

BANCA D'ITALIA

ABRIDGED VERSION OF THE

REPORT

FOR THE YEAR

1969

PRESENTED BY THE GOVERNOR TO THE
ORDINARY GENERAL MEETING OF SHAREHOLDERS

HELD IN ROME ON 30 MAY, 1970

ROME

PRINTING OFFICE OF THE BANCA D'ITALIA

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I. – The World Economy

The economic trend in the main industrial countries was again marked in 1969 by sustained progress in production and foreign trade. But these favourable tendencies were accompanied by an appreciable speeding-up of the rate of inflation, coupled with the persistence, even though in a less marked form, of major disequilibria and structural deficiencies in balances of payments. Policies for curbing demand, introduced too late and relying mainly on monetary instruments, helped to accentuate the rise in interest rates. In the last months of the year demand inflation was reinforced by cost inflation brought about by the concentration of wage increases within too short a space of time to allow them to be absorbed by the rise in productivity. The wage push thus replaced the pressure initially exerted by demand, prolonging the inflationary processes and fostering expectations of their continuance. Demand inflation and restrictive monetary policies designed to combat it, on the one hand, and the effort to achieve a new equilibrium between the different variables of the system in order to absorb the cost inflation, on the other hand, led almost everywhere, in the second half of the year, to a gradual slackening of the rate of growth, creating new problems for the authorities concerned, who are endeavouring to keep it within acceptable limits. Thus, beset by domestic problems, the industrial countries have been unable to increase—indeed, have actually reduced in relation to their gross national product—their contribution of real resources to the developing countries; the latter, however, have benefited by the improvement in the terms of trade between primary products and industrial products.

Further strains have resulted from massive movements of capital stimulated by the persistence of interest rate differentials and expectations of changes, subsequently fulfilled, in some monetary parities, as well as by political uncertainties and the existence of appreciable differences in the structures of capital markets, forms of investment and methods of taxation.

The tensions resulting from these developments have, however, been kept in check by closer international monetary cooperation, which is increasingly proving to be an essential instrument for directing and sometimes correcting national economic policies.

The agreement on the creation of special drawing rights became operative with the first allocation of 3.5 billion dollars at the beginning of this year; the main users of the new instrument up to the present have been the United Kingdom and a few developing countries, while the main creditors have been, apart from the United States, Italy, Germany and Japan. The arrangement with the South African Government for the sale of newly-mined gold on the free market or to the Fund created the basis for an orderly flow of gold into the international monetary system. The increase of more than one-third in the Fund quotas, already approved, will be implemented at the end of next autumn. The further strengthening of the reciprocal monetary arrangements centred on the Federal Reserve System proves the acknowledged usefulness of this instrument for the recycling of international means of payment; it was emphasised that the total utilisation of the lines of credit has already reached an amount exceeding that of drawings on the Fund and of sales of gold to the official monetary authorities of the countries participating in these arrangements. Lastly, the countries belonging to the European Economic Community approved a short-term support mechanism operated by the respective central banks and designed to finance temporary balance of payment deficits due to any accidental difficulties or divergences of economic trends which may develop despite the co-ordination of monetary policies. The combination of these agreements has set in motion a mechanism suitable for providing the international monetary system with an adequate volume of both conditional and unconditional liquidity. At the same time, there has been an appreciable easing in economic and monetary relations between the industrial countries as a result of the devaluation of the French franc last August and the revaluation of the German mark in October, following upon the change in the parity of sterling in 1967. These operations have gradually created a structure of par values based on more realistic relationships.

Despite the slowing-down which occurred in the United States, the rate of growth in the industrial countries as a whole kept around 5 per cent, that is, at a level not far below that of the preceding year and in line with the long-term trend, mainly thanks to the favourable results achieved in Japan and in the two main countries of the European Economic Community.

The labour market was characterised by tendencies which normally emerge towards the end of the upward phase of the business cycle.

Thus the level of employment, after a few years of relative stability, following the revival of production about a year earlier, rose in nearly all industrial countries not only in the manufacturing sector but also in the economy as a whole. Similarly, unemployment fell in most countries, although remaining in some at levels higher than those reached in previous expansionary phases. The tensions in the labour market, as is also shown by the higher ratio between vacancies and the number of unemployed, increased everywhere; this phenomenon was particularly marked in the German Federal Republic. The rise in productivity, which had already advanced substantially in 1968, continued, especially in the manufacturing sector, but at a slackening rate. On the other hand, the increase in wages and labour costs quickened everywhere except in France. By the end of the year the wage push had become very strong, particularly in Germany, Italy and the United Kingdom; consequently, as is normal in these phases of the cycle, the rise in unit cost became faster, this phenomenon being more pronounced for the economy as a whole than for manufacturing industry alone.

The most dynamic component of demand in practically all the industrial countries was the domestic component, although foreign demand, which had been the main motive force behind the expansion in 1968, continued to be well sustained. The growth in private consumption was the result of the rise in employment and the larger wage increases; the growth in fixed investment took place mainly in engineering and means of transport, while construction activity remained almost stationary.

The rise in prices, measured by the deflator of the gross national product, quickened everywhere, but was particularly marked in the United States and France; the countries in which it was most pronounced were generally those in which there was a larger increase in unit labour costs. The rise in wholesale prices was generally greater than that in consumer prices. This phenomenon was due to the expansion in investments, the poor agricultural harvests, the increase in indirect taxation and the general rise in import prices, owing to the higher prices of primary products and the upward movement of prices of manufactured goods. Towards the end of the year and in the first months of 1970 the upward tendencies strengthened again in Germany and Italy, while slackening slightly in the countries where the increase in prices had been more marked in the preceding period and had shown a higher annual average.

The policies for curbing demand adopted previously spread with an increasingly restrictive emphasis. They contributed to the gradual cooling-down of the economic climate in the second half of the year, particularly in the United States, creating the conditions for a further slackening of production.

Fiscal policy, based both on heavier taxation and on the curbing of expenditure, was completely successful only in France, where it led to a surplus, however small, in the overall cash position, and in the United Kingdom, where the budget shifted from a deficit to a substantial surplus; appreciable results were also achieved in the United States, where a Federal budget deficit of 25 billion in 1968 was followed by a surplus of 3 billion in 1969. But in these countries, as in others, the task of controlling demand was entrusted primarily to monetary policy, shaped mainly with a view to the attainment of domestic aims. Official discount rates rose appreciably everywhere either in response to increases which had already occurred in market rates or with the object of anticipating and stimulating such rises. At the end of February of this year the official rates were still at unusually high levels in the United Kingdom, France and Canada; since then a downward movement has started, initiated by the United Kingdom. The programme of control involved the authorities in a wide range of measures of intervention: the raising of obligatory reserves, the imposition of quotas on bank credit, the control of the foreign position of commercial banks, the prohibition of interest payment on accounts held by non-residents, the tightening of the credit conditions governing consumer sales, special deposits for payments of imports, etc., are the instruments whose use was gradually resorted to in the various countries in order to influence the volume and cost of credit.

Contrary to expectations, despite the slowing-down in the growth of national incomes, the volume of world trade expanded slightly faster than in the preceding year. The degree of interdependence between economies thus increased, particularly among countries with similar characteristics; thus, in line with the long-term trend, intra-EEC trade expanded much more than that among the countries of the OECD and among the industrial countries of the West, and the trade of these, in turn, grew more than the average of world trade. On the other hand, trade among socialist countries increased less than trade with the rest of the world. The creation of a transferable currency at least partly convertible into gold with a parity based on a realistic evaluation

of international costs and prices, which is at present being studied, could provide a stimulus to trade not only between socialist economies and western countries but also among the socialist economies themselves.

The balance of payments position continued in 1969 to be characterised by major disequilibria. As far as the current account is concerned, heavy deficits occurred again in the United States, France and Canada and large surpluses persisted in Germany, Italy and Japan. Nevertheless, if the year's results are assessed in the light of the trends which have been becoming increasingly clear during the last few months, appreciable improvements in the direction of the required reversal of positions or major reductions in the imbalances are observable almost everywhere except in Japan and Canada, where the surplus and deficit, respectively, increased. The most important changes are occurring in the United Kingdom, which moved from a large deficit in 1968 to a surplus in 1969— a shift of over one and a half billion dollars, with prospects of further improvement this year; in Germany, where the current account surplus was reduced as a result of the adjustments of the mark and the franc and pressure of domestic demand; and in France, where the position is rapidly moving towards the achievement of a substantial surplus.

Movements of medium and long-term capital and short-term bank funds were not always in the directions suitable for producing a stabilising effect. In the United States a large net outflow of medium and long-term capital, which, together with the current account deficit, helped to bring about an unprecedented liquidity shortage, was coupled, owing to the restrictive monetary policy pursued by the U.S. authorities, with a large inflow of short-term funds which led to the formation of a substantial overall balance of payments surplus. In Germany, too, an outflow of long-term capital twice as large as that in the preceding year more than counterbalanced the surplus on current account, producing a large overall deficit; there were substantial contrary movements of short-term funds coinciding with the expectations of revaluation of the currency which arose during two different periods in the year. Stabilising flows of funds took place, on the other hand, in Canada and France, while in Italy the capital outflow considerably exceeded the surplus on current account.

Viewed as a whole, the overall balance of payments results for 1969 reveal some basically unbalanced structures: the United States'

surplus in respect of goods and services is quite insufficient to finance unilateral transfers and capital exports on a scale appropriate to that country's international responsibilities; Japan's current surplus will go on increasing beyond acceptable limits unless the authorities adopt further measures of liberalisation or encourage larger capital exports; in Italy, the current account surplus and the capital account deficit of unprecedented size, constitute a structure which is not in accordance with the long-term aims of economic policy.

The total volume of world reserves at the end of the year was practically unchanged in comparison with December 1968. This fact, though it relates to a short period during which there was an exceptional expansion in world trade, is a further argument in favour of the deliberate creation of reserves in the form of special drawing rights. Throughout the year, however, there was a succession of large fluctuations in reserves, and especially in their foreign exchange component. The contraction in international liquidity resulting from the surplus of the United States balance of payments, measured on official transactions basis, was offset by the increase in gold reserves and net creditor positions in the Fund, and by the growth in the official sterling holdings of countries of the sterling area. The official reserves of the countries of the European Economic Community were reduced to the advantage of those of the United States, Japan and the United Kingdom and, generally speaking, those of the developing countries.

The behaviour of demand in industrial countries and the policies of containment, relying mainly on the monetary instrument, created the conditions for a general rise in interest rates. The initial impulse was given by the United States, where monetary policy was brought to bear with unprecedented force on the volume and cost of credit. This line of action, together with a regulation limiting the maximum rates which the banks are allowed to pay on their deposits, led at the beginning of 1969 to a large-scale liquidation of certificates of deposits, that is, of one of the banks' most important means of collecting funds. The banks were thus obliged to compete with each other in the Euro-dollar market, from which they obtained increasing amounts which reached a maximum of about ten billion dollars. This action, coming on top of the pressures resulting from speculative movements, which in turn were prompted by the expectations of revaluation of the German mark in April-May and in September, had as its counterpart an inflow

of funds from Italian, French and Belgian official holdings, to which were added the exports of funds by U.S. residents attracted by the high returns offered by the Euro-dollar market. The result was a rise in interest rates on this market up to as high as 13 per cent towards the middle of the year; after that, in alternating phases, the situation became gradually easier. Not until the early months of this year was there any appreciable reduction in the debtor position of the U.S. banks, partly as a result of measures adopted by the monetary authorities. The conditions prevailing on the Euro-dollar market and the state of domestic markets created by the restrictive monetary measures adopted by the individual countries helped to push up the whole structure of interest rates in all the industrial countries. This brought about an adjustment which appreciably reduced the divergences between the rates applied in the different markets. The same process of alignment was observable in the case of long-term rates, though to a smaller extent. Nevertheless, the overall picture remains one of a high-rate structure even in comparison with that—already well above the level of a few years earlier—obtaining towards the end of 1968.

In the light of the events of the year and the prospects for 1970 it is possible to distinguish the problems needing to be tackled by the national authorities and by international monetary cooperation in the near future. These problems are bound up, directly or indirectly, with an inflationary explosion—only second in violence to that of the Korean war period—which is the culmination of a cumulative process consisting of years of creeping inflation and lack of financial discipline. This is a phenomenon which has not only become the constant torment of wage-earners, businessmen and savers but has also made it increasingly difficult for the government authorities to reconcile internal and external objectives and short-term needs with the long-term requirements connected with structural differences in production, taxation and finance, and to overcome the public's ever-increasing resistance due to accumulated inflationary expectations rekindled by the upward movement of costs.

The primary source of concern in all countries is undoubtedly the trend of prices, which will rise at least as much in 1970 as they did last year; the second half of this year may bring some possibilities of an easing of the tensions insofar as the anti-inflationary measures begin to succeed. The rises in unit costs are, however, steadily spreading

and becoming increasingly difficult to control both because they are hardly liable to be curbed at all by use of fiscal policy, and still less by monetary policy, and because the possibility of their transfer on prices ultimately weakens the resistance of government and business circles to accepting them. Cost pressures will probably produce their full effects this year, the ultimate result being their partial transfer on prices, in the absence of which more serious consequences might ensue.

These phenomena show how difficult it is to reconcile a high rate of expansion and of utilisation of human and material resources with stability. The past few years have, it is true, on the whole been characterised by a high rate of growth, but there have also been long pauses due precisely to the failure of the efforts to reconcile the two aims stated above: periods of cyclical upswing have always led to the heating-up of the economy—labour market pressures, price rises, balance of payments deficits—which have finally halted the expansionary process as a result of adjustments brought about (and it could not have been otherwise) through changes in prices, profits, investments, the level of employment and, in some instances, through exchange rates variations.

The final effect has been partly to nullify the wage increases gained. Experience, by showing that correct demand policies are essential in order to prevent over-heating of the economy, has also made it clear that these policies, despite the ever-increasing refinement of the instruments of intervention, are still inadequate, particularly in the sphere of government decision-making. The lack of success of incomes policies can hardly be disputed; it is attributable to a wide variety of causes: the difficulty of applying them in boom periods, when they are most needed; the existence of the sliding-scale; the differences in wage levels between regions and between sectors of economic activity; the failure of above-average productivity gains to be reflected in prices and the refusal to accept wage increases smaller than those in productivity when the latter are above average; and, most of all, the lack of any clear idea of the aims to be achieved by these policies, resulting in their general abandonment. Nevertheless, the international economic organisations are beginning to consider whether there ought not to be a thorough re-examination of the whole problem. It will probably have to be reconsidered on the basis of a different relationship between the advance in money incomes and the rise in productivity, in the direction of recognition of the undoubted effect of the former on the latter in

the medium term (it being generally admitted that in the short term very large wage increases tend to upset economic equilibrium instead of stimulating the rise in productivity, which may even slow down); and the problem must be tackled within a multinational framework in which all the social partners involved—the government, trade unions and employers—participate in the working-out of medium-term economic objectives.

A second subject of concern is the dangers of recession inherent in the maintenance of anti-inflationary policies by the United States. Observers no longer maintain unanimously as they did a few months ago, that it is absolutely necessary to avoid any diminution of the severity of restrictions, because nearly all the economic indicators—including the trend of unemployment, which is the most worrying from the social point of view, but excluding the movement of prices, still being pushed up by past pressures of demand and costs—point to a certain worsening of the economic situation: in January-March, for the second consecutive quarter, the gross national product contracted, and this time considerably more than had been expected.

It must not be forgotten that the United States' share of world trade is very large. An American recession could thus bring about a downturn in the world business cycle. This explains why western countries attach great importance to the choice of the most appropriate moment for a gradual revision of the demand policies applied in the United States, and especially monetary policy, which has been somewhat relaxed in the last few months, and why so much concern is raised by the action of the U.S. authorities, who are obviously inclined to take all necessary steps to keep the recession within acceptable limits but are at the same time politically committed to curbing inflation and avoiding a premature relaxation such as that of the summer of 1968. Similar questions arise, though less dramatically, with regard to the economic policies of France and the United Kingdom. Conversely, in the case of Germany and Italy the international organisations' recommendations favour policies designed to curb demand.

The process of eliminating external disequilibria made only modest progress in 1969. This is probably due to the growing weight, in the formation of these imbalances, of structural causes as apposed to cyclical factors. On the one hand there is the growing interdependence of national economies, as revealed by the tendency of international trans-

actions to increase more than national incomes, the mobility of medium and long-term capital and of bank funds and, lastly, the ability of multinational companies suddenly to shift their liquid resources from one country to another or from one currency to another. On the other hand, not only do the targets of economic policy continue to diverge in response to the different priorities assigned to them in the various countries but there are also great differences in levels of productivity — and, still more important, in the variations in these levels—between the different industrial sectors in the same country and between one economic system and another. Consequently, while the balance of payments disequilibria which are due to cyclical reasons and the trend of demand can be corrected without too much difficulty, this is not true of those attributable to the other factors mentioned above. Situations therefore arise where, despite the pursuit of the right demand policies, the competitive position of one country nevertheless changes compared with that of another, thus creating incompatibility between internal and external targets.

There are some who think a possible answer to this problem would be to introduce greater flexibility of exchange rates within groups of similar countries. The changes in monetary parities which took place from the autumn of 1967 onwards were, it is now unanimously agreed, decided upon much too long after the emergence of the fundamental disequilibria which prompted them; the delay caused, among other things, sudden massive movements of funds and contributed in no small measure to the instability of the international monetary system in recent years. These disorders have increasingly demonstrated the need for more timely adjustments of monetary parities, frequent and small in extent, designed to help correct an emerging fundamental disequilibrium, and for a slight widening of the present exchange rate margins in order to forestall or check speculative and reversible movements of funds from one centre to another. The aims pursued by the countries interested in these solutions are very limited. They obviously exclude both unlimited and very wide fluctuation of exchange rates; what is in fact proposed is a slight widening of the present margins up to a maximum of 2 per cent and the possibility of parity adjustments of up to 2 or 3 per cent per year.

A related problem is the re-establishment of orderly cross-frontier flows of capital. The balance of payments difficulties encountered in

turn by the main industrial countries—first the United States and the United Kingdom, then France and after that Italy and Germany— have spread the belief that the interruption of these flows in order to combat speculative phenomena and tax evasion, even though only in a manner compatible with international commitments, is not feasible except by the use of methods which are liable to restrict the freedom of current transaction (goods, services, tourism) and thus to lead sooner or later to isolation of the country in question, the breaking of the links which integrate it in the rest of the international economic area in which it operates and in the community of industrial countries—in short, to lead to economic and financial autarky, the precursor of moral and material impoverishment.

In other words, free international movement of capital is increasingly seen to be one of the essential prerequisites for the continuance of the process of integration between the various economies, which cannot be held up other than for very short periods. The danger of the development of tensions can only be eliminated by the harmonisation of both fiscal legislations and market structures. The most recent experience also shows that freedom of capital movements is a source of flexibility which helps to facilitate the achievement of balance of payments aims. Actually, many industrial countries deliberately plan for or do in fact attain a goods and services surplus vis-a-vis the rest of the world, that is, a net export of real resources. In the absence of a corresponding outflow of public or private capital this surplus would result in an increase in reserves which, beyond certain limits, represents the form of export of real resources which is least desirable for the national economies and for the system as a whole.

A problem of no small importance, which is beginning to be viewed with some apprehension, is that of the future behaviour of the balance of payments of the United States. The basic trend observable is the tendency of that country's current account balance to decrease in proportion to the national income; the present forecasts for 1970 appear to point the formation of a surplus, which, however, is expected to remain far below the levels reached in 1963-64. Moreover, owing to the relaxation of monetary restrictions and the slowing down of business activity, it is not inconceivable that there might be a certain outflow of short-term funds, so that the basic deficit might be reflected in the deficit on official transactions basis.

It is widely believed that such a development ought not to create serious problems this year for the monetary authorities of the other industrial countries because both the working funds of the Euro-dollar market and official reserves in the intervention currency have previously been greatly depleted. But the situation is fraught with disquieting possibilities. For the same phenomenon could continue into 1971 and subsequent years, since the restoration of internal stability in the United States is not necessarily reflected, as is shown by the events of the early 1960's, in a balance of payments equilibrium. Under these circumstances the monetary authorities of the other western countries might be faced with the dilemma of whether to accumulate dollars and thus expose themselves to the repercussions of an economic policy which they have not helped to formulate or to impose some restriction on their acceptance.

The latter choice might entail an appreciation of the European currencies vis-a-vis the dollar—a solution for which the countries of the European Economic Community will be prepared only insofar as they have made progress towards the achievement of a substantial degree of convergence of their economic policies shaped in the light of common objectives; that is, insofar as they have advanced along the road to at least partial political unification, which will make possible a gradual harmonisation of their monetary policies. It should be pointed out, however, that in this event the monetary equilibrium between the United States and Europe could be radically changed as a result of a transfer of economic and political responsibilities to the old continent.

The development of the principles adopted at the Conference of Heads of State and Governments held at The Hague last December has cleared the way for these countries of action. The preoccupations of central banks are obviously centred on the consequences of a further increase in the degree of liberalisation of capital movements within the Community, the reduction of the margins of fluctuation of European currencies in relation to each other, the proposed establishment of a European reserve fund and the progressive unification of monetary policies.

The means, timing and techniques adopted for the attainment of these aims are at present the subject of much discussion, which will inevitably be influenced by the forthcoming negotiations for the entry of the

United Kingdom and other countries into the EEC. One cannot overlook the growing conviction that the unification of monetary policies cannot constitute the driving force of the whole process of integration; the very most that is acceptable is a parallelism between progress in the monetary field and progress in the field of economic policy, avoiding divergence between the two. Any other line of action would involve the danger of advancing without the support of public opinion and in the absence of informed political decisions.

Interest rates.— The yield in the financial markets continued the vigorous upward movement which had occurred in the early months of 1969. The rise continued until January 1970 with characteristics which differed according to the maturities of the securities.

For the 3-month funds—excluding the British market, where high rates had been established since the 1976-1968 crisis and the Swiss market, the reactions of which are, for institutional reasons, more moderate—the rise during 1969 was around 2 percentage points calculated on a mean annual basis, with a maximum of 3.3 points for Euro-dollars; the movement was irregular, with pauses followed by sharp increases, particularly high at the end of the two semesters.

In the long-term securities market the rise in rates on the secondary market was more regular, without the uncertainties which had been a feature of their progress throughout much of 1968. Financial yields in Italy, Germany, the Netherlands and Belgium, which in the past had been outside the general trend, although displaying differing degrees of rigidity, showed the same movement.

On the whole the increase was much less than that for short-term rates. However, since the periods of increase and those of initiation of the process were different from country to country, the mean variation on an annual basis (60 per cent for public securities and 80 per cent for private securities) does not adequately represent the phenomenon; in fact on the Italian, German, Dutch and Swiss markets the rise continued in the first quarter of the current year.

It has therefore been felt appropriate to extend the comparison to the increases which occurred between October 1968, when the acceleration of the increase in long-term rates in the most important markets began, and March 1970. In January of the current year, when the

upward movement reached its peak in most markets, the mean rise was 1.3 percentage points, with a maximum of 1.7 for the United States and a minimum of 0.9 for Italy. Over the entire period under consideration the mean of the maximum variations which occurred was 1.6 percentage points, with Italy and Sweden at the upper and lower limits respectively; in a few countries, particularly in United States and, to a greater extent, in the United Kingdom, the rise was partly offset by a fall in the early months of the year. When account is taken of the different market conditions in the longer period and the institutional characteristics of the financial systems, such as, for example, the lack of a money market in Italy to relieve the pressures on long-term rates and the prevalence of institutional investors in Sweden, the characteristics and extent of the rise seem not have differed very greatly.

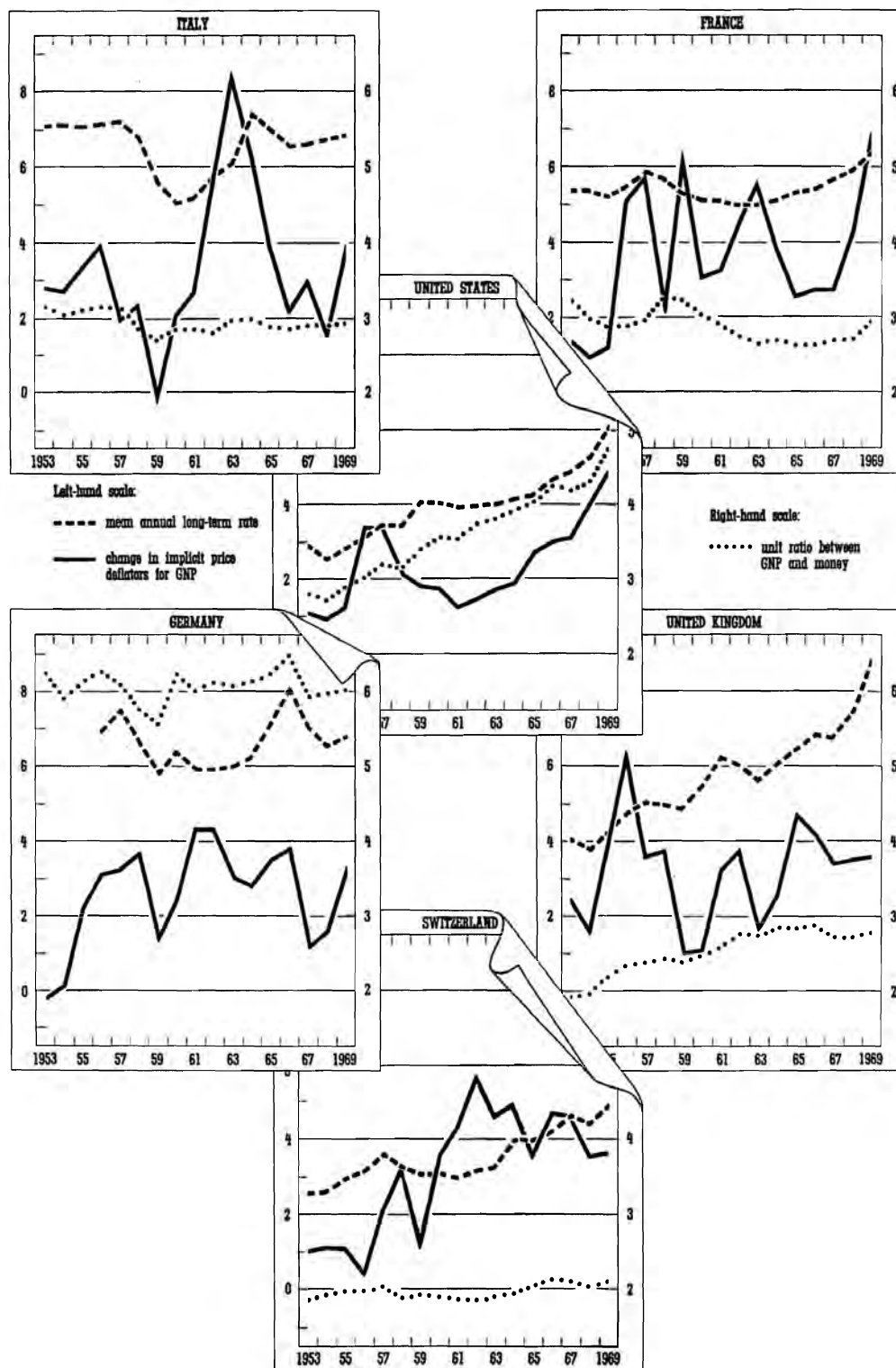
Previous Reports have drawn attention to the study of the causes which allowed this upward movement of interest rates to develop. The origin was traced, from the geographical point of view, to the United States and, from the functional point of view, to the policy pursued by that country in combating inflation, and also to certain transmission mechanisms of the effects connected with the international monetary base, especially in the Euro-dollar market. Other contingent factors, such as monetary crises, had contributed to short-lived increases or reductions in rates.

Since increasing credence is being given to the thesis that a return to the level of rates ruling prior to the rise is improbable, it now seems appropriate to direct the analysis toward trying to identify any basic trends which have led to the general rise in financial yields.

For this purpose a comparison has been made, for the period 1953-1969, between the long-term rate, the income velocity of money and the rate of inflation for certain countries, including Italy (Chart 1).

Although with small differences of timing, these three magnitudes appear to move, in most cases, in the same direction. However, there are times, in certain countries, when monetary restrictions, significant in this context whenever the income velocity of money increases, push interest rates up despite a falling trend in the rate of inflation, and vice versa; this happened, for example, in the United States from 1958 to 1961, in Germany from 1962 to 1964 and, less clearly, in France from 1959 to 1963. An exceptional case is Switzerland, a market from

CHART 1



Interest rate, income velocity of money and rate of inflation in certain countries

Note: The definition of money is that adopted by the International Monetary Fund; for Italy use has been made of the monetary base.

the basic trend of the interest rate appears opposite to that of the inflation rate.

The lack of uniformity in trends may, however, not be decisive for the purpose of attributing the pre-eminent role, in determining the level of interest rates, to one of the two variables examined; for the divergence of trend could be the consequence of timing differences in the perception of inflation, which vary from one market to another and are subject to change depending on the continuity of the inflationary process and the modifications undergone by the economies in the course of time.

The argument is corroborate, however, by the observation that only in the markets in which the income velocity of money has a tendency to grow—namely, the United States, the United Kingdom and, to a lesser extent, Switzerland—do the financial yields show a long-term upward movement; the other countries simply provide examples of wide oscillations (Italy and France) or frequent fluctuations (Germany).

It therefore seems quite plausible to put forward the hypothesis that monetary policy has played the most important role in determining the level and fluctuations of long-term interest rates. Since, moreover, changes in the direction of monetary policy are nearly always linked with inflationary phenomena, the analysis is transposed to the validity of these connections.

There is good statistical evidence that the demand for bonds by private individuals and companies decreases as inflation grows. If the scale of public and private investment plans is not capable of being revised, because of institutional rigidity or the existence of adequate margins of real profit, then in order to place an equal amount of securities under the new conditions it is necessary to re-establish the real rate desired by the market, by raising the nominal rate. This will tend to be low if the proportion of securities which can be placed with financial intermediaries and the Central Bank is high; in turn, the amount of these purchases will depend on the sensitivity to the degree of inflation of the funds acquired by the intermediaries and on the amount of the new monetary base which can be created through this channel. If, however, savings which, as a result of inflation, are not attracted to investment in bonds, instead of being directed to the acquisition of other financial assets (for example shares) were to be converted into a greater demand

for real assets or were to be exported, the policy of intervention on the market by the monetary authorities would be difficult to implement or costly in terms of reserves.

If, under the conditions of rising rates described above, the financial intermediaries, in particular the banks, are not free to fix the interest rates which they pay for the acquisition of funds, the transmission of the effects to longer term rates is more immediate since, the funds collected being reduced, the contribution of these operators on the bond market is also reduced.

Since January 1970, as has already been pointed out, the rates on most markets have shown wider fluctuations for short-term securities than for long-term securities. In Italy, Germany and Switzerland, however, the rise continued. The center of the reversal of trend has again been the United States market; the diminution of the tensions in this market has been retransmitted by the Euro-dollar market to the other national markets with very slight differences of timing.

The inflationary pressure which have arisen or already exist in European countries have meanwhile made the present levels of rates compatible with the new economic situations of those countries. In this way resistance to the reduction of rates has been transferred from the United States market to the European markets; this resistance can be overcome, first, to the extent to which the rate of inflation is kept under control and, secondly, if the policies which are applied to achieve this object do not involve direct effects on the level of rates.

II. — Economic conditions in Italy

The national accounts and the economic situation

General trends.— The main problems of the Western industrial countries—inflationary pressures, high interest rates and balance of payments disequilibria—also characterised the course of the Italian economy in 1969.

At the beginning of the year these problems were not yet affecting our country's economic policy, the expansionary trend of which had been accentuated towards the middle of 1968 by the addition of fiscal measures—designed to stimulate domestic demand especially for investment—to a monetary policy aiming to finance the expansion at a pace somewhat above the medium-term average at stable interest rates.

The main targets of economic policy were in fact to speed up the rate of growth within limits ensuring that its continuity would not be impaired and to attain a new balance between domestic demand and supply by adjusting the former to the levels of the latter.

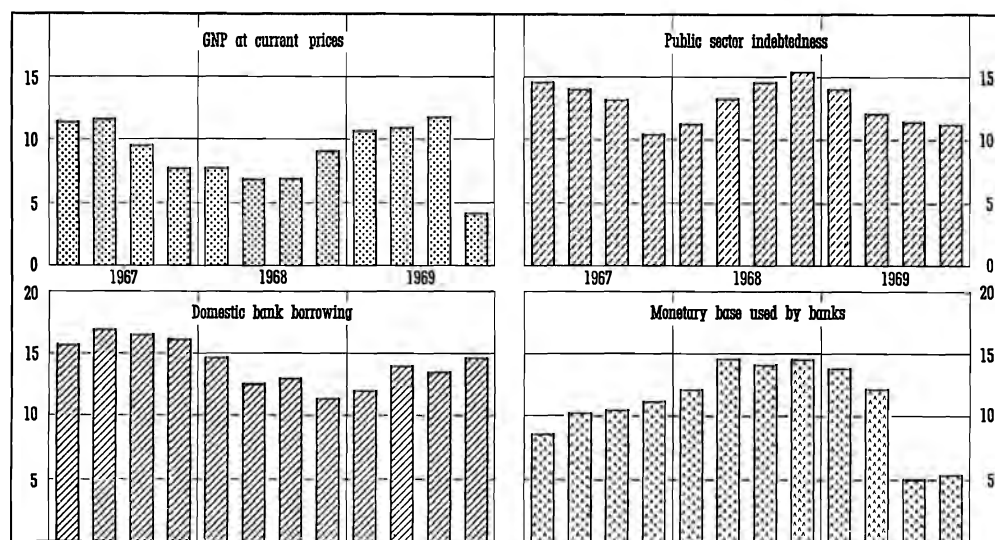
Towards the end of 1968 and at the beginning of 1969 the economic situation was developing in these directions. The rise in domestic demand and in incomes, after its hesitant movement in the early part of 1968, was quickening appreciably. In particular, there was a strengthening of demand for directly productive investments, coupled with that already high in the building sector: industrial production was increasing substantially, with a corresponding improvement in dependent employment.

As early as the spring of 1969, however, the expansionary effect of the public finance was slackening, although the increase in spending decisions continued; subsequently, payments of salary arrears and pension increases rose rapidly, but were partly offset by the slowing down of other expenditure, especially on investment (Chart 2).

On the other hand, towards the middle of the year the acceleration of the rise in prices and the growth in the overall balance of payments deficit due to capital exports made it necessary to reduce the sizeable liquidity margin of the credit system so as to counter the creation of inflationary expectations and make the economy respond more promptly to any corrections or changes in direction which might subsequently

be found necessary. The formation of the banks' monetary base slowed down appreciably, particularly in the third quarter; nevertheless, owing to the preceding liquidity situation, this did not prevent the financing of the expansion of the economy, especially in the form of borrowing from banks, to continue at the same level as before though at higher interest rates. The system's liquidity situation having changed, the formation of the monetary base was resumed towards the end of the year at a rate proportional to the forecast of income growth at current prices.

CHART 2



Trend of the gross national product and certain financial aggregates

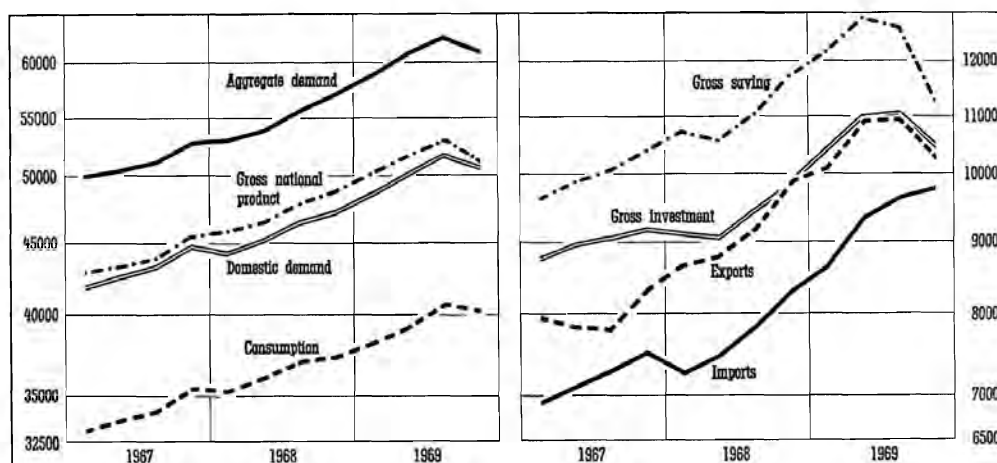
(Percentage changes for each quarter on the corresponding period of the previous year. For bank borrowing, the monetary base and the indebtedness of the public sector, the changes are calculated on the average quarterly positions)

As a result of the tendencies briefly outlined above, the growth of the economy already slackened somewhat in real terms in the second quarter, during which, as mentioned, the proportions of the inflationary component were becoming substantial; the expansion nevertheless continued at a satisfactory rate throughout the summer, accompanied by a sustained growth in foreign trade, especially on the import side: this halted the rise in the surplus on current account, confirming the favourable overall trend of domestic demand (Chart 3).

Consumption was in fact stimulated by the higher level of dependent employment, by the rise in wages at rates practically twice as high as a year earlier and by the larger current transfers effected by the public

authorities. The trend of capital investment was also sustained owing to the high degree of utilisation of productive capacity and the still satisfactory movement of overall profits due to the increase in production and the possibility of transferring to prices the increased costs, especially for raw materials.

CHART 3



Trends in demand, supply and their components

(Quarterly estimates on an annual basis, in billions of current lire, seasonally adjusted; logarithmic scale)

Average industrial output in the first eight months of the year was 8 per cent higher than in the corresponding period of 1968.

The trade union disputes concerning the renewal of major labour contracts, which began in September and continued for about three months with demonstrations of unusual violence, halted the expansionary phase. The main sectors affected were metallurgy, engineering, the chemical industry and the rubber industry; the effects of the repeated long discontinuities of activity on production were aggravated by the high degree of integration of working processes and the interdependence of firms, which also prompted the application of new strike tactics deliberately designed to increase the production losses.

Industrial activity in the period from July to November, the month during which the longest trade union disputes occurred, fell by 12 per cent, with maximum drops of over 30 per cent in some branches of activity. Furthermore, owing to the repercussions on tertiary activities, the national product contracted in the last quarter by 2.1 per cent in terms of current prices and even more in terms of constant prices. The

loss in production led to a reduction in exports, while imports continued to increase, though at a slower rate; the current account surplus therefore declined appreciably in the third quarter, not owing to an improvement in domestic demand but because of the deterioration in supply.

In the average annual results, summarised in the national accounts, the events of the autumn were mainly reflected in the national product, the increase in which, at 5.0 per cent in real terms, was one point below that in 1968, despite the opposite results of the harvests in the two years, which were down in 1968 and up in 1969; thus, if only non-agricultural activities are considered, the discrepancy is greater. In particular, gross manufacturing output, which contributes practically one-third to the formation of the gross domestic product, increased, still at constant prices, by 4.0 per cent, that is, less than half as much as in 1968.

Furthermore, the implicit price deflators for the national product, which in the last three years and especially in 1968 had shown only moderate increases, rose by 4.0 per cent, reflecting the development of strong inflationary pressures.

On the demand side, in the middle of the year the rise in domestic demand quickened as compared with the small increases of the preceding year, falling into line again with the trend of expansion both for consumption and for investment (Table 1). The composition of the

AGGREGATE DEMAND AND SUPPLY
(Percentage yearly changes)

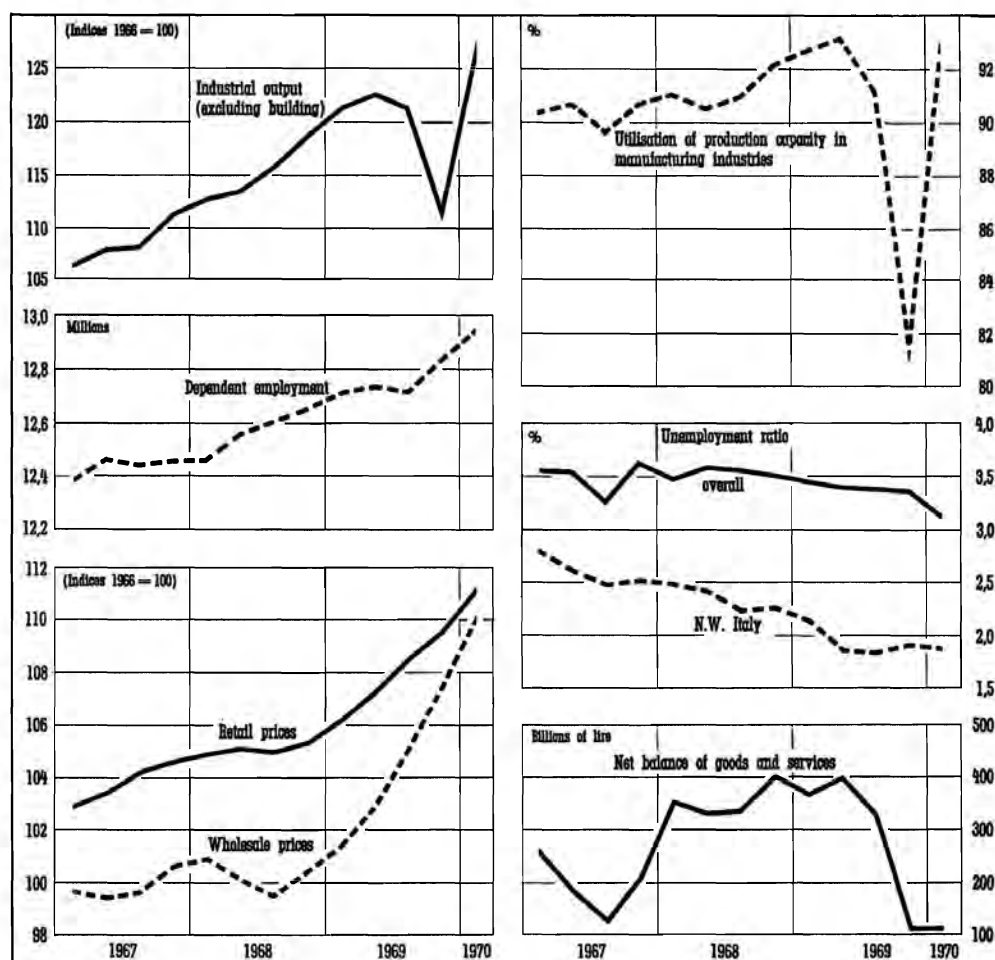
TABLE 1

I t e m s	at current prices		at 1963 prices		implicit prices	
	1968	1969	1968	1969	1968	1969
Demand:						
Consumption	6.7	8.7	4.6	5.3	2.0	3.2
Gross investment	4.4	14.7	3.3	7.9	1.1	6.3
Domestic demand	6.2	9.9	4.3	5.8	1.8	3.9
Exports of goods and services	14.5	15.6	15.4	14.1	- 0.8	1.3
Aggregate demand	7.5	10.9	6.2	7.4	1.2	3.3
Supply:						
Gross national product	7.6	9.2	6.0	5.0	1.5	4.0
Imports of goods and services . . .	7.0	21.3	7.5	20.7	- 0.5	0.5

Source: Report on the Economic Situation in Italy.

additional overall demand, although exports had again increased substantially, thus shifted towards values closer to the medium-term trend. On the supply side, the share of imports increased.

CHART 4



Trends of certain economic indicators

Notes: Seasonally adjusted figures, except in the case of prices. The figures refer: to quarterly averages for productive capacity, prices and the balance of goods and services; to the Istat quarterly surveys for employment and unemployment.

The economic indicators for the first months of 1970, with their sometimes contrasting results, show the difficulties of returning to a more normal situation. The disputes of the autumn, ended by negotiations at national level, left after-effects at factory level, where it was often not found possible to achieve a level of activity corresponding to the volume of outstanding orders, so that the recovery fell short of expectations. Subsequently further disputes arose for the renewal of

contracts in other major industrial sectors, such as textiles and electrical engineering, with strikes mainly in March and April.

Industrial output in the first quarter of 1970 was 5 per cent higher than in the same period of 1969 and in March, seasonally adjusted, only 2 per cent above the peak reached in July, 1969. On the other hand, while this was reflected in the degree of utilisation of plant capacity, which returned to the earlier maximum, on the employment side the January survey showed a large increase in the number of wage and salary earners in all non-agricultural sectors and an appreciable reduction in the overall rate of unemployment, which fell to its lowest levels since 1963-1964 (Chart 4).

Other signs of tension continued to appear in prices, the rise in which subsequently speeded up, especially in the case of wholesale prices, and in the balance of payments, where, owing to the unsatisfactory recovery in exports and the increase in imports, the balance on current account showed no improvement after the contraction of the last quarter of 1969.

Disposable income of households, and private consumption. — The disposable income of households increased in 1969 by 10.4 per cent, a considerably larger rise than in the preceding year; this was due both to the larger increase in incomes of the factors of production and to the active policy of redistribution pursued by the public authorities, reflected in an increase in transfers of 16.1 per cent, against 13.8 in 1968. Furthermore, the net burden of fiscal and parafiscal charges was reduced.

In terms of purchasing power, despite the reabsorption caused by the increase in retail prices for goods and services, the available income of households rose by 7.3 per cent, against 5.7 per cent in 1968, unlike the national product, which, as has been seen, increased more slowly in real terms.

The increase in households' available income was not accompanied by a similar rise in consumption; both average and marginal propensity to consume decreased, leading to a growth in savings formation, which went up by 19.5 per cent.

Nevertheless, private consumption still increased by 8.8 per cent in monetary terms, against 6.3 per cent in 1968, and in real terms by 5.7

per cent, equal to the average rate for the period in question, against 4.7 per cent in the preceding year (Table 2).

As regards the trend of the main items of expenditure, purchases of durable goods again showed only a limited increase in 1969.

TOTAL PRIVATE CONSUMPTION

TABLE 2

Items	Billions of lire (at current prices)	Percentage changes				Percentage breakdown		
		at current prices		at 1963 prices		(at current prices)		
		1968	1969	1968	1969	1967	1968	1969
		1967	1968	1967	1968			
Food and drink	13,393	4.0	7.7	3.7	4.9	42.4	41.5	41.0
Clothing and other personal items	3,312	5.7	6.4	4.5	3.9	10.5	10.4	10.1
Rent, fuel and electricity	4,396	9.1	10.2	3.9	6.4	13.0	13.3	13.6
Household durables:								
Furniture, fittings, appliances and serv-								
ices	1,860	8.4	6.6	6.4	3.8	5.7	5.8	5.7
Radio, television and other recreational								
facilities	567	1.7	3.1	2.3	2.4	1.9	1.8	1.7
Private means of transport								
Purchase	886	2.5	6.1	2.9	6.3	2.9	2.8	2.7
Use	1,546	12.1	19.0	9.7	14.4	4.1	4.3	4.7
Hygiene and health	2,597	9.1	11.8	6.5	7.9	7.5	7.7	8.0
Transport and communication	958	5.9	7.4	2.4	5.7	3.0	3.0	2.9
Hotels and public houses	1,005	6.2	10.1	4.2	6.7	3.0	3.0	3.1
Entertainment	1,437	7.7	11.7	4.9	7.8	4.2	4.3	4.4
Miscellaneous expenditure	1,418	7.1	6.5	6.2	3.8	4.4	4.5	4.3
Private domestic consumption	33,375	6.1	8.7	4.5	5.7	102.6	102.4	102.2
Residents' expenditure abroad	343	25.6	29.4	18.6	21.9	0.7	0.9	1.1
less: non-residents' expenditure in Italy	1,077	3.3	10.5	1.7	7.6	3.3	3.3	3.3
Private national consumption	32,641	6.3	8.8	4.7	5.7	100.0	100.0	100.0

Source: Report on the Economic Situation in Italy.

On the other hand, expenditure on the use of private vehicles continued to rise strongly, indicating a considerable degree of inelasticity in relation to prices, which had risen substantially.

Lastly expenditure on housing increased further as a proportion of total private consumption, again owing to the monetary component, which, however, rose less than in the preceding year owing to the measure freezing rents.

Investment and saving.— The revival of fixed investment, which started in the second half of 1968, continued throughout the greater part of 1969 but was subsequently affected by the events of the autumn, which slowed down the completion of work in progress and postponed the starting of new projects. The year's results at constant prices show that their increase was practically the same as in the preceding year (8.2 per cent as against 7.7 per cent) (Table 3); the discrepancy is larger in terms of current prices (15.0 against 10.1 per cent) because the implicit prices, which were practically stable in 1968, rose considerably, mainly owing to building, as a result of the tensions induced by its vigorous expansion.

TABLE 3

GROSS INVESTMENT

Type of investment	Billions of lire (at current prices)		Percentage changes				Percentage breakdown (at current prices)	
			at current prices		at 1963 prices			
	1968	1969	1968	1969	1968	1969	1968	1969
	by sectors of use							
DIRECTLY PRODUCTIVE INVESTMENT	4,770	5,359	8.1	12.3	6.2	7.1	52.0	50.8
Agriculture	682	684	10.4	0.3	7.8	- 3.4	7.4	6.5
Industry	2,410	2,767	5.9	14.8	3.8	8.9	26.3	26.2
Other sectors	1,678	1,908	10.5	13.7	9.1	8.7	18.3	18.1
SOCIAL INVESTMENT	4,395	5,184	12.3	18.0	9.5	9.4	48.0	49.2
Dwellings (1)	2,901	3,713	15.3	28.0	12.0	17.4	31.7	35.2
Other sectors	1,494	1,471	7.0	- 1.5	4.9	- 6.8	16.3	14.0
GROSS FIXED INVESTMENT	9,165	10,543	10.1	15.0	7.7	8.2	100.0	100.0
	by type of goods							
Buildings	5,909	7,078	12.4	19.8	9.3	10.7	64.4	67.2
Residential (1)	2,999	3,846	15.3	28.2	11.9	17.6	32.7	36.5
Non-residential	1,780	2,138	13.4	20.1	10.1	10.7	19.4	20.3
Public works	1,130	1,094	4.0	- 3.2	1.1	- 9.2	12.3	10.4
Plant and machinery	2,296	2,472	4.2	7.7	3.0	4.7	25.1	23.4
Means of transport	960	993	11.5	3.4	11.2	2.7	10.5	9.4
GROSS FIXED INVESTMENT	9,165	10,543	10.1	15.0	7.7	8.2	100.0	100.0
Change in stocks	190	190	—	—	—	—	—	—
GROSS INVESTMENT	9,355	10,733	4.4	14.7	3.3	7.9	—	—

Source: General Report on the Economic Situation in Italy.

(1) The discrepancy between the two series is due to residential buildings not used for dwelling.

The fall in industrial output in the last months of the year also affected the change in stocks, which was the same as in 1968, in which year it had slowed down considerably; if, therefore, stocks are included in the comparison, the rate of growth of gross investment in 1969 is found to be considerably above the preceding year, being more than twice as great in quantity (7.9 against 3.3 per cent) and more than three times as great in terms of current prices (14.7 against 4.4 per cent).

The ratio of fixed investment to the gross national product rose, but is still far below what it was at the beginning of the 1960s; there is no improvement if dwellings are excluded.

The contribution of the building sector and especially residential building, to the growth in investment was in fact even greater than in 1968 and actually represented four-fifths of the increase both in value and in quantity although there was a decline in public works.

Residential building was also responsible for the rise in social investment, which declined in the other sectors except for telecommunications.

The expansion in directly productive investment, although it quickened, was affected by the reduced capital formation in agriculture. The revival of investment in industry was the most important feature; its rate more than doubled in comparison with that—admittedly very modest—in 1968 (from 5.9 per cent to 14.8 in value and from 3.8 to 8.9 in quantity), although the year's results for that sector were most affected by the events of the autumn, particularly as regards machinery and means of transport; net of depreciation allowances the improvement becomes much bigger.

Savings formation, although it continued to grow at a rate higher (11.1 per cent) than the national product, was less, in terms of the actual additional amount, than capital investment, in view of the latter's improved trend. The surplus on current transactions with foreign countries was thus reduced, but still remained high at 2.9 per cent of the national product (Table 4).

The pattern of saving, further concentrated in 1969 on the household sector, the share of which rose to 80 per cent, not only

TABLE 4

INVESTMENT AND SAVING
(in per cent of the gross national product at current prices)

Items	1961	1962	1963	1964	1965	1966	1967	1968	1969
Gross investment	24.9	25.0	24.9	22.3	19.6	19.3	20.4	19.8	20.9
Net investment	16.4	16.6	16.6	13.8	11.1	10.8	12.2	11.7	12.6
Current account balance . .	1.3	0.7	- 1.4	1.2	3.8	3.4	2.4	3.5	2.9
Total net saving . . .	17.7	17.3	15.2	15.0	14.9	14.2	14.6	15.2	15.5

Source: General Report on the Economic Situation in Italy.

increase the role of financial intermediaries in providing the public authorities and business with the funds they need for their investment activity, but may also restrict the launching of new projects.

Employment, productivity and the cost of labour.— In 1969 total employment declined by 1.0 per cent; for although there was an increase in the use of labour by industry and especially building, and although the flight from agriculture was on a smaller scale than the

TABLE 5

EMPLOYMENT AND DOMESTIC PRODUCT PER UNIT OF LABOUR
(Percentage yearly changes)

Year	Private sector						Whole economy
	Agriculture	Industry (1)	Building	Tertiary activities (2)		Total	
				Total	of which: Trade and services		
<i>Employment (in terms of permanently employed units)</i>							
1967	0.1	3.5	2.6	2.8	3.4	2.3	2.3
1968	- 10.2	1.1	0.3	2.1	2.5	- 1.4	- 1.1
1969	- 4.4	1.5	2.7	- 3.3	- 4.8	- 1.2	- 0.9
<i>Gross product at factor cost at 1963 prices</i>							
1967	7.5	9.4	5.7	6.6	7.2	7.4	6.8
1968	- 2.7	8.9	8.0	7.8	6.9	6.3	5.9
1969	2.5	4.3	9.6	6.1	5.9	5.0	4.7
<i>Gross product per employed person</i>							
1967	7.3	5.7	3.0	3.7	3.7	5.0	4.3
1968	8.3	7.7	7.7	5.6	4.3	7.8	7.2
1969	7.2	2.7	6.7	9.8	11.1	6.3	5.6

Source: Report on the Economic Situation in Italy.

(1) Excluding building. — (2) Excluding income from buildings.

very substantial movement in the previous year, in the tertiary activities the upward trend halted, leading to a decline, especially in trade, public houses and miscellaneous services. This did not cause any worsening of unemployment because the labour force was further reduced.

Furthermore, unlike in 1968, the number of marginally employed persons declined, so that the decrease in employment, expressed in terms of permanently employed labour units, was smaller than in the preceding year (a fall of 0.9 per cent, against one of 1.1 in 1968) (Table 5).

As a result of the foregoing and, above all, of the slowing down in national product formation due to the events of the autumn, labour productivity, measured as the gross output per employed person, failed to reach the rate of increase attained in the previous year, which was the highest in the last decade, even though it still rose at a rate faster than the medium-term trend. The development by sectors was completely

COSTS AND PRICES
(Percentage yearly changes)

TABLE 6

Year	Value added at factor cost (1963 prices)	Total employment (measured in terms of permanently employed units)	Value added per unit of labour	Wage and salary income per employee (1)	Labour cost per unit of output	Implicit price deflator for gross product at factor cost
<i>Whole system</i>						
1967	6.8	2.3	4.3	7.2	2.7	2.5
1968	5.9	- 1.1	7.2	7.9	0.6	1.9
1969	4.7	- 0.9	5.6	7.3	1.7	4.1
<i>Private sector</i>						
1967	7.4	2.3	5.0	8.7	3.5	2.8
1968	6.3	- 1.4	7.8	8.4	0.5	1.5
1969	5.0	- 1.2	6.3	7.8	1.4	4.0
<i>Manufacturing industries</i>						
1967	9.9	3.6	6.1	10.5	4.1	0.9
1968	8.9	1.0	7.8	6.8	- 0.9	0.5
1969	4.0	1.4	2.6	6.9	4.3	3.9
<i>Building industry</i>						
1967	5.7	2.6	3.0	8.6	5.5	5.4
1968	8.0	0.3	7.7	10.1	2.3	3.8
1969	9.6	2.7	6.7	4.5	- 2.1	6.5

Source: Report on the Economic Situation in Italy.

(1) Net of Government's contributions.

lacking in uniformity, having been characterised by a marked slackening in industry, except for building, and by an unprecedented rise in the tertiary sector.

The change in costs per unit of product in the private sector as a whole was much smaller than in manufacturing industry, owing to the decline not only in building but also in agriculture and tertiary activities. In the last-mentioned two sectors, although wage and salary income per employee increased as much as or more than in manufacturing industry, the rise in productivity was sufficient to absorb it almost completely (Table 6).

In the economy as a whole the increase in the unit cost of labour was slightly greater than in the private sector but still remained well below the rise in implicit price deflators per unit of output.

Implicit price deflators and distribution.— The trend of labour costs, which is only partly within the scope of independent decisions by enterprises, represents the most important component of implicit price deflators; but their final determination also depends on the movement of other incomes, some of which, such as interest, are also affected by factors outside the firm while others are subject to change depending on the behaviour of demand and the keenness of competition in the market in which the enterprises operate.

In 1969 other incomes per unit of output, viewed as a whole, showed almost the same increases as dependent labour incomes, but with certain internal differences: the components registering the largest rises were interest and dividends; net saving by enterprises and the incomes of self-employed persons and their associates increased appreciably, while rents showed a smaller rise. Movements differed, however, from sector to sector.

In industry, excluding building, the implicit price deflators rose less than in the system as a whole, although the labour cost per unit of output increased further, since the other net incomes per unit of output and probably their most variable component, saving by enterprises, declined.

Nevertheless the rise in implicit price deflators was above the medium-term trend and, in particular, in manufacturing industry reached 3.9 per cent, an amount quite unusual in that sector, so that, contrary

to what usually happens, it contributed nearly as much to the inflationary component of the domestic product as it did to the real component (Table 7).

TABLE 7

IMPLICIT PRICE DEFLATORS AND GROSS DOMESTIC PRODUCT,
BY SECTORS OF ECONOMIC ACTIVITY

Sector	Implicit price deflators (percentage change)		Contribution from individual sectors			
			to implicit price deflators in GDP		to GDP at constant prices	
	1968 1967	1969 1968	1968 1967	1969 1968	1968 1967	1969 1968
PRIVATE SECTOR	1.5	4.0	1.1	3.1	5.0	4.0
Agriculture	- 2.3	7.5	- 0.2	0.7	- 0.3	0.3
Industry	1.1	4.4	0.4	1.5	3.1	1.9
Extractive	4.1	- 2.8	—	—	0.1	—
Manufacturing	0.5	3.9	0.1	1.0	2.3	1.1
Electricity and gas	- 1.0	2.1	—	—	0.2	0.2
Total	0.5	3.5	0.1	1.0	2.6	1.3
Building	3.8	6.5	0.3	0.5	0.5	0.6
Tertiary activities	2.8	2.5	0.9	0.9	2.2	1.8
Transport and communic.	2.5	0.6	0.1	—	0.6	0.7
Trade	0.5	- 0.2	0.1	—	0.8	0.4
Banking and insurance	3.8	6.7	0.1	0.3	0.3	0.3
Miscellaneous services	3.3	4.7	0.2	0.3	0.4	0.3
Buildings	8.2	5.9	0.4	0.3	0.1	0.1
GOVERNMENT	5.0	5.2	0.5	0.6	0.3	0.2
GROSS DOMESTIC PRODUCT AT FACTOR COST	1.9	4.1	1.6	3.7	5.3	4.2
INDIRECT TAXES	- 1.3	3.6	- 0.1	0.4	0.6	0.6
GROSS DOMESTIC PRODUCT AT MARKET PRICES	1.5	4.1	1.5	4.1	5.9	4.8

Source: Report on the Economic Situation in Italy.

In the building sector, on the other hand, the sharp increase in prices, greater than in all other branches of activity except agriculture (where the rise followed a decline in 1968), was caused by the growth in other incomes per unit of output. This seems to indicate, as confirmed by the similar situation in 1965, that enterprises, when determining prices, apply a margin proportional to the increase in variable costs even when this depends solely on materials and the labour cost per unit of output has remained virtually stable.

The share of other incomes in the gross product at factor cost, which can be taken as an indicator of gross profits, was thus practically unchanged in the three major sectors of activity, but with a difference within industry between building and the other types of industrial activity.

Within the whole system, where closer analysis is possible owing to the availability of more detailed data, there is found to be, as regards other incomes, a slight decline in the proportion represented by income from enterprise in favour of households' capital; as has already been seen, this helped to raise household incomes slightly more than the national product (Table 8).

DISTRIBUTION OF INCOME

TABLE 8

I t e m s	Billions of lire	Percentage changes		Percentage breakdown		
		1968 1967	1969 1968	1967	1968	1969
Income from dependent labour (1) . . .	23,639	8.4	9.1	56.5	56.7	56.7
Domestic income	23,315	8.4	9.0	55.8	56.0	55.9
Net income from abroad	324	8.5	15.7	0.7	0.7	0.8
Social charges . . . . .	....	....	....	....	....	....
Income from enterprise	14,123	7.0	8.3	34.5	34.1	33.9
Income of the self-employed including associates and corporations' undis- tributed profits	13,219	6.9	8.6	32.2	31.8	31.7
Taxes on income and current transfers to Government	904	7.2	4.4	2.3	2.3	2.2
Households' capital income	3,993	13.4	10.7	9.0	9.4	9.6
Rents . . . . .	....	....	6.1	....	....	....
Interests . . . . .	....	....	17.0	....	....	....
Dividends . . . . .	....	....	17.3	....	....	....
Governments' capital income	1,124	5.9	14.9	2.6	2.6	2.7
less: interest on public debt	1,192	14.7	13.2	2.6	2.8	2.9
NET NATIONAL PRODUCT AT FACTOR COST	41,687	8.2	9.0	100.0	100.0	100.0

Source: General Report on the Economic Situation in Italy.
(1) Net of Government's contributions.

Production

Agriculture.— The 1969 farming season produced good results, enabling to outweigh the previous year's decline and to exceed the 1967 gross marketable product in terms of volume, although that year's

gross product figures were not quite attained owing to the marked increase in goods and services purchased (Table 9).

All sectors were affected by the expansionary trend, with minor variations between them; the largest increase was in tree crops, thanks to the good harvests of grapes and above all of olives, which more than offset the poor overall fruit crop.

TABLE 9

GROSS MARKETABLE PRODUCT AND GROSS PRODUCT OF AGRICULTURE

Items	Value at current prices 1969 (billions of lire)	Percentage changes (1)					
		value		volume		implicit price deflators	
		1968	1969	1968	1969	1968	1969
Marketable product	6,064.8	- 3.1	9.9	- 1.6	3.4	- 1.5	6.3
Field crops, including fodder	2,035.5	- 4.5	7.9	- 3.3	3.4	- 1.2	4.3
Tree crops	1,695.8	- 11.3	14.9	- 8.0	4.0	- 3.6	10.5
Animal products	2,335.8	4.9	8.4	4.8	2.9	0.1	5.3
Purchase of goods and services	1,391.5	3.6	7.5	4.1	5.7	- 0.5	1.7
Gross value added at market prices . . .	4,673.3	- 5.0	10.7	- 3.0	2.8	- 2.1	7.7

Source: Report on the Economic Situation in Italy.

(1) In comparison with previous year.

Among field crops, there was a further increase in the case of hard wheat, which is till tending to replace soft wheat in many areas; all the other main cereals showed substantial increases, as practically also did all vegetables and garden produce.

The animal products sector showed the smallest increase; it should be borne in mind, however, that this followed an already expanding trend in the preceding year.

The rise in implicit price deflators was large, the greatest in the decade, and made possible a substantial improvement in the terms of trade with the goods and services employed, with favourable effects on farm incomes, both in absolute terms and, still more, per capita, owing to the continued reduction of agricultural employment.

Industry.— As a result of the exceptionally large number of working hours lost, the gross industrial product at constant prices (Table 10) increased in 1969 less than half as much as in 1968 (4.3 against 8.9 per cent). If we include the building sector, which, on the

TABLE 10

VALUE ADDED OF INDUSTRIAL ACTIVITY AT FACTOR COST

I t e m s	Valute at constant prices in billions of lire			Per-centage break-down 1969	Percentage changes		
	1967	1968	1969		1967/1966	1968/1967	1969/1968
GROSS PRODUCT:							
including building	13,191	14,343	15,083	100.0	8.7	8.7	5.2
excluding building	10,954	11,927	12,434	82.4	9.4	8.9	4.3
Industries: Extractive	246	261	280	1.8	2.9	6.1	7.3
Manufacturing	9,770	10,639	11,065	73.4	9.9	8.9	4.0
Electricity, gas, water	938	1,027	1,089	7.2	5.6	9.5	6.0
Building	2,237	2,416	2,649	17.6	5.7	8.0	9.6

Source: Report on the Economic Situation in Italy.

other hand, increased its rate of growth between the two years, the discrepancy is smaller (5.2 against 8.7 per cent).

The slowing down was attributable to manufacturing output and, to a smaller extent, to output of electricity and gas; the extractive industries, on the other hand, showed an improvement.

As has already been mentioned, the overall picture for the year was strongly influenced by the losses of production in the last four months. For in January-August the rate of increase in industrial activity was about two points above the previous year, being almost doubled in the case of consumer goods, higher for capital goods and lower for producer goods (Table 11).

In the consumer goods group, the trend of domestic demand for motor vehicles was also favourable; annual output, on the other hand fell (4.7 per cent), while both exports and imports increased. The increase of the incidence of these two trade flows on output and registrations had already been observable in the first eight months of the year; in that period practically 90 per cent of the increase in motor vehicle output had been allocated on the international markets, while 84 per cent of the increase in the registrations were for vehicles of foreign make.

In the capital goods group, the events of the autumn widened the gap between the growing domestic demand for iron and steel products and the structurally limited possibilities of supply; the balance of trade

with foreign countries, practically in equilibrium in 1968, was negative to the extent of 149 billion in 1969 as a result of changes of opposite sign in the two flows of trade—a marked increase in imports (46.7 per cent) and a reduction in sales abroad (2.6 per cent).

TABLE 11
PERCENTAGE CHANGES IN INDICES OF INDUSTRIAL PRODUCTION (1)

Sectors	Corrected indices				Corrected and adjusted indices		
	Changes in relation to the same period in the preceding year				Changes in relation to the immediately preceding period		
	1968	1969			1969		
		Year	Jan.-Aug.	Sept.-Dec.	1st qtr.	2nd qtr.	3rd qtr.
GENERAL INDEX (excluding building)	6.3	3.3	8.0	— 5.4	2.5	1.0	— 8.6
Producer goods	8.9	2.6	7.1	— 5.9	1.2	2.7	— 8.8
<i>of which:</i>							
Chemical	11.4	— 0.9	5.7	— 13.8	— 0.7	3.3	— 14.7
Petroleum derivatives	9.8	10.9	13.5	6.6	5.1	6.1	— 4.3
Electricity	8.0	6.0	8.5	1.3	2.2	2.5	— 3.3
Capital goods	7.0	1.6	8.2	— 10.9	2.1	1.1	— 13.5
<i>of which:</i>							
Building materials	13.3	3.1	5.8	— 2.0	0.5	— 2.0	— 0.5
Iron and steel goods	8.5	— 0.2	8.5	— 16.5	3.0	0.2	— 19.2
Non-ferrous metals	13.1	5.2	10.7	— 4.6	2.2	4.3	— 10.5
Machinery (excluding electrical domestic appliances)	4.0	0.7	8.3	— 12.8	1.6	4.1	— 17.5
Industrial vehicles	19.8	— 2.2	16.8	— 34.9	5.6	— 4.6	— 35.5
Consumer goods	4.5	5.3	8.3	—	3.6	0.1	— 3.7
<i>of which:</i>							
Foodstuffs	5.0	4.3	6.8	1.7	2.0	— 0.4	0.2
Textiles	— 0.2	6.9	6.3	7.8	4.2	2.2	1.0
Footwear	14.2	2.0	5.1	— 4.2	— 2.7	1.7	— 3.5
Clothing	— 3.5	3.9	5.1	1.9	3.3	— 2.1	0.6
Furniture	8.1	7.1	9.1	5.7	0.9	3.3	1.5
Electrical domestic appliances	7.0	3.9	15.8	— 16.9	8.8	3.5	— 25.9
Motor vehicles (2)	9.0	— 4.7	7.9	— 28.4	4.9	— 14.1	— 18.6
Artificial and synthetic textile fibres	16.1	12.6	15.1	7.8	5.6	6.8	— 4.1

(1) Istat Indices, the annual changes in which differ from those given in Table 10 on the basis of the value added of industrial activity at factor cost. The correction for months with an equal number of working days and the adjustment for seasonal changes were made by the Bank of Italy.— (2) Motor vehicles are included partly under capital goods and partly under consumer goods.

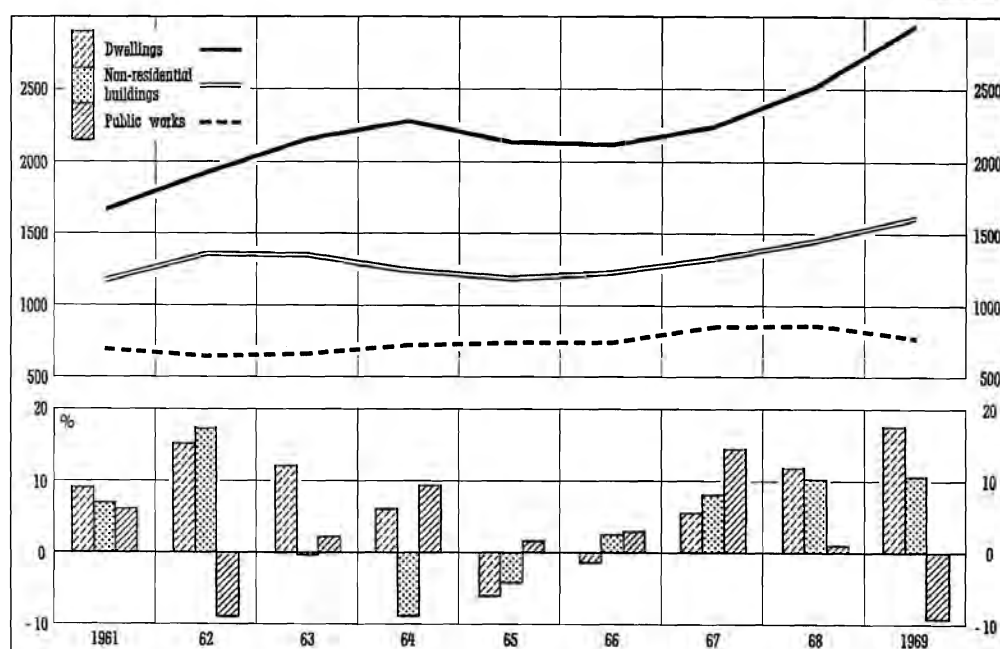
In the sector of producer goods, processing of crude petroleum increased by 10.9 per cent (13.5 per cent in the first eight months). The increased refinery activity was attributable to growing domestic

consumption of fuel oil, gas oil and petrol and to the larger volume of exports of petroleum products.

The building boom continued in 1969, though slackening in the latter part of the year, so that the increase between the last quarter of 1968 and the corresponding period of 1969 was 7.5 per cent, i.e. less than the average rise for the year (9.6 per cent).

Dwellings contributed even more than in 1968 to the increase in building activity (17.6 per cent); non-residential buildings rose by 10.7 per cent, while public works fell by 9.2 per cent (Chart 5).

CHART 5



Gross fixed investment in building
(billions of lire at constant prices)

Source: Report on the Economic Situation in Italy.

Employment and wages.

The absorption of labour by industry continued at a quickening pace in 1969; in the other sectors, however, employment fell, this movement being in line with the trend in the case of agriculture and contrary to the tendency of the last few years in tertiary activities. The final effect was a decline in overall demand for labour (1.0 per cent lower than in 1968) (Table 12).

TABLE 12

EMPLOYMENT

(Changes in thousands by comparison with the previous year)

Sectors	1967		1968		1969		1969 Number (thou- sands of units)
	Jobs	Labour supply	Jobs	Labour supply	Jobs	Labour supply	
Industry (excluding building) .	128		114		104		6,072
Building	33		- 6		54		1,976
Agriculture	- 104		- 309		- 224		4,023
Services	166		163		- 132		6,800
Unemployment (increase -) . .		80		- 5		31	663
Domestic labour force (in- crease -)		38		- 67		- 222	19,534
Workers abroad (increase -) .		105		34		- 7	264
Total . . .	223	223	- 38	- 38	- 198	- 198	

Prepared by the Bank of Italy from Istat data. The yearly figures shown in this and subsequent tables are the arithmetic mean of the four figures found annually by Istat.

In industry 158,000 jobs were created, of which about one-third were in building; the contribution of this sector, very marked in the early part of the year and practically down to nil in the latter part, was responsible for the quickening of activity recorded in the whole sector; for in the other branches of industry, taken as a whole, the additional demand for labour was practically the same as in the preceding year.

The unused part of the labour supply, that is, the total number unemployed, declined both in absolute terms and in relation to the labour force, the unemployment ratio having fallen to 3.4 per cent, from 3.5 in 1968. This trend became more pronounced during the year and was accentuated at the beginning of 1970; this applied only to the unemployed, the number of which declined for both sexes and for all sectors of economic activity except services; for young people seeking first employment, on the other hand, there was an increase, as there had been for many years, although it was smaller than in 1968.

In 1969, unlike in the preceding year, trade union activity was very intense owing to the larger number of contracts falling due for renewal, which moreover related to sectors characterised by a high level of employment. Altogether about 5 million workers were affected

by the renewals, including 3 million in industry, representing nearly fifty per cent of wage and salary earners.

The negotiations, which were concentrated in the second half of the year, a few months in advance of the expiry of the contracts, gave rise to particularly bitter labour conflicts, with a loss of about 300 million working hours, mainly in the last four months; furthermore, the nature of the strikes was such as to cause declines in production more than proportional to the reduction in hours worked.

In the manufacturing sector the most important agreement was reached in the metal-working and mechanical engineering sector, both owing to the number of persons affected, about 1,300,000 for public and private enterprises combined, and owing to the extent of the improvements. From the economic point of view, the new contract, which includes also important innovations as regards the new norms introduced, entails overall burdens for enterprises which are difficult to define in terms of quantity and greater than the increase in the monetary earnings of workers; furthermore, their distribution over the three-year period of validity of the contract provides for a marked concentration in the first year, from the beginning of which the whole of the improvements in contractual wages becomes payable. As regards the norms introduced, provision is made, among other things, for the gradual reduction of working hours down to 40 hours a week. Practically the same benefits were granted in the chemical-pharmaceutical branch, involving 220,000 employees.

The speeding-up of the rate of increase in minimum contractual wages in 1969 affected all sectors of activity, and especially agriculture and industry (Table 13). Contributory factors were the jump of 6 points in the sliding scale, the first phase of the abolition of the zonal basis of assessment and the improvements granted by firms or at province level. No effect was produced, on the other hand, except in the case of the chemical industry and quarrying by the contractual renewals which took place towards the end of the year, since these only became applicable from 1 st January 1970.

The rise in wages accelerated appreciably in the first two quarters, during which the demand for labour was more expansionary and some strain on the supply side developed in the more industrialised areas;

GROSS MINIMUM CONTRACTUAL WAGES (1)
(percentage changes)

TABLE 13

Sectors	1968 1967	1969 1968	Dec. 68 Dec. 67	Dec. 69 Dec. 68	Feb. 70 Feb. 69	Feb. 70 Dec. 69
<i>Wages</i>						
Agriculture	5.1	10.8	3.8	14.9	17.2	5.7
Industry	3.9	7.3	3.4	9.9	21.6	13.2
Extractive	4.1	8.9	3.4	18.9	20.6	2.1
Building	4.3	6.9	3.6	8.2	21.2	16.2
Manufacturing	3.6	7.5	3.2	10.9	22.3	12.1
of which: textiles	5.7	5.9	3.7	7.7	8.8	1.7
metals and eng.	1.9	6.3	2.4	7.6	32.0	23.7
chemicals	2.6	6.7	2.4	27.7	34.3	5.8
Electricity and gas	5.1	3.6	5.2	3.7	8.4	5.0
Trade	4.8	5.2	5.4	5.9	10.2	5.9
Transport	3.5	5.1	3.5	8.5	14.0	6.0
<i>Salaries</i>						
Industry	3.0	5.2	2.4	8.1	14.8	7.8
Trade	4.5	5.5	5.3	5.9	9.5	5.3
Public administration	3.1	3.6	3.6	5.3	5.0	0.8

Source: Istat.

(1) Excluding family allowances.

however, supply still remained high in the subsequent period, as is shown by the trend of both contractual wages and actual earnings (Table 14).

EARNINGS IN INDUSTRY (1)
(percentage changes)

TABLE 14

Sectors	1968(2) 1967(2)	1969(2) 1968(2)	3rd qtr 1968 3rd qtr 1967	3rd qtr 1969 3rd qtr 1968
Industry as a whole (including building) . .	4.3	8.8	5.2	10.3
Manufacturing industry	4.5	9.1	5.1	11.3
of which: food	5.1	11.3	4.9	15.4
textiles	6.0	8.6	4.7	13.2
metals and engineering	3.2	9.0	4.0	11.1
chemicals	3.1	10.4	3.9	12.8
Building	4.5	7.2	4.3	9.1

(1) Excluding family allowances and other fringe benefits. Industries surveyed by the Ministry of Labour and Social Security.— (2) Average for the first three quarters.

A comparison of their trends shows that, unlike what happened in 1968, the wage drift gradually slackened in the first three quarters of the year, especially in the metals and engineering and foodstuffs sectors.

Prices

The upward trend of prices, which had started in the second half of 1968 after a long period of stability, continued and became more marked in 1969: at the end of the year the level of wholesale prices was up by 7.3 per cent, a greater rise than the yearly average increase (3.9 per cent), owing to the different trends in the two years (Table 15).

TABLE 15

DOMESTIC WHOLESALE PRICES

(percentage changes in indices; 1966 = 100)

Indices	1968 1967	1969 1968	Dec. 68 Dec. 67	Dec. 69 Dec. 68	Apr. 69 Dec. 68	Dec. 69 Apr. 69	Mar. 70 Dec. 69
<i>Istat</i>							
General index	0.4	3.9	0.1	7.3	1.3	6.0	2.5
Classification by origin:							
Agricultural	1.8	5.9	1.8	7.4	2.2	5.1	2.2
Non-agricultural	—	3.5	- 0.3	7.4	1.1	6.2	2.5
Product classification (1):							
Foodstuffs	0.5	4.9	1.4	6.8	1.5	5.3	1.8
Vegetable	3.2	4.4	- 1.7	9.1	5.3	3.6	3.8
Animal	- 0.1	9.0	8.2	5.9	- 3.1	9.3	- 0.5
Food Manufactures	- 1.2	3.7	1.0	5.7	0.6	5.0	1.2
Industrial raw materials and manufactures	0.2	3.4	- 0.5	7.5	1.2	6.3	2.9
Raw Materials	- 0.6	9.0	- 0.5	16.4	3.1	12.9	1.3
Manufactures	—	2.9	- 0.2	6.5	1.2	5.3	3.0
Classification by use:							
Consumer goods	- 0.2	3.9	0.5	6.5	1.5	4.9	1.7
Capital goods	1.3	6.6	1.0	12.5	1.9	10.4	5.0
Producer goods	1.3	- 2.5	- 3.6	0.3	- 1.8	2.2	0.3
<i>Milan Chamber of Commerce</i>							
General index:	- 0.1	4.9	0.8	10.1	1.0	9.0	1.0
Foodstuffs	- 1.3	5.0	3.3	4.3	- 0.9	5.3	0.8
Industrial raw materials . . .	0.3	4.8	- 0.3	12.6	1.8	10.6	1.2

(1) Istat figures reworked by the Bank of Italy. The index for industrial raw material prices does not include construction timber, lignite, crude petroleum and quarrying products, these being included in the overall index for industrial raw materials and manufactures.

The upward trend affected both agricultural products and non-agricultural products, being mainly due, in the case of the former, to limitations in supply, and in the case of the latter, to rises in costs which were reflected in the price level owing to the fact that domestic demand was brisker than in the previous year, although still remaining within the limits of the medium-term trend.

TABLE 16

RETAIL PRICES AND COST OF LIVING

(percentage changes in indices; 1966 = 100)

Indices	1968 1967	1969 1968	Dec. 68 Dec. 67	Dec. 69 Dec. 68	Apr. 69 Dec. 68	Dec. 69 Apr. 69	Mar. 70 Dec. 69
RETAIL PRICES							
General index	1.4	2.7	1.0	4.2	1.2	2.9	1.6
Food products	0.3	2.8	0.7	3.8	1.1	2.7	1.4
Non-food products and services	2.1	2.5	1.3	4.4	1.3	3.1	1.8
Clothing	1.3	2.4	1.2	4.7	0.8	3.9	1.8
Hygiene and health	2.5	2.3	1.7	2.9	1.5	1.4	1.2
Durables and non-durables (1)	1.9	3.0	2.2	6.1	0.6	5.4	2.1
Electricity and gas	- 1.2	- 2.2	- 5.6	3.2	1.3	1.9	1.2
Housing	4.2	4.5	4.7	4.7	1.8	2.8	3.1
Transport and communications	1.8	2.3	0.4	3.5	1.9	1.6	1.9
Recreational and cultural goods and services	3.3	3.3	1.4	5.9	1.0	4.8	0.8
Other goods and services	2.0	2.9	1.9	4.8	1.1	3.7	2.3
Non-food products	0.8	1.8	- 0.1	4.5	1.1	3.4	1.5
Services	3.5	3.3	2.8	4.5	1.5	2.9	2.0
COST OF LIVING							
General index	1.3	2.8	1.4	4.3	1.2	3.1	1.6
Food	0.4	2.7	1.1	3.7	0.8	2.9	1.5
Clothing	1.9	2.9	1.6	5.9	1.0	4.9	1.6
Electricity and fuels	- 0.6	—	- 3.0	4.8	0.7	4.1	2.0
Housing	4.7	5.3	5.4	5.5	2.7	2.7	2.6
Miscellaneous expenditure	1.9	2.6	1.3	4.1	1.3	2.7	1.5

Source: Istat.

(1) For domestic use, and services connected with housing.

Consumer prices rose less than wholesale prices both on an yearly average basis (2.7 against 3.7 per cent) and during 1969 (4.2 and 7.3 per cent respectively); this tendency continued in the first quarter of 1970 (Table 16).

The difference between the two rates, which had been of opposite sign in the previous years, became apparent towards the end of 1968 and increased in the following twelve months, during which the rate of increase of retail prices nearly always remained below that of wholesale prices. This is mainly explained by the difference in composition of the two indices, the former of which, as is well known, does not include the prices for raw materials and manufactured products used in building, that is, two groups of goods which showed the largest rises.

Balance of payments.

General trends.— As a result of a large increase in the net capital outflow and a small contraction in the current account surplus, Italy's balance of payments in 1969 showed an overall deficit of 1,391 million dollars. The repercussions on the foreign position of the central monetary institutions were reduced by the movements of bank funds: for the banks restored equilibrium in their foreign accounts, in accordance with the regulations introduced in March 1969 (Table 17).

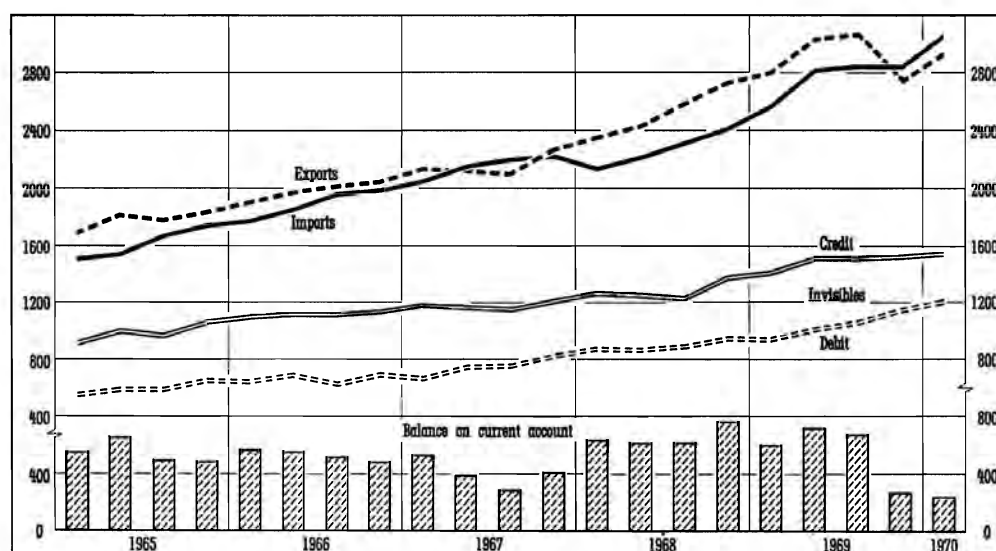
The deterioration in respect of capital movements was more accentuated in the second and third quarters, when conditions were disturbed by, among other things, the events affecting the German mark; the overall net outflow of funds reached 3,432 million, against 1,691 million in 1968.

The current account surplus, seasonally adjusted, remained during the first three quarters at levels a little above the averages for 1968, mainly owing to the larger contribution of services and unilateral transfers. In the last quarter, while the surplus in respect of invisibles was reduced, the trade balance deteriorated appreciably owing to the contraction in exports (11 per cent), which in turn was chiefly attributable to the many working days lost through strikes in major sectors of Italian industry. In the year as a whole the current account surplus amounted to 2,369 million, 258 million less than in 1968 (Chart 6).

With regard to Italy's relations with the different geographical areas, the current account surplus with the developed countries declined to 2,459 million from 2,699 million in 1968; the contraction did not

affect the United States, the trade balance with that country having improved, unlike what happened with all the other areas, especially the EEC. The largest capital outflow to developed countries was to the « other OECD countries », a statistical group including Switzerland,

CHART 6



Balance on current account

Current account of the balance of payments

(Quarterly figures in millions of dollars, seasonally adjusted)

which, as it is well known, is the source of practically all remittances of bank-notes (Table 18).

The balance of payments with developing countries was particularly affected by the large imports of raw materials and the more modest growth in exports, causing a trade deficit which was almost entirely reflected in the balance on current account, which closed with a deficit of 91 million dollars (against a surplus of the same size in 1968); the net outflow of capital to this group of countries was also larger than in the previous year (459 against 297 million). This was reflected in a substantial increase in the financial resources provided to developing areas, with a rise, in particular, in long-term trade loans and credits.

In relation to the socialist countries, while the approximate equilibrium on current account recorded in 1968 was repeated in the year under review, capital movements resulted in a larger net outflow, attributable to the granting of financial credits connected with exports.

GLOBAL BALANCE

(in million)

SECTION 1

Items	Credit		Debit		Balance	
	1968	1969	1968	1969	1968	1969
Goods and services	14,589.9	16,869.4	12,302.6	14,913.3	2,287.3	1,956.1
1. Merchandise (fob)	10,097.7	11,642.4	9,049.9	11,058.4	1,047.8	584.0
2. Freight and insurance	611.5	647.0	977.9	1,059.1	- 366.4	- 412.1
2.1 Freight	600.0	635.0	961.9	1,038.6	- 361.9	- 403.6
2.2 Insurance	11.5	12.0	16.0	20.5	- 4.5	- 8.5
3. Other transportation	544.5	595.0	388.0	410.0	156.5	185.0
3.1 Passenger fares	275.0	315.0	63.0	70.0	212.0	245.0
3.2 Other	269.5	280.0	325.0	340.0	- 55.5	- 60.0
4. Travel	1,475.7	1,632.3	363.3	493.1	1,112.4	1,139.2
5. Investment income	455.7	706.9	422.4	601.4	33.3	105.5
6. Government services and transactions	116.5	126.2	108.7	100.0	7.8	26.2
6.1 Military transactions	69.1	73.4	—	—	69.1	73.4
6.2 Other transactions	47.4	52.8	108.7	100.0	- 61.3	- 47.2
7. Other services	1,288.3	1,519.6	992.4	1,191.3	295.9	328.3
7.1 Workers' earnings	520.2	578.4	71.6	59.6	448.6	518.8
7.2 Other	768.1	941.2	920.8	1,131.7	- 152.7	- 190.5
Transfers payments	619.7	686.0	280.1	273.6	339.6	412.4
8. Private transfers	561.5	595.3	73.2	87.1	488.3	508.2
8.1 Emigrants' remittances	401.0	426.2	—	—	401.0	426.2
8.2 Other grants	160.5	169.1	73.2	87.1	87.3	82.0
9. Public transfers	58.2	90.7	206.9	186.5	- 148.7	- 95.8
9.1 Reparations	—	—	6.7	20.6	- 6.7	- 20.6
9.2 Miscellaneous contributions	48.4	85.5	200.2	165.9	- 151.8	- 80.4
9.3 Grants	9.8	5.2	—	—	9.8	5.2
Total . . .	15,209.6	17,555.4	12,582.7	15,186.9	2,626.9	2,368.5

OF PAYMENTS SUMMARY

of dollars)

TABLE 17

SECTION II

Items	ASSETS						LIABILITIES					
	Credit		Debit		Balance		Credit		Debit		Balance	
	1968	1969	1968	1969	1968	1969	1968	1969	1968	1969	1968	1969
Capital movements	1,006.7	952.0	3,159.0	4,819.2	- 2,152.3	- 3,867.2	1,596.2	1,778.8	1,134.6	1,343.6	461.6	435.2
10. Private long-term	970.7	914.7	1,874.2	2,444.6	- 903.5	- 1,529.9	1,486.2	1,655.6	1,082.0	1,273.1	404.2	382.5
10.1 Direct investments . . .	116.5	102.4	377.7	385.7	- 261.2	- 283.3	412.1	559.1	80.3	140.7	331.8	418.4
10.2 Portfolio investments . .	112.0	156.2	391.0	617.2	- 279.0	- 461.0	393.2	592.8	343.5	618.0	49.7	- 25.2
10.3 Other	1.3	0.9	1.1	2.6	0.2	1.7	43.1	42.9	23.0	20.1	20.1	22.8
10.4 Loans	178.5	51.0	263.1	517.5	- 84.6	- 466.5	329.1	318.5	265.5	195.0	63.6	123.5
10.5 Long-term trade credits	562.4	604.2	581.4	705.2	- 19.0	- 101.0	308.7	130.8	267.7	299.3	41.0	- 168.5
10.6 Short-term trade credits	—	—	259.9	216.4	- 259.9	- 216.4	—	11.5	102.0	—	- 102.0	11.5
11. Repatriation of Italian bank- notes	—	—	1,127.3	2,255.9	- 1,127.3	- 2,255.9	—	—	—	—	—	—
12. Local government	—	—	—	—	—	—	—	—	4.9	—	- 4.9	—
13. Central Government	36.0	37.3	157.5	118.7	- 121.5	- 81.4	110.0	123.2	52.6	65.6	57.4	57.6
13.1 Long-term loans	36.0	37.3	155.5	118.7	- 119.5	- 81.4	110.0	123.2	52.6	65.6	57.4	57.6
13.2 Other long-term assets and liabilities	—	—	2.0	—	- 2.0	—	—	—	—	—	—	—
Monetary movements	1,586.7	846.7	3,064.6	2,376.5	- 1,477.9	- 1,529.8	941.4	2,969.4	90.8	48.4	850.6	2,921.0
14. Central monetary institutions	1,353.4	693.2	1,267.8	143.2	85.6	550.0	1.4	156.2	26.2	1.6	- 24.8	154.6
14.1 Accounts with IMF . .	133.3	31.5	—	—	133.3	31.5	—	—	—	—	—	—
14.2 Gold	—	—	523.4	32.6	- 523.4	- 32.6	—	—	—	—	—	—
14.3 Other reserves	1,189.3	139.0	414.6	110.6	774.7	28.4	—	—	—	—	—	—
14.4 Liabilities to official in- stitutions	—	—	—	—	—	—	1.4	156.2	26.2	1.6	- 24.8	154.6
14.5 Other foreign assets and liabilities	30.8	522.7	329.8	—	- 299.0	522.7	—	—	—	—	—	—
15. Banks	233.3	153.5	1,796.8	2,233.3	- 1,563.5	- 2,079.8	940.0	2,813.2	64.6	46.8	875.4	2,766.4
15.1 Foreign assets	233.3	153.5	1,796.8	2,233.3	- 1,563.5	- 2,079.8	—	—	—	—	—	—
15.2 Foreign liabilities	—	—	—	—	—	—	940.0	2,813.2	64.6	46.8	875.4	2,766.4

SECTION III

Items	Credit		Debit		Balance	
	1968	1969	1968	1969	1968	1969
Current account	15,209.6	17,555.4	12,582.7	15,186.9	2,626.9	2,368.5
Capital movements	2,602.9	2,730.8	4,293.6	6,162.8	- 1,690.7	- 3,432.0
Errors and omissions	—	—	308.9	327.7	- 308.9	- 327.7
Total . . .	17,812.5	20,286.2	17,185.2	21,677.4	627.3	- 1,391.2
Monetary movements	2,528.1	3,816.1	3,155.4	2,424.9	- 627.3	1,391.2

REGIONAL BALANCE
(in million)

Items	Developed countries					
	United States		EEC countries		Others	
	1968	1969	1968	1969	1968	1969
Goods						
credit	1,089.3	1,272.8	4,079.0	4,983.4	1,892.2	2,025.6
debit	973.3	1,134.6	3,526.3	4,611.0	1,547.8	1,827.9
balance	116.0	138.2	552.7	372.4	344.4	197.7
SERVICES						
credit	1,166.8	1,472.5	1,234.0	1,444.8	902.2	954.8
debit	757.1	1,024.9	670.4	812.5	629.1	752.1
balance	409.7	447.6	563.6	632.3	273.1	202.7
UNILATERAL TRANSFERS						
credit	244.0	254.9	95.8	117.0	138.5	143.7
debit	22.3	26.3	9.8	10.1	7.1	10.8
balance	221.7	228.6	86.0	106.9	131.4	132.9
CURRENT ACCOUNT						
credit	2,500.1	3,000.2	5,408.8	6,545.2	2,932.9	3,124.1
debit	1,752.7	2,185.8	4,206.5	5,433.6	2,184.0	2,590.8
balance	747.4	814.4	1,202.3	1,111.6	748.9	533.3
CAPITAL MOVEMENTS						
credit	335.7	320.3	449.8	780.9	820.6	754.5
debit	387.0	385.4	448.5	846.1	1,766.7	2,985.6
balance	- 51.3	- 65.1	1.3	- 65.2	- 946.1	-2,231.1
MONETARY MOVEMENTS						
credit	1,200.0	640.8	290.4	862.9	565.8	1,634.7
debit	187.0	145.2	1,076.2	918.3	1,132.0	1,152.9
balance	1,013.0	495.6	- 785.8	- 55.4	- 566.2	481.8
ERRORS, OMISSIONS AND MULTILATERAL SETTLEMENTS	-1,709.1	-1,244.9	- 417.8	- 991.0	763.4	1,216.0

TABLE 18

OF PAYMENTS SUMMARY

of dollars)

Total		Developing countries		Socialist countries		International organisations and unclassified		T O T A L	
		1968	1969	1968	1969	1968	1969	1968	1969
7,060.5	8,281.8	2,401.4	2,588.0	612.2	724.8	23.6	47.8	10,097.7	11,642.4
6,047.4	7,573.5	2,362.1	2,734.6	566.1	679.5	74.3	70.8	9,049.9	11,058.4
1,013.1	708.3	39.3	- 146.6	46.1	45.3	- 50.7	- 23.0	1,047.8	584.0
3,303.0	3,872.1	600.0	648.5	72.5	80.0	516.7	626.4	4,492.2	5,227.0
2,056.6	2,589.5	590.7	618.5	118.2	132.0	487.2	514.9	3,252.7	3,854.9
1,246.4	1,282.6	9.3	30.0	- 45.7	- 52.0	29.5	111.5	1,239.5	1,372.1
478.3	515.6	47.0	45.1	—	—	94.4	125.3	619.7	686.0
39.2	47.2	3.9	19.8	2.9	1.1	234.1	205.5	280.1	273.6
439.1	468.4	43.1	25.3	- 2.9	- 1.1	- 139.7	- 80.2	339.6	412.4
10,841.8	12,669.5	3,048.4	3,281.6	684.7	804.8	634.7	799.5	15,209.6	17,555.4
8,143.2	10,210.2	2,956.7	3,372.9	687.2	812.6	795.6	791.2	12,582.7	15,186.9
2,698.6	2,459.3	91.7	- 91.3	- 2.5	- 7.8	- 160.9	8.3	2,626.9	2,368.5
1,606.1	1,855.7	526.6	508.4	152.3	215.5	317.9	151.2	2,602.9	2,730.8
2,602.2	4,217.1	823.4	967.4	216.0	383.2	652.0	595.1	4,293.6	6,162.8
- 996.1	-2,361.4	- 296.8	- 459.0	- 63.7	- 167.7	- 334.1	- 443.9	-1,690.7	-3,432.0
2,056.2	3,138.4	65.0	319.3	96.2	226.0	312.9	132.4	2,530.3	3,816.1
2,395.2	2,216.4	230.2	25.9	86.1	54.4	446.1	128.2	3,157.6	2,424.9
- 339.0	922.0	- 165.2	293.4	10.1	171.6	- 133.2	4.2	- 627.3	1,391.2
-1,363.5	-1,019.9	370.3	256.2	56.1	3.9	628.2	431.4	- 308.9	- 327.7

Current account.— In 1969 Italy's foreign trade was characterised by a market revival of import, which rose by 21 per cent against 5 per cent in 1968, and a slight slackening of the rate of growth of exports, which declined from 17 to 15 per cent. The deficit on merchandise account, which had been particularly small in 1968 (63 billion lire), thus rose to 450 billion, a figure close to the average level for 1965-1967 (Table 19).

The c.i.f. prices of imported goods remained on the average stationary by comparison with the 1968 levels: there was a sharp increase in the prices of ferrous and non-ferrous metals owing to the rise on the international markets for them, offset by reductions in the prices of other primary products (especially cereals, oilseeds and fruit and crude oil). In the finished goods sector the higher prices of industrial machineries were counterbalanced by the reductions for means of transport, chemical products and textiles.

With regard to export prices, there was a rise of 3 per cent, so that the increase in the volume of exports was 12 per cent; the rise in the unit value of exported goods took place mainly in the second half of the year and applied particularly to foodstuffs.

During the year there was a marked disparity in the course of Italy's foreign trade; after the sustained expansion of the first two quarters there was a slowing down in the third quarter, followed in the fourth, under the influence of the strikes, by a halt in the rise in imports and a fall in exports (Chart 7).

The large production losses were immediately reflected in smaller exports, although Italian producers tried to meet the foreign demand by drawing on stocks. The drop was substantial, as the labour disputes was concentrated in the metallurgy, mechanical engineering and chemical industries, which provide about two-thirds of our total sales abroad. On the import side the restraining effect of the strikes was less marked. It should first of all be pointed out that incoming deliveries of finished capital goods largely correspond to orders placed in advance; furthermore, in the consumer goods sector, the decline in demand was modest in extent because households were able to offset, by incurring debt and resorting to accumulated savings, the temporary reduction in incomes due to the strikes.

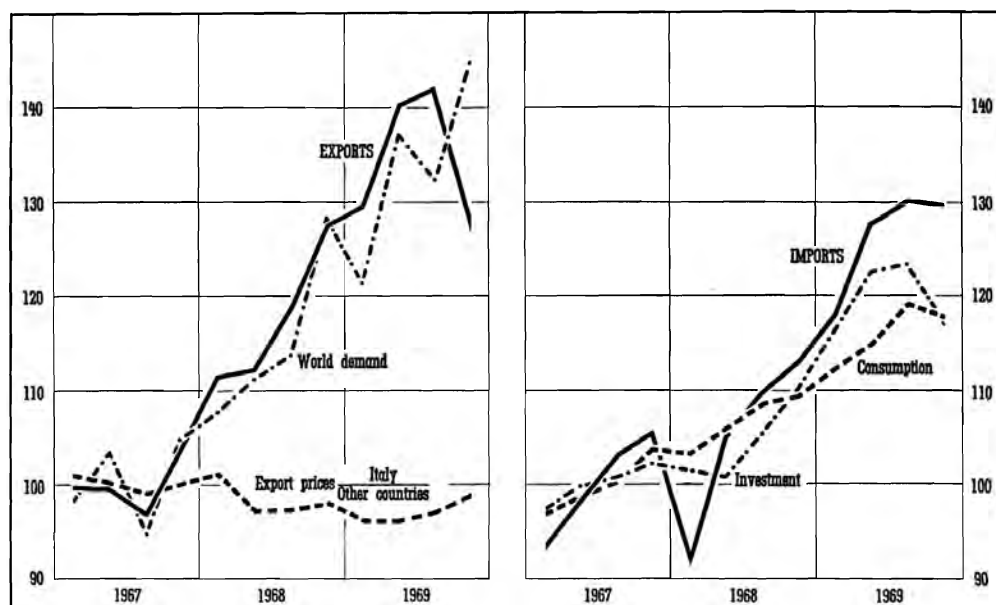
TABLE 19

ITALY'S FOREIGN TRADE
(in billions of lire)

Items	1968			1969			Percentage changes				Percentage composition	
	Exports	Imports	Balance	Exports	Imports	Balance	Exports		Imports		Exports	Imports
							1968 1967	1969 1968	1968 1967	1969 1968	1969	1969
<i>Merchandise composition</i>												
Raw materials	81.6	826.3	- 744.7	89.5	946.9	- 857.4	10.9	9.7	- 1.8	14.6	1.3	12.2
Semi-finished products	882.7	998.3	- 115.6	947.0	1,351.1	- 404.1	28.5	7.3	0.5	35.3	12.9	17.4
Consumer goods	3,040.3	2,007.1	1,033.2	3,639.3	2,450.4	1,188.9	15.9	19.7	3.6	22.1	49.6	31.5
food	547.1	1,238.1	- 691.0	631.6	1,425.7	- 794.1	- 2.8	15.4	- 1.7	15.1	8.6	18.3
other non-durables	1,273.7	315.0	958.7	1,571.3	400.6	1,170.7	22.0	23.4	9.1	27.2	21.4	5.2
durables	1,219.5	454.0	765.5	1,436.4	624.1	812.3	19.9	17.8	16.8	37.5	19.6	8.0
Capital goods	1,725.4	1,060.8	664.6	2,016.3	1,319.1	697.2	15.6	16.8	12.0	24.3	27.5	16.9
plant, machinery and equipment	1,339.8	825.1	514.7	1,562.9	1,031.7	531.2	12.9	16.6	7.4	25.0	21.3	13.2
industrial motor vehicles	289.0	177.1	111.9	330.7	214.2	116.5	30.5	14.4	41.0	20.9	4.5	2.8
others	96.6	58.6	38.0	122.7	73.2	49.5	13.9	27.0	9.7	24.9	1.7	0.9
Producer goods	636.0	1,536.2	- 900.2	638.6	1,713.6	- 1,075.0	12.7	0.4	8.0	11.5	8.7	22.0
fuel and power	361.6	1,044.4	- 682.8	357.2	1,128.8	- 771.6	13.8	- 1.2	5.4	8.1	4.9	14.5
others	274.4	491.8	- 217.4	281.4	584.8	- 303.4	11.2	2.5	13.8	18.9	3.8	7.5
Total . . .	6,366.0	6,428.7	- 62.7	7,330.7	7,781.1	- 450.4	17.0	15.1	4.7	21.0	100.0	100.0
<i>Geographical distribution</i>												
DEVELOPED COUNTRIES	4,438.4	4,162.6	275.8	5,191.0	5,134.2	56.8	17.5	16.9	7.9	23.3	70.8	66.0
EEC	2,550.0	2,327.2	222.8	3,114.6	3,011.5	103.1	20.9	22.1	9.5	29.4	42.5	38.7
Belgium-Luxembourg	264.4	200.8	63.6	286.5	276.6	9.9	9.4	8.3	11.5	37.7	3.9	3.6
France	801.2	728.2	73.0	1,060.9	966.6	94.3	21.8	32.4	11.2	32.7	14.5	12.4
West Germany	1,189.3	1,148.4	40.9	1,441.1	1,459.5	- 18.4	23.9	21.2	8.3	27.1	19.7	18.7
Netherlands	295.1	249.8	45.3	326.1	308.8	17.3	18.4	10.5	8.9	23.6	4.4	4.0
Other Western Europe	968.3	803.2	165.1	1,022.1	921.6	100.5	5.5	5.5	1.6	14.7	13.9	11.8
United Kingdom	281.2	272.8	8.4	263.7	312.4	- 48.7	7.0	- 6.2	0.7	14.5	3.6	4.0
Switzerland	285.8	156.1	129.7	328.2	185.9	142.3	10.2	14.8	9.8	19.1	4.4	2.4
Others	401.3	374.3	27.0	430.2	423.3	6.9	1.4	7.2	- 0.7	13.1	5.9	5.4
United States	681.2	748.4	- 67.2	795.5	881.9	- 86.4	26.2	16.8	12.5	17.8	10.9	11.4
Others	238.9	283.8	- 44.9	258.8	319.2	- 60.4	13.4	8.3	2.4	12.5	3.5	4.1
DEVELOPING COUNTRIES	1,479.4	1,809.0	- 329.6	1,617.5	2,155.8	- 538.3	16.8	9.3	0.4	19.2	22.1	27.7
SOCIALIST COUNTRIES	380.2	441.9	- 61.7	453.0	481.4	- 28.4	17.0	19.1	- 5.4	8.9	6.2	6.2
USSR	109.8	179.8	- 70.0	179.4	154.4	25.0	40.4	63.4	4.5	- 14.1	2.4	2.0
Others (1)	270.4	262.1	8.3	273.6	327.0	- 53.4	9.6	1.2	- 11.1	24.8	3.8	4.2
IMPORTS UNALLOCATED	68.0	15.2	52.8	69.2	9.7	59.5	- 8.2	1.8	- 3.8	- 36.2	0.9	0.1
TOTAL . . .	6,366.0	6,428.7	- 62.7	7,330.7	7,781.1	- 450.4	17.0	15.1	4.7	21.0	100.0	100.0

Central Statistical Office figures reworked by Bank of Italy.— (1) Albania, Bulgaria, Czechoslovakia, China Mainland, North Korea, Eastern Germany, Mongolia, Poland, Rumania, Hungary, North Vietnam.

CHART 7



Principal factors affecting Italy's foreign trade
(Seasonally adjusted indices, 1966 = 100)

The main impetus to the growth in imports was given, in 1969, by purchases of raw materials and semi-finished products. These purchases, which had come in very slowly in the preceding year owing to heavy drawings on stocks, began to expand again steadily owing to the dual necessity of adjusting the available supplies of these products to the increased activity of enterprises and of replenishing stocks.

Imports of finished capital goods also rose considerably owing to the revival in capital investment. Within this category, for the second year in succession, there was a particularly large increase in purchases of aircraft.

Imports of finished consumer goods grew much faster than in 1968; this was mainly due to the revival of purchases of foodstuffs, itself attributable in turn to the growth in domestic consumption, only partly covered by the crops and harvests of the last two farming years. There were also considerable increases in imports of durable consumer goods.

In order to show the effect of the work stoppages on exports, the breakdown of the latter by types of goods has been made separately for the first nine months of the year and for the last quarter (Table 20). Until September there had been a marked rise in the rate of increase of sales of finished consumer and capital goods. This trend was matched

on the supply side by the high level of domestic production and on the demand side by sharp rise in imports by certain countries (EEC and United States), which are Italy's main buyers for these products. There was a certain slackening, on the other hand, in exports of semi-finished products and producer goods owing to the domestic market's increased need of them.

TABLE 20

MERCHANDISE COMPOSITION OF EXPORTS
(in billions of lire)

Product groups	1968		1969		Percentage changes in 1969 (1)		
	Jan.-Sept.	Oct.-Dec.	Jan.-Sept.	Oct.-Dec.	Jan.-Sept.	Oct.-Dec.	Jan.-Dec.
Raw materials	60.9	20.7	67.7	21.8	11.2	5.3	9.7
Semi-finished products	626.7	256.0	723.5	223.5	15.4	- 12.7	7.3
Consumer goods	2,197.4	842.9	2,744.3	895.0	24.9	6.2	19.7
Food	396.9	150.2	452.5	179.1	14.0	19.2	15.4
Other non-durables	924.3	349.4	1,183.7	387.6	28.1	10.9	23.4
Durables	876.2	343.3	1,108.1	328.3	26.5	- 4.4	17.8
Capital goods	1,246.0	479.4	1,541.1	475.2	23.7	- 0.9	16.8
Plant, machinery and equip.	963.6	376.2	1,191.9	371.0	23.7	- 1.4	16.6
Industrial motor vehicles	213.2	75.8	255.5	75.2	19.8	- 0.8	14.4
Others	69.2	27.4	93.7	29.0	35.4	5.8	27.0
Producer goods	467.6	168.4	481.7	156.9	3.0	- 6.8	0.4
Fuel and power	261.8	99.8	265.2	92.0	1.3	- 7.8	- 1.2
Others	205.8	68.6	216.5	64.9	5.2	- 5.4	2.5
Total	4,598.6	1,767.4	5,558.3	1,772.4	20.9	0.3	15.1

(1) In relation to the same period of the previous year.

In the last quarter of the year, while demand was expanding rapidly, the strikes in the sectors mainly producing for foreign markets drastically reduced the country's export capacity. The drop in sales was greater for the products of the petrochemical and metallurgical industries than for those of the engineering industry. The greater importance of exports to the latter presumably caused Italian manufactures to draw on their stocks of finished product and temporarily to sacrifice the home market by lengthening their normal domestic delivery terms.

In 1969 there was an increase in the relative importance of our trade with the EEC countries; more than half the expansion in imports and exports was with these countries, whose share in Italy's total trade

rose, compared with 1968, from 36 to 39 per cent for imports and from 40 to 43 per cent for exports.

With regard to trade with other countries, mention should be made of an appreciable worsening of our trade balance with the United Kingdom owing to a large rise in imports and a decline in exports.

Imports from the United States grew faster than in the previous year, the major part being accounted for by iron and steel products, which the Italian market particularly needed. Exports rose rapidly until July and then gradually slackened. Trade with the developing countries and the Socialist economies received a further impetus.

The deficit of 219 million dollars on transport account in 1969 was 13 million greater than that in the previous year; the deterioration was due to the further increase in the deficit in respect of sea and land transport, only partly offset by the improvement in the air sector.

In terms of volume, imports by sea were up by 14 per cent, while there was a rise of 9 per cent in freight payments, due to the greater share of ships under the Italian flag in bringing goods to Italy and the appreciable decline in tanker rates.

During the year the Italian merchant fleet was also able to increase the traffic between foreign countries thanks to improvements both in its structure and in its operational efficiency, raising the total tonnage by 250,000 tons to 6.8 million. In the passenger sector, too, the results were better than in the previous year .

Altogether, taking into account the expenses incurred by the fleet in Italy and abroad, sea transport showed an estimated deficit of 177 million dollars in 1969, against 142 million in 1968.

In land transport, imports by rail were up by 1.5 million tons, but the percentage increase in expenditure was less than that in quantity because a larger proportion reached Italy without passing through third countries.

The growth in air traffic of goods and passengers continued in 1969; Italian-owned aircraft were very active in these fields, achieving increases of 25 and 19 per cent, respectively, in goods and passengers carried. The surplus on air transport improved further, from 119 million dollar in 1968 to 148 million.

In 1969 receipts from foreign tourism in Italy reached 1,632 million dollars, that is, 156 million, or 11 per cent, more than in the previous year. This result is attributable to the revival of the tourist flow to Italy after the standstill in 1968. A particularly important contribution was made by visitors from Germany and the United States; the number of overnight stays by these rose by about 3.5 million, or more than two-thirds of the total increase. Arrivals from the United Kingdom were also higher than in 1968, while the inflow of French tourists declined for the second year in succession.

The growth in passive tourism was particularly large in 1969; allocations of foreign exchange to Italians going abroad amounted to 493 million dollars, or 36 per cent more than in 1968.

The net inflow of foreign exchange in respect of workers' earnings investment income and emigrants remittances from abroad in 1969 was 1,051 million dollars, an increase of 168 million over that in the previous year. Income from labour and capital made a particularly large contribution, of about 70 million dollars, to the rise, while the increase in emigrants' remittances, at 25 million, was more modest.

Capital movements.— The causes which had brought about large deficits in Italian capital movements in the years 1965-1968 were still operating in 1969, and were also reinforced by speculative factors connected, in particular, with the expectations of German mark revaluation and the uncertainties concerning the country's internal situation. The net outflow last year was therefore the largest so far recorded; it was more than double the 1968 figure, having risen from 1,691 to 3,432 million dollars.

The usual evaluation of the influence of the various factors behind capital movements shows that the deterioration in 1969 is mainly attributable to fiscal and institutional factors, a category which also includes the above-mentioned speculative phenomena, and to the evolution of the system for granting credits directly and indirectly connected with exports. The surplus in capital movements due to autonomous factors declined, while interest rate differentials caused a net outflow of almost the same size as in the previous year (Table 21).

In 1969 the inflow of foreign capital was 26 million dollars smaller than in 1968 and net exports of Italian capital were greater by 1,715

TABLE 21

ESTIMATED CLASSIFICATION OF FACTORS AFFECTING
ITALIAN CAPITAL MOVEMENTS

(millions of dollars)

Factors	1965	1966	1967	1968	1969
Autonomous factors (1)	347	105	99	189	41
Export financing and aid (2)	- 480	- 405	- 473	- 512	- 598
Interest rates (3)	25	- 348	- 62	- 400	- 450
Fiscal and institutional factors (4)	- 227	- 479	- 397	- 737	-2,165
Total (5) . . .	- 335	-1,127	- 833	-1,460	-3,172

Pro memoria:

<i>Remittances of Italian bank notes from abroad</i>	- 313	- 559	- 801	- 1,127	- 2,256
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(1) Italian direct investments abroad and foreign direct investments in Italy, other investments (real estate), public authorities' foreign loans, long-term foreign commercial credits.— (2) Italian long and short-term commercial credits, Italian public authorities' loans and investments abroad, and part of Italian private-sector loans abroad.— (3) Private-sector foreign loans, short-term foreign commercial credits, part of Italian private-sector loans abroad, part of bank-note remittances and part of Italian portfolio investments abroad.— (4) Part of bank-note remittances, foreign portfolio investments in Italy and part of Italian portfolio investments abroad.— (5) The total differs from the overall balance of capital movements owing to the estimation of the proportion of bank-note remittances connected with current transactions.

million, so that the overall deterioration in capital movements was 1,741 million (Table 22).

Direct investments increased by 147 million dollars. The transactions behind them, except for operations connected with oil companies, were numerous and generally small in amount and were concentrated, as in previous years, in the mechanical engineering, chemical and financial sectors. Investments came mainly from Switzerland, which continued to play an important role as a financial intermediary, and the United States.

Portfolio investments increased by 200 million to 593 million. About one-quarter of this amount was accounted for purchases of listed shares undertaken by foreign mutual investment funds in order to comply with the requirements of the regulations issued by the monetary authorities in April 1969. Under these regulations foreign mutual funds are permitted to operate in Italy essentially on the condition that at least half the value of their portfolios consist of Italian securities.

The net inflow due to private loans almost doubled owing both to the decline in repayments and to the large credits granted towards the end of the year to certain Italian enterprises and banking institutions. Loans tied to imports (mainly of aircraft from the United States) ac-

counted for about one-fifth of total borrowing; a smaller proportion consisted of operations by foreign companies with subsidiaries in Italy.

Public-sector loans, net of repayments, amounted to 53 million and consisted mainly of operations between the EIB and the Cassa per il Mezzogiorno (Southern Italy Development Fund).

CAPITAL MOVEMENTS

TABLE 22

(millions of dollars)

I t e m s	Credit		Debit		Balance	
	1968	1969	1968	1969	1968	1969
Foreign capital	1,596.2	1,778.8	1,134.6	1,343.6	461.6	435.2
Investments:						
direct	412.1	559.1	80.3	140.7	331.8	418.4
portfolio	393.2	592.8	343.5	618.0	49.7	25.2
other	43.1	42.9	23.0	20.1	20.1	22.8
Loans:						
private	329.1	318.5	265.5	195.0	63.6	123.5
government or government-guaranteed	110.0	123.2	52.6	65.6	57.4	57.6
local authorities	—	—	—	4.9	—	4.9
Trade credits:						
medium and long-term	308.7	130.8	267.7	299.3	41.0	168.5
short-term	—	11.5	102.0	—	102.0	11.5
Italian capital	1,006.7	952.0	3,159.0	4,819.2	-2,152.3	-3,867.2
Investments:						
private: direct	116.5	102.4	377.7	385.7	261.2	283.3
portfolio	112.0	156.2	391.0	617.2	279.0	461.0
other	1.3	0.9	1.1	2.6	0.2	1.7
public	—	—	2.0	—	2.0	—
Loans:						
private	178.5	51.0	263.1	517.5	84.6	466.5
government or government-guaranteed	36.0	37.3	155.5	118.7	119.5	81.4
Trade credits:						
medium and long-term	562.4	604.2	581.4	705.2	19.0	101.0
short-term	—	—	259.9	216.4	259.9	216.4
Bank note remittances	—	—	1,127.3	2,255.9	-1,127.3	-2,255.9
Balance	—	—	—	—	-1,690.7	-3,432.0

In the case of long-term import credits, repayments exceeded new borrowing by 168 million dollars, mainly owing to certain large operations in the oil sector. The opposite was the case with short-term credits, so that the overall net outflow was 157 million, against 61 million in 1968.

Italian direct investments totalled 386 million dollars and consisted mainly of large operations to finance oil-prospecting and contributions of Italian companies to their foreign subsidiaries (made almost entirely in the first half of the year, when domestic interest rates were relatively low).

Portfolio investments amounted to 617 millions a rise of 226 million, approximately three-quarters of which was attributable to purchases of units of foreign mutual investment funds. There was little change in disinvestments.

The Italian banks' share in the placing of securities issued abroad declined, from the second quarter of 1969, owing both to the reduction in issues on the Euro-market and, above all, to the measure introduced in March by the monetary authorities limiting participation in issuing consortia of foreign loans (Table 23).

TABLE 23

ITALIAN BANKS' SHARE IN THE PLACING OF SECURITIES ISSUED ABROAD
(millions of dollars)

Items	1968			1969		
	Jan.-Mar.	Apr.-Dec.	Year	Jan.-Mar.	Apr.-Dec.	Year
New issues (1) made by:						
RESIDENTS	—	75	75	—	155	155
of which: allotted to banks	—	56	56	—	86	86
placed with residents	—	52	52	—	79	79
NON-RESIDENTS	1,198	2,824	4,022	1,078	738	1,816
of which: allotted to banks	61	154	215	66	69	135
placed with residents	30	94	124	42	47	89
TOTAL	1,198	2,899	4,097	1,078	893	1,971
of which: allotted to banks	61	210	271	66	155	221
placed with residents	30	146	176	42	126	168

(1) Only those in which Italian banks took part.

Private loans granted in 1969 amounted to 518 million; those not connected with exports totalled 300 million, the increase of 160 million being chiefly due to operations carried out in the first half of the year by Italian enterprises possessing subsidiaries in Italy. The year under review also saw the transfer of 48 million dollars representing the pro-

ceeds of two bond issues, one by the Inter-American Development Bank and the other by the EIB, issued at the end of 1968.

The public sector granted loans totalling 119 million to developing countries, consisting almost entirely of financial credits in connection with Italian exports.

Among Italian capital movements, the largest increase was shown by remittances of bank-notes, which rose from 1,127 to 2,256 million dollars; as in previous years, over 95 per cent came from Switzerland.

In order to assess the uses made of the bank-notes sent from Switzerland it may be useful to examine capital movements with that country as a whole, in view of the fact that, insofar as the bank-notes finance investments in Italy under foreign name, an increase in remittances should have as its counterpart a like increase in the inflow of funds from Switzerland. Now in 1969 the increase in remittances of bank-notes was actually accompanied by a decline in the net inflow of funds from Switzerland.

TABLE 24

CREDITS DIRECTLY AND INDIRECTLY CONNECTED WITH EXPORTS
(millions of dollars)

I t e m s	1969			1969		
	Granted	Repaid	Net credit-granting (+)	Granted	Repaid	Net credit-granting (+)
Medium and long-term commercial credits	581.4	562.4	19.0	705.2	604.2	101.0
Developed countries . . .	69.7	56.1	13.6	73.2	61.5	11.7
Developing countries . .	404.9	365.8	39.1	447.2	345.7	101.5
Socialist countries	106.8	140.5	- 33.7	184.8	197.0	- 12.2
Financial credits	274.3	40.9	233.4	333.6	54.1	279.5
Developing countries . .	169.3	35.4	133.9	140.5	38.8	101.7
Socialist countries	105.0	5.5	99.5	193.1	15.3	177.8
Total . . .	855.7	603.3	252.4	1,038.8	658.3	380.5
Developed countries . . .	69.7	56.1	13.6	73.2	61.5	11.7
Developing countries . .	574.2	401.2	173.0	587.7	384.5	203.2
Socialist countries	211.8	146.0	65.8	377.9	212.3	165.6

Remittances of bank-notes increased further in the early part of 1970, reaching 325 million dollars in January and the first 15 days of February, against 220 million in the corresponding period of 1969. Re-

gulations issued on 14th and 18th February 1970 required that the crediting of bank-notes be centralised at the Central Cash Office of the Bank of Italy. After the introduction of these measures, remittances of Italian banknotes from abroad for crediting to capital accounts fell, dropping from 121 million in the first half of February to 25 million in the second. In March and April they totalled 86 and 107 million respectively, against 183 and 193 million in the corresponding months of 1969.

In 1969 medium and long-term credits directly and indirectly connected with exports increased by 183 million dollars, two-thirds of which was accounted for by commercial credits and the remainder by financial credits. As repayments rose less, net credit-granting went up from 252 to 380 million (Table 24).

Monetary movements.— In 1969 the balance of payments deficit was financed to the extent of 704 million dollars by the Bank of Italy and the Italian Exchange Office and, for the remaining 687 million, by the banks.

On 31st December 1969 the overall foreign position of the central monetary authorities was therefore reduced to 5,328 million dollars, of which 4,696 million represent the net official reserves and 632 million the medium and long-term assets. The banks, in accordance with the instructions issued in March, which were discussed in last year's Report, practically restored balance in their foreign accounts (Table 25).

New regulations concerning the foreign position of banks were issued on 27th March 1970. According to these the banks may maintain, from 1st April onwards, a net debit position vis-à-vis foreign countries for an amount not exceeding the increase, in comparison with the position on 28th February 1970, in the foreign exchange export financing granted to residents.

At the end of March 1970 the gross foreign assets of the Bank of Italy and the Italian Exchange Office amounted to 5,566 million dollars, equivalent to about four times the balance of payments deficit incurred in 1969 and more than five months' imports. On the same date the credit quota with the International Monetary Fund was 945 million dollars and the unutilised balance under the swap arrangements with the Federal Reserve System and the United States Treasury was 700 million.

TABLE 25

FOREIGN POSITION OF THE BANK OF ITALY,
THE ITALIAN EXCHANGE OFFICE AND ITALIAN BANKS

(month-end figures in millions of dollars)

Items	December				March 1970
	1966	1967	1968	1969	
<i>Bank of Italy—Italian Exchange Office</i>					
Official reserves:					
Reserves in gold or with gold guarantee	3,301.5	3,244.8	3,820.9	3,822.0	3,986.5
Gold	2,413.6	2,399.9	2,923.3	2,955.9	2,978.4
Special drawing rights	—	—	—	—	120.0
IMF position					
gold tranche	564.7	526.7	393.4	312.4	304.9
GAB	70.0	65.0	251.0	300.5	330.0
bilateral borrowing	250.0	250.0	250.0	250.0	250.0
Net EMF position	3.2	3.2	3.2	3.2	3.2
Reserves with lira guarantee	139.8	624.8	124.8	156.8	32.0
foreign securities in lire	124.8	124.8	124.8	156.8	32.0
central bank swaps	15.0	500.0	—	—	—
Convertible currencies	1,287.8	1,419.1	958.4	898.0	949.4
Total gross official reserves . . .	4,729.1	5,288.7	4,904.1	4,876.8	4,967.9
Short-term liabilities	— 49.8	— 50.6	— 25.8	— 180.4	—1,021.0
Central bank swaps	—	—	—	—	— 800.0
others	— 49.8	— 50.6	— 25.8	— 180.4	— 221.0
Total net official reserves . . .	4,679.3	5,238.1	4,878.3	4,696.4	3,946.9
Medium and long-term position:					
Foreign securities: in foreign currency	252.8	247.3	200.9	35.3	37.8
in lire	89.7	100.7	300.2	163.1	163.0
Consolidated accounts	95.4	88.4	158.8	130.0	105.1
Italian securities in foreign currency	457.2	418.9	494.4	303.2	291.8
Special drawing rights account	—	—	—	—	— 105.0
Total . . .	895.1	855.3	1,154.3	631.6	492.7
Total Bank of Italy-IEO . . .	5,574.4	6,093.4	6,032.6	5,328.0	4,439.6
<i>Banks</i>					
Assets	3,307.4	3,596.4	5,159.9	7,239.7	6,666.0
Liabilities	3,077.2	3,561.7	4,437.1	7,203.5	6,498.8
Balance	230.2	34.7	722.8	36.2	167.2

The maximum facilities available under the swap arrangement with the Federal Reserve System were raised, in March 1970, from 1,000 to 1,250 million; at the same time a three-month credit agreement was concluded with the United States Treasury for an amount of 250 million.

During a period of balance of payments deficit the problem arises as to what assets are to be liquidated, jointly with or as an alternative to recourse to the various forms of indebtedness, so as to ensure that available balances in dollars, which are the intervention currency, shall always remain sufficient. During 1969 and the first quarter of 1970 this aim was pursued mainly by requesting the banks to restore equilibrium in their respective foreign accounts and, with regard to part of the deficit not financed in this manner, by having recourse to the medium and long-term position and to short-term borrowing from the central bank.

The medium and long-term position was reduced during the year under review by 523 million dollars. The main operations which, in 1969, affected the Bank of Italy's short-term liabilities were: in the first half of the year, the advance building-up of lira funds by the U.S. Treasury, mainly for use on the maturing of a note in lire held by the IEO for the equivalent of 125 million dollars; and recourse in September to the swap arrangement with the Federal Reserve for 300 million dollars, repaid in November. In the first quarter of 1970 use was made on several occasions of the above-mentioned swap arrangement, for a total of 800 million dollars; recourse was also had during the same quarter to a swap arrangement with the Bank for International Settlements for 155 million.

The restoration of equilibrium in the banks' foreign accounts was effected by expanding their liabilities to a greater extent than their assets, so that the growth in the banks' intermediary function was not interrupted.

The largest changes were in their convertible currency position, while their lira position underwent no appreciable change (Table 26). More than half the foreign exchange which flowed into Italy via the banks (412 million out of 698) was used to reduce the dollar position with the Italian Exchange Office (Table 27); current arrangements between the IEO and the banks for lira-dollar swaps were therefore reduced by the end of the year to 1,590 million. As has been customary

TABLE 26

ITALIAN BANKS' FOREIGN POSITION

(changes and outstanding amounts, by currencies, in millions of dollars)

Items	1969					Outstanding amounts at end	
	quarters				Year	1968	1969
	I	II	III	IV			
<i>U.S. Dollars</i>							
Assets	142.4	304.0	- 44.4	1,156.4	1,558.4	3,449.8	5,008
Liabilities	- 105.3	591.1	204.6	1,348.0	2,038.4	2,662.1	4,700.5
Balance	247.7	- 287.1	- 249.0	- 191.6	- 480.0	787.7	307.7
<i>Swiss francs</i>							
Assets	85.3	- 60.0	19.5	126.1	170.9	433.1	604.0
Liabilities	70.7	189.9	- 67.2	69.7	263.1	531.5	794.6
Balance	14.6	- 249.9	86.7	56.4	- 92.2	- 98.4	- 190.6
<i>Pounds sterling</i>							
Assets	30.5	28.5	8.0	1.0	68.0	103.3	171.3
Liabilities	- 12.6	12.1	- 29.1	24.4	- 5.2	120.7	115.5
Balance	43.1	16.4	37.1	- 23.4	73.2	- 17.4	55.8
<i>Deutsche Marks</i>							
Assets	- 161.4	164.8	170.9	9.0	183.3	700.0	883.3
Liabilities	51.5	107.4	23.2	81.9	264.1	397.8	661.9
Balance	- 212.9	57.4	147.6	- 72.9	- 80.8	302.2	221.4
<i>Dutch florins</i>							
Assets	- 12.9	- 17.6	- 4.3	- 0.2	- 35.0	73.0	38.0
Liabilities	6.1	25.7	- 5.5	- 14.0	12.3	35.7	48.0
Balance	- 19.0	- 43.3	1.2	13.8	- 47.3	37.3	- 10.0
<i>French francs</i>							
Assets	7.5	- 16.9	- 3.1	- 2.9	- 15.4	33.8	18.4
Liabilities	31.2	- 20.7	11.0	- 2.7	18.8	12.6	31.4
Balance	- 23.7	3.8	- 14.1	- 0.2	- 34.2	21.2	- 13.0
<i>Other currencies</i>							
Assets	- 2.3	1.2	11.4	- 7.4	2.9	54.4	57.3
Liabilities	7.4	8.5	14.0	- 16.5	13.4	17.8	31.2
Balance	- 9.7	- 7.3	- 2.6	9.1	- 10.5	36.6	26.1
<i>Forward commitm. and claims</i>							
Assets	—	—	—	—	—	—	—
Liabilities	- 1.8	29.3	11.9	- 13.5	25.9	13.8	39.7
Balance	1.8	- 29.3	- 11.9	13.5	- 25.9	- 13.8	- 39.7
TOTAL {							
Assets	89.1	404.0	158.0	1,282.0	1,933.1	4,847.4	6,780.5
Liabilities	47.2	943.3	163.0	1,477.3	2,630.8	3,792.0	6,422.8
Balance	41.9	- 539.3	- 5.0	- 195.3	- 697.7	1,055.4	357.7
<i>Italian lire</i>							
Assets	52.1	53.3	12.5	28.8	146.7	312.5	459.2
Liabilities	68.1	74.0	- 55.7	49.2	135.6	645.1	780.7
Balance	- 16.0	- 20.7	68.2	- 20.4	11.1	- 332.6	- 321.5
TOTAL {							
Assets	141.2	457.3	170.5	1,310.8	2,079.8	5,159.9	7,239.7
Liabilities	115.3	1,017.3	107.3	1,526.5	2,766.4	4,437.1	7,203.5
Balance	25.9	- 560.0	63.2	- 215.7	- 686.6	722.8	36.2

Positive balance indicates increase in net assets or reduction in net liabilities.

TABLE 27

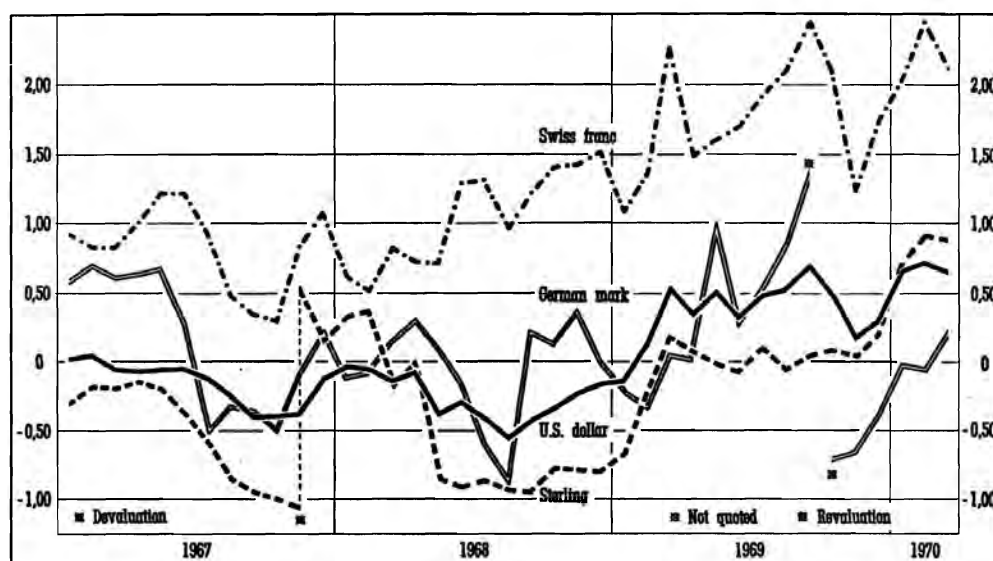
ITALIAN BANKS' FOREIGN EXCHANGE POSITION

(amounts in million of dollars)

At end of	Swaps with rate		Total
	guaranteed	not guaranteed	
1968 - December	1,973.7	28.4	2,002.1
1969 - January	2,119.9	28.4	2,148.3
March	2,064.3	28.3	2,092.6
June	1,760.0	28.3	1,788.3
September	1,604.3	28.3	1,632.6
December	1,561.8	28.3	1,590.1
1970 - March	1,552.8	31.5	1,584.3

for several years, the greater part of the banks' foreign exchange operations were carried out on the Euro-dollar market (Table 28).

CHART 8



Percentage discrepancies between official exchange rate and lira parity

(A positive discrepancy indicates a premium, and a negative discrepancy a discount, on the foreign currency in terms of the lira)

The unfavourable trend of the balance of payments was reflected in the spot rate for the lira against the dollar; the Italian currency was constantly at a discount (Chart 8) and frequently touched the upper intervention limit (629.50). The pressure on the lira was greatest in Sep-

ITALIAN BANKS' FOREIGN POSITION IN DOLLARS
(changes and outstanding amounts in millions of dollars)

TABLE 28

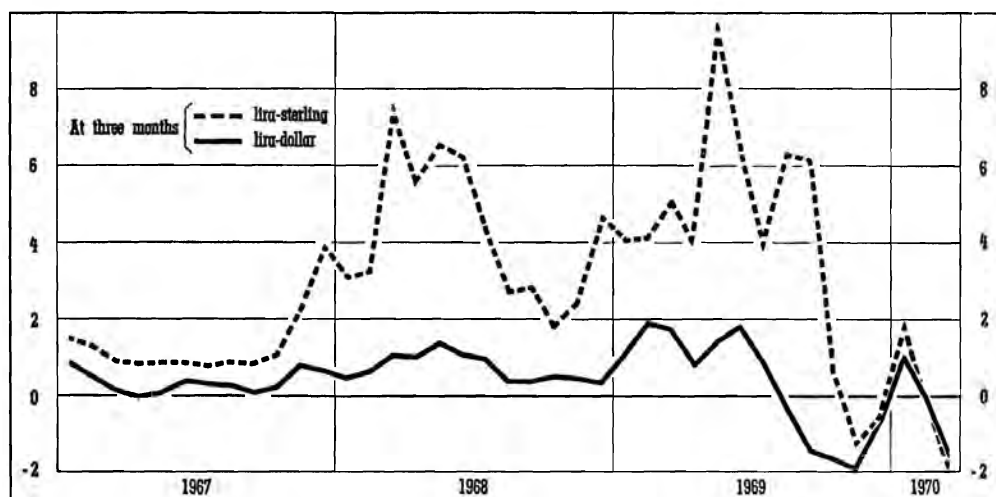
Country	1969					Outstanding amounts at end		
	quarters				Year	1968	1969	
	I	II	III	IV				
EURO-DOLLAR MARKET								
United Kingdom								
Assets	130.4	268.8	- 35.1	204.2	568.3	1,415.2	1,983.5	
Liabilities	- 36.3	185.1	41.9	590.7	781.4	599.1	1,380.5	
Balance	166.7	83.7	- 77.0	- 386.5	- 213.1	816.1	603.0	
Switzerland								
Assets	11.0	90.9	- 25.7	192.7	268.9	286.9	555.8	
Liabilities	2.3	261.2	10.4	81.3	355.2	476.0	831.2	
Balance	8.7	- 170.3	- 36.1	111.4	- 86.3	- 189.1	- 275.4	
France								
Assets	141.0	- 55.3	46.0	423.9	555.6	369.2	924.8	
Liabilities	- 90.9	44.8	53.8	527.9	535.6	380.3	915.9	
Balance	231.9	- 100.1	- 7.8	- 104.0	20.0	- 11.1	8.9	
Belgium								
Assets	- 71.6	42.0	- 4.5	27.4	- 6.7	151.3	144.6	
Liabilities	- 59.3	- 23.6	58.3	58.8	34.2	241.2	275.4	
Balance	- 12.3	65.6	- 62.8	- 31.4	- 40.9	- 89.9	- 130.8	
Germany								
Assets	- 7.9	44.3	13.7	160.6	210.7	40.0	250.7	
Liabilities	- 65.5	83.0	- 19.5	- 76.9	- 78.9	147.2	68.3	
Balance	57.6	- 38.7	33.2	237.5	289.6	- 107.2	182.4	
Netherlands								
Assets	- 21.4	10.2	17.0	- 1.4	4.4	56.3	60.7	
Liabilities	- 14.5	13.2	16.0	71.8	86.5	103.8	190.3	
Balance	- 6.9	- 3.0	1.0	- 73.2	- 82.1	- 47.5	- 129.6	
Middle East								
Assets	- 5.1	- 5.1	5.6	- 12.3	- 16.9	39.5	22.6	
Liabilities	17.1	6.2	13.4	- 6.3	30.4	89.4	119.8	
Balance	- 22.2	- 11.3	- 7.8	- 6.0	- 47.3	- 49.9	- 97.2	
Latin American countries								
Assets	13.7	- 17.8	- 4.5	- 48.9	- 57.5	125.4	67.9	
Liabilities	33.7	14.3	16.8	22.5	87.3	113.5	200.8	
Balance	- 20.0	- 32.1	- 21.3	- 71.4	- 144.8	11.9	- 132.9	
Eastern European countries								
Assets	7.2	- 38.9	22.3	27.8	18.4	144.7	163.1	
Liabilities	10.4	- 4.8	27.1	64.9	97.6	54.0	151.6	
Balance	- 3.2	- 34.1	- 4.8	- 37.1	- 79.2	90.7	11.5	
Other countries								
Assets	10.4	- 22.3	- 11.3	- 4.2	- 27.4	285.1	257.7	
Liabilities	92.7	- 85.9	- 6.9	7.8	7.7	274.0	281.7	
Balance	- 82.3	63.6	- 4.4	- 12.0	- 35.1	11.1	- 24.0	
TOTAL {	Assets	207.7	316.8	23.5	969.8	1,517.8	2,913.6	4,431.4
	Liabilities	- 110.3	493.5	211.3	1,342.5	1,937.0	2,478.5	4,415.5
	Balance	318.0	- 176.7	- 187.8	- 372.7	- 419.2	435.1	15.9
UNITED STATES								
Assets	- 53.4	3.0	- 42.8	153.8	60.6	287.5	348.1	
Liabilities	4.7	93.9	- 20.8	- 3.5	74.3	156.6	230.9	
Balance	- 58.1	- 90.9	- 22.0	157.3	- 13.7	130.9	117.2	
OTHER ASSETS AND LIABILITIES (1)								
Assets	- 11.9	- 15.8	- 25.1	32.8	- 20.0	248.7	228.7	
Liabilities	0.3	3.7	14.1	9.0	27.1	27.0	54.1	
Balance	- 12.2	- 19.5	- 39.2	23.8	- 47.1	221.7	174.6	
TOTAL {	Assets	142.4	304.0	- 44.4	1,156.4	1,558.4	3,449.8	5,008.2
	Liabilities	- 105.3	591.1	204.6	1,348.0	2,038.4	2,662.1	4,700.5
	Balance	247.7	- 287.1	- 249.0	- 191.6	- 480.0	787.7	307.7

(1) Not included in the Euro-dollar statistics.

tember, on the eve of the revaluation of the Deutsche Mark; in that month sales of dollar on the market by the Bank of Italy were particularly high, in excess of 480 million dollars.

The innovations introduced between the end of 1968 and the first months of 1969 in the policy pursued by the Bank in its interventions, which were mentioned in the last Report, were consolidated during the year. The Bank continued to refrain from telling the market what its buying and selling intervention limits would be, so that the exchange rate was able to vary during the day depending on the quotation of the international market; at the same time an element of uncertainty was introduced, which acted as a brake on speculative demand for dollars.

CHART 9



Forward lira-dollar and lira-sterling rates

*(Premium (+) or discount (-) of the lira on the dollar
and sterling in per cent per annum of the spot rate)*

The forward quotation for the lira against the dollar, although undergoing frequent fluctuations, showed a tendency to deteriorate; this was mainly due to the development of swap operations undertaken by the banks, to the steady rise in interest rates in Italy and, more generally, to the trend of the balance of payments and the resultant uncertainties regarding the lira (Chart 9). As a result of the improvement in the British balance of payments, the lira was also at a discount against sterling in the latter part of the year.

Public finance

The main feature of the trend of the Treasury's cash operations in 1969 was the reduced recourse to new borrowing, a development which had appeared impossible in view of the expectations which had reasonably been entertained at least up to last autumn. It was, however, the result of fortuitous factors which prevented the normal course of operations in the last months of the year. Actually if we consider, instead of the calendar year, the twelve-month period ended February or March 1970, that is, a period of time within which, also owing to the closing of the financial year, the process of revival of full spending activity can be regarded as having been completed, the trend is reversed, showing a substantial increase in the deficit, the volume of which falls not far short of that forecast in the previous Report. In order, however, properly to assess its significance it must be borne in mind that it was affected by the continuing delay in the collection of some categories of direct taxes.

It should also be stressed that, notwithstanding the decline in the deficit, the proportion of it that was covered by short-term financing, largely in the form of subscription of securities by the Bank of Italy, increased considerably, mainly as a result of the difficult capital market conditions.

The course of the cash budget particularly affected the net Government arrears of expenditure, owing to the large discrepancy which developed in relation to the budget on an appropriation basis: the increase in net arrears of expenditure is to be regarded as unusually large even if related not to the calendar year but to the financial year (the only accounting standard of reference for arrears), which benefited from the larger budget expenditures in the two « supplementary » months January and February 1970.

The local authorities, in turn, show only a small expansion of the cash deficit, but this is a result of their spending capacity's being restricted by the limited possibilities of raising funds rather than of any structural improvement in budget management, as is shown by the growth in the expenditure arrears, which was larger than in the past and due to the constant rise in appropriations.

Turning to the real effects of public intervention, that is to the contribution made by the Government to the growth in GNP, a tentative assessment, which in a wider framework is extended further on in the chapter to cover the last eighteen years, shows how in 1969 only a limited proportion of the growth in GNP can be attributed to the direct action of the public authorities, unlike in 1968, when the contribution of the public sector was more than one-quarter of the percentage increase in GNP.

A forecast of the possible trend during the current year of the financial transactions of the public sector is possible only for the Central Government and the autonomous agencies, concerning which information is provided by the budget appropriations. These point to a slowing down of the rate of increase of requirements; it should be borne in mind, however, that the Government budget will probably very shortly have to assume the burden of the deficits accumulated by the public health institutions in 1968 and 1969, and also, in cash terms, suffer the compensatory effects of the slackening of spending activity at the end of 1969. No information is available at present regarding the amount of the indebtedness accumulated by the above-mentioned institutions in the past two years: it may, however, be roughly assessed at over 600 billion lire.

The total cash requirement of the Treasury, the Central Post Office Savings Fund and the autonomous Government agencies in the 1969 calendar year was just under 1,800 billion lire, about 200 billion less than in the previous year (Table 29).

In order to interpret these results properly it is necessary to bear in mind that the stoppages of work at the end of the year by Government employees resulted in the postponement of certain quite substantial items of expenditure until the early months of 1970; revenue was also affected, but to a somewhat smaller extent.

The decrease in requirements between the two years was more than offset by the increase in the first quarter of 1970 over the same quarter of the previous year; between the two twelve-month periods up to March 1969 and March 1970 respectively, requirements increased from 1,950 to 2,450 billion lire, in round figures. The results for the first quarter of 1970 are, however, affected, to an extent which can be assessed at close to 200 billion, by the non-collection of a proportion

TABLE 29

TREASURY CASH REQUIREMENTS AND THEIR COVERAGE (1)

(calendary years and quarters; cash position; billions of lire)

Item	1968		1969		1970 1st quarter
	1st quarter	Total	1st quarter	Total	
Overall cash requirements					
Budget deficit (—)	— 358	— 1,364	— 178	— 599	— 1,549
Treasury operations	181	161	— 80	— 554	826
Extra-budgetary operations (—)	— 279	— 818	— 119	— 636	— 329
Total	— 456	— 2,021	— 377	— 1,789	— 1,052
of which: for lending operations (—)	— 406	— 1,223	— 285	— 926	— 291
through budget	— 214	— 721	— 179	— 484	— 140
extra-budgetary	— 192	— 502	— 106	— 442	— 151
Coverage of overall cash requirements					
Medium and long-term bonds, excluding Bank of Italy	399	1,093	398	358	30
Postal savings	— 13	348	6	375	40
Treasury Bills, excluding Bank of Italy	19	74	15	— 146	— 42
Borrowing from Bank of Italy	80	500	— 36	1,214	964
of which: current account (2)	143	121	49	— 399	594
Other indebtedness (3)	— 29	6	— 6	— 12	60
Total	456	2,021	377	1,789	1,052
of which: short-term financing	57	922	— 24	1,422	1,019
medium and long-term financing (4)	399	1,101	398	370	34
Net indebtedness (5)	50	798	92	863	761

(1) For the first quarter of 1970 some figures have been estimated.— (2) The figures with a plus sign indicate greater Treasury borrowing.— (3) Including change in Government note and coin circulation and the foreign debt.— (4) Excluding foreign debt.— (5) Change in the financial situation, that is, borrowings less lendings.

of the two-monthly installment of direct taxes owing to the tax officials' strike.

Separate consideration of the individual components of the deficit shows that the sharp fall in the budget, strictly defined, of about 750 billion lire was practically offset by the worsening in respect of minor Treasury operations. The latter in fact ultimately had to bear the burden of some payments, especially personnel expenses and transfers to Social Security Institutions, which could not be debited directly to the budget owing to the strikes.

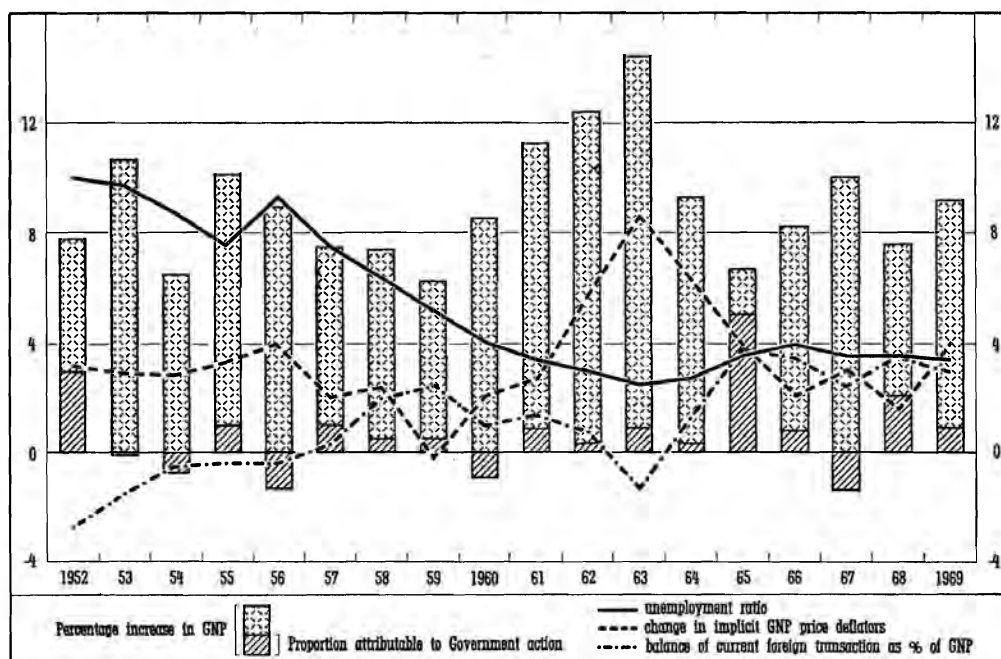
In 1969 the Treasury's overall requirements were mainly financed by sales to the Bank of Italy of medium and long-term securities, which

were concentrated especially in the second half of the year, at the time of the tensions on the capital market. The issues of Treasury Bills, too, not having been taken up by the banks, were subscribed almost entirely by the Bank of Italy (Table 29).

The combination of large security issues and a small volume of expenditure led to an improvement in the Treasury's liquidity situation, namely the elimination of the current account deficit with the Bank of Italy and the emergence of a balance in favour of the Treasury, which at the end of 1969 had reached 113 billion lire.

In order to determine the income effects produced by the general Government, use has been made of a scheme of analysis based on a model already employed by the OECD (Chart 10).

CHART 10



Contribution of the Government to the increase in the gross national product

A general observation which can be made when one examines the comparative trend of the various phenomena throughout the period examined concerns the apparent absence of any system in the effects of the measures of anticyclical policy adopted by the Government. During the 1960s, only in 1965, and to a smaller extent in 1968, the Government's action, in a situation characterised by a surplus on the current account of the balance of payments and by moderate rates of

increase in prices, is seen to have appreciably contributed to the growth in income. During the other years its behaviour appears to have been unadjusted to the circumstances, often ultimately producing procyclical effects.

It must be admitted that budgetary policy is difficult to apply, as is shown by the experience not only of Italy but also of many other countries. Its effectiveness is bound up not only with the nature of the measures decided upon but also, and above all, with the timeliness with which they are applied. For in addition to the « recognition lag » which elapses between the appearance of cyclical phenomena and their statistical recording, there is also a « decision » lag, at the Government and Parliamentary levels, and an « implementation » lag at the public administration level. Only in the last-mentioned case, of course, can reference justly be made to the efficiency of the administrative apparatus, and even then only within the limits of the freedom of action allowed to it by the law and by the accounting regulations.

Italy's experience in the past twenty years shows, in particular, how, among the available instruments, only meagre use has been made of taxation for anticyclical purposes. In most cases taxation has been resorted to only in order to raise funds for financing new expenditure; but there has not always been parallelism between the making of the expenditures thus financed and the actual receipt of the sums in question, so that they have often led to a net drain of funds (offset, of course, in other periods by an excess of payments). In the revenue sector, however, a special case is represented by social contributions: their handling by means of temporary measures of « fiscalisation » (i.e. reducing social contributions and increasing correspondingly central Government transfers to Social Security Institutions) has produced timely and very effective results. If account is also taken of the effects achieved by the revision of pension payments, incidentally always with an upward trend, it must be concluded that the most dynamic component in the Government sphere is represented by the Social Security sector.

There was also little continuity and effectiveness in the measures taken to stimulate the economy by means of direct investments and capital account transfers; in some years this category of expenditure produced restrictive effects. A constant expansionary trend, on the

other hand, was shown by public consumption, which assumed an increasingly important role in the 1960s, reaching an exceptional peak in 1963, mainly in connection with the substantial increase in personnel expenditure.

With regard to the timing of the incidence of public investments, certain reserves should be made: for it is reasonable to assume that their effect on the economy actually occurs, at least partly, in periods prior to those in which the expenditures by the Government are recorded, this being due to prefinancing by the market. The expenditures by the public authorities which commissioned projects lag some time behind the implementation of the works themselves, depending on their state of progress, when it has not actually been provided that payment is to be divided into annual instalments.

An examination, in particular, of the trends in the last two years shows, in short, how in 1968 the Government authorities' action was mainly related to public consumption, investment, improvement of Social Security benefits and the partial « fiscalisation » of Social Security contributions. The tax burden, strictly defined, hardly increased and is furthermore partly offset by transfers to enterprises and households. In 1969, on the other hand, the fiscal authorities appear to have made a less important contribution, which was mainly reflected in public consumption and, once again, in the increase in pension payments and the « fiscalisation » of certain social contributions.

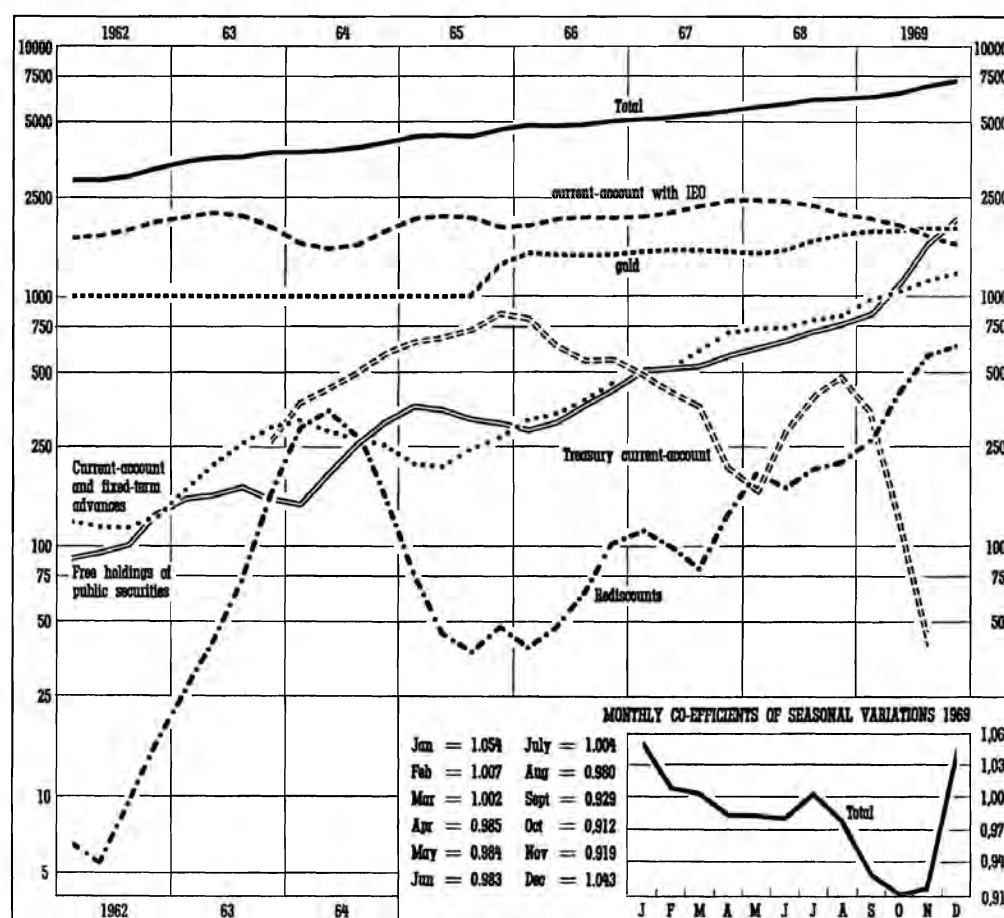
Operations of the Bank of Italy and the Italian Exchange Office

The Bank of Italy's balance sheet.— The changes in the assets and liabilities vis-à-vis the Treasury are attributable, in the year under review, not only to the financing of the public sector's spending programmes but also, through it, to the regulation of the money and capital markets. This was reflected in an increase in the Bank's security portfolio and in the substantial decrease in the average positive current account balance with the Treasury (Chart 11). In 1969 lendings to the Treasury increased by 1,242.1 billion (against 514.1 billion in 1968) reaching the level of 4,060.1 billion, representing 38.1 per cent of total assets (Table 30). The yearly average total of these lendings in 1969 was 3,031.3 billion, representing an increase of 23.2 per cent over the pre-

vious year, mainly due to the expansion in the portfolio of public securities.

The end-of-month values of the Treasury's current account balance showed the characteristic bimonthly fluctuation due to the incidence of dates for the payment of direct taxes and became positive in favour of the Treasury in the last five months of the year owing both to large issues of public securities in September and December and to the reduction in payments, partly connected, as has already been stated in the previous chapter, with the civil servants' strike.

CHART 11



Main lendings of the Bank of Italy
(seasonally adjusted amounts in billions of lire)

The holdings of public securities increased, from December to December, by 1,421.8 billion, due to a volume of subscriptions and purchases on the market (2,260.0 billion) almost double that in 1968,

BANK OF ITALY
(at ends of months;

Assets	1967 December	1968 December	1969			
			March	June	September	December
Lendings to the Treasury	2,303.9	2,818.0	2,770.7	2,836.4	3,496.5	4,060.1
cash } Government notes and coins	24.0	14.1	15.3	18.6	13.9	11.0
} postal items for collection	20.2	22.7	8.1	13.2	13.0	28.6
current account	165.9	286.7	336.1	77.7	—	—
miscellaneous services	61.4	91.5	94.8	70.5	107.8	137.7
special advances	339.0	339.0	339.0	339.0	339.0	339.0
discounts: obligatory agricultural stockpiling and grain purchases (1)	776.1	830.1	840.4	859.5	884.3	905.3
securities } freely available	746.7	1,034.6	940.6	1,278.7	1,926.1	2,446.6
} others (2)	153.4	182.1	179.2	179.2	212.4	191.9
other lendings (2)	17.2	17.2	17.2	—	—	—
Lendings to the credit system:						
banks	1,669.0	1,828.8	1,546.3	1,930.2	1,505.3	2,358.4
advances } in current account	799.5	753.1	803.7	937.0	795.0	865.3
} at fixed term	408.1	578.5	402.4	479.6	396.3	758.6
discounts	461.4	497.2	340.2	513.6	314.0	734.5
deferred payments	—	—	—	—	—	—
special institutions	25.4	26.0	24.5	26.5	33.6	72.7
advances	1.0	2.7	1.6	2.6	5.7	16.9
discounts	5.5	5.5	4.4	4.5	5.1	12.7
bonds (2)	18.9	17.8	18.5	19.4	22.8	43.1
Lendings to the foreign sector, and gold	1,507.6	1,834.9	1,840.4	1,847.1	1,857.4	1,857.1
gold held	1,499.9	1,827.0	1,827.6	1,835.5	1,846.2	1,847.4
foreign currency holdings (2)	3.9	4.1	6.3	4.7	6.6	5.2
advances	—	—	2.7	3.1	0.8	0.8
bonds (2)	2.9	2.9	2.9	2.9	2.9	2.8
shares (2)	0.7	0.7	0.7	0.7	0.7	0.7
foreign currency securities representing debts of Italy (2)	0.2	0.2	0.2	0.2	0.2	0.2
Other lendings	91.4	105.1	113.2	111.4	102.8	120.5
advances	0.9	3.2	3.5	3.3	2.3	2.0
bonds (2)	10.2	10.1	10.1	10.1	10.1	9.9
shares (2)	47.9	52.9	54.9	52.6	52.9	52.7
other items (2)	32.4	38.9	44.7	45.4	37.5	55.9
Total items shown in consolidated statement	5,597.3	6,612.8	6,295.1	6,751.6	6,995.6	8,468.8
Lendings to the Italian Exchange Office	2,539.2	2,232.7	2,077.6	2,198.8	2,130.4	1,906.1
interest-bearing current account	2,474.0	2,085.9	1,837.9	1,884.9	1,622.7	1,626.2
special IMF account (2)	61.4	144.8	182.4	220.8	224.5	195.4
other special accounts (2)	3.7	1.9	57.2	93.0	283.1	84.4
endowment funds (2)	0.1	0.1	0.1	0.1	0.1	0.1
Other items	215.5	236.6	75.6	151.3	167.1	268.3
expenses less receipts	156.7	179.3	18.2	100.3	116.1	229.8
bills for collection	0.2	0.3	0.4	0.3	0.3	0.4
funds for administration	33.6	29.6	29.6	23.3	23.3	—
depreciation (2)	25.0	27.4	27.4	27.4	27.4	38.1
Total according to accounting statement	8,352.0	9,082.1	8,448.3	9,101.7	9,293.1	10,643.2

(1) Included in the item « domestic bills of exchange » in the official return.— (2) Included in the item « sundry debtors » in the official return.
(5) Included in the item « sight liabilities » in the official return.

POSITION

TABLE 30

in billions of lire)

Liabilities	1967 December	1968 December	1969			
			March	June	September	December
Deposits of the Treasury	3.0	—	1.3	—	80.8	112.7
accounts in lire (3)	3.0	—	—	—	—	—
accounts in foreign currency (3)	—	—	1.3	—	1.1	—
current account	—	—	—	—	79.7	112.7
Deposits of the credit system:						
banks						
obligatory reserves in cash (4)	2,138.6	2,412.1	2,510.6	2,656.8	2,519.5	2,758.4
other accounts	129.2	140.3	80.9	86.5	91.8	149.6
giro accounts and payment orders (5)	23.9	90.6	22.0	15.8	33.1	85.3
free current accounts	105.1	49.4	58.7	70.3	58.6	64.0
tied acc. { as cover for cashiers' checks	0.2	0.3	0.2	0.4	0.1	0.3
time balances . . . . .	..	..	..	..	..	..
Special institutions	142.3	198.3	31.5	108.3	26.7	221.0
free current accounts	142.3	128.5	8.0	72.0	10.1	17.6
cash services (3)	—	69.8	23.5	36.3	16.6	203.4
Deposits of the foreign sector	93.2	162.3	264.0	351.0	531.7	310.0
external accounts in lire (4)	23.6	12.0	20.4	32.1	19.5	25.0
IMF's deposits (3)	61.4	144.8	182.4	220.8	224.6	195.4
cash services (3)	1.2	1.4	0.8	2.0	1.4	2.1
cooperation agreements (3)	2.4	2.2	2.3	2.3	2.3	2.3
other accounts in lire (3)	4.6	1.9	58.0	93.7	283.9	85.2
accounts in foreign currency (3) . . . . .	..	..	0.1	0.1	..	..
Other deposits	66.9	51.6	48.1	94.6	56.7	157.9
free current accounts	8.4	8.3	7.4	9.0	9.0	5.2
other accounts in lire (3)	57.0	41.4	38.2	83.2	45.1	149.7
accounts in foreign currency (3)	1.5	1.9	2.5	2.4	2.6	3.0
Appropriations and miscellaneous items (3)	394.8	455.3	469.5	504.9	512.3	527.2
Capital and reserves	14.3	15.9	16.1	16.9	17.4	17.8
Circulation	5,154.1	5,409.6	4,950.6	5,131.2	5,289.0	6,120.2
notes	5,125.7	5,389.9	4,932.5	5,112.7	5,270.9	6,099.9
checks (5)	28.4	19.7	18.1	18.5	18.1	20.3
Total items shown in consolidated statement	8,136.4	8,845.4	8,372.6	8,950.2	9,125.9	10,374.8
Deposits of the Italian Exchange Office	0.1	0.1	0.1	0.2	0.1	0.1
free current account	0.1	0.1	0.1	0.2	0.1	0.1
Other items	215.5	236.6	75.6	151.3	167.1	268.3
expenses less receipts	156.7	179.3	18.2	100.3	116.1	229.8
depositors of bills for collection (3)	0.2	0.3	0.4	0.3	0.3	0.4
funds for administration (3)	33.6	29.6	29.6	23.3	23.3	—
depreciation (3)	25.0	27.4	27.4	27.4	27.4	38.1
Total according to accounting statement	8,352.0	9,082.1	8,448.3	9,101.7	9,293.1	10,643.2
Among the memorandum accounts the obligatory reserves in securities appear for the following amounts	2,146.7	2,420.4	2,510.8	2,539.5	2,576.3	2,555.3

return.— (3) Included in the item « sundry creditors » in the official return.— (4) Included in the item « tied accounts » in the official return.—

against sales and repayments totalling 810.7 billion (848.8 in 1968) and accounting deductions connected with the trend of security prices.

Altogether the Bank of Italy's participation in the issues of public securities allocated in 1969 amounted to 36.4 per cent, compared with 22.9 per cent in the previous year. A large proportion of total subscriptions was made in order to regulate liquidity flows to the market, since the issue of the securities by the Government is normally in advance of the time of the actual expenditure.

The Bank of Italy's direct interventions on the market resulted in an excess of purchases of 166 billion lire, against 429 billion of net sales in 1968.

The proportion represented by freely available public securities in relation to the total of the Bank's security holdings amounted last December to 78.8 per cent (Table 31). Within the remaining portion of securities there were increases in Government securities and bonds of special institutions used in reserve and appropriation funds and in the Treasury Bills used for the investment of obligatory reserves lodged in cash by the banks.

Altogether, during the year, the amount of securities held by the Bank was more than doubled, reaching 2,747.8 billion lire and the yearly average holding on a day-to-day basis increased by 76.4 per cent (from 946.0 to 1,668.9 billion).

The amount of bills rediscounted in respect of obligatory agricultural stockpiling and wheat purchase on behalf of the Government increased during the year owing to new presentations and, to a greater extent owing to the conversion into bills of the interest and tax connected with the renewal of the bills. At the end of 1969 the Bank's commitments for rediscounts in relation to the Government agricultural transactions amounted to 905.3 billion and represented 95.2 per cent of the total of financing of this type by the whole credit system.

The conditions governing financing of the credit system underwent major innovations during the year under review with regard to the cost of credit granted by the central bank. The standard discount rate and the interest rate on advances, which had remained fixed at the level of 3.50 per cent since 7th June 1958, were changed by four different measures introduced during 1969 and in March 1970.

BANK OF ITALY'S SECURITY HOLDINGS
(balance sheet values in billions of lire)

TABLE 31

Securities	Free	Obligatory reserves in cash	Reserves		Appropriations	Total	Average annual amount
			ordinary	extra-ordinary			
31st December 1968							
Fixed-interest:							
Treasury Bills	13.8	66.0	—	—	—	79.8	101.1
Postal interest-bearing certificates	175.0	—	—	—	—	175.0	22.7
Government securities	559.7	—	1.2	0.5	121.2	722.6	517.5
Bonds:							
autonomous government agencies	44.3	—	—	—	—	44.3	64.0
on behalf of the Treasury	135.8	—	0.1	0.4	58.7	195.0	157.6
ENEL-ENI-IRI	—	—	—	—	7.2	7.2	7.2
other bonds	—	—	0.2	—	20.6	20.8	21.3
Shares	—	—	7.5	5.0	40.3	52.8	50.9
Italian securities in foreign currency and foreign securities in lire	—	—	. .	0.3	3.4	3.7	3.7
Total . . .	968.6	66.0	9.0	6.2	251.4	1,301.2	946.0
31st December 1969							
Fixed-interest:							
Treasury Bills	55.0	282.0	—	—	—	337.0	226.4
Postal interest-bearing certificates	175.0	—	—	—	—	175.0	175.0
Government securities	840.6	—	6.9	3.8	127.3	978.6	735.6
Bonds:							
autonomous government agencies	132.5	—	—	—	—	132.5	62.2
on behalf of the Treasury	961.4	—	1.0	0.4	52.5	1,015.3	378.2
ENEL-ENI-IRI	—	—	—	—	7.0	7.0	7.1
other bonds	—	—	0.2	—	45.8	46.0	27.6
Shares	—	—	1.7	1.8	49.3	52.8	53.7
Italian securities in foreign currency and foreign securities in lire	—	—	—	0.3	3.3	3.6	3.1
Total . . .	2,164.5	282.0	9.8	6.3	285.2	2,747.8	1,668.9

The first measure concerned fixed-term advances, for which, in March 1969, there was introduced a system of progressive surcharges on the basic rate (from 0.5 points to a maximum of 1.5) depending on the frequency of operations during a half-year.

In the rediscount sector the Ministerial Decree of 21st June 1969 laid down that the official rate would continue to be applied at the level of 3.50 per cent to operations relating to: a) bills for the financing of past year's stockpiling programmes for wheat and other agricultural

products, or connected with the 1962-1963 and 1963-1964 wheat-marketing seasons, or agrarian bills issued in accordance with Art. 6 of Law No. 1760 of 5th July 1928; *b*) bills other than the above, if the banks concerned, in the preceding calendar half-year, had rediscounted bills of this type totalling, on an average, less than 5 per cent of the amount of the obligatory reserves constituted in the middle of the half-year. Exceeding of this limit entailed, from 1st July 1969, the application of a surcharge of 1.5 percentage points on the basic rate, which, however, was regarded as automatic for operations carried out by the registered central credit institutions.

Lastly, the Ministerial Decrees of 14th August 1969 and 7th March 1970, while they did not modify the rate applied to the operations referred to under sub-paragraph (*a*) above, raised the official rate for the others respectively to 4 and 5.50 per cent, leaving the standard for the application of the 1.5-point surcharge unchanged.

These decrees introduced increases of the same amount in the interest rate on current-account and fixed-term advances, the above-mentioned system of surcharges also remaining applicable to the latter.

Lending operations to the banks and special institutions amounted at the end of 1969 to 2,431.1 billion lire, representing an increase of 576.3 billion (against 160.4 billion in 1968), thus raising the proportion of the total represented by this item to 22.8 per cent.

The annual average amount of lendings to the credit system was 1,518.6 billion lire. The proportion represented by current-account advances declined to 49.2 per cent (62.9 in 1968), to the advantage of fixed-term advances and rediscounts (Table 32). The use of credit lines increased, during 1969, from 38.7 to 45.0 per cent for ordinary operations and from 95.3 to 98.1 per cent for special operations.

In the category of fixed-term advances, the Bank of Italy's total lendings to the banks in 1969 amounted to 6,679.5 billion lire; the number of banks which benefited by these operations during 1969 rose, although the main bulk of the lending was concentrated among a few of them.

There were also increases in the average amount of advances granted, from 15.8 to 22.6 billion lire, in the duration of the operations, practically all being for a period of 22 days, and in the rate of interest,

TABLE 32

LENDINGS TO THE CREDIT SYSTEM

(average amounts in billions of lire)

Items	Quarters				Year
	I	II	III	IV	
1968					
Advances in current account					
Securities deposited (1)	1,661.6	1,587.4	1,614.3	1,646.8	1,627.5
Treasury Bills	100.6	96.4	79.7	74.0	87.6
Government	590.7	602.6	633.4	651.2	619.5
on behalf of the Treasury	418.9	344.5	350.4	355.9	367.4
others	551.4	543.9	550.8	565.7	553.0
Credit lines (2)	1,275.2	1,215.3	1,237.3	1,263.4	1,247.8
outstanding (2)	663.5	643.7	622.6	614.6	636.1
used in %	52.0	53.0	50.3	48.6	51.0
Advances at fixed term (2)					
Securities deposited	145.2	167.7	182.5	286.7	195.5
Amount outstanding	117.2	135.3	146.4	228.9	157.0
Deferred payments (2) . . . . .	..	0.2	—	—	..
Discounts (2)	330.6	132.4	180.4	157.5	200.2
Bonds of special institutions (2)	18.7	18.2	18.0	17.8	18.2
Total lendings	1,130.0	929.8	967.4	1,018.8	1,011.5
1969					
Advances in current account					
Securities deposited (1)	1,681.4	1,715.7	1,747.5	1,793.1	1,734.4
Treasury Bills	74.1	74.0	65.8	60.9	68.7
Government	671.1	696.6	710.0	730.0	701.9
on behalf of the Treasury	321.0	291.6	294.7	319.6	306.7
others	615.2	653.5	677.0	682.6	657.1
Credit lines (2)	1,284.8	1,315.0	1,335.0	1,372.8	1,326.9
outstanding (2)	702.9	729.2	755.5	802.7	747.6
used in %	54.7	55.5	56.6	58.5	56.3
Advances at fixed term (2)					
Securities deposited	340.7	507.0	405.7	527.4	445.2
Amount outstanding	270.6	399.5	315.3	400.5	346.5
Deferred payments (2)	—	—	—	—	—
Discounts (2)	395.8	362.3	448.8	393.4	400.1
Bonds of special institutions (2)	18.0	18.8	20.8	40.0	24.4
Total lendings	1,387.3	1,509.8	1,540.4	1,636.6	1,518.6

(1) The total par value of securities at ends of months.— (2) at end of 10-day periods.

by virtue of the afore-mentioned measures introduced during the year under review.

In 1969 the average weighted rate paid on fixed-term advances was 4.70 per cent; the greater part of them, 61 per cent, were granted at rates of 5 and 5.50 per cent, the remainder being distributed in almost equal parts between operations carried out at 3.50 per cent and those at 4 and 4.50 per cent.

The total of bills accepted for rediscounting during 1969 amounted to 2,079.9 billion lire for ordinary discounts, representing an increase of 85 per cent over the corresponding figure for 1968. The portion in respect of the first half-year (884.1 billion) was rediscounted at the old rate of 3.50 per cent, while the operations carried out in the second half-year (1,195.8 billion) were effected at an average weighted rate of 5.12 per cent.

With regard to the liabilities of the Bank of Italy to the credit system, the banks' obligatory reserves, deposited in cash, increased by 14.4 per cent (12.8 in 1968) from December to December, following an increase of 11.8 per cent in the banks' deposits subject to reserve between November 1968 and November 1969 and a larger excess of the amount deposited over that required.

At the end of 1969 the proportion of the Bank's lendings to individuals and miscellaneous bodies in relation to the total of its assets was about 11 per cent, that is, practically the same as at the end of 1968.

The issue of the Bank of Italy's checks was about the same as in the preceding year with regard to its overall total, the number of checks and their average amount, while their average life increased from 6.37 to 7.61 days and the average volume of checks in circulation increased only slightly (Table 33).

Notes in circulation reached 6,099.9 billion lire at the end of 1969, having increased during the year by 710.0 billion compared with 264.2 billion in 1968. The growth in the average volume in 1969, however, was no different from that in 1968, having been a little over 9 per cent in both years. The monthly increases varied, during the first seven months of the year, around an average of 7.4 per cent (against 9.1 per cent in the corresponding period of 1968), while in the period August-December the figure rose to 11.5 per cent (against 9.5 in 1968).

TABLE 33

BANK OF ITALY'S NOTES AND CHECKS IN CIRCULATION

Period	Notes in circulation			Bank checks				
	At end of month		average	average	issued			average life in days
	not seasonally adjusted	seasonally adjusted			value	number	average amount	
	<i>(billions)</i>				<i>(thousands)</i>			
1967 - Year . . .	—	—	4,222.8	21.2	1,657.6	1,218	1,371.0	5.48
1968 - Jan. . . .	4,535.0	4,539.5	4,628.2	23.0	140.3	118	1,189.0	4.32
Feb. . . .	4,446.4	4,551.1	4,378.6	17.8	75.2	73	1,030.1	5.74
Mar. . . .	4,547.0	4,602.2	4,399.0	17.9	91.8	84	1,092.9	6.02
Apr. . . .	4,552.4	4,640.6	4,486.4	20.3	100.7	92	1,094.6	6.12
May . . .	4,602.4	4,691.5	4,497.2	18.6	100.3	96	1,044.8	6.52
Jun. . . .	4,780.2	4,742.3	4,566.1	18.9	88.0	87	1,011.5	6.43
Jul. . . .	4,843.3	4,743.7	4,686.5	20.3	111.0	104	1,067.3	6.51
Aug. . . .	4,747.1	4,771.0	4,766.3	19.3	88.0	82	1,073.2	6.57
Sep. . . .	4,785.6	4,814.5	4,651.7	18.7	86.1	85	1,012.9	7.30
Oct. . . .	4,695.1	4,830.3	4,637.4	18.0	94.2	92	1,023.9	6.90
Nov. . . .	4,741.7	4,853.3	4,607.0	18.9	89.7	85	1,055.3	6.91
Dec . . .	5,389.9	4,864.5	5,072.5	22.2	108.4	116	934.5	7.06
Year . . .	—	—	4,614.7	19.5	1,173.7	1,114	1,052.5	6.37
1969 - Jan. . . .	4,872.5	4,887.2	4,950.0	20.5	110.1	121	909.9	6.89
Feb. . . .	4,831.7	4,945.4	4,706.4	19.3	76.9	72	1,068.1	7.34
Mar. . . .	4,932.5	4,982.3	4,764.9	18.9	98.9	87	1,136.8	6.83
Apr. . . .	4,892.2	4,987.0	4,837.6	19.5	94.8	86	1,102.3	7.02
May . . .	4,914.3	5,019.7	4,806.4	27.0	110.7	91	1,216.5	9.01
Jun. . . .	5,112.7	5,072.1	4,881.7	20.6	87.7	89	985.4	7.93
Jul. . . .	5,261.5	5,163.4	5,041.6	22.1	108.1	100	1,081.0	7.04
Aug. . . .	5,311.3	5,332.6	5,267.2	22.4	89.9	84	1,070.2	7.06
Sep. . . .	5,270.9	5,308.1	5,175.2	18.4	89.1	93	958.1	7.51
Oct. . . .	5,218.7	5,380.1	5,138.0	21.1	102.6	101	1,015.8	7.14
Nov. . . .	5,330.5	5,444.8	5,172.1	25.2	88.7	86	1,031.4	9.05
Dec . . .	6,099.9	5,485.5	5,715.9	27.6	110.8	106	1,045.3	8.37
Year . . .	—	—	5,038.1	21.9	1,168.3	1,116	1,051.7	7.61

The ratio, on an annual basis, between the gross national product at current prices and the average circulation, including Government notes and coin, showed an upward trend during the first three quarters of the year, as a result of a rise in the GNP amounting, at the end of September, to 10.6 per cent and an increase of 8.4 per cent in the circulation. Subsequently, the reduction in production in the fourth quarter having reduced the growth in the national product for 1969 as a whole

to 9.2 per cent, that is, the same as the increase in the circulation, the indices of the ratio returned to their initial levels (Table 34 and Chart 12).

TABLE 34

GROSS NATIONAL PRODUCT AND CURRENCY CIRCULATION

(the figures relate to the 12 months ending with the month shown)

Period	Wage and salary income (WSI)				GNP less WSI	Gross national product (GNP)	Average circulation of bank notes plus Government notes and coin (C)	WSI	GNP-WSI	GNP
	domestic		foreign	total				C	C	C
	private sector	public sector						1966 = 100		
	(billions of lire)									
1967 - Dec. . . .	15,476	4,256	258	19,990	23,814	43,804	(1)4,484	102.7	102.2	102.4
1968 - Mar. . . .	15,794	4,330	256	20,380	24,168	44,548	4,589	102.3	101.4	101.8
Jun. . . .	15,984	4,417	252	20,653	24,616	45,269	4,686	101.5	101.1	101.3
Sep. . . .	16,520	4,509	255	21,284	24,772	46,056	4,794	102.2	99.5	100.7
Dec. . . .	16,802	4,595	280	21,677	25,457	47,134	4,889	102.1	100.2	101.1
1969 - Mar. . . .	17,101	4,691	287	22,079	26,165	48,244	4,988	101.9	101.0	101.4
Jun. . . .	17,519	4,787	297	22,603	26,884	49,487	5,075	102.6	102.0	102.2
Sep. . . .	17,989	4,873	326	23,188	27,735	50,923	5,195	102.8	102.8	102.8
Dec	18,388	4,927	324	23,639	27,817	51,456	5,341	101.9	100.3	101.0

(1) Adjusted for the incidental factor due to the bank employees' strike.

The overall deficit in Italy's balance of payments in 1969, amounting to 869.5 billion lire, entailed a reduction of only 440.4 billion in the IEO's foreign assets and liabilities (314.9 billion) and in those of the Bank of Italy (125.5 billion), having been financed to the extent of 429.1 billion by the reduction in the banks' net foreign assets (Table 35).

At the end of 1969 gold held amounted to 1,847.4 billion lire, a rise of 20.4 billion over the end-1968 level. The increases in the gold reserve were due mainly to purchases from the IMF and to the receipt of 4.8 billion in respect of interest and commissions, over against negative changes consisting mainly of sales to the BIS for the conversion into gold of its profits (1.5 billion) and to the Central Bank of Somalia (0.5 billion).

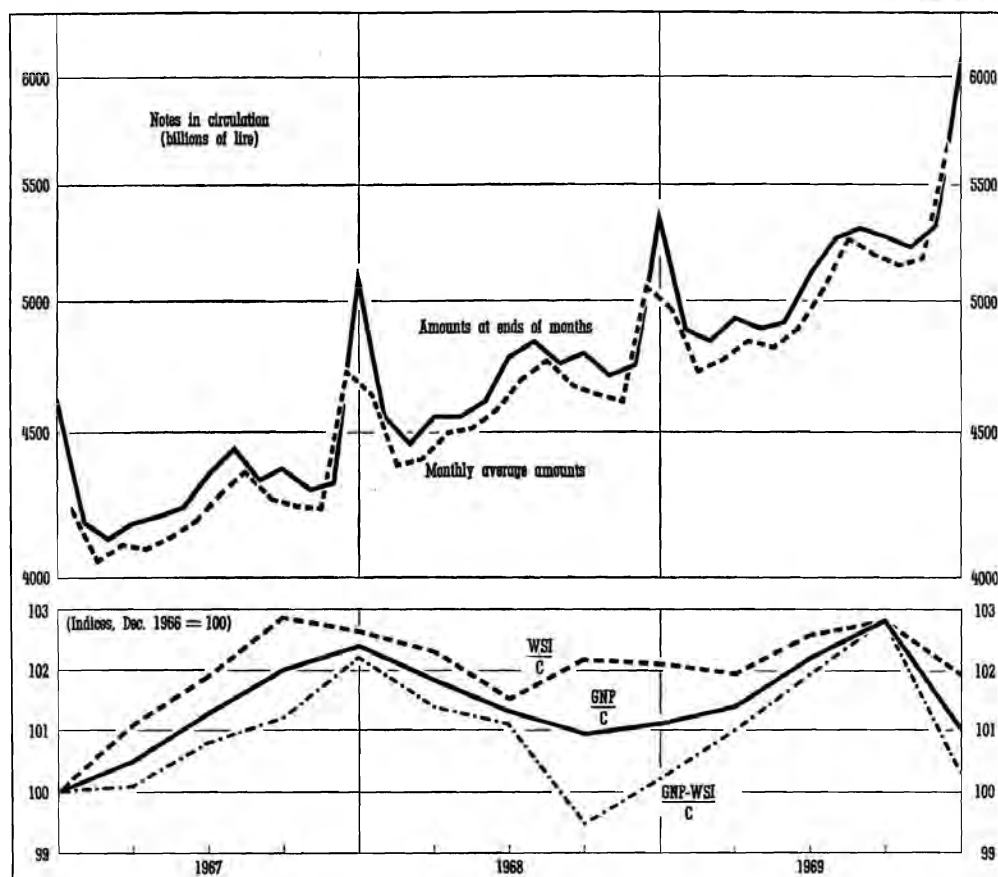
TABLE 35

FOREIGN POSITION IN GOLD, FOREIGN CURRENCIES AND LIRE
OF THE BANK OF ITALY AND THE ITALIAN EXCHANGE OFFICE
(billions of lire)

Items	Bank of Italy		IEO		Total		Bank of Italy		IEO		Total	
	1968	1969	1968	1969	1968	1969	1968	1969	1968	1969	1968	1969
	<i>amounts</i> (+ assets. — liabilities)						<i>changes</i> (+ increase in assets and decrease in liabilities, — decrease in assets and increase in liabilities)					
Foreign assets	1,834.9	1,857.1	2,100.5	1,786.5	3,935.4	3,643.6	329.7	22.2	-375.5	-314.0	-45.8	-291.8
Gold	1,827.0	1,847.4	—	—	1,827.0	1,847.4	327.1	20.4	—	—	327.1	20.4
Reserves with gold guarantee	—	—	561.0	541.3	561.0	541.3	—	—	32.9	-19.7	32.9	-19.7
Net IMF position	—	—	245.9	195.3	245.9	195.3	—	—	-83.4	-50.6	-83.4	-50.6
gold tranche	—	—	97.7	97.7	97.7	97.7	—	—	—	—	—	—
lira tranche	—	—	148.2	97.6	148.2	97.6	—	—	-83.4	-50.6	-83.4	-50.6
IMF gold certificates	—	—	156.2	156.2	156.2	156.2	—	—	—	—	—	—
EMF gold tranche	—	—	2.0	2.0	2.0	2.0	—	—	—	—	—	—
GAB certificates	—	—	156.9	187.8	156.9	187.8	—	—	116.3	30.9	116.3	30.9
Reserves with lira guarantee	—	—	78.0	98.0	78.0	98.0	—	—	-312.5	20.0	-312.5	20.0
Short-term foreign securities	—	—	78.0	98.0	78.0	98.0	—	—	—	20.0	—	20.0
Central bank swaps	—	—	—	—	—	—	—	—	-312.5	—	-312.5	—
Cash and short-term securities	4.1	5.2	597.1	558.2	601.2	563.4	2.6	1.1	-288.3	-38.9	-285.7	-37.8
Available at sight	4.1	5.2	457.8	344.2	461.9	349.4	2.6	1.1	172.9	-113.6	175.5	-112.5
Foreign Treasury Notes	—	—	139.3	214.0	139.3	214.0	—	—	-461.2	74.7	-461.2	74.7
Assets at medium and long-term	3.8	4.5	719.6	393.6	723.4	398.1	—	0.7	187.1	-326.0	187.1	-325.3
Foreign securities: in foreign currency	0.7	0.7	125.6	22.1	126.3	22.8	—	—	-29.0	-103.5	-29.0	-103.5
in lire	2.9	3.6	184.0	98.5	186.9	102.1	—	0.7	124.8	-85.5	124.8	-84.8
Consolidated lendings and special accounts	—	0.2	101.2	83.7	101.2	83.7	—	—	44.3	-17.5	44.3	-17.5
Italian securities in foreign currency	0.2	—	308.8	189.3	309.0	189.5	—	—	47.0	-119.5	47.0	-119.5
Items offset on liabilities side	—	—	144.8	195.4	144.8	195.4	—	—	5.3	50.6	5.3	50.6
IMF's lira deposits	—	—	144.8	195.4	144.8	195.4	—	—	83.4	50.6	83.4	50.6
Short-term transactions	—	—	—	—	—	—	—	—	-78.1	—	-78.1	—
Non-residents' deposits	-162.3	-310.0	-2.7	-3.6	-165.0	-313.6	-72.7	-147.7	80.6	-0.9	7.9	-148.6
Accounts in lire	-17.5	-114.6	-1.9	-2.5	-19.4	-117.1	10.7	-97.1	2.3	-0.6	13.0	-97.7
Accounts in foreign exchange	—	—	-0.8	-1.1	-0.8	-1.1	—	—	0.2	-0.3	0.2	-0.3
Items offset on assets side	-144.8	-195.4	—	—	-144.8	-195.4	-83.4	-50.6	78.1	—	-5.3	-50.6
IMF's lira deposits	-144.8	-195.4	—	—	-144.8	-195.4	-83.4	-50.6	—	—	-83.4	-50.6
Short-term transactions	—	—	—	—	—	—	—	—	78.1	—	78.1	—
Net position	1,672.6	1,547.1	2,097.8	1,782.9	3,770.4	3,330.0	257.0	-125.5	-294.9	-314.9	-37.9	-440.4
Foreign transactions									-294.9	-314.9		
Deposits in lire									-81.7	-133.0		
Domestic transactions									-11.5	-11.8		
IEO current account									-388.1	-459.7		

The balance of the current account held with the Bank by the Italian Exchange Office was reduced during 1969 by 459.7 billion lire. Of this, 314.9 billion was attributable to the decline in the IEO's foreign position, 82.4 billion was due to the increase in lira liabilities, mainly as a result of operations with the Federal Reserve, 50.6 billion was due to the increase in the IMF's lira holdings and the remainder was due to domestic transactions.

CHART 12



Notes in circulation and ratio between gross national product and circulation

Of the increase in the IMF's lira deposits in 1969, 5.3 billion was attributable to the excess of payments made by foreign central banks in respect of drawings, 17.0 billion to the crediting to the Fund of the countervalue of the afore-mentioned gold purchase by the Bank and 31.5 billion to Italian payments under the GAB, while 3.2 billion of profits was transferred by the Fund to Italy.

The Italian Exchange Office's Balance Sheet.— The IEO's total assets declined in 1969 by 255.0 billion lire, which was a smaller decrease than in the preceding year (369.5 billion).

From December to December the IEO's foreign lendings fell from 2,100.5 to 1,786.5 billion lire and their proportion of the total declined from 87.1 to 82.8 per cent (Table 36). With regard to short-term assets, which went up by 12.0 billion, the largest changes were: *a*) the increase in GAB gold certificates (from 156.9 to 187.8 billion) as a result of the implementation and the net cancellation of credits to France (19.1 billion) and Great Britain (28.8 billion) respectively, and of the transfer to Italy of part of the IMF's indebtedness to Germany (40.6 billion); *b*) the decline in convertible currencies (from 675.1 to 656.2 billion) due to a fall in sight assets and cash coupled with an increase in foreign securities, mainly attributable to the transfer of securities maturing in 1970 from the medium and long-term sector to the short-term sector. These operations concerned the lira bonds issued by Canada (20 billion) and those issued in dollars by the U.S. Treasury (84.4 billion), the IBRD (13.8 billion) and the UNO (0.2 billion).

Medium and long-term assets fell, from December to December, by 326.0 billion lire (from 719.6 to 393.6 billion). The largest changes were in foreign securities owing to the afore-mentioned transfers and to the premature redemption of the lira bonds issued by the United States (62.5 billion); other factors were the partial repayment of the credit to the Bank of England and the sales of Italian foreign exchange securities (IMI-EXIMBANK), which fell from 111.8 to 2.8 billion.

Consolidated position of the Bank of Italy and the Italian Exchange Office.— The consolidation of the accounts of the Bank of Italy and the IEO, homogenously classified by major sectors, makes possible an overall examination of the inter-relationships between the changes in the note circulation and the trend of the operations of the two institutions with the foreign sector, the Treasury and the domestic market (Table 37).

ITALIAN EXCHANGE

(at ends of months;

Assets	1967 December	1968 December	1969			
			March	June	September	December
Lendings to the Treasury	242.0	241.8	252.4	291.9	316.8	302.1
transfers in foreign currency	23.5	30.9	41.8	68.2	95.4	85.9
financing of stockpiles	47.8	48.4	48.4	48.7	48.7	49.0
other accounts in lire	52.5	44.1	44.0	41.0	41.9	41.8
accounts in foreign currency	3.8	—	—	—	—	—
securities: freely available	107.3	110.5	110.3	125.0	121.6	116.4
others	7.1	7.9	7.9	9.0	9.2	9.0
Lending to the credit system:						
banks	0.4	0.1	0.2	0.1	0.1	0.1
accounts: in lire	—	—	—	—	—	—
in foreign currency	0.4	0.1	0.2	0.1	0.1	0.1
special institutions	33.1	46.5	47.3	47.3	47.3	46.6
accounts in foreign currency	23.0	36.6	37.4	37.4	37.4	37.4
securities: freely available	10.0	9.8	9.8	9.8	9.8	9.1
others	0.1	0.1	0.1	0.1	0.1	0.1
Foreign assets	2,476.0	2,100.5	1,954.4	2,050.4	1,979.7	1,786.5
IMF gold tranche	97.7	97.7	97.7	97.7	97.7	97.7
IMF lira tranche	293.0	293.0	293.0	293.0	293.0	293.0
EMF gold tranche	2.0	2.0	2.0	2.0	2.0	2.0
IMF gold certificate	156.2	156.2	156.2	156.2	156.2	156.2
GAB gold certificates	40.6	156.9	130.0	128.1	147.2	187.8
holdings available at sight	363.0	457.8	395.2	488.1	440.7	344.2
swaps	312.5	—	—	—	—	—
foreign securities:						
short-term: in lire	78.0	78.0	78.0	78.0	78.0	98.0
in foreign currency	600.5	139.3	84.6	87.6	319.0	214.0
long-term: in lire	59.2	184.0	183.6	182.8	99.7	98.5
in foreign currency	154.6	125.6	125.2	124.6	63.6	22.1
consolidated accounts and special accounts:						
in lire	48.3	35.2	39.5	36.9	36.9	34.4
in foreign currency	8.6	66.0	65.9	65.2	57.6	49.3
foreign currency securities representing debts of Italy	261.8	308.8	303.5	310.2	188.1	189.3
Other lendings	23.8	22.0	8.8	24.1	13.3	20.6
Securities in lire	5.4	5.4	4.5	4.5	4.5	4.3
other securities	18.4	16.6	4.3	19.6	8.8	16.3
Total items shown in consolidated statement	2,775.3	2,410.9	2,263.1	2,413.8	2,357.2	2,155.9
Lendings to the Bank of Italy	0.1	0.1	0.1	0.2	0.1	0.1
current account at Rome office of Bank of Italy	0.1	0.1	0.1	0.2	0.1	0.1
Other items	6.3	1.2	1.2	1.2	1.2	1.2
items offset on liabilities side	5.1	—	—	—	—	—
depreciation	1.2	1.2	1.2	1.2	1.2	1.2
Total according to accounting statement	2,781.7	2,412.2	2,264.4	2,415.2	2,358.5	2,157.2

OFFICE POSITION

TABLE 36

in billions of lire)

Liabilities	1967 December	1968 December	1969			
			March	June	September	December
Deposits of the Treasury	22.6	39.9	37.0	49.8	50.5	43.2
accounts: in lire	2.2	2.0	3.6	4.5	3.1	2.5
in foreign currency	20.4	37.9	33.4	45.3	47.4	40.7
Deposits of the credit system:						
banks . . . . .	—	..	..	..	0.1	..
accounts: in lire	—	—	—	—	—	—
in foreign currency . . . . .	—	..	..	..	0.1	..
special institutions	18.8	21.4	23.9	23.2	23.3	59.9
accounts: in lire	—	—	—	—	—	—
in foreign currency	18.8	21.4	23.9	23.2	23.3	59.9
Non-residents' deposits	83.3	2.7	3.4	3.5	3.3	3.6
external accounts in lire	3.5	0.8	1.4	1.7	1.3	1.1
special accounts in lire	0.7	1.1	1.6	1.4	1.4	1.4
accounts in foreign currency	—	—	—	—	—	—
special accounts in foreign currency	79.1	0.8	0.4	0.4	0.6	1.1
Other deposits	22.0	12.0	12.3	31.6	32.0	19.2
payment orders	12.0	8.2	7.9	24.6	20.1	11.3
other accounts in lire	10.0	3.5	4.0	5.1	11.4	7.4
accounts in foreign currency	—	0.3	0.4	1.9	0.5	0.5
Appropriations and miscellaneous items	89.2	102.0	108.7	106.7	117.3	123.6
Reserve fund	0.3	0.3	0.3	0.4	0.4	0.4
Total items shown in consolidated statement	236.2	178.3	185.6	215.2	226.9	249.9
Lendings by the Bank of Italy	2,539.2	2,232.7	2,077.6	2,198.8	2,130.4	1,906.1
interest-bearing current account	2,474.0	2,085.9	1,837.9	1,884.9	1,622.7	1,626.2
special IMF account	61.4	144.8	182.4	220.8	224.5	195.4
other special accounts	3.7	1.9	57.2	93.0	283.1	84.4
endowment fund	0.1	0.1	0.1	0.1	0.1	0.1
Other items	6.3	1.2	1.2	1.2	1.2	1.2
items offset on assets side	5.1	—	—	—	—	—
depreciation	1.2	1.2	1.2	1.2	1.2	1.2
Total according to accounting statement	2,781.7	2,412.2	2,264.4	2,415.2	2,358.5	2,157.2

In 1969 monetary gold and net foreign lendings declined by 11.7 per cent, falling from 3,770.4 to 3,330.0 billion lire. In particular, at the end of the year under review gold represented 27.2 per cent of the circulation and the assets of the two bodies, cash and short-term

CONSOLIDATED POSITION OF THE BANK OF ITALY
AND THE ITALIAN EXCHANGE OFFICE
(at ends of months; in billions of lire)

TABLE 37

Sectors	1967	1968	1969			
	December	December	March	June	September	December
ASSETS						
Lendings to the Treasury	2,545.9	3,059.8	3,023.1	3,128.3	3,813.3	4,362.2
Securities	1,014.5	1,335.1	1,238.0	1,591.9	2,269.3	2,763.9
Loans	1,531.4	1,724.7	1,785.1	1,536.4	1,544.0	1,598.3
Lendings to the credit system:						
Banks	1,669.4	1,828.9	1,546.5	1,930.3	1,505.4	2,358.5
Special credit institutions	58.5	72.5	71.8	73.8	80.9	119.3
Lendings to the foreign sector and gold	3,983.6	3,935.4	3,794.8	3,897.5	3,837.1	3,643.6
Gold held	1,499.9	1,827.0	1,827.6	1,835.5	1,846.2	1,847.4
Cash and short-term securities	1,947.4	1,385.0	1,245.7	1,338.5	1,541.2	1,398.9
Assets at medium and long-term . . .	536.3	723.4	721.5	723.5	449.7	397.3
Other lendings	115.2	127.1	122.0	135.5	116.1	141.1
Total . . .	8,372.6	9,023.7	8,558.2	9,165.4	9,352.8	10,624.7
LIABILITIES						
Deposits and credits of the Treasury . .	25.6	39.9	38.3	49.8	131.3	155.9
Deposits of the credit system:						
Banks	2,267.8	2,552.4	2,591.5	2,743.3	2,611.4	2,908.0
Obligatory reserves in cash	2,138.6	2,412.1	2,510.6	2,656.8	2,519.5	2,758.4
other accounts	129.2	140.3	80.9	86.5	91.9	149.6
Special credit institutions	161.1	219.7	55.4	131.5	50.0	280.9
Deposits of the foreign sector	176.5	165.0	267.4	354.5	535.0	313.6
Other deposits	88.9	63.6	60.4	126.2	88.7	177.1
Capital resources	498.6	573.5	594.6	628.9	647.4	669.0
Currency circulation	5,154.1	5,409.6	4,950.6	5,131.2	5,289.0	6,120.2
Total . . .	8,372.6	9,023.7	8,558.2	9,165.4	9,352.8	10,624.7

securities less foreigners' deposits accounted for 16.0 per cent and medium and long-term assets for 5.9 per cent. With regard to relations with the Treasury, the expansion in security holdings, which were more than doubled in 1969, over against a reduction of 14.4 per cent in other net assets, raised the contribution of that sector from 50.5 to 62.0 per cent of the combined amount of the circulation and

assets. These two items of the consolidated liabilities showed a December-to-December overall increase of 806.1 billion (against 330.4 billion in 1968), associated from the accounting point of view with different behaviour of various operating sectors during the year under review; emphasis should be laid in this connection on the continuance of the expansionary trend in the Treasury sector at a higher rate than in 1968; a similar development took place in the case of the banks, which in the previous year, on the other hand, had had a negative effect on the volume of the circulation. Lastly, the foreign position as a whole showed a more marked tendency to operate as a restrictive factor, in comparison with its modest limiting effect at the end of December 1968 (Table 38).

TABLE 38

**SUMMARISED CONSOLIDATED BALANCE SHEET OF THE BANK OF ITALY
AND THE ITALIAN EXCHANGE OFFICE**
(billions of lire)

Sectors	Assets			Liabilities			Balance		
	December		change	December		change	December		change
	1968	1969		1968	1969		1968	1969	
<i>(amounts at end of year)</i>									
Foreign sector and monetary gold . . .	3,935.4	3,643.6	- 291.8	165.0	313.6	148.6	3,770.4	3,330.0	- 440.4
Treasury	3,059.8	4,362.2	1,302.4	39.9	155.9	116.0	3,019.9	4,206.3	1,186.4
Banks	1,828.9	2,358.5	529.6	2,552.4	2,908.0	355.6	- 723.5	- 549.5	174.0
Special institutions . .	72.5	119.3	46.8	219.7	280.9	61.2	- 147.2	- 161.6	- 14.4
Other items	127.1	141.1	14.0	63.6	177.1	113.5	63.5	- 36.0	- 99.5
Circulation (notes and checks)	—	—	—	5,409.6	6,120.2	710.6	- 5,409.6	- 6,120.2	- 710.6
Capital resources . . .	—	—	—	573.5	669.0	95.5	- 573.5	- 669.0	- 95.5
Total . . .	9,023.7	10,624.7	1,601.0	9,023.7	10,624.7	1,601.0	—	—	—
<i>(average yearly amounts) (1)</i>									
Foreign sector and monetary gold . . .	3,916.1	3,813.7	- 102.4	106.6	335.9	229.3	3,809.5	3,477.8	- 331.7
Treasury	2,729.9	3,420.3	690.4	38.1	84.2	46.1	2,691.8	3,336.1	644.3
Banks	1,104.9	1,624.2	519.3	2,366.9	2,666.7	299.8	- 1,262.0	- 1,042.5	219.5
Special institutions . .	61.5	84.1	22.6	71.1	74.3	3.2	9.6	9.8	19.4
Other items	105.4	111.1	5.7	54.6	74.3	19.7	50.8	36.8	- 14.0
Circulation (notes and checks)	—	—	—	4,740.5	5,190.9	450.4	- 4,740.5	- 5,190.9	- 450.4
Capital resources . . .	—	—	—	540.0	627.1	87.1	- 540.0	- 627.1	- 87.1
Total . . .	7,917.8	9,053.4	1,135.6	7,917.8	9,053.4	1,135.6	—	—	—

(1) On the basis of the balances of the end-of-month statements.

Monetary base

During 1969 the total volume of monetary base increased by 1,245 billion lire, an amount similar to the one experienced in the preceding year (1,241 billion). The increase was due to 1,500 billion of financing to the Treasury and 476 billion of financing to the banks. The foreign sector, on the other hand, taking also into account the reduction in the banks' foreign position, absorbed monetary base to the extent of 648 billion lire, while the « other sectors » (an item which combines the minor operations of the BI-IEO) absorbed 83 billion.

Of the new monetary base, 1,153 billion lire were held by the public and non-bank financial intermediaries, while 92 billion went to the banks (Table 39).

The annual amounts given above are the result of somewhat irregular movements during the year.

During the first half-year, at a time of increasing deficit in the country's foreign accounts, but still without any large increase in prices, the growth in the monetary base was sufficient to permit expansion of the system's liquidity at virtually stable interest rates; the distinct slowing down in the increase in monetary base which took place in the second quarter, as shown by the seasonally adjusted figures, did not prevent a steady expansion in lendings and deposits during this period, having been offset largely by a decrease in banks' excess reserves. Also in the first half of the year, despite the raising of the rate on advances by the Bank of Italy, the level of market rates (bond yields and rates on bank lending) was kept unchanged by a marked stepping-up of open market purchases of securities by the central bank.

In the third quarter, in connection with a more pronounced rise in the general level of prices and the resulting emergence of inflationary expectations, and with a deficit on foreign account tending to go far beyond the stated limit of compatibility with the policy of interest-rate stability, the rate of increase in monetary base was further reduced down to a level of about 3 per cent per annum (Table 40). In the meantime there was a sharp rise in the demand for monetary base on the part of the public, and consequently a further reduction, according to the seasonally adjusted figures, in banks' excess reserves, and a slackening of the rate of expansion of bank lending. The expansion of the mon-

MONETARY BASE CREATION

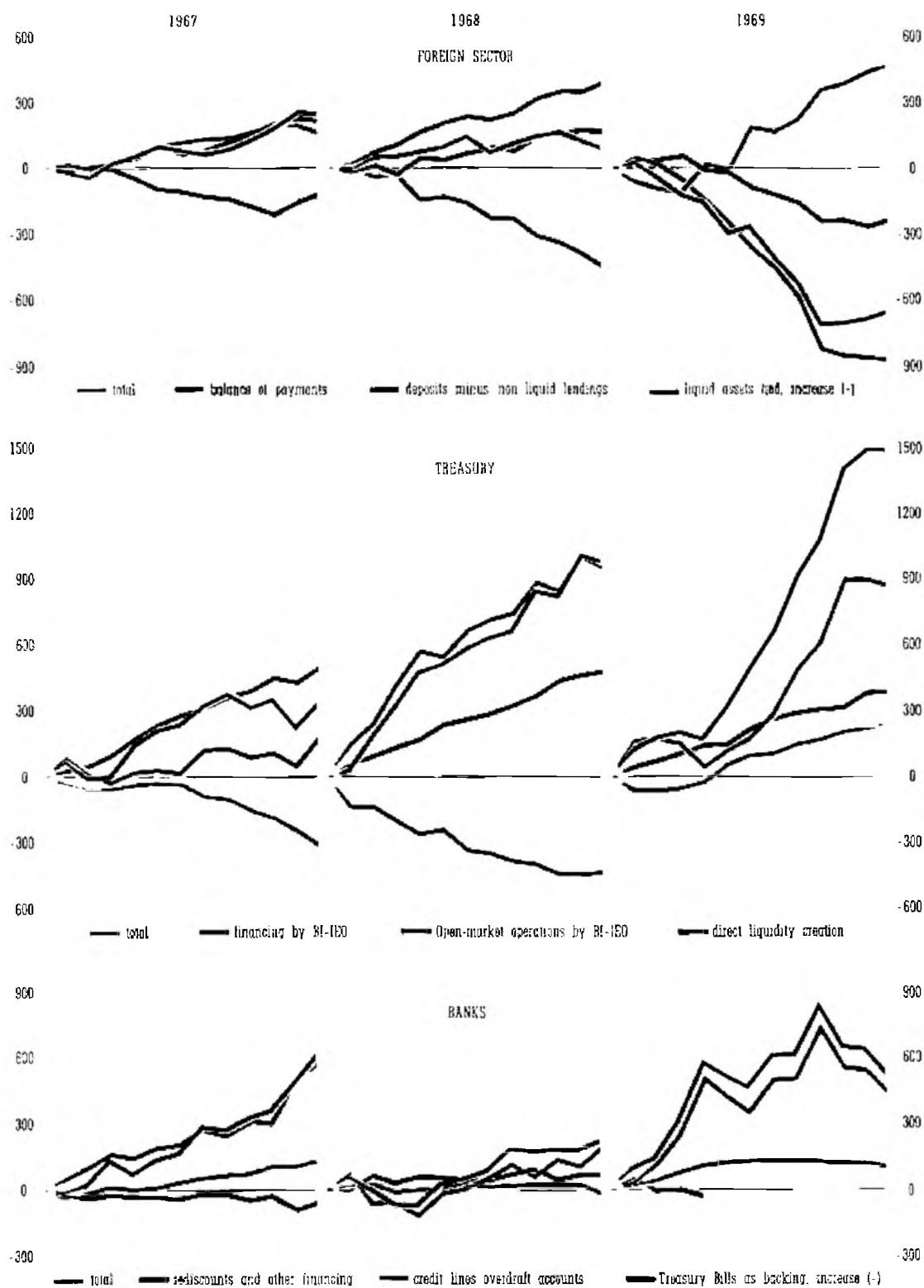
(cumulative monthly changes; seasonally adjusted figures; billions of lire)

TABLE 39

MONETARY BASE
(changes in billions of lire)

Items	1967	1968	1969	1969 by quarters			
				I	II	III	IV
SOURCES							
Foreign sector	242.9	122.6	- 647.9	- 234.2	- 144.8	- 223.6	- 45.3
autonomous factors	202.4	393.3	- 869.2	- 226.9	- 334.4	- 201.3	- 106.6
action by monetary authorities	40.5	- 270.7	221.3	- 7.3	189.6	- 22.3	61.3
Treasury	404.6	921.8	1,500.4	- 25.1	113.4	699.6	712.5
Treasury: excluding open-market operations by BI-IEO	(711.0)	(1,345.5)	(1,232.6)	(23.9)	(- 40.7)	(627.4)	(622.0)
autonomous factors	1,274.4	2,044.6	1,766.0	379.3	220.5	659.6	506.6
action by monetary authorities	- 869.8	- 1,122.8	- 265.6	- 404.4	- 107.1	40.0	205.9
Banks	626.6	220.5	475.9	- 287.9	222.4	- 259.6	801.0
Other sectors	- 57.8	- 23.8	- 83.1	- 24.6	- 83.0	6.7	17.8
Total . . .	1,216.3	1,241.1	1,245.3	- 571.8	108.0	223.1	1,486.0
autonomous factors	1,476.8	2,437.9	896.8	152.4	- 113.9	458.3	400.0
action by monetary authorities	- 260.5	- 1,196.8	348.5	- 724.2	221.9	- 235.2	1,086.0
USES							
Public and non-bank financial intermediaries	1,017.7	576.8	1,153.1	- 535.0	289.0	159.2	1,239.9
Public	951.0	518.5	1,095.7	- 372.4	213.1	244.6	1,010.4
notes and coin	486.2	207.2	707.0	- 371.0	160.1	184.6	733.3
Treasury bills and deposits with the Treasury and BI (1)	18.3	- 43.5	15.3	- 11.8	- 9.3	53.7	- 17.3
Deposits with the Post Office	446.5	354.8	373.4	10.4	62.3	6.3	294.4
Special credit institutions	66.7	58.3	57.4	- 162.6	75.9	- 85.4	229.5
Banks	198.6	664.3	92.2	- 36.8	- 181.0	63.9	246.1
Obligatory reserves and backing for cashiers' cheques (*)	249.6	402.9	415.5	134.7	171.4	- 97.1	206.5
cash	217.5	273.6	346.3	98.4	146.4	- 137.6	239.1
Treasury bills (2)	- 30.4	109.3	69.2	36.3	25.0	40.5	- 32.6
special reserves in securities (3)	62.5	20.0	—	—	—	—	—
Excess reserves	- 51.0	261.4	- 323.3	- 171.5	- 352.4	161.0	39.6
cash	56.6	70.6	14.4	- 87.9	18.6	- 18.7	102.4
sight deposits with BI	19.2	11.0	9.3	- 59.2	5.3	5.7	57.5
unused margin on overdrafts	- 11.0	8.1	- 24.4	- 6.3	- 131.3	165.3	- 52.1
Treasury bills and other claims on the Treasury (4)	- 34.2	12.4	- 114.6	- 27.0	- 84.6	- 8.6	5.6
convertible currencies	- 81.6	159.3	- 208.0	8.9	- 160.4	17.3	- 73.8
(*) Long-term securities in the obligatory reserve	487.2	461.2	397.0	164.7	56.1	6.4	169.8

(1) Including the Bank of Italy's checks and excluding, from May 1969, Treasury bills.— (2) Excluding, from May 1969, Treasury bills as backing for cashiers' checks.— (3) Taken from the BI's holdings and used, in place of cash or Treasury bills, for reserves already created or in course of creation.— (4) Treasury bills are excluded from May 1969 onwards.

SOURCES AND USES

Items	1967				
	quarters				Year
	I	II	III	IV	
SOURCES					
Foreign sector	- 136.1	46.4	351.1	- 18.5	242.9
Balance of payments (1)	- 179.3	41.1	362.4	- 21.8	202.4
Banks' transactions with non-residents	34.3	145.5	- 69.3	57.6	168.1
Liquid assets tied	8.9	- 140.2	58.0	- 54.3	- 127.6
Treasury	- 149.5	100.1	156.1	297.9	404.6
Financing by BI-IEO	- 240.7	30.7	13.2	54.7	- 142.1
(of which: open-market operations by BI-IEO (2)	(- 54.0)	(28.4)	(- 121.5)	(- 159.3)	(- 306.4)
Direct liquidity creation (3)	91.2	69.4	142.9	243.2	546.7
Banks (4)	- 137.0	- 47.4	- 10.3	821.3	626.6
Other sectors	8.4	- 7.1	- 10.9	- 48.2	- 57.8
BI-IEO's net financing of special credit institutions and other agencies	5.8	3.2	- 2.4	- 7.9	- 1.3
BI-IEO's open-market operations in non-Government securities	- 0.4	- 0.9	- 0.1	- 1.3	- 2.7
BI-IEO's other minor operations, net	3.0	- 9.4	- 8.4	- 39.0	- 53.8
Total	- 414.2	92.0	486.0	1,052.5	1,216.3
USES					
Public and non-bank intermediaries	- 389.6	282.3	65.8	1,059.2	1,017.7
Public	- 319.1	167.7	144.0	958.4	951.0
notes and coin	- 373.6	148.3	55.6	655.9	486.2
Treasury bills and deposits at Treasury and BI (5)	5.5	- 24.1	44.8	- 7.9	18.3
sight assets with Post Office	49.0	43.5	43.6	310.4	446.5
Special credit institutions	- 70.5	114.6	- 78.2	100.8	66.7
Banks	- 24.6	- 190.3	420.2	- 6.7	198.6
Obligatory reserve and cash and Treasury bills as backing for cashiers' cheques (3)	50.9	121.2	2.6	74.9	249.6
(long-term securities)	(153.1)	(68.0)	(118.7)	(147.4)	(487.2)
Excess reserves	- 75.5	- 311.5	417.6	- 81.6	- 51.0
Total	- 414.2	92.0	486.0	1,052.5	1,216.3
Total including obligatory reserves in long-term securities	(- 261.1)	(160.0)	(604.7)	(1,199.9)	(1,703.5)
SOURCES					
Foreign sector	0.9	0.9	3.5	1.7	7.2
Balance of payments (1)	0.4	1.5	2.1	1.9	6.0
Banks' lendings abroad	0.9	- 1.4	7.1	3.2	10.0
Banks' deposits collected abroad	1.8	4.0	8.0	1.9	16.6
Liquid assets tied	4.3	33.6	19.5	- 12.6	45.6
Treasury	- 3.5	3.2	- 1.7	- 2.2	- 4.4
Financing by BI-IEO	1.2	2.3	1.5	1.3	6.5
Direct liquidity creation (3)	8.9	- 2.3	8.8	17.2	35.7
Banks (4)	- 1.0	0.5	1.9	3.3	4.7
USES					
Public and non-bank intermediaries	2.3	2.4	2.0	1.1	8.0
Public	2.2	1.9	2.1	3.7	10.4
notes and coin	1.9	1.7	1.8	1.4	7.0
Treasury bills and deposits at Treasury and BI (5)	13.3	- 5.5	- 3.4	16.1	20.1
sight assets with Post Office	2.4	2.4	2.5	1.0	8.6
Special credit institutions	- 29.8	105.0	0.6	- 3.3	40.0
Banks	- 1.0	0.5	1.9	3.3	4.7
Obligatory reserve and cash and Treasury bills as backing for cashiers' cheques (3)	1.3	2.4	1.6	1.0	6.4
Excess reserves	- 7.5	- 7.7	6.3	9.7	- 0.5
Total	1.2	1.7	1.9	2.0	6.9

(1) Including accounting discrepancies with Bank of Italy-Italian Exchange Office (IEO) for the foreign sector.— (2) In Government securities and Treasury bills backing for cashiers' cheques.— (4) Rediscounting of ordinary portfolio, overdrafts, advances for fixed periods, postponed payments and ing Bank of Italy's checks; excluding Treasury bills from May 1969.— (*) The percentage changes calculated on the unadjusted figures may differ from

OF MONETARY BASE

TABLE 40

1968					1969				
quarters				Year	quarters				Year
I	II	III	IV		I	II	III	IV	
Absolute changes in billions of lire (unadjusted figures)									
- 75.9	88.2	281.5	- 171.2	122.6	- 234.2	- 144.8	- 223.6	- 45.3	- 647.9
- 70.7	97.1	387.0	- 20.1	393.3	- 226.9	- 334.4	- 201.3	- 106.6	- 869.2
- 11.7	- 36.4	- 265.2	- 114.7	- 428.0	- 81.0	401.8	0.3	132.9	454.0
6.5	27.5	159.7	- 36.4	157.3	73.7	- 212.2	- 22.6	- 71.6	- 232.7
88.9	112.0	369.5	351.4	921.8	- 25.1	113.4	699.6	712.5	1,500.4
80.4	69.8	250.5	99.1	499.8	- 35.8	88.6	608.0	456.1	1,116.9
(- 202.3)	(- 132.2)	(- 49.7)	(- 39.5)	(- 423.7)	(- 49.0)	(154.1)	(72.2)	(90.5)	(267.8)
8.5	42.2	119.0	252.3	422.0	10.7	24.8	91.6	256.4	383.5
- 579.2	153.7	- 136.6	782.6	220.5	- 287.9	222.4	- 259.6	801.0	475.9
- 0.4	- 26.5	- 10.2	13.3	- 23.8	- 24.6	- 83.0	6.7	17.8	- 83.1
2.2	- 0.5	3.8	11.9	17.4	- 1.0	0.8	2.7	18.5	21.0
- 0.3	- 0.3	- 0.3	- 0.5	- 1.4	- 0.2	1.0	3.3	21.6	25.7
- 2.3	- 25.7	- 13.7	1.9	- 39.8	- 23.4	- 84.8	0.7	- 22.3	- 129.8
- 566.6	327.4	504.2	976.1	1,241.1	- 571.8	108.0	223.1	1,486.0	1,245.3
- 593.1	308.3	- 50.0	911.6	576.8	- 535.0	289.0	159.2	1,239.9	1,153.1
- 499.7	228.8	36.8	752.6	518.5	- 372.4	213.1	244.6	1,010.4	1,095.7
- 490.0	222.1	- 28.8	503.9	207.2	- 371.0	160.1	184.6	733.3	707.0
- 8.2	- 21.1	31.9	- 46.1	- 43.5	- 11.8	- 9.3	53.7	- 17.3	15.3
- 1.5	27.8	33.7	294.8	354.8	10.4	62.3	6.3	294.4	373.4
- 93.4	79.5	- 86.8	159.0	58.3	- 162.6	75.9	- 85.4	229.5	57.4
26.5	19.1	554.2	64.5	664.3	- 36.8	- 181.0	63.9	246.1	92.2
62.5	148.0	68.3	124.1	402.9	134.7	171.4	- 97.1	206.5	415.5
(179.4)	(89.9)	(74.4)	(117.5)	(461.2)	(164.7)	(56.1)	(6.4)	(169.8)	(397.0)
- 36.0	- 128.9	485.9	- 59.6	261.4	- 171.5	- 352.4	161.0	39.6	- 323.3
- 566.6	327.4	504.2	976.1	1,241.1	- 571.8	108.0	223.1	1,486.0	1,245.3
(- 387.2)	(417.3)	(578.6)	(1,093.6)	(1,702.3)	(- 407.1)	(164.1)	(229.5)	(1,655.8)	(1,642.3)
Percentage changes (seasonally adjusted figures) (*)									
2.4	1.6	1.4	- 2.2	3.2	- 1.5	- 5.0	- 10.2	- 0.2	- 16.2
2.9	3.1	2.1	1.9	10.4	- 1.1	- 7.6	- 12.1	- 1.0	- 20.5
14.9	12.3	8.8	11.8	57.0	19.4	10.7	- 0.2	10.3	45.5
11.1	4.6	1.9	5.4	24.8	13.7	21.0	4.4	11.5	60.0
8.1	- 22.0	- 21.0	- 5.5	- 37.0	- 18.9	64.9	44.6	- 2.1	89.2
3.5	2.5	2.4	1.0	9.8	1.9	2.5	5.3	3.4	13.5
8.3	4.7	5.9	0.5	20.6	2.6	5.6	15.7	9.3	37.0
1.6	1.7	1.3	1.3	6.0	1.3	1.3	1.1	0.9	4.7
- 5.8	10.0	3.0	6.1	13.3	16.1	8.1	0.3	- 2.2	23.1
3.5	2.2	1.2	0.8	7.8	2.3	2.0	3.4	2.4	10.5
0.7	2.3	1.2	0.9	5.2	2.3	2.1	3.4	2.1	10.3
3.3	3.0	0.5	0.7	7.7	2.7	1.7	5.0	3.2	13.2
0.1	1.0	- 19.1	- 27.0	- 40.3	- 14.6	7.2	28.9	4.6	23.4
2.7	1.9	2.3	1.2	8.4	1.8	2.7	1.9	0.7	7.2
13.2	- 4.5	0.3	10.1	19.5	- 15.1	- 2.0	- 6.6	49.5	16.2
..	3.9	4.0	1.2	9.3	2.5	- 0.7	- 4.2	3.3	0.7
1.9	2.5	3.6	1.8	10.1	3.6	2.2	0.3	2.9	9.2
- 5.8	9.9	3.6	- 0.8	6.5	- 0.8	- 12.4	- 17.3	4.1	- 25.2
2.2	2.7	2.2	0.8	8.2	2.5	1.0	0.7	2.7	7.0

from May 1969 including Treasury bills.— (3) Including securities as special reserves of banks in Southern Italy. From May 1969, excluding foreign exchange transactions, less Treasury bills deposited as collateral for advances and postponed payments (until end of Aprile 1969).— (5) Includes those calculated on adjusted figures because of the variability of the seasonal coefficients through years.

etary base was controlled mainly by slowing down the increase of central-bank lending to the banks; the rapid increase of such a lending in the first half of the year, together with the reduction in the banks, positive foreign position, had made possible an expansion of bank loans faster than that of deposits. By acting on this channel of monetary base creation and increasing at the same time the open-market purchases of long-term public securities, an attempt was made to concentrate the restrictive effect only on the short-term end of the market. However, the well-known absence of a wide and efficient money market, capable of acting as a shock absorber between short and long-term rates, caused these effects to be rapidly transmitted to the long-term market. In other terms the open market purchases of securities by the Bank of Italy, which aimed also at ensuring a volume of security issues close to the one envisaged and announced at the beginning of the year, though much larger than envisaged, were insufficient to prevent a widespread increase of long-term rates.

In the fourth quarter, partly in order to meet the persistent growth in demand from the public, the rate of creation of monetary base was increased once more and raised to an annual level of about 11 per cent. Nevertheless the banks' excess reserves remained, by the end of December, at the levels reached in September, that is, some 320 billion lire below the figure for December 1968; the rates of yield on bonds showed an increase of about one point over six months earlier, and the interest rates on bank lendings were correspondingly higher.

As a result of the change in the policy of liquidity regulation which has been described above, the total creation of monetary base in 1969 was lower than the figure of 1,500 billion lire announced in last year's Report.

There were also substantial changes, in relation to the forecasts produced there, in the flows of monetary base from the various channels; the foreign sector, which was assumed to contribute for a positive amount equal to the reduction in the net non-liquid position of the banks (about 200 billion lire), exerted, as already said, a strong absorption effect. Largely as a consequence, the volume of monetary base, created by financing to the Treasury and by rediscount and advances to the banks, was much larger than had been forecast (the former was 1,500 billion lire against a forecast of 1,200 and the latter 476 billion

against a forecast of 200). In particular, there was a substantial increase in the Bank of Italy's security holdings, as had been envisaged in the event of a large absorption of liquidity by the balance of payments deficit; the amount of the Bank's public security holdings rose by 1,448 billion lire, as compared with a minimum forecast, for the case of balance of payments equilibrium, of 650 billion and a maximum forecast, in the event of a deficit, of only 1,000 billion.

With regard to the uses of monetary base, demand from the public was about 150 billion greater than forecast; consequently, and due also to the reduction in the overall formation of monetary base, the growth in total banks reserves, was strongly curtailed.

The behaviour of the balance of payments and of the Treasury cash deficit, which were different from what had been assumed as a basis for the forecasts, and the afore-mentioned differences in the creation of monetary base and in its distribution among users, affected the demand and the supply of both bank credit and deposits. More specifically there was a smaller formation of bank deposits (3,665 billion lire against 4,300 forecast) and a greater expansion of loans (3,104 billion lire against the 2,600 forecast); such a movement, despite the partial depletion of the existing excess reserves, was reflected in a smaller demand for securities by the banking system, a demand which amounted to 1,170 billion lire instead of the 1,600-1,700 forecast.

As demand for fixed-interest securities from private individuals—for reasons which are described in detail in the appropriate chapter of the Report—was also substantially reduced (1,027 billion lire against a forecast of 1,600 billion), net total issues of securities amounted to 3,678 billion lire, against the approximately 3,900 billion forecast; the larger purchases by the central bank indeed proved insufficient to offset the decline in subscriptions by the banks and by the economy. The reduction, however, affected mainly the issue of public securities, the placing of which would only lead, in the given situation, to a corresponding positive change in the Treasury's current account balance with the Bank of Italy.

Sources of monetary base.— In 1969 the balance of payments produced a reduction of monetary base of 869 billion lire, offset to the extent of 221 billion by the effects of the decrease in the banks'

net positive foreign position. The final result therefore amounted to 648 billion.

In the previous year the foreign sector had created monetary base to the extent of 123 billion lire (due to a balance of payments surplus of 393 billion, offset by the banks' foreign operation to the extent of 270 billion).

The operations designed to restore equilibrium in the banks' net foreign position—which amounted to 452 billion lire at the end of 1968 and was reduced to 22 billion at the end of 1969—were concentrated, in accordance with the regulations issued in April, in the first half of the year. The balance of banks' external position was achieved by increasing the liabilities more than the assets; indeed at the end of the year assets had increased by 40.3 per cent and liabilities by 62.3 per cent with respect to the figures of December 1968.

The increase in foreign deposits, together with the continuing obligation of keeping the foreign position balanced, rendered unavailable for conversion into national currency an amount of 208 billion lire of liquid foreign currency; nevertheless the addition of monetary base, from the point of view of its effects on bank liquidity, amounted to only 221 billion lire (as compared with the improvement of 429 billion in the net position).

The effect produced on the monetary base by the Treasury's cash requirements, which can be considered an exogenous factor for the monetary authorities, can be adjusted through the choice of the forms in which the financing is provided. The financing of the Treasury includes also open-market operations; these, however, have a different significance because, through them, an effect is produced on market liquidity independently of the extent of the Treasury requirements: what happens is merely that the Bank of Italy, as the holder of claims on the Treasury, takes the place of the market, or vice versa.

In the course of 1969, despite the existence of a smaller Treasury cash deficit than in the previous year, the creation of monetary base due to that sector increased greatly (by 1,500 billion lire against 922 in 1968) (Table 41). The main factors responsible for this increase were the larger purchases of newly issued securities (1,180 billion against 768 billion) and the open-market operations carried out by

TABLE 41

MONETARY BASE CREATION: TREASURY
(changes in billions of lire)

Items	1967	1968	1969	1969 by quarters			
				I	II	III	IV
<i>Autonomous factors: budget deficit (+) or surplus (-)</i>	1,274.4	2,044.6	1,766.0	379.3	220.5	659.6	506.6
<i>Action by monetary authorities (1)</i>	- 869.8	-1,122.8	- 265.6	- 404.4	- 107.1	40.0	205.9
Operations in Government securities	- 843.9	-1,092.8	- 230.4	- 397.4	- 99.3	49.5	216.8
Public debt (2)	- 537.5	- 669.1	- 498.2	- 348.4	- 253.4	22.7	126.3
Long-term securities . .	- 537.5	- 669.1	- 537.0	- 348.4	- 212.2	43.9	67.5
Treasury bills for free investments (3) . .	—	—	85.1	—	5.1	21.2	58.8
Treasury bills included in liquidity at the end of April 1969	—	—	46.3	—	46.3	—	—
Open-market operations by BI-IEO	- 306.4	- 423.7	267.8	- 49.0	154.1	72.2	90.5
Long-term securities . .	- 306.4	- 423.7	178.9	- 49.0	91.8	45.0	91.1
Treasury bills (3) . .	—	—	88.9	—	62.3	27.2	0.6
Operations by the Central Post Office Savings Fund (4)	- 25.9	- 30.0	- 35.2	- 7.0	- 7.8	- 9.5	- 10.9
<i>Total effect, resulting from: . .</i>	404.6	921.8	1,500.4	- 25.1	113.4	699.6	712.5
Direct liquidity creation . .	546.7	422.0	383.5	10.7	24.8	91.6	256.4
Postal accounts	446.5	354.8	373.4	10.4	62.3	6.3	294.4
Other operations (5) . .	100.2	67.2	10.1	0.3	37.5	85.3	38.0
Financing by BI-IEO (6) . .	- 142.1	499.8	1,116.9	- 35.8	88.6	608.0	456.1
Operations in short and long-term securities (7)	115.9	344.3	1,447.8	- 68.9	316.2	677.5	523.0
Subscriptions of new issues net	422.3	768.0	1,180.0	- 19.9	162.1	605.3	432.5
Open-market operations . .	- 306.4	- 423.7	267.8	- 49.0	154.1	72.2	90.5
Other financing	- 258.0	155.5	- 330.9	33.1	- 227.6	- 69.5	- 66.9
of which:							
Treasury current account	- 371.3	120.8	- 399.4	49.4	- 258.4	- 157.4	- 33.0

(1) The sign refers to the effect produced on the creation of monetary base: that is, the Bank of Italy's sales on the market and security issues bear a negative sign.— (2) Issues net of BI-IEO subscriptions.— (3) From May 1969.— (4) In relation to guarantee deposits and non-Government securities.— (5) This includes special reserve certificates of the « banchi meridionali », allowance also being made for the reducing effect due to the fact that the Treasury bills included in the liquidity total on 30 April 1969 are no longer regarded as monetary base.— (6) The figure does not include the transfer of 97.3 billion lire to the EEC (FEOGA section), actually not made until January 1970. The figure for securities is exclusive of the depreciation of securities as shown in the Balance Sheet of BI at 31st December 1961.— (7) Up until 30 April 1969, open-market transactions in Treasury bills are included under « Other financing ».

the Bank of Italy; the latter involved net purchases of securities of 268 billion lire, whereas in the previous year there had been net sales amounting to 424 billion.

The creation of monetary base for lendings to the Treasury was particularly great in the second half of the year; in that period, owing also to the sector's greater cash requirements, the creation of monetary base offset the losses due to the balance of payments deficit and provided, especially in the last quarter, together with the Bank of Italy's financing to the banks, the liquidity necessary to sustain the expansion of bank loans.

The central bank's lending to the banks constitutes, at times of growing demand for credit, a flexible instrument for regulation the overall volume of monetary base and acting quickly on the level of interest rates. This is a consequence of the fact that such a lending is more directly subject to control at the discretion of the central bank; the initiative passes to the banks only if they decide to pay off previously contracted indebtedness without asking for the renewal.

Lendings to the banks increased in 1969 by 476 billion lire, that is more than in 1968 but less than in 1967.

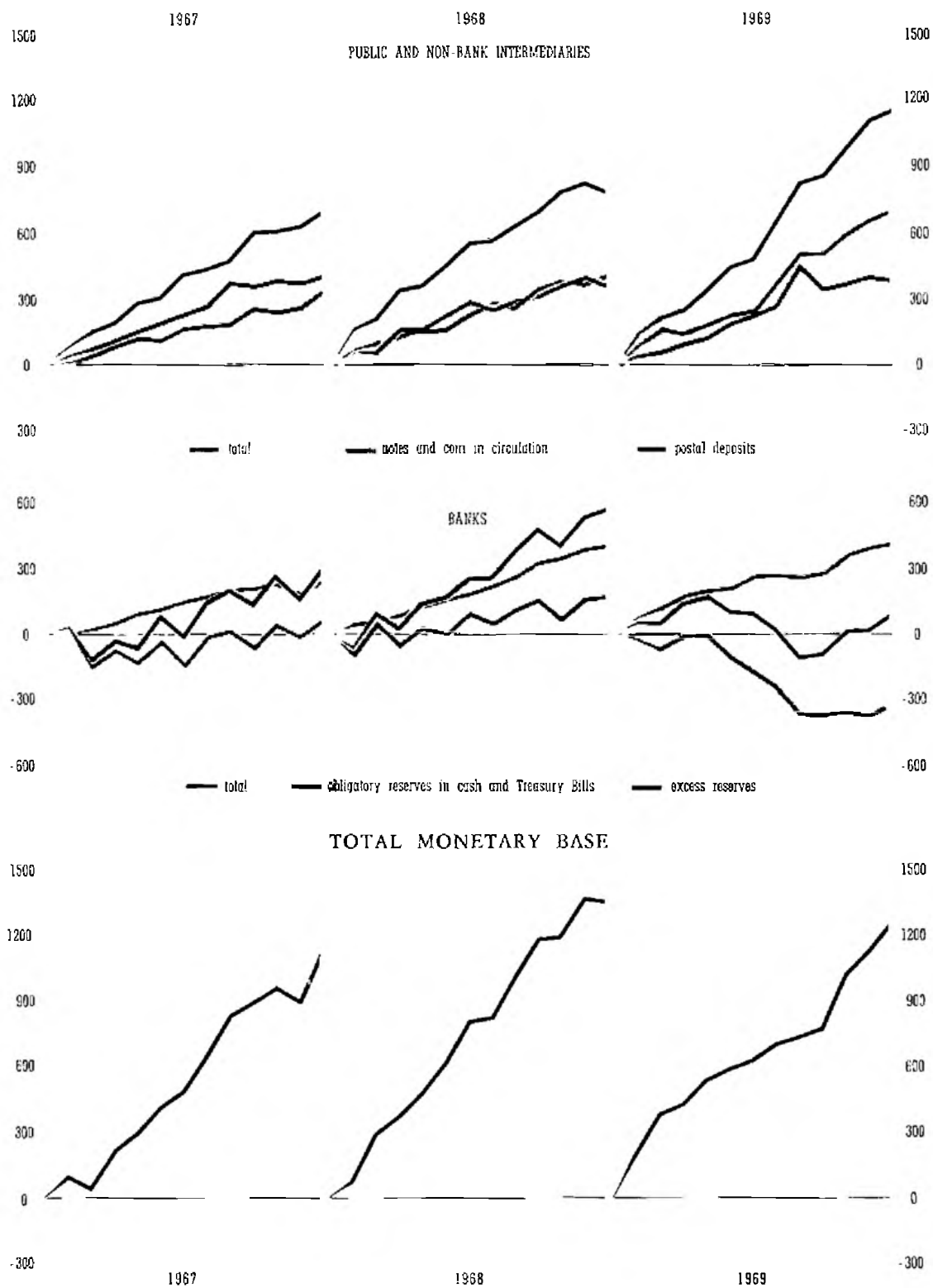
The overall expansion was due, as usual, to a very large increase in the fourth quarter and to a negative change for the total of the three previous quarters.

However, an analysis of the seasonally adjusted trend of lendings reveals a very high rate of expansion in the first quarter (16.1 per cent), an appreciable slowing down in the next two quarters (8.1 per cent in the second and 0.3 in the third) and a negative value in the last quarter (—2.2 per cent) (Table 40).

The increase in the rates on fixed-term advances by the Bank of Italy to banks, which was decided in March, and the increase of the rediscount rates decided in August were designed to give greater flexibility to the authorities' control of lendings to the banks, by adding a cost element to the otherwise merely quantitative regulation. Initially the increase in the cost of fixed-term advance was also intended, as was fully explained in last year's Report, to align that rate with the yield of the new Treasury Bills. The continuing policy of curbing bank liquidity necessitated the extension of the increases also to the official

USES OF MONETARY BASE

(cumulative monthly changes; seasonally adjusted figures; billions of lire)



discount rate. The recent further adjustment in the official discount rate, designed to bring it into line with the level of rates ruling on the market, provides confirmation of the new principles of monetary policy, which tend to be based more than before on regulation of the cost of borrowing.

Uses of monetary base.— In 1969 the public absorbed monetary base for 1,095 billion lire, consisting of 707 billion of currency circulation, 373 billion of postal deposits and 15 billion of deposits with the Treasury, Bank of Italy checks, and other minor items (Table 39).

The factors effecting the public's demand for monetary base have already been discussed in previous Reports, but those referred to there, (i.e. national income at current prices, labour income, consumption, interest rates) can explain only partially the behaviour observed in the course of 1969.

Indeed, only in the first two quarters of the year did the public's monetary base follow the cyclical behaviour of income, although increasing less rapidly than the latter. More exactly, on the basis of seasonally adjusted figures, the currency in circulation rose at rates of 2.7 and 1.7 per cent respectively, for the two quarters (the total monetary base held by the public rose by 2.3 and 2.1 per cent), against increases in the national product at current prices, of 3.3 and 3.0 per cent respectively.

In the third quarter, on the other hand, mainly owing to the increase in pensions paid by the social security institutions, the demand for notes and coins increased rapidly (5.0 per cent) while the gross national product remained unchanged; the rate of increase of postal deposits slackened slightly however and therefore the total monetary base held by the public showed a more steady trend, with an increase of 3.4 per cent for the quarter.

Finally in the fourth quarter, the rate of increase of notes and coins in circulation remained fairly high, having been affected also by the delay in the payment of the thirteenth monthly instalment made, owing to entirely fortuitous events, on a date closer than normal to the end of the year; on the other hand the GNP declined by 1.2 per cent. Owing to a further reduction in the rate of accumulation of postal

deposits, probably due to the slowing down of productive activity and the decrease in the system's liquidity, the total monetary base held by the public increased by 2.1 per cent, the same rate as in the first two quarters of the year.

The deposits of non-bank financial intermediaries showed in 1969 a trend not unlike that of previous periods. The changes within the year are closely correlated with the payments of coupons on securities in circulation (Table 39).

The trend of monetary base held by the public is reflected, with the opposite sign, in the variations in banks' reserves.

The total of these reserves, allowance being made for seasonal variations, continued to increase during the first half of 1969, but with different trends in the two components. For, while obligatory reserves continued to expand owing to the growth in deposits, excess reserves decreased steadily. This decline, which was extremely marked in the second quarter, is attributable to the changing trend of demand for credit and of deposits, not offset by an increase in the banks' borrowing from the central bank.

In the third quarter, as a result of the already described movements in the total creation of monetary base and in demand by the public, overall bank reserves declined markedly. The reduction affected only excess reserves, as obligatory reserves still rose slightly as consequence of the strain on bank liquidity; the supply of bank credit slowed down markedly during the quarter, and this led, in view of the steady and rapid expansion in demand, to a rise in interest rates.

The supply of credit again expanded slightly in the fourth quarter, when the rate of increase in monetary base quickened. The excess reserves also benefited from this tendency and increased slightly; at the end of the year, however, they were 323 billion lire less than in December 1968. Owing to the increase in deposits, there was also a marked reduction in the ratio between liquid funds and deposits, which was down to 3.2 per cent at the end of the year under review, against 4.6 per cent in December 1968.

Forecasts for 1970.— In order to make a forecast for the development of monetary base in 1970 it is necessary to attempt, at least as working hypotheses, certain assessments of the movement of the main

real aggregates. Partly on the basis of some recent official estimates, it is then assumed that during the year the increase in the gross national product at current prices may amount to about 14 per cent over 1969; the expansion in the GNP is expected to be due to an increase in demand for consumption approximately equal to, or a little greater than, that of the gross national product and to a somewhat larger demand for total gross investment (over 20 per cent, at least half of this being due to the rise in prices). It is also assumed that exports and imports will increase at rates of 10 and 20 per cent respectively, and that the overall balance of payments deficit may be in the region of 300 billion lire. Lastly, still with reference to the figures obtained from recent official statements regarding the whole of the public sector, it is assumed, that there will be an overall cash deficit for the sector comprising the Treasury, Central Post Office Savings Fund and autonomous Government agencies, of 2,600 billion lire.

Starting from these hypotheses an attempt may be made to assess the expansion of the economy's main assets and liabilities, the growth in the bank intermediation and the volume of monetary base necessary for this expansion.

The demand for monetary base by the public and by the non-bank financial intermediaries will probably be around 1,200-1,300 billion lire and the growth in bank deposits could be around 4,600 billion; demand from the public for fixed-interest securities, assuming that the present prices remain stable, might reach 1,300 billion.

With this formation of domestic financial assets, account being taken of the trend of the balance of payments and of other minor assets and liabilities of the banks, it would be possible to finance the Treasury's cash deficit, mentioned above, and to lend funds to the other sectors of the economy to the extent of some 5,000 billion lire; such a lending can take the form of bond issues directly and through special credit institutes for about 1,500 billion, and the form of bank loans for the remainder. Financing of private investments would also be provided by the issue of securities on foreign markets for an amount of about 600 billion lire, and by issues of shares and other minor forms of fund-raising, the amount of which is not directly influenced by the creation of monetary base.

The total issue of long and short-term securities on the domestic market, taking into account those from the public sector, might be in the region of 3,500-3,600 billion lire; these would be subscribed in the above-mentioned amount of 1,300 billion lire by private individuals and for the remainder by the banks and by the Bank of Italy.

The volume of new monetary base which is compatible with the above forecasts and with the continuation of the present level of interest rates, would be in the region of 1,700-1,800 billion lire.

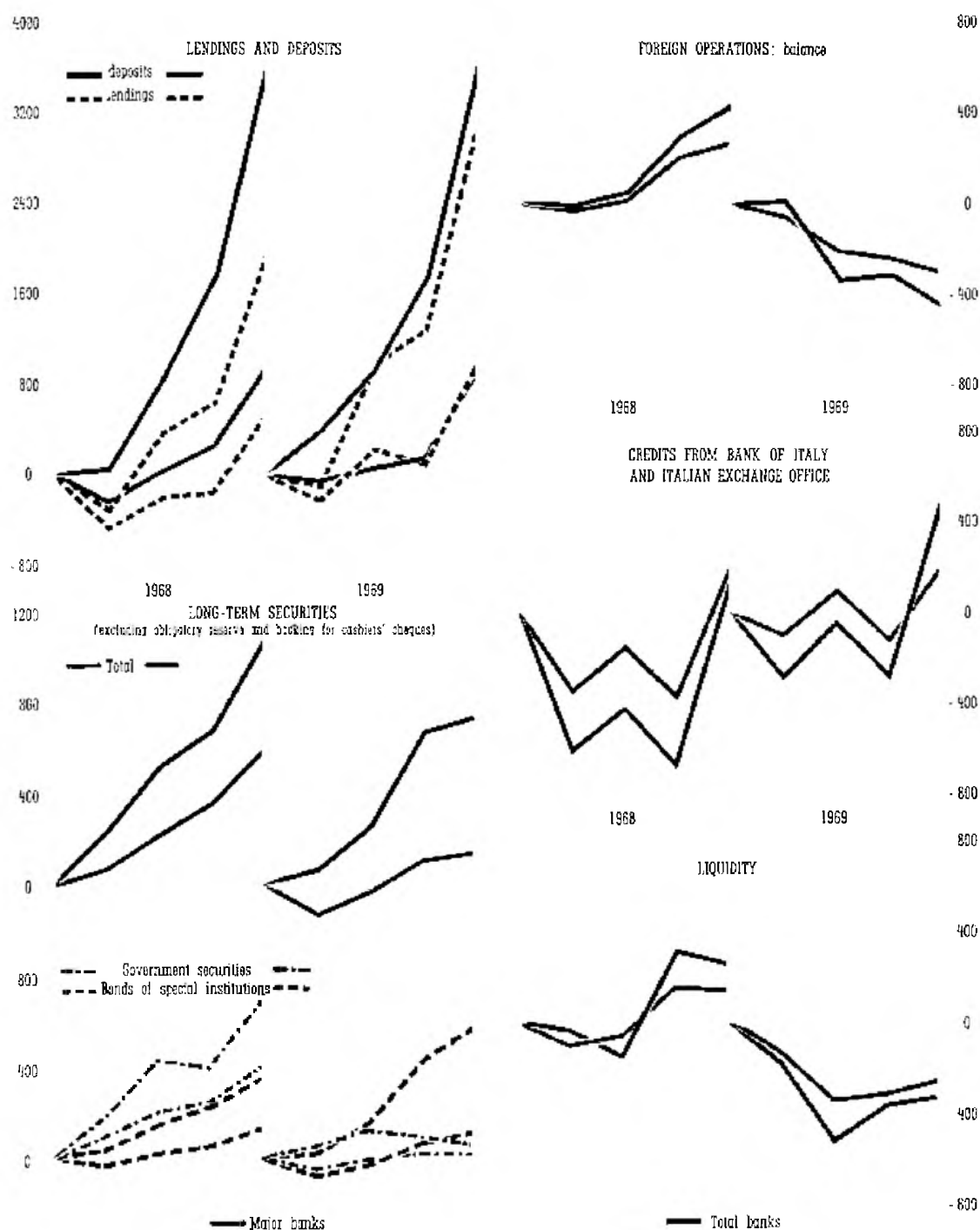
Banking

Development of banking in 1969.— In our country the banking system, owing to the role of primary importance which it plays in the channelling of funds, is particularly and immediately sensitive to the course of economic and financial events including, above all, measures of monetary policy; similarly, the reactions and adaptations of the system to new situations acquire special importance. Last year, when it was decided to adopt direct measures to modify general credit conditions, the banking system quickly adjusted itself to the change in the market, above all by bringing interest rates up to the new levels.

The favourable progress of productive activity and investments in the first eight months of the year and the expectations of price increases led to a greater demand for bank credit, despite the rise in interest rates. The formation of deposits, however, was limited despite the higher rates offered to depositors, mainly because of the greater inclination of the public towards possession of monetary base and the acquisition of foreign assets. The annual growth of lendings had already exceeded that of deposits half-way through the year; this scissor movement was accentuated in the second half-year. At the end of the year the difference between the two rates was more than 3 points; a similar difference, but in favour of deposits, had been recorded at the end of 1968 (according to data adjusted to eliminate the effect of the bank strike at the end of 1967).

This trend was reflected, on the assets side, by a smaller increase in the securities portfolio, despite increasing yields in the second half of the year and, on the liabilities side, by a greater demand for financing

TREND OF THE BANKS' MAIN BALANCE-SHEET ITEMS

(sum of absolute quarterly changes, in billions of lire)

by the bank of issue, despite the higher cost. Although the direct support provided by the central bank to the system was maintained, during the year, at an average level 500 billion lire higher than that of 1968, bank liquidity was considerably reduced and fell, in December, to 3.2 per cent of deposits (against 4.6 per cent a year earlier).

Marked differences from the general trend experienced by the system as a whole occurred among banks of different sizes. The analysis of the adjustment of the liquidity position indicates that the action of the monetary authorities has affected more directly the « major banks », which, through a process of more extensive adjustment (Chart 15), spread its effects to the rest of the banking system and to the economy. Thus, the new rules governing the cost of recourse to the central bank, which involve the application of increases to the official rate in relation to the amount and frequency of requests for financing, more directly affected the « major banks », for which this form of fund raising represented, at the end of 1968, 8.5 per cent of the total, compared with 4.7 for the rest of the system. Similarly, the reduction in income from foreign assets, resulting from the requirement that banks should balance their position, almost exclusively affected their profit and loss accounts. They, however, more than the others, modified their lending rates, having increased them, during the year, according to the results of the profit and loss accounts sent to the Bank of Italy, by 0.34 per cent (0.31 for the system). The changes made, officially in two stages, to the inter-bank agreement have helped to transmit to the other banks, too, the effects of making credit of last resort more expensive; the increase which they experienced was, however, more limited owing to the lower level of the their dealings with the Bank of Italy and abroad.

On the deposit side also, the trend towards an increase in rates seems to have started with the larger banks which, since they operate mainly in large urban centres, have a clientèle consisting mainly of large businesses with great bargaining power which are more sensitive to the yields on their funds and more aware of alternative forms of investment. The profit and loss accounts show, however, that the unit cost of raising funds increased, for the « major banks » by 0.16 per cent and that this increase was slightly less than that for other groups of banks. This seems to indicate that the action taken by the « major banks » to acquire

deposits was centred mainly on extending to a wider range of depositors the more favourable terms already applied to first-class customers, rather than a general increase in the deposit rates which, for these banks, are structurally at higher levels than the average levels for the system.

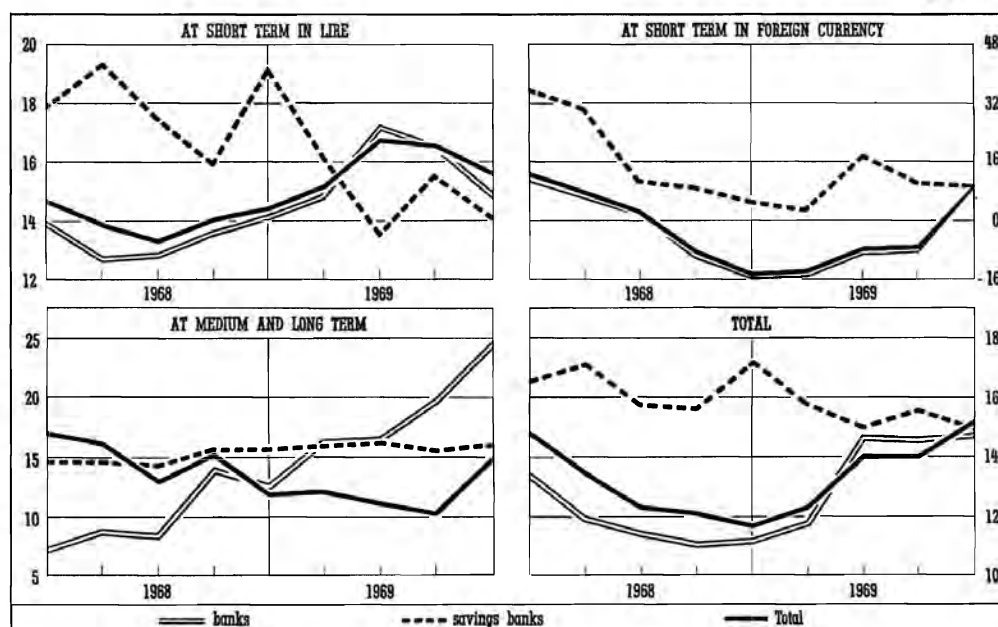
It may be expected that, in the future, interest rates will show more frequent and wider fluctuations than in the past, since they have become more sensitive to the liquidity conditions of the market as a result of the changes made in the method of issuing Treasury Bills, (although these have not yet been fully tried out), the variability of the cost of credit of last resort and the liberalisation of rates on inter-bank accounts. The possibility of more frequent variations in interest rates in the short-term is reflected, in view of the greater « stickiness » of deposit rates compared with lending rates, in the profit and loss accounts, which benefit from the phase of rising rates and are adversely affected in the opposite phase.

The proportions reached by the process of readjustment in which the banking system played a leading part in 1969 shook the already weak foundations of the inter-bank agreement, which has not in fact been renewed for the current year. The effects produced by the alignment of rates on the profit and loss accounts were different for the individual groups of banks; for the « major banks » the increase in deposit rates did not in fact involve any reduction in the net proceeds from their own lending and fund-raising operations, nor reduce the growth in trading profits, as however did happen in the case of the « small and minor banks », which succeeded in passing on to their lending rates only a portion of the greater cost paid for deposits, partly owing to the greater elasticity of the demand for credit in relation to the interest rate. This different incidence of the process of adjustment of interest rates on the profit and loss accounts made it impossible to apply a common system of deposit rates, which for the larger banks are now situated at a higher level or at least very close to the maximum acceptable by small banks.

The abandonment of the banking agreement may give a further stimulus, for the marginal banks, to the attempt to reach a new equilibrium particularly through a reduction in operating costs, which in certain cases may be achieved by means of concentration or merger—which, in the last analysis, would reduce the cost to the community of the banks' activities as intermediaries.

Domestic lendings.— The signs for revival in the annual growth rate of lendings which were emerging in the second half of 1968 after a year of gradual slowing down were confirmed in the sharp acceleration of the first half of 1969; in June, the annual growth rate was equal to 14.0 per cent (compared with 12.3 per cent a year earlier). In the second half of the year the growth continued, but at a more limited rate as a result of the pause which occurred in the third quarter, only partly offset by the progress in the last three months (Chart 16). In 1969 domestic lendings increased by 3,114 billion lire, or 15.1 per cent, compared with 2,012 billion or 10.8 per cent in 1968, reaching in December 23,731 billion (Table 42). Eliminating from the figures the effects of the strike at the end of 1967, the difference compared with 1968, although reduced, still seems significant (3.4 points).

CHART 16



Domestic lendings of banks and savings banks

(year-to-year percentage changes as at the end of each quarter,
corrected for the incidental movements at the end of 1967)

In particular in the first 6 months short-term lendings in lire, which at the end of 1969 represented 8.1 per cent of total lendings, rose steadily (in May they had reached, on an annual basis, the maximum expansion: 17 per cent), while medium and long-term lendings began to slow down from March onwards, and the reduction

BANKS' ASSETS AND LIABILITIES
(changes in billions of lire)

TABLE 42

I t e m s	B A N K S				SAVINGS BANKS		CENTRAL CREDIT INSTITUTIONS		GRAND TOTAL	
	Major		Total		Total		1968	1969	1968	1969
	1968	1969	1968	1969	1968	1969				
A S S E T S										
Liquid assets	132.3	- 254.3	218.8	- 301.0	32.4	- 12.8	10.9	- 12.3	262.1	- 326.1
cash and deposits with BI	37.1	12.0	59.8	19.4	21.7	3.8	0.8	0.4	82.3	23.6
borrowing margin	- 30.3	1.4	- 8.9	1.2	6.8	- 13.6	10.1	- 12.7	8.0	- 25.1
Treasury Bills (1)	18.1	- 107.9	18.8	- 108.6	—	—	—	—	18.8	- 108.6
other claims on the Treasury and the Central Post Office Savings Fund convertible currencies	- 6.4	6.0	- 4.2	- 4.7	- 2.1	- 1.4	..	..	- 6.3	- 6.1
Obligatory reserves and backing for cashiers' cheques	113.8	- 165.8	153.3	- 208.3	6.0	- 1.6	—	—	159.3	- 209.9
cash	250.5	196.6	615.4	586.4	221.7	214.2	1.9	- 0.2	839.0	800.4
Treasury Bills	127.2	149.3	266.8	340.3	—	—	0.6	- 0.5	267.4	339.8
long-term securities	57.3	42.6	110.3	73.6	0.1	- 10.0	—	—	110.4	63.6
Tield liquid foreign assets	66.0	4.7	238.3	172.5	221.6	224.2	1.3	0.3	461.2	397.0
Domestic lendings	- 90.0	164.6	- 151.9	233.4	- 5.1	1.3	—	—	- 157.0	234.7
at short term: in lire	553.1	919.8	1,464.7	2,365.9	594.7	624.3	- 47.1	123.5	2,012.3	3,113.7
in foreign currency	717.3	857.1	1,627.0	2,106.8	316.9	291.7	- 6.8	179.8	1,937.1	2,578.3
at medium and long-term	- 172.2	58.8	- 229.5	109.8	3.1	5.9	—	—	- 226.4	115.7
Securities pledged	8.0	3.9	67.2	149.3	274.7	326.7	- 40.3	- 56.3	301.6	419.7
Treasury Bills	192.3	112.5	313.4	231.4	37.4	19.9	- 270.5	290.9	80.3	542.2
bonds	- 52.8	- 132.2	- 55.4	- 126.7	1.4	- 4.9	—	—	- 54.0	- 131.6
shares	242.9	244.4	371.8	355.0	36.3	24.9	- 270.6	290.9	137.5	670.8
Securities available	2.2	0.3	- 3.0	3.1	- 0.3	- 0.1	0.1	..	- 3.2	3.0
Treasury Bills	368.6	- 26.7	561.5	- 67.1	188.9	208.8	195.7	9.0	946.1	150.7
bonds	—	26.9	—	26.9	—	—	—	—	—	26.9
shares	365.7	- 97.2	563.7	- 149.4	188.5	208.5	199.5	9.8	951.7	68.9
Investments in affiliates	2.9	43.6	- 2.2	55.4	0.4	0.3	- 3.8	- 0.8	- 5.6	54.9
Foreign lendings	33.9	14.3	45.8	28.2	7.4	31.6	1.0	1.2	54.2	61.0
Inter-bank accounts	762.0	1,145.0	988.1	1,245.7	1.2	0.5	—	—	989.3	1,246.2
Accounts with special credit institutions	17.7	9.8	245.9	163.3	162.2	- 69.7	169.0	- 272.9	577.1	- 179.3
Other items	35.6	- 0.2	120.8	12.7	75.4	74.5	1.0	5.6	197.2	92.8
Total . . .	470.2	638.2	780.0	1,281.0	55.4	377.4	- 19.8	72.5	815.6	1,730.9
L I A B I L I T I E S										
Customers' deposits	2,726.2	2,919.6	5,202.5	5,779.9	1,371.6	1,470.0	42.1	217.3	6,616.2	7,467.2
time and savings deposits	955.5	904.3	2,544.3	2,529.2	1,131.0	1,059.5	- 6.7	76.6	3,668.6	3,665.3
sight deposits	230.7	- 116.2	1,028.6	561.8	646.0	545.8	—	—	1,674.6	1,107.6
Residents' foreign currency deposits	724.8	1,020.5	1,515.7	1,967.4	485.0	513.7	- 6.7	76.6	1,994.0	2,557.7
Third parties' funds held for administration	23.1	13.4	61.4	- 4.6	1.4	- 1.5	—	—	62.8	- 6.1
Non-residents' deposits	47.8	- 0.7	105.1	17.3	52.6	61.4	0.3	0.8	158.0	79.5
Lendings by BI-IEO (2)	521.9	1,451.5	578.5	1,717.2	- 18.6	4.9	—	—	559.9	1,722.1
rediscounts ordinary portfolio	201.6	214.8	244.5	375.7	25.4	13.3	- 103.3	113.5	166.6	502.5
deferred payments and fixed-term advances	62.6	136.8	35.9	230.4	- 0.1	6.6	—	—	35.8	237.0
credit on open account (ordinary advances)	120.1	51.7	145.1	74.8	17.2	- 2.3	8.1	107.6	170.4	180.1
Capital resources	19.0	26.3	63.8	70.5	8.3	9.0	- 111.4	5.9	- 39.3	85.4
Inter-bank accounts	52.4	4.3	143.9	54.4	26.4	46.2	3.5	18.3	173.8	118.9
Accounts with special credit institutions	314.0	- 131.2	529.0	- 14.2	- 0.4	- 23.8	152.8	- 130.4	681.4	- 168.4
Other items	5.2	- 132.7	40.6	- 153.2	- 30.7	- 8.7	5.3	88.4	15.2	- 73.5
Total . . .	604.7	595.9	955.2	1,258.1	184.5	318.7	- 9.8	50.1	1,129.9	1,626.9

(1) Until April 1969.— (2) Including transactions in foreign currency.

in foreign currency lendings began to level out. In the following quarter, too, it was the movement of short-term lendings in lire, the growth rate of which stabilised at an average level of 16.2 per cent, which set the pace for the general trend. In the last quarter, however, they slowed down, while there was a marked increase in foreign currency and medium and long-term lendings.

During the year short-term lendings in lire increased by 2,578 billion, or 15.6 per cent (compared with 1,937 billion, or 13.3 per cent, in 1968), reaching 19,188 billion in December. One factor which contributed to a certain extent to this development was the greater demand for prefinancing loans due to the reduction in loans by the special credit institutions. In particular, the more marked expansion in the first half-year is attributable to the favourable trend of productive activity, accompanied by an adequate flow of monetary base. In the third quarter, on the other hand, the pause is explained by the more limited increase in the monetary base, the normal summer lull in production and the greater propensity of the public to hold cash. Lastly, the reduction in the growth rate in the fourth quarter (from 16.6 to 15.6 per cent) may be explained—apart from by the continued tendency of the public to hold cash—by the adverse trend of industrial production and, to a certain extent, by an improvement in the operating conditions of the special credit institutions.

Medium and long-term lendings increased during the year by 420 billion lire, equal to 15 per cent (compared with 302 billion, or 12.1 per cent, in 1968), while foreign currency lendings to residents rose by 116 billion, or 9 per cent (compared with a reduction of 226 billion and 14.9 per cent in 1968).

The growth of foreign currency lendings to residents was not, however, commensurate with the sustained expansion of imports, with which they are structurally linked. This is due to the fact that the disturbances which affected the French franc, the Deutsche Mark and the lira itself discouraged Italian borrowers from assuming exchange risks. The volume of this financing, after having increased by 90 billion lire in the first half of the year, was reduced by 137 billion in the third quarter when the expectation of revaluation of the Deutsche Mark became stronger, and then increased again at the end of the

TABLE 43

BANKS' FOREIGN CURRENCY LENDINGS TO RESIDENT CUSTOMERS

Currency	1967	1968	1969			
			March	June	September	December
<i>End-of-period totals in billions of lire</i>						
U.S. dollars	270.0	188.4	143.3	185.0	233.4	244.5
Swiss francs	599.3	689.4	681.1	863.1	702.3	815.8
Pounds sterling	24.5	3.5	4.1	1.9	2.2	2.4
Deutsche Marks	433.4	148.7	233.3	81.9	59.6	78.4
French francs	19.2	4.2	4.7	3.2	1.4	1.4
Dutch florins	3.2	10.0	17.7	23.1	19.6	9.9
Other currencies	7.7	27.2	7.3	3.6	6.7	2.0
Total . . .	1,357.3	1,071.4	1,091.5	1,161.8	1,025.2	1,154.4
<i>Percentage breakdown</i>						
U.S. dollars	19.9	17.6	13.1	15.9	22.8	21.2
Swiss francs	44.2	64.4	62.4	74.3	68.5	70.7
Pounds sterling	1.8	0.3	0.4	0.2	0.2	0.2
Deutsche Marks	31.9	13.9	21.4	7.0	5.8	6.8
French francs	1.4	0.4	0.4	0.3	0.1	0.1
Dutch florins	0.2	0.9	1.6	2.0	1.9	0.8
Other currencies	0.6	2.5	0.7	0.3	0.7	0.2
Total . . .	100.0	100.0	100.0	100.0	100.0	100.0

year to a level close to the maximum reached in June (Table 43). So far as the individual currencies are concerned, there was a reduction in financing expressed in German marks (6.8 per cent of the total at the end of 1969 compared with 13.9 per cent a year earlier). Preference switched to the Swiss franc and, to a lesser extent, to the dollar; at the end of the year, financing in Swiss francs represented 71 per cent of the total (against 64 per cent at the end of 1968). This is connected with the lower cost of this currency: in 1969, interest rates for first-class customers fluctuated between 4.75 and 7.75 per cent, being concentrated mainly around 6 per cent, while for the U.S. dollar the range of variation was between 6.5 and 8 per cent, the most frequent rates being between 7 and 7.50. As is well known, the lower cost of financing in Swiss francs is associated with the forward quotation of this currency against the dollar: insofar as the Swiss franc is at a premium, the banks, which obtain this currency by means of swaps against dollars, profit from the premium and are therefore in a position to charge their customers lower rates of interest.

The trend of domestic lendings is the result of directly opposed developments in the banking and savings bank sectors; between one December and the next the annual rate of expansion increased by 4.7 points for the banks (from 10.1 to 14.8 per cent), whereas for the savings banks it fell by 1.6 (from 16.5 to 14.9 per cent).

So far as the savings banks are concerned, the rate of expansion of lendings has seemed to be closely linked with that of deposits, especially savings deposits, which represent the greater part of them. There was no similar link for the banks, which offset the effects of reduced formation of deposits by wider recourse to other forms of fund raising, cutting down their investments in securities and substantially reducing their own liquidity.

The new lendings in 1969 went to the public and private sectors (Table 44) in exactly the same proportions as in 1968 (18.1 and 81.9 per cent respectively). In particular, lendings to the public sector increased by 557 billion lire, or 13 per cent (compared with 364 billion, or 9.8 per cent, in 1968) and those to the private sector by 2,557 billion and 15.5 per cent (compared with 1,648 billion and

TABLE 44

BANK LENDINGS AND DEPOSITS BY CATEGORIES OF CUSTOMERS
(billions of lire)

Categories of customers	Absolute changes						Percentage changes			
	Lendings		Deposits		Net position		Lendings		Deposits	
	1968	1969	1968	1969	1968	1969	1968	1969	1968	1969
Public sector	364.3	557.0	485.2	286.6	120.9	270.4	9.8	13.6	21.6	10.5
local authorities . . .	198.9	311.3	102.9	144.4	96.0	166.9	16.2	21.8	27.6	30.3
autonomous Government agencies . . .	19.5	53.5	1.4	6.1	20.9	47.4	45.5	85.7	4.8	22.0
social insurance funds	50.2	37.1	32.0	52.3	18.2	89.4	44.8	22.9	8.9	13.3
other public agencies	103.8	126.6	344.2	81.5	240.4	45.1	13.4	14.4	26.8	5.0
public enterprises . .	8.1	135.5	7.5	119.1	15.6	16.4	0.5	8.7	3.9	59.4
Private sector	1,648.0	2,556.7	3,183.4	3,378.7	1,535.4	822.0	11.1	15.5	12.8	12.0
major companies . . .	235.3	514.4	152.9	12.6	82.4	527.0	8.4	16.9	19.7	1.4
other enterprises and households	1,412.7	2,042.3	3,030.5	3,391.3	1,617.8	1,349.0	11.7	15.2	12.6	12.5
of which: households (1)	240.4	139.1	2,193.0	2,169.0	1,952.6	2,029.9	13.8	7.0	16.1	13.7
Total . . .	2,012.3	3,113.7	3,668.6	3,665.3	1,656.3	551.6	10.8	15.1	13.5	12.2

(1) Estimated.

11.1 per cent). In this sector there was a reduction in lendings to households, which increased by 7 per cent (against 13.8 per cent in 1968). Excluding households from the category « other enterprises and households », the growth rate of lendings in favour of medium and small-sized enterprises is 5 points higher than in 1968 (approximately 1,900 billion, equal to three-quarters of the total lendings to the private sectors); for the « major companies » the difference is greater (8.5 points, 514 billion and 20.1 per cent).

Within the public sector there was a particularly large increase in lendings to « public enterprises » (136 billion, compared with a reduction of 8 billion in 1968) and local authorities (311 billion against 199 billion), while the « other public agencies » received credits for an amount slightly higher than that in 1968 and the autonomous Government agencies made repayments of 54 billion.

The net debit position of the public sector towards the banking system showed a total increase of 270 billion (compared with a reduction of 121 billion in 1968). For the « local authorities » net indebtedness increased by 167 billion; for the « other public agencies » and for the social insurance funds there was a reduction in net borrowing; the autonomous Government agencies, however, moved from a net debit position to a net credit position.

A substantial difference in trend is observable between the major enterprises of the public sectors and those of the private sector. The former, although having substantially greater recourse to bank lending, increased their net debit position by only 16 billion lire, having made a large amount of deposits; the major private companies, on the other hand, increased their net indebtedness by no less than 527 billion, since, in addition to having received a larger volume of funds, they also reduced their deposits. It is estimated that the net credit position of households towards the banking system increased to an extent similar to that in 1968, while the medium and small enterprises in the private sector doubled their net indebtedness, which in the year rose to nearly 700 billion.

Security holdings.— The banks' investments in fixed-interest securities in 1969 were smaller than in the previous year (1,137 billion lire against 1,550 billion) (Table 45). Taking into account the increased

TABLE 45

SECURITIES HELD BY BANKS

(balance sheet values; changes in billions of lire)

Items	1966	1967	1968	1969	1966	1967	1968	1969
	Banks				Savings Banks			
Long-term securities	637.7	642.1	1,173.8	378.1	648.7	322.0	446.4	457.6
Government	215.8	105.4	432.6	121.0	79.5	1.5	24.6	15.5
on behalf of Treasury (1)	79.9	191.3	283.6	- 0.3	144.8	31.2	35.7	18.8
non-mortgage bonds . . .	75.0	109.8	180.1	91.0	100.2	78.1	81.1	150.6
mortgage bonds	213.0	240.8	155.8	155.2	14.0	42.9	70.0	81.5
ENEL	33.7	- 7.9	77.3	28.4	232.7	155.1	239.0	213.4
ENI	9.1	- 7.1	3.1	- 2.6	44.2	10.3	- 10.7	- 13.7
IRI	3.7	- 1.8	1.1	- 9.3	- 4.4	- 11.2	- 15.3	- 11.5
foreign, in lire	4.2	2.4	5.1	4.8	29.2	0.1	0.8	- 2.2
others (2)	3.3	9.2	35.1	- 10.1	8.5	14.0	21.2	5.2
Treasury Bills	89.0	32.8	73.7	- 134.8	2.4	- 44.2	1.5	- 14.9
Shares	23.7	9.7	- 5.2	58.5	- 0.1	—	0.1	0.2
Total . . .	750.4	684.6	1,242.3	301.8	651.0	277.8	448.0	442.9
	Central credit institutions				Total			
Long-term securities	24.7	36.1	- 69.8	301.0	1,311.1	1,000.2	1,550.4	1,136.7
Government	34.2	33.2	14.5	- 24.8	329.5	140.1	471.7	111.7
on behalf of Treasury (1)	160.1	- 59.1	59.0	59.1	384.8	163.4	378.3	77.6
non-mortgage bonds . . .	7.7	17.4	- 82.2	172.7	182.9	205.3	179.0	414.3
mortgage bonds	- 4.5	- 4.0	34.1	- 5.8	222.5	279.7	259.9	230.9
ENEL	- 120.3	58.6	- 71.5	- 0.1	146.1	205.8	244.8	241.7
ENI	- 39.6	- 23.5	- 5.6	91.4	13.7	- 20.3	- 13.2	75.1
IRI	- 8.0	1.2	- 7.0	- 0.7	- 8.7	- 11.8	- 21.2	- 21.5
foreign, in lire	0.3	0.4	—	—	33.7	2.9	5.9	2.6
others (2)	- 5.2	11.9	- 11.1	9.2	6.6	35.1	45.2	4.3
Treasury Bills	- 0.1	- 0.6	—	—	91.3	- 12.0	75.2	- 149.7
Shares	5.0	- 4.8	- 3.7	- 0.8	28.6	4.9	- 8.8	57.9
Total . . .	29.6	30.7	- 73.5	300.2	1,431.0	993.1	1,616.8	1,044.9

(1) Bonds issued by CREDIOP on behalf of the Treasury and of the autonomous Government agencies.

(2) Bonds of industrial borrowers, local authorities and « Autostrade ».

purchase of shares (58 billion compared with a reduction of 9 billion in 1968), the volume of funds invested by the banking system in capital-market securities was 347 billion less than in the previous year.

The greatest reduction was in public securities (189 billion compared with 850 billion in 1968); on the other hand, there was a considerable expansion in purchases of bonds issued by the non-mortgage credit

institutions (414 billion against 179 billion) and ENI (75 billion compared with sales of 13 billion); lastly, subscriptions to land and agricultural funds and of ENEL securities were of the same order of magnitude in both years.

The decline in purchases of fixed-interest securities was more marked in the first half-year (474 billion, or 31 per cent of the total issued) than in the second (663 billion and 37 per cent), whereas in 1968 purchases by the banks had accounted for 50 per cent of total issues and were distributed approximately equally between the first and second half-years.

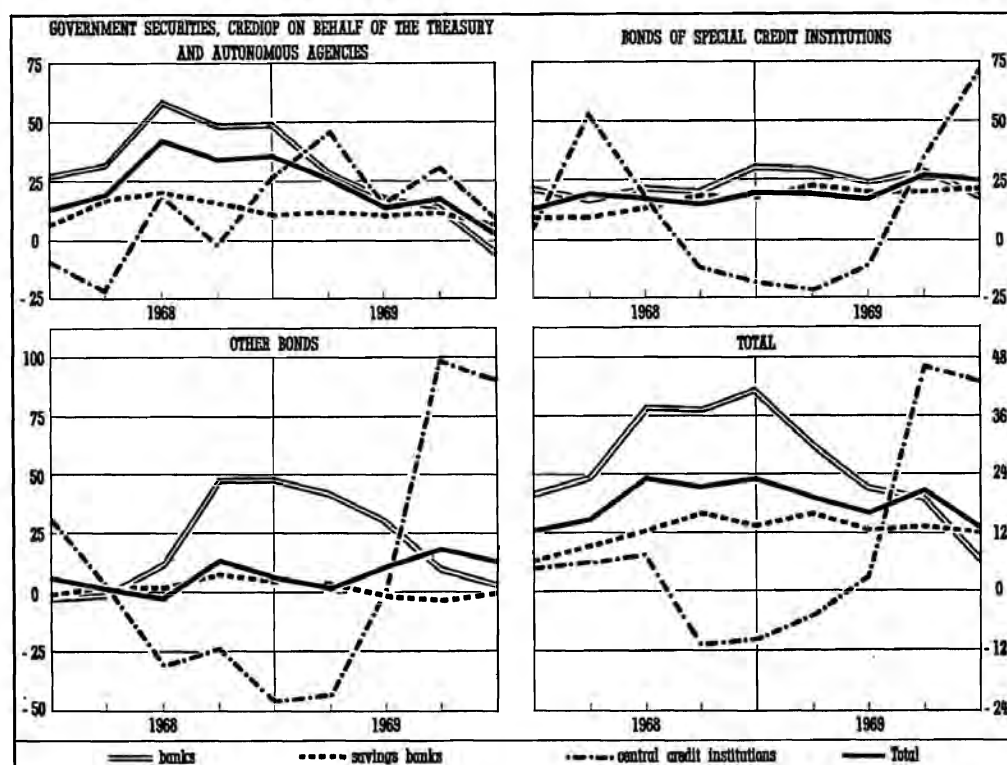
In face of a high demand for loans and a falling off in deposits, the banks in fact increasingly concentrated on institutional lending. In the second half-year, in addition to the more marked difference between the growth rate of lendings and deposits, there were also factors connected with the trend of the capital market. The banks, which in the first half-year had taken up 216 billion of public securities, sold 27 billion in the second half-year. Their action was therefore not stimulated by the increase in rates of yield but, on the contrary, was governed by considerations of possible losses on capital account in the event of portfolio disinvestments. The increase of 663 billion in subscriptions of fixed-interest securities in the second half-year is due, as to 70 per cent, to purchases of bonds of special credit institutions which the banks, owing to the reduced possibilities of direct placing with the public, have had to make in order to enable these institutions to perform their function.

A study of the behaviour of the individual groups of banks shows a different pattern for the banks, savings banks and central credit institutions (Chart 17). The banks, which in 1968 had subscribed three-quarters of the fixed-interest securities taken up by the banking system, last year reduced their participation to only one-third (378 billion lire out of 1,137 billion). But the savings banks acquired an approximately equal volume of securities in the last two years, increasing their share in the total flow of funds from 29 to 40 per cent, while the central credit institutions substantially increased their holdings.

Short-term securities held by the banking system declined in 1969, by 150 billion lire, against an increase of 75 billion in 1968. This decrease was partly due to less use being made of Treasury Bills (65 bil-

lion against 113) to meet the obligatory reserve requirement and, above all, to the sharp reduction of holdings of Treasury Bills for free investment (215 billion, against 38 billion the previous year). The new rules in this field, involving the possibility of more frequent and larger changes in the rate of yield of these securities and, above all, excluding the possibility of realising them automatically at the Bank of Italy, resulted in fact, especially in a period of tight liquidity, in the banking system's being less interested in these securities, despite the greater yield offered.

CHART 17



Long-term securities held by banks and savings banks excluding securities deposited for obligatory reserves and to back cashiers' cheques and shares

(Balance-sheet figures; year-to-year percentage changes at the end of each quarter)

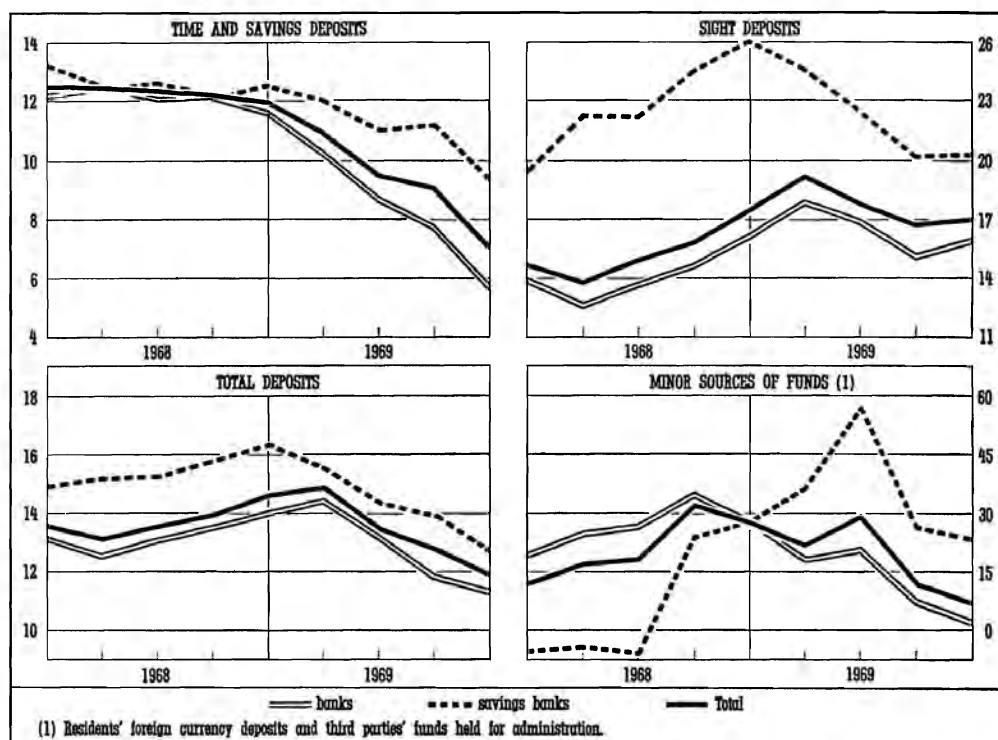
Customers' deposits.— At the end of 1969 bank deposits amounted to 34,458 billion lire, showing an increase on the year of 3,665 billion lire, equal to that of the previous year (Table 42); thus the annual rate of expansion was reduced from 13.5 to 11.9 per cent. This slackening becomes even more consistent (2.7 percentage point) if the in-

crease for 1968 is calculated on the basis of data adjusted to exclude the effects of the strike on the results for the end of 1967.

During 1969 the interest rates offered to depositors were increased; calculations made on the basis of the banks' profit and loss accounts show that the cost of obtaining ordinary deposits, including fiscal chargers, increased on average by 0.17 percentage points.

During the year a period of moderate expansion in the first quarter, continuing the trend which began in the spring of 1968, was followed by a decline in the subsequent months, more marked in the second quarter (Chart 18). This unfavourable tendency applied in particular

CHART 18



Deposits with banks and savings banks, and minor sources of funds
(year-to-year percentage changes as at the end of each quarter,
adjusted for the incidental movements at the end of 1967)

to time and savings deposits, which increased by 1,108 billion lire, or 567 billion less than in 1968; the annual growth rate declined continuously over the whole twelve-month period, and in December it was 5 percentage points less than for 1968 (7 per cent against 11.9). The slackening occurred despite the fact that, during a large part of the

year, the return on deposits continued to increase steadily. To some extent it may have been due to the demand for consumer products, which grew until the occurrence of the events on the labor market in the autumn, and to the rising trend of prices, but the determining factor seems to have been the changes in the choices made by savers as regards the investment of their funds; in particular, investments abroad made in 1969 were more than 1,000 billion lire higher than those in the previous year. The importance assumed by this last factor also seems to be confirmed by the fact that four-fifths of the reduction in the increase in savings deposits related to time deposits, which by their nature are more sensitive to the evolution of the general political and economic situation and to the rates of yield of other forms of financial investment.

In addition to these causes of slackening in the formation of savings deposits, which affected demand, on the supply side there was a tendency by the banks to build up sight deposits, which are less affected by fiscal charges. This tendency seems to have become accentuated during the year as deposit rates increased, despite the lower profitability, for the banks, of the obligatory reserves which have to be constituted in respect of such deposits.

Sight deposits increased by 2,558 billion lire, representing a growth of 17 per cent, compared with 1,994 billion lire and 15.3 per cent in 1968. However, if the data are adjusted to exclude the effect of the strike at the end of 1967, the trend is reversed, since the annual average growth rate for 1968 is then slightly above that for 1969. The trend in 1969 was marked by an acceleration in the first quarter, followed by a sharp reduction in the next two quarters and a revival at the end of the year. The increase recorded in 1969 is the result of a fall of 63 billion lire in time deposits and an increase of 2,621 billion in ordinary deposits, which at the end of 1968 represented 90 per cent of the total of current accounts. The reduction in time (« tied ») deposits is also probably connected with the attraction of yields abroad; it was smaller, however, than that in 1968 (201 billion) since this factor was offset by the flow of funds arising from the transfer of bank deposits from the « savings » category to current accounts.

In the first quarter, despite the reducing effect produced on the monetary base by the foreign component and a smaller contribution by public expenditure, current accounts accelerated owing to the in-

terventions of the central bank and the expanding trend of lendings. Subsequently, as a result of the changes in monetary policy, the growth in current accounts slackened, despite the impulse given by the growth in bank lendings. The slackening continued in the third quarter, while in the fourth quarter there was a modest revival in the annual rate of expansion.

Since the slowing down of bank deposits is mainly attributable to the evolution of time and savings deposits, it had a greater effect on the savings banks, whose funds structurally consist to a large extent of deposits of this kind (69.5 per cent at the end of 1968, against 44.3 per cent for the banks). Actually, although, in absolute values, the reduction in the increase in savings deposits was a good deal greater for the banks than for the savings banks (467 and 100 billion lire respectively), in the case of the banks this was offset by the greater expansion of current accounts (452 billion, compared with only 29 billion for the savings banks). In total, the deposits of the savings banks increased during the year by 1,059 billion lire compared with 1,131 billion in 1968 and those of the banks by 2,529 billion compared with 2,544 billion (Table 42). On the other hand a particularly favourable trend was shown by the central credit institutions, which obtained new deposits amounting to 77 billion lire (against a reduction of 7 billion in 1968).

The analysis by categories of customers shows that the public sector almost halved its contribution to the total increase in deposits (from 13.2 to 7.8 per cent) (Table 44); in absolute values public sector deposits showed an increase of 287 billion lire against 485 billion in 1968, almost entirely accounted for by local authorities and public enterprises. The « other public agencies », however, deposited a considerably smaller amount of funds than in the previous year (82 billion, compared with 344); the social insurance funds, on the other hand, reduced their deposits by 52 billion, whereas they had increased them by 32 billion in 1968.

So far as the private sector is concerned, the slackening in the rate of growth was less than 1 percentage point (from 12.8 to 12.0 per cent) as a result of the good progress of deposits by medium and small-sized enterprises and households, which increased by 3,391 billion lire, representing 92.5 per cent of the total increase in 1969 (against

3,031 billion and 82.6 per cent in 1968); large enterprises, however, reduced their deposits by 13 billion lire, compared with an increase of 153 billion in the previous year.

Profit and loss account.— In order to identify the causes which contributed to determining the trend of profits for the year, overall data of costs and receipts supplied by the banks have been analysed on the basis of the price components (expenses and receipts per cent) and the amounts to which they refer.

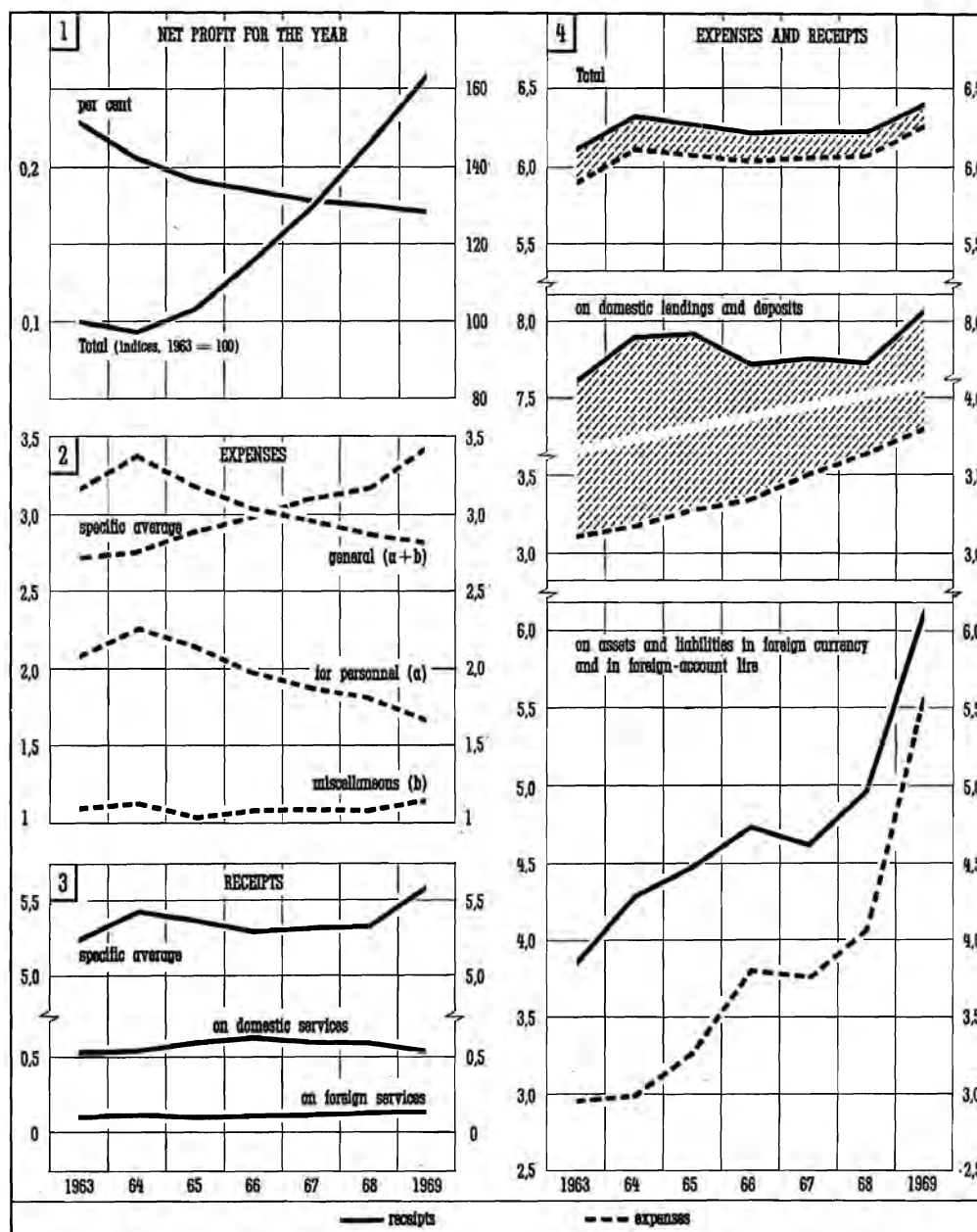
The *indices of specific expenses and receipts per cent* have been obtained by relating the individual expense and receipt items to the average amount of the corresponding asset items (monthly moving average based on data for five quarters). The *indices of average specific unit cost (or receipts)* are given by the ratio between the total specific expenses (or receipts) and the average total of the statement of accounts: they are a weighted average of the various specific unit expenses, with weighting coefficients represented by the proportions of the various liabilities (assets) to the total accounting position. The *relative expense (cost)* of a given liability item is therefore represented by the ratio between the cost per cent of this liability and the average cost of the liabilities. The *indices of general expenses per cent* (and « other receipts ») are obtained by reference to the grand total of the assets. The *index of total expenses per cent*, given by the ratio between total expenses and liabilities, is therefore equal to the sum of the index of the specific average expense per cent and of the general expenses per cent; if this is subtracted from the corresponding index of receipts, we obtain the *index of profit per cent*.

It is important to emphasise that the profit is only one of the two elements which direct the course and measure the results of the banks' credit activities; since the available data do not provide adequate information on the other element, that of the risk, it is not possible to say to what extent changes in the unit profit have been offset by changes in the risk.

An analysis of the data for the period 1963-69 shows that, except in 1964, the banks' total profits increased at an average annual rate of about 8.5 per cent; since the volume of the banks' activities as intermediaries increased faster, particularly in the first three years, the

profit per cent declined without interruption (Chart 19/1); the indices of total expenses and receipts per cent, however, showed changes in the same direction (Chart 19/4). In the period 1964-68 the specific and general expenses moved in opposite directions, the former increasing and the latter decreasing (Chart 19/2); however, thanks to the

CHART 19



Banks' profit and loss account
(unit expenses and receipts; per cent and total profit)

fact that the changes were almost equal in extent, the result was a practically constant rise in the index of total expenses. Also different, but with the trend reversed, was the progress of receipts on assets and « other receipts » in the same period but, owing to the smallness of the changes in the latter, the index of total receipts reflects that of specific receipts (Chart 19/3).

The downward trend of the curve of profit per cent is attributable partly to the growth in competition within the banking system and partly to the changes in monetary policy.

Since there is a fairly large number of banks of some size within the Italian banking system, competition is stronger than in other sectors of the economy and in other countries. It has been made keener by the integration of markets, the growth in industrial activity and the policy of the monetary authorities, which has enabled the larger banks to extend their areas of activity. The support given to the prices of fixed-interest securities between 1966 and 1969 also helped to stimulate competition; on the one hand, it led to the transfer to securities of part of the savings which would otherwise have been deposited with the banks and, on the other hand, by making the yield on one category of the banks' activities fixed and certain, it reduced the mobility of the whole structure of bank lending rates. These two factors induced the banks to use increases in the rates paid on deposits as a means both of influencing the public's choices and of attracting funds from each other.

An intensification of the competition seems to be confirmed, apart from by the frequent infringements to the bank agreement on interest rates, also by the fact that in the three-year period 1967-69 there are many more cases than in the preceding period in which there was a positive correlation between relative expenses and the proportion of the corresponding liabilities of total assets. Insofar as the possibilities of choice by the banks are not limited by restrictions of an administrative nature, a relatively larger increase in the cost of deposits compared with that of other forms of indebtedness reflects, if accompanied by a parallel increase in the ratio of deposits to total liabilities, the difficulties experienced by the banks in inducing the market to accept the combinations which are most favourable for them.

The relatively expansionary monetary policy of the period 1964-1968 is another factor which may have contributed to the reduction in the

unit profit of the banks. In a period in which the banks have adequate monetary base, the volume of banking activities tends to approach the limit represented by equality between marginal expenses and receipts: this leads to an expansion in total profit and a reduction in profits per cent.

In 1969, however, despite a more restrictive monetary policy, the profit per cent (0.170 against 0.176 in 1968) continued to fall; total profits, however, rose from nearly 79 billion lire to nearly 87 billion, an increase of about 11.5 per cent (against 13.7 per cent, the highest for seven years, in 1968). The general increase in market rates gave rise to specific expenses and receipts substantially higher than in previous years; since the slight reductions in general expenses and receipts from services were not sufficient to offset this upward movement, total expenses and receipts, which had remained almost constant in the period 1965-68, increased appreciably (Chart 19/4).

The contraction in the profit per cent occurred despite the fact that, for the first time since 1964, the difference between the profit per cent on lendings and unit costs of deposits increased. The reason for the trend of the profit per cents is also to be sought in the fall in prices of long-term securities; the constant increases in « losses on securities and bills of exchange » and « amortisations and appropriations » seem in fact to indicate that the banks have charged against 1969 part of the potential capital losses on their holdings of securities.

The security market

In 1969 the fixed-interest security market was influenced by the emergence of a new economic and financial situation which required greater control in the creation of the monetary base; this led to a change in the Bank of Italy's policy of intervention on the bonds market and to an increase in yields coupled with greater variability in the prices of securities.

This development, however, had only a modest influence on the demand for funds in the market, since public-sector issues, which amounted to about two-thirds of the total, present a considerable degree of rigidity to variations in the cost of raising money and have to be made, in accordance with the long-term expenditure plans, in the years for

which they are authorised. But a considerable effect was produced on the supply of funds, which in the period of stability of prices came almost exclusively from the public and the banks, while during the period of adjustment of rates it has been provided mainly by the central bank. In the first quarter of 1970 renewed interest in fixed-interest securities was shown by private investors.

In the equity market there was a revival in share prices and in capital increases against cash payment as a result both of the restriction imposed on the activity of investment trusts operating in Italy, coupled with the prospects created by the steps already taken and in course of implementation in favour of the market, and of the expectations of a decline in the purchasing power of the currency.

Fixed-interest securities.— At the end of 1967 the average rates of the bonds issued by the industrial credit institutions and public enterprises, which are the main indicator of the state of the Italian bond market, were at a level (6.70 per cent) below those on the principal foreign capital markets, with the exception of Switzerland; during 1968 and even more so in the early part of 1969, while domestic rates remained stable, foreign rates underwent a sharp increase. In the second half of 1969 there began on the Italian market, too, an upward movement which, accelerated by foreign requirements but influenced above all internally by the prospect of deterioration in the purchasing power of the currency, brought domestic yields, during the early months of the present year, to the same level as foreign yields.

The rise to the present level came about over a period of seven months (August 1969 - February 1970) and in the initial phase it was more rapid for Government securities, which had nominal rates and effective yields about one point lower than those of bonds and shares which were close to par value; the most substantial increases took place, however, in the early months of the present year, when the interventions in support of the market were, in view of the continuance of high interest rates on foreign markets and the need for greater control in the creation of monetary base, at first reduced and then, in the bond sector, suspended.

In the Government security sector, the monthly average yields of long-term Treasury Bills rose from 5.59 in August to 6.36 in December

and 7.52 in March 1970, representing an increase of almost two points compared with the same month of the previous year. The rates on bonds issued on behalf of the Treasury and the autonomous agencies rose in turn from 6.80 in August 1969 to 7.38 in December and 8.74 per cent in March 1970, thus reaching a level about 0.20 per cent above that of the securities of the credit institutions (8.58 per cent), as a result both of the abandonment of support and of the fact that a part of these securities has not yet been floated. In March 1970 the yields on the two groups also showed an increase of about two points compared with a year earlier.

Throughout the period of stability in rates the differences in effective yields on securities bearing different nominal interest rates were contained within modest limits; but during the period of increase, the difference widened to between 0.60 and one and a half points in favour of securities bearing a lower coupon. In April 1970 the average effective rate of bonds with a 5 per cent coupon had reached 9.56, while those of bonds with 6 and 7 per cent coupons were respectively 8.61 and 7.94 (Table 46).

TABLE 46

AVERAGE YIELD OF BONDS
(for different nominal rates)

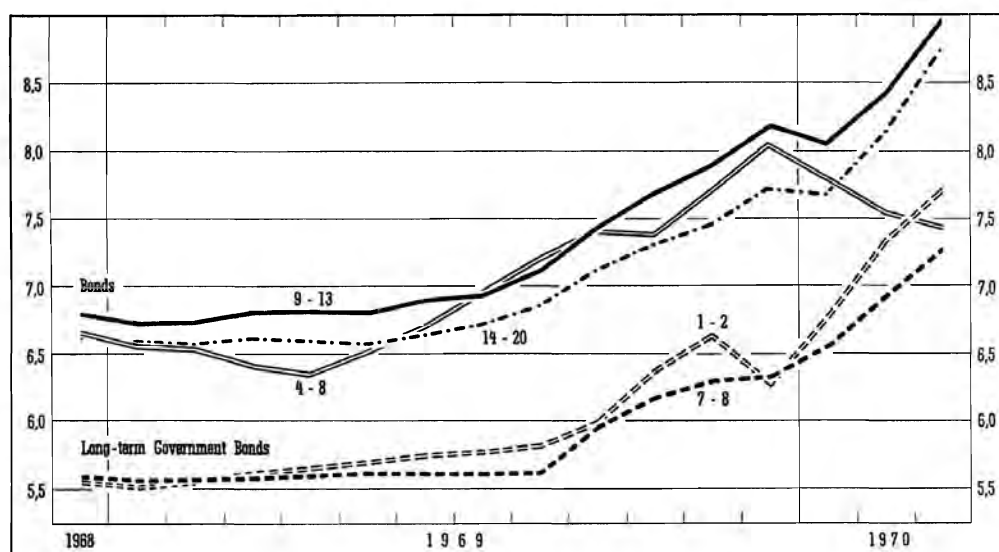
Period	Nominal rate							
	5 %	5.50 %	6 %	7 %	5 %	5.50 %	6 %	7 %
	<i>current</i>				<i>with redemption bonus</i>			
1968 - Dec.	5.59	6.11	6.29	—	6.88	7.17	6.71	—
1969 - »	6.00	6.47	6.72	—	8.55	8.43	7.60	—
1970 - Jan.	5.99	6.44	6.74	7.34	8.49	8.32	7.67	7.90
Feb.	6.02	6.53	6.98	7.29	8.68	8.65	8.22	7.91
Mar.	6.20	6.72	7.23	7.39	9.37	9.25	8.82	8.03
Apr.	6.23	6.77	7.16	7.37	9.56	9.37	8.61	7.94

The preference of savers for high coupons, which is due to the greater depreciation suffered by securities with lower nominal rates, rather than for redemption bonuses, even though these are large, is associated with the variability shown by security prices in recent times and with the uncertainty of yield from the redemption bonus. These

considerations influence particularly the behaviour of private savers who, also because they might not continue to hold the securities until maturity and therefore may not benefit from the redemption bonus, attach greater importance to the current rate.

While in a period of monetary expansion short-term interest rates are generally lower than medium and long-term rates, in a restrictive situation they tend to adopt the opposite position. The lower capital loss involved in disposal of short-term securities compared with long-term securities with the same characteristics in fact leads banks and firms requiring cash to dispose of the securities with earliest maturity. Furthermore, enterprises, in the face of high long-term rates, prefer to raise short-term finance pending an improvement in market conditions. All this creates a structure in which short-term rates tend to rise faster and to exceed medium and long-term rates.

CHART 20



Yield on 6 % bonds and long-term Government Bonds according years of residual life

The study of the changes which have occurred in the structures of Italian interest rates in the most recent period presents some difficulty, since the composition of the securities held in relation to their residual life shows that they are at present centred mainly on long-term maturities, while short-term securities relate to loans of modest amount and do not permit continuity of observation. Nevertheless, an analysis of the behaviour of interest rates on bonds in 1969 shows that the

increase in yields first affected short-term securities (with a rise from 6.35 to 8.04 per cent between April and December 1969), and then rates on medium and long-term securities (which increased in the same period from 6.80 to 8.15 and from 6.60 to 7.72 per cent respectively). In the early months of 1970, while medium and long-term securities, after falling back for a while, continued to rise and in March reached 9.05 and 8.70 per cent, rates on shorter-term securities fell by 0.61 per cent to the lower margin of the rate structure (7.42 per cent). (Chart 20).

Rates on issue, parallel to the trend of rates on the secondary market but at a different pace, showed marked increases in the second half of 1969 and the early months of the current year.

In particular, loans placed in the second half of 1969, during the initial period of the rise in rates, still showed yields on issue lower than those of the secondary market (6.70 compared with 6.90 per cent in the third quarter and 7.25 compared with 7.60 per cent in the fourth). In the early months of 1970 the situation changed: loans placed in January yielded an effective rate of 7.90 per cent against market rates of 7.75; in the subsequent months, however, while market rates have risen considerably, rates on issue have remained more or less stable.

The alternation at the higher level of one and then the other category is typical of periods of adjustment of the general level of rates. In a situation of relative stability the « indicative » rate appears to be that of the secondary market. The uncertainty experienced recently by the market has made it necessary to test, by means of the rate offered on issue, the views of investors on the yield desired, so that this has in practice taken over the function of indicator of the new level of rates. The subsequent rise in secondary-market rates can be explained partly as being the temporary effect of the transition from a period of stability to one of greater variability in prices and partly by the preference for new securities with higher coupons than those of securities in circulation.

In 1969 net issues of long-term fixed-interest securities totalled 3,343 billion lire, representing an increase of 8 per cent compared with the previous year (against 3,092 billion and 43 per cent

in 1968). Including ordinary Treasury Bills for free investment (340 billion) the total of issue was 3,683 billion, a figure lower than the maximum estimate of 4,150 billion given in the previous Report; the difference is considerably reduced if account is taken of the fact that this estimate includes 234 billion of certificates for consolidation of Treasury debts to the Bank of Italy, the issue of which, planned for 1969, took place in the first quarter of the current year (Table 47).

TABLE 47

NET ISSUES OF FIXED-INTEREST SECURITIES
BY CATEGORIES OF ISSUERS, SECURITIES AND INVESTORS
(billions of lire)

Issuers and type of security Investors	Fixed-interest securities						Shares	TOTAL
	Treasury (1)	ENEL ENI IRI (2)	Special Credit insti- tutions	Other enter- prises	Inter- national institu- tions	Total		
1968								
Bank of Italy and Italian Ex- change Office	219.7	—	— 1.3	0.2	— 0.1	218.5	2.2	220.7
Banks	860.2	245.3	438.9	0.2	5.9	1,550.5	— 12.8	1,537.7
Other financial intermediaries . .	54.8	— 9.2	67.7	—	0.9	114.2	18.7	132.9
Companies, private and foreign investors	209.1	313.7	683.3	— 34.0	37.0	1,209.1	464.6	1,673.7
Total . . .	1,343.8	549.8	1,188.6	— 33.6	43.7	3,092.3	472.7	3,565.0
1969								
Bank of Italy and Italian Ex- change Office	1,189.7	— 1.1	26.6	0.2	— 0.5	1,214.9	1.6	1,216.5
Banks	195.6	296.3	645.2	— 2.9	2.5	1,136.7	9.2	1,145.9
Other financial intermediaries . .	9.2	— 4.5	35.9	— 0.5	5.7	45.8	8.9	54.7
Companies, private and foreign investors	157.6	263.4	576.5	— 56.6	4.7	945.6	661.4	1,607.0
Total . . .	1,552.1	554.1	1,284.2	— 59.8	12.4	3,343.0	681.1	4,024.1

(1) Including bonds issued on behalf of the Treasury and those of the autonomous Government agencies and local authorities. Excluding ordinary Treasury Bills and interest-bearing certificates of the Central Post Office Savings Fund.— (2) Including bonds issued by « Autostrade S.p.A. » (IRI Group) (146.6 billion in 1968 and 88.6 in 1969).

For 1970 the issues of fixed-interest securities (including ordinary Treasury Bills for free investment) on the domestic market may be estimated at 3,750 billion lire; the moderate increase compared with 1969 is explained by the greater recourse to the international market planned by certain large Italian issues (approximately 600 billion compared with 125 billion in 1969).

Of the funds raised by the Treasury and the autonomous agencies, which amounted to 1,552 billion lire, equal to 46.4 per cent of the total, three-fifths are destined for infrastructure financing in the agricultural, building and transport sectors, and the remainder for covering financial interventions (increases in endowment and revolving funds of public enterprises and Southern credit institutions, the deficit of the State Railways) and expenditure of a social nature (settlements of deficits of mutual aid institutions and increasing of the social fund for pensions (Table 48).

TABLE 48

NET ISSUES OF FIXED-INTEREST SECURITIES

(percentage breakdown)

Issuers	1959-61	1962-63	1964-65	1966-67	1968	1969
<i>Treasury</i> (1)	27.7	— 0.1	26.1	49.3	43.5	46.4
<i>ENEL, ENI, IRI</i> (2)	10.3	17.6	33.1	14.4	17.8	16.6
<i>Total public sector</i> . . .	38.0	17.5	59.2	63.7	61.3	63.0
<i>Special credit institutions</i>	47.4	68.9	39.9	35.3	38.4	38.4
<i>Companies</i>	14.0	11.6	0.5	— 0.6	— 1.1	— 1.8
<i>International institutions</i>	0.6	2.0	0.4	1.6	1.4	0.4
<i>Total</i> . . .	100.0	100.0	100.0	100.0	100.0	100.0
Annual average (billions of lire)	835	1,088	1,713	2,620	3,092	3,343
Percentage of total issues of securities (fixed-interest and shares)	67.0	66.1	77.6	85.8	86.7	83.1

(1) Including bonds issued on behalf of the Treasury and those of the autonomous Government agencies and local authorities.— (2) Including bonds issued by « Autostrade S.p.A. » (IRI Group).

Public enterprises had recourse to the market for an amount of 554 billion lire, equal to that for the previous year, but slightly lower in relative terms (16.6 per cent against 17.8). The greater part of the public-sector issues were made by ENEL, which continued to issue bonds to finance capital expenditure (234 billion lire) and cover payment of compensation (210 billion) to the former electric companies, which, as is well known, operate mainly in the chemical, financial, metallurgical and telecommunications sectors. The remainder was placed in equal proportions by the Autostrade (Highways) Company of the IRI Group and by ENI; the latter also had recourse to the international market.

The amount raised by the special credit institutions on the bond market reached 1,284 billion lire (38.4 per cent of the total), representing an increase of 96 billion compared with 1968: a large part of the increase related to bonds of the institutions providing credit to industry and public works. The property credit institutions, as a result of the difficulties referred to earlier, raised funds to an amount (469 billion) only slightly above that of 1968, although the demand for loans was very strong. Private enterprises did not make any new issues and the international institutions considerably reduced their recourse to the Italian bond market.

In the second part of 1969, when difficulties in the placing of new loans with the public had become apparent, some issuers relieved the demand for funds on the domestic market by resorting to foreign markets and the international market to raise loans in foreign currency. The funds raised by special institutions and public enterprises, by means of bond loans and borrowing from banks, amounted to 125 billion lire during 1969 (47 billion in 1968); fund-raising continued at a higher rate in the first quarter of 1970, during which it reached 230 billion.

The new market conditions led, at various periods in the year, to considerable variations in the participation of the individual categories of investors in new issues. The expectation of an increase in rates (or of a reduction in prices) which arose in the Italian market from March 1969 onwards, in conjunction with the first movement in the short-term rates sector, began to make their effect felt from July onwards, although only by a reduction in the demand for new securities by private and institutional investors and not by the disposal of existing holdings (Table 49).

INVESTORS OF FIXED-INTEREST SECURITIES
(percentage breakdown)

TABLE 49

Investors	1959-1961	January 1962 June 1964	July 1964 December 1965	1966-67	1968	1969
Bank of Italy and Italian Exchange Office	2.8	5.4	3.9	6.8	7.1	36.3
Banks	26.9	31.8	55.2	44.1	50.1	34.0
Other financial intermediaries	8.4	34.1	10.4	1.8	3.7	1.4
Companies, private and foreign investors	61.9	28.7	30.5	47.3	39.1	28.3
Total . . .	100.0	100.0	100.0	100.0	100.0	100.0
Average on yearly basis (billions of lire)	835	1,132	1,847	2,620	3,092	3,343

The « Company, private and foreign investors » category, consisting mainly of households subscribed fixed-interest securities totalling 946 billion, representing a reduction of 264 billion compared with 1968 (28 per cent of the total against 39). The reduction was accompanied by an increase of 197 billion in subscriptions for new shares and of about 90 billion in foreign investment trust certificates. The purchases of fixed-interest securities by this category were concentrated in the first half-year (1,000 billion), during which the increases in interest rates had occurred only in the money market; in the second half-year the amount of new subscriptions was almost equal to that of disposals so that, in the period of progressive reduction in prices of securities, this category made no contribution to absorbing new loans.

As already pointed out, investment in fixed-interest securities was adversely affected in 1969 by fears of losses on capital account, associated with uncertainties about the future of the purchasing power of the currency. The relative rapidity with which the process of adjustment of rates took place enabled the first-mentioned fears to be reduced to a minimum, so that, despite the aggravation of the monetary anxieties, savers showed a renewed interest in fixed-interest securities in the first quarter of 1970.

Subscriptions by the public, after the standstill of the second half of 1969, amounted in this period to 480 billion lire, equal to about three-fifths of total issues.

The banks behaved in much the same way as private individuals and increased their holding of securities by 778 billion in the first seven months of the year, and by 359 billion in the remaining five months; the total increase of 1,137 billion was 414 billion less than in the previous year (639 billion if ordinary Treasury Bills are also taken into account).

The action of the banks, for whom the purchasing power of the currency is a factor of minor significance, indicates that a large proportion of the disposals of securities made in the period of falling prices form part of their normal activity as intermediaries; this seems to confirm the hypothesis that an increase in yields on securities, by creating potential capital losses, reduces the propensity of the banks to liquidate their security holdings.

The reasons for the sharp contraction in investments in securities are to be sought above all in the changes which took place in the liquidity position of the banks, the structure of interest rates and the liquidity of securities, i.e. in the more rapid growth in lendings compared with deposits, the increased cost of raising funds and the reappearance of variable security prices.

On the whole therefore, while there were no large liquidations of security holdings, there was a certain reluctance to subscribe to new-issue securities which, in the second part of the year, were taken up mainly by the Bank of Italy. The Bank, which in recent years had been able to restrict the net increase in its own holding of securities while operating actively on the market, in the year under review substantially increased its subscription of new loans (1,272 billion lire compared with 694 billion in the previous year) and purchases in support of prices on the secondary market, and at the same time had to reduce sales to the banking system and to private individuals.

The knowledge of the amount and distribution, during the year, of the funds made available on the capital market as a result of redemptions and payments of coupons is particularly useful in planning the schedule of new issues. Insofar as it is applied to the subscription of new securities, this flow constitutes an increasingly important element of self-expansion of the market. In 1969 it reached 2,464 billion lire, equal to 51 per cent of the gross issues of fixed-interest securities (against 2,130 billion and 49 per cent in the previous year) and 62 per cent of it was formed in the first and third quarter and the remainder in the second and fourth, with a high concentration respectively, in the months of January and July, April and October.

The breakdown of the redemptions, amounting to 1,229 billion lire, is as follows: by the Treasury, directly or through CREDIOP, 43.6 per cent (of which slightly less than half was applied to renewal operations); by the special credit institutions 39.1 per cent; by public enterprises 11.4 per cent and by other issuers 5.9 per cent. The more extensive participation of the Treasury in redemption of loans, compared with its share of the securities in circulation (35.6 per cent at the end of 1968) is due to the shorter average life of Government securities compared with other securities.

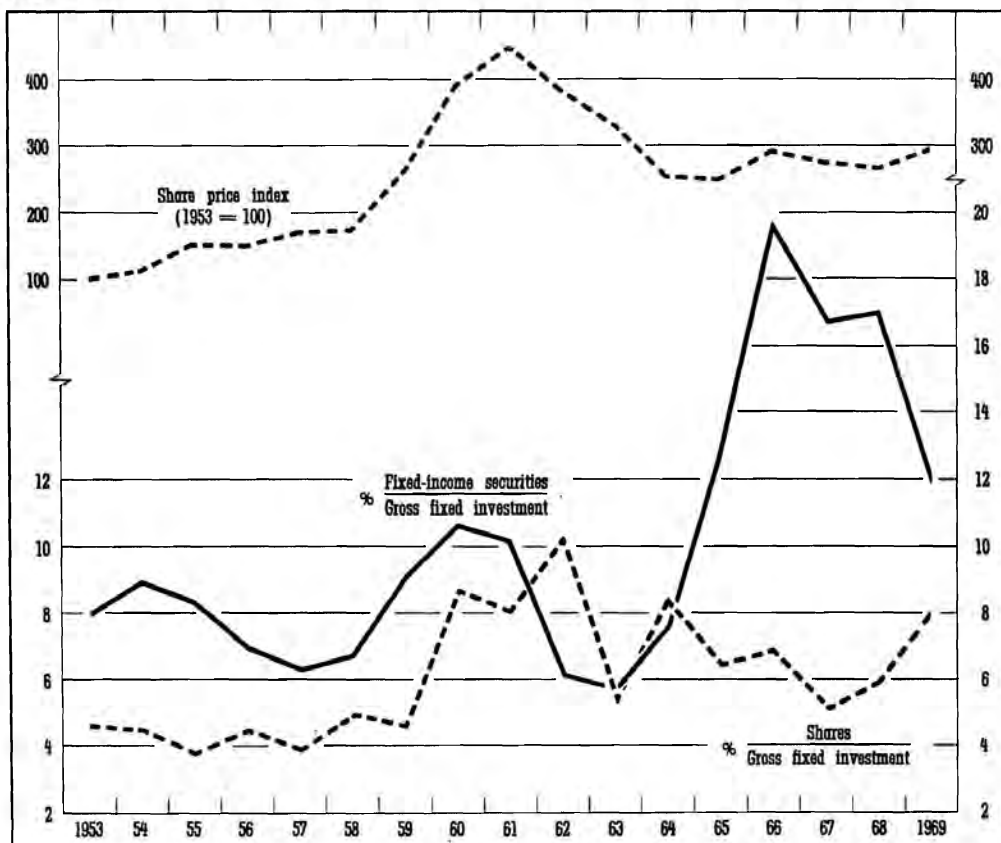
The breakdown of the interest liability (1,235 billion lire) reflects the participation of the individual sectors in total indebtedness, with a less than proportional liability for the Treasury, however, owing to the lower nominal rate of public securities; in 1969 the Treasury paid 33.8 per cent of the total interest, the special institutions 42.4 per cent, public enterprises 17.8 per cent and other issuers 6.0 per cent.

Shares.— A notable feature of the equity market in 1969 was a marked recovery in share prices, accompanied by a considerable growth in stock exchange bargains, a slight increase in dividends distributed and a very large rise in issues of shares against payment. The intervention of investment trust funds on the market, following the regulation that they must invest at least 50 per cent of their portfolios in Italian securities, helped the revival of the equity market, by the direct and indirect effects deriving from net purchases of shares of over 80 billion lire (equal to 12 per cent of new issues).

Until 1968 capital increases, after the peak of 1962, had remained stationary at around the level of 500 billion a year; consequently, a progressive reduction had taken place in the relative importance of shares compared with total issues of securities (from 40 per cent in 1962 to 14 per cent in 1968). In the year under review this trend was interrupted; share issues net of duplications amounted to 681 billion, equal to 17 per cent of total issues. Among the factors which enabled enterprises to increase the amount of risk capital raised, prompted by the increased demand for fixed investment, mention may be made of the upward trend of share prices, due in turn to the presence on the market of a demand which was sometimes very keen and which encouraged the placing of new share issues without any negative repercussions on their prices on the secondary market; the steady rise in the cost of raising money by means of bonds, which reduced the margin of desirability, in terms of total cost, of borrowing compared with increasing enterprises' own funds; the reduced interest of the public in investment in fixed-interest securities; the tax advantages introduced in the previous year; and lastly, the ending of the negative effects of the introduction of the withholding tax on dividends and its subsequent amendments.

The connections between the movement of prices and subscriptions of bonds on the one hand and capital increases on the other are clearly shown by a study of developments which have affected the market since 1953. Between the progress of share prices and capital increases, which may be identified with the demand for shares from the « companies, private and foreign investors » sector, as the proportion of demand from other sectors is very modest, there is a high degree of positive correlation, as can be seen from an examination of the movements of the market over a sufficiently long period. The type of relationship new existing between issues of shares and demand for fixed-interest securities by the « company, private and foreign investors » sector is not exactly defined for the period of steady growth in the size of the capital market (1953 - 1961), whereas it can be sufficiently traced, as a substitution ratio, in the last five years (Chart 21).

CHART 21



Issues of shares and their principal determining factors

(share prices, securities acquired by the « companies, private and foreign investors » sector and investments)

Subscriptions to capital increases by groups of investors in the « companies, private and foreign investors » sector (private individuals, companies and non-residents) confirm the trends which have been in operation for several years, namely, a progressive reduction in the relative size of private share holdings, a standstill in the holding of share capital by companies, and an increase in shares held by non-residents.

Italian share prices, unlike those on the main foreign stock markets, showed a rising trend during 1969, reflected by a positive change of 16.6 per cent in the share price index. The volume of bargains on the stock exchanges also increased substantially, particularly in the periods of marked increase in prices, rising from 1,487 billion in 1968 to 2,408 billion in the year under review.

The yields on shares, which fell from 4.41 per cent to 3.86 per cent between December 1968 and December 1969, were reduced to an extent relatively smaller than the increase in prices, owing to a rise in dividends distributed.

A study of the monthly progress of share prices enables two periods to be distinguished, corresponding to the first and second half years, which are very similar, being characterised by an initial standstill, followed by considerable rises and then by smaller falls. The most outstanding increase took place in the month of April when the demand for shares—inspired by the new regulations on portfolio investments of foreign investment trust in Italy and by good results in the dividend season—was very strong, resulting in an acceleration in the number of bargains (84 per cent higher than in the same period of the previous year) and causing share prices to rise, by the middle of the month, by 20 per cent compared with March. The flow of funds which the investment trust directed to the share market during the period January to May, calculated on the basis of the net increases in their share holdings, is estimated at around 30 billion lire.

A second revival in prices can be traced after the summer pause in conjunction with the announcement of the forthcoming inclusion in official prices of certain bank shares and with Government approval of the draft law on investment trusts and further tax advantages for increases in capital against payment; this brought the share price index in November to its highest level for the year. In December, however,

probably as a reflection of the trade union disputes and production losses connected with them, a large supply of securities caused prices to fall.

In the period June to December the positive effect of the contribution of investment trusts to demand for shares, estimated at about 50 billion lire, certainly played a part in determining the movement of prices; however, a judgment regarding the effects of the policy pursued by investment trusts on the efficiency of operation of the market seems to be premature.

The activity of the special credit institutions

The demand for investment funds reached exceptional dimensions in 1969, particularly in the second part of the year. Whereas in 1968 the greatest impulse to demand for credit came from residential building, in 1969 the industrial sectors were responsible for the expansion; demand for financing applied to the real estate credit institutions, which was keen in the early part of the year, slackened off in the last months of 1969 as the expansionary effects of the transitional town-planning regulations wore off.

In the second part of the year the institutions reduced their assumption of new lending commitments pending the establishment of more balanced conditions on the capital market; in the industrial credit sector this attitude was also affected by the presence of a large subsidised area, characterised by the lack of automatic arrangements for the adjustment of the rates recognised by the Government to the institutions to changes in the cost of obtaining resources.

In 1969 the funds raised by the special credit institutions amounted to 3,116 billion lire compared with 2,661 billion in 1968; the resources for normal financing activities, i.e. excluding bonds on behalf of the Treasury, slackened compared with the previous year, having increased by 2,001 billion lire or 14.0 per cent against 2,162 billion or 17.9 per cent in 1968.

The new economic conditions which developed half-way through the year and their effects on capital market rates led to difficulty in obtaining funds, which gradually increased, especially for the real estate

credit institutions. In the last five months of the year the increase in the volume of bonds, medium-term savings deposits and interest-bearing certificates amounted to 375 billion lire, compared with 672 billion in the corresponding period of the previous year.

An alternative source of funds, however, was recourse to foreign markets, although at increasing cost, in the period of greater instability of the Italian capital market. The industrial credit institutions raised about 100 billion lire outside the country, either by issuing Eurobonds or by obtaining loans direct from foreign banks. Recourse to foreign sources continued on a very large scale in 1970, reaching 210 billion lire in the first three months.

In 1969 the volume of lendings by the special credit institutions increased by 3,034 billion lire, against 2,434 billion in 1968; the increase was due to operations on behalf of the Treasury, which reached an unprecedented level (Table 50).

TABLE 50

LENDINGS BY SPECIAL CREDIT INSTITUTIONS

(billions of lire)

Type of loan	Outstand- ing at end 1969	Changes			
		absolute		per cent	
		1968	1969	1968	1969
DOMESTIC LENDINGS	14,110.7	1,839.4	1,665.3	17.4	13.4
Medium and long-term	13,335.8	1,731.1	1,609.9	17.3	13.7
industry and public works	8,284.6	991.2	879.4	15.5	11.9
real estate	4,408.7	667.2	673.6	21.7	18.0
agricultural improvement	642.5	72.7	56.9	14.2	9.7
Short-term credit to agriculture	774.9	108.3	55.4	17.7	7.7
FOREIGN LENDINGS	721.4	108.8	277.0	32.4	62.3
Financial credits	494.8	121.1	163.8	57.7	49.5
Lendings to non-residents	226.6	- 12.3	113.2	- 9.8	99.8
Total . . .	14,832.1	1,948.2	1,942.3	17.8	15.1
ON BEHALF OF THE TREASURY	4,405.7	485.3	1,091.4	17.2	32.9
Total . . .	19,237.8	2,433.5	3,033.7	17.7	18.7

The remaining financing activities showed a sharp reduction in short-term transactions and in domestic medium and long-term transactions, as a result of the difficulties experienced in obtaining funds in the latter part of the year; loans abroad, on the other hand, increased markedly from one year to the other in the case of financial

credits granted under the export credit insurance system and still more in the case of lendings to non-residents, granted for the most part to companies of international importance.

The slackening in short-term financing activities, which was particularly pronounced, involved both credits for farmers' working capital and equipment and operations related to marketing of products.

Medium and long-term loans increased by 1,610 billion lire, compared with 1,731 billion in 1968. The contraction occurred in the sector of credit to industry and public works, and agricultural improvement loans, while real estate financing increased slightly more than in 1968.

A characteristic feature of medium and long-term credit activity is the increasing intervention by the Government with the object of directing savings towards certain sectors and areas by fixing preferential rates.

In the last two years about half the increase in the domestic and foreign lendings of the special credit institutions has been accounted for by subsidised financing.

The burden on the Government budget due to the granting of interest-reducing subsidies, which totalled 36 billion lire in the ten-year period 1950-59 and 957 billion in the following ten years has gradually increased, rising from 8 billion in 1959 to 204 billion in 1968 and 236 billion in 1969, and amounting, in these last two years, to 2.3 and 2.4 per cent respectively of budget revenues (Table 51). Expenditure for the years 1968 and 1969 increased considerably as a result of the allocations made to assist enterprises affected by flood damage. In the coming years this burden will increase, unless the acceptance of new financing demands is restricted, as a result of the larger contribution by the Government due to the increase of at least one percentage point in the basic rates payable to the credit institutions and also to the provision of larger subsidies to the main projects in Southern Italy.

The greatest effect on the Government budget is attributable to action in favour of industry, as a result of the larger amount of subsidised credit provided.

Borrowings at preferential interest rates by industrial enterprises rose between 1960 and 1969 from 35 to 72 per cent of the total

TABLE 51

BURDEN ON THE GOVERNMENT OF INTEREST-REDUCING SUBSIDIES (1)
(billions of lire)

Sector and object	Financial years			
	Average		1968	1969
	1950-59	1960-67		
INDUSTRY, COMMERCE AND ARTISANS	0.8	37.8	140.0	162.6
medium and small-sized industries	—	11.6	22.0	27.0
industrialisation of the South	0.2	14.9	36.2	43.0
export credits	0.3	3.0	19.4	19.4
natural disasters	—	0.9	39.1	50.3
other	0.3	7.4	23.3	22.9
BUILDING	1.1	3.4	13.5	13.6
AGRICULTURE	1.7	23.5	50.6	59.3
improvement credit	1.5	12.2	28.6	35.5
credit for working capital	0.1	6.9	7.1	6.4
natural disasters	0.1	4.4	14.9	17.4
TOTAL . . .	3.6	64.7	204.1	235.5

(1) Relates to amounts appropriated for the year; only in respect of the part charged against the Cassa per il Mezzogiorno (industrialisation of the South) do the figures refer to actual disbursements during the year.

indebtedness towards the special credit institutions; in particular in the last three years more than four-fifths of the new credits received by industry benefited from interest-rate subsidies.

The unit advantage to the beneficiary enterprises at the beginning 1970 has increased; so that the maintenance of the previous subsidised rates at a time when market rates are rising, and in a period when the effective cost of borrowing is already being reduced owing to the decline in the value of the currency, may be regarded as a further Government contribution to covering the cost of money.

The activity of the special credit institutions for industry and public works in 1969 was characterised by a sharp expansion in export credits and in lendings to non-residents, which was offset by a considerable slackening in loans for the financing of investments.

The large increase in operations relating to the export credit insurance system is the result not only of the raising of the maximum limit on guarantees which may be undertaken by the Government but also by the maturity of commitments undertaken in earlier years and

the reduction in repayments (Table 52). In this sector, particularly financial credits, the time-lags between the assumption of the obligation and the provision of the funds create, both for the institutions supplying the funds and for the country, the risk that the operations will be carried out at a time when the situation of the capital market and of the balance of payments is less favourable. Moreover the substantial rise in financial credits, together with the tendency of those to exporters to be for longer maturity, has increasingly reduced the proportion of repayments compared with credit provided, thus limiting the possibility of granting new credit. The ratio between repayments and new transactions, which in the period 1964-1966 was 61.3 per cent, fell in the subsequent two years to 48 per cent, and to 32.5 per cent in 1969. In this last year the funds were entirely raised on the market, the refinancing institution having intervened almost exclusively by the granting of interest-rate subsidies. Financial credits, largely « tied » to supplies by Italian enterprises, were to a greater extent directed to the Socialist countries; in particular the USSR benefited from nearly two-thirds of the increase in loans.

TABLE 52

EXPORT CREDITS GRANTED
BY THE SPECIAL INDUSTRIAL CREDIT INSTITUTIONS (1)
(billions of lire)

Type of loan	Amounts outstan- ding at end 1969	Credit provided		Repayments		Net increases		Lending commit- ments at end 1969
		1968	1969	1968	1969	1968	1969	
Credits to exporters	534.0	255.7	274.8	162.8	119.4	92.9	155.4	356.2
Financial credits	494.8	145.0	197.8	23.9	34.0	121.1	163.8	368.0
tied	235.3	69.3	133.5	1.3	6.8	68.0	126.7	308.3
not tied	259.5	75.7	64.3	22.6	27.2	53.1	37.1	59.7
Total . . .	1,028.8	400.7	472.6	186.7	153.4	214.0	319.2	724.2

(1) Excluding refinancing and consolidation by the Italian Exchange Office and the National Insurance Institute, amounting at the end of 1969 to 114.4 billion lire (92.5 billion at the end of 1968).

The smaller increase in operations connected with the financing of investments affected all sectors of economic activity, particularly public works and services, as regards both subsidised-rate and market-rate transactions.

This tendency may be associated, on the one hand, with the greater recourse of enterprises to risk capital and, on the other, with the difficulties of raising funds experienced in the latter part of the year and also, in the case of subsidised-rate transactions alone, with the fact that the credit institutions were waiting for the adjustment of the lending rates chargeable by them to the new level of costs of obtaining funds.

The average weighted cost of subsidised borrowing in 1969, as a national average, was 4.7 per cent as in 1968; for enterprises situated in Central and Northern Italy it was 5.4 per cent and for those situated in the South, 3.6 per cent. The average rate of ordinary and subsidised credits was 5.9 per cent for the whole of Italy, 6.5 per cent for Central and Northern Italy and 5 per cent for the South. During 1969 and the early months of 1970 the difference between market rates and subsidised rates widened, finally reaching nearly five percentage points.

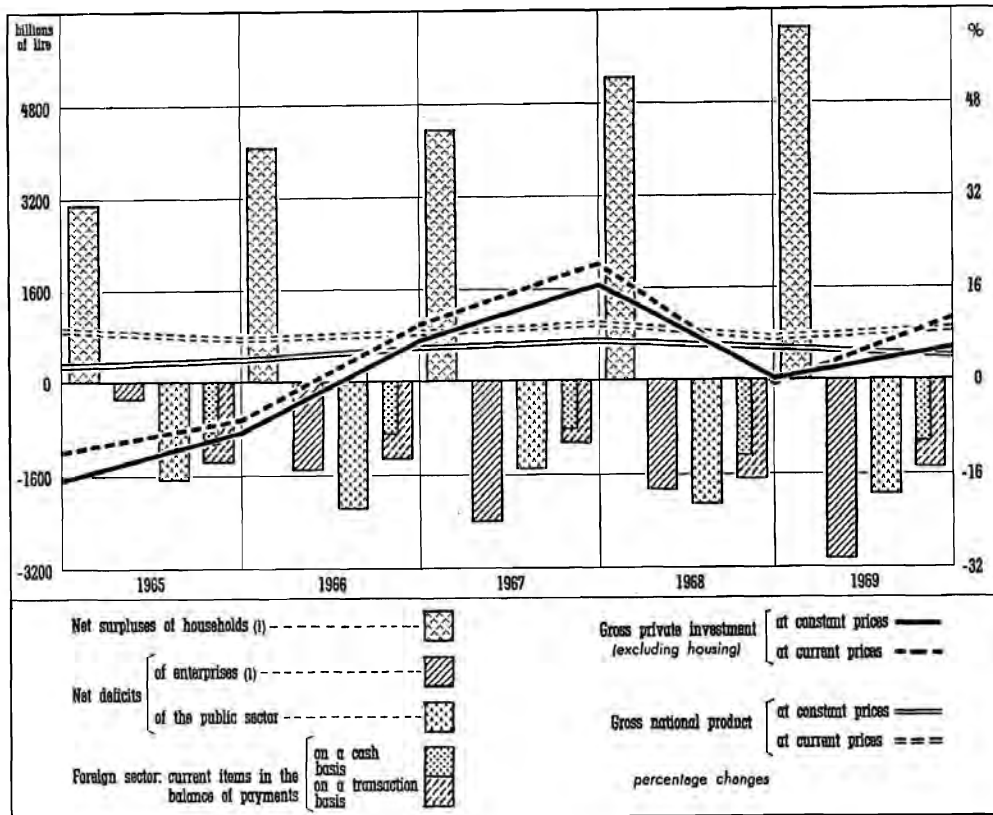
Financing of the economy

Financial accounts.— In 1969 the trend of households' assets and liabilities resulted in a surplus of 6,120 billion lire, which, expressed as a ratio of the sector's available income, represents a rise to 15.7 per cent from 14.7 per cent in 1968 (if the statistics are adjusted for the incidental factors which affected some items at the end of 1967). As households' propensity to save increased to 16.3 per cent, from 15.1 per cent in the previous year, the increase in the volume of the sector's saving was primarily in the form of financial assets, domestic and foreign, which were subsequently channelled into financing of the requirements of the other sectors (Table 53 and Chart 22).

In 1969 the net indebtedness of enterprises increased sharply over the previous year, rising to 3,030 billion lire from 1,820 billion (both figures adjusted for incidental movements).

From the overall picture of the financial accounts it appears that the strengthening of the expansionary impulses to economic activity compared with the previous year was mainly due to enterprises, while the excess of public sector investment over saving was smaller than

CHART 22



Financial balances of sectors
(changes in billions of lire)

(1) The figures for 1967 and 1968 have been adjusted for the incidental factors at the end of 1967.

in 1968. The deficit of the foreign sector (in respect of current items), though remaining at a high level, declined from 1,640 to 1,480 billion lire.

Financial assets of the economy.— In 1969 the expansion of the liquid assets of the economy (« households » and « enterprises ») was the same, in absolute terms, as in the preceding year, the rise having amounted to 4,680 billion lire, making a growth rate of 11.6 per cent (lower than the 12.9 per cent in 1968). (Tables 54 and 55).

Foremost among the sectors which, by seeking to obtain funds from the banking system and the Treasury, brought about a corresponding formation of liquidity, was the economy, demand from which reached 3,370 billion lire (against 2,140 billion in 1968). Of this

NATIONAL FINANCIAL
(changes in billions of lire;

Sectors	1 9 6 8											
	Households	Enterprises	Credit institutions				Public sector				Foreign Sector	Unclassified and discrepancies
			BI-IEO	Banks	Special credit institutions	Insurance companies	Central authorities	Local authorities	Social Insurance Funds	Autonomous Government agencies		
Classes of assets and liabilities												
A) Gold	—	—	327.1	—	—	—	—	—	—	—	327.1	—
a) Notes and coin	189.4	20.0	— 9.9	72.0	— 0.1	— 0.7	— 0.2	—	— 2.7	1.3	—	—
Notes and coin	—	—	264.2	—	—	—	3.5	—	—	—	1.4	—
b) Demand deposits	937.0	983.8	2.5	289.8	— 44.9	7.1	1.0	102.7	22.6	138.4	— 11.6	133.8
Demand deposits	—	—	57.3	2,451.0	— 0.6	—	206.0	—	—	52.7	157.9	— 362.1
1) Bank deposits	937.0	976.5	—	2,058.2	—	7.1	— 1.6	102.9	37.7	— 1.4	—	—
2) Cheques in clearing	—	—	—	— 133.7	—	—	—	—	—	—	—	— 133.7
3) Cashiers' cheques outstanding	—	—	—	— 49.6	—	—	—	—	—	— 22.5	—	— 27.1
4) Postal deposits	—	15.3	—	— 6.7	—	—	8.6	—	—	—	—	—
5) Interbank accounts	—	—	—	254.8	0.8	—	—	—	—	—	—	—
Interbank accounts	—	—	—	442.4	— 0.6	—	—	—	—	—	—	— 186.2
6) Depos. at Bank of Italy & IEO	—	—	57.3	19.1	58.5	—	—	—	0.1	—	— 11.6	— 8.8
7) Deposits at Central auth.	—	— 8.0	2.5	— 1.6	— 27.6	—	197.4	— 0.2	— 40.5	139.2	—	133.6
8) Dep. at auton. Gov. agencies	—	—	—	—	—	—	—	—	16.6	52.7	—	36.1
9) Foreign and others	—	—	—	157.9	— 76.6	—	2.6	—	8.7	23.1	157.9	— 42.2
c) Other deposits	1,844.4	455.6	173.2	403.9	22.5	—	3.6	—	— 5.0	—	— 5.4	—
Other deposits	—	—	268.2	1,963.6	299.3	—	339.5	—	—	— 14.8	8.3	28.7
1) Bank deposits	1,256.0	418.6	—	1,674.6	—	—	—	—	—	—	—	—
2) Postal deposits	309.5	30.0	—	—	—	—	339.5	—	—	—	—	—
3) Interbank accounts	—	—	—	295.2	22.5	—	—	—	—	—	—	—
Interbank accounts	—	—	—	289.0	—	—	—	—	—	—	—	28.7
4) Spec. cred. inst. sav. cert.	297.3	—	—	—	297.3	—	—	—	—	—	—	—
5) Foreign deposits	—	—	173.2	— 164.9	—	—	—	—	—	—	— 5.4	—
Foreign deposits	—	—	— 5.4	—	—	—	—	—	—	—	8.3	—
6) Others	— 18.4	7.0	—	273.6	—	—	3.6	—	— 5.0	—	—	—
Others	—	—	273.6	—	2.0	—	—	—	—	— 14.8	—	—
d) Short-term securities	— 1.8	—	— 360.0	82.8	0.1	—	174.8	—	—	—	— 453.7	—
e) Short-term loans	—	226.2	37.8	2,912.1	59.0	—	110.1	—	— 37.0	6.8	547.2	— 17.9
Short-term loans	175.2	1,243.6	—	691.6	169.9	16.0	209.8	133.1	169.8	116.6	921.8	— 3.1
1) Banks loans	175.6	1,167.9	—	1,710.7	—	2.1	75.7	133.1	141.0	19.5	—	—
2) Special credit institutions loans	—	55.7	—	—	55.7	—	—	—	—	—	—	—
Special credit institutions	—	—	—	197.8	3.5	—	—	—	—	—	—	—
Special credit institutions	—	—	—	3.5	197.8	—	—	—	—	—	—	—
4) BI-IEO	— 0.4	—	317.4	167.6	15.1	—	132.4	—	2.7	—	—	—
5) Foreign and others	—	226.2	— 279.6	1,003.6	— 0.2	—	110.1	—	— 37.0	6.8	547.2	— 17.9
Foreign and others	—	20.0	—	520.5	— 43.0	18.1	1.7	—	26.1	97.1	921.8	— 3.1
f) Long-term loans	—	— 11.9	98.0	301.6	1,768.2	34.1	816.0	— 0.7	54.8	— 2.0	100.1	25.6
Long-term loans	359.4	1,520.8	—	—	260.3	— 0.1	86.7	783.3	— 0.4	11.4	165.4	— 3.0
1) Banks	64.8	171.4	—	301.6	—	—	—	65.8	— 0.4	—	—	—
2) Special credit institutions	270.0	1,178.1	—	—	1,659.4	— 0.1	0.2	212.6	—	— 1.4	—	—
3) Foreign	—	— 13.0	44.0	—	108.8	—	—	—	—	—	100.1	25.6
Foreign	—	67.9	—	—	— 7.6	—	32.5	—	—	7.3	165.4	—
4) Others	—	1.1	54.0	—	—	34.1	816.0	— 0.7	54.8	— 2.0	—	—
Others	24.6	103.4	—	—	267.9	—	54.0	504.9	—	5.5	—	— 3.0
g) Bonds	1,300.0	17.0	360.8	1,550.4	73.2	71.6	— 38.3	—	7.5	—	3.6	—
Bonds	—	516.2	—	—	1,188.6	—	1,005.4	46.9	—	291.4	291.4	5.9
1) Gov. and auton. Gov. agencies	187.8	6.0	219.3	850.0	45.7	7.5	— 18.1	—	— 2.6	—	1.2	—
Gov. and auton. Gov. agencies	—	—	—	—	—	—	1,005.4	—	—	291.4	—	—
2) Bonds of spec. credit inst.	675.8	8.0	— 1.3	438.9	13.6	47.4	— 9.8	—	16.0	—	—	—
Bonds of spec. credit inst.	—	—	—	—	1,188.6	—	—	—	—	—	—	—
3) Other bonds	289.5	3.0	— 0.1	261.5	12.6	16.4	— 10.4	—	— 5.9	—	2.4	—
Other bonds	—	516.2	—	—	—	—	—	46.9	—	—	—	5.9
4) Foreign bonds	146.9	—	142.9	—	1.3	0.3	—	—	—	—	291.4	—
h) Shares and equity participations	85.0	267.1	5.0	32.8	15.5	29.4	407.0	46.6	11.2	—	236.1	— 7.9
Shares and equity participations	—	765.6	—	71.0	82.5	0.2	—	—	—	—	208.5	—
i) Other assets	1,171.2	44.8	—	—	—	—	—	—	—	— 2.4	—	—
Other liabilities	—	—	—	—	—	230.1	7.4	—	284.1	—	692.0	—
1) Actuarial reserves	479.2	35.0	—	—	—	230.1	—	—	284.1	—	—	—
2) Others	692.0	9.8	—	—	—	—	7.4	—	—	— 2.4	692.0	—
j) Unclassified and discrepancies	—	—	—	—	—	—	—	—	—	—	—	434.7
Unclassified and discrepancies	—	—	44.8	312.3	— 218.4	—	—	—	—	—	191.7	104.3
Total assets	5,525.2	2,002.6	634.5	5,645.4	1,893.5	141.5	1,299.2	148.6	51.4	142.1	870.0	568.3
Total liabilities	534.6	4,046.2	634.5	5,489.5	1,781.6	246.2	2,033.1	963.3	453.5	457.3	2,511.8	— 229.3
Net financial surplus or deficit	4,990.6	2,043.6	—	155.9	111.9	104.7	733.9	814.7	402.1	315.2	1,641.8	797.6

ASSETS AND LIABILITIES

figures in italics denote liabilities)

TABLE 53

		1 9 6 9														
Total			House-holds	Enter-prises	Credit institutions				Public sector				Foreign Sector	Unclassi-fied and discrep-ancies	Total	
Assets	Liabilities				BI-IEO	Banks	Special credit institutions	Insur-ance compa-nies	Central author-ities	Local author-ities	Social Insur-ance Funds	Auton-omous Govern-ment agencies			Assets	Liabilities
327.1	327.1	A)	—	—	20.5	—	—	—	—	—	—	—	20.5	—	20.5	20.5
269.1	—	a)	634.4	60.0	3.0	14.9	—	—	0.6	—	0.1	12.3	—	—	719.3	—
—	269.1		—	—	710.0	—	—	—	8.8	—	—	—	0.5	—	—	719.3
2,562.2	—	b)	1,283.0	1,270.3	5.9	7.1	242.6	7.6	201.4	144.4	219.8	241.1	13.0	280.2	3,404.8	—
—	2,562.2		—	—	266.4	2,767.6	15.6	—	143.3	—	—	277.7	208.5	142.7	—	3,404.8
2,058.2	2,058.2	1)	1,283.0	1,193.7	—	2,554.9	—	7.6	10.9	144.3	41.5	6.1	—	—	2,554.9	2,554.9
-133.7	-133.7	2)	—	—	—	117.2	—	—	—	—	—	—	—	117.2	117.2	
-49.6	-49.6	3)	—	—	—	97.3	—	—	—	—	—	10.4	—	86.9	97.3	
8.6	8.6	4)	—	52.5	—	2.0	—	—	54.5	—	—	—	—	—	54.5	54.5
255.6	—	5)	—	—	—	93.4	101.3	—	—	—	—	—	—	—	194.7	—
—	255.6		—	—	—	115.4	15.6	—	—	—	—	—	—	63.7	—	194.7
57.3	57.3	6)	—	—	266.4	15.1	61.2	—	210.0	—	1.0	—	13.0	1.7	266.4	266.4
197.4	197.4	7)	—	24.1	5.9	3.9	2.2	—	88.8	0.1	118.8	234.2	—	168.0	88.8	88.8
52.7	52.7	8)	—	—	—	—	—	—	—	—	250.7	277.7	—	27.0	277.7	277.7
115.7	115.7	9)	—	—	—	-208.5	77.9	—	2.3	—	-107.2	11.2	-208.5	38.2	-246.7	-246.7
2,892.8	—	c)	1,294.9	252.6	111.9	372.2	152.5	—	8.1	—	1.3	—	83.8	—	1,729.7	—
—	2,892.8		—	—	430.1	776.9	114.6	—	320.9	—	—	5.0	137.3	45.1	—	1,729.7
1,674.6	1,674.6	1)	886.0	221.6	—	1,107.6	—	—	—	—	—	—	—	—	1,107.6	1,107.6
339.5	339.5	2)	290.9	30.0	—	—	—	—	320.9	—	—	—	—	—	320.9	320.9
317.7	—	3)	—	—	—	-223.3	-152.5	—	—	—	—	—	—	—	-375.8	—
—	317.7		—	—	—	-330.7	—	—	—	—	—	—	—	45.1	—	-375.8
297.3	297.3	4)	114.9	—	—	—	114.9	—	—	—	—	—	—	—	114.9	114.9
2.9	—	5)	—	—	-111.9	249.2	—	—	—	—	—	—	83.8	—	221.1	—
—	2.9		—	—	83.8	—	—	—	—	—	—	—	137.3	—	—	221.1
260.8	—	6)	3.1	1.0	—	346.3	—	—	8.1	—	1.3	—	—	—	341.0	—
—	260.8		—	—	346.3	—	0.3	—	—	—	—	5.0	—	—	—	341.0
-278.9	-278.9	d)	3.3	—	332.0	-166.2	0.1	—	110.7	—	—	—	58.3	—	169.0	169.0
3,844.3	—	e)	—	128.1	318.7	4,000.7	3.6	—	648.5	—	41.5	483.4	1,729.3	568.5	6,785.3	—
—	3,844.3		104.0	2,427.9	—	2,212.0	83.8	2.1	-180.5	233.3	144.2	17.4	1,403.6	337.5	—	6,785.3
1,710.7	1,710.7	1)	103.8	2,376.8	—	2,694.0	—	2.9	43.0	233.3	12.3	53.5	—	—	2,694.0	2,694.0
55.7	55.7	2)	—	25.6	—	—	25.6	—	—	—	—	—	—	—	25.6	25.6
201.3	—	3)	—	—	—	77.2	18.2	—	—	—	—	—	—	—	59.0	—
—	201.3		—	—	—	18.2	77.2	—	—	—	—	—	—	—	—	59.0
317.4	317.4	4)	0.2	—	318.5	505.2	22.2	—	-207.7	—	1.4	—	—	—	318.5	318.5
1,559.2	—	5)	—	128.1	0.2	1,229.5	3.8	—	648.5	—	41.5	483.4	1,729.3	568.5	3,688.2	—
—	1,559.2		—	25.5	—	1,725.0	15.6	0.8	15.8	—	157.9	70.9	1,403.6	337.5	—	3,688.2
3,183.8	—	f)	—	80.6	57.2	419.7	1,809.0	30.0	649.9	4.3	40.0	1.5	5.5	25.3	3,120.0	—
—	3,183.8		316.4	1,413.5	—	—	300.9	0.3	99.7	642.7	27.0	10.4	364.7	1.6	—	3,120.0
301.6	301.6	1)	40.9	326.2	—	419.7	—	—	1.5	78.1	27.0	—	—	—	419.7	419.7
1,659.4	1,659.4	2)	260.0	1,163.3	—	—	1,532.0	0.3	0.2	109.7	—	1.5	—	—	1,532.0	1,532.0
265.5	—	3)	—	80.4	18.0	—	277.0	—	—	—	—	—	5.5	25.3	370.2	—
—	265.5		—	-165.6	—	—	145.7	—	22.8	3.1	—	5.7	364.7	—	—	370.2
957.3	—	4)	—	0.2	75.2	—	—	30.0	649.9	4.3	40.0	1.5	—	—	798.1	—
—	957.3		15.5	89.6	—	—	155.2	—	75.2	458.0	—	6.2	—	1.6	—	798.1
3,345.8	—	g)	1,049.2	1.0	917.0	1,136.7	54.7	33.0	40.1	—	0.9	—	0.7	—	3,151.3	—
—	3,345.8		—	494.3	—	—	1,284.2	—	1,338.8	2.2	—	221.4	-192.2	2.6	—	3,151.3
1,296.8	—	1)	159.2	1.0	1,200.0	189.3	36.4	2.9	18.3	—	3.8	—	0.7	—	1,560.2	—
—	1,296.8		—	—	—	—	—	—	1,338.8	—	—	221.4	—	—	—	1,560.2
1,188.6	—	2)	574.7	2.0	26.6	645.2	18.0	24.1	10.9	—	4.5	—	—	—	1,284.2	—
—	1,188.6		—	—	—	—	1,284.2	—	—	—	—	—	—	—	—	1,284.2
569.0	—	3)	205.5	2.0	0.9	302.2	6.4	11.8	10.9	—	1.6	—	1.4	—	499.1	—
—	569.0		—	494.3	—	—	—	—	—	2.2	—	—	—	2.6	—	499.1
291.4	291.4	4)	109.8	—	-308.7	—	6.7	—	—	—	—	—	-192.2	—	-192.2	-192.2
1,127.8	—	h)	370.0	299.8	0.2	78.8	9.1	31.3	244.8	62.3	3.5	3.0	244.3	4.5	1,324.4	—
—	1,127.8		—	835.4	—	65.5	51.6	0.3	—	—	—	—	371.6	—	—	1,324.4
1,213.6	—	i)	1,907.7	46.4	—	—	—	—	—	—	—	1.3	—	—	1,955.4	—
—	1,213.6		—	—	—	—	—	224.0	14.7	—	320.0	—	1,396.7	—	—	1,955.4
514.2	514.2	1)	511.0	33.0	—	—	—	—	224.0	—	320.0	—	—	—	544.0	544.0
699.4	699.4	2)	1,396.7	13.4	—	—	—	—	14.7	—	—	1.3	1,396.7	—	1,411.4	1,411.4
434.7	—	j)	—	—	—	—	—	—	—	—	—	—	—	150.7	150.7	—
—	434.7		—	—	130.1	-182.2	-12.5	—	—	—	—	—	204.4	10.9	—	150.7
18,922.3	—		6,542.5	2,138.8	1,536.6	5,849.7	1,948.2	86.7	1,697.0	211.0	302.7	257.4	2,076.8	-116.8	22,530.4	—
—	18,922.3		420.4	5,171.1	1,536.6	5,639.8	1,838.2	226.7	1,856.4	878.2	437.2	521.9	3,556.9	447.0	—	22,530.4
—	—		6,122.1	3,032.3	—	209.9	110.0	140.0	159.4	667.2	134.5	264.5	1,480.3	563.8	—	—

TABLE 54

CONSOLIDATED ACCOUNT OF THE LIQUIDITY-CREATING INSTITUTIONS

(changes in billions of lire)

I t e m s	1967	1968	1969	1969 by quarters			
				I	II	III	IV
ASSETS							
Foreign sector (net)	202.4	393.3	- 869.2	- 226.9	- 334.4	- 201.3	- 106.6
Economy	2,603.5	2,143.6	3,371.8	88.5	1,085.7	514.1	1,683.5
at short term	1,995.6	1,343.1	2,480.8	- 286.7	1,016.6	199.0	1,551.9
at long term	607.9	800.5	891.0	375.2	69.1	315.1	131.6
Public sector	916.2	1,808.3	1,472.4	- 185.2	200.8	832.3	624.5
Net Government indebted-							
ness (1)	- 421.0	446.6	- 110.0	- 560.0	196.7	310.8	- 57.5
others: at short term	575.6	525.9	813.6	381.8	- 158.1	139.4	450.5
at long term	761.6	835.8	768.8	- 7.0	162.2	382.1	231.5
Other sectors (2)	798.9	969.1	990.2	- 120.2	384.2	239.4	486.8
at short term	155.4	206.7	136.1	- 184.2	199.0	- 105.3	226.6
at long term	643.5	762.4	854.1	64.0	185.2	344.7	260.2
Discrepancies (3)	- 413.0	- 131.5	- 138.1	258.5	- 345.5	- 154.2	103.1
Total	4,108.0	5,182.8	4,827.1	- 185.3	990.8	1,230.3	2,791.3
LIABILITIES							
Economy	3,811.4	4,592.5	4,679.5	- 96.0	853.3	870.4	3,051.8
notes and coin (4)	328.2	359.4	694.4	- 356.9	151.4	190.7	709.2
deposits (4)	1,570.1	2,220.8	2,553.3	118.8	637.2	312.0	1,485.3
time and savings deposits . .	1,913.2	2,014.1	1,428.5	141.5	65.8	360.1	861.1
short-term securities	- 0.1	- 1.8	3.3	0.6	- 1.1	7.6	- 3.8
Public sector	274.4	307.4	8.7	123.8	- 64.2	534.8	- 585.7
notes and demand deposits . .	274.4	307.4	8.7	123.8	- 64.2	534.8	- 585.7
Other sectors (2) (3)	22.2	282.9	138.9	- 213.1	201.7	- 174.9	325.2
notes and demand deposits . .	55.8	260.5	295.3	- 214.9	87.6	14.7	407.9
other liquid assets	- 33.6	22.4	- 156.4	1.8	114.1	- 189.6	- 82.7
TOTAL LIQUIDITY:							
PRIMARY	2,228.5	3,148.1	3,551.7	- 329.2	812.0	1,052.2	2,016.7
SECONDARY	1,879.5	2,034.7	1,275.4	143.9	178.8	178.1	774.6
Total	4,108.0	5,182.8	4,827.1	- 185.3	990.8	1,230.3	2,791.3

(1) The Government's short-term requirements included in this item have been calculated by deducting from the total deficit the amount of long-term Government securities taken by subscribers other than liquidity-creating institutions.— (2) Special credit institutions and insurance companies.— (3) Includes the unclassified items.— (4) The figures have been adjusted for the incidental factors at the end of 1967.

amount approximately 74 per cent consisted of short-term borrowing from the banks, which, on the basis of seasonally adjusted figures, underwent the largest expansion in the second quarter, and then fell off in the second half of the year. The public sector's recourse to the liquidity-creating institutions decreased, mainly owing to the reversal of sign of the Government's net indebtedness (adjusted for the amount of long-term securities subscribed by the economy). On the other hand,

TABLE 55

THE ECONOMY'S FINANCIAL ASSETS AND THEIR COUNTERPARTS

(amounts and changes in billions of lire)

Description	Amount at end 1967	1967	1968	1969	1969 by quarters (1)			
					I	II	III	IV
Financial assets:								
DOMESTIC	68,839	5,747	6,744	6,621	759	1,467	1,171	3,224
Liquid assets (2)	40,356	3,811	4,593	4,679	96	853	870	3,052
Other deposits and savings certificates	1,315	185	286	119	55	36	11	17
Fixed-interest securities	9,830	1,205	1,170	940	626	358	34	78
Shares and equity participations	12,757	36	170	325	5	75	156	99
Other financial assets	4,581	510	525	558	179	145	100	134
FOREIGN	6,152	703	1,234	2,060	442	666	528	424
Short-term loans (net) and long-term loans	1,431	28	213	208	11	207	41	51
Other financial assets	4,721	675	1,021	1,852	431	459	487	475
Total (3)	74,991	6,450	7,978	8,681	1,201	2,133	1,699	3,648
Against financing of:								
ECONOMY	54,837	4,449	4,581	5,592	657	1,472	1,262	2,201
FROM DOMESTIC SOURCES	50,416	4,268	4,275	5,512	637	1,421	1,279	2,175
Short-term indebtedness	17,325	2,048	1,419	2,532	251	1,023	208	1,552
Medium and long-term indebtedness	18,456	1,970	2,326	2,388	693	301	908	486
Shares and equity participations	14,635	250	530	592	195	97	163	137
FROM FOREIGN SOURCES	4,421	181	306	80	20	51	17	26
Medium and long-term indebtedness	1,029	32	70	164	35	60	26	43
Shares and equity participations	3,392	213	236	244	55	111	9	69
FOREIGN SECTOR (4)	5,508	999	1,642	1,480	322	456	612	90
PUBLIC SECTOR (consolidated)	16,371	1,464	2,168	1,841	140	467	316	978
UNCLASSIFIED (5)	-1,725	-462	-413	-232	82	-262	-491	379
Total	74,991	6,450	7,978	8,681	1,201	2,133	1,699	3,648
Economy's finan. surplus or deficit:								
at short term (6)	24,346	1,948	3,460	2,266	210	134	673	1,517
at long term	-4,192	53	63	823	334	795	-236	70
Net surplus (7)	20,154	2,001	3,397	3,089	544	661	437	1,447

(1) Figures partly estimated.— (2) The figures have been adjusted for the incidental factors at the end of 1967.— (3) The economy's gross financial saving.— (4) Current surplus or deficit of the balance of payments on a transaction basis.— (5) Including discrepancies.— (6) Excluding net short-term foreign commercial credit.— (7) The quarterly figures of the economy's net financial surplus in 1968 were: 456 625 566 1,750

there was an increase in 1969 in the liquid assets created as the counterpart of the indebtedness of the other components of the sector; in particular, short-term indebtedness was almost doubled, increasing fastest in

the fourth quarter, while recourse to the capital market became more difficult. The foreign sector, on the other hand, absorbed liquidity, confirming the inverse correlation between the trend of the balance of payments and the development of the economy's demand for short-term credit. Lendings by the liquidity-creating institutions to the « other sectors » were mainly the result of loans granted by the banks to the special institutions. This is a financial circuit which in the past has made possible considerable expansion of the capital market and has enabled the inadequacy of enterprises' self-financing to be compensated by means of medium and long-term loans from the special institutions, over against the formation of monetary and quasi-monetary holdings. Whereas in the first half of 1969, and particularly in the first quarter, the favourable trend of the capital market enabled the special institutions to obtain funds by placing securities with households, in the second half of the year the banks played an important part in the provision of funds to these institutions, both by subscribing fixed-interest securities and, as occurred in the last quarter, by granting short-term inter-bank loans.

In 1969 the increase in notes and coin was very large (13.3 per cent); the rate of expansion is reduced if account is taken of the economy's average holding of notes and coin (10.9 per cent). The movement of the currency circulation during the year was affected most of all by the greater percentage increase in money incomes and, in particular, in view of the greater cash preference of rural holders, by the increase in marketable agricultural production at current prices. Another significant factor is the marked acceleration in August, in which month the pension increase began to be paid out. The rise in bank interest rates does not appear to have contributed during the year to shifting any substantial amount of notes into bank accounts as would be indicated by the trend of savings deposits, statistical evidence concerning which suggests a considerable degree of substitutability. The calculated changes between end-of-period figures appear to be increased by incidental factors, such as the delay of a few days in the payment of December salaries and pensions by the Treasury, which moved on to January part of the receipts of bank-notes which usually occur at the end of the year. Subsequently, in the period January-April 1970, there was a further vigorous expansion in notes and coin, due to the rise in the total of wage and salary incomes.

At the end of 1969 liquid assets of the economy consisted, to the extent of more than one-third, of bank current accounts, which represented 37 per cent of the amount of these assets. Bank current accounts thus continued to increase their relative importance, in accordance with the trend which has been observable for some years. The ratio between the change in sight deposits and the growth in income fell, however, to 59 per cent (against 67 per cent in 1968) and there were marked fluctuations in their expansion during 1969. The increase in these deposits was encouraged in the first half of the year by shifts into this investment category of funds more akin to savings deposits, owing to the interest rate policy pursued by the banks, tax reasons and probably also the higher growth rate of consumption. In the first two quarters of 1969 these factors counterbalanced the public's growing propensity to acquire foreign financial assets and the increased use of reserve monetary holdings by enterprises, due to the expansion in productive activity. In the third quarter the decline in sight deposits, which are more sensitive to cyclical variations, was probably attributable to the changes in monetary policy; towards the end of that quarter there was a renewed quickening of the rate of increase of sight deposits, stimulated by the increase in preference for liquidity as distinct from investment in fixed-interest securities, and to the slowing down of productive activity.

The expansion in total bank deposits, despite the favourable trend of current accounts, was smaller in 1969 than in the previous year owing to the movement of savings deposits which, at the end of 1969, represented 37.4 per cent of the amount of liquid assets, and which contributed less than one-quarter to liquidity formation in that year.

Postal savings deposits, in turn, continued to lose ground in relation to bank deposits, both in continuation of the general trend of the financial markets and owing to the difference in rates of yield created in 1969 in favour of bank deposits. Postal deposits represented 11.1 per cent of total liquid assets at the end of 1969 and their contribution to the formation of new liquidity declined to 6.9 per cent.

The ratio between the formation of new domestic financial assets and the increase in the monetary base works out, for 1969, at about 5.3 against 5.4 in 1968 and 4.7 in 1967; for bank deposits alone the figure is 2.9, 3.1 and 2.5 respectively. These ratios, which represent the

ex-post multiplier in relation to the monetary base, confirm its limited range of short-term fluctuation, assuming unchanged reserve conditions. The slight decline which took place in 1969 in comparison with 1968 is explained not only by the larger proportion of currency held by the public but also by the shifting of available funds from savings deposits to current accounts, which require a larger volume of monetary base.

The increased external financing requirements of enterprises was the largest counterpart item to the formation of the economy's total financial assets (64 per cent); the foreign sector's contribution decreased (17 per cent) and the part played by the public sector deficit was also reduced.

The economy's net short-term financial balance (excluding commercial claims on the foreign sector), which can be regarded to some extent as an indicator of the funds available for spending by the private sector, showed an increase of 2,270 billion lire (compared with 3,460 billion in the previous year). Particularly characteristic of the cyclical movement is the liquidity surplus of the enterprise sector; this decreased by 720 billion lire, in contrast to the increase of 440 billion in 1968.

Total lendings to the economy.— The total flow of credit obtained by the economy in 1969 was 5,590 billion lire, representing 10.9 per cent of the gross national product, against 9.7 per cent in the previous year (Table 55).

The trend was determined by the expansion of short-term indebtedness, the growth rate of which rose to 14.6 per cent (against 8.9 per cent in 1968), confirming the tendency for its relative importance to increase during phases of reviving investment activity. The growth rate of medium and long-term indebtedness, on the other hand, was lower than in 1968 (12.9 per cent against 14.4), primarily owing to the decline in loans granted by the special credit institutions. The divergence in the trend of the two forms of financing was accentuated in the last quarter, partly owing to the smaller supply of funds from the economy to the special institutions.

As regards the classification of financing by branches of economic activity, it is found that industry (excluding building) almost doubled its short-term borrowing from the banking system (1,120 billion lire against 570 billion in 1968), while it obtained medium and long-term funds totalling 1,470 billion (against 1,310 billion in the previous year). Consequently, the proportion of short-term loans to total ex-

ternal financing received rose from 30.3 to 43.3 per cent. There was also an increase in the ratio of industry's short-term borrowings to the gross product at factor cost.

The rise in total borrowing by the building industry was fairly large in 1969, although smaller than in the preceding year (16.8 and 18.4 per cent respectively). The percentage of this financing provided by the special credit institutions fell from 66 to 62 per cent.

Households' financial savings.— As already mentioned, the increase in households' propensity to save in 1969 was mainly reflected in the formation of larger financial assets; these were formed to the extent of 6,540 billion lire, representing an increase of 13.8 per cent in comparison with previous year (Table 56).

ANALYSIS OF HOUSEHOLDS' FINANCIAL SAVING

TABLE 56

Items	Amounts (1) at end of		Flows (1)			
	1965	1969	1966	1967	1968	1969
<i>(billions of lire)</i>						
Notes and coin (2)	3,118	4,710	341	298	319	634
Bank deposits (2)	10,117	17,956	1,605	1,777	2,288	2,169
Postal deposits	3,360	4,625	348	317	309	291
Other deposits and savings certificates .	686	1,433	158	190	278	121
Fixed-interest securities	5,600	10,461	1,202	1,164	1,153	939
Shares and equity participations (3) . .	5,956	6,406	50	20	40	160
Actuarial reserves	2,864	4,746	431	461	479	511
Foreign assets	2,397	5,819	431	607	884	1,717
Total . . .	34,098	56,156	4,566	4,834	5,750	6,542
<i>(percentage breakdown)</i>						
Notes and coin	9.1	8.4	7.5	6.2	5.5	9.7
Bank deposits	29.7	32.0	35.2	36.8	39.8	33.2
Postal deposits	9.9	8.2	7.6	6.6	5.4	4.4
Other deposits and savings certificates .	2.0	2.6	3.5	3.9	4.8	1.9
Fixed-interest securities	16.4	18.6	26.3	24.1	20.1	14.4
Shares and equity participations	17.5	11.4	1.1	0.4	0.7	2.4
Actuarial reserves	8.4	8.4	9.4	9.5	8.3	7.8
Foreign assets	7.0	10.4	9.4	12.5	15.4	26.2
Total . . .	100.0	100.0	100.0	100.0	100.0	100.0

(1) Figures partly estimated.— (2) For 1967 and 1968 the flows have been adjusted for the incidental factors at the end of 1967.— (3) Shares and equity participations are valued at market prices, the par value of the amounts held being multiplied by the ratio between stock exchange value and par values at the end of 1969. The market value of shares held by households at the end of 1965, as obtained by applying the calculated index to 1965 prices, was 5,600 billion lire.

The year 1969 saw the continuance, under the influence of the trend which have characterised the domestic and international financial markets, of the tendency of households to change the pattern of their preferences as regards the structure of their financial assets. The most important phenomenon, from many points of view, was the increase in the proportion of financial savings employed in assets abroad, owing to the higher rates of yield obtainable, the political and social uncertainties and the people's desire to diversify the assets held as regards both the debtors and the types of security, which was thwarted by the lack of suitable financial instruments on the Italian markets. Whereas between end-1965 and end-1968 the average yearly growth rate of households' financial investments abroad was 21.4 per cent (as against an average growth rate of 13.7 per cent for all financial assets), it reached 40 per cent in 1969.

The expansion in financial assets abroad, in which 26 per cent of gross financial savings were invested in 1969 (against 15 per cent in 1968), was in contrast to the reduction in the proportion represented by bank deposits. For households, although they played a larger part than enterprises in the expansion of the systems' liquid assets, accumulated only 2,580 billion lire in the various forms of deposits and interest-bearing certificates (as against 2,870 billion in 1968), thus reducing their contribution to the sector's gross financial saving to 39.5 per cent. The average growth rate of households' liquid assets, which was 13.4 per cent between end-1965 and end-1968, thus declined to 12.8 per cent in 1969. This took place despite the fact that in the last months of 1969, owing to the instability of the prices of fixed-interest securities and the rise in bank deposit rates, households increased their liquidity preference.

The process of substitution also affected fixed-interest securities. Households in fact subscribed an amount of fixed-interest securities which was below the average for the previous three-year period, thereby reducing to 14.4 per cent the proportion of financial savings allocated to investment in bonds.

There were marked variations in this movement during the year. Whereas in the first half of 1969 the proportion subscribed by households was 65 per cent of issues, which is even higher than in the corresponding period of 1968 (47 per cent), in the second half of the year it fell to almost nil, so that at the end of 1969 it was down to 28 per cent of the total (against 37 per cent in 1968).

To some extent the inclusion of smaller amounts of fixed-interest securities in households' holdings was compensated by larger purchases of shares, encouraged by the expectations of rising prices and also by the support given by authorised foreign investment funds. Thus in the domestic market households confirmed their greater inclination towards equity investment, on top of the increased propensity indirectly shown via the foreign sector. This change in preferences may benefit the process of investment financing when the financial instruments now being discussed in Parliament become available.

Whereas, on the one hand, the institutional limitations and the requirements of the sectors which issue financial instruments have had a restrictive effect on households' financial investments, on the other hand, the changes which occurred in 1969 in the pattern of distribution of the sector's financial savings in turn affected the supply of funds to the financial intermediaries and the forms of indebtedness of the ultimate users of savings.

In 1969 the large proportion of savings channelled abroad reduced the funds received by banks, which obtained 33 per cent of households' savings (against 37 per cent between end-1965 and end-1968), and those going to the special institutions, which obtained 10 per cent of savings (whereas the proportion was still as high as 15 per cent between end-1965 and end-1968). This created tensions, especially in the liquidity situation of the banks, which also finally had to bear the burden of the special institutions' requirements.

The proportion of households' savings received by the Treasury, in its function as a financial intermediary, is less stable since it depends not only on the preferences of the household sector but also on the placing of Government securities, which is decided on the basis of the public authorities' requirements and the aims of monetary policy. On an average for the period 1966-1968, the proportion of households' savings received by the Treasury, including via the Post Office Savings Departments, was 16 per cent; in 1969 the proportion was down to 7 per cent.

Direct financing to enterprises, however, although remaining at modest levels, showed an increase, especially that in the form of subscription of shares (160 billion lire), which represented 2.4 per cent of households' financial savings (a larger proportion than the average for 1966-1969).

Forms of enterprises' external financing.— In the period 1959-1969, chosen as the standard of reference, the loans received by enterprises directly from the economy and from the foreign sector represented on average a fairly small proportion of external financing (18.2 per cent). The trend, moreover, was clearly downwards: between 1959 and 1962 direct lendings represented 21.4 per cent, and between 1963 and 1969 the percentage was reduced to 16.9 per cent. Excluding the foreign sector, direct financing declines, between the two parts of the period, from 9.3 to 8.2 per cent.

This development is the cause of the high growth rate of enterprises' short-term indebtedness in recent years (15.1 per cent in 1969), and helps to explain the recourse which that sector had, for fixed-maturity medium and long-term financing, to borrowing from the special institutions, particularly in cases where this financing was obtainable on preferential terms.

Excluding endowment funds, it appears that in recent years enterprises' risk capital has increased only to a modest extent, while the rise in direct bond indebtedness is entirely attributable to public enterprises (Table 57). In 1969 the financial structure of these enterprises

ANALYSIS OF ENTERPRISES' EXTERNAL FINANCING

TABLE 57

Items	Amounts at end of		Flows			
	1965	1969	1966	1967	1968	1969
<i>(billions of lire)</i>						
Short-term loans	11,330	18,524	1,594	1,928	1,244	2,428
Medium and long-term loans	8,322	13,647	928	1,210	1,521	1,413
Bonds	3,351	5,187	317	403	516	494
Shares and equity participations (1) . . .	16,923	20,077	437	324	481	621
Endowment funds provided by the public sector	1,007	1,739	93	140	284	215
Total . . .	40,933	59,174	3,369	4,005	4,046	5,171
<i>(percentage breakdown)</i>						
Short-term loans	27.7	31.3	47.3	48.1	30.7	47.0
Medium and long-term loans	20.3	23.1	27.5	30.2	37.6	27.3
Bonds	8.2	8.8	9.4	10.1	12.8	9.6
Shares and equity participations (1) . . .	41.3	33.9	13.0	8.1	11.9	12.0
Endowment funds provided by the public sector	2.5	2.9	2.8	3.5	7.0	4.1
Total . . .	100.0	100.0	100.0	100.0	100.0	100.0

(1) Shares and equity participations are valued at market prices, the par value of the amounts held being multiplied by the ratio between stock exchange value and par values at the end of 1969.

INVESTMENTS AND THEIR COVERAGE
(changes in billions of lire)

TABLE 58

Items	Public sector (consolidated)	Government equity participations and ENEL	Other enterprises and housing	House holds	Credit institutions (consolidated)	Total	Foreign sector (2)
1968 (1)							
Gross fixed capital formation	1,408	1,230	6,365	—	162	9,165	—
Ditto, excluding housing			3,721				
Net increase in inventories . . . . .	....	71	119	—	—	190	—
Transfers in capital account	653	- 15	- 598	- 11	—	29	- 29
Gross saving	54	496	4,466	5,625	376	11,017	-1,662
Capacity (+) or need of (-) financing	-2,007	- 790	-1,420	5,636	214	1,633	-1,633
Financial assets (3)	954	87	2,028	5,803	6,359	15,231	870
Liquid assets	114	7	1,670	2,915	41	4,747	- 17
Fixed-interest securities	- 10	....	17	1,300	1,557	2,864	4
Other assets (net)	385	39	115	1,503	4,726	6,768	647
Shares and equity participations	465	41	226	85	35	852	236
External financing (4)	3,122	877	3,469	175	6,196	13,839	2,512
Short-term loans	1,069	- 8	1,252	175	4,910	7,398	1,180
Long-term loans	2,053	601	1,735	—	1,180	5,569	1,124
by: banking system (5)	1,199	245	236	—	—	1,680	187
other credit institutions	311	194	1,271	—	—	1,776	111
public sector	—	- 18	120	—	273	375	—
economy and foreign sector (6)	543	180	108	—	907	1,738	826
Shares and equity participations	—	284	482	—	106	872	208
Net financial investments	-2,168	- 790	-1,441	5,628	163	1,392	-1,642
Adjustments	161	—	21	8	51	241	9
1969 (1)							
Gross fixed capital formation	1,368	1,423	7,582	—	170	10,543	—
Ditto, excluding housing			4,134				
Net increase in inventories . . . . .	....	41	149	—	—	190	—
Transfers in capital account	847	- 39	- 749	- 13	—	46	- 46
Gross saving	- 212	590	4,716	6,702	445	12,241	-1,508
Capacity (+) or need of (-) financing	-2,427	- 835	-2,266	6,715	275	1,462	-1,462
Financial assets (3)	924	187	1,828	6,635	7,873	17,447	2,077
Liquid assets	318	119	1,463	3,098	244	5,242	97
Fixed-interest securities	- 19	7	- 6	1,049	1,428	2,459	1
Other assets (net)	311	48	84	2,118	6,161	8,722	1,735
Shares and equity participations	314	13	287	370	40	1,024	244
External financing (4)	2,765	1,022	4,434	104	7,693	16,018	3,557
Short-term loans	559	136	2,292	104	6,540	9,631	1,641
Long-term loans	2,206	695	1,498	—	1,096	5,495	1,544
by: banking system (5)	1,523	295	364	—	—	2,182	- 327
other credit institutions	166	145	1,289	—	—	1,600	284
public sector	—	- 18	108	—	149	239	—
economy and foreign sector (6)	517	273	- 263	—	947	1,474	1,587
Shares and equity participations	—	191	644	—	57	892	372
Net financial investments	-1,841	- 835	-2,606	6,531	180	1,429	-1,480
Adjustments	- 586	—	340	184	95	33	18

(1) The changes in liquid assets for 1968 have been adjusted for the incidental factors at the end of 1967; the figures for 1969 are provisional.— (2) The foreign sector's financing requirements do not exactly tally with the balance of payments on a transaction basis, expressed by net financial investments.— (3) The financial assets of the Government equity participations, Enel and other enterprises correspond to the total assets of the enterprise sector of the financial accounts less the compensation payments made by Enel under Law N. 1,643 of 6 December 1962.— (4) The external financing of « other enterprises » corresponds to the enterprise sector's total liabilities, less the public enterprises' borrowing and plus an estimated amount for loans obtained for households' investments in housing.— (5) Includes the BI-IEO'S subscriptions of long-term securities.— (6) In the case of public enterprises, funds originating from forms of self-financing such as retirement funds are also included.

benefited by the increase in endowment funds, which, together with equity issues, represented 18.7 per cent of their external financing (191 billion lire); these enterprises also obtained 54.1 per cent of their external funds by direct bond issues, more than half of which were subscribed by the banking system. The remainder of their financing requirements were covered by medium and long-term borrowing from the special institutions (12.7 per cent of external funds) and by financing received from abroad (1.5 per cent) (Table 58).

The main form of financing of « other enterprises » in 1969, on the other hand was short-term borrowing from the banking system (54.0 per cent in 1969), representing a larger proportion than in the previous years. The loans obtained by « other enterprises » from the special institutions, though they were still the most important form of cover for their medium and long-term requirements in the absence of an adequate supply of risk capital, fell to 24.9 per cent of their external funds (against 31.1 per cent in 1968). There was on the other hand an increase in the relative importance of medium and long-term loans granted by the banking system (7.9 per cent of external funds).

The « other enterprises » obtained funds by equity issues representing 15.5 per cent of their total external financing, which was above the average percentage for the preceding years, so that in 1969, taking advantage of the more favourable conditions of the market for variable yield securities, the « other enterprises » improved the composition of the external financial contribution to their financing by increasing, although to a modest extent, the proportion of risk capital.

Financing of investment.— In 1969 the public sector's share in the formation of the country's capital assets by means of direct investments fell to 12.7 per cent (against 15.1 per cent in 1968). The public sector's gross requirements were also increased by the acquisition of financial assets. The public sector thus had to resort to the savings of other sectors for a gross amount of 2,770 billion lire (against 3,120 billion in 1968) and, net of financial assets, of 1,840 billion (against 2,170 billion in 1968). Notwithstanding the reduction in its net requirements, the public sector resorted to the Bank of Italy for 1,100 billion lire (as compared with 500 billion in 1968); this recourse was mainly concentrated in the last two quarters of 1969. On the other

hand, the sector was able to place with the banks only 200 billion lire of long-term securities (against 860 billion in 1968) and repaid to the banks 150 billions' worth of short-term securities.

For 1969 the marked discrepancy between the public sector's financing requirements and net financial investment is attributable to the revision of the Government budget figures for the purposes of the national accounts; readers are referred in this connection to the chapter on Public Finance.

In 1969 gross fixed capital formation by public enterprises increased at the rate of 15.7 per cent, which was higher than in 1968; the rise was due, in particular, to capital investment in the engineering industry in Southern Italy and to greater investment by the iron and steel industry and the chemical and telephone industries. In the same year, however, the increase in inventories was almost halved compared with 1968, so that the total investments of the group increased by 12.5 per cent, keeping the participation of public enterprises in total capital formation almost unchanged. The gross internal savings of enterprises, consisting mainly of depreciation, increased by 19 per cent and made possible, despite the high rate of growth in capital investment, a rise to 40.3 per cent (from 38.1 in 1968) in the self-financing ratio.

In 1969 the growth rate of fixed capital formation by « other enterprises » at current prices was 11.1 per cent, which figure rises to 19.1 per cent if dwellings are included.

The « other enterprises » also include investments in dwellings by households, owing to the lack of reliable statistics on these. From the total liabilities of households there has been deducted an estimated amount in respect of loans obtained for investment in dwellings, and this has been added to the figure for the external financing of « other enterprises », shown in Table 58.

The gross savings of « other enterprises » increased in 1969 by 5.6 per cent and the self-financing ratio, in relation to the sector's total capital formation, fell to 61 per cent from 68.9 per cent: correspondingly, net recourse to the market rose to 2,610 billion lire, compared with 1,440 in 1968. The greater recourse to external financing was due to the higher growth rate of investments, which, as already pointed out, was mainly reflected in increased short-term indebtedness, while the financing obtained from the special credit institutions was reduced.

The ratio between the flow of the own funds and total investments of « other enterprises » was also lower in 1969 than in 1968 (69.3 per cent against 76.3 per cent), despite the increased placing of share issues.

In 1969 households were again the only sector, if the modest results of the credit institutions are disregarded, to achieve a financial advance: the total resources which households made available to other sectors, as already noted, were of the order of 6,120 billion (against 4,990 billion in 1968) if the total of loans for purchases of dwellings is included in the indebtedness (Tables 53 and 58).

The unchanged excess of savings over net financial investments of households suggests that, in 1969, the total of direct investments made by « households », mainly in dwellings, ought not to have been significantly higher than in 1968, at least for the part not financed by enterprises. While households did not devote a larger amount of savings to the purchase of dwellings, the sector nevertheless switched part of its resources from internal financing by channelling them, as already noted, towards the purchase of foreign assets.

The pronounced and growing divergence between sectors which generate savings and sectors which carry out investments and the limited amount of funds directly raised by enterprises made necessary greater intervention by the credit institutions in 1969. These granted loans to the economy and the public sector totalling 6,430 billion lire (compared with 5,530 billion in 1968), representing 77 per cent of the financing obtained by these sectors (72 per cent in 1968). The credit institutions also granted credits abroad for 1,240 billion lire (against 1,030 billion in 1968), but they raised 1,970 billion lire (against 520 billion in 1968) from the foreign sector and thus counterbalanced, at least in part, the outflow of resources to foreign countries from the economy. In particular, in 1969 the divergence between the forms of lending to which financial savings were originally applied and the pattern of demand for funds resulted, for an amount of about 3,380 billion lire (including the 420 billion transferred by the Central Post Office Savings Fund), in short-term liquid assets being transformed into long-term credit instruments suitable for financing domestic investment (Table 59).

CREDIT INSTITUTIONS' CONSOLIDATED ACCOUNT
(changes in billions of lire)

TABLE 59

Items	1967			1968			1969		
	Assets	Liabilities	Balance	Assets	Liabilities	Balance	Assets	Liabilities	Balance
<i>Short term</i>									
Gold	- 8.8	—	- 8.8	327.1	—	327.1	20.5	—	20.5
Notes and coin (1)	0.4	322.3	- 321.9	- 8.5	344.4	- 352.9	- 2.5	695.6	- 698.1
Demand deposits (1)	201.8	1,727.6	- 1,525.8	- 9.2	2,231.2	- 2,240.4	- 77.3	2,880.1	- 2,957.4
Other deposits	171.4	1,724.6	- 1,553.2	8.3	1,968.5	- 1,960.2	137.3	1,306.0	- 1,168.7
Securities: domestic	0.1	—	0.1	176.6	—	176.6	107.4	—	107.4
foreign	38.5	—	38.5	- 453.7	—	- 453.7	58.3	—	58.3
<i>Loans</i>									
to central authorities	- 372.3	—	- 372.3	209.8	—	209.8	- 180.5	—	- 180.5
other domestic	2,203.7	1.9	2,201.8	1,695.1	18.1	1,677.0	2,672.5	- 0.8	2,673.3
foreign	410.8	302.7	108.1	695.6	547.2	148.4	1,275.5	1,729.3	- 453.8
Total: domestic	2,115.4	3,776.2	- 1,660.8	1,904.5	4,579.2	- 2,674.7	2,727.6	4,784.1	- 2,056.5
foreign	530.2	302.9	227.3	736.6	530.2	206.4	1,283.6	1,826.1	- 542.5
<i>Long term</i>									
Loans: domestic	1,787.6	116.3	1,671.3	2,049.2	267.9	1,781.3	2,056.6	155.2	1,901.4
foreign	109.8	- 6.3	116.1	152.8	- 7.6	160.4	259.0	145.7	113.3
Bonds	713.2	466.2	247.0	1,557.4	690.0	867.4	1,427.5	570.3	857.2
Shares and equity participations	98.1	65.4	32.7	35.4	106.4	- 71.0	40.4	56.6	- 16.2
Other assets and liabilities	6.0	512.2	- 506.2	- 76.6	30.1	- 106.7	77.9	154.7	- 76.8
Total: domestic	2,624.5	1,160.1	1,464.4	3,421.0	1,094.0	2,327.0	3,904.3	936.3	2,968.0
foreign	90.2	- 6.3	96.5	297.2	- 7.2	304.4	- 42.9	146.2	- 189.1
TOTAL	5,360.3	5,232.9	127.4	6,359.3	6,196.2	163.1	7,872.6	7,692.7	179.9

(1) For 1967 and 1968 the figures have been adjusted for the incidental factors at the end of 1967.

**CAPITAL FORMATION, AND ITS FINANCING, IN A GROUP COMPRISING
138 ITALIAN MANUFACTURING COMPANIES (a)**
(billions of lire)

TABLE 60

Year	Fixed capital formation (b)	Increase or decrease of inventories	Capital formation (b)		Self-financing (c)				External sources of financing			Total financing	Difference between financing and gross capital formation	Movement of net bank indebtedness
			gross	net	gross		net		medium and long-term borrowing	bonds	payments by shareholders			
					billions	per cent	billions	per cent						
(1)	(2)	(3)=(1)+(2)	(4)	(5)	(6)=(5) : (3)	(7)	(8)=(7) : (4)	(9)	(10)	(11)	(12)=(5)+(9)+(10)+(11)	(13)=(12) (3)	(14)	
1963 . .	783.5	101.4	884.9	623.0	295.5	33.4	33.6	5.4	205.6	- 19.3	38.7	520.5	- 364.4	313.1
1964 . .	675.3	67.7	743.0	473.4	329.5	44.3	59.8	12.6	289.1	39.5	108.1	766.2	23.2	3.7
1965 . .	434.8	51.5	486.3	204.7	365.6	75.2	84.0	41.0	147.2	22.9	11.6	547.3	61.0	74.1
1966 . .	402.4	67.9	470.3	141.5	388.8	82.7	60.1	42.5	112.6	- 18.6	57.1	539.9	69.6	51.2
1967 . .	445.0	117.7	562.7	235.0	394.2	70.1	66.6	28.3	46.8	- 17.6	26.5	449.9	- 112.8	86.7
1968 . .	442.8	13.1	429.7	58.6	463.6	107.9	92.6	158.0	92.7	- 7.2	10.8	559.9	130.2	- 87.3
1969 . .	548.6	54.7	603.3	192.8	479.5	79.5	69.0	35.8	112.1	- 27.7	42.1	606.0	2.7	- 51.8

(a) The figures cover 19 fewer companies than last year; however, some companies not included last year have now been included.— (b) Disinvestments have been estimated, for the companies which do not state their amount, on the basis of the amounts written back from depreciation funds.— (c) Self-financing takes account of changes in retirement funds and in the sums realised on disposal of assets.

The financing of capital expenditure in manufacturing industry according to companies' balance sheets.— The revival of investments, forecast last year on the basis of the business results of a group of 157 companies in the 1968 trading year, was reflected in the results of the usual investigation based on the balance sheets of manufacturing companies (Table 60).

This year the investigation covers a group of 138 companies; the difference in the range of the sample in the various years depends on the promptness with which the balance sheets become available so that the data can be statistically processed and published in the Report.

In 1963, the first year of the period studied, the sample covers 260 companies, and this number was reduced over the seven years to 138. This sharp contraction, which occurred mainly from 1965 onwards, bears witness to the extent of the process of concentration, impelled by the need for functional (including financial) improvements, and stimulated by tax reliefs; all reasons which have chiefly affected the large companies.

The figures for the group of companies considered show an increase of 23.9 per cent in fixed capital formation in 1969, which is larger than that recorded by industry as a whole (14.8 per cent according to national account). The greater increase is due to the preponderance in the sample considered here of companies in which there is Government participation and large private companies (with net capital of at least 20 billion lire), which categories show, as a whole, an increase in gross fixed capital formation of 24.9 per cent.

The change in inventories, which in 1968 was negative (— 13.1 billion lire), amounted in 1969 to 54.7 billion. The increase relates almost entirely to the engineering industry (45.7 billion) and is probably due to the interruptions in productive activity in the autumn, which led to the accumulation of semi-processed products, and to the stiffening of prices of raw materials on the international markets, which stimulated the formation of due to cyclical reasons and influenced the valuation of the remainder.

In view of the particularly sharp rise in inventories, gross capital formation increased even more (40.4 per cent) than fixed capital, while net capital formation, which more than trebled, demonstrates the efforts made by companies to increase their productive capacity to meet the prospective growth in demand.

Compared with the substantial expansion in capital formation, the increase in gross self-financing was much more limited (3.4 per cent), so that the ratio between the two was considerably reduced (79.5 against 107.9 per cent in the previous year).

Gross self-financing also includes, in addition to depreciation and undistributed profits, changes in dividends which, until they are paid, constitute an internal financial source of the company concerned.

Recourse to medium and long-term external funds, as it exceeded the difference between gross capital formation and gross saving, made possible, not only the repurchase of a small quantity of securities and a greater deferment of payment of other current debts, but also a reduction in net indebtedness to the banking system.

Among the individual sources of external financing, mention may be made of the sharper reduction in bonded debt, following a trend which has now continued for four years, and a revival in the intake of risk capital, which rose from 10.8 billion lire to 42.1 billion. The switch between the two forms of financing is due to the revival, particularly following the good profits in 1968, of interest by savers in equity investment, which corresponded with a preference on the part of companies for financing the expansion of productive capacity by means which would not reduce their liquidity and would not further increase the rigidity of their profit and loss accounts.

The movement of financial and real flows described was reflected in the capital structure of the companies considered (Table 61). The proportion of indebtedness was reduced from 39.1 to 38.5 per cent of liabilities, continuing the trend of the previous year, and at the same time its structure was improved by an increase in the relative importance of medium and long-term debts compared with short-term debts.

The economic results for the last year were affected by the production losses in the autumn (Table 62). Gross profits—calculated excluding increases in retirement funds and the revaluation of assets which were already the source of hidden reserves—were reduced by 1.4 per cent and net profits by 28.2 per cent. The larger fall in net profits is at least partly due to the higher rates of depreciation, which raised the proportion, in relation to fixed capital, from 5.75 per cent in 1968 to 5.91 per cent in 1969. If changes in retirement funds

TABLE 61

**STRUCTURE OF THE BALANCE SHEETS
OF A GROUP OF 138 ITALIAN MANUFACTURING COMPANIES**

Items	1967		1968		1969	
	billions of lire	per cent	billions of lire	per cent	billions of lire	per cent
ASSETS						
Land buildings and plant . .	6,081.1	57.1	6,449.5	58.2	6,947.5	59.1
Inventories	1,211.0	11.4	1,198.0	10.8	1,252.6	10.7
Shares and securities	1,401.9	13.2	1,444.9	13.0	1,505.6	12.8
Receivables	1,759.6	16.5	1,778.5	16.0	1,821.6	15.5
Cash and banks	188.5	1.8	218.3	2.0	222.7	1.9
Total assets . . .	10,642.1	100.0	11,089.2	100.0	11,750.0	100.0
LIABILITIES						
Share capital	1,878.4	17.7	1,888.1	17.0	1,921.1	16.4
Reserves	941.1	8.9	956.1	8.6	975.6	8.3
Depreciation funds	2,886.3	27.1	3,196.7	28.8	3,558.9	30.3
Retirement funds	523.4	4.9	567.4	5.1	649.8	5.5
Medium and long-term debts	1,887.8	17.7	1,973.2	17.8	2,057.8	17.5
of which: bonds	482.2	4.5	474.9	4.3	447.3	3.8
Payables	1,553.4	14.6	1,570.3	14.2	1,723.8	14.7
Banks	844.5	7.9	789.4	7.1	740.9	6.3
Net profit	127.2	1.2	148.0	1.4	122.1	1.0
Total liabilities . . .	10,642.1	100.0	11,089.2	100.0	11,750.0	100.0

(which are in fact freely available to the enterprises and not subject to interest) are included in the results, gross profits are increased by 5.3 per cent and net profits reduced by 4.0 per cent.

The reduction in profits was more marked in the engineering industry, in which there were decreases of 9.6 and 61.0 per cent in gross profits and net profits respectively; if the increases in retirement funds are included, these changes become a rise of 2.2 per cent and a decline of 15.3 per cent respectively.

The distribution of profits shows a smaller fall (6.8 per cent) in dividends than in net profits; however, the considerable recourse to advance depreciation seems to indicate that a considerable number of companies have decided to put reasons of internal saving before remuneration of capital. This is a policy which obviously can be adopted only for a short period; otherwise savers will lose interest in equity investment.

A comparison of the results achieved by the major Italian companies (the group of 138) with those of the most important companies in France, Germany, Netherlands, Belgium and Luxembourg shows that, in the period 1965-68, Italian companies reached a level of self-financing (83 per cent) not far short of that of all the other companies of the European Community (93 per cent). It must, however, be borne in mind that this is partly due to lower investments.

TABLE 62

**GROSS AND NET PROFITS IN A GROUP
OF 138 ITALIAN MANUFACTURING COMPANIES**
(billions of lire)

Year	Net profits and increases in capital and reserves (a)	Depreciation	Increase in retirement funds	Adjusted profits (b)	
				gross	net
				(4)=(1)+(2)+(3)	(5)=(4)-(2)
1963	89.0	261.9	59.8	410.7	148.8
1964	102.3	269.6	42.7	414.6	145.0
1965	131.4	281.6	49.1	462.1	180.5
1966	127.9	328.8	44.9	501.6	172.8
1967	135.0	327.5	42.8	505.3	177.8
1968	166.7	371.1	43.9	581.7	210.6
1969	119.7	410.6	82.5	612.8	202.2

(a) Net profits plus increase and reserves, less losses and calls upon shareholders.— (b) Gross profits correspond to gross self-financing, plus dividends paid in the year (but relating to the previous year) and less the difference between the accounting value of assets sold or demolished and the corresponding amounts written back from depreciation funds.

Substantial differences remain in the composition of external funds, of which payments by shareholders represent about a quarter in the Italian companies and almost half in the other companies of the European Community.

III. – Excerpts from the Governor's Concluding Remarks

The spread of inflation, international liquidity and the foreign exchange system

The outstanding features of economic developments in the main industrial countries in 1969 can be identified in the spread of inflationary pressures, the preponderant recourse to monetary policy and the resultant rise in interest rates, and the intensification of transfers of short-term funds. At the centre of the picture is the decision of the United States authorities to regulate overall demand by the adjustment of the money supply, a step dictated by the need to exert a more direct influence on the level of demand.

According to the Federal Reserve and the President's economic advisers, the price increases in the United States, their spread to other countries and the deterioration of the current account of the balance of payments are supposed to be manifestations of a process of inflation fostered by a large Government budget deficit in a situation close to full employment of the economy's resources. The rise in interest rates, they contend, is due to a large expansion in the demand for funds not matched by an adequate growth in supply, owing to a tendentially restrictive monetary policy.

This interpretation is opposed by another according to which both these phenomena are due to a monetary policy which is in fact expansionary. The cause of the inflationary tensions lies, according to this interpretation, not in public expenditure as such but in the ways in which it has been financed, namely by an excessive creation of money. This, it is said, has set in motion the process consisting of expectations of increasing price rises and a growing propensity of lenders to ask and borrowers to accept higher nominal interest rates. In short, this second interpretation places the expansionary monetary policy, and not its opposite, at the origin of the high rates.

In the present state of our knowledge it seems beyond doubt that the increased public expenditure unaccompanied by additional taxation is the cause of the inflationary tensions in the United States. The Federal Government budget deficit shows an increasing deterioration from 1965 until the second half of 1968, when the Government introduced the

temporary surtax of 10 per cent on the profits of corporations and on private incomes and imposed ceilings on the expansion of the main categories of expenditure. The inflationary potential inherent in the growth of public expenditure was increased by the nature of the expenditure, the highest annual rate of increase being in the components connected with the military sector. The rise in prices had certain redistributive effects in favour of firms and created expectations of their continuance. There was a further increase in overall demand, in monetary incomes and in the volume of money required for transactions, leading to pressures on interest rates.

The restrictive fiscal and monetary policy adopted towards the end of 1968 affected the course of the American economy during 1969, a year of slackening expansion according to the Federal Reserve, in which unutilised productive capacity and the rate of unemployment increased appreciably, industrial output underwent a sharp reversal of trend, the rise in costs was accentuated and corporation profits contracted, while the rate of increase in prices did not slow down. Nevertheless, fixed capital investment by the manufacturing sector continued to expand at a growing annual rate. This is probably attributable to the belief that the restrictive monetary policy was of a temporary nature. Under these conditions it seems safe to say that the most showing result achieved by the restrictive policy in 1969 manifested itself at the international level: the high interest rates ruling in the United States helped to bring about a shift of liquid dollar funds held by non-residents, promoting their transfer from official authorities to private sector, a process which was reflected in an improvement in the United States' balance of payments on official transactions basis.

Assuming that the monetary base was the strategic variable through which the money supply was regulated, it would have been more logical to accept the assumption that the whole range of interest rates would undergo the variations due to such an action. Instead, limits were maintained on the interest rates on deposits and certificates of deposits and, at the same time, the public's access to the Treasury Bill market was restricted by a raising of the minimum denomination of newly issued bills. The widening of the gap between the free rates and the regulated rates led to a reduction in deposits and impelled the banking system to safeguard its own share of the market, threatened by the yields of financial assets offered by intermediaries not subject

to regulated rates. The increases in long-term interest rates and the rates paid on the deposits of branches abroad were in fact accentuated by the official fixing of the rates on time deposits of residents and the following reduction in deposits of this category. The banks' reaction was on the one hand to sell substantial quantities of bonds, thus aggravating the fall in prices, and on the other hand to attract deposits via their foreign branches by offering exceptionally high rates, which consequently spread to the markets of the various countries concerned.

The American authorities have found that the deviations brought about by the constraints on rates lengthen the periods of time required to enable monetary policy to produce results and diminish its effectiveness; the unusual scale of the deviations showed that these constraints bring about movements contrary to the aims pursued by the control of credit expansion. Last January the monetary authorities therefore decided to fix the maximum rates on time deposits and certificates of deposits close to the free rates; but there remained the burdensome legacy of the new markets, which, by their very existence, increased the system's ability to resist the effects of monetary policy.

In June 1969 the monetary authorities had adopted measures concerning the constitution of obligatory reserves, as a counterpart to the changes in deposits received by American banks through their foreign branches. These measures had two aims: on the one hand, to discourage further obtaining of deposits on the Euro-dollar market, with a view to helping to reduce the pressures on interest rates, and, on the other hand, to prevent too large a reflux of liquid funds from the Euro-dollar market into the reserves of central banks, in order to soften the impact to which the international monetary system would have been subjected when the conditions offered by American banks had reduced the attractiveness to non-residents of keeping their available liquid funds with these banks.

At the beginning of 1970, United States monetary policy became less restrictive, probably because of a belief that an accentuation of the signs of economic recession would have provoked the reaction of the country's political leadership and that the latter might have adopted expansionary policies which would have produced inflationary forces even more serious than those which the monetary authorities were trying to curb. At the same time the pressures on costs and the expect-

ations that they will become worse have been intensified, on the eve of the outbreak of trade union disputes in some sectors of industry. The monetary authorities must therefore decide how much to expand the money supply and allow the cost increases to be passed on to prices. Actually, business expectations are now being revised. This revision, necessitated by rapid deterioration in profits, financing difficulties and slowing down of some components of demand, could lead to a curtailment of investment programmes and ultimately to a contraction in productive activity and employment on a scale harmful to the United States and the rest of the world. Since, with such prospects, the need for domestic economic revival would prevail on requirements connected with external equilibrium and, on the other hand, stable monetary conditions at high levels of output and employment could coexist, as has already occurred in the past, with a balance of payments deficit, dollars might continue to be in abundant supply, accentuating the disadvantages of a system based on fixed exchange rates.

The worsened prospects are reflected in the fall in prices of shares of United States corporations in recent weeks. The downward trend of prices began in the last months of 1968, almost simultaneously with the introduction of the monetary restriction, during which yields on fixed-interest securities rose to unprecedented levels. The persistence and extent of the decline influenced the movement of share prices in the other industrial countries, owing to the growing number of channels of communication between security markets.

In the United Kingdom, undeniable success was achieved by fiscal and also monetary policy in keeping in check the various components of domestic demand and thus reversing the country's external position; in view of these developments, the monetary authorities were able, this year, to lower the discount rate twice, the second time as part of the measures designed to produce a cautious revival of domestic demand. The future trend may, however, be strongly affected by the movement of labour costs, the recent behaviour of which seems to be renewing inflationary pressures.

In France, after the devaluation of last August, which took place while a marked inflationary process was still in progress, the authorities introduced an intensive programme of fiscal and monetary restriction, which is proving particularly effective in curbing domestic demand, so

that there seem to be good prospects of a slowing down of the rise in prices, which are also subject to direct controls.

In Germany the mark was revalued after the expansion in domestic demand and the strains of the labour market had brought about an upward movement of prices which is still accelerating. While the measure had the effect of restoring equilibrium in foreign relations, its contribution to moderating the domestic boom will depend on the success of the action taken to curb demand, hitherto centred mainly on changes in the discount rate, which has been increased several times since April 1969, when it stood at 3 per cent, until March of this year, when it reached 7.5 per cent.

The differing degrees of expansion of demand within the individual countries and the resultant divergences in price trends produced balance of payments disequilibria which in some cases were corrected and in others aggravated by capital movements brought about by interest rate differentials and by expectations of changes in monetary parities and political and social anxieties. During the two-year period 1968-1969 the maximum change in the net foreign creditor position of the monetary institutions was 5.1 billion dollars in France, 6.2 in Germany and 1.5 in Italy. The same change for the European Economic Community was 8.9 billion.

It is thus confirmed that the increased interdependence of the Western economies, in the absence of any coordination of economic policies, requires that the international monetary system should possess a certain degree of flexibility, either with regard to the multilateral and bilateral credits on which it can rely or with regard to the exchange rates between the various currencies, or both of these.

The discussions concerning the reform of the international monetary system which were started in 1963 led to the decision to create special drawing rights totalling 9.5 billion dollars over the three-year period 1970-1972, of which 3.5 billion have been distributed this year. The Amendment to the IMF Articles of Agreement contains ideas put forward by the Bank of Italy: the reform of the system, the Bank contended, would have to be such as to enable the volume of international liquidity to be adjusted to the requirements for financing the balance of payments the scale of which is greater the larger the increase in the volume of trade and capital movements; the volume of international liquidity would have to be determined by decisions of interna-

tional institutions independently of the supply of newly-mined gold; and the system would have to be based on the acceptance of fixed rates of exchange.

The Bank of Italy upheld these views in the conviction that acceptance of fixed exchange rates would help to speed up the process of economic integration and that the latter, if carried out within the framework of institutions such as the European Economic Community, would have accelerated the process of political unification. Last year's Report referred to an adaptation to changed conditions and a certain preference was expressed for systems that included moderately flexible exchange rates. Recent events lead us to confirm this preference and to consider as a progress the discussions initiated within the international institutions on reforms that do not rule out acceptance of a certain degree of flexibility in the exchange rates between the various currencies, duly limited by international agreements so as to restrict the margin of uncertainty. This course would create the conditions for greater monetary independence vis-à-vis external factors, and especially in relation to the U.S. dollar, without destroying the link between the markets, which has allowed in the past, and will allow in the future, a steady growth of trade, which, in turn, is one of the prerequisites for improving the standard of living in Western countries.

At the beginning of the 1960s Italy shared the hopes, expressed by authoritative international bodies, that economic planning would be centred on incomes policy, which was interpreted as the responsible participation of trade unions in the taking of decisions concerning the production of income, its utilisation and distribution. It should be admitted that in Italy, as in other countries, it has not been possible to coordinate the trade unions' demands with the other variables which determine economic equilibrium; everywhere the result has been cost tensions of varying intensity. Nor is there any prospect of a reduction in the variability of wage increases in relation to productivity in the various countries. Furthermore, the differing degree of elasticity of import demand in relation to income, in a period in which the latter is increasing rapidly, will also tend to increase the complexity of the process of adjustment. The balance of payments disequilibria may in turn be aggravated, because there is very widespread anxiety among businessmen concerning domestic and international political stability, and political factors make it difficult to determine the direction of capital movements.

Although the modern world, partly as a result of its very dynamism, is particularly prone to inflationary pressures, the intensity of such pressures will probably continue to vary, so that it will be difficult to reconcile a greater degree of economic interdependence with a system of fixed exchange rates; hence it may be necessary to resort to a limited flexibility. Such an innovation might stimulate the transformation of the European Economic Community into an economic union, if the currencies of the member countries were to become interchangeable among themselves on the basis of fixed rates, while being convertible into non-EEC currencies at fluctuating rates. This would presuppose some progress towards the unification of economic and monetary policies. But should this progress be made by coordinating and harmonising the various policies, or by first of all unifying the institutional structures within which such policies are carried out? I tend to favour the second solution. I believe priority should be given to the unification of the institutions; I believe less in the possibilities of coordination. The process of bringing economies closer together by stages has probably exhausted its driving force.

Some people suggest that the central banks should immediately pool part of their reserves so as to promote the coordination of economic policies. These suggestions are based on the idea that central banks, as they are largely autonomous bodies, would be better fitted for laying down long-term policies and would be capable of influencing Government decisions. Without even considering the soundness of the idea underlying this argument, however, it seems doubtful whether a community institution could fulfil the function which it is proposed to assign to it; it would probably be exposed to conflicting political pressures more than the individual central banks are at present and the effect would be exactly the opposite of what was intended.

When the European Economic Community was founded, it was thought that greater economic prosperity would ease social tensions. Actually, they became more acute—on the one hand because the high standard of living obtained itself made individuals aware of the possibility of aiming even higher; and on the other hand because backward social conditions, which, for various reasons, exist almost everywhere, have become less and less tolerable.

These growing tensions call for an effort of adaptation in the institutional field at both the domestic and the international level.

It must be admitted, however, that the existing institutions, although imperfect, have allowed the high degree of cooperation between the Western economies to remain unimpaired. Italy has made an active contribution to international cooperation and, even in view of recent events, has no reason to regret it; some of the country's difficulties have been mitigated thanks to this cooperation. The difficulties have been due to certain developments, some new and some merely aggravated, in our economic situation, both in its internal productive and monetary aspects and in its financial relationship with other countries. Let us now turn our attention to these developments.

The repercussions of capital movements on Italy's balance of payments

After five years of surpluses, Italy's balance of payments closed with a considerable deficit in 1969 owing to the intensification of net capital exports. The deficit became exceptionally large in the first two months of 1970, but contracted appreciably in the following two months owing to the less unfavourable trend of the current account but, most of all, of capital movements. To finance this deficit recourse was had to the reciprocal swap arrangement with the Federal Reserve Bank of New York. This action was based on two considerations:

- as has been pointed out in the past, reserve assets are invested with an eye to combining liquidity and yield; however, considerable balance of payments deficits—attributable either to unforeseeable fluctuations in the current account balance due to interruptions in production or to capital movements—may give rise to requirements that cannot conveniently be met by disinvestment;
- as the magnitude and the timing of the correction of the deficit are difficult to foresee, it may be advisable to finance it by utilising short-term credits; in Italy's case, when recourse was had to such credits, talks had been started concerning medium-term financing operations, the result of which was impossible to forecast.

With regard to capital exports and their effects on the process of financing domestic investment, justifiable concern has been expressed and inaccurate statements made. Of the resources formed as a result

of the high levels of production achieved in Italy, part, representing the surplus on the balance of payments current account, was invested abroad. The ensuing increase in the country's assets took the form of export financing, private financial assets and foreign exchange reserves. The persistence of a surplus on current account during the period 1965-1969, equal to 3.2 per cent of the gross national product, indicated the Italian economy's inability to turn a large proportion of the savings formed within it into domestic investment. In the body of this Report and in these Concluding Remarks, mention is made of the causes which impeded domestic investment: the failure of the public authorities to adjust their structure to the complex functions which they have to perform; the lack of appropriate financial instruments; the high level of business indebtedness; and the uncertainties as to future prospects. Within this framework, the monetary policy pursued during this period was aimed at making good the loss of liquidity due to capital exports. It was not until the summer of 1969 that the strengthening of inflationary pressures, together with the losses of reserves, forced the authorities to pursue a less expansionary policy, with unfavourable effects on the cost of financing.

The phenomenon of private capital exports, which is generally identified with that part of it which consists of the illegal export of bank-notes, is in fact more complex. The anxiety felt about the consequences of this phenomenon are not without foundation and the monetary authorities consider it their duty to suppress its illegal manifestations, without, however, risking to do disastrous damage to the freer trade and payments system which, not without difficulty, has been attained.

The discontinuation of the repurchase of bank-notes by the Bank of Italy, the adoption of a tax on reimported notes and the creation of the so-called financial lira are solutions that amount to the reintroduction of foreign exchange control. Some people are asking for foreign exchange control to be re-established in a situation of progressive international integration in which the size of the domestic market is clearly inadequate to meet the requirements of consumers and producers, as is shown by their increasing recourse to foreign products, foreign markets, advanced technologies wherever they are to be found and, in general, to an evergrowing international component, both in the organisation of production and in consumer expenditure. This

component is also finding its way into choice of portfolio investment, and may have helped to accelerate the export of capital for the purpose of achieving the desired diversification—all the more so because this diversification has been impeded by the policy pursued within the country, which has accentuated the undifferentiated nature of our capital market.

All the solutions suggested have been considered by us, including that of asking foreign banks, and especially those in Switzerland, to give us their lists of Italian depositors. We refrained from making this request because we believed that it would be refused, as have been similar requests made by countries with greater bargaining power than we had. The Bank of Italy's refusal to repurchase reimported bank-notes leads to their allocation on the foreign market at an exchange rate lower than the official rate, in order to meet demand from tourists and emigrants. Similar results are produced by a tax on reimported bank-notes. Nor would the introduction of the financial lira be a new solution; it has been found in practice that it is effective insofar as the divergences in prices between the official market and the capital market are restricted by intervention by the authorities and thus, ultimately, by sales of foreign exchange taken from the reserves. Lastly, the solutions in question tend to lose their effectiveness quickly unless they are reinforced by the multiplication of controls, which in turn produce increasing distortions.

The Bank of Italy preferred to confine its intervention to the measure taken last February whereby Italian bank-notes returning from abroad are collected centrally at the Bank of Italy, thus lengthening the time between their being dispatched and their being credited on capital account. In the period March-May 1969 bank-notes totalling 336 billion lire were repurchased; in the corresponding period of 1970 the total was reduced to about 150 billion lire; the percentage difference between the price for bank-notes and the official rate was kept between 1 and 2.5 per cent. The Bank also restricted the length of time within which importers and exporters, respectively, could advance payment for goods and defer collection of payments, the aim of this being to limit the export of short-term capital connected with goods transactions and stimulated by the interest-rate differential between the domestic and international markets. Lastly, in a situation in which the differential tended to decrease or even to be reversed—that is, when

credit abroad became cheaper than in Italy—the Bank of Italy allowed banks to refrain from complying with the obligation to balance their foreign exchange position and make use of foreign credits to finance Italian exports, the purpose of this step being to place Italian exporters on an equal footing with their foreign competitors.

The Bank of Italy is still convinced that any autarkic policy has regressive effects on the evolution of income and we hope that this conviction will continue to inspire the country's economic and financial policy. Compulsory measures are limited in their effectiveness and in any case restricted in terms of time. Hybrid systems do not last and sooner or later lead to autarky. External payments equilibrium must be sought by creating conditions of yield and taxation for domestic investment which are competitive with the alternative opportunities offered abroad, and a general situation that favours the investment of foreign capital to outweigh the outflow.

This is the direction in which we have acted during the recent period and it is satisfying to note that Italy continues to be a country in which foreign private financial institutions are prepared to invest very large amounts of capital; we refer to the loan operations already concluded and those which are likely to be so in the near future. We are reaping the benefit of a persevering policy of financial cooperation tenaciously pursued at all levels: it is gratifying to recall the readiness with which the United States Treasury and the Federal Reserve Bank of New York, in the brief space of one day, increased their credit lines to the Bank of Italy by 500 million dollars, and the readiness with which American, Canadian, British, German and other banks participated in the conclusion of the major loan operation to which we have referred.

The total of the loan operations completed and approaching completion amounts to about one billion dollars. Most of them have been negotiated on the basis of an interest rate which is variable from half-year to half-year in relation to that applicable to inter-bank dollar funds on the London market and they give the borrower the option of premature redemption without payment of any penalty. It seemed to us desirable to include this clause in order to give ourselves the possibility of paying off the loans as soon as our balance of payments conditions permit or, possibly, of replacing loans at high interest rates with others on less burdensome terms.

We arranged that the borrowers should temporarily pay the countervalue in dollars into accounts at the Bank of Italy in order to eliminate the expansionary effect on domestic liquidity and relieve the borrowers of the need to maintain lira holdings in excess of their immediate needs. During the period in which these sums remain on deposit at the Bank of Italy, the procedure is tantamount to the imposition of an obligatory reserve of 100 per cent. The proceeds of these loans were used by the Bank to repay short-term debts contracted in the first two months of the year. We have thus consolidated our indebtedness and correspondingly increased our net official reserves. The increase in May was about 400 million dollars.

Wages, costs, prices and the equilibrium of enterprises

The recent wage increases, coming on top of the rises in prices of imported raw materials, confront the monetary authorities with complex problems from the dual angle of curbing inflation and safeguarding the economic equilibrium of enterprises as prerequisites of growth.

It is necessary to undertake a quantitative assessment making adequate allowance for foreseeable increases in the cost of labour per unit of output; it is necessary to establish to what extent it is possible to transfer the cost increases to prices and what are the results of the contraction in expected profits as regards capital investment decisions, and in current profits for financing purposes; lastly, it is necessary to estimate the propagation effects of the price increases in the various sectors. For this purpose a distinction must be made between the sector comprising the activities most exposed to foreign competition and that comprising the activities which are relatively free from such competition, since the possibility of enterprises to adjust their prices to the requirement of covering costs, plus an appropriate profit margin, is less or greater depending on whether they belong to the former or the latter category.

When direct costs go up owing to rises in the cost of raw materials or the cost of labour or to a combination of both these causes, enterprises tend to transfer the increases to consumers; but the greater or lesser

extent and rapidity of such transfer depends on the greater or lesser strength of demand in relation to the higher or lower degree of utilisation of productive capacity.

The empirical studies made show the irregularity of the evolution of productivity, which rises faster at the beginning of the expansionary phase of the business cycle and slows down as its peak is approached. This trend appears to be attributable to the lack of homogeneity of the factors of production, as a result of which, as demand expands and the degree of utilisation of productive capacity increases, use is made of progressively less efficient equipment and labour, leading to declining returns per unit employed. The rate of increase in productivity actually falls when the system, under the pressure of inflationary processes, is most in need of higher productivity. Under these conditions the rate of monetary expansion represents an instrument for curbing demand and, ultimately, profits. Recourse to it may become even more necessary when the shortening of working hours restricts the possibilities of utilisation of invested capital and thus the possibilities of expanding supply. But the monetary instrument is undoubtedly imperfect owing to its insufficiently selective nature and owing to the difficulty, in the short term, of controlling the volume of credit, which also depends on the behaviour of businessmen, by regulation of the monetary base.

Whereas, in the sectors less exposed to international competition, increases in labour costs are accompanied by large positive changes both in prices and in unit profits, in the sectors which are open to competition, domestic prices display greater sensitivity to variations in prices of foreign products. If the latter are stable, increases in the cost of labour per unit of output bring about, in the short term, reductions in the quota of other incomes, which, owing to the interdependence between sectors, are adversely affected also by rises in labour costs in other less exposed activities. An increase in the prices of competing foreign products makes possible, on the other hand, an increase in profits and offsets the negative effect of the higher labour costs on unit profits. The rises in productivity in the sectors exposed to international competition are greater than the average rises throughout the system; this difference is probably largely attributable to technological reasons, but the positive effect of foreign competition cannot be ruled out.

Under a system of free trade and fixed exchange rates, the last barrier which prevents a further transfer of cost increases to prices consists of international prices. When this barrier has been reached, increased expenditure is directed towards imported goods. A rejection effect takes place via the balance of payments, which moves from equilibrium to deficit or from surplus to a smaller surplus. In these circumstances, growing monetary demand can coexist with stationary domestic production and employment. The proposition that the economy should be given as much liquidity as it needs is tantamount to saying: do not give any liquidity which feeds a balance of payments deficit.

In the course of the controversies concerning the interpretation of the relationships between prices and cost increases brought about by wage increases, it is often asserted that the present price rises are due to structural deficiencies in our economy. These do admittedly play a part in restricting the possibilities of supply, especially in housing, public transport, public health services, etc. Our Reports have for a long time emphasized the harmful effects of inadequate investment in the social infrastructure. It has been repeatedly stated that this inadequacy would be reflected, sooner or later, in cost and price increases. But it is not wise to expand monetary demand while disregarding the possibility of bringing supply into line with it, as if to emphasize past mistakes; for the short-term effect will not be to improve supply but only to curtail the purchasing power won through the labour conflicts.

The problem of the relationship between the rate of inflation and structural deficiencies is bound up with observance of the conditions for monetary stability; for the latter to be maintained it is necessary that the increase in monetary demand due to wage increases should be coupled with a corresponding growth in the real flow of resources. This correspondence can also be achieved as the structural deficiencies are remedied, but inevitably at a slower pace than for short term variations in economic conditions.

In most cases, however, the adaptation of the social infrastructure has not run up against any financial limits, nor, certainly, have such restrictions hampered the building of workers' dwellings; the limitations have been and are of a different nature and their removal calls for unremitting effort by the public authorities, an arduous task which cannot be implemented merely by public opinion. If there is an inadequate

supply of social services, it may be decided to impose administrative restrictions on prices; but it is essential to realise the inherent contradiction in policies which expand purchasing power when they give rise, sooner or later, to the need to introduce price controls in order to defend the purchasing power which has been so liberally distributed. The defence may furthermore prove to be illusory if the excess demand is concentrated in the sectors where the controlled price list does not apply: the ultimate result may be even larger price rises or increased imports, or both these phenomena.

Inflationary impulses from abroad will continue in 1970 to be one of the factors pushing up domestic prices, but they will be greatly aggravated by wage increases. According to estimates made at the end of last year by the Technical Committee of the Ministry for the Budget, the average increase in the cost of labour per worker in the economy as a whole in 1970 is likely to be 13 per cent. More recent data from another source point to an even larger average increase of about 16-17 per cent.

In the industrial sector, which is more affected than the others by the wage claims, the rises are expected to be higher; according to the estimates of the above-mentioned Committee, the increase in industrial earnings in 1970 is likely to be between a minimum of 11 per cent in the sector for which no renewals of contracts are scheduled and a maximum of 21 per cent in the other sectors; in the latter, according to other estimates, the increases will be very much greater.

The differences in wage movements are, however, merely temporary and tend to disappear as the wage contracts in other sectors expire, as is shown by the textile sector, where workers have obtained an increase similar to that in the engineering sector.

With further contracts expiring during the year, three quarters of all industrial workers will have received wage rises representing practically uniform rates of increases by the end of 1970. This uniformity is in contrast in the various sectors to the very wide range of changes in productivity; for instance, with regard to the industries whose contracts have already been renewed, there is a great difference between the metallurgical and chemical industries, on the one hand, and the engineering and textile industries, on the other. In the case of the former, both very capital-intensive industries, with relatively newly-constituted and

therefore technologically advanced plants, the productivity increases are high; in the case of the latter, conditions are much less favourable, factors contributing to this being the existence of firms which differ greatly in efficiency and size and also the limited impetus imparted by scientific research and technical innovations. For the engineering industries, furthermore, the situation is made more serious by the fact that the prices of their raw materials rose particularly sharply during the year.

In any case, the rate of wage increases in general has been more than double compared to the productivity gains possible in the most rapidly advancing sectors. Consequently the wage rises are bound to be reflected, to a greater or lesser degree, in higher labour costs per unit of output, and although their extent will differ from sector to sector they will be sufficient to create serious difficulties for the maintenance of financial balance by enterprises, even assuming that they are partly transferred to prices.

Still according to the above-mentioned document produced by the Ministry for the Budget, the maximum limit beyond which industrial prices should not be allowed to increase is 6 per cent. This limit is seen to have already been exceeded in view of the difference of 6.5 per cent between the level reached in March 1970 and the average for 1969, while compared with the figure for a year earlier it works out at nearly 9 per cent, so that the rate of increase in prices in Italy, which had up to last year been below that in other Western countries, is now greater than that in most of them.

The difficulties experienced by small and medium-sized firms —on which the impact of prime cost is generally stronger—are sapping their capacity to survive, so that they are tending to seek protection from big companies, even abroad, or from public enterprises.

Many foreign enterprises are acquiring participations in Italian firms, thus in a number of cases weakening their autonomous and promising growth potential. In other cases, Italian firms are taken over by others in the public sector of the economy. Often the price is paid to the foreign holding companies in whose name all or part of the shares in the enterprises taken over had been registered. The concentration of means of production in the public sector sometimes leads to a technical improvement in the enterprises, but in other cases to a restriction of the area of competition or to the forced rescuing of inefficient firms, both of which developments are harmful to the proper working of the mixed economy.

The promise of credit facilities in order to halt these processes does not help, because there are limits not only to credit-granting possibilities but also to the firm's capacity for taking up credit. It is therefore necessary to examine the mechanism of business financing.

In the last twenty years enterprises have financed their investment by increasing their recourse to borrowing; this, in turn, has taken the form of indebtedness to financial intermediaries. The effect of this process has been an increase in the financial intermediaries' raising of funds through the creation of liquid or quasi-liquid credit instruments. In the five years 1951-1955 loans to the economy through the direct issue of credit instruments represented 13.8 per cent of overall financing; this ratio decreased to 11.3 per cent in the period 1956-1962 and to 8.2 per cent in the period 1963-1969. In the same periods the public's liquid assets rose by annual averages of 14.4 per cent, 13.2 per cent and 12.4 per cent, while the rates of increase in the gross national product at current prices were 10.2, 8.9 and 9.5 per cent.

The method mainly used by enterprises to meet their long-term financial requirements was to borrow from the special credit institutions, often at rates subsidised by the Government. The special credit institutions, for their part, obtained the funds by issuing bonds, which were largely subscribed by the banks. This financial circuit and the preferences of savers, together with the reduced share of direct financing, led to the formation of large balances of money and quasi-money mostly in the form of bank deposits.

The separation of the centres of savings formation from those making the investments became gradually more pronounced; in 1969 the share of net household savings in relation to total savings rose to 80 per cent. This not only proves that the process of financing depends on the continuity of household saving but also indicates the complexity of the financial intermediaries' task of supplying both the public authorities and business with the funds they require for their activities.

The harmful repercussions are most noticeable in private enterprises, which, owing to their present financial situation, seem to have little inclination to compensate for the shortage of risk capital by further borrowing. Public enterprises are less sensitive to the burden of indebtedness, since they are less hard-pressed both by the requirements of business liquidity and by those of the rate of return on risk capital. The Report shows that in the past six years there has been approximate

equality between public and private enterprises in the rate of gross saving; the former, however, have made bigger increases in their fixed technical assets, so that their rate of self-financing is lower than that of private enterprises. In industry, fixed investment undertaken by public enterprises in 1969 represented 38 per cent of the sector's total investment.

Interest rates, inter-bank competition and organisation of the capital and money markets

The wide fluctuations in interest rates have revived discussion concerning the relationships between prices, interest rates and monetary policy. Without embarking on theoretical arguments, we think that it can be said that in the presence of inflationary expectations nominal rates reflect these expectations, generally with a time-lag, and tend towards the maintenance of a relatively stable level of real returns, which, furthermore, under the pressure of increasing economic interdependence, tend to assume fairly uniform values in the markets of all developed countries.

History shows that changes in prices are usually coupled with changes in interest rates in the same direction; this has been observed, for instance, in the United States and the United Kingdom over the decades. This relationship was suddenly disrupted at the time of the second world war; in both the United States and the United Kingdom, during the war and the immediate postwar period, the expansion of the public debt was accompanied by stability of interest rates, achieved by policies of rapid expansion of the money volume coupled with compulsory curbing of private expenditure. At the beginning of the 1950s interest rates in both countries were at abnormally low levels. It was in this situation that their rise began. The increase was gradual, although in the United Kingdom the maintenance of external equilibrium necessitated a structure of interest rates higher than that ruling in the United States. In more recent years, inflationary expectations have played an important part in bringing about the rise in nominal rates.

In both the United States and the United Kingdom, 1969 was the year in which there was an accentuation of monetary policies mainly

based on control of the quantity of money. While those interest rates which were free to move reached very high levels, those which were held down by administrative regulations created greater tensions in the market areas where freedom prevails. It would appear that the peaks have been reached, but it is also probable that the failure to control inflationary pressures and expectations of their continuance will keep interest rates at high levels in the immediate future.

This picture of extreme tension in international interest rates and growing difficulties in controlling capital flows forms the background to the decisions taken by the Italian monetary authorities in the first half of 1969, which became operative in the second half of the year. These measures were inspired not only by the need to help to reduce the pressures leading to capital exports by promoting the alignment of domestic interest rates with international rates, but more particularly by the conviction that the inflationary pressures from abroad which appeared in the Italian market in the first half of 1969 would be supplemented by other impulses — the full force of which was not known when the decisions were being made— deriving from the settlement of labour disputes affecting a large number of dependent workers.

The manner in which the increase in interest rates took place in Italy will be discussed a little further on; with regard to the choice of timing, it should be emphasized that this made it possible, within a period of about six months, for Italian interest rates to be brought to a level close to the highest prevailing abroad.

As interest rates in Italy had approached the peak at the time when in the major markets, despite some contrast, a downward trend was becoming apparent, the problem arose whether this movement ought to be followed or if, on the other hand, it was and is advisable to aim at a relationship between Italian and foreign interest rates corresponding to the need to attract capital to Italy. The progress of integration within the European Economic Community, the possible enlargement of the Community and a policy of increasing participation to international markets, together with the acceleration of the adjustment of Italian wage levels to Community levels, theoretically give Italy the position of a net capital-importing country, at least as long as there is a gap between the amount of capital available per person employed in Italy and that in the other industrial countries of Europe.

In order to interpret the policy pursued with regard to interest rates it is necessary to mention the distinctive features of the Italian market, from the point of view both of the responsiveness of rates to changes in the monetary base and of the interdependence between short and long-term rates.

The monetary authorities create the so-called monetary base, consisting of the legal tender and of financial assets which are eligible without limits for inclusion in the obligatory reserves or freely convertible into cash at the central bank. In relation to the trend of income and its distribution and to the changes in the interest rate —variables which in turn are influenced by the speed of creation of the monetary base and the channels through which this takes place— the public decides what proportion of the above-mentioned assets it will hold and what proportion it will transform into bank deposits or securities. An increase in the interest rate leads to a reduction in demand for the monetary base from the public and a growth in formation of bank deposits. According to the results of econometric surveys it seems safe to say that, between these two assets, there is a substitutability ratio capable of converting, out of present holdings, about 300 million of currency into deposits within the period of one year if there is an increase of one percentage point in their rate of return; this effect is further heightened by the action of the credit multiplier. This means that the results of a restrictive monetary policy would be much more strongly felt, but with a possibility of giving rise to the distortions which have been experienced elsewhere, if the banking system were unable to absorb, by means of the free determination of rates, as least the first impact of the restrictions, or if, at times of administrative limitations on rates, there were not available on the market a sufficient amount of short-term securities whose yield could vary according to the liquidity situation.

Since in Italy the ratios between monetary and quasi-monetary balances on the one hand, and the gross national product, on the other hand, are very high, it would appear desirable to create a more appropriate structure of yield on financial assets. A contribution to the attainment of this aim might be made by the observance of limits to the rate applicable to bank deposits; this would entail the necessity of offering the public money-market securities at rates not subject to administrative restriction and extremely sensitive to variations in market conditions,

which could serve as a vehicle for the investment of liquid funds not going into bank deposits.

The deeper knowledge of our economic system and the transformations to which it is subject could not fail to be reflected in our attitude towards the possible solutions of the complex problems with which monetary policy is faced. With regard to the interest rates charged on loans and paid on deposits, our policy as expressed in the Report to General Meeting held on 30th May 1962, « has always been to prefer those types of restraint which work through agreements among the banks themselves. We have no intention of suddenly adopting the kind of intransigent attitudes for which we sometimes chide our colleagues in the banks, and we shall resist the proposals, which are often made to us, to adopt coercive controls which, in our view, are humiliating both for those who impose and for those who are subject to them ». In the same year we stressed the desirability of introducing limits on the rates applicable to inter-bank accounts. Subsequently, however, we modified this attitude and at the beginning of this year we lifted the restrictions on the determination of interest rates which can be paid on inter-bank accounts. We felt that by this measure we were giving a start to the creation in our country of a market through which the liquid funds of banks will be redistributed on the basis of the indications derived from the fluctuations in interest rates.

In the five-year period 1964-1968, under the pressure of increasingly keen competition between banks, interest rates on deposits rose at a moderate but steady pace, while lending rates showed a tendency to decline, fluctuating as the monetary situation changed in the various phases of the business cycle. In the first half of 1969 lending rates remained fundamentally stable, despite the obvious upward trend of prices; in the second half they began to increase. The rise in deposit rates quickened in the first quarter of 1970.

A survey of the data on the rates applied to bank lending operations, started in January, 1969 in cooperation with a group of highly mechanised banks which administer more than half of the country's deposit funds, revealed a continuous increase in bank financing costs from the third quarter of 1969, which became more marked at the time of the changes in the official discount rate. From an overall average of 6.81 per cent at the end of June, the figures rose to 7.51 per cent at the

end of September, 7.99 per cent at the end of the year and 8.22 per cent at the end of March 1970, with a wide spread between the values observed. The rates rise gradually from the centres in the Western regions of the country to those in the East and from the North to the South, with the exception of Central Italy; the discrepancy is more than offset by the far-reaching special allowances enjoyed by the Southern regions and the islands.

The process of adjustment of rates in the second half of 1969 was faster in the case of lending rates, owing to the characteristic « stickiness » of deposit rates; this enabled banks of all sizes to achieve satisfactory financial results. On the other hand, the trend in the first months of this year suggests that, partly also owing to the heavier administrative expenses resulting from higher personnel costs, the banks' profit and loss accounts will come under heavy strain. It is quite possible that smaller banks will suffer more from this than the large ones, so that the process which, in the banking sector as in others, is driving enterprises towards concentration will receive a further impetus. We confirm that we are watching this process closely and that it is not regarded as being contrary to the public interest provided that it does not jeopardize a banking structure capable of preserving a high degree of internal competition.

In the Italian credit system the competitive factors are relatively more important than in many other countries. The revival of a latent competition in recent years probably had its origin in the economic expansion, which increased the degree of integration of the Italian economy into the international system. The recent course of monetary policy has, in turn, helped to intensify competition. Its strengthening is confirmed by the reduction in the profit per lira handled by the banking system. The rise in the cost of raising funds has been offset by rapid rationalisation, which has greatly reduced the incidence of overheads and checked the decline in unit profits.

The alignment of bond rates began in the second half of 1969; it took place in a series of sudden movements, separated by periods of relative stability. Recourse to a gradual adjustment created greater uncertainty in investors regarding future tendencies than would have been produced by an adjustment made in one single step, even though larger. The choice of method was prompted mainly by two considerations:

- an immediate adjustment might have led to a volume of bond sales beyond the monetary authorities' possibilities of control;
- the adjustment coincided with the period of unrest connected with the trade union disputes; too sharp a fall in prices might have been interpreted both at home and abroad as a sign of crisis.

The monetary authorities preferred just to reduce their interventions gradually as rates declined. At the beginning of this year it was decided to cease intervention completely, except in the case of nine-year Government Bonds. Looking at the whole period of time during which Italy has changed over from an era of stability of rates to one of variation, it is found that the average decline in prices for our bonds has been the same as elsewhere.

An examination of the trend of subscriptions for bonds shows that the expectations of impending declines in prices in our market up to March 1969 produced their first effects from the month of July, with an appreciable slackening in demand for bonds by both institutional and private investors, but without the occurrence of any major portfolio disinvestments. In particular, an examination of the behaviour of banks shows that the sales of bonds in the period of declining prices largely formed part of their normal activity as intermediaries and that the volume of bank portfolios increased, from July to December, by 362 billion.

A special situation arose in the field of mortgage bonds, which had in the previous year benefited by a tacit guarantee of repurchase at the selling price by banking institutions connected with the bodies issuing them. This guarantee, while on the one hand had made it possible to expand the mortgage bond market, had on the other hand induced among subscribers the belief that they represented a substitute for deposits—that is, that they were transformable into cash on sight. When the gap between the yield on mortgage bonds and that on other bonds became too wide, the holders of mortgage bonds, considering the sacrifice of yield excessive in comparison with the advantage of the price stability, showed a tendency to dispose of them. The continuation of support for the prices might have forced the banks engaged in the support operations to resort to financing from the Bank of Italy. In order to avoid the excessive creation of liquidity which might have resulted from this, the authorities introduced a premium which rose

according to the date of repayment or, as an alternative, an increase from 5 to 6 per cent in the nominal rate on old mortgage bonds, the resultant burden being borne by the Government budget.

The decline in bond prices and the corresponding rise in actual yields were associated with the widening of the gap between bonds with higher coupons and bonds with lower coupons. The gap is due to the fact that private savers, with an eye to a possible sale of the bonds before maturity, prefer those with a higher immediate rate, since in that case they possess something certain, the coupon, as compared with an uncertain and remote factor, namely the redemption price.

With a view to defining the lines which will guide the policy of regulation of the long and short-term credit market and of intervention by the Bank of Italy in the bond market, it seems worth while to review the behaviour of the central bank during the past four years. Some people have said that the policy of supporting the prices of bonds, introduced in 1966, caused an excessive expansion of the economy's liquidity and prepared the conditions in which the current inflationary phenomena have occurred. It has been asserted by others that the discontinuance of this policy should have taken place earlier; while others, again, have stated that the policy should not have been discontinued at all.

The policy of intervention on the bond market in order to stabilize prices was introduced by the Bank of Italy in the second quarter of 1966 with the object of achieving two aims:

- to ensure the allocation to the public of new issues of substantial absolute amount, greater than was customary on the Italian market, by increasing the propensity of private individuals to invest in bonds thanks to the reduced risk of capital loss;
- to prevent a rise in domestic interest rates during a period of insufficient public and private investment activity.

Of the two aims pursued by the stabilization policy, that of the creation of a wider bond market was largely achieved. Purchases of bonds by the public in the three years 1966-1968 amounted to 1,300 billion on an annual average, against about 600 billion in the preceding three-year period, and even in 1969 they remain above 1,000 billion. Despite the unusually large volume of the new issues, the ratio between

bonds placed with the public and the total of issues returns to high levels between 1966 and 1968.

The object of stimulating investment activity was only partly attained; a more aggressive policy might have been desirable, but it would have been imprudent to implement it by pushing the level of interest rates down still further, since under changed market conditions the process of adjustment would have been more difficult. When the above-mentioned policy was decided upon it was not foreseen— nor perhaps could it have been— that long and short-term interest rates abroad would rise to such exceptional heights; more pragmatically, it was in fact decided to take a cautious line.

It certainly cannot be said that, during the period under review, the policy pursued by the Bank of Italy had the result of making it lose control of the process of creation of the monetary base. The latter increased to the same extent as the national income in current terms, during a period in which the price rise showed no sign of acceleration. The base created produced a growing expansionary effect because the banking system operated with a lower ratio between liquid funds and deposits, and this in fact was why the Bank of Italy, in the middle of 1969, exercised tighter control over the system's liquidity. The money volume increased at rates below those of the long-term average trend, and this development may be attributed to the stabilization policy pursued with a view to transferring the public's preferences towards bonds. This assertion does not contradict the preceding one, to the effect that the financial circuit via which firms financing took place led to the formation of large monetary and quasi-monetary balances consisting mainly of bank deposits; it merely means that the process of formation of these balances was not accelerated by the central bank's policy regarding the purchase and sale of bonds.

The critics who maintain that the policy of supporting bond prices was changed at the wrong time put forward two main lines of argument:

- they claim that the new policy was decided upon primarily in order to reduce the balance of payments deficit created by capital exports; it would have been preferable, they say, for this purpose to resort to the stricter implementation of administrative controls;
- the alignment between domestic and foreign interest rates ought really to have been brought about at the time when fluctuations,

even over a wide range, in the latter appeared to indicate a downward trend; it would have been better to hold back until equilibrium was re-established at a lower level.

We believe that we have already answered both these objections; we have confirmed that it is not true that the decisions adopted in the first half of 1969 and implemented in the second half of that year and at the beginning of 1970 were inspired only by balance of payments conditions. The gradual abandonment of the supporting of bond prices forms part of the set of measures adopted by the Bank of Italy in order to exercise more direct control over the creation of the monetary base. In a period marked by growing price tensions and expectations of their aggravation owing to higher production costs it appeared desirable to put an end to the economy's possibility of obtaining a monetary base theoretically unlimited in quantity by the sale of bonds which would be automatically absorbed by the Bank of Italy's purchases.

In the first half of 1969 the outlines of the present situation were in fact becoming sufficiently apparent, this situation being one characterised by the importance assumed by the irregular behaviour of autonomous factors contributing to the creation of the monetary base, i.e., the balance of payments, preponderantly influenced by capital movements, and the Treasury. We have emphasised more than once that since the second half of 1969 the Treasury's requirements have been practically the only factor in the creation of the monetary base. It should be added that in a number of cases even the Bank of Italy's operations with the banks are due to the requirements of local authorities or social security bodies; the Bank assists those banks or central institutions which require money for this or that purpose among the large municipalities which would otherwise find it impossible to pay salaries to their own employees. Somewhat similar cases occur when the banks subsidize social security bodies so as to prevent the cessation of hospital assistance. In these cases, as in those described above, the monetary authorities' interventions have been dictated by considerations not properly pertaining to the policy they are entitled to pursue; we are convinced that under present conditions interventions of this nature cannot continue and we consider it our duty to act accordingly.

In view of the growing deficits of the public sector, which occur at irregular intervals, it would be imprudent to reintroduce a policy

of unlimited support of bond prices. In case the Treasury deficit grows out of proportion to the economy's possibilities and the capital market has to be protected, partly in the interests of the Treasury itself, from the disturbances which would inevitably result, a buffer must be created between long-term securities and the rest of the financial system, so that the pressure exerted by the Treasury's requirements of funds is reflected in a rise in short-term rates without immediately affecting yield on all other financial assets. In other words, the capital market must be made more independent of the Treasury deficit so as to prevent the deficit from becoming the main factor determining long-term rates. This could be achieved by making short-term rates more sensitive, although this effect is limited by the speed with which impulses are transmitted to the other rates in the system. An efficient money market is even more necessary when, under conditions of growing budget deficits, two further unbalancing factors come into play, one being due to the time-lag between the fund-raising operation represented by the issue of bonds and the corresponding expenditures and the other being connected with erratic movements in public requirements due to events of various kinds which administratively impede the flow of collections or of payments. As these factors are largely exogenous, it is desirable that the fluctuations which they impart to the monetary base in the short term should be reflected in variations in short-term rates, so as to restrict the extent of those in long-term rates and thus make possible the orderly operation of the capital market.

The creation of a new type of Treasury Bill for free investment, the reimplementation of Central bank policy on discount rates and on rates on advances, accompanied by the introduction of a differentiation of these rates, and the liberalisation of the rates on inter-bank funds, were all measures aimed at promoting, in our system, the organisation of a more responsive money market. Over the next few months this mechanism will have to be refined; to this end the Treasury's requirements will have to be financed to a larger extent by means of money-market paper and possibly of medium-term bonds to be offered for subscription to the public at the Bank of Italy's branches at variable rates of interest. We also think that the Central Post Office Saving Funds could be financed by the issue of savings certificates bearing interest at a rate extremely sensitive to variations in money-market conditions; if the recently created Provincial and Municipal Credit Department were to

place all or part of its securities with the Central Post Office Savings Fund, it would be possible to provide the money necessary for financing local authorities by resorting alternatively to capital-market or money-market instruments.

At the same time the Bank of Italy might intervene more directly to guide the banks in determining their deposit rates. This does not mean that the central bank wishes to return to the so-called compulsory cartel; the intention is rather to exert supervision on the banks coupled with a system of incentives. In the case of banks which obtain deposits by offering interest rates within the maximum limits fixed by the authorities, it would be possible to apply an increase to the interest rates paid on sums deposited in the obligatory reserves.

To sum up:

- a)* in view of the persistence of large public-sector deficits and the irregularity of their appearance, we do not consider it possible for the Central Bank, although continuing to purchase long-term securities, to provide an unlimited guarantee of the stability of their interest rates;
- b)* we consider it necessary to protect the capital market by the organisation of a money market on which the public is offered the possibility of subscribing to short-term securities the price of which varies freely in accordance with market conditions;
- c)* supplementing this action, and insofar as it is found possible to ensure that the public's monetary holdings are not diverted to unregulated markets, it is considered desirable that the Bank of Italy should perform the function of coordinating the behaviour of banks with regard to the fixing of rates on deposits by periodically assessing a maximum limit, related, with suitable differentials, to some of the more significant rates observed on the capital and money markets.

This action will be facilitated if the public bodies will refrain from asking the banks with which they deposit their liquid assets to pay interest rates exceeding the maxima indicated by the monetary authorities. It must be admitted that in recent times the action of public bodies has contributed to the disorder in the field of deposit rates: bodies holding

liquid assets of several hundred billion lire have a bargaining power which exempts them from the limitations to which ordinary depositors are subject. When they take advantage of their bargaining power they actually increase their own funds by imposing a kind of tax, the burden of which is transferred to the economy as a whole.

The forms of financing of the public and private sectors must be adapted to new conditions. The field of activity of bodies that can raise funds only through the issue of bonds has widened greatly and is continuing to grow. Inflationary pressures have become stronger and their appearance has led to an extension of the range of measures whereby the various social groups protect themselves from their effects.

In this situation it is increasingly essential for the financing of the public sector to be effected through the issue of bonds with yields that are more sensitive to market conditions. An example of this new trend is the ENEL loan placed abroad this month. The success achieved by this loan at time when fixed-interest securities were not finding buyers shows that, in the present circumstances, international markets attach more importance to the flexibility of the coupon, in both directions, than to a constant high level of effective yield at maturity.

The Bank of Italy regards it as its duty to adapt the organisation of the capital and money markets so as to ensure their orderly operation, and in this endeavour it will enjoy the cooperation of the banks and other credit institutions. We wish in this connection to emphasize the assistance obtained particularly from the public-sector institutions and the « banks of national interest » in the allocation of bond issues. The alignment of the yields on fixed interest securities on the Italian market with the higher levels prevailing on the international market and in other national markets gives us greater freedom of action. The Bank of Italy will check that the volume and timing of issues of securities for public subscription are consistent with the domestic and international markets' absorptive capacity. Further amounts may be purchased directly by the Bank of Italy insofar as this does not encourage inflationary processes. Should the issues offered on the market not be fully subscribed, the Bank will duly respect these limits and refrain from intervening to take up the amounts remaining unsold.

Public expenditure and credit control

In last year's Report, when examining the general economic situation at the beginning of 1969 and emphasising the improved trend of domestic demand, we did not fail to mention certain less favourable signs which were appearing in our economy and which, coming on top of the uncertainties prevailing at the international level, made it necessary for us to take great care to ensure that the line of monetary policy which we had adopted, designed to promote the continuation of the expansionary phase, should not promote inflationary pressures. In the following months the destabilising influences became stronger; the contrasting features in the economic picture became increasingly numerous and the succession of events more and more rapid, so as sometimes to give rise to contradictory interpretations which made it difficult to decide what measures to adopt.

In view of the increased expectations of inflation and of a balance of payments deficit running far in excess of the limit of about 500 billion lire—the amount declared to be maximum that could be offset by the Bank of Italy's intervention from the point of view of its repercussion on the process of creation of the monetary base—the Bank took action, in the second and third quarters of the year, to slow down that process. As at the same time there was a substantial increase in demand for monetary base by the public, the central bank's decision led to sharp reduction in bank liquidity and a slackening of the credit expansion. In the fourth quarter, partly in order to meet the persistently growing demand from the public, the creation of monetary base was speeded up again and raised to an annual rate of about 11 per cent. At the end of December the banks' liquid assets were close to their September level, the contraction in the course of the year amounting to 323 billion lire. The demand for credit was being met at increasing rates of interest.

The events of last autumn caused very serious losses in production and their effects are still being felt. Although the labour disputes were concluded by negotiations at national level, serious disagreements remained at factory level, where it is often still not possible to achieve an output matching orders. The recovery has therefore been far from complete and the failure of labour relations to return to normal is giving

rise to new uncertainties. Further disputes in connection with renewals of agreements in other important sectors, such as the textile and electrical industries, gave rise to major strikes, mainly in March and April; other production losses have been caused by the general strikes held in favour of social reforms and as a protest against the cost of living. In the first quarter of 1970 industrial output was 5.2 per cent up on the same period of 1969 and in March, allowance being made for seasonal variations, only 2.5 per cent above the July 1969 peak; the preliminary data for April show a further weakening of the trend. The unsatisfactory recovery in production reduces the possibilities of reabsorption of the increased costs, and the shortening of working hours, together with the limitations imposed on overtime, results, in view of the shortage of skilled labour, in a reduction of available productive capacity.

On the demand side, the rise in the income of dependent workers will probably bring about an increase in consumption which, in monetary terms, has been estimated at an average of about 14 per cent for 1970. As for fixed investment, if the present capital investment projects of public and private enterprises are carried out, in view of the rise in prices, the rate of growth in expenditure is likely to be much higher than that forecast for private consumption, although residential building is likely to show little progress in real terms this year after the marked expansion of the last two years. There should also be a sharp rise in demand owing to the need to replenish inventories.

The Report stresses the obstacles that are encountered both in Italy and in many other countries by a policy aimed at coordinating the volume of public expenditure with the other components of demand so as to ensure economic equilibrium. The Report states that on top of the time lag, which elapses between the manifestation of the economic phenomena and their statistical recording, there is also a decision time, at parliamentary and government level, and an implementation time, at administration level. This makes it difficult to foresee sufficiently accurately the consequences of expenditure decisions which have accumulated in periods different from those in which the expenditure actually takes place.

Consideration of the period 1951-1969 leads to the general conclusion that Government departments are unable to adapt their action to the changing needs of the economy.

Only in 1965 and to a lesser extent in 1968 did they exert a substantial corrective influence on the general economic trend by contributing appreciably to the growth of income at a time when current-account in the balance of payments was showing a surplus and there were no price tensions.

In 1969 as a whole the public authorities' action was less expansionary—which seemed to be consistent with the changed situation as regards the balance of payments and prices. There was, however, an increase in current expenditure, while investment showed a substantial decline. Moreover, this expenditure was concentrated in the second half of the year and accelerated in the first few months of 1970.

If this rate of expansion were to continue, overall domestic demand, in monetary terms, would increase in 1970 to an extent far in excess of the possibilities of adjustment of supply, leading to price rises much larger than the maximum which has on many occasions been stated to be acceptable.

The price system is passing through a phase of marked strains. The prices of manufactured goods have already been discussed; in March wholesale prices were 9.1 per cent higher than a year earlier, which represents an average increase of 6.3 per cent for the year even if they were to remain unchanged for the rest of 1970; but the trend is still upwards. The rise in prices for capital goods has been particularly sharp; in March the cost of a residential building was 20.9 per cent above the value twelve months earlier. The increase in prices for machinery and equipment was also pronounced, this being a phenomenon common to the main international markets, which confirms how phases of overheating mainly affect capital goods, owing to both the greater variability of demand and the structure of supply, which is increasingly characterised by a high degree of specialisation. The price rise is less marked in the case of consumer goods, the index of which in March was 5.0 per cent higher than twelve months earlier.

The anxieties due to this state of tension, present and expected, cannot be allayed merely by the knowledge that it fits into an inflationary international context. In this connection it should be recalled that, although it has become customary, in considering the price policies pursued by enterprises, to relate them to the changes in prices in competing countries and although, for the economy as a whole, the idea

of relative stability has now become commonplace, this concept being understood as the acceptance of an inflationary component provided that it remains within limits not exceeding the average in other countries, this does not mean that this idea can be regarded as a valid standard for any rate of price variation. Its observance could avoid balance of payments disequilibria, but it does not solve, within the country, the no less serious disequilibria which a large rise in prices creates in the distribution of income and in the formation and utilisation of savings.

It is true that in the short term the increase in prices, by improving profit formation, can assist investments; but the price rise produces a far more harmful economic effect, curtailing the purchasing power of fixed incomes earners, creating confusion in savers' preferences with regard to the various financial assets and deranging the channels through which funds flow. The financial system is thus confronted with two categories of difficulties, namely those due to the quantity of funds required in relation to the volume of additional demand and those which the price rise creates in the process of formation and channelling of savings.

It must therefore not be forgotten that we have to compare, at least in the short run, the possibilities offered by the productive system with the demand. The proportions which certain fundamental economic variables will assume in 1970 will be conditioned by events which have already occurred, including, as already mentioned, the expansion of private consumption. But the latter is a limiting factor to which the two other main components of domestic demand, the current expenditure of the public sector and capital investment expenditure, will have to adjust themselves. The fact that the pressure on resources is already excessive is shown by the trend of prices and of the current account of the balance of payments.

In the present circumstances there is therefore an alternative between investment, on the one hand, and public consumption, on the other. A contraction of the former would greatly hamper the pace of future development, with repercussions on employment and the competitiveness of Italian products, and would also mean giving up productivity gains that are necessary in order to neutralise, at least partially, the large increases in labour costs. Already in the 1960s the rise in investment was very low, constituting the most unsatisfactory aspect

of the economic results of the whole decade and contrasting sharply with the development in the 1950s, when the upward trend in investment was appreciably faster than that in income. The fact that, despite this profound difference, the rate of growth of income was nearly the same in the two periods, was possible— apart from the different nature of the effects produced by the application of technological progress— by the very large extent to which advantage was taken of external economies in the more industrialised areas of Italy. Thus, coupled with the task of speeding up the industrialisation of Southern Italy, there is also the urgent need to bring the economic infrastructure up to standard throughout the whole country. It is therefore in the public sector— also owing to the unified direction of its main component, the Government— that the problem of the compatibility between the volume of available resources and the extent of the demand first of all arises, together with that of the assignment to the latter of an order of priority based strictly on the need to remedy the serious lack of infrastructure.

It may happen, however — and it seems far from improbable— that notwithstanding the gravity of the situation the necessary sense of proportion will be lacking owing to ever-increasing pressures from all sectors. Even in the last few months the Treasury, on which the financial repercussions of these pressures ultimately converge, has been assuming sole responsibility for the creation of new monetary base, although this appears for the moment to be partly due to making up for enforced suspensions of operations at the end of last year. If the growth in public expenditure could not be restrained, it would be difficult to avoid a worsening of the tensions which are at present hampering the re-establishment of real and financial equilibrium; these tensions are already going beyond the limits envisaged at the beginning of the year, which were themselves wide but in a way accepted as being inevitable and in the long run regarded as capable of being offset by future increases in production.

Prices have reached higher levels than were expected; demand for credit remains high, although its cost is rising, pushed up by investment requirements the volume of which is being increasingly influenced by the nominal component, and for which cover is increasingly being sought in sources of finance outside the enterprises concerned;

and there is continually growing demand for funds on the market for fixed-interest securities. In these circumstances it is extremely difficult for the responsible authorities to maintain control over the volume of credit, when it is left to this alone the task of regulating demand. There is an urgent need for this to be reinforced by an effective budgetary policy which, in awareness of the limits to be observed with regard to public indebtedness and of the consequences which would result for monetary equilibrium if these limits were exceeded, takes steps to spread out over time the actual expenditures, both old and new, and to ensure that they are financed in the most suitable ways, by resorting without hesitation to taxation in ways which do not hamper savings formation.

The most subtle instruments of monetary policy cannot protect the economy from the inflationary pressures that derive from public expenditure which, at all levels, tends to expand, is implemented with increasing delay, and in most cases has a destabilising effect. If the national and local communities, via their representative bodies, refuse to co-ordinate their demands for social services with the volume of available resources, and if the provision of these services continues to be characterised by inefficiency and waste, the harsh necessity will arise of enduring that most inequitable of all taxes, that is, inflation.

We ought all to remember the admonition which Luigi Einaudi gave in this same place at a difficult time which our country had to endure and overcome: « at the end of the road which, by expediency and desire of popularity, we are induced to travel— he said— lies the abyss of destruction of the monetary unit and social chaos ». And he concluded: he who gives these warnings also wishes « to proclaim aloud the certainty that, if we will it, we ourselves shall not travel along that road ».

Gentlemen,

Our meetings in this hall take place at regular intervals of time, but although nothing changes in their formal setting, to which tradition imparts value and warmth, the document which is now presented to you here contains evidence of an evolution which is not superficial. We have no intention of opposing it, and it would be foolish and

vain to attempt to do so. If anything, we are anxious that this evolution may not always be assisted, as we would wish, to the extent and in the ways which technical progress and the world around us clearly demand. These hopes seem to have a counterpart in the refinement of the research and analysis to which, not unprofitably, the group which drafts this Report devotes its efforts; but it is becoming steadily less easy, and less appropriate, to give a uniform account, if that is expected of us, of all the major happenings of the twelve months under review; this is prevented not only by the rapid and crowded succession of events and their intricate interrelationships but also by the primary need to throw light on the ideas, developments and trends which appear to be of more than ephemeral significance. Only a misplaced desire for originality could induce us to avert our attention from the phenomena which, it is widely agreed, are characteristic features of our time: either from the essentially economic matters which we endeavour to illustrate in the analytical part of the Report or from others, further from our field, on which we sometimes briefly touch in these Concluding Remarks because they seem to indicate the directions in which we are moving and could not with impunity be ignored.

For it has in fact been said that the choice nowadays is not between changing and not changing but between changing deliberately and letting ourselves be changed. If we do not reject the validity of this alternative, there follows the necessity of timely and constant participation in the far-reaching changes which are in progress and take place not by slow transition but sharply concentrated in time and thus often convulsively and with traumatic effects. Careful observation can avail itself of the aid of new and ancient sciences to obtain insights into the body of society in order to reveal the presence and nature of the processes which are establishing themselves in it and enable us to deduce, from the diagnosis, an indication of the appropriate methods of treatment. It is not likely that we shall otherwise be able to prevent disorderly and tumultuous pathological processes, in the face of which, once they have broken out, the choice seems to be confined to unfelicitous reactions—a description equally applicable both to violent repression and to belated adaptation—the last of which, by its probable irrationality and inadequacy, can hardly be expected to avoid further enforced adaptations.

But we should not venture to embark, even for a brief incursion, on a field in which the seed of philosophical speculation has already been widely sown and which, in the world, is seen to be furrowed in all directions by the implements of political action, if our country were not one of the many in which the instability of the environmental conditions combines with basic inadequacies to retard, if not to threaten, the birth and ripening of many hoped-for fruits; and, above all, if certain of these inadequacies did not lead us back into the economic sphere, presenting again to our joint attention problems which for the most part are not new but whose solution cannot be indefinitely deferred nor left to be provided by fortuitous and unforeseeable developments: for without active and prompt participation we should expose ourselves to the risks, and indeed the consequences, which we have described.

This purpose of guidance is required first of all where it can also be most fully performed, namely within a community. In our country it is still required, and with renewed intensity, for the correction of territorial and sectoral imbalances no less than for the creation of the conditions necessary for economic growth and social progress, when these are wholly or partly lacking. It is needed, to —to mention only the major tasks— in view of the choices which constitute the logical prerequisite and inevitable limit of planning, and in view of the vexed boundary line which must be observed by trade union claims within the framework of an incomes policy.

It is quite natural that in a world so rich in communications and competition many problems do not remain confined within a narrow geographical area; and we would certainly not regret this, even though the possible solutions and their modes of implementation will have to suffer the tempering effect of other sovereign wills and other interests, or just of different system. An undeniable positive effect, even for those who look askance at this permeability, this osmosis, and thus also these interdependences between nations, lies in the fact that they reveal situations calling for correction or alleviation to which they may be susceptible; such as when an unsatisfactory combination of the factors of production leads to losses of capital and labour, both attracted by more favourable prospects of employment and remuneration.

The view may be further widened to include the external relationships of a fragmented Europe for which the only way to avoid allowing itself to be changed is by finding the strength to overcome irrational ideological allurements, thus achieving, in its larger, integrated form, in which disillusioned Europeans hardly still dare to place their hopes, those formal and technical changes which would enable it to hold its own.

This is a task which we all, in different ways, are in duty bound to shoulder if, while not rejecting the past, we are to make Italy and Europe into the land of our future; a task which requires that we should overcome the human fear of change, of transformations, and acquire the conviction that well-conceived changes, rational transformations are essential and urgent if we wish to approach that ideal state of society in which preservation of natural assets is coupled with wider sharing of the fruits of production.

In this respect, too, we must not allow time to pass by without imprinting on it the mark of our constructive will.

IV. – The banks' capital and reserves

Under agreements concluded between the representatives of the Italian and Libyan Governments, 251 shares in the Bank of Italy's capital held by the Libyan Savings Bank (Cassa di risparmio della Libia) were made available. With the approval of the Board of Directors, these shares were sold to Italian institutions of the same type, according to a principle which made it possible to increase to one hundred shares, conferring voting right, the holding of those savings banks which, although shareholders, had not previously had a vote, and to distribute the remainder among all the savings bank and first-classe loan offices which previously had no shares.

On 31st December the distribution of shares was as follows:

Shareholders with voting rights:

Savings banks and loan offices	76	with	177,896	shares and	471	votes
Public-law credit institutions	8	»	54,500	»	»	141 »
Banks of national interest	. 3	»	21,000	»	»	54 »
Social insurance funds	. . 1	»	15,000	»	»	34 »
Insurance companies	. . . 9	»	31,500	»	»	99 »
97 with 299,896 shares and 799 votes						

Shareholders without voting right:

Savings banks and loan offices	<u>14</u>	with	<u>104</u>	shares
Total:	<u>111</u>	with	<u>300,000</u>	shares

Compared with the end of 1968 there were 12 more shareholders, including four with voting rights.

In 1969 the ordinary and extraordinary reserves underwent the following changes:

	Ordinary reserve fund	Extraordinary reserve fund
Amount on 31st Decem- ber 1968	Lit. 9,239,754,963	Lit. 6,392,715,272
plus:		
– allocation from profits for 1968	» 194,271,092	» 194,271,092
– income received in 1969 from investment of reserves	» 794,518,587	» 813,003,497
	<u>Lit. 10,228,544,642</u>	<u>Lit. 7,399,989,861</u>
less:		
– distribution to share- holders of a part of the income accruing in the course of 1968 (Arti- cle 56 of the Statute)	<u>Lit. 76,044,000</u>	<u>Lit. 49,956,000</u>
Amount on 31st Decem- ber 1969	<u><u>Lit. 10,152,500,642</u></u>	<u><u>Lit. 7,350,033,861</u></u>

**V. – BALANCE SHEET
AND PROFIT AND LOSS ACCOUNT**

BALANCE SHEET AS

A S S E T S		
Gold	L.	1,847,451,250,622
Cash in hand	»	39,631,812,752
Domestic bills of exchange	»	1,652,507,460,599
Bills for collection	»	384,406,187
Advances	»	1,643,548,832,902
Italian Exchange Office current account	»	1,626,186,437,748
Government or Government-guaranteed securities	»	2,446,565,655,692
Premises	»	1
Miscellaneous debtors	»	680,527,456,208
Advances to the Treasury: extraordinary	»	339,000,000,000
Miscellaneous services for account of Government	»	137,642,331,217
		L.
Securities and other valuables deposited	»	10,413,445,643,928
		L.
Items written off in past years	»	21,791,858,354,498
		1,972,264,216
GRAND TOTAL		L.
		21,793,830,618,714

Audited and found correct. — Rome, 12th May, 1970

THE AUDITORS

DOMENICO AMODEO
ALBERTO CAMPOLONGO
RAFFAELE D'ADDARIO
BRUNO DE MORI
GIUSEPPE GUARINO

THE ACCOUNTANT GENERAL

ARMANDO PESCATORE

AT 31st DECEMBER, 1969

SEVENTY-FOURTH YEAR

LIABILITIES

[illegible]

THE GOVERNOR

GUIDO CARLI

GENERAL PROFIT FOR THE

EXPENDITURE		
Administration	L.	66,575,440,886
Emoluments of Directors, etc.	»	353,493,525
Transport of notes, coin and other valuables	»	138,966,030
Note printing	»	3,203,726,824
Expenditure on premises	»	1,013,592,713
		71,285,219,978
Circulation tax on notes and demand drafts	L.	14,810,513,200
Income and corporation taxes	»	23,000,000,000
Sundry taxes and dues	»	4,030,068,095
		41,840,581,295
Amounts written off	L.	82,787,591,777
Interest payable	»	33,625,321,789
Charities and other contributions	»	250,266,513
		L. 229,788,981,352
Net profit for distribution	»	6,400,718,444
TOTAL		L. 236,189,699,796

APPROPRIATION

To ordinary reserve	
To extraordinary reserve	
To shareholders	
To the Government	
TOTAL	

Audited and found correct. — Rome, 12th May, 1970.

THE AUDITORS

DOMENICO AMODEO
ALBERTO CAMPOLONGO
RAFFAELE D'ADDARIO
BRUNO DE MORI
GIUSEPPE GUARINO

THE ACCOUNTANT GENERAL

ARMANDO PESCATORE

AND LOSS ACCOUNT

YEAR 1969

RECEIPTS		
Discounts	L.	47,275,349,852
Interest on advances	»	45,323,583,296
Interest on other assets	»	58,204,623,540
Commissions and custody fees	»	2,981,536,533
Profits on foreign transactions	»	682,047,475
Sundry profits	»	13,172,013,478
		167,639,154,174
Interest on Government securities	L.	68,271,923,698
Revenue from real estate	»	278,621,924
		68,550,545,622
TOTAL L.		236,189,699,796

OF PROFIT

.	L.	1,280,143,689
.	»	1,280,143,689
.	»	30,000,000
.	»	3,810,431,066
DISPOSABLE PROFIT	L.	6,400,718,444

THE GOVERNOR

GUIDO CARLI

ADMINISTRATION OF THE BANK OF ITALY

AS AT 31st DECEMBER, 1969

BOARD OF DIRECTORS

Guido CARLI * - GOVERNOR AND CHAIRMAN OF THE BOARD
Paolo BAFFI * - GENERAL MANAGER
Rinaldo OSSOLA - DEPUTY GENERAL MANAGER
Antonino OCCHIUTO - DEPUTY GENERAL MANAGER AND SECRETARY TO THE BOARD

DIRECTORS

Guido BORSELLINO CASTELLANA	Antonio FONDA SAVIO *
Gaetano CARBONE *	Paolo MONICO
Umberto CARUSO *	Lucio MORODER
Carlo D'AMELIO	Remo MORONE
Giovanni Battista DEL BALZO	Giambattista PARODI *
Danilo DE MICHELI	Giovanni POGGI
Luigi FANTOLA	

* Member of the Executive Committee.

BOARD OF AUDITORS

Domenico AMODEO	Bruno DE MORI
Alberto CAMPOLONGO	Giuseppe GUARINO
Raffaele D'ADDARIO	

ALTERNATE AUDITORS

Michele BENEDETTI	Antonio CONFALONIERI
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CENTRAL ADMINISTRATION

MANAGERS

Corrado PIROVINE	Paolo BISERNI
Alfredo VERNUCCI *	Luca ROSANIA
Guido RUTA	Giovanni SANTOPONTE
Francesco MASERA	Armando PESCATORE
Felice FRASCA	Renato DE MATTIA

* Manager of the Italian Exchange Office.

