## cak growth, low inflation and monetary policy is too tight and th

whilst inflation falls then the stance of passed on in the form of lower interest from Mr Blair, But the benefits of low has been the message from successive said that low inflation is a pre-condition tion for low interest rates. Often it is or sustainable economic growth. This Chancellors and But inflation need to be for this to be true the main justificasays Gerard Lyons appropriate for Europe, style interest rates are -203et 15At 3niwoda ni beəl ərt gnixlst

rate cut has improved UK rates, the charge of another base factors remain the main influence on where in Europe, Although domestic alyst for much needed rate cuts elsewas fully justified and provided the catcut their key repo rate from 3.0% should be welcome. T day's decision by the Bundesbank to Low inflation is interest rates will remain low tight fiscal policies mean for some time. This casing

through high interest rates. tionary mentality but meant many which not only reinforced this defladue to the Exchange Rate Mechanis anti-inflationary policies. It was also tion in the 1970s led to the adoption excessively tight. monetary policy in Europe has been because the analysis UK interest rates are too hi Throughout the 1980s and 1990s experience of high infla This was partly

can hamper growth.

3.55%. Far from being too low, on UK, by contrast, interest rates are 5.75% whilst headline inflation is guide to the stance of policy. In the that German 'real' interest rates ing official rates for inflation mean and the discount rate is 2.5%. Adjust-In Germany inflation is now Thus 'real' interest rates are Real interest rates give a 1.6% Sis CC

borrowers and penalising savers.

Although the data immediately ahead rest of the seventies a surge in inflation real interest rates were 1.6% and from pean countries had negligible real inter-1968-73 were only 0.1%. During the est rates. Between 1960-67 Britain's Throughout the sixties most Euro-

improving, the recovery is still weak suggested the German economy was Bundesbank meeting

countries have yet to fully follow suit, Just in Germany but across Europe. The Germans have learnt this, but other rates seen in the 1960s is more appropriate for monetary policy now and not from 1974-79. The level of real interest real interest rates between 1960-67 and Bundesbank eased policy, real interest rates have dropped steadily and are rates were 3.7%. In recent years, as the In the 1980s, Germany's 0.9%, the same level as German real interest

try, the discount rate, currently at an DM to weaken. And if it doesn't, there-by causing problems for German indusremain low for some time. Second, they wish to see a weaker DM. I expect the There were two clear messages the First, German interest rates are set to Bundesbank wanted to send this time. thing the German economy needs. strengthened. A stronger DM is the DM to weaken, only not to deliver a rate cut. The DM subsequently cials hinted at an easing, helping the tion. In July, various Bundesbank offifully aware of the likely market reac-The Bundesbank would have been last

structural change suggests the recovery will remain weak. In July last year the

supply growth slowing and the inflation outlook good this justified the easing. ctary growth and inflation. With money still a stable relationship between mon-Bundesbank's research showed there is

3 interest rates and have consistently been too pessimistic about European start of last year financial markets have particularly as problems for the franc would have boosted the mark. Since the pressure in favour of EMU and also because the Germans would have been keen to avoid a French currency crisis overlooked the strong domestic case for there must have been some indirect mine its credibility by cutting rates solely to help the French. Of course the Bundesbank is not going to undercut rates just to help the French, But

suit with rate cuts. The French have been European countries. Many have followed a softer DM is good news for other lower rates in Germany, and elsewhere. Low German rates and the prospect of

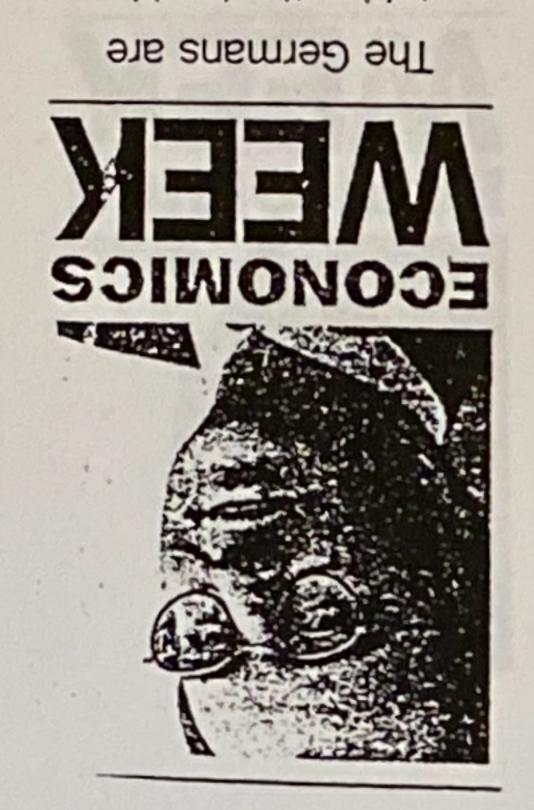
cut, with many believing the Germans The financial markets have been sus-picious of the intentions behind the rate all-time low of 2.5%, could fall again,

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Bank of France may resist of extremely low interest rates but the pursue a Japanese style monetary policy pressure from the French Government on the franc has lifted. But there is still move, as they have cut rates the pressur the main beneficiaries of the German hurdle. Even Germany faces problem chances but fiscal policies remain the The latest rate cuts improve EMU?

European interest rates to stay low. problems too. By mid-October, ten bility but it will add to the pressure for Cities and Municipalities warned that local government was on the brink of not be viewed as credible by the markets, potentially causing currency ins 1997 budgets. Some budget plans may Last week the German Association o European countries will unveil their

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