BANCA D'ITALIA

ABRIDGED VERSION OF THE

REPORT

FOR THE YEAR

1972

PRESENTED BY THE GOVERNOR TO THE

ORDINARY GENERAL MEETING OF SHAREHOLDERS

HELD IN ROME ON MAY 30, 1973

ROME

PRINTING OFFICE OF THE BANCA D'ITALIA

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Problems and prospects

The realignment of exchange rates for the major currencies agreed upon in Washington in December 1971 was not able to put international monetary relations on to a solid footing. Persistent commercial imbalances and the massive dollar overhang continued to feed speculative pressures, requiring continuous interventions on the official exchange markets and restrictions on capital flows. In early 1973, the flood of speculative flows took on extreme crisis proportions, culminating in the second dollar devaluation in 14 months and the floating of the major industrialized countries' currencies.

Recent experience has verified that the solution to problems stemming from payments disequilibria cannot be reached exclusively through a realignment of parities and once again posed, in all its urgency, the problem of reforming the international monetary system and the rules which govern world trade. In 1972 the disequilibria in trade balances widened in respect to the previous year: the deficit of the United States climbed from 2.7 to 6.8 billion dollars, the surplus of Germany from 6.6 to 8.3 and that of Japan by 7.9 to 9.0 billion.

After the fall-off registered in the preceding year, in 1972 US exports expanded considerably in volume; there was however no accompanying drop in imports but, in fact, an increase, so that the worsening of the terms of trade contributed towards exacerbating the trade balance disequilibria. The factors underlying this development can be partially traced to the lack of synchrony in economic recovery, which in the United States occurred ahead of and to a greater extent than in its main competitors and was fostered by an expansionary monetary policy which that country set out upon in 1971. Import performance was also affected by the attitude of exporters in several countries whose currencies were devalued vis-à-vis the dollar. These businessmen, in order not to lose that portion of the US market they had managed to capture, did not raise their export prices as much as expected. The problem of curbing US imports seems, in addition, to be hindered by their low elasticity in respect to price swings. This latter phenomenon is partially justified by the United States' growing dependence on foreign suppliers for raw material needs, especially for oil.

Another anticipated upshot of the Smithsonian agreements was that the large sum of dollars that had been sent abroad during the monetary crisis of 1971 was expected to flow back to the United States. Nonetheless this only took place to a minor extent — even in the presence, up to autumn 1972, of market conditions favourable to such a reflow as interest rates in Europe remained below those in the United States — reflecting the vaster problem of confidence in the exchange rates structure resulting from the agreements. As a matter of fact, recurrent conditions of instability on foreign exchange markets generated additional outflows of funds from the United States.

The fact that the reflow of funds towards the United States did not take place brings once again to the fore the problem of regulating capital flows and finding a solution which, while preserving the benefits of liberalization, shelters at the same time the system from speculative attacks. Different standpoints have emerged on this question: on the European side the call is for measures which affect the capital account of the balance of payments; while the Americans favour adjustments in the current account sector, even through changes in exchange rates, in order not to hamper the free flow of capital. This latter position was made clear both at the time the dollar was devalued and during later meetings of the Group of Ten, when the United States stated its desire to eliminate controls on capital outflows by the end of 1974. At that date the problem of capital flows will resurface in all its gravity if in the meantime measures have not been taken to reabsorb the bulk of dollars in circulation created by past and present US deficits.

The problem of controlling capital flows is, in addition, linked to that of regulating the Eurodollar market. It has already been noted in last year's Report how the institutional features of this market are such as to allow for an autonomous process of deposit creation that, in the absence of controls, makes the economies of the single countries particularly vulnerable, both because the Euromarket represents a transmission belt between the United States and Europe for monetary turmoil and because it abets speculative attitudes, providing those active on exchange markets with the necessary financial resources. For these reasons, numerous quarters have requested that the introduction of appropriate controls on the Euromarket take place with the cooperation of the United States and take into account the probable reactions of those operating on it. More specifically the need was felt to study the behaviour of the multinational corporations and the role they played in the recent crises.

The process of European economic and monetary unification saw, during the course of 1972, the setting up of provisions narrowing the fluctuation margins among the European currencies. Nevertheless this agreement quickly displayed its functional limitations, even becoming itself an element of instability in the system. Besides its functional rigidity from the technical standpoint, owing to the necessity of intervening as a rule at the margins and not inside them — providing the central banks little elbow room for defending against speculative manoeuvres — at the root of the unsatisfactory outcome was the particular cumbersomeness of intra-Community regulations. In fact, while these required that the settlement of credit and debit positions take place in the various reserve instruments, in the proportion in which they are held in the debtor's reserves, the settlement of debts in international relationships could, as always, be carried out in dollars.

This rule, introduced with the intention of fostering a gradual harmonization of the reserves of the Community countries, soon proved unworkable because of the large spread between the official price of gold and its quotation on the free market. At the time that the agreement on margins was negotiated, that spread was not so large: afterwards, the yellow metal's price on the free market swung sharply upward, fed by a growing speculative demand associated in the course of 1972 with a temporary drop in supply, until reaching recently a price nearly triple the one that was quoted in August 1971. The result was the freezing of gold in the coffers of the central banks as a non-reconstitutable means of payments or, for intra-Community settlements, only a partially reconstitutable one.

The fragility of the intervention system and of the settlement of intra-Community debtor positions became clear in June, when the United Kingdom decided to dissociate itself from the agreement on margins in order to avoid losing reserves or going once again into debt just when it had finished repaying former loans, and later when Italy was allowed to intervene in dollars to defend the lira's exchange rate within the Community band.

Even the improvements made on the agreement at the end of the year, which permitted all the participating countries to intervene in Community currencies inside the margins and which furnished a temporary solution to the problem of gold in intra-Community settlements, did not succeed in dampening the indirect effects of the speculative attacks on the dollar at the start of 1973 that eventually resulted in the floating of the lira and the revaluation of the Deutschemark.

International trade grew in 1972 by 17 per cent as against 12 per cent in the previous year. The speed-up mainly reflects the rise in unit export prices stemming from the dollar's first devaluation and the inflationary pressures present in most economies. In quantity, the increase of world trade was equal to 8 per cent in 1972 versus the exceptionally low gain of 5.5 per cent that took place in 1971. In both years, these growth rates were only slightly higher than those of world output, in contrast to what occurred in the period 1967-1970, when the former was on average about twice as high as the latter. The comparison between the two periods gives an indication of how the monetary instability of the last few years has contributed to the slowdown in the growth of world trade.

The growth rate of the gross national product of the industrial countries was higher in 1972 than the average during the 1960's. This improvement can be linked in large measure to the results obtained in the non-European countries, and especially in the United States, which recovered fully from the recessional phase beginning in 1970. For the European countries, which a year after the United States also went into a period of cyclical weakness, the turnaround was less vigorous. In most of these countries the increase in GNP, though higher than in the previous year, was below respective medium-term averages.

These developments took place while consumer prices were showing contrasting behaviours: in the European countries growth rates either picked up steam or stayed on the high levels of 1971, while in Japan and in the United States they continued to fall. Nonetheless, by the end of the year and the early months of 1973, nearly all the industrial economies were commonly experiencing a sharp swelling of inflationary pressures. The main factor in this development is the greater leeway, in a year of increasing domestic demand such as 1972, to tack onto prices the rises registered in output costs. To this can be added the dropping, or the easing, in several countries of price and wage control measures enacted in the preceding two-year period.

To fight the renewed inflationary pressures, recourse was made towards the end of the year to a less expansionary monetary policy, which in several countries was even made restrictive by increasing the discount rate and compulsory reserves. The effectiveness of the monetary instrument has nonetheless been hampered by the obbligation to maintain, in the presence of massive flows of speculative capital, the agreed exchange rates.

In order to neutralize the negative impact on investments and employment of moves, aimed at holding down prices, relying strictly on monetary manoeuvres, in some countries in 1972 the authorities introduced incomes policy measures, ranging from freezing prices and wages to attempts to control these through agreements with employers and trade union representatives. Policy-makers turned to the first form as an emergency measure, in order to allow a breathing space for implementing more complete stabilization programmes, as well as to influence public opinion and contribute to dispelling by this means the inflationary psychology. The freeze on prices and wages, nevertheless, was only enacted for short periods of time, as a temporary measure before shifting over to programmes of a voluntary nature. The statistical results on the performance of prices do not make it possible to come up with a clearcut evaluation of the effectiveness of incomes policies. Without doubt the United States registered positive results, nevertheless there was a sharp increase in inflationary pressures when the second phase of the stabilization programme, introduced in 1971, was moved into the third phase, characterized by less rigid control forms.

The extent and proportions of the inflationary phenomenon have led the Economic Policy Committee of the OECD to recommend that its member countries take anti-inflationary measures. More specifically, the member countries of the European Economic Community have jointly set the target of slowing the rate of increase of prices down to 4 per cent by the end of 1973, envisaging in addition to the recourse to monetary, fiscal and incomes policies, a series of measures aimed at eliminating the imbalances existing in manpower distribution, temporarily reducing the tariffs and quotas on imports, intensifying the fight against the process of industrial concentration and monopoly positions and keeping the lid on rising food prices.

However, the joint action against rising prices comes at a time when the member countries are out of step cyclically and utilizing available resources to different degrees. In those countries where utilization rates are lower it is more difficult to line up with a common anti-inflationary policy, since the authorities must fight simultaneously against inflation and recession. Within the sphere of the EEC, Italy and the United Kingdom have the highest rate of unemployment and are the countries where industrial investments during the 1964-1970 period were carried out at the slowest pace. Since the second half of 1969, our country has gone through a phase marked by a sluggish rate of expansion, comparable only to the situation in the United Kingdom, where, moreover, growth at a snail's pace has lasted much longer. In that country, carrying out an expansionary policy meets relatively steeper hurdles because of a higher propensity for inflation, as well as because of persistent deficits in the trade balance. Freedom from a fixed exchange rate parity has allowed the United Kingdom to accomplish in 1972 a growth rate in the GNP higher than that of the preceding year.

Through the agreement to narrow fluctuation margins, it was also intended to make economic policies converge towards common objectives in order to eliminate disparities at the root of balance-of-payments disequilibria and thus move nearer economic unification. However, the fact that the agreement was not accompanied by the other measures vital to integration, not only did not further progress but actually resulted in a step backwards, since to eliminate the disruptions caused by the agreement it was necessary to implement decisions on a national level that ran counter to the unification process.

One of the main measures necessary in order to achieve unification is the gradual pooling of reserves as a first step towards an automatic system of credit facilities with the adequate resources and duration to make possible a stabilization policy aimed at defending the fluctuation margins and countering the perverse effects of speculative capital movements. Along these lines, during April this year the European Fund for Monetary Cooperation was set up. Although its initial tasks are limited, it provides the basis for setting up a European central banking system and for making external relations a Community responsibility.

A fundamental contribution to the European integration process could be made by creating a unified capital market, characterized, among other things, by common legislation for joint-stock companies and stock exchanges as well as a homogeneous tax system.

Another feature could be more energetic Community action to aid the most handicapped regions, thereby paving the way for launching or intensifying the industrialization process in these areas. Up to this date no decision has yet been taken to begin solving regional problems: general agreements reached at the Summit meeting of EEC heads of State or Government, held in Paris last October, concern FEOGA (European Agricultural Fund) interventions in the sector and the setting up of a Regional Development Fund.

The free floating of certain European currencies confirms that at present the process of harmonizing cyclical developments can only be pursued by allowing limited exchange rate flexibility in intra-Community monetary relations, able to offset and correct differences in cost and price trends.

The crisis of the first quarter of 1973 forced the Community member countries to choose between giving unlimited and unconditioned support to the dollar or accepting a gradual rise in their currencies' relative value, amounting to a loss of competitiveness vis-à-vis the rest of the world. In making their choice they have had to take into account the fact that the European countries' economies are not fully integrated and that, consequently, the Community has not been able to take up a common stance in foreign relations.

Reform of the international monetary system and revision of the present trade policies of the various countries represent the long-term commitment resulting from the Smithsonian agreements. Negotiations on monetary problems were begun in 1972 when the International Monetary Fund set up an *ad hoc* body, the so-called Committee of Twenty; trade negotiations will begin next autumn within the framework of GATT.

The basic problems to be solved concern first the need to make sure that, in the future, balance-of-payments disequilibria are promptly corrected through adequate adjustment measures. Therefore, better and more timely use of demand regulation policies should be made to go hand in hand with more efficient use of the exchange rate mechanism.

In the second place, an efficient international monetary system should be capable of creating an adequate volume of international liquidity to meet payment needs: hence the necessity to deliberate on the problem of future reserves composition and, in particular, to define the role of special drawing rights, gold and reserve currencies. With regard to the latter, the problem of the vast bulk of dollars presently in circulation has again arisen, along with that of the dangers this presents to the system's stability and, hence, of finding some form of consolidation.

Moreover, the stability of the international monetary system requires measures capable of reducing or eliminating the destabilizing effects of short-term capital movements without hindering international transactions. Finally, the new system must give greater importance to the problems of the Third World countries, especially with regard to finding solutions for increasing the flow of real resources towards the nations grouped under this heading.

The system of exchange rate relations which grew out of the Group of Ten's decisions of March last year, with all the European currencies (some jointly and others independently) and the yen freely floating against the dollar, does not as yet ensure the conditions of stability and lack of speculation necessary to keep reform negotiations moving ahead.

Continuous changes are taking place in the international monetary system at a pace which reform negotiations, because of still existing radical differences of opinion, do not seem able to keep abreast of. In such a situation, and after a fairly positive experience of floating, the introduction of flexible exchange rate relations among currency areas having basically fixed internal exchange rates, would seem one instrument for achieving the above-mentioned aims. On condition, however, that on one hand the countries abide by a good conduct code providing continuity and new vitality to international monetary cooperation and ensuring that the IMF receives the necessary instruments to keep floating exchange rates from setting off a scramble for competitive advantages or turmoil on the currency markets, and on the other hand, that the integration process within the areas involved takes place in such a way that the internal system of fixed exchange rates reflects the basic homogeneity of economic conditions in countries within the area.

The problems facing the delegates in future trade negotiations vary considerably from those tackled and partly dealt with in the 1967 Kennedy Round. Although the general reduction of tariffs, the major achievement of the Kennedy Round, was a considerable step towards liberalizing world trade, this instrument was neither efficient enough nor sufficient to regulate international relations.

The enlargement and strengthening of economic blocks and the growing awareness of the inter-relationship between monetary and trade phenomena, stress the need for coming up with overall solutions which are not merely limited to removing existing obstacles to trade but attempt to reconcile the economic and political objectives which the single countries intend to pursue. Accomplishing such solutions is all the more pressing since the alternative would be an involution of trade relations, the first symptoms of which are already looming on the horizon and gaining force in protectionist attitudes, especially within the United States. Were this to happen, the crises which so far have only affected the monetary system would eventually spill over into the entire network of international economic relations.

Cyclical developments, economic policies and financial markets

In 1972 international economic activity was characterized by a sustained upswing in nearly all the major industrialized countries — even if not always occurring in synchrony or with equal vigour — and by the speeding up of inflationary forces towards the end of the year. The monetary realignment of December 1971, permitting a new round of expansion in world trade, played a positive role in the turnaround, but did not lead during the course of the year towards accomplishing the envisaged process of adjustment. Trade and payments disequilibria continued to widen, provoking at the start of 1973 a new monetary crisis, which culminated in the 10 per cent devaluation of the dollar and in the revaluation of the Deutschemark by 3 per cent (vis-à-vis special drawing rights and gold) and in the joint float of the EEC currencies, with the exception of the lira and the pound sterling which were allowed to float freely as were the Swiss franc and the yen.

The recovery of the US economy, starting in the second half of 1971, picked up speed throughout 1972, resulting in a rise in the growth rate in real terms of 6.5 per cent versus 2.7 in 1971. In France overall demand continued to expand strongly for the fourth year running. In nearly all the other industrial countries, on the other hand, recovery took place only in the second half of the year and was especially intense in the fourth quarter in Japan, West Germany and the United Kingdom, a country where stagnant domestic demand had been entrenched for some three years. Investments in plants and equipment represented the most dynamic demand factor in France and the United States, where they increased by 13.5 per cent at constant prices in respect to 1971. In the other countries, expansive thrust was mainly provided by private consumption. In addition there was an appreciable expansion in exports of goods and services in West Germany (mainly in the second half the year) and in investments for dwellings in Japan and the Netherlands.

Unemployment, nonetheless, grew in all the industrial countries, with the exception of the United States and Canada; however, towards the end of 1972 and the beginning of this year the seasonally adjusted rate of unemployment began to ease downwards in line with the renewed productive vigour.

In the manufacturing sector, the upturn in output, together with the further reduction of manpower hours, were translated into an appreciable rise in productivity. Combined with a more limited rise in pay scales over the course of the year, actual wages per unit of output fell off considerably. In spite of this, almost everywhere the growth rate of wholesale prices was higher than in 1971, demonstrating that changes in costs are not automatically transmitted to prices, as the enterprises seem to follow criteria based on long-term considerations and in setting prices mainly take into consideration present demand conditions and prospects.

Given the hefty increase in prices for foodstuffs (on average more than 10 per cent in the industrial countries) and for raw materials, the general index of wholesale prices rose even faster than that for manufactured goods. The latter spurted particularly towards the end of the year, gaining momentum as the calendar turned in every country, even in those like the United Kingdom and West Germany, where its expansion in 1972 was at a lower rate than in 1971 (Table 1).

TABLE 1

DEVELOPMENT OF WHOLESALE PRICES IN THE MAIN INDUSTRIAL COUNTRIES IN 1972 AND THE 1st QUARTER OF 1973 (1)

(percentage variat. on a yearly basis: a - *June 72/Dec. 71;* b - *Dec. 72/June 72;* c - *March 73/Dec.72)*

Countries	Foodstuffs			Raw industrials			Manufactured products			Total		
	a	b	c	a	b	c	a	b	c	a	b	c
Italy	2.9	16.7	23.6	7.8	12.4	62.3	3,4	6.9	12.4	4.0	10.3	22.3
France	8.2	19.4	15.6	2.2	16.6	44.4	5.2	11.2	15.6	5.2	13.8	21.3
West Germany	12.0	14.8	16.4	1.6	11.8	16.4	4.2	4.2	11.2	5.6	6.4	13.6
United Kingdom	..	..	..	4.2	22.0	31.2	7.3	7.6	5.2	..	..	..
United States	14.2	21.8	68.0	10.4	10.8	60.0	3.4	4.4	16.4	5.8	7.0	22.0
Japan	3.8	7.0	17.6	0.4	25.4	31.2	1.6	8.8	15.4	1.4	10.4	19.2

Source: OECD, Main Economic Indicators; National Bulletins.

(1) Provisional and partly estimated data for the 1st qr. 1973 (owing to the introduction of VAT, for Italy the variations refer to the difference between March and January).

In spite of the end-1971 monetary realignment, the disequilibria in trade and in the current account section of the balance of payments between the major countries showing a surplus (Japan and West Germany) and the United States widened even further (Table 2). The US deficit on current account rose by 2.8 to nearly 8 billion dollars, as a result of the substantial increase in the trade balance deficit, which grew from 2.7 to 6.8 billion dollars. More than half of this deficit occurred vis-à-vis Japan whose already ponderous surplus on current account further swelled, this time by 1 billion dollars (its trade surplus rose from 8 to 9 billion).

The economic recovery was accompanied by a general upswing in the flow of goods from country to country. The changes in exchange rates of the currencies of the main industrial countries, resulting from the monetary realignment of December 1971, make it difficult to give an exact estimate of the growth rate for international trade in real terms, nonetheless the main factors point to a growth of about 7 per cent, considerably higher, that is, than the exceptionally low figure registered in 1971 (5.5).

In any case, however, it now appears that the trend for the international movement of goods is less buoyant than it was, on average, dur-

Table 2

BALANCES OF PAYMENTS OF THE GROUP OF TEN COUNTRIES AND OF SWITZERLAND

(millions of dollars)

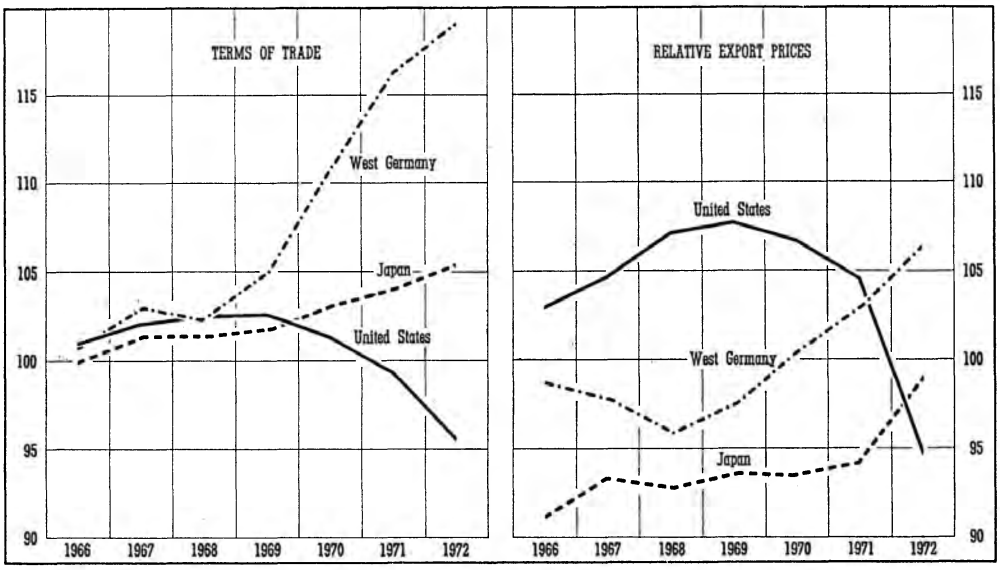
Items	EEC countries	United Kingdom	United States	Japan	Switzerland and other countries	Total
			1971			
Current account	3,018	2,594	- 2,824	5,874	664	9,326
goods (fob)	*7,210*	*782*	*- 2,666*	*7,897*	*1,195*	*14,418*
services	*170*	*2,340*	*3,416*	*- 1,763*	*- 197*	*3,966*
transfers	*- 4,362*	*- 528*	*- 3,574*	*- 260*	*- 334*	*- 9,058*
Capital movements	2,497	- 1,805	- 7,542	- 73	- 1,038	- 7,961
Errors and omissions	2,798	859	-11,052	1,876	2,273	- 3,246
Balance (1)	8,313	1,648	-21,418	7,677	1,899	- 1,881
			1972			
Current account	4,520	44	- 7,983	6,722	- 239	3,064
goods (fob)	*9,767*	*- 1,700*	*- 6,816*	*9,021*	*448*	*10,720*
services	*24*	*2,279*	*2,598*	*- 1,831*	*- 209*	*2,861*
transfers	*- 5,271*	*- 535*	*- 3,765*	*- 468*	*- 478*	*10,517*
Capital movements	- 1,803	1,241	- 1,770	- 2,365	25	- 4,672
Errors and omissions	2,762	- 1,400	- 3,807	384	1,192	- 869
Balance (1)	5,479	- 115	-13,560	4,741	978	- 2,477

Source: Bank for International Settlements and national sources.

(1) To ensure uniformity, balance-of-payments figures have been calculated net of all monetary movements. Possible differences, in respect to the single national statements, mainly regard capital movements and errors and omissions.

ing the Sixties. More specifically, whereas during the period 1967-1970, at an average annual growth rate for world output of 5.4 per cent, there was a corresponding average growth rate in volume for world exports of 10.5 per cent, in the last two years the growth rate of international trade has hovered never very far from that of world production. The recurrent monetary crises of the last few years have combined to slow down the expansion of international commerce, on the overall level, although intra-Community trade (not counting the new member countries) has continued to be extremely dynamic, substantiating what is by now a long-term trend.

Chart 1



Terms of trade and relative export prices of the United States, West Germany and Japan

(1963 = 100)

Source: IMF, Internatonal Financial Statistics; UNO, Monthy Bulletin of Statistics.

The causes which during the course of the year determined a worsening of trade imbalances were manifold. First off, consideration must be given to the powerful effects on trade stemming from changes in exchange rate parities. Whereas in the 1966-1969 period the index of the ratio of export prices to import prices revolved around 100 for those countries most active in world merchandise trade (United States, West Germany and Japan), in recent years this ratio has ranged widely in the different countries (Chart 1). In particular, during 1972 the United States' terms of trade appreciably worsened, going from 99.3

to 95.6; in contrast, those of West Germany and Japan further improved, climbing respectively from 116.2 to 119 and from 103.9 to 105.4. Nonetheless, the leads and lags, with which the changes of prices tend to be reflected in the volume of trade, appear more extensive than once thought. This is due also to the fact that the United States, while devaluing the dollar, has continued to pursue an expansionary economic policy, thereby appreciably stimulating imports. In 1972 the United States' wider deficit in trade was for the most part determined by a sizeable boost in imports, mainly of finished products. This therefore seems to corroborate those who noted a low substitution elasticity with domestic output for American imports.

In most of the industrial countries the turnaround in productive activities was fostered by expansionary fiscal and monetary policy in the early part of the year. Starting in the summer, as the recovery gradually gained ground and was accompanied by a swelling of inflationary ground forces, the authorities shifted towards a more restrictive monetary policy, linked in some countries with measures aimed at the direct control of wages and prices.

Several countries introduced restrictive monetary measures with the objective of neutralizing the inflows of funds from abroad. In West Germany the authorities tried to brake these movements by gradually steepening the percentage of compulsory reserves on the bank deposits of non residents and intervening in the foreign debtor position of the non-banking public, forcing these latter to tie up a sum equivalent to 50 per cent of their foreign debts in a non-interest-paying account (Bardepot) at the central bank. At the beginning of this year, on the decision of the monetary authorities (Belgium and the Netherlands) or through agreement among the commercial banks (France and West Germany) negative interest rates were set for the bank deposits of non residents at an annual rate of 10 per cent.

Seeking to curb the inflationary forces, which picked up greater steam towards the end of 1972, other industrial countries (United Kingdom and the Netherlands) following the example of France and the United States, also introduced direct controls on prices and incomes. The United States, for its part, at the end of the second phase of the incomes policy moved over in January of 1973 to a third phase, characterized by looser controls than the second. Within a short time, however, because of the rapid rise in prices for agricultural produce and industrial raw materials, especially petroleum, the authorities were forced to intervene with tighter controls in these sectors.

What took place in 1972 in France and, above all, in the United States seems to confirm the opinion of those who feel that direct controls yield positive results on the development of prices and incomes over the short run and provide a certain breathing spell for resolving contingent difficulties and implementing an economic policy designed for a longer period. A target had been set for an increase in wholesale prices of 2.3 per cent in the United States between December 1971 and the same month of 1972. In reality there was a boost of 3.4 per cent; nonetheless, if the prices of foodstuffs which were not under any control at the production level are deducted, the rate of increase drops to 2.8 per cent. Econometric surveys made in that country would demonstrate that the controls were able to slow down the rise in prices by about 2 per cent. However, the rapid spate of rises as *phase 2* ended seems to indicate that such a policy only temporarily bottled up the inflationary impulses which burst out no sooner had the stopper been loosened and favourable expectations for overall demand panned out.

Foreign and international financial markets

The more stable conditions met in late-1971 on money and financial markets continued into the first months of 1972, imparting a basic steadiness or downward pressure on interest rates. As the year moved on, short-term rates began to rise across a wide front; long-term rates, however, remained practically firm, except in West Germany and in the United Kingdom.

The first hint of tension on the *money market* was provided by the US market, where during the month of February the downward movement bottomed and turned in the other direction in the wake of a growing demand for funds, stemming both from the vigorous expansion of output and the expectation of a future increase in rates in relation to foreseeable rising Treasury indebtedness.

In the second half of the year a further upward push was spurred by the increased supply of government securities and the restrictive tack of monetary policy, carried out mainly through open market operations aimed at absorbing bank liquidity. Thus call money rates and those on three month Treasury bills, albeit still at a level below that of the previous year, soared upward, moving from one December to the next respectively, from 4.1 and 4.0 per cent to 5.3 and 5.1 per cent.

The Eurodollar market reflected patterns on the US money market, though with less upward impetus. The spread between three-month Eurodollar rates and those in the United States narrowed, with sharp increases in July and October, when tensions appeared on the foreign exchange market (Chart 2).

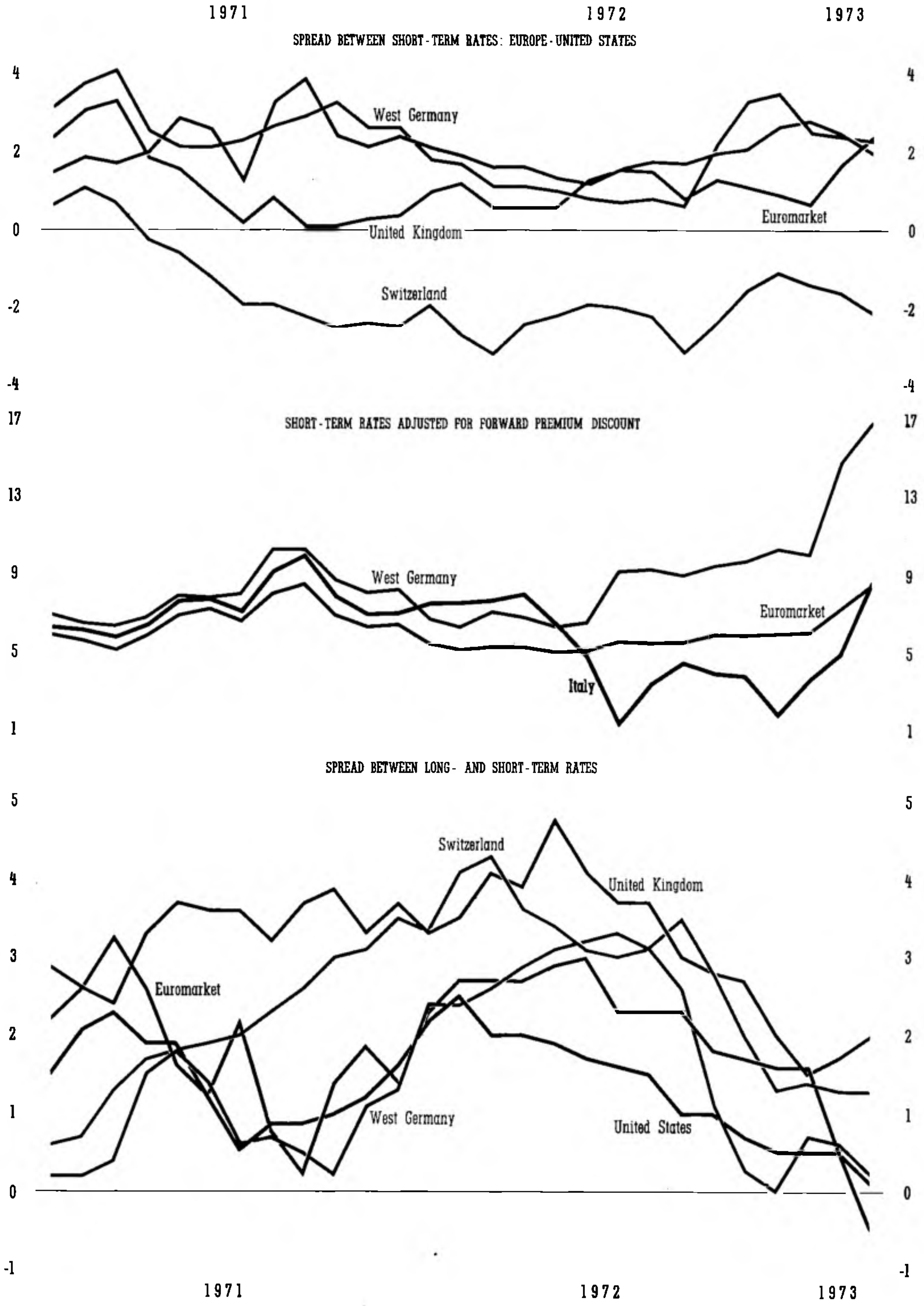
The upward trend of short-term rates in the United States and on the Eurodollar market was soon followed in Switzerland (March) and in the United Kingdom (May). In this last country a buoyant demand for funds in the wake of a surge in productive activity was not matched by supply because of the pound sterling crisis and restrictive measures taken to throttle inflation. As a result the spread between short-term rates in the United Kingdom and the United States widened. The advantage however was not enough to brake the flight from sterling, hampered however by the floating exchange rate.

In the second half of the year the rise in short-term interest rates spread to all of the other European countries under study; namely Belgium, the Netherlands, France and West Germany, whose alignment in the fight against inflation was underlined by the joint decision of the EEC finance ministers in November 1972 to carry out a restrictive monetary policy.

An analysis of money markets, based strictly on interest rates, might produce misleading results owing to the influence of strong institutional factors and to uncertainties in exchange rate relationships.

Last summer's pound sterling crisis, and the speculation against the dollar in its immediate aftermath were reflected in an upward spurt in call money and three-month rates in the United Kingdom and on the Eurodollar market, because of higher indebtedness in those currencies considered weakest and because of the conversions of money market instruments denominated in these currencies. The simultaneous

COMPARISON OF INTEREST RATES IN SOME MARKETS



rush towards the strong currencies of the continental European countries and Japan caused a temporary drop in their call money rates and, to a more limited extent, in their three-month rates.

In West Germany, in particular, three month rates held steady and the spread widened between them and those of assets, with the same maturity, denominated in the weak currencies. Speculative expectations, however, were running high enough to markedly increase the advantage of investing in mark-denominated assets, as is shown by the performance of three-month German rates, adjusted for the premium of the mark against the dollar on the spot market. The rise of the adjusted three-month rate becomes more evident when compared with the opposite change in direction taking place in the same period in the short-term rate in Italy; that is, the return on maturing long-term Treasury bonds, considered an indicator of underlying pressures on our money market.

The February 1973 crisis set off a steep upward rise in Eurodollar rates, closing the gap between these and short-term rates in West Germany and the United Kingdom. The soaring of German short-term rates, suitably adjusted, and the parallel widening of the profit margin for arbitrage provide clear justification for the size of inflows to West Germany. The forward demand for mark-denominated assets was so buoyant that it pushed the rates on Eurodeposits in marks towards negative values, while the three-month rates on Eurodollars hit levels last seen prior to 1971.

The relaxed atmosphere which characterized the *bond markets* in the majority of European countries reflects like conditions in the United States and on the Euromarket, and seems to be attributable to the wide spreads existing between long- and short-term rates, which contributed towards generating expectations of rising short-term rates in the immediate future and rising long-term rates only much farther on, notably, when the gap has narrowed enough to make tempting a sharp shift from long-term to short-term assets (Chart 2).

The analysis of the performance of interest rates in the industrial countries reveals the role played by expectations of changes in exchange rates among the major currencies on international monetary flows. During the first half of the year, while there was still a certain amount of confidence in the stability of the central rates set in December 1971, there was a, albeit slight, reflow of funds back to the United States. For the entire first half of 1972, in the presence of a deficit on current account of 4.2 billion dollars, the official reserve transactions balance came to a deficit of 3.2 billion, versus 11.2 in the same period of 1971.

In Europe, for the January-May period, the bulk of flows once again regarded West Germany's balance of payments. The overall balance of capital flows, including errors and omissions and adjusted for window dressing operations, was unchanged; its components however showed marked changes: namely, the outflow of long-term capital was just about balanced by the inflow of short-term funds.

Since the start of the year, the continuing confidence in the mark and expectations of a temporary drop in long-term rates in West Germany encouraged an increase in portfolio investments by foreigners. With the enactment of the *Bardepot* in the month of March, there was a further increase in purchases of fixed-interest securities. A portion of the foreign funds raised by German enterprises was intermediated by the banking system through the floating of medium-term securities offered for purchase to non residents.

In June the pound sterling crisis undermined the exchange rates of the dollar and lira and spurred new pressures for a revaluation of the mark and yen. The dollar's weakness on exchange markets sparked in the June-July period a new round of outflows from the United States towards West Germany, Switzerland and the Netherlands. In the afore-mentioned two months inflows of capital in West Germany reached 4.8 billion dollars. The purchases of mark-denominated securities and the influx of unidentified funds reached their peak in June and there was also a turnaround in the direct short-term indebtedness of the German enterprises abroad.

At the beginning of July the authorities increased from 40 to 50 the *Bardepot* percentage and made the acquisition of German fixed-interest securities by non residents subject to mandatory authorization. Still more rigorous measures were taken by the Swiss authorities, including severe curbs on foreign investments in the country, including those in real estate. The Netherlands introduced restrictions on the movement of funds by multinational corporations, as well as tighter controls on commercial credits.

The spreading of controls on long-term capital flows, even in countries which up to a short time ago were committed to liberal policies in this field, is an important feature of financial market developments in 1972. During last year and especially up until the introduction of new control measures, long-term capital movements, in the form of portfolio investments, represented the most dynamic element of international monetary flows.

The buoyant expansion of these flows was grounded upon structural and cyclical motivations, such as favourable prospects on the American stock market, an eye cast by British investors for European markets on the eve of the United Kingdom's entry into the EEC and Japanese policies geared towards internationalizing their capital market. Together with these elements one should not forget, however, the impact of measures taken by numerous countries to control short-term capital flows. As a matter of fact, portfolio investments remained, over most of last year, the smoothest channel for moving speculative funds from one market to another.

With the curbs introduced in West Germany during the last year on purchases of mark-denominated German securities and reinforced in the early months of 1973, controls on portfolio investments are now in force in all the major EEC countries thus making even more difficult the creation of a European capital market.

In the monetary crisis that took place in February and March of this year, the currencies subject to upward pressures were once again those of the EEC countries — with the exception of Italy — and Japan. Although it was this latter country that registered the highest surplus on current account vis-à-vis the United States, the most massive flow of funds poured into West Germany, because of greater freedom for investment in the German market in respect to that of Japan.

The extent of capital flows brought about by the dollar crisis can be indirectly quantified by recalling that in the month of February the German official reserves increased by 6 billion dollars and those of Japan by 1.2 billion. And reserves of the Netherlands, Belgium and Switzerland increased altogether by another 2 billion dollars. After the brief let-up in the aftermath of the dollar's 10 per cent devaluation announced on February 12, there was a fresh burst of speculative activity, linked with the recurrent voice of a joint float for the EEC currencies and of their further appreciation in respect to the dollar. On March 1 alone, the European central banks purchased 3.6 billion dollars, the Bundesbank taking up 2.7 of these.

Speculative flows were mainly channelled through the Euromarket. Data available at this time seem to substantiate that the Eurobanks, to meet the conversion of dollar-denominated deposits, used — once forward coverage of liabilities in currencies other than the dollar became too expensive — a portion of their dollar liquidity with the American banking system and enlarged their indebtedness with it. The American banks thus functioned as lenders of last resort for the Eurodollar market during the crisis, thus increasing the creation of international liquidity base. The deposits of the foreign branches of the American banks with their parent banks were cut in half in the week of the dollar devaluation, while the credits of the large American commercial banks to their foreign correspondents augmented by 2 billion dollars in the February-March period.

The fall in dollar deposits corroborates their ready availability, that is, their nature as liquid reserves. This raises the possibility that the foreign exchange reserves of Eurobranches need not be of the same currency as the banks' foreign deposit liabilities. The quick recourse to indebtedness with the American banks stresses the point, confirmed moreover by the dealers themselves, that excess reserves can drop to nearly zero, thereby further expanding the credit capacity of the Euromarket.

This is thus further evidence, in accordance with some worries expressed by several monetary authorities on the system's solvency, of the urgency to have timely information on the liquidity position of banks operating on the Euromarket and, furthermore, to impose flexible reserve requirements, according to the economic situation.

The above-described developments followed upon a year of constant growth in the volume of intermediation on the Eurocurrencies market, which during 1972 registered an expansion even more vigorous than in the year before, reaching at end-December a balance-sheet total of 135 billion dollars (Table 3).

The expanding geographical reach of the banks operating on the Euromarket and the founding of new Eurobranches — of the Japanese banks, for instance — further strains the lack of available data, limited to eight European countries and to overall balance statistics.

Table 3

EUROCURRENCY MARKET

Items	Amounts at end of			Semi-annual changes					
	1970	1971	1972	1970		1971		1972	
				I	II	I	II	I	II
	(billions of dollars)								
Eurocurrencies including interbank accounts									
Credits	78.3	100.4	135.0	6.8	13.2	7.5	14.6	8.7	25.9
Eurodollars	*60.4*	*71.7*	*98.0*	*4.4*	*8.4*	*4.7*	*6.6*	*5.5*	*20.8*
Other Eurocurrencies	*17.9*	*28.7*	*37.0*	*2.4*	*4.8*	*2.8*	*8.0*	*3.2*	*5.1*
Deposits	75.3	97.9	132.0	5.7	12.8	7.0	15.6	9.4	24.7
Eurodollars	*58.7*	*70.8*	*97.0*	*3.2*	*9.3*	*3.2*	*8.9*	*5.2*	*21.0*
Other Eurocurrencies	*16.6*	*27.1*	*35.0*	*2.5*	*3.5*	*3.8*	*6.7*	*4.2*	*3.7*
Eurocurrencies not including interbank accounts (1)	57.0	71.0	96.0	13.0		14.0		25.0	
Eurodollars	*46.0*	*54.5*	*75.0*	*4.0*	*4.5*	*3.0*	*5.5*	....	....
absorbed by U.S.	*12.7*	*9.3*	*10.4*	*- 0.1*	*- 3.7*	*- 2.3*	*- 1.1*	*0.3*	*0.8*
by other countries	*33.3*	*45.2*	*64.6*	*4.1*	*8.2*	*5.3*	*6.6*	....	....
Other Eurocurrencies	*11.0*	*16.5*	*21.0*	*4.5*		*5.5*		*4.5*	
	(unit ratios)								
Net Eurodollars / Amount absorbed by United States	3.6	5.9	7.2	—	—	—	—	—	—
Amount absorbed by { Other countries / United States	2.6	4.9	6.2	—	—	—	—	—	—
	(annual percentage rates)								
3-month Eurodollar deposits	7.3	6.4	6.0	- 1.5	- 2.2	—	- 0.9	- 1.3	0.9
4-6 month U.S. commercial paper	5.7	4.7	5.4	- 0.6	- 2.5	- 0.3	- 0.7	- 0.1	0.8
U.S. federal funds	4.9	4.1	5.3	- 1.4	- 2.7	—	- 0.8	0.4	0.8

Sources: Bank for International Settlements. Federal Reserve Bulletin - Board of Governors, Federal Reserve System.

(1) Excluding exchanges of interbank funds carried out within the group of eight reporting countries but including estimates of bank indebtedness to non-bank residents and of conversion into or from other currencies.

The market continued to be fed, in the presence of the US balance-of-payments deficit, by the growing volume of deposits by central banks of countries not belonging to the Group of Ten and by the expansion of the Eurobond market, which gave rise to large redeposits of borrowed long-term funds, waiting for investment.

As regards the currencies used in Eurobanking operations, the dollar, albeit continuing to be used to a widening extent in absolute terms, already had begun to lose ground percentually on both sides of the balance sheet in 1970-1971. This drop increased sharply, especially on the assets side, during the first dollar crisis. The trend bottomed in the first half of 1972, turned around in the second but seems to have taken on fresh downward impetus in the first quarter of 1973.

Data on the increase in absolute terms and on the relative position of the dollar against all Eurocurrencies make it possible to fill in the picture of the sequence in which speculation takes place in a system of fixed exchange rates characterized by wide freedom in capital flows. In the periods in which there were no expectations of imminent parity changes, the so-called *hot money* collects in dollar-denominated accounts, which usually pay higher returns. The remaining deposits are taken out in the currencies which show the greatest resistence to devaluation or are historically subject to appreciation.

When the balances in Eurodollars, such as in the second half of 1972, grow large enough and the United States' basic balance does not seem to indicate any reasons why the inflow to the banks should taper off, the dollar begins to show signs of weakening, with a forward discount on exchange markets.

This sets off orders to convert Eurodollar deposits into deposits denominated in the strong currencies. The banking systems of the strong-money countries register a rise in non residents' deposits as the dollars flow in and are, in turn, deposited with the central bank. The conversion process is bolstered by the loss of reserves — usually deposits held in the United States — of countries which, as the crisis unfolds, are passing through a negative cyclical moment, such as Italy in 1972. Finally in the crisis's aftermath we find there has been a swelling of official reserves and Eurodeposits and, on the other side, of the US deficits on liquidity and official transactions basis.

It thus follows that influxes to the Euromarket of liquidity stemming from deficits in the US balance of payments produce expansive impulses. This effect will be larger the more it is in the public's interest to leave their funds in the Euromarket, rather than to put them back in the markets of origin and reconvert them into domestic currencies. Since the European banks are subject, on average, to less controls in managing assets in foreign currency than those in domestic money, they use their advantage to pay higher rates on Eurodeposits than on ordinary ones. They can thus maintain a spread between the rates paid in the market of origin and those in which they operate, both on the borrowing and the lending side, with the shift in emphasis from one to the other geared according to the economic situation. The establishment of fair play for banking activities carried out in domestic currencies and in Eurocurrencies is a necessity — together with control of the international liquidity held by the Eurobanks — if the authorities wish to hinder the repetition of international monetary crises, such as the recent ones.

The balances of payments of the members of the Group of Ten and Switzerland registered an overall deficit of some 4 billion dollars. The net deterioration, in respect to the surplus of 1.5 billion in 1971, mainly reflects the changes taking place on current account, especially the worsening of the deficit of the United States.

The imbalances in international settlements had only limited effects on the creation of new international liquidity base, because of operations carried out by several central banks, aimed at consolidating part of their foreign currency reserves. The creation of new liquidity through the deficit of the US balance of payments was, in fact, partially offset by the purchase, for some 9 billion dollars, of medium- and long-term US Treasury securities on the part of some central banks; as a result, it amounted to 2.5 billion dollars, which were nearly entirely distributed among the commercial banks and the public (Table 4).

The increase of international liquidity base in the hands of the official authorities, equal to 4.3 billion dollars, resulted from the allocation of some 3 billion dollars of SDRs (the final *tranche* of the issue set for the first activation period) and by the increase of the unused credit lines at the US Federal Reserve.

Table 4

INTERNATIONAL LIQUIDITY BASE

(millions of dollars)

Items	Changes									Amounts outstanding end of 1972
				Semi-annual						
	1970	1971	1972	1970		1971		1972		
				I	II	I	II	I	II	
				Sources						
Monetary gold	– 1,759	2,619	– 509	– 72	– 1,687	– 198	2,817	– 379	– 130	39,043
Ordinary and special drawing rights in IMF	4,095	2,453	3,024	3,571	524	1,983	470	2,892	132	16,298
Unused credit lines at the Federal Reserve Bank of New York and the IMF	– 609	– 1,498	1,299	– 180	– 429	304	– 1,802	490	809	10,391
Liquid liabilities: United States	2,745	14,257	2,550	1,355	1,390	2,031	12,226	– 230	2,780	53,700
United Kingdom	868	3,963	– 613	890	– 22	1,189	2,774	– 470	– 143	9,846
Total	5,340	21,794	5,751	5,564	– 224	5,309	16,485	2,303	3,448	129,278
Memoranda:										
Liquid liabilities of Federal Republic of Germany	....	....	....	758	....	....	....	....	....	6,016 (2)
Other liquidity (of United States and United Kingdom)	– 1,373	6,668	11,941	123	– 1,496	6,138	530	5,890	6,051	25,168
				Uses						
Official reserves	9,810	25,734	4,279	7,185	2,625	10,545	15,189	2,254	2,025	110,297
Monetary gold and other assets	*1,727*	*3,574*	*3,814*	*3,319*	*– 1,592*	*2,089*	*1,485*	*3,003*	*811*	*65,732*
Liquid claims on:										
United States	*7,784*	*20,324*	*380*	*3,415*	*4,369*	*7,457*	*12,867*	*– 959*	*1,339*	*40,086*
United Kingdom	*299*	*1,836*	*85*	*451*	*– 152*	*999*	*837*	*210*	*– 125*	*4,479*
Memoranda:										
Liquid claims on Federal Republic of Germany	....	....	....	– 95	....	....	....	....	....	....
Other liquidity	– 165	7,291	9,296	– 112	– 53	3,107	4,184	3,838	5,458	17,344
Public	578	1,903	– 25	446	132	268	1,635	– 336	311	9,632
Liquid claims on:										
United States	*9*	*– 224*	*673*	*7*	*2*	*78*	*– 302*	*344*	*329*	*4,265*
United Kingdom (1)	*569*	*2,127*	*– 698*	*439*	*130*	*190*	*1,937*	*– 680*	*– 18*	*5,367*
Commercial banks	– 5,048	– 5,843	1,497	– 2,067	– 2,981	– 5,504	– 339	385	1,112	9,349
Liquid claims on United States	*– 5,048*	*– 5,843*	*1,497*	*– 2,067*	*– 2,981*	*– 5,504*	*– 339*	*385*	*1,112*	*9,349*
Memoranda:										
Public's and banks' liquid claims on Federal Republic of Germany	1,546	515	– 527	853	693	– 838	1,353	– 583	56	5,911
Other liquidity held by the public and the banks	– 1,208	– 623	2,645	235	– 1,443	3,031	– 3,654	2,052	593	7,824

Sources: Bulletins of central banks, the International Monetary Fund and other government agencies.

(1) Also includes commercial banks' sterling assets.— (2) The sum of the public's and banks' liquid claims on Federal Republic of Germany at the end of 1972 and those of the monetary authorities at the end of May, 1970 as reported in the Bulletin of the *Bundesbank*.

Gross official reserves grew, on the whole, by more than 26 billion dollars. Against this increase, the liabilities of the United States towards foreign official authorities rose by some 10 billion, while those of the United Kingdom remained more or less stationary. Taking into account the creation of SDRs, the difference of some 13 billion dollars, not explained by the increase in the liabilities of the United States and the United Kingdom towards foreign official authorities, appears to depend, apart from the incompleteness of statistical information for several countries on liabilities to foreign official authorities, upon the multiplier processes operating on the Euromarket, linked also to investment in it of a portion of official foreign currency reserves.

Less than half the increase of gross official assets involved the countries of the Group of Ten and Switzerland, which all together increased their reserves by 10.7 billion dollars. This increment turns out to be much less than that of the previous year, even if the changes are calculated in SDRs: gross assets, in fact, swelled by 27 billion in 1971, if calculated on the basis of the dollar's new parity, and 20 billion if expressed in SDRs.

In the other countries the growth in gross official reserves was circa 16 billion dollars, nearly wholly determined by the sharp increase in convertible currencies. This phenomenon, which reached record proportions in 1972, was concentrated in few countries and was determined basically by three diverse factors: the increase of the surplus on current account of the Arab oil-producing countries; the heavy inflow, to Australia and Brazil, of foreign capital for investment and loans, the ever greater weight of tourism surpluses in several countries in the Mediterranean basin such as Spain, Portugal, Greece and Turkey.

The gross official reserves of the Group of Ten countries and Switzerland came, as of March 31, 1973, to 124.4 billion dollars. The gold portion, calculated at the price of 42 dollars an ounce, covered 28 per cent of the total, marking a drop of 4 percentage points in respect to the previous year's share. Foreign currency reserves, instead, took on a heavier weight, going from 56 to 61 per cent. SDRs and the reserve position with the IMF represented, respectively, 5.2 and 4.3 per cent of the total (Table 5).

The effects of changes in official reserves on monetary policy pursued in 1972 by the major industrial countries can be gleaned through analysis of developments in the central banks' balance sheets. The restrictive tack of monetary policy first decided by the United States and then taken up by numerous other countries, mostly in the second half of the year, shows up in the dynamics of monetary base

TABLE 5

OFFICIAL RESERVES OF THE GROUP OF TEN COUNTRIES AND OF SWITZERLAND

(millions of dollars)

Items	Italy	Other EEC	United Kingdom	United States	Other Countries	Total
	Amounts outstanding as of March 31, 1973					
Assets	6,500	54,964	6,036	14,365	42,522	124,387
Gold	3,483	13,244	901	11,651	5,574	34,853
Foreign currencies	1,965	33,683	4,266	8	26,362	66,284
of which: dollars	*1,329*	*32,380*	*3,805*	—	*17,996*	*55,510*
SDR allocations	345	1,586	1,093	2,491	914	6,429
SDR transfers	67	1,531	- 364	- 316	288	1,206
IMF and GAB	384	3,140	140	531	1,131	5,326
Other	256	1,780	—	—	8,253	10,289
Liabilities	437	3,239	7,644	71,415	394	83,129
Total	6,063	51,725	- 1,608	-57,050	42,128	41,258
	Percentage breakdown					
Assets	*100.00*	*100.00*	*100.00*	*100.00*	*100.00*	*100.00*
Gold	*53.58*	*24.10*	*14.92*	*81.11*	*13.11*	*28.02*
Foreign currencies	*30.23*	*61.28*	*70.68*	*0.06*	*62.00*	*53.29*
of which: dollars	*20.45*	*58.91*	*63.05*	—	*42.33*	*44.63*
SDR allocations	*5.31*	*2.89*	*18.11*	*17.34*	*2.15*	*5.17*
SDR transfers	*1.03*	*2.78*	*- 6.03*	*- 2.20*	*0.67*	*0.97*
IMF and GAB	*5.91*	*5.71*	*2.32*	*3.69*	*2.66*	*4.28*
Other	*3.94*	*3.24*	—	—	*19.41*	*8.27*

Source: International Monetary Fund and Bank for International Settlements.

creation flows in Belgium and the Netherlands. The other countries registered, on the other hand, an expansion of the total flow of monetary base creation in the second half of 1972, because lags in the implementation of a tight monetary policy kept it from having an effect upon the size of the half-year flow (Table 6).

The foreign component of monetary base prevails over the domestic one in all countries under study, except for France, Italy and the United Kingdom. From the analysis of the half-year flows there emerges a plainly negative correlation between the two fundamental components of the monetary base; the correlation is less clear in Belgium, Switzerland and Japan, probably because of seasonal inflows. These observations seem to confirm the opinion that the monetary authorities act over the short run to stabilize the overall flow of base, and thus react to undesired shifts in the flow of the foreign component by making offsetting swerves in the domestic component.

It should not be forgotten that the flow of the foreign component does not exclusively reflect market forces but results from the combined action of these and offsetting interventions of the monetary authorities. Actually, the authorities carry out the offsetting policy in two distinct moves: first they smooth out the oscillations of the foreign component flow, then they match that swing with shifts in the opposite direction in the flow of the domestic component. Thus the negative correlation seen for nearly all the countries under study tends to under-rate the authorities' wider stabilizing actions by measuring only the second offsetting moves.

When gauging the authorities' intentions to completely isolate monetary policy from destabilizing external influences, or to make certain adjustments of monetary aggregates to changes coming from abroad, it seems pertinent to compare the flows of the external component with the basic overall flow.

It can be thus noted that, in the last three years, the United Kingdom and Sweden have plainly refused to trasmit to the total flow of monetary base changes stemming from the foreign component; Belgium, West Germany, Switzerland, Canada and Japan seem to have clearly subjected the creation of monetary base to pressures stemming from abroad; the data relative to Italy, France and the Netherlands do not make possible a clearcut conclusion.

DOMESTIC AND FOREIGN COMPONENTS OF THE

(millions

Items	Amounts at end of			Semiannual changes					
	1970	1971	1972	1970		1971		1972	
				I	II	I	II	I	II
BELGIUM									
Credits	3,878	4,156	4,667	166	88	376	– 210	489	22
foreign	*2,888*	*3,317*	*3,905*	*158*	*146*	*328*	*12*	*320*	*268*
domestic	*990*	*839*	*762*	*8*	*– 58*	*48*	*– 222*	*169*	*– 246*
Monetary base	3,796	4,180	4,768	66	42	246	26	372	216
Other domestic debts	82	– 24	– 101	100	46	130	– 236	117	– 194
FRANCE									
Credits	15,712	17,308	22,861	137	937	3	1,593	931	4,622
foreign	*4,467*	*7,668*	*8,997*	*1,753*	*1,040*	*871*	*2,330*	*1,105*	*224*
domestic	*11,245*	*9,640*	*13,864*	*–1,616*	*– 103*	*– 868*	*– 737*	*– 174*	*4,398*
Monetary base	15,554	17,196	22,621	– 95	758	504	1,138	1,201	4,224
Other domestic debts	158	112	240	232	179	– 501	455	– 270	398
WEST GERMANY									
Credits	23,388	27,267	31,811	1,994	4,781	3,224	– 546	2,715	1,829
foreign	*14,290*	*17,663*	*22,265*	*1,721*	*4,808*	*3,197*	*– 601*	*3,887*	*715*
domestic	*9,098*	*9,604*	*9,546*	*273*	*– 27*	*27*	*55*	*–1,172*	*1,114*
Monetary base	18,524	22,294	28,153	710	2,568	2,022	765	1,543	4,31[illegible]
Other domestic debts	4,864	4,973	3,658	1,284	2,213	1,202	–1,311	1,172	–2,487
ITALY									
Credits	18,266	20,664	24,815	784	1,328	1,216	1,392	331	3,820
foreign	*5,522*	*6,404*	*5,704*	*– 549*	*1,045*	*683*	*264*	*– 355*	*– 345*
domestic	*12,744*	*14,260*	*19,111*	*1,333*	*283*	*533*	*1,128*	*686*	*4,165*
Monetary base	17,360	19,964	23,865	462	1,704	1,010	1,797	150	3,751
Other domestic debts	906	700	950	322	– 376	206	– 405	181	69
NETHERLANDS									
Credits	3,367	3,585	4,249	235	373	83	39	312	352
foreign	*3,229*	*3,474*	*4,456*	*155*	*552*	*257*	*– 105*	*525*	*457*
domestic	*138*	*111*	*– 207*	*80*	*– 179*	*– 174*	*144*	*– 213*	*– 105*
Monetary base	2,903	3,131	3,418	124	28	168	– 25	352	– 65
Other domestic debts	464	454	831	111	345	– 85	64	– 40	417

Source: International Monetary Fund, International Financial Statistics.
(1) For Switzerland and Canada, millions of US dollars.

TABLE 6

BALANCE SHEETS OF SOME CENTRAL BANKS

of SDRs) (1)

Items	Amounts at end of			Semiannual changes					
				1970		1971		1972	
	1970	1971	1972	I	II	I	II	I	II
UNITED KINGDOM									
Credits	11,993	11,972	14,527	382	1,238	490	– 511	437	2,118
foreign	*–9,545*	*–1,633*	*–4,572*	*2,957*	*931*	*3,890*	*4,022*	*–1,685*	*–1,254*
domestic	*21,538*	*13,605*	*19,099*	*–2,575*	*307*	*–3,400*	*–4,533*	*2,122*	*3,372*
Monetary base	11,304	10,726	13,001	38	1,138	– 7	– 571	355	1,920
Other domestic debts	689	1,246	1,526	344	100	497	60	82	198
SWEDEN									
Credits	3,014	3,269	3,592	– 129	189	64	224	30	293
foreign	*762*	*1,028*	*1,451*	*– 50*	*116*	*203*	*73*	*256*	*167*
domestic	*2,252*	*2,241*	*2,141*	*– 79*	*73*	*– 139*	*151*	*- 226*	*126*
Monetary base	2,424	2.687	2,941	– 127	203	– 27	317	– 33	287
Other domestic debts	590	582	651	– 2	– 14	91	– 93	63	6
SWITZERLAND									
Credits	5,517	7,139	7,936	– 133	856	– 338	1,426	26	500
foreign	*5,129*	*6,769*	*7,554*	*– 128*	*835*	*– 329*	*1,472*	*55*	*474*
domestic	*388*	*370*	*382*	*– 5*	*21*	*– 9*	*– 46*	*– 29*	*26*
Monetary base	5,165	6,889	7,756	– 263	753	– 169	1,382	– 71	676
Other domestic debts	352	250	180	130	103	– 169	44	97	– 176
CANADA									
Credits	4,980	5,770	6,690	50	310	310	480	500	420
foreign	*4,740*	*5,710*	*6,020*	*1,170*	*230*	*210*	*760*	*420*	*– 110*
domestic	*240*	*60*	*670*	*–1,120*	*80*	*100*	*– 280*	*80*	*530*
Monetary base	5,270	6,060	7,000	20	270	310	480	340	600
Other domestic debts	– 290	– 290	– 310	30	40	—	—	160	– 180
JAPAN									
Credits	19,389	21,498	26,986	– 800	3,806	–1,861	2,442	9	5,479
foreign	*4,839*	*14,145*	*16,914*	*430*	*756*	*2,961*	*5,339*	*449*	*2,320*
domestic	*14,550*	*7,353*	*10,072*	*–1,230*	*3,050*	*–4,822*	*–2,897*	*– 440*	*3,159*
Monetary base	17,203	21,214	27,371	– 722	3,167	– 936	3,439	– 688	6,845
Other domestic debts	2,186	284	– 385	– 78	639	– 925	– 997	697	–1,366

II. – THE ITALIAN ECONOMY

ECONOMIC TRENDS AND THE CREATION OF INCOME

National accounts and the economic situation

In 1972, in the presence of continued expansive thrusts provided by foreign demand and moves by the public administration, the most serious negative impulses plaguing the economy in prior years gradually slackened and the imbalances stemming from these reverse forces were partially offset.

Inventory rebuilding, as stocks approached desired volumes, returned to normal levels; the fall-off in home building, which lasted for two years, hit bottom; direct productive investments, which on a yearly average footing were still on the downgrade, began to turn around in the final months; and private consumption reacted positively, even if marked with some uncertainty, to the expansion of disposable income. The recovery in productive activity made possible substantial increases in productivity, especially in the industrial sector, and determined, together with the smaller increase in wage rates, a reduction in labour cost per unit of output thereby mitigating one source of further inflationary pressures and increasing profits.

In 1972 once again, however, the increment in real demand, even though higher than in the previous year, was not enough to ensure a sufficient utilization of available resources: industrial employment fell by 1.4 per cent, the degree of utilization of productive capacity in the manufacturing industries was still low and the current account sector of the balance of payments registered a large surplus.

Exports once again played a major role in supporting demand, increasing by more than 11 per cent at constant prices. This serves to substantiate the role played by the foreign demand component, in the present Italian institutional context, in countering the intensity and duration of the depression.

On the domestic demand side, there was a bottoming of the recessive impulses that began in 1971 with the downslide in building and the drop in stockbuilding.

Anticyclical moves by the public sector, both through the investments of the state-controlled companies and through the autonomous changes in the public administration's budget, served once again in 1972 as important props, though less so than in the previous year. The public administration's deficit — defined as the deficit for current operations net of foreign transfers, plus the value of investments carried out — passed the 2,800 billion mark. The increase in the deficit, though substantial was nonetheless lower than the exceptional one in 1971, when large pay hikes were granted to the civil servants.

The support action carried out by the public administration through the expansion of transfers and public consumption was reduced by the sharp rises in revenue from direct taxes which reached 21 per cent. As a result, income creation received an additional push equal to more than 3 per cent of the real income in 1971. Moreover, appreciable expansionary effects, mainly on investments, were generated by the decree of May 25, 1972, n. 202, which permitted an immediate exemption from turnover tax on capital goods, even if it is difficult to quantify to what extent this move was translated into a smaller price rise for capital goods or into a larger increment in profits.

Altogether, overall demand increased by 5.1 per cent at constant prices mainly as a result, as noted above, of the export prop, while fixed investments continued to fall off slightly on the overall level but more markedly in the industrial sector and for public works. As a result the percentage of resources exported climbed from 20.5 per cent in 1971 to 21.7 per cent in 1972, while that of resources invested dropped further from 15.6 to 14.8 per cent. The climb in private consumption, equal to 3.8 per cent at constant prices, was less than there were good grounds to expect from the performance of the private sector's real disposable income and its distribution. The unchanged pattern of the average propensity to consume around the low levels reached in 1971 might reflect both a spill-over of the climate of uncertainty into the first part of 1972, and the gradual way in which the effects of the public administration's action, founded basically on the increase of transfers to the households, work their way through the economy.

The development of supply was characterized by an appreciable recovery in imports (more than 13 per cent in real terms), which sharpened in the latter part of the year and carried over into the first two months of 1973. Domestic output, while being negatively influenced by the unfavourable climatic conditions in the primary sector, was basically conditioned by the state of demand in the industrial and services sectors. The index of utilized capacity in the manufacturing industries reveals, in fact, that the wide margins of unutilized capacity

TABLE 7

TRENDS IN AGGREGATE DEMAND AND SUPPLY

(at current prices)

Items	Billions of lire	Percentage changes			
	1972	4th qtr 71 / 4th qtr 70	4th qtr 72 / 4th qtr 71	4th qtr 71 / av. 1971	4th qtr 72 / av. 1972
Demand:					
consumption	54,490	10.1	12.5	3.8	5.8
gross investment	13,902	2.6	15.2	4.0	11.5
domestic demand	68,392	8.4	13.1	3.8	6.9
exports of goods and services	14,938	14.7	10.8	7.1	5.2
aggregate demand	83,330	9.5	12.6	4.4	6.6
Supply:					
gross national product	68,976	10.0	10.4	4.7	5.8
imports of goods and services	14,354	7.1	24.3	2.8	10.6

Source: General Report on the Economic Situation in Italy. For percentage changes Banca d'Italia quarterly and seasonally adjusted estimates have been used.

of the preceding year, mainly in the capital goods sector, were not appreciably lower on a yearly average basis, even though they narrowed sharply in the last quarter (Table 7).

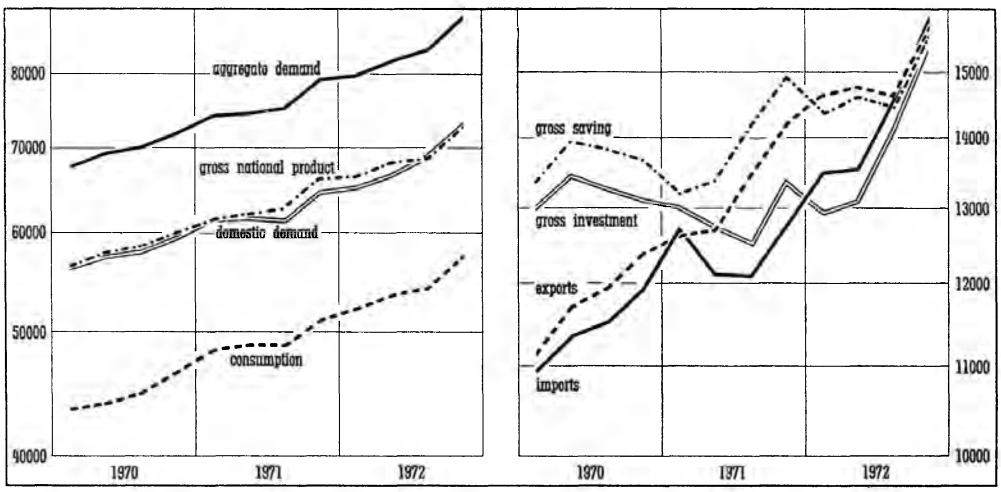
Under these conditions the recovery of demand, and hence the monetary and fiscal policies stimulating it, cannot have had an inflationary impact. If on one hand more vigorous demand, by allowing the transfer onto prices of a part of the rising costs, paved the way for a certain widening of profit margins, on the other, it opened the road through production gains — mainly in the industrial sector — for those increases in productivity which sharply narrowed the expansion of unit costs.

The economic situation

After a stagnant performance for the first three quarters, with some first signs of recovery in domestic demand in the third, the economic situation in 1972 turned highly positive in the fourth (Chart 3).

In the first quarter in fact there was a rapid backslide from the improvement scored in the final quarter of 1971. An improvement which, as pointed out in last year's Report, was not based on the proper conditions to ensure a lasting recovery; notably the rebalancing

CHART 3



Trends in demand, supply and their components

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

of the firms' financial structures and a sufficient degree of utilization of productive capacity. The new fall-off in domestic demand, mainly stemming from a downturn in investments, was reflected in the cutting back of industrial production, while employment also suffered worse results.

The negative trend was verified by the outcome for the second quarter, during which it became clear that the stoppage in the early months of the year was not merely owing to a certain amount of caution on the part of businessmen in view of the approaching political elections. There was an ongoing weakness in domestic demand that was joined by a substantial drop in exports which up to that point had been, practically without interruption, the basic support of productive activity. In this period it also became evident that it would be impossible for the public administration to carry out the volume of investments which the Annual Plan had stressed as a basic condition for sparking off recovery.

In the third quarter some early signs of a turnaround began to appear: the speed-up of imports was the first indication of an improved situation for domestic demand now being fanned by investments, reflecting the combined action of manifold factors. In the first place there was an increase in inventory building spurred by the fear of further rises in world prices and by precautionary moves in the face of possible interruptions in productive activity as contracts came up for renewal at the end of the year. In addition, the impact of fiscal measures exempting capital goods purchases from turnover tax began to be felt, while on the profits side it began to appear that results would be better than last year. This latter development furnished better prospects in terms of the financial structure of the firms, in a period in which short-term credit conditions were still favourable and medium- and long-term operations were steadily burgeoning (Chart 4).

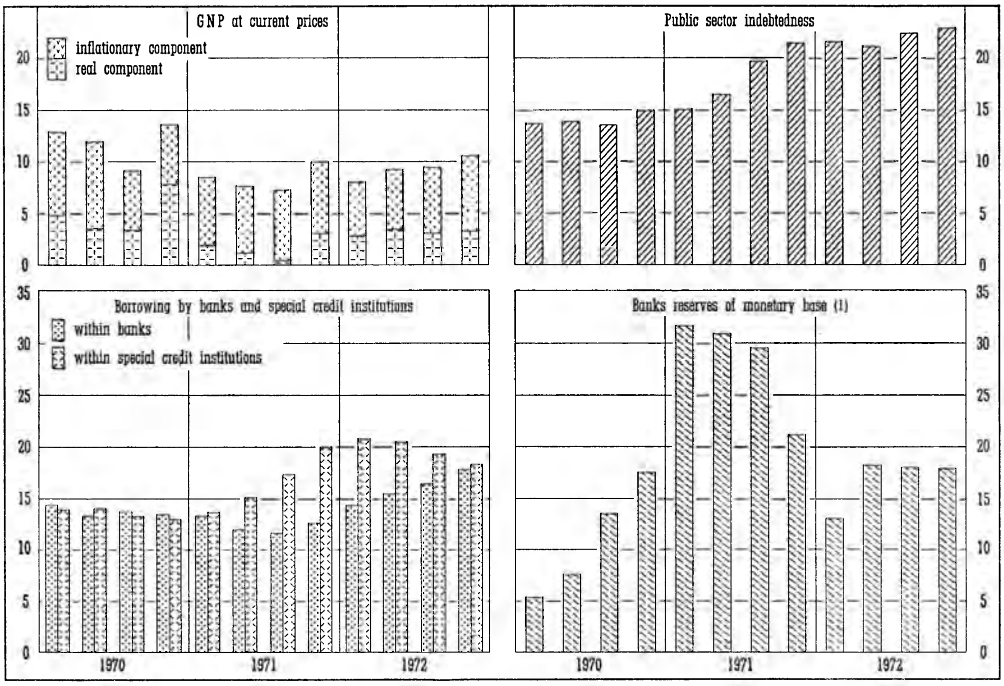
From October on, industrial production shot vigorously forward, bringing the degree of utilization of productive capacity, which during the previous nine months had been in steady descent, up to levels higher than those of end-1971. At the same time non-agricultural employment began to rise. The main support still came from gross investments, but was accompanied also by private consumption which, apart from the impact of substantial public transfers, was fanned by the anticipated purchase of several goods, in connection with the introduction of VAT scheduled for the first day of 1973. Further support came from a renewed increase in exports.

The recovery in demand thus made it possible to make forward strides, also through the boost in prices that inevitably accompanies this phenomenon, in the process of adjusting the firms' accounts, after the rises in costs of the previous years.

The difference between the level of economic activity in the final quarter and the annual average was wider than any scored in the previous three years, signalling a balanced supply and demand structure potentially ideal for ensuring more permanent recovery (Table 7).

As the economy moved from one year to the next there was no lack, however, of negative factors and qualifications. The most outstanding of these was prices, which were speeding headlong forward

CHART 4



Trend of the gross national product and certain financial aggregates

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

(1) Corrected for variations in the coefficient of compulsory reserves.

even in comparison with the other countries, both on the wholesale and consumer level, as a result of the combined impact of new inflationary pressures of a domestic nature and of those coming from abroad. Another serious problem was the uncertain situation caused by the reappearance of the crisis of the international monetary system and the speculative capital flows that go along with it. Still up in the air moreover were the unresolved labour negotiations in the engineering and steel industries, with their full accompaniment of strikes and slowdowns of productive activities, the unknowns involved with the reactions of the prices system to the introduction of VAT, and finally the impact the new contracts would have on labour costs.

The situation at the beginning of 1973 differed from that of the previous year not so much for the diverging patterns in the early months of several important indicators, but for the presence of those conditions fundamental to a sound recovery which were lacking at this time last year. The perking up of domestic demand seems more firmly grounded because it is based, with regard to investments, on a positive evolution in the formation of savings by the firms and favourable demand prospects coinciding with the continued existence of ready credit conditions. In addition the firms seem to have begun to reorganize the structure of their factors, updating them to the changed labour and market conditions thereby paving the way, in the presence of sound demand levels, for further gains in productivity.

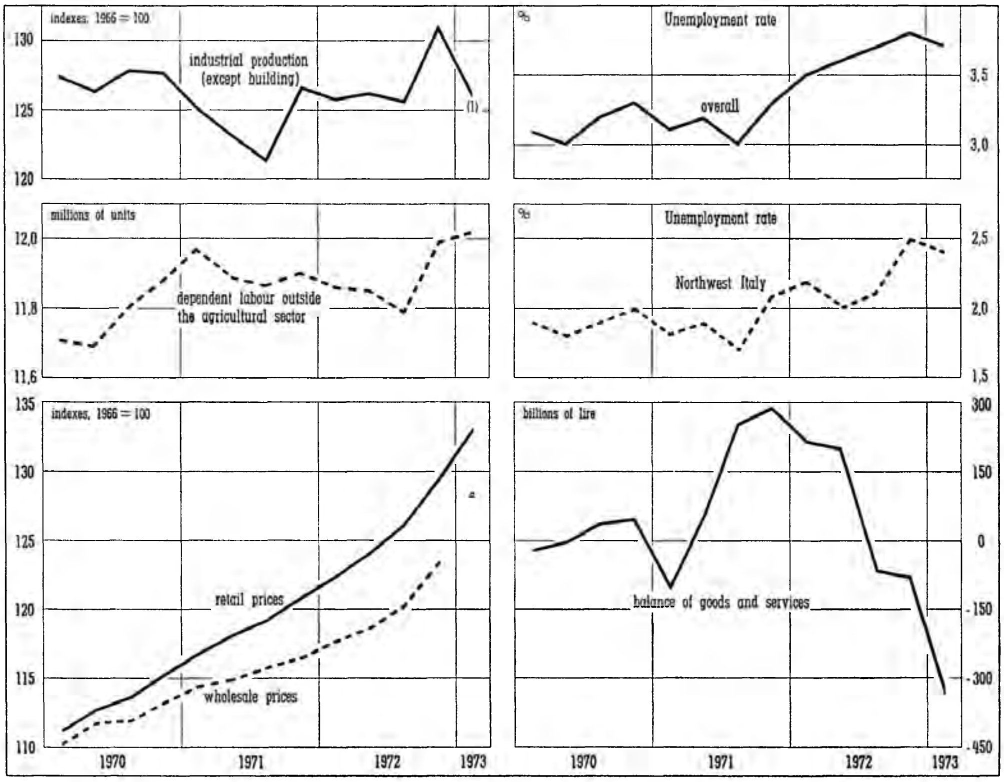
As regards consumption, it now appears highly unlikely that propensity will fall yet further below the already low levels reached hitherto in a year in which the numerous new work contracts will provide the households with additional available income and in which fears of an employment fall-off should be partially dissipated. Moreover, the performance of the small businesses seems to be perking up, a development that on one side points to the presence of good demand prospects for a sector having a built-in bias towards consumer goods, and, on the other, adds fuel to forecasts for a better employment situation.

In addition, the drag stemming, up to the middle of last year, from the recession in building has faded and that alone should be enough to offset the tapering thrust, in respect to previous years, of support action provided by the investment activities of the state-controlled companies.

The largest obstacles looming on the horizon are linked mainly with price behaviour: apart from the inflationary momentum inherited from the past three year period, the impact on costs of the new labour contracts, the reactions to the switchover to VAT, there has been no relief from the unbalancing impulses generated by world-wide inflation which tend to be magnified by the lira's downward float.

From the most recent statistics indicators, it emerges that the Istat index of industrial production, although having fallen in the first two months, reached a level little above that of the previous year for the corresponding months, and when the productive activity of the engineering sector — hit by numerous strikes preceding the signing of the new agreement — is not included in calculations, it rises to a level substantially higher than the average for the past year. The persistence of vigorous demand patterns, in the presence of bottled up supply, is reflected by the steep drop in the balance of foreign trade in goods and services (even if, because of striking customs workers, data on trade for the

CHART 5



Trends of some economic indicators

(1) First half.

Notes: Data seasonally adjusted, with the exception of prices; for industrial production and prices: quarterly average; for employment and unemployment: quarterly Istat data; the balance on goods and services does not include factor income. Data for the first quarter of 1973 are provisional and partly estimated; more specifically, since no comparison can be made with previous data, the index for wholesale prices is simply shown by a point.

month of March may have gone partially unreported). With regard to this, a seasonally adjusted deficit of more than 350 billion, notably a negative difference of 600 billion in respect to the same period of the previous year, seems to be highly indicative (Chart 5). An improvement, even if slight, shows up in non-agricultural employment and is reflected in a reduction in the rate of unemployment, which steadily climbed all through 1971.

As has been noted, more than once the most worrisome symptoms come from the prices front: together with an increase in consumer prices of 3.3 per cent between December and March, there was an expansion of 3.7 per cent, between January and March, for wholesale prices. If we add the rise that took place between December and January, which it was not possible to quantify for the reasons shown below but which was certainly much higher than the 0.7 per cent which shows up in the artithmetical comparison between the Istat indexes for these months, the rate of increase turns out to be of unprecedented proportions — except during the years of the last world war — in the annals of recent Italian economic experience. Even if it is predictable, and several indicators of international prices seem to confirm it, that the growth rates will slacken off in the next few months, the fact remains that the increase that has already taken place in three months is equal to that which occurred over the entire second half of 1972 or, going back in time, in all of 1970.

Domestic demand

Income deriving from dependent labour in the public and private sectors grew at a nearly even pace (11.5 and 10.7 per cent respectively), while the incomes from the independent activities of individuals, whose number seems to have sharply declined, expanded to a more limited extent (7.1 per cent). The increase of incomes from capital, finally, was rather low (5.3), as a result of declining interest rates (Table 8).

The increase of money incomes (9.3 per cent) was translated, because of the net effect of transfer payments, into a slightly higher increase in the disposable income of households (10.0 per cent), a development similar to that of 1971.

The percentage of expenditure on *food and drink* fell as it had on average during the previous decade; the percentage for housing, which depends basically on the relative price, declined along with it (Table 9).

Among the sections on the uprise was that of private vehicles. This item registered for the second year running, in fact, an increase in relative prices which for many years had shown a steadily downward trend. The slim rate of increase in demand in real terms seems to reflect this development.

TABLE 8

THE HOUSEHOLDS' DISPOSABLE INCOME AND ITS USES

Items	Billions of lire			Percentage variations	
	1970	1971	1972	1971/1970	1972/1971
INCOME	45,509	50,309	54,977	*10.5*	*9.3*
from dependent labour	27,979	32,176	35,648	*15.0*	*10.8*
private sector	22,373	25,472	28,204	*13.9*	*10.7*
public sector	5,271	6,342	7,070	*20.3*	*11.5*
net from abroad	335	362	374	*8.1*	*3.3*
independent activities of individuals (1)	13,132	13,411	14,358	*2.1*	*7.1*
capital	4,398	4,722	4,971	*7.4*	*5.3*
CURRENT TRANSFERS					
from the public administration	8,199	9,786	11,521	*19.4*	*17.7*
from the rest of the world	391	445	471	*13.8*	*5.8*
HOUSEHOLDS' TOTAL EARNINGS	54,099	60,540	66,969	*11.9*	*10.6*
minus:					
social security contributions	6,631	7,545	8,375	*13.8*	*11.0*
transfers	382	532	535	*39.3*	*0.6*
capital and income tax	2,764	3,158	3,823	*14.3*	*21.1*
DISPOSABLE INCOME (1)	44,322	49,305	54,236	*11.2*	*10.0*
CONSUMPTION	37,302	40,375	44,356	*8.2*	*9.9*
SAVINGS (1)	7,020	8,930	9,880	*27.2*	*10.6*

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

The drop in the volume of gross fixed investments (3.5 per cent), which was a feature of 1971, reached bottom in 1972. The expansionary trend of the second half of the year made possible a comeback from the first half's decline, limiting the overall fall-off in respect to 1971 to a scarse 0.2 per cent. In money terms, as a result of another steep rise in implicit prices (5.3 per cent), even if lower than those of the previous year and the preceding three-year period (6.8 and 8.1 per cent respectively), the variation in gross fixed investments came to plus 5.1 per cent versus 3.1 in 1971.

Taking into consideration the 580 billion in current prices against 255 in 1971 spent on the building up of stocks, in spite of a fall-off in inventories in the agricultural sector, gross investments increased by 7.5 per cent in money terms and 2.0 in real terms (Table 10).

TABLE 9

TOTAL PRIVATE CONSUMPTION

Items	Billions of lire	Percentage breakdown			Percentage changes at 1963 prices		Price index (1963=100)	
	at current prices							
	1972	1970	1971	1972	1971/1970	1972/1971	1971	1972
Food and drink	17,058	*39.7*	*39.0*	*38.5*	*1.8*	*1.5*	129.0	137.8
Clothing and other personal items	4,636	*10.4*	*10.3*	*10.5*	*0.9*	*3.5*	136.2	146.7
Housing, fuel and electricity	5,563	*12.9*	*12.9*	*12.5*	*3.5*	*4.0*	144.2	148.0
Household durables:								
furniture, fittings, appliances and services	2,759	*6.0*	*6.1*	*6.2*	*4.3*	*6.1*	127.0	133.7
radio-television sets and other entertainment facilities	745	*1.8*	*1.7*	*1.7*	*- 2.3*	*5.3*	119.7	125.4
Private means of transport:								
purchase	1,481	*2.9*	*3.2*	*3.3*	*14.7*	*4.4*	113.9	123.4
use	2,339	*4.9*	*5.1*	*5.3*	*4.4*	*9.7*	147.5	152.8
Hygiene and health	4,041	*8.6*	*8.9*	*9.1*	*4.0*	*7.2*	154.6	161.5
Transport and communication	1,206	*2.8*	*2.7*	*2.7*	*2.9*	*5.0*	142.4	148.3
Hotels, bars and restaurants	1,533	*3.2*	*3.4*	*3.5*	*6.2*	*2.6*	146.9	160.9
Entertainment and cultural fare	1,847	*4.3*	*4.2*	*4.2*	*- 1.8*	*1.9*	151.8	163.0
Miscellaneous expenditure	1,886	*4.2*	*4.3*	*4.2*	*6.2*	*7.1*	116.9	119.7
Private domestic consumption	45,094	*101.7*	*101.8*	*101.7*	*2.9*	*3.7*	134.6	142.4
Residents' expenditure abroad	603	*1.2*	*1.3*	*1.3*	*5.1*	*8.8*		
less: non-residents' expenditure in Italy	1,341	*- 2.9*	*- 3.1*	*- 3.0*	*8.6*	*2.0*		
private national consumption	44,356	*100.0*	*100.0*	*100.0*	*2.8*	*3.8*	134.8	142.6

Source: General Report on the Economic Situation in Italy.

Saving, which once again expanded at a less rapid pace than income because of the exceptional deficit in the public administration's current account expenditure, was lower, in terms of flows, than investments. This determined a shrinking of the balance-of-payments surplus on current account, from 995 billion in 1971 to 848 in 1972 and thus a narrowing of the relative ratio of saving to income (Table 11).

In 1972, as in the previous year, the increase of gross fixed investments resulted largely from the activities of the public sector.

This was the result of action carried out by the public enterprises and state-controlled companies in particular (16.9 per cent), given that the direct investments made by the public administration registered a

TABLE 10

GROSS INVESTMENT

Type of investment	Billions of lire		Percentage breakdown		Percentage changes			
	at current prices						at 1963 prices	
	1971	1972	1971	1972	1971	1972	1971	1972
	by sector of use							
DIRECTLY PRODUCTIVE INVESTMENT	6,960	7,210	*54.9*	*54.1*	*7.6*	*3.6*	*- 0.6*	*- 1.5*
Agriculture	756	801	*6.0*	*6.0*	*1.2*	*6.0*	*- 3.4*	*1.1*
Industry	4,180	4,270	*33.0*	*32.0*	*11.5*	*2.2*	*1.5*	*- 2.8*
Other sectors	2,024	2,139	*15.9*	*16.1*	*2.6*	*5.7*	*- 3.3*	*- 0.1*
SOCIAL INVESTMENT	5,720	6,112	*45.1*	*45.9*	*- 1.9*	*6.9*	*- 8.5*	*1.5*
Dwellings (1)	3,613	3,874	*28.5*	*29.1*	*- 7.0*	*7.2*	*- 11.7*	*2.0*
Other sectors	2,107	2,238	*16.6*	*16.8*	*8.2*	*6.2*	*1.5*	*0.7*
GROSS FIXED INVESTMENT	12,680	13,322	*100.0*	*100.0*	*3.1*	*5.1*	*- 3.5*	*- 0.2*
	by type of goods							
Construction	7,623	7,999	*60.1*	*60.0*	*- 1.7*	*4.9*	*- 7.0*	*- 0.4*
buildings: residential (1)	3,730	3,988	*29.4*	*29.9*	*- 7.4*	*6.9*	*- 12.0*	*1.7*
non-residential	2,447	2,550	*19.3*	*19.1*	*2.9*	*4.2*	*- 2.3*	*- 0.9*
public works	1,446	1,461	*11.4*	*11.0*	*7.0*	*1.0*	—	*- 5.1*
Plants and machinery	3,839	3,986	*30.3*	*29.9*	*12.5*	*3.8*	*1.6*	*- 0.5*
Vehicles	1,218	1,337	*9.6*	*10.0*	*7.4*	*9.8*	*0.1*	*1.4*
GROSS FIXED INVESTMENT	12,680	13,322	*100.0*	*100.0*	*3.1*	*5.1*	*- 3.5*	*- 0.2*
Change in stocks	255	580	—	—	—	—	—	—
GROSS INVESTMENT	12,935	13,902	—	—	*- 2.1*	*7.5*	*- 9.0*	*2.0*

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.

TABLE 11

INVESTMENT AND SAVING

(percentages of the gross national product at current prices)

Items	1964	1965	1966	1967	1968	1969	1970	1971	1972
Gross investment	22.3	19.6	19.3	20.4	19.9	21.4	22.7	20.5	20.2
Net investment	13.8	11.1	10.8	12.2	11.7	13.2	14.1	11.9	11.5
Current account balance	1.2	3.8	3.4	2.4	3.5	2.9	0.9	1.6	1.2
Total net saving	15.0	14.9	14.2	14.6	15.3	16.1	15.0	13.5	12.7

Source: General Report on the Economic Situation in Italy.

drop of 2.4 per cent. The percentage of investments, owing to the direct or indirect action of the government, thus climbed from 32.8 to 33.4 per cent between 1971 and 1972 and from 44.5 to 45.5 if we exclude the investments for the dwellings sector (Table 12).

The anticyclical action of the public enterprises curtailed the downslide in industrial investments both directly and indirectly by providing an added prop to demand. In the absence of similar offsetting activities

TABLE 12

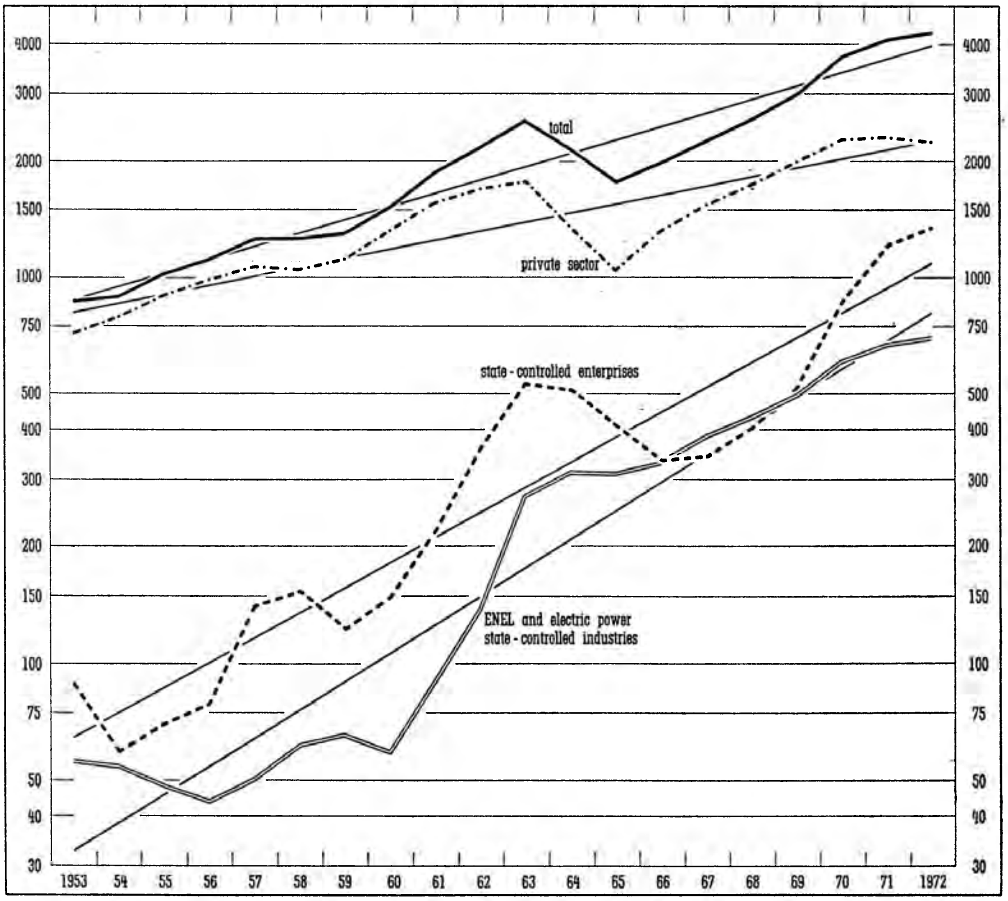
PUBLIC AND PRIVATE DOMESTIC GROSS INVESTMENT BY SECTOR OF ECONOMIC ACTIVITY

Type of investment	Billions of lire (at current prices)		Percentage breakdown			Percentage changes		
	1971	1972	1967	1971	1972	1970/1969	1971/1970	1972/1971
AGRICULTURE	878	913	8.6	6.9	6.8	10.1	1.6	4.0
Private enterprises	756	801	7.4	5.9	6.0	9.1	1.2	6.0
Public enterprises	122	112	1.2	1.0	0.8	17.0	4.3	- 8.2
INDUSTRY	4,180	4,270	27.4	33.0	32.1	25.1	11.5	2.2
Private enterprises	2,330	2,262	18.6	18.4	17.0	17.8	0.3	- 2.9
Public enterprises (1)	1,850	2,008	8.8	14.6	15.1	39.2	29.6	8.5
TRANSPORT AND COMMUNICATIONS	1,298	1,491	9.7	10.2	11.2	18.4	18.1	14.9
Private enterprises	366	430	3.3	2.9	3.2	12.0	3.4	17.5
Public enterprises (1)	932	1,061	6.4	7.3	8.0	21.7	25.1	13.8
COMMERCE, CREDIT, INSURANCE AND SERVICES	1,624	1,713	14.1	12.8	12.9	10.7	- 1.4	5.5
Private enterprises	1,582	1,652	13.8	12.5	12.4	9.9	- 0.7	4.4
Public enterprises (1)	42	61	0.3	0.3	0.5	42.1	- 22.2	45.2
DWELLINGS	3,613	3,874	30.2	28.5	29.1	7.0	- 7.0	7.2
Private enterprises	3,482	3,724	28.1	27.5	28.0	8.5	- 6.9	7.0
Public enterprises (1)	131	150	2.1	1.0	1.1	- 21.2	- 9.7	14.5
TOTAL	11,593	12,261	90.0	91.4	92.0	14.4	3.1	5.8
Private enterprises	8,516	8,869	71.2	67.1	66.6	11.3	- 2.7	4.1
Public enterprises	3,077	3,392	18.8	24.3	25.4	27.0	23.6	10.2
PUBLIC ADMINISTRATION	1,087	1,061	10.0	8.6	8.0	21.2	2.8	- 2.4
FIXED GROSS INVESTMENT	12,680	13,322	100.0	100.0	100.0	15.0	3.1	5.1
Public sector	4,164	4,453	28.8	32.8	33.4	25.2	17.4	6.9

Source: General Report on the Economic Situation in Italy.
(1) For 1972, partly estimated data.

in 1964 and 1965 when the decrease in profits was less steep than that of the past two years, there was a sharper downslide in investments not only at constant prices but also in money terms. Moreover it should be recalled that in the years immediately prior to the earlier period development had been more extensive (Chart 6).

CHART 6



Industrial investments by the private and public sector

(billions of lire; semi-logarithmic scale)

Both the necessity for the firms to bring their productive structure into line with the changed conditions in the labour world and the growing weight of the special credit institutions in the enterprises' medium- and long-term debt structure, concurred to limit the decline in industrial investments, especially those of the private enterprises.

Domestic supply

Production results for the 1972 agricultural year were extremely disappointing. It is necessary to go back to 1960 to find a negative change in the gross marketable product in real terms equal to 2.9 per cent — that is, a fall-off similar to that of the year under study — and all the way back to 1954 to find a worse outcome.

Since the purchase of goods and services increased even further, even if at a rate (3.7 per cent) lower than the long-period trend, the shrinking of added value in real terms was even greater than that registered for marketable output: 4.9 per cent versus the 5.0 of 1960 and 5.7 in 1954.

The performance of farm incomes was only partially affected by the unsatisfactory harvest. Price growth was, in fact, extremely marked (8.5 per cent for the implicit price deflator of gross marketable production and 10.0 for that of the gross product), favoured both by the behaviour of international agricultural prices and domestic imbalances between demand and supply for several outputs. In this way there was an improvement in the dynamics of relative prices and, given the further narrowing of the active farm population, a substantial increase in incomes per employee. As the result of a sharp increase in farm wages, the major beneficiaries of this development were the dependent workers.

Industrial activity after the recession of the previous year, in which for the first time in more than twenty years there was a reduction in real terms, registered in 1972 a moderate recovery; i.e., an increase in the gross product of 3.9 per cent.

Of particular importance to this development, which nonetheless was not up to the trend, was the favourable performance of manufactured output. This rose by 4.2 per cent. In addition, there was also an upswing in electricity and gas output (8.4 per cent). In contrast were the stagnancy in the construction sector (0.2 per cent) after two years of recession and the modest growth scored in the mining and quarrying industries (2.4 per cent) (Table 13).

TABLE 13

INDUSTRIAL GROSS PRODUCT AT FACTOR COST

Items	Values at 1963 prices in billions of lire			Percentage breakdown 1972	Percentage changes		
	1970	1971	1972		1970/1969	1971/1970	1972/1971
GROSS PRODUCT:							
including construction	16,392	16,302	16,935	*100.0*	*6.3*	*- 0.5*	*3.9*
excluding construction	13,805	13,852	14,480	*85.5*	*7.8*	*0.3*	*4.5*
INDUSTRIES:							
extractive	304	287	294	*1.7*	*3.4*	*- 5.6*	*2.4*
manufacturing	12,274	12,261	12,773	*75.4*	*8.0*	*- 0.1*	*4.2*
electricity, gas, water	1,227	1,304	1,413	*8.4*	*7.9*	*6.3*	*8.4*
CONSTRUCTION	2,587	2,450	2,455	*14.5*	*- 1.3*	*- 5.3*	*0.2*

Source: General Report on the Economic Situation in Italy.

The turnaround in industrial production was for the most part uncertain during a good portion of the year with a spotty performance typical for the different sectors until the end of the year when a generalized recovery took hold across the economy after the basic stagnation characterizing the first nine months (Chart 7).

In the first quarter only several industries were able to sustain the expansionary surge that characterized the latter months of 1971, while an increasing number of negative results gradually caused the general index to fall below the levels reached earlier.

From a sectorial breakdown it emerges that a determining weight in the slowdown was flagging production in the industries turning out capital goods (3.0 per cent), except for non-ferrous metals, and a fall-off in the output of producer and consumer goods (0.7 per cent each) although the prior heading was still positively influenced by results in the chemicals and electric power sectors and the second by those in foodstuffs and textiles.

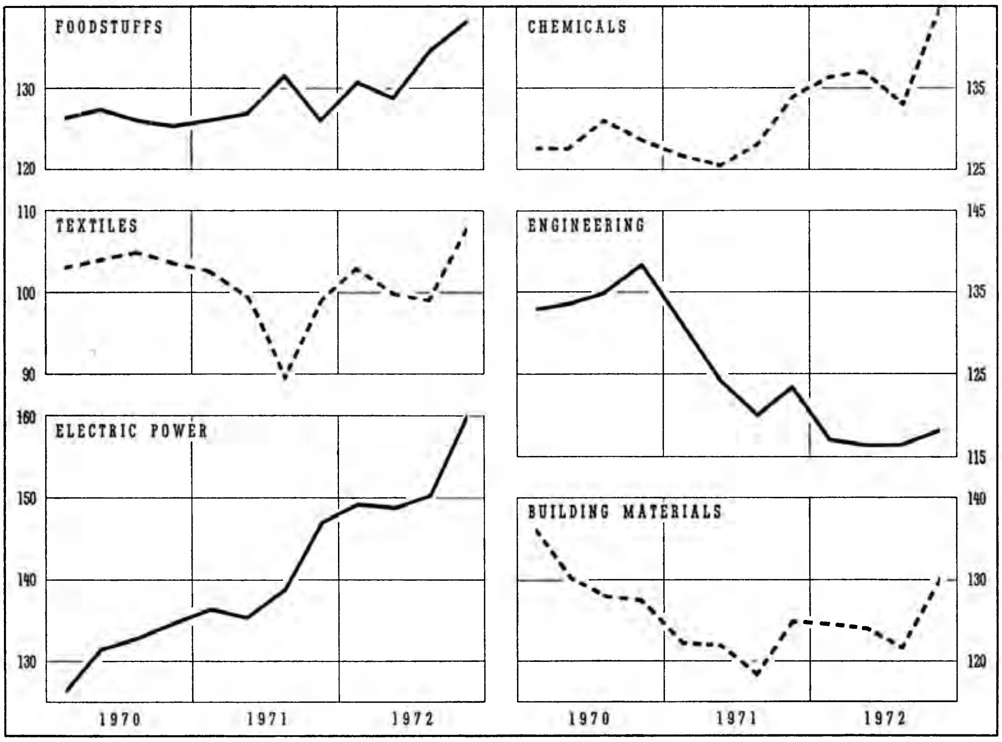
During the second quarter a slight improvement was noticeable, even if the output of producer goods continued to slow down and that of consumer goods levelled off at the rate reached in the first quarter.

The outcome in the first sector reflected mixed developments, for in spite of a vigorous upturn in petroleum derivatives, there were drops in the production of electric power and chemicals which, from the month of June on, were conditioned by the growing number of work hours lost as the result of labour strife.

For consumer goods the productive lull was determined by unfavourable performances in the foodstuffs and textile industries which were not sufficiently offset by the turnaround in the furniture, clothing, electric home appliances and motor vehicle sectors.

Positive results in steels, non-ferrous metals and industrial vehicles broke, in the meantime, the negative trend taking place in the capital goods sector, although the news out of the engineering industry was still negative.

CHART 7



Production in some industries

(calculated from Istat indexes; corrected and seasonally adjusted; basis 1966 = 100; quarterly averages)

No improvement could be seen during the summer months and in fact negative outcomes spread to an ever growing number of industries. At this moment the external demand prop weakened as reflected in a fall-off in exports of manufactured goods of 141 billion lire mainly involving the engineering, chemicals and foodstuffs sectors, while the performance of exports of metallurgical goods remained positive, though less buoyant than in the previous quarter.

The output of the chemicals, petroleum derivatives and fibre industries were steadily harder hit by the increasing number of hours being lost in labour conflicts. It was not until October, when the new contracts had been signed, that production began to pick up once again in these sectors. Further progress was registered in the steel sector, reflecting both good export performance and the impact of corporate strategy increasing stocks, and in the consumer goods sectors as a result of upward pressure felt in foodstuffs and furniture.

A general trend did not emerge from these mixed results until autumn when there was a steep swing upward, spreading to almost every industry in the manufactured goods sector and providing a determining weight in the average annual results.

The most marked stimulus to the turnaround was provided once again by foreign demand, accompanied moreover throughout the course of the year by a more dynamic domestic demand both for consumer and capital goods. A speed-up was registered in particular in the process of building up stocks, stimulated by the fear of possible future boosts in the prices of semi-finished and raw materials.

In spite of the work hours lost in the mechanical engineering and steel sector, second only to the losses of the last quarter of 1969, the upward surge in the output of capital goods made an appreciable contribution to the turnaround in the general index's performance. Along with the positive results in steel output, stimulated by more vigorous domestic demand (for steel the increase was of 12.5 per cent in respect to the third quarter), there was a sharp acceleration in the manufacture of building materials and industrial vehicles reflecting the afore-mentioned upturn in building activity that took place mainly in the last half of the year.

After two unpromising years, interrupted only by the isolated jump in the third quarter of 1971, the production of capital goods by the engineering sector also began to perk up, specifically in the production of non-electrical machinery.

Substantial gains were also made in those sectors turning out producer goods, mainly as a result of the turnaround in chemicals output once the labour negotiations picture was cleared up.

With the exception of electrical home appliances and automobiles, which were hard hit by the continuing waves of strikes, the consumer goods fields all took off appreciably, with the greatest improvements being scored in textiles, furniture, paper, rubber and artificial and synthetic fibre textiles. Favourable results were also registered for foodstuffs, clothing and footwear.

Employment, wages, prices and the distribution of income

Employment

In 1972. labour demand, continuing the downward trend begun in 1970, fell by 1.7 per cent as compared with the previous year. This downslide accelerated in the industrial sector, where 118 thousand workers lost their jobs, but was to a large measure offset by a burgeoning manpower demand in the services sector that was translated into 94 thousand new jobs (Table 14) for a rise of 1.4 per cent. Finally, the exodus from the agricultural sector (— 8.1 per cent), although slowing down during the year (— 6.2 per cent), was not in line with the anticyclical pattern which has characterized changes in labour demand in this sector during the last decade.

As is usually the case when productive activity is being reorganized, the hardest hit were the least qualified labourers and the most vulnerable professional categories. In fact, the shrinkage was worst felt by hired hands and independent labourers and, within the sphere of dependent labour, by blue collar rather than white collar workers. In industry women were most affected: the cut-back in their numbers amounted to about 70 per cent of the total drop (Table 15).

The strengthened position of dependent labour as against hired hands and helpers was very marked in agriculture where the 8.1 per cent drop in overall employment contrasts with the 0.6 per cent increase in dependent workers. In industry and the services the phenomenon took the form, respectively, of a smaller drop and heavier increase for this category of workers in respect to total employees.

TABLE 14

EMPLOYMENT SITUATION

(variations in thousands of units compared with the previous year)

Sectors	1970 Uses	1970 Sources	1971 Uses	1971 Sources	1972 (1) Uses	1972 (1) Sources	1972 (1) amounts (*thousands of units*)
				Northwest Italy			
Industry	39		33		- 68		3,176
Agriculture	- 44		- 16		- 56		442
Services	55		- 25		47		1,980
Unemployment (increase —)		2		- 4		- 14	126
Labour forces (increase +)		48		- 4		- 63	5,724
Total	*50*	*50*	- *8*	- *8*	- *77*	- *77*	
				Northwest and central Italy			
Industry	89		- 13		- 45		3,048
Agriculture	- 159		- 29		- 153		1,147
Services	107		- 4		35		2,989
Unemployment (increase —)		36		- 16		- 22	247
Labour forces (increase +)		1		- 30		- 141	7,431
Total	*37*	*37*	- *46*	- *46*	- *163*	- *163*	
				Southern Italy and the islands			
Industry	33		16		- 5		1,812
Agriculture	- 137		14		- 81		1,709
Services	102		- 39		12		2,028
Unemployment (increase —)		10		22		- 52	324
Labour forces (increase +)		- 12		- 31		- 22	5,873
Total	- *2*	- *2*	- *9*	- *9*	- *74*	- *74*	
				Italy			
Industry	161		36		- 118		8,036
Agriculture	- 340		- 31		- 290		3,298
Services	264		- 68		94		6,997
Unemployment (increase —)		48		2		- 88	697
Labour forces (increase +)		37		- 65		- 226	19,028
Total	*85*	*85*	- *63*	- *63*	- *314*	- *314*	

Calculated on Istat data.

(1) Average yearly data for 1971 and 1972 have been adjusted by Istat on the basis of the 1971 demographic survey and therefore cannot be compared with the previous figures.

There was also a fall-off, though less than in 1971, in the average number of monthly work hours per employee; these showed a marked tendency to drop in connection with the gradual shortening of the working week to 40 hours and with increased labour strife in some sectors.

Over the entire manufacturing industry, the combined pattern of employment and average work hours during the first three quarters shows, as compared quarter-by-quarter with last year, a gradual down-swing in the total input of labour. Assuming that the annual change in work hours per employee equals the average for the first three quarters (— 1.9 per cent), then the increase in productivity would be 6.9 per cent, a percentage which would bring the trend back to medium-term values.

TABLE 15

EMPLOYMENT BY SECTOR, STATUS AND SEX IN 1972

(variations in thousands of units compared with 1971)

Sectors	Men	Women	Men and women
		Dependent	
Agriculture	- 13	20	7
Industry	- 31	- 54	- 85
Services	55	30	85
TOTAL . . .	11	- 4	7
		Overall	
Agriculture	- 179	- 111	- 290
Industry	- 36	- 82	- 118
Services	48	46	94
TOTAL . . .	- 167	- 147	- 314

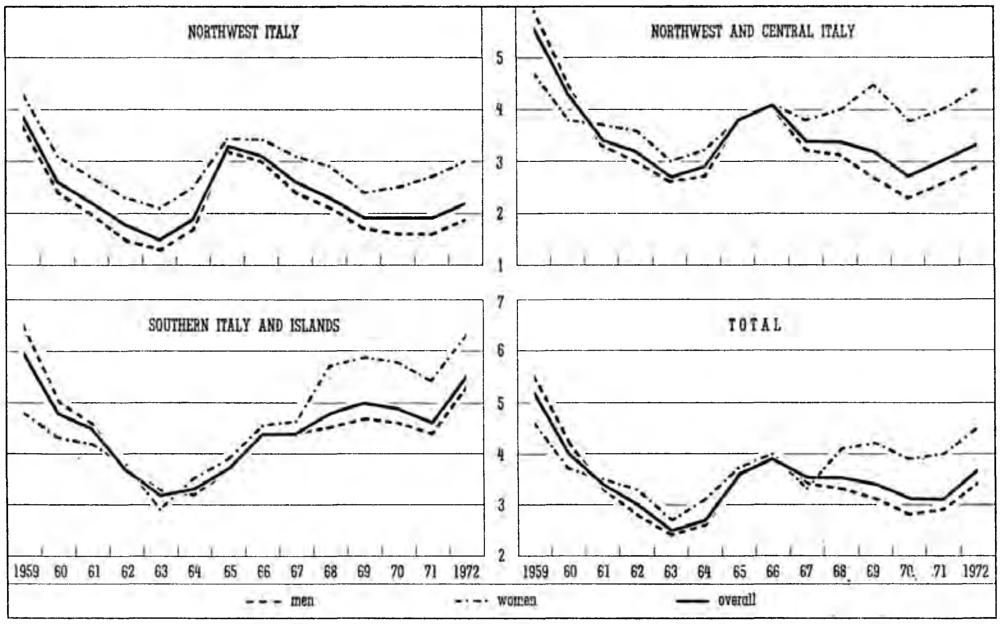
Source: Istat.

Apart from doubts as to its exact size, due to the lack of precise knowledge on average hours worked in the fourth quarter, the productivity increase in 1972 seems to reflect, as usually happens during periods of revived expansion of industrial activity, the potentials for reaching economies of scale. It is likely that this has been reinforced by the most recent investment activity of the enterprises which was focused mainly on reorganizing and modernizing plants in the attempt to remould the productive structure to fit changes in labour patterns within the factories.

The labour force which, after 1970's slight increase, began to shrink during the following year, registered a further and more marked decline (1.2 per cent). This was the result of a gradual deterioration in the employment situation over the last two years. The huge exodus from agriculture and the lack of job-openings in industry, only partly tempered by increased employment in the services sector, resulted in the addition of many previously employed workers to the ranks of the inactive population.

Moreover, weaknesses met on the labour market had their impact on unemployment, whose increase (14.4 per cent) was solely due to the fact that young people were unable to find their first job (31.8 per cent more).

CHART 8



Unemployment rates by geographical area and by sex

(percentage rates)

Calculated from Istat data

The plight of these new job hunters and the general cut-back in labour forces was reflected in a higher unemployment rate all across the country: this was particularly marked in the South and the islands where the unemployment rate had fallen steadily during the previous two years (Chart 8).

Wages

The approach of contract deadlines, affecting the most important sectors, was accompanied by numerous work interruptions. Negotiations for renewal of industry-wide contracts of workers in the chemicals, metallurgy and engineering, construction, foodstuffs and printing sectors, of farm labourers, and of employees in the commercial sector and in banks were particularly arduous, given the breadth of claims, and resulted, especially towards the end of the year, in considerable labour strife. In fact, the trade unions, enlarging upon lines that had already been traced during the previous three years, chiefly focused their efforts on coordinating requests within each sector as well as spelling out those general aims common to all sectors involved in the contract renewals.

The first of these two approaches took the form, as happened in previous years in the engineering sector and in the steel industry, of grouping in one single contract the work rules concerning employees in different branches of the chemicals industry.

The second point regards a more far-reaching intervention by the trade unions in defining the level of professional qualifications, with respect to the plants' internal organization and, then, in working out the pay scales.

TABLE 16

GROSS MINIMUM CONTRACTUAL WAGES (1)

(percentage changes)

Sectors	1971 / 1970	1972 / 1971	Dec. '71 / Dec. '70	Dec. '72 / Dec. '71
WAGES				
Agriculture	13.7	18.1	16.0	20.3
Industry	11.9	9.2	10.8	12.1
Extractive	11.9	8.3	6.2	10.5
Manufacturing	13.5	10.4	11.9	14.2
foodstuffs	10.3	24.0	12.2	30.1
textiles	13.4	10.6	7.3	14.5
metals and eng.	6.5	7.2	6.6	11.3
chemicals	9.7	10.2	8.9	23.3
Construction	9.4	7.2	9.3	8.4
Electricity, gas and water	8.1	8.9	6.7	12.0
Trade	11.5	13.6	13.1	12.3
Transport	11.8	8.0	10.3	8.8
SALARIES				
Industry	9.8	9.0	9.3	12.4
Trade	9.7	13.1	11.0	12.7
Public Administration	9.3	2.2	9.3	6.2

Source: Istat.
(1) Excluding family allowances.

On average, wage rises were generally lower than in the previous year and even more so than in 1970. Moreover, wage development varied from sector to sector, as did the timing of wage increases in connection with the events most affecting the labour market in 1972. Broken down sectorially, the lower rate of increase registered in the yearly average for minimum contractual wages (excluding fringe benefits) in industry as whole (9.2 as against 11.9 per cent in 1971; Table 16) contrasts with faster growth in commerce and still greater expansion in agriculture (respectively 13.6 and 18.1 per cent in 1972 compared with 11.5 and 13.7 per cent in 1971). Within the manufacturing sector the highest increase was registered in the foodstuffs section, notably 24.0 per cent.

TABLE 17

ACTUAL EARNINGS IN INDUSTRY (1)

(percentage changes)

Sectors	1971/1970 (2)	1972/1971 (2)	3rd qtr 1971/3rd qtr 1970	3rd qtr 1972/3rd qtr 1971
Industry as a whole	15.8	11.5	15.6	11.3
Extractive	16.9	9.1	12.5	11.5
Manufacturing	16.6	11.7	16.3	11.5
foodstuffs	14.4	17.8	12.6	21.0
textiles	20.1	10.4	14.7	11.5
metals and eng.	11.7	10.8	11.9	10.4
chemicals	16.3	9.2	15.2	12.1
Construction	11.7	8.7	11.8	9.5
Electricity, gas and water	9.0	15.0	12.4	10.9

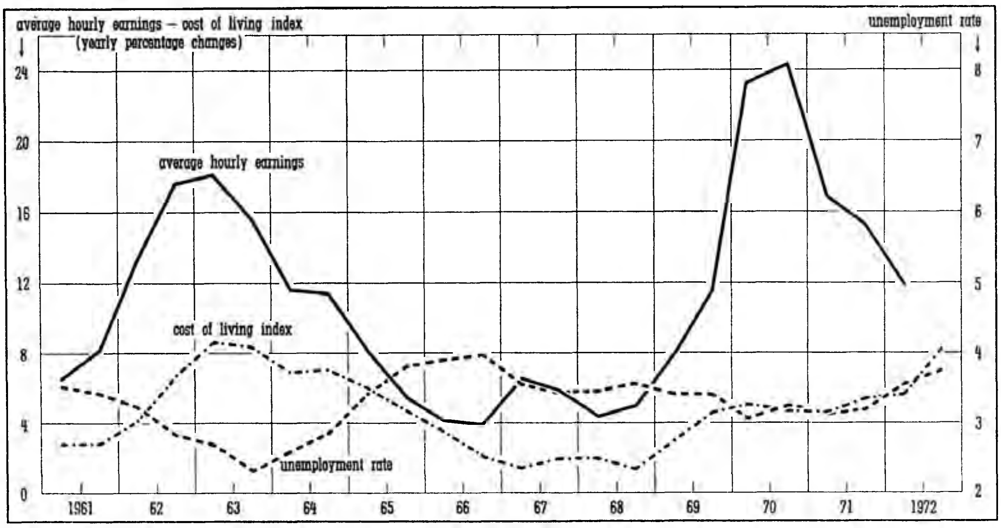
Source: Ministry of Labour and Social Welfare.
(1) Excluding family allowances and other fringe benefits.— (2) Average for the first three quarters.

With regard to the timing of the wage increases, from available data it emerges that upward pressures were greater during the second half of the year. In fact, wage increases in all sectors except commerce appear sharper when data from one end of the year to the other are compared rather than yearly averages.

In the presence of a gradually growing surplus of labour over the year, the rise in contractual wages was spurred by a 13 point increase in the cost-of-living index which, in terms of wage increases, corresponds to about 5 per cent. Further reasons for wage increases were both the shorter working week at equal wages and the final stage of a process ending regional differences in industrial wage scales.

During the first three quarters of 1972, for industry in general and the manufacturing sector, the increment of actual earnings compared with the corresponding period in 1971, equalled respectively 11.5 and 11.7 per cent (Table 17). In the latter sector, during the second half of 1971 and to an even greater extent during the first six months of 1972, there was a progressive slowing down from the peak reached with 1970's exceptional wage increases (Chart 9).

CHART 9



Actual earnings in the manufacturing industry,
trade union cost of living index and unemployment rate
(for wages and the cost of living index: half-yearly changes as compared with the same period of the previous year; for the unemployment rate: half-yearly averages)
Source: Ministry of labour and social security; Istat

The wage increases described above, fanned by the more than proportionate rise in indirect costs, resulted in a continuation of the marked upswing in the labour costs per dependent worker in the private sector (10.5 per cent; Table 18). The improvement in output per man (4.9 per cent) — due both to better production results for the year and to the continuing fall-off in the number of employed persons — in part offset the rise in labour costs per unit of output, which rose by 5.4 per cent; that is at a rate which, although only half that for each of the two previous years, is still high when one considers that 1972 represented, for many sectors, the final phase of the contract cycle.

Broken down by sectors, agriculture registered the development most out of step with the general pattern. Both the heftier wage increases and the unsatisfactory harvests rendered impossible an increase in productivity up to the medium-term trend. Hence, the labour cost per man climbed, in agriculture, by 16.0 per cent and the cost per unit of output by 12.2 per cent. The services sector registered, comparatively, the least marked rise in costs, whereas in the industrial sector the pace of development was more or less equal to the average for the private sector.

TABLE 18

COST OF LABOUR IN THE PRIVATE SECTOR

(yearly percentage changes)

Years	Gross product at factor cost (1963 prices)	Total employment (number of permanent employees) (1)	Output per man	Labour income per dependent worker (1)	Labour cost per unit of output
			Private sector (excluding housing)		
1970	5.5	0.5	4.9	17.2	11.7
1971	1.4	- 1.5	2.9	14.5	11.2
1972	3.3	- 1.5	4.9	10.5	5.4
			Agriculture		
1970	- 0,4	- 7.6	7.8	16.9	8.5
1971	1.6	- 4.1	5.9	18.3	11.6
1972	- 4.9	- 8.1	3.4	16.0	12.2
			Industry		
1970	6.3	2.4	3.8	18.6	14.2
1971	- 0.5	- 1.4	0.9	12.9	11.9
1972	3.9	- 0.9	4.8	10.7	5.6
			Manufacturing industry		
1970	0.8	3.3	4.6	18.9	13.7
1971	- 0.1	0.2	- 0.3	12.5	12.8
1972	4.2	- 0.6	4.8	11.0	5.9
			Services (excluding housing)		
1970	6.6	3.1	3.4	13.7	10.0
1971	4.0	—	4.0	15.6	11.1
1972	5.5	1.4	4.0	9.0	4.8

Source: General Report on the Economic Situation in Italy.

(1) For 1972, data on employment, overall and dependent, are estimated.— (2) Net of social charges paid for by the government.

Prices

Impulses generated by a climate of international inflation and by factors which are more markedly of domestic origin — such as increased labour costs and limited supply of certain foodstuffs — caused a steady rise in wholesale prices during 1972: at year's end they climbed at a rate of 7.3 per cent, more than twice 1971's increase (2.7 per cent) and higher also than the average for the year of 4.1 per cent (Table 19).

Prices for industrial raw materials were characterized, after two years of drifting downward, by a fast and steady upswing. Numerous factors contributed to the increase on the international markets though underlying these was the larger volume of demand in industrial countries owing to the improved cyclical situation. The upward trend was spurred, generally speaking, by expectations of widening sales as well as by speculative operations linked with uncertainties on the foreign exchange markets. On the domestic market the rise in prices was, however, more limited (10.3 per cent at the end of the year) mainly owing to price patterns for petroleum products, since increased costs were partially absorbed by the state through extension of the tax reduction at the production level.

The upward trend of prices for manufactured goods continued, becoming more marked during 1972 (5.2 per cent). Impulses pushing prices higher originated, at a time of inflationary tendencies in the main competitor countries, from the considerable price rise for raw materials and steady growth of unit labour costs. However, the impact on prices was not uniform during the year, becoming more intense only during the last months, when revived domestic demand and widespread expectations of further price increases (in connection also with the changed tax system) eased the transfer of rises in costs onto prices.

In the foodstuffs section prices soared (11.0 per cent). Until July the tendency to rise was limited to few foodstuffs, and in particular beef, where insufficient domestic production necessitated a greater volume of imports just when international prices were climbing. From August on, price boosts spread to most products, rising far above the usual seasonal highs. In the vegetable section, prices were affected by the marked fall-off in output of many widely consumed varieties as the

TABLE 19

DOMESTIC WHOLESALE PRICES

(percentage changes in indexes, 1970 = 100)

Indexes	1971 / 1970	1972 / 1971	Dec. 71 / Dec. 70	Dec. 72 / Dec. 71	July 72 / Dec. 71	Dec. 72 / July 72	Mar. 73 / Jan. 73
					(on a yearly basis)		
Istat							
General index	3.4	4.1	2.7	7.3	3.9	11.7	3.7
Classification by origin:							
Agricultural	2.2	10.3	4.5	18.5	9.5	29.5	7.3
Non-agricultural	3.6	3.0	2.4	5.4	3.0	8.6	3.0
Classification by product (1):							
Foodstuffs	3.4	6.0	3.4	11.0	4.4	19.7	3.9
Vegetable	1.2	7.1	2.0	16.7	6.9	29.3	7.1
Animal	4.4	12.2	8.3	16.1	8.3	25.9	4.1
Food manufactures	4.3	2.9	2.3	5.8	1.6	11.5	1.8
Industrial raw materials and manufactures	3.4	3.3	2.4	5.9	3.8	8.6	3.7
Raw materials	-4.1	3.8	- 2.4	10.3	8.0	13.1	10.4
Manufactures	4.3	3.6	2.9	5.2	3.4	7.6	2.1
Classification by use:							
Consumer goods	3.7	5.5	2.9	9.3	5.0	14.8	3.3
Capital goods	1.3	2.9	1.8	5.3	4.2	6.7	5.5
Producer goods	6.2	-0.2	2.7	1.0	- 3.4	7.3	2.1
Milan Chamber of Commerce							
General index:	0.9	4.7	1.7	9.0	4.5	14.9	5.8
Foodstuffs	1.4	9.1	3.9	12.8	7.8	18.9	4.5
Industrial raw materials	0.6	2.9	0.9	7.4	3.1	13.2	6.3

(1) Istat figures reworked by the Banca d'Italia. The index for industrial material prices does not include construction timber, lignite, crude oil and quarrying products, these being included in the overall index for industrial raw materials and manufactures.

result of unfavourable weather conditions; in the livestock section prices registered a huge upswing, which seems to reflect a heavy rise in feed costs. An upshot of the price increases was a rise, towards the end of the year, in prices in the food processing industries.

The upward movement of retail prices, which gathered speed during the second half of 1971, continued at an even faster pace during 1972. Thus, the general index registered, during the year, the most outstanding jump of the last two decades (7.4 per cent); based on annual averages, this increase is lower (5.7 per cent) (Table 20).

The uptrend in prices was steady over the span of the whole twelve month period, thus reflecting the ongoing rises of all components. Until July the upward movement of prices took place at a relatively slower pace (5.6 per cent at an annual rate) and was mainly pulled along by increases in foodstuffs and some categories of services, especially those connected with hotels and repairs and maintenance of household fixtures. Afterwards, towards the end of the summer, steep rises in some widely consumed foodstuffs sharpened the growth of the general index which, in October, was propelled further upwards by the increment in telephone rates. Greater price boosts finally spread also to the durable and non-durable goods sections, notably those for household use and clothing; as a result, retail prices climbed at an annual rate of 9.5 per cent between July and December. The public authorities' policy of holding down the majority of prices under their control limited

TABLE 20

RETAIL PRICES AND COST OF LIVING

(percentage changes in indexes, 1970 = 100)

Indexes	1971 / 1970	1972 / 1971	Dec. 71 / Dec. 70	Dec. 72 / Dec. 71	July 72 / Dec. 71	Dec. 72 / July 72	Mar. 73 / Dec. 72
					(on a yearly basis)		
RETAIL PRICES							
General index	4.8	5.7	4.7	7.4	5.6	9.5	13.2
Food products	4.0	6.3	4.6	8.8	6.6	11.5	13.5
Non-food products and services	5.4	5.3	4.7	6.4	4.9	8.2	12.6
Clothing	6.2	6.1	5.8	7.2	3.9	11.6	14.3
Hygiene and health	3.9	3.3	3.8	3.3	2.8	4.0	8.8
Durables and non-durables (1)	6.3	5.4	5.4	5.8	3.9	8.2	12.8
Electricity and gas	3.9	—	2.1	0.3	0.8	- 0.5	- 7.3
Housing	3.6	4.1	3.3	4.8	5.2	4.0	14.9
Transport and communications	6.0	5.3	3.1	8.6	5.3	12.8	16.8
Recreational and cultural goods and services	7.7	7.0	9.4	6.3	3.8	9.4	8.4
Other goods and services	5.4	8.6	4.5	11.5	13.8	7.7	20.8
Non-food products	6.1	4.9	4.8	5.3	4.6	6.0	11.9
Services	4.8	5.6	4.6	7.6	5.3	10.5	13.6
COST OF LIVING							
General index	5.0	5.6	4.7	7.4	5.8	9.3	12.2
Food	3.9	6.1	4.2	8.6	7.1	10.2	13.2
Clothing	7.3	6.1	6.1	7.6	3.9	12.5	14.5
Electricity and fuels	4.0	- 0.1	2.0	0.1	1.2	- 1.4	- 6.2
Housing	2.9	2.9	3.1	3.1	3.6	2.3	13.8
Miscellaneous expenditure	6.5	6.4	5.5	7.6	5.8	9.8	11.3

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

the generation of further inflationary impulses: despite the rise in telephone rates, controlled prices in fact rose, between December 1971 and December 1972, by 3.9 per cent; uncontrolled prices registered an increment of 9.0 per cent.

The surge of retail prices picked up further speed during the first quarter of 1973 (13.2 per cent at a yearly rate, between December and March); the upswing affected all the items which are not controlled by the public authorities, with relatively higher peaks for fruit and vegetables, drinks, services and vehicle purchases.

The distribution of income

The final outcome of the above-mentioned employment and wage developments was a higher than average rate of increase for income from dependent labour which, given price and productivity patterns, did not far outstrip the performance of other incomes (10.9 and 8.8 per cent; Table 21). The sector most out of line was agriculture, where income from labour increased by 17.4 per cent compared with a drop for the other incomes (—1.2 per cent). In industry, in 1972 once

TABLE 21

MOVEMENT OF INCOMES BY SECTORS OF ECONOMIC ACTIVITY

Sectors	Annual percentage changes					Percentage ratios: income from dependent labour (1)		
	Income from dependent labour			Other incomes		Gross product		
	1971	1972 (1)	1972 (2)	1971	1972	1970	1971	1972
Agriculture	15.0	17.4		3.0	− 1.2	*20.6*	*22.5*	*25.6*
Industry	11.6	10.0	*10.8*	− 5.8	8.9	*63.6*	*67.4*	*67.7*
manufacturing	*13.3*	*10.9*		*− 7.5*	*10.6*	*66.9*	*71.2*	*71.3*
Services	17.5	11.0		6.9	12.0	*39.7*	*41.9*	*41.7*
excluding housing	*17.5*	*11.0*		*6.8*	*14.0*	*46.1*	*48.4*	*47.8*
PRIVATE SECTOR	13.9	10.7	*11.2*	2.2	8.8	*48.4*	*51.1*	*51.5*
excluding housing	*13.9*	*10.7*		*1.5*	*9.2*	*51.4*	*54.3*	*54.6*
WHOLE SYSTEM	15.1	10.9	*11.3*	2.4	8.8	*53.3*	*56.2*	*56.6*

Source: General Report on the Economic Situation in Italy.
(1) and (2) respectively excluding and including employers' social charges paid for by the government.

again, measures narrowing employers' contributions to social security charges were responsible for keeping labour costs down. At the same time they acted to iron out changes in the two components of income within the sector.

The portion of income paid to dependent labour was, therefore, little above that of the previous year (respectively 56.6 and 56.2 per cent of the entire system's gross product), as a result of the corresponding rise in the percentages for the agricultural and industrial sectors (this rise was considerable in the case of the former and slight for the latter) and of a minor backslide for services.

The balance of payments

The international currency crisis and, in particular, expectations of the lira's devaluation had a marked influence on the Italian balance of payments from June onwards. The greatest impact on the foreign exchange market was experienced in capital movements, although negative effects and distorsions also spilled over into the current account section.

For the entire year, the balance of payments registered a deficit of 747 billion lire, due to a surplus on current account of 843 billion and net capital outflows of 1,345 billion, errors and omissions being negative for 245 billion. Compared with 1971, there was a 138 billion drop in the surplus on current account and increase in net capital outflows of 727 billion (Table 22).

The difficulties met with in the balance of payments during an awkward cyclical phase have necessitated a foreign exchange policy aimed at making sure that negative developments in our foreign accounts do not interfere with the main policy goal of providing adequate support to the revival of domestic economic activity.

On June 27 the convertibility of lira bank notes was discontinued and during the same month the commercial banks and special credit institutions were once again encouraged to borrow from abroad. On January 22, 1973 coinciding with the deterioration in those capital movements items most susceptible to control through exchange rate variations, the two-tier exchange market was set up and the time limits for payment of commercial credits were narrowed in order to

TABLE 22

BALANCE OF PAYMENTS (1)

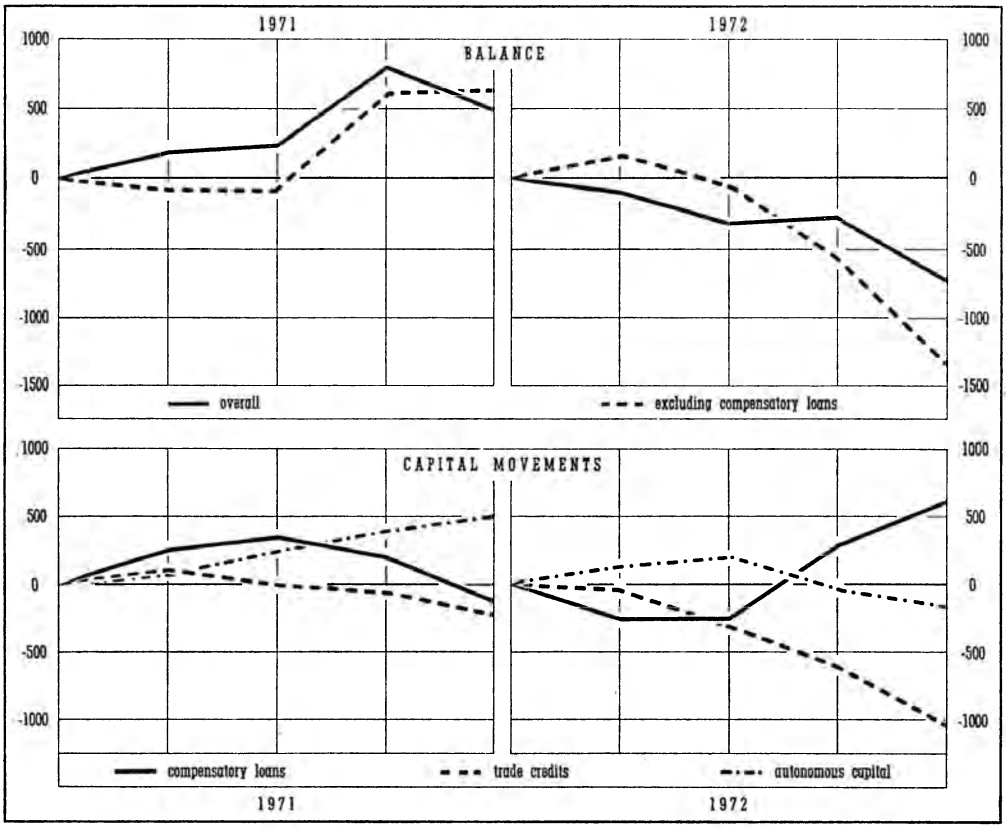
Items	Credit		Debit		Balance	
	1971	1972	1971	1972	1971	1972
			(billions of lire)			
Current account	13,910.6	15,765.4	12,929.4	14,921.9	981.2	843.5
Goods (fob)	*9,274.4*	*10,721.2*	*9,203.0*	*10,720.0*	*71.4*	*1.2*
Services	*3,974.0*	*4,234.8*	*3,215.4*	*3,639.8*	*758.6*	*595.0*
Unilateral transfers	*662.2*	*809.4*	*511.0*	*562.1*	*151.2*	*247.3*
Capital movements	3,373.9	3,578.9	3,748.1	4,924.2	- 374.2	- 1,345·3
Errors and omissions	—	—	117.5	245,2	- 117.5	- 245.2
Total	17,284.5	19,344.3	16,795.0	20,091.3	489.5	- 747.0
Monetary movements (2)	262.0	822.6	751.5	75.6	- 489.5	747.0
Central bank	*156.5*	*566.9*	*629.7*	*74.8*	*- 473.2*	*492.1*
Commercial banks	*105.5*	*255.7*	—	—	*105.5*	*255.7*
Exchange adjustments	—	—	*121.8*	*0.8*	*- 121.8*	*- 0.8*

(1) The data given, which have been approved by the balance-of-payments Committee, differ, in some items, from those published in the General Report on the Country's Economic Situation since they take into account additional readings and estimates made in recent months.— (2) Figures under the balance column with a minus sign indicate an increase in assets or a drop in liabilities.

curtail the formation of ulterior foreign trade credits. Finally, following the dollar's devaluation on February 13, 1973 it was decided also to float the commercial lira along with the financial one. Chart 10 pictures the movement of balance-of-payments aggregates of particular analytical interest during 1972. Speculative pressure against the lira shows up mainly in leads and lags: the anticipation of payments and the delay in receipts, appearing in the statistical breakdown (Table 26) under the item *short-term trade credits,* caused a net outflow of funds equal to nearly 1,000 billion lire, partially offset by net compensatory loans amounting to 600 billion. Had these latter loans not been taken out, the balance of payments would have registered an *autonomous* deficit of around 1,350 billion. Also emerging from the same Chart 10 is the gradual deterioration of those capital movements items, investment and non-compensatory loans, which are usually positive in Italy.

Current accounts were affected first by the development of domestic demand, where signs of recovery determined greater recourse to imports, and then by foreign demand which, especially during the last half of the year, acted as a stimulus to exports (Charts 11 and 12).

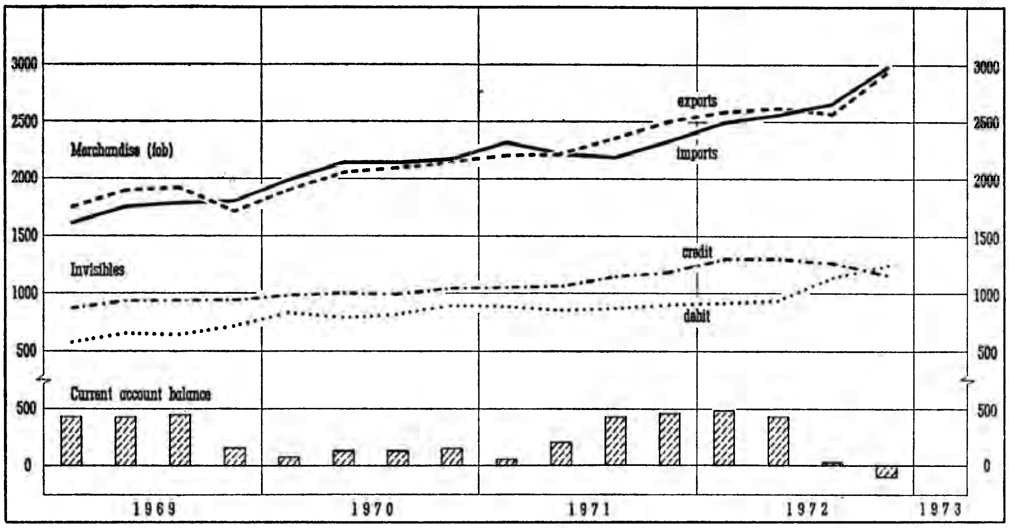
CHART 10



Balance of payments and capital movements

(cumulative quarterly data in billions of lire)

CHART 11

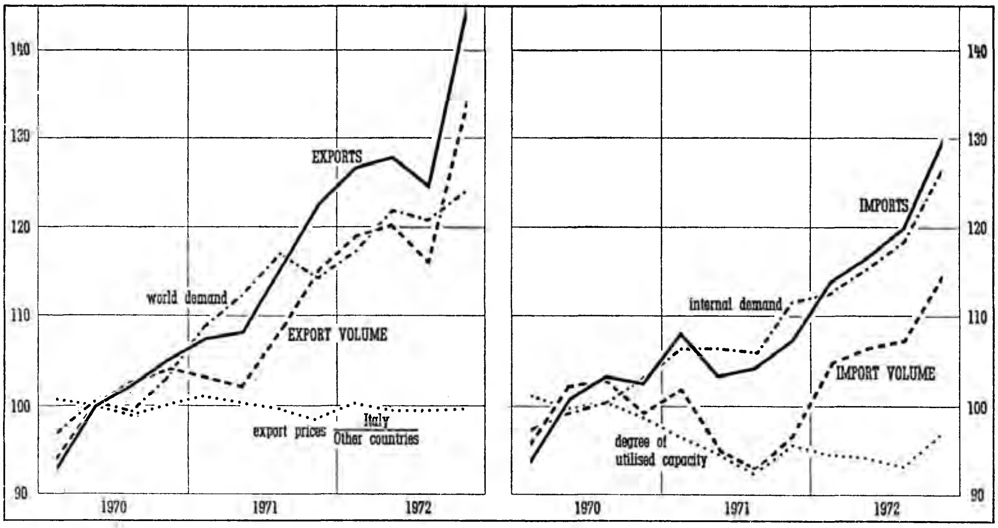


Current account of the balance of payments

(quarterly figures, in billions of lire, seasonally adjusted)

As a matter of fact, the current account surplus would have been higher during the year under study than that registered in 1971 had exceptional factors not caused distortions in the currency flow linked to tourism and emigrants' remittances and increased purchases of non-monetary gold.

CHART 12



Principal factors affecting Italy's foreign trade

(Seasonally adjusted indexes, 1970 = 100)

Merchandise trade

According to customs data gathered by Istat, exports continued to accelerate, increasing by 15.5 per cent; i.e., at a faster rate than in 1971 (13.4 per cent) and the 1967-1971 average (11.3 per cent). For imports, valued *cif,* there was a full about-turn: the fall-off in the growth rate, from 20.6 to 5.8, between 1970 and 1971 gave way to a substantial recovery (13.6 per cent). As a result, the trade deficit dropped from 540 to 429 billion lire and imports now represent 104.0 per cent of exports versus the 105.8 of 1971.

The growth rate of the two trade flows appears even more buoyant if one takes into account the virtual standstill of prices after the previous year's exceptional increase: given the rise in average unit values of 1.2 per cent for exports and 1.5 for imports (respectively 6.1 and 7.8 per cent in 1971), the former grew in real terms by 14.2 per cent and the latter by 11.8 (6.9 and −1.8 per cent in 1971).

Chart 12 shows the trend of exports and imports — both at current values and at constant values — and of the main variables which, according to past experience, are the basic determinants of Italy's foreign trade.

The relative stability of prices after the hefty increases of the past three years was the most outstanding feature of 1972; this seems to reflect the reluctance — in the aftermath of the parity realignment of December 1971 — of the main exporting countries to increase their export prices in terms of their own currencies when these prices, expressed in dollars, had already risen owing to the revaluation of their respective currencies vis-à-vis the dollar.

The sluggish pace of domestic economic activity continued, forcing Italian producers to actively seek the expansion of outlets abroad. Favoured by a slight actual devaluation of the lira stemming from the end-1971 Smithsonian agreements, along with an increase in export prices in national currency of 1.2 per cent (as against an average increase for the OECD countries of about 2.2), they were able to export 14.2 per cent more goods (in volume) than in 1971, despite the fact that overall export by OECD countries only grew by 9 per cent in real terms during 1972. Some contribution towards this outcome may have been derived — with regard to sales to developing countries — from the larger amount of subsidized export financing granted by our credit system.

The annual increase in exports is not the result of any improvement in sales levels throughout the year. The slow growth rhythm of the first six months and the marked acceleration during the second half of the year which characterized 1971, were followed in 1972 by a further upswing in the first quarter, stagnation during the second quarter and a fall-off during the third. In fact, had the export levels of end-1971 merely held steady throughout 1972, there would have been an increase of circa 8 per cent. This value rose mainly because of the sudden upswing during the last quarter of 1972 (in particular during December). It is not yet clear what factors lie behind this increase; uncertainties linked with the changeover from turnover tax to VAT could have urged exporters to speed up foreign sales. The exceptional nature of this increase seems to be confirmed by data for the first months of 1973, which show particularly low growth rates for exports.

Due to increased sales in 1972, our share of world exports of manufactured goods, having reached a peak of 7.3 per cent in 1968 and then dropped to 7.2, once again rose, this time to about 7.4 per cent.

Imports advanced throughout all of 1972, showing a tendency to accelerate during the second half of the year (this speed-up continued over into the first months of 1973). Our foreign purchases hovered closely around the performance of the two basic variables (domestic demand and degree of productive capacity utilized), that they have been closely bound to during past years. Thus, an acceleration of their growth rate seems likely during 1973 if expectations of a further revival of productive activity are confirmed. Another factor contributing to this increase was the gap between domestic and import price patterns (the former grew by about 4 per cent as against 1.5 for the latter), thus favouring foreign goods over domestic ones.

The most dynamic categories of goods in the recovery of imports were finished consumer goods (in particular non-foodstuffs) and semi-finished goods; on the other hand, a below-average increase was registered for producer goods and the *plants, machinery and equipment* subheading of capital goods. The standstill in purchases of energy sources can be linked to the 6 per cent drop in exports of refined products.

Export increases were heaviest for finished consumer goods and finished capital goods (particularly industrial vehicles). Sales of food-stuffs augmented at a slightly higher rate than purchases; however, because of the greater initial weight of imports, the deficit registered a further increase.

The main changes in the geographical distribution of our trade resulted, with regard to imports, from another rise in purchases from the EEC — representing 45 per cent of all imports — in particular from France, Belgium and the Netherlands; from the recovery of imports from the Socialist countries (excluding the USSR) and from the very much below average increase in those from the United States and the developing countries (oil sales were of considerable importance to the latter). In exports the EEC countries also played a larger role (especially France), receiving 45 per cent of our total sales; exports to the United Kingdom soared and those to the developing countries were above average.

Table 23 lists the percentages, of our total imports and exports, registered by the different goods categories from 1951-1955 until today.

On the imports side, and in terms of percentages, the major variations consisted in the continually dwindling weight of raw materials, which dropped from a quarter of the total to less than a tenth, and the upward swing, from 1956-1960 on, of finished consumer goods (from 25 to 35 per cent). Within this category the most dynamic sections were durable goods, whose percentage tripled, and *other non-durable goods* (this section mainly consists of products of the textile, clothing and footwear, chemicals and rubber industries). The percentage for finished capital goods also registered a leap forward: it should be noted that increases in this sector took place between the five-year periods 1956-1960 and 1961-1966 and that afterwards it went through a period of relative stagnancy. Within this category, the *plants, machinery and equipment* section registered the greatest increase.

On the exports side, the most noteworthy development was the steady increase of finished capital goods, which moved from 17 per

TABLE 23

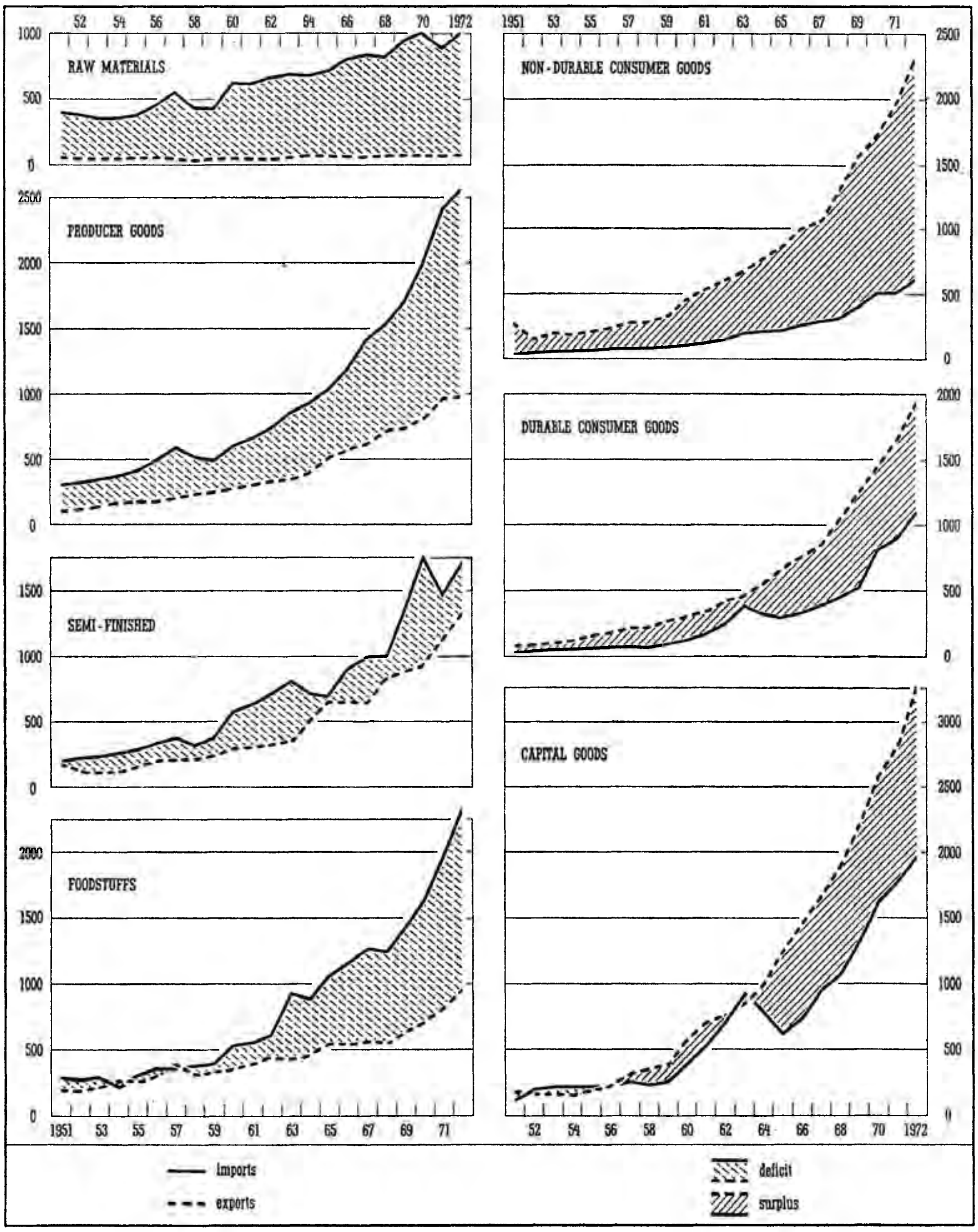
DISTRIBUTION OF ITALY'S FOREIGN TRADE BY COMMODITY CLASSES

(percentage distribution in current values - five-year averages)

Items	IMPORTS 1951-1955	IMPORTS 1956-1960	IMPORTS 1961-1965	IMPORTS 1966-1970	IMPORTS Average 1971-1972	EXPORTS 1951-1955	EXPORTS 1956-1960	EXPORTS 1961-1965	EXPORTS 1966-1970	EXPORTS Average 1971-1972
Raw materials	24.5	21.9	15.8	12.6	9.0	5.2	2.9	1.8	1.1	0.7
Producer goods	23.2	23.5	20.2	22.2	23.5	13.0	12.4	11.0	10.5	9.6
fuel and power	*19.2*	*17.9*	*13.6*	*14.9*	*15.8*	*7.7*	*7.0*	*5.1*	*5.1*	*4.7*
others	*4.0*	*5.6*	*6.6*	*7.3*	*7.7*	*5.3*	*5.4*	*5.9*	*5.4*	*4.9*
Semi-finished	15.8	17.3	16.9	17.1	15.0	13.2	13.0	12.7	12.2	12.2
Finished consumer goods	24.4	25.1	30.0	31.8	34.9	51.7	50.9	47.8	46.1	47.5
foodstuffs	*18.1*	*17.8*	*19.1*	*19.2*	*20.3*	*22.7*	*19.8*	*13.4*	*9.3*	*8.7*
others non-durable	*3.1*	*3.4*	*4.1*	*5.0*	*5.2*	*19.5*	*17.8*	*20.2*	*20.3*	*21.1*
durable	*3.2*	*3.9*	*6.8*	*7.6*	*9.4*	*9.5*	*13.3*	*14.2*	*16.5*	*17.7*
Finished capital goods	12.1	12.2	17.1	16.3	17.6	16.9	20.8	26.7	30.1	30.0
plants, machinery, equipment	*9.5*	*9.4*	*13.6*	*13.0*	*14.0*	*11.9*	*14.4*	*20.2*	*24.4*	*24.2*
industrial motor vehicles	*1.8*	*2.0*	*2.6*	*2.4*	*2.5*	*3.8*	*4.9*	*5.0*	*4.0*	*4.0*
others	*0.8*	*0.8*	*0.9*	*0.9*	*1.1*	*1.2*	*1.5*	*1.5*	*1.7*	*1.8*
Total	100	100	100	100	100	100	100	100	100	100

cent in 1951-1955 to settle during the last years at circa 30 per cent. This rise is to be found wholly in the *plants, machinery and equipment* section whose percentage has doubled until it now accounts for nearly a quarter of all Italian exports. The other important structural

CHART 13



Trend of Italy's foreign trade by commodity classes

(billions of current lire)

Calculated from Istat data

change concerns the finished consumer goods category which, while still accounting for nearly half our foreign sales, underwent considerable changes in its make up: foodstuffs fell from 23 to 9 per cent while durable goods moved, correspondingly, from 10 to circa 18 per cent; the percentage for *other non-durable goods* instead held steady (around 20 per cent), as did that for the semi-finished goods category.

The graphs in Chart 13 allow us to follow changes in the structure of Italian trade from 1951 until today. From them it can be clearly noted that the growing deficit in the raw materials, producer goods, semi-finished goods and foodstuffs categories was offset, in an industrial-processing economy like Italy's, by the growing surplus of the finished goods manufacturing sectors.

Exchange of services

The transport balance registered a deficit of 130 billion lire as against 115 in 1971 (Table 24). These results should be linked with the drop in the air transport surplus and increase in the overland transport deficit, while the deficit for sea transport remained even.

The quantity of merchandise imported by sea rose by 6 per cent, with a higher growth rate for dry cargo (8 per cent) than for liquids (5 per cent). On average, there was a fall-off in freight rates (between 1971 and 1972) for both dry and liquid goods; more specifically, during the first half of the year they stood well below the levels registered for the corresponding months of 1971, rising above them during the second half. The performance of freight rates affected unit transport costs which also fell: expenditure for shipping imports amounted to 782 billion; that is, 6 billion less than in the previous year. This decline only showed up in the Italian fleet's portion of freight costs for imports while the rest of the world's increased slightly.

Italian merchant marine revenues for transporting export merchandise or merchandise traded among third countries grew, overall, by scarcely 2 per cent; this was due to the above-mentioned trend of freight rates and to the drop in quantity of goods loaded in Italy, offset by increased trade with third countries. On the whole, the maritime sector registered a deficit of around 79 billion, roughly the same as in 1971.

TABLE 24

TRANSPORT BALANCE

(billions of lire)

Items	Shipping 1971	Shipping 1972	Overland (1) 1971	Overland (1) 1972	Air 1971	Air 1972	Total 1971	Total 1972
RECEIPTS	*694.0*	*704.9*	*25.0*	*26.3*	*194.5*	*199.2*	*913.5*	*930.4*
Freight:								
for export	118.8	115.5	—	—	18.7	15.5	137.5	131.0
among third countries, in transit, for mail	319.0	332.6	25.0	26.3	7.3	7.3	351.3	366.2
Passenger fares (2)	90.6	87.9	—	—	131.0	137.0	221.6	224.9
Expenditure of foreign fleets in Italy	165.6	168.9	—	—	37.5	39.4	203.1	208.3
PAYMENTS	*773.8*	*783.8*	*155.0*	*162.7*	*99.4*	*113.9*	*1,028.2*	*1,060.4*
Freight for import (3)	557.5	565.9	155.0	162.7	23.1	25.4	735.6	754.0
Passenger fares	10.0	9.7	—	—	43.8	48.6	53.8	58.3
Expenditure of the Italian fleet abroad	206.3	208.2	—	—	32.5	39.9	238.8	248.1
BALANCE	*- 79.8*	*- 78.9*	*- 130.0*	*- 136.4*	*95.1*	*85.3*	*- 114.7*	*- 130.0*

(1) Including oil pipeline rights.— (2) Excluding fares taken by the Italian merchant marine fleet (43.1 in 1971 and 44.2 in 1972) and the Italian commercial air fleet (47.7 in 1971 and 47.4 in 1972) for transporting Italian passengers.— (3) Excluding freight receipts of the Italian merchant marine fleet (230.8 in 1971 and 215.9 in 1972) and the Italian commercial air fleet (13.0 in 1971 and 16.0 in 1972).

The deterioration in the deficit of the overland transport section, which climbed to nearly 136 billion, was the result of a larger increase in the amount of merchandise imported than exported by railroad.

With regard to air traffic, on the revenues side the items concerning passenger transport and the expenditure of foreign fleets in Italy registered a slight increase while all outgoing flows soared. Consequently, the surplus fell from 95 to 85 billion.

The foregoing pattern of surplus and deficit figures in the transport balance resulted in the contribution of the Italian air and sea fleets, in the form of savings and gains in foreign currency of about 755 billion, 12 billion less than during the previous year.

Foreign travel

The tourism balance closed with a surplus of 655 billion lire, more or less equal to that of the previous year. The standstill in the net movement of foreign currency reflected a faster increase on the outflow rather than the influx side: foreign currency outlays for tourism in fact rose by 16.9 per cent; receipts by 7.6 per cent.

Overnight stays of foreign tourists in Italian hotels rose by 3.4 per cent (3.8 if one also includes tourists staying elsewhere). The rise in prices of the main tourist services in Italy during 1972 (6.9 per cent) and increase in the length of the tourists' overnight stays — although the latter only concerns hotels below the first class category — do not seem to offer sufficient justification for the behaviour of receipts. In fact, the provision of June 27, forbidding the crediting of lira bank notes in capital accounts, was responsible for distorsions in the currency inflow linked with tourism. This can also be clearly seen in data on Italian tourism abroad, since the increase in outflows, especially towards the end of the year, is too high to have been solely caused by a rise in the number of Italians visiting foreign countries.

Analysis of tourism trends during 1972 seems to confirm the importance events on the foreign currency scene have on the development of flows stemming from tourism (Table 25). During the second half of the year, and in particular during the fourth quarter, as the discount on the lira bill rose, currency receipts dropped by 8 per cent — even

TABLE 25

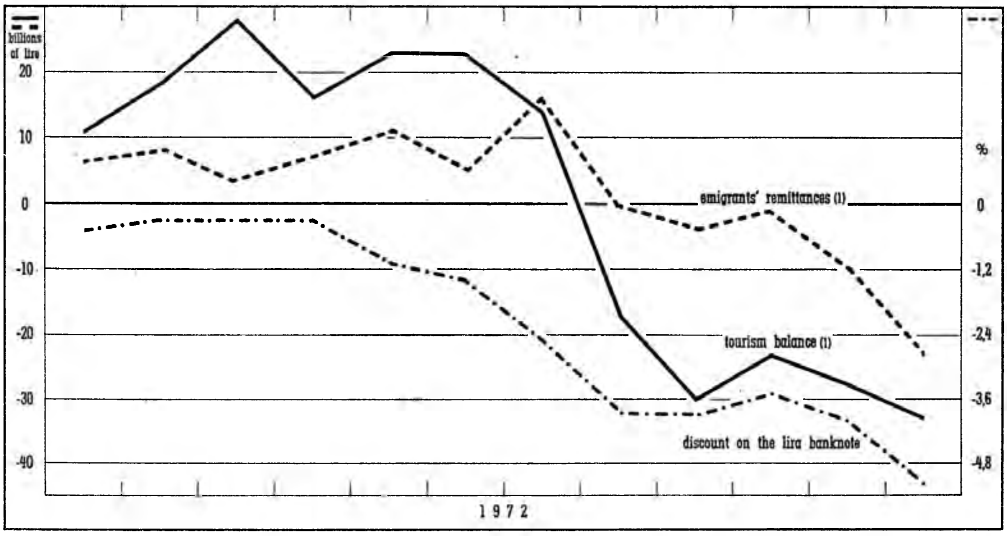
TOURISM DEVELOPMENT IN 1972

(billions of lire)

Items	1972				% variations 1972/1971			
	1st half	quarters III	quarters IV	Year	1st half	quarters III	quarters IV	Year
Tourism: credits	506.9	511.3	248.3	1,266.5	20.3	5.5	- 8.1	7.6
debits	216.6	216.5	178.3	611.4	- 13.5	36.6	56.1	16.9
Balance . . .	290.3	294.8	70.0	655.1				
Overnight stays of foreigners in Italian hotels (thousands)	18,379	24,250	5,252	47,881	6.2	1.6	1.9	3.4
Index of prices of « tourism » services (1970=100)	110.6	113.7	115.5	112.6	6.3	7.1	7.8	6.9
Discount on the lira bank note in respect to the official exchange rate in Switzerland (%)	- 0.6	- 3.4	- 4.2	- 2.2				

though the number of tourists' overnight stays in Italy and the prices for tourism services rose, respectively, by 1.9 and 7.8 per cent — while outflows registered an upswing of 56 per cent. The relationship between the deterioration in the tourism balance and the depreciation of the lira emerges plainly in Chart 14.

CHART 14



Tourism balance, emigrants' remittances and discount on the lira banknote

(1) Absolute variations between 1971 and 1972.

Substantiation of the alteration in tourism flows described above was obtained, in particular, with regard to relations with Germany. Following the OECD agreements described in last year's Report, some central banks have begun, since the end of 1969, to exchange information on purchases and sales of foreign bank notes in their respective countries. Using data provided by the German central bank, it has been possible to reconstruct the balance of tourism movements in lire and therefore compare its development with that of the rates for our bank note on foreign exchange markets (Table 26).

The inflow of foreign currency from Italian workers' earnings and remittances amounted to 745 billion lire, an increase of 2.7 per cent over the previous year. During the year, foreign currency remittances followed the same pattern as tourism flows (Chart 14); in fact, they rose during the first six months, compared with the corresponding period of 1971, by circa 13 per cent, whereas during the second half of the year they registered a fall-off of 6 per cent. The fact that lira could be purchased abroad at a more favourable exchange rate was most probably behind the reduction in remittances in foreign currency in favour of those, nonquantifiable, in lire.

The deficit in capital income took another turn for the worse last year, moving from 19 to 51 billion, mainly as the result of the servicing of loans taken out abroad by Italian institutions.

The deficit under *other services* almost doubled, rising to 279 billion, due to a deterioration in the balances on all items under that section.

The main reason for the fall, from 192 to 104 billion, in the public sector's net transfers was the reduced deficit vis-à-vis FEOGA (European Agricultural Fund).

TABLE 26

BALANCE ON TOURISM MONETARY FLOWS WITH GERMANY IN 1972

(billions of lire)

Items	Quarters			
	I	II	III	IV
Balance: in foreign currency	26.7	55.5	91.5	17.4
in lire	15.5	28.0	52.1	24.6
overall	42.2	83.5	143.6	42.0
Percentage in lire over total (%)	37	34	36	59
Discount on the lira banknote in respect to the official exchange rate in Switzerland (%)	- 0.4	- 0.9	- 3.4	- 4.2

Capital movements

Net capital outflows in 1972 amounted to 1,345 billion lire. If, in order to make a homogeneous comparison with past results, compensatory loans are deducted from the total, then this figure rises to 1,695 billion or three times as much as the previous year's total, similarly calculated, of 240 billion (Table 27). If one then includes the probable outflow of funds through the export of Italian bank notes, no longer convertible after June, this net outflow becomes greater even than the record high reached in 1969 (2,310 billion).

TABLE 27

CAPITAL MOVEMENTS

(billions of lire)

Items	Credit 1971	Credit 1972	Debit 1971	Debit 1972	Balance 1971	Balance 1972
FOREIGN CAPITAL	2,288.6	2,456.6	1,301.2	1,896.9	987.4	559.7
Investments:						
direct	476.4	475.4	152.8	111.9	323.6	363.5
portfolio	301.8	387.1	232.0	355.9	69.8	31.2
other	26.3	38.7	10.0	9.8	16.3	28.9
Loans:						
private	882.1	1,142.6	475.9	521.3	406.2	621.3
government or government-guaranteed	239.4	64.6	241.4	235.9	- 2.0	- 171.3
other public agencies	123.4	203.0	46.4	130.4	77.0	72.6
Trade credits:						
medium- and long-term	162.7	145.2	142.7	153.5	20.0	- 8.3
short-term	76.5	—	—	378.2	76.5	- 378.2
ITALIAN CAPITAL	1,085.3	1,122.3	2,446.9	3,027.3	-1,361.6	-1,905.0
Investments:						
direct	152.7	188.3	401.8	313.0	- 249.1	- 124.7
portfolio	246.6	316.6	364.3	727.8	- 117.7	- 411.2
other	0.1	0.4	2.6	4.8	- 2.5	- 4.4
Loans:						
private (1)	119.9	119.7	175.6	257.0	- 55.7	- 137.3
government or government-guaranteed	23.6	21.5	65.8	28.1	- 42.2	- 6.6
Trade credits:						
medium- and long-term	542.4	475.8	496.3	550.5	46.1	- 74.7
short-term	—	—	382.7	594.2	- 382.7	- 594.2
Bank note remittances	—	—	557.8	551.9	- 557.8	- 551.9
Balance	—	—	—	—	- 374.2	-1,345.3

(1) Loans tied to exports, net of repayments, were equal to 21.9 billion in 1971 and 11.8 billion in 1972.

The size of this deterioration was the result of the rapid expansion of speculative components linked with domestic and international currency crises. Thus, ample use was made of potentials to carry out short-term movements linked with the financing of current transactions, and the formation of *short-term* positions was observed — in particular through portfolio investments, whose speculative component prevailed over that connected with traditional factors, such as interest rates.

The net amount of direct foreign investments grew by 40 billion, in connection solely with a fall-off on the disinvestment's side from 153 to 112 billion.

The surplus relative to foreign portfolio investments, equalling 31 billion, was less than half last year's amount, whereas the volume of underlying transactions climbed from 534 to 743 billion: the greater share of this activity was in listed stocks and can for the most part be ascribed to speculative factors.

Direct Italian investments abroad gave rise to a net outflow of 125 billion, versus 249 in 1971. More specifically, net financing of oil exploration, amounting to 33 billion, was reduced by about a third; financial participation in foreign companies by Italian enterprises and commercial banks declined, respectively, from 78 to 57 and from 27 to 23 billion.

Italian portfolio investments abroad, net of disinvestments, amounted to 411 billion, circa four times more than in the previous year. The increase in underlying transactions mainly concerned listed securities (9 per cent), mutual funds (12 per cent) and, above all, bonds (72 per cent). The larger part of bond activity refers to transactions on the international market, although a small part of the outflow concerns new issues.

In fact, Italian banks participating in international consortia underwriting and placing foreign loans sold only 85 billion worth of securities to residents. More specifically, issues of loans denominated in dollars dropped from 64 to 52 per cent of the total while securities denominated in the same currency and placed with residents increased from 42 to 66 per cent. In effect, the majority operations regarding Italian portfolio investments concern dollar-denominated Eurobonds.

Bank note remittances reached a volume of 552 billion, roughly the same as in 1971. As already mentioned, this outflow took place almost entirely during the first half of the year: after the measure of June 27, only bank notes remitted from abroad prior to that date were credited in capital accounts.

Foreign private and state-guaranteed loans resulted in a net inflow of 450 billion, 46 billion more than in the previous year. If one excludes operations carried out on the initiative of the monetary authorities, net foreign loans amounted to 100 billion, compared with 540 for the year before. Private Italian loans to foreigners gave rise to a deficit of 137 billion lire, 82 billion higher than in 1971; the net outflow resulting from public loans dropped from 42 to 7 billion. The change in the former's performance can for the most part be attributed to lira-denominated securities issued in Italy by international agencies which amounted to 115 billion versus 40 in 1971.

In the medium- and long-term section, import and export credits moved from surpluses of, respectively, 20 and 46 billion to deficits of 8 and 75 billion between 1971 and 1972. More specifically, the performance of export credits was affected, with a time lag of about a year, by wide swings in overall funds available for insurance purposes.

Speculative expectations seem to have had a particularly heavy impact on the short-term section, where import credits passed from a net inflow of 77 to an outflow of 378 billion and the export credits deficit, equalling 594 billion, worsened by 211 billion.

In May 1972, the permissible time lag for the prepayment of imports was extended from 30 to 90 days. In January 1973, this limit was again cut back to 30 days while the permissible delay for the deferred payment of exports was reduced from 360 to 90 days.

Monetary movements

The 1972 balance-of-payments deficit was financed for 492 billion lire by tapping the net foreign assets of the central monetary institutions and for the remaining 255 billion by increasing the net foreign debtor position of the commercial banks. The deterioration in foreign accounts, registered mainly during the second half of the year, was kept within bounds by the compensatory loans taken out by the special credit institutions and listed under capital movements.

At the end of the year, the total net assets held by the Banca d'Italia and the UIC amounted to 3,546 billion, 3,460 of which in net official reserves; the banks' net foreign position registered a deficit of 351 billion (Table 28).

The drop in official reserves almost entirely concerned dollar holdings. No marked changes were to be observed in gold and gold-

TABLE 28

FOREIGN POSITION OF THE BANCA D'ITALIA, THE UFFICIO ITALIANO DEI CAMBI AND ITALIAN BANKS

(month-end figures)

Items	December				March 1973 (1)
	1971	1972	1971	1972	
Banca d'Italia - UIC	*(millions of dollars)*		*(billions of lire)*		
Official reserves:					
Reserves in gold or with gold guarantee (2)	3,470.9	3,563.6	2,164.7	2,223.6	2,218.0
Gold	2,883.9	2,883.0	1,802.4	1,801.9	1,804.3
Special drawing rights	227.9	341.4	142.5	213.4	213.4
IMF reserve position	355.9	336.0	217.8	206.3	200.3
Net EMF position	3.2	3.2	2.0	2.0	—
Convertible currencies	3,063.2	2,225.2	1,781.2	1,293.7	1,141.4
US dollars	2,432.1	1,629.7	1,414.2	947.5	769.2
Swiss francs	150.1	157.9	87.3	91.8	105.9
Deutschemarks	425.2	386.5	247.2	224.7	231.4
others	55.8	51.1	32.5	29.7	34.9
Total gross official reserves	6,534.1	5,788.8	3,945.9	3,517.3	3,359.4
Short-term liabilities	– 105.9	– 99.2	– 61.6	– 57.7	– 259.6
Central bank swaps	—	—	—	—	– 244.0
Others	– 105.9	– 99.2	– 61.6	– 57.7	– 7.2
Total net official reserves	6,428.2	5,689.6	3,884.3	3,459.6	3,108.2
Medium- and long-term position:					
Foreign securities: in foreign currency	38.6	40.4	22.4	23.5	22.1
in lire	144.6	152.4	84.1	88.6	101.6
Consolidated accounts	53.7	52.4	31.3	30.5	30.5
Italian securities in foreign currency	254.2	244.4	148.0	142.1	138.4
Special Drawing Rights account	– 212.0	– 318.1	– 132.5	– 198.8	– 198.8
Total	279.1	171.5	153.3	85.9	93.8
Total Banca d'Italia - UIC	6,707.3	5,861.1	4,037.6	3,545.5	3,202.0
Banks					
Assets	13,266.0	19,869.8	7,714.2	11,552.2	. . .
Liabilities	13,429.6	20,472.6	7,809.1	11,902.8	. . .
Balance	*– 163.6*	*– 602.8*	*– 94.9*	*– 350.6*	*– 469.8*

(1) Provisional data.— (2) Reserves in gold or with gold guarantee are calculated on the basis of the exchange rate of 703,297.396 lire per fine kilogramme, which was fixed by Law-decree n. 14 of January 28, 1960 and is calculated from a price of 35 dollars per ounce of gold and an exchange rate of 625 lire per dollar.

TABLE 29

THE BANKS' ASSETS AND LIABILITIES IN THE MAIN EUROCURRENCIES

(end-period data in billions of lire)

Items	1964	1965	1966	1967	1968	1969	1970	1971	1972
Dollars									
assets	374.0	853.6	1,169.5	1,254.5	1,825.1	2,770.4	3,977.4	4,887.5	7,593.2
liabilities	781.2	888.4	1,061.9	1,241.4	1,549.1	2,759.4	4,184.6	4,579.9	7,753.1
balance	*– 407.2*	*– 34.8*	*147.6*	*13.1*	*276.0*	*11.0*	*– 207.2*	*307.6*	*– 159.9*
Swiss francs									
assets	30.9	40.0	57.7	77.8	183.3	270.5	413.9	705.1	578.0
liabilities	36.6	49.7	67.7	106.6	117.6	220.3	371.9	479.7	532.6
balance	*– 5.7*	*– 9.7*	*– 10.0*	*– 28.8*	*65.7*	*50.2*	*42.0*	*225.4*	*45.4*
Sterling									
assets	25.3	25.8	50.9	34.9	36.9	77.6	51.6	47.5	168.1
liabilities	74.5	48.8	66.0	82.0	63.2	61.4	120.2	286.1	101.8
balance	*– 49.2*	*– 23.0*	*– 15.1*	*– 47.1*	*– 26.3*	*16.2*	*– 68.6*	*– 238.6*	*66.3*
Deutsche marks									
assets	34.4	44.9	41.1	125.2	291.6	398.0	614.1	732.4	1,193.2
liabilities	14.6	54.1	67.6	84.2	201.1	370.8	483.1	955.5	1,646.8
balance	*19.8*	*– 9.2*	*– 26.5*	*41.0*	*90.5*	*27.2*	*131.0*	*– 223.1*	*– 453.6*
Other Eurocurrencies									
assets	7.7	14.0	94.1	21.5	33.0	5.0	38.8	60.9	219.8
liabilities	6.2	5.4	40.2	6.6	8.8	26.2	55.8	69.7	157.0
balance	*1.5*	*8.6*	*53.9*	*14.9*	*24.2*	*– 21.2*	*– 17.0*	*– 8.8*	*62.8*
TOTAL EUROCURRENCIES assets	472.3	978.3	1,413.3	1,513.9	2,369.9	3,521.5	5,095.8	6,433.4	9,752.3
TOTAL EUROCURRENCIES liabilities	913.1	1,046.4	1,303.4	1,520.8	1,939.8	3,438.1	5,215.6	6,370.9	10,191,3
TOTAL EUROCURRENCIES *balance*	*– 440.8*	*– 68.1*	*109.9*	*– 6.9*	*430.1*	*83.4*	*– 119.8*	*62.5*	*– 439.0*

guaranteed reserves, with the exception of special drawing rights which grew as a result of the third annual allocation in January 1972.

At the beginning of 1973, speculative pressures on the lira caused a further drop in net official reserves of 316 billion lire during January, due almost entirely to a 184 billion decrease in convertible currencies and a 129 increase in short-term liabilities, which mainly consisted in swaps with the Danish and Belgian central banks. During February and March no particular variations in currency reserves were registered, following the adoption, first, of the two-tier market and, second, of the floating exchange rate.

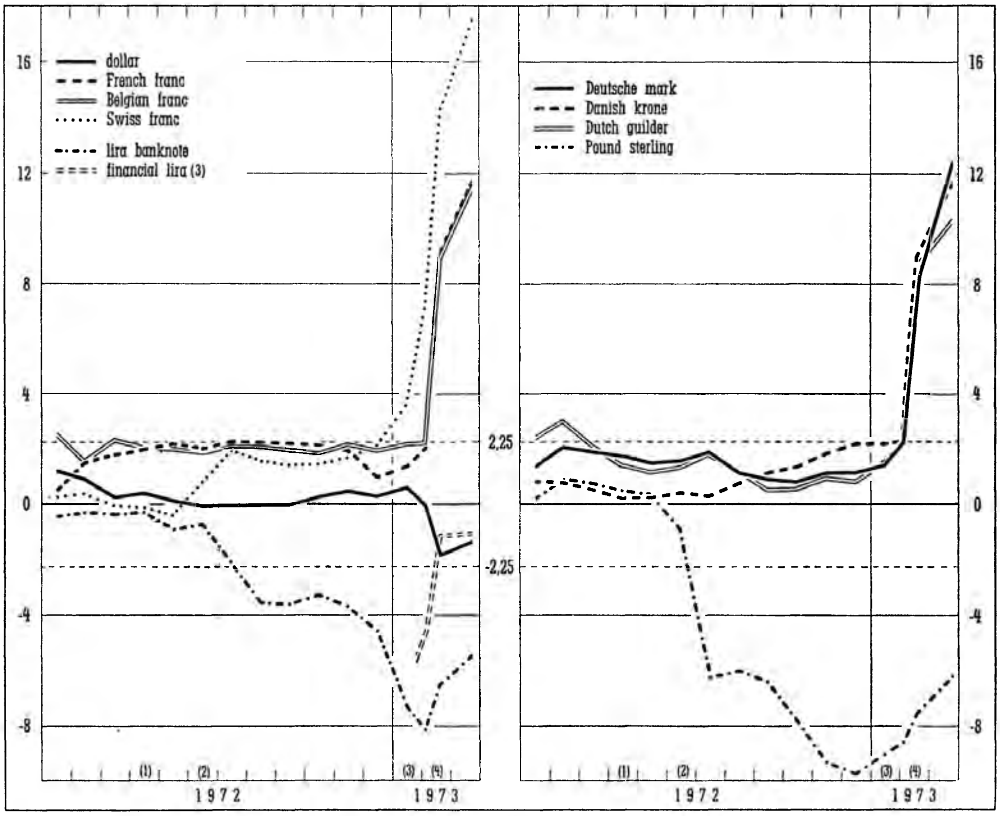
Repeated disruptions on the exchange market which characterized 1972 from June onwards and the downward plunge of the level of reserves forced the monetary authorities not only to encourage fund raising abroad by the special credit institutions but also, as a corrective measure, to regulate the banks' foreign position, allowing them to take up a net foreign debtor position. At end-1972 this position registered a deficit of 351 billion, 255 higher than the previous year. An analysis of the gross flows reveals a marked increase in the banking system's foreign intermediation: in fact, overall assets and liabilities, in currency and in lire, vis-à-vis non residents, rose by 7,931 billion lire during 1972. It is mainly on the Eurocurrency market that the Italian banks have increased their intermediation: during recent years, alongside operations in Eurodollars, those in Deutsch Euromarks and Swiss Eurofrancs have become increasingly important (Table 29).

Spot and forward rates for the lira

In the months following the Smithsonian agreements of December 1971, the lira's spot rate, although at a discount in relation to the key currencies, kept easily within the new, wider fluctuation margins. The premium of the Belgian franc and the Dutch guilder vis-à-vis the lira, after peaking during the first months of the year, gradually dropped until April, when they were quoted below the 2.25 per cent margin (the maximum permitted spread between the rates for two Community currencies as established in the Basle agreements, in force as of April

24). The dollar, quoted at a premium on the lira at the beginning of the year, drew near the central rate during the second quarter when the Italian balance of payments was showing positive results (Chart 15).

CHART 15



Trend of spot rates

(percentage variations, indicating the premium or discount, are calculated in relation to: the central rate for the lira, for foreign currencies; the official exchange rate for the lira bank note until January 22; the commercial lira, for the financial lira and lira bank note, from January 23)

(1) Agreement to narrow Community exchange-rate fluctuation margins.— (2) Floating of the sterling. Discontinuation of the convertibility of lira banknotes.— (3) Introduction of the two-tier exchange market; the graph shows the rates for the commercial lira after January 23. Floating of the Swiss franc.— (4) Devaluation of the dollar. Floating of the commercial lira.

The lack of effective controls on short-term speculative movements and the difficulties involved in keeping the currencies of countries with different cyclical patterns within a narrow band added fuel to speculative tensions on the currency markets from June onwards, finally forcing their closure from the 23rd to the 27th of the month. The international crisis of end-June involved first the pound sterling, which moved outside the fluctuation margins in relation to the dollar and the EEC currencies, and then the lira. Our currency hovered near the maximum depreciation limit of the Community *snake* and was only kept there at the cost of massive interventions.

With still no let-off in speculative pressures against the lira, as the new year began, the authorities decided to introduce a two-tier exchange market that came into force on January 23. The floating of the financial lira, which dropped several points compared with the commercial lira's rate, was followed almost immediately by that of the Swiss franc.

During February further speculative movements against currencies which seem most likely to appreciate vis-à-vis the dollar, caused the currencies markets to close for a second time. When they reopened the first substantial change in the end-1971 monetary realignment had been made; the dollar had been devalued and yen and commercial lira were now floating.

The forward market for the lira also followed diverging trends in 1972, the pivotal event being the June currency crisis. A first stage, when the forward lira was quoted at a premium on the dollar, was followed by an about-turn due to devaluation expectations surrounding the lira. The lira's depreciation reached its highest point, in particular in the one-month rate, in July and December, with peaks of 12 per cent. The introduction of the two-tier market in Italy, the devaluation of the dollar and, following this, the depreciation of the lira after it was floated, helped to put our currency back at a premium on the dollar during March 1973.

Public finance

In 1972, despite the economy's need for a vigorous expansion of demand in the public sector also aimed at solving structural problems, the impulses produced by the public administration were chiefly generated only indirectly through an increase in the private sector's disposable income.

Public works brought to completion were nearly stationary, despite the steep rise in their costs. Although activity in this sector was also crippled by delays, as many functions were transferred from the central administration to the newly set up Regions which were not yet ready to perform their new tasks, by and large it reflected structural weaknesses in the decision-making and implementation processes.

The growth of the private sector's disposable income was mainly the result of provisions enacted in the middle of the year: increases in pensions, exemptions granted in indirect taxation, aimed at smoothing over the transition from IGE (turnover tax) to VAT (value added tax) and the Treasury's further absorption of part of employers' social security contributions.

With regard to the tax system's automatic mechanisms, the stabilizing effect of indirect taxation, affected by the performance of demand, was contrasted by the pro-cyclical action of direct taxation, which was particularly marked this year.

As for 1973, despite some predictable improvement in the quantity of public works carried out, heavy expansion in this section of public demand is not foreseeable. Moreover, as far as the government is concerned, expenditure commitments for direct investment have registered sharp fall-offs over the last two years, and their effect on 1973 cannot be neutralized by the recently decided interventions for school building, agriculture, harbours and land protection.

From the standpoint of 1973 fiscal policy, the substitution of VAT for IGE, local taxes on consumption and other minor taxes is of considerable importance: it is difficult at the moment to predict the effects of these changes, which might necessitate compensatory interventions. Moreover, with regard to the impact on prices, in addition to the asymmetrical effects among sectors where the overall tax burden has increased and those in which it has dropped, it should also be noted that the delay in publishing VAT regulations (and some rates) and hence the public's lack of familiarity with the new tax unleashed upward pressures on prices caused by other factors.

The budget calculated on a cash basis, given the continual growth of expenditure arrears, registered a deficit far below that for the budget calculated on an obligation basis. The increase was not exceptional with respect to the previous year (from 3,050 to 3,620 billion), despite the standstill in revenues from indirect taxation, because of expanded direct taxation and payments behaviour — among which there was a marked decrease in transfers to INPS (National Social Security Institution) and in indirect tax refunds.

The overall rise in payments can basically be put down to employees' salaries, government purchases of goods and services and transfers to the autonomous government agencies. The expansion of tranfers to local authorities is the result of handing over to the recently set up Regions some of the functions carried out by the central government until March 1972.

Overall tax revenues grew by 5.6 per cent (versus 9.3 in 1971): more specifically, while the receipts from direct taxation increased by 20 per cent, those from indirect taxation remained more or less steady. The reasons behind this trend for 1972 can be attributed to both the general performance of the economic system and the effects of discretionary measures.

The swell in revenues from income and wealth taxes can be explained by noting that: *a)* disposable income, at current prices, has grown over the last year at an average yearly rate of circa 11 per cent which, due to the progressiveness of this type of taxation involves an even greater increase in yield; *b)* strikes of personnel in direct tax bureaus which occurred in 1969 and 1970 had caused a drop in revenues which carried over even into the first half of 1971; *c)* the rise in the salaries and wages portion of total national income, sparked off by increases registered in the 1970s, could have determined a lower impact of tax evasion on the total of disposable income.

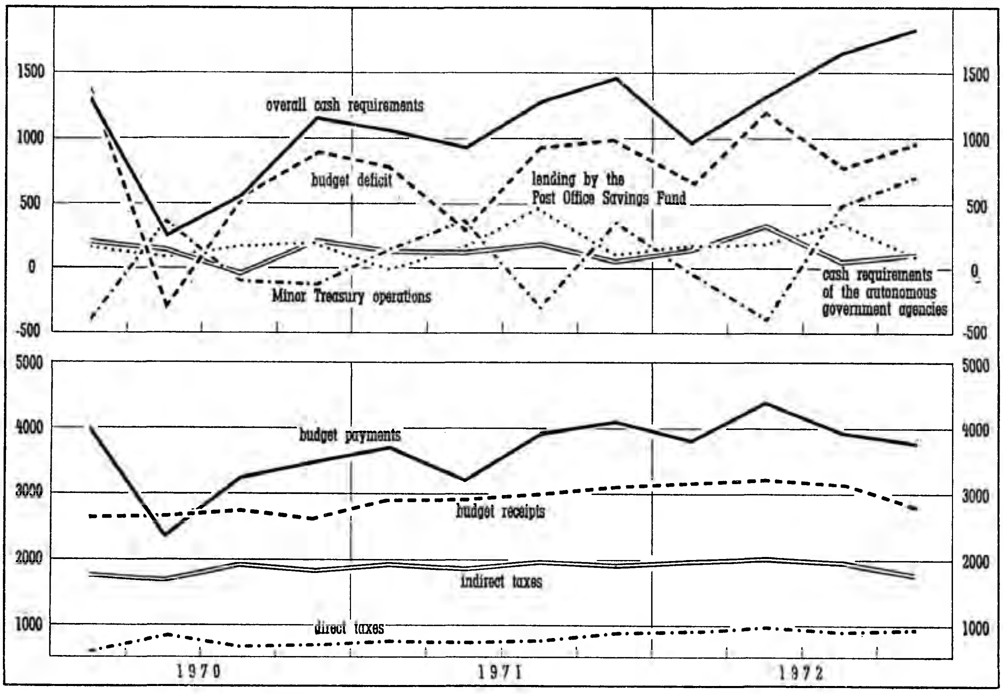
The drop in revenues from indirect taxation can, for the most part, be put down to exemption for inventory purchases and investments granted in May 1972 which neutralized the effects, moreover limited, of increased demand.

The exemption clause removed a hurdle to investment programmes which had already been decided but put off until the more favourable tax treatment came into force. With regard to inventories, rules governing the changeover from turnover tax to VAT not only removed difficulties affecting their increases but may also have stimulated the exporting enterprises to build up their inventories of products ready for sale.

In any case, from May 1972 on the exemption clause favoured the firms' financial situation because more funds, equal to the sum of unpaid turnover tax, were made available.

The cash operations of the Government sector (including not only budget operations but also those of the Treasury, the Central Post Office Savings Fund and the autonomous government agencies) resulted in overall cash requirements amounting to 5,760 billion, compared with 4,760 in 1971; the increase basically depends upon the expansion of budget operations and net disbursements in minor Treasury operations.

CHART 16



Performance of the components of the Government sector's cash requirements

(quarterly data seasonally adjusted; billions of lire)

From Chart 16, based on quarterly-adjusted data, it emerges that cash requirements — which had already soared in the second quarter owing to the increase in funds granted by the public sector to the public enterprises and special credit institutions — reached the highest level during the last part of the year as a result of both considerable Treasury disbursements, more than offsetting the slowdown in budget payments, and the marked fall-off in collections.

Post Office saving, after an about-turn registered between 1970 and 1971 — stemming from the performance of spreads between rates for Post Office deposits and bank deposits as well as from the economy's ample liquidity — continued to grow during 1972.

The exceptional increase in Post Office current accounts during December was due to contingent reasons, such as the budget's delay in gathering revenues from turnover tax collected through the Post Office current accounts and, most likely, the effects of bank strikes during that month.

In 1972, decisions regarding public debt policy were based, given the slim creation of monetary base through the Foreign and Banking

TABLE 30

TREASURY CASH REQUIREMENTS AND THEIR COVERAGE (1)

(calendar years and quarters; billions of lire)

Items	1971 1st quarter	1971 Total	1972 1st quarter	1972 Total	1973 1st quarter
Overall cash requirements					
Budget deficit (−)	-1,012	-3,046	- 930	-3,621	-1,635
Minor Treasury operations	278	- 507	526	- 744	845
Extra-budgetary operations	- 151	-1,205	- 349	-1,398	- 397
Total	- 885	-4,758	- 753	-5,763	-1,187
for lending operations (−)	*- 253*	*-1,556*	*- 350*	*-1,667*	*- 326*
through budget	*- 238*	*- 833*	*- 167*	*- 886*	*- 42*
through Central Post Office Savings Fund	*- 15*	*- 723*	*- 183*	*- 781*	*- 284*
Coverage of overall cash requirements					
Medium- and long-term bonds excluding Banca d'Italia	266	1,522	535	1,473	- 50
Post Office savings	133	1,134	290	1,715	26
Treasury Bills, excluding Banca d'Italia	53	978	171	989	175
Borrowing from Banca d'Italia	396	1,040	- 293	1,551	1,020
current account (2)	*49*	*- 212*	*- 171*	*528*	
Foreign indebtedness	37	- 17	- 19	- 15	- 2
Other indebtedness	..	101	69	50	18
Total	885	4,758	753	5,763	1,187
Short-term domestic financing	*577*	*3,244*	*239*	*4,297*	*1,242*
medium- and long-term domestic financing	*271*	*1,531*	*533*	*1,481*	*- 53*
Net indebtedness (3)	632	3,202	403	4,096	861

(1) For the first quarter of 1973 some figures have been estimated.— (2) The figures with a plus sign indicate greater Treasury borrowing.— (3) Change in the financial situation; that is, borrowings less lendings.

sectors, on the criterion of providing the economic system with enough liquidity to satisfy its financial requirements.

Therefore, despite increased cash requirements, placements of securities on the market were highly curtailed. In particular, issues of Treasury bonds for free investment, which in 1971 resulted in a net acquisition of funds equalling 600 billion, in 1972 reached a level not much higher than the minimum necessary to offset refunds of the previous year's issues. Moreover, purchases of medium- and long-term securities by the banks and other buyers, excluding the Banca d'Italia, dropped from 1,522 to 1,473 billion (Table 30).

Therefore, in 1972 the Treasury made a very much larger contribution to monetary base creation than in the previous year. More specifically, recourse to the Banca d'Italia grew considerably, especially in the form of medium- and long-term securities purchases.

The marked drop in the deficit for cash operations by the local authorities in 1972 must be seen in the light of the new functions taken over by the Regions which did not use all of the funds allocated to them from the Budget. As a result they registered a surplus of about 370 billion (representing the difference between receipts of circa 520 billion and expenditure for about 150) counterbalanced by the increase in their deposits with the Treasury.

THE MONEY MARKET AND THE FINANCIAL MARKET

During 1972, continuing the trend first begun at end-1970, all of the monetary and financial aggregates, both those directly controlled by the monetary authorities and those most responsive to market forces, registered a sharp climb. Together with an appreciable drop in the average level of interest rates, there was a further increase in the degree of liquidity in the economy, particularly as regards the enterprises.

The increase in the monetary base and in bank reserves was more rapid in the first half of the year, basically in connection with the financing needs of the Treasury. This was achieved, among other things, by not renewing two issues of Treasury bills for free investment that fell due in this period.

Thanks to the sufficient degree of liquidity in the banking system, lending rates and yields on long-term securities fell markedly in the first quarter. In April, realizing that economic activity continued to stagnate and the level of interest rates was still too high in respect to the needs, especially of the small- and medium-sized enterprises, the monetary authorities lowered the official discount rate and the rate on advances by half a point, accompanying this with an equal reduction of the yield paid on the banking system's voluntary deposits at the Banca d'Italia. As result there was a speed-up in the velocity of circulation of free bank reserves which, together with the expansion of the monetary base, brought downward pressure on the entire structure of bank lending rates and further raised the prices of fixed-interest securities.

Bank lending rates shrunk, according to data gathered by the *Centrale dei Rischi,* by circa 30 hundredths of a point in the first quarter of 1972, in respect to the level of 8.60 per cent of the previous year's final quarter, and by 70 hundredths in the second quarter.

While the returns on long-term securities on the secondary market decreased in nearly the same measure as lending rates, the narrowing of the banks' borrowing rates, again according to data from the same source, took place at an appreciably slower pace.

Together with the drop in interest rates the expansion of credit (loans and investments in securities) and bank deposits continued at a rhythm that, seasonally adjusted, was fairly similar to that observed in the second half of 1971.

The Treasury, through the financing of its deficit, continued to have an immediate influence on banking assets, on one side creating the means of payment which incremented deposits, and on the other issuing securities taken up by the banks.

The monetary crisis at the end of June had an immediate restrictive impact on the banks' excess reserves, draining nearly 300 billion lire. As an indirect result of this, there was a perk-up of demand on the secondary market for long-term securities which nonetheless did not give rise to substantial increases in rates, thanks to intervention by the Central Bank. In addition, the monetary authorities intervened by removing the restrictions on the banks' foreign indebtedness, and by restoring the volume of monetary base through an adequate financing of the Treasury at the Banca d'Italia.

A 200 billion lire issue of Treasury bills, partially aimed at replacing a lot maturing in the same month, was easily placed in July at an overprice of 1.10 per cent against the basic asking price of 94.50.

The steady worsening of foreign accounts led, in the second half of the year, to a slowdown in the creation of monetary base and an acceleration in the demand for credit. The expansion of overall financing and the consequent formation of financial assets were nonetheless mainly stimulated by the demand growing out of the recovery in economic activity and in investments. The banks were able to develop the intermediation process using the excess reserves already in their possession. Because of the lack of corresponding demand they were not however able to use the large amount of liquidity in foreign currencies made available by the removal of restrictions on foreign indebtedness.

In spite of its gradual absorption into compulsory reserves, the banking system's excess reserves kept to sufficiently high levels during the summer, as substantiated by the favourable reception on the part of the market, in September, of a new issue of Treasury bills.

The lowering of lending rates, though gradual, continued; in the third quarter the drop was 17 hundredths and in the fourth another 18.

During the year lending rates registered on average a level 1.15 percentage points lower than the previous year's (7.88 per cent in 1972 versus 9.03 in 1971) thereby saving borrowers nearly 350 billion since, all told, loans totalled some 35,000 billion. It should be noted that the drop was widest for the large enterprises and the state-controlled companies, and less than average for the small- and medium-sized enterprises. Yields on long-term securities again showed some tendency to diminish in the summer, after the foreign currency crisis of end-June and the early days of July. Sales by the Banca d'Italia made it possible to limit the fall-off and facilitated defence of ongoing levels when, in November and December, a new speculative wave against our money generated fresh pressures on the secondary market.

The creation of monetary base, seasonally adjusted for abnormal working conditions in the banks in the months of November and December, came, in the year under study, to around 4,400 billion (3,363 in 1971). The increase in banks' reserves, not counting the increase in foreign currency liquidity, came to 1,166 billion (1,888 billion including foreign currency liquidity) against 1,529 in the previous year). The potential to expand credit was, however, magnified by the concentration of the increase in the first half of the year, as well as by the reduction of the marginal coefficient for compulsory reserves, which fell from 17.6 per cent in 1971 to 14.6 in 1972 in connection with the increment in the composition of some deposits.

Overall bank deposits increased by 10,446 billion; by making adjustment for the seasonal distortions at the end of the year, the increase can be set at 8,650, still substantially higher in absolute terms than that of the previous year (7,205) but identical to it in relative terms (18 per cent).

The increase in loans, which in the second half of 1972 showed, for reasons noted above, a substantial rise, was more than 5,783 billion, equal to 18.9 per cent, against 3,533 billion, equal to 13.1 per cent in 1971. For this aggregate also, however, the abnormal working conditions in the banks at the end of the year may have led to an exceptionally high increase.

The downward trend of interest rates in the first half of the year and their relative steadiness in the second fostered a buoyant demand for long-term securities on the part both of banks — which purchased

2,904 billion worth (versus 2,327 billion in 1971; excluding Treasury bills and Post Office certificates) — and of the non-banking public which invested 1,901 billion in these assets (1,786 billion in 1971).

The net purchases of the Central Bank came to 1,141 billion in 1972 against 750 in 1971.

Thanks to the potential offered by the demand performance, overall issues in 1972 came to nearly 6,500 billion, 1,000 billion more than in 1971.

Taking greatest advantage of the increased placement potential were the public enterprises and the Treasury. For the latter nearly 500 billion worth of issues regard the consolidation of prior short-term debts (AIMA and the local authorities).

The medium-term industrial credit institutions also increased their fund raising through bonds (1,752 billion 1972 versus nearly 1,453 in 1971), partially offset however by the reduction in this activity registered by the medium-term real estate institutions (694 billion in 1972 versus some 776 in 1971). It should be recalled, however, that these latter institutions had increased their issues to a particularly high degree in 1971 in order to benefit from the special facilities provided by law. On the overall level, taking into account also the other forms of supply, the net outlays of funds on the part of the special credit institutions kept in 1972 to the previous year's levels. Similar to what has been noted for the banks, the expansion was slower in the first half (nearly 1,250 billion) and speedier in the second (nearly 1,900 billion); over the whole year the increase was 3,146 billion, equal to 16.6 per cent against 3,321 in 1971, or 21.2 per cent.

In sum, also counting fund gathering through stock issues — which was favoured by the markets' upward performance, especially in the second half of the year — and financing from abroad, which shrunk in respect to the preceding year as the result of debt repayments, the expansion of financial flows during the course of 1972 made feasible, apart from the financing of the public sector for 7,560 billion, the granting of some 10,000 billion in credits to the enterprises and households sector, namely an increase of 2,000 billion over the preceding year.

Investments at current prices in this sector were 650 billion higher than those of the preceding year, given the basically unchanged state of gross self-financing in the enterprises and dwellings sector; the result was that the enterprises' financial assets grew to an appreciably greater extent than in the previous year.

The creation of new financial assets equalled about 17,400 billion (after adjustment for the unusual movements at the end of the year in notes in circulation, in postal and in bank accounts), versus 12,900 during 1971. After deducting the part absorbed by the enterprises there remains an increase of nearly 11,800 billion for the households. Given the rise in this sector's indebtedness (some 500 billion) it emerges that the portion of the households' savings invested in financial assets was equal to 80.1 per cent of gross national saving and 17.1 per cent of the GNP, versus respectively 67.8 and 15 per cent in 1971.

Comparison between the forecast and the outcome for 1972

Certain differences, partially connected with the failure of several assumptions on which the previsions themselves were based, emerge in a comparison between the forecasts and seasonally adjusted results for 1972. More specifically, the growth in line with the hypothesis of the gross national product at current prices (9.3 per cent, even if the price component was 1 per cent higher than predicted) was accompanied by an expansion in overall investments, at current prices, of 7.5 per cent instead of 12 per cent. The balance of payments also registered a larger deficit (747 billion versus 300) because of the higher net export of capital, and the public sector showed a deficit of 5,760 billion against the nearly 4,500 forecast.

The Treasury's larger deficit helps to explain the higher growth of the banks' and special credit institutions' deposits — which expanded in all by 9,050 billion rather than the 8,000 predicted — as well as the greater demand for fixed-interest securities on the part of the banking system (2,904 billion versus 2,200). The deficit was also financed to a larger extent than foreseen by postal savings, which rose by nearly 1,500 billion instead of 1,200.

Income growth and the downward movement of interest rates in the first half of the year, followed by a basic levelling off, even if in the presence of certain upward pressures, in the second half stimulated the public and the non-banking intermediaries to purchase securities for 1,900 billion, a sum identical to that forecast.

The positive performance of overall demand for fixed-interest securities paved the way for some 500 billion more in issues than had been predicted (5,985 billion versus 5,500). This difference mainly reflects greater activity by the special credit institutions, while that of the Treasury and the enterprises (including the IRI, ENI and ENEL groups) remained unchanged.

The banks' and the special credit institutions' higher than predicted fund mobilization made possible a substantially greater expansion of loans than foreseen. Given the incomplete accomplishment of private investments, this financing was mainly translated, as shown above, into a greater increase in the enterprises' liquid assets.

The overall creation of monetary base, adjusted seasonally and for foreign currency liquidity, turns out to have been substantially in line with what was predicted in last year's Report, while the part absorbed by the public shows up slightly higher than foreseen in relation to the above-noted performance of postal savings fund gathering.

Forecasts for 1973

Forecasts on the performance of monetary and credit flows for 1973 are based on the assumption of a GNP development of 15 per cent at actual prices and 4.5 per cent at constant prices. These assumptions emerge from an updating of forecasts, including those in the Budget Ministry's annual plan, taking into account both the definitive data of national accounts for 1972 and the changes that have taken place in the economic situation. More specifically, gross overall investments, at current prices, should grow in step with income, reaching the sum of 16,000 billion. The hypotheses are compatible with an overall balance-of-payments position in near equilibrium. The achievement of the foregoing level of investments would allow the financing of a deficit of the Treasury sector, Central Post Office Savings Fund and the autonomous agencies of up to 7,000 billion; this amount seems in line with the trend of the cash requirements in the first four months of 1973. The increase of cash requirements, in respect to 1972, is partially the outcome of

TABLE 31

MONETARY BASE

(changes in billions of lire)

Items	1970	1971	1972 year	1972 Quarters I	1972 Quarters II	1972 Quarters III	1972 Quarters IV
SOURCES							
Foreign Sector	319.1	478.0	-31.3	-130.0	371.2	-68.3	-204.2
balance of payments	222.9	489.0	-746.8	-102.4	-223.4	50.4	-471.4
banks' position and its regulation	96.2	-11.0	715.5	-27.6	594.6	-118.7	267.2
Treasury	2,991.0	2,611.2	4,270.9	364.1	1,177.8	1,177.3	1,551.7
(excluding open-market operations by BI-UIC)	(3,153.2)	(3,064.4)	(4,509.3)	(422.6)	(1,248.4)	(1,185.8)	(1,652.5)
cash needs	3,226.0	4,757.7	5,762.5	752.7	1,288.5	1,674.5	2,046.8
public debt and open-market operations	-32.6	-2,098.1	-1,538.9	-326.0	-175.1	-651.1	-386.7
other operations	-202.4	-48.4	47.3	-62.6	64.4	153.9	-108.4
Banks	-1,276.1	89.6	1,434.7	-134.5	126.4	-68.4	1,511.2
Other sectors	-40.8	183,8	-529.4	66.9	-65.8	-395.3	-135,2
release of compulsory reserves in monetary base	259.5	30.5	-2.2	-1.4	1.4	-2.0	-0.2
Total	1,993.2	3,362.6	5,144.9	166.5	1,609.6	645.3	2,723.5
Total (excluding Post Office deposits)	(1,671.8)	(2,347.3)	(2,726.8)	(-140.0)	(730.5)	(481.6)	(1,654.7)
USES							
Public and non-bank intermediaries	824.3	1,833.7	3,257.3	-298.6	878.1	166.9	2,510.9
Public	768.8	1,823.5	3,125.3	-55.3	596.9	461.6	2,122.1
notes and coins	504.8	667.0	1,320.2	-346.4	337.0	124.8	1,204.8
deposits with Treasury and BI (1)	27.0	24.5	108.7	-4.1	29.7	70.2	12.9
Post Office deposits	237,0	1,132.0	1,696.4	295.2	230.2	266.6	904.4
Special credit institutions	55.5	10.2	132.0	-243.3	281.2	-294.7	388.8
Banks	1,168.9	1,528.9	1,887.6	465.1	731.5	478.4	212.6
Compulsory reserves and backing for cashiers' cheques (*)	782.1	1,161.9	1,237.3	382.1	390.7	42.0	422.5
cash	529.2	729.8	316.8	3.7	81.7	-71.9	303.3
Treasury bills	-16.6	379.7	913.9	371.0	307.6	115.9	119.4
« special » reserves in securities (2)	269.5	52.4	6.6	7.4	1.4	-2.0	-0.2
Liquidity in lire	302.4	483.7	-71.4	71.7	-308.1	539.3	-374.3
vault cash	26.3	5.8	155.6	-109.0	61.1	-41.0	244.5
sight deposits with BI	75.5	390.8	-192.3	47.5	-97.8	226.8	-368.8
unused borrowing margin	212.0	87.2	-38.3	148.3	-284.6	356.6	-258.6
other credits	-11.4	-0.1	3.6	-15.1	13.2	-3.1	8.6
Liquidity in foreign currency	84.4	-116.7	721.7	11.3	648.9	-102.9	164.4
(*) Other long-term securities in the compulsory reserves	243.8	451.8	688.9	220.0	126.7	121.1	221.1

(1) Including cheques issued by the Banca d'Italia.— (2) Deposited in replacement of existing cash and Treasury bill reserves.

an expansion of fund transfers to other agencies of the public sector, including fund withdrawals made by the newly established Regions. These withdrawals, through not expanding the overall savings requirements on the part of the public sector, swell the banks' accounts, thereby altering the smooth functioning of banking activity.

Under all of the foregoing assumptions the increase of currency in circulation can be set at some 1,100 billion and that of deposits (with the banks, P.O. and the special credit institutions) at slightly less than 12,500 billion. Demand for fixed-interest securities and shares on the part of the public, if the ongoing price stability holds, could come to some 3,000 billion. Overall issues of long-term fixed-interest securities could reach 6,500 billion.

Loans granted by the special credit institutions (net of repayments) and the banks should come to 8,500 billion; the forecast reflects a certain slowdown in the growth of bank loans; nonetheless, taking into consideration transfers and financing on the part of the Treasury and of funds mobilized on the financial market, said credit expansion will give rise to a growth of the liquid assets and securities of the enterprises, equal to that of 1972 (nearly 6,000 billion).

The overall creation of monetary base compatible with the abovementioned financial flows turns out to be nearly 500 billion greater than that of 1972 (not counting the portion of excess reserves in foreign currency).

The Central Bank's operations and the regulation of monetary base

The Central Bank's assets and the creation of monetary base

The balance of payments drained off 747 billion worth of monetary base, mainly as a result of capital movements. The deficit was registered chiefly during the last part of the year (Table 32) but, if data are seasonally adjusted, it appears that the deficit began in mid-year and gradually worsened up until December (Chart 17). The monetary authorities reacted against the loss of foreign currency reserves by removing, as of the end of June, the limits imposed on the banking system with regard to taking up foreign debtor positions. As a result of this provision, the net foreign debtor position increased by 256 billion; nonetheless, its impact on domestic liquidity was nullified by deposits, practically identical in value to the variation in net position, in tied foreign currency accounts with the Banca d'Italia (Table 32).

TABLE 32

MONETARY BASE CREATION: FOREIGN SECTOR

(changes in billions of lire)

Items	1970	1971	1972				
			Year	quarters			
				I	II	III	IV
Balance of payments (1)	*222.9*	*489.0*	*- 746.8*	*- 102.4*	*- 223.4*	*50.4*	*- 471.4*
current account	- 59.9	494.4	- 290.7	244.3	142.9	- 34.1	- 643.8
capital movements	329.5	59.3	- 526.1	- 342.3	- 220.2	- 23.2	59,6
errors and omissions	- 47.2	- 64.2	69.8	- 4.9	- 146.1	107.8	113.0
Banks' position and its regulation (a)	*96,2*	*- 11.0*	*715.5*	*- 27.6*	*594.6*	*- 118.7*	*267.2*
deposits collected abroad (increase +)	1,810.5	1,496.3	4,093.5	- 323.7	239.2	609.8	3,568.2
non-liquid foreign lendings (increase −)	-1,770.3	-1,368.3	-3,696.4	365.2	- 148.4	- 757.6	-3,155.6
tied liquid assets (increase −)	56.0	- 139.0	580.1	- 69.1	649.2	—	—
tied deposits in foreign currency with the BI-UIC (increase −) (b)	—	—	- 261.7	—	- 145.4	29.1	- 145.4
Total effect	*319.1*	*478.0*	*- 31.3*	*- 130.0*	*371.2*	*- 68.3*	*- 204.2*
in lire: net foreign position of BI-UIC (2)	234.7	472.9	- 753.8	- 140.6	- 278.0	31.9	- 367.1
exchange rate adjustments	—	121.8	0.8	- 0.7	0.3	2.7	- 1.5
in foreign currency: banks' liquidity in foreign currency (c)	84.4	- 116.7	721.7	11.3	648.9	- 102.9	164.4
N.B.: net foreign position of the banks (c) − (a) + (b)	- 11.8	- 105,7	- 255.5	38.9	- 91.1	44.9	- 248.2

(1) Including accounting discrepancies between figures found by BI-UIC for foreign sector and the balance of payments.— (2) Excluding tied deposits in foreign currency with the BI-UIC.

The foregoing measure was also accompanied by the automatic abolition of previous limits on domestic use of the liquid foreign currency assets already held by the commercial banks (about 600 billion in June and 580 billion for the entire year); since the banks purchased another 142 billion of technically liquid foreign assets, the latter increased overall by 722 billion. These can be converted into lire at the Central Bank only within the limits of repayments for the *spot* *and forward* ceiling at the UIC (Italian Exchange Office). The only contribution the remainder could make to monetary base creation (or to reducing the drainage from foreign operations) would come about if it were lent to domestic businessmen as a substitute for foreign currency purchases. During the second half of the year expectations of exchange rate changes however, caused clients to repay nearly 1,000 billion in foreign currency loans. Thus, making foreign currency liquidity available to the banks did not have any impact on credit expansion. For this reason we have chosen to show separately, in Table 31, both the overall creation of monetary base and the change in excess bank reserves net of the foreign currency component.

Operations for financing the Treasury resulted in the creation of 4,271 billion in monetary base (4,509 if the impact of net sales of securities on the open market is excluded); notably, a substantially larger amount than in the immediately preceding years (Table 31). The sharp increase, as already mentioned, was the result of deliberate action on the part of the monetary authorities, aimed at providing the banking system, given the trend of the other components, with a large enough volume of liquid assets to enable credit demand to expand steadily. Financing of the Treasury through the direct placing of securities on the market was curbed (1,539 billion in 1972, versus 2,098 in 1971; Table 34), even though the sector's cash deficit overshot by 1,005 billion that of the previous year (5,763 billion versus 4,758).

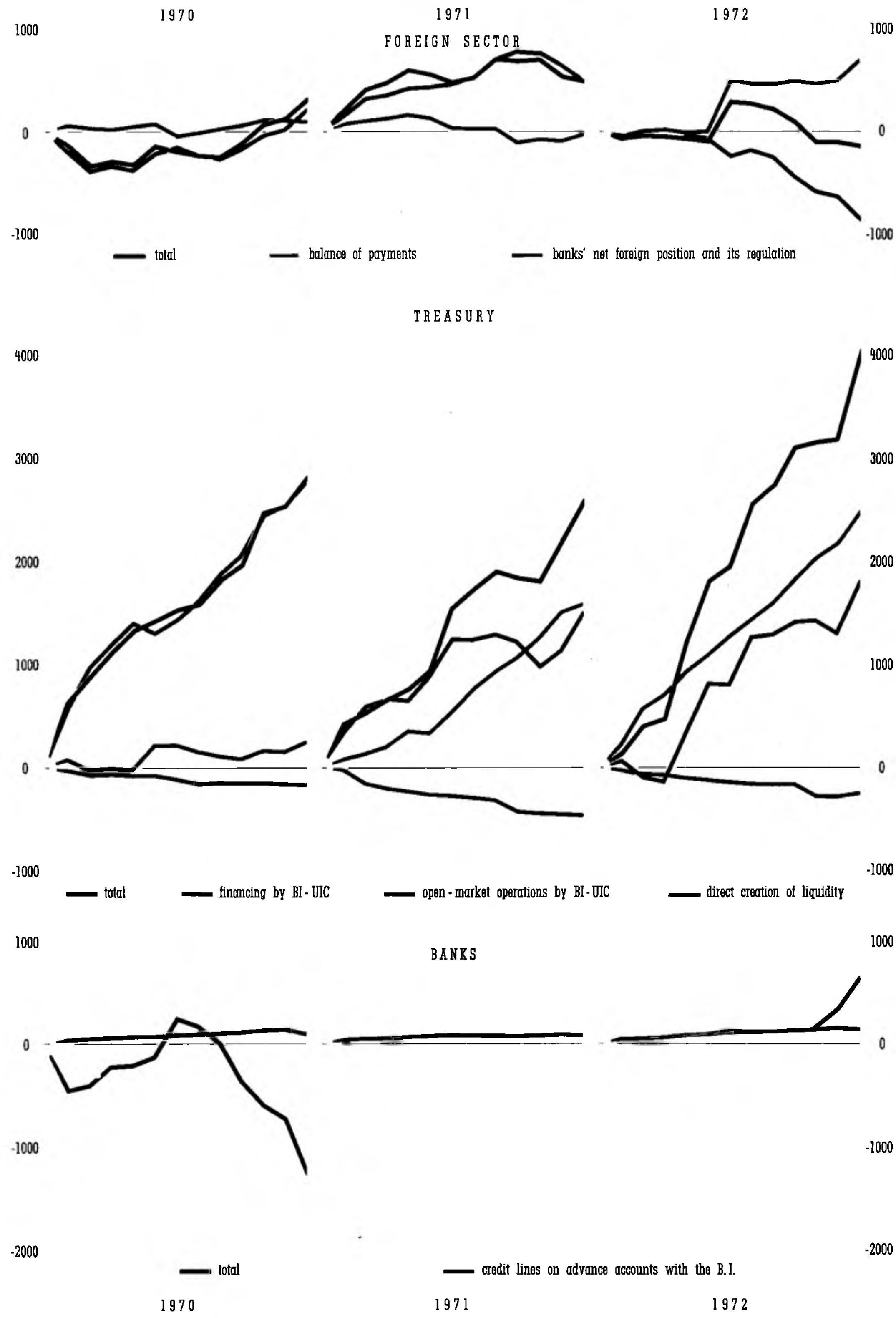
Two-thirds of the financing of the BI-UIC is represented by the net change in the public's securities portfolio resulting from purchases of new issues for 1,380 billion (1,154 in 1971), redemptions of matured securities for 293 billion and sales at going market prices amounting to 238 billion (Tables 33 and 34).

In order to transfer the financing of the Treasury to the Central Bank, net issues of ordinary Treasury bills for free investment were curtailed; these amounted to 75 billion during the year versus 600 in 1971 (Table 36). More specifically, two issues for a total of 375 billion, maturing during the first six months were not renewed. In the second half of the year issues were placed in July, September and November for a total, net of repayments, of 450 billion.

The November issue was carried out not for reasons of liquidity regulation, but in view of the Treasury's end-year cash requirements;

SOURCES OF MONETARY BASE

(cumulative monthly changes, data adjusted seasonally and for random movements at end-1972; billions of lire)



USES OF MONETARY BASE

(cumulative monthly changes, data adjusted seasonally and for random movements at end-1972; billions of lire)

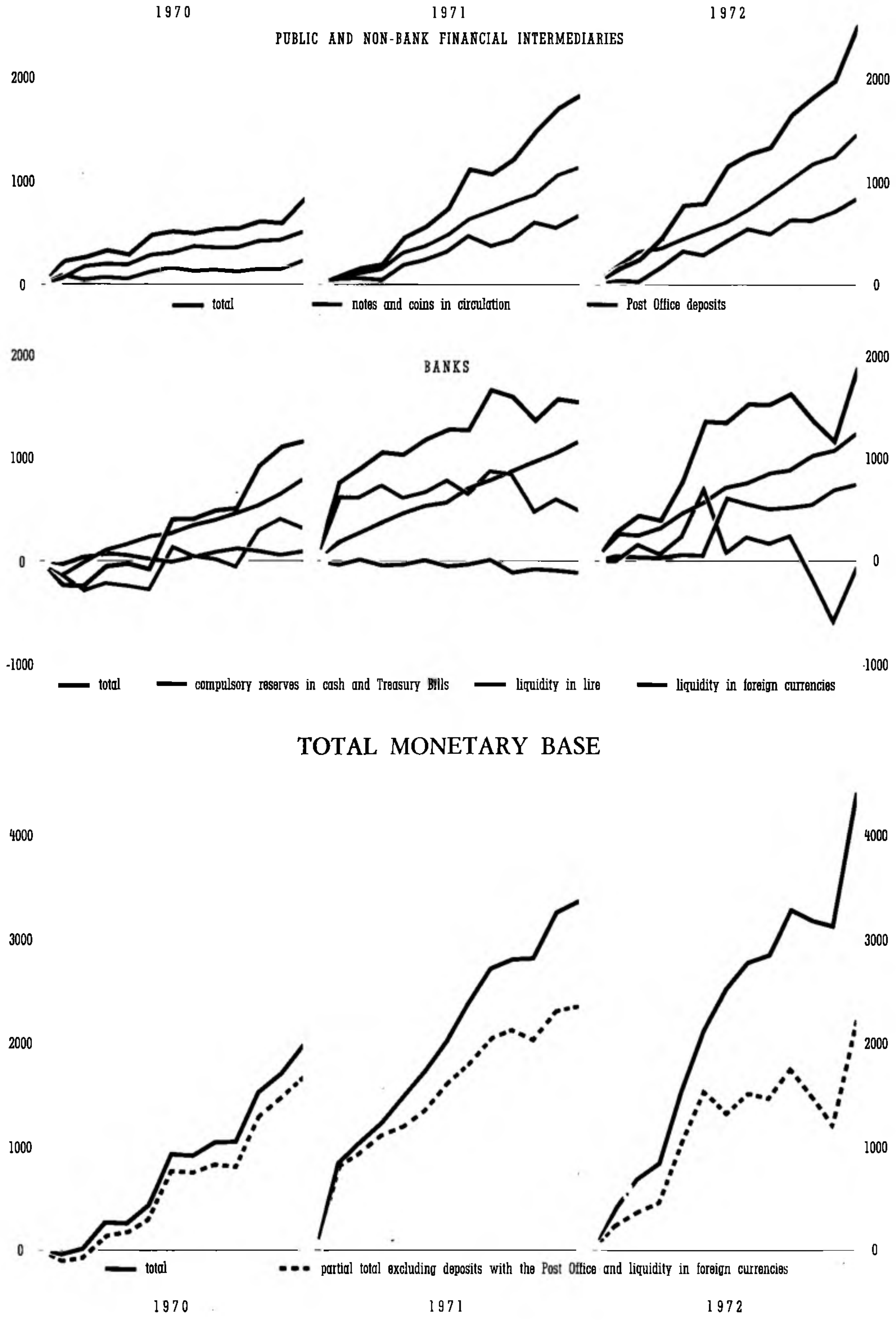


TABLE 33

MONETARY BASE CREATION: TREASURY

(changes in billions of lire)

Items	1970	1971	1972 Year	1972 quarters I	II	III	IV
Budget deficit (+) or surplus (—)	*3,226.0*	*4,757.7*	*5,762.5*	*752.7*	*1,288.5*	*1,674.5*	*2,046.8*
Intervention by monetary authorities (1)	*- 235.0*	*-2,146.5*	*-1,491.6*	*- 388.6*	*- 110.7*	*- 497.2*	*- 495.1*
Operations in government securities	- 32.6	-2,098.1	-1,538.9	- 326.0	- 175.1	- 651.1	- 386.7
Public debt (2)	129.6	-1,644.9	-1,300.5	- 267.5	- 104.5	- 642.6	- 285.9
Treasury bills for free investment	99.4	- 548.8	- 74.6	200.0	175.0	- 250.0	- 199.6
Long-term securities . .	30.2	-1,096.1	-1,225.9	- 467.5	- 279.5	- 392.6	- 86.3
Open-market operations by BI-UIC	- 162.2	- 453.2	- 238.4	- 58.5	- 70.6	- 8.5	- 100.8
Treasury bills	- 115.2	- 49.3	—	—	—	—	—
Long-term securities (3)	- 47.0	- 403.9	- 238.4	- 58.5	- 70.6	- 8.5	- 100.8
Other operations (4)	- 202 4	- 48.4	47.3	- 62.6	64.4	153.9	- 108.4
Total effect	*2,991.0*	*2,611.2*	*4,270.9*	*364.1*	*1,177.8*	*1,177.3*	*1,551.7*
Direct liquidity creation . .	248.6	1,571.5	2,719.5	657.4	585.6	455.6	1,020.9
Post Office deposits . . .	237.0	1,132.0	1,696.4	295.2	230.2	266.6	904.4
Other operations (5) . . .	11.6	439.5	1,023.1	362.2	355.4	189.0	116.5
Financing by BI-UIC (6) . .	2,742.4	1,039.7	1,551.4	- 293.3	592.2	721.7	530.8
Net subscriptions of new issues:							
Treasury bills, Central Post Office Savings Fund certificates and credit certificates (AIMA)	- 221.8	373.7	- 292.8	—	31.6	- 324.4	—
Long-term securities . .	1,320.2	1,154.3	1,379.9	- 18.0	96.5	464.4	837.0
Open-market operations (3)	- 162.2	- 453.2	- 238.4	- 58.5	- 70.6	- 8.5	- 100.8
Treasury current account .	1,704.3	- 212.0	528.1	- 170.9	495.7	512.6	- 309.3
Other financing (7)	101.9	176.9	174.6	- 45.9	39.0	77.6	103.9

(1) The sign refers to the effect produced on the creation of monetary base: i.e., Banca d'Italia sales on the market and securities issues bear a negative sign.— (2) Issues net of BI-UIC subscriptions.— (3) Excluding government securities sold to the banks for compulsory reserves.— (4) Guarantee deposits at the Central Post Office Savings Fund, foreign debts and net lending of banks and special credit institutions to autonomous agencies.— (5) Including government securities held as compulsory reserves in place of cash and Treasury bills.— (6) The figures for securities do not make allowance for depreciation, which is shown in the balance sheet of BI at December 31, 1970, 1971 and 1972.— (7) Including government securities sold to the banks for compulsory reserves.

TABLE 34

SIZE AND MOVEMENT OF THE PUBLIC SECURITIES HOLDINGS OF THE BANCA D'ITALIA AND OF UIC

(balance sheet values in billions of lire)

Securities	Initial amount	Increase due to: Purchases on issue	Increase due to: market purchases	Reduction due to: market sales	Reduction due to: redemptions	Accounting revaluations and profits on sales	Final amount
1971							
Short-term:	*175.0*	*548.7*	*329.8*	*49.3*	*454.8*	—	*549.4*
Treasury bills: for free investment	—	49.3	—	49.3	—	—	—
for compul. reserves	—	—	329.8	—	279.8	—	50.0
Post Office interest-bearing certificates	175.0	175.0	—	—	175.0	—	175.0
Credit certificates (AIMA)	—	324.4	—	—	—	—	324.4
Medium- and long-term:	*3,365.1*	*1,296.9*	*30.5*	*456.3*	*142.6*	*14.5*	*4,108.1*
Long-term government securities	446.8	69.1	0.7	152.4	8.8	5.2	360.6
Treasury certificates:							
ordinary	428.4	135.3	—	—	29.5	—	534.2
special	293.7	31.4	—	—	34.2	—	290.9
Consolidated and redeemable securities:							
school building	391.9	470.6	—	2.9	29.9	0.3	830.0
others	16.3	—	. .	. .	2.0	—	14.3
Bonds:							
autonomous government agencies	269.3	231.5	1.0	5.9	7.1	0.3	489.1
on behalf of the Treasury	1,518.7	359,0	28.8	295.1	31.1	8.7	1,589.0
Total	3,540.1	1,845.6	360.3	505.6	597.4	14.5	4,657.5
1972							
Short-term:	*549.4*	*206.6*	—	—	*549.4*	—	*206.6*
Treasury bills: for free investment	—	—	—	—	—	—	—
for compul. reserves	50.0	—	—	—	50.0	—	—
Post Office interest-bearing certificates	175.0	175.0	—	—	175.0	—	175.0
Credit certificates (AIMA)	324.4	31.6	—	—	324.4	—	31.6
Medium- and long-term:	*4,108.1*	*1,575.1*	*120.6*	*367.7*	*195.3*	*16.9*	*5,257.7*
Long-term government securities	360.6	2.0	5.8	108.1	—	7.0	267.3
Treasury certificates:							
ordinary	534.2	547.9	. .	—	48.3	—	1,033.8
special	290.9	—	—	—	38.2	—	252.7
Consolidated and redeemable securities:							
school building	830.0	114.3	. .	8.0	41.3	0.8	895.8
others	14.3	—	. .	. .	. .	. .	14.3
Bonds:							
autonomous government agencies	489.1	96.5	1.5	54.9	17.6	- 0.5	514.1
on behalf of the Treasury	1,589.0	814.4	113.3	196.7	49.9	9.6	2,279.7
Total	4,657.5	1,781.7	120.6	367.7	744.7	16.9	5,464.3

in fact, during this last period it did not seem a good idea to issue Treasury bills because of the usual seasonal movements of the banks' accounts.

In all three issues, the nominal rates offered were 5.50 per cent (advance), and demand far outpaced supply, especially in July. The actual interest rate for bonds sold stood at 4.40 per cent in July and 4.30 in September; in November the issue was made at the nominal rate (Table 35).

TABLE 35

TREASURY BILLS FOR FREE INVESTMENT

(monthly movements)

Date	Repayments	Supply	Tender rate	Amount of bids	Allocation	Actual rate
1971 – Feb.	76.6	—	—	—	—	—
Mar.	50.0	200.0	6.00	338.3	200.0	5.50
May	—	175.0	5.75	130.4	(1)175.0	5.25
July	—	150.0	6.00	145.3	(2)150.0	6.00
Sept.	—	200.0	6.00	279.6	200.0	5.70
1972 – Mar.	200.0	—	—	—	—	—
May	175.0	—	—	—	—	—
July	150.0	200.0	5.50	410.0	200.0	4.40
Sept.	200.0	400.0	5.50	507.0	400.0	4.30
Nov.	—	200.0	5.50	241.5	200.0	5.50

(1) 44.6 of which to the Banca d'Italia.— (2) 4.7 of which to the Banca d'Italia.

Heavy demand for Treasury bills in July seems to confirm that there is no immediate link between the export of capital and bank liquidity, mainly because the banks were forbidden to invest in lira-denominated assets abroad. In November the rate was higher owing to the gradual fall-off in the banks' excess reserves in lire; here again it seems that motives linked with interest-rate levels in other countries can be discarded.

Over the year, support purchases of fixed-interest securities on the secondary market amounted to 121 billion (Table 35), nearly all in securities issued by Crediop (Credit Consortium for Public Works) on behalf of the Treasury. The number of purchases was greater at the beginning of the summer and at the end of the year, coinciding with the currency crises, whereas sales were highest in summer. These operations made it possible to largely iron out price fluctuations and had a positive effect on the demand for fixed-interest securities on the part of financial intermediaries and the public.

Until late autumn, given the abundance of liquidity, the banking system resorted to little financing by the Central Bank and, except on rare occasions, only to cover temporary seasonal cash requirements. The movements took place mainly within the credit lines for ordinary advances, thus these operations had little impact on the overall creation of monetary base.

The credit line for current account advances grew over the year at a slightly faster pace than in previous years. The half percentage point drop in rediscounting rates and rates on ordinary advances (from 4.50 to 4.00 per cent for rediscounting and from 4.00 to 3.50 for advances) decided upon in April (along with the reduction in rates for free deposits with the Banca d'Italia) does not seem to have had any marked effects on financing behaviour even though it served to stress the expansionary monetary policy, thereby spurring the financial intermediaries to react in line with this trend, in particular with regard to the supply of credit.

The other components of monetary base — especially fixed-term advances — only registerd movements of a certain importance at the end of June and the first days of July, when the currency crisis rapidly siphoned off a considerable amount of monetary base (about 300 billion) in comparison to the banks' excess reserves.

At the end of November, the impact of the new currency crisis, combined with issues of Treasury bills for free investment, forced the banks to resort more regularly to financing by the Banca d'Italia. On this occasion, the demand for credit was mainly channelled by the monetary authorities towards fixed-term advances.

The fear that funds loaned in this manner might, even indirectly, encourage capital outflows, caused the monetary authorities, at the beginning of December, to increase by 2 points (from 3.50 to 5.50 per cent) the basic rate for the latter form of financing (while the increases up to 1.50 per cent introduced in 1969 remained unaltered).

However, following the tendency in other countries to raise official rates, it seemed both unnecessary and undesirable to raise the rediscounting rate and the rate for ordinary advances as well. Indeed, the substantial effects of a general increase in central bank rates would not have been much different from those caused by raising only the rate for fixed-term advances, but it would have sparked off expectations of a generalized upswing in interest rates — a far from desirable result with regard to managing the long-term securities market and, more generally speaking, achieving economic revival. Nonetheless, there was no lack of upward pressures on some categories of bank rates towards the end of the year.

The expansion of financing in the form of fixed-term advances took on particularly large dimensions in December, reaching the sum of 1,431 billion at the end of the year (at the end of October the amount was nil; at end-November it stood at 72 billion; in mid-December it had overshot the 600 billion mark). At the end of January the debt had already dropped down to about 300 billion and at the beginning of March had completely disappeared. Variations in the total for ordinary discounting were, instead, negligible and those in the ordinary advance accounts kept within limits and followed the seasonal patterns already registered in previous years.

The Central Bank's liabilities and the uses of monetary base

The increment in the deficit of the consolidated account of the Banca d'Italia and the UIC during 1972 can be broken down into: 1,484 billion in bank notes in circulation, 631 in the special credit institutions' deposits, 386 in disposable deposits and compulsory reserves and the remainder in capital and reserves and other minor items (Table 36).

Bank notes in circulation, which grew considerably but steadily during the year, from November onwards shot upwards, reaching a peak of 8,790 billion at end-December, for a yearly increase of 20.3 per cent. The huge expansion in the amount of bank notes during the last quarter should be viewed in the light of the abnormal working conditions in the banks as well as seasonal movements.

Post Office deposits also registered a particularly marked increase, spurred by the unusual end-year financial conditions; (1,696 billion,

TABLE 36

CONSOLIDATED BALANCE SHEET OF THE BANCA D'ITALIA AND THE UFFICIO ITALIANO DEI CAMBI

(amounts and changes in billions of lire)

Items	Amounts at end of 1972	1970	1971	1972 Year	1972 quarters I	II	III	IV
ASSETS				*(changes)*				
Lending to the Foreign sector and gold (1)	4,227.8	466.5	533.3	- 412,9	- 82.7	- 128.9	- 8.7	- 192.6
Lending to the Treasury	9,531.8	2,308.0	1,013.8	1,574.9	- 381.3	736.0	637.8	582.4
current account	*1,907.7*	*1,591.6*	*- 212.0*	*528.1*	*- 171.0*	*495.8*	*512.6*	*- 309.3*
securities (2)	*5,464.3*	*776.2*	*1,117.5*	*806.7*	*- 135.3*	*57.4*	*131.4*	*753.2*
other credit	*2,159.8*	*- 59.8*	*108.3*	*240.1*	*- 75.0*	*182.8*	*- 6.2*	*138.5*
Lending to the banks (3)	2,338.8	-1,488.2	2.5	1,472.9	- 282.9	411.1	- 425.0	1,769.7
Lending to the special credit institutions .	166.6	30.1	17.9	- 7.7	- 12.4	- 10.6	0.7	14.6
Other accounts	514.1	53.6	258.2	61.1	- 30.4	336.6	- 314.4	69.3
TOTAL . . .	16,779.1	1,370.0	1,825.7	2,688.3	- 789.7	1,344.2	- 109.6	2,243.4
LIABILITIES								
Currency in circulation	8,790.5	524.9	661.6	1,483.9	- 457.5	393.7	80.4	1,467.3
Notes	*8,747.5*	*519.2*	*662.1*	*1,466.3*	*- 458.6*	*392.9*	*85.1*	*1,446.9*
Banca d'Italia cheques	*43.0*	*5.7*	*- 0.5*	*17.6*	*1.1*	*0.8*	*- 4.7*	*20.4*
Deposits of the special credit institutions . . .	1,086.5	218.1	- 43.6	631.0	- 339.5	312.9	111.5	546.1
Deposits of the banks	5,019.5	604.6	1,120.6	386.2	51.2	129.3	125.8	79.9
compulsory reserves and backing for cashiers' cheques	*4,334.5*	*529.0*	*729.9*	*316.8*	*3.7*	*81.7*	*- 71.9*	*303.3*
other accounts	*685.0*	*75.6*	*390.7*	*69.4*	*47.5*	*47.6*	*197.7*	*- 223.4*
Deposits and credit of the Treasury	199.0	- 187.8	- 42.7	0.7	- 85.5	142.7	- 88.3	31.8
current account	—	*- 112.7*	—	—	—	—	—	—
other accounts	*199.0*	*- 75.1*	*- 42.7*	*0.7*	*- 85.5*	*142.7*	*- 88.3*	*31.8*
Deposits of the Foreign sector	682.2	231.2	60.3	77.1	55.9	3.7	- 11.6	29.1
Other accounts	159.2	- 2.5	- 20.4	0.8	- 14.3	307.4	- 327.1	34.8
Equity capital	842.2	- 18.5	89.9	108.6	..	54.5	- 0.3	54.4
TOTAL . . .	16,779.1	1,370.0	1,825.7	2,688.3	- 789.7	1,344.2	- 109.6	2,243.4

(1) Differences compared with the balance-of-payments monetary movements are the result of reclassification of foreign currencies held in administration on behalf of third parties.— (2) Balance-sheet values net of end-year depreciation.— (3) This item differs from Table 31 because it does not include the unused borrowing margin on ordinary advance accounts and, up to Aprile 1969, the deduction of Treasury bills deposited as collateral for advances and postponed payments.— (4) From December 1969, this item includes the special credit institutions' foreign currency deposits with the BI-UIC equalling at end-1972, 637.9 billion lire.— (5) From June 1972, this item includes the banks' foreign currency deposits with the BI-UIC equalling, at end-1972, 261.7 billion lire.

versus 1,132 in 1971); translated into percentages this becomes 24.3 versus 19.4 for the previous year. Savings accounts and interest-bearing certificates, which continued to yield a higher interest rate than the types of bank deposit most resembling them, grew to almost the same extent during the two years (21.7 per cent in 1972 and 20.7 in 1971). Instead, current account deposits increased by 341 billion, equal to about 47.5 per cent versus 9 per cent in 1971. The marked upswing took place in December and, as already described in the chapter on *Public Finance,* depended upon delays in crediting to the Budget revenues from general turnover tax collections (about 100 billion) and the incidental holding of funds normally kept in the banks.

The growing monetary base reserves — up 1,888 billion between December 1971 and December 1972, 1,166 of which in lire and 722 in foreign currency — paved the way for credit, at falling rates, to expand rapidly during most of the year. The increase in reserves was particularly high during the last six months of the year (Chart 18).

The satisfactory liquidity situation already existing at the beginning of the year enabled the banks to go ahead with their policy of reducing lending rates and, by fostering the demand for securities, continued also to exert positive pressure on the decrease of relative yields. The drop of about half a percentage point, at the beginning of April, in the average return on the banking system's free deposits with the Banca d'Italia and in the rate on ordinary advances, resulted in an equal drop in the average yield from the banks' excess reserves, from 2.4 to 1.9 per cent, as already described in last year's Report. Along with the rapid increase in reserves, linked with the aforementioned operations for financing the Treasury, these provisions have resulted in a further, marked reduction in the entire interest-rates structure, provoking also a rapid expansion of credit, despite stagnant economic activity.

From the beginning of the summer on, the fall-off in the growth rate of the lira-denominated components of the monetary-base bank reserves, in connection with the performance of foreign accounts, led to the gradual use of excess reserves to create compulsory reserves.

Liquidity in lire continued to decline in October, owing to seasonal factors, and in November because of the above-mentioned advance issue of Treasury bills for 200 billion. At end-November, the effects of the currency crisis combined with the impact of rate increases for fixed-term advances; the upshot was temporary liquidity tensions, which disappeared in the first months of 1973.

At the end of December 1972 excess bank reserves amounted to 2,500 billion, 1,753 of which in lire and 747 in foreign currency; the ratio of liquidity to deposits equalled 4.3 per cent for the total and 3 for the portion in lire. A year earlier the excess reserves amounted to 1,849 billion, almost entirely in lire. The highest level in absolute value, and in relation to deposits, was reached in May 1972.

Compulsory reserves, as already mentioned, increased between end-1971 and end-1972 by 1,237 billion (Table 31). Comparing this increase with that in clients' bank deposits, between November 1971 and November 1972, there emerges a marginal ratio of 14.6 per cent compared with 17.6 per cent for the previous year; thus, an upswing in compulsory reserves, not much steeper than the previous year, was able to back a very much greater increase in bank intermediation.

Banking

Bank intermediation and liquidity

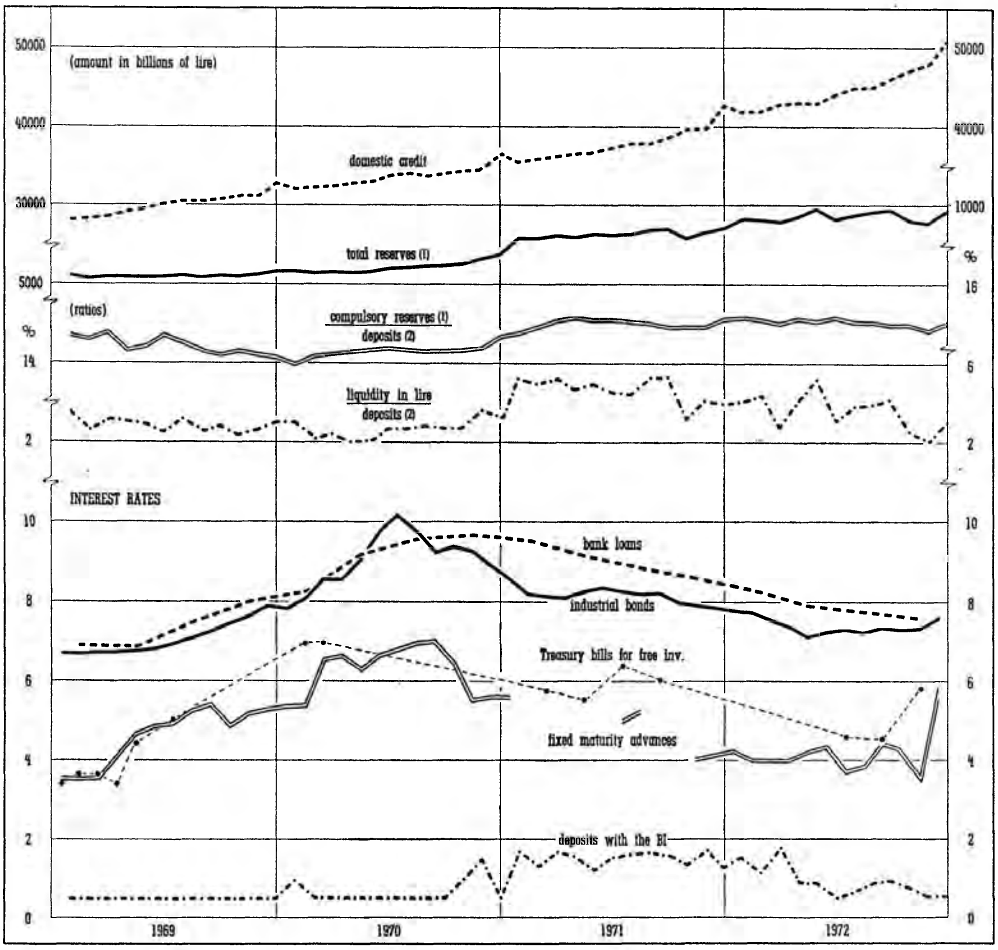
The upswing in the demand for bank loans during 1972 brought about a rapid growth in the volume of bank intermediation and a shift in the structure of the banks' balance-sheet assets from securities to loans. Bank credit expansion was fostered by the banks' excess reserve position at the beginning of the year and by maintaining an easy monetary policy. During the second half of the year this policy had to be toned down owing to the balance-of-payments constraint, which was made tighter by the narrowing of fluctuation margins for EEC currencies, as described in the chapter on the *Balance of Payments.*

During the year, the fall-off in the growth rate of the banks' monetary base was offset by a rise of the credit multiplier, stemming from a decline in both the marginal ratio of compulsory reserves to deposits and the bank liquidity ratio (Chart 19).

The trend of domestic currency excess reserves reflects not only monetary policy measures but also the process of adjusting bank liquidity to the lower reserve levels required under normal banking conditions;

this behaviour on the part of the banks was affected by the reduction in interest rates on free deposits with the Banca d'Italia. In the light of rising yields on Treasury bills and expanding interbank accounts, as well as in relation to the higher cost of the banks' recourse to Banca d'Italia credit facilities, it appears that, during the last quarter, liquidity declined more than the banks desired. This disequilibrium disappeared towards the end of the year, partly as a result of the fact that banks were allowed to enter swaps at par with the UIC, thereby making it easier to convert foreign currency liquidity into lire.

CHART 19



Bank reserves, credit and financial ratios.. Money and financial market interest rates

(1) In monetary base.— (2) The value of deposits at December 1972 is adjusted for random movements.

At the end of the year, the drop in liquidity concerned only the *major* banks which, although experiencing an expansion of deposits almost equal to the system's average, greatly speeded up their lending activity (Table 37).

Table 37

BANKS' ASSETS AND LIABILITIES

(changes in billions of lire)

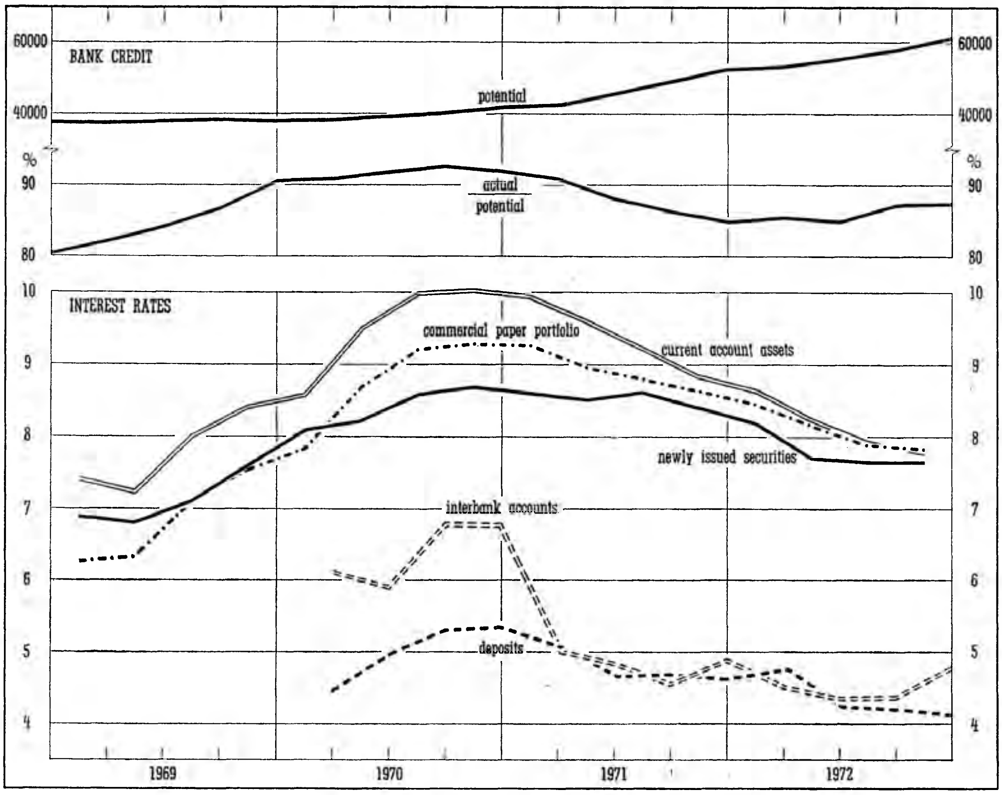
Items	BANKS Major 1971	Major 1972	BANKS TOTAL 1971	TOTAL 1972	SAVINGS BANKS TOTAL 1971	SAVINGS BANKS TOTAL 1972	CENTRAL CREDIT INSTITUTIONS 1971	CENTRAL CREDIT INSTITUTIONS 1972	GRAND TOTAL 1971	GRAND TOTAL 1972
DOMESTIC ASSETS	3,861.6	7,285.0	8,585.1	14,941.5	2,918.2	3,904,2	1,445.2	1,430.9	12,948.5	20,276.6
Liquidity in lire	428.1	- 277.9	467.3	- 160.7	26.0	35.8	- 11,9	52.2	481.4	- 72.7
cash and deposits with BI	*378.8*	*- 235.0*	*393.3*	*- 123.6*	*5.5*	*31.6*	*- 3.5*	*54.1*	*395.3*	*- 37.9*
unused borrowing margin	*43.5*	*- 37.7*	*71.6*	*- 33.9*	*23.0*	*- 2.6*	*- 8.4*	*- 1.9*	*86.2*	*- 38.4*
Other claims on the Treasury and the Central Post Office Savings Fund	*5.8*	*- 5.2*	*2.4*	*- 3.2*	*- 2.5*	*6.8*	..	..	*- 0.1*	*3.6*
Compulsory reserves and backing for cashiers' cheques	428.0	461.4	1,172.4	1,342.3	424.2	523.9	- 1.5	0.7	1,595.1	1,866.9
cash	*237.6*	*- 23.2*	*715.5*	*260.7*	—	—	—	—	*715.5*	*260.7*
Treasury bills	*206.4*	*487.2*	*375.2*	*915.7*	*0.3*	*- 5.0*	—	—	*375.5*	*910.7*
long-term securities	*3.0*	*- 1.5*	*52.4*	*6.6*	—	—	—	—	*52.4*	*6.6*
other long-term securities	*- 19.0*	*- 1.1*	*29.3*	*159.3*	*423.9*	*528.9*	*- 1.5*	*0.7*	*451.7*	*688.9*
Domestic credit (a+b+c+d+e)	1,509.9	2,246.0	3,889.4	5,191.1	1,015.3	2,043.5	1,188.6	935.4	6,093.3	8,170.0
Securities available *(a)*	542.6	- 425.8	1,075.5	6.2	306.3	742.6	944.8	- 377.5	2,326.6	371.3
Treasury bills	*409.8*	*- 451.3*	*517.2*	*- 544.1*	—	—	*138.4*	*- 138.1*	*655.6*	*- 682.2*
bonds	*153.4*	*32.4*	*596.1*	*565.9*	*299.7*	*748.7*	*809.2*	*- 240.6*	*1,705.0*	*1,074.0*
shares	*- 20.6*	*- 6.9*	*- 37.8*	*- 15.6*	*6.6*	*- 6.1*	*- 2.8*	*1.2*	*- 34.0*	*- 20.5*
Securities pledged *(b)*	- 33.6	557.4	98.2	846.3	- 58.0	184.1	53.5	874.1	93.7	1,904.5
Treasury bills	*- 12.0*	*136.1*	*- 7.1*	*154.4*	*- 0.3*	..	—	*609.0*	*- 7.4*	*763.4*
bonds	*- 10.8*	*422.1*	*120.2*	*685.8*	*- 57.7*	*184.1*	*55.0*	*265.1*	*117.5*	*1,135.0*
shares	*- 10.8*	*- 0.8*	*- 14.9*	*6.1*	..	..	*- 1.5*	—	*- 16.4*	*6.1*
Domestic lending *(c)*	964.8	2,127.7	2,597.2	4,254.9	744.3	1,116.4	190.1	411.2	3,531.6	5,782.5
short-term: in lire	*863.7*	*2,717.7*	*2,162.4*	*4,707.0*	*191.0*	*562.1*	*39.0*	*423.3*	*2,392.4*	*5,692.4*
in foreign currency	*72.7*	*- 640.9*	*67.2*	*- 970.0*	*20.9*	*- 57.7*	—	—	*88.1*	*-1,027.7*
medium- and long-term	*28.4*	*50.9*	*367.6*	*517.9*	*532.4*	*612.0*	*151.1*	*- 12.1*	*1,051.1*	*1,117.8*
Accounts with special credit institutions *(d)*	22.5	- 34.6	77.6	45.2	22.2	- 40.8	- 0.3	27.2	99.5	31.6
Investments in partnerships *(e)*	13.6	21.3	40.9	38.5	0.5	41.2	0.5	0.4	41.9	80.1
Interbank accounts	- 90.9	537.9	644.1	1,566.4	989.9	686.1	152.6	266.8	1,786.6	2,519.3
Other items	1,586.5	4,317.6	2,411.9	7,002.4	462.8	614.9	117.4	175.8	2,992.1	7,793.1
FOREIGN ASSETS	821.4	3,003.4	1,317.6	3,744.9	1.1	5.0	—	—	1,318.7	3,749.9
Liquid foreign assets	- 28.3	44.3	13.8	132.4	2.5	6.5	—	—	16.3	138.9
monetary base in foreign currencies	*- 91.1*	*412.9*	*- 115.9*	*683.9*	*- 0.7*	*19.3*	—	—	*- 116.6*	*703.2*
Foreign credit	849.7	2,959.1	1,303.8	3,612.5	- 1.4	- 1.5	—	—	1,302.4	3,611.0
TOTAL	4,683.0	10,288.4	9,902.7	18,686.4	2,919.3	3,909.2	1,445.2	1,430.9	14,267,2	24,026.5
DOMESTIC LIABILITIES	3,694.2	7,103.8	8,476.3	14,704.5	2,921.1	3,896.1	1,445.2	1,430.9	12,842.6	20,031.5
Customers' deposits	1,900.6	2,682.0	5,127.6	7,331.3	2,010.0	2,972.5	68.1	141.8	7,205.7	10,445.6
time and saving deposits	*267.2*	*406.1*	*1,173.5*	*1,953.7*	*888.4*	*1,280.2*	—	—	*2,061.9*	*3,233.9*
demand deposits	*1,633.4*	*2,275.9*	*3,954.1*	*5,377.6*	*1,121.6*	*1,692.3*	*68.1*	*141.8*	*5,143.8*	*7,211.7*
Residents' foreign currency deposits	- 30.5	64.6	- 34.7	155.5	0.2	7.5	—	—	- 34.5	163.0
Third parties' funds held for administration	32.0	34.5	- 43.6	- 47.1	50.9	- 79.6	0.3	0.1	7.6	- 126.6
Lending by BI-UIC (1)	- 54.3	459.8	- 53.0	661.8	- 24.2	143.3	166.8	623.5	89.6	1,428.6
rediscounting	—	—	*- 39.7*	*35.6*	*- 1.9*	*- 0.1*	—	—	*- 41.6*	*35.5*
delayed payments and fixed-term advances	*- 75.5*	*398.3*	*- 43.9*	*521.9*	*- 5.6*	*137.2*	*117.2*	*617.9*	*67.7*	*1,277.0*
ordinary advances (credit lines)	*21.2*	*61.5*	*30.6*	*104.3*	*- 16.7*	*6.2*	*49.6*	*5.6*	*63.5*	*116.1*
Equity capital	3.4	5.8	49.7	108.1	36.3	75.7	4.0	5.5	90.0	189.3
Interbank accounts	81.2	606.1	473.7	1,100.2	99.8	78.8	1,016.3	389.3	1,589.8	1,568.3
Accounts with special credit institutions	103.1	99.4	366.4	107.7	147.8	126.6	93.1	- 4.1	607.3	230.2
Other items	1,658.7	3,151.6	2,590.2	5,287.0	600.3	571.3	96.6	274.8	3,287.1	6,133.1
FOREIGN LIABILITIES	988.8	3,184.6	1,426.4	3,981.9	- 1.8	13.1	—	—	1,424.6	3,995.0

(1) Including transactions in foreign currencies.

Domestic credit increased by 8,170 billion, equal to a 19.6 per cent rise, an appreciable increment in relation to 1971 (6.093 billion and 17.1 per cent). The expansion of customers' deposits, calculated on the basis of the banks' financial statements, amounted to 10,446 billion, which falls to 8,600 billion (7,205 in 1971) if one deducts the estimated value of the increase caused by year-end strikes.

The impact of these strikes on the banking sector has been assessed on the basis both of indications from estimates of bank demand functions and of an analysis of data time-series.

CHART 20



Potential and actual bank credit

Given the foregoing developments in credit, deposits and liquidity volumes as well as the 1,867 billion increase in compulsory reserves, the banks were forced to resort to the Central Bank for the sum of 1,429 billion, almost entirely during December; this flow also reflects the above-mentioned random movements which, it is estimated, accounted for a third of it. Finally, the banks resorted to foreign loans and increased, over the year, their net indebtedness by about 250 billion, on authorization granted by the monetary authorities in June 1972.

Credit market conditions are summarized by comparing the actual growth of bank credit with the maximum increase allowed by the banks' holdings of monetary base reserves (Chart 20).

The ratio of actual values to potential values is a comprehensive indicator, since the potential credit variable reflects all of the above-mentioned variables affecting the supply of bank credit and also assumes — on the basis of econometric estimates — a given time-lag structure in the liquidity position's adjustment process.

The development of potential values points to continuing rapid growth of the banking system's supply of credit; however, the quickened growth rate of actual credit first limited the widening of the spread between theoretical and actual values early in the year and, second, caused an about-turn in this trend over the final half. Tensions which characterized the credit market over the last months were sharpened by the fact that a greater use of credit lines took place at a moment when the amounts borrowed were a rather low percentage of the credit lines granted to customers.

TABLE 38

BANK LENDING RATES (1)

Items	Quarters									
	1970		1971				1972			
	III	IV	I	II	III	IV	I	II	III	IV
Categories of credits										
Portfolio: of commercial paper . .	9.20	9.28	9.26	8.96	8.81	8.64	8.45	8.15	7.90	7.81
of financial assets	9.45	9.35	9.19	8.92	8.90	8.90	8.49	8.32	7.67	7.38
Demand deposits	9.99	10.03	9.96	9.62	9.24	8.85	8.65	8.24	7.92	7.79
Foreign transactions	8.71	8.76	8.42	7.72	7.33	7.37	6.73	6.31	6.09	5.74
Guarantees	8.20	8.64	8.19	7.74	7.78	7.59	6.62	6.23	7.11	7.05
Some branches of economic activity										
Fuel and power	9.53	9.40	8.88	8.01	7.38	7.12	7.05	7.12	6.62	6.87
Building	10.20	10.29	10.19	9.85	9.67	9.50	9.33	8.91	8.76	8.61
Foodstuffs and similar	9.77	9.80	9.65	9.29	8.98	8.83	8.50	8.11	7.94	7.67
Petroleum and natural gas	9.49	9.66	9.41	8.73	8.26	7.86	7.33	7.03	6.60	6.49
Metallurgy	9.51	9.40	9.12	8.62	8.19	7.79	7.52	7.15	6.82	6.72
Engineering	9.65	9.72	9.62	9.16	8.81	8.49	8.21	7.84	7.53	7.40
Chemicals	9.63	9.54	9.45	9.00	8.39	8.04	7.62	7.28	7.14	6.92
Rubber	9.27	9.58	9.35	8.88	8.46	8.03	7.79	7.21	6.96	6.89
Textiles and clothing	9.69	9.65	9.57	9.17	8.90	8.67	8.33	7.94	7.71	7.53
TOTAL . . .	9.58	9.66	9.53	9.14	8.86	8.60	8.32	7.91	7.74	7.56

(1) Quarterly averages of the rates on operations registered by the Central Risks Office. Excluding interbank and intercredit financing.

The fading of expectations of capital gains on long-term securities helped to increase the supply-of-loans component of total potential credit — whereas in 1971 high yields on newly issued securities had curbed it — so that the continual fall of bank lending rates does not reflect the developing ratio of actual credit to potential credit. Moreover, the behaviour of bank rates can also be explained by their stickiness — greater than for the other yield rates — in moving towards their equilibrium levels: the drop in lending rates, fostered by the lower deposit rates, in fact made up for 1971's unsatisfactory decrease (Table 38).

Interest rates on deposits, despite the favourable liquidity position, rose in the first quarter of 1972 owing to keener competition within the banking system. From the second quarter on, the reduction of deposit rates agreed upon by the banks allowed the yield to be brought into line with money market conditions; the decline in deposit rates continued over the second half of the year, thus the average rate on resident customers' deposits was 0.47 points lower than the average for 1971 (Table 39).

Table 39

BANK DEPOSIT RATES (1)

Items	Quarters									
	1970		1971				1972			
	III	IV	I	II	III	IV	I	II	III	IV
Categories of liabilities										
Demand deposits: free	5.31	5.42	5.01	4.57	4.56	4.50	4.74	4.03	4.04	3.98
tied	5.35	5.20	5.80	5.74	5.58	5.59	5.35	5.36	5.12	5.13
Savings deposits: free	4.65	4.75	4.25	3.80	3.89	3.66	4.14	3.75	3.76	3.58
tied	5.40	5.52	5.39	5.39	5.39	5.41	5.40	5.21	5.32	5.25
Third parties' funds for administr.	3.80	2.89	2.82	1.45	3.86	3.96	3.91	3.68	3.92	3.84
Foreign currency accounts:										
of residents	6.85	6.26	5.66	5.30	4.91	5.25	4.99	4.26	3.52	4.00
of non-residents	6.01	5.51	4.85	4.71	4.72	4.71	3.85	3.13	3.50	3.22
of foreign corresp.: free . . .	8.36	6.85	6.91	6.30	6.39	5.62	5.24	4.60	4.32	4.42
tied . . .	8.55	7.93	6.78	5.96	6.86	6.35	5.09	4.97	4.88	5.66
Banks' and credit institutions' accounts	6.18	6.00	5.44	4.97	5.08	5.03	5.06	4.60	4.66	4.42
banks' free deposits	*6.79*	*6.77*	*5.02*	*4.85*	*4.54*	*4.92*	*4.51*	*4.36*	*4.37*	*4.79*
Total for ordinary customers . . .	5.32	5.35	5.07	4.68	4.70	4.62	4.76	4.25	4.22	4.11
Grand total . . .	6.00	5.87	5.45	5.00	5.10	4.95	4.87	4.40	4.37	4.43

(1) Rates in force at end-quarter on deposits over 20 billion lire.

In conclusion, the effects of an easy monetary policy, which were first felt in 1971, developed their full impact in 1972, both in terms of expanded credit flows and of lower interest rates.

The banks' intermediation on the international markets was even more vigorous. They raised 3,982 billion worth of funds (1,426 in 1971), which were used to increase foreign credits (3,612 billion versus 1,304 in 1971) and liquid assets in foreign currency (132 billion compared with 14 in 1971). The excess of funds borrowed abroad over foreign loans helped to improve the liquidity position in lire late in 1972. Here again the general development pattern was mainly determined by the *major* banks (Table 37).

The increase in foreign currency monetary base exceeded the upturn in foreign currency liquid assets, since the measures taken at end-June and the beginning of December, authorizing the banks to take up net external debtor positions, freed assets — previously blocked by the restriction on the banks to maintain a balanced position — for use in expanding domestic lending. In fact, between July and December, these measures were less of an incentive both because foreign currency monetary base was larger than the banks' *plus* position and because of widespread expectations of the lira's devaluation. However, this situation was reversed when the banks, on December 4, were allowed to take out loans in foreign currency with the UIC at guaranteed exchange rates.

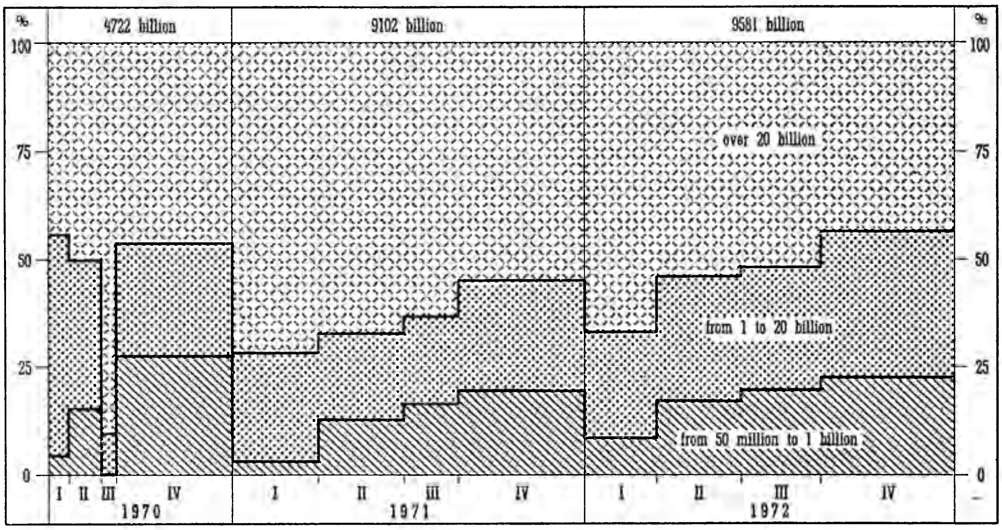
Along with the opportunity to use foreign currency liquid assets to increase domestic lending, the end-June currency provisions allowed the banks to increase their net external liabilities. In reality, at the end of June there were no incentives for the banks to borrow abroad because of higher short-term interest rates on the Eurodollar market than domestic interbank rates, expectations of a revaluation of some foreign currencies, abundant lira liquidity and uncertain credit demand. Changes in some of these conditions, along with the previsions of December 4, fostered an increase in net external liabilities late in the year.

At the end of the year bank loans had reached the 36,368 billion level, showing an 18.9 per cent increase over December 1971 (13.1 per cent in the previous year); although the increase was probably inflated by the above-mentioned random movements at end-year, there was a reversal of the slowdown registered over the three years 1969-1971. Moreover, average bank lending rates continued to fall, dropping from 8.60 per cent at end-1971 to 7.56 per cent in the fourth quarter of 1972 (Table 38).

Considering the low interest-rate elasticity which characterizes credit demand, it appears that other factors were mostly responsible for the expansion of demand. Along with the growth in production and investment over the year, the enterprises' tendency to acquire financial assets was also responsible for the acceleration in the recourse to the banking system. Among the above assets a more important role was played by net foreign trade credits, whose increase largely accounts for the deterioration in the balance of payments on a cash basis.

Over the year, the expansion of credit supply was sufficient to satisfy the additional demand for loans at decreasing interest rates. Larger supply resulted in a rise in the amount of credit granted, which was concentrated less on large-sized loans than in the previous year (Chart 21). This development, along with the widening of interest rate spreads between different classes of loan size — which continued despite the fact that rates on loans exceeding 20 billion declined less

CHART 21



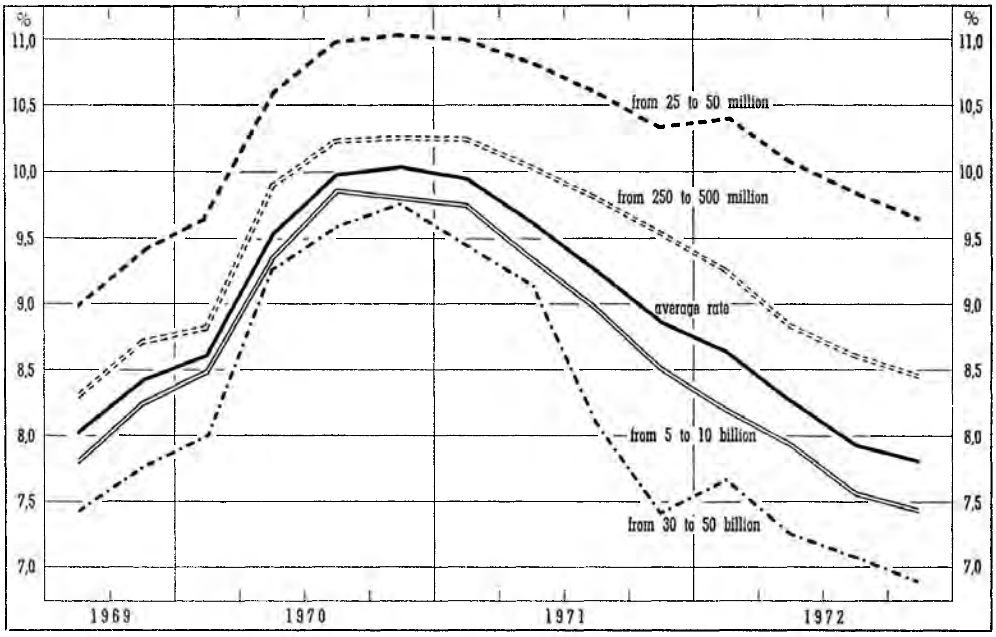
Percentage distribution of increases in financing classed according to loan size

Credit increases (in billions of lire) during the different periods are shown on the horizontal axis; the division of increases into three groups according to loan size are represented on the vertical axis (aggregate indebtedness of each customer towards the banking system).

than in 1971 when there was a sharp fall-off — seems to point to the banks' completion of their policy of gradually reducing loan rationing, to the extent that the structure of lending rates alone made it possible to maintain the preferred composition in terms of loans of different size and, therefore, different degree of risk (Table 38 and Chart 22). This interpretation is supported by the larger drop in the small customers' degree of use of the loan granted.

Results for the entire year stem from opposite trends during the two halves of the year, with growth gathering considerable speed during the second half when expectations of the lira's devaluation caused a massive export of short-term capital. Thus, a huge upswing

CHART 22

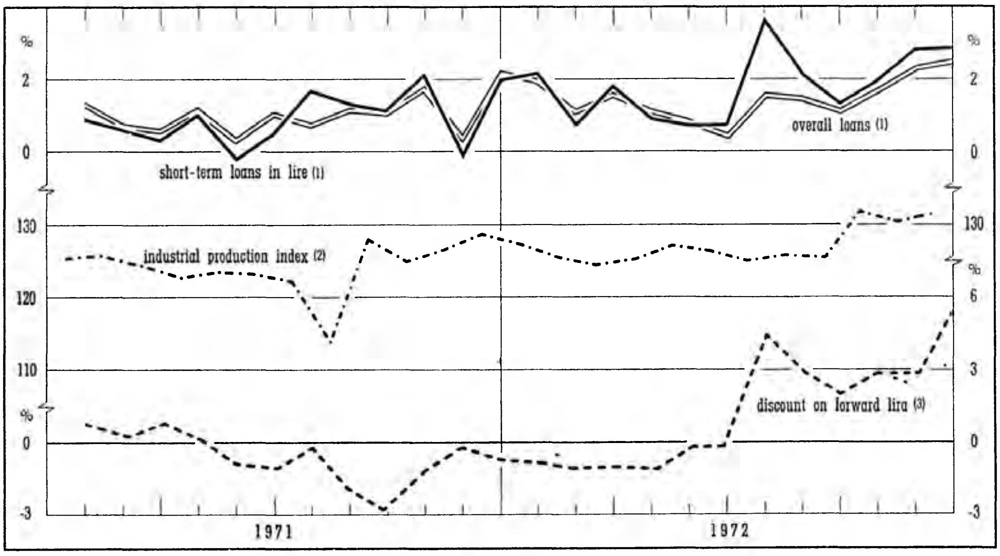


Lending interest rates for some groups according to size of loans
(current accounts)

in overall lending was registered in July, along with a marked tendency on the part of the enterprises to substitute foreign currency debts with short-term borrowing from the banks — the former showing a 520 billion fall-off, equal to a third of the total, in July itself. The largely speculative nature of credit demand between June and August is also evidenced by the stagnation of industrial production during the same period. Following a certain slowdown during September, lending speeded up once again, and reached the highest rates of the year in a period when renewed uncertainty on the lira's parity was coupled with the production upswing (Chart 23).

The smaller flow of monetary base to the banks and the increased demand for loans point to a related tension arising on the credit market during November and December. This tension shows up, moreover, in the deceleration of the decline in average lending rates (which dropped from 0.69 points in the first half of the year to 0.35 points during the second), in the fact that, for some classes of large-sized loans, this fall-off came to a halt in the last quarter and in the renewal (January 1973) of the banks' commitment to limit competition in lending at interest rates lower than the minimum allowed by their own agreement.

CHART 23



Bank loans

(1) Monthly percentage variation rates on seasonally adjusted data.— (2) Seasonally adjusted data.— (3) Regarding the three months lira–dollar exchange.

Foreign currency loans, following the end-June and July speculation crisis, continued to fall; for the whole of the last two quarters the reduction amounted to about 1,000 billion. Parallely, the banks' debtor position with the Ufficio Italiano dei Cambi decreased by circa 1,200 billion of which 774 billion lire concern loans in dollars, which had soared during 1971, and 209 billion, loans in Swiss francs. Loans in Deutschemarks, however, increased — although their total is still low — as a result of the sharp decline in their interest rates, carrying a forward cover against revaluation risks for an average of only 20 per cent. These developments reveal the customers' differing expectations regarding parity changes early in 1973. Moreover, uncertainties on the foreign exchange front over the last two years in general induced borrowers to hedge against exchange rate risks. Foreign currency credits covered by forward operations, which were completely negligible at the end of 1970 (0.3 per cent), leaped up to 13.3 per cent of total credit at end-1972.

The nature of the acceleration in overall loans — in connection with the emergence of symptoms of a recovery in economic activity and strengthened by the upswing in the enterprises' domestic and foreign financial assets — accounts for the higher portion of short-term financing as well as loans to private enterprises in the year's total flow. The larger amount of loans granted to medium- and small-sized private firms in turn was partly responsible for the lively growth of short-term loans, whose proportion of the total liabilities of the Economy's private sector turned out to be very high. Bank loans granted to the local authorities also increased in terms of percentage of the total credit.

The banks counterbalanced the larger flow of high-risk or low-liquidity loans by checking the reduction of interest rates on such loans; the result was a wider spread between the cost of borrowing for state-controlled enterprises and private companies, on one hand, and that for individual enterprises and local authorities, on the other (Table 38).

The public sector's net liabilities towards the banking system expanded heavily (about 3,700 billion, versus 2,400 in 1971), owing to both the faster expansion of borrowing — particularly by the local authorities and autonomous government agencies — and the shrinkage in deposits, following 1971's sharp rise. The upswing in households' deposits, instead, resulted in a greater increase in the total assets of the enterprises and households sector than in 1971 (5,600 billion, as against nearly 3,500), despite the firms' heavier borrowing.

The distribution of new loans by sectors of economic activity reflects, as does distribution by types of borrowers, the different intensities in demand for credit and, in some cases, changes in the debt structure. Bank financing rose substantially in the transport sector (46 per cent), in telephone (131 per cent) and health services (71 per cent), in the petroleum (46 per cent), metallurgy (22 per cent) and chemicals industries (23 per cent). The rubber and mechanical engineering industries registered unappreciable growth rates (12 and 14 per cent, respectively), although higher than in the previous year; the portion of bank loans in their total debt soared. Loans for mines and quarries, agriculture and the foodstuffs industry, non-metallic minerals, paper and building industries progressed at a low rate (Table 61).

The spread between borrowing costs in the various sectors of economic activity also widened, since the initially higher rates experienced smaller decreases (Table 38). Such different behaviour of interest rates is mainly a supply phenomenon, as in the case of loans granted to different types of borrowers, in the sense that banks discriminate between firms according to their ability to tap other credit sources, their size and the cyclical developments in the economic sector to which they belong.

During the year, overall net purchases of securities by the banks amounted to 3,882 billion (3,000 in 1971) (Table 37).

Excluding the portion deposited for compulsory reserves — which, owing to the sharp upswing in savings deposits, was especially high in 1972 (1,606 billion compared with 880 in 1971 including, respectively, 911 and 375 billion of Treasury bills) — the amount of newly issued securities, including Treasury bills which the banks freely decided to include in their portfolio, amounted to 2,276 billion (2,420 in 1971).

The term structure of portfolio investments was altered to take in more long-term securities, thus reflecting a decrease in the supply of Treasury bills for free investment (75 billion of net issues in 1972 versus 958 in 1971).

The factors mentioned earlier, along with the timing of securities issues, fostered a shift towards loans in the structure of the bank credit flow. Until May, the supply of fixed-interest securities available to the banking system was far from large, even in comparison to that of the same period of 1971, and was acquired by the banks in a period of falling yields; more specifically, no Treasury bills for free investment were issued, even though 375 billion reached maturity. During the last six months of the year, the excess of new long-term securities issues over the non-banking public's demand showed an increase, with repercussions on yield rates, which were also sharpened by stronger pressures on the side of trade credit demand, particularly towards the end of the year.

The gradual narrowing of the spread between bank lending rates and rates on new issues, from the second quarter on, partially accounts for the changes in the structure of bank credit flows which took place mainly during the first half of the year.

In 1972, the reduction of the ratio of securities to the total of new bank credit (from 42 per cent in 1971 to 29 per cent) arises from the contrasting development patterns for commercial banks and savings banks. The former, institutionally more exposed to trade credit demand fluctuations, reduced their share of securities from 33 to 18 per cent. Vice versa, the savings banks increased their percentage of the total from 27 to 45 per cent; however, after taking into account these banks' central credit institutions which purchased securities for a considerable sum in 1971, the savings bank system is also seen to have reduced its percentage of securities, from 57 to 48. The shift from securities to loans mainly concerned the *major* banks, which made few purchases of securities for free investment.

There was a 1,904 billion increase in securities deposited as compulsory reserves owing to heavy liquidity needs at end-year also stemming from the bank strikes; in fact, at the end of November, the change with respect to the same month in 1971 amounted to only 235 billion.

At the end of 1972 bank deposits had reached 57,670 billion, with an annual increase of 22.1 per cent, which is reduced to 18.5 per cent (18 per cent in 1971) once data are adjusted for random movements at end-year.

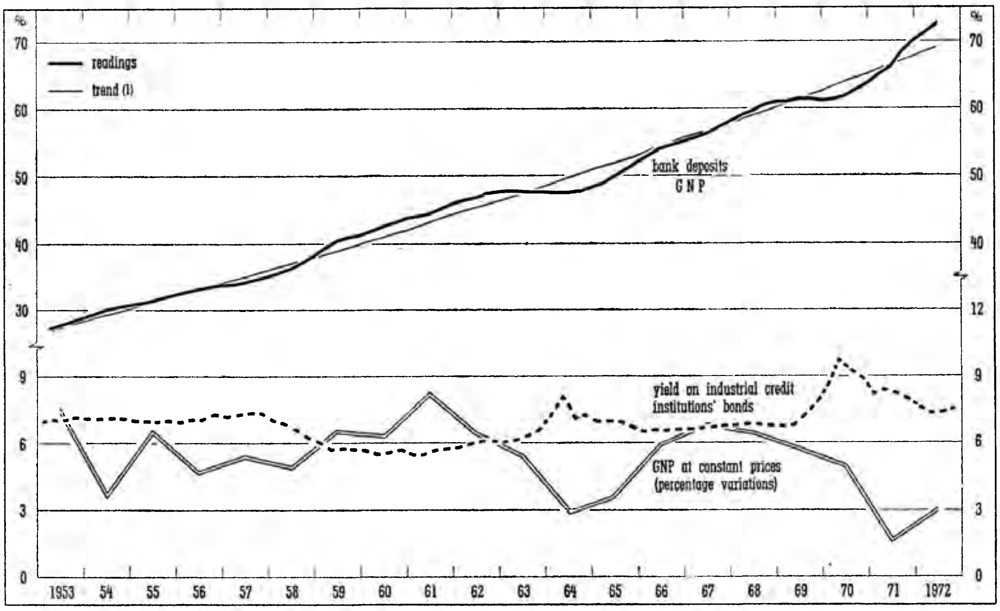
Given the institutional features of the Italian money market, the demand for bank deposits, including current accounts, must be analyzed within the framework of the development of overall financial assets. For 1972 as a whole, the percentage of bank deposits in financial saving decreased as a result of the financial asset portfolio adjustment process which always follows a period of pronounced change in bank deposits. More specifically, diversification among assets denominated in different currencies resulted in the public's shift towards foreign assets, which was fostered — from mid-year on — by the emergence of expectations of the lira's depreciation.

In contrast, the shift of funds from bank deposits to Post Office deposits seems to have lost the relevance it had in 1971, despite the wider spread between the yield on Post Office interest-bearing certificates and that on bank deposits in 1972.

Preference for liquidity over fixed-interest securities, which declined in 1971 owing to the upward trend in securities prices, increased in 1972 because of a greater uncertainty about future prices and a narrower spread between the average yearly yield on long-term securities and that on bank deposits.

With regard to the long run trends, in 1972 the ratio of average bank deposits to gross national product continued to increase faster than the trend line, as a result of the expansionary role played by monetary policy on the economy from mid-1970 on, when this ratio registered the maximum negative shift away from the trend (Chart 24).

CHART 24



Bank deposits and gross national income (2)

(1) Quadratic interpolation.— (2) Ratio of the average size of bank deposits to the gross national product for the 12-month period centered on the quarter used for reference. The amounts at end-1967 and end-1972 are adjusted for random movements.

Whereas the rise in the ratio of bank deposits to GNP does not mirror money market conditions — since the demand for deposits is, above all, a function of wealth — divergencies of this ratio's trend away from the long-term trend reflect the anticyclical nature of monetary policy. In 1972 — another year which was characterized by flagging economic activity — the expansion of bank deposits, at a higher rate than that implied by the longer-term correlation with the growth rate of the nominal GNP, was fostered by the monetary authorities in order to bring about a decline in the cost of credit and to stimulate a revival of production. The development of the Economy's liquid assets mirrors the rise of bank deposits which are the main component of these assets (Table 40).

The percentage of savings deposits in the total of bank deposits, after the adjustments for random movements at end-year, rose as a result of a sharper fall in interest rates on current accounts — which led to a reversal of the sign of the yield difference between the two types of deposits (Table 39).

The stronger tendency towards a more balanced composition of bank deposits, which represents a reversal of the 1969 and 1970 trend, caused the banks to reduce the marginal ratio of required reserves to be covered with monetary base.

TABLE 40

BANK DEPOSITS, LIQUID ASSETS AND GROSS NATIONAL PRODUCT

(rates of increase)

Period	Bank deposits	Primary liquidity (M 1)	Liquid assets (M 2)	Gross national product		
				at current prices	at constant prices	implicit GNP deflator
1951 - 1957	16.4	11.0	12.8	9.6	5.8	3.7
1958 - 1963	16.2	14.2	14.2	10.0	6.3	3.5
1964 - 1965	13.1	11.8	11.8	8.6	3.4	4.9
1966 - 1968	14.5	13.4	12.9	8.6	6.3	2.3
1969 - 1972	16.2	19.8	15.2	9.9	3.8	6.0
1969	11.9	15.7	11.4	10.2	5.7	4.2
1970	16.1	27.2	13.6	11.8	4.9	6.6
1971	18.0	18.8	17.1	8.3	1.6	6.6
1972	18.9	17.9	18.5	9.3	3.2	5.9

M 1 = Currency + bank and Post Office current accounts.
M 2 = M 1 + bank and Post Office savings deposits.

On the basis of the analytical profit and loss figures reported to the Banca d'Italia, in 1972 the banks' net earnings amounted to 122 billion, with an 11.9 per cent increase over 1971; this was in line with performances shown in previous years. Total balance-sheet assets grew much faster (22.3 per cent), or at the highest rate registered during the last decade; as a result earnings per unit dropped to a larger degree than in previous years. The results in terms of earnings per unit were mainly affected by a narrowing of the spread between unit revenues and costs of domestic and foreign intermediation, following the trend started in 1971. With the revenues per unit of services still fairly stable, the narrower spread was only partly offset by the fall in overhead costs per unit, which reflects in particular the decrease of costs for personnel and which practically counterbalanced the last two years' increase.

On the whole, there was a decline in the level of overall unit costs and revenues, due virtually to the fall in specific average costs and revenues as a result of the downturn in main market interest rates over most of the year.

Over recent years the savings banks' unit revenue has gradually gone near to the lower level registered by the commercial banks; for 1972, profit and loss figures reveal instead a greater spread between the earnings per unit in the two banking categories: whereas the commercial banks' earnings fell, those of the savings banks remained fairly steady. This is the consequence, above all, of the increasing spread between revenues and average specific unit costs, which was only partly offset by the different magnitude of the decrease in overhead costs for the two banking categories.

The commercial banks' characteristic of operating at lower lending and deposit rates levels than the savings banks, seems to have become more pronounced, as revealed by the larger decline in specific unit revenues and costs registered in the profit and loss figures. In order to explain this larger fall-off one should take into account the fact that the banks — especially those which because of their magnitude most influence the category's overall performance — are not only more directly affected by impulses stemming from monetary policy measures but also deal with customers who are very sensitive to market conditions and operate largely in the short-term market section, where rates change much faster than in the medium- and long-term sections.

Structural development during the five years 1967-1972

The growing importance of bank size in determining the banking institutions' behaviour and balance-sheet structure made felt the need to compile statistics, from 1967 on, on the basis of the banks' size. As the five-year period has come to an end, and on the occasion of the forthcoming reclassification of banks (Table 41), it would seem appropriate to discuss briefly the main structural changes that have taken place within the banking system between 1967 and 1972.

In order to regroup the banks according to their size it has been necessary to establish new maximum-values for the classes so that normal expansion of the volume of bank intermediation over a period of time does not result in the

TABLE 41

CLASSIFICATION OF THE BANKS BY SIZE GROUPS

Bank groups	1967					1972							
	Number	Index of closeness (1)	Share of: Intermediation (2)	Share of: Branches (3)	Share of: Employees (3)	Number	Indexes of: identity (4)	Indexes of: Rank (5)	Indexes of: Closeness (1)	Share of: Intermediation (2)	Share of: Branches (3)	Share of: Employees (3)
Banks	258	—	100.0	100.0	100.0	241	0.94	0.98	—	100.0	100.0	100.0
major	5	—	42.0	24.3	45.0	5	1.00	1.00	—	41.1	23.4	43.0
large	5	69.6	19.2	19.6	19.7	5	1.00	0.70	76.8	18.9	19.2	20.7
medium	11	61.0	15.8	18.3	14.3	11	1.00	0.84	64.6	15.9	18.2	14.5
small	20	88.6	10.4	14.1	8.6	20	1.00	0.86	92.6	10.8	14.0	9.0
minor	217	88.7	12.6	23.7	12.4	200	0.93	0.96	97.3	13.3	25.2	12.8
Savings banks . . .	87	—	100.0	100.0	100.0	87	1.00	0.99	—	100.0	100.0	100.0
major and large .	3	—	33.6	23.4	30.0	3	1.00	1.00	—	31.1	22.7	30.1
medium	4	61.5	16.0	14.8	15.8	4	1.00	0.80	66.4	16.8	14.9	16.7
small	28	71.5	34.8	36.8	37.1	29	1.00	0.94	72.3	36.7	38.0	36.6
minor	52	90.8	15.6	25.0	17.1	51	0.98	0.98	90.2	15.4	24.4	16.6
Commercial banks .	345	—	100.0	100.0	100.0	328	0.96	—	—	100.0	100.0	100.0
banks	258	—	73.3	67.3	76.3	241	0.94	0.98	—	72.8	67.4	75.2
savings banks . .	87	—	26.7	32.7	23.7	87	1.00	0.99	—	27.2	32.6	24.8

(1) Percentage ratio of the volume of intermediation of the first bank in the group to that of the last bank in the group above.— (2) Defined as the total of customers' deposits, special credit institutions' deposits, third parties' funds held for administration, capital and reserves. Averages of quarterly data.— (3) At June 30.— (4) Ratio of the number of banks in the group under both headings to number of banks forming the group under the first heading.— (5) Measure of the variations in rank expressed by the Spearman coefficient applied to banks in the same group under both headings (the index takes the value + 1 if the rank is the same and − 1 if the rank is reversed).

banks' gradually crowding into the large-sized headings; the new values have been obtained by increasing the 1967 values on the basis of the five-year growth rate of the banking institutions.

Comparison between the two classifications points, above all, to the almost complete lack of change in the composition of the various headings, thus showing the steady degree of concentration of the Italian banking system; even the distribution, between commercial and savings banks, of the volume of intermediation, number of branches and personnel has remained more or less unchanged, whereas within the two categories there has been only a slight shift from large-sized to small-sized banks.

First, an outstanding feature is the general and growing tendency of the banks to operate on the foreign markets as well, which is evidenced above all by the spreading abroad of the Italian banking network (branches, offices, purchases of capital stock of credit institutions, entering into cooperation agreements with foreign-based banks) and by the analogous increase in the number of foreign financial intermediaries in Italy.

The Italian banks' balance-sheets show a large rise in operations with non resident customers; this was concentrated entirely in the commercial banks category which increased its foreign intermediation at an average annual rate of over 30 per cent, or at about twice that for domestic intermediation. The different sized banks contributed to the phenomenon to about the same extent, thus the *major* banks still dominate in this market and their share remains above the 70 per cent level.

Owing to the provisions in force in Italy during the period under study, regarding the banks' net external position, and perhaps also because of the banks' tendency, at least at times when tensions in their lira liquidity position are absent, to draw a clear line between their domestic and foreign activity, the balance of foreign assets and liabilities was almost nil in relation to the total volume of intermediation. Therefore, there is no need to take into account the foreign component in order to analyze structural changes in domestic intermediation.

The volume of domestic intermediation by the banks, calculated on the basis of deposits, grew over the five years at a far higher average yearly rate (15.3 per cent) than the nominal gross national product (9.5 per cent). This phenomenon is part of the general development of financial intermediation and of the increasing dissociation between sources and uses of savings which has accompanied the growth of the Italian economy.

Changes in the composition of the banking system's assets and liabilities (excluding other items and non resident accounts) between 1967 and 1972 bring to light other structural modifications (Table 42).

In previous Reports stress has been given to the massive transfer of funds from savings deposits to current accounts; it only remains to say that this took place while current accounts were showing a tendency to provide, until 1970, an increasing advantage in terms of interest rates over savings deposits.

The decreasing resort to financing by the Central Bank can, for the most part, be attributed to the different cyclical conditions of the two periods under comparison (recovery in 1967, relative stagnation

TABLE 42

BALANCE-SHEET STRUCTURE OF THE BANKS

(main financial ratios) (1)

Bank groups	Liquidity in lire / Deposits	Reserves (2) / Deposits	Domestic loans / Domestic loans + securities	Short-term loans / Domestic loans	Domestic loans + securities / Total funds	Interbank balance / Balance-sheet total (3)	Deposits / Balance-sheet total (3)	Current accounts / Deposits	BI-UIC credits / Total funds
Banks									
major *1967*	7.1	24.7	88.4	99.3	78.7	– 4.6	76.9	68.4	5.3
1972	6.5	24.5	82.0	98.8	77.6	– 4.1	80.3	80.8	2.7
large *1967*	2.5	23.9	84.1	89.3	73.7	1.8	79.1	51.1	5.1
1972	2.7	23.8	79.9	84.8	76.0	– 0.4	77.8	63.3	4.1
medium *1967*	2.7	23.4	81.6	96.4	72.4	0.1	82.3	51.4	4.3
1972	2.1	23.7	82.5	94.2	72.6	0.1	78.9	62.5	2.1
small *1967*	2.1	22.3	83.3	94.9	63.7	8.5	93.3	35.1	2.2
1972	1.5	22.3	82.6	91.0	60.8	13.9	92.9	48.2	1.6
minor *1967*	2.4	19.4	78.7	94.9	69.9	7.4	89.1	36.1	2.6
1972	1.9	20.8	79.3	92.7	66.4	8.5	85.7	46.2	1.9
Total for banks and central *1967*	4.4	23.4	84.3	96.1	74.5	—	86.5	54.6	4.6
credit institutions (4) *1972*	3.8	23.5	81.1	93.9	73.6	—	88.8	66.0	2.8
Savings banks									
major and large *1967*	1.7	14.6	61.4	47.6	74.8	7.7	75.3	27.6	3.8
1972	1.2	16.9	61.5	48,2	67.5	14.0	74.0	47.8	1.8
medium *1967*	2.6	15.2	70.8	50.1	63.2	17.2	90.5	29.2	3.3
1972	1.7	17.7	74.4	47.6	57.8	21.3	90.8	48.8	2.0
small *1967*	2.0	14.8	69.5	50.5	62.8	17.5	90.8	29.1	2.0
1972	1.3	17.5	72.0	44.8	62.6	17.2	87.6	44.4	1.6
minor *1967*	2.3	15.1	70.7	53.3	64.7	13.6	93.1	20.7	1.6
1972	1.5	17.6	74.3	45.7	63.6	15.1	90.8	34.8	1.2
Total for savings banks and *1967*	3.8	14.7	61.4	51.4	78.6	—	85.7	28.1	4.6
ICCRI (4) *1972*	4.6	17.1	62.2	51.8	78.6	—	84.4	45.7	2.8
Total for the system (5) *1967*	4.3	21.1	78.0	86.2	75.4	—	86.3	47.5	4.6
1972	4.1	21.7	75.4	83.3	75.0	—	87.5	60.2	2.8

(1) Calculated from the average of balance-sheet data of end-March and end-September. — (2) Including backing for cashiers' cheques.— (3) Deficits are marked with a minus sign.— (4) The balance-sheet total is calculated net of interbank accounts with the respective central institutions.— (5) Obtained as the sum of the two totals in note (4).

in 1972); moreover, the changes introduced in the Central Bank's rate system may have curbed the banking system's tendency to refinance with the monetary authorities.

On the asset side, there was a change in the composition of credits: for the system as a whole the percentage of loans dropped, during the five-year period, from 78.0 to 75.4 per cent. This change reflects the phenomenon of large issues of fixed-interest securities by the government and of an increasing long-term indebtedness by the enterprises. With regard to loans, medium- and long-term ones registered a tendency to increase which might be enhanced by the authorization, granted to the commercial and cooperative banks in 1972, to increase the share of their total funds to be used for such longer-term operations.

Other structural changes in intermediation appear if one distinguishes between commercial banks and savings banks and divides them according to size.

With regard to the savings banks, ties with the central institutions seem to have strengthened considerably, as suggested to some extent by the findings of an analysis of interbank relationships. The accounts of the individual savings banks, grouped according to size, reveal that the ratio of credits over deposits was kept unchanged by investing an increasing part of their total funds through the intermediation of their central credit institution. Thus, a sort of integration has taken place within the savings bank group to an extent and in a way which does not seem to have been matched by the commercial banks. The lower degree of competition which takes place among the savings banks, owing to a more rigid territorial division of their operative areas, may have fostered this integration which, on the other hand, in part explains the relative increase in the market share of the savings banks with respect to the commercial banks. Since indirect intermediation through ICCRI (Central Institute of Italian Savings Banks) mainly concerned purchases of securities, the savings banks' group registered a huge increase in the percentage of loans over the total of their credits.

Among the commercial banks, the phenomenon of indirect intermediation grew to a lesser extent, as revealed by the balance and volume of interbank accounts (Table 42). Moreover, intermediation continued to take place, rather than through the central credit institutions, above all through relations among banks of different sizes: in fact, whereas the small and minor banks' deposit-raising capacity grew faster than their capacity for direct investment in loans and securities, so that the percentage of their funds invested on the interbank market rose, the larger banks kept the ratio of credits to deposits more or less unchanged (the *major* banks) or increased it slightly (the *large* banks) and, above all, expanded the securities component of their assets. Overall, the distribution of credit between loans and securities tended to even out among the various bank size-groups.

Another feature which still characterizes operations by the savings banks compared with those by the commercial banks is the former's relatively larger activity in the medium- to long-term maturity sector, both on the lending and borrowing side (medium- and long-term loans, savings deposits); this can be observed from both their assets-liabilities structures and market shares, once one takes into account, for the latter, the fact that about 25 per cent of the banking system's total deposits flow into the savings bank section. This feature became less marked between 1967 and 1972, partly following a general development of the entire banking system, which has experienced a drop in the percentage of savings deposits over total deposits; partly owing to the banks' tendency to expand medium- and long-term loans and purchases of securities to a greater extent than the savings bank system. With regard to the latter, and with reference to the same items, the result was a decrease in the market share of the savings banks which, however, continued to keep the percentage of medium- and long-term loans (72.3 per cent) and of securities not deposited for compulsory reserves (46.5 per cent) fairly high during 1972: for these items the market shares of the savings banks in 1967 were respectively 78.2 and 49.5 per cent.

The last consideration concerns the portion of assets assigned to compulsory reserves (monetary base and securities) as compared with deposits; that of the commercial banks remained steady while, instead, that of the savings banks grew considerably. This is accounted for by the fact that the savings banks were subject to the reserve requirements only in 1958 and then only for the amount of additional deposits; thus, their average reserve ratio, calculated on the basis of stocks, grows in step with deposits.

The securities market

In 1972, the volume of assets traded on the securities market expanded further. Net issues of fixed-interest securities and shares were equal to 10.5 per cent of the gross national product, versus 10.5 in 1971. The average index for bond prices rose, between one December and the next, by about 5 per cent and that for share prices by over 10 per cent.

In the fixed-interest securities section, conditions favouring purchases by the banks and the public permitted the Banca d'Italia to perform a series of interventions on the stock exchanges, aimed at ensuring smooth trading and that certain unfavourable expectations, mainly stemming from domestic and international currency events, did not have a lasting impact on market prices. In fact, price fluctuations — resulting from market forces as they developed throughout the year — were short-lived and of small dimension.

The steady supply of new flotations, favourable conditions for securities yields and the positive development of the real and monetary aggregates which influence the public's demand for bonds, paved the way for the inclusion of large quantities of new issues in the households' and enterprises' portfolios.

The banking system greatly increased its purchases of securities in respect to the previous year, thus bolstering demand for newly issued securities. In 1972, frequent recourse was made to fund raising abroad, through both bond issues and medium- and long-term borrowing of Eurocurrencies. These operations mostly took place during the second half of the year and were generally based on the need to offset the drop in reserves, caused by the export of capital.

In the share section, issuing activity remained buoyant and once again mainly concerned unlisted companies. Risk capital was raised in order to re-equilibrate company finances, to adjust controlling interests in enterprises, to acquire fresh financial resources for new investments and, in some cases, to cover prior operating losses. A good climate for issuing activity was provided by the usual extrapolative expectations in the wake of the marked growth of prices for shares of highly capitalized companies and, in addition to these, by further favourable expectations, based upon objective forecasts of an improvement in the enterprises' nominal yield.

Bonds

Net issues of government securities and of bonds on the domestic market amounted to 5,985 billion (5,034 in 1971); this is equivalent to 8,088 billion in gross issues (7,143 in 1971) (Table 43). Of the latter, 4,648 billion (4,439 in 1971) were placed through bank channels with the institutional investors and the Banca d'Italia and 1,150 (642 in 1971) with the public; the remaining 2,290 billion (2,062 in 1971) concern issues on tap of the special credit institutions.

Issues were spread out more evenly over the year than in the past with the usual peak, albeit lower, in the fourth quarter.

TABLE 43

DOMESTIC AND FOREIGN NET ISSUES OF INDUSTRIAL SECURITIES CLASSIFIED BY CATEGORIES OF INVESTORS, SECURITIES AND ISSUERS

(billions of lire)

Investors / Securities and issuing sectors	Banca d'Italia and UIC	Banks	Public	Total	Foreign sector (1)	Total
			1971			
Fixed-interest securities	*922*	*2,326*	*1,786*	*5,034*	*437*	*5,471*
Treasury (2)	732	1,403	126	2,261	26	2,287
other issuers	190	923	1,660	2,773	411	3,184
Shares	*3*	*3*	*971*	*977*	—	*977*
Total	*925*	*2,329*	*2,757*	*6,011*	*437*	*6,448*
			1972			
Fixed-interest securities	*1,180*	*2,904*	*1,901*	*5,985*	*448*	*6,433*
Treasury (2)	1,172	1,308	180	2,660	- 146	2,514
other issuers	8	1,596	1,721	3,325	594	3,919
Shares	21	*- 13*	*1,233*	*1,241*	—	*1,241*
Total	*1,201*	*2,891*	*3,134*	*7,226*	*448*	*7,674*

(1) Foreign issues include direct financing.— (2) Including bonds on behalf of the Treasury and bonds of the autonomous government agencies and of the local authorities. Excluding ordinary Treasury bills, Central Post Office Savings Fund interest-bearing certificates and short-term Treasury bills.

Flotations and bank financing in foreign currency amounted to 448 billion (437 in 1971), the result of a net Treasury refund of 146 billion and net fund raising by other issuers of 594 billion. The latter operations mostly took place during the second half of the year.

On the domestic market the Treasury issued new securities, directly or through the Credit Consortium for Public Works, for a face value of 3,283 billion. The category in question also includes local authorities' issues (65 billion, versus 37 in 1971). Taking into account redemption of matured securities during the year or of securities drawn by lot and redeemed (481 billion), spreads between face value and placement price (142 billion) and coupons cashed in during the year (787 billion), the Treasury raised fresh funds for a sum of 1,873 billion (1,641 in 1971). These funds are equivalent to 2,660 billion of net issues (2,261 in 1971); that is, about a fifth of the total of the same securities at end-1971 (20.1 per cent as against 21.1 in the previous year). The share of the market covered by the above issuer was much the same as in the previous year. About 40 per cent of Treasury issues, including spreads and redemptions, regarded social interventions mostly for the State Railways, school building, hospitals and financing of local authorities' deficits. An equal portion concerned transfers to productive enterprises and the remaining fifth financed increases in the endowment funds of the public financing organizations. There was a further increase in the Treasury's role of intermediary as compared with its role as final user.

Gross flotations by other issuers amounted to 4,805 billion. Reimbursements during the year came to 1,120 billion; spreads between face value and bid value price equalled 360 billion and coupons paid 1,260 billion. The net amount of funds raised, however, reached 2,065 billion, equivalent to 3,325 of net issues; in 1971 the totals were, respectively, 1,683 and 2,773 billion.

In comparison with the Treasury these fund raisers, through the redemption mechanism and the payment of coupons, exert a slighter relative pressure on the securities market for an equal volume of gross issues. In fact, net funds mobilized by them equalled about 43 per cent at face value of the securities supply versus the Treasury's 57 per cent; coupons cashed in during the year equalled 6.0 per cent of the securities in question at the end of 1971, compared with 5.9 per cent for the Treasury.

Of overall net issues by the sector under study, 822 billion concern ENEL (National Electricity Agency), ENI (National Hydrocarbon Agency) and IRI (Institute for Industrial Reconstruction), 2,446 the special credit institutions and 106 the international institutions; private enterprises, instead, redeemed 50 billion. Compared with 1971, there was a rise in the share of the market occupied by ENEL and the public financing organizations (+ 2.8 percentage points) and the international institutions (+ 1.1). However, it should be noted that the former's weight was still well below that of the 1961-1969 period but clearly on the uprise after the crisis of 1970, whereas the latter only slightly exceeded its past, albeit always quite low, level. With regard to both the special institutions and ENEL and the public financing organizations, net new issues accounted for about a sixth of total securities of the respective sectors at end-1971 (16.6 versus 18.4 in the previous year for the special institutions and 16.3 against 12.5 for ENEL-ENI-IRI).

Net issues amounted to 43.1 per cent of the year's gross real investments. If the comparison is limited to funds raised by the *other issuers* (net of loans to international institutions) and to productive investments alone, the resulting percentage is 44.6.

Issuing activity was accompanied during the year by a large number of new authorizations on the part of the Interministerial Committee for Credit and, within its jurisdiction, of the Banca d'Italia. At end-1972, there remained 3,921 billion in unavailed authorizations and 233 billion in requests under review. Taking into account authorizations given by Parliament, the autonomous government agencies' requirements, the passing of certain bills concerning new issues and expected fund raising by other issuers, it is estimated that the supply of newly issued securities will reach 9,300 billion in 1973. Since 2,150 billion of securities in circulation (either those drawn by lot or falling due) will be redeemed, and given placement spreads of 550 billion, the net demand for funds from the fixed-interest securities market may come to around 6,600 billion. This total would be equal to 8.4 per cent of the gross national product forecast for 1973. During the same period 2,300 billion will be paid against coupons, equal to 34.8 per cent of the forecast net issues.

More specifically, the Treasury would raise 3,000 billion, more than half of which for social interventions, about a quarter for transfers to productive enterprises and the remainder for increasing the public endowment funds; these calculations include 500 billion worth of certificates issued by the Central Post Office Savings Fund to consolidate debts taken out by the local authorities with the banking system. Among the issuers, ENEL and the public financing organizations are expected to take up 1,200 billion and it is estimated that the special institutions require 2,400 billion.

The demand for fixed-interest securities by the public — non-banking intermediaries, households and enterprises — grew from 1,786 to 1,901 billion, while their relative share of the total dropped, also as a result of increased issues, from 35.5 to 31.8 per cent (Table 44). The increase in absolute value can, for the most

TABLE 44

INVESTORS IN FIXED-INTEREST SECURITIES

(percentage breakdown)

Investors	Yearly average 1961-68	1969	1970	1971	1972
Banca d'Italia and UIC	5.9	36.2	41.7	18.3	19.7
Banks	43.8	33.9	30.7	46.2	48.5
Other financial intermediaries (1)	10.5	1.4	2.9	2.5	1.5
Enterprises, households and foreign investors	39.8	28.5	24.7	33.0	30.3
Total	100.0	100.0	100.0	100.0	100.0
Total in billions of lire	1,880	3,351	2,610	5,034	5,985

(1) Over the three years 1962-1964, purchases by the Central Post Office Savings Fund equalled 20 per cent of the total.

part, be linked to the growth in monetary income produced by the economic system; working against this, however, were the average increases in the rate of inflation and in the variability of bond prices. There was less support for demand, compared with the previous year, because of the decrease in immediate returns from securities and in capital gains, even though the latter continued to stay on high levels.

Purchases were spread out unevenly over the year, peaking in the first quarter and bottoming in the fourth; the pattern was the same as in previous years although the second quarter drop was sharper than usual and demand in the first quarter higher. The upswing and following decrease reflect the impact of capital gains which were considerable during the first half of the year, only to turn negative during the second; this fall was accompanied, especially during November and December, by greater price instability and unfavourable expectations arising from uncertainties on the lira's value on foreign markets.

The globally favourable outcome was only achieved because the state of our economico-financial system and its development patterns remained basically unchanged. Should these conditions remain firm during 1973, it can be estimated — on the basis and within the limits of a historical analysis of the determinants, using the regression method — that purchases of securities by the public will drop by about a fifth. The pressure which the growth of the gross national product could exert on them should, in fact, be neutralized by an increase in the average rate of inflation and the probable lack of capital gains which, in contrast, helped the market in 1972. The smaller number of fixed-interest securities in the public's portfolio will, presumably, be offset by heavier purchases of shares and enlarged bank deposits.

The banks' demand for government securities and bonds has been dealt with in the chapter entitled *Banking*. From the standpoint of the securities market, it should be noted that the banks requested permission to sell Eurobonds on the domestic market, for an amount equal to 376 million dollars and were authorized to sell 205. Of these, 147 were placed with the public and the remainder was absorbed into the same banks' portfolios. The amount of Eurobonds issued by international placement consortia in which Italian banks took part, equalled 4.9 billion dollars.

During the current year, if existing trends do not hamper the smooth running of intermediation activity, the banks' demand for securities could register a hefty increase both in absolute terms and as a share of total issues (48.5 per cent in 1972). This forecast, still based on analysis with the regression method, does not consider, however, the effect of the above-mentioned 500 billion consolidation operation of local authorities' debt, since this merely results in shifting the entry from one heading to another under the banks' assets. Apart from this operation, the banks' demand for securities could be affected by downward pressures owing to the lack of capital gains on securities. This factor, however, should be more than offset by the share of new bank deposits which, according to past experience, goes towards bond purchases.

Overall purchases by the Banca d'Italia-UIC equalled 1,180 billion, versus 922 in 1971. The contribution to the primary market was about one-fifth and should remain on that level during 1973, to keep issuing activity as well as trading on the secondary market running smoothly.

During the year under study, 1,380 billion flowed into the monetary authorities' portfolio, as a result of the combined effect of private placement purchases and the redemption of matured paper; moreover, 300 billion worth of securities already in their portfolio were sold and 100 billion worth purchased through interventions on the stock exchanges.

A special econometric survey, based on daily statistics, was made in order to estimate the importance of the variables which influence Banca d'Italia interventions on the stock exchanges, aimed at reducing fluctuations in bond prices. The sample, consisting of 184 observations corresponding to the same number of trading days, covers the period from June 1972 to March 1973.

The results statistically confirm the existence, on a daily basis, of an inverse link between the level of bank reserves — free deposits and/or unused borrowing margin with the Banca d'Italia — and interventions. The link remains, although reduced in size and statistical significance, if the overall volume, or certain components, of monetary base in circulation are taken into consideration. The verification of this link on a systematic basis substantiates direct observation of the behaviour of some banks which, while the policy of rate support is in force, use the stock exchange as an alternative channel to indebtedness with the Banca d'Italia for creating monetary base.

Since the yields level — according to a thesis which is accepted in theory and has been confirmed by previous econometric research — is prevalently set by the volume of monetary base in circulation (in fact directly set, owing to the limited activity of the Italian money market), the results of the survey would seem to bear out the particular stabilizing function of Banca d'Italia interventions insofar as they help to compensate for erratic variations in the volume of bank reserves and in the level of interest rates, which cannot be immediately offset in any other way.

The methodology and result of these studies will be dealt with more fully in another publication by the Bank.

The decline in yields from fixed-interest securities, which began in August 1970, ended in May 1972 (Table 45). Once again, the event itself and the following phase of slow growth were dominated by expectations on the domestic market, reflecting the performance of

TABLE 45

AVERAGE ACTUAL YIELD ON FIXED-INTEREST SECURITIES

Assets	July 1969	July 1970	July 1971	May 1972	March 1973	Changes between July 70 / July 69	Changes between May 72 / July 70	Changes between Mar. 73 / May 72
Government securities	5.66	8.08	7.15	6.48	6.70	*2.42*	*- 1.60*	*0.22*
Consolidated	4.96	5.55	5.58	5.24	5.05	*0.59*	*- 0.31*	*- 0.19*
Redeemable	5.78	8.13	7.38	6.54	6.68	*2.35*	*- 1.59*	*0.14*
Treasury bonds	5.62	8.10	7.09	6.47	6.74	*2.48*	*- 1.63*	*0.27*
Bonds	6.63	9.43	8.15	7.11	7.23	*2.80*	*- 2.32*	*0.12*
On behalf of Treasury	6.72	9.54	8.58	7.22	7.38	*2.82*	*- 2.32*	*0.16*
Industrial credit institutions	6.93	10.19	8.25	7.13	7.38	*3.26*	*- 3.06*	*0.25*
Real estate credit institutions	5.95	7.70	7.43	6.88	6.75	*1.75*	*- 0.82*	*- 0.13*
ENEL-ENI-IRI	6.86	10.17	8.41	7.27	7.49	*3.31*	*- 2.90*	*0.22*
Other companies	7.07	10.85	8.86	7.36	7.67	*3.78*	*- 3.49*	*0.31*

long-term rates on some foreign markets, especially the German one, and of short-term rates on most markets, including the Eurocurrency market.

At the end of May 1972, market prices for fixed-interest securities had, on average, regained about four-fifths of the decrease that took place during the 1969-1970 crisis. The corresponding fall-off in rates showed the usual dissimilarities in relation to the nature of securities, their maturity, the coupon and the various concepts of return (Table 46).

Compared with July 1970, government securities registered a drop of 1.6 percentage points in rates, equal to an average gain of about 10 lire per 100 lire of capital, and stood at 6.5 per cent of actual yield. Bonds registered a 2.3 point rate decrease, equal to 14 lire of average capital gain, and reached 7.1 per cent of actual yield. The most notable drop was registered for bonds issued by private enterprises (— 3.5 percentage point rate fall-off), medium-term industrial credit institutions (— 3.1) and public financing organizations (— 2.9).

A breakdown of securities according to their coupon shows that the yield fell by 4.5 percentage points for five-per-cent securities, by 2.9 for six-per-cent securities and by 1.2 per cent for seven-per-cent ones (Chart 25). Between the two extreme definitions of yield — that is, immediate yield and the return from securities when they reach maturity — the rate of decrease was, on average, 73 hundredths of a point higher in the latter case.

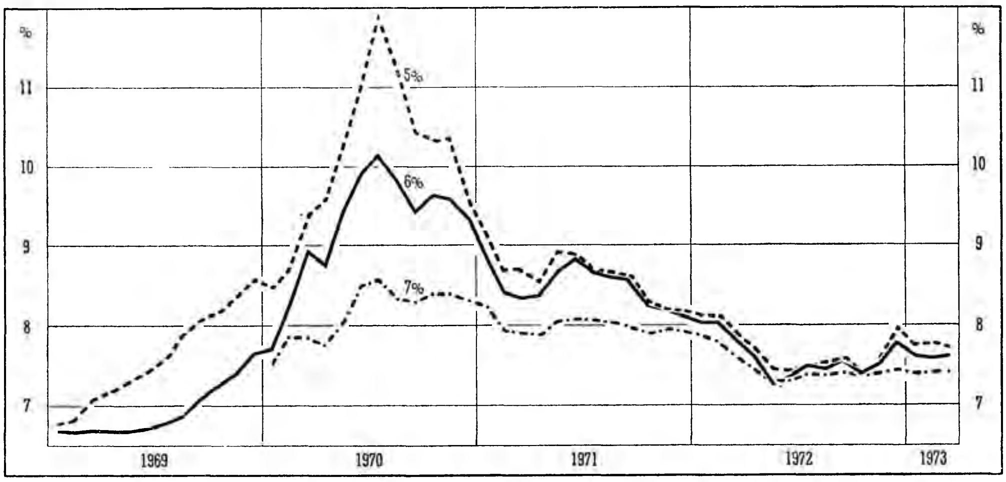
TABLE 46

YIELD ON BONDS CLASSIFIED BY THEIR NOMINAL RATE

Nominal rate / Months	5 %	6 %	7 %	5 %	6 %	7 %	5 %	6 %	7 %
	immediate (1)			*average actual* (2)			*last repayment* (3)		
1969 – Jul.	5.75	6.38	—	7.57	6.74	—	6.59	6.53	—
Dec.	6.00	6.78	—	8.55	7.65	—	7.21	7.16	—
1970 – Jul.	6.83	7.93	7.82	11.94	10.15	8.52	9.13	8.83	8.09
Dec.	6.15	7.51	7.71	9.56	9.35	8.32	7.70	8.28	7.95
1971 – Jul.	5.90	7.20	7.55	8.67	8.66	8.04	7.19	7.85	7.73
Dec.	5.76	6.92	7.48	8.15	8.12	7.93	6.94	7.43	7.63
1972 – May	5.56	6.54	7.16	7.46	7.26	7.29	6.48	6.86	7.18
Dec.	5.63	6.74	7.23	7.96	7.79	7.45	6.75	7.21	7.29
1973 – Mar.	5.58	6.66	7.21	7.71	7.59	7.41	6.71	7.08	7.26

(1) Ratio of coupon to rate or price at issue, taking into account six-monthly payment.— (2) Discount rate to be applied to future yields on the bond, in the event of repayment at average maturity, in order to obtain a present value equal to the rate or price at issue.— (3) Discount rate to be applied to future yields on the bond in the least favourable hypothesis for the investor of repayment at the final maturity date, in order to obtain a present value equal to the rate or price at issue.

CHART 25

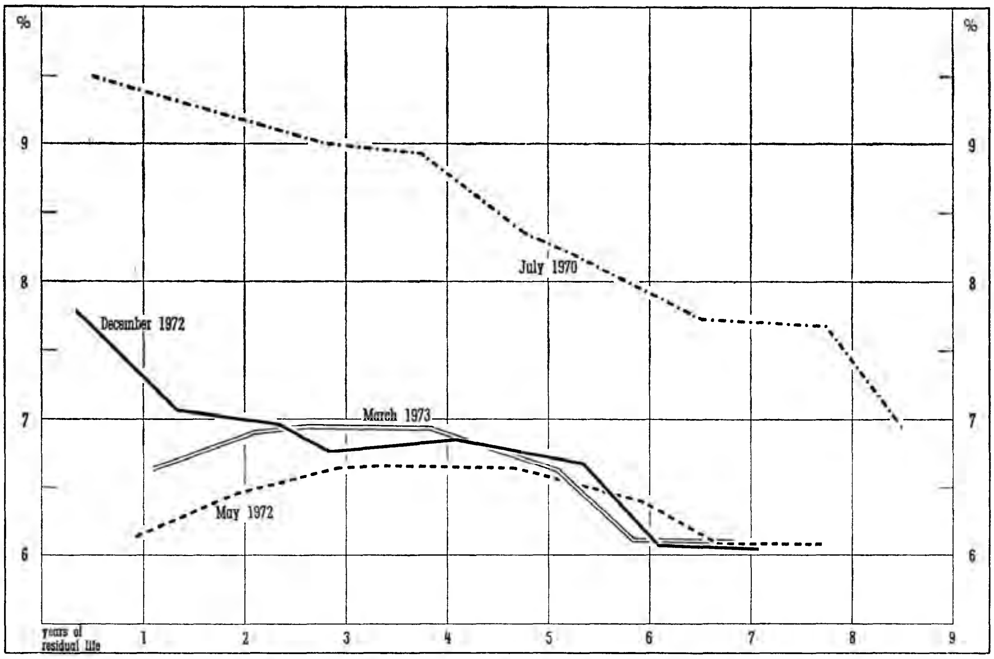


Yields on bonds classified by coupon rate

In May 1972, the term structure of returns was typical of a phase of abundant liquidity, with short-term rates running below long-term ones (Chart 26). This means that the former, originally higher than the latter, described a longer curve, while the whole spectrum of interest rates moved lower, thereby encouraging the possession of long-term securities.

All these observations corroborate what has so far been learnt about the public's preferences; briefly, while interest rates are falling, higher capital gains are to be made on securities with lower coupons and shorter term to maturity. From the standpoint of market behaviour, it follows that, while rates fall there is more trading on the stock exchange in securities with a lower coupon and, therefore, there is less need for the authorities to intervene.

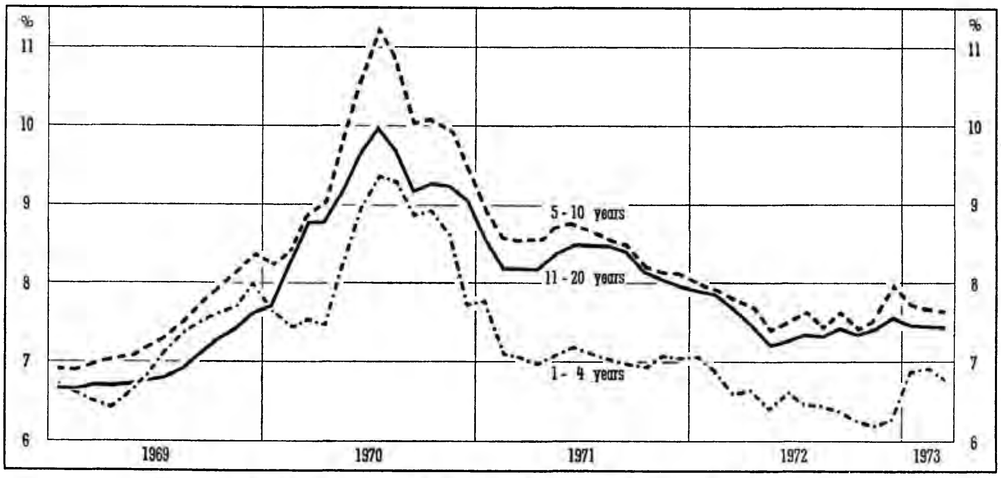
Chart 26



Yields on Treasury bonds classified by maturity

May gave way to a period of uncertainty on future patterns, mostly reflecting growing short-term rates on the foreign and international markets that exerted downward pressures on bond rates, thereby causing portfolio adjustments in direct contrast to those carried out at the beginning of the year. The June currency crisis had an immediate impact on the liquidity of the system and thus on yields, generating a state of latent weakness in prices. Moreover, the government's cautious control of the monetary base, normal in a fixed exchange rate system, was mostly reflected in the shape of the term to maturity-yield curve, typical of periods of relative tensions in the system's liquidity; in fact, for several months short-term rates on Treasury bills stood more than one percentage point above long-term ones. Beginning in November, the range of average actual yields on all other securities also narrowed, drawing short-term rates close to long-term ones; the heaviest growth was registered for yields on securities with a residual life of less than five years (Chart 27).

CHART 27



Yields on bonds classified by years of residual life

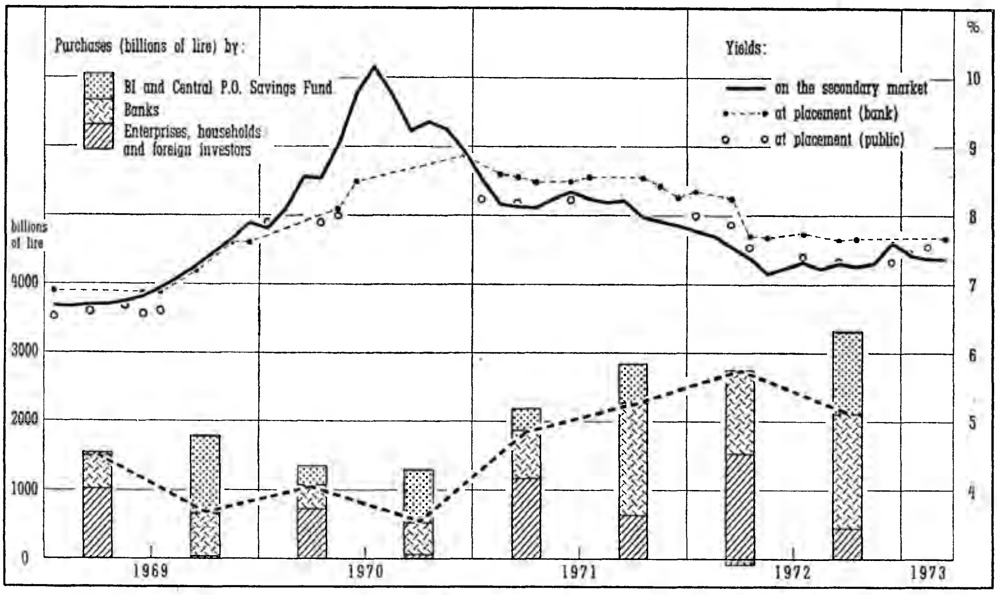
Despite these tensions, auctions of ordinary Treasury bills, at unchanged nominal rates, pushed demand above supply and on many occasions bids topped the auction price. This development, besides being linked with imperfections in our money market, could also mean that the banks correctly saw the above-mentioned rate fluctuation as being temporary and considered foreign to the market the origin of the disequilibria, focused, as was noted, on the foreign currency section.

Between December 1972 and the following January, in addition to the above-mentioned liquidity tensions, there was a heavy demand for shares, the upshot of expectations on potential developments on the foreign currency and the company front.

Cushioning the impact of all these tensions on fixed-interest securities quotes necessitated a greater volume of Banca d'Italia purchase interventions than in the recent past, even though the total of interventions in absolute terms was not especially high (1-2 billion per trading day). Following the decision of end-January to create a section for the financial lira in the foreign exchange market, pressures weakened; nonetheless they picked up steam once again during the February international monetary crisis only to fade in its aftermath.

Once the foregoing disruptions had ceased, securities yields were finally affected by the liquidity level, which remained fairly high compared with the volume of economic activity and proved once again to be the main determinant of our interest-rates structure.

CHART 28



Rates on issue and market yields on fixed-interest securities

As proof that nothing had changed in monetary policy aims, rates on publicly offered newly issued securities, which had moved into line with market levels during the second quarter of 1972, remained firm for the rest of the year and during the first quarter of 1973 (Chart 28). The monetary authorities therefore deemed that the fluctuation of long-term rates in 1972 was out of step with the level of money supply even though, in accordance with the technique of intervention on the secondary market used over the last two years, they allowed the market to express, within certain limits, its reaction to the impact of foreign currency tensions on the market value of securities.

Shares

The placement of new equities and the contribution of funds by shareholders registered a further rise (1,241 billion, as against 977 in 1971). Despite continuing stock exchange crises and unresolved problems within the sphere of joint-stock company activity, the stock market still plays a primary role in investment financing and the smooth running of financial management linked with productive activity. The amount raised equals 8.9 per cent of gross investments carried out over the year under study and 17.2 per cent of the same investments, net of those for social goals (respectively 7.5 and 14.0 in 1971).

Through these issues the companies sought to establish a more balanced ratio of risk capital to debt capital, to restructure ownership participations, mobilize further resources for new investments and, finally, cover accumulated operating losses. Further details of the outcome of some of these aims and an assessment of them, insofar as this is possible from an analysis of company balance sheets, will be given in the chapter analyzing a sample group of enterprises.

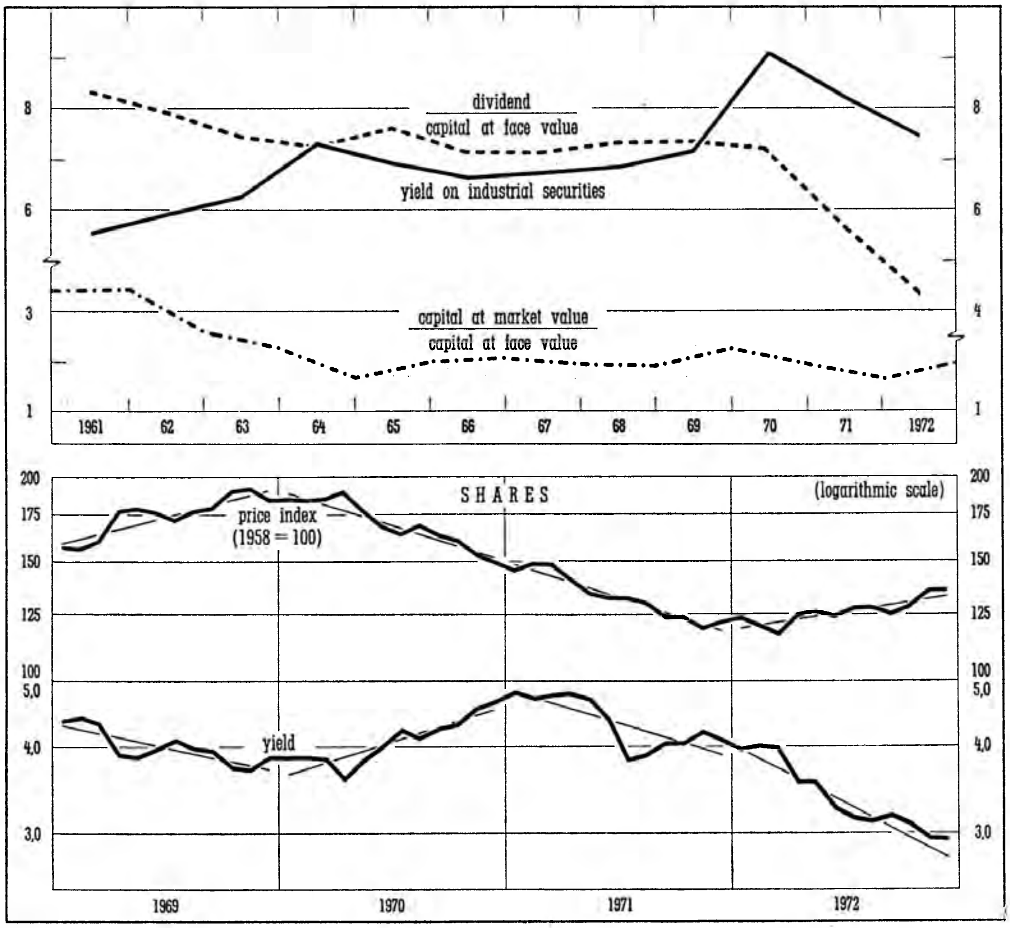
Compared with the total amount of funds raised, issues by listed companies moved up from 8.1 per cent in 1971 to 8.8 in 1972, a modest achievement when one considers that in 1970 the same percentage was 18.9. Nonetheless, these issues mainly concerned the state-controlled enterprises (5.2 per cent, versus nil in 1971), whereas the main private companies mobilized negligible amounts compared with the total and with their importance on the secondary market (1.6 versus 7.3 in 1971). Although what was said last year (on the highly unfavourable conditions for gathering risk capital met by the listed companies) has not been rectified, it is still a fact that the market is quicker to register current or expected improvements in the enterprises' profitability, thereby providing the holders of listed shares, together with a higher fluctuation index, a faster mirror image of the determinants of their portfolio choices.

Improvement in the official section of the stock market was accompanied by a higher average ratio of market value to face value of shares of the companies in that section, estimated at 1.95 compared with 1.63 in 1971 (Chart 29). Moreover, in December 1972 fewer companies — 7.3 per cent if taken at market value (12.3 in 1971) and 24.3 if taken at face value (42.7 in 1971) — registered a market value below nominal. That the market value be at least equal to the face value is, by law, compulsory when carrying out new issues.

The unlisted companies raised nine-tenths of the total. Among them, the state-controlled enterprises reduced by over 10 per cent their share of the primary market, while medium- and small-sized companies increased their share by almost the same amount.

The largest sum was mobilized by the mechanical engineering industry (23.8 per cent compared with 34.5 in 1971); issues by the finance and insurance companies were especially heavy (16.9 per cent versus 12.6 in 1971) as were those of the chemicals companies (15.5 per cent, versus 6.6 in 1971). Companies operating within the textile and clothing, foodstuff and metallurgy industries, the telephone, telegraph and postal services, and the construction industry mobilized, in that order, between 7.9 and 3.1 per cent; with the exception of the construction industry these percentages were higher or equal to those registered the previous year.

CHART 29



Prices and yields on shares and fixed-interest securities

Demand for shares and the activity of mutual investment funds

The yearly survey on share ownership provides information on the economy's revived demand — with the exception of companies involved in directly productive activities — and on the decrease in demand from abroad (Table 47).

TABLE 47

SHARES BY CATEGORIES OF HOLDERS

(end-year amounts; percentage breakdown; total in billions of lire)

Categories of holders	Yearly average 1961-68	1969	1970	1971	1972
Households	*35.5*	*32.9*	*32.2*	*29.9*	*28.7*
Companies	*45.5*	*44.1*	*43.7*	*45.3*	*46.0*
Foreign investors	*16.7*	*20.2*	*21.4*	*22.2*	*22.8*
Banking system	*0.9*	*1.0*	*0.9*	*0.9*	*0.9*
Other financial intermediaries	*1.4*	*1.8*	*1.8*	*1.7*	*1.6*
Total . . .	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
listed	*47.9*	*39.6*	*39.0*	*36.1*	*34.4*
unlisted	*52.1*	*60.4*	*61.0*	*63.9*	*65.6*
Total at market value	17,306	19,472	20,318	17,282	17,446

The growth is particularly heavy in the *non-banking public* category which, after a loss of interest in 1971, returned to the market, attracted presumably by the lively pace of rates and by widespread optimistic expectations on the future of company activity. An expansive impact was probably given by the greater volume of shares offered to the public and by the reduced enthusiasm for purchasing fixed-interest securities, owing to the higher inflation rate and fall-off in expected capital gains.

Enterprises other than joint-stock ones and, above all, the public agencies also expanded their demand for shares, in accordance with a fairly regular development pattern which results in a slight but constant growth in their portion of the total of the companies' face-value portfolio.

The financial houses further increased in absolute value their demand for shares, which was already equal to one-fifth of new issues in 1971, and were one year ahead of the non-banking public in making a similar increase. The upswing of purchases over the last two years has not yet brought them up to the portion of the market covered by these companies before the 1964 stock exchange crisis. This category includes the 11 mutual funds authorized and in fact operating in Italy and whose demand for shares on our market can be quantified for the year at about 32 billion (16 in 1971). These purchases are set against net subscriptions for about 21 billion (33 in 1971). The gap between purchases and increase in assets is, for the most part, counterbalanced by a fall in the funds' liquidity.

Taking into account the way in which these funds are managed and the inadequacy of regulations on the subject, the year's results tend to support the assumption that these dealers sharpen speculative movements thus tending to exacerbate rather than offset some of the defects in our stock exchange. Since foreign experience appears to bear out this opinion, it is of the utmost importance to set up, for the funds operating in Italy and for those which will be started by our intermediaries, a legal framework, particularly concerning taxation, which accentuates their role as institutional investors and limits their speculative tendencies.

At the end of 1972, the net worth of the mutual funds in question had nearly reached 360 billion lire, a growth of 75 billion over the previous year; the heavier increase, in respect to the value of purchases, is obviously due to the upturn of prices for securities already held in their portfolio. Liquidity equalled 7.6 per cent of the amount shown (14.6 in 1971). The net inventory value of *their holdings* grew on average, between one December and the next, by 23.4 per cent (20.1 during the previous year).

The increase is about double that emerging from a sample portfolio of the entire list of shares; in sum, fund management during the year turned out to be particularly favourable to the investor.

Share prices

The average index for shares rose from 122.3 to 136.0; this growth took place almost entirely during the second half of the year (Chart 29). The trend carried over into the first quarter of 1973, at the end of which the share index had hit 147.7, corresponding to a 8.6 per cent increase over last December.

The upswing in prices — which mainly involved shares of companies whose net worth includes a high percentage of real-estate assets — can, for the most part, be seen as stemming from fears surrounding the internal and external stability of the lira and, in addition, from expectations of an increase in the enterprises' real earnings. In sum, this growth was purely anticipatory, in that the return from shares dropped by 1.2 percentage points — if measured by the ratio of dividend to coupon rate net of unaccrued interest of the companies included in the Banca d'Italia sample — and by 1.3 if one considers, for the same sample, the ratio of distributed dividend to the shares' face value.

On the whole, 1972 dividends, based on the firms' performance in 1971, did not offer much to the investor. In absolute value, the total of dividends distributed by the companies in the sample equalled 137 billion, compared with 170 and 235 respectively in 1971 and 1970. Information regarding the current year, although pointing to recovery, tends to exclude any chance of large improvements in profit distribution to shareholders.

Since repeated studies on the longer-term determinants of share prices tend to substantiate the determining role of dividends in setting the companies' market value, it must be held that the above-mentioned growth will be consolidated if increased profits will show up in increased dividends fairly soon. It should be recalled however that, in setting the firms' market value, a certain role is also played by the enterprises' degree of indebtedness — which fell during the year owing to the combined effects of greater profits and a reduced share of distributed profits in the total — and the return on bonds — which dropped on average in 1972 and has still not risen. Thus both these factors have had a positive, though limited, impact on determining a lasting higher average market value for the companies.

The activity of the special credit institutions

Demand for credit from the special institutions fell slightly below that of 1971 but was more representative of actual investment decisions. On the supply side, the system's liquidity conditions opened the way for the regular mobilization of resources and granting of credit to foster investments.

Intermediation activity showed no change from the previous year's level, which had been exceptionally high, partially owing to a rebound from the fall-off registered in the previous two years. Two distinct phases can be noted: a slowdown during the first part of the year followed by a marked upturn during the next six months in which operations at ordinary rates also played an appreciable part. Despite abundant liquidity conditions, the industrial enterprises resorted to ordinary rate operations to a much higher degree than the average for the years immediately prior to 1971. This points to the enterprises' preference for longer-term forms of indebtedness as external financing takes on greater importance in their financial structure. As a result, special credit played a larger role in financing investments, a fact which confirms the institutions' anticyclical behaviour during recent events.

The downslide in demand for credit registered by the special institutions depended on the absence of the random factors which in 1971 had caused it to grow unusually fast, such as the Chemicals Plan, reduced credit facilities provided by the new law for the Mezzogiorno and revival of credit facilities for the building sector.

In contrast to the previous year, when industrial applications particularly regarded the chemicals branch and subsidized operations, in 1972 there was greater sectorial and dimensional diversification, with a certain amount of buoyancy also in ordinary operations, most probably linked with large-scale undertakings. In the building sector, in particular, applications for ordinary loans registered an increase during the second part of the year reflecting a fresh planning spurt in this sector.

In step with the policy stimulating the accomplishment of already planned investments, the number of applications accepted and the amount of credit granted exceeded, in overall terms, 1971's buoyant levels. The increase in loans concerned operations on behalf of the Treasury, for the most part earmarked for the endowment funds of the agencies directing the state-controlled enterprises and for covering expenditure regarding social programmes (Table 48).

An analysis of credit flows according to customer category reflects the progressively smaller investment role played by the private sector. The public sector, besides increasing its direct recourse to the bond

TABLE 48

LENDING BY SPECIAL CREDIT INSTITUTIONS (1)

(billions of lire)

Type of loan	Provided		Repaid		Net increase	
	1971	1972	1971	1972	1971	1972
DOMESTIC	5,154.7	5,119.5	1,833.8	1,973.5	3,320.9	3,146.0
Medium- and long-term	4,883.1	4,838.5	1,578.8	1,701.2	3,304.3	3,137.3
industry and public works	3,594.7	3,550.5	1,176.2	1,226.0	2,418.5	2,324.5
real estate	1,174.2	1,179.3	359.4	426.4	814.8	752.9
agricultural improvement	114.2	108.7	43.2	48.8	71.0	59.9
Short-term credit to agriculture	271.6	281.0	255.0	272.3	16.6	8.7
FOREIGN	164.0	154.4	147.4	208.5	16.6	- 54.1
Financial credits	137.6	101.0	107.1	123.2	30.5	- 22.2
Lending to non-residents	26.4	53.4	40.3	85.3	- 13.9	- 31.9
Total	5,318.7	5,273.9	1,981.2	2,182.0	3,337.5	3,091.9
ON BEHALF OF THE TREASURY	1,447.1	1,988.6	203.0	254.0	1,244.1	1,734.6
TOTAL	6,765.8	7,262.5	2,184.2	2,436.0	4,581.6	4,826.5

(1) Including *other loans* and excluding financing of compulsory stockpiling system operations (Table 53).

market, received in fact a substantial percentage of loans granted by the industrial credit institutions; the greatest beneficiaries were the state-controlled enterprises, in connection with the expansion of investment activity (Table 49). With regard to real-estate credit — where the public are the main beneficiaries — the higher increase in loans to the households than to the enterprises reflects the depressed situation in the dwellings sector.

The fall-off in loans to the private sector (1,788 billion versus 2,344) mainly regarded the large enterprises which, since they are quicker to adjust their own productive and financial structure, had, from 1971 on, expanded their investments and medium- and long-term indebtedness. Given the lack of hindrances to fund gathering and the availability of financial resources for subsidized credit, the remaining enterprises were also able to receive substantial financing. It thus appears that the small- and medium-sized enterprises have also revived to some extent their investment programmes.

The cost of raising funds on the bond market continued to fall: only during the last quarter of the year did it inch up, only to ease

TABLE 49

LENDING BY THE SPECIAL CREDIT INSTITUTIONS
BY CATEGORIES OF CUSTOMERS (1)

(billions of lire)

Categories of customers	1971			1972		
	Industrial	Real-estate & agricultural	Overall	Industrial	Real-estate & agricultural	Overall
	Absolute changes					
PUBLIC SECTOR	924.5	44.9	969.4	1,291.9	60.3	1,352.2
Local authorities	414.9	2.9	417.8	404.1	5.2	409.3
Autonomous government agencies	– 4.6	—	– 4.6	– 3.1	—	– 3.1
Other public bodies	10.2	8.5	18.7	—	12.4	12.4
Public enterprises	504.0	33.5	537.5	890.9	42.7	933.6
state-controlled	458.3	– 0.9	457.4	828.6	25.1	853.7
others	45.7	34.4	80.1	62.3	17.6	79.9
PRIVATE SECTOR	1,494.0	850.2	2,344.2	1,032.6	755.6	1,788.2
Main companies	835.4	45.5	880.9	429.5	31.9	461.4
Other enterprises and households	658.6	804.7	1,463.3	603.1	723.7	1,326.8
households (2)	—	390.0	390.0	—	400.0	400.0
TOTAL	2,418.5	895.1	3,313.6	2,324.5	815.9	3,140.4
	Percentage changes					
PUBLIC SECTOR	*22.2*	*14.7*	*21.7*	*25.4*	*17.2*	*24.9*
Local authorities	*28.8*	*24.2*	*28.7*	*21.8*	*34.9*	*21.9*
Autonomous government agencies	*– 2.4*	. .	*– 2.3*	*– 1.6*	. .	*– 1.6*
Other public bodies	*242.8*	*22.8*	*45.1*	. .	*27.1*	*20.6*
Public enterprises	*20.0*	*13.1*	*19.4*	*29.5*	*14.8*	*28.2*
state-controlled	*19.3*	*– 7.8*	*19.2*	*29.2*	*234.6*	*30.0*
others	*31.3*	*14.1*	*20.6*	*32.5*	*6.3*	*17.0*
PRIVATE SECTOR	*29.0*	*14.0*	*20.9*	*15.5*	*10.9*	*13.2*
Main companies	*35.5*	*29.9*	*35.2*	*13.5*	*16.1*	*13.6*
Other enterprises and households	*23.6*	*13.6*	*16.8*	*17.5*	*10.7*	*13.0*
households (2)	—	*15.4*	*15.4*	—	*13.7*	*13.7*
TOTAL	*26.0*	*14.0*	*21.1*	*19.8*	*11.2*	*16.5*

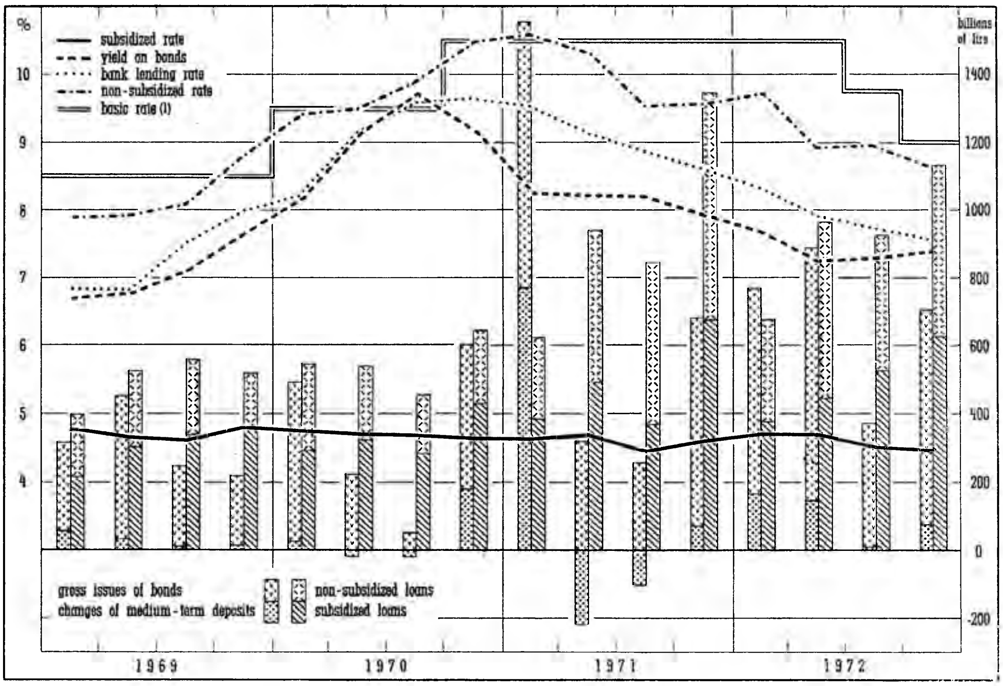
(1) Excluding loans on behalf of the Treasury, foreign lending and financing of compulsory stockpiling system operations.— (2) Estimates.

back down during the following months. The lending rate pattern was less even: an increase during the first quarter, relative to the higher risk factor in the loans being approved, was followed by a marked drop in the following quarters; on average rates were about one percentage point below those of the previous year (Chart 30).

The drop coincided with a further increase in ordinary loans; this would confirm the enterprises' preference for expanding their medium- and long-term indebtedness when the spread between the cost of this instrument and that of bank credit is narrowed.

Once again, in 1972 there was a large flow of subsidized credit at an average cost substantially similar to that of the year before; for industrial credit operations this rate equalled, on average, 4.56 per cent, while the average rates for subsidized and ordinary operations stood at 6.64 per cent.

CHART 30



Loans, main forms of supply and average rates of the industrial special credit institutions

(1) In effect for subsidized operations in favour of medium- and small-sized industries and the Mezzogiorno.

The expansion of subsidized credit, apart from affecting the siting of investments, also influenced the size structure of our industrial system, opening up funds for the smaller-sized enterprises and thus fostering their expansion. This also resulted from the fact that some special institutions are only permitted to grant loans to the medium- and small-sized enterprises. However, the mere fact that an enterprise comes under this heading does not make it automatically eligible for credit, since the undertaking is also judged on the grounds of whether it satisfies certain technico-economic criteria, which form the basis for measuring the risk involved and how rationally the funds are to be invested.

The resources set aside by the new law for the Mezzogiorno opened the way for the revival of interest-reducing subsidies and capital grants. In fact the increase in outlays for financial incentives in 1972 mainly regards the relative costs of industrializing the Mezzogiorno, determined by the large volume of investments negotiated within the framework of national planning programmes (Table 50).

TABLE 50

COST TO THE GOVERNMENT OF INTEREST-REDUCING SUBSIDIES AND CAPITAL GRANTS (1)

(billions of lire)

Sector and object	Fiscal years				
	Average		1970	1971	1972
	1950-59	1960-69			
INTEREST-REDUCING SUBSIDIES	3.6	94.8	311.5	280.2	356.5
INDUSTRY, COMMERCE AND ARTISANS	0.8	59.6	231.3	185.4	242.7
medium- and small-sized industries	—	14.2	33.4	47.5	57.5
industrialization of the Mezzogiorno	0.2	19.9	136.3	56.5	110.8
export credits	0.3	6.2	22.4	28.9	23.9
natural disasters	—	8.7	7.0	13.2	13.0
other	0.3	10.6	32.2	39.3	37.5
BUILDING	1.1	5.4	13.8	23.8	46.3
AGRICULTURE	1.7	29.8	66.4	71.0	67.5
improvement credit	1.5	16.3	40.9	48.5	48.8
credit for working capital	0.1	6.7	10.0	12.0	—
natural disasters	0.1	6.8	15.5	10.5	18.7
CAPITAL GRANTS FOR INDUSTRIES IN THE MEZZOGIORNO	0.1	22.4	81.3	32.5	77.2
TOTAL	3.7	117.2	392.8	312.7	433.7

(1) Relates to amounts appropriated for the fiscal year; only in respect of the part charged against the *Cassa per il Mezzogiorno* do the figures refer to actual disbursements during the year. Contributions paid according to provisions regarding the Regions are not included.

In addition to the increase in funds raised by the special credit institutions to satisfy the economy's credit requirements, there was an upswing in fund mobilization by Crediop (Credit Consortium for Public Works) on behalf of the Treasury and, as already mentioned, a rise in indebtedness abroad, encouraged by the monetary authorities in order to neutralize the impact of capital outflows (Table 51).

Monetary policy fostered bond placement and reduced its relative costs, with positive repercussions on the volume of subsidized credit dependent on government allocations. Despite tensions felt in the last months of the year, the average yield on industrial bonds registered a drop of about three-quarters of a point compared with 1971. The industrial and agricultural credit institutions were able to take advantage of the favourable market conditions. The real-estate credit institutions, on the other hand, registered a slowdown, owing to the uncertain progress of building activity.

TABLE 51

FUND-RAISING SOURCES OF THE SPECIAL CREDIT INSTITUTIONS

(changes in billions of lire)

Types of liabilities / Sectors of origin	Credit institutions: industrial 1971	industrial 1972	real-estate 1971	real-estate 1972	agricultural 1971	agricultural 1972	Total 1971	Total 1972
TYPES OF LIABILITIES								
Bonds (1)	1,571.6	1,913.9	940.8	790.5	7.6	69.2	2,520.0	2,773.6
Deposits and interest-bearing certificates	521.4	399.7	—	—	—	—	521.4	399.7
Rediscounting	—	—	—	—	17.3	16.4	17.3	16.4
Current accounts and advances with the banks	71.9	- 3.0	- 48.8	- 31.1	97.7	- 22.3	120.8	- 56.4
Mediocredito funds	188.9	70.9	—	—	—	—	188.9	70.9
Foreign loans	196.1	417.3	—	—	—	—	196.1	417.3
Capital and reserves	113.1	102.9	37.5	67.0	4.2	8.8	154.8	178.7
Others	51.0	80.4	14.5	18.4	32.6	25.4	98.1	124.2
Total . . .	2,714.0	2,982.1	944.0	844.8	159.4	97.5	3,817.4	3,924.4
SECTORS OF ORIGIN								
Public and companies	1,524.3	1,470.8	736.7	427.3	- 0.8	58.6	2,260.2	1,956.7
Banca d'Italia and UIC	- 0.9	- 2.0	5.5	10.2	18.4	16.3	23.0	24.5
Banks	714.6	817.3	94.1	298.8	100.9	- 3.2	909.6	1,112.9
Other credit institutions (2)	94.6	126.9	78.1	52.8	9.5	2.7	182.2	182.4
Public sector (3)	172.9	148.0	29.6	55.7	31.4	23.1	233.9	226.8
Foreign sector	208.5	421.1	—	—	—	—	208.5	421.1
Total . . .	2,714.0	2,982.1	944.0	844.8	159.4	97.5	3,817.4	3,924.4
Bonds on behalf of the Treasury	1,275.0	1,766.2	—	—	—	—	1,275.0	1,766.2
Total . . .	3,989.0	4,748.3	944.0	844.8	159.4	97.5	5,092.4	5,690.6

(1) Excluding bonds of the Mediocredito centrale (medium-term credit institution), the value of those in circulation having increased by 58 billion in 1971 whereas it dropped by 3 billion in 1972.— (2) Special credit institutions and insurance institutions.— (3) Treasury, Regions, Cassa per il Mezzogiorno (own funds), Central Post Office Savings Fund and national insurance institutions.

Fund raising on the capital market was more buoyant during the first half of the year than the second; respectively 1,871 billion through bonds and medium-term deposits versus 1,303. During the second half there was a marked drop in medium-term deposits, which are especially sensitive to market conditions and to rates being paid on alternative forms of lending, notably bank deposits. The foregoing decline may also be linked to the fact that the interbank agreement on medium-term borrowing rates was not renewed when it lapsed in April which, judging by the banks' large issues of interest-bearing certificates, strengthened their competitive position.

Once again in 1972, albeit to a smaller degree than in 1971, it was the public who provided the greatest percentage of resources. Their contribution however flagged during the later months, thus there was need for stepped up purchases by the banks which, on the overall level, provided 28.4 per cent of the institutions' ordinary resources.

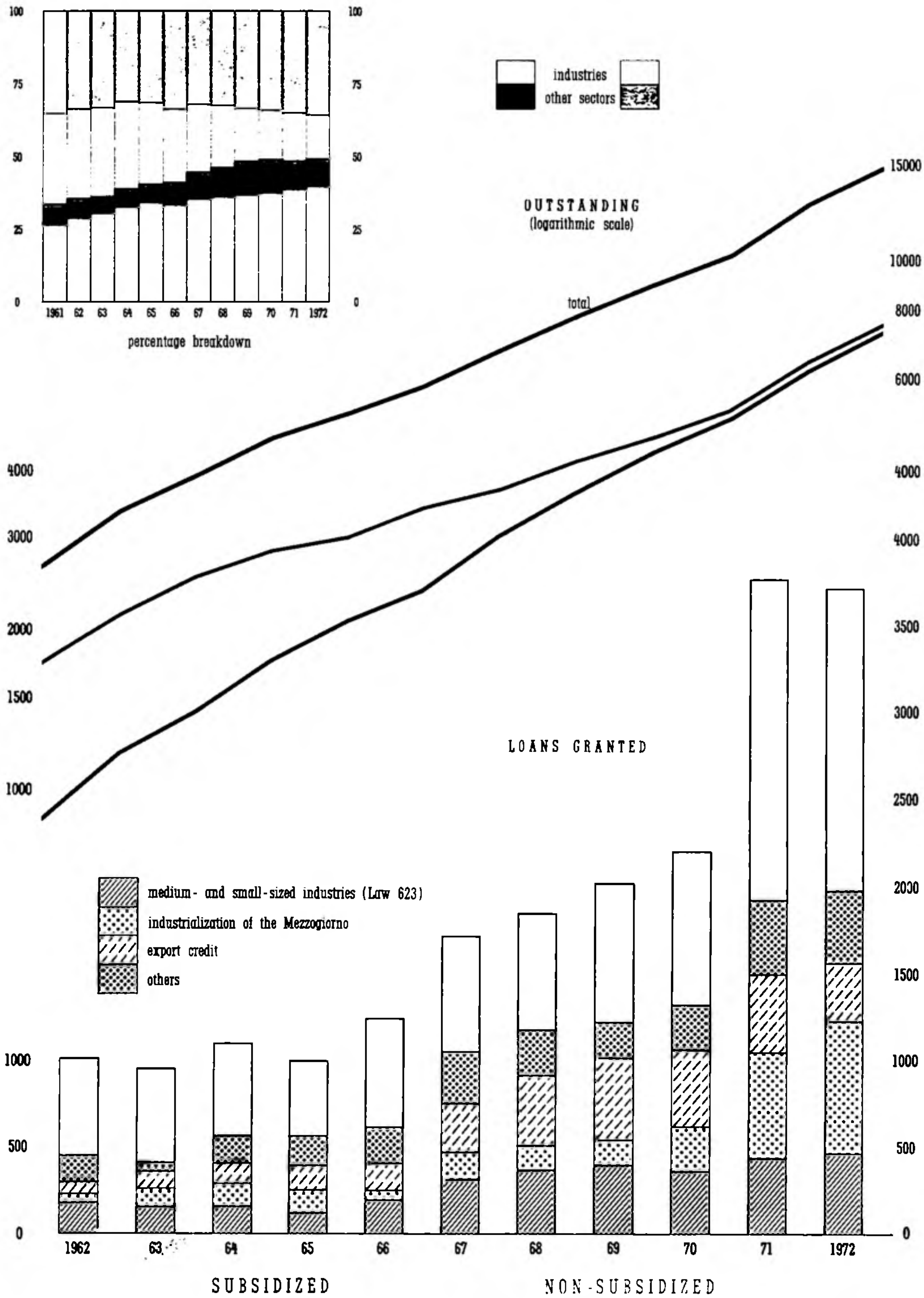
The industrial credit institutions

Turning to a more detailed study of the activity of the various sections, industrial credit resources were mainly channelled towards financing domestic productive activities; with regard to foreign loans, repayments exceeded outlays.

Domestic loans, while maintaining fairly high levels, registered a lower growth rate than in the previous year (19.8 versus 26.0 per cent). The absence of hurdles to fund gathering fostered the contracting of loans at ordinary rates, mainly directed towards the services (especially the telephone sector) and public works. The industrial sector also took out a higher amount of loans at ordinary rates than the average for the five years prior to 1971; the majority of these loans went to the more industrialized regions (Piedmont, Lombardy, Liguria). With regard to subsidized credit — the expansion of which was enhanced by the considerable availability of funds set aside by the government, in line with a pattern which was first observed after Law n. 717 of 1965 came into force — operations for industrializing the Mezzogiorno registered an upswing (Chart 31). These, along with export credits, have, over the last years, been the main factors under-

MEDIUM-TERM INDUSTRIAL CREDIT INSTITUTIONS' FINANCING

(billions of lire)



lying the expansion of the area of subsidized credit. Subsidized credit has expanded in fact, from 49 per cent of all loans granted between 1961 and 1966 to 58 per cent during the period 1967-1972 (for the same years operations relating to laws for the Mezzogiorno rose from 18 to 24 per cent).

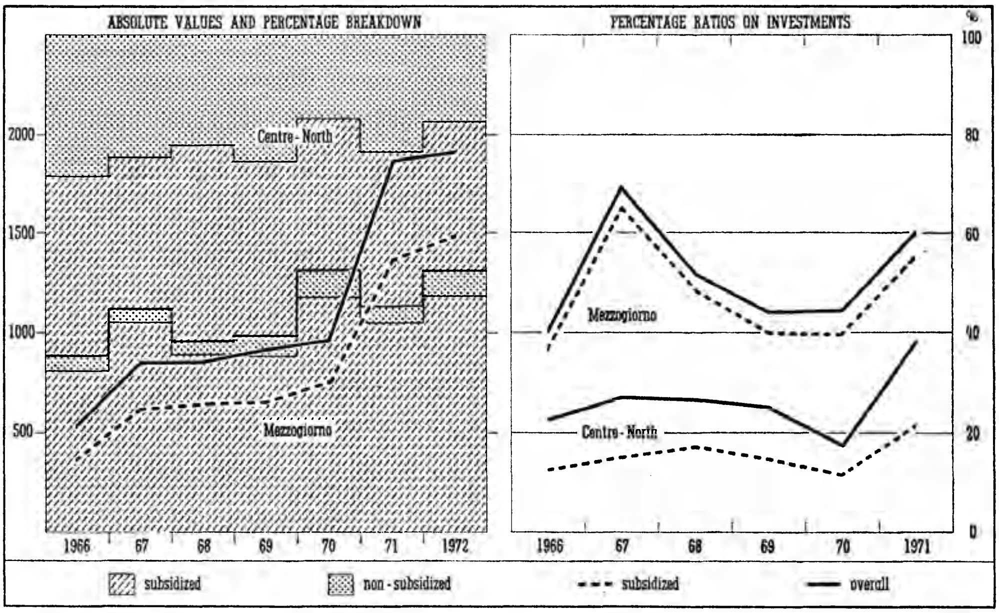
The industrial sector received, net of export credits, 1,915 billion worth of loans (1,873 in 1971 and an average of 817 billion over the period 1966-1970), 77 per cent of which at special terms. More than two-fifths of the sector's net indebtedness concerned the metallurgy industry; there was some expansion not only in the paper and printing section but also in textiles, most likely owing to financial requirements connected with the process of reorganizing the sector.

Playing an appreciable role in the expansion of medium- and long-term credit in 1971 were moves made by the enterprises funding short-term loans contracted in the period the special institutions were having difficulties mobilizing resources. In 1972, in the absence of such phenomena, investment expenditure was presumably more highly covered by medium- and long-term financing, justifiable by the drop in the enterprises' internal savings, which has been a feature of recent years. During the period 1966-1972, special loans to industries, net of export credit, accounted for 36 per cent of investments carried out in the sector; this percentage, which had held fairly steady over the first years of the period, struck bottom in 1970, as investments rose and loans stagnated. In 1971, the percentage hit its peak (45 per cent), hovering around the same level in 1972. These ratios, although not taking into account time lags, give an idea of the role played by the special institutions' credit in financing investment. As regards the main branches of industry, greater use was made of this form of coverage in chemicals and metallurgy and less in mechanical engineering; thus it would appear that the large enterprises, and especially the more capital-intensive ones, are more dependent on indebtedness.

The part played by special credit in net changes in the industrial sector's external financing rose from 19 per cent over the period 1961-1966 to 24 per cent between 1967 and 1972 (from 13 to 20 per cent when only counting subsidized credit).

Mezzogiorno-sited manufacturers received 52.5 per cent of all special institution financing earmarked for the industrial sector. Over nine-tenths of this was granted in the form of soft loans. The expansion of credit flows to the Mezzogiorno's manufacturing enterprises is due to, apart from heavier investment activity in these regions especially from 1969 on, increased financial coverage through indebtedness and, in particular, through subsidized operations. During the period 1966-1971 (when data on the territorial distribution of real aggregates became available), loans on average amounted to 52 per cent of investments, versus 34 per cent for the entire country. Manufacturers in these regions on average received 44 per cent of overall outlays versus the average of 28 per cent of the national total for industrial investments (Chart 32).

CHART 32



Loans to the industrial sector by geographical area and category of operations
(absolute values in billions of lire)

Despite the fact that soft credit has been extensively granted, the principle of using it to solve regional disequilibria seems to have been established. This has been bolstered moreover by the minimal quotas in favour of the southern regions set for public financing and expenditure by the new law for the Mezzogiorno and by more recent measures regarding subsidies.

In the export credit sector the revival of demand for credit can be linked with the unsteady performance of domestic demand, which spurred businessmen to seek out new orders from abroad. The revival involved both loans to domestic exporters and to foreign countries. The greatest boost came from the latter which, since they are granted against inter-governmental agreements, concern huge export operations. The expansion of loan applications was facilitated by an increase, from 500 to 750 billion, in the ceiling placed on guarantees; taking into account carryovers, the 1972 ceiling rose to about 850 billion.

The ample granting of financial guarantees, against a fluid financial backdrop, spurred the institutions to accept a large volume of applications (1,258 billion versus 767 in 1971). Another plus factor was the introduction of a scheme for automatically adjusting the rate on these operations, which eliminated the problem that arises when changes in the cost of fund raising take place between the commitment and the actual allocation of funds. The new system does not, therefore, require administrative measures to adjust basic rates and, in moments when the cost of fund mobilization is on the uprise, offsets the institutions' reluctance to undertake financing commitments.

Outlays of export credit, instead, registered a net fall-off which, since financial difficulties were non-existent, seems to reflect the limitations placed on financial guarantees in 1970. These had been introduced with the intention of shifting resources towards the financing of domestic investments. In fact, there is a long lag before changes in the ceiling on financial guarantees show up in outlays. In 1972 the latter covered 3.2 per cent of overall exports, compared with an average of 5.5 per cent over the period 1968-1971 (10.5 versus 19.3 per cent, if one considers only capital goods). Over a third of the outlays themselves were refinanced by the Mediocredito centrale (medium-term credit institution); this was only possible because of increases made in its endowment fund over the last years.

Owing to the substantial amount flowing back in the form of repayments, outlays exerted no pressure whatsoever on the capital market. The effect on capital movements, even taking into account loan consolidation carried out through the UIC, was also negligible and far below that of recent years (60 billion versus an average of 250 for the three years 1969-1971).

A survey of both financial guarantees granted and loan commitments outstanding — the latter equalling over 1,300 at end-1972 — reveals the likelihood of an expansion of outlays over the short run which could be speeded up should measures to guarantee exchange risks be applied. Given the increase in repayments, this probable expansion would only in part be translated into an increase in net resources transferred abroad; in any case it can still be regulated, although there will be time lags, through the yearly ceilings for guarantees — set at 700 billion for 1973 — and in addition is constrained by the link between financial guarantee commitments and the availability of funds for reducing interest rates.

The real-estate credit institutions

The still unsatisfactory performance of investments for dwellings conditioned the activity of the real-estate credit institutions. The latter were not able to take full advantage of the buoyant demand for mortgage bonds owing to the strict link between issues of these and outlays which, in turn, depend on work progress and fixed coverage ceilings.

The institutions issued mortgage bonds for about 100 billion less than in the previous year (Table 52). However it should be noted that,

TABLE 52

ACTIVITY OF THE REAL ESTATE CREDIT INSTITUTIONS

Period	Credit provided: Total	Credit provided: Subsidized (1)	Gross bond issues	Bonds issued / Credit provided	Net purchase of bonds: by banks	Net purchase of bonds: by public
	(billions of lire)			*(percentage values)*		
1968	875.7	47.2	734.3	83.9	54.1	39.2
1969	944.7	34.5	771.1	81.6	48.4	40.9
1970	1,028.5	45.1	1,033.7	100.5	20.3	73.4
1971	1,174.2	48.8	1,243.6	105.9	14.7	78.3
1972	1,179.3	50.1	1,147.7	97.3	37.9	54.1
1971 – 1st qtr.	250.9	8.6	299.4	119.3	– 58.2	152.5
2nd »	236.1	13.5	236.9	100.3	8.1	83.1
3rd »	282.2	5.8	248.1	87.9	68.1	20.8
4th »	405.0	20.9	459.2	113.4	46.3	49.0
1972 – 1st qtr.	264.4	20.1	244.6	92.5	14.6	81.6
2nd »	255.8	13.6	257.1	100.5	– 8.6	101.0
3rd »	273.8	2.7	239.9	87.6	51.0	35.0
4th »	385.3	13.7	406.1	105.4	75.4	16.9

(1) According to law n. 1179 of Nov. 1, 1965.

towards the end of 1971, they mobilized funds in advance to cover loan commitments, encouraged both by favourable placement conditions and by the fact that the government's offer of a refund premium would soon lapse. Thus, despite the fall-off in issues, they were able to keep the outlays at the same level as in 1971 and to continue to reduce their short-term indebtedness with the banks.

Purchases of mortgage bonds by the public rose from an average of 40 per cent of net issues over the two years 1968-1969 to one of 69 per cent for the following three years. The public's propensity to purchase mortgage bonds was favourably affected by the gradual narrowing of the spread between their return and that on other fixed-interest securities and by an increase in the immediate yield, which resulted from an upturn in the nominal rate set at the beginning of 1970. In fact, this increase affects investors, not only because there is a rise in the *sure portion* of the yield, but also because it tends to curb ups and downs in mortgage bond prices which follow in the wake of market fluctuations. In 1972 fewer securities of this type were included in the banks' compulsory reserves (130 versus 190 billion in 1971) than would have been possible according to the performance of savings deposits.

Loans granted by the special institutions for dwellings accounted for 31 per cent of financing for housing projects (32 per cent in 1971), whereas the banks' contribution was larger (13 versus 9 per cent) and can be linked with a revival in the number of building starts. The percentage for public investments and social security and insurance institutions remained more or less unchanged; savings directly invested by the public, after the 1969-1970 expansion, registered another fall-off in relative terms — owing to the dearth of available housing and the lower economic viability of investments — as prices soared and tax burdens increased.

Subsidized loans amounted to 50 billion; of this sum only 100 million concerned outlays spurred by the June 1971 measures for reviving credit subsidies. Another 250 billion worth of loan applications have now reached the final stages before approval, 150 of which based on the subsidized credit measure passed in 1965.

The agricultural credit system

Direct financing to the agricultural sector registered a slump both in the short-term and in the longer-term credit sections (Table 53).

The fall-off in working credit — which mainly involved loans for operational expenses and the authorized institutions, which are most active in this sector — seems to indicate that the farms are making less use of this credit, in connection with the positive trend of prices on output. However, one cannot exclude the possibility that this is in some way linked with the transfer to the Regions of administrative functions regarding eligibility for agricultural credit and, in general,

TABLE 53

LENDING BY THE AGRICULTURAL CREDIT SYSTEM

(billions of lire)

Items	Special institutions		Other institutions		Total	
	1971	1972	1971	1972	1971	1972
AMOUNTS OUTSTANDING	1,136.6	1,207.2	743.1	782.4	1,879.7	1,989.6
Working credit	370.3	381.0	488.5	508.3	858.8	889.3
Improvement credit	766.3	826.2	254.6	274.1	1,020.9	1,100.3
LOANS	385.8	389.7	588.3	575.5	974.1	965.2
Working credit	271.6	281.0	536.6	519.5	808.2	800.5
operational expenses	*132.4*	*139.5*	*316.9*	*277.9*	*449.3*	*417.4*
purchase of equipment	*62.2*	*73.3*	*86.1*	*104.8*	*148.3*	*178.1*
other purposes	*77.0*	*68.2*	*133.6*	*136.8*	*210.6*	*205.0*
Improvement credit	114.2	108.7	51.7	56.0	165.9	164.7
cultivable land	*23.2*	*26.9*	*11.9*	*12.4*	*35.1*	*39.3*
farm buildings	*45.8*	*41.7*	*20.6*	*23.6*	*66.4*	*65.3*
other purposes	*45.2*	*40.1*	*19.2*	*20.0*	*64.4*	*60.1*
REPAYMENTS	295.4	319.0	512.2	536.3	807.6	855.3
Working credit	252.2	270.2	492.8	499.8	745.0	770.0
Improvement credit	43.2	48.8	19.4	36.5	62.6	85.3
NET INCREASES (*)	90.4	70.7	76.1	39.2	166.5	109.9
Working credit	19.4	10.8	43.8	19.7	63.2	30.5
Improvement credit	71.0	59.9	32.3	19.5	103.3	79.4
(*) Financing of stockpiling system operations	16.7	6.6	43.7	31.1	60.4	37.7
compulsory	*24.0*	*12.2*	*39.2*	*26.3*	*63.2*	*38.5*
voluntary	*– 7.3*	*– 5.6*	*4.5*	*4.8*	*– 2.8*	*– 0.8*
Other loans	– 2.7	– 2.1	—	—	– 2.7	– 2.1

agricultural intervention. An upswing, on the other hand, was registered in loans for mechanizing productive activity which continued to depend on the national revolving fund.

With regard to long-term credit, only loans for acquiring cultivable land registered a slight increase in the wake of an upturn during the last part of the year; the fall-off in loans for land reclamation reflects the slow progress of farm reorganization which was hindered by the tapering off of interventions under the second Green Plan.

Operations for financing compulsory stockpiling — which increased in value as a result of accumulated tax and interest rate burdens for lack of measures regulating past operations — registered a slighter increase, mainly owing to a drop in the cost of rediscounting paper at the Central Bank.

In 1972, there was some variation in the financial structure of the special agricultural credit institutions, as the result of fresh bond issues adding over 50 per cent to the value of those in circulation. The proceeds paved the way for a reduction of short-term indebtedness with the participating banks; the result was less imbalance between the maturity due-dates on loans and on the resources covering them. Autonomous fund-raising sources (*bonds* and *capital and reserves*) still account for a slim portion of the total of ordinary resources, excluding those for financing compulsory stockpiling (18.6 per cent at end-1972, versus 14.1 per cent at end-1971).

Owing to the development of the mechanization process, of action aimed at increasing the size of production units and fostering the changeover to forms of direct farm management, as well as the parallel fall-off in self-financing, the financial requirements of agriculture, like those of the other sectors, grew over the last decade, thereby necessitating ever greater direct or indirect public intervention (interest-reducing subsidies and advances to the institutes). Loans granted with public funds represented at end-1972 45.5 per cent of the total, compared with 36.4 at end-1961 (905 versus 218 billion).

The financing of the Economy

In 1972, overall financing to domestic sectors, which are the final users of resources, equalled 17,600 billion. If we deduct funds supplied to the Economy by the public sector, either directly by investing in the equity capital of public enterprises or by granting credit, or indirectly through the credit institutions, we come up with a final figure of 16,430 billion, or 30.8 per cent more than in 1971, when the increase equalled 29.6 per cent.

The distribution of financing between the Economy (comprising the Households and Enterprises sectors) and the public sector, after the far-reaching shifts that took place in favour of the latter during 1971, showed little change during the year under study (42.9 per cent to the public sector and 57.1 to the Economy) (Table 54).

TABLE 54

LENDING TO DOMESTIC FINAL-USER SECTORS

(billions of lire)

Items	Flows			Percentage breakdown		
	Average 1966-1970	1971	1972	Average 1966-1970	1971	1972
TOTAL LENDING TO:						
Economy	4,960	7,971	10,041	*63.4*	*55.6*	*57.1*
enterprises: private	*3,501*	*5,220*	*6,110*	*44.7*	*36.4*	*34.7*
public (1)	*992*	*2,172*	*2,880*	*12.7*	*15.1*	*16.4*
households	*467*	*579*	*1,051*	*6.0*	*4.1*	*6.0*
Public sector (consolidated) (2)	2,865	6,378	7,555	*36.6*	*44.4*	*42.9*
Total	7,825	14,349	17,596	*100.0*	*100.0*	*100.0*
SOURCES OF LENDING						
Banking system	4,067	7,385	10,085	*52.0*	*51.5*	*57.3*
Other credit institutions	1,621	3,233	3,131	*20.7*	*22.5*	*17.8*
Public sector (consolidated)	352	751	725	*4.5*	*5.2*	*4.1*
Economy (3)	1,414	2,291	3,075	*18.1*	*16.0*	*17.5*
Foreign sector	371	689	580	*4.7*	*4.8*	*3.3*

(1) See Table 62.— (2) If the funds supplied directly and indirectly to the Economy by the public sector are excluded, lending to that sector falls to 4,592 and 6,387 billion respectively in 1971 and 1972 and total credit is reduced to 12,563 and 16,428 billion in the two years; with regard to the period 1966-1970 the public sector's average borrowing falls to 2,200 billion and overall average credit drops to 7,160 billion.— (3) Including unclassifiable miscellaneous items.

The buoyant demand for financial assets on the part of households and enterprises made available the resources necessary to cover, both directly through the purchases of securities and indirectly through the banking system, the financing requirements of the public sector and the enterprises; while the current account surplus in the balance of payments absorbed the remainder (Table 55).

Whereas in the intermediate term the portion of total financing which the Economy received from the special credit institutions continued to rise in the wake of expanded subsidized credit and because of the tax treatment that makes direct financing through securities hardly advantageous for both the enterprises as seekers and the households and same enterprises as suppliers, in 1972 this portion dropped below the average for recent years (26.4 per cent compared with 28.9 over the period 1964-1971). This behaviour reflects the flagging growth rate of investments in home purchases and in industry. In contrast, the banking system's contribution to the Economy's total financing climbed back upward (50.8 per cent of the total), mainly in connection with stock building and the revival of financial asset purchases. The Economy itself contributed to its financing to a larger extent (10.3 per cent, against 8.2 over the period 1964-1971), following the marked upswing in its securities issues.

Loans by the banking system continued to cover the largest portion of financing to the public sector, in 1972 their portion (66.1 per cent) was above the medium-term average. The share directly provided by the Economy and, more specifically, by the households, through securities purchases and the accumulation of their Post Office deposits and in the form of actuarial reserves with the social insurance institutions, inched up (26.5 per cent of the total), while the special credit institutions' share showed an opposite pattern.

During the year under study, the behaviour of the financial balances of the sectors which are final users of resources, expressed as a ratio of the gross national product, reflected the slower growth rate of investment in respect to the Economy's saving flows, the public sector's expansionary role and the persistent surplus in the balance of payments on current account.

More specifically, the appreciable rise in the Economy's financial surplus, which increased from 6 per cent of the GNP between 1964 and 1970 to 7.8 and 10.7 per cent in the last two years, indicates that the sector did not impart an expansive impetus to economic activity. The enterprises' financial deficit was lower than in the previous year (3,390 billion, against 3,950), owing to the recovery of firms' profits and the unsatisfactory performance of investments in plants and equipment. The development of the households' assets and liabilities led

NATIONAL FINANCIAL

(changes in billions of lire;

Sectors / Classes of assets and *liabilities*	1971 Households	Enterprises	Credit institutions: BI-UIC	Credit institutions: Banks	Credit institutions: Special credit institutions	Insurance companies	Public sector: Central authorities	Public sector: Local authorities	Public sector: Social Insurance Funds	Public sector: Autonomous government agencies	Foreign Sector	Unclassified and discrepancies
A) Gold	—	—	- **1.8**	—	—	—	—	—	—	—	- *1.8*	—
a) Notes and coins	**590.2**	**65.0**	**2.0**	**3.8**	**7.1**	**0.8**	**2.4**	—	**1.3**	**2.6**	—	—
» » »	—	—	*662.1*	—	—	—	*15.1*	—	—	—	- *2.0*	—
b) Demand deposits	**2,150.0**	**2,310.1**	**3.6**	**895.3**	**30.8**	**58.8**	**11.2**	**391.2**	**289.0**	- **34.2**	**36.6**	- **68.9**
» »	—	—	*469.8*	*5,752.3*	*29.1*	—	*53.2*	—	—	-*114.0*	-*114.7*	- *2.2*
1) Bank deposits	2,150.0	2,223.3	—	*5,109.8*	—	58.8	9.5	391.0	278.2	- 1.0	—	—
2) Coupon collection float	—	—	—	- 62.0	—	—	—	—	—	—	—	- *62.0*
3) Cashiers' cheques outstanding	—	—	—	*25.6*	—	—	—	—	—	16.9	—	8.7
4) P. O. deposits	—	59.4	—	2.3	—	—	*61.7*	—	—	—	—	—
5) Interbank accounts	—	—	—	591.1	175.7	—	—	—	—	—	—	—
» »	—	—	—	*616.9*	*29.1*	—	—	—	—	—	—	*120.8*
6) Depos. at Banca d'Italia & UIC	—	—	*469.8*	475.7	- 41.6	—	—	—	2.4	—	36.6	- 3.3
7) Deposits at central auth.	—	27.4	3.6	2.9	- 9.0	—	- *8.5*	0.2	25.6	- 98.9	—	39.7
8) Dep. at auton. gov. agencies	—	—	—	—	—	—	—	—	—	-*114.0*	—	-114.0
9) Foreign and others	—	—	—	-114.7	- 94.3	—	1.7	—	- 17.2	48.8	-*114.7*	- *61.0*
c) Other deposits	**3,585.9**	**70.6**	**179.1**	**2,051.3**	**293.0**	—	**56.9**	—	- **1.3**	—	**3.4**	—
» »	—	—	*733.3*	*3,495.2*	*520.7*	—	*1,072.6*	—	—	*56.9*	*320.3*	*39.9*
1) Bank deposits	2,061.9	—	—	*2,061.9*	—	—	—	—	—	—	—	—
2) P. O. deposits	1,002.6	70.0	—	—	—	—	*1,072.6*	—	—	—	—	—
3) Interbank accounts	—	—	—	1,180.2	293.0	—	—	—	—	—	—	—
» »	—	—	—	*1,433.3*	—	—	—	—	—	—	—	*39.9*
4) Spec. cred. inst. sav. cert.	521.4	—	—	—	*521.4*	—	—	—	—	—	—	—
5) Foreign deposits	—	—	179.1	141.2	—	—	—	—	—	—	3.4	—
» »	—	—	*3.4*	—	—	—	—	—	—	—	*320.3*	—
6) Others	—	0.6	—	729.9	—	—	56.9	—	- 1.3	—	—	—
»	—	—	*729.9*	—	- *0.7*	—	—	—	—	*56.9*	—	—
d) Short-term securities	**10.5**	—	**686.6**	**1,021.5**	- **56.5**	—	*1,352.1*	—	—	—	*310.0*	—
e) Short-term loans	—	**306.2**	**63.9**	**3,958.3**	**151.7**	—	**161.7**	—	**12.7**	-**193.9**	**1,496.3**	- **52.5**
» »	*138.0*	*1,868.5*	- *39.6*	*1,736.1*	*104.0*	- *19.4*	-*208.8*	*365.8*	*53.0*	*158.0*	*1,814.7*	- *65.9*
1) Bank	*138.0*	*1,817.0*	—	2,480.5	—	- *2.6*	- *26.3*	*365.8*	*132.2*	*56.4*	—	—
2) By special credit institution	—	*9.3*	—	—	9.3	—	—	—	—	—	—	—
3) To special credit institution	—	—	—	70.4	142.9	—	—	—	—	—	—	—
» » »	—	—	—	*142.9*	*70.4*	—	—	—	—	—	—	—
4) BI-UIC	—	- *0.3*	- 76.3	*88.6*	*12.1*	—	-*176.7*	—	—	—	—	—
5) Reserve position in the IMF	—	—	45.6	—	—	—	—	—	—	—	*45.6*	—
6) SDR's	—	—	94.6	—	—	—	—	—	—	—	*94.6*	—
7) Foreign and others	—	306.2	—	1,407.4	- 0.5	—	161.7	—	12.7	-193.9	1,496.3	- 52.5
» » »	—	*42.5*	- *39.6*	*1,504.6*	*21.5*	- *16.8*	- *5.8*	—	- *79.2*	*101.6*	*1,674.5*	- *65.9*
f) Long-term loans	—	- **21.6**	**54.4**	**1,051.1**	**3,200.2**	**49.9**	**904.1**	**6.5**	**16.8**	—	**531.9**	—
» »	*441.2*	*3,551.9*	*66.9*	—	*312.2*	- *1.2*	*74.2*	*1,151.3*	*206.0*	*49.2*	- *21.8*	- *36.6*
1) Bank	*94.0*	*797.5*	—	1,051.1	—	—	- *3.1*	-*128.7*	*291.4*	—	—	—
2) Special credit institution	*335.0*	*2,433.5*	—	—	3,183.6	- *1.2*	—	*418.7*	—	- *2.4*	—	—
3) Foreign	—	- 22.3	- 16.1	—	16.6	—	—	—	—	—	531.9	—
»	—	*202.9*	*66.9*	—	*186.3*	—	*6.8*	*77.0*	—	- *8.0*	- *21.8*	—
4) Other	—	0.7	70.5	—	—	49.9	904.1	6.5	16.8	—	—	—
»	*12.2*	*118.0*	—	—	*125.9*	—	*70.5*	*784.3*	- *85.4*	*59.6*	—	- *36.6*
g) Bonds	**1,683.5**	**15.0**	**885.2**	**2,326.4**	**80.3**	**47.5**	- **37.6**	—	**34.8**	—	**17.0**	—
»	—	*508.7*	—	—	*2,229.1*	—	*1,747.9*	*26.6*	—	*483.2*	*46.5*	*10.1*
1) Gov. and auton. gov. agencies	47.2	6.0	728.5	1,388.2	53.5	6.4	- 17.5	—	18.6	—	0.2	—
» » » » »	—	—	—	—	—	—	*1,747.9*	—	—	*483.2*	—	—
2) Special credit institution	1,446.1	9.0	5.4	702.5	20.1	36.4	- 12.2	—	21.8	—	—	—
» » »	—	—	—	—	*2,229.1*	—	—	—	—	—	—	—
3) Other	122.1	—	185.6	235.7	- 3.3	2.0	- 7.9	—	- 5.6	—	16.8	—
»	—	*508.7*	—	—	—	—	—	*26.6*	—	—	—	*10.1*
4) Foreign bonds	68.1	—	- 34.3	—	10.0	2.7	—	—	—	—	*46.5*	—
h) Stocks & inv. in other firms' capital	**155.0**	**623.1**	**3.6**	**45.4**	- **21.1**	**8.2**	**747.7**	**77.5**	- **1.9**	—	**376.6**	**8.9**
» » » » » » »	—	*1,446.1*	—	*15.7*	*212.2*	*5.2*	—	—	—	—	*343.8*	—
i) Other assets and liabilities	**1,263.9**	**72.1**	**101.8**	**20.5**	—	—	—	—	—	**0.3**	**16.3**	—
» » »	—	*16.3*	—	—	—	*365.8*	*12.4*	—	*397.8*	—	*682.6*	—
1) Actuarial reserves	703.6	60.0	—	—	—	*365.8*	—	—	*397.8*	—	—	—
2) Other	560.3	12.1	101.8	20.5	—	—	—	—	—	0.3	16.3	—
»	—	*16.3*	—	—	—	—	*12.4*	—	—	—	*682.6*	—
j) Unclassified and discrepancies	—	—	—	—	—	—	—	—	—	—	—	**110.3**
» » »	—	—	*85.9*	*42.3*	*97.2*	—	—	—	—	—	*81.7*	-*196.8*
Total assets	**9,439.0**	**3,440.5**	**1,978.4**	**11373.6**	**3,685.5**	**165.2**	**1,846.4**	**475.2**	**351.4**	-**225.2**	**2,478.1**	- **2.2**
» *liabilities*	*579.2*	*7,391.5*	*1,978.4*	*11041.6*	*3,504.5*	*350.4*	*4,118.7*	*1,543.7*	*656.8*	*633.3*	*3,459.3*	-*251.5*
Net financial surplus or *deficit*	**8,859.8**	*3,951.0*	—	**332.0**	**181.0**	*185.2*	*2,272.3*	*1,068.5*	*305.4*	*858.5*	*981.2*	**249.3**

ASSETS AND LIABILITIES

figures in italic denote liabilities)

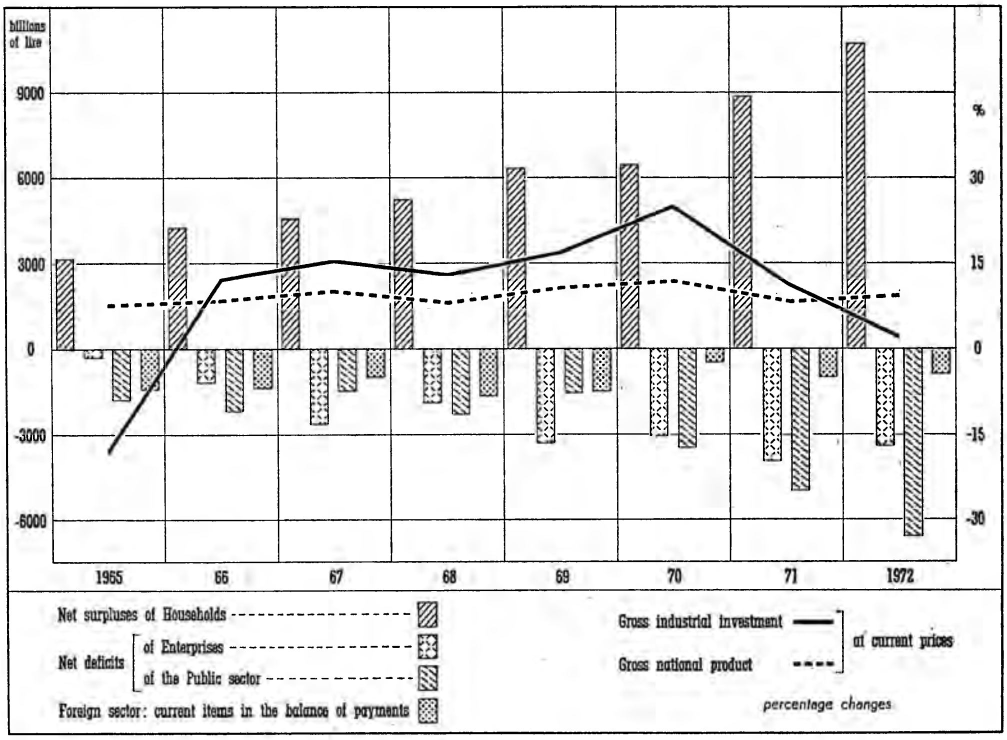
TABLE 55

Total			1972													
					Credit institutions				Public sectos						Total	
Assets	Liabilities		Households	Enterprises	BI-UIC	Banks	Special credit institutions	Insurance companies	Central authorities	Local authorities	Social Insurance Funds	Autonomous government agencies	Foreign Sector	Unclassified and discrepancies	Assets	Liabilities
- 1.8	*- 1.8*	A)	—	—	- 0.5	—	—	—	—	—	—	—	*- 0.5*	—	- 0.5	*- 0.5*
675.2	—	a)	1,237.4	75.0	- 2.0	163.9	- 6.8	0.1	5.8	—	- 0.2	14.7	—	—	1,487.9	—
—	*675.2*		—	—	*1,466.3*	—	—	—	*13.3*	—	—	—	*8.3*	—	—	*1,487.9*
6,073.5	—	b)	3,138.0	4,844.4	24.0	3,521.3	344.0	25.5	19.5	239.6	- 132.2	- 263.5	- 1.3	245.0	12,004.3	—
—	*6,073.5*		—	—	*419.3*	*8,563.3*	*4.3*	—	*523.5*	—	—	*14.5*	*713.4*	*1,766.0*	—	*12,004.3*
5,109.8	*5,109.8*	1)	3,138.0	4,479.6	—	*7,376.6*	—	25.5	18.4	- 130.2	- 151.9	- 2.8	—	—	7,376.6	*7,376.6*
- 62.0	*- 62.0*	2)	—	—	—	1,348.7	—	—	—	—	—	—	—	*1,348.7*	1,348.7	*1,348.7*
25.6	*25.6*	3)	—	—	—	*499.5*	—	—	—	—	—	36.0	—	463.5	499.5	*499.5*
61.7	*61.7*	4)	—	341.5	—	18.1	—	—	*359.6*	—	—	—	—	—	359.6	*359.6*
766.8	—	5)	—	—	—	1,677.1	57.3	—	—	—	—	—	—	—	1,734.4	—
—	*766.8*		—	—	—	*687.2*	*4.3*	—	—	—	—	—	—	*1,042.9*	—	*1.734.4*
469.8	*469.8*	6)	—	—	*419.3*	- 230.6	631.0	—	—	—	0.5	—	- 1.3	19.7	419.3	*419.3*
- 8.5	*- 8.5*	7)	—	23.3	24.0	- 5.4	- 17.7	—	*163.9*	369.8	280.3	- 257.7	—	- 252.7	163.9	*163.9*
- 114.0	*- 114.0*	8)	—	—	—	—	—	—	—	—	—	*14.5*	—	14.5	14.5	*14,5*
- 175.7	*- 175.7*	9)	—	—	—	713.4	- 326.6	—	1.1	—	- 261.1	- 39.0	*713.4*	- 625.6	87.8	*87.8*
6,238.9	—	c)	4,916.1	75.7	- 118.4	806.3	54.2	—	—	—	- 1.0	—	- 2.6	—	5,730.3	—
—	*6,238.9*		—	—	*575.9*	*4,226.4*	*394.4*	—	*1,354.9*	—	—	*7.6*	*- 671.5*	*- 157.4*	—	*5,730.3*
2,061.9	*2,061.9*	1)	3,233.9	—	—	*3,233.9*	—	—	—	—	—	—	—	—	3,233.9	*3,233.9*
1,072.6	*1,072.6*	2)	1,274.9	80.0	—	—	—	—	*1.354.9*	—	—	—	—	—	1,354.9	*1,354.9*
1,473.2	—	3)	—	—	—	780.9	54.2	—	—	—	—	—	—	—	835.1	—
—	*1,473.2*		—	—	—	*992.5*	—	—	—	—	—	—	—	*- 157.4*	—	*835.1*
521.4	*521.4*	4)	399.7	—	—	—	*399.7*	—	—	—	—	—	—	—	399.7	*399.7*
323.7	—	5)	—	—	- 118.4	- 553.1	—	—	—	—	—	—	- 2.6	—	- 674.1	—
—	*323.7*		—	—	*- 2.6*	—	—	—	—	—	—	—	*- 671.5*	—	—	*- 674.1*
786.1	—	6)	7.6	- 4.3	—	578.5	—	—	—	—	- 1.0	—	—	—	580.8	—
—	*786.1*		—	—	*578.5*	—	*- 5.3*	—	—	—	—	*7.6*	—	—	—	*580.8*
1,662.1	*1,662.1*	d)	2.7	—	- 712.0	964.9	- 5.7	—	*646.1*	—	—	—	*- 396.2*	—	249.9	*249.9*
5,904.4	—	e)	—	972.4	2,175.3	8,444.9	116.2	—	848.8	—	14.6	820.8	4,093.5	- 158.5	17,328.0	—
—	*5,904.4*		*500.0*	*3,287.7*	*10.5*	*5,648.5*	*- 79.2*	*- 39.0*	*687.5*	*586.4*	*1,061.7*	*932.2*	*4,728.2*	*3.5*	—	*17,328.0*
2,480.5	*2,480.5*	1)	*500.0*	*3,274.2*	—	4,664.7	—	*9.3*	*4.9*	*586.4*	*164.3*	*125.6*	—	—	4,664.7	*4,664.7*
9.3	*9.3*	2)	—	*3.1*	—	—	3.1	—	—	—	—	—	—	—	3.1	*3.1*
213.3	—	3)	—	—	—	27.3	120.2	—	—	—	—	—	—	—	147.5	—
—	*213.3*		—	—	—	*120.2*	*27.3*	—	—	—	—	—	—	—	—	*147.5*
- 76.3	*- 76.3*	4)	—	*- 0.9*	2,115.9	*1,434.7*	*- 16.7*	—	698.8	—	—	—	—	—	2.115.9	*2,115.9*
45.6	*45.6*	5)	—	—	- 11.5	—	—	—	—	—	—	—	*- 11.5*	—	- 11.5	*- 11.5*
94.6	*94.6*	6)	—	—	70.9	—	—	—	—	—	—	—	*70.9*	—	70.9	*70.9*
3,137.4	—	7)	—	972.4	—	3,752.9	- 7.1	—	848 8	—	14.6	820.8	4,093.5	- 158.5	10,337.4	—
—	*3,137.4*		—	*11.3*	*10.5*	*4,093.6*	*- 89.8*	*- 48.3*	*- 16.2*	—	*897.4*	*806.6*	*4,668.8*	*3.5*	—	*10,337.4*
5,793.3	—	f)	—	229.9	56.3	1,117.8	2,976.4	46.4	1.271.0	11.3	21.4	—	580.4	—	6,310.9	—
—	*5,793.3*		*550.5*	*3,160.6*	*66.3*	—	*499.9*	*8.2*	*60.0*	*1,488.2*	*12.8*	*- 20.8*	*175.1*	*310.1*	—	*6,310.9*
1,051.1	*1,051.1*	1)	*200.0*	*695.2*	—	1,117.8	—	—	*0.4*	*209.4*	*12.8*	—	—	—	1,117.8	*1,117.8*
3,183.6	*3,183.6*	2)	*345.0*	*2,273.0*	—	—	3,030.5	8.2	*- 0.4*	*410.3*	—	*- 5.6*	—	—	3,030.5	*3,030.5*
510.1	—	3)	—	229.9	- 0.7	—	- 54.1	—	—	—	—	—	580.4	—	755.5	—
—	*510.1*		—	*86.0*	*66,3*	—	*357.2*	—	*3.0*	*72.6*	—	*- 4.7*	*175.1*	—	—	*755.5*
1,048.5	—	4)	—	—	57.0	—	—	46.4	1,271.0	11.3	21.4	—	—	—	1,407.1	—
—	*1,048.5*		*5.5*	*106.4*	—	—	*142.7*	—	*57.0*	*795.9*	—	*- 10.5*	—	*310.1*	—	*1,407.1*
5,052.1	—	g)	2,105.3	45.0	1,158.4	2,904.4	51.0	66.1	- 43.5	—	21.6	—	—	8.0	6,316.3	—
—	*5,052.1*		—	*772.6*	—	—	*2,446.3*	—	*1,994.0*	*54.9*	—	*576.0*	*408.6*	*63.9*	—	*6,316.3*
2,231.1	—	1)	64.5	18.0	1,149.6	1,300.3	38.7	11.0	- 17.7	—	- 2.4	—	—	8.0	2,570.0	—
—	*2,231.1*		—	—	—	—	—	—	*1,994.0*	—	—	*576.0*	—	—	—	*2,570.0*
2,229.1	—	2)	1,219.3	20.0	9.0	1,123.0	7.4	48.6	- 12.8	—	31.8	—	—	—	2,446.3	—
—	*2,229.1*		—	—	—	—	*2,446.3*	—	—	—	—	—	—	—	—	*2,446.3*
545.4	—	3)	420.2	7.0	—	481.1	- 3.5	5.9	- 13.0	—	- 6.3	—	—	—	891.4	—
—	*545.4*		—	*772.6*	—	—	—	—	—	*54.9*	—	—	—	*63.9*	—	*891.4*
46.5	*46.5*	4)	401.3	—	- 0.2	—	8.4	0.6	—	—	- 1.5	—	*408.6*	—	408.6	*408.6*
2.023,0	—	h)	245.0	654.9	7.9	62.6	24.3	8.2	665.1	98.0	- 4.6	—	394.7	- 10.8	2,145.3	—
—	*2,023.0*		—	*1,740.5*	—	*71.2*	*162.8*	*0.9*	—	—	—	—	*169.9*	—	—	*2,145.3*
1,474.9	—	i)	1,270.3	103.9	0.8	—	—	—	—	—	—	173.4	28.9	—	1,577.3	—
—	*1,474.9*		—	*28.9*	—	—	—	*497.1*	*18.6*	—	*306.9*	—	*557.1*	*168.7*	—	*1,577.3*
763.6	*763.6*	1)	714.0	90.0	—	—	—	*497.1*	—	—	*306.9*	—	—	—	804.0	*804.0*
711.3	—	2)	556.3	13.9	0.8	—	—	—	—	—	—	173.4	28.9	—	773.3	—
—	*711.3*		—	*28.9*	—	—	—	—	*18.6*	—	—	—	*557.1*	*168,7*	—	*773.3*
110.3	—	j)	—	—	—	—	—	—	—	—	—	—	—	-1,537.0	- 1,537.0	—
—	*110.3*		—	—	*51.5*	*- 828.3*	*- 53.9*	—	—	—	—	—	*244.7*	*- 951.0*	—	*- 1,537.0*
35,005.9	—		12,914.8	7,001.2	2,589.8	17,986.1	3,553.6	146.3	2.766.7	348.9	- 80.4	745.4	5.093.6	-1,453.3	51,612.7	—
—	*35,005.9*		*1,050.5*	*8,990.3*	*2,589.8*	*17,681.1*	*3,374.6*	*467.2*	*5,297.9*	*2,129.5*	*1.381.4*	*1,509.5*	*5,937.1*	*1,203.8*	—	*51,612.7*
—	—		11,864.3	*1,989.1*	—	305.0	179.0	*320.9*	*2,531.2*	*1,780.6*	*1,461.8*	*764.1*	*843.5*	*2,657.1*	—	—

to the creation of a 10,760 billion financial surplus, equal to 19.8 per cent of disposable income (18 per cent in 1971 and 13.6 on average over the period 1964-1970). The increased weight of the households' financial saving was the result of a high propensity to save and the fall-off in investments channelled towards home purchases, determined chiefly by a substantial decrease in supply.

The public sector's financial deficit, continuing the trend begun in 1970, grew appreciably during the year under study, moving from 7.3 to 9.3 per cent of the GNP. Finally, the impetus provided by the Foreign sector, whose deficit on current account fell from 981 to 844 billion, declined slightly (Chart 33).

CHART 33



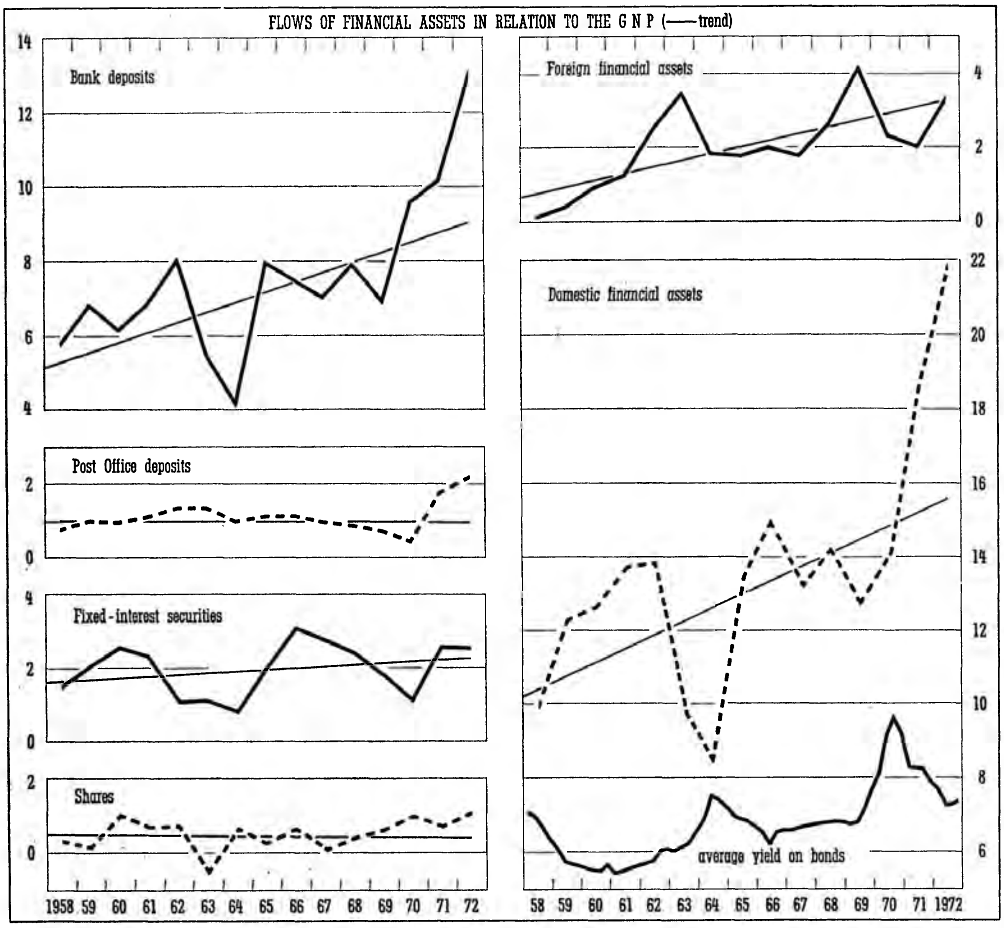
Financial balances of the sectors

(changes in billions of lire)

The Economy's financial assets

The Economy's propensity to purchase financial assets, equalling 15.6 per cent of the GNP between 1964 and 1970, rose sharply during the last two years, rising to 20.4 per cent in 1971 and 25.2 in the year under study (Chart 34 and Table 56). This performance, made possible by the expansionary monetary policy, was due to the public administration's huge current account deficit and the increase in the enterprises' liabilities, linked with heavier financial investments. As a result, the public sector's share in the overall creation of financial assets rose (36.7 per cent compared with 35.7 in 1971), while the share repre-

CHART 34



The Economy's financial assets

(changes in relation to the GNP) (1)

(1) The trends were calculated for the period 1951-1971.

senting enterprises' indebtedness fell from 61.9 to 57.7 per cent, despite its increment in absolute terms. The relative importance of the Foreign sector also decreased (Table 57).

About half of the Economy's increased demand for financial assets can be attributed to the Enterprises sector which expanded its financial investments by about 60 per cent over the previous year's substantial amount (5,600 billion versus 3,440 in 1971) increasing both its short-term foreign assets and liquid and financial investments on the domestic market.

The expansion in the enterprises' foreign assets, which was mainly achieved by delaying receipt of trade credits and anticipating payment of imports, grew out of expectations of parity changes. The increase in liquid assets in lire stemmed chiefly from the fall-off in interest rates. The increased money balances, which rose from 2,450 to 3,600 billion also owing to a larger sales volume towards the end of the year, reflect both easy money conditions and the enterprises' slack investment activity.

TABLE 56

RATIO OF THE ECONOMY'S FINANCIAL ASSETS TO THE NATIONAL PRODUCT

Years	Changes: financial assets / GNP	Changes: liquid assets / GNP	Yield on bonds
1964	10.2	5.8	6.97
1968	16.9	9.7	6.54
1969	16.9	9.0	6.73
1970	16.5	10.8	8.63
1971	20.4	13.1	8.02
1972	25.2	16.5	7.29
1964-1970 Average	15.6	9.3	6.91

Share purchases and investments in other firms' capital, which kept to 1971's high levels (about 650 billion), reflect the trend, marking the productive enterprises' behaviour in recent years, to develop equity capital ties with other enterprises, to take over smaller companies and to establish firm ties with foreign enterprises operating in the same sector, as well as to the sharp growth of the holding companies.

At the end of 1972 the Economy's financial assets amounted to 123,000 billion; that is 17.1 per cent above the previous year's level (14.7 in 1971), not counting changes in share prices. The most pronounced increase regarded chiefly foreign financial assets: 25.5 per cent versus 7.1 in 1971. On the domestic side, liquid assets rose by 19.1 per cent (16.1 during the previous year); more specifically, bank and Post Office savings deposits showed buoyant results, climbing by 4,800 billion in 1972.

TABLE 57

THE ECONOMY'S FINANCIAL ASSETS AND THEIR COUNTER-ITEMS

(amounts and changes in billions of lire)

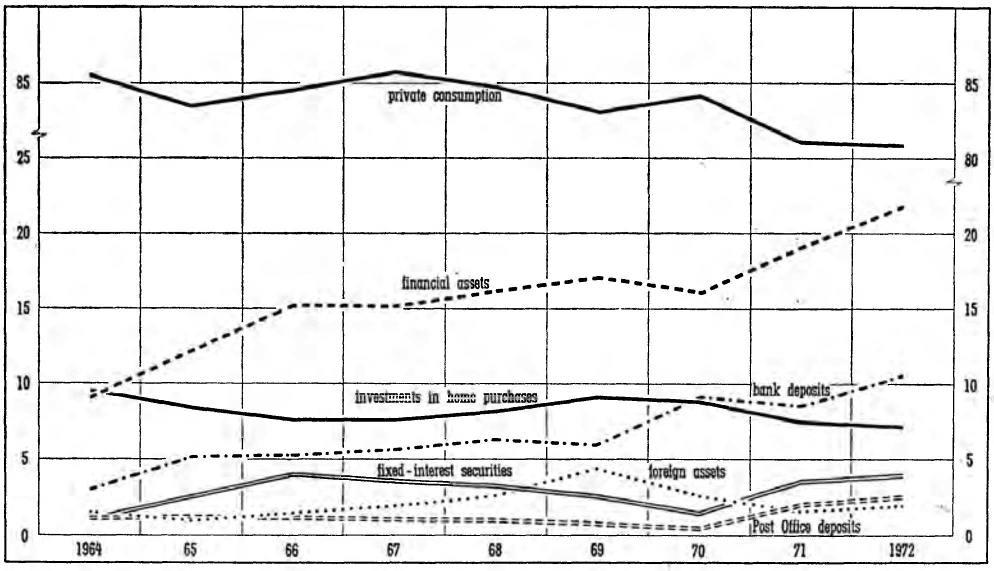
Items	Amount at end 1971	1970	1971	1972 Year	1972 Quarters (1) I	II	III	IV
Financial assets:								
DOMESTIC	93,355	8,262	11,623	15,087	1,837	3,552	2,698	7,000
Liquid assets (2)	59,594	6,308	8,260	11,386	507	2,417	2,048	6,414
Other deposits and savings certificates	2,120	164	522	403	163	148	14	78
Fixed-interest securities	13,553	645	1,630	1,749	869	556	297	27
Stocks and investments in other firms' capital	11,612	576	434	731	100	230	137	264
Other financial assets	6,476	569	777	818	198	201	202	217
FOREIGN	10,269	1,351	1,256	2,329	450	485	572	822
Short-term loans (net) and long-term loans	2,366	396	284	1,202	80	285	287	550
Other financial assets	7,903	955	972	1,127	370	200	285	272
Total (3)	103,624	9,613	12,879	17,416	2,287	4,037	3,270	7,822
Against financing of:								
ECONOMY								
Short-term indebtedness	24,344	2,416	2,007	3,788	- 393	521	610	3,050
Medium- and long-term indebtedness	29,881	2,691	4,518	4,512	1,227	770	1,202	1,313
Stocks and investments in other firms' capital	15,833	920	845	1,126	208	360	178	380
Funds granted by the public sector	2,492	211	601	615	28	405	157	25
Total	72,550	6,238	7,971	10,041	1,070	2,056	2,147	4,768
Foreign sector	*5,832*	*882*	*613*	*509*	*206*	*145*	*- 8*	*166*
FOREIGN SECTOR (4)	7,901	476	981	844	353	407	336	- 252
PUBLIC SECTOR (consolidated)	26,449	3,452	4,592	6,387	741	1,164	2,137	2,345
UNCLASSIFIED (5)	- 3,276	- 553	- 665	144	123	410	- 1,350	961
TOTAL	103,624	9,613	12,879	17,416	2,287	4,037	3,270	7,822
Economy's finan. surplus or deficit:								
short-term (6)	37,370	4,056	6,775	8,001	1,063	2,044	1,452	3,442
long-term	- 6,296	- 681	- 1,867	- 626	154	- 63	- 329	- 388
Net surplus (7)	31,074	3,375	4,908	7,375	1,217	1,981	1,123	3,054

(1) Figures partly estimated.— (2) Figures adjusted for random movements at end-1972.— (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 commercial credit to foreign customers.— (7) During 1971 the Economy's financial balances were . . . 326 783 758 3,041

A marked propensity to save and a further drop in investment for home purchases on the part of the households gave rise to the creation of a huge volume of financial assets for the sector, which rose from 14.8 per cent of disposable income over the years 1964-1970 to 19.1 in 1971 and 21.8 per cent in 1972 (Chart 35).

During the year under study the fall-off in the number of houses built, the hefty upswing in dwelling purchase prices and the new tax system about to come into force curbed direct investments in home purchases on the part of the households, thus fostering demand for financial assets. It appears unlikely that prospects regarding the lira's purchasing power, which became more uncertain during the second part of the year, had any appreciable impact on the distribution of saving between real and financial investments. On the contrary, due partially to persistent uncertainties regarding the economic situation, the households' preference for types of financial investment other than non-liquid assets sharpened.

Chart 35



Households' financial assets (1)

(changes in relation to disposable income)

(1) The graph also includes consumption and investments-in-building trends, in relation to the disposable income of the Households sector, for the purpose of allowing a comparison with the evolution of financial assets in the sector.

From a study of the distribution of financial saving it emerges, in effect, that the percentage of liquid assets increased (from 61.5 to 65.9) while investments in fixed-interest securities contracted (14.4 per cent of the total, against 17.1 in 1971). The heavier upswing in liquid assets, compared with overall financial saving, shows up clearly in the performance of bank deposits (up from 44.6 to 48.9 per cent). Moreover, Post Office deposits, displaying no let-up from their expansive performance, amounted to 10.8 per cent of the total (Table 58).

The lesser relative importance of fixed-interest securities, which nonetheless increased in absolute terms, is linked not only with the above-mentioned conditions but also with the fear that the rises registered in interest rates on the foreign markets from spring onwards would spread to the domestic market. The demand for securities, after making seasonal adjustments, was, in fact, fairly heavy during the first half of the year and contrastingly weak during the second.

Although share purchases picked up slightly, they remained on fairly low levels (1.5 per cent of the total), pointing to both the households' slight propensity to invest in this type of instrument — chiefly because of the decline in returns — and the gradual shrinking

TABLE 58

ANALYSIS OF HOUSEHOLDS' FINANCIAL ASSETS (1)

Items	Amounts at end of		Average flows	Flows			
	1963	1971	1964-1971	1969	1970	1971	1972
	(billions of lire)						
Notes and coins (2)	2,641	5,703	382	614	423	590	737
Bank deposits (2)	8,263	26,887	2,328	2,333	4,070	4,212	5,772
Post Office deposits	2,681	5,717	379	291	156	1,003	1,275
Other deposits and P. O. certificates	567	2,137	196	121	172	532	410
Fixed-interest securities	4,580	13,192	951	943	642	1,615	1,704
Shares (3)	7,021	4,626	71	160	230	40	175
Actuarial reserves	2,227	5,968	468	502	527	704	714
Foreign assets	1,632	6,548	757	1,758	891	743	1,028
Total	29,612	70,778	5,532	6,722	7,111	9,439	11,815
	(percentage breakdown)						
Notes and coins	*8.9*	*8.1*	*6.9*	*9.1*	*6.0*	*6.3*	*6.2*
Bank deposits	*27.9*	*38.0*	*42.0*	*34.7*	*57.3*	*44.6*	*48.9*
Post Office deposits	*9.1*	*8.1*	*6.9*	*4.3*	*2.2*	*10.6*	*10.8*
Other deposits and P. O. certificates	*1.9*	*3.0*	*3.5*	*1.8*	*2.4*	*5.6*	*3.5*
Fixed-interest securities	*15.5*	*18.6*	*17.2*	*14.0*	*9.0*	*17.1*	*14.4*
Shares	*23.7*	*6.5*	*1.3*	*2.4*	*3.2*	*0.4*	*1.5*
Actuarial reserves	*7.5*	*8.4*	*8.5*	*7.5*	*7.4*	*7.5*	*6.0*
Foreign assets	*5.5*	*9.3*	*13.7*	*26.2*	*12.5*	*7.9*	*8.7*
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

(1) Figures partly estimated.— (2) For 1972 flows are adjusted for random movements at end-year.— (3) In order to exclude the influence of changes in market prices, the total for shares at the end of 1971 can be obtained by applying the calculated index for stock prices at the end of 1963; this sum was 10,304 billion, equal to 13.5 per cent of total assets.

of offers to the public of newly issued securities as a result of a decline in the relative importance of increases in the capital of listed companies.

Contractual saving with the insurance companies and social insurance institutions, which is structurally modest in comparison with the Anglosaxon countries where it accounts for from one-third to one-half of the households' financial savings, continued to lose ground in relation to other financial assets (6.0 per cent compared with 7.5 in 1971). Finally, foreign financial assets, which consisted of a larger ratio of bonds than in 1971, held steady at around 8 per cent of the total.

Enterprises' liabilities

The total flow of financing to the Economy amounted to 10,040 billion, equal to 18.3 per cent of the private gross product and 78.2 per cent of private investments (respectively 14.3 and 56.9 per cent over the years 1960-1972) (Table 59).

TABLE 59

RATIOS OF THE ECONOMY'S FINANCIAL LIABILITIES TO INCOME AND INVESTMENT

Years	Change in financial liabilities			Credit to building sector
	Gross private product	Gross private investment		Gross investment in housing
		(1)	(2)	(3)
1951	7.1	31.5	33.8	28.2
1959	9.0	35.6	42.2	24.6
1970	13.5	51.3	60.1	33.9
1971	16.0	67.3	82.5	33.9
1972	18.3	78.2	98.1	33.3
1951-1959 Average	8.1	33.3	37.3	26.0
1960-1972 »	14.3	56.9	68.0	35.0

(1) Including investments in buildings.— (2) Excluding investments in buildings.— (3) Excluding housing financed by the public sector.

Since the upswing in the households' indebtedness can be estimated at around 1,050 billion for the year, that of the enterprises equals 8,990 billion; that is, a 21.6 per cent increase over the previous year. The interruption of the positive correlation existing up to 1970 between the behaviour of the ratio of gross investment to GNP and the ratio of enterprises' external financing to GNP is chiefly connected with the fall-off in internal saving in 1971 and the above-mentioned increase in financial investments during the year under study.

Short-term financing accounted for 36.6 per cent of the total (25.3 in 1971). Since development flagged with regard to investment in fixed assets — where initial financing mainly takes the form of short-term indebtedness — it appears that the hefty upswing in demand for bank credit, which may have been affected by the abnormal working conditions in the banks at end-year, is linked mainly with stepped-up inventory building, the extension of payment terms for non resident customers of the Italian enterprises and also with the reduction in the foreign currency settlement terms for merchandise imports (Table 60).

TABLE 60

ANALYSIS OF THE STRUCTURE OF BALANCE-SHEET LIABILITIES AND EXTERNAL FINANCING OF THE ENTERPRISES

Items	Amounts at end of		Average flows	Flows				
	1963	1971	1964–1971	1968	1969	1970	1971	1972
	(billions of lire)							
Short-term loans	10,762	22,740	1,515	1,275	2,436	2,275	1,869	3,288
Medium- and long-term loans	6,493	19,701	1,618	1,562	1,530	2,132	3,568	3,189
special credit institutions	*4,361*	*13,698*	*1,124*	*1,204*	*1,163*	*1,264*	*2,434*	*2,273*
Bonds	2,112	5,947	429	516	494	44	509	772
Shares and investments in other firms' capital (1)	16,684	15,833	550	474	622	920	845	1,126
Capital funds granted by the public sector (2)	779	2,492	218	284	215	211	601	615
Total	36,830	66,713	4,330	4,111	5,297	5,582	7,392	8,990
	(percentage breakdown)							
Short-term loans	*29.2*	*34.1*	*35.0*	*31.0*	*46.0*	*40.8*	*25.3*	*36.6*
Medium- and long-term loans	*17.6*	*29.5*	*37.4*	*38.0*	*28.9*	*38.2*	*48.3*	*35.5*
special credit institutions	*11.8*	*20.5*	*26.0*	*29.3*	*22.0*	*22.6*	*32.9*	*25.3*
Bonds	*5.8*	*8.9*	*9.9*	*12.6*	*9.3*	*0.8*	*6.9*	*8.6*
Shares and investments in other firms' capital (1)	*45.3*	*23.7*	*12.7*	*11.5*	*11.7*	*16.4*	*11.4*	*12.5*
Capital funds granted by the public sector (2)	*2.1*	*3.8*	*5.0*	*6.9*	*4.1*	*3.8*	*8.1*	*6.8*
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

(1) In order to exclude the influence of changes in market prices, the volume of stock and investments in other firms' capital at the end of 1971 can be obtained by applying the index relative to stock market prices at end-1963; this is estimated at 26,723 billion. Risk capital, including capital funds granted by the public sector, in this case represents 37.6 per cent of total liabilities.— (2) Includes funds granted by the local authorities.

Medium- and long-term indebtedness in the form of loans and bonds, whose flows almost doubled in 1971, declined over the year under study to 3,960 billion, equal to 44.1 per cent of external financing (55.2 in the previous year). More specifically, loans granted by the special credit institutions, although still accounting for the largest portion of medium- and long-term financing, registered a slight fall-off in absolute value and a heavier drop in relative terms. This development, which is partly the result of a slowdown in the growth rate of institutions' lending and also of the above-mentioned recovery of short-term indebtedness, regarded financing, to both the manufacturing and building sectors, and concerned both loans at subsidized rates and those at market rates. Medium- and long-term financing by the banks also registered a fall-off compared with 1971, despite the fact that measures introduced during the year enlarged their possibilities for intervention in this sector.

Instead, bond issues which were made solely by the public enterprises, soared (772 billion against 509). The diverging trend of bond indebtedness compared with overall medium- and long-term indebtedness was the result of ENEL's (National Electricity Agency) huge bond flotations both to cover its compensation payments and finance its investments, given the fall-off in its internal saving. Bond issues were also fostered by improved market conditions, owing to the downward movement of interest rates and the banks' heavy demand for this financial instrument.

Risk capital, in the form of shares, equity capital and endowment funds, amounted to 19.3 per cent of the enterprises' overall financing; that is, about one and a half percentage points over the average for the 1964-1971 period. Although the government's contribution to the public enterprises via grants has become appreciable (35 per cent of the total of resources raised externally by the enterprises during the year, compared with 28 per cent on average for the period 1964-1971), in 1972 it appears that a certain revival of the share component contrasted with the trend in recent years (with the exception of 1970) for the relative importance of shares as a financal instrument to lessen. Increases in equity capital through the sale of new share issues amounted to 1,126 billion, compared with 845 in 1971.

Financing of the enterprises by sector of economic activity

As we know, the distribution of overall financing among sectors of economic activity basically reflects the growth rate of the gross product and of investments — being respectively indexes of the need for working capital and fixed capital — as well as the development of the enterprises' gross profits and the depreciation and self-financing policy connected with this.

The fall-off in the volume of funds received by the enterprises operating in the mechanical and non-metallic minerals industry sectors compared with 1971 is linked, above all, with the slack growth rate of the gross product and the near stagnancy of investments. With regard to the mechanical engineering enterprises, the fall-off concerned medium- and long-term financing and loans by the public and Foreign sectors; on the other hand loans by the banking system rose considerably, back to medium-term levels (50 per cent of the total). With regard to companies operating in the non-metallic minerals sector, short-term debt as well as indebtedness to the special credit institutions declined (Table 61).

The remaining industrial sectors greatly increased their volume of financing. More specifically, the metallurgy enterprises — with investments growing at a faster rate than the general average for industry and the gross product registering a favourable development — doubled both their indebtedness with the credit institutions and their raising of risk capital, as compared with 1971. Medium- and long-term loans, which are more indicative of investment activity, amounted to 57 per cent of overall financing (35 per cent in 1971).

The petroleum industry also received more than double 1971's volume of financing, mainly in the form of bank credit. On the other hand, the chemicals industry, grouped with the previous sector and the rubber sector for comparability with the gross product, received external financing for about the same amount as in 1971. Finally recourse to indebtedness by enterprises in the rubber industry dropped considerably. The performance of real variables does not offer sufficient explanation, given also the different growth rates of credit demand in the three branches, of the sharp increase in external debt. Since the latter occurred

TABLE 61

FINANCING OF THE ECONOMY BY SECTORS OF ECONOMIC ACTIVITY

(changes in billions of lire)

Sources of credit / Sectors of economic activity	Banking system	Special credit institutions and insurance companies (1)	Public sector (2)	Securities (3)	Foreign sector (4)	Total	Short-term financing / Total financing	Short-term financing (amounts) / Gross product (5)
							(percentage ratios)	
			1971					
ECONOMY	2,846	2,795	757	1,354	219	7,971	*25.2*	*53.5*
Industry (6)	1,723	1,377	503	904	77	4,584	*37.2*	*82.3*
Mechanical	*295*	*547*	*137*	*249*	*81*	*1,309*	*22.2*	*73.5*
Metallurgical	*220*	*219*	*86*	*22*	*85*	*632*	*34.5*	*177.1*
Non-metallic minerals processing	*109*	*63*	*11*	*19*	*2*	*204*	*52.5*	*77.2*
Chemicals and petroleum (7)	*537*	*447*	*210*	*177*	*45*	*1,416*	*38.3*	*123.4*
Textiles, etc. (8)	*148*	*57*	—	*32*	*23*	*260*	*55.0*	*68.4*
Wood, paper, etc.	*61*	*20*	—	*39*	*16*	*136*	*40.4*	*63.6*
Electricity, gas and water	*303*	*- 17*	*48*	*342*	*- 181*	*495*	*61.2*	*43.1*
Others	*50*	*41*	*11*	*24*	*6*	*132*	*36.4*	*77.9*
Other sectors	1,123	1,418	254	450	142	3,387	*8.9*	*37.9*
			1972					
ECONOMY	4,669	2,629	730	1,898	115	10,041	*37.7*	*56.6*
Industry (6)	2,381	1,210	389	1,323	- 25	5,278	*44.2*	*88.0*
Mechanical	*569*	*205*	*67*	*254*	*21*	*1,116*	*48.7*	*77.3*
Metallurgical	*350*	*544*	*31*	*59*	*- 29*	*955*	*36.6*	*190.4*
Non-metallic minerals processing	40	26	*3*	*27*	*3*	*99*	*35.4*	*76.8*
Chemicals and petroleum (7)	*858*	*288*	*230*	*326*	*- 5*	*1,697*	*50.4*	*144.6*
Textiles, etc. (8)	*225*	*89*	—	*98*	*- 7*	*405*	*53.6*	*68.4*
Wood, paper, etc.	*103*	*43*	—	*62*	—	*208*	*45.7*	*59.8*
Electricity, gas and water	*175*	*- 15*	*51*	*489*	*- 5*	*695*	*25.5*	*51.3*
Others	*61*	*30*	*7*	*8*	*- 3*	*103*	*56.3*	*81.5*
Other sectors	2,288	1,419	341	575	140	4,763	*30.6*	*39.3*

(1) In conformity with the tables of the financial accounts, lending by special credit institutions regarding agriculture, housing and real estate excludes the difference between nominal value and market-value emerging in the sale, by the borrower, of the lender's mortgage bonds.— (2) Including granted funds supplied by the Treasury and by local authorities.— (3) Including securities subscribed to by non-residents. Shares issued by state-controlled companies are net of those acquired by the government agencies in exchange for the funds granted by the Treasury.— (4) Including only long-term trade credit; with regard to securities see footnote (3).— (5) Ratios of the short-term credit totals to the gross product, at production factors cost of the individual sectors of activity (the source of the latter is Istat).— (6) Excluding the food and building industries which are included in the other sectors.— (7) Including the rubber industry.— (8) Including clothing, leather and footwear.

for the most part in the petroleum enterprises, it is likely that stable prices in the sector, while costs were rising, had a negative impact on self-financing and that the larger amount of credit received was also used to increase financial investments.

The higher recourse to indebtedness by the electric power, gas and water sector, nearly one-third in the form of bond issues, should be linked with the marked deterioration in the profit and loss accounts of companies in that branch, which was the result of rising costs and stable prices.

Financing of investments by sector

The public sector's financing needs amounted to 4,289 billion, compared with 4,664 in the previous year. The sector's investment expenditure increased by 15 per cent, mainly as a result of the appreciable rise in outlays by the local authorities (16.5 per cent). Instead, both capital account transfers and purchases of financial assets fell as compared with 1971; more specifically, there was a pronounced decrease in the social insurance institutes' and local authorities' bank deposits, whereas capital funds granted to the public enterprises and special credit institutions only declined slightly (Table 62).

Since the public administration's current account deficit, already pronounced in 1971, expanded even further, the authorities were forced to resort to other sectors' savings for a gross amount of 7,555 billion (6,378 in 1971). More specifically, the local authorities, social insurance institutes and autonomous government agencies increased their recourse to the banking system by two-thirds, taking into account the above-mentioned trend of deposits, the banking system's net contribution to financing said sectors rose from 239 to 1,779 billion. This mainly concerns the local authorities, whose net debt with the banks stood at 933 billion in 1972, against net repayments for 139 billion in 1971.

In 1972, the public enterprises expanded their investments in fixed assets by 14.4 per cent; given the increase in inventories, their investments rose by 15.8 per cent and thus their percentage of overall capital formation moved up from 20.7 to 22.3. The public enterprises also purchased more financial assets and, in particular, more liquid assets, which rose from 30 to 388 billion.

TABLE 62

INVESTMENTS AND THEIR COVERAGE

(changes in billions of lire)

Items	Public sector (consolidated)	State-controlled companies and ENEL	Other enterprises and housing	Households	Credit institutions (consolidated)	Total	Foreign sector
			1971				
Investments: in fixed assets	2,016	2,439	7,945	—	280	12,680	—
(excluding housing)			*4,332*				
in inventories	....	239	16	—	—	255	—
Transfers in capital account	861	- 14	- 829	—	—	18	- 18
Financial assets (2)	1,787	169	3,157	9,439	12,565	27,117	2,478
Liquid assets	753	30	2,416	6,337	1,793	11,329	40
Fixed-interest securities	- 4	....	15	1,683	2,575	4,269	17
Other assets (net)	215	20	222	1,264	8,203	9,924	2,044
Shares and investments in other firms' capital	823	119	504	155	- 6	1,595	377
Total requirements	***4,664***	***2,833***	***10,289***	***9,439***	***12,845***	***40,070***	***2,460***
Financial liabilities (3)	6,378	2,172	5,546	138	12,238	26,472	3,459
Short-term loans (4)	3,688	831	1,038	138	9,787	15,482	2,326
Other loans: from domestic sectors	1,086	320	3,355	—	542	5,303	742
from foreign sectors	76	- 144	363	—	253	548	—
Bonds (5)	1,528	552	- 43	—	1,465	3,502	47
Shares and investments in other firms' capital	—	613	833	—	191	1,637	344
Gross saving (6)	-1,674	661	5,042	9,301	600	13,930	- 995
Adjustments	- 40	—	- 299	—	7	- 332	- 4
Total coverage	***4,664***	***2,833***	***10,289***	***9,439***	***12,845***	***40,070***	***2,460***
			1972 (1)				
Investments: in fixed assets	2,318	2,790	7,914	—	300	13,322	—
(excluding housing)			*4,030*				
in inventories	....	310	270	—	—	580	—
Transfers in capital account	803	- 19	- 766	—	—	18	- 18
Financial assets (2)	1,168	472	5,002	11,815	16,669	35,126	5,093
Liquid assets	- 249	388	3,207	8,195	663	12,204	- 4
Fixed-interest securities	- 2	....	45	2,105	2,992	5,140	—
Other assets (net)	660	- 56	1,235	1,270	12,959	16,068	4,702
Shares and investments in other firms' capital	759	140	515	245	55	1,714	395
Total requirements	***4,289***	***3,553***	***12,420***	***11,815***	***16,969***	***49,046***	***5,075***
Financial liabilities (3)	7,555	2,880	6,533	500	16,506	33,974	5,937
Short-term loans (4)	4,947	735	2,553	500	14,218	22,953	4,381
Other loans: from domestic sectors	1,042	720	2,776	—	419	4,957	977
from foreign sectors	71	- 30	145	—	424	610	—
Bonds (5)	1,495	822	- 49	—	1,258	3,526	409
Shares and investments in other firms' capital	—	633	1,108	—	187	1,928	170
Gross saving (6)	-2,884	673	5,016	11,315	630	14,750	- 848
Adjustments	- 382	—	871	—	- 167	322	- 14
Total coverage	***4,289***	***3,553***	***12,420***	***11,815***	***16,969***	***49,046***	***5,075***

(1) 1972 figures are provisional; moreover they are adjusted for random movements at end-year.— (2) The financial assets of the state-controlled companies, 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. 1643 of December 6, 1962.— (3) The external financing of *other enterprises* corresponds to the enterprise sector's total liabilities (less the compensation payments made by ENEL), less the public enterprises' borrowing and plus an estimated amount for loans obtained for households' investments in housing.— (4) Includes the BI-UIC's purchases of long-term securities issued by the public sector.— (5) Issued on the domestic market; bonds issued on the international markets are included in the item *other loans from the foreign sectors*.— (6) Households' gross saving has been made equal to net financial investment.

On the other hand, gross saving, following 1970 and 1971's decline, increased only slightly, from 661 billion in 1971 to 673; this trend was more pronounced with regard to the state-controlled enterprises, which self-financed a larger percentage of plants and equipment (27.1 per cent compared with 24.2 in 1971). Given the hefty upswing in their overall financial requirements, the public enterprises resorted to external sources of financing for a far greater amount, 2,880 billion against 2,172.

Loans granted by the special credit institutions rose from 434 to 846 billion, in connection with investment activity by IRI (Institute for Industrial Reconstruction) and ENI (National Hydrocarbon Agency) whereas the amount of risk capital, mostly made up of capital funds granted by the Treasury, remained around the same level as in 1971. Net bond issues on the domestic market rose from 552 to 822 billion, thus their relative weight on total liabilities increased.

There was a decrease in bank credit compared with 1971, despite higher recourse to it by IRI and ENI to prefinance a large volume of investments. Short-term borrowing by ENEL decreased, in terms of flows, in comparison with the fairly high level registered in 1971, although the amount of financing was far from negligible. It should be recalled that ENEL, with a 50 billion increase in investments, greatly expanded bond issues, which amounted to 701 billion, as against 546 in 1971.

Investments in plants and equipment by the *other enterprises and housing* sector remained fairly stable whereas, excluding the housing sector, they registered a 7 per cent decrease. If inventories are also taken into account, the result is a 2.8 per cent rate of increase.

Gross saving by the sector under study held steady on the 1971 level since the households appear to have directly invested a much smaller amount of saving in home purchases — as seems to be borne out by the smaller change in the sector's overall saving, estimated on the basis of national accounts data, in respect to the change in net financial investment and by the sharp decrease in the number of houses built — gross self-financing by *other enterprises* should have soared.

It should be stressed that, given the size of statistical discrepancies shown in Table 62 the amount of gross saving of *other enterprises and housing* might be underestimated. There was a hefty increase in the financial assets of *other enterprises and housing,* which rose from 3,157 to 5,002 billion for the reasons given in the paragraph on the Economy's assets. Since recourse to external financing increased by 987 billion, the sector's financial deficit fell from 2,389 billion in 1971 to 1,531 in 1972 and, consequently, the portion of real investments covered by external funds fell.

With regard to the various categories of liabilities, trends have not differed to any great extent from those described in the preceding paragraphs. More specifically, there was a further increase in financing through share issues, whose percentage in total liabilities and in gross investment increased, respectively, from 15 to 17 and from 10.5 to 13.5 per cent.

Reported manufacturing industry results

From the annual survey of the manufacturing companies' balance-sheets, it emerges that in 1972 there was an improvement in the companies' operating results, linked with signs of a recovery in production and the near-completion in almost all sectors of the restructuration process started by the industries during the last three years.

Signs of improvement in the economic conditions can be gleaned from the increase in gross profits and net balance-sheet profits and from the upswing in investments by the small-sized firms (those in the sample with a net worth of under 20 billion) which are usually highly tuned to short-term cyclical tendencies (Tables 63, 64 and 65).

Some indication that company management has been less affected by events of an extraordinary nature may be read into the smaller volume of fixed disinvestments (— 24 per cent compared with 1971) and by the appreciable reduction in the depreciation of real and financial items bringing the phenomenon back to virtually normal dimensions.

As usual, the analysis concerns a group of large- and medium-sized enterprises (134 in the year under study) which account for over a third of the entire manufacturing industry's fixed-asset investments.

With regard to sample companies as a whole, gross fixed-capital creation amounted to 1,407 billion, a drop of 7 per cent compared with the previous year. This performance is in contrast with that of

TABLE 63

INVESTMENTS AND THEIR FINANCING IN A GROUP OF 134 ITALIAN MANUFACTURING COMPANIES

Predominantly state-controlled and private companies classed in terms of net worth

(billions of lire)

Items	Predominantly state-controlled companies (9 companies)		Private companies with net worth over 20 billion (16 companies)		Private companies with net worth up to 20 billion (109 companies)	
	1971	1972	1971	1972	1971	1972
Gross fixed investment	666.1	713.7	692.1	518.9	156.0	174.3
gross changes in fixed capital	*638.0*	*636.4*	*436.5*	*430.2*	*139.6*	*111.3*
Changes in securities and investments in other firms' capital	36.8	- 7.1	427.2	93.1	13.2	43.2
(1) Total investment in fixed assets	702.9	706.6	1,119.3	612.0	169.2	217.5
Gross self-financing	115.2	217.8	260.4	259.5	85.3	125.0
Stock paid in	25.0	0.4	50.5	143.5	21.9	55.9
Repayments of ENEL credit	10.9	11.4	62.7	67.1	0.3	0.3
(2) Total of sources of non-borrowed funds	151.1	229.6	373.6	470.1	107.5	181.2
(2) : (1) *per cent*	*21.5*	*32.5*	*33.4*	*76.8*	*63.5*	*83.3*
Medium- and long-term borrowing	474.9	526.3	405.7	25.3	70.4	75.2
(3) Total of sources of medium- and long-term funds	626.0	755.9	779.3	495.4	177.9	256.4
Balances (3)−(1)	- 76.9	49.3	- 340.0	- 116.6	8.7	38.9
Changes in net bank indebtedness	154.6	- 16.5	342.2	16.8	56.8	- 25.5
Increase or decrease in inventories	74.5	83.1	75.6	- 116.0	47.1	- 12.4

the entire industrial sector (+ 2.2 per cent) even though for both groups the pattern was the result of diverging trends for investments by the state-controlled enterprises (+ 7.1 per cent in the sample and + 8.5 in the total) and those by the private enterprises (— 18.3 per cent in the sample and — 2.9 in the total) (Table 63). Since most of the companies surveyed are large-sized ones, the decline in their capital accumulation, compared with an increase for industry as a whole, should point to increased investment by the entire sector of medium- and small-sized enterprises during the year.

Deducting from total investments those intended to replace obsolete facilities, the decrease in capital goods creation appears less marked (3 per cent), pointing to the fact that, in 1972, the increase in productive

TABLE 64

STRUCTURE OF THE BALANCE SHEETS OF A GROUP OF 134 ITALIAN MANUFACTURING COMPANIES

Items	1962		1971		1972	
	billions of lire	per cent	billions of lire	per cent	billions of lire	per cent
	Predominantly state-controlled companies (9 companies)					
ASSETS						
Land, buildings and equipment (*)	727.0	*47.1*	2,594.0	*63.5*	3,084.4	*65.2*
Inventories	208.7	*13.5*	538.6	*13.2*	621.7	*13.1*
Long-term financial assets	214.3	*13.9*	364.5	*8.9*	357.5	*7.6*
Receivables	330.7	*21.4*	574.8	*14.0*	640.9	*13.6*
Cash and credits to banks	63.5	*4.1*	15.5	*0.4*	24.0	*0.5*
Total assets	1,544.2	*100.0*	4,087.4	*100.0*	4,728.5	*100.0*
LIABILITIES						
Share capital	446.4	*28.9*	549.2	*13.4*	548.8	*11.6*
Reserves	175.8	*11.4*	87.1	*2.1*	49.3	*1.0*
Retirement funds	40.9	*2.6*	144.6	*3.6*	177.1	*3.8*
Medium- and long-term debts	471.0	*30.5*	1,925.8	*47.1*	2,452.1	*51.9*
bonds	6.0	*0.4*	3.1	—	2.7	—
Payables	225.5	*14.6*	619.6	*15.2*	748.2	*15.8*
Debts to banks	156.0	*10.1*	760.9	*18.6*	752.8	*15.9*
Net profit	28.6	*1.9*	0.2	—	0.2	—
distributed	27.0	*1.7*	5.7	*0.1*	—	—
Total liabilities	1,544.2	*100.0*	4,087.4	*100.0*	4,728.5	*100.0*
	Private companies (125 companies)					
ASSETS						
Land, buildings and equipment (*)	1,798.4	*34.8*	3,213.0	*36.7*	3,380.3	*37.4*
Inventories	710.8	*13.7*	1,627.7	*18.6*	1,499.3	*16.6*
Long-term financial assets	784.4	*15.2*	1,755.7	*20.1*	1,892.0	*21.0*
Receivables	1,634.2	*31.6*	2,009.7	*23.0*	2,054.7	*22.8*
Cash and credits to banks	245.4	*4.7*	139.3	*1.6*	194.5	*2.2*
Total assets	5,173.2	*100.0*	8,745.4	*100.0*	9,020.8	*100.0*
LIABILITIES						
Share capital	1,363.2	*26.4*	1,694.6	*19.4*	1,436.6	*15.9*
Reserves	1,039.4	*20.1*	716.2	*8.2*	928.3	*10.3*
Retirement funds	287.0	*5.5*	854.4	*9.8*	953.6	*10.6*
Medium- and long-term debts	1,023.1	*19.8*	1,902.2	*21.7*	1,879.6	*20.8*
bonds	544.1	*10.5*	422.2	*4.8*	386.8	*4.3*
Payables	1,019.4	*19.7*	2,247.0	*25.7*	2,443.5	*27.1*
Debts to banks	320.2	*6.2*	1,279.3	*14.6*	1,324.6	*14.7*
Net profit	120.9	*2.3*	51.7	*0.6*	54.6	*0.6*
distributed	110.2	*2.1*	68.5	*0.8*	69.9	*0.8*
Total liabilities	5,173.2	*100.0*	8,745.4	*100.0*	9,020.8	*100.0*

(*) Net of depreciation; this adjustment was necessary in order to ensure comparison with data on the structure, which changed considerably between 1971 and 1972 also owing to the elimination of sources of income and corresponding transfers from endowment funds.

capacity did not differ much from that of the previous year, despite the slowdown in investment. However, if the enterprises are grouped according to their size, it appears that, whereas the large public and private enterprises' capital stock increased by about the same amount (1,067 billion, versus 1,074 in 1971), that of the smaller-sized companies in the sample decreased (111 compared with 140) (Table 63). This fact shows that the large enterprises are still going ahead with the process of industrial concentration, not only by taking over small-sized enterprises but also by directly expanding their productive capacity. With regard to this, the phenomenon of purchases of majority interests by the large private companies seems to have slowed down considerably; their investments in long-term financial assets dropped by over one-fifth compared with 1971. The improved economic outlook may have had some impact on the phenomenon, on one hand, by making takeovers less convenient and more difficult for the enterprises and, on the other, by reducing the need for companies to diversify risks by investing in sectors of activity other than their own.

TABLE 65

GROSS AND NET PROFITS IN A GROUP OF 134 ITALIAN MANUFACTURING COMPANIES

(billions of lire)

Years	Net profits and increase in net worth	Amortization	Increase in retirement funds	Profits	
				gross	net
	(1)	(2)	(3)	(4)=(1)+(2)+(3)	(5)=(4)−(2)
1963	112.4	320.3	71.8	504.5	184.2
1964	120.7	339.5	46.6	506.8	167.3
1965	141.9	360.9	57.6	560.4	199.5
1966	159.4	411.6	49.8	620.8	209.2
1967	161.3	419.1	51.8	632.2	213.1
1968	184.8	478.0	46.8	709.6	231.6
1969	121.2	522.5	95.2	738.9	216.4
1970	25.7	567.9	138.1	731.7	163.8
1971	− 202.2	581.1	113.5	492.4	− 88.7
1972	− 204.8	641.4	131.8	568.4	− 73.0

Financing needs, resulting from the above-mentioned performance of investments in fixed capital and financial assets, were covered by the state-controlled enterprises, the large private and small-sized companies with funds other than those raised through indebtedness (self-financing, fund raising through shares and repayment of ENEL credit) for 33, 77 and 83 per cent respectively (21, 33 and 64 per cent in 1971). With regard to the remaining demand for funds, this was entirely covered by the public and small-sized enterprises through recourse to medium- and long-term indebtedness, whereas the large private companies financed only 4 per cent of long-term real and financial investments by this method (Table 63). This category of companies covered the spread between formation of fixed assets and long-term liabilities with funds raised through end-year sales of large quantities of finished products, exceptionally heavy in some sectors, in connection with the changeover from turnover tax to VAT. The different self-financing methods of the public and private enterprises can, in the first place, be attributed to structural differences but also, to a certain extent, to cyclical behaviour.

The state-controlled enterprises' borrowing from the special credit institutions was as extraordinarily high as in 1971. Besides the greater propensity they show to finance their needs through indebtedness, this instrument responds to their need to integrate the amount of self-financing, which is very low compared with investments, with funds having the same availability feature as long-term assets.

For the private enterprises, especially the small-sized ones, financial requirements were covered mainly through internal saving and shares in an attempt to improve the firms' capital structure, which is appreciably unbalanced on the debit side, in order to take advantage of better conditions for acquiring financial resources. This company restructuring process is parallel to the moves made by the firms on the asset side to rid themselves of economically obsolete productive facilities, and its success basically depends on the availability of risk capital. In 1972, the private enterprises almost tripled the amount of funds obtained by this method compared with the previous year, and used about half the amount to rebuild equity capital which had been eaten away by losses. Thus, these companies managed to keep their ratio of debts to total liabilities (excluding retirement funds) practically unchanged at around the 63 per cent mark, whereas the public enterprises, having issued no shares, allowed it to increase from 81 to 84 per cent.

The adjustment of productive structures to market conditions, which was fostered by the restructuring of the enterprises over the last three years, and the revival of demand in the last part of the year helped halt the shrinking of profit margins and to increase earnings volume. In fact, gross earnings per unit of capital rose slightly from 5 to 5.2 per cent, whereas overall earnings increased by about 15 per cent (Table 65). There was also an improvement in net operating results for the year; nonetheless this only showed up in a tightening of losses (88 billion on 1971 and 73 in 1972). Consequently, in 1972 also, it was decided to partly tap reserves in order to distribute dividends.

In the present economic situation, characterized by symptoms of recovery, such a policy of defending dividends may be considered a valid method for fostering the enterprises' growth, insofar as it expresses the entrepreneurs' optimistic expectations and, therefore, may pave the way for future mobilization of risk capital, an instrument more necessary than in the past to remove the financial hurdles to development.

III. – THE GOVERNOR'S CONCLUDING REMARKS

The Evolution of the International Monetary System

The period since the last Annual Meeting has been dominated by monetary events, both within countries and in their external relations. Domestic and international monetary developments are irreducibly linked: had there been more orderly monetary management in the main industrial countries at least, there would be less urgency to reform the system erected in the postwar period, which was based upon fixed parities changeable only in situations of fundamental disequilibrium.

The Washington agreement of December 1971 represented, under certain aspects, progress towards choosing the pattern for building a monetary order.

The realignment of exchange rates involved all currencies, including the dollar. Hence it represented a move towards a more symmetrical system than the one devised at Bretton Woods which bestowed upon the dollar the special role of bridge-currency for the conversion into gold of all the other convertible currencies. However, the measures taken in August 1971, which cut the link between the dollar and gold, also formally weakened the technical justifications for the asymmetry on the basis of which the authorities of the convertible-currency countries were hitherto required to defend their own exchange rates vis-à-vis the dollar, whereas the US authorities were under no such obligation. After August 1971, special treatment for the dollar could only be based upon its still dominant position on the international money and capital markets. Nonetheless, even this position has been undermined by fears of devaluation, which have twice proved to be founded, while the US authorities have kept the dollar inconvertible both in terms of gold and of other reserve instruments.

The desire for greater symmetry in international monetary relations is an outgrowth of the gradual trend towards the creation of large areas of comparable economic and commercial weight: the European

Economic Community's foreign trade, excluding intra-Community commerce which should be considered internal trade — if related settlements were made in Community-created monetary instruments — exceeds that of the United States. Japan trails somewhat behind; nonetheless it must be classed among those countries, or groups of countries, which together dominate the world economy.

A further outcome of the Smithsonian agreement was substantial recognition that the determination of exchange rates, especially for the main industrial countries, is not by its nature a unilateral question, or even a bilateral one. The multilateral negotiations were arduous. But they demonstrated that, despite conflicts of interest among actual or evolving monetary areas and the deep-rooted persistence of mercantilistic instincts, there exists an underlying solidarity among those in charge of running the world economy. This solidarity was further demonstrated last March at the ministerial meeting of the Group of Ten in Paris and of the Committee of Twenty held in Washington. It is grounded in the awareness of the common interest in the smooth working of the international monetary system, in an era in which technology and integration in manifold forms have assured that the goods, services and ideas coming from the rest of the world play an important role in our individual and collective lives. This awareness, rather than any change in the mechanism and in the agreements governing them, differentiates the present situation from the one that characterized the period between the two world wars.

Finally the change in the dollar's parity, for the first time in little less than 40 years, and hence not since that currency had been made the support of the international monetary system founded at Bretton Woods, opened the way for the United States to be able to use the exchange rate as a variable in the adjustment process. This tended to eliminate another of the system's asymmetries: an asymmetry, in this case, unfavourable to the reserve currency country. The variation in the dollar's parity and, to different extents, in the parities of the currencies of the other main industrial countries was another indication of the trend, which appeared some years ago, to have exchange rate changes play a wider role in achieving and maintaining domestic and external equilibrium.

All parties involved in negotiations for the reform of the international monetary system are agreed that it is necessary to modify the way in which the Bretton Woods agreements have been applied concerning parity changes. At last March's meeting agreement was reached on the *fixed but adjustable parities* formula. In the meantime, however, market developments have forced many countries to resort to a type of flexibility that tends to blur the concept of parity.

Indeed, in December 1971 the United States announced a new parity for the dollar, but not its convertibility; nor a commitment to defend the new parity on exchange markets. Hence, we asked last year just what was « the economic logic linking the declaration of official parity of the dollar and declaration of the parities of the other currencies » and expressed our doubts on the possibility, under the circumstances, of defending such a system from the consequences of flows of unwanted funds. Over the last twelve months, the majority of Western European countries, inside and outside the EEC, have had to resort to floating in a form which is for some global, for others partial. The intensity with which funds have left, or poured first into one country and then into another, has not, in fact, made possible any other choice. The rise in intensity has been matched by the frequency with which those massive shifts of funds have taken place, as businessmen everywhere attempted to ward off losses, or profit, from expected parity changes in the currencies considered, in turn, the weakest or strongest links in the chain.

The weakening of the notion of parity was heralded by the introduction of the concept of *central rate.* The new exchange rate structure set up in December 1971 did not bring about the improvement in the US balance of payments that might have restored confidence in the dollar's new parity. The mercantilistic attitudes still underlying international economic relations prevented exchange rates from being adjusted to the necessary degree. Moreover, the initial stage, during which devaluation tends to produce perverse effects on the current account balance, appears to have become longer. The speedier recovery of the US economy also added to the negative impact on the balance of payments.

The task of defending parities has generally become more difficult due to the weaker effectiveness of policies aimed at keeping an appropriate ratio between domestic prices and the average of prices in the countries most active in world trade. In the Western World, today, prices and costs only partially respond to changes in the equilibrium between supply and demand of goods and productive factors that can be obtained over the short run by using conventional instruments — including monetary ones — to regulate demand, while still avoiding unacceptably high social costs. To a constantly growing extent cost and price trends depend upon the behaviour of organized social groups, which determine them largely independently of supply and demand conditions.

In a situation such as this, parities, even when representing an equilibrium position at the outset, tend to become rapidly obsolete. If they are not promptly adjusted, exchange rates tend, in fact, to break away from parities under the pressure of swift and massive flows of funds.

The dichotomy that has been a feature of monetary and credit regulations in the majority of the European countries, with regard to the domestic and international market, has given rise to what can be ultimately considered as a market monetary power endowed, so to speak, with extraterritoriality. The Eurodollar and other Eurocurrency markets, thriving upon a lack of controls similar to those regulating banking activities on domestic markets, upon the economies of scale which its international dimension makes possible, and upon the professional talent which growth and profit potentials have attracted within its sphere, has seen its initially marginal impact develop in the span of a few years into an influence matching and competing with the one exerted by the national monetary authorities on their own markets. This is especially so in Europe, where the regulation of monetary base and credit is fragmented into so many domestic policies which are supposed to be autonomous.

The existence on the Euromarket of dollar-denominated financial resources without their corresponding counterpart in the United States has led to their being attracted into official reserves. This has been possible because of the size of the reservoir from which they flow and because of the convertibility commitment of the currencies with declared exchange rates.

Unless we assume an abdication on the part of the monetary authorities, the power to create money and credit will also have to be regulated in those sectors which have grown up as outposts of the movement towards integrating national banking and financial systems. This is not a simple task, but the challenge will have to be taken up.

We should not fall, however, into the trap of believing that the stability of the international monetary system can be secured simply through the creation of a panoply of controls on international capital movements. We shall discuss this topic later on in these concluding remarks, but it should be stressed at this point that the integration of economies, the spread of technological progress, the attainment of economies of scale, in those production sectors where they are crucial, can be crippled by restricting the circulation of capital; keeping in mind that financial flows do not always ensure the expected effects of rationalizing production. Nor should it be forgotten that exchange control generally starts with capital movements, but tends to spread its grip to the flow of goods and services. Controls on foreign currency settlements, that have proliferated over the last few years for financial transactions, have recently touched the trade sector.

If in most countries inflation is eroding at confidence in the currency from within, it is illusory to hope that confidence will be restored in an international currency, which constitutes at the level of official and private operations the necessary corollary to a system built around fixed exchange rates. The system set up at Bretton Woods rested upon the assumption that monetary stability would be safeguarded in the largest economy and that this, in turn, would be transmitted to the rest of the world since, as a condition for exporting and importing, the other industrial countries would be forced to compete with the largest economy in efficiency and price stability.

The need for reforming the system became compelling as the redistribution of economic power moulded the international economy into a more balanced, polycentric-type shape. The need was felt because the European economies, once again capable of independent cyclical behaviour, could not — without damaging the growth process and deviating from the order of socio-economic priorities accepted in Europe — remain unsheltered from the influence of a US monetary policy meant to cater in the first place for American requirements. In addition, the growing depreciation of the dollar in terms of buying power made it too costly to hold reserves of liquidity in the form of monetary assets on the United States, on the part of countries already possessing large reserves in that currency. Thus resistance towards building up these reserves stiffened, especially whenever fresh additions were linked to US investments abroad at a moment when the technological gap seems to have shrunk.

The restoration of orderly and stable monetary conditions, a prerequisite to a smooth-functioning international monetary system, has been hampered in Europe by the massive flows of dollars inundating those countries which have pursued more stringent monetary and credit policies. Shifts of dollar liquidity hamper stabilization policies, even when the United States itself is not experiencing inflation. In a system built around large monetary areas, the importance of the country with the highest propensity for stability grows, since the impulses being transmitted by the economy which from the point of view of overall real and financial resources continues to dominate, are not focused on the *target country,* but are diluted across the entire group of the countries forming each monetary area.

Experience over these last few years has taught that, in practice, recourse by a single country to technical instruments such as flexible foreign exchange rates, exhausts its usefulness long before the country has succeeded in sheltering its economic and monetary policy from the inflows of liquidity in dollars. Since nearly 50 per cent of the foreign trade of EEC countries is intra-Community trade, no single member can make an appreciable use of exchange rate changes to solve what is essentially a monetary problem with the United States, without at the same time jeopardizing its own competitive position within the Community. Not even joint floating solves the problem, as far as concerns competition with the United States on respective domestic markets and on those of third countries. The fact that the equilibrium rate for capital movements tends to diverge from that for current account transactions makes it hard to do without administrative controls on capital flows, if only in the form of a separation of the two exchange markets. But administrative controls are less damaging in terms of inefficiency in the allocation of resources, if applied along the perimeter of a wider area.

Joint floating presupposes that the conditions within the participating economies be homogeneous. Last year we warned that fledgling Community monetary unification would succeed to the degree in which it was sheltered from the tensions rocking the international monetary system as a result of the divergencies in cyclical trends of the major industrial countries and of differences in their economic and monetary policies. We added that: « The progressive limitation of national autonomy in the areas of foreign trade, capital movements and credit policies, and, in the final analysis, of global demand policy could influence economic development favourably in some countries and regions, adversely in others ».

The European Economic Community was not able to meet in a concerted fashion that which has been called the *American monetary challenge,* because cyclical patterns in the different member countries continue to diverge; in other words, although largely integrated on the commercial level, the Community has not achieved a high enough degree of economic integration. The latter extends beyond the commercial sector, to the factors of production, the institutions in which those factors are organized in modern Western societies, the rules which promote and govern their circulation, fiscal and social security burdens, the yield on savings and investment, and income transfers. Without economic integration some countries may be damaged if they give up the autonomous use of exchange rates and other monetary policy instruments. As things stand today, it appears likely that full participation in the joint float would have pushed exchange rates in the direction suiting the needs of the nations which in effect did take part, and hence in a direction detrimental to the others.

If moving towards monetary union well in advance of economic integration can harm some countries, they will not give their consent until the Community is in a position to come up with measures designed to level the gap between the direct gainers and losers in the process of unification. The narrowing of the intra-Community fluctuation margins — which implies a reduction not only in the autonomy of interest rate policy, but also in manoeuvring room for fighting currency speculation — was accompanied by agreements making intra-Community settlements harder than the norm outside the Community. This has not been counterbalanced by the type of credit facilities that have been agreed upon, which are not even satisfactory on the strictly technical level.

Indicative of the attitude still prevalent in the Community were the reactions to proposals submitted at Brussels last March to increase the credit potential of the European Fund for Monetary Cooperation. The proposals were made in the course of negotiations which centered around renunciation of the autonomous use of exchange rates to meet primarily the needs of some member countries whose monetary equilibrium was endangered by inflows of foreign funds.

The Italian proposal to raise the Fund's resources to 10 billion units of account was a compromise between the actual situation and the British proposal for unlimited credit. It was based upon the conviction that a commitment to float jointly would stand no chance of thwarting speculation if the size of resources available to defend the joint parities was not credible.

Beyond the immediate operational considerations these negotiations were of course a testing ground for the priority which Community members are willing to give to growth and full employment, even when these goals are threatened in a country other than their own. Imbalances in payments similar to those within the Community crop up within the single countries. In the latter there exists monetary and fiscal mechanisms which make it possible to stretch the adjustment process over a longer period of time. The nearly total lack of these mechanisms in the Community context makes that process abrupt, exacerbating it until it exacts large sacrifices in terms of priorities among the objectives of economic policy. If at present the fight against inflation seems to be of utmost priority, European monetary union cannot nonetheless pivot around a mechanism which tends to place the goals of growth and full employment at the bottom or, in other words, to overturn a value system that has received nearly universal acceptance in the postwar period.

The International Monetary Crisis and the Floating of the Lira

Our policy choices during 1972 and the beginning of 1973 were shaped by the criterion of keeping the balance-of-payments constraint from hampering the pursuit of a policy of money management aimed essentially at stimulating a recovery in productive activity and employment, without undermining the forward momentum of European economic integration.

As 1972 opened, the low degree of plant utilization and the stagnant behaviour of unit and overall profits, on the heels of 1971's particularly unsatisfactory performance, discouraged fresh undertakings. Construction activity continued to flag at low levels, even if the first signs of a slight recovery could be noted. The public administration was unable to promote the expansion of demand proposed by government policymakers; activity in the public works sector slowed down, even while outlays were rising. Exports continued to represent the most dynamic component of overall demand, but their expansion was faltering, after the 1971 year-end spurt.

The depressed economic situation kept price increases within more moderate bounds than those being experienced in the other European countries, which had already turned the corner towards vigorous recovery. The climb in wholesale prices, which between December and June moved at a 4 per cent annual pace, was for the most part spurred by pressures from abroad, such as hefty jumps in raw materials and beef quotations. The growth rate of manufactured goods prices continued to lag behind that for costs per unit of output — thus heightening the inflationary potential building up within the system.

In the January-May period, our balance of payments was showing particularly favourable results — especially because of the increase in the current account surplus — thus making feasible the policy of prepaying loans taken out in the previous two years: in these five months repayments amounted to 260 billion lire and the other items on the balance of payments showed a surplus of 160. Under these conditions monetary policy was kept on the previous year's expansive track, moving, rather, towards an acceleration of the most directly controlled components in respect to the second half of 1971. Seasonally adjusted, the creation of monetary base, channelled for the most part through the financing of the Treasury's cash needs, came to nearly 2,500 billion in the first six months of 1972, against some 3,300 for all of 1971; bank reserves, again for the first six months of 1972, rose by nearly 1,300 billion, only slightly less than over the entire arc of the preceding year.

The sharp expansion of the Banca d'Italia's *other assets* gradually led, during 1971, to an increase in the banks' unused borrowing margin in ordinary advance accounts as a result of the repayment of funds previously borrowed from these accounts and, later, to the accumulation of deposits with the Central Bank. These accounts stayed at a high level in the early months of 1972. In April it was decided to lower the return paid on them, linking this decision with a reduction of 0.50 per cent in the discount and advance rates, in order to foster greater use of the banks' excess reserves and stimulate a faster decline in interest rates.

The banking system reacted as hoped, increasing its credit lines and securities investments and fostering a further lowering of the entire interest rate structure. The level of lending rates in the second quarter of 1972 settled 0.70 per cent lower than that of the fourth quarter of the previous year.

Given the volume of outstanding loans, it can be calculated that every percentage point the lending rate falls means nearly 100 billion in per-quarter savings for borrowers. Every type of loan was affected by the reduction in rates but, as already noted in 1971, the cut-back was lower for the small- and medium-sized enterprises and larger for the public enterprises and, more generally, for large enterprises.

In the first six months of 1972 the overall flow of domestic financing to all sectors of the economy, excluding the Treasury, was some 3,600 billion, versus 2,400 for the same half in 1971.

Bank loans, or nearly 80 per cent of the total, registered a faster rise for operations in favour of enterprises and agencies located in Southern Italy and the islands (5.5 per cent increase versus 3.4 per cent for the other regions).

In the month of June the international monetary system was rocked by a deep crisis. A string of unfavourable news on the performance of the United Kingdom's balance of payments and the restatement of the British government's policy to give priority to domestic development targets fed expectations of an imminent devaluation of the pound. This set off massive flows of funds both through leads and lags in exports and imports, and the conversion of foreign-owned, pound-denominated deposits. After a brief shutdown of the foreign exchange markets, the British government announced its decision to float the pound sterling.

Despite the fact that Italy's reserve and balance-of-payments situation appeared solid at the end of June, expectations of further rises in costs and prices bolstered the conviction that sooner or later the lira would follow in the pound sterling's footsteps. The upshot was a round of speculative attacks against our currency, which forced the Banca d'Italia to sell more than 900 billion lire on foreign currency exchange markets during June and July, nearly a third of this in the last three days of June.

At the end of that month, measures were taken aimed at curbing certain forms of outflows and at curtailing their impact on reserves, through the acquisition of liquid financial resources denominated in other currencies. More specifically:

— the facility of crediting lira bank notes in capital accounts was discontinued and at the same time the policy of encouraging foreign indebtedness was reactivated; as a result foreign currency loans for circa 500 billion lire were contracted in June-July and another 400-worth were taken out before the end of the year;

— there was no relaxation of the ban on the banks' taking on net creditor positions abroad while instead they were given the go-ahead to assume net debtor positions vis-à-vis the same sector;

— the banks were instructed to keep their overall foreign exchange position balanced, through the repayment of outstanding dollar-lira swaps with the UIC — this latter measure fostered the reflow into reserves of those dollars acquired by Italian businessmen to repay foreign-currency loans taken out with the commercial banks; in the June-December period these loans fell off by 1,150 billion and repayments made to the UIC amounted to 1,161 billion.

The uncertain international monetary situation and rising demand in many industrial countries were reflected in the behaviour of prices for raw materials and foodstuffs. This worked its way into domestic prices, sharpening the difficulties already appearing in the wake of a bad agricultural year. The economic situation in Italy continued to stagnate, even if there seemed to be a turnaround in investments, especially in inventory building, as indicated by an acceleration of imports. Monetary policy was kept on an expansive tack, even if liquidity inflow from abroad completely fell away.

Overall domestic financing of the economy, excluding the Treasury, came to 12,500 billion in 1972, against circa 9,000 in the previous year; the portion going to the public sector and the public enterprises increased faster than the total. Outlays to the Southern regions and the islands rose by 19.6 per cent, versus 16.9 per cent for the other regions. Bank lending rates continued to fall, albeit more slowly, in the second half of the year, finishing on average for the year 1.15 percentage points below the previous year's level. In the closing part of 1972, with credit still widely available, the acceleration of exports, and vigorous stockbuilding activity and consumption — spurred by pension increases and the impending switchover to VAT — gave a decisive lift to productive activity. Company profits improved and there were clear signs of recovery in investments. In the construction sector the turnaround in non-residential building in progress since the beginning of the year was joined by a still uncertain, but improved, performance in home-building.

Industrial output registered, between the third and fourth quarter, the exceptional jump of 7 per cent, generating a sharp recovery in productivity, and provided a respite in the steady growth of unit labour costs. However, improved demand conditions, against an international background of expanding inflation, spurred the spread of price rises to manufactured goods, which, while demand was stagnating, had been lagging behind cost increases. Further pushes originated from raw material quotations, already soaring on world markets. In addition there were increases connected with the imminent changeover of the tax system.

Though it had survived the violent crisis of June-July, the lira continued to be attacked throughout nearly all of the second half of 1972 by domestically generated speculative pressures. These were veiled by the usual summer inflow of foreign currency, which made interventions on foreign exchange markets unnecessary. The telltale signs were the speed in which imports were settled and especially the delay in the settlement of exports: the loss of reserves stemming from this behaviour can be set in the seven months between June and December 1972, at some 850 billion lire. At first the authorities took compensatory steps by contracting loans abroad; later, that is in January 1973, when it seemed wise to curtail the further expansion of these loans, they decided to shorten the terms of payment for foreign trade in order to restrict the creation of export credit.

Thus moves aimed at defending the quantity of our reserves were integrated with others shielding their quality.

According to the agreements put into force on April 24, 1972, interventions to keep the spread between the exchange rates of any two Community currencies from exceeding 2.25 per cent were to be carried out in Community currencies; interventions in dollars only being permitted when that currency's exchange rate reaches its outer limits. These same agreements also stated that eventual debtor positions growing out of interventions in Community currencies were to be settled through the proportional use of all of the debtor country's reserve instruments; the ongoing market price applying for currencies and the official one for gold.

Conforming to these rules would have forced our country to continuously relinquish gold at a price growing ever more out of line with the free market quotation, and made it practically impossible to recoup these gold losses should the balance-of-payments situation turn around: we would thus have had to suffer an unjustified drain, while other countries would have received an unjustified gain.

In order that the lira might be kept within the agreed-upon Community band the agreement was modified at the end of June. We were then permitted to intervene exclusively in dollars, an eventuality which had been expressly anticipated in the agreements. In this way our reserve losses in the June-December period, of 318 billion lire, were strictly in dollar-denominated assets.

Throughout all of the second half, the lira hovered close to the floor of the Community band; the strongest Community currencies having all risen to the maximum appreciation permitted vis-à-vis the dollar. This meant that our country was forced to maintain its exchange rate vis-à-vis the dollar close to its central rate, in a period in which the balance of payments was registering a substantial deficit. In the autumn, speculative pressures against the lira stiffened: as the leads and lags for trade settlements widened, there was an increase in capital outflows earmarked for securities investments. Capital flows, after deducting trade credits, offsetting loans and banknote remittances, are usually in surplus in Italy; instead they registered a deficit of 230 billion in the third quarter of 1972 and one of 130 in the last.

In the fourth quarter interventions on the foreign exchange spot market accelerated and at the same time interventions were also made on the forward market, in order to keep the spread in spot and forward rates from sparking off further capital outflows. Further measures aimed at fortifying the foreign exchange market were taken at the beginning of December; while the interest rate on fixed-maturity advances was increased the UIC declared itself ready to provide a portion of the lire which the banks needed for their end-of-the-year operations, against dollar sales, with exchange guarantees. As a result the UIC's creditor position for forward dollars turned around to a short position of nearly 350 billion lire.

As the year came to a close, the seasonally adjusted Italian balance of payments, despite the recovery of exports in course, showed a deficit on current account. This reflected a speed-up of raw material and semi-finished purchases at steadily rising prices, and the reduction of net receipts for services, while the net capital outflow was expanding and only being partially offset by recourse to foreign loans. Interest rate conditions played no part in stimulating these outflows. Net of the surcharge levied against non-residents, our long-term rates were above those on the Euromarket, in France, West Germany, the United Kingdom and in the other major countries. A negative spread did open up in autumn in respect to short-term rates in West Germany and the United Kingdom, but not so wide as to spark off large movements of funds. The key stimulant was expectations of devaluation, reflected in the discount on forward lira. The latter was narrowed by the interventions mentioned above: had these interventions been carried out by the commercial banks, they would have lopped off reserves.

Correcting the disequilibrium by adjusting domestic interest rates seemed an unwise course, as any adjustment would have had to be so large that it would have had a disruptive influence on the financial system. But basic to any decision against recourse to monetary measures was the state of the economy; a rollback in credit would have throttled the recovery just as it was getting under way.

Against this backdrop it was decided to set up a two-tier exchange rate. In the Report given in May 1970 we had already expounded on the advantages and disadvantages of such a solution. At the time we stated that the establishing of a financial lira would have resulted effective « insofar as the divergencies in prices between the official market and the financial market » ... were « restricted by intervention by the authorities and thus, ultimately, by sales of foreign currency taken from the reserves ». As it happened the spread between rates on the two markets was kept in bounds, without the need to intervene, by the decision in February to allow the commercial lira to float. Nonetheless, the establishment of the two-tier market provides no protection against changes in the terms of payment on the part of foreign traders.

In March of 1969 repeated proposals were made insisting that the flight of capital from Italy could be blocked by suspending the purchase of bank notes abroad by the UIC. On that occasion I stated « it is necessary to warn that any such measure will be ineffective in a country in which inflows from foreign tourists and remittances from workers abroad amount to some two and a half billion dollars per year. It seems plain that the foreign currency saved by not repurchasing bank notes will be offset by the reduced inflow of currency imported by tourists, who will purchase their bank notes abroad and refrain from exchanging their own currency on the official market. The same behaviour can be expected of Italian workers abroad and this would respond above all to their right to a fair deal. Nor would it be worthwhile to station an arrayment of special police along the border to carry out personal searches on foreigners coming to visit our country ».

Events have clearly borne out these predictions: the total of net receipts from tourism and emigrants' remittances slid from 330 billion in the final quarter of 1971 to 213 in the same period of 1972; considering the upward momentum of these flows in the first half of the year, it can be estimated that this phenomenon sapped some 150 billion lire from the balance of payments. It is possible that these measures did produce a modicum of desired results, but to a much lower measure than reported statistically.

The series of monetary flair-ups in February and March of this year must be laid squarely to the size of flows of funds spurred by expectations of parity changes. The size of reserve losses suffered by Italy during January and the first part of February, notwithstanding the ban on crediting bank notes and the establishment of the two-tier market, ruled out any solution that would entail a further draining of reserves. In the light of a deficit in the balance of payments on current account, it would not have been feasible to keep the lira's value vis-à-vis the other European currencies unaltered and accept the constraint of limiting its fluctuation to no more than 2.25 per cent of their respective parities. Acceptance of that constraint would have been possible had the embryonic European Fund for Monetary Cooperation been equipped with the financial resources necessary to convince the market that eventual reserve losses would not, sooner or later, lead to a parity change.

The decisions of February and March gave rise to bitter criticism; it was charged that it was merely a ploy masking an actual devaluation of the lira. Another oft-repeated argument was that it would have caused Italy to break loose from its European moorings.

As to the first of these two accusations, it should be recalled that arriving at the new level in exchange rates while the authorities were making defensive interventions precludes any willingness on their part to cause a depreciation. To keep the old level would have entailed higher reserve losses. These losses would have led to a decision to devalue, without sufficient reserves to contain the size of the change.

Non-participation in the joint European float does not seem liable to the interpretation that it caused a break between Italy and Europe; if anything just the opposite is true: our currency was suddenly affected by shortcomings in international and domestic behaviour, the latter cutting across every social group and fostered by the policies carried out over past years. As a result, the process of integrating our economy in the Community has been slowed.

I called that behaviour and its consequences to the attention of the monetary authorities towards the middle of January 1972; at that time I wrote: « The international monetary situation is in unstable equilibrium; it is likely that the restructuring process will lead to the establishment of monetary areas; one of these would revolve around the enlarged European Economic Community. The acceleration of integration within this area will force the member countries to move more quickly towards homogeneous economic structures. Do the transformations we have recently achieved and those on slate support the conviction that our economy is able to make this evolutionary transition? Are not symptoms appearing that might lead to the opposite conclusion? And that is to say of its gradual drift away from the European Community? »

We had better, however, take sides on one or the other interpretation of the difficulties lying before us, and make it plain once and for all if it is our belief that the remedy lies in speeding up the process of merging economic activities into a state or quasi-state apparatus ever less mindful of the restraints necessarily respected by the managers of private enterprises that survive on their efficiency, and that all problems can be solved by the money printers, provided that they are willing to obey the command to ceaselessly crank their presses. If this is really the case, however, we cannot pretend that the majority of citizens should take seriously the repeated declarations promising to keep a solid link between our economy and those of the rest of the Western World.

The Enterprises within the Framework of Economic Integration

All of the Western economies are presently undergoing thorough transformations which have also touched upon labour relations and the distribution system, but none have deviated from a market economy. The founding treaty of the European Economic Community explicitly states that it shall pursue its own goals in the establishment of a common market, thereby implying rules revolving around the enterprise. These rules presuppose the existence of private and public enterprises, managed autonomously and operating on an equal basis.

A hostile attitude, sometimes masked sometimes not, towards private enterprises has taken root in our country over the years and a preference for public enterprises had even entered into the law books: for instance, the law of October 22, 1971 n. 685, art. 27, paragraph 6 reads like this: « The Municipality shall use the expropriated areas for the construction of productive facilities for industrial, handicraft, commercial or tourism purposes » and the paragraph goes on « should competing claims be made, preference shall be given to those presented by public agencies and state-controlled companies ».

The rules governing labour relations in private employment have been brought into line with those governing public employment with the aim of guaranteeing job security. The private enterprises are presently threatened with a generous law in favour of war veterans, that also covers other categories suffering war damages, which hitherto has been restricted to the employees of public agencies, including municipal workers. This law brings about a situation in which the private owner is not able to make overhead projections and is ever more tempted to give in to takeover offers by a larger firm or a public agency.

The employees greet this transfer from the private to the public sector with little remorse, yearning to become members of a privileged community. The process is monotonously one way; not once has it happened that a municipally-run company that goes out of business because of accumulated liabilities, even in a field where it has no monopoly, ever had its service returned to a private enterprise.

The widening of the public sector is detrimental to the process of management recruitment: the circle of eligible citizens tends to shrink around the members of the political parties in power thereby fostering a bureaucratic corps of managers, with little zeal for innovation. The expansion of public enterprise tends in the long run to award those groups which can most easily influence the executive branch.

It does not seem haphazard to state that the public sector's action has been geared more towards extending its reach than towards improving the administration of those sectors already under its control. This has inserted an element of instability in the institutional framework which I believe has had a negative impact on the process of capital accumulation. When the Italian market was first opened to foreign competition, that process was stimulated and there was a sharp rise in investments. In the ensuing years the private enterprises' fears for their own survival may have convinced them of the wisdom of limiting their investment activities to reorganization programmes, before full employment had been reached. Supply has expanded basically through increases in productivity, mainly in the manufacturing industries. Consequently the system has not grown as fast as it might have.

Capital that might have gone into domestic investment has instead been exported. Had we tried to promote more vigorous investment in real assets, depressing the yield on financial assets through the expansion of liquidity, the result most likely would have been a larger exodus of funds towards foreign financial assets. Below-par domestic investment, a surplus in the balance of payments on current account, and the outflow of capital are all phases of a vicious circle experienced by an economy which is open to the international market, but has a different organizational structure.

The public enterprise has unquestionably proved itself a potent development instrument in the Mezzogiorno; the same has been and can be true when it comes to accomplishing fundamental aims both in the infrastructure and the basic industry sectors, and providing operational guidelines to other industrial sectors as well. But expanding the public enterprises field of action through interventions aimed chiefly at proffering a lifeline to floundering firms but not responding to a coherent economic policy design, leads to the degeneration of public and private enterpreneurship and slams shut the door to European integration.

Without efficient enterprises, the dismantling of economic borders produces an asymmetry of effects, since the penetration of foreign enterprises is not matched by a similar movement in the other direction. The resulting imbalance sets off a reaction which in the long run boils down to an attempt to use the arm of public industry as a hedge against the feared expansion of foreign industry.

To avoid that the gradual transference of management responsability to the public sector and that hardships being experienced by the private enterprises (which are partially at the bottom of this process) do not combine to drive a wedge between our country and Europe; we must urge the aid of European forces for undertakings aimed at solving our structural problems. Parallely, we must clear the way by speeding up the adjustment process for our institutions. In addition we must eliminate those hurdles regarding the joint stock company and the stock market which make it comparatively more difficult in our country to finance enterprises, for the households to profitably invest their savings and to implement an economic plan which, dictated by basic choices, guarantees the free exercise of entrepreneural decision-making. In direct contrast with this policy is the oft-deplored dearth of public action in its most directly pertinent sphere, from environmental protection to education, from professional training to assistance and the other basic social services.

In the autumn of 1969 trade union pressure, after having been applied during contract negotiations for the usual matters, such as the improvement of wages and reduction of the working week, shifted, on the factory level, to those aspects most closely linked to on-the-job working conditions and, on the national level, to those problems of general interest concerning the betterment of the labourer's general standard of living. Relations inside the factory broke down against the combination of demands and the ensuing methods of struggle, reflecting states of mind uneager to evolve toward constructive goals.

From mid-1970 on, a clear pattern could be discerned in which the wave of claims, which initially might have appeared similar to those produced in 1962-1963, now had shifted its focus towards sweeping social changes. The demands were often confused, but rarely lacking in appeal. Their scope went beyond the redistribution of income and reflected the need for radical innovation. Development clogged against the bars that were thrown up in front of productive activity.

It grew harder to overcome the crisis inasmuch as its solution seemed linked, both on the factory level and on that of the system, to the re-establishment of relationships which could no longer be resolved in a return to past normalcy, but the outcome of the quest for a new one. The task would not be an easy one, since neither the problems nor the solutions were clearly defined and there would inevitably be collisions not only of interests, but of ideological viewpoints.

The structure of the enterprises was strained both on the economico-financial and on the organizational level. The fall-off in profits, that began towards the end of 1969 in terms of units of output, reached exceptional lows in 1971 also in terms of overall volume. The most hardhit categories, as emerges from a survey taken of the balance sheets of 423 manufacturing companies with a net worth of at least 1 billion lire, were first the state-controlled companies and, among the privately owned, the smallest and largest companies.

The impact of declining profits on the private enterprises' investment programmes varied in intensity. Already in 1971 the smaller companies, also on account of their greater financial difficulties, were forced to sharply cut back their investment projects, while the larger ones slowed down theirs — which, nonetheless remained positive —

gearing them chiefly towards retooling company structures to the situation created by the increase in wage costs and by the changes that had taken place in labour relations. Indicative of this behaviour was the growing tendency on the part of the large firms to slough off facilities that had become economically obsolete. The value of these operations, expressed in book-keeping terms, doubled in 1970 and tripled in 1971 in respect to the 100 billion registered in 1969. A similar pattern did not occur in the state-controlled companies, since they had already taken steps along these lines during the recession of 1964-1965. In 1972 the phenomenon seems to have decelerated to a level some 25 per cent below that of the previous year, thus indicating a trend towards normalization in enterprise management.

The process of restructuring the productive apparatus was accompanied by parallel behaviour in the financial field. The recovery in share-issuing on the part of the Italian companies can in fact be linked to their need to restore financial equilibrium, in order to clear the way for the implementation of development programmes.

In 1972 the investments of the entire industrial sector, which in 1971 according to recently released data had still shown a slight increase, dropped at constant prices by 3 per cent. The anticyclical action of the state-controlled companies was not sufficient to offset completely the decline in investments on the part of the private enterprises, despite the broad support given to industrial investments by the special credit institutions which, bolstered by a monetary policy geared to fostering intermediary activities, were able to satisfy to a considerable extent the backlog of loan requests.

The effects of the enterprises' different investment performances began to be felt already during 1972. Capital accumulation — which had been vigorous for the state-controlled companies and still fairly active for the large private concerns — fostered a rise in productivity, both directly and indirectly through the reorganization of the productive process leading to labour savings.

Adjustment in employment levels, hardly noticeable in the prior year, was more marked in 1972, as the enterprises two-pronged actions to improve the productive efficiency of their facilities and more rationally organize the factors of production worked their effects. In addition, numerous small business failures also took their toll on the employment level.

In the early months of 1972, achievement, albeit partial, of the above aims helped to curtail the increase of manpower costs per unit of output. In the second half, the first hints of perking demand and price rises fostered an increase in unit and overall profits. From national accounts data it can be estimated that there was a turnaround in the enterprises' net savings after the previous year's drop; the 9 per cent growth of incomes in the industrial sector (excluding those earned by employees) supports this assumption.

Looming on the horizon together with these signs of improvement were contract renewals involving more than three million industrial employees. The importance that is attached to both the way in which the new contracts were negotiated, and to their contents, seems justified when we consider that they occur within a wage reality which, in the last decade, has gradually approached the European average, almost fully matching it in terms of labour cost. Whereas in 1960 in the manufacturing sector the latter was nearly 25 per cent less in Italy than the average for the other countries, the United Kingdom included, by 1970 the gap had been substantially closed. In fact in that year it was down to 6 per cent, an average deriving from quite different situations from sector to sector: costs in the footwear and clothing industry were still appreciably below the European averages, those for foodstuffs and means of transportation were basically equal, while costs in the metallurgy sector were higher.

Rises stemming from the recently signed contracts must be weighed in this light. The chemical workers' contract put into effect immediate rises of 14 per cent in terms of contractual wages, as emerges from the official indexes, and an estimated 18 per cent in terms of labour cost for its entire span of three years, the latter necessarily approximative because of the difficulty of calculating the cost of several items. These increments are lower even if not far off those awarded by the 1969 contract, nonetheless they cannot be considered any less serious in terms of their impact on competitiveness for the reasons mentioned above. A similar conclusion may be drawn from the settlement in the mechanical engineering sector even if, given its more recent signing, its impact on the contractual wage indexes has not yet been quantified.

Without doubt, from the way in which the bargaining was accomplished and the work stoppages themselves, the trade unions demonstrated a greater representative capacity while both sides of the table displayed a more responsible attitude towards the problems relating to the enterprises' global reality; both are hopeful signs in the quest for normalcy in productive activities. The limited space dedicated in the new contracts to agreements regarding labour organization inside the factory and the postponement of this phase of factory-level bargaining inserts, however, an element of uncertainty in the planning of productive activities and above all of investment programmes. This, however, has been mitigated by the contents of several statements made by trade union leaders. Application of the new contracts aimed at coordinating factory-level bargaining with goals touching society as a whole can be accomplished only by constant cooperation between the trade unions' national headquarters and their factory councils. The fact that the latter fully represent workers' interests on the factory level does not contradict the need for coordinating each factory's demands within the framework of more general problems touching the entire working class.

A string of fresh burdens was thus thrust upon the enterprises as they were approaching a satisfactory degree of internal equilibrium, threatening consolidation of the partial recovery experienced in the final months of the year and, above all, the start of a fresh round of investments as the plants reached full capacity levels and profits began to rise. Adding to these burdens sharply contradicts the conclusions of several recently held debates from which there emerged some signs of agreement between economists and politicians approaching the problem from a different standpoint. There was agreement in recognizing the market's intermediation role in supply and demand relations and its function as an indicator of efficient combinations of the factors of production, within an institutional framework capable of offsetting oligopolistic tendencies. There was also consensus that enterprises are organizations governed by the principle of economic viability and responding to the needs of specialization and of the decentralization of the decision-making process, as also imposed by the modern productive process. Finally opinions converged upon the necessity of limiting the spread of the public area.

These considerations call for coherent behaviour, not only in terms of trade union relations. This does not only mean coming up with innovative production methods, but, more specifically, deciding where the emphasis shall be placed in the production of goods and services: leaving to market forces the fundamental choice of the composition of demand, provided that intervention by the political authorities channels these forces towards goals having the public's consensus. Should profit be considered the final objective, distortion would arise in productive activity as the supply structure dictated that of demand. This might exact costs in terms of resources waste and debasement of the social and physical environment. The concept of economic efficiency itself would become uncertain, unless we succeeded in guaranteeing the autonomy of the goals of productive activity, in respect to the activity itself. The efficiency of the entire system, in fact, derives from its capacity to fulfill requirements which, insofar as relevant to the society as a whole, transcend the immediate aims of the single productive units.

If a balance is to be struck in factory-level relations it is essential for us to direct overall demand towards fulfilling those needs whose urgency is recognized every day by wider segments of the public.

We have noted that the cost of labour in our country has nearly reached the level of our neighbours, nonetheless the same data reveal that wages remain at lower levels, the difference mainly taken up by the higher burden of social security charges on our industries. These charges, in 1969, took up 29 per cent of the overall wage bill in the Italian manufacturing industry, against 20 per cent, on average, in the other Community member countries, the United Kingdom included. This is an example of the reciprocal ties linking the economic situation and the reforms; setting one against the other, as has been often done, basically creates false dilemmas, as is generally the case when short- and long-term problems are counterposed. That is, when we are not talking about a situation in which the means for the present and overall solution of the problems themselves and thus, the need to make choices are lacking.

An example of this is the employment problem. The low employment rate for adults and the gradual decline of this rate attest to the existence of a large pool of manpower reserves over and above those officially jobless, made up of people who do not even bother looking for work when the market is depressed.

Like the potential source of energy compressed in the ice packing a glacier, exploitable only gradually as the heat melts it, these manpower reserves become actual only when demand is such as to suck them into the market and, through on-the-job training they gain enough experience to qualify as skilled workers.

The solution to the problems of unemployment and underemployment lies in regulating the cycle to keep up sustained and steady productive activity. Fast spurts of productive activity are choked quickly off by scarsities in readily available manpower and can bring about, as experience in the recent past has demonstrated, the contradictory coexistence of problems related to full employment and the under-utilization of labour.

The country's development requires a productive nucleus, whose efficiency is constantly being honed by international competition, to stimulate the entire system and provide its own determining contribution towards balancing foreign accounts.

But this does not mean that demand composition cannot, and must not, for that matter, be channelled towards meeting the needs highest on society's list of priorities and which have been repeatedly urged by the planning bodies. If the enterprises' investments must be guided by the action of the planning bodies in regard to the public and private productive system, satisfying society's more specific needs still remains the task of public expenditure. As things stand now one cannot fail to note the government's inability to implement an adequate policy of social investments in the near future, but this serious shortcoming cannot continue over the intermediate period.

Recent years' experience has demonstrated the public administration's incapacity to expand its direct investments to the degree held necessary. The weight of these investments, in respect to overall public spending, has appreciably diminished: from 10.5 per cent on average in the 1950s, to 7.8 in the following decade, and to 6.4 in the most recent years.

This trend has highly conditioned the growth of the supply of public goods and services and has thereby to a large degree helped bring about the social and economic difficulties we are presently facing; despite the fact that the expansion of public investments has been given high priority in every government programme of recent years.

Current Problems

The thoroughness with which we have analyzed the transformations that have taken place in our economy, as well as recent domestic and international monetary events, does not absolve us from our duty to examine and offer solutions to the current problems most directly interesting us as the Central Bank in the light of the far-reaching changes occurring in the international monetary system. The most crucial problem is inflation. The economies of the industrial and raw-material producing countries have been struck by an inflationary storm that is without precedent in the last twenty five years. In the second half of 1972, wholesale prices soared, mainly in the industrial raw materials and foodstuffs sectors. Between June and December, the general index rose at a yearly rate which ranged from 6.4 per cent in West Germany to 13.8 per cent in France. As a result of tensions spreading into the manufactured goods sector, the index reached exceptionally high levels during the first quarter of the year: about 22 per cent on a yearly basis in the United States and 14 in West Germany. Inflows of funds from abroad weakened the central banks' capacity to control the money stock; moreover, financing of the government deficit has had a similar impact.

The declaration of the dollar's inconvertibility, following a long process stretching from March 1968 to August 1971, combined with the expansion of dollar deposits held by the official authorities and the public both inside and outside the United States. *De facto* convertibility of the dollar into gold for private non US residents was maintained until 1968 by sharing the relative burden among the countries taking part in the gold pool. Towards the end of 1967 and the beginning of 1968, it seemed that this form of convertibility at the official price of 35 dollars per ounce would result in the outflow of all gold reserves to the public. At that time we made known our intention to offset our market gold sales covering pool commitments by purchasing equivalent amounts from the United States Treasury. In March, support for the free market price of 35 dollars per ounce was withdrawn. The dollar continued to be convertible for the central banks; however, in August 1971 this form of convertibility was also abolished.

The United States' external indebtedness stemming from monetary movements rose from 38 billion dollars at end-1968 to 83 at the end of 1972. Almost the entire amount of dollars created through this form of indebtedness flowed to the central banks: the amount of dollars held in reserves increased from 17 to 62 billion; most of which flowing into the central banks of West Germany, Japan, France, Benelux and Switzerland. During the same period, the Eurodollar market expanded at the same pace: the dollar-denominated assets and liabilities of the commercial banks of eight European countries rose, respectively, from 27 to 97 billion and from 30 to 98. At the same time the market for other Eurocurrencies, mainly Deutschemarks and Swiss francs, which was practically non-existent at the end of 1968, also expanded. Excluding assets and liabilities towards US residents, in December 1972 the commercial banks of the eight countries administered a volume of foreign-currency denominated funds amounting to about 120 billion dollars.

One feature of the present international monetary system is the lack of any commitment on the part of the United States, Canada, Japan, Switzerland, the United Kingdom, Italy, and Ireland to intervene in defence of their parities; the remaining Community countries and Sweden and Norway will defend their reciprocal parities, but not against the US dollar. Despite persistent warnings about the need to limit the multiplier effects arising from deposits of reserve currencies in countries other than the issuing ones and from the diversification of these currencies, lately the latter phenomenon has been especially marked, mainly in terms of the Deutschemark.

None of the oil-producing countries deposit dollars in the United States and all of them have converted dollars into other currencies. Under these circumstances, floating exchange rates hamper the further accumulation of reserve currencies and the conversion of one currency into another and act as a stabilizing factor for the system. The results of the recent test run appear satisfactory. Other countries carry out a policy aimed at fostering the use of portions of excess reserves to purchase raw materials, thereby helping to push their prices upwards. The search for profitable investments entails shifts of liquid assets, which adversely affect the financial markets. Frequently shares are purchased on the basis of prices which bear no relation to the enterprises' capital or their performance. Gold is becoming ever more enticing.

The smooth running of the international monetary system is hampered by the coexistence of excess liquidity and increasing limitations on its use. The widening spread between the official price of gold and market prices has persuaded official holders to regard it as a frozen component of their reserves; we warned our European partners of this last June and, after six months of negotiations obtained their pledge to hammer out common solutions aimed at removing the freeze on the use of gold in intra-Community settlements. Gold can, in fact, be used in these settlements, through operations which will be settled when a new official price has been determined or when the central banks are once again allowed to trade on the free market, and official or market prices are considered acceptable. The use of dollars in settlements runs up against barriers, insofar as certain creditor countries refuse to accept them into their reserves. Finally, within the Community framework the amount of resources administered by the European Fund for Monetary Cooperation is negligible. Given these circumstances, the time is ripe to call a halt to our various crusades and meet head on the problem of the place of gold in the international monetary system.

On various occasions I have expressed doubts as to the possibility of re-establishing an international monetary system based on the principle of universality; that is, a system in which the obligation to settle debts and credits among countries by means of reserve instruments available in limited quantities would force each country, without exception, to respect the balance-of-payments constraint. Then and still today, I find it difficult to imagine a system in which the adjustment process takes place in the same way in the large and the small, the developed and the developing countries. Along the spectrum which ranges from a single universally acceptable currency to one currency for each province or city, there are single economic areas in which the degree of integration is higher than that possible for outside zones. The development of monetary areas consisting of countries bound to each other by a system of fixed exchange rates and to other areas by more flexible exchange rate relationships, has led some observers to draw the conclusion that reserves are superfluous. Others believe that the function of reserves might be to control possible exchange rate fluctuations among the areas so that they reflect the medium-term trend of the basic balance of payments.

If among the integrating countries there exist differences in the propensity to inflation and divergent cyclical trends, surpluses and deficits will show up in their balances of payments. If priority is given to integration then the adjustment process must take place without recourse to changes in exchange rates. However, the integration process must be put on a proper footing by also providing an adequate supply of credit lines, administered by a regional organization to which reserves should gradually be transferred. A possible solution for the new international monetary system would be to set up funds for monetary cooperation on a regional level and grant them the power to create monetary units which the member states would use in settling balance-of-payments surpluses and deficits. The abovementioned monetary units would have many of the characteristics of special drawing rights; suspicions that their creation was influenced by the contingent needs of a dominating economy would be less likely to arise. Relations between the various monetary areas would benefit from reciprocal credit arrangements that would be adjusted from time to time by mutual agreement, geared to the need of defending the desired exchange rates. Thus, the need for reserves, in both gold and special drawing rights, would be reduced.

A polycentric international monetary system does not necessarily imply weakening of the general cohesion among its different units. The more the adjustment process among the large areas takes place through a system of flexible exchange rates, the more necessary it becomes to abide by the rules which ensure the orderly development of trade and carrying out of settlements. A system of this type must rely upon institutionalized consultation on the national and area level. The International Monetary Fund is the institution best suited to this purpose. It should be added, moreover, that as we arrive, through the existence of a flexible system, at more credible exchange rates between the currencies of the large areas, the less exposed the latter will be to destabilizing shocks from funds shifting from one market to another in expectation of parity changes.

When special drawing rights were introduced, it was felt that their creation would be regulated according to the liquidity needs of the international monetary system. Their creation was envisaged for a time when the US balance-of-payments deficit would cease to provide the system with liquidity. When they were evolved, it was not thought that SDRs would be the only means of increasing reserves; a certain amount of gold might continue to enter the system, though not enough to meet requirements. Despite massive influxes of dollars to the international monetary system resulting from the balance-of-payments deficit, about 10 billion worth of SDRs were created; the rigidity of the procedures for their activation prevented the amount of SDRs from being adjusted to meet changing circumstances. Newly mined gold was absorbed by the market at rising prices.

One solution to the problem of restoring gold circulation within the international monetary system might be to raise the official price of gold considerably. The resulting overnight surge of liquidity creation could be kept in bounds by agreeing that the central banks, when intervening to defend the exchange rate level, would not be allowed to sell gold to each other but on the free market, up to the amount gained from the revaluation of gold, when the market quotation rises above the official price. This would act to neutralize the liquidity thus created. The deficit country would repurchase its own currency from non-resident holders or, alternatively, would purchase the creditor's currency through gold sales on the free market. The central banks' residual gold holdings could circulate among the same banks or be transferred to the International Monetary Fund in exchange for SDRs or sold on the market. The Fund could sell portions of the gold it holds on the free market in order to obtain the necessary currencies for its operations. The Washington agreement of March 1968 would have to be revoked. Newly mined gold should enter into the free market.

If the solution of an increase in the official price of gold were rejected, as an alternative the notion of an official price could be done away with altogether. In this case the central banks could exchange gold among themselves on the basis of an agreed price and sell and purchase the metal on the free market. SDRs would no longer be expressed in terms of gold content; they would become an abstract unit on the basis of which relations between national currencies would be expressed. The international monetary system would change over from material to immaterial money, backed solely by man's own wisdom. The price of gold in central bank transactions could be determined either on the basis of market prices or periodically revalued in relation to the weighted average trend of prices for internationally traded goods and services, through decisions taken by international bodies. Thus, gold and SDRs would be assigned two different functions, fulfilling two distinct and equally important requirements: to provide the single national communities with a means of storing value or, basically, the means for maintaining their foreign purchasing power, and also to provide the international community with the system's numéraire for expressing the parity ratios of the single currencies.

The central banks' freedom to sell portions of their gold holdings on the market would enhance the effects which can be obtained through the above-mentioned open market operations on the Eurodollar market. Letting gold once again circulate within the international monetary system would offer a further opportunity of moving the reserve structure closer to what is considered desirable and would thus provide an element of stability to the system.

The foregoing solutions to use gold in intra-Community settlements do not solve the problems faced by countries such as Italy with a large percentage of gold in their reserves. Since there are widespread expectations that gold can be sold at a higher price than the present official one, these countries find themselves unable to benefit from that increase just when they may be running balance-of-payments deficits. Until someone comes up with a global solution to the problem of the price of gold, it might be feasible to consider a partial solution for intra-Community settlements. The creation of monetary units on the part of the European Fund for Monetary Cooperation and their allocation to the member countries would have an expansionary impact on liquidity no different from an increase in the price of gold in intra-Community settlements, but would be more in line with the logic of economic and monetary union. If no solution were found, we believe that our country should be quite cautious in taking on the obligations imposed by narrowing the fluctuation margins between the Community currencies.

However, it is not enough to re-establish these commitments in order to bring the nation's economy into step with that of the other European countries. The main roadblocks which have hindered progress towards common positions must be tackled.

Italy's shortcomings, and those of her associates and of the Community organizations, have raised obstacles towards unification. Little has been done on the institutional level. As far as concerns the heterogeneous nature of the economies' structures and dynamics, experience has shown that removing trade barriers will not alone spark off an autonomous process towards integration. The free circulation of goods and services does not ensure that uniform prices for production factors will be attained within a free trade area. The additional condition of full mobility of production factors could help to achieve this aim; but entrusting labour mobility with the predominant task of pulling the economies' structures closer together would involve both a drop in the growth rate of the economy providing the manpower and human costs which no country could accept without serious reservations.

The basic failure of monetary unification projects which rely on formal obligations can undoubtedly be ascribed to the fact that the heterogeneous nature of structures has been disregarded. We have, for instance, asked the Community to provide us with subsidies so that we can move ahead in adjusting our productive structures; but the insistence with which we requested aid was matched by our inability to use that which we obtained.

Finally, homogeneous structures do not mean parallel development. If the long-run trends of costs and prices differ widely in the various Community countries while a system of rigidly fixed exchange rates is in force, then the balance of payments on current account can only be kept in equilibrium in the countries with higher rates of inflation at the cost of minor success in bringing the growth of income closer to its potential. Even without considering the equilibrium of the balance of payments on current account as a constraint, if the return on investments differs from country to country then the costs of unification will be greater for those countries less able to attract the area's productive investments, and this would result in their having a lower growth rate.

Thus, our contribution to the integration process should not be exercised through the resigned acceptance of the method that makes unification depend on imposing certain constraints on symbol-variables, such as the rate of money growth and the relations which link the various European currencies. Our contribution must be free of the fear that any criticism we make of the methods being used will leave us vulnerable to attacks of being anti-European. There was no fear of such accusations among the *Members of Parliament* who, at Community meetings, rejected plans put forward by the Commission for a restructuring of agricultural prices, and challenged the underlying rationale for the existence of a European unit of account used in settling payments for agricultural trade. Those who took this stance thought that by magnifying the effect of revaluations and devaluations on domestic prices, parity changes would be definitely eliminated. However, since this result was not obtained, is not the time ripe to now ask ourselves whether by persisting with this ficticious system we will create tensions harmful to the integration process?

A more reasonable way of dealing with unification problems is that of moving on to the comparison and to the coordination of programmes regarding medium-term real flows — in which the strategic variable is the volume of investments — in order to ensure the consistency of the balance on current account and on intra-Community capital movements. This process could lead to a partial revision of each country's income and investment targets. When, instead, it is not made clear at the beginning that the various targets are in conflict, the adjustment process is necessarily left to the play of market forces and uncoordinated economic policy interventions. In this type of situation it is quite likely that the whole burden of bringing the objectives into line will be left on the shoulders of one group of countries, while another group makes no move to revise its own aims. We do not think it is futile to widen the discussion of the foregoing issues, as far as this lends to spreading the certainty that the European choice is irrevocable, not only because commitments have already been undertaken but above all because it responds to deeply rooted yearnings within Italy.

During Italy's *Risorgimento* the European ideal was deeply engrained in the effort to achieve national unity, so that the two ideals were not seen as contradictory but as phases of a single process moving towards the expression of a culturally homogeneous community. Events in the last decades have given a sense of urgency to what might have seemed a utopian vision during the last century, so that the accomplishment of European unification is considered an indispensable development for the very survival of the values embodied in national ideals.

During the period covering June 1, 1972 to February 13, 1973 — the day on which, together with the announcement of the dollar's devaluation, it was decided to float the lira — the Banca d'Italia was forced to intervene in support of the lira with foreign exchange sales amounting to 2,824 billion lire, under the terms of the Community agreement narrowing fluctuation margins. If the currency sales made by the Ufficio italiano dei cambi for its own operations are included then the total rises to 3,024 billion. This represents 78 per cent of the Banca d'Italia-UIC's net external assets at the beginning of the period. If we had not taken out compensatory loans and assuming that priority was given to the use of convertible currencies, the latter would have been completely wiped out and our gold holdings, including gold-convertible reserves, would have fallen from 2,208 billion to 764. This did not happen thanks to a series of operations, of a one-time nature; namely, unwinding the UIC's long position of 870 billion in respect to swaps with the banks; activation of swaps creating a short position for the UIC of 544 billion vis-à-vis the banks; and compensatory loans amounting to 939 billion. Despite the above-mentioned operations, the Banca d'Italia-UIC's net foreign position registered a fall-off of 671 billion and the banks' foreign indebtedness, excluding operations involving compensatory loans, increased by 145 billion.

The Banca d'Italia-UIC's foreign position, calculated on the basis of a gold price of 42.22 dollars per ounce and of the new exchange relations, amounted to 3,454 billion on February 13; on April 30, the total was 3,501 billion. From February 15 to April 30 the banks' indebtedness, excluding the above-mentioned operations, grew by 322 billion. During the same period recourse to compensatory loans was almost non-existent; instead, a few funding operations took place, moving the due dates of these debts to between 1976 and 1980.

After February 13, intervention policy on the exchange market was, in principle, based on the need to avoid, as far as possible, sharp swings in rates and to earmark the possible inflow of foreign currency for the repayment of swaps, debts with banks, and the compensatory loans. As it happened, currency influxes were only registered during the second half of February. These did not amount to much and were mostly used to repay swaps. Instead, during the following months it became necessary to intervene occasionally through currency sales, to avoid too great a depreciation of the lira; nonetheless, these sales did not affect the volume of reserves, given the influx, in April and May, of the receipts of loans taken out by ICIPU (Public Utility Credit Institute) and IMI (Italian Industrial Credit Institution).

From balance-of-payments data it emerges that in 1972 capital movements, particularly those linked with a different use of the terms of payment for exchanges of goods, led to the building of a deficit: as a result, the net outflow of funds amounted to 1,345 billion lire, versus 374 in 1971. The current account balance also deteriorated, although only slightly: between 1971 and 1972, the relative surplus, in fact, dropped from 981 to 844 billion; this result was influenced by unusual factors, such as large imports of gold, moreover at rising prices, during the last four months and the above-mentioned distortions in flows from tourism and emigrants' remittances.

During the first months of 1973, excluding March when results were distorted by the customs strike, a large increase was registered in imports, along with a marked slowdown in exports. The former are moving up at a vigorous pace, in connection with revived productive activity and the replenishing of inventories: their value was inflated further by the rise in international prices and by the impact of the lira's depreciation. The slowdown in exports was influenced by shortages in the supply of mechanical engineering products, the result of prolonged strikes. On the whole, during the first four months, the balance of payments registered an overall deficit of about 550 billion lire, two-thirds of which in January alone when large numbers of investors made heavy purchases of foreign securities.

On the basis of the exchange rate relations — as they unfolded in the first three weeks of May — between the lira, the Community currencies and the dollar, the weighted average devaluation rate, in respect to exchange rates on February 9, was 8.50 per cent for imports and 9.70 per cent for exports. These relations allowed manufacturers to transfer costs onto the prices of their products without harming their competitive position.

We have stated that the policy followed by the monetary authorities during 1972 was based on the need to keep the balance-of-payments constraint from undermining those moves aimed by-and-large at stimulating a recovery of productive activity. On the other hand the origin itself of upward price movements seemed to rule out that satisfying results might be obtained by manoeuvring monetary aggregates. In January of this year, this interpretation of the facts was accepted: once the two-tier market had been set up it was decided that part of the enterprises' burden of social security contributions would be switched over to the government. The cost of labour, but not wages, had reached, and in some cases surpassed, the level registered in the other Community countries, the difference owing wholly to the enterprises' social security burdens. Transference to the government of part of these contributions was seen as a move towards lining up the Italian economic structure with that of the remaining European countries.

Had this measure been put into force immediately, focused on the manufacturing industry sector and linked with price controls on products of the major industries it would have been effective in fostering the revival of production and curbing inflationary pressures. But since it was designed to include all the enterprises, rather than a chosen few, important power centres made no move to get it approved. Once again it appears that the economic policy followed in our country tends towards keeping the production system permanently afflicted, every now and again promoting some merciful intervention to bring thanks showering down upon the inner circle backing these measures. The most obscure scruples are invoked to obstacle measures benefitting all the enterprises; however these scruples vanish the moment it is a question of increasing the endowment funds of the state-holding companies. We have not yet rid ourselves of our ancient predilection for *tyrannical laws* which *being of use to one or to few, are most ensnaring.*

While the balance-of-payments constraint weakened, steps were taken on the international and Community level to strengthen existing anti-inflationary policies. The OECD member countries committed themselves to coordinating their respective fiscal and monetary policies, in an attempt to help curtail inflationary phenomena; more specifically, the Community countries established ceilings on the creation of money. Most countries overshot these bounds.

In 1972, the United Kingdom's money stock increased by 25 per cent against an increase of about 11 per cent in income at current prices, about 7 per cent of which stemming from price rises. The lowest rate of increase for the money stock (12 per cent) was registered by the Netherlands against an increase of 14 per cent in income at current prices, 10 per cent of which due to price rises. With regard to the other countries, increases were registered at intermediate rates, although certainly higher than growth rates for income at current prices; Italy showed an increase of 18.6 per cent, against a 9.3 per cent increase in income and 5.9 for prices.

The goals which the Community bodies set for themselves have not been accomplished. On the other hand, the tightening of monetary policy would immediately tend to affect mainly the level of output; in fact, in the Community countries the inflation component linked with cost increases is more dynamic than pressures arising from increased demand. In addition the money stock is only one of the components determining credit volume: an equal increase in means of payment can support widely differing levels of expansion of overall credit. It is this latter variable in particular which must be watched if we wish to correct, over the short run, the volume of overall demand; in most countries, its rate of development also widely exceeded that of income at current prices.

In the first quarter of this year further upward impulses from abroad superimposed on the ongoing rise in domestic costs and prices caused the rate of price increases in Italy to move up to among the highest being registered in the industrial countries; nonetheless the increase seems among the lowest in the manufactured goods sector, whereas there was a particularly large upswing in the agricultural and industrial raw materials sector, where imports carry considerable weight. Progress was made towards restoring more balanced conditions for the enterprises; the economic system was shaken out of the lethargy in which it had seemed to loll in the recent past. This opinion is confirmed by the latest data on industrial production, even though in the first quarter of the year the overall index, seasonally adjusted, dropped by almost 6 per cent compared with the last quarter of 1972; this fall-off was, in fact, greatly influenced by production slowdowns in the wake of strikes in the mechanical engineering sector preceding the signing of the national contract. If this sector is excluded, the slowdown in productive activity is reduced by two-thirds, which indicates that, after the previous quarter's hefty increases, production is evening out to a level over 5 per cent higher than 1972's average.

Information provided by our branches reveals that the private enterprises, after having refrained from increasing investments in 1972, are now behaving differently: it seems that large-scale investments projects are being carried out all over the country. The trend, even for the large enterprises, is towards medium-sized production units scattered throughout the nation but tending to be located where there is less industrial congestion, and especially in the Mezzogiorno. The new productive set-up seems to be based on medium-sized plants that revolve around a central decision-making body as far as concerns investment planning, financing and marketing. If, however, we are witnessing a promising revival of private initiative, the same sources reveal that these investments will not promise much new employment. As regards financing methods, in Northern and Central Italy about half the funds were raised through indebtedness while in the South the amount was about two-thirds.

The first thrust towards recovery was provided by foreign demand and by stockbuilding, spurred by expectations of changes in the tax system, while the contribution of public expenditure for social infrastructures was a meager one. The same forces at the origin of those imbalances which hindered an upswing are still at work within the economic system. Signs of growing tensions in various sectors are looming on the horizon. Price increases could upset the expansion of economic activity.

The awareness of the difficulty of bringing downward pressures on prices through recourse to fiscal and monetary policies has led a large number of countries to set up administrative controls on prices and incomes. The controls were effective in temporarily slowing down the growth rate of costs and prices, allowing the increase in demand to foster an upswing in production. Although the dismantling of those controls was met by a rapid surge in prices, the experiment does not warrant a negative assessment. There is no reason to rule out the use of this instrument in Italy although, in the awareness that this country lacks the proper administrative structures, the scope ought perhaps to be limited.

The periodic comparison between demand and potential supply essentially leads to an examination of the increase in public expenditure and of its consistency with development lines in the private sector. The estimates for 1973 show that on the basis of the exchange rate relationships between the lira and the Community currencies, the balance of payments should close in approximate equilibrium. This forecast is based on the assumption that policy measures succeed in slowing down the inflationary pressures present in our economy bringing them back to levels close to those being experienced in most of the industrial countries; as well as in keeping the possible current account deficit within an amount that can be financed with inflows of capital. Another condition is that the Government sector's net indebtedness must not accelerate in respect to the growth rate of the first part of the year.

Conditions are looming that will make it necessary to use demand-regulating instruments in order to curb pressures on real resources: there will appear a clear-cut need for corrective intervention through increased taxation. If interventions to regulate demand are carried out through monetary policy measures, they are bound to run up against the tightening of constraints due to the expansion of the volume of long-term securities created for financing the public sector's needs.

The amount of outstanding bonds will, in time, create complex problems: at the end of 1965, the volume of outstanding securities was about 13,000 billion lire; for those issued by the Treasury, it was about 4,000 billion. At the end of 1972 the volume of outstanding securities hit the 41,000 billion mark and those issued by the Treasury, 16,000 billion. Given this recent upswing, their average maturity is much longer, thus market yield fluctuations, albeit slight, bring about massive changes in capital value. This circumstance stresses the need for a continuous action aimed at defending the price of securities, in order to ensure an adequate demand by the public; however, monetary base creation must be viewed as a function of securities price pegging necessities. Therefore, possible restrictive action must be limited to other channels of monetary base creation and, more specifically, to direct bank financing. In the last five years, the percentage of securities in the Banca d'Italia's portfolio rose from 6 to 15 per cent of total outstanding issues.

The policies which we have followed during recent years, when intervening on the bond market, have made possible the easy placement, at sufficiently low interest rates, of large issues of both public and private securities. From this point of view, the setting up of the external two-tier market for the lira and the floating of exchange rates provided us with greater freedom.

It would seem advisable to reduce, at least relatively, the volume of issues by augmenting taxation. It is no less important to have a more segmented structure of public debt so that short-term rates can fluctuate more widely and, at the same time, some stability for long-term rates can be ensured if necessary.

In the past, the large volume of public bonds has not made it possible to carry out adequately an interest-rate policy in line with the achievement of goals; when we begin to progress towards a European system of fixed exchange rates, control over short-term interest rates will have to be sufficiently elastic. It is to be hoped that, in the future, long-term public securities will only be issued in order to finance cash requirements resulting from investment expenditure and that, when necessary, financing through short-term securities will also be permitted.

One cause of the Central Bank's increased difficulties in regulating monetary base, was the massive transfers made by the Treasury to the Regions of funds which were then deposited with the banks. These transfers result in an upswing in the volume of liquid funds available to the banking system as a whole: however, they are spread unevenly within the system, since the banks compete fiercely in order to acquire them. This has a corroding influence on competition: the acquisition of funds is bargained over in a way which contradicts the system's logic and causes distortions in credit activity. We shall suggest that the authorities impose specific compulsory reserves for these Regional funds.

The present economic recovery has been interpreted in contrasting lights: some people put stress on the rise in output, others on the accompanying rapid expansion of prices. The latter took place both because inflation is rife throughout the world and because, over recent years, it was only curbed in our country to the extent that we did not manage to expand demand. Numerous factors concurred to pressure the upward spiral of costs; increases in unit costs were not transferred onto prices and, as a consequence, the equilibrium of the firms suffered. Under these conditions, no policy could have enabled the system to achieve nearly full utilization of productive capacity without passing through inflation. We issued frequent warnings on this count. Today, however, in a period in which the system is nearing full utilization of available facilities, given the existing limits on such utilization, the solution to the problems that are arising is mainly the responsibility of the monetary authorities.

The balance of payments on current account is developing in such a way as to confirm that we have nearly reached that point of utilization. A deficit could be tollerated for a short time, to the extent in which it was related to an expansion of investments aimed at strengthening the production structure. It is our belief, however, that we must reject the idea that the possible formation of a deficit should be neutralized by further variations in the actual exchange rates between the lira and the Community currencies. Fiscal and monetary policy intervention must conform to this constraint.

A revival of productive activity without the corresponding effective utilization of resources in both the public and private sector is in danger of being only short-lived rather than the long-awaited beginning of a new expansionary phase.

Therefore, it is necessary to review carefully the policies followed in recent years, which have been too highly directed towards maintaining existing employment structures. By crystallizing the status quo and offering a sort of public guarantee for the permanence of production factors in low productivity areas, such policies have actually worked counter to full employment.

In view of this, we should go back to the drawing board with plans that have not borne their expected fruits in order to reduce the huge deficits that have cropped up in the transport and postal services sectors and in public services in general. Thus, we can avoid that measures aimed at restructuring the sectors do not themselves become, in practice, a means of financing outdated structures.

Within the framework of industrial policy, it will also be necessary to reduce the importance that has been given to interventions, such as: the act for the textile industry which, as it worked out has merely meant the indiscriminate allocation of subsidized resources, rather than selective support of the sector's more economically viable businesses; Law n. 1470, in various and even recent reincarnations, regarding the reorganization of small-sized industries, which, as experience has clearly shown, has had a long and negative record in serving to overcome crises; or in some way GEPI (the State Industrial Management and Holding Company) which, in our opinion, can hardly be allocated continually growing resources.

There is no escaping the fact that the tendency to keep the present situation alive is sanctioned by the politicians, entrepreneurs, and trade unions. Underlying this behaviour, legitimate motives of a social nature mingle with others, certainly less explicit but nevertheless present, based on defending outright positions of privilege.

Gentlemen,

The manoeuvring space allowed the Central Bank has shrunk and is still shrinking, as a result of the growing impact of decisions regarding the volume of government expenditure and its use, incentives to public and private investment and, above all, the definition of labour relations. We shall do the best, within our power, to make sure that the recovery of economic activity is not hindered by financial hurdles. This depends on the maintenance of a continuous flow of investments and this continuity in turn, under the present institutional system, is highly determined by the financing of the industrial credit institutions. These institutions raise funds, for the most part, through bond placements which have to compete with placements by the real-estate credit institutions and state holding companies. The above-mentioned demand for funds must be coordinated with the Government sector's funding needs and the latter are not adjustable over the short run. The Central Bank may be compelled to purchase securities to the extent required to ensure the smooth running of the securities markets. Otherwise, a percentage of total financing might have to be raised through recourse to short-term credit. In coincidence with fewer purchases of securities by the Central Bank there might be a corresponding increase in its financing to the banks, if we wish to maintain a steady flow of credit to the productive sectors; in this case as well, money would be created. Should it become necessary to limit the overall volume of credit, the reduction, owing to the rigidity of the public sector's demand, would mainly affect the directly productive sectors. Shouts of protest would again be raised; the monetary authorities would be blamed for creating a situation that arises from a widespread incapacity in this country to manage our affairs in a modern, clearsighted, innovative fashion. The foregoing chain of events will surely take place unless proposals for further government expenditure are resisted for the time being.

Throughout the course of the debate on monetary policy, the Banca d'Italia's behaviour has been assessed in various ways, nonetheless there has been general consent on the efficiency of the Central Bank. These acknowledgements are received with pride by our personnel; if we deserve any praise at all it is only because we have acted independently while performing our duties. Nonetheless warning should be given that along with this increased efficiency we have found ourselves with less scope to display it in concrete moves, because of contrasting steps taken elsewhere which have led to changes in the economic conditions. The harmonization of goals must precede and not trail behind monetary policy moves; it cannot take place without the cooperation of the trade unions: from the role of conflict strategists they must shift over to the role of participants in the management of the economy. Nor can there be harmonization without the cooperation of the entrepreneurs, who are duty bound to make the institutional framework in which they operate more acceptable, showing their awareness of the fact that, in a modern society, the contrast between *ostentatious wealth and accursed poverty* is becoming increasingly intollerable.

The above remarks would tempt me further along a path leading far from monetary policy themes. Its direction is towards the great themes facing our society. Thus, let me conclude by using the words of a famous Italian, Giustino Fortunato. « No country...... is more backward than our own in its sense of freedom. What is our idea of a free man, according to our ancient creed? Not one who is equal to another, and like him subject to the same law; but he who is his own master and has, at the same time, power over others. Only he who can command, only he who need not obey is free and his own master. And this is why, not only are our people the most individualistic, but also the most authoritarian in the civilized world: authoritarian to the very core; such is our legacy, our education, our surroundings. Either slaves or masters, inherently rebellious or domineering, this is our nature; obeying the fundamental, unquestionable right of each man from the early ages on to enforce his own law. This is our inheritance, and it still courses through our veins: .... unless Italy wants, sooner or later, to revert to what she was.... our most compelling task is to educate; this, then, must be our starting point: a long, vast and difficult task, if to educate means to make the unaware aware, but a worthy and a noble one. It is not enough to assert that freedom is everything; however, to say, as others have said, that absolute rule is preferable to freedom, runs against civilization and contradicts history ».

IV. – THE BANK'S CAPITAL AND RESERVES

Capital.— In 1972, the merging of the two insurance institutes resulted in slight changes in the number of shareholders with voting rights.

On December 31, 1972, they were distributed 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 . . .	8	»	31,500	»	»	95	»
	96	with	299,896	shares	and	795	votes

Shareholders without voting rights:

Savings banks and loan offices	14	with	104	shares
Total:	110	with	300,000	shares

Reserves.— During 1972 the reserve funds underwent the following changes:

	Ordinary reserve fund	Extraordinary reserve fund
Amount on December 31, 1971	Lit. 16,580,220,113	Lit. 14,294,729,348
increase:		
– allocation from profits for the year 1971 . .	» 4,912,044,245	» 4,912,044,245
– income received in 1972 from investment and reserves	» 1,163,080,000	» 1,497,717,993
	Lit. 22,655,344,358	Lit. 20,704,491,586

	Ordinary reserve fund	Extraordinary reserve fund
decrease:		
– distribution to shareholders of a part of income accruing in the course of 1971 (Article 56 of the Statute) .	Lit. 80,853,313	Lit. 63,146,687
Amount on December 31, 1972	Lit. 22,574,491,045	Lit. 20,641,344,899

V. – BALANCE SHEET
AND PROFIT AND LOSS ACCOUNT

BALANCE SHEET AS

ASSETS

Gold	L.		1,801,916,705,648
Cash	»		66,641,539,245
Domestic bills of exchange:			
discounting for the banks	L.	44,009,577,567	
discount on Treasury bills and coupons	»	—	44,009,577,567
Advances:			
current account	L.	880,730,409,506	
fixed-maturity	»	1,431,299,868,500	2,312,030,278,006
Deferred payment at the clearing system	L.		—
Foreign currency external assets	»		2,216,193,636
Ufficio Italiano Cambi:			
ordinary current account	L.	1,194,849,520,555	
special accounts	»	1,323,129,603,187	2,517,979,123,742
Extraordinary advances to the Treasury	L.		339,000,000,000
Discounting for financing stockpiling	»		1,104,053,234,341
Treasury current account	»		1,907,658,610,478
Miscellaneous services on behalf of government - debit balance	»		499,013,869,318
Investment in government or government-guaranteed securities	»		5,245,806,392,998
Investment of reserve funds and other funds set aside			
government or government-guaranteed securities	L.	249,970,788,635	
other assets	»	187,706,118,105	437,676,906,740
Office buildings	L.		1
Other assets	»		275,571,980,152
	L.		16,553,574,411,872
Commitments:			
unused part of credits on advance accounts	L.		765,908,404,337
Deposits:			
guarantee	L.	4,058,969,533,418	
for compulsory bank reserves	»	4,154,611,957,000	
others	»	2,312,513,716,742	10,526,095,207,160
Securities and other valuables on deposit	L.		939,903,237
Items written off in past years	»		1,764,632,416
TOTAL	L.		27,848,282,559,022

Audited and found correct. – Rome, May 4, 1973

THE AUDITORS

Domenico Amodeo
Alberto Campolongo
Raffaele D'Addario
Bruno De Mori
Giuseppe Guarino

THE ACCOUNTANT GENERAL

Armando Pescatore

SEVENTY NINTH YEAR

OF DECEMBER 31, 1972

LIABILITIES

Notes in circulation	L.		8,747,476,914,000
Bank drafts and other sight liabilities	»		316,129,105,813
Free deposits on current account	»		180,469,751,330
Tied time deposits on current account	»		1,174,063,521
Compulsory deposits on current account:			
compulsory bank reserves	L.	4,330,558,003,559	
others	»	3,969,412,240	4,334,527,415,799
Foreign currency deposits:			
on behalf of UIC	L.	899,553,589,000	
others	»	2,216,193,636	901,769,782,636
Foreign lira accounts:			
on behalf of UIC	L.	423,576,014,187	
others	»	51,710,495,092	475,286,509,279
Miscellaneous services on behalf of the government - credit balance	L.		139,254,086,677
Treasury services for various agencies	»		427,907,956,242
Other funds set aside	»		641,033,453,207
Other liabilities	»		319,451,044,827
Capital	L.	300,000,000	
Ordinary reserves	»	22,574,491,045	
Extraordinary reserves	»	20,641,344,899	43,515,835,944
Net profit for 1972	L.		25,578,492,597
	L.		16,553,574,411,872
Commitments	L.		765,908,404,337
Depositors	»		10,526,095,207,160
Securities and other valuables	»		939,903,237
Items written off in past years	»		1,764,632,416
TOTAL	L.		27,848,282,559,022

THE GOVERNOR

GUIDO CARLI

GENERAL PROFIT

FOR THE

EXPENDITURE			
Administration	L.	168,289,194,865	
Emoluments of Directors, etc.	»	342,363,104	
Transport of notes, coins and other valuables	»	211,205,354	
Note-printing and note-destruction	»	5,274,393,907	
Computerized data processing	»	5,443,220,778	
Expenditure on premises	»	1,778,414,914	
			181,338,792,922
Circulation tax on notes and demand drafts	L.	19,888,217,300	
Income and company taxes	»	25,000,000,000	
Sundry taxes	»	744,014,385	
			45,632,231,685
Depreciation and allowances	L.		93,040,319,219
Interest paid on Treasury accounts	»		41,891,121,508
Other interest paid out	»		8,879,284,154
Charity and social and cultural aid contributions	»		327,429,583
	L.		371,109,179,071
Net profit for distribution	»		25,578,492,597
TOTAL	L.		396,687,671,668

PROFIT

To ordinary reserves	
To extraordinary reserves	
To shareholders	
To the Treasury	
TOTAL	

Audited and found correct. – Rome, May 4, 1973

THE AUDITORS

DOMENICO AMODEO
ALBERTO CAMPOLONGO
RAFFAELE D'ADDARIO
BRUNO DE MORI
GIUSEPPE GUARINO

THE ACCOUNTANT GENERAL

ARMANDO PESCATORE

AND LOSS STATEMENT

YEAR 1972

RECEIPTS

Discounts	L.	13,609,777,595	
Interest on advances	»	26,713,194,543	
Interest on other assets	»	19,820,258,088	
Commissions and other fees	»	3,929,769,314	
Other revenues	»	46,129,285,971	
			110,202,285,511
Interest and premiums on securities	L.	286,167,805,105	
Revenue from real estate	»	317,581,052	
			286,485,386,157
		Total . . . L.	396,687,671,668

DISTRIBUTION

L.	5,115,698,519
»	5,115,698,519
»	30,000,000
»	15,317,095,559
L.	25,578,492,597

THE GOVERNOR

Guido Carli

ADMINISTRATION OF THE BANK OF ITALY

AS OF DECEMBER 31, 1972

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

Alessandro BARNABO'
Guido BORSELLINO CASTELLANA
Gaetano CARBONE *
Umberto CARUSO *
Carlo D'AMELIO
Giovanni Battista DEL BALZO
Danilo de MICHELI
Luigi FANTOLA
Antonio FONDA SAVIO *
Lucio MORODER
Remo MORONE
Giambattista PARODI *
Giovanni POGGI

* Member of the Executive Committee.

BOARD OF AUDITORS

Domenico AMODEO
Alberto CAMPOLONGO
Raffaele D'ADDARIO
Bruno DE MORI
Giuseppe GUARINO

ALTERNATE AUDITORS

Michele BENEDETTI
Antonio CONFALONIERI

CENTRAL ADMINISTRATION

MANAGERS

Guido RUTA	– Chief Legal Adviser
Francesco MASERA	– Economic Adviser
Paolo BISERNI	– Central Manager for Supervision of Banks
Armando PESCATORE	– Accountant General
Mario ERCOLANI	– Central Operations Manager
Giuseppe CRISCUOLO	– General Inspector
Pietro BATTAGLIA	– Central Manager for Technical Services
Ugo BRUNO	– Central Manager for Administration of Premises and Property
Lamberto CANTUTI CASTELVETRI	– Central Manager

LIST OF ABBREVIATIONS

AIMA	Azienda di Stato per gli interventi sul mercato agricolo — Government Agency for Intervention on the Agricultural Market —
BI	Banca d'Italia
CAS	Central Administration Services
CREDIOP	Consorzio di credito per le opere pubbliche — Credit Consortium for Public Works —
EEC	European Economic Community
EMF	European Monetary Fund
ENEL	Ente nazionale energia elettrica — National Electricity Agency —
ENI	Ente nazionale idrocarburi — National Hydrocarbon Agency —
FEOGA	Fondo europeo di orientamento e garanzia agricola — European Agricultural Fund —
GAB	General Agreements to Borrow
GATT	General Agreements on Tariffs and Trade
GEPI	Società di gestioni e partecipazioni industriali — State Industrial Management and Holding Company —
GNP	Gross national product
ICCRI	Istituto di credito delle casse di risparmio italiane — Credit Institute of Italian Savings Banks —
ICIPU	Istituto di credito per le imprese di pubblica utilità — Public Utility Credit Institute —
IGE	Imposta generale sull'entrata — General turnover tax —
IMF	International Monetary Fund
IMI	Istituto mobiliare italiano — Italian Industrial Credit Institute —
INPS	Istituto nazionale della previdenza sociale — National Social Security Institute —
IRI	Istituto per la ricostruzione industriale — Institute for Industrial Reconstruction —
ISTAT	Istituto centrale di statistica — Central Institute for Statistics —
OECD	Organization for Economic Cooperation and Development
RSB	Regional Statistics Bureau
SDR	Special drawing rights
UIC	Ufficio italiano dei cambi — Italian Exchange Office —
UNO	United Nations Organization
VAT	Value added tax