BANCA D'ITALIA

ORDINARY GENERAL MEETING OF SHAREHOLDERS

HELD IN ROME ON 31 MAY 1986

ABRIDGED REPORT FOR THE YEAR 1985

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CONTENTS

LIST OF TABLES

LIST OF FIGURES

THE INTERNATIONAL ECONOMY

RECENT DEVELOPMENTS AND ECONOMIC POLICIES

The economic performance of the industrial countries

The average national income of the industrial countries increased by 2.8 per cent in real terms in 1985, as against 4.7 per cent in 1984. The slowdown of economic expansion in the United States, where GNP rose only one third as fast as in the previous year, was not offset by growth elsewhere. Indeed, expansion in the rest of the industrial world was slower than in 1984 (3.0 as against 3.4 per cent), owing partly to the deceleration of US growth. The growth differential between the United States and the rest of the OECD area, which had been very large in 1984, was reversed — GNP growth was 2.2 per cent in the United States and 3.0 per cent overall for the rest of the OECD. The disparity with respect to the EEC vanished. Domestic demand expanded at almost the same rate.

Inflation in the industrial countries as a group, as measured by the consumer price index, was 4.1 per cent in 1985, half a percentage point less than in 1984. The dispersion of inflation rates also decreased, but the distance between one end of the range and the other is still substantial, about 7 percentage points between Italy and Japan, compared with 8.6 points in 1984. The decisive factor in the slowdown in inflation was the decline in raw material prices. For Japan and the European Community countries, the impact on import prices was amplified in the second half of the year by the appreciation of their respective currencies against the dollar. For the United States, a lag in passing exchange rate movements on to domestic prices, together with foreign exporters' efforts to defend their market shares in the face of the weak dollar, muted the inflationary impact of the depreciation of the dollar.

Nominal wage growth continued to slow down throughout the OECD area. This trend, which has been evident in the industrial economies since the turn of the eighties, is linked to macroeconomic strategies that accord priority to curbing inflation. Wage deceleration has been the result of a decline in inflationary expectations and an increase in unemployment and has been helped, in some cases, by specific measures to adjust wage indexation machinery.

In the first few months of 1986 the industrial economies enjoyed the disinflationary benefits of the fall in oil prices. This was reflected in wholesale price indices, which include oil and oil products and therefore registered substantial decreases in several of the major industrial nations. There is reason to anticipate that nominal wages will adjust to lower inflation rates in future — both the persistent excess supply of labour and the improved flexibility of the labour market can be expected to produce such an effect.

The increase in the demand for labour in 1985 was a new development compared with the trend of the last few years. However, the expansion of the labour force offset the gains in employment, so that the unemployment rate in the OECD as a whole decreased only slightly to about 8.5 per cent of the civilian labour force.

The emergence and widening of the unemployment differential between the United States and the European Community since the late seventies has often been attributed to different trends in real labour costs with respect to productivity. Since the second oil shock, however, the leading European economies have experienced considerable wage moderation together with rising productivity (Table 1), which has inverted the tendency of increases in labour costs to outstrip productivity gains that characterized the seventies.

Table 1

REAL LABOUR COSTS, LABOUR PRODUCTIVITY, GROSS OUTPUT AND UNEMPLOYMENT IN THE UNITED STATES AND THE FOUR MAJOR EEC COUNTRIES

(average annual rates of change, 1979-85)

	Real labour costs (1) (2)	Labour productivity (1) (3)	GDP/GNP	Unemployment rate (4)
United States	—	2.5	1.9	0.2
EEC	1.8	3.2	1.1	0.9
Germany	*1.0*	*2.9*	*1.2*	*0.8*
France	*1.4*	*3.5*	*1.1*	*0.6*
United Kingdom	*2.4*	*3.8*	*1.0*	*1.1*
Italy	*2.7*	*3.0*	*1.4*	*0.5*

Source: OECD and Istat.

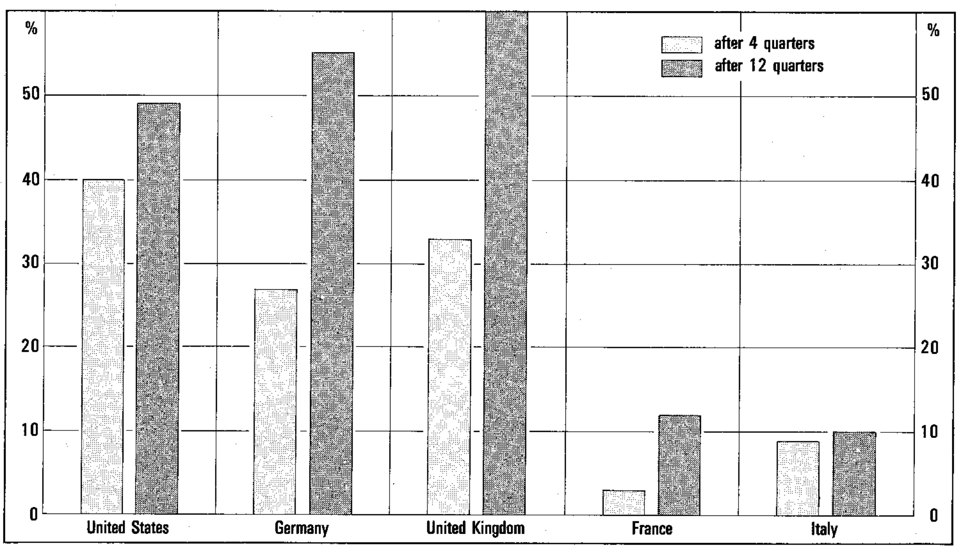
(1) Manufacturing industry. — (2) Per capita wages and salaries adjusted using the deflator of value added. — (3) Value added per employee. — (4) Average change.

The experience of 1979-85 suggests that a significant factor in the differing unemployment trends has been the difference in growth rates. Economic expansion in the United States has averaged almost one point a year faster than in Europe. The behaviour of unemployment rates, which to some extent reflects the gap between potential and actual output, nonetheless shows that sustained growth itself is a necessary but not a sufficient condition for the recovery of full employment. Empirical simulations indicate that the response of unemployment rates to output impulses varies greatly in velocity and magnitude from country to country (Figure 1). As actual GDP grows faster than potential output, the unemployment rate decreases significantly in the United States, where adjustment is prompter than in the other countries, and in Germany and the United Kingdom. The decline is only marginal in France and Italy. In view of the general narrowing of the differential between the rise in labour costs and productivity, the varying strength of the link between output and unemployment implied by these results suggests that labour market rigidity is more severe in some countries than in others.

Figure 1

OUTPUT AND UNEMPLOYMENT (1)

(change in the unemployment rate in response to an increase in real output one percentage point greater than that in potential output)



Source: OECD.

(1) Assuming that actual output grows over four quarters at an annualized rate that is one point greater than that of potential output.

The developing economies

In 1985 the economic situation of the less developed countries showed signs of deterioration after the progress made in 1984. Their growth rate slowed from 4.1 to 3.2 per cent as a result of the deceleration in economic activity in the industrial countries and the contraction of world trade. Fuel-exporting countries suffered from the persistent slackness of demand for oil, while countries heavily dependent on external financing from private sources encountered difficulties stemming from the continuing contraction of private financial flows.

The volume of the LDCs' exports virtually stagnated, after having increased by more than 7 per cent in 1984, while imports contracted slightly. Despite a worsening in the terms of trade of more than 2 per cent, their balance-of-payments deficit on current account remained stable. The deficit of the capital importing countries increased for the first time in three years, rising from $23 billion to $27 billion — about a quarter of the deficit registered in 1981.

The pace of internal adjustment was unsatisfactory. Especially in many heavily indebted LDCs, the persistence of rapid inflation and low or even negative real returns on domestic savings has prevented the generation of a flow of resources large enough to make up for the diminished availability of external financing and the growing burden of interest payments on the debt.

Consumer price increases in the LDCs averaged 39 per cent, slightly faster than in 1984. This acceleration was due principally to extremely rapid inflation in several Latin American countries, while in most other LDCs inflation appears to have stabilized or begun to decline.

Economic policy in the industrial countries

Monetary policy. — The stance of monetary policy in the major industrial countries last year was more expansionary than in 1984. The velocity of circulation of the monetary aggregates decreased everywhere, except as regards M1 in Japan. In some countries, however, the need to defend the exchange rate necessitated temporary tightenings of liquidity that drove short-term interest rates up. The United Kingdom raised base rates sharply at the beginning of the year, as the pound sterling came under heavy pressure; rates then declined in the course of the following months, until January 1986 when the rate was raised in response to renewed exchange rate pressure. Following the September agreement among the monetary authorities of the five leading industrial nations, Japanese short-term interest rates were raised by about a point and a half in order to bring about an appreciation of the yen. Elsewhere, short-term yields diminished, with minor fluctuations. The decline amounted to more than a point in France and Germany, somewhat less in the United States. Longer-term rates declined everywhere, most markedly in the United States, Canada and France.

The monetary authorities of the major countries sent a significant signal as to the outlook for interest rates by their decision to reduce discount rates simultaneously at the beginning of March 1986. The German decision to lower the discount rate by half a percentage point was emulated by Japan and the United States. Other countries, such as the Netherlands, France and Italy, moved in the same direction. German and Japanese policymakers judged at the time that a reduction in interest rates was warranted by the favourable inflation outlook and their respective currencies' exchange rates with the dollar. For the US authorities, the reduction was possible because the joint action reduced the risk of a precipitous depreciation of the dollar. The concerted lowering of discount rates was repeated on 21 April by the United States and Japan (from 7.0 to 6.5 per cent and 4.0 to 3.5 per cent respectively), confirming the downward trend of nominal interest rates as inflation receded. Base rates in the United Kingdom were reduced to 10.5 per cent, two points lower than their level at the start of the year. Italy also lowered its discount rate, from 15 to 14 per cent in March and then to 13 per cent in April.

The progress made since the start of the decade in curbing price inflation and the credibility achieved by the monetary authorities on that front have recently made possible a more active use of the monetary instruments, with greater attention being paid to cyclical developments and the exchange rate. In the major countries, therefore, the emphasis on strict control of the aggregates has diminished, supplanted by more flexible conduct of monetary policy. Shifts in the demand for money, produced in part by financial innovation, were more frequently reflected in the evolution of monetary aggregates than in interest rates.

In the United States and the United Kingdom, the two countries where quantitative targets have been given greatest prominence in framing monetary policy since the beginning of the eighties, the aggregates overshot the targets by a wide margin in 1985. According to the Federal Reserve, the overshooting of the target for M1 was the result of a shift in the allocation of financial savings towards more liquid assets following a fall in their opportunity cost with respect to the components of the wider aggregates not included in M 1. The authorities' accommodation of the excessive growth of the money supply may also have been dictated partly by a desire not to impede the depreciation of the dollar, which in turn could check the deterioration of the current account deficit and help defuse protectionist pressures.

In the United Kingdom, sterling M3 overshot the upper limit of its target range in early 1985. In October the authorities suspended the monitoring of this aggregate, simultaneously announcing that they were discontinuing the traditional practice of mopping up liquidity through overfunding. Since then, the main target variable has been MO, the monetary base, which has behaved in the desired manner. The exchange rate has also acquired greater importance as an indicator for monetary policy.

In Germany and Japan, the expansion of the monetary aggregates in 1985 was in line with the targets. In Germany, the central-bank money stock increased by 4.6 per cent, thus keeping to the upper part of its target range for the year (3 to 5 per cent).

In France, despite corrective measures at mid-year, the growth in M2R continued to exceed the target level, mainly because of substantial money creation via the external sector, while domestic credit kept to the target growth path. Only in November did the authorities increase the reserve requirement while simultaneously lowering the intervention rate in order to prevent excessive overshooting.

Fiscal policy. — General government financial balances for the seven major industrial countries showed a deficit of 3.5 per cent of GDP, the same as in 1984. The budget deficit increased in the United States and Italy but contracted in Japan and Germany. In the United Kingdom too, despite the reduction in oil revenues, the deficit was narrowed thanks to public spending cuts. In France and Canada, the ratio of the budget deficit to GDP was unchanged.

The OECD's indicators, which adjust budget balances for their cyclical component, also show that the major industrial countries continued to be divided into two groups — the United States, Canada and Italy with expansionary fiscal policies and the others with restrictive stances.

In the six years since the end of the seventies, the government budget deficit has been reduced by 3.5 percentage points with respect to GNP in Japan and by more than 1.5 points in Germany, while it has remained virtually unchanged in the United Kingdom. In the United States, Canada and Italy the deficit increased by more than 4 percentage points over the same period. These results reflect the determination of some industrial countries in pursuing a medium-term strategy of fiscal restraint aimed at slimming the public sector and reducing the budget deficit. In most cases, however, the public sector's weight within the economy has not diminished. Nowhere was the ratio of total tax revenues to GDP lower in 1985 than in 1979, although the increase was much smaller in the United States than in the other major countries (half a point with respect to GNP, as compared with a high of 9 points for Italy). The only country in which public expenditure declined as a share of GDP, and only modestly at that, was Germany. The only other industrial country to make progress in cutting the incidence of government revenues and expenditures was the Netherlands, and the overall importance of the public sector there remains very great indeed.

On the revenue side, the combined effects of fiscal drag and tax policy varied significantly from one economy to another.

On the expenditure side, many countries had difficulty in holding down spending for welfare and servicing the public debt. Cuts in welfare benefits met considerable political and institutional opposition, while the large and growing public debt and the high cost of borrowing caused interest payments to increase rapidly.

OECD and IMF projections for 1986 indicate that the fiscal impact should be moderately restrictive in the major industrial countries taken as a whole. There should also be an attenuation of the divergence between the United States, where the effects of the recently inaugurated strategy of budgetary discipline should begin to make themselves felt, and the other countries, where a gradual easing of the restrictive stance is expected, except in Japan.

In the United States, the Gramm-Rudman-Hollings balanced-budget amendment of December 1985 lays down a schedule for the automatic reduction of the federal deficit, which should shrink to $172 billion in the current fiscal year and subsequently diminish by $36 billion a year to reach balance by fiscal 1991. In Germany the general government deficit should decline to less than 1 per cent of GDP this year. The discretionary impact of the fiscal stance should prove slightly expansionary, however, as a result of the application of the first stage of the income tax reduction programme, with tax cuts amounting to 0.6 per cent of GDP. In the United Kingdom the budget objective for the current fiscal year is to decrease the public sector borrowing requirement to 1.75 per cent of GDP, or slightly less than had been planned in last year's budget.

Oil and the world economy

The sharp drop in oil prices early in 1986 should lend renewed vigour to the expansion of world output and further reduce inflation rates.

The impact effect on current payments balances of an oil price in line with the most recent forecasts by the leading international agencies — $16.00-$17.50 a barrel on average for 1986 — is estimated, volumes remaining unchanged, at savings of about $60 billion (equivalent to 0.7 per cent of GNP) for the industrial economies and $18 billion for net oil-importing LDCs. The oil-exporting countries would lose $70 billion in revenues, and other net oil exporters, including the Soviet Union, would lose another $8 billion. Assuming that the consumer prices of oil products fall by as much as crude oil prices and disregarding the repercussions on the prices of other energy products, the immediate impact on inflation in the industrial countries should be a reduction of about 1.6 points in the domestic demand deflator.

The complex second-round interactions have been explored by the IMF and the OECD assuming average crude oil prices of $16.00 and $17.50 a barrel, respectively, for 1986 and $15.00 for 1987. Their projections also postulate exchange rates constant at their March 1986 levels and unchanging fiscal policies and monetary growth targets. These forecasts are given in Table 2.

Table 2

FORECASTS OF MAIN MACROECONOMIC VARIABLES BY GROUPS OF COUNTRIES

		Inflation (1)		Real domestic demand		Real GNP/GDP		Current payments balance (2)	
		1986	1987	1986	1987	1986	1987	1986	1987
		(change in %)						*(billions of dollars)*	
Industrial countries	(a)	3.5	2.8	3.5	3.3	3.3	3.0	−20	−35
	(b)	2.8	2.9	3.6	3.4	3.0	3.2	14	−9
of which: United States	(a)	3.3	2.8	3.3	3.5	3.0	3.8	−145	−130
	(b)	3.1	3.1	3.6	3.3	2.9	3.6	−111	−109
Japan	(a)	0.5	0.3	4.0	3.8	3.3	3.3	80	75
	(b)	0.5	1.3	4.2	4.4	3.0	3.2	72	62
Germany	(a)	—	−0.3	4.5	4.3	3.5	2.5	30	20
	(b)	—	1.0	4.1	3.6	3.7	2.7	25	20
European countries	(a)	4.8	3.8	3.5	3.3	2.8	2.3	60	30
	(b)	2.6	3.0	3.6	3.0	2.9	2.5	64	48
Non-oil LDCs	(a)	....	....	....	....	....	....	....	....
	(b)	32.2	15.8	....	....	4.0	4.6	−25	−27
Oil-exporting countries	(a)	....	....	....	....	....	....	....	....
	(b)	8.2	7.5	....	....	−0.1	−0.3	−44	−31

Sources: OECD and IMF.
(a) OECD: assuming oil prices averaging $17.50 a barrel in 1986 and $15.00 in 1987 and nominal exchange rates unchanged at the levels obtaining at the beginning of March 1986. — (b) IMF: assuming oil prices averaging $16.00 a barrel in 1986 and $15.00 in 1987 and real exchange rates unchanged at the levels obtaining at the beginning of March 1986. — (1) For the OECD, the private consumption deflator; for the IMF, consumer price index. — (2) For the IMF, including official transfer payments.

On these postulates, the overall effect on the industrial countries would be positive. Inflation would average less than 3 per cent in 1987, some 2-2.5 points lower than would be the case if crude oil prices held at their 1985 average. The decline in import prices, in fact, should be transmitted to domestically produced oil and to alternative energy sources, amplifying the initial effect and imparting a disinflationary impulse to wages and salaries. These results are based on the assumption that lower costs will be fully passed on to prices. If instead some countries opted to use part of the improvement in the terms of trade to reduce the budget deficit, inflation would slow less rapidly there, which might entail shifts in competitiveness and changes in balances of payments.

Domestic demand should expand at a rate of 3.5-3.6 per cent in 1986 and 3.3-3.4 per cent in 1987. In the scenario described here, the demand stimulus stemming from the improvement in the terms of trade is supplemented by the positive impact of the lower interest rates that the reduction in inflation should generate endogenously, at least in the short run, for given rates of growth in monetary aggregates. This stimulus would vanish if policymakers decided to revise their monetary targets in line with progress in disinflation. If monetary policy stances were to differ from country to country, it would affect interest rate differentials, influencing exchange rates and consequently the current account positions. Budget policies will be equally important in determining the extent of the demand stimulus; overall, they may prove to be more restrictive, in that the oil and gas producers (the United Kingdom, the United States, Norway, Canada) might seek to offset the decline in oil revenues by increasing taxes or cutting expenditure, while other countries might decide to transfer part of the benefit to the public finances.

The OECD and IMF scenarios indicate that the rate of growth in GDP would accelerate between 0.6 and 0.8 points in each of the two years, to about 3.0 per cent. The stimulus from domestic demand should more than offset the negative impact of reduced exports to the oil-exporting countries, reflecting the assumed slower adjustment of expenditure there than in the industrial countries. According to the IMF, the current payments balance for the industrial countries as a group should improve substantially, from a deficit of $54 billion in 1985 to a $14 billion surplus in 1986, then register a modest deficit again in 1987. The OECD estimates a smaller improvement of about $40 billion in the first year.

The non-oil LDCs will benefit most from the decline in international interest rates and the increased import demand from the industrial countries. Overall, in any case, the positive effects of the decline in oil prices will be modest. In fact, only a few of these countries will manage to increase real incomes, while others, the most heavily indebted, will use the additional availability of resources to improve their external financial positions.

For the oil exporters, the decline in oil revenues will presumably require a downward adjustment in both imports and growth rates. The speed and magnitude of the adjustment will vary from country to country. Some, for the most part the Gulf states, which still have trade surpluses for the moment, will be able to finance part of the fall in foreign exchange earnings by running down reserves. Other more heavily indebted countries, such as Mexico, Venezuela and Nigeria, will have to trim their imports much more quickly because of the rigid constraints on further borrowing to which they are subject. For them, the cost of the adjustment in terms of growth prospects will be much heavier. Average income for the oil-exporting countries will presumably decline over the next two years, while their overall deficit on current account will be much larger: \$44 billion in 1986 and \$31 billion in 1987, as compared with \$6 billion in 1985.

EXCHANGE RATES AND WORLD TRADE

Exchange rates

The dollar, the yen and the Deutschemark. — Events in 1985 were dominated by the reversal of the trend in the dollar exchange rate, which the monetary authorities of the main industrial countries helped bring about by means of exchange market intervention and by modifying the stance of monetary policy. The coordinated use of appropriate instruments made it possible to correct the substantial exchange rate distortions that had developed between the major currencies over the preceding four years.

The first phase of concerted intervention took place at the end of February 1985. The aim on that occasion was to overturn expectations of an unstoppable appreciation of the US dollar that did not take sufficient account of fundamentals in the major economies. The subsequent decline in the dollar was induced by the steady deterioration in the balance of payments on current account and the fall in US interest rates, which declined more rapidly than those in other important industrial countries until July. However, the dollar decline did not seem fast enough to have a significant impact on the US current account deficit within a reasonable period of time.

In order to give fresh impetus to the move towards better balance between the exchange rates of the major currencies, the monetary authorities of the five leading industrial countries met in New York on 22 September and decided to take further initiatives, publicly announcing the objectives of their action. Substantial concerted exchange market interventions were carried out in the weeks that followed. As with the interventions at the end of February, the Bank of Italy made a substantial contribution. There was also a pronounced adjustment of monetary policy in Japan, where interest rates were encouraged to rise, producing a favourable differential between real rates there and in the United States. The positive interest rate differential between short-term dollar and DM assets narrowed, but did not disappear entirely.

The action of the monetary authorities achieved its primary objective: by April 1986 the nominal effective exchange rate of the dollar against a weighted basket of thirteen currencies was 25 per cent below the peak of March 1985, when it had shown an appreciation of

46 per cent in relation to the 1980 average. The depreciation vis-à-vis the yen and the Deutschemark was about 34 per cent. However, the average effective exchange rate for 1985 was still 3.2 per cent above that for 1984. It is estimated that in the twelve months to March the real exchange rate of the dollar declined by about 20 per cent when measured on the basis of the wholesale prices of manufactured goods. Over the same period the real depreciation against the yen and the Deutschemark was just under 30 per cent, but on average for 1985 the effective rate showed an appreciation of 1.5 per cent over the preceding year.

The nominal effective exchange rate of the yen rose by 25 per cent between March 1985, the turning point of the dollar, and April 1986, when the dollar fell below 170 yen, its lowest level since the Second World War. In the twelve months that ended in March, the real exchange rate of the yen rose by 18 per cent. The yen's performance reflected not only the effects of the initiatives in the monetary field but also the success in controlling inflation and the continued improvement in Japan's current account surplus, which reached almost $50 billion last year.

The nominal effective exchange rate of the Deutschemark rose by 7 per cent between March 1985 and April of this year but remained unchanged between 1984 and 1985 on an annual average basis. There was a real appreciation of about 6 per cent in the twelve months to April and a slight depreciation (1.3 per cent) between the 1984 and 1985 averages. The appreciation that began in the early spring of 1985 had its roots in the overall improvement in the German economy; prices were virtually stable, the current account surplus had risen substantially to more than $13 billion in 1985 and the expansion in activity that began in the second half of the year was expected to continue in 1986. The confidence in the Deutschemark is demonstrated by the considerable increase in long-term capital inflows, which virtually doubled to DM 52 billion in 1985, almost offsetting the traditionally large outflow of long-term funds from Germany.

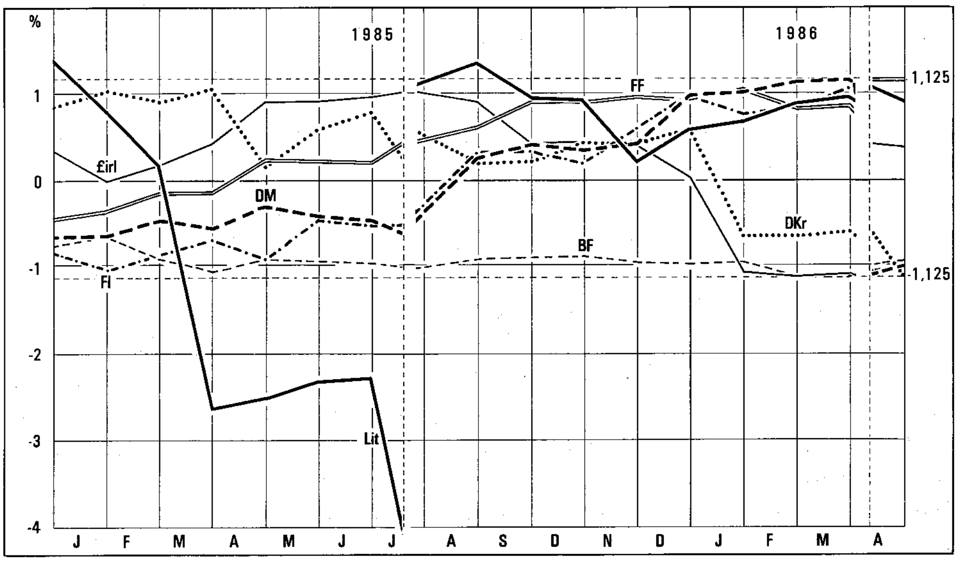
The European Monetary System. — The EMS exchange rate system coped fairly easily with the changed situation, marked by the pronounced and rapid weakening of the dollar, which some observers had thought might cause serious dislocation.

In the first half of last year the position of most of the currencies except the lira remained stable within the band of fluctuation. The lira weakened noticeably in February and March, when the trend of the dollar exchange rate reversed, and again in the first three weeks of July (Figure 2). After the realignment on 20 July the lira moved above the narrow band of fluctuation, whereas the Deutschemark and the Dutch guilder rose towards the upper threshold. As the dollar continued to depreciate at a rapid pace, expectations of a further realignment became widespread from mid-November onwards, prompted by the approach of elections in France, public statements by economic policymakers in major EEC countries and, above all, the perception that almost three years of relative exchange rate stability had produced significant variations in relative competitive positions that had not been offset by the adjustments in central rates at the July realignment.

Figure 2

EMS EXCHANGE RATES

(percentage changes with respect to central rates)



(1) Realignment of 20 July 1985. — (2) Realignment of 6 April 1986.

The Deutschemark, the Dutch guilder and the French franc moved towards the upper limit of fluctuation, whereas the Belgian franc weakened, followed by the Irish pound and the Danish krone. The lira lost ground temporarily but then returned to the upper part of the narrow band. During this phase, the positive differential between real short-term rates in France and Italy and those in other member states continued to narrow, so that the positions of the French franc and the lira were determined primarily by the support interventions by the French and Italian central banks. Money market rates in Belgium and Ireland rose, differentials vis-à-vis the other EMS countries widened and substantial exchange market interventions were carried out. Downward pressure on the lira continued to mount, but as the Italian monetary authorities considered its exchange rate within the EMS to be appropriate, they adopted exchange control and credit measures on 16 January of this year.

The pressures on the EMS currencies eased from the middle of January onwards. Nevertheless, the tendency for the Deutschemark, the French franc, the lira and the Dutch guilder to remain near the upper limit and for the other currencies to settle at the opposite extreme became more marked. After the French elections the market perceived that the political factors that had prevented adjustment of the franc exchange rate in the preceding months no longer applied. In the second half of March the speculative pressures on the French currency became significant and the Bank of France had to intervene on a substantial scale to support it; short-term rates on Euro-francs rapidly rose above 20 per cent. The Belgian franc and the Irish pound also came under strong downward pressure. The Italian lira, by contrast, remained in the uppermost part of the fluctuation band, with the Bank of Italy making intervention purchases of Deutschemark and smaller purchases of dollars. On Thursday 3 April the Bank of France withdrew from the market at the close of European trading; the following day the official quotations of the European currencies were suspended to prevent speculative movements and the authorities called for the renegotiation of central rates.

The new official exchange rates decided by the Ministers of Finance and central bank Governors of the EEC countries came into effect on 7 April 1986; they provided for the bilateral exchange rate of the French franc to be devalued by 5.8 per cent against the Deutschemark and the Dutch guilder, by 4 per cent against the Belgian franc and the Danish krone and by 3 per cent against the lira and the Irish pound. In the next few days the Deutschemark and the Dutch guilder adopted a position close to the lower limit, whereas the French franc and the lira were near the upper threshold of the narrow band.

The exchange rate of the pound sterling displayed particularly large fluctuations in 1985. There was an effective appreciation of 15 per cent in the first seven months of the year as a result of the rise in interest rates induced by central bank action in January. The subsequent fall in interest rates and oil prices caused an equally pronounced depreciation in the second half of the year and especially in the early months of 1986; in February of this year the pound returned to the level of twelve months previously. The downward trend was countered by inducing a renewed increase in interest rates.

World trade

In 1985 world merchandise trade expanded at about the same pace as output (2.9 per cent), whereas in 1984 it had risen at a rate of 8.7 per cent, twice that of production. The slowdown in world trade was due primarily to two factors: first, the weakening of the stimulus that had derived in 1984 from the rapid growth in US imports, which came down from 24 to 9 per cent last year, and secondly the stagnation in Japanese imports, which had risen by 11 per cent in 1984. Since the volume of imports by European countries increased at about the same rate as in the preceding year (5.6 per cent), the overall rate of growth in industrial countries' imports fell from 13 to 5 per cent.

The pronounced slowdown in world trade in 1985 and the accompanying profound change in the structure of world demand by region and type of product affected the exports of the main country groups differently. The impact was particularly severe not only on exports by oil-exporting countries, which declined by 4.1 per cent, but also on the exports of the other developing countries, which increased by only 3.4 per cent, compared with 12 per cent the previous year.

The rate of growth of industrial countries' exports also slowed down appreciably, falling from 9.3 per cent in 1984 to 3.9 per cent last year as a result of the weakening of demand from outside the area and the contraction in trade within it. Italy achieved the highest rate of growth among the seven main industrial countries (7.5 per cent), but the other countries also recorded increases in market share, including France and the United States, whose exports actually declined by 1 per cent owing to their substantial loss of competitiveness in recent years.

The fall in the average dollar unit values of world trade that had begun in 1981 continued last year. Whereas the prices of manufactures rose by 1 per cent after falling steadily for four years, those of non-oil raw materials declined by as much as 12.2 per cent and oil prices decreased by 4.4 per cent. Combined with the change in the composition of imports and exports of the main country groups, the variations in international prices led to an improvement of 2 per cent in the terms of trade of the industrial countries and a pronounced 4 per cent deterioration in those of oil-exporting developing countries. These shifts in the terms of trade caused the trade deficit of the industrial countries to contract by $6.5 billion to about $38 billion and the surplus of the oil exporters to decline by about $5 billion to $64 billion in 1985.

The other developing countries suffered a less severe deterioration of 1.2 per cent in their terms of trade, though this was enough to wipe out a large part of the gains of the previous two years. The events of last year fully account for the increase in the trade deficit of these countries to $24 billion, compared with $20 billion in 1984.

CAPITAL MARKETS, EXTERNAL DEBT AND INTERNATIONAL LIQUIDITY

International capital markets

Gross medium and long-term lending by the international markets expanded strongly to $257 billion in 1985, an increase of 30 per cent over the preceding year. Net lending increased less rapidly, from $145 billion to $170 billion.

The trend towards securitization gained momentum. Bond issues and back-up facilities accounted for more than 80 per cent of total gross lending, compared with less than half at the beginning of the decade. Bond issues came to $168 billion, a rise of 50 per cent over 1984, while back-up facilities totaled $47 billion, five times the level recorded in 1983. Syndicated credits, by contrast, declined for the third year in succession to stand at $42 billion, less than half the peak figure recorded in 1982; of this amount, $7.1 billion was granted under debt restructuring agreements.

The concentration of lending on the industrial countries, which had begun in 1982 with the debt crisis in the developing countries, grew more pronounced in 1985. This tendency is partly a reflection of the increase in capital flows between industrial countries caused by the emergence of large current account disequilibria within the area and the growing integration of domestic and international capital markets. Industrial countries absorbed 81 per cent of total gross lending, compared with 76 per cent in 1984. By contrast, the share of non-oil developing countries declined from 14 to 9 per cent, and their borrowing also fell in absolute terms. Direct lending to eastern European countries expanded considerably to more than $5 billion, compared with $3.3 billion in 1984.

The increasing securitization of capital flows was accompanied by major changes in the role of the commercial banks in international markets. The decline in the quality of their assets, primarily as a result of the debt crisis in developing countries, obliged the banks to tackle the problem of capital adequacy, partly in order to conform with the guidelines of the supervisory authorities. On the one hand they slowed down the growth in their traditional deposit-taking and lending activities and on the other they increased their capital bases.

The need to improve their capital ratios prompted the commercial banks to engage in operations that generated fee income but did not increase the size of their balance sheets. They stepped up their trading in bonds and other securities and developed new operations that were not necessarily reflected in their balance sheets, since the commitments to which they gave rise were contingent on future events. Operations of this kind include note issuance facilities, interest rate and currency swaps, financial futures and options. At the same time, other financial intermediaries and even non-banks entered segments of the market that had traditionally been the preserve of the banks, such as the deposit market. This led to an overlapping of the roles played by the various kinds of intermediary and a heightening of competition in the financial services market, which in turn created a further strong incentive to innovate.

The external debt problem

The debt situation of the developing countries again became acute last year, after signs of an improvement in 1984. The heightened difficulties of the most heavily indebted countries and the continuing reluctance of the international financial markets to grant them new loans made it clear that there was a need to reinforce the strategy for dealing with the debt crisis. Above all, three years into the crisis it did not seem possible to continue with adjustment primarily on the basis of limiting imports, investment and consumption in the developing countries.

The plan put forward by US Treasury Secretary Baker at the Annual Meetings of the IMF and the World Bank in Seoul in October last year ("A Program for Sustained Growth") acceded to the widely-expressed view that a return to growth in the debtor countries and the restoration of normal relations with creditors were essential if the debt problem was to be resolved in the medium term. The plan represents a turning-point in the formulation of the strategy for tackling the debt problem and an important benchmark for overcoming the crisis in the years ahead.

At the end of 1985 the external debt of debtor developing countries totalled $888 billion, an increase of 5.7 per cent over 1984. The ratio of debt to exports of goods and services rose from 153 per cent in 1984 to 163 per cent, mainly as a result of a contraction in exports.

Despite debt restructuring and the fall in interest rates, the debt service payments of the indebted developing countries rose by more than $5 billion to $131 billion, of which $72 billion represented interest payments. The ratio of debt servicing to exports deteriorated, rising from 23 to 24 per cent for the debtor developing countries as a whole and from 42 to 44 per cent for the group of fifteen heavily indebted countries affected by the Baker Plan.

Net external lending to developing countries contracted for the fourth consecutive year. In 1985 it was only slightly above one quarter of the $100 billion recorded in 1981, owing mainly to the substantial and continued reduction in net credit from private sources, which fell from $73 billion in 1981 to $13 billion in 1984 and $11 billion last year. In the case of the fifteen heavily indebted countries, the reduction in total net external lending was even more pronounced, falling from $62 billion in 1981 to $1 billion in 1985, when net outflows from private sources were recorded. Moreover, in recent years the reduction in external lending to developing countries has been compounded by capital flight on a massive scale. The IMF estimates that capital outflows from this group of countries totaled about $36 billion in 1982 and were of the order of $10 billion last year. The outflows from Latin America appear to have been particularly large.

The pronounced contraction in credit from private sources was not alleviated by expansion in other flows of external finance. Official transfers, which had stagnated at around $13.5 billion since 1981, increased slightly to $16 billion last year; direct investment remained practically unchanged at about $10 billion.

IMF credit, which was granted entirely to indebted developing countries, came to $4 billion, 50 per cent less than in 1984; net of considerable repurchases by member countries, such credit fell to $0.2 billion, compared with $5 billion in 1984 and more than $11 billion in 1983.

The level of lending by multilateral development banks was unsatisfactory, partly as a result of the contraction in investment programmes by developing countries and the difficulties they encountered in financing their share of the cost of such projects.

International liquidity

Official reserves, defined as the sum of foreign exchange, SDRs and reserve positions in the IMF, totaled $441 billion at the end of 1985, an increase of 11 per cent over 1984; expressed in SDRs, however, they recorded a slight decrease (1 per cent) owing to the depreciation of the dollar.

The increase in total official reserves was due largely to the expansion in foreign exchange reserves ($38 billion). IMF-related reserve assets rose by almost $6 billion, but as a proportion of total official reserves they decreased slightly, to stand at 14.2 per cent at the end of the year.

In 1985 and the early months of this year discussions continued within the Group of Ten and the IMF on the role of the SDR in a system in which borrowed reserves constitute a substantial part of the total. Moreover, not only is international credit unavailable to countries that have no access to the markets, but it does not necessarily provide adequate liquidity for the world economy as a whole, given potentially unstable market conditions. In this context, Italy continued to assert the validity of an internationally-administered mechanism for the creation of official reserves and the need to resume allocations of SDRs on the basis of a stable quantitative criterion that would gradually increase the proportion of total reserves in the form of SDRs and the ratio of owned reserves to borrowed reserves over the long term.

THE ITALIAN ECONOMY

DEMAND, OUTPUT
AND THE BALANCE OF PAYMENTS

The results for 1985

The Italian economy has been expanding since 1983, but it grew a little more slowly last year than in 1984 (by 2.3 as against 2.8 per cent). This was in line with the rates recorded by the other EEC countries, though Italian domestic demand again rose faster, with the differential in the rates of increase widening further in the early part of the year and then reversing.

Employment rose by around 100,000 as a result of an increase of 330,000 in services and decreases of respectively 89,000 and 135,000 in agriculture and industry. The number of employees rose by 1 per cent, while self-employment contracted, thus reversing the trend that had prevailed since the beginning of the eighties. Nonetheless, the 0.5 per cent increase in total employment was insufficient to absorb all the increase in the labour force, which followed a similar pattern to that of the last few years. Female workers accounted for over two thirds of the expansion and the growth in the labour supply in the South of Italy accelerated again after easing in 1984. The national unemployment rate rose from 10.4 to 10.6 per cent while that for the South of Italy rose by 0.8 points to 14.7 per cent, even though this area accounted for over 80 per cent of the new employment. Moreover, the female unemployment rate in the south rose to 25.1 per cent and that for people aged less than 29 increased to 35.8 per cent (compared with respectively 13.7 and 21.1 per cent in the centre-north).

The downturn in inflation continued, but progress was slow. The average annual rate of consumer price inflation, which had come down by 4 points in 1984, slowed by 1.6 points (from 10.8 to 9.2 per cent), which was 2 points less than planned. Over the year it fell by barely half a point to 8.8 per cent in December. The small reduction in consumer price inflation reflected both the slowness with which the prices of manufactures decelerated in 1984 and the first half of 1985 and the failure of the twelve-month increases in administered prices and public service charges to come down any further. The reduction in wholesale price inflation was more pronounced and came primarily in the second half of the year as a result of the fall in industrial raw material prices. The average annual increase amounted to 7.3 per cent, which was 3 points less than that recorded in 1984. The inflation differential vis-à-vis the other OECD countries, which had narrowed sharply in 1984, improved further for consumer prices but widened again for wholesale prices, to stand at respectively 5.5 points and 6 points at the end of the year.

The deficit on the current account of the balance of payments rose from 5.1 to 8.0 trillion lire. The deterioration was primarily attributable to the increase in the trade deficit in the first half of 1985 and was actually less pronounced than had been forecast at the beginning of the year owing to the marked depreciation of the dollar and the slower pace of economic activity in Italy. The average annual increase in import volume amounted to 9 per cent, which was slightly higher than the corresponding figure for exports and much larger than the growth in GDP. The trade deficit for the year was held down to 23 trillion lire, compared with 19 trillion in 1984. Among the invisible items, the rise in the surplus on tourism was annulled by the increase in debt servicing and the decrease in the surplus on other services and transfer payments. The financing of the current account deficit led to a worsening of Italy's net external debt; excluding the gold reserves, this approaches $32 billion, in part because a larger proportion of liabilities were denominated in currencies other than the dollar.

The budget again provided an expansionary stimulus to economic activity, though it was less strong than in 1984. Both the net borrowing and the current deficit of general government expanded in relation to GDP, as did the state sector borrowing requirement, even when the settlements of past debts are excluded.

Though the basic objective of exchange rate policy remained that of using the Community agreement to foster the slowdown in inflation and encourage firms to improve their efficiency through internal measures, it proved possible to allow the lira to slide gradually within the EMS to help maintain price competitiveness. Advantage was taken of the periods of dollar weakness to minimize the impact of imported inflation. The real exchange rate, calculated on the wholesale prices of manufactures, remained unchanged on average but dropped by about 1 point over the year, primarily as a result of the depreciations in February and March and the realignment in July.

The lira prices of the foreign inputs of industry excluding construction rose by 7 per cent. The steady fall in raw material prices was actually outweighed by the depreciation of the lira against the dollar during the year. The prices of domestic inputs went up by 8 per cent and unit labour costs by 7.3 per cent. The latter figure was the result of an 11 per cent increase in labour costs per employee (due in part to the cut made in the relief on employers' social security contributions immediately after the realignment of the lira in the EMS) and a 2.4 per cent improvement in productivity. Total unit costs rose by 7.3 per cent, half a point less than output prices. Consequently, profit margins widened further.

Households' disposable income expanded by 1.5 per cent in real terms. Above-average increases were recorded in entrepreneurial income and income from self-employment, while gross income from employment rose by about 1 per cent. The steady growth in incomes coupled with the increase in households' wealth in real terms had an expansionary effect on consumption, which rose faster than disposable income (2.0 as against 1.5 per cent). There was thus a small increase in the propensity to consume.

Investment activity proceeded at a rapid pace and, with wide margins of unutilized capacity, continued to be directed towards modernizing and reorganizing plant and production processes. The improvement in profit margins and the favourable capital market conditions enabled firms to finance their investments with resources they had ploughed back or raised through share issues.

Fixed investment rose by 4.1 per cent on average, with that in machinery and equipment increasing by over 10 per cent so that its ratio to GDP matched both the peak levels of the late seventies and the current performance of the other industrial countries. The increase in stocks was strictly confined to meeting the needs of production, partly on account of the high cost of finance.

Exports rose by 8 per cent in volume compared with 1984. The growth was concentrated in the second half of the year, when cyclical conditions favoured exporting; sales abroad were also stimulated by the gains in competitiveness Italy made in European markets, which offset the losses it suffered in the dollar area. The gap between the import and export growth rates narrowed.

As regards the domestic sources of income, agricultural value added at constant prices declined by 2.4 per cent and that of construction by 1.4 per cent. The 2.3 per cent overall increase in income was attributable to the increases in the value added of services and industry excluding construction (up respectively by 4.5 and 1.7 per cent).

The phase of the cycle through which the Italian economy has been passing in the last few years has encouraged relatively faster growth in services, in line with the longer-term tendency common to both the centre-north and the less industrialized south.

Over the last five years the growth in employment in services in the southern regions exceeded the loss of jobs in agriculture and industry, whereas in the centre-north it only just prevented an overall fall. Employment in both market and non-market services expanded faster in the south than in the centre-north. The upturn was fueled primarily by distribution and catering services, which appear to be overgrown in the south. This confirms the hypothesis that the expansion of some branches of services reflects an excess supply of labour rather than a response to actual demand.

The changes in the demand for labour that have resulted in employment in private and public services accounting for 60 per cent of the total in both the north and the south corresponds to developments in the structure of the economy. In both parts of the country the ratio of investment in market services to GDP has been rising for several years, albeit faster in the north than in the south. At the national level the real gross output of market services net of rents rose from 34 per cent of value added at factor cost in 1976-80 to 36 per cent in 1981-84 and exceeded 37 per cent last year. The increase in the share of services was even sharper in the southern regions, though the structure of the economy is changing more slowly there, since the services sector mainly comprises traditional activities (Table 3).

The decline in the importance of industry and the rise in that of services, coupled with even more pronounced shifts in the pattern of employment, have been evident to a greater or lesser extent in the changes that have occurred in all the leading industrial countries.

In Italy the transformation and rationalization of production made necessary by the difficulties industry encountered in the seventies have included the transfer of some functions previously performed within industrial companies to the market-services sector. The average annual increase in the number of workers providing business services exceeded 4 per cent in 1980-83 and 15 per cent in 1984-85.

The changes in the level and composition of the demand for labour have been in response to the efficiency challenge with which Italy's economy has also had to grapple. In addition, however, there is the pressing and difficult problem of achieving a significant reduction in unemployment, which will require not only high and stable growth rates but also a much closer alignment with the other industrial countries as regards inflation and the budget deficit.

Table 3

INVESTMENT, OUTPUT AND EMPLOYMENT

	Agriculture	Industry	Services	Services excluding dwellings	Non-market services	Total
			Value added at factor cost *(percentage composition)* **Italy**			
1976-80	6.7	42.1	40.2	34.3	11.0	100.0
1981-84	6.8	40.9	41.6	35.8	10.7	100.0
1985	6.4	40.0	43.1	37.5	10.5	100.0
			South of Italy			
1976-80	14.1	29.9	40.0	33.1	16.0	100.0
1981-84	14.3	28.8	41.1	34.9	15.8	100.0
			Investment/GDP *(percentage)* **Italy**			
1976-80	1.3	4.6	9.5	5.3	1.6	17.0
1981-84	1.1	4.3	9.8	5.8	1.6	16.8
1985	1.0	4.3	10.1	6.4	1.6	17.0
			South of Italy (1)			
1976-80	0.7	1.1	2.8	....	0.6	5.2
1981-84	0.6	0.9	2.9	....	0.6	5.0
			Employment *(change in thousands)* **Italy**			
1978-80	−77.3	26.8	232.9			182.4
1981-84	−118.1	−164.0	322.1			40.0
1985	−129.5	−147.4	371.2			94.3
			South of Italy			
1978-80	−47.8	19.0	101.6			72.8
1981-84	−71.1	−17.2	118.5			30.2
1985	−27.6	−33.0	137.8			77.2

Source: Istat.
(1) In relation to the GDP of all Italy.

Oil and the prospects for the Italian economy

The collapse of the oil price and the further depreciation of the dollar were the major developments in the early months of 1986. Italy's terms of trade have improved by 5 per cent compared with the last quarter of 1985 and the prospects for the Italian economy in 1986 are now brighter as regards prices, the balance of payments and growth.

Price inflation has started to slow down again, and fairly sharply. In April the cost of living rose by 0.3 per cent over the month and by 6.6 per cent compared with April 1985. Despite increases in some public service charges, the average monthly increase in the cost of living over the first four months (0.5 per cent) was roughly half that in the year-ago period. Both in February and in March wholesale prices actually fell compared with the previous month, bringing the twelve-month rate of increase down to practically nil (0.3 per cent), for the first time since 1969. Raw material prices have been falling for some months now, but manufacturing prices are still showing a slight tendency to rise, thus preventing a narrowing of the inflation differential vis-à-vis the other major industrial countries.

The trade balance is beginning to reflect the pronounced improvement in the terms of trade. In the first quarter the deficit amounted to about 5.5 trillion lire, which was 2.5 trillion less than a year earlier. The improvement was almost entirely due to the reduction in the energy deficit, since the increase in the surplus on other goods was not material. The growing difficulties encountered by Italian exports to the OPEC countries and the dollar area have not yet been fully offset by the expected upturn in domestic demand in European countries.

Economic activity appears to be fueled primarily by domestic demand. In the first quarter of 1986 the seasonally adjusted index of industrial output was more than 2 per cent higher than in the last quarter of 1985. Over the coming months the improvement in the terms of trade is likely to stimulate further growth in domestic demand. In particular, after slowing in the second half of last year, investment can be expected to pick up strongly in response to firms' greater self-financing capacity. GDP growth in 1986 could amount to around 3 per cent and be coupled with a 200,000 rise in employment, lower-than-targeted inflation rates, a balance-of-payments surplus and a consequent reduction in Italy's high level of external debt.

On the other hand, it appears that no progress has yet been made in correcting the structural imbalances underlying the public sector borrowing requirement. The fall in oil prices will produce only a small reduction in the budget deficit net of interest payments. The ratio of this aggregate to GDP is still much higher than in any other major industrial country and the reduction that has been made (see the chapter on Public Finances) is the result of fiscal measures that will have a once-and-for-all effect in 1986.

A far-reaching reorganization of public expenditure and a faster reduction in the budget deficit continue to be necessary conditions for faster and sustained growth in income and employment.

A prerequisite for improving the competitiveness of the economy as a whole is that resources should also be used efficiently in the sectors not exposed to international competition. In turn, it is essential that Italy be able to increase the funds available for investment without creating current external deficits if the industrial base is to grow and the rationalization of existing private and public services is to be accompanied by an expansion in infrastructures.

The fact that the growth in the labour force is primarily in the southern regions and that these still suffer from considerable external diseconomies indicate which part of the country needs to be given preferential treatment in locating investment.

The high level of industrial profits that the improved terms of trade will help to produce in 1986 could permit a move away from the pattern of investment typical of the last few years by facilitating a widening of the productive base. Since the end of the seventies the need to increase the productivity of the existing capital stock has led firms to concentrate investment in the centre-north, with the result that the rate of investment has declined almost continuously in the southern regions. The nature of the programmes many industrial firms implemented to modernize and reorganize their production not only provided scope for cutting costs but also made it easier to adjust capacity rapidly. If the expansion in production facilities should occur in the areas where they are already mainly located, the South of Italy would be seriously disadvantaged.

DOMESTIC DEMAND

Households' consumption

Consumption by Italian households expanded by 2.0 per cent in volume terms in 1985, after a 2.1 per cent expansion in 1984. In value terms, the increase was 11.7 per cent (Table 4).

Table 4

APPROPRIATION ACCOUNT FOR HOUSEHOLDS

	1983	1984	1985	
	% changes	% changes	% changes	billions of lire
Gross domestic earnings	13.8	11.7	10.7	273,285
of which: general government	*16.5*	*14.7*	*10.2*	*71,749*
Net labour income from abroad	10.4	10.8	−0.5	2,531
Gross income from unincorporated businesses and self-employment, dividends and other capital income	13.0	16.3	12.3	199,300
Net interest	19.4	22.7	4.9	41,700
Social security benefits	22.4	11.3	11.6	145,250
of which: paid by general government	*22.3*	*11.3*	*12.0*	*133,782*
Employees' social security contributions (−)	21.5	11.5	7.2	18,725
Self-employed workers' social security contributions (−)	16.2	14.3	11.9	8,899
Direct taxation (−)	25.9	10.1	10.7	85,700
of which: condonation of income tax evasion	*167.3*	*−76.3*	*−94.2*	*69*
surtax on imputed or actual rental income	—	*−84.0*	—	—
Other items	46.2	37.7	11.1	5,200
Gross disposable income	**14.2**	**14.4**	**11.1**	**553,942**
at 1970 prices (1)	−0.9	3.0	1.5	72,342
Domestic consumption of households	**14.6**	**13.4**	**11.7**	**422,103**
at 1970 prices	−0.5	2.1	2.0	55,124
Average propensity to consume *(percentage ratios)*	**76.5**	**75.8**	**76.2**	

Source: Istat and Bank of Italy estimates.
(1) Adjusted using the implicit price deflator of households' domestic consumption.

The real expansion of domestic consumption, which was slower than that registered in the late seventies, also held steady at about the 1984 rate; the rates of increase in spending on non-durables and semi-durables remained broadly unchanged, whereas purchases of consumer durables accelerated sharply. The expansion in consumer spending occurred despite the halving of the rate of real income growth, which was 1.5 per cent as against 3.0 per cent in 1984. The consequence was a slight increase in the propensity to consume, from 75.8 to 76.2 per cent.

The increase in consumer spending was encouraged by the consolidation of expectations of economic growth. What is more, households' net financial assets grew considerably faster than did disposable income, while on average for the year there was a further decline in inflationary expectations, and actual price rises also slowed down slightly. The resulting expansionary stimuli were partially counteracted by the brake on consumer expenditure deriving from persistently high real interest rates.

The increase in households' disposable income was attributable to income from unincorporated businesses, self-employment and capital, which again rose faster than all other components of income, though not to the same extent as in 1984. By contrast, gross wages and salaries expanded slightly less than overall disposable income. The share of the latter received from government, including interest payments and net of taxes and employees' social security contributions, was substantially unchanged.

Investment

Gross investment rose at a rate of 3.8 per cent, thus continuing the expansion begun in 1984. Fixed investment remained buoyant, rising by 4.1 per cent to pass the 1981 peak, but stockbuilding was slower, 393 billion lire at constant prices, compared with 416 billion in 1984.

The investment pattern in 1985 evidenced two distinct aspects of the Italian investment cycle over the past two years: first, an even more marked predominance of rationalization over expansion than in the previous cycle; and second, rapid capital formation in the services sector, where a modernization analogous to that carried out by large industrial firms in the late seventies appears to be taking place.

The former aspect is reflected in the increased pace of change in the composition of new fixed capital. The small rise in the share of GDP accounted for by investment — to 17.0 per cent, still lower than the 17.6 per cent registered in 1980-81 — in fact conceals divergences between the main components of demand for capital goods (Table 5). There was a further decrease in investment in housing (0.8 per cent) and a sharper decline in investment in public works (2.6 per cent) and in buildings for industrial uses or services (2.2 per cent). By contrast, investment in machinery and metal equipment and in motor vehicles increased by 11.4 per cent in 1985, following the revised Istat estimate of 15.1 per cent in 1984, so that the share of GDP for this component rose to 8.3 per cent, the highest level since 1970.

Table 5

GROSS FIXED INVESTMENT BY TYPE OF CAPITAL GOOD: 1970-1985

(as a percentage of GDP; at 1970 prices)

	1970-72	1973-74	1975-79	1980-81	1982-83	1984-85	1985
Machinery, metal equipment and transport equipment	7.2	7.8	6.7	7.7	7.1	8.0	8.3
of which:							
industrial and agricultural machinery	*2.8*	*3.2*	*2.4*	*2.4*	*1.8*	*1.6*	*1.7*
data processing machines (1)	*0.4*	*0.6*	*0.8*	*1.2*	*1.5*	*2.4*	*2.7*
transport equipment (2)	*1.8*	*1.8*	*1.8*	*2.2*	*2.1*	*2.1*	*2.1*
other (3)	*2.2*	*2.2*	*1.7*	*1.9*	*1.7*	*1.9*	*1.8*
Other goods and equipment (4)	1.0	1.1	0.8	0.8	0.6	0.6	0.5
Non-residential buildings (5)	6.5	5.9	5.2	4.9	4.8	4.5	4.4
Dwellings	5.8	5.1	4.4	4.2	4.0	3.8	3.7
Total	**20.5**	**19.9**	**17.1**	**17.6**	**16.5**	**16.9**	**17.0**

Source: Based on Istat data.
(1) Office and data processing machines. — (2) Apart from cars, trucks and trailers, this item includes ships, aeroplanes and railway and other rolling stock. — (3) Electrical goods, precision instruments, metal furniture and tools. — (4) Primarily wooden furniture, wooden and plastic appliances and glass manufactures. — (5) Includes both public works and buildings for industrial use and the production of services.

The speed with which production is being rationalized and fixed capital replaced and modernized is also demonstrated by a sharp acceleration in investment in office and data processing machinery. Such investment, which has expanded uninterruptedly since the mid-seventies, was some 70 per cent higher in 1984-85 than in the previous two years, while investment in production machinery failed to top the low level of 1982. As compared with the previous investment cycle, expenditure on data processors has doubled as a share of GDP and now substantially exceeds more traditional productive investment (2.7 as against 1.7 per cent of GDP). Hence, in the current cycle capital formation has been propelled by the installation of electronic machinery to monitor and control production, manage stocks and orders, automate office work and meet other information processing needs in industry and services. Spurred by persistently high real yields on financial assets, firms have directed their capital spending towards gains in productivity.

Table 6

PUBLIC AND PRIVATE GROSS FIXED INVESTMENT BY BRANCH OF ECONOMIC ACTIVITY

(at 19 70 prices)

	Billions of lire	Share of total %	Percentage changes					
	1985	1985	1980/1979	1981/1980	1982/1981	1983/1982	1984/1983	1985/1984
Agriculture, forestry and fisheries	864	5.7	0.4	−4.3	−7.7	−5.5	−0.8	−4.6
Private	*702*	*4.6*	*3.5*	*−2.7*	*−16.8*	*6.4*	*−21.7*	*17.2*
Public (1)	*162*	*1.1*	*7.8*	*−11.7*	*39.8*	*−42.2*	*129.1*	*−47.2*
Industry	3,922	25.7	14.9	−3.4	−11.7	−7.4	8.4	6.5
Private	*2,649*	*17.4*	*14.1*	*−6.5*	*−14.6*	*−13.7*	*13.5*	*8.1*
Public (2)	*1,273*	*8.3*	*17.3*	*5.0*	*−4.7*	*6.2*	*−0.6*	*3.4*
Market services (3)	5,728	37.6	12.1	4.4	−2.3	0.1	10.7	7.7
Private	*4,009*	*26.3*	*14.8*	*14.8*	*−8.6*	*−2.2*	*9.0*	*9.4*
Public (2) (4)	*1,719*	*11.3*	*4.6*	*4.6*	*18.4*	*5.9*	*14.6*	*4.0*
of which:								
Transport and communications	2,236	14.7	11.5	1.5	2.1	2.7	7.0	3.6
Private	*549*	*3.6*	*25.4*	*7.8*	*−21.2*	*−2.2*	*−11.9*	*1.3*
Public	*1,687*	*11.1*	*4.1*	*2.5*	*18.7*	*5.0*	*15.4*	*4.3*
Distributive trades and other services	3,492	22.9	6.3	5.1	−5.1	−1.8	13.3	10.5
Private	*3,460*	*22.7*	*6.1*	*5.2*	*−5.3*	*−2.2*	*13.7*	*10.8*
Public (4)	*32*	*0.2*	*28.6*	*3.7*	*6.4*	*45.2*	*−13.0*	*−11.1*
Dwellings	3,325	21.8	4.9	0.7	−4.5	−2.4	−0.7	−0.8
Private	*3,061*	*20.1*	*7.9*	*1.8*	*−5.6*	*−1.3*	*−3.9*	*0.1*
Public (5)	*264*	*1.7*	*−26.5*	*−15.3*	*14.8*	*−19.1*	*49.7*	*−10.5*
Non-market services	1,406	9.2	3.3	4.3	3.9	−10.2	6.0	1.1
Total economy	15,245	100.0	9.4	0.7	−5.2	−3.8	6.2	4.1
Private	*10,421*	*68.4*	*11.4*	*0.1*	*−9.8*	*−4.2*	*3.2*	*6.6*
Public	*4,824*	*31.6*	*4.4*	*2.1*	*6.8*	*−3.0*	*12.8*	*−1.1*

Source: Based on Istat data.

(1) State payments for investment in agriculture. — (2) Including state-controlled companies. — (3) Excluding dwellings. — (4) Excluding banks of national interest. — (5) Subsidized housing.

The rapid change in the composition of investment has been accompanied by a significant modification in the structure of domestic supply and intensifying international economic integration. Estimates based on 1980 prices show that the persistent weakness of domestic demand for agricultural and industrial machinery has been partially offset by an expansion of exports, which amounted to 70 per cent of total output in 1985 as against 59 per cent in 1983. In the case of data processing equipment, import penetration and the propensity to export are markedly cyclical, but vary around a high level (45-50 per cent) that has remained relatively constant over time. In 1984 and 1985 the industry's output expanded more or less in step with the rapid growth of domestic demand; in the second half of 1985 its share of the domestic market declined, but a larger portion of output was exported.

By its very nature, the replacement of fixed productive capital tends to spread to all stages of the production cycle (from manufacture to distribution) and to all branches of economic activity (from merchandise production to the supply of services). The impact on the organization of labour varies considerably from sector to sector, depending on the way in which the new equipment is used. As has been happening since 1981, the rate of investment in 1984-85 was higher in market services than in industry, suggesting that the tertiary sector is increasingly engaged in modernization and rationalization (Table 6).

Investment in machinery, equipment and transport equipment peaked at mid-year and then declined to below its first-quarter level. However, a number of factors suggest that this should not be interpreted as a cyclical downturn. First, March 1985 was the deadline for small and medium-sized industrial firms to claim capital grants from the Ministry of Industry for purchases of electronically controlled machinery; the deadline accelerated the pace of investment during the first half of the year by prompting firms to bring forward existing investment plans. Moreover, in the final quarter of the year there was a recovery in expectations by machinery and equipment producers of new orders over the short term, and industrial firms announced substantial investment programmes.

A sample survey conducted by the Bank of Italy on manufacturing firms with more than 20 employees revealed that their fixed investment increased by 7.3 per cent in 1985 (Table 7). Although rationalization has continued — especially in public sector firms, where employment declined by 4.8 per cent and productive capacity was reduced — the last few years have witnessed the first, tentative signs of an increase in the share of investment going to expand capacity, though such investment still accounts for less than 25 per cent of the total.

Table 7

INVESTMENT AND EMPLOYMENT IN MANUFACTURING INDUSTRY: 1985 AND PROJECTIONS FOR 1986

(percentage changes over previous year)

Company size (employees)	Investment (1)				Employment at year-end			
	1985			1986	1985			1986
	Projected	Actual	Achievement rate (2)	Projected	Projected	Actual	Achievement rate (3)	Projected
20 — 99 .	−8.0	5.6	114.8	−2.7	−0.4	−0.8	99.6	0.2
100 — 499 .	−1.4	12.2	113.9	−5.2	−1.7	−2.3	99.4	−0.4
500 — 999 .	4.4	4.2	99.7	14.5	−1.8	−2.4	99.4	−0.8
above 999 .	19.3	5.4	88.3	19.7	−2.9	−4.6	98.2	−2.9
Total . . .	**7.7**	**7.3**	**99.6**	**8.4**	**−1.8**	**−2.9**	**98.9**	**−1.1**

Source: Bank of Italy.

(1) At 1985 prices. For 1986 the annual change in the investment deflator is that estimated by firms. — (2) The ratio of actual investment in 1985 to firms' end-1984 projections for 1985. — (3) Ratio of actual employment at end-1985 to firms' end-1984 projections for end-1985.

This very modest tendency is partly confirmed by the 1986 investment plans announced by manufacturing firms; a fairly steady rate of expansion of 8.4 per cent, which should be easily attainable in view of increased profitability, is coupled with plans for expanding productive capacity, while employment should decline more slowly (— 1.1 per cent). Although these forecasts are less gloomy than those of recent years, 1986 still holds out no prospect of an expansion in manufacturing capacity substantial enough to avert a decline in industrial employment.

DOMESTIC SUPPLY

Agriculture

For the second year running output declined. Crops suffered from the particularly bad weather, with frost in most regions in January and a prolonged rainless spell at the end of the summer.

The fall in agricultural production contributed to the further deterioration in the sector's trade deficit from 11.8 to 13.4 trillion lire.

Employment declined by 89,000 or 3.7 per cent, with a sharper fall for self-employed workers. Investment decreased by nearly 5 per cent, with an acceleration of the downward trend that has been under way almost without interruption since 1978.

The findings of a recently published Istat analysis of 1982 Census data covering a sample of 10 per cent of Italian farms reveal the major changes that occurred in the agricultural sector in the seventies.

Farms on which all or most workers are family members grew in importance and nine farms out of ten can be classified as "peasant" farms. These account for three fifths of the total farmed area and tend to be very small, though they show large geographical variations in size. The other 10 per cent of farms, on which workers are all or mostly non-family, are now mainly large, especially in the North and the Centre of Italy.

Notwithstanding the virtually unchanged average size of farms (7.2 hectares) compared with the 1970 Census, Italian agriculture has been reorganizing, albeit slowly, as the increase in the proportion of farms of over 20 hectares confirms (Table 8). Especially in the south, however, there are still a great many very small farms, which act as a brake on the overall efficiency of the sector owing to their limited scope for improving their organization and production in line with technical and market developments.

There was a more pronounced strengthening of the structure of livestock farms, with a large reduction in family-run farms, especially in the north; this was coupled with an increase in large farms, which are more closely integrated with the food-processing industry.

Table 8

DISTRIBUTION OF FARMS BY SIZE AND GEOGRAPHICAL AREA

(percentages)

	SIZE CLASS IN HECTARES											
	1961 Census				1970 Census				1982 Census			
	up to 5	5.01 to 20	20.01 to 50	over 50	up to 5	5.01 to 20	20.01 to 50	over 50	up to 4.99	5 to 19.99	20 to 49.99	50 and over
	Number of farms											
North	73.5	22.8	2.8	0,9	69.9	25.0	3.8	1.3	68.5	25.1	4.7	1.7
Centre	68.0	26.8	3.9	1.3	72.1	22.3	3.7	1.9	74.4	19.4	4.0	2.2
South	81.3	15.2	2.3	1.2	81.0	15.2	2.4	1.4	80.7	15.1	2.7	1.5
Italy	**76.3**	**19.8**	**2.8**	**1.1**	**75.8**	**19.7**	**3.1**	**1.4**	**75.7**	**19.0**	**3.6**	**1.7**
	Total farm land											
North	20.2	33.9	13.0	32.9	16.7	30.9	14.5	37.9	14.2	27.9	16.2	41.7
Centre	16.0	34.3	14.9	34.8	14.8	25.3	13.3	46.6	13.9	21.7	14.4	50.0
South	22.5	24.6	12.4	40.5	21.3	23.5	12.4	42.8	19.4	22.3	13.5	44.8
Italy	**20.4**	**30.1**	**13.1**	**36.4**	**18.3**	**26.7**	**13.4**	**41.6**	**16.4**	**24.3**	**14.7**	**44.6**

Source: Istat, *Censimento generale dell'agricoltura (1961, 1970 and 1982).*

Between 1970 and 1982 output per man/day expanded by 64 per cent, but the increase was much larger in the Centre and North of Italy than in the South (Table 9). The rise in output per hectare amounted to 27 per cent but did not show large geographical disparities. The rise can probably be attributed not only to the spread of technical progress but also to the large-scale abandonment of marginal land. The greater uniformity with which land productivity increased compared with labour productivity confirms that the south continues to have an excess of agricultural workers and that in the seventies they were unable to find more profitable alternative employment.

On the whole the census data point to positive changes in agricultural structures. Modernization will nonetheless have to proceed faster, both because Community pricing policy will tend to give less protection to farm incomes — for budget reasons and in response to the pressure of non-European producers — and because the accession of Spain and Portugal will intensify competition, especially in typically southern crops. The new Italian programme for agriculture covering the period 1986-90 has a 16.5 trillion lira budget and should make a useful contribution to improving the efficiency and competitiveness of farms.

Table 9

VALUE ADDED PER MAN/DAY AND HECTARE OF FARMED LAND

(thousands of 1970 lire)

	Per man/day			Per hectare of utilized agricultural area		
	1970	1982	% change	1970	1982	% change
North	5.5	10.0	81.4	348.1	447.8	28.6
Centre	4.5	8.4	87.8	245.5	322.7	31.4
South	6.6	9.1	38.4	247.2	305.6	23.6
Italy	**5.7**	**9.4**	**63.8**	**281.4**	**357.3**	**27.0**

Source: Istat, *Il valore aggiunto dell'agricoltura per regione 1970-1982* and *Censimento generale dell'agricoltura (1970 and 1982).*

Industry

Industrial value added rose by 1.2 per cent, or much less than in 1984, and has still not returned to its 1980 level (Table 10). Industry excluding construction (energy products and manufacturing) recorded a slightly larger increase (1.7 per cent). The growth in physical output also slowed down considerably, with the general index of industrial production rising by 1.2 per cent, as against 3.4 per cent in 1984 (Table a4).

Following Istat's publication of the new 1980-based index of industrial production, the Bank of Italy has updated its indices of manufacturing industry's potential output and capacity utilization rate.

Table 10

INDUSTRIAL VALUE ADDED AT MARKET PRICES

	Values at 1970 prices (billions of lire)			% composition 1985	% changes		
	1983	1984	1985		1983/82	1984/83	1985/84
VALUE ADDED:							
including construction	34,724	35,716	36,153	100.0	−2.2	2.9	1.2
excluding construction	29,610	30,580	31,087	86.0	−2.3	3.3	1.7
Goods:							
manufactured goods	25,543	26,491	26,971	74.6	−2.2	3.7	1.8
energy products	4,067	4,089	4,116	11.4	−3.4	0.5	0.7
Construction and public works	5,114	5,136	5,066	14.0	−1.8	0.4	−1.4

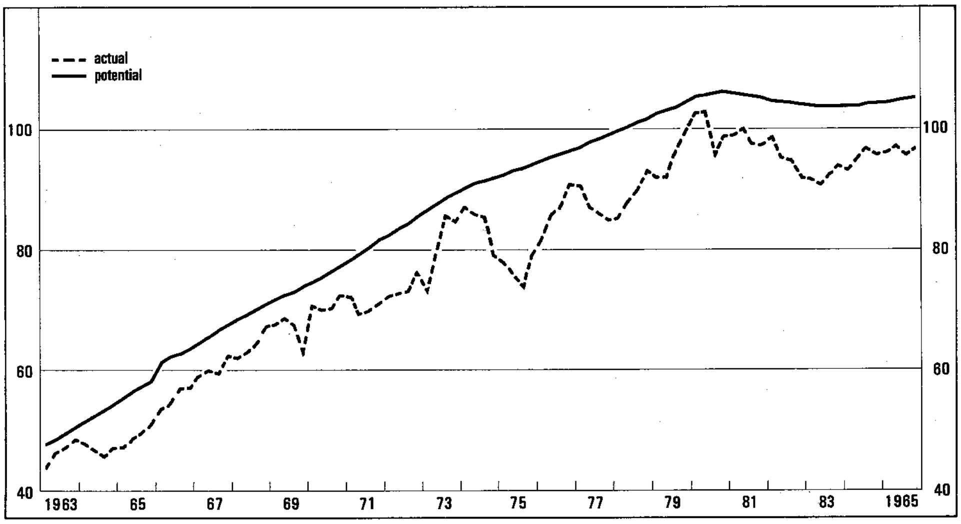
Source: Istat.

The curve of potential output (Figure 3) rose steadily from the fifties to the end of the seventies, though the pace gradually slowed (from an average annual rate of 8.5 per cent between 1954 and 1963, to 6 per cent between 1964 and 1973, to 2.7 per cent between 1974 and 1980). In 1980 there was an unprecedented break; at the end of the year the index stopped rising and then began to fall slowly. The decline came to a halt towards the middle of 1983 and there has recently been a slight recovery. Nonetheless, in 1985 industry's potential output was still 1 per cent less than the peak recorded in 1980.

Figure 3

ACTUAL AND POTENTIAL OUTPUT IN INDUSTRY EXCLUDING CONSTRUCTION

(indices, average actual output in 1980= 100)



The long standstill in the expansion of potential output has been confirmed not only by other studies using different procedures from the Wharton method used by the Bank, but also by the Isco surveys of the rate of capacity utilization. Dividing the index of actual production by firms' declared capacity utilization rate gives an "implicit potential output" that recorded an even sharper peak in 1980 than the Bank of Italy index.

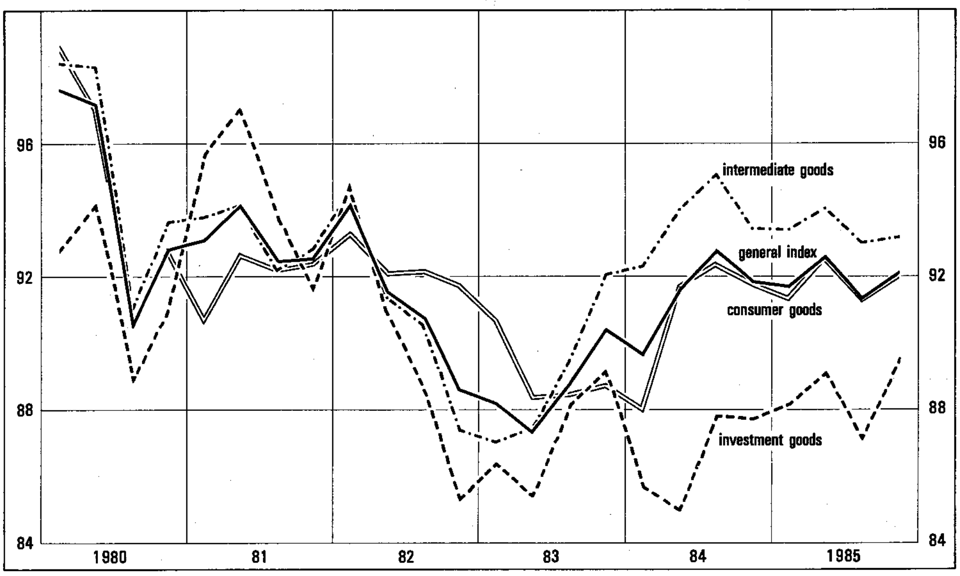
The downturn in 1980 involved nearly every branch of industry, though it took different forms. For the most part the contraction in capacity ranged from 5 to 20 per cent over two to four years, with the decline subsequently halting but with no firm signs of a recovery. This group includes vehicles, machine tools, metal products and some traditional branches. In other branches capacity did not decrease, but its expansion came to a stop or slowed considerably after 1980. This group includes food and chemical products (excluding pharmaceuticals). Only office and data processing machines, pharmaceuticals, and paper and publishing appear to buck the trend.

One of the many reasons for this fundamental shift is that the much greater flexibility of the latest generations of industrial machinery has made it less necessary to maintain reserve capacity. Firms have exploited this possibility to the full in the face of fiercer international competition (from both other OECD countries and newly industrializing countries), considerable structural excess capacity in some branches and persistent pressure on costs, all of which spurred far-reaching reorganization.

Furthermore, belief in a fundamental tendency for the economy to grow steadily year by year had been shaken by the succession of domestic and external shocks. However, the slight recovery in the Bank's potential output index since 1983 suggests a turn for the better in firms' longer-term expectations.

Figure 4

RATE OF CAPACITY UTILIZATION IN INDUSTRY EXCLUDING CONSTRUCTION



The capacity utilization rate also peaked in 1980, subsequently coming down by an average of about one point per quarter — albeit with wide fluctuations due to the short-term irregularity of industrial production — to a minimum of 87.2 in the second quarter of 1983, when the cycle turned up (Figure 4). The index then rose again and since 1984 it has varied between 91 and 92, which is slightly above the long-term average of 90.3 but still well below the values recorded at cyclical peaks in the past and with as yet no clear upward or downward trend.

Services

The fall in agricultural output and the slowdown in the growth of industrial production were accompanied by a further substantial expansion in the supply of market services (4.5 per cent), which was reflected in an increase in employment of over 300,000, for the most part employees (up 256,000 or 6 per cent).

In terms of value added, the best performance was recorded by "Other market services" (10.2 per cent) and "Credit and insurance" (8.4 per cent) (Table 11). Among the former, "Business services provided to enterprises" continued their rapid medium-term expansion, fueled both by the development of new services and by the decentralization of functions that industrial companies had previously performed in-house, while as regards the services provided to households, the stagnation in private education was offset by a sharp rise in health, recreational and cultural services.

Table 11

VALUE ADDED OF MARKET SERVICES AT MARKET PRICES

(billions of lire)

Sector	1985		Percentage changes					
			Volume			Prices		
	1970 prices	Current prices	83/82	84/83	85/84	83/82	84/83	85/84
Wholesale and retail trade	12,941	87,471	–0.2	3.2	2.3	12.9	9.3	10.7
Lodging and catering	2,014	19,908	–0.8	3.5	1.5	19.1	9.8	11.9
Transport	4,596	35,159	–1.2	3.7	3.2	19.1	12.4	10.3
Communications	2,005	11,465	5.8	5.6	5.3	15.8	10.0	10.5
Credit and insurance	4,435	39,075	3.1	4.3	8.4	11.1	7.0	9.8
Other market	7,984	56,469	1.1	7.7	10.2	15.4	8.8	9.1
Renting of buildings	5,098	44,558	0.3	1.0	0.8	17.5	23.4	12.9
Total	**39,073**	**294,105**	**0.6**	**4.1**	**4.5**	**15.0**	**11.3**	**10.6**

Source: Istat.

Table 12

CHANGE IN THE COMPOSITION OF VALUE ADDED AND EMPLOYMENT IN THE MAIN INDUSTRIAL COUNTRIES

(percentages)

	Italy	France	Germany	United Kingdom	United States	Japan
			1973			
VALUE ADDED						
Agriculture	7.8	6.7	2.9	2.7	3.9	5.9
Industry	42.2	38.1	47.0	39.2	34.1	46.3
manufacturing	*30.0*	*28.3*	*36.3*	*28.5*	*24.9*	*35.1*
Services	50.0	55.2	50.1	58.1	62.0	47.8
private	*37.6*	*44.4*	*37.8*	*45.2*	*48.8*	*39.6*
general government	*12.4*	*10.8*	*12.3*	*12.9*	*13.2*	*8.2*
EMPLOYMENT						
Agriculture	16.6	11.4	7.3	2.9	4.2	13.4
Industry	38.3	39.7	47.5	42.4	33.1	37.2
manufacturing	*28.2*	*28.3*	*36.1*	*34.7*	*24.8*	*27.4*
Services	45.1	48.9	45.2	54.7	62.7	49.4
private	*30.1*	*32.7*	*30.1*	*35.8*	*46.5*	*41.3*
general government	*15.0*	*16.2*	*15.1*	*18.9*	*16.2*	*8.1*
			1983			
VALUE ADDED						
Agriculture	6.0	4.0	2.1	1.9	2.0	3.3
Industry	40.1	34.4	41.3	35.7	31.7	42.1
manufacturing	*27.1*	*25.3*	*31.8*	*21.0*	*21.1*	*30.5*
Services	53.9	61.6	56.6	62.4	66.3	54.6
private	*39.2*	*48.0*	*43.0*	*47.6*	*53.4*	*44.0*
general government	*14.7*	*13.6*	*13.6*	*14.8*	*12.9*	*10.6*
EMPLOYMENT						
Agriculture	12.1	8.1	5.6	2.7	3.5	9.3
Industry	34.8	33.8	41.9	33.6	28.0	34.7
manufacturing	*25.5*	*24.3*	*32.4*	*26.7*	*19.8*	*24.5*
Services	53.1	58.1	52.5	63.7	68.5	56.0
private	*35.8*	*39.5*	*33.3*	*41.7*	*52.8*	*47.1*
general government	*17.3*	*18.6*	*19.2*	*22.0*	*15.7*	*8.9*

Source: Based on OECD data and the *Relazione generale sulla situazione economica del paese.*

The increase in the turnover of the domestic distribution system and the expansion in the volume of foreign trade sustained the growth in "Wholesale and retail trade", while "Lodging and catering" recorded only a small increase. The 5.3 per cent growth in the supply of "Communications" was in line with trend and only a little less than in 1984. The regular increases in demand and productivity in this branch have permitted the self-financing of a substantial proportion of its heavy investment programme.

The expansion in services over the last few years has shifted the composition of domestic supply, and they now account for over half the total. This development is common to all the main industrial countries and is revealed most sharply by the changes in employment (Table 12).

The increasing importance of services in the economy can be attributed both to the shift in final demand towards "luxury" goods with higher income elasticities and to a slow change in the structural interdependencies between sectors, which, in turn, reflects closer integration with industry and a consequent rise in the intermediate consumption of services. The upward trend of the contribution of public services inherent in urbanization and the growing complexity of government's role has been compounded over the last decade by the increase in the direct supply of social services.

The energy balance

Last year saw a further increase in the domestic consumption of primary energy, though at 1.5 per cent this was smaller than in 1984. The growth in Italy's energy requirement was in line with the estimated figures for the OECD as a whole in both periods and can be attributed to the general recovery in economic activity. By contrast, in relation to GDP the demand for energy decreased by 0.8 per cent, in line with the trend recorded since 1977, after standing still in 1984.

The increase in final consumption was limited to the transport and household sectors. Industry's demand for energy fell by 2 points, while its energy intensity in relation to value added recorded the sharpest fall of the last four years.

The composition of the energy requirement reflects substantial changes in the pattern of final demand. Industry has achieved the greatest reduction in energy intensity: over the ten years following the first oil shock, industrial energy consumption per unit of output fell by 37 per cent in the OECD and by 32 per cent in the EEC. Within

Table 13

INDICATORS OF DEPENDENCE ON ENERGY

	1973	1975	1978	1979	1980	1981	1982	1983	1984	% change 1973-1984
ITALY										
Energy deficit/GDP (1)	2.1	4.6	3.9	4.2	5.8	7.5	6.3	6.0	5.8	
Total net imports (2)	114.7	106.5	116.6	123.1	122.5	119.5	116.4	110.2	118.7	+3.5
Net oil imports (2)	104.6	89.8	95.8	100.0	97.8	93.2	90.3	83.5	84.8	−18.9
FRANCE										
Energy deficit/GDP (1)	1.5	3.2	2.9	3.4	4.8	5.2	5.0	4.3	4.4	
Total net imports (2)	146.6	125.5	142.5	155.4	150.4	130.4	120.1	113.9	115.5	−21.2
Net oil imports (2)	129.6	103.2	112.5	121.9	113.4	94.7	88.9	83.8	84.9	−34.5
GERMANY										
Energy deficit/GDP (1)	1.3	2.5	2.3	1.2	4.2	4.9	4.5	4.1	4.2	
Total net imports (2)	151.0	137.7	154.3	164.0	156.0	134.2	130.2	129.1	128.8	−14.7
Net oil imports (2)	148.0	125.3	141.3	147.1	133.3	111.2	105.6	104.1	106.0	−28.4
UNITED KINGDOM										
Energy deficit/GDP (1)	1.9	3.4	1.4	0.5	0.2	−0.9	−1.4	−2.2	−1.6	
Total net imports (2)	115.5	92.7	46.2	27.8	12.5	−12.4	−22.0	−35.3	−22.5	
Net oil imports (2)	115.7	90.8	42.2	19.2	1.9	−18.5	−28.9	−44.3	−39.7	
JAPAN										
Energy deficit/GDP (1)	2.0	5.1	3.2	4.4	6.6	6.2	6.0	5.0	4.8	
Total net imports (2)	321.6	303.2	322.7	338.6	324.9	304.8	291.6	290.9	317.4	−1.3
Net oil imports (2)	277.8	253.2	272.9	281.8	257.4	230.6	216.3	217.0	227.0	−18.3
UNITED STATES										
Energy deficit/GDP (1)	0.5	1.4	1.8	2.3	2.9	2.5	1.7	1.5	1.4	
Total net imports (2)	291.5	291.9	421.3	406.2	299.4	237.3	187.4	204.1	220.7	−24.3
Net oil imports (2)	298.9	308.1	418.6	413.6	331.9	283.5	229.3	228.0	248.2	−17.0

Source: Based on OECD data and the *Relazione generale sulla situazione economica del paese.*
(1) At current prices. — (2) Millions of TOE.

Europe, above average reductions were achieved by France, Italy and Germany in that order. New technologies and energy-saving policies have contributed most to the achievement of savings, especially in Italy. The incidence of energy intensive industries remained unchanged in the EEC as a whole, though it diminished in France and, albeit to a lesser extent, in the United Kingdom as a result of contractions in the production capacity for some steel products and construction materials. In Italy, by contrast, these two branches, and particularly the cement industry, grew in importance and more than offset the drastic reduction in basic chemicals.

Even though Italy's performance in reducing the energy intensity of the economy has been comparable with that of the rest of the OECD, the country remains more vulnerable to shocks. Its high level of energy dependence compared with the other main industrial countries is a major factor contributing to the rigidity of the external constraint, the principal obstacle to faster growth. The energy deficit was equivalent to 5.8 per cent of GDP in 1984-85, a substantial improvement compared with the 1981 peak of 7.5 per cent, but not enough to return to the roughly 4 per cent level obtaining after the first oil crisis (Table 13). Japan, whose dependence on energy had originally been the most similar to Italy's, has gradually reduced its ratio from 6.2 per cent in 1981 to 4.8 per cent in 1984. Furthermore, in contrast with the other OECD countries, the decline in energy intensity in Italy has slowed considerably over the last three years. Lastly, even though Italy has made substantial progress in diversifying its energy sourcing, it has failed to bring the share of oil in the total energy requirement down to the OECD average (in 1984: Italy 59 per cent; OECD 44 per cent).

EMPLOYMENT, WAGES AND PRICES

Employment

Employment in the economy as a whole increased by 0.5 per cent over 1984, responding favourably to the expansion in output and to the amendments to the legislation governing training, part-time work and special schemes for short-time working; in absolute terms, the increase corresponded to more than 100,000 jobs (Table 14). The number of employed workers rose by 146,000, but there was a fall of 40,000 in the ranks of the self-employed. As in recent years, the overall figures conceal strong disparities between different sectors. Employment contracted appreciably in agriculture, industry and construction; the only increase was one of 3.0 per cent, or 300,000 jobs, in the services sector, which now employs more than 55 per cent of the labour force.

Table 14

EMPLOYMENT IN ITALY

(percentage changes on previous year)

	Total employment				Employees			
	1982	1983	1984	1985	1982	1983	1984	1985
Agriculture	−5.6	−0.1	−3.8	−3.7	−3.7	−2.7	−5.2	−1.3
Industry	−1.6	−2.5	−3.8	−1.9	−2.1	−3.0	−4.1	−2.2
of which: fuel & power products	*−0.5*	*−0.5*	..	*−0.2*	*−0.4*	*−0.6*	*−0.1*	*−0.3*
manufacturing	*−1.9*	*−2.9*	*−3.6*	*−2.0*	*−2.2*	*−3.2*	*−4.0*	*−2.3*
industry excluding construction	*−1.9*	*−2.8*	*−3.5*	*−1.9*	*−2.2*	*−3.1*	*−3.9*	*−2.2*
construction	*−0.9*	*−1.6*	*−4.7*	*−2.0*	*−1.7*	*−2.7*	*−4.7*	*−2.0*
Market services	2.7	2.6	5.2	3.9	2.8	2.0	4.5	6.0
of which: distributive trades, lodging and catering	*2.8*	*2.6*	*4.4*	*1.8*	*3.4*	*1.1*	*4.4*	*2.9*
transport & communications	*0.1*	*1.0*	*−0.4*	*1.9*	*−0.5*	*1.6*	*−1.0*	*2.5*
credit and insurance	*4.0*	*1.1*	*2.6*	*1.8*	*4.0*	*1.1*	*2.6*	*1.9*
other market services	*4.4*	*4.4*	*12.0*	*10.4*	*4.6*	*4.2*	*10.3*	*15.0*
Market goods and services	**−0.5**	**..**	**0.1**	**0.5**	**−0.5**	**−1.2**	**−1.0**	**1.1**
Non-market services	**1.4**	**1.0**	**1.0**	**0.8**	**1.4**	**1.0**	**1.0**	**0.8**
Total	**−0.2**	**0.2**	**0.3**	**0.5**	**−0.1**	**−0.7**	**−0.5**	**1.0**

Source: Istat.

The increase in employment in the tertiary sector occurred mainly in miscellaneous services, which have been expanding at rates in excess of 10 per cent for several years. Within this group, which is highly heterogeneous, there was a strong expansion in activities geared towards firms and in other services for which demand is particularly income elastic, such as health care and leisure activities.

The shake-out of labour in industry excluding construction slowed down and finally halted in the second half of the year. It is also significant that the number of hours paid by the Wage Supplementation Fund declined by 16.1 per cent, the first such decrease since 1980.

The labour force again grew significantly in 1985 (by 0.8 per cent, or 200,000 persons) owing to demographic factors and a rise in the participation rate from 40.9 to 41.1 per cent; as in previous years, the increase occurred entirely in female employment, where the activity rate rose from 27.8 to 28.2 per cent, while the male rate remained at the level of 54.7 recorded in 1984.

The imbalance between the growth in the labour force and the increase in employment caused the number of persons seeking employment to rise to 2.5 million. The unemployment rate touched 10.6 per cent, or 12.3 per cent if recourse to the Wage Supplementation Fund is taken into account. The number of young persons seeking work increased by 7.0 per cent and accounted for the entire increase in unemployment, while adult unemployment remained unchanged.

The 1984 legislation on training, part-time work and special schemes for short-time working began to have an effect last year. The number of persons affected by training schemes rose from 32,000 to 153,000, of whom 108,000 have already found work. The increase in part-time work was equally significant; although this form of employment is still far less widespread than in the major industrial countries, it affected 100,000 persons last year, mainly women. Small and medium-sized firms employing 50 workers or less accounted for respectively 75.7 and 70.2 per cent of the persons involved in part-time and training schemes.

The characteristics of the labour market in the eighties. — Profound changes occurred on both the supply and demand sides of the labour market in the first half of the eighties. Overall, more than 400,000 new jobs were created (Table 15); employment in services recorded an unprecedented expansion of more than 1.6 million, but the decline in agricultural employment continued and there was a sizable contraction of 700,000 jobs in industry, the first fall in industrial employment to occur in Italy. At the same time, important changes were occurring on the supply side, such as the rise in the participation rate among women and a large influx of young people into the labour market.

Table 15

CHANGES IN EMPLOYMENT AND THE SUPPLY OF LABOUR IN THE 1980s

(thousands)

	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85	1979-85
Total employment (1)	165.6	97.3	−32.2	38.0	60.0	107.0	435.7
agriculture (1)	−80.0	−105.0	−149.0	−2.0	−94.0	−89.0	−519.0
industry (1)	54.0	−54.0	−123.0	−187.0	−271.0	−134.9	−715.9
services (1)	191.6	256.3	239.8	227.0	425.0	330.9	1,670.6
Job seekers (2)	−2.5	212.3	155.8	211.3	127.5	80.5	784.8
Labour force (2)	272.3	267.5	106.0	276.0	217.0	175.0	1,313.8
Unemployment rate (2)	7.6	8.5	9.1	9.9	10.4	10.6	2.9
Activity rate (2)	39.8	40.2	40.3	40.6	40.9	41.1	1.7

Source: Based on Istat data.
(1) National accounts data. — (2) Labour force data.

For a more informative analysis, however, it is essential to examine the figures on intersectoral flows, which make it possible to evaluate year-to-year shifts from one sector to another and from employment to unemployment or withdrawal from the labour market.

A large proportion of the persons seeking work remain unemployed for more than a year; indeed, there is a tendency for this hard core of unemployment to swell. In recent years job seekers have also shown greater reluctance to leave the labour market, a sign of changed sociocultural attitudes.

Employees in sectors other than agriculture showed a high degree of immobility over the entire period under examination, with the proportion switching from one sector to another being less than 20 per cent a year. In the case of industrial workers, the most frequent destinations were the services sector, with values close to 10 per cent, and non-employment (pensioners, housewives, etc.). Workers in the services sector, who include central and local government employees, have the lowest mobility rate of any sector and the only significant flows are into industry or out of the labour market entirely.

Among self-employed persons as a whole there was greater mobility towards other occupations or withdrawal from the labour market; in services, in particular, there were significant transfers into dependent employment. By contrast, the figures for self-employed farmers transferring to other sectors of the economy were very low, an indication of the closed nature of the sector; the numbers leaving the labour market were especially high, averaging around 15 per cent a year, probably on account of the high average age of workers in this sector.

The analysis therefore shows that elements of flexibility and substantial rigidities exist side by side in the Italian labour market. Flexibility is evident in the large numbers of workers transferring between industry and services, with flows of the order of 7 or 8 per cent a year in each direction. There are also comparable movements from self-employment to dependent employment and vice versa. On the other hand, rigidity is apparent in the particularly small flows of job-seekers into employment, which showed no tendency to increase over the period examined; the majority of unemployed persons, a high proportion of them young people, continue to seek work, but with little likelihood of success. The average duration of unemployment has therefore steadily lengthened from 13 months in 1980 to 20 in 1985, significantly higher than the average for the OECD countries as a whole.

Wages and labour costs

In 1985 the only labour agreements to be renewed were in certain parts of the credit sector, private gas companies and telephone companies. This and the reduction in industrial disputes brought a dramatic reduction in the number of hours lost through strikes, which fell from 61 million in 1984 to 25 million last year, the lowest figure since 1954.

There was a further reduction in the rate of increase in nominal per capita wages, which rose overall by an average of 9.6 per cent (9.5 per cent in the private sector and 9.7 per cent in general government) compared with 12.3 per cent in 1984 (Table 16). Wage drift and increases due to settlements at company level were small owing to the persistence of difficult conditions in the labour market.

Table 16

LABOUR COSTS IN THE PRIVATE SECTOR

(percentage changes)

	Value added at market prices (1)	Total employment	Output per employed worker	Wages per employee	Labour costs	Unit labour costs
	Private sector (excluding renting of buildings) (2)					
1980	4.6	0.8	3.7	21.7	21.5	17.2
1981	0.2	0.2	−0.1	19.9	19.6	19.7
1982	−0.8	−0.4	−0.4	16.4	17.7	18.2
1983	−0.1	..	−0.2	14.2	15.9	16.1
1984	3.0	0.2	2.8	11.6	11.2	8.1
1985	2.6	0.5	2.1	9.5	10.1	7.9
	Agriculture					
1980	4.0	−2.8	7.0	23.2	23.8	15.7
1981	−0.1	−3.8	3.9	21.3	21.9	17.4
1982	−2.5	−5.6	3.3	18.4	19.6	15.7
1983	8.8	−0.1	8.9	17.5	17.6	8.0
1984	−3.4	−3.8	0.4	10.8	10.6	10.2
1985	−2.4	−3.7	1.4	9.7	10.4	9.0
	Industry excluding construction (3)					
1980	4.7	0.2	4.5	21.0	19.6	14.4
1981	−0.9	−4.1	3.4	25.3	24.1	20.0
1982	−2.1	−2.7	0.6	17.0	19.1	18.4
1983	−2.3	−4.3	2.1	15.2	17.2	14.8
1984	3.3	−4.2	7.8	12.7	12.5	4.3
1985	1.7	−0.8	2.4	8.9	9.9	7.3
	Construction					
1980	4.0	1.1	2.8	20.5	20.7	17.3
1981	1.0	1.8	−0.8	18.1	18.2	19.1
1982	−2.1	−0.9	−1.2	17.1	18.2	19.6
1983	−1.8	−1.6	−0.2	13.5	15.5	15.7
1984	0.4	−4.7	5.4	10.4	9.7	4.1
1985	−1.4	−2.0	0.7	9.0	10.0	9.3
	Services (excluding renting of buildings) (2)					
1980	4.6	2.4	2.2	23.2	24.2	21.6
1981	1.1	2.7	−1.5	18.5	18.6	20.4
1982	1.0	2.7	−1.6	16.3	16.7	18.6
1983	0.7	2.5	−1.8	14.9	16.4	18.6
1984	4.5	5.0	−0.5	11.7	10.8	11.3
1985	5.0	3.8	1.2	8.7	8.5	7.2

Source: Istat.
(1) 1970 prices; the figures for agriculture, industry and services include imputed bank services. — (2) Includes "Other non-market services". — (3) Net of the full-time worker equivalent of the hours of wage supplementation paid.

There were no significant disparities between the various sectors of the economy, apart from the rate of increase of wages in market services (8.5 per cent), which was about 1 percentage point below the average. Hence the wage structure was little changed over the year. Viewed over a longer time span, however, the relative position of public employees has improved substantially; despite the ceilings on salary increases, their incomes have risen faster than the average, with the ratio to incomes in the economy as a whole increasing from 1.10 at the end of the seventies to 1.25 in the last two years.

The degree of inflation-proofing provided by wage indexation on the trade union index rose again to 54 per cent, after having fallen to 44 per cent in 1984 owing to measures fixing wage adjustments in advance (Figure 5).

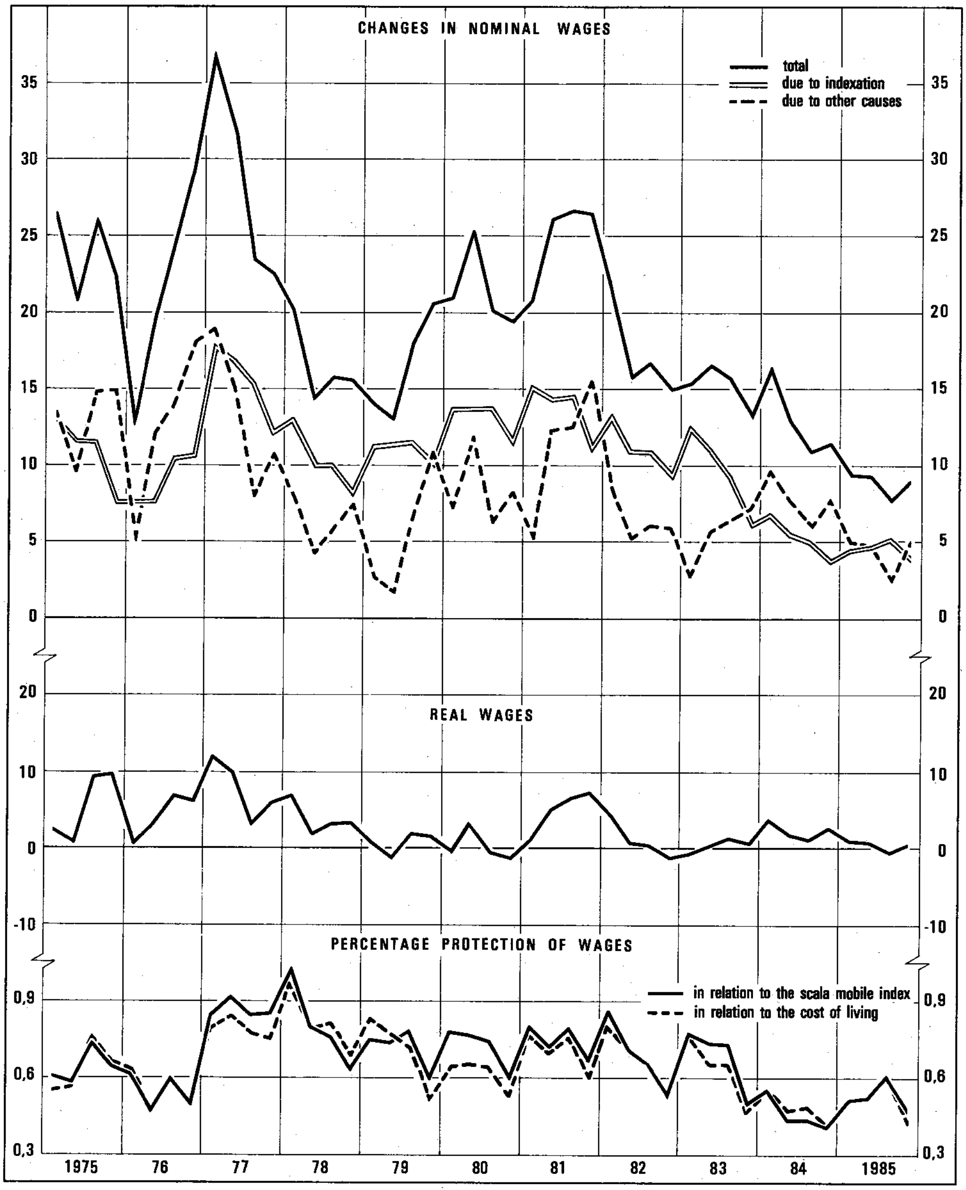
At the beginning of 1986 the new wage indexation mechanism that had initially been adopted for public employees was extended to cover workers in all sectors. The new system differs from its predecessor with regard to the frequency of adjustment, which is now half yearly instead of quarterly, and the method of adjustment, which provides for 100 per cent indexation of net monthly wages of 580,000 lire for all workers and 25 per cent coverage for a second tranche running from this amount up to base pay plus the cost-of-living allowance. There is also provision for neutralizing the effects of changes in indirect taxes on prices, although there is some perplexity about the way in which this clause should be applied. (This subject is discussed in more detail in the Bank's Economic Bulletin No. 2, February 1986.)

Unit labour costs increased by 8 per cent in the private sector. There were appreciable differences between the various branches owing to cyclical and structural disparities in the rate of productivity growth. In industry excluding construction, the rate of change in unit labour costs rose from 4.3 to 7.3 per cent; in services it fell from 11.3 to 7.2 per cent and in agriculture from 10.2 to 9.0 per cent. Except in agriculture, these variations were smaller than those in the corresponding value added deflators, causing a substantial improvement in profitability and a steady return to the income distribution pattern of the early seventies. Specifically, in market goods and services as a whole, the labour share of income adjusted to take account of the composition of employment fell from 77.7 to 76.7 per cent; even larger changes occurred in the energy sector (a fall from 45.3 to 42.8 per cent) and in credit and insurance (a decrease from 66.4 to 61.3 per cent), while in manufacturing industry the labour share remained unchanged, after having contracted substantially in previous years.

Figure 5

NOMINAL AND REAL PER CAPITA WAGES AND THE PERCENTAGE PROTECTION OF WAGES IN INDUSTRY EXCLUDING CONSTRUCTION (1)

(percentage changes over the same quarter of the previous year; percentage of inflation protection. Data net of persons receiving wage supplementation)



(1) Real wages are determined by the ratio of nominal wages to the consumer price index for the families of manual workers and employees. The percentage protection of wages is the ratio of the change in wages due to wage indexation to the change in the corresponding price index.

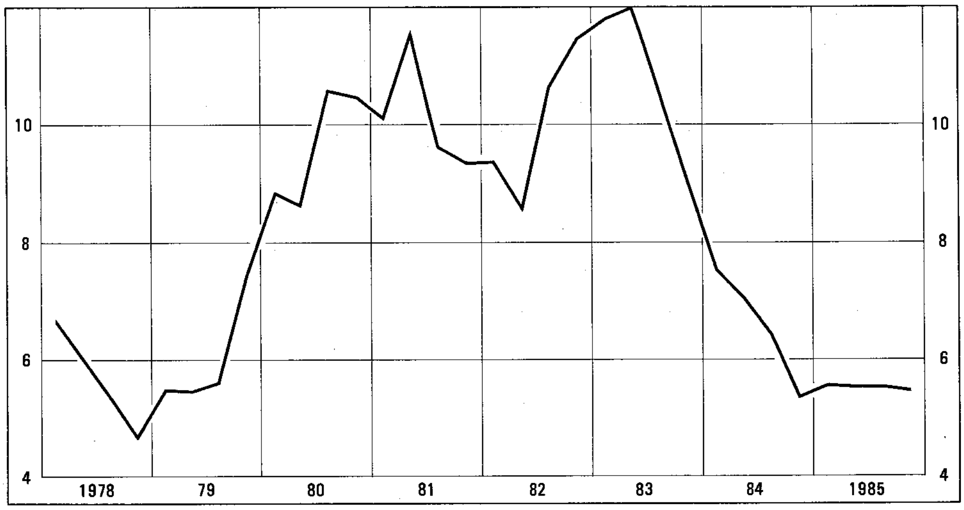
Prices

Inflation slowed down by only two percentage points, after a substantial reduction in 1984; consumer prices rose by 9.2 per cent, the smallest rate of increase since the first oil crisis, and narrowed the inflation differential between Italy and the major industrial countries by about one percentage point, from 6.5 to 5.5 points (Figure 6). The cost of living index rose by less (8.6 per cent), since it is not as strongly affected by the prices of services, which continued to rise at a fairly rapid pace. In both indices, the slowdown in the course of the year was very small, less than one percentage point between January and December.

Figure 6

ITALY'S CONSUMER-PRICE INFLATION DIFFERENTIAL VIS-A-VIS THE OECD

(difference between quarterly twelve-month rates of inflation)



Source: Istat and OECD.

There was a more marked slowdown in wholesale prices, however, where the rate of increase fell from 10.4 to 7.3 per cent; the substantial reduction in the rise in raw material prices offset the faster increase in those of industrial manufactures.

The behaviour of the wholesale prices of manufactures was strongly affected by the changes in the main factor costs. In the first half of the year the latter rose faster than output prices (Table 17), but in the second half the pronounced slowdown in various costs was reflected only partly in selling prices, and profit margins widened.

Among cost components, variations in the prices of imported inputs were determined largely by movements in the dollar exchange rate. In the first half of the year the lira prices of raw materials measured on the Confindustria index rose at an annual rate of more than 9 per cent. In the second half of the year, however, the depreciation of the dollar created conditions that favoured a marked slowdown in the cost of imported industrial inputs.

Table 17

TOTAL UNIT COSTS AND FINAL PRICES IN INDUSTRY EXCLUDING CONSTRUCTION

(percentage changes)

	1980-81 (1)	1982-83 (1)	1984	1985	1985-I / 1984-II (2)	1985-II / 1985-I (2)
Unit labour costs (3)	17.3	16.6	4.4	7.3	9.5	8.8
Total input prices:	27.2	10.2	11.7	7.4	12.5	−5.2
domestic (4)	18.3	15.0	10.6	8.0	10.8	5.5
foreign:	32.5	7.7	12.3	7.0	13.4	−10.8
energy	57.5	5.6	6.4	3.4	11.5	−19.0
intermediate products	18.0	7.8	13.2	11.0	18.2	−5.5
other raw materials	27.2	12.4	24.2	8.5	12.3	−9.5
Total unit costs	**23.4**	**12.5**	**7.4**	**7.3**	**10.8**	**2.5**
Output prices	**21.2**	**12.8**	**10.7**	**7.8**	**9.9**	**3.7**

(1) Average of annual percentage changes. — (2) Annualized compound rates. — (3) Adjusted to exclude workers receiving wage supplementation. — (4) Weighted net of intersectoral transactions.

The increase in administered prices and public service charges exceeded the target of 7 per cent by one percentage point and displayed no deceleration in the course of the year (Table 18). The largest increases in controlled prices again occurred in public service charges, which rose at a rate of 9.4 per cent, while the smallest change was the increase of 5.7 per cent in rents, which rose again in 1985 following the temporary freeze imposed the preceding year.

In the first quarter of 1986 the further depreciation of the dollar and the fall in oil prices were reflected in a significant reduction in the rate of inflation. The wholesale price index fell in February and March and for the first time since 1969 showed no appreciable change in relation to the same period of the preceding year. In April the cost of

Table 18

DEVELOPMENT OF SELECTED CONSUMER PRICES

(percentage changes)

	Administered prices: Goods	Administered prices: Public services	Administered prices: Rents	Administered prices: Total	Monitored prices	Unregulated prices	General consumer price index
1982	19.7	17.4	16.1	18.3	17.8	15.8	16.5
1983	14.0	21.6	18.8	17.5	12.9	14.0	14.7
1984	8.3	12.2	23.7	12.3	8.5	10.6	10.8
1985	7.0	9.4	5.7	7.6	7.5	9.8	9.2
Dec. 84 / 1984	2.8	3.3	2.0	2.8	3.0	4.2	3.8
Dec. 85 / 1985	4.0	2.4	4.2	3.4	2.3	3.6	3.5
Changes over the year							
1982	19.8	16.3	18.4	18.3	16.8	15.5	16.1
1983	10.1	19.9	25.9	16.2	7.8	11.9	12.6
1984	6.9	9.7	10.8	8.6	7.7	9.8	9.4
1985	8.2	8.5	8.1	8.3	6.9	9.2	8.8
Percentage contribution to consumer price inflation (1)							
1982	11.8	7.9	3.6	23.3	7.5	69.2	100.0
1983	9.7	11.1	4.6	25.4	6.1	68.5	100.0
1984	7.8	9.0	8.2	25.0	5.4	69.6	100.0
1985	7.5	8.3	2.6	18.4	5.5	76.1	100.0

Source: Istat.

(1) Calculated in relation to the average annual increase and level of the relevant index numbers.

living was 0.3 per cent higher than in March and 6.6 per cent higher over the year. By contrast, the trend in manufactures prices appears to be less favourable; although slowing down, the rate of increase still does not reflect the fall in production costs (Table 19).

Table 19

WHOLESALE AND CONSUMER PRICES

(percentage changes in indices; 1980=100)

	1984	1985	Dec. 84 / Dec. 83	Dec. 85 / Dec. 84	Dec. 85 / 1985	1st qtr. 86 / 1st qtr. 85	1st half 85 / 2nd half 84	2nd half 85 / 1st half 85
	Wholesale prices						Annualized compound rate	
General index	10.4	7.3	8.2	5.9	1.5	2.5	9.9	3.0
Foodstuffs	8.5	6.2	5.0	6.9	2.5	5.9	8.9	3.9
Industrial raw materials	13.3	6.5	9.6	1.3	−1.9	−6.4	10.2	−2.6
oil	*14.6*	*5.6*	*13.0*	*−8.1*	*−8.0*	*−30.6*	*16.1*	*−19.3*
non-oil	*12.9*	*6.8*	*8.6*	*4.3*	..	*1.6*	*8.4*	*3.3*
Industrial products	10.0	8.3	9.4	7.7	2.6	5.1	10.3	5.3
excluding oil products	9.8	8.5	9.4	7.6	2.6	6.6	9.7	6.2
	Consumer prices							
General index	10.8	9.2	9.4	8.8	3.5	....	11.0	7.1
Food products	9.1	8.7	7.8	8.8	3.3	....	10.5	7.6
Non-food products	10.4	8.6	9.3	8.5	3.6	....	10.1	7.2
Services	13.3	10.4	11.4	9.4	3.5	....	12.1	7.5

Source: Based on Istat data.

THE BALANCE OF PAYMENTS ON CURRENT ACCOUNT

On a transactions basis the current account recorded a deficit of 8,032 billion lire in 1985, an increase of nearly 3 trillion on 1984. The deterioration was due to the trade deficit, which rose from 10,775 to 13,444 billion lire (Table 20).

Table 20

CURRENT ACCOUNT BALANCES

(billions of lire)

	1984	1985
Goods	**−10,775**	**−13,444**
Goods cif-fob (customs data)	*−19,135*	*−23,115*
Services	**3,403**	**3,320**
Transport and insurance	−2,220	−2,345
Foreign travel	11,412	12,362
Income from capital	−6,855	−7,479
Income from labour	2,543	2,531
Other	−1,477	−1,749
Unilateral transfers	**2,288**	**2,092**
Private	2,556	2,691
Public	−268	−599
Total...	**−5,084**	**−8,032**

Merchandise trade

The trade deficit on a customs basis (cif-fob) amounted to 23,115 billion lire, roughly 4 trillion more than in 1984. Inflows and outflows increased in value at similar rates (between 16 and 17 per cent), so that the extent to which exports covered imports remained almost unchanged.

The average unit value in lire of total exports rose by 8.1 per cent, a little less than in the previous year; that of exports of manufactures (excluding oil and coal products) increased by 7.9 per cent. The rise in the average unit value in lire of imported goods (7.4 per cent) was less than the corresponding export figure and slowed more sharply compared with 1984.

Offsetting the improvement in the terms of trade was a 1.3 per cent growth rate differential between merchandise imports and exports in volume terms. This gap was nonetheless narrower than that recorded in 1984 (2.3 per cent).

Merchandise exports grew by 7.5 per cent in volume in 1985, as against 6.6 per cent the previous year. This acceleration was achieved even though the growth in world trade slowed down. Measured in terms of the volume of the industrial countries' exports, the slowdown in growth amounted to over 5 points, the rate falling from 9.3 to 3.9 per cent. Other measures, such as the volume of world trade and the weighted average of real income in Italy's export markets, give similar results. Over the two years 1984-85 the difference between the volume growth in Italy's exports and those of the industrial countries as a whole was less marked (14.6 as against 13.6 per cent). In volume terms Italy's merchandise imports expanded by 8.9 per cent, in line with 1984 (9.1 per cent), despite the slower growth in domestic demand (2.4 as against 3.3 per cent).

Nearly two thirds of the 1985 trade deficit was accounted for by the balance with the OPEC countries, which recorded a shortfall of 13,604 billion lire, an increase of over 5 trillion lire compared with 1984. The deficit with the other EEC countries was also large, having deteriorated from 5,666 billion lire to 8,722 billion. By contrast, the balance of trade with the centrally planned economies improved, since Italy's still substantial deficit of 4,010 billion lire was 2.3 trillion less than the year before. There was an even larger improvement in trade with North America, on which a surplus of 8,917 billion lire was earned, almost double the 5,330 billion recorded in 1984.

Energy and food and agricultural products, for many years now the principal cause of the external constraint on the Italian economy, were again the largest deficit items.

In 1970 Italy's energy shortfall was equivalent to 1.4 per cent of GDP. This proportion then rose to 4.3 per cent after the first oil crisis and 5.9 per cent after the second. There has not been any significant improvement in the eighties, and the ratio declined only slightly last year, from 5.8 to 5.6 per cent, since the full effect of the fall in oil prices had still to make itself felt. In absolute terms the deficit amounted to almost 40 trillion lire.

In relation to GDP the shortfall on food and agricultural products declined between 1975 and 1984 from 2.9 to 2.3 per cent. By contrast, in 1985 it rose to 2.5 per cent of GDP (17.5 trillion lire).

Manufacturing industry (apart from food products) continued to make a substantial positive contribution to the trade balance, generating a surplus of 33.5 trillion lire, equivalent to over 4.8 per cent of GDP. This was slightly down on 1984, but was still one of the best performances since 1970 and confirms the improvement since 1980.

The international position of Italian manufacturing industry

The difficult adjustment of Italy's trade balance after the second oil crisis has prompted suggestions that deindustrialization might be one cause. By contrast, the rapid rise in import penetration in some sectors has been interpreted as part of a process of "efficient" specialization by Italian industry in the final phases of production.

Since 1973 the composition of the trade flows of manufacturing industry, excluding food products, has changed significantly in a way that has also consolidated the Italian model of specialization.

Comparing indicators of specialization and import penetration confirms the persistence of previously identified underlying trends: import penetration has risen throughout manufacturing industry, albeit unevenly, and the export share of output has increased in many branches, not just those with structural surpluses.

These developments can be attributed to the international integration of production, which has also provoked an increase in intra-industry trade.

It is nonetheless still open to question whether the international position of Italian industry is uniform or combines strength in some areas with weaknesses in some specific branches and, if so, whether these are temporary or structural.

Some light can be thrown on this issue by comparing sectoral trade balances and capacity utilization rates over time.

The strong branches include a group (non-metalliferous minerals, metal products, agricultural and industrial machinery, textiles and clothing, rubber and plastic products, and domestic appliances and television sets) for which the potential supply can be considered to be in line with expected long-term (domestic and foreign) demand, with variations in capacity utilization serving to adjust to short-term changes.

The weak branches are marked either by rising or at least persistent deficits. In some it is the quantity of domestic supply that is inadequate, in others the quality.

Supply-side bottlenecks are found for office and data processing machinery and for motor vehicles and engines. The relationship between the trade deficit and capacity utilization in the former suggests that, especially in the eighties, the expansion in potential output failed to keep up with the exceptional growth in demand, notwithstanding its having proceeded at annual rates of between 30 and 40 per cent. The surplus recorded by vehicles and engines in the seventies gradually contracted and in recent years has been replaced by a deficit coupled with an above-normal capacity utilization rate.

There is greater cause for concern in the situation of branches, such as basic metals and chemicals, with persistent deficits that are often coupled with considerable idle capacity. Presumably these branches are unable to meet international competition in either the domestic or the world market, and can therefore be said to suffer from a "competitive disadvantage". These deficit branches are the principal obstacle to a strengthening of the international position of Italian industry and a curb on the contribution it can make to easing the external constraint.

Invisibles

The surplus on invisibles amounted to 5,412 billion lire, about 300 billion less than in 1984.

Foreign travel generated a surplus of 12,362 billion lire, up from 11,412 billion. Inflows expanded by 10.8 per cent, which was roughly the same rate as recorded in 1984, while outflows increased by 18.3 per cent, which was nonetheless down on the 33.2 per cent of the previous year. The seasonally adjusted figures also indicate a slowdown over the year.

Italian tourism prices rose by 11.6 per cent. The expenditure of foreign tourists therefore remained virtually unchanged in real terms since the number of days spent in Italy increased by 2.8 per cent (compared with a decline of 2.2 per cent in 1984) while average unit expenditure dropped by 3.4 per cent. This result was achieved in a year that saw little or no change in Italy's competitive position vis-a-vis tourists' home countries.

The further large rise in Italian residents' expenditure on foreign travel was the resultant of a weighted average increase of about 8.5 per cent in the lira equivalent of tourism prices abroad and an increase of about 9 per cent in expenditure at constant prices.

Income from capital was in deficit to the tune of 7,479 billion lire (as against 6,855 billion) as a result of payments amounting to 17,171 billion (up 12.1 per cent) and receipts amounting to 9,692 billion (up 14.4 per cent).

Interest rates in international money and capital markets were lower than in 1984, so that the increase in the deficit reflected the rise in net foreign debt and the year-on-year depreciation of the lira. Further progress was made in 1985 in reducing the share of dollar liabilities, a policy originally adopted to limit the burden caused by the appreciation of the US currency and the high nominal interest rates on dollar debt. This tended to reduce the interest component but also limited the beneficial effect that the downturn of the dollar during the year had on payments expressed in lire.

CAPITAL FLOWS

Italy recorded a net capital inflow of 814 billion lire in 1985, compared with an inflow of 5,612 billion lire in 1984 (Table 21). A net inflow of 10,333 billion lire during the first half was followed by outflows of 2,408 billion and 7,111 billion respectively in the third and fourth quarters. The outflows consisted mainly of bank capital and investment, and were partly offset by net inflows of other medium and long-term components and trade credit.

Table 21

CAPITAL FLOWS

(net; billions of lire)

	1984	1985	1985			
			1st qtr.	2nd qtr.	3rd qtr.	4th qtr.
Medium and long-term capital	**3,021**	**4,825**	**2,839**	**2,223**	**1,182**	**−1,419**
Investment	−1,026	−828	565	1,517	−304	−2,606
Loans	2,410	4,743	1,736	529	1,416	1,062
Trade credit	1,516	997	203	825	−43	12
Other (1)	121	−87	335	−648	113	113
Short-term capital	**2,591**	**−4,011**	**−140**	**5,411**	**−3,590**	**−5,692**
Trade credit (2)	−2,547	1,387	94	986	706	−399
Banking flows (3)	5,138	−5,398	−234	4,425	−4,296	−5,293
Total . . .	**5,612**	**814**	**2,699**	**7,634**	**−2,408**	**−7,111**

(1) The distribution between the 3rd and 4th quarters is estimated. — (2) With maturities up to 360 days. — (3) Change in banks' net external position, corrected for exchange rate adjustments. 1984 figures take account of the arrangements regarding the foreign assets held by Banco Ambrosiano in liquidation.

Direct investment

For the seventh consecutive year direct Italian investment abroad exceeded direct foreign investment in Italy. The net investment flows were 3,586 billion and 1,916 billion lire respectively (against 3,505 billion and 2,267 billion in 1984). The disparity thus widened to 1,670 billion lire, from 1,238 billion in 1984. New outwards investment increased from 4,091 billion to 4,474 billion lire, while disinvestment increased from 586 to 888 billion.

Since the early eighties, Italy's role in cross-frontier investment has changed. Italy is no longer a net importer but a net exporter of capital for the purchase of productive assets. In the four years from 1981 to 1984, the industrial countries with the highest net outflows of direct investment capital were Canada and the Netherlands, equivalent to 1.0 per cent of GDP (Table 22). The outflows amounted to 0.14 per cent in Italy, 0.27 per cent in West Germany, and 0.11 per cent in France. Belgium-Luxembourg and the United States recorded inflows of 0.89 and 0.38 per cent of GDP respectively.

Table 22

DIRECT INVESTMENT AND EXPORTS OF THE LEADING INDUSTRIAL COUNTRIES

	Balance of inward and outward direct investment		Outward direct investment		Export values	
	1970-1980	1981-1984	1970-1980	1981-1984	1970-1980	1981-1984
	(thousandths of GDP)		*(percentage composition)*			
EEC countries (1)						
Belgium-Luxembourg	5.6	8.9	1.6	0.6	6.0	5.2
Denmark	0.8	−0.7	0.2	0.4	2.1	1.5
France	0.6	−1.1	5.3	8.9	10.5	9.7
Germany	−1.5	−2.7	9.6	10.4	18.6	17.0
Netherlands	−4.2	−10.0	5.5	7.9	6.9	6.5
United Kingdom	−4.4	−5.5	14.3	19.6	9.4	9.4
Italy	1.4	−1.4	1.3	4.7	7.3	7.2
United States	−3.8	3.8	50.7	22.0	20.3	21.1
Japan	−1.8	−3.3	6.6	13.7	11.9	14.8
Canada	−1.7	−10.4	4.9	11.8	7.0	7.6
Total	**−2.3**	**−0.1**	**100.0**	**100.0**	**100.0**	**100.0**

Source: IMF, *International Financial Statistics* and *Balance of Payments Statistics*.
(1) Excluding Greece and Ireland.

Only Italy, France and Denmark have changed from a net direct investment inflow in the seventies to a net outflow in the eighties; the United States switched in the opposite direction. For France and Italy, however, the amount of outward investment in 1981-84 was of the same order of magnitude as the amount of inward investment over the previous decade, whereas the value of American-owned productive assets abroad still far exceeds the amount of direct foreign investment in the United States.

The acceleration in the international expansion of Italian corporations presumably reflects such factors as the growing size of some industrial groups, diversification into sectors where internationalization is a more pressing necessity, and the more advanced technology embodied in a number of products and production processes. As a consequence, the presence of Italian firms in international markets is now comparable with that of firms based in the other advanced industrial countries.

New direct foreign investment in Italy increased from 2,758 billion lire in 1984 to 4,182 billion in 1985, while disinvestment soared from 491 billion to 2,266 billion.

Portfolio investment and loans

Foreigners' interest in portfolio investments in the Italian financial market was even more lively last year than in 1984, thanks to the high yields on government securities and the excellent performance of the stock market. New foreign purchases of Italian securities amounted to 14,971 billion lire and sales to 12,851 billion, both flows expanding by more than 150 per cent with respect to the previous year. The net surplus of 2,120 billion lire was four times as large as the one recorded in 1984 (Table 23).

Table 23

PORTFOLIO INVESTMENT

(billions of lire)

	1984			1985		
	Investment	Dis-investment	Balance	Investment	Dis-investment	Balance
Foreign capital	**5,619**	**5,084**	**535**	**14,971**	**12,851**	**2,120**
Government securities	3,794	3,251	543	9,731	7,669	2,062
Treasury bills	1,072	1,203	−131	3,810	3,460	350
Treasury bonds	100	74	26	531	486	45
Treasury certificates in ECUs	102	9	93	621	64	557
Treasury certificates and other	2,520	1,965	555	4,769	3,659	1,110
Listed shares	1,329	1,118	211	4,763	4,580	183
Bonds	496	715	−219	477	602	−125
Italian capital	**1,404**	**1,766**	**−362**	**1,797**	**3,200**	**−1,403**
Foreign investment funds	442	992	−550	749	1,295	−546
Government securities	138	227	−89	308	349	−41
Listed shares	583	412	171	142	395	−253
Bonds	241	135	106	598	1,161	−563

About two thirds of these transactions concerned government securities, net foreign purchases of which amounted to 2,062 billion lire, concentrated in May, June and July (3,035 billion lire), while sales occurred predominantly in the fourth quarter, when the balance turned negative with net disposals of about 1,000 billion lire.

Foreign investors also showed interest in other Italian securities. Bond purchases, at 480 billion lire, remained at about the level of the previous year, but purchases of listed shares rose from 1,329 billion to 4,763 billion lire, although the net investment proved to be just 183 billion lire. The second half of the year was marked by significant disinvestment to realize the profits achieved owing to the rise in the stock market and the depreciation of the dollar. As the shares were sold at higher prices than had been paid for them, the number of Italian shares held by non-residents increased, despite the approximate equality in the value of purchases and sales.

Italian portfolio investment abroad also expanded significantly, from 362 billion to 1,403 billion lire, owing chiefly to the measure taken in December 1984 to allow Italian investment funds to invest a portion of their assets in foreign securities without having to lodge the non-interest-bearing deposit on foreign investment. Data on the composition of these funds' portfolios indicate that holdings of foreign securities rose from nil at the end of 1984 to about 680 billion lire at the end of 1985. The lowering of the deposit requirement from 50 to 40 per cent and then to 30 per cent does not appear to have significantly stimulated Italian portfolio investment abroad.

The net capital inflow generated by foreign loans expanded from 4,205 billion lire in 1984 to 7,063 billion in 1985. Both gross outflows and gross inflows were much more substantial last year owing to the renegotiation of medium and long-term debts involving more than 5,000 billion lire, which was accomplished without affecting the official reserves. The net capital outflow stemming from private and public Italian loans to borrowers abroad increased from 1,795 billion to 2,320 billion lire.

Short-term capital flows and the exchange rate of the lira

Short-term capital movements, in the form of trade credits and bank funds, resulted in a net outflow of 4,011 billion lire in 1985, as against a net inflow of 2,591 billion in 1984. After exchange adjustments, the net external indebtedness of Italian banks, which had increased by more than 5,000 billion lire in 1984, decreased by 5,398 billion. The outflow of bank capital was partly offset by an inflow of trade credit in the amount of 1,387 billion lire (Table 21).

Despite the official freeze on banks' external indebtedness, there was a net inflow of banking capital of more than 4,000 billion lire over the first half of 1985. In the third quarter, admonitions to the banks to bring their net debtor positions back within the limits produced capital outflows more or less comparable to the previous overshoots. Towards the end of the year strong expectations arose of an imminent realignment of EMS central rates. There was a sharp rise in the three-month forward discount of the lira against the Deutschemark, reversing the sign of the interest cover differential from + 1.5 percentage points in September to — 3 points in December. As a consequence, Italian importers and exporters reduced their foreign exchange positions, producing a dramatic effect on the net external liabilities of Italian banks, which declined by 5,293 billion lire in the fourth quarter. The resulting strains in the foreign exchange market, which are discussed in detail in the Bank of Italy's Economic Bulletin, No. 2 (February 1986), were exacerbated by disinvestment in Italian securities by non-residents.

The freeze on banks' external indebtedness was removed in December. In January 1986 the foreign exchange financing requirement for export credits was reintroduced, as was the ban on the early settlement of import contracts. These measures, together with others enacted at the same time, quickly restored orderly conditions in the foreign exchange market. The first quarter of 1986 saw an inflow of 5,021 billion lire in bank funds. After the EMS realignment in April, these measures were rescinded and exchange restrictions were eased further, resuming the gradual liberalization that has now been under way for several years.

Short-term trade credits followed basically the same pattern as bank capital over the year, with a net inflow of 1,800 billion lire over the first three quarters and a net outflow of about 400 billion in the fourth quarter. Unlike bank capital, therefore, trade credits produced a net inflow on the year, which amounted to 1,387 billion lire.

Between January 1985 and April 1986 the nominal effective exchange rate of the lira rose by 1.6 per cent, the result of an appreciation of 25.2 per cent against the dollar and a depreciation of 8.6 per cent against the EEC currencies. The central rates of the lira within the EMS were realigned downwards by 6 per cent in July. In the EMS realignment of April 1986 the lira was positioned mid-way between the revalued Deutschemark and the devalued French franc.

Italy's net financial position and external financial openness

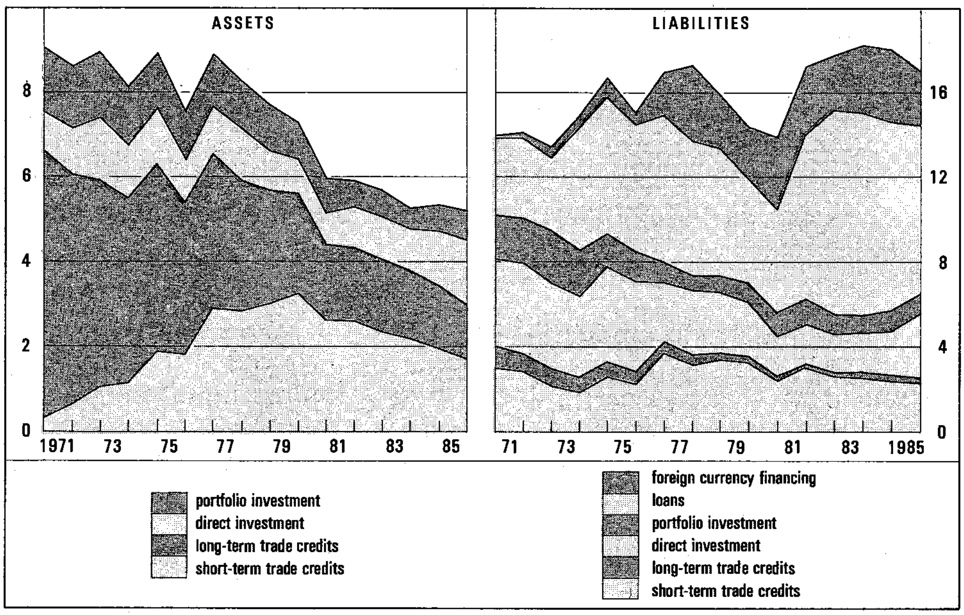
Italy's external financial position deteriorated by $9.4 billion last year to a negative balance of $31.8 billion, net of official gold reserves, or 7.8 per cent of GDP (as against 7.1 per cent at end-1984). The deterioration was due mainly to the need to finance the current payments deficit and to the increase in the dollar equivalent of liabilities denominated in other currencies.

The long period during which external financial transactions were regulated caused significant changes in the structure of capital flows, and consequently in Italy's degree of financial openness. Between 1970 and 1985 foreign financial assets acquired through official channels by households and firms declined from 9.1 to 5.2 per cent of their total financial assets (Figure 7). The bulk of the decline occurred between 1976 and 1980, at first owing to a reduction in outward investment and then, from 1979 onwards, to a decrease in export financing assets, especially those at medium and long term.

Figure 7

FOREIGN FINANCIAL ASSETS AND LIABILITIES OF THE PRIVATE SECTOR

(percentages of the total)



By contrast, the share of the non-bank private sector's total liabilities accounted for by external liabilities rose from 14 to 17 per cent between 1970 and 1985, with a low point of just over 13 per cent in 1972 (Figure 7).

The assumption of external liabilities reflected the trend of the current account balance. Thus, the large deficits recorded in 1973-76 and 1980-85 were accompanied by a rise in the external share of total liabilities from 13.4 to 17.0 per cent between end-1972 and end-1976 and from 14.4 per cent at end-1979 to 17.0 per cent at end-1985.

The servicing of medium and long-term debt, which will come to \$5.6 billion a year over the next five years, and the increasing importance of such highly volatile capital inflows as trade credits, portfolio investment and bank funds will influence the behaviour of Italy's overall balance of payments in the medium term.

PUBLIC FINANCES

Notwithstanding corrective measures, the fall in inflation and the return to growth after the stagnation of 1980-83, the public sector borrowing requirement net of settlements of past debts rose from 90.7 trillion lire in 1983 to 101.9 trillion in 1984 and to 112.3 trillion in 1985. In relation to GDP it only declined very slightly from 16.8 to 16.6 per cent and then 16.4 per cent (Table 24).

Table 24

BORROWING REQUIREMENTS

(as a percentage of GDP)

	1983	1984	1985
State sector borrowing requirement	16.3	15.5	17.9
Net of settlements of past debts	16.3	15.5	16.1
Public sector borrowing requirement	16.8	16.6	17.5
Net of settlements of past debts	16.8	16.6	16.4
Enlarged public sector borrowing requirement	17.2	16.8	17.6
Net of settlements of past debts	17.2	16.8	16.6

As a ratio to GDP, the borrowing requirement of the narrower state sector (again net of debt settlements, which are larger for this sector) followed a less regular course, primarily as a result of the takeover in 1984 by banks (in exchange for government securities delivered in 1985) of some of the outstanding liabilities of local health units, which reduced the latter's drawings on the Treasury in that year. After falling from 16.3 to 15.5 per cent of GDP in 1984, the state sector borrowing requirement rose to 110.2 trillion lire, or 16.1 per cent of GDP.

The Government Planning and Forecasting Report's target of 96.3 trillion — raised to 99.9 trillion in February 1985 — was thus exceeded. The overshoot can be attributed to the growth in the needs of INPS owing to a surge in disbursements for pensions. The increase in current expenditure net of interest payments exceeded not only the 7 per cent target, set equal to the objective for consumer price inflation, but also the actual increase in these prices.

If settlements of debts not recorded in the accounts of previous years are included, the borrowing requirements of both sectors are found to have expanded considerably compared with 1983-84, when no such operations were undertaken. Inclusion of this item takes the 1985 PSBR to 119.7 trillion lire, since the government refunded the excess tax paid by banks and settled the past debts of some non-state public bodies. The increase for the state sector was even larger, since it includes the settlement of debts incurred by local health units and the suppressed health insurance institutions, which were recorded in the accounts of the broader public sector as they arose.

The public sector is reckoned to have had a slightly expansionary effect on economic activity in 1985. This assessment is based on indices of the relevant nominal and real aggregates (including the change in the purchasing power of the public debt), with suitable lags between impulses and effects.

Analysis of the public sector's operations over the last three years shows that the small reduction in the GDP ratio of the borrowing requirement net of debt settlements was due to slower growth in interest payments and non-state public bodies' deposits with the credit system. Net of these two items, the borrowing requirement grew steadily from 6.2 per cent of GDP in 1983 to 6.4 per cent in 1984 and to 6.6 per cent in 1985.

On a national accounts basis the GDP ratio of public sector expenditure, net of interest payments and financial operations, rose by about half a point after falling in 1984. The upturn was primarily due to the increase in expenditure on social services, especially pensions and health care. Spending on the former was boosted both by the payment of the balance of cost-of-living allowances corresponding to the difference between the target and actual inflation rates in 1984 and by the increases approved for entitlements accrued in earlier years. The rise in health care spending reflected health service doctors' higher salaries under their new labour contract and the rapid increase in the cost of medicines.

The ratio of taxes and social security contributions to GDP declined slightly (Table 25). By and large, the target set for this aggregate was reached, even though some of the measures introduced generated less revenue than had been assumed in official forecasts while others planned for introduction during the year did not materialize. This positive outcome was due to the fact that some important taxes (IRPEG, ILOR, the flat-rate withholding tax on interest and, to a lesser extent, IRPEF) generated larger revenues than had been forecast in the budget.

Table 25

MAIN INDICATORS OF PUBLIC SECTOR FINANCES

(as a percentage of GDP)

	1983	1984	1985
Fiscal revenue (including EEC levies and social security contributions)	42.0	41.1	40.8
Total public sector expenditure	58.9	59.3	60.2 (1)
Deficit on current account	7.0	8.0	8.2
Net indebtedness	13.1	14.2	15.0 (1)
Net indebtedness, excluding settlements of past debts	13.1	14.2	14.2

(1) Gross of settlements of past debts corresponding to 0.8 per cent of GDP.

Direct tax revenues grew faster than GDP, primarily as a result of fiscal drag on personal income tax and the strong rise in corporate profits in 1984. By contrast, indirect tax revenues grew more slowly than GDP, owing to the performance of VAT and the failure to raise many specific taxes in line with inflation. Social security contributions only kept up with the rise in income, despite the measures to speed up payments and reduce the proportion of health care contributions charged to the budget.

The adjustment of the fiscal deficit provided for in the Finance Law and other important measures was less effective than expected. Notably, the steps taken in the social security field failed to keep government transfers to INPS within the limits set; budget and off-budget transfers amounted to 32.1 trillion lire, as against the original forecast of 22.5 trillion.

The ceilings imposed on the growth in public employees' unit wages were exceeded, albeit only slightly, owing to the combined effect of automatic wage mechanisms and the payment of the last instalment of the 1982-84 labour contract increases. The rise in earnings was only a little larger than the actual rate of inflation. The implementation of some revenue-boosting measures, notably the condonation of building offences, was postponed. On the other hand, numerous laws increasing expenditure were approved. Those regarding pensions, in particular, increased the burden on the budget on an accruals basis by around 4 trillion lire in 1985, which was only part-paid during the year and will rise to around 10 trillion in 1988 when the system reaches a steady state.

The fiscal deficit resulted in the public debt rising from 560.2 trillion lire at the end of 1984 to 681.8 trillion at the end of 1985, and from 91.1 to 99.6 per cent as a ratio to GDP. In contrast with the previous year, the government's market debt increased more slowly than the total. Recourse to the central bank consequently expanded very substantially, in part owing to the difficulty encountered in placing securities with the market towards the end of the year.

The policy of lengthening the maturity of the public debt was continued in the favourable conditions created by the further fall in inflation. The proportion of total market debt in the form of medium and long-term securities increased from 44.5 to 52.5 per cent, while that of Treasury bills fell from 32.7 to 26.9 per cent. In the first sector there was a further shift towards longer maturities with the placement of a large volume of 10-year Treasury credit certificates. At the end of 1985 the average residual maturity of government securities was 3 years and 5 months, as against 2 years and 6 months a year earlier.

Part of the difficulty encountered in controlling the needs of the public sector and its borrowing in the financial market stems from the conflict between the structural nature of the fiscal deficit and the cyclical nature of budget procedures, which appear inadequate to control the growth of public finances in the medium-to-long term.

The outlook for 1986

The budget policy formulated in the Finance Law and other, mainly tax, measures is designed to keep the state sector borrowing requirement net of settlements of past debts at its 1985 level. This implies a 1.5 point reduction in its ratio to GDP, from 16.1 to 14.6 per cent.

Achievement of this objective will be made easier by a number of measures that were approved in 1985 but which are producing their effects this year. Specifically, the changes made in taxpayers' assessment of their incomes and turnovers for IRPEF and VAT should increase revenues. Furthermore, the bulk of the revenues of the postponed condonation of building offences should be collected this year.

The fiscal policy adopted is also intended to curb transfers to non-state public bodies, in the first place by allowing them to increase their own revenues.

Another factor tending to reduce the borrowing requirement is the increase in the excise duties on oil products, due in part to the government having taken the benefits of the fall in oil prices as tax. The higher rates should yield an additional' 4 trillion lire. On the other hand, the requirement will be increased by the changes made in IRPEF rates to offset fiscal drag. These are expected to reduce revenues by 5.4 trillion lire in 1986 and by nearly 8 trillion in 1987.

The net effect of the legislation described should be a 10 trillion lira reduction in the borrowing requirement. According to the estimates recently published by the Treasury, measures to achieve a further reduction of 3 trillion will be necessary if the target set for the state sector borrowing requirement is to be achieved.

Despite the size of the adjustment, the upward trend of the PSBR has not been curbed, since many of the measures boosting revenues or cutting expenditures are of a one-shot nature, serving to reduce the level of the deficit but not its rate of growth.

The developments described highlight the need to persist with the policy of curbing public expenditure and especially its current component. This is confirmed in the recent Treasury plan for employment and economic recovery. According to the guidelines laid down in earlier documents, the adjustment of public finances should be pursued through gradual reductions in the borrowing requirement net of interest payments and, above all, in the current deficit. To this end, both current expenditure in real terms and the ratio of tax to GDP need to be kept unchanged. Achievement of these results, in conjunction with changes in some structural features of the economy, would help to ensure more balanced and lasting growth.

THE MONEY AND FINANCIAL MARKETS

The outcome for 1985

The Bank of Italy maintained a monetary stance for the year consistent with the aim of curbing inflation, but it faced operating conditions complicated by the increasing public debt, which expanded nearly twice as fast as corporate debt. The insufficiency of the budget and incomes policy measures actually taken, together with the consequences of the appreciation of the dollar in the first half of the year, made it impossible to bring consumer price inflation down to the 7 per cent target set in the Government's Forecasting and Planning Report. The poor progress in disinflation and the pressure on the financial market exerted by public borrowing slowed the reduction in nominal interest rates on government securities, which nevertheless fell by about one percentage point more than did inflation.

At the end of the year the expansion of both domestic credit to the private sector and the money supply were near the targets indicated by the Interministerial Committee for Economic Planning in September 1984. However, the growth of the money supply early in the year and that of credit in the last two months both diverged significantly from the programmed paths, necessitating corrective measures. The size and volatility of the state sector borrowing requirement, in particular, hampered interest rate policy and the control of the monetary base. Moreover, the changes in money market conditions brought about by the central bank were not always promptly transmitted to the behaviour of firms and savers owing to the slow response of bank rates.

In the first quarter the expansion of the money supply accelerated, spurred by a borrowing requirement well above the forecast and partly in response to a reallocation of financial wealth. This caused a temporary deviation from the planned growth path for the money supply, which expanded at an annual rate of nearly 17 per cent over the first four months. The failure of state borrowing to slow down to a rate compatible with the target for the year, together with the deterioration of the trade deficit, made correction unavoidable. In April, when the Treasury's line of credit with the Bank of Italy had been used up, the yield on government securities was raised by nearly one point to over 14 per cent, largely offsetting the decline in yields that had occurred during the first quarter.

In subsequent months, thanks in part to lower interest rates on bank deposits, the demand for government securities strengthened. The measures to contain monetary expansion were reinforced by central bank open market operations to mop up liquidity. Banks were also invited to observe the limit on external indebtedness. In the four months from May to August, the money supply grew more slowly, at an annual rate of 12 per cent, while the expansion of credit to the private sector remained within the target for the year.

The gradual reduction in yields on government securities therefore resumed, gathering way in the early autumn. The average rate on Treasury bills, which had declined by 0.25 points between April and August, was lowered by an additional 0.75 points in September and October to about 13.25 per cent. To diminish the resulting discrepancy between this and the prevailing money market rates, in early November the official discount rate was lowered by half a point to 15 per cent.

The depreciation of the dollar fueled expectations of an EMS realignment involving the lira. Towards the end of November these expectations led to both hedging and speculation that created heavy demand for foreign exchange. A portion of bank credits in foreign currencies was converted into lira lending, with a consequent reduction in the banking system's net external debt. Export settlements were postponed and import settlements brought forward. The outcome was a sharp deterioration in the country's foreign exchange situation. Official reserve losses amounted to 2.6 trillion lire in November, mostly in the last week of the month, and 4.6 trillion in December.

Convinced that the exchange rate of the lira was appropriate, the Bank of Italy intervened massively in the market to stifle any potential rekindling of inflation stemming from devaluation.

As a result of the reimbursement of foreign currency loans and the outflow of trade credit, bank lending in lire soared over the last two months of the year, the rate of expansion during December being virtually unparalleled in the past two decades. In the month lira lending increased by nearly 15 trillion lire (compared with 2.5 and 4.2 trillion in December 1984 and December 1983 respectively). This amounted to a seasonally adjusted annual rate of 60 per cent, following a 35 per cent rise in November.

The outflow of foreign exchange decreased bank liquidity, and this was only partly offset by Bank of Italy refinancing. To compensate, the banks sharply cut their subscription of government securities. Net of issues in settlement of past debts, the value of government securities placed in the fourth quarter was 12.5 trillion lire less than in the fourth quarter of 1984, while the Treasury's funding needs were only 2.3 trillion lire less. In the same quarter, net of funding of past debts, banks' holdings of Treasury bills and Treasury credit certificates remained virtually unchanged, compared with an expansion of 16.6 trillion lire over the last three months of 1984.

Central bank refinancing, which was expanded in order to overcome the problems created by the disruption of the centralized clearing service due to industrial action by Bank of Italy employees, was conceded at steadily higher interest rates. The rate on repurchase agreements rose from 15.7 to 18.9 per cent between end-October and end-January. Banks' free liquid reserves contracted to negative liquidity averaging 2 trillion lire in November and 8 trillion lire in December.

Despite the increased interest rates on open market operations and the soaring corporate demand for credit, bank lending rates continued their downward course. Between end-October and end-December the average cost of lira lending declined by more than half a percentage point.

To halt the outflow of foreign exchange, the behaviour of firms and banks had to be modified by means of specific measures, including administrative regulations. In mid-January the floor-price rate on Treasury bills was raised, most sharply on three-month bills. A ceiling was imposed on the expansion of bank lending in lire over the first six months of the year and the requirement to finance export credits in foreign currency was reintroduced at the rate of 75 per cent.

The temporary reimposition of the ceiling saved the private sector from having to bear the burden of higher interest rates. The January measures were strictly contingent and did not represent a change in the fundamental approach of the monetary authorities, which consists in the use of indirect techniques of credit control.

The effect of the measures was immediate, and the outflow of official reserves was reversed. The bulge in lira lending was slimmed down in line with the ceiling. The success of the measures, together with an improved outlook for the balance of payments and inflation, made it possible to lower the discount rate by one percentage point to 14 per cent in March. Following the EMS realignment in early April, involving chiefly the French franc, the foreign exchange restrictions introduced in January were rescinded and capital movements were further liberalized. In view of the encouraging trend of prices and the trade balance and the decline in interest rates worldwide, the discount rate was lowered by another point in late April and again in late May, bringing it to 12 per cent.

Lending to the private sector and total domestic credit. — When adjustment is made for the abnormal speculative expansion of bank lending in lire towards the end of the year, credit to the non-state sector grew by 36.5 trillion lire, or 10.2 per cent, in 1985. The actual accounts show an expansion of 46.6 trillion lire, or 13 per cent, just slightly exceeding the target of 12 per cent set in the autumn of 1984 (Table 26). The increase in total lending to the private sector, which includes funds raised abroad and through share issues, was 62.1 trillion lire, or 12.8 per cent. However, as a ratio to GDP it declined from 9.3 per cent in 1984 to 9.1 per cent (Table 27).

Table 26

CREDIT, MONEY SUPPLY AND FINANCIAL ASSETS

(twelve-month growth rates)

	Domestic credit		Money supply		Liquid assets (M3)	Financial assets (2)
	Financing of the non-state sector (1)	Total	M2A	M2		
1981 - Dec. (3)	13.5	18.1	10.0	10.0	16.3	17.0
1982 - Dec. (3)	13.4	20.9	18.0	18.0	18.0	19.9
1983 - Dec.	13.2	20.7	11.5	12.3	13.6	20.5
1984 - Dec. (4)	15.6	19.7	11.2	12.1	14.0	19.7
1985 - Dec. (5)	13.0	18.1	10.1	11.1	11.6	17.6
	(10.2)	(16.9)				
1986 - Mar. (6)	11.3	16.5	8.9	9.4	11.1	17.2

(1) Financing by banks and special credit institutions and securities issued by enterprises on the domestic market. The non-state sector comprises households and firms, insurance companies and public bodies not included in the state sector. — (2) Domestic financial assets, net of shares and actuarial reserves. — (3) Adjusted for the deposit against payments abroad. — (4) Adjusted for the distortions in banking statistics connected with the elimination of the ceiling on bank lending. — (5) The growth rates of financing of the non-state sector and total domestic credit indicated in brackets are adjusted for the abnormal expansion in banks' lira loans in November-December 1985. — (6) Provisional. For M3 and financial assets, data refer to January.

Even including the year-end bulge in bank lending, the 1985 share of total credit flows to the private sector intermediated by banks and special credit institutions was about 75 per cent, as in 1984. The growth differential between lending by banks and that by special credit institutions widened again, the latter expanding by 9.5 per cent, or 6 points less than bank lending. Adjusted for the surge in bank lending, however, the gap narrows to 1.5 points. The contribution of medium-term foreign loans was larger than in 1984. The corporate debt to sales ratio diminished again after the increase registered in 1984, resuming the trend shown since the second half of the seventies.

Despite a robust rise in investment in plant and equipment for the second consecutive year, corporate debt rose only modestly, thanks to greater self-financing. Profit margins widened, especially for medium-sized and large firms, and financial costs diminished as a share of sales revenues. Financial profits expanded, thanks to careful management of working capital. Stockbuilding was held to the minimum necessary to supply production needs, while the composition of financial assets shifted towards government securities, which accounted for 15 per cent of the total at the end of the year. Corporate liquidity, as measured by lira assets, increased on average for the year.

Table 27

TOTAL DOMESTIC CREDIT AND LENDING TO THE PRIVATE SECTOR

(changes in billions of lire)

	1981	1982	1983	1984	1985
Total domestic credit	**73,336**	**100,640**	**120,626**	**139,723**	**153,706**
State sector borrowing requirement (1)...	45,238	69,036	85,194	91,400	107,111
Finance to the non-state sector (2) .... (+)	28,098	31,604	35,432	48,323	46,595
finance to public bodies (3) .... (−)	*1,742*	*3,363*	*4,390*	*7,020*	*2,427*
foreign loans .... (+)	*8,641*	*3,074*	*755*	*−839*	*2,064*
endowment funds .... (+)	*3,154*	*7,384*	*9,431*	*6,548*	*5,130*
share issues (4) .... (+)	*2,001*	*2,038*	*2,967*	*4,948*	*4,361*
other items (5) .... (+)	*3,757*	*3,582*	*4,691*	*5,410*	*6,399*
Total finance to the private sector .... (=)	**43,909**	**44,319**	**48,886**	**57,370**	**62,122**
Percentage changes (6)	*17.5*	*14.6*	*13.7*	*13.3*	*12.8*
As a percentage of GDP	*10.9*	*9.4*	*9.1*	*9.3*	*9.1*

(1) Net of borrowing abroad, Treasury loans to credit institutions and securities issued to fund debts. — (2) The non-state sector comprises households and firms, insurance companies and the public bodies not included in the state sector. Loans to the sector include the funding operations under footnote (1) and, for 1981 and 1982, exclude bank loans to finance the non-interest-bearing deposit on payments abroad. The 1984 figures are adjusted for the distortions in banking statistics connected with the elimination of the ceiling on bank lending. — (3) Credit institutions' lending to non-state public bodies, adjusted for the funding mentioned in footnote (1) above and local authorities' bond issues. — (4) Net share issues of private sector companies and third parties' contributions to state-controlled companies. — (5) Bad debts of the credit institutions, acceptances, atypical securities and other minor items.— (6) Growth rates are calculated net of shares in view of the difficulty of determining their outstanding amount.

The return of much of industry to health, the good profits outlook and the rise of new capital market intermediaries such as investment funds made it possible to channel a substantial flow of equity capital to firms. Fund-raising by new share issues in the stock market amounted to about 4.3 trillion lire, or 7 per cent of total financing. This was lower than the level recorded in 1984, which had, however, been much higher than in previous years. The main beneficiaries of this flow of funds have so far been a small number of large industrial groups. The growth and diversification of share offerings in the early part of 1986 confirm both the tendency of firms to strengthen their capital and their widespread success in regaining financial soundness.

The public sector's demand for credit again expanded faster than that of the corporate sector. The state sector borrowing requirement for the year overshot the target set in September 1984 by 13 trillion lire and in total exceeded 107 trillion lire, or 22 per cent of the initial debt. The result was an expansion of total domestic credit of 153.7 trillion lire, or 18.1 per cent. Adjusting for the year-end lending bulge, the rate of expansion was 16.9 per cent, slower than the 19.7 per cent recorded in 1984. The ratio of total credit to GDP declined from 22.7 per cent to 21.0 per cent. The share of total credit going to the state sector increased from 65 to 75 per cent.

Financial assets and the money supply. — Financial assets expanded by 17.6 per cent, compared with the 18.1 per cent growth in total domestic credit. Despite the substantial absorption of liquidity by the balance-of-payments deficit, the growth of financial portfolios outstripped that of GDP by more than 6 percentage points. Including share ownership, the value of the private sector's domestic financial assets at the end of the year was more than twice the gross domestic product, an increase of more than 40 percentage points compared with the previous year.

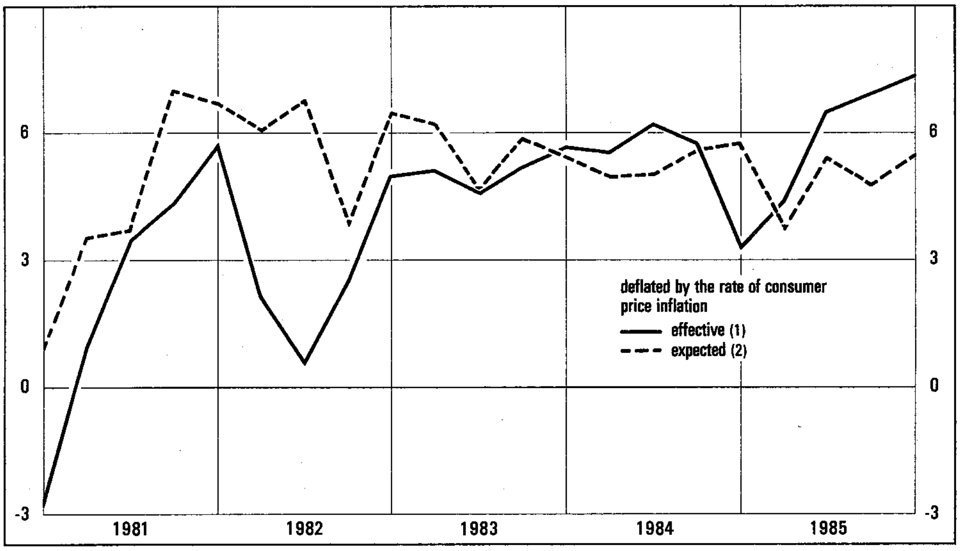
The M2 money supply expanded by 11.1 per cent, in line with the growth in nominal GDP. The expansion of M2A (i.e. M2 net of bank certificates of deposit) was one point less. Other financial assets grew nearly three times as fast, by 30 per cent. The absorption of these massive amounts of financial assets by savers' portfolios is accounted for partly by the maintenance of sufficiently high real yields on government securities and adequate differentials with respect to more liquid assets and partly by the popularization of a new financial product, namely investment fund units, which showed very substantial capital gains as a result of buoyant share prices.

Adjusted for actual consumer price inflation, the yield on six-month Treasury bills averaged 5 per cent over the year, half a point less than in 1984. The yield earned by companies declined by about one point owing to the increase in taxation (Figure 8). Nominal interest rates declined. The yield on Treasury bills decreased by 1.5 points, and the average rate on bank deposits by nearly as much. The maximum deposit rate dropped by 2.5 percentage points, again producing a significant differential with respect to government securities and hence facilitating sales of the latter.

Private sector holdings of government securities expanded by 26 per cent. Expectations of a gradual decline in nominal interest rates lent further impetus to the shift towards longer maturities that had begun in 1984. Investors were strongly attracted to investment fund units, which satisfied the desire for portfolio diversification in terms of instruments and issuers, at the expense of traditional financial

Figure 8

REAL RATE OF INTEREST ON 6-MONTH TREASURY BILLS



(1) The nominal Treasury bill rate, calculated as the average of the last month of each quarter and the first month of the next, deflated by the annualized change in consumer prices over the six following months. — (2) The nominal Treasury bill rate, calculated as in footnote (1) above, deflated by the annualized expected change in consumer prices over the six following months compared with the six previous months using Mondo Economico survey data.

products that also act as savings instruments, such as bank deposits. There was no negative impact on the demand for government securities, however, because about 70 per cent of the net proceeds of the funds' sales were invested in Treasury securities. Firms were able to revive a major channel for direct access to personal savings via the stock market and the investment funds; their dynamic financial management enhanced their role in the financial and money markets, at times in competition with credit intermediaries.

The outlook for 1986

The successful management of the exchange crisis and the slowdown in the expansion of bank lending in early 1986 have made it possible to resume the lowering of interest rates. The fall has been rapid, benefiting from the improvement in the general economic situation and the decline in interest rates abroad. The official discount rate has been lowered by 3 points, while the rate on temporary financing by the Bank of Italy has been brought down from 19 per cent at the beginning of February to less than 12 per cent in May in response to improved liquidity. The interest rates on Treasury bills have come down by 2.5 points from their January peak and nearly 2 points compared with their end-1985 level.

The decline in bank rates, which had been lowered more than those on government securities in the course of 1985, has not been as pronounced. Minimum lending rates have returned to their end-1985 levels, after the sharp rise early in the year, but at the end of April average lending rates were still nearly a point higher than in December. Maximum deposit rates, however, have declined by about half a point so far this year; the slowness of their response reflects not only the built-in inertia of the deposit market but also the sharpening competition from investment funds and other forms of financial investment.

Through direct talks with a broad group of institutions, the central bank urged banks to respond more promptly to the market's signals of declining interest rates. Moreover, in May the group of banks pledging to subscribe a set quota of securities at Treasury bill auctions in proportion to their volume of business was enlarged to include the twenty leading banks, which together account for more than 50 per cent of Italian bank deposits and supply two thirds of the demand for Treasury bills.

In the three months to the end of February, bank deposits declined slightly in seasonally adjusted terms. The twelve-month expansion consequently slowed from 13.3 per cent in November to 8.1 per cent in February. Deposits began to expand again in March and April, owing partly to the rapid growth in government borrowing and the inflow of funds from abroad, bringing the pace of growth of M2 for the first four months to 9 per cent, which is in the middle of the four-point-wide target range for the expansion of the money supply set in September 1985 and confirmed in February.

Domestic credit to the non-state sector has grown at a slightly faster pace than the 7 per cent target for the year, which when adjusted for the abnormal growth in lending in the last two months of 1985 corresponds to a rate of about 9 per cent. Measured with respect to the actual figures for end-1985, this aggregate — that is, bank lending, special credit and net corporate bond issues — expanded at a seasonally adjusted pace of 8 per cent in the first four months of the year. The deflation of the bulge in bank lending in lire achieved by the imposition of the ceiling was partly offset by an acceleration in lending in other currencies and in loans by industrial credit institutions. The first quarter also saw bond issues by state holding companies worth 3.5 trillion lire.

The fast growth of the state component caused the expansion of total domestic credit to exceed the 13 per cent target by three percentage points. The state sector borrowing requirement for the first four months came to 40 trillion lire, 2 trillion more than the uncomfortably high level of 1985. Seventy-five per cent of the requirement was met by securities issues and most of the rest by drawings on the Treasury's overdraft facility with the Bank of Italy, which in fact exceeded the credit limit related to the budget approved by Parliament.

A slowdown in the growth of government borrowing to bring its overall pace into line with the 110 trillion lire target for the year appears necessary if interest rates on government securities are to come down in line with inflation. If this action is accompanied by longer-term measures to right the public finances it will help to improve savers' expectations and maintain substantial demand for government securities, thus keeping the creation of monetary base within limits consistent with the targets for the growth in the money supply and the expansion in credit to the private sector.

THE CENTRAL BANK'S OPERATIONS AND CONTROL OF THE MONETARY BASE

Control of the monetary base

Net of changes in the compulsory reserve coefficient, monetary base and bank reserves increased by 14.6 and 18.1 per cent respectively in 1985 (Table 28); the rate of growth was affected by the expansion in liquidity in the closing months of the year as a direct and indirect result of the disruption of the clearing system operated by the Bank of Italy. The gradual return to more normal liquidity conditions and the restrictions introduced to curb the outflow of foreign exchange reserves brought the twelve-month rate of increase in bank reserves down to 10.5 per cent in January 1986 and 9.5 per cent in March and reduced that in monetary base to 10.3 and 10.9 per cent in these two months respectively.

Table 28

MONETARY BASE AND BANK DEPOSITS

(percentage changes on an annual basis) (1)

	1983	1984	1985	1984 Quarters I	II	III	IV	1985 Quarters I	II	III	IV	1986 Ist qtr. (3)
Compulsory reserves												
adjusted (2)	14.4	12.9	14.8	−0.1	24.6	12.0	18.6	7.9	24.7	13.0	12.9	−12.5
unadjusted	*19.8*	*16.1*	*19.1*									
Bank reserves												
adjusted (2)	14.0	14.0	18.1	−0.9	24.9	5.0	25.0	3.0	27.6	10.3	28.6	−21.0
		(12.2)	(20.0)				(19.8)	(7.5)				
unadjusted	*16.9*	*16.9*	*21.8*									
Monetary base												
adjusted (2)	13.3	12.5	14.6	2.5	21.2	6.7	18.7	7.9	22.5	7.5	19.1	−4.1
		(11.4)	(15.7)				(15.5)	(10.8)				
unadjusted	*15.0*	*14.4*	*17.3*									
Bank deposits	13.3	11.6	10.1	8.3	9.9	13.4	16.2	16.9	11.6	11.1	2.9	3.7

(1) Based on end-of-period values. The quarterly figures are seasonally adjusted. — (2) Adjusted for the change in the compulsory reserve coefficient and for the non-interest-bearing deposit against lending in excess of the ceiling. The figures in brackets are adjusted for the estimated 1 trillion lira abnormal rise in banks' cash balances at end-1984. — (3) Provisional.

Analysis of the main sources of monetary base creation (Table 29) illustrates both the expansionary effect of the public sector borrowing requirement and the severity of the external constraint. The total

Table 29

MONETARY BASE (1)

(changes in billions of lire)

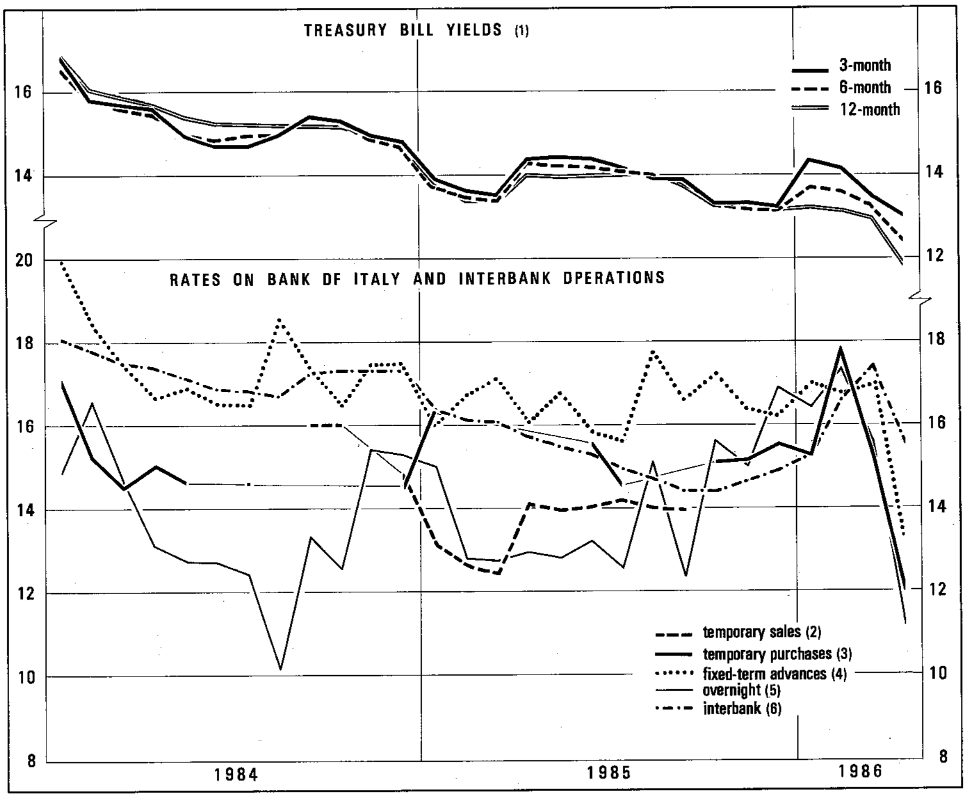
	1983	1984	1985 Year	1985 Quarters I	II	III	IV	1986 1st qtr. (2)
Foreign sector (3)	**8,840**	**5,141**	**−13,735**	**−4,605**	**3,051**	**−3,176**	**−9,006**	**−1,170**
Balance of payments	3,793	57	−8,352	−4,372	−1,371	1,115	−3,724	
Net foreign position of banks	4,996	5,138	−5,393	−234	4,425	−4,297	−5,292	
Treasury	**4,514**	**10,027**	**27,518**	**10,135**	**−405**	**3,538**	**14,249**	**12,218**
Borrowing requirement	88,257	95,387	122,816	27,863	32,827	32,719	29,408	27,451
Net sales of securities	−74,829	−75,431	−82,586	−16,920	−32,194	−27,218	−6,254	−13,875
primary market	−53,220	−70,419	−81,107	−14,527	−30,028	−27,067	−9,484	−16,982
Treasury bills	8,632	−13,187	1,802	4,090	−10,230	−5,989	13,931	−787
Treasury credit certificates	−59,602	−54,436	−68,696	−16,544	−12,533	−18,940	−20,679	−9,336
other securities	−2,250	−2,796	−14,213	−2,073	−7,266	−2,139	−2,736	−6,859
of which: securities issued to fund debts	—	—	*−10,403*	—	*−7,036*	*−2,938*	*−429*	
open market	−21,609	−5,012	−1,479	−2,393	−2,166	−151	3,230	3,107
of which: repurchase agreements	*−1,628*	*2,661*	*4,933*	*−1,261*	*440*	*2,301*	*3,453*	*4,193*
Other financing (4)	−8,914	−9,929	−12,711	−807	−1,037	−1,963	−8,904	−1,258
Refinancing	**−3**	**−218**	**5,881**	**17**	**−306**	**2,258**	**3,911**	**−6,202**
Other sectors	**−747**	**−1,104**	**−589**	**−830**	**−497**	**−1,501**	**2,239**	**−4,538**
TOTAL	**12,604**	**13,847**	**19,075**	**4,718**	**1,845**	**1,118**	**11,393**	**−42**
Non-state sector	**4,081**	**3,861**	**4,002**	**−1,655**	**1,389**	**−116**	**4,384**	**−405**
Banks	**8,523**	**9,986**	**15,072**	**6,373**	**455**	**1,234**	**7,009**	**363**
Compulsory reserves	9,092	8,855	12,213	8,926	−941	2,418	1,810	4,746
Non-interest-bearing deposits against excess lending	−927	−2	—	—	—	—	—	877
Excess reserves	359	1,133	2,859	−2,553	1,396	−1,184	5,200	−5,260

(1) Rounding may cause discrepancies in totals. — (2) Provisional. — (3) The creation of monetary base by the foreign sector does not match the sum of the items indicated owing to differences between the balance-of-payments statistics and the consolidated balance sheet of BI-UIC and to the inclusion, up to January 1983, of the convertible currencies of banks. — (4) PO deposits of the public and the banks, foreign loans, indemnities lodged with the Deposits and Loans Fund, loans granted by banks and special credit institutions to autonomous government agencies, and the deposits of social security institutions with the Treasury.

expansion in monetary base came to 19,075 billion lire, monetary financing of the Treasury increased by 27,518 billion (22.4 per cent of the borrowing requirement) and the net outflow of foreign exchange reserves exceeded 13,700 billion; in 1984, by contrast, monetary base had been created through both channels — 10,027 billion lire from monetary financing of the Treasury (10.5 per cent of the borrowing requirement) and 5,141 billion lire from the external sector. The increase in refinancing (5,881 billion lire), which was concentrated mainly in the second half of 1985, only partly offset the simultaneous destruction of monetary base via the external sector and reflected the appreciable increase in fixed-term advances, which were granted, at increasingly punitive interest rates, in order to ensure the operation of the payments system during the disruptions mentioned above.

Figure 9

SHORT-TERM INTEREST RATES



(1) Average yields at auction; compound interest, calendar year. — (2) Maximum rate in the month. — (3) Minimum rate in the month. — (4) Weighted average of the official rate and penalty rates. — (5) Monthly average of daily rates. — (6) Monthly average of data reported at 10-day intervals.

The expansion in monetary financing of the budget deficit reflects the difficulties encountered in selling sufficient government securities to meet the borrowing requirement at the interest rates offered by the Treasury; including operations to fund past debts, the borrowing requirement exceeded 122 trillion lire, but sales of government securities came to only 82,586 billion. The difficulties this created for control of the monetary base are also apparent from the direction of central bank intervention in the money market; whereas in 1984 the Bank of Italy had financed the banking system primarily through fixed-term advances and temporary purchases of securities (Figure 9), last year temporary sales again became substantial, amounting to 27,120 billion lire in gross terms, compared with 12,591 billion the preceding year.

Developments in 1985

The year opened with a reduction in discount rate from 16.50 to 15.50 per cent; the move, which brought official interest rates back to the level of the previous August, took account of the fall in inflation and the slowdown in bank lending after the substantial increase in the second and third quarters of 1984 and accentuated the decline in yields that had begun in the last few months of that year.

In the first few months of 1985 the situation in the money market changed rapidly as a result of the large and unexpected expansion in the budget deficit and the contraction in the supply of government securities on the secondary market caused by changes in the provisions on the tax-deductibility of interest paid by companies; this led to greater demand for new issues of Treasury credit certificates, but the volume offered was not increased sufficiently to cover the growing borrowing requirement and to offset the shortfall in sales of Treasury bills (1,731 billion lire in the first two months) caused by slack demand in view of the progressive reduction in floor-price rates.

The disparity between the Treasury's financing requirements and sales of securities widened in March, when the terms offered on the first Treasury credit certificates to be issued by the tender method also failed to find favour with investors. The result was a substantial drawing on the Treasury's current account (4,810 billion lire), practically exhausting the overdraft facility by the end of the month. In the first three months of the year sales of government securities totaled 14,527 billion lire, compared with a borrowing requirement of 27,863 billion; drawings on the Treasury's current account exceeded 8 trillion lire in addition to the 10 trillion used in the final quarter of 1984.

Despite the destruction of monetary base by the external sector, the Bank of Italy therefore had to sell securities in the market to curb the expansion in bank liquidity, in contrast to its operations dictated by seasonal factors in the early months of previous years. Meanwhile, the growth in bank deposits continued to accelerate, rising at an annual rate of 16.9 per cent in the first quarter of 1985, compared with 16.2 per cent in the preceding quarter.

In the absence of a fiscal policy aimed at reversing the excessive expansion in the borrowing requirement, the need to bring the monetary financing of the Treasury down to a level compatible with the targets for flows of funds necessitated an increase in interest rates on government securities at the end of April, after a further auction of Treasury credit certificates had proved unsatisfactory. In view of the temporary nature of the move, the increase was larger at the short end of the maturity range (Figure 9); the base yield on three-month Treasury bills was raised by more than one point, and that on twelve-month bills by 60 basis points. At the same time the maximum rate on temporary purchases offered by the Bank of Italy was raised substantially, from 12.45 to 14.10 per cent. At the beginning of May the first coupon on Treasury credit certificates and Treasury bond yields were also increased slightly.

The demand for government securities picked up; favourable seasonal factors and the resumed inflow of funds via the banking system halted the outflow of foreign exchange reserves in April and created a flow in the opposite direction in the months that followed. The expansion in bank deposits slowed down substantially to an annual rate of 11.6 per cent in the second quarter, though it remained above the level consistent with the targets for the year.

During the summer the monetary authorities again called upon the banks to comply with the limit on net foreign indebtedness introduced a year earlier; in this way it was possible to wipe out the large second-quarter increase in their net foreign position, which had fueled the supply of domestic credit. Shorter-term Treasury bill rates gradually decreased.

The measures to contain the growth in bank reserves were effective, aided by the demand for securities at issue and the conversion of temporary sales of securities by the Bank of Italy into outright sales; at the end of August the increase in bank reserves and bank deposits in relation to the preceding December came to 12.1 and 13.4 per cent respectively on a seasonally adjusted annual basis.

A cut in bank deposit rates at the very end of August stimulated increased demand for Treasury bills the following month; the demand for some maturities exceeded the supply, causing yields to fall. Demand for Treasury credit certificates was equally strong, both in mid-September and at the beginning of October, when the issue of Treasury bonds also met with considerable success. The substantial volume of sales enabled the Bank of Italy to let the remaining securities repurchase agreements run their course.

In October the yield on Treasury bills was reduced further; the average rate was 0.7 points lower than in August 1985 and 1.4 points below that recorded in December 1984. For the first time since January, the banking system found it necessary to seek substantial financing from the Bank of Italy, partly owing to payments in connection with the large purchases of Treasury paper. In the course of the month the Bank of Italy made temporary purchases of securities totaling 14 trillion lire gross and 7 trillion net. In response to the movement in market rates, the discount rate was therefore reduced from 15.50 to 15 per cent with effect from 8 November. At the same time, the penal rates on frequent recourse to fixed-term advances were reduced, thereby increasing the flexibility of these operations, which began to be used more frequently again.

The tensions in the foreign exchange market, which had suddenly become more acute towards the end of November, prompted borrowers to repay their foreign currency debt by borrowing in lire, on which interest rates had fallen in parallel with those on Treasury bills. The massive outflow of foreign exchange reserves (6,100 billion lire between mid-November and the end of the year) exacerbated the already difficult liquidity situation caused by the problems in the payments system.

It became increasingly difficult to sell government securities in the market, partly because the yields offered on new issues of Treasury bills were further reduced, albeit gradually. Despite considerable purchases of securities at issue by the Bank of Italy, drawings on the Treasury's overdraft facility amounted to 6,808 billion lire in November alone, 1,912 billion more than permitted by law; the overshoot was eliminated within the statutory 20-day period, thanks to tax revenues received in December.

To counter the outflow of foreign exchange that was gradually gathering pace and to ensure that banking transactions were carried out in an orderly manner, the Bank of Italy supplied the banking system with liquidity by purchasing securities on a temporary basis at progressively higher interest rates and by activating the penal rates on fixed-term advances. The effect of the move was particularly apparent in very short-term rates: overnight rates rose from an average of 15.6 per cent in October to 16.8 per cent in December, with a peak of 18 per cent; interbank rates also increased, from 14.4 to 14.9 per cent.

Given the tighter monetary conditions, it was to be expected that the fall in bank interest rates would at least halt, if not give way to a rise, since the demand for loans in lire was increasing at the extremely rapid annual rate of 46 per cent in the last two months of the year and deposits were stationary. Bank interest rates nonetheless continued to decline, although more slowly.

Despite liquidity being negative net of central bank financing, the official reserves decreased by a further 2 trillion lire in the first half of January. In these circumstances, a general increase in yields sufficient by itself to curb exchange rate speculation quickly enough would have had to be so large that it would have had serious repercussions on economic activity and government debt servicing.

In mid-January it was decided to reintroduce the ceiling on bank lending in lire until the end of June, at the same time as raising Treasury bill rates, with the largest increases at the short end of the maturity range, and introducing exchange controls to stem the outflows of capital (see the chapter on Capital Flows). The profile of the permitted growth in bank lending was designed to neutralize rapidly the abnormal increase in lending that had occurred in the closing months of 1985 and to bring the expansion in the aggregate back into line with the objectives for 1986.

The package of measures reduced market uncertainty by reaffirming the authorities' intention to defend the position of the lira within the EMS after the July realignment. Demand for Treasury bills picked up, causing allotment rates to decline in relation to floor-price rates; the yields on twelve-month bills remained unchanged between the middle and the end of January, despite an increase of 32 basis points in the floor-price rate.

The impact of the measures was reinforced by the change in the mix of central bank intervention in the money market. A larger proportion of the banking system's demand for funds, which was boosted by the raising of the compulsory reserve coefficient, was met by means of temporary purchases of securities rather than fixed-term advances; the volume of the former was exceptionally high — more than 15 trillion lire outstanding at the end of January and almost 10 trillion a month later — but it was regulated in such a way as to induce a sharp increase in the average rate, which reached 18.7 per cent in February, higher than the maximum rate on fixed-term advances. By taking advantage of the flexibility afforded by securities repurchase agreements, it was possible to tighten the controls on bank reserves; between December and February the overnight and interbank rates increased further by averages of 0.6 and 1.7 percentage points respectively, with the overnight rate exceeding 20 per cent on occasion.

The banking system steadily reduced outstanding lending in lire in line with the ceiling, and lending rates rose; demand for foreign currency loans revived and by the end of February the foreign exchange reserves had already increased. The improvement in expectations was evident in the substantial purchases of Treasury bonds, which were issued monthly from the beginning of the year onwards, whereas the market's interest in Treasury credit certificates waned in relative terms.

In March, when the clearing system had returned to normal, the banking system's total borrowing from the central bank decreased; the fixed-term advances totaling 2,821 billion lire that had been outstanding at the end of the preceding month matured and the volume of temporary purchases fell by 1,371 billion lire; the rate of interest on the latter fell to a monthly average of 15.3 per cent. The contraction in lending to the banking system made it possible to offset the substantial drawings of 5,834 billion lire on the Treasury overdraft facility caused by an unforeseen surge in the borrowing requirement. In the first quarter the monetary base contracted by 4.1 per cent on an annual basis, confirming that bank liquidity had returned to more normal levels.

This progress and the sharp slowdown in inflation made it possible to reduce the discount rate to 14 per cent at the end of March, mirroring similar moves in the majority of western countries. In April, after the realignment within the EMS, Treasury bill yields fell below 13 per cent, thus returning to the levels of the autumn of 1979; the average rate on temporary purchases was 13.3 per cent, while overnight rates fell by almost four percentage points to 11.7 per cent. The issue of six-year Treasury credit certificates convertible into fixed-rate bonds after one year was well received by the market.

The discount rate was reduced to 13 per cent at the end of April in view of the improvement in the balance of payments and the expectation that the further slowdown in inflation would continue. Yields on Treasury bonds were lowered to about 11 per cent in May and the first coupon on Treasury credit certificates was cut from 13.8 to 12.5 per cent; the demand for these securities was very high. At the end of the month a further one-point reduction was made in the discount rate.

In May the Bank of Italy also took steps to further develop the market in government securities and to increase its stability by enlarging the group of credit institutions that for the last two years or so have undertaken to subscribe a predetermined volume of Treasury bills at auction and to sell them on to investors, thereby ensuring continuity of demand for such securities and fostering orderly market conditions.

BANKING

During most of 1985 banks' business suffered from a weakening in the demand for credit that reflected firms' increased self-financing capacity and the weakening of economic activity. Nonetheless, towards the end of the year there was a sharp upturn in the demand for lira loans, fueled by expectations of a devaluation of the lira. This surge in lending, however, was completely reabsorbed in the early months of 1986 as a result of the monetary and exchange rate policy measures described in earlier chapters. After the first few months of 1985 fund-raising showed a tendency to slacken and this became more pronounced from December onwards. In the central part of the year the causes of the slowdown included both monetary base policy and that for yields on government securities, which banks did not try to counter; more recently, it has reflected the growing shift in the public's demand from bank deposits to alternative financial instruments.

Table 30

BANK DEPOSITS AND LOANS (1)

(percentage rates of increase)

	1981	1982	1983	1984	1985					1986 1st quarter (5)
					Year	I qtr.	II qtr.	III qtr.	IV qtr.	
Deposits	9.2	18.2	13.3	11.6	10.1	16.9	11.6	11.1	2.9	3.7
Loans (2)	10.2	9.8	14.0	17.1	15.6	15.4	12.3	10.8	24.5	–8.0
Treasury bills (3)	7.1	43.0	–11.4	–7.7	–35.1	–29.1	6.0	–48.6	–53.9	–71.6
Medium & long-term securities (4)	5.4	18.8	30.4	12.0	18.5	17.8	30.2	12.8	13.1	6.5

(1) Quarterly data are seasonally adjusted annualized rates. — (2) Including investments in bankers' acceptances and the funding of bank loans but excluding loans to finance the deposit on purchases of foreign exchange in force from May 1981 to February 1982. The foreign currency component is valued net of exchange rate adjustments. The 1984 figures have been adjusted for the elimination of the ceiling on loans. — (3) Net of operations under the Ministerial Decree of 27.9.1974. Temporary purchases of securities under repurchase agreements with the Bank of Italy are also excluded while temporary sales are included. — (4) Net of the effect of the funding of bank loans. — (5) Provisional.

Lending grew over the year by 15.6 per cent, which was 1.5 points less than in 1984 (Table 30). A large part of this growth was due to the acceleration in lending in November and December; when this is adjusted for, the growth drops to 10.9 per cent. During these two months foreign currency loans were switched into lira loans on a substantial scale. The increase in deposits declined from the previous year's 11.6 per cent to 10.1 per cent. In the last few months of 1985 the

PROFIT AND LOSS ACCOUNTS OF THE BANKS: FORMATION OF PROFIT (1)

	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985 (3)
	As a percentage of total resources									
Net interest income	**3.43**	**3.21**	**2.92**	**2.75**	**3.46**	**3.54**	**3.30**	**3.37**	**3.36**	**3.24**
Non-interest income	**0.89**	**0.94**	**0.98**	**0.95**	**1.00**	**1.23**	**1.27**	**1.19**	**1.28**	**1.29**
securities trading	*0.25*	*0.34*	*0.46*	*0.45*	*0.44*	*0.56*	*0.66*	*0.55*	*0.66*	*0.69*
Gross income	**4.32**	**4.15**	**3.90**	**3.70**	**4.46**	**4.77**	**4.57**	**4.56**	**4.64**	**4.53**
Operating expenses	3.04	2.91	2.78	2.72	3.01	2.95	2.97	3.15	3.15	3.03
staff costs	*2.42*	*2.21*	*2.08*	*1.99*	*2.20*	*2.14*	*2.06*	*2.31*	*2.27*	*2.18*
Net income	**1.28**	**1.24**	**1.12**	**0.98**	**1.45**	**1.82**	**1.60**	**1.41**	**1.49**	**1.50**
Allocations to provisions (net)	0.95	0.87	0.76	0.69	0.99	1.30	0.99	0.72	0.71	0.67
for loan losses	*0.29*	*0.37*	*0.37*	*0.33*	*0.44*	*0.44*	*0.46*	*0.43*	*0.39*	*0.32*
Extraordinary income and withdrawals from provisions for loan losses	0.01	0.01	—	0.04	0.01	0.03	0.08	0.03	0.02	0.07
Profit before tax	**0.34**	**0.38**	**0.36**	**0.33**	**0.47**	**0.55**	**0.69**	**0.72**	**0.80**	**0.90**
Tax	0.18	0.21	0.19	0.14	0.24	0.27	0.40	0.43	0.44	0.47
Net profit	**0.16**	**0.17**	**0.19**	**0.19**	**0.23**	**0.28**	**0.29**	**0.29**	**0.36**	**0.43**
	Other data									
Total resources *(billions of lire)*	169,371	208,183	250,435	307,772	372,503	441,537	507,235	591,493	662,436	771,837
Number of employees	227,338	239,901	249,999	261,505	274,889	287,420	293,002	299,879	302,814	304,090
Total resources per employee *(millions of lire)*	745	868	1,002	1,177	1,355	1,536	1,755	1,998	2,215	2,538
Staff costs *(millions of lire)*	18.0	19.2	20.8	23.4	29.8	32.8	36.1	46.2	50.2	55.2
	Percentage rates of increase									
Staff costs	11.8	6.7	8.3	12.5	27.8	9.7	13.2	28.0	8.7	10.0
Total resources per employee:										
in nominal terms	16.6	16.5	15.4	17.5	15.1	13.4	14.3	14.0	10.7	14.6
in real terms (2)	0.1	−1.3	2.7	1.5	−5.0	−4.5	−1.8	−1.0	0.3	5.5

(1) Excluding central credit institutions and, except for the item "Number of employees", credit institutions which at the dates in question submitted profit and loss returns at times other than the end of the year. From 1983, the figures for net interest income and non-interest income, especially from securities trading, are not comparable to those for previous years. — (2) Deflated using the cost-of-living index. — (3) Provisional.

7

banks met the demand for lira loans, which expanded much faster than deposits, by disinvesting heavily from Treasury bills and reducing their purchases of other securities.

In the first four months of 1986 the stabilization package produced a sharp fall in lira loans, while lending in foreign currency rose considerably from February onwards. By end-April the twelve-month rate of increase in total lending had fallen to 9.3 per cent, with the lira component rising by 11.3 per cent. Over the same period the slowdown in fund-raising was more pronounced, the rate falling to 7.7 per cent.

In 1985 the banking system maintained its share of total lending to non-financial businesses at the high level of the previous year. By contrast, deposits' share of total financial assets decreased from 49.8 to 47.3 per cent. On the other hand, banks not only placed a large volume of government securities but also developed their supply of services such as portfolio management. In addition, they set up numerous investment fund management companies and financed leasing and factoring companies on an increasing scale.

Bank interest rates came down substantially. The 1985 average rate on lira loans was 2 points down on the equivalent 1984 figure, while the unit cost of deposits dropped by 1.1 points. Since the structure of banks' balance sheets did not shift significantly, these changes caused net interest income to decrease from 3.36 to 3.24 per cent of total resources (Table 31). This was offset by a reduction in operating expenses from 3.15 to 3.03 per cent, largely owing to the virtual halt in the expansion of staff.

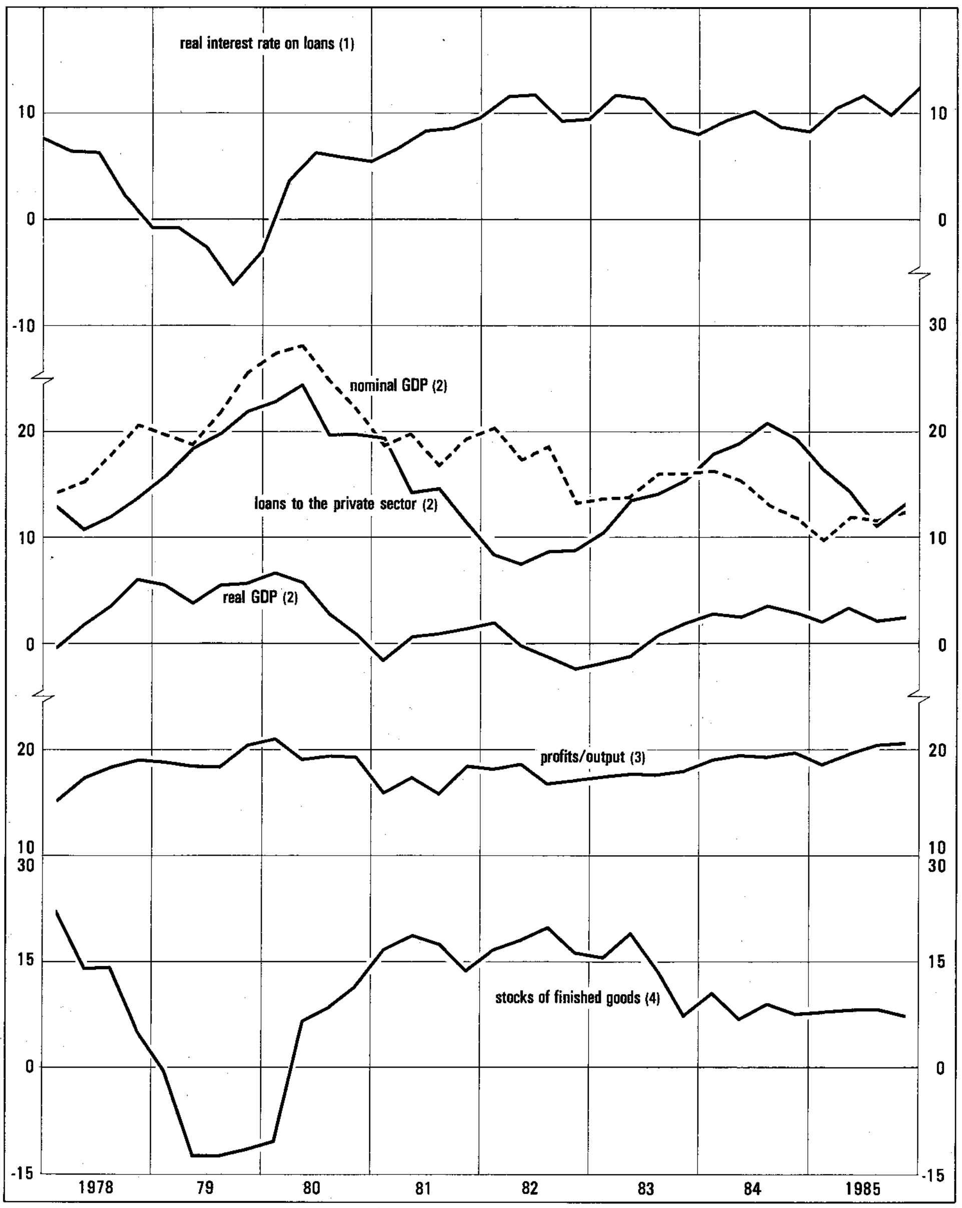
Lending

The 15.6 per cent rise in bank loans in 1985 was the result of an increase of 21.8 per cent in the lira component and a decrease of 22.3 per cent in the foreign currency component. When the data are adjusted for the surge at the end of the year (estimated at about 10 trillion lire), the increase in lira loans reduces to 16.4 per cent and bank lending declined over the year in relation to GDP.

Customers' borrowing behaviour varied considerably among the various categories. Figures supplied by the Bank of Italy's Central Risks Office indicate a 4.6 per cent fall in large companies' demand for credit, as against an increase of 21.6 per cent in that of small and medium-sized firms. Consequently the major banks, which traditionally finance large corporations, lost a further share of the market to the small and medium-sized banks and savings banks.

Figure 10

BANK LENDING AND ECONOMIC ACTIVITY



(1) The average interest rate on lira loans deflated using the rate of increase in industrial wholesale prices. — (2) Rates of increase over the twelve months ending in the relevant quarter. For loans the values are calculated using average quarterly data net of funding operations and exchange rate adjustments. — (3) The ratio of gross operating profits in industry excluding construction to the sector's output net of intersectoral transactions; seasonally adjusted data at current prices. — (4) Stocks of finished good in industry (deviation from normal); calculated on ISCO-Mondo Economico business opinion survey monthly data.

The year can be divided into two parts. The fall in demand for credit, which was especially pronounced in the early months, persisted until the beginning of the autumn. Furthermore, during the summer months the monetary authorities invited banks to respect the limit on their net foreign positions more strictly, which curbed the supply of foreign currency loans. Then, in the second half of November, lending in lire began to accelerate and was especially strong in December as a result of the deterioration in exchange rate expectations and because the parallel increase in money market rates made it profitable for customers able to borrow from banks at less than the prime rate to do so and invest the proceeds in securities. In the last two months of the year lira loans and total lending expanded by respectively 46.3 and 29.3 per cent on a seasonally adjusted annual basis.

Securities

Banks' securities portfolios expanded by about 17.3 trillion lire (9.3 per cent), as against 11.9 trillion in 1984. About 9.5 trillion of this amount was accounted for by securities issued in settlement of tax credits and to fund public bodies' debts, operations that were not undertaken in 1984.

Banks' holdings of Treasury bills fell by 35.1 per cent over the year, compared with a decline of 7.7 per cent in 1984 (Table 30). Their ratio to deposits also fell, from 10.1 to 6.0 per cent, and the average life to maturity shortened, with the proportion falling due within one month rising from 24.4 to 42.8 per cent between end-1984 and end-1985.

This substantial reduction in Treasury bills was matched by a 31.1 per cent increase in floating rate Treasury credit certificates, which rose from 15.4 to 18.4 per cent of deposits. The replacement of Treasury bills with credit certificates responded to expectations of lower interest rates and the improvement in the liquidity of credit certificates as a result of the development of a broader secondary market. However, with their holdings of Treasury bills at a low level and faced with a larger than usual decline in fund-raising, in the first quarter of 1986 banks disposed of a substantial volume of credit certificates (about 6.8 trillion lire).

As in 1984, the stock of special credit institution bonds recorded hardly any growth (1.8 per cent). The easing of the securities investment requirement in 1984 and the early part of 1985 led to a 7.4 per cent fall in banks' holdings of these securities, which consequently declined further in relation to deposits, from 13.5 to 11.3 per cent. The share of short-term and floating rate securities in banks' investment portfolios fell from 56.3 to 54.4 per cent, with a reversal of the trend that had been recorded since 1978.

Deposits

Bank deposits expanded by 10.1 per cent, as against 11.6 per cent in 1984 (Table 30). Net of certificates of deposit, the increase was 8.9 per cent.

Over the first four months of the year the annualized rate of increase was 16.7 per cent. From May onwards, in conjunction with a widening of the differential between the yields on government securities and deposits, there was a sharp slowdown. This became even more pronounced in December and the early months of this year, primarily owing to the increasing popularity of investment funds and portfolio management services. In the period from the end of November 1985 to April of this year bank deposits expanded at an annualized rate of 3.9 per cent.

The liquidity strains that developed between December 1985 and March 1986 led to a fall in interbank deposits of nearly 10 trillion lire, compared with a rise of about 1 trillion in the year-ago period. At the same time the differential between the interbank rate and the yield on Treasury bills widened from 1.5 to 4.3 points (Table a21).

Bank disintermediation proceeded in 1985 and accelerated sharply in the early months of this year. However, banks have been active in the development of new financial instruments, both by establishing trust and investment fund management companies and by supplying portfolio management services directly to the public.

The substantial decline in the banks' share of intermediation business over the last five years has been coupled with an increase in their importance in the payments system. Between 1980 and 1985 the ratio of currency to GDP decreased from 6.4 to 5.8 per cent, while the number of current accounts increased by 29.5 per cent.

Even though the banking payments system is still almost entirely based on traditional procedures, 1985 nonetheless saw a further expansion in the network of automated teller machines.

Interest rates

The average rate on lira loans fell over the year from 18.9 to 16.6 per cent, and that on deposits from 12.9 to 11.3 per cent. The reductions in the minimum lending and maximum deposit rates were even larger, amounting to about two and a half points (Table a21).

Lending rates came down most in the first and fourth quarters. In the latter, banks lowered their rates considerably, despite growing demand for credit and tight liquidity. Between September and December the rate on lira loans decreased by nearly one point, while their ratio to deposits — a summary indicator of the pressure of demand on banks' resources — jumped from 45.9 to 47.9 per cent on a seasonally adjusted basis. In the first quarter the measures taken by the authorities pushed the average lending rate up by nearly one point for a short time, while the decline in deposit rates came to a halt. In April bank rates started to come down again in response to reductions in the yields on government securities, cuts in the official discount rate and the easing of the ceiling on bank lending — over the month the ABI prime rate fell by three quarters of a point.

The size of the fall in lending rates over the year reflects the lag with which they follow changes in the yields on government securities.

The reduction in deposit rates in 1985 was the largest for ten years, and since 1984 these rates have been following the decline in those on Treasury bills and bank loans more closely than previously. The larger proportion of floating rate securities in banks' portfolios has made the average yield on assets more responsive to changes in money market rates, and the greater flexibility this provides has led banks to make larger adjustments in the unit cost of deposits than in similar periods in the past.

In structural terms the stickiness of bank interest rates can be attributed to two factors: first, adjustment costs make a few large changes cheaper than a large number of small ones; and second, uncertainty about the reaction of competitors in an oligopolistic market discourages frequent price changes. There is therefore scope for making bank rates more flexible in the future by intensifying competition and improving the efficiency of markets. Since the removal of the ceiling on bank lending in June 1983 there have been signs that competition is playing a greater role in decisions to vary lending rates.

Profit and loss accounts

Banks' net interest income declined from 3.36 to 3.24 per cent of their total resources (Table 31). This result was primarily due to the reduction of nearly one point (from 10.4 to 9.5 per cent) in the differential between the average yield on lira loans and the unit cost of deposits, the effect of which was reinforced by a small decrease in lending's share of business volume.

The other forms of bank income were largely unchanged in relation to total resources so that the reduction in net interest income was almost entirely reflected in gross income, which declined from 4.64 to 4.53 per cent of total resources. Only the increase in income from securities trading appears significant, though smaller than in previous years. Moreover, the increase was partly due to special factors such as some large banks' disposal of all or part of their interests in other credit institutions.

The incidence of operating expenses fell from 3.15 to 3.03 per cent, with the staff component falling from 2.27 to 2.18 per cent, primarily as a result of the slowdown in the expansion of employment. This had started in 1982, but was much more pronounced in 1985, when the increase amounted to only 0.4 per cent. The slowdown also contributed to the first rise recorded in the eighties in total resources per employee expressed in real terms.

The fall in operating expenses offset that in net interest income, so that net income remained virtually unchanged. Banks reduced the incidence of their allocations to provisions from 0.71 to 0.67 per cent. Specifically, allocations to loan loss provisions fell from 0.39 to 0.32 per cent and banks also made larger withdrawals from these provisions than in the past. These developments reflected not only the slower increase in major banks' bad debts but also the recovery of default interest on loans to public bodies subsequently funded with securities, for which loss provisions had previously been made.

Profit before tax rose from 0.80 to 0.90 per cent of total resources and net profit also rose, though to a lesser extent (from 0.36 to 0.43 per cent) owing to the larger incidence of tax. The special factors described above — disposals of interests in other credit institutions and the recovery of default interest — accounted for more than half the increase in bank profits. The increase in profits is consistent with banks' need to remunerate their expanding capital base. In 1985 own funds again increased in relation to deposits, rising to 8.4 per cent, while the ratio of net profit to own funds rose from 8.1 to 9.2 per cent.

THE SPECIAL CREDIT INSTITUTIONS AND LEASING AND FACTORING COMPANIES

The special credit institutions

The demand for special credit was weak, despite the continuation of the expansionary phase of the investment cycle. Domestic lending by the special credit institutions increased by 8.5 per cent, compared with 13.6 per cent in 1984 (Table 32). After relatively sustained growth in the first quarter, there was a marked deceleration in the second and third, owing partly to the particularly large volume of advance repayments; signs of a recovery appeared in the last two months of the year and developed into an acceleration in the early part of 1986.

Table 32

DOMESTIC LENDING BY THE SPECIAL CREDIT INSTITUTIONS

(percentage changes)

	1981	1982	1983	1984	1985
Industrial	21.3	19.9	9.6	12.0	9.3
short-term	*58.1*	*32.2*	*−2.7*	*34.6*	*33.4*
Public works	10.6	18.9	32.2	22.9	3.2
Real estate	17.7	14.5	14.3	(2) 13.2	9.6
Agriculture	23.4	14.4	(1) 13.2	(2) 12.6	8.2
Total	**19.3**	**17.9**	(1) **13.4**	(2) **13.6**	**8.5**

(1) Excluding the data for Banco di Sardegna, which began operations as an agricultural credit section on 1 January 1983, the growth rate of lending by the agricultural credit institutions was 19.5 per cent and that by the special credit institutions as a whole was 13.9 per cent. — (2) Taking into account the formation of the agricultural credit section of Istituto Bancario San Paolo di Torino, which began operations in October 1984 and to which the agricultural improvement loans previously granted by its real estate credit section have been attributed, the rate of growth of lending by the real estate credit institutions was 10.9 per cent, that by the agricultural credit institutions 25.0 per cent and that by the special credit institutions as a whole 14.0 per cent.

The growth in lending to the private sector slowed down from 12.7 to 9.7 per cent (Table 33), but the expansion in loans to the public sector decelerated much more sharply, from 20.0 per cent in 1984 to 3.4 per cent. In particular, local authorities reduced their demand for credit, which had been very strong in previous years thanks to central government bearing the entire debt servicing charge; the new regulations governing unused portions of loans deposited with the institutions by municipalities and provinces also had a negative bearing on their demand for credit. This state of affairs was reflected in the stagnation in lending by the public works credit sections after three years of rapid growth (Table 32).

Table 33

DOMESTIC LENDING BY THE SPECIAL CREDIT INSTITUTIONS BY CLASS OF BORROWER

	PUBLIC SECTOR			PRIVATE SECTOR					TOTAL
		Local authorities	Autonomous government agencies	Total	Financial and insurance companies	Non-financial firms		Households	
							state controlled		
				changes in billions of lire					
1984 - Subsidized	223	178	26	4,450	−6	3,667	291	789	4.673
Unsubsid. .	3,558	2,937	417	7,135	870	5,440	1,268	825	10,693
Total . . .	**3,781**	**3,115**	**443**	**11,585**	**864**	**9,107**	**1,559**	**1,614**	**15,366**
1985 - Subsidized	195	220	−7	3,993	−2	3,243	−298	752	4,188
Unsubsid. .	576	1,130	−723	5,924	1,425	3,434	1,060	1,065	6,500
Total . . .	**771**	**1,350**	**−730**	**9,917**	**1,423**	**6,677**	**762**	**1,817**	**10,688**
				percentage changes					
1984 - **Total**	**20.0**	**23.7**	**18.0**	**12.7**	**26.6**	**13.1**	**10.1**	**11.1**	**(1) 13.6**
1985 - **Total**	**3.4**	**8.3**	**−25.1**	**9.7**	**34.6**	**9.0**	**4.5**	**11.2**	**8.5**

(1) The percentage change in total lending has been adjusted as in Table 32.

Lending by industrial credit institutions should have benefited from the growth in investment in machinery and equipment, but here too there was a slowdown, albeit smaller than in other types of lending, from 12.0 to 9.3 per cent. The high level of corporate self-financing and the greater volume of direct recourse to the financial markets by large industrial groups depressed credit demand, especially to the larger institutions, which also had to contend with a contraction in export credit. These factors did not have an appreciable effect on the activity of the other institutions, however, which were able to take advantage of the expansion in subsidized investment credit.

The rationalization of financial management in large firms also had qualitative effects on the institutions' activities. The interposing of financial companies, including leasing and factoring companies, between the special credit institutions and the final users of credit further weakened the link between industrial credit and investment, thereby narrowing the differences between the financial products offered by the special credit institutions and those of the banks, especially as regards maturities.

The increasing overlap between bank credit and loans from the special credit institutions has intensified competition and contributed to a narrowing of interest spreads on new operations. With bank interest rates falling rapidly, the special credit institutions held the differential between the cost of short-term unsubsidized credit and minimum bank rates constant over the year, despite the greater stickiness of CD interest rates, which declined by less owing to the competition from government securities and investment funds.

Operations at 18 months or less continued to expand rapidly despite the absence of limits on the expansion in bank lending, rising at a rate of 33.4 per cent compared with 34.6 per cent in 1984.

Combined with high and variable rates of inflation, the changes in investment, the financial markets and the institutional and legislative framework over the last decade have left their mark on the operations of the industrial credit institutions. There has been a decline in the demand for large long-term fixed rate loans, which had been strong until the early seventies, partly owing to the easy access to interest subsidies. Regional medium-term credit institutions and some of the special credit institutions for southern Italy, which in the past had been active mainly in the subsidized field, have greatly expanded their lending at market rates, thanks to brisk demand for medium-term loans at fixed or variable interest rates from medium-sized firms. The larger institutions have encountered greater difficulties, which they have tackled by engaging in foreign currency operations covered by government exchange guarantees, by greatly expanding their short-term activities (partly to avoid the duty on medium and long-term loans), by increasing their investments in securities and by developing activities that are not strictly associated with lending. These have primarily involved issuing bonds convertible into the shares of other companies and, more recently, providing services such as the management and placement of share issues. Activities of this kind are carried out both directly and via subsidiaries.

In 1985 there were signs of increasing specialization of operations within groups and careful coordination of their financial resources. The special credit institutions that are parent companies of financial groups offset the slow expansion in their more traditional activities by increasing their shareholdings in related companies, thereby also altering the structure of their profit and loss accounts; thanks to the participations acquired in recent years, the income from subsidiary companies is beginning to make a significant contribution to total profits.

Lending

The special credit institutions' domestic lending increased by 10,688 billion lire, compared with 15,366 billion in 1984 (Table 33). The private sector took up 9,917 billion lire (11,585 billion in 1984), but the flow of credit to the public sector amounted to only 771 billion lire, as against 3,781 billion in 1984. In particular, net lending to the autonomous government agencies decreased owing to the repayment of a 700 billion lire loan by the State Railways, which increased its direct recourse to the domestic and international capital markets.

The institutions were affected by competition from the Deposits and Loans Fund, which greatly increased its credit to local authorities and granted a loan of 1 trillion lire to the telecommunications company SIP under the 1985 Finance Law.

Credit to industry and the services sector. — Lending to non-financial companies slowed down, especially to industrial firms, with the rate of expansion in loans to industry falling from 10.5 per cent in 1984 to 7.9 per cent last year. There was a particularly large reduction in borrowing by large enterprises.

The growth in lending to industry at market interest rates was extremely small, 2.6 per cent as against 10.9 per cent in 1984. On the other hand, there was a rapid expansion in unsubsidized credit to the services sector, especially the wholesale and retail trades and financial activities; this represented a substantial additional, albeit indirect flow of special credit to the industrial sector. Apart from loans to companies operating in the financial services sector, such as leasing and factoring companies, a large volume of credit was granted to financial companies managing the financial resources of industrial groups.

Subsidized lending to industry recovered strongly, rising by 2,342 billion lire, or 17.5 per cent net of export credit.

Credit for housing. — The continuing difficulties afflicting the residential construction sector were again reflected in relatively slack demand for special credit to finance housebuilding. Disbursements came to 4,219 billion lire, only slightly above the 1984 figure (4,038 billion); the ratio of disbursements to housing investment remained more or less stable, falling from 13.4 to 13 per cent, despite a reduction in credit incentives. Subsidized disbursements declined slightly, from 1,089 billion lire to 1,010 billion, thus breaking a five-year trend.

By contrast, disbursements at market rates increased from 2,949 billion lire in 1984 to 3,209 billion last year as a result of the decline in long-term interest rates, which nevertheless still constitute an obstacle to borrowing by households.

Lending for housebuilding was affected by competition from the banks, which are also offering mortgage loans, generally at medium term; the difference between the term of bank mortgages and those granted by special credit institutions has narrowed, since the latter are now repayable over a period of between 10 and 15 years rather than 20 years as previously, so that bank loans to finance house purchases may prove competitive owing to the more rapid lending procedures and the greater market penetration provided by the banks' extensive branch network.

The slowdown in inflation opens up the prospect of a revival in the long-term financing of housebuilding; the fall in nominal long-term interest rates will ease the problems of access to credit, partly because loan maturities can be lengthened to allow borrowers to spread the cost of house purchase over a sufficiently long period. On the other hand, it can also cause serious difficulties for borrowers and hence for lending institutions. Those who took out fixed rate loans when interest rates were higher find that their instalment payments are much larger than expected in real terms. As a result, applications for early repayment increased by 45 per cent to more than 1 trillion lire. Moreover, the real estate credit institutions' bad debts increased by 39 per cent, owing partly to developers' difficulties in selling houses.

Export credit. — Export credit granted by the special credit institutions declined further from the already low levels of recent years; the volume outstanding actually fell by 1,364 billion lire.

This development, which was due to the slower growth in exports to certain regions, reflects the difficulties encountered in the two areas of export credit in which the special credit institutions conduct most of their business: lending in lire and foreign currency buyer credits. Lending in lire was adversely affected by the ceiling of 5 million lire on individual transactions eligible for interest subsidies and by the reduction in the institutions' all-inclusive commission from 1.75 to 1.05 per cent in August.

The special credit institutions' foreign currency lending was strongly affected by the narrow subsidy margins permitted under international agreements (the Consensus) and by the smaller number of intergovernmental trade agreements, which commonly involve financing by the institutions.

Agricultural credit. — The expansion in agricultural credit was held back by the poor performance of the farm sector for the second year in succession. Working credit increased by 6.8 per cent, a much slower rate of growth than in 1984 (15.4 per cent) but faster than the rise in gross marketable production (3.9 per cent at current prices). The uptake of short-term agricultural credit per unit of output therefore increased further owing to a continued squeeze on farm incomes. The trend was encouraged by the availability of interest subsidies from funds allocated in the 1985 Finance Law, which enabled more than 7,000 billion lire to be disbursed in subsidized loans, compared with 6,493 billion in 1984 (Table 34). The rediscounting of agricultural bills with the Bank of Italy made it possible to grant a further 1,100 billion lire at rates below those of the market, almost as much as was granted in this way in 1984.

Improvement credit showed a less pronounced slowdown, rising by 10.8 per cent, as against 12.8 per cent in 1984. The ratio of disbursements to investment in the sector remained virtually unchanged. The main expansion was in operations at market rates financed by borrowing abroad under government exchange guarantees.

The bad debts of the agricultural credit institutions operating primarily in the improvement credit field increased substantially (by 32 per cent), but they continue to equal only about 2.4 per cent of total lending.

The national agricultural plan and the implementation of the EEC regulation on improving farm efficiency, which lay the foundations for a more structured policy of intervention in the farming sector, may lead to a larger expansion in long-term agricultural credit.

Fund-raising and the management of securities portfolios

The changes in methods of raising funds, which had been occurring primarily in the large industrial credit institutions in past years, spread to the rest of the special credit sector in 1985. Certificates of deposit and borrowing abroad are now beginning to decline among the institutions that first used these methods of fund-raising, but their share of the total borrowed funds of agricultural and real estate credit institutions has increased significantly. This change, which has enabled the banks to reduce their contribution to the funds of the special credit institutions, has been facilitated by the easing of market regulation; the banks' securities investment requirement has been reduced to 4 per cent of the increase in deposits and the maximum interest rate on special credit institution bonds has become less of a constraint in view of the fall in interest rates.

Table 34

LENDING BY THE AGRICULTURAL CREDIT SYSTEM

(billions of lire)

	Agricultural special credit institutions (1)			Other authorized institutions			General total		
	Subs.	Unsub-sidized	Total	Subs.	Unsub-sidized	Total	Subs.	Unsub-sidized	Total
	Disbursements in 1984								
Working credit	**2,690**	**1,093**	**3,783**	**3,803**	**2,772**	**6,575**	**6,493**	**3,865**	**10,358**
Improvement credit	**613**	**210**	**823**	**173**	**44**	**217**	**786**	**254**	**1,040**
	Disbursements in 1985								
Working credit	**2,872**	**1,396**	**4,268**	**4,197**	**2,722**	**6,919**	**7,069**	**4,118**	**11,187**
Current expenditure	2,006	893	2,899	3,103	1,889	4,992	5,109	2,782	7,891
Purchases of livestock	50	98	148	91	107	198	141	205	346
Purchases of machinery	131	121	252	247	194	441	378	315	693
Advances against agricultural products	40	5	45	148	12	160	188	17	205
Loans to agricultural agencies and cooperatives	645	279	924	608	520	1,128	1,253	799	2,052
Improvement credit	**543**	**403**	**946**	**128**	**36**	**164**	**671**	**439**	**1,110**
Rural construction	185	115	300	18	14	32	203	129	332
New plantings	18	8	26	6	—	6	24	8	32
Irrigation	17	6	23	3	—	3	20	6	26
Soil preparation	6	5	11	1	1	2	7	6	13
Expansion of holdings	76	26	102	13	1	14	89	27	116
Other improvements	241	243	484	87	20	107	328	263	591
	Outstanding credit at end-1985								
Working credit	**3,427**	**1,170**	**4,597**	**4,354**	**1,781**	**6,135**	**7,781**	**2,951**	**10,732**
Improvement credit	**5,034**	**1,423**	**6,457**	**1,000**	**160**	**1,160**	**6,034**	**1,583**	**7,617**

(1) Since 1983 Banco di Sardegna has operated through an agricultural credit section; since October 1984 Istituto Bancario San Paolo di Torino has operated through an agricultural credit section, to which the agricultural improvement credits previously granted by its real estate credit section have been attributed.

Bond issues increased by 6.1 per cent to 5,468 billion lire; almost half of the expansion was in fixed interest securities, which benefited from a hardening of expectations of a further decline in yields. It should also be remembered that this category includes the bulk of convertible bonds, gross issues of which came to 660 billion lire, compared with 58 billion in 1984.

The growth in certificates of deposit was less than half that recorded in 1984 (2,069 billion lire as against 4,216 billion), in line with the growth in lending by special credit institutions established in the form of public limited companies, which rely chiefly on funds raised in this way. Half the net increase for the year was attributable to agricultural credit institutions, which simultaneously reduced their short-term bank debt.

Fund-raising in foreign currencies continued to increase, although at a slower pace than in 1984 (12.3 per cent against 27.8 per cent). Net of repayments, loans received from international financial institutions (principally the EIB) came to about 2,500 billion lire, more or less the same as in 1984.

Despite disinvestment by public works credit sections and the fiscal measures of November 1984, the proportion of the institutions' portfolios consisting of government securities continued to increase, though at a greatly reduced rate (9.4 per cent, compared with 31.7 per cent in 1984); their liquid resources, which are held predominantly in government securities, remained at the high levels recorded in recent years in relation to lending commitments.

Shareholdings and participations rose from 2,409 billion lire to 2,744 billion, partly as a result of an increase in business in convertible bonds and warrants but also owing to an intensification of the group policies pursued by some institutions; participations in subsidiary companies accounted for around 50 per cent of the increase.

Profit and loss accounts

The fall in interest rates on new operations, which has been under way since 1983, was reflected in a reduction in borrowing and lending rates in relation to total resources; lending rates fell from 14.80 to 14.22 per cent and borrowing rates from 11.66 to 11.18 per cent (Table 35). The reduction was aided by the higher proportion of short-dated and variable rate operations in the institutions' balance sheets; long-term operations had the opposite effect, however, rates on new business remaining higher than those on maturing transactions.

Table 35

PROFIT AND LOSS ACCOUNTS OF THE SPECIAL CREDIT INSTITUTIONS: FORMATION OF PROFIT

	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985 (1)
	As a percentage of total resources									
Interest income	8.83	9.51	10.43	10.97	11.76	12.91	14.41	14.72	14.80	14.22
Interest expenses	7.10	7.62	8.18	8.57	9.03	10.00	11.40	11.63	11.66	11.18
Net interest income	**1.73**	**1.89**	**2.25**	**2.40**	**2.73**	**2.91**	**3.01**	**3.09**	**3.14**	**3.04**
Non-interest income	0.04	0.03	−0.01	−0.02	0.03	0.01	−0.05	−0.05	0.02	0.01
Gross income	**1.77**	**1.92**	**2.24**	**2.38**	**2.76**	**2.92**	**2.96**	**3.04**	**3.16**	**3.05**
Operating expenses	0.39	0.42	0.44	0.49	0.61	0.66	0.73	0.77	0.82	0.84
staff costs	*0.31*	*0.33*	*0.34*	*0.37*	*0.44*	*0.44*	*0.44*	*0.48*	*0.50*	*0.52*
Net income	**1.38**	**1.50**	**1.80**	**1.89**	**2.15**	**2.26**	**2.23**	**2.27**	**2.34**	**2.21**
Depreciation & allocations to provisions	0.95	1.01	1.42	1.49	1.82	1.71	1.36	1.41	1.46	1.28
Extraordinary income and expenditure	0.05	0.03	0.24	0.05	0.09	0.16	0.13	0.24	0.17	0.16
Profit before tax	**0.48**	**0.52**	**0.62**	**0.45**	**0.42**	**0.71**	**1.00**	**1.10**	**1.05**	**1.09**
Tax	0.26	0.29	0.41	0.24	0.24	0.32	0.42	0.39	0.42	0.41
Net profit	**0.22**	**0.23**	**0.21**	**0.21**	**0.18**	**0.39**	**0.58**	**0.71**	**0.63**	**0.68**
	Other data									
Total resources (billions of lire)	66,260	72,138	79,501	84,775	91,890	104,073	124,147	141,254	158,815	176,805
Number of employees	8,270	8,664	8,926	9,990	10,318	10,654	11,130	11,840	12,045	12,045
Total resources per employee *(millions of lire)*	801	833	891	849	891	977	1,115	1,193	1,319	1,460
Staff costs per employee *(millions of lire)*	24.67	27.35	29.91	31.23	39.64	43.18	49.06	56.93	66.17	75.40
	Percentage rates of increase									
Staff costs per employee	17.7	10.9	9.4	4.4	26.9	8.9	13.6	16.0	16.2	13.9
Total resources per employee:										
in nominal terms	11.6	4.0	7.0	−4.7	4.9	9.7	14.1	7.0	10.6	10.7
at constant prices (2)	−4.3	−11.9	−4.9	−17.7	−13.4	−7.6	−1.9	−6.9	−0.1	2.0

(1) Provisional. — (2) Deflated using the cost-of-living index.

Net interest income also contracted from 3.14 to 3.04 per cent of total resources, after increasing steadily between 1976 and 1984. The gross income ratio showed a similar trend. The narrowing of margins, which reflected the squeezing of the spread on new operations at a time of falling interest rates and keen competition among intermediaries, was contained by the increase in the ratio of capital and reserves to total resources from 9.6 to 10.2 per cent.

Net income showed an even larger reduction owing to the increase in operating expenses, which was due entirely to the further rise recorded in staff expenses despite the slower increase in staff numbers.

Notwithstanding the fall in net income, profits before tax rose from 1.05 to 1.09 per cent of total resources, thanks mainly to the institutions' policies with regard to the sources and applications of funds; in particular, allocations to depreciation and provisions decreased from 1.46 per cent in 1984 to 1.28 per cent last year.

Net profits after tax increased from 0.63 to 0.68 per cent of total resources but remained broadly unchanged at 7 per cent in relation to capital and reserves.

Leasing and factoring companies

The continuing diversification of the financial system brought further rapid growth in the financing of business by intermediaries that are not themselves banks or special credit institutions but are for the most part related to such intermediaries. Overall, leasing and factoring companies provided industry with a net flow of finance in excess of 3 trillion lire (compared with about 2 trillion in 1984), greatly increasing their market share at the expense of traditional intermediaries, which nevertheless provide the funds needed for their operations.

In view of the importance leasing and factoring companies have assumed, a survey has been launched via the branches of the Bank of Italy to amplify the information gathered for the 1984 Annual Report and place it on a regular footing. The survey, which is still at the development stage, is based on returns from more than 50 leasing companies and 35 factoring companies covering approximately 80 and 90 per cent of the business in their respective markets.

Leasing companies. — The activities of leasing companies were not affected by the weakness of credit demand, since they serve primarily small and medium-sized firms, which made much less use of self-financing and direct fund-raising than large firms. Leasing companies were therefore able to seize the opportunity offered by the continued rapid growth in investment to increase their market share by aggressive marketing.

The value of leasing contracts signed by the group of companies surveyed, which can be taken as an indicator of the gross flow of finance, increased by 30 per cent to 4,609 billion lire, a more rapid rate of increase than the rise in expenditure on machinery and equipment (19 per cent). The increasing use of subsidies to reduce rental costs provided strong stimulus, with subsidized operations accounting for more than one fifth of the total.

The volume of financing implicit in leasing contracts outstanding at the end of 1985 totaled 6,193 billion lire for the group of companies surveyed, an increase of 30.8 per cent (Table 36); for the sector as a whole, the figure is put at 7,500 billion.

Table 36

LEASING (1)

(amounts outstanding in billions of lire)

	1984	1985
Finance provided (2)	4,734	6,193
Finance received from credit institutions	3,951	5,219
short-term lira loans	*1,784*	*3,029*
medium and long-term loans	*2,090*	*1,942*
foreign currency loans	*77*	*248*

(1) Data on 51 companies. — (2) The value of goods leased under outstanding contracts net of the capital repayments implicit in the rentals already received.

In the sample of companies considered, the proportion of operations relating to machinery and equipment increased in line with the trend of economic activity; there was also an expansion in property leasing, though this item continues to be small in relation to the total.

The leasing companies' borrowing from the credit system, which is by far their most important source of funds, increased in line with the growth in their financing. However, the maturity composition of their debt changed radically; short-term debt rose sharply to account for more than 60 per cent of lira borrowing from this source, which increased substantially, whereas fund-raising in foreign currency remained small; on the other hand, medium-term borrowing contracted, despite the fact that it would provide a better maturity match for the expected flow of receipts.

Factoring companies. — The activities of factoring companies also continued to expand at a very rapid rate, boosted by the favourable economic climate and the more widespread use of techniques to improve treasury management in industrial firms. In particular, companies in which industrial groups have a shareholding increased their market share, partly as a result of the establishment of two new companies related to state holding companies.

Claims assigned to the factoring companies included in the survey increased by 2,383 billion lire to stand at 7,339 billion at the end of 1985 (Table 37), a rate of increase of 48 per cent, almost the same as in the preceding year.

Table 37

FACTORING

(amounts outstanding in billions of lire)

	Companies controlled by banks		Other		Total	
	1984	1985	1984	1985	1984	1985
Claims acquired	3,196	4,580	1,760	2,759	4,956	7,339
Finance provided	2,009	2,865	1,573	2,392	3,582	5,257
Finance received from credit institutions	1,720	2,476	1,342	2,026	3,062	4,502
short-term lira loans	*1,394*	*2,205*	*997*	*1,631*	*2,391*	*3,836*
medium and long-term lira loans	*262*	*168*	*345*	*342*	*607*	*510*
foreign currency loans	*64*	*103*	—	*53*	*64*	*156*
Number of companies covered by the survey	20	21	12	14	32	35

Although operations without recourse increased slightly faster than those with recourse, the services offered by these companies continue to be predominantly financial, in view of the high ratio of lending to assigned claims. Moreover, by raising funds from the banking system at rates close to prime rate and providing services for small and medium-sized businesses, these companies can operate profitably without needing to engage in other typical factoring activities, such as the provision of insurance and trading services. The proportion of credits without recourse rose from 17 per cent at the end of 1984 to 20 per cent last year but remained well below the average for factoring companies in other countries.

Lending by factoring companies rose by about 1,675 billion lire to 5,257 billion. The ratio of lending to assigned claims (72 per cent on average) appears to vary more according to the type of company than to whether operations are with or without recourse; it appears to be higher among factoring companies whose shareholders are predominantly industrial firms (87 per cent).

The companies continued to adjust the composition of their principal balance sheet liabilities with the aim of improving profitability. Short-term liabilities to banks increased significantly to 3,836 billion lire, compared with 2,391 billion at the end of 1984; there was also a rise, though on a smaller scale, in foreign currency liabilities (156 billion lire, as against 64 billion in 1984), whereas medium and long-term liabilities decreased from 607 to 510 billion lire. Total borrowing from the credit system (4,502 billion lire) covered the bulk of the factoring companies' assets; at the end of the year their capital and reserves amounted to about 528 billion, compared with 398 billion in 1984.

INSTITUTIONAL INVESTORS

In 1985 fund-raising by Italian institutional investors (investment fund management companies and insurance companies) and investment management services increased sharply to about 35 trillion lire. At once cause and effect of soaring share prices, the expansion is the consequence of savers' desire for greater diversification of their financial assets, achieved with the assistance of specialists.

The fastest growth was recorded by the investment funds, notably the Italian funds, which recorded net fund-raising of 15.3 trillion lire and capital gains of nearly 3.4 trillion, thus increasing their portfolio assets from just 1.1 trillion lire to 19.8 trillion. The portfolio of foreign investment funds increased from 4.2 trillion lire at end-1984 to 7.5 trillion lire at end-1985, with capital gains accounting for 2.8 trillion of the increase. The assets handled by investment management services also grew substantially, from 11.2 trillion to 26.5 trillion lire. Insurance companies' actuarial reserves, net of provisions for reinsurance, increased from 23.6 trillion to 28.8 trillion lire, the sharpest increase being achieved by the life insurance sector.

The investment funds

The number of Italian investment funds rose from 11 in December 1984 to 48 in April 1986. Their net worth increased from 1,146 billion lire to 19,783 billion in 1985 and more than doubled to over 44,000 billion lire between January and April 1986. This explosive growth resulted both from accelerating net fund-raising (19.0 trillion lire in the first four months of 1986, compared with 15.3 trillion lire in the whole of 1985) and from the buoyant performance of share prices.

Despite the enormous growth of the industry and the fourfold increase in the number of funds, concentration remained very high: three management companies running seven funds held about 45 per cent of the net assets of all the funds and more than 51 per cent of their equity portfolio.

Government securities were the largest component of the funds' portfolios in 1985, although they did decline from 69 to about 60 per cent of the total (Table 38). The portion accounted for by shares rose accordingly from 16 to 27 per cent (or, in absolute terms, from 176 billion to 5,095 billion lire).

Table 38

ITALIAN INVESTMENT FUNDS

(end-of-period balance-sheet values in billions of lire)

	1984 Dec.	1985				1986 Mar.
		Mar.	June	Sept.	Dec.	
Treasury bills	31	329	1,180	1,332	578	959
Treasury credit certificates	693	2,880	4,191	6,171	9,240	14,901
Treasury certificates in ECUs	—	51	78	196	303	676
Index-linked Treasury certificates	—	—	—	4	8	1
Treasury bonds	48	251	296	421	1,141	3,816
Deposits and Loans Fund certificates	—	—	—	—	—	11
Government securities	*772*	*3,511*	*5,745*	*8,124*	*11,270*	*20,364*
Autonomous agencies	23	112	210	211	233	267
Public works consortium on behalf of the Treasury	—	—	1	2	16	15
Special credit institutions (1)	68	232	347	506	614	1,022
Firms and public enterprises	80	261	543	754	1,020	1,882
Bonds	*171*	*605*	*1,101*	*1,473*	*1,883*	*3,186*
Shares	*176*	*775*	*1,851*	*3,266*	*5,095*	*10,824*
Total lira-denominated securities	**1,119**	**4,891**	**8,697**	**12,863**	**18,248**	**34,374**
Securities denominated in foreign currency	**—**	**17**	**58**	**200**	**678**	**1,151**
Net worth	1,146	5,013	9,015	13,408	19,783	36,980

(1) Including certificates of deposit.

The expansion in holdings of shares eased somewhat in early 1986, however, when the funds responded cautiously to the soaring stock market and put an increasing proportion of their net new resources into government securities. Nevertheless, the enormous rise in share prices meant that the portion of portfolio assets accounted for by shares continued to increase.

In any event, the investment funds had a decisive influence on the performance of the stock market over the first four months of 1986. While diminishing relative to net fund-raising, in absolute value the funds' net share purchases increased nearly fivefold over the same period in 1985, from 750 billion lire to about 3.4 trillion. At end-April 1986 their shares holdings amounted to 12.9 trillion lire, about 30 per cent of their overall securities portfolios.

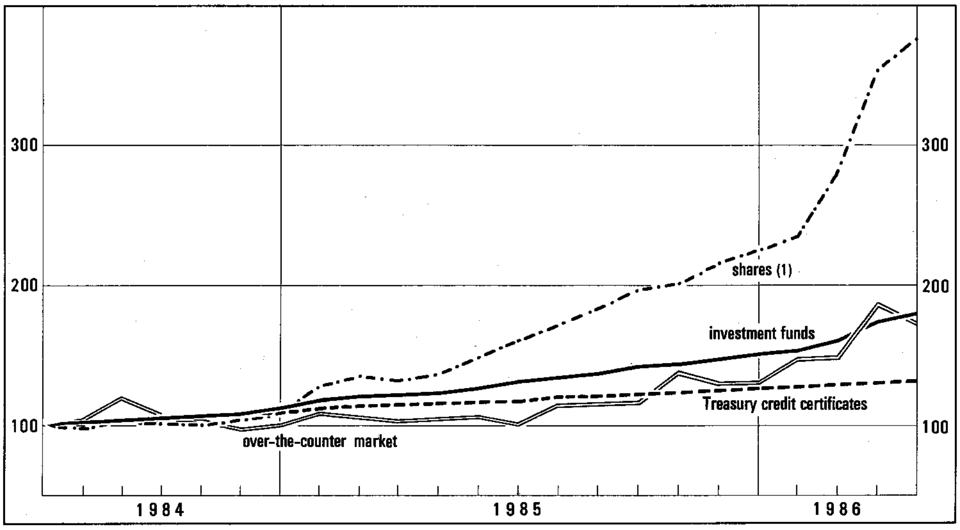
Holdings of foreign securities, which had been totally absent at end-1984, were worth about 680 billion lire by end-1985, i.e. 3.6 per cent of portfolio assets. The preferred markets were Germany and the United States, with investment being mainly in shares; at the end of 1985 these two markets accounted for about half of the Italian funds' total foreign assets.

In addition to the favourable tax treatment they enjoy, a prime factor in the success of the funds is the high yields they have achieved over this period. The Bank of Italy's capital value index for the funds as a whole registered growth of 35 per cent in 1985 and 19.7 per cent over the first four months of 1986 (Figure 11).

Figure 11

SECURITIES INVESTMENTS: CAPITAL VALUE INDICES

(base 100 on 2 July 1984)



(1) Milan Stock Exchange index.

The performances of individual funds as measured by this index were strongly differentiated. In the case of funds that had been operating for at least a year at the end of April, the gross yields for the twelve months ending on that date ranged from 51 per cent to 96 per cent for share-based and mixed funds, and from 14 to 29 per cent for bond-based funds.

The net worth of the foreign investment funds operating in Italy also expanded sharply in the course of 1985, from 4.2 trillion to 7.5 trillion lire (Table 39). Net fund-raising was about the same as in 1984, but there was a substantial increase in the value of their assets, especially in the second half of the year. In December their securities portfolios accounted for about 95 per cent of their total net worth.

Table 39

FOREIGN INVESTMENT FUNDS

(end-of-period balance-sheet items in billions of lire)

	1984 Dec.	1985 Mar.	1985 June	1985 Sept.	1985 Dec.
Italian securities	3,372	3,993	4,708	5,546	6,203
shares	*1,685*	*2,065*	*2,703*	*3,390*	*3,756*
Foreign securities	585	732	766	747	916
shares	*482*	*573*	*641*	*586*	*748*
Total securities portfolio	3,957	4,725	5,474	6,293	7,119
Net worth	4,233	4,947	5,691	6,571	7,469

The value of the foreign funds' Italian portfolio nearly doubled on the year (from 3,372 billion to 6,203 billion lire), mainly as a result of an increase in their holdings of shares (from 1,685 billion to 3,756 billion lire). The value of foreign securities also increased substantially, notably in the first and last quarters, from 585 billion to 916 billion lire. Proportionally, however, holdings of foreign securities declined from 14.8 to 12.9 per cent of the total portfolio, although for some funds the proportion was more than 30 per cent.

Investment management services

The continuing diversification of the Italian financial system last year affected not only the investment funds but also the related sphere of investment management.

The data available to the Bank of Italy indicate that savers entrusted some 14 trillion lire to professional investment management services last year, so that including capital gains the total value of the portfolios handled rose to about 26.5 trillion lire at the end of the year, compared with 11.2 trillion lire at the end of 1984. The number of portfolios is about 168,000, which gives an average account size of almost 160 million lire, indicating the relative affluence of these investors. By way of comparison, the average holding of investment fund units was 27 million lire at the same date.

At the end of 1985 these services were provided mainly by credit institutions, either directly (78 per cent) or indirectly via subsidiaries or affiliates (14 per cent); almost all portfolios were managed on a discretionary basis, with the investor just indicating the general investment criteria.

The trends observed in 1985 carried over into the first quarter of 1986. The value of managed portfolios increased by 21.6 per cent, reflecting substantial fund-raising (estimated at 3.9 trillion lire) and large capital gains. The funds raised were used primarily for investment in government securities (2.9 trillion lire), while purchases of shares were relatively modest (300 billion lire).

The insurance companies

At the end of December, authorized insurance companies numbered 212, of which 51 were representatives of foreign companies. Their total assets increased by 21 per cent over the year, from 27.7 trillion to 33.5 trillion lire (Table 40). Their securities portfolios rose

Table 40

ASSETS OF THE INSURANCE COMPANIES

(balance-sheet items in billions of lire)

	Deposits and cash	Securities (1)	Mortgages & annuities	Real estate	Total
			life sector		
1984	234	5,830	1,375	3,765	11,204
1985 (2)	334	7,857	1,400	4,137	13,728
			casualty sector		
1984	1,629	10,128	141	4,606	16,504
1985 (2)	1,780	12,885	174	4,917	19,756
			total		
1984	1,863	15,958	1,516	8,371	27,708
1985 (2)	2,114	20,742	1,574	9,054	33,484

(1) In lire and foreign currency, including participations. — (2) Partly estimated.

rapidly in value (by 30 per cent), while their holdings of real estate and liquid assets increased more slowly (by 8 and 13 per cent respectively). The trend of the last five years therefore continued; over this period the real estate component has declined from 36 to 27 per cent of total assets and liquid assets from 11 to 6 per cent, while securities investment has risen from 45 to 62 per cent.

The life insurance companies' securities portfolio rose in value by 35 per cent to 7.9 trillion lire at the end of 1985 (Table 41), the bulk of the increase being accounted for by investment in Treasury credit certificates, holdings of which rose from 1.9 trillion to 3.2 trillion lire. Holdings of special credit institution bonds expanded from 1.1 trillion to 1.3 trillion lire in value, but declined from 19 to 17 per cent of total portfolio assets.

Table 41

INSURANCE COMPANIES' PORTFOLIOS OF SECURITIES

(balance-sheet items in billions of lire)

	Public sector			Special credit institutions	Firms and public enterprises	Certificates of deposit	Shares (1)	Securities in foreign currency	Total
	Treasury bills	Treasury credit certificates	Other						
				life sector					
1984	—	1,864	619	1,114	779	28	832	574	5,830
1985 (2)	—	3,200	805	1,316	934	11	953	638	7,857
				casualty sector					
1984	198	1,617	721	3,707	678	54	1,732	1,421	10,128
1985 (2)	200	2,453	917	4,466	885	31	2,362	1,571	12,885
				total					
1984	198	3,481	1,340	4,821	1,477	82	2,564	1,995	15,958
1985 (2)	200	5,653	1,722	5,782	1,819	42	3,315	2,209	20,742

(1) Including equity participations. — (2) Partly estimated.

The casualty insurance companies' securities portfolio increased in value by 27 per cent in the course of the year to 12,885 billion lire. The rise was due mainly to larger holdings of Treasury credit certificates (2.5 trillion as against 1.6 trillion lire), special credit institution bonds (from 3.7 trillion to 4.5 trillion lire), and shares (from 1.7 trillion to 2.4 trillion lire). By contrast, there was a relatively modest increase in assets denominated in foreign currencies, which accounted for 12 per cent of their portfolio at the end of the year.

THE SECURITIES MARKET

The securities market recorded further growth in 1985. This was fueled by shares as well as by bonds and government securities, which amounted to 637 trillion lire at the end of the year (compared with 521 trillion at end-1984). The market capitalization of listed shares doubled over the year to 100 trillion lire, while turnover on the Milan stock exchange rose from 7.1 to 26.3 trillion as a result of the doubling of both prices and volume. The growth in the share market was stimulated by the improvement in corporate profitability and the activity of institutional investors (in particular investment funds). Finally, the authorities responsible for overseeing the market enhanced its transparency and stability through measures to improve the quality and availability of information on company accounts and strengthen investor protection.

Bonds and government securities

Gross issues of bonds and government securities amounted to 412 trillion lire, or 59.1 per cent of GDP, as against 377 trillion and 61.5 per cent in 1984 (Table 42). Government securities accounted for 91.3 per cent of the supply, the rest consisting of issues by special credit institutions (7.4 per cent) and firms and public corporations (1.3 per cent).

Table 42

ISSUES OF SECURITIES AND NET RECOURSE TO THE MARKET

(billions of lire)

	Gross issues		Net issues		Net recourse (1)	
	1984	1985	1984	1985	1984	1985
Public sector	344,235	376,647	73,005	97,333	19,293	40,881
Treasury bills	227,747	256,281	9,300	13,181	−11,981	−8,116
Treasury credit certificates	95,250	97,210	56,738	78,567	31,413	51,111
Other securities (2)	21,238	23,156	6,967	5,585	−139	−2,114
Special credit institutions	27,879	30,316	8,531	6,917	−6,085	−9,341
Firms and public corporations	4,476	5,473	2,035	2,352	−1,080	−916
Total	**376,590**	**412,436**	**83,571**	**106,602**	**12,128**	**30,624**
As a percentage of GDP	*61.5*	*59.1*	*13.7*	*15.3*	*2.0*	*4.4*

(1) Gross issues less redemptions, premiums or discounts and paid coupons. For Treasury bills, gross issues less redemptions and premiums or discounts. For certificates of deposit of the special credit institutions, net issues less interest payments. — (2) Net of funding operations.

Excluding funding operations, gross issues of government securities amounted to 377 trillion lire (344 trillion in 1984), of which over two thirds served to renew expiring debt. The smallness of the increase in issues (9.6 per cent) was due in part to the deliberate lengthening of the average residual life of the public debt over the last three years. Net issues totaled 107 trillion lire (84 trillion in 1984), of which 92 trillion consisted of medium and long-term securities.

The private sector and non-residents took up 58 per cent of the net issues, Italian investment funds 12 per cent and banks 6 per cent. The Bank of Italy's net purchases, excluding those under repurchase agreements, amounted to 18.8 trillion lire and were made mainly in December in connection with the abnormal growth in bank liquidity described in earlier chapters.

The volume of outstanding government securities expanded over the year by 109 trillion lire to 516 trillion.

The reduction in the uncertainty surrounding the renewal of very large volumes of short and very-short-term securities, achieved by lengthening the average maturity of new issues, has permitted a more balanced development of the market. The average residual life of government securities, which fell to a low of 15 months at the end of 1982, reached 3 years and 5 months at the end of 1985. This has curbed the growth in annual redemptions by distributing them over a longer time span.

Interest payments were also on a relatively small scale. Coupon payments amounted to 35.9 trillion lire (32.4 trillion in 1984), considerably less than the roughly 50 trillion forecast for 1986, when the effects of the January 1985 switch to annual coupons on Treasury credit certificates will be felt in full.

The range of securities offered was extended during 1985 with the aim of meeting investors' requirements and reducing the cost of the debt. Treasury bond issues were made more frequently; they carried three-year and, starting in February, two-year maturities and amounted to 17,289 billion lire (17,750 billion in 1984). Eight-year Treasury certificates in ECUs were also issued more frequently; sales of these securities were restricted to the domestic market and raised 3,367 billion lire (1,688 billion in 1984). The securities of this kind subsequently sold to non-residents amounted to 235 billion lire (21 billion in 1984). Starting in mid-July, monthly issues of five-year Treasury credit certificates with half-yearly coupons based on the yield on twelve-month Treasury bills were offered at a fixed price. Subsequently, the authorities dropped the uniform-price auction method for start-of-the-month issues of ten-year Treasury credit certificates and reverted to fixed price sales.

Net recourse to the market by borrowers other than the Treasury was positive in the case of the State Railways and ANAS (1,513 billion), IRI (43 billion) and international institutions (483 billion), while it was negative for the special credit institutions (-7,680 billion), ENEL (— 924 billion) and ENI (— 343 billion).

The substantial volume of new issues was accompanied by an increase in turnover in the secondary market. Specifically, trading on the Milan stock exchange, though still fairly small, expanded from 2.8 to 3.1 trillion lire for government securities and from 1.5 to 2.3 trillion for bonds. The growth in the secondary market also had a positive effect on the primary market since it increased the liquidity of securities.

The interest rates on government securities came down with inflation, the yields at issue on twelve-month Treasury bills and longer dated Treasury credit certificates falling by respectively 1.5 and 1.4 points. The yield differential thus remained virtually unchanged in absolute terms, but widened slightly in relation to the yield on Treasury bills.

The yield at issue on three-year Treasury bonds rose by over one point in the summer, but by April 1986 had returned to the level of the first quarter of 1985 (12.58 per cent) and then came down further in May to 11.03 per cent. The yields on Treasury certificates in ECUs decreased by nearly one point (from 9.59 per cent in February to 8.74 per cent in November), in line with the general downturn in the rates on ECU-denominated securities. The ex post real yields on Treasury credit certificates fell in 1985 compared with the two previous years (Table 43).

Table 43

EX POST REAL YIELDS ON TREASURY CREDIT CERTIFICATES

(percentages)

Year of purchase (1)	Year of disposal (1)					
	1980	1981	1982	1983	1984	1985
1979	– 1.61	– 0.74	0.95	2.71	4.00	4.41
1980	—	0.15	2.27	4.21	5.47	5.67
1981	—	—	4.45	6.31	7.30	7.09
1982	—	—	—	8.19	8.75	7.98
1983	—	—	—	—	9.32	7.88
1984	—	—	—	—	—	6.46

(1) End of period.

Shares

Private sector companies' share issues in 1985 were virtually unchanged compared with the previous year. The 14.7 trillion lira total for issues by non-bank companies comprised 9.5 trillion by state-controlled companies (6.2 trillion in 1984) and 5.2 trillion by private sector companies (5.1 trillion in 1984) (Table 44). Net issues by the latter, obtained by adjusting for the double-counting caused by inter-company investments, amounted to 4.4 trillion lire, of which 2.2 trillion was by listed companies (including 400 billion lire of savings shares and 100 billion of preference shares). When dividends are also deducted, listed private sector companies' recourse to the share market is found to have been on a relatively small scale (1.15 trillion lire, as against 1.1 trillion in 1984). These companies failed to adapt their behaviour promptly to the structural change engendered by the larger number of institutional investors and the changed attitude of savers to investment in shares.

Table 44

GROSS SHARE ISSUES (1)

	Billions of lire				% composition			
	1982	1983	1984	1985	1982	1983	1984	1985
Listed companies	**2,892**	**3,959**	**5,694**	**4,693**	52.5	32.8	50.4	31.9
state controlled	*1,974*	*3,269*	*3,760*	*2,161*	*35.8*	*27.1*	*33.3*	*14.7*
private sector	*918*	*690*	*1,934*	*2,532*	*16.7*	*5.7*	*17.1*	*17.2*
Unlisted companies	**2,619**	**8,118**	**5,599**	**10,026**	47.5	67.2	49.6	68.1
state controlled	*1,108*	*5,981*	*2,434*	*7,348*	*20.1*	*49.5*	*21.6*	*49.9*
private sector	*1,511*	*2,137*	*3,165*	*2,678*	*27.4*	*17.7*	*28.0*	*18.2*
Total	**5,511**	**12,077**	**11,293**	**14,719**	100.0	100.0	100.0	100.0
state controlled	*3,082*	*9,250*	*6,194*	*9,509*	*55.9*	*76.6*	*54.9*	*64.6*
private sector	*2,429*	*2,827*	*5,099*	*5,210*	*44.1*	*23.4*	*45.1*	*35.4*

(1) Excludes shares issued by the credit system.

A substantial number of shares, totaling 460 billion lire, were issued in 1985 to meet stock exchange listing requirements. These issues, which were generally made at a fixed price, were all fully subscribed on the first day, and when auction methods were tried the allotment prices were well above the minimum selling price.

The 13 new companies listed in 1985 (including two that moved up from the over-the-counter market) took the total to 188, including 20 suspended companies; 167 of these are listed on the Milan stock exchange. The total issued share capital of listed companies amounted to 26,275 billion lire at the end of 1985, of which about 5,600 billion was owned directly by the companies themselves.

Among the close substitutes of shares, there were large issues of convertible bonds (1,420 billion lire, of which 760 billion were sold directly by firms) and savings shares (one issue of 460 billion). In many cases the conversion offer involved savings shares, for which the lack of voting rights is partly compensated by more favourable tax and dividend treatment.

Share prices soared, under the impetus of an excess of demand over supply in conjunction with good news about corporate profitability. The Milan stock exchange index rose by 100.7 per cent over the year (compared with a rise of 21 per cent in 1984).

The Italian share market was not the only one to perform strongly, although the increase in share prices in 1985 — after the dreadful performance of the seventies — was much larger than in most other countries, where substantial advances had already been made in earlier years. Moreover, these developments have come at a time of general improvement in the business sector, with corporate profits increasing considerably in 1985 and the outlook for 1986 highly encouraging in many sectors.

The net profits of the listed companies whose 1985 annual accounts have already been published (121 out of 188) rose from 2,005 to 2,908 billion lire, an increase of 45 per cent, which came on top of that of 72.5 per cent recorded in 1984. The weighted average price/earnings ratio based on end-1985 prices amounted to 23, giving a real rate of interest of 4.4 per cent (6.6 per cent in 1984), which is in line with the long-run real rate as approximated by the real yield to maturity at the same date on index-linked Treasury certificates (5 per cent).

The consolidated accounts of 30 of the most important financial groups traded on the stock exchange (including some unlisted companies) show even sharper increases in profits (94 per cent in 1985 and 134.7 per cent in 1984), which confirms the return of large firms to profitability.

The Italian investment funds broadened the share market and thus helped to increase the liquidity of shares, with positive effects on saver demand. The funds' net investment in shares was not very large in relation to their total fund-raising (3.6 trillion lire out of 15.3 trillion in 1985) but was substantial in relation to the small size of the Italian market; together with purchases by portfolio management services (0.5

trillion lire out of total investments of 14 trillion) it accounts for a good part of the total demand.

Gross foreign investment in listed shares amounted to 4,763 billion lire (1,329 billion in 1984). Disinvestment was concentrated in the second part of the year, when prices were higher, so that net investment amounted to only 183 billion (211 billion in 1984).

The growth in the share market accelerated sharply in the early part of this year — in the first four months issues by listed companies totaled 2.9 trillion lire, with private sector companies accounting for 1.8 trillion. Share turnover on the stock exchange rose to 23.8 trillion lire (5.9 trillion a year earlier) and share prices rose by 68 per cent (compared with 23.2 per cent).

The large rise in share prices in the first half of 1986 appears to have been due in part to a demand fueled by expectations of capital gains. In order to buttress market operators' solvency, the Consob raised the margin requirements on forward and option contracts. This culminated in the margin being raised to 100 per cent for forward purchases on 15 January 1986 and for forward sales on 11 March. On 2 April the Consob barred the short sale of call options, but continued to allow forward short sales to maintain market flexibility.

For its part the Bank of Italy took steps to ensure orderly settlements and limit the use of provisional certificates of title issued by banks. As of the June 1986 settlement, members of clearing houses unable to deliver certificates on the due date will be required to make a non-interest-bearing deposit equal to 30 per cent of their value. Non-delivery arising directly from dealings with clearing houses will be exempted.

HOUSEHOLDS' SAVING AND THE FINANCING OF ENTERPRISES

The trend in financial balances

In 1985 the ratio of the financial balance of households to GDP declined by about half a percentage point, while the net indebtedness of enterprises and the public sector rose by respectively 0.9 and 0.7 per cent of GDP. As a result, net foreign indebtedness was larger than in 1984 (Table 45). Adjusted for inflation, the movements in the ratios of the domestic sectors' financial balances to GDP were similar to those in nominal terms owing to the slight slowdown in consumer prices during the year.

Table 45

FINANCIAL BALANCES (1)

(percentages of GDP)

	Households	Enterprises	Public sector (consolidated) (2)	External sector	Households	Enterprises	Public sector & BI-UIC
					(adjusted for inflation) (3)		
1976	16.3	−10.1	−9.9	1.5	1.8	−3.0	0.6
1977	15.4	−4.7	−8.7	−1.1	6.2	−0.4	−2.2
1978	16.8	−4.3	−10.2	−2.4	8.7	−1.0	−3.7
1979	15.7	−3.5	−10.0	−1.7	2.3	1.3	1.0
1980	13.5	−8.6	−9.8	2.4	−0.8	−3.5	2.8
1981	14.7	−7.0	−12.8	2.3	2.6	−2.6	−1.7
1982	15.7	−4.9	−14.0	1.5	4.2	−1.1	−3.1
1983	16.7	−4.7	−14.0	−0.2	7.4	−1.9	−4.9
1984	17.4	−4.7	−15.3	0.8	10.0	−2.6	−7.6
1985	17.0	−5.6	−16.0	1.2	9.5	−3.6	−7.9

(1) Financial assets and liabilities include pension and severance pay funds. — (2) Net indebtedness; includes actuarial reserves of social security institutions. — (3) For a more detailed description of the method used, see the article "The inflation adjustment of financial balances" in the Bank of Italy's *Economic Bulletin*, No. 1, October 1985.

Households sustained a loss of purchasing power equivalent to 7.5 per cent of GDP on their financial assets; the gain recorded by the public sector was of the same order.

As in 1984, the decline in the purchasing power of households' financial assets was more than offset by the net flow of interest income; adjusted for inflation, the sector's financial gain of about 1 per cent of GDP was primarily at the expense of the public sector, including the central bank.

Households' saving and financial assets

Households' financial saving remained broadly unchanged in relation to disposable income, decreasing from 21.4 per cent in 1984 to 21 per cent in 1985. The flow of gross domestic financial assets was 123,883 billion lire, about 10,700 billion more than in the preceding year (Table 46); calculated in relation to the initial stock, the rate of growth fell from 18.8 to 16.9 per cent.

Table 46

FINANCIAL ASSETS OF HOUSEHOLDS (1)

(billions of lire)

	Year-end stocks			Flows				
	1980	1984	1985	1981	1982	1983	1984	1985
Notes and coin	19,235	31,167	34,028	3,381	2,669	3,068	2,814	2,859
Bank deposits	160,549	276,015	307,256	20,023	39,648	25,143	30,652	31,241
Post Office deposits	28,451	42,517	50,507	1,915	2,800	3,687	5,664	7,990
Treasury bills	30,397	99,163	114,676	21,845	10,765	13,874	19,845	14,134
Special credit institutions' deposits & savings certificates	5,776	19,625	21,168	1,356	6,858	1,364	4,271	1,543
Treasury credit certificates	8,008	75,312	108,536	3,208	5,268	29,475	27,942	31,609
Other government securities	8,234	17,645	19,160	1,179	−1,465	3,332	5,370	1,321
Other medium & long-term securities (2)	9,478	21,551	24,503	895	2,714	4,528	3,654	2,940
Units in Italian investment funds	—	1,146	19,783	—	—	—	1,055	15,256
Shares & participations	24,513	46,703	85,916	663	87	203	141	1,335
Foreign assets	3,568	6,525	9,309	374	146	85	545	664
Other financial assets (3)	56,700	94,366	107,356	8,109	8,762	9,905	11,171	12,991
Total	**354,909**	**731,735**	**902,198**	**62,947**	**78,252**	**94,664**	**113,124**	**123,883**

(1) Partly estimated data. — (2) Excluding foreign bonds. — (3) Actuarial reserves, pension and severance pay funds, atypical securities and bankers' acceptances.

Households' financial saving is reckoned to have remained at the high levels of recent years as a proportion of total saving by the sector (84 per cent). The shifts in the composition of wealth to the detriment of the real estate component were amplified by the stagnation in property values and the rise in share prices. Provisional estimates of the proportion of households' assets held in the form of dwellings, land and durable consumer goods suggest that gross financial assets increased from 32 to around 36 per cent of total wealth in 1985.

The information available on rents and house and flat prices indicate that the real yield on this form of investment has been negative in recent years. By contrast, the average yield on households' financial assets in the form of money and securities other than shares, deflated for the change in consumer prices, became positive in 1983 and averaged 3.7 per cent last year; the rise of about one and a half percentage points over 1984 was due to a shift towards higher-yielding types of asset. The increased profitability of investments in financial instruments, which produced a further rise of about 13 points in the ratio of financial assets to disposable income, was substantially greater if one also takes account of the yields on holdings of shares and investment fund units, the performance of which is described in earlier chapters.

The rapid increase in purchases of investment fund units partly reflects the desire on the part of savers to diversify their portfolios, in which government debt has accounted for a growing share in recent years; government paper doubled as a proportion of households' financial assets between the end of 1980 and the end of 1984, rising from 13.1 to 26.3 per cent. Last December investment fund units accounted for 2.2 per cent of households' total assets (calculated in terms of flows, the proportion was 12.3 per cent), while public sector securities made up 26.9 per cent, about half a percentage point more than at the end of 1984. In assessing these changes, it should be borne in mind, however, that the slowdown in direct purchases of government securities by households was accompanied by a greater accumulation of such paper in the investment funds' portfolios.

The twelve-month rate of growth in households' deposits and other liquid assets included in M2 fell from 12.6 to 12 per cent between the end of 1984 and the end of 1985; the growth differential between money and total financial assets therefore remained large (4.9 percentage points, compared with 6.2 in 1984), continuing the trend that has been evident since the beginning of the decade.

The financing of enterprises and their liquidity situation

The favourable trend in self-financing and the fact that the expansion of investment in fixed capital and stocks was less vigorous than in 1984 enabled firms to limit their external financing at a time when interest rates were still high. Even including the abnormal bulge in bank lending in the closing stages of the year, which is put at about 10 trillion lire, firms' external financing came to 54,398 billion, compared with 51,447 billion in 1984 (Table 47). The decrease in the flow of endowment funds and special credit was substantially outweighed by increased recourse to bank loans and borrowing abroad; the switch from a net outflow of capital of 840 billion in 1984 to foreign borrowing of about 2 trillion last year reflected changes in interest rate differentials. The financial assets of enterprises increased further in relation to GDP, although at a slower rate than in the past.

Table 47

ANALYSIS OF CORPORATE SECTOR EXTERNAL FINANCING

(billions of lire)

	Year-end stocks			Flows				
	1980	1984	1985	1981	1982	1983	1984	1985
Loans: short-term (1)	98,721	172,996	200,123	11,217	12,965	18,974	28,522	29,944
special credit institutions	*5,121*	*12,151*	*14,889*	*2,181*	*1,668*	*307*	*2,873*	*2,738*
medium and long-term (1)	72,674	140,519	147,494	20,964	11,800	9,933	8,851	11,614
banks	*11,743*	*17,257*	*19,527*	*1,958*	*240*	*1,710*	*1,605*	*2,270*
special credit institutions	*44,132*	*73,481*	*78,860*	*10,131*	*8,746*	*6,905*	*7,412*	*6,534*
foreign	*15,006*	*46,778*	*45,358*	*8,641*	*3,074*	*755*	*−839*	*2,064*
Bonds	13,289	23,044	24,888	820	4,589	2,392	1,906	1,844
Shares	124,530	239,899	520,269	2,001	2,038	2,967	4,948	4,361
Endowment funds (2)	12,505	38,986	44,475	3,154	7,384	9,431	6,548	5,130
Other participations	6,521	9,304	10,936	853	1,066	901	1,121	1,632
Other financial liabilities (3)	10,716	21,028	24,983	3,352	−2,460	−70	−449	−126
Total	**338,956**	**645,776**	**973,168**	**42,361**	**37,381**	**44,528**	**51,447**	**54,398**

(1) Flows include bad debts and funded debts and are adjusted for bank loans used to finance the deposits on external payments and for exchange rate variations. The 1984 figures are adjusted for the distortions in banking statistics connected with the removal of the ceiling on bank lending. — (2) Net of state-controlled enterprises' funded bank debts. — (3) Includes acceptances bought by non-bank investors, atypical securities, bank loans used to finance the deposit on external payments and, as regards year-end amounts, the bad debts of credit institutions.

The value added of non-financial enterprises as defined in the national accounts, for which a larger body of information is available, increased less rapidly than in 1984 (by 11.4 per cent, as against 13.3 per cent), but the rate of growth was more than half a percentage point higher than the rise in incomes from employment, including the imputed incomes of self-employed persons. The gross profits of non-financial enterprises as a whole therefore showed a further increase (13.4 per cent) following the very large expansion of 18.9 per cent in 1984 (Table 48); moreover, the reduction in net interest charges, which are described in greater detail below, contributed to a further rise in self-financing on top of the strong recovery in 1984 (20.6 per cent, compared with 29.3 per cent in 1984). The ratio of self-financing to investment in stocks and fixed capital, including residential investment, rose to 87.1 per cent, the highest figure since the middle of the last decade and a contrast to the low of 60.1 per cent recorded in 1981.

Table 48

FORMATION OF THE BORROWING REQUIREMENT OF NON-FINANCIAL ENTERPRISES

(billions of lire)

	1981	1982	1983	1984 (1)	1985 (1)
Gross operating profits *(1)*	75,423	87,275	92,415	109,856	124,585
(−) Net interest charges *(2)*	34,901	36,071	37,259	38,571	37,650
(−) Other items *(3)*	−940	−1,027	−717	−975	−232
Self-financing	41,462	52,232	55,872	72,261	87,167
(−) Fixed investment *(4)*	64,409	68,928	72,274	84,448	95,171
(−) Change in stocks *(5)*	4,532	4,866	−893	4,963	4,897
Net indebtedness *(6)*	−27,479	−21,563	−15,509	−17,150	−12,900
Financial balance of enterprises *(7)*	−25,254	−19,840	−21,698	−24,725	−33,998
Financial balance of autonomous government agencies excluding ANAS *(8)*	376	−288	−2,973	−980	−818
Balancing item *(6) - (7) - (8)*	−2,601	−1,434	9,163	8,555	21,916

(1) Provisional and partially estimated.
Source: Estimates based on Istat national accounts data for *(1), (3), (4)* and *(5)* and Bank of Italy data for *(2), (7)* and *(8)*. "Other items" include direct taxes and dividends paid by firms, less general government investment grants and the change in pension and severance pay funds. The financial balance of enterprises differs from that shown in Table 45 owing to the exclusion of pension and severance pay funds from liabilities. ANAS is classified as part of general government in the national accounts.

Borrowing from credit institutions and bond issues rose by 14.2 per cent overall, as against 15.7 per cent in 1984. If the figures are adjusted for the abnormal expansion in bank credit in the last two months of 1985, the rate of growth in firms' domestic debt was 10.7 per cent; in relation to value added, the aggregate remained broadly unchanged at the low levels of recent years.

Including the expansion in lending in the latter part of the year, the banks met more than half of firms' total demand for credit; bank loans accounted for 54.2 per cent of total lending to firms (Table 47), compared with 53 per cent in 1984, when there had been a vigorous expansion owing to the removal of the lending ceiling. The percentage met by special credit institutions declined right across the maturities range; the share represented by their medium and long-term loans, which are traditionally the most important component, diminished from 14.4 to 12 per cent and short-term credit came down from 5.6 to 5 per cent. Corporate recourse to the bond market remained small, falling by 62 billion to 1,844 billion lire, or 3.4 per cent of the overall flow.

Investor interest in risk capital was heightened by the satisfactory level of profits, enabling companies to raise a considerable volume of funds through share issues for the second year in succession. Share issues represented 8 per cent of total financing, compared with 9.6 per cent in 1984 and an average of 5.6 per cent in the early eighties. It was mainly large companies that obtained finance in this way, partly because their profitability improved more markedly than that of smaller firms.

The reduction in endowment funds, which declined from 12.7 per cent of total financing in 1984 to 9.4 per cent last year, reflected in part the improvement in the operating results of a growing number of public corporations, thus reducing the transfers of state funds required to cover their losses; the privatization of some enterprises and the sale of shares to the public also helped reduce the need for state finance.

The effective average cost of domestic debt fell by about one and a half percentage points, from 17.8 to 16.4 per cent. Net interest charges declined by 2.4 per cent, by contrast with the increase of 3.5 per cent recorded in 1984, and their incidence on gross operating profits diminished for the fourth consecutive year, to stand at 30.2 per cent, compared with 35.1 per cent in 1984. Since 1981, when net interest charges absorbed 46.3 per cent of gross profits, the proportion has thus declined by about 16 percentage points, thanks to the relative decrease in interest payable.

The acquisition of financial assets by firms was fueled by the substantial formation of internal funds and the high yields on such assets. Domestic financial assets excluding shares rose from 32.1 to 33.4 per cent of value added between 1984 and 1985, despite the fact that the average rate of increase over the year (15.7 per cent) was one percentage point less than in 1984; liquidity, measured by the ratio of enterprises' assets comprised in M3 to value added, was slightly higher than in 1984, rising from 29.4 to 29.9 per cent.

SUPERVISORY ACTIVITY

The transformation taking place in the Italian financial system can be seen in the changes in savings flows and in the creation of new instruments, markets and intermediaries. The share of money, and especially of bank deposits, in total financial assets is tending to decline, while those of government securities, shares and investment fund units are rising. The addition of new and more diversified elements in the system's structure is increasing competition.

Credit intermediaries are playing an active part in this process. They have responded to disintermediation by expanding and improving their range of services. In many cases they have fostered innovation by setting up specialized organizations in the new sectors of financial business. The major banks have also looked outside Italy for opportunities to expand the volume and range of their operations.

Supervision seeks to promote the necessary functional and structural adjustments in the system and maximize their positive effects on the efficiency of credit institutions. At the same time it aims to prevent the transformation itself from generating instability.

Entry controls

The establishment of credit institutions. — 1985 saw the full implementation of Community Directive 77/780 on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions. The legislation enacted in the first part of 1985 was followed by the resolutions of the Interministerial Committee for Credit and Savings and the ensuing regulations issued by the Bank of Italy. The promulgation of the new legislation ends the virtual ban on the establishment of new banks, which has been a feature of the Italian banking scene for the last twenty years. It also entails the switch to a system of authorizations based on the satisfaction of objective criteria.

Under Italian law the "fit and proper person" criterion has been extended to shareholders in a position to influence the operations of new banks. The size of shareholdings considered to allow such influence has been fixed at 2 per cent or more of the total.

The capital requirement for new credit institutions has been set at a level that will not exclude new operators but will nonetheless ensure an adequate capital base.

With the aim of allowing a gradual adjustment to the new legislation, applications for the establishment of new credit institutions will also be examined in the light of market needs until December 1989, the end of the transitional period set by Directive 77/780.

In its resolution of 31 October 1985 the Credit Committee laid down the criteria for the Bank of Italy to follow when examining applications to set up new credit institutions during the transitional period. The Bank will give favourable consideration to plans that would: strengthen the supply of banking services in under-banked areas; reduce the concentration of the supply of banking services; or diversify banking facilities in the area of establishment. The activities promoters intend to undertake will also be an important factor in the Bank's assessment. In exercising its powers of authorization, the Bank of Italy will use the indicators of productivity, competition and adequacy of supply it has prepared on the basis of surveys and analyses conducted to enable it to regulate the expansion and geographical distribution of the banking system.

Geographical distribution. — The national branch plan that was unveiled in July 1985 is approaching the final authorization stage. The guidelines underlying the Bank of Italy's decisions were laid down in the Credit Committee's resolution of 26 June 1985 and are consistent with the policy of stimulating banks to greater efficiency and increasing the supply of banking services where necessary.

To achieve these objectives, the acceptance of applications was based on operational criteria covering both the "economic needs" of the market and bank-specific factors.

As regards the former, the aim was to increase banking facilities in poorly served areas and to extend the branch network to new residential and industrial zones. Assessments were made in part by updating and supplementing the analyses used for the previous plan, the basic features of which were communicated to the credit system. The "catchment areas" for banking services to households were redefined and a new indicator was developed for areas with a high level of services to enterprises.

Assessment of the bank-specific features was on the basis of each bank's efficiency, in terms of profitability, and the strength of its technical and organizational structures.

The efficiency of the banking system can be increased not only by expanding the branch network and thereby stimulating competition but also by modifying the networks of individual banks. For this reason the Bank of Italy encourages network rationalization based on the transfer of existing branches and the expansion of those conducting only a limited range of operations.

The role of branches providing a full range of services and acting as the only point of contact between banks and their customers is bound to be changed by the possibilities opened up by the advance of technology. The optimal network may well include automated teller machines on their own.

Regulations and controls

The regulation of banking. — Further progress was made in enhancing credit institutions' decision-making autonomy by rationalizing the constraints imposed on their activities. In particular, authorizations of individual transactions are being replaced by limits within which credit institutions are free to operate autonomously. Among other things, this reveals the criteria underlying supervision more simply and clearly.

As a result of this policy, the number of loan authorizations granted in 1985 fell to around 7,800, or barely one third of the 1984 total. The reduction in recent years in the number of authorizations allowing banks to exceed their lending limits has been partly due to the different developments of the aggregates on which these regulations are based and, in particular, to the increase in banks' own funds.

The transformation taking place in banking has also involved their medium and long-term operations. The regulation of those denominated in lire is already based on limits within which banks can operate autonomously, but these constraints vary from one category of bank to another. The increasing uniformity of the operations undertaken by the various categories of bank suggests the need to assess the feasibility of regulatory frameworks that will help to level the competitive playing field.

Foreign currency operations, by contrast, are covered by the same regulations for every category of bank, but developments in international markets have made some revisions necessary. For example, the lengthening of maturities in the restructuring of some developing countries' foreign debt has put pressure on Italian banks' operating limits. More generally, widespread innovation in international banking (especially off-balance-sheet operations) calls for a revision of the regulations in the light of the new conditions.

To meet this need, the supervisory authorities have begun to review all the regulations governing banks' medium and long-term operations, an exercise with practical implications for the functional specialization that is one of the pillars of the Italian credit system.

1985 provided additional confirmation of the tendency for credit intermediaries to diversify their activities and broaden their range of financial services. A recent survey shows rapid growth in banks' portfolio management business, conducted both directly and through trust companies. The value of managed assets rose from less than 10 trillion lire at end-1984 to over 29 trillion at 31 March 1986.

Off-site supervision. — The revision of the standard prudential return was completed during the year with the cooperation of the banking system. After carefully assessing the costs and benefits, banks will have to improve their accounts and accounting procedures, invest in computer programs and make the best possible use of the new information that will become available.

Law 114/1986 (implementing EEC Directive 83/350) on supervision on a consolidated basis requires credit institutions to supply the Banking Supervision Department with accounting data on groups as a whole and on their main component companies. The Law is another step in the process of improving the instruments of control (consolidation of banks' foreign business, returns on intra-group positions), which will advance further with the new standard return and the additional information it will give for the analysis of the situation of Italian banking groups.

The picture provided by supervision on a consolidated basis and the revision of the standard return will be filled in by Law 281/1985 on the ownership of banks. The notifications for which it provides will make it possible to know the identity of beneficiary shareholders, even when the shares are held by nominees. The information on indirect ownership via subsidiaries will also reveal corporate shareholders. The steady flow of information provided directly by shareholders and the powers of investigation foreseen by the Law will permit changes in the pattern of ownership to be monitored.

Inspections. — A total of 178 general inspections and 10 sectoral inspections were carried out in 1985. The general inspections covered three special credit institutions and 15.9 per cent of the banks in Italy, compared with 18.7 per cent in 1984; the customer deposits and lending of these banks amounted to about 60 trillion lire, or 8.5 per cent of the total for the banking system.

Under agreements with the US and UK supervisory authorities, inspections were carried out at the New York and London branches of an Italian bank in conjunction with the inspection at the parent bank in Italy.

The inspections showed that most of the banks were in satisfactory operating condition and soundly managed.

Analysis of the credit institutions' profitability, based on the sample of banks inspected in 1984 and 1985, has shown that there are still substantial differences depending on the size and type of the institutions, their area of operations and the quality of management. The survey confirms that the profits of medium-sized and large banks depend less on net interest income and more on income from services. Net interest income continued to be higher in the case of smaller banks; it declined slightly for Italy's international banks, primarily because of the larger share of business conducted abroad, where sharper competition keeps interest margins narrower.

International cooperation. — International cooperation in banking supervision is steadily strengthening. Many countries have endorsed the principles laid down in the Basle Concordat of 1983. The revision of national regulations and practices in order to bring them into line with the principles agreed internationally and to achieve a progressive convergence of supervisory standards and practices is proceeding apace.

The purpose of the Concordat is to make banking supervision more effective. The exchange of information between establishments in different countries and between the supervisory authorities of different nations is a fundamental prerequisite for the achievement of this objective.

Italy took a significant step in this direction by passing Law 114/1986 on the control of banks' equity participations. For purposes of supervision on a consolidated basis, the Law permits information on banks' equity participations to be exchanged with the supervisory authorities of other EEC countries and, on a reciprocal basis, with those of non-EEC countries as well. It also provides for the information obtained in this way to be verified by on-site inspection.

The recent development of innovative financial transactions by international banks has been analyzed by international organizations. At the request of the Governors of the central banks of the Group of Ten, the Committee on Banking Regulations and Supervisory Practices has examined the most important kinds of transactions from the point of view of risk and their implications both for banking operations and for supervision. The Committee's findings have been communicated to the credit institutions affected.

The risks of international lending can be better contained if the banks strengthen their capital bases by various means, including the adoption of suitable policies for making provisions against bad and doubtful debts. A comparative study by this Committee has confirmed that tax treatment has a decisive influence on the size of banks' risk provisions with respect to "sovereign debtors". The central bank Governors of the Group of Ten countries endorsed the Committee's recommendation that the tax authorities take a more favourable view of the matter. The Bank of Italy has brought the issue to the attention of the Ministry of Finance.

Worldwide cooperation has been accompanied by significant progress within the European Community. In June 1985 the Commission submitted to the Council a White Paper outlining the actions needed to unify the European market by the end of 1992. The recommended strategy involves a shift in emphasis from the harmonization of regulations to the reciprocal recognition of the individual members' existing techniques and products.

Community organs may be able to act more effectively once directives and recommendations concerning financial services can be approved by qualified majority, as laid down in the Single European Act amending the Treaty of Rome. Italy's supervisory authorities are preparing to adjust to the tasks deriving from the acceleration of European integration.

The overall health of the credit system

During 1985 the Italian credit markets saw the consolidation of several changes of special relevance to efficiency and stability, the principal concerns of banking supervision. Bad and doubtful debts expanded more slowly, presumably as a delayed reaction to the improvement in the condition of firms. The rapid expansion of the stock market, investment funds and investment management services lent additional impetus to the fundamental changes that have been occurring in banking for the past few years. Major credit institutions, including public ones, launched substantial share issues via the stock market; as well as being a significant institutional development in itself, this is an indication of the major banks' efforts to adjust, which have also been evident in the greater variety of services offered, their expanding international business and the restructuring of their organization and costs.

These developments can best be appreciated over a period of years. Between 1981 and 1985 the decline of bank intermediation as a share of total savings flows was accompanied by a decline in net interest income; operating costs proved relatively rigid; and the risks on balance sheet assets increased in connection with, the poor performance of the economy.

Generally, the Italian banking system has reacted well to these developments. The level of own funds has risen, thanks primarily to self-financing. Services have been expanded, most notably trading in securities; in this field the leading banks are predominant, accounting for more than half the entire banking system's net income from securities transactions in 1985. Rationalization is well under way, the degree of automation is high and labour productivity has risen, especially in the larger banks. The effort to achieve more efficient organizational structures is a far-reaching one, however, and still demands a strong commitment on the part of the banks.

There are still disparities, some geographical, between the various segments of the banking system and within these as regards capital ratios, sources of own funds and the riskiness of assets.

Capital adequacy. — The improvement in capital ratios continued last year, though unequally both among the various size groups and legal categories and within these. The ratio of banks' own funds to customer deposits rose from 7.0 per cent in 1981 to 10.6 per cent in 1985.

In the case of special credit institutions, the ratio of own funds to total borrowing rose from 9.4 per cent in 1981 to 12.2 per cent in 1985.

Self-financing and recourse to the capital market. — In the five years from 1981 to 1985 profits contributed on average around 80 per cent to the recapitalization of the banking system.

Nevertheless, appropriations from gross profits tended to decline in relation to total resources, particularly in the case of cooperative banks, where they fell from 1.3 per cent in 1981 to 0.7 per cent in 1985. Two factors were responsible for this tendency: on the one hand a slight contraction in net income as a percentage of total resources since 1981 (the peak during the period from 1975 to 1985) and on the other a rise in net profits, which in some sections of the banking system was connected partly with the need to offer competitive yields on their securities.

Recourse to the capital market made a much smaller contribution to the increases in capital than self-financing.

Lending risks. — The bad and doubtful debts of banks and special credit institutions alike increased more slowly in 1985. The rate of growth was 21.6 per cent in the case of banks (rising from 13,939 to 16,950 billion lire) and 23.8 per cent in that of special credit institutions (increasing from 5,278 to 6,533 billion lire), compared with 28.1 and 26.6 per cent respectively in 1984.

As mentioned above, this development can be regarded as a first sign of the improved earning capacity and financial situation of the corporate sector.

Investment funds

It is little more than three years since the enactment of Law 77/1983 and two since the first Italian investment fund began operations, and yet this form of financial intermediation has developed tremendously.

Since the launch of the new institutions, the supervisory authorities' activities have been directed towards ascertaining that the requirements for market access are met and maintained, approving fund rules and constructing a system of statistical returns that will enable them to verify that the management companies and funds are complying with the limits imposed on their activities.

At the end of April 1986, 34 management companies were registered with the Bank of Italy. At the same date 48 funds were in operation, of which 5 specialized mainly in shares, 21 in bonds and 22 had a mixed portfolio.

The general criteria that the supervisory authorities have applied when approving fund rules are designed to protect the position of subscribers and ensure that the terms on which transactions with the funds are conducted are unambiguous. In implementing these criteria, the authorities have simplified the procedures by reducing the period between the subscription and issue of units, standardized the methods of distributing profits and systematically examined ancillary contracts to ensure that they accord with the principles laid down in the funds' rules.

The need to augment and improve the information contained in the management companies' published statements of account prompted the supervisory authorities to modify the funds' standard quarterly report in order to provide clearer information on the way each fund is managed.

Awareness that the large number of funds entering the market and the rapid growth of mixed and share-based funds could place pressure on share prices in the relatively narrow Italian stock market made the managers of share-based funds cautious about the composition of their portfolios in the first part of this year; this does not conflict with their rules, which were drawn up in such a way as to give them a high degree of flexibility in reaching their day-to-day decisions.

The enlargement of the funds' scope for operations abroad may also ease the pressures they exert on the Italian stock market.

Until April 1986 the funds enjoyed exemption from the non-interest-bearing deposit required under the exchange control regulations on purchases of foreign securities equal to a maximum of 10 per cent of the value of their assets six months previously. With the agreement of the Bank of Italy, the Ministry for Foreign Trade has reduced the time lag for determining the assets base on which to apply the 10 per cent exemption to three months; the reduction is being phased in gradually so that the system will have steadied by June 1986. This modification was preferred to raising the maximum exemption in order to avoid increasing the funds' advantage over other intermediaries and to allow newly established funds to enter the foreign sector more quickly.

THE GOVERNOR'S CONCLUDING REMARKS

For several years central banks have operated in an economic environment that is evolving rapidly and sometimes turbulently, at both the domestic and international levels. They have been and still are faced with exchange, money and capital markets characterized by more intense activity and profound changes, which are reflected in the mobility of capital, exchange rate fluctuations, the level and volatility of interest rates and new forms of intermediation.

Sophisticated networks linking financial intermediaries, markets and customers, clearing techniques not requiring the actual transfer of traded securities and new settlement instruments that replace traditional ones are revealing new possibilities in payments systems, in financial transactions and in treasury management by banks, firms and public authorities.

These developments require the Bank of Italy, no less than the entire credit system, to make continual improvements in the way in which it fulfils its institutional responsibilities. The workload has increased in each of the functions it is required to perform, be it monetary and foreign exchange policy, supervision and intervention in the credit sector or the provision of financial services. The staff of the Bank has risen to this increased challenge.

The Bank is called upon to do even more — to combine these distinct yet inseparable functions, to exploit the positive aspects of market developments while containing the potential causes of instability, and to carry out cogently and effectively the market operations and administrative actions for the management of money and credit.

Both at the Head Office and in the branches, there is a growing need for sound and at the same time adaptable professional skills in the economic, legal and technical fields, for managerial and executive ability and for reliable but flexible patterns of organization.

Constant attention and considerable resources are being devoted to staff training. In this effort we are guided by the conviction that the distinguishing mark of the staff of a modern central bank is to be found in the balanced combination of basic interdisciplinary training and specialist knowledge and experience.

Assessment and recognition of the various levels of responsibility are indispensable, with staff being selected on the basis of merit.

Special attention was paid last year to matters involving automated data processing, with steps being taken to integrate the organizational and data processing functions more closely. The preparatory stage of the work associated with the introduction of the "New Lira" was completed.

In April, agreement was reached with the trade union delegations on staff pay and conditions for the three-year period from 1985 to 1987. The negotiations, which opened the round for the credit sector as a whole, were protracted, complex and occasionally bitter, but a positive conclusion was eventually reached. During certain stages of the discussions the operations of the Bank's departments and branches were disrupted, suggesting the need for a code of conduct that would achieve a better balance between trade union rights and the obligations associated with service to the community.

The agreements that were reached are designed to satisfy three requirements, namely to enhance the Bank's ability to perform its functions by setting professional competence and efficiency above automaticity, to go further towards satisfying trade union requests for information on planned organizational and technological innovations with a general impact on working conditions and to make significant improvements in staff pay and conditions, while adhering to the limits on salary increases set by national economic policy. Implementation of the agreements is now incumbent upon the Administration and the staff as a whole.

The world economy

The rate of growth in the industrial economies was almost halved last year; the pronounced slowdown in the United States was not offset by faster growth in the other major countries. The expansion in the European economy continued to be less vigorous than in similar stages of past cycles and investment remained sluggish. The growth in world trade fell from 9 to 3 per cent and the elasticity of trade with respect to economic activity returned to the low levels of the early eighties. The current account imbalances of the three major industrial countries became more pronounced: in the United States the deficit rose to a record $118 billion and the country became a net debtor for the first time in more than seventy years; Japan's surplus rose to $49 billion and Germany's to $13 billion.

Unemployment remained below 3 per cent of the labour force in Japan, while in the United States it fell to 7 per cent, after having touched 11 per cent at the end of 1982. In Europe, however, it is still around 11 per cent, despite the slow growth in the supply of labour and the progress made in narrowing the gap between wage and productivity growth in recent years; together with sluggish aggregate demand, the labour-saving nature of investment continued to play an important role in this respect.

The most positive aspect of economic developments in the main industrial countries was the further reduction in inflation; in 1985 the increase in consumer prices fell to 4 per cent, less than at any time for twenty years, and the wholesale prices of industrial goods rose by 2 per cent. The dispersion of inflation rates around the mean narrowed.

In most industrial countries the trend in industrial unit labour costs continued to favour the slowdown in inflation; in Germany, Japan and the United States they increased by less than 2 per cent. The dollar prices of raw materials were also a significant factor, with those of non-oil products falling by a year-on-year average of 12 per cent and oil prices by 4 per cent. Since the dollar export prices of manufactures rose by 1 per cent, the terms of trade of primary products deteriorated further, falling to their lowest level since the Second World War. Over the years, the effect of factors tending to reduce the demand for primary products, such as the use of technologies with a lower raw material content and the reduction of inventories as, a result of high real interest rates, has been compounded in some sectors by an expansion in supply, particularly in that of agricultural products.

The fall in inflation in industrial countries to the levels of the fifties and sixties is the result of economic policies dating from the early eighties aimed at correcting the root causes of the problem; these have led to reduced dependence on oil (the decisive factor in the breakdown of the OPEC cartel), increased resource mobility, more flexible production methods and a weakening of the mechanisms that severed the link between wage growth and productivity.

There are therefore grounds for hoping that the Great Inflation is over; the challenge now is to return to a growth path of full employment combined with price stability.

At the beginning of 1986 the world economic scene was altered by the accelerated decline of the dollar and to an even greater extent by the collapse in oil prices, which fell by over 40 per cent in the space of a few weeks. Although the impact of these developments on individual countries and regions will differ substantially, for the world economy as a whole they should be conducive to stronger growth, a reduction in unemployment and an easing of the financial strains that have accumulated over more than a decade.

The gradual weakening of oil prices had been due to success in energy conservation and the development of alternative sources, but the price collapse that occurred in January was caused to some extent by temporary factors and may therefore be partly reversible. Uncertainty is heightened by events such as the accident that occurred at a nuclear power station a few weeks ago.

Scenarios constructed by international organizations on the assumption of an average oil price of around $15 per barrel suggest that the oil receipts of oil-exporting developing countries will fall by $70 billion in 1986 and those of planned economies by $5 billion. Developing countries that are net oil importers should enjoy a reduction of more than $15 billion in their energy bill; in some of them, part of these resources will probably be used to improve their external financial position and will therefore not translate into higher imports. The demand stimulus required to offset the reduction in imports by oil exporters and to allow world trade to grow will have to come from the industrialized countries, which are expected to save some $60 billion as a result of the fall in oil prices. Growth in the industrialized world is expected to increase by more than one percentage point over a two-year period and inflation to fall by between 2 and 2.5 points. The growth in real incomes associated with the slowdown in prices should sustain demand and help hold down wage demands.

Recent economic data indicate, however, that realization of the growth potential created by the fall in oil prices is proceeding slowly. It is essential that economic activity should accelerate in the countries that have defeated inflation and have substantial balance-of-payments surpluses on current account. Conditions are also favourable to a continuation of the fall in interest rates.

The economic policies of the industrialized countries must also take account of longer term considerations. Oil remains a basically scarce commodity; too rapid a resumption in energy consumption and a relaxation of efforts to conserve energy and develop alternative sources would jeopardize the progress made so far and might lead to a rebound in oil prices.

A turning point was reached in the foreign exchange markets in 1985. The upward trend in the dollar exchange rate was reversed and the attitude of the United States changed with regard to the external value of its currency. The gradual depreciation of the dollar began in February, induced by interventions by European central banks, including the Bank of Italy. In early September, signs of upward pressure on American interest rates seemed to foreshadow a renewed appreciation of the dollar. On 22 September the authorities of the five leading industrial countries therefore publicly announced that they had decided to bring about a fall in the dollar exchange rate by various means, including concerted intervention. Their action, in which Italy participated significantly, was immediately effective, partly because it came at a time when changes in the dollar trend were expected and the US balance of payments on current account was clearly in disequilibrium. In the months that followed, the depreciation of the dollar was consolidated by the worsening of the current account deficit and the easing of monetary conditions in the United States, as well as by changes in short-term interest rates made in concertation with the other leading countries.

The dollar has now declined against both the yen and the Deutschemark by almost 35 per cent from the peaks recorded in February 1985; if the other currencies and the composition of US foreign trade are taken into account, the effective depreciation was less, around 25 per cent. In real terms, the dollar exchange rate is now close to the levels recorded in the three years from 1980 to 1982, when the US current account was broadly in balance.

The burden of correcting the balance-of-payments disequilibria between the three leading economies cannot be allowed to fall wholely on exchange rates, which are slow to influence trade flows; this task should now be performed primarily by coordinating aggregate demand policies.

Given the present state of integration of the foreign exchange markets and the high mobility of capital, the exchange rates of the major currencies are influenced predominantly by financial variables and expectations. They can therefore overreact to actual or expected changes in monetary and fiscal policies, with potentially adverse repercussions on trade in goods and services. The stabilization of exchange rates and expectations therefore calls for monetary and fiscal policies to be carefully dosed and coordinated at international level. Beyond the short term, consistency between the macroeconomic paths of the leading countries must be restored in order to eliminate the structural disequilibria between saving and investment.

Whereas structural balance-of-payments surpluses depress the underlying rate of growth of the world economy, cyclical variations in demand, especially in the United States, cause fluctuations in exchange rates, external accounts and international liquidity. Large shifts in exchange rates give rise to fresh real economic shocks and trade friction, jeopardizing international adjustment and growth.

Overall, the European Monetary System stood up well to the repercussions of the fall in the dollar; signs of strain appeared only when the dollar depreciation became too rapid. The adjustment of the central rate of the lira was carried out in July, when there were no pressures in the European exchange markets. The general realignment of rates, which was prevented on that occasion by non-economic factors, was carried out in April of this year.

Cooperation among the central banks participating in the EMS was effective in preventing and counteracting strains, particularly during the fall in the dollar, when interventions in Community currencies might have conflicted with those in dollars. The mechanism for mobilizing official ECUs was activated for the first time; intervention in the private ECU market, which various central banks have been undertaking, albeit on a small scale, was recognized to be useful; and proposals that will permit a link between the official and private ECU markets, which are currently separate, are now under examination.

The developing countries were adversely affected last year by the deterioration in their terms of trade and the slowdown in imports by industrialized countries. The situation was exacerbated by the reduction in lending from private and official sources. The depreciation of the dollar, the decline in international interest rates and the fall in the price of oil have brought an improvement in the overall position of debtor countries, but the situation has become more difficult for those that are net oil exporters.

The growing disparities in conditions in the countries involved lend weight to the view that the external debt problem should be tackled by using measures and instruments tailored to the situation in individual countries while still conforming to uniform general criteria. At the same time, these countries must have a genuine prospect of growth and of an easing of their external financial constraints. The plan put forward by the US Treasury Secretary offers a useful framework, on account of the attention it pays to a resumption of growth, the willingness it displays to provide international support and its recognition of the global nature of the problem. However, implementation of the plan is proving difficult.

The debtor countries must be ready to draw up adjustment plans in collaboration with the Bretton Woods institutions. The scale of capital flight underlines the crucial need to restore confidence at home. The monetary stabilization programmes of Argentina and Brazil demonstrate that awareness of this need is spreading.

It is the duty of the industrial countries to create a climate that will stimulate an expansion of demand and world trade and promote financial stability. The Paris Club will continue to make a substantial contribution to easing the burden on the debtor countries by renegotiating official loans. Another important step is the commitment to give favourable consideration to the resumption of official credit guarantees for exports to debtor countries that implement the necessary adjustment programmes, as was reaffirmed at the recent meeting of the Interim Committee of the IMF.

The operational capacity of the World Bank should be strengthened by agreeing on the general increase in its capital and replenishing the resources of the International Development Association. The World Bank should devise intervention techniques better tailored to the need for structural adjustment of external positions and should strengthen its cooperation with the IMF in the formulation of macroeconomic policies and structural measures.

The commercial banks, which have recognized their specific interest in resolving the problem, have undertaken in principle to grant fresh loans; the amount and cost of such funds will have to take greater account of the progress made by debtor countries in restoring external equilibrium.

International cooperation has been effective in coping with crisis situations in recent years, but it has failed to bring about substantial improvements in the system of exchange rates and international liquidity regulation.

The recent initiatives to stabilize the exchange rates of the major currencies signaled a return to closer cooperation. The Interim Committee of the IMF has endorsed some of the suggestions made in the Group of Ten report on the functioning of the international monetary system; it has identified the introduction of procedures for the multilateral surveillance of economic policies in the major countries as the first step towards improving the system. The criteria and techniques for detecting divergences in national economic policies are being defined. The potential contribution of the SDR in making the supply of official reserves more stable has been acknowledged.

These views were confirmed and given fresh impetus at the recent meeting of the Heads of State and Government of the major countries; they constitute the first steps towards a more closely managed system of exchange rates and international liquidity. Further advances, including target-zone mechanisms, cannot be achieved until the serious balance-of-payments disequilibria of the major countries have been corrected. Awareness of the limitations of the current initiatives and of the difficulties that stand in their way should not discourage efforts to achieve fundamental improvements in the system.

In Europe, the curbing of inflation, the reduction of external deficits and improved prospects for growth are creating the conditions for a resumption of the process of integration.

With the Single European Act of last December, the European Council has endorsed the objectives contained in the White Paper of the Commission of the European Communities on the internal market, which proposes the gradual dismantling of the barriers that still impede the free movement of goods, capital and labour and thus block the creation of a market of continental dimensions on which firms can base their investment and expansion plans. At the same time, the principle of majority voting has been introduced for the most important decisions concerning these matters, which had previously required unanimity. The complete unification of markets will be a test of Europe's ability to advance and that of individual countries to participate in this development.

The Italian economy and monetary and exchange rate policies

In recent months the Italian economy has been benefiting from the decline in the dollar and the fall in oil prices, an opportunity to ease the constraints on balanced growth that must not be missed.

The events of 1985 demonstrated the force of these constraints. Though confirming the renewed strength of the economy, the overall results for the year were less impressive than had been expected.

Gross domestic product grew by 2.3 per cent, equalling the European Community average and creating a hundred thousand new jobs, but the expansion was not robust enough to prevent a worsening of unemployment,, which is increasingly concentrated in the south of Italy. For the first time in thirteen years inflation fell below 10 per cent for the year, but it was still two points above target, while Italy's four-point inflation differential with the rest of the Community narrowed only slightly. The twelve-month inflation rate remained virtually unchanged with respect to December 1984. The state sector borrowing requirement amounted to 16.1 per cent of GDP, as compared with the target of 14.4 per cent. The balance of payments on current account recorded a deficit of 8 trillion lire as against 5 trillion in 1984, despite an improvement in the second half of the year.

Over the year, the expansion of the most significant aggregates for the conduct of monetary policy was relatively close to the targets set in September 1984 and confirmed in February 1985. Credit to the private sector expanded by 13 per cent as against a target of 12 per cent. Total domestic credit, including government borrowing, increased by 18 per cent instead of the 16 per cent planned. The money supply grew by 11 per cent, compared with a target of 10 per cent. All these figures were distorted by exceptional events that occurred towards the end of the year, to which I shall return later.

Independently of the performance of the real and monetary aggregates, the persisting disequilibria, particularly those in public finances, leave the economy exposed to latent instability that emerges as soon as fiscal and incomes policies are eased or falter; there is a growing risk that inflation will be rekindled by the pressure of expectations on aggregate demand, domestic costs and the exchange rate.

In 1985 the risk materialized twice, once in the spring and again towards the end of the year. On both occasions monetary policy had to be tightened to contain the danger.

Early in the year, the high exchange rate of the dollar drove up the lira prices of raw material imports. The expansion of exports to the United States was not enough to offset weak sales in other markets. In Europe, the declining competitiveness of Italian products combined with stagnant demand to hold down export growth. In the first half of the year growth in export volume came to a halt.

The stagnation in foreign demand was offset by an expansion of domestic demand. Investment in machinery and equipment remained buoyant. Expanding consumer expenditure was fueled by rising disposable income, stemming largely from government transfer payments. Increased import volume and higher import prices combined with the slowdown in exports to produce a worsening deficit on the external current account.

Any downward adjustment of the lira's exchange rate within the EMS prior to the expected depreciation of the dollar would have unleashed new inflationary pressures and was in any case hardly feasible during the protracted weakness of the Deutschemark. Indeed, during this phase Italy had had to make substantial intervention purchases to prevent an appreciation of the lira.

With the reversal of the trend of the dollar, a downward adjustment became possible. This met the need to regain international competitiveness after the erosion caused by differential price movements since the previous realignment in March 1983. The rigorous exchange rate stance which we have adopted within the EMS to curb inflation and encourage firms to take lasting cost-cutting measures would lose its efficacy if there were no provision for making adjustments when the point is reached at which disadvantages outweigh advantages. In late February and early March the lira was allowed to slip from the upper to the lower part of the EMS band of fluctuation.

During those months, the budget deficit diverged from its appointed course. Financing it by securities issues at the prevailing interest rates became a problem. In March the Treasury borrowing requirement amounted to 13.4 trillion lire, but there was a sharp fall in demand for government securities. The Treasury drew almost 5 trillion lire on its current account with the Bank of Italy, reaching its overdraft limit, even though the latter had increased by 6.9 trillion lire in January. For the first six months of the year the state sector borrowing requirement was 40 per cent larger than in the first half of 1984.

In the spring, uncertain expectations during the run-up to the local elections and the referendum on the *Scala mobile* were combined with the risk of a surge in domestic demand triggered by public spending and fueled by the heightened liquidity of the economy. The monetary aggregates were expanding faster than planned. Thanks to the improved situation of firms, financing to the productive sector was within the target range. However, the expansion of the banks' net external indebtedness, which had exceeded the set limits, gave grounds for concern.

Non-monetary financing of the public sector borrowing requirement necessitated an increase of almost one point in yields on government securities in April. The monetary and credit aggregates were brought more closely into line with the targets, partly by means of securities repurchase agreements and warnings to the banks to respect the ceiling on foreign indebtedness.

Measured in relation to December 1984 and on an annual basis, the pace of expansion in monetary base slowed down from 16 per cent in May to 12.5 per cent in July. The growth differential between total financial assets and the money supply, which had prevailed for the previous five years but had almost disappeared in the early part of 1985, re-emerged in the summer. By contrast, total domestic credit continued to expand faster than the target owing to the pressure of the public sector borrowing requirement.

Once the inflation risks associated with expectations and domestic demand had been averted, Italy was able to restore its competitiveness by adjusting the central rate of the lira within the EMS in July.

The realignment preempted market expectations and came at a time when the depreciation of the dollar and the fall in commodity prices on world markets kept the inflationary impact to a minimum. The recovery of economic activity in Europe, and especially in Germany, widened the scope for improving Italy's trade balance.

I have commented on another public occasion on the dollar quotation at the fixing of 19 July and the conduct of the Bank of Italy in this regard. The detailed scrutiny to which these events have been subjected has confirmed that the Bank acted correctly.

In the second half of the year, exports recorded a volume increase of 13 per cent on an annual basis while import growth slowed down, partly owing to a pause in the expansion in domestic demand. The rate of increase in consumer spending remained broadly unchanged. Investment in plant and machinery declined, after having expanded by 40 per cent in real terms in the space of two years.

The Bank of Italy maintained tight control over the monetary base in order to complete the correction of the monetary aggregates and complement the exchange rate adjustment. In September, a reduction of more than half a percentage point in deposit rates helped to widen the differential between yields on Treasury bills and those on bank deposits. In October, the banks' liquidity fell to the lowest average daily level since the beginning of the year, turning negative net of fixed term advances and securities repurchase agreements.

The dollar began to depreciate sharply as a result of the agreement among the five leading industrial countries on exchange rate intervention policy; Italy participated in the concerted action, with market sales of $1.7 billion from its reserves between 23 September and 3 October.

The rise in wholesale prices slowed down. Italy's external accounts improved and the fall in import prices offered new scope for reducing inflation. The incipient fall in oil prices on international markets became more pronounced.

The success of its auctions enabled the Treasury to reduce the yield on bills by about half a percentage point in October, bringing the average rate down to 13.27 per cent.

These developments made it possible to continue easing the restrictions on foreign payments and led to a reduction in the official discount rate and the rate on advances from 15.5 to 15 per cent on 7 November.

Business sentiment changed abruptly in the last week of November. A foreign exchange crisis broke out, which lasted for thirty trading days from then until the middle of January and proved to be one of the most serious of recent years.

There was a widespread conviction that the lira would be devalued again; a number of factors may have helped form this impression. Expectations of further imminent realignments of Community currencies were aroused by the strengthening of the Deutschemark and reinforced by official statements from some of the countries belonging to the EMS. Domestic factors may also have played a part; the implementation of budget measures to complement the July realignment of the lira had been delayed, the passage of the

Finance Law was proving laborious and negotiations between trade unions and employers on labour costs had been broken off.

In the last five trading days of November sales of foreign exchange by the Bank of Italy were running at a daily average of more than $150 million. The forward discount on the lira soared, prompting the repayment of foreign borrowings. The outflow continued at a rapid pace throughout December and the first two weeks of January, causing a reduction of $5.3 billion in the foreign exchange reserves.

Given the structurally high degree of liquidity in the economy, the sudden decision by businesses to reduce their foreign liabilities had repercussions on the banking system; in December, when economic activity was no more than moderate, lending in lire rose by 15 trillion lire; on a seasonally adjusted annual basis the rate of growth reached 60 per cent, while the twelve-month rate rose to 22 per cent. The increasing expense of recourse to the Bank of Italy was not reflected in the cost or volume of bank lending.

To have given way to market pressure would have been to endorse adverse expectations of the external and internal value of the lira that were not justified by the state of the economy. The subsequent use of exchange rate management for purposes of economic policy would have been jeopardized and the benefits to the trade account would have been small compared with the cost of higher inflation. The July realignment had restored Italy's price competitiveness to the level of mid-1983. The profits and financial situation of industrial firms, particularly large companies, provided them with room for manoeuvre. An improvement in the balance of payments on current account had been evident for some months and could be expected to continue in 1986 in view of the decline of the dollar and the fall in oil prices. A failure to stand firm would have prevented the downward trend in the cost of imported primary and intermediate products from feeding through into domestic prices.

The exchange rate had to be maintained if the improvement on the cost front was to benefit the fight against inflation.

The foreign exchange reserves constituted the first line of defence in their unique role as an instrument for giving the market time to assimilate actual and potential improvements in the balance of payments and price trends. Since the desired change in expectations was slow to materialize, it was decided in mid-January to take action on three fronts, namely to raise interest rates on government securities, to reintroduce the ceiling on the growth in bank lending in lire until June and to require export credits to be financed in foreign currency.

These measures were supplemented by tightening the restrictions on the availability of bank liquidity and, above all, raising its cost, although the effect was partly offset to prevent the flow of funds abroad from placing intolerable strains on the payments system.

Central bank refinancing increased by 5.8 trillion lire in December to stand at nearly 9 trillion lire, but the high level of banks' reserves was more apparent than real. Some of these funds became inaccessible when strikes by Bank of Italy staff closed the clearing accounts at the end of November. Net of borrowing from the central bank, the credit institutions' liquidity was decidedly negative over the month as a whole.

Taken together, these exceptional events strongly affected the monetary and credit aggregates; in particular, figures on the monetary base show an increase of almost 15 per cent between the beginning and the end of 1985. The stringency of the tightening towards the end of the year can be gauged from the rapid rise in short-term interest rates. The average cost of new advances granted by the Bank of Italy in various forms rose by two percentage points between the beginning of November and the end of December and by almost a further point in January, reaching 19 per cent in the case of securities repurchase agreements. Overnight interest rates rose even more sharply.

The measures taken in mid-January had an immediate effect on expectations. The foreign exchange reserves that had been sold during the crisis were repurchased with no gain to traders.

The improvement in the general economic climate made it possible to resume the reduction in interest rates at the end of February. From March onwards, the decline spread from short and very short-term rates, where the increase had been most pronounced, to longer-term government securities.

Three one-point reductions in the discount rate and the rate on advances were made on 21 March, 24 April and 26 May, bringing both rates down to 12 per cent.

The yield at issue on twelve-month Treasury bills fell from 13.35 per cent at the beginning of February to 10.96 per cent in the most recent auction; that on four-year Treasury bonds decreased from 13.33 to 10.33 per cent on the current issue. The banks' net liquidity gradually recovered, becoming positive in April, owing partly to the resumption of inflows of capital from abroad. The constraints imposed by the lending ceiling sharply curbed the speculative element in lending in lire, which was brought back to the level considered appropriate for financing the projected growth in economic activity.

In April the decline in bank interest rates resumed, with deposit rates falling more markedly than lending rates, which had decreased by 2.3 points during 1985 in the wake of the fall in money market rates. The restrictive measures taken in January had caused a rise of almost one point; this was reversed and the downward trend set in again.

With the foreign exchange crisis over, Italy was able to arrive at the realignment of EMS central rates, which had been requested by France on 4 April following the French parliamentary elections, in a satisfactory monetary and foreign exchange condition free of immediate strains.

The decision to pitch the central rate of the lira mid-way between the appreciating Deutschemark and the depreciating French franc was the most appropriate way of reconciling the two objectives of reducing inflation and restoring balance-of-payments equilibrium. It was consistent with the policy followed during the exchange crisis at the end of 1985, and its validity was confirmed by the behaviour of the lira in the foreign exchange markets and by the inflow of reserves.

A week after the realignment, the restrictions on capital movements that had been imposed in January were removed and new measures were taken to liberalize external financial transactions.

On the inflation front, expectations turned downwards, and were reinforced month after month by the actual inflation data. The wholesale price index declined in both February and March, so that it now stands at the level of twelve months ago. The fall in raw material prices has not yet carried over into the trend of manufactures prices, which seems so far to reflect greater concern for profitability than competitiveness; in March the prices of manufactures were 1.4 per cent higher than in December and 6.1 per cent above the level recorded in March 1985. The slowdown in the cost of living has resumed; after a long pause at 8.5 per cent, its twelve-month rate of increase fell to 6.3 per cent in May.

In February the trade balance began to reflect the decline in the lira prices of oil and oil products. The surplus on trade in non-energy merchandise also increased. Economic activity is expanding, sustained by domestic demand, and there are signs of a recovery in fixed investment following the pause in the second half of 1985.

The size of the state sector borrowing requirement remains the principal cause for concern. Over the first four months of 1986 it amounted to 40 trillion lire, as against 38 trillion in the same period of 1985. To cover new financing needs and renew maturing securities, government issues will have to average 32 trillion lire a month for the rest of the year. Should even a tenth of that amount fail to be subscribed, the consequent Treasury drawings on its overdraft with the Bank of Italy would cause bank liquidity to approximately double, once again raising problems of monetary control.

The return of normal liquidity conditions and market sales of securities to cover the state sector borrowing requirement made it possible to cut the twelve-month rate of expansion in the monetary base to 10.3 per cent in January and 9.4 per cent in April. Though the growth in the money supply and credit to the corporate sector accelerated in April, it remained in line with the targets.

Monetary policy continues to have little room for manoeuvre. Financing a rapid acceleration in the growth in economic activity could come into conflict with the present trend of the public sector borrowing requirement. Monetary and credit aggregates will continue to be monitored closely, especially during the phasing-out of the ceiling on lending, to permit prompt correction of any excessive expansion.

An evolving financial system

The Italian financial system is undergoing a transformation that both mirrors similar developments abroad and reflects features peculiar to the Italian economy.

The transformation started with the money market. Its modernization, which began in the mid-seventies, created the technical conditions for more effective monetary and exchange rate policy and more diversified financing of the budget deficit. Participation in the European Monetary System involved a tightening of domestic monetary and credit policy.

Firms have come under strong pressure to implement rigorous reorganization programmes to regain their vitality. The conflict between the growing volume of resources absorbed by the public sector and the need to restore price stability and prevent unsustainable balance-of-payments deficits was a contributory factor in the rise in real interest rates to a very high level.

The imbalance in the state sector's finances has its roots in the deficit net of debt interest, which rose from 6 to 7 per cent of national income in 1985. The very real difficulty of reducing this deficit sometimes leads to schemes being conjured up for cost-free adjustment of the public finances. Underlying these schemes is the idea that it is sufficient to reduce the portion of the deficit corresponding to the interest burden.

Determined efforts to curb the interest burden will, of course, have to continue, but the problem of public finances will not be solved unless the flows causing the budget deficit to expand are stemmed at source. Adjustment will require concurrent action to curb both components of the deficit.

When proposals for compulsory reductions in interest rates are put forward, it appears to be forgotten that the amount of savings the state can attract to finance its deficit spending is not fixed but varies with the yield and risk conditions offered. If the government uses its power of fiat to worsen these conditions, or provokes fears that they will worsen, it makes borrowing more difficult and in the long run more costly.

The government's financing needs are now so large that such instruments as the banks' securities investment requirement have also been blunted. Even on the unrealistic assumption that banks had to invest all new deposits in government securities, only a small part of the borrowing requirement would be covered. For the bulk of its financing needs, the government would still have to turn to a market reeling from the effects of the introduction of the requirement.

The ownership of government securities is very widely spread. The number of custodian accounts households have with banks runs into millions. The value of these holdings tends to be small: at the end of 1985 more than 60 per cent of such deposits with some major banks were worth less than 20 million lire and the average did not exceed 35 million. In addition, the share of government securities held by investment funds and portfolio management services is expanding rapidly. The watchfulness of households and the expertise of fund managers make the market react rapidly to changes in economic advantage.

The Bank of Italy is committed to encouraging the adjustment of interest rates as conditions in the economy change. Both constant dialogue with the Treasury and close collaboration with the banks are fundamental to the achievement of this objective. Over the years the forms of cooperation developed with the major banks — without prejudice to decision-making autonomy — have stabilized the demand for government securities at issue and helped to broaden and steady the secondary market.

Encouraged by high real interest rates, households have expanded their financial investment in recent years and diminished their purchases of real assets, especially housing. Firms have reorganized their operations and restructured their finances, reducing their reliance on external resources.

Although these basic trends persisted last year, new attitudes also emerged. Households began to diversify their financial wealth and firms, especially those of medium and large size, showed greater interest in share issues as a means of raising funds.

The stock exchange was the meeting point of the new attitudes of firms and households. The improvement in firms' current and expected profits together with the better macroeconomic outlook helped trigger a rapid rise in share prices. The index doubled in 1985 and doubled again in the first part of this year before fluctuating wildly in the last few days.

While the direct relationship between the Treasury and savers has been built up over a period of ten years, with the supply of securities tending to exceed the demand, the link between firms and savers has been re-established in a very short space of time, with the demand for shares running ahead of the supply. In 1985 the latter was boosted by share issues of listed companies amounting to nearly 5 trillion lire, by the flotation of new companies and the sale, above all by groups in the public sector, of substantial blocks of shares in excess of those needed to maintain control. This, however, fell short of the rise in demand, attributable notably to investment funds and portfolio management services. The funds have raised 35 trillion lire in less than two years of operation and have invested about one fifth of this in the equity market, but in the early months of this year they became more cautious in the face of the continuous rise in share prices.

The business of the investment funds is subject to statutory and other constraints designed to ensure proper management and risk diversification but not to prevent the danger of over-rapid growth. The Bank of Italy is responsible for seeing that these constraints are respected. Funds' operational policies are the responsibility of their management companies. A farsighted approach, especially for funds that invest in shares, requires a medium-term strategy that will result in consistent policies not only for investment but also for fund-raising.

The prolonged boom in share prices has encouraged listed firms to make large new issues. In the first four months of 1986 these amounted to 3 trillion lire and others totaling over 4 trillion have been approved. There is also scope for sustaining the supply of shares through further partial privatization of state-controlled companies. Credit institutions will also have to make a significant contribution by advising businesses to seek stock market listing when their prospects and size are adequate. Merchant banking, in which some institutions are already allowed to engage, therefore needs to be developed rapidly within a suitable regulatory framework.

The rationalization of market structures, initiated in the last few years with the automation of data processing and the centralized administration of government securities, has continued with the preparation of a book-entry system that will eliminate the physical transfer of certificates in clearing houses. A similar advance will be possible for non-government securities once Parliament removes the legal obstacles to their centralized handling by the body set up for this purpose, Montetitoli. This will not be sufficient, however, unless listed companies and banks rapidly make the preparations needed to exploit the service to the full. At present, the use made varies considerably from one bank to another and is generally small. In the meantime, a non-interest-bearing deposit of 30 per cent of the value of securities not delivered when due has been introduced with the aim of limiting the movement of provisional certificates of title issued by banks and ensuring more orderly settlements.

An efficient capital market helps to improve the allocation of resources and makes it easier for firms to raise funds. Other things being equal, it makes capital cheaper and permits a larger volume of investment to be financed. This is why the shortcomings from which it still suffers need to be eliminated.

The same reasoning holds for the reform of exchange controls and the removal of the constraints on financial transactions with non-residents that had to be imposed in the past. Today, in a situation in which it is proving difficult to achieve the coordination of national policies made necessary by the greater mobility of capital compared with goods and services, liberalization is not without risk, especially for an economy that is still adjusting. Nonetheless, we are determined to follow this path.

The combined behaviour of the Treasury, households and firms is modifying the traditional role of banks. A growing share of saving is being invested in non-monetary instruments; whereas money accounted for over 65 per cent of the total flow of financial assets in 1980, it now accounts for about 40 per cent. The role of the specialized businesses that stimulate and channel flows of savings is growing and competition in the markets is intensifying.

The banking system is reacting to these developments. To a greater or lesser extent all the banks are expanding the range of services they supply and diversifying their activities.

Payments services are particularly suited to the widespread application of informatics. The advance of computers and telecommunications has made data transmission networks an indispensable infrastructure. In view of the leading role they play in the payments system, banks are in a position to exploit all the opportunities offered by the development of technology. A great deal has been done, but there appears to be a need for a quantum leap in both the way and the amount the new settlement systems are used; this calls for fuller utilization of existing systems rather than additional investment in equipment.

Technological innovations are encroaching on the functions of the traditional banking establishment, to the point of replacing it in some operations. The importance of branches is tending to decline and banks' growth strategies are becoming increasingly diversified and flexible. Partly in the light of these developments, credit institutions will be allowed greater latitude once the forthcoming branch plan has been implemented. This new approach has already been adopted in the partial liberalization of branch transfers.

Another way banks can diversify their activities is by setting up legally separate and functionally specialized organizations. The creation of multi-function banking groups is in line with the tendency to decentralize corporate structures that can be seen in other sectors and countries. This enhances the banking system's flexibility and its ability to adapt to the changing needs of the economy, but accentuates the interdependence between companies and sectors, thereby increasing the danger of crisis situations spreading.

With the removal of the ban on the establishment of new credit institutions, the question of how desirable and possible it is to separate banking from industry has come to the fore again. The large proportion of public credit intermediaries in Italy attenuates the problem, but does not eliminate it entirely. On several occasions I have called attention to this issue, which is of more immediate concern today in view of the high level of firms' liquidity. The moral suasion the central bank can exercise may prove insufficient to prevent potentially dangerous situations from developing. A rigorous statutory separation of ownership is feasible, as the example of the United States shows. At all events it is necessary to safeguard banks' independence of their customers in their operations.

Further disintermediation and fiercer competition did not prevent banks from recording generally good results last year and strengthening their capital bases. Notwithstanding a narrowing of the interest margin, the profitability of the banking system was unchanged. The rise in operating expenses was curbed and this was accompanied by a substantial increase in the volume of business per employee. Banks recorded a further increase in their capital and reserves, which rose in relation to customer deposits from 9.9 to 10.6 per cent.

Bad debts increased to 6.2 per cent of total _loans and to nearly one third of capital and reserves, but the pace of the increase was slower. Even though Italian banks' exposure to the most heavily indebted developing countries accounts for a smaller proportion of their foreign lending than the average of the industrial countries, an increase in their provisions appears advisable. To this end it is worth examining the case for such provisions to receive special fiscal treatment along the lines of the arrangements made in other countries.

The positive results achieved by the banking industry in 1985 must not blind us to the difficulties facing a sector that is crucial to the rest of the economy and which will have to adapt and reorganize on a vast scale. Increasing competition is spurring change but it also entails greater corporate risk. Not all banks are equally well placed to succeed. The weaker ones will have to resolve their problems, perhaps even by merging with other banks. The nature of banking requires the evolution of the system to proceed without jeopardizing its overall stability.

By reorganizing their own operations, banks will be able to extend their traditional central role to the modernization of the financial sector as a whole. In this far from easy task they enjoy the full support of the Bank of Italy.

Italian banking law: its permanent features and development

Italian banking law comprises a central core, the Banking Law proper as set out in Decree Law 375 of 1936 and subsequent amendments, and layers of other laws regarding particular categories of banks or specific intermediaries. This stratification of regulations means that a comprehensive and up-to-date presentation of banking law would be valuable; the Bank of Italy intends to promote this aim by publishing a codified edition in the near future.

The fiftieth anniversary of the promulgation of the Banking Law is an additional reason for reflecting on the legal and institutional forms of credit activity. The fact that the order established half a century ago has successfully weathered the profound changes in Italy's economic, financial and banking structures can be attributed to the 1936 Banking Law having identified and adopted the basic principle governing the defence of savings and entrusted the latter's protection to a group of flexible and effective institutions. Several other countries can be seen to have adopted a similar approach in the legal and institutional reforms that they have either already implemented or are preparing.

It is worth briefly recalling these principles and institutions. Because it links a vast number of economic agents over time on a fiduciary basis, financial intermediation — and banking, its nucleus — constitutes a system and involves risks requiring forms of prudential control and a policy for its structure. A correct allocation of resources requires credit institutions to act independently of the other sectors of the economy. The legislative framework within which they operate allows the authorities responsible for governing credit to intervene promptly and flexibly with administrative measures. The exercise of control is entrusted to a single technical body endowed with operational autonomy.

Events over many years and reflection on their economic significance have led to the reinstatement of the view that credit institutions are enterprises that invest and risk their capital, whatever its origin; that this capital is a small fraction of their total resources; that their business is conducted in conformity with decisions for which the directors bear responsibility; and that their basic features are unaffected by whether they are publicly or privately owned.

The development of this view was neither linear nor without its uncertainties. With the spread of investment incentives linked to credit, institutions that had been set up to support the growth of the economy in accordance with market principles were made to operate in a context where priority was given to public aims, thereby impairing the autonomy of management organs in arriving at their decisions. The mistaken approach of bending credit to serve planning policy aims caused lending to some sectors to exceed the amounts consistent with the principle of risk diversification. The ensuing damage affected the institutional order as well as intermediaries' capital. In the second half of the seventies the crises in some large medium-term credit institutions that the rise in oil prices helped to trigger brought this phase to an end.

In recent years there has been a change of course. Legislation is again being based on criteria that enhance the autonomy and responsibility of directors and make the framework for operations more certain. The practice of intervening on a piecemeal, case-by-case basis that was segmenting and ossifying the system has been abandoned. Parliament has approved laws of a general nature that supplement the Banking Law and enhance some of its provisions.

In 1981 the supervision of the medium and long-term credit institutions was put on a uniform regulatory basis and binding restrictions were imposed on their risk concentration. In the same year the Treasury Minister issued directives on publicly-owned banks that confirmed their freedom from external influence and their nature as enterprises exposed to competition. They also provided that the operations of these banks may not be subjected to special restrictions and that they can strengthen their capital bases by raising funds in the market.

It was also felt necessary in this period to strengthen the supervision of banks. This need was recently translated into legislation. Law 281/1985 regulates the identification of the owners of bank shares, giving substance to a principle embodied in the 1936 Banking Law, and provides instruments for revealing potential conflicts of interest obscured by the interposition of nominees. Law 114/1986 implements the Community directive on supervision on a consolidated basis. It empowers the Bank of Italy to obtain information directly about banks' subsidiaries and makes elusion of supervisory controls a penal offence. Parliament is also examining a bill to apply uniform sanctions to banks of all kinds whose lending behaviour promotes the interests of third parties at the expense of the bank's.

The law implementing the Community directive on freedom of entry to the credit market reaffirmed the entrepreneurial nature of banks and formally introduced the "fit and proper person" criterion in the choice of directors.

In addition to these legislative changes, the exercise of the regulatory powers assigned to the credit authorities has been revised. The instruments and procedures of banking supervision have been directed more to increasing competition and enhancing intermediaries' decision-making autonomy.

This approach has been adopted in the Bank of Italy's supervisory activity regarding branches, geographical restrictions on operations, changes in statutes, the raising of capital in the markets and derogations from operational limits. Procedures have been streamlined and the number of authorizations granted by the Supervision Department in relation to individual loans has been reduced by nearly two thirds.

Experience over the years has highlighted the viability and resilience of the Banking Law. These features will continue to make it possible to guide the development of the Italian financial system and the updating of regulations in accordance with the requirements of an open industrialized economy. In the immediate future, intervention will concern primarily three major areas: revision of the regulations governing some sectors of banking; financial innovation; and the internationalization of banking.

Revision of the sectoral regulations appears particularly desirable for savings banks and special credit institutions. The recent reform of savings banks' statutes has prepared the ground for them to use a greater variety of capital-raising instruments, undertake a wider range of operations and clarify the relations between their governing organs. The development of savings banks is hindered by some regulations designed for purposes that have ceased to be relevant and are incompatible with the requirements of competitive banking markets. A comprehensive new law would allow a broad legal framework to be drawn up, leaving the detailed regulations to be established in secondary legislation and the savings banks' own statutes.

The environment in which the special credit institutions operate has changed in many respects over recent years. The costs and dangers of excessive borrowing convinced firms to improve the balance between their equity and loan capital. The shortening of investment time horizons in response to both technological progress and the more pronounced variability of economic conditions has often resulted in the demand for finance being in the no man's land between special credit institutions and banks, thereby highlighting the problem of the relationship between short and longer-term credit. The structure of the Italian credit system rests on the specialization of intermediaries according to the maturities of their operations. If this principle is to be respected, both the short-term lending of the special credit institutions and the medium-term lending of banks will need to be kept within consistent bounds. It will also be necessary to reduce the disparities in the limits on different banks' direct and indirect lending beyond the short term.

The large industrial credit institutions are moving towards a multi-product model, though their principal object remains the financing of firms' growth. Some of these institutions are extending their operations to include the underwriting and placing of corporate securities. The changes that are taking place suggest, firstly, that the ownership of these institutions should be enlarged, with the aim of broadening their strategies, strengthening their capital bases and giving greater play to their assessment by the market; and, secondly, that the extent of state participation in their capital should be reconsidered. The smaller industrial credit institutions also have to decide on changes to their ownership structures and the desirability of mergers. Both these paths could be taken with the aim of enhancing their potential.

The other special credit institutions appear to be hampered by legal restraints on the operational and geographical scope of their business. To some extent these reflect market conditions that have now changed. New guiding principles will have to be formulated, in part by enlarging and unifying the sectors in which these institutions are authorized to operate. Here again, it may well be appropriate to employ secondary legislation, which would also allow the technical forms of these institutions' fund-raising and lending to be modified rapidly.

In recent years financial innovation has been spurred by a wide variety of factors: the explosion of domestic and international debt; exceptionally high and variable interest rates; wide fluctuations in exchange rates; incentives to circumvent constraints; the revision of regulations governing intermediaries; and the opportunities offered by computers and telecommunications. The creation of new instruments, operators and markets is spreading from the world's leading financial centres to the rest of the industrial countries.

Techniques have been developed for unbundling the risk, liquidity, yield, currency denomination and maturity features of financial instruments, which are then packaged so as to be separately negotiable or else reassembled in innovative forms leading to the creation of new securities. A growing share of intermediation now flows through securities markets with a corresponding increase in the share of total intermediation in the form of negotiable instruments.

Analysis of these developments, to which a recent study promoted by the central banks of the Group of Ten countries has contributed, has revealed the benefits of such changes, but also their dangers. In the short term, innovation improves the working of markets, expands the range of instruments available, intensifies competition and tends to reduce transaction costs.

On the other hand, innovation puts the stability of the system at greater risk since it tends to blur the boundaries between the various kinds of intermediary, compound the difficulty of assessing commitments, and lower the quality of assets by allowing prime borrowers greater scope to tap markets directly. We are therefore again faced with the need — inherent in the nature of supervision — to reap the benefits of the new while averting the threat of instability it entails.

In my remarks last year I drew attention to the problems that innovation was already creating for the Italian regulatory and supervisory framework. The network of debtor and creditor positions that make up financial markets is becoming more intricate and is crossing the institutional boundaries between credit institutions and other financial intermediaries.

The connection between raising funds and granting credit is inherent in the notion of credit institutions, which are subjected to specific and particularly thorough controls. This approach, however, fails to encompass operators whose business does not involve such a connection because it is based on only one of the terms. The activities of these operators also need to be regulated and subjected to prudential controls, though these may differ from those applied to credit institutions, or at any rate be less severe.

The introduction of forms of prudential control on non-bank businesses does not remove the substantial differences distinguishing them from credit institutions. Even when their supervision is assigned to the central bank, as in the case of investment funds, they do not have access to lending of last resort. This needs to be understood both by these businesses, which are responsible for the management of financial resources, and by savers, who must be aware that the value of their investments is variable and depends on market developments.

Italian banks have been expanding their foreign business for many years, initially by financing an increasingly open economy and subsequently through the creation of an extensive network of branches and subsidiaries in the leading international financial centres. Of banks' total volume of business, the foreign component — including foreign currency loans to residents — accounts for about a quarter, with foreign establishments contributing about half this amount.

The interpenetration of national markets has led to the emergence of the internationally ramified bank as a new object of supervision. The broader scale of operations requires parent banks to strengthen their internal decision-making and control functions adequately. The supervisory authorities in the major countries have established procedures for mutual cooperation with the aim of making supervision more effective and ensuring that banks are competing on an equal footing. The authorities act on two levels: bilateral control over individual credit institutions through exchanges of information and agreements on how interventions are to be made; and multilateral drafting of regulations and criteria for the supervision of banks' foreign establishments.

The internationalization of banking should be given new impetus by the Single European Act and the White Paper on the Community market, which also foresees the unification of the capital and financial services market by the end of 1992 through a series of directives. Agreements between supervisory authorities and the drafting of legislation, in which Italy participates actively in the Community, will continue to stimulate and orientate the development of the legal framework of financial intermediation. The past has shown that Italy's banking law has considerable capacity both to evolve and to incorporate experience acquired at the international level.

The objectives of economic policy

A modern and efficient credit system is essential for stability and growth. Its contribution will steadily increase as the economy it serves begins to record new successes, measured by the ultimate yardstick of growth in national income and employment.

The public finances are beset by deep-rooted causes of instability. There are still weaknesses and contradictions in the sectoral and geographic distribution of resources, even within the industries that have adjusted the fastest.

Awareness of the need to complete the task of restoring economic equilibrium has grown and has recently been translated into economic policy objectives set forth in important government policy documents.

In recent years, restructuring has been taking place in industry and the parts of the services sector most closely associated with it, although it cannot be said that the process has yet been completed. The economy is a single entity, however, and part of the cost of adjustment has fallen on the budget. It is now time to resolve the problems of the public finances; if this is not done, all that has been achieved so far will be at risk, precisely because the economy is indivisible.

Numerous measures have already been taken, some of them of substance, but they are designed solely to contain the explosion in expenditure implicit in existing legislation. The ratio of public expenditure to GDP has not yet begun to come down.

Implementation of a broadly based policy is hampered by the repercussions that the nature and scale of the necessary measures would inevitably produce in various sections of society. The costs of such a policy would be felt immediately, and in terms of the social welfare function they may appear higher than the potential benefits to the economy as a whole, some of which would not emerge until later.

The depreciation of the dollar and the fall in oil prices are now creating favourable conditions that may reduce these costs. At the same time, the uncertainty about how long the improved external conditions will last accentuates the need for prompt action to achieve the economic policy objectives that have been set.

The improvement in Italy's terms of trade in relation to their average for 1985 is currently estimated to be in excess of 10 per cent, a figure that indicates the scale of the additional resources that are potentially available. Appropriately, priority in allocating the immediate benefits of cheaper oil has been given to sustaining competitiveness, reducing the budget deficit and maintaining the incentive to save energy.

The shift in the terms of trade provides greater latitude for domestic demand to increase without incurring further deficits on the current account of the balance of payments and increasing Italy's already substantial foreign debt; it also creates room for higher investment.

The increase in domestic demand may be close to 4 per cent in real terms in 1986 and exports are likely to expand by a similar amount. National income may rise by about 3 per cent and employment by around 200,000. Despite the fact that domestic demand will grow more strongly than output, the fall in import prices will allow a current account surplus to emerge and will accelerate the decline in inflation.

Realization of the favourable prospects for 1986 will not wipe out the legacy of years of imbalance in the public debt, in industrial capacity, in the labour market and in the competitiveness of the entire economy.

Industrial capacity stagnated or even contracted during the first half of the eighties; in 1985 it was still below the 1980 level. The generation of profits in industry and the improved prospects for growth may trigger an expansion in the industrial base. Since the end of the seventies, the need to improve productivity has meant that the bulk of investment has been made in the centre and north of the country. If the expansion of capacity occurred mainly in the existing industrial centres, the south of Italy would be placed at a further disadvantage. The nation as a whole would suffer serious harm if the additional resources of capital and labour were distributed unevenly across the country.

The shift in the terms of trade cannot permanently alleviate the external constraint. The balance of trade in volume terms is continuing to shift to Italy's disadvantage, creating the danger of substantial trade deficits should the movement in the terms of trade be reversed. Moreover, if the elasticity of imports with respect to GDP continues to be as high over the medium term as it has been in recent years, an increase in exports in line with the expansion in world demand will not prevent the external constraint from again impeding growth. Sustained development therefore requires a significant expansion in domestic supply and a change in its composition coupled with efforts to achieve greater competitiveness and efficiency throughout the economy, including the sectors that are shielded from international competition.

All the proposed public finance measures and the economic policy guidelines set out in the documents mentioned above are directed towards solving these problems; their implementation is now a matter of urgency.

The guidelines laid down for fiscal policy are designed to hold the growth in current expenditure to the rate of inflation, increase capital expenditure in line with nominal GDP and maintain the tax burden at its current level in relation to GDP, though more fairly distributed among the various classes of taxpayer. Efforts to reduce the budget deficit are being concentrated mainly on social security, health care and local authority finances, reviewing the size and nature of transfers to firms and households and overhauling and strengthening the machinery for monitoring payment commitments and ensuring that revenues are available to finance expenditures.

The Bank of Italy's Research Department has conducted simulations for the period from 1986 to 1988 assuming the implementation of such a fiscal policy, an oil price of between $15 and $20 a barrel and an expansion of about 4 per cent in world trade. The link between international developments and domestic behaviour and policies is close and has a decisive influence on the results, and the underlying assumptions are subject to varying degrees of uncertainty. Hence, exercises of this kind should not be taken as forecasts, but nonetheless they are thought-provoking and may help shape the decisions that have to be made.

Over the three-year period, the simulations indicate an average annual growth of 3 per cent in GDP and nearly 4 per cent in domestic demand, an increase in employment at nearly twice the 1985 rate, broad balance on the external current account and a further slowdown in inflation.

With the state sector borrowing requirement declining in relation to national income, output and investment would be stimulated by improved expectations and the lower interest rates that would become possible. The virtuous combination of economic growth, a smaller interest burden and a reduction in the budget deficit net of interest would bring the expansion in the public debt back under control.

The slowdown in inflation would not, however, eliminate the inflation differential vis-a-vis our competitors; this cannot be cured by external factors, which also apply to other countries. The differential stems from the domestic components of costs; though less powerful than previously, they are continuing to make the prices of Italian products rise faster than those elsewhere.

Even an increase in employment on the scale indicated by the simulations would be insufficient to absorb the full rise in the labour force, which will continue to expand significantly until the early nineties owing to demographic factors and rising participation rates, particularly among women.

To eliminate the inflation differential and achieve a larger increase in employment, fiscal adjustment will have to be supplemented by incomes policy. Expanding employment must take precedence over increasing the incomes of those in work. The reduction in costs deriving from productivity gains and the fall in raw material prices must translate into a slowdown in the prices of manufactures, rather than larger increases in wages and profit margins. The improvement in industrial relations is having a significant beneficial effect; the agreement on employment in the public sector led to reform of the *scala mobile* in the private sector as well and the new wage indexation mechanism will pass on inflationary pressures less rapidly. Administered prices and public service charges must be set at a level that promotes disinflation while curbing consumption, particularly of energy, and encouraging investment to expand the supply of goods and services that are in demand.

Provided they are based on appropriately rigorous criteria, both fiscal policy and incomes policy can be slanted in favour of the economy of the southern regions in order to reduce the regional disparities in economic development and contain unemployment. Substantial government resources have already been allocated for the south under the Finance Law and the laws providing for special measures in favour of firms in the south and incentives for young entrepreneurs; they must now be put to effective use. The hoped-for employment effects will not materialize if the social partners have no confidence in the final outcome and the labour market lacks the necessary flexibility. Investment by small and medium-sized local firms would then be impeded, capital would flow less freely to the south and a brake would be put on the movement of albeit small numbers of unemployed towards the centre and north, where there may be a shortage of labour in the not too distant future.

If action were taken on all these economic policy fronts, the easing of the external constraint and the reduction in the public sector borrowing requirement would allow nominal and real interest rates to come down without this conflicting with a policy for money and credit designed to complete the task of eradicating the inflation that has dominated the Italian economy since the beginning of the seventies. The Bank remains firmly committed to this objective.

Ladies and Gentlemen,

The strategy for restoring monetary stability that I outlined a few years ago was rooted in three fundamental principles: a rigorous management of the money supply and the exchange rate, incomes behaviour that paid due attention to macroeconomic compatibility, and the restoration of the budget as an instrument of economic policy. Underlying this formulation was our awareness of the limitations of monetary policy when it has to fight inflationary pressures singlehanded and our conviction that only by taming inflation would it be possible to engender a rate of growth that would have a significant impact on unemployment.

We have dosed the severity of monetary and exchange rate policy in accordance with these criteria, trusting in a pragmatic use of such instruments rather than in mechanical rules, whose limitations have been revealed by the experience of other nations.

The effectiveness of this method has been demonstrated by the fact that it succeeded in curbing inflation during the protracted period of dollar appreciation and unfavourable terms of trade.

Significant objectives on the long road back to monetary equilibrium are now within reach; inflation is receding towards levels only experienced during the years of stability, which were also the years of fastest growth.

External factors are accentuating the slowdown in prices, just as it was external factors that contributed powerfully to the original outbreak of rapid inflation. It is impossible to predict how long the present favourable circumstances will last. The task before us is not just to reap the immediate fruits but to take advantage of the situation to advance at less sacrifice towards the solution of our underlying economic problems.

We have never been among those who considered surrender to inflation unavoidable, and by our actions we have opposed that attitude. Today, an objective assessment of the progress made and of the more encouraging outlook will hopefully avert the danger of euphoria.

Italy's closer involvement in the economic and monetary policy coordination of the leading industrialized countries, which was agreed at the Tokyo Summit, confirms the progress we have made, but at the same time it commits us to renewing our efforts to complete the adjustment of our economy and return to stable growth that would more fully realize the country's potential.

The creation of jobs demanded by the scale of unemployment and its concentration among young people requires an expansion in the industrial base. The change in relative prices to the benefit of manufactures is creating favourable conditions on the cost front; it is primarily the responsibility of firms to translate these into a slowdown in prices rather than increases in nominal incomes, into real investment rather than purchases of financial assets. The credit system must feel that its part in this endeavour is not only to perform the essential task of screening projects seeking finance but also to increase its own efficiency.

The budget must be overhauled and made more flexible if investment is gradually to strengthen without encountering resource constraints. The restoration of sound public finances is rightly at the heart of government policy. The need for action is now urgent in view of the trends that are under way. The increase in the public debt is continuing to outstrip the rise in national income. Rather than falling, the deficit net of interest payments increased in 1985. The reduction in the interest burden made possible by the slowdown in inflation will count for little if it is replaced by other items of expenditure.

A budget that has been reduced to normal proportions in relation to national income, modified as regards the composition of expenditure and restored to its function as an instrument of economic policy is necessary to guarantee stability, balanced growth and social progress.

STATISTICAL APPENDIX

LIST OF TABLES

GOODS AND SERVICES AND DISTRIBUTION

(billions of lire

	Final domestic consumption			Gross fixed capital formation	Variations in stocks and statistical discrepancies	Exports			Total of sources and uses	Imports		
	Households	Collective consumption (1)	Total			Goods fob	Services (2)	Total		Goods cif	Services (3)	Total
					Uses							
1976 . . .	99,504	24,049	123,553	31,396	5,666	31,210	4,675	35,885	*196,500*	37,240	2,603	39,843
1977 . . .	120,329	29,965	150,294	37,203	3,477	40,020	5,608	45,628	*236,602*	43,120	3,399	46,519
1978 . . .	139,902	36,381	176,283	41,494	2,940	47,563	6,533	54,096	*274,813*	48,638	3,921	52,559
1979 . . .	169,396	45,235	214,631	50,927	6,545	59,955	8,402	68,357	*340,460*	65,484	4,778	70,262
1980 . . .	212,488	57,307	269,795	67,016	17,648	66,776	10,360	77,136	*431,595*	86,698	6,154	92,852
1981 . . .	254,661	75,293	329,954	81,149	4,532	86,085	12,207	98,292	*513,927*	105,113	7,235	112,348
1982 . . .	299,470	89,806	389,276	89,560	4,866	99,286	14,524	113,810	*597,512*	117,939	9,089	127,028
1983 . . .	343,981	106,943	450,924	96,766	−893	110,642	16,008	126,650	*673,447*	123,825	9,778	133,603
1984 . . .	389,136	122,354	511,490	112,055	4,963	129,297	19,526	148,823	*777,331*	150,129	12,083	162,212
1985 . . .	434,100	136,870	570,970	124,850	4,897	150,070	24,142	174,212	*874,929*	175,039	15,047	190,086

Source: Istat.
(1) Consumption of general government and private social security institutions. – (2) Net of final consumption in Italy by non-residents, which is included, however, in final domestic

USE OF INCOME AND

(billions of lire

	Final national consumption							Gross capital formation
	Households			Collective consumption			Total final consumption	
	Domestic	Net tourism	Total	General government	Private social security institutions	Total		
1976	99,504	−1,993	97,511	23,133	916	24,049	*121,560*	37,062
1977	120,329	−3,324	117,005	28,991	974	29,965	*146,970*	40,680
1978	139,902	−4,211	135,691	35,257	1,124	36,381	*172,072*	44,434
1979	169,396	−5,515	163,881	43,890	1,345	45,235	*209,116*	57,472
1980	212,488	−5,927	206,561	55,636	1,671	57,307	*263,868*	84,664
1981	254,661	−6,437	248,224	73,297	1,996	75,293	*323,517*	85,681
1982	299,470	−8,468	290,984	87,329	2,477	89,806	*380,790*	94,426
1983	343,981	−10,582	333,399	104,143	2,800	106,943	*440,342*	95,873
1984	389,136	−11,139	377,997	119,214	3,140	122,354	*500,351*	117,018
1985	434,100	−11,997	422,103	133,375	3,495	136,870	*558,973*	129,747

Source: Istat.

OF GROSS DOMESTIC PRODUCT AND INCOME
at current prices)

Gross domestic product								Transactions with the rest of the world			Gross national disposable income	Net national disposable income
Gross operating surplus (4)	Compensation of employees			Net indirect taxes			GDP	Net compensation of employees	Net property & entre-preneurial income and other items	Net indirect taxes to the EEC		
	To resident workers	To non-resident workers	Total	To general government	To the EEC	Total						
	Sources											
58,167	86,845	108	86,953	11,647	−110	11,537	*156,657*	476	−991	110	*156,252*	140,459
68,372	106,364	137	106,501	15,063	147	15,210	*190,083*	810	−905	−147	*189,841*	170,399
80,956	124,148	167	124,315	16,740	243	16,983	*222,254*	1,119	−1,329	−243	*221,801*	199,437
102,454	148,719	176	148,895	18,457	392	18,849	*270,198*	1,373	19	−392	*271,198*	244,764
128,302	183,919	235	184,154	26,168	119	26,287	*338,743*	1,488	110	−119	*340,222*	307,556
146,480	225,209	335	225,544	28,834	721	29,555	*401,579*	1,635	−2,677	−721	*399,816*	359,149
172,175	263,895	456	264,351	33,411	547	33,958	*470,484*	2,079	−4,974	−547	*467,542*	418,633
188,082	304,675	497	305,172	46,765	−175	46,590	*539,844*	2,296	−5,096	175	*537,219*	481,283
223,363	339,226	571	339,797	52,117	−158	51,959	*615,119*	2,543	−5,825	158	*611,995*	*549,036*
251,518	*376,735*	*728*	*377,463*	*55,653*	*209*	*55,862*	*684,843*	2,531	−6,635	−209	*680,530*	611,400

consumption. – (3) Net of final consumption abroad by residents. – (4) Net of imputed bank services.

FORMATION OF CAPITAL
at current prices)

Gross national saving								Gross national disposable income	Net lending or net borrowing (–) of the nation	
Transactions with the rest of the world: balances							TOTAL		Total	of which: balance of capital transactions
Goods and services	Net tourism	Net income from employment	Net income from capital	Net indirect taxes	Transfers	Total				
−3,958	1,993	476	−1,070	110	79	−2,370	*34,692*	*156,252*	−2,343	27
−891	3,324	810	−1,230	−147	325	2,191	*42,871*	*189,841*	2,175	−16
1,537	4,211	1,119	−1,257	−243	−72	5,295	*49,729*	*221,801*	5,261	−34
−1,905	5,515	1,373	−782	−392	801	4,610	*62,082*	*271,198*	4,553	−57
−15,716	5,927	1,488	−996	−119	1,106	−8,310	*76,354*	*340,222*	−8,291	19
−14,056	6,437	1,635	−4,069	−721	1,392	−9,382	*76,299*	*399,816*	−9,225	157
−13,218	8,468	2,079	−5,885	−547	1,411	−7,674	*86,752*	*467,542*	−7,412	262
−6,953	10,582	2,296	−6,515	175	1,419	1,004	*96,877*	*537,219*	1,181	177
−13,389	11,139	2,543	−7,565	158	1,740	−5,374	*111,644*	*611,995*	−5,084	290
−15,874	11,997	2,531	−8,421	−209	1,786	−8,190	*121,557*	*680,530*	−7,802	388

Table a 3

LABOUR COSTS PER UNIT OF OUTPUT AND VALUE ADDED PER WORKER, BY SECTOR

Sector	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
					Labour costs by unit of output *(Current lire per thousand lire of value added at 1970 prices)*					
Market goods and services	*1,562.6*	*1,859.0*	*2,092.8*	*2,345.2*	*2,753.0*	*3,292.8*	*3,888.6*	*4,518.4*	*4,893.9*	*5,285.2*
Agriculture, forestry and fisheries	**1,861.8**	**2,353.6**	**2,669.3**	**2,926.8**	**3,386.4**	**3,974.1**	**4,600.0**	**4,968.8**	**5,475.8**	**5,966.1**
Industry	**1,494.9**	**1,782.3**	**1,999.2**	**2,213.8**	**2,542.5**	**3,039.3**	**3,600.0**	**4,132.7**	**4,297.8**	**4,628.2**
Excluding construction	1,458.9	1,721.0	1,910.5	2,104.1	2,405.8	2,875.0	3,396.7	3,889.3	4,050.7	4,355.2
Energy products	493.7	584.5	642.5	750.0	917.9	1,129.3	1,306.3	1,614.2	1,820.8	2,001.0
Manufactures	1,628.9	1,914.8	2,134.5	2,334.8	2,633.8	3,142.8	3,723.4	4,237.7	4,378.9	4,697.0
Construction	1,677.3	2,106.5	2,484.0	2,834.0	3,325.3	3,960.8	4,737.2	5,479.6	5,704.4	6,232.6
Services	**1,476.9**	**1,744.8**	**1,974.2**	**2,259.6**	**2,760.3**	**3,324.0**	**3,943.2**	**4,688.8**	**5,241.0**	**5,640.9**
Distributive trades, lodging & catering	1,536.7	1,889.8	2,159.4	2,445.0	2,958.5	3,652.8	4,422.2	5,268.4	6,072.3	6,571.4
Transport & communications	1,860.2	2,156.4	2,403.2	2,822.7	3,410.9	4,066.9	4,827.6	5,492.6	5,877.1	6,382.3
Finance and insurance	1,687.0	1,829.1	2,033.8	2,218.2	2,763.8	3,137.2	3,501.2	4,416.5	4,645.6	4,776.9
Miscellaneous services	1,327.4	1,620.8	1,845.9	2,123.5	2,578.1	3,197.1	3,848.9	4,477.0	5,119.5	5,529.5
Non-market services	**2,080.9**	**2,575.1**	**3,110.9**	**3,817.4**	**4,785.5**	**6,209.3**	**7,241.3**	**8,449.7**	**9,564.5**	**10,454.3**
General government	2,090.2	2,589.6	3,137.3	3,862.5	4,861.8	6,340.1	7,397.8	8,655.4	9,799.8	10,720.4
TOTAL	**1,610.6**	**1,929.5**	**2,198.1**	**2,498.8**	**2,967.0**	**3,621.3**	**4,266.4**	**4,967.9**	**5,427.6**	**5,864.0**
					Value added at market prices per worker *(thousands of lire at 1970 prices)*					
Market goods and services	*3,983.5*	*4,053.6*	*4,150.7*	*4,335.5*	*4,490.2*	*4,494.0*	*4,481.7*	*4,476.2*	*4,600.4*	*4,694.0*
Agriculture, forestry and fisheries	**1,705.0**	**1,736.6**	**1,816.7**	**1,978.9**	**2,117.4**	**2,200.0**	**2,272.5**	**2,474.8**	**2,484.2**	**2,517.9**
Industry	**4,227.9**	**4,291.1**	**4,395.5**	**4,634.9**	**4,814.8**	**4,819.3**	**4,794.4**	**4,808.1**	**5,138.3**	**5,304.1**
Excluding construction	4,634.6	4,705.3	4,851.3	5,135.1	5,346.2	5,376.8	5,360.9	5,387.6	5,763.3	5,973.7
Energy products	21,561.4	21,355.3	22,549.7	23,151.0	21,846.2	21,497.5	21,469.4	20,856.4	20,969.2	21,140.2
Manufactures	4,060.0	4,142.0	4,248.2	4,519.6	4,776.9	4,806.1	4,782.6	4,818.5	5,183.1	5,384.1
Construction	2,847.5	2,872.3	2,863.1	2,944.8	3,028.2	3,004.5	2,968.1	2,962.9	3,122.2	3,142.7
Services	**4,788.7**	**4,844.3**	**4,913.5**	**4,995.6**	**5,084.6**	**5,009.5**	**4,925.5**	**4,827.4**	**4,774.3**	**4,803.7**
Distributive trades, lodging & catering	3,330.2	3,377.9	3,452.6	3,535.8	3,625.5	3,560.0	3,482.1	3,384.1	3,345.1	3,355.6
Transport & communications	4,267.5	4,424.0	4,559.1	4,764.7	4,881.8	4,823.8	4,918.7	4,907.9	5,136.5	5,233.9
Finance and insurance	10,708.2	10,593.0	10,729.0	10,975.5	11,075.9	10,948.3	10,516.7	10,721.3	10,897.2	11,594.8
Miscellaneous services	4,421.0	4,420.5	4,391.0	4,381.8	4,399.4	4,330.8	4,218.6	4,087.8	3,931.9	3,926.2
Non-market services	**2,680.0**	**2,675.6**	**2,640.5**	**2,603.9**	**2,614.2**	**2,598.8**	**2,580.1**	**2,578.4**	**2,586.3**	**2,590.1**
General government	2,940.9	2,919.5	2,871.9	2,831.2	2,841.9	2,826.4	2,807.1	2,803.9	2,817.6	2,829.2
TOTAL	**3,774.1**	**3,829.4**	**3,902.3**	**4,048.0**	**4,177.9**	**4,173.4**	**4,155.1**	**4,147.5**	**4,249.1**	**4,325.9**

Source: Istat.

Tav. a 4

INDUSTRIAL PRODUCTION BY ECONOMIC PURPOSE

(indices, 1980 = 100; seasonally adjusted)

	FINAL INVESTMENT GOODS				FINAL CONSUMER GOODS				INTERMEDIATE GOODS				OVERALL INDEX
	For industry	Transport equipment	Multi-sector	Total	Durable	Semi-durable	Non-durable	Total	For industry	For consumer goods	Mixed purpose	Total	
1976	89.2	75.4	57.3	75.6	83.4	90.2	81.1	84.0	83.8	95.5	91.7	84.0	*86.2*
1977	94.2	77.7	60.2	79.3	88.4	90.7	79.9	85.0	86.8	91.2	91.6	85.0	*87.2*
1978	90.6	78.4	72.6	82.1	88.6	82.0	87.3	86.3	85.6	93.8	93.1	86.3	*88.8*
1979	89.1	82.4	88.6	87.7	94.0	94.9	94.3	94.4	91.6	100.4	97.6	94.4	*94.7*
1980	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	*100.0*
1981	101.2	114.5	100.8	103.4	90.7	99.9	102.3	97.4	98.8	100.4	97.4	97.4	*98.4*
1982	88.3	112.7	105.2	95.8	88.8	101.1	103.9	97.6	91.0	99.4	93.7	97.6	95.4
1983	79.5	121.0	110.3	92.6	85.3	92.0	104.7	94.2	86.6	96.0	90.9	94.2	*92.3*
1984	77.7	119.4	126.5	94.4	88.0	94.5	106.0	96.3	87.6	102.6	93.8	95.2	*95.4*
1985	80.3	118.0	144.2	99.2	88.2	92.2	110.8	97.5	86.0	103.5	93.4	94.9	*96.5*
1979 - I	86.4	78.7	81.2	83.1	91.0	90.5	91.0	90.9	86.4	99.2	97.0	96.1	*92.0*
II	84.1	77.0	86.3	83.5	90.5	93.7	93.1	92.5	90.1	96.4	95.1	94.8	*92.0*
III	89.9	83.5	91.1	89.1	93.9	95.0	95.1	94.7	93.1	104.0	98.7	99.1	*95.9*
IV	96.1	90.5	96.0	95.0	100.5	100.3	98.2	99.4	96.9	101.8	100.6	100.4	*99.1*
1980 - I	100.6	100.0	96.3	99.0	106.3	105.0	101.5	103.7	99.6	104.4	103.6	103.3	*102.7*
II	103.0	103.8	100.4	102.3	105.2	104.1	99.3	102.1	101.4	104.5	103.3	103.3	*102.7*
III	98.0	93.7	99.5	97.7	92.6	94.6	98.1	95.7	98.5	93.8	95.3	95.4	*95.9*
IV	98.4	102.5	103.7	101.0	95.9	96.3	101.2	98.5	100.5	97.2	97.8	98.0	*98.7*
1981 - I	103.0	112.0	106.1	105.1	92.2	96.5	99.5	96.6	99.6	98.5	98.2	98.5	*98.9*
II	106.4	116.6	100.9	107.1	92.9	100.2	101.9	98.2	101.5	101.7	96.6	98.6	*99.9*
III	99.8	115.3	99.4	102.4	89.5	101.4	102.9	97.6	98.0	99.8	94.2	96.1	*97.7*
IV	95.5	114.1	96.7	98.9	88.0	101.4	105.0	97.9	96.2	101.6	94.2	96.4	*97.3*
1982 - I	96.5	114.5	105.2	101.3	89.7	103.7	104.1	98.8	96.9	102.6	95.7	97.7	*98.7*
II	90.4	112.0	105.0	96.9	89.3	101.6	102.1	97.3	92.6	97.7	93.1	94.2	*95.7*
III	85.6	112.0	106.8	94.2	88.4	100.3	104.3	97.4	88.1	101.3	91.0	93.2	*94.8*
IV	80.8	112.3	103.7	90.7	87.7	98.7	105.1	97.0	86.5	96.1	87.9	89.8	*92.4*
1983 - I	81.6	113.8	105.5	91.8	85.9	96.7	105.2	95.8	86.0	95.2	87.4	89.2	*91.9*
II	77.2	119.3	108.7	90.6	83.5	91.2	105.0	93.4	85.8	93.5	88.5	89.4	*90.9*
III	79.8	122.3	111.7	93.3	85.9	91.8	102.7	93.6	86.4	95.5	90.7	91.3	*92.4*
IV	79.5	128.5	115.4	94.9	86.1	88.4	106.2	94.0	88.1	99.9	92.7	93.9	*94.1*
1984 - I	78.0	112.1	112.6	92.3	85.6	88.2	103.7	92.8	87.2	100.3	92.7	93.9	*93.3*
II	77.5	116.2	119.2	92.3	88.8	95.6	106.1	96.9	86.3	102.3	94.7	95.5	*95.4*
III	78.2	123.0	130.7	96.1	90.4	95.3	107.5	97.9	89.2	103.7	95.1	96.5	*96.9*
IV	77.2	116.3	143.5	96.8	87.2	98.8	106.8	97.5	87.9	104.0	92.7	94.9	*96.1*
1985 - I	77.8	118.2	148.4	98.5	88.2	92.2	108.3	96.5	83.7	103.6	93.7	94.8	*96.0*
II	80.3	119.6	145.4	99.7	89.6	91.9	111.9	98.3	87.5	104.3	93.7	95.5	*97.2*
III	81.0	113.5	138.9	97.8	86.9	92.5	111.1	97.2	86.7	103.3	92.6	94.5	*96.0*
IV	82.1	120.6	144.1	100.8	88.3	92.4	112.1	98.0	86.0	102.9	93.5	94.8	*96.9*

Source: Based on Istat data.

Table a 5

WHOLESALE PRICES BY ECONOMIC PURPOSE (1)

(indices, 1980 = 100)

	Overall index	Final consumer goods				Final capital goods	Intermediate goods	Foodstuffs (2)	Industrial goods (2)	Industrial raw materials (2)
		Food	Other non-durable goods	Durable goods	Total					
1976	57.1	61.3	53.4	58.0	57.8	58.5	56.2	62.1	55.9	54.0
1977	66.6	72.8	65.5	68.1	69.3	68.0	64.0	72.9	66.0	60.6
1978	72.2	81.6	71.2	74.2	76.5	75.2	68.2	80.6	71.4	64.3
1979	83.3	89.9	80.2	84.6	85.4	84.5	81.4	89.0	81.7	80.4
1981	116.6	114.6	116.7	112.8	114.9	119.4	117.5	115.0	116.0	119.8
1982	132.8	133.4	134.6	125.0	131.9	137.1	132.6	131.9	131.6	136.1
1983	145.7	147.4	153.3	136.4	146.8	155.0	143.2	145.1	146.1	145.6
1984	160.8	161.4	170.4	147.7	161.2	170.2	158.8	157.5	160.7	164.9
1985	172.6	173.4	188.2	158.2	174.6	183.5	169.1	167.3	174.1	175.6
1979 - I	77.7	87.1	75.2	79.3	81.3	80.7	74.3	85.7	76.4	71.6
II	81.3	89.1	77.1	82.1	83.4	83.2	79.2	87.7	79.5	78.1
III	84.7	90.2	81.2	86.3	86.2	85.5	83.4	89.2	83.0	83.5
IV	89.5	93.7	87.0	90.8	90.7	88.6	88.7	93.5	87.9	88.4
1980 - I	95.4	96.8	94.9	94.9	95.7	93.9	95.5	97.0	94.2	96.2
II	98.8	98.4	98.2	98.6	98.3	98.5	99.2	98.1	98.6	99.9
III	101.0	100.7	100.6	101.5	100.8	102.3	100.9	100.2	101.7	100.5
IV	104.8	104.1	106.3	105.0	105.3	105.3	104.4	104.7	105.6	103.3
1981 - I	109.2	107.2	110.6	107.8	108.4	111.4	109.4	108.0	109.5	110.0
II	114.8	113.1	113.9	110.3	113.1	117.6	115.8	113.6	114.2	117.6
III	118.8	115.6	117.7	113.7	116.0	122.5	120.5	116.3	118.0	123.7
IV	123.6	122.5	124.5	116.1	122.0	126.1	124.3	122.2	122.3	127.8
1982 - I	127.6	127.6	127.2	120.4	125.8	130.9	128.4	127.0	125.9	131.7
II	130.2	130.4	129.3	124.1	128.7	135.6	130.4	129.3	129.1	133.4
III	134.4	135.3	137.0	126.1	133.8	138.6	134.0	133.0	133.4	137.8
IV	138.9	140.3	144.9	129.4	139.3	143.3	137.7	138.2	138.1	141.3
1983 - I	141.1	142.8	148.9	132.4	142.4	148.6	138.8	140.6	141.7	140.6
II	143.4	144.5	152.0	135.2	144.7	153.3	140.5	142.0	144.8	142.0
III	146.7	148.8	153.9	137.3	147.8	156.8	144.0	146.3	147.1	146.4
IV	151.6	153.7	158.4	140.6	152.3	161.2	149.3	151.5	150.8	153.2
1984 - I	156.4	157.3	166.3	143.6	157.0	166.0	154.2	154.7	155.9	159.4
II	159.9	161.3	168.8	146.9	160.4	169.2	157.8	157.5	159.4	163.5
III	161.9	162.5	170.9	148.9	162.1	171.2	160.0	158.0	161.9	166.3
IV	165.0	164.4	175.6	151.4	165.0	174.5	163.2	159.6	165.4	170.4
1985 - I	169.5	168.3	182.3	155.1	169.7	179.5	167.5	163.5	170.0	175.4
II	173.2	174.2	188.2	157.9	174.9	182.8	170.1	168.0	173.8	178.1
III	173.1	174.1	189.7	158.8	175.6	184.7	169.1	167.4	175.1	175.6
IV	174.7	176.9	192.5	160.8	178.2	187.1	169.7	170.4	177.7	173.4
1986 - I	173.8	178.8	191.1	163.0	179.1	191.7	166.3	173.1	178.8	164.1

Source: Istat.

(1) The pre-1981-I figures were obtained by dividing the figures of the 1976-based index by the conversion factor linking the 1976 and 1980-based series with reference to the 1980 average. – (2) Based on Istat data.

Table a 6

CONSUMER PRICES

(indices)

	POPULATION AS A WHOLE (1) (1980 = 100)												WORKER AND EMPLOYEE HOUSEHOLDS (2) (1985 = 100)					
		Goods				Other than food & services								Categories of expenditure				
	Overal index	food	non-food	total	Services	clothing & foot-wear	hous-ing, fuel & elec-tricity	furni-ture, furnish-ings, etc.	medical care and health	trans-port & commu-nications	recrea-tion, enter-tainment, educa-tion, & cultural services	other goods & services	Overall index	food	clothing	elec-tricity & other fuels	housing	miscel-laneous expen-diture
1977	64.1	67.7	61.1	64.4	63.4	63.3	55.6	66.7	64.8	64.0	67.7	57.1	33.1	37.1	34.1	22.5	29.6	31.2
1978	71.9	76.4	67.9	72.2	71.1	72.7	60.7	73.5	73.6	69.6	74.5	65.1	37.2	42.0	39.1	25.0	31.9	34.9
1979	82.5	86.5	78.1	82.3	82.9	82.9	74.7	82.9	82.9	80.4	84.3	77.0	43.1	47.7	44.6	29.9	40.1	40.7
1980	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	52.2	54.7	53.2	45.2	47.7	51.1
1981	117.8	116.3	117.1	116.8	120.6	117.1	120.3	118.4	122.8	117.8	115.8	119.8	62.2	64.4	62.6	57.3	55.5	61.8
1982	137.2	135.4	135.6	135.5	141.7	135.9	143.2	136.6	142.6	137.4	132.1	140.4	72.4	74.7	72.4	69.8	64.8	71.9
1983	157.3	152.0	154.7	153.4	167.5	154.4	170.2	154.3	159.2	160.9	155.3	163.7	83.2	84.4	82.2	82.5	77.2	83.4
1984	174.3	165.9	170.8	168.5	189.7	171.9	198.8	169.0	177.3	178.1	172.7	182.1	92.1	92.1	91.1	91.7	95.0	92.0
1985	190.3	180.3	185.5	183.0	209.4	190.4	213.4	184.1	202.5	190.7	189.8	200.9	100.0	100.0	100.0	100.0	100.0	100.0
1979 - I	77.8	82.4	72.4	77.4	78.6	77.9	68.8	78.6	79.4	74.4	79.8	71.4	40.4	45.4	41.8	26.4	38.1	37.7
II	80.6	85.4	74.9	80.2	81.6	80.7	71.2	81.0	81.8	77.9	82.6	74.2	42.1	47.2	43.5	27.1	39.3	39.6
III	83.4	87.6	79.0	83.4	83.6	83.0	75.7	83.7	83.3	81.7	85.4	78.1	43.6	48.3	44.7	30.6	40.0	41.3
IV	88.1	90.6	85.9	88.3	87.8	89.8	83.1	88.0	86.9	87.5	89.3	84.1	46.1	49.9	48.3	35.4	42.9	44.0
1980 - I	93.8	95.0	93.2	94.1	93.1	93.4	92.8	93.1	90.5	94.5	93.5	93.6	49.1	52.1	49.7	41.1	45.5	47.7
II	97.5	97.8	97.2	97.5	97.4	98.0	96.6	98.3	95.6	98.3	97.6	96.8	50.9	53.4	52.3	42.8	46.9	49.8
III	101.6	101.3	102.2	101.8	101.3	100.6	103.0	101.7	101.7	102.3	101.0	101.9	53.0	55.3	53.5	48.1	47.7	52.0
IV	107.1	105.8	107.4	106.6	108.1	108.0	107.6	106.9	112.3	104.9	107.9	107.6	55.8	57.9	57.5	48.9	50.9	55.0
1981 - I	111.0	109.2	110.8	110.0	113.7	110.7	112.1	111.7	116.8	111.6	111.1	112.5	58.7	60.6	59.3	51.7	53.3	58.5
II	115.9	114.5	115.4	115.0	118.4	115.2	117.8	116.8	121.0	115.7	113.5	118.2	61.2	63.4	61.5	56.0	54.3	60.9
III	119.4	118.2	118.4	118.3	122.2	117.2	123.2	120.1	124.2	119.3	116.6	121.6	63.0	65.3	62.5	59.6	55.6	62.7
IV	124.9	123.5	124.0	123.8	127.9	125.3	128.2	124.9	129.3	124.6	121.9	126.8	66.0	68.3	66.9	61.9	58.9	65.3
1982 - I	129.9	128.4	128.1	128.2	134.3	128.9	134.1	129.5	135.9	128.8	126.8	133.1	68.5	70.8	68.7	64.3	61.5	68.0
II	133.9	131.7	131.9	131.8	139.2	133.6	137.9	134.6	141.4	131.8	129.8	138.3	70.6	72.5	71.2	66.0	63.5	70.3
III	139.4	138.3	137.4	137.8	143.4	136.0	144.8	138.1	144.8	140.9	133.7	142.2	73.6	76.3	72.5	71.4	64.7	73.0
IV	145.6	143.2	144.7	144.0	149.9	145.0	156.2	144.0	148.1	148.1	138.2	148.2	77.0	79.2	77.3	77.2	69.3	76.3
1983 - I	150.9	146.6	148.9	147.8	158.9	148.2	161.9	148.8	151.9	153.0	148.8	156.8	79.8	81.2	78.9	79.6	72.0	79.8
II	155.3	150.0	152.9	151.5	165.0	152.2	164.6	152.9	159.5	159.6	154.0	161.6	82.1	83.2	81.3	80.5	73.6	82.7
III	158.8	153.8	155.8	154.8	169.2	154.3	168.7	155.7	161.6	163.2	157.1	166.1	84.1	85.5	82.3	83.3	75.0	84.5
IV	164.3	157.7	161.0	159.5	177.0	162.6	185.4	159.9	163.8	167.9	161.4	170.3	87.0	87.8	86.3	86.7	88.3	86.6
1984 - I	169.1	161.4	166.1	163.9	182.7	165.8	194.9	164.1	166.7	173.5	166.9	176.0	89.5	89.7	88.0	90.8	92.9	89.2
II	173.0	165.2	169.4	167.4	187.4	169.7	198.3	167.4	175.3	176.0	171.5	180.1	91.4	91.7	90.2	91.2	94.7	91.1
III	175.5	166.9	171.3	169.3	191.9	171.7	199.0	169.9	181.2	179.8	174.2	183.7	92.6	92.7	91.1	91.0	95.6	92.7
IV	179.7	169.8	176.2	173.2	196.8	180.3	202.9	174.6	186.2	183.1	178.4	188.4	94.7	94.4	95.2	93.8	96.6	94.8
1985 - I	184.9	174.6	180.2	177.6	203.9	183.8	209.3	179.0	197.6	186.5	184.8	194.3	97.2	97.0	96.8	99.1	97.5	97.3
II	189.3	179.3	184.7	182.2	207.9	188.6	213.3	183.0	201.9	190.3	188.1	199.4	99.4	99.4	99.1	101.5	98.7	99.4
III	191.5	181.7	186.4	184.2	210.6	190.7	212.3	185.4	204.1	191.7	190.9	203.0	100.5	100.8	100.1	98.9	99.5	100.7
IV	195.7	185.4	190.6	188.2	215.3	198.4	218.5	189.1	206.5	194.4	195.4	206.7	102.8	102.8	104.0	100.6	104.2	102.5
1986 - I	....	....	....	....	....	....	....	....	....	....	....	....	104.6	104.1	105.5	98.5	105.8	105.2

Source: Istat.

(1) The pre-1981-I figures were obtained by dividing the figures of the 1976-based index by the conversion factor linking the 1976 and 1980-based series with reference to the 1980 average. – (2) The pre-1981-I figures were obtained by dividing the figures of the 1976-based index by the conversion factor linking the 1976 and 1980-based series with reference to the month of December 1980.

MAIN ITEMS OF THE BALANCE OF

(billions

	CURRENT ACCOUNT									
	GOODS (FOB)						SERVICES & TRANSFERS		CURRENT ACCOUNT BALANCE	
	Imports		Exports		Balance		Balance		Un-adjusted (5+7)	Seasonally adjusted (6+8)
	Un-adjusted	Seasonally adjusted	Un-adjusted	Seasonally adjusted	Un-adjusted	Seasonally adjusted	Un-adjusted	Seasonally adjusted		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
1976	34,309		30,782		–3,527		1,184		*–2,343*	
1977	39,639		39,521		–118		2,293		*2,175*	
1978	44,587		47,047		2,460		2,801		*5,261*	
1979	60,069		59,278		–791		5,344		*4,553*	
1980	79,814		65,823		–13,991		5,700		*–8,291*	
1981	97,043		85,011		–12,032		2,807		*–9,225*	
1982	108,707		97,968		–10,739		3,327		*–7,412*	
1983	114,063		109,381		–4,682		5,865		*1,183*	
1984	138,577		127,802		–10,775		5,691		*–5,084*	
1985	161,771		148,327		–13,444		5,412		*–8,032*	
1981 - I	23,440	22,405	19,217	19,103	–4,223	–3,302	–490	757	*–4,713*	–2,545
II	25,394	24,909	21,545	20,672	–3,849	–4,237	1,124	743	*–2,725*	–3,494
III	22,617	24,642	20,997	22,282	–1,620	–2,360	1,643	661	*23*	–1,699
IV	25,592	25,086	23,252	22,953	–2,340	–2,133	530	646	*–1,810*	–1,487
1982 - I	27,942	26,780	23,640	23,492	–4,302	–3,288	–877	708	*–5,179*	–2,580
II	27,107	26,607	25,198	24,243	–1,909	–2,364	1,267	807	*–642*	–1,557
III	25,107	27,408	22,844	24,244	–2,263	–3,164	2,598	1,166	*335*	–1,998
IV	28,551	27,912	26,286	25,989	–2,265	–1,923	339	645	*–1,926*	–1,278
1983 - I	28,059	26,942	25,387	25,191	–2,672	–1,751	–366	1,564	*–3,038*	–187
II	28,225	27,711	27,080	26,077	–1,145	–1,634	2,232	1,661	*1,087*	27
III	26,285	28,754	26,382	27,961	97	–793	2,949	1,260	*3,046*	467
IV	31,494	30,655	30,532	30,151	–962	–504	1,050	1,380	*88*	876
1984 - I	33,611	32,308	32,476	32,223	–1,135	–85	–853	1,060	*–1,988*	975
II	34,724	34,096	32,373	31,205	–2,351	–2,891	2,027	1,322	*–324*	–1,569
III	32,482	35,545	30,697	32,528	–1,785	–3,017	3,002	1,355	*1,217*	–1,662
IV	37,760	36,628	32,256	31,846	–5,504	–4,782	1,515	1,954	*–3,989*	–2,828
1985 - I	39,934		34,100		–5,834		223		*–5,611*	
II	41,482		35,435		–6,047		1,250		*–4,797*	

(1) Rounding may cause discrepancies in the totals. — (2) The 1984 figures are adjusted for the arrangements regarding the foreign assets of Banco Ambrosiano in

Table a 7

PAYMENTS ON A TRANSACTIONS BASIS (1)

of lire)

CAPITAL MOVEMENTS							
Medium and long-term	Short-term	Total	ERRORS AND OMISSIONS	CHANGES IN BANKS' NET EXTERNAL POSITION (2)	CHANGES IN OFFICIAL RESERVES (3)	EXCHANGE RATE ADJUSTMENTS	OVERAL BALANCE *(9 + 13 + 14) = −(15 + 16 + 17)*
(11)	*(12)*	*(13)*	*(14)*	*(15)*	*(16)*	*(17)*	*(18)*
295	1,189	1,484	−672	2,638	−196	−911	*−1,531*
895	−949	−54	−391	3,493	−5,061	−162	*1,730*
910	409	1,319	416	−1,158	−5,697	−141	*6,996*
−266	−2,138	−2,404	−325	1,004	−2,626	−202	*1,824*
3,054	−305	2,749	−716	7,886	−1,946	318	*−6,258*
9,652	1,734	11,386	−628	1,322	−2,208	−647	*1,533*
7,250	−2,065	5,185	−294	−1,505	3,921	105	*−2,521*
1,284	616	1,900	710	6,792	−11,183	598	*3,793*
3,021	−2,547	474	4,667	6,654	−7,666	955	*57*
4,825	1,387	6,212	−6,532	−4,849	13,698	−497	*−8,352*
1,642	169	1,811	−505	−18	3,321	104	*−3,407*
3,178	113	3,291	463	1,118	−1,567	−580	*1,029*
1,320	3,202	4,522	−587	−1,547	−2,453	42	*3,958*
3,512	−1,750	1,762	1	1,769	−1,509	−213	*−47*
1,863	−1,165	698	973	−174	3,716	−34	*−3,508*
2,488	−487	2,001	−671	409	−1,298	201	*688*
844	1,038	1,882	−428	517	−2,394	88	*1,789*
2,055	−1,451	604	−168	−2,257	3,897	−150	*−1,490*
685	−169	516	395	2,231	−137	33	*−2,127*
113	894	1,007	761	3,681	−6,554	18	*2,855*
537	146	683	−426	−1,122	−2,603	422	*3,303*
−51	−255	−306	−20	2,002	−1,889	125	*−238*
1,121	262	1,383	−2,617	826	2,194	202	*−3,222*
−631	−1,492	−2,123	1,443	4,218	−3,189	−25	*−1,004*
1,527	−978	549	1,343	630	−4,285	546	*3,109*
1,004	−339	665	4,498	980	−2,386	232	*1,174*
2,839	94	2,933	−1,694	877	2,771	724	*−4,372*
2,223	986	3,209	217	4,262	−2,385	−506	*−1,371*

liquidation. — (3) A minus sign indicates an increase in assets or a decrease in liabilities.

BALANCE OF PAYMENT

(billio

	CURRENT ACCOUNT							CAPITAL MOVEMENTS	ERRORS & OMISSIONS	OVERALL BALANCE
	Goods (2)	Freight	Foreign travel	Emigrants' remittances	Income from capital	Other services	Total			
										Rece
1976	29,449	1,011	2,101	743	1,070	3,357	*37,731*	2,880	358	–
1977	39,682	1,370	4,202	1,246	1,191	3,901	*51,592*	3,477	–	–
1978	45,992	1,507	5,334	1,655	1,721	4,587	*60,796*	4,829	236	–
1979	55,021	1,863	6,816	2,005	2,746	6,077	*74,528*	7,603	272	–
1980	65,419	2,346	7,032	2,211	4,067	7,584	*88,659*	10,422	–	–
1981	83,093	2,623	8,585	2,614	6,020	8,804	*111,739*	19,039	–	–
1982	94,866	2,634	11,278	3,166	7,067	11,048	*130,059*	19,324	–	–
1983	103,614	2,975	13,721	3,447	5,722	12,953	*142,432*	18,390	–	–
1984	120,408	3,859	15,098	3,865	7,668	16,540	*167,438*	28,543	3,772	–
1985	138,337	4,548	16,722	4,312	8,692	19,933	*192,544*	44,769	–	–
										Pay
1976	33,416	–	588	–	1,982	3,381	*39,367*	3,133	–	–
1977	42,586	–	788	–	2,143	4,516	*50,033*	3,196	110	–
1978	45,996	–	1,024	–	2,656	5,815	*55,491*	3,374	–	–
1979	62,247	–	1,252	–	3,418	6,677	*73,594*	6,985	–	–
1980	83,770	–	1,633	–	5,040	8,361	*98,804*	6,318	217	–
1981	97,110	–	1,892	–	10,171	10,241	*119,414*	9,278	553	–
1982	112,055	–	2,350	–	12,882	12,820	*140,107*	11,474	323	–
1983	112,790	–	2,768	–	12,140	14,028	*141,726*	15,218	85	–
1984	138,760	–	3,686	–	15,222	17,024	*174,692*	25,004	–	–
1985	157,048	–	4,360	–	17,072	21,557	*200,037*	37,144	8,484	–
										Bal
1976	–3,967	1,011	1,513	743	–912	–24	*–1,636*	–253	358	*–1,531*
1977	–2,904	1,370	3,414	1,246	–952	–615	*1,559*	281	–110	*1,730*
1978	–4	1,507	4,310	1,655	–935	–1,228	*5,305*	1,455	236	*6,996*
1979	–7,226	1,863	5,564	2,005	–672	–600	*934*	618	272	*1,824*
1980	–18,351	2,346	5,399	2,211	–973	–777	*–10,145*	4,104	–217	*–6,258*
1981	–14,017	2,623	6,693	2,614	–4,151	–1,437	*–7,675*	9,761	–553	*1,533*
1982	–17,189	2,634	8,928	3,166	–5,815	–1,772	*–10,048*	7,850	–323	*–2,521*
1983	–9,176	2,975	10,953	3,447	–6,418	–1,075	*706*	3,172	–85	*3,793*
1984	–18,352	3,859	11,412	3,865	–7,554	–484	*–7,254*	3,539	3,772	*57*
1985	–18,711	4,548	12,362	4,312	–8,380	–1,624	*–7,493*	7,625	–8,484	*–8,352*

(1) Rounding may cause discrepancies in totals. – (2) Imports cif, exports fob. – (3) The 1984 figures have been adjusted for the arrangements regarding the foreign assets

ON A SETTLEMENTS BASIS (1)

of lire)

CHANGES IN BANKS' NET EXTERNAL POSITION (3) (4)	CHANGES IN OFFICIAL RESERVES (4)									EXCHANGE RATE ADJUST-MENTS
	Gold	Convertible currencies	ECUs	SDRs	Reserve position in the IMF	Short-term liabilities	Medium & long-term position	Revaluation of gold (5)	Total	
i p t s										
2,638	–	–	–	–	–	66	1,665	6,351	*8,082*	–
3,493	–	–	–	–	–	94	–	1,643	*1,737*	–
–	–	–	–	–	–	–	–	2,072	*2,072*	–
1,004	–	781	–	–	11	–	–	8,262	*9,054*	–
7,886	–	–	–	–	–	139	281	22,550	*22,970*	318
1,322	–	–	–	–	–	–	379	773	*1,152*	–
–	2,343	2,519	2,544	–	–	–	–	–	*7,406*	105
6,792	–	–	–	13	–	211	9	13,686	*13,919*	598
6,654	1,512	–	–	–	–	–	–	–	*1,512*	955
–	2,357	7,281	6,020	467	133	–	427	–	*16,685*	–
m e n t s										
–	6,351	1,914	–	13	–	–	–	–	*8,278*	911
–	1,658	4,197	–	46	–	–	897	–	*6,798*	162
1,158	2,080	1,774	–	118	262	37	3,498	–	*7,769*	141
–	4,247	–	5,974	232	–	20	1,207	–	*11,680*	202
–	18,030	2,221	4,008	143	514	–	–	–	*24,916*	–
–	623	1,506	703	324	113	91	–	–	*3,360*	647
1,505	–	–	–	168	73	37	284	2,923	*3,485*	–
–	10,949	8,451	5,013	–	689	–	–	–	*25,102*	–
–	–	6,207	6	252	437	92	294	1,890	*9,178*	–
4,849	–	–	–	–	–	41	–	2,946	*2,987*	497
a n c e										
2,638	−6,351	−1,914	–	−13	–	66	1,665	6,351	*−196*	−911
3,493	−1,658	−4,197	–	−46	–	94	−897	1,643	*−5,061*	−162
−1,158	−2,080	−1,774	–	−118	−262	−37	−3,498	2,072	*−5,697*	−141
1,004	−4,247	781	−5,974	−232	11	−20	−1,207	8,262	*−2,626*	−202
7,886	−18,030	−2,221	−4,008	−143	−514	139	281	22,550	*−1,946*	318
1,322	−623	−1,506	−703	−324	−113	−91	379	773	*−2,208*	−647
−1,505	2,343	2,519	2,544	−168	−73	−37	−284	−2,923	*3,921*	105
6,792	−10,949	−8,451	−5,013	13	−689	211	9	13,686	*−11,183*	598
6,654	1,512	−6,207	−6	−252	−437	−92	−294	−1,890	*−7,666*	955
−4,849	2,357	7,281	6,020	467	133	−41	427	−2,946	*13,698*	−497

of Banco Ambrosiano in liquidation. – (4) A minus sign indicates an increase in assets or a decrease in liabilities. – (5) Including the revaluation of ECUs issued against gold.

Table a 9

INDICATORS OF COMPETITIVENESS BASED ON WHOLESALE PRICES AND AVERAGE UNIT PRICES FOR EXPORTS OF MANUFACTURES

(indices, 1980 = 100)

	Competitiveness in foreign markets (average unit values)	Competitiveness in domestic and foreign markets with respect to (based on wholesale prices)							
	13 industrial countries	13 industrial countries	EEC countries	Germany	France	United Kingdom	Belgium	Netherlands	United States
1976	94.4	95.5	97.4	93.6	99.4	123.0	87.5	91.9	87.3
1977	96.9	97.6	99.1	93.8	106.4	119.9	88.0	89.9	91.2
1978	93.5	94.6	95.7	91.2	101.6	112.5	86.9	88.7	96.3
1979	95.6	96.3	96.3	92.6	100.5	107.4	90.6	93.7	99.8
1981	96.9	96.2	99.5	101.6	98.8	91.3	103.2	99.5	78.6
1982	96.3	95.5	99.5	98.7	101.5	92.6	112.3	94.9	72.3
1983	94.6	98.4	103.7	100.9	106.6	99.9	120.1	98.1	70.6
1984	97.0	99.1	106.0	103.8	107.9	101.6	124.5	100.4	65.5
1985	95.8	98.6	105.1	104.8	104.1	99.5	124.4	101.3	65.3
1979 - I	93.9	93.6	93.9	89.8	98.6	110.4	85.8	88.4	98.5
II	93.4	96.0	96.4	92.6	101.3	106.8	90.3	93.7	97.8
III	97.5	97.1	97.0	93.7	101.4	103.4	92.3	95.7	101.1
IV	97.7	98.4	97.8	94.2	100.7	108.9	93.8	97.0	101.7
1980 - I	99.2	100.0	99.4	97.2	101.2	105.6	97.8	98.0	101.7
II	99.6	99.7	99.6	98.8	100.2	101.3	98.8	99.7	100.2
III	101.2	100.0	99.8	100.4	99.1	99.2	100.5	99.4	102.0
IV	99.8	100.1	101.2	103.4	99.6	94.2	102.6	102.3	96.3
1981 - I	98.1	98.1	100.4	103.6	99.6	88.8	103.4	100.9	86.6
II	95.6	95.7	99.1	101.4	99.2	87.5	102.9	100.5	77.2
III	98.6	96.2	100.3	102.6	98.3	94.3	104.0	100.8	73.7
IV	95.1	94.6	98.2	98.9	98.1	94.7	102.3	95.9	76.8
1982 - I	95.8	94.8	98.8	99.6	98.9	92.1	107.6	95.3	74.7
II	95.9	94.9	98.7	98.3	99.0	92.5	112.6	95.2	73.8
III	98.4	95.8	100.1	98.3	104.2	91.3	113.9	94.5	70.7
IV	94.9	96.3	100.5	98.5	103.6	94.3	115.2	94.5	70.1
1983 - I	95.5	99.1	103.6	100.8	104.8	105.9	118.2	97.1	74.4
II	93.5	98.8	103.7	100.6	107.4	99.4	119.5	98.6	72.3
III	93.1	97.9	103.6	101.2	107.0	96.9	120.8	97.9	68.3
IV	96.3	97.7	103.8	101.0	107.2	97.5	122.0	98.7	67.5
1984 - I	95.7	97.9	104.2	101.5	107.4	98.6	123.2	98.1	67.3
II	95.9	99.1	105.4	103.0	107.7	100.8	124.2	99.5	68.0
III	98.1	99.7	106.7	104.8	108.3	102.3	124.9	101.2	64.4
IV	98.3	99.9	107.6	105.7	108.0	104.7	125.8	102.9	62.6
1985 - I	97.5	100.5	108.8	107.1	108.4	107.9	126.6	104.7	60.2
II	95.3	98.9	105.9	105.8	105.2	98.1	125.3	102.2	62.6
III	95.1	97.0	102.7	103.1	101.8	93.9	122.5	98.9	66.1
IV	95.2	98.0	103.1	103.1	101.1	98.0	123.0	99.5	72.3

Source: Based on Istat, OECD and IMF data.

Table a 10

ITALY'S EXTERNAL FINANCIAL POSITION

(billions of dollars)

	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Memorandum item:										
lira-dollar exchange rate at end of year	875	872	830	804	930	1,200	1,370	1,659	1,936	1,678
Bank of Italy and UIC (1)	3.2	8.1	11.1	18.2	23.1	20.1	14.1	20.2	20.9	15.9
Banks	12.8	15.4	23.1	30.1	31.3	37.1	34.9	35.7	37.4	48,0
Other channels: trade credit (2)	7.6	8.7	12.0	17.0	16.7	14.8	13.1	12.5	11.9	16.0
Short-term assets	**23.6**	**32.2**	**46.2**	**65.3**	**71.1**	**72.0**	**62.1**	**68.4**	**70.2**	**79.9**
Bank of Italy and UIC	0.9	1.2	1.5	1.7	1.5	1.2	0.9	0.7	0.6	0.4
Banks	0.1	. .	0.1	. .	0.1	0.2	0.2	0.2	0.2	0.4
Other channels: foreign loans (3)	2.7	2.6	3.0	3.4	4.1	4.1	4.5	4.7	5.4	7.2
trade credit (3)	9.4	9.2	10.4	11.6	10.1	8.5	8.1	8.2	7.2	7.4
Medium and long-term assets	**13.1**	**13.0**	**15.0**	**16.7**	**15.8**	**14.0**	**13.7**	**13.8**	**13.4**	**15.4**
TOTAL ASSETS.	**36.7**	**45.2**	**61.2**	**82.0**	**86.9**	**86.0**	**75.8**	**82.2**	**83.6**	**95.3**
Bank of Italy and UIC	0.1	0.2	0.2	0.2	0.3	0.2	0.1	0.2	0.1	0.1
Banks	16.8	23.4	30.0	38.4	47.0	50.2	44.9	48.0	52.1	62.7
Other channels: trade credit (2)	7.4	7.1	9.3	11.6	11.7	12.9	10.5	10.7	10.6	13.4
Short-term liabilities	**24.3**	**30.7**	**39.5**	**50.2**	**59.0**	**63.3**	**55.5**	**58.9**	**62.8**	**76.2**
Bank of Italy and UIC: monetary liabilities	7.0	6.3	2.7	1.2	1.2	1.0	0.4	0.3	–	–
SDR account	0.4	0.4	0.4	0.6	0.7	0.8	0.8	0.7	0.7	0.8
Banks	0.1	0.1	0.3	0.3	0.3	0.5	0.8	0.8	0.6	0.3
Other channels: borrowing abroad	13.8	14.1	16.6	17.6	23.6	33.2	39.1	40.5	40.6	48.5
of which: compensatory loans special account	*4.6*	*3.9*	*3.1*	*0.6*	*0.7*	*0.5*	*0.3*	*0.2*	. .	. .
trade credit	0.9	0.9	1.0	0.9	0.8	0.7	0.5	1.1	1.3	1.3
Medium and long-term liabilities	**22.2**	**21.8**	**21.0**	**20.6**	**26.6**	**36.2**	**41.6**	**43.4**	**43.2**	**50.9**
TOTAL LIABILITIES	**46.5**	**52.5**	**60.5**	**70.8**	**85.6**	**99.5**	**97.1**	**102.3**	**106.0**	**127.1**
Bank of Italy and UIC (1)	3.1	7.9	10.9	18.0	22.8	19.9	14.0	20.0	20.8	15.8
Banks	–4.0	–8.0	–6.9	–8.3	–15.7	–13.1	–10.0	–12.3	–14.7	–14.7
Other channels: trade credit	0.2	1.6	2.7	5.4	5.0	1.9	2.6	1.8	1.3	2.6
Short-term balance	**-0.7**	**1.5**	**6.7**	**15.1**	**12.1**	**8.7**	**6.6**	**9.5**	**7.4**	**3.7**
Bank of Italy and UIC	–6.5	–5.5	–1.6	–0.1	–0.4	–0.6	–0.3	–0.3	–0.1	–0.4
Banks	–	–0.1	–0.2	–0.3	–0.2	–0.3	–0.6	–0.6	–0.4	0.1
Other channels: loans	–11.1	–11.5	–13.6	–14.2	–19.5	–29.1	–34.6	–35.8	–35.2	–41.3
trade credit	8.5	8.3	9.4	10.7	9.3	7.8	7.6	7.1	5.9	6.1
Medium and long-term balance	**-9.1**	**-8.8**	**-6.0**	**-3.9**	**-10.8**	**-22.2**	**-27.9**	**-29.6**	**-29.8**	**-35.5**
OVERALL BALANCE	**-9.8**	**-7.3**	**0.7**	**11.2**	**1.3**	**-13.5**	**-21.3**	**-20.1**	**-22.4**	**-31.8**

(1) Net of gold reserves. From 1979 onwards the figures include ECUs created against transfers of gold. – (2) The assets include exports on deferred payment terms and advance payments for imports; the liabilities include advance receipts in respect of exports and imports on deferred payment terms. – (3) New series.

Table a 11

CONSOLIDATED ACCOUNTS OF THE PUBLIC SECTOR

(billions of lire)

	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Revenue										
Current revenue	**55,477**	**69,481**	**85,115**	**102,300**	**134,484**	**166,930**	**208,206**	**255,835**	**286,904**	**320,315**
Direct taxes	12,334	16,458	22,408	26,628	38,045	51,575	66,686	84,084	93,942	105,471
Indirect taxes	15,021	19,485	22,368	25,347	34,128	39,025	47,680	60,396	68,524	74,302
Social security contributions	21,910	26,191	31,081	39,227	48,960	59,145	73,791	88,125	97,550	107,929
– actual	19,929	23,732	27,772	34,947	43,755	52,516	66,150	78,232	85,969	95,117
– imputed	1,981	2,459	3,309	4,280	5,205	6,629	7,641	9,893	11,581	12,812
Income from capital	1,124	1,370	1,734	2,408	3,153	3,792	4,229	4,640	4,990	6,270
Sales of goods and services	3,874	4,522	5,324	6,115	6,716	8,636	11,054	13,140	15,287	18.471
Other	1,214	1,455	2,200	2,575	3,482	4,757	4,766	5,450	6,611	7,872
Capital account revenue	**301**	**1,115**	**339**	**267**	**580**	**681**	**867**	**1,292**	**1,942**	**2,180**
TOTAL REVENUE	**55,778**	**70,596**	**85,454**	**102,567**	**135,064**	**167,611**	**209,073**	**257,127**	**288,846**	**322,495**
Expenditure										
Current expenditure	**63,220**	**77,687**	**98,046**	**116,535**	**147,680**	**195,575**	**244,934**	**293,582**	**336,193**	**376,403**
Wages and salaries	19,774	24,846	30,182	37,617	47,698	64,026	75,064	87,792	100,343	100,868
Intermediate consumption	7,750	9,519	11,415	14,435	17,686	22,796	28,802	34,687	40,322	46,891
Social services	24,421	28,963	36,577	42,426	53,465	71,204	87,795	107,377	119,475	133,782
Subsidies to firms	2,273	2,766	3,833	4,060	4,764	5,353	7,861	9,909	10,506	13,219
Interest payments	7,439	9,664	13,360	16,046	21,525	29,465	40,592	49,522	60,675	65.889
Other	1,563	1,929	2,679	1,951	2,542	2,731	4,820	4,295	4,872	5,754
Capital account expenditure	**7,791**	**9,521**	**11,005**	**13,413**	**17,718**	**22,775**	**28,786**	**34,332**	**40,129**	**48,860**
Gross investment	6,169	7,372	8,101	9,610	13,094	17,293	21,877	26,051	30,116	31,312
Investment grants	1,478	2,091	2,247	2,522	2,977	4,744	6,380	7,410	8,757	10,269
Other	144	58	657	1,281	1,647	738	529	871	1,256	7,279
TOTAL EXPENDITURE	**71,011**	**87,208**	**109,051**	**129,948**	**165,398**	**218,350**	**273,720**	**327,914**	**376,322**	**425,263**
Deficit on current account	**-7,743**	**-8,206**	**-12,931**	**-14,235**	**-13,196**	**-28,645**	**-36,728**	**-37,747**	**-49,289**	**-56,088**
Total deficit	**-15,233**	**-16,612**	**-23,597**	**-27,381**	**-30,334**	**-50,739**	**-64,647**	**-70,787**	**-87,476**	**-102,768**

Source: Based on data contained in the *Relazione generale sulla situazione economica del paese.*

Table a 12

FINANCING OF THE PUBLIC SECTOR BORROWING REQUIREMENT (1)

(billions of lire)

	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Medium and long-term securities, excluding BI portfolio	746	7,925	14,178	12,175	–2,303	5,727	23,429	66,968	55,942	83,937
Treasury bills, excluding BI portfolio	2,076	15,090	9,270	9,926	26,218	28,234	29,039	10,377	14,918	–1,878
Treasury bills in compulsory reserves	–652	–	–	–	–	–	–	–	–	–
Post Office funds	2,636	3,211	4,871	6,748	2,195	2,591	3,586	4,937	6,057	9,268
Lending by credit institutions	2,651	–2,978	–140	2,558	752	988	5,193	5,699	8,711	–2,098
to: *central government bodies*	*34*	*36*	*32*	*490*	*343*	*819*	*783*	*–139*	*10*	*–89*
social security institutions	*67*	*190*	*155*	*255*	*280*	*–1,254*	*242*	*225*	*755*	*–2,203*
local authorities	*2,570*	*–3,224*	*–170*	*1,740*	*148*	*1,459*	*3,105*	*3,441*	*6,651*	*394*
autonomous govt. agencies	*–80*	*73*	*–161*	*71*	*–74*	*–68*	*1,065*	*2,059*	*1,315*	*–307*
municipal enterprises	*60*	*–53*	*5*	*2*	*55*	*33*	*–1*	*113*	*–19*	*107*
Other domestic debt (2)	111	137	234	160	136	79	160	208	232	71
Foreign debt	202	77	273	581	787	2,515	2,570	1,259	2,271	2.937
TOTAL...	**7,770**	**23,462**	**28,686**	**32,148**	**27,785**	**40,134**	**63,977**	**89,448**	**88,131**	**92.237**
Borrowing from BI-UIC	9,938	–4,008	5,024	343	9,930	13,692	12,589	1,259	13,726	27.479
of which: overdraft on BI account	*1,694*	*–420*	*1,910*	*3,476*	*8,944*	*6,186*	*6,598*	*–8,622*	*18,554*	*6,340*
TOTAL BORROWING REQUIREMENT	**17,708**	**19,454**	**33,710**	**32,491**	**37,715**	**53,826**	**76,566**	**90,707**	**101,857**	**119,716**
Financing of ENEL			**898**	**1,068**	**2,790**	**1,056**	**3,389**	**2,138**	**1,756**	**1,106**
of which: bond issues			*867*	*209*	*471*	*–756*	*1,213*	*1,081*	*1,045*	*669*
loans from credit institutions			*–269*	*477*	*58*	*–109*	*794*	*–309*	*1,022*	*182*
borrowing abroad			*300*	*382*	*2,261*	*1,921*	*1,382*	*1,366*	*–311*	*255*
TOTAL BORROWING REQUIREMENT OF THE ENLARGED PUBLIC SECTOR			**34,608**	**33,559**	**40,505**	**54,882**	**79,955**	**92,845**	**103,613**	**120,822**

(1) Rounding may cause discrepancies in the totals. – (2) Treasury currency in circulation, loans of insurance companies to local authorities, stockpiling bills not yet rediscounted and bank deposits with the Treasury.

Table a 13

STATE SECTOR EXPENDITURE, REVENUE AND BORROWING REQUIREMENT

(billions of lire)

	1981	1982	1983	1984	1985
EXPENDITURE					
Wages, salaries and pensions	40,850	49,662	57,295	64,862	71,131
Purchases of goods and services	9,613	11,551	14,961	18,848	19,318
Interest payments	27,328	38,914	47,105	57,593	63,456
Direct investment	6,971	8,684	11,316	12,610	11,530
Loans and shareholdings	8,074	12,872	16,059	12,411	14,133
of which: local authorities	*2,751*	*3,901*	*3,896*	*3,725*	*4,303*
financial institutions	*1,864*	*573*	*1,767*	*1,716*	*2,454*
public enterprises	*3,006*	*7,384*	*9,431*	*6,548*	*5,467*
Disbursements to: local authorities	44,579	56,936	72,288	75,727	91,504
of which: health care	*18,449*	*24,423*	*30,656*	*33,307*	*39,552*
social security institutions	12,574	23,176	27,437	29,626	36,490
enterprises	5,924	9,086	11,493	13,450	13,203
households	2,575	3,028	4,679	6,109	7,448
other	4,293	4,614	4,486	8,355	11,753
Other expenditure	4,656	7,992	9,600	11,553	12,092
TOTAL EXPENDITURE ...	**167,437**	**226,515**	**276,719**	**311,144**	**352,058**
REVENUE					
Direct taxes					
of which: Personal income tax	29,006	37,051	46,546	51,073	61,852
Corporate income tax	3,131	3,636	5,457	8,117	9,172
Local income tax	5,239	6,253	7,635	8,027	10,554
Withholding tax on interest income	7,948	10,835	10,642	15,618	13,909
Indirect taxes					
of which: Value added tax	24,099	29,186	36,081	41,882	45,126
Business taxes (stamp duties, duties on government concessions, etc.)	5,443	6,332	7,345	8,871	9,731
Excise duty on oil products	7,027	8,244	11,585	13,014	13,651
Excise duty on other manufactures (spirits, beer, sugar, gas and electricity, methane, etc.)	1,038	1,174	1,294	1,316	1,178
Tax on tobacco consumption	2,299	3,199	3,732	4,134	4,399
Total tax revenue	**89,939**	**115,110**	**145,906**	**164,845**	**179,489**
EEC levies	2,996	3,516	4,111	4,539	4,745
Sales of goods and services	6,583	8,212	9,932	11,920	14,992
Health care and other social security contributions	11,507	19,222	19,256	24,245	27,534
Other income	6,799	8,465	9,257	10,208	12,885
TOTAL REVENUE ...	**117,824**	**154,525**	**188,462**	**215,757**	**239,645**
BORROWING REQUIREMENT	**49,613**	**71,990**	**88,257**	**95,387**	**112,413**

Table a 14

THE PUBLIC DEBT (1)

(face value; billions of lire and percentage composition)

	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
					Amounts outstanding					
Medium and long-term securities, excluding BI portfolio	16,413	24,927	39,502	52,008	49,527	55,802	80,893	149,832	207,740	294,567
of which: held by banks	*10,947*	*18,072*	*26,663*	*34,375*	*31,435*	*32,435*	*47,907*	*81,094*	*96,285*	*127,593*
Treasury bills, excluding BI portfolio	9,620	24,709	33,979	43,905	70,123	98,357	127,395	137,772	152,691	150,814
of which: held by banks	*6,929*	*18,334*	*23,910*	*25,117*	*35,437*	*39,097*	*56,514*	*51,317*	*44,743*	*26.568*
Post Office funds	16,023	19,234	24,105	30,853	33,048	35,639	39,225	44,162	50,219	59.487
Lending by credit institutions	16,840	14,262	14,122	16,680	17,432	18,420	23,613	29,312	38,024	35.925
to: central government bodies	*326*	*362*	*393*	*883*	*1.226*	*2.045*	*2.828*	*2,689*	*2,699*	*2,609*
social security institutions	*1,587*	*1,778*	*1,932*	*2,188*	*2,468*	*1,213*	*1,455*	*1,680*	*2,435*	*232*
local authorities	*14,359*	*11,135*	*10,965*	*12,705*	*12,853*	*14,312*	*17,417*	*20,857*	*27,508*	*27.902*
autonomous government agencies	*204*	*677*	*516*	*587*	*513*	*445*	*1.511*	*3,570*	*4,885*	*4,578*
municipal enterprises	*364*	*311*	*316*	*317*	*372*	*405*	*403*	*516*	*497*	*605*
Other domestic debt	1,032	1,170	1,404	1,563	1,700	1,779	1,938	2,147	2,379	2.450
Foreign debt	1,474	1,616	1,941	2,392	3,433	6,578	9,731	12,505	16,285	18.254
SUB-TOTAL	**61,402**	**85,918**	**115,053**	**147,402**	**175,262**	**216,575**	**282,796**	**375,730**	**467,337**	**561,497**
Borrowing from BI-UIC	40,994	38,026	43,153	43,255	52,978	66,555	78,670	79,631	92,863	120.286
of which: medium and long-term securities	*16,081*	*24,882*	*30,771*	*27,759*	*28,261*	*29,647*	*28,891*	*30,393*	*36,367*	*45.083*
Treasury bills	*18,028*	*7,588*	*3,987*	*3,657*	*2,641*	*8,099*	*12,086*	*12,670*	*6,641*	*21.658*
overdraft on BI account	*5,216*	*4,796*	*6,706*	*10,182*	*19,126*	*25,312*	*31,910*	*23,288*	*41,842*	*48.182*
other borrowing	*1,669*	*760*	*1,689*	*1,657*	*2,950*	*3,497*	*5,783*	*13,280*	*8,013*	*5.363*
TOTAL	**102,396**	**123,944**	**158,206**	**190,657**	**228,240**	**283,130**	**361,466**	**455,361**	**560,200**	**681,783**
					Percentage composition					
Medium and long-term securities, excluding BI portfolio	16.0	20.1	25.0	27.3	21.7	19.7	22.4	32.9	37.1	43.2
Treasury bills, excluding BI portfolio	9.4	20.0	21.5	23.0	30.7	34.8	35.2	30.3	27.3	22.1
Post Office funds	15.7	15.5	15.2	16.2	14.5	12.6	10.9	9.7	8.9	8,7
Lending by credit institutions	16.5	11.5	8.9	8.8	7.7	6.5	6.5	6.4	6.8	5.3
Other domestic debt	1.0	0.9	0.9	0.8	0.7	0.6	0.5	0.5	0.4	0.4
Foreign debt	1.4	1.3	1.2	1.2	1.5	2.3	2.7	2.7	2.9	2.7
Borrowing from BI-UIC	40.0	30.7	27.3	22.7	23.2	23.5	21.8	17.5	16.6	17.6

(1) Rouding may cause discrepancies in totals.

BANKS' ASSETS

(billions

	ASSETS										
	Bank reserves			Lending		Bad debts & protested bills	Shares	Interbank accounts	Accounts with special credit institutions		External assets (5)
	Excess reserves in lire (2)	Compulsory reserves (3)	Deposits against excess lending	Loans & bankers' acceptances	Lira securities (4)					of which: savings certificates	
1976 - Dec.	2,412	16,624	–	72,693	44,788	1,308	1,329	23,367	1,425	128	10,630
1977 - "	3,251	20,265	–	79,154	67,415	1,932	1,601	26,685	2,761	1,148	12,819
1978 - "	5,092	25,282	–	86,834	86,397	2,732	1,966	35,297	3,642	1,319	18,247
1979 - " (8) ...	3,900	30,668	–	105,673	99,805	4,117	2,307	41,872	3,717	1,090	23,060
1980 - "	4,393	33,740	591	126,693	112,490	5,776	3,069	54,282	4,759	1,312	27,409
1981 - "	4,869	36,641	1,298	142,455	120,378	7,047	3,497	65,951	6,598	1,699	40,523
1982 - "	3,648	45,171	820	155,312	151,951	9,267	5,158	77,552	7,507	3,553	42,386
1983 - "	3,925	54,082	–	178,800	180,092	11,566	6,602	89,503	7,662	3,451	52,271
1984 - Jan.	3,168	63,065	–	184,371	158,153	12,201	6,736	56,485	6,813	3,080	44,493
Feb.	2,742	61,319	–	185,652	152,663	12,533	6,808	56,332	7,105	3,018	41,822
Mar.	2,850	60,020	–	187,052	153,537	12,709	6,837	58,705	6,514	2,903	41,036
Apr.	2,986	59,944	–	191,657	157,837	13,064	7,058	56,725	6,591	2,887	40,507
May	3,352	59,020	–	192,670	157,360	13,291	7,308	60,151	6,659	2,856	41,262
June	3,629	58,529	–	195,892	160,215	13,445	7,401	61,419	6,519	2,830	40,846
July	2,967	59,294	–	205,147	159,476	13,760	7,910	57,643	6,121	2,844	39,974
Aug.	3,155	60,051	–	203,313	160,521	13,935	8,025	58,860	6,355	2,757	39,120
Sept.	2,312	60,273	–	206,224	169,103	14,061	8,048	63,300	6,102	2,584	41,442
Oct.	3,891	61,860	–	209,393	172,319	14,332	8,114	62,960	6,494	2,605	46,574
Nov.	5,408	62,583	–	211,903	173,353	14,315	8,161	66,540	6,582	2,578	57,235
Dec.	4,994	62,813	–	215,594	187,037	14,569	8,600	94,512	8,277	3,038	64,193
1985 - Jan.	4,012	73,644	–	219,498	171,708	15,123	8,696	68,337	7,153	3,014	56,687
Feb.	2,978	73,070	–	219,305	168,335	15,253	8,748	67,504	6,427	3,000	61,862
Mar.	2,303	71,628	–	218,923	173,794	15,525	8,913	67,993	6,388	3,068	60,878
Apr.	3,124	71,563	–	223,684	177,183	15,767	8,882	67,819	6,365	3,055	62,313
May (9) ...	4,118	71,621	–	223,991	177,277	16,064	8,877	69,108	6,647	3,057	61,705
June	3,589	70,696	–	222,795	186,589	16,208	8,778	66,928	6,520	3,128	64,337
July	3,138	72,106	–	229,592	183,502	16,504	8,752	65,036	5,870	3,191	60,974
Aug.	2,690	73,054	–	224,590	186,333	16,692	8,686	66,493	6,444	3,750	55,031
Sept.	2,797	73,088	–	224,087	193,057	16,967	8,936	65,308	6,210	3,783	....
Oct.	2,802	74,714	–	227,424	191,893	17,337	9,263	64,180	6,858	3,743	....
Nov. (9) ...	4,160	75,118	–	231,372	194,603	17,520	9,233	75,323	7,356	3,692	....
Dec. (10) ..	7,920	74,826	–	244,193	199,407	17,791	9,421	96,831	9,107	3,786	71,095
1986 - Jan. (9)....	2,883	83,124	–	238,240	176,002	18,335	9,742	72,504	7,833	3,685	....
Feb. (11) ..	3,000	81,620	555	233,450	175,280	18,490	9,870	63,600	7,670	3,710	....
Mar. (11) ..	2,600	79,450	877	232,510	177,530	18,800	10,060	64,310	8,660	3,740	....

(1) Rounding may cause discrepancies in totals. – (2) Excluding deposits with the Post Office and the Deposits and Loans Fund. – (3) Includes backing for cashiers' cheques. – foreign currency accounts. – (8) Owing to errors in the procedures previously used by some banks for automatically calculating loans, a break in the series occurs in December 1979: the the Bank of Italy. – (10) Estimated data for foreign assets and liabilities. – (11) Provisional.

Table a 15

AND LIABILITIES (1)

of lire)

LIABILITIES									MEMORANDUM		
					Funds raised abroad				Loan guarantees		
Deposits (6)	Other domestic funds (7)	Lending by BI-UIC	Interbank accounts	Deposits of special credit institutions	(5)	of which: non-residents' lira accounts	Equity capital	Other items		of which: bankers' acceptances issued	
123,405	1,458	2,345	21,310	4,958	13,966	609	5,147	1,987	14,500	–	.... Dec. - 1976
152,025	1,232	2,552	24,332	4,664	19,319	798	6,518	5,241	17,211	–	.... " - 1977
187,088	2,577	2,315	31,486	4,945	24,035	942	7,750	5,293	22,238	–	.... " - 1978
224,644	2,305	5,079	35,749	4,798	29,795	1,109	9,795	2,954	26,166	696	..(8) " - 1979
254,341	1,900	2,427	47,414	5,377	41,590	1,320	12,462	7,691	32,405	2,535	.... " - 1980
277,771	2,066	2,981	58,306	5,039	55,694	1,638	16,758	10,642	39,393	3,572	.... " - 1981
328,450	2,318	3,625	68,599	6,623	56,339	2,296	21,312	11,506	45,966	2,707	.... " - 1982
372,245	3,568	6,349	83,320	5,252	72,669	3,022	29,518	11,582	51,854	1,590	.... " - 1983
361,124	3,563	9,556	51,661	4,874	65,443	3,067	29,542	9,722	52,336	1,398	.... Jan. - 1984
354,890	3,962	9,550	51,701	4,584	62,088	3,002	29,307	10,894	51,987	1,234	.... Feb.
356,640	4,127	8,046	52,595	4,469	62,052	3,363	32,103	9,228	52,720	1,027	.... Mar.
356,320	4,100	9,920	51,242	4,291	61,868	3,018	35,780	12,848	53,709	935	.... Apr.
354,733	4,204	6,494	53,207	3,560	65,211	2,959	36,233	17,431	54,168	880	.... May
357,464	4,303	8,517	55,063	4,144	65,630	2,995	36,427	16,347	54,225	837	.... June
360,724	4,430	7,646	52,595	4,044	66,401	3,056	36,650	19,802	55,371	776	..... July
361,348	4,184	5,162	54,444	4,058	65,419	3,372	36,897	21,823	54,389	747	.... Aug.
367,774	4,251	4,977	60,036	3,620	68,312	3,477	37,031	24,864	55,919	716	.... Sept.
371,107	4,722	7,105	59,523	3,173	72,989	3,482	37,149	30,169	55,858	715	.... Oct.
372,163	4,624	4,975	63,471	3,448	84,076	3,652	37,200	36,123	56,711	696	.... Nov.
415,581	4,949	2,864	89,233	4,518	91,908	3,879	36,989	14,547	58,313	608	.... Dec.
411,126	5,347	3,838	63,626	5,165	85,280	3,974	36,846	13,630	57,483	572	.... Jan. - 1985
405,608	5,718	4,293	65,914	4,683	91,191	4,222	36,935	9,140	59,605	569	.... Feb.
407,372	5,893	2,881	63,837	4,689	89,485	4,213	38,690	13,498	60,030	554	.... Mar.
410,346	5,556	5,400	65,612	3,730	92,816	4,178	41,898	11,342	60,288	509	.... Apr.
406,055	5,397	3,684	67,077	3,746	92,991	4,389	42,154	18,303	60,002	476	..(9) May
410,718	5,541	2,574	65,568	5,002	95,822	4,294	41,609	19,606	60,881	462	.... June
414,333	5,416	2,670	61,868	4,283	93,365	4,413	42,086	21,453	61,164	456	..... July
414,780	5,352	3,093	62,107	3,952	87,512	4,586	42,090	21,127	60,983	456	.... Aug.
420,848	5,616	4,827	59,555	4,332	....	4,920	42,398	....	61,189	424	.... Sept.
422,048	5,548	3,309	57,921	3,849	....	4,762	42,731	....	61,272	422	.... Oct.
421,486	6,002	2,991	70,446	3,458	....	4,517	42,907	....	62,006	415	..(9) Nov.
457,740	6,467	8,740	89,866	4,461	95,033	4,672	43,179	25,105	63,711	377	.(10) Dec.
447,466	6,585	5,451	66,683	5,228	....	4,775	43,250	....	63,832	443	..(9) Jan. - 1986
438,360	6,480	4,090	59,140	4,860	....	....	43,340	....	65,080	780	.(11) Feb.
438,350	6,350	1,280	59,700	4,860	....	....	46,030	....	68,440	1,010	.(11) Mar.

(4) Treasury bills are at face value, medium and long-term securities at book value. – (5) UIC data. – (6) Lira deposits of resident customers. – (7) Trustee accounts and residents' discrepancy has been estimated at about 350 billion lire and is ascribable entirely to short-term lending in lire. – (9) The data on liquidity had to be estimated owing to industrial action at

BANKS' PROFIT AND LOSS ACCOUNTS,

(in billions

	INTEREST RECEIVED						INTEREST PAID					Net interest income (c) = (a)-(b)
	Deposits with BI-UIC & Treasury	Domestic lending in lire	Securities & parti-cipations	Interbank accounts	Foreign currency assets	Total (a)	Domestic deposits in lire	BI-UIC financing	Interbank accounts	Foreign currency liabilities	Total (b)	
Banks and savings												
1976	832	11,632	3,153	1,836	737	18,190	10,138	128	1,446	677	12,389	5,801
1977	1,050	13,870	5,371	2,304	1,031	23,626	14,246	96	1,617	985	16,944	6,682
1978	1,307	13,497	7,337	2,229	1,416	25,786	15,367	70	1,641	1,387	18,465	7,321
1979	1,597	15,155	8,987	2,623	2,259	30,621	17,971	92	1,924	2,172	22,159	8,462
1980	1,806	23,059	10,495	3,735	4,070	43,165	23,377	107	2,989	3,819	30,292	12,873
1981	2,010	29,530	12,654	5,304	7,025	56,523	30,030	127	4,062	6,677	40,896	15,627
1982	2,285	32,519	16,783	6,623	6,511	64,721	36,542	117	5,048	6,278	47,985	16,736
1983	2,904	34,535	22,459	6,962	5,491	72,351	41,426	237	5,266	5,479	52,408	19,943
1984	3,531	37,440	23,518	6,925	7,176	78,590	43,366	397	5,364	7,225	56,352	22,238
1985 (3)	4,182	39,092	25,911	6,700	7,825	83,710	45,137	494	5,423	7,643	58,697	25,013
Banks												
1976	780	9,238	2,127	1,094	722	13,961	7,662	101	1,350	667	9,780	4,181
1977	945	10,980	3,762	1,381	979	18,047	10,577	76	1,460	943	13,056	4,991
1978	1,131	10,543	5,149	1,314	1,336	19,473	11,154	57	1,502	1,311	14,024	5,449
1979	1,331	11,683	6,213	1,557	2,113	22,897	12,744	77	1,769	2,034	16,624	6,273
1980	1,486	17,712	7,254	2,399	3,803	32,654	16,640	89	2,774	3,571	23,074	9,580
1981	1,627	22,520	9,088	3,430	6,566	43,231	21,468	108	3,768	6,243	31,587	11,644
1982	1,814	24,543	12,077	4,546	6,096	49,076	25,939	99	4,653	5,890	36,581	12,495
1983	2,260	25,862	15,664	4,808	5,077	53,671	29,099	207	4,797	5,089	39,192	14,479
1984	2,694	27,588	16,121	4,744	6,579	57,726	30,101	362	4,755	6,660	41,878	15,848
1985 (3)	3,181	28,715	18,021	4,420	7,130	61,467	31,391	459	4,748	6,997	43,595	17,872
Banks of												
1976	213	1,973	540	102	327	3,155	1,703	20	376	323	2,422	733
1977	234	2,347	802	126	389	3,898	2,093	19	384	399	2,895	1,003
1978	264	2,105	939	135	532	3,975	2,032	9	343	541	2,925	1,050
1979	288	2,277	1,011	117	858	4,551	2,111	18	385	855	3,369	1,182
1980	294	3,383	1,211	108	1,509	6,505	2,681	25	640	1,398	4,744	1,761
1981	319	4,194	1,426	163	2,656	8,758	3,499	26	681	2,507	6,713	2,045
1982	352	4,630	1,988	286	2,415	9,671	4,211	26	828	2,331	7,396	2,275
1983	407	4,694	2,198	396	1,997	9,692	4,470	40	699	1,984	7,193	2,499
1984	473	4,801	1,990	456	2,505	10,225	4,410	58	704	2,520	7,692	2,533
1985 (3)	591	4,751	2,286	460	2,688	10,776	4,704	78	574	2,639	7,995	2,781
Public-law												
1976	201	2,538	627	148	230	3,744	2,026	33	322	194	2,575	1,169
1977	253	2,759	1,199	227	320	4,758	2,805	21	341	304	3,471	1,287
1978	297	2,625	1,562	230	404	5,118	2,926	21	380	403	3,730	1,388
1979	360	2,871	1,941	341	645	6,158	3,444	29	433	605	4,511	1,647
1980	409	4,233	2,383	498	1,144	8,667	4,532	34	693	1,074	6,333	2,334
1981	448	5,328	3,190	641	1,834	11,441	5,760	47	1,101	1,759	8,667	2,774
1982	492	6,003	3,807	919	1,765	12,986	6,971	42	1,512	1,699	10,224	2,762
1983	673	6,495	5,005	1,023	1,412	14,608	7,857	126	1,710	1,449	11,142	3,466
1984	778	7,120	5,271	1,169	1,820	16,158	8,115	203	1,922	1,833	12,073	4,085
1985 (3)	875	7,176	6,197	901	2,166	17,315	8,385	272	2,047	2,131	12,835	4,480

(1) Components may not add up to totals because of rounding. As of 1983 the figures for interest on securities and position with the Bank of Italy, as well as those for "Other income", special times. – (3) Provisional.

BY CATEGORY OF BANK (1)

of lire)

Other income (d)	Other income: of which: securities transactions	Gross earnings margin (e) = (c) + (d)	Operating costs (f)	Operating costs: of which: staff costs	Operating surplus (g) = (e)-(f)	Provisions (h)	Provisions: of which: for loan losses	Extraordinary income and withdrawals from provisions (i)	Taxes (l)	Net profit (g)-(h) + (i)-(l)	Total resources	No. of staff	
banks (2)													
1,515	426	7,316	5,151	4,101	2,165	1,611	490	18	310	262	169,371	227,338	 1976
1,949	699	8,631	6,047	4,610	2,584	1,819	772	23	437	351	208,183	239,901	 1977
2,461	1,156	9,782	6,972	5,211	2,810	1,893	925	–5	464	448	250,435	249,999	 1978
2,937	1,389	11,399	8,365	6,119	3,034	2,129	1,014	120	445	580	307,772	261,505	 1979
3,708	1,625	16,581	11,204	8,206	5,377	3,705	1,631	39	881	830	372,503	274,889	 1980
5,437	2,477	21,064	13,033	9,437	8,031	5,725	1,945	145	1,208	1,243	441,537	287,420	 1981
6,452	3,353	23,188	15,061	10,433	8,127	5,005	2,352	392	2,009	1,505	507,235	293,002	 1982
7,052	3,257	26,995	18,643	13,668	8,352	4,249	2,558	206	2,565	1,744	591,493	299,879	 1983
8,448	4,363	30,686	20,852	15,018	9,834	4,686	2,555	142	2,903	2,387	662,436	302,814	 1984
9,665	5,040	34,678	23,421	16,832	11,257	5,182	2,438	827	3,659	3,243	771,837	304,090	... (3) 1985
1,166	336	5,347	3,814	3,006	1,533	1,103	420	25	240	215	130,307	172,651	 1976
1,411	478	6,402	4,395	3,341	2,007	1,365	657	2	351	293	159,889	182,352	 1977
1,727	803	7,176	5,102	3,816	2,074	1,340	759	–28	335	371	194,553	189,920	 1978
2,036	946	8,309	6,159	4,535	2,150	1,403	785	85	332	500	231,563	199,478	 1979
2,603	1,128	12,183	8,157	6,067	4,026	2,619	1,329	39	737	709	282,254	210,449	 1980
3,971	1,774	15,615	9,597	6,994	6,018	4,119	1,538	127	948	1,078	337,072	219,741	 1981
4,563	2,282	17,058	11,139	7,725	5,919	3,371	1,695	270	1,497	1,321	388,400	224,833	 1982
5,199	2,425	19,678	13,709	10,038	5,969	2,929	1,635	323	1,863	1,500	449,364	230,416	 1983
6,269	3,277	22,117	15,444	11,131	6,673	2,903	1,590	163	1,946	1,987	496,995	232,457	 1984
7,510	4,028	25,382	17,531	12,646	7,851	3,527	1,560	802	2,539	2,587	581,088	233,022	... (3) 1985
national interest													
273	56	1,006	949	773	57	84	72	41	3	11	34,445	42,438	 1976
301	83	1,304	1,065	827	239	192	144	5	33	19	39,837	43,659	 1977
333	113	1,383	1,196	925	187	149	145	10	26	22	46,241	45,106	 1978
421	159	1,603	1,400	1,076	203	236	215	66	22	11	52,237	47,241	 1979
577	220	2,338	1,847	1,390	491	362	273	19	115	33	64,921	48,464	 1980
975	373	3,020	2,088	1,578	932	872	243	69	31	98	78,305	50,097	 1981
923	386	3,198	2,448	1,769	750	560	372	171	262	99	89,975	51,373	 1982
1,116	519	3,615	2,970	2,263	645	505	452	291	317	114	98,991	51,393	 1983
1,329	640	3,862	3,171	2,383	691	424	335	179	249	197	105,556	50,850	 1984
1,670	961	4,451	3,491	2,607	960	536	289	118	330	212	119,440	50,081	... (3) 1985
banks													
385	110	1,554	1,130	905	424	343	155	–8	57	16	37,437	52,459	 1976
508	176	1,795	1,282	1,016	513	423	151	15	98	7	46,120	55,428	 1977
609	300	1,997	1,461	1,144	536	445	171	–20	47	24	56,503	56,132	 1978
662	315	2,309	1,825	1,394	484	370	172	–10	52	52	68,077	58,530	 1979
841	387	3,175	2,372	1,839	803	667	319	1	95	42	83,445	61,937	 1980
1,221	560	3,995	2,798	2,146	1,197	1,040	430	27	122	62	98,844	64,233	 1981
1,541	784	4,303	3,215	2,335	1,088	766	308	36	204	154	117,431	65,849	 1982
1,706	720	5,172	4,085	3,153	1,087	655	259	3	297	138	138,297	67,319	 1983
2,019	999	6,104	4,728	3,573	1,376	832	374	10	329	225	147,732	68,201	 1984
2,427	1,171	6,907	5,158	3,906	1,749	1,281	328	569	554	483	174,718	68,634	... (3) 1985

are not comparable with those for earlier years. – (2) Except in the item "Number of staff", excludes credit institutions which at the time were reporting for special periods and at

BANKS' PROFIT AND LOSS ACCOUNTS,

(in billions

	INTEREST RECEIVED						INTEREST PAID					Net interest income (c) = (a)-(b)
	Deposits with BI-UIC & Treasury	Domestic lending in lire	Securities & parti-cipations	Interbank accounts	Foreign currency assets	Total (a)	Domestic deposits in lire	BI-UIC financing	Interbank accounts	Foreign currency liabilities	Total (b)	
												Ordinary
1976	249	3,219	625	540	140	4,773	2,670	34	530	132	3,366	1,407
1977	306	3,956	1,113	626	217	6,218	3,730	27	592	195	4,544	1,674
1978	373	3,856	1,702	559	319	6,809	3,994	20	631	290	4,935	1,874
1979	439	4,281	2,080	632	485	7,917	4,545	20	795	456	5,816	2,101
1980	495	6,551	2,292	1,015	897	11,250	5,868	22	1,207	856	7,953	3,297
1981	541	8,414	2,875	1,367	1,583	14,780	7,601	25	1,634	1,496	10,756	4,024
1982	595	8,744	3,992	1,625	1,378	16,334	8,912	20	1,831	1,328	12,091	4,243
1983	720	9,085	5,230	1,685	1,130	17,850	9,971	28	1,901	1,152	13,052	4,798
1984	889	9,525	5,293	1,590	1,522	18,819	10,315	85	1,698	1,612	13,710	5,109
1985 (3)	1,044	10,243	5,637	1,523	1,556	20,003	10,787	92	1,592	1,544	14,015	5,988
												Cooperative
1976	117	1,508	335	304	25	2,289	1,263	14	122	18	1,417	872
1977	152	1,918	648	402	53	3,173	1,949	9	143	45	2,146	1,027
1978	197	1,957	946	390	81	3,571	2,202	7	148	77	2,434	1,137
1979	244	2,254	1,181	467	125	4,271	2,644	10	156	118	2,928	1,343
1980	288	3,545	1,368	778	253	6,232	3,559	8	234	243	4,044	2,188
1981	319	4,584	1,597	1,259	493	8,252	4,608	10	352	481	5,451	2,801
1982	375	5,166	2,290	1,716	538	10,085	5,845	11	482	532	6,870	3,215
1983	460	5,588	3,231	1,704	538	11,521	6,801	13	487	504	7,805	3,716
1984	554	6,142	3,567	1,529	732	12,524	7,261	16	431	695	8,403	4,121
1985 (3)	671	6,545	3,901	1,536	720	13,373	7,515	17	535	683	8,750	4,623
												Savings
1976	52	2,394	1,026	742	15	4,229	2,476	27	96	10	2,609	1,620
1977	105	2,890	1,609	923	52	5,579	3,669	20	157	42	3,888	1,691
1978	176	2,954	2,188	915	80	6,313	4,213	13	139	76	4,441	1,872
1979	266	3,472	2,774	1,066	146	7,724	5,227	15	155	138	5,535	2,189
1980	320	5,347	3,241	1,336	267	10,511	6,737	18	215	248	7,218	3,293
1981	383	7,010	3,566	1,874	459	13,292	8,562	19	294	434	9,309	3,983
1982	471	7,976	4,706	2,077	415	15,645	10,603	18	395	388	11,404	4,241
1983	644	8,673	6,795	2,154	414	18,680	12,327	30	469	390	13,216	5,464
1984	837	9,852	7,397	2,181	597	20,864	13,265	35	609	565	14,474	6,390
1985 (3)	1,001	10,377	7,890	2,280	695	22,243	13,746	35	675	646	15,102	7,141
												Central credit
1976	–	636	272	181	–	1,089	34	71	951	–	1,056	33
1977	1	610	519	214	1	1,345	35	34	1,183	2	1,254	91
1978	4	601	527	181	2	1,315	35	33	1,149	2	1,219	96
1979	4	44	64	195	2	309	4	2	261	3	270	39
1980	6	469	435	414	4	1,328	29	122	1,159	11	1,321	7
1981	8	650	529	567	6	1,760	14	34	1,595	18	1,661	99
1982	21	780	596	812	5	2,214	42	29	1,909	9	1,989	225
1983	41	629	773	811	12	2,266	49	86	1,922	17	2,074	192
1984	32	572	871	807	42	2,324	41	98	1,908	42	2,089	235
1985 (3)	28	433	1,003	969	73	2,506	46	88	2,042	70	2,246	260

(1) Components may not add up to totals because of rounding. As of 1983 the figures for interest on securities and position with the Bank of Italy, as well as those for "Other income", are times. – (3) Provisional.

Table a 16 *cont'd*

BY CATEGORY OF BANK (1)

of lire)

Other income (d)	of which: securities transactions	Gross earnings margin (e) = (c) + (d)	Operating costs (f)	of which: staff costs	Operating surplus (g) = (e)-(f)	Provisions (h)	of which: for loan losses	Extraordinary income and withdrawals from provisions (i)	Taxes (l)	Net profit (g)-(h) + (i)-(l)	Total resources	No. of staff	
credit banks (2)													
357	136	1,764	1,145	872	619	405	118	−3	88	123	39,691	50,521	 1976
410	166	2,084	1,335	972	749	427	227	−10	136	176	49,422	54,065	 1977
538	298	2,412	1,586	1,130	826	437	293	−5	167	217	60,725	57,061	 1978
651	353	2,752	1,886	1,337	866	461	270	35	155	285	73,153	59,895	 1979
805	392	4,102	2,516	1,823	1,586	878	442	36	323	421	86,867	64,109	 1980
1,241	655	5,265	2,998	2,095	2,267	1,196	484	30	490	611	103,350	67,636	 1981
1,403	792	5,646	3,386	2,260	2,260	1,083	548	57	585	649	113,331	69,137	 1982
1,549	818	6,347	4,049	2,808	2,298	957	452	32	653	720	130,764	70,381	 1983
1,896	1,138	7,005	4,600	3,177	2,405	832	464	−38	677	858	147,809	71,246	 1984
2,309	1,385	8,297	5,457	3,777	2,840	932	524	66	885	1,089	175,318	71,187	... (3) 1985
banks													
151	34	1,023	590	456	433	271	75	−5	92	65	18,734	27,233	 1976
192	53	1,219	713	526	506	323	135	−8	84	91	24,510	29,200	 1977
247	92	1,384	859	617	525	309	150	−13	95	108	31,084	31,621	 1978
302	119	1,645	1,048	728	597	336	128	−6	103	152	38,096	33,812	 1979
380	129	2,568	1,422	1,015	1,146	712	295	−17	204	213	47,021	35,939	 1980
534	186	3,335	1,713	1,175	1,622	1,011	381	1	305	307	56,573	37,775	 1981
696	320	3,911	2,090	1,361	1,821	962	467	6	446	419	67,663	38,474	 1982
828	368	4,544	2,605	1,814	1,939	812	472	−3	596	528	81,312	41,323	 1983
1,025	500	5,146	2,945	1,998	2,201	815	417	12	691	707	95,898	42,160	 1984
1,104	511	5,727	3,425	2,356	2,302	778	419	49	770	803	111,612	43,120	... (3) 1985
banks													
349	90	1,969	1,337	1,095	632	508	70	−7	70	47	39,064	54,687	 1976
538	221	2,229	1,652	1,269	577	454	115	21	86	58	48,294	57,549	 1977
734	353	2,606	1,870	1,395	736	553	166	23	129	77	55,882	60,079	 1978
901	443	3,090	2,206	1,584	884	726	229	35	113	80	76,209	62,027	 1979
1,105	497	4,398	3,047	2,139	1,351	1,086	302	–	144	121	90,249	64,440	 1980
1,466	703	5,449	3,436	2,443	2,013	1,606	407	18	260	165	104,465	67,679	 1981
1,889	1,071	6,130	3,922	2,708	2,208	1,634	657	122	512	184	118,835	68,169	 1982
1,853	832	7,317	4,934	3,630	2,383	1,320	923	−117	702	244	142,129	69,463	 1983
2,179	1,086	8,569	5,408	3,887	3,161	1,783	965	−21	957	400	165,441	70,357	 1984
2,155	1,012	9,296	5,890	4,186	3,406	1,655	878	25	1,120	656	190,749	71,068	... (3) 1985
institutions (2)													
30	24	63	37	20	26	12	1	–	1	13	8,223	821	 1976
−220	−227	−129	38	20	−167	62	54	199	5	−35	9,817	885	 1977
−216	−224	−120	42	22	−162	56	52	198	6	−26	10,040	914	 1978
15	8	54	35	17	19	8	–	1	2	10	3,224	695	 1979
53	36	60	81	38	−21	16	−26	23	2	−16	14,052	1,140	 1980
94	72	193	90	46	103	51	1	–	3	49	16,248	1,191	 1981
91	66	316	113	51	203	176	24	38	7	58	18,194	1,284	 1982
149	92	341	150	72	191	100	62	−6	40	45	18,986	1,345	 1983
135	100	370	155	80	215	100	44	6	48	73	18,906	1,356	 1984
140	114	400	177	84	223	80	62	52	78	117	22,492	1,371	... (3) 1985

not comparable with those for earlier years. – (2) Except in the item "Number of staff", excludes credit institutions which at the time were reporting for special periods and at special

ASSETS AND LIABILITIES OF THE

(billions

	ASSETS										
	Cash and deposits	Loans					Loans on behalf of the Treasury	Own portfolio (5)			TOTAL
		Domestic	Financing of stockpiling	Foreign		Total		Government securities	Bonds	Shares & participations	
				Buyer credits	Credits to non-residents						
	(2)	(3)	(4)						(6)		
1976 - Dec.	9,105	42,043	552	1,427	345	44,367	13,209	568	618	274	68,141
1977 - "	8,038	47,915	568	1,704	319	50,506	12,959	1,283	468	317	73,571
1978 - "	8,384	54,445	677	1,762	325	57,209	12,670	1,733	558	394	80,948
1979 - "	5,607	60,253	682	1,923	233	63,091	12,059	2,202	510	734	84,203
1980 - "	6,122	68,644	714	2,588	228	72,174	11,403	2,205	596	856	93,356
1981 - "	4,854	81,877	591	3,196	441	86,105	10,572	2,860	2,001	1,145	107,537
1982 - "	5,452	96,529	627	3,916	443	101,515	9,913	8,149	2,229	1,702	128,960
1983 - "	5,195	109,934	727	4,321	372	115,354	9,684	11,409	2,356	2,023	146,021
1984 - Jan.	6,266	109,583	727	4,148	337	114,795	9,222	12,432	2,356	2,023	147,094
Feb.	4,943	110,216	727	3,996	325	115,264	9,219	14,500	2,356	2,023	148,305
Mar.	5,099	111,370	739	3,974	319	116,402	9,219	14,904	2,609	2,028	150,261
Apr.	5,006	111,961	739	4,096	322	117,118	9,221	13,448	2,609	2,028	149,430
May	4,013	112,714	739	4,108	300	117,861	9,216	13,060	2,609	2,028	148,787
June	4,833	113,293	752	4,085	284	118,414	8,818	13,110	2,381	2,181	149,737
July	4,180	114,622	752	3,951	250	119,575	8,817	14,564	2,381	2,181	151,698
Aug.	4,244	115,983	752	4,014	236	120,985	8,816	15,346	2,381	2,181	153,953
Sept.	4,468	116,776	758	4,153	236	121,923	8,819	14,860	2,473	2,236	154,779
Oct.	3,661	119,058	758	4,192	232	124,240	8,819	14,595	2,473	2,236	156,024
Nov.	3,802	120,770	758	4,311	242	126,081	8,802	14,764	2,473	2,236	158,158
Dec.	4,964	125,300	766	4,214	371	130,651	9,193	15,023	2,132	2,409	164,372
1985 - Jan.	5,724	124,966	766	4,067	375	130,174	8,703	15,969	2,132	2,409	165,111
Feb.	5,347	125,984	766	4,320	359	131,429	8,705	16,972	2,132	2,409	166,994
Mar.	5,435	127,461	778	4,211	342	132,792	8,703	17,162	2,562	2,423	169,077
Apr.	4,222	127,864	778	4,197	306	133,145	8,703	16,319	2,562	2,423	167,374
May	4,410	127,703	778	4,259	298	133,038	8,697	16,141	2,562	2,423	167,271
June	5,482	127,131	791	4,192	295	132,409	8,271	16,929	2,826	2,476	168,393
July	5,407	127,798	791	3,939	272	132,800	8,226	19,029	2,826	2,476	170,764
Aug.	5,080	129,284	791	3,918	265	134,258	8,225	18,905	2,826	2,476	171,770
Sept.	5,512	129,930	799	3,808	249	134,786	8,224	18,566	2,975	2,572	172,635
Oct.	4,694	130,431	799	3,768	247	135,245	8,223	18,667	2,975	2,572	172,376
Nov.	4,206	131,849	799	3,746	244	136,638	8,205	18,144	2,975	2,572	172,740
Dec.	4,601	135,988	806	3,543	238	140,575	8,593	16,441	2,645	2,744	175,599
1986 - Jan. (12)......	5,329	136,566	806	3,302	255	140,929	8,060	17,037	2,645	2,744	176,744
Feb. (12)	5,585	138,559	806	3,202	295	142,862	8,057	16,108	2,645	2,744	178,001

(1) From January 1983 onwards includes the agricultural credit section of Banco di Sardegna and from October 1984 the agricultural credit section of Istituto Bancario S. Paolo di Torino. – (2) voluntary stockpiling operations, equal to 93,3 billion lire at that date. From September 1983 onwards includes the future instalments on the bad debts of all the institutions (previously only those of the (5) Including securities in foreign currencies. – (6) From the fourth quarter of 1981 onwards includes securities issued by the Deposits and Loans Fund totalling 1,275.3 billion lire at end-December (8) Includes the proceeds of bond issues disbursed to special credit institutions. – (9) Includes compensatory loans in foreign currency deposited with the Bank of Italy. – (10) Paid-up capital include provisions of a reserve nature created out of gross profits and on which third parties have no claim. At end-December 1979 equity capital according to the new definition, which includes certain

Table a 17

SPECIAL CREDIT INSTITUTIONS (1)

of lire)

LIABILITIES											
Bonds		Certificates of deposit (7)	Rediscounts	Short-term financing	Public funds	Mediocredito centrale funds (8)	Foreign currency loans (9)	Equity capital (10)	Other	TOTAL (11)	
On behalf of the Treasury	Other										
13,589	38,172	4,269	505	1,522	2,056	1,418	5,682	2,889	45	70,147	.... Dec. - 1976
13,367	43,731	5,193	524	1,697	2,097	1,409	5,406	3,475	26	76,925	.... " - 1977
12,970	49,436	6,519	575	2,398	2,177	1,452	5,081	4,222	20	84,850	.... " - 1978
12,280	54,693	6,695	595	2,756	2,479	1,515	3,074	5,339	23	89,449	.... " - 1979
11,714	60,979	7,444	602	3,620	2,680	1,697	4,007	6,772	25	99,540	.... " - 1980
10,905	68,863	9,515	696	5,034	3,091	2,097	5,953	8,360	34	114,548	.... " - 1981
10,015	77,172	18,060	699	4,230	3,712	2,379	9,605	10,028	22	135,922	.... " - 1982
9,120	85,134	19,264	818	4,540	4,696	2,436	13,965	12,612	31	152,616	.... " - 1983
8,626	84,425	19,062	818	4,159	4,707	2,388	14,087	12,612	31	150,915	.... Jan. - 1984
8,613	84,744	19,441	818	4,442	4,516	2,440	14,069	12,612	31	151,726	.... Feb.
8,553	85,147	19,891	861	4,038	4,545	2,413	14,392	13,413	34	153,287	.... Mar.
8,551	84,583	20,153	861	4,041	4,527	2,407	14,701	13,413	34	153,271	.... Apr.
8,550	84,665	20,476	861	4,040	4,508	2,408	14,843	13,413	34	153,798	.... May
8,543	85,617	21,178	890	4,123	4,394	2,426	15,149	14,596	42	156,958	.... June
8,199	85,282	21,203	890	3,778	4,394	2,302	15,616	14,596	42	156,302	.... July
8,183	85,495	21,102	890	3,984	4,507	2,350	16,067	14,596	42	157,216	.... Aug.
8,179	85,898	21,000	848	4,059	4,547	2,393	16,619	14,893	37	158,473	...... Sept.
8,162	86,789	21,052	848	4,353	4,586	2,400	17,057	14,893	37	160,177	.... Oct.
8,160	87,696	21,617	848	4,906	4,898	2,404	17,256	14,893	37	162,715	.... Nov.
8,159	89,554	23,480	941	5,620	4,771	2,422	17,852	15,244	46	168,089	.... Dec.
7,678	89,229	23,705	941	4,836	4,746	2,382	17,885	15,244	46	166,692	.... Jan. - 1985
7,638	89,993	24,424	941	4,317	4,759	2,402	18,442	15,244	46	168,206	.... Feb.
7,571	90,738	24,988	943	4,335	4,861	2,390	18,474	16,015	45	170,360	.... Mar.
7,568	90,228	24,857	943	4,104	4,822	2,390	18,758	16,015	45	169,730	.... Apr.
7,566	90,590	24,816	943	4,352	4,793	2,391	18,736	16,015	45	170,247	.... May
7,566	92,369	25,521	863	4,101	4,855	2,350	18,727	17,135	59	173,546	.... June
7,253	92,037	25,397	863	3,652	4,980	2,342	18,967	17,135	59	172,685	.... July
7,180	92,035	25,057	863	3,850	5,305	2,376	19,265	17,135	59	173,125	.... Aug.
7,174	93,603	24,634	1,017	3,180	5,442	2,397	19,263	17,573	41	174,324	...... Sept.
7,147	93,562	24,593	1,017	4,015	5,469	2,467	19,550	17,573	41	175,434	.... Oct.
7,145	93,802	24,604	1,017	4,318	5,483	2,509	19,742	17,573	41	176,234	.... Nov.
7,146	95,022	25,549	889	6,626	5,364	2,521	20,053	18,105	43	181,318	.... Dec.
6,546	95,118	25,743	889	5,399	5,616	2,477	19,844	18,105	43	179,780	.... (12) Jan. - 1986
6,524	95,194	26,039	889	5,288	5,790	2,522	19,520	18,105	43	179,914	.... (12) Feb.

Including liquid funds in foreign currencies. The volume of deposits with the Bank of Italy is derived from the accounts for that institution. – (3) From December 1981 onwards includes financing of real estate institutions and public works sections). – (4) From December 1981 onwards excludes financing of voluntary stockpiling operations, which is included among agricultural working credit. – 1981, 1,510.2 billion at end-1982, 1,363.1 billion at end-1983, 1,200.8 billion at end-1984 and 1,034.4 billion at end-1985. – (7) Includes savings certificates and other medium-term deposits. – and reserves. As from March 1980 the components of equity capital have been classified as "Own funds", comprising capital and reserves created out of net profits, and "Other equity funds", which items previously excluded, stood at 5,645.8 billion lire net of uncalled capital. – (11) Refers to the items defined as fund-raising plus bonds issued on behalf of the Treasury. – (12) Estimated.

(billions

	Treasury bills (1)	BONDS AND										
		Public sector									Special credit	
		Government securities					Local government agencies	Autonomons government agencies	Bonds on behalf of Treasury	Total	Industrial	Public works
		Variable rate Treasury credit certificates	Treasury bonds	Other certificates	Bonds of Deposits & Loans Fund	Other						
												Gross
1976	46,500	–	1,500	2,489	503	309	–	100	238	*5,139*	3,452	829
1977	66,400	5,500	1,655	6,585	4,851	127	–	300	366	*19,384*	3,718	1,035
1978	62,750	9,684	10,499	1,484	1,795	–	–	200	244	*23,906*	3,761	1,523
1979	58,250	15,250	4,824	244	168	–	–	100	–	*20,586*	3,740	1,414
1980	127,500	12,930	21	–	–	–	–	–	147	*13,098*	5,375	768
1981	198,041	9,200	5,500	2,685	1,275	–	–	–	–	*18,660*	6,478	1,011
1982	273,278	47,250	3,050	1,429	429	84	–	–	–	*52,242*	7,153	1,536
1983	266,351	74,650	13,000	1,632	–	–	–	2,000	–	*91,282*	6,152	2,735
1984	227,747	95,250	17,750	1,688	–	–	–	1,800	–	*116,488*	5,490	2,791
1985	256,281	97,210	17,289	13,775	–	–	–	2,500	–	*130,774*	8,487	1,322
												Re
1976	38,595	–	–	344	73	152	21	104	509	*1,203*	1,154	86
1977	61,605	–	546	425	87	199	23	120	587	*1,987*	1,544	109
1978	56,869	–	806	740	759	189	26	151	640	*3,311*	1,907	150
1979	48,428	5,000	3,167	1,077	782	163	33	165	691	*11,078*	2,163	192
1980	102,000	10,184	1,716	1,209	792	124	35	188	712	*14,960*	2,706	238
1981	164,258	6,250	1,500	1,196	800	137	38	205	810	*10,936*	3,666	288
1982	240,674	19,000	4,661	1,772	980	144	40	238	889	*27,724*	4,602	338
1983	255,280	7,130	9,198	1,764	1,000	122	43	257	896	*20,410*	4,827	417
1984	218,447	38,250	9,171	2,558	1,010	108	46	271	961	*52,375*	5,758	594
1985	243,100	17,100	13,000	2,290	1,022	82	50	284	1,014	*34,842*	6,737	761
												Premiums, discounts
1976	–	–	23	219	96	30	–	10	49	*427*	591	131
1977	–	–	157	986	806	27	–	30	67	*2,073*	463	133
1978	–	–	232	199	298	–	–	16	34	*779*	323	202
1979	–	31	116	33	21	–	–	5	–	*206*	135	122
1980	–	55	1	–	–	–	–	–	9	*65*	256	78
1981	–	134	92	–	–	–	–	–	–	*226*	172	36
1982	–	873	19	–	–	–	–	–	–	*892*	83	28
1983	–	868	62	–	–	–	–	–	–	*930*	92	72
1984	–	262	146	–	–	–	–	–	–	*408*	26	13
1985	–	1,543	314	–	–	–	–	–	–	*1,857*	72	7
												Net
1976	7,905	–	1,477	1,926	334	127	–21	–14	–320	*3,509*	1,707	612
1977	4,795	5,500	952	5,174	3,958	–99	–23	150	–288	*15,324*	1,711	793
1978	5,881	9,684	9,461	545	738	–189	–26	33	–430	*19,816*	1,531	1,171
1979	9,822	10,219	1,541	–866	–635	–163	–33	–70	–691	*9,302*	1,442	1,100
1980	25,500	2,691	–1,696	–1,209	–792	–124	–35	–188	–574	*–1,927*	2,413	452
1981	33,783	2,816	3,908	1,489	475	–137	–38	–205	–810	*7,498*	2,640	687
1982	32,604	27,377	–1,630	–343	–551	–60	–40	–238	–889	*23,626*	2,468	1,170
1983	11,071	66,652	3,740	–132	–1,000	–122	–43	1,743	–896	*69,942*	1,233	2,246
1984	9,300	56,738	8,433	–870	–1,010	–108	–46	1,529	–961	*63,705*	–294	2,184
1985	13,181	78,567	3,975	11,485	–1,022	–82	–50	2,216	–1,014	*94,075*	1,678	554

(1) For these securities the net issues are obtained by deducting redemptions from gross issues.

GROSS AND NET ISSUES OF SECURITIES

of lire)

GOVERNMENT SECURITIES											
institutions		Government agencies and firms									
Real estate	Total	ENEL	ENI	IRI EFIM	Motor-ways (IRI)	Private firms	International institutions	Total	TOTAL bonds & government securities	SHARES	
issues											
2,810	*7,091*	1,202	–	100	100	163	–	*1,565*	*13,795*	2,135	 1976
2,981	*7,734*	1,298	200	157	–	256	–	*1,911*	*29,029*	2,357	 1977
3,088	*8,372*	1,300	65	140	–	258	–	*1,763*	*34,041*	3,608	 1978
3,240	*8,394*	625	–	610	–	100	–	*1,335*	*30,315*	3,893	 1979
4,172	*10,315*	1,196	–	–	–	171	50	*1,417*	*24,830*	4,133	 1980
5,372	*12,861*	352	742	502	–	807	–	*2,403*	*33,924*	8,812	 1981
5,782	*14,471*	2,386	611	2,300	–	893	–	*6,190*	*72,903*	6,892	 1982
5,700	*14,587*	2,471	352	300	–	1,175	–	*4,298*	*110,167*	12,534	 1983
4,257	*12,538*	2,774	–	750	–	802	150	*4,476*	*133,502*	11,784	 1984
5,253	*15,062*	2,777	125	873	–	1,148	550	*5,473*	*151,309*	14,977	 1985
demptions											
533	*1,773*	236	80	83	47	81	13	*540*	*3,516*	–	 1976
610	*2,263*	260	117	52	53	81	13	*576*	*4,826*	–	 1977
647	*2,704*	387	95	83	86	81	13	*745*	*6,760*	–	 1978
841	*3,196*	404	116	112	103	84	18	*837*	*15,111*	–	 1979
1,036	*3,980*	725	116	127	107	99	13	*1,187*	*20,127*	–	 1980
976	*4,930*	1,104	117	123	111	98	13	*1,566*	*17,432*	–	 1981
1,136	*6,076*	1,160	63	131	115	115	19	*1,603*	*35,403*	–	 1982
1,411	*6,655*	1,388	64	246	91	115	19	*1,923*	*28,988*	–	 1983
1,810	*8,162*	1,729	154	306	96	135	18	*2,438*	*62,975*	–	 1984
2,282	*9,780*	2,108	228	177	103	463	32	*3,111*	*47,733*	–	 1985
and double counting											
433	*1,155*	58	–	7	12	6	–	*83*	*1,665*	263	 1976
462	*1,058*	66	26	20	–	–	–	*112*	*3,243*	511	 1977
381	*906*	46	4	7	–	–	–	*57*	*1,742*	623	 1978
286	*543*	12	–	22	–	–	–	*34*	*783*	1,161	 1979
353	*687*	–	–	–	–	–	4	*4*	*756*	1,048	 1980
215	*423*	4	3	22	–	1	–	*30*	*679*	1,626	 1981
137	*248*	12	5	–	–	–	–	*17*	*1,157*	888	 1982
128	*292*	1	–	–	–	–	–	*1*	*1,223*	1,635	 1983
22	*61*	–	–	–	–	–	3	*3*	*472*	2,010	 1984
25	*104*	–	–	–	–	–	10	*10*	*1,971*	2,757	 1985
issues											
1,844	*4,163*	908	–80	10	41	76	–13	*942*	*8,614*	1,872	 1976
1,909	*4,413*	972	57	85	–53	175	–13	*1,223*	*20,960*	1,846	 1977
2,060	*4,762*	867	–34	50	–86	177	–13	*961*	*25,539*	2,985	 1978
2,113	*4,655*	209	–116	476	–103	16	–18	*464*	*14,421*	2,732	 1979
2,783	*5,648*	471	–116	–127	–107	72	33	*226*	*3,947*	3,085	 1980
4,181	*7,508*	–756	622	357	–111	708	–13	*807*	*15,813*	7,186	 1981
4,509	*8,147*	1,214	543	2,169	–115	778	–19	*4,570*	*36,343*	6,004	 1982
4,161	*7,640*	1,082	288	54	–91	1,060	–19	*2,374*	*79,956*	10,899	 1983
2,425	*4,315*	1,045	–154	444	–96	667	129	*2,035*	*70,055*	9,774	 1984
2,946	*5,178*	669	–103	696	–103	685	508	*2,352*	*101,605*	12,220	 1985

SOURCES AND USES OF MONETARY BASE (1)

(changes in billions of lire)

	SOURCES								TOTAL MONETARY BASE	USES				
	FOREIGN SECTOR			TREASURY			REFI-NANCING	OTHER SECTORS		NON-STATE SECTOR	BANK RESERVES			
	Balance of payments	Banks' net external position	TOTAL (2)	Borrowing require-ment	Other financing (3)	TOTAL					Compul-sory reserves	Non-interest-bearing deposit against excess lending	Excess reserves	TOTAL
1976	–1,531	2,647	1,102	14,867	5,332	9,535	–1,656	–4,018	*4,963*	1,691	4,415	–	–1,144	3,271
1977	1,730	3,425	5,140	22,567	26,543	–3,976	227	5,003	*6,395*	1,835	3,664	–	896	4,560
1978	6,997	–1,067	5,911	34,305	29,321	4,984	–56	–979	*9,860*	2,936	5,076	–	1,848	6,924
1979	1,824	1,054	2,868	30,403	29,643	760	2,624	689	*6,941*	2,631	5,508	–	–1,198	4,310
1980	–6,258	6,932	708	37,018	27,278	9,740	–2,576	–2	*7,869*	3,670	3,046	626	527	4,199
1981	1,533	–1,521	25	53,293	39,060	14,233	119	–5,738	*8,639*	4,430	2,946	821	442	4,209
1982	–2,521	–3,062	–5,647	72,702	60,026	12,676	638	2,670	*10,336*	3,528	8,544	–519	–1,218	6,808
1983	3,793	4,994	8,840	88,257	83,743	4,514	–3	–747	*12,604*	4,081	9,092	–927	359	8,523
1984	57	5,138	5,141	95,387	85,360	10,027	–218	–1,104	*13,847*	3,861	8,855	–2	1,133	9,986
1985	–8,352	–5,398	–13,735	122,816	95,298	27,518	5,881	–589	*19,075*	4,002	12,213	–	2,859	15,072
1984 - Jan.	–750	579	–199	2,435	–2,256	4,691	1,525	–657	*5,360*	–2,795	9,005	–	–850	8,155
Feb.	–508	–626	–1,150	6,597	7,859	–1,262	–6	88	*–2,331*	–214	–1,690	–2	–425	–2,117
Mar.	–1,964	833	–1,284	9,392	7,719	1,673	–1,502	727	*–386*	724	–1,298	–	187	–1,110
Apr.	750	451	1,372	9,300	10,035	–736	1,870	–2,198	*308*	267	–79	–	121	41
May	–1,569	2,739	1,165	7,731	8,259	–528	–1,952	447	*–867*	–333	–918	–	383	–535
June	–185	790	586	2,822	5,409	–2,587	2,298	1,132	*1,429*	1,354	–491	–	566	75
July	1,864	–78	1,783	8,053	7,076	977	–635	–1,060	*1,066*	1,326	765	–	–1,025	–260
Aug.	1,682	–655	1,026	7,165	6,060	1,105	–1,624	–832	*–325*	–1,327	817	–	185	1,001
Sept.	–437	198	–238	10,164	11,109	–945	–182	1,243	*–121*	455	204	–	–780	–576
Oct.	1,258	–626	631	9,331	8,890	442	2,127	–803	*2,396*	–801	1,587	–	1,610	3,197
Nov.	2,638	294	2,932	11,614	7,851	3,762	–2,126	–1,252	*3,316*	1,045	729	–	1,542	2,271
Dec.	–2,722	1,239	–1,483	10,784	7,349	3,435	–9	2,062	*4,004*	4,161	224	–	–381	–156
1985 - Jan.	160	498	663	5,247	–1,316	6,563	976	–969	*7,233*	–2,579	10,934	–	–1,122	9,812
Feb.	–1,595	173	–1,327	9,213	10,001	–788	455	96	*–1,565*	–267	–571	–	–728	–1,298
Mar.	–2,937	–905	–3,941	13,403	9,042	4,361	–1,414	44	*–950*	1,191	–1,437	–	–703	–2,141
Apr.	–3,002	2,979	–23	10,025	11,708	–1,683	2,521	–1,210	*–394*	–857	–67	–	529	463
May(4)	496	797	1,294	9,694	7,036	2,659	–1,716	–895	*1,341*	333	40	–	968	1,009
June	1,135	649	1,781	13,107	14,488	–1,381	–1,111	1,609	*898*	1,914	–914	–	–102	–1,016
July	1,229	–1,466	–248	10,560	7,521	3,039	97	–1,035	*1,854*	1,286	1,409	–	–841	568
Aug.	1,310	–1,805	–465	7,442	7,585	–144	426	–463	*–646*	–1,193	962	–	–415	547
Sept.	–1,424	–1,026	–2,463	14,717	14,075	642	1,735	–3	*–90*	–209	47	–	72	119
Oct.	–537	–1,262	–1,801	7,243	1,802	5,441	–1,520	–266	*1,855*	–258	1,617	–	496	2,113
Nov.(4)	–1,676	–945	–2,620	13,931	8,144	5,786	–320	–191	*2,655*	1,227	414	–	1,014	1,428
Dec.	–1,511	–3,085	–4,585	8,234	5,212	3,022	5,751	2,696	*6,883*	3,415	–221	–	3,689	3,468

(1) Rounding may cause discrepancies in totals. – (2) The creation of monetary base by the foreign sector does not tally with the sum of the items indicated owing to differences between the balance-of-payments statistics and the consolidated balance sheet of BI-UIC and to the inclusion of the convertible currencies of banks up to January 1983. – (3) Securities sold in the market (excluding those purchased with advances under the Ministerial Decree of 27.9.74), P.O. deposits, foreign loans, the social security institutions' deposits with the Treasury, indemnities lodged with the Deposits and Loans Fund and loans granted by banks and special credit institutions to autonomous government agencies. – (4) The figures do not tally with the BI-UIC accounts since they had to be estimated owing to industrial action at the Bank of Italy.

Table a 20

INTEREST RATES: BANK OF ITALY OPERATIONS

(percentages)

OFFICIAL

	Current accounts (1)			Bill discounting		
		Tied				
	At sight	8-day	Compulsory reserves (3)	Ordinary bills (base rate)	Agricultural working and improvement credits (4)	Ordinary advances
At 1 Jan. 1958	0.50	1.50	4.25	4.00	4.00	4.00
From: 7 June 1958	»	»	3.75	3.50	3.50	3.50
14 Aug. 1969	»	»	»	4.00	»	4.00
9 Mar. 1970	»	»	»	5.50	»	5.50
1 Oct. 1970	»	»	5.50	»	»	»
11 Jan. 1971	»	»	»	»	»	5.00
5 Apr. 1971	»	»	»	5.00	»	»
14 Oct. 1971	»	»	»	4.50	»	4.00
10 Apr. 1972	»	1.00	»	4.00	»	3.50
17 Sept. 1973	»	»	»	6.50	6.50	6.50
20 Mar. 1974	»	»	»	9.00	9.00	9.00
27 Dec. 1974	»	»	»	8.00	8.00	8.00
28 May 1975	»	»	»	7.00	7.00	7.00
15 Sept. 1975	»	»	»	6.00	6.00	6.00
2 Feb. 1976	»	»	»	7.00	7.00	7.00
25 Feb. 1976	»	»	»	8.00	»	8.00
18 Mar. 1976	»	»	»	12.00	»	12.00
4 Oct. 1976	»	»	»	15.00	»	15.00
13 June 1977	»	»	»	13.00	»	13.00
29 Aug. 1977	»	»	»	11.50	»	11.50
4 Sept. 1978	»	»	»	10.50	»	10.50
8 Oct. 1979	»	»	»	12.00	»	12.00
6 Dec. 1979	»	»	»	15.00	»	15.00
29 Sept. 1980	»	»	»	16.50	»	16.50
23 Mar. 1981	»	»	»	19.00	9.50	19.00
25 Aug. 1982	»	»	»	18.00	»	18.00
11 Apr. 1983	»	»	»	17.00	9.00	17.00
16 Feb. 1984	»	»	»	16.00	8.50	16.00
7 May 1984	»	»	»	15.50	»	15.50
4 Sept. 1984	»	»	»	16.50	»	16.50
4 Jan. 1985	»	»	»	15.50	»	15.50
8 Nov. 1985	»	»	»	15.00	8.00	15.00
22 Mar. 1986	»	»	»	14.00	7.50	14.00
25 Apr. 1986	»	»	»	13.00	7.00	13.00
27 May 1986	»	»	»	12.00	6.50	12.00

EFFECTIVE

		Repurchase agreements			
		Purchases		Sales	
	Fixed term advances (2)	Minimum	Average	Maximum	Average
1984 - Jan.	19.96	17.00	17.83	–	–
Feb.	18.52	15.20	16.63	–	–
Mar.	17.45	14.50	16.07	–	–
Apr.	16.65	15.00	15.74	–	–
May	16.92	14.60	15.12	–	–
June	16.53	–	–	–	–
July	16.49	14.60	15.07	–	–
Aug.	18.50	–	–	–	–
Sept.	17.36	–	–	16.00	15.79
Oct.	16.50	–	–	16.00	15.29
Nov.	17.47	–	–	–	–
Dec.	17.48	14.50	15.66	14.75	14.11
1985 - Jan.	15.95	16.30	16.65	13.10	12.94
Feb.	16.68	–	–	12.60	12.35
Mar.	17.10	–	–	12.45	12.30
Apr.	16.04	–	–	14.10	13.28
May	16.75	–	–	14.00	13.62
June	15.85	15.55	15.69	14.00	13.54
July	15.60	14.55	14.69	14.20	13.29
Aug.	17.69	–	–	14.00	13.45
Sept.	16.58	–	–	13.95	13.53
Oct.	17.19	15.05	16.20	–	–
Nov.	16.41	15.10	15.61	–	–
Dec.	16.17	15.50	16.54	–	–
1986 - Jan.	16.97	15.25	17.88	–	–
Feb.	16.76	17.85	18.71	–	–
Mar.	16.99	15.25	17.26	–	–
Apr.	13.31	12.00	13.47	–	–

(1) Current accounts of banks, social security institutions, insurance companies and, as from 1 January 1963, central credit institutions, special credit institutions, and public corporations. Until 10 April 1972 there was also provision for 15-day, 3-month and 6-month tied accounts at 2, 2.50 and 2.75%, respectively. – (2) From 24 March 1969 onwards the average rate of interest, weighted in accordance with the penalty of 0.50 percentage points for each new transaction occurring within 6 months of the preceding one up to a maximum of 1.50 points over the base rate. On 18 June 1973 the penalty was increased to 1 percentage point and the maximum to 3 points. From 31 December 1973 onwards 3, 2 or 1 point penalties have been applied to each transaction occurring within 90, 120 or 150 days of the preceding transaction (between 27 December 1974 and 27 May 1975 the penalties were 3.5, 2.5 and 1.5 points respectively); as from 16 February 1984 the relevant periods were reduced to 5, 15 and 30 days; on 8 November 1985 the penalties were reduced to 2.25, 1.25 and 0.50 points. – (3) Since 28 December 1982 the rate of interest on the proportion of reserves corresponding to the ratio of certificates of deposit to total funds subject to reserve requirements has been fixed at 9.50%. – (4) From 31 January 1972 the rate of interest on operations connected with compulsory stockpiling and state purchases of grain was fixed at 1 per cent.

Table a 21

MONEY MARKET AND BANK INTEREST RATES (1)

(percentages)

	TREASURY BILL YIELDS (2)				BANK INTEREST RATES										
	3-month bills	6-month bills	12-month bills	Average (3)	Interbank accounts (4) (5)	Deposits (6)	Loans (7)		Deposits (4)			Loans (4)			ABI prime rate (8)
							In lire	Total	Maximum	Normal	Average	Minimum	Normal	Average	
1976	17.81	16.49	14.25	16.63	–	10.95	17.73	17.33	–	–	–	–	–	–	17.67
1977	14.87	15.42	15.35	15.24	–	12.26	19.53	18.58	–	–	–	–	–	–	18.41
1978	11.47	12.18	12.51	11.99	–	10.66	16.86	16.00	–	–	–	–	–	–	15.71
1979	13.66	12.14	12.57	12.51	11.71	10.24	15.96	15.43	12.39	9.29	–	14.64	17.95	–	15.43
1980	15.94	15.98	15.47	15.92	16.77	11.79	20.32	19.41	14.86	10.88	–	19.03	22.14	–	19.93
1981	19.63	19.84	19.12	19.70	19.31	13.89	22.89	21.83	17.60	12.55	–	21.44	24.70	–	22.13
1982	19.38	19.37	19.43	19.44	19.91	15.03	23.08	21.65	18.82	13.44	–	21.62	25.03	–	21.54
1983	17.83	17.77	18.05	17.89	18.31	14.24	21.24	19.58	17.62	12.47	–	19.44	23.46	–	19.19
1984	15.30	15.29	15.43	15.37	17.27	12.93	19.07	17.73	16.14	11.75	–	17.64	22.23	–	17.67
1985	13.86	13.73	13.63	13.71	15.25	11.66	17.51	16.23	14.48	10.39	–	16.36	21.01	–	16.55
1984 - Jan.	16.81	16.55	16.84	16.72	18.04	–	–	–	17.12	12.13	–	18.70	23.03	–	18.50
Feb.	15.79	15.81	16.00	15.91	17.82	–	–	–	16.93	12.07	–	18.52	22.90	–	18.50
Mar.	15.66	15.61	15.81	15.71	17.41	13.22	19.78	18.38	16.39	11.72	–	17.85	22.37	–	17.50
Apr.	15.60	15.45	15.67	15.57	17.35	–	–	–	16.26	11.64	–	17.57	22.17	–	17.50
May	14.95	14.99	15.34	15.16	17.10	–	–	–	16.09	11.60	–	17.37	22.03	–	17.00
June	14.71	14.86	15.21	15.02	16.86	12.80	18.93	17.61	15.86	11.64	–	17.11	21.87	–	17.00
July	14.71	14.99	15.21	15.06	16.79	–	–	–	15.81	11.60	–	17.01	21.76	–	17.00
Aug.	14.95	14.99	15.21	15.08	16.72	–	–	–	15.78	11.67	–	16.96	21.71	–	17.00
Sept.	15.42	15.39	15.21	15.34	17.20	12.76	18.72	17.43	15.79	11.70	–	17.44	22.10	–	18.00
Oct.	15.27	15.30	15.14	15.23	17.31	–	–	–	15.85	11.70	–	17.71	22.30	–	18.00
Nov.	14.95	14.90	14.89	14.90	17.31	–	–	–	15.90	11.73	–	17.72	22.29	–	18.00
Dec.	14.82	14.69	14.68	14.70	17.31	12.92	18.91	17.54	15.95	11.76	–	17.69	22.25	–	18.00
1985 - Jan.	13.93	13.75	13.77	13.77	16.36	–	–	–	15.45	11.17	–	17.19	21.82	–	17.00
Feb.	13.62	13.46	13.36	13.42	16.09	–	–	–	15.15	10.87	–	16.89	21.49	–	17.00
Mar.	13.54	13.38	13.38	13.40	16.04	12.47	18.26	16.84	15.14	11.02	11.61	16.82	21.43	18.59	17.00
Apr.	14.41	14.31	14.00	14.24	15.67	–	–	–	15.05	11.14	11.58	16.78	21.35	18.44	17.00
May	14.47	14.22	13.90	14.15	15.46	–	–	–	14.86	11.04	11.41	16.69	21.32	18.36	17.00
June	14.41	14.18	13.95	14.12	15.28	11.87	17.79	16.44	14.73	10.74	11.27	16.58	21.24	18.27	17.00
July	14.22	14.08	13.99	14.07	14.96	–	–	–	14.52	10.27	11.00	16.53	21.10	18.15	17.00
Aug.	13.95	13.99	14.05	14.00	14.73	–	–	–	14.42	10.20	10.90	16.50	21.04	18.02	17.00
Sept.	13.93	13.82	13.68	13.79	14.41	10.99	17.43	16.10	13.82	9.69	10.44	15.96	20.61	17.72	16.00
Oct.	13.28	13.33	13.20	13.27	14.39	–	–	–	13.63	9.49	10.20	15.63	20.34	17.33	16.00
Nov.	13.31	13.16	13.16	13.18	14.64	–	–	–	13.55	9.48	10.19	15.45	20.26	17.14	15.88
Dec.	13.23	13.10	13.14	13.14	14.93	11.29	16.62	15.52	13.43	9.56	10.11	15.29	20.16	16.86	15.88
1986 - Jan.	14.34	13.73	13.19	13.58	15.25	–	–	–	13.37	9.67	10.17	15.29	20.23	16.85	15.88
Feb.	14.17	13.59	13.08	13.40	16.71	–	–	–	13.36	9.73	10.22	15.65	20.54	17.45	16.00
Mar.	13.46	13.19	12.88	13.07	17.39	....	....	....	13.41	9.82	10.28	15.76	20.62	17.75	16.00
Apr.	12.99	12.39	11.84	12.28	15.50	–	–	–	12.95	9.43	9.99	15.43	20.21	17.53	15.25

(1) Annual figures are the average of monthly values. – (2) Annual compound rates; the calculation is based on the financial year until 1976 and on the calendar year from 1977 onwards. The annual rates are averages of the monthly rates. – (3) Weighted average of allotment rates in the public auctions. – (4) Monthly average of rates reported at 10-day intervals. Normal rates are those applied most frequently; average rates are the weighted average of rates on individual positions weighted with the relevant balances. – (5) Maximum rate applied to the lira sight deposits of resident credit institutions with a debit balance of more than 1 billion lire. – (6) Average end-quarter rates on sight and time deposits and current accounts of 20 million lire or more recorded by the Central Risks Office. – (7) Quarterly average of lending rates recorded by the Central Risks Office. – (8) The monthly data refer to the end of the month in question.

Table a 22

INTEREST RATES: SECURITIES

(averages)

	Variable rate Treasury credit certificates	Treasury certificates in ECUs	Index-linked Treasury certificates	Other government securities		Bonds						Shares
				Treasury bonds	Total	Credit institutions		ENEL ENI IRI	Firms	Total		
						industrial	real estate					
1976	....	....	....	12.66	12.62	13.39	12.15	13.43	14.35	13.13		4.15
1977	....	....	....	14.71	14.71	14.56	14.48	14.53	15.40	14.60		4.58
1978	....	....	....	13.05	13.18	13.34	13.61	13.36	14.02	13.52		4.92
1979	....	....	....	13.02	13.12	13.58	13.69	13.68	14.48	13.78		3.18
1980	....	....	....	15.25	15.30	15.39	15.16	15.71	16.56	15.65		2.43
1981	20.25	....	....	19.36	19.35	19.68	19.54	19.44	21.52	19.78		1.89
1982	20.78	....	....	20.22	20.21	20.28	21.58	20.19	21.39	20.62		2.24
1983	19.82	13.11	....	18.30	18.25	17.93	18.72	17.68	18.52	17.99		2.45
1984	16.98	11.51	3.40	15.60	15.57	14.82	15.86	14.55	15.09	14.93		3.09
1985	14.68	9.88	4.61	13.71	13.68	13.08	13.19	12.62	13.12	12.96		2.69
1984 - Jan. ...	18.48	11.75	....	16.92	16.91	16.59	17.56	16.01	16.79	16.59		2.62
Feb. ...	18.03	11.39	....	16.33	16.34	15.80	17.16	15.36	15.89	15.89		2.49
Mar. ...	17.48	11.31	....	15.68	15.69	15.25	16.33	15.04	15.04	15.35		2.39
Apr. ...	17.37	11.70	....	15.74	15.74	15.08	15.96	14.72	15.27	15.16		2.43
May ...	17.05	11.49	2.51	15.75	15.71	14.95	15.89	14.67	15.25	15.03		2.54
June ...	16.73	11.52	2.75	15.54	15.47	14.73	15.96	14.63	14.78	14.87		2.62
July	16.45	11.59	2.88	15.18	15.12	14.28	15.69	13.99	14.89	14.43		3.32
Aug. ...	16.48	11.44	3.31	15.28	15.22	14.32	15.55	13.96	15.08	14.45		3.15
Sept. ...	16.63	11.51	3.52	15.64	15.58	14.45	15.35	14.24	15.15	14.58		3.57
Oct. ...	16.69	11.59	3.73	15.35	15.32	14.31	15.22	14.13	14.50	14.49		4.01
Nov. ...	16.36	11.60	4.02	15.25	15.23	14.29	14.94	14.33	14.36	14.44		4.05
Dec. ...	16.01	11.18	4.46	14.53	14.52	13.84	14.74	13.54	14.03	13.93		3.94
1985 - Jan. ...	15.15	10.32	4.49	13.27	13.22	12.85	13.52	12.44	12.75	12.71		3.50
Feb. ...	14.50	10.17	4.27	13.29	13.25	12.49	13.21	12.38	12.34	12.52		3.14
Mar. ...	14.23	9.99	4.40	13.51	13.48	12.78	13.11	12.45	12.71	12.73		3.13
Apr. ...	14.44	9.96	4.53	13.57	13.53	13.22	13.03	12.86	13.39	13.12		3.19
May ...	15.02	10.38	4.67	13.89	13.85	13.42	13.04	12.81	13.45	13.18		2.73
June ...	15.06	10.90	4.80	13.91	13.87	13.42	13.27	12.67	13.33	13.18		2.70
July	14.99	10.05	4.87	14.12	14.08	13.23	13.26	12.55	12.32	13.06		2.58
Aug. ...	14.89	9.63	4.35	14.09	14.04	13.38	13.21	12.75	13.61	13.21		2.50
Sept. ...	14.70	9.54	4.46	13.76	13.74	13.08	13.13	12.58	14.10	12.97		2.34
Oct. ...	14.59	9.21	4.54	13.75	13.73	12.80	13.08	12.43	13.04	12.77		2.31
Nov. ...	14.29	9.41	4.95	13.72	13.70	13.04	13.16	12.76	12.95	12.91		2.18
Dec. ...	14.28	9.00	4.95	13.67	13.66	13.27	13.27	12.81	13.41	13.10		2.02
1986 - Jan. ...	14.14	8.21	4.89	13.46	13.43	12.97	13.28	12.05	13.24	12.84		1.90
Feb. ...	14.65	8.62	4.91	13.83	13.80	13.07	13.20	11.89	12.93	12.79		1.68
Mar. ...	14.53	8.86	5.25	13.37	13.35	12.55	12.97	11.07	11.98	12.36		1.41
Apr. ...	14.01	8.45	5.28	12.28	12.27	11.69	12.52	10.45	12.45	11.76		1.28

FINANCIAL ASSETS OF THE PRIVATE

(changes in

	1976	1977	1978	1979	1980	1981	1982
FINANCIAL ASSETS:							
Domestic	**34,090**	**39,688**	**52,221**	**62,090**	**60,338**	**81,113**	**94,107**
M 1	11,987	15,212	19,156	25,366	19,264	22,339	30,148
M 2	25,374	31,363	36,461	43,540	34,284	36,306	60,476
M 3	27,726	34,879	40,174	51,762	51,145	61,266	72,141
Special credit institution deposits and savings certificates	–58	236	1,033	423	414	1,356	6,858
Medium and long-term securities	209	51	5,707	3,221	–1,394	5,558	8,031
Investment fund units	–	–	–	–	–	–	–
TOTAL . . .	*27,877*	*35,166*	*46,914*	*55,406*	*50,165*	*68,180*	*87,030*
Shares and participations (2)	1,230	116	529	675	2,143	1,204	1,260
Other financial assets (3)	4,983	4,406	4,778	6,009	8,030	11,729	5,817
Foreign	**-2,276**	**1,050**	**501**	**3,610**	**745**	**511**	**2,885**
Short-term credit (net)	–1,189	949	–409	2,138	305	–1,734	2,065
Loans	–722	–274	832	1,052	50	640	–219
Medium and long-term securities	–351	–201	–67	–177	–179	–287	77
Shares and participations	–14	576	145	597	569	1,892	962
TOTAL . . .	**31,814**	**40,738**	**52,722**	**65,700**	**61,083**	**81,624**	**96,992**
AGAINST FINANCING OF:							
Private sector	**22,113**	**20,494**	**25,233**	**32,822**	**43,550**	**48,962**	**45,031**
Short-term borrowing	10,611	9,264	9,046	16,983	18,718	12,022	14,448
banking system (4)(5)	*10,362*	*8,958*	*8,191*	*16,009*	*17,112*	*9,841*	*12,780*
special credit institutions (5)	*249*	*306*	*855*	*974*	*1,606*	*2,181*	*1,668*
Medium and long-term borrowing	6,602	6,764	9,975	10,805	15,532	24,940	19,323
loans: banks	*1,261*	*1,413*	*2,329*	*3,591*	*4,062*	*3,166*	*1,231*
special credit institutions (4)	*4,392*	*4,430*	*5,243*	*4,801*	*6,866*	*11,914*	*10,512*
public sector	*16*	*80*	*–58*	*–296*	*–86*	*399*	*–83*
foreign	*–22*	*–395*	*1,487*	*2,227*	*4,497*	*8,641*	*3,074*
bonds	*955*	*1,236*	*974*	*482*	*193*	*820*	*4,589*
Shares and participations	2,412	2,719	4,392	2,531	5,201	6,008	10,488
shares (6)	*1,194*	*997*	*892*	*865*	*1,923*	*2,001*	*2,038*
endowment funds (7)	*765*	*1,177*	*2,494*	*836*	*2,952*	*3,154*	*7,384*
other participations	*453*	*545*	*1,006*	*830*	*326*	*853*	*1,066*
Other financial liabilities (8)	2,488	1,747	1,820	2,503	4,099	5,992	772
Foreign sector (9)	**-2,343**	**2,175**	**5,261**	**4,553**	**-8,291**	**-9,225**	**-7,412**
Public sector (consolidated) (10)	**15,524**	**16,553**	**22,637**	**27,014**	**33,328**	**51,415**	**65,942**
Unclassified (11)	**-3,480**	**1,516**	**-409**	**1,311**	**-7,504**	**-9,528**	**-6,569**

(1) Rounding may cause discrepancies in the totals. – (2) Excludes shares issud by state-controlled companies and taken up by their parent companies. – (3) Includes actuarial foreign currency loans; also includes securities issued to fund debts and credit institutions' bad debts. The lending of the banking system excludes loans to pay the non-interest-bearing state-controlled companies. – (7) Net of the funding of state-controlled companies' debts with banks. – (8) Retirement funds, credit institutions' bad debts, an estimate of atypical basis. – (10) Includes the actuarial reserves of social security institutions. – (11) Includes the balances of financial intermediaries.

SECTOR AND THEIR COUNTERPARTS: FLOWS (1)

billions of lire)

1983	1984	1985	1984 I	1984 II	1984 III	1984 IV	1985 I	1985 II	1985 III	1985 IV
115,324	**138,714**	**141,941**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
23,491	30,792	25,695	–14,357	4,263	5,404	35,483	–12,984	3,134	5,160	30,385
45,104	54,889	53,448	–15,500	4,821	11,591	53,977	–7,929	5,378	9,012	46,987
60,272	75,913	68,665	984	7,863	14,630	52,436	886	14,736	14,240	38,803
1,364	4,272	1,543	1,348	1,343	65	1,516	1,853	588	–1,638	740
41,870	43,140	43,267	20,030	13,302	6,581	3,227	14,721	8,792	10,351	9,404
–	1,163	15,975	–	–	310	854	3,789	3,488	3,547	5,150
103,506	*124,488*	*129,450*	*22,362*	*22,508*	*21,586*	*58,033*	*21,249*	*27,604*	*26,500*	*54,097*
1,096	1,850	–1,520	....	....	....	....	....	....	....	....
10,722	12,376	14,011	2,896	3,087	3,084	3,310	3,250	3,560	3,417	3,784
3,656	**6,355**	**3,509**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
–616	2,547	–1,387	–262	1,492	978	339	–94	–986	–706	399
1,630	386	1,357	351	182	–253	106	34	–256	542	1,037
–545	–79	39	–68	–80	99	–30	116	61	4	–142
3,187	3,501	3,500	....	....	....	....	....	....	....	....
118,980	**145,069**	**145,450**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
52,380	**65,444**	**67,053**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
20,091	34,311	33,249	8,484	6,797	9,090	9,940	3,116	3,545	3,190	23,399
19,784	*31,438*	*30,511*	*8,618*	*5,823*	*9,044*	*7,953*	*2,647*	*3,501*	*2,938*	*21,425*
307	*2,873*	*2,738*	*–134*	*974*	*46*	*1,987*	*469*	*44*	*252*	*1,974*
15,490	14,784	18,119	2,696	2,154	5,108	4,827	7,094	1,832	4,051	5,142
3,030	*3,882*	*5,018*	*756*	*1,255*	*799*	*1,071*	*1,029*	*1,212*	*1,064*	*1,713*
8,624	*9,026*	*8,351*	*1,533*	*781*	*3,517*	*3,196*	*2,397*	*394*	*2,889*	*2,671*
689	*809*	*842*	*270*	*143*	*738*	*–342*	*918*	*–37*	*–88*	*49*
755	*–839*	*2,064*	*–51*	*–527*	*–938*	*678*	*2,418*	*–547*	*113*	*80*
2,392	*1,906*	*1,844*	*188*	*502*	*992*	*224*	*332*	*810*	*73*	*629*
13,299	12,617	11,123	....	....	....	....	....	....	....	....
2,967	*4,948*	*4,361*	....	....	....	....	....	....	....	....
9,431	*6,548*	*5,130*	*2,600*	*3,708*	*5*	*235*	*2,456*	*1,544*	*602*	*528*
901	*1,121*	*1,632*	*280*	*280*	*281*	*281*	*408*	*408*	*408*	*408*
3,500	3,732	4,562	848	930	1,009	945	1,183	1,108	1,137	1,133
1,183	**-5,084**	**-8,032**	**-1,988**	**-324**	**1,217**	**-3,989**	**....**	**....**	**....**	**....**
75,812	**94,378**	**109,839**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
-10,395	**-9,669**	**-23,410**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**

reserves, an estimate of atypical securities, the non-interest bearing deposit on payments abroad and other minor items. – (4) Flows are adjusted for changes in exchange rates on deposit on payments abroad. – (5) Includes acceptances acquired. – (6) Net share issues by private sector companies and the contribution of third parties to the financing of securities, loans granted by insurance companies and bank loans used to pay the non-interest-bearing deposit on payments abroad. – (9) Balance of payments on a transactions

FINANCIAL ASSETS OF THE PRIVATE

(in billions

	1975	1976	1977	1978	1979	1980	1981
FINANCIAL ASSETS							
Domestic	**194,237**	**228,674**	**267,913**	**325,026**	**402,068**	**545,201**	**664,783**
notes and coin	12,304	13,953	15,781	18,534	21,001	24,544	28,839
demand deposits: with banks	45,568	55,536	68,224	83,567	104,145	121,452	138,739
with the Post Office	1,465	1,835	2,532	3,592	5,912	4,325	5,083
M1	*59,337*	*71,324*	*86,537*	*105,692*	*131,058*	*150,321*	*172,661*
saving deposits: banks (2)	48,731	59,879	73,578	87,112	100,838	112,163	124,215
P.O.	11,846	14,085	16,537	20,308	24,756	28,451	30,366
M2	*119,914*	*145,288*	*176,651*	*213,112*	*256,652*	*290,935*	*327,242*
Treasury bills	207	2,559	6,074	9,787	18,007	33,737	57,983
Bankers' acceptances	–	–	–	–	2	1,133	1,847
M3	*120,122*	*147,846*	*182,725*	*222,899*	*274,661*	*325,805*	*387,072*
Deposits and savings certificates with special credit institutions	3,727	3,669	3,905	4,939	5,362	5,776	7,132
Medium and long-term securities	17,253	17,376	17,288	22,005	27,723	27,023	33,172
of which: Treasury credit certificates	*11*	*44*	*912*	*2,102*	*6,826*	*8,380*	*11,830*
Investment fund unit (3)	–	–	–	–	–	–	–
Shares and participations (4)	23,737	25,402	25,208	31,618	44,748	128,994	168,125
Other financial assets	29,398	34,381	38,787	43,565	49,574	57,603	69,282
Actuarial reserves + retirement funds	*29,156*	*34,111*	*38,486*	*43,174*	*48,889*	*56,592*	*63,964*
Deposits on payments abroad + other (5)	*243*	*270*	*301*	*391*	*684*	*1,012*	*5,318*
Foreign (4)	....	**13,056**	**14,215**	**16,281**	**20,027**	**22,941**	**23,384**
Short- term credit (net)	....	175	1,395	2,240	4,342	4,653	2,280
Loans	....	8,428	7,886	8,668	9,555	10,008	11,105
Medium and long-term securities	580	974	941	1,094	1,480	2,148	1,360
Shares and participations	2,987	3,479	3,993	4,279	4,650	6,132	8,639
TOTAL . . .	....	**241,730**	**282,128**	**341,307**	**422,095**	**568,142**	**688,167**
AGAINST FINANCING OF							
Private sector	**149,315**	**171,581**	**192,004**	**222,460**	**267,810**	**390,029**	**476,028**
Short-term borrowing	46,091	56,433	65,142	73,296	88,843	106,333	119,255
banking system (6)	*44,962*	*55,054*	*63,457*	*70,756*	*85,329*	*101,212*	*111,953*
special credit institutions (6)	*1,129*	*1,379*	*1,685*	*2,540*	*3,514*	*5,121*	*7,302*
Medium and long-term borrowing	53,092	60,647	67,282	76,778	86,052	102,332	129,855
loans: banks	*5,404*	*6,665*	*8,078*	*10,408*	*13,998*	*18,060*	*21,226*
special credit institutions	*31,013*	*35,134*	*39,130*	*43,610*	*47,209*	*53,464*	*63,688*
public sector	*2,856*	*2,872*	*2,953*	*2,895*	*2,599*	*2,513*	*2,912*
foreign	*4,655*	*5,775*	*5,572*	*7,285*	*9,150*	*15,006*	*27,891*
bonds	*9,164*	*10,201*	*11,549*	*12,580*	*13,096*	*13,289*	*14,138*
Shares and participations	32,989	34,339	36,613	46,036	61,475	143,556	181,482
shares	*27,014*	*27,168*	*27,177*	*33,247*	*46,746*	*124,530*	*155,437*
endowment funds	*3,754*	*4,417*	*5,595*	*7,974*	*8,789*	*12,505*	*18,090*
other participations	*2,221*	*2,754*	*3,841*	*4,815*	*5,940*	*6,521*	*7,955*
Other financial liabilities (7)	17,143	20,162	22,967	26,350	31,440	37,808	45,436
Foreign sector	....	**-1,490**	**2,145**	**9,969**	**22,993**	**33,384**	**17,574**
Public sector (consolidated) (8)	**89,721**	**105,245**	**121,798**	**144,435**	**171,449**	**204,777**	**256,192**
Unclassified (9)	....	**-33,606**	**-33,819**	**-35,557**	**-40,157**	**-60,048**	**-61,627**

(1) Rounding may cause discrepancies in totals. – (2) Including banks' repurchase agreements with customers and certificates of deposit. – (3) Units of Italian investment funds. excludes loans used to pay the non-interest-bearing deposit on payments abroad. – (7) Retirement funds, credit institutions' bad debts, acceptances acquired by investors other than (8) Includes social security institutions' actuarial reserves. – (9) Includes the balances of credit institutions and discrepancies.

Table a 24

SECTOR AND THEIR COUNTERPARTS: STOCKS (1)

of lire)

1982	1983	1984				1985			
		I	II	III	IV	I	II	III	IV
738,767	**889,570**	**....**	**....**	**....**	**1,090,418**	**....**	**....**	**....**	**1,507,247**
32,308	36,256	33,945	35,263	35,706	39,922	38,228	39,633	39,490	43,607
164,648	182,934	170,134	173,519	178,444	209,733	197,846	199,689	205,725	230,434
5,852	7,110	7,863	7,424	7,459	7,437	8,034	7,920	7,187	8,745
202,809	*226,299*	*211,942*	*216,206*	*221,609*	*257,091*	*244,107*	*247,242*	*252,402*	*282,787*
151,743	169,670	167,757	167,859	173,590	188,103	192,172	194,064	197,218	207,866
33,166	36,853	37,624	38,080	38,535	42,517	43,503	43,855	44,553	50,507
387,718	*432,822*	*417,323*	*422,144*	*433,734*	*487,712*	*479,782*	*485,161*	*494,172*	*541,159*
70,024	85,562	102,388	105,703	108,904	107,552	116,467	125,954	131,304	123,307
1,471	1,101	864	697	628	544	520	437	406	354
459,213	*519,485*	*520,575*	*528,544*	*543,266*	*595,808*	*596,769*	*611,552*	*625,882*	*664,821*
13,990	15,354	16,702	18,045	18,110	19,625	21,478	22,067	20,429	21,168
42,209	84,997	107,108	118,205	125,866	128,308	146,002	153,707	164,889	173,360
18,256	*51,340*	*68,434*	*78,102*	*83,349*	*84,794*	*99,977*	*106,599*	*118,037*	*123,892*
–	–	–	–	310	1,163	5,037	9,073	13,413	19,784
148,448	184,143	....	....	....	247,547	....	....	....	516,137
74,907	85,591	88,487	91,573	94,657	97,967	101,217	104,778	108,194	111,978
73,227	*83,671*	*86,699*	*89,727*	*52,755*	*95,783*	*99,244*	*102,706*	*106,167*	*109,629*
1,680	*1,920*	*1,788*	*1,846*	*1,902*	*2,184*	*1,973*	*2,072*	*2,027*	*2,349*
28,531	**35,461**	**....**	**....**	**....**	**46,434**	**....**	**....**	**....**	**54,351**
3,562	2,987	....	....	....	2,517	....	....	....	4,363
12,536	16,364	....	....	....	19,344	....	....	....	19,739
1,735	1,278	....	....	....	1,320	....	....	....	1,249
10,698	14,832	....	....	....	23,253	....	....	....	29,000
767,298	**925,031**	**....**	**....**	**....**	**1,136,852**	**....**	**....**	**....**	**1,561,598**
508,293	**596,125**	**....**	**....**	**....**	**729,336**	**....**	**....**	**....**	**1,069,379**
133,039	152,629	160,009	166,309	175,948	185,452	188,722	191,423	193,974	215,591
124,069	*143,351*	*150,866*	*156,191*	*165,784*	*173,301*	*176,103*	*178,759*	*181,059*	*200,702*
8,970	*9,278*	*9,143*	*10,118*	*10,164*	*12,151*	*12,620*	*12,663*	*12,915*	*14,889*
152,253	173,906	....	....	....	193,211	....	....	....	206,691
22,457	*25,486*	*26,243*	*27,498*	*28,297*	*29,368*	*30,397*	*31,609*	*32,673*	*34,386*
73,707	*81,466*	*82,662*	*83,549*	*86,301*	*89,694*	*91,196*	*91,842*	*94,060*	*96,890*
2,829	*3,518*	*3,788*	*3,931*	*4,669*	*4,327*	*5,244*	*5,207*	*5,119*	*5,169*
34,515	*42,297*	....	....	....	*46,778*	....	....	....	*45,358*
18,745	*21,139*	*21,326*	*21,828*	*22,821*	*23,044*	*23,376*	*24,186*	*24,260*	*24,888*
174,636	214,640	233,610	253,620	270,815	288,189	....	....	....	575,680
140,373	*171,257*	*188,418*	*205,578*	*222,738*	*239,899*	....	....	....	*520,269*
25,617	*32,408*	*34,635*	*37,902*	*38,355*	*38,986*	*41,455*	*43,005*	*43,609*	*44,475*
8,646	*10,975*	*10,557*	*10,140*	*9,722*	*9,304*	....	....	....	*10,936*
48,365	54,950	57,278	58,839	61,227	62,484	65,518	67,051	69,618	71,417
4,167	**11,361**	**....**	**....**	**....**	**2,373**	**....**	**....**	**....**	**-13,124**
322,134	**397,946**	**....**	**....**	**....**	**492,324**	**....**	**....**	**....**	**602,163**
-67,296	**-80,401**	**....**	**....**	**....**	**-87,181**	**....**	**....**	**....**	**-96,820**

– (4) 1985 figures are estimates. – (5) Includes an estimate of atypical securities and other minor items. – (6) Includes acceptances acquired; the lending of the banking system credit institutions, an estimate of atypical securities, loans granted by insurance companies and bank loans used to pay the non-interest-bearing deposit on payments abroad. –

Table a 25

FINANCING OF INVESTMENT

(billions of lire)

	Households	Firms and dwellings	Public sector (consolidated) (1)	Financial intermediaries (consolidated) (2)	TOTAL	Foreign sector
			1984			
Gross fixed investment	–	79,037	30,116	2,902	112,055	–
Changes in stocks	–	4,963	–	–	4,963	–
Capital transfers	–	–8,361	8,071	–	–290	290
Financial assets	113,232	31,837	11,109	101,187	257,365	27,732
liquid assets	58,465	17,448	37	–5,242	70,708	–56
medium and long-term securities	36,960	6,102	1,004	22,777	66,843	389
shares and participations (3)	691	4,660	8,244	1,315	14,910	2,546
other loans (net) (4)	17,116	3,627	1,824	82,337	104,904	24,853
FINANCIAL REQUIREMENT	**113,232**	**107,476**	**49,296**	**104,089**	**374,093**	**28,022**
Gross saving (5)	110,709	38,229	–49,289	11,995	111,644	5,084
Financial liabilities (6)	2,523	62,921	105,487	92,094	263,025	22,648
short-term borrowing (7)	2,188	32,123	30,740	72,193	137,244	22,385
loans and other borrowings: domestic	335	13,041	9,063	11,444	33,883	–3,728
foreign	–	–839	2,271	3,926	5,358	–
medium and long-term securities	–	1,906	63,413	2,007	67,326	–93
shares and participations (8)	–	12,617	–	755	13,372	4,084
provisions for severance pay and pensions	–	4,073	–	1,769	5,842	–
Adjustments	–	6,326	–6,902	–	–576	290
SOURCES OF FINANCE	**113,232**	**107,476**	**49,296**	**104,089**	**374,093**	**28,022**
NET FINANCIAL INVESTMENT	**110,709**	**–31,084**	**–94,378**	**9,093**	**–5,660**	**5,084**
			1985			
Gross fixed investment	–	90,527	31,312	3,011	124,850	–
Changes in stocks	–	4,897	–	–	4,897	–
Capital transfers	–	–15,756	15,368	–	–388	388
Financial assets	124,602	20,848	13,171	90,136	248,757	14,493
liquid assets	56,051	12,615	2,019	–17,699	52,986	236
medium and long-term securities	35,990	7,320	934	53,358	97,602	1,530
shares and participations (3)	1,881	99	7,951	3,962	13,893	2,238
other loans (net) (4)	30,680	814	2,267	50,515	84,276	10,489
FINANCIAL REQUIREMENT	**124,602**	**100,516**	**59,851**	**93,147**	**378,116**	**14,881**
Gross saving (5)	120,736	45,929	–56,088	10,750	121,327	8,032
Financial liabilities (6)	3,866	63,187	123,010	82,397	272,460	6,461
short-term borrowing (7)	3,301	29,948	23,075	59,123	115,447	–5,925
loans and other borrowings: domestic	565	13,590	3,129	17,598	34,882	6,999
foreign	–	2,064	2,937	1,591	6,592	–
medium and long-term securities	–	1,844	93,869	2,751	98,464	668
shares and participations (8)	–	11,123	–	–48	11,075	4,719
provisions for severance pay and pensions	–	4,618	–	1,382	6,000	–
Adjustments	–	–8,600	–7,071	–	–15,671	388
SOURCES OF FINANCE	**124,602**	**100,516**	**59,851**	**93,147**	**378,116**	**14,881**
NET FINANCIAL INVESTMENT	**120,736**	**–42,339**	**–109,839**	**7,739**	**–23,703**	**8,032**

(1) The sector's financial liabilities include the actuarial reserves of the social security institutions. – (2) Credit institutions and other financial intermediaries. – (3) Excluding the shares issued by state-controlled companies and taken up by their parent companies. – (4) The figures for financial intermediaries include bad debts and overdue instalments. – (5) Households' gross saving has been put equal to their net financial investment. – (6) Financial liabilities have been adjusted for exchange rate changes affecting foreign currency loans, include credit institutions' bad debts and have been adjusted for securities issued to fund debts. The figures for the external financing of the sector "Firms and dwellings" were obtained by adding to firms' liabilities an estimate of mortgages received by households for investment in dwellings. – (7) Includes BI-UIC financing of the Treasury. – (8) Net issues by private sector companies and the contribution of third parties to the financing of state-controlled companies.

THE BANK'S CAPITAL AND RESERVES

Capital. — Having remained unchanged during 1985, the distribution of the 300,000 shares of the Bank's capital was as follows at 31 December:

Shareholders with voting rights:

Savings banks and pledge banks	76	with	177,898	shares	and	471	votes
Public-law credit institutions	7	"	54,500	"	"	137	"
Banks of national interest	3	"	21,000	"	"	54	"
Social security institutions	1	"	15,000	"	"	34	"
Insurance companies	7	"	31,500	"	"	91	"
	94	with	299,898	shares	and	787	votes

Shareholders without voting rights:

Savings banks and pledge banks	12	with	102	shares
Total ...	106	with	300,000	shares

Reserves. — The changes in the ordinary and extraordinary reserve funds during 1985 are given below; the composition is also indicated in accordance with Article 2 (6) of Law no. 649 of 25 November 1983.

		Ordinary reserve fund		Extraordinary reserve fund
Amount at 31 December 1984	Lit.	375,554,592,932	Lit.	403,670,860,915
increase: due to appropriation of 20 per cent of profits for the year 1984	"	79,055,926,755	"	79,055,926,755
due to income received in 1985 from investment of reserves ...	"	51,439,362,068	"	62,169,537,553
decrease: due to distribution to shareholders of a part of the income accruing in the course of 1984 (Article 56 of the Statutes)	"	295,894,775		316,105,225
Amount at 31 December 1985	Lit.	505,753,986,980	Lit.	544,580,219,998

BALANCE SHEET

AND PROFIT AND LOSS ACCOUNT

BALANCE SHEET

ASSETS

GOLD				
I on hand . . . Lit.			2,633,369,526,940	
II on deposit abroad . . . "			26,039,478,550,729	28,672,848,077,669
GOLD CREDITS (EMCF) . . . Lit.				9,882,452,283,103
CASH ON HAND . . . "				732,375,213,421
DISCOUNTS AND ADVANCES				
I portfolio discounts:				
— ordinary bills . . . Lit.		180,341,070,939		
— stockpiling bills . . . "		1,926,910,513,253	2,107,251,584,192	
II advances:				
— current account . . . Lit.		563,542,126,872		
— fixed term . . . "		6,209,379,242,500		
— under Treasury Decree of 27.9.1974 . . . "		—	6,772,921,369,372	
III deferred payments in the clearing system . . . Lit.			—	8,880,172,953,564
BILLS FOR COLLECTION WITH CORRESPONDENTS . . . Lit.				—
EXTERNAL ASSETS IN FOREIGN CURRENCIES				
I ECUs . . . Lit.			7,170,599,845,150	
II other assets:				
— banknotes and foreign currency bills . . . Lit.		547,995,621		
— current accounts with correspondents . . . "		4,804,846,132,637		
— time deposits . . . "		1,077,473,329,741		
— other . . . "		110,482,462,490	5,993,349,920,489	13,163,949,765,639
DOLLAR CREDITS (EMCF) . . . Lit.				2,164,926,596,472
ITALIAN FOREIGN EXCHANGE OFFICE (UIC)				
I current account . . . Lit.			10,986,177,824,596	
II special accounts . . . "			3,492,899,070,350	14,479,076,894,946
EXTRAORDINARY ADVANCE TO THE TREASURY . . . Lit.				—
TREASURY CURRENT ACCOUNT . . . "				48,182,131,481,222
SUNDRY CLAIMS ON THE GOVERNMENT . . . "				849,227,162,879
SECURITIES				
I government and government-guaranteed securities:				
— freely available . . . Lit.		60,816,744,960,058		
— investment of statutory reserves . . . "		774,322,069,314		
— investment of staff severance pay and pension funds . . . "		1,292,519,096,016	62,883,586,125,388	
II securities of companies and agencies:				
— investment of statutory reserves . . . Lit.		60,209,091,911		
— investment of staff severance pay and pension funds . . . "		712,982,734,399	773,191,826,310	
III shareholdings and participations:				
— in subsidiary companies and agencies				
investment of statutory reserves . . . Lit.	1,789,217,433			
investment of staff severance pay and pension funds . . . "	97,867,093,239	99,656,310,672		
— in associated companies and agencies				
investment of statutory reserves . . . Lit.	5,184,387,166			
investment of staff severance pay and pension funds . . . "	12,898,686,197	18,083,073,363		
— in other companies and agencies				
investment of statutory reserves . . . Lit.	115,264,141,823			
investment of staff severance pay and pension funds . . . "	147,707,953,830	262,972,095,653	380,711,479,688	64,037,489,431,386
carried forward Lit.				191,044,649,860,301

LIABILITIES

NOTES IN CIRCULATION	Lit.		46,994,411,869,000
BANCA D'ITALIA DRAFTS	"		670,962,291,812
OTHER SIGHT LIABILITIES			
I transfer orders	Lit.	97,495,000,000	
II other	"	4,889,800,639	102,384,800,639
FREE DEPOSITS ON CURRENT ACCOUNT	Lit.		3,379,930,894,224
TIED DEPOSITS ON CURRENT ACCOUNT	"		—
DEPOSITS FOR CASH DEPARTMENT SERVICES	"		194,976,872,210
COMPULSORY DEPOSITS			
I compulsory bank reserves	Lit.	75,692,677,157,152	
II collateral for the issue of bankers' drafts and guaranteed personal cheques	"	12,311,757	
III tied deposits in relation to investment abroad	"	31,211,454,031	
IV in respect of companies in the process of incorporation	"	81,701,887,609	
V in respect of bank lending in excess of the ceiling	"	—	
VI other	"	36,295,147,389	75,841,897,957,938
DEPOSITS IN FOREIGN CURRENCY ON BEHALF OF THE UIC	Lit.		—
EXTERNAL ACCOUNTS IN LIRE ON BEHALF OF THE UIC	"		3,492,899,070,350
EXTERNAL LIABILITIES			
I deposits in foreign currencies	Lit.	1,619,342,974	
II external accounts in lire	"	165,521,452,978	167,140,795,952
ECU LIABILITIES (EMCF)	Lit.		12,047,378,879,575
SUNDRY LIABILITIES TOWARDS THE GOVERNMENT	"		491,796,308,595
SUNDRY PROVISIONS			
I for gold price fluctuations (under Decree Law no. 867 of 30.12.1976)	Lit.	34,793,307,248,104	
II for losses ensuing from exchange rate management (under Decree Law no. 867 of 30.12.1976)	"	1,200,795,276,401	
III for losses on bill portfolio	"	234,919,178,078	
IV for losses on foreign exchange	"	1,599,969,976,261	
V for losses on securities	"	3,245,059,095,132	
VI for contingent losses	"	2,403,006,748,480	
VII for insurance cover	"	642,691,685,925	
VIII for building works	"	1,352,335,650,099	
IX for renewal of equipment	"	326,250,000,000	
X for taxation	"	1,468,835,226,241	
XI for staff severance pay and pensions	"	2,515,333,000,000	
XII for grants to BI pensioners and their surviving dependants	"	600,811,537	
XIII for severance pay to contract staff under Law no. 297 of 29.5.82	"	105,602,273	49,783,209,498,531
	carried forward Lit.		193,166,989,238,826

BALANCE SHEET

ASSETS

		brought forward Lit.		191,044,649,860,301
UIC ENDOWMENT FUND		Lit.		500,000,000,000
REAL PROPERTY				
I Bank premises		Lit.	1,513,472,307,944	
II investment of staff severance pay and pension funds		"	185,254,617,729	1,698,726,925,673
OTHER INVESTMENTS OF STAFF SEVERANCE PAY AND PENSION FUNDS		Lit.		22,969,888,890
FURNITURE AND EQUIPMENT				
I furniture and fittings		Lit.	62,986,962,262	
II equipment		"	126,485,057,299	
III coins and collections		"	307,195,088	189,779,214,649
SUNDRY ITEMS				
I banknotes in production		Lit.	10,676,395,716	
II procedures, studies and designs of the technical departments:				
I completed	Lit. 43,241,026,355			
I in preparation	" 8,190,009,238		51,431,035,593	
III sundry debtors		Lit.	117,214,298,125	
IV other		"	2,162,411,931,955	2,341,733,661,429
ACCRUED INCOME		Lit.		2,454,060,160,704
PREPAID EXPENSES		"		—
		Lit.		198,251,919,711,646
MEMORANDUM ACCOUNTS				
I Securities and other valuables:				
— held as collateral	Lit. 10,909,402,566,389			
— other	" 538,240,579,041,830		549,149,981,608,219	
II Depositaries of securities and valuables:				
— domestic	Lit. —			
— foreign	" 829,739,376,551		829,739,376,551	
III Unused overdraft facilities		Lit.	1,875,341,643,699	
IV Debtors for securities receivable (BI forward sales)		"	3,664,000,000,000	
V Securities receivable (BI forward purchases)		"	—	
VI Debtors for foreign currencies and lire receivable (BI forward sales)				
— domestic	Lit. —			
— foreign	" 6,621,278,926,949		6,621,278,926,949	
VII Foreign currencies and lire receivable (BI forward purchases)		Lit.	6,621,278,926,949	
VIII Exchequer for depreciation allowances		"	469,319,054,705	569,230,939,537,072
		TOTAL . . . Lit.		**767,482,859,248,718**

Audited and found correct. — Rome, 24 April 1986

THE AUDITORS

DOMENICO AMODEO
ALBERTO CAMPOLONGO
VITTORIO CODA
GIUSEPPE GUARINO
LUIGI GUATRI

LIABILITIES

			brought forward Lit.	193,166,989,238,826
ACCUMULATED PROPERTY DEPRECIATION			Lit.	354,313,430,288
ACCUMULATED DEPRECIATION OF FURNITURE AND FITTINGS			"	62,819,409,324
ACCUMULATED DEPRECIATION OF EQUIPMENT			"	117,410,172,337
ACCUMULATED DEPRECIATION OF THE PROCEDURES, STUDIES AND DESIGNS OF THE TECHNICAL DEPARTMENTS			"	23,382,366,736
SUNDRY ITEMS				
I sundry creditors	Lit.		29,190,146,645	
II other	"		512,327,621,854	541,517,768,499
ACCRUED EXPENSES			Lit.	130,666,388,440
DEFERRED INCOME			"	1,150,029,097,682
CAPITAL	Lit.		300,000,000	
ORDINARY RESERVE FUND	"		505,753,986,980	
EXTRAORDINARY RESERVE FUND	"		544,580,219,998	1,050,634,206,978
REVALUATION SURPLUS RESERVE UNDER LAW No. 72 OF 19.3.1983			Lit.	1,304,000,000,000
NET PROFIT FOR DISTRIBUTION			"	350,157,632,536
			Lit.	198,251,919,711,646
MEMORANDUM ACCOUNTS				
I Depositors of securities and other valuables	Lit.		549,149,981,608,219	
II Securities and valuables on deposit	"		829,739,376,551	
III Holders of unused overdraft facilities	"		1,875,341,643,699	
IV Securities for delivery (BI forward sales)	"		3,664,000,000,000	
V Creditors for securities for delivery (BI forward purchases)	"		—	
VI Foreign currencies and lire for delivery (BI forward sales)	"		6,621,278,926,949	
VII Creditors for foreign currencies and lire for delivery (BI forward purchases)				
— domestic	Lit.	—		
— foreign	"	6,621,278,926,949	6,621,278,926,949	
VIII Depreciation allowances	Lit.		469,319,054,705	569,230,939,537,072
			TOTAL . . . Lit.	**767,482,859,248,718**

THE ACCOUNTANT GENERAL
LUIGI GIANNOCCOLI

THE GOVERNOR
CARLO AZEGLIO CIAMPI

PROFIT AND LOSS ACCO

EXPENDITURE AND LOSSES

COSTS OF ADMINISTRATION						
central and local boards			Lit.	1,361,992,641		
staff:						
wages and salaries and related costs	Lit.	529,420,686,779				
pensions and severance payments	"	217,636,147,454		747,056,834,233		
provision of services			Lit.	79,527,149,787		
other			"	134,459,457,709		962,405,434,370
TAXES AND DUTIES						
stamp duty on the circulation of banknotes and demand drafts			Lit.	—		
other taxes and duties:						
current year	Lit.	17,813,844,703				
previous years	"	812,159,268,000		829,973,112,703		829,973,112,703
INTEREST PAID						
on compulsory bank reserves			Lit.	4,166,723,075,408		
other			"	6,634,936,921		4,173,358,012,329
EXPENDITURE ON SECURITIES TRANSACTIONS					Lit.	8,241,183,076
EXPENDITURE ON FOREIGN TRANSACTIONS					"	10,280,073
LOSSES ON SECURITIES DEALINGS					"	—
EXCHANGE RATE LOSSES					"	—
LOSSES ON REALIZATION OF ASSETS					"	—
CONTRIBUTIONS TO CHARITIES AND SOCIAL AND CULTURAL ACTIVITIES					"	1,186,163,062
TECHNICAL DEPARTMENTS — INITIAL STOCKS					"	16,603,240,336
EXPENDITURE ON TRANSACTIONS WITH THE TREASURY					"	2,544,713,078,000
VALUATION LOSSES						
on securities			Lit.	16,518,065,782		
on foreign exchange			"	298,830,023,739		
on other assets			"	—		315,348,089,521
DEPRECIATION						
of Bank premises			Lit.	54,281,288,208		
of furniture and fittings			"	12,261,336,092		
of equipment			"	16,639,346,215		
of the procedures, studies and designs of the technical departments			"	10,640,352,090		
other			"	194,567,686		94,016,890,291
APPROPRIATION OF INVESTMENT INCOME TO RESERVES						
to ordinary reserve fund			Lit.	51,439,362,068		
to extraordinary reserve fund			"	62,169,537,553		113,608,899,621
				carried forward	Lit.	9,059,464,383,382

INCOME AND PROFITS

INTEREST RECEIVED					
on discounts and advances:					
ordinary portfolio discounts		Lit. 28,357,516,659			
stockpiling portfolio discounts		" 19,119,576,882			
advances		" 278,782,371,334		326,259,464,875	
on lending to the Treasury			Lit.	506,799,693,660	
on lending to the UIC			"	1,340,253,826,082	
on lending abroad			"	331,499,871,654	
other			"	10,913,812,147	2,515,726,668,418
INTEREST, PREMIUMS AND DIVIDENDS ON SECURITIES					
freely available					
fixed rate:					
Treasury bills		Lit. 1,356,392,807,733			
variable rate Treasury credit certificates		" 3,059,993,526,576			
other government securities		" 1,703,133,307,727		6,119,519,642,036	
government-guaranteed securities		" 235,607,715,059		6,355,127,357,095	
investment of reserves and staff severance pay and pension funds					
fixed rate:					
government and government-guaranteed securities	Lit. 203,910,053,220				
other securities	" 104,905,308,423	308,815,361,643			
from participations (not represented by securities) in:					
subsidiary companies and bodies	Lit. 4,978,864,464				
associated companies and bodies	" 1,146,947,200				
other companies and bodies	" 21,864,780,021	27,990,591,685		336,805,953,328	6,691,933,310,423
INCOME FROM PARTICIPATION IN THE UIC ENDOWMENT FUND				Lit.	78,408,853,350
PROFITS FROM DEALINGS IN AND REDEMPTION OF SECURITIES				"	390,689,375,952
EXCHANGE RATE GAINS				"	143,760,803,812
COMMISSIONS AND OTHER FINANCIAL REVENUE				"	231,529,197,017
INCOME FROM REAL PROPERTY				"	10,055,187,493
PROFITS FROM THE SALE OF:					
real property			Lit.	—	
other property			"	602,917,895	602,917,895
TECHNICAL DEPARTMENTS - FINAL STOCKS				Lit.	20,138,959,868
TECHNICAL DEPARTMENTS - PROCEDURES, STUDIES AND DESIGNS COMPLETED DURING THE YEAR				"	6,322,006,956
VALUATION GAINS					
on securities			Lit.	—	
on foreign exchange			"	—	
on other assets			"	—	—
				carried forward Lit.	10,089,167,281,184

PROFIT AND LOSS ACCO

EXPENDITURE AND LOSSES

	brought forward Lit.		9,059,464,383,382
ALLOCATIONS TO PROVISIONS			
for losses on bill portfolio	Lit.	—	
for losses on foreign exchange	"	398,800,000,000	
for losses on securities	"	535,000,000,000	
for contingent losses	"	—	
for insurance cover	"	50,000,000,000	
for building works	"	54,000,000,000	
for renewal of equipment	"	30,000,000,000	
for taxation	"	750,000,000,000	
for staff severance pay and pensions	"	43,713,000,000	
for grants to BI pensioners and their surviving dependants	"	243,831,856	
for severance pay of contract staff under Law no. 297 of 29.5.82	"	27,434,452	1,861,784,266,308
NON-OPERATING LOSSES AND EXTRAORDINARY CHARGES	Lit.		13,860,071
	Lit.		10,921,262,509,761
NET PROFITS	"		350,157,632,536
	TOTAL... Lit.		**11,271,420,142,297**

APPROPRIATION

TO ORDINARY RESERVE FUND ....

TO EXTRAORDINARY RESERVE FUND ....

TO SHAREHOLDERS ....

TO THE TREASURY ....

Audited and found correct. - Rome, 24 April 1986

THE AUDITORS

DOMENICO AMODEO
ALBERTO CAMPOLONGO
VITTORIO CODA
GIUSEPPE GUARINO
LUIGI GUATRI

INCOME AND PROFITS

	brought forward Lit.		10,089,167,281,184
WITHDRAWALS FROM PROVISIONS			
for losses on bill portfolio	Lit.	—	
for losses on foreign exchange	"	298,830,023,739	
for losses on securities	"	16,518,065,782	
for contingent losses	"	178,251,520	
for insurance cover	"	—	
for building works	"	54,281,288,208	
for renewal of equipment	"	—	
for taxation	"	812,159,268,000	
for staff severance pay and pensions	"	—	
for grants to BI pensioners and their surviving dependants	"	90,136,000	
for severance pay of contract staff under Law no. 297 of 29.5.82	"	16,170,026	1,182,073,203,275
NON-OPERATING PROFITS AND EXTRAORDINARY EARNINGS	Lit.		179,657,838
	TOTAL... Lit.		**11,271,420,142,297**

OF PROFITS

	Lit.	70,031,526,507
	"	70,031,526,507
	"	30,000,000
	"	210,064,579,522
	TOTAL... Lit.	**350,157,632,536**

THE ACCOUNTANT GENERAL
GIANNOCCOLI LUIGI

THE GOVERNOR
CARLO AZEGLIO CIAMPI

ADMINISTRATION OF THE BANK OF ITALY
AS AT 31 DECEMBER 1985

DIRECTORATE

Carlo Azeglio CIAMPI	— GOVERNOR AND CHAIRMAN OF THE BOARD OF DIRECTORS
Lamberto DINI	— DIRECTOR GENERAL
Antonio FAZIO	— DEPUTY DIRECTOR GENERAL
Tommaso PADOA-SCHIOPPA	— DEPUTY DIRECTOR GENERAL AND SECRETARY TO THE BOARD OF DIRECTORS

BOARD OF DIRECTORS

Gaetano CARBONE*
Giovanni CASTELLANI
Francesco CONTI
Gaetano DI MARZO
Luigi FALAGUERRA*
Luigi FANTOLA
Angelo FERRATI
Paolo Emilio FERRERI*
Callisto GEROLIMICH COSULICH
Giuseppe GIOIA
Lucio MORODER
Giovanni Battista PARODI*
Giulio PONZELLINI

* Member of the Executive Committee

BOARD OF AUDITORS

Domenico AMODEO
Alberto CAMPOLONGO
Vittorio CODA
Giuseppe GUARINO
Luigi GUATRI

ALTERNATES

Natalino IRTI
Arnaldo MAURI

CENTRAL MANAGERS

Giorgio SANGIORGIO	— CHIEF LEGAL ADVISER
Antonio MONTORO	— INSPECTOR GENERAL
Luigi PATRIA	— CENTRAL MANAGER FOR TECHNICAL DEPARTMENTS
Felice SCORDINO	— CENTRAL MANAGER FOR THE ROME BRANCH
Vincenzo DESARIO	— CENTRAL MANAGER FOR BANKING SUPERVISION
Antonio FINOCCHIARO	— SECRETARY GENERAL
Rainer Stefano MASERA	— CENTRAL MANAGER FOR ECONOMIC RESEARCH
Pierluigi CIOCCA	— CENTRAL MANAGER FOR CENTRAL BANK OPERATIONS
Luigi GIANNOCCOLI	— ACCOUNTANT GENERAL

LIST OF ABBREVIATIONS

ABI — *Associazione bancaria italiana*
Italian Bankers' Association

ANAS — *Azienda Nazionale Autonoma delle Strade Statali*
State Road Agency

BI-UIC — *Banca d'Italia-Ufficio italiano dei cambi*
Bank of Italy-Italian Foreign Exchange Office

CICR — *Comitato interministeriale per il credito e it risparmio*
Interministerial Committee for Credit and Savings (Credit Committee)

CIP — *Comitato interministeriale per i prezzi*
Interministerial Committee on Prices

CIPE — *Comitato interministeriale per la programmazione economica*
Interministerial Committee for Economic Planning

Confindustria — *Confederazione generale dell'industria italiana*
Confederation of Italian Industry

Consob — *Commissione nazionale per le societa e la borsa*
Companies and Stock Exchange Commission

EFIM — *Ente partecipazioni e finanziamento industria manifatturiera*
Shareholding and Financing Agency for Manufacturing Industry

ENEL — *Ente nazionale energia elettrica*
National Electricity Agency

ENI — *Ente nazionale idrocarburi*
National Hydrocarbon Agency

ILOR — *Imposta locale sui redditi*
Local income tax

INA — *Istituto nazionale assicurazioni*
National Insurance Institute

INAM — *Istituto nazionale per l'assicurazione contro le malattie*
National Health Insurance Institute

INPS — *Istituto nazionale per la previdenza sociale*
National Social Security Institute

INVIM — *Imposta nazionale sul valore immobiliare*
Capital gains tax on property

IRI — *Istituto per la ricostruzione industriale*
Institute for Industrial Reconstruction

IRPEF — *Imposta sul reddito delle persone fisiche*
Personal income tax

IRPEG — *Imposta sul reddito delle persone giuridiche*
Corporate income tax

Isco — *Istituto nazionale per lo studio della congiuntura*
National Institute for the Study of the Economic Situation

Istat — *Istituto centrale di statistica*
Central Institute for Statistics

SACE — *Sezione speciale per l'assicurazione del credito all'esportazione*
Special Department for the Insurance of Export Credits

UIC — *Ufficio italiano dei cambi*
Italian Foreign Exchange Office