BANCA D'ITALIA

ABRIDGED VERSION OF THE

REPORT

FOR THE YEAR

1962

PRESENTED TO THE

ORDINARY GENERAL MEETING OF SHAREHOLDERS

HELD IN ROME ON 31st MAY, 1963

ROME
PRINTING OFFICE OF THE BANCA D'ITALIA
1963

BANCA D'ITALIA

ABRIDGED VERSION OF THE

REPORT

FOR THE YEAR

1962

PRESENTED TO THE

ORDINARY GENERAL MEETING OF SHAREHOLDERS

HELD IN ROME ON 31st MAY, 1963

ROME
PRINTING OFFICE OF THE BANCA D'ITALIA
1963

CONTENTS

REPORT OF THE GOVERNOR

I. *General Economic Conditions*

The pattern of cyclical movements in the three major areas of the Western industrial world, the European Economic Community, the United Kingdom and the United States, which had displayed some striking divergencies in recent years, tended to become more uniform in 1962.

In all the major industrial countries the pace of economic expansion slowed down, the first symptoms having appeared in Europe as early as the summer of 1961, but in the United States not until the following spring. In Europe, the phenomenon was accompanied by a rapid increase in labour costs and an appreciable rise of domestic prices, while in the United States both remained remarkably stable (Table 1).

Other important aspects of the Western world's economy last year were a far-reaching redistribution of income to the detriment of profits and the benefit of wages in a number of countries, considerable changes in the composition of industrial production (Chart 1), a slight easing of labour shortages on the European continent and the concurrent persistence of unemployment in the Anglo-Saxon countries, and, finally, a tendency for international trade and balances of payments to come closer to equilibrium.

On the average, European expansion slowed down rather less than it had done in 1961, but there were considerable differences in intensity and characteristics as between various areas and countries. In the European Economy Community, a rate of expansion of 4.5 per cent last year compared with 5.2 per cent in 1961; in the United Kingdom, stagnation was almost

Domestic Prices and Wages

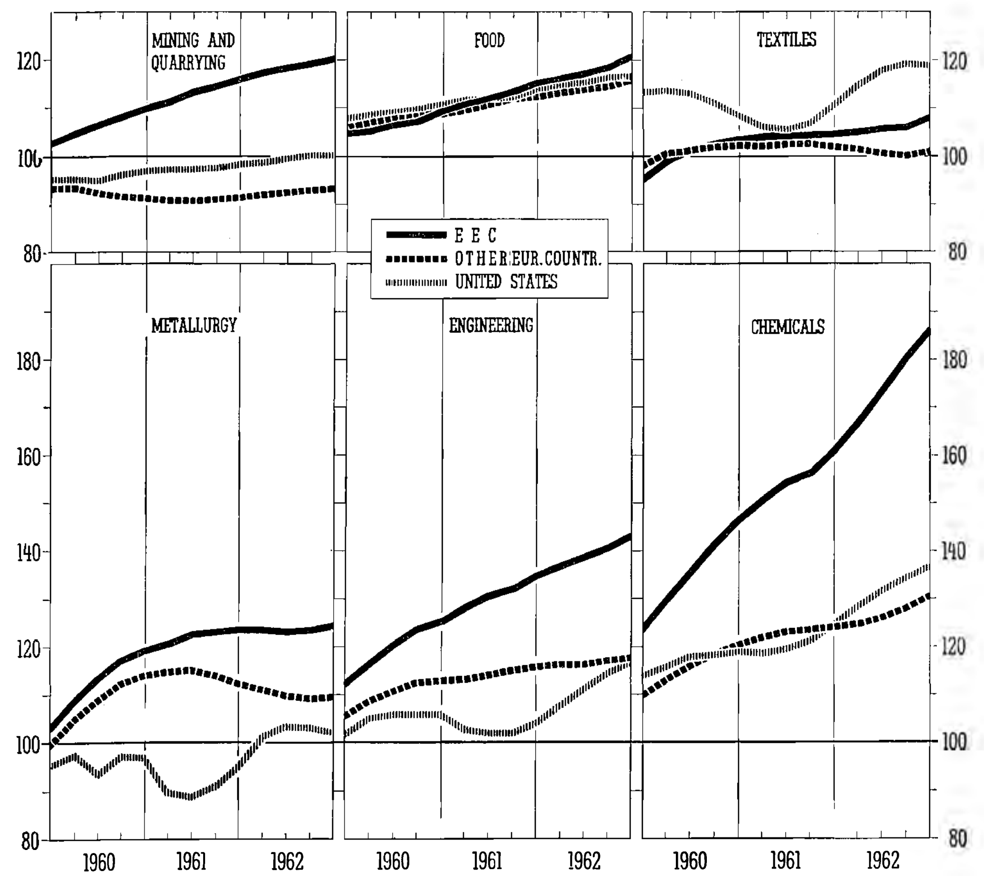
TABLE 1

(annual percentage changes)

Country	Wholesale prices		Retail prices		Hourly earnings in manufacturing industry	
	1961	1962	1961	1962	1961	1962
France	2.1	2.7	3.3	4.9	7.7	8.2
Western Germany	1.4	1.1	2.5	3.5	10.1	10.9
Italy	0.2	3.0	2.1	4.7	7.3	14.9
Belgium	— 0.2	0.8	1.0	1.4	3.6	7.7
Netherlands	— 0.7	0.9	1.7	3.3	12.7	8.9
Sweden	1.8	1.8	2.4	4.7	8.7	7.4
Austria	2.1	5.4	3.6	4.4	11.0	8.7
United Kingdom	2.6	2.3	3.4	4.3	6.5	3.4
United States	— 0.4	0.3	1.1	1.4	2.3	3.0

Sources: O.E.C.D. and official national statistics.

CHART 1



Industrial output in major branches

(12-month changes at quarterly intervals - 4th quarter 1957 = 100)

complete. Within the E.E.C. itself, at the same time, there were differences in the behaviour of the separate components of aggregate supply and demand.

The E.E.C., the United Kingdom and the United States.— In the European Economic Community, France alone was the conspicuous exception to escape a general cyclical downswing, which elsewhere was caused by the weakness of foreign demand and, above all, by the slower expansion of investment demand. By contrast, consumer demand, though varying in intensity from one country to another, went ahead at very nearly the same rate as in the preceding year and so became the main impulse factor in this faltering cyclical phase (Table 2).

TABLE 2

Growth Rates of Real Demand

(annual percentage changes)

Country	Private consumption		Public consumption		Gross fixed investment		Gross domestic product		Exports of goods and services	
	1961	1962	1961	1962	1961	1962	1961	1962	1961	1962
France	5.5	5.8	4.6	5.2	8.0	5.8	4.6	5.2	11.5	8.7
Western Germany	7.3	5.2	7.2	10.2	10.1	6.3	6.7	5.8	3.6	4.9
Italy	7.7	6.6	3.2	5.3	12.4	8.9	8.3	6.8	17.6	11.6
Belgium	2.6	2.5	4.5	5.0	8.2	4.7	3.9	3.0	5.9	7.5
Netherlands	4.5	4.5	2.9	4.0	7.4	5.1	4.6	3.1	3.7	5.5
United Kingdom	1.4	1.4	5.4	2.2	7.1	− 2.0	1.3	0.1	3.2	1.3
United States	2.0	4.6	5.7	7.0	− 0.6	8.2	1.7	5.7	2.0	4.0

Sources: O.E.C.D. and official national statistics.

The United Kingdom followed up its very slow expansion of 1961 with almost complete stagnation last year.

The direction in which the components of total demand moved was much the same as in the European Economic Community, but the checks were stronger and the impulses weaker. Investment demand actually declined as a result of sharp contraction in the machinery and industrial equipment branches; general causes were further reinforced by the atmosphere of uncertainty due to the protracted Brussels negotiations, and by the growing volume of unutilized capacity. Foreign demand remained almost stationary because of the competitive weakness of British industry. Even consumption demand, especially from the private sector, expanded only at a slow pace. Industrial output increased by less than 1 per cent.

Now, the United Kingdom's National Economic Development Council has set a target rate of 4 per cent for expansion in 1963, that is, only a little less than the European Economic Community; but the achievement of this target rate is held to be contingent upon the containment of cost rises within the limits of productivity rises and upon support for sterling through international co-operation.

In the United States the initially vigorous recovery which set in early in 1961 carried the economy to new high levels in the course of 1962, but lost much of its impetus in the latter half of the year (Chart 1). Although a real increase of 5.3 per cent raised GNP to 544 billion dollars, hopes of an early absorption of unutilized capacity were sadly disappointed.

Investment demand was the principal protagonist both of the initial spurt and the subsequent slackening. Foreign demand rose only a little. As in Europe, consumption demand was the really strong sustaining factor: public consumption, with its slight cyclical sensitivity, remained high throughout the whole period, especially in the space industry and defence; private consumption had a continuous rising trend, especially in the consumer durables sector (Table 2). Industrial output rose in all major branches, and in the aggregate by 8 per cent over the preceding year.

The Present Outlook.— The current business cycle in which the Western world now finds itself, has taught us one clear lesson: it is that the cyclical problems of the major industrial countries display growing similarity in an international economic setting in which Italy, after her unprecedented industrial spurt, now occupies a secure place.

We have also had yet another clear demonstration of the close interdependence between the fundamental objectives of economic policy, namely, development, high employment levels, balance-of-payments equilibrium and price stability: failure in any one of these compromises the achievement of the others.

An active development policy demands appropriate measures in the fields of education, research, public health and organization, the elimination of monopolistic practices and restrictions, and economic and financial intervention to encourage investment and to improve the channels through which saving reaches investors. On the other hand, the premise of an active development policy is the maintenance of an appropriate rate of increase in aggregate demand, which conditions the optimism of entrepreneurs and the level of employment. Any structural imbalance in international payments due to a diminution of competitive strength abroad is bound to have such psychological repercussions on business that it becomes difficult or impossible to maintain demand at adequate levels, and it may even constrain governments to interrupt the process of growth. But competitive strength abroad, on which last year's Annual Report laid particular stress, depends in its turn on domestic price stability. Whether prices are pushed up by cost inflation or pulled up by demand inflation, their rise directly or indirectly affects the rate of development and hence, ultimately, the level of employment.

The events of the past few years are particularly instructive in this respect.

Throughout the United Kingdom's postwar attempts to speed up the expansion of the economy, one balance-of-payments crisis after another forced the government to put into reverse after a while the expansionary measures it had adopted. If, today, the British are launching forth upon a new experiment with the declared intent not to take the balance-of-payments effects too seriously for the time being, they can do so in reliance upon international co-operation and in the knowledge that cyclical swings on the continent have created a margin of external competitiveness in their favour which should be sufficient to vouchsafe success for the new course. In the absence of such involuntary assistance from abroad, they would certainly find the going much harder.

The difficulties which the German monetary authorities encountered in 1959 and 1960 in their attempt to cool down the overheated boom created by excessive demand expansion must be ascribed to the government's failure to supplement monetary action with other economic policy measures. As a result, the already conspicuous surplus in the German balance of payments was further swollen by an inflow of capital, which was highly undesirable in these circumstances. Ultimately, the imbalance had to be removed by revaluing the currency.

A very similar situation exists today in Switzerland, where the boom does not appear to be easily amenable to monetary treatment alone. Exclusive reliance on monetary measures would attract capital from abroad, which would increase domestic liquidity and so contribute to a further expansion of total demand.

In the United States, the current situation is one of internal imbalance, the symptoms of which are a low rate of growth, insufficient utilization of available productive capacity including manpower, and an adverse balance of payments. It is true that the external deficit is due not to current trade, which indeed shows large surpluses, but to net private capital exports, to public capital exports and to military expenditure abroad—and these latter factors, of course, are to a large extent outside the control of monetary authorities. Obviously, expansionary action designed to stimulate the economy, such as the President's tax reduction proposals, threatens, at least initially, to make inroads into the current trade surplus and so to aggravate the overall balance-of-payments deficit.

In the European Economic Community wages tend to rise much faster than productivity. The movement varies in intensity from one country to another, but it is a general one and has gradually been gathering speed over the last two years, and especially since the second half of 1962. This cost inflation was, in part, translated into a strong rise of domestic prices, followed necessarily by a weakening of external competitive strength; in part, it cut into profit margins and consequently diminished self-financing capacity. Firms are finding it difficult to make good this deficiency by raising more outside finance, given that the wage earners' and the entrepreneurs' propensities to save are altogether different.

There is more than one way, therefore, in which cost inflation can quickly check expansion and cause unemployment. In some countries, like Germany and the Netherlands, wages were also pushed up by the long-standing excess of aggregate demand; in France and Italy, wages had long lagged behind productivity and now quickly caught up with it, and the wage rise was further reinforced by the diffusion of sectoral labour shortages. But whatever may have been the original cause of cost inflation, and leaving aside the circumstance that it may appear to be a " normal " feature of the final phase of a boom, there can be no doubt that the monetary authorities cannot combat cost inflation effectively by means of a general credit restriction, which would simply stop economic expansion dead in its tracks. Whether the monetary authorities do something or do nothing, the result would, paradoxically, be the same sooner or later: expansion would be checked and unemployment would ensue.

The cyclical problems which, at the present moment, claim the urgent attention of monetary authorities in the industrial countries create a dilemma in the short run, not only as between internal and external purposes, but also as between conflicting internal ones. For the Anglo-Saxon countries the most pressing of these problems are how to achieve expansion and balance-of-payments equilibrium; for the Common Market countries they are how to stop cost inflation and get expansion going again.

These conflicts can, up to a point, be resolved by international monetary co-operation. There are some who argue, for instance, that the Anglo-Saxon countries' economic expansion ought to be financed by the European Economic Community, and that the capital outflow from the United States could be reduced if European capital markets were better and more efficiently organized. But international monetary co-operation has its unsurmountable limits, and beyond these limits we are back in the area of conflicting imperatives. This is where the use of policies alternative or supplementary to monetary policy comes in. Some of these have been much discussed in international circles in recent years, such as countercyclical fiscal and budgetary policies and public debt management; these would seem to be the most suitable for resolving the conflict.

Experience is a stern teacher. European governments have learnt that any efforts to maintain price stability through general demand restriction check growth whenever the price rise is due to cost inflation or occurs at a time when the economy is bumping along the full-employment ceiling; demand restriction can therefore be applied only when all else fails. In their turn, the Anglo-Saxon governments have come to realize that expansion inevitably comes to grief on balance-of-payments difficulties which are not always easily overcome by international co-operation. With these experiences behind them, the major industrial countries' governments have now formally accepted the principle and the need of an incomes policy as the only way out of the intolerable dilemma between unemployment and inflation.

The principle is that the average rise of the wage level must match the tendential average rise of productivity within the economic system (4 per cent in France, 3-4 per cent in Germany, 3.25 per cent in the United Kingdom). This much is common ground, even though the door is left open to certain adjustments and exceptions. For example, a wage pause such as was introduced in the United Kingdom in 1961 and in Austria in 1962, or a slight cost inflation such as occurred in the Netherlands in 1954-55, may prove to be helpful in certain situations for reasons of external balance; a redistribution of incomes as between wage and other income earners may be advisable to increase the rate of investment or to raise social insurance benefits.

Incomes policy is the fruit of a new concept of economic relationships, which is now gaining ground everywhere in the industrial countries of the West: in the Netherlands, where it was initiated as early as 1950; in France, where it is part and parcel of the current five-year plan; in the United Kingdom, where the first steps are being made with the creation of the National Economic Development Council and the National Incomes Commission; in Germany, where the government propose to publish every year their estimate of national income and expenditure with a view to showing the extent to which current labour claims can be satisfied by real wage increases; and in the United States, which about a year ago embarked upon a policy of " guidelines ", by which it is hoped to contain wage rises within the limits of productivity rises. In the Netherlands, in France and in the United Kingdom incomes policy is built into or accompanied by general economic planning.

To sum up the lesson of the postwar years, it has become quite clear that the fundamental problem of how to combine stability and growth cannot, in the short run, be resolved in conditions of nearly full employment without containing incomes within productivity rises.

Italy.— For the Italian economy 1962 was another year of expansion, but of slower expansion than at any time since 1959.

In real terms, gross national income rose by 6.1 per cent (Table 3)—still a high rate, even though it fell short of the previous year's 8.1 per cent. The difference is in large part attributable to agriculture, which raised its product considerably in 1961 but, owing to exceptionally adverse weather conditions, only very slightly in 1962. Industrial output expanded at almost equal rates in both years, the annual index (including building) having risen by 9.3 per cent in 1962 and by 9.5 per cent in 1961.

The general wage level, which had already begun to rise towards the end of 1961, last year went up must faster than productivity, with the result that costs increased sharply (Table 4).

TABLE 3

Condensed National Accounts

Origin of resources	Billion lire at current prices (1)		Composition per cent	Percentage change 1961/62 at		Annual average rate of increase at 1954 prices		
	1961	1962	1962	current prices	1961 prices	1950-58	1958-61	1950-61
Value added in agriculture, forestry and fisheries	3,397	3,659	*13.1*	7.7	..	3.3	1.5	2.9
Value added in industry	8,474	9,566	*34.1*	*12.9*	..	9.0	10.9	9.5
Value added in tertiary activities	5,601	6,318	*22.5*	*12.8*	..	4.0	7.0	4.8
Value added in public administration	2,081	2,384	*8.5*	*14.6*	..	3.5	5.0	3.9
Adjustments	−1,281	−1,376	− *4.9*	*7.4*	..	8.6	3.8	7.2
Gross domestic product at factor cost	18,272	20,551	*73.3*	*12.5*	..	5.5	7.8	6.1
Taxes not included above in the value of goods and services	2,724	3,000	*10.7*	*10.1*	..	4.0	9.0	5.3
Gross domestic product at market prices	20,996	23,551	*84.0*	*12.2*	..	5.3	7.8	6.0
Net income from abroad	87	104	*0.4*	*19.5*	..	18.7	16.5	18.1
Gross national product	21,083	23,655	*84.4*	*12.2*	*6.1*	5.4	7.8	6.0
Imports of goods and services	3,760	4,389	*15.6*	*16.7*	*15.2*	8.8	20.2	11.8
Total . . .	24,843	28,044	*100.0*	*12.9*	*7.5*	5.8	9.8	6.8
Use of resources:								
Exports of goods and services	3,871	4,336	*15.5*	*12.0*	*11.6*	11.8	17.9	13.5
Resources disposable for domestic uses	20,972	23,708	*84.5*	*13.0*	*6.8*	5.0	8.5	5.9
Consumption	15,578	17,592	*62.7*	*12.9*	*6.4*	4.4	6.6	5.0
of which: private	13,305	14,929	*53.2*	*12.2*	*6.6*	4.3	6.6	4.9
public	2,273	2,663	*9.5*	*17.2*	*5.3*	5.7	4.3	5.3
Gross investment	5,394	6,116	*21.8*	*13.4*	*7.7*	7.7	13.8	9.4

(1) Source: Report on the Economic Situation in Italy.

TABLE 4

Dependent Labour Incomes (1)

Sectors and Branches	Billion lire		Composition per cent		Index 1962 (1961=100)
	1961	1962	1961	1962	
1. *Private sector*	*6,986.8*	*8,195.4*	*77.6*	*78.0*	*117.3*
Agriculture, forestry and fisheries	503.0	580.3	*5.6*	*5.5*	*115.4*
Industry	4,178.0	5,014.1	*46.4*	*47.7*	*120.0*
Tertiary activities	2,305.8	2,601.0	*25.6*	*24.8*	*112.8*
2. *Public sector*	*2,019.5*	*2,309.7*	*22.4*	*22.0*	*114.4*
Total . . .	9,006.3	10,505.1	*100.0*	*100.0*	*116.6*

(1) Including gross wages and remunerations in kind to workers, employees and managing staff, as well as social insurance contributions; excluding mixed capital-and-labour incomes earned by artisans, share farmers, etc., as well as the incomes of family helpers.
Source: Report on the Economic Situation in Italy.

Looking at the wage rises in the context of the cyclical phase in which they took place, they can only in small part be interpreted as an effect induced by the previous period's demand. On the contrary, most of them must be regarded as autonomous and, far from being a consequence of demand expansion, they were instead a cause both of an excessive expansion of demand and of a rise in prices.

With labour costs per unit of product rising, prime costs generally increased and, apart from exercising a strong upward pressure on prices, also diminished the liquidity of firms and narrowed their gross profit margins. Ultimately, the strain was transmitted to the sources of outside finance for producer firms.

The redistribution of income to the benefit of wage earners modified the average propensity to save.

The liquidity of firms diminished, but at the same time the liquidity of consumers increased greatly as a result of higher wages.

The increase in labour incomes gave rise to a strong expansion of monetary consumption demand, which in turn accelerated the pace of growth of aggregate demand in monetary terms, in spite of a relative decline of investment demand and a slowing down of foreign demand. In these circumstances, aggregate demand, which had increased by 10.8 per cent in 1961, last year rose by 12.9 per cent.

Investment demand (Table 5) followed the previous year's trend and expanded only just a little more than aggregate demand; foreign demand, lastly, expanded slightly less than aggregate demand and quite considerably less than it had done in 1961.

TABLE 5

Gross Fixed Investment

Sectors	Value (billion current lire)		Percentage change in		
	1961	1962	volume	price	value
Agriculture	528	597	*7.2*	*5.5*	*13.1*
Industry	1,607	1,817	*7.5*	*5.2*	*13.1*
Transport and communications	884	1,005	*13.1*	*0.5*	*13.7*
Building construction	1,236	1,528	*14.5*	*7.9*	*23.6*
Public works	486	478	*− 8.2*	*7.2*	*− 1.6*
Others	358	421	*11.2*	*5.8*	*17.6*
Total fixed investment	5,099	5,846	*8.9*	*5.2*	*14.6*

Source: Report on the Economic Situation in Italy.

For some years foreign demand and domestic investment demand had been far the most dynamic factors in aggregate demand, but last year the position was completely reversed.

The price level, which had remained remarkably stable throughout the period of strongest growth, 1959 to 1961, last year went up by 5 per cent in spite of the restraining effects of imports. The 1961 surplus on foreign trade in goods and services turned into a deficit in 1962 and the deterioration still continues.

The price increases became apparent first at points where supply was weakest, but later became general. Certain major agricultural products were in short supply owing to adverse weather conditions and the effects of these shortages were quickly transmitted to wages through sliding scales; in turn, the wage increases rapidly spread to all sectors.

Generally speaking, prices went up less immediately and less fast than wages, so that profit margins were squeezed. Now this is definitely a symptom of cost inflation, for in demand inflation prices rise earlier and quicker than costs, and profits grow more than wages.

A situation such as that described above displays many of the typical characteristics of full employment, when money incomes tend to increase faster than real national product.

In such a situation there is only one alternative to a price rise, and that is a decrease in the level of employment and output, which inevitably follows from the disinflation of aggregate demand. But while these effects are certain, the price effect is less so, at least when the process is not spread out over time but is concentrated and pervades the whole economy within a few months.

Thus Italy was faced last year with the full difficulties of the problem of how to reconcile a high rate of expansion, a high level of employment and price stability—and that even though the last few years' considerable reduction of the pool of unemployed and underemployed manpower has certainly not yet propelled Italy into the ranks of full-employment countries.

II. *Production and Prices*

Agricultural Production.— From the point of view of weather, 1962 was one of the worst years for Italian agriculture in a very long time. Only wheat and grapes escaped heavy damage.

While agricultural output had gone up sharply in 1961 after the preceding year's reserve, the 1962 index (1961 = 100) was only 101.9. Taking the average output over the four years 1952-55 as a reference base, last year's index of 125.3 compares with 124.0 in 1961, so that the increase was 1 per cent; the corresponding increase in 1961 had been 6.5 per cent, and in 1960 there had been a decline of 3.4 per cent.

As in the two previous years, the highly weather-susceptible grain crops were the determining element in total agricultural production; small as it was, the increment in aggregate output last year owed nearly everything to the wheat harvest, which was about 15 per cent larger than the year before.

In its turn, viticulture, which had suffered a reverse in 1961, did very well last year and, by expanding its output by 27 per cent, made a sizeable contribution to total agricultural production. Without wheat, total production would have been almost the same as in 1961, and without both wheat and wine it would have shrunk by 4.4 per cent.

The damaging effects of weather conditions made themselves felt throughout most of the year. In early spring, late frosts and heavy rain did much damage to herbaceous crops and especially vegetables; the summer's prolonged drought affected mainly forage crops, maize and potatoes. Rain in late summer prevented the harmful effects of the drought from spreading to other crops such as grapes and sugar beet, but towards the end of the year another wave of frost ravaged citrus fruit and vegetable crops, and, worst of all decimated the already poor olive crop.

However, the weather damage, especially to tree crops, might have been worse if the new orchards planted in recent years had not begun to fruit, and if cultivation techniques and methods had not improved as much they did.

In spite of undoubted technical progress the general rate of increase in agricultural output over the last few years was slower than before. Between 1953/54 and 1958/59 the average annual rate of increase had been 3.3 per cent; between 1958/59 and 1961/62 it was only 1.6 per cent. At the same time, demand for food products expanded very considerably, with the twin result that the excess of imports over exports of food increased and prices rose.

In a situation in which the trend is for output to expand markedly less than consumption and demand, poor harvests due to unfavourable weather conditions have a much more pronounced effect on prices than they would have in a more balanced situation.

The agricultural sector's gross money receipts were, according to our estimates, about 10 per cent higher last year than in 1961, having risen from 2,825 to 3,117 billion lire. The increment was larger than that of gross marketable product, because, with fewer people living on the land, the value of self-consumption rose by less than 3 per cent and its volume actually contracted by 3 per cent.

Industrial Production.— Industrial output expanded at very nearly the same rate last year as it did in 1961. The annual index calculated by the Central Statistical Institute for industrial production (excluding building) rose from 198.4 to 217.0 (1953 = 100), which corresponds to a rise of 9.4 per cent.

However, the rise in industrial production owed nearly everything to the previous year's impetus: the mere fact that during the first three months of 1962 the index remained at the high level of late 1961 was enough to lift the whole year's volume of output well above that of the previous year. The monthly production indices did not begin to rise again until the last three months of 1962.

The expansion of production was accompanied by a moderate increase in employment. To judge by the annual average figures calculated from quarterly surveys conducted by the Central Statistical Institute, industrial employment, excluding Italians in temporary jobs abroad, rose by 3.2 per cent last year, compared with 4.4 per cent in 1961. Industrial investment expanded again, but much less than in 1961. The rate of increase last year was 13.1 per cent at current and 7.5 per cent at constant prices, whereas the corresponding 1961 figures had been 22.8 and 18.6 per cent. However, the 1961 and the almost equal 1960 rates of expansion were altogether exceptional and are therefore not a meaningful yardstick of comparison. Last year's figures are seen in proportion much better when set against the average annual rate of growth of gross fixed investment since 1953, which was 10.5 per cent in monetary and 8.7 per cent in real terms.

Undoubtedly, a climate of doubt and hesitancy surrounded investment decisions last year, owing to the converging effects of a number of factors, such as the growth of industrial capacity thanks to the last few years' massive investment, the cyclical dimming of business prospects, diminished self-financing margins within firms and the greater cost of outside finance. In these circumstances last year's new investment, in so far as it was not in response to policy incentives, was largely carried out in the course of such large-scale investment programmes as were already under way or had at least been definitely decided on before.

In the steel industry, investment rose quite considerably last year, thanks to the enormous current investment programme of government-controlled companies; the same can be said of a few minor branches, including cement and paper.

In the context of the Western world's industrial production generally, Italy for the fourth successive year headed the list of all the individual countries' rates of growth. Over the last four years together, the volume of industrial output in Italy increased by more than 50 per cent, whereas at best results elsewhere did not exceed 30 per cent.

In overall terms, as was noted before, industrial output in Italy last year expanded at almost the same rate as in 1961, but there were considerable internal shifts.

The capital goods sector which, after its exceptional spurt in 1960, still went ahead vigorously enough in 1961, last year saw its rate of growth dip below the trend line. After increases of 20.0 and 10.9 per cent in 1960 and 1961, respectively, last year's rate of only 7.9 per cent was less even than the average for all industrial production together.

The production of consumer goods, by contrast, rose very much more last year than it had done in 1961, the two rates of increase being 8.6 and 4.6 per cent. Base materials expanded at the almost identical rates of 12.3 per cent in 1961 and 11.7 per cent in 1962.

The drop in the cyclically highly sensitive rate of increase in capital goods production and the concurrent rise in that of consumer goods production were the dominant features of the Italian economy last year, and indeed were common to a number of other Western European countries as well.

The slow-down in the engineering sector, where the situation of various branches differs greatly both from a structural and a cyclical point of view, may be ascribed to a variety of causes. With heroic simplification it may be said that the major factors of weakness were a diminution of the propensity to invest, a slackening of foreign demand and some loss of competitive strength.

For the rest, the rate of increase in engineering output decreased in all the countries of the European Economic Community, and in all of them, at the same time, the automobile industry was in vigorous expansion.

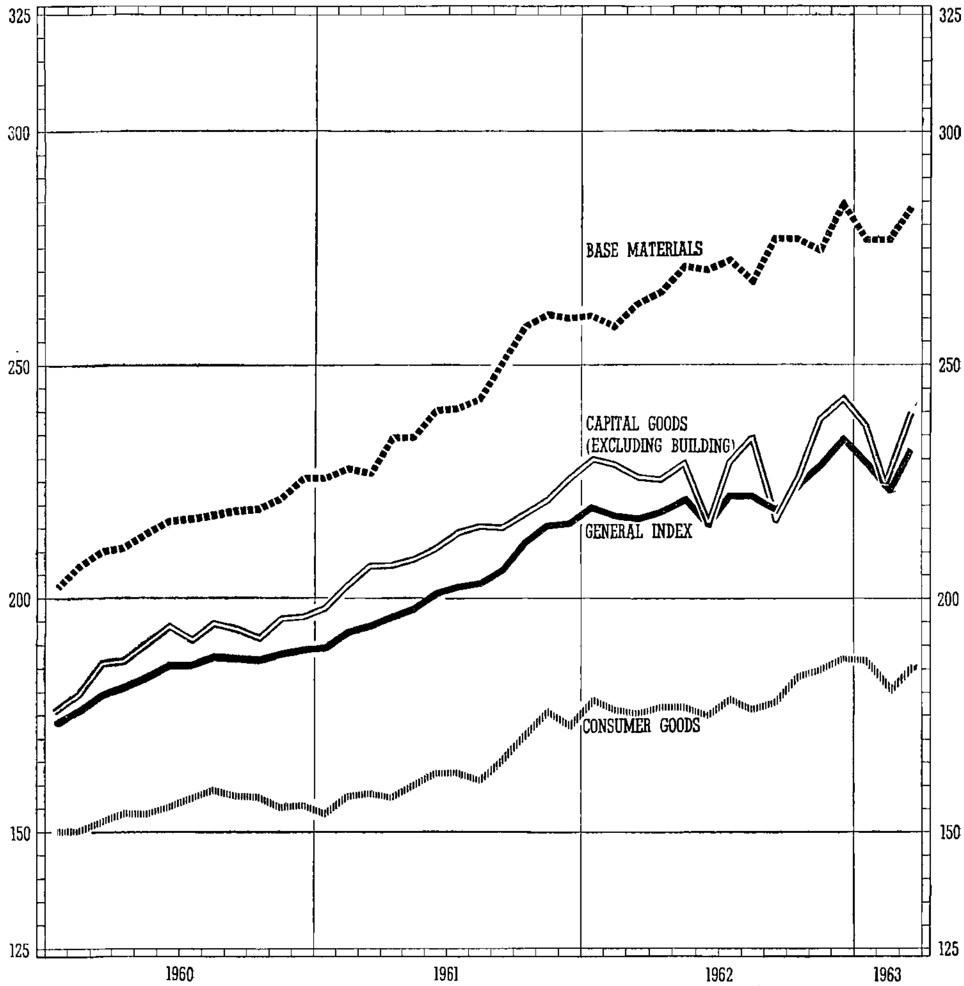
Electric power generation increased by 6.9 per cent over 1961. For the second year running, rainfall conditions were poor, so that thermal power stations had to be drawn on to an even greater extent to make good the short-fall from hydro-electric stations and to meet growing demand.

Expansion in the consumer durables sector, as in 1961, again owed most to electric household appliances and transport vehicles, even though the production of motor cycles contracted sharply; elsewhere, gains were fairly small and some branches, like sewing machines, actually declined.

As regards non-durable consumer goods, nearly all branches improved their performance last year. Outstanding in the most important of them, the food industry, was the advance of the sweets and soft drink branches, whereas the generally rising demand for food products and its changing composition left the subsistence food sectors almost stationary. Some seasonal processing activities, like cheese-making and sugar refining, suffered from shortages of their agricultural base products.

It is interesting to note the time distribution of industrial production last year. At the end of 1961, the index of industrial production stood 14.2 per cent above its level of twelve months before, having risen steadily all through the year, with an acceleration during the last four months; in 1962, there was a further improvement in January, but thereafter the index remained almost stationary until the end of the year, when it resumed its advance (Chart 2).

CHART 2



General index of industrial production
and indices of production of base materials, capital goods and consumer goods
(1953 = 100; seasonally adjusted)

Naturally enough, industrial production felt the impact of last year's general cyclical pattern, exemplified in the slackening of the rate of increase in foreign demand and, even more so, in domestic investment demand. As regards supply strictly speaking, the cost-benefit ratio within the system underwent considerable modifications last year, to the detriment of profit expectations and of competitive strength abroad.

Added to this were the more random effects of industrial strikes, especially in the steel and engineering industries which together account for about one third of value added in the whole of Italian industry. The damaging effects of these strikes can be clearly traced in the seasonally adjusted indices.

Once these chance factors ceased to operate towards the end of the year, industry picked up in response to strong domestic consumption demand swelled by higher labour incomes; ultimately, the recovery began to spread to some capital goods branches. The general index rose by 6.9 per cent between September and December (Table 6), and this surely is more than can be ascribed simply to the resumption of production after the strikes.

TABLE 6

Percentage Changes in the Indices of Industrial Production

(seasonally adjusted figures; 1953 = 100)

Indices	Periods					
	Dec. 61 / Dec. 60 12 months	Dec. 62 / Dec. 61 12 months	May 62 / Dec. 61 5 months	Oct. 62 / May 62 5 months	Dec. 62 / Oct. 62 2 months	Mar. 63 / Mar. 62 12 months
GENERAL INDEX (excluding building)	14.2	8.4	2.5	1.5	4.3	6.6
Base materials and fuel	*15.1*	*9.2*	*4.3*	*2.3*	*2.4*	*8.0*
Chemical products and oil and coal derivatives	20.7	10.5	4.4	4.0	1.8	8.7
Electricity and gas	5.5	8.7	1.9	0.8	5.8	3.7
Others	1.5	2.5	7.4	– 5.6	1.1	11.3
Capital goods (excluding building)	*15.3*	*7.6*	*1.2*	*– 1.3*	7.7	*6.0*
Metallurgical products	7.4	4.6	1.5	– 1.7	4.8	2.1
Engineering products	21.5	2.8	– 1.3	– 6.9	11.8	4.6
Transport equipment	21.5	20.9	3.1	2.0	14.9	14.2
Building materials	12.0	7.2	2.9	5.5	– 1.3	6.2
Consumer goods	*10.9*	*8.3*	*2.3*	*3.7*	*2.1*	*5.8*
Non-durables	10.0	1.1	– 0.4	3.7	– 2.1	6.1
Semi-durables	8.1	11.8	6.3	3.6	1.5	6.1
Durables	19.6	14.8	– 1.3	3.9	12.0	4.5

Wholesale Prices.— The strong cyclical upswing in which the Italian economy had found itself since the middle of 1959 had left wholesale prices by and large stable until August 1961 and subject only to the general influence of international raw material prices. Since then, however, wholesale prices have displayed a pronounced upward tendency.

For the whole of the 26 months between June 1959 and August 1961, the Central Statistical Institute's index registered an increase of only 1 per cent; during the 19 months between August 1961 and March 1963 it went up by 8 per cent. Between December 1961 and December 1962 the increase amounted to 4.6 per cent, and the average rise over the year 1962 was 3 per cent (Table 7).

The wholesale prices of manufactures had on the whole a slightly falling tendency between 1953 and 1959, such small cyclical fluctuations as there were having been due mostly to international movements in the prices of raw materials.

Since then domestic raw material prices have continued to follow international prices slightly downwards, but manufactures have begun to rise slowly. This scissor movement first became apparent around the middle of 1960 and continued throughout 1961. In 1962 it became even more pronounced, but the hardening of international prices towards the end of the year began to have its effect on domestic prices early in 1963 and reinforced the existing upward tendency of the prices of manufactures.

Retail Prices and the Cost of Living. — In its turn, the general level of retail prices in Italy last year reflected the strain on wholesale prices. With services also becoming more expensive at the same time, retail prices rose by 4.7 per cent over the average of the year—more than twice as much as in 1961 (2.1 per cent) and more than twice as much, too, as would correspond to the long-term trend.

At the end of 1962, the index actually stood 6.5 per cent above its end-1961 level. The exceptionally hard winter further reinforced the rising tendency, so that in March 1963 the retail

TABLE 7

Index of Domestic and International Wholesale Prices

(1953 = 100)

Index	1961	1962	1961 Dec.	1962 Mar.	1962 Dec.	1963 Mar.	Percentage change 1962/1961	Dec. 61/Dec. 60	Dec. 62/Dec. 61	Mar. 63/Mar. 62
a) DOMESTIC PRICES:										
Central Statistical Institute:										
General index	99.0	102.0	99.9	101.4	104.5	106.2	*3.0*	*0.9*	*4.6*	*4.7*
Foodstuffs	100.3	105.5	102.5	104.7	110.0	112.0	*5.2*	*2.3*	*7.3*	*7.0*
Industrial raw materials and manufactures (1)	98.1	99.7	98.1	99.1	100.7	102.2	*1.6*	—	*2.7*	*3.1*
Industrial raw materials (1)	97.5	95.3	96.5	96.4	94.3	95.4	— *2.3*	— *1.6*	— *2.3*	— *1.0*
Manufactures	97.8	100.3	98.0	99.6	102.0	103.4	*2.6*	*0.2*	*4.1*	*3.8*
Consumer goods	97.6	101.9	98.9	101.3	105.0	106.7	*4.4*	*1.1*	*6.2*	*5.3*
Capital goods	103.6	104.6	103.8	104.0	105.9	107.2	*1.0*	*1.2*	*2.0*	*3.1*
Auxiliary industrial materials	97.3	96.4	96.6	96.1	97.7	99.3	— *0.9*	— *2.1*	*1.1*	*3.3*
Chamber of Commerce, Milan:										
General index	96.9	97.7	97.5	97.6	98.8	101.1	*0.8*	*1.0*	*1.3*	*3.6*
Foodstuffs	97.8	102.6	100.9	101.6	105.0	108.3	*4.9*	*5.7*	*4.1*	*6.6*
Industrial raw materials and manufactures	96.6	95.7	96.1	95.9	96.2	98.3	— *0.9*	— *0.6*	*0.1*	*2.5*
b) INTERNATIONAL PRICES:										
Volkswirt:										
General index	99.1	97.6	98.7	98.6	97.6	99.1	— *1.5*	*0.5*	— *1.1*	*0.5*
Foodstuffs	90.8	90.2	91.1	91.0	90.5	93.0	— *0.7*	*1.0*	— *0.7*	*2.2*
Industrial raw materials	103.9	101.8	102.9	102.9	101.6	102.6	— *2.0*	— *0.2*	— *1.3*	— *0.3*

(1) In our re-elaboration of the Central Statistical Institute's indices timber and lignite are not included in the index of industrial raw materials, but are included in the combined index of industrial raw materials and manufactures.

price index was 7.8 per cent higher than at the corresponding date in 1962.

As regards the cost of living, the national index rose by 5.8 per cent over the average of last year, again twice as much as in 1961 (2.9 per cent), and at the end of the year stood 7.3 per cent higher than in December 1961. The increase is striking in comparison with the 2.8 per cent annual average rise between 1953 and 1961. During the first quarter of 1963 the index rose by another 4.2 per cent, and over the last 12 months, that is, between March 1962 and March 1963, the rise was 9.6 per cent.

As in wholesale and retail prices, so also in the cost of living it was food prices which rose rather more than others. Over the last 12 months, food probably accounted for more than half of the increase in the cost of living and rents for about a quarter.

Wages.— The wage level rose particularly sharply in 1962, partly owing to the renewal of many collective agreements and partly as an effect of sliding wage scales. In some sectors special causes contributed to the rise. Gross wage rates for industrial workers, exluding family allowances, went up by 11.3 per cent in the course of the year; effective earnings, including remunerations in kind, overtime pay, etc., went up even more, namely, by 14.6 per cent.

In manufacturing industry, the increase in effective earnings, at 14.9 per cent, was not only higher than the domestic industrial average, but higher also than the corresponding rise in all other major countries.

II. *The Balance of Payments*

The surplus in the Italian balance of payments, which had been sizeable ever since 1958 and amounted to 577 million dollars in 1961, sharply dropped last year to just under 50 million dollars (Table 8).

TABLE 8

Overall Balance of Payments (1)

(million dollars)

Items	Credit 1961	Credit 1962	Debit 1961	Debit 1962	Balance 1961	Balance 1962
A. *Goods and Services*						
Goods (fob)	4,103.4	4,581.5	4,659.3	5,459.0	— 555.9	— 877.5
Transport	554.3	601.1	678.6	700.2	— 124.3	— 99.1
Insurance	67.8	69.8	65.6	68.4	2.2	1.4
Foreign travel	755.1	847.3	107.6	123.6	647.5	723.7
Investment income	88.8	107.0	140.3	200.5	— 51.5	— 93.5
Workers' remittances	214.6	287.2	24.1	27.2	190.5	260.0
Government services	62.0	56.0	61.9	94.1	0.1	— 38.1
Miscellaneous	347.0	391.2	277.6	348.0	69.4	43.2
Total . . .	6,193.0	6,941.1	6,015.0	7,021.0	178.0	— 79.9
Offshore procurements and military services	59.1	79.8	0.7	—	58.4	79.8
Total . . .	6,252.1	7,020.9	6,015.7	7,021.0	236.4	— 0.1
B. *Unilateral Transfers*						
Emigrants' remittances	260.7	301.4	—	—	260.7	301.4
Other donations	54.9	45.2	—	—	54.9	45.2
Reparations	—	—	17.1	23.0	— 17.1	— 23.0
Miscellaneous aid	—	—	26.4	29.7	— 26.4	— 29.7
Total . . .	315.6	346.6	43.5	52.7	272.1	293.9
C. *Total of* A + B	6,567.7	7,367.5	6,059.2	7,073.7	508.5	293.8
D. *Capital Movements* (2)						
Foreign borrowing and lending:						
a) Public	85.1	74.4	37.8	47.2	47.3	27.2
b) Private	139.5	111.1	33.0	113.7	106.5	— 2.6
Contractual repayments:						
a) Public	19.4	19.0	34.6	37.3	— 15.2	— 18.3
b) Private	2.4	4.3	18.9	37.6	— 16.5	— 33.3
Investment abroad and from abroad:						
a) Public	—	—	—	—	—	—
b) Private	782.7	1,061.1	151.9	224.4	630.8	836.7
Disinvestment:						
a) Public	—	—	—	—	—	—
b) Private	68.6	30.1	289.5	289.5	— 220.9	— 259.4
Total . . .	1,097.7	1,300.0	565.7	749.7	532.0	550.3
E. *Monetary Movements* (2)						
a) Official gold and convertible currency holdings	—	180.1	339.5	201.8	— 339.5	— 21.7
b) Transactions with the IMF	—	40.0	175.3	—	— 175.3	40.0
c) Other official assets abroad	63.8	118.2	166.1	616.7	— 102.3	— 498.5
d) Bank assets abroad (net)	39.7	457.5	—	27.2	39.7	430.3
Total . . .	103.5	795.8	680.9	845.7	— 577.4	— 49.9
F. *Balancing items*						
Repatriation of Italian bank notes	—	—	329.6	765.9	— 329.6	— 765.9
Leads and lags as between customs and foreign exchange statistics, errors and omissions	—	—	133.5	28.3	— 133.5	— 28.3
Total . . .	—	—	463.1	794.2	— 463.1	— 794.2

(1) The figures, which have been approved by the Committee for the Balance of Payments, have been adjusted in the light of new statistics and estimates during the last two months and therefore differ in certain respects from the provisional figures of the *Report on the Economic Situation in Italy.*

(2) The credit columns show changes in foreign assets; the debit columns indicate changes in foreign liabilities. If positive, the amounts indicate a reduction in foreign assets or an increase in foreign liabilities; if negative, they indicate an increase in foreign assets or a reduction in foreign liabilities.

Large inroads into the 1961 surplus were made both by trade in goods and services, where the entire surplus of 236 million dollars was wiped out, and by capital movements (including the balancing items) where the balance worsened by 313 million dollars; unilateral transfers worked in the opposite direction, but only to the small extent of 22 million dollars.

At first, the capital account took the brunt of the deterioration, but during the second half of the year it suddenly spread also to the merchandise account.

Cyclical swings in world trade combined with strong internal expansionary factors. While these were partly due to a deliberate effort to absorb the balance-of-payments surplus by increased imports,they were partly also an effect of the redistribution of income in Italy and domestic price movements.

This combination of positive and negative factors both tending to destroy our balance-of-payments surplus is really a synthesis of the recent course of the Italian economy. We now have decidedly less freedom of action than before.

There are several reasons why Italian imports expanded so much in 1962. One fundamental reason is that the income elasticity of our imports is very high: we estimate that a 1 per cent increase in national income raises imports by 1.8 per cent. Other reasons were connected with particular aspects of the Italian economy in 1962—for instance, the redistribution of income to the benefit of wage earners, the increase in food import quotas and tariff reductions designed to counteract the rise in the cost of living and in domestic costs generally.

Given that labour incomes rose more than national income last year, it was only natural that demand for consumer goods expanded sharply. One result was that imports rose, another that prices went up under the combined impact of scarce domestic supplies and growing demand for consumer goods in other European countries.

Exports, in their turn, expanded at a slower rate than of late. So far as agricultural products are concerned, the reason was short supply at home; manufactures suffered from a slackening of foreign demand for capital goods, especially on the part of developing countries, where money to pay for imports was scarce.

Again, productivity improved more in firms producing for export than in those producing for domestic consumption, and export prices by and large remained stable. But it must be remembered that a rise in domestic prices tends to spread to export prices and so to impair the competitive strength of our products. Our exports and imports of goods and services now balance each other exactly; if the balance of payments is not to become an obstacle to a 5-6 per cent annual increase in national income, the volume of our exports of goods and services will have to expand at a much higher average annual rate. We need that much more exports because the surplus on unilateral transfers may well be offset by net capital outflows and because imports are, as was noted, highly elastic with respect to income.

Throughout the rapid expansion of the Italian economy between 1950 and 1962 export demand grew relatively faster than consumption and investment demand: in real terms, exports increased by 13 per cent a year on the average, investment by 9.1 and consumption by 5.1 per cent, and domestic demand as a whole by 6.9 per cent (Table 9).

TABLE 9

Growth rates and composition of aggregate demand in Italy, 1950-62

(in constant 1954 prices)

Components of total demand	Percentage composition of total demand at the beginning of the period (1)	Average annual percentage increase 1950-62 (2)	Contribution of each component to increment in total demand 1950-62 (3)	Percentage composition of total demand at the end of the period (4)
Consumption	73.8	5.1	49.1	60.1
Gross investment	17.0	9.1	25.7	21.8
Exports of goods and services	9.2	13.0	25.2	18.1
Total	100.0	9.6	100.0	100.0

If our national income is indeed to expand at an annual rate of 5-6 per cent, then we can rely on nothing except export expansion; an expansion of domestic consumption cannot make good any possible contraction of the exports of goods and services.

In Italy, where there is no full employment as yet, an increase in total demand resting on export expansion tends to be reflected principally in higher employment, whereas an increase in total demand resting on the growth of consumption in the presence of higher wages pushes prices up and, through the balance-of-payments effect, may enforce measures to check the process of growth.

It follows that competitiveness must be the lodestar of our production, for only then can we hope fully to achieve our income and employment targets. In other words, our foreign trade needs the continuing favourable influences of foreign demand shifting towards our goods and services for reasons of price and quality and salesmanship, and the shifts must be big enough to offset the opposite balance-of-payments effects of a rate of growth so much faster than the average of other countries.

The foreign exchange statistics for the first quarter of 1963 (Table 10) suggest that the negative tendency which had become evident in Italy's foreign payments last year, is now becoming more pronounced—so much so that the deficit on current items, which was only 16 million dollars for the corresponding period of 1962, amounted to 211 million dollars this year.

The immediate prospects for our balance of payments depend, on the one hand, on world economic conditions, and, on the other, on domestic factors. Less buoyant foreign demand may well slow down our rate of export expansion, while imports may become subject to opposite influences. This applies principally to certain food imports, but also to some engineering products and capital goods.

Should these predictions come true in the course of 1963, the deterioration in our merchandise trade with foreign countries, which was quite plain during the last quarter of 1962 and the first quarter of this year, would be likely to assume such

Table 10

Balance of Payments

(Foreign exchange receipts and disbursements in million dollars)

	Receipts		Disbursements		Balance		Balance	
	1961	1962	1961	1962	1961	1962	Jan. - March 1962	Jan. - March 1963
A. *Current items*								
1) Exports, imports cif	3,851.1	4,457.4	4,937.3	5,884.2	— 1,086.2	— 1,426.8	— 295.8	— 510.3
2) Freights	281.0	299.1	—	—	281.0	299.1	76.4	65.7
3) Foreign travel	755.1	847.3	107.6	123.6	647.5	723.7	90.0	97.1
4) Emigrants' remittances	417.7	511.0	—	—	417.7	511.0	97.4	98.8
5) Investment income	88.8	107.0	140.3	200.5	— 51.5	— 93.5	— 10.2	— 12.0
6) Other services	496.2	551.5	389.2	502.0	107.0	49.5	5.2	12.8
7) Balance of other payments	17.1	116.7	22.1	—	— 5.0	116.7	9.7	25.8
8) Total . . .	5,907.0	6,890.0	5,596.5	6,710.3	310.5	179.7	— 27.3	— 222.1
9) Government transactions	46.9	67.5	—	—	46.9	67.5	11.2	11.2
10) Total A . . .	5,953.9	6,957.5	5,596.5	6,710.3	357.4	247.2	— 16.1	— 210.9
B. *Capital movements*								
11) Private	1,265.4	1,946.8	1,092.5	2,166.0	172.9	— 219.2	— 86.0	— 57.4
12) Public	73.8	51.7	26.7	29.8	47.1	21.9	8.1	0.7
13) Total B . . .	1,339.2	1,998.5	1,119.2	2,195.8	220.0	— 197.3	— 77.9	— 56.7
C. *Balance* (A + B)	—	—	—	—	577.4	49.9	— 94.0	— 267.6
D. *Monetary Movements*								
Banking system's foreign assets (1) and liabilities:								
14) Commercial banks	39.7	430.3	—	—	39.7	430.3	— 43.5	153.7
15) Bank of Italy	—	35.4	203.4	—	— 203.4	35.4	104.5	3.1
Italian Exchange Office:								
16) Investment and disinvestment abroad	10.6	33.6	92.5	513.2	— 81.9	— 479.6	— 98.9	— 3.6
17) Subscriptions to international organizations	—	—	3.5	3.5	— 3.5	— 3.5	—	—
18) Foreign assets (1) and liabilities	21.8	0.1	10.6	10.9	11.2	— 10.8	— 8.2	— 0.6
19) Official holdings (1)	—	180.1	339.5	201.8	— 339.5	— 21.7	140.1	115.0
20) Total D . . .	72.1	679.5	649.5	729.4	— 577.4	— 49.9	94.0	267.6
21) Grand total . . .	7,365.2	9,635.5	7,365.2	9,635.5	—	—	—	—

(1) An increase is denoted by the minus sign (—).

proportions that we could hardly hope to offset it by the surplus on services and unilateral transfers.

The Exchange of Goods and Services.— International trade expanded last year by 4.8 per cent in terms of value and 5 per cent in terms of volume, under the varying impact of an increase in consumption demand in Europe, the limited purchasing power of developing countries and the recovery of industrial production in the United States. This means that the slow-down in the pace of expansion of international trade, which had brought its rate of growth in value terms down from 11 per cent in 1960 to 4 per cent in 1961, came to a halt last year. At the same time prices fluctuated a good deal less.

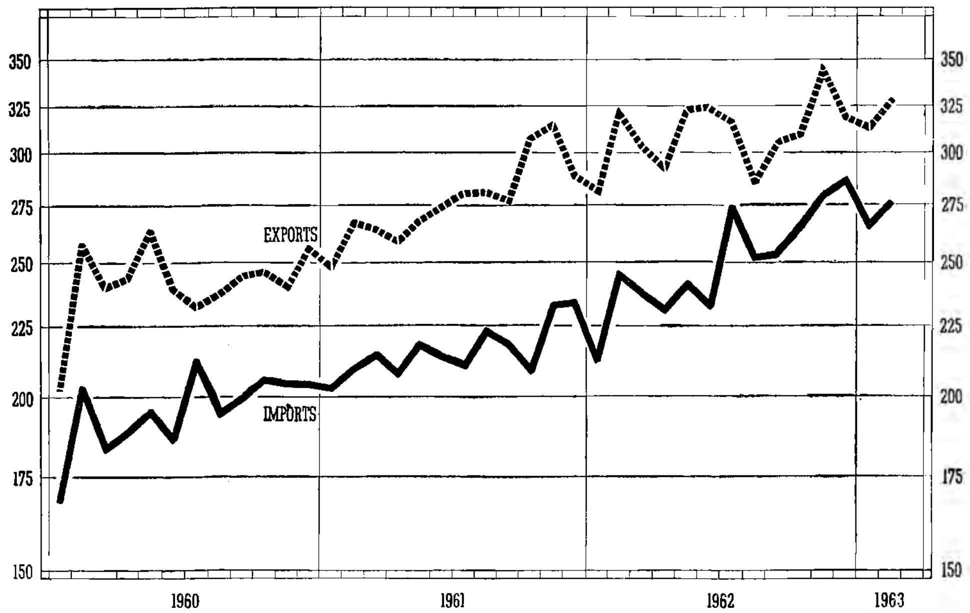
Italy's foreign trade was affected only marginally by international developments, in so far as domestic factors, such as changes in the level and distribution of incomes and internal price movements, exercised the dominating influence.

The considerable and widespread expansion of merchandise exports, which had been so prominent a feature of most of the year 1961 and the early months of 1962, slackened appreciably during the second half of the year. Imports, on the other hand, were pushed up first by the government's deliberate policy with the intention of absorbing the balance-of-payments surplus, and later by rising domestic consumption demand (Chart 3).

At current prices, the value of imports rose by 16 per cent last year, compared with a rise of 11.5 per cent in the value of exports. In absolute figures, as ascertained by the customs authorities, imports rose from 3,265 to 3,785, and exports from 2,614 to 2,916 billion lire; consequently, the trade deficit increased from 650 to 869 billion lire, and the proportion of imports covered by exports dropped from 80 to 77 per cent.

While productivity rose more in Italy last year than in any other industrial country except France, wages also increased more than elsewhere, so that we lost some of the comparative advantages we had built up since 1953 and the expansion of our exports slowed down. It is true that by comparison with

CHART 3



Italian imports and exports

(seasonally adjusted value indices; logarithmic scale - 1953 = 100)

1953 our products are now in a very strong competitive position abroad, but the margin of advantage we have gradually gained must not be regarded as a reserve to be whittled down any further with impunity. It was this margin which was the determining factor in securing Italy a place in the ranks of the industrial countries, and it is this margin which is now a condition of equilibrium for our balance of payments.

Compared with the foreign sales of other Common Market countries, of the EFTA countries, the United States and Canada, Italian exports to major industrial countries were still competitive enough, even though our lead was on the whole not as long as it had been in 1961. From Table 11, which shows the percentage increases in the value of twelve industrial countries' exports, it will be seen that Italy still occupied first place among the countries considered.

Balance-of-payments difficulties depressed purchasing power in most developing countries, and this was one of the strongest restraining influences on the increase in foreign demand last

TABLE 11

Percentage Increases in the Value of Exports by Selected Industrial Countries

Country	1961 / 1960	1962 / 1961
Belgium	4.3	10.9
France	5.2	2.0
Germany	6.3	3.9
Netherlands	2.7	5.7
United Kingdom	4.4	2.8
Sweden	6.7	6.8
Switzerland	8.5	8.6
Austria	7.3	5.1
Denmark	3.4	7.6
Canada	9.1	7.7
United States	1.7	3.5
Italy	14.6	11.5

Source: *O.E.C.D. General Statistics,* March 1963.

year. Actually, foreign consumption demand remained buoyant, but there were definite symptoms of a slackening of foreign demand for capital goods. The resulting effects on Italy's exports pushed last year's index (in terms of volume) down just below the trend line.

As regards services, the estimates for the balance on transport account put the final overall deficit at 99 million dollars last year—much less than in 1961, thanks to higher shipping and airline receipts from foreign passengers.

Tourism made considerable further progress last year. Some 21 million foreign visitors spent 847 million dollars in Italy, and both figures are about 12 per cent higher than in 1961. The tourist flow from other countries of the European Economic Community displayed the relatively strongest increase and now accounts for more than half the total; visitors from the United States were a little fewer than one million, much as in the two preceding years.

The diffusion of foreign travel to the great masses of the population was reflected in hotel bookings, where hotels of second category and below had the relative advantage.

In the opposite direction, more Italians also travelled abroad last year, thanks to the increase in incomes and the spread of motor cars. Over the last five years, the expenditure of Italian tourists abroad increased by an annual average of about 15 per cent to reach 124 million dollars in 1962.

Improved employment conditions at home sharply reduced the outward migratory flow from 378,000 persons in 1961 to 314,000 in 1962. The bulk of them, 299,000, went to European countries, and Common Market countries alone absorbed nearly half the total.

Emigrants' remittances from abroad amounted to 588 million dollars in 1962, that is, 112 million dollars more than in 1961—thanks, in part, to wage increases in Common Market countries, and in part to the fact that Italian workers were employed in higher-grade jobs abroad. Of the total, 301 million dollars are shown in the balance of payments under unilateral transfers as remittances from emigrants, and the remaining 287 million under services as earnings by temporary emigrants.

Capital Movements.— Long-term capital movements among the industrial countries were conditioned, as before, by differences in cyclical patterns and growth prospects. In its turn, the flow of financial resources to developing countries was to a large extent determined by the latters' greater or lesser progress in creating attractive conditions and investment opportunities for foreign capital. Balance-of-payments considerations played their part, too, in so far as the main source of funds for developing countries is usually the public sector and the amounts involved are therefore rather sensitive to influences emanating from the exporting country's balance of payments.

In Europe, the progressive dismantlement of exchange controls enhanced the freedom of international capital movements. Once the European countries' capacity to save was strong enough for them to eliminate this obstacle to capital exports, the flow of private investment abroad gradually increased, though Europe as a whole, and the countries of the European Economic Community in particular, still have a net surplus on private capital account.

In Italy, foreigners invested 1,061 million dollars last year (Table 12), as against 783 in 1961. [1] Direct foreign investment rose from 210 to 379 million dollars, portfolio investment from 554 to 656 million dollars, and other investment, especially in real estate, from 20 to 27 million dollars.

TABLE 12

Foreign Investment and Disinvestment in Italy

(million dollars)

Items	1961	1962
A. *Investment:*		
Direct	209.5	378.6
Portfolio	553.6	655.5
Other	19.6	27.0
Total A . . .	782.7	1,061.1
B. *Disinvestment:*		
Direct	12.4	23.9
Portfolio	268.9	255.3
Other	8.2	10.3
Total B . . .	289.5	289.5
C. *Net investment* (A — B)	493.2	771.6

Foreign disinvestment, on the other hand, amounted to about 290 million dollars in both years. Direct disinvestment rose from 12 to 24 million dollars, portfolio disinvestment dropped from 269 to 255 million dollars, and other disinvestment amounted to 10 million, as against 8 million in 1961.

Taking account of intervening changes in share and bond prices, the total value of foreign investment in Italy at the end of 1962 was 3,439 million dollars. Of these, 73 per cent were in various branches of industry, including electric power, and 26 per cent in services. Four fifths of the foreign funds invested in Italy came from European countries, especially Switzerland, and about 13 per cent from the United States.

(1) The figures are not comparable with those of previous Annual Reports, because the basis and method of calculation have been changed in an effort to arrive at a truer picture of effective investment and disinvestment than was possible before.

In their turn, Italians invested a good deal more abroad last year. Net investment in foreign countries, excluding transactions by the Italian Exchange Office which are counted as monetary movements, amounted to 194 million dollars last year, as against 83 million in 1961 (Table 13).

TABLE 13

Private Italian Investment and Disinvestment Abroad

(million dollars)

Items	1961	1962
A. *Investment:*		
Involving foreign exchange transfers	106.1	186.3
Through other means of transfer	45.8	38.1
Total A . . .	151.9	224.4
B. *Disinvestment:*		
Involving foreign exchange transfers	22.0	13.9
Through other means of transfer	29.5	4.6
For war reparations	17.1	11.6
Total B . . .	68.6	30.1
C. *Net investment* (A — B)	83.3	194.3

Calculated on the basis of authorized transfers, total Italian investment abroad amounted to 1,037 million dollars at the end of 1962, with a wide spread over countries and sectors.

In implementation of the second directive of the E.E.C. Commission regarding the application of Article 67 of the Treaty of Rome, the Italian authorities on March 8, 1963, extended to all residents the freedom to invest in foreign securities, which had previously been limited to specified types of institutes, agencies and finance companies.

Financial aid to developing countries amounted to a total of 555 million dollars last year, against 361 million in 1961; within that total, bilateral aid rose from 309 to 493 million dollars, and multilateral aid from 52 to 62 million. Allowing for intervening repayments, the net capital outflow on this score was 416 million dollars last year, compared with 239 million in 1961. This large increase was made possible partly by the government's raising the ceiling for export credit guarantees from 150 billion lire to 240 billion for the fiscal year 1961/62 and to 270 billion for 1962/63, and partly by exporters taking advantage of a new form of credit permissible under Article 21 of Law No. 635, of July 5, 1961.

Italy's policy in the matter of development aid and the amounts so made available in 1962, must be assessed in the light of the structural economic problems of a nation whose income per head of population still lags far behind that of other industrial countries. There are obvious limitations on the use of public funds for development abroad so long as the budget has to sustain the growing burden of development in depressed areas at home and of the programme to industrialize agriculture.

IV. *International Liquidity Problems and Monetary Movements*

International Liquidity Reserves.— Contrary to what happened in 1961, but in line with the 1959 and 1960 trend, reimbursements to the International Monetary Fund greatly exceeded new currency purchases from it in 1962. Member nations resold the equivalent of 1,490 dollars to the Fund during the year, which is not only more than ever before since the foundation of the Fund, but more than twice as much as they drew.

As regards the currencies involved, demand for Common Market currencies fell off a little during the year, so that their share in total purchases diminished from 53 per cent in 1961 to 46 per cent. The proportion of U.S. dollars, which had accounted for 53 per cent of the total in 1960 and 30 per cent in 1961, dropped to 19 per cent last year, while the proportion of sterling rose from only 5 per cent in 1961 to 34 per cent.

One of the most interesting developments last year was the growing importance of second-line liquidities in international reserves, that is, the substitution of credits in domestic currency, in an amount equivalent to about 500 million dollars, for foreign exchange holdings.

These second-line liquidities have the advantage for the creditor that they eliminate the exchange risk connected with actual foreign currency holdings, while yielding comparable returns; they have the disadvantage of being less easy to spend, but it may be hoped that further refinement of monetary techniques will perhaps do away with this drawback in the future.

In recent years, one particular factor has greatly helped to speed up the velocity of circulation of international liquidity reserves and so to mitigate deficiencies in a number of countries, and that was the strong expansion of the Eurodollar market and, to a lesser degree, of the other Euromarkets (Eurosterling, DM, Swiss francs, guilders, French francs, lire, etc.).

The Eurodollar market, which is outside the United States and consists mostly of transactions between European commercial banks, takes in short-term dollar deposits and furnishes short-term dollar credits from sources other than American banks and at conditions which are generally more favourable than those of American banks.

The inflow of funds comes to about one half from central banks (direct loans to non-American banks, deposits with the Bank for International Settlements redeposited by the latter with non-American banks, swaps or deposits with local commercial banks); the other half comes from U.S. residents (individuals, business, insurance and shipping companies, banks, etc.) and from residents of other countries who wish to keep some funds of their own in U.S. dollars.

The Eurodollar market owes its origin and gradual development to two circumstances: first, to the growing abundance of dollars due to the persistent balance-of-payments deficit of the United States and the growing importance of the dollar as a reserve and international trading currency; and secondly, to the rigidity of lending and borrowing rates and the wide spread between them both in the United States and elsewhere. Such as it is, the Eurodollar market is one—and perhaps the most important—of the many facets of international competition among banks in the wake of the progressive dismantling of exchange barriers which followed the reintroduction of external convertibility at the end of 1958. The market exercises some beneficial pressure on the rigidity of rates of interest, especially lending rates, which is the result of government regulations and interbank agreements; it is therefore a levelling factor which makes it more and more difficult for the industrial countries to pursue divergent monetary policies.

Short-run International Liquidity Problems: Monetary Co-operation Between Governments and Central Banks.— Monetary co-operation between the central banks of the major industrial countries began with the Basle declaration in March 1961, on the occasion of the revaluation of the mark and the guilder. Its first result was massive support for sterling during the later months of the same year, together with agreements concerning the London gold market. Subsequently, it developed mainly through the growing intervention of the U.S. authorities in the exchange markets, for which there was more and more scope as the Americans bought European currencies first autonomously and then under bilateral agreements. Last year, finally, this kind of monetary co-operation received a new impulse from novel American moves as well as from the spate of new ideas originating in the numerous proposals for reforming the international monetary system.

From February 1962 onwards the Federal Reserve Bank of New York, authorized to undertake foreign operations on behalf of the Federal Reserve System, began to purchase European currencies from the U.S. Treasury. The amounts involved were small at first—altogether 33.5 million dollars, of which an equivalent of 0.5 million in lire; but later the bank negotiated with a number of major central banks those reciprocal monetary agreements which have become known in technical usage as swaps and stand-by swaps.

In essence, these agreements provide for mutual credit facilities: one central bank undertakes to exchange, upon request, its own currency against that of another central bank, for instance the Federal Reserve, up to a predetermined amount and within a predetermined period—generally three or six months. If the credit line is used, the foreign exchange proceeds of the swap are, pending their expenditure, placed in time deposits or money market paper yielding the same interest as U.S. Treasury Bills of equal maturity; later, they are spent in spot or forward operations in support of the local currency concerned. Unless the swap is renewed on expiry, the sums taken up are repaid at the same rate of exchange against restitution of the other central bank's currency, so that each of the two parties receives an exchange guarantee expressed in its own currency.

Credits so opened on the basis of reciprocal monetary agreements concluded since March 1962 amount to 1,100 million dollars.

The Federal Reserve uses the foreign exchange it gets from swaps under such reciprocal agreements for spot operations on the market, usually against dollars; the central banks which are partners to the agreement act as intermediaries. So far, the Federal Reserve has not entered the forward market on its own account and has limited its direct interventions to a minimum. Other things being equal, therefore, the operation as a whole has the effect that the central bank concerned replaces non-guaranteed dollars in its reserves by dollars carrying an exchange guarantee in terms of local currency.

Some months before the Federal Reserve, in October 1961, the U.S. Treasury began operating on the exchange market with foreign currency funds it obtained from the repayment of earlier credits, from its own purchases at times of lesser pressure on the dollar, and from borrowing against three-month certificates of indebtedness.

In October 1962, the U.S. Treasury broke new ground by issuing non-negotiable paper—bills, certificates, or bonds—of longer maturities than the three months of the original notes; these were denominated in foreign currency and carried, generally, a rate of interest adjusted to the U.S. market rate for securities of equal maturity.

In these operations the partner is the central bank which issues the currency of denomination. The central bank thereby acquires for its reserves short-term funds which it can use in an emergency (such as a stock exchange slump, the Cuban crisis, etc.), and the respective government can invest its budget surpluses (as happened in Switzerland) instead of leaving them idle. The U.S. Treasury, on the other hand, gains foreign exchange resources which it can subsequently use in spot or forward operations on the exchange market or with central banks abroad.

All this goes to show how far monetary co-operation has gone since the Basle agreements. It became much more intensive and subtle in the course of last year, in spite of some central banks' reluctance to assume obligations contingent upon future events or to widen their currencies' functions beyond those pertaining purely to domestic affairs.

The Bank of Italy took an active part in building up these powerful defences for the international monetary system. Indeed, some of its operations became the model for a whole series of others later adopted by the U.S. authorities. All the same we are, like other central banks, very much aware that these defensive measures are no substitute for a monetary order designed to equilibrate the current balance of payments and that, in particular, the soundness of the dollar rests essentially on its being freely convertible into gold at the present parity, which is safeguarded not only by judicious policies, but ultimately. by the enormous economic and financial potential of the United States. It remains, as before, the responsibility of governments and central banks to maintain parity in exchange rates and balance in foreign accounts; all that co-operation in its various forms can do is to give them a period of grace until the measures they have taken or intend taking to redress the situation show their full effects.

The U.S. authorities tend to regard the co-operation agreements (both the reciprocal monetary agreements and the use of medium-term credit lines) as a first line of defence for the dollar, ahead of intervention by the International Monetary

Fund. Apart from their long-run purposes, which will be discussed presently, these agreements certainly do answer a tactical need: by providing funds to overcome seasonal balance-of-payments disequilibria and pressure from reversible monetary flows (especially from countries with a low towards countries with a high ratio of gold to total reserves), they cointain, prevent or delay the growth of reserves in countries having a temporary surplus. Instead of more reserves, the surplus countries then accumulate credits in their own currency, and the ultimate effect is to relieve pressure on the U.S. gold stock.

While the European countries approve the principles and techniques adopted so far, they would like to see more accent placed on multilateral methods in the construction of the network of agreements, whereas the U.S. authorities appear to prefer a strictly bilateral approach.

Co-operation on the London Gold Market and within the European Monetary Agreement.— Central Bank co-operation among the Basle group with a view to controlling the London gold price continued throughout 1962 and the early months of this year. Gold is bought and sold in whatever way is judged most appropriate to the changing market situation. The members of the " Basle Club " have kept to their undertaking to abstain from individual purchases and from indirect operations which would lead to much the same result. By the end of 1962, the gold pool had a surplus, which was partly distributed to the members and partly held in reserve for future events.

More than once in the course of last year the market was indeed under heavy strain: the Algerian troubles in January, renewed pressure on the dollar in connection with the collapse of stock exchange prices in May, threats to the Canadian dollar in June and July, the Cuban crisis in the third week of October, and so on and so forth. The influence of these events, on the other hand, was mitigated by Russian gold sales, by President Kennedy's reassuring declarations, and, towards the end of the year, by a slackening of Indian demand for gold. Thanks to co-ordinated central bank action, the price of gold fluctuated only within reasonable limits throughout all these vicissitudes (35.07—35.20 dollars per ounce). It is quite obvious that the market's knowledge of close central bank co-operation in this field eased speculative strains and helped to keep the calm.

Indeed, with the probable slowing-down of the increase in South African reserves and of Indian demand, quiet conditions ought to prevail on the market throughout the coming months, provided no serious political or economic disturbances break the peace.

No doubt we should all congratulate ourselves on the scope and efficiency of monetary co-operation in this field, but if we go beyond tactical motives to strict principles, it is rather difficult to see what useful function the London gold market has in the Western monetary system. If anything, it seems to complicate the task of central banks. Surely, it is an astonishingly illogical situation if, on the one hand, the central banks and the Federal Reserve system in particular do the best they can to limit conversions of dollars into gold, and if, on the other hand, their direct or indirect operations on the London gold market give practically limitless satisfaction to all the so-called non-legitimate demand for gold—that is, demand for hoarding and speculation. What is more, it is to all intents and purposes one-way speculation only, in so far as the speculators can raise large funds at reasonable cost on the well-supplied Eurodollar market, and at the same time can always be sure of being able to convert the gold they buy into dollars at the rate of 35 dollars per ounce; at the worst, they would lose little in comparison with the likely gains they hope to reap.

In their turn, the countries members of the Organization for Economic Co-operation and Development, which collaborate through the European Monetary Agreement, worked last year towards solutions rather similar to those implied by the above-mentioned bilateral agreements concluded by the U.S. Treasury and Federal Reserve, and by the I.M.F. transactions to be discussed later.

The United Kingdom, confirming its attitude at previous annual negotiations, had annouced its firm intention not to renew beyond 1962 Part II of the agreement, which concerned the multilateral settlement of the balances. Great Britain argued that the built-in dollar guarantee on reciprocal official holdings had become not only discriminatory but superfluous, in so far as the same end could be achieved by other means, especially through bilateral understandings of the above-mentioned type.

After protracted discussions, a compromise was hammered out, according to which the dollar guarantee would, in dealings with the United Kingdom, no longer apply to all official holdings, which include long-term assets, but only to working balances sufficient to enable the central banks to discharge their regulatory function on the market.

Acknowledging that bilateral currency support agreements between central banks have become an essential ingredient of modern monetary techniques, the partners to the E.M.A. also decided to report to the Bank for International Settlements whenever the negotiations opened by any central bank with a view to obtaining short-term assistance led to the conclusion of such an agreement. The B.I.S. is to be notified not only of the existence of the agreement, but of all subsequent operations carried out under its terms, and in its turn is to inform the other participating central banks and, informally, also the Board of Management of the European Monetary Agreement.

Under these procedures the Bank of England concluded, in February and March of this year, support agreements involving 250 million dollars with the Swiss National Bank, the Bank of France, the Federal Bank of Germany and the Bank of Italy.

Another line of defence for the international monetary system is the self-discipline which countries not responsible for key currencies have voluntarily accepted in the management of their exchange reserves. This is no less effective for being removed from the limelight of publicity.

The central banks of the Common Market countries did not significantly raise the proportion of gold in their reserves last year over the 1961 level; some, indeed, diminished it. Given the persistent deficit in the U. S. balance of payments, this self-imposed moderation obviously could not save the U.S. Treasury from further gold losses, but it did contain them.

Monetary Co-operation within the O.E.C.D., the E.E.C. and the I.M.F.— As was noted before, the defences built up by the Basle agreements and those possible within the framework of the E.M.A. and the mutual facilities envisaged by the Treaty of Rome are in no way a substitute for a sound balance-of-payments policy, nor for continuous and close co-ordination of monetary policies with a view to diminishing—or quickly eliminating—divergencies between them.

This fact is very much in the minds of the Organization for Economic Co-operation and Development and the European Economic Community, and especially the former's Economic Policy Committee and Working Party No. 3, and the latter's Monetary Committee. These have been carefully watching the position of surplus countries (France and, until last October, Italy) as well as of deficit countries with a slow rate of development (the United States, United Kingdom and Canada) and have kept these countries' monetary policy under constant critical review.

Such major economic policy measures as Italy has taken with the principal intent of accelerating the integration of the Italian into the international market have been warmly welcomed. Foremost among them were the abolition of residual quantitative restrictions on industrial imports, unilateral tariff reductions, advance debt repayment, liberalization of portfolio investments, etc.

Our monetary policy is unanimously approved by the international authorities. They are, of course, conscious of the calculated risks we incur by injecting additional liquidity into the economy in certain circumstances, but they consider that this course is, at least at present, the only one which permits the economy's various impulse forces to work to the benefit of expansion and external balance. This, at any rate, is the general judgement from the point of view of the ends pursued; as regards the means, they are generally regarded as the most appropriate in the present situation, even though there is some doubt about the wisdom of our decision last October to open up our money market to the world at large.

This policy admittedly holds some threats to price stability, as indeed is amply shown by the disturbing developments since last autumn. In these circumstances, the international monetary authorities advocate that we should do three things: work out an incomes policy with a view to preventing an undue rise in costs; make further cuts in some of our customs tariffs; and reform our public finances so as to give the government some new countercyclical weapons.

The arrangements of January 1962, by which ten major industrial countries agreed to strengthen the International Monetary Fund by standing ready to lend " supplementary resources " to an equivalent of 6 billion dollars, became operative in October last year. Switzerland, although not a member of the Fund, was invited by the latter to associate herself with these arrangements in some form compatible with the country's special position, and the Swiss authorities have given favourable consideration to this invitation. The proposal is that Switzerland should undertake a commitment to lend to the Fund up to an equivalent of 200 million dollars.

Meanwhile the Fund also reviewed its policy towards primary-producing countries and confirmed its intention to apply flexible criteria to the scrutiny of requests for drawings to make good a sudden drop in export earnings.

Long-run International Liquidity Problems: Reform Proposals for the International Monetary System. The short-run problem of international liquidity, wich has been discussed under the heading of monetary co-operation between governments and central banks, in substance boils down to the balance-of-payments deficit of countries responsible for reserve currencies. The long-run problems is entirely different, although the distinction is not always kept as clear as it ought to be: it is the problem of how to adjust monetary reserves to the growing volume of world trade.

This question has now been discussed for years in ever widening circles and interest in it flared up again during the last few months. A few of the prolific crop of reform plans and proposals (Roosa, E.E.C., Posthuma) have reached the stage of examination by international bodies, others (Maudling) are approaching it; academic economists have joined in and their proposals have aroused the greatest interest and created a beneficial ferment of ideas.

In the last analysis, all the reform plans imply a tacit or formal undertaking by central banks to hold part of their reserves in a form other than gold, that is, in the form of credits either to particular countries or to an international monetary institution and denominated in foreign or domestic currency or else in some accounting unit. Another common, though unequally stressed, feature of these plans is that they all envisage a fund of currency resources to be constituted in some international monetary institution interposed between borrowers and lenders; however, there is considerable difference of opinion as to the liquidity of these deposits.

Nearly all the reform plans furthermore insist on a gold exchange guarantee for the currency pool or the credits to the fund, though this is sometimes limited to foreign exchange accruing in the future. In the Roosa proposal the absence of a gold guarantee is tempered by the provision that, in specific cases, an exchange guarantee may be expressed in the creditor's currency.

Some plans are set within the framework of the E.E.C. and its institutions, others have a bilateral approach. The Triffin plan has world-wide scope, but can be adapted to the regional scale.

While all these plans agree on the purpose of increasing the volume of international liquidity, they advocate different mechanisms. Supposing the U.S. balance of payments to be either in surplus or equilibrium—which is a situation in which, under normal conditions, international liquidity would diminish or remain stationary—Mr. Roosa would increase international liquidity by having the United States buy European currencies or accept them in settlement of her surpluses through swaps. Mr. Maudling comes to the same result by suggesting that such holdings of the debtor countries' currencies as the creditor countries should continue to build up, be subsequently redeposited with the International Monetary Fund in special accounts. In the Posthuma plan balances of payments have no effect on international liquidity, which is, instead, increased by new gold production and by reductions in the proportion of gold in total reserves. Professor Triffin, lastly, would increase international liquidity at will by means of I.M.F. loans.

The view that central bankers take of the various aspects of the long-run and short-run problems of international liquidity is dictated by their judgement of the effective chances of co-operation within the framework of the E.E.C., the Paris agreement on supplementary resources for the I.M.F., the O.E.C.D., or, finally, on a world-wide scale. It is not an immutable judgement, but always reflects the present moment's political and economic realities.

Our own view is that the tools so far applied to the solution of short-run international liquidity problems serve their purpose and are a pointer to where we should go from here. Given that the problem of the reserve currencies is ultimately the same as that of defending the international monetary system, we believe that responsibilities are divided: it is up to the authorities in charge of reserve currencies to make every effort to equilibrate their country's balance of payments as quickly as possible, and it is up to the others to lend their help so as to give the deficit countries a reasonable period of grace.

To this end we believe it is necessary to work towards the ever closer co-ordination not only of monetary policies, but also of budgetary and fiscal policies and of public debt management. We also need to define a joint policy in the matter of the composition and management of reserves.

As regards the long-run problem, we find it hard to give credence to the opinion that the stability of the gold exchange standard is at present under any real threat from a shortage of means of payments and consequently from world-wide deflation. It is not to be excluded, of course, that such threats might materialize in some years; but even then we are confident that when the time comes the Western countries will not fail to work together for suitable solutions. There is no need to worry now about how this is to be done, and through what institutions. This is why we do not see the need for any drastic reform of the international monetary system and prefer a flexible formula. There is no reason why we should not be able to increase international liquidity by expanding transactions under agreements—and preferably multilateral agreements—which can be adapted currently to the changing realities of the political and economic world.

Hence we do not like systems of automatic commitments by creditors and automatic rights for debtors; we do not like schemes where the initiative lies exclusively with debtors and creditors; and we are against gold guarantees in so far as they undermine any form of sound discipline. We do not deny the responsibilities of surplus countries, but we do believe that the only effective systems are those which do not prejudice monetary discipline and we are prepared to accept automatic mechanisms only to the limited extent, and within the very short periods of time, that they may be useful in counter-acting reversible money flows.

While, therefore, we firmly reject the principle of monetary integration prior to political integration, we equally firmly believe in the merits and great scope of monetary co-operation, especially by central banks, within the framework of existing international institutions.

Monetary Movements in the Italian Balance of Payments. Domestic Liquidity.— In Italy's experience the measures adopted for the solution of international liquidity problems find their reflection in the monetary movements of the balance of payments. To put it in a nutshell, the foreign component of liquidity last year expanded monetary circulation by 308 billion lire, while raising official gold and convertible currency holdings by 22 million dollars and other official assets abroad by 459 million dollars (Table 14).

Monetary Movements TABLE 14

(million dollars)

Movements reflected in the balance sheet of the	1961	1962
a) Bank of Italy:		
Official holdings of gold and convertible currencies	339.5	21.7
Transactions with the I.M.F.	74.2	493.9
Other official assets abroad	203.4	— 35.4
Total *a)*	617.1	480.2
(billion lire incl. leads and lags)	*387.4*	*308.8*
b) Banking system:		
Net bank liabilities abroad	— 39.7	— 430.3
(billion lire)	— *24.8*	— *268.9*
Total *a)* + *b)*	577.4	49.9
(billion lire)	*362.6*	*39.1*

At the same time the banking system's net foreign liabilities increased by 430 million dollars (269 billion lire). The net gain to domestic liquidity from free business transactions with abroad—free in the sense that they were made at the business men's own discretion and for the sake of their own profit—therefore works out at only 39 billion lire 308—269), compared with 363 billion in 1961. The sharp contraction of the surplus of foreign receipts over foreign payments, and hence the relatively larger increase in global payments compared with global receipts, was therefore reflected in the smaller contribution which the foreign component made to domestic liquidity.

As in 1961, the monetary authorities again intervened last year to create liquidity or to direct it towards the banking system. But while in 1961 the authorities had, from July onwards, used the foreign exchange channel by letting the Italian Exchange Office deposit dollars with the banks, another method was adopted in January 1962, when the compulsory reserve ratio for banks was lowered, and again in October, when banks were authorized to carry net foreign currency liabilities abroad.

This last measure has to be considered in the wider context of the simultaneous reorganization of the Italian money market, whereby the system of issuing Treasury Bills was altered and new regulations were applied to interbank deposits; at the same time, as was mentioned before, residents were granted greater freedom of capital movement through portfolio investment. The purpose was, on the one hand, to reduce the demand for liquidity due to structural distortions in our domestic market, and on the other hand, to promote the further integration of Italy into the international economy. With the intention of creating an efficient money market and of achieving a more balanced distribution of the flow of savings as between the money and the capital market, we diversified the range of interest rates and offered alternative uses for funds at home and abroad.

Officials Assets Abroad.— Italy's official reserves (gold holdings of the Bank of Italy and the Italian Exchange Office plus the latter's convertible currency holdings), increased by only 22 million dollars last year, as will be seen from Table 15, which analyses the degree of liquidity of official foreign assets. The official reserves reached a total of 3,441 million dollars at the end of 1962, of which 65 per cent were gold and 35 per cent convertible currencies, mostly dollars. Adding to this the balance of plus and minus changes in the Bank of Italy's convertible currency holdings and in both institutes' lire accounts abroad, it will be seen that the total of first-line reserves grew by 43 million dollars to reach 3,548 million dollars at the end of the year.

In second-line reserves two changes occurred: *a)* a diminution of 40 million dollars in Italy's net position with the International Monetary Fund, the so-called gold tranche, that is, the gold quota (68 million dollars) and drawings on the lire quota (175 million dollars at the end of 1961 and 135 million at the end of 1962); *b)* an increase of 50 million dollars as a result of the United States' partial use of the credit line opened to them by the Italian Exchange Office under the swap agreement between the Federal Reserve Bank of New York and the Bank of Italy.

TABLE 15

Foreign Assets of the Italian Exchange Office and the Bank of Italy

(End - period figures in million dollars)

Items	1961	1962	1963 March
1) First-line reserves:			
Gold: Exchange Office	625.0	643.4	685.9
Bank of Italy	1,600.0	1,600.0	1,600.0
Total . . .	2,225.0	2,243.4	2,285.9
Convertible currencies: Exchange Office	1,194.2	1,197.5	1,040.1
Total official reserves . . .	3,419.2	3,440.9	3,326.0
Convertible currencies: Bank of Italy	137.2	174.3	164.5
Lire accounts abroad: Exchange Office	— 17.8	— 1.7	— 2.4
Bank of Italy (excluding I.M.F.)	— 33.0	— 65.3	— 58.8
Total 1) . . .	3,505.6	3.548.2	3,429.3
1) Second-line reserves:			
24-month U.S. Treasury notes redeemable upon notice	—	—	198.5
Swaps with central banks	—	50.0	—
Net position with I.M.F.	243.0	203.0	203.0
Total 2) . . .	243.0	253.0	401.5
Total 1) + 2) . . .	3,748.6	3,801.2	3,830.8
3) Medium- and long-term assets			
15-month U.S. Treasury notes	—	198.5	—
5-year U.S. Treasury notes redeemable after 15 months	—	—	58.0
Foreign currency bonds issued by the Italian government	147.3	336.3	332.2
Foreign currency bonds issued by non-residents	34.1	49.0	48.7
Lire bonds issued by non-residents	—	27.2	27.2
Subscription International Development Association	7.7	11.2	11.2
E.P.U. balance	2.4	1.2	1.2
Consolidated credits and special accounts	161.2	156.3	158.6
Argentinian loan reserve account	19.8	18.3	18.3
Bilateral clearings	0.2	2.5	1.5
Total 3) . . .	372.7	800.5	656.9
Total foreign assets of the Italian Exchange Office and the Bank of Italy (1 + 2 + 3)	4,121.3	4,601.7	4,487.7

While, therefore, first- and second-line reserves underwent no more than negligible changes in 1962, the Exchange Office's medium- and long-term assets abroad more than doubled, from 373 million dollars at the end of 1961 to 801 million at the end of 1962.

All these assets together amounted at the end of last year to 4,602 million dollars (as against 4,121 million at the end of 1961); gold reserves accounted for 49 per cent of this total, convertible currencies for 28 per cent, second-line reserves for 6 per cent and medium- and long-term assets for 17 per cent.

Foreign Exchange Operations by the Banking System.— Italian banks took immediate advantage of their renewed freedom to maintain debit balances abroad in convertible currencies, with the startling result that a net credit balance of 150 million dollars at the end of October had turned into a net debit balance of 175 million within a month and to 363 million by the end of December (Table 16).

The currency composition of the banking system's foreign assets and liabilities underwent considerable change last year in response to money rates of interest and spot and forward rates. The biggest change occurred in dollars, where assets increased over the year by 48 per cent and liabilities nearly doubled, so that the end-1961 credit balance of 75 million turned into a debit balance of 180 million, that is, the difference between 979 million assets and 1,158 million liabilities (Table 17). The scene of nearly all these changes was the Eurodollar market (Table 18).

The banks' forward commitments again expanded strongly in the course of last year (Table 19). In turn, their foreign currency credits to Italian clients rose by 53 per cent to an end-1962 total of 1,312 million dollars (Table 20). The most striking increase took place in Swiss franc credits, where the amount outstanding at the end of 1962 was 547 million dollars, in German mark and Dutch guilder credits; dollar credits remained almost stationary. Looking at bank deposits and loans classified by foreign currencies and lire pertaining to foreign transactions, it will be seen that the inflow of dollars from abroad, from domestic clients and from the Italian Exchange Office was reflected not only in credits to foreign and Italian clients but also in spot sales of dollars against forward purchases (Table 21).

TABLE 16

The Italian Banks' Overall Position in Foreign Exchange and Lire Accounts

(End-month figures in million dollars)

Items	1961 December	1962 June	1962 October	1962 November	1962 December	1963 March
ASSETS						
A. Assets abroad:	979.1	1,247.4	1,470.2	1,400.9	1,457.2	1,536.1
1) *in convertible currencies*	*933.1*	*1,175.1*	*1,407.5*	*1,333.3*	*1,384.3*	*1,420.0*
sight deposits	350.1	436.1	528.2	453.1	502.9	483.6
time deposits and short-term investment	480.7	610.6	749.2	756.5	719.4	780.2
short-term claims	102.3	128.4	130.1	123.7	162.0	156.2
2) *in non-convertible currencies*	*3.2*	*3.3*	*2.7*	*2.7*	*2.9*	*3.3*
3) *in lire accounts*	*42.8*	*69.0*	*60.0*	*64.9*	*70.0*	*112.8*
B. Forward commitments abroad	454.0	660.8	977.5	1,084.3	1,308.4	2,099.9
C. Domestic assets in foreign exchange	907.9	1,168.5	1,232.2	1,302.4	1,365.0	1,590.0
D. Forward commitments in Italy	3.0	2.4	1.6	1.4	2.1	2.7
E. Total assets	2,344.0	3,079.1	3,681.5	3,789.0	4,132.7	5,228.7
LIABILITIES						
F. Liabilities abroad:	1,153.4	1,394.5	1,619.7	1,829.8	2,061.8	2,294.4
1) *in convertible currencies*	*868.0*	*1,066.4*	*1,257.4*	*1,508.1*	*1,747.0*	*1,946.9*
deposit by non - residents	797.6	965.6	1,136.0	1,359.0	1,569.8	1,765.9
short-term debts	70.4	100.8	121.4	149.1	177.2	181.0
2) *in non-convertible currencies*	*2.9*	*4.9*	*5.2*	*4.7*	*2.7*	*2.6*
3) *in lire accounts*	*282.5*	*323.2*	*357.1*	*317.0*	*312.1*	*344.9*
G. Forward commitments abroad	470.7	703.4	1,057.5	1,100.9	1,306.7	2,088.4
H. Clients' foreign exchange deposits in Italy	280.0	352.9	391.7	348.5	381.8	401.2
I. Accounts with the Italian Exchange Office	2.9	4.4	4.0	3.9	4.1	3.5
J. Forward commitments in Italy	10.7	13.0	14.2	19.6	16.3	14.7
K. Total liabilities	1,917.7	2,468.2	3,087.1	3,302.7	3,770.7	4,802.2
L. Net position in convertible currencies vis-a-vis abroad	65.1	108.7	150.1	— 174.8	— 362.7	— 526.9
M. Net position vis-a-vis abroad (A — F)	— 174.3	— 147.1	— 149.5	— 428.9	— 604.6	— 758.3
N. Overall net position (E — K)	426.3	610.9	594.4	486.3	362.0	426.5
O. Net position in foreign bank notes, non-convertible currencies and lire accounts	— 245.1	— 283.9	— 329.3	— 243.3	— 222.9	— 208.3
P. Spot-and-forward facilities drawn (N — O)	671.4	894.8	923.7	729.6	584.9	634.8
Q. Forward facilities drawn (G + J — B — D)	24.4	53.2	92.6	34.8	12.5	0.5

TABLE 17

Convertible Currency Assets and Liabilities of Italian Banks

(End-month figures in million dollars)

Currency	1961 December	1962 June	1962 October	1962 November	1962 December	1963 March
Dollars						
Assets	661.1	845.8	1,040.5	964.3	979.4	942.5
Liabilities	586.3	713.6	770.9	945.2	1,159.2	1,210.7
Balance	74.8	132.2	269.6	19.1	— 179.8	— 268.2
Swiss francs						
Assets	72.3	100.6	137.7	135.1	146.7	145.9
Liabilities	101.2	147.6	228.4	278.0	300.6	392.7
Balance	— 28.9	— 47.0	— 90.7	— 142.9	— 153.9	— 246.8
Sterling						
Assets	100.5	146.1	135.5	133.2	131.0	175.6
Liabilities	93.3	120.3	119.8	145.8	157.0	211.9
Balance	7.2	25.8	15.7	— 12.6	— 26.0	— 36.3
German marks						
Assets	55.8	53.0	56.3	63.0	72.1	81.7
Liabilities	51.1	41.9	65.5	83.4	75.4	76.0
Balance	4.7	11.1	— 9.2	— 20.4	— 3.3	5.7
Dutch guilders						
Assets	8.2	7.8	16.8	15.7	10.3	20.1
Liabilities	4.8	4.8	33.3	44.8	37.1	40.9
Balance	3.4	3.0	— 16.5	— 29.1	— 26.8	— 20.8
French francs						
Assets	8.1	8.7	8.7	8.9	8.8	17.6
Liabilities	3.9	4.2	4.1	4.8	4.7	6.7
Balance	4.2	4.5	4.6	4.1	4.1	10.9
Other currencies						
Assets	11.1	13.1	12.0	11.8	12.0	13.4
Liabilities	5.9	6.0	5.6	6.1	7.8	8.0
Balance	5.2	7.1	6.4	5.7	4.2	5.4
Total						
Assets	917.1	1,175.1	1,407.5	1,332.0	1,360.3	1,396.8
Liabilities	846.5	1,038.4	1,227.6	1,508.1	1,741.8	1,946.9
Balance	70.6	136.7	179.9	— 176.1	— 381.5	— 550.1
Bank notes, balance of forward commitments and swaps against lire						
Assets	16.0	—	—	1.3	24.0	23.2
Liabilities	21.5	28.0	29.8	—	5.2	—
Balance	— 5.5	— 28.0	— 29.8	1.3	18.8	23.2
Grand total						
Assets	933.1	1,175.1	1,407.5	1,333.3	1,384.3	1,420.0
Liabilities	868.0	1,066.4	1,257.4	1,508.1	1,747.0	1,946.9
Balance	65.1	108.7	150.1	— 174.8	— 362.7	— 526.9

TABLE 18

Eurodollar Assets and Liabilities of Italian Banks

(End-month figures in million dollars)

Country	1961 December	1962 June	1962 September	1962 December
United Kingdom				
Assets	158.5	151.7	156.6	144.7
Liabilities	102.0	143.0	149.0	376.0
Balance	56.5	8.7	7.6	— 231.3
Switzerland				
Assets	109.0	140.8	156.5	140.0
Liabilities	66.0	101.0	82.0	99.0
Balance	43.0	39.8	74.5	41.0
France				
Assets	39.2	59.3	49.9	54.7
Liabilities	76.0	86.0	92.0	164.0
Balance	— 36.8	— 26.7	— 42.1	— 109.3
Belgium				
Assets	33.4	6.5	14.1	13.2
Liabilities	8.0	18.0	13.0	46.0
Balance	25.4	— 11.5	1.1	— 32.8
Germany				
Assets	19.9	18.3	23.6	40.9
Liabilities	28.0	67.0	49.0	23.0
Balance	— 8.1	— 48.7	— 25.4	17.9
Netherlands				
Assets	13.4	22.1	20.7	15.7
Liabilities	13.0	28.0	30.0	69.0
Balance	0.4	— 5.9	— 9.3	— 53.3
Other countries				
Assets	93.7	137.3	166.0	152.7
Liabilities	254.0	231.0	197.0	241.0
Balance	— 160.3	— 93.7	— 31.0	— 88.3
Total				
Assets	467.1	536.0	587.4	561.9
Liabilities	547.0	674.0	612.0	1,018.0
Balance	— 79.9	— 138.0	— 24.6	— 456.1

TABLE 19

Forward Commitments with Counterpart Abroad

(End-month figures in million dollars)

Currency	1961 December	1962 June	1962 October	1962 November	1962 December	1963 March
Dollars						
Assets	337.3	541.7	735.9	769.1	869.0	1,294.6
Liabilities	134.9	138.4	269.6	303.0	372.6	642.0
Balance	202.4	403.3	466.3	466.1	496.4	652.6
Swiss francs						
Assets	12.3	33.3	33.5	35.1	55.5	43.1
Liabilities	207.5	362.3	480.2	423.5	434.0	571.0
Balance	— 195.2	— 329.0	— 446.7	— 388.4	— 378.5	— 527.9
Sterling						
Assets	92.3	80.3	158.2	221.9	305.9	663.1
Liabilities	67.7	66.1	136.0	160.4	235.2	595.6
Balance	24.6	14.1	22.2	61.5	70.7	67.5
German marks						
Assets	9.5	4.5	26.5	25.3	49.5	51.0
Liabilities	32.0	89.9	86.0	114.3	156.0	151.6
Balance	— 22.5	— 85.4	— 59.5	— 89.0	— 106.5	— 100.6
Dutch guilders						
Assets	0.2	0.4	21.8	30.4	26.8	43.2
Liabilities	23.7	41.2	79.8	91.3	100.4	111.1
Balance	— 23.5	— 40.8	— 58.0	— 60.9	— 73.6	— 67.9
French francs						
Assets	0.2	—	—	—	—	3.2
Liabilities	2.0	1.7	1.7	1.5	2.1	9.9
Balance	— 1.8	— 1.7	— 1.7	— 1.5	— 2.1	— 6.7
Other currencies						
Assets	2.2	0.7	1.6	2.5	1.7	1.7
Liabilities	2.9	3.8	4.2	6.9	6.4	7.2
Balance	— 0.7	— 3.1	— 2.6	— 4.4	— 4.7	— 5.5
Total						
Assets	454.0	660.8	977.5	1,084.3	1,308.4	2,099.9
Liabilities	470.7	703.4	1,057.5	1,100.9	1,306.7	2,088.4
Balance	— 16.7	— 42.6	— 80.0	— 16.6	1.7	11.5

TABLE 20

The Italian Banks' Foreign Exchange Credits to Domestic Clients

(End-month figures in million dollars)

Currency	1961 December	1962 June	1962 October	1962 November	1962 December	1963 March
Dollars	548.0	577.5	444.6	469.4	523.7	520.2
per cent of total	*63.9*	*51.5*	*37.7*	*37.7*	*39.9*	*34.0*
rate of interest	*5.25*	*4.50-4.75*	*5.0-5.25*	*5.0*	*5.0-5.25*	*5.0*
Swiss francs	238.9	390.4	556.0	542.6	546.7	789.5
per cent of total	*27.9*	*34.8*	*47.2*	*43.6*	*41.7*	*51.5*
rate of interest	*5.25*	*4.50*	*4.50-5.0*	*4.75-5.0*	*4.75-5.25*	*4.50*
Sterling	11.5	11.9	9.0	9.3	8.7	10.9
per cent of total	*1.3*	*1.1*	*0.8*	*0.7*	*0.7*	*0.7*
rate of interest	*7.50*	*5.25-5.75*	*5.75 6.0*	*5.50*	*5.50-5.75*	*5.50-6.50*
German marks	32.1	93.2	82.9	121.8	118.5	111.8
per cent of total	*3.7*	*8.3*	*7.1*	*9.8*	*9.0*	*7.3*
rate of interest	*5.25*	*4.25-4.75*	*4.75-5.0*	*4.50-5.0*	*4.75-5.50*	*5.0-5.25*
Dutch guilders	21.9	41.0	77.7	91.7	101.7	88.6
per cent of total	*2.6*	*3.7*	*6.6*	*7.4*	*7.7*	*5.8*
rate of interest	*5.25*	*4.0-4.75*	*4.75-5.25*	*4.25-5.0*	*4.75-5.25*	*4.50-5.0*
French francs	3.0	2.6	2.6	2.9	3.5	3.4
per cent of total	*0.3*	*0.2*	*0.2*	*0.2*	*0.3*	*0.2*
rate of interest	*5.75*	*5.25-5.50*	*5.25-5.50*	*5.25*	*5.25*	*5.0-5.50*
Other currencies	3.0	4.2	5.3	7.3	9.4	8.0
per cent of total	*0.3*	*0.4*	*0.4*	*0.6*	*0.7*	*0.5*
rate of interest	*6.25-6.50*	*4.25-7.25*	*4.75-7.25*	*4.50-7.0*	*4.75-8.75*	*4.75-8.75*
Total . . .	858.4	1,120.8	1,178.1	1,245.0	1,312.2	1,532.4

The renewal of the cross-currents of inflowing funds between the domestic and foreign money markets, the new regulations concerning interest rates on interbank deposits, and the introduction of a new system of issuing Treasury Bills were all designed to create an efficient money market in Italy and to afford Italian banks an opportunity to base their decisions on reasonably homogeneous yardsticks of comparison at home and abroad. The equilibrium rate for foreign exchange demand and supply vis-à-vis foreign markets or the Italian Exchange Office

TABLE 21

Foreign Exchange Assets and Liabilities of Italian Banks

(End-month figures in million dollars)

Items	Dollars: United States	Dollars: Italy	Dollars: Other countries	Dollars: Total	Swiss francs	Sterling	German marks	Dutch guilders	French francs	Other currencies	Total
December 31 1961											
Deposits:											
foreign	39.3	—	547.0	586.3	101.2	93.3	51.1	4.8	3.9	30.3	870.9
domestic	—	184.1	—	184.1	21.2	44.2	12.2	1.8	5.0	14.4	282.9
lire (balance)	6.4	—	—	6.4	17.9	9.1	11.4	14.4	41.8	138.7	239.7
foreign exchange liabilities	—	—	—	—	197.9	—	23.5	23.5	1.7	0.8	247.4
Total	45.7	184.1	547.0	776.8	338.2	146.6	98.2	44.5	52.4	184.2	1,640.9
Loans:											
foreign	194.0	—	467.1	661.1	72.3	100.5	55.8	8.2	8.1	30.3	936.3
domestic	—	581.5	—	581.5	252.0	12.3	33.3	22.7	3.0	3.1	907.9
foreign exchange claims	—	—	197.9	197.9	—	25.1	—	—	—	—	223.0
Total	194.0	581.5	665.0	1,440.5	324.3	137.9	89.1	30.9	11.1	33.4	2,067.2
June 30 1962											
Deposits:											
foreign	39.6	—	674.0	713.6	147.6	120.3	41.9	4.8	4.2	38.9	1,071.3
domestic	—	251.3	—	251.3	23.0	52.0	15.5	3.9	3.1	8.5	357.3
lire (balance)	19.8	—	—	19.8	13.3	22.9	21.9	21.7	28.2	126.4	254.2
foreign exchange liabilities	—	—	—	—	329.8	—	86.2	40.8	1.7	3.5	462.0
Total	59.4	251.3	674.0	984.7	513.7	195.2	165.5	71.2	37.2	177.3	2,144.8
Loans:											
foreign	309.8	—	536.0	845.8	100.6	146.1	53.0	7.8	8.7	16.4	1,178.4
domestic	—	608.8	—	608.8	403.1	12.7	94.9	42.2	2.6	4.2	1,168.5
foreign exchange claims	—	—	394.0	394.0	—	14.8	—	—	—	—	408.8
Total	309.8	608.8	930.0	1,848.6	503.7	173.6	147.9	50.0	11.3	20.6	2,755.7
October 31 1962											
Deposits:											
foreign	....	—	....	770.9	228.4	119.8	65.5	33.3	4.1	40.6	1,262.6
domestic	—	293.2	—	293.2	29.2	47.3	12.9	3.8	4.1	5.2	395.7
lire (balance)	35.0	—	—	35.0	18.2	31.3	16.0	21.8	38.4	136.4	297.1
foreign exchange liabilities	—	—	—	—	447.7	—	59.7	58.0	1.7	2.7	569.8
Total	....	293.2	....	1,099.1	723.5	198.4	154.1	116.9	48.3	184.9	2,525.2
Loans:											
foreign	428.7	—	611.8	1,040.5	137.7	135.5	56.3	16.8	8.7	14.7	1,410.2
domestic	—	478.2	—	478.2	572.0	9.8	84.4	79.9	2.7	5.2	1,232.2
foreign exchange claims	—	—	454.4	454.4	—	22.8	—	—	—	—	477.2
Total	428.7	478.2	1,066.2	1,973.1	709.7	168.1	140.7	96.7	11.4	19.9	3,119.6
November 30 1962											
Deposits:											
foreign	....		....	945.2	278.0	145.8	83.4	44.8	4.8	10.8	1,512.8
domestic	—		—	266.6	18.2	43.7	11.2	3.2	4.1	5.4	352.4
lire (balance)	32.4	—	—	32.4	18.2	0.4	14.8	22.8	38.7	124.8	252.1
foreign exchange liabilities	—	—	—	—	388.9	—	89.2	60.9	1.5	4.5	545.0
Total	....	266.6	....	1,244.2	703.3	189.9	198.6	131.7	49.1	145.5	2,662.3
Loans:											
foreign	372.5	—	591.8	964.3	135.1	133.2	63.0	15.7	8.9	15.8	1,336.0
domestic	—	509.0	—	509.0	555.1	11.7	122.9	93.5	2.9	7.3	1,302.4
foreign exchange claims	—	—	455.9	455.9	—	54.3	—	—	—	—	510.2
Total	372.5	509.0	1,047.7	1,929.2	690.2	199.2	185.9	109.2	11.8	23.1	3,148.6
December 31 1962											
Deposits:											
foreign	141.2	—	1,018.0	1,159.2	300.6	157.0	75.4	37.1	4.7	15.7	1,749.7
domestic	—	304.6	—	304.6	17.3	41.0	10.8	2,2	4.3	5.7	385.9
lire (balance)	34.7	—	—	34.7	6.7	13.4	13.5	24.2	30.6	119.0	242.1
foreign exchange liabilities	—	—	—	—	378.8	—	106.6	73.6	2.1	4.4	565.5
Total	175.9	304.6	1,018.0	1,498.5	703.4	211.4	206.3	137.1	41.7	144.8	2,943.2
Loans:											
foreign	417.5	—	561.9	979.4	146.7	131.0	72.1	10.3	8.8	38.9	1,387.2
domestic	—	561.3	—	561.3	558.4	9.4	120.1	102.8	3.6	9.4	1,365.0
foreign exchange claims	—	—	488.4	488.4	—	64.6	—	—	—	—	553.0
Total	417.5	561.3	1,050.3	2,029.1	705.1	205.0	192.2	113.1	12.4	48.3	3,305.2

is now settling down around 3.50 per cent; beyond this rate, it is normally not profitable to take in foreign exchange on outside markets but better to draw on the Italian Exchange Office's still disposable spot-and-forward facilities, and below this rate there is no point in offering foreign exchange abroad, but better to sell to the Exchange Office. Naturally, these choices depend on each bank's degree of lire liquidity and on the margin which separates it from the spot-and-forward ceiling.

V. *Government finance*

The administrative budget for 1961/62 closed with a current deficit of 296 billion lire, the initial estimates having allowed for 285 billion. Including also capital movements but not public debt operations, the overall deficit worked out at 381 billion lire, as against 377 billion originally budgeted for (Table 22).

Contrary to what happened in the two preceding fiscal years, therefore, the out-turn was very close to the initial estimates on balance, even though the level of both revenue and expenditure was much higher.

For 1963/64 the initial estimates budget for a current deficit of 389 and an overall deficit of 502 billion lire (Table 23). Both these amounts are more than 100 billion lire in excess of the corresponding initial estimates for 1962/63, and both will certainly have to be revised upwards again, when the Green Plan and the Rural Housing Plan, for instance, require further expenditure which has to be financed by credit.

To cover its cash requirements, the Treasury last year relied largely on Post Office savings and on the proceeds of Treasury Bills. The latter provided 80 billion lire more in 1962 than in 1961, thanks exclusively to purchases by the Bank of Italy. Under the new system of Treasury Bill allocations the Bank has been building up its own holdings, so as to be in a position, if need be, to intervene in the money market in the opposite sense, as a seller of Treasury Bills. Long-term credits, including foreign ones, were drawn on only to the extent of 29 bil-

TABLE 22

Budget Position for the Fiscal Years 1961/62, 1962/63 and 1963/64

(administrative budget; billion lire)

Items	1961/62 Initial estimates	1961/62 Subsequent variations	1961/62 Final results (1)	1962/63 Initial estimates	1962/63 Subsequent variations	1962/63 Revised estimates 31-3-63	1963/64 Initial estimates
Current Section:							
Revenue	4,050	501	4,551	4,482	227	4,709	5,265
Expenditure	4,335	512	4,847	4,761	598	5,359	5,654
Surplus or deficit (—)	— 285	— 11	— 296	— 279	— 371	— 650	— 389
Capital Movements:							
Revenue:							
a) Issue of securities	—	318	318	—	110	110	—
b) Issues for various indemnities (2)	3	—	3	3	—	3	3
c) Issue of Treasury coin	—	11	11	—	—	—	—
d) Balancing items	16	2	18	11	—	11	24
e) Other	46	9	55	23	3	26	26
	65	340	405	37	113	150	53
Expenditure:							
a) Repayment of public debt (3)	361	2	363	267	—	267	307
b) Balancing items	16	2	18	11	—	11	24
c) Other	138	2	140	133	7	140	139
	515	6	521	411	7	418	470
Surplus or deficit (—)	— 450	334	— 116	— 374	106	— 268	— 417
Overall results:							
Revenue	4,115	841	4,956	4,519	340	4,859	5,318
Expenditure	4,850	518	5,368	5,172	605	5,777	6,124
Overall surplus or deficit (—)	— 735	323	— 412	— 653	— 265	— 918	— 806
Net result of public debt operations	— 358	327	— 31	— 264	110	— 154	— 304
Net surplus or deficit (—)	— 377	— 4	— 381	— 389	— 375	— 764	— 502

(1) Provisional figures.
(2) Mainly compensation for confiscation of Italian property abroad.
(3) Including the withdrawal of Treasury currency, payments into the Amortisation Fund for Treasury Bonds and redemption of bonds issued by the Credit Consortium for Public Works.

TABLE 23

Government Finance

(administrative budget; billion lire)

Fiscal years (a)	Net revenue (b)	Net expenditure (b)	Ratio of revenue to expenditure (per cent)	Net deficit			Public investment	Surplus of investment over deficit
				Current section	Capital movements	Total		
1	2	3	4=2 : 3	5	6	7=5+6=2—3	8	9=7+8
1959/60	3,727	4,151	*89.8*	— 337	— 87	— 424	972	548
1960/61	4,004	4,472	*89.5*	— 411	— 57	— 468	966	498
1961/62	4,606	4,987	*92.4*	— 296	— 85	— 381	1,071	690
1962/63	4,505	4,894	*92.1*	— 279	— 110	— 389	933	544
1963/64	5,291	5,793	*91.3*	— 389	— 113	— 502	1,005	503

(a) The figures for 1959/60, 1960/61 and 1961/62 are provisional, those for 1962/63 and 1963/64 are initial estimates.
(b) Current items plus the "other" capital items shown in Table 21.

lion lire, as against 143 billion in 1961. To all intents and purposes, the only operation of this kind was a bond issue by the Credit Consortium for Public Works, to finance rural housing. The remaining new issues of government securities, including Green Plan bonds, were by and large offset by the redemption of 1962 Treasury Bonds, or else, as in the case of Railway Bonds, were absorbed by the Central Post Office Savings Fund.

In these circumstances the Treasury's cash position naturally deteriorated. With only the Bank of Italy's Treasury Bill purchases providing new cash and with the large-scale extinction of short-term debts especially to private and institutional investors, the larger cash deficit forced the Treasury to borrow from the Bank of Italy again in 1962, after it had repaid the sizeable sum of 162 billion lire to the Bank in 1961. The Bank furnished altogether 191 billion lire, mainly through Treasury Bill purchases, as mentioned above, and through Italian Exchange Office loans.

As regards budgetary arrears, the tendency for disbursements due, and their balance over receipts due, to increase continued in 1961/62, but was rather less pronounced than the year before. More arrear payments came in, revaluation and settlement of accounts provided more net relief, and finally, fairly large amounts were carried forward into future fiscal years, as permitted by law. If these latter amounts had remained in the arrears budget, disbursements due would have had to be shown as much greater; on the other hand, future budgets now inherit a considerable amount of liabilities already covered by financial provision.

In relative terms, some improvement took place in 1961/62. Both the ratio of receipts due to budgetary revenue and the ratio of disbursements due to budgetary expenditure fell, and a greater proportion of prior arrears was settled in cash. This does not necessarily mean that either kind of arrears is showing a tendency to shrink in global terms, but it does imply that they both tend to quicken their turnover.

It was a most welcome innovation last year that the government, in its Report on the Economic Situation in Italy, gave far more analytical details about budgetary arrears, so that it is now possible to sort out what belongs to the present, what to the past and what to the future.

If, on the basis of these indications, the end-1962 figures of arrears are corrected by eliminating purely nominal items, items not admitting of immediate disbursement for administrative reasons, and items already settled in cash in the meantime, the total of disbursements due falls from 2,546 to 1,181 billion lire, and the total of receipts due from 921 to 601 billion; consequently, the balance of liabilities contracts from 1,625 to 580 billion lire. This is still rather worse than the situation on June 20, 1961, when the corresponding corrected figures were 980, 560 and 420 billion lire.

VI. *The Money and Capital Markets and the Control of Liquidity*

Throughout 1962 the monetary authorities endeavoured to keep the market liquid enough to supply a regular flow of funds to the expanding economy. At the same time they strengthened the structural position of the money market with a view to making it more efficient and to facilitate control of money and capital flows.

For the first time since compulsory reserves were introduced in 1947, the reserve ratio was altered in January last year, when bank liquidity began to be under some strain. The maximum ratio was reduced from 25 to 22.5 per cent; it varies with the size of deposits and the minimum for commercial banks was fixed at 10 per cent of deposits. These measures set free liquid resources throughout the whole banking system.

With the intention of making the money market more flexible, and of eliminating the drawbacks of the previous open tap system of issuing Treasury Bills and of the banks' ability to vary the composition of their compulsory reserves at will, the Joint Ministerial Committee on Credit, at its meeting on May 16, 1962, pronounced itself in favour of a reform of the Treasury Bill issue and of certain amendments to the rules governing compulsory reserves.

So long as Treasury Bills were issued in unlimited quantities, the banks had it in their power to get the Treasury into debt beyond its actual cash requirements, and at rates of interest which bore no relation to the market situation.

When the reform project was discussed in last year's Annual Report, it was already pointed out that a constant Treasury Bill rate reduced the incentive for the banks to look for commercial employment of their funds and distorted the flow of liquid resources as well as the whole system of money rates. When the banks were liquid, it was profitable for them to invest their excess cash in an easily monetizable security, and this swelled the Treasury's deposits in current account with the Bank of Italy and was apt to convey a false impression of financial ease.

The reform has now created a money market paper carrying an interest rate variable according to the market's liquidity position, issued in limited quantities according to the Treasury's cash needs, and negotiable with the central bank. The reform was enacted on October 12, 1962, by a decree by the Minister of the Treasury, which lays down the rules governing the issue of Treasury Bills. Since last November, therefore, Treasury Bills have been issued once a month only and in amounts determined before the 10th day of the month of issue, in relation to the banks' requirements for purposes of their compulsory reserves and to the Treasury's cash needs; the day of allocation is the 25th of the month.

At present, the Treasury Bill rate is 3.50 per cent, which corresponds to an issue price of 96.50 for every 100 lire nominal value. This is called the basic price, and bidding above it must be in 10 hundredths of a lira or multiples thereof.

Treasury Bills are allocated exclusively to banks and banking associations. These receive, at the basic price, the full amount they need to fill up their compulsory reserves; the rest of the monthly quota is allocated to them for free investment at the so-called free price, that is, the lowest still successful bid. Any unallocated Treasury Bills can be bought by the Bank of Italy at the basic price. At any time during the month the banks can deal in Treasury Bills with the Bank of Italy, and private investors wishing to buy or sell them can do so at the Bank of Italy or at other banks.

The Bank of Italy buys Treasury Bills from banks or the public at a price adjusted to the remaining maturity by the basic rate, and sells them at a price similarly adjusted by the free rate, that is, the last successful bid.

The second part of the reform was an amendment to the rules governing compulsory reserves. Banks are now no longer free to vary the distribution of their reserves between cash and securities at will. Since December 1, 1962, cash reserves may not fall below 10 per cent of the excess of deposits over capital, which means, in practice, that compulsory reserves are now made up of a 44 per cent cash component and a 56 per cent Treasury Bill component; the Bills deposited remain tied until maturity.

The same limitations with respect to the amount and substitutability of Treasury Bills also apply to the reserves of savings banks.

At its meeting on November 16, 1962, the Credit Committee adopted measures to control the movement and rates of interest of interbank deposits and to fit them into the money market which was being created. This was important in so far as the amounts involved are large, often include much of the liquid resources of minor banks, and, when remunerated at high rates, raise money costs and discourage investment in securities.

For these reasons it was laid down that interest rates applicable to interbank deposits may not exceed the free Treasury Bill rate as established at the monthly tenders.

To ensure compliance with this rule, the Committee empowered the Bank of Italy to require all, or specific, banks to pay into special time deposits at the Bank all or part of the funds held in deposit or current accounts from other banks; these special accounts at the Bank of Italy earn 2.50 per cent if tied for three months, or 2.75 per cent if tied for six months. The same rates are applicable to voluntary deposits by banks; since they are lower than the permissible rates on interbank deposits, a contravening bank required by the Bank of Italy under its new powers to hand over its interbank deposits would lose the difference between the interest rate it has to pay on these deposits and the rate it earns from the Bank of Italy.

On January 28, 1963, the Credit Committee took yet another step towards reorganizing the money and capital markets and differentiating interest rates.

First of all, the Committee formally acknowledged that the interbank agreement is in the public interest and that the interest rates paid on interbank deposits answer the need to differentiate short rates from medium and long rates and so to ensure the orderly functioning of the capital market. To avoid distortions in the distribution of liquid funds and to re-establish equilibrium between the different sectors the Bank of Italy has powers to require one or more banks to channel part of their resources into specified types of investment.

The Committee furthermore decided that the control of interest rates was an integral part of the interbank agreement, of the agreement among special credit institutes, and of the authorization for the issue of securities. To eliminate ambiguities, it was stated explicitly that 18- to 60-month time deposits were to be regarded as medium-term savings deposits and that the interest rate on them may not exceed 5 per cent; banks may not accept deposits tied for more than 18 months, nor special credit institutes deposits tied for less than 18 months, barring exceptions defined by law or by the Committee itself.

To foster the integration of the Italian capital market into foreign markets, to adapt its interest rates to the latter and so to enhance the efficiency of the capital market, Italian residents have been authorized to invest in securities, both shares and bonds, quoted on stock exchanges abroad. This measure is the counterpart, on the capital market, of another taken with respect to the money market in November, whereby banks were authorized to carry foreign exchange debt balances.

The more precise definition of short-, medium- and long-term funds does away with overlapping and mutual interference between the different sectors and avoids the distortion of interest rates; at the same time it makes room for a transfer of funds from one to the other sector at conditions and rates which correspond both to the changing market situation and to the public interest.

Liquidity Control.— The economy's growing liquidity requirements were last year satisfied almost entirely by the banks, seing that neither the public sector nor the foreign sector created much liquidity.

Banks had been in a rather tight position ever since the middle of 1961, when the central bank stepped in to enable them to satisfy credit demand by firms. During the second half of that year, it will be recalled, the Bank of Italy put 205 billion lire at the banking system's disposal, mainly through foreign exchange credits by the Italian Exchange Office. This method was chosen at the time in the light of the country's favourable foreign exchange reserve position and of the particular liquidity needs of the big banks, which have a large foreign business and lost some of their liquidity as a result of their obligation to settle their foreign debt balances. These banks have, in any event, considerable liquidity needs not only because their credit business is larger, but also because they are the depositaries of part of the medium and small banks' liquid resources.

In the expectation of a further expansion of credit demand and of a less friendly disposition on the capital market, about 200 billion lire of bank resources were set free in January 1962 through a 10 per cent reduction of the compulsory reserve ratio. The banks used about half these funds to decrease their indebtedness to the Exchange Office and the Bank of Italy, and the rest for normal credit business and for the purchase of considerable amounts of bonds issued by special credit institutes.

During the second quarter of the year, when both the Treasury and the foreign sector absorbed liquid resources, the exceptionally large increase in bank assets was made possible by a further liquidity injection of 142 billion lire, in the form of advances in domestic and foreign currency.

During the last quarter of the year, which was characterized by a large balance-of-payments deficit and very strong credit demand, the banks turned to the Bank of Italy for yet another 168 billion lire, mostly through drawings on their credit margins.

At the same time Italian banks were again authorized to maintain debt balances abroad. The idea was to enable liquid resources to be shifted from one market to another and to level out short-term interest rates. Taking advantage of this provision, the banks raised 285 billion lire of liquid resources abroad in the second half of 1962, and another 96 billion during the first quarter of the current year.

Indirectly, bank liquidity was eased to the extent of 192 billion lire by the redemption of Nine-year Treasury Bonds maturing on January 1st, 1963, and by the permission to use bonds and shares as backing for cashier's cheques; this should gradually, as the cheques fall due, release about 90 billion lire's worth of Treasury Bills now deposited as collateral.

The economy's gross liquid assets at the end of 1962 amounted to 18,323 billion lire (Table 24), having risen by 2,712 billion or 17.4 per cent over the year, compared with a corresponding

TABLE 24

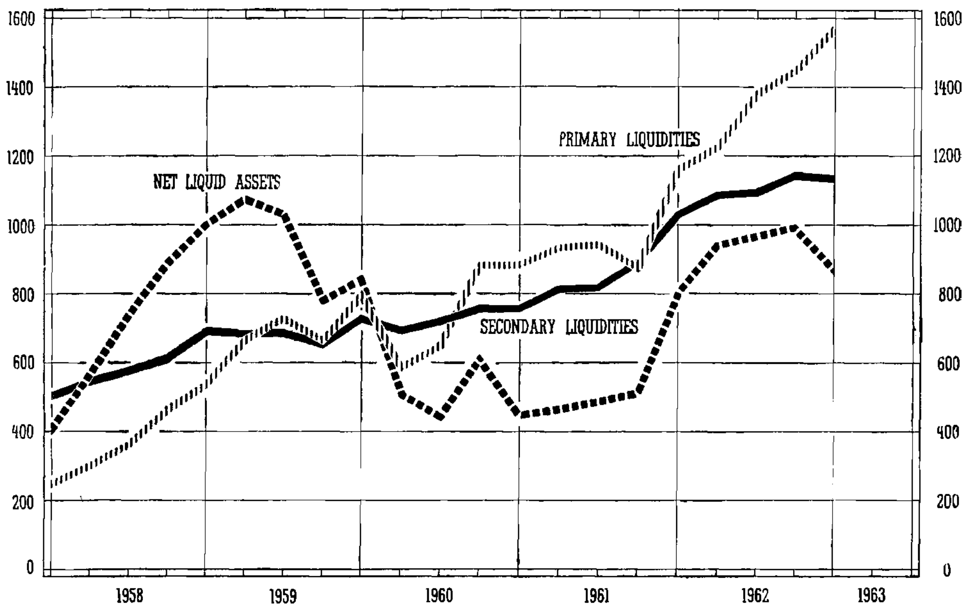
Short-term Credit and Liquid Assets

(end-year figures in billion lire)

Year	Credits to				Gross liquid assets			Surplus of		Net liquid assets
	Treasury	Private sector	Foreign sector	Total	Primary liquidities	Secondary liquidities	Total	Credits over primary liquidities	Gross liquid assets over credits	
	1	2	3	4=1+2+3	5	6	7=5+6	8=4—5	9=7—4	10=7—2
1955 . . .	3,380.6	3,681.3	484.4	7,546.3	4,523.1	2,878.6	7,401.7	3,023.2	— 144.6	3,720.4
1956 . . .	3,469.7	4,220.7	593.9	8,284.3	4,910.6	3,371.8	8,282.4	3,373.7	— 1.9	4,061.7
1957 . . .	3,531.1	4,577.1	782.1	8,890.3	5,169.6	3,874.1	9,043.7	3,720.7	153.4	4,466.6
1958 . . .	3,821.9	4,799.6	1,248.6	9,870.1	5,702.3	4,564.3	10,266.6	4,167.8	396.5	5,467.0
1959 . . .	3,897.3	5,479.8	1,782.2	11,159.3	6,497.0	5,294.0	11,791.0	4,662.3	631.7	6,311.2
1960 . . .	3,897.5	6,655.6	2,113.6	12,666.7	7,379.5	6,050.1	13,429.6	5,287.2	762.9	6,774.0
1961 . . .	3,878.9	8,046.9	2,476.2	14,402.0	8,534.9	7,076.7	15,611.6	5,867.1	1,209.6	7,564.7
1962 . . .	4,019.5	9,718.1	2,515.2	16,252.8	10,103.9	8,219.3	18,323.2	6,148.9	2,070.4	8,605.1

increase of 2,182 billion or 16.2 per cent in 1961. 1,569 billion lire of gross liquid asset formation last year was in the form of primary liquidities (bank notes, coin and current accounts) and 1,143 billion in the form of secondary liquidities (Chart 4).

CHART 4

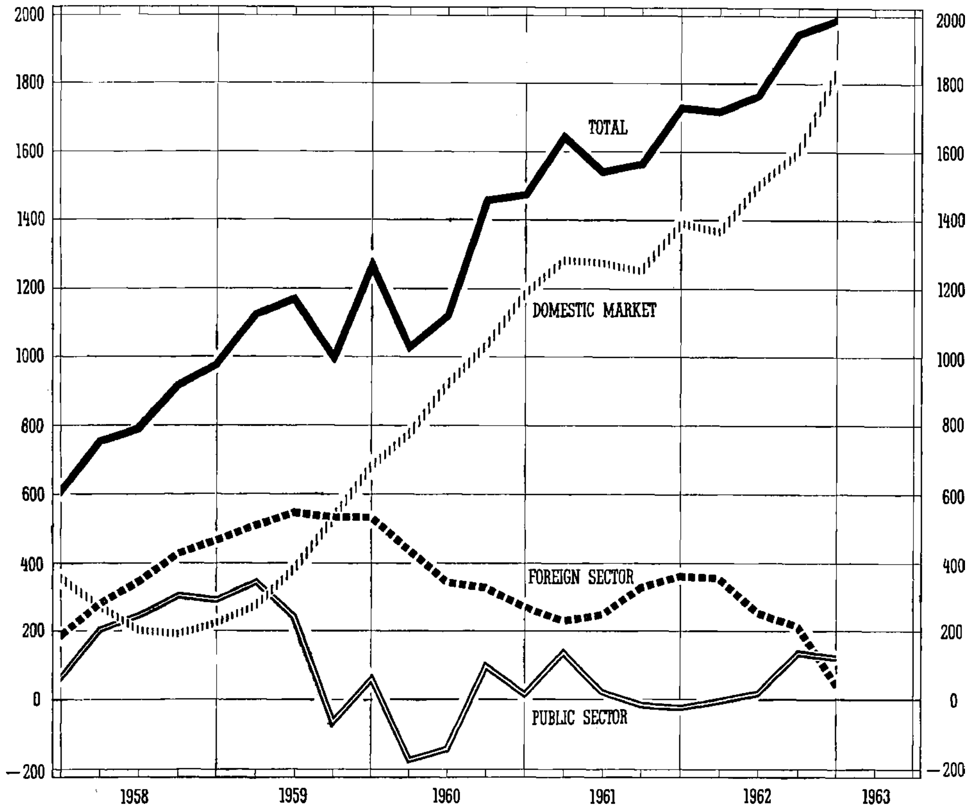


Liquid assets

(12-month changes at quarterly intervals; billion lire)

Total liquidity creation through the short-term credit system amounted to 2,014 billion lire (Chart 5), of which 39 billion lire are attributable to the foreign sector, 140 billion to the Treasury and 1,835 billion to credits to the domestic market. In overall terms, the percentage increase was only a little larger than in 1961, but with reference to the domestic market alone it was a good deal larger, namely, 23.3 per cent compared with 20.9 per cent in 1961.

CHART 5



Short-term credit

(12-month changes at quarterly intervals; billion lire)

Banking.— On December 31, 1962, there were 1,258 registered banking firms in Italy, 3 less than at the same date in 1961, 12 firms having been struck and 9 newly registered.

A good indication of the present structure of the Italian banking system is the classification of banks, bank deposits and bank loans according to the geographical range of operations, the size of deposits and the legal status of the banks. From the first point of view, it is interesting to note the relative importance in the Italian system of banks operating within a fairly small geographical range. Banks operating in 30 or more provinces had 32 per cent of all bank deposits and were responsible for 38 per cent of all bank loans at the end of 1962; banks operating in more than 1 but less than 30 provinces accounted for 49 per cent of total deposits and 48 per cent of total loans, and the figures for banks operating in one province only were 19 per cent of deposits and 14 per cent of loans. These figures, as well as the divergence between the respective proportions of deposits and loans, confirm that it is one of the functions of the big banks to redistribute, through the mechanism of interbank deposits, part of the resources of smaller banks.

Another interesting point is brought out by Table 25, which shows that in Southern Italy and the Islands 60 per cent of deposits and loans are handled by 6 big banks which, on the national scale, account for 41 per cent of total loans and 35 per cent of total deposits. In capital-deficient provinces, therefore, the banking system is largely represented by nation-wide banks which are institutionally well equipped to ensure a flow of funds from one part of the country to another in any direction.

Classification by the amount of deposits shows the strength of the central range of banks. Leaving aside at one extreme small rural and artisan savings banks and a few others with less than 1 billion lire of deposits, and at the other extreme the biggest banks with more than 100 billion of deposits, the central 388 banks represented 31 per cent of the total number of banking firms, held 31 per cent of total deposits at the end of 1962 and handled 26 per cent of total loans. For the rest, the big banks' higher loan/deposit ratio confirms again their intermediating functions. Banks with more than 100 billion lire of deposits had a loan/deposit ratio of 81 per cent at the end of last year, banks with less than 1 billion a ratio of 55 per cent.

As regards legal status, finally, the four major categories of banks—public-law credit institutes, banks of national interest, commercial banks and savings banks—were remarkably

TABLE 25

Loans and Deposits of Some Categories of Banks Classified by Major Geographical Areas

(end-1962 figures; billion lire)

Banks	Loans				Deposits			
	Northern Italy	Central Italy	Southern Italy & Islands	Total	Northern Italy	Central Italy	Southern Italy & Islands	Total
	Absolute figures							
Banks of national interest . . .	1,630	485	361	2,476	1,597	662	443	2,702
6 big banks	2,531	993	973	4,497	2,310	1,424	1,316	5,050
Other banks	4,452	1,434	620	6,506	6,806	1,808	808	9,422
All banks	6,983	2,427	1,593	11,003	9,116	3,232	2,124	14,472
	Percentage share in national total							
Banks of national interest . . .	*65.8*	*19.6*	*14.6*	*100.0*	*59.1*	*24.5*	*16.4*	*100.0*
6 big banks	*56.3*	*22.1*	*21.6*	*100.0*	*45.7*	*28.2*	*26.1*	*100.0*
Other banks	*68.4*	*22.1*	*9.5*	*100.0*	*72.2*	*19.2*	*8.6*	*100.0*
All banks	*63.5*	*22.0*	*14.5*	*100.0*	*63.0*	*22.3*	*14.7*	*100.0*
	Composition per cent							
Banks of national interest . . .	*23.3*	*20.0*	*22.7*	*22.5*	*17.5*	*20.5*	*20.9*	*18.7*
6 big banks	*36.2*	*40.9*	*61.1*	*40.9*	*25.3*	*44.1*	*62.0*	*34.9*
Other banks	*63.8*	*59.1*	*38.9*	*59.1*	*74.7*	*55.9*	*38.0*	*65.1*
All banks	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

evenly distributed. In terms of total deposits, the range was between 25 per cent for savings banks and 19 per cent for banks of national interest at the end of 1962, and in terms of assets it was between 24 per cent for public-law credit institutes and 20 per cent for savings banks and their banking association. Poeple's co-operative banks handled something like 11 per cent both of deposits and credits.

The Bank of Italy's controls over the banking system are partly preventive and partly corrective. The former work through a system of authorizations and usually apply only to a few aspects of banking business. The latter, on the other hand, are designed to discover and repress irregularities and non-compliance and, in serious cases, may lead to the dissolution of managing bodies or even to the liquidation of the firm.

The boundaries between the two kinds of controls are not rigorous, in so far as any authorization normally requires a previous check-up, and in turn a check-up can lead to the granting of an authorization previously withheld.

The system is complemented by the Bank of Italy's part in preparing official regulations affecting the banking system. On the one hand it makes the requisite enquiries and drafts the provisions subsequently embodied in ministerial decrees, and on the other hand it scrutinizes draft bills and furnishes such information as the branches of government may need.

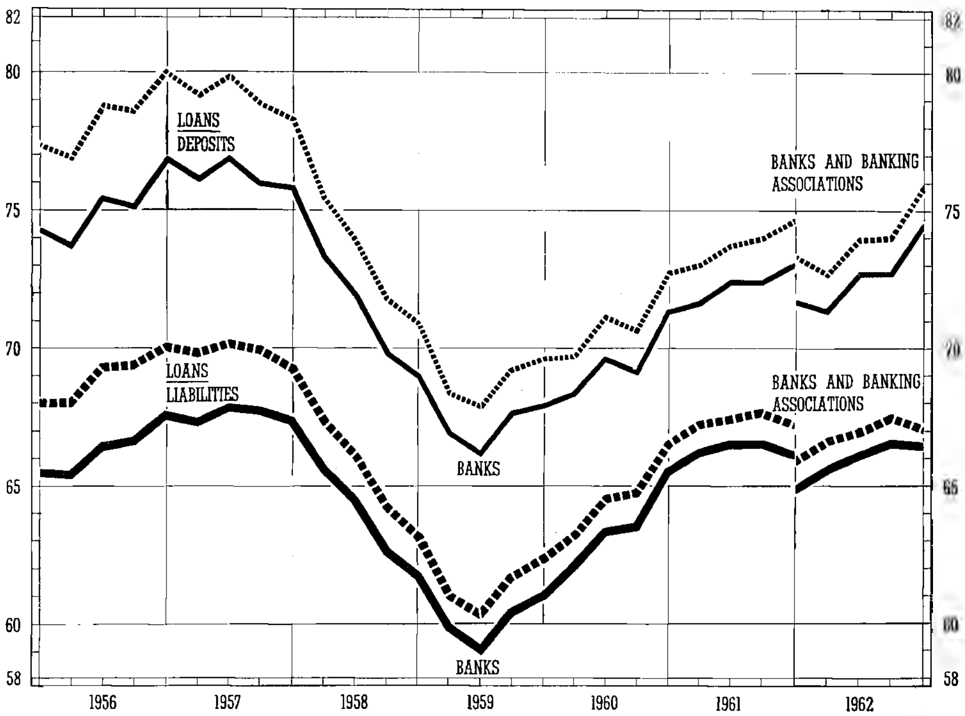
Finally, the Bank of Italy engages in what may be called collateral activities in making special studies, for example, in 1962, of the standard statute of some categories of banks.

Bank Liquidity.— The general business conditions more than once recalled in this Report last year caused the demand for bank credit to expand very considerably. In response to this demand, which had actually become insistent already towards the end of 1961, the banking system stepped up its lending at a steadily accelerating pace throughout the year, save for seasonal variations.

Another important feature of banking operations last year was the increase in security investments: about one third of all security issues on the capital market was absorbed by the banking system, as against 20 and 21 per cent in 1961 and 1960, respectively.

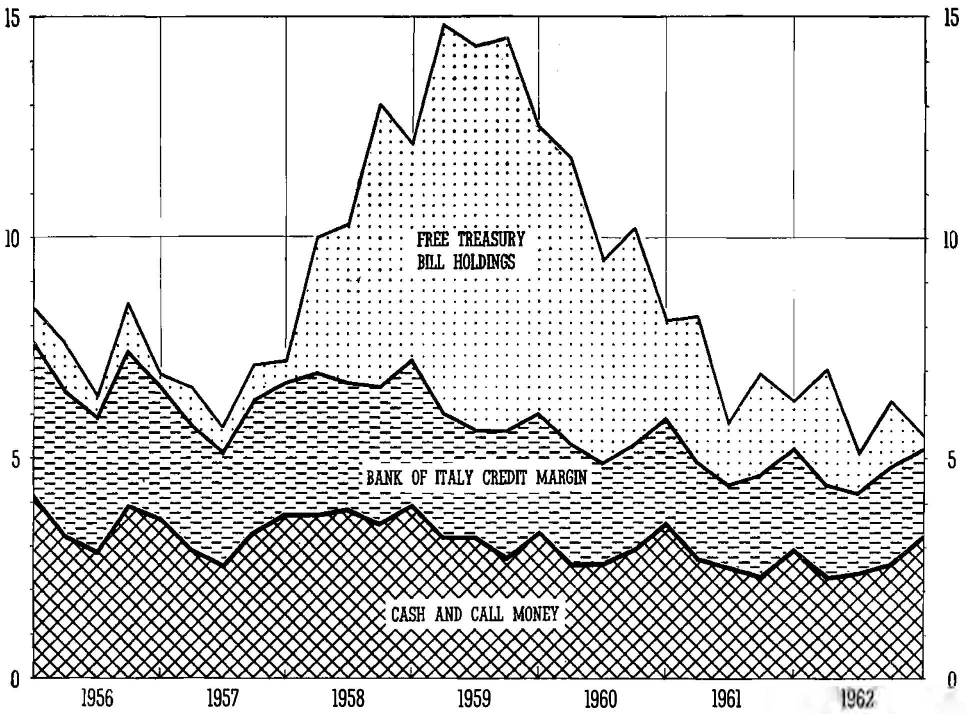
However, the pressure towards a more rapid expansion of bank credits found no adequate counterpart in the rate of growth of deposits (Chart 6). The widening gap between the two rates of expansion made things all the more difficult for the banks as the excess liquidities they had accumulated in 1958 and 1959 had already been largely used up in 1960 and all but exhausted in 1961. Towards the middle of 1961, in fact, the banks' liquid assets had touched the lowest level since the 1958 trough, both in absolute terms and in relation to deposits (Chart 7).

CHART 6



Percentage ratio of bank loans to deposits and total liabilities

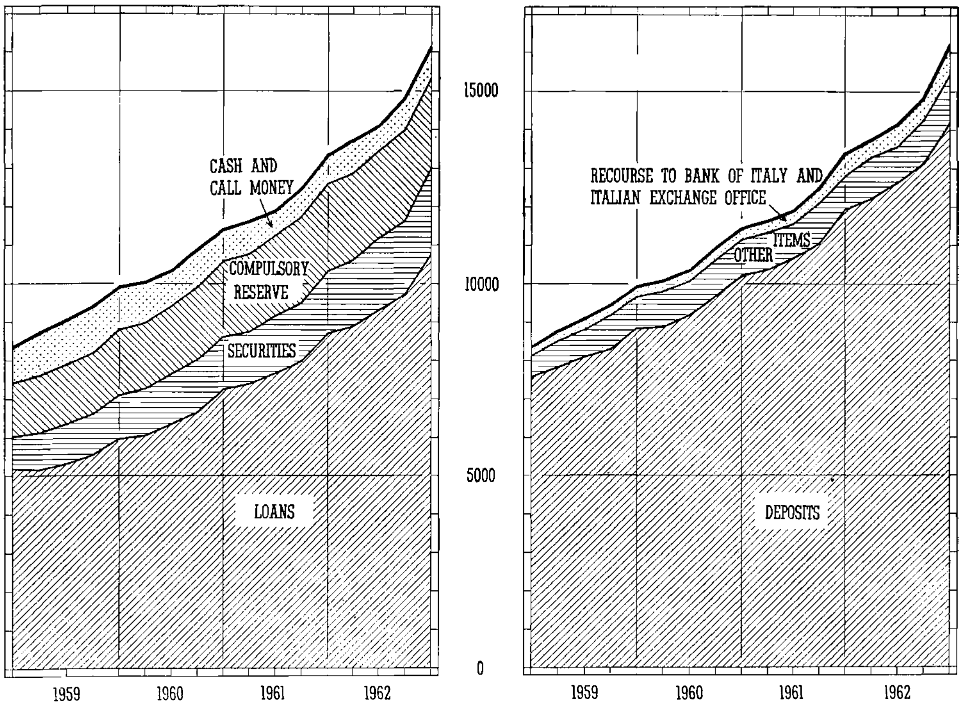
CHART 7



Percentage ratio of liquid assets to deposits

Notwithstanding these difficulties, the banking system expanded its assets last year by 1,995 billion lire, or 22.8 per cent, to reach an end-year total of 10,737 billion lire. In 1961 the increase had been 500 billion lire less than that, and the percentage rate nearly 3 points lower (Chart 8).

CHART 8



Consolidated balance sheet of the banking system

(end-quarter figures in billion lire)

Foreign currency credits again expanded more than lire credits, and indeed lengthened their lead in 1962, given the wider scope of foreign exchange lending operations and the differentials of domestic and international rates of interest. As in 1961, it was the big banks that were most active in this field, but other banks too moved in to an appreciable extent.

The banks' security investments, in their turn, grew much more than they had done in 1961—by 567 as against 334 billion lire.

Bonds issued by special credit institutes, I.R.I., E.N.I. and business companies, took up 86 per cent of the new investments

(46 per cent in 1961), whereas the increase in Treasury Bill holdings was only half as big as the year before; other government securities took up less new bank money, and holdings of railway bonds and bonds issued on behalf of the Treasury declined a little.

So much for the growth of bank assets. Bank deposits in their turn grew at a faster rate than in 1961. Over the whole year, they increased from 11,914 to 14,165 billion lire, the increment of 2,251 billion representing a rate of growth of 18.9 per cent; in 1961 they had increased by 1,738 billion, or 17.1 per cent.

Current accounts were the spearhead of the advance, in contrast to 1961 when savings deposits increased most. These latter last year expanded only a little more than they had done in 1961, namely, by 1,134 billion lire or 17.8 per cent, as against 17.2 per cent in 1961. Technically, this was due to a slowing-down in the accumulation of time deposits for the first time since the war. Given the public's marked liquidity preference, the sharp increase in sight deposits more than offset the slow-down in time deposits.

Special Credit Institutes.— As forecast in last year's Annual Report, there was growing investment demand last year both in the public and the private sector for the types of medium- and long-term credit which special credit institutes provide, with consequent heavy commitments for the institutes.

New resources accruing to them amounted to 1,300 billion lire, 300 billion more than the year before; the rate of expansion, at 25.8 per cent, also exceeded the 1961 rate of 24.3 per cent.

Net of the 176 billion lire proceeds of bonds issued by the Credit Consortium for Public Works on account of the Treasury, and net also of stockpiling operations largely financed by rediscounts from the central bank, new resources still expanded by 1,058 billion or 24.2 per cent, as against 809 billion or 22.8 per cent in 1961. To a greater extent than before, the source of these new funds was the capital market, thanks in part to the banking system's large-scale subscription to the bonds of special credit institutes.

Bond issues, which had furnished 537 billion lire in 1961, provided 765 billion last year, and their share of new resources for ordinary loans rose from 66.4 to 72.3 per cent; at 29.7 per cent, their rate of expansion was more than 5 points ahead of the rate of expansion of total resources. Correspondingly, the special credit institutes gained yet more weight in the capital market: in terms of net proceeds, the institutes' 718 billion lire accounted for 43.7 per cent of all new security issues last year, as against 39.5 per cent in 1961 (Table 26), and for 69.5 per cent of all fixed-interest security issues, as against 58.1 per cent in 1961.

TABLE 26

Special Credit Institutes' Loans and Bonds Outstanding (1)

Type of institute and loan	End-year figures (billion lire)		Annual increases (per cent)	
	1961	1962	1961	1962
Industrial credit institutes:				
Loans	2,622.6	3,295.2	*21.4*	*25.6*
of which: on special funds	189.5	174.6	*— 9.8*	*— 7.9*
Bonds	1,591.3	2,057.9	*22.9*	*29.3*
Land and building credit institutes:				
Loans	955.8	1,284.3	*33.5*	*34.4*
Bonds	916.1	1,209.1	*35.5*	*32.0*
Agricultural credit institutes:				
Land improvement credits	284.2	311.0	*10.4*	*9.4*
Bonds	64.2	69.7	*2.6*	*8.6*
Total:				
Medium- and long-term loans	3,862.6	4,890.5	*23.3*	*26.6*
Bonds	2,571.6	3,336.7	*26.4*	*29.7*

(1) Excluding loans to the Treasury, short-term credits to agriculture and stockpiling finance.

More funds were provided to special credit institutes by the banking system in one form or another last year, especially during the third and fourth quarters.

Time deposits and interest-bearing certificates, on the other hand, furnished only 65 billion lire, as against 77 billion in 1961, so that their share in new resources for ordinary loans dropped from 9 to 6 per cent.

Similarly, new resources originating in foreign loans and in large part ear-marked for Southern Italy were a good deal less than in 1961, namely, 9 as against 33 billion lire.

All these new resources went into an overall credit expansion of more then 1,300 billion lire, or 28.1 per cent, which, in relative terms, exceeded even the 1961 record rate of 24.3 per cent. It was the sequel of an expansion which began in the middle of 1961 and fits into the pattern outlined in last year's Annual Report, namely, that medium- and long-term credit operations by special credit institutes were in a phase of expansion owing to the Treasury's increasing reliance upon them and to the largely induced growth of credit demand by private firms.

The Stock Exchange.— In the presence of the saving public's patent unwillingness to invest in securities and of increased financial requirements by firms, the supply of security issues was regulated through a system of authorizations, which apply to the quality, quantity and timing of issues, and large portions of the supply were absorbed by banks and other institutional investors.

Net of redemptions and duplications, the proceeds of security issues last year were 1,642 billion lire, or 26 per cent more than in 1961 (Table 27); since the government again made no direct claims on the market, this sum was entirely raised on shares and non-government bonds. From the same Table it will be seen how prominent a part the banking system played as a source of investable funds: stepping up their bond subscriptions by 278 billion lire over 1961, the banks took up 506 billion last year, largely bonds issued by special credit institutes. Outstanding among other institutional investors was the Central Post Office Savings Fund which, after only 17 billion mostly for industrial credit bonds in 1961, last year took bonds for 109 billion, of which 55 billion from special credit institutes, and 43 billion Green plan bonds in exchange for an equal amount of Nine-year Treasury Bonds maturing on January 1, 1962.

Private investors and companies, while still playing a conspicuous part, provided rather less new funds than the year

TABLE 27

New Security Issues (1)

(billion lire)

Types of security	1961 Bank of Italy & Italian Exchange Office	1961 Banks (2)	1961 Special Credit Institutes	1961 Central Post Office Savings Fund	1961 Insurance companies & social insurance funds	1961 Private investors and companies	1961 Total	1962 Bank of Italy & Italian Exchange Office	1962 Banks (2)	1962 Special Credit Institutes	1962 Central Post Office Savings Fund	1962 Insurance companies & social insurance funds	1962 Private investors and companies	1962 Total
Government securities:														
Government stock	2.5	7.6	0.5	− 1.0	3.6	− 21.1	− 7.9	− 47.4	28.7	− 5.3	− 43.2	− 1.0	− 40.3	−108.5
Bonds issued for Treasury account (3)	16.6	55.9	3.7	3.1	10.7	53.2	143.2	77.0	− 9.1	− 3.8	99.1	0.2	7.1	170.5
Total	19.1	63.5	4.2	2.1	14.3	32.1	135.3	29.6	19.6	− 9.1	55.9	− 0.8	− 33.2	62.0
Bonds:														
Industrial credit institutes	3.0	78.4	− 0.6	15.4	16.1	171.6	283.9	2.3	248.7	1.2	31.2	81.0	73.0	437.4
Other special credit institutes	0.3	63.2	7.2	—	34.6	124.8	230.1	− 0.1	118.8	19.3	23.3	30.0	89.5	280.8
I.R.I.	− 0.1	10.0	0.8	− 0.7	4.3	55.2	69.5	—	20.3	− 2.9	− 1.1	− 3.1	− 18.0	− 4.8
E.N.I.	—	11.2	—	—	4.3	30 4	45.9	—	54.7	1.0	—	− 3.0	12.1	64.8
Business companies	—	− 7.9	0.1	—	1.7	99.5	93.4	0.2	36.8	2.2	—	11.4	113.6	164.2
Local authorities	—	—	—	—	—	11.5	11.5	—	—	—	—	—	− 0.5	− 0.5
International credit institutions	2.1	9.5	0.2	—	—	3.2	15.0	5.1	7.1	5.0	—	—	12.8	30.0
Total bonds	5.3	164.4	7.7	14.7	61.0	496.2	749.3	7.5	486.4	25.8	53.4	116.3	282.5	971.9
Shares							530.7							716.5
less Duplicated items . . .							*113.9*							*108.3*
Total shares (net)						416.8	416.8						608.2	608.2
Total bonds and shares						913.0	1,166.1						890.7	1,508.1
Grand total	24.4	227.9	11.9	16.8	75.3	945.1	1,301.4	37.1	506.0	16.7	109.3	115.5	857.5	1,642.1

(1) Actual proceeds, net of redemption.
(2) Including banking associations.
(3) Railway, Green Plan and Rural Housing Bonds.

before, namely, 858 billion as against 945. These were strongly concentrated in equities (608 billion as against 417 billion in 1961), while bonds were out of favour and attracted only 250 billion, as against 528 billion in 1961. Allowing for the higher total, the share of private investors and companies dropped from 73 per cent in 1961 to 52 per cent last year.

At the end of 1962, 7,880 billion lire of fixed-interest securities were in circulation, of which 2,254 billion were government stock and 1,913 billion of the latter Nine-year Treasury Premium Bonds. Of the 5,626 billion lire of other bonds, special credit institutes accounted for 3,336 billion.

The total amount was made up of 29 per cent of government securities and 71 per cent of other bonds; an almost identical distribution was evident in the bond holdings of the banking system.

In absolute figures, banks held 2,243 billion lire of fixed-interest securities at the end of last year, of which 573 billion in Treasury Bonds and 1,083 in bonds of special credit institutes; private investors had 4,360 billion (1,121 Treasury Bonds and 1,652 bonds of special credit institutes); and finally, insurance companies and social insurance funds owned 550 billion, of which 390 were bonds of special credit institutes.

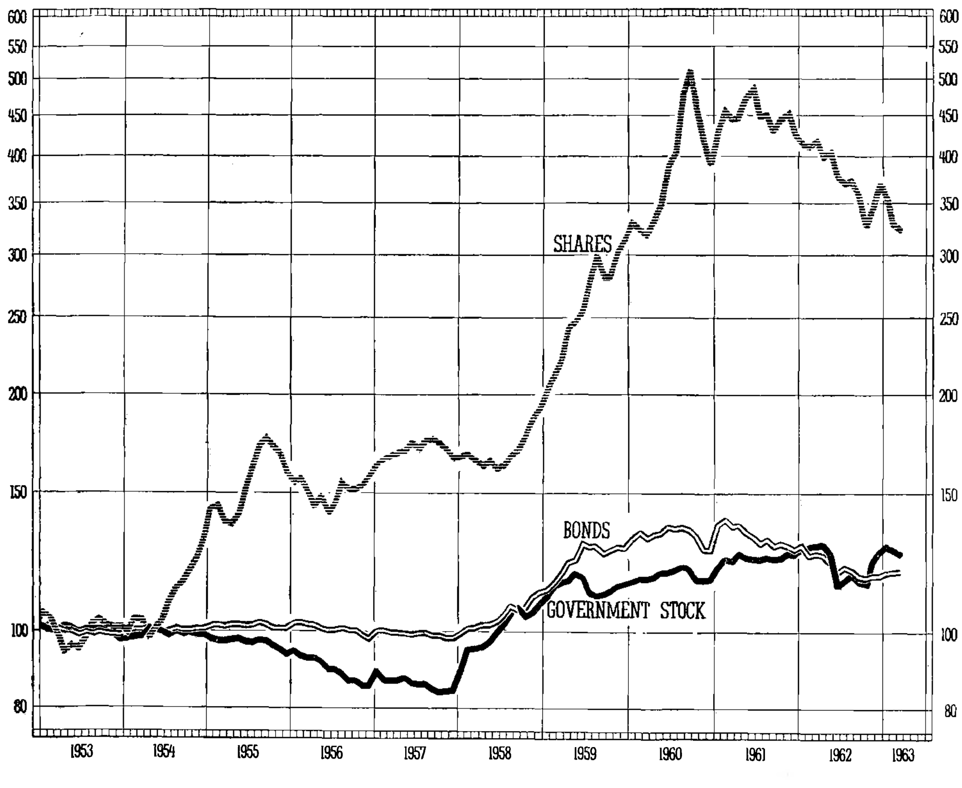
From the point of view of prices, the stock exchange had a trying year in 1962. Inevitably, the slump in stock prices abroad had its depressing influence in Italy, and the psychological repercussions of the government's economic policy further unsettled a market which, after its almost uninterrupted climb between the middle of 1958 and the middle of 1961, was uncertain enough already.

The nationalization of the electricity industry and the withholding tax on dividends caused an alternating pattern of retreat and slight recovery of stock prices, and the long and laborious legislative path of both provisions left the undertone of the market generally weak. When the electricity nationalization bill was finally enacted, the market had already discounted its effects, but the withholding tax continued to cast its shadow over stock prices well after it became law.

The strain was somewhat eased by the whole set of monetary and credit measures adopted to reorganize the market, and their stimulating influence was evident especially towards the end of the year and in the early months of 1963.

Over the whole year, both bond and share prices declined almost uninterruptedly, though fluctuations were rather more frequent and wider in the equity section (Chart 9). Government stocks did comparatively well by ending the year at much the

CHART 9



Indices of stock exchange prices
(1963 = 100; semilogarithmic scale)

same price as they had entered it, thanks to a marked recovery during the latter half of the year which more than wiped out the sharp June losses. The value index of 1 lira of yield (1953 = 100) was 126.2 at the end of december 1962, as against 124.9 at the end of 1961.

Average annual yields were higher than in 1961 in all sections of the market. For non-government bonds yields rose slowly but continuously from 5.44 to 5.95 per cent; government stock, on the other hand, maintained a fairly constant average yield of 4.80 per cent throughout the first five months of the year, then yields jumped to 5.30 per cent on the average during the five following months, dropped back to 5 per cent in November and finally to 4.88 per cent in December.

Equity yields rose from an average of 2.90 per cent during the first five months to 3.50 per cent until the end of October, and finished the year with 3.69 per cent in November and 3.45 per cent in December (Chart 10).

CHART 10

Security yields

(per cent per annum)

VII. *The Economy's Total Supply and Use of Funds*

The Supply of Funds: The Credit System and the Capital Market.— Between them, the credit system and the capital market furnished the economy last year with new medium- and long-term funds in the amount of 2,356 billion lire—more than twice as much as only three years ago (1,008 billion in 1959) and well in excess of the 1,786 billion of 1961.

Special credit institutes, the Central Post Office Savings Fund and insurance companies and funds together provided 1,524 billion lire, 32.6 per cent more than the 1,149 billion of 1961. Business companies raised another 832 billion (as against 637 billion in 1961) through share and bond issues.

Including stockpiling bills, commercial banks furnished the economy with 2,098 billion lire of short-term funds, or 38.9 per cent more than in 1961, bringing their total supply of finance (excluding minor banking firms) to 10,995 billion lire at the end of 1962—23.2 per cent above the end-1961 level. The special credit institutes raised their total supply of funds to the economy by 26.3 per cent to an end-1962 total of 5,321 billion lire.

The Use of Funds: Public and Private Investment. Public investment expenditure in 1962 amounted to 1,438 billion lire, that is, 100 billion more than in 1961 (Table 28). The increment

TABLE 28

Public Investment Expenditure

(billion lire)

Investment by	1961	1962
Government	574	654
Local authorities	310	325
Autonomous government agencies	93	96
Cassa per il Mezzogiorno	229	218
Central Post Office Savings Fund	50	94
INA-Casa	82	51
Total . . .	1,338	1,438

came almost entirely from government spending, especially for agriculture and public works, and from the Central Post Office Saving Fund's higher investment in non-government bonds.

The slight reduction in the investment outlays of the *Cassa per il Mezzogiorno* is attributable to a falling-off of loans financed from foreign sources. INA-Casa, in its turn, spent less last year because it was winding up the last phase of its second seven-year investment programme, which has meanwhile been brought to its final conclusion in the early months of this year.

The higher financial requirements for public investment were covered principally by larger public saving, in the form of the current surpluses in the consolidated accounts of public administration (government, local authorities and autonomous government agencies) and by incurring larger debts—as was noted, for the Treasury's own indebtedness, in the Chapter on Government Finance.

TABLE 29

The Finance of Private Investment

(billion lire)

Sources	1961	1962
Share and bond issues	637	832
Loans by agricultural, land and building credit institutes (1)	267	355
Loans by industrial credit institutes (1)	423	619
	1,327	1,806
less Funds supplied by the Treasury to banks and credit institutes	90	141
	1,237	1,665
Loans by insurance companies (2)	53	78
	1,290	1,743
Depreciation reserves	1,475	1,637
Balancing item: direct investment by savers, self-financing by companies and net balance of short-term operations with banks	1,291	1,298
Total private investment	4,056	4,678

(1) Excluding loans to the public sector.
(2) Excluding loans to the public sector, security investment and bank deposits.

The private sector, in its turn, raised some 450 billion lire more on the capital market last year than in 1961; about half of these were the proceeds of share and bond issues, and the other half consisted almost exclusively of loans by special credit institutes.

Depreciation reserves went up by just a little over 10 per cent, and the balancing item (which includes direct investment by savers, self-financing by companies and the net balance of short-term operations with banks) remained pratically stationary (Table 29).

Money Supply and Finance Funds.— At the end of 1962 the total of money supply and finance funds at the economy's disposal amounted to 42,795 billion lire, including 18,323 billion of primary and secondary liquidities and 24,472 billion lire of securities and non-security assets other than liquid (Table 30). While the proportion of finance funds in the total had been growing of late, the shift was reversed in 1962 as a result of the fall in the market prices of shares (at which these are valued in the calculation) and of the considerable increase in gross liquid assets; the latter accounted for 43 per cent of the total at the end of 1962, as against 38 per cent at the end of 1961.

Finance funds, calculated without taking account of intervening changes in share prices, increased last year by 6.3 per cent, compared with a 17.4 per cent growth in gross liquid assets; with reference to the preceding year, the percentage increase of finance funds was a little less, and that of gross liquid assets more.

The reduced receptiveness of the market required more ample security investment by the credit system, that is, the Bank of Italy, commercial banks and banking associations, and the Central Post Office Savings Fund; as a result, considerable amounts of assets were shifted from the money to the capital market.

New medium- and long-term funds went almost entirely into the domestic market (Table 31), the total of 2,271 billion lire being made up of share issues and of loans and mortgages largely

TABLE 30

Flow of Money Supply and Finance Funds

(billion lire)

	end-1962 position	Annual changes 1960	1961	1962
Public sector.				
Short-term credit:				
Bank of Italy and Italian Exchange Office	299.6	39.9	− 223.3	34.9
Banks	2,690.3	− 31.3	179.9	190.3
Private investors and companies	1,029.6	54.4	24.8	− 84.6
Total . . .	4,019.5	63.0	− 18.6	140.6
Government securities:				
Banks	750.1	− 15.3	63.3	19.6
Central Post Office Savings Fund	152.5	1.1	2.5	55.9
Private investors and companies	1,620.0	170.4	50.4	− 43.1
Total . . .	2,522.6	156.2	116.2	32.4
Total public sector . . .	6,542.1	219.2	97.6	173.0
Domestic Market.				
Short-term credit:				
Bank of Italy and Italian Exchange Office	473.5	22.9	240.4	150.7
Banks	9,244.6	1,168.5	1,150.9	1,684.0
Total . . .	9,718.1	1,191.4	1,391.3	1,834.7
Loans and mortgages:				
Banks	1,009.4	98.5	128.4	165.1
Central Post Office Savings Fund	1,833.0	212.7	252.7	286.7
Special credit institutes	3,723.5	474.6	614.2	829.8
Insurance companies and Social Insurance Funds	1,173.2	111.9	112.0	141.3
Total . . .	7,739.1	897.7	1,107.3	1,422.9
Securities:				
Banks	1,681.9	253.0	209.5	526.9
Central Post Office Savings Fund	137.2	17.0	14.7	53.4
Private investors and companies	17,798.0	922.7	982.0	1,032.8
less issues by special credit institutes	3,336.7	430.5	537.4	765.1
Total . . .	16,280.4	762.2	668.8	848.0
Total domestic market . . .	33,737.6	2,851.3	3,167.4	4,105.6
Foreign sector.				
Net position of the Bank of Italy and Italian Exchange Office	2,893.1	101.0	387.4	308.0
Net position of the banks	377.9	167.6	− 24.8	− 269,0
Total foreign sector . . .	2,515.2	268.6	362.6	39.0
Total credit, loans, mortgages and securities . . .	42,794.9	3,339.1	3,627.6	4,317.6
Primary liquidities.				
Notes and coin	3,134.5	196.8	360.0	389.9
Current accounts	6,969.4	685.7	795.4	1,179.1
Total . . .	10,103.9	882.5	1,155.4	1,569.0
Secondary liquidities.				
Post Office savings books and savings deposits	7,993.0	732.8	995.3	1,231.3
Others	226.3	23.3	31.3	− 88.7
Total . . .	8,219.3	756.1	1,026.6	1,142.6
Non-security assets other than liquid.				
Bank of Italy and Italian Exchange Office	574.3	− 20.9	49.8	116.6
Banks	710.6	271.2	− 16.5	71.8
Central Post Office Savings Fund	2,208.8	201.1	191.1	221.9
Special credit institutes	386.8	44.1	76.8	64.7
Insurance companies and Social Insurance Funds	1,173.2	111.9	112.0	141.3
Total . . .	5,053.7	607.4	413.2	616.3
Securities.				
Government securities	1,620.0	170.4	50.4	− 43.1
Bonds by special credit institutes	2,119.0	225.0	353.8	294.0
Industrial, I.R.I. and E.N.I. bonds	1,279.0	202.0	211.4	130.6
Shares	14,400.0	495.7	416.8	608.2
Total . . .	19,418.0	1,093.1	1,032.4	989.7
Total money supply and finance funds . . .	42,794.9	3,339.1	3,627.6	4,317.6

TABLE 31

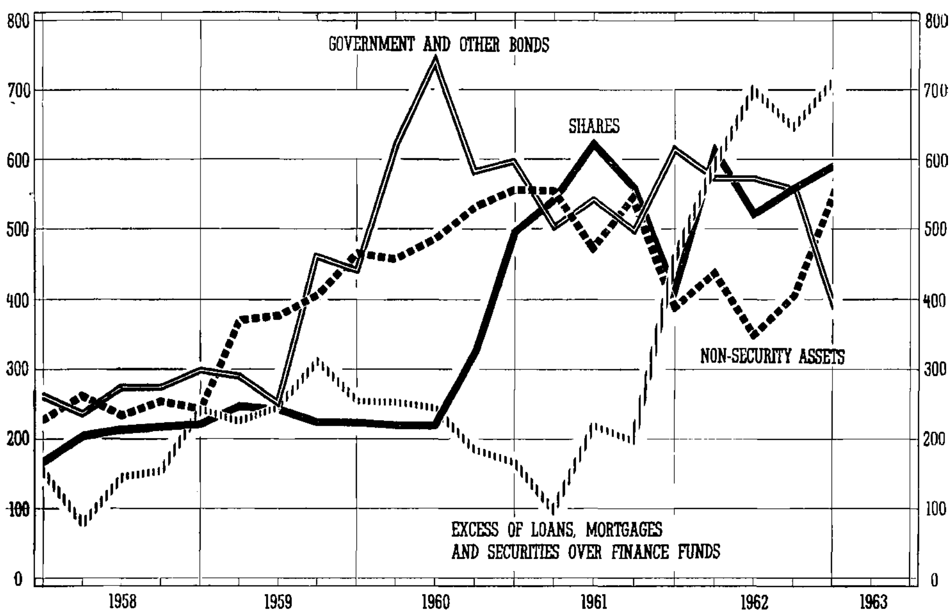
Loans, Mortgages, Securities and Finance Funds

(end-year position in billion lire)

	1955	1956	1957	1958	1959	1960	1961	1962
Loans, Mortgages and Securities	8,557.7	9,667.6	10,996.7	12,556.6	18,270.9	23,188.9	26,741.8	26,542.1
of wich:								
Treasury	1,583.3	1,751.2	1,826.7	1,832.5	2,166.5	2,346.3	2,469.1	2,522.6
Domestic market	6,974.4	7,916.4	9,170.0	10,724.1	16,104.4	20,842.6	24,272.7	24,019.5
Finance funds	8,702.3	9,669.5	10,843.3	12,160.1	17,639.2	22,426.0	25,532.2	24,471.7
of wich:								
Non-security assets (1) . .	2,382.3	2,638.5	2,866.3	3,106.1	3,594.2	4,186.0	4,599.2	5,053.7
Government securities (2)	1,025.0	1,116.0	1,179.0	1,170.0	1,391.0	1,585.0	1,642.0	1,620.0
Special credit institute bonds (2)	550.0	681.0	826.0	990.0	1,179.0	1,413.0	1,787.0	2,119.0
Other bonds (2)	335.0	394.0	482.0	674.0	735.0	952.0	1,154.0	1,279.0
Shares (2)	4,410.0	4,840.0	5,490.0	6,220.0	10,740.0	14,290.0	16,350.0	14,400.0
Excess of loans, mortgages and securities over finance funds . . .	—144.6	— 1.9	153.4	396.5	631.7	762.9	1,209.6	2,070.4

(1) Miscellaneous bank resources; time deposits at special credit institutes; Post Offices savings certificates and actuarial reserves of insurance companies excluding short-term credits and securities.
(2) In private or company ownership. The figures are based on market values, not on book values, nominal values or estimates as may appear in other Tables.

CHART 11



Security assets and non-security assets other than liquid

(12-month changes at quarterly intervals; billion lire)

by special credit institutes; the public sector claimed barely 32 billion lire as the net balance between the redemption of Treasury debts and new bond issues by the Credit Consortium for Public Works.

The cyclical pattern of non-liquid asset formation is illustrated in Chart 11, in terms of 12-month changes at quarterly intervals. It will be seen that until 1961 there was a marked inverse correlation between the curves for share issues and fixed-interest security issues (government and other bonds); this is explained by the fact that in phases of high liquidity and decreasing production investors prefer fixed-interest securities, while equity issues predominate during an upswing.

VIII. *Excerpts from the Governor's concluding remarks*

Gentlemen,

The considerations which I propose to put before you draw their substance from the whole body of our Report on the year 1962 and its detailed description and analysis of economic and especially monetary conditions.

Costs, Prices and the Balance of Payment.— The year 1962 was one in which the distribution of income among the factors of production underwent considerable modifications in Europe, and in Italy more than elsewhere. The share of labour increased to the detriment of the share of other factors, not without disturbance to the relations between employers and workers. Hand in hand with the redistribution of incomes went a rise in their nominal value proportionally larger than that of goods and services.

The monetary authorities had the choice of adapting the economy's liquidity to the requirements deriving from higher incomes, including all or part of their price component in the shape of the cost-induced price rises, or of restricting credit to the amount necessary to finance production at constant prices, even if this meant that some firms might have to close down production.

To accept the responsibility of financing cost increases which were bound, at least in part, to spread to prices has involved us in exceedingly complex problems and difficult decisions. The central bank played its full part in taking and implementing these decisions. But we have no ground for complacency: while we succeeded in maintaining a high level of production, we did not succeed in the no less important objective of keeping prices stable.

Wholesale prices, which had remained remarkably stable until August 1961, subsequently displayed a pronounced upward tendency. At first the rise was confined mainly to agricultural prices, but more recently non-agricultural prices took the lead. The general level of retail prices rose by 6.5 per cent between the end of 1961 and the end of 1962, and in the early months of 1963 it climbed even faster owing to the exceptionally hard winter. Spreading beyond food, rents and services, the retail price rise eventually reached manufactured products, which had resisted longest.

If we go back over ten years to 1953, the statistics clearly outline the successive stages of the initial increase in productivity, the rise in profits and their use to finance new plant, which in turn raised productivity still further and was followed, finally, by rising wages. As we approach the most recent period, the pattern becomes more complicated and less easy to interpret, in so far as the wage rise sometimes fell short of the increase in productivity and sometimes exceeded it, with the result that profits fell, cost increases were passed on to prices, and more credit was needed for the same level of investment.

The very expectation of price rises, especially if it rests on a demand expansion manifestly incapable of being satisfied by a corresponding expansion of supply, induces employers to be generous in their wage concessions to workers.

In some cases wage increases originated in the private and subsequently spread to the public sector. In some cases it was the other way around, and the propagation of originally public wage rises to the private sector, much the largest employer of labour, occasionally diminished the competitive capacity of private firms to the point of impairing their ability to maintain the level of employment. Here again the time sequence is hard to establish. Nevertheless, we cannot evade the conclusion that if government-controlled agencies and companies neglect their duty of economically rational management and have easy access to credit, the very expansion of the area of public enterprise implies a danger of dual wage policies, which would be prejudicial to balanced development in the economy.

Cost-induced price rises can, of course, happen only to the extent that the monetary authorities increase the money supply to meet demand. This statement means that the causal chain leads from higher wages and prices to a larger money supply and not in the opposite direction. In other words, in the system of monetary equilibrium wages appear as an autonomous variable: if they rise ahead of average productivity and are not offset by falling profits, the wage increase spreads to prices if it is financed by a larger money supply. If higher wages are offset by lower profits, it may happen that the resulting new distribution of income depresses the level of investment.

This interpretation of the causal relationship between costs, prices, profits and money supply does not mean that, for our part, we take a passive view of the functions of monetary authorities in the sense that they must necessarily supply the economy with all the liquidity it demands. On the contrary, last year's events in many countries testify to a stiffening resistance on the part of monetary authorities against financing a cost-induced rise in prices.

As regards ourselves we did not think it right to apply restrictions, because in our judgement there were sufficient margins of manpower to combine with other factors of production, and increased imports of resources would absorb our balance-of-payments surplus. Our choice of the manner of our liquidity injections was dictated largely by its foreseeable effects.

In spite of the existing margins of elasticity in domestic supply, the latter proved unable in some cases, like building and foodstuffs, to meet growing demand. As regards food in particular, weather-conditioned crop failures caused some major items to be in such short supply that even the easing of imports could not make good the deficiency. This was another source of unusually large price rises which, although their causes were localized and transitory, were quickly propagated through the mechanism of sliding wage scales.

In some sectors the strain on prices was aggravated by the converging effects of domestic and foreign demand. A clear case in point was again food, where prices felt the impact of a redistribution of incomes not only at home but also abroad, as well as the repercussions of the European Economic Community's common agricultural policy.

To sum up, the monetary authorities fashioned their policy last year to two circumstances: first, the increase in labour costs per unit of product and the resulting rise in prices, and second, the balance of payments, which showed a surplus during the first and a deficit during the second half of the year, and on balance still a surplus for the whole year. In these circumstances the monetary authorities, while injecting liquidity into the economy, did not inject enough to finance the whole of the transfer of the cost increase to prices, leaving part of it to cut into profits. They did inject enough liquidity, though, to prevent stoppages of production in any sector, and incidentally so allowed domestic demand to expand in excess of domestic supply and thereby to mop up part of the current surplus in the balance of payments.

Now, in 1963, the monetary authorities find themselves in the presence of persisting price strains and of a balance of payments in deficit on current account, almost exclusively by reason of merchandise imports growing much faster than exports. It it not only that we see definite symptoms of our own products being less competitive on foreign markets, but foreign products are beginning to be more competitive at home. Our increased purchasing power makes us absorb imported goods more readily. With open lines of communication between the domestic and the foreign market, domestic liquidity flows out to international markets.

In addition, Italy was a capital exporter in 1962 and even more so this year. Capital movements constitute a part of our balance of payments which we cannot afford to overlook, and for this reason we have made special efforts to trace them as closely as possible by assembling all possible information and estimates on the transfer of Italian capital to foreign countries.

In all, the entire set of capital movements which have a bearing on the balance of payments produced a deficit of 152 billion lire in 1962, compared with a surplus of 43 billion in 1961.

The deficit was fully offset by surpluses on current account, so that we still had an overall surplus of 31 billion lire. But if we look just at the last quarter of 1962 and the first quarter of 1963, we find a current deficit of 125 and a capital deficit of 151 billion lire, so that we had an overall deficit of 276 billion in six months. This is a sharp deterioration in comparison with the corresponding quarters of 1961 and 1962, when the external accounts just about balanced.

On March 31, 1963, official reserves of gold and convertible currencies amounted to 3,326 million dollars; first-line reserves (official reserves plus the Bank of Italy's net foreign assets) together with second-line reserves (net position with the International Monetary Fund plus the counterpart of swaps with foreign central banks) amounted to 3,831 million dollars. Official reserves covered about seven months' worth of imports, and first- and second-line reserves about 8 months.

However, in appraising the adequacy of our official reserves we must think also of the level of domestic liquidity, which gives us the measure of the potential expansion of domestic demand. To the extent that it could not be satisfied by domestic supply, it might, of course, pull the balance of payments further into deficit. Higher domestic liquidity requires higher external liquidity, that is, more official reserves. At the end of 1962, the ratio of official reserves to primary liquidities was 21 per cent, as against 26 and 25 per cent at the end of 1960 and 1961, respectively. This fall in the ratio restricts the monetary authorities' freedom of action on the domestic and on the international plane alike, in the latter case with special reference to aid to developing countries.

Italy stepped up her contributions to developing countries from 239 million dollars in 1961 to 416 million last year. This corresponds to one per cent of gross national product and is more than enough in the light of the high domestic need for savings. We cannot do more in the absence of rational co-ordination of development aid, which seems to be as far off as ever, and in the absence of more multilateral methods of distribution and of closer controls over the use of these funds in the beneficiary countries. Some of the major industrial countries are wont to indulge in international comparisons to underline the relative size of their own contributions; but this can mean but little so long as development aid continues to go to the donor country's former colonial territories or to nations with which it has special political or economic ties.

We wish to stress that aid to developing countries is a responsibility of government and must be financed by budget appropriations; it is inadmissible to finance it by monetary resources even as a temporary stop-gap pending budgetary provision.

Let us consider now more particularly the short-run problems of international liquidity, which, in effect, boil down to defending the reserve currencies. Clearly, it is the duty of the countries responsible for reserve currencies to achieve as soon as possible a lasting equilibrium in their external payments and in the meantime to contain the deficit within limits compatible with the rest of the world's desire to hold such currencies. Equally clearly, other countries have a duty to conduct themselves as good creditors, though this obligation cannot possibly involve indefinite commitments. So long as Italy's balance of payments was in surplus, we fully lived up to our responsibilities by helping to build effective defences for the international monetary system within the framework of the International Monetary Fund, the European Monetary Agreement and bilateral agreements with the Federal Reserve System and the United States Treasury. Our actual or potential contributions on this score add up to something like one billion dollars or more.

The defences built up by international action are amply sufficient to finance the needs of reserve-currency countries in the near future. There is no urgency at all to strengthen these defences, at any rate until they have been tested; what we do need to do urgently is to make them more efficient by working out, amongst ourselves in the European Economic Community and in the wider group of industrial countries generally, a common policy with respect to the composition and management of reserves.

Our country, then, has not been laggard in helping to solve the problem of short-run international liquidity. If anything more should be required of us in this line, we consider that the only possible form would be an increase in our I.M.F. quota. Simple comparison with other major industrial countries indeed makes it quite clear that our quota is altogether too low in relation not only to our country's economic importance, but also to its commitments to furnish supplementary resources. What is more, an increase in our quota appears indispensable in order to replenish the Fund's lire resources, which are now down to working balances. Finally, given the present deficit in our balance of payments, recourse to the International Monetary Fund is not to be excluded, and the amount of possible drawings depends, of course, on the quota.

The Control of Liquidity and its Internal Distribution.— The Treasury and the Bank of Italy last year created liquidity in an amount of 591 billion lire. These financed a liquidity increase in the economy of 390 billion lire in bank notes and coin, net of the cash holdings of the issuing agencies and commercial banks; of the rest 171 billion went to finance the increase in the compulsory reserves of banks and the residual 30 billion represent the change in bank liquidity.

The liquidity injection to the banking system had its counterpart in an increase in the public's liquidity, in the form both of bank deposits and of bank notes and coin. As is well known, the process of credit creation which leads to the growth of bank deposits can go on so long as the banking system has enough liquid resources to effect its payments into the compulsory reserve accounts and to keep in hand whatever is judged necessary for the proper conduct of business.

The expansion of bank credits and other investments, and the corresponding growth of deposits, last year required about 397 billion lire to be paid by the banks into the compulsory reserve accounts. The reduction of the reserve ratio with respect to existing reserves provided 226 billion of this total, while the rest was borrowed from the Bank of Italy. Ultimately, as mentioned before, the effect was to raise bank liquidity by 30 billion lire.

The Treasury's transactions with the Bank of Italy and the market, the Bank of Italy's dealings in government securities, and the operations of agencies which act on behalf of the Treasury—that is, accept deposits which are then paid into the Treasury's accounts with the Bank of Italy—have all been combined with each other and with the central bank's other operations in such a manner that their total liquidity effect should be in line with our policy intentions.

Obviously, the chances of arriving at appropriate combinations of the various cash operations of the Treasury depend on the size of the budget surplus or deficit. Unless the orders of magnitude involved are compatible with the requirements of liquidity control, it is difficult to make the whole set of the Treasury's cash operations fit flexibly into the tactics of monetary policy.

So far, the flow of budgetary revenue and expenditure has always been such that it was possible to finance the Treasury's cash deficit by operations which, combined with those of the autonomous agencies, did not exceed the limits within which the economy's liquidity could be made to match the intentions of the monetary authorities. It is not unlikely, however, that the Treasury's cash deficit may grow, and if it does, we may find it more difficult, or indeed impossible, to manoeuver in this way. We would then have to reconsider the whole problem of the size of the deficit and of the type of securities by which to finance it, and we may well find it necessary to cover the deficit by government bond issues.

The composition of the public debt was rather different in 1962 from the year before, as a result of the greater use of methods of finance which create bank liquidity. The proportion of long-term debts fell from 32 to 29 per cent, and the proportion of short-term debts to the Bank of Italy rose from 13 to 16 per cent. The share of Treasury Bills declined, and that of Post Office savings rose, but the investment of these savings by the Central Post Office Savings Fund kept the latter's position neutral.

The new system of issuing Treasury Bills by monthly tender in amounts adjusted to the Treasury's cash needs has proved satisfactory. The Treasury fixed its issues so as to reabsorb almost the whole of its credit balance in current account with the Bank of Italy. This was the correct procedure: if due proportions are maintained among the Treasury's cash operations and as between them and the Treasury's cash needs, the effect should be to keep the balance of the Treasury's current account with the Bank of Italy near zero. A credit balance covered by outstanding Treasury Bills means that the Treasury has to pay more interest charges.

Difficulties may arise in case the Treasury's cash needs require Treasury Bill issues in excess of the banking system's capacity to absorb them. We are fully aware that this is a matter subject to our own influence: we can always, by injecting liquidity into the banking system, raise its capacity to absorb Treasury Bills enough to take care of the proposed issue. But if ever Treasury Bill issues could be placed only at the cost of liquidity creation beyond the economy's needs at stable prices, this would be the clearest possible indication of inflationary budget financing.

In case Treasury Bill issues need to be in excess of the baning system's capacity of absorption at a given level of liquidity, and assuming that the monetary authorities have correctly determined that level and are, therefore, reluctant to raise it, the central bank has discretion to purchase, or not, the portion of the monthly quota which the market has not taken up. If the central bank does not purchase and part of the issue of Treasury Bills, therefore, remains unallocated, the Treasury will be forced to draw on its current account and so to make it plain that its needs are financed by monetary means. This will not happen if, by co-operation between the Treasury and the central bank, the Treasury's needs are at once financed by the issue of government bonds.

But then the government competes with industry for investable funds and we have a problem in terms of real resources. We shall have to decide whether the government's budgetary cash needs are, or are not, compatible with the realization of all the other public and private investment programmes which draw their funds from the capital market.

Such a conflict between the financial requirements of the Treasury and those of production did, in fact, arise for the industrial credit institutes. The Treasury's indirect claims on the market through these special credit institutes—in the case, for instance, of the Green Plan for the improvement of agriculture—has the tendential effect of increasing the proportion of these institutes' loans to the Treasury in their total loans. Seeing that the amount of investable funds on the market is fairly rigid and that the share of them which the industrial credit institutes can hope to obtain by their bond issues is not greatly expandable, it would seem evident that if the Treasury attracts larger funds through the special credit institutes, production gets less.

On balance of the economy's foreign operations, the Bank of Italy and the Italian Exchange Office last year bought 308 billion lire's worth more foreign exchange than they sold. In 1961, the foreign sector's liquidity creation had stemmed almost exclusively from the balance-of-payment surplus, the Bank and the Exchange Office having financed a corresponding excess of foreign exchange purchases over sales; in 1962, by contrast, 269 of the 308 billion lire excess for which the Bank created liquidity went to finance foreign borrowing by the banking system. Having been authorized in October again to build up net debit positions abroad, Italian banks raised altogether 320 billion lire's worth of liquid resources abroad in the months of November and December.

This reopening of the connections between the domestic and foreign money market takes its place in a whole set of provisions which I have more than once had occasion to discuss. In the present context I would merely point out that the creation of an Italian money market in which fixed quantities of Treasury Bills are made available at variable prices was bound to produce, and indeed after some initial adjusting movements immediately after the reorganization did produce, a succession of inflows and outflows of foreign exchange. Banks began to administer their lire and foreign exchange cash holdings as one single unit. Whether at any moment they prefer Italian or foreign Treasury Bills or other international money market securities depends, among other things, on comparative money rates in different markets.

Some doubts have been expressed as to the wisdom of our reestablishing the connection between the domestic and foreign market, in so far as this removes from our control one of the components of domestic liquidity. I would reply that the remedy may lie in the mechanism of variable interest rates which we have recently created. If need be, we could, of course, always separate the markets again, but we should be loath to do that, because I think we should learn to control domestic liquidity without having to interrupt the process of the integration of the Italian into the international economy. We might, however, regulate the conditions of foreign borrowing by the banks, just as we have regulated their reciprocal relations at home.

Thanks to the liquidity injections by the Bank of Italy and the Italian Exchange Office, the banking system was able to expand its domestic lending and security investment more than the year before and so contributed to a corresponding growth of the public's liquid resources. Last year's increment of loans to the domestic market, in the amount of 1,835 billion lire—compared with 1,391 billion in 1961—came almost entirely from the banks; adding foreign lending and loans to the public sector, short-term credit expanded by a total of 2,014 billion lire. As against that, gross liquid assets rose by 2,712 billion; the surplus of gross liquid assets over credits to the domestic market grew by 877 billion lire, mostly by liquid asset formation corresponding to security investments, which channelled liquid funds towards the capital market and so made good the public's reluctance to take up the whole of the supply of security issues. The increment of the surplus of gross liquid assets over domestic credits, that is, of the public's net liquid assets, was rather unevenly distributed: large companies lost a lot of liquidity, medium and small companies gained. A new survey conducted by the Bank of Italy last year and covering 80 per cent of all liquid assets, reveals that the net liquid assets of large companies contracted by 440 billion lire and those of other companies and private individuals increased by 690 billion.

Anxious to improve our knowledge of monetary flows, we made a survey of 500 major agencies and companies with annual sales presumably in excess of 1,500 million lire, or, in the absence of information about sales, possessing plant of such value as might be considered to correspond to sales of that order of magnitude. Government-controlled agencies and companies were included regardless of the value of their sales. Now, the amount of external finance used by this group of companies was 779 billion lire in 1961 and 1,329 billion in 1962, of which 663 billion went to government-controlled and 666 billion to major private companies. The disparity between the two years' figures shows up the consequences of diminished self-financing capacity in the presence of rather large investment programmes. The branches in which net indebtedness increased most in 1962 were chemicals, mineral oils and electric power.

This conspicuous increase in the need for outside funds coincided with profound changes in their sources: in 1961 the banking system furnished 19 per cent of outside resources, in 1962 33 per cent.

The net bank debts of government-controlled agencies and companies rose from 524 billion lire in 1961 to 719 billion in 1962, those of the major private companies from 257 to 502 billion lire.

Classification of these figures by categories of economic activity enables us to make the following statements.

(1) The reasons for last year's increase in the net bank debts of the major private companies were the difficulty of placing security issues on the market, the diminution of self-financing and the debt repayments of subsidiary electricity companies to their mother company. The sectors in which the phenomenon assumed far and away the largest proportions were electric power and chemicals; in the latter case, such security issues as were floated were not enough to finance plant construction in

progress. Two thirds of the increase in the net indebtedness of major private companies were concentrated in these two sectors. There can be no doubt that E.N.E.L., the new government corporation which, in taking over the nationalized electricity companies has inherited their bank debts, must fund these as soon as market conditions allow.

(2) Among government-controlled industry, the largest increase in bank credits occurred in the hydrocarbon sector, which was carrying out previously established investment programmes.

(3) The exceptional increase in the indebtedness of both private and government-controlled companies was not fully matched by an increase in the value of fixed investment and working capital. The difference was used to finance export credits, only part of which could rely on industrial credit institutes; of 269 billion lire of export credits outstanding on December 31, 1962, special credit institutes had financed only 110 billion. The rest of the difference was employed by holding companies to purchase shares of their subsidiaries: the public's increased liquidity preference helped to expand bank credit to the large holding companies which, in their turn, transferred the proceeds through stock exchange transactions to minority shareholders desiring to sell.

Certain conclusions can also be drawn from an examination of the structure—and the last two years' changes in the structure—of industry's indebtedness to the banks, according as the companies concerned are large or medium- and small-sized and belong to the public or the private sector.

(*a*) The ratio of net bank debts to the value of sales is higher in the case of government-controlled than of private companies. Although the latters' net indebtedness almost doubled in the course of last year, they still depend only marginally on bank credit, and some firms, for instance in the engineering sector, continued last year to maintain a net credit position vis-à-vis the banks.

(*b*) The net bank debts of government-controlled agencies and companies have, in some cases, assumed such dimensions as to warrant closer scrutiny. In the mineral oil sector alone the relevant figure increased by 35 per cent last year. Adding to this the credits extended directly or indirectly by special credit institutes to finance exports against deferred payment, we cannot escape the conclusion that this huge indebtedness makes it necessary to co-ordinate this sector's investment programmes with those of other sectors.

(*c*) Government-controlled agencies and companies borrow mostly from public-law credit institutes and banks of national interest, but last year by far the most conspicuous increase took place in credits from commercial banks and people's co-operative banks; in terms of net indebtedness, the year's increases were 113 and 64 per cent, respectively.

All categories of banking firms which make up the banking system as a whole mistakenly tend to equate credits to government-controlled firms with credits to government itself from the point of view of risk evaluation, and banking firms with a private-enterprise structure seem to be more prone than others to this belief. The ease of access to bank credit seems to have played its part in inducing some government-controlled agencies and companies to rely on bank credit more than is right from the point of view of proper balance among various sources of finance, so much so that the problem has engaged the attention of the Joint Ministerial Committee for Credit.

Extending our examination to industrial credit institutes, we may say that the distribution of their outstanding loans seems satisfactory. Given that these institutes lend mostly to finance new plant, the distribution of their operations among the various sectors of the economic system is obviously a determinant of the latter's structure.

If the government wishes, as a matter of policy, to strengthen medium and small firms, it stands to reason that these categories must be given more credit; but that means giving less credit to other firms and to the public sector, and adapting interest subsidies to the sums that can effectively be made available to such firms, without raising expectations which might have to be disappointed.

Of all the credits extended by industrial credit institutes, the share of credit to medium and small enterprise was 29 per cent in 1960 and 35 per cent in 1962; correspondingly, the share of large private companies fell from 23 to 19 per cent and that of the public sector from 38 to 36 per cent. The average credit expansion in 1962 was 26 per cent, and credits to medium and small enterprise expanded by 33 per cent.

While industrial credit institutes raised their credit to medium and small enterprise relatively more, the growing pressure of demand led banks to do the opposite. Savings banks, finally, reduced their credits to public corporations to make room for an exceptional increase of 83 per cent in credits to major private companies. Since these credits are usually unsecured, they need, in most cases, an authorization by the Bank of Italy and, given the conditions of the capital market last year, such authorizations were not withheld.

In spite of the last two years' changes in the distribution of bank credits among various categories of borrowers, it still remains true that the great bulk of bank credits goes to sectors comprising innumerable small and very small firms. This is especially true of people's co-operative and commercial banks, although the latter, as we have seen, did not remain unresponsive to the appeal of government-controlled agencies and companies, to which they lent an extra 67 billion lire in 1961 and 121 bilion in 1962. Nevertheless, the commercial banks' credits outstanding with small and medium firms, in the amount of 1,878 billion lire at the end of 1962, exceed those of any category of banks.

There is much talk at times about the influence the banking system has in fostering this or that kind of productive activity, as if the banking system handled merely the surplus of personal savings and not also the funds deposited by the self-same producers who make use of bank credit. A correct measurement of the effects of the banking system's activities can only be based on intersectoral monetary flows, and these, in turn, can be calculated only with reference to the changes in each sector's net debit and credit position. The trouble is that, while this sort of calculation can be carried out for big firms, it becomes rather difficult for medium and small firms, where the entrepreneur as head of the firm can hardly be distinguished from the entrepreneur as head of the family. In cases of this kind debit and credit positions seem to alternate much more frequently.

Another difficulty is that these firms often borrow from and lend to each other, so that it is hard to identify with precision the ultimate destination of the funds that a bank makes available to any particular firm.

In collectivist economies all firms, of whatever form, are strictly forbidden to borrow from any other or lend to any other firm. All payments and all receipts go through the central bank, with which each firm has its own account, and wages may be paid out in bank notes. In these circumstances the central bank keeps account of and can measure all monetary flows from one sector to another, and on this basis checks whether the plan is being carried out according to its pre-established time schedule. Credit is regarded as the instrument by which money assets are redirected from sectors temporarily in surplus to others temporarily in deficit, but it plays no part whatever in determining the direction of investment, which is financed exclusively by public saving on the part of public administration.

Notwithstanding the profound differences between our economic order and that of collectivist countries, in both cases the moment at which the purpose of an investment is decided is when the funds specifically destined for it are made available. In our economy, that is the moment when a security issue is floated or when an industrial credit institute grants a loan. Exceptionally, at times when the banking system finds itself obliged to extend its operations into the field of competence of industrial credit institutes, the banks do have some influence, but only within the limits of such investment credits as they grant. The fundamental functions of the banking system always remain, on the one hand, to create a money supply and, on the other hand, to act as intermediaries in shifting liquidities from surplus to deficit sectors, for use as working capital. In the first of these function the banking system is the channel through which the monetary authorities regulate the level of money supply in the economy.

Collaboration between firms and the authorities responsible for authorizing security issues, between these authorities and special credit institutes, and between the latter and the credit control authorities, is quite sufficiently developed to enable investment to be co-ordinated without impairing the entrepreneur's freedom of decision. Companies, and especially the larger companies, are used by now to furnish all the information necessary to discuss their long-term investment programmes and the authorization for any security issue is set within an overall finance plan approved by the credit control authorities on the basis of adequate knowledge about the various internal and external sources of finance. The credit control authorities try to balance the various sources of finance, but in 1962 it proved impossible to do so, given that the need was so great that we had to condone recourse to bank credit beyond the desirable limits.

Among the measures which influence investment special mention must be made of privileged credits, credits, that is, which are eligible for interest subsidies on the basis of case-by-case decisions by government departments. By granting or not granting the subsidy, the government can exercise a selective influence on new investment. The importance of this can be measured by the fact that of all the credits industrial credit institutes had outstanding at the end of last year about one third was privileged, and the proportion is even higher if we take only the new credits extended in 1962.

With more co-ordination in the government's regional industrialization policy we would most probably find we need to overhaul the present incentives system so as to fit all separate measures organically into one comprehensive system of unitary conception. Indeed, there might be a lot to be said for departing altogether from the present system which rests so largely on credit incentives. But whatever solution may be adopted, the decisions which determine the direction of industrial development in any particular area will always be incumbent upon government; given these decisions, it will be up to the banks to exercise their own judgement as to whether the companies requesting credits are capable of repaying them within the agreed time.

The credit control authorities' influence on investment has become somewhat more important through the regulation of the activities of industrial credit institutes and their co-ordination with the security issues floated directly by companies. The directives to be followed have been more closely defined in geographical and sectoral terms, but within these directives the institutes remain free to conduct their credit business according to their own judgement. Geographically speaking, the results would appear satisfactory. The distribution of new loans granted to industry by industrial credit institutes last year was as follows: 47 per cent to southern regions and the islands, 41 per cent to north-western regions, and the rest to north-eastern and central regions. Southern regions and the islands received 52 per cent more credit than the year before, and north-western regions 30 per cent more; in 1961 the corresponding increases had been 27 and 28 per cent. In other words, credits to southern industry expanded about twice as fast last years as in 1961.

In their turn, credits to the sector of public services expanded much faster in southern Italy and the island than elsewhere in the country; the increase was 24 per cent as against a national average of 18 per cent.

As regards the distribution of the industrial credit institutes' loans by sectors of economic activity, the figures clearly reflect the intentions of the control authorities. We find a strong concentration in public services, and especially electric power, where companies had to carry on with work on plant already in construction, but could not raise funds directly on the market. Large funds were channelled to telephone companies, which had to rely on credit, because failure to revise the tariff schedules narrowed their self-financing margins, and to shipping companies, for the shipbuilding programme concerning lines of national interest. Other sectors to which industrial credit institutes extended far more loans than before include engineering, iron and steel, chemicals, and, to a lesser but still considerable extent, textiles (where intensive modernization schemes are under way to offset the big increase in labour cost per unit of product) and the food processing industry, which is building new factories largely within the framework of the Mezzogiorno development plan.

The geographical distribution of mortgage loans on urban property extended by land and building credit institutes likewise shows some changes that are worth mentioning. The credit expansion in southern Italy and the islands was far in excess last year of that in central and northern Italy, and the peak points were Sardinia, Calabria, Apulia and the Abruzzi. As before, the strongest concentration of mortgage loans was in Latium and Lombardy, which accounted, respectively, for 26 and 28 per cent of all new mortgage loans last year; the reason for this marked concentration is, of course, the presence of the cities of Rome and Milan in those regions.

Although land credits extended last year were far in excess of those granted in 1961, there is a widespread belief that they diminished. This belief clearly stems from the fact that so many more credits are requested than granted. On December 31, 1962, the land credit institutes had credit applications for 347 billion lire under examination, had passed on applications for 240 billion with a favourable opinion, and had made conditional contracts for 264 billion. These figures make it quite clear that if all applications were to be granted, they would make heavy inroads into the claims of other productive activities.

It is, perhaps, not strictly speaking our business to analyse and express an opinion on the growing social cost of the lack of rational town-planning. But this social cost now begins to be reflected in the costs firms have to bear in the shape of higher wages, fewer working hours and lower working efficiency. I would consider it as my duty, therefore, to point out that the local inflation of property values, which is especially characteristic of large cities, is a matter that gives rise to some preoccupation, both because of its effect on the distribution of wealth and of its partly psychological repercussions on monetary equilibrium. However, in the absence of at least an outline of town-planning principles, the authorities responsible for credit control can hardly forestall by their own decision a future depending on choices yet to be made.

The industrial and land credit institutes' need for resources has increased beyond the capital market's supply, with the result that only 24 per cent of their bond issues were taken up by the public last year, as against 59 per cent in 1961. Banks and banking associations furnished the special credit institutes with 520 billion lire of new resources, which amount to 49 per cent of the total, and in the third quarter of last year alone the proportion was 56 per cent.

The Structure of Interest Rates. The monetary authorities have given much thought to the question of how to promote, within the limits of their powers, the creation of a structure of interest rates susceptible of generating a distribution of the public's liquid assets more in line with the use to which the investable funds are put. There is no need for me to recall here what measures we have taken; they have been discussed with many of you beforehand and you have loyally co-operated in their implementation. I shall limit myself, therefore, to explaining the motives behind these measures and the methods of their application.

In the determination of the structure of interest rates, considerations relating to the public's liquidity preference cannot be separated from those relating to the liquidity of the various investments financed by cash resources. This latter is subject to the influence of long-run factors, the foremost of which is the process of development in our economy which affects all sections of the market, including the capital market.

In the economically and financially most advanced countries the evolution of the money and capital markets and the related growing importance of financial intermediaries have had the effect of making capital assets more liquid. The creation of a number of categories of securities, which as such are more readily negotiable than the real goods (buildings, plant, equipment, etc.) they represent, was accompanied by a continuous improvement of the negotiability of these securities, to the point of making money market paper interchangeable with the capital market's securities which are the counterpart of long-term investment.

The tendency of advanced societies to invest larger portions of capital in easily negotiable and increasingly liquid securities raises new problems for monetary policy. The boundary between liquid and non-liquid assets becomes blurred. The spectrum of liquidities is assuming more and more importance in response to the growing need to offer savers a wide choice, and conversely changes in the public's liquidity preference generate changes in the price of securities which, while easily negotiable, are not entirely liquid. Given that securities nowadays represent a growing share of national wealth, their price fluctuations may assume disturbing dimensions. It follows that we need an interest policy which helps to contain the amplitude of stock price fluctuations.

An analysis of the compound structure of short and long rates clarifies the tendency of the cross-currents between them by showing up, for instance, that short rates tend to vary more and are normally lower than long rates; but beyond that, such an analysis also points to the need to adjust the structure of rates of interest to the changing equilibrium conditions of the market.

In attempting to create a system of interest rates in line with specific purposes of monetary policy we had no intention whatever to perpetuate any particular level of rates, nor had we any preconceived ideas about their structure. On the contrary, we thought it right to proceed empirically and to learn from experience.

Our empirical methods can be summarized as follows:

a) The determination of short-term deposit rates, which fluctuate more sharply than long rates, is left to the judgement of the banks. With this attitude the monetary authorities wish to make it clear that they do not consider themselves, at present, to be possessed of sufficient knowledge to replace the market by their own rules. They prefer to rely on the experience of the banks, in the conviction that immediate everyday contact with the market is a better guide than the views of any centralized administration. The monetary authorities do ascertain, however, whether the rates of interest fixed by the banks are in line with the purposes of monetary policy. To the extent that the bankers have agreed on any particular structure of interest rates which appears to us to answer the above purpose, we would ask them to respect it and, when they judge it to be overtaken by events, to propose its modification.

b) As regards medium- and long-term funds, the rates of interest, which are less subject to fluctuations, are determined by the direct intervention of the monetary authorities, especially in the case of bond issues. The rate of interest and all the other conditions which determine effective bond yields are agreed in each separate case with the Bank of Italy in the light, naturally, of the present and prospective conditions of the capital market and the money market.

c) The structure of interest rates which is the result of the rates established by the current interbank agreement and those established by the monetary authorities on the occasion of their authorization for a security issue seems, at the moment, to answer the need of promoting a distribution of the public's investable funds between bank deposits and security investment such as to give the monetary authorities adequate scope for liquidity control.

It depends, of course, on the conduct of the monetary authorities, and, in particular, on the liquidity creation of the Treasury and the Bank of Italy, whether and how much bank deposits can grow. The banks are obliged to maintain certain proportions between the public's deposits and their own tied deposits in compulsory reserve accounts, and for this reason the banks are not free to determine the volume of credit and thereby the amount of money supply which is its counterpart. However, when the banks raise their deposit rates, and consequently stimulate the public's preference for keeping a larger portion of funds in liquid form, they do generate an equidirectional short-term movement of bond yields, which means that bond prices fall. This may force the monetary authorities to intervene directly or indirectly to support bond prices, not least in order to make sure that the Treasury can raise finance at acceptable conditions. In this manner the monetary authorities may be led to create liquidity beyond the limits they judge desirable. It follows that effective liquidity control cannot do without interventions designed to maintain a balanced structure of interest rates.

When I say a balanced structure of interest rates I mean that it must answer two purposes: it must prevent short-term deposit rates from rising to such an extent that they pull up the long rates, and it must prevent them from falling below certain levels, which would simply divert part of the liquid resources from the banking system to other forms of investment less susceptible to control by the monetary authorities.

Compliance with the interest rates making up the structure approved by the monetary authorities in no way displaces the banks from their position as the link between the central bank and the capital market. Ever since government securities, not only of short but of long maturity, and securities of government corporations began to enter the banks' portfolios in far from negligible quantities, this connecting function has become established practice even in the countries which were the cradle of orthodox banking. But this function would cease to be discharged in the public interest if the banks, contrary to the rules which govern a given structure of interest rates, were to invade the territory of special credit institutes by attracting funds which, otherwise, would have gone to these institutes in the form of bond subscriptions.

If banks attract to themselves monetary assets which should have spread throughout the productive system through many other channels, and if they make it a habit to finance the formation of new fixed assets especially on the part of large firms, then we may have to introduce adequate controls. This view of ours has found expression in the provision by which the Joint Credit Committee gave power to the Bank of Italy to require specific banks, or groups of banks, to set aside special liquidity reserves whenever we should become aware of distortions in the distribution of the public's saving.

I need hardly mention, surely, that the normal functioning of the capital market depends on other conditions as well.

In particular, the public will buy bonds only on condition that it believes the purchasing power of money will be maintained. In addition, government policy must be such as to offer reasonable assurance that no measures will be taken which would lead to sudden changes in the qualitative composition of the securities traded on the market, where a large increase in the supply of certain stocks might depress their prices.

A case in point is the manner in which the nationalization of the electricity industry was carried through in Italy. Great care was taken to minimize the effect on the stock market of a sudden qualitative change in so large a proportion of equities. The companies which owned the electricity firms were left in existence and they will be paid compensation in ten annual instalments, which can be discounted by special credit institutes in case some company wished to make productive investment sooner. This solution has not, of course, relieved the market of all the repercussions of so profound a change in the content of electricity shares, but the effects were much less serious than they would have been if the compensation had been paid at once in the form of bonds.

The modalities of the nationalization of the electricity industry have been widely and fully discussed. In the present context I would merely state that they were inspired by the need not to allow the monetary authorities to lose control over the market. The payment of compensation in ten annual instalments makes it possible to raise the necessary funds on the market without seriously disturbing its equilibrium. Even if the companies entitled to compensation payments speed up the latters' conversion into liquid form by discounting them with special credit institutes, this would not prevent the monetary authorities from confining such operations within the limits compatible with market equilibrium; furthermore, E.N.E.L.'s powers to issue bonds against subscription in electricity shares enable shareholders to convert equity into bonds without depriving the monetary authorities of their ability to regulate the supply of bonds.

As regards the possibility of index loans I would point out that these have already been tried in some countries without success. Even apart from these unsatisfactory experiences, however, I would mention the following drawbacks.

a) An index expressed in terms of output, product prices, gross receipts, profit margins, and such like, can be applied only to bonds issued by companies which produce an identifiable good, but hardly to bonds issued to finance such public investment as cannot be covered by budget surpluses. Does anyone really believe in the viability of a financial policy resting on the co-existence of two categories of bonds in the same market? Would this not simply mean increasing the cost of funds raised by non-index loans?

b) One of the consequences of such a system might be that an index is applied also to the bonds of government or quasi-government corporations whose activity is such that they cannot assume output and prices as parameters. The index could then be expressed only in terms of the general price level or other measures of the purchasing power of money. In that case the same solution would surely have to be extended also to government stock. Would this really widen the market, or would it not rather increase the cost of the enormous amounts which the government must raise somehow, directly or indirectly?

For the rest, it is our conviction that the public should be offered a greater variety of securities and that, if need be, we should create new types to meet the public's preferences. For this reason we have revised our previous views about convertible bonds and have authorized a convertible loan stock to be issued by *Finsider*. This holding company had entered the market in support of its subsidiaries' equity, and by limiting the price fluctuations of steel shares had contributed to the stability of the market as a whole. By the convertible bond issue the company is now to obtain from the market the funds laid out in advance for the purchase of shares and for financing current investment programmes. The public will be offered a stock which throws a bridge from the present to the future, when investors may well prefer equities.

To sum up, the capital market is one integrated system; the more it is improved, the more interdependence will there be among its various sections. When the customary self-financing capacity of firms is curtailed for transitory or lasting reasons, companies become more dependent upon the capital market, and unless the latter can supply what they need, they may have to borrow from the banks. But this cannot go on indefinitely without peril to the preservation of a credit base compatible with monetary stability.

The Problems of the Immediate Future.— If I have dwelt so much upon short-term problems, it was because I believe that they are the ones which must above all engage the attention of the central bank. Some of them are urgent. Unless we at once adopt energetic measures to solve them, we shall be in no position even to think of long-term policies. The forces which combine to push up prices, the deficit in our balance of payments, the pressure on the capital market of convergent public and private demand for funds to finance domestic and foreign investment as well as exports against deferred payment—all these are urgent problems to which we must attend in the immediate future.

This Report explains the reasons which have generated a price rise often in excess of that in other major industrial countries. There are many reasons and we must guard against any partial interpretation of the phenomenon; the very variety of causes might confuse our view of the events of the recent past and prevent us from disentangling the causes and their interconnections so as to find those to which to attribute most weight. I regard it as my duty to repeat that the principal cause of the price rise was, and still is, the increase in wage levels in excess of the increase in average productivity in the economy as a whole.

The problem of the relationship between productivity, wages, costs and prices requires solutions concerned with the long no less than with the short period. National income cannot rise at a rate corresponding to the target of our economic policy, nor can it be distributed between investment and consumption in proportions such as to eliminate existing imbalances, unless we accept the fact that private consumption must grow less fast than real national income. This means we must create more capital, and especially more social overhead capital yielding no immediate returns.

I have said earlier that the cost increases have not been entirely passed on to prices, but that part of them were absorbed by profits. The problem now is to get going a process of readjustment between costs and prices on the basis of a new equilibrium which safeguards the international competitive strength of our economy. But it has to be underlined that the effect of wages rising faster than average productivity in the economy as a whole cannot be offset by price movements in the presence of a general mechanism of sliding wages. There are, in the productive process, latent forces which push up the price level. It is our duty not to add to them.

The redistribution of income last year was associated with a lower propensity to save. In 1961 national income at current prices rose by 10.5 per cent and gross capital formation by 15.3 per cent; in 1962 national income at current prices rose by 12.2 per cent and gross capital formation by only 10.3 per cent. In terms of constant prices the slow-down in the rate of increase in real saving was even more pronounced, given the relatively bigger price rise in 1962 compared with 1961.

Although the redistribution of income deprived firms of profits which might otherwise have been used for new investment, this does not necessarily imply a diminution of the total supply of saving. It may imply less voluntary saving and, therefore, a need to make good the deficiency by more public saving. If this should be held to be impossible, the policy of income redistribution must stop at the limits drawn by its effects on the provision of finance for investment. To transgress this limit means endangering the balance of payments. In 1962, an increase of 10.3 per cent in gross formation of saving was accompanied by an increase of 13.4 per cent in gross saving destined for domestic uses, the difference being furnished by drawing down the balance-of payments surplus on current account.

Experience suggests that the relation which exists in our economy between personal saving and self-financing by firms cannot easily be modified in the short run. This is confirmed by the time sequence of an initial rise in wage costs followed by a rise in retail prices. While the rise in retail prices tends to reabsorb the increased purchasing power of distributed incomes and so to limit their allocation to saving, the same price rise also tends to reconstitute the self-financing margins of firms.

If the monetary authorities restrict the money supply they impede this process of readjustment, and the deficiency of domestic saving is then balanced by a reduction of investment, which depresses the level of employment.

Having learnt from experience, the governments of all major industrial countries have now formally accepted the need for an incomes policy as the only way out of the intolerable dilemma between unemployment and inflation.

The reasons which impose an incomes policy also define its scope and field of application. Without necessarily aiming at a limitation of real consumption, incomes policy is generally so conceived as to regulate cost and price movements in such a manner that incomes grow in an orderly and socially acceptable fashion; it should leave room for such differentials as may be necessary in order to preserve to wages their fuction of determining the distribution of manpower, and in order not to petrify any given economic structure. It is also common ground that incomes policy must apply with substantially equal principles both to those incomes which are determined by bilateral negotiations and which account for the bulk of gross national product, and to those which are determined indirectly by market prices.

Incidentally, the interdependence between a certain distribution of incomes, a certain level of investment and the maintenance of incentives for rational production through the most efficient combination of factors of production, is at present the subject of critical reappraisal also among the planners of collectivist economies.

If countries with such profoundly different economic orders both feel a need to adjust the distribution of incomes to the requirements of economic growth, this may be taken as proof of overriding importance. Least of all may such an incomes policy be neglected in a country like ours, where voluntary saving is the mainstay of investment. Voluntary saving may be supplemented by a contractual saving, but even then the latter's amount cannot be determined coercively in our economic order. The link between the distribution of income and the amount of saving confirms the need for an incomes policy, which, of course, must be comprehensive, in so far as one could not imagine it to apply to some incomes and not to others.

The monetary authorities have the task of matching investment with disposable saving. To this end they have to set up and maintain a capital market through which saving is channelled to investment at the best conditions. The monetary authorities have the task of preventing investment from being financed by liquidity creation such as would cause aggregate demand to expand beyond potential supply, in cases when the excess of demand is more than can be met by reabsorbing the balance-of-payments surplus or by digging into reserves more deeply than is judged right to finance cyclical fluctuations without prejudice to the external stability of the currency.

If all the public and private investment programmes known to us were to be carried out, they would, in 1963, require special credit institutes, public agencies and private companies to issue bonds, net of repayments, and shares in an amount which we estimate to be well in excess of 2,000 billion lire. Special credit institutes would be responsible for the major part of these, given that they would be called upon to lend out something like 1,600 billion lire, most of which they would have to raise on bond issues. Of this total, 900 billion lire would represent loans on behalf of the Treasury or to meet credit demand stimulated by interest contributions by the Treasury.

Nor do these estimated 2,000 billion lire include direct Treasury issues, such as might well become necessary, especially if the cash deficit should grow. In any event, if expenditures which properly pertain to government are financed without revealing their entire amount when the budget estimates are submitted to Parliament, it is much harder to assess the effective needs of public finance.

The rate of increase in industrial investment was not matched, in 1962, by an equivalent rate of increase in self-financing, and this, as I have had occasion to repeat more than once, has forced companies to look for more outside finance; in so doing, they came up against a deficiency in the supply of saving. Larger portions of personal saving were kept away from the stock market to be used instead for the construction of dwellings, and the very composition of personal wealth changed to the detriment of the relative share previously invested in securities. Hence the growing demand for capital, including funds needed for public investment, failed to find an adequate supply on the market and the resulting strain was overcome only thanks to a whole set of interventions on the part of the monetary authorities.

The net proceeds of total security issues last year were 1,642 billion lire. The public took up only 857 billion, and the rest was subscribed by banks and banking associations as well as by agencies whose cash resources go to the Treasury—in other words, money supply was created to take up the securities. The banks were enabled to step in because the central bank raised their liquidity and thereby ultimately the liquidity of the public.

We could do this in 1962 because the resulting larger demand of the public, while not matched by an equivalent expansion of domestic supply, could be met by imports which reabsorbed our balance-of-payments surplus. In 1963 the situation is no longer the same. Our balance of payments is heavily in deficit, and we cannot afford to expand liquidity any further to make room for security issues. Inescapably, all the expenditures which have to be financed on the capital market, whether they are expenditures by government, local authorities, public corporations, other public bodies or private companies, will have to be subjected to a critical reappraisal and will have to be co-ordinated. If total requirements exceed disposable saving, less urgent expenditure will have to be postponed. The task will be eased if priorities are established according to a general plan.

Faced with last year's cost increases which, even though part of them were absorbed by profits, unavoidably also spread to prices, the central bank regarded it as its duty to inject sufficient liquidity into the system to finance production at rising prices, so as not to endanger the continuity of growth. We acted under no compulsion and accept full responsibility for what we did. But we would not be doing our duty as a central bank if we failed to give notice that in the present conditions of our balance of payments we cannot go on creating liquidity generating an excess of demand over domestic supply, in order to satisfy the flow of unco-ordinated public and private investment demand which reaches the capital market in excess of the foreseeable supply of saving. If we did, we would risk an external deficit of such dimensions as to be incompatible with the maintenance of the currency reserves which, as a country so strongly dependent on international trade, we must have.

In that case, the situation which, while difficult enough, still is, and can be, kept under control, would cease to be controllable.

It is, finally, up to the central bank, the banking system and the other institutes which are part of our credit system to put at the disposal of government an efficient capital market, and a money market flexibly responding to changing business conditions and linked with the capital market. I should hardly need to repeat again that we cannot have an efficient market without a proper co-ordination of the inflow of short-term and long-term funds, and that such co-ordination is impossible in the absence of disciplined behaviour by all credit institutions, whether they are subject to public or to private law. Within the limits of autonomy conceded to each of the two categories of institutions and in compliance with the general rules applicable to all, the system has a sufficient degree of competition to stimulate progress.

Gentlemen,

The year 1962 was not an easy one either for those who make monetary policy of for those who have to implement it. Both have had to overcome considerable difficulties. For our part, we were comforted by the conviction that we were doing our duty and by the certainty that we could rely on your loyal collaboration. I want to say once more that collaboration does not imply mere passive acceptance of our arrangements. On the contrary, we firmly believe in the merits of a discussion in which you freely express your opinions according to a long tradition which has proved its worth. We shall continue to accept your advice and to adapt our behaviour to changing needs, as they appear and are brought to our knowledge with your help. Such controls as it is our duty to exercise over your activities, we shall continue to administer with prudence, in fulfilment of our task to safeguard the nation's saving, as the law requires us to do.

It is surely a matter in which we may take satisfaction that informed discussions among employers and workers, academic and business men, now take it for granted that there is more to the defence of monetary stability than the esoteric decisions of the central bank. It requires the deliberate collaboration of all social groups through their representative organs—trade unions, local government at municipal, provincial and regional level, and government itself. Let us not lose courage if occasionally the pattern of response to the day's events seems confused; it would be demanding the impossible at this stage to expect leadership from social forces not yet used to accept responsibilities of a general character. The process by which they rise to such responsibilities is not completed, nor can it be completed in a short while.

But while this process goes on, you and we have to live up to our own responsibilities, which are not light. For your part, you have to conduct yourselves impartially without giving way to outside pressures, and to exercise your independent judgement within the limits of the controls which surround your activities. Whether the organization of your firm falls into the sphere of public or of private law is irrelevant in this context: every one of them must vie with all the others so that all of them may become efficient instruments for advancing the common weal. As regards ourselves, it is our duty to safeguard the conditions in which you can act impartially. It is our duty also to defend our independence against the power of the state. This does not imply insubordination of any kind, but independence in the sense of being a dialectic counterweight in the machinery of government: the limits of the central bank's co-operation are marked by the point at which, in its conviction, the stability of our currency ceases to be safe.

IX. *Administration*

Organization and Staff.— In the course of the reorganization scheme for the Bank of Italy's offices outside headquarters, which began to be put into effect in 1961 and was to limit the Bank's representation to provincial capitals, the Board of Directors decided last year to close down all the remaining Agencies, including that of Biella, which had previously been raised from the status of Branch Office to that of Agency.

At the end of 1962, the Bank had 7,453 persons in its employment. This was 47 less than a year before, terminations in 1962 having numbered 275 and new appointments 228.

A thorough revision of personnel matters was carried through in 1962. The Bank had, in 1961, committed itself to a reform of the staff rules in force since 1938; after prolonged negotiations with trade union representatives the examination and discussion of staff claims with respect to remuneration and certain basic principles of employment have now been completed.

A number of new concepts were introduced in line with some of the articles of the Italian constitution and with the rules governing the status of civil servants. This applies, in particular, to equal pay for women, the abolition of probationary periods, recruitment of executive staff and accountants through public competition, promotion by evaluation on the basis of professional merit and length of service; and the introduction of examinations at crucial points of a staff member's career.

The reform has loosened up the staff hierarchy through rationalization of the promotion system and the abolition of certain grades which were defined not functionally but merely in terms of remuneration. To make this possible, a new system was introduced by which all staff members are to receive automatic within-grade salary increases every two years.

Furthermore, the Administration has built into the new staff rules a mechanism of adjustment of salaries and pensions to changes in *per caput* national income. Beginning January lst, 1964, all salaries and pensions will be subject to biennial review, so as to adjust both to variations in *per caput* national income, as ascertained on the basis of the preceding four years' indices; the range of possible adjustments is to lie within the limits of variations in real and in monetary terms.

Note circulation. In 1962 changes in the composition of the note issue were in line with the last few years' trend. The share of 10,000-lire notes, which at the end of 1961 was 79.1 per cent of the combined value of bank notes and 500-lire coins, had risen to 81.2 per cent by the end of 1962; the proportion of all other denominations declined slightly.

In spite of the conspicuous increase of notes in circulation—from 552.2 to 608.8 million notes between the end of one year and the next—the exchange of worn-out notes, especially those of 1,000 lire which deteriorate fastest owing to their use in so many small transactions, was speeded up with a view to maintaining a satisfactory standard. In this way 14.6 per cent of the total value of bank notes and 500--lire coins in circulation on December 31, 1961, were withdrawn last year, and 40 per cent of 1,000-lire notes outstanding at the same date; the corresponding figures in 1961 had been 14.2 and 31.6 per cent, respectively.

For some time the Bank of Italy has been considering the issue of new notes, and last year a design was approved. The new notes are now in production and a sufficient stock is being accumulated to begin issuing them at the end of the current year.

Capital, Reserves, and the Profit and Loss Account. Having acquired 99 shares from the Modena Savings Bank, the Mirandola Savings Bank last year became a shareholder of the Bank of Italy, without voting rights.

On December 31, 1962, the Bank's shares were, therefore, distributed as follows:

Shareholders owning 100 or more shares and therefore entitled to vote:

72	Savings Banks	177,647	shares	with	468	votes
8	Public-law credit institutes .	54,500	»	»	141	»
3	Banks of national interest .	21,000	»	»	54	»
1	Social Insurance Fund . .	15,000	»	»	34	»
9	Insurance companies . . .	31,500	»	»	99	»
93	Shareholders	299,647	shares	with	796	votes
6	Savings banks	353	shares			
99	Shareholders	300,000	shares			

Ordinary Reserves, which stood at 3,755.3 million lire on December 31, 1961, rose during the year to 4,320.2 million. This was the result of an appropriation of 115 million from 1961 profits, 502.9 million investment income from the reserve fund itself, and a diminution of 53 million, which represents distribution to shareholders of part of the 1961 investment income from the fund (under Article 56 of the Statute).

Extraordinary Reserves rose from 2,037.8 million lire on December 31, 1961, to 2,325 million at the end of 1962. This was the result of an appropriation of 115 million from 1961 profits, 203.2 million investment income from the reserve fund itself, and a diminution of 31 million, representing distribution to shareholders of part of the 1961 investment income (under Article 56 of the Statute).

In applicatiom of Article 54 of the Statute, the Board of Directors proposes, and the Treasury authorizes, the following appropriation of the Bank's net profit of Lit. 617.41 million for the year 1962:

	(million lire)
To Ordinary Reserve, 20 per cent	123.48
To shareholders, 6 per cent on capital	18.00
To Extraordinary Reserve, 20 per cent	123.48
To shareholders, a supplementary dividend of 4 per cent on capital	12.00
To the government, the residual of	340.45
Total net profit . . .	617.41

In accordance with Article 56 of the Statute, the Board of Directors further proposes a distribution to shareholders of another 30 per cent on capital, or 90 million lire, out of investment income from the ordinary and extraordinary reserve funds. This amount corresponds to 1.55 per cent of the overall reserves on December 31, 1961, and is, therefore, below the 4 per cent laid down in Article 56 as the upper limit of distribution under this heading.

THE GOVERNOR
GUIDO CARLI

BALANCE SHEET

AND GENERAL PROFIT AND LOSS ACCOUNT

BALANCE SHEET AS

ASSETS

Gold	L.	1,000,000,000,000
Cash in hand	»	12,108,905,851
Domestic bills of exchange	»	615,412,982,356
Bills for collection	»	268,763,284
Advances	»	260,373,538,378
Deferred clearing house payments	»	12,015,304,000
Foreign exchange balances abroad	»	63,479,142,814
Italian Exchange Office-current account	»	2,146,040,796,785
Government or government-guaranteed securities	»	243,651,538,418
Premises	»	1
Miscellaneous debtors	»	131,599,180,321
Advances to the Treasury: extraordinary	»	485,000,000,000
	L.	4,969,950,152,208
Securities and other valuables deposited	»	4,845,362,096,502
	L.	9,815,312,248,710
Items written off in past years	»	9,069,552
GRAND TOTAL	L.	9,815,321,318,262

Audited and found correct - Rome, 10th May, 1963

The Auditors

ALESSANDRO BACCAGLINI
BRUNO DE MORI
MARIO MAZZANTINI
FELICE PAPPALARDO
RAFFAELE PILOTTI

p. p. **The Accountant General**

ARNALDO FALSINI

OF DECEMBER 31, 1962

LIABILITIES

Note circulation	L.		3,234,450,413,500
Bank drafts, cashier's cheques and other sight liabilities	»		42,864,257,314
Current accounts	»		122,281,814,680
Time deposits (incl. compulsory reserves)	»		987,825,943,201
Miscellaneous creditors	»		236,938,279,924
Treasury current account	»		320,310,579,475
Miscellaneous services for account of government	»		17,716,202,296
Net profit for 1962	»		617,414,358
			4,963,004,904,748
Capital	L.	300,000,000	
Ordinary reserves	»	4,320,260,352	
Extraordinary reserves	»	2,324,987,108	6,945,247,460
	L.		4,969,950,152,208
Depositors	»		4,845,362,096,502
	L.		9,815,312,248,710
Items written off in past years	»		9,069,552
GRAND TOTAL	L.		9,815,321,318,262

The Governor

GUIDO CARLI

GENERAL PROFIT

FOR THE

EXPENDITURE			
Administration and contributions to staff retirement fund	L.	31,461,629,808	
Directors' emoluments	»	314,176,063	
Transport of notes, coin and other valuables	»	120,301,451	
Note printing	»	5,156,390,568	
Expenditure on premises	»	672,133,190	
			37,724,631,080
Circulation tax on notes and demand drafts	L.	6,865,653,099	
Income and company taxes	»	5,200,378,246	
Sundry taxes and dues	»	411,267,197	
			12,477,298,542
Amounts written off	L.		5,289,741,922
Interest payable	»		699,599,423
Charity and other contributions	»		105,814,617
	L.		56,297,085,584
Net profit for distribution	»		617,414,358
TOTAL	L.		56,914,499,942

APPROPRIATION

To Ordinary Reserve	
To Extraordinary Reserve	
10 % Dividend to shareholders	
To the government	
TOTAL DISTRIBUTABLE	

Audited and found correct - Rome, 10th May, 1963

The Auditors

ALESSANDRO BACCAGLINI
BRUNO DE MORI
MARIO MAZZANTINI
FELICE PAPPALARDO
RAFFAELE PILOTTI

p. p. **The Accountant General**

ARNALDO FALSINI

AND LOSS ACCOUNT

YEAR 1962

RECEIPTS

Discounts	L.	18,233,405,136	
Interest on advances	»	5,040,579,528	
Interest on other assets	»	23,282,080,352	
Commissions and custody fees	»	1,539,481,172	
Profits on foreign transactions	»	2,078,051,495	
Sundry profits	»	637,011,642	
			50,810,609,325
Interest on government securities	L.	5,835,805,334	
Revenue from real estate	»	268,085,283	
			6,103,890,617
Total . . . L.			56,914,499,942

OF NET PROFIT

	L.	123,482,872
	»	123,482,872
	»	30,000,000
	»	340,448,614
profit for the Year	L.	617,414,358

The Governor

Guido Carli

THE ADMINISTRATION OF THE BANK OF ITALY (1962)

BOARD OF DIRECTORS

CHAIRMAN: Guido CARLI * – GOVERNOR OF THE BANK

Paolo BAFFI * – GENERAL MANAGER

Ernesto BINDOCCI – DEPUTY GENERAL MANAGER AND SECRETARY TO THE BOARD

Paolo BLUMENSTIHL
Renato BRANZI
Gaetano CARBONE *
Gian Luigi DONES *
Antonio FONDA SAVIO *
Francesco MAILLER
Pericle MARTELLI
Paolo MONICO
Lucio MORODER
Eugenio VACCARI *
Ernesto VACCARINO
Giambattista VIRGA

* Member of the Executive Committee.

BOARD OF AUDITORS

Alessandro BACCAGLINI
Bruno DE MORI
Felice PAPPALARDO
Raffaele PILOTTI
Mario MAZZANTINI

ALTERNATE AUDITORS

Domenico AMODEO
Raffaele D'ADDARIO

THE CENTRAL ADMINISTRATION

MANAGERS

Tullio RICCIO
Ciro de MARTINO
Paolo VECCHIA
Vincenzo ONORATELLI
Emilio RANALLI
Salvatore GUIDOTTI