BANCA D'ITALIA

ORDINARY GENERAL MEETING OF SHAREHOLDERS

HELD IN ROME ON 30 MAY, 1987

ABRIDGED REPORT
FOR THE YEAR
1986

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THE WORLD ECONOMY

RECENT DEVELOPMENTS AND ECONOMIC POLICIES

In 1986 the industrial economies enjoyed a 9 per cent improvement in their terms of trade, thanks mainly to the fall in the price of oil, which was equivalent to over 1 per cent of their combined gross product.

The benefits of lower energy costs consisted principally in a slowdown in inflation, which came down to the levels prevailing in the early sixties. The stimulus to economic activity was modest, however. Gross national product increased by just 2.4 per cent in real terms, as against 3.0 per cent in 1985. The expansionary impulse stemming from stronger domestic demand was more than offset by the contraction engendered by reduced net exports to the developing countries. The intensity of interaction between the industrial and the developing countries and the sign of the overall impact of the changes in the terms of trade were not correctly estimated when the forecasts for the world economy for 1986 were made. In particular, it had been assumed that in the short run the adjustment of expenditure to the fall in oil prices would be slower in the crude oil exporters than in the importing countries. In fact, however, the fuel exporters quickly trimmed their purchases from abroad, but domestic demand in the industrial countries responded more slowly than expected to the gain in the terms of trade and the decline in interest rates. For the industrial economies as a whole, the fiscal policy stance was slightly restrictive.

Overall, there was an acceleration in household consumption, which expanded by 3.7 per cent as against 3.0 per cent in 1985. This was fueled by rising real income and the increased financial wealth from capital gains associated with the decline in long-term interest rates. In some of the leading countries (Germany and Japan), part of the added income was utilized to acquire financial assets, which was reflected in a rise in the propensity to save.

Capital formation slowed sharply, despite the improved profitability of firms. Private fixed investment expanded by just 1 per cent in volume, as against 10 per cent the previous year, because of expectations of only modest demand expansion, persistently high real interest rates and exchange rate uncertainty.

The very large growth rate differential between the United States and the rest of the OECD area that had marked the first two years of the current expansion beginning in 1983 has been gradually eliminated. In 1986, the expansion of GNP was the same in the United States as in the other OECD countries and the EEC — 2.5 per cent. Nor were there any significant differences in the growth of domestic demand.

Inflation slowed down dramatically, even though in several countries (Spain, Denmark and Switzerland as well as Italy) part of the benefit of lower energy prices was channeled to the public finances. For the industrial countries as a whole, consumer prices rose by 2.3 per cent, as against 4.1 per cent in 1985. The deceleration of the GNP deflator was less pronounced, coming down from 3.8 to 3.4 per cent. Consumer prices declined by 0.2 per cent in Germany and held virtually stable in Japan, while inflation was very moderate in the United States as well (2 per cent). The greatest progress in disinflation was made in Italy, France and the United Kingdom, where the inflation rate declined by about three percentage points. Wholesale prices in the leading economies declined on average by more than 4 per cent.

The decline in oil prices and the weakness of non-oil raw material prices were decisive in the reduction of inflation. For Japan and the EEC countries, the impact on import prices was amplified by the appreciation of their currencies (Table 1). In the United States, the inflationary effect of the depreciation of the dollar was moderated by the tendency of overseas exporters to counteract the variation in exchange rates by narrowing their profit margins.

The slight expansion of the demand for labour that manifested itself in 1984 and 1985 continued last year. Total employment in the OECD countries increased by 1.6 per cent. The rise in employment was accompanied by a comparable expansion of the labour force, owing above all to higher participation rates stimulated by the increased demand for labour and the enhanced flexibility of labour markets. The unemployment rate therefore remained unchanged at about 8 per cent for the industrial countries as a group. The gap between North America and Europe widened, however, as the rate declined further in the United States (from 7.2 to 7.0 per cent) and in Canada (from 10.5 to 9.6 per cent), while it held at 11.4 per cent for the EEC, rising in France, Italy and the United Kingdom and declining in Germany (from 8.3 to 7.9 per cent) and in some smaller countries (the Netherlands, Denmark and Belgium). In Japan the unemployment rate rose to a postwar high of 2.8 per cent.

The rate of growth in the developing countries accelerated slightly, from 3.2 to 3.5 per cent, but there were marked differences between groups of countries, some of which were damaged by the sharp deterioration of the terms of trade and the shortage of external financing.

Table 1

PRICES AND LABOUR COSTS IN THE UNITED STATES, JAPAN AND THE EEC

(percentage changes)

	Consumer prices	Import prices (1)	Unit labour costs (2)	Wages (3)
United States				
1983	3.2	−4.1	1.8	4.5
1984	4.3	1.8	3.1	4.9
1985	3.5	−2.5	4.1	4.5
1986	2.0	−3.1	2.7	2.8
Japan				
1983	1.9	−9.2	1.8	2.5
1984	2.2	−2.7	0.5	3.9
1985	2.1	−3.6	0.1	3.4
1986	0.6	−38.7	3.0	3.5
EEC				
1983	7.8	5.0	4.6	9.9
1984	6.7	9.3	5.2	7.6
1985	5.8	3.3	4.8	6.8
1986	3.3	−13.1	4.3	6.2

Sources: EEC, OECD and IMF.
(1) Average unit values. — (2) For entire economy. — (3) Earnings per employee, entire economy.

In the fuel-exporting countries, the drop in export earnings from crude oil forced a rapid adjustment, which meant an overall decline in income of 0.7 per cent. The cost in terms of growth was particularly high for such heavily indebted countries as Mexico and Nigeria, because of the severe financial constraints on them. Despite a very substantial contraction of 22 per cent in the volume of imports and an expansion of 10 per cent in exports, the fuel-exporting countries' balance of payments on current account deteriorated from a surplus of \$3 billion in 1985 to a deficit of \$36 billion in 1986.

For the non-fuel LDCs, the fall in oil prices combined with the benefits of increased imports by the industrial countries and a decline in interest rates to accelerate growth. In the primary product exporters, whose terms of trade remained virtually unchanged, the rate of growth rose from 3.2 per cent in 1985 to 5.2 per cent. Thanks especially to the performance of several Asian LDCs, the best results were obtained by countries exporting manufactures, which achieved a substantial increase in income (6 per cent) and in export volume (14 per cent).

The internal adjustment of the most heavily indebted countries slowed down. Budget deficits, at 4.5 per cent of GDP, returned nearly to the levels of 1983, after declining to about 3 per cent as a result of the stabilization programmes implemented in 1984 and 1985. Moreover, inflation in the most heavily indebted countries is still almost three times as fast as the average for all LDCs, despite a slowdown in consumer price inflation from 127 per cent in 1985 to 76 per cent last year.

Their exports diminished by 7 per cent in volume terms, while those of the LDCs as a whole expanded by 8 per cent. Given their persistent difficulties in securing external financing, the large debtors suffered a decline in the volume of imports for the fourth time in the last five years. In 1986 their import volume was 40 per cent less than in 1981, the year before the outbreak of the debt crisis.

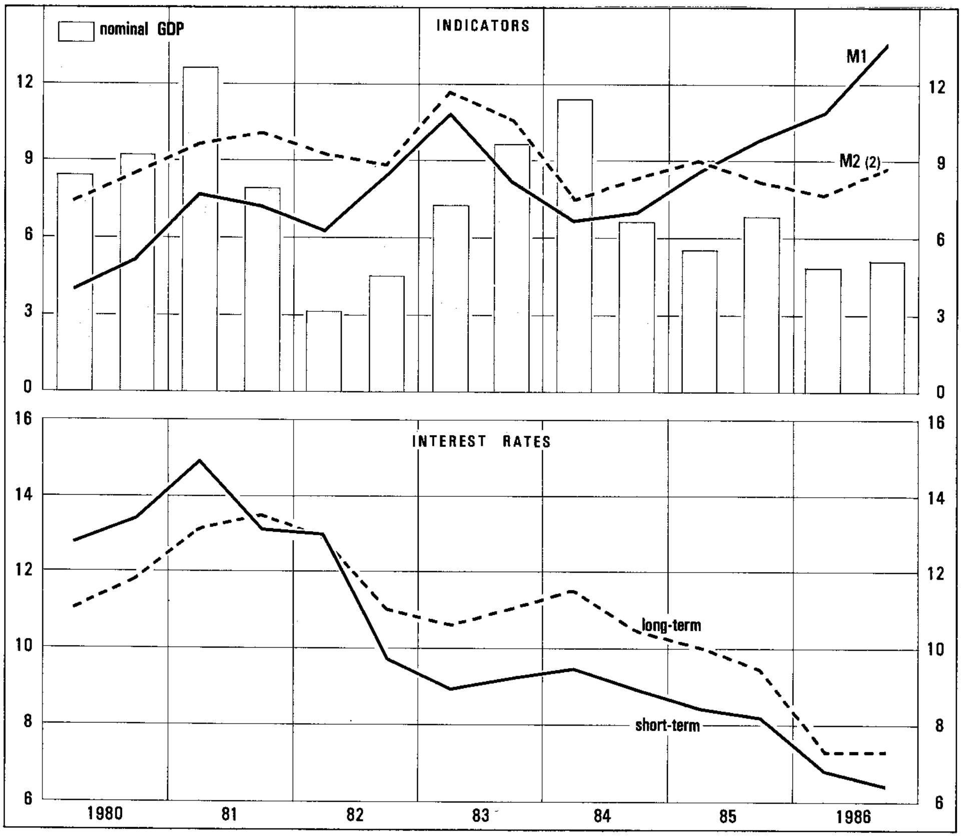
Monetary policies. — The stance of monetary policies in 1986 was generally more expansionary than the year before. For the major industrial countries as a group, there was a faster expansion of M1 and M2 (12.2 and 8.6 per cent respectively), and both these aggregates grew substantially faster than did nominal product. Both short-term and long-term interest rates declined (Figure 1).

The pronounced increase in liquidity reflected the desire of policymakers to hasten the reduction of interest rates and in this way stimulate economic growth at a time of rapid disinflation. Large-scale intervention in the foreign exchange markets in support of the dollar helped spread the effects of the rapid expansion of the money supply in the United States to other countries.

The growth of the reference aggregates in the major industrial countries overshot the targets. In the United States M2 was held within the predetermined limits, but M1 was above the target range throughout 1986, prompting the Federal Reserve to discontinue the publication of quarterly targets for this aggregate in the second half of the year. In Germany, for the first time since 1978 the expansion of central bank money (7.7 per cent in the reference period) overshot the upper limit of the target range by more than two percentage points, owing mainly to massive inflows of foreign exchange. In the United Kingdom sterling M3 also strayed far from the target path. However, the figures on the performance of these aggregates tend to overestimate the stimulus to the economy from monetary policy. In 1986 part of the expansion in liquidity was matched by an increased demand for money occasioned by the decline in interest rates and the gathering momentum of financial innovation and deregulation, notably in France and the United Kingdom.

Figure 1

MONETARY POLICY INDICATORS AND INTEREST RATES FOR THE MAJOR INDUSTRIAL COUNTRIES (1)



Sources: IMF and BIS.

(1) Monetary aggregates and nominal income: annualized rates of change on the previous half-year in per cent. — (2) M2 except for Germany (M3) and the United Kingdom (sterling M3).

Nominal interest rates declined everywhere in the course of the year, although the trend was temporarily interrupted in several countries by exchange rate pressures. In the United Kingdom the base rate was raised at the start of the year following pressure on sterling. It was then lowered steadily over succeeding months until October, when the pound came under renewed pressure. In France the intervention rate was gradually lowered by almost two percentage points, but towards the end of the year it was temporarily raised again in response to intensified pressures on the franc. Elsewhere, the reduction of interest rates was more continuous; it was quite substantial (two or three points) in Japan, Canada and Italy, more modest in the United States. Only in Germany was there no significant change. The fastest decreases in long-term interest rates came in France and the United States.

After a period of stability, US interest rates came under upward pressure in April 1987, rising by about half a point compared with the end of 1986. In Germany and Japan, by contrast, interest rates have declined since the beginning of the year. There has thus been a widening of the differential in favour of dollar assets, which had been progressively narrowed in 1986, most especially vis-à-vis the Deutschemark.

The monetary authorities' management of official rates was influenced partly by the desire to accentuate the fall in market interest rates associated with the slowdown in inflation and partly by the higher priority assigned to exchange rate objectives. The greater attention paid to interest rates and exchange rates in the conduct of monetary policy can be attributed in part to financial innovation, which has weakened the basis of monetary control founded upon quantitative targets. After the reduction in official rates in all the leading countries in March and April 1986, the Federal Reserve twice lowered its discount rate during the summer, bringing it down to 5.5 per cent, and thereby encouraging a further depreciation of the dollar. The Japanese authorities lowered the discount rate to 3 per cent in October as part of their bilateral agreement with the United States to stabilize the dollar/yen exchange rate, and reduced it again to 2.5 per cent in February 1987.

Monetary action in Germany sought to curb the expansion of domestic liquidity produced by the massive inflow of capital, most of which came from the dollar area. The excessive growth of the target aggregate led the authorities to delay the reduction in official interest rates, even though the persistent strength of the Deutschemark signalled fairly tight monetary conditions, particularly in the second half of the year. Only after the realignment of EMS central parities on 11 January 1987 were the discount and lombard rates lowered by half a point, to 3 and 5 per cent respectively, in view of the continuing appreciation of the Deutschemark.

Judging from the announced growth targets, the stance of the monetary authorities in the leading countries in 1987 will not differ greatly from that of 1986. In the United States, however, the rise in short-term interest rates in April indicates the emergence of domestic liquidity strains connected with problems in financing the current account deficit.

Fiscal policies. — Net public sector borrowing in the industrial countries as a group remained at 3.4 per cent of GDP, the same as in 1985. The ratio of the budget deficit to GDP increased slightly in France and the United Kingdom, while it declined by more than a point in Italy and Canada. In the United States, Japan and Germany it was unchanged.

According to the indicators devised by international organizations to express changes in the budget balance net of cyclical variations, the impact of the public sector was slightly restrictive, after three years of moderate stimulus. This reflected fiscal austerity measures in Canada and also, though more modest, in the United States. Fiscal policy became less restrictive in the other leading countries, which for some years now have been pursuing strategies to restore their public finances to a sound footing in the medium term.

In the United States, the federal budget deficit for the 1986 fiscal year was $221 billion, practically $50 billion over the target. Despite the widening of the actual deficit, it is estimated that the fiscal impact was neutral, compared with a cumulative expansionary effect of 3 per cent from 1980 to 1985.

In Japan the budget impact was less restrictive than in 1985, thanks to measures enacted in April to stimulate domestic demand. Germany continued its policy of curbing public spending and the budget deficit, which was held to 1 per cent of GNP. At the same time, income tax reductions equivalent to 0.6 per cent of GNP came into effect at the beginning of the year as the first step in a broader reform of taxation. The overall fiscal impact was neutral.

On the revenue side, a number of countries have enacted or are studying proposals for tax reform based on the principles of allocative efficiency, simplicity and fairness.

In the United States, the law passed in late 1986 has reduced the number of income tax brackets, lowered tax rates and broadened the tax base. The highest corporate income tax rate has been reduced from 46 to 32 per cent, while the minimum rate has been raised. The reform, which will become fully effective in 1988, is not expected to affect overall tax revenue over the next five years; the decline in receipts from personal income taxes should be offset by increased revenue from corporate income tax.

The proposals now being considered in Japan aim to ease the tax burden on personal incomes by measures similar to those taken in the United States. The rates of corporate tax would be reduced over three years. The decline in revenue from direct taxes would be offset from 1988 onwards by the introduction of a value added tax.

In Germany, further cuts in direct taxation are planned for 1988, for a total of DM 13.7 billion, or 0.6 per cent of GNP. The authorities have also announced that a broader tax reform reducing personal income tax rates and modifying corporate taxation will be implemented by 1990.

OECD and IMF projections indicate that the impact of fiscal policy in the principal countries as a group will be slightly more restrictive in 1987 than in 1986. The sharply contractive effect expected in the United States, where the budget act passed in December 1985 should begin to make itself felt more strongly, will not be offset by the merely neutral fiscal stance in the rest of the industrial countries.

The budget for the 1987 fiscal year puts the US federal deficit at $173 billion, or 3.9 per cent of GNP, as against 5.3 per cent in 1986, as a result of reduced expenditure and a temporary increase in revenue generated by the tax reform. The results for the first half of the fiscal year show a containment of the deficit, but sharper restrictions will be needed in the rest of the year if the target is to be achieved.

In Japan, the additional expenditure approved in late 1986 to stimulate domestic demand, partly in response to international urging, is not thought to be sufficient to correct the restrictive stance that has prevailed so far. In the main European countries, the budget deficit as a share of GDP is not expected to vary significantly from 1986. The fiscal impact should be virtually neutral in Germany and slightly restrictive in France, where the deficit is to be reduced as part of a medium-term strategy of decreasing government intervention in the economy, in part through large-scale privatization.

The world economic outlook. — The latest IMF and OECD forecasts do not envisage any change in the terms of trade of the industrial countries in 1987. The expansion of demand and of economic activity will still benefit in part from external stimulus, in that some countries will still be feeling the delayed effects of the fall in the cost of oil and other raw materials.

Domestic demand is expected to expand at a rate of about 2.5 per cent, one point less than in 1986. The expected recovery in investment, fueled by large profits and easy monetary conditions, will not be large enough to offset the deceleration in consumption, owing partly to the restrictive fiscal stance. External demand will have only a slightly negative influence, thanks to a recovery in the imports of the LDCs. This will enable GNP in the industrial countries to expand by some 2.5 per cent, about the same as last year but more than half a point less than had been forecast towards the end of 1986.

Such slow economic expansion does not appear sufficient to make significant inroads into unemployment. Some improvement is expected in the United States, but in Europe the unemployment rate will remain at its current level of 11.5 per cent, while in Japan it could rise to 3 per cent.

Inflation in the industrial area will be about 3 per cent, thanks in some cases to the lag with which lower import costs have fed through into domestic prices and in general to the absence of domestic cost pressures. Nominal wages are expected to rise by 4 per cent and unit labour costs by under 3 per cent. Profit margins should stabilize.

The variations that have occurred in exchange rates will influence the distribution of demand and output among the leading economies. The external contribution to growth will continue to be negative in Japan and the leading European countries, while in the United States it will turn positive for the first time since 1980. The growth of domestic demand is expected to decelerate sharply in the United States, from 3.5 to around 2 per cent, as a result of the restrictive budget measures, and to slow down to 3 per cent in Europe; forecasts for Japan range from 2.5 to 3.8 per cent.

According to OECD estimates, economic activity will be stronger in the United States than in the rest of the industrial area. The growth rate is expected to rise in the US, while it will remain practically unchanged in Japan and will decline to around 2 per cent in Europe. The IMF, on the other hand, forecasts no significant difference in growth rates between the major countries. The outlook for the German economy is particularly unsatisfactory, with both national and international forecasting agencies estimating growth at between 1 and 2 per cent in 1987.

The leading international institutions forecast no change in the terms of trade of the LDCs. Many of them will nonetheless have to continue to adjust to the deterioration suffered in 1986. This, coupled with the slowdown in the growth of domestic demand in the industrial economies, will cause the growth rate to decline to about 3 per cent, as against 3.5 per cent in 1986. Output is expected to stagnate in the fuel-exporting countries and to grow at a rate of 4 per cent in the other LDCs.

These forecasts partially incorporate the expected effects of the commitments entered into by the governments of the major countries in the Louvre Agreement of 22 February 1987 and reaffirmed at the Washington meeting on 8 April. The principle underlying the Agreement is the recognition that reducing the current account imbalances among the major countries to sustainable proportions will require a shift in the expansion of domestic demand to the countries with substantial surpluses, while maintaining strong growth in the industrial area as a whole. However, this redistribution of economic activity has not yet been sufficiently backed by fiscal policy in the major countries.

In these circumstances, there is an urgent need for coordination of macroeconomic policies, which was brought to the attention of the international community by the Tokyo summit of the Heads of State or Government of the seven leading industrial countries in May 1986. It was agreed at that time to form a Group of Seven Finance Ministers with a mandate to perform periodic analysis of the objectives and forecasts of the seven countries, in collaboration with the IMF, on the basis of a broad range of macroeconomic indicators in order to ensure the international compatibility of the policies pursued.

However, difficult problems have emerged, with regard not only to the criterion for assessing the medium-run sustainability of current payments disequilibria, and hence the compatibility of present policies, but also to the ability of sovereign nations subject to political and institutional constraints to accept the discipline inherent in the coordination exercise, including stricter mechanisms for the implementation and verification of the agreed corrective measures.

EXCHANGE RATES AND WORLD TRADE

Exchange rates and the current accounts of the leading industrial countries

The dollar, the yen and the Deutschemark. — The depreciation of the dollar continued during 1986 and the first four months of this year. By April 1987 the effective exchange rate of the US currency was 34 per cent below the peak reached at the end of February 1985 (a decline of more than 30 per cent in real terms) and had fallen below its 1980 level. During the period in question the dollar has depreciated by 45 per cent against the Deutschemark, 42 per cent against the ECU and 46 per cent against the yen, whose exchange rate has recently risen to an unprecedented post-war level.

At the Tokyo summit in May 1986 the governments of the seven leading industrial countries recognized the need to promote the adjustment of current account disequilibria through the adoption of economic policies that would reduce the disparity between saving and investment in the three largest countries. During the months that followed, the US Administration encountered difficulties in implementing the programme of measures to reduce the budget deficit, while fiscal policy remained restrictive in Japan and more or less neutral in the Federal Republic of Germany. Moreover, interest rates were not reduced in Japan by as much as in the United States and were kept unchanged in Germany.

At the European Council meeting in Gleneagles in September the central banks of the EEC countries agreed on action to curb the appreciation of European currencies against the dollar. After a brief period of stability, during which the dollar exchange rate fluctuated around DM 2 and 154 yen, the downward pressures on the dollar reappeared, particularly with regard to the yen. The announcement of a bilateral agreement between Japan and the United States at the end of October and further massive intervention by the Japanese central bank caused the dollar to strengthen by 4 per cent against the yen between the last week of October and mid-December, when the bilateral exchange rate stood at 163 yen to the dollar; over the same period the US currency depreciated by 1 per cent against the Deutschemark. The yen/DM exchange rate returned to the level recorded at the start of the year. The dollar began to weaken again in the last week of December, depreciating by a further 5 per cent in effective terms between then and the end of February.

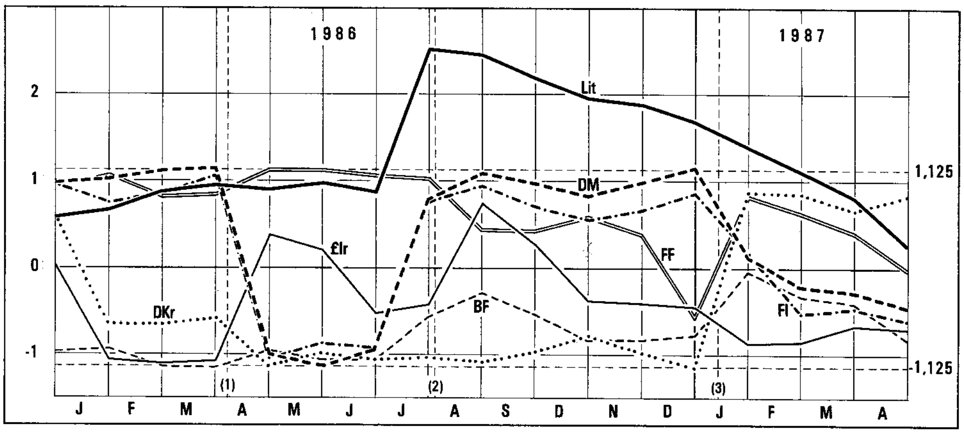
In Paris in February of this year the members of the Group of Five and Canada agreed to cooperate closely to foster exchange rate stability at around the levels then obtaining (153 yen and DM 1.83 to the dollar) and to intensify the coordination of domestic economic policies. However, these commitments were not translated into action, apart from a half-point reduction in the discount rate in Japan. The net intervention purchases of dollars totaling more than $20 billion in late February and March, to which the US Federal Reserve System contributed a significant amount, made it possible to resist the pressures on the dollar. However, the dollar resumed its downward path in April, so that by the end of the month it was being quoted at 139 yen and DM 1.79; the effective exchange rate was 4 per cent below the level recorded in the week following the Louvre Agreement.

The European Monetary System. — The exchange rates between the currencies participating in the EMS exchange rate mechanism displayed a high degree of stability in the two months following the realignment of April 1986 (Figure 2).

Figure 2

EMS EXCHANGE RATES

(percentage changes with respect to central rates; end-of-period data)



(1) Realignment of 6 April 1986. — (2) Realignment of 7 August 1986. — (3) Realignment of 12 January 1987.

During the summer, the pronounced weakening of the dollar and the continued narrowing of the differential vis-à-vis interest rates in the Federal Republic of Germany and the Netherlands, where rates had been kept unchanged, caused the Deutschemark and the Dutch guilder gradually to strengthen. The Irish pound came under downward pressure and on 4 August its central rate was reduced by 8 per cent against the other EMS currencies.

In the second half of September the DM was pushed towards the upper limit of the band by substantial inflows of capital into Germany, accentuated partly by the liberalization of exchange controls in France and Denmark. The Bank of France made intramarginal interventions to counteract downward pressure on the franc. The lira was unaffected by the tensions and remained above the narrow band of fluctuation. The interventions carried out in support of the dollar after the Gleneagles Agreement, especially by the Deutsche Bundesbank, eased the pressure in the foreign exchange markets and brought the Deutschemark back towards the centre of the band.

However, in the first few weeks of December the DM again moved towards the upper limit, partly owing to the increase in very short-term interest rates in Germany. The German authorities decided not to accommodate the seasonal increase in the demand for money in order to avoid further inflating the money supply, which had already exceeded the targets. Short-term interest rates were raised in France and Italy too in order to maintain cohesion within the EMS. Strong pressures developed within the System at the end of the year in connection with a renewed weakening of the dollar to below DM 2. Political developments in the Federal Republic of Germany and France helped fuel expectations of a possible realignment. Influences working in the opposite direction included the narrowing of inflation differentials, which had made it possible to keep real exchange rates within the area virtually unchanged at the levels attained after the April realignment, and the improvement in current account balances in all member countries except Denmark.

The negative factors prevailed, so that pressure mounted. On 7 January the French franc was allowed to sink to the lower limit against the Deutschemark. The Deutsche Bundesbank had not intervened in the few days previously, but the EMS Agreement now obliged it to make large-scale intervention purchases to support the franc.

On 8 January the Bank of Italy let the lira exchange rate slip by 1.3 per cent, bringing the currency close to the centre of the band, where it stabilized without the need for further intervention. However, pressure increased on the other currencies in difficulties, especially the French franc, so that it became clearly impossible to continue to defend the official parities. On 12 January 1987 the Ministers of Finance and central bank Governors of the EEC countries decided to carry out the eleventh realignment since the inception of the EMS. The central rates of the Deutschemark and Dutch guilder were raised by 3 per cent and that of the Belgian franc by 2 per cent against all the other EMS currencies.

Market exchange rates showed very little change immediately after the realignment. Only Italy experienced inflows of capital. From the beginning of February onwards the realization that the decline in German interest rates was permanent dissipated any remaining doubts about the sustainability of the new central rates; capital began to flow back into France and the other countries that had not revalued. The scale of capital inflows into Italy, which by then had substantially exceeded the outflows that had occurred before the realignment, was a factor in the monetary authorities' decision on 13 March to reduce the discount rate by half a point and to curb the creation of credit via the external sector by introducing a 25 per cent reserve requirement on changes in banks' net foreign currency liabilities.

The current accounts of the three leading industrial countries. — In the last two years the considerable changes in the nominal exchange rates of the dollar, the yen and the Deutschemark against the currencies of the other leading industrial countries translated into comparable variations in real exchange rates (Table a8). Nevertheless, current account disequilibria actually increased and assumed unprecedented proportions: a deficit of $141 billion for the United States and surpluses of $86 and 37 billion for Japan and Germany respectively. The deterioration of $23 billion in the US current account since 1985 was entirely due to a parallel worsening of the trade deficit to $170 billion on the basis of customs data.

The reasons why US foreign trade has failed to improve are still being examined. Trade with the rapidly industrializing countries in the Far East and Canada accounts for 32 per cent of the overall deficit. Since the currencies of these countries have not appreciated against the dollar, American producers have not been able to restore their competitiveness in these markets.

The commodity markets and world trade

Raw materials and oil. — The dollar prices of primary products excluding energy fell by 3.8 per cent on the IMF index. Their relative prices in relation to those of manufactured exports by industrial countries came down by around 19 per cent to their lowest level since the thirties; in the case of raw materials from developing countries alone the decline was 16 per cent. Oil prices fell by almost 50 per cent on an annual average basis.

International trade and the current accounts of the major areas. — In the light of the collapse in oil prices, the main change in the volume of world trade was a substantial contraction of 22 per cent in imports by fuel-exporting countries, whereas those by industrial countries increased by 9 per cent.

The trade balance of the industrial countries deteriorated sharply in volume terms, with imports expanding by 9 per cent, three times the rate of growth of exports. Nevertheless, the improvement of 9.4 per cent in their terms of trade, the largest gain of the post-war period, eliminated the trade deficit of more than $40 billion recorded in 1985. Their current account improved by around $45 billion to show a deficit of only $7.5 billion.

By contrast, the trade balance of developing countries improved very substantially at constant prices. Fuel exporters offset part of the effect of the fall in oil prices by adjusting the volume of their trade, thereby limiting the reduction in their surplus, which amounted to slightly less than $20 billion. Their aggregate current account moved back into a deficit of $36 billion after briefly recording a modest surplus of $3 billion the previous year. Non-fuel developing countries reduced their current account deficit by about $15 billion to $11.9 billion, mainly as a result of the expansion in the volume of trade, since their terms of trade remained stable.

World trade in agricultural products. — The eighties have seen world trade in agricultural products grow by an average of 1.5 per cent a year, one third the rate recorded in the preceding decade and one percentage point slower than the growth in supply. The value of world agricultural trade decreased from 14.9 per cent of total trade in 1980 to 13.8 per cent in 1985. The industrial countries' agriculture balance shifted from a surplus of around $1 billion in 1980 to a deficit of more than $3 billion in 1985.

The European Community's changed position in world trade in foodstuffs was due largely to the operation of the Common Agricultural Policy, which helped to reduce and in some cases eliminate the deficits in various products and to increase the surpluses in others. Cereals are a case in point; the shortfalls of the seventies gave way to growing surpluses from 1980 onwards, reaching $2.7 billion in 1985.

The position of individual countries in the Community market also changed profoundly. As regards trade in products explicitly covered by the rules of the CAP, Italy's deficit vis-à-vis the rest of the Community steadily increased to more than $7 billion in 1984-85 owing to the rise in the deficit with the Federal Republic of Germany, France and the Netherlands. By contrast, there were improvements in the position of Germany, whose deficit in agricultural products decreased between 1977-78 and 1984-85, and especially those of France and the Netherlands, which recorded growing surpluses. Marked differences were also evident in the behaviour of countries' exports of agricultural products to other members of the Community. Between 1970 and 1985 Germany recorded the largest gains in all member countries' markets and in all products, including some typical of the Mediterranean region. France's market share contracted significantly, but Italy achieved modest improvements in some sectors where it has structural deficits while suffering sometimes significant losses of market share in sectors in which it should have exploited its greater comparative advantages, such as fruit, vegetables and wine.

CAPITAL MARKETS, EXTERNAL DEBT AND OFFICIAL RESERVES

International capital markets

For the international capital markets 1986 was the third consecutive year of strong expansion. Total gross lending amounted to $376 billion, an increase of 34 per cent over the previous year. As in 1985, loans renegotiated in the light of the fall in interest rates and the continuing improvement in credit terms accounted for a large proportion of operations. Net of renegotiations and double counting, the flow of lending rose to $262 billion, against $182 billion the previous year.

The BIS reporting banks' external assets expanded by a record $477 billion at constant exchange rates in 1986, mainly owing to strong growth in the second half of the year. The expansion was double that of 1985 and 80 per cent larger than the previous record achieved in 1981. Much of it, however, was due to the exceptional expansion of interbank assets, which rose from 78 to 90 per cent of the total between 1985 and 1986.

International bond issues increased by 35 per cent to $226 billion. After allowing for refinancing operations, net issues came to about $156 billion, an increase of 25 per cent over 1985. Straight and convertible bond issues showed the largest growth. The volume of floating rate issues, by contrast, slipped back from $58 to 51 billion in spite of an increase in the second half of the year.

After three years of steady decline, syndicated loans showed signs of a recovery, with total new credits rising from $42 to 48 billion. Lending terms improved further for borrowers: the average spread over LIBOR fell from 60 basis points in 1985 to 40 in 1986.

Back-up facilities, on the other hand, contracted sharply, with total issues falling from $47 to 27 billion. This reduction was more than offset by recourse to Eurocommercial paper and other non-underwritten facilities. Within the space of just two years, the ECP market has become the second largest after that in straight bonds.

Gross lending to industrial countries continued to increase its share of the total in 1986, rising from 82 to 91 per cent. By contrast, lending to both non-oil LDCs and Eastern Europe was halved, falling to 4 and 1 per cent of the total respectively.

With regard to the currency composition, lending in dollars remained stable at around 64 per cent of the total at constant exchange rates. The yen strengthened its position among the main international currencies, particularly in the bond market, where issues in yen reached a new peak of 8 per cent. On the other hand, the share of lending in ECUs declined noticeably, both in the bond market, where it contracted from 4.6 to 2.9 per cent, and especially in the syndicated loan market, where it fell from 6.2 to 1.7 per cent.

External debt

The debt situation of LDCs worsened during 1986. For the fifteen most heavily indebted countries, the debt service ratio rose to 44 per cent, the highest level since the one recorded in 1982, at the onset of the debt crisis.

The Eastern European countries' gross debt in convertible currencies rose for the second year running, from $96 billion at the end of 1985 to $115 billion a year later. Their debt/export ratio rose from 124 to 174 per cent over the same period. The current account balance of these countries in convertible currencies recorded a deficit of $1 billion, the first deficit since 1981. Some of this deterioration was attributable to the Soviet Union, whose exports were adversely affected by the fall in oil prices.

The proposal for tackling the debt crisis put forward in October 1985 by US Treasury Secretary Baker did not produce the hoped-for results during 1986. External financing failed to match expectations, mainly on account of the commercial banks' growing reluctance to increase their exposure to debtor countries. Furthermore, the macroeconomic environment was less favourable than envisaged, since the expansion in economic activity in the industrial countries and the growth in world trade were both lower than had been forecast.

On account of restructuring, the short-term portion of total LDC debt fell from 18 per cent in 1985 to 16 per cent last year. Seventeen rescheduling agreements involving debts totaling $13 billion were concluded by the Paris Club during 1986. Long-term debts renegotiated by commercial banks amounted to $62 billion, compared with around $13 billion in 1985. Mexico accounted for $44 billion of this, Brazil for $7 billion and Nigeria for $4 billion.

Notwithstanding rescheduling and the fall in interest rates, LDCs' payments to service medium and long-term debt are estimated by the World Bank to have exceeded new loans for the third year in succession. In the case of the most heavily indebted countries, this negative transfer totaled $26 billion, equal to more than 3 per cent of their GDP.

This development reflected the decrease in net foreign lending to LDCs for the fifth consecutive year to $35 billion in 1986. The contraction in credit from private sources was not offset by an increase in either official transfers or direct investments, which totaled $14 and 13 billion respectively.

New IMF credit to LDCs amounted to around SDR 4 billion, the same figure as in 1985. Following the sharp increase in repayments on loans granted to these countries since 1982, however, net IMF lending was negative last year for the first time since the onset of the debt crisis.

Lending by multilateral development banks expanded at a satisfactory pace, although by less than suggested by Secretary Baker. The World Bank greatly increased its total lending, especially fast-disbursing structural and sectoral adjustment loans. The rise in World Bank disbursements and the agency's expanding role in efforts to tackle the debt crisis mean that agreement to increase the Bank's capital must be reached in the near future. In the absence of such agreement, lending could reach the permitted limits in the financial year ending in June 1988.

Commercial bank lending fell short of the volume proposed in the Baker initiative. In dollar terms, the exposure of BIS reporting banks towards the most heavily indebted countries rose by $4.3 billion, or 1.5 per cent. The increasing delays in reaching agreement on financial packages for these countries also gave rise to difficulties.

Official reserves

At the end of 1986 the official reserves (excluding gold) of IMF member countries stood at $505 billion, an increase of 14 per cent over the previous year. The expansion occurred solely in the reserves of the industrial countries and was due mostly to their interventions in support of the dollar. The rapid increase in the foreign exchange reserves of industrial countries accounted for 88 per cent of the total growth in international reserves.

The deterioration in the external position of the LDCs caused their official reserves to decline by $14 billion (8 per cent), mainly owing to the large decrease registered by oil-exporting countries. The contraction was even more marked (17 per cent) if reserves are expressed in SDRs. At the end of last year the total reserves held by LDCs stood at $158 billion, more than 8 per cent lower than at the close of 1980; over the same period their share of total official reserves fell from 42 to 31 per cent.

As a result of the rise in the price of gold from $327 to 391 per ounce during 1986, the market value of gold reserves increased from $310 to 372 billion. On the other hand, official ECU reserves declined slightly. The rise in ECUs created by the EMCF against dollar payments by participating countries was outweighed by a fall in those created against gold as a result of the decline in the value of gold expressed in ECUs.

THE ITALIAN ECONOMY

DEMAND, OUTPUT AND THE BALANCE OF PAYMENTS

The outturn for the year

The exceptional improvement recorded in the terms of trade in 1986 as a result of the fall in the price of oil and the depreciation of the dollar fostered a swing into surplus on the current account of the balance of payments and a slowdown in the rate of inflation. At the same time it generated conditions favourable to a rise in GDP.

The growth in real GDP (2.7 per cent) was slightly higher than the average for the EEC and the OECD. However, it was unchanged compared with the previous year and failed to make a significant impact on the underlying trends that have emerged in the labour market in recent years.

The increase in employment (121,000) fell far short of the increase in the labour force (351,000). The unemployment rate rose from 10.3 per cent in 1985 to 11.1 per cent, and from 11.7 to 12.4 per cent when workers on Wage Supplementation are included. The gap between labour market conditions in the Centre-North and those in the South widened further. In the Mezzogiorno, where unemployment is concentrated among women and young people of less than 29, the rate rose from 14.3 to 16.5 per cent, while in the Centre-North it remained virtually unchanged (8.5 per cent, as against 8.4 per cent). In terms of equivalent workers based on the new national accounts definition, unemployment rose by 0.8 per cent, with most of the increase among self-employed workers. The sectoral results show that the further rise in employment in services more than offset the continued declines in agriculture and industry.

The average increase in prices in 1986 amounted to 5.9 per cent, which was in line with the target rate for the year. The increases introduced in the duties on oil products affected the transmission of the collapse in oil prices and reduced its disinflationary impact on consumer prices. On the other hand, the rise in the latter was curbed by the new mechanism for cost-of-living allowances introduced at the beginning of 1986; one of its effects was to reduce the frequency of such increases. Inflation came down steadily during 1986, and in the last part of the year the Italian rate of consumer price inflation slowed to about 4 per cent, the lowest level for eighteen years. The inflation differential vis-à-vis the other leading industrial countries narrowed to about 2 points.

The pricing policy followed by industrial firms, which sought to improve their overall profit margins while holding down their export prices, prevented a more pronounced decrease in this differential. In manufacturing industry a 3.7 per cent rise in unit labour costs combined with a 2.6 per cent fall in the prices of inputs to leave total unit costs virtually unchanged over the year. By contrast, production prices rose by 3.0 per cent and average export unit values declined by 0.6 per cent.

The current account of the balance of payments recorded a surplus of 6 trillion lire. Compared with the 1985 deficit, there was a swing of nearly 13 trillion lire. This was less than the improvement in the trade balance (17.5 trillion lire), owing to the large increase in public transfers, which was coupled with virtually no change in the surplus on services.

When the external accounts are examined in terms of value and volume, the external surplus is found to have been produced by the 14 point improvement in the terms of trade. The increase in imports in volume terms (5.1 per cent) having actually exceeded that in exports (3.1 per cent).

This increase was nonetheless in line with the growth in world demand, even though the price competitiveness of Italian goods steadily declined over the year and firms had to cope with substantial changes in the relative importance of their markets. The OPEC crisis, the large loss of competitiveness in the dollar area, the problems of the non-oil developing countries and of those in Eastern Europe stimulated exporters to build up their business in Western Europe. The share of total exports going to the other EEC countries rose by more than 5 points to over 53 per cent.

The improvement in the terms of trade and the consequent opening of a differential between the rise in the prices of domestic factors of production and that of sales prices considerably boosted firms' purchasing power in real terms, as well as producing a less pronounced increase in that of households. The 8.1 per cent rise in the GDP deflator was matched by an increase of 5 per cent in the deflator of domestic demand.

Even though the public sector borrowing requirement decreased compared with 1985, the net indebtedness of general government increased further. At the aggregate level, public finances are estimated to have had a moderately expansionary effect on the economy, in part owing to the smaller loss of purchasing power incurred by the public debt. Monetary and exchange rate policy continued to foster the slowdown in inflation and the restructuring of industry.

Corporate profits were used, both in Italy and abroad, to invest not only in capital goods but also in financial assets.

Gross capital formation expanded again, albeit more slowly than in 1985 (1.2 per cent compared with 3.3 per cent), and ran at a rate in volume terms close to the record levels of 1980. Investment in machinery, equipment and transport equipment had already reached a new peak the year before, and expanded by an additional 3.1 per cent. Investment serving to rationalize production and modernize obsolete plant was coupled last year with a moderate amount of investment serving to expand capacity.

Households' disposable income rose by 2.5 per cent in real terms. The firmer prospects of continued growth and the greater value of real wealth encouraged a rise in consumption, especially of durable goods. Sales of the latter increased by nearly 6 per cent. The lags with which non-durable consumption responds to changes in wealth led to its expanding more moderately (2.5 per cent). Overall, final national consumption rose by 3.8 per cent, the highest rate since the beginning of the eighties. This was paralleled by a reduction in households' propensity to save.

The distribution of income shifted in favour of unearned income. In the private sector the share of value added at factor cost that was accounted for by the compensation of employees and income from self-employment fell from 70.1 to 68.4 per cent.

The recent revision of the national accounts

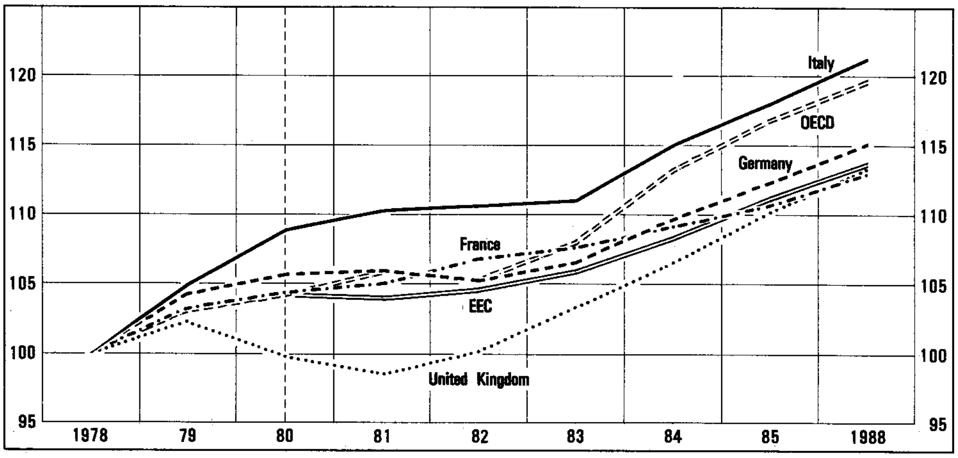
Though not yet complete, Istat's revision of the national accounts has resulted in Italy's GDP being revalued in both nominal and real terms by about 17 per cent on average between 1980 and 1985.

On the sources side, the changes affected every sector. At constant prices the value added of services was revalued by more than 30 per cent. In turn, the figures for the various branches of industry were increased by between 12 and 16 per cent, while the revaluation of agricultural value added was only about 4 per cent. On the uses side, both consumption and investment were increased at constant prices, the former by about 14 per cent and the latter by more than 38 per cent. The revision only resulted in moderate changes in the flows of exports and imports, though this did have a significant effect on their annual rates of change.

Figure 3

GDP IN SELECTED INDUSTRIAL COUNTRIES

(indices based on 1980 prices; 1978 = 100)



Sources: Istat and OECD.

The new national accounts data clearly called for a review of the major developments in the Italian economy since the second oil shock. In this new reading, the early eighties can be seen as a period basically marked by stagnation, though GDP income did continue to expand slowly. The cyclical pattern of the first part of the decade thus remains very much the same, but the underlying trend becomes slightly more expansionary. The revision has, of course, modified Italy's position in relation to other countries. In particular, Figure 3 reveals even more sharply than the old accounts just how big a GDP-growth differential developed in Italy's favour vis-à-vis the OECD and EEC countries between 1979 and 1981, and also that this differential was subsequently maintained. The expansion in plant, machinery and transport equipment investment was stronger in Italy than in any of the other major industrial countries, which were nonetheless also engaged in restructuring their production facilities. On the basis of the new data, Italy's ratio of investment of this type to GDP has been regularly higher than in the other countries since 1980 (Table 2).

Table 2

INVESTMENT IN PLANT, MACHINERY AND TRANSPORT EQUIPMENT, IMPORTS AND THE EXTERNAL CURRENT BALANCE

(as a percentage of GDP)

	1978	1979	1980	1981	1982	1983	1984	1985	1986 (1)
	Investment in plant, machinery and transport equipment *(national accounts data at 1980 prices)*								
Germany	8.0	8.5	8.6	8.2	7.7	8.0	7.7	8.3	8.5
France	8.2	8.3	9.0	8.8	9.0	8.9	8.9	9.4	9.6
United Kingdom	8.3	8.7	8.5	7.7	7.7	7.8	8.4	8.7	8.2
Italy (old series)	7.4	7.8	8.6	8.7	8.3	7.9	8.7	9.3	—
Italy (new series)	—	—	11.5	11.0	10.4	10.0	10.5	10.9	11.0
	Imports *(national accounts data at 1980 prices)*								
Germany	26.4	28.0	28.6	28.3	28.5	28.2	28.9	29.5	29.6
France	20.5	22.1	23.5	23.7	24.8	24.5	25.0	26.0	27.1
United Kingdom	23.5	25.4	25.1	24.8	25.9	26.3	28.1	27.9	28.9
Italy (old series)	24.2	26.3	27.4	25.9	26.5	26.4	28.0	30.0	—
Italy (new series)	—	—	24.0	22.8	22.6	22.1	23.8	24.4	24.9
	External current balance *(at current prices)*								
Germany	1.4	−0.8	−1.7	−0.7	0.5	0.6	1.1	2.2	3.9
France	0.6	..	−1.4	−1.4	−3.0	−1.7	−0.8	−0.6	−0.1
United Kingdom	0.4	..	1.5	2.3	1.2	0.7	−0.3	0.8	−0.3
Italy (old series)	2.4	1.7	−2.4	−2.3	−1.6	0.2	−0.8	−1.0	—
Italy (new series)	—	—	−2.2	−2.2	−1.5	0.4	−0.6	−0.8	0.7

Sources: Istat, EEC and OECD.
(1) EEC estimates for Germany, France and the United Kingdom.

The pace of reorganization and rationalization in the eighties depended to a considerable extent on the dynamic role that small and medium-sized firms continued to play in Italian industry, as well as reflecting the major restructuring programmes that large firms were able to implement.

As to the change in stocks at constant prices, the revision of the national accounts resulted in this item increasing from 0.9 to 1.4 per cent of GDP.

Despite the strong investment performance and a high ratio of investment to income, the Italian economy's average propensity to import was below those of France, Germany and the United Kingdom (Table 2). This is undoubtedly one of the most important developments revealed by the revision. Specifically, it would appear that the Italian economy has been able to satisfy a large part of the recent strong demand for many types of capital goods.

The new data also modified the patterns of growth in exports and imports. In the early eighties, while income became larger, the volume of imports was regularly smaller. Measured ex post, there was a sizable reduction in the ratio between import and GDP growth rates, which fell to a level below that of any other major European country. In turn, the correlation between Italian exports and world demand became stronger.

Comparison of the old and new national accounts series on the sources side shows that the greater growth in GDP in the period 1980-85 can be attributed to services and manufacturing industry, the two sectors for which the revision produced the largest differences. For the former, the uninterrupted growth of the old series underwent an acceleration, while for the latter the downturn of the early eighties was less pronounced and the subsequent expansion faster.

The important changes made in the compilation of employment statistics, which are now expressed in terms of equivalent units and net of workers on Wage Supplementation, have led to recorded employment expanding at a faster pace. This is due less to higher figures for employee employment than to the rise in self-employment. Between 1980 and 1985 the number of self-employed units expanded from 30.2 to 31.8 per cent of the total, while the old national accounts showed it increasing from 28.1 to 28.9 per cent over the same period.

The rise in employment due to the revision was concentrated almost entirely in the services sector. For industry, the new method of considering workers on Wage Supplementation according to the hours actually worked did not significantly alter the results already obtained using analogous methods. In view of the larger increase recorded in gross industrial product, the improvement in labour productivity in the eighties is considerably enhanced, while unit labour costs rose by about one point less per year than previously estimated.

The increase in the deflator of industrial prices in the eighties is somewhat smaller in the new series, though the difference is less pronounced than that for labour costs. The deflator for the construction industry was also revised downwards, while those of all the other items on the sources side rose more sharply. Overall, there was a small slowdown in the rate of increase of the GDP deflator. On the uses side, this is reflected in slower consumer price inflation (an average difference of — 0.4 points in the annual rate between 1981 and 1985).

The distribution of income in the period 1980-85 changes considerably with the new accounts. The share of the compensation of employees in value added at factor cost for the economy as a whole falls below 50 per cent (48 per cent), a decrease of nearly 10 points compared with earlier estimates. Adding in an estimate of the income from self-employment, the difference remains of the same order: 70 per cent, compared with over 80 per cent. On the other hand, there were no substantial differences as regards the pattern of change in the distribution of income. Comparison of the average values for the period also reveals an increase of about 3 points in the private sector's propensity to save, from 29 to 32 per cent. Preliminary analysis suggests that this was due to the upward revision of the saving of the corporate sector.

The outlook for 1987

The latest forecasts prepared by international organizations agree that growth in world trade in 1987 will not exceed 3 per cent, one point less than both the outturn for last year and the end-1986 forecast for this year. The main implications of this for the Italian economy, which is expected to repeat last year's rise in GDP in view of the strength of domestic demand, concern the risk of Italy getting cyclically further out of step compared with its major trading partners. Such a development would weigh on the external accounts. Last year's surplus on current account could well be seriously eroded, if not wiped out, during the course of the year should the incipient deterioration in real balances revealed by the figures for the first quarter persist.

As well as a very sharp improvement in the energy deficit (down to about half the 8 trillion lire recorded in the first quarter of 1986), the sectoral breakdown of the January-March trade balance in value terms shows a marked worsening of the surpluses in the other sectors, from 2,500 to 600 billion lire. The main determinant of this result appears to have been the decline in exports in volume terms.

Domestic demand may grow in real terms by one point more than GDP, benefiting again from a large increase in both public and private consumption. The latter is likely to continue to reflect the increases in households' real disposable income and financial wealth deriving from the improvement in the terms of trade and labour contract renewals. The prospects for capital formation are less certain. The upturn forecast in the February issue of the Bank of Italy's *Economic Bulletin* and confirmed by company surveys might be undermined in the private sector by the change in the international scenario and in the public sector by cutbacks in programmes that have already been approved. Public finances appear to be on a less satisfactory path than expected owing to a tendency for current expenditure to substitute that on capital account. The rise in the former could make it difficult to achieve the target set for the state sector borrowing requirement. Such an outcome would tend to skew the composition of domestic demand and cause GDP growth to be stimulated primarily by the expansion in consumption.

The rise in employment will continue, but it will again fail to absorb the inflow of new labour. The lira prices of imports are expected to remain virtually unchanged over the year, so that the external contribution to the slowdown in inflation will be weaker and further progress in this direction will increasingly depend on domestic factors.

The twelve-month rate of consumer price inflation turned positive in March (+ 0.6 per cent) and was considerably up on the second half of 1986. Apart from the recovery in the prices of energy products, the increase in those of capital goods was substantial and exceeded that of final consumer goods by more than two points. The slowdown in consumer price inflation has come to a halt, with the February twelve-month rate equal to that of last November. In April the cost-of-living index, based on the expenditure of blue and white-collar households and available with a shorter delay, was up 4.2 per cent on twelve months earlier, compared with 4.3 per cent in December.

DOMESTIC DEMAND

Households' consumption

Households' national consumption rose by 3.8 per cent in real terms and by 10.1 per cent in value. The growth in consumption on the economic territory was smaller, 3.2 per cent at constant prices, owing to a substantial increase in spending abroad by residents and a decline in the number of visitors from the United States.

On the basis of preliminary estimates consistent with the new national accounts, households' disposable income increased by 8.6 per cent in value and by 2.4 per cent in real terms; the propensity to consume thus rose by more than 1 percentage point (Table 3).

Table 3

APPROPRIATION ACCOUNT FOR HOUSEHOLDS

(percentage changes over the preceding year)

	1981	1982	1983	1984	1985	1986
Gross domestic earnings	23.1	15.6	13.9	12.7	12.1	6.6
of which: general government	*32.3*	*16.1*	*14.7*	*12.7*	*10.1*	*7.6*
Net labour income from abroad	9.9	27.2	10.4	10.8	−0.5	3.9
Emigrants' remittances	25.1	21.3	7.5	13.7	13.4	−19.5
Gross income from unincorporated businesses and self-employment, dividends and other capital income	15.9	15.0	15.3	15.2	11.2	13.5
Net interest	50.5	47.8	8.3	13.6	4.3	−3.9
Social security benefits	33.2	23.3	32.5	10.0	15.3	9.8
Employees' social security contributions (—)	22.5	29.5	22.5	11.5	8.9	11.2
Self-employed workers' social security contributions (—)	13.2	64,0	16.2	14.2	11.2	16.6
Direct taxation (—) (1)	35.9	23.9	22.8	13.8	14.1	9.7
Gross disposable income (2) (3)	**21.2**	**16.4**	**16.4**	**13.7**	**12.0**	**8.6**
at 1980 prices (4)	2.8	0.5	1.3	2.1	2.4	2.4
Households' national consumption	**19.7**	**17.1**	**15.1**	**14.1**	**12.4**	**10.1**
at 1980 prices	1.5	1.0	0.2	2.4	2.8	3.8

Sources: Istat and preliminary estimates by the Bank of Italy.

(1) Including the surtax on rental income. — (2) Including payments in connection with the condonation of tax and building offences. — (3) For the calculation of disposable income, the definition of the size and legal form of enterprises included in the household sector is that used in the old national accounts. — (4) Adjusted using the implicit price deflator of households' national consumption.

The temporary non-availability of sectoral Istat data consistent with the revised national accounts means that the estimates of households' disposable income are less accurate than usual. According to provisional calculations based on the new data, disposable income increased at a real average annual rate of 1.8 per cent between 1980 and 1985, as against a rate of 0.9 per cent indicated by the unrevised data. The rate of growth in national consumption at 1980 prices now also works out much higher; between 1980 and 1985 it grew at an average annual rate of 1.6 per cent, as opposed to that of 0.9 per cent indicated by the old accounts. Not only were the rates of growth in the first two years higher, but the expansion continued in 1983, in contrast to earlier findings.

The adjustment in the rate of growth in disposable income was thus larger than that in consumption; the cumulative disparity between the two variables widened until 1983 but was gradually eliminated thereafter.

The accentuation of the rising trend in the propensity to consume in 1986 at the same time as an increase of 5.9 per cent in purchases of durable goods stemmed from improved expectations about real incomes and continuing increases in households' real wealth.

The growth in disposable income was held back by households' payments in connection with the condonation of building offences. Net of this item, which it would not be appropriate to treat as current expenditure, the increase in disposable income came to around 9 per cent, or 3 per cent in real terms, thus reducing the increase in the propensity to consume by around one half.

Income from unincorporated business and from self-employment made the largest contribution to the expansion in disposable income. On the other hand, the increase in gross wages and salaries was small (6.6 per cent), representing an increase of less than 6 per cent in per capita earnings net of employees' social security contributions. The growth in disposable income was also curbed by the rise in direct taxation on households, despite the effect of the reductions in personal income tax.

Investment

Gross fixed investment increased again last year after remaining static in the second half of 1985. The average annual rate of increase was nevertheless lower than in the preceding year (1.2 per cent compared with 3.3 per cent), but the very heavy restocking suggested by the national accounts moderated the slowdown in the rate of growth of total investment, which rose by 3.5 per cent, compared with 3.8 per cent in 1985.

The slowdown in capital formation occurred in the components that had provided the greatest boost to investment in 1985. The rate of growth in investment in machinery, equipment and transport equipment fell from 7.4 to 3.1 per cent; investment in machinery and equipment continued to increase at a brisk pace (4.7 per cent) but there was a contraction in industrial vehicles and aircraft (— 3.3 per cent for transport equipment as a whole). Fixed capital investment by the public sector (including state-controlled companies) remained static overall, but there was a shift in emphasis towards the industrial sector; private sector companies halved the rate of growth of their investment in industrial sectors and market services and reduced investment in agriculture.

In order to evaluate these results it is necessary to examine the profound changes resulting from the introduction of the new national accounts. These relate both to the level of investment by type of good and by investing sector in 1982, which Istat chose as the reference point since most of the new data were available for that year, and to the rate of capital accumulation over the six years from 1980 to 1985.

The adjustment in the figures for 1982 causes radical changes in the composition by type of capital good (Table 4). On the basis of more detailed information on the intermediate and final uses of products, it has been estimated that the volume of tools and metal furniture purchased by the Italian economy in 1982 had been around nine times higher than previously estimated (1.3 per cent of GDP, as against 0.2 per cent).

The adjustment in the figures for non-residential premises was much smaller than that for machinery and equipment, accentuating the already substantial disparity between these two components of investment. The finding of the 1981 Census that the housing stock was well above the figure consistent with estimates of housing investment during the seventies necessitated a very large adjustment in the figures on expenditure on residential property. The scale of the revaluation, 44 per cent for 1982, has been determined on the basis of the new survey of building licences, the special survey of extraordinary maintenance (estimated at around 30 per cent of housing investment) and an estimate of unauthorized building (around 5 per cent of housing investment).

The overall effect of changing the composition of investment by type of good owing to the change in the reference year, rebasing the national accounts series at 1980 prices and adjusting the growth in each component is to reduce the rate of increase in fixed investment between 1980 and 1985. The old national accounts had indicated that investment in 1985 was higher than the cyclical peak of 1980, but now it has been shown that it was 2.2 per cent lower than that level and it did not reach the 1980 figure last year either (Table 4).

Table 4

GROSS FIXED INVESTMENT BY TYPE OF CAPITAL GOOD AND INVESTING SECTOR: OLD AND NEW NATIONAL ACCOUNTS

(percentages)

	Revision of the level for 1982 (at 1980 prices)			Revision of the rate of growth (2) (indices at constant prices; 1980 = 100)		
	Investment	Investment/net product (1)		1985		1986
	New NA / Old NA	Old NA	New NA	Old NA	New NA	New NA
	by type of capital good					
Machinery, equipment and other goods	177.8	5.5	8.3	110.3	101.4	106.2
of which: industrial and agricultural machinery	*174.6*	*2.4*	*3.5*	*72.5*	*84.9*	*87.1*
data processing machinery (3)	*112.0*	*1.0*	*0.9*	*231.9*	*177.0*	*189.5*
tools and metal furniture	*1,045.1*	*0.2*	*1.3*	*74.8*	*108.3*	*112.5*
Transport equipment	106.0	2.6	2.3	109.5	111.1	107.4
Construction	125.1	11.2	11.8	93.4	92.9	92.3
of which: dwellings	*144.2*	*5.2*	*6.4*	*92.4*	*96.8*	*94.9*
non-residential premises etc. (4)	*108.2*	*6.0*	*5.4*	*94.2*	*88.5*	*89.3*
Total	**137.5**	**19.5**	**22.4**	**101.4**	**97.8**	**99.0**
	by investing sector					
Agriculture	186.4	19.5 (6)	34.0 (6)	80.3	88.5	86.8
Industry	159.6	13.1 (6)	18.7 (6)	91.2	105.8	109.4
Market services (5)	114.8	16.7 (6)	14.3 (6)	121.6	93.5	96.3
Non-market services	92.5	14.6 (6)	12.7 (6)	104.3	95.1	95.8

Source: Based on Istat data.
(1) Investment by type of good is shown in relation to the net product of the economy as a whole (at factor cost); see also footnote 6. — (2) Indices have been calculated for the old and new national accounts at 1970 and 1980 prices respectively. — (3) Office and data processing machines and precision instruments. — (4) Non-residential premises and "civil engineering" (formerly "public works"). — (5) Net of investment in dwellings attributed to "renting of buildings". — (6) Investment by investing sector is shown in relation to the value added of the sector in question (at factor cost).

In the revised accounts 1985 expenditure on machinery and equipment remains above the 1980 level, but only by 1.4 per cent. The growth in demand for computers and precision instruments has been scaled down but remains well above that for other capital goods, whereas the decline in investment in agricultural and industrial machinery was less marked than had been indicated in the old national accounts (Table 4). This therefore confirms the direction, though not the scale, of the previously indicated shift of investment towards data processing equipment and machines for controlling production and away from more conventional machinery.

In 1986 the slowdown in investment in market services from a real rate of growth of 10.1 per cent to one of 3.0 per cent was due to a further decline in investment by the public sector and a slower expansion in private sector investment (Table 5).

In the public sector, the plans to introduce new technology and modernize and expand market services were not matched by a corresponding increase in expenditure. There was a marked fall in capital spending by municipal transport companies, while investment in the communications sector remained broadly unchanged in money terms. In the private sector the rate of growth in fixed capital formation by transport and communications companies remained very high (14.8 per cent), but there was a decrease of about two-thirds in the rate of growth of investment in commercial activities and other services. This may have been due in part to the slower growth in the sector's output (3.3 per cent, compared with 5.4 per cent in 1985), while the substantial increase of about 3.5 percentage points in gross profits as a proportion of value added appears to have had no effect on real capital accumulation.

The smallness of the overall increase in gross fixed investment was due in part to a further decline of 2.0 per cent in expenditure on housing, which accounts for more than one-quarter of capital formation after the revision of the national accounts by Istat. The contraction in such investment by the private sector was less than that recorded in 1985, but there was a further reduction in expenditure on housing by the public sector.

The restructuring and development of industrial enterprises

The economic and financial situation of industrial enterprises at the beginning of the second half of the eighties is broadly satisfactory, although some sectors are still having difficulty returning to profitability and their prospects for growth continue to be uncertain. The marked improvement in profits and the strengthening of companies' balance sheets, which was helped by the change in the terms of trade in 1986, are the result of an adjustment that has been under way for several years.

Table 5

PUBLIC AND PRIVATE GROSS FIXED INVESTMENT BY INVESTING SECTOR

(at 1980 prices)

	Billions of lire	Share of total %	Percentage changes					
	1986	1986	1981/1980	1982/1981	1983/1982	1984/1983	1985/1984	1986/1985
Agriculture, forestry and fisheries	7,345	7.8	−5.4	−2.4	3.9	−1.2	−6.6	−2.0
Private	*6,451*	*6.9*	*−4.7*	*−6.9*	*10.8*	*−12.3*	*1.8*	*−3.8*
Public (1)	*894*	*0.9*	*−11.8*	*42.5*	*−41.2*	*134.1*	*−45.2*	*13.7*
Industry	31,130	33.2	−0.1	−7.0	1.1	8.3	3.9	3.5
Private	*24,418*	*26.0*	*−1.2*	*−7.9*	*−0.4*	*10.6*	*3.4*	*1.8*
Public (2)	*6,712*	*7.2*	*4.9*	*−3.0*	*7.3*	..	*6.0*	*10.1*
Market services (3)	23,551	25.1	−5.1	−4.6	−10.7	5.1	10.1	3.0
Private	*17,328*	*18.5*	*−6.3*	*−10.4*	*−16.3*	*0.5*	*16.3*	*7.4*
Public (2) (4)	*6,223*	*6.6*	*−0.5*	*17.6*	*5.9*	*15.7*	*−2.4*	*−7.7*
of which:								
Transport and communications	9,942	10.6	4.4	−7.7	−2.8	10.7	4.0	−0.8
Private	*3,912*	*4.2*	*10.0*	*−31.6*	*−15.5*	*−1.2*	*18.9*	*14.8*
Public	*6,030*	*6.4*	*−1.1*	*17.9*	*5.1*	*16.6*	*2.3*	*−8.8*
Distributive trades, credit and other services	13,609	14.5	−11.0	−2.3	−16.0	0.7	15.3	5.9
Private	*13,416*	*14.3*	*−11.2*	*−2.4*	*−16.5*	*0.9*	*15.6*	*5.5*
Public (4)	*193*	*0.2*	*30.5*	*4.7*	*43.8*	*−15.5*	*−7.4*	*53.2*
Dwellings	24,859	26.5	−0.1	−5.0	3.9	0.6	−2.4	−2.0
Private	*23,880*	*25.5*	*−0.4*	*−5.4*	*5.0*	*−1.4*	*−1.6*	*−1.0*
Public (5)	*979*	*1.0*	*5.6*	*3.1*	*−16.9*	*51.5*	*−16.8*	*−20.5*
Non-market services	6,911	7.4	−5.7	−11.3	−9.6	9.2	15.2	0.8
Total economy	93,796	100.0	−2.3	−5.7	−1.6	4.4	3.3	1.2
Private	*72,077*	*76.8*	*−2.6*	*−7.6*	*−1.3*	*1.5*	*4.1*	*1.6*
Public	*21,719*	*23.2*	*−1.1*	*1.3*	*−2.5*	*14.7*	*0.9*	..

Source: Based on Istat data (new national accounts).

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

Two processes are involved here; first the almost continuous development of small and medium-sized firms, bringing with it a steady growth in output and employment, and secondly economic and financial restructuring, characterized by modest growth in large companies; the latter process grew more pronounced in the eighties against the background of non-accommodating monetary and exchange rate policies and substantial state transfer payments.

The expansion in small and medium-sized industrial firms, which had begun in the mid-seventies and derived partly from the decentralization of production by major companies, accelerated between 1978 and 1980 in response to a marked increase in demand. According to Istat data, companies with between 20 and 99 employees rapidly increased their investment and their value added (by 6.2 per cent a year), thus confirming that the expansion entailed capital widening, as well as increasing their market share (Table 6); the higher productivity generated by the virtuous circle of growth enabled them to raise per capita labour incomes by more than large companies.

Table 6

INVESTMENT, LABOUR AND VALUE ADDED IN INDUSTRIAL ENTERPRISES, BY SIZE

(percentages)

	Small and medium-sized (20-99 employees)			Large (more than 200 employees)			
	1974-77	1978-80	1981-84	1974-77	1978-80	1981-84	1985-86
Investment							
index (1980 = 100) (1)	84.4	87.5	103.6	118.9	98.8	93.6	104.2
ratio to value added	14.7	12.9	12.9	16.4	12.9	11.8	....
Value added							
rate of growth	3.5	6.2	5.0	1.2	2.3	1.6	....
percentage of total (2)	21.7	23.4	25.6	67.1	64.4	59.9	....
Hours worked							
rate of growth (3)	....	....	....	−1.2	−1.2	−6.6	−3.0
Employment (4)							
rate of growth (5)	0.3	0.6	1.5	−0.4	−1.2	−5.2	−5.3
percentage of total (2)	26.4	27.6	30.6	61.6	60.3	56.3	....
Hours of absence from work (6)							
percentage of contractual working hour	9.7	8.0	8.1	14.8	14.5	9.5	....

Source: Based on Istat survey of gross product and Confindustria data.

(1) The figure for large enterprises in 1985-86 relates to the growth in investment in enterprises with more than 500 employees (Bank of Italy survey). — (2) Percentage of total for enterprises with more than 20 employees. — (3) The figures for large enterprises relate to firms with more than 500 employees. — (4) Including workers receiving wage supplementation. — (5) The figure for large enterprises in 1985-86 relates to the growth in employment in firms with more than 500 employees. — (6) Hours of absence on account of illness, short-term leave, maternity leave, accidents and strikes. in the case of small and medium-sized enterprises, the figures relate to firms with up to 50 employees.

These trends, which were evident in all sectors, continued during the four years from 1981 to 1984, despite the new stance of monetary and exchange rate policy. The growth in capital formation by firms with between 20 and 99 employees was such as to maintain the ratio between investment and output at a level above that for large companies (12.9 per cent, compared with 11.8 per cent). Their market share in terms of value added increased further, reaching 25.6 per cent on average over the period, compared with 23.4 per cent between 1978 and 1980; the growth in employment accelerated, offsetting part of the very large contraction recorded by medium-sized and large companies (Table 6). Their gross profit margin equaled the 1980 peak, reaching 38.3 per cent in 1984. The development of small and medium-sized enterprises appears to have been helped partly by the fact that the number of new entrants has exceeded the number of firms leaving the market.

The measures to strengthen the organizational and manufacturing structure of small and medium-sized firms do not appear to have been accompanied by a comparable modernization of their financial management.

The rapid growth in output and the limited range of alternative ways of raising external finance have led to an increase in borrowing from the banking system, especially at short term. On the basis of data on manufacturing companies with fewer than 100 employees polled by the Company Accounts Clearing House, the ratio of debt to value added rose from 67 to 75 per cent between 1982 and 1985. Moreover, small and medium-sized firms benefited less than major companies from the heightening of competition among banks following the expiry of the credit ceiling in 1983. Accordingly, the fall in interest charges contributed much less to the improvement in small firms' profitability than the average for the economy as a whole, decreasing by only three percentage points in relation to value added over the four years from 1982 to 1985. The higher proportion of bad debts in industries where the majority of small companies are to be found also reflects the high failure rate among smaller firms.

Small and medium-sized firms appear to have used only a small part of their internal and borrowed funds remaining after capital investment to purchase securities and participations, preferring to employ their financial resources to boost their marketing efforts. Net trade credit, expressed as a proportion of value added, rose from 7.6 per cent in 1982 to 12 per cent in 1985.

Unlike that of small and medium-sized industrial firms, the performance of large companies differed over time. In the mid-seventies, when there was a marked downturn in investment, companies with more than 200 employees increased their output at a modest rate of 1.2 per cent a year and labour productivity by 1.7 per cent a year, whereas gross profit margins fluctuated around the very low levels to which they had fallen at the beginning of the decade (Table 7). The gap between internal funds and financial requirements was covered by borrowing, particularly among larger companies; according to data from Mediobanca, such firms financed 47 per cent of their gross fixed investment from their own resources between 1976 and 1978, whereas in other companies internal funds exceeded capital expenditure by 20 per cent.

Table 7

PRODUCTIVITY, LABOUR COSTS AND PROFITS IN INDUSTRIAL ENTERPRISES, BY SIZE

(annual average rates of growth) (1)

	Small and medium-sized (20-100 employees)			Large (more than 200 employees)		
	1974-77	1978-80	1981-84	1974-77	1978-80	1981-84
Labour productivity (2)	3.2	5.6	3.4	1.7	3.6	7.2
Labour income per employee (3)						
nominal	25.6	19.3	16.9	21.3	16.5	15.9
real (4)	6.9	2.8	1.8	3.0	0.4	0.5
Unit labour costs (5)						
nominal	21.7	13.0	13.1	18.9	12.3	7.7
Implicit value added deflator (6)	19.9	15.9	13.8	18.9	13.5	10.7
Profits						
real value (7)	−1.0	10.8	6.2	1.4	2.5	5.5
percentage of value added *(average percentage value)*	32.1	34.0	36.8	24.5	25.6	30.2

Source: Based on Istat survey of gross product and Confindustria data.
(1) Compound growth rates. — (2) Value added per employee at 1980 prices. — (3) Labour income equals wages and salaries *plus* employers' social security contributions *plus* appropriations for redundancy payments, pensions, etc. — (4) Deflated using the general retail price index. — (5) Labour costs per unit of output, expressed as a ratio between labour income and value added at 1980 prices. — (6) Calculated from the national account deflators of value added. — (7) Adjusted using the implicit price deflator of gross fixed investment.

Large companies began to modernize their plant between 1978 and 1980. The slowdown in the growth of real labour incomes, owing partly to the new measures to reduce employers' social security contributions, created room for an increase in operating profits (Table 7). After 1980, the stance of monetary and exchange rate policy permitted neither the effective advance repayment of debt as a result of negative real interest rates nor increases in competitiveness by means of devaluation. There was therefore a growing incentive for companies to give priority to reducing unit costs by reorganizing the main factors of production.

Fixed capital formation remained unchanged in volume over the period under review, but its composition shifted even more clearly towards technologically advanced products for modernizing plant.

Recourse to the Wage Supplementation Fund encouraged labour saving, first in the motor industry and then in the industrial sector as a whole; in the case of major companies this took the form of a reduction of 6.6 per cent a year in the number of hours worked between 1980 and 1984; the trend continued in 1985 and 1986, though at the slower rate of 3.0 per cent. At the same time there was an intensification in the use of labour, as shown by the increase in per capita working hours and a reduction in hours lost through absences from 14.5 per cent of contractual working hours between 1978 and 1980 to 9.5 per cent between 1981 and 1984.

The changes in the organization of capital and labour raised productivity; despite the very small increase of 1.6 per cent in value added, the output per worker of companies with more than 200 employees increased at an annual average rate of 7.2 per cent (Table 7). In the space of three years gross operating profits thus rose by about 8 percentage points as a proportion of value added, from 26.8 per cent in 1980 to 34.4 per cent in 1984.

The restructuring of production by major enterprises was accompanied by equally far-reaching financial restructuring in the eighties. On the basis of information on companies gathered by the Company Accounts Clearing House, the ratio of borrowing to value added fell from 104 per cent in 1981 to 88 per cent in 1985, a decline of 16 percentage points. The decrease was much more pronounced in the case of public sector companies, which began from a level more than twice that for private sector firms. The ratio of gross interest charges to value added fell from 25 to 19 per cent over the five-year period; in the case of large companies this was due partly to the reduction in their outstanding debt (Table 8).

The strengthening of the capital base of major companies and the substantial volume of self-financing were not sufficient to generate a larger direct expansion in capacity. Since demand growth was expected to be modest, resources were invested increasingly in government securities and shareholdings. The overall increase in financial investments together with the growth in operating income helped increase profitability. Interest income more than doubled as a proportion of value added, rising from 3.5 per cent in 1981 to 7.7 per cent in 1985, causing net interest charges to fall from 21 to 11 per cent of value added (Table 8).

Table 8

SIGNIFICANT RATIOS AND FLOW OF FUNDS OF LARGE ENTERPRISES (1)

	1981	1982	1983	1984	1985
			(percentage of value added)		
All enterprises					
Financial debt	103.8	96.7	95.3	94.9	88.0
Gross interest charges	24.6	24.7	23.9	22.9	19.2
Financial income	3.5	5.0	6.6	7.8	7.7
Net interest charges	21.1	19.7	17.3	13.1	11.5
Net trade credit	2.0	0.5	−0.3	−11.4	−10.4
Private enterprises					
Financial debt	69.8	68.0	68.5	70.0	66.2
Gross interest charges	19.2	18.2	17.0	16.2	14.7
Financial income	3.7	4.2	6.7	7.3	8.5
Net interest charges	15.5	14.0	10.3	8.9	6.2
Net trade credit	12.5	7.1	8.0	8.6	5.2
			Flow of funds (percentage of total)		
All enterprises					
Sources					
Self-financing	52.1	58.4	60.7	66.5	76.5
Capital raising	17.3	19.6	21.2	16.4	20.6
Borrowing from banks	29.5	18.6	17.0	17.4	2.9
Bonds	1.1	3.4	1.1	−0.3	. .
Uses					
Fixed investment	52.2	61.7	59.4	53.7	63.7
Stocks	10.7	8.4	2.3	13.1	11.9
Financial assets (2)	20.2	21.8	21.6	20.3	17.0
Net trade credit	9.9	4.5	0.8	16.5	−0.1
Other (3)	7.0	3.6	15.9	−3.6	7.5
Private enterprises					
Sources					
Self-financing	59.7	70.8	71.9	72.9	85.9
Capital raising	14.7	9.9	6.4	8.9	8.7
Borrowing from banks	22.1	15.4	19.5	18.2	3.9
Bonds	3.5	3.9	2.2	..	1.5
Uses					
Fixed investment	39.8	48.2	39.4	35.3	46.3
Stocks	11.2	10.5	. .	14.8	10.2
Financial assets (2)	20.9	29.6	35.8	29.2	18.3
Net trade credit	14.1	−2.6	5.4	5.3	−1.0
Other (3)	14.0	14.3	19.4	15.4	26.2

Source: Based on data from the Company Accounts Clearing House.
(1) Closed sample of enterprises with a turnover of more than 100 billion lire or 1,000 employees in 1980. — (2) Comprise cash, bank deposits, securities and participations. — (3) Comprises dividends and the change in other assets and liabilities.

Purchases of shareholdings appear to reflect a strategy of expansion by acquisition. Investment abroad has accentuated this trend, especially in the case of large private sector companies. Despite the fact that Italian firms still tend to prefer to export rather than establish subsidiaries abroad, Italy has become a net exporter of capital for productive investment.

Industrial investment: 1986 results and forecasts for 1987

The Bank of Italy's regular sample survey of manufacturing firms with at least 20 employees shows that the substantial investment programmes drawn up for 1986 were largely achieved (99.2 per cent), giving rise to an increase in expenditure of 9.6 per cent at constant prices over 1985. Despite the reappearance of the traditional tendency for large companies to overestimate their investment plans, the expansion in investment occurred mainly among enterprises with 500 employees or more; companies in this category nevertheless recorded a further contraction in employment, unlike smaller firms.

The appreciable improvement in gross operating profits and the acceleration in the growth in output, which firms believe was responsible for an increase of more than one percentage point in the effective capacity utilization rate, both helped companies achieve the expenditure planned at the end of 1985.

Corporate expenditure plans for 1987 indicate a renewed acceleration in investment, except in some basic industries. The decisions taken at the end of 1986 were undoubtedly influenced by the cyclical factors indicated above and were based on more optimistic expectations than those formed in more recent months, especially regarding the prospects for growth in the world economy. Although available data on investment in machinery and transport equipment in the economy as a whole in the first quarter of the current year are consistent with the survey's indications of rapid growth, it is possible that companies' investment plans will be scaled down as the year proceeds.

DOMESTIC SUPPLY

Agriculture

The outcome for 1986. — After two successive years of poor results, agricultural production recorded an upturn in 1986. Output increased by 1.6 per cent in real terms, though this did not make good all the shortfall compared with 1983. The 1986 crop year was also marked by considerable reductions in production costs and by further decreases in both employment and investment.

The increase in agricultural production was coupled with little or no change in the sector's trade balance, which was influenced by a number of temporary factors.

Compared with previous years, agricultural producer prices recorded a much smaller increase (1.9 per cent). At a time of falling inflation, this result reflected the high level of stocks and the persistence of competitively priced imports. It was considerably offset, however, by the sharp fall in the prices of the goods and services acquired by farmers (— 3.2 per cent). The rise in agricultural incomes was nonetheless significantly smaller than in the other sectors of the economy.

As regards employment, another 24,000 equivalent full-time units, or 0.9 per cent of the total, left the agricultural sector. The exodus mainly involved employee workers and the Southern regions. Investment declined by 2 per cent to run at the lowest level since the beginning of the eighties.

Italian medium-term policy for agriculture. — The recent approval of Law 752/1986 governing expenditure connected with the five-year plan for agriculture (1986-90) offers an occasion for some considerations on the structural differences between agriculture in Italy and the other EEC countries and on the guidelines embodied in national policy in this area.

In 1985 Italy accounted for 17.4 per cent of the utilized agricultural area in the Community, 30 per cent of the employment and 43.4 per cent of the total number of farms. By contrast it accounted for something less than 20 per cent of Community production and ranked second to France in importance. In terms of value added, Italy's share rises to 24 per cent, in view of the lower incidence of intermediate consumption (Table 9). The divergence between both the structural conditions and the level and composition of gross market production in Italy and the rest of the Community is reflected in the the sector's trade deficit, which, in relation to GDP, is one of the largest in the Community.

Table 9

THE STRUCTURE OF AGRICULTURE IN THE MAIN EEC COUNTRIES IN 1985

	Italy	Germany	UK	France	Netherlands	EEC-10
	percentage composition					
Utilized agricultural area	17.4	11.9	18.5	31.0	2.0	100.0
Employment	30.1	18.2	8.1	20.7	3.3	100.0
Number of farms (1)	43.4	11.8	4.0	17.3	2.1	100.0
Gross market production (2)	19.4	18.1	12.7	26.5	8.6	100.0
Gross value added (at market prices) (2)	24.3	15.4	10.9	26.7	7.4	100.0
	in relation to the EEC average					
Gross market production per worker (2)	64.6	99.4	156.3	127.9	262.7	100.0
Gross market production per hectare (2)	111.9	151.9	68.6	85.3	428.9	100.0

Source: EEC, *The Agriculture Situation in the Community, 1986.*
(1) 1983 figures, except for Italy (1982). — (2) Calculated at constant prices using the method adopted by the EEC.

The revised national accounts show that the final output of Italian agriculture expanded at an average annual rate of 0.6 per cent between 1980 and 1986. This much slower rate of growth compared with the seventies was due not only to bad weather in several years but also to the weakness of international markets and the decline in relative prices. Though marked by widely differing patterns in the various member countries, agricultural production in the Community as a whole increased at an average annual rate of 1.3 per cent.

The slowdown in the growth of agricultural production during the eighties, with food consumption increasing more slowly than in the past, but nonetheless faster than in the other industrial countries, has resulted in the food and agricultural deficit remaining unchanged in real terms until 1984 and then expanding considerably. The root causes of the deficit appear to lie in the institutional and geographical difficulties that have prevented domestic farming from satisfying a larger share of the demand for certain products (in particular, meat and milk products). Equally important is the failure to achieve greater penetration of export markets with the products for which Italy has a relative advantage (typically, Mediterranean products), when conditions were much more propitious. Developments in the Community and in the rest of the world suggest that substantial changes will have to be made in Italian agriculture just to avoid a further deterioration in the situation. The priority areas for structural intervention include farm size, the factors fostering higher productivity and the area under irrigation.

Public intervention could accelerate this process and simultaneously improve working conditions in agriculture, a step that is indispensable if the younger generations are to enter the industry on a sufficient scale. The gap that has opened up between agriculture in Italy and the rest of the Community is considerable. Italy is the only country in which the average size of farms has remained virtually unchanged over the last fifteen years — it is now half the figure for Germany, the Netherlands and Belgium and less than one third of that for France, Denmark and Ireland. On the other hand, large-scale irrigation projects that were put in hand at the beginning of the eighties, for the most part in the South of Italy, are nearing completion. These will increase the amount of irrigated land by about one million hectares or one third of the present total. These measures could benefit Italy's "Mediterranean" agriculture, where EEC production falls short of demand, provided that the infrastructures needed to exploit this land to the full are created and a careful selection of crops made in the light of a comprehensive view of the production and processing sectors.

The national plan for agriculture that was approved in 1985 focuses intervention policy on: the removal of the legislative and institutional obstacles that have accumulated and the rationalization of farm structures (the fostering of mergers and owner farming); the promotion of innovation in production systems (mechanization and genetic improvement, etc.); and the improvement of relationships with markets. Law 752 of 8 November 1986 provides the necessary financial support for the plan with the appropriation of 16.5 trillion lire, more than one third of which can be spent in the two years 1986-87.

Industry

Results in 1986 and prospects for 1987. — Industrial value added rose by 2.7 per cent to exceed the previous peak recorded at the turning point of the last cycle in 1980. This overall result reflected the contrasting performances of industry excluding construction, which expanded strongly by 3.4 per cent, and construction, which contracted slightly by 0.2 per cent (Table 10).

Table 10

INDUSTRIAL VALUE ADDED AT MARKET PRICES

	Values at 1980 prices (billions of lire)			% composition 1986	% changes		
	1984	1985	1986		1984/83	1985/84	1986/85
VALUE ADDED:							
including construction	150,996	152,959	157,149	100.0	3.1	1.3	2.7
excluding construction	124,168	126,044	130,293	82.9	3.7	1.5	3.4
Goods:							
manufactured goods	110,249	111,930	115,613	73.6	4.2	1.5	3.3
energy products	13,919	14,114	14,680	9.3	0.3	1.4	4.0
Construction and public works	26,828	26,915	26,856	17.1	0.3	0.3	−0.2

Source: Istat.

The index of industrial production, which excludes building, also showed a sharp rise (2.7 per cent), though smaller than that in value added.

The acceleration of the recovery in 1986 can be attributed primarily to domestic demand and in particular to households' consumption, while foreign demand made a smaller contribution, owing both to the slow growth in world trade and to the decline in Italy's competitiveness during the year.

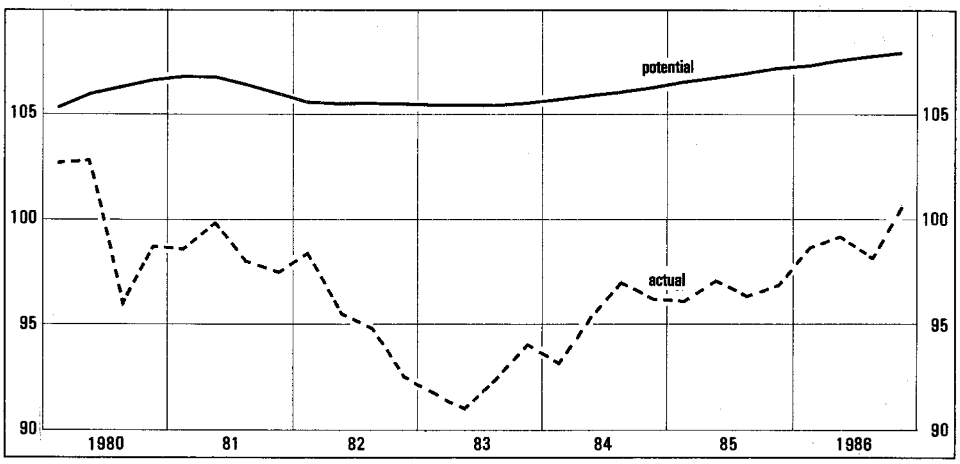
The upturn in industrial activity was reflected in a higher level of plant capacity utilization compared with the previous year, even though potential output began to rise again moderately after the downturn recorded in 1981-83. The pattern of capacity utilization over the year paralleled that of production, rising to a peak in the third quarter. Last year's values were nonetheless below the peaks recorded at the top of the previous cycle in the first quarter of 1980 (Figure 4).

In the first quarter of 1987 the index of industrial production maintained the level reached at the end of the previous year. Estimates based on electricity consumption indicate that performance remained on this plateau in April, even though business opinion surveys continued to indicate favourable prospects, with demand rising and stocks of finished products only slightly above their normal level.

Figure 4

ACTUAL AND POTENTIAL OUTPUT IN INDUSTRY EXCLUDING CONSTRUCTION

(indices, average actual output in 1980 = 100)



Sources: Istat and Bank of Italy.

The revision of the national accounts. — Istat's recent revision of the national accounts for the 1980s results in the industrial performance revealed by cyclical indicators being somewhat modified. In the first place, the new figures reduce the extent of the downturn in productive activity recorded in 1982-83 by the index of industrial production. This fell by 8 per cent between 1980 and 1983, while the value added figures of the new national accounts indicate a fall of only 3.4 per cent.

The revision has also made substantial changes in the picture of the structure of industry. The most striking is that in the engineering industry's average share of total production, which rose by no less than six points from 22.7 to 28.5 per cent. When the production of transport equipment is included, the proportion rises to over 35 per cent. By contrast, the importance of the chemical industry is reduced (from 11.6 to 8.2 per cent), as is that of the food industry (from 10.9 to 8.8 per cent); for the other branches, the revision only involved minor changes. The overall effect of the revision thus appears to be an increase in the role of the branches producing capital goods at the expense of those producing consumer and intermediate goods.

Services

The value added of market services rose by 3.2 per cent, which was significantly less than in the previous year (4.9 per cent) but nonetheless still a much larger increase than that recorded by manufacturing (2.6 per cent; Table 11). The share of market services in gross domestic product has risen steadily during the eighties and reached 47.3 per cent last year. When non-market services are also considered, the services sector as a whole accounted for 59.2 per cent of GDP.

Table 11

VALUE ADDED OF MARKET SERVICES AT MARKET PRICES

	Values at 1980 prices (billions of lire)			% composition 1986	% changes		
	1984	1985	1986		1984/83	1985/84	1986/85
Wholesale and retail trade	66,910	69,921	72,019	36.1	6.2	4.5	3.0
Lodging and catering	11,515	11,798	11,932	6.0	3.0	2.5	1.1
Transport	16,139	16,529	17,151	8.6	0.1	2.4	3.8
Communications	4,725	5,085	5,292	2.6	5.3	7.6	4.1
Credit and insurance	19,062	20,137	21,523	10.8	1.7	5.6	6.9
Other market services	42,313	45,517	46,808	23.4	9.5	7.6	2.8
Renting of buildings	23,837	24,560	25,005	12.5	1.9	3.0	1.8
Total	**184,501**	**193,547**	**199,730**	**100.0**	**5.1**	**4.9**	**3.2**

Source: Istat.

Excluding the capital intensive services (rail, sea and air transport and communications) and those subject to strict entry controls (credit and insurance), the remaining 75 per cent of market services are based primarily on forms of self-employment and family businesses.

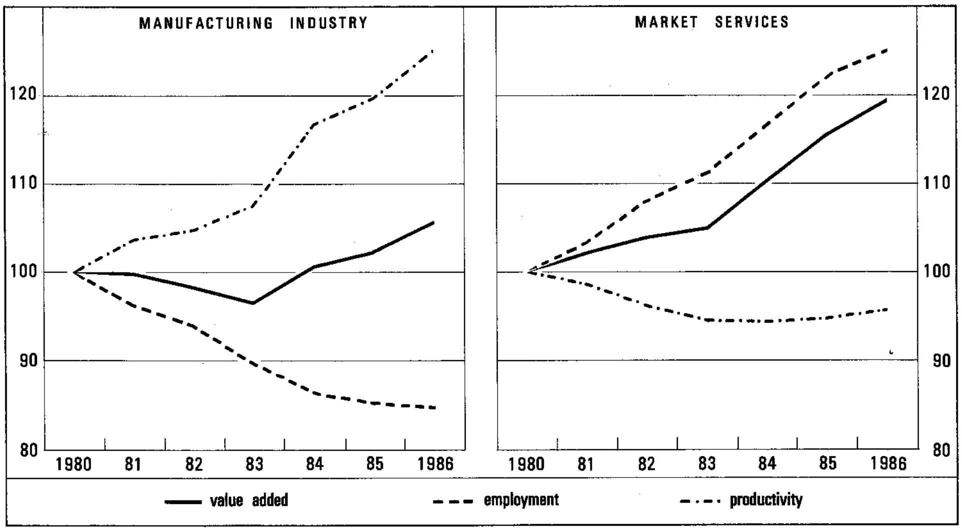
The analyses of jobs made in connection with the revision of the national accounts show how the segmentation of the labour market enables a demand for labour that often has daily and seasonal peaks to be met through a supplementary supply comprising working wives, employees doing second jobs and not requiring the payment of social security contributions, other irregularly employed or temporary workers, and non-resident foreigners.

The growth of the services sector in the Italian economy is in line with developments in the other industrial countries. Nonetheless, there is cause for some concern in the forms this growth has taken, in view of the slow pace of productivity gains and the failure to implement the changes needed to make more efficient use of the new resources. The value added per worker in market services is now actually lower than it was at the beginning of the eighties. The 0.8 per cent average annual decrease is in sharp contrast with the corresponding 3.8 per cent increase in manufacturing industry (Figure 5). The wide gap revealed between the rise in employment and that in productivity is not matched in any of the other major European countries, where employment in market services has remained unchanged (Germany) or expanded slightly (France and the United Kingdom), while value added has risen at average annual rates not dissimilar to Italy's (1.9 per cent in France and 3.2 per cent in the United Kingdom).

Figure 5

VALUE ADDED, EMPLOYMENT AND PRODUCTIVITY IN MANUFACTURING INDUSTRY AND MARKET SERVICES

(indices, 1980 = 100)



Source: Istat.

Some branches, of which telecommunications is an important example, have been exceptions to this rule and have achieved substantial productivity improvements.

The telecommunications industry plays a fundamental role in modern economies, not only in view of its high level of fixed investment but also because of the external economies it can generate by permitting the potential of information technology to be exploited to the full.

Between 1970 and 1986 the number of subscribers to the public telephone service increased at an average annual rate of 7 per cent. The value added of the communications sector (which includes the postal service) rose at an average annual rate of 6 per cent, attributable both to the increases in traffic per subscriber and to the shift in demand to higher quality services (direct-dialled trunk calls, telex and data transmission, etc.). Over the same period telephone charges declined in relation to consumer prices at an average annual rate of just under 5 per cent. This was partly the result of the tariff policy pursued, which also had the effect of causing serious problems in raising the finance needed to implement the operating companies' investment programmes in the second half of the seventies.

The Italian telecommunications system is based on the concessions granted to companies in the STET Group, which is controlled by IRI. The inclusion of the telecommunications industry in this part of the system of state shareholdings permits a high degree of vertical integration not only between the suppliers of telecommunications apparatus and services but also with the domestic semiconductor industry.

Table 12

FORECAST GROWTH OF THE TELECOMMUNICATION SYSTEM

	Spontaneous growth			Growth with incentives		
	1984	1989	1994	1984	1989	1994
Users *(thousands)*						
Telephone service (subscribers)	16,516	20,800	25,000	16,516	21,150	25,550
Telex and teletext service	64	145	260	64	145	260
Data transmission service (no. of modems)	154	290	522	154	290	522
Cable radio	14,200	14,875	15,600	14,200	14,875	15,600
	1985-94			1985-94		
Capital expenditure *(billions of 1983 lire)*						
Exchanges	12,150			14,230		
Transmission systems	18,400			19,630		
Other items	5,070			5,410		
Telex and data	2,100			2,100		
Satellite communications	330			740		
Cable radio	1,650			1,800		
New services	1,400			1,750		
Total	**41,100**			**45,660**		

Source: Ministry of Industry.

The telecommunications industry also makes an important contribution to the demand for high technology investment goods, with purchases running at around 4,000 billion lire per year. The scenarios put forward in government documents show this sector as accounting for a little less than one fifth of all investment in machinery and equipment over the next ten years.

The ten-year plan for telecommunications approved by the Interministerial Committee for Economic Planning at the beginning of August 1985 and the industrial policy for telecommunications approved by the Interministerial Committee for Industrial Policy early in December 1986 respond to the following needs: to exploit new production techniques and network technologies (digital transmission, electronic switching, optical fibre cables and satellites); to optimize the economies of scale offered by the public network; and to reconsider the extent to which the markets for user systems and value added services should be liberalized.

The guidelines for intervention in this sector are designed to promote a reorganization that will eliminate the overlapping of responsibilities and duplication of equipment between the various operating companies, accelerate the spread of both traditional and innovative services and encourage an early modernization of plant. Achievement of these objectives would also help to attenuate the serious employment problems facing the suppliers of apparatus.

Two scenarios for the growth of the public network are shown in Table 12. The first assumes "natural" growth, based primarily on self-financing, the second foresees accelerated growth supported by public finances in a manner still to be decided.

Energy

Results for the year. — The increase in the domestic consumption of primary energy was slightly smaller than in 1985 (1.5 per cent as against 1.9 per cent), despite the increases in economic activity having been the same in the two years (2.7 per cent) and energy prices having collapsed. This pattern was common to the whole of the OECD area. Most of the increase in demand was met by domestic sources, whose share of the total supply rose from 18.7 to 19.6 per cent as a result of an increase in the production of natural gas.

This further reduction in the energy intensity of GDP was due both to the savings deriving from the more temperate weather — which caused a significant reduction in the total energy requirement — and to the cautious reaction to the pronounced fall in the relative prices of energy, part of which was in any case absorbed by increases in the taxes on some products. This factor, together with the strategies of technological innovation pursued by firms looking beyond the short term, fostered further progress in the projects aimed at rationalizing the use of energy.

The rise in the final consumption of energy was primarily attributable to the sharp increase in passenger and goods road traffic. Notwithstanding a reduction in the demand for heating, the consumption for civil purposes also increased moderately, as did that of industry, where the combined effect of the fall in the price of oil relative to that of coal and the continued recovery in production was an increase in the consumption of oil in absolute terms. This was the first such increase since 1978-79 and for the most part can be attributed to the cement industry.

The energy problem in the medium term. — The about-turn in the conditions in the international energy market in 1986 offers an opportunity for a reassessment of Italy's energy problems in the light of developments in the other industrial countries.

Examination of the energy intensity of these contries in the period 1970-85 shows that the ratio of Italy's primary energy requirement to GDP only decreased by 13 per cent, compared with 22 per cent for the United States, 27 per cent for Japan, 32 per cent for the United Kingdom and 19 per cent for Germany.

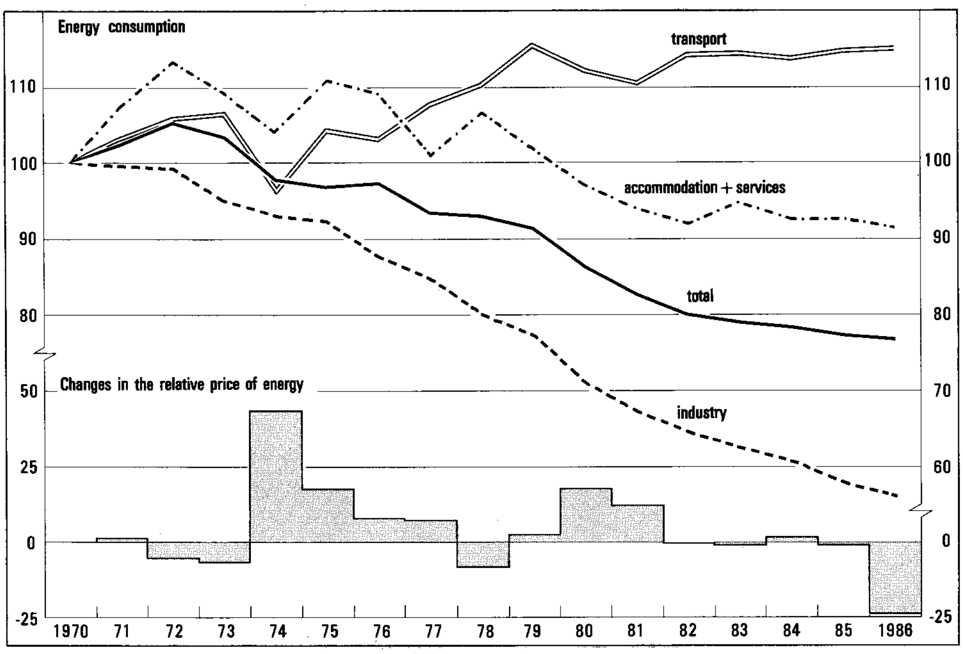
Specific consumption by sector (Figure 6) shows that the best results were achieved by industry (— 4.2 and — 3.6 per cent of consumption per unit of value added respectively in 1980-83 and 1983-86). There was also a decrease in the accommodation and services sector, especially in the early eighties. By contrast, the transport sector achieved no savings at all, with unit consumption only tending to stabilize after the substantial rise recorded in the second half of the seventies.

During the period in question, the share of net imports in the total energy requirement remained almost static at something over 80 per cent. Considerable progress was nonetheless made in diversifying Italy's sources of energy. By contrast, other countries made some progress in replacing external sources with domestic ones. This development was most pronounced in the eighties and reflected the growing use of nuclear energy.

The last thirteen years have shown that aggregate assessment of the energy requirement based exclusively on the ratio of the growth in the demand for energy to that of income may prove insufficient, insofar as it ignores the effects of changes in relative prices, sectoral shifts in the structure of the economy towards less energy intensive services and the scope for energy savings inherent in investment in new generations of capital goods. When the energy requirement and income are examined separately, they are found to have developed differently in several years. Specifically, the energy requirement decreased steadily between 1979 and 1983, falling from 149 to 139 million TOE and then rose again between 1983 and 1986 by nearly 9 million TOE, so that last year's figure was close to that recorded at the end of the seventies. By contrast, GDP recorded average annual growth rates of 1.4 and 3 per cent respectively in the two periods.

Figure 6

SPECIFIC ENERGY CONSUMPTION BY MAJOR SECTOR (1970 = 100) (1) AND CHANGES IN THE RELATIVE PRICE OF ENERGY (2)



Source: Based on Istat data.
(1) Final consumption of energy: for industry, as a ratio to the value added at factor cost of manufacturing industry at constant prices; for the other aggregates, as a ratio to real GDP at market prices. — (2) Changes in the ratio of the index of the output prices of the energy sector gross of taxes to the general price index.

The conclusion that changes in the energy requirement are no longer related to GDP growth is not confirmed, however, by the analysis of two periods in which price developments were similar. The results of this analysis indicate that the large reductions in the energy requirement engendered in the early eighties by the increase in prices associated with the second oil crisis, have given way to a positive correlation between the energy requirement and income growth.

With the usual margins of uncertainty, the projections made for the national energy plan and the national energy conference show the energy requirement continuing to grow through the year 2000. The tendency for the demand for energy to increase materially is also present in low-growth scenarios. The objective of enhancing the economy's competitiveness urgently requires choices in the energy field, especially since the external constraint could tighten as a consequence of the limited availability of energy at the world level.

From the standpoint of long-term industrial policy, failure to participate in the main lines of research and development could result in Italy being dependent on imported technologies in a sector of strategic importance. In addition, consideration of the problems connected with the production of energy cannot neglect its effects on the environment.

The drag on the external accounts associated with the energy deficit could nonetheless be considerably attenuated by policies promoting new energy-saving projects, with measures on urban traffic, goods transport and heating systems, along the lines followed in other countries.

EMPLOYMENT, WAGES AND PRICES

Employment

The demand for labour. — The total number of persons employed increased by about 100,000 last year, thanks to the growth of output. In its revised national economic accounts, Istat has estimated total employment in terms of full-time equivalent workers, defined as standard units of the total labour input used in economic activity. This full-time equivalent employment is considered net of workers on wage supplementation and takes account both of the employment of non-resident foreign workers and the extent of second jobs. Under this new definition, the expansion of employment was more pronounced, rising by about 200,000 units, or 0.8 per cent, compared with 1985 (Table 13). The greater part of the increase was accounted for by self-employment, which increased by 120,000 units. After a slight decline in 1985, self-employment increased its share of total employment last year to 32 per cent.

Table 13

EMPLOYMENT IN ITALY

(full-time equivalent; percentage changes on previous year)

	Total employment				Employees			
	1983	1984	1985	1986	1983	1984	1985	1986
Agriculture	2.4	−2.6	−3.1	−0.9	−2.4	−4.0	0.2	−2.5
Industry	−3.2	−4.0	−1.2	−0.6	−4.0	−4.1	−1.3	−1.2
of which: fuel & power products	*−1.3*	*1.1*	*0.7*	*..*	*−1.3*	*1.1*	*0.7*	*..*
manufacturing	*−4.2*	*−4.2*	*−1.0*	*−0.9*	*−4.6*	*−4.5*	*−1.1*	*−1.5*
industry excluding construction	*−4.1*	*−4.0*	*−1.0*	*−0.9*	*−4.5*	*−4.3*	*−1.0*	*−1.5*
construction	*−0.3*	*−4.1*	*−2.0*	*0.3*	*−1.9*	*−3.3*	*−2.4*	*−0.3*
Market services	2.8	5.3	4.5	2.4	1.2	5.6	5.8	2.4
of which: distributive trades, lodging and catering	*2.5*	*3.7*	*2.7*	*1.0*	*..*	*4.9*	*4.6*	*2.3*
transport & communications	*2.5*	*0.5*	*0.7*	*1.7*	*1.4*	*−0.1*	*..*	*2.3*
credit and insurance	*1.8*	*2.6*	*1.4*	*2.7*	*1.8*	*2.6*	*1.4*	*2.7*
other market services	*4.0*	*12.6*	*10.8*	*5.3*	*2.8*	*12.8*	*13.5*	*2.5*
Market goods and services	**0.3**	**0.4**	**1.2**	**0.8**	**−1.8**	**−0.2**	**1.8**	**0.3**
Non-market services	**1.6**	**2.4**	**2.1**	**0.9**	**1.6**	**2.4**	**2.1**	**0.9**
Total	**0.5**	**0.8**	**1.4**	**0.8**	**−1.0**	**0.4**	**1.9**	**0.4**

Source: Istat.

By sector, patterns were notably divergent, though less so than in previous years. The only sector that recorded an increase in employment was services, with a gain of 250,000 units, or 1.9 per cent. Employment in construction remained virtually unchanged. The revision of the national accounts not only revalued output and employment for the economy as a whole but also modified the shares of the individual components. The most pronounced adjustment of employment came in market services. The share of self-employment was revised upwards in all the main sectors of economic activity except agriculture, which suggests that the structural differences between Italy and the other advanced economies are more substantial than had been presumed.

The figures also reveal the importance of second jobs and the employment of foreigners. The latter was estimated at 600,000 full-time equivalent workers in 1986, or 2.6 per cent of the total, while second jobs accounted for 1.8 million units, or 7.9 per cent. Disaggregating the overall increase in employment since 1980, which has amounted to 900,000 units, we find that its principal components have been second jobs (which increased by 412,000 units) and foreign workers (330,000 units). This explains the discrepancy between the expansion of employment between 1980 and 1986 reported in labour force surveys, which found an increase of 1.8 per cent in the number of resident persons engaged in one or more full or part-time jobs, and that recorded by the national accounts, which registered an increase of 4.1 per cent in standard employment units.

Using this measure, nearly 60 per cent of total employment is now accounted for by services, including those provided by the public sector. The services sector expanded by about 2.3 million full-time equivalent units (20.8 per cent) between 1980 and 1986. Growth was particularly rapid in the sector of miscellaneous services, where standard employment increased by one million units, or 57 per cent.

In industry excluding construction, full-time equivalent employment net of wage supplementation declined by a further 50,000 units in 1986, or 0.9 per cent, despite the pick-up in economic activity.

The labour force. — The supply of labour, defined as resident individuals engaged in one or more labour activities or in search of employment, expanded by 350,000, or 1.5 per cent, in 1986. By far the larger part of the increase, 300,000 persons, was accounted for by women, for whom the demographic effect of a growing working-age population was combined with a rising participation rate. The expansion of employment provided work for only a third of the new members of the labour force. The unemployment rate thus rose to 11.1 per cent, as against 10.3 per cent in 1985, or 12.4 per cent including workers on wage supplementation, as against 11.7 per cent in 1985. A majority of the unemployed (1.9 million out of 2.6 million) were young people.

The geographical disparity in labour market conditions worsened in 1986. The unemployment rate held constant at 8.0 per cent in the North of Italy but rose from 14.2 to 16.5 per cent in the South, where female unemployment rose from 24.3 to 27.2 per cent. Owing to demographic factors, the growth of the labour force has been concentrated in the Southern regions, which accounted for two thirds of the expansion over the past two years, or 340,000 persons, while the pace of economic activity has not stimulated significant additional demand for labour there, with employment rising by no more than 70,000 over the same period.

Wages and labour costs

Industrial relations. — The agreement reached between Confindustria and the trade union confederations on 8 May 1986 settled the long-standing dispute over the payment of fractions of scala mobile points. The settlement provided for the incorporation of the two disputed points into wages in May and September and the payment of 100,000 lire to each employee in two instalments.

In the second half of the year, industrial relations were dominated by negotiations for the renewal of national labour contracts covering the major industries, the civil service, tourism and lodging and catering services. The contracts for workers in metallurgy and engineering and in textiles, which were signed in February, were almost the last in the current wage round, which was relatively long, in that many of the contracts had expired in 1985.

During the disputes over the new contracts, 39.5 million man-hours were lost owing to strikes, considerably fewer than in previous wage rounds. This, together with the sharp reduction of absenteeism, continues the appreciable decline in industrial unrest in the last few years, which is a result not only of changes in the pattern of labour relations but also of the weakness of the labour market.

Wages and labour costs. — Gross wages per employee (Table 14) rose by 6.1 per cent on the year, just over half the increase registered in 1985 (10 per cent) and in line with the target inflation rate. Since most of the major contract renewals came at the end of 1986 and in early 1987, earnings were unaffected by adjustments in basic rates. The wage

Table 14

LABOUR COSTS AND PRODUCTIVITY (1)

(percentage changes)

	Value added at market prices (2)	Total employment	Output per employed worker	Wages per employee	Labour costs	Unit labour costs
			Total (excluding renting of buildings)			
1981	0.9	0.0	0.9	23.9	22.6	21.4
1982	0.1	0.6	−0.5	15.3	16.2	16.7
1983	0.6	0.5	0.1	15.0	16.0	15.9
1984	3.4	0.8	2.6	12.2	11.4	8.6
1985	2.9	1.4	1.5	10.0	10.2	8.6
1986	2.8	0.8	2.0	6.1	7.7	5.6
			Agriculture			
1981	0.4	−5.0	5.7	17.8	17.9	11.6
1982	−2.8	−5.7	3.1	17.1	14.1	10.7
1983	8.8	2.4	6.2	17.5	22.7	15.5
1984	−3.9	−2.6	−1.4	11.0	9.0	10.6
1985	0.7	−3.1	3.9	11.7	12.5	8.3
1986	1.2	−0.9	2.2	5.1	6.5	4.2
			Industry excluding construction			
1981	−0.2	−3.6	3.6	22.9	20.9	16.7
1982	−1.6	−2.6	1.0	15.7	17.6	16.4
1983	−1.7	−4.2	2.7	16.0	16.8	13.8
1984	4.2	−4.2	8.7	14.9	14.0	4.9
1985	1.7	−1.0	2.7	10.5	11.6	8.7
1986	3.3	−0.9	4.3	6.2	8.1	3.7
			Construction			
1981	−1.9	1.7	−3.5	27.7	27.4	32.0
1982	−3.5	−0.1	−3.4	14.8	16.2	20.3
1983	1.0	−0.3	1.3	12.2	10.9	9.5
1984	0.3	−4.1	4.6	11.2	11.5	6.6
1985	0.3	−2.0	2.4	9.8	10.9	8.3
1986	−0.2	0.3	−0.5	4.0	5.7	6.2
			Services (excluding renting of buildings)			
1981	2.0	3.2	−1.2	20.1	18.3	19.7
1982	1.9	4.6	−2.6	15.1	15.8	18.8
1983	0.9	2.8	−1.8	15.4	16.2	18.4
1984	5.2	5.3	−0.1	10.9	8.9	9.1
1985	4.9	4.5	0.4	10.0	9.4	9.0
1986	3.3	2.4	0.9	5.4	6.6	5.6

Source: Istat.
(1) Net of the full-time worker equivalent of the hours of wage supplementation paid. — (2) 1980 prices; the figures for agriculture, industry and services include imputed bank services.

and salary increases that did take place were therefore largely due to indexation and wage drift. Except in the energy sector, where the new contract was already in force in 1986, increases in individual industries did not differ significantly from the average. Wages and salaries in general government, however, exceeded the average by about one percentage point.

Real wages per employee remained virtually unchanged overall. In industry they increased by 0.5 per cent, as against a 1.2 per cent increase in 1985, while they decreased by 0.5 per cent in market services. Over the last five years real wages have more or less stagnated, lagging behind the average gain in productivity as a result of both the limits on nominal wage increases fixed by the Government's inflation targets and the high rate of unemployment.

The new cost-of-living mechanism, with six-monthly increases and graduated coverage for income bands above a minimum, came into effect in 1986. The degree of indexation of average wages in manufacturing, measured in terms of their elasticity with respect to the trade union price index, was 52 per cent, compared with 60 per cent in 1985. For the *scala mobile* component alone, the effect of the new mechanism can be estimated at a half-point reduction in wage growth.

Compensation per employee increased by 7.7 per cent on average in 1986, or about 1.5 percentage points more than the rise in wages and salaries. The discrepancy was virtually the same in all industries, except banking and insurance, and was due essentially to the faster increase in compulsory contributions and provisions for pension funds. A rise of 2 per cent in overall productivity, however, held the rise in unit labour costs to 5.6 per cent, three points less than in 1985. The productivity gain was especially large (4.3 per cent) in industry excluding construction, making it possible to halve the rate of increase in unit labour costs from 8.8 to 3.9 per cent.

Prices

Thanks to international events, the slowdown in inflation was sharply accentuated in the course of 1986.

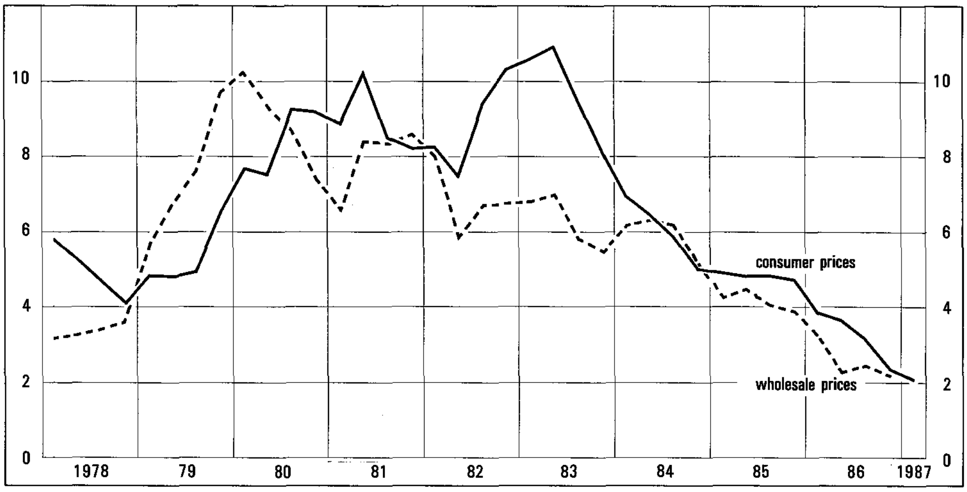
The twelve-month change in wholesale prices turned negative in the second quarter, owing to the fall in oil prices and the steady depreciation of the dollar. The improvement compared with 1985 was more than 8 percentage points, with a decrease of 0.9 per cent contrasting with a rise of 7.3 per cent.

Consumer price inflation slowed gradually in the course of the year, especially in the first and last quarters, with an average rise of 5.9 per cent as against 9.2 per cent in 1985. This was in line with the Government's target inflation rate. Italy's inflation differential vis-à-vis the other major industrial countries, measured in terms of consumer prices, narrowed by more than 2 percentage points between January and December, closing the year at 2.2 points (Figure 7). The narrowing of the gap stemmed in part from the direct and indirect effects of the about-turn in oil prices, amplified by Italy's greater external energy dependence, and in part from the success in slowing the rise in unit labour costs.

Figure 7

INFLATION DIFFERENTIALS VIS-A-VIS OECD COUNTRIES (1)

(based on quarterly twelve-month inflation rates)



(1) The differential for consumer prices refers to the OECD area as a whole, while that for wholesale prices is vis-à-vis the weighted average of Italy's 13 main trading partners.

The striking improvement of more than 14 points in the terms of trade had only a slight impact on domestic producer prices. The GDP deflator rose by 8.1 per cent, very slightly less than the 8.9 per cent registered in 1985. The fact that only part of the benefit of lower oil prices was passed on is explained by the widening of profit margins in industry and by the increases in excise duty on petroleum products in order to moderate the stimulus to domestic consumption.

The increase in unit labour costs was also very moderate, 3.7 per cent, because of the delay in concluding wage negotiations and the continuing strong gains in productivity in industry. The 3.0 per cent rise in the producer price index was only half as large as in 1985, but it was still much greater than the change in unit variable costs.

Manufacturers' pricing decisions were designed to offset a decline in orders and profitability in some overseas markets by widening domestic profit margins. In particular, the importance of exports to the dollar area and to OPEC countries may help account for the significant divergence between the rates of increase in the domestic prices of manufactures and in their average unit export prices.

The downward trend in inflation faltered in the early part of 1987, with the twelve-month rate of increase in consumer prices remaining stationary at 4.2 per cent over the first four months; nevertheless, the inflation differential between Italy and the OECD average narrowed to less than two points.

Disinflation: 1980-86. — At the end of 1986, the twelve-month rise in consumer prices stood at 4.2 per cent, the lowest rate since before the first oil shock. The positive achievements of 1986 must be attributed to the effects of the fall in oil prices and the depreciation of the dollar (Table 15). Even in previous years, however, there had been a slow but steady reduction in the rate of consumer price increase, from a peak of 22 per cent in November 1980 to 8.8 per cent in December 1985.

Table 15

DETERMINANTS OF INFLATION

(average compound rates of change)

	Dollar/lira exchange rate	World prices				Domestic prices			
		in US dollars:			in lire:				
		Primary products		Manufactures	Total merchandise import prices	Unit labour costs (private sector (1)	Other incomes per unit of output private) sector (1)	GDP deflator at market prices (1)	Consumer prices
		Total	Fuel						
1979-80	0.5	35.5	47.6	12.3	25.2	15.1	19.6	18.2	18.0
1981-82	25.7	2.0	8.3	−4.3	19.9	17.1	16.7	17.4	18.0
1983-85	12.2	−5.1	−6.1	−1.9	7.8	10.2	11.5	11.4	11.5
1979	−2.1	36.5	39.7	13.6	20.4	13.0	18.7	15.9	14.8
1980	3.1	34.5	55.9	11.1	30.3	17.2	20.6	20.6	21.2
1981	32.7	4.7	13.5	−5.3	28.6	17.7	17.9	18.5	19.5
1982	19.0	0.7	3.3	−3.4	11.7	16.4	15.6	16.2	16.5
1983	12.3	−9.0	−12.6	−3.6	5.2	13.6	14.6	15.3	14.7
1984	15.7	−1.3	−1.6	−3.4	11.4	7.6	12.1	10.2	10.8
1985	8.7	−4.7	−3.7	1.5	7.0	9.6	8.0	8.9	9.2
1986	−21.9	−27.4	−42.6	19.4(2)	−15.9	4.7	10.8	8.1	5.9

Source: Based on Istat, United Nations and Confindustria data.
(1) Data for 1979-80 are based on national accounts at 1970 prices. — (2) Provisional (average of first three quarters).

This progress was made at a time of volatile raw material prices and exchange rates. The second oil shock caused the dollar prices of energy imports to rise by 40 and 56 per cent in 1979 and 1980 respectively. From 1981 to 1985 the dollar strengthened steadily against all the major currencies; between early 1981 and early 1985 its appreciation with respect to the lira was more than 100 per cent. The international components contributed to inflation throughout the period from 1980 to 1985, and it was not until 1986 that they became disinflationary. The impact of these factors was especially strong in Italy owing to the economy's pronounced external openness, its comparatively heavy dependence on imported energy, especially oil, and the high degree of wage indexation.

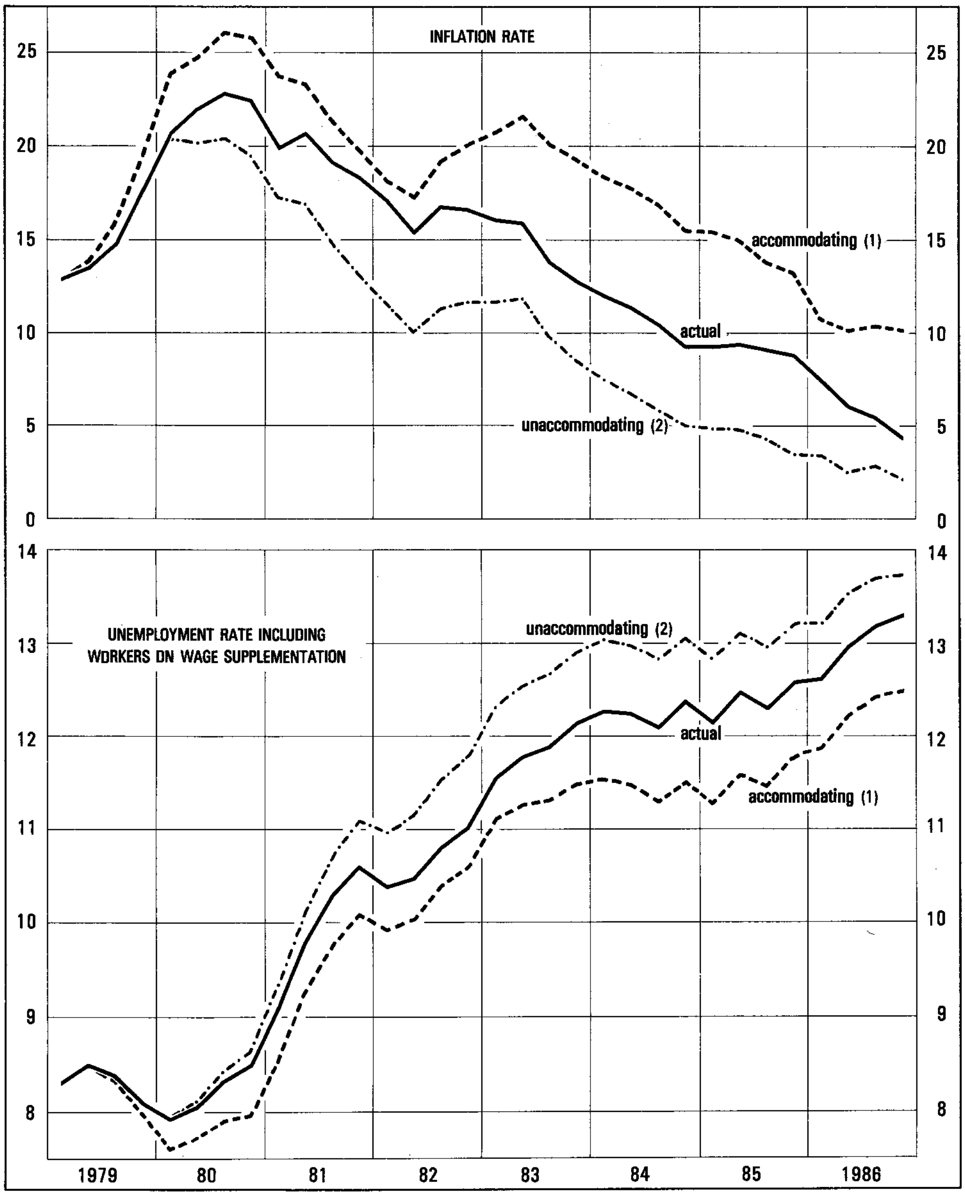
Throughout these years Italy applied a set of policies designed to blunt the negative impact of exogenous factors, control the expansion of domestic demand and close the inflation gap with the other industrial countries. In the absence of an effective fiscal policy, the pursuit of these objectives relied primarily on monetary and exchange rate policy together with some incomes policy measures. Exchange rate policy, conducted in the framework of the European Monetary System, successfully averted full accommodation of the inflation differential between Italy and its Community partners. Meanwhile, a reversal in monetary policy brought a rise of 10 points in the real interest rate on Treasury bills between mid-1979 and mid-1982, since when it has been held at about 6 per cent. The large and growing budget deficit has been financed chiefly by issuing securities, thus avoiding the dangers of excessive monetary financing.

Monetary and exchange rate policy were reinforced, by the adoption of incomes policy measures in 1983 and 1984. The degree of cost-of-living coverage provided by the *scala mobile* was reduced by 15 per cent in 1983 in order to curb the inflation-propagating effects of wage indexation. In 1984 *scala mobile* "programming" was enacted, consisting in linking the index not to past inflation but to a target rate for the current year. The measure was designed to accelerate disinflation by lowering inflationary expectations and weakening one of the key factors in the persistence of inflation. Policy on administered prices was also modified to conform to the Government's inflation targets. The potential of this policy as an anti-inflation tool was limited during these years, however, by the need to bolster the finances of public utilities, which had deteriorated sharply during the seventies, and by the large budget deficit.

A quantitative analysis of the impact of external factors and of the economic policies followed during the period of disinflation has been performed using the Bank of Italy's econometric model for a series of simulations based on a range of assumptions regarding international variables and economic policies. The results confirm that, had there been no exogenous stimuli, the rate of price inflation would have been substantially lower. On average for the period from 1980 to 1985, external factors contributed about 6 percentage points to the rate of consumer price inflation. The effect of the external shocks was transmitted through the economy gradually, because of the lag with which prices adjusted to higher production costs.

Figure 8

INFLATION AND UNEMPLOYMENT RATES WITH DIFFERENT EXCHANGE RATE POLICIES



Sources: Based on data of the old Istat national accounts series.

(1) Real effective exchange rate of the lira fixed at the value of the first quarter of 1979. — (2) Nominal effective exchange rate of the lira fixed at the value of the first quarter of 1979.

The speed of disinflation appears to have been fundamentally determined by the internal components of inflation, which declined steadily throughout the period. The study therefore assesses the effects of the economic policies followed on the domestic components of inflation, comparing the actual results with those that would have been produced with different policy approaches.

Maintaining a constant real exchange rate for the lira from the time of Italy's entry into the EMS onwards would have produced modest gains in output and employment but considerably greater inflation, averaging 4 points higher than the rates actually registered. A policy of maintaining a constant nominal exchange rate over those same years, on the other hand, would have significantly curbed inflation (by about 3 points on average) but at the cost of substantial losses in output and employment (averaging about 2 per cent) and increasingly large trade deficits (Figure 8).

As for monetary policy, the assumption of either more or less restrictive measures than those actually adopted yields results for income and inflation of about the same order of magnitude as those just described. However, monetary policy and exchange rate policy cannot be considered separately. The increase in interest rates over these years helped offset the negative impact on the external accounts of the rise in the real exchanges rate of the lira and encouraged an inflow of capital. Both policies were decisive in lowering the rate of inflation. The adoption of fully and immediately accommodating exchange rate and monetary policies would have greatly accelerated inflation in return for a slight gain in output and employment. Severely restrictive policies, by contrast, would have curbed inflation more effectively and more rapidly, but at the cost of substantial losses in income and a deterioration of the external accounts that would have made the policy unsustainable in the medium run.

THE BALANCE OF PAYMENTS ON CURRENT ACCOUNT

The most direct and visible consequences of last year's events in the international oil and foreign exchange markets were to be seen in the external accounts. The substantial recovery in the terms of trade produced a rapid improvement in the current account on a transactions basis, similar in size to the deterioration caused by the second oil crisis (Table 16).

Table 16

CURRENT ACCOUNT BALANCES

(billions of lire)

	1985	1986
Goods	**−11,930**	**5,850**
Goods cif-fob (customs data)	*−21,208*	*−3,632*
Services	**2,920**	**2,504**
Transport and insurance	−2,345	−1,934
Foreign travel	12,362	10,579
Income from capital	−7,596	−7,466
Income from labour	2,630	2,673
Other	−2,131	−1,348
Unilateral transfers	**2,138**	**−2,277**
Private	2,527	2,174
Public	−389	−4,451
Total . . .	**−6,872**	**−6,077**

Source: For customs data, Istat.

Merchandise trade

Valued on a customs basis (cif-fob), merchandise trade produced a deficit of 3,632 billion lire last year, about one sixth that recorded in 1985.

The average unit value of imports fell by 17.7 per cent; in the case of imported energy it declined by almost one half owing to the combined effect of the fall in dollar prices and the depreciation of the

US currency against the lira. The decline in the value of the dollar also reduced the lira unit value of imported raw materials, despite a rise in their dollar prices last year following a decline in 1985. Imports of manufactured goods benefited from slight reductions in price, both in the national currencies of foreign suppliers and in lire.

The average unit value of total exports decreased by 4.6 per cent, owing partly to a fall in the world market prices of petroleum products comparable to that in crude oil prices. There was a slight decline in the unit value of exports of manufactures, compared with an 8 per cent increase in 1985. As well as the general easing of inflationary pressures, this reflected firms' efforts to defend their market shares by applying different pricing policies to foreign buyers, a line of action necessitated by the heightening of international competition, the weakening of demand and, in some cases, the appreciation of the lira. Firms with a wide range of products in both domestic and foreign markets had greater room for manoeuvre with regard to export prices since they were able to widen their profit margins on domestic sales.

This led to a marked disparity between developments in competitiveness abroad and in the home market. Competitiveness in foreign markets, measured by the ratio between the index of average unit values of manufactured exports from Italy and the corresponding index for its main competitors, deteriorated slightly, mostly towards the end of the year. Import competitiveness, expressed as the ratio of manufactured output prices to the average unit value of imported manufactures, deteriorated by 3.8 per cent in 1986 as a whole, after having improved by 1.9 per cent in 1985.

The volume of imports expanded by 7.7 per cent in 1986, almost twice as fast as in the previous year. The rate of increase in domestic demand did not change significantly, however, rising only from 3.1 to 3.2 per cent.

The discrepancy between the rate of growth in imports and that in domestic demand is attributable partly to the loss of competitiveness, but also to continued growth in the volume of energy imports, which had begun to rise in late 1985 after contracting for a number of years. The sharp decline in relative prices was one of the factors in the recovery of consumption. Imports were boosted further by the revival in refining for export.

Total exports increased by 3.8 per cent in volume, slightly faster than in 1985, when they had risen by 3.1 per cent. However, the expansion in world demand, measured in terms of the volume of exports from industrial countries, weakened from more than 4 per cent in 1985 to 3 per cent last year.

The policy of holding down export prices limited the deterioration in export competitiveness during the year as a whole. Sales declined in some markets, such as North America and the United Kingdom, where the prices of Italian manufactured goods in local currency tended to rise faster than those of domestic products owing to the behaviour of exchange rates. However, the contraction was less than had been expected. The defence of the market shares won previously in these countries was presumably aided by favourable conditions of non-price competitiveness. Similar factors explain the increased penetration in other markets, chiefly in Europe, to which exporters switched sales that were no longer possible elsewhere owing to the appreciation of the lira or the fall in demand.

External dependence on energy and agricultural products

Net imports of energy averaged 1.6 per cent of gross domestic product and 5.3 per cent of foreign merchandise trade in the early seventies. On the basis of the revised GDP data, the two percentages had risen to 6.4 and 15.8 per cent respectively in 1981; last year they fell to 2.2 and 6.5 per cent. Energy nevertheless continues to be one of the main items in the trade deficit.

Among the major industrial countries, Italy and Japan, which are both poorly endowed with energy resources, are the most heavily dependent on imported energy. Expressed in tons of oil equivalent, Italy's net imports stood at 80.4 per cent of total energy requirements last year, only slightly below the level of the early seventies. In Japan, on the other hand, the proportion has declined substantially from the very high level of more than 90 per cent recorded after the first energy crisis, so that it is now close to the figure for Italy. In the other industrial countries it has also decreased markedly, especially since the second oil crisis. Everywhere except in the United Kingdom the reduction was mainly the result of an expansion in the generation of nuclear energy, which now accounts for more than half of domestic energy production in France and even in Japan. Gas, hydroelectric and geothermal power accounted for the bulk of primary energy production in Italy.

For many years the deficit in agricultural products and food has been second only to that in energy as a major cause of disequilibrium in merchandise trade. This became particularly clear in 1986, when the two deficits were once again of the same order of magnitude as a result of the fall in the value of net imports of energy; the energy deficit came to 19,260 billion lire and that in agricultural products to 16,411 billion lire.

The dimensions of the problem affecting Italy's balance of payments can better be assessed by classifying and aggregating data in accordance with different criteria to those habitually employed. If agricultural products used for non-food industrial purposes are reallocated to the industries in which they are consumed, the 1986 "food" deficit is reduced by a substantial 4.5 trillion lire and the traditional surpluses of other sectors, such as textiles and clothing, footwear and furniture, contract accordingly.

Even after such adjustment, the imbalance nevertheless remains large and has been static as a proportion of GDP throughout the eighties. Geographically, the largest deficits have long been in trade with EEC countries; from the point of view of type of good, they have been in products directly or indirectly related to foods of animal origin (live animals, butchered meat, milk and milk products, but also inputs for livestock farming such as fodder and other animal feed).

At the beginning of the last decade the deficit on trade in agricultural products and food with other EEC countries accounted for no more than a quarter of the total deficit; the proportion has steadily increased, so that it represented more than one half last year. At the same time, agricultural trade with these countries increased as a proportion of total agricultural trade, but the growth was almost entirely in imports; the deficit vis-à-vis the EEC therefore also rose as a proportion of total trade in such products, whereas the ratio for trade with non-Community countries decreased significantly.

For many years the demand for food products has been declining as a proportion of households' total domestic consumer demand in Italy. Its composition by type of good has also changed markedly, reflecting the shift in consumer preference towards higher quality items, such as animal products. The structure of domestic production has not entirely kept pace with these changes; it has certainly not managed to close the initial gap. The propensity to import has increased in the sectors where demand has been strongest.

The effects of Community agricultural policy are also partly to blame for the insufficient progress made in some areas of domestic supply. The greater protection given to products typical of Northern

Europe has accentuated the specialization of those countries. Italy, by contrast, has not benefited from similar measures to aid traditional Mediterranean products.

Market specialization of exports

Over the last twenty years a high and stable proportion of Italy's exports has been concentrated on the EEC, especially France and Germany; on average, around half of total exports have gone to this area. Sales to OPEC countries increased strongly between the first oil shock and 1981 but contracted thereafter, so that by 1986 they were little higher than in the early seventies. The North American market increased substantially in relative importance in the early eighties, whereas there was a gradual decline in exports to centrally planned European economies.

The relative specialization of Italian exports in OPEC markets, which was high throughout the fifteen years from 1970 to 1985, helped boost Italy's overall export penetration in the seventies, but it had a dampening effect in the eighties. Between the two oil crises, OPEC demand expanded at a rate two and a half times the average for the world market; the proportion of Italian exports shipped to these countries rose rapidly from little more than 4 per cent to 16.5 per cent and Italy's share of their markets increased substantially in both value and volume. In the eighties the fall in demand from this group impaired the overall penetration of Italian exports. These effects were only partly and temporarily offset by the expansion in sales in the US market, where demand was growing much more rapidly and the competitiveness of home-produced goods was weakened by the appreciation of the dollar. Last year these factors also decreased in importance.

The present picture of the development of world markets presents uncertainties for the future of Italian exports. Over the medium term, the prospects for demand growth are unfavourable in the industrial countries and even more so in fuel-exporting countries. An expansion in Italian exports to non-oil developing countries is impeded by the need of many of them to reduce their external debt and by competition from other industrial countries, especially the United States and the newly industrializing countries. Far Eastern markets remain relatively buoyant, but up to now it has been difficult to gain increased access; they still absorb only just over 2 per cent of Italian exports, equivalent to 3 per cent of their total imports.

The decisive role of traditional European markets, which continue to provide outlets for more than half of Italy's exports, has thus been reaffirmed. Here the crucial question remains that of competitiveness, not only in terms of price but also, and to a growing extent, in all aspects affecting relative product quality.

Invisibles

The serious deterioration in the invisibles balance last year was only partly caused by temporary factors. It was consistent with a trend that for many years has indicated a decline in the positive net contribution invisibles make to the current balance (Table 17).

Table 17

MAIN ITEMS OF THE CURRENT ACCOUNT

(balances as a percentages of total current transactions)

	1960	1965	1970	1975	1980	1985	1986
Goods (fob)	−5.8	3.2	−1.0	−1.2	−7.3	−2.8	1.5
Foreign travel	4.9	5.3	2.4	2.5	3.0	2.9	2.7
Income from capital	−0.3	−0.4	−0.1	−1.2	−0.3	−1.8	−1.9
Other services	1.3	1.2	0.2	−0.9	−0.3	−0.4	−0.2
Private transfers	2.6	2.1	1.3	0.6	0.6	0.6	0.5
Public transfers	−0.2	−0.3	−0.8	−0.4	..	−0.1	−1.1
Total	**2.5**	**11.1**	**2.0**	**−0.6**	**−4.3**	**−1.6**	**1.5**

Last year official transfers showed a net outflow of 4,451 billion lire, an increase of more than 4,000 billion over 1985. Almost 1,000 billion lire of the additional net disbursements was attributable to Italy's increased foreign aid commitments; the remainder related to the Community budget.

Italy became a net contributor to the Community budget for the first time last year. The situation is unlikely to change in the near future, given the recent accession of countries that will presumably remain net recipients over the medium to long term.

In 1986 there was a surplus of 10,579 billion lire on foreign travel, compared with one of 12,362 billion in 1985. Receipts declined by 7.9 per cent, whereas payments rose by 14.5 per cent.

The domestic prices of tourist services rose by 9.5 per cent. Hence in real terms total expenditure by foreign visitors to Italy fell by 15.9 per cent. Since the number of visitors did not differ significantly from that recorded in 1985, the decline was due entirely to a reduction in per capita expenditure. This was not caused by a shortening of stays — indeed, non-residents' overnight stays in Italian hotels increased by about 3 per cent — but by a shift in the nationality mix away from those with a higher propensity to spend, such as US citizens; 13.2 per cent fewer visitors from the United States came to Italy. According to OECD data, many other European countries were similarly affected, and in some cases worse than Italy. The main reasons lay in non-economic factors, such as terrorist incidents and environmental pollution caused by the nuclear disaster in the Soviet Union. In Italy, the disappointing results from the provision of tourist services to non-residents were also due in part to the loss of competitiveness of 5.2 per cent vis-à-vis the countries from which visitors came.

Expenditure abroad by Italian tourists continued to increase strongly, despite a 2 per cent fall in the lira equivalent of consumer prices in the main countries they visited. Real expenditure rose by 16.8 per cent, a far higher rate of growth than that in income. The increase in spending was stimulated by the marked loss of competitiveness (8 per cent on average in 1986) by domestic tourist services by comparison with those in the main countries visited by Italian tourists.

CAPITAL FLOWS

In 1986 Italy's official reserves rose by 3,489 billion lire, net of exchange rate adjustment and the revaluation of gold holdings (Table 18). The increase was the result of the current account surplus of 6,077 billion lire, a net outflow of non-bank capital of 6,266 billion lire and a net inflow of 6,454 billion through banking channels; almost all of the latter occurred in the first half of the year, when the ceiling on lira lending was still in force.

Table 18

CAPITAL FLOWS

(net; billions of lire)

	1985	1986	1986			
			1st qtr.	2nd qtr.	3rd qtr.	4th qtr.
Medium and long-term capital	**3,952**	**−1,422**	**432**	**422**	**−1,462**	**−814**
Direct investment	−1,555	−4,526	44	48	−2,237	−2,381
Foreign loans	7,063	4,926	677	1,138	842	2,269
Italian loans	−2,320	−1,825	−367	−707	−204	−547
Trade credit	1,020	27	59	−113	378	−297
Other	−256	−24	19	56	−241	142
Short-term capital	**2,249**	**−4,844**	**326**	**1,696**	**−3,751**	**−3,115**
Portfolio investment	717	−2,756	−1,760	2,363	−2,577	−782
Trade credit (1)	1,532	−2,088	2,086	−667	−1,174	−2,333
Total non-bank flows	**6,201**	**−6,266**	**758**	**2,118**	**−5,213**	**−3,929**
Banking flows (2)	**−5,299**	**6,454**	**5,590**	**1,803**	**−2,362**	**1,423**
Memorandum items:						
Current account balance	−6,872	6,077	−5,325	1,963	7,744	1,695
Errors and omissions	−7,681	−2,776	−2,129	425	−2,066	994
Official reserves (2)	−13,651	3,489	−1,106	6,309	−1,897	183

(1) With maturities up to 360 days. — (2) Changes in stocks net of exchange rate adjustments and, for official reserves, of gold revaluation.

The gross capital movements generated by non-bank financial transactions expanded to 117 trillion lire in inflows and 123 trillion in outflows. Of these transactions, foreign loans generated a surplus of 4,926 billion lire and all the other components produced net outflows, resulting from the continuing internationalization of Italian corporations, the sale by Lafico of its interest in Fiat, increased purchases of foreign securities by Italian investment funds, and short-term trade credit. The net outflows deriving from these movements exceeded 11 trillion lire and took place mainly in the second half of the year.

Expansion abroad by Italian industrial groups gave rise to a net capital outflow of 3,968 billion lire for the year. There was also a net outflow of foreign capital, disinvestment exceeding new investment in Italy by 558 billion lire. Italy's status as a net exporter of productive capital, which it first achieved at the start of this decade, was therefore enhanced.

New outward investment by Italian residents in 1986 totaled 4,975 billion lire, as against 4,360 billion in 1985; about a third of it was in the financial sector. Almost all of Italy's outward investment was directed to other industrial countries; investment in the United States and France amounted to more than 1 and 2 trillion lire respectively. Disinvestment from abroad by Italian residents increased slightly from 889 to 1,007 billion lire.

Foreign disinvestment from Italy was much more substantial, outweighing new investment. This does not, however, signal a reversal of the trend that has prevailed throughout the postwar period, namely the growing presence of foreign and multinational firms in Italian industry; indeed, new foreign investment in Italy increased from 4,182 to 6,572 billion lire, confirming the international interest in the Italian market. The increased net disinvestment in 1986 stemmed from Lafico's sale of its Fiat shares.

For several years now financial facilities accorded to foreign buyers of Italian merchandise have been contracting, not only as a share of total exports but in absolute value. The total of subsidized and unsubsidized export credit granted in 1986 amounted to 10.7 trillion lire, compared with 13.7 trillion in 1985; it represented just 7.3 per cent of the value of Italian exports, compared with 12.1 per cent in 1982 (Table 19).

Table 19

MEDIUM AND LONG-TERM EXPORT CREDIT

(billions of lire)

	1982	1983	1984	1985	1986
Trade credit	6,454	8,583	7,179	5,556	4,045
Italian loans (1)	1,616	1,536	2,669	3,251	3,307
Foreign-to-foreign loans (2)	4,010	1,981	3,467	4,867	3,301
Total export credit	**12,080**	**12,100**	**13,315**	**13,674**	**10,653**
as a percentage of total exports	12.1	10.9	10.2	9.4	7.3
Subsidized credit (3)	**7,731**	**4,665**	**7,314**	**6,913**	**5,303**

(1) Including claims paid by SACE and loans not tied by contract to export flows. — (2) Source: Mediocredito Centrale. — (3) Subsidy applications accepted by Mediocredito Centrale.

There has been a significant reduction in state-subsidized export credit because of regulations governing interest rate subsidies in lire and the constraints imposed by international agreements. Despite the amendments made last year, the latter caused the differential between market and subsidized rates to narrow further to just over 2 percentage points, compared with 10 points in 1982.

The net inflow produced by residents' borrowing abroad decreased from 7,063 to 4,926 billion lire. The only types of loan for which net inflows increased were those that have been liberalized. The net capital inflow from government or government-guaranteed loans decreased, while repayments of other authorized loans exceeded new credit outlays. For the second consecutive year a large volume of outstanding loans was renegotiated as a result of the better terms offered to Italian borrowers.

Portfolio investment in Italy by non-residents produced a net inflow of 543 billion lire, sharply down from 2,120 billion in 1985 (Table 20). If disinvestments made in 1986 but not recorded during the year because of delays in registration are taken into account, the net inflow becomes a net outflow of about the same size.

Table 20

PORTFOLIO INVESTMENT

(billions of lire)

	1985			1986		
	Investment	Dis-investment	Balance	Investment	Dis-investment	Balance
Foreign capital	**14,971**	**12,851**	**2,120**	**23,523**	**22,980**	**543**
Government securities	9,731	7,669	2,062	11,898	7,508	4,390
Treasury bills	3,810	3,460	350	1,175	1,194	– 19
Treasury bonds	531	486	45	824	544	280
Treasury certificates in ECUs	621	64	557	178	4	174
Treasury certificates and other	4,769	3,659	1,110	9,721	5,766	3,955
Listed shares	4,763	4,580	183	10,490	14,498	– 4,008
Bonds	477	602	– 125	1,135	974	161
Italian capital	**1,797**	**3,200**	**– 1,403**	**6,519**	**9,818**	**– 3,299**
of which: purchases by Italian investment funds	....	....	– 678	2,072	5,101	– 3,029
Foreign investment fund units	749	1,295	– 546	1,775	1,596	179

The balance for the year is the result of divergent patterns of behaviour for the various types of financial investment. Non-residents' purchases of government and other bonds exceeded sales by some 4,551 billion lire, a larger figure than in 1985. The only months in which there was net foreign investment were April, May and November; disinvestment prevailed in the rest of the year. By contrast, disinvestment in shares exceeded new investment in every month, giving rise to total net disinvestment of more than 4 trillion lire. Both purchases and sales of shares increased sharply, the former rising from 4,763 billion lire in 1985 to 10,490 billion lire last year and the latter from 4,580 to 14,498 billion.

Turning to Italian capital, net outward investment by residents amounted to 3,299 billion lire, more than twice as much as in 1985. The outflow was generated chiefly by the purchase of foreign securities by Italian investment funds. Such purchases, which were less than the maximum exempted from the non-interest-bearing deposit on foreign exchange, brought the funds' holdings of foreign securities to more than 3.7 trillion lire at the end of the year, as against 678 billion at the end of 1985.

Short-term trade credit gave rise to net outflows of 2,088 billion lire for the year. In the first quarter the closing of open speculative positions taken towards the end of 1985 produced a net inflow of 2,086 billion lire. The direction of flow was reversed in the last three quarters by the need to finance foreign trade, and in particular exports. Late in the year pressure on the lira in the foreign exchange markets accentuated the outflows at a time of high corporate liquidity.

The short-term outflows in the form of portfolio investment and trade credit were more than offset by banking inflows. The banking system's net external indebtedness increased by 6,454 billion lire during the year, after taking account of exchange rate adjustments. The expansion in net foreign currency liabilities occurred almost entirely in the first half of the year. There was a net outflow of funds in the late summer after the removal of the ceiling on lira lending. The net debtor position in external lire also increased, by 1,179 billion lire, despite a growth in assets, which was due in part to the decision to allow resident banks to grant foreign correspondents 10-day credit lines for use in settling Italian exports.

In January and February 1987, when there was a covered differential of about two percentage points between the lira and the major foreign currencies, an inflow of about 3 trillion lire occurred through banking channels, most of it in foreign currency. In March banking inflows diminished to 597 billion lire, partly as a result of the extension of reserve requirements to the increase in banks' net foreign currency deposits. In April the reduction of external lira liabilities resulted in a net outflow of banking funds. Over the first four months of the year, net banking capital inflows combined with an overall payments surplus of 3,550 billion lire to increase Italy's official reserves by about 6 trillion lire.

The nominal effective exchange rate of the lira was 7 per cent higher year on year, owing mainly to a substantial appreciation of 28.2 per cent against the dollar. Against the EEC currencies, however, the lira depreciated by 2.1 per cent. Over the twelve months it showed a larger overall appreciation of 9.7 per cent. At the start of 1987 the dollar depreciated further and strong pressures developed within the EMS affecting first the French franc and then, to a lesser extent, the lira. Almost all of the lira's downward movement within the band occurred on 8 January, when market exchange rates anticipated the realignment of parities of 11 January, which eased the speculative pressures. For the rest of the month the lira was constantly above the narrow band of fluctuation and the Bank of Italy sold lire in the foreign exchange markets.

In subsequent months the lira continued to appreciate against the dollar, though less sharply than before, but it weakened slightly within the EMS. The decline gathered momentum in late April and came to an end on 8 May, by which time the lira had depreciated by about 1.5 percentage points against all the major EMS currencies and fallen below the narrow band of fluctuation. This movement was consistent with the agreement among the central banks to make more flexible use of the fluctuation bands under the EMS exchange rate mechanism.

Italy's net external indebtedness declined last year, thanks to the surplus on current account. Expressed in dollars, however, the country's external financial position worsened because of the rise in the dollar equivalent of net liabilities denominated in other currencies, so that liabilities exceeded assets net of gold reserves by more than $34 billion. If official gold reserves are included, Italy's net debtor position was $8.1 billion. Between the end of 1985 and the end of 1986 net liabilities declined from 6.7 to 5.2 per cent of GDP (or 1.2 per cent including gold reserves).

In the seventies Italian foreign exchange controls were designed to curb capital outflows, making it possible to keep interest rates lower than those abroad. The lira devalued less than it would have in the absence of restrictions, so that additional inflationary pressures were averted. In the present decade, Italy's higher domestic interest rates have frequently generated capital inflows, which have raised problems of liquidity control and led to the adoption of measures to regulate inflows as well.

A general review of foreign exchange regulations was begun in the early eighties. In September 1986 Parliament enacted Law 599, which had originally been tabled in late 1983. The revision will have been completed when the Government has issued the implementing decrees for which the legislation provides. On the administrative level, procedures have been repeatedly streamlined and foreign exchange controls relaxed. The measures adopted in May 1987, in advance of the agreed deadline, honoured Italy's international commitment to abolish the compulsory deposit on investment abroad and further streamlined the exchange regulations and procedures for residents. Among other things, this entailed raising foreign exchange allowances for travel abroad to the levels obtaining in the OECD and extending the period for which foreign exchange accounts can be held, in some cases making it possible for parent companies to operate centralized accounts; the requirement to finance prepayments for exports in foreign exchange was abolished, the size of transactions not subject to exchange formalities was increased and the requirement to obtain foreign exchange documentation from an agent bank for external trade transactions was eliminated.

PUBLIC FINANCES

The combined effect of the corrective measures adopted in earlier years, the continued expansion in economic activity, the fall in the price of oil and the slowdown in inflation served to halt the growth in the government's funding needs in 1986. The state sector borrowing requirement decreased slightly, from 110.24 to 109.59 trillion lire net of settlements of past debts, thus achieving the objective of zero growth. The borrowing requirement of the public sector, which includes local authorities and social security institutions, recorded a larger fall as a result of local authorities having borrowed less from the credit system. This aggregate dropped from 112.27 to 109.83 trillion lire and from 13.9 to 12.3 per cent as a ratio to GDP (Table 21).

The decrease in both the public and the state sector borrowing requirements was the result of a rise in interest expenditure and a larger fall in the balance on other operations.

Table 21

BORROWING REQUIREMENTS

(as a percentage of GDP)

	1984	1985	1986
State sector borrowing requirement	13.2	15.2	12.3
Net of settlements of past debts	13.2	13.7	12.3
Public sector borrowing requirement	14.1	14.9	12.3
Net of settlements of past debts	14.1	13.9	12.3
Enlarged public sector borrowing requirement	14.4	15.0	12.3
Net of settlements of past debts	14.4	14.1	12.3

On the one hand, the continued expansion in economic activity increased the flow of tax revenues and, on the other, it reduced some expenditures, notably that on Wage Supplementation benefits. The expansion in revenues was also due to the fall in the price of oil, which allowed the duties on oil products to be raised without increasing prices.

Interest expenditure was pushed up further by the increase in the size of the debt. Public sector interest payments rose from 67.21 to

77.51 trillion lire, and from 8.3 to 8.7 per cent as a ratio to GDP. Owing to the lags inherent in the mechanism for adjusting the coupons of floating rate securities to changes in Treasury bill rates, the slowdown in inflation only had a small impact on interest payments in 1986. The greater part of the benefit will be felt this year.

Net of interest payments and settlements of past debts, the public sector borrowing requirement decreased from 45.06 to 32.32 trillion lire, and in relation to GDP from 5.6 to 3.6 per cent. This result owed much to a number of measures of a financial nature that reduced local authorities' net withdrawals from the Treasury and postponed to later years the inclusion in the budget of funds made available to the state shareholdings and ENEL. Taken together, these financial operations are estimated to have reduced the borrowing requirement by 8 trillion lire in 1986.

The overall effect of public finances on economic activity remained expansionary. This view derives from an analysis of the indicators that determine the range of the effects produced. The indicator based on the budget aggregates expressed in nominal terms (excluding purely financial items) suggests that there was no significant change in the contribution of the public sector to aggregate demand. By contrast, that based on the same variables expressed in real terms and the change in the purchasing power of the public debt points to a powerful expansionary impulse.

According to the new national accounts data, the ratio of total budget receipts to GDP rose from 39 to 39.4 per cent between 1985 and 1986, as a result of the 4.2 trillion lire produced by the building offences condonation. Notwithstanding the measures adopted to boost revenues, which generated an extra 6 trillion lire, the ratio of tax receipts and social security contributions to GDP remained virtually unchanged at about 35 per cent, excluding the receipts from the building offences condonation and imputed social contributions but including the revenues accruing to the European Community (Table 22).

The changes made to personal income tax rates to offset fiscal drag and the lag with which corporate profits are taxed resulted in the ratio of direct taxes to GDP remaining virtually unchanged at close to 13 per cent, notwithstanding the considerable increase in receipts from corporate income and local taxes produced by the rise in profits between 1984 and 1985, together with the revenues from the taxation of corporate bodies' income from government securities. Indirect tax revenues expanded faster than GDP, primarily as a result of the increase in the duties on oil products. Social contributions also outpaced GDP, the moderate rise in wages having been supplemented by changes in the structure of contributions.

Table 22

MAIN INDICATORS OF PUBLIC SECTOR FINANCES

(as a percentage of GDP)

	1984	1985	1986
Fiscal revenue (including EEC levies and social security contributions)	35.1	34.9	35.1
Total public sector expenditure	50.3	51.6 (1)	50.6
Deficit on current account (national accounts)	6.9	7.0 (1)	6.3
Net indebtedness (national accounts), excluding settlements of past debts	11.7	12.0	11.3
Net indebtedness (flow-of-funds accounts), excluding settlements of past debts	12.3	12.2	11.7

(1) Gross of settlements of past debts corresponding to 0.6 per cent of GDP.

Net of financial operations, interest payments and settlements of past debts, public expenditure decreased in relation to GDP from 42.6 to 42 per cent. This result did not so much reflect a reversal of the expansionary trend that developed in the early eighties as the effect of a series of factors, primarily of a short-lived nature. In the first place, the improvement in the terms of trade reduced the incidence of public expenditure since outlays rise with the deflator of domestic demand, which was curbed by the fall in the prices of oil and other raw materials. Secondly, the delay in signing the new labour contracts for the public sector resulted in expenditure totaling about 2,000 billion lire being postponed to this year. In turn, the change in the frequency of cost-of-living increases, the tightening of the means testing for family allowances, the reduction in Wage Supplementation benefits and the increase in health service charges are estimated to have saved about 2,500 billion lire.

The effect of the outturn for revenues and expenditures described above was to increase the public debt from 681.73 to 792.74 trillion lire, with a further rise in relation to GDP from 84.6 to 88.6 per cent.

Analysis of the composition of the public debt shows that there was a shift in favour of market funding and a corresponding decline in central bank financing. This can be attributed to the improvement in inflation expectations, which, coupled with the turnaround in the external accounts, permitted a reduction in the amount of money created by the Treasury.

The policy of lengthening the average maturity of the debt was continued in 1986 with large issues of seven and ten-year Treasury credit certificates. The expectations of a fall in both inflation and yields also permitted large sales of mainly three and four-year Treasury bonds, particularly in the early part of the year.

The average maturity to redemption of the public debt rose from two years and six months to three years and five months between the end of 1984 and the end of 1985, and lengthened further last year to three years and nine months. At the same time the proportion of floating rate securities decreased.

The outlook for 1987

The budget policy set out in the Government's financial planning document approved by Parliament in September is intended to continue the adjustment that was put in hand last year. It reaffirms the guidelines already prescribed in earlier documents: expenditure on current account to grow in line with inflation; that on capital account to expand in line with income; and fiscal revenue to remain unchanged in relation to GDP. Notwithstanding the start of major public works projects, observance of these rules should allow the state sector borrowing requirement net of interest payments to be reduced by more than 7,000 billion lire. The public debt will record a further large increase, but the interest burden should decrease, as the sharp fall in Treasury bill rates during 1986 is passed on to longer-term liabilities. The total state sector borrowing requirement is targeted at about 100 trillion lire, compared with 109.59 trillion in 1986, with a fall of 1.9 points in relation to GDP (from 12.3 to 10.4 per cent).

According to the planning document, this result is to be achieved through sectoral interventions designed to reduce the expenditure on major items — social security, health and local authority financing. Limits have been fixed for the amounts to be transferred to social security institutions and local authorities. However, the measures that should help to ensure these limits are respected have not yet been formulated.

This makes it uncertain whether the planned reduction of nearly 10 trillion lire in the state sector borrowing requirement will be achieved, insofar as the trend growth of expenditure may diverge from the path set in the budget.

There is also evidence that last year's results in controlling the public sector borrowing requirement have not been consolidated. The effects of some of the measures adopted, especially on the revenue side, were of short duration or of decreasing intensity; as, for example, those to speed up the collection of social security contributions, the building offences condonation and the provisions requiring non-state public bodies to redeposit a part of their balances with credit institutions in their centralized Treasury accounts. It is also worth noting that the corrective action taken with regard to expenditure reduced the amount of disbursements but failed to curb its growth rate significantly.

Achieving more effective control on expenditure remains a priority requirement — the expansionary trend has not been tamed. The underlying forces that boost spending in the fields of social security, health and local authority financing are still at work. The need for action to curb expenditure is confirmed by analysis of budget operations on an accruals basis. For lack of data, this has to be restricted to the central government budget, which saw expenditure commitments in the period 1983-86 rise much faster than the net disbursements of the state sector. This will inevitably result in a tendency for disbursements to rise faster in coming years.

On the revenue side, the need for a redistribution of the tax burden, the changes under way in the structure of the economy and the prospect of a European market for goods and capital make a far-reaching reorganization of the tax system necessary. The scale of tax evasion and avoidance and of the erosion of the tax base — highlighted by the recent revision of national income — provides scope for a policy designed to increase fiscal revenue in relation to GDP. Legislative action in this field needs to be accompanied by a strengthening of administrative action. New tax measures will in any case be necessary to offset the drying-up of extraordinary receipts.

A part of the difficulty encountered in recent years in controlling public deficits can be attributed to the inadequate analysis of the structural problems in the procedures for the management of public finances. The changes introduced by the resolutions adopted by the Senate and Chamber of Deputies Budget Committees while preparing the 1987 budget are designed to bring forward the decision on multi-year planning objectives, to set their formulation within the framework of medium and long-term trends, and to identify instruments and procedures for ensuring the desired results are achieved.

It is necessary that these new procedures should be fully implemented in coming years, in accordance with the guidelines laid down in the final report on the Parliamentary inquiry into the reform of Law 468/1978, the basis for the resolutions discussed above. Such application of the new procedures is especially important for the multi-year budget in both the no-change and the planning versions.

THE MONEY AND FINANCIAL MARKETS

The outcome for 1986

Monetary policy exploited all the room for manoeuvre created by the improvement in the terms of trade, the slowdown in inflation and the achievement of the targets for public finances. Interest rates were lowered across the board. Partly as a result of financial innovation, lending to the non-state sector expanded by 11.5 per cent, which was comparable to the growth in GDP but above the 7 per cent target.

Real interest rates on government securities came down during the year, but were high enough to allow nearly 90 per cent of net issues to be placed in the market and the growth in the money supply to be held close to 9 per cent, the central value of the target range. The increase in the monetary base was kept under control: when the effects of the abnormal events that boosted bank liquidity at the end of 1985 are eliminated, its rate of expansion fell from 12.1 to 8.2 per cent.

The growth of the share market and the progressive liberalization of exchange controls gave additional impetus to the transformation of Italy's financial structure. Firms diversified their sources of finance and intensified their financial management activities. For their part, households had a broader range of investments from which to choose. On the one hand, financial innovation sustained the demand for credit while, on the other, it helped to curb the growth in money. In these circumstances the relationships between the action of the monetary authorities, the increase in the monetary and credit aggregates and the changes in the macroeconomic variables that are the final objectives of monetary policy became more complex. It was necessary to respond more flexibly to monetary and credit developments in the light of the sometimes conflicting messages sent by real and financial indicators.

The damping of the exchange crisis that developed towards the end of 1985, the general improvement in economic conditions and the slowdown in the growth of bank lending produced by the ceiling allowed an easier monetary policy stance to be adopted from March on. Between March and May the prospect of lower inflation contributed to the authorities lowering the discount rate to 12 per cent in a series of quick steps totaling nearly 3 points. Over the first six months of the year the rates on Treasury bills came down by a similar amount. Bank rates, which had come down faster than those on government securities in 1985, also decreased, but more slowly.

Despite the reduction in the yield differential between bank deposits and government securities, the growth in the money stock was very small in the first half of the year. The increase in share market activity and the success of investment funds resulted in a shift in the composition of households' portfolio towards less liquid assets. This tendency was also fueled by expectations of further reductions in interest rates, which sustained the demand for government securities and enabled a large proportion of the state sector borrowing requirement to be financed in the market.

After the abolition of the ceiling in June, the expansion in bank lending gradually built up again, and was supplemented by further strong growth in that of special credit institutions. The decline in the interest rates on government securities continued, but at a slower pace.

The rise in bank lending accelerated in the last quarter of the year to an equivalent annual rate of 18 per cent. This was due both to financial arbitrage operations by corporate treasuries, which were reflected in an increase in firms' liquidity, and to acquisitions of equity interests in Italy and abroad by a number of industrial groups. It was nonetheless feared that an excessive increase in lending might push up domestic demand, albeit with a lag, to above the level consistent with the objectives of lower inflation and external account adjustment. To forestall this danger and counter the turbulence that developed in the exchange market, the control of liquidity was tightened in the last part of the year and the interest rates on central bank financing operations and in the interbank market rose sharply. The fall in the interest rates on government securities came to a halt.

The more restrictive stance of monetary policy was also justified by the difficulty of placing government securities, which led to a large creation of monetary base through domestic channels in the last quarter. Between September and November, bank deposits expanded at average annual rates of around 18 per cent. The speedup reflected the halt in the rise of share prices and the consequent slowdown in the sales of investment fund units. Another temporary factor may have been the introduction, decided in September 1986, of a 6.25 per cent withholding tax on interest earned on government securities.

The rise in bank deposits slowed at the beginning of 1987, but the strong growth in lending continued. In the first half of January the need to reduce the pressure on the lira in foreign exchange markets led the central bank to tighten its control on bank liquidity and money market rates rose to over 13 per cent. After the exchange market strains had disappeared in the wake of the EMS realignment on 11 January, the liquidity situation became easier and the rates on the Bank of Italy's short-term financing operations were gradually lowered.

The calmer conditions in exchange markets, together with favourable interest rate differentials, led firms to increase their short-term foreign currency borrowing. In February, the slowdown in bank lending in lire was coupled with a pronounced increase in that denominated in foreign currencies. The net debt of the banking system towards the Bank of Italy, which had amounted to about 10 trillion lire at the end of January, was down to almost nothing at the beginning of March. In the middle of March a reserve requirement (equal to 25 per cent of monthly changes in banks' net external positions) was imposed with the aim of curbing the foreign-based expansion of credit and liquidity. The introduction of this reserve resulted in domestic and foreign resources receiving the same treatment. Following similar measures in other European countries and in Japan, the official discount rate was lowered at the same time by half a point to 11.5 per cent. The combined effect of these measures was to halt the inflow of foreign funds via the banks in the last part of March.

To round off the package, the central bank concerted with numerous banks and invited them not to grant loans at conditions that would encourage firms to engage in round tripping, thereby boosting banks' assets.

Lending to the private sector and total domestic credit. — In 1986 the expansion in lending to the non-state sector (i.e. bank and special credit institution loans plus the net bond issues of firms) amounted to 46 trillion lire, an increase of 11.5 per cent on the initial stock (Table 23). The increase in this aggregate was nearly the same as that recorded in 1985, when the outcome was influenced by the anomalous growth in bank loans at the end of the year. Accounting figures show a 10 trillion lira decrease in the flow of bank loans compared with 1985, and a roughly equal increase in the funds raised from special credit institutions and through bond issues. The net volume of the latter reflected the almost 3.5 trillion lire raised in this way by state-controlled companies with the related debt service charged to the budget.

To determine the trend of lending to the non-state sector, adjusted to eliminate the anomalous peak recorded at the end of 1985, the rate of increase in the twelve months through November can be considered. This rose from 10.5 per cent in 1985 to 13.1 per cent last year, while the total lending of banks and special credit institutions increased in the twelve months through November 1986 by respectively 12.4 and 12.9 per cent (compared with 11.3 and 9.2 per cent in the corresponding period in 1985).

Table 23

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		
1982 - Dec. (3)	13.4	20.9	18.0	18.0	18.0	18.0
1983 - Dec.	13.2	20.7	11.5	12.3	13.6	19.6
1984 - Dec. (4)	15.6	19.7	11.2	12.1	14.0	19.0
1985 - Nov.	10.5	17.9	12.2	13.3	13.3	16.9
- Dec.	12.9	18.1	10.2	11.2	11.7	16.7
1986 - Nov.	13.1	16.1	8.7	9.8	8.2	18.3
- Dec.	11.5	15.2	8.2	9.4	8.2	17.2
1987 - Apr. .... (5)	12.4	15.0	9.1	11.3	7.6	....

(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 actuarial reserves, severance pay provisions and pension funds. — (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) Provisional. For M3 and financial assets, data refer to February.

The total finance provided to the private sector, including the funds raised abroad and in the share market, amounted to 68 trillion lire, an increase of 12.4 per cent. In relation to GDP, the total flow of finance to firms and households decreased slightly to 7.6 per cent. While the volume of foreign loans remained virtually unchanged, there was a considerable increase in the proceeds of share issues, which more than doubled from 4.3 trillion lire in 1985 to over 10 trillion last year (Table 24).

The funds raised by firms in the capital markets by way of share and bond issues accounted for more than 20 per cent of the total flow of credit granted to the private sector, while the share intermediated by banks and special credit institutions dropped to around 60 per cent, one of the lowest values since 1980 (Figure 9). Even though the diversification of the capital markets that is under way tends to increase the importance of the non-bank channels of corporate finance, the peak in share issues recorded in 1986 was related to the exceptional growth of the share market. The full effects of the revision of the regulations governing the stock exchange and listed companies and of the introduction of Italian investment funds were compounded by the improvement in corporate profitability and the fall in inflation and interest rates. For the second year running, the market capitalization of the companies listed on the stock exchange more than doubled. Turnover was two and a half times the 1985 figure and nearly ten times that for 1984. In turn, the gross issues of listed companies tripled, rising from 5 to 15 trillion lire.

Table 24

TOTAL DOMESTIC CREDIT AND LENDING TO THE PRIVATE SECTOR

(changes in billions of lire)

	1982	1983	1984	1985	1986
Total domestic credit	**100,640**	**120,626**	**139,723**	**153,947**	**152,388**
State sector borrowing requirement (1)...	69,036	85,194	91,401	107,471	106,343
Finance to the non-state sector (2) .... (+)	31,604	35,432	48,322	46,476	46,045
finance to public bodies (3) .... (−)	*3,362*	*4,390*	*7,020*	*2,453*	*−249*
foreign loans .... (+)	*3,074*	*755*	*−839*	*2,308*	*1,954*
endowment funds .... (+)	*7,384*	*9,431*	*6,548*	*5,132*	*1,704*
share issues (4) .... (+)	*2,038*	*2,967*	*4,948*	*4,310*	*10,606*
other (5) .... (+)	*1,034*	*4,552*	*5,341*	*7,390*	*7,419*
Total finance to the private sector .... (=)	**41,772**	**48,749**	**57,300**	**63,163**	**67,977**
Percentage changes (6)	*12.8*	*13.1*	*13.4*	*12.9*	*12.4*
As a percentage of GDP	*7.7*	*7.7*	*8.0*	*7.8*	*7.6*

(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 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 credit institutions, acceptances, atypical securities and other minor items. As of 1985 the difference between the finance provided by leasing, factoring and consumer credit companies and their net borrowing from credit institutions is also included. — (6) Based on end-of-period data.

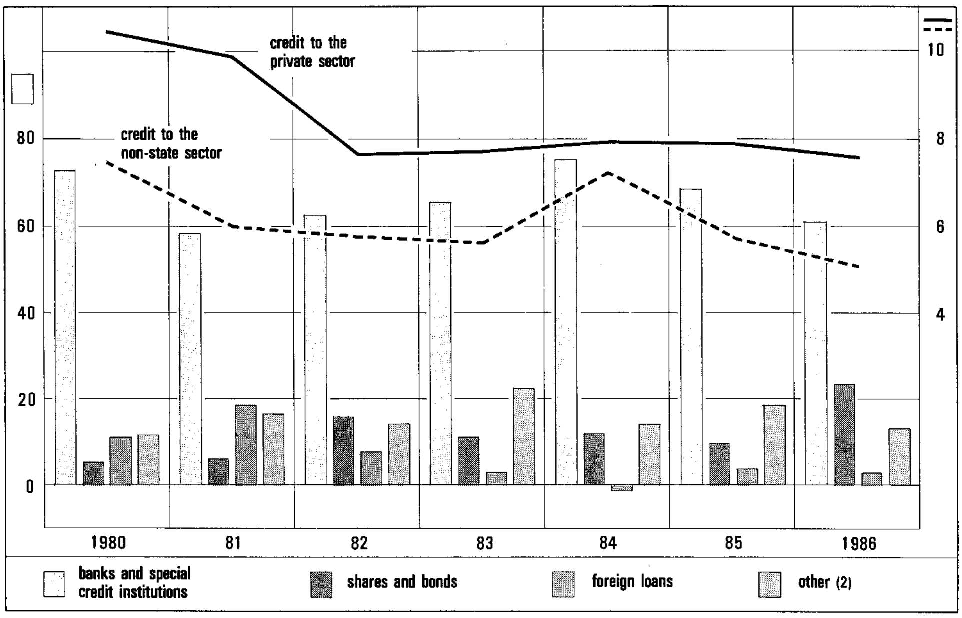
The bunching of issues in the second half of the year contributed to the weakening of share prices. The banks participating in underwriting and placement consortia had to take up a part and their share portfolio doubled in the last quarter from 1 to 2 trillion lire. The principal beneficiaries of the increased volume of share purchases were large firms — 70 per cent of the year's issues were made by five large industrial groups.

The higher level of self-financing and greater recourse to the capital markets will tend to reduce large firms' demand for bank credit in the medium term. Moreover, the variability of bank lending has increased in the short term since it is used to meet peak funding requirements, sometimes connected with arbitrage operations in Italy and abroad. The centralized cash management of the major industrial groups has increased competition in this segment of the loan market. In 1986 this development was reflected in the reduction in the rates banks charged their major customers. These fell below their prime rates and on occasion were actually unprofitable. The ratio of facilities used to those accorded fell to 25 per cent for the largest categories of loans, whereas it remained virtually unchanged for the others.

Figure 9

CREDIT TO THE PRIVATE SECTOR (1)

(composition and flows in relation to GDP; percentages)



(1) The figure is based on the data in Table 24. — (2) Includes: endowment funds; other participations; funds provided by leasing, factoring and consumer credit companies; public sector loans; credit institutions' bad debts; and other minor items.

Corporate finances improved considerably in 1986. In relation to value added, the gross operating surplus rose and net interest expenditure decreased, while gross fixed investment and stockbuilding both slowed compared with the previous year. Consequently, investment in financial assets increased: firms' holdings of bank deposits, bonds and government securities expanded by 13 per cent, as against 12 per cent in 1985. The ratio of this increase in firms' liquid assets to that in their short-term debt vis-à-vis banks and special credit institutions was 112 per cent, compared with 73 per cent the year before. There was a further strengthening of the network of inter-firm links, with a corresponding increase in equity investments both in Italy and abroad. Net trade credits also increased, marking a reversal of the 1985 result.

The debt of the public sector again expanded faster than that of the corporate sector. The domestic state sector borrowing requirement amounted to 106.3 trillion lire, a marginal increase on the previous year and equal to 17.6 per cent of the initial stock. Total domestic credit expanded by 152.4 trillion lire, an increase of 15.2 per cent on the initial stock — three points less than in 1985 but two points more than the target. In relation to GDP, the flow of total domestic credit decreased from 19 to 17 per cent, while the share absorbed by the public sector remained unchanged at 70 per cent.

Financial assets and money. — The expansion in total domestic credit together with the issue of shares led to a considerable increase in the private sector's financial assets. Holdings of domestic assets rose by 17.2 per cent, over 6 points faster than GDP. The revised national accounts indicate that, net of shareholdings, the financial wealth of firms and households at the end of 1986 amounted to 136 per cent of GDP, 7 points up on the figure for 1985. When shareholdings are included, the ratio of financial assets to GDP is found to have risen from 199 to 230 per cent.

The growth in the M2 money supply amounted to 9.4 per cent, nearly two points less than that in GDP. Net of bank certificates of deposit, the money supply (M2A) grew by 8.2 per cent, as against 10.2 per cent in 1985. This moderate growth in money — achieved notwithstanding the overshoot of total domestic credit — can be attributed in part to the revival of savers' interest in fixed rate medium-term securities as a result of the steady fall in interest rates and expectations of a sharp slowdown in inflation.

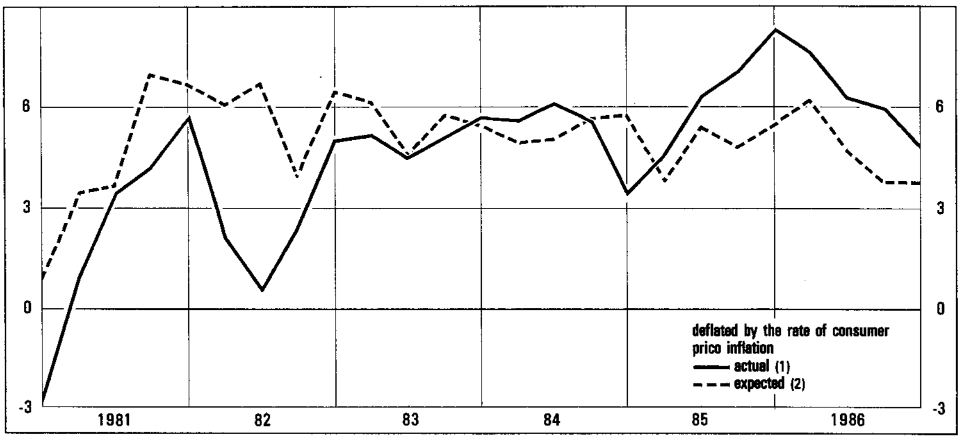
The real yield on 6-month Treasury bills, based on actual consumer price inflation and net of tax, averaged around 7 per cent, two points above the 1985 figure. The real yield came down gradually from the very high level of the beginning of the year and was below 5 per cent in the first quarter of this year (Figure 10). The reduction in the real yields on Treasury bills over the year was due to the fall in nominal rates, which averaged 3.5 points for the three maturities. There was an even sharper fall in the nominal rates on Treasury bonds, for which the after-tax yields at issue came down from 13.7 to 9.2 per cent. The net issues of these securities rose from 4 to 35 trillion lire, and they covered the greater part of the Treasury's net recourse to the market.

Bank deposit rates fell from 10.1 to 7.6 per cent, one point less than the fall in Treasury bill rates. Most of the decrease came in the first half of the year and was stimulated by the central bank in concertation with a broad range of individual banks. In the same period the rise in share prices intensified expectations of gains on the units of investment funds and fostered the latter's expansion. More than a quarter of the flow of financial assets in 1986 was accounted for by investment fund units and shares, while bank deposits represented only 23 per cent. The corresponding figures for the previous year were

12 and 29 per cent. Investment funds also enabled households to diversify their portfolios with the addition of foreign securities totaling over 3 trillion lire, the purchases of which were exempt from the non-interest-bearing deposit on foreign exchange.

Figure 10

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.

The expansion in households' financial wealth has increased the demand for portfolio diversification. The possibility of entrusting the management of shareholdings to investment funds supervised by the Bank of Italy and the Consob has reduced the risk investors perceive in such investments. The growth in these intermediaries had a pronounced impact on the share market last year. Even though about 70 per cent of the total resources of investment funds were invested in bonds and government securities, their net purchases of shares amounted to 60 per cent of the issues of listed companies.

The outlook for 1987

In recent months the demand for new issues of government securities has flagged. The composition of demand, which has shifted in favour of short-term maturities, suggests an increase in investors' liquidity preference. This is confirmed by the rapid growth in bank deposits. In March and April these expanded at an annual rate of around 14 per cent, taking the growth in M2 to over 9 per cent in the first four months of the year and above the target range. Certificates of deposit recorded an especially rapid rise, net of which the growth in money was only slightly over 8 per cent.

After rising rapidly in the early part of the year, bank lending in lire and foreign currencies slowed down in March and April. Consequently, the annual rate of increase in the first four months was slightly below 10 per cent. The increase in the lending of special credit institutions was of the same order, but followed a more regular path. Overall, the rise in the public sector's demand for credit was coupled with some slackening in that of the private sector in the last few months, but the rate of expansion in lending to the non-state sector since the beginning of 1987 has remained around 11 per cent, which is above the target for the year.

Developments in the macroeconomic situation and in public finances confirm the need to maintain the objectives fixed last autumn for the expansion of credit and the growth in the money supply. The growth in nominal GDP appears to be in line with the original projection, but the pace at which domestic demand is rising, fueled by private consumption, is tending to reduce the forecast external surplus.

An overshooting of the target for the state sector borrowing requirement would make it necessary for the Treasury to borrow more in the capital markets. In the last two months the fall in the yields on government securities has halted. The rates on the Bank of Italy's temporary finance, which had dropped sharply after the mid-January realignment of the EMS currencies, moved upwards again in May.

If the progress made in curbing inflation is to be consolidated, the level and structure of interest rates over the rest of the year will have to be such as to allow government securities to be taken up by savers. In view of the probable increased freedom of capital movements, considerable flexibility in the management of money market interest rates and greater scope for management of the exchange rate within the EMS fluctuation band will be necessary to control the growth in the money supply and the expansion of credit.

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

Control of the monetary base

Interest rate measures and central bank intervention in the money market last year can be divided into three distinct phases. The exchange rate crisis that had developed at the end of 1985 necessitated a brief period of severe restriction, reflected in an increase in interbank rates and Treasury bill yields and in the temporary reintroduction of the ceiling on bank lending. Once that had been overcome, controls on bank reserves could be eased in the spring. With orderly conditions in the exchange market, the balance of payments improving and the monetary and credit aggregates expanding moderately, the rapid fall in inflation persuaded the authorities to make a substantial reduction in interest rates on government securities, reinforced by three successive one-point cuts in official rates. From the summer onwards, the acceleration in the monetary and credit aggregates and occasional signs of weakness in the demand for securities called for a progressive tightening of liquidity and action to halt the decline in yields on government stock.

The overall improvement by comparison with 1985, which was made easier by the fact that the Treasury borrowing requirement was kept within the target range and by the good balance-of-payments performance, is evident both in the slower growth in monetary base and bank reserves and in the better balance between the various sources of monetary base creation. Net of the changes in the compulsory reserve coefficient and after adjustment for the estimated effects of the expansion in bank liquidity at the end of 1985 caused by the disruption of centralized accounting operations at the Bank of Italy, the growth in monetary base amounted to 8.2 per cent, compared with 12.1 per cent in 1985, while bank reserves increased by 8.8 per cent, compared with 14 per cent (Table 25).

Analysis of the composition of monetary base creation shows a substantial contraction in domestic sources, especially monetary financing of the Treasury. Monetary base grew by 9.2 trillion lire (Table 26), there was an inflow of liquidity from abroad amounting to 3.5 trillion lire, and monetary creation via the Treasury came to 11 trillion, equivalent to 10 per cent of the borrowing requirement; in 1985 the external sector had destroyed more than 13.6 trillion lire, while Treasury recourse to central bank financing had exceeded 27.5 trillion, 22.4 per cent of the borrowing requirement. Refinancing of the banking system returned to a normal level last year, after being increased by almost 6 trillion lire in 1985 mainly to allow orderly interbank operations while centralized accounting operations were disrupted.

Table 25

MONETARY BASE AND BANK DEPOSITS

(percentage changes on an annual basis) (1)

	1984	1985	1986	1985 Quarters I	II	III	IV	1986 Quarters I	II	III	IV	1987 Ist qtr. (2)
Compulsory reserves												
adjusted (3)	12.9	14.8	10.1	12.2	24.5	13.0	7.1	-6.3	22.5	4.9	18.8	-1.0
unadjusted	*16.1*	*19.1*	*11.9*									
Bank reserves												
adjusted (3)	14.0	18.1	5.0	3.8	29.1	9.9	25.3	-16.6	18.1	9.4	15.6	7.5
		(14.0)	(8.8)				(12.8)	(-7.3)				
unadjusted	*16.9*	*21.8*	*7.8*									
Monetary base												
adjusted (3)	12.5	14.6	5.8	7.9	24.1	7.1	17.3	-2.3	8.8	9.4	9.3	6.3
		(12.1)	(8.2)				(9.6)	(4.5)				
unadjusted	*14.4*	*17.3*	*7.5*									
Bank deposits	11.6	10.1	8.9	16.9	11.4	10.7	3.2	4.5	8.5	8.9	15.5	6.3

(1) Based on end-of-period values. The quarterly figures are seasonally adjusted. — (2) Provisional. — (3) 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 2.6 trillion lira abnormal rise in banks' cash balances at end-1985 caused by disruption of centralized accounting operations as a result of strikes by Bank of Italy staff.

Private investors and the banking system purchased 85.74 trillion lire of government securities at issue, equal to 89 per cent of total Treasury issues; in 1985 the proportion had been 83 per cent, excluding securities issued to fund past debts. Moreover, the strengthening of expectations of a reduction in interest rates heightened investor preference for fixed rate securities; net purchases of Treasury bonds at issue by the market came to 31.5 trillion lire, equivalent to 37 per cent of total subscriptions; in 1985 they had totaled 2.6 trillion lire, or 4 per cent.

Among the uses of monetary base, cash in circulation increased by 3,143 billion lire, or 6.9 per cent, as against 9.7 per cent in 1985 ; such a slowdown at a time when the appreciable reduction in interest rates might have encouraged the holding of banknotes can be explained only in part by the slower growth in consumption at current prices and may have been influenced by the long-term trend towards the use of more sophisticated payment instruments.

Table 26

MONETARY BASE (1)

(changes in billions of lire)

	1984	1985	1986 Year	1986 Quarters I	II	III	IV	1987 Ist qtr. (2)
Foreign sector (3)	**5,141**	**−13,677**	**3,543**	**−894**	**6,122**	**−1,903**	**218**	**5,357**
Balance of payments	57	−8,352	−2,965	−6,696	4,506	465	−1,240	1,685
Net foreign position of banks	5,138	−5,299	6,454	5,590	1,803	−2,362	1,423	3.672
Treasury	**10,027**	**27,519**	**10,994**	**11,084**	**−10,802**	**3,229**	**7,484**	**1,684**
Borrowing requirement	95,388	122,828	110,192	26,247	19,937	36,206	27,803	24,602
Net sales of securities	−75,431	−82,889	−87,563	−14,300	−29,956	−32,170	−11,137	−22,024
primary market	−70,419	−81,409	−85,740	−16,741	−33,143	−22,068	−13,788	−13,516
Treasury bills	−13,187	1,802	−6,455	−785	−2,508	−7,885	4,723	8,025
Treasury credit certificates	−54,436	−68,695	−48,164	−9,024	−19,894	−6,260	−12,986	−15,631
Treasury bonds	−3,941	−2,625	−31,542	−7,185	−10,522	−7,740	−6,095	−5,148
other securities (4)	1,145	−11,891	421	253	−219	−183	570	−762
of which: securities issued to fund debts	—	*−10,403*	—	—	—	—	—	—
open market	−5,012	−1,480	−1,823	2,441	3,187	−10,102	2,652	−8,508
of which: repurchase agreements	*2,661*	*4,933*	*1,913*	*4,148*	*3,897*	*−8,843*	*2,711*	*−5,445*
Other financing (5)	−9,929	−12,420	−11,635	−863	−782	−807	−9,183	−894
Refinancing	**−218**	**5,881**	**−4,333**	**897**	**−5,275**	**−834**	**878**	**−1,237**
Other sectors (6)	**−1,104**	**−647**	**−1,004**	**−10,848**	**8,779**	**−362**	**1,427**	**−3,233**
TOTAL (6)	**13,847**	**19,076**	**9,200**	**240**	**−1,176**	**130**	**10,007**	**2,571**
Non-state sector	**3,861**	**4,002**	**3,143**	**−655**	**−755**	**463**	**4,090**	**−3,193**
Banks (6)	**9,986**	**15,073**	**6,057**	**894**	**−421**	**−333**	**5,917**	**5,763**
Compulsory reserves	8,855	12,213	9,022	4,746	−1,038	644	4,668	6,121
Non-interest-bearing deposits against excess lending	−2	—	—	877	462	−1,334	−5	—
Excess reserves (6)	1,133	2,860	−2,965	−4,729	154	357	1,254	−357

(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. — (4) Contains a discrepancy due to bank charges on purchases of securities for customers and to accounting lags. — (5) PO deposits of the public and 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. — (6) The series has been adjusted to exclude the growth in banks' deposits with the Bank of Italy caused by the method of recording monthly stock exchange settlements.

The expansion in compulsory reserves was less than three quarters that recorded in 1985 (9,022 billion, against 12,213 billion) owing to the slowdown in deposit growth. As regards intermediation in lire, the average reserve coefficient for the banking system as a whole (measured as the ratio of the reserves lodged in one month to the deposits subject to reserves in the preceding month) rose from 19.6 per cent in January 1986 to 20.2 per cent a year later, and thus moved even closer to the maximum of 22.5 per cent laid down in current regulations.

In March 1987 the reserve requirement was extended to changes in the banks' foreign exchange liabilities net of those reinvested abroad. The measure established a link between inflows of foreign capital through the banking system and the demand for bank reserves, thereby facilitating the control of total credit and placing foreign currency business on a par with that in lire. In the past, control of the banks' foreign currency operations had necessitated imposing quantitative limits on the expansion in their net external positions; if such limits remain in force for more than a short period, they can cause inefficiency in the allocation of resources by perpetuating the market shares of individual banks.

Central bank intervention in 1986 and the early months of 1987

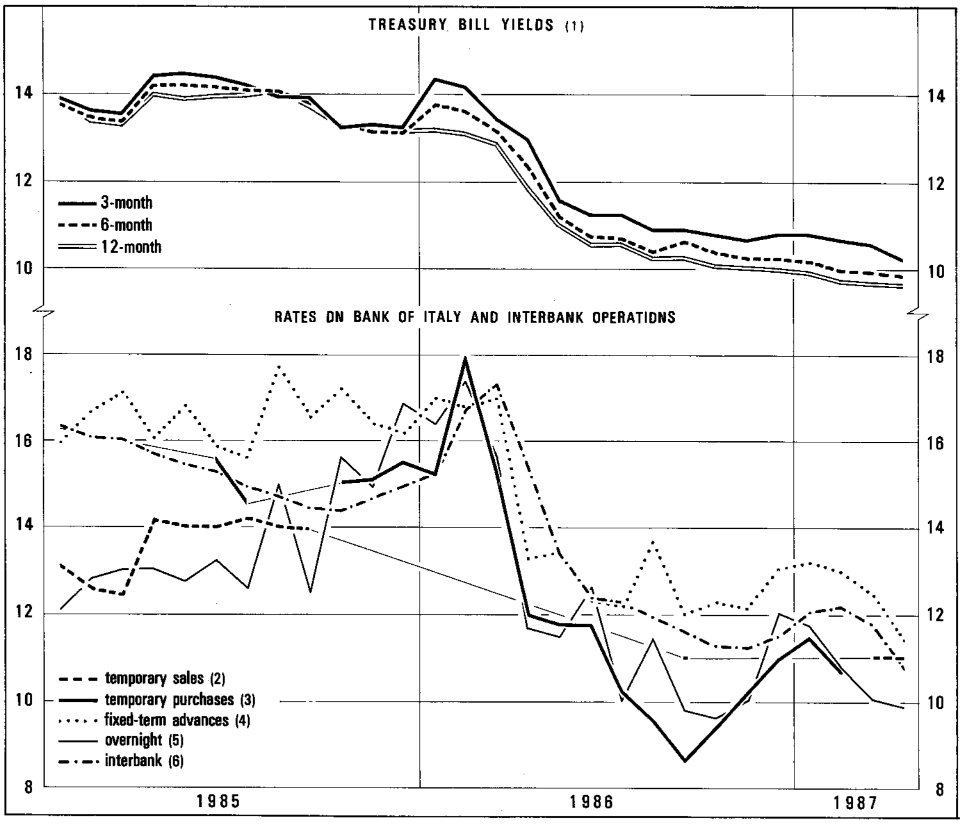
Monetary policy was tightened at the beginning of 1986 in view of the deepening of the currency crisis. Interest rates on lending by the Bank of Italy, which had already increased substantially since the previous October, continued to rise to peaks in excess of 18 per cent (Figure 11). In mid-January the measures to contain liquidity were reinforced by raising Treasury bill rates. The expansion in bank lending in lire was curbed by temporarily reintroducing the credit ceiling; coupled with certain exchange control restrictions, this halted the outflow of capital. Bank liquidity net of refinancing by the central bank turned sharply negative.

The successful defence of the lira's central rate within the European Monetary System dispelled uncertainty and brought a rapid improvement in the situation. In February and March the demand for government securities revived, especially for Treasury bonds, and the official reserves increased by more than 1.7 trillion lire. It thus became possible to ease conditions in the money market. The resumption of operations in the banks' centralized accounts also helped reduce the banking system's debt with the Bank of Italy; overnight rates fell to

15.6 per cent in March and those on securities repurchase agreements to 15.3 per cent. At the end of the month the improved money market conditions and the pronounced slowdown in inflation permitted a cut in the discount rate from 15 to 14 per cent.

Figure 11

SHORT-TERM INTEREST RATES



(1) Average yields at auction; compound interest, calendar year. Since September 1986 tax has been withheld on yields at the rate of 6.25 per cent. — (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.

Bank interest rates also declined and the downward trend continued in the second quarter; with inflation expected to continue to slow down sharply and with the balance of payments improving substantially, market interest rates came down further, encouraged at the end of April and in May by two more one-point reductions in the discount rate, bringing it to 12 per cent. Between March and June Treasury bill yields fell by about three percentage points; the pace of the reduction quickened after the realignment of EMS currencies in April. Issue yields on Treasury bonds and Treasury credit ce rtificates, which had continued to attract investor interest, came down by a similar amount.

Bank of Italy lending to the banking system contracted in April but expanded again in May, when purchases of government securities at issue exceeded the borrowing requirement, and especially in June, when demand for securities and the Treasury cash surplus of 4,411 billion lire caused pressures to develop in the money market.

Total purchases of government securities at issue by the market in the first half of the year came to almost 50 trillion lire, compared with a borrowing requirement of slightly more than 46 trillion. The annual rate of growth in monetary base, seasonally adjusted and after correction for the exceptional expansion in bank liquidity in late 1985, was 6.6 per cent, in line with the growth in deposits.

From the summer onwards, monetary control was made more difficult by fluctuations in market demand for government securities owing to the waning of expectations of a further reduction in interest rates. A particularly large contraction occurred in July, when there was net disinvestment in medium and long-term securities and total sales fell short of the borrowing requirement by more than 10 trillion lire. The resultant creation of liquidity was offset by reducing lending to the banking system by almost 7 trillion lire; despite the Bank's net subscriptions of securities totaling almost 4 trillion lire, the unused margin on the Treasury's overdraft facility contracted from 11,442 to 5,113 billion lire during the month.

In August the rates on Treasury bonds and ten-year Treasury credit certificates remained unchanged and sales picked up, though they still failed to meet the borrowing requirement. As a result, the scale of lending to the banking system and the rates of interest on such operations continued to decline; temporary sales of securities had to be made in the first half of September in order to control liquidity.

Two factors shaped developments towards the end of the year. The first was the introduction of withholding tax on income from government securities. The measure was accompanied by an increase in gross yields to ease the effect on investors and cushion the impact on Treasury financing.

The second factor, an acceleration in the monetary and credit aggregates, emerged ever more clearly as data became available, but the performance of the real economy offered no immediate explanation for the faster increase; the inflation trend was still downwards, the balance of payments continued to show good results and the indices of industrial output did not indicate an exceptionally strong expansion. The acceleration in deposit growth was due largely to businesses' decisions to adjust their financial portfolios, partly in view of the narrowing of the differential between yields on government securities and those on bank deposits, especially certificates of deposit; the increasing liquidity of the economy nonetheless gave rise to concern about the repercussions it might have on prices and the balance of payments.

The volume of temporary financing offered to the banking system was managed so as to cause a tightening of conditions in the money market, as reflected in an increase in the cost of such finance. The decline in yields on government securities resumed tentatively in September and October but halted again in November, when market demand weakened once more; in particular, subscriptions of Treasury bills were less than redemptions despite support from the group of banks participating in the bill auctions.

Demand for securities contracted further in December. In the second half of the year as a whole, net purchases of securities at issue by the market totaled 35.8 trillion lire, as against a borrowing requirement of more than 64 trillion. Monetary base increased at a seasonally adjusted annual rate of 9.3 per cent, reflecting the difficulties encountered in placing government securities and the acceleration in the growth of bank deposits. The change in expectations was confirmed by the particularly sharp fall in demand for convertible Treasury credit certificates.

The tighter money market conditions enabled the authorities to weather a brief spell of exchange rate pressure at the turn of the year, which was resolved by realigning EMS central rates in mid-January. After the realignment, the Bank of Italy provided the banks with ample financing to enable them to meet the reserve requirement on the increase in deposits in December and swiftly reduced the rates at which it was granted to close to the discount rate; the cost of temporary purchases of securities, which had risen from 12.3 per cent in mid-December to 13.6 per cent at the beginning of January, fell back to about 12 per cent at the end of the month.

Market interest in Treasury credit certificates revived in February. Issues were more than seven times oversubscribed both at the beginning of the month and at mid-month, when a lower interest rate was offered; applications did not reflect true market demand but represented attempts to minimize the effects of scaling-down. In the same month there was a large inflow of foreign currency generated by borrowing abroad by residents to take advantage of an interest rate differential in favour of foreign currency debt and by expectations of exchange rate stability following the realignment.

The increase in foreign exchange reserves in the first half of March, which coincided with a renewed weakening of demand for government securities, stimulated an expansion in bank liquidity and thus enabled the banks to repay their entire debt to the central bank. The growth in foreign currency lending in the first two months of the year, which was accompanied by a continued strong rise in bank lending in lire, caused credit to the non-state sector to increase at a rate likely to conflict with the objectives for 1987 and gave rise to concern about the possible repercussions of an acceleration in domestic demand on the balance of payments and on prices.

In such circumstances, the restrictive effects of a rise in domestic interest rates would normally have been blunted by greater inflows of capital. The introduction of the reserve requirement on banks' net external liabilities in foreign currencies in mid-month was designed to resolve this problem. At the same time, the differential between official rates and money market rates was reduced by half a point by lowering the discount rate to 11.5 per cent, following similar moves in other industrial countries. Inflows of foreign exchange ceased after the announcement of the measures; excess liquidity was mopped up by selling securities on the open market outright and under repurchase agreements.

The arrangements for issues of Treasury credit certificates were modified in April, as were those for Treasury bonds in May, in order to prevent a repetition of the speculative oversubscription of securities that had occurred in February. The "tap" issue method was chosen, whereby the terms are set in advance but not the issue volume, which is determined subsequently by the Treasury closing subscriptions at the end of the day on which the desired amount has been reached or exceeded; every application lodged before the close of subscriptions is accepted.

The current procedure for issuing government securities distinguishes between short-term securities, for which the tender system is used, and medium and long-term securities, which are issued mainly at predetermined interest rates; this makes it possible to stabilize the cost of Treasury borrowing at longer maturities while allowing any disparity between the actual and expected demand for securities to be transmitted to the yield curve via short-term rates. If this system is to operate effectively, the rates at which Treasury bills are allotted must be more flexible than is possible with the practice of fixing base rates close to market rates.

In April the Treasury borrowing requirement for the month was higher than expected; the market's purchases of securities at issue were not sufficient to absorb the resulting excess liquidity, which was exacerbated by inflows of foreign exchange, initially on a large scale. Demand for Treasury bonds and bills was particularly low by comparison with the amounts on offer except in the case of three-month bills; investor preference for shorter maturities seems to indicate greater uncertainty about future interest rate trends, partly owing to the halt in the slowdown of inflation.

The Bank of Italy intervened by selling securities under repurchase agreements and by making outright open market sales amounting to more than 4 trillion lire; some of the latter related to Treasury bonds issued at the beginning of the month.

BANKING

The demand for bank credit was sustained by the expansion in production and further strengthened in the second half of 1986 and the first few months of 1987 by a tendency for prime customers to borrow funds for financial investments. After the expiry of the ceiling on lending in June, banks satisfied the demand from such customers at rapidly declining interest rates close to those available in the money market. It was not until March 1987 that the expansion in credit began to slow down; in recent months lending in lire has been adversely affected by the decline in demand for credit by major borrowers and by the Bank of Italy calling on the major banks to curb the increase in their lending, while foreign currency loans have been checked by the introduction of reserve requirements on banks' net foreign currency positions.

Deposits expanded slowly in the first half of 1986, when the flow of savings to the stock market and investment funds was very heavy, but picked up in the last four months of the year as expectations of further reductions in interest rates and related capital gains on securities receded. Certificates of deposit grew at a particularly fast rate, owing not only to favourable market conditions but also to changes in the regulations aimed at broadening the banks' operational scope; the strong expansion in certificates of deposit carried over into 1987.

The fall in interest rates on bank loans and deposits was comparable to that in yields on government securities, a trend that continued during the first four months of 1987. In the credit market this tendency was coupled with a widening of the gap between the terms applied to major customers and those offered to other borrowers.

Lending

Overall bank lending rose by approximately 23.7 trillion lire in 1986, equal to 9.7 per cent of the amount outstanding at the end of 1985. The size of the increase was affected by the surge that had occurred in December 1985; calculated for the 12 months ending in November it works out at 12.4 per cent for 1986, compared with 11.3 per cent for 1985.

Lending to firms increased by approximately 16.8 trillion lire, or 8.2 per cent; for the twelve months ending in November 1986 the rate of increase was 11.2 per cent. Banks also provided finance to firms by purchasing shares and bonds worth approximately 2.7 trillion lire.

Lira lending continued to expand rapidly during the first two months of 1987; between December 1986 and February 1987 the three-month rate of increase, seasonally adjusted and on an annual basis, rose from 15.8 to 19.5 per cent. After the realignment of EMS central rates, foreign currency lending also increased by 2.3 trillion lire owing to the favourable differential over interest rates abroad. The acceleration in lending halted in March and April, principally on account of the behaviour of the lira component. The expansion worked out at 9.9 per cent over the first four months of 1987 as a whole.

Recent developments in bank lending. — The dependence of large firms on bank credit has been gradually reduced in recent years by increased self-financing, an improvement in their ability to raise funds directly in the capital market and by financial restructuring. The major industrial groups have kept down their borrowing per unit of output by establishing holding companies to even out financial imbalances between member companies and rationalize inventory management. They have also greatly reduced trade credit to smaller firms, thereby making them bear part of the cost of working capital. These innovations tend to reduce major companies' recourse to bank loans in the medium term, but accentuate its volatility in the short term, since this type of financing is being used increasingly to meet sudden expansions in production and to exploit opportunities for financial arbitrage at home and abroad.

The bargaining power of major firms vis-à-vis banks has increased, as can be seen from the rise in the number of credit lines per customer. Data from the Central Credit Register show that although the average for the system as a whole remained broadly unchanged between 1979 and 1986, that for prime customers increased from 14 to 19.

The same conclusions can be drawn from the ratio of credit used to credit granted; it began to fall in 1977 in the case of large loans but the overall ratio declined more noticeably between 1983 and 1986, owing partly to a reduction in borrowing by major firms but more to a particularly marked rise in facilities granted. The utilized portion of credit lines fell from 48 to 39 per cent in the case of customers with total borrowing of 30 billion lire or more and came down to 25 per cent in that of customers with over 200 billion lire in loans.

Deposits

In 1986 bank deposits rose by about 41 trillion lire, or 8.9 per cent, against 42 trillion, or 10.1 per cent, in 1985 (Table 27). Net of certificates of deposit, the increase was 32.8 trillion lire (7.4 per cent) against 36.4 trillion lire (8.9 per cent) in 1985.

Table 27

BANK DEPOSITS AND LOANS (1)

(percentage rates of increase)

	1982	1983	1984	1985	1986					1987 Ist quarter (5)
					Year	I qtr.	II qtr.	III qtr.	IV qtr.	
Deposits	18.2	13.3	11.6	10.1	8.9	4.5	8.5	8.9	15.5	6.3
Loans (2)	9.8	14.0	17.1	15.6	9.7	−7.9	15.5	17.0	17.0	11.2
Treasury bills (3)	43.0	−11.4	−7.7	−35.1	20.7	−63.5	118.1	94.1	37.1	−23.2
Medium & long-term securities (4)	18.8	30.4	12.0	18.3	4.5	9.6	5.4	−3.5	6.5	−4.1

(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 repurchase agreements with the Bank of Italy and operations under the Ministerial Decree of 27.9.1974. — (4) Net of the effect of the funding of bank loans, repurchase agreements with the Bank of Italy and operations under the Ministerial Decree of 27.9.74. — (5) Provisional.

During the first eight months of the year deposits expanded slowly, at an annual rate of 6.3 per cent. This was due both to tight control of monetary base and to the public's growing preference for government securities and investment fund units. The development of new types of savings instruments limited the growth in the portion of bank deposits held primarily as a store of value. In August the 12-month rate of growth in current account deposits was 9.5 per cent, against 2.6 per cent in savings deposits, including certificates of deposit.

During the last four months of 1986 the annualized expansion in total deposits rose to 15.6 per cent, reflecting on the one hand the fall in share prices, which caused investment funds to lose some of their glamour, and on the other to the fading of expectations of capital gains on securities, which made government stock more difficult to sell. The faster growth may have been stimulated in part by the introduction of withholding tax on interest from government securities in September; another factor was the narrowing of more than one and a half percentage points in the differential, net of tax, between yields on government securities and those on deposits.

Almost one third of the growth in deposits in the last four months of the year was due to a revival of interest in certificates of deposit.

The expansion in such instruments was even stronger in early 1987, by which time other forms of deposit were increasing less rapidly; in the first four months of this year the volume of CDs in circulation rose by approximately 8.5 trillion lire, against 2.9 trillion in the same period of 1986.

Notwithstanding the strong expansion in CDs in the last few months of 1986, current account deposits increased as a proportion of total bank deposits last year, thus confirming the trend of the last ten years, during which they have risen from 51 to 55 per cent of the total.

Figures on the number of current accounts per head, their average size and their turnover rate (Table 28) show that this form of deposit is serving increasingly as a liquidity reserve rather than as a financial investment, as it had in the seventies. The main factor that had previously prevented the banks from offering differentiated yields on the various types of deposit is thus vanishing.

Table 28

PAYMENT SERVICES AND BANKING OPERATIONS

	Demand deposits as percentage of total		Number of demand deposits per 100 inhabitants	Average size of demand deposits (millions of lire)	Bank payment operations per inhabitant (2)	Turnover rate (2) (3)
	Italy	Abroad (1)				
1977	51.0	35.3	16.6	22.3	....	....
1980	54.6	32.8	20.9	21.3	....	....
1983	53.4	31.5	22.8	16.6	10.9	12.4
1986	54.8	32.2 (4)	26.6	15.4	12.1	14.9

Source: Bank of Italy, IMF and CIPA survey.
(1) Average of figures for France, Germany, the United Kingdom and the United States. — (2) For banks included in the CIPA survey. — (3) Ratio between total volume of funds transferred during the year and average balance in demand deposits over the same period. — (4) Figure for 1985.

The banks' role in the payment system. — The expanding and more exacting demand for payment services by all sectors of the economy and the spread of savings instruments as alternatives to deposits have greatly increased the importance of payment services as a part of banking activities. Moreover, technological and financial innovation has led to the introduction of new products and the entry of new operators into a field traditionally dominated by the banks. It is thus increasingly important for the banks to offer a wide range of high quality payment services both in order to maintain their market shares and to participate in the process of financial diversification that is taking place in Italy.

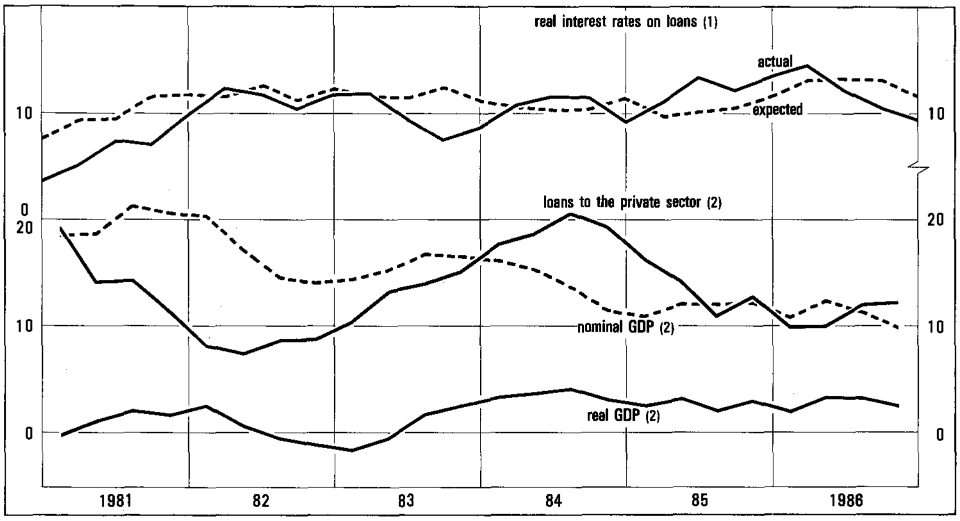
The report on the Italian payment system recently published by the Bank of Italy identifies a number of inadequacies in the provision of bank payment services that help to explain the high incidence of cash transactions. It was found that some bank payments take longer to execute in Italy than in other countries and that banks' scales of charges do not encourage the use of payment instruments that may be more efficient. In order to improve the functioning of the payment system, the report sets out a detailed programme of measures affecting all the institutions providing payment services.

Interest rates

Between December 1985 and December 1986 the average interest rate on lira loans fell by 2.9 percentage points and that on deposits by 2.5 points; the rate on foreign currency loans declined by 1.2 percentage points, closely following the movement in the cost of fund-raising in the international market. These reductions, the largest for ten years, were close to those in money market rates. The real lending rate also fell by almost 2 points during the year, offsetting the 1985 rise caused by the pronounced slowdown of inflation (Figure 12). The real rate on deposits, net of tax, declined by a similar amount.

Figure 12

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.

During the first few months of 1986 the fall in lending rates was held back by the effects of the ceiling on lending, so that the differential between the lira lending rate and the average yield on Treasury bills rose by 1.8 percentage points in the first half of the year.

During the same period the proportion of loans granted at rates not exceeding the ABI prime rate contracted sharply from 43 to 24 per cent; the differential between the average lending rate and the prime rate thus widened.

The decline in lending rates that had already begun in the second quarter in the wake of the three reductions in the discount rate between March and May gathered momentum after the expiry of the credit ceiling.

The downward trend continued in the first four months of 1987, when average bank rates fell by around half a point. By the end of April almost all deposit and lending rates for prime customers had responded to the half-point adjustment in the discount rate in March.

Deposit rates followed the movement in money market rates more closely than did lending rates. Despite the rapid decline in money market rates, the differential between Treasury bill rates and deposit rates narrowed less markedly than in previous cycles.

Profit and loss accounts

Banks' net interest income, the difference between interest income and interest expenses, rose from 3.24 to 3.45 per cent of total resources (Table 29), mostly as a result of the expansion in lira loans from 31.8 to 33.4 per cent of total interest-bearing funds. A more modest contribution came from the widening of the differential between average yields on securities portfolios and the unit cost of deposits as a result of the maturing of bonds purchased at low nominal rates. The margin between the average yield on loans and the unit cost of deposits remained stable year on year, rather than declining as it did on previous occasions when market rates fell. This reflected the stringency of the credit ceiling in the early months of the year; until May the average lending rate was higher than at the end of 1985.

Banks' non-interest income rose from 1.29 to 1.40 per cent of total resources. Profits from securities trading increased from 0.69 to 0.77 per cent; within this item the most noticeable increase was in commissions for the placement of new issues, which rose at twice the rate of other trading profits as a result of substantial sales of investment fund units to the public.

The expansion in the provision of services, which are highly labour intensive, contributed to a slight increase in operating expenses from 3.03 to 3.06 per cent of total resources. Staff costs rose from 2.18

Table 29

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

	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986 (2)
	As a percentage of total resources									
Net interest income	**3.21**	**2.92**	**2.75**	**3.46**	**3.54**	**3.30**	**3.37**	**3.36**	**3.24**	**3.45**
Non-interest income	**0.94**	**0.98**	**0.95**	**1.00**	**1.23**	**1.27**	**1.19**	**1.28**	**1.29**	**1.40**
securities trading	*0.34*	*0.46*	*0.45*	*0.44*	*0.56*	*0.66*	*0.55*	*0.66*	*0.69*	*0.77*
Gross income	**4.15**	**3.90**	**3.70**	**4.46**	**4.77**	**4.57**	**4.56**	**4.64**	**4.53**	**4.85**
Operating expenses	2.91	2.78	2.72	3.01	2.95	2.97	3.15	3.15	3.03	3.06
staff costs	*2.21*	*2.08*	*1.99*	*2.20*	*2.14*	*2.06*	*2.31*	*2.27*	*2.18*	*2.20*
Net income	**1.24**	**1.12**	**0.98**	**1.45**	**1.82**	**1.60**	**1.41**	**1.49**	**1.50**	**1.79**
Allocations to provisions (net)	0.87	0.76	0.69	0.99	1.30	0.99	0.72	0.71	0.67	0.66
for loan losses	*0.37*	*0.37*	*0.33*	*0.44*	*0.44*	*0.46*	*0.43*	*0.39*	*0.32*	*0.29*
Extraordinary income and withdrawals from provisions for loan losses	0.01	—	0.04	0.01	0.03	0.08	0.03	0.02	0.07	0.01
Profit before tax	**0.38**	**0.36**	**0.33**	**0.47**	**0.55**	**0.69**	**0.72**	**0.80**	**0.90**	**1.14**
Tax	0.21	0.19	0.14	0.24	0.27	0.40	0.43	0.44	0.47	0.61
Net profit	**0.17**	**0.19**	**0.19**	**0.23**	**0.28**	**0.29**	**0.29**	**0.36**	**0.43**	**0.53**
	Other data									
Total resources *(billions of lire)*	208,183	250,435	307,772	372,503	441,537	507,235	591,493	662,436	771,837	838,517
Number of employees	239,901	249,999	261,505	274,889	287,420	293,002	299,879	302,814	304,090	307,122
Total resources per employee *(millions of lire)*	868	1,002	1,177	1,355	1,536	1,755	1,998	2,215	2,538	2,730
Staff costs *(millions of lire)*	19.2	20.8	23.4	29.8	32.8	36.1	46.2	50.2	55.4	60.0
	Percentage rates of increase									
Staff costs	6.7	8.3	12.5	27.8	9.7	13.2	28.0	8.7	10.0	8.3
Total resources per employee:										
in nominal terms	16.5	15.4	17.5	15.1	13.4	14.3	14.0	10.7	14.6	7.6
in real terms (3)	– 1.3	2.7	1.5	– 5.0	– 4.5	– 1.8	– 1.0	0.3	5.5	1.4
Number of employees	5.5	4.2	4.6	5.1	4.6	1.9	2.3	1.0	0.4	1.0

(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) Provisional data. — (3) Deflated using the cost-of-living index.

to 2.20 per cent. However, the 1 per cent increase in staff numbers was accompanied by a rise in total resources per employee of 1.4 per cent at constant prices, a significant increase even after the exceptional 5.5 per cent rise in 1985.

Net income rose from 1.50 to 1.79 per cent of total resources; provisions remained stable at levels below the average for the last ten years on account of reduced risks of capital losses on holdings of securities. Withdrawals from provisions for loan losses fell back to very low levels, after increasing sharply in 1985 owing to special factors. Gross and net profits thus expanded considerably to respectively 1.14 and 0.53 per cent of total resources, much higher levels than recorded in the past.

THE SPECIAL CREDIT INSTITUTIONS AND LEASING AND FACTORING COMPANIES

The special credit institutions

The recovery in lending by special credit institutions that had begun in late 1985 accelerated last year, fueled by the upturn in investment, the reimposition of the ceiling on bank lending in the first half of the year, and the buoyant demand for credit for financial purposes. With inflation slowing down markedly, domestic lending by the institutions expanded by 12.4 per cent, nearly four percentage points more than it had in 1985 (Table 30).

Table 30

DOMESTIC LENDING BY THE SPECIAL CREDIT INSTITUTIONS

(percentage changes)

	1982	1983	1984	1985	1986
Industrial	19.9	9.6	12.0	9.3	14.6
short-term	*32.2*	*−2.7*	*34.6*	*33.4*	*58.4*
Public works	18.9	32.2	22.9	3.2	0.8
Real estate	14.5	14.3	(2) 13.2	9.6	13.1
Agriculture	14.4	(1) 13.2	(2) 12.6	8.2	12.7
Total . . .	**17.9**	(1) **13.4**	(2) **13.6**	**8.5**	**12.4**

(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; not taking it into account, 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 brisk growth of private investment in 1985 was fully reflected in the volume of intermediation by the special credit institutions in 1986. As a consequence of the ceiling on bank lending, there was a very sharp increase in special credit in the first five months, followed by a slowdown in the summer. From September to the end of the year there was another fairly strong expansion, partly as a result of loans to finance the purchase of blocks of shares.

Lending rates remained relatively stable in the first half of the year, despite lower yields on government securities and reduced fund-raising costs to the institutions. In the second half, stiffer competition from banks prompted a lowering of rates in line with those on bank loans. The industrial credit institutions cut their medium and long-term lending rates by 2.9 percentage points in the course of the year and their short-term rates by 2.7 points. As a result, their interest margin on new lending widened in the first half of the year and narrowed in the second.

In the first four months of 1987 the institutions' lending decelerated slightly, so that by the end of April the twelve-month rate of expansion was about 10.5 per cent. As part of the policy of encouraging competition between credit intermediaries, the residual securities investment requirement for banks was not renewed for 1987, and the obligation to maintain the volume of securities previously purchased under the requirement was also removed. Gross bond issues did not suffer, rising sharply to 4,284 billion lire in the first quarter as against 2,812 billion in the same period of 1986.

Lending

Domestic lending by the special credit institutions expanded by 16,825 billion lire, as against 10,688 billion in 1985. The sections for public works credit did not share in this recovery; indeed, their lending growth was smaller than the very slight expansion of 1985. This was reflected in the slow growth of credit to the public sector, which increased by a total of 590 billion lire, or 2.5 per cent, as against 771 billion, or 3.4 per cent, in 1985.

Bad debts increased by 16.1 per cent, a slower rate than in the recent past (25.5 per cent in 1985 and 26.6 per cent in 1984). For the industrial credit institutions, the slowdown from 16.2 per cent in 1985 to 6.9 per cent was due to developments in the leading institutions, whose bad debt provisions diminished, in part because a number of loans were written off. The rate of increase for the smaller institutions remained high, though lower than in 1985.

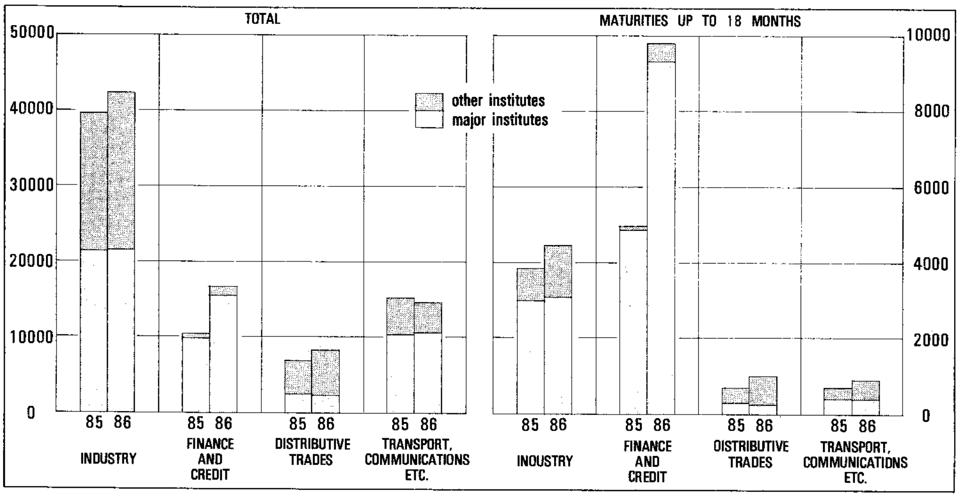
Credit to industry and the services sector. — Half of the increase of 10,567 billion lire in the industrial credit institutions' domestic lending consisted of disbursements to financial companies (Figure 13), much of it in short-term loans and almost all by the leading institutions.

Lending by the smaller industrial credit institutions, which goes chiefly to small and medium-sized industrial firms, expanded by 17.2 per cent. In particular, lending by regional credit institutions and the special credit sections of public-law banks increased by 19 and 22 per cent respectively. This rapid growth, which here too was marked in short-term loans, appears to have been due only partly to the ceiling on bank lending. There was a very sharp increase in short-term subsidized loans using streamlined application procedures, especially in the North.

Figure 13

DOMESTIC LENDING OF THE INDUSTRIAL CREDIT INSTITUTIONS BY SECTOR

(amounts in billions of lire)



Excluding export credit, subsidized lending expanded very strongly. The increase in such credit to the services sector was particularly rapid, largely because of higher lending to commercial firms (Table 31). Subsidized industrial credit also grew substantially, though at a slightly slower rate than in 1985; its growth was particularly impressive in comparison with that of unsubsidized special credit to industry.

Credit for housing. — After years of declining growth rates, housing credit extended by the special credit institutions recovered sharply last year, rising by 4,237 billion lire, or 14.8 per cent, as against 2,511 billion, or 9.6 per cent, in 1985 (Table 31). The main cause of the acceleration was a sharp reduction of more than 3 percentage points in interest rates. The expansion was most marked in the second half of the year and continued during the early months of 1987. The twelve-month growth rate of lending by real estate and housing institutions increased from 12.7 per cent in December to 14.5 per cent in April.

Table 31

DOMESTIC LENDING BY THE SPECIAL CREDIT INSTITUTIONS BY SECTOR

(in billions of lire)

	Agriculture		Housing		Industry		Transport, communications, misc. services		Exports		Total	
	1985	1986	1985	1986	1985	1986	1985	1986	1985	1986	1985	1986
	Disbursements											
Subsidized . . .	3,747	4,440	1,010	1,437	4,567	5,576	1,183	1,772	1,350	604	11,857	13,829
Unsubsidized .	2,019	2,247	3,209	5,082	8,591	9,764	12,235	19,100	—	—	26,054	36,193
Total . . .	**5,766**	**6,687**	**4,219**	**6,519**	**13,158**	**15,340**	**13,418**	**20,872**	**1,350**	**604**	**37,911**	**50,022**
	Net increase in lending											
Subsidized . . .	743	1,240	967	1,209	2,342	2,345	829	1,199	−693	−1,265	4,188	4,728
Unsubsidized .	344	448	1,544	3,028	615	1,306	3,997	7,315	—	—	6,500	12,097
Total . . .	**1,087**	**1,688**	**2,511**	**4,237**	**2,957**	**3,651**	**4,826**	**8,514**	**−693**	**−1,265**	**10,688**	**16,825**
	Percentage increase in lending											
Subsidized . . .	*9.3*	*14.2*	*16.3*	*17.5*	*17.5*	*14.9*	*20.7*	*24.8*	*− 10.3*	*−20.8*	*11.0*	*11.2*
Unsubsidized .	*13.4*	*15.4*	*7.6*	*13.9*	*2.6*	*5.3*	*9.8*	*16.4*	—	—	*7.4*	*12.9*
Total . . .	***10.3***	***14.5***	***9.6***	***14.8***	***7.9***	***9.1***	***10.8***	***17.2***	***− 10.3***	***−20.8***	***8.5***	***12.4***

The demand for home loans is particularly sensitive to nominal interest rates. The practice of stipulating fixed-instalment repayments meant that the sharp rise in nominal rates in the seventies significantly raised the borrowing "threshold", defined as the ratio of the instalment to the borrower's income. The decline in interest rates in 1986 has once again made home loans accessible to large numbers of households.

Export credit. — The export credits of the special credit institutions contracted for the second consecutive year, registering a decline of 1,846 billion lire following one of 1,364 billion in 1985. The reduction in interest rate incentives and the change in the pattern of Italy's exports were significant factors in the downturn; exports to countries outside Europe have declined whereas those to members of the EEC, which do not enjoy credit subsidies, have increased. The troubles of many developing countries have not only held down the demand for export credit in line with export trends but at the same time have heightened lending risks and reduced the availability of credit.

Agricultural credit

Agricultural lending accelerated in 1986. At the end of the year outstanding credit amounted to 21,221 billion lire (Table 32), 15.7 per cent higher than at the end of 1985, as against an expansion of 8.4 per cent the previous year. This was faster than the average for overall lending by the credit system, so that the share of agricultural credit in total lending to the non-state sector recovered after two years of decline.

Table 32

LENDING BY THE AGRICULTURAL CREDIT SYSTEM

(billions of lire)

	Agricultural special credit institutions			Other authorized institutions			General total		
	Sub-sidized	Unsub-sidized	Total	Sub-sidized	Unsub-sidized	Total	Sub-sidized	Unsub-sidized	Total
	Disbursements in 1985								
Working credit	**2,872**	**1,396**	**4,268**	**4,197**	**2,722**	**6,919**	**7,069**	**4,118**	**11,187**
Improvement credit	**543**	**403**	**946**	**128**	**36**	**164**	**671**	**439**	**1,110**
	Disbursements in 1986								
Working credit	**3,381**	**1,571**	**4,952**	**5,130**	**2,982**	**8,112**	**8,511**	**4,553**	**13,064**
Current expenditure	2,329	1,059	3,388	3,878	2,147	6,025	6,207	3,206	9,413
Purchases of livestock	45	109	154	87	101	188	132	210	342
Purchases of machinery	114	119	233	256	209	465	370	328	698
Advances against agricultural products	29	5	34	150	31	181	179	36	215
Loans to agricultural agencies and cooperatives	864	279	1,143	759	494	1,253	1,623	773	2,396
Improvement credit	**632**	**457**	**1,089**	**235**	**92**	**327**	**867**	**549**	**1,416**
Rural construction	147	135	282	23	39	62	170	174	344
New plantings	19	6	25	5	1	6	24	7	31
Irrigation	11	3	14	3	—	3	14	3	17
Soil preparation	4	45	49	—	1	1	4	46	50
Expansion of holdings	88	62	150	28	5	33	116	67	183
Other improvements	363	206	569	176	46	222	539	252	791
	Outstanding credit at end-1986								
Working credit	**3,936**	**1,322**	**5,258**	**5,334**	**2,034**	**7,368**	**9,270**	**3,356**	**12,626**
Improvement credit	**5,463**	**1,748**	**7,211**	**1,174**	**210**	**1,384**	**6,637**	**1,958**	**8,595**
Total	**9,399**	**3,070**	**12,469**	**6,508**	**2,244**	**8,752**	**15,907**	**5,314**	**21,221**

Working credit expanded faster than overall agricultural credit, its pace accelerating from 6.8 per cent in 1985 to 17.6 per cent last year, thanks to rapid growth in subsidized lending, which increased by 19.1 per cent. This was a consequence of a reduction in the cost of credit and the availability of ample public funds for interest subsidies. The minimum subsidized credit rates (which had remained unchanged since 1982, at rates ranging from 7.0 to 11.75 per cent, depending on purpose) were lowered substantially during the year; in November and December they ranged from 3.8 to 7.6 per cent.

Interest rates on unsubsidized loans also declined significantly, although they were still high in real terms. Relending the net proceeds from discounting bills with the Bank of Italy continued to have a damping effect on the cost of unsubsidized loans. The volume of agricultural bills discounted by the Bank at the regulation rate (6.5 per cent from May onwards) was 1.1 trillion lire, about the same as in 1985.

Improvement credit expanded less rapidly. Outstanding loans at the end of the year amounted to 8,595 billion lire, an increase of 12.8 per cent as against one of 10.8 per cent in 1985. The increase appears more substantial when compared with the modest growth in capital formation in the farm sector. The ratio of special credit disbursements to overall agricultural investment rose from 8 to 10 per cent. Only in part, however, did this represent greater recourse to subsidized credit to meet investment costs as a result of interest rate reductions comparable to those for working credit, since a greater share of agricultural credit than in 1985 went to projects outside farming proper, such as investment in food processing, as reflected in the significant increase in the item "other improvements" (Table 32). Unsubsidized lending also increased substantially, mainly on account of loans financed by borrowing abroad under government exchange guarantees.

The slowdown in inflation, which was particularly pronounced in the agricultural sector, made it difficult for many farmers to service their debt. The bad debts of the agricultural credit institutions continued to soar, rising by 35.7 per cent, and early repayments were substantial.

Fund-raising and the management of securities portfolios

The special credit institutions' fund-raising from their principal sources increased more slowly than their lending in 1986. Despite an appreciable expansion in their capital, their holdings of government securities therefore decreased for the first time since the beginning of the eighties.

The progressive easing of the securities investment requirement on banks in recent years, which related only to fixed rate securities, helped stimulate a restructuring of liabilities in 1986, with a shift to floating rate securities. This was most marked in the case of non-industrial credit institutions, but was somewhat attenuated by growing expectations of lower interest rates. Bond issues expanded by 7,171 billion lire, compared with 5,468 billion in 1985, a significant proportion consisting of convertible issues and bonds with warrants, which increased by 2,664 billion lire. The rest of the expansion in bond issues was more or less equally divided between fixed rate issues (2,060 billion lire, compared with 2,770 billion in 1985) and floating rate and index-linked issues (2,447 billion as against 2,077 billion in 1985).

The bond issues of the industrial credit institutions were subscribed principally by non-banks, whereas those of the real estate and agricultural institutions were taken up mostly by banks (Table 33). This pattern depended only partly on the securities investment requirement, which in the second half of the year merely obliged banks not to reduce their holdings of eligible securities. The removal of the requirement will encourage more competitive methods of fund-raising by all types of special credit institution.

Table 33

CONTRIBUTION OF BANKS TO FUND-RAISING BY THE SPECIAL CREDIT INSTITUTIONS (1)

(percentages)

Type of institution	Stocks				Flows		
	1983	1984	1985	1986	1984	1985	1986
Industrial	40.4	35.8	33.5	29.3	−6.8	6.5	−11.6
Public works	60.5	55.7	50.7	49.2	33.3	−17.3	—
Real estate	64.8	61.3	60.2	58.7	8.0	49.5	44.9
Agricultural	68.7	65.5	57.3	60.0	51.8	−31.5	88.1
Total	**50.6**	**46.4**	**43.7**	**40.9**	**10.6**	**13.4**	**10.9**

(1) Includes banks' subscriptions of bonds (net of those bought in operations on behalf of the Treasury), medium-term deposits, short-term financing and participations in the institutions' capital. Fund-raising does not include compensatory loans from the central bank.

Issues of certificates of deposit expanded by 2,709 billion lire, as against growth of 2,069 billion in 1985. The increase was fastest among the smaller industrial credit institutions, which used the funds raised to finance their short-term lending.

Fund-raising abroad amounted to 1,828 billion lire, mostly in loans from the European Investment Bank, which came to about 1,200 billion lire during the year, net of repayments. At the end of the year foreign loans enjoying government exchange guarantees, most of which came from the EIB, accounted for about 60 per cent of the special credit institutions' outstanding foreign borrowing, which was valued at 21,878 billion lire.

The reduction in the tax advantages of government securities, which was carried a step further with the measures adopted in September 1986, affected the institutions' holdings of such securities, which contracted from 16,441 billion lire at the end of 1985 to 14,511 billion a year later.

Profit and loss accounts

The general decline in nominal interest rates affected the lending and borrowing rates of the special credit institutions, although its impact was softened by the continuing large share of fixed rate medium and long-term loans in their balance sheets.

Net interest income as a percentage of total resources remained virtually unchanged at 3.06 per cent, as against 3.04 per cent in 1985 (Table 34), despite the favourable terms the institutions obtained on new lending in the first half of the year and an increase in dividends on shares and participations, which for the first time in years made an appreciable contribution to income.

The institutions' gross income differed significantly from their net interest income for the first time in a decade, thanks to the significant contribution of non-interest income (0.14 per cent of total resources). In particular, there was a notable rise in income from securities transactions, generated not only by capital gains on government securities and bonds but also by share issues.

Operating costs as a percentage of total resources continued their long-term upward trend, rising from 0.84 to 0.88 per cent, owing in part to staff costs, which increased despite a reduction in the number of employees. Staff costs per employee rose by 13.9 per cent, as in 1985. Consequently, net income was broadly in line with the results of the last five years. Depreciation and allocations to provisions were smaller (1.15 per cent of total resources as against 1.28 per cent in 1985), thanks in part to the slower increase in bad debts, so that profit before tax rose sharply, from 1.09 to 1.37 per cent of total resources.

Despite a rise in the incidence of tax on total resources from 0.41 to 0.56 per cent, which reflected the reduction in the tax advantage on government securities and other factors, net profit increased from 0.68 to 0.81 per cent of total resources and from 7.2 to 7.8 per cent of capital and reserves.

Table 34

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

	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986 (1)
	As a percentage of total resources									
Interest income	9.51	10.43	10.97	11.76	12.91	14.41	14.72	14.80	14.22	13.46
Interest expenses	7.62	8.18	8.57	9.03	10.00	11.40	11.63	11.66	11.18	10.40
Net interest income	**1.89**	**2.25**	**2.40**	**2.73**	**2.91**	**3.01**	**3.09**	**3.14**	**3.04**	**3.06**
Non-interest income	0.03	−0.01	−0.02	0.03	0.01	−0.05	−0.05	0.02	0.01	0.14
Gross income	**1.92**	**2.24**	**2.38**	**2.76**	**2.92**	**2.96**	**3.04**	**3.16**	**3.05**	**3.20**
Operating expenses	0.42	0.44	0.49	0.61	0.66	0.73	0.77	0.82	0.84	0.88
staff costs	*0.33*	*0.34*	*0.37*	*0.44*	*0.44*	*0.44*	*0.48*	*0.50*	*0.52*	*0.54*
Net income	**1.50**	**1.80**	**1.89**	**2.15**	**2.26**	**2.23**	**2.27**	**2.34**	**2.21**	**2.32**
Depreciation & allocations to provisions	1.01	1.42	1.49	1.82	1.71	1.36	1.41	1.46	1.28	1.15
Extraordinary income and expenditure	0.03	0.24	0.05	0.09	0.16	0.13	0.24	0.17	0.16	0.20
Profit before tax	**0.52**	**0.62**	**0.45**	**0.42**	**0.71**	**1.00**	**1.10**	**1.05**	**1.09**	**1.37**
Tax	0.29	0.41	0.24	0.24	0.32	0.42	0.39	0.42	0.41	0.56
Net profit	**0.23**	**0.21**	**0.21**	**0.18**	**0.39**	**0.58**	**0.71**	**0.63**	**0.68**	**0.81**
	Other data									
Total resources *(billions of lire)*	72,138	79,500	84,775	91,890	104,073	124,146	141,254	158,815	176,805	189,746
Number of employees	8,664	8,926	9,990	10,318	10,654	11,130	11,840	12,045	12,109	11,948
Total resources per employee *(millions of lire)*	8,326	8,907	8,486	8,906	9,768	11,154	11,930	13,185	14,601	15,881
Staff costs per employee *(millions of lire)*	27.35	29.91	31.23	39.64	43.18	49.06	56.93	66.17	75.40	85.87
	Percentage rates of increase									
Staff costs per employee	10.9	9.4	4.4	26.9	8.9	13.6	16.0	16.2	13.9	13.9
Total resources per employee:										
in nominal terms	3.9	7.0	−4.7	4.9	9.7	14.2	7.0	10.5	10.7	8.8
at constant prices (2)	−12.0	−4.9	−17.7	−13.4	−7.6	−1.9	−7.0	−0.1	2.0	2.5

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

Leasing and factoring companies

Leasing and factoring companies, whose activities for the most part complement those of the banks and special credit institutions but occasionally compete with them, last year strengthened their position among intermediaries engaged chiefly in the financing of industry. The net flow of credit from companies included in the periodic surveys by the Bank of Italy amounted to 3.8 trillion lire in 1986 as against 3.2 trillion in 1985. The expansion was slower in the first half than in the second, which suggests that these companies were affected by the restrictions on bank lending, since they rely on the banks for finance. This dependence aids the rapid transmission of monetary stringency, but at the same time it heightens the risk that solvency problems among these new intermediaries, which are not subject to specific regulation, will have direct repercussions on the credit system.

Leasing companies. — Leasing business continued to expand at a brisk pace, though less rapidly than in 1985. The value of contracts signed by the companies covered by the Bank of Italy survey was 8.1 trillion lire (the estimate for all leasing companies was approximately 10 trillion lire), an increase of 29 per cent, as against one of 32 per cent in 1985 (Table 35). Despite this slightly slower growth, which was consistent with the deceleration in investment, the ratio of leasing contracts to investment in machinery, equipment and transport equipment rose further from 5.8 to 7.0 per cent.

Table 35

LEASING (1)

(amounts outstanding in billions of lire)

	1984	1985	1986
Finance provided (2)	4,732	6,269	8,100
Finance received from credit institutions	4,055	5,378	7,197
short-term lira loans	*1,778*	*3,242*	*4,808*
medium and long-term lira loans	*2,167*	*1,838*	*2,091*
foreign currency loans	*110*	*298*	*298*

(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.

The leasing companies' business grew faster than that of the industrial credit institutions, faster even than that of the most dynamic of these, namely the regional credit institutions, whose loans are the closest substitutes for leasing contracts. Though higher than in 1985, the average value of such contracts was still only about 40 million lire.

The expansion in leasing business was due in part to interest rates. The cost of leasing decreased more sharply than that of finance from other types of intermediary — about 4 percentage points as against 3 in the case of industrial credit institutions. This faster reduction implies a squeezing of the interest margin for leasing companies, since bank and special credit lending rates represent the cost of funds to them.

Finance from the credit system, which provides the bulk of the leasing companies' funds, expanded sharply (34 per cent). Medium-term credit recovered after the decline of 1985, but the rate of growth remained modest, only 14 per cent compared with the 48 per cent increase in short-term borrowing. If the distortions caused by the flat-rate withholding tax on medium and long-term loans from credit intermediaries were eliminated, the leasing companies could achieve a better maturities balance in their resources.

Factoring companies. — Strong demand for credit from medium-sized and small industrial and commercial enterprises continued to be the mainspring in the expansion of factoring, which grew substantially last year, though less rapidly than in 1984 and 1985.

Claims assigned to the factoring companies surveyed by the Bank of Italy, which constitute some 90 per cent of the factoring market, totaled 9,403 billion lire at the end of the year (Table 36); the growth rate worked out at 30.3 per cent, as against 46 per cent in each of the two previous years. As in the past, most of the expansion occurred in the last quarter.

Table 36

FACTORING

(amounts outstanding in billions of lire)

	Factoring companies by banks controlled			Other			Total		
	1984	1985	1986	1984	1985	1986	1984	1985	1986
Claims acquired	3,196	4,580	5,858	1,762	2,637	3,545	4,958	7,217	9,403
Finance provided	1,974	2,865	4,006	1,573	2,393	3,195	3,547	5,258	7,201
Finance received from credit institutions	1,720	2,477	3,260	1,342	2,026	2,642	3,062	4,503	5,902
short-term lira loans	*1,394*	*2,244*	*3,085*	*997*	*1,707*	*2,228*	*2,391*	*3,951*	*5,313*
medium and long-term lira loans	*262*	*147*	*101*	*345*	*266*	*359*	*607*	*413*	*460*
foreign currency loans	*64*	*86*	*74*	—	*53*	*55*	*64*	*139*	*129*
Number of companies covered by the survey	20	21	21	12	14	14	32	35	35

The volume of finance provided by the factoring companies increased by 37.0 per cent, faster than the growth in acquired claims, to stand at 7,201 billion lire at the end of 1986. The strongest expansion (39.8 per cent) was achieved by bank-controlled companies, which were more aggressive, especially in the second half of the year. The ratio of these companies' lending to assigned claims rose from 62.6 to 68.4 per cent but remained well below that for other factoring companies, which was 90.1 per cent at the end of 1986.

The factoring companies' interest margin remained virtually unchanged, with both lending rates and the cost of borrowing from the banks declining by about 3 percentage points.

The factoring companies continued to finance their operations by borrowing from the credit system; funds from this source expanded by 31 per cent to 5,902 billion lire at the end of the year. The high liquidity of the major industrial groups that control some of the factoring companies permitted an increase in financing from non-bank shareholders from 314 billion lire at the end of 1985 to 563 billion a year later.

INSTITUTIONAL INVESTORS

The consolidation of the general improvement in the economy and the development of the financial market increased savers' propensity to invest in securities. The rise in share prices and the desire of households to diversify their financial assets interacted with the growth in investment funds, while the increased demand for supplementary pension schemes from firms and individuals was reflected in the strong expansion in the business of life insurance companies.

Institutional investors and investment management services attracted savings totaling 58 trillion lire in 1986.

The largest expansion was recorded by Italian investment funds, especially in the first few months of the year. By the end of 1986 their net assets had risen to more than 65 trillion lire as a result of net fund-raising of 37.5 trillion and capital gains of 7.8 trillion, net of profits distributed to unit-holders; the net assets of foreign investment funds increased by 3.2 trillion lire, owing entirely to capital gains.

Insurance companies increased their technical reserves from 28.6 to 34.7 trillion lire, net of reinsurance commissions; most of the growth occurred in the life insurance sector.

Investment management business expanded strongly last year, with managed assets rising from 27.3 to 47 trillion lire.

Investment funds

The net assets of Italian investment funds tripled in 1986, rising from 19.8 to 65.1 trillion lire, and the number of new accounts increased almost fourfold. Net fund-raising came to 37.5 trillion lire, more than twice the figure for 1985.

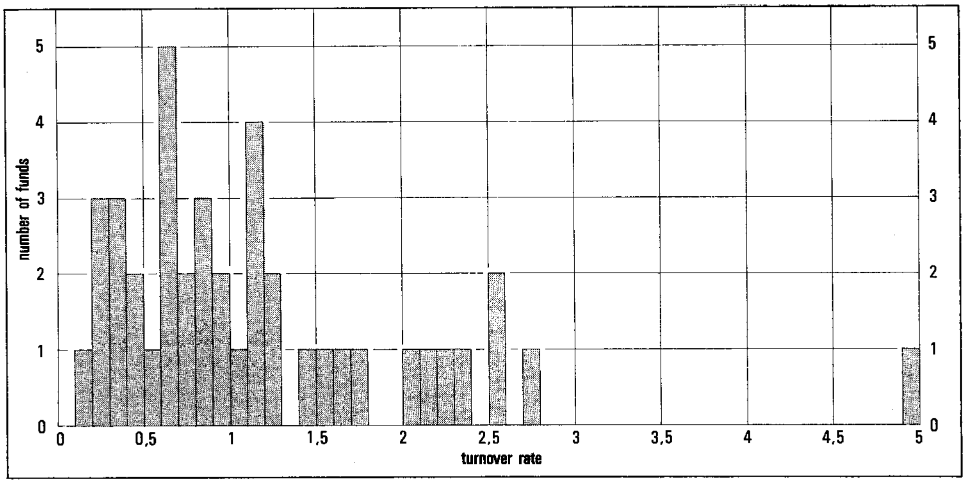
At the end of December there were 60 funds in operation, of which 18 had been launched during 1986. Despite the rise in the number of funds, the degree of concentration in the sector remained more or less unchanged; at the end of December the funds marketed by the three largest management companies held almost 43 per cent of the net assets of all the funds and 48 per cent of their Italian equity portfolio, compared with 45 and 51 per cent respectively in 1985.

The portfolio turnover rate, defined as the ratio of the value of trading (adjusted to exclude net fund-raising) to holdings of securities, averaged 1.2 in 1986 for the funds that had completed the quarterly return at the end of 1985; values ranged from a low of 0.14 to a high of 5 but were concentrated around unity, with the rates for 21 of the 41 funds examined falling between 0.5 and 1.5 (Figure 14). For the equity portfolio alone, the indicator shows an estimated average value of 1.8 for share-based and mixed funds.

Figure 14

PORTFOLIO TURNOVER RATES OF ITALIAN INVESTMENT FUNDS

(January-December 1986)



At the end of December the funds' portfolios totaled 62.6 trillion lire. Government securities declined slightly as a proportion of the total to stand at 57 per cent, compared with 60 per cent a year earlier (Table 37).

Table 37

ITALIAN INVESTMENT FUNDS

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

	1985 Dec.	1986 Mar.	1986 June	1986 Sept.	1986 Dec.	1987 Mar. (1)
Government securities	*11,270*	*20,364*	*30,636*	*34,514*	*35,844*	*37,859*
Treasury bills	*578*	*959*	*1,780*	*1,753*	*1,085*	*1,160*
Treasury credit certificates	*9,240*	*14,901*	*21,200*	*24,429*	*26,419*	*29,579*
Treasury certificates in ECUs	*303*	*676*	*830*	*810*	*836*	*764*
Treasury bonds	*1,141*	*3,816*	*6,812*	*7,452*	*7,340*	*6,338*
Bonds	*1,876*	*3,186*	*4,216*	*4,950*	*5,153*	*5,457*
Shares	*5,095*	*10,824*	*14,240*	*17,423*	*17,887*	*18,947*
Total lira-denominated securities	18,241	34,374	49,092	56,887	58,884	62,263
Securities denominated in foreign currency	678	1,151	2,206	3,402	3,727	4,505
Total portfolio	**18,919**	**35,525**	**51,298**	**60,289**	**62,611**	**66,768**
Other net assets (2)	864	1,455	1,581	2,063	2,468	2,413
Net worth	**19,783**	**36,980**	**52,879**	**62,352**	**65,079**	**69,181**

(1) Provisional. — (2) Including certificates of deposit.

At the same date holdings of Italian shares were almost four times as high as at the end of 1985 (17.9 trillion lire as against 5.1 trillion), but they only expanded from 26.9 to 28.6 per cent of the total portfolio. The funds showed little interest in unlisted shares, holdings of which remained negligible.

Holdings of foreign securities expanded strongly, rising from 700 to more than 3,700 billion lire and increasing their share of the total portfolio from 3.6 to 6 per cent. The largest component consisted of shares (2,300 billion lire), issued mainly in the markets of the United States (590 billion), Germany (570 billion) and France (340 billion); the most prominent items among bonds were issues by international institutions (510 billion) and on the German market (390 billion).

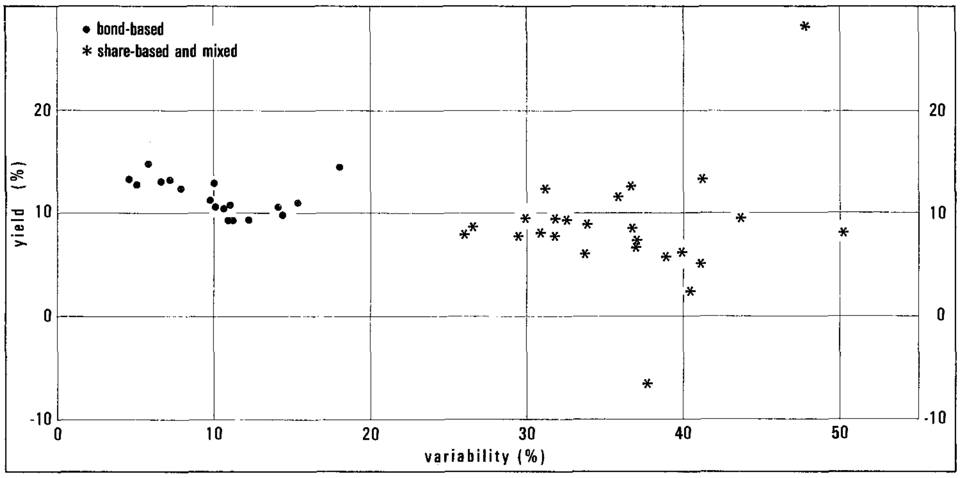
The yield on investment fund units remained high last year. Despite the downturn in share prices after the rapid increase in the early part of the year, the Bank of Italy's capital value index for the funds as a whole increased by 24.6 per cent. In the first three months of 1987 the rise in the index slowed down to 1.4 per cent, owing partly to the further slight decline in share prices.

There continued to be marked differences in the indices for individual funds; in the twelve months to March 1987 the gross ex post yields of funds that had been in operation for at least a year ranged from 8.8 to 14.7 per cent in the case of bond-based funds and from —6.7 to 28.2 per cent in that of share-based and mixed funds, which are more susceptible to fluctuations in share prices (Figure 15).

Figure 15

YIELD AND VARIABILITY OF ITALIAN INVESTMENT FUNDS (1)

(April 1986-March 1987)



(1) Those operating at the end of March 1986. Annualized average values and standard deviations of the monthly yields in the period.

The net assets of foreign investment funds operating in Italy rose from 7.5 to 10.7 trillion lire last year (Table 38). Net redemptions of around 200 billion lire were outweighed by substantial capital gains, which accrued mainly in the first quarter of the year. At the end of December their securities portfolio amounted to 10.3 trillion lire.

Table 38

FOREIGN INVESTMENT FUNDS

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

	1985 Dec.	1986			
		Mar.	June	Sept.	Dec.
Italian securities	6,203	8,555	8,209	9,055	9,047
shares	*3,756*	*5,475*	*5,137*	*5,870*	*5,767*
Foreign securities	916	1,133	1,314	1,240	1,263
shares	*748*	*977*	*1,129*	*1,085*	*1,078*
Total portfolio	**7,119**	**9,688**	**9,523**	**10,295**	**10,310**
Other net assets	350	534	587	531	360
Net worth	**7,469**	**10,222**	**10,110**	**10,826**	**10,670**

The largest growth was in holdings of Italian securities, which rose from 6.2 to 9 trillion lire, and especially in shareholdings, which increased from 3.8 to 5.8 trillion. Their external portfolio showed a less pronounced expansion, rising from 0.9 to 1.3 trillion lire; here too, most of the increase occurred in holdings of shares, which rose from 0.7 to 1.1 trillion lire.

Investment management services

Investment management services expanded further in 1986. On the basis of a Bank of Italy survey covering all credit institutions and a larger sample of non-bank investment managers than had been polled in 1985, it is estimated that the savings entrusted to the sector exceeded 14.5 trillion lire last year; at the end of 1986 the financial assets under management came to around 47 trillion lire, compared with 27.3 trillion in 1985 for the wider sample. The size of the average customer portfolio increased substantially to almost 200 million lire at the end of December, eight times the average holding of investment fund units (25 million lire).

The business carried out by credit institutions almost doubled, so that at the end of 1986 they managed assets totaling 42.8 trillion lire, compared with 24.4 trillion a year earlier. According to the survey, non-bank companies managed around 4.2 trillion lire in assets, against 2.9 trillion at the end of 1985.

The proportion of total assets invested in government securities fell from 76 per cent at the end of 1985 to 72 per cent last year and the percentage held in shares showed a corresponding increase from 11 to 15 per cent. This equity component, which consisted almost entirely of listed shares, was larger among non-bank investment managers (24 per cent) than among credit institutions (14 per cent). The proportion of bonds increased slightly to 12 per cent of the total.

Insurance companies

The growth in the insurance sector that began in the early eighties continued last year. Premium income and reserves increased at a rapid pace, especially in the life insurance sector; as mentioned above, the performance of the latter was due to increased demand for individual and company-based supplementary pension schemes.

At the end of the year 216 insurance companies were authorized to operate in Italy, of which 54 were foreign companies. Their main balance sheet assets — securities, real estate, mortgages and deposits — increased from 33.5 to 40.5 trillion lire last year, while their net worth rose to 8.3 trillion (Table 39). The composition of their total assets continued to change, with the securities component rising from 62 to 67 per cent and the real estate portfolio contracting by 3 percentage points.

The premium income from direct insurance in Italy by the 56 companies providing life insurance rose by 38 per cent, from 2.6 to 3.6 billion lire; it has almost doubled in the last three years. The gradual spread of company-based supplementary pension schemes is evident in the growth in group policies, which accounted for around 14 per cent of premium income last year.

Total technical reserves net of reinsurance commissions increased by 3.4 trillion lire. The sector remained highly concentrated; at the end of December the leading five companies held more than 80 per cent of total reserves. Net worth increased by 15 per cent to 3 trillion lire.

Table 39

ASSETS AND LIABILITIES OF THE INSURANCE COMPANIES

(balance-sheet items in billions of lire)

	Main assets					Technical reserves (3)	Net worth
	Deposits and cash	Securities (1)	Mortgages & annuities (2)	Real estate	Total		
				life sector			
1985	282	7,878	1,377	4,025	13,562	12,080	2,604
1986 (4)	288	11,112	1,349	4,198	16,947	15,448	2,985
				casualty sector			
1985	1,725	12,971	290	4,912	19,898	16,535	4,185
1986 (4)	1,747	16,064	326	5,464	23,601	19,256	5,343
				total			
1985	2,007	20,849	1,667	8,937	33,460	28,615	6,789
1986 (4)	2,035	27,176	1,675	9,662	40,548	34,704	8,328

Source: Based on ANIA data.
(1) In lire and foreign currency, including participations. — (2) Net of corresponding liabilities. — (3) Net of reinsurance. — (4) Partly estimated.

In a year of strong expansion in the share market, the life insurance companies increased their investment in shares only moderately from 1 to 1.2 trillion lire, thereby reaffirming their traditional prudence in making financial investments. Their receipts were invested mainly in government securities, especially Treasury credit certificates, holdings of which increased from 3.2 to 4.5 trillion lire (Table 40).

Given the composition of the life companies' securities portfolio and its high degree of indexation, yields on reserves for revalutable policies have been comparable to those attainable in the financial market in recent years. In 1986 the companies earned yields averaging 16 per cent, but recognized credits of 13 per cent to policy-holders. The ratio of recognized credits to yields continued to grow, rising to 81 per cent.

In the casualty sector, premium income from direct insurance in Italy rose from 14.1 to 16 trillion lire, an increase of 14 per cent over 1985. The largest item, 48 per cent of the total, was premiums from compulsory motor insurance. Total technical reserves net of reinsurance commissions increased by 2.7 trillion lire. The companies' net worth rose by 28 per cent, whereas their main assets increased by 19 per cent over the year.

Table 40

INSURANCE COMPANIES' PORTFOLIOS OF SECURITIES

(balance-sheet items in billions of lire)

	Public sector				Special credit institutions (1)	Firms and public enterprises	Shares (2)	Securities in foreign currency	Total
	Treasury bills	Treasury credit certificates	Treasury bonds	Other					
					life sector				
1985	35	3,188	288	482	1,344	902	987	654	7,880
1986 (3)	34	4,490	895	631	1,970	1,179	1,207	705	11,111
					casualty sector				
1985	188	2,497	335	445	4,744	799	2,326	1,635	12,969
1986 (3)	136	2,769	1,017	542	5,557	1,160	3,040	1,843	16,064
					total				
1985	223	5,685	623	927	6,088	1,701	3,313	2,289	20,849
1986 (3)	170	7,259	1,912	1,173	7,527	2,339	4,247	2,548	27,175

Source: Based on ANIA data.
(1) Including certificates of deposit. — (2) Including equity participations, which in turn include units in Italian investment funds amounting to 37 billion lire for the life sector and 18 billion lire for the casualty sector in 1986. — (3) Partly estimated.

Their holdings of securities expanded from 13 to 16.1 trillion lire. The main change occurred in Treasury bonds, which rose from 3 to 6 per cent of the portfolio; the share of securities issued by special credit institutions contracted slightly to 35 per cent but remained larger than that of government securities (28 per cent).

THE SECURITIES MARKET

There was continued expansion last year both in the bond market, which was supplied mainly by the public sector to meet its financing requirement, and in the share market, where the further improvement in the economic and financial health of firms enabled them to raise a substantial volume of risk capital. The public sector turned increasingly towards fixed rate securities, whereas companies issued a significantly higher volume of savings shares. Moreover, securities with features mid-way between those of shares and bonds, such as investment fund units, convertible bonds and bonds with warrants, became much more common. Supply and demand were matched by raising the prices of financial instruments of all kinds.

The increase in the number of market operators led to keener competition, reducing transaction costs and increasing market turnover. The larger volume of trading increased the depth of the secondary market and the significance of market price-setting. The speed of the expansion in the share market revealed the limitations of its present organizational structure. In particular, the increase in trading volume exacerbated the problems of share delivery, since share certificates are not held centrally.

The growth in the market encouraged the introduction of new financial instruments for forward and option dealings in securities; in particular, financial futures and options on government securities gained ground as part of the process of market diversification aimed at giving market operators greater opportunities for covering the risks that most concern them.

In 1986 and the first few months of 1987 steps were taken to create a market structure able to bear the increased level of activity and to raise efficiency. The introduction of the new regulations of the Monte Titoli securities clearing house and the further moves towards centralizing the administration of government securities at the Bank of Italy were aimed at facilitating settlements and increasing market efficiency. It was decided that interest on government securities and similar paper issued after 30 September 1987 will be taxed on the same basis as bonds, thereby gradually reducing market segmentation due to differences in tax treatment. In order to expand the flow of risk capital to firms, the Interministerial Committee for Credit and Savings and the Bank of Italy established the statutory framework for merchant banking activities by banks' subsidiaries by defining the operations that merchant banking companies may undertake and laying down the rules for the acquisition of interests in such companies by banks and central credit institutions.

Bonds and government securities

Gross issues of bonds and government securities amounted to 449.2 trillion lire, or 50.2 per cent of GDP, against 412.4 trillion and 51.2 per cent in 1985. There was a slight shift in the composition of the total; the public sector accounted for 89.7 per cent of issues, but the proportion issued by special credit institutions increased to 8.2 per cent and that floated by firms and public corporations to 2.1 per cent (Tables 41 and a17).

Table 41

ISSUES OF SECURITIES AND NET RECOURSE TO THE MARKET

(billions of lire)

	Gross issues		Net issues (1)		Net recourse (2)	
	1985	1986	1985	1986	1985	1986
Public sector (3)	376,645	402,976	97,331	97,459	40,879	30,940
Treasury bills	*256,281*	*265,866*	*13,181*	*9,697*	*– 8,116*	*– 8,371*
Treasury credit certificates	*97,209*	*79,255*	*78,567*	*53,534*	*51,111*	*15,064*
Treasury bonds	*17,288*	*53,276*	*3,973*	*35,025*	*– 1,067*	*29,236*
Special credit institutions	30,316	36,740	6,917	8,437	– 7,745	– 6,076
certificates of deposit	*15,254*	*18,645*	*1,739*	*2,174*	*– 1,390*	*– 833*
Firms and public corporations	5,473	9,454	2,196	6,144	– 858	2,663
Total	**412,434**	**449,170**	**106,444**	**112,040**	**32,276**	**27,527**
As a percentage of GDP	*51.2*	*50.2*	*13.2*	*12.5*	*3.6*	*3.1*

(1) Gross issues adjusted for redemptions, premiums and discounts. For Treasury bills, gross issues less redemptions. — (2) Gross issues adjusted for premiums and discounts, redemptions and coupons net of withholding tax. — (3) Net of funding operations.

Net recourse to the market (defined as gross issues adjusted for issue premiums and discounts, redemptions and interest net of withholding tax) was well down on 1985 (30.9 trillion lire, compared with 40.9 trillion). In particular, net recourse in the form of Treasury bills was negative for the fourth year in succession (-8.4 trillion) and that in Treasury credit certificates in ECUs (1.3 trillion) was curbed by the appreciation of the lira. By contrast, net market recourse via Treasury bonds increased strongly to 29.2 trillion lire, almost twice that in floating rate Treasury credit certificates (15.1 trillion). At a time of falling yields, the shift in market preference towards fixed rate securities was encouraged partly in order to weaken further the link between the cost of the public debt and the behaviour of short-term interest rates. With the same object in view, substantial amounts of Treasury credit certificates (14.9 trillion lire) were issued with the option to convert them into fixed rate securities during 1987.

Particularly large bond issues were made by special credit institutions (18.1 billion lire), IRI (2.3 trillion lire in ordinary bonds and 0.9 trillion in convertible bonds or bonds with warrants), ENEL (2.8 trillion) and the State Railways (2.5 trillion). International institutions increased their presence in the fixed rate market.

Euro-lira bond issues on international markets by non-resident agencies and companies came to 600 billion lire, compared with 200 billion in 1985; they bore interest at nominal rates of between 10.25 and 11.50 per cent and had maturities of between five and eight years.

Issues of this kind, which first appeared in September 1985, may be made in amounts of between 50 and 150 billion lire by non-resident companies and agencies to finance investment in Italy and must be arranged through an underwriting syndicate led by an Italian bank or one of its foreign subsidiaries. For the purposes of foreign exchange regulations, Euro-lira bonds are treated in the same way as foreign currency bonds issued by non-residents. Interest on lira securities issued abroad by the Italian Treasury or by international institutions is exempt from taxation.

In March 1987 discounted Treasury certificates were issued for the first time; 1.9 trillion lire were sold, out of an issue volume of 3 trillion. A further issue was made the following month on more attractive terms, which made it possible to dispose of 1.7 trillion lire of the 2.5 trillion on offer.

The discounted Treasury certificates issued in March and April are seven-year securities with coupons paid annually and are redeemable at maturity. Apart from the first coupon, interest is paid at half the yield on 12-month Treasury bills, the rate to which Treasury credit certificates are linked. The discounted certificates were offered at a substantial discount using the uniform-price auction method; in the case of the March issue, the base price was set at 74 per cent of the certificates' face value. The maturity of the May issue was reduced to four years.

In April and May the arrangements for selling Treasury credit certificates and Treasury bonds were changed, in that the issue volume will no longer be announced. To spare savers the inconvenience of having applications scaled down, it was decided to meet demand in full during the subscription period but to give the Treasury the option of closing subscriptions early. The fact of not announcing the issue volume and the easing of the limits on the amount that can be placed at medium and long term have made it possible to improve the signals coming from the market by eliminating speculative demand caused by the allotment mechanism.

Nominal yields on bonds and government securities declined substantially in 1986 owing to the slowdown in inflation. The decline was fairly pronounced in the first half of the year, continued at a slower pace in the second half and in the first quarter of 1987 and came to a halt in April 1987. The removal of tax exemption for interest on new issues of government securities and similar paper was one of the factors that modified the relative advantages for different categories of investor.

Net yields at issue on 12-month Treasury bills and Treasury credit certificates fell by 3.89 and 4.01 percentage points respectively. The yield differential between the two kinds of security remained almost unchanged in absolute terms but increased in relation to the Treasury bill rate. In the first four months of 1987 the two yields came down by only 0.3 percentage points.

Net issue yields on Treasury bonds declined from 13.39 to 9.22 per cent. There was a slowdown in the final quarter of the year that also affected conversion rates on convertible Treasury credit certificates, which fell from 11 per cent in January 1986 to 8.50 per cent in September and 8.20 per cent net in the last three months of the year.

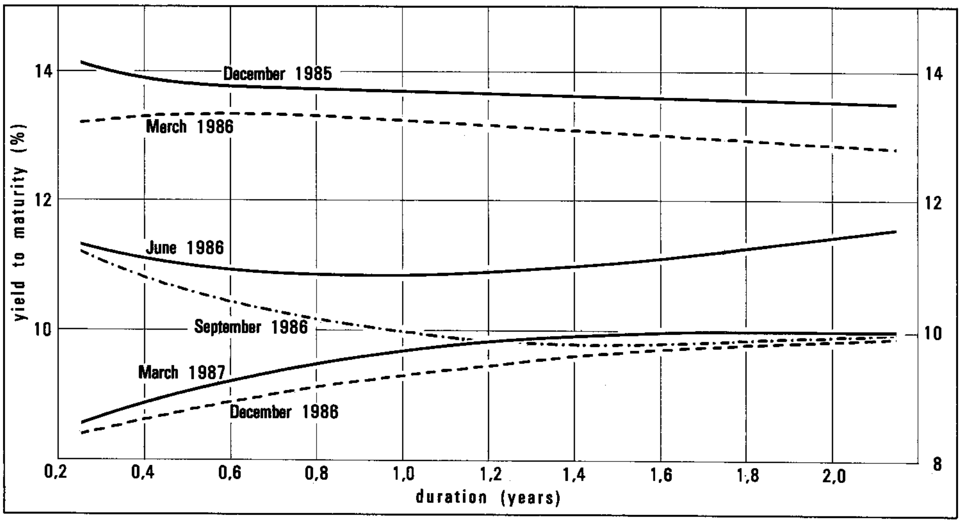
Secondary market yields and issue yields have not always been in step (Table a21). For example, yields on quoted Treasury bonds were 0.92 percentage points higher than net issue yields in the second half of the year, compared with a differential of only 0.09 percentage points in the first half. This helps explain the difficulties encountered in selling such securities in the latter part of the year. In the case of floating rate Treasury credit certificates, the yield differential in favour of the secondary market was 0.29 points in 1986.

The increased recourse to Treasury bonds to finance the public sector borrowing requirement added depth to the secondary market in these securities, restoring the significance of the yield curve and making it possible to analyse the curve's behaviour over recent months. Yields declined across the board in the first nine months of the year; in the fourth quarter the curve took on an upward slope owing to the stabilization of expectations about longer-term interest rates and to the downward pressure on rates at the shorter end of the range caused by the reduction in issue yields on short-term securities.

At the end of March 1987 the curve was still positively sloped, confirming that expectations of a decline in interest rates had run their course (Figure 16).

Figure 16

TIME/YIELD CURVES (1)

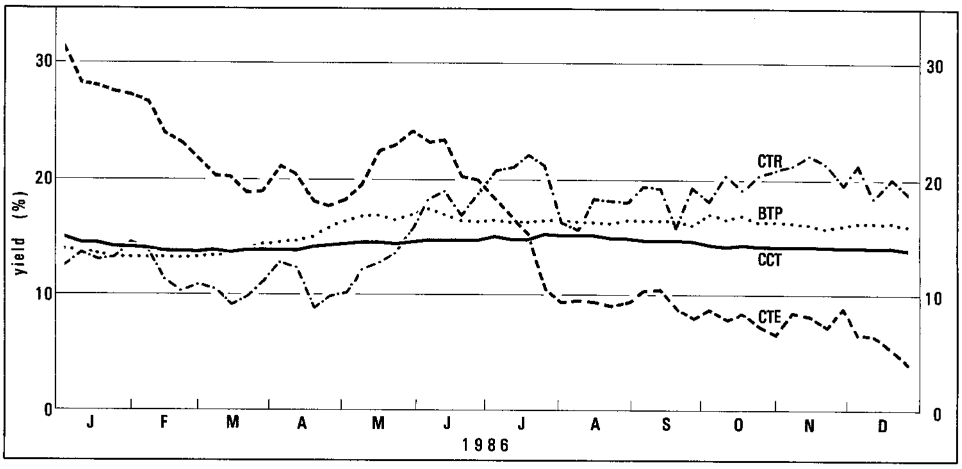


(1) Constructed by interpolating the yields to maturity of listed Treasury bonds.

The profitability and variability of investments in Treasury bonds and the various kinds of Treasury credit certificate can be assessed by looking at the behaviour of ex post yields on all quoted securities of these kinds (Figure 17). In 1986 the yield on index-linked Treasury certificates was 20.04 per cent, higher than that on Treasury bonds (16.36 per cent) or on floating rate Treasury credit certificates (13.98

Figure 17

EX POST ANNUAL YIELDS ON GOVERNMENT SECURITIES (1)



per cent); the high ex post yields on index-linked Treasury certificates and Treasury bonds are explained by the substantial rise in prices, while the low yield of 2.72 per cent on Treasury credit certificates in ECUs was attributable to the appreciation of the lira against the ECU and the fall in the price of these securities (Table 42). The differential between the various ex post yields was very narrow if a longer period is examined; over the last three years the yields on investments in floating rate Treasury credit certificates, Treasury bonds and Treasury credit certificates in ECUs were broadly similar (16.48, 16.56 and 16.02 per cent respectively).

Table 42

ANNUAL EX POST YIELDS (1)

	Year	Interest rates	Capital gains	Exchange rate changes	Inflation rate (2)	Total
Floating rate Treasury credit certificates . .	1984	....	....	—	—	19.59
	1985	....	....	—	—	15.94
	1986	....	....	—	—	13.98
Treasury bonds	1984	16.47	1.62	—	—	18.36
	1985	15.32	−0.30	—	—	14.97
	1986	12.47	3.45	—	—	16.36
Treasury certificates in ECUs	1984	12.12	1.83	0.04	—	14.22
	1985	10.90	10.34	8.77	—	33.10
	1986	10.60	−4.13	−3.13	—	2.72
Index-linked Treasury certificates	1984	—	—	—	—	—
	1985	3.38	−1.01	—	9.88	12.45
	1986	3.35	6.97	—	8.76	20.04

(1) Calculated by the multiplicative method. — (2) Implicit GDP deflator at factor cost.

Shares

In 1986 the share market displayed exceptional growth and offered much greater opportunities as a source of corporate finance. The capitalization of companies quoted on the Milan stock exchange almost doubled from 98 to 190 trillion lire owing to the rise in share prices, substantial capital increases and numerous new listings; the number of companies admitted to the market (43, of which 5 were already listed on other Italian exchanges) was as high as in the preceding five years taken together. At the end of December the stock exchanges listed a total of 222 companies, including those whose quotation had been suspended; 202 of them were listed on the Milan exchange. The volume of transactions on the Milan stock exchange was 66.5 trillion lire, around two and a half times the figure for 1985 (26 trillion) and almost ten times that for 1984 (7 trillion).

Gross share issues by listed and unlisted companies came to around 23.8 trillion lire last year, compared with 15 trillion in 1985 and an average of 11 trillion over the five years from 1981 to 1985; 0.8 trillion of this was offered for public subscription. In addition, around 2 trillion lire in shares already in circulation was offered for sale during the year.

The rise in share prices in the first half of the year favoured issues by listed companies, which were responsible for 62 per cent of gross issues, compared with 31 per cent in 1985 (Table 43). A substantial portion of the issues and public offers of shares were non-voting securities; in particular, issues of savings shares came to 6.5 trillion lire, 44 per cent of issues by listed companies. By contrast, issues by unlisted companies declined to around 9 trillion lire, compared with 10.3 trillion in 1985.

Table 43

GROSS SHARE ISSUES

	Billions of lire				% composition			
	1983	1984	1985	1986	1983	1984	1985	1986
Listed companies	**4,121**	**5,980**	**4,693**	**14,837**	*32.9*	*50.7*	*31.3*	*62.3*
state controlled	3,269	3,970	2,161	3,652	*26.1*	*33.7*	*14.4*	*15.3*
private sector	852	2,010	2,532	11,185	*6.8*	*17.0*	*16.9*	*47.0*
Unlisted companies	**8,413**	**5,804**	**10,284**	**8,955**	*67.1*	*49.3*	*68.7*	*37.7*
state controlled	5,996	2,434	7,348	5,365	*47.8*	*20.7*	*49.1*	*22.6*
private sector	2,417	3,370	2,936	3,590	*19.3*	*28.6*	*19.6*	*15.1*
Total	**12,534**	**11,784**	**14,977**	**23,792**	*100.0*	*100.0*	*100.0*	*100.0*
state controlled	9,265	6,404	9,509	9,017	*73.9*	*54.4*	*63.5*	*37.9*
private sector	3,269	5,380	5,468	14,775	*26.1*	*45.6*	*36.5*	*62.1*

Issues were highly concentrated among a small number of issuers; five public and private sector groups (Montedison, IRI, Olivetti, Fiat and ENI) accounted for 70 per cent of total issues of quoted securities and offers for sale.

Special credit institutions and firms also made very large issues of convertible bonds and bonds with warrants totaling 5.4 trillion lire, compared with 2.2 trillion in 1985. Indirect issues by firms accounted for around 3.7 trillion lire of the total and were made almost entirely by Mediobanca and IRI. Direct issues by firms amounted to around 1.7 trillion.

The growth in the share market also affected the activity of the credit system. Besides issuing 0.8 trillion lire in savings shares, the banks floated shares worth more than 2.8 trillion lire, of which 1.4 trillion was in listed shares. Banks and special credit institutions participated in a large number of the placement and underwriting syndicates formed to handle issues and public offers of shares and convertible bonds.

The Italian and foreign investment funds and investment management services played a prominent role in the share market. At the end of the year the Italian shares in their portfolios accounted for respectively 12.4 and 3.5 per cent of the capitalization of the Milan stock exchange.

The Milan stock exchange index rose by 64 per cent last year. Share prices rose strongly in the first five months of the year, peaking in mid-May at a level 110 per cent above that recorded at the beginning of the year, but subsequently they fell back amidst sharp fluctuations; the pronounced fall in June was followed by a recovery in July and August and a further decline in the last four months of the year.

The profits of listed companies continued to increase last year. The net profits of the 159 companies for which 1986 accounts are available rose from 4.3 to 5.4 trillion lire, an increase of 25 per cent. The weighted average price/earnings ratio stood at 30 at the end of 1986, compared with a value of 23 for the same sample of companies a year earlier.

Movements in share prices during the year were influenced by the unevenness of supply and demand. In the first quarter the net purchases of shares by Italian investment funds alone were around 20 per cent higher than issues of listed shares, thus exerting strong upward pressure on share prices. On the other hand, the index fell during the periods when most of the issues were made. In June, when the issue volume was very large, the Milan stock exchange index showed a particularly marked fall of around 15 per cent, despite heavy buying by investment funds. Towards the end of the year a further high concentration of issues again depressed prices; on that occasion the steadying effect of the investment funds was limited by a fall in their inflow of resources.

HOUSEHOLDS' SAVING AND THE FINANCING OF ENTERPRISES

The trend in financial balances

The financial surplus of households was the equivalent of 14.5 per cent of GDP in 1986, about the same as in 1985, while the net indebtedness of the public sector and of enterprises diminished by 1.5 and 2.5 percentage points respectively. Italy's external position swung from net indebtedness of about 0.8 per cent of GDP to net credit of about the same amount (Table 44).

Table 44

FINANCIAL BALANCES (1)

	Households	Enterprises	Public sector (2) (consolidated)	External sector	House-holds	Enterprises	Public sector (2) (consolidated)	External sector
	(in billions of lire)				*(as a percentage of GDP)*			
1980	45,843	−29,237	−33,546	8,569	11.7	−7.5	−8.6	2.2
1981	59,075	−27,994	−52,019	10,324	12.6	−6.0	−11.1	2.2
1982	73,466	−22,530	−66,363	8,371	13.5	−4.1	−12.2	1.5
1983	92,603	−27,536	−76,525	−2,408	14.7	−4.4	−12.1	−0.4
1984	106,128	−28,266	−94,378	4,152	14.7	−3.9	−13.1	0.6
1985	116,014	−39,780	−109,923	6,872	14.4	−4.9	−13.6	0.8
1986	129,251	−21,825	−108,220	−6,077	14.5	−2.4	−12.1	−0.8

(1) As of 1985, the flows of liabilities of households and enterprises include credit from a group of consumer credit, leasing and factoring companies. — (2) Net indebtedness: includes technical reserves of social security institutions.

Adjusted for the decline in the purchasing power of financial assets, the changes in financial balances differed considerably from those in the unadjusted figures. In relation to GDP, households' saving was more than 3 percentage points higher than in 1985 owing to slower inflation and households' increasing holdings of assets with variable capital values, such as investment fund units. The public sector deficit, by contrast, widened by nearly 2 points.

Adjusted for the decline in the purchasing power of financial assets, households' interest income amounted to almost 3 per cent of GDP. Similarly adjusted, interest payments by the public sector and by enterprises came to respectively 3.7 and 3.0 per cent of GDP, compared with 0.9 and 2.3 per cent in 1985.

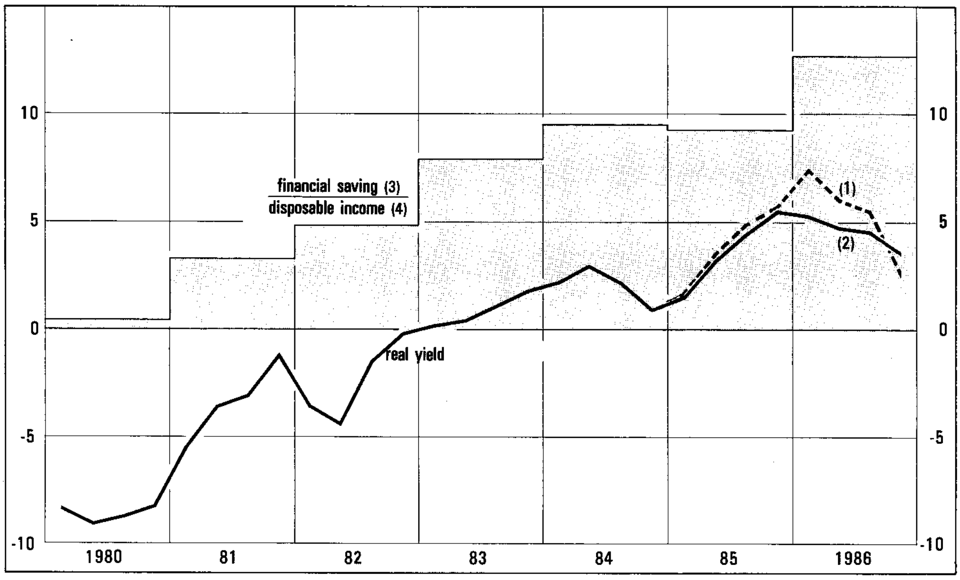
Households' saving and financial assets

Households' financial saving rose slightly from 16.0 to 16.2 per cent of the disposable income of the private sector; adjusted for inflation, the increase was more substantial, 12.8 per cent compared with 9.2 per cent in 1985 (Figure 18). The disposable income of the private sector has been used because data on households' disposable income consistent with the revised national accounts are not available.

Figure 18

HOUSEHOLDS' FINANCIAL SAVING

(percentages)



(1) Real rate of return, net of tax, on money, securities and Italian investment fund units. — (2) Real rate of return, net of tax, on money and securities. — (3) Adjusted for inflation. — (4) Of the private sector.

The flow of households' financial assets was 140.9 trillion lire in 1986; this represented a rise in the stock of assets, net of shares, of 17.1 per cent, as against one of 18.0 per cent in 1985. Liabilities increased by 11.6 trillion lire, or 20.9 per cent, compared with 18.3 per cent in 1985 (Table 45).

The further increase in the average propensity for financial saving, adjusted for inflation, was prompted in part by the rise in the real yield on financial assets. Between 1985 and 1986 the real yield on households' holdings of money and securities rose by nearly one percentage point; including the capital gain on the value of investment fund units, the increment was about 1.5 points (Figure 18).

The proportion of the flow of assets in the form of investment fund units more than doubled from 12.2 to 26.6 per cent, while that of money (M2) and government securities declined. The decline in the yield on fund units in the second half of the year affected the real return on financial assets, which exceeded 7 per cent in the first quarter but had diminished to 2.5 per cent by the end of the year.

Table 45

FINANCIAL ASSETS AND LIABILITIES OF HOUSEHOLDS (1)

(billions of lire)

	Year-end stocks	Flows				
	1986	1982	1983	1984	1985	1986
Notes and coin	37,363	2,770	3,145	2,906	3,060	2,481
Bank deposits	334,823	39,650	25,136	30,659	31,229	27,577
Post Office deposits	61,090	2,800	3,687	5,664	7,989	10,584
Treasury bills	119,568	10,428	16,045	20,036	15,377	4,725
Special credit institutions' deposits & savings certificates	23,747	6,858	1,364	4,260	1,550	2,583
Treasury credit certificates	127,460	5,269	29,473	27,945	31,649	19,460
Other government securities	36,500	– 1,464	3,333	5,366	1,438	16,691
Other medium & long-term securities (2)	27,426	2,714	4,526	3,623	2,655	2,201
Units in Italian investment funds	65,079	—	—	1,055	15,256	37,509
Shares & participations	150,554	87	203	141	1,337	3,895
Foreign assets (3)	11,724	146	85	545	664	– 298
Other financial assets (4)	119,405	8,760	9,965	10,249	12,441	13,459
Total assets	**1,114,739**	**78,017**	**96,962**	**112,449**	**124,645**	**140,867**
Debt to banks (5)	38,027	2,470	2,435	4,065	6,048	8,293
Debt to special credit institutions	20,970	1,764	1,720	1,614	1,817	2,940
Other financial liabilities (6)	8,227	317	204	242	752	382
Total liabilities	**67,224**	**4,551**	**4,359**	**5,921**	**8,618**	**11,615**

(1) Partly estimated data. — (2) Excluding foreign bonds. — (3) Lira and foreign currency bonds plus foreign investment fund units. — (4) Technical reserves, pension and severance pay funds, atypical securities and bankers' acceptances. — (5) Flows include bad loans. Tha data for 1984 are adjusted for the distortion induced by the end of the ceiling on bank lending. — (6) Includes loans from social security and insurance institutions. Stock data include banks' bad loans. As of 1984 stocks and as of 1985 flows include financing by a group of non-bank consumer credit companies.

The decline in nominal interest rates stimulated demand for mortgage loans by reducing the incidence of the initial repayment instalments on households' disposable income. Lending to households by special credit institutions, mainly real estate institutions, expanded by 16.3 per cent as against 11.2 per cent in 1985. Mortgage lending by banks increased by 28.5 per cent as against 26.8 per cent in 1985.

Consumer credit also grew rapidly during the year. The amount outstanding at the end of 1986, which was divided almost equally between bank lending (personal loans and revolving credit cards) and credit from specialized finance companies, may be estimated at more than 12 trillion lire, an increase of 17 per cent over 1985.

The financing of enterprises and their liquidity

The self-financing capacity of enterprises strengthened further in 1986, thanks in part to improved profitability and in part to the decline in net interest charges. The funds which thus became available, coupled with slightly higher borrowing than in 1985 and slower growth in fixed investment and stockbuilding, resulted in a substantial increase in financial assets, the flow of which virtually doubled.

Table 46

FINANCIAL ASSETS AND LIABILITIES OF ENTERPRISES

(billions of lire)

	Year-end stocks	Flows				
	1986	1982	1983	1984	1985	1986
Liquid assets (M3)	171,250	16,842	12,559	17,163	11,512	13,950
of which: bank deposits	144,773	13,789	11,073	14,577	9,484	13,468
Treasury credit certificates	20,728	523	2,974	5,583	5,874	5,373
Other government securities	5,211	−6	599	586	628	3.108
Other medium and long-term securities	4,752	998	959	5	857	1,010
Italian shares (1)	675,246	1,173	893	1,709	−2,847	4,174
Net short-term foreign trade credits	6,215	2,065	−616	2,547	−1,532	2,088
Medium and long-term foreign trade credits and loans	20,333	−219	1,630	386	1,578	1,759
Foreign shares	32,791	882	2,526	2,780	2,292	3,761
Other financial assets (2)	5,873	−3,280	371	620	612	429
Total assets	**942,399**	**18,978**	**21,894**	**31,380**	**18,973**	**35,652**
Debt: short-term (3)	214,793	12,966	18,974	28,523	27,642	22,844
of which: banks (4)	188,227	11,298	18,666	25,650	23,852	14,977
special credit institutions	19,365	1,668	308	2,873	2,114	5,924
medium and long-term (5)	159,774	11,801	9,931	8,855	13,874	14,395
of which: banks	21,161	240	1,710	1,606	2,271	1,633
special credit institutions (6)	82,050	8,746	6,904	7,413	6,970	7,695
foreign	43,385	3,074	755	−839	2,308	1,954
Bonds	30,140	4,589	2,392	1,906	1,687	5,395
Shares	796,469	2,038	2,967	4,948	4,310	10,606
Endowment funds (7)	46,017	7,384	9,431	6,548	5,132	1,704
Other participations	12,031	899	765	1,046	1,639	1,487
Other financial liabilities (8)	28,565	−2,460	−70	−449	−131	−4
Total liabilities (9)	**1,287,789**	**37,216**	**44,390**	**51,377**	**54,153**	**56,428**

(1) Does not include shares issued by state-controlled enterprises purchased by their holding companies. — (2) Includes technical reserves of insurance companies, bankers' acceptances, foreign bonds and other minor items. — (3) As of 1985 flows include financing from a group of factoring companies. — (4) Flows include bad debts and consolidations and are adjusted for bank loans financing the deposit on external payments and for exchange rate changes. The data for banks for 1984 are adjusted for the distortion of banking statistics caused by the end of the bank lending ceiling. — (5) As of 1985 flows include credit from a group of leasing companies. — (6) Flows include bad debts and consolidations. — (7) Net of state-controlled enterprises' consolidation of debt to banks. — (8) Includes acceptances by non-bank investors, atypical securities, bank lending used to finance the deposit on external payments and, for stock data, bad debts to credit institutions. — (9) Excludes severance pay and pension funds.

The flow of total liabilities of enterprises rose from 54.2 to 56.4 trillion lire last year (Table 46). Lending by the credit system accounted for 54 per cent of total finance, while share and bond issues and increases in the endowment funds of state-controlled enterprises contributed 31 per cent; in 1985 these sources had provided 65 and 20 per cent respectively.

Improved profitability and the exceptional rise in share prices until mid-year spurred corporate fund-raising through share issues, which more than doubled to 10.6 trillion lire.

The increase in enterprises' financial assets accelerated sharply from 18.9 trillion lire in 1985 to 35.3 trillion last year, equivalent to just under two thirds of total external financing. The component consisting of money and securities other than shares increased by 13.1 per cent, compared with an 11.8 per cent gain in 1985. The expansion of bank deposits amounted to 13.5 trillion lire, as against 9.5 trillion in the previous year. Purchases of Treasury bonds exceeded 3.1 trillion lire, five times the 1985 figure.

In 1986 the ratio of M3 assets and non-share securities to value added reached its highest level since the start of the decade. The upward trend over the past five years has been due to increased purchases of government securities, while bank deposits have gradually diminished. Enterprises' liquid assets and securities now exceed 97 per cent of their short-term debt to banks; in terms of flows, the figure was 112 per cent in 1986.

The growth in enterprises' domestic assets excluding shares was accompanied by an expansion in their foreign assets. Firms granted net short-term trade credit of 2.1 trillion lire, compared with net short-term trade debt of 1.5 trillion lire in 1985.

Net investment in Italian shares came to 4.2 trillion lire in 1986, increasing the degree of financial concentration and in some instances strengthening the position of controlling groups. The internationalization of Italian companies, which has been under way throughout the eighties, continued last year with direct investment and acquisitions of minority participations worth some 3.8 trillion lire, 50 per cent above the already high levels of the previous three years.

Net interest payments by enterprises declined by about 4.8 trillion lire after contracting by 1.0 trillion in 1985. In relation to value added they diminished by more than one percentage point from 6.2 to 4.9 per cent. This was attributable to a decrease in the average effective cost of domestic borrowing from 16.6 to 15.3 per cent and a reduction in outstanding debt as a share of value added, as well as to the increase in financial assets.

SUPERVISORY ACTIVITY

The Italian banking and financial system is currently subject to forces that are remoulding its functions and structure.

Financial innovation is modifying the forms in which households' saving is invested and the ways in which enterprises manage their cash flows. This has given rise to new instruments, new markets and new intermediaries, diminished the traditional role of the credit institutions and heightened competition.

The financial markets have also been affected by the trend towards international integration. The countries of the European Community are committed to the formation of a single financial market by 1992, within which all intermediaries will enjoy the right of establishment and be able to operate under regulations that are fundamentally uniform. European credit institutions must therefore prepare to compete in a wider and more highly competitive area.

In its action to safeguard the stability and efficiency of the credit system, the Bank of Italy has a responsibility to promote the adaptation of the regulatory and supervisory framework to changing needs and to encourage intermediaries to devise strategies consistent with the underlying developments in financial markets.

Entry controls

The establishment of credit institutions. — Legislation passed in 1985 incorporating EEC Directive 77/780 into Italian law has generally liberalized entry into the credit system, although during the transitional period lasting until December 1989 the Bank of Italy will still be able to take account of the economic needs of the market in examining applications to form new banks.

The renewed possibility of establishing credit institutions, the strong improvement in corporate liquidity, especially for the largest firms, and the growth of the stock market have helped create a situation conducive to the acquisition of the control of banks by financial and industrial groups.

The principle of separation between banking and commerce, designed to safeguard the stability and the allocative efficiency of the credit system, is a cornerstone of Italian banking regulations. The Banking Law of 1936 contains provisions governing banks' participations in the capital of non-financial enterprises; however, it does not specifically regulate capital links in the opposite direction. Law 281/1985 ensures transparency in the ownership of credit institutions by requiring them to report all shareholdings of 2 per cent or more in their capital to the Bank of Italy, but it contains no provisions to prevent the intermingling of interests between the two sectors.

A resolution approved by the Interministerial Committee for Credit and Savings on 20 March 1987 reaffirms the principle of separation and lays down implementing regulations. In exercising its power to authorize the establishment of new banks, the Bank of Italy is required to take account of the need to prevent persons with direct or indirect non-financial interests from setting up banks in which they would have dominant positions. The Bank will also examine the relations of the founding shareholders, including financial companies, with legally separate enterprises which can be shown to be members of the same group on account of technical, financial or organizational links. As to the acquisition of interests in existing banks, the separation between banking and commerce will continue to be safeguarded by the "moral suasion" exercised by the Bank of Italy in accordance with principles reaffirmed by the Credit Committee; stronger deterrents in this sphere would require specific legislation.

The same resolution also strengthens the regulations governing connected lending and lays down that the statutes of credit institutions shall contain provisions to ensure against privileged treatment for shareholders and connected companies.

The separation requirement relates only to dominant interests in credit institutions, not to minority holdings. The latter may usefully enable the banking industry to draw on entrepreneurial expertise from other sectors as well as helping to strengthen banks' capital.

Geographical distribution. — The Branch Plan approved by the Bank of Italy in June 1986 authorizes the opening of 504 new branches, the transformation of 86 offices providing limited services into branches that can offer a full range, and the relocation of 96 existing branches. The full implementation of the Plan will increase the number of bank branches by 3.9 per cent.

The Bank of Italy granted authorizations on the basis of both projected customer demand for banking services and the banks' need to expand. With regard to customer demand, the Bank's aim was to improve banking coverage throughout the country and to strengthen banking services in poorly served areas. As a rule, the needs of the banks have been met by giving preference to network reorganization and favouring the expansion of the banks that have proved the most efficient in terms of profitability and management.

With the aim of fostering the rationalization of branch networks, banks may now relocate offices authorized under the Branch Plan. The authorities have also reintroduced the simplified procedure eliminating the need for prior authorization of branch transfers within specified "market areas", which had been suspended during the preparation of the Plan. Furthermore, the Credit Committee recently adopted a resolution designed to promote the rationalization of the present network by allowing banks greater freedom in the geographical distribution of their branches. The same resolution allows banks to buy and sell branches and lays down guidelines for standardizing branch functions, which are currently highly disparate.

The expansion of banks abroad proceeded last year with the authorization of 6 branches (4 in Community countries and 2 in the Far East) and 8 representative offices.

Regulations and controls

The regulation of banking. — The supervisory authorities have taken steps to enable banks to keep abreast of innovation and cope with the growing competition in the domestic and international markets by broadening the range of operations that credit institutions can undertake, whether directly or through subsidiaries. Insurance brokers, trade financing companies and licensed stock exchange dealers are examples of some of the kinds of companies in which banks may now acquire interests. The diversification of operations is nonetheless limited by the need to maintain both the separation between banking and commerce and the advantages of specialization.

The greater operational and geographical diversification of credit institutions has been facilitated by the provisions enacted to implement EEC Directive 83/350 on banks' participations (Law 114/1986 and the resolution of the Credit Committee of 20 March

1987). These measures provide for supervision on a consolidated basis and thus strengthen the information-gathering powers of the Bank of Italy.

The major Italian banks can now enter the leading financial centres abroad by acquiring interests in companies that are already operating there, since on 19 September 1986 the Credit Committee supplemented an earlier resolution of January 1981 by empowering the Bank of Italy to authorize participations in foreign financial conglomerates.

With the aim of removing a competitive handicap, the criteria adopted for the authorization of Italian banks' establishments in offshore centres have been revised, in accordance with the principles agreed in international fora. The Credit Committee's resolution of 19 September empowered the Bank of Italy to authorize Italian banks to acquire or maintain banking participations in countries whose systems of banking supervision are not optimal but which allow the Italian authorities access to the information needed for effective supervision, provided that the activity of such subsidiaries is restricted to fund-raising on behalf of the groups to which they belong.

On 6 February the Credit Committee accepted a longstanding recommendation of the Bank of Italy by resolving to remove the administrative obstacles that had prevented banks from contributing to the development of merchant banking in Italy and at the same time set limits to their involvement.

To be consistent with the principle of maintaining the separation between banking and commerce, merchant banking business has to be undertaken by separate companies, in which banks can participate in conformity with the general rules governing interests in banking-related companies. Additional prudential rules, outlined by the Credit Committee and detailed in the notices issued by the Bank of Italy, are designed to ensure that initiatives adhere to the spirit of the resolution.

The need to create more uniform competitive conditions for the various categories of bank, especially in view of the impending integration of the European credit market, led the Credit Committee to pass a resolution on 21 May 1987 approving the revision of the regulations governing banks' operations beyond the short term. The conditions governing lira facilities, which had previously varied widely, were standardized, while the changes regarding foreign currency loans are designed to enable Italian banks to participate more effectively in foreign markets, though still with limits on maturity mismatching.

Inspections. — The analytical methods used in inspections are continually being improved and adapted to the disparate conditions encountered in different banks. The assessment of the quality of banks' assets is one of the main aims of inspections. The introduction of capital ratios that take account of the riskiness of bank loans makes it more important that bad debts are identified, a function that can only be adequately performed by way of inspections. Inspectors are also paying increasing attention to banks' organizations and control systems in order to make a thorough assessment of their ability to adapt in today's conditions of rapid change.

A total of 186 general inspections were carried out in 1986, involving one special credit institution and 16.8 per cent of the Italian banking system. The customer deposits and lending of these institutions amounted to 73.69 trillion lire, or 9.5 per cent of the total.

International cooperation. — Within the European Community a process has begun that will lead to the completion of the internal market by 1992. The main stages of this development and the means of accomplishing it are set out in the White Paper approved by the European Council in June 1985. As far as the financial sector is concerned, this will involve the liberalization of capital movements and financial integration. It is the duty of the supervisory authorities to ensure, at both national and Community level, that this goal is attained without impairing either the stability or the efficiency of the Italian banking system.

If financial integration is to be achieved, both of the mechanisms indicated in the White Paper must operate, namely the mutual recognition of national regulations and techniques regarding financial services and the harmonization of national legislation. Application of the principle of mutual recognition alone could compromise the equality of competitive conditions and create instability in the long term if there is pronounced disparity between the operations banks can undertake in a given market under their home-country legislation. There is thus a need to bring greater uniformity to the regulations governing credit and financial activities in the member states. The minimum level of harmonization required must be that which can provide sufficient stability in the credit system to safeguard savings and ensure that freedom of establishment and freedom to supply services do not cause distortions of competition likely to lead to instability.

The areas in which harmonization is a necessary prerequisite include the definition of a credit institution, of the operations it may perform and of the holdings it may acquire, the regulation of ownership, and the means of ensuring the independence of banks. Technical negotiations at Community level have already started on these questions and in due course they will lead to proposals for a second directive on banking coordination.

The need to avoid distortions of competition between banks that are operating in the same market but regulated by different sets of rules is not confined to the European Community. In April 1987 the Basle Committee on Banking Regulations and Supervisory Practices, which is composed of the central banks of the Group of Ten countries, laid the foundations for a multilateral understanding on capital requirements for banks operating in international markets along the lines of January's agreement between the supervisory authorities of the United States and the United Kingdom.

The regulations introduced recently on the compulsory minimum capital ratios for banks have brought Italy into step with international trends.

The economic conditions of banks

Capital adequacy. — Banks continued to improve their capital structure at approximately the same pace as in 1985. Own funds increased by 19 per cent to 59,625 billion lire, while the ratio of own funds to customer deposits rose from 10.6 to 11.6 per cent.

This strengthening of the capital structure of Italian banks is confirmed by comparison with other countries. A survey of the 256 leading European banks shows that the Italian banking system strengthened its capital base the most in the eighties, with the ratio of capital to volume of business rising by an average of almost 4 points and that of capital to risk-weighted assets, as defined by the EEC, increasing by more than 5 points.

The recent development of the share market and the changes in the statutes of public-law banks allowing them to raise capital in the market have reinforced self-financing and enabled Italy to introduce compulsory minimum capital ratios for banks. At its meeting of 23 December 1986 the Credit Committee took note of the Bank of Italy's intention to fix two separate ratios for general application, one based on the riskiness of assets and the other on the volume of business.

The Bank of Italy may require particular classes of bank or even individual institutions to observe ratios higher than the minimum levels established for the system as a whole if this is warranted by a higher degree of risk.

The adoption of a system of compulsory capital ratios is part of the programme of measures the supervisory authorities have been putting into effect for some time to induce an expansion in the credit system's own funds. It responds on the one hand to the need to continue strengthening the less highly capitalized banks at a time of increasing competition and on the other to the use of supervisory tools capable of combining the pursuit of stability with maximum respect for independent decision-making and the entrepreneurial nature of banking.

The capital requirements establish a link between the expansion of banks and their ability to generate sufficient profits to make the necessary allocations to provisions and attract additional capital. They are an incentive to improve productivity and efficiency and also help meet the need to harmonize the principal supervisory regulations in the different countries.

In the case of special credit institutions, the ratio of own funds to total borrowing has remained constantly above that for banks over the last five years, rising from 9 per cent in 1982 to 13.1 per cent in 1986.

Lending risks. — The banks' bad and doubtful debts increased from 16,950 to 20,092 billion lire during 1986, a rise of 18.5 per cent. Notwithstanding the slower rate of increase, the volume of bad debts as a percentage of lending rose to 6.7 per cent for the system as a whole.

The bad and doubtful debts of the special credit institutions increased by 16.1 per cent, rising from 6,660 to 7,734 billion lire. Between 1982 and 1986 bad debts as a percentage of lending rose from 3.4 to 5 per cent, lagging constantly more than one and a half points behind the same ratio for banks.

Investment funds

Last year saw strong expansion in the investment fund sector, with the total number of funds in operation rising from 42 to 60 (5 specializing in shares, 26 in bonds and 29 with a mixed portfolio).

The net assets of the funds increased from 19.8 to 65.1 trillion lire last year; fund-raising net of repurchases accounted for 83 per cent of the growth (37.5 trillion lire), the remainder being due to share price increases and operating profits net of distributed income. In this phase of rapid expansion, the supervisory authorities have aimed to ensure that the sector develops in accordance with the principles laid down in law while at the same time continuing to refine the methods of collecting the information needed to analyze the funds' operations and verify that they are complying with their obligations.

Article 4 of Law 77/1983 states that investment funds' operations must rest on the principle of risk diversification and assigns to the Banking Supervision Department the task of translating this principle into operational rules. In order to ensure the necessary spreading of risks, the Bank of Italy laid down that a fund's investment in the securities of a single issuer should not exceed 5 per cent of the fund's assets, but raised the limit to 10 per cent for a three-year period ending in April 1987 in order to ease the start of operations by the funds, with the added proviso that the total value of holdings exceeding the 5 per cent threshold should not amount to more than 40 per cent of a fund's total assets.

Surveys carried out before the expiry of the transitional period revealed that the possibility of exceeding the 5 per cent limit was being used mainly by the larger funds, which were thus able to channel their resources towards the share market's leading securities. As the number of companies listed on the stock exchange still appeared insufficient to ensure an adequate diversification of investments and in view of the advisability of facilitating the launch of funds recently established or due to begin operations in the near future, the Bank of Italy announced an extension of the transitional period to 30 June 1990; the limit for investment in any one issuer has been reduced to 7.5 per cent of a fund's assets and that for investments exceeding the 5 per cent threshold cut to 30 per cent of assets.

The funds must be monitored systematically if adverse trends in the sector as a whole or in individual funds are to be detected promptly. This need will be met by the system for the automatic processing of data supplied to the Banking Supervision Department, which will shortly come into operation, and by the start of inspections at the beginning of 1987.

THE GOVERNOR'S CONCLUDING REMARKS

I prefaced my remarks to last year's General Meeting by recalling the breadth and intensity of the transformation taking place in both the Italian and international economy and by inviting the credit system and the Bank of Italy to re-examine their functions and review their methods of performing them.

Innovation and change continued to stir up the financial markets in 1986; the financial system's awareness of the problems increased, as did its determination to face and resolve them. Action has now been set in motion to strengthen the existing financial structures and to define and create new ones in what will have to be a long-term programme aimed at achieving objectives that reach beyond the present decade.

Logical time and chronological time do not always coincide. This lack of synchronism conjures up the year 2000, not because it can be expected to produce extraordinary events but because there is a discrepancy between the real world and the institutions in our field too and because we recognize it is up to us to eliminate this discrepancy by modifying institutions and their environment.

Such divergences are part of the evolutionary process, with everyday reality continually influencing institutions and vice versa; however, if one phase in the sequence is delayed, there is a danger that the whole process of advancement will come to a halt. The banks, which are still the linchpin of financial intermediation, are called upon to make a decisive contribution to the development of new instruments, institutions and markets. At the same time, they must grow stronger and reorganize to face the pressures of competition, which are being accentuated by financial innovation and European integration.

The Bank of Italy and the banking system are not alone in facing this challenge. Interest in the problems of finance has never been keener among academics, businessmen, the public and members of Parliament. The debate has been frank and thorough. More than ever before, the central bank has been called upon to explain and argue its views on the structure of the credit system and monetary management and to reconsider its position even when this is based on many years of analysis and experience.

In its own organization, the Bank of Italy is taking action that should increase the effectiveness of monetary and exchange rate policy, make its interventions in the credit system more incisive, raise the standard and reliability of banking services offered to the public, especially in the payments system and securities trading, and exploit the benefits of greater integration between the Bank's central and regional offices.

New operational arrangements, the more widespread use of high-technology equipment, the coordination of decentralized data processing projects and steps to diversify and enhance the experience of the staff are the main internal objectives the Bank is seeking to achieve.

The ability of managers at head office and in the branches, the professional competence of the staff and their sense of commitment and dedication assure success in this endeavour.

The world economy

Economic activity in the industrial countries

The rate of economic growth in the industrial countries slowed down from 3 per cent in 1985 to 2.4 per cent last year and continued to diminish in the first few months of 1987. The main impact of the fall in oil prices was on the rate of inflation, which declined by around three percentage points last year. Those who had believed that the slowdown in inflation and the decline in interest rates on their own could restore sustained growth were disappointed. Domestic demand proved insufficiently strong and the worsening of the trade balance with developing countries in volume terms offset the expansionary effect of the improvement in the terms of trade.

The acceleration in private consumption contrasted with a slowdown in public consumption and investment, especially the latter, which has been discouraged by the prospect of a weak expansion in demand and by the existence of idle capacity, despite the corporate sector's improved profitability. Uncertainty about the future behaviour of exchange rates and fears that protectionism might block access to important markets had a further dampening effect. These factors and the continuing high level of real interest rates have raised the yield threshold for new investment.

Even though growth was slower than expected, the stance of fiscal policy in the industrial countries as a whole was restrictive in 1986.

Steps to bring about the necessary reduction in the US budget deficit have not been matched so far by adequate reflationary measures in the other major countries, where concern prevails about the potential dangers of expanding demand more vigorously by boosting public expenditure; they doubt whether budgetary measures can be used to stimulate activity without causing an irreversible increase in the budget deficit.

At a time when domestic demand in the United States and the developing countries is being depressed by balance-of-payments constraints, the inability of Europe and Japan to boost world trade is heightening the risk of stagnation in the world economy.

More than 30 million people are without work in the industrial countries. Unemployment has decreased in North America, but in Europe it remains at rates of around Il per cent and in Japan it is rising, though still at a low level.

In the United States the deficit on the current account of the balance of payments reached $141 billion last year. The terms of trade improved, since the depreciation of the dollar was more than offset by the fall in the price of oil and other imported raw materials. The worsening of the deficit occurred in the real trade balance and was due to stagnation in the volume of exports at a time when imports were increasing rapidly. Signs of an improvement appeared in the autumn, but since the depreciation of the dollar is now feeding through to the terms of trade, the deficit is expected to narrow only marginally in value terms in 1987.

The exchange rate of the dollar has changed substantially over the last two years. Yesterday it was quoted at 144 yen and DM 1.82, whereas in February 1985 it had touched peaks of 263 yen and DM 3.47. The exchange rate movements have had only a limited impact on American competitiveness; exporters in other industrial countries have defended their shares of the US market by paring profit margins, and some countries in South-East Asia and Latin America have maintained or even improved their competitive position by tying their currencies to the dollar or by letting them depreciate. For their part, American companies initially concentrated on restoring their profit margins in export markets.

Changes in the cyclical position of the US economy in relation to those of the other industrial countries are proving slow to materialize; after increasing by 18 per cent in the United States and by only 7 per cent in the other OECD countries between 1982 and 1985, domestic demand expanded at an annual rate of 3.5 per cent in both areas in 1986 and the early months of this year.

The US current account deficit stands in contrast to the surpluses of Japan and the Federal Republic of Germany, which came to $86 and 36 billion respectively in 1986, in both cases equivalent to about 4 per cent of national product. Medium-term scenarios indicate that at current exchange rates and with unchanged economic policies the disequilibria between the three major countries will reduce only slightly before the end of the decade.

Such large imbalances between the current accounts of the major countries and the associated massive accumulation of net external financial assets and liabilities are a serious obstacle to the restoration of exchange rate stability and a return to a satisfactory growth path at world level. Even the maintenance of an open trading system is in jeopardy.

In the absence of more expansionary economic policies, the slowness of the adjustment in the external accounts of the major countries is accentuating the downward pressure on the dollar, thus posing a new threat to international financial stability, fueling inflation in the United States and curbing growth in countries with appreciating currencies.

As long ago as last September, when the decline in the US currency began to gather pace, these considerations formed the basis of the dollar support agreements reached at Gleneagles by the central banks of the European Community, which were the forerunner of the broader agreements concluded at the annual meeting of the International Monetary Fund. When the dollar came under renewed pressure, further meetings were held in October and again in February and April of this year at which commitments were made to coordinate policy and exchange market intervention among the leading industrial countries.

The depreciation of the dollar was held in check at the cost of massive intervention by the European countries and by Japan, especially the latter; it was only recently that the United States contributed to this effort. In the first four months of 1987 the United States' balance-of-payments deficit on current account was financed entirely by the increase in liabilities towards foreign monetary authorities.

Intervention alone cannot stabilize exchange rates, however. A greater willingness to cooperate has become evident, but if pronouncements are to be credible and effective they must be translated into corresponding domestic economic measures.

In 1986 the situation of the developing countries was affected both by the pronounced worsening of their terms of trade and by the slowdown in growth in the industrialized world. Whereas the effect of the deterioration in their terms of trade may be estimated at $100 billion assuming constant trade volumes, the increase in the current account deficit of these countries was only $24 billion, thus indicating the scale of their adjustment efforts. The condition of economies that rely mainly on exports of oil and other raw materials worsened considerably. With 1980 equal to 100, the ratio of the prices of non-oil commodities to those of manufactures fell from a peak of 128 in 1974 to an average of 72 in 1986; over the last year the decline amounted to 14 points. Signs of a recovery in raw material prices only began to emerge in the early months of 1987.

The difficulties faced by the most heavily indebted countries grew still more acute. Despite the fall in interest rates and the depreciation of the dollar, debt servicing began to rise again in relation to export earnings. The US initiative of October 1985 made a resumption of economic growth the centrepiece of the programmes of restructuring in the most heavily indebted countries, and assumed the availability of increased finance and a favourable international environment. It has taken longer than expected to reach agreement with the Plan's intended beneficiaries, adjustment programmes have run into difficulties and world demand has grown more slowly than predicted. The deterioration in the terms of trade of the largest debtors was one factor in the swing in their current account from balance in 1985 to a deficit of $12 billion last year. Brazil has suspended the servicing of its medium and long-term bank loans. Following the debt agreements reached a few months ago with Mexico and Nigeria, only those with Argentina and the Philippines are now nearing conclusion.

In 1986 the World Bank essentially achieved the lending objectives set under the Plan, but the contribution from private sources was inadequate, with bank lending to the fifteen most heavily indebted countries increasing by only $4 billion. The initiatives to make the terms on which bank loans are renegotiated more flexible and thus less costly and to encourage the conversion of loans into bonds or other securities should be viewed favourably.

The difficulty of ensuring that the volume of lending from private sources is as large as originally planned and the increase in borrowing requirements mean that lending via official bilateral and multilateral channels must be increased. Despite the agreements to reschedule substantial amounts of debt under the auspices of the Paris Club, the need for significant increases in the resources of the World Bank and the regional development banks and for an expansion in subsidized loans and aid to the poorest countries is becoming urgent.

The Bretton Woods institutions remain the natural forum for strengthening the procedures for international economic coordination, promoting an adjustment in balance-of-payments disequilibria, fostering growth in the world economy and tackling the problem of the developing countries' foreign debt; they have the technical expertise and independence to win acceptance for their appraisals even from the major countries and to promote the establishment of a system in which the costs of adjustment are distributed more evenly.

As to the means of achieving these ends, the route indicated in the report of the Group of Ten on the functioning of the international monetary system published almost two years ago appears to be more valid than ever. Its recommendations are beginning to be implemented both in the activities of the Fund and within the Group of Seven; the multilateral surveillance of member countries' economic policies should lead to operational prescriptions and subsequent checks on their implementation. The ground was prepared by establishing a system of targets and indicators, which reinforces the pool of shared information and gives continuity and objectivity to assessments and subsequent verifications, thus helping foster a recognition of the constraints imposed on the policies of sovereign countries by the interdependence of their economies.

The European countries and the Community

Inflation rates in the European countries continued to converge towards a lower level against the background of a strengthening of the structure of their economies and an improvement in their financial situation. The rate of growth remains unsatisfactory, especially after years of near stagnation; in 1986 it matched the average for the other industrial countries, the expected acceleration having failed to materialize.

The performance of the German economy continues to be weak; activity expanded by one point less than expected last year and the slowdown has accentuated to the point where growth in 1987 is now forecast at around 1.5 per cent. The trend decline in the supply of labour owing to demographic factors is fostering a reluctance to exploit the economy's potential more fully; the unemployment rate has fallen to 8 per cent in Germany, the only one of the four major European countries in which unemployment has declined.

In other countries, some of which still have to make further progress in containing inflation and budget deficits and to consolidate their achievements in these fields, the scope for more sustained expansion is limited by the weakness of growth in the major economies.

The European Monetary System, which has proved its resilience in the face of instability in the world economy in recent years, is entering a new phase. In its first few years it derived cohesion from both external and internal factors, in the shape of the strength of the dollar and the priority all member countries gave to monetary stability. The countries with higher inflation accepted a real appreciation of their currencies in order to curb the rise in prices and domestic costs; currency realignments and even restrictions on capital movements enabled them to overcome the tensions that inevitably developed during the gradual convergence of inflation rates.

The picture is now changing, partly as a result of the system's very success. The slowdown in inflation now allows countries to assign greater importance to expanding employment. The substantial progress made in liberalizing capital movements and opening up Europe's financial markets is limiting the scope for independent monetary policies and may give rise to destabilizing movements of funds. In addition, the decline in the dollar is tending to weaken cohesion among the European currencies.

The exchange market interventions that preceded the realignment of January 1987 were the heaviest since the creation of the EMS. The realignment itself was largely in response to factors unconnected with the behaviour of the fundamental economic variables.

These developments confirm that in addition to the primary need to bring about a convergence of member countries' economies there is a need to strengthen the EMS and adapt its mechanisms to the new conditions.

The completion of a market without barriers to the movement of goods and factors of production requires the Community to resolve the underlying inconsistency between the free circulation of capital, exchange rate stability and autonomy of monetary policy. To seek a solution by relaxing the discipline of the exchange rate agreements would mean sacrificing the contribution that the EMS has made for more than eight years to the stabilization of prices and to orderly trade relations.

Increased capital mobility and the ability to make instantaneous changes in the composition of financial portfolios mean that a number of essential prerequisites must be met; first, a more flexible and coordinated use of monetary instruments in times of tension, with rapid changes in short-term interest rate differentials, secondly closer cooperation in exchange market intervention and acceptance of their monetary impact and thirdly more active management of exchange rates within the permitted band of fluctuation.

Furthermore, the potential increase in destabilizing capital movements necessitates an expansion in Community credit lines and a review of the circumstances in which they may be used; such action would enhance the credibility of the EMS. Financial integration must continue to advance, but it would be advisable to maintain a capability to regulate financial flows through the exceptional and temporary use of restrictions on speculative capital movements, as foreseen in the Treaty establishing the EEC.

The drive to liberalize the financial markets coincided with the enlargement of the Community and the launch of an ambitious programme to integrate and open up markets, which was given concrete form in the Single European Act. To guarantee attainment of these objectives by the deadline of 1992, the capacity for Community policy intervention should be strengthened, whereas in fact it has been weakened by the increased cost of agricultural support and the hardening of defensive attitudes in industry. Integration will not advance unless economic growth assumes equal importance alongside monetary stability in the overall framework of economic policy.

The Italian economy

The last year

In 1986 the fruits of resolute action and favourable external trends combined in a way that had not occurred since the time of the first oil crisis, which had combined with internal disequilibria to lock the Italian economy in the vice of inflation and sap its potential for growth. Last year the tangled skein of problems that had marked the last fifteen years was unraveled.

The growth in output and especially in domestic demand accelerated to 2.7 and 3.2 per cent respectively. The improvement in the terms of trade reduced the trade deficit by 18 trillion lire and brought the balance of payments on current account back into surplus by 6 trillion lire.

Italian firms achieved substantial profits and their investment in plant and equipment was large, higher in relation to GDP than was the case in the other leading European economies. They competed successfully in world markets in which prices were falling. The major Italian groups were also very active in the financial markets and made substantial acquisitions abroad.

The state sector borrowing requirement was held below the 110 trillion lire recorded in 1985. Net of interest payments and settlements of past debts, it was reduced from 47 to 36 trillion lire.

Most important of all, inflation was brought down to an average of 5.9 per cent for the year and 4.2 per cent over the twelve months to December. The present pace of consumer price inflation is the slowest since 1968. The inflation differential between Italy and the other leading industrial countries, which had been nine percentage points at the start of the eighties, has now narrowed to two points.

The statistical picture of 1986 is one of both light and shade, however. The continued rapid rise of 8 per cent in the GDP price deflator indicates the persistence of domestic inflationary factors. Although the trade balance improved substantially at current prices, valued at constant 1985 prices it deteriorated by 7 trillion lire. The budget deficit remains very large, and last year's success in containing it was due not only to action to correct the underlying trends but also to favourable cyclical factors and temporary measures. Though regaining their profitability and credit standing both at home and abroad, Italian firms have not so far shown a renewed inclination to make large-scale investment in additional capacity. The expansion in economic activity created 120,000 jobs last year, but it was not enough to reduce the unemployment rate, which rose further to 11.1 per cent.

The progress made in 1986 was certainly due in part to the depreciation of the dollar and even more to the fall in oil prices, but ultimately it was the result of economic policy measures to tackle the domestic causes of inflation and halt the drift in prices and supply conditions that had occurred at the beginning of the decade.

In retrospect, 1986 was the culmination of a long period of disinflation. The Italian economy has been saved from irreparable harm, but significant problems remain. Unemployment, which is unresolved nationwide and extremely serious in the South, remains a crucial issue; it is the point of reference underlying our analysis of disinflation, corporate recovery, the problem of the public finances, and the external constraint.

Disinflation

In 1980 inflation in Italy was running at 22 per cent. World oil and commodity prices had been rising at an explosive pace of over 30 per cent per year since the beginning of 1979. The rise in the prices of primary products was followed by the sharp appreciation of the US dollar against other major currencies between the autumn of 1980 and the spring of 1985. A large number of Italians feared that inflation would spiral into hyperinflation. Many doubted that it could be curbed, and were even more sceptical that this could be done without stifling the nation's industry.

At the beginning of the decade monetary policy and exchange rate policy were harnessed in a steadfast effort to combat the renewed outbreak of inflation.

The rigorous approach to exchange rate management, which used the discipline inherent in the EMS exchange rate mechanism to good advantage, curbed imported inflation but also necessitated a permanent reduction in domestic production costs. The exchange rate policy could not have been applied, however, if external equilibrium had not been maintained by keeping interest rates high.

The "divorce" between the Treasury and the central bank was the institutional act that consolidated this monetary stance. Its practical effect is summed up in the change from negative to positive real interest rates. Given the widening gap between government revenue and expenditure and the escalating public debt, higher interest rates first eliminated excess demand and then prevented its recurring.

The need to limit the repercussions of monetary stabilization on output and employment and to restore equilibrium without disrupting capital formation meant that the change of course and the implementation of the new policy approach had to be gradual. The momentum of wage and price increases, the limitations of fiscal policy and the imperfections of the market made it impossible to disinflate by means of monetary shock treatment without incurring very heavy real costs.

Attenuated though they were by the gradualness of the process, the costs of the new monetary and exchange rate policies themselves stimulated a growing awareness of the damage caused by inflation and of the need for stronger commitment in the community at large. The changes in the wage indexation system introduced by agreement between labour and management in 1983 and by government decree in 1984, together with easier industrial relations, brought the rise in labour costs back down to levels not incompatible with a return to stability; the expansion in the budget deficit was resisted and policy on public service charges and administered prices sought to reconcile allocative and distributive requirements with the need to avoid fueling inflation.

Although oil prices remained at their peak and the rapid appreciation of the dollar continued, the convergence of the various components of economic policy brought inflation down to single figures by the autumn of 1984. After a pause due chiefly to the restoration of profit margins, inflation declined to its present level during 1986, aided by the favourable global environment and the expectations engendered by a succession of economic achievements.

This protracted battle against inflation did not prevent employment from continuing to rise, in contrast to developments in the rest of Europe. The problem of unemployment nevertheless grew more acute, mainly owing to the growth of the labour force.

Between 1980 and 1986 the demand for labour increased by 1.8 per cent, but the labour supply expanded by 5.8 per cent, propelled by population growth and a rise in the participation rate among women. The demand for labour was depressed by slow economic growth and by the fact that this period saw the industrial restructuring made necessary in the first half of the seventies by changes in international and domestic income distribution and relative prices. The rise in the unemployment rate amounted to 3.5 percentage points, two points less than the average for the major European countries.

Employment contracted by 1 million in industry and by 500,000 in agriculture, but the services sector, both public and private, created 1.7 million jobs, more than a third of them in services to enterprises. The faster growth in the labour force in the South caused the unemployment rate there to rise by five points to 16.5 per cent. In the Centre and North it rose by three points to 8.5 per cent.

A renewed strong commitment to the development of Southern Italy is indispensable to any lasting reduction in unemployment. Forecasts for the coming decade have long made it clear that whereas in the Centre and North the contraction of the population of working age will reduce the excess supply of labour, in the South unemployment rates will continue to rise. Substantial resources have been appropriated for the South. If they are not to be wasted, the institutions laid down in the long-range plan must be fully operational, entrepreneurs must have scope for initiative and there must be continuous and careful checks to ensure that government action is consistent with the objectives.

The improved health of the business sector

The phase of disinflation largely coincided with the recuperation of the business sector. In fact, the two processes have some causes in common and have reinforced one another.

Ten years ago it seemed that if entrepreneurship was to survive in Italy small firms had no option but to use semi-legal labour nor large ones any alternative but to accumulate debt that would be eroded by negative real interest rates.

At the beginning of the eighties the new orientation of monetary and exchange rate policy led some observers to fear the impoverishment of Italian industry, despite the expansion in profits and investment it had enjoyed from 1978 to 1980.

The spectre of deindustrialization did not materialize, however. The strict stance on exchange rates and real interest rates maintained during the eighties has forced large firms to adapt to the changed pattern of prices and costs and it has not deterred smaller businesses, where adjustment was already under way. The process was greatly assisted by the re-emergence of wage restraint and the development of an industrial relations climate more favourable to the pursuit of improved productivity. Both of these factors helped curb the rise in unit labour costs, and substantial transfers of public resources relieved firms of the cost of overmanning and helped offset corporate losses.

The recovery of the business sector was an important element in the fight against inflation. Productivity growth, which curbed prices as well as unit costs, was generated by new investment, new technology, new combinations of resources and product innovation; the fact that the expansion in economic activity, though slow, was faster than that achieved in other European countries was a further contributory factor. The decline in inflation, in turn, enabled firms to plan ahead with greater certainty.

Despite stronger stimulus and the improved economic climate, the recuperation of the corporate sector would not have been possible if management and workers had not shown an ability to resolve the problems of the seventies. That ability has been proven.

The response differed in kind and in timing between small and large firms and, among large ones, between the private and public sectors.

The available data on the eighties show that small and medium-sized firms grew steadily, unaffected by cyclical variations. From 1981 to 1984 the output of industrial units with between 20 and 100 employees grew by 5 per cent per year and was higher than the national average, employment rose by 1.5 per cent annually and investment continued to grow at a pace not far short of that of the 1978-80 expansion. In 1984 their gross profit margin rose to 38 per cent of value added. Their borrowing was heavier than the average for enterprises as a whole, but the cost was covered by their operating profits.

In large firms, the modernization of plant and the reorganization of production began when it became clear that competitiveness could no longer be fully recouped by devaluation nor would debt be eroded by negative real interest rates. Between 1981 and 1984 large private and public sector industrial firms raised productivity by 9 per cent per year; labour inputs were reduced at an annual rate of 7 per cent. Companies also reorganized their finances; in relation to value added, debt declined by 16 percentage points and gross interest charges by 6, while financial income doubled.

The overhaul of production and organizational arrangements in the large public sector companies was hampered by the fact that they are heavily represented in the most severely troubled industries. Initially it was also delayed by the persistence of the view that they should contribute directly to the maintenance of output and employment. The process of change was eventually set in motion by the trend towards reducing the state's role in the production of non-strategic goods, which took hold in Italy and elsewhere.

Turning from past accomplishments to the present and the prospects for the future, we see that some of the problems facing the business sector are unique to one or other of the three types of enterprise; they can be tackled by exploiting the complementary features of the different kinds of firm.

Large private sector companies have channeled increased resources into financial investments and the acquisition of equity in other firms, both at home and abroad. Investment in equity participations has been prompted to some extent by the discrepancy between the underlying economic value and the stock market valuation of many firms. Above all, given the slow expansion of world demand, in certain industries the acquisition of subsidiaries is not only less costly but also less risky than the construction of new plant and is undertaken for specific purposes, such as better access to markets and to technology, more efficient links between different stages of production, and risk diversification. Traditional economies of scale are becoming less important, whereas greater significance is being attached to scope economies and to the integration of information technology and services into the production process.

Large Italian industrial groups have laid new stress on the international dimension of their business. In 1986 net direct investment abroad was the equivalent of two thirds of Italy's current account surplus and involved a number of very large transactions. The Bank of Italy ensured that the foreign exchange flows associated with these transactions and with a substantial disinvestment in Italy by non-residents were orderly.

The strategic consistency and profitability of foreign investments depend on the sound judgement of senior management. The availability of liquid assets gives firms greater freedom to implement their policies, but at the same time it increases the danger that the pursuit of short-term capital gains may distract them from the ultimate goal of producing goods and services.

Macroeconomically, the benefit that may derive from foreign subsidiaries comes via the balance of payments. The soundness of major firms' investment decisions will determine the scale of their contribution to easing the external constraint, and thus creating employment, in ways that will complement their traditional contribution as exporters of goods and services. The Italian economy is not yet sufficiently mature to become a permanent net exporter of capital. Balanced resource allocation requires that the capacity of firms to employ labour and to overcome the remaining manifestations of economic backwardness be strengthened.

The action that remains to be taken to complete the rehabilitation of public sector enterprises will be able both to exploit and to help consolidate the improved economic situation of the country. Public sector enterprises can make a substantial contribution to improving the infrastructure essential to the overall efficiency of the economy. Transportation and telecommunications are particularly important in this regard; the productive potential made possible by information technology cannot be developed fully without extending and modernizing the nation's telecommunications network.

Notwithstanding the advances that have made small and medium-sized firms a strong component in the Italian economy, firms of this size are encountering difficulties, and not only in expanding. Innovation continues to be spread thinly; moreover, the replication of the North-South divide among small firms on a number of fronts such as productivity, business start-ups and profitability is a further cause for concern. The financial weakness of small businesses is exacerbated in the South, as can be seen in their greater recourse to bank loans and their lower debt servicing capacity. Now and in the foreseeable future, the continued creation of jobs depends principally on the vitality of small and medium-sized firms, but an adequate growth in employment cannot be achieved if large firms do not play their part.

The problem of the public finances

The glaring productivity gap between the public and the private sectors affects the ability to compete, to produce and to create jobs in an economy that is increasingly integrated with the rest of the world. A growing volume of private resources is being spent to make up for the shortcomings of the government sector. The citizens of this country realize the urgent need for a vast improvement in the efficiency of public services as a means of enhancing the functionality and cohesion of a civilized society.

Regulations and procedures must be streamlined. Conformity with the precepts of good management and impartiality, which Article 97 of the Constitution establishes as the standard in the administration of public offices, must be assured by rules for monitoring performance and by a closer correspondence between performance and earnings. First and foremost, better services presuppose new patterns of organization.

The central government budget must be restored to its proper role as the indispensable instrument of government: the guarantor of the provision of public goods essential to society, a flexible tool for the regulation of the economic cycle and a reliable point of reference for balanced economic growth. The revitalization of the public sector presupposes not only reform of the structure and operations of the public administration but also a thorough revision of budget procedures and action to moderate expenditure trends and sustain the growth in revenue.

In the spring of 1986 the Budget Committees of the two houses of Parliament supported experimental changes to streamline the budget's passage through Parliament and deepen the involvement of the executive branch in decisions regarding budgetary policy. The aim of the modifications is to bring forward decisions on medium-term planning objectives, to ensure that the framing of such objectives takes account of actual trends in public finances, to make achievement of the desired results more certain and to restore the original function of the budget as an integrated instrument of macroeconomic policy by excluding measures for specific sectors, such as health, social security and local government finances.

The short time available for drafting the economic and financial planning document and the Cabinet crisis of July 1986 made it impossible to apply the new procedure in full for the 1987 financial year. When it is fully implemented in future years it should be complemented by an assessment of the trend in the public finances and the cost of bills entailing expenditure, a task that should be entrusted to a technical body.

Despite the progress made in 1986, the persistence of factors that give rise to serious concern about the public finances in both the short and the long run confirm the urgent need to limit the budget deficit.

We are not blind to the difficulties that must be overcome by the Government's budget proposals, which hinge on achieving a balanced budget net of interest payments. Above all else, an awareness of the problems involved should reinforce the Government's resolve to keep the expansion of current expenditure down to the rate of inflation.

The effects of long-term social, economic and demographic pressures need to be resisted or offset. In the pensions field, the provision of welfare assistance should be made more strictly conditional upon effective need, the criteria for eligibility should be reviewed in order to increase the redistributive effect of expenditure on pensions and the retirement rules should be amended to reflect changes in society. In the health service, efficiency must be improved in order to reduce costs and raise the standard of service. Grants to industry must be directed more specifically to raising productivity and expanding the productive base, and their size must take account of the recovery in corporate profitability.

The need to increase tax revenue as a share of GDP as one of the ways of restoring budget balance is demonstrated by the persistence of tax avoidance, tax evasion and erosion of the tax base. The scale of these phenomena has been made more evident by the recent revision of national income.

Merely maintaining the incidence of tax at its present level will require prompt action, since certain sources of extraordinary revenue will soon dry up. Above all, progress must be made in tax reform, designed not only to produce a permanent rise in revenue but also to eliminate distributive inequalities and distortions in the use of resources, to lower some tax rates (partly in order to reduce the incentive for evasion), to adjust the balance between direct and indirect taxation and to extend automatic collection procedures. To stabilize local finances, charges for certain services should be linked more closely to the cost of provision. The unification of the European market will itself necessitate a review of existing tax systems, primarily with a view to standardizing the basis and rates of indirect taxation.

The balance-of-payments constraint

The failure to restore the public finances to equilibrium is eroding the competitiveness of the entire economy and the availability of saving. It is exacerbating the constraints imposed by the balance of payments on growth and employment.

The turnabout in the terms of trade in 1986 made good about half the deterioration that had taken place in the period covering the first and second oil crises. However, there is inherent instability in the relationship between world prices of manufactures and those of primary products. Competition has been accentuated by the slowdown in the growth of world trade. The position of Italian industry is not without its weak points, at a time when the manufacturing sector, on which Italy relies to balance its external accounts, is being called upon to offset a deterioration in the other main items of the balance of payments on current account.

Net foreign exchange earnings from tourism, which were already making a far smaller relative contribution to the current balance than they had until the early sixties, have been affected in recent years by a loss of competitiveness compared with other Mediterranean countries and the rising propensity of Italians for foreign travel.

Net receipts from private transfers have declined perceptibly. Net outflows on account of public transfers are increasing, owing to Italy's position in the international community and its increased commitment to international cooperation and development assistance.

The financing of the external payments deficits of the eighties has generated a net external debtor position whose interest costs amount to 4 per cent of current foreign exchange earnings.

Regardless of cyclical variations, the energy question remains the crucial factor in Italy's external constraint. Since 1970 the ratio of overall energy requirements to GDP has diminished by 16 per cent, less than in other countries. The proportion of energy demand met by domestic production did not change significantly after either the first or the second oil crisis; it remains below 20 per cent. A selection of domestic and international scenarios for the next decade show that growth rates of the order of 3 per cent a year, which would barely be sufficient to avoid aggravating the difficulties of the Italian labour market, would entail a steady rise in the deficit on the energy account to about 3.5 per cent of GDP by the end of the period, as against 2.2 per cent in 1986.

Major and unavoidable policy choices must be made urgently in the energy field. If they do not lead either to energy savings or to the production of energy at lower import cost, the increased energy imports connected with economic expansion will have to be offset by a corresponding increase in Italy's foreign exchange earnings from trade in other products. This implies forgoing increased consumption of consumer goods and presupposes an ability to raise competitiveness in order to win a larger share of world trade.

Italy's deficit on trade in foodstuffs and food products is substantial and rising even at constant prices; in 1986 it reached 12 trillion lire.

The slowdown in the expansion of demand from the OPEC countries, followed by the depreciation of the dollar and more recently by the erection of barriers to penetration of the markets of the Far East have prompted Italian manufacturers to strengthen their presence in European markets, which are highly competitive and already account for more than half of Italian exports. The stance adopted by large Italian firms towards Community-wide operations is a response to this challenge, as is the recovery in productivity and profitability achieved by the industries that are the most prominent in world markets.

Italian society needs rapid as well as stable economic growth, and it has the resource potential to achieve it. Action to encourage exports must certainly include measures targeted at individual sectors, but more important it must create favourable general conditions. Inflation has been curbed, though not conquered, and the industrial fabric has been revitalized; these are now realities. The same cannot be said of reform of the public administration and the restoration of a sound budget, on which the overall efficiency of the economy is crucially dependent. If the constraints on the expansion of output and employment are to be eased, it is essential that resolute action be taken in these areas and that business and labour do not abandon their commitment to price stability and the consolidation of the corporate recovery.

The outlook for 1987

In these first few months of 1987 the world economic outlook has turned gloomier. World trade is slowing down. The downward trend in the dollar prices of major raw materials is being reversed. The price of crude oil has risen to the level of February 1986.

In Italy the gap between the rate of expansion of domestic demand and that of GDP that emerged in 1986 is widening. In March the capacity utilization rate in industry came close to the high levels achieved in early 1980. New labour contracts have further boosted households' disposable income; the acceleration in consumer spending, which is still benefiting from last year's improvement in the terms of trade, is threatening to crowd out investment by firms, which is expanding rapidly.

It is uncertain whether the planned reduction of 10 trillion lire in the public sector borrowing requirement by comparison with 1986 can be achieved. Far from declining in line with the annual target, the requirement for the first few months of 1987 was similar in absolute terms to the figure for the same period of last year. Expenditure will rise during the remainder of 1987 as the full effects of new labour contracts with public employees make themselves felt.

Domestic demand seems to be expanding more quickly than in the other leading industrial countries. The trade balance shows a widening gap between expanding imports and stagnating exports. In the first four months of the year the surplus on trade in non-energy products was 3 trillion lire less than in the same period of 1986. The oil deficit has worsened month by month. Last year's balance-of-payments gains are being eroded more rapidly than had been expected.

The twelve-month rate of consumer price inflation has stabilized at around 4.2 per cent; wholesale prices have begun to rise once more.

The trend in the prices of manufactures must be brought permanently into line with those in Italy's main competitors. In an international environment in which the forces of stagnation are threatening to prevail over those of expansion, it is essential to maintain competitiveness. Now that the nationwide labour contracts have been concluded, it is up to individual firms to defend their competitiveness, chiefly by seeking to improve productivity and, where necessary, holding down their profit margins.

During these four months, the action of the Bank of Italy has been directed first and foremost to moderating the growth of credit to the private sector. After an acceleration early in the year, bank lending in lire and in foreign currency slowed down in March and April, bringing the annual rate of expansion in the first four months back down to 10 per cent. Over the same period, credit to the non-state sector expanded by 11 per cent. Partly as a result of weak demand for government securities, deposits have been growing at a faster pace since March, thus threatening to obstruct the slowdown in bank lending.

Firm monetary and exchange rate policy will be required to keep the Italian economy on a stable growth path that is not jeopardized by renewed balance-of-payments deficits or resurgent inflation.

Money and finance

Like its counterparts in other industrial countries, the Italian financial system is going through a period of rapid change involving markets, intermediaries, savers and enterprises.

In the strategy adopted by the Bank of Italy, the measures affecting the structure of the financial system and the conduct of monetary policy have both been directed towards the goal of reducing inflation. The success achieved does not terminate our commitment to stability, but rather spurs us to speed up the modernization of the financial system and enables us to proceed with the liberalization of exchange controls.

The need to advance on these three fronts makes it even more urgent to ease the constraints placed on monetary policy by the large public sector deficits and the high level of government debt. The progress already made with the refinement of monetary policy instruments is evident in our day-to-day operations; this continues to be an important activity, but it cannot take the place of the more rigorous measures required to correct the imbalance in public finances that is impeding the development of the Italian economy.

The development of the financial system

Direct financing of the public sector by private investors has intensified in line with the protracted decline in bank deposits as a proportion of financial assets.

The changes in corporate financing are of more recent date, but they have occurred very rapidly; the stock market has been revitalized by the improvement in the condition of the business sector and by the inflow of resources via investment funds and portfolio management services. In 1986, 19 per cent of the flow of resources to the productive sector, the bulk of which went to the major industrial groups, was raised through share issues, compared with an average of 6 per cent in the ten preceding years.

Large firms have devised new forms of financial operation and are occasionally acting as financial intermediaries. They are combining their increased profitability with a willingness to manipulate items on both sides of the balance sheet; financial assets are viewed both as cash management instruments and as a means of attack or defence, while liabilities are taken up not only for productive purposes or to finance investment but also to make financial acquisitions, sometimes in the context of takeover battles.

Compared with the situation in the mid-seventies, the Italian system of financial intermediation now offers a far wider range of instruments and institutions, more in keeping with the level of economic development the country has achieved and better able to cope with complex processes of resource allocation. As it has evolved, however, it has developed mechanisms, weaknesses and potential abnormalities that make it necessary to reconsider the current arrangements for protecting savings and regulating the currency.

Macroeconomic control requires a coherent view of the process whereby savings are transferred from surplus to deficit sectors. Supervision aimed at protecting savings and ensuring the stability of financial intermediaries, to which I shall return later, is necessarily more thorough in regard to credit institutions and to instruments that are close substitutes for bank credit and money.

The monetary policy implication of the greater diversity of the credit system is that the link between the action of the central bank and the public's expenditure decisions tends to depend more crucially than in the past on interest rates and less on the availability of credit. With a greater variety of financial instruments, it is more difficult for one monetary or credit aggregate alone to reflect the state of the economy and serve as a basis for policy. The method adopted by the Bank of Italy, which involves establishing and announcing several objectives within a coherent flow-of-funds framework, suits this new reality. The use of the econometric model enhances the consistency of monetary policy action and underlines the role assigned to the final objectives.

Developments in the monetary and credit aggregates in 1986 and early 1987 reflect and confirm these considerations. Last year the M2 money supply expanded at a rate of 9.4 per cent, thus remaining close to the middle of the target range; the rate of change in the money supply net of certificates of deposit and in monetary base was more modest, 8.2 per cent in both cases. Credit to the private sector expanded by 11.5 per cent, however, significantly faster than the target of 7 per cent, owing to an acceleration from the autumn onwards.

The heightened competition among the banks for the business of major firms manifested itself in a sharp expansion in the volume of credit granted, which was more than seven percentage points higher than the growth in credit actually used. Developments such as this give rise to fears that in their pursuit of business the banks sometimes go beyond the limits dictated by the optimization of operating profits and resource allocation. On the demand side, the need for funds to finance investment and production was augmented by demand associated with companies' financial operations carried out at home and abroad. In 1986 firms acquired almost 17 trillion lire more in financial assets than in 1985, mainly on account of increases of 8.5 trillion lire in shares, 4 trillion lire in trade credit and foreign loans and 2.5 trillion lire in liquid assets. The fact that a considerable proportion of bank lending was used for financial purposes is also apparent from the volume of bank loans granted to financial companies and the large groups that are most active in the share market.

Although the behaviour of the exchange rate, inflation and output was in line with the targets, steps were taken to counteract excess lending to the non-state sector; liquidity could have flooded out of the financial sector into the real economy, causing uncontrollable short-term disequilibria. In the last quarter of 1986 money market intervention kept the banks' gross liquidity at around the normal level and reduced their net liquidity from 3 trillion lire to a negative figure of 4.5 trillion; the average rates on securities repurchase agreements rose by four percentage points. Inflows of foreign exchange following the EMS realignment in the middle of January 1987 exceeded the outflows that had occurred in the preceding weeks.

The authorities also responded to the excessive growth in lending through closer concertation with the major banks. The reduction in the discount rate on 13 March and the introduction of the reserve requirement on increases in the banks' net foreign currency liabilities made conditions less attractive for inflows of foreign capital. The second of these measures not only serves the cyclical objective of curbing the banks' fund-raising abroad but also strengthens the system for regulating banks' liabilities.

Recent experience has confirmed both the success achieved in developing indirect monetary control instruments and the need for further progress. The Bank stepped up its repurchase agreements in government securities in order to increase the effectiveness of its actions; in 1986 it carried out 65 such operations involving a total of 137 trillion lire, compared with 51 transactions amounting to 66 trillion in 1985. The turnover of the interbank market and the number of participants have increased, but greater variety in the types and maturities of contracts and in trading mechanisms would be desirable. As regards measures to improve the payments system, the overhaul of the procedures for accessing centralized accounts and effecting clearing operations will enable the interbank market to operate throughout the day and access settlements in their accounts at the central bank in real time from anywhere in Italy.

The new regulations concerning certificates of deposit are designed to improve the transmission of monetary policy stimuli. The banking system has responded positively; between the end of August 1986 and April 1987 the volume of certificates in circulation almost doubled to 30 trillion lire. Crediting interest on deposits more frequently, as is the custom in other countries, would ease the seasonal fluctuations in the money market now caused by the practice of crediting interest only once a year.

The authorities influence the composition of financial portfolios not only by means of monetary instruments and measures to protect savings but also through taxation.

As a result of the 1974 tax reform, taxation has been extended to all financial assets and all forms of income, tax rates have been standardized, distinctions between different categories of issuer have been eliminated and the taxation of dividends and income from investment fund units has been simplified. Further important steps remain to be taken before the system may be considered coherent; there are still areas in which the tax base is being eroded, in particular with regard to capital gains on shares. It is difficult to see any logical uniformity in the plethora of indirect taxes on financial transactions, with the result that the working of the financial market is distorted. Businesses are moving away from heavily taxed instruments such as bills of exchange and making greater use of others, such as "bankers' receipts", that are less well protected legally but preferable from the point of view of tax; the duration of loan contracts and even the distribution of flows among intermediaries are being influenced by taxes that ultimately yield little revenue.

Financial integration and the liberalization of exchange controls

The integration of Italy's national financial market into the international system first entailed removing the administrative constraints imposed on foreign transactions from the early seventies onwards. The gradual dismantling of these restrictions over the last few years proceeded in line with the improvement in the general state of the economy and was concluded by the measures taken three weeks ago.

Further progress will be made with the introduction of the decrees for which Law 599 of 26 September 1986 provides. The Bank of Italy's own contribution to the formulation of the decrees is based on a broad interpretation of the freedom to engage in foreign transactions within the limitations set by the Law; the legislation confirmed, inter alfa, the

Foreign Exchange Office's monopoly of foreign exchange operations and the criminal nature of foreign exchange offences, provisions that have no counterpart in the other countries of the Community. We are firmly of the opinion that the complete integration of Italian firms into the world market in goods, capital and financial services cannot be postponed, even if the disequilibria that halted the liberalization of exchange controls begun so courageously in the fifties and continued in the sixties have not been completely eliminated.

Operating in an environment of increased capital mobility will require Italian monetary policy to be oriented even more strongly towards stability and to pay greater attention to monetary conditions in other countries. It will mean facing the repercussions of an adjustment in residents' portfolios on a scale that is difficult to estimate after a long period of rigid control. Even after the transitional period, larger and more frequent changes in interest rates may be necessary, since the lack of exchange controls will make capital movements more sensitive to exchange rate expectations.

The decision to advance along the road of liberalization stems from a deeply-held conviction of the social and economic needs of a modern industrial country. This in no way lessens the challenge it entails. The Bank of Italy has taken care to strengthen the foreign exchange reserves, which constitute the first line of defence. Appropriate action must now follow at both domestic and international level to complete the revitalization of the economy and to ensure that the international community cooperates in the way required by closer international interdependence.

Monetary control and Treasury financing

In the light of the new configuration of the Italian financial system and its integration with the rest of the world, the question of the linkage between the behaviour of the public sector and monetary management arises with renewed urgency. Although the trend increase in the public sector borrowing requirement that had lasted since 1979 was broken last year, government debt still grew by 17 per cent, a rate six points faster than the growth in national income.

A more vigorous policy to restore sound government finances would allow a less rigid monetary policy, which in turn would reduce the burden of public debt since lower interest rates would help boost economic growth and cut government expenditure. It is in this way that monetary policy can ease the burden of the public finances. The ratio of the borrowing requirement to the annual expansion in monetary base, which is currently around ten to one, shows how illusory it would be to believe that the financing of the public sector can be facilitated by expanding the money supply without running the risk of rekindling inflation.

Short-term or floating rate securities still make up 83 per cent of outstanding government debt; in 1986 net issues of medium-term fixed rate securities accounted for more than 30 per cent of the borrowing requirement, the highest percentage for many years. At a time of renewed confidence in the purchasing power of the lira, the willingness of savers to invest at fixed rates for periods of several years was also fostered by the structure of interest rates. The demand for fixed rate securities has weakened in recent months.

The impact that the financial behaviour of the state sector has on monetary policy also stems from the pronounced short-term volatility of the borrowing requirement. The practice of setting a ceiling on tender rates close to the market rate and the mechanism of the Treasury overdraft facility with the central bank mean that imbalance between the demand for government securities and the supply affects banks' reserves, despite the "divorce" between the Treasury and the Bank of Italy. Since it is impossible to achieve market equilibrium by determining in advance both the interest rate on securities and the issue volume, it would seem advisable to fix the quantity of paper offered and let demand determine the price in the case of short-term borrowing, and to do the opposite for medium and long-term securities. In accordance with this approach, the recent decision to issue medium and long-term government securities on pre-arranged terms and to leave open the quantity on offer avoids inflated applications made solely to gain an advantage in the allocation of securities and creates more orderly market conditions. Likewise, with regard to Treasury bill issues the cessation of the present practice of setting floor prices would allow the auction method to operate properly again and give more effective control over liquidity. The liberalization of exchange controls has made it even more necessary to have operational arrangements that give interest rates the complete flexibility required for management of the currency.

The protection of savings and the structure of the credit system

The growth of intermediation outside the credit system and the advisability of regulating and controlling such business were widely discussed last year and were the subject of several studies, some initiated by the authorities. The analysis of the causes of this development and of its nature, scale and implications for the protection of savings and the effectiveness of monetary policy confirmed the need, which proved to be universally accepted, for all forms of financial intermediation to be appropriately regulated, in line with the tendency in most of the other industrial countries.

Asked to give Parliament the benefit of the Bank's experience and judgement, I recommended that suitably graduated supervision should be introduced for the forms of financial intermediation that are now exempt, with the aim of promoting stability as well as transparency and proper practices. Prudential controls should not be restricted to banking and banking-related activities. On the other hand, the aim of forestalling instability and protecting savings can and must be pursued in conjunction with those of streamlining operations, improving intermediaries' efficiency and enhancing competition between them. As regards the assignment of supervisory duties, arrangements will have to be developed that avoid a dispersion of responsibility for the controls designed to defend stability. These need to embrace the totality of banks and financial intermediaries and require a systemic view of the problems involved, coupled with scope for rapid operational intervention.

Pressure for change, both in the banking and financial system and in the regulatory and supervisory framework, is also being generated by the international integration under way in this field. In the EEC the aim is to establish a single market by the end of 1992, with complete freedom of establishment for intermediaries and freedom to provide financial services under uniform rules. This objective is to be achieved through harmonization of the basic rules by means of Community Directives, which now only require majority approval, and leaving other national features to be dealt with by mutual recognition.

In the last twelve months the Interministerial Committee for Credit and Savings and the Bank of Italy have given strong impetus to change in the structure of the credit system by completing the implementation of several elements of a design for a new configuration of the credit system. In addition to the provisions regarding mandatory capital ratios, relationships between banking and commerce, and banks' branch networks, which I shall discuss later, decisions were taken on banks' operations beyond the short term and their investments abroad, merchant banking activities, the Interbank Deposit Protection Fund, supervision on a consolidated basis, and the abolition of all geographical restrictions on the operations of foreign banks' branches.

Bank capital

Bank capital, which represents the resources provided by investors, is of special importance in view of the amount of savings entrusted to banks by third parties and the risk inherent in loans to customers.

In recent years the Italian banking system has shown a good capacity for building up its capital base, the strength of which now compares favourably with that of other banking systems, though the aggregate figure hides considerable differences between individual banks. The ratio of capital and reserves to total customer deposits has risen over the last five years from 7 to 11.6 per cent. Share issues by large banks made a substantial contribution to the 3.6 trillion lira increase in own funds in 1986: public-law banks raised 800 billion lire and the banks of national interest 1 trillion. Since then, the latter have made additional issues totaling 2 trillion.

The recent measure introducing mandatory minimum capital ratios for banks is in response to the need to buttress stability in a phase of growing competition. It became possible to adopt these provisions, which give binding force to indicators that were already in use, after a period devoted to building up banks' capital and reserves, developing the share market and making the changes required to enable public sector banks to have access to it. Similar rules to those applied to banks should be introduced both for special credit institutions and for other types of financial intermediary, thereby helping to make competitive conditions more uniform.

The capital adequacy requirements will intensify the stimulus for banks to improve their efficiency and enhance their entrepreneurial skills. The determination of different capital ratios according to the theoretical riskiness of the various categories of assets confirms the neutrality of the supervisory authorities with respect to banks' operating choices and is consistent with the easing of entry controls and restrictions on operations. Banks will thus be freer to adopt the strategy of their choice, but their plans for growth will depend much more on their ability to generate profits, and hence to create or attract the necessary capital. The link between earning capacity and volume of business, between the profit and loss account and the balance sheet, will become much closer.

Compliance with capital ratios is a necessary, but not a sufficient condition for sound operations. They complement but do not replace the supervisory authorities' assessments of the quality of banks' assets as a whole, of their balance sheet strength and profitability, and of the effectiveness of their internal organization and control procedures, which are appraised on the basis of prudential returns and inspections.

The new regulations imply that part of the Italian banking system will have to find additional capital. At the end of last year, 130 banks, or slightly more than one tenth of the total number, were below the minimum levels now required and will need to raise an estimated 4 trillion lire to make up for the deficiency. Taken together, the other banks had a surplus of 16 trillion.

One of the factors contributing to the need for capital and reserves is the increase in risk that has occurred recently. Over the last five years bad debts have risen from 4 to 6.7 per cent of total loans and are now equivalent to one third of own funds, including loss provisions. The general improvement in economic conditions has not prevented this development; small and medium-sized firms have come to account for a larger proportion of bank lending and their generally higher failure rate results in a greater incidence of bad debts.

For enterprises, and hence also for banks, the ability to generate profits is the primary guarantee of continued capital strength. The operating profit of the Italian banking system has risen over the last ten years from 1.2 to 1.8 per cent of its total assets. However, if the accounting figures are adjusted to give a reasonable return on the growing volume of own funds, profitability is found to have fluctuated slightly around a constant value. The flattering results achieved in 1986 were due in part to factors such as the temporary reintroduction of the ceiling on bank lending and the very large increase in income from securities business. Looking ahead, banks' profitability will depend on their ability to cope with fiercer competition; they will come under increasing pressure to rationalize operations by reducing costs, exploiting market opportunities and improving their organizational efficiency.

Many of the banks that do not meet the capital requirements at present are either small or medium-sized. The merger of structurally weak banks with stronger ones would be an appropriate response to the demands of minimum ratios, insofar as it would promote a better distribution of the capital resources of the banking system as a whole. Equity participation in Italian banks by foreign intermediaries could also serve to strengthen their capital bases and could bring about the exchange of operating know-how made necessary by European integration and international competition.

Households and firms also provide banks with capital. If these flows are to last and grow larger, banks will have to achieve results that will allow their securities to provide competitive yields.

The contribution that non-financial firms can make to banks' capital is restricted by the need to protect the autonomy of banking. The objectives of allocative efficiency and stability of the banking system have resulted in the separation between banking and commerce being adopted as one of the cornerstones of our banking legislation. Recent developments in industry and finance led the Interministerial Committee for Credit and Savings to reaffirm the principle of separation and to protect it by administrative means, giving the Bank of Italy responsibility for preventing the creation of credit institutions dominated by non-financial firms or groups, tightening the restrictions on connected lending, and encouraging intermediaries to add provisions to their Statutes to avoid preferential treatment being given to shareholders and associated companies.

The separation between banking and commerce regards the acquisition of controlling interests, but not minority interests. As I indicated to Parliament last autumn, minority interests are not only a source of capital but can also serve as a means of transferring the entrepreneurial expertise of industrial firms to banks.

The capital base of the special credit sector has also been strengthened. Own funds more than doubled over the last five years, with those of the industrial credit institutions rising from 11 to 15 per cent of their total borrowed funds and those of the other categories from 7 to 11 per cent. After the substantial recapitalizations charged to the budget in the wake of the crisis in the chemical industry, self-financing has been the main source of new capital, supported by steadily rising profits until 1984. In the last two years this improvement has come to a halt, while the tendency for lending risks to increase has persisted.

In the future, many special credit institutions will have to meet part of their capital needs by drawing on external sources, both by enlarging the shareholder base of those in public ownership and by issuing forms of equity in the capital markets.

The same economic logic that requires private sector credit institutions to remunerate the owners of their equity and to compete for the capital they need must also apply to the banks and special credit institutions in the public sector. Where it constitutes an obstacle, the regulatory framework will have to be changed, in conformity with the principle of competitive equality between credit institutions, defined by law as enterprises irrespective of their public or private status.

The specialization of credit intermediaries

The criterion of specialization is one of the features that serves to distinguish the structure of a financial system. In the industrial countries the financial products and services supplied are basically the same, though their relative importance differs. The manner in which the supply of these products is divided among the various types of operator in each system defines its specialization boundaries. These vary both from one place to another and from one period to another, but some differentiation of operations between categories of intermediaries is always present because it reflects the advantages deriving from skill specialization, simplified management and the spreading of risks.

The categories of credit intermediaries currently to be found in the various financial systems were mostly established in the period following the banking crises of the thirties. Thus, in Italy we have the 1936 Banking Law with its emphasis on the distinction between banks and special credit institutions. As in other countries, the continuous, if irregular, development of new instruments and intermediaries has been coupled with an erosion of the boundaries of specialization. Both these tendencies have gathered pace in the last few years. The creation of a European financial market will involve a narrowing of the differences between financial categories and structures.

Rather than being a hindrance to Italian intermediaries' competitiveness, the rules governing our financial system can be arranged to provide an institutional and organizational framework permitting customers' diversified requirements to be satisfied as effectively as possible. Within a group that is managed in the light of one overall strategy, old and new elements can have not only specific functions but also separate legal identities and capital, as well as autonomous fund-raising capabilities.

The solution based on a group of diversified companies with centralized control will be suitable for only a small number of major organizations. Within this structure it will be possible to include the whole range of intermediaries that has been developed over the years, as well as other entities in which non-financial companies will be free to participate, provided they do not violate the separation between banking and commerce. The implementation of such a blueprint will require the creation of clear divisions between the operational spheres of the various parts making up the group.

Small and medium-sized credit institutions will continue to have a key role to play in the financing of the economy. In their case operational diversification and the search for the optimal size of activities may be achieved best not by adopting the centralized group model but by individual banks creating links and arranging other forms of cooperation.

The choice of a financial group's structure and functions lies with the governing body of each parent company. The instruments for exercising control and the whole regulatory framework will have to be extended and used to take account of such financial conglomerates. The supervisory authorities will cooperate in defining the content of the various specializations and the requirements for their mutual independence.

Branch policy

The granting of credit, the taking of deposits and the operation of the payments system all require close contact with customers, and hence a branch network. In view of its implications for efficiency, competition and stability, the configuration of the branch network forms part of supervisory policy. The authorities have made active use of their regulatory powers in this field.

Door-to-door methods of selling financial products involve relations with customers that contain an element of risk. The protection of savers requires that these methods should be regulated by forbidding the supply of banking products in the strict sense (a function reserved exclusively to bank branches) and limiting their use to the distribution of uniform and highly standardized products, such as investment fund units.

The authorization of more than 500 new branches in 1986 is the latest step in a rationalization programme that the supervisory authorities have implemented through successive branch network plans with the aim of fostering an orderly expansion of the banking system and triggering competition by breaking down the longstanding geographical segmentation of the banking market.

We have now entered the phase designed to allow banks to organize their own networks. They have already been authorized to transfer branches within specified areas without restrictions. Since September the installation of automated teller machines has been considerably liberalized. Pursuant to a recent resolution of the Interministerial Committee for Credit and Savings, the Bank of Italy will authorize the transfer of branches between banks and standardize the different categories of branches, thereby allowing those performing a limited range of operations to become full branches. A new simplified authorization procedure will increase the scope for relocating existing branches, with the Bank of Italy assessing only the acceptability of individual bank's technical and organizational structures. Looking ahead, it will be possible to adopt a similar procedure for the authorization of new branches.

Ladies and Gentlemen,

In these concluding remarks I have referred more than once to the phase of disinflation that has been under way since the start of this decade. In retracing the main developments of this process, my assessment and the very tone of my presentation today were bound to differ profoundly from the opinions expressed on this occasion in years not long past, when it was vital to call attention to the economic and other perils inherent in the inflation that has gripped Italy for a decade and a half.

These repeated warnings were always based on painstaking analysis of the phenomenon to identify its causes, both immediate and more remote, exogenous and structural. Hence we did not have to confine ourselves to diagnosing the ailment but were also able to prescribe remedies and outline adjustments in economic policy.

Our analysis gave us faith in Italy's ability to climb back up what many had considered an impossibly slippery slope and a conviction that the central bank's task was not merely to regulate the economic cycle but to tackle the root causes of inflation and by its example encourage others to do likewise. This faith and conviction sustained us in our day-to-day policy-making. Though well aware of the limited effectiveness of the Bank's actions when it was acting virtually alone, as was not infrequently the case, we never wavered in our pursuit of the restoration of stability, which we regarded as the key to balanced economic growth.

However, if anyone thinks that today's assessment of events betrays complacency about the present state of affairs, he is quite mistaken. Our unflagging commitment to research, whose fruits are reflected in the body of the Report and which have shaped these concluding remarks, enables and indeed obliges us, even as we record the progress made, to point out that the recovery is still incomplete, that longstanding problems have yet to be resolved and that fresh problems lie ahead.

We have sought to dispel the widely held opinion that disinflation and the revitalization of a large part of the economy are no more than the fortuitous product of external events by demonstrating that these accomplishments are due primarily to domestic policy measures and the response of market forces. At the same time, however, we have emphasized that Italy, of all the industrial economies, remains the most vulnerable to instability and that it has only limited scope for countermeasures.

One false step could put us back into the plight from which we have extricated ourselves. In a world economy that offers scant stimulus to growth and in which free trade itself is threatened, even a momentary lapse in the discipline dictated by our close interdependence with the rest of the world, a surrender to the illusion that we could evade the unresolved problems of our economy, would be enough to rekindle inflation, which has been damped down but not stamped out, tighten the external constraint, which has been relaxed but not eliminated, and shake confidence, which has been restored but not yet consolidated.

If we are to avert these dangers, we must all raise our sights to the more noble aspirations of society, and not allow ourselves to be lured into the shortsighted pursuit of self-interest.

We are within reach of a society that can provide employment for the younger generation, tackle the problems of the South with fresh resolve, make the choices necessary to accommodate the increasingly widespread desire for new lifestyles, be a full and respected member of the international community, and temper the risks of economic activity through monetary stability, collective solidarity and clear rules. Our achievements must spur us on to further effort.

The corrective action that the private sector expects of the public sphere requires rigorous control of expenditure and efficiency in the provision of public services. The institutions on which our nation has relied for the past two decades in pursuing the goals of social solidarity proper to an advanced society that is sensitive to economic inequalities have revealed built-in flaws that make their operation incompatible with the fundamental equilibria of the economy. Their elimination will require reform of the institutions themselves. Though difficult, such an undertaking is essential if we are to give social policy solid foundations and a guarantee of longevity and not jeopardize cylical and growth policies.

The newly-found vigour of the corporate sector should be harnessed to expand the productive base; the future pattern of earnings growth and industrial relations should be directed to the same end. In a free economy, in which it is government's responsibility to correct the shortcomings of the market, even very high profit levels are socially acceptable if at the same time enterprises demonstrate their ability to promote non-inflationary growth of the economy, create employment and develop products that reflect a changing society's values for the quality of life.

The Bank of Italy will continue to work for the realization of this design, contributing technical competence, impartiality and devotion to the public welfare. That is the spirit that infuses the Report which I submit to this meeting. The monetary and financial problems facing us are intertwined with the other fundamental problems of our economy. It is our duty to point out the need for complementary lines of action to resolve them and to take all necessary measures within our own sphere.

STATISTICAL APPENDIX

LIST OF TABLES

SOURCES AND

(seasonally

	QUARTERLY NATIONAL ACCOUNTS								
	SOURCES								TOTAL
	Agriculture forestry and fisheries (1)	Industry (1)	Market services (1)	Imputed output of bank services (−)	Non-market services (1)	Other indirect taxes	GDP	Imports of goods and services	
	(billions of lire at 1980 prices)								
1980	22,305	152,506	166,494	16,607	45,730	20,004	*390,432*	93,561	*483,993*
1981	22,433	151,605	170,112	16,208	46,726	20,204	*394,872*	90,020	*484,892*
1982	21,842	148,670	173,745	16,072	47,519	20,123	*395,827*	89,401	*485,228*
1983	23,663	146,445	175,581	16,267	48,155	20,143	*397,720*	87,981	*485,701*
1984	22,803	150,996	184,501	16,460	49,136	20,767	*411,743*	97,920	*509,663*
1985	22,884	152,959	193,547	17,484	49,844	21,314	*423,064*	103,125	*526,189*
1986	23,265	157,149	199,730	18,252	50,853	21,937	*434,682*	108,342	*543,024*
1980 - I	5,518	38,474	41,816	4,137	11,295	5,015	*97,982*	23,381	*121,364*
II	5,587	38,398	41,665	4,169	11,398	5,017	*97,896*	22,398	*120,294*
III	5,560	37,642	41,363	4,170	11,484	4,966	*96,844*	24,327	*121,171*
IV	5,640	37,991	41,650	4,131	11,552	5,007	*97,709*	23,455	*121,164*
1981 - I	5,610	37,912	41,696	4,101	11,600	5,012	*97,792*	22,029	*119,758*
II	5,597	38,233	42,447	4,058	11,656	5,068	*98,944*	22,801	*121,745*
III	5,659	37,687	42,768	4,049	11,709	5,054	*98,828*	22,347	*121,176*
IV	5,567	37,772	43,201	4,001	11,761	5,070	*99,370*	22,842	*122,213*
1982 - I	5,560	37,703	43,973	4,015	11,815	5,104	*100,140*	23,466	*123,606*
II	5,424	37,505	43,717	4,016	11,862	5,058	*99,550*	22,906	*122,456*
III	5,342	36,807	42,980	4,026	11,903	4,976	*97,982*	22,039	*120,021*
IV	5,516	36,656	43,076	4,015	11,939	4,984	*98,156*	20,990	*119,146*
1983 - I	5,858	36,630	43,048	4,018	11,967	4,996	*98,481*	21,572	*120,053*
II	5,805	36,488	43,518	4,019	12,007	5,002	*98,801*	21,739	*120,540*
III	6,041	36,497	44,224	4,094	12,059	5,054	*99,781*	22,463	*122,244*
IV	5,959	36,829	44,790	4,136	12,122	5,091	*100,656*	22,207	*122,863*
1984 - I	5,647	37,462	45,496	4,133	12,198	5,137	*101,808*	23,583	*125,391*
II	5,855	37,502	45,704	4,146	12,263	5,166	*102,344*	24,033	*126,377*
III	5,700	38,305	46,400	4,063	12,316	5,231	*103,889*	24,653	*128,543*
IV	5,601	37,727	46,900	4,118	12,359	5,233	*103,701*	25,650	*129,352*
1985 - I	5,502	37,955	47,704	4,209	12,384	5,267	*104,603*	25,401	*130,005*
II	5,695	38,332	48,232	4,309	12,426	5,322	*105,699*	25,522	*131,221*
III	5,846	38,237	48,507	4,462	12,482	5,335	*105,945*	25,479	*131,424*
IV	5,841	38,435	49,105	4,503	12,552	5,389	*106,817*	26,723	*133,540*
1986 - I	5,526	38,405	49,209	4,561	12,630	5,384	*106,593*	27,181	*133,774*
II	5,937	39,556	50,178	4,538	12,698	5,513	*109,343*	26,572	*135,916*
III	5,954	39,413	50,348	4,595	12,747	5,522	*109,388*	28,228	*137,616*
IV	5,848	39,776	49,995	4,558	12,779	5,518	*109,358*	26,361	*135,719*

Sources: Istat (new national accounts series).
(1) Value added at market prices.

USES OF INCOME

adjusted data)

USES						HOUSEHOLDS' DOMESTIC CONSUMPTION					
						BY TYPE OF GOOD				BY TYPE OF CONSUMPTION	
Buildings and public works	Machinery, equipment and vehicles	Households' consumption	Collective consumption	Change in stocks	Exports of goods and services	Consumer	Semi-durable	Durable	Services	Food	Non-food
						(billions of lire at 1980 prices)					
49,915	44,865	244,126	58,055	9,694	77,338	95,330	49,369	27,073	72,354	67,615	176,511
49,195	43,406	247,788	59,600	1,787	83,116	96,311	49,231	27,938	74,308	67,882	179,906
45,942	41,343	250,402	61,319	4,021	82,201	97,972	47,594	28,086	76,750	68,943	181,459
46,318	39,609	251,328	63,029	1,328	84,089	99,717	46,669	27,226	77,716	69,910	181,418
46,585	43,124	256,859	64,308	8,307	90,480	101,114	47,624	28,155	79,966	70,648	186,211
46,355	46,312	263,753	66,564	9,107	94,098	102,849	48,355	29,706	82,843	71,035	192,718
46,049	47,747	272,194	68,534	11,503	96,997	105,276	49,636	31,455	85,827	71,634	200,560
12,597	11,111	60,709	14,275	2,231	20,440	23,604	12,456	6,674	17,959	16,779	43,914
12,489	11,171	60,942	14,457	1,976	19,260	23,749	12,407	6,720	18,050	16,871	44,055
12,438	11,238	61,242	14,587	3,001	18,664	23,932	12,343	6,824	18,153	16,956	44,296
12,391	11,345	61,233	14,736	2,486	18,974	24,045	12,163	6,855	18,192	17,009	44,246
12,431	11,208	61,521	14,812	337	19,449	24,039	12,228	6,897	18,385	17,001	44,548
12,438	11,025	61,842	14,871	831	20,739	24,029	12,344	6,966	18,503	16,966	44,876
12,413	10,637	62,058	14,894	–306	21,479	24,058	12,370	6,971	18,662	16,935	45,126
11,912	10,537	62,367	15,023	925	21,449	24,185	12,289	7,104	18,758	16,980	45,356
11,487	10,662	62,496	15,147	2,151	21,662	24,329	12,136	7,138	18,892	17,113	45,382
11,344	10,488	62,588	15,383	1,476	21,178	24,486	11,910	7,054	19,132	17,239	45,344
11,582	10,140	62,731	15,348	483	19,736	24,591	11,798	7,023	19,322	17,318	45,415
11,529	10,052	62,588	15,441	–89	19,625	24,566	11,750	6,871	19,404	17,273	45,318
11,604	9,879	62,489	15,553	591	19,937	24,684	11,774	6,770	19,283	17,351	45,160
11,572	9,891	62,561	15,769	35	20,711	24,853	11,628	6,709	19,385	17,445	45,130
11,590	9,783	62,835	15,796	623	21,619	25,029	11,577	6,786	19,422	17,520	45,294
11,552	10,056	63,442	15,912	79	21,823	25,151	11,690	6,961	19,626	17,594	45,834
11,591	10,430	64,023	15,843	1,534	21,969	25,248	11,804	7,016	19,903	17,655	46,316
11,617	10,741	64,225	16,015	1,773	22,007	25,247	12,004	6,997	19,981	17,628	46,601
11,739	10,895	64,136	16,124	2,504	23,144	25,241	11,917	7,017	19,989	17,651	46,513
11,637	11,058	64,474	16,326	2,496	23,360	25,378	11,900	7,125	20,093	17,714	46,782
11,589	11,540	64,887	16,490	2,089	23,410	25,512	11,870	7,236	20,297	17,715	47,200
11,667	11,582	65,766	16,565	2,595	23,046	25,631	12,076	7,444	20,620	17,739	48,032
11,507	11,592	66,351	16,694	1,810	23,470	25,783	12,144	7,508	20,907	17,783	48,559
11,592	11,599	66,749	16,815	2,613	24,173	25,923	12,265	7,518	21,019	17,798	48,927
11,466	11,713	67,333	16,937	2,383	23,942	26,065	12,400	7,693	21,177	17,823	49,512
11,540	12,044	67,838	17,051	2,442	25,000	26,233	12,446	7,856	21,322	17,859	49,998
11,595	12,000	68,416	17,146	3,593	24,865	26,422	12,444	7,962	21,597	17,942	50,483
11,448	11,990	68,607	17,399	3,085	23,190	26,556	12,346	7,944	21,731	18,010	50,567

Table a 2

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

Sector	1980	1981	1982	1983	1984	1985	1986
			Labour costs by unit of output *(Current lire per thousand lire of value added at 1980 prices)*				
Market goods and services	*682.8*	*814.3*	*954.9*	*1,110.1*	*1,198.5*	*1,302.3*	*1,368.0*
Agriculture, forestry and fisheries	**927.3**	**1,033.5**	**1,142.6**	**1,325.5**	**1,461.4**	**1,588.4**	**1,648.0**
Industry	**613.4**	**735.7**	**862.8**	**981.9**	**1,038.0**	**1,128.6**	**1,177.8**
Excluding construction	607.5	713.2	830.6	951.0	1,003.7	1,092.3	1,134.9
Energy products	244.5	311.5	365.7	449.5	503.7	550.5	590.6
Manufactures	655.4	765.4	890.5	1,012.7	1,062.5	1,156.1	1,198.6
Construction	617.6	815.4	981.3	1,074.6	1,145.5	1,240.6	1,317.8
Services	**673.4**	**805.5**	**957.0**	**1,131.5**	**1,229.7**	**1,336.8**	**1,411.0**
Distributive trades, lodging & catering	550.1	678.3	818.9	951.9	1,056.2	1,167.4	1,227.8
Transport & communications	975.8	1,167.1	1,408.3	1,597.0	1,700.6	1,832.0	1,914.6
Finance and insurance	577.5	635.7	718.0	933.5	1,009.1	1,051.5	1,063.0
Miscellaneous services	539.9	663.0	784.7	926.2	1,047.8	1,173.1	1,283.1
Non-market services	**980.3**	**1,257.3**	**1,444.1**	**1,664.5**	**1,853.5**	**2,031.5**	**2,183.0**
General government	983.0	1,268.3	1,452.9	1,678.4	1,874.3	2,040.8	2,207.8
TOTAL	**722.0**	**876.8**	**1,024.0**	**1,188.4**	**1,288.8**	**1,399.3**	**1,477.0**
			Value added at market prices per worker *(thousands of lire at 1980 prices)*				
Market goods and services	*17,352.0*	*17,562.9*	*17,482.8*	*17,498.2*	*18,080.1*	*18,412.5*	*18,812.3*
Agriculture, forestry and fisheries	**7,450.6**	**7,884.8**	**8,140.0**	**8,611.3**	**8,516.8**	**8,818.8**	**9,050.1**
Industry	**19,261.6**	**19,603.9**	**19,606.2**	**19,955.4**	**21,432.8**	**21,981.6**	**22,722.9**
Excluding construction	20,235.1	20,899.1	21,096.1	21,557.6	23,287.3	23,870.6	24,898.3
Energy products	79,388.2	77,915.6	77,032.2	74,140.0	73,567.7	74,089.2	77,060.4
Manufactures	18,355.1	18,996.1	19,202.1	19,723.1	21,437.5	21,991.0	22,927.7
Construction	15,861.7	15,308.9	14,786.7	14,973.7	15,660.5	16,038.0	15,958.2
Services	**19,287.4**	**19,078.7**	**18,589.5**	**18,263.9**	**18,306.6**	**18,419.8**	**18,604.0**
Distributive trades, lodging & catering	17,477.8	17,274.2	16,797.8	16,359.4	16,683.3	16,919.4	17,214.7
Transport & communications	15,825.5	15,671.6	15,630.4	15,254.7	15,371.7	15,806.6	16,133.3
Finance and insurance	54,638.5	53,008.9	51,279.6	50,147.1	49,705.3	51,779.4	53,901.8
Miscellaneous services	19,007.1	19,031.7	18,499.7	18,639.3	18,123.5	17,587.7	17,179.1
Non-market services	**12,542.2**	**12,515.0**	**12,468.6**	**12,434.8**	**12,394.9**	**12,315.1**	**12,453.0**
General government	13,399.4	13,387.0	13,412.2	13,464.0	13,483.8	13,531.2	13,584.6
TOTAL	**16,557.2**	**16,708.3**	**16,621.4**	**16,618.2**	**17,076.9**	**17,329.3**	**17,681.0**

Source: Istat.

Table a 3

INDUSTRIAL PRODUCTION BY ECONOMIC PURPOSE

(indices, 1980= 100; seasonally adjusted)

	FINAL INVESTMENT GOODS				FINAL CONSUMER GOODS				INTERMEDIATE GOODS				MANUFAC-TURING	OVERALL INDEX
	For industry	Transport equipment	Multi-sector	Total	Durable	Semi-durable	Non-durable	Total	For industry	For consumer goods	Mixed purpose	Total		
1977	94.2	77.7	60.2	79.3	88.4	90.7	79.9	85.0	86.8	91.2	92.7	91.6	86.5	*87.2*
1978	90.6	78.4	72.6	82.1	88.6	82.0	87.3	86.3	85.6	93.8	94.4	93.1	87.9	*88.8*
1979	89.1	82.4	88.6	87.7	94.0	94.9	94.3	94.4	91.6	100.4	97.8	97.6	94.1	*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	*100.0*
1981	101.2	114.5	100.8	103.4	90.7	99.9	102.3	97.4	98.8	100.4	95.8	97.4	98.4	*98.4*
1982	88.3	112.7	105.2	95.8	88.8	101.1	103.9	97.6	91.0	99.4	91.9	93.7	95.1	*95.4*
1983	79.5	121.0	110.3	92.6	85.3	92.0	104.7	94.2	86.6	96.0	89.8	90.9	92.0	*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	95.3	*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	96.3	*96.5*
1986	82.5	131.0	145.5	103.1	93.7	94.3	113.7	101.1	86.5	103.9	95.6	96.5	98.8	*99.2*
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	102.9	*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	103.0	*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	95.6	*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	98.5	*98.7*
1981 - I	102.3	111.2	104.9	104.4	92.1	96.3	99.4	95.9	99.7	98.2	98.0	98.3	98.6	*98.5*
II	106.7	116.0	100.8	107.2	92.6	100.1	102.2	98.1	101.5	101.6	96.6	98.5	100.1	*99.9*
III	99.8	115.9	100.7	102.8	89.4	101.7	102.7	97.6	98.0	100.1	94.4	96.4	97.8	*97.9*
IV	95.8	114.9	96.7	99.3	88.6	101.4	105.0	98.1	96.0	101.7	94.3	96.4	97.3	*97.5*
1982 - I	96.0	114.2	104.3	100.8	89.8	103.6	103.6	98.6	97.1	102.4	95.6	97.6	98.3	*98.5*
II	90.8	111.5	104.9	97.2	89.1	101.5	102.0	97.2	92.7	97.6	93.1	94.2	95.4	*95.7*
III	85.7	112.3	108.1	94.7	88.1	100.5	104.1	97.3	88.0	101.5	91.1	93.3	94.6	*94.9*
IV	80.7	112.8	103.4	90.6	88.1	98.7	105.9	97.5	86.4	96.2	87.9	89.8	92.2	*92.5*
1983 - I	81.2	113.5	104.8	91.3	86.2	96.7	104.7	95.8	86.2	95.0	87.4	89.2	91.4	*91.8*
II	77.4	118.7	108.5	90.6	83.3	91.1	105.0	93.3	85.9	93.5	88.4	89.4	90.5	*90.9*
III	80.0	122.7	113.2	93.8	85.6	91.9	102.9	93.6	86.2	95.7	90.7	91.3	92.2	*92.5*
IV	79.4	129.1	114.7	94.8	86.2	88.4	106.4	94.1	88.0	99.9	92.7	93.8	93.8	*94.1*
1984 - I	77.7	121.8	112.0	92.0	86.2	88.2	102.8	92.8	87.5	99.9	92.8	93.9	92.7	*93.2*
II	77.3	114.9	118.6	91.8	88.2	95.4	106.1	96.6	86.4	102.5	94.6	95.5	95.0	*95.2*
III	78.6	123.6	132.8	96.9	90.3	95.5	108.2	98.2	88.9	104.0	95.1	96.5	97.1	*97.1*
IV	77.2	117.3	142.7	96.8	87.3	98.8	107.0	97.6	87.7	103.9	92.8	94.9	96.3	*96.1*
1985 - I	77.6	118.1	148.6	98.3	89.2	92.3	107.1	96.5	84.4	103.0	94.0	94.9	95.7	*96.0*
II	80.1	117.5	145.3	99.2	88.8	91.7	112.0	98.0	87.6	104.6	93.6	95.5	96.9	*97.0*
III	81.6	114.7	140.9	98.8	86.9	92.7	112.3	97.7	86.4	103.9	92.6	94.6	96.2	*96.4*
IV	82.0	121.6	142.1	100.5	87.9	92.2	112.0	97.8	85.6	102.7	93.4	94.6	96.5	*96.7*
1986 - I	83.1	126.9	139.7	101.6	91.3	96.9	113.1	100.7	85.9	106.1	94.6	96.3	98.8	*98.7*
II	83.9	131.7	146.9	104.4	92.8	93.6	112.8	100.2	86.0	103.7	96.1	96.6	98.8	*99.1*
III	81.1	128.3	144.6	101.6	92.0	93.0	113.2	99.2	86.2	102.2	95.5	95.9	97.6	*98.2*
IV	81.9	137.3	150.7	104.8	98.7	93.8	115.6	103.4	87.9	103.7	96.4	97.1	100.1	*100.5*

Source: Based on Istat data.

Table a 4

WHOLESALE PRICES BY ECONOMIC PURPOSE *(1)*

(indices, 1980 = 100)

	Overall index	Final consumer goods				Final capital goods	Raw materials and intermediate goods		
		Food	Other non-durable goods	Durable goods	Total		Energy (2)	Non-energy (2)	Total
1977	66.6	72.8	65.5	68.1	69.3	68.0	51.6	66.4	64.0
1978	72.2	81.6	71.2	74.2	76.5	75.2	51.9	71.1	68.2
1979	83.3	89.9	80.2	84.6	85.4	84.5	63.6	84.7	81.4
1981	116.6	114.6	116.7	112.8	114.9	119.4	139.9	113.4	117.5
1982	132.8	133.4	134.6	125.0	131.9	137.1	161.9	127.3	132.6
1983	145.7	147.4	153.3	136.4	146.8	155.0	176.9	137.0	143.2
1984	160.8	161.4	170.4	147.7	161.2	170.2	200.0	151.3	158.8
1985	172.6	173.4	188.2	158.2	174.6	183.5	216.2	160.5	169.1
1986	171.1	178.4	192.6	165.3	179.9	194.0	146.1	162.5	159.9
1980 - I	95.4	96.8	94.9	94.9	95.7	93.9	89.0	96.6	95.5
II	98.8	98.4	98.2	98.6	98.3	98.5	98.4	99.3	99.2
III	101.0	100.7	100.6	101.5	100.8	102.3	102.8	100.6	100.9
IV	104.8	104.1	106.3	105.0	105.3	105.3	109.9	103.3	104.4
1981 - I	109.2	107.2	110.6	107.8	108.4	111.4	123.7	106.9	109.4
II	114.8	113.1	113.9	110.3	113.1	117.6	138.6	111.5	115.8
III	118.8	115.6	117.7	113.7	116.0	122.5	147.9	115.4	120.5
IV	123.6	122.5	124.5	116.1	122.0	126.1	149.5	119.8	124.3
1982 - I	127.6	127.6	127.2	120.4	125.8	130.9	150.7	124.3	128.4
II	130.2	130.4	129.3	124.1	128.7	135.6	153.8	126.1	130.4
III	134.4	135.3	137.0	126.1	133.8	138.6	166.0	128.2	134.0
IV	138.9	140.3	144.9	129.4	139.3	143.3	177.1	130.6	137.7
1983 - I	141.1	142.8	148.9	132.4	142.4	148.6	173.3	132.5	138.8
II	143.4	144.5	152.0	135.2	144.7	153.3	171.7	134.9	140.5
III	146.7	148.8	153.9	137.3	147.8	156.8	177.8	137.9	144.0
IV	151.6	153.7	158.4	140.6	152.3	161.2	184.8	142.8	149.3
1984 - I	156.4	157.3	166.3	143.6	157.0	166.0	192.2	147.3	154.2
II	159.9	161.3	168.8	146.9	160.4	169.2	195.1	151.0	157.8
III	161.9	162.5	170.9	148.9	162.1	171.2	200.8	152.6	160.0
IV	165.0	164.4	175.6	151.4	165.0	174.5	211.9	154.4	163.2
1985 - I	169.5	168.3	182.3	155.1	169.7	179.5	222.6	157.5	167.5
II	173.2	174.2	188.2	157.9	174.9	182.8	222.0	160.6	170.1
III	173.1	174.1	189.7	158.8	175.6	184.7	210.9	161.5	169.1
IV	174.7	176.9	192.5	160.8	178.2	187.1	209.2	162.5	169.7
1986 - I	173.8	178.8	191.1	163.0	179.1	191.7	181.8	163.5	166.3
II	170.7	178.3	191.1	164.8	179.3	193.4	144.9	162.6	159.8
III	169.3	177.7	191.8	166.0	179.5	194.9	127.6	161.9	156.6
IV	170.5	178.6	196.4	167.2	181.6	196.2	130.3	161.9	157.0
1987 - I	173.1	179.8	198.9	170.3	183.7	201.6	142.0	162.8	159.6

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 5

CONSUMER PRICES (1)

(indices, 1985 = 100)

	POPULATION AS A WHOLE												WORKER AND EMPLOYEE HOUSEHOLDS					
	Overall index	Goods			Services	Other than food & services							Overall index	Categories of expenditure				
		food	non-food	total		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		food	clothing	elec-tricity & other fuels	housing	miscel-laneous expen-diture
1977	33.7	37.5	32.9	35.2	30.3	33.3	26.1	36.2	32.0	33.6	35.7	28.4	33.3	37.5	34.2	22.6	29.5	31.3
1978	37.8	42.4	36.6	39.5	33.9	38.2	28.4	39.9	36.3	36.5	39.2	32.4	37.4	42.5	39.2	25.0	31.9	35.0
1979	43.4	48.0	42.1	45.0	39.6	43.5	35.0	45.0	40.9	42.1	44.4	38.3	43.3	48.3	44.7	29.9	40.1	40.8
1980	52.5	55.5	53.9	54.6	47.8	52.5	46.9	54.3	49.4	52.4	52.7	49.8	52.4	55.4	53.4	45.3	47.7	51.3
1981	61.9	64.5	63.1	63.8	57.6	61.5	56.4	64.3	60.6	61.8	61.0	59.6	62.2	64.4	62.5	57.3	55.5	61.8
1982	72.1	75.1	73.1	74.0	67.7	71.4	67.1	74.2	70.4	72.1	69.6	69.9	72.4	74.7	72.4	69.8	64.7	71.9
1983	82.7	84.3	83.4	83.8	80.0	81.1	79.8	83.8	78.6	84.4	81.8	81.5	83.3	84.4	82.2	82.5	77.2	83.4
1984	91.6	92.0	92.1	92.1	90.6	90.3	93.2	91.8	87.6	93.4	91.0	90.6	92.1	92.1	91.1	91.7	95.0	91.9
1986	105.9	105.5	103.7	104.5	108.9	108.3	100.6	106.4	104.6	104.3	109.0	108.3	106.1	105.3	108.4	94.0	108.5	107.2
1980 - I	48.6	51.9	49.6	50.7	43.7	48.9	43.4	50.3	43.4	49.3	47.4	46.0	49.1	52.1	49.7	41.1	45.5	47.7
II	50.5	53.5	51.7	52.6	45.7	51.3	45.1	53.1	45.8	51.3	49.5	47.6	50.9	53.4	52.3	42.8	46.9	49.8
III	52.6	55.3	54.4	54.9	47.6	52.7	48.1	55.0	48.7	53.4	51.2	50.1	53.0	55.3	53.5	48.1	47.7	52.0
IV	55.4	57.8	57.2	57.5	50.7	56.5	50.3	57.8	53.9	54.8	54.7	52.9	55.8	57.9	57.5	48.9	50.9	55.0
1981 - I	58.3	60.6	59.7	60.1	54.3	58.1	52.5	60.6	57.7	58.5	58.5	56.0	58.7	60.6	59.3	51.7	53.3	58.5
II	60.9	63.5	62.2	62.8	56.6	60.5	55.2	63.5	59.8	60.6	59.8	58.9	61.2	63.4	61.5	56.0	54.3	60.9
III	62.7	65.6	63.8	64.6	58.4	61.6	57.7	65.2	61.3	62.5	61.4	60.5	63.0	65.3	62.5	59.6	55.6	62.7
IV	65.6	68.5	66.8	67.6	61.1	65.8	60.1	67.8	63.8	65.3	64.2	63.1	66.0	68.3	66.9	61.9	58.9	65.3
1982 - I	68.3	71.2	69.1	70.1	64.1	67.7	62.9	70.4	67.1	67.5	66.8	66.3	68.5	70.8	68.7	64.3	61.5	68.0
II	70.3	73.0	71.1	72.0	66.5	70.2	64.6	73.1	69.8	69.1	68.4	68.8	70.6	72.5	71.2	66.0	63.5	70.3
III	73.2	76.7	74.1	75.3	68.5	71.4	67.9	75.0	71.5	73.9	70.4	70.8	73.6	76.3	72.5	71.4	64.7	73.0
IV	76.5	79.4	78.0	78.7	71.6	76.2	73.2	78.2	73.1	77.7	72.8	73.8	77.0	79.2	77.3	77.2	69.3	76.3
1983 - I	79.3	81.3	80.3	80.8	75.9	77.8	75.9	80.8	75.0	80.2	78.4	78.1	79.8	81.2	78.9	79.6	72.0	79.8
II	81.6	83.2	82.4	82.8	78.8	80.0	77.1	83.0	78.8	83.7	81.1	80.4	82.1	83.2	81.3	80.5	73.6	82.7
III	83.5	85.3	84.0	84.6	80.8	81.1	79.1	84.6	79.8	85.5	82.8	82.7	84.1	85.5	82.3	83.3	75.0	84.5
IV	86.3	87.5	86.8	87.1	84.5	85.4	86.9	86.9	80.9	88.0	85.1	84.8	87.0	87.8	86.3	86.7	88.3	86.6
1984 - I	88.9	89.6	89.6	89.6	87.2	87.1	91.4	89.1	82.3	91.0	87.9	87.6	89.5	89.7	88.0	90.8	92.9	89.2
II	90.9	91.6	91.3	91.5	89.5	89.1	92.9	90.9	86.5	92.3	90.3	89.7	91.4	91.7	90.2	91.2	94.7	91.1
III	92.2	92.6	92.3	92.5	91.6	90.2	93.3	92.3	89.5	94.3	91.8	91.4	92.6	92.7	91.1	91.0	95.6	92.7
IV	94.4	94.2	95.0	94.6	94.0	94.7	95.1	94.8	91.9	96.0	94.0	93.8	94.7	94.4	95.2	93.8	96.6	94.8
1985 - I	97.1	96.9	97.2	97.0	97.4	96.5	98.1	97.2	97.6	97.8	97.4	96.8	97.2	97.0	96.8	99.1	97.5	97.3
II	99.4	99.5	99.6	99.5	99.3	99.1	100.0	99.4	99.7	99.8	99.1	99.3	99.4	99.4	99.1	101.5	98.7	99.4
III	100.6	100.8	100.5	100.6	100.6	100.2	99.5	100.7	100.8	100.5	100.6	101.1	100.5	100.8	100.1	98.9	99.5	100.7
IV	102.8	102.9	102.8	102.8	102.8	104.2	102.4	102.7	102.0	101.9	102.9	102.9	102.8	102.8	104.0	100.6	104.2	102.5
1986 - I	104.4	104.4	103.0	103.6	106.3	105.4	102.0	104.3	102.8	103.3	107.4	105.6	104.6	104.1	105.5	98.5	105.8	105.2
II	105.5	105.2	103.3	104.1	108.5	107.5	101.0	106.0	104.5	104.1	108.2	107.7	105.8	104.9	107.5	95.3	107.5	106.8
III	106.1	105.8	103.6	104.5	109.5	108.5	99.3	106.9	105.1	104.7	109.5	109.0	106.4	105.5	108.5	92.0	108.3	107.8
IV	107.4	106.8	104.8	105.7	111.2	111.7	100.1	108.4	105.8	105.3	110.7	110.8	107.7	106.5	111.9	90.4	112.3	108.8
1987 - I													109.1	108.1	113.2	91.8	113.7	110.2

Source: Istat.

(1) The pre-1986-I figures were obtained by dividing the figures of the 1980-based index by the conversion factor linking the 1980 and 1985-based series with reference to the 1985 average.

BALANCE OF PAYMENT

	CURRENT ACCOUNT							CAPITAL MOVEMENTS	ERRORS & OMISSIONS (3)	OVERALL BALANCE
	Goods (2)	Freight	Foreign travel	Emigrants' remittances	Income from capital	Other services	Total			
Rece										
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 (7) .	138,470	4,548	15,953	4,048	8,695	20,017	*191,731*	41,777	–	–
1986 (7) .	134,371	4,116	14,691	3,946	7,031	19,140	*183,295*	56,937	–	–
Pay										
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	–	1,634	–	5,040	8,361	*98,805*	6,318	216	–
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	112,791	–	2,767	–	12,140	14,028	*141,726*	15,218	85	–
1984	138,760	–	3,686	–	15,222	17,024	*174,692*	25,004	–	–
1985 (7) .	157,155	–	3,591	–	17,191	21,555	*199,492*	37,055	5,313	–
1986 (7) .	139,087	–	4,112	–	15,497	23,934	*182,630*	58,973	1,594	–
Bal										
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	5,398	2,211	–973	–777	*–10,146*	4,104	–216	*–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	–9,177	2,975	10,954	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	–18,685	4,548	12,362	4,048	–8,496	–1,538	*–7,761*	4,722	–5,313	*–8,352*
1986	–4,716	4,116	10,579	3,946	–8,466	–4,794	*665*	–2,036	–1,594	*–2,965*

(1) Rounding may cause discrepancies in totals. – (2) Imports cif, exports fob. – (3) As of 1985 unclassifiable capital movements and items in transit are included under the
sign indicates an increase in assets or a decrease in liabilities. – (6) Including the revaluation of ECUs issued against gold. – (7) New series for the item "Foreign travel".

Table a 6

ON A SETTLEMENTS BASIS *(1)*

of lire)

CHANGES IN BANKS' NET EXTERNAL POSITION (4) (5)	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 (6)	Total	
ipts										
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*	957
–	2,357	7,258	6,019	468	133	–	428	–	*16,663*	–
5,006	4,327	2,197	–	–	232	81	188	–	*7,025*	–
ments										
–	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*	–
–	–	6,209	6	252	436	93	294	1,890	*9,180*	–
4,818	–	–	–	–	–	58	–	2,946	*3,004*	489
–	–	–	3,018	206	–	–	–	5,409	*8,633*	433
ance										
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	–6,209	–6	–252	–436	–93	–294	–1,890	*–7,668*	957
–4,818	2,357	7,258	6,019	468	133	–58	428	–2,946	*13,659*	–489
5,006	4,327	2,197	–3,018	–206	232	81	188	–5,409	*–1,608*	–433

heading "Errors and omissions". – (4) The 1984 figures have been adjusted for the arrangements regarding the foreign assets of Banco Ambrosiano in liquidation. – (5) A minus

MAIN ITEMS OF THE BALANCE OF

(billions

	CURRENT ACCOUNT									
	GOODS (FOB) (2)						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)
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	80,464		65,971		−14,493		5,975		*−8,518*	
1981	99,945		86,687		−13,258		2,982		*−10,276*	
1982	110,292		98,332		−11,960		3,578		*−8,382*	
1983	113,162		109,450		−3,712		6,120		*2,408*	
1984	139,885		129,630		−10,255		6,103		*−4,152*	
1985	156,446		144,516		−11,930		5,058		*−6,872*	
1986	137,869		143,719		5,850		227		6,077	
1982 - I	28,239	27,151	23,729	23,663	−4,510	−3,488	−746	601	*−5,256*	−2,887
II	27,502	27,078	25,292	24,548	−2,210	−2,530	1,308	892	*−902*	−1,638
III	25,422	27,818	22,929	24,245	−2,493	−3,573	2,628	1,230	*135*	−2,343
IV	29,129	28,245	26,382	25,876	−2,747	−2,369	388	855	*−2,359*	−1,514
1983 - I	27,832	26,755	25,401	25,343	−2,431	−1,412	−276	1,395	*−2,707*	−17
II	27,996	27,546	27,095	26,266	−901	−1,280	2,335	1,886	*1,434*	606
III	26,072	28,554	26,397	27,903	325	−651	2,934	1,238	*3,259*	587
IV	31,262	30,307	30,557	29,938	−705	−369	1,127	1,601	*422*	1,232
1984 - I	33,924	32,589	32,938	32,911	−986	322	−692	905	*−1,678*	1,227
II	35,048	34,428	32,834	31,769	−2,214	−2,659	2,033	1,491	*−181*	−1,168
III	32,785	35,939	31,136	32,908	−1,649	−3,031	3,382	1,667	*1,733*	−1,364
IV	38,128	36,929	32,722	32,042	−5,406	−4,887	1,380	2,040	*−4,026*	−2,847
1985 - I	40,243	38,679	34,777	34,722	−5,466	−3,957	278	2,289	*−5,188*	−1,668
II	40,207	39,461	37,485	36,329	−2,722	−3,132	1,814	1,298	*−908*	−1,834
III	35,988	39,506	34,616	36,489	−1,372	−3,017	1,826	−351	*454*	−3,368
IV	40,008	38,800	37,638	36,976	−2,370	−1,824	1,140	*1,822*	−1,230	−2
1986 - I	38,508	37,090	35,143	35,048	−3,365	−2,042	−1,960	−123	*−5,325*	−2,165
II	35,674	35,075	36,611	35,497	937	422	1,026	454	*1,963*	876
III	29,235	32,196	34,336	36,143	5,101	3,947	2,643	918	*7,744*	4,865
IV	34,452	33,508	37,629	37,031	3,177	3,523	−1,482	−1,022	*1,695*	2,501

(1) Rounding may cause discrepancies in the totals. — (2) The quarterly figures are based on foreign exchange statistics. – (3) The 1984 figures are adjusted for the

Table a 7

PAYMENTS ON A TRANSACTIONS BASIS *(1)*

of lire)

CAPITAL MOVEMENTS			ERRORS AND OMISSIONS	CHANGES IN BANKS' NET EXTERNAL POSITION (3) (4)	CHANGES IN OFFICIAL RESERVES (4)	EXCHANGE RATE ADJUSTMENTS	OVERALL BALANCE (9+13+14) = −(15+16+17)
Medium and long-term	Short-term	Total					
(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)
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*
2,807	−305	2,502	−242	7,886	−1,946	318	*−6,258*
9,491	1,734	11,225	584	1,322	−2,208	−647	*1,533*
6,999	−2,065	4,934	927	−1,505	3,921	105	*−2,521*
997	616	1,613	−228	6,792	−11,183	598	*3,793*
2,610	−2,547	63	4,146	6,654	−7,668	957	*57*
4,669	1,532	6,201	−7,681	−4,818	13,659	−489	*−8,352*
−4,178	−2,088	−6,266	−2,776	5,006	−1,608	−433	−2,965
1,732	−1,165	567	1,181	−174	3,716	−34	*−3,508*
2,449	−487	1,962	−372	409	−1,298	201	*688*
815	1,038	1,853	−199	517	−2,394	88	*1,789*
2,003	−1,451	552	317	−2,257	3,897	−150	*−1,490*
587	−169	418	162	2,231	−137	33	*−2,127*
48	894	942	479	3,681	−6,554	18	*2,855*
499	146	645	−601	−1,122	−2,603	422	*3,303*
−137	−255	−392	−268	2,002	−1,889	125	*−238*
960	262	1,222	−2,766	826	2,194	202	−3,222
−637	−1,492	−2,129	1,306	4,218	−3,189	−25	*−1,004*
1,147	−978	169	1,207	630	−4,287	548	*3,109*
1,140	−339	801	4,399	980	−2,386	232	*1,174*
2,997	169	3,166	−2,350	877	2,772	723	*−4,372*
2,003	1,012	3,015	−3,478	4,262	−2,386	−505	*−1,371*
1,676	760	2,436	−1,515	−4,138	2,906	−143	*1,375*
−2,007	−409	−2,416	−338	−5,819	10,367	−564	*−3,984*
−1,328	2,086	758	−2,129	5,190	1,697	−191	*−6,696*
2,785	−667	2,118	425	1,588	−6,144	50	*4,506*
−4,039	−1,174	−5,213	−2,066	−2,983	2,805	−287	*465*
−1,596	−2,333	−3,929	994	1,211	34	−5	*−1,240*

arrangements regarding the foreign assets of Banco Ambrosiano in liquidation. — (4) A minus sign indicates an increase in assets or a decrease in liabilities.

Table a **8**

ITALY'S REAL EFFECTIVE EXCHANGE RATES *(1)*

(indices, 1980 = 100)

	13 industrial countries	EEC	Germany	France	UK	Belgium	Netherlands	US
1977	*97.4*	*98.9*	93.6	106.2	119.7	87.8	89.7	91.0
1978	*93.1*	*94.2*	89.8	99.9	110.6	85.4	87.3	94.7
1979	*95.7*	*95.7*	92.0	99.9	106.7	90.0	93.2	99.2
1981	*98.0*	*101.4*	103.6	100.7	93.1	105.2	101.5	80.1
1982	*98.1*	*102.3*	101.4	104.3	95.2	115.5	97.5	74.3
1983	*100.6*	*106.0*	103.1	109.0	102.2	122.8	100.2	72.2
1984	*102.0*	*109.1*	106.7	110.9	104.4	128.0	105.1	67.4
1985	*100.4*	*107.1*	106.5	105.9	101.1	126.5	106.3	66.4
1986	*103.2*	*107.1*	104.3	103.8	109.5	126.1	114.8	88.6
1980 - I	*100.8*	*100.1*	97.9	101.9	106.4	98.6	98.7	102.5
II	*99.7*	*99.5*	98.8	100.2	101.3	98.8	99.7	100.2
III	*99.6*	*99.4*	100.0	98.7	98.8	100.1	99.0	101.6
IV	*99.9*	*100.9*	103.2	99.4	94.0	102.4	102.2	96.1
1981 - I	*99.0*	*101.3*	104.5	100.5	89.6	104.3	101.8	87.4
II	*97.7*	*101.2*	103.5	101.2	89.4	105.0	102.6	78.8
III	*98.3*	*102.4*	104.9	100.5	96.4	106.3	103.1	75.4
IV	*97.2*	*100.8*	101.6	100.7	97.2	105.0	98.5	78.9
1982 - I	*97.4*	*101.4*	102.3	101.6	94.6	110.5	97.9	76.7
II	*96.8*	*100.6*	100.2	101.0	94.3	114.8	97.1	75.2
III	*98.5*	*103.0*	101.1	107.2	94.0	117.2	97.2	72.7
IV	*99.8*	*104.1*	102.1	107.5	97.8	119.5	98.0	72.7
1983 - I	*101.3*	*105.9*	103.1	107.2	108.4	120.9	99.3	76.1
II	*100.4*	*105.4*	102.2	109.2	101.0	121.4	100.2	73.5
III	*100.0*	*105.9*	103.4	109.3	99.0	123.5	100.0	69.8
IV	*100.4*	*106.7*	103.8	110.2	100.3	125.5	101.5	69.4
1984 - I	*101.3*	*107.9*	104.9	111.0	102.0	127.4	103.6	69.6
II	*102.0*	*108.6*	105.9	110.7	103.7	127.8	104.6	69.9
III	*102.3*	*109.6*	107.4	111.0	104.8	128.1	105.8	66.1
IV	*102.4*	*110.3*	108.4	110.7	107.3	128.9	106.6	64.1
1985 - I	*102.9*	*111.4*	109.7	110.9	110.4	129.6	107.6	61.7
II	*101.3*	*108.5*	108.3	107.7	100.4	128.2	107.3	64.1
III	*98.4*	*104.3*	104.4	103.0	95.0	124.1	104.5	67.0
IV	*99.0*	*104.3*	103.8	101.8	98.6	124.0	105.8	73.0
1986 - I	*101.2*	*105.7*	103.9	102.2	105.8	124.9	110.8	81.0
II	*101.7*	*106.0*	103.9	103.9	102.4	124.9	114.1	85.3
III	*103.9*	*107.8*	104.3	104.7	110.6	126.9	116.8	92.4
IV	*105.9*	*109.0*	105.0	104.5	119.1	127.8	117.3	95.8

Sources: Based on Istat, OECD and IMF data.
(1) Calculated with reference to the wholesale prices of manufactures in domestic and foreign markets.

Table a 9

ITALY'S EXTERNAL POSITION

(amounts in billions of lire)

	1977	1978	1979	1980	1981	1982	1983	1984 (1)	1985 (1)	1986 (1) (2)
Non-bank assets										
Direct investments	4.1	4.8	5.9	7.0	7.4	8.1	9.8	14.2	17.7	27.6
Portfolio and other investments	3.7	5.1	5.0	5.5	4.5	4.4	3.9	4.9	7.8	14.8
Loans	2.6	3.0	3.4	4.1	4.1	4.5	4.7	5.4	7.2	9.4
Trade credits	17.9	22.4	28.6	26.8	23.3	21.2	20.7	19.1	23.0	29.0
of which: short-term	*8.7*	*12.0*	*17.0*	*16.7*	*14.8*	*13.1*	*12.5*	*11.9*	*15.6*	*19.7*
TOTAL ...	**28.3**	**35.3**	**42.9**	**43.4**	**39.3**	**38.2**	**39.1**	**43.6**	**55.7**	**80.8**
Non-bank liabilities										
Direct investments	6.9	8.0	9.1	8.9	7.7	7.4	7.3	11.6	19.0	25.7
Portfolio and other investments	2.2	2.8	4.3	6.0	5.4	4.7	4.4	3.3	6.6	10.8
Private loans	10.5	11.1	9.9	12.4	17.9	21.2	21.0	19.4	20.1	23.4
Official loans	3.6	5.5	7.7	11.2	15.3	17.9	19.5	21.2	28.4	35.8
Trade credits	8.0	10.3	12.5	12.5	13.6	11.0	11.8	11.9	14.4	16.8
of which: short-tem	*7.1*	*9.3*	*11.6*	*11.7*	*12.9*	*10.5*	*10.7*	*10.6*	*13.1*	*15.1*
TOTAL ...	**31.2**	**37.7**	**43.5**	**51.0**	**59.9**	**62.2**	**64.0**	**67.4**	**88.5**	**112.5**
Net non-bank position	**-2.9**	**-2.4**	**-0.6**	**-7.6**	**-20.6**	**-24.0**	**-24.9**	**-23.8**	**-32.8**	**-31.7**
Net position of banks	**-8.1**	**-7.1**	**-8.6**	**-15.9**	**-13.4**	**-10.6**	**-12.9**	**-15.1**	**-14.6**	**-21.9**
Net position of Banca d'Italia and UIC (3)	**2.4**	**9.3**	**17.9**	**22.4**	**19.3**	**13.7**	**19.7**	**20.7**	**15.3**	**19.4**
TOTAL NET POSITION	**-8.6**	**-0.2**	**8.7**	**-1.1**	**-14.7**	**-20.9**	**-18.1**	**-18.2**	**-32.1**	**-34.2**
(in thousands of lire)	*—7.5*	*—0.2*	*7.0*	*—1.0*	*—17.6*	*—28.6*	*—30.0*	*—35.2*	*—53.9*	*—46.2*
Net position excluding investments (4)	–7.3	0.7	11.2	1.3	–13.5	–21.3	–20.1	–22.4	–32.0	–40.1
Memorandum items:										
– official gold reserves	11.3	14.3	20.1	36.7	29.0	23.7	26.2	21.6	23.6	26.1
– lira/dollar exchange rate	872	830	804	930	1,200	1,370	1,659	1,936	1,678	1,351

(1) New series data for investments. – (2) Provisional. – (3) Assets are stated net of gold reserves but, as of 1979, inclusive of ECUs received in exchange for gold. – (4) Defined until last year as "Net financial position".

Table a 10

CONSOLIDATED ACCOUNTS OF THE PUBLIC SECTOR

(billions of lire)

	1980	1981	1982	1983	1984	1985	1986
Revenue							
Current revenue	**134,324**	**167,041**	**208,421**	**256,984**	**287,514**	**324,833**	**365,494**
Direct taxes	37,608	51,293	67,442	85,281	93,776	106,034	116,051
Indirect taxes	33,522	38,297	46,649	58,029	67,368	72,851	81,961
Social security contributions							
– actual	44,488	53,130	67,217	79,126	86,955	97,116	(1)110,984
– imputed	5,242	6,673	7,699	10,088	11,930	13,329	13,780
Income from capital	3,122	3,790	3,993	4,614	4,928	6,785	6,833
Sales of goods and services	6,017	7,994	9,866	11,807	13,908	16,249	18,265
Other	4,325	5,864	5,555	8,039	8,649	12,469	17,620
Capital account revenue	**708**	**1,189**	**1,860**	**913**	**2,516**	**2,681**	**2,656**
TOTAL REVENUE	**135,032**	**168,230**	**210,281**	**257,897**	**290,030**	**327,514**	**368,150**
Expenditure							
Current expenditure	**151,838**	**199,065**	**245,149**	**295,188**	**336,850**	**381,290**	**422,065**
Compensation of employees	49,073	65,468	76,213	88,286	99,813	110,675	(1)120,166
Intermediate consumption	17,084	21,662	26,595	31,985	37,489	44,115	48,313
Social services	54,990	73,136	88,935	109,707	121,805	139,245	153,447
Subsidies to firms	6,255	6,539	8,437	11,208	11,308	12,482	14,980
Interest payments	21,412	29,309	40,081	48,982	60,067	67,209	77,508
Other	3,024	2,951	4,888	5,020	6,368	7,564	7,651
Capital account expenditure	**17,955**	**23,829**	**29,188**	**33,390**	**37,632**	**47,671**	**46,749**
Gross investment	13,856	19,024	23,259	27,075	30,050	34,072	35,559
Investment grants	3,365	4,777	5,887	6,248	7,172	8,412	10,548
Other	734	28	42	67	410	5,187	642
TOTAL EXPENDITURE	**169,793**	**222,894**	**274,337**	**328,578**	**374,482**	**428,961**	**468,814**
Deficit on current account	**–17,514**	**–32,024**	**–36,728**	**–38,204**	**–49,336**	**–56,457**	**–56,571**
Total deficit	**–34,761**	**–54,664**	**–64,056**	**–70,681**	**–84,452**	**–101,447**	**–100,664**

Source: Based on data contained in the *Relazione generale sulla situazione economica del paese.*
(1) Includes 2.2 trillion lire of health contributions for public employees.

Table a 11

FINANCING OF THE PUBLIC SECTOR BORROWING REQUIREMENT (1)

(billions of lire)

	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986
Medium and long-term securities, excluding BI portfolio	7,925	14,178	12,175	–2,303	5,727	23,429	66,968	55,942	83,948	77,384
Treasury bills, excluding BI portfolio	15,090	9,270	9,926	26,218	28,234	29,039	10,377	14,918	–1,878	8,369
Post Office funds	3,211	4,871	6,748	2,195	2,591	3,586	4,937	6,057	9,268	11,300
Lending by credit institutions	–2,978	–140	2,558	752	988	5,193	5,699	8,711	–2,098	1,519
to: *central government bodies*	*36*	*32*	*490*	*343*	*819*	*783*	*–139*	*10*	*–89*	*–199*
social security institutions	*190*	*155*	*255*	*280*	*–1,254*	*242*	*225*	*755*	*–2,203*	*66*
local authorities (2)	*–3,224*	*–170*	*1,740*	*148*	*1,459*	*3,105*	*3,441*	*6,651*	*394*	*1.002*
autonomous govt. agencies	*73*	*–161*	*71*	*–74*	*–68*	*1,065*	*2,059*	*1,315*	*–307*	*597*
municipal enterprises	*–53*	*5*	*2*	*55*	*33*	*–1*	*113*	*–19*	*107*	*52*
Other domestic debt	137	234	160	136	79	160	208	232	72	23
Foreign debt	77	273	581	787	2,515	2,570	1,259	2,271	2.937	856
TOTAL . . .	**23,462**	**28,686**	**32,148**	**27,785**	**40,134**	**63,977**	**89,448**	**88,131**	**92,249**	**99,451**
Borrowing from BI-UIC	–4,008	5,024	343	9,930	13,692	12,589	1,259	13,726	27,479	10,980
of which: overdraft on BI account	*–420*	*1,910*	*3,476*	*8,944*	*6,186*	*6,598*	*–8,622*	*18,554*	*6,340*	*4,525*
TOTAL BORROWING REQUIREMENT	**19,454**	**33,710**	**32,491**	**37,715**	**53,826**	**76,566**	**90,707**	**101,857**	**119,728**	**110,431**
Financing of ENEL		**898**	**1,068**	**2,790**	**1,056**	**3,389**	**2,138**	**1,756**	**1,115**	**–25**
of which: bond issues		*867*	*209*	*471*	*–756*	*1,213*	*1,081*	*1,045*	*669*	*1,297*
loans from credit institutions		*–269*	*477*	*58*	*–109*	*794*	*–309*	*1,022*	*182*	*–666*
borrowing abroad		*300*	*382*	*2,261*	*1,921*	*1,382*	*1,366*	*–302*	*264*	*–656*
TOTAL BORROWING REQUIREMENT OF THE ENLARGED PUBLIC SECTOR		**34,608**	**33,559**	**40,505**	**54,882**	**79,955**	**92,845**	**103,622**	**120,843**	**110,406**

(1) Rounding may cause discrepancies in the totals. – (2) For 1986, includes the loans disbursed by the state sector to local authorities with centralized Treasury accounts and recorded by banks during the delay before the completion of the relevant procedures under the item "Tied deposits with the Treasury".

Table a 12

THE PUBLIC DEBT (1)

(face value; billions of lire and percentage composition)

	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986
					Amounts outstanding					
Medium and long-term securities, excluding BI portfolio	24,927	39,502	52,008	49,527	55,802	80,893	149,832	207,740	294,558	374,514
of which: held by banks	*18,072*	*26,663*	*34,375*	*31,435*	*32,435*	*47,907*	*81,094*	*96,285*	*127,468*	*128,806*
Treasury bills, excluding BI portfolio	24,709	33,979	43,905	70,123	98,357	127,395	137,772	152,691	150,814	159,187
of which: held by banks	*18,334*	*23,910*	*25,117*	*35,437*	*39,097*	*56,514*	*51,317*	*44,743*	*26,584*	*30,510*
Post Office funds	19,234	24,105	30,853	33,048	35,639	39,225	44,162	50,219	59,487	70,787
Lending by credit institutions	14,262	14,122	16,680	17,432	18,420	23,613	29,312	38,024	35,925	37,444
to: central government bodies	*362*	*393*	*883*	*1,226*	*2,045*	*2,828*	*2,689*	*2,699*	*2,609*	*2,411*
social security institutions	*1,778*	*1,932*	*2,188*	*2,468*	*1,213*	*1,455*	*1,680*	*2,435*	*232*	*298*
local authorities (2)	*11,135*	*10,965*	*12,705*	*12,853*	*14,312*	*17,417*	*20,857*	*27,508*	*27,902*	*28,904*
autonomous government agencies	*677*	*516*	*587*	*513*	*445*	*1,511*	*3,570*	*4,885*	*4,578*	*5,175*
municipal enterprises	*311*	*316*	*317*	*372*	*405*	*403*	*516*	*497*	*605*	*657*
Other domestic debt	1,170	1,404	1,563	1,700	1,779	1,938	2,147	2,379	2,451	2,475
Foreign debt	1,616	1,941	2,392	3,433	6,578	9,731	12,505	16,285	18,204	17,377
SUB-TOTAL . . .	**85,918**	**115,053**	**147,402**	**175,262**	**216,575**	**282,796**	**375,730**	**467,337**	**561,440**	**661,783**
Borrowing from BI-UIC	38,026	43,153	43,255	52,978	66,555	78,670	79,631	92,863	120,286	130,955
of which: medium and long-term securities	*24,882*	*30,771*	*27,759*	*28,261*	*29,647*	*28,891*	*30,393*	*36,367*	*45,083*	*52,681*
Treasury bills	*7,588*	*3,987*	*3,657*	*2,641*	*8,099*	*12,086*	*12,670*	*6,641*	*21,658*	*23,056*
overdraft on BI account	*4,796*	*6,706*	*10,182*	*19,126*	*25,312*	*31,910*	*23,288*	*41,842*	*48,182*	*52,707*
other borrowing	*760*	*1,689*	*1,657*	*2,950*	*3,497*	*5,783*	*13,280*	*8,013*	*5,363*	*2,511*
TOTAL . . .	**123,944**	**158,206**	**190,657**	**228,240**	**283,130**	**361,466**	**455,361**	**560,200**	**681,726**	**792,738**
					Percentage composition					
Medium and long-term securities, excluding BI portfolio	20.1	25.0	27.3	21.7	19.7	22.4	32.9	37.1	43.2	47.3
Treasury bills, excluding BI portfolio	20.0	21.5	23.0	30.7	34.8	35.2	30.3	27.3	22.1	20.1
Post Office funds	15.5	15.2	16.2	14.5	12.6	10.9	9.7	8.9	8.7	8.9
Lending by credit institutions	11.5	8.9	8.8	7.7	6.5	6.5	6.4	6.8	5.3	4.7
Other domestic debt	0.9	0.9	0.8	0.7	0.6	0.5	0.5	0.4	0.4	0.3
Foreign debt	1.3	1.2	1.2	1.5	2.3	2.7	2.7	2.9	2.7	2.2
Borrowing from BI-UIC	30.7	27.3	22.7	23.2	23.5	21.8	17.5	16.6	17.6	16.5

(1) Rouding may cause discrepancies in totals. – (2) For 1986, includes the loans disbursed by the state sector to local authorities with centralized Treasury accounts and recorded by banks during the delay before the completion of the relevant procedures under the item "Tied deposits with the Treasury".

Table a 13

STATE SECTOR EXPENDITURE, REVENUE AND BORROWING REQUIREMENT

(billions of lire)

	1982	1983	1984	1985	1986
EXPENDITURE					
Wages, salaries and pensions	49,662	57,295	64,863	71,736	77,605
Purchases of goods and services	10,931	13,912	16,840	19,620	21,659
Interest payments	38,914	47,105	57,579	63,558	73,647
Direct investment	8,684	11,316	12,610	11,889	13,526
Loans and shareholdings	12,872	16,059	12,692	14,824	11,058
of which: local authorities	*3,901*	*3,896*	*3,725*	*4,304*	*5,671*
financial institutions	*573*	*1,767*	*1,726*	*2,750*	*2,774*
public enterprises	*7,384*	*9,431*	*6,548*	*5,469*	*1,840*
Disbursements to: local authorities	56,850	71,396	73,902	91,082	98,830
of which: health care	*24,423*	*30,656*	*33,307*	*39,752*	*41,874*
social security institutions	23,176	27,437	29,626	36,615	38,844
enterprises	9,086	11,493	13,383	12,958	14,547
households	3,028	4,679	6,109	7,442	8,537
other	4,614	4,486	8,355	10,468	12,268
Other expenditure	7,992	9,599	11,409	10,958	11,496
TOTAL EXPENDITURE . . .	**225,809**	**274,777**	**307,368**	**351,150**	**382,017**
REVENUE					
Direct taxes					
of which: Personal income tax	37,051	46,546	51,073	61,852	66,838
Corporate income tax	3,636	5,457	8,117	9,173	12,017
Local income tax	6,253	7,635	8,027	10,555	13,717
Withholding tax on interest income	10,835	10,642	15,618	13,910	16,129
Indirect taxes					
of which: Value added tax	29,186	36,081	41,882	44,911	49,322
Business taxes (stamp duties, duties on government concessions, etc.)	6,330	7,189	8,475	9,443	9,657
Excise duty on oil products	8,244	11,585	13,014	13,653	19,165
Excise duty on other manufactures (spirits, beer, sugar, gas and electricity, methane, etc.)	1,174	1,294	1,316	1,177	1,308
Tax on tobacco consumption	3,199	3,732	4,134	4,399	5,127
Total tax revenue, net of accounting operations, discounts and bank commissions	**114,405**	**143,969**	**161,015**	**178,098**	**202,653**
Receptis from the building offences condonation	–	–	–	226	4.223
EEC levies	3,516	4,110	4,539	4,895	6,905
Sales of goods and services	8,212	9,932	11,920	14,478	15,448
Health care and other social security contributions	19,222	19,256	24,245	28,453	30,298
Other income	8,464	9,253	10,262	12,575	12,298
Total receipts, net of accounting operations, discounts and bank commissions	**153,819**	**186,520**	**211,981**	**238,725**	**271,825**
BORROWING REQUIREMENT	**71,990**	**88,257**	**95,387**	**112,425**	**110,192**

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	
1977 - Dec.	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	180,089	11,566	6,602	89,503	7,662	3,451	52,271
1984 - "	4,994	62,813	–	215,594	187,037	14,570	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	71,629	–	218,923	173,794	15,526	8,913	67,993	6,388	3,068	60,878
Apr.	3,124	71,564	–	223,684	177,183	15,768	8,882	67,819	6,365	3,055	62,313
May (9)	7,451	71,622	–	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	16,505	8,752	65,036	5,870	3,191	60,974
Aug.	2,690	73,054	–	224,591	186,333	16,693	8,686	66,493	6,445	3,750	55,031
Sept.	2,797	73,088	–	224,414	193,046	16,969	8,936	65,308	6,210	3,783	58,851
Oct.	2,802	74,705	–	227,646	191,894	17,338	9,264	64,178	6,860	3,746	61,454
Nov. (9)	5,778	75,118	–	231,372	194,604	17,520	9,235	75,323	7,356	3,692	67,500
Dec.	7,921	74,826	–	244,223	199,258	17,800	9,422	96,873	9,141	3,799	72,513
1986 - Jan. (9)	3,270	83,123	–	238,266	175,821	18,355	9,742	72,453	7,855	3,701	63,513
Feb. (9)	2,783	81,740	513	233,444	175,238	18,490	9,870	63,580	7,725	3,717	57,522
Mar.	3,293	79,547	740	232,514	176,872	18,786	10,079	64,534	8,655	3,742	56,053
Apr.	3,581	79,012	408	237,871	185,034	19,120	10,001	65,696	8,798	3,885	56,500
May	4,660	79,036	631	238,486	186,298	19,389	9,992	66,355	8,709	3,874	57,753
June	3,407	78,541	1,028	239,144	182,111	19,552	10,326	63,737	7,528	3,870	58,914
July	3,433	79,163	1,205	249,287	185,701	20,076	10,546	61,478	6,590	3,615	53,034
Aug.	3,115	79,424	–	244,688	187,791	20,274	10,476	66,768	6,884	3,942	53,196
Sept.	3,673	79,156	–	245,233	197,636	20,676	10,591	70,147	6,966	3,910	56,337
Oct.	2,982	81,212	–	253,920	196,124	21,002	11,146	73,507	7,715	3,890	61,614
Nov.	5,255	82,776	–	257,703	202,297	21,162	11,275	85,913	8,839	4,274	65,863
Dec.	4,680	83,794	–	266,040	211,150	20,963	11,719	107,793	8,846	4,179	70,750
1987 - Jan.	3,928	93,504	–	270,012	186,872	21,512	11,949	76,964	8,154	4,052	....
Feb.	3,347	91,670	–	269,749	186,114	21,913	12,241	70,236	8,355	4,109	....
Mar. (10)	5,900	89,800	–	266,130	192,800	22,350	....	....	....	....	....

(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: th the Bank of Italy. – (10) Provisional.

Table a 14

AND LIABILITIES *(1)*

of lire)

LIABILITIES									MEMORANDUM		
Deposits (6)	Other domestic funds (7)	Lending by BI-UIC	Interbank accounts	Deposits of special credit institutions	Funds raised abroad (5)	of which: non-residents' lira accounts	Equity capital	Other items	Loan guarantees	of which: bankers' acceptances issued	
152,025	1,232	2,552	24,332	4,664	19,319	798	6,518	5,241	17,211	–	.... Dec. - 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
372,240	3,568	6,349	83,320	5,252	72,669	3,022	29,518	11,584	51,854	1,590	.... " - 1983
415,581	4,949	2,864	89,233	4,518	91,908	3,879	36,989	14,547	58,313	609	.... " - 1984
411,126	5,347	3,838	63,626	5,165	85,280	3,974	36,846	13,628	57,483	572	.... Jan. - 1985
405,608	5,718	4,293	65,914	4,683	91,191	4,222	36,935	9,143	59,605	569	.... Feb.
407,372	5,893	2,881	63,837	4,689	89,485	4,213	38,690	13,500	60,030	554	.... Mar.
410,346	5,556	5,401	65,612	3,730	92,816	4,178	41,898	11,344	60,288	509	.... Apr.
406,055	5,397	3,684	67,077	3,746	92,991	4,389	42,154	21,636	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	42,087	21,453	61,164	456	..... July
414,780	5,352	3,093	62,107	3,952	87,512	4,586	42,090	21,128	60,983	456	.... Aug.
420,848	5,616	4,827	59,575	4,332	93,513	4,920	42,398	18,510	61,189	424	.... Sept.
422,048	5,548	3,309	57,913	3,845	91,517	4,762	42,731	29,230	61,272	422	.... Oct.
421,486	6,002	2,991	70,446	3,458	102,350	4,517	42,907	34,166	62,006	415	.. (9) Nov.
457,743	6,467	8,740	89,879	4,459	98,319	4,673	43,179	23,191	63,711	377	.... Dec.
447,476	6,585	5,451	66,683	5,218	90,762	4,776	43,247	6,976	63,828	443	.. (9) Jan. - 1986
438,354	6,477	5,627	59,148	4,863	86,424	4,377	43,438	6,574	65,427	784	.. (9) Feb.
438,426	6,355	2,691	59,487	4,799	87,975	4,572	46,039	5,301	68,126	1,010	.... Mar.
440,682	6,732	2,872	59,377	4,570	89,110	4,154	49,699	12,978	69,794	1,044	.... Apr.
438,320	6,395	2,512	58,372	4,843	92,273	4,611	49,855	18,740	72,387	918	.... May
439,994	5,979	4,335	57,167	5,500	92,447	4,893	50,159	8,705	72,847	803	.... June
440,833	6,327	4,218	57,325	5,439	85,182	4,796	50,965	20,221	72,494	647	..... July
440,751	6,301	2,977	61,487	4,813	84,439	5,233	51,009	20,838	72,891	564	.... Aug.
449,658	6,394	3,526	66,576	4,863	88,148	5,052	51,203	20,046	73,979	465	.... Sept.
455,895	5,934	3,352	71,306	4,381	93,776	5,269	51,321	23,259	75,062	415	.... Oct.
458,624	5,956	2,924	82,334	4,600	99,875	5,001	51,564	35,207	75,271	390	.... Nov.
498,678	4,815	4,407	97,980	5,340	102,858	6,019	51,585	20,072	64,230	307	.... Dec.
488,510	5,458	3,177	73,078	5,857	....	5,421	51,582	....	64,518	299	.... Jan. - 1987
481,036	5,098	3,081	68,301	4,981	....	5,736	52,007	....	64,479	301	.... Feb.
483,970	4,830	3,170	....	....	....	....	55,540	....	65,500	290	. (10) 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
	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)	(c) = (a)-(b)
												Banks and savings
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	4,182	39,092	25,911	6,700	7,825	83,710	45,137	494	5,423	7,643	58,697	25,013
1986 (3)	4,581	39,309	23,693	6,289	5,994	79,866	39,386	662	5,042	5,853	50,943	29,923
												Banks
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	3,181	28,715	18,021	4,420	7,130	61,467	31,391	459	4,748	6,997	43,595	17,872
1986 (3)	3,475	28,783	16,076	4,301	5,404	58,039	27,338	629	4,331	5,297	37,595	20,444
												Banks of
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	591	4,751	2,286	460	2,688	10,776	4,704	78	574	2,639	7,995	2,781
1986 (3)	620	4,655	2,211	469	2,060	10,015	4,117	225	674	1,978	6,994	3,021
												Public-law
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	875	7,176	6,197	901	2,166	17,315	8,385	272	2,047	2,131	12,835	4,480
1986 (3)	964	7,532	4,849	1,128	1,632	16,105	7,338	232	1,560	1,639	10,769	5,336

(1) Rounding may cause discrepancies in totals. As of 1983 the figures for interest on securities and positions with the Bank of Italy, as well as those for "Non-interest income", special times. – (3) Provisional.

BY CATEGORY OF BANK *(1)*

of lire)

Non-interest income (d)	of which: securities transactions	Gross income (e) = (c) + (d)	Operating expenses (f)	of which: staff costs	Net income (g) = (e)-(f)	Allocations to provisions (net) (h)	of which: for loan losses	Extraordinary income and withdrawals from provisions (i)	Taxes (l)	Net profit (g)-(h) + (i)-(l)	Total resources	Number of staff	
banks (2)													
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
9,944	5,319	34,957	23,421	16,832	11,536	5,182	2,438	548	3,659	3,243	771,837	304,090	 1985
11,684	6,469	40,607	25,655	18,444	14,952	5,504	2,458	135	5,133	4,450	838,517	307,590	... (3) 1986
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
7,789	4,307	25,661	17,531	12,646	8,130	3,527	1,560	523	2,539	2,587	581,088	233,022	 1985
8,981	5,080	29,425	19,108	13,760	10,317	3,607	1,737	55	3,487	3,278	628,450	235,266	... (3) 1986
national interest													
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	 1985
1,883	1,133	4,904	3,739	2,779	1,165	389	245	25	442	359	125,610	49,951	... (3) 1986
banks													
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
2,706	1,450	7,186	5,158	3,906	2,028	1,281	328	290	554	483	174,718	68,634	 1985
3,021	1,576	8,357	5,795	4,386	2,562	1,215	429	−9	756	582	187,880	70,614	... (3) 1986

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
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	1,044	10,243	5,673	1,523	1,556	20,003	10,787	92	1,592	1,544	14,015	5,988
1986 (3)	1,151	10,082	5,380	1,437	1,154	19,204	9,361	142	1,608	1,160	12,271	6,933
												Cooperative
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	671	6,545	3,901	1,536	720	13,373	7,515	17	535	683	8,750	4,623
1986 (3)	740	6,514	3,636	1,267	558	12,715	6,522	30	489	520	7,561	5,154
												Savings
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	1,001	10,377	7,890	2,280	695	22,243	13,746	35	675	646	15,102	7,141
1986 (3)	1,106	10,526	7,617	1,988	590	21,827	12,048	33	711	556	13,348	8,479
												Central credit
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	28	433	1,003	969	73	2,506	46	88	2,042	70	2,246	260
1986 (3)	4	400	718	513	55	1,690	51	88	1,222	57	1,418	272

(1) Rounding may cause discrepancies in totals. As of 1983 the figures for interest on securities and positions with the Bank of Italy, as well as those for "Non-interest income", special times. — (3) Provisional.

BY CATEGORY OF BANK (1)

of lire)

Non-interest income (d)	of which: securities transactions	Gross income (e) = (c) + (d)	Operating expenses (f)	of which: staff costs	Net income (g) = (e)-(f)	Allocations to provisions (net) (h)	of which: for loan losses	Extraordinary income and withdrawals from provisions (i)	Taxes (l)	Net profit (g)-(h) + (i)-(l)	Total resources	Number of staff	
credit banks (2)													
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	 1985
2,757	1,726	9,690	5,941	4,085	3,749	1,167	652	13	1,279	1,316	194,195	71,306	... (3) 1986
banks													
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	 1985
1,320	645	6,474	3,633	2,510	2,841	836	411	26	1,010	1,021	120,765	43,395	... (3) 1986
banks													
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	 1985
2,703	1,389	11,182	6,547	4,684	4,635	1,897	721	80	1,646	1,172	210,067	72,324	... (3) 1986
institutions (2)													
−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	22,475	1,371	 1985
143	116	415	147	78	268	54	43	11	105	120	21,724	1,386	... (3) 1986

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

(billions

	ASSETS										
	Cash and deposits (2)	Loans					Loans on behalf of the Treasury	Own portfolio (5)			TOTAL
		Domestic (3)	Financing of stockpiling (4)	Foreign		Total		Government securities	Bonds (6)	Shares & participations	
				Buyer credits	Credits to non-residents						
1977 - Dec.	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 - "	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.	5,330	136,566	806	3,302	255	140,929	8,060	17,037	2,645	2,744	176,745
Feb.	5,590	138,535	806	3,195	292	142,828	8,057	16,108	2,645	2,744	177,972
Mar.	5,580	141,376	819	3,261	353	145,809	8,058	15,329	2,442	2,758	179,976
Apr.	5,238	142,262	819	3,188	278	146,547	8,056	14,340	2,442	2,758	179,381
May	5,113	143,540	819	3,286	271	147,916	8,056	14,690	2,442	2,758	180,975
June	5,137	142,008	833	3,136	187	146,164	7,619	15,720	2,577	3,072	180,289
July	6,103	142,748	833	2,903	164	146,648	7,614	16,085	2,577	3,072	182,099
Aug.	5,146	143,283	833	2,874	174	147,164	7,613	16,809	2,577	3,072	182,381
Sept.	5,478	144,726	848	2,821	161	148,556	7,613	16,639	2,509	3,163	183,958
Oct.	4,200	147,062	848	2,897	232	151,039	7,721	15,516	2,509	3,163	184,148
Nov.	4,464	148,823	848	2,871	216	152,758	7,683	15,205	2,509	3,163	185,782
Dec.	4,567	152,813	855	2,962	225	156,855	8,057	14,511	1,992	3,398	189,380
1987 - Jan. (12)	5,760	152,702	855	2,763	223	156,543	7,494	15,890	1,992	3,398	191,077
Feb. (12)	5,256	154,239	855	2,775	237	158,106	7,493	15,883	1,992	3,398	192,128

(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 other medium-term deposits. – (8) Includes the proceeds of bond issues disbursed to special credit institutions. – (9) Includes compensatory loans in foreign currency deposited with the Bank of and "Other equity funds", which 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 behalf of the Treasury. – (12) Estimated.

SPECIAL CREDIT INSTITUTIONS *(1)*

of lire)

LIABILITIES											
Bonds		Certificates of deposit	Rediscounts	Short-term financing	Public funds	Mediocredito centrale funds	Foreign currency loans	Equity capital	Other	TOTAL	
On behalf of the Treasury	Other	(7)				(8)	(9)	(10)		(11)	
13,367	43,731	5,193	524	1,697	2,097	1,409	5,406	3,475	26	76,925	.... Dec. - 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
8,159	89,554	23,480	941	5,620	4,771	2,422	17,852	15,244	46	168,089	.... " - 1984
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	3,896	5,469	2,467	19,550	17,573	41	175,315	.... Oct.
7,145	93,802	24,604	1,017	4,318	5,483	2,509	19,742	17,573	41	176,234	.... Nov.
7,145	95,022	25,549	889	6,626	5,364	2,521	20,050	18,105	43	181,314	.... Dec.
6,546	95,118	25,743	889	5,399	5,616	2,477	19,857	18,105	43	179,793	.... Jan. - 1986
6,524	95,188	26,039	889	5,288	5,790	2,521	19,589	18,105	43	179,976	.... Feb.
6,523	95,709	26,305	973	5,745	5,912	2,541	20,234	18,968	35	182,945	.... Mar
6,512	96,176	26,433	973	6,358	6,058	2,576	20,312	18,968	35	184,401	.... Apr.
6,512	97,042	26,879	973	6,027	6,333	2,602	20,931	18,968	35	186,302	.... May
6,490	97,879	27,743	934	5,074	6,400	2,544	21,254	20,033	39	188,390	.... June
6,107	97,201	27,791	934	3,793	6,410	2,452	21,262	20,033	39	186,022	.... July
6,095	97,198	27,818	934	3,854	6,443	2,519	21,234	20,033	39	186,167	.... Aug.
6,091	97,893	27,860	1,050	3,910	6,424	2,507	21,274	20,554	26	187,589	...... Sept.
6,090	97,126	28,937	1,050	4,707	6,220	2,517	21,367	20,554	26	188,594	.... Oct.
6,090	98,125	29,280	1,050	5,395	6,427	2,527	21,172	20,554	26	190,646	.... Nov.
6,089	102,193	28,258	943	6,354	6,522	2,538	21,878	21,226	74	196,075	.... Dec.
5,490	102,243	28,417	943	5,080	6,557	2,484	21,980	21,226	74	194,494	.... (12) Jan. - 1987
5,457	102,392	28,753	943	4,706	6,586	2,569	20,405	21,226	74	193,111	.... (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, 1,034.4 billion at end-1985 and 849.4 billion at end-1986. – (7) Includes savings certificates and Italy. – (10) Paid-up capital 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, new definition, which includes certain 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

(billions

	Treasury bills (1)	BONDS AND — Public sector — Government securities — Variable rate Treasury credit certificates	Treasury bonds	Other certificates	Bonds of Deposits & Loans Fund	Other	Local government agencies	Autonomous government agencies	Bonds on behalf of Treasury	Total	Special credit — Industrial	Public works
												Gross
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	97,209	17,288	13,775	–	–	–	2,500	–	*130,772*	8,487	1,322
1986	265,866	79,255	53,276	2,079	–	–	–	2,500	–	*137,110*	10,535	922
												Re
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
1986	256,169	25,150	17,750	2,092	1,035	55	36	625	1,056	*47,799*	7,183	1,086
											Premiums,	**discounts**
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	–	1,542	315	–	–	–	–	–	–	*1,857*	72	7
1986	–	571	501	–	–	–	–	477	–	*1,549*	122	9
												Net
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	3,973	11,485	–1,022	–82	–50	2,216	–1,014	*94,073*	1,678	554
1986	9,697	53,534	35,025	–13	–1,035	–55	–36	1,398	–1,056	*87,762*	3,230	–173

(1) For these securities the net issues are obtained by deducting redemptions from gross issues.

Table a 17

GROSS AND NET ISSUES OF SECURITIES

of lire)

GOVERNMENT SECURITIES										SHARES	
institutions		Government agencies and firms							TOTAL bonds & government securities		
Real estate	Total	ENEL	ENI	IRI EFIM	Motor-ways (IRI)	Private firms	International institutions	Total			
issues											
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	151,307	14,977	1985
6,638	18,095	2,780	655	3,741	–	1,457	821	9,454	164,659	23,792	1986
demptions											
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	334	103	463	32	3,268	47,890	–	1985
3,360	11,629	1,469	339	619	98	699	55	3,279	62,707	–	1986
and double counting											
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	–	–	–	–	–	9	9	1,970	2,757	1985
72	203	14	–	–	–	–	17	31	1,783	4,920	1986
issues											
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	539	–103	685	509	2,196	101,447	12,220	1985
3,206	6,263	1,297	316	3,122	–98	758	749	6,144	100,169	18,872	1986

SOURCES AND USES OF MONETARY BASE *(1)*

(changes in billions of lire)

	SOURCES								TOTAL MONETARY BASE (4)	USES				
	FOREIGN SECTOR			TREASURY			REFINANCING	OTHER SECTORS (4)		NON-STATE SECTOR	BANK RESERVES			
	Balance of payments	Banks' net external position	TOTAL (2)	Borrowing requirement	Other financing (3)	TOTAL					Compulsory reserves	Non-interest-bearing deposit against excess lending	Excess reserves (4)	TOTAL (4)
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	29,642	760	2,624	689	*6,941*	2,631	5,508	–	–1,198	4,310
1980	–6,260	6,935	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	39,059	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	95,388	85,361	10,027	–218	–1,103	*13,847*	3,861	8,855	–2	1,133	9,986
1985	–8,352	–5,299	–13,677	122,828	95,309	27,519	5,881	–647	*19,076*	4,002	12,213	–	2,860	15,073
1986	–2,965	6,454	3,543	110,192	99,198	10,994	–4,333	–1,004	*9,200*	3,143	9,022	–	–2,965	6,057
1985 - Jan.	160	498	663	5,241	–1,322	6,563	976	–969	*7,233*	–2,579	10,934	–	–1,122	9,812
Feb.	–1,595	173	–1,427	9,213	10,001	–789	455	–121	*–1,882*	–267	–571	–	–1,044	–1,615
Mar.	–2,937	–905	–3,841	13,403	9,042	4,361	–1,414	–32	*–926*	1,191	–1,437	–	–679	–2,116
Apr.	–3,002	2,979	–23	10,025	11,708	–1,683	2,521	–918	*–102*	–857	–67	–	822	755
May (5)	496	797	1,293	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	1,224	*513*	1,914	–914	–	–487	–1,401
July	1,229	–1,466	–248	10,578	7,539	3,039	97	–650	*2,239*	1,286	1,409	–	–456	953
Aug.	1,671	–2,092	–407	7,442	7,585	–144	426	–556	*–681*	–1,193	962	–	–449	513
Sept.	–1,525	–940	–2,463	14,717	14,075	642	1,735	32	*–55*	–209	47	–	107	153
Oct.	–620	–1,179	–1,801	7,243	1,802	5,441	–1,520	–768	*1,352*	–258	1,617	–	–6	1,611
Nov. (5)	–1,931	–687	–2,620	13,931	8,144	5,786	–320	–27	*2,819*	1,227	414	–	1,178	1,592
Dec.	–1,433	–3,126	–4,585	8,235	5,212	3,023	5,751	3,034	*7,223*	3,415	–221	–	4,029	3,808
1986 - Jan.	–3,044	388	–2,630	1,030	–7,416	8,447	–3,262	–1,143	*1,412*	–2,647	8,727	–	–4,668	4,058
Feb.	–1,578	2,274	708	12,712	13,445	–733	150	–1,418	*–1,293*	370	–1,793	555	–425	–1,662
Mar. (6)	–2,074	2,928	1,028	12,505	9,135	3,370	4,010	–8,287	*121*	1,622	–2,188	322	364	–1,502
Apr.	2,287	–1	1,987	14,002	18,269	–4,266	–6,729	6,672	*–2,337*	–1,791	–574	–309	337	–546
May	1,555	2,182	3,790	10,345	13,479	–3,134	–400	1,490	*1,745*	341	51	275	1,079	1,405
June	664	–378	345	–4,411	–1,009	–3,402	1,854	617	*–585*	695	–515	497	–1,262	–1,280
July	1,459	–567	889	13,889	10,687	3,202	–147	–1,011	*2,934*	1,965	615	179	176	970
Aug.	703	–1,464	–763	8,051	9,223	–1,172	–1,214	277	*–2,872*	–1,080	83	–1,507	–369	–1,792
Sept.	–1,697	–331	–2,030	14,265	13,066	1,199	527	371	*68*	–422	–54	–5	550	490
Oct.	–651	1,953	1,283	7,078	4,223	2,855	19	–3,096	*1,060*	–433	2,074	–	–580	1,494
Nov.	–133	–550	–657	14,701	10,389	4,313	–605	1,665	*4,715*	795	1,590	–1	2,331	3,920
Dec.	–456	20	–408	6,024	5,708	316	1,465	2,858	*4,231*	3,728	1,004	–5	–496	503

(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 series has been adjusted for the growth in bank funds with the Bank of Italy attributable to the procedures for recording monthly stock exchange settlements. – (5) 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. – (6) The figure for "Refinancing" and "Other sectors" were affected by the provisional accounting procedures adopted as a result of the industrial action of the previous months.

INTEREST RATES ON BANK OF ITALY OPERATIONS

OFFICIAL

	Current accounts (1)			Bill discounting		
	At sight	Tied: 8-day	Tied: 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
14 Mar. 1987	"	"	"	11.50	"	11.50

EFFECTIVE

	Fixed term advances (2)	Repurchase agreements: Purchases Minimum	Purchases Average	Sales Maximum	Sales Average
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	–	–
May . .	13.41	11.75	12.43	–	–
June .	12.35	11.75	12.45	–	–
July . .	12.21	10.25	10.99	–	–
Aug. . .	13.69	9.55	10.51	–	–
Sept. .	12.00	8.60	9.78	11.00	10.63
Oct. . .	12.29	9.40	10.76	–	–
Nov. .	12.14	10.25	11.08	–	–
Dec. .	13.03	11.00	11.98	–	–
1987 - Jan. . .	13.20	11.50	12.50	–	–
Feb. . .	13.00	10.70	11.18	–	–
Mar. . .	12.50	–	–	11.00	10.18
Apr. . .	11.50	–	–	11.00	10.43

(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) On 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 was fixed at 9.50%. On 17 July 1986 the higher return on reserves was extended to certificates with maturities of between 3 and 6 months and the rate was reduced to 8.5 per cent with effect from I November. – (3) 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. – (4) The weighted average rate on actual operations. As of 16 February 1984 the penalties applied were 3.5, 2.5 and 1.5 points for operations undertaken within respectively 5, 15 and 30 days of the preceding ones. On 8 November 1985 the penalties were reduced to 2.25, 1.25 and 0.50 points.

MONEY MARKET AND BANK INTEREST RATES (1)

	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)		Certificates of deposit (4)		ABI prime rate (8)
							In lire	Total	Maximum	Average	Minimum	Average	6-month	12-month	
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	–	14.64	–	–	–	15.43
1980	15.94	15.98	15.47	15.92	16.77	11.79	20.32	19.41	14.86	–	19.03	–	–	–	19.93
1981	19.63	19.84	19.12	19.70	19.31	13.89	22.89	21.83	17.60	–	21.44	–	–	–	22.13
1982	19.38	19.37	19.43	19.44	19.91	15.03	23.08	21.65	18.82	–	21.62	–	–	–	21.54
1983	17.83	17.77	18.05	17.89	18.31	14.24	21.24	19.58	17.62	–	19.44	–	–	–	19.19
1984	15.30	15.29	15.43	15.37	17.27	12.93	19.07	17.73	16.14	–	17.64	–	–	–	17.67
1985	13.86	13.73	13.63	13.71	15.25	11.66	17.51	16.23	14.48	–	16.36	–	–	–	16.55
1986	11.93	11.46	11.15	11.40	13.42	9.32	15.65	14.53	11.99	8.89	14.08	15.93	11.98	11.99	14.18
1985 - Jan. ..	13.93	13.75	13.77	13.77	16.36	–	–	–	15.45	–	17.19	–	–	–	17.00
Feb. ..	13.62	13.46	13.36	13.42	16.09	–	–	–	15.15	–	16.89	–	–	–	17.00
Mar. ..	13.54	13.38	13.38	13.40	16.04	12.47	18.76	16.84	15.14	11.61	16.82	18.59	14.72	14.82	17.00
Apr. ..	14.41	14.31	14.00	14.24	15.67	–	–	–	15.05	11.58	16.78	18.44	14.53	14.83	17.00
May ..	14.47	14.22	13.90	14.15	15.46	–	–	–	14.86	11.41	16.69	18.36	14.47	14.68	17.00
June ..	14.41	14.18	13.95	14.12	15.28	11.87	18.27	16.44	14.73	11.27	16.58	18.27	14.23	14.63	17.00
July ..	14.22	14.08	13.99	14.07	14.96	–	–	–	14.52	11.00	16.53	18.15	13.93	14.34	17.00
Aug. ..	13.95	13.99	14.05	14.00	14.73	–	–	–	14.42	10.90	16.50	18.02	13.89	14.24	17.00
Sept. .	13.93	13.82	13.68	13.79	14.41	10.99	17.96	16.10	13.82	10.44	15.96	17.72	13.65	14.03	16.00
Oct. ..	13.28	13.33	13.20	13.27	14.39	–	–	–	13.63	10.20	15.63	17.33	13.28	13.69	16.00
Nov. ..	13.31	13.16	13.16	13.18	14.64	–	–	–	13.55	10.19	15.45	17.14	13.22	13.61	15.88
Dec. ..	13.23	13.10	13.14	13.14	14.93	11.29	16.93	15.52	13.43	10.11	15.29	16.86	13.21	13.61	15.88
1986 - Jan. ..	14.34	13.73	13.19	13.58	15.25	–	–	–	13.37	10.17	15.29	16.86	13.15	13.51	15.88
Feb. ..	14.17	13.59	13.08	13.40	16.71	–	–	–	13.36	10.22	15.65	17.45	13.16	13.52	16.00
Mar. ..	13.46	13.19	12.88	13.07	17.39	11.05	17.37	16.10	13.41	10.28	15.76	17.75	13.27	13.59	16.00
Apr. ..	12.99	12.39	11.84	12.28	15.50	–	–	–	12.94	9.98	15.42	17.53	13.02	13.43	15.25
May ..	11.60	11.23	11.00	11.18	13.47	–	–	–	12.35	9.36	14.78	17.02	12.48	12.76	14.50
June ..	11.24	10.78	10.57	10.74	12.51	9.07	16.71	15.20	11.67	8.59	13.89	16.20	11.84	11.70	13.50
July ..	11.24	10.71	10.56	10.75	12.35	–	–	–	11.51	8.30	13.54	15.50	11.63	11.49	13.50
Aug. ..	10.92	10.39	10.27	10.44	11.97	–	–	–	11.48	8.28	13.39	15.24	11.53	11.39	13.50
Sept. .	10.92	10.61	10.28	10.54	11.68	8.62	15.11	13.81	11.16	8.13	13.15	14.92	11.33	10.99	13.00
Oct. ..	10.79	10.38	10.08	10.35	11.32	–	–	–	11.03	7.90	12.89	14.49	10.92	10.75	13.00
Nov. ..	10.69	10.25	10.02	10.27	11.27	–	–	–	10.85	7.79	12.70	14.23	10.73	10.39	13.00
Dec. ..	10.81	10.25	10.01	10.25	11.59	8.55	14.01	13.00	10.69	7.62	12.55	13.93	10.69	10.18	13.00
1987 - Jan. ..	10.81	10.19	9.93	10.14	12.07	–	–	–	10.65	7.66	12.48	13.83	10.53	9.99	13.00
Feb. ..	10.69	9.98	9.74	9.93	12.19	–	–	–	10.43	7.49	12.29	13.78	10.08	9.88	12.88
Mar. ..	10.57	9.92	9.68	9.92	11.71	....	....	....	10.24	7.34	12.15	13.65	9.88	9.69	12.50
Apr. ..	10.23	9.85	9.65	9.84	10.92	–	–	–	10.01	7.09	11.83	13.41	9.75	9.60	12.50

(1) Annual figures are the average of monthly values. – (2) Annual compound rates, calendar year. Since September 1986 a 6.25 per cent withholding tax has been levied. – (3) Weighted average of allotment rates in the public auctions. – (4) Monthly average of rates reported at 10-day intervals. 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 21

INTEREST RATES ON 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				
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
1986	12.41	8.52	4.49	11.47	11.45	10.56	11.10	9.96	10.36	10.56	1.58
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	1.25
May . . .	13.12	8.35	5.19	10.89	10.87	10.28	11.19	9.45	10.83	10.36	1.32
June . . .	12.19	8.42	4.65	10.85	10.83	9.80	10.55	9.39	9.13	9.85	1.71
July	11.74	8.60	4.20	11.06	11.04	9.74	10.46	9.56	8.76	9.87	1.73
Aug. . . .	11.58	8.72	3.88	10.81	10.79	9.72	10.30	9.70	9.26	9.87	1.50
Sept. . . .	11.10	8.52	3.80	10.43	10.42	9.54	10.09	9.48	9.42	9.58	1.55
Oct. . . .	10.79	8.35	3.72	10.26	10.25	9.12	9.63	8.98	8.89	9.22	1.57
Nov. . . .	10.60	8.55	3.99	10.33	10.33	9.20	9.43	8.80	8.80	9.16	1.62
Dec. . . .	10.51	8.56	4.15	10.05	10.05	9.05	9.63	8.70	8.65	9.09	1.73
1987 - Jan. . . .	10.39	8.53	4.09	9.78	9.78	8.97	9.63	8.20	8.74	8.96	1.69
Feb. . . .	10.24	8.42	4.43	9.84	9.83	9.02	9.53	8.29	8.48	8.92	1.78
Mar. . . .	10.04	8.40	4.55	10.03	10.03	9.13	9.36	8.51	8.18	8.96	1.78
Apr. . . .	9.90	8.22	4.64	10.08	10.07	9.28	9.43	8.70	8.01	9.09	1.67

FINANCIAL ASSETS OF THE PRIVATE

(billions

	1977	1978	1979	1980	1981	1982	1983
FINANCIAL ASSETS:							
Domestic	**38,158**	**52,217**	**62,081**	**60,329**	**81,114**	**94,109**	**115,373**
M 1	15,214	19,156	25,365	19,264	22,340	30,147	23,470
M 2	31,365	36,459	43,539	34,285	36,307	60,477	45,100
M 3	34,880	40,173	51,760	51,146	61,267	72,142	60,267
Special credit institution deposits and savings certificates	236	1,034	423	414	1,356	6,858	1,364
Medium and long-term securities	52	5,707	3,218	–1,389	5,558	8,034	41,864
Investment fund units (2)	–	–	–	–	–	–	–
TOTAL ...	*35,168*	*46,914*	*55,401*	*50,171*	*68,181*	*87,034*	*103,495*
Shares and participations (3)	116	529	675	2,143	1,204	1,260	1,096
Other financial assets (4)	2,874	4,774	6,005	8,016	11,729	5,816	10,782
Foreign	**1,050**	**501**	**3,610**	**746**	**511**	**2,885**	**3,481**
Short-term trade credits (net)	949	–409	2,138	305	–1,734	2,065	–616
Medium and long-term trade credits and loans	–274	832	1,052	50	640	–219	1,630
Medium and long-term securities	–201	–67	–177	–179	–288	77	–545
Shares and participations (5)	576	145	597	569	1,892	962	3,013
TOTAL ...	**39,207**	**52,718**	**65,690**	**61,075**	**81,625**	**96,994**	**118,854**
AGAINST FINANCING OF:							
Private sector	**20,492**	**25,217**	**32,752**	**43,517**	**48,976**	**44,863**	**52,303**
Short-term borrowing	9,264	9,045	16,983	18,720	12,022	14,448	20,092
banks (6)(7)	*8,958*	*8,190*	*16,009*	*17,113*	*9,841*	*12,780*	*19,784*
special credit institutions (7)	*306*	*855*	*974*	*1,607*	*2,181*	*1,668*	*308*
factoring companies (8)	–	–	–	–	–	–	–
Medium and long-term borrowing	6,762	9,977	10,801	15,534	24,940	19,322	15,488
banks	*1,411*	*2,332*	*3,589*	*4,062*	*3,166*	*1,232*	*3,028*
special credit institutions (6)	*4,430*	*5,242*	*4,800*	*6,867*	*11,914*	*10,510*	*8,624*
leasing and consumer credit companies (8)	–	–	–	–	–	–	–
public sector	*80*	*–58*	*–296*	*–86*	*399*	*–83*	*689*
trade credits and foreign loans	*–395*	*1,487*	*2,227*	*4,497*	*8,641*	*3,074*	*755*
bonds	*1,236*	*974*	*481*	*194*	*820*	*4,589*	*2,392*
Shares and participations	2,718	4,375	2,465	5,164	6,023	10,321	13,163
shares (9)	*997*	*892*	*865*	*1,923*	*2,001*	*2,038*	*2,967*
endowment funds (10)	*1,177*	*2,494*	*836*	*2,952*	*3,154*	*7,384*	*9,431*
other participations (11)	*544*	*989*	*764*	*289*	*868*	*899*	*765*
Other financial liabilities (12)	1,748	1,820	2,503	4,098	5,992	771	3,560
Foreign sector (13)	**2,175**	**5,261**	**4,553**	**-8,569**	**-10,324**	**-8,371**	**2,408**
Public sector (14)	**16,737**	**22,767**	**27,651**	**33,546**	**52,019**	**66,363**	**76,525**
Unclassified (15)	**-197**	**-527**	**734**	**-7,419**	**-9,046**	**-5,861**	**-12,382**

(1) Rounding may cause discrepancies in the totals. – (2) Units of Italian investment funds. – (3) Excludes shares issued by state-controlled companies and taken up by their the units of foreign-based investment funds. – (6) Flows are adjusted for changes in exchange rates on foreign currency loans; also includes securities issued to fund debts and since 1985. – (9) Net share issues by private sector companies and the contribution of third parties to the financing of state-controlled companies. – (10) Net of the funding of state-loans granted by insurance companies and bank loans used to pay the non-interest-bearing deposit on payments abroad. – (13) Balance of payments on a transactions basis. – (14)

Table a 22

SECTOR AND THEIR COUNTERPARTS: FLOWS *(1)*

of lire)

1984	1985	1986	1985				1986			
			I	II	III	IV	I	II	III	IV
137,644	**140,746**	**169,591**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
30,813	26,069	34,951	−12,778	2,677	5,415	30,756	−14,134	4,097	5,825	39,163
54,893	53,821	55,344	−7,734	4,925	9,263	47,368	−17,818	2,134	11,051	59,977
75,917	68,992	59,269	1,075	14,277	14,486	39,155	−2,288	3	10,069	51,486
4,260	1,550	2,583	1,864	589	−1,638	735	630	1,437	117	399
43,108	43,102	47,844	14,959	8,920	9,983	9,240	12,687	12,954	10,316	11,887
1,055	15,256	37,509	3,634	3,288	3,344	4,990	12,954	15,422	6,378	2,755
124,340	*128,900*	*147,205*	*21,532*	*27,074*	*26,175*	*54,120*	*23,983*	*29,816*	*26,880*	*66,527*
1,850	−1,510	8,069	....	....	....	....	....	....	....	....
11,454	13,356	14,317	3,090	3,391	3,269	3,607	3,239	3,529	3,564	3,984
6,184	**2,871**	**6,920**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
2,547	−1,532	2,088	−169	−1,012	−760	409	−2,086	667	1,174	2,333
386	1,578	1,759	−14	99	363	1,130	296	992	249	222
−79	−12	−508	101	46	−11	−149	−21	−124	−505	141
3,330	2,838	3,582	....	....	....	....	....	....	....	....
143,829	**143,618**	**176,512**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
64,452	**66,941**	**70,848**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
34,312	30,946	27,629	2,536	2,964	2,936	22,511	−7,851	5,106	8,751	21,623
31,439	*27,156*	*19,762*	*1,805*	*2,659*	*2,422*	*20,271*	*−11,025*	*5,252*	*7,439*	*18,095*
2,873	*2,114*	*5,924*	*312*	*−114*	*95*	*1,821*	*2,688*	*−632*	*826*	*3,042*
–	*1,676*	*1,943*	....	....	....	....	....	....	....	....
14,789	20,712	26,570	6,873	2,685	4,570	6,585	9,404	3,018	4,967	9,180
3,884	*5,017*	*5,151*	*1,027*	*1,213*	*1,064*	*1,713*	*931*	*1,367*	*941*	*1,912*
9,027	*8,787*	*10,635*	*2,506*	*503*	*2,997*	*2,781*	*3,430*	*1,156*	*2,202*	*3,848*
–	*2,032*	*2,041*	*508*	....	....	....	....	....	....	....
811	*882*	*1,394*	*−71*	*−3*	*−55*	*1,011*	*197*	*1,027*	*143*	*27*
−839	*2,308*	*1,954*	*2,571*	*−347*	*−16*	*100*	*341*	*−52*	*241*	*1,424*
1,906	*1,687*	*5,395*	*332*	*810*	*73*	*472*	*3,995*	*−990*	*931*	*1,459*
12,542	11,081	13,797	....	....	....	....	....	....	....	....
4,948	*4,310*	*10,606*	....	....	....	....	....	....	....	....
6,548	*5,132*	*1,704*	....	....	....	....	....	....	....	....
1,046	*1,639*	*1,487*	....	....	....	....	....	....	....	....
2,809	4,201	2,852	1,094	1,019	1,048	1,040	1,239	565	427	621
−4,152	**−6,872**	**6,077**	**−5,188**	**−908**	**454**	**−1,230**	**−5,325**	**1,963**	**7,744**	**1,695**
94,378	**109,923**	**108,172**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**
−10,849	**−26,374**	**−8,585**	**....**	**....**	**....**	**....**	**....**	**....**	**....**	**....**

parent companies. — (4) Includes actuarial reserves, an estimate of atypical securities, the non-interest-bearing deposit on payments abroad and other minor items. — (5) Includes credit institutions' bad debts. The lending of banks excludes loans to pay the non-interest-bearing deposit on payments abroad. — (7) Includes acceptances acquired. — (8) Included controlled companies' debts with banks. — (11) Excludes the participations of the Treasury. — (12) Retirement funds, credit institutions' bad debts, an estimate of atypical securities, Includes the actuarial reserves of social security institutions. — (15) Includes the balances of financial intermediaries and discrepancies.

(billions

	1976	1977	1978	1979	1980	1981	1982
FINANCIAL ASSETS							
Domestic	**229,829**	**268,095**	**326,550**	**401,391**	**545,330**	**668,049**	**747,611**
notes and coin	13,953	15,781	18,534	21,001	24,544	28,839	32,308
demand deposits: with banks	55,535	68,224	83,567	104,145	121,452	138,739	164,648
with the Post Office	1,835	2,532	3,592	5,912	4,325	5,083	5,852
M1	*71,323*	*86,537*	*105,693*	*131,058*	*150,321*	*172,661*	*202,808*
savings deposits: banks (2)	59,879	73,578	87,111	100,837	112,163	124,214	151,744
PO	14,085	16,537	20,307	24,755	28,450	30,366	33,166
M2	*145,287*	*176,652*	*213,111*	*256,650*	*290,934*	*327,241*	*387,718*
Treasury bills	2,559	6,074	9,788	18,007	33,737	57,983	70,024
Bankers' acceptances	–	–	–	2	1,133	1,847	1,471
M3	*147,846*	*182,726*	*222,899*	*274,658*	*325,804*	*387,072*	*459,213*
Deposits and savings certificates with special credit institutions	3,669	3,905	4,939	5,362	5,776	7,132	13,990
Medium and long-term securities	17,192	17,630	23,689	27,730	27,016	33,161	42,200
of which: Treasury credit certificates (3)	*44*	*1,262*	*3,794*	*6,844*	*8,378*	*11,830*	*18,256*
Investment fund units (4)	–	–	–	–	–	–	–
Shares and participations	25,190	25,027	31,442	44,052	129,131	171,402	157,300
Other financial assets	35,932	38,808	43,582	49,588	57,603	69,283	74,907
Actuarial reserves + retirement funds	*34,111*	*38,486*	*43,174*	*48,889*	*56,592*	*63,964*	*73,227*
Deposits on payments abroad + other (5)	*1,821*	*321*	*408*	*699*	*1,011*	*5,319*	*1,680*
Foreign	**13,057**	**14,215**	**16,281**	**20,027**	**22,940**	**23,384**	**28,530**
Short-term trade credit (net)	175	1,394	2,240	4,342	4,653	2,280	3,562
Medium and long-term trade credits and loans	8,428	7,886	8,668	9,555	10,008	11,105	12,536
Medium and long-term securities	975	942	1,094	1,480	2,147	1,360	1,734
Shares and participations (6)	3,479	3,993	4,279	4,650	6,132	8,639	10,698
TOTAL...	**242,886**	**282,311**	**342,831**	**421,418**	**568,270**	**691,433**	**776,141**
AGAINST FINANCING OF							
Private sector	**171,540**	**191,962**	**222,392**	**267,676**	**391,191**	**478,091**	**516,173**
Short-term borrowing	56,432	65,142	73,297	88,843	106,332	119,254	133,040
banks (7)	*55,053*	*63,457*	*70,757*	*85,329*	*101,211*	*111,952*	*124,070*
special credit institutions (7)	*1,379*	*1,685*	*2,540*	*3,514*	*5,121*	*7,302*	*8,970*
factoring companies (8)	–	–	–	–	–	–	–
Medium and long-term borrowing	60,647	67,279	76,776	86,049	102,330	129,855	152,253
banks	*6,665*	*8,076*	*10,408*	*13,997*	*18,059*	*21,225*	*22,457*
special credit institutions	*35,134*	*39,130*	*43,609*	*47,207*	*53,464*	*63,689*	*73,707*
leasing and consumer credit companies (8)	–	–	–	–	–	–	–
public sector	*2,872*	*2,953*	*2,895*	*2,599*	*2,513*	*2,912*	*2,828*
trade credits and foreign loans	*5,775*	*5,572*	*7,284*	*9,150*	*15,005*	*27,891*	*34,515*
bonds	*10,201*	*11,549*	*12,580*	*13,096*	*13,289*	*14,138*	*18,745*
Shares and participations	34,299	36,573	45,969	61,344	144,720	183,547	182,515
shares	*27,168*	*27,177*	*33,247*	*46,746*	*125,835*	*157,605*	*148,440*
endowment funds	*4,417*	*5,595*	*7,974*	*8,789*	*12,505*	*18,090*	*25,617*
other participations (9)	*2,714*	*3,801*	*4,748*	*5,809*	*6,380*	*7,852*	*8,458*
Other financial liabilities (10)	20,162	22,968	26,350	31,440	37,808	45,435	48,365
Foreign sector	**-1,490**	**2,145**	**9,970**	**22,975**	**33,366**	**17,556**	**4,149**
Public sector (11)	**102,338**	**119,075**	**141,842**	**169,493**	**203,039**	**255,058**	**321,421**
Unclassified (12)	**-29,502**	**-30,871**	**-31,373**	**-38,726**	**-59,326**	**-59,272**	**-65,602**

(1) Rounding may cause discrepancies in totals. – (2) Includes certificates of deposit and banks' repurchase agreements with customers. – (3) Includes ordinary certificates, – (6) Includes the units of foreign-based investment funds. – (7) Includes acceptances acquired; the lending of the banks excludes loans used to pay the non-interest-bearing deposit investors other than credit institutions, an estimate of atypical securities, loans granted by insurance companies and bank loans used to pay the non-interest-bearing deposit

SECTOR AND THEIR COUNTERPARTS: STOCKS *(1)*
of lire)

1983	1984	1985 I	1985 II	1985 III	1985 IV	1986 I	1986 II	1986 III	1986 IV
884,589	**1,060,650**	**....**	**....**	**....**	**1,545,998**	**....**	**....**	**....**	**1,985,667**
36,256	39,922	38,433	39,382	39,755	43,730	43,320	42,591	42,741	46,841
182,913	209,733	197,846	199,688	205,463	230,686	217,104	222,797	228,127	261,921
7,109	7,437	8,034	7,920	7,187	8,745	8,603	7,736	8,081	9,350
226,278	*257,092*	*244,313*	*246,990*	*252,405*	*283,161*	*269,027*	*273,124*	*278,949*	*318,112*
169,687	188,103	192,161	194,057	197,208	207,866	202,848	199,861	204,185	217,675
36,853	42,517	43,503	43,855	44,552	50,506	51,840	52,864	53,766	61,090
432,818	*487,712*	*479,977*	*484,902*	*494,165*	*541,533*	*523,715*	*525,849*	*536,900*	*596,877*
85,561	107,550	116,450	125,921	131,254	123,224	137,956	135,281	134,781	127,200
1,101	544	520	437	406	348	926	776	455	296
519,480	*595,806*	*596,947*	*611,260*	*625,826*	*665,105*	*662,597*	*661,906*	*672,136*	*724,373*
15,354	19,614	21,478	22,067	20,429	21,164	21,794	23,231	23,348	23,747
84,986	128,362	141,734	150,864	161,048	171,940	183,470	197,904	209,605	221,890
51,340	*84,794*	*96,168*	*104,129*	*114,745*	*122,973*	*130,462*	*139,478*	*145,471*	*148,188*
–	1,146	5,028	9,069	13,411	19,783	36,980	52,880	62,351	65,079
179,120	218,619	....	....	....	557,544	....	....	....	825,800
85,649	97,103	100,195	103,585	106,853	110,462	113,702	117,230	120,793	124,778
83,730	*94,920*	*98,221*	*101,523*	*104,824*	*108,126*	*111,666*	*115,206*	*118,746*	*122,286*
1,919	*2,183*	*1,974*	*2,062*	*2,029*	*2,336*	*2,036*	*2,024*	*2,047*	*2,492*
35,462	**46,799**	**....**	**....**	**....**	**58,065**	**....**	**....**	**....**	**71,287**
2,987	2,517	....	....	....	4,195	....	....	....	6,215
16,364	19,344	....	....	....	19,739	....	....	....	20,333
1,279	1,320	....	....	....	1,335	....	....	....	1,214
14,832	23,619	....	....	....	32,796	....	....	....	43,525
920,051	**1,107,450**	**....**	**....**	**....**	**1,604,063**	**....**	**....**	**....**	**2,056,954**
590,252	**701,224**	**....**	**....**	**....**	**1,096,296**	**....**	**....**	**....**	**1,400,808**
152,629	184,051	186,741	188,862	191,158	211,879	202,442	206,520	213,343	234,444
143,351	*169,142*	*171,101*	*172,917*	*174,699*	*193,180*	*180,569*	*184,794*	*190,305*	*207,878*
9,278	*11,327*	*11,639*	*11,525*	*11,620*	*13,441*	*16,129*	*15,497*	*16,323*	*19,365*
–	*3,582*	*4,001*	*4,420*	*4,839*	*5,258*	*5,744*	*6,230*	*6,715*	*7,201*
173,904	197,145	....	....	....	213,026	....	....	....	234,623
25,485	*29,369*	*30,396*	*31,609*	*32,673*	*34,386*	*35,317*	*36,684*	*37,625*	*39,537*
81,465	*85,762*	*87,373*	*88,129*	*90,454*	*93,394*	*96,023*	*97,353*	*99,104*	*103,020*
–	*7,864*	*8,372*	*8,880*	*9,388*	*9,896*	*10,406*	*10,917*	*11,427*	*11,937*
3,518	*4,329*	*4,258*	*4,255*	*4,200*	*5,210*	*5,408*	*6,435*	*6,577*	*6,604*
42,297	*46,778*	....	....	....	*45,408*	....	....	....	*43,385*
21,139	*23,044*	*23,376*	*24,186*	*24,260*	*24,731*	*28,726*	*27,736*	*28,667*	*30,140*
208,710	258,408	....	....	....	601,189	....	....	....	854,517
165,553	*210,371*	....	....	....	*546,687*	....	....	....	*796,469*
32,408	*38,986*	....	....	....	*44,177*	....	....	....	*46,017*
10,749	*9,051*	....	....	....	*10,325*	....	....	....	*12,031*
55,009	61,620	64,566	66,009	68,490	70,202	73,229	74,382	76,383	77,224
12,845	**6,006**	**....**	**....**	**....**	**-14,638**	**....**	**....**	**....**	**-11,185**
397,946	**492,324**	**....**	**....**	**....**	**606,794**	**....**	**....**	**....**	**716,069**
-80,992	**-92,105**	**....**	**....**	**....**	**-84,389**	**....**	**....**	**....**	**-48,739**

those for health insurance institutions and Treasury certificates in ECUs. – (4) Units of Italian investment funds. – (5) Includes an estimate of atypical securities and other minor items. on payments abroad. – (8) Included since 1984. – (9) Excludes the participations of the Treasury. – (10) Retirement funds, credit institutions' bad debts, acceptances acquired by on payments abroad. – (11) Includes social security institutions' actuarial reserves. – (12) Includes the balances of financial intermediaries and discrepancies.

THE BANK'S CAPITAL AND RESERVES

Capital. — Some shareholders disposed of their interests in the Bank's capital during 1986, so that the distribution of shares and votes at 31 December was as follows:

Shareholders with voting rights:

Savings banks and pledge banks	79	with	177,922	shares	and	474	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	"
	97	with	299,922	shares	and	790	votes

Shareholders without voting rights:

Savings banks and pledge banks	9	with	78	shares
Total	106	with	300,000	shares

Reserves. — The changes in the ordinary and extraordinary reserve funds during 1986 are given below; the composition is also indicated in accordance with Article 2(6) of Law 649/1983.

Amounts in lire	Ordinary reserve fund	Extraordinary reserve fund
Balance at 31 December 1985	505,753,986,980	544,580,219,998
increase: due to appropriation of 20 per cent of profits for the year 1985	70,031,526,507	70,031,526,507
due to income received in 1986 from investment of reserves	89,840,351,104	81,422,669,868
decrease: due to distribution to shareholders of a part of the income accruing in the course of 1985 (Article 56 of the Statutes)	376,506,243	404,693,757
Balance at 31 December 1986	665,249,358,348	695,629,722,616

BALANCE SHEET
AND PROFIT AND LOSS ACCOUNT

BALANCE SHEET

ASSETS

GOLD				
I on hand			2,345,100,087,890	
II on deposit abroad			23,188,990,992,103	25,534,091,079,993
GOLD CREDITS (EMCF)				8,800,640,785,733
CASH ON HAND				48,825,634,767
DISCOUNTS AND ADVANCES				
I portfolio discounts:				
— ordinary bills		238,116,730,069		
— stockpiling bills		2,028,571,799,167	2,266,688,529,236	
II advances:				
— current account		1,857,685,204,320		
— fixed term		1,534,342,932,625		
— under Treasury Decree of 27.9.1974		—	3,392,028,136,945	
III deferred payments in the clearing system			—	5,658,716,666,181
BILLS FOR COLLECTION WITH CORRESPONDENTS				—
EXTERNAL ASSETS IN FOREIGN CURRENCIES				
I ECUs			10,139,175,113,264	
II other assets:				
— banknotes and foreign currency bills		705,830,124		
— current accounts with correspondents		740,082,589,732		
— time deposits		1,034,019,369,571		
— other		131,069,750,533	1,905,877,539,960	12,045,052,653,224
DOLLAR CREDITS (EMCF)				1,338,534,443,150
ITALIAN FOREIGN EXCHANGE OFFICE (UIC)				
I current account			14,215,829,882,832	
II special accounts			3,149,727,403,049	17,365,557,285,881
EXTRAORDINARY ADVANCE TO THE TREASURY				—
TREASURY CURRENT ACCOUNT				52,706,998,167,560
SUNDRY CLAIMS ON THE GOVERNMENT				777,877,573,198
SECURITIES				
I government and government-guaranteed securities:				
— freely available		70,058,293,110,965		
— investment of statutory reserves		400,398,194,183		
— investment of staff severance pay and pension funds		941,297,815,261	71,399,989,120,409	
II securities of companies and agencies:				
— investment of statutory reserves		660,503,229,097		
— investment of staff severance pay and pension funds		1,019,536,789,891	1,680,040,018,988	
III shareholdings and participations:				
— in subsidiary companies and agencies				
investment of statutory reserves	655,396,631			
investment of staff severance pay and pension funds	128,798,026,898	129,453,423,529		
— in associated companies and agencies				
investment of statutory reserves	9,330,958,015			
investment of staff severance pay and pension funds	25,051,939,959	34,382,897,974		
— in other companies and agencies				
investment of statutory reserves	148,897,041,368			
investment of staff severance pay and pension funds	181,877,016,581	330,774,057,949	494,610,379,452	73,574,639,518,849
			carried forward	197,850,933,808,536

LIABILITIES

NOTES IN CIRCULATION		50,527,823,678,000
BANCA D'ITALIA DRAFTS		739,087,521,535
OTHER SIGHT LIABILITIES		
I transfer orders	—	
II other	2,799,250,001	2,799,250,001
FREE DEPOSITS ON CURRENT ACCOUNT		674,550,907,280
TIED DEPOSITS ON CURRENT ACCOUNT		—
DEPOSITS FOR CASH DEPARTMENT SERVICES		52,838,718,659
COMPULSORY DEPOSITS		
I compulsory bank reserves	84,714,072,391,613	
II collateral for the issue of bankers' drafts and guaranteed personal cheques	233,696,801	
III tied deposits in relation to investment abroad	20,136,830,316	
IV in respect of companies in the process of incorporation	19,421,922,712	
V in respect of bank lending in excess of the ceiling	178,068,000	
VI other	88,102,637,349	84,842,145,546,791
DEPOSITS IN FOREIGN CURRENCY ON BEHALF OF THE UIC		—
EXTERNAL ACCOUNTS IN LIRE ON BEHALF OF THE UIC		3,149,727,403,049
EXTERNAL LIABILITIES		
I deposits in foreign currencies	3,899,504,470	
II external accounts in lire	242,939,276,861	246,838,781,331
ECU LIABILITIES (EMCF)		10,139,175,228,883
SUNDRY LIABILITIES TOWARDS THE GOVERNMENT		878,334,494,669
SUNDRY PROVISIONS		
I for gold price fluctuations (under Decree Law 867/1976)	30,572,738,707,020	
II for losses ensuing from exchange rate management (under Decree Law 867/1976)	1,200,795,276,401	
III for losses on bill portfolio	234,919,178,078	
IV for losses on foreign exchange	1,599,974,253,181	
V for losses on securities	3,833,744,665,152	
VI for contingent losses	2,403,006,748,480	
VII for insurance cover	676,691,685,925	
VIII for building works	1,352,335,914,883	
IX for renewal of equipment	356,250,000,000	
X for taxation	1,568,744,188,241	
XI for staff severance pay and pensions	2,957,833,000,000	
XII for grants to BI pensioners and their surviving dependants	746,857,598	
XIII for severance pay to contract staff under Law 297/1982	519,578,644	46,758,300,053,603
	carried forward	198,011,621,583,801

AMOUNTS IN LIRE

BALANCE SHEET

ASSETS

brought forward			197,850,933,808,536
UIC ENDOWMENT FUND			500,000,000,000
REAL PROPERTY			
I Bank premises		1,563,399,804,153	
II investment of staff severance pay and pension funds		184,262,333,333	1,747,662,137,486
OTHER INVESTMENTS OF STAFF SEVERANCE PAY AND PENSION FUNDS			24,241,054,304
FURNITURE AND EQUIPMENT			
I furniture and fittings		66,389,107,367	
II equipment		148,908,453,858	
III coins and collections		307,195,088	215,604,756,313
SUNDRY ITEMS			
I banknotes in production		7,785,150,215	
II procedures, studies and designs of the technical departments:			
I completed	45,430,324,797		
I in preparation	7,710,116,220	53,140,441,017	
III sundry debtors		76,604,736,959	
IV other		1,149,174,394,419	1,286,704,722,610
ACCRUED INCOME			2,455,050,304,547
PREPAID EXPENSES			—
			204,080,196,783,796
MEMORANDUM ACCOUNTS			
I Securities and other valuables:			
— held as collateral	5,594,209,164,170		
— other	693,216,479,299,980	698,810,688,464,150	
II Depositaries of securities and valuables:			
— domestic	—		
— foreign	1,857,010,544,043	1,857,010,544,043	
III Unused overdraft facilities		889,959,539,405	
IV Debtors for securities receivable (BI forward sales)		3,780,500,000,000	
V Securities receivable (BI forward purchases)		—	
VI Debtors for foreign currencies and lire receivable (BI forward sales)			
— domestic	—		
— foreign	4,950,000,000,000	4,950,000,000,000	
VII Foreign currencies and lire receivable (BI forward purchases)		4,950,000,000,000	
VIII Exchequer for depreciation allowances		753,236,422,953	715,991,394,970,551
TOTAL . . .			**920,071,591,754,347**

Audited and found correct. — Rome, 30 April 1987

THE AUDITORS

DOMENICO AMODEO
VITTORIO CODA
LUIGI GUATRI
ARNALDO MAURI

LIABILITIES

		brought forward	198,011,621,583,801
ACCUMULATED PROPERTY DEPRECIATION			403,274,077,232
ACCUMULATED DEPRECIATION OF FURNITURE AND FITTINGS			66,029,633,903
ACCUMULATED DEPRECIATION OF EQUIPMENT			125,527,842,702
ACCUMULATED DEPRECIATION OF THE PROCEDURES, STUDIES AND DESIGNS OF THE TECHNICAL DEPARTMENTS			23,190,988,570
SUNDRY ITEMS			
I sundry creditors		518,111,226,717	
II other		772,988,393,463	1,291,099,620,180
ACCRUED EXPENSES			145,104,851,210
DEFERRED INCOME			957,998,260,664
CAPITAL		300,000,000	
ORDINARY RESERVE FUND		665,249,358,348	
EXTRAORDINARY RESERVE FUND		695,629,722,616	1,361,179,080,964
REVALUATION SURPLUS RESERVE UNDER LAW 72/1983			1,304,000,000,000
NET PROFIT FOR DISTRIBUTION			391,170,844,570
			204,080,196,783,796
MEMORANDUM ACCOUNTS			
I Depositors of securities and other valuables		698,810,688,464,150	
II Securities and valuables on deposit		1,857,010,544,043	
III Holders of unused overdraft facilities		889,959,539,405	
IV Securities for delivery (BI forward sales)		3,780,500,000,000	
V Creditors for securities for delivery (BI forward purchases)		—	
VI Foreign currencies and lire for delivery (BI forward sales)		4,950,000,000,000	
VII Creditors for foreign currencies and lire for delivery (BI forward purchases)			
— domestic	—		
— foreign	4,950,000,000,000	4,950,000,000,000	
VIII Depreciation allowances		753,236,422,953	715,991,394,970,551
		TOTAL . . .	**920,071,591,754,347**

THE ACCOUNTANT GENERAL

LUIGI GIANNOCCOLI

THE GOVERNOR

CARLO AZEGLIO CIAMPI

AMOUNTS IN LIRE

PROFIT AND LOSS ACCOUNT

EXPENDITURE AND LOSSES

COSTS OF ADMINISTRATION			
central and local boards		1,506,271,763	
staff:			
wages and salaries and related costs	616,104,946,694		
pensions and severance payments	239,411,793,874	855,516,740,568	
provision of services		93,274,180,240	
other		151,777,402,295	1,102,074,594,866
TAXES AND DUTIES			
stamp duty on the circulation of banknotes and demand drafts		—	
other taxes and duties:			
current year	37,608,638,205		
previous years	470,091,038,000	507,699,676,205	507,699,676,205
INTEREST PAID			
on compulsory bank reserves		4,627,343,274,989	
other		80,408,978,515	4,707,752,253,504
EXPENDITURE ON SECURITIES TRANSACTIONS			9,729,567,561
EXPENDITURE ON FOREIGN TRANSACTIONS			33,116,739
LOSSES ON SECURITIES DEALINGS			—
EXCHANGE RATE LOSSES			158,875,850,948
LOSSES ON REALIZATION OF ASSETS			—
CONTRIBUTIONS TO CHARITIES AND SOCIAL AND CULTURAL ACTIVITIES			1,478,871,384
TECHNICAL DEPARTMENTS — INITIAL STOCKS			20,138,959,868
EXPENDITURE ON TRANSACTIONS WITH THE TREASURY			2,634,323,069,000
VALUATION LOSSES			
on securities		41,314,429,980	
on foreign exchange		177,295,723,080	
on other assets		—	218,610,153,060
DEPRECIATION			
of Bank premises		48,999,735,216	
of furniture and fittings		8,276,400,884	
of equipment		18,277,309,074	
of the procedures, studies and designs of the technical departments		11,685,221,109	
other		14,270,551	87,252,936,834
APPROPRIATION OF INVESTMENT INCOME TO RESERVES			
to ordinary reserve fund		89,840,351,104	
to extraordinary reserve fund		81,422,669,868	171,263,020,972
		carried forward	9,619,232,070,941

INCOME AND PROFITS

INTEREST RECEIVED				
on discounts and advances:				
ordinary portfolio discounts		22,177,008,405		
stockpiling portfolio discounts		19,833,627,828		
advances		208,626,068,189	250,576,704,422	
on lending to the Treasury			556,882,369,347	
on lending to the UIC			725,641,271,372	
on lending abroad			284,875,925,935	
other			8,598,756,873	1,826,575,027,949
INTEREST, PREMIUMS AND DIVIDENDS ON SECURITIES				
freely available				
interest-bearing:				
Treasury bills	1,940,091,892,587			
variable rate Treasury credit certificates	4,160,156,498,239			
other government securities	1,500,308,532,752	7,600,556,923,578		
government-guaranteed securities		181,964,199,147	7,782,521,122,725	
investment of reserves and staff severance pay and pension funds				
interest-bearing:				
government and government-guaranteed securities	174,649,512,844			
other securities	161,958,439,096	336,607,951,940		
from participations (not represented by securities) in:				
subsidiary companies and bodies	6,026,962,610			
associated companies and bodies	1,713,075,040			
other companies and bodies	29,016,559,721	36,756,597,371	373,364,549,311	8,155,885,672,036
INCOME FROM PARTICIPATION IN THE UIC ENDOWMENT FUND				301,984,778,117
PROFITS FROM DEALINGS IN AND REDEMPTION OF SECURITIES				113,282,121,851
EXCHANGE RATE GAINS				497,037,752,789
COMMISSIONS AND OTHER FINANCIAL REVENUES				—
INCOME FROM REAL PROPERTY				12,426,388,118
PROFITS FROM THE SALE OF:				
real property			1,044,560,000	
other property			2,705,915,269	3,750,475,269
TECHNICAL DEPARTMENTS - FINAL STOCKS				16,832,501,214
TECHNICAL DEPARTMENTS - PROCEDURES, STUDIES AND DESIGNS COMPLETED DURING THE YEAR				12,343,707,693
VALUATION GAINS				
on securities			—	
on foreign exchange			—	
on other assets			—	—
			carried forward	11,205,364,831,943

AMOUNTS IN LIRE

PROFIT AND LOSS ACCOUNT

EXPENDITURE AND LOSSES

brought forward		9,619,232,070,941
ALLOCATIONS TO PROVISIONS		
for losses on bill portfolio	—	
for losses on foreign exchange	177,300,000,000	
for losses on securities	630,000,000,000	
for contingent losses	—	
for insurance cover	34,000,000,000	
for building works	49,000,000,000	
for renewal of equipment	30,000,000,000	
for taxation	570,000,000,000	
for staff severance pay and pensions	442,500,000,000	
for grants to BI pensioners and their surviving dependants	240,356,061	
for severance pay of contract staff under Law 297/1982	413,976,371	1,933,545,332,432
NON-OPERATING LOSSES AND EXTRAORDINARY CHARGES		317,019,495
		11,553,003,422,868
NET PROFITS		391,170,844,570
TOTAL...		**11,944,174,267,438**

APPROPRIATION

TO ORDINARY RESERVE FUND . . . .

TO EXTRAORDINARY RESERVE FUND . . . .

TO SHAREHOLDERS . . . .

TO THE TREASURY . . . .

Audited and found correct. - Rome, 30 April 1987

THE AUDITORS

DOMENICO AMODEO
VITTORIO CODA
LUIGI GUATRI
ARNALDO MAURI

INCOME AND PROFITS

	brought forward	11,205,364,831,943
WITHDRAWALS FROM PROVISIONS		
for losses on bill portfolio	—	
for losses on foreign exchange	177,295,723,080	
for losses on securities	41,314,429,980	
for contingent losses	—	
for insurance cover	—	
for building works	48,999,735,216	
for renewal of equipment	—	
for taxation	470,091,038,000	
for staff severance pay and pensions	—	
for grants to BI pensioners and their surviving dependants	94,310,000	
for severance pay of contract staff under Law 297/1982	—	737,795,236,276
NON-OPERATING PROFITS AND EXTRAORDINARY EARNINGS		1,014,199,219
	TOTAL...	**11,944,174,267,438**

OF PROFITS

	78,234,168,914
	78,234,168,914
	30,000,000
	234,672,506,742
TOTAL...	**391,170,844,570**

THE ACCOUNTANT GENERAL

LUIGI GIANNOCCOLI

THE GOVERNOR

CARLO AZEGLIO CIAMPI

ADMINISTRATION OF THE BANK OF ITALY
AT 31 DECEMBER 1986

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

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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
Luigi PATRIA — CENTRAL MANAGER FOR TECHNICAL DEPARTMENTS
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
Giorgio MAYDA — INSPECTOR GENERAL

LIST OF ABBREVIATIONS

ABI	—	*Associazione bancaria italiana* Italian Bankers' Association
ANAS	—	*Azienda Nazionale Autonoma delle Strade Statali* State Road Agency
ANIA	—	*Associazione Nazionale fra le imprese assicuratrici* National Association of Insurance Companies
BI	—	*Banca d'Italia* Bank of Italy
CIPA	—	*Convenzione interbancaria per i problemi dell'automazione* Interbank Convention on Automation
Confindustria	—	*Confederazione generale dell'industria italiana* Confederation of Italian Industry
Consob	—	*Commissione nazionale per le società 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
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