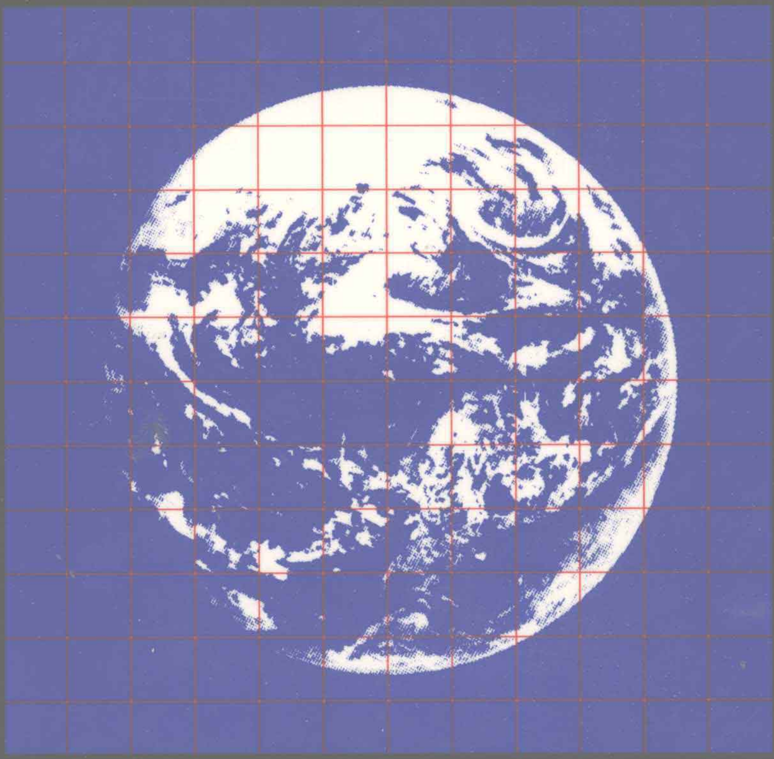
WORLD ECONOMIC AND FINANCIAL SURVEYS

WORLD ECONOMIC OUTLOOK

MAY 1992



INTERNATIONAL MONETARY FUND

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World Economic Outlook

May 1992

A Survey by the Staff of the International Monetary Fund

INTERNATIONAL MONETARY FUND
Washington, DC

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Assumptions and Conventions

A number of assumptions have been adopted for the projections presented in this report. It has been assumed that average real effective exchange rates will remain constant at their March 1–13, 1992 levels except for the bilateral rates among the exchange rate mechanism (ERM) currencies, which are assumed to remain constant in nominal terms; that "present" policies of national authorities will be maintained; that the average price of oil will be $16.68 a barrel in 1992, $17.20 a barrel in 1993, and remain unchanged in real terms over the medium term; and that the six-month U.S. dollar LIBOR will average 4½ percent in 1992 and 5½ percent in 1993. These are, of course, working hypotheses rather than forecasts, and the uncertainties surrounding them add to the margin of error that would in any event be involved in the projections. The estimates and projections themselves are based on statistical information available on April 10, 1992.

The following conventions have been used throughout the report:

. . . to indicate that data are not available;

— to indicate that the figure is zero or less than half the final digit shown;

– between years or months (e.g., 1991–92 or January–June) to indicate the years or months covered, including the beginning and ending years or months;

/ between years or months (e.g., 1991/92) to indicate a fiscal or financial year.

"Billion" means a thousand million.

Minor discrepancies between constituent figures and totals are due to rounding.

* * *

As used in this report, the term "country" does not in all cases refer to a territorial entity that is a state as understood by international law and practice. As used here, the term also covers some territorial entities that are not states but for which statistical data are maintained on a separate and independent basis.

Preface

The projections and analysis contained in the *World Economic Outlook* are an integral element of the IMF's ongoing surveillance of economic developments and policies in its member countries and of the global economic system. The IMF has published the *World Economic Outlook* annually from 1980 to 1983 and biannually since 1984.

The survey of prospects and policies is the product of a comprehensive interdepartmental review of world economic developments, which draws primarily on the information the Fund staff gathers through its consultations with member countries. These consultations are carried out in particular by the Fund's area departments together with the Exchange and Trade Relations and Fiscal Affairs Departments.

The country projections are prepared by the Fund's area departments on the basis of internationally consistent assumptions about world activity, exchange rates, and conditions in international financial and commodity markets. For approximately 50 of the largest economies—accounting for 90 percent of world output—the projections are updated for each *World Economic Outlook* exercise. For smaller countries, the estimates are based on the projections prepared at the time of the regular Article IV consultations with member countries or in connection with the use of Fund resources; for these countries, the estimates used in the *World Economic Outlook* are updated incrementally to reflect changes in global economic conditions.

The analysis in the *World Economic Outlook* draws extensively on the ongoing work of the Fund's area and specialized departments, and is coordinated in the Research Department under the general direction of Michael Mussa, Economic Counsellor and Director of Research. The *World Economic Outlook* project is directed by Flemming Larsen, Assistant Director, together with Peter B. Clark, Chief of the World Economic Studies Division.

Other contributors to the current issue include David T. Coe, Michael Wattleworth, Staffan Gorne, Garry J. Schinasi, Przemyslaw Gajdeczka, Manmohan S. Kumar, Marianne Schulze-Ghattas, Enrique G. Mendoza, and José M. Barrionuevo. Steven A. Symansky, Leonardo Bartolini, and Sheila Bassett generated the model simulations underlying the alternative scenarios. The authors of the annexes are indicated in each case. The Fiscal Analysis Division of the Fiscal Affairs Department computed the fiscal impulse measures. Anthony G. Turner, Sungcha Hong Cha, and Toh Kuan provided research assistance, and Cathy Wright coordinated data processing. Esha Ray of the External Relations Department edited the manuscript and coordinated production of the publication. Susan Duff, Margarita Lorenz-Santin, and Nora Mori-Whitehouse were responsible for word processing.

The analysis has benefitted from comments and suggestions by staff from other departments, as well as by Executive Directors following their discussion of the *World Economic Outlook* on April 6, 8, and 10, 1992. However, both projections and policy considerations are those of the IMF staff and should not be attributed to Executive Directors or to their national authorities.

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World Economic Prospects and Policies

The recent slowdown in the world economy has proved more persistent than projected in the October 1991 *World Economic Outlook* (Table 1). The revised projections suggest that, following a small decline in world output in 1991, growth will recover to about 1½ percent in 1992 before gaining more momentum in 1993. At the time of writing, there were signs of recovery in some of those industrial economies that have been in recession, but some other countries continued to show signs of weakness. Although the sluggishness of many cyclical indicators continues to highlight the downside risks to the short-term projections, there are several positive aspects of the current situation.

- In many of the industrial countries, the recent weakness of activity has occurred under conditions of moderate and generally declining rates of inflation, in sharp contrast to the recessions of 1974–75 and 1980–82 (Chart 1). This has permitted a substantial reduction of short-term interest rates, particularly in North America, but also in Japan and the United Kingdom.
- In contrast to the 1974–75 and 1980–82 episodes, there have been no major supply-side disturbances from commodity markets in the recent phase of slow growth. This is a major reason for the relatively moderate downturn experienced in most cases in 1991 compared with the two previous recessions.
- Some of the main forces behind the weakness of activity in 1991 are no longer at work or are diminishing. The uncertainties related to the crisis in the Middle East have dissipated, and the household and corporate sectors have been reducing their high levels of indebtedness. As financial balances are being consolidated, the basis for a resumption of more satisfactory growth is improving.
- Increased adjustment efforts by many developing countries during the past several years are now beginning to bear fruit. Together with the effect of declining interest rates, this has strengthened their economic performance despite the weakness of activity in the industrial world.

Industrial Countries

Early signs of recovery in the United States and Canada gave way to renewed weakness in the latter part of 1991, while the United Kingdom remained in recession. At the same time, there was evidence of a slowdown in Japan and continental Europe. Activity in North America appears to have strengthened in early 1992 but various indicators continue to point to a hesitant recovery. The main causes of continued sluggishness include the effect on spending of the efforts by households and enterprises to reduce indebtedness and of the weakness of certain asset prices. In Europe, growth also has been restrained by the persistently high level of real interest rates. More generally, business and consumer confidence deteriorated again in a number of countries in late 1991 following earlier improvements.

With the weakening of activity, short-term interest rates have been lowered considerably in the United States, Canada, Japan, and the United Kingdom. In view of the low rates of capacity utilization (except in Japan) and the slowdown in the growth of liquidity, the decline in interest rates has helped to cushion the downturn and improve the prospects for recovery without increasing inflationary pressures. Barring evidence that recovery is faltering, however, further easing would not seem warranted, and the monetary authorities should stand ready to tighten promptly in response to signs of an increase in potential inflationary pressures. In this context, the behavior of monetary aggregates should be closely monitored to prevent overshooting of liquidity growth as occurred during the recoveries following the two previous downturns.

In Europe, growth slowed considerably during 1991 and is expected to remain subdued in 1992. Structural impediments continue to hamper higher sustainable growth, and several of the smaller countries are in the process of adjusting to financial strains that emerged in the latter part of the 1980s. A recent restraining factor has been the tight monetary stance in Germany, which is required to contain inflationary pressures associated with rapid monetary growth, the sharp increase in the budget deficit in 1990–91 in the wake of unification, and strong wage pressures. For some of Germany's partner countries, the spillover effects of tighter monetary conditions have been consistent with the need to reduce inflation further. However, for most European countries, the spillover has restrained demand when activity was already generally quite weak, and when inflation was abating.

Slower growth in Germany in 1992 should help to dampen inflationary pressures and may well result in

Table 1. Overview of the Projections
(Annual changes in percent, unless otherwise noted)

			Current Projections		Differences from October 1991 Projections[1]	
	1990	1991	1992	1993	1991	1992
World output	2.2	−0.3	1.4	3.6	−0.8	−1.3
Industrial countries	2.5	0.8	1.8	3.3	−0.5	−1.0
United States	1.0	−0.7	1.6	3.5	−0.4	−1.4
Japan	5.2	4.5	2.2	3.9	−0.1	−1.2
European Community	2.9	0.8	1.8	2.8	−0.7	−0.5
Developing countries excluding Eastern Europe and former U.S.S.R.	3.5	3.3	6.7	5.4	0.7	1.0
Africa	0.9	1.4	2.7	3.0	−1.4	−0.3
Asia	5.6	5.8	5.5	5.7	0.8	0.3
Middle East	4.2	0.4	15.0	7.3	0.7	4.1
Western Hemisphere	−0.1	2.8	2.7	4.2	1.3	—
Eastern Europe and former U.S.S.R	−2.9	−16.9	−14.6	. . .	−6.6	. . .
Eastern Europe[2]	−7.1	−16.6	−1.0	3.9	−4.6	−3.3
Former U.S.S.R.	−2.0	−17.0	−17.5	. . .	−7.0	. . .
Memorandum						
Developing countries excluding Eastern Europe, former U.S.S.R., and Middle East	3.3	4.2	4.2	4.8	0.8	0.3
World trade volume	4.1	3.3	5.0	6.3	2.6	—
Industrial country import volume	4.5	2.5	3.5	5.6	0.8	−1.1
Developing country import volume	4.1	6.5	9.2	7.8	8.2	3.0
Commodity prices						
Oil[3]	28.2	−17.0	−8.9	3.1	−0.6	−9.8
(In U.S. dollars a barrel)	22.04	18.30	16.68	17.20	−0.13	−1.93
Non-fuel[4]	−7.9	−4.7	1.2	4.2	1.0	−2.0
Consumer prices						
Industrial countries	4.9	4.4	3.3	3.2	−0.2	−0.5
Developing countries excluding Eastern Europe and former U.S.S.R.	80.0	41.4	37.6	16.1	3.7	16.1
Eastern Europe and former U.S.S.R.	22.0	92.8	713.5	. . .	−23.7	. . .
Eastern Europe[2]	149.1	134.7	95.0	44.0	36.2	66.9
Former U.S.S.R.	5.6	86.0	1,000.0	. . .	−34.0	. . .
Six-month LIBOR (in percent)[5]	8.4	6.1	4.5	5.5	−0.5	−2.5

Note: Real effective exchange rates are assumed to remain constant at the levels prevailing during March 1–13, 1992, except for the bilateral rates among the ERM countries which are assumed to remain constant in nominal terms. This implies an effective depreciation of the U.S. dollar by about 2 percent relative to the assumption underlying the October 1991 *World Economic Outlook*.

[1] These figures are not equal to the difference between the current projections and the projections for country aggregations shown in the October 1991 *World Economic Outlook*. Rather, the latter were revised using updated weights which were also used in the current *World Economic Outlook* (see Statistical Appendix, p. 97), and the differences shown here are therefore based on aggregates using the same updated weights.

[2] The countries in Eastern Europe comprise Bulgaria, the Czech and Slovak Federal Republic, Hungary, Poland, Romania, and Yugoslavia.

[3] Simple average of the U.S. dollar spot price of U.K. Brent, Dubai, and Alaska North Slope crude oil; assumptions for 1992 and 1993.

[4] In U.S. dollars; based on world export weights.

[5] London interbank offered rate on six-month U.S. dollar deposits; assumptions for 1992 and 1993.

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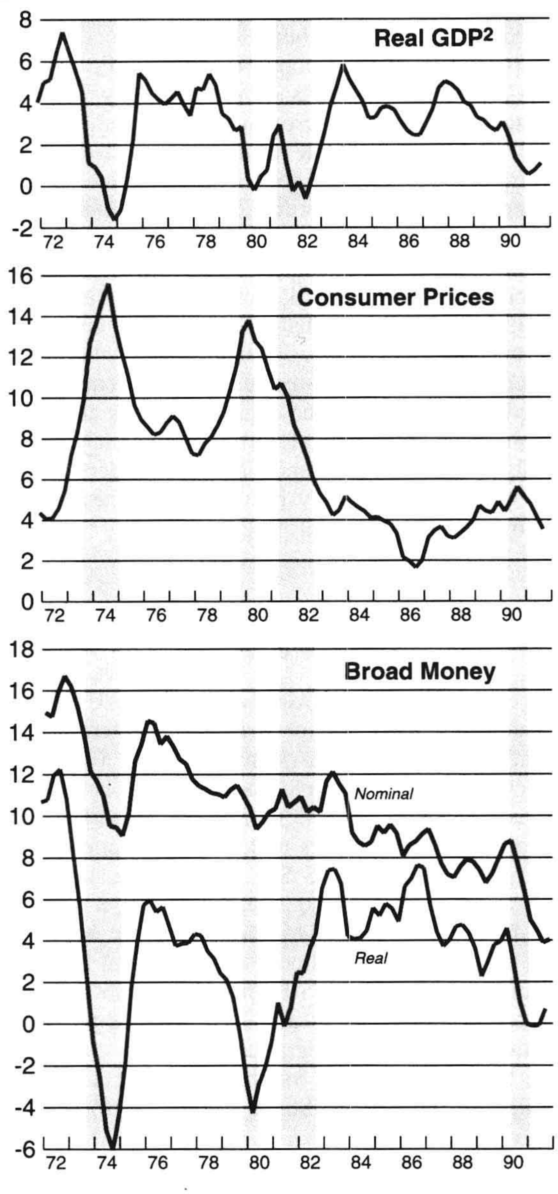
Chart 1. Six Major Industrial Countries: Output, Inflation, and Money Supply[1]
(Percent change from four quarters earlier)



[1]Data for the United States, Canada, Japan, France, Italy, and the United Kingdom. Germany is not included because of the break in the monetary data in 1990 following unification. Consumer prices exclude the impact of mortgage interest rates. The change in the real money supply is defined as the change in the nominal money supply less the change in consumer prices. All indicators are computed using GDP-weighted averages of changes in the series for each country. Shaded areas represent periods of recession in the United States as defined by the National Bureau of Economic Research (NBER). The NBER has July 1990 as the start of the most recent recession in the United States, but has not yet dated the end of the recession; for the purposes of this chart, the end of the recession is put at the first quarter of 1991, which was followed by three quarters of positive GDP growth.

[2]GNP for Japan.

some easing of money market conditions, but the prospects for lower interest rates in Europe would be enhanced if Germany's fiscal consolidation plans were implemented more rapidly than currently envisaged. For other European countries, including potential future members of the European Community (EC), economic policies are guided by the need to safeguard or strengthen the credibility of the authorities' commitment to meet the convergence criteria for economic and monetary union, to continue progress in reducing inflation, and to enhance medium-term growth prospects.

More generally, it is essential that the response to the short-term policy concerns be consistent with the medium-term growth strategy followed since the early 1980s. The basic objectives of this strategy include the achievement of a high degree of price stability—which may be defined as a low and stable rate of inflation that does not distort economic decisions; the promotion of saving, especially by reducing public sector deficits; and the elimination of obstacles to an efficient allocation of resources and to high employment through appropriate structural reforms.

Allowing interest rates to decline during a period of sluggish economic activity, moderating inflation, and below-target growth of monetary aggregates should not be viewed as a departure from the medium-term strategy, but rather as symmetric to a nonaccommodating monetary stance when output exceeds potential. Similarly, if the underlying fiscal position is on the medium-term adjustment path, allowing the automatic budgetary stabilizers to operate during a recession should be viewed as symmetric to deficit reduction through rapid growth of tax revenues during phases of recovery. These policy rules obviously will not prevent cyclical fluctuations, but they may help prevent policy mistakes as have often occurred in previous postwar business cycles.

The extent to which these principles can be applied in particular cases during a period of cyclical weakness will depend on progress toward the medium-term objectives. For most of the industrial countries, the record in this regard is mixed. An important achievement has been the marked improvement in price and growth performance in the industrial world during the past decade, following the stagflation of the 1970s and early 1980s. At the same time, structural reforms and other elements of the strategy still remain to be fully implemented. In addition, the failure to eliminate unsustainable budget deficits in some countries—especially the United States, Italy, and Canada—during the long period of expansion in the 1980s is a major reason for the persistently high level of real long-term interest rates and for the steepness of yield curves. The large structural budget deficits constitute the single most important obstacle to the achievement of satisfactory noninflationary growth over the medium term. They also imply that any easing of fiscal policy would only aggravate the upward pressure on long-term interest rates and further undermine confidence.

The unfinished task of fiscal consolidation underlines the crucial importance of resuming progress toward deficit reduction. Canada is now in the process of implementing a strategy aimed at substantially eliminating the budget deficit by the mid-1990s. In the United States, the Budget Enforcement Act of 1990 provides a useful step but recent budget projections show that further significant adjustment needs to be undertaken over and above the provisions of the Act. In Europe, budget consolidation is a major priority in the Maastricht agreement on convergence criteria for participation in the final stage of economic and monetary union in the EC. The challenge ahead will be to implement these objectives in the context of a reinvigorated medium-term strategy.

The industrial countries also have the main responsibility to work toward a successful outcome of the Uruguay Round of multilateral trade negotiations. A collapse of these negotiations could adversely affect business confidence—which is already fragile. It would also lead to a further increase in trade tensions and threaten global economic performance. A decisive political effort by the EC, the United States, and Japan is required to break the current deadlock. Strong political support is also needed to defuse trade tensions and roll back the impediments to trade built up in recent years.

Developing Countries

The developing countries as a group (excluding Eastern Europe and the former U.S.S.R.) are expected to see a strengthening in growth performance during the period ahead, with real GDP growth projected to average 6 percent a year in 1992–93, compared with 3½ percent in 1990–91. Most of this strengthening reflects the recovery of output projected for the Middle East region. In addition, there is evidence of improved performance in a growing number of countries as a result of their stabilization and reform efforts. The decline in short-term interest rates in North America and Japan—which is providing relief for heavily indebted countries—and the projected recovery in the industrial countries should also contribute to stronger growth.

The role of domestic policies in improving the outlook for the developing countries is most apparent in the Western Hemisphere. Many of these countries experienced a strengthening of growth in 1991 notwithstanding the unfavorable external environment, and they are expected to continue to improve their performance on the basis of sustained expansion of investment and exports. In some cases these developments have been accompanied by clear signs of a reversal of capital flight and a resumption of direct investment and other spontaneous capital inflows.

In conjunction with comprehensive structural reforms aimed at enhancing the efficiency of resource allocation, fiscal consolidation and monetary restraint have been the key elements of successful adjustment policies and of greater resilience in the face of adverse external developments. Elimination of excessive fiscal deficits helps to raise domestic saving and reduce reliance on foreign borrowing, and it is instrumental in improving confidence and encouraging private investment. There is substantial evidence that fiscal consolidation can contribute to stronger economic performance and—if accompanied by cuts in nonproductive public expenditures—can do so without sacrificing priority areas that are crucial for economic growth and social equity.

One of the most visible results of the strengthened debt strategy has been the decline in aggregate debt and debt-service ratios. The reduction in debt burdens has taken place primarily in the highly indebted middle-income countries. In contrast, progress in alleviating the debt burden of the small low-income economies—including those in sub-Saharan Africa—has been slow. The Paris Club has recently expanded the concessionality of official bilateral debt-restructuring agreements in cases justified by the needs of the debtor countries and by the strength of their adjustment efforts. Commercial creditors must also continue to implement appropriate debt-restructuring options on a timely basis for countries that are pursuing strong adjustment programs.

Eastern Europe and the Former U.S.S.R.

Part of the slowdown in world activity in 1991 reflected the dramatic contraction of output in Eastern Europe and the former U.S.S.R. A major factor behind the contraction has been the inevitable—albeit larger-than-expected—costs of transition from the distortions and misallocations of resources under central planning. The inability of the former U.S.S.R. to maintain supplies of energy and raw materials to its partner member countries of the former Council for Mutual Economic Assistance (CMEA) and Eastern Europe's large terms of trade loss vis-à-vis the former U.S.S.R. have also contributed to the drop in output. There are, however, signs that the economic contraction is beginning to bottom out in some of the Eastern European countries. In contrast, in the republics of the former Soviet Union, further output losses may be in store.

The reform process in Eastern Europe was characterized by an early and welcome liberalization of prices, trade, and exchange markets. Efforts to control inflation generally have been less successful, partly because of difficulties in consolidating fiscal positions under conditions of severely declining output. While stabilization policies must continue to receive high priority, the acceleration of institution-building and structural reforms to stimulate supply is also essential to limit the costs of transition.

Reform of the financial sector, a hardening of budget constraints, and measures to privatize state assets are particularly urgent. Where privatization cannot be achieved immediately, it is important to establish commercial accountability and incentive structures within state-owned enterprises. To ensure the success of the transformation process, it is also vital that the rest of the world open their markets to the exports of the reforming countries. Some steps in this direction have been taken by the EC and other industrial countries, but further measures are required to remove remaining obstacles, particularly for agricultural products.

For the republics of the former Soviet Union and other economies that have begun the process of transition from central planning to a market-based economic system, including some Asian countries, the experience of Eastern Europe underlines the need for a comprehensive approach to structural reform, as well as for a decisive effort at stabilization. The Baltic countries and the other states of the former U.S.S.R. are also facing the challenge of averting a collapse of inter-republic trade. To achieve financial stability and to maintain an open trading environment within the ruble area it will be necessary for the Russian Federation and other republics to establish closer coordination of economic policies and, in particular, a more unified approach to price reform and to monetary and exchange rate policy. It is also a matter of urgency to dismantle inter-republic export barriers and other obstacles to mutually beneficial trade.

Republics that decide to introduce separate currencies—and several have already announced their intention to do so—will have greater scope to pursue more independent financial policies. However, the need for a strong stabilization effort will be no less urgent than in the ruble area, particularly if the authorities are aiming to achieve convertibility at an early stage. Furthermore, cooperative efforts on trade and payments issues will be crucial to the common task of successful economic restructuring. For the international community, it is a major challenge to respond to the needs of the republics for guidance and financial assistance as they struggle to overcome the legacies of the past.

* * *

This *World Economic Outlook* incorporates for the first time data for east Germany. From 1991 onward, all estimates for Germany refer to the unified country, unless stated as applying to west Germany. Through 1990, national accounts data and indicators of domestic economic and financial activity apply to west Germany only, while data for central government and the balance of payments cover west Germany through mid-1990. Because of the break in the data for Germany, developments over time, and comparisons with previous issues of the *World Economic Outlook*, should be interpreted with care. Data for the former U.S.S.R. refer to the geographical area covered by the federation until the recent independence of the constituent republics.

Industrial Countries

Economic activity continued to be sluggish in the latter part of 1991 and early 1992 in North America, the United Kingdom, and several smaller industrial countries that have been in recession. In addition, signs of a slowdown became apparent in a number of other industrial countries. As a result of persistent weakness, some countries have eased the thrust of policy with the aim of supporting activity. The significant decline in short-term interest rates in North America and Japan—made possible by the continued moderation of inflation—is expected to contribute to a strengthening of growth during 1992.

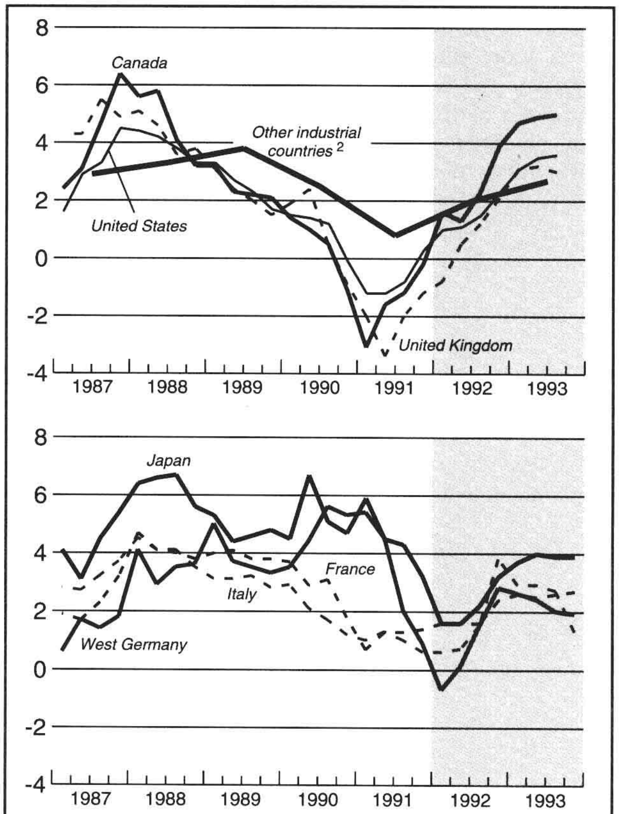
Only in a few cases have expansionary fiscal measures been adopted, a reflection of the priority attached to the medium-term objectives that have guided policy since the early 1980s. Indeed, several countries appear to have pursued a relatively tight fiscal stance in 1991, partly offsetting the automatic stabilizers. The limited room to ease the thrust of fiscal policy can be attributed to the large structural budget deficits that persist in a number of countries, and the considerable gaps between the fiscal imbalances and the authorities' medium-term deficit targets. Recent slippages suggest that major efforts will be required over the next few years to bring fiscal consolidation back on track, particularly in the United States and Italy, but also in some of the smaller industrial countries. In Germany, where unification necessarily led to a major budgetary imbalance, consolidation is required in the coming years to reduce the deficit to a sustainable level.

Performance in 1991 and Prospects for Recovery

Economic growth in the industrial countries declined from 2½ percent in 1990 to ¾ of 1 percentage point in 1991. The slowdown reflected recessions in North America, the United Kingdom, and a number of smaller industrial countries, as well as slower growth in Japan and continental Europe, particularly in Germany (Chart 2). A modest rebound is expected during 1992, even though average growth may not exceed 1¾ percent for the year as a whole; this would be about 1 percentage point below the projection in the October 1991 *World Economic Outlook.*[1]

A number of factors account for the weaker-than-expected performance in 1991 and the lackluster nature of the projected recovery: adjustments in private sector financial positions (discussed more fully in Annex I) and a renewed worsening of consumer confidence in most of

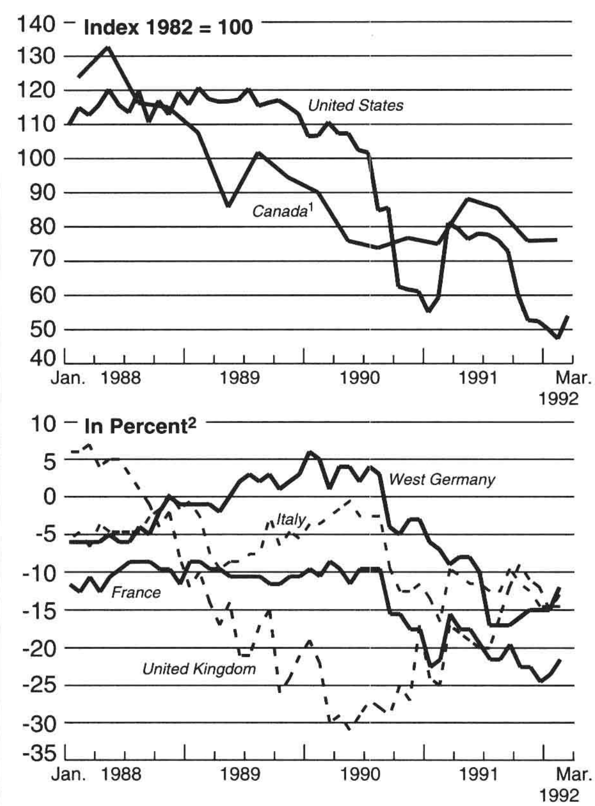
Chart 2. Industrial Countries: Growth of Real GDP[1]
(Percent change from four quarters earlier)



[1]GNP for west Germany and Japan. Shaded areas indicate staff projections.
[2]Annual observations, as quarterly data are not available for some countries.

[1] Although the downward revisions to the forecast for economic growth in 1991 and 1992 in this and the three previous *World Economic Outlooks* are significant, forecasting errors are typically large during periods of major cyclical fluctuations. It should nevertheless be noted that the forecasting record of the *World Economic Outlook* for the major industrial countries has improved in recent years (see Annex VIII).

Chart 3. Six Major Industrial Countries: Indicators of Consumer Confidence



Sources: United States, the Conference Board; Canada, the Conference Board of Canada; and for the lower panel, European Community.

[1]Quarterly observations.

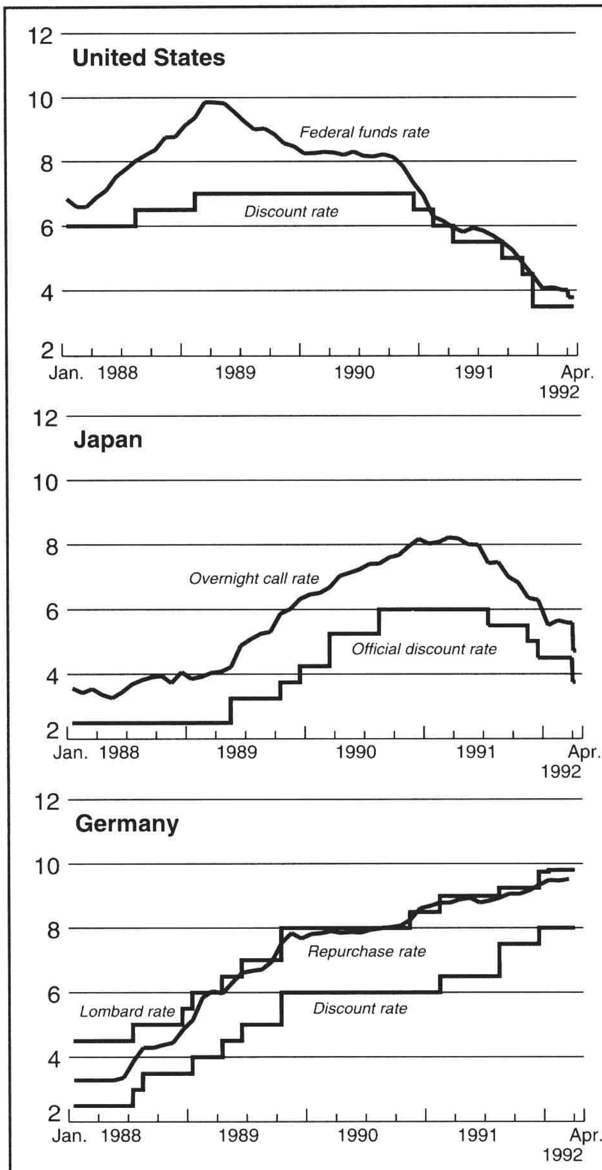
[2]The percentage of respondents expecting an improvement in their situation minus the percentage expecting a deterioration.

the major industrial countries (Chart 3); increased taxation and the tight stance of monetary policy in Germany as well as relatively high interest rates in the rest of Europe; and a reduction in the growth of business investment spending in Japan. These factors also highlight the uncertainties that attach to the near-term outlook.

Monetary and Fiscal Developments

Monetary conditions have mirrored the different cyclical positions of the three major industrial countries in 1991 (Charts 4 and 5; Annex VI). To support activity against a background of reduced inflationary pressures, the U.S. Federal Reserve lowered both the discount rate and the federal funds rate by about 3 percentage points during 1991, with the discount rate falling to its lowest level since 1964. There was a further reduction of ¼ of 1 percentage point in the federal funds rate in April 1992, amid signs of a weak recovery. The Bank of Japan lowered its discount rate from 6 percent to 4½ percent during 1991 as growth slowed, and the overnight call rate also fell by over 2 percentage points. On April 1,

Chart 4. Three Major Industrial Countries: Policy-Related Interest Rates[1]
(In percent a year)



[1]End of month except for the federal funds rate, which is the average of daily observations, and the repurchase rate, which is the average of weekly data.

Chart 5. Major Industrial Countries: Real Interest Rates[1]
(In percent a year)

[1]Interest rates deflated by the annual increase in the GDP deflator; annual averages through 1989 and quarterly data for 1990-91.
[2]A weighted average of yields on government bonds with remaining maturities of ten years or nearest, using 1987 GDP weights.
[3]Three-month certificate of deposit rates for the United States and Japan; three-month treasury bill rate for Italy; rate on three-month prime corporate paper for Canada; and three-month interbank deposit rates elsewhere with the following exceptions: Eurodollar rate for the United States before 1976; Gensaki rate for Japan before July 1984; money market rate for France before 1970; and the discount rate for Italy before 1978.

1992 Japan's discount rate was lowered further to 3¾ percent in view of weaker domestic activity and recent trends in prices, money supply, and market interest rates. In contrast, the Bundesbank raised both the discount rate and the Lombard rate to historically high levels by the end of 1991—8 percent and 9¾ percent, respectively—in response to inflation rising above 4 percent, strong wage pressures, and growth of M3 at the top of the target range. Due to the requirements of the exchange rate mechanism (ERM) of the European Monetary System

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