Saudi oil for 93 percent of the actual market price. Simultaneous with this supply strategy of the nationalized firms, the government has significantly backed ELF-Erap and CFP on the domestic markets by giving them a bigger percentage cut in total distribution at the expense of Mobil and other U.S. oil multinationals.

Profiles of Key Industrial Sectors

AUTO: The auto industry had a record year in 1976, based in part on sustained consumer spending until the fourth quarter. Total production for the year was 3.4 million vehicles, reflecting a 17 percent increase in automobile production, a 35 percent increase in small utility and truck production, but a marked 21.4 percent decline in heavy trucks. Renault was number one in production with 1.365 million vehicles, followed by Peugeot at 758,000; Citroen at 679,000 and Chrysler France at 510,000. The industry as a whole was able to prevent stockpiling during the course of the year by forcibly keeping stocks low, even creating extended delivery periods when necessary. On the basis of these record production figures for the year, the newly merged Peugeot-Citroen interests showed a consolidated turnover of 35 billion francs. However, the prospects for 1977 are not bright, as auto producers are predicting a sharp curtailing of sales. Investments in 1977 for Peugeot-Citroen and Renault are projected at 2 billion francs at present to cover both improvements in productive capacity and new models.

CHEMICAL: The French chemical industry was literally saved this year by the organic chemicals wing of the sector, which will largely be responsible for the projected record turnover of 90 billion francs in 1976, an increase of 17 percent from the previous year. For chemical fibers, the leading chemical firm Rhône Poulenc suffered a 500 million franc deficit in 1976, while the entire industry had a parallel loss of 500 million francs in the mineral sector, primarily fertilizers. Fertilizers did particularly poorly in 1976, especially following the summer's drought; nitrogenous fertilizer production dropped 14 percent for the year, complex fertilizers 11 percent and superphosphates 13 percent.

The activities of the chemical engineering firm Technip stands in marked contrast to the general deterioration of this industry. In the past two months, Technip has won 6.5 billion francs in trade deals with the Soviet Union and Poland, for construction of three separate petrochemical and related refining and processing complexes. The largest deal is a four billion franc petrochemical refinery project with Poland, signed at the close of 1976. Technip has also just recently signed a one billion franc contract with Qatar for construction of a steam cracking unit which will also have spinoff facilities for production of ammonia.

STEEL: Overall steel production for the year reached 23.2 million tons, a 7.8 percent increase from 1975, but still 14 percent below the levels of two years ago. The hardest hit sector was rolled steel, reflecting the collapse in construction and housing during the year. Plant efficiency for this wing of the industry is currently only 60 percent, and weekly work hours per employee are at a low 32. Sacilor-Sollac, France's number one producer of rolled steel, had a sharp cutback in production to 6.5 million tons out of a total capacity of 9 million. The rate of decline in flat steel production was not as sharp in 1976 in part because of the sustained activity in auto. However, the industry as a whole faces a major debt financing problem in the immediate future. Total industry indebtedness equalled total turnover in 1976, or 33 billion francs. Private investments in 1976 reached scarcely 2.8 billion francs, hardly sufficient to cover 2.5 billion in interest payments due. The outlook for 1977 is even bleaker, with private investments currently projected at two billion francs. In the long term, Sacilor-Sollac and Usinor, the leading flat steel producer, have plans for eliminating close to 12,000 workers from their combined workforce of 90,000. The proposed government bailout plan for the antiquated Lorraine steel industry fits right into the vicious pattern of "rationalization" rather than expansion which will be promoted in the first quarter of 1977. Out of a projected three billion franc investment, one third will go to phasing out 14,000 jobs and the rest to modernizing plant and equipment. Because of the desperateness of the steel situation, the government has relented in backing up a total of seven billion francs in low interest loans in 1977, on the condition that this be used for make-work jobs on the spot and plant "modernization."

Italy Needs Credit Lines To Maintain Recovery

ITALY

A mild economic recovery in Italy resulted in a 12.3 per cent increase in industrial production and a 35.5 per cent increase in exports for 1976. While exports increased by taking advantage of the lira devaluation, however, the devaluation contributed to a 46 per cent increase in the cost of imports as producers were forced to pay higher prices for raw material imports.

These high import costs generated major domestic problems: Italy had the second worst trade deficit in its history; there was massive internal debt accumulation, a 1976 inflation rate of 20.5 per cent, and corresponding discontent from the trade unions in the face of a lowered standard of living.

The Andreotti government has staked everything on the expansion of foreign trade, the only way out of its present economic dilemma.

The Soviet Credit Line

In 1976, 38 percent of Italy's total credit extension was to the Soviet Union; estimates for this year (including a still-to-be-signed $650 million credit line) are that 50 percent of Italy's credit will go to the Soviet Union. Italy is blacklisted on the traditional loan market and therefore cannot supply this credit from its own funds.

Italian Foreign Minister Forlani and Soviet Foreign Trade Minister Komarov worked out the $650 million credit line last month but Italy has stalled on finalizing the agreement because of a lack of funds — a delay that has already cost the Italian industrialists close to one billion dollars in lost orders from the Soviet Union. Moscow-based representatives of major Italian firms — including Montedison, Fiat, Finmeccanica and Snia Viscosa — visited the Italian Embassy in Moscow Jan. 6 to pressure the Italian government for quick implementation of the $650 million credit line before Italy is squeezed out of international competition. But Italy, running a $6 billion annual trade deficit is in no position to provide the credit.

The trade credit conditions Italy is able to offer the Soviet Union are almost prohibitive: making Soviet contracts or credit paper negotiable on the international financial markets in case Italy wishes to "sell" such instruments or use them for security for its own international credit needs; restricting repayment to an eight-year period without the usual three year "grace" period; and raising the Soviet interest payment to 7.95 percent from the 7.55 percent originally agreed upon by Forlani and Komarov.

Italian Foreign Trade Minister Rinaldo Ossola, stalling for time to try and come up with the credit line to formalize the Soviet contract, has postponed his Feb. 20 trip to Moscow where the contract was to be signed.

Italy's internal consumption, despite import increases has contracted because of the austerity measures imposed to support the lira throughout 1976. The highest monthly Consumer Price Index increases were registered at 1.8 and 3.4 percent for September and October 1976 respectively. The CPI will undoubtedly be worsened by the Feb. 5 "anti-inflationary tax package" passed by the Italian Parliament. In order to avoid an open confrontation with the trade unions over using cost of living, the Italian Council of Ministers passed a tax package which, ironically will indirectly reduce the living standards of the working class, increasing consumer prices by one percent. The package will provide $1.6 billion for the government and is designed to cut labor costs by 5 percent. At the same time, the Value Added Tax was increased from 12 to 14 percent. The package also exempted employees from $1.4 billion in payments into a social benefits fund, which will be covered by an additional tax.

The Council of Ministers also increased the cost of petroleum products — excluding gasoline.

Production increased steadily throughout 1976 rising 12.3 percent over 1975 figures. But the high level of output depended on rising government subsidies to the state-owned industries to make up the difference between their increased earnings and the even greater increase in their costs after the January 1976 collapse of the lira. As a result, the indebtedness of the state-sector industries has passed the danger mark. Despite the apparent industrial boom, Italy's economy, which depends on a constant, high throughput of costly raw materials, is running at a net loss.

The latest available production figures, comparing the

Production By Industry

	Steel Thousand Tons (Monthly Average)	Auto Thousands (Monthly Average)	Buildings Completed Million Cubic Meters (Monthly Average) Total	Residential
1973	1,750	152.1	11.4	7.7
1974	1,984	135.9	10.7	7.0
1975	1,818	112.4	13.5	9.1
1976		130.4		
Jan	1,818	110.3	13.3	8.6
Feb	1,748	111.2	13.2	7.2
Mar	1,909	125.3	10.0	6.4
Apr	1,741	109.1	9.7	6.2
May	2,054	135.4	11.1	6.8
Jun	2,039	128.2		
Jul	2,159	152.2		
Aug	1,679			
Sep	2,141			
Oct	2,164			

Trade And Payments

Billion Lire

	Imports (CIP) (Monthly Average)	Exports (FOB) (Monthly Average)	Trade Balance	Million Dollars U.S. Current Account	Million Dollars U.S. Overall Payments
1973	1,352	1,081	-271	-2,510	- 197
1974	2,217	1,640	-577	-7,817	-4,633
1975	2,091	1,897	-194	- 528	-2,673
1976					
Jan	2,088	1,769	-319		
Feb	2,338	1,880	-459	I. Quarter	
Mar	3,098	2,511	-587	-1,413	-2,344
Apr	3,070	2,362	-708		
May	3,246	2,737	-510	II. Quarter	
Jun	3,013	2,526	-487	-1,338	- 183
Jul	2,883	2,988	+105		
Aug	2,574	2,226	-348		
Sep	3,224	2,721	-503	- 390	
Oct	3,295	2,965	-230	- 230	- 80
Nov	3,604	2,980	-624		+ 390

SOURCE:OECD, IMF

July-October 1976 period to the same quarter 1975, showed impressive increases in indicator sectors: chemical up 24.4 percent; textile, 15.4 percent; metallurgy, 13.2 percent; rubber, 9.8 percent, and machinery, percent. Industrial production for October 1976 compared to 1975 was up 10 percent; November 1976 to November 1975, up 17 percent and December 1976 to December 1975, up 21.9 percent.

Exports of primarily manufactured goods increased in the first eleven months of 1976 by 35.5 percent to a total of $31.6 billion. Imports however rose even further, by 46 percent, for a cash total of $37 billion ($9 billion alone being accounted for by energy supply imports).

On the basis of these figures, the *Journal of Commerce* estimated that Italy's 1976 foreign trade deficit would be the second worst ever. The *Journal* estimate that the trade deficit had tripled from 1975 to $6 billion in 1976.

Increased exports were the only thing that saved Italy from total bankruptcy. Exports were largely increased due to the dumping of crude steel and other goods on the European market, and the beginning of delivery on large deals to the Soviet Union and the Arab countries. The devaluation — caused increase in imports — primarily of oil and food products — and the resulting gigantic foreign trade deficit, have begun to squeeze the central government's investment in the public sector industries. This cutback in investments to the heavily indebted public sector threatens to collapse the vital public steel and chemicals industries.

Currently the Italian Senate is modifying the government's main investment program, the industrial reconversion plan, slashing it from a projected investment of 3800 billion lire to 750 billion. The Italian Reconstruction Institute (IRI), the major steel producer through its subsidary, Finsider, is threatened with bandruptcy. IRI President Petrilli warned on Feb. 4 that unless IRI was given an immediate 670 billion lire to cover just its operating costs the company would be forced to close. IRI's overall debt is 14,300 billion lire and its continued operations are vital to Italian industrial recovery. In November 1976 total steel production was estimated at 23.1 million tons and the state sector alone produced 16.7 millions tons (4 million of which was specialized steel). Of the total state sector output, IRI's Finsider produced 12.8 million tons (2.8 million of which were specialized steel).

Montedison, the partially state owned petrochemical complex which was originally slated to get 2000 billion lire of the projected 3800 billion lire is now to get only bare-bones operating costs of $ 700 million from the industrial reconversion bill. Montedison however began to show signs of recovery from July to December of 1976, when it began delivery to the Soviet Union of complete chemical plant facilities. Montedison ended 1976 with a deficit of only 50 billion lire as compared to 200 billion lire deficit in 1975. This concern accounts for 15 percent of Italy's trade with the Soviet Union.

Two major private companies, Fiat auto and Pirelli rubber, are slated for major capital investments in 1977 based on increased trade with the Soviet Union and the developing countries. Fiat received a major infusion of capital in a deal signed Dec. 5 with Libya which increased the auto company's capital from 150 to 165 billion lire. With this capital investment, Fiat intends to reopen its nuclear energy production sector and invest heavily in Italy and Brazil, particularly in improved plants, and increased industrial vehicle production. On Feb. 2 Carlo Rossi, the executive in charge of Fiat's Termeccanica and Turbogas announced the sector's merger under the name Termeccanica Nucleare, the new nuclear development sector of Fiat.

Fiat director general, Romiti, a representative of Italy's pro-industrial expansion faction announced a total investment of one trillion lire for 1977, 860 billion lire of which the auto, industrial vehicles, and specialized steel sections of Fiat will receive 50 percent of which will be invested in model changes and production improvements. Of the 290 billion lire for the auto industry, 260 billion will be invested in Italy and 30 billion will be invested in Brazil. Of the total industrial vehicle investment of 385 billion lire, 275 billion will go to Italy to complete the modernized Grottamindara plant. Fiat — Romiti will only slightly increase passenger car production in 1977, producing a projected 1,308,000 vehicles as compared to 1,339,000 in 1975.

Pirelli rubber company, and its subsidiaries, announced on Jan. 9 that it will increase its capital from 70 to 130 billion lire. The capital inflow — despite incessant rumors — is not from the Arabs but from state-owned Mediobanco, which is underwriting 50 percent of Pirelli's new stock purchases.

The Pirelli company, despite the fact that it has paid negligible stock dividends in four years, is expected to break even this year. Plans for reorganization protend a major expansion. Pirelli is expected to restructure the companies into four major categories — pneumatic, cable, industrial products and consumer products. According to *Il Mondo* of Feb. 2 Pirelli is ready to "deprovincialize" its operations. A spokesman for the company stated that Pirelli technology is the most advanced in Europe and that the company is now ready to reach out into the international markets.

West German Policy And Production At The Crossroads

WEST GERMANY

Private and governmental policymakers are now debating the underlying crisis in the West German economy. At the end of 1976, industry chalked up some gains relative to the shattering minus signs of 1976; but the economy is running at a loss in real terms, as its productive base deteriorates, new capital investment declines, and crucial margins of its erratic liquidity flows go into public debt financing rather than expanded capacity and technological innovation.

The exports on which at least half of West German economic activity directly depends grew 14 percent in 1976, and though imports rose 17 percent, a $14 billion trade surplus was achieved which the BRD press pointedly compared with the U.S. deficit of the same size. Sales to the most essential single group of trading partners, the Common Market, rose, especially in the fourth quarter as demand from Britain, Italy, and even France picked up. December industrial production (providing a 6.5 percent increase in the index for the calendar year) showed a 10 percent decline from November; but incoming orders that month, especially for the crucial capital goods sector, climbed counter to the overall orders' plummet in the fourth quarter (Tables I and II).

Yet heavy industry, especially the steel and machinery sectors, is still in deep trouble, with so much excess capacity that upward blips in orders could easily be handled without new investment. Investment growth, along with the expansion of capital goods exports it presupposes, has now emerged as the subject of policy debate.

Reporting this month that investment plans for industry as a whole for the 1977 remain below the minimal 1976 levels, a deputy director of the influential German Chamber of Commerce, Dr. Broicher, complained that "rationalization still holds priority over expansion." However, Broicher did not venture beyond familiar pleas for expanded research and development through corporate tax relief and a corresponding willingness on the part of companies to overcome their "defensive investment tendency." For its part, the government has insisted that real export-led growth of investment will be pursued in opposition to inflationary fiscal and monetary attempts to "stimulate" the still-depressed economy.

This week, too, the Dresdner Bank insisted that, owing to the soundness of the USSR's economy, its indebtedness to the West should be no obstacle to trade; BRD industrialists and their financial daily, *Handelsblatt*, have welcomed and publicized the Comecon central bank's transferable ruble proposal for gold-backed clearinghouse settlement and promotion of trade and investment arrangements among the socialist sector, Third World, and advanced sector. Nevertheless, a low ceiling persists on the BRD's ability to generate the giant increments in credit facilities for the East-West, North--South transfers of capital goods it seeks.