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Government vs Human Nature

The Quest for Revenue

Since the dawn of time mankind has been doing battle with the greedy ruling class be it a monarchy, democracy, dictatorship, tribal leader or communistic authority. History is merely a saga of the trials, tribulations and injustices that have always been carried out by those in power against those who inevitably become their subjects. This timeless pursuit of revenue has littered the journals of history with countless tax revolts, civil uprisings and outright revolutions throughout both ancient times as well as present 20th century events.

Sometimes government has listened to the people and tax revolts have taken the form of enlightened wisdom. **Figure #1** is an illustration of a Roman sesterius issued in the year 119 AD by the Emperor Hadrian. The reverse side of Roman coinage served a function of general newspaper. Coins were often used to inform the population of some great victory or new social program and even the opening of a public works project such as the Coliseum. In this case, the Sesterius depicts Hadrian responding to the frustration of the people concerning high taxation. Hadrian gathered all the back tax records of the people and took them to Trajan's Forum in Rome and burned every last one. This tax relief wiped out over 900 million sesteri owed by the people in back taxes to the previous administration. As a result, Hadrian was one of the first emperors of Rome to enact a tax amnesty program.

Government's endless pursuit of power and revenue has always gone too far. The climax of this endless battle has always concluded with the abolishment of government and its replacement by its benevolent reincarnation that ultimately becomes the very thing it once promised to replace. Even Adam Smith wrote about this problem in his Wealth of Nations back in 1776.

"It is the highest impertinence of kings and ministers to pretend to watch over the economy of private people and to restrain their expense, either by sumptuary laws, or by prohibiting the importation of foreign luxuries. They are themselves always, and without exception, the greatest spend thrifts in the society. Let them look well after their own expense, and they may safely trust private people with theirs. If their own extravagance does not ruin the state, that of their subjects never will."

Roman Emperor Hadrian
Tax Revolt of 119AD

This Roman Sesterius issued to commemorate the burning of all tax records in the Trajan Forum wiping out 900 million back taxes

No matter how much we study the recorded past, somehow, someway government always ignores sound advice and determines that it is, in some magical way, different from all previous incarnations of authority. At times, government will argue that the past is totally irrelevant simply because we have modern technology in the age of lunar landings. But this argument is merely a smoke screen to allow the self-interest of those in power to ignore common sense. Nowhere in the debate to they recognize that human nature has not changed over time. Mothers still mourn for the death of a son in battle and the average man on the street still resents high levels of taxation as much today as he did in the time of Constantine the Great.

Government always fails to see how it has grown from its own pursuit of power and revenue transforming itself into the very thing it once pledged to replace. Even the American Revolution sought to overthrow the greedy monarchy of Britain through its slogans of "no taxation without representation." Today, the American dream has been transformed into the worst nightmare of our Founding Fathers. Where once a greedy monarchy tried to extort taxes of 10%, the average American now pays more than 40% in taxes. Americans succeeded in overthrowing a king only to replace him with politicians.

This seemingly endless cycle of benevolence, corruption, suppression, persecution and revolution appears to be linked to the dark side of human nature. This is why it is wisely said that while power corrupts, supreme power corrupts supremely. Government has always sought to restrain and control the nature of mankind for its personal gain. Even when government has attempted to control the social behavior of man, it still fails to succeed. **Figure #2** is a Roman Prostitute token issued around the time of Tiberius (14-37AD). At the time, Tiberius sought to eliminate prostitution by declaring it to be illegal to pay a prostitute with money that bore the image of the Emperor. Since all official coinage displayed the image of the Emperor, the solution to the problem was clear. The brothels issued tokens denominated in units of the Roman As. The client merely purchased his tokens and used them to finally pay the prostitute thereby committing no offense. The prostitute in turn redeemed her tokens at the end of the day with the brothel. Such tokens were issued for nearly 100 years until the law was finally deemed to be a failure and rescinded following the Civil War of 68-69 AD.

Modern day government still fails to display any better sense of controlling the masses. When Congress decided they wanted to raise taxes in 1986, one item that they attacked was interest deductibility for car purchases. Instead of collecting the intended revenue, the net result gave birth to the leasing industry. In business, tax laws sought to require companies to depreciate assets over greater periods of time even though all their upfront costs might be paid in the current year. Leasing helped solve that problem since it eliminated the extended depreciation period by avoiding legal title of ownership. Consequently, the company could take the full deduction for its expenses in the current year rather than over a 3 to 5 year period. These schemes are nothing different than those employed in countless recorded situations throughout time. Like the prostitutes of Rome, we merely transform a transaction into something else and commerce continues to go on its merry way.

Sometimes, government reacts quite violently or passes even more severe laws seeking to get its pound of flesh. While Congress would certainly disagree, they played a very key role in creating the entire S&L crisis. In the 1986 tax reform, many deductions for real estate were eliminated as government pursued greater revenue. Suddenly, real estate no longer became tax effective and investors began to bail out. Congress created a one way market where the majority wanted to cash in. Unfortunately, since the issue was tax driven and not economic driven, there were no buyers. Default after default began to unfold as property values crashed and lenders found themselves holding the bag. Congress responded by focusing on the small percentage of fraud cases and tried to blame the private sector and ultimately tax dollars

Roman Prostitute Token

circa 20-90AD

were then spent to bailout the savers.

History warns that days where political unrest begin to rise to the surface are directly linked to periods of excessive taxation. In 1381, **Wat Tyler** was the leader of the Kentish peasantry who marched upon London to petition King Richard I to provide some tax relief. To a large extent, the rising tax burden had been accelerated by the Black Death which had killed up to 50% of the laborers over a 50 year period. The feudal system collapsed and landlords for the first time bid for workers and paid them in coin rather than in crops. The King merely needed revenue and taxes rose drastically on a per capita basis as he quickly saw a new source of revenue - wages. As the peasantry protested in London, the Mayor called out the troops and Wat Tyler was slain. The Crown promised relief from the poll-tax but never provided it in the end.

Government's resorting to use of force to collect taxation still goes on today. In Germany, the tax authorities surrounded Merril Lynch and two other banks earlier this year. The tax authorities were looking for German citizens who have placed their funds offshore. The telephones were blocked, including all cellular phones as the police surrounded and cut off all access to the offices. Brokers were escorted back to their homes where a search for any customer files was then conducted. This single incident has had the net opposite effect that the German government intended. Instead of frightening the people into paying higher taxes, huge amounts of capital have been fleeing to Switzerland. This net capital outflow has been so significant, that the cross- rate between the DM and Swiss caused the DM to decline and the Swiss to rally. What the German tax authorities don't realize is that once that capital leaves due to such police state action, it is unlikely to return in the near future. The people have simply lost all confidence in Germany and can no longer trust it to protect the basic freedom of privacy.

In Japan the same issue has affected the FX markets for the Japanese yen. The sharp massive decline in the yen in a single month of over 10% was also due to the rising concern that the Japanese government is about to assign tax ID numbers to all its citizens. Many high networth individuals from Japan have been flying to the Caribbean and stopping by our offices along the way. If this rumor becomes reality, as it is most likely will next year, this factor alone could help create a 2 year dollar bull market going into 1998.

Whenever a government becomes desperate for revenue, it always burns down the barn to get at the rat. Even when the US installed the income tax, it realized that given the Constitution and the safeguards it contained for the people against the silent encroachment of government, it needed to remove those basic rights of freedom. Unlike all other forms of law where you are innocent until proven guilty, when it comes to taxes, you are assumed to be guilty and it is the taxpayer who must prove his innocence. In effect, the IRS can simply claim that you owe $1 million dollars and you must prove that they are wrong. If you cannot, well they can confiscate all your assets. Clearly, there is not much difference between the IRS and the king.

The single greatest lesson that government needs to learn, regardless of its political constitution, is that the people will pay only those taxes that they deem to be fair and reasonable. Once government's demands exceed such levels of fairness, as defined by its own people, then the battle begins.

While history is littered with countless episodes of violent confrontation over taxation, there are also interesting accounts of total avoidance of taxation on the part of the people. Even today, if we look at Italy, the economic statistics show that the nation is on the brink of defaulting on its national debt. Yet when you travel to Italy, one cannot help but notice the vibrant underground economy all conducting business in a world floating with cash. Eventually, a violent clash will emerge because the people have created a world in which they simply ignore government. The financial pressure is then placed upon government, then it will ultimately force it to act severely to prevent its own demise. In the end, a national default becomes inevitable.

In the United States, the current flat tax movement is none other than government pursuing its enchanted dream. The idea behind the flat tax is to **ELIMINATE** all the loopholes. The flat tax proposals are **NOT** tax relief but instead represent tax increases for some, reductions for others and merely a reshuffling of the tax burden. In reality, the flat tax will prove to be the single easiest form of taxation to avoid and will open far more loopholes than it will close. If enacted, the flat tax could result in creating the next real big recession.

If you look at a car dealer who might have several hundred cars on his lot, the amount of capital tied up in inventory is usually far greater than the net worth of the dealer. Consequently, his inventory is typically financed by a bank who in turn has a lien upon the inventory as collateral. This means that interest must be a deductible item for business - particularly those involved in durable goods. Once interest is allowed to be deductible for business but not on a personal level, the possibilities become endless. You can form a corporation and sell your home to it thereby enjoying capital gains. Then you can rent your home from the corporation which would then be able to deduct the mortgage interest expenditure. Any profits you might wish to shift into your corporation could then be paid back to yourself in the form of a dividend which would render it tax free.

The possibilities for reclassifying **"earned"** income into **"unearned"** tax free income are endless. Even companies can setup an offshore subsidiary, shift the bulk of its


THE DEATH OF WAT TYLER.

manufacture to these offshore ventures, import its goods at the highest possible cost and repay its profits back in the form of interest or dividends from the subsidiary completely tax free. The net losers will not only be the treasury, but also the American people who will see their jobs migrate to other parts of the world.

If government tried to close this loophole of not allowing corporations to deduct interest as part of its cost of production, then the flat tax will severely reduce economic activity rather than enhance it. Business inventories will need to be reduced drastically in turn reducing manufacture quite sharply in the near-term. Eventually, the glut of inventory will be disposed of but business will need to operate with less inventory in the system. Such an error would immediately cause a recession that might last 2 to 3 years before any return to normal activity unfolds.

The other problem that a flat tax presents is quite interesting. While it is widely recognized that the discrimination against capital gains has resulted in long-term investment moving offshore, the flat tax does nothing to restore this trend. If company A offers a 8% dividend and company B offers a 4% dividend, investors will flow to the highest yield. Nevertheless, company B might be paying a lower dividend because it is spending more capital on R&D while company A is enjoying short-term gains. Under the Democrats, capital has been taught that short-term investment is the best and punishment will be associated with long-term investment. After 40 years of such social engineering, it is highly doubtful that we can expect capital to suddenly change its philosophy without some prodding with reverse discrimination of a higher short-term tax rate with a much lower long-term tax rate where business is concerned. But here too, government just cannot admit that much of modern technology may have been designed in the US, it was manufactured overseas where short-term taxes are high and long-term investment enjoys almost a tax free status.

Taxation is becoming a very major issue globally. As we move into 1996, this issue will singlehandedly become perhaps the most important. Political elections are coming due everywhere from Russia and Israel to the UK, Australia and Japan. Of course the US elections will be a big issue and tax reform will play an important role as well. The risk of massive swings in capital flows globally next year are clearly rising as tax issues rise to the surface in Germany and Japan not to mention Canada and the United States. Just how this will play out is difficult to say but the one clear bull market to emerge will be none other than volatility.

The flat tax issue in the US is most likely going to fall flat on its face as the wealth of loopholes begin to emerge. To add spice to the confusing brew for 1996, we expect the elections in Russia to turn very nationalistic. By the end of 1996, the old cold war will begin to re-emerge once again. And then there is Hong Kong due to be handed over in 1997. So welcome to the new age of volatility, confusion and at times pandemonium. 1996 looks to be the year from Political Hell.


PRINCETON
EUROPEAN
WEEKLY
FT100
DAX
CAC40
Gilts
Bunds
Notionals
Currencies
LIBOR
PIBOR
Covering
Britain - France
and Germany
FX-Bonds-Share Mrkts

UNITED STATES

ECONOMIC GROWTH: The US economy rebounded vigorously in the July- September quarter, growing at an annualized rate of 4.2% in real terms. The third quarter rebound partly reflected special factors such as a surge in residential construction and heavy purchases of consumer durables following a sharp decline in long-term interest rates. Companies also failed to cut the rate at which they accumulated stocks of unsold goods. A stocks overhang could depress growth in the fourth quarter.

Consumer spending increased at an annualized rate of 2.9%, down from 3.4% in the second quarter. Business capital spending grew at an annualized 8.3% against 11.3% in the second quarter.

The low inflation component was as striking as the rapid growth. The GDP "deflator" - a broad measure of inflation - rose at an annual rate of 0.6%, down from 1.6% in the second quarter. A "fixed-weight" index showed inflation at 1.8 down from 3.2%.

INDUSTRIAL PRODUCTION: US industrial production fell in September for the first time in five months, indicating that economic growth is likely to remain moderate. The Federal Reserve said manufacturing output rose 0.2% in September but the increase was not sufficient to offset a large drop in electricity usage following the return of cooler weather.

Production as a whole fell 0.2% following an erratic 1.1% gain in August. The rate of capacity utilization declined to 83.8% against 84.2% in August, a further sign that inflationary pressures are receding.

Industrial production grew at an annual rate of 3.5% over the third quarter, following a decline of 2.3% in the previous three months.

EMPLOYMENT: US payroll employment grew modestly in September, providing further evidence that the economy is returning to a stable growth path after weakness earlier this year. The Labor Department said non-farm payroll rose 121,000 in September.

The employment gain was sufficient to hold the jobless rate stable at 5.6%, but not large enough to put upward pressure on inflation. While generally encouraging, the figures showed that job growth remains concentrated in the service sector. Employment in services rose 106,000 in September, with solid gains in retailing and health care. Construction added 16,000 jobs.

Employment in manufacturing, however, fell 32,000, bringing the total job losses since March to 200,000. The sector was forced to cut production earlier this year following an unexpected rise in inventories of unsold goods.

INFLATION: The Labor Department said consumer prices rose a less than expected 0.1% in September. The rate of inflation dropped to 2.5% a year, from 2.6% in August. The consumer price index was held down by a large decline in energy prices and by modest declines in clothing and transport costs.

RETAIL SALES: The Commerce Department said retail sales rose 0.3% between August and September, slightly more than expected. That comes after August's downward-revised gain of 0.5%, and a July decline of 0.4%. Excluding cars, sales rose a robust 0.7%. The figures showed strength in nearly all sectors except cars, which saw a setback after exceptional strength in August.

INVENTORIES: Inventories held by US businesses grew for the 17th consecutive month in August, according to the Commerce Department, despite the biggest increase in total business sales in a year. Stocks of unsold goods grew 0.4% in August to a seasonally adjusted $969.12 billion following a revised 0.5% increase in July - with most of the August rise occurring at the retail level. Previously, the department said inventories had risen by a smaller 0.3% in July.

Total business sales were up 1.5% in August to a seasonally adjusted $686.09 billion, the biggest increase since a 3.1% rise in August 1994.

PURCHASING MANAGERS' INDEX: The purchasing managers' index - a guide to the health of the manufacturing industry - rose to 48.3% in September against 46.9% in August. However, it remained below the 50% level predicted by many economists - the level widely regarded as marking the threshold for growth in the sector.

The figures indicated that the US economy is rebounding but growth is unlikely to be rapid enough to put upward pressure on inflation. The purchasing survey indicated that manufacturing industry has not yet recovered fully from its troubles earlier this year when excessive levels of inventories prompted cuts in production and employment. The index has been below the 50% threshold for growth in four of the past five months.

INDUSTRIAL PRODUCTION: US industrial production fell in September for the first time in five months, indicating that economic growth is likely to remain moderate. The Federal Reserve said manufacturing output rose 0.2% in September, but the increase was not sufficient to offset a sharp drop in electricity usage following the return of cooler weather, causing utility output to drop 5.4%.

Production as a whole fell 0.2% following an erratic 1.1% gain in August. The rate of industrial capacity utilization declined to 83.8% against 84.2% in August, a further sign that inflationary pressures are receding

DURABLE GOODS: New orders for US durable goods rose a higher- than-expected 3% in September, and 8.5% in the year to

September, signalling solid business investment growth in spite of an earlier manufacturing shakeout.

The September increase, which followed a revised 5.1% gain in August, reflected an erratic 10.8% rise in orders for aircraft and other transport equipment. Electrical machinery orders - including communications equipment - were up 5.2%.

HIGH TECH TRADE GAP: A report published by the American Electronics Association said the US trade deficit in high technology products and services rose to $11.7 billion in the first half of this year, a 56% increase over the first half of 1994. Total exports increased 20% to $60 billion, but imports rose 25% to $71.7 billion. Much of the increased deficit, according to the AEA, came from increased imports of products from the Asia-Pacific region, excluding Japan.

The negative trade balance of these countries with the US rose to $15.7 billion, a 27% increase versus the first half of last year. The US had a positive high technology trade balance with Europe of $7.6 billion, up 15% from $6.6 billion. Trade with Japan showed a deficit of $15.7 billion, up 27%. The AEA said that part of the reason for the increased trade deficit is that some countries restrict imports of American products.

TRADE DEFICIT: Strong growth in exports prompted a sharp and unexpected decline in the US trade deficit in August according to the Commerce Department. The deficit fell from $11.2 billion in July to $8.8 billion in August, its lowest level since December. The drop reflected a 3.7% increase in imports from July to $65.7 billion, a record in cash terms. Strength of exports was concentrated in capital goods and cars. Imports were unchanged at $74.6 billion, reflecting the sluggish growth of US consumer demand.

The sharpest improvement regionally was in trade with western Europe. The bilateral deficit with the European Union dropped to $494 million against $2.7 billion in July. The deficit with Mexico fell to $1.1 billion, the lowest since January. The deficit wit Japan fell only slightly to $5.1 billion.

There is some evidence that growth of exports is overtaking that of imports. In the first eight months of the year, exports of goods grew 15.7% relative to the same period last year. Imports of goods rose 15.4%. The deficit for the year to date was $82.1 billion against $70.1 billion in the same period last year.

UNITED KINGDOM

TRADE DEFICIT: The Central Statistical Office reported that the UK's trade deficit was 1.1 billion Sterling in July, up from 868 million Sterling in June, and 772 million Sterling in July 1994. Although the UK recorded larger deficits in April this year and December 1994, these months were affected by erratic imports of cruiser ships and artwork. July's deficit was also adversely affected by lower levels of oil sales and swings in the diamond trade. Meanwhile, currency swings left export prices rising faster than import prices, improving the balance slightly.

The data fueled fears that the improvement in trade seen earlier in the recovery may now be coming to an end. With growth in imports now outstripping underlying export growth, the CSO admitted "the latest estimate of the trend suggests that the UK whole world deficit is widening".

EXPORTS: British exports to the US fell a seasonally adjusted 11.1% in the three months to July, compared with the previous three months, according to the CSO. However, exports to Germany rose 9.5% in this period while sales to Belgium, Holland and the Netherlands grew by 10.6%.

The data suggests that traders are seeing a growing divergence between different regions as world growth patterns shift. The CSO said volume of UK exports, measured overall, was 12.7 billion Sterling ($20.1 billion) in July, unchanged from the previous month. On a three-monthly basis, exports were 2.6% higher in the three months to July, compared with the previous three months. Because export prices rose 3.2% in this period, the actual rise in export volumes was only 0.7%.

CAR EXPORTS: The CSO said exports of cars from the UK to the rest of the world were a seasonally adjusted 18% higher in the three months to July than a year before. However, in a shift that suggests the trend is turning, exports fell 11% between the three months to April and the three months to July of this year.

Exports to the EU accounted for much of the fall, dropping by 13% in the period. Exports to non-EU countries - which account for about 30% of overseas sales - also fell by 5% in the same period.

ECONOMIC GROWTH: The Central Statistics Office said gross domestic product in the three months to September was 0.5% higher than in the previous three months. This was the same rate of expansion as in the previous quarter and the fourteenth successive quarter of growth.

The annual rate, however, slipped back in the year to the third quarter to 2.4% from 2.8% in the year to the previous quarter. This was the slowest annual rate of growth for more than two years and in line with rates which have been sustainable in the past without pushing up inflation.

While the manufacturing sector continued to display signs of weakness, the service sector remained robust, notwithstanding recent weakness in retail sales. The CSO said service sector output grew by 0.7% between the second and third quarters and was 3.2% higher in the latest quarter compared with the same quarter a year earlier.

MANUFACTURERS OUTPUT: Manufacturers stepped up their production in August, reversing the drop in output seen in July. But while car manufacturers, computing and soft drinks raised production, other sectors such as machine tools and pharmaceuticals reported declining activity. Although manufacturing expanded strongly last year, it slowed earlier this year amid slower export growth.

CAR OUTPUT: Car production fell in September for the first time in 15 months as manufacturers reacted to sales in August that disappointed hopes of a strong recovery in Mainland European markets. Car output for the first three quarters of the year nevertheless remained 7% higher than in the same period of 194 and is still on course to reach the highest yearly total for two decades.

The Society of Motor Manufacturers and Traders said the figures from the CSO were disappointing. Total UK car output in September was 111,182, down 11.2% from September 1994. Output for export, at 54,423, was 2.3% lower than a year before.

PURCHASING MANAGER'S INDEX: The purchasing manager index, which surveys business activity, fell in September to its lowest level for three years. The data fuelled suspicions that manufacturing output has eased in recent months.

Measured overall, the purchasing manager's index, which consists of data on stocks, output, demand, delivery times and employment, fell to a seasonally adjusted 50.5% in September. Since any figure above 50% indicates month-on-month growth, the data suggested that manufacturing activity had expanded slightly between August and September. However, the rate of expansion was the slowest seen for three years, and a breakdown of the data suggested that this easing in growth had been associated with company destocking.

The level of purchases by companies from other companies eased. The level of new orders reported by companies fell back between August and September. Overall output was reported to have risen slightly between August and September.

The survey of some 300 managers suggested that a lower level of demand and orders is prompting many companies to sell off stock. Although the survey suggested that some price pressures in industry are easing, this did not entirely allay the City of London fears that inflationary pressures could reappear next year if demand recovers.

MANUFACTURING GROWTH RATE EASING: Two business surveys reported that orders were now rising at a slower rate. The British Chambers of Commerce said the proportion of companies reporting increased levels of sales had fallen in the last quarter. The BCC survey of some 7000 companies, conducted in September, found that the proportion of manufacturing companies reporting higher export sales, compared to those reporting lower ones, was a positive balance of 29%. This was down from the previous quarter's level of 35%, with a similar slowdown reported in the growth of export orders.

Dun and Bradstreet, the business information group, said that businesses were now considerably less optimistic about the outlook for profits, sales, new orders and exports.

SKILLS SHORTAGES - PAY RISES STEADY: According to a survey by DHL, the express delivery group, almost half of all British exporters are experiencing skills shortages. However, the survey notes that with shortages concentrated in a few specific areas of manufacturing, they are having limited pressure on overall wage levels.

Surveys from the Confederation of British Industry, the UK's largest employer's organization and Income Data Service also report that pay settlements show little sign of significant acceleration, with the low level of public-sector settlements keeping the average rate of wages growth below the level of inflation.

The CBI reported that manufacturing pay awards averaged 3.5% in the three months to September, fractionally up from 3.4% recorded in the three months to June, and higher than the 3% seen in the same period last year. Service sector awards averaged 3.4% in the three months to September, down from 3.9% a year before.

The IDS data noted that most public sector settlements were between 2% and 3%, while of the 95 private-sector settlements monitored only half were more than 3.5%

VISITOR SPENDING: The amount spent by tourists at UK visitor attractions last year exceeded BP1 billion ($1.5 billion) for the first time and represented a 5% increase on the previous year, according to the English Tourist Board. The number of visits to both admission charging and free attractions increased by 2% to 387 million last year, with overseas visitors accounting for 19%.

GERMANY

TRADE BALANCE: Germany's trade in July continued to shrug off the effects of the strong D-Mark earlier this year, with exports rising by 3.6% compared with July 1994 to DM 56 billion ($38 billion). The Federal Statistics Office said imports declined over the same period by 0.8% to DM50.1 billion, leaving a visible trade surplus for the month of DM5.9 billion compared with DM3.6 billion in July last year. According to provisional Bundesbank calculations, Germany's current account balance of payments was DM5.9 billion in deficit in July because net payments abroad for services and transfers were double the visible trade surplus. In July 1994, Germany's current account showed a DM11.2 billion deficit. The visible trade surplus rose to DM51.7 in the first seven months from DM41.9 billion. The statistics office also reported that German wholesale turnover in August fell by 1% in real, seasonally adjusted terms from July. However, it was 3% higher in real terms than in August last year.

EMPLOYMENT CONCERNS: Growing unemployment prompted a worried government to declare job creation as its "central task". The number of unemployed grew in September a seasonally adjusted 48,000 to about 3.5 million, or 9.2% of the workforce. Since February, the jobless total has increased 100,000, despite an estimated 2.5% increase in gross domestic product. High labor costs have led manufacturers and other industries to slash jobs and boost productivity by operating with fewer workers.

In west Germany, unemployment increased by 14,000 and in the east by 34,000, according to the Federal Labor Office. The jobless rate in eastern Germany was unchanged from a year ago at 13.8%.

INDUSTRIAL ORDERS: New orders for German industry in August fell following a strong rise a month earlier, but the government and analysts warned that the figures should be treated with caution because of a recent changeover in the way they are calculated. The August figures may also be unrepresentative because they were affected by the summer holidays, the ministry said.

August new orders fell 2.4% compared with July and slipped 0.2% compared with the same period a year earlier. A more representative measurement - the combined figures for July and August compared with the same period last year - showed that foreign orders had risen 4.7% while domestic orders had fallen 1.3%.

WHOLESALE PRICES AND INFLATION: West German wholesale prices rose by 0.4% month-on-month in September after falling 0.5% in August. The year-on-year rise was 1.3%, compared to 1.0% last month.

West German inflation fell a provisional 0.1% in October on the previous month for the second month running and remained stable at a n annual 1.6%.

REVISED FACTORY ORDERS: Germany said growth in new orders received by manufacturers in the first half was much lower than previously estimated. The Economics Ministry slashed its estimate of order growth in the 6-month period to 3%, down from a previously estimated 3.8%.

WEST GERMAN OUTPUT: Manufacturers in Western Germany expect a marked slowdown in output next year, according to survey from the Munich-based Ifo economic research institute.

A poll of 350 companies employing more than a quarter of the regions manufacturing labor force

TAX REVENUE SHORTFALL: According to the government's tax forecast committee, slower economic growth and higher demand for investment subsidies in eastern Germany will cause a shortfall of DM11.4 billion ($7.7 billion) in 196 tax revenues.

The DM11.4 billion shortfall from the committee's last estimate in May is higher than the DM10 billion projected in September by Mr. Theo Waigel, the finance minister, and is likely to make it difficult for the government to keep within the planned 1996 budget deficit of DM60 billion.

The tax committee, which meets twice a year said all levels of government would be missing a combined DM26.1 billion this year and a total of DM29.4 billion next year because of lower revenues. Anticipating the shortfalls, Mr. Waigel has ordered spending restrictions at all ministries, demanding a that any expenditure over DM1 million had to be cleared by the finance ministry.

TAX PROBE: German tax authorities have stepped up their investigations into people suspected of evading tax by sending money abroad, prompting sharp complaints from two of the country's leading banks. Tax investigators said up to 2,000 clients of Commerzbank were being investigated for possible offences.

The cases, like those at several other German and foreign banks which have been visited by tax officials, center on the 30% withholding tax levied by the German government on investment income and attempts by private investors to avoid paying this. It is not illegal to invest money abroad, but the earnings on such investment must be declared for tax.

GERMAN GROWTH FORECAST: German consumer spending will recover next year but economic growth will be a modest 2.5% because of the building boom that followed unification in 190 will come to an end, according the country's main economic institutes.

The institutes warned that the slowing of demand in the construction industry, especially in eastern Germany, meant unemployment was likely to remain above 9%, but they are expecting stronger economic growth in the second half of the year. They also warned the government would find it difficult to keep the budget under its DM60 billion ($43 billion) target next year. Slower-than-expected economic growth this year will contribute to a shortfall in tax revenue that the government estimates at DM20 billion over this year and next.

The controversial "solidarity" income tax surcharge re-introduced that year to finance the soaring costs of unification was unlikely to be lifted soon because eastern Germany was still dependent on assistance. Transfers to the east, according to the institutes, will total DM194 billion. The Federation of German Chambers of Industry and Commerce said the report confirmed that " the blockade of growth forces through excessive taxes and levies is continuing" The federation wared that the solidarity tax and higher social insurance costs would dampen investment and work against growth.

INDUSTRIAL PRODUCTION: German industrial production in August was weaker than expected. Seasonally adjusted industrial production fell 3.4% compared with July, and was down by 0.9% compared with a year earlier. At the same time the economics ministry revised its July industrial production figures downwards to 1.7%, from a provisional 3.3%.

WEST GERMAN OUTPUT EXPECTATIONS: According to a survey from the Munich-based Ifo economic research institute, manufactures in western Germany expect a marked slowdown in output. A poll of 350 companies, employing more than a quarter of the region's manufacturing labor force, indicated that output would grow by an average of 2% next year after nearly 5.5% in 1995. However, during 1996 production should exceed the previous record level reached in early 1992 before the recession of 1993.

Ifo said the investment goods sector was expected to show the fastest output growth this year, for the first time this decade. It should continue to lead production growth next year, but at a slower rate. Output of the raw material and production goods sector would continue to grow until late 1996, when a decline is expected to set in. Output of consumer goods and consumer durables was expected to stagnate until the middle of next year, with production in labor intensive sectors such as clothing and shoes suffering from plant closures and transfer of production to low-cost areas abroad.

MONEY GROWTH: The Bundesbank said M3 rose at an annualized rate of 1.5% in September over the fourth quarter of 1994, compared with 0.8% the previous month and only 0.3% in July.

JAPAN

IMPORTED VEHICLE SALES: September sales of imported cars, trucks and buses in Japan surged 20% to 35,966 from a year earlier. Of the total, 33,715 foreign-made autos were sold, up 23%, while truck sales fell 8.7% o 2,250. Imports increased for the 23rd straight month because of lower prices resulting from a stronger yen and foreign producers' expanded Japanese sales networks, while overall vehicle demand has stalled. This year through September, imported vehicle sales climbed 28% to 284,706.

MACHINE ORDERS: Private machinery orders in Japan fell in August for the second month running, according to the Economic Planning Agency. Private sector machinery orders, excluding those in the shipbuilding and electric power industries, dropped 3.9% month- on-month because of a 8.3% fall in demand from the manufacturing sector.

The fall follows a 6.3% decline in July. Compared with machinery orders in the same month a year ago, August showed a 2.4% growth. If government orders and orders from abroad are included, the August total was 5.9% up from the previous month, and 5.5% up from a year ago.

ECONOMIC GROWTH: Mr. Isamu Miyazaki, director general of the Economic Planning Agency said Japan's economy is expected to recover early next year in response to record low interest rates, a weaker yen, and increased public spending.

The government's chief economic forecaster's comments accompanied the EPA's latest monthly report, which gave a bleak picture of the present state of the economy. The report said the economy still shows "signs of weakness". It cited as evidence a continued rise in stocks of unsold goods and materials in the steel and chemicals industry, record unemployment, slower export growth and slower growth in housing starts. Steel and chemicals inventories both rose in response to weaker demand from the car and housing industries.

A report on bankruptcies underlined the grim situation. The number of corporate collapses in the first half of the fiscal year rose by 9.3% to 7,549, the worst six monthly toll for nine years. They include 21 subsidiaries of Hyogo Bank and Kizo Shinyo Kumai, which collapsed in August.

However, Mr. Miyazaki was encouraged by growing investment in new plant in the electronics and machinery industries. The EPA report said that September's Y14,220 billion pump priming package and record low official discount rate of 0.5% would "combine well" to stimulate activity.

MONEY SUPPLY: Japanese money supply grew at an annual 2.8% in September, from a revised 2.9% in August, according to preliminary report by the Bank of Japan. The sedate growth in benchmark money supply, M2 plus certificates of deposit, came in spite of a radical easing of monetary conditions in September. The Bank of Japan cut the official discount rate on September 8 to 0.5%, the lowest of any leading economy in post-war years and drove money market rates even lower. However, a BOJ official said it was too early to judge the impact of the rate cuts.

A broader measure of liquidity, also including postal savings and government bonds, grew at 3.8% in September, compared with 3.6% in August.

TRADE SURPLUS: Japan's trade surplus fell 5.1% in the six months to September, as slower export growth to the US was partly offset by a sharp rise in trade with the rest of Asia. The third successive year-on-year fall, to $56.18 billion, was driven by a rise in imports, up nearly a quarter in the first half of the fiscal year, and helped by the strength of the yen, which has made foreign goods cheaper than domestic products.

A decline in car exports was the main factor in the first six- monthly fall in four years in Japan's trade surplus with the US. The bilateral trade gap fell by 13.9% to $23.3 billion during the six months.

The trade surplus with the rest of Asia, Japan's fastest growing investment and export market, rose 21.4% for the 11th half-year running, to $38.07 billion, nearly two-thirds more than the surplus with the US.

The September surplus fell 5.8%, year-on-year, to $11.3 billion last month. The surplus with the US declined 23.9% to $4.4 billion. A sharp slowdown in export growth, to 6.9% last month, from 12.6% in August, was the main surprise to economic analysts.

VEHICLE EXPORTS: Japan's motor-vehicle exports for the six months ended Sept. 30 fell 16% from a year earlier to 1.8 million units, the lowest level since 1975. Of the total, auto shipments fell 14% to 1.4 million vehicles, and exports to the US slumped 27% to 614,557. Spurred by the stronger yen, Japanese auto makers have moved more production abroad.

YEN POLICY COST: The Bank of Japan spent the best part of $13.7 billion in September in its attempt to revive the stagnant economy by driving down the yen against the US dollar. That figure represents the increase in the central bank's foreign exchange reserves in September, to set a world record, for the eighth month running, of $179.86 billion, according to the finance ministry. The bulk of the increase, an estimated $11 billion, came from market intervention, with the remainder from profits on managing the banks own funds.

FRANCE

TRADE SURPLUS: France had a FFr9.06 billion ($1.8 billion) trade surplus in August, a sharp rise over the previous month's FFr4.47 billion. The official figures, which took the surplus for the first eight months of the year to FFr72.5 billion, against FFr47.7 billion in the same period in 1994, demonstrated the resilience of French exports. Exports rose from FFr113.2 billion in July to FF118.6 billion, including about FFr2.5 billion from Airbus sales. The trade surplus with European Union partners rose from FFr1.7 billion in July to Fr3 billion. Deficits with Japan, Germany and the US, all shrank. In terms of products, agricultural goods expanded their surplus, as did industrial and military equipment.

INDUSTRIAL PRODUCTION: French industrial production in July/August rose 0.2%, after a fall of 0.3% in June.

MONEY SUPPLY: French M3 money supply rose 0.9% in August, after the July figure was revised to 0.9% from a provisional 1.0% rise.

SOCIAL SECURITY SYSTEM DEFICIT: According to an official audit committee, the deficit in the French social security system is expected to reach FFr64.5 billion ($13.24 billion) this year, which is higher than previously forecast.

According to the Commision des Comptes, the combined deficit in the three main branches of the welfare system - Healthcare, pensions and family allowances - will be about FFr2.5 billion higher than forecast in the July report. The expected total shortfall of Fr64.5 billion compares with a deficit of FFr55 billion last year.

The report by the Commision des Comptes confirmed the gravity of the french financial problems. It comes at a time that prime minister Alain Juppe is preparing reforms aimed at eliminating the deficit by 1997. The issue is regarded as one of the most important challenges facing his administration as a reduction in France's deficits is needed to enable lower interest rates and to satisfy the conditions for European monetary union.

Mr Juppe has said he aims to cut the deficit to FFr30 billion next year and to zero in 1997. Measures are expected to include an increase in the rate or scope of the CSG, a tax on most forms of income, increased contributions from welfare recipients and spending curbs in hospitals.

Although all the branches of the welfare system are in deficit, it is the health insurance system which accounts for most of the shortfall. The gap between receipts and expenditure in the national health insurance scheme is expected to reach FFr36.5 billion this year, about FFr1 billion more than predicted in July. The increase partly reflects a continued rise in health expenditure, despite government pressure for restraint in prescriptions by general practitioners.

BASE LENDING RATES RISE: France's biggest commercial banks announced they were raising their base lending rates from 7.9% to 8.2% - a move which will add to fears about a slowdown in the French economy. The move followed an increase in French market interest rates and a key official interest rate as investors have expressed concern about French economic policy, and about the government's ability to achieve its deficit reduction targets.

DEFICIT REDUCTION PRIORITY: President Jaques CHIRAC set the reduction of France's public deficits as a precondition for all his goals for the country, including joining Germany

AUSTRALIA

CURRENT ACCOUNT DEFICIT: Mr. Kim Beazley, Australia's finance minister, said the federal government would revise downward its current account deficit forecast for 1995/96 in January next year. In the May budget, the government indicated that it expected a current account deficit of A$27 billion ($20.6 billion) in the current financial year - little changed from the 1994/95 figure and about 5.5% of the gross domestic product. However, the slowdown in the economy, coupled with improvement in prices for commodity exports and the ending of the eastern states' drought has lead to an improvement in the trade position. Most analysts expect a 1995/96 trade deficit of around A$22 billion.

INFLATION WARNING: Australia's Reserve Bank, the country's central monetary authority reiterated a warning that annual inflation was expected to increase in the year ahead and, even on an "underlying" basis, exceed 3%. But it is said this would not be "inconsistent with the bank's inflation objective, provided inflation returns to the 2-3% range within a reasonable time". The bank, in its October bulletin, added that the slowdown in Australia's economic growth rate, coupled with the recent recovery in the Australian dollar, should be "more conducive to price stability".

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