C$462.765 billion, up C$889 million from September's $461.876 billion, the bank said. M3 consists of M2 along with non-personal fixed term deposits and foreign currency deposits of Canadian residents deposited in Canada.

DEPARTMENT STORE SALES: Canada's department store sales rose 0.3% in October to C$1.176 billion (US$871 million) from September, StasCan said. October's sales were up 5.3% from the year-earlier month. cumulative sales in the first 10 months of 1995 increased 4.6% from the earlier period. All figures are seasonally adjusted. On an unadjusted basis, major department store sales fell 9.3% from October 1994 to C$639.4 million.

StatsCan said year-over-year sales at discount stores have increased every month this year except February. In October, such sales accounted for 54.4% of total department store sales.

CONSUMER PRICE INDEX: Canada's consumer price index fell an unexpected 0.1% in October from September as prices for travel, gasoline and women's clothing fell, according to StatsCan. At 133.8, the index was still 2.4 higher than in October 1994. The index stood at 100 in 1986.