

## CENTRAL BANK RATES: 1863 – 1998

The data relating to the **discount rate** refer to the National Bank of the Sardinian States from 1863 to 1867, the National Bank in the Kingdom of Italy from 1867 to 1893, and the Bank of Italy from 1894 to 1998.

Law 449/1893 relating to the establishment of the Bank of Italy provided that discounting could be carried out at a **‘normal’ rate** for banking, business and private customers, on bills of exchange, checks and other financial instruments (treasury bonds, pledges on assets, coupons).<sup>1</sup> The maximum maturity of the underlying securities was set at four months. The methods for determining the ‘normal’ discount rate changed over time, as the Bank of Italy changed from a private banking institution (under public control for issuance activities carried out under a government concession) to a central bank.<sup>2</sup> With the 1936 Banking Law, the discounting operations of the Bank of Italy were limited to credit institutions only (it could not engage in commercial banking).<sup>3</sup> In the following years, discounting operations gradually lost their importance, while the signalling value of the official discount rate (as it was called under the 1936 Banking Law) began to increase as a fundamental parameter of monetary policy.

From 1969 until 1986 there was also a provision mandating an increase to the official discount rate to be applied to credit institutions which, in the previous six months, had made use of discount operations for average amounts exceeding one per cent of the stock of lending subject to minimum reserves or for the redemption of bills of exchange with special characteristics.

Alongside the normal discount rate, from the moment the 1893 law was enacted until 1928, a **‘favourable’ rate** was envisaged to discount bills presented by cooperative banks and agricultural credit institutions (one percentage point lower than the ‘normal’ one).<sup>4</sup>

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<sup>1</sup> Law 449/1893 established the possibility for the Bank of Italy to carry out discounting and credit advance operations exclusively. This law, concerning all issuing activity in Italy, also limited the activities of the Banco di Napoli and the Banco di Sicilia to discounting and credit advance operations, further establishing that the ‘normal’ rate would be the same for the three issuing banks.

<sup>2</sup> The ‘normal’ discount rate was initially established with a resolution, subject to government authorization, of the Board of Directors of the Bank of Italy (according to the 1893 law). As of 1907, ‘the Minister of the Treasury [...] can promote changes in the normal rate of discount [of the Bank of Italy and of the Southern issuing institutions] when he deems that market conditions require it’ (Law 804/1907, Annex A). With the reform of the Statute of the Bank of Italy in 1928, without prejudice to the requirement of ministerial authorization, the power to establish the normal discount rate passed from the Board of Directors to the Governor. The 1936 Banking Law gave the Governor of the Bank of Italy the sole right to present proposals to the Minister of the Treasury to change the official discount rate. The actual change was ordered by the Minister of the Treasury by decree. The system was finally modified only at the beginning of the 1990s, when Law 82/1992 gave the Governor the power to autonomously issue a measure to modify the discount rate (and the interest on current account and fixed-term advances) if this was necessary to control market liquidity. As of 1 January 1999, with the start of European monetary union, the Bank of Italy ceased to determine the official discount rate.

<sup>3</sup> Advances to commercial customers, on the other hand, were still permitted.

<sup>4</sup> Discounting at a ‘favourable’ rate, provided for in Italian law since 1885 (Article 2 of Law 3167/1885), was permitted up to a sum equal to half of the capital considered for the issue and subject to overall limits which, initially fixed at 70 million lire for the Bank of Italy, 21 million lire for the Banco di Napoli and 4.5 million lire for the Banco di Sicilia, were then raised

From 1895 until 1928, a third rate was envisaged, the '**reduced**' **discount rate** (Royal Decree 639/1895), set by government decree as the lower limit for discount operations to be offered, at the discretion of the Bank, to particular categories of customers for bills with a maturity of no more than three months and guaranteed by first-rate business and banking institutions.<sup>5</sup> From the end of the First World War, discounts at a reduced or preferential rate were drastically cut back (since they were not advantageous for the issuing institution in view of the tax on circulation in excess of normal limits), and then ceased completely at the end of the 1920s.

The **interest rate on ordinary advances** was available from 1893 to 1998.

According to the 1893 law, the ordinary advance would be guaranteed by a pledge on securities or goods, to be granted only in the form of a current account credit line, renewable upon expiry, which was initially set at six months and subsequently reduced to four months starting in 1907.<sup>6</sup> The methods for determining the interest rate for advances were basically the same as those for the discount rate.

The rate on ordinary advances also applied to fixed-term advances which, starting from 1967, could be granted at the discretion of the Bank of Italy at the request of the financial intermediary concerned in relation to its temporary cash requirements (the refinancing function of the banking system). Initially, there were three initial maturity dates: at 8, 15 and 22 days; after 1992 the maturity date could vary from 1 to 32 days. Since March 1969, alongside the base rate, which coincided, as mentioned, with the rate on ordinary advances, a surcharge was envisaged for advances with a fixed maturity – the interest rate increased for transactions subsequent to the first one entered into during the six-month period, as a way to avoid excessive use of this instrument. After 1991, there was a single surcharge, with an upper limit of 1.75 per cent.

The sources for the reconstruction of the historical series of the various types of rates are the official publications of the Bank of Italy and its predecessor institutions. Summary tables for the time intervals under consideration are available in the individual volumes referred to in the bibliography. The time intervals taken into consideration in each publication are shown in the Excel sheet attached to the data sheet.

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in 1907 to 100 million lire for the Bank of Italy, 30 million lire for the Banco di Napoli and 9 million lire for the Banco di Sicilia (Law 804/1907, Annex A).

<sup>5</sup> The 'reduced' and the normal discount rates are respectively the floor and the ceiling of the effective rates that the Banca d'Italia (as well as the southern issuing institutions) applied to specific customers and to the type of securities presented for discounting. The presence of preferential rates alongside the 'normal rate' meant that issuing institutions could apply different discounting conditions depending on the degree of customer reliability and it made the situation in Italy similar to that of the majority of countries adopting the gold standard. The number of interest rate classes with which banks worked was reduced in periods of monetary tightening, when the discount was granted only at the highest rates. The normal rate tended to stay the same and only changed when it was not enough, for the management of circulation, to bring all the discounting operations transactions to the highest rate class.

<sup>6</sup> Law 804/1907, Annex A.

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