Report of the Deutsche Bundesbank

for the Year 1983

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Note: In order to expedite publication of the English version of this Report the following sections contained in the German original have been omitted:

Part A	Bank supervision, domestic and external monetary and foreign exchange policy regulations of the Deutsche Bundesbank
Part C	Fund for the Purchase of Equalisation Claims
Appendices to Parts B and C	Nos. 1, 3, 4 and 5

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Contents

Part A
General Part

The currency and the economy in 1983

I. Economic developments and central bank policy 1
1 Upturn in economic activity 3
2 Progress in the consolidation of public budgets 15
3 The external situation under the influence of sharp exchange rate fluctuations 24
4 Monetary policy remains on a steadying course 33
(a) Monetary target for 1983 and money market management during the year; monetary target for 1984 33
(b) Recent experience with the central bank money stock as a monetary indicator and intermediate target 37
(c) Strong monetary expansion 39
(d) Private demand for credit stronger . . . 42
(e) Business situation and profitability of the banking groups 44
(f) Productive capital market 45
5 Competitiveness in export markets well maintained despite a few weak spots 51

II. International monetary developments and policy 59
1 The situation in the world economy 59
2 International trade and current transactions . . 60
3 Exchange rate developments and policy . . . 62
(a) Trends in major freely floating currencies . 64
(b) Developments within the European Monetary System 67
(c) Exchange market intervention policy . . . 70
(d) Issues relating to the international monetary system 74
4 The development of global monetary reserves . 74
5 The debt problems of the developing countries 76
6 The international financial markets 81
7 Financial assistance granted by the IMF and the multilateral development banks 83

Part B
Notes on the Deutsche Bundesbank's annual accounts for 1983

1 Legal basis, classification and valuation . . . 88
2 Annual accounts 88

Part D

Report of the Central Bank Council 111

Appendix to Part B

Annual accounts of the Deutsche Bundesbank as at December 31, 1983
Balance sheet as at December 31, 1983 . . . 116
Profit and loss account for the year 1983 . . . 118

The German original went to press on April 12, 1984

Part A: General part

The currency and the economy in 1983

I. Economic developments and central bank policy

The economic performance of the Federal Republic of Germany in 1983 was quite satisfactory on the whole. Aggregate production grew again, for the first time since 1980. Over the whole of 1983 the real gross national product was almost 1½ % higher than in 1982. The rise in production gathered pace, however, in the course of the year, the annual growth rate in the fourth quarter being as high as 3 %, and according to the available data economic expansion continued unabated in the first few months of 1984. The most important stimuli for the economic recovery emanated at first from the domestic market, particularly from housing construction and private consumer demand. At the same time, enterprises' willingness to invest grew, initially as a result of the investment grant enacted in spring 1982 but increasingly also on account of improved sales and profitability expectations in business. The higher volume of investment is being directed to modernising and extending productive capacity, and the increased application of modern technology is strengthening the competitiveness of the German economy in international trade. The revival in investment activity must therefore be viewed as a key to safeguarding the economic future, not only because of its immediate favourable effects on overall demand and production but also and particularly in view of long-term growth and employment opportunities. Exports were an additional support, as from last summer, for the cyclical upswing at home. Increasing investment activity and growing foreign demand have been buttressing economic growth since then without further government pump-priming measures; growth has therefore become self-sustaining. 1

Another positive item on the economic record for last year is, moreover, that a higher degree of financial stability was attained at the same time as the economic recovery. This was particularly true for monetary stability. In spite of influences from abroad that tended to push up prices — at times quite strongly — domestic industrial producer and consumer prices rose less in 1983 than in the previous year or any year since 1978. Construction prices also went up very little, while agricultural producer prices actually fell somewhat. Experience has shown that price movements are always subdued in the first year of a cyclical upswing, as the increase in productivity is relatively large and wages go up moderately. As the economic recovery proceeds, however, more and more problems occur, but they can be overcome if employers and employees remain conscious of the need for stability, particularly when negotiating on wages and salaries.

The progress made towards the necessary consolidation of government finance in Germany was also anything but minor. The reduction of budget deficits was continued in 1983, largely by reducing the rise in expenditure, and to a lesser extent by further increasing some taxes and social security contributions. Although this also entailed cuts in capital expenditure, particularly among the local authorities, this policy of consolidation, i.e. of lowering the government deficit (specifically: its structural part), did not hamper the economic recovery; the "overconsolidation" which had been feared in some quarters did not materialise. A major reason why the strong reduction in the budget deficits increased the scope for private investment was that public sector calls on the capital market fell. In future, it will be important not to jeopardise the successes achieved by this consolidation policy.

Measured by the extent of unemployment, the first positive reactions observable on the labour market have been modest. However, changes in the employment situation always tend to lag well behind cyclical improvements. Looked at from this point of view, the decline in the seasonally adjusted number of unemployed since summer 1983 certainly warrants optimism.

Key data on overall economic developments

Period	Gross national product 1	Employed persons 2		Unemployment ratio 3	Consumer prices; 4 annual increase	Balance on current account
	Annual change					
	%		Thousands	%	%	DM billion
1970 to 1973 5	+ 4.2	+ 0.5	+ 140	0.8	+ 5.3	+ 5.3
1974 to 1979 5	+ 2.4	− 0.6	− 150	3.5	+ 4.6	+10.5
1980 to 1983 5	+ 0.4	− 0.8	− 210	5.8	+ 4.9	− 5.7
1974	+ 0.5	− 1.3	− 360	2.2	+ 7.0	+26.6
1975	− 1.6	− 2.8	− 760	4.0	+ 6.0	+ 9.9
1976	+ 5.6	− 0.8	− 220	4.0	+ 4.3	+ 9.9
1977	+ 2.8	− 0.2	− 40	3.9	+ 3.7	+ 9.5
1978	+ 3.5	+ 0.6	+ 150	3.8	+ 2.7	+18.1
1979	+ 4.0	+ 1.3	+ 340	3.3	+ 4.1	−11.1
1980	+ 1.9	+ 1.0	+ 260	3.3	+ 5.5	−28.6
1981 p	− 0.3	− 0.8	− 200	4.8	+ 5.9	−13.1
1982 p	− 1.1	− 1.8	− 470	6.7	+ 5.3	+ 8.7
1983 p	+ 1,3	− 1.7	− 450	8.1	+ 3,0	+10.1

1 At 1976 prices. — **2** Persons employed in Germany; absolute figures rounded. — **3** Unemployed persons as % of the total labour force.— **4** Cost of living index for all households. — **5** Annual averages. — **p** Columns 1 to 3 provisional.

In 1983, the Bundesbank again endeavoured to buttress the cyclical recovery by its policies without endangering the stabilisation of prices. In the first few months of the year, the Bundesbank's interest rate and liquidity policy aided the fall in interest rates which had got under way. This policy was all the more defensible as the Deutsche Mark initially remained strong on the foreign exchange markets. As the year went on, however, both a pace of monetary expansion that overshot the target and the weakening of the Deutsche Mark on the foreign exchange markets signalled that this relatively easy monetary policy stance might in fact have posed dangers to stability in the longer run. As a result of carefully regulated liquidity and interest rate policy adjustments — including, in particular, the raising of the lombard rate from 5% to 5½% in September — together with other factors, e.g. major outflows of funds at times, the growth in the money stock moderated up to the end of the year. The monetary target for 1983 — an increase of 4 to 7% in the central bank money stock from the fourth quarter of 1982 to the fourth quarter of 1983 — was indeed utilised to the full, but it was not exceeded. By setting a monetary target for 1984 which envisages a growth in the central bank money stock of 4 to 6%, the Bundesbank underlined its intention of safeguarding the progress made towards stability and at the same time providing monetary conditions permitting satisfactory economic growth.

However, there are still some risks with respect to global economic influences. Last year, Germany's economy was put under strain by occasional marked fluctuations in the Deutsche Mark, and the temporary overvaluation of the U.S. dollar on the foreign exchange markets made price stabilisation at home more difficult. Moreover, it must not be forgotten that the resulting short-term stimuli for exports may turn out to be problematic in the long run. In actual fact, the factors determining exchange rate levels, particularly those affecting the relation between the Deutsche Mark and the U.S. dollar, are unclear, and to a large extent they cannot be influenced by Germany. A further risk factor, which will be described in more detail in the second part of this Report, consists in the overindebtedness of several major developing countries. However, the teamwork in international debt management between the International Monetary Fund, the banking system and central banks gives grounds for hoping that possible cases of conflict can be limited and eventually solved, provided that debtor countries pursue a policy of reestablishing their creditworthiness.

1. Upturn in economic activity

Cyclical recovery after an improvement in underlying conditions and profitability

In 1983, after almost three years of slowdown, expansionary forces gathered pace again in the Federal Republic of Germany. The economic recovery started at the beginning of the year and increased in breadth and intensity as the year went on. The pattern of the recovery differed from that of earlier upswings in that the first positive impulses came not from foreign demand but from the home market. A major factor was that, as fiscal policy kept strictly to the consolidation of the public budgets, expectations strengthened that this would give more scope for private enterprise, while basic monetary conditions improved too. A further stimulus came from government measures to encourage investment in trade and industry and promote housing construction. However, the decisive factor was the marked improvement in the profitability of private enterprises, which had been precarious for years and was partly responsible for the economic setback of preceding years. The gross income of producing enterprises (excluding the housing sector and financial institutions), which is a good indicator of the development of earnings from current business, rose by around 14% in 1983, i.e. very much more than in the preceding year (+7%). However, this must be seen in conjunction with the previous decline in earnings in 1980–81: even after the improvement in 1983 the share of the gross income of producing enterprises in national income, at a good 21½%, was still some 1½ percentage points lower than in 1979, and very much below the level of the beginning of the seventies (over 25%).

Return on fixed assets higher than in earlier years

Nevertheless, the better earnings situation meant that the capital tied up in producing enterprises was yielding a rather better return, with prospects of a further improvement. This is an essential precondition for more capital being spent on fixed assets, thereby creating new jobs. Relative to the fixed assets in producing enterprises (excluding housing, farms and financial institutions), and after deduction of the estimated "entrepreneurs' remuneration" for proprietors' work in firms not organised in the form of an incorporated enterprise, the gross income of enterprises rose to almost 10%, while the figure for the two previous years had been just over 8%. Even though these estimates need to be treated with caution and the changes in the return on capital are a better indicator than its absolute level, the improvement does suggest that the return on fixed assets in the enterprise sector may be coming back to a level which offers a reward for the much higher risk which investment of this kind inevitably entails in comparison with investment in securities; however, present estimates show that this reward is still very much lower than it was in the seventies or sixties.

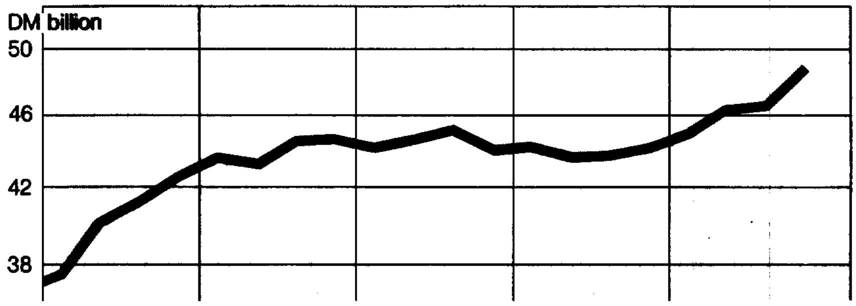
Improvement in earnings mainly due to relief on the cost side

A particularly important factor, especially in view of the desirability of making the upswing durable, is that the improvement in entrepreneurial earnings came mainly from a slowdown in the growth of costs, and not from an acceleration in price rises, which would undoubtedly have contained the seeds of another economic reversal. While there was a further sharp expansion in depreciation and indirect taxes in 1983 — the latter in connection with the increase in value-added tax towards the middle of the year — imports placed hardly any additional burden on enterprises' cost accounts, taking the year as a whole. Prices for goods from abroad dropped until well into the spring of 1983 as the Deutsche Mark at first tended to appreciate against the currencies of major trading partners, but as the year went on the resultant cost advantages were lost again since the Deutsche Mark/dollar rate greatly deteriorated. Another important factor easing the pressure on enterprises' cost accounts was that expenditure on wages and salaries, including social security contributions, rose only slightly

Capital formation and income of enterprises*

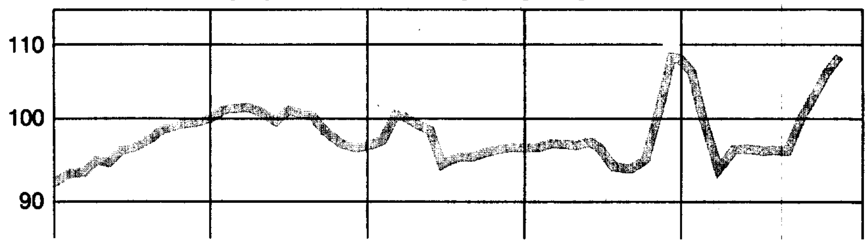
Gross fixed capital formation
at current prices

quarterly, seasonally adjusted; log. scale



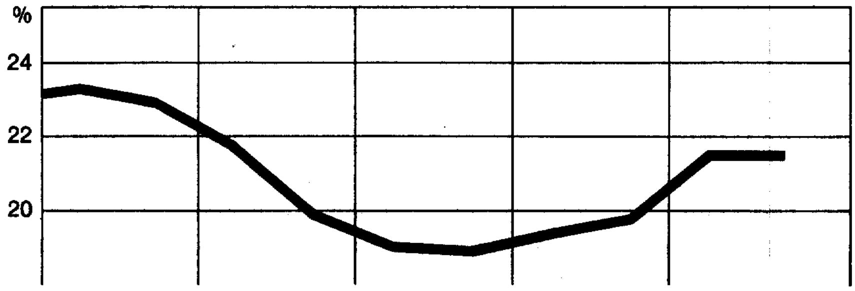
Memorandum item
Domestic orders received
by the capital goods sector (excluding vehicle building), value

1980=100, seasonally adjusted, 4-month moving averages, log. scale



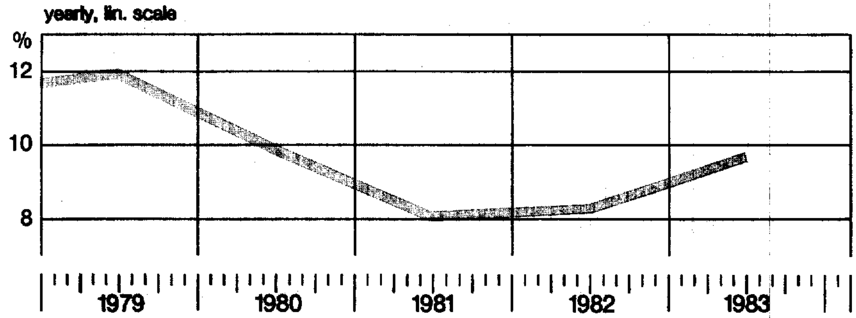
Gross income 1) of producing enterprises
as a percentage of national income

half-yearly, seasonally adjusted, lin. scale



Return on fixed assets 2)

yearly, lin. scale



* Excluding letting of dwellings and excluding financial institutions.- ° Affected by the deadline for claiming the investment grant and by large-scale orders.- 1) Domestically generated entrepreneurial and property income of enterprises less net interest paid to other sectors, net rents, etc.- 2) Gross income of enterprises (less imputed entrepreneurs' remuneration) relative to net fixed assets at replacement prices; estimated by the Bundesbank.

in 1983, viz. by 1½ % (after 2 % in 1982 and 4½ % in 1981). Firstly, collectively agreed wage and salary increases in 1983, at an average of 3 %, were kept distinctly (around 1 percentage point) below the level of the previous year; secondly, the number of wage and salary earners continued to decrease until the autumn of 1983. On average over the year, it was about 2 % lower than in the previous year. Total expenditure on imports, personnel, indirect taxes and depreciation increased by around 2 % in 1983; this was markedly less than in the previous years (1982: 3 %, 1981: 7 %) and also less than turnover at home and abroad, which went up by 3½ % last year. Financing costs in 1983 were also less of a burden on enterprises than in 1982, even if the decline in interest rates on the credit markets, as discussed in more detail below (p. 45), did not continue throughout 1983.

Number of insolvencies drops over the course of the year

The generally more favourable trend of enterprises' earnings from current business should not, however, obscure the fact that there are still considerable differences in profitability. In particular, quite a number of firms still seem to be suffering from the belated consequences of the preceding recession and the resultant loss of assets. Moreover, the number of corporate insolvencies in 1983, at 11,850, was not very much lower than in 1982; however, as the year went on, the number of bankruptcies began to fall off somewhat. Insolvencies cause losses not only for the banks (see p. 44), but also for the other enterprises which are the subject of this analysis.

Noticeable improvement in the investment climate

The investment climate in the Federal Republic of Germany improved noticeably in 1983. An initial major stimulus here was imparted by the investment grant scheme approved in spring 1982. Many firms made use of it and extensive orders were placed for machinery and equipment before the deadline of December 31, 1982. Then the demand for capital goods stabilised at a higher level than before this spate of orders, and gathered pace distinctly over the rest of the year, not least because of the evident improvement in earnings prospects. From December 1982 to November 1983 (it is better to take this period on account of the large number of orders placed at the end of 1982 in response to the investment grant) the domestic orders received by the capital goods industry (excluding vehicle construction) were around 5 % higher than in the preceding twelve-month period, after showing a decline in the previous two years. In the first few months of 1984 demand for machinery and equipment increased further, seasonally adjusted.

Marked increase in fixed capital formation

Expenditure on machinery and equipment rose markedly during 1983, particularly in the second quarter and at the end of the year (a factor here was that goods on which the investment grant was to be claimed had to be delivered by the end of 1983). Industrial construction investment also rose over the course of last year, suggesting a greater propensity to invest in capacity expansion, which generally involves greater construction activity. In the final analysis total gross fixed capital formation by enterprises went up by 6½ % in 1983 over the previous year, when it had declined. The main investors in this field in the manufacturing sector were the producers of capital and consumer goods, but the construction industry and electricity- and gas-producing enterprises also invested very much more in 1983 than in 1982. In the basic and producer goods industries — for instance, in the steel and oil industries — capital expenditure was well below the previous year's figure.

Strong rise in stocks

A considerable stimulus was given to economic activity last year by stockbuilding, too. The progressive upturn in production and improving sales prospects at home and abroad caused enterprises to increase their stocks of primary materials to a greater extent than in the previous year. A further indicator of this is that imports of semi-manufactures and primary products rose noticeably in the course of 1983; in the fourth quarter they were 13% above the comparable figure for the previous year in volume, far more than consistent with the increase in production and sales. In addition, trade and industry built up their stocks of finished products considerably, to be able to cope with the growth in demand. In the economy as a whole, stocks increased by just on DM 19 billion in 1983, according to calculations by the Federal Statistical Office; this was nearly three times as much as a year before.

Although households have little scope for extra expenditure ...

While enterprises' improving operating results in 1983 encouraged investment, and steered the expenditure of GNP more in the direction needed for future growth and employment, there was relatively little scope in households' income for additional private consumer expenditure last year. At any rate, in 1983 households had only slightly (½%) more wage and salary income at their disposal than a year before after deduction of the wage tax withheld by employers and social security contributions (the actual amount of income tax paid on total wages and salaries is, however, not known because many employees receive tax rebates or have to make additional payments following the tax assessment procedure). There was only a comparatively slight rise in the income paid by the public authorities in the form of pensions and assistance payments last year, at 2½% as compared with 5% in 1982; in addition to savings on children's benefits and on assistance for vocational training, the postponement of the pension adjustment until July 1, 1983 was a significant factor here. The income of all households from their financial assets — which, at an estimated DM 85.5 billion, accounted for around 8% of total disposable income in 1983 — was about 6% below the previous year's level as interest rates declined. Including self-employed persons' withdrawals from entrepreneurial income for private purposes, households may be taken to have had about 2½% more income in 1983 than in 1982.

... there is a relatively powerful rise in private consumption

However, households spent more on consumption in 1983, namely about 4% more over the year as a whole. In real terms this was an increase of 1%, after a decline for the previous two years. In the first few months of the year especially, when the economic recovery was just starting, there was a powerful rise in private consumer demand. As the year went on, however, its role as pacemaker in the upswing passed to other components of demand. In 1983, taken as a whole, perceptibly more was spent on consumer durables than a year before. Accumulated demand and attractive prices sent orders for passenger cars shooting up. Furniture and other household items were also more in demand, as were technical innovations, e.g. in the field of consumer electronics and home computers. Consumers tended to be more cautious in purchasing goods for everyday use and services. Their expenditure on holidays abroad, for instance, was lower in 1983 than in 1982. Over the first few months of 1984 private consumer demand appears to have risen rather more strongly.

Revival in private consumer demand partially at the expense of saving

The expansion in private consumption in 1983 was very largely at the expense of private saving. Total saving by households in 1983 was 6½% below the 1982 figure; it was equivalent to 13% of disposable income last year, as compared with around 14% in 1982 and 15% in 1981. The slowdown in saving owed something not only to the more optimistic assessment of the economic outlook, which apparently caused many people to feel that such high risk provision as in the last few years was no longer necessary, but also to the fact that the blocking period for considerable amounts — altogether DM 22.5 billion — of bonus-carrying savings deposits ended in 1983. Quite a large percentage of these funds was not reinvested but used for consumption purposes. In the first part of the year in particular this would appear to have contributed to the rise in the demand for consumer durables mentioned above.

Key economic variables in the Federal Republic of Germany

Item	Unit	1980	1981	1982	1983	1980	1981	1982	1983
						Percentage change from previous year			
Aggregate demand									
Private consumption	DM billion	834.0	873.2	899.4	935.1	+ 7.0	+ 4.7	+ 3.0	+ 4.0
Public consumption	DM billion	297.9	317.8	325.3	333.5	+ 8.9	+ 6.7	+ 2.4	+ 2.5
Fixed capital formation	DM billion	338.0	338.2	329.1	344.4	+ 10.9	+ 0.1	− 2.7	+ 4.6
Machinery and equipment	DM billion	127.9	128.7	125.2	135.4	+ 6.9	+ 0.6	− 2.7	+ 8.1
Construction	DM billion	210.1	209.6	203.9	209.0	+ 13.5	− 0.3	− 2.7	+ 2.5
Increase in stocks	DM billion	18.9	1.2	6.6	18.7	.	.	.	.
Domestic expenditure	DM billion	1,488.8	1,530.5	1,560.5	1,631.7	+ 7.6	+ 2.8	+ 2.0	+ 4.6
External surplus **1**	DM billion	− 3.1	+ 13.2	+ 38.4	+ 39.6	.	.	.	.
Exports	DM billion	430.6	495.9	535.9	538.6	+ 12.4	+ 15.2	+ 8.1	+ 0.5
Imports	DM billion	433.7	482.6	497.5	499.1	+ 16.6	+ 11.3	+ 3.1	+ 0.3
Gross national product at current prices	DM billion	1,485.7	1,543.7	1,598.9	1,671.2	+ 6.5	+ 3.9	+ 3.6	+ 4.5
Memorandum items									
Orders received by the manufacturing sector	1980 = 100	100.0	104.5	103.4	107.9	+ 3.9	+ 4.5	− 1.0	+ 4.4
Domestic orders	1980 = 100	100.0	98.8	98.3	103.1	+ 3.0	− 1.2	− 0.5	+ 4.9
Foreign orders	1980 = 100	100.0	116.7	114.4	118.3	+ 5.8	+ 16.7	− 1.9	+ 3.4
Orders received by the construction industry	1980 = 100	100.0	85.3	85.9	94.4	+ 2.7	− 14.7	+ 0.6	+ 10.0
Distribution of income									
Wage and salary income	DM billion	842.1	881.3	900.2	915.3	+ 8.4	+ 4.7	+ 2.1	+ 1.7
do. as a percentage of national income	%	73.3	74.3	73.4	71.6	.	.	.	.
Entrepreneurial and property income	DM billion	307.3	304.9	325.7	362.2	− 0.9	− 0.8	+ 6.8	+ 11.2
Memorandum items									
Gross income of producing enterprises	DM billion	240.0	225.5	241.4	275.7	− 4.8	− 6.1	+ 7.1	+ 14.2
do. as a percentage of national income	%	20.9	19.0	19.7	21.6	.	.	.	.
National income	DM billion	1,149.4	1,186.2	1,225.9	1,277.5	+ 5.7	+ 3.2	+ 3.3	+ 4.2
Production									
Gross national product at 1976 prices	DM billion	1,265.5	1,262.0	1,247.5	1,263.2	+ 1.9	− 0.3	− 1.1	+ 1.3
Productivity **2**	1976 = 100	113.3	115.1	116.3	120.2	+ 1.8	+ 1.6	+ 1.0	+ 3.4
Output in the producing sector (excluding construction) **3**	1980 = 100	100.0	98.3	95.5	96.4	+ 0.3	− 1.7	− 2.8	+ 0.9
Construction output **3**	1980 = 100	100.0	92.5	88.5	86.5	− 2.0	− 7.5	− 4.4	− 2.2
Employment									
Employed persons	Millions	26.3	26.1	25.6	25.2	+ 1.0	− 0.8	− 1.8	− 1.7
Wage and salary earners	Millions	23.0	22.8	22.4	22.0	+ 1.4	− 0.6	− 2.0	− 1.9
Memorandum item									
Total number of man-hours worked	1976 = 100	99.4	97.6	95.5	93.6	+ 0.2	− 1.8	− 2.1	− 2.1
Unemployed persons	Thousands	889	1,272	1,833	2,258	+ 1,5	+ 43.1	+ 44.2	+ 23.2
do. as a percentage of									
the total labour force	%	3.3	4.8	6.7	8.1	.	.	.	.
the dependent labour force	%	3.8	5.5	7.5	9.1	.	.	.	.
Prices									
GNP deflator	1976 = 100	117.4	122.3	128.2	132.3	+ 4.5	+ 4.2	+ 4.8	+ 3.2
Memorandum item									
Unit labour costs in the economy as a whole **4**	1976 = 100	116.1	121.7	126.0	126.7	+ 5.9	+ 4.8	+ 3.5	+ 0.6
Cost of living index for all households	1976 = 100	117.0	123.9	130.5	134.4	+ 5.5	+ 5.9	+ 5.3	+ 3.0
Producer prices of industrial products	1980 = 100	100.0	107.8	114.1	115.8	+ 7.5	+ 7.8	+ 5.8	+ 1.5
Overall construction price level	1980 = 100	100.0	105.3	108.1	109.9	+ 10.9	+ 5.3	+ 2.7	+ 1.7
Index of import prices	1980 = 100	100.0	113.6	116.2	115.8	+ 15.0	+ 13.6	+ 2.3	− 0.3

1 Balance of transactions in goods and services with other countries (including GDR). — **2** Gross national product at 1976 prices per man-hour worked; calculated by the Bundesbank. — **3** Results for kind of activity units. — **4** Index of gross wages and salaries per employee divided by index of real GNP per employed person. —

The figures from the national accounts from 1981 onwards are provisional.

Longer-term assets gain ground in the context of private acquisition of financial assets

In the context of the acquisition of financial assets, private savers concentrated more on longer-term assets last year. Favourites here were fixed interest securities, especially public bonds, together with longer-term investments in time deposits and bank savings bonds. The strong inflow of private savings to insurance enterprises also continued, while the inflow of funds to the building and loan associations last year did not regain the 1982 level. The net inflow to savings accounts with banks was also relatively low in 1983, lying one-sixth below the previous year's figure. Total new saving in 1983 was likewise depressed by the fact that households were more inclined to borrow in order to buy consumer goods as interest rates on loans were rather lower.

Strong increase in demand for housing

Demand for new housing gave a powerful boost to the economic recovery in the first few months of 1983. The decision to go ahead with building projects was facilitated by the approval of new government promotional measures towards the end of 1982. People having a house built were able to offset more of the interest against tax while a special programme, "Interim Finance for Loans for Building Purposes", offered further assistance. Considerable funds were also made available by the Federal and Länder Governments in 1983 for publicly-assisted housing construction; moreover, loans for housing purposes were available on better terms than in 1982 (although interest rates on mortgage loans rose again slightly as the year went on). In addition, the rise in building prices was quite low in comparison with earlier recovery phases, despite the heavier demand evident in housing since the beginning of 1982. Towards the end of 1982 and in the first few months of 1983 there was a leap in demand for housing, but even after the spate of orders in the first few months of the year demand remained at a high level. Over the year as a whole the construction industry received about one-fifth more orders for new residential buildings than in 1982, both by value and by volume. Orders for new projects were far in excess of the number of projects completed during the same period; altogether, around 341,000 housing units were completed in 1983, just on 2% fewer than in 1982, but at the end of the year construction firms had far more orders in hand (about 16% more by volume) than at the end of 1982. This suggests that the level of housing construction will remain relatively high during the 1984 building season as well.

High level of housing provision

Over the medium term, however, housing construction cannot be expected to go on rising, firstly because the provision of housing in the Federal Republic of Germany has already reached a fairly high level in both quality and quantity. As the resident population is declining, such provision would therefore continue to improve even if construction stayed at its present level or dropped slightly. In some areas the supply of housing is already in excess of demand and the number of apartments standing empty for a time is increasing, and although further steps have been taken to liberalise rent legislation, rents have not really risen more than formerly. Even new apartments built with government assistance cannot always be let at the rents fixed, which contain an element of subsidy since the interest burden on public loans is low, and there are other forms of governmental assistance. Secondly, as confidence in monetary stability returns, the motive for the "flight into fixed assets" will disappear, and that will not only affect new construction activity but also ease the pressure on the real estate market generally. Certainly prices are falling in many areas, especially outside the conurbations, for single-family homes and owner-occupied apartments.

Reorientation in housing policy

The changes in conditions on the housing market justify considering a reorientation in housing policy. So far as is apparent at present, a cutback in traditional government-assisted housing construction is likely, especially since the cost of assistance has now reached an average of some DM 80,000 per unit (for the initial phase). New tax approaches to housing assistance are also being discussed. These issues need clarifying, not least because the possibility of deducting interest on borrowed funds introduced at the end of 1982 — and limited to DM 10,000 — only applies to new owner-occupied homes finished or purchased before January 1, 1987. But granting permanent interest deduction would not be compatible with the previous tax practice of fixing a very low rented value for owner-occupied homes. As on earlier occasions, Parliament here is ultimately faced with the need to weigh the interest that economic policy has in personal asset formation against the disadvantages that may result from continuing to direct a not inconsiderable part of the limited supply of capital in the economy into housing construction, which ties up capital for longer periods of time, thus competing with those areas of the economy where investment in fixed assets can strengthen competitiveness and durably safeguard employment.

Public orders for construction work remain at a low level

Public sector demand for construction work was very low in 1983; over the year as a whole orders for public construction projects barely reached the low level of the previous year. In view of the need to consolidate the public budgets, the Federal and Länder Governments and the local authorities exercised considerable restraint, and at the turn of 1983–84 public construction demand did not pick up, even though the financial situation of the local authorities improved noticeably (for more details see p. 18).

Powerful expansion of foreign demand in the second half of the year

In the economic recovery in 1983 foreign demand did not play the pace-setting role that it had generally played in earlier upswings, remaining at a relatively low level during the first half of the year. After that, however, it picked up markedly and made a major contribution to the upturn in domestic economic activity. Over the year as a whole the manufacturing sector received only 3½ % more orders from abroad than in 1982, but in the fourth quarter of 1983 the inflow of new export orders was 16 % above the previous year's level. In the first two months of 1984 the gap over 1983 grew further, to 21 %. The expansion in foreign demand affected practically all the main areas of the manufacturing sector. It was particularly strong in the basic and producer goods sector, and taking the average of January/February 1984 foreign orders in the chemical industry were 25 % higher than a year before. In the steel industry new export orders have latterly been even further above the — admittedly extremely low — level of the preceding year, and if this trend continued it would help the steel works to some extent to cope with their acute problems. The structural difficulties in this area are by no means overcome. In the most important capital goods sectors, export orders in February showed a year-on-year rise of a good fifth.

Exporters profit from the cyclical recovery abroad

When their foreign business began to pick up as from mid-1983, German exporters started to participate, with a certain time-lag, in the international cyclical upswing which had commenced in the United States and Japan towards the end of 1982 and spread to some western European countries during 1983. In addition, the price competitiveness of German suppliers improved in the course of 1983 as the rate for the U.S. dollar rose against the Deutsche Mark. How precarious such advantages based on exchange rate movements are, however, was shown by the recent reversal of this trend, which had the U.S. dollar losing 7 % of its value against the Deutsche Mark from the end of January. It would therefore appear to be of much greater importance that German suppliers, as described in more detail below (p. 51), are holding their own on foreign markets independent of these more temporary influences. However, the present competitive position cannot be regarded as secure over the longer term, and unremitting efforts will be needed to strengthen enterprises' capacity to invest so that they can keep up with technological progress, for, failing this, they will not be able to stand up to international competition in the long run. In view of Germany's high degree of integration in the world economy — exports of goods and services make up roughly 30 % of domestic production — any loss of international competitiveness, which depends not only on prices but also on the technological standard of exporters, would worsen the structural difficulties at home and especially the employment problem.

Shift in the use of goods in favour of investment

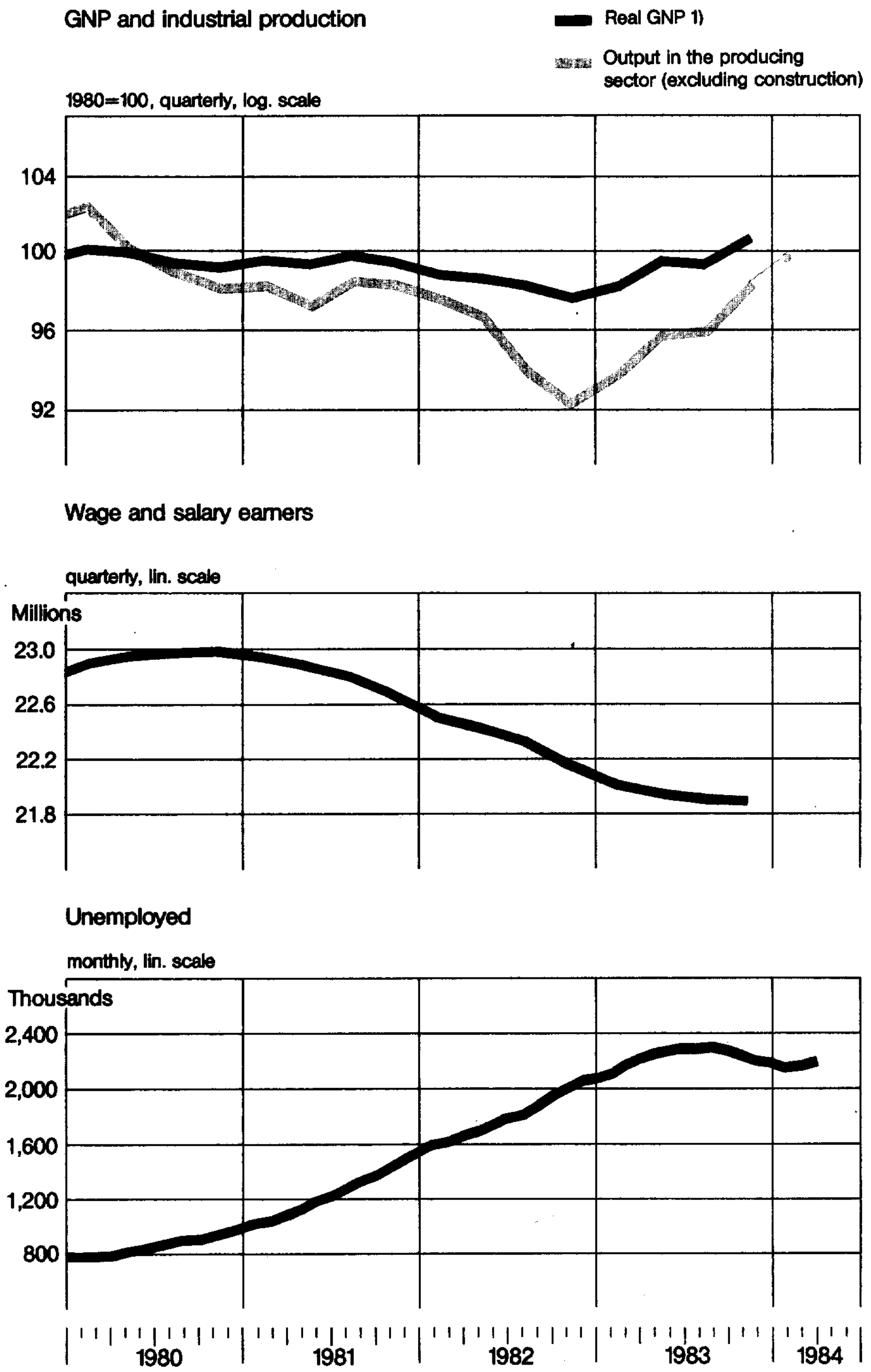
These demand trends brought a shift in the relative use of goods in the economy as a whole during 1983 in favour of investment and to the detriment of consumer spending. Of the total growth in the nominal gross national product last year (a good DM 72 billion) almost DM 27.5 billion (or 38 %) was spent on new assets and stocks, fully DM 23 billion (or 31.5 %) of this alone by producing enterprises (i. e. enterprises excluding housing and financial institutions). In 1982, on the other hand, rising consumption expenditure and a higher external surplus absorbed practically the whole increase in the national product. On a longer-term comparison, the overall investment ratio was admittedly still very low in 1983. At 21½ % of GNP, it remained on average over the year distinctly below the level of 1980 (24 %), i. e. before the economy was affected by the cyclical setback. In the early seventies, prior to the first oil price shock, around 27 % of total GNP had been spent on investment. In 1983 some 56 % of total nominal GNP was devoted to consumption by households and about 20 % to public consumption, altogether rather less than a year before. The shift in the overall use of goods, of which there were initial signs in 1983, was therefore in the right direction; but the level of investment is still not high enough to lastingly safeguard enterprises' competitive position and thus secure jobs over the longer term.

Increase in overall production...

Production in the economy as a whole reacted relatively quickly to the improvement in the economic climate. The real gross national product left the cyclical trough at the turn of 1982–83 and rose strongly in the course of last year. In the fourth quarter it was over 3 % higher than a year before (after adjustment for working-day variations). This represented an increase of nearly 1½ % in the national product over the year as a whole, more than had generally been expected at the beginning of the year. Over the entire year, economic growth in 1983 probably lagged slightly behind the increase in overall production potential over the same period (rather more than 1½ %), and it may therefore be taken that the utilisation of production capacity throughout the economy did not rise, at least on average for the year; there was, however, a corresponding change in the trend during the year. In the manufacturing sector, taken by itself, the degree of utilisation of plant and equipment rose sharply as 1983 went on. According to surveys by the Ifo Institute, which are admittedly based on appraisals by enterprises, utilisation of plant capacity reached 80½ % of the standard level in December 1983 (seasonally adjusted), against just on 75½ % at the end of 1982. At the peak of the previous cycle, at the turn of 1979–80, the degree of utilisation reported by enterprises had, however, been 85½ %.

... with considerable differences between the sectors

The various economic sectors made very different contributions to the growth of the gross domestic product in 1983. In the producing sector (excluding construction) taken as a whole, output was about 1 % higher in 1983 than in 1982, when production had dropped by 3 %. The growth differential between the various industries was greater than ever last year, largely as a result of the still unsolved structural problems in the economy. While healthy industries were quick to participate in the recovery process, other industries which have had excess capacity for years, the reduction of which has been stopped or at least braked with the aid of subsidies, fell further behind. Among the front-runners in the growth of production were the producers of office machines and EDP equipment, with a rise of 15½ % in output in 1983. Their products were very much in line with the trend towards high-technology machinery and equipment, which the business community is increasingly using in order to maintain its competitiveness. Some other areas of the capital goods sector also stepped up production appreciably over the course of the year, but only achieved a modest seasonally adjusted



1) Rebased from the price base 1976=100; adjusted additionally for working-day variations.- •=January/February.

growth on average during the year (e.g. road vehicle building and electrical engineering). In the basic goods sector there was a particularly strong rise (of 7½ %) in production in the chemical industry, whereas the steel industry and petroleum processing failed to regain their 1982 levels, even though their output went up markedly in the second half of last year. Coal mining and the shipyards had to cut down their production considerably, coal mining by almost 10 % and the shipyards by around 17 %. The total value added in the construction industry in 1983 was no higher than in 1982, despite the increase in demand; however, the trend in the finishing trades was significantly better than that in civil engineering and building.

Disproportionate increase in the tertiary sector

The long-term trend towards a disproportionately rapid expansion of the tertiary sector of the economy continued last year. In some service areas, especially banking and insurance, the value added in 1983 was distinctly larger than in the economy as a whole. The value added in the transport sector, however, was noticeably lower than in 1982, no doubt largely because of the structural shift away from "heavy" material-intensive products to "lighter" high-technology goods that need less transport space. Production in agriculture and forestry also dropped, mainly owing to relatively low harvests.

Noticeable differential between south and north in the recovery process

Some of the sectors that are adversely affected by the structural changes are concentrated in the North of Germany (North-Rhine Westphalia, Schleswig-Holstein, Lower Saxony, Hamburg and Bremen), and this is presumably the reason why the value added in this area was less favourable in 1983 — as also in earlier years — than in Southern Germany (Hesse, Rhineland-Palatinate, Bavaria and Baden-Württemberg),[1] where many of the industries that are profiting from the structural changes are mainly located. The same differences are apparent on the labour market.

Lagged reaction of the labour market to the upturn in production

As usual, the recovery in Germany was reflected on the labour market only after a certain time-lag. Firstly, especially in the manufacturing sector, many firms which had introduced short-time working were able to mobilise considerable reserves of labour to step up their production by going back on to full-time work. At the beginning of 1983 the employment exchanges had 1.2 million employees registered as being on short time, by the beginning of 1984 the figure had dropped to half that level and in March 1984 it was 618,000. Considering that, on average, about one-third fewer working hours than usual are worked by employees on short time, the return to normal working hours had a purely arithmetical employment effect of about 200,000 persons. Secondly, further jobs were lost in sectors suffering from structural changes, especially in the North of Germany. Outside the manufacturing sector the loss of jobs continued in distribution and transportation, but the construction industry — given the upturn in construction activity — and the services sector, which has been increasing the number of jobs on offer for some time, took on more employees in the course of the year. Altogether, the total labour force in the economy as a whole first dropped further in 1983; not until the last few months of the year did it virtually stabilise, seasonally adjusted. On average over 1983 the number of employees fell by 430,000 or around 2 %, but the gap compared with the previous year narrowed noticeably as the year went on.

Easier situation on the labour market for demographic reasons

The situation on the labour market was eased to some extent in 1983 as, owing to demographic factors, the inflow to the market was smaller than in earlier years. The number of persons starting work and looking for a company traineeship, however, rose again last year. Just on 680,000 training contracts were concluded, around 46,000 more than in the previous training year. On the other hand, a large number of persons reached retirement age last year or took advantage of special arrangements to retire at 59. A further positive factor was that, as in the previous year, some foreign workers decided to return home. The number of foreigners residing in the Federal Republic of Germany declined slightly, for the first time for quite a long while.

Peak of unemployment passed in the summer of 1983

The average number of unemployed persons in 1983, at 2.26 million, was again higher — by 425,000 — than in the previous year. The unemployment ratio was 8.1 % of the total labour force (in line with international statistical practice) or 9.1 % of the dependent labour force (as it is usually calculated in the Federal Republic of Germany, although the unemployment figure also includes persons who were formerly self-employed). In August 1983 the number of unemployed

1 Saarland and Berlin have been disregarded here because of their special structure and geographical position.

Conditions on the labour market

Thousands; averages

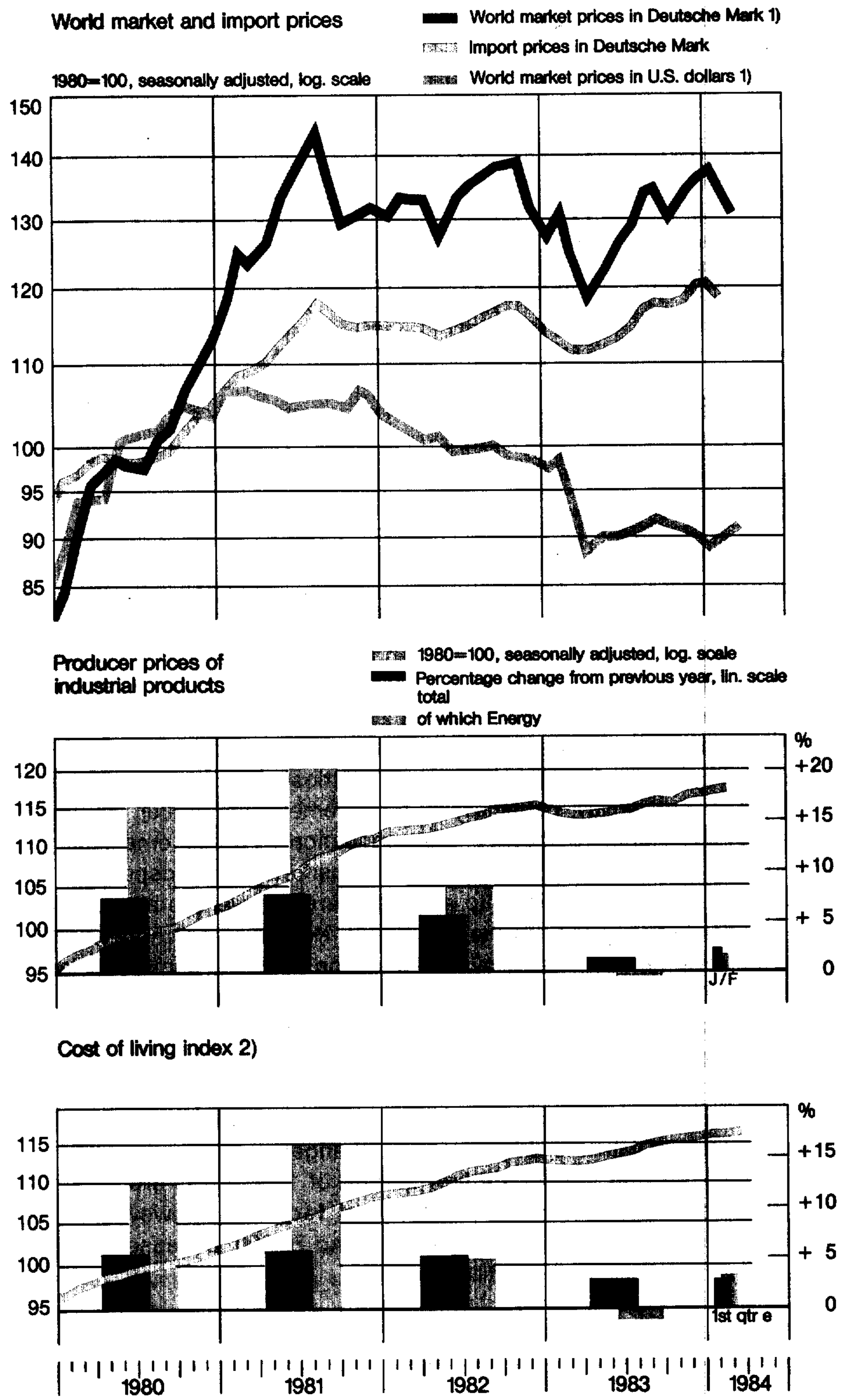
Item	1982	1983 Total	1983 1st half	1983 2nd half	Change from previous year Total	Change from previous year 1st half	Change from previous year 2nd half
Wage and salary earners	22,395	21,962	21,882	22,042	−433	−514	−352
Short-time workers	606	675	877	473	+ 69	+368	−231
Inflow of vacancies 1	1,124	1,247	627	620	+123	− 2	+124
Number of vacancies	105	76	75	76	− 29	− 51	− 8
Placements through employment exchanges 1	1,395	1,557	741	816	+162	+ 13	+150
Unemployed	1,833	2,258	2,331	2,185	+425	+543	+307
Men	1,021	1,273	1,357	1,189	+252	+340	+164
Women	812	985	974	996	+173	+203	+143
Memo items							
Unemployed young people (under 20)	165	192	192	193	+ 27	+ 43	+ 12
Those looking for part-time work	238	246	250	242	+ 8	+ 8	+ 7
Unemployed foreigners	246	292	304	280	+ 46	+ 62	+ 31

1 Total number in the period covered.

passed its cyclical peak. It had dropped by about 100,000 by February 1984. While this trend did not continue in March, there are reasons for thinking that there has been no change in the basic trend towards a gradual improvement on the labour market. At the end of March 1984 the number of unemployed registered at the employment exchanges was 2.24 million on a seasonally adjusted basis; this amounts to 9% of the dependent and 8% of the total labour force. High unemployment remains a challenge to all those concerned with economic and labour market policy, especially to management and labour. Section 5 of this part of the Report discusses the connection between employment and German economic competitiveness on world markets. The prospects of bringing unemployment down quickly to a more bearable level are admittedly slim; this will certainly not happen in the short term. Nevertheless, there has been a gradual improvement in the employment situation since the summer of last year and this is reflected not only in the above-mentioned change in the trend of unemployment but also in a distinct increase in placements by the Federal Labour Office. Around 1.56 million persons looking for work, 11½% more than in the previous year, were placed in jobs by the employment exchanges in 1983. Nearly two-thirds of them obtained longer-term employment. The number of vacancies registered with the employment exchanges also rose noticeably over the course of the year, and in the first quarter of 1984 it was around one-fifth above the previous year's level. The stock of vacancies, however, remained very low in 1983, at an annual average of around 76,000, because the new vacancies reported were as a rule filled quickly.

Price climate more relaxed despite rise in demand for goods

The price situation in the Federal Republic of Germany in 1983 was relaxed on the whole although the aggregate demand for goods increased strongly, as outlined above. On the one hand, competition evidently remained fierce on sales markets and this clearly helped to keep price rises small; on the other, enterprises found it easier than before to absorb fluctuations on the cost side as their profit margins had widened. The noticeable drop in import prices during the early months of the year due to the rise in the external value of the Deutsche Mark helped to keep domestic price movements down. The oil-exporting countries also lowered their prices for crude oil noticeably under the continued influence of the plentiful supply. As the year went on, however, external trends again began to push up prices at home; the prime influence here was a marked decline from the spring onwards in the value of the Deutsche



1) Index of Hamburgisches Weltwirtschaftsarchiv; rebased from original base 1975=100.- 2) Rebased from original base 1976=100.- e Estimated.

Mark against the U.S. dollar, the currency used for invoicing on the international energy markets and also for many raw materials. Later, however, as set forth in more detail below (see p. 26), this trend was reversed. Some suppliers of raw materials seem to have reacted to the rise in the U.S. dollar against the Deutsche Mark and the currencies of other major industrial countries by lowering their dollar prices, as the real purchasing power of their foreign-business receipts increased considerably as a result of the rise in the rate. Nevertheless, there was a substantial rise in the prices of goods imported into Germany as from the spring of 1983 and the earlier drop in these prices, which was also partly due to exchange rate movements, was largely offset. On average over 1983 import prices remained slightly below the previous year's level, but in the first two months of 1984 they rose on average a good 5½ % above the comparable 1983 figure.

Sluggish increase in industrial producer prices

Price stimuli from abroad have so far worked through to the domestic market only with a time-lag and to varying degrees. At the industrial producer level many firms were obviously hoping to improve their earnings not by raising prices but by cutting costs and increasing sales. Altogether, industrial producer prices remained stable, seasonally adjusted, during the first half of the year; in the second half they began to go up, particularly in the basic goods sector, where higher prices for imports always have an especially strong effect. There was not so steep a rise in prices for capital and consumer goods, even in the second half of 1983. Over the year as a whole industrial producer prices were only 1½ % higher than a year earlier (when they rose by almost 6 %). In February 1984 the gap compared with the preceding year was rather wider, at 2½ %. Finished products from the capital goods sector were almost 3 % dearer during this period than a year before. In the construction industry only moderate price increases were at first possible. On average the overall construction price level in 1983 was 1.7 % higher than in the previous year, but towards the end of 1983 it was 3 % higher than a year before.

Markedly lower price rises at the consumer level

At the consumer level the average rate of price rises dropped to 3 % in 1983, after 5.3 % and 5.9 % in 1982 and 1981. A contributory factor here was that energy (electricity, gas, petroleum products and coal), taken as a whole, was cheaper in 1983 than in 1982, while foodstuffs grew only slightly dearer. In the first half of 1983 fruit and vegetables were very reasonably priced after good crops, while an ample supply of animal products in the second half of the year helped to keep prices down and partly compensated for the renewed rise in prices for vegetable products when the new crops turned out poor. The rise in prices for manufactured goods (excluding energy) dropped to 3 % on average in 1983, after 5½ % in 1982. Competition here on domestic markets was so strong, even though demand had picked up, that the increase in value-added tax in the middle of the year could not, in many cases, be passed on directly to consumers. There was an above-average rise in payments for services and in rents in 1983; in the first few months of the year, in particular, rents for old property and subsidised housing rose fairly strongly; as the year went on, however, this trend slackened noticeably. Rents for privately financed housing were not increased as much as in 1982. The fear that is often heard in connection with the amendment of rent legislation that this might cause rents to go up in the long run has thus turned out to be baseless. In the first few months of 1984 seasonally adjusted consumer prices rose only slightly; while the year-on-year growth rate had narrowed to around 2½ % in the autumn of 1983, it had widened again to around 3 % by March this year. The decisive factor here, nevertheless, was that consumer prices in the same period of 1982 had been falling.

2. Progress in the consolidation of public budgets

Policy of consolidation successfully continued

The economic recovery and its vigour are to a certain extent to be regarded as a success of the fiscal policy strategy. In conformity with the policy stance which had been adopted a year previously, the main emphasis of this strategy in 1983 was on reducing the structural nucleus of the budgetary deficits, mainly by cutting down expenditure. To assist in this, special measures were taken to foster private capital formation. The policy of budgetary consolidation had a positive effect on the financial markets and thus eased the pressure on the financial accounts of enterprises, which stepped up their investment activity in the course of last year. The fact that in the final analysis business activity picked up more sharply than expected also exercised a favourable influence on the budgetary situation of the central, regional and local authorities; not least for this reason, the deficits in 1983 turned out to be substantially smaller than had been expected in the budgets at the beginning of the year. The fears expressed in some quarters that the consolidatory measures would prevent an economic recovery have therefore not been borne out.

Course of fiscal policy set mainly by the Act Accompanying the 1983 Budget

The course of fiscal policy in 1983 was set during the second half of 1982, when the economic outlook again gave rise to fears of considerable additional burdens caused by tax shortfalls and higher unemployment. For both fiscal and overall economic reasons, the central, regional and local authorities were faced with the necessity of trying to prevent the budgetary deficits from getting out of hand. The budgets for 1983 were thus characterised by efforts to economise. Under the current legislation the possibilities for this were limited, however, so that further statutory measures were required. In December 1982 Parliament approved the Act Accompanying the 1983 Budget, which eased the strain on the budgets of the central, regional and local authorities by DM 18 billion net, DM 12 billion of which affected the Federal budget alone. These measures consisted mainly of reductions in the consumption spending of the central, regional and local authorities as well as expenditure cuts and higher contribution rates for the social security funds, thereby lowering the grants payable by the Federal Government. Furthermore, the rate of value-added tax was raised as from July 1, 1983 so as to improve the basic tax conditions for capital formation with the aid of the additional revenue, viz. to the detriment of the expenditure of GNP for consumption purposes. As a first step, trade tax relief became effective at the beginning of 1983; in addition, as mentioned before, the deduction from the tax liability of interest on loans raised in connection with the construction of owner-occupied homes was extended for a limited period.

Rise in expenditure smaller than envisaged at the planning stage

In actual fact, as the budgets were implemented, substantial further reductions in expenditure were made over and above the spending cuts decided on at the planning stage. In part this was ascribable to spending policy, and in part the demands made on the budgets decreased for a variety of reasons; the gradual improvement in the labour market situation during the year was another reason why the spending appropriations were not fully used. Expenditure by the central, regional and local authorities ultimately rose by only 2% in 1983. Its growth rate thus slowed down again (having amounted to 3% in 1982) and was only about half as high as that of nominal GNP. This was in conformity with the objective of achieving budgetary consolidation mainly through restraint in spending. Even after inclusion of the social security funds, spending by the public sector increased less (by 3%) than the national product; the ratio of government expenditure to GNP therefore dropped to 51% in 1983 (it had stood at almost 52% in 1981 and 1982).

Increase in consumption expenditure curbed

Given the pattern of expenditure, i.e. from the qualitative point of view, it is significant that the central, regional and local authorities succeeded in keeping the rise in their consumption expenditure (apart from the interest payments) within relatively narrow limits in 1983. Current transfers by the central, regional and local authorities (including grants to the social security funds) were actually 2% smaller than a year previously. This was partly due to cuts in children's benefits for families in the middle- and higher-income brackets and to reductions in various other social benefits. An even more important factor was the sharp decline in the grants required by the Federal Labour Office, which have to be paid by the Federal Government. Another significant point, besides the raising of the contribution rate to unemployment insurance as from the begin-

Finances of the public authorities*

Item	1980	1981	1982 p	1983 pe	1980	1981	1982 p	1983pe
	DM billion				Percentage change from previous year			
A. Expenditure, receipts and cash results								
Central, regional and local authorities								
Expenditure								
Personnel expenditure	164.1	174.2	178.9	184.0	+ 8.0	+ 6.2	+ 2.7	+ 3.0
Other operating expenditure	77.0	82.0	86.0	89.0	+ 8.1	+ 6.6	+ 4.8	+ 3,5
Transfers	130.9	142.4	147.2	144.5	+ 7.9	+ 8.8	+ 3.3	− 2
Interest	29.6	36.8	45.1	51.5	+18.3	+24.1	+22.7	+14
Direct capital outlays	62.2	59.2	53.3	50.0	+12.5	− 4.9	−10.0	− 6,5
Indirect capital expenditure **1**	36.1	37.3	37.7	39	+ 6.3	+ 3.3	+ 1.2	+ 3.5
Other expenditure **2**	11.2	13.6	13.9	15.5	+29.1	+21.0	+ 2.7	+ 7
Total expenditure	511.1	545.5	562.0	572,5	+ 9.3	+ 6.7	+ 3.0	+ 2
of which								
Federal Government	228.3	247.7	258.8	265	+ 7.3	+ 8.5	+ 4.5	+ 2.5
Länder Governments	208.6	217.4	222.7	227.5	+ 8.8	+ 4.2	+ 2.4	+ 2
Local authorities	145.6	152.1	152.5	151	+11.7	+ 4.5	+ 0.4	− 1
Receipts								
Tax receipts	365.0	370.3	378.7	396.5	+ 6.5	+ 1.5	+ 2.3	+ 4.5
Other receipts	86.8	95.7	113.4	122.5	+11.9	+10.2	+18.5	+ 8
Total receipts	451.8	466.0	492.1	519	+ 7.5	+ 3.1	+ 5.6	+ 5.5
of which								
Federal Government	199.5	207.8	222.6	234	+ 6.9	+ 4.2	+ 7.1	+ 5
Länder Governments	186.2	190.8	198.7	206.5	+ 5.0	+ 2.5	+ 4.1	+ 4
Local authorities	139.9	142.0	145.0	149	+11.9	+ 1.5	+ 2.1	+ 3,5
Cash deficit (−)	− 59.3	− 79.5	− 69.9	− 53.5	.	.	.	.
of which								
Federal Government	− 28.8	− 39.9	− 36.2	− 31	.	.	.	.
Länder Governments **3**	− 23.2	− 27.6	− 25.3	− 20.5	.	.	.	.
Local authorities	− 5.7	− 10.1	− 7.5	− 1.5	.	.	.	.
Social security funds								
Expenditure	272.1	293.8	310.2	317.5	+ 7.6	+ 8.0	+ 5.6	+ 2.5
Receipts	275.3	299.2	315.0	315.5	+ 8.6	+ 8.7	+ 5.3	+ 0.0
Cash surplus (+) or deficit (−)	+ 3.2	+ 5.4	+ 4.8	− 2	.	.	.	.
Public authorities, total								
Expenditure	745.6	797.3	827.8	850,5	+ 8.5	+ 6.9	+ 3.8	+ 3
Receipts	689.5	723.2	762.7	795	+ 7.6	+ 4.9	+ 5.5	+ 4,5
Cash deficit (−)	− 56.1	− 74.1	− 65.1	− 55.5	.	.	.	.
	Level at end of year in DM billion				Change from previous year in DM billion			
B. Indebtedness of the central, regional and local authorities								
Loans against borrowers' notes	334.4	409.3	449.4	474	+51.4	+74.9	+40.1	+24.5
Securities	111.9	110.7	142.4	175.5	+ 1.1	− 1.1	+31.6	+33.5
Other debt	22.3	25.5	23.0	21	+ 2.2	+ 3.2	− 2.5	− 2
Total indebtedness **4**	468.6	545.6	614.8	671	+54.7	+77.0	+69.2	+56
of which								
Federal Government	232.3	273.1	309.1	341.5	+26.8	+40.8	+36.0	+32.5
Länder Governments	137.8	165.2	190.6	211.5	+21.9	+27.3	+25.5	+21
Local authorities	88.1	95.1	101.8	104	+ 4.7	+ 7.0	+ 6.7	+ 2

* In the cash definition, which differs in several respects from that of the government account of the national accounts. — **1** Expenditure on investment grants and loans to third parties, plus the acquisition of participations. — **2** Transfer of the Community share in tax revenue, differences in clearing transactions between the central, regional and local authorities, and special transactions. — **3** For technical accounting reasons the cash deficit of the Länder Governments differs from the balance of receipts and expenditure. — **4** The main reason why the change in indebtedness differs from the cash deficit is that the change in cash resources also helps to finance it. — **p** Provisional. — **pe** Partly estimated. Discrepancies in the totals are due to rounding.

ning of 1983, was that the pension insurance contributions payable on financial benefits under the Work Promotion Act were lowered.[1] Moreover, expenditure by the Federal Labour Office on unemployment benefits fell well short of the budget appropriations. On the other hand, spending on unemployment assistance (mainly to persons out of work for a longer period), which must be paid by the Federal Government direct, went up more steeply than envisaged. On balance, however, about DM 1 billion less than provided for in the budgets was spent on the jobless and on short-time workers, in view of the unexpectedly vigorous economic recovery. A further DM 1.5 billion was saved on other Federal Labour Office expenditure. The growth of personnel expenditure (+3%) was slowed down because the pay settlement for wage and salary earners in the public service was lower than in the previous year; besides, the raising of officials' pay (from July 1) was limited to 2%. Moreover, the central, regional and local authorities apparently no longer increased their staff. The endeavours to economise were also reflected in the small rise in other operating expenditure (+3½%).

Capital expenditure declines further

Capital expenditure by the central, regional and local authorities, mainly on construction, dropped again in 1983 (−6½%). Spending on completed projects was still affected by the sharp reduction in public construction orders in 1980 and 1981. New orders, by contrast, in 1983 just remained at the relatively low level of the preceding year. There were some signs in the course of 1983 that the financial scope for capital projects was gradually widening slightly, for the local authorities, the most significant public investors, have made particular progress in consolidating their budgets.

Growth of interest burden no longer quite so strong

The endeavours of the central, regional and local authorities to reduce their deficits also helped to ensure that interest expenditure did not expand as steeply in 1983 as before. Because the payments usually have to be made annually in arrears, most of the additional spending on interest last year was, however, attributable to the borrowing effected in 1982. The cost of interest was influenced by the fact that both new public borrowing and capital market rates had dropped at that time. (The further decline in net borrowing by the public sector in 1983 and the even lower average level of interest rates last year will only be reflected in the interest to be paid in 1984.) Interest expenditure grew by 14% in 1983 (against 23% and 24%, respectively, in the two preceding years) and thus still placed a heavy extra burden on the budgets. How strongly the follow-up costs of the high new indebtedness are being felt in the meantime is shown by the fact that the higher interest payments made up a good half (over DM 6 billion) of the overall expansion of the central, regional and local authorities' expenditure in 1983. Interest expenditure thus reached a total of DM 51.5 billion; its share in the budget volume of the central, regional and local authorities rose to 9% last year (it had amounted to not quite 4% ten years previously).

Increase in receipts stronger than expected

The trend of receipts likewise helped to lower the deficits. Altogether, the receipts of the central, regional and local authorities grew by 5½% in 1983. This was primarily because tax revenue went up more strongly than expected (viz. by 4½%) in view of the more favourable economic situation; the result of the official tax estimate of October 1982, on which the budgetary plans had largely been based, was finally exceeded by DM 5 billion. The overall tax ratio — i. e. the ratio of tax revenue to nominal GNP — at just over 23½% in 1983, was unchanged compared with the preceding year; it was thus slightly below its average level since the beginning of the seventies. A significant factor among the other receipts was that the Bundesbank profit transferred to the Federal Gov-

1 The pension insurance funds, whose receipts suffered by this measure, were assisted mainly by a six-month postponement of the pension adjustment.

ernment, at DM 11 billion, was actually slightly larger than a year before; the fact that the local authorities raised their fees and charges very sharply was also of significance.

Shifts in the structure of taxes

Within the tax system, a slight shift of emphasis towards indirect taxes took place last year, primarily because of the raising of value-added tax in mid-1983.[1] The sharp increase in turnover tax revenue (+8½%) was admittedly only in part ascribable to the raising of the tax rate; another cause was the upturn in consumption, especially at the beginning of the year, and the buoyancy of housing construction. Among the direct taxes, corporation tax went up even more sharply, viz. by 10½%; this was mainly due to the improved profitability of incorporated enterprises in the wake of the economic recovery. Receipts from taxes on personal income increased by 2% in 1983, the yields of assessed income tax and wage tax following very divergent trends. Revenue from assessed income tax dropped further last year (−7½%). A major reason for this was that only very small final payments were received from assessments for preceding years (possibly because tax relief measures previously introduced were increasingly having an effect). Besides, the refunds which were made to employees liable to assessment because too much wage tax had been withheld at source or because losses had been incurred on other kinds of income (which refunds are to be deducted from income tax revenue) again grew sharply in 1983. (These refunds, which cannot be attributed precisely to the various items, were equivalent to approximately 45% of the recorded revenue from assessed income tax last year.) On the other hand, other employees liable to assessment made back payments included in the income tax revenue (either because too little wage tax had been withheld or because they had received other kinds of income); the volume of such back payments is not known. If only on account of this overlapping with assessed income tax, it is not possible to deduce the tax burden on wage and salary income from the trend in wage tax revenue, which rose by 4½% in 1983 and hence over three times as much as total gross wages and salaries. Another significant factor in 1983 was that the measures adopted as part of the Act Accompanying the 1983 Budget (such as the abolition of the so-called "lump-sum tax allowance" for officials) raised wage tax revenue, taken as a whole, but only affected a limited group of employees.

Sharp decline in deficits

It was mainly as a result of spending cuts, but also owing to the favourable trend of receipts, that regional and local authorities made considerable progress in consolidating their budgets. Their deficits in 1983, at DM 54 billion, were DM 16 billion smaller than a year previously, whereas deficits of a magnitude similar to that of 1982 (DM 70 billion) had been expected in the budgets. Inclusion of the social security funds alters the volume of the deficits incurred in 1983 only slightly (DM 55 billion). This mode of calculation, however, results in an improvement of only about DM 10 billion in the overall public sector budget over the preceding year, mainly because of the less favourable results of the pension insurance funds. As a proportion of GNP, the overall public sector deficit fell to 3¼%; in the last two years taken together it has thus been reduced by 1½ percentage points.

Further relief measures taken for 1984

The central, regional and local authorities intend to continue the policy of consolidation in the current year as well. Important preconditions for this were created by the Act Accompanying the 1984 Budget, which was adopted at the end of last year. It includes savings of DM 5 billion on the statutory benefits of the central, regional and local authorities and the social security funds. Further substantial amounts are to be saved by postponing the next adjustment of

1 The temporary, repayable investment assistance levy (with a yield of DM 0.5 billion in 1983) is not included in tax revenue; it is treated as borrowing in the Federal budget.

Record of economic policy measures

I. Domestic and external monetary policy

1983

January 20	The banks' rediscount quotas and the ceiling for the purchase of prime bankers' acceptances are raised by a total of DM 5.5 billion with effect from February 1.
March 17	The Bundesbank lowers the discount rate from 5% to 4% and the lombard rate from 6% to 5% with effect from March 18. At the same time the banks' rediscount quotas are reduced by DM 5 billion with effect from April 5 so as to absorb some of the excess liquidity which has arisen among the banks as a result of substantial foreign exchange inflows prior to the realignment in the European Monetary System (EMS).
March 21	The central rates in the EMS are realigned. The Deutsche Mark is revalued by 5½%, the Netherlands guilder by 3½%, the Danish krone by 2½% and the Belgian and Luxembourg franc by 1½%; the French franc and the Italian lira are devalued by 2½% each and the Irish pound by 3½%.
March 31	The Board of Governors of the International Monetary Fund (IMF) decides to increase total quotas in the Fund from SDR 61 billion to SDR 90 billion under the Eighth General Review of Quotas. It is also agreed to extend the refinancing facilities available to the Fund under the General Arrangements to Borrow (GAB) and to enlarge the GAB from SDR 6.5 billion to SDR 17 billion.
April 7	The Bundesbank approves its annual accounts for 1982 and transfers DM 11 billion of its net profit to the Federal Government.
June 30	Following its regular review of the monetary target in mid-year, the Bundesbank reaffirms its monetary target for 1983, which provides for the increase in the central bank money stock to be kept within a range of 4 to 7% (between the fourth quarter of 1982 and the fourth quarter of 1983). It indicates that it still considers it possible to meet the target up to the end of the year if the slowdown in monetary expansion observed in the second quarter continues.
July 7	After a prolonged break, the Bundesbank again enters into repurchase agreements in securities with domestic banks. In the latter part of the year as well, the banks are supplied with additional liquidity on a short-term reversible basis only, on terms that are in line with market conditions.
September 8	The Bundesbank raises the lombard rate from 5% to 5½% with effect from September 9.
December 15	The Bundesbank announces its monetary target for 1984: the growth of the central bank money stock between the fourth quarter of 1983 and the fourth quarter of 1984 is to be kept within a range of 4 to 6%. The new monetary target is so gauged as not to jeopardise the objective of monetary stability and to create monetary conditions permitting strong real economic growth.
December 26	The revised and enlarged General Arrangements to Borrow (GAB) enter into force. Under these arrangements the Fund may now also borrow to finance its lending to Fund members that are not participants in the GAB.
December 30	The new IMF quota of the Federal Republic of Germany (SDR 5.4 billion) becomes effective on payment of the increase in the quota to the Fund.

II. Economic and fiscal policy

1983

January 1	Major parts of the Act Accompanying the 1983 Budget come into force. The Act contains measures to consolidate the budgets and encourage capital formation. Altogether, the relief for the central, regional and local authorities in 1983 amounts to DM 18 billion net, DM 12 billion of which is for the Federal Government alone. Important measures are: savings on children's benefits and other welfare benefits of the central, regional and local authorities, cuts in subsidies, limitation of the growth in personnel expenditure by raising officials' pay and pensions only slightly, viz. by 2%, on July 1, 1983; increase in the turnover tax rates to 14% (7%) as from July 1, 1983, and use of the additional receipts to provide tax relief in order to improve the basic tax conditions for capital formation; introduction of a non-interest-bearing, repayable investment assistance levy, the revenue from which is used to foster housing construction. Furthermore, expenditure is cut down and the contribution rates are raised in the field of social security, thus curtailing the grants payable by the Federal Government.
January 27	In its 1983 Annual Economic Report the Federal Government states that the aim of its economic policy is to lastingly improve the prospects for employment by modifying major basic conditions for economic activity, primarily with a view to strengthening the propensity to invest. It considers an overall economic performance in which the real gross national product grows perceptibly in the course of 1983, and thus on average regains the level of the preceding year, to be within reach. Moreover, the average annual increase in consumer prices should not exceed some 4%.
April 28	The Fiscal Planning Council is of the opinion that the authorities should press on faster with budgetary consolidation in the next few years in keeping with the expected progress of the economic recovery. This should be done mainly through effective and lasting limitation of the growth of expenditure, and not by raising the overall burden of taxes and other levies.

June 14

The Federal Government approves government subsidies for the German steel industry to the amount of DM 3 billion up to the end of 1985. One-half of this sum is to be contributed by the Länder Governments. In addition to the raising of the investment grant from 10% to 20% (DM 1.2 billion), DM 1.8 billion is earmarked for structural improvements (funds for welfare plans and to subsidise the closing down of production capacity).

June 29

On the basis of the coalition agreements of March and the decisions of principle taken in mid-May, the Federal Government approves the draft Federal budget for 1984 and the fiscal plan for the period until 1987. The growth of Federal expenditure is limited to about 2% in 1984 and some 3% in the following years. The financial deficit is to be kept down to DM 37.5 billion in 1984 and reduced progressively to DM 23 billion by 1987.

At the same time several new bills are approved. The Act Accompanying the 1984 Budget is designed to relieve the pressure on the public budgets by approximately DM 10 billion in all. The savings on statutory benefits of the central, regional and local authorities and the social security funds amount to DM 5 billion; in addition, the receipts of the social security funds are to be increased by some DM 5 billion by making more special payments and sickness benefits liable to contributions. Further savings are also envisaged, primarily by postponing the wage and salary increases in the public service. Under the 1984 Tax Relief Act, the second half of the additional revenue accruing from the raising of the value-added tax rate as from mid-1983 is to be used mainly to alleviate the property tax burden on the business community and for special depreciation allowances.

November 21

In its Report for 1983–84 the Council of Economic Experts notes a perceptible improvement in the economic situation. The economic recovery has been triggered by the change in the behaviour of investors and consumers and not, as in the past, by an upturn in foreign demand. At the present time there is no need for short-term economic policy measures. The Council expresses concern, however, about the fact that not enough has been done to remove the domestic impediments to economic growth, and it recommends inter alia the continuation of the consolidation policy pursued by the public authorities as well as of a wage policy that helps to lower costs.

December 2

The Fiscal Planning Council shares the view of the Council of Economic Experts that the consolidation policy has not impeded, but on the contrary fostered, the economic recovery. It emphasises that in 1984 and the following years priority should be given to the gradual reduction of the public deficits, and that budgetary consolidation should begin with expenditure cuts.

December 9

The Bundestag approves the 1984 Federal budget and its Accompanying Acts (the latter with only minor amendments as compared with the bills). After the deliberations the Federal budget shows an expenditure volume of DM 257 billion (+ 1½% over the amount envisaged for 1983) and a financial deficit of DM 34 billion; on the receipts side the estimate for the profit transfer by the Bundesbank is raised by DM 2.5 billion to DM 9 billion.

1984

February 2

In its 1984 Annual Economic Report the Federal Government designates a sound budgetary policy, a tax policy that encourages performance and capital formation, and the elimination of bureaucratic obstacles as preconditions for the transition of the economic recovery to a period of sustained growth. It considers an increase of 2½% in the real gross national product and a decline in unemployment to not quite 8% of the total labour force to be attainable in 1984 and a more favourable growth figure to be quite possible. Furthermore, the rise in consumer prices could again be limited to 3% on an annual average.

April 5

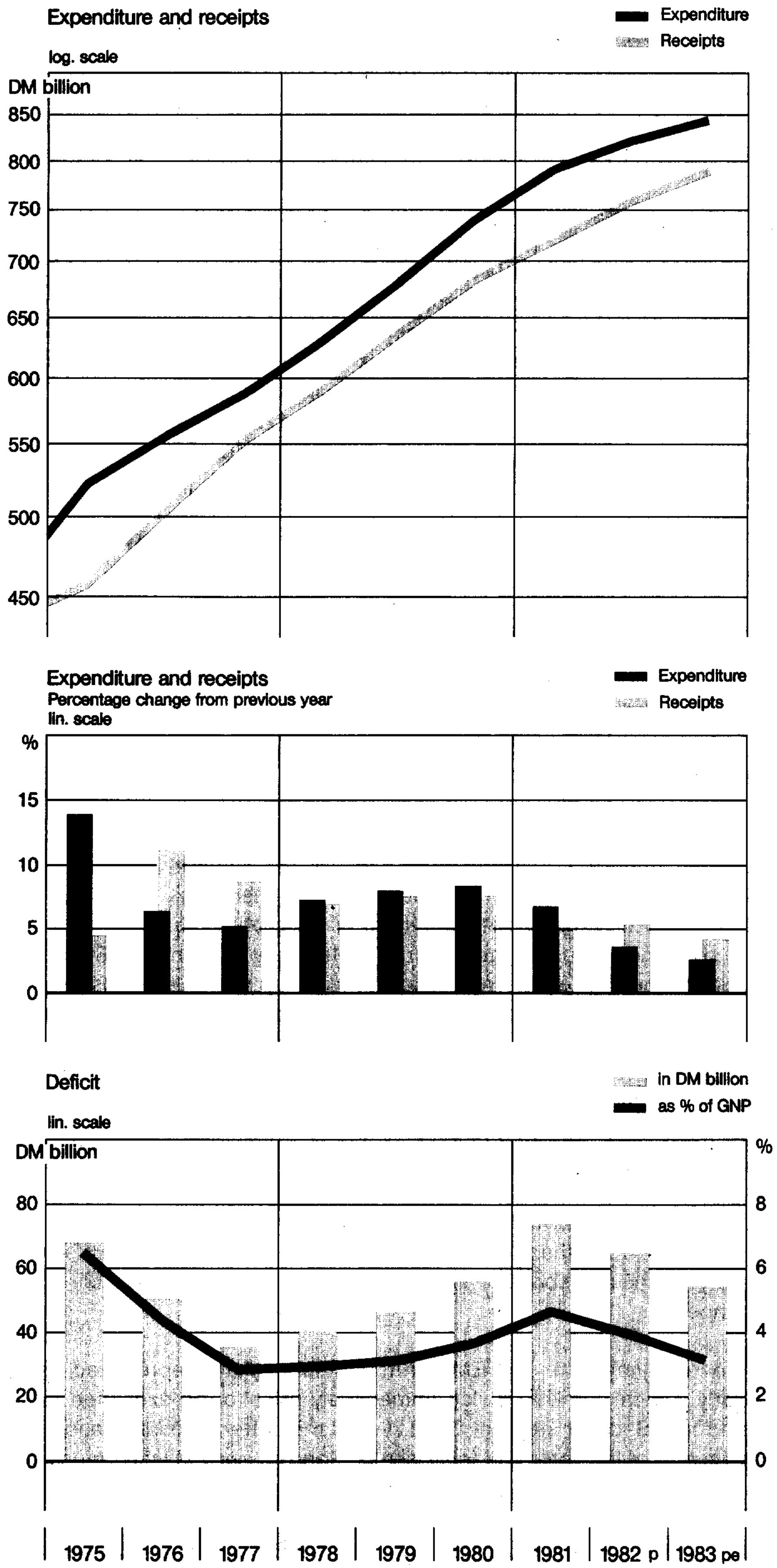
The Fiscal Planning Council adheres to the objective of limiting the growth of public sector expenditure to some 3% a year in the medium term. It emphasises that measures to assist families and modify the taxation of wages and income must be in harmony with the task of consolidating the budgets, which continues to have top priority.

wages and salaries in the public service to the year 1985. In addition, the social security funds are to receive about DM 5 billion more by making special payments and sickness benefits subject to contributions to a greater extent. At the same time a Tax Relief Act was approved, under which the additional receipts from the increase in value-added tax, which will be effective for the entire year in 1984, are to be used in particular to ease the burden of property tax on enterprises and to provide certain special depreciation facilities. If the measures decided on in the last three years (beginning with "Operation '82") are viewed as a whole, the pressure on the public sector budgets will have been alleviated to the extent of about DM 55 billion[1] by end-1984 (this makes clear at the same time that, in the absence of these measures, the public deficits would have been likely to rise further). The bulk of the savings, at about DM 35 billion, consisted of cuts in consumption expenditure. Approximately DM 20 billion (net) came from higher levies, predominantly additional receipts of social security contributions; it is significant in this context that it was not possible to reduce the massive deficits incurred by the Federal Labour Office without raising the contribution rate. Besides the statutory measures, reductions were made, when planning and implementing the budgets, in personnel expenditure (not least through restraint in new recruitment), in other operating expenditure and also on a considerable scale in capital spending.

Course of the consolidation

In 1984 the reduction of the deficits will in all probability be assisted by economic developments: tax receipts are likely to grow more vigorously than last year for cyclical reasons, and expenditure on unemployment might even decline. Besides, the starting position for the new budget year was more favourable than was assumed only shortly before the end of last year; this was not taken into account in the plans that were completed in 1983. The same goes for the Federal Government's receipts from the profit transfer by the Bundesbank, which were put at DM 9 billion in the budget, but according to the annual accounts of the Bundesbank (see page 110) amount to just over DM 11 billion. The deficits of the central, regional and local authorities in 1984 will therefore probably be smaller than was estimated towards the end of last year, unless new burdens arise. This does not mean, however, that the task of consolidation has been completed. In the current year as well a substantial part of the domestic acquisition of financial assets will still be used for government purposes; it would be desirable to gain more scope from now on for the financing of private capital formation, the most significant buttress of economic growth. Given the longer-term growth and employment problems it also appears doubtful in this context whether the ideas developed in earlier years about the size of the public sector deficit which is tolerable under "normal" economic conditions can still serve as a guideline for future fiscal policy. Concepts stemming from the time when, under the influence of the Act to Promote Economic Stability and Growth, the prime concern was to smooth out cyclical fluctuations with the aid of fiscal policy measures, and when it was not yet the primary aim of economic and fiscal policy to strengthen the basic conditions for the growth of our economy over the long term so as to encourage structural changes and safeguard competitiveness, now hardly appear to be suitable criteria. If the conditions for growth over the medium term are to be improved, reducing the high ratio of government expenditure to GNP is, moreover, no less important than lowering the deficits. Even in 1984 the "government ratio" will presumably approach 50%, against 47% ten years earlier and barely 40% twenty years before. Bringing down the government ratio of course calls for considerable fiscal policy staying power; just as its rise took place over a fairly long period of time (chiefly in the years from 1970 to 1975), it can be reduced perceptibly only step by step. In line with this objective, endeavours should also be made, when

1 This disregards the repercussions of the course of economic activity, which has been influenced by these measures, on the public budgets.



* Central, regional and local authorities and social security funds.- p Provisional.- pe Partly estimated.

drawing up the budgets for 1985, to take advantage of the probable continuation of the favourable economic trend to reduce the government ratio further. The more the private sector develops sufficient momentum of its own, while the consolidation policy is adhered to, the more room for manoeuvre the central, regional and local authorities will themselves regain for performing important public functions. First indications of this are already emerging, for instance in the fact that the principal public investors, the local authorities, are able to become more active again in that area. One precondition for this is, however, that the relatively restrictive attitude to consumption expenditure is not abandoned.

The conditions for a reduction in income tax

If the present course of fiscal policy is pursued further, it is to be expected that financial scope will arise in the medium term for lowering wage tax and assessed income tax (together with family policy measures). It is admittedly difficult to judge to what extent the public authorities in the Federal Republic of Germany will have to shoulder burdens that have not so far been allowed for, e. g. burdens emanating from the European Communities. If only for that reason, it is uncertain how rapidly the process of consolidation can advance. When choosing the time and extent of the tax reduction it must at all events be ensured that it does not jeopardise anew the incipient consolidation of the public sector budgets.

3. The external situation under the influence of sharp exchange rate fluctuations

Balance of payments largely in equilibrium

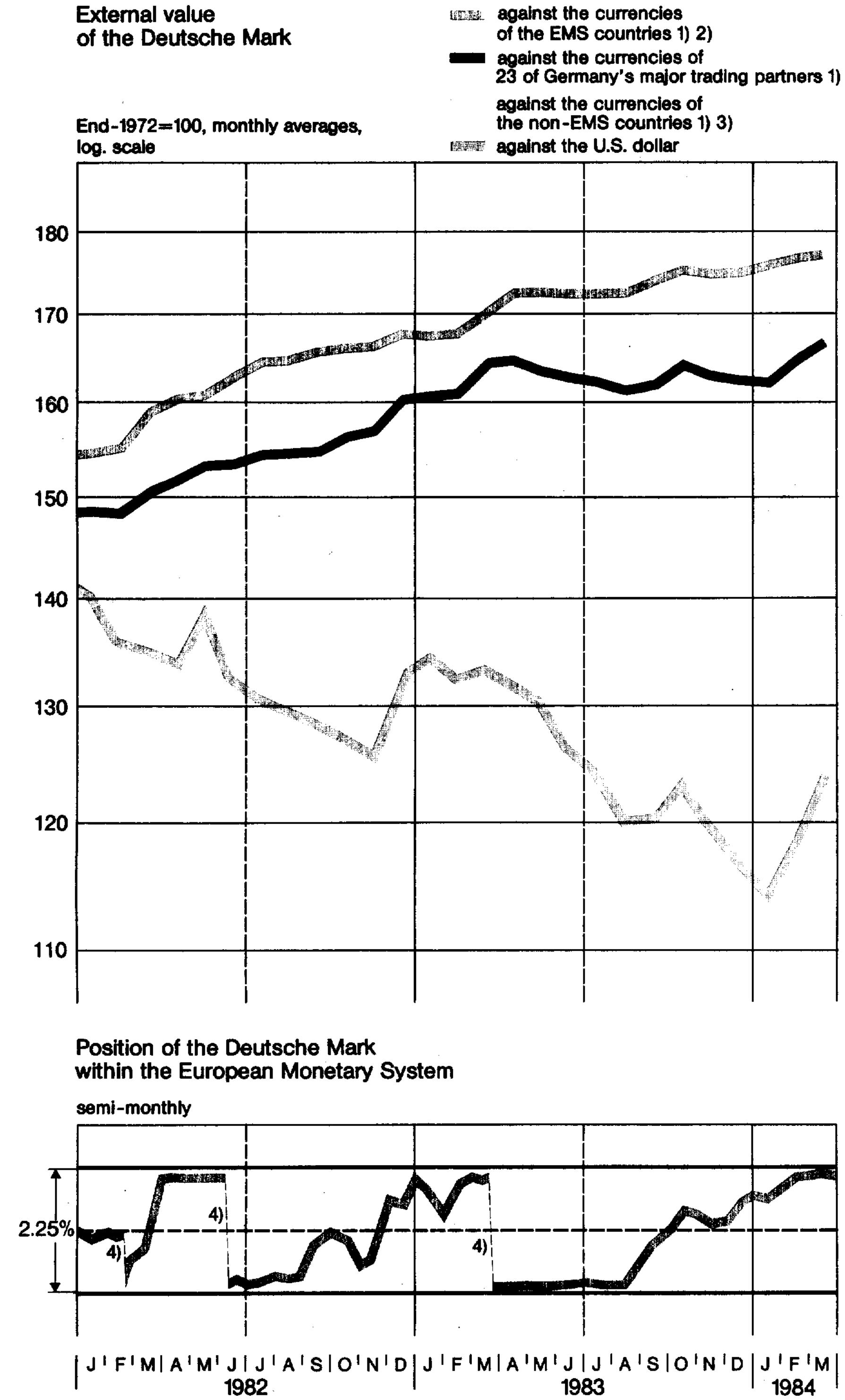
Judging by the annual results, external payments were virtually in equilibrium in 1983: on current account Germany again achieved a small surplus, which, at DM 10 billion, was slightly larger than a year earlier. The net outflows in long-term capital transactions were almost as large as the surplus on current account; compared with 1982 the outflow of funds halved. The monetary reserves did not change to any significant degree; the net external assets of the Bundesbank, calculated at balance sheet rates, declined by only DM 1.5 billion.

Temporary exchange rate tensions in the EMS

However, this generally gratifying overall picture was clouded at times by sharp exchange rate fluctuations. Thus, the Deutsche Mark was distinctly strong against all major currencies between the beginning of the year and the realignment of exchange rates in the European Monetary System (EMS) in March 1983; against the U.S. dollar, in particular, it held up well during this time. This period of strength of the Deutsche Mark was accompanied by substantial speculative inflows of foreign exchange, which played a part in expanding the money supply at the time. The realignment of March 21 was something of a turning point; afterwards, at any rate, the Deutsche Mark tended to be weak. This seems to have owed something to the fact that the appreciation of the Deutsche Mark against the EMS currencies — at 5½ % on a weighted average, as measured by central rates — was generally considered relatively high. It was not until September that the Deutsche Mark definitely left the bottom edge of the exchange band in the EMS; in this connection, the adjustment of the lombard rate of the Bundesbank to the higher market rates was probably of some significance.

Depreciation of the Deutsche Mark against the U.S. dollar after the realignment in the EMS

After the realignment in the EMS the Deutsche Mark depreciated sharply, particularly against the U.S. dollar. Immediately prior to the exchange rate adjustment the U.S. dollar stood at DM 2.39, but thereafter it soared, reaching DM 2.72 at the end of the year; the dollar rise reached its peak in mid-January, at an exchange rate of DM 2.84 per U.S. dollar (or an 18½ % appreciation since March 1983). Although other major "third currencies", such as the Japanese yen (21¼ %), the pound sterling (11 %) and the Swiss franc (8¾ %), also appreciated against the Deutsche Mark during the same period, this loss in value of the Deutsche Mark was probably not an autonomous weakness attributable



1) Weighted external value of the Deutsche Mark, geometric mean.- 2) Excluding the pound sterling.- 3) Including the pound sterling and the U.S. dollar.- 4) Realignment of exchange rates in the EMS.- Latest position: March 1984.

to economic developments in Germany, but primarily a reflection of the general strength of the dollar, which manifested itself especially strongly vis-à-vis the Deutsche Mark as the most exposed currency. High interest rates in the United States, the favourable trend in the U.S. economy and political factors not only prevented any depreciation, which might otherwise have resulted from the growing deficit on the United States' current account, but also enhanced the upward movement of the U.S. dollar. The Deutsche Mark, as the antipole of the U.S. currency, was particularly affected by its tendency to rise.

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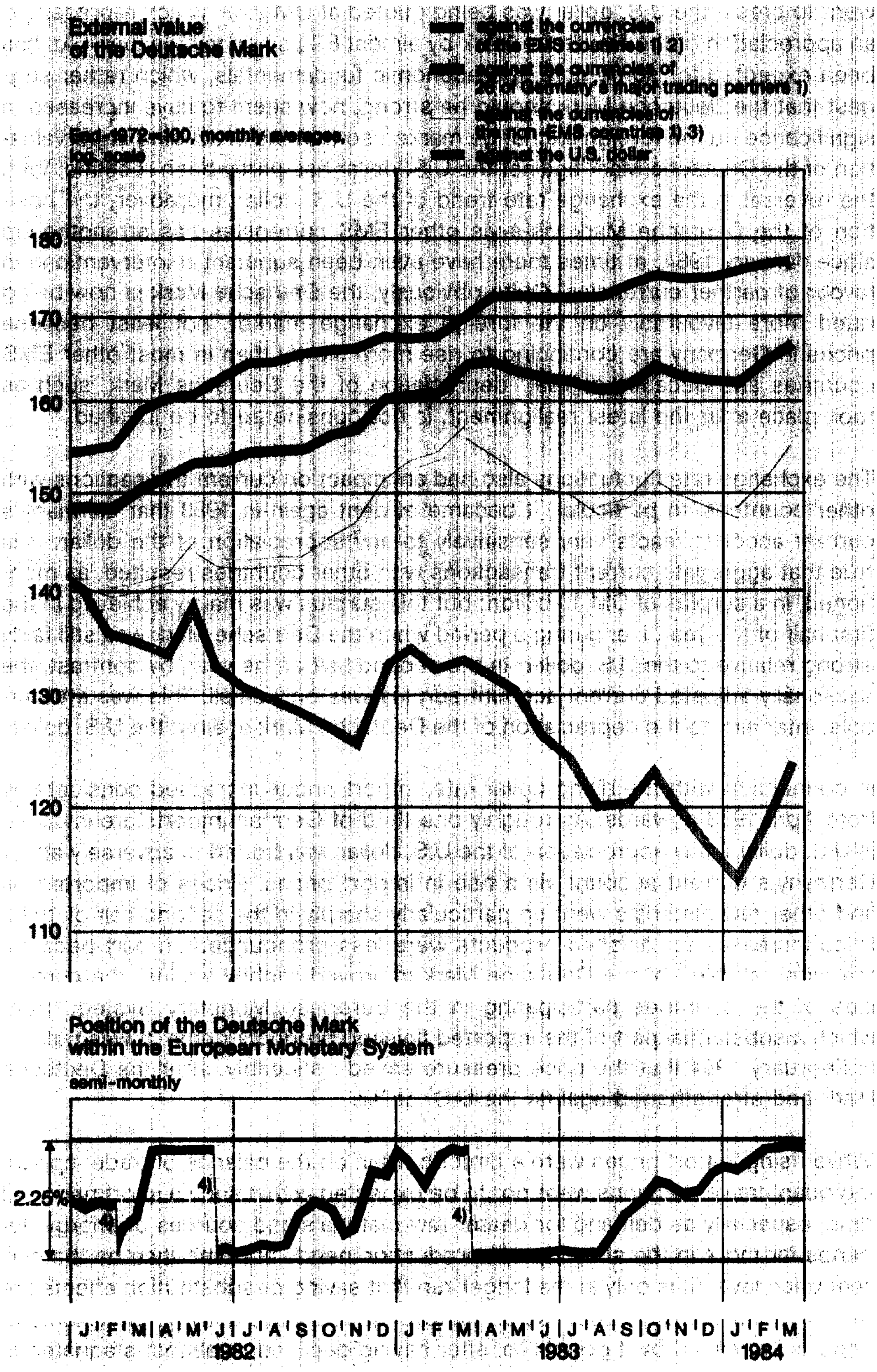

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Renewed firming of the Deutsche Mark since mid-January 1984

During January 1984, however, the exchange rate trend, which had been so unfavourable for the Deutsche Mark, changed direction again and the Deutsche Mark gained a great deal of ground vis-à-vis the U.S. dollar. When this Report went to press, the U.S. dollar was being quoted at DM 2.63, which represented an appreciation of the Deutsche Mark by almost 8 % since mid-January. As has been expected for some time, the economic fundamentals, which rather suggest that the Deutsche Mark should be strong, now seem to have increased in significance on the foreign exchange market, so that the preceding undervaluation of the Deutsche Mark against the U.S. dollar has partly been rectified. With the reversal in the exchange rate trend of the U.S. dollar, moreover, the position of the Deutsche Mark vis-à-vis other EMS currencies has strengthened since January 1984; at times there have even been substantial interventions in favour of partner currencies. Quite obviously, the Deutsche Mark is now being rated more favourably on the foreign exchange market, not least because prices in Germany are continuing to rise more slowly than in most other EMS countries and because a "real" depreciation of the Deutsche Mark, such as took place after the latest realignment, is not considered to be justified.

Deterioration of the current account in the course of 1983 . . .

The exchange rate fluctuations also had an impact on current transactions with other countries. In particular, it became evident again in 1983 that Germany's current account reacts very sensitively to any appreciation of the dollar. It is true that aggregate current transactions with other countries resulted, as mentioned, in a surplus of DM 10 billion; but this surplus was mainly achieved in the first half of the year, i. e. during a period when the Deutsche Mark was still fairly strong relative to the U.S. dollar. In the second half of the year, by contrast, the seasonally adjusted current account surplus was only small. This was attributable, inter alia, to the depreciation of the Deutsche Mark against the U.S. dollar.

. . . owing to exchange-rate-induced rises in import prices

In connection with the rising dollar rate, import prices increased considerably from April 1983 onwards. As roughly one-third of German imports are invoiced in U.S. dollars, any appreciation of the U.S. dollar was bound to adversely affect Germany's current account via a rise in import prices. Prices of imported oil and other raw materials went up particularly sharply in the second half of 1983. Price increases for finished products were less pronounced, in part because the external value of the Deutsche Mark improved slightly against the currencies of the countries participating in the European Monetary System, from which a substantial part of the imported finished products come. It was not until February 1984 that the price pressure eased noticeably, after the Deutsche Mark had strengthened against the U.S. dollar.

Steep cyclical rise in the volume of imports

While rising import prices were a direct burden on the balance of trade, opposing quantitative reactions were not to be expected within such a short period of time, especially as demand for dearer raw materials and sources of energy depends far more in the short run on production needs at home than on the current price level (it is only in the longer run that saving or substitution effects are felt). Therefore, mainly because of the level of economic activity, the volume of imports increased by a good 4 %, after having declined or almost stagnated in 1981 and 1982 — also as a result of the cyclical trend. The expansion of German demand for imports thus imparted considerable stimuli to the economies of our trading partners, with the industrial countries of Western Europe profiting significantly.

Sharp growth of imports of finished goods

It is striking that imports of finished goods expanded again in 1983 (by 7 % in volume terms). After two rather sluggish years, the tendency apparent up to 1980 for foreign finished goods to gain ground on the German market seems to be reasserting itself again. During the period under review more road vehicles, office machines, data processing systems and electrical engineering products, in particular, were bought abroad. Raw materials and semi-finished goods, ex-

Major items of the balance of payments

DM billion

Item	1976	1977	1978	1979	1980	1981	1982	1983
A. Current account								
1. Foreign trade								
Exports (f.o.b.) 1	256.6	273.6	284.9	314.5	350.3	396.9	427.7	432.3
Imports (f.o.b.) 1	214.6	227.7	235.8	282.7	331.4	357.3	365.2	378.9
Balance	+42.1	+45.9	+49.2	+31.8	+18.9	+39.6	+62.6	+53.5
2. Supplementary trade items 2 and merchanting trade	− 0.1	+ 0.0	+ 2.1	+ 0.2	− 0.0	+ 1.0	+ 2.1	+ 4.9
Balance of trade	+42.0	+46.0	+51.2	+32.0	+18.9	+40.6	+64.7	+58.4
3. Services	−14.2	−18.2	−15.3	−21.9	−23.0	−26.9	−27.7	−21.8
of which								
Foreign travel	−14.6	−16.4	−19.0	−21.6	−25.2	−25.8	−26.3	−24.4
Investment income	+ 3.3	+ 0.4	+ 5.1	+ 3.2	+ 4.2	+ 0.5	− 2.2	+ 4.1
4. Transfer payments	−17.9	−18.2	−17.8	−21.2	−24.5	−26.8	−28.3	−26.5
of which								
Remittances of foreign workers	− 6.7	− 6.1	− 6.3	− 7.0	− 7.5	− 7.9	− 7.8	− 7.4
Transfers to the European Communities (net)	− 3.5	− 3.5	− 1.9	− 4.0	− 4.5	− 6.5	− 7.5	− 6.1
Balance on current account	+ 9.9	+ 9.5	+18.1	−11.1	−28.6	−13.1	+ 8.7	+10.1
B. Capital account								
1. Long-term capital transactions								
(a) German investment abroad (increase: −)	−19.9	−23.1	−24.1	−20.9	−28.8	−27.6	−30.1	−34.6
of which								
Direct investment	− 6.2	− 5.1	− 7.2	− 8.2	− 7.4	− 8.8	− 8.0	− 7.4
Advances and loans of enterprises	− 0.3	− 0.3	− 0.2	− 1.0	− 0.6	− 0.8	− 1.1	− 0.7
Portfolio investment	− 0.9	− 5.4	− 4.2	− 3.0	− 7.7	− 6.0	−11.4	−10.4
Advances and loans of banks	− 9.7	− 9.6	− 8.5	− 5.4	− 9.4	− 5.3	− 3.7	− 8.4
Official	− 2.4	− 2.1	− 3.3	− 2.4	− 2.3	− 4.9	− 4.4	− 5.6
(b) Foreign investment in Germany (increase: +)	+19.1	+10.5	+21.3	+33.1	+34.5	+35.9	+14.2	+27.2
of which								
Direct investment	+ 3.4	+ 2.2	+ 3.3	+ 3.2	+ 0.8	+ 0.8	+ 2.6	+ 2.9
Advances and loans of enterprises	+ 1.4	+ 0.5	+ 0.2	+ 0.4	+ 1.4	+ 4.2	+ 3.8	+ 0.5
Portfolio investment	+ 4.8	+ 2.3	+ 3.2	+ 5.9	+ 0.9	+ 1.0	+ 2.7	+13.6
Advances and loans of banks	+ 4.9	+ 5.0	+14.8	+22.8	+ 8.5	+ 7.0	− 3.9	− 1.7
Official	+ 4.8	+ 0.5	− 0.0	+ 0.9	+23.1	+23.0	+ 9.2	+12.1
Balance of long-term capital transactions	− 0.8	−12.6	− 2.8	+12.2	+ 5.7	+ 8.3	−15.9	− 7.4
2. Short-term capital transactions (net capital exports: −)								
(a) Enterprises and individuals	− 5.7	+ 4.6	− 2.9	− 5.3	+ 7.6	+ 8.2	+ 2.7	− 7.3
Financial credits	− 0.0	+ 8.5	+ 1.0	− 3.7	+13.3	+13.0	+ 3.6	− 1.0
Trade credits	− 5.7	− 3.9	− 3.9	− 1.7	− 5.7	− 4.8	− 0.9	− 6.3
(b) Official	− 0.6	− 0.0	+ 1.2	− 0.3	− 0.4	+ 3.0	+ 0.7	− 3.3
(c) Banks	+ 6.7	+ 8.1	+10.1	+ 4.1	− 8.9	−10.3	+ 8.1	+ 2.0
Assets	− 2.7	+ 1.2	− 2.2	− 1.7	− 7.1	−11.2	+ 4.3	+ 5.3
Liabilities	+ 9.4	+ 6.9	+12.3	+ 5.8	− 1.8	+ 0.9	+ 3.8	− 3.3
Balance of short-term capital transactions	+ 0.4	+12.6	+ 8.4	− 1.5	− 1.6	+ 0.9	+11.5	− 8.5
Balance on capital account	− 0.3	− 0.0	+ 5.6	+10.7	+ 4.1	+ 9.2	− 4.4	−15.9
C. Balance of unclassifiable transactions (balancing item)	− 0.8	+ 0.9	− 3.9	− 4.5	− 3.4	+ 1.6	− 1.2	+ 1.8
D. Balancing item to the external position of the Bundesbank 3	− 7.5	− 7.9	− 7.6	− 2.3	+ 2.2	+ 3.6	− 0.4	+ 2.4
E. Change in the net external assets of the Bundesbank (increase: +) (A plus B plus C plus D)	+ 1.3	+ 2.6	+12.2	− 7.3	−25.7	+ 1.3	+ 2.7	− 1.6

1 Special trade. — 2 Mainly warehouse transactions for account of residents and deduction of goods returned and of commission processing. — 3 Counterpart of changes in the Bundesbank's external position which are not caused by external current and capital transactions: mainly the allocation of IMF special drawing rights and changes in the Deutsche Mark value of the external position of the Bundesbank owing to valuation adjustments; as from 1982 also the differences between the transaction values and the changes in the external position as shown in the Weekly Return at balance sheet rates. Discrepancies in the totals are due to rounding.

cept those included in energy sources, were also imported on a larger scale in 1983 (+2% in real terms). Imports of energy, however, virtually stagnated in volume terms, despite a distinct rise in the gross national product. The high level of energy prices obviously led to the continued sparing use of energy. In the area of energy imports, however, considerable changes took place. Imports of petroleum products increased strongly again in 1983 (by 16% in volume compared with the preceding year). By contrast, German imports of crude oil declined sharply again, namely by 10% in terms of volume. These shifts in energy imports are due to the fact that, in view of the keen price competition on the market for specific petroleum products, the processing of crude oil in German refineries, with relatively high value added at home, is often less economic than the direct importation of petroleum products. As the overall import prices of energy declined in 1983 (by 6% as measured by unit values), despite price rises in the second half of the year, the amount spent on total energy imports, at DM 85 billion, was distinctly smaller than a year earlier (DM 90 billion). After deducting energy exports (DM 15 billion in 1983), Germany's overall energy account showed a deficit of DM 70 billion (against DM 74 billion in 1982).

Strong growth of exports as from mid-1983

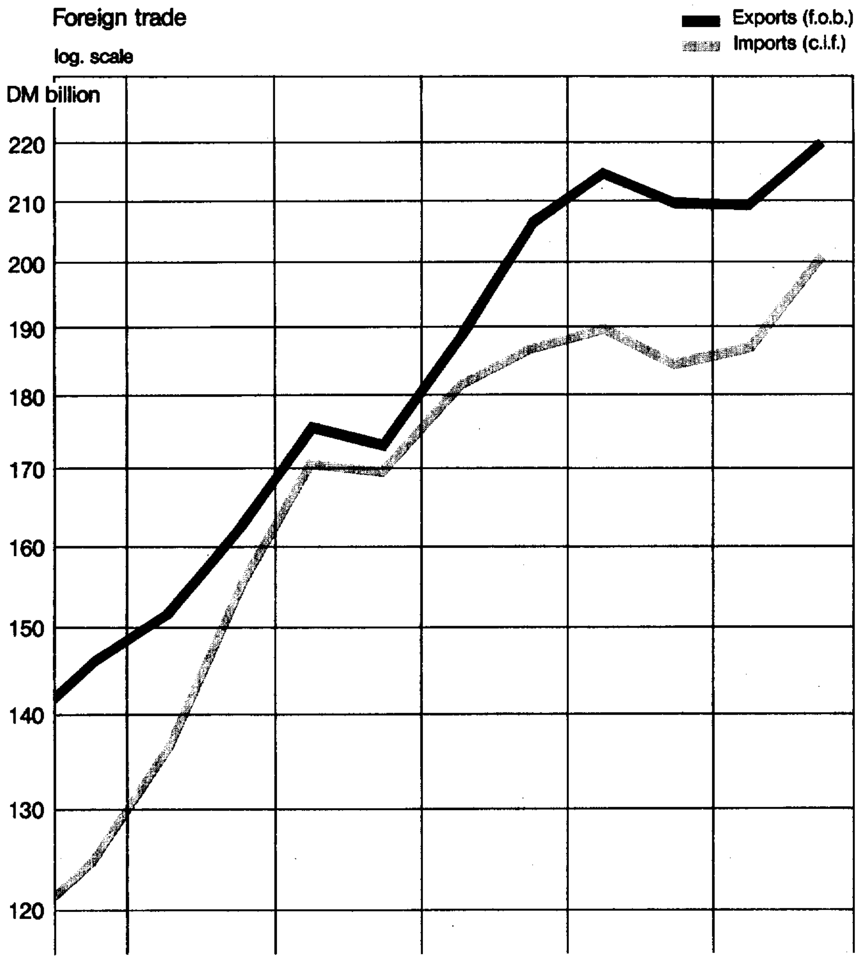
Not until mid-1983, i. e. much later than in the case of imports, did German exports also begin to expand again on a considerable scale, following a one-year period of stagnation. From then on at least part of the cyclical and exchange-rate pressure deriving from imports could be absorbed. Owing to their subdued development in the first half of the year, exports hardly changed in value or volume over the whole of 1983. In the second half of the year, however, seasonally adjusted exports increased by about 5% in both real and nominal terms compared with the first half of 1983. This revival of exports is the more remarkable as major customer countries for German products, such as France and Italy, are lagging behind in the world-wide economic recovery, since unsolved structural and stabilisation problems are continuing to loom large in these nations. Besides, the OPEC countries drastically cut down their import demand in 1983, as the further fall in their oil revenue made it necessary for them to postpone or even abandon some of their ambitious development plans. Large-scale industrial plant construction, in particular, was affected by this change in the global economic environment. If, nevertheless, exports started to expand strongly again in the course of 1983, this was due, firstly, to the fact that Germany's other sales markets experienced a strong economic upswing which resulted in the demand for imports growing sharply there. As their export receipts improved, inter alia owing to the rise in the world market prices of raw materials, even many highly indebted developing countries found it possible to relax some of their import restrictions slightly. Secondly, their success in the field of exports suggests that German exporters have in general remained competitive; this point is dealt with in greater detail below (page 51). The appreciation of the dollar improved the competitive situation for German industrial products, especially in the "dollar area"; however, the associated nominal depreciation of the Deutsche Mark exceeded the degree that appears justified in the light of longer-term price and cost relationships, so that the possibility of a correction of this exchange rate leap has to be taken into account. It is not to be expected, therefore, that the price advantages for German exports will long remain as large as they are now.

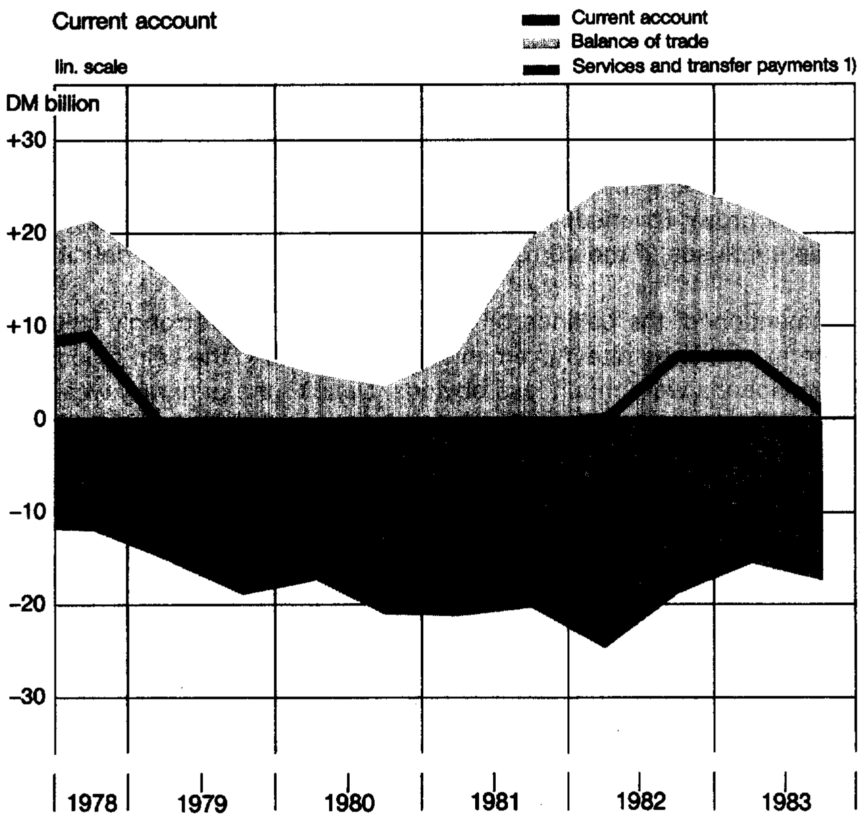
Exports pick up in virtually all branches of industry

As economic activity revived all over the world, exports from the basic and producer goods sector, in particular, gathered pace. Exports of chemical goods increased most, but the German steel industry also stepped up its sales abroad distinctly in the course of the year — although it started from a very low level. As capacity utilisation was low in some industries, the higher foreign demand for such mass products could generally be satisfied without much delay. The export business of the consumer goods sector was also buoyant, primarily because the economic recovery in most western industrial countries was at

Foreign trade and current account

half-yearly, seasonally adjusted





1) Including supplementary trade items and balance of merchanting trade.

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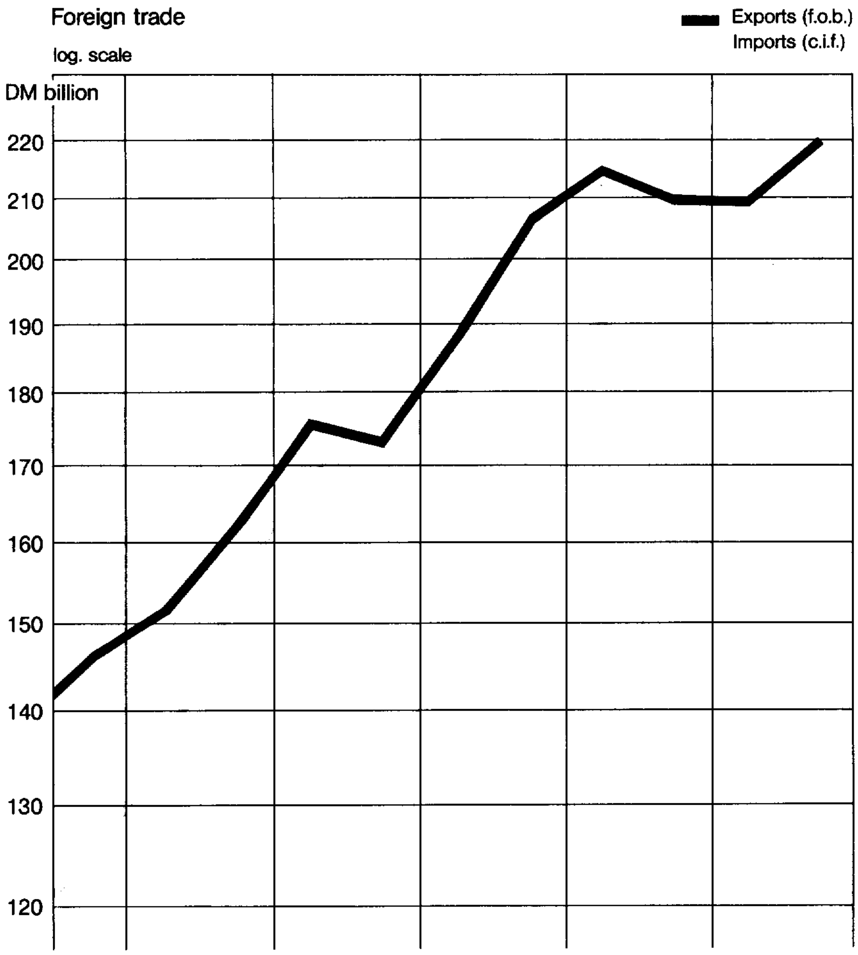
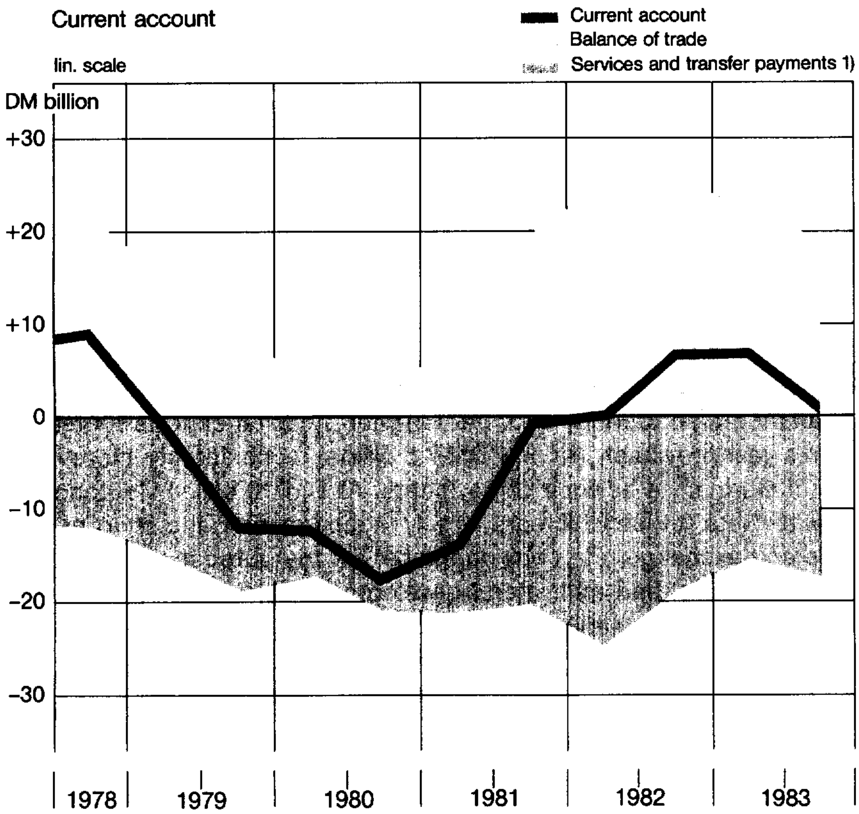
Foreign trade and current account

half-yearly, seasonally adjusted





1) Including supplementary trade items and balance of merchanting trade.

first mainly fuelled by consumer demand. On the other hand, real exports of capital goods, especially from the mechanical engineering sector, remained rather sluggish; it was not until the second half of the year that new foreign orders expanded noticeably in this field. The renewed growth of exports has given considerable additional impetus to domestic economic activity since mid-1983.

Decline in the trade surplus, but also in the deficits on "invisible" current transactions

The time-lag between the rise in imports caused by the growth of domestic demand and the subsequent increase in foreign demand for German products was partly responsible for the slight fall from quarter to quarter in the seasonally adjusted trade surplus. In 1983 overall foreign trade — on an f.o.b. basis[1] — produced a surplus which, at DM 53.5 billion, was DM 9 billion smaller than a year before. The fact that the current account, as mentioned, nevertheless showed a small improvement over the preceding year was due to a favourable trend in "invisible" transactions with other countries — a trend that is unlikely to be repeated in this form. Germany's deficits on services and transfer payments accounts (including freight and insurance costs payable on imports) totalled DM 48.5 billion in 1983 and were thus DM 7.5 billion smaller than a year before. This was due above all to the improvement on investment income account, where Germany moved from a deficit of over DM 2 billion in 1982 to a surplus of more than DM 4 billion. Several factors were acting in the same direction here, e. g. the return to current account surpluses and the associated increase in Germany's net external assets; the rise in the dollar, which caused the Deutsche Mark value of the interest income from dollar assets to go up accordingly; and the differing maturity structures of German external assets and liabilities, which meant that the global decline in interest rates caused interest payments to other countries to decrease more than the interest income on the receipts side. In addition, the deficit on foreign travel dropped slightly, after having stood at roughly the same level in the two preceding years. The deficit on transfer payments account likewise declined a little, mainly because Germany's net contributions to the EEC budget went down by DM 1.5 billion to DM 6 billion over the whole of 1983.

Rising deficits on services and transfer payments likely in the longer run

In the somewhat longer run, however, the deficits on "invisible" transactions are likely to increase again. It will not be possible for the investment income account to improve as markedly as hitherto once special influences of the kind described cease to play a role. Moreover, the deficits on foreign travel will increase again as "mass income" goes up, and the payments to the EEC will probably also grow. To offset these burdens, Germany must basically aim at rising trade surpluses, if the current account is not to move into deficit.

Halving of net long-term capital exports

While, as mentioned, the balance on current account was strongly influenced by short-term exchange rate movements, the reactions in the field of long-term capital transactions were much less obvious. Despite the generally weak trend of the Deutsche Mark during 1983, net long-term capital exports halved compared with a year previously (to only DM 7.5 billion), considerably improving the structure of Germany's balance of payments. At DM 10 billion, "autonomous" net capital exports (those which are largely independent in the short run of interest rate and exchange rate considerations) for the purpose of direct investment and of bilateral and multilateral development aid loans were admittedly about as large as a year earlier, but a small surplus in favour of Germany was recorded on balance in 1983 in the other sectors of long-term capital transactions, after considerable outflows had been registered here in the preceding

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1 In accordance with international practice when drawing up balances of payments, but in contrast to the official German foreign trade statistics, imports as well as exports are recorded here at their value at the border of the foreign exporting country (f.o.b. value). The freight and insurance costs payable on imports are ascribed to services, so that the overall balance on current account is not affected by this change. On an f.o.b./c.i.f. basis, i. e. according to the official foreign trade statistics, the trade surplus (which is smaller for methodological reasons) fell from DM 51.3 billion in 1982 to DM 42 billion in 1983.

year. This reversal was not so much due to the movement of interest rates (taking the average of 1983, the interest rate differential vis-à-vis the United States decreased only slightly) or to the actual course of the exchange rate of the Deutsche Mark, although a certain parallelism between Deutsche Mark depreciation and capital exports is discernible in particular months. It seems, rather, as if long-term capital movements are crucially influenced by a change in exchange rate expectations. In the course of 1983, with the dollar rising, the exchange risk of dollar assets was obviously rated higher, so that the interest rate disadvantage of Deutsche Mark assets was less significant. It is striking, at all events, that inflows of long-term funds predominated in the second half of 1983, when the rate of the dollar was distinctly higher than in the first half of the year, whereas previously long-term capital had been exported on a considerable scale.

Restrictions on capital exports counterproductive

This process of a gradual reappraisal of currency positions by domestic and foreign investors would certainly have been greatly disrupted, if not prevented altogether, if the German authorities had followed the suggestions occasionally made in some quarters to the effect that administrative restrictions should be imposed on capital exports. Even the slightest hint of interventions in the field of capital transactions with a view to making it more difficult to move out of the Deutsche Mark would have impaired confidence in the German currency and would in some cases have deterred non-residents from placing as many funds in Germany as they actually did.

Substantial foreign purchases of German bonds and public sector borrowers' notes

Non-residents showed particular interest in German bonds, and since August 1983 they have acquired unprecedented amounts of such paper. Especially in this field, the interest rate disadvantage as compared with dollar assets was obviously more than offset by expectations of an appreciation of the Deutsche Mark in the longer run, indicating that foreign confidence in the Deutsche Mark as an investment currency was unbroken despite the weak tendency of the Deutsche Mark at the time. In 1983 foreign investors acquired, in addition to German bonds (DM 10.8 billion), a somewhat larger amount of long-term borrowers' notes of the Federal and Länder Governments (DM 12.1 billion compared with DM 9.2 billion in 1982). The great bulk of these capital imports took the form of purchases of borrowers' notes from the banks' holdings, rather than direct borrowing abroad by public authorities, which is no longer necessary in external economic terms when the current account is in surplus. This is also the main reason why public sector liabilities arising from the borrowers' note loans of OPEC countries (the Federal Government had raised substantial direct loans of this type in 1980–81) decreased slightly for the first time last year. By contrast, investors from European industrial countries, whose balance of payments situation continued to improve in 1983, bought more such Deutsche Mark paper last year. The purchases of bonds and public sector borrowers' notes were, however, partly at the expense of the direct investment of long-term funds with German banks. The banks' external liabilities arising from deposits and borrowers' notes therefore decreased (by DM 1.7 billion) in the course of last year, much as in 1982.

Constant level of capital outflows in the private sector

While foreigners stepped up their long-term investment in Germany, private capital exports through purchases of foreign bonds and through bank lending to non-residents last year, at DM 21 billion,[1] were roughly at the level of the preceding year (DM 19.5 billion). In 1983 residents acquired an unprecedented amount (DM 4.6 billion) of foreign shares, which seemed attractive on account of the world-wide bull market in shares. At the same time, however, interest in foreign currency bonds issued by non-residents slackened markedly; last year investment in such paper (mainly dollar bonds), at DM 5.3 billion net, was only

1 Adjusted for the repayment of "Carter Notes" by the U.S. Treasury.

half as large as in 1982. In view of the high exchange rate of the dollar and the greater share of dollar assets in the portfolios of private and institutional investors, German investors, too, were obviously paying more attention to the exchange risk in the case of dollar bonds, whereas in the case of investments in U.S. shares the possibility of price gains on the stock exchange was the prime consideration.

Banks more cautious in their lending operations

The rather sluggish expansion of banks' long-term external lending suggests that the banks were very slow to extend new external loans because of the greater risks in this field of business. It is true that the long-term external assets of the banks rose by DM 8.5 billion (net) in the course of last year and thus somewhat more than in 1982 (DM 6.25 billion),[1] but this rise was determined not so much by an increase in new lending business as by the decline in repayments. Under some rescheduling agreements, due redemptions were postponed, so that, despite the decline in new lending business against 1982, the overall level of international lending rose sharply, albeit "involuntarily" in some cases.

Short-term capital movements determined by exchange rate tensions in the EMS

Unlike long-term capital transactions, short-term capital movements in 1983 were characterised by sharp fluctuations, especially in connection with exchange rate tensions in the EMS. Prior to the realignment in March, substantial short-term funds flowed into Germany, primarily through the banks. During the first quarter, net short-term capital imports, i.e. after deducting the funds that had flowed out again by the end of March, amounted to just over DM 15 billion (including the balancing item of the balance of payments). This period of foreign exchange inflows, which were accompanied by correspondingly substantial interventions, was followed by a period of outflows lasting virtually until the end of the year and resulting in net capital exports totalling DM 22 billion. This massive reversal in short-term capital movements was mainly due to the fact that, after the realignment in the EMS (which had brought a substantial revaluation of the Deutsche Mark), there was no longer an imminent risk of an appreciation of the Deutsche Mark, so that short-term Deutsche Mark borrowing became attractive again in EMS countries in which interest rates were much higher than in Germany (or in the Euro-DM market). But the outflow of short-term funds from Germany seems to have owed something not only to these fluctuations in the short-term Deutsche Mark position of other countries but also to the fact that the Euro-DM market hardly expanded at all in the course of last year. During 1983, the volume of short-term Deutsche Mark loans raised by German firms in the Euro-market thus declined, for the first time since 1979. Moreover, in contrast to a year earlier, just over DM 6 billion (net) flowed from enterprises in the form of trade credits since export claims grew at a faster pace as export business picked up during the second half of the year, while no additional advance payments were received because of the decline in orders for large-scale projects and foreign construction work.

Little change in overall monetary reserves

The net external assets of the Bundesbank hardly changed at all on balance in 1983; at the end of the year they were, as mentioned, about DM 1.5 billion smaller than at the beginning of the year, calculated at current balance sheet rates. In the course of the year, to be sure, the movement in the monetary reserves varied, depending on the situation prevailing on the exchange market, especially in the EMS, as explained elsewhere in this Report (see p. 67); but over the year inflows and outflows of foreign exchange almost cancelled out in the external position of the Bundesbank. At the end of 1983, therefore, the Bundesbank's dollar holdings, which continue to be valued at DM 1.73 per U.S. dollar, were almost as large as at the beginning of the year. While the share of dollar assets (excluding the dollars provisionally contributed to the European

1 Adjusted for the repayment of "Carter Notes" by the U.S. Treasury.

Monetary Cooperation Fund [EMCF]) in the gross monetary reserves hardly changed at all in the course of last year, the share of claims on the International Monetary Fund (IMF), i.e. the reserve position in the IMF and special drawing rights, increased appreciably (namely from 14½ % to just under 18 %) owing to Deutsche Mark drawings by the IMF. A further increase in Fund-related Bundesbank assets is to be expected in view of the assistance programmes agreed by the IMF with major debtor countries and the greatly enlarged access of the Fund to refinancing facilities, which — as far as the German share is concerned — have to be provided by the Bundesbank. By contrast, the claims of the Bundesbank on the EMCF at the end of 1983 made up a correspondingly smaller part of the gross monetary reserves (19 %) than at the beginning of the year (23 %).[1] Recently, however, these reserve assets, which normally can be used only within the EMS, have increased considerably again in connection with the exchange rate tensions in the EMS. Besides, in view of the turnaround in the dollar rate the Bundesbank did not sell on the exchange market all the dollars it received from outside the market (such as interest receipts), so that the net external assets, valued at balance sheet rates, increased by about DM 6 billion during the first quarter of this year.

4. Monetary policy remains on a steadying course

(a) Monetary target for 1983 and money market management during the year; monetary target for 1984

Monetary target for 1983

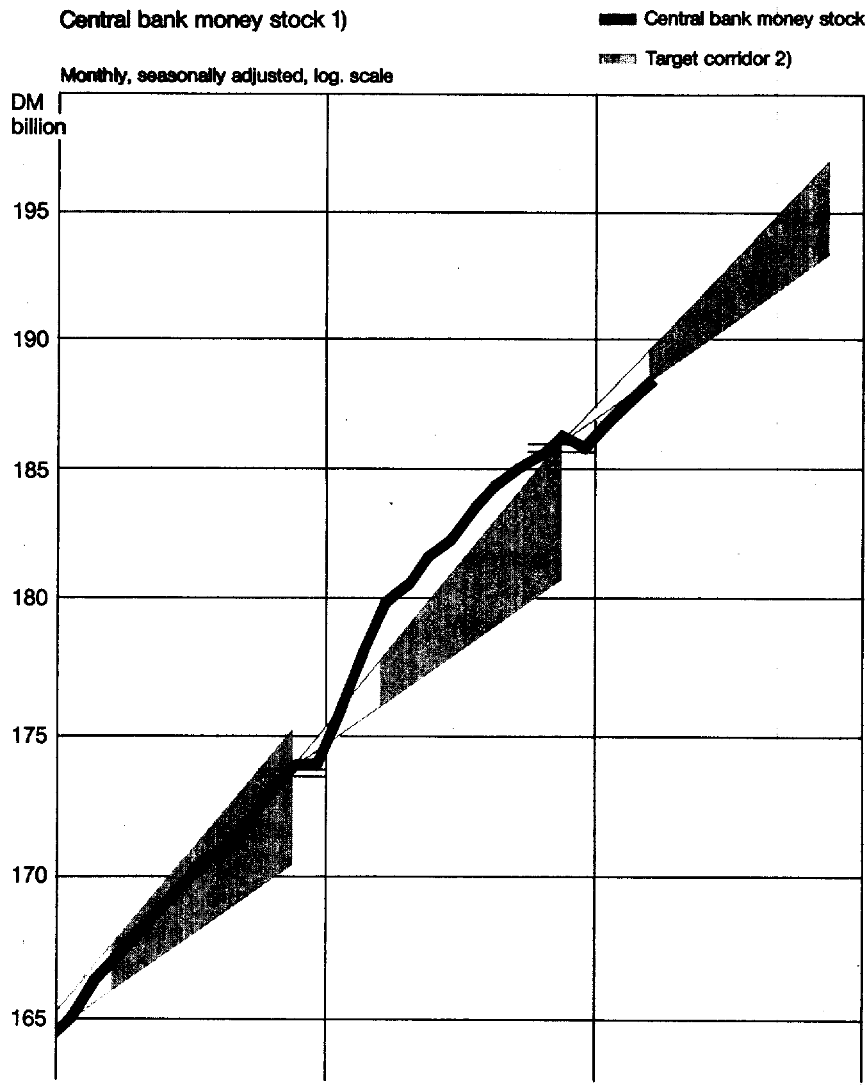
The objective of monetary policy last year was to provide scope for the economic recovery while further promoting stability. The Bundesbank made this objective clear when setting the monetary target for 1983, which — as in 1982 — provided for the central bank money stock to rise within a range of 4 to 7 % in the course of the year. The Bank indicated that as long as the low level of economic activity remained among the foremost economic problems, and as price and cost trends and the external position permitted, it intended to allow monetary expansion to continue in the upper half of the target range, just as in 1982.

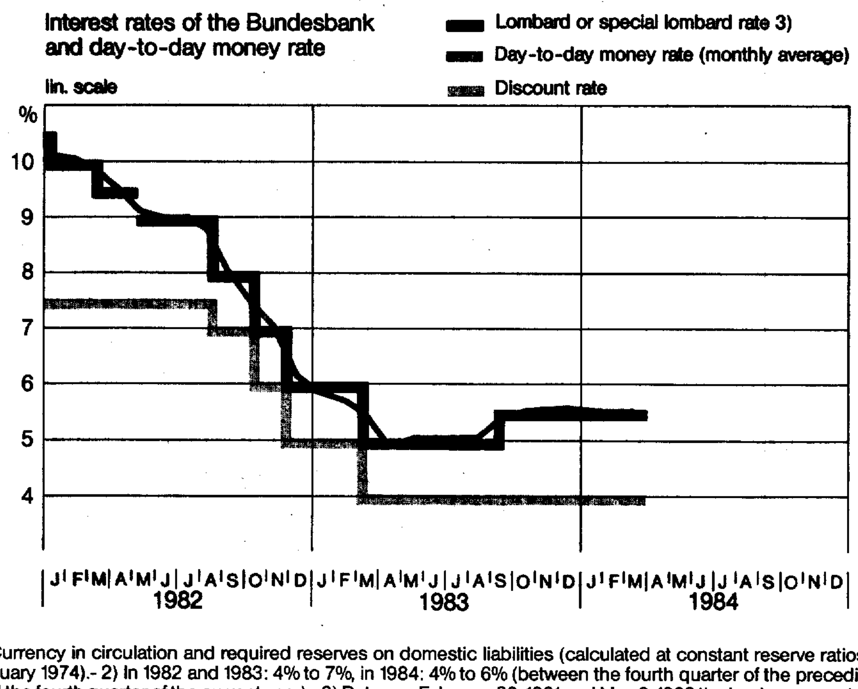
Ample supply of liquidity up to the spring

Around the turn of 1982–83 the Bundesbank, in line with its stated objectives, sought to ease financing conditions in the economy further, if at all possible. There were signs of a domestic upswing starting at the end of 1982, but it also became evident that the economy would have to do without any major external demand stimuli, in contrast to the situation in earlier recoveries. Price prospects seemed favourable and the Deutsche Mark was firm on the foreign exchange markets. In the circumstances the Bundesbank encouraged a further relaxation of conditions in the money market in the first few months of the year. Mid-February saw massive inflows of foreign exchange from EMS countries, which led to an unwelcome increase in bank liquidity as the year went on. This acted for a time as an additional spur to the fall in domestic interest rates. In the light of this situation, the Central Bank Council decided to lower the discount and lombard rates by another full percentage point each to 4 % and 5 % respectively in the second half of March and also to cut the banks' rediscount quotas by DM 5 billion at the beginning of April. In order to regain control over bank liquidity as soon as possible the Bundesbank thus reversed an increase in rediscount quotas of about the same amount made in February. This also seemed appropriate because — owing partly to special factors — in the first quarter of 1983 the central bank money stock increased at a fairly rapid rate.

1 After taking account of the difference between the ECU value and the book value of the reserves provisionally contributed.

Growth of the central bank money stock and movement of interest rates





1) Currency in circulation and required reserves on domestic liabilities (calculated at constant reserve ratios, base: January 1974).- 2) In 1982 and 1983: 4% to 7%, in 1984: 4% to 6% (between the fourth quarter of the preceding year and the fourth quarter of the current year).- 3) Between February 20, 1981 and May 6, 1982 the banks were not granted lombard loans at the lombard rate (during that period the Bundesbank granted the banks special lombard loans at a special rate as and when required).

Limits to monetary relaxation reached

The package of measures adopted in March 1983 reached the limits prevailing in the circumstances to the relaxation of monetary policy. This was shown inter alia by the movement of interest rates, as only short-term money market rates and lending rates responded to the cut in the central bank rates. Longer-term money market rates and yields in the capital market went up after the reduction in central bank rates and the realignment in the EMS which immediately followed it. Several factors combined to bring this about: no further foreign exchange inflows were in prospect after the realignment; on the contrary, there were soon sizable outflows of funds from Germany; in addition, interest rates in the United States started to move upwards again in May, encouraging capital outflows, while the Deutsche Mark weakened against most major currencies.

Cautious countermeasures by liquidity policy

The foreign exchange outflows after the realignment in the EMS and the cut in rediscount quotas as from the beginning of April caused bank liquidity to fall in the spring to a level which seemed consistent with the desired expansion of the money stock. This fall was slowed down somewhat, however, by the fact that the large Bundesbank profit (DM 11 billion) transferred in April 1983 was disbursed immediately in cash transactions. In the early summer the Bundesbank tightened its liquidity policy stance in the money market somewhat more. This seemed advisable because the growth of the central bank money stock continued at a rate above the target corridor, while there were signs that the hoped-for economic recovery was turning out to be stronger than had been expected. Following its regular review of the target in mid-year, when the central bank money stock was expanding at an annual rate of some 9% against the fourth quarter of 1982, the Bundesbank explicitly reaffirmed its monetary target and also indicated that it considered it possible to meet the target up to the end of the year.

Interest rate policy adjustment in the autumn

In the ensuing period, which extended well into the summer, the liquidity policy measures were designed to make the banking system rely rather more heavily on lombard loans. The slight reduction in liquidity and the unfavourable interest and exchange rate expectations for the Deutsche Mark finally caused money market rates to part company with central bank interest rates and tend to rise. By increasing the lombard rate from 5% to 5½% at the beginning of September the Bundesbank signalled that it was responding to overall monetary developments. The raising of the rate obviously strengthened confidence and enhanced expectations in the financial and foreign exchange markets. Market rates eased for some while and the Deutsche Mark tended to firm. In combination with the more cautious stance of liquidity policy and the market-induced upturn in interest rates since the spring, the slight lifting of the lombard rate also helped to significantly restrain the increase in the central bank money stock from the beginning of the autumn. At 7%, its growth rate between the fourth quarter of 1982 and the fourth quarter of 1983 was within the 1983 target corridor, after having been considerably faster at times.

Monetary target for 1984

Around the turn of 1983–84 the task facing economic policy in the immediate future was how to safeguard and, if possible, extend the progress made towards stabilisation in the face of the continuing economic recovery. These objectives are not at variance with hopes of further economic growth but are, rather, aimed precisely at steadying such growth and safeguarding it by a high degree of monetary stability. Only in a non-inflationary environment can demand and production grow without harsh anti-inflation measures having to be adopted sooner or later, which no country can avoid if stability is seriously jeopardised or has been lost. For 1984, therefore, the Bundesbank set a growth target for the central bank money stock which is acceptable in the medium term: in December 1983 the Central Bank Council decided to keep the growth of the central bank money stock within a somewhat narrower target corridor in 1984. When calculating the target an average annual expansion in

The monetary targets and their implementation

%

Year	Target: growth of the central bank money stock			Actual growth (rounded figures)	
	in the course of the year 1	on an annual average	Concretising of target in the course of the year	in the course of the year 1	on an annual average
1975	8	—	.	10	—
1976	—	8	.	—	9
1977	—	8	.	—	9
1978	—	8	.	—	11
1979	6—9	—	Lower limit	6	—
1980	5—8	—	Lower limit	5	—
1981	4—7	—	Lower half	4	—
1982	4—7	—	Upper half	6	—
1983	4—7	—	Upper half	7	—
1984	4—6	—	.	—	—

1 Between the fourth quarter of the preceding year and the fourth quarter of the current year; 1975: December 1974 to December 1975.

overall production potential of about 2% in 1984 was assumed. In addition, allowance was made for an "unavoidable" price increase of some 3%. These growth rates resulted in an expansion of some 5% in the central bank money stock both on an annual average in 1984 and in the course of the year, i. e. the four-quarter time period which the Bundesbank uses to define its monetary target. The target corridor was reduced to ±1 percentage point around its midway point and the official monetary target was defined as a growth of 4 to 6% in the central bank money stock between the fourth quarter of 1983 and the fourth quarter of 1984. When deriving the new target corridor the Bundesbank took account of the fact that a relatively high basic level was reached last year. This will help to meet part of the demand for money in 1984. Growth of overall production in 1984 will in all probability outpace the rise in production potential. The derivation of the monetary target was therefore also based in part on the assumption of higher capacity utilisation.

Large profit transfers may place a burden on monetary policy

The new target period opened comparatively smoothly in 1984, especially as special factors had very little impact on monetary developments in the first few months of this year, in contrast to a year earlier. The Federal Government has agreed to the Bundesbank profit being transferred in instalments this year, with the first instalment (DM 5 billion) being made in April and further monthly instalments of DM 1.5 billion each between May and August. This arrangement is to be retained in the future whenever similar conditions prevail. Hitherto it has been necessary to produce in the money market, immediately before the transfer, an adequate "liquidity shortage" which was then offset as the profit transferred was soon used for cash transactions. Transferring the profit in instalments facilitates money market management and reduces the sudden increases in bank liquidity associated with the old system, and there is no need for the Bundesbank to adjust the assistance it gives to the banks in advance to the sudden spate of liquid funds. Nevertheless, spreading out the profit transfer does not rule out the possibility of a conflict between the Bundesbank's monetary functions and the monetary consequences of transferring a large Bundesbank profit to the government. Such a conflict could arise in particular if the transfer is made at a time when the Bundesbank has to provide additional central bank balances for other reasons, as was the case in spring 1983, when there was a heavy flow of foreign exchange into the Bundesbank within the European Monetary System, which added to bank liquidity and tended also to increase the money in the hands of non-banks.

(b) Recent experience with the central bank money stock as a monetary indicator and intermediate target

Unusually rapid currency growth at the beginning of the year

Owing to a number of special influences affecting monetary growth, the Bundesbank found it more difficult in 1983 than in the preceding years to influence interest rates and liquidity in the money market at an early date so as to bring them into line with its monetary target. It was only after some while that the underlying longer-term monetary trend became clearly evident. In the first few months of last year the sharp acceleration in monetary growth seemed at first to be partly caused by reversible special factors. There was an unusually rapid rise in currency in circulation as — presumably for speculative reasons — more Deutsche Mark notes were held outside Germany as well. This was suggested in particular by the slower reflux of notes from abroad and the very strong demand at times for Deutsche Mark notes in high denominations. When the Deutsche Mark came under persistent pressure from the spring onwards, however, the sustained rise in currency in circulation in the further course of the year had to be ascribed largely to domestic influences. While, taking the average of the last five years, currency in circulation has not grown faster than the gross national product, in 1983, when currency in circulation expanded by 8½ %, the currency ratio climbed fractionally. Cash payments apparently increased more than overall turnover. Since 1975 there have been signs that the "secular" trend towards a decrease in the currency ratio in the wake of the expansion of cashless payments has come to an end. One reason for this may be that transactions in the underground economy, which are usually settled in cash, have increased further.

Reserve-carrying deposits also accelerate sharply

The "reserve component" of the central bank money stock (i. e. required minimum reserves on domestic liabilities, calculated at constant reserve ratios) also expanded strongly at the beginning of last year's target period. On several occasions the growth of reserve-carrying deposits was stimulated by disruptive influences, the significance of which was not always fully recognised until afterwards. Thus, not only did the banks' central bank balances increase owing to speculation, before the EMS realignment, on a revaluation of the Deutsche Mark but so did — to an extent which is hard to assess — the money in the hands of non-banks, which is mostly held in non-cash forms. Unusually large amounts of bonus-carrying savings deposits, which were released at the beginning of the year and were only sluggishly reinvested at longer term or used for consumption, also contributed to the acceleration of monetary growth. Finally, the large transfer of Bundesbank profit to the Federal Government in April, which, if used for cash transactions, has an expansionary effect on the money supply, like government borrowing from the central bank, likewise tended to enlarge the money stock. During this period the Bundesbank was practically forced to provide the banks, on reasonable terms, with central bank balances to accommodate the rise in minimum reserve requirements associated with the temporary surge in reserve-carrying deposits. If the Bundesbank — as it was urged, particularly by those who had considered the target for monetary growth in 1983 to be too lax — had "refused" to provide adequate liquidity, in order to keep the growth of the central bank money stock strictly on target, this might have caused disruptions in the financial markets which would have been incompatible with the envisaged longer-term basic orientation of monetary policy. In 1983 — as also on earlier occasions — the Bundesbank therefore refrained from taking any abrupt action to counter potentially reversible special movements in monetary growth.

Special influences disappear in the second quarter

In the second quarter the special influences faded out, as expected. After the realignment, funds flowed out of the country, and some of the savings deposits released at the beginning of the year were used to acquire more longer-term financial assets. When this period of "self-correction" came to an end in mid-

Monetary developments

Change during year 1

Item	1977	1978	1979	1980	1981	1982	1983
	DM billion						
A. Central bank money requirements of banks and liquidity policy measures of the Bundesbank 2							
1. Provision (+) or absorption (−) of central bank balances by							
Change in central bank money 3 (increase: −)	−10.9	11 −14.1	− 7.8	− 6.5	− 2.7	− 7.5	− 10.1
Foreign exchange movements (excluding foreign exchange swaps and foreign exchange transactions under repurchase agreements)	+ 8.4	+ 20.3	− 5.2	− 24.6	− 3.1	+ 1.7	− 2.4
Cash transactions of the central and regional authorities (excluding shifts of Federal balances under section 17 of the Bundesbank Act)	+ 5.0	− 2.1	+ 3.9	+ 0.3	+ 1.1	− 4.1	+ 1.7
Transfer of the Bundesbank's profit to the Federal Government	−	−	−	−	+ 2.3	+ 10.5	+ 11.0
Other factors	− 4.5	− 3.8	− 5.2	− 7.9	− 9.4	− 12.1	− 9.2
Total 1	− 2.1	+ 0.3	− 14.3	− 38.8	− 11.8	− 11.4	− 9.0
2. Liquidity policy measures							
Change in minimum reserves	+ 8.2	− 1.8	− 3.2	+ 10.5	+ 4.1	+ 5.4	− 0.2
Change in refinancing facilities	+ 6.5	+ 4.4	+ 5.1	+ 12.1	+ 5.1	+ 7.7	− 0.7
Open market transactions (with non-banks, in "N paper" and in long-term securities)	− 0.7	− 3.6	+ 2.7	+ 4.5	− 0.1	+ 1.5	+ 2.4
Reversible assistance measures 4	−	−	− 2.3	+ 10.5	+ 3.9	+ 0.2	+ 3.3
Total 2	+14.0	− 1.1	+ 2.4	+ 37.6	+ 13.0	+ 14.8	+ 4.7
3. Remaining deficit (−) or surplus (+) (1 plus 2)	+11.9	− 0.8	− 11.9	− 1.2	+ 1.2	+ 3.4	− 4.3
covered or absorbed by							
Recourse to unused refinancing facilities (reduction: +)	− 5.5	− 0.2	+ 9.7	− 1.4	+ 1.3	− 3.5	+ 3.3
Raising (+) or repayment (−) of lombard or special lombard loans	− 6.5	+ 1.0	+ 2.2	+ 2.6	− 2.5	+ 0.1	+ 1.0
	%						
B. Key monetary indicators							
Central bank money stock 2, 5	+ 9.8	11 + 11.9	+ 5.5	+ 5.5	+ 3.1	+ 5.9	+ 6.8
Memorandum item							
As an annual average	+ 9.0	11 + 11.4	11 + 9.0	+ 4.8	+ 4.4	+ 4.9	+ 7.3
M1 (= currency in circulation and sight deposits)	+11.2	+ 14.3	+ 3.8	+ 4.4	− 0.8	+ 6.7	+ 8.2
M2 (= M1 plus time deposits for less than 4 years)	+11.1	+ 13.4	+ 8.4	+ 9.3	+ 9.0	+ 5.2	+ 2.6
M3 (= M2 plus savings deposits at statutory notice)	+11.2	+ 11.1	+ 5.8	+ 6.3	+ 5.0	+ 7.3	+ 5.9
Lending by banks and the Bundesbank to domestic non-banks	+ 9.4	+ 11.5	+ 11.5	+ 9.4	+ 8.9	+ 6.5	+ 6.7
	DM billion						
C. Money stock and its counterparts							
Money stock M3 (= 1 plus 2 less 3 less 4 less 5)	+58.9	+ 64.8	+ 39.2	+ 42.8	+ 36.1	+ 54.8	+ 45.3
Counterparts in the balance sheet							
1. Volume of credit 6	+94.2	+125.4	+139.0	+126.3	+132.0	+104.4	+113.2
of which							
Bank lending to domestic non-banks	+95.8	+122.6	+140.9	+122.4	+129.9	+106.1	+111.3
− to enterprises and individuals 7	+42.3	+ 49.0	+ 67.5	+ 56.3	+ 41.7	+ 30.0	+ 44.0
− to the housing sector 8	+26.8	+ 38.9	+ 44.8	+ 44.5	+ 40.7	+ 36.1	+ 48.0
− to public authorities	+26.7	+ 34.7	+ 28.5	+ 21.6	+ 47.5	+ 40.0	+ 19.3
2. Net external assets 9	+10.1	+ 7.1	− 21.8	− 10.6	+ 11.9	+ 4.5	+ 1.2
3. Monetary capital	+42.9	+ 54.8	+ 75.8	+ 61.7	+ 86.0	+ 46.5	+ 67.1
of which							
Savings deposits at agreed notice	+ 0.8	+ 7.7	+ 3.3	− 1.9	− 2.1	+ 4.3	− 2.0
Bank savings bonds	+13.4	+ 10.3	+ 14.8	+ 17.8	+ 14.0	+ 11.9	+ 13.0
Time deposits for 4 years and over	+13.6	+ 17.0	+ 18.7	+ 14.6	+ 13.8	+ 7.2	+ 27.2
Bank bonds outstanding 10	+ 9.7	+ 14.2	+ 33.6	+ 26.7	+ 53.6	+ 14.1	+ 22.6
4. Central bank deposits of domestic public authorities	− 0.8	+ 2.5	− 1.7	− 1.9	− 0.2	+ 0.5	+ 0.9
5. Other factors	+ 3.3	+ 10.4	+ 3.8	+ 13.2	+ 22.0	+ 7.2	+ 1.0

1 Unless otherwise indicated, based on end-of-month figures. — **2** Based on daily averages of the last month of the period and the last month of the previous period, respectively. — **3** Currency in circulation (as from March 1978 excluding the banks' cash balances of domestic notes and coins, which are deductible from the required minimum reserves) and required reserves on the banks' domestic liabilities at current reserve ratios; changes in the required reserves resulting from changes in the reserve ratios are shown in item A2. — **4** Open market transactions under repurchase agreements in bills and securities, foreign exchange swaps and foreign exchange transactions under repurchase agreements, and shifts of Federal balances under section 17 of the Bundesbank Act. — **5** Reserve component calculated at constant reserve ratios (base: January 1974). — **6** Banks and the Bundesbank; including credit based on the purchase of securities. — **7** Excluding housing. — **8** Excluding credit based on the purchase of securities. — **9** Banks and the Bundesbank. — **10** Excluding bank holdings. — **11** The statistical break caused by the redefinition of the central bank money stock (see footnote 3) has been eliminated.
Discrepancies in the totals are due to rounding.

year, monetary expansion remained fairly strong at first. But in view of the progressive revival in domestic demand, which had been buttressed by the expansionary basic stance of monetary policy since the autumn of 1981, there was a growing risk of the money supply in the economy becoming too large in the longer run. In the ensuing period the Bundesbank therefore sought to curb monetary growth somewhat so as to create monetary conditions conducive to non-inflationary, sustained economic growth, in addition to achieving the monetary target for 1983.

Monetary growth on potential path in the second half of the year

As overall monetary growth began to slacken in the second half of 1983 this objective was achieved with some delay. Although the initial differences in the rates of growth of currency in circulation and the minimum reserve component were not fully offset over the year as a whole, this did not fundamentally call in question the suitability of the central bank money stock as an indicator of and intermediate target for monetary policy. This impression is confirmed if the broadly defined money stock M3 is used as a supplementary criterion. Last year M3 showed comparable fluctuations in growth, and over 1983 as a whole it expanded almost as strongly as the Bundesbank's key monetary indicator.

Decreasing uncertainty permits narrowing of the corridor

In view of the uncertainties prevailing at the beginning of each target period it has seemed advisable in the past few years to allow monetary policy some discretionary room for manoeuvre in the shape of a target corridor of 3 percentage points. This was intended to give the Bundesbank some scope for responding to unexpected developments in economic activity, prices and exchange rates in the course of the year without it having to abandon the basic principles of a monetary policy geared to longer-term objectives. At the latest starting point at the turn of 1983–84, the uncertainties about general economic trends and price movements in the foreseeable future seemed, however, less marked, so that the target corridor for 1984 could be narrowed from 3 to 2 percentage points. A margin of uncertainty of about 2 percentage points is needed, if only because of the short-term irregularities in the functioning of the financial markets, which have to be taken into account in current monetary targeting.[1]

(c) Strong monetary expansion

Volatile influences affect the money creation process

Like the central bank money stock, overall money in the hands of domestic non-banks expanded strongly in the course of last year, though at a varying pace. With economic recovery getting under way at the turn of 1982–83 and the fall in interest rates continuing until the spring of 1983, bank lending to domestic enterprises and individuals became a much more important determinant in the first half of 1983; public sector borrowing from domestic banks also remained at a very high level at first. This pointed to a sharp upturn in monetary growth from the outset. Moreover, monetary expansion was stimulated in the first few months of the year by the special influences described in detail in the previous section. As some of these factors had corrected themselves by mid-year, the rapid underlying pace of monetary expansion was somewhat obscured at times. The rise in interest rates at the longer end of the financial markets between the spring and autumn increased investors' propensity to reduce their cash holdings in favour of higher-yielding but less liquid assets later in the year; this tended to curb monetary growth. In addition, public authorities needed fewer bank credits from mid-year onwards as they made more headway in budget consolidation. Under the impact of these restraining factors the pace of monetary growth slackened as from the late summer. In December 1983 the

1 In the chart showing the monetary target for 1984 (and retrospectively for 1982 and 1983) the target corridor has not been shown in colour up to March as the growth of the central bank money stock is normally subject to large random fluctuations around the turn of the year. According to calculations made by the Bundesbank, from the spring onwards the average random deviation from trend does not exceed the width of the corridor.

money in the hands of domestic non-banks in the broad definition M3[1] exceeded its level of December 1982 by 6% or DM 45 billion. It thus expanded strongly, but slightly less than overall bank lending to domestic non-banks and also not quite as fast as the central bank money stock.[2] At the beginning of 1984, too, monetary growth was on an acceptable scale.

Diverging trends of the individual money stock components

Last year the trends of the individual money stock components largely followed a pattern that is typical of periods with low deposit rates. The fall in bank deposit rates which had started in the autumn of 1981 continued until the spring of 1983. Thereafter savings rates (apart from bonus payments) remained unchanged at the level they had reached, which was low even by historical standards (the rate applying to savings deposits at statutory notice was 3%). Short-term time deposit rates firmed slightly as interest rates went up in the money market in the course of the year, but they did not regain the level of the end of 1982. Because of their unattractive yields, shorter-term time deposits and borrowed funds were run down noticeably in the first half of the year, whereas sizable amounts initially continued to flow into savings accounts at statutory notice, which traditionally bear low interest and which had registered an unusually large inflow of released bonus-carrying savings at the beginning of 1983. Sight deposits, which bear practically no interest at all, and currency in circulation rose rapidly; in view of the lower interest rate level, the opportunity cost of holding money in this most liquid form was not rated as high as before. Altogether, 1983 saw a further increase in cash and quasi-money holdings in the economy, in spite of the strong and sustained economic recovery. Owing to the diverging trends of the individual money stock components, the money stock in the narrowest definition M1 grew at a distinctly faster pace, at just over 8%, and the money stock M2, at 2½%, at a slower pace, than the overall money stock M3 (which went up by 6%, as mentioned).

Strong reaction of monetary capital formation to rising interest rates

Unlike the rates paid on shorter-term bank deposits, the rates paid on long-term bank liabilities were raised quite sharply after the turnaround in the movement of interest rates last spring. Some bank bonds and bank savings bonds, for example, yielded over 1 percentage point more in the autumn than in the spring of last year. Encouraged by this upturn in long-term rates, households saved a growing proportion of their income towards the end of the year, giving clear preference to longer-term assets over liquid ones. The larger inflow of longer-term savings provided a sound basis for financing the heavier investment activity. Over the year as a whole, monetary capital formation at banks, at DM 67 billion, was almost half as large again as a year before (DM 46 billion). The increase in longer-term monetary capital was thus much steeper than the growth of the broadly defined money stock M3. Long-term time deposits and borrowed funds accounted for the greater part (DM 27 billion) of the longer-term funds accruing to the banks. These also include registered bank bonds, which are taken up mostly by institutional investors, and borrowers' notes issued by banks, which, unlike bearer bonds, need not be written down by purchasers in their balance sheets when interest rates are rising. This is, however, important to institutional investors only. In fact, large amounts of bearer bonds (DM 23 billion) and bank savings bonds (DM 13 billion), too, were sold to domestic non-banks. Short-dated paper was of no great significance in 1983 but the maturities of quite a number of bank bonds were curtailed substantially under special arrangements. The further development of these bank issues — which may serve as surrogates for time deposits — will have to be watched closely in future since any major increase in such bank liabilities, which are not

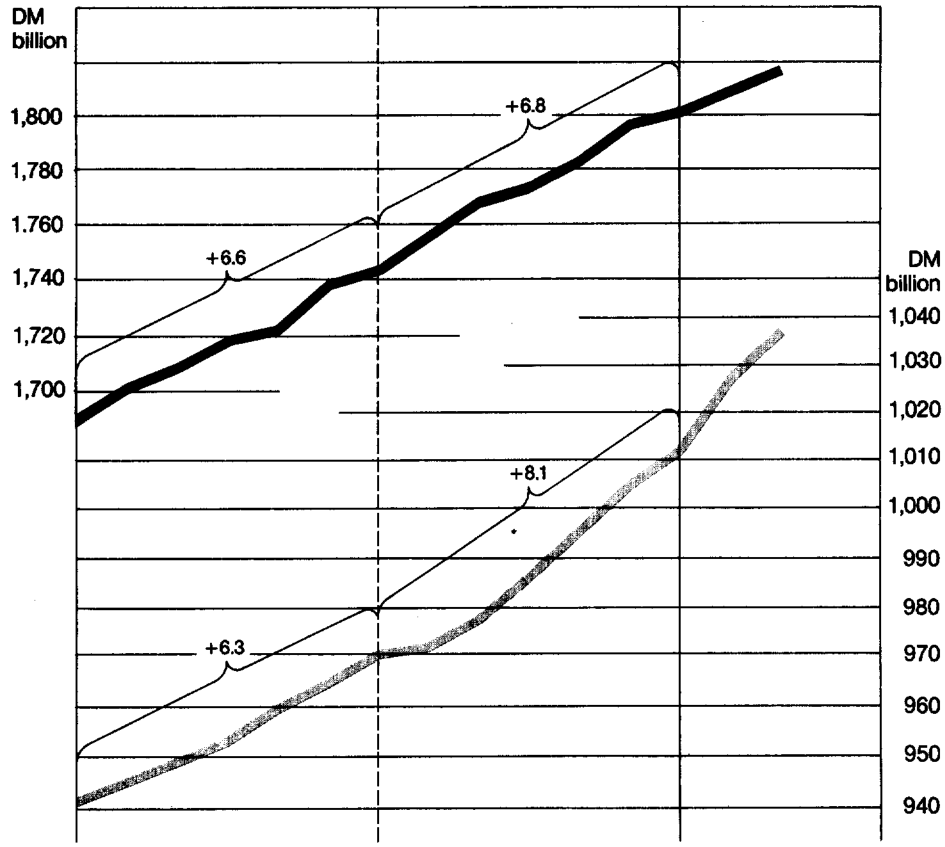
1 The money stock M1 comprises currency and sight deposits; M2 encompasses the aggregate M1 plus time deposits and funds borrowed for less than four years; M3 consists of the aggregate M2 plus savings deposits at statutory notice.

2 The main reason for this is that currency in circulation, which rose more steeply than shorter-term bank deposits, carries greater weight in the central bank money stock than in the money stock M3.

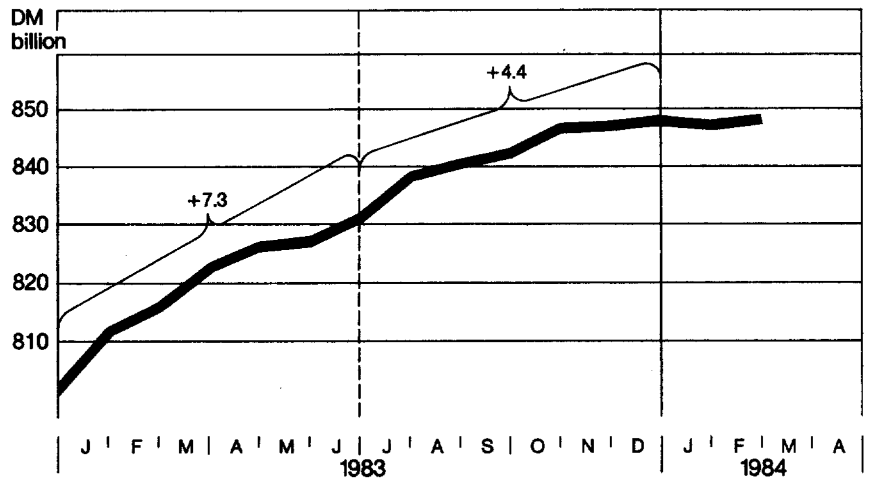
seasonally adjusted; log. scale

Credit expansion
and monetary capital formation

Percentage change, expressed as an annual rate
Lending by the banking system 1) to domestic non-banks
Monetary capital formation 2)



Broadly defined
money stock (M3) 3)



1) Banks and the Bundesbank; including credit based on the purchase of Treasury bills and securities.- 2) Domestic non-banks' longer-term financial assets at banks excluding time deposits and funds borrowed for less than four years and excluding savings deposits at statutory notice.- 3) Currency, sight deposits, time deposits and funds borrowed for less than four years, savings deposits at statutory notice.

subject to minimum reserve requirements, could blunt the minimum reserve tool.

Credit expansion stimulates money creation

As suggested above, the money creation process was given a fairly strong boost by the banks' lending business last year. Outstanding lending by the banking system (including the Bundesbank) to domestic non-banks increased by 6½ %, the same rate as in 1982; in absolute terms it rose by DM 113 billion, against DM 104 billion in 1982. The relative significance of public and private demand for credit changed in a way that should be conducive to the economic recovery. In this connection it should be borne in mind that the increase in the level of bank lending understates new lending to the private sector, as unusually large amounts (some DM 7.5 billion) were written off the banks' domestic loans in the first few months of last year. The slackening of public sector demand for credit was thus accompanied by a "crowding-in" of private credit demand, which, as mentioned (page 16), had a favourable impact on private investment activity. Over the year as a whole the rise in bank lending to the public sector, at 5 % (or DM 21 billion), was only half as steep as in 1982 and, for the first time since 1980, smaller than the increase in bank lending to the private sector. These figures do not fully reflect, however, the Government's actual recourse to the financial markets and its direct contribution to monetary expansion. The profit transfer by the Bundesbank to the Federal Government (of DM 11 billion) tended to increase the money supply, while the productiveness of the bond market enabled the public authorities, notably the Federal Government, to place large issues of securities in the non-bank sector; this was one of the main reasons why those authorities borrowed less from banks than in 1982.

Varying external influences impede monetary management

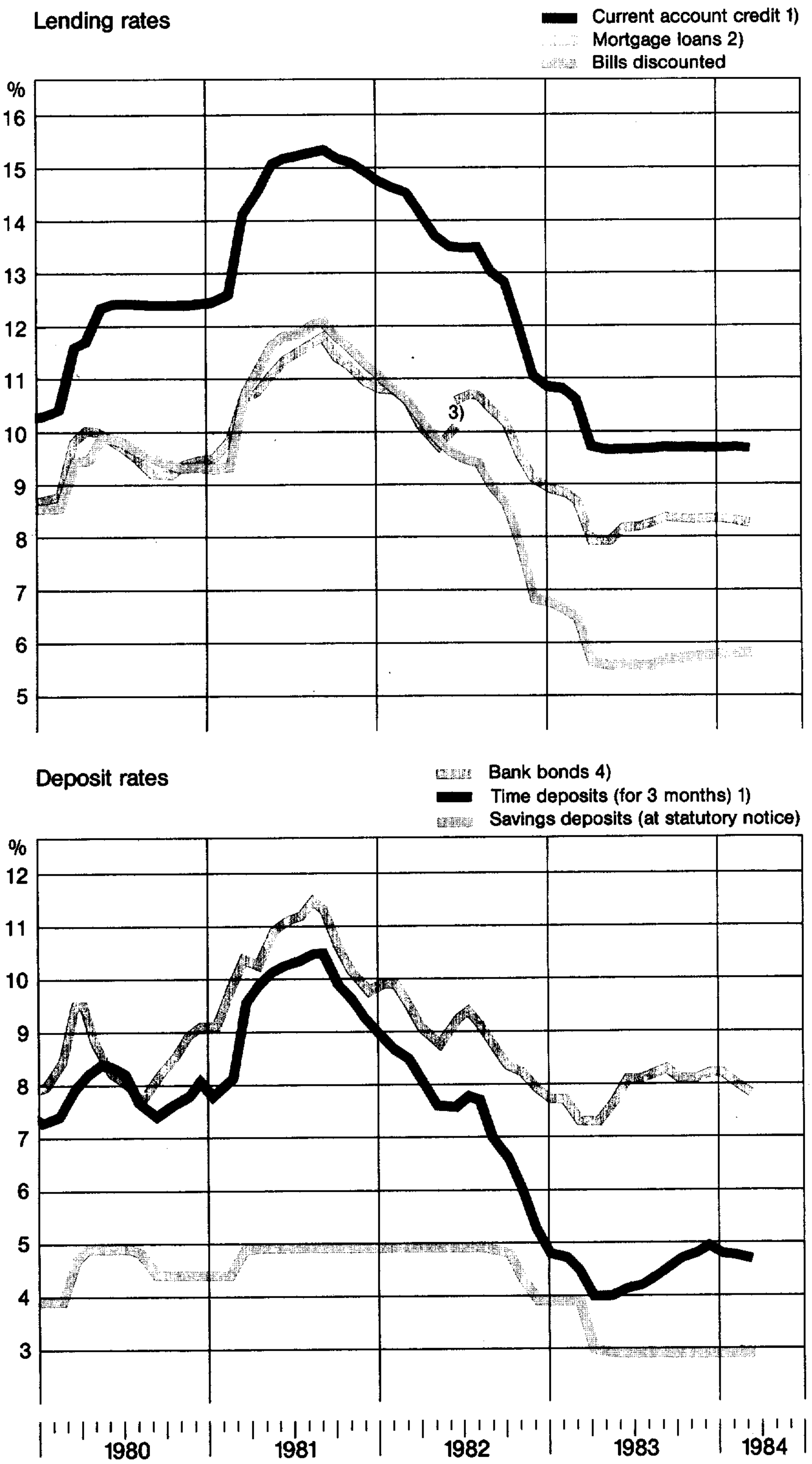
On balance, domestic non-banks' external payments had little effect on domestic money creation in the past year as a whole. In the short run, the net external assets of the banks and the Bundesbank, which mirror the inflows and outflows of funds in non-banks' external current and capital transactions, fluctuated sharply. This sometimes made a forward-looking control of monetary expansion difficult. As mentioned, there were heavy inflows of funds before the realignment in the European Monetary System in March last year, followed by even heavier outflows afterwards. When German interest rates became attractive once more by international standards in the autumn, this produced a tendency for capital to flow in again, which persisted at the beginning of the new year. Until the time this Report went to press, this factor, coupled with the relatively strong current account position, caused the net external assets of the banking system to rise rapidly.

(d) Private demand for credit stronger

Private credit demand revives along a broad front

The banks' lending to enterprises and individuals grew sharply last year in line with the brisker investment activity of the business community and in the housing sector. Domestic banks' lending to the private sector expanded by over 7 % against barely 5½ % in the previous year. But in 1983, in contrast to 1982, the business community did not take up any loans from foreign banks on balance. Lending by domestic banks to private customers picked up along a broad front. In particular, credit demand in the housing sector took off as a result of the fall in interest rates. Here bank lending climbed by 9½ %. Households, too, took advantage of the improved interest rate conditions and financed their rising consumption expenditure more and more through "consumer credits". Bank lending to wage and salary earners rose by 8½ %. The business community expanded its borrowing from banks comparatively moderately, at 5 %, in spite of its growing investment activity. However, enterprises' borrowing is substantially understated in the statistics because of the abovementioned large write-downs and valuation adjustments, which chiefly involved claims on enterprises. Apart from this, enterprises depended less on outside funds last year, as they were able to draw on previously accumulated financial reserves and a large inflow of internal resources, reflecting the improvement in their profitability.

Movement of selected bank interest rates



1) Under DM 1 million.- 2) Secured by residential real estate; effective rate.- 3) As from June 1982 only average interest rate for mortgage loans at variable interest rates: the figures are not fully comparable with previous figures (June 1982 estimated).- 4) Yield on bonds outstanding.

Heavy demand for longer-term loans

Financial consolidation in the enterprise sector progressed further, inasmuch as enterprises — as well as other private debtors — took advantage of the lower interest rates to convert their debt from short-term into long-term. When in spring the fall in lending rates came to a halt and interest rates were at times expected to rise again, the consolidation of shorter-term debt was intensified.

Over the whole of 1983 longer-term direct lending to the private sector increased by 8% and thus considerably more than short-term lending (5%). New commitments for long-term loans developed even more dramatically, which suggests that long-term loans will tend to go on rising, at least in the near future.

Turnaround in interest rates without adverse effects on investment

In the spring of 1983 the decline in bank lending rates that had started in October 1981 ceased. From that date onwards there was virtually no change in the rates for short-term loans. The higher cost of the banks' refinancing through the money market and at the Bundesbank affected, if at all, only special terms applying to specific bank customers. At the end of the year the business community paid on average 1 to 1½ percentage points less interest on short-term bank loans than at end-1982 and about 6 percentage points less than in the autumn of 1981. The cost of longer-term advances, by contrast, increased by ½ to 1 percentage point between spring and autumn 1983, the rise being somewhat greater for credits with fixed interest rates than for those with variable rates. Subsequently, the rates stabilised at the higher level. At the end of the year long-term credits with fixed interest rates cost nearly as much as at end-1982, while the rates on variable-rate mortgage loans were over ½ percentage point lower. In comparison with autumn 1981 the fall in interest rates here was likewise considerable. The present interest rate level does not seem to be an obstacle to the expansion of investment activity that is taking shape quite clearly outside the housing sector.

(e) Business situation and profitability of the banking groups

Banks with long-term business benefit from the credit demand

In 1983, much as in 1982, the strong demand for longer-term loans fostered the balance sheet growth of those banks in which, by tradition, long-term business plays a major role. In the case of banks more heavily engaged in savings deposit business, the expansion of longer-term loans profited additionally from the comparatively attractive margins between the interest on long-term lending and that on shorter-term deposits. The latter took a positive turn after the slight rise in interest rates for longer-term credit, as interest rates on shorter-term deposits went up only a little and savings deposits bore low interest rates. Owing partly to these interest rate trends, but also because of the wide range of customers characteristic of these banks, there was a stronger increase in lending by credit cooperatives (8.2%) and savings banks (6.9%) to domestic non-banks than in lending by all banks. The expansion of lending by mortgage banks (7.2%) as well as by regional and other commercial banks (8%) was likewise above the average. By contrast, the rise in lending by the central giro institutions and the banking groups depending more on the money market, i.e. the central institutions of credit cooperatives and private bankers, was below the average. In contrast to the totality of banks, the big banks' short-term lending to non-banks was very strong, one reason being that enterprises shifted their borrowing from the Euro-markets back to domestic banks last year.

Profitability in banking good, but mixed

In 1983, the banks' profitability was favourable again. As regards the operating result, which does not include the considerable earnings from the banks' own business and the losses in value in lending business, there seems in many cases to have been an improvement over the already high figure for 1982.[1] One of the reasons was that, seen over the year as a whole, the interest rate margin remained fairly wide, although it may have narrowed somewhat in the course of the year. The profitability of many banks continued to be impaired by the need for large write-downs and provisions for loan losses. In particular, banks doing much business with large-scale enterprises or with heavy commitments in for-

1 See "The profitability of German banks in 1982", Monthly Report of the Deutsche Bundesbank, Vol. 35, No. 8, August 1983, p. 13.

eign countries appear to have taken additional precautionary measures. By contrast, the savings banks and credit cooperatives seem to have suffered smaller loan losses. More than any other banks, they were in a position to enlarge their capital and reserves out of internally generated funds. In view of the risks inherent in banking business, a substantial improvement in the banks' capital base is imperative. Moreover, a number of events in 1983 confirm once again the necessity of a better spreading of credit risks in the banking industry. Another urgent problem that is still to be solved is that of improving the prudential averting of danger on the basis of consolidated balance sheets (as has long been called for by the Bundesbank) so as to avoid the multiple use of the liable capital of banks affiliated with each other.

(f) Productive capital market

Financial markets marked by consolidation

In 1983 the domestic financial markets were marked by consolidation. Many borrowers took advantage of the improved market conditions to rectify imbalances in their financial structure; to a growing degree they gave preference to longer-term interest rate commitments. Last year, the longer-term new indebtedness (loans with a period of notice of one year and over) of the domestic non-financial sectors was DM 17 billion higher than in the previous year, whereas in the short-term field borrowing was DM 15 billion lower than in 1982. In line with this, the pattern of financial asset acquisition changed in favour of longer-term types of investment. A major reason for this was the relatively sharp decline in short-term interest rates, which already in 1982 fell distinctly below the yields attainable on longer-term investments, not least as a reaction to the Bundesbank's policy of relaxation. As a result, the capital market developed into the most important area of the overall flow of funds in 1983.

Strong propensity of the general public to invest . . .

The security markets — as the classical transmission channel for longer-term funds — naturally played a key role in this process. In particular, the general public's demand for investments in securities was strong, after the banks had sharply lowered the interest rates on deposits, especially savings deposits, in the first half of the year. In all, the domestic non-financial sectors invested DM 39 billion in bonds and shares last year; this was more than one-fifth of their entire acquisition of financial assets, against just under 15% in 1982.

. . . despite fluctuating interest rates

By far the greater part of these funds flowed into the bond market, where, over the whole of 1983, issuers encountered a remarkably strong and at the same time constant propensity to invest, accompanied by some quite volatile interest rate movements. With hindsight it is plain that in the initial months up to the spring — and sporadically even later in the year — market participants' investment decisions were guided by an interest rate optimism that ran far ahead of the true potential for interest rate reductions. Only when the yield on bonds fell from barely 8% at the beginning of the year to 7¼% in March 1983 and, shortly afterwards, the interest rate trend in the U.S. financial markets turned upwards, did a more cautious appraisal of future interest rate movements emerge for the first time. It appears that at the long end of the markets no new interest rate hopes were pinned on the Bundesbank's lowering of the discount and lombard rates in mid-March; in fact, yields in this area crept up gradually. In the spring the change in investors' expectations was reflected in an extremely wide-ranging pattern of interest rates in the bond market. There was a gap of more than 2¼ percentage points between the yield on long-term and that on short-term securities, compared with one of 1 percentage point at the beginning of the year. At the beginning of June the interest rate on domestic bonds, at 8¼% on average, exceeded its lowest level of March 1983 by more than a full percentage point again. Around this time there was growing concern that the exceptionally sharp monetary expansion and the unfavourable exchange rate movements might endanger the successes already achieved in the field of stability policy. Substantial interest rate fluctuations occurred in the summer of 1983, with the yield on bonds reaching a peak of almost 8½%; this fostered a more sceptical appraisal of interest rate prospects. A gentle touch on the monetary brakes in the late summer and the raising of the lombard rate at the beginning of September 1983 had a calming effect on the markets.

Large investment purchases by non-residents ...

Subsequently this situation gave way to cautious interest rate optimism which eventually culminated in a renewed — albeit very short-lived — rise in bond prices when non-residents' growing interest in Deutsche Mark assets fired the imagination of market participants in two respects: firstly because of the expected favourable movement of Deutsche Mark bond prices, and secondly because of the possible appreciation of the Deutsche Mark. From the late summer onwards, foreign investors acquired record amounts of Deutsche Mark bonds, far in excess of their large purchases in the "revaluation years" 1978 and 1979. In all, last year non-residents bought Deutsche Mark bonds to the amount of over DM 14 billion, just under DM 11 billion of which was accounted for by domestic bonds and DM 3.5 billion by foreign Deutsche Mark bonds. But towards the end of the year foreign investors exercised restraint in the German market, when exchange rate movements turned distinctly against the Deutsche Mark and the international interest rate trend moved upwards again. As a result, under the impact of fluctuating international interest rate movements, the domestic interest rates on bonds varied between 8% and 8½% in the final months of 1983. It was not until the new year that a certain downward "breakthrough" was achieved, when the Deutsche Mark regained ground world-wide in February 1984, and large amounts of funds flowed from abroad into the German capital market again. However, a certain dependence on the international interest rate and exchange rate movements remained, even though this dependence is sometimes looser and sometimes closer.

... and by domestic non-banks

Last year the main emphasis of domestic demand for bonds shifted from the banks to non-bank investors. In 1983 they bought almost DM 43 billion of domestic and foreign bonds, i.e. DM 6 billion more than in 1982, although saving by households declined in 1983. A notable feature is the steadiness of non-banks' investment, particularly in the second half of the year. During this period they were apparently guided in their decisions more by the relative yield advantage of investment in bonds over bank deposits for four years and more than by short-term interest rate trends. When long-term interest rates had risen to a level of 8 to 8½%, this gap averaged 2½ percentage points, against 1 to 1½ points six months earlier.

Decreasing importance of the banks' investments in bonds

A conspicuous contrast to this was formed by the rapid change, probably in response to the short-term price movements in the bond market, in the banks' investment purchases. But apart from this, the banks also seem to have had less scope for bond investments of their own because of the steep rise in private customers' credit demand, particularly in the longer-term field. The banks' bond purchases in 1983, at a total of DM 35 billion, were DM 8 billion smaller than the comparable figure for 1982.

Banks remain the most important group of issuers

However, the position of principal issuers was retained by the banks, which normally finance a large part of their longer-term direct loans to private and public borrowers on the bond market. In 1983 they received DM 51.5 billion from sales of their own bonds, or DM 7 billion more than in 1982. There were substantial shifts of emphasis in the composition of the sales of bank bonds, reflecting to a certain degree the changes in the thrust of credit demand during the year. A factor of special importance in this connection was the changed debt policy stance of the public sector, which borrowed more heavily in the bond market direct instead of taking up funds from banks.

Acquisition of financial assets and incurrence of liabilities by the domestic non-financial sectors*

Item	1981 p DM billion	1981 p %	1982 p DM billion	1982 p %	1983 pe DM billion	1983 pe %	Memo item Change from previous year DM billion 1982 p	Memo item Change from previous year DM billion 1983 pe
Acquisition of financial assets								
Longer-term 1	128.6	63.5	144.5	77.5	160.6	87.1	15.9	16.1
of which								
at banks	15.1	7.5	53.4	28.6	58.8	31.9	38.2	5.5
Bonds	47.0	23.2	20.3	10.9	30.4	16.5	−26.7	10.1
Shares	6.0	3.0	6.6	3.5	8.9	4.8	0.5	2.3
Short-term	74.0	36.5	42.0	22.5	23.8	12.9	−32.0	−18.3
of which								
at banks 2	58.6	28.9	33.5	18.0	15.0	8.1	−25.1	−18.5
Total	202.6	100	186.5	100	184.3	100	−16.1	− 2.2
Incurrence of liabilities and issue of shares								
Longer-term	173.5	72.2	164.2	81.7	182.8	89.5	− 9.3	18.6
of which								
at banks	103.4	43.0	81.5	40.6	94.9	46.5	−21.8	13.4
Bonds	− 3.7	− 1.5	28.0	13.9	33.8	16.6	31.7	5.8
Shares	3.6	1.5	4.5	2.2	5.9	2.9	0.9	1.4
Short-term	66.9	27.8	36.8	18.3	21.5	10.5	−30.1	−15.3
of which								
at banks	29.6	12.3	15.1	7.5	18.8	9.2	−14.5	3.6
Total	240.4	100	201.0	100	204.3	100	−39.4	3.3

* Households, enterprises (including housing), government (including social security funds). — **1** Financial assets with maturities of more than one year, including all savings deposits and all purchases of securities (regardless of their maturity). — **2** Including cash balances. — **p** Provisional. — **pe** Partly estimated. Discrepancies in the totals are due to rounding.

Decline in sales of communal bonds and mortgage bonds

Accordingly, the supply of communal bonds, which primarily serve the purpose of financing bank lending to the public authorities, decreased distinctly in significance. Net sales of these securities in 1983, at DM 28.5 billion, were almost DM 8 billion smaller than in 1982. Sales of mortgage bonds, the second traditional financing instrument of the issuing institutions, were also sluggish; at DM 8.5 billion they fell slightly short of the previous year's figure (DM 9 billion). But this was by no means due to a general decline in the demand for mortgage loans, but first and foremost was the mirror image of a shift in demand for housing loans in favour of those institutions which finance their credits predominantly out of deposit business and were therefore in a position to offer relatively favourable terms, in view of the rise in interest rates in the bond market. For instance, in 1983 the savings banks registered a rise in demand for housing loans of more than half as much again as in 1982, while in the case of private mortgage banks the corresponding loan commitments barely exceeded the level of 1982. In all, expansive stimuli did not reach the issuing institutions, either in lending business with the public sector or in the field of mortgage loans.

Steep increase in supply of "other" bank bonds

In lending business with trade and industry the issuing institutions and their affiliates met with a brisk demand for longer-term credits, either new ones or ones intended to replace short-term loans. Consequently, the supply of "other" bank bonds, which are primarily issued to finance such credits, went up by leaps and bounds last year. Net redemptions amounting to DM 5 billion in 1982 were followed by net bank placements of such securities totalling DM 7.5 billion in 1983. Especially the central giro institutions placed large amounts in the market, probably to offset the sluggish pace of loan business with the public sector. Private mortgage banks also seem to have enlarged their sales last year. There was a conspicuous rise in the amount of these securities outstanding among the other banks, which likewise increasingly used this financing instrument in view of the strong propensity to buy apparent in the bond market.

Public issuers take advantage of absorptive markets

As already mentioned, public issuers took advantage of the productive state of the markets last year by raising funds direct in the bond market instead of taking up loans against borrowers' notes. This explains why in 1983 sales of public bonds (including bonds of the Federal Railways and Federal Post Office) climbed by DM 6 billion to DM 34.5 billion, although the deficits that had to be financed were noticeably reduced at the same time. Taking the central, regional and local authorities together, the share of financing via the bond market in the total net incurrence of liabilities in 1983 rose from barely two-fifths to three-fifths. In the main this was the outcome of the changed debt policy of the Federal Government, which increased its bond issues in 1983 by just under DM 7 billion to DM 29.5 billion net. It thus met about 90% of its total financing needs in this way against approximately 60% a year earlier. Half of the amount placed was accounted for by regular sales of five-year special Federal bonds and Federal savings bonds sold in the form of tap issues (DM 15.5 billion), the remainder by sales of standard bonds and medium-term notes (DM 14 billion).

Brisk issuing activity in the market for foreign Deutsche Mark bonds

Issues of bonds of foreign borrowers denominated in Deutsche Mark continued to be buoyant last year, practically all the bonds sold going to non-residents. In many cases, foreigners prefer these securities to German bonds because the interest accruing is not subject to German investment income tax (known as "coupon tax"), which is withheld at source from the interest paid to foreigners by domestic issuers. In 1983, too, this unequal tax treatment caused foreign investors to accept comparatively low (gross) yields on foreign Deutsche Mark bonds, even though domestic bonds are frequently to be rated higher with respect to soundness and marketability. In the last six months this yield discount on foreign Deutsche Mark bonds came to between ¼ and 1 percentage point (with a wide spread). True, at the present time this is not a direct burden on the German market. But there is a tendency for this special tax treatment for the interest income of non-residents — which was originally introduced as a protection against undesired capital inflows — to act, besides other factors, as an incentive for foreign issuers to borrow in Deutsche Mark at favourable interest rates. It is probable that in this way some of the funds supplied by non-residents are diverted from Deutsche Mark bonds of domestic issuers to foreign Deutsche Mark bonds.

The year of the share

Last year the German share market, which had been overshadowed by the bond market for many years, moved into the focus of interest of many domestic and foreign investors. In 1983 its contribution to overall capital formation was again only moderate, but in terms of stock exchange turnover it surpassed the bond market in that year. There was a sharp jump in domestic share prices, which climbed from one peak to another with only a few interruptions and without any major setbacks. Already last spring, when it reached a first peak, the index of share prices calculated by the Federal Statistical Office was 25% above the level of the beginning of the year. There were two more price surges in the summer and towards the end of the year, during which prices mounted by a further 8%. At the beginning of February 1984 they hit a new high which exceeded the price level of early 1983 by 48%.

Strong stimuli from abroad . . .

The remarkable price rise in the German share market certainly owes something to the preceding upward movement in the markets of other industrial countries, particularly the bull market in U.S. shares. In a number of cases the decisions of investors operating on an international scale gave a strong stimulus to share price movements in Germany. Even after the substantial price rises last year, foreigners obviously considered German shares to be an attractive alternative investment, the more so as the rising dollar made German shares "cheaper" for buyers who calculate on a dollar basis; indeed, it can be assumed that the sharp rise in share prices (which are calculated in Deutsche Mark) owed something to exchange rate movements.

Purchases of bonds, by group of buyers and type of securities

DM billion (market value)

Purchasers	Year	Domestic bonds Total	Bank bonds	Industrial bonds	Public bonds 1	Foreign bonds 2	All bonds
Residents	1978	39.7	30.6	− 0.8	9.9	3.6	43.3
	1979	37.2	36.0	− 1.0	2.3	3.7	40.9
	1980	44.9	41.9	− 1.2	4.3	7.3	52.3
	1981	68.3	70.7	− 0.9	− 1.5	6.2	74.5
	1982	70.5	45.3	− 0.6	25.8	11.0	81.5
	1983	74.7	47.2	− 0.6	28.1	5.7	80.5
Banks	1978	20.2	16.7	− 0.2	3.7	1.2	21.4
	1979	1.1	3.3	− 0.2	− 2.0	2.6	3.7
	1980	14.1	15.6	− 0.1	− 1.5	3.3	17.3
	1981	17.0	18.0	− 0.0	− 1.0	0.5	17.6
	1982	44.3	31.8	− 0.1	12.6	− 1.2	43,1
	1983	35.9	25.9	− 0.1	10.1	− 0.7	35.2
Non-banks	1978	16.0	13.9	− 0.6	2.7	2.3	18.3
	1979	38.2	32.7	− 0.9	6.4	1.1	39.3
	1980	29.1	26.2	− 1.1	4.0	4.1	33.2
	1981	51.5	52.7	− 0.9	− 0.3	5.7	57.2
	1982	24.5	13.5	− 0.5	11.6	12.2	36.7
	1983	36.4	21.3	− 0.5	15.6	6.5	42.9
Open market operations of the Bundesbank	1978	3.5	−	−	3.5	−	3.5
	1979	− 2.1	−	−	− 2.1	−	− 2.1
	1980	1.8	−	−	1.8	−	1.8
	1981	− 0.2	−	−	− 0.2	−	− 0.2
	1982	1.7	−	−	1.7	−	1.7
	1983	2.4	−	−	2.4	−	2.4
Non-residents 3	1978	0.1	e − 1.2	e − 0.2	1.5	×	0.1
	1979	4.0	e 0.4	e − 0.1	3.7	×	4.0
	1980	0.3	e − 0.3	e − 0.0	0.7	×	0.3
	1981	− 1.5	e − 0.3	e − 0.0	− 1.1	×	− 1.5
	1982	2.2	e − 0.5	e − 0.0	2.8	×	2.2
	1983	10.8	e 4.5	e − 0.0	6.3	×	10.8
Total 4	1978	39.8	29.4	− 1.0	11.4	3.6	43.4
	1979	41.2	36.4	− 1.1	6.0	3.7	45.0
	1980	45.2	41.5	− 1.3	4.9	7.3	52.6
	1981	66.9	70.5	− 1.0	− 2.6	6.2	73.1
	1982	72.7	44.8	− 0.6	28.6	11.0	83.7
	1983	85.5	51.7	− 0.6	34.4	5.7	91.3

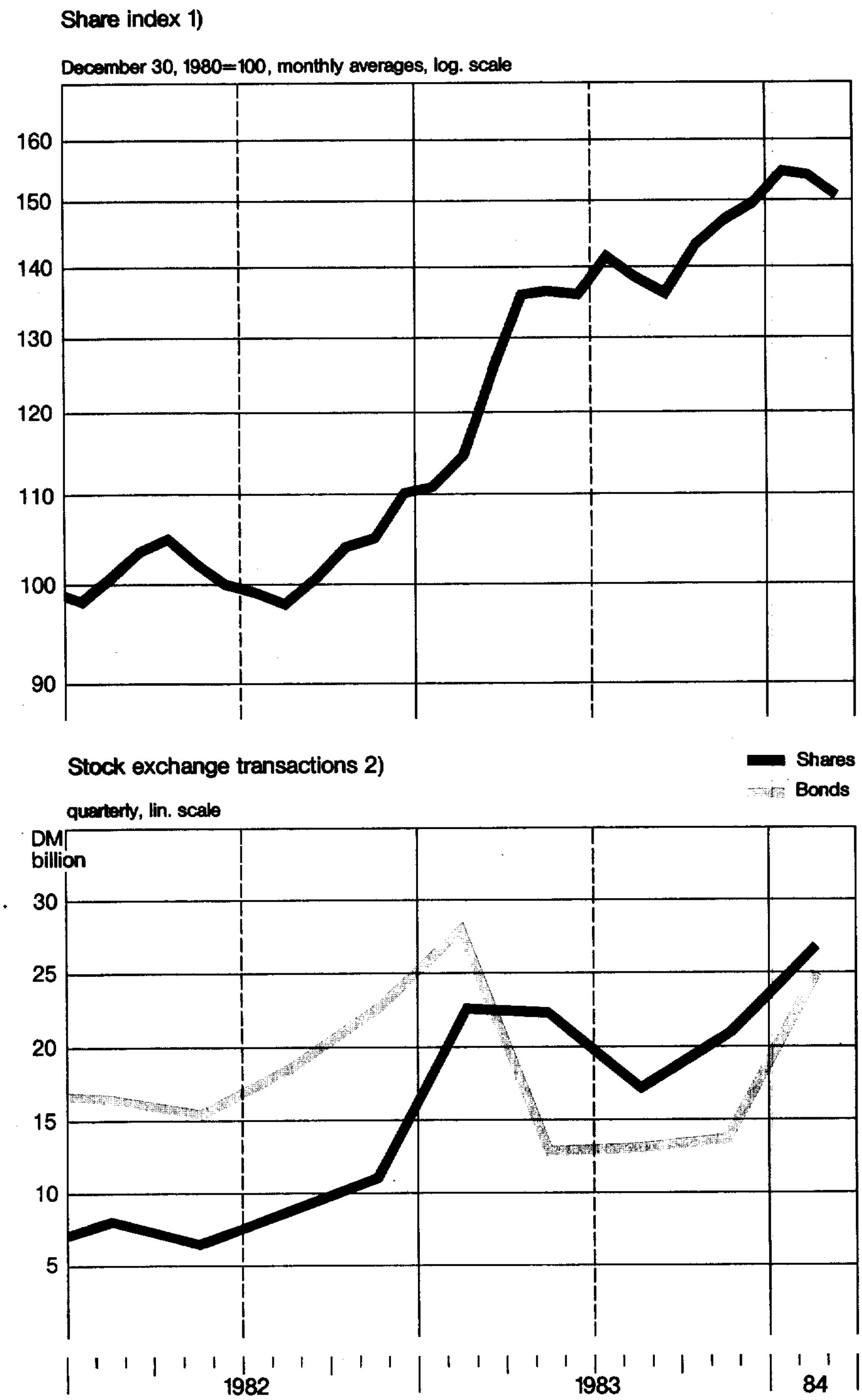
1 Mostly bonds, medium-term notes, Federal savings bonds and 5-year special Federal bonds. — 2 Net purchases (+) or net sales (−) of foreign bonds by residents. — 3 Net purchases (+) or net sales (−) of domestic bonds by foreigners. — 4 Net sales plus/less changes in issuers' holdings of their own bonds. — e Estimated. Discrepancies in the totals are due to rounding.

... and from greatly improved earnings expectations of enterprises

In addition to the stimulating effects deriving from foreign share markets and exchange rate movements, the domestic share market also benefited from the improved earnings situation of German enterprises. The urgently required adjustment in progress there had positive effects on the climate in the German share market in several respects. The expectations of higher returns on investment in fixed assets enhanced enterprises' willingness to invest. At the same time, their stimulating effects on share prices and the demand for equities improved in text-book fashion the preconditions for channelling the supply of savings into uses that will strengthen the growth potential of the German economy over the longer term.

Financing through shares more attractive

In part, domestic enterprises seem to be taking advantage of the improved conditions for financing through shares. With sales of DM 7.25 billion (market value), the amount raised in the share market in 1983 was over DM 1 billion higher than in the previous year. Moreover, it looks as if the vigorous growth of the share markets has fundamentally strengthened enterprises' readiness to issue equities; this is reflected in the fact that more and more companies are considering an approach to the stock exchange. However, the share market's



1) Index of the Federal Statistical Office.- 2) Spot dealings in domestic securities at market value.

contribution to the procurement of capital and reserves by issuing new shares (or, in anticipation, by issuing convertible bonds) was modest last year. Partly, the institutional obstacles to share issues and to the establishment of public limited companies are still too great (double taxation under property tax legislation, difficulties in changing the form of organisation, problems of access to and organisation of the security markets and the provision of risk capital), even though the Federal Government has begun to remove, or has already removed, some of these obstacles. In some cases, however, aversions to new issues or to changing the form of organisation are rooted in the negative attitude of the proprietors of enterprises (fear of a change in the ownership situation or of an extension of codetermination), which would have to be overcome.

New ways of forming own funds

More recently established or smaller enterprises — whose readiness to innovate and to invest is indispensable to the economy — have practically no means of raising risk capital through the share market. Here it is up to the banks and large enterprises in particular to facilitate new firms' equity financing through the market. The recent debate on the role of equity investment companies and the numerous new firms established in this area has made it clear that the outstanding problems here have been recognised. At the same time the Federal Government is taking steps to explore the fiscal and legal possibilities of facilitating the establishment of businesses and enterprises as well as the formation of additional risk capital even outside the stock exchange.

5. Competitiveness in export markets well maintained despite a few weak spots

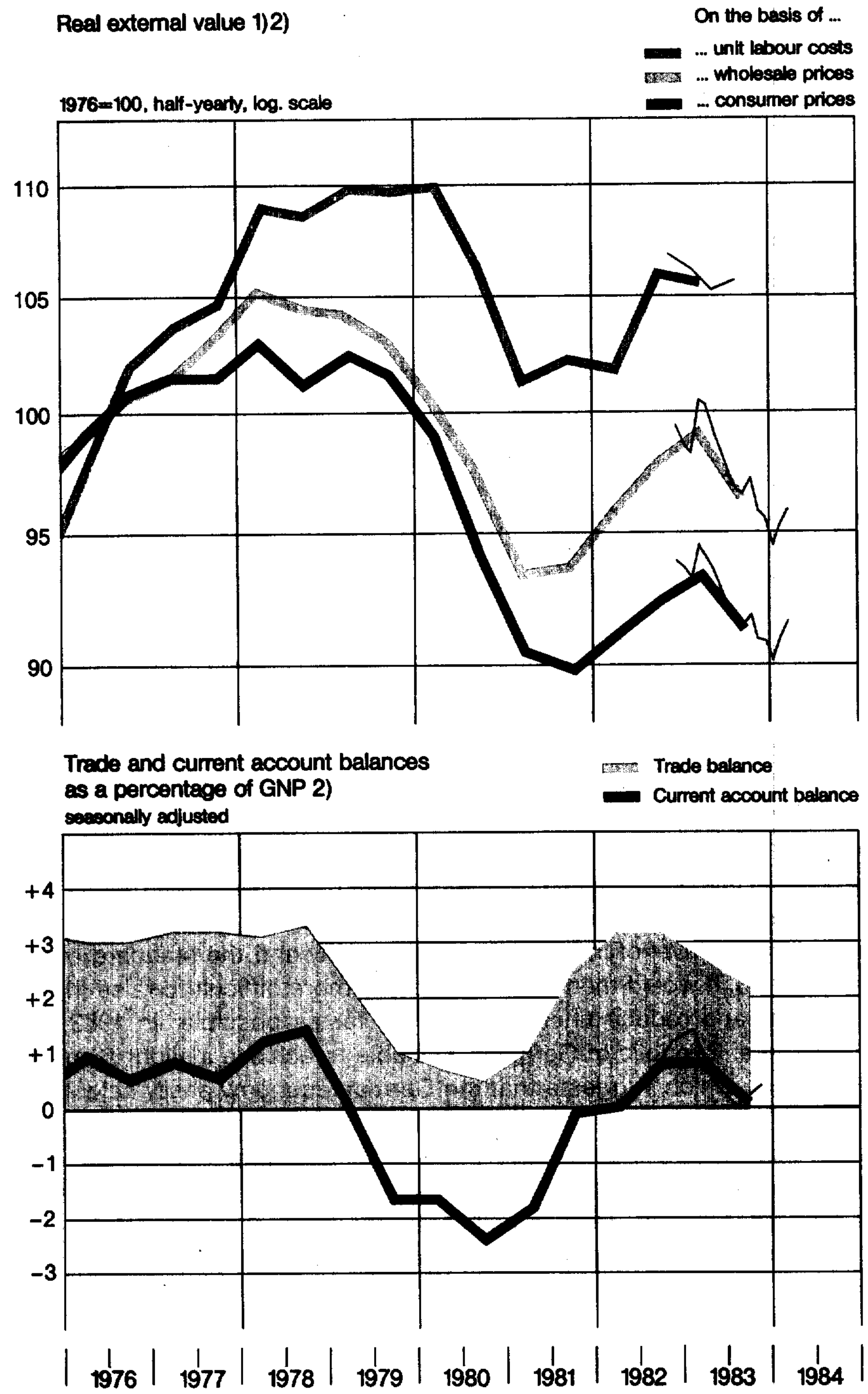
Competitiveness in export markets — a key factor for the German economy

The economic recovery in the Federal Republic of Germany over the course of 1983 was, as already stated, strongly dependent on the revival of exports. This confirmed yet again that the level of economic activity in our country is very largely determined by success or failure in foreign trade. That follows simply from the fact that exports of goods and services account for roughly 30% of domestic value added (although such exports are accompanied by nearly the same volume of imports of goods and services). The importance of exports is, however, underlined by the fact that the main export areas in the Federal Republic of Germany are at the same time the linchpin of German industry, they are sectors which employ a large number of people and engage in considerable capital investment, with major opportunities for helping technical innovations to achieve a breakthrough. To put it differently, if German exporters were not sufficiently competitive on world markets, this would not only be detrimental to our balance of payments and the exchange rate for our currency; it would also jeopardise the real level of incomes in our economy and the standard of living of our population. It would then be progressively more difficult to raise the level of employment and reduce unemployment as far as possible; in 1983, as in 1982, the Federal Republic of Germany was able to achieve a slight surplus on current account, which suggests that the German economy easily held its own under difficult conditions on world markets. But bearing in mind that domestic production capacities were not nearly fully utilised during that period, which tended to stimulate exports, and that, contrary to the previous trend, the deficits on the services and transfer payments accounts dropped considerably, even if only temporarily, it cannot be automatically inferred from the current account surplus of 1983 that international competitiveness is assured over the longer term.

Current account deficits from 1979 to 1981 caused partly by the prior deterioration in competitiveness

The fact that the economy of the Federal Republic of Germany is rather vulnerable on the external flank emerged in the years from 1979 to 1981, when the German current account showed high deficits for the first time for many years, necessitating the adoption of a restrictive economic policy. These difficulties are now largely overcome, but at the time they were due to a variety of factors. In large part they were certainly attributable to the fact that up to the autumn of 1979 the Deutsche Mark appreciated disproportionately strongly — more, at any rate, than was consistent with Germany's stability lead over other countries at the time. This weakened the competitiveness of the German economy with respect to prices and production costs. This became fully evident when the prices for imported energy and raw materials rose yet again in 1979 and 1980, while the upturn in domestic demand associated with the pump-priming measures initiated in 1978 absorbed a larger part of domestic production and made exports appear to be a rather less pressing matter to German producers. The

Real external value and current account



1) Weighted nominal external value of the Deutsche Mark against the currencies of major trading partners, adjusted for differences in rates of cost and price increase (geometric means).- 2) Quarterly and monthly figures as well from the end of 1982 onwards.

deficit on current account of DM 28.5 billion run by the Federal Republic of Germany in 1980 was the highest in absolute terms ever recorded by an individual country up to that date.

Return to current account surpluses in 1982

The return to surpluses on current account in 1982 and 1983 suggests, however, that the Federal Republic of Germany has been able to hold its own more effectively on sales markets abroad of late. German products have become sufficiently attractive again to foreign buyers for the heavy demand for imports in the Federal Republic of Germany, especially the higher energy bill and the massive deficits on services and transfer payments accounts, to be met. Factors on the import side also played a part in the improvement on current account; in particular, efforts to conserve energy were successful, and the OPEC countries slightly lowered the price of their oil; quite apart from this, the economic slowdown in Germany which lasted until the end of 1982 slightly reduced German demand for imports. But the decisive factor was no doubt that German exporters were able to improve their position on world markets.

German exports again expand faster than world trade

While the volume of world trade on average in 1983 was slightly below the figure for 1980, real exports by the Federal Republic of Germany in the last three years increased by about 10%; the share of Germany in world trade (calculated at 1980 prices) therefore rose from 10% in 1980 to just over 11% in 1983. Apart from the world-wide decline in oil exports, part of this statistical increase was due to the fact that the Federal Republic of Germany benefited from the regional structure of its exports, since the markets that have been expanding have traditionally been among our main customers, while those market segments which have been growing at a below-average rate or even shrinking have played only a minor part in German exports. For example, German exporters were hardly affected by the cutback in imports into Latin American countries (by about one-third in real terms from 1981 to 1983) since the Latin American sub-continent accounted for only 3.3% of total German exports before the cutback (2.3% in 1983). On the other hand, Germany profited from the fact that merchandise trade within Western Europe, its traditional sales market, expanded noticeably in comparison with that in other regions.

Exporters win back most of the market shares they had lost

The disproportionately steep growth in exports from the Federal Republic of Germany also owes something to the fact that German products fared better on average on their various regional markets than goods from competing countries. It is true that the losses of market shares that were sustained in the seventies have not been fully made good again in the last three years but the Federal Republic of Germany has nevertheless been strikingly successful, especially if it is also borne in mind that the market shares gained are not limited to specific groups of goods or regions but are spread throughout most of the export range, with the exception of high-technology products (see p. 56).

International competitiveness improved

Following these successes, enterprises themselves now take a generally more favourable view of their international competitiveness, as a survey made in February 1984 by the German Federation of Industry and Commerce shows. Firstly, the Federal Republic of Germany appears to come off well in non-price factors such as quality and after-sales service; the argument that German firms keep to their delivery dates, which so often used to be put forward as an advantage for German exporters, is no longer as significant as it used to be, since capacities are idle world-wide. Secondly, cost trends have taken a turn for the better, given the change in exchange rate relationships.

Relatively moderate rise in wage costs in the Federal Republic of Germany, compared with other countries

From 1980 onwards production costs in the Federal Republic of Germany, measured in national currency, rose more slowly than in the preceding years and also than in other countries; a correction of the cost burden of earlier years has thus got under way. Earnings in the manufacturing sector — gross wages and salaries and additional wage components — are of particular significance here, if only because of their magnitude. There has been a marked slowdown in the rate of increase of wage costs in all western industrial countries in recent years, but there are still strong divergencies between the trends in wages and salaries in different countries. Per capita wages and salaries in the manufacturing sector in the Federal Republic of Germany rose by 22% from 1979 to 1983 (as compared with an increase of 34% from 1975 to 1979), but in the other major industrial countries wage costs have gone up on average over the last four years by 55%; the gap vis-à-vis the major European countries (included in this

Indicators of the international competitiveness of the Federal Republic of Germany

Year	Wages and salaries per employee 1 2	Output per employee 1	**Unit labour costs 1**	Unit labour costs in major trading partners 1 3	Nominal external value of the Deutsche Mark 3	Unit labour cost differential adjusted for exchange rate movements 4	**Memo item** Price differential adjusted for exchange rate movements 4 5
	1	2	3	4	5	6 = 3÷4×5	7
	1972 = 100						
1975	135	105	128	146	115	101	101
1976	147	117	126	154	122	100	102
1977	160	121	132	166	130	104	105
1978	169	123	138	175	137	108	108
1979	181	129	140	184	142	108	106
1980	193	128	151	201	142	107	101
1981	203	129	158	217	138	101	96
1982	212	130	164	232	146	103	99
1983	221	137	161	237	152	104	100
	Percentage change						
1975/79	+ 34	+ 22	+ 9	+ 26	+ 23	+ 7	+ 5
1979/83	+ 22	+ 7	+ 15	+ 29	+ 7	− 4	− 6

1 Manufacturing sector. — 2 Gross wages and salaries. — 3 Weighted with shares in foreign trade with 13 major trading partners. — 4 Unit labour cost or price differential adjusted for movements in the nominal external value. — 5 On the basis of wholesale prices of industrial products.

average) was even greater, for wage costs climbed in Italy by 90%, in France by 63½% and in the United Kingdom by 60%, although the rate of increase has now decelerated somewhat in these countries as well. However, productivity, i.e. output per employee, has developed rather less favourably in the Federal Republic of Germany than in most other countries. Measured by unit labour costs, i. e. expenditure on wages and salaries per unit of output, Germany's lead was therefore not quite so large. From 1979 to 1983 unit labour costs in German industry rose by 15%, as compared with 29% on a weighted average in 13 major trading partners.

Relatively low rise in unit labour costs over the last four years, even after taking exchange rate changes into account

The advantage of the lower rise in labour costs in the Federal Republic of Germany was however reduced over the last four years by a relatively strong appreciation of the Deutsche Mark. During that period the Deutsche Mark depreciated considerably against the U.S. dollar, but it was valued very much higher against most other currencies, especially those in the European Monetary System, and on a weighted average against 13 major industrial countries the external value of the Deutsche Mark has gone up by about 7% since 1979. That is rather less than would have been consistent with the cumulative discrepancy in unit labour costs vis-à-vis other countries (11%). If, to permit an international comparison of cost differences, relative unit labour costs are taken together with exchange rate movements, it can be seen that even after adjustment for exchange rate movements unit labour costs in the Federal Republic of Germany have risen rather more slowly over the last four years than those abroad (by 4%). This development contrasts with that from 1975 to 1979, when unit labour costs in Germany, adjusted for exchange rate movements, increased by 7% more than those abroad. The more favourable trend recently in unit labour costs in the Federal Republic of Germany on an international comparison has offset some of the factors which have made German firms less competitive of late.

Overall cost situation also greatly affected by other factors

As in the case of labour costs, industry in the Federal Republic of Germany has probably been less adversely affected than that in other countries by the cost of raw materials over the last four years, since, owing to a comparatively favourable exchange rate trend for the Deutsche Mark, the price increases for these products on world markets did not have such a strong impact in this country as elsewhere. It is true that the Deutsche Mark has declined in value against the U.S. dollar and other hard currencies in recent years, but the currencies of a number of European countries, in particular, have depreciated even more strongly against the dollar, so that Germany was better off than these competing countries with respect to raw materials imports. It is not, however, possible to judge, on the basis of the data available, precisely how important these divergencies in materials costs really were for competitiveness. Comparisons on the basis of major cost factors can of course only give a rough indication of general trends. They would also need to be supplemented by the cost burden resulting from capital input (interest) and capital utilisation (depreciation); it is even less possible to achieve reliable results here. Cost comparisons on the domestic market, however, have shown that these kinds of costs are of relatively minor significance.

Higher costs not passed on in full in prices

According to the available statistics, the strong competition on world markets has continued to prevent German firms in recent years from passing on the rises in export production costs — even though these were lower than in earlier years — fully in prices. This has narrowed the profit margins obtainable on exports. In fact, the earning power of German enterprises with a high percentage of export business has not dropped less since the beginning of the seventies than that of sectors which are less export-oriented. As the results of the Bundesbank's statistics on enterprises' annual accounts show, the profit for the year as a percentage of turnover in the chemical industry, for example, decreased from 4.3 % (in 1970) and 3.1 % (in 1974) to 1.8 % in 1982, and in mechanical engineering it fell from 4.3 % to 1.4 %. In electrical engineering the profit-turnover ratio went down between 1970 and 1982 from 4.7 % to 1.7 %, and in the motor industry it declined from 3.6 % to 1.6 %. In industries with lower export ratios[1] the profit for the year in 1970 was between 3½ % and 4½ % of turnover; this ratio had likewise dropped markedly by 1982, falling to between 1 % and just under 2 %. Here the profit squeeze in the years up to 1982 was not limited to the export industries, and even in them it was not caused solely by external factors; for it was not possible to pass on higher costs fully in prices on the domestic market either. But as already outlined elsewhere in this Report, the earnings situation improved again in 1983, presumably more among firms with a high percentage of exports as the Deutsche Mark was depreciating.

A "strong", not a "weak", currency safeguards competitiveness over the longer term

Even if the recent trend in costs and earnings suggests that the Federal Republic of Germany has been able to gain ground vis-à-vis its main competitors and has made good much of the competitiveness it lost in the second half of the seventies, the fundamental problems and weaknesses that still remain should not be overlooked. The improvement in German competitiveness with respect to prices and costs since 1979 has largely been due to the real depreciation of the Deutsche Mark; however, a depreciation of one's currency, unless it is the outcome of previous definite over-valuation, is not, as past experience has shown, a promising strategy over the longer term. Depreciation results in a deterioration in the terms of trade for a country, and leads to a reduction in real income and a rise in domestic prices "due to the depreciation". Moreover, especially at a time when domestic demand is expanding, it may trigger a wage-price spiral with all its adverse implications for the economy, and especially for employment. Considered in these terms, the exchange rate is not a suitable instrument for ensuring external competitiveness in the long run. German exporters must be able to hold their own on foreign markets even when, as has been the case since the end of January 1984, the downward trend stops and a renewed rise in the rate for the Deutsche Mark reflects the fact that the intrinsic value of the German currency is more stable than that of other

1 Especially clothing, steel and light metal construction, paper and cardboard processing, wood processing and the production of plastic goods.

Exports of high-technology products from selected countries*

Item	1972	1976	1978	1980	1982	1983 pe
	Export shares in %					
Germany	26.3	21.7	21.6	20.0	17.0	17
of which						
EDP	40.2	24.8	16.0	16.7	14.5	14½
Telecommunications	22.8	19.1	20.2	19.6	16.5	14½
Electron tubes, transistors	17.4	15.3	19.3	17.1	11.0	11
Measuring instruments	25.6	24.0	22.9	21.6	20.2	21
Medical equipment	36.4	33.1	31.5	29.4	26.1	26½
France	11.1	10.9	10.4	10.3	8.1	8
United Kingdom	13.8	11.5	11.7	12.6	11.1	10
Switzerland	3.5	3.6	4.1	3.6	3.2	3
Japan	13.0	18.2	18.5	18.2	20.3	25
United States	32.2	34.1	33.7	35.3	40.2	37
	In US$ billion					
Selected countries, total	8.4	20.6	29.8	44.2	49.7	54
of which Germany	2.2	4.5	6.5	8.8	8.5	9

* France, Germany, Japan, Switzerland, United Kingdom, United States. — **pe** Partly estimated. Discrepancies in the totals are due to rounding.

currencies and a certain upward movement of the nominal exchange rate could be appropriate to keep the external value of the Deutsche Mark stable in real terms.

Ground lost in exports of high-technology products

An examination of the competitiveness of the German economy needs supplementing in certain areas. Here we can only go into the question of how German exports of high-technology products have developed over the last ten years. The main concern here is not where Germany stands today in the spectrum of technological and scientific inventions and discoveries, but in how far new technological know-how is being translated into new products, with the success of these innovations being reflected in international trade. The share of these exports in total German exports is at present not very large in terms of quantity, but this area is showing the strongest growth and is thus one of those with the best prospects for the future. For a country like the Federal Republic of Germany these are goods which are unlikely to be exposed to competition from less highly developed countries for the time being, and this area therefore offers a good chance of compensating for the growth of international competition in the "older" industrial products. According to the available data, the Federal Republic of Germany has lost ground in exports of selected high-technology products as compared with major competitors, although the value of these exports has risen strongly. Of the US$ 54 billion which the six major supplier countries (United States, Japan, Federal Republic of Germany, United Kingdom, France and Switzerland) earned from exports of EDP equipment, communications technology, electron tubes, measuring instruments and medical equipment, the Federal Republic of Germany accounted for only 17 % as compared with 21½ % in 1978 and — admittedly with a very much lower market volume — 26 % in 1972. The Japanese, on the other hand, starting from very low export figures, very rapidly increased their exports of these high-technology products. Japan now has a market share of 25 % and has pushed the Federal Republic of Germany down into third place. The United States, the principal supplier of these products, was also able to raise its share on a longer-term comparison to 37 %. (According to data now available for 1983, however, the position of the Federal Republic of Germany probably deteriorated no further last year.) If the Federal Republic of Germany were to fall further behind in the development of marketable and competitive high-technology products, this would not only be disadvantageous to our foreign trade position. Since these are key areas of economic expansion which stimulate growth in many other sectors of the economy, success or failure here may be of vital importance for the economy as a whole and not least for employment trends. Awareness of this fact has grown recently, and reports from industry suggest that there has been a revival of innovation, especially in the field of micro-electronics. In 1983 German exports of high-technology products not only grew strongly; they were also slightly more than in the previous year above the level of imports, which itself was notably high. Especially in the case of measuring instruments and medical equipment there was a distinct rise in the Federal Republic of Germany's trade surplus. There was no further growth in the trade deficit on EDP equipment or electron tubes either (see the table on p. 58).

Relatively high German expenditure on research . . .

High expenditure on research and development in the Federal Republic of Germany is certainly over the longer term a major prerequisite for the maintenance of an appropriate performance in the technology field. For years private and public German expenditure for this purpose has been increasing at a faster pace than the national product. According to the figures for 1981 — more recent data are not available — the Federal Republic of Germany is near the top of the international table as regards expenditure on research, which includes expenditure on personnel and other, non-personnel spending as well as investment in research. German expenditure on research, like that of the United States, Japan and the United Kingdom, accounted for 2½ % of the gross domestic product, while France, for example, spent 2 % of GDP on this. It is striking, however, that in Japan research is mainly left to industry, while in the Federal Republic of Germany and the United States the government accounts for about one-half of expenditure. In the United States, however, military research expenditure plays a major part.

. . . but this needs to find expression in more investment

To maintain international competitiveness it is essential for the results of research to be converted into new marketable products and improved production techniques, even if government financial aid is finally withdrawn in specific cases. The economic structure has to be adapted to modern technology through a constant adjustment process, in which greater flexibility on the goods and factor markets is just as important as more investment in fixed assets. This means that the level of the investment ratio is a major criterion of the dynamism and competitiveness of an economy. In the period of technological transformation which the world economy is now going through, adequate earnings must be ensured and general economic conditions improved to make it worth-while to take risks and modernise the economy by stepping up investment.

Further efforts needed to safeguard competitiveness

Considerable progress was made in this direction last year, but the pressure to adjust to which exporters are now exposed will remain fairly strong in the foreseeable future. The advance of Japan and the threshold countries on the world market shows that even positions which seemed secure can easily be jeopardised. Moreover, it is out of the question for the Federal Republic of Germany to seek to maintain its international competitiveness by means of a "defensive strategy", such as a depreciation of the Deutsche Mark in real terms would constitute. Nor could recourse to protectionist measures ever be considered; both these courses would ultimately only have adverse repercussions. On the contrary, economic dynamism and flexibility must be secured by consistent efforts to foster structural change while maintaining monetary stability. What is needed above all is "offensive" adjustment. A great deal of the responsibility here lies with the employers and trade unions. The responsibility is greater than is implied by considering wage costs alone. In view of the challenge presented by the strengthening of international competition, constant adjustment is essential, for jobs can be safeguarded only if workers are mobile and flexible. It

German foreign trade in high-technology products
("technology account")

DM billion

Item	1978	1980	1981	1982	1983 p
Exports					
EDP	1.8	2.8	3.2	3.7	4.8
Telecommunications	3.6	4.0	4.5	5.0	4.8
Electron tubes, transistors	1.7	2.2	2.3	2.4	2.9
Measuring instruments	3.5	4.6	5.4	6.0	6.4
Medical equipment	1.8	2.1	2.5	2.9	3.3
Total 1	12.9	16.1	18.4	20.6	22.9
Imports					
EDP	2.2	3.3	3.9	4.2	5.3
Telecommunications	1.8	2.2	2.6	2.7	2.8
Electron tubes, transistors	2.3	3.3	3.4	3.4	3.9
Measuring instruments	1.9	2.8	3.1	3.4	3.4
Medical equipment	0.8	1.0	1.1	1.3	1.4
Total 1	9.1	12.6	14.1	14.9	16.9
Balance (export surplus: +)					
EDP	− 0.4	− 0.5	− 0.6	− 0.5	− 0.5
Telecommunications	+ 1.8	+ 1.8	+ 2.0	+ 2.3	+ 2.0
Electron tubes, transistors	− 0.6	− 1.1	− 1.1	− 0.9	− 1.0
Measuring instruments	+ 1.6	+ 1.9	+ 2.3	+ 2.7	+ 3.0
Medical equipment	+ 1.0	+ 1.1	+ 1.4	+ 1.6	+ 1.9
Total 1	+ 3.8	+ 3.5	+ 4.3	+ 5.7	+ 6.0

1 Including nuclear reactors. — **p** Provisional.
Discrepancies in the totals are due to rounding.

would be a particularly grave misunderstanding if the view were to gain ground that technological progress must be restrained, rather than encouraged to the best of our ability, if jobs are to be preserved. If the Federal Republic of Germany had not achieved the present high standard of production technology, the real income of the population would be lower, economic dynamism would be less and unemployment would possibly be higher. Technological progress may mean that jobs are saved in one area through rationalisation (otherwise there would be no rationalisation effect), but further jobs are created elsewhere if commercial exploitation of the technological progress brings adequate earnings. The demand for labour will rise both in research and development and among the producers of capital goods, and not least among exporters if competitiveness there can be improved through rationalisation. As developments over 1983 have shown, exports impart a major stimulus to the economy of the Federal Republic of Germany, which is so closely integrated in the world economy, and this year as well the level of exports will be of crucial importance for the economic situation as a whole. Securing growth in exports, however, presupposes that the Federal Republic remains competitive on world markets, both with regard to the range of goods on offer, i.e. including new high-technology products, and in respect of production techniques. Investment to make German exporters more competitive will therefore create more jobs (not necessarily in every sector of the economy, but certainly in the economy as a whole). A highly developed industrial country like the Federal Republic of Germany cannot avoid the need to adjust its economic structure to changing international demand and supply conditions.

1. The situation in the world economy

Improvement in global economic prospects . . .

Last year saw a distinct improvement in the economic situation of the industrial countries of the West. After economic activity in the OECD countries had increased only slightly in 1980–81 and even declined a little in 1982, the real gross national product of these countries grew again last year by an estimated 2¼ %. As the year progressed, economic growth accelerated considerably; in the second half of 1983, in comparison with the same period of the previous year, it reached about 3½ %. However, up to the present only the United States, where the upswing began earlier and was particularly strong, has succeeded in considerably raising the level of employment and reducing its high unemployment. In the other countries unemployment has risen further, albeit no longer to the same degree as in preceding years. Moreover, the preconditions for a gradual decline in unemployment have tended to improve since success was achieved everywhere in containing inflation. The average increase in consumer prices in the OECD area slowed down from 8 % in 1982 to about 5 % last year, i.e. about the same average rate as before the first oil price hike. With average annual rates of price increase of 1.9 % and 3 %, respectively, Japan and Germany headed the list among the major industrial countries, followed by the United States with 3.2 %. In contrast, the rate of inflation in Italy and France was still 15 % and 10 %, respectively. Interest rates also continued to decline, but they dropped much less than rates of inflation, and they even rose again slightly from the middle of the year. Taking the average for the ten largest industrial countries (about 11 %), at the long end of the market they were about 1 percentage point lower in 1983 than in the preceding year. Another positive aspect of the development of the world economy last year is the fact that there was a revival in world trade. As a result, many countries were able to reduce their current account deficits. All these factors taken together brought the industrial countries closer to the goal of sustained and non-inflationary growth again for the first time for many years.

. . . above all the result of combating inflation and allowing market forces to operate more strongly again

But for the determined pursuit of anti-inflation policies in recent years economic recovery in all the major countries would not have been possible. The regaining of confidence in the stability of the value of money was also a precondition for market forces operating more strongly again. Moreover, last year witnessed a distinct improvement in the enterprise sector's earnings position in many countries, owing not least to moderation in wage policies. In addition, in spring 1983 there was a sharp fall in crude oil prices on international markets and this had a favourable impact on domestic demand, the movement of prices and the current accounts of the oil-importing countries. A certain part was also played by the fact that many countries wholeheartedly fostered structural change in their economies and gave greater scope to private initiative again, inter alia by providing tax relief. During the process of economic recovery those countries which achieved the most progress in their stabilisation policies, and at the same time relied more on the free play of market forces, always fared better.

Further economic upswing still involves risks

On the other hand, the risks which still attach to the further development of economic activity should not be underestimated. In many countries the upswing initially emanated from housing construction and private consumption, with the containment of inflation being helpful in many and varied ways. However, a lasting upward trend in economic activity, and hence a gradual increase in employment, presuppose a durable strengthening of the propensity to invest as well. Investment activity has in fact started moving ahead relatively strongly in major countries, including the United States in particular as well as Japan and Germany. The high level of U.S. interest rates, brought about especially by the budget deficit, has not had a major adverse impact on this development so far, but could in the longer run impair the propensity to invest. At any rate, persistently high budget deficits and corresponding shortfalls in the U.S. current account position would increasingly reduce the prospects of lower U.S. interest rates, not least because this could undermine confidence in the domestic and external value of the dollar. Instead of lower interest rates, higher rates would rather be likely, with all the negative implications this would have for the world economy. However, many other countries are also only just beginning to consolidate their public finances. This is also automatically reflected in the interest rate levels of these countries. To this extent, lower interest rates there do not depend on developments in the United States alone. Finally, the prospects for the world economy are also overshadowed by the international debt crisis. Thanks to close international cooperation it has been possible to keep it under control. A further positive development of economic activity in the industrial countries and persistent adjustment efforts in the debtor countries are important preconditions for the situation continuing to ease gradually.

2. International trade and current transactions

Recovery of world trade

With the revival in economic activity in the industrial countries world trade grew distinctly again in 1983. On the basis of the average development of exports and imports, the volume of international trade increased by about 2% over the previous year's level. In contrast, global merchandise trade declined in 1982 by 2.5%. The revival of world trade was mainly due to a sharp rise in the demand for imports on the part of the industrial countries, especially the United States, thus benefiting this group of countries in the main. A dampening effect continued to be exercised on world trade last year by the balance of payments problems of developing countries, chiefly those in Latin America and Africa, but with numerous OPEC countries now also playing a part. These obstacles can only be overcome in so far as economic growth in the industrial countries stimulates the exports of countries in a weak balance of payments position, thus providing them with some scope for a further increase in imports.

Sharply declining current account deficits of the developing countries

In 1983 the imports of the developing countries taken together, but excluding the OPEC countries, fell by an estimated 1% in real terms, after an even greater decline, particularly among the heavily-indebted countries, had been unavoidable in 1982. On the other hand, last year these countries achieved an increase of about 5% in their exports, which had gone up slightly also in 1982. In addition, rising raw materials prices improved the terms of trade of the developing countries for the first time since 1979. Supported by lower interest rates on their outstanding debt, their aggregate current account deficit therefore declined last year to \$ 45 billion. It was thus about \$ 30 billion less than the record amount registered in 1981. By far the greatest part of this improvement was accounted for by the threshold countries, which include Brazil, Mexico and Argentina as the countries most heavily in debt.

Considerable deterioration in the aggregate balance on current account of the OPEC countries

In contrast, there was a further deterioration in the aggregate balance on current account of the OPEC countries. After their aggregate current account surplus had risen to over \$ 110 billion in 1980, these countries registered a deficit of some \$ 15 billion as early as 1982. It may have increased to an estimated \$ 30 billion in 1983. The further deterioration in their current account position was partly due to the downward pressure on prices in international crude oil markets, which continued up to spring 1983 and led to lower OPEC selling prices as well. At the OPEC conference in London in March last year the agreed official benchmark price was lowered, for the first time since the price increases of 1973, from \$ 34 to \$ 29 per barrel, with the members simultaneously agreeing to counteract the declining price for oil by reducing their total output to a maximum of 17.5 million bpd and in addition keeping to specific country quotas. The further decline in sales had almost as strong a downward effect on the OPEC countries' oil receipts as their loss in earnings through low-

Current account balances of selected countries and groups of countries

US$ billion

Group of countries/Country	1978	1979	1980	1981	1982	1983p
A. OECD countries						
Seven major countries	+21	−11	− 34	− 1	− 7	−14
United States	−15	− 1	0	+ 5	− 11	−41
Japan	+17	− 9	− 11	+ 5	+ 7	+21
Canada	− 4	− 4	− 1	− 5	+ 2	+ 3
Germany	+ 9	− 6	− 16	− 6	+ 3	+ 4
France	+ 7	+ 5	− 4	− 5	− 12	− 4
United Kingdom	+ 2	− 1	+ 7	+13	+ 9	+ 3
Italy	+ 6	+ 5	− 10	− 8	− 6	+ 2
Other countries	− 9	−18	− 36	−26	− 23	−10
Total	+13	−28	− 70	−28	− 30	−24
B. OPEC countries						
Low-population 1	+ 8	+34	+ 87	+57	0	−24
High-population 2	−10	+31	+ 23	− 5	− 17	− 8
Total	− 1	+65	+111	+52	− 16	−31
C. Other developing countries						
Threshold countries 3	−12	−25	− 40	−45	− 29	−20
Other countries	−14	−14	− 20	−31	− 36	−25
Total	−26	−39	− 60	−76	− 65	−45
D. Other non-OECD countries 4	−12	− 8	− 9	−10	+ 3	+ 4
E. Statistical discrepancy (Total A to D)	−27	−11	− 28	−62	−108	−97

1 Kuwait, Libya, Qatar, Saudi Arabia, United Arab Emirates and the non-member Oman. — 2 Algeria, Ecuador, Gabon, Indonesia, Iran, Iraq, Nigeria, Venezuela. — 3 Countries which in 1979 had a per capita income of at least US$ 1,500 and a share of the manufacturing sector in the gross domestic product of at least 20%: Argentina, Brazil, Chile, Hong Kong, Mexico, Singapore, South Korea, Taiwan, Uruguay. — 4 Centrally planned economies (China, Indo-Chinese countries, Mongolia, North Korea, eastern European countries, USSR), Malta, South Africa, Yugoslavia. — p Provisional.
Sources: OECD, IMF and national statistics.

er prices. After the volume of their exports had already fallen by an average of 17% per year from 1980 to 1982, it declined again by 8% in 1983, thus falling to only half the amount exported in 1979. The renewed drop in OPEC countries' sales was chiefly due to the fact that both for structural and for cyclical reasons oil consumption in the OECD countries initially continued to decline before reviving noticeably at the end of 1983, for the first time since 1979. Moreover, as a result of the rising level of oil production in other countries, the members of OPEC once again lost market shares. The high-population OPEC countries, which had recorded considerable current account deficits already in 1982, initiated vigorous adjustment measures as a consequence, like the most heavily indebted developing countries. They reduced the volume of their imports by an estimated 15%. Despite their falling export revenues, they were able even to improve their current account balances as a result. In contrast, the OPEC countries with low populations but large reserves more or less maintained the volume of their imports. For this reason the aggregate current account position of this group of countries, which primarily includes Saudi Arabia and the relatively small countries bordering on the Gulf, deteriorated last year to a much greater extent than the current account position of all the OPEC countries taken together, and moved into considerable deficit, for the first time since the oil price increases of 1973.

Polarisation of current account developments among the industrial countries

Mirroring the decline in the OPEC countries' oil revenue, the aggregate trade deficit both of the industrial countries and of the developing countries continued to fall last year. In the process, there was a slight improvement in the OECD countries' balance on current account, judging by present estimates, although developments varied widely within this group of countries.[1] The trade deficit of the United States increased to an unusually large extent, reflecting mainly a considerable decline in exports to Latin America (an important market for the United States); the consequences of the appreciation of the U.S. dollar; and a large rise in imports in line with the upswing in U.S. economic activity. Especially in the capital and consumer goods sectors, including vehicles, the foreign trade figures in 1983 deteriorated by a further $ 20 billion against the preceding year, whereas net oil imports did not fall so strongly as in 1982 owing to the revival in economic activity. According to provisional official figures, the U.S. deficit on current account last year grew as a result by $ 30 billion to $ 40 billion. Thus, the deficit on current account in the balance of payments of the United States increased to a far greater extent than in 1977. In so far as the weakness of the U.S. current account position is attributable to the exchange rate or to cyclical factors, it benefited — as already mentioned — the other industrial countries, and in particular Japan, whose current account surplus rose by $ 14 billion to $ 21 billion and would probably have increased even more strongly if it had not been for voluntary export restraints of various kinds. The current account positions of most other OECD countries also improved last year, albeit by no means only as a result of the influences emanating from the United States. France, for example, reduced the considerable current account deficit it still had in 1982 by two-thirds by cutting down the volume of imports. Since the second quarter of 1983 its current account balance has even been virtually in equilibrium. Apart from the current account of the United States, that of the United Kingdom was practically the only one to deteriorate. U.K. imports of industrial goods in particular rose sharply for cyclical reasons. As a result, the current account surplus of the United Kingdom, which was considerable in 1981 and 1982, declined last year to only $ 3 billion.

Improvement in the U.S. capital account

The sharp deterioration in the current account position of the United States had its counterpart in an improvement on capital account, with dollar rates on the foreign exchange markets firming up again. U.S. banks reduced the volume of their new lending to other countries from $ 109 billion in 1982 to only $ 25 billion in 1983. In contrast, new deposits with U.S. banks by non-residents declined only from $ 64 billion to $ 51 billion. Capital transactions between banks correspondingly resulted in inflows into the United States in 1983 which exceeded those of 1982 by $ 71 billion. This improvement not only offset the increase in the current account deficit but also made up for the considerable rise in inflows from unidentified transactions. The position "errors and omissions" in the U.S. balance of payments, which had previously been positive, declined against 1982 by no less than $ 34 billion. This could partly be associated with the fact that capital flight from the heavily indebted countries to the United States declined considerably or even came to a standstill.

3. Exchange rate developments and policy

Exchange rates determined by the strong dollar

The movement of exchange rates was determined again last year by forces that almost always operated in favour of the U.S. dollar and hence simultaneously against other major currencies. The outcome was a rise of 8% in the weighted external value of the U.S. dollar against 23 major trading partners on the basis of the Bundesbank's method of calculation (weighted with bilateral shares in foreign trade) in the course of the year. At the end of 1983 the U.S. currency was valued almost 20% higher than at the end of 1972, i.e. shortly before the dollar began falling, a process that did not cease until summer 1980 after a decline in its weighted external value of 12%. Not only in the case of the U.S. dol-

1 The current account balances of the industrial countries as a group in particular must be viewed with considerable caution ever since big gaps appeared in global current account data. Nevertheless, the changes in these balances ought to give a fairly reliable reflection of developments (see also the Reports of the Deutsche Bundesbank for the years 1981 and 1982).

Balance of payments of the United States

US$ billion

Item	1976	1977	1978	1979	1980	1981	1982	1983 p	Change in 1983 from 1982 p
A. Current account									
Merchandise trade									
Exports	114.7	120.8	142.1	184.5	224.2	237.0	211.2	200.2	−11.0
Imports	124.2	151.9	176.0	212.0	249.8	265.1	247.6	260.8	+13.1
Balance	− 9.5	− 31.1	− 34.0	− 27.6	− 25.5	− 28.1	− 36.4	− 60.6	−24.2
of which									
Capital goods	26.8	25.8	26.8	33.8	43.0	44.9	35.5	28.5	− 7.0
Automotive vehicles, parts and engines	− 4.6	− 5.8	− 9.3	− 8.0	− 10.4	− 11.1	− 17.2	− 23.8	− 6.6
Consumer goods (non-food)	− 9.1	− 12.9	− 18.5	− 17.7	− 17.8	− 22.3	− 24.8	− 30.8	− 6.0
Petroleum and products	− 33.5	− 43.6	− 40.7	− 58.5	− 76.3	− 73.7	− 55.0	e −48.5	+ 6.5
Other industrial supplies and materials	1.8	− 2.0	− 3.8	7.7	14.9	8.5	7.6	− 2.3	− 9.9
Services	18.7	21.2	23.6	32.2	33.0	39.6	33.2	28.4	− 4.8
Unilateral transfers	− 5.0	− 4.6	− 5.1	− 5.6	− 7.1	− 6.9	− 8.0	− 8.6	− 0.6
Balance on current account	4.2	− 14.5	− 15.4	− 1.0	0.4	4.6	− 11.2	− 40.8	−29.6
B. Capital account									
(Net capital imports: +)									
Private capital movements	− 25.7	− 16.2	− 26.8	− 7.0	− 33.4	− 25.1	− 22.7	33.7	+56.4
Bank transactions	− 10.4	− 4.7	− 17.5	6.4	− 36.1	− 41.7	− 45.1	26.3	+71.4
U.S. claims reported by U.S. banks	− 21.4	− 11.4	− 33.7	− 26.2	− 46.8	− 83.9	−109.3	− 25.0	+84.4
U.S. liabilities reported by U.S. banks	11.0	6.7	16.1	32.6	10.7	42.2	64.3	51.3	−13.0
Portfolio investment	− 4.8	− 2.5	0.8	1.6	4.6	4.5	5.2	9.7	+ 4.5
Direct investment	− 7.6	− 8.2	− 8.2	− 13.3	− 5.6	12.3	13.4	1.9	−11.5
Other transactions	− 2.9	− 0.9	− 2.0	− 1.7	3.7	− 0.2	3.9	2 −4.2	− 8.1
U.S. Government claims on non-residents	0.4	− 2.3	− 2.2	− 3.8	− 4.5	− 5.1	− 5.2	− 4.6	+ 0.6
Balance on capital account	− 25.3	− 18.5	− 29.0	− 10.8	− 37.9	− 30.2	− 27.9	29.1	+57.0
C. Statistical discrepancy	10.5	− 2.0	12.5	25.4	29.6	24.2	41.4	7.1	−34.3
D. Balance on official reserve transactions (A plus B plus C)	− 10.6	− 35.0	− 31.9	13.6	− 7.9	− 1.4	2.3	− 4.6	− 6.9
Official reserve assets 1	2.6	0.4	− 0.7	0.0	7.0	4.1	5.0	1.2	− 3.8
Liabilities to foreign official institutions (Increase: −)	− 13.1	− 35.4	− 31.2	13.6	− 14.9	− 5.5	− 2.7	− 5.8	− 3.1

1 Excluding SDR allocations. — **2** January to September; for the fourth quarter these transactions are still included in the statistical discrepancy. — **p** Provisional. — **e** Estimated.
Discrepancies in the totals are due to rounding.
Source: U.S. Department of Commerce.

lar but also with respect to other currencies, the movement of exchange rates last year contrasted noticeably with trends in current account positions as well as with other influences which, at least over the longer term, are believed to determine the direction and strength of the trend in a currency's exchange rate. Significant improvements in the current account balances of not a few European countries went hand in hand with a weakening of exchange rates or only slight rises in them. Japan's economic strength too was only partially reflected in the yen's exchange rate. As in the years following the transition of all major currencies to floating, this again raises the question as to the contribution of the exchange rate to the current account adjustment process. This relates not only to the equilibrating function of the exchange rate as an important price in macro-economic terms but also to its hardly less important function as an indicator for governments and central banks. At all events, the persistent strength of the U.S. dollar seems rather to have enhanced the determination of some policy-makers in the United States not to change the stance of economic and fiscal policy. Exchange rate developments did not, however, run counter only to adjustment needs. While the strength of the U.S. dollar helped the United States to finance its expansionary fiscal policy, it constituted an additional burden in some countries as regards the process of reducing interest rates. The discussions on the issue have revealed at the same time the desire to bring exchange rates back into more harmony with the requirements of a functioning adjustment process in the longer run, with the economic and monetary policies of all important countries helping towards this goal.

(a) Trends in major freely floating currencies

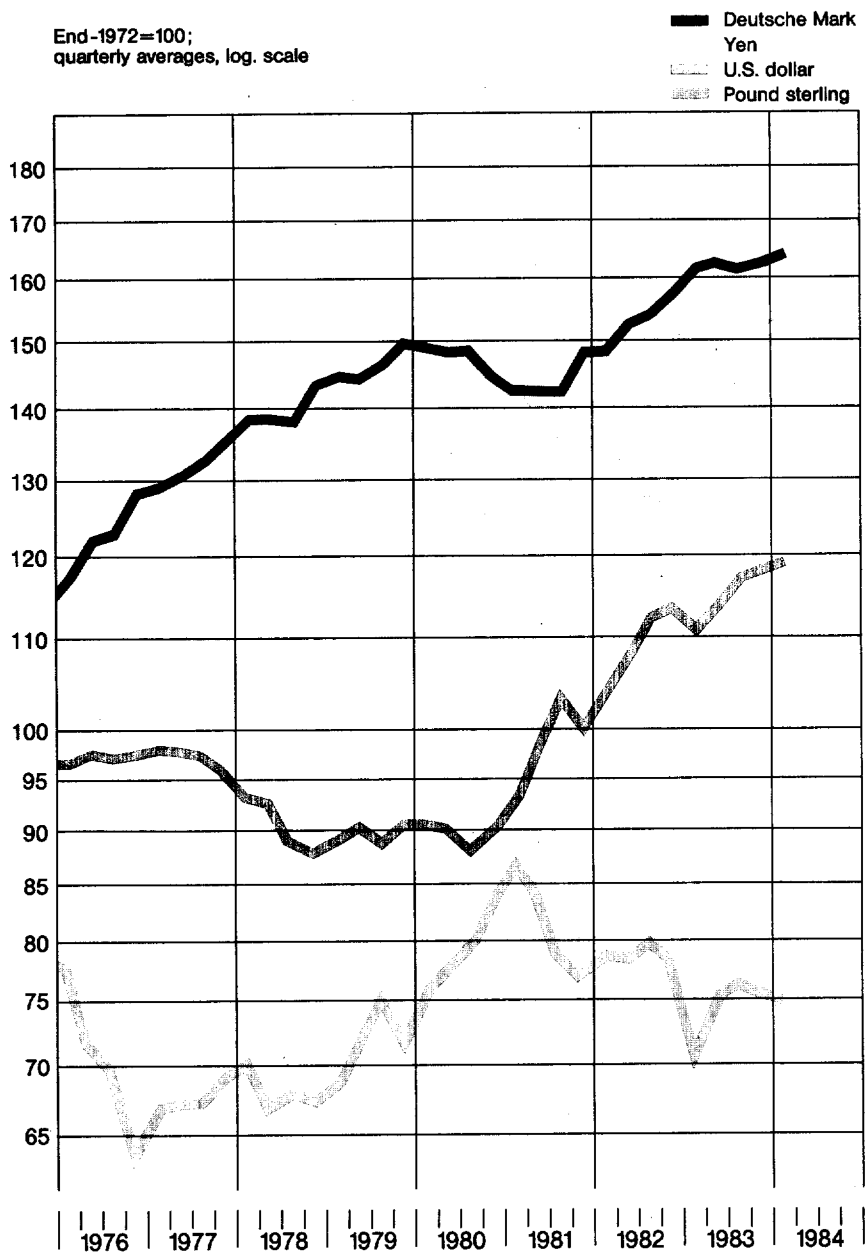
After further strengthening of the U.S. dollar . . .

The further strengthening of the U.S. dollar over the year 1983 was rather unexpected. Many observers considered in particular the sharp deterioration in the U.S. trade and current account balances, which since November 1982 had seemed to be a contributory factor to the temporary weakening of the U.S. dollar on the exchange markets, to be a lasting burden on the U.S. currency, especially since U.S. monetary policy was simultaneously becoming more expansionary. For one thing, the renewed rise in the U.S. dollar in spring 1983 was related to the return to higher interest rates and interest rate expectations in the United States. The stiffer conditions in the financial markets chiefly reflected the surge in economic activity in the United States. In addition, the hopes of an imminent correction in the stance of U.S. budget policy faded and the continuing sharp rise in monetary growth now tended to be viewed with concern. Moreover, the rise in U.S. share prices operated in favour of the U.S. dollar. As time went on, the dollar probably also profited from the marked decline in U.S. capital exports mentioned above. When the rising trend of the U.S. dollar accelerated considerably at the end of July, the central banks of the major countries jointly resisted this development by selling large amounts of dollars in some cases. However, these measures did not have a lasting effect. By the end of last year the U.S. dollar had again made good the intermittent weakening of its weighted external value and initially rose further. Factors of a non-economic nature played a role in this process. It remains to be seen whether the decline in the dollar rate from February 1984 onwards has initiated the reversal in trend on the exchange markets that is generally expected.

. . . Deutsche Mark valued at low level

The Deutsche Mark lost more in value vis-à-vis the U.S. dollar last year than other major currencies. The decline in its rate against the U.S. currency amounted to 13%. The exchange rate of the Deutsche Mark accordingly also declined against most other freely floating currencies, especially the yen and

Weighted external value of major currencies*



* Against the currencies of 23 countries in each case; geometrically weighted in accordance with the average regional pattern of foreign trade turnover (exports plus imports) from 1978 to 1980.

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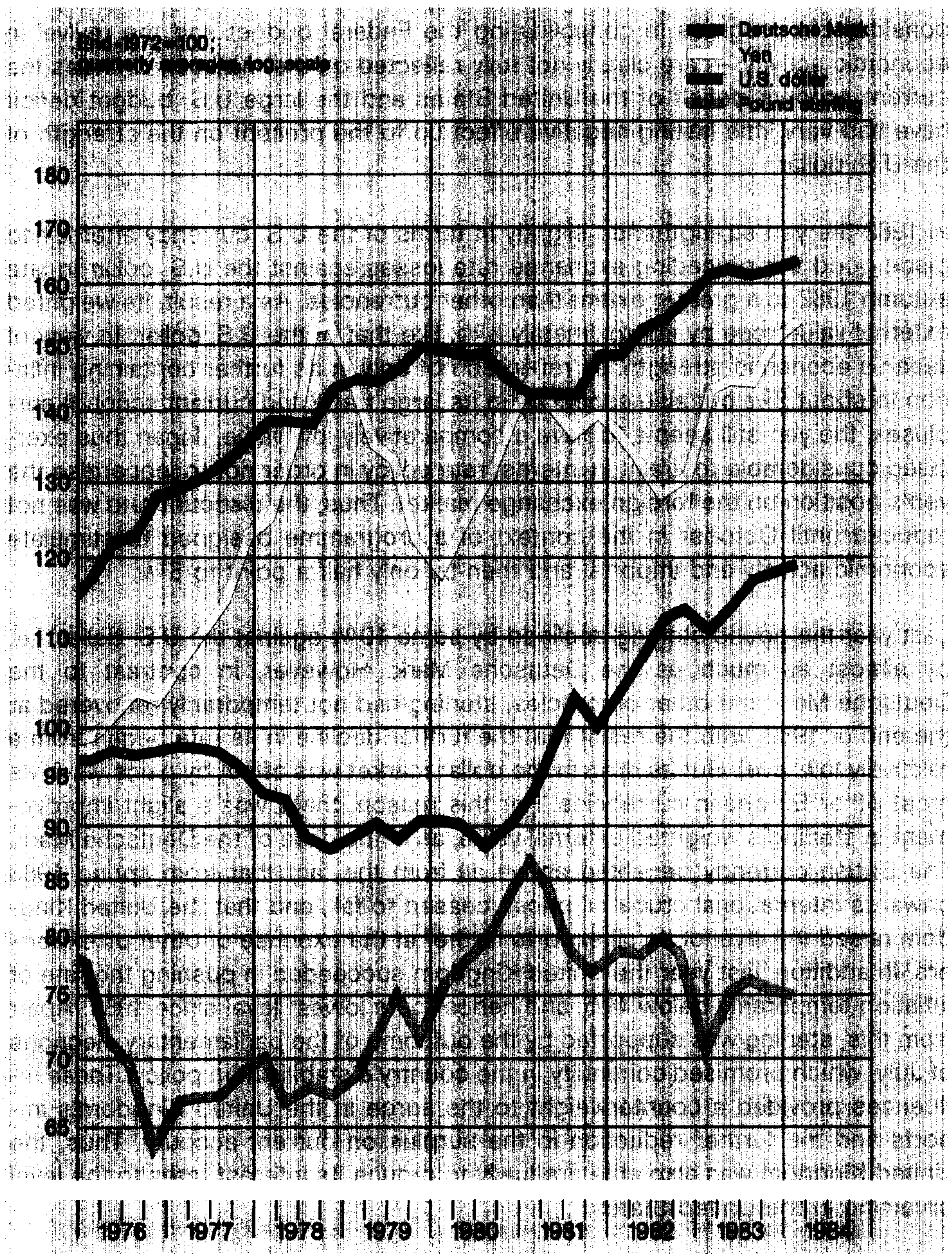
Weighted external value of major currencies*



* Against the currencies of 23 countries in each case; geometrically weighted in accordance with the average regional pattern of foreign trade turnover (exports plus imports) from 1978 to 1980.

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Fundamental strength of the yen only partly visible in its exchange rate

In 1983 the yen strengthened slightly in terms of the U.S. currency after it had made good the preceding exchange rate losses against the U.S. dollar in late autumn 1982 to a greater extent than other currencies. As a result, its weighted external value rose by approximately 8%, like that of the U.S. dollar. In view of Japan's economic strength, as reflected not only in its further containing inflation to about 2% but also especially in its large trade and current account surpluses, the yen still seems to have a comparatively low value. Japan thus exercised considerable restraint in interest rate policy in order not to jeopardise the yen's position on the foreign exchange market. Thus, the discount rate was not reduced until October in the context of a programme designed to stimulate economic activity and imports, and then by only half a point to 5%.

Sterling holds up well

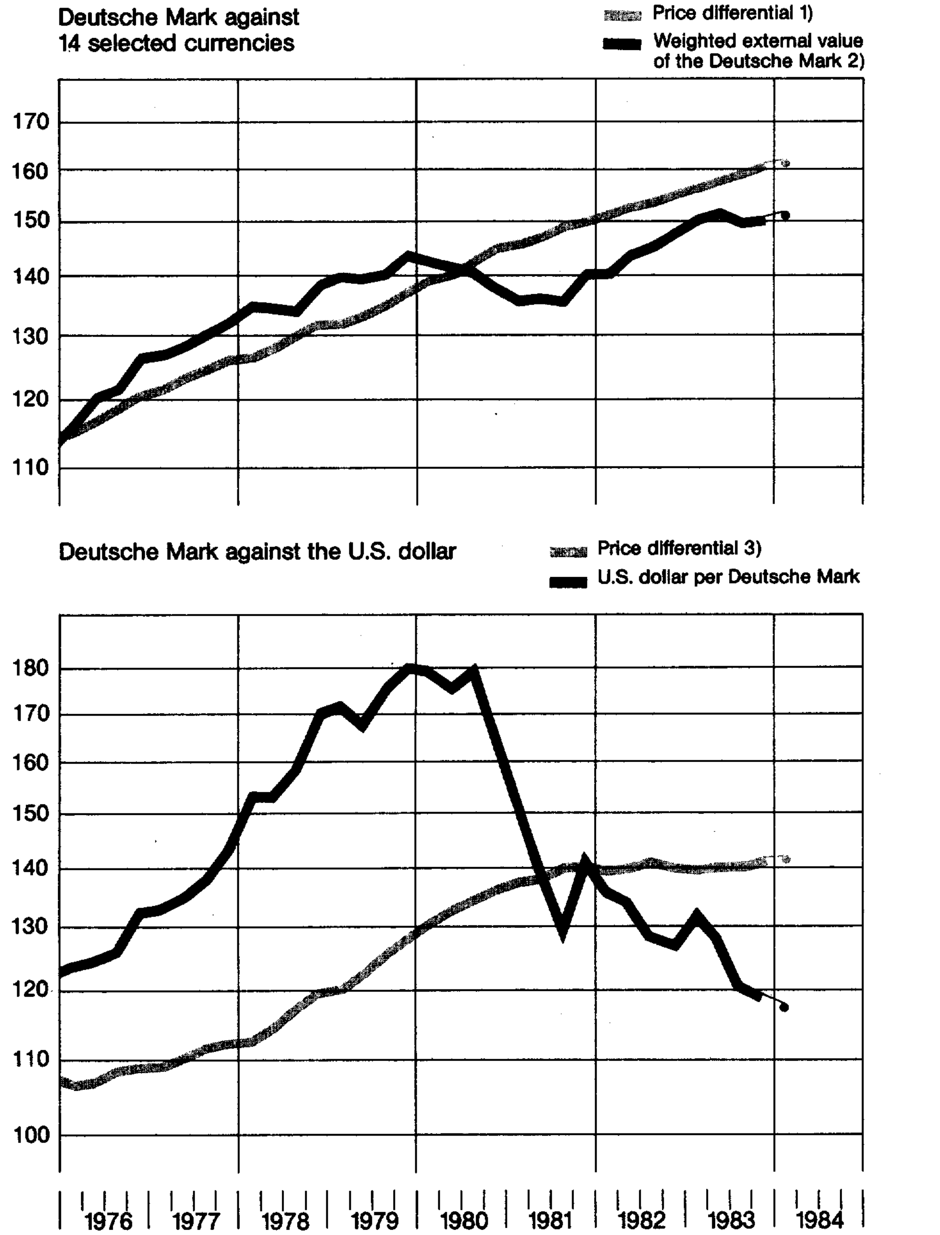
Last year the pound sterling declined by some 10% against the U.S. dollar, i.e. by almost as much as the Deutsche Mark. However, in contrast to the Deutsche Mark and other currencies, sterling had not temporarily recovered at the end of 1982, with the result that the further decline in its rate began from a relatively low level. But its drop in the dollar market was offset by gains vis-à-vis most other European currencies. For this reason, there was a slight improvement in sterling's weighted external value, as in the case of the Deutsche Mark. The British currency benefited above all from the fact that from spring 1983 onwards international crude oil prices ceased to fall, and that the United Kingdom raised the level of its oil exports further at the expense of other oil exporters. In addition, last year the United Kingdom succeeded in pushing the rate of inflation temporarily below 4%, and hence to its lowest level since 1968. Apart from this, sterling was supported by the outcome of the parliamentary elections of July, which promised continuity in the country's stabilisation policy. These influences provided a counterweight to the surge in the United Kingdom's imports and the further reduction in the surplus on current account. Thus, the United Kingdom was also able gradually to reduce its interest rates to the level obtaining in the United States.

Swiss franc again strongest European currency

Of all the European currencies, the Swiss franc declined least against the U.S. dollar in 1983. The fall in its rate, at 8%, amounted to only two-thirds of the decline in the Deutsche Mark's position vis-à-vis the U.S. currency. The improvement in its exchange rate vis-à-vis most other currencies was correspondingly greater. In fact, the weighted external value of the Swiss franc rose by 6%. However, the gain of 5% against the Deutsche Mark only offset the preceding year's loss. As a result, the Swiss franc again came close to its historical record level. Whereas in 1982 a considerable interest rate differential had developed between Switzerland and Germany in favour of the Deutsche Mark, the interest rate differential between the two currencies became noticeably smaller last year. This was also reflected in the development of official interest rates. When the Bundesbank lowered its discount rate by 1 percentage point in March 1983, the Swiss National Bank followed with a reduction of only half a point.

External value of the Deutsche Mark and inflation differentials

December 1972=100, quarterly averages, log. scale



1) Geometric mean, weighted with foreign trade turnovers (exports plus imports), of the movement of consumer prices in 14 other industrial countries relative to that in the Federal Republic of Germany.- 2) Geometrically weighted mean against the currencies of 14 other industrial countries.- 3) Movement of consumer prices in the United States relative to that in the Federal Republic of Germany.- Latest position: February 1984.

(b) Developments within the European Monetary System

Relatively long period of weakness of the Deutsche Mark following the March 1983 realignment . . .

Following the realignment of central rates in March 1983, which — as already mentioned in the Report for the Year 1982 — involved a revaluation of the Deutsche Mark against all other currencies in the system, the Deutsche Mark remained decidedly weak into August. The Deutsche Mark was frequently at its lower intervention point within the band, especially vis-à-vis the French franc, which had come under most pressure before the realignment. The German currency was supported by considerable purchases of Deutsche Mark. In addition, the Banque de France and other central banks bought large amounts of Deutsche Mark via intramarginal interventions. Although the initial weakness of the Deutsche Mark on the foreign exchange market corresponded to earlier experience with revaluations, this time it persisted for a comparatively long period. After the realignment of central rates, the Deutsche Mark came under pressure not only because the leads and lags in foreign trade operating against the currencies that were devalued now reversed direction and, moreover, short-term Deutsche Mark positions were unwound. Above and beyond this, other outflows of short- and long-term capital evidently took place as well. The Bundesbank's net external position deteriorated by about DM 17 billion up to the end of April as a result of obligatory and intramarginal support operations within the EMS in favour of the Deutsche Mark. The impact of these outflows was unquestionably desirable in terms of liquidity policy because they helped to restrain the growth of the money supply. In the course of the remaining part of the year our EMS partners continued to take advantage of the pattern of exchange rates, which was in their favour, to undertake additional purchases of Deutsche Mark. A large part of the Deutsche Mark acquired by foreign central banks in this way was invested in the market with the agreement of the Bundesbank, and to this extent did not increase the Bundesbank's Deutsche Mark liabilities to monetary authorities abroad. The total amount of Deutsche Mark purchases undertaken since the realignment was therefore much larger than is reflected in the net external position of the Bundesbank. From the realignment of central rates up to the end of 1983 total net Deutsche Mark purchases amounted to about DM 30 billion. By contrast, from the beginning of the year up to the realignment the corresponding sales of Deutsche Mark totalled only about DM 16 billion. The only interventions to have an impact on bank liquidity in Germany, of course, were those which led to changes in the Bundesbank's net external position.

. . . provides relief for partner countries

The only gradual appreciation of the Deutsche Mark on the foreign exchanges made it easier for German industry to adjust to the new central rates, as the most recent revaluation of the Deutsche Mark distinctly exceeded the inflation differentials that had arisen since the realignment. It was of help to the partner countries that they could utilise the amounts of Deutsche Mark which they took up on the market to repay quickly the liabilities they had previously incurred with the European Monetary Cooperation Fund. The corresponding claim which the Bundesbank had on the EMCF, which had risen to the ECU equivalent of DM 6.2 billion before the realignment, was thus offset by the end of June. As mentioned above, the other central banks were also able to increase or replenish their gross monetary reserves. It was not least the weakness of the Deutsche Mark that made it possible for most partner countries to reduce their interest rates considerably after the realignment. The most marked fall in interest rates occurred in Belgium, where the discount rate had been lowered by 5 percentage points by June 1983. This could, however, have strengthened the conviction of the markets that the Belgian monetary authorities were determined to exploit any scope for cutting interest rates. Both this and the hitherto unsatisfactory progress made in consolidating public budgets may help to account for the Belgian franc's marked tendency towards weakness against all other EMS currencies since autumn 1983, a weakness which is persisting despite a clear improvement in Belgium's current account.

Persistent economic divergences

In recent years the accelerated pace at which realignments have occurred has signalled the danger that the EMS could become a system of crawling pegs that only passively registers persistent divergences in the economic development and economic policy of the participating countries and seeks to offset them by realigning the central rates of their currencies. Over the longer term, such a process has to be averted. It is true that progress has been achieved, especially with respect to current account positions. The five EMS countries of France, Italy, Belgium, Denmark and Ireland, which still had large current account deficits in 1982, have meanwhile improved their positions considerably. Their aggregate deficit on current account has fallen from $ 24 billion to $ 5 billion. In other major fields, however, there continues to be a lack of comparable

Changes in the net external position of the Bundesbank due to operations in the foreign exchange market and other foreign exchange movements*

DM billion

Period	Net external position, total	Operations in the exchange market: Deutsche Mark/ dollar market **1**	Operations in the exchange market: EMS **2**	Other foreign exchange movements
1982				
January 1 to February 21 **3**	− 1.5	− 1.3	− 0.6	+ 0.4
February 22 to June 13 **3**	+ 3.4	− 1.6	+ 4.4	+ 0.6
June 14 to December 31	+ 1.3	− 3.7	− 0.2	+ 5.2
1982, total	+ 3.2	− 6.6	+ 3.7	+ 6.2
1983				
January 1 to March 20 **3**	+17.1	+ 0.4	+12.5	+ 4.2
March 21 to April 30	−16.6	− 2.1	−16.8	+ 2.3
May 1 to August 31	− 4.8	− 7.2	− 3.5	+ 5.9
September 1 to December 31	+ 0.3	− 5.8	+ 0.0	+ 6.1
1983, total	− 4.0	−14.7	− 7.8	+18.5
1984				
January 1 to March 31	+ 7.1	− 2.4	+ 4.4	+ 5.0

* Excluding liquidity swaps and changes due to valuation adjustments. Recorded according to the date on which the transaction was conducted and not according to the value date; discrepancies between these figures and those of the balance of payments are therefore possible. — **1** Including U.S. interventions. — **2** Including Deutsche Mark interventions by other central banks, where they affect the external position of the Bundesbank. — **3** Last day before new central rates in the EMS became effective.
Discrepancies in the totals are due to rounding.

progress in the direction of greater convergence. Although the rate of price increases has slowed down further in all the partner countries, in most cases it is still far too high and there has been hardly any reduction in the discrepancies in price movements between the more stable countries and the others. As regards public sector budgets, in a number of important EMS countries there seems to have been no progress whatsoever in the process of consolidating them. Moreover, the fact that individual countries still maintain exchange control restrictions and special exchange rate arrangements must not be overlooked. Progress towards greater economic convergence can be measured not least by the rate at which such protective measures are dismantled. The considerable increase in public sector foreign debt in a number of countries is also an indication that efforts to adjust must not be relaxed. In addition, over the last twelve months persistent divergences in economic developments made themselves felt to a relatively slight degree only because the strength of the U.S. dollar constituted a burden on the Deutsche Mark in particular.

Proposals on strengthening private use of the ECU

With the aim of encouraging greater progress towards monetary integration, the EEC Commission recently proposed that the private use of the ECU should be fostered in the member states. Above all, it expects that this would bring about progress in integrating capital markets. To this end the ECU should be equated with a foreign currency in all the member states of the Community. In fact, an international market has meanwhile developed, which specialises in ECU issues. Since no capital controls of any kind exist in Germany, residents can purchase and hold ECU-denominated financial assets. In other countries of the Community, in contrast, there are considerable restrictions on the use of the ECU as an investment instrument under the foreign exchange legislation that applies there. In Germany, however, only very limited use has evidently been made of this investment option up to the present. Although ECU assets yield a slightly higher amount in terms of nominal interest than Deutsche Mark assets with a comparable period to maturity, it has to be borne in mind that owing to the repeated revaluations of the Deutsche Mark within the EMS the Deutsche Mark equivalent of ECU-denominated securities has declined over a relatively long period of time. Depending on the base period chosen, the advantage of an ECU-denominated investment in terms of its interest yield is therefore distinctly smaller or may even be more than offset. German investors seeking an alternative to the Deutsche Mark would probably tend to prefer greater opportunities to make a profit than ECU investments are able to offer. Only incurring ECU-denominated liabilities is subject to restrictions in Germany. In this context, a role is played by the fact that under existing regulations the ECU cannot be considered a currency and also cannot be necessarily equated with a currency. It is seen as a unit of account whose value is determined by the development of the exchange rate of other currencies. It is correspondingly subject to Section 3 of the Currency Act, under which the approval of the Bundesbank is required for residents to incur index-linked Deutsche Mark liabilities. The Bundesbank has not granted such approval in the past, in order to keep financial transactions in Germany free of index clauses. Incidentally, there is no evidence that the process of European integration could be fostered by the ECU serving as a sort of "parallel currency". At all events, the basic problem within the Community, namely the persistent divergences in economic developments between the member states and the lack of will to take the necessary corrective steps, cannot be papered over in this way.

(c) Exchange market intervention policy

International study of intervention policy

After the Heads of State and Government of the seven major industrial countries had pledged at the Versailles summit in June 1982 to work jointly for greater stability of the world monetary system, it was initially agreed to have a group of experts conduct a thorough analysis of experience with exchange market intervention as a means of stabilising exchange rates under a system of floating rates. The study was commissioned mainly in reaction to the change in U.S. intervention policy in spring 1981. Whereas at the end of 1977, when the dollar came under considerable downward pressure, the United States began to intervene much more actively on the foreign exchange market in coordination with its partner countries, the Reagan Administration practically ceased the intervention activities of the United States shortly after taking office. It justified this step by expressing its conviction that the foreign exchange markets functioned best if they were left to themselves; in addition, it pointed out the danger of possible conflicts between exchange market interventions and a monetary policy geared to stability, and emphasised in particular its intention to achieve greater stability both of the dollar and of the foreign exchange markets above all through an improvement in the economic fundamentals. Most of the partners of the United States also by no means considered exchange market intervention to be one of the main instruments of exchange rate policy. Cooperation in intervention policy included for them the willingness to seek a minimum of coordination also in other fields that play a role in the development of exchange rates. The question therefore arose as to how far the usefulness of intervention in stabilising exchange rates can be confirmed and a tool of international cooperation perhaps be strengthened again.

Limited usefulness of intervention

The Group entrusted with the study and comprising experts from the finance ministries and central banks of the seven summit countries as well as one representative each of the EEC Commission and EEC Presidency submitted its report in March 1983. The major conclusions of the report can be summarised in four points:

— Exchange rates can be influenced more effectively through intervention over the short run and temporarily than over the longer run.

- Longer-term exchange rate stability is fostered better by an economic policy geared to stability than by intervention.

- Coordinated intervention can be more effective than the same total amount of intervention by a single country, but the conditions for successful coordination are exacting.

- Monetary authorities may from time to time jointly come to the conclusion that certain exchange rates have moved away from their underlying trend determined by the fundamentals, even though intervention is unable to achieve much in terms of countering such a movement.

Bundesbank's policy confirmed

These conclusions coincide with the view held by the Bundesbank from the outset, which is that intervention can be useful under certain circumstances but that its effectiveness does not simply depend on the scale of intervention operations but is also determined by factors relating to market psychology and signal effects whose impact is the greater the better monetary authorities cooperate internationally in conducting such operations. The conclusions of the study also underline the necessity constantly emphasised by the Bundesbank of monetary, fiscal and economic policies being compatible with the objectives of operations on the foreign exchange market.

Williamsburg decisions on exchange rate policy only reaffirmation of traditional policies

The finance ministers and central bank governors of the seven summit countries saw in the results of the Intervention Study a confirmation of the necessity, in the interests of greater exchange rate stability, of gearing policies designed to foster non-inflationary growth at the national level to jointly agreed measures and, moreover, of taking greater account of the international implications of domestic economic policies. In addition, they emphasised their readiness to intervene jointly on the exchange markets if there was agreement that such action would be helpful. The Heads of State and Government supported this policy at their conference in Williamsburg in May 1983. In principle, this took full account of Germany's position in particular, which admittedly only means that insights already gained in the past were reaffirmed at the highest level. Ever since floating began all major decisions and announcements concerning exchange rate and intervention policy have attributed a certain role in stabilising exchange rates to the exchange market operations of central banks. At the same time, however, it has always been emphasised that durable international monetary stability presupposes greater consistency and convergence in the economic policies of the major countries.

No change in the Bundesbank's intervention policy

Last year the Bundesbank again did not attempt to counteract the persistent pressure on the Deutsche Mark/dollar rate to any great extent through exchange market intervention. Although the overall amount of U.S. dollars it sold on the exchange market was considerable, these sales were still smaller than the Bundesbank's receipts of U.S. dollars from the interest payments on its invested foreign exchange reserves as well as from other transactions outside the exchange market (see also the table on p. 69). Without these recycling operations the process of self-regulation of the market, which is not always easy under a floating rate system, would probably have been made even more difficult, quite apart from the fact that Germany's monetary reserves would have risen considerably, which, given the weak tendency of the Deutsche Mark, would have been in keeping neither with the international rules on managing floating exchange rates nor with domestic liquidity and monetary policy needs.

Major decisions and announcements on exchange rate and intervention policy since the beginning of floating

Paris, March 16, 1973

Communiqué on the monetary conference of the enlarged Group of Ten (excerpts)

3. The ministers and central bank governors took note of the decisions of the members of the EEC announced on Monday (March 11, 1973). Six members of the EEC and certain other European countries, including Sweden, will maintain 2¼ % margins between their currencies. The currencies of certain countries, such as Italy, the United Kingdom, Ireland, Japan and Canada, remain, for the time being, floating. However, Italy, the United Kingdom and Ireland have expressed the intention of associating themselves as soon as possible with the decision to maintain EEC exchange rates within margins of 2¼ % and meanwhile of remaining in consultation with their EEC partners.
5. (Ministers and governors) agreed in principle that official intervention in exchange markets may be useful at appropriate times to facilitate the maintenance of orderly market conditions . . . Each nation stated that it will be prepared to intervene at its initiative in its own market, when necessary and desirable, acting in a flexible manner in the light of market conditions and in close consultation with the authorities of the nation whose currency may be bought or sold . . .
10. Ministers and governors expressed their unanimous conviction that international monetary stability rests, in the last analysis, on the success of national efforts to contain inflation. They are resolved to pursue fully appropriate policies to this end.

Washington, June 13, 1974

Decision of the Executive Board of the IMF on Guidelines for the Management of Floating Exchange Rates (excerpts)

These Guidelines are based on the assumption that in any situation of floating it may be desirable (a) to smooth out very short-run fluctuations in market rates and (b) to offer a measure of resistance to market tendencies in the slightly longer run, particularly when they are leading to unduly rapid movements in the rate, and (c) to the extent that it is possible to form a reasonable estimate of the medium-term norm for a country's exchange rate, to resist movements in market rates that appear to be deviating substantially from that norm. Guidelines of this kind are necessary, inter alia, in order to arrive at a clear conception of what competitive exchange alteration is, and to provide safeguards against it.

The Guidelines

1. A member with a floating exchange rate should intervene on the foreign exchange market as necessary to prevent or moderate sharp and disruptive fluctuations from day to day and from week to week in the exchange value of its currency.
2. . . ., a member with a floating rate may act, through intervention or otherwise, to moderate movements in the exchange value of its currency from month to month and quarter to quarter, and is encouraged to do so, if necessary, where factors recognized to be temporary are at work . . ., the member should not normally act aggressively with respect to the exchange value of its currency (i. e., should not so act as to depress that value when it is falling, or to enhance that value when it is rising).
6. Members with a floating rate will bear in mind, in intervention, the interests of other members including those of the issuing countries in whose currencies they intervene. Mutually satisfactory arrangements might usefully be agreed between the issuers and users of intervention currencies, with respect to the use of such currencies in intervention . . .

Certain of the terms used in the guidelines may be defined as follows:

ii) "Exchange market intervention" would normally be measured by the movement of reserves, adjusted as appropriate for compensatory official borrowing. Consideration might also be given to including in the concept of intervention changes in official foreign exchange positions other than reserves.

Rambouillet, November 17, 1975

Declaration of the Heads of State and Government of the six principal industrial countries (excerpt)

12. With regard to monetary problems, we affirm our intention to work for greater stability. This involves efforts to restore greater stability in underlying economic and financial conditions in the world economy. At the same time, our monetary authorities will act to counter disorderly market conditions, or erratic fluctuations in exchange rates . . .

Washington, April 30, 1976

Article IV of the Second Amendment to the Articles of Agreement of the IMF, which was approved by the Board of Governors and entered into force on April 1, 1978 (excerpts)

Section 1 – General obligations of members regarding exchange arrangements

In particular, each member shall:

i) endeavour to direct its economic and financial policies toward the objective of fostering orderly economic growth with reasonable price stability, with due regard to its circumstances;
ii) seek to promote stability by fostering orderly underlying economic and financial conditions and a monetary system that does not tend to produce erratic disruptions;
iii) avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members; and
iv) follow exchange policies compatible with the undertakings under this Section.

Section 3 – Surveillance over exchange arrangements

a) The Fund shall oversee the international monetary system in order to ensure its effective operation, and shall oversee the compliance of each member with its obligations under Section 1 of this Article.
b) In order to fulfil its functions under (a) above, the Fund shall exercise firm surveillance over the exchange rate policies of members, and shall adopt specific principles for the guidance of all members with respect to those policies . . .

Washington, April 29, 1977

Decision of the Executive Board of the IMF on the implementation of Article IV of the proposed Second Amendment to the Articles of Agreement of the IMF (excerpt)

Principles for the Guidance of Members' Exchange Rate Policies

A. A member shall avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members.
B. A member should intervene in the exchange market if necessary to counter disorderly conditions which may be characterized inter alia by disruptive short-term movements in the exchange value of its currency.
C. Members should take into account in their intervention policies the interests of other members, including those of the countries in whose currencies they intervene.

Washington, April 16, 1981

Press release by the U.S. Treasury

The U.S. monetary authorities have decided to keep intervention to a minimum, intervening at the most when disorderly exchange market conditions make it appear necessary. Treasury Undersecretary Sprinkel justified this policy on May 4, 1981 before the Joint Economic Committee of Congress. He emphasized that the Administration was aiming at greater stability in the dollar and the exchange markets, primarily through an improvement in underlying economic conditions.

Versailles, June 6, 1982

Declaration of the seven Heads of State and Government and representatives of the European Community (excerpt)

It is essential to intensify our economic and monetary cooperation. In this regard, we will work towards a constructive and orderly evolution of the international monetary system by closer cooperation among the authorities representing the currencies of North America, of Japan and of the European Community in pursuing medium-term economic and monetary objectives. In this respect we have committed ourselves to the undertakings contained in the attached statement.

Statement of international monetary undertakings (excerpt)

1. We accept a joint responsibility to work for greater stability of the world monetary system. We recognize that this rests primarily on convergence of policies designed to achieve lower inflation, higher employment and renewed economic growth, and thus to maintain the internal and external values of our currencies. We are determined to discharge these obligations in close collaboration with all interested countries and monetary institutions.
2. We attach major importance to the role of the IMF as a monetary authority and we will give it our full support in its efforts to foster stability.
3. We are ready to strengthen our cooperation with the IMF in its work of surveillance, and to develop this on a multilateral basis taking into account particularly the currencies constituting the SDR.
4. We rule out the use of our exchange rates to gain unfair competitive advantages.
5. We are ready, if necessary, to use intervention in exchange markets to counter disorderly conditions, as provided for under Article IV of the IMF Articles of Agreement.

Washington, April 29, 1983

Statement of the finance ministers and central bank governors of the seven summit nations and the representative of the EEC on the Intervention Study (excerpt)

We have reached agreement on the following:

A. The achievement of greater exchange rate stability, which does not imply rigidity, is a major objective and commitment of our countries.
B. The path to greater exchange rate stability must lie in the direction of compatible mixes of policies supporting sustainable non-inflationary growth. This will be the primary objective of a strengthened multilateral surveillance as agreed in Versailles.
C. In the formulation of our domestic economic and financial policies, our countries should have regard to the behaviour of our exchange rates, as one possible indication of need for policy adjustment. Close attention should also be given to the interactions and wider international implications of policies in each of our countries.
D. Under present circumstances, the role of intervention can only be limited. Intervention can be useful to counter disorderly market conditions and to reduce short-term volatility. Intervention may also on occasion express an attitude towards exchange markets. Intervention will normally be useful only when complementing and supporting other policies. We are agreed on the need for closer consultations on policies and market conditions; and, while retaining our freedom to operate independently, are willing to undertake coordinated intervention in instances where it is agreed that such intervention will be helpful.

Williamsburg, May 30, 1983

Declaration of the Heads of State and Government of the seven summit nations and the representative of the EEC on economic recovery (excerpts)

In pursuance of these objectives, we have agreed as follows:

2. The consultation process initiated at Versailles will be enhanced to promote convergence of economic performance in our economies and greater stability of exchange rates, on the lines indicated in an annex to this Declaration. We agree to pursue closer consultations on policies affecting exchange markets and on market conditions. While retaining our freedom to operate independently, we are willing to undertake coordinated intervention in exchange markets in instances where it is agreed that such intervention would be helpful.
5. We have invited ministers of finance, in consultation with the Managing Director of the IMF, to define the conditions for improving the international monetary system and to consider the part which might, in due course, be played in this process by a high-level international monetary conference.

Annex to the above Declaration (excerpts)

B. In accordance with the agreement reached at Versailles, we are focusing our attention on issues in the monetary and financial fields including interaction with policies in other areas. We shall take fully into account the international implications of our own policy decisions. Policies and objectives that will be kept under review include:
3. Exchange Rate Policy. We will improve consultations, policy convergence and international cooperation to help stabilize exchange markets, bearing in mind our conclusions on the Exchange Market Intervention Study.

(d) Issues relating to the international monetary system

Institutional limitations to scope for exchange rate movements between major currencies not possible

At the Williamsburg summit it was also decided to explore the possibilities of improving the international monetary system and to examine what part could be played by a high-level international monetary conference at an appropriate time. This task has meanwhile been entrusted to the Group of Ten, which will base its contribution on the work conducted beforehand by various international organisations. Three issues in particular are to be given detailed study, namely the causes behind excessive exchange rate fluctuations, the possibilities of strengthening the role of the IMF in supervising the exchange rate and economic policies of its members and in fostering the adjustment process, and problems relating to international liquidity. It appears that these studies have been associated in some quarters with the expectation that it is possible to place institutional limitations on the movement of exchange rates between the major currencies in some way. However, such ideas are bound to encounter considerable doubts, particularly in Germany, whose currency plays an important role as an international investment and reserve instrument. In view of their present-day scale, shifts in international financial flows cannot be kept under control without adequate flexibility in exchange rates. In order to make exchange rates more stable, it is therefore necessary above all to come to grips with the factors behind disruptive capital movements, the way being pointed in this direction by the decisions taken at recent summit conferences. What safeguards and flanking measures for exchange rate policy might be appropriate will probably not be a subject for serious consideration until the fundamental economic conditions in the major countries have converged so closely that a high degree of exchange rate stability can be justified and basically expected.

4. The development of global monetary reserves

Renewed rise in global monetary reserves

In 1983 the identified gross monetary reserves of the IMF countries increased by $ 23 billion after having suffered a considerable decline in the two preceding years, for the first time since 1959. However, the reduction in 1981 and 1982, by a total amount of $ 46 billion, was largely due to valuation adjustments. The fall in the gold price had led to a considerable decline in the ECU balances created by depositing gold with the European Monetary Cooperation Fund on the basis of a market-related valuation. Moreover, owing to exchange rate movements there was a decline in the U.S. dollar equivalent of the value of reserves held in currencies other than the U.S. dollar. If these influences are ignored, then the decline in global reserves is reduced to only $ 8 billion. In contrast, the sharp rise they registered in 1983 was due to real reserve creation that was only mitigated by valuation adjustments. Excluding changes in value, global monetary reserves actually increased by an estimated $ 28 billion.

Increase in foreign exchange reserves and IMF reserve positions

An increase in the foreign exchange holdings of central banks constituted the main component in the growth of monetary reserves in 1983. Calculated at current exchange rates, foreign exchange holdings rose by $ 10.4 billion, primarily through a rise in holdings of U.S. dollars. In addition, reserve positions in the IMF went up by $ 13 billion. $ 6 billion was accounted for by the latest increase in quotas, which became effective for most members last December through corresponding subscription payments (a quarter of which are usually in SDRs). To this extent, however, only the composition, but not the level, of global monetary reserves has changed. Only the increase in reserve positions in the IMF above and beyond the increase in quotas reflecting drawings on the Fund by countries in a weak balance of payments position and based on a corresponding growth of the reserve claims of the creditor countries in the IMF constitutes an increase in gross global monetary reserves. The aggregate reduction in members' holdings of SDRs was at the same time somewhat lower than the reduction associated with the increase in quotas, because the Fund fi-

Gross monetary reserves of IMF countries *

US$ billion

Type of reserves/Group of countries	Level at end of year 1980	1983 p	Change in course of year 1981	1982	1983 p
A. Type of reserves					
Gold **1**	40.2	39.9	− 0.0	− 0.2	− 0.1
Special drawing rights	15.1	15.1	+ 4.0	+ 0.5	− 4.5
Reserve position in the IMF	21.5	40.9	+ 3.3	+ 3.3	+12.9
ECU balances	63.7	45.3	−13.5	− 8.9	+ 3.9
— against gold	47.6	33.8	−10,2	− 7.0	+ 3.4
— against U.S. dollars	13.9	10.6	− 2.4	− 1.8	+ 0.9
— arising from very short-term financing	2.2	0.9	− 0.9	− 0.0	− 0.4
Foreign exchange	310.1	286.5	−12.3	−21.6	+10.4
U.S. dollars	197.3	(175.1)	− 9.1	−20.9	(+ 7.8)
Deutsche Mark	40.8	(26.5)	− 6.3	− 5.3	(− 2.7)
Yen	10.6	(9.1)	− 0.5	− 0.3	(− 0.7)
Swiss francs	9.1	(5.9)	− 1.6	− 0.9	(− 0.7)
Pounds sterling	9.0	(5.6)	− 2.8	− 0.7	(+ 0.1)
French francs	3.8	(2.8)	− 0.8	− 0.2	(− 0.0)
Netherlands guilders	2.7	(1.7)	− 0.1	− 0.5	(− 0.4)
Unidentified assets	36.8	(54.1)	+ 8.9	+ 7.2	(+ 1.2)
Total reserves	450.6	427.7	−18.5	−27.0	+22.6
Memorandum items					
1. Total reserves excluding ECU balances arising from contributions of gold **2**	406.6	397.5	− 8.3	−20.0	+19.2
2. After additional adjustment for changes in value due to exchange rate movements **3**	406.6	**pe** 426.7	+ 5.0	−12.6	**pe** +27.7
Gold **1**	43.8	43.5	− 0.0	− 0.2	− 0.1
Special drawing rights	15.1	18.6	+ 5.6	+ 1.5	− 3.6
Reserve position in the IMF	21.5	46.4	+ 5.5	+ 4.7	+14.7
ECU balances **4**	2.2	1.6	− 0.5	+ 0.1	− 0.2
Foreign exchange	324.0	**pe** 316.6	− 5.6	−18.7	**pe** +16.9
of which					
Deutsche Mark	40.8	(36.4)	− 1.0	− 3.6	(+ 0.2)
B. Regional distribution 5					
OECD countries	273.0	251.8	−20.2	−12.7	+11.7
of which					
EEC countries	161.4	131.4	−24.9	−14.3	+ 9.2
United States	26.8	33.7	+ 3.3	+ 3.9	− 0.2
Japan	25.7	25.6	+ 3.6	− 4.9	+ 1.3
Canada	3.9	4.3	+ 0.4	− 0.5	+ 0.5
Germany	52.6	46.7	− 4.9	+ 1.0	− 2.1
France	30.8	24.1	− 5.1	− 5.7	+ 4.1
United Kingdom	21.4	12.1	− 5.4	− 2.8	− 1.1
Italy	26.0	22.9	− 3.0	− 6.0	+ 6.0
OPEC countries	89.7	80.8	− 0.8	−10.8	+ 2.8
Low-population	44.2	50.0	+ 6.4	− 3.5	+ 2.9
High-population	45.5	30.8	− 7.2	− 7.4	− 0.2
Other developing countries	76.1	61.8	− 4.7	− 9.4	− 0.1
Threshold countries **6**	32.4	27.3	− 0.5	− 7.1	+ 2.5
Other countries	43.7	34.5	− 4.2	− 2.3	− 2.6
Other IMF countries	11.8	31.5	+ 7.2	+ 6.0	+ 6.4
IMF countries, total	450.6	427.7	−18.5	−27.0	+22.6
Memorandum items					
Total reserves excluding ECU balances arising from contributions of gold **2**	406.6	397.5	− 8.3	−20.0	+19.2
of which					
OECD countries	229.0	221.6	−10.0	− 5.7	+ 8.4
EEC countries	117.4	101.2	−14.7	− 7.3	+ 5.9
Germany	40.4	38.3	− 2.0	+ 3.0	− 3.0
France	20.3	16.9	− 2.6	− 4.1	+ 3.3
United Kingdom	19.0	10.5	− 4.9	− 2.5	− 1.2
Italy	17.4	17.1	− 1.0	− 4.7	+ 5.4

* Including Switzerland. — The figures in brackets show the level at end-September 1983 or the corresponding change. — **1** Valued at $ 42.22 per ounce of fine gold. — **2** The gold underlying the ECU balances was included in the other gold holdings again. — **3** Changes in reserve holdings not denominated in dollars (other than gold) have been converted into dollars at average rates based on end-of-year rates. The adjusted level as at end-1983 has been calculated from the original level and the cumulative changes. — **4** Only balances arising from very short-term financing. The dollar holdings underlying the ECU balances were included in other foreign exchange again. — **5** For the definition of the groups of countries see the table on page 61. — **6** Excluding Taiwan. — **p** Provisional. — **pe** Partly estimated.
Discrepancies in the totals are due to rounding.
Sources: IMF and BIS.

nanced part of its lending activities by transferring some of its own special drawing rights.

Growth of reserves concentrated in a few countries

A large proportion of the increase in monetary reserves was accounted for by France and Italy. Capital inflows after the realignment within the EMS in March 1983, together with continued borrowing abroad, enabled both countries to replenish their reserves and even to increase them. Apart from them, only Australia, China and Mexico were able to increase their foreign exchange reserves to any significant extent. Moreover, the financing of the IMF's lending operations and the corresponding increase in reserve positions in the IMF was accounted for mainly by Saudi Arabia and the United States. In this context, Germany's reserve position in the Fund rose by only about $ 240 million because drawings in Deutsche Mark contrasted at the same time with various repayments in Deutsche Mark together with the subscription payment of another member country in Deutsche Mark (as is explained in detail in Part B of this Report). In overall terms it is not to be feared that the development of reserves last year might have paved the way for a more expansionary economic policy world-wide with possible inflationary consequences.

Restraint advisable regarding demands for new SDR allocations

There are no unambiguous criteria for answering the question of whether existing holdings of reserves are appropriate to ensure the smooth functioning of the international monetary system and the world economy. The purpose of monetary reserves is to ensure a country's international solvency. However, the decisive point in this context is not only the level of a country's reserves but also its capacity to incur debt internationally. For this reason, the aggregate volume of existing reserve holdings is just as inadequate an indication of the appropriateness of the global supply of reserves as the aggregation of the reserve needs that are often vociferously claimed by individual countries. The latter are not infrequently based more on the desire to create greater scope for expenditure ("reserves to spend") than on the willingness to hold a larger volume of reserves ("reserves to hold"). Restraint is therefore advisable with respect to the louder calls for the creation of special drawing rights recently made precisely by countries with a considerable need to adjust. There is a danger here that not a few countries are expecting their financial position to be alleviated as a result, which would be to the detriment of urgently necessary and indispensable adjustment efforts. But new allocations of SDRs would be of hardly any help to countries in balance of payments difficulties if, as a result, the regaining of their creditworthiness were to be called into question. Moreover, it is necessery to warn against the illusion that a major additional transfer of resources could be achieved via SDR allocations. Experience shows that distributional problems at the national level cannot be solved through the creation of money. This is just as unlikely at the international level. It would therefore also be wrong to attempt to justify a new allocation of special drawing rights by pointing to the uneven distribution of monetary reserves in the world. With such objectives in mind, SDR allocations would, moreover, hardly be compatible with the IMF's Articles of Agreement.

5. The debt problems of the developing countries

Time gained through successful crisis management

The international debt crisis broke out openly in mid-1982 and since then has repeatedly constituted an acid test of the ability to cooperate on the part of all those involved — governments, central banks, creditor banks and international organisations. The main objective has been to prevent a perfectly conceivable collapse (with all its consequences) of the international financial system, greatly expanded and complicated as it is and hence susceptible to disturbances. At the same time, however, even at this initial stage the limits to providing bridging loans from whatever sources had to be kept in sight and called to mind as need be. The demands of crisis management had to be carefully weighed against other considerations of both a basic and a practical nature. It was necessary as well to guard against the danger of depriving the adjustment constraints that had become evident during the crisis of their effect through granting credit on too generous a scale. Moreover, financial assistance by official bodies definitely had to be combined with contributions from the creditor banks, so as to defuse the evident liquidity crisis of the heavily-indebted countries and prevent it from developing ultimately into a solvency crisis. The complete default on payments by these countries would not only have created considerable and irreversible losses for the creditor banks directly affected but would probably also have cut off the debtor countries from an important source of capital flows for their development for years to come. It is a noteworthy success that as a result of this joint action it has proved possible to prevent a collapse of the international financial system, even though the debt crisis is by no means resolved thereby but time has only been gained. This time must now be used to consolidate the situation. For this, no generally valid recipes are available. In the final analysis, it is a question of bringing about a better relationship between the debt service obligations, i.e. the interest payments and loan repayments, of the individual countries and their economic potential.

Considerable adjustment efforts by the debtor countries . . .

First and foremost, considerable efforts on the part of the debtor countries themselves are required in order to overcome the debt crisis on a durable basis. Although developments beyond their influence played a considerable part in determining the timing and extent of the crisis, their own high rates of inflation, the widespread recourse to indexation and subsidies, the unsatisfactory state of public finance and the deep-rooted structural problems in their economies indicate that in most cases the debt crisis was by no means only or mainly due to external factors but was all too frequently the reflection of chronic macro-economic imbalances deriving quite evidently from domestic influences. Meanwhile the majority of the developing countries have indeed responded to a considerable extent to the expectations placed in them to adjust to the much narrower financial scope available to them. Generally more restrictive economic policies have led above all to a distinct decline in their imports and made possible the above-mentioned notable reduction in the aggregate current account deficit of this group of countries. Mexico has adjusted most. After this country's imports had already been cut by almost $ 10 billion in 1982, they declined in 1983 by an additional $ 6 billion, or 40 %. In the event, Mexico's creditworthiness has recovered amazingly quickly, with the result that its balance of payments difficulties for the time being appear to be more or less under control. Argentina, Brazil and Chile have also experienced a sharp reduction in their imports. However, the heavily-indebted countries will only be able to regain international confidence on a lasting basis if there is not only an improvement in their balance of payments situation but also a reduction to an acceptable level in the imbalances in their domestic economies. This would also foster the return of flight capital and encourage foreign direct investment and thus tend to reduce their dependence on international bank credits over time.

. . . facilitated by improvements in the global economic situation

As far as external causes are concerned, the debt problems of many countries are also a belated effect of the two oil price hikes in the 1970s and the successful recycling of the foreign exchange surpluses of the OPEC countries. It was precisely the payments balances of many developing countries dependent on imports that were thrown out of equilibrium — precarious as this equilibrium always was — by the increases in oil prices. For reasons associated with the development of these countries, their current account deficits reached proportions that could not easily be financed by capital inflows from various sources and development aid provided by the industrial countries. However, after the oil price hikes the current accounts of most developing countries remained in deficit longer and deeper than those of many industrial countries because, firstly, it was more difficult for the developing countries to increase their exports and,

External debt of the developing countries *

US$ billion

Item	1978	1979	1980	1981	1982	1983
A. Long-term	283	336	391	456	508	566
Public	116	133	153	170	189	212
Private	166	203	238	286	319	355
B. Short-term	52	59	85	104	125	102
C. Total (A plus B)	334	395	475	560	633	669
By foreign trade structure						
Oil exporters	68	79	95	125	148	155
Oil importers	266	316	380	434	486	514
By area						
Latin America	132	158	193	246	283	294
Middle East	27	32	36	41	46	51
Rest of Asia	79	93	115	131	153	165
Africa	37	45	51	56	63	66
Europe	47	55	67	71	72	75
Other countries	12	12	13	15	16	18
Memorandum items						
Debt service payments	48	61	73	97	108	97
Interest	18	26	39	55	63	59
Repayment of long-term loans	29	35	34	43	45	37
Debt service as a percentage of receipts from exports of goods and services	18.1	18.1	17.2	21.3	24.5	21.6

* Excluding the major oil exporters, among which are Algeria, Indonesia, Iran, Iraq, Kuwait, Libya, Nigeria, Oman, Qatar, Saudi Arabia, United Arab Emirates and Venezuela; but including European developing countries and Eastern European members of the IMF. — Excluding debt to the IMF.
Discrepancies in the totals are due to rounding.
Source: IMF.

secondly, in the process of recycling petrodollars, the international banks offered credits quickly and on a generous scale, which made it appear that even large current account deficits could be financed over the longer term. Moreover, the financing techniques developed for this purpose fostered the illusion among both the lenders and the borrowers that commitments, once entered into, could be refinanced effortlessly. However, these hopes collapsed when a determined anti-inflationary stance was adopted in U.S. monetary policy from October 1979 onwards and unaccustomedly high rates of interest had to be paid thereafter on the growing mountain of debt. For the countries whose debt was denominated primarily in U.S. dollars this implied a considerable burden in terms of real interest rates, which not only considerably increased the cost of budget and balance of payments financing with the aid of private credits from abroad, but also made the value of some investments that had been made at low or even negative real interest rates appear dubious with the benefit of hindsight. Above all else, balance of payments problems were considerably exacerbated through the sharp rise in debt service payments. The developing countries suffered all the more from the setback in world economic activity, which led to a noticeable drop in their export earnings. In the meantime, however, the global economic climate is increasingly favouring the adjustment efforts being made by these countries. Even though U.S. interest rates still appear to be high in absolute terms, they are nevertheless distinctly below the level of preceding years. Apart from this, the recovery now under way in the industrial countries should above all considerably improve the sales opportunities of the heavily-indebted countries. This, of course, presupposes that the industrial countries undertake not to place any protectionist obstacles in the path of the adjustment efforts of the debtor countries. This implies not only resolutely keeping open the markets of the industrial countries for imports from the developing countries but also not subsidising exports, as this could also be at the expense of the developing countries. At any rate, it would be a fateful turn of events if the heavily-indebted countries were to succeed in cutting back domestic demand, thus creating the major precondition for improving their balance of payments position, but were then not able to utilise this leeway in order to notably increase their exports. As a result they would be forced to cut back their imports even further, with this in turn seriously disrupting their development and further exacerbating the losses in real income and living standards that are in any case inevitable. At the very least, this would be grist to the mills of those who consider the present adjustment programmes to be socially unfair and politically impracticable. The success of the developing countries in export markets will, of course, depend to a considerable extent on the export orientation of the individual economies. Up to the present it has been primarily the countries of the Far East that have succeeded in exploiting the opportunities inherent in global economic activity. With the exception of the Philippines, they have generally not been confronted with balance of payments difficulties, although some of them are likewise heavily in debt.

Role of the IMF as intermediary between the debtor countries and the banks

A key role accrued to the International Monetary Fund already in the acute stage of crisis management. This role has since grown further. Being at the "interface" between financing and adjustment, the IMF is the "natural" body to provide medium-term balance of payments assistance combined with economic policy conditions, depending on the circumstances of the individual case, and, in doing so, to take into account the principle of equal treatment. Even though the Fund has accumulated a great amount of experience, it was confronted with a completely new situation in some respects. This applies especially to its role as intermediary between debtor countries and creditor banks. It was clear from the outset that, in providing financial resources, the Fund could not be a substitute for the banks. The sums involved alone made this impossible. Other considerations of a more fundamental nature also excluded this, the key factor being not so much the role of the banks in the past as their task of being intermediaries for the flow of savings to the developing countries also in the future. Thus, at this stage the IMF felt it necessary, with the more or less explicit support of a number of national monetary authorities, to negotiate with the creditor banks in order to bring about promising package solutions. In doing so, the Fund could rely on the enlightened self-interest of the banks, which would have suffered considerable losses if the solution of the problem had been left entirely to the workings of the market — as was explicitly recommended in some quarters. It is obvious that such an approach could be accepted only with reservations and only as part of the action taken to manage the crisis. Of course, after overcoming the acute stage of the crisis all the more restraint is called for vis-à-vis efforts to subject the future financial needs of certain countries and groups of countries, as well as the way these needs could be met, to the planning and control of the IMF or other international bodies. This would involve considerable potential for conflict since, despite all the common ground with regard to final objectives, in some cases individual interests are quite at variance with each other. It is much more important for all those concerned to draw the necessary consequences from the experience of the recent past. The developing countries as well as other countries should weigh up the limits to their external indebtedness more carefully than in the past. The banks need to take greater account of the principles of banking prudence and precaution when granting credits. Not least, national supervisory bodies must insist with the necessary weight that the rules of banking prudence are adhered to. Incidentally, these should be agreed internationally as far as possible. Apart from this, it is important to ensure sufficient transparency of the international credit and bond markets in order that the rules of the market should be able to continue to function in the sense that they enable countries whose creditworthiness is beyond doubt to procure funds and at the same time exert pressure to adjust where a country's creditworthiness is not absolutely assured. At all events, there can be no question either of the IMF taking over the role of the banks and other financial intermediaries for certain countries and groups of countries over the long term and on a large scale or of the pressure to adjust arising from the shortage of private financial resources being reduced through the Fund's activities or the activities of other bodies.

Balance of payments assistance by the BIS and national monetary authorities

Apart from the central role assumed by the IMF, the monetary authorities of the industrial countries made a noteworthy contribution in the context of crisis management. The loans granted by the Fund are financed chiefly from the quotas of countries in a relatively strong balance of payments and reserve position and hence with "usable currencies" as well as by special loans from individual members. The Bundesbank has always been an important creditor of the Fund in both these categories. When from the spring of 1982 onwards Hungary, Mexico, Brazil, Argentina and Yugoslavia ran into payments difficulties one after the other, the Bundesbank also participated in bridging operations conducted by the Bank for International Settlements either through placing deposits with the BIS or by giving guarantees for the repayment of credits financed by the BIS itself. In the course of granting such bridging loans, which served the short-term prefinancing of drawings on the IMF, the BIS at one time had total loans outstanding of $ 3 billion, of which the Bundesbank accounted for about $ 300 million in the form of financial contributions and guarantee obligations. In the context of these operations, Mexico received not only considerable assistance from the BIS totalling $ 925 million but was also granted an equally large bilateral credit by the U.S. monetary authorities. All the loans granted by the BIS have meanwhile been repaid, albeit in some cases — especially in the case of Brazil — only after a number of difficulties had been overcome. However, the generally successful provision of "fire-fighting assistance" by the BIS does not imply that it can be repeated ad lib. The bridging loans were designed for exceptional cases and in some cases the central banks involved supported them only after they had set reservations aside. The decisive factor was that it became very obvious in a number of cases that the solvency of some heavily-indebted countries could be maintained, and hence a serious threat to the international financial and monetary system averted at the same time, only by granting financial assistance quickly. This criterion may have benefited a number of large and particularly heavily-indebted countries — such as Mexico and Brazil — but as far as can be seen it was not felt to be discriminatory by other countries, although some of them suffered balance of payments difficulties themselves for the first time through regionalisation effects. But they, too, would probably have been pulled into the whirl of the debt crisis to a very much greater extent if the large countries had been denied fast assistance.

Considerable contributions from the banks

Within the context of the package solutions arranged by the IMF it was the banks themselves, relying on the adjustment programmes agreed with the Fund, that played their part in order to safeguard the solvency of the highly-indebted countries. On the one hand, together with official financial assistance they made additional long-term bank credits available. After total net lending by the private sector to the non-oil developing countries had fallen from about $ 70 billion in 1981 to $ 36 billion in 1982, at least an estimated $ 20 billion in loans could be raised last year. On the other hand, of the bank credits granted to developing countries falling due in 1983 and 1984, amounts totalling about $ 60 billion were rescheduled over the longer term. Thus, together with parallel measures by official creditors, it was possible to prolong almost $ 70 billion of loans falling due. As a result, the debt service payments of this group of countries declined again for the first time in a long while. The burden on the balance of payments in the form of interest payments and repayments of long-term loans went down from $ 108 billion in 1982 to an estimated $ 97 billion last year. In terms of their revenue from exports of goods and services, the average debt service burden of the developing countries declined over the same period from 25 % to 22 %, and including short-term debts, many of which were converted into long-term ones in 1983, from 53 % to 45 %. Before the beginning of the second round of oil price increases, when their total foreign debt was only

Contributions of the Bundesbank to short-term bridging facilities of the BIS in favour of countries in a weak balance of payments position

US$ million

Borrower/maturity	BIS facility	Bundesbank contribution: Guarantee	Bundesbank contribution: Deposit at the BIS
National Bank of Hungary			
April 7, 1982 to Jan. 7, 1983	100	25	25
May 17, 1982 to Nov. 17, 1982	110	10	10
Oct. 26, 1982 to April 26, 1983	300	40	40
April 29, 1983 to June 30, 1983	100	10	10
Bank of Mexico			
Aug. 30, 1982 to Aug. 23, 1983	[1] 925	120	–
Central Bank of Brazil			
Dec. 28, 1982 to Nov. 30, 1983	1,450	110	–
Central Bank of the Argentine Republic			
Jan. 28, 1983 to May 31, 1983	[2] 500	20	–
National Bank of Yugoslavia			
April 22, 1983 to Nov. 15, 1983	300	25	–
Maximum level of simultaneous recourse to the BIS or commitment by the Bundesbank.	2,975	295	75

1 The U.S. monetary authorities made an identical amount available in addition. — 2 Not drawn.

about half its level at the end of 1983, these ratios were only 18 % and 38 %, respectively. In the interests of a liberal international payments and monetary system it is desirable for the banks to continue to pay attention to cooperative solutions to the problem of maintaining the solvency of individual debtor countries. In this context, it would be particularly helpful if their rescheduling operations were not only restricted to short-term claims falling due but were also to take greater account of problems foreseeable over the longer term.

6. The international financial markets

Reduction in new international lending

According to BIS estimates, after allowing for double counting and repayments as well as exchange-rate-induced changes in inter-bank positions not denominated in U.S. dollars, the volume of financial resources provided by the international financial markets totalled about U.S.$ 130 billion in 1983. Total new lending in 1982 had come to about $ 150 billion and in 1981 it was touching $ 200 billion. This reduction in newly granted credits can be partially explained by the balance of payments position of the OPEC countries and the correspondingly reduced current account deficits of the oil-importing countries. The conclusions drawn from the international debt crisis naturally also played an important role. To this extent, the calmer pace of developments on the international financial markets above all marks a return to more normal conditions. This is also revealed by the fact that the decline was mainly restricted to the inter-bank loan markets, which had grown particularly strongly beforehand whereas the net volume of issues on the international bond markets, where a greater premium has always been placed on the borrower's creditworthiness, at about $ 60 billion, almost reached the same high level as in the preceding year. The table on the international credit and bond markets does not reflect this decline in international lending to the same extent because the figures do not include short-term loans, which fell particularly sharply.

Decline in new bank lending concentrated in OECD countries

The decline in medium and long-term international bank lending totalling $ 31 billion on a gross basis chiefly affected loans to OECD countries. As mentioned above, many of these countries succeeded in reducing their current account deficits, whereas the simultaneous deterioration in the U.S. current account position was offset by a decline in U.S. capital exports. The lower level of borrowing from banks was also partly due to the fact that issuers in these coun-

International credit and bond markets

US$ billion

Item	1979	1980	1981	1982	1983 p
A. Medium and long-term international bank loans [1]	[10] 79.3	[10] 81.0	94.6	98.2	67.2
Borrowing sectors					
Public [2]	61.6	50.9	54.1	64.8	47.6
Private	17.7	30.1	40.5	33.4	19.5
Borrowing countries [3]					
OECD countries	28.9	41.8	47.4	54.4	30.5
Seven major countries	12.7	23.9	27.8	31.2	15.2
Other countries	16.2	17.9	19.6	23.2	15.3
OPEC countries	8.8	7.0	6.0	8.0	7.2
Other developing countries	32.6	28.2	37.8	32.2	24.8
Centrally planned economies [4]	8.6	3.0	2.0	0.9	1.1
Other countries [5]	0.5	1.0	1.5	2.7	3.6
Types of loans					
Euro-credits	79.3	81.0	91.3	90.8	60.2
Traditional credits	.	.	3.4	7.4	7.0
Memorandum items					
Other credits [6]	.	.	[11] 53.1	5.2	13.3
Rescheduling operations	.	.	6.6	3.8	57.6
B. International bond issues	40.6	39.8	52.8	75.5	77.1
Borrowing sectors					
Public [2]	27.4	25.5	28.2	42.0	43.9
Private	13.2	14.3	24.6	33.5	33.2
Borrowing countries [3]					
OECD countries	28.1	28.8	39.6	60.1	60.3
OPEC countries	0.4	0.2	0.4	0.5	0.4
Other developing countries	2.6	1.5	3.8	3.6	2.2
Other countries	0.4	0.4	0.3	0.5	0.9
International organisations					
European	3.9	3.6	2.5	3.5	6.8
Other	5.1	5.3	5.0	7.3	6.6
Types of issues					
Euro-bonds [7]	18.7	20.4	31.3	50.3	50.1
Traditional foreign bonds [8]	20.3	18.0	20.5	25.2	27.0
Special issues [9]	1.6	1.4	1.0	—	—
Currencies of issue					
U.S. dollar	15.4	17.1	32.9	48.3	43.9
Deutsche Mark	9.1	8.7	2.7	5.4	6.7
Swiss franc	9.8	7.6	8.4	11.4	13.5
Yen	3.1	2.1	3.3	3.9	4.1
Other	3.1	4.2	5.5	6.6	9.0
C. Total (A plus B)	119.9	120.8	147.5	173.7	144.3

1 Publicised loans running for more than one year granted mostly by international bank syndicates (Euro-credits) or in national currency by national bank syndicates (traditional credits) and almost entirely financed on a roll-over basis which have not necessarily been taken up yet. — 2 Including public enterprises and financial institutions and including international organisations. — 3 For the definition of the groups of countries see the table on page 61. Borrowing operations by foreign subsidiaries are included under the country of domicile of the parent company. — 4 Including CMEA institutions. — 5 Including international organisations. — 6 Mainly loan commitments of stand-by type. — 7 Primarily internationally syndicated issues; including private placements and variable-rate bonds. From 1981 also including medium-term CDs with variable rates. — 8 Nationally syndicated issues in domestic currency. — 9 Direct placements with monetary authorities and governments. — 10 Including loan commitments of stand-by type, but excluding traditional credits. — 11 Including large loans to U.S. enterprises amounting to about US$ 41 billion granted in connection with mergers, but hardly taken up at all. — p Provisional.
Discrepancies in the totals are due to rounding.
Sources: OECD, World Bank.

tries were able to raise a greater volume of funds on the international bond markets than in earlier years if account is also taken of funds taken up via international bodies. The relatively limited decline in new loan commitments to the developing countries is explained by the fact that the greater part of credits granted in 1983 reflects the package solutions that were necessary in the context of managing the debt crisis. Of the new credit commitments totalling $ 25 billion, only $ 10 billion was granted "spontaneously", with the major part being accounted for by countries in Asia. The largest loans among these countries that continue to be considered creditworthy went to South Korea ($ 3.2 billion), Malaysia ($ 1.1 billion), and India and Hong Kong ($ 0.7 billion each). The increased commitments of the banks in heavily-indebted countries naturally led to these having to accept higher interest rate spreads, with the result that the benefits of declining interest rates on the dollar market were felt to a correspondingly lower degree. On the other hand, medium and long-term new loans granted to the OPEC countries remained practically unchanged. However, the simultaneous increase in their current account deficits produced a considerable rise in their need for finance. According to the BIS statistics, this gap was also financed by these countries continuing to draw down their deposits with Western banks.

Renewed gradual increase in the Deutsche Mark share on the bond market

As in the preceding year, the volume of issues on the international bond markets, which changed only slightly, was accounted for to a very large extent by issuers in the OECD countries. At 43%, the share of issues placed by the corporate sector remained approximately at its previous high level. In contrast, the role of the U.S. dollar as a currency of issue declined for the first time for many years. Its market share fell from 64% in 1982 to 57% last year. The shares accounted for by the Swiss franc and the Deutsche Mark rose correspondingly from 15% to 18% and 7% to 9%, respectively, revealing renewed greater confidence on the part of international creditors in the stable value of such investments. Even so, the German currency is still far below the importance it attained in 1980, when over 20% of total issues was denominated in Deutsche Mark. It is also noteworthy that the importance of bonds with variable interest rates continued to increase, except in the Deutsche Mark sector, however, owing to misgivings on the part of the Bundesbank in terms of the monetary policy implications of this development and corresponding agreements with German banks of issue.

Efforts by banking supervisory authorities to ensure better observance of prudential regulations

The subdued development of international lending is in line with the efforts being made by banking supervisory authorities to bring the banks' capital into better harmony with their international lending. These efforts were fostered, incidentally, at the international level when central banks, by revising the "Basle Concordat" in May 1983 under the auspices of the BIS, reaffirmed the principle that banks should be supervised on the basis of consolidated balance sheets. In addition, in June 1983 the EEC Council of Ministers approved a corresponding Directive which had to pass into national law within two years (see the comments on banking supervision in Part A of this Report).

7. Financial assistance granted by the IMF and the multilateral development banks

Sharp rise in loan assistance by the IMF

In 1983 the volume of new lending by the IMF grew by approximately two-thirds to SDR 12.6 billion ($ 13.5 billion) in comparison with the preceding year. With loan repayments over the same period totalling SDR 2 billion, net lending by the Fund thus came to SDR 10.6 billion, or over 80% more than in 1982. Of this amount, SDR 9.2 billion was accounted for by non-OPEC developing countries in the Third World, with the largest amounts going to Brazil (SDR 2 billion), India (SDR 1.5 billion), and Mexico (SDR 1 billion). The remaining net drawings were for the benefit of a few OPEC countries as well as Yugoslavia, Romania and Hungary. Despite the surge in its lending activities, the Fund met only a relatively small part of the total financing requirements of its members. However, of the aggregate current account deficit of the developing countries, as much as 20% was financed via the IMF. In contrast, this share was no more than 7% in 1982, when their combined deficit was much larger. Despite this marked increase, the assistance granted by the Fund — as mentioned above — continued to be restricted primarily to its acting as a catalyst which enabled other sources of finance to be kept open to the degree necessary. Thus, the additional support given by the Fund was mainly reflected in drawings on credit tranches and the Extended Fund Facility. In both cases, IMF assistance can in

Purchases and repurchases under IMF credit facilities

SDR billion

Item	1980	1981	1982	1983
Credit tranches	1.8	3.4	2.5	4.9
Extended Fund Facility	0.6	2.1	2.1	4.6
Compensatory Financing Facility	1.0	1.2	2.6	2.8
Buffer Stock Facility	—	—	0.1	0.3
Total purchases	3.4	6.8	7.4	12.6
Total repurchases	3.3	2.1	1.8	2.0
Net purchases	0.2	4.7	5.8	10.6

Discrepancies in the totals are due to rounding.
Source: IMF.

principle only be granted in association with stabilisation or structural adjustment programmes, with certain economic policy conditions being adhered to. In contrast, there was only a slight rise in drawings under the Compensatory Financing Facility and the Buffer Stock Facility. Of the IMF's loans outstanding at the end of 1983, which totalled about SDR 30 billion, 74% was accounted for by loans generally involving stricter economic policy conditions. A year earlier this share had been only 71%.

Improvement in the Fund's liquidity through bridging loans

The surge in lending by the IMF clearly reflects the "Policy of Enlarged Access to Fund Resources" adopted in 1981. Under this policy, members with large and persistent balance of payments deficits may draw considerably larger amounts in the context of adjustment programmes. At the same time, however, this has led to a growing shortage of Fund resources, above all because the additional balance of payments assistance granted under the policy of "Enlarged Access", which is not covered by the resources available from members' quotas, has to be financed by Fund borrowings from the monetary authorities of countries in a strong balance of payments and reserve position. Although the principle continues to apply that the Fund may normally only make loan commitments whose refinancing seems to be assured, last year it was not possible to adhere to this principle at times, with the result that over the course of the year a commitment gap arose between the Fund's outstanding loan commitments and its available resources. In order to close this gap, at the end of 1983 the BIS and a number of central banks declared their willingness in principle to extend to the IMF various credit lines totalling SDR 6 billion. The Saudi Arabian Monetary Agency intends to contribute SDR 3 billion of this amount. Most of the other half will be made available by the BIS, with the central banks of 19 industrial countries bearing the associated risks to the extent that they do not make the resources available directly (as in the case of Japan and Belgium). The Bundesbank, with a contribution of SDR 415 million, has assumed the largest share, whereas the United States is not involved in this operation. As a result, the liquidity problems that have arisen in connection with past loan commitments can be bridged at least until the second half of 1986; from then on, relatively large loan repayments to the IMF ought to lead to some improvement in its liquidity position.

Longer-term strengthening of the Fund through an increase in quotas . . .

The Fund's gradually emerging shortage of liquidity was a major contributory factor in the marked increase in the Fund's long-term resources agreed at the beginning of 1983 being ratified by the end of the year. As a result, the latest increase in quotas came into effect at the end of November last year after the great majority of members had finally agreed to it. Most countries, including Germany, have meanwhile paid up their quota increases, with the consequence that the new quotas have become effective for the individual countries. Germany's quota rose from SDR 3.2 billion to SDR 5.4 billion, with its share in total quotas growing from 5.3% to 6%. With the overall increase in quotas from

SDR 61 billion to about SDR 90 billion the IMF has additional usable own resources of about SDR 20 billion, corresponding to about two-thirds of the increase in aggregate quotas. Quota payments were effected to this estimated extent in special drawing rights or the currencies of countries in a strong balance of payments and reserve position, i. e. in resources the Fund can use in its lending activities.

. . . and through an enlargement of the GAB

Besides the above measures, the Fund's borrowed resources were also considerably strengthened by the decision by the members of the Group of Ten at the end of 1983 to enlarge the General Arrangements to Borrow (GAB). Including the contribution of Switzerland, which became the eleventh participant of the GAB in April 1984, and a parallel borrowing agreement with Saudi Arabia, the IMF thus has available a revolving medium-term refinancing facility totalling SDR 18.5 billion, or almost three times as much as the GAB credit lines available to it since 1976. The share provided by the Bundesbank rose by about SDR 1 billion to SDR 2.4 billion. In addition to their being enlarged, the General Arrangements to Borrow were also made considerably more valuable because they can now be activated to refinance drawings by all members of the Fund — and not only in the case of balance of payments difficulties faced by the participants of the GAB themselves — to the extent that the IMF has an undeniable need for liquidity. The additional conditions for activating the GAB in favour of third countries include the fact that the loans to be financed are tied to adjustment programmes and that the nature and extent of the balance of payments problems are such as might endanger the international monetary system. However, the total volume of the GAB is unlikely to be available to the Fund in full since it must be expected that in case of need some participating countries would be unable to provide loans owing to balance of payments difficulties of their own or would even require IMF assistance themselves.

Continuation of "Enlarged Access" policy for a limited period

In 1983 it was also decided, in view of the continuing large balance of payments deficits of many countries, to continue the "Policy of Enlarged Access to Fund Resources", which was intended only to bridge the period until the latest increase in quotas came into effect, initially up to the end of 1984 in modified form. Thus, depending on the size of the balance of payments need and the scope of a country's adjustment efforts, the IMF can undertake loan commitments up to the end of 1984 under the policy of "Enlarged Access" envisaging assistance up to a maximum of 102 % or 125 % of a country's quota in a single year or, alternatively, 306 % or 375 % over a period of three years. Total recourse to the Fund's resources by any given country — including drawings outstanding — may not exceed an upper limit of 408 % or 500 % of its quota as a result. However, no account is taken of drawings under the Compensatory Financing Facility or the Buffer Stock Facility. Although the members' scope for drawings as a percentage of their new quotas appears smaller than previously, in fact this arrangement means that most IMF member countries have slightly higher absolute upper limits for drawings under the policy of "Enlarged Access" than they had before the quota increase. Apart from this, exceptions can be made under unusual circumstances. Moreover, the scope for drawings under the Fund's special facilities increased by an average of over 20 % in the end, although here, too, the upper limits as a percentage of the new quotas were reduced.

Financial basis of the Fund now adequate

After the financial basis of the IMF had been considerably strengthened through the increase in quotas, the enlargement of the GAB and its being made available to finance loans granted to all IMF members, as well as through the provision of bridging loans mentioned above, the Fund is sufficiently equipped for its tasks in the foreseeable future. The potential financial obligations of the Bundesbank vis-à-vis the Fund have meanwhile reached the considerable amount of some DM 32 billion, not taking into account the contingent liabilities from the above-mentioned BIS bridging loan. Of this amount, approximately DM 11 billion had been utilised as per end-1983. If the remaining potential for utilisation by the IMF were to be activated to any great degree, then the share of IMF-related assets in terms of the Bundesbank's total liquid reserves, which amounted to about 18% at the end of 1983, would rise considerably. Although it can be assumed that such assets can be mobilised in case of need, the possibility cannot be excluded from the outset that in certain situations this could have serious consequences for the liquidity of the Fund. Since, owing to Germany's position in the world economy and especially in the light of the function of the Deutsche Mark as an important investment and reserve currency, the Bundesbank must have a considerable volume of liquid reserves available, there is a limit to its assuming further commitments, with respect inter alia to the composition of its reserves alone.

Growing resources of the development banks owing to new refinancing devices

Last year also saw a further rise in the total loan commitments of the multilateral development banks. In this context, it was possible once again to mobilise additional resources for the developing countries through co-financing instruments in conjunction with private and public sector lenders. However, in comparison with earlier years the volume of lending grew at a more moderate pace. This reflects the fact that many countries have meanwhile begun a critical review of their development policies. Nevertheless, the international financial markets continued to be a rich source of capital for the development banks. Gross borrowing by the World Bank, the volume of which is primarily determined by its loan commitments in the preceding years, increased in the 1982–83 financial year by $ 1.8 billion to $ 10.3 billion in comparison with the previous year. The increase in the amount of capital raised last year was, however, entirely due to issues of short-term bonds on the U.S. market. The recourse to such refinancing instruments, which began at the beginning of 1984 with the issue of paper with variable interest rates on the Euro-market and was further developed through the possibility opened to central banks, governments and international institutions to invest U.S. dollars at short term, made it easier for the World Bank to raise funds but could, if it were to exceed a certain amount, also raise questions in terms of monetary policy and development policy considerations.

Germany still an important source for traditional borrowing

In 1983 Germany's capital market was again one of the main sources of traditional borrowing by multilateral development banks. In the case of the World Bank, Germany's financial contribution to this type of borrowing, which has stagnated at a level of $ 8.5 billion since the 1981–82 financial year, totalled 13%. Including currency swap transactions,[1] this share was even as high as 17% last year. Only Switzerland accounts for a larger share, calculated on the same basis. Germany has maintained its importance in this respect up to the present in the current year as well. Since it first took up loans on the German capital market in 1957, the World Bank has thus been able to raise credits in Germany and through direct placements of Deutsche Mark loans with the monetary authorities of individual developing countries totalling over DM 35 billion in all, of which about DM 20 billion was outstanding at the end of 1983. Borrowings by the Inter-American Development Bank (IDB) and the Asian Development Bank (ADB) in Germany totalled DM 600 million each last year, corresponding to a financial contribution by Germany of 17% in the case of the IDB and as much as 24% with respect to the ADB. While the African Development Bank had not approached the German capital market in 1983, it resumed its borrowing activities in Germany again with a public sector loan totalling DM 100 million in March this year.

1 Under such arrangements, those involved in the swap transaction essentially exchange bond liabilities denominated in different currencies. In this way, the World Bank gains access to currencies bearing a relatively low rate of interest without having direct recourse to the national markets concerned.

Part B: Notes on the Deutsche Bundesbank's annual accounts for 1983

1. Legal basis, classification and valuation

Legal basis, accounting system and annual accounts

The legal basis for the annual accounts of the Bank is provided by section 26 of the Deutsche Bundesbank Act (Gesetz über die Deutsche Bundesbank) of July 26, 1957 (Federal Law Gazette I, page 745); the provisions of that section regarding the accounting system and the annual accounts remained unchanged during the year under review.

Classification of the annual accounts

On the assets side of the balance sheet, item 3 "Claims on the European Monetary Cooperation Fund in connection with the European Monetary System" was subdivided as follows:

3.1 ECU balances resulting from the provisional contribution of gold and dollar reserves less
Difference between the ECU value and the book value of the reserves contributed
3.2 ECU balances resulting from transfers from other central banks
3.3 Other claims

On the liabilities side, the former item "Counterpart in respect of the valuation of the gold and dollar reserves provisionally contributed to the European Monetary Cooperation Fund" was deleted. The new classification results in a shortening of the balance sheet.

In the profit and loss account, the item "Receipts from purchases and sales of foreign currencies and from the valuation of the monetary reserves and other foreign currency positions" was added. The expenditure item "Write-downs of monetary reserves and other foreign currency positions" was deleted.

Valuation

The provisions of the Companies Act (Aktiengesetz) were applied mutatis mutandis in the valuation (section 26 of the Bundesbank Act).

2. Annual accounts

The annual accounts for 1983 are attached to this Report as an Appendix; as usual, the notes on them are in the same order as the items in the balance sheet and profit and loss account. At the same time a report is rendered on the Bank's activities during 1983.

Balance sheet

Comparison of balance sheet figures

At December 31, 1983 the balance sheet total amounted to DM 197,148.1 million — on the basis of the new classification — as against DM 186,328.0 million at end-1982.

Comparison of balance sheet figures

DM million

Assets	December 31 1982	December 31 1983
Gold	13,687.5	13,687.5
Reserve position in the International Monetary Fund and special drawing rights		
Drawing rights within the reserve tranche	4,178.3	7,705.0
Loans under special borrowing arrangements	3,159.2	2,503.7
Special drawing rights	4,881.5	4,394.1
Claims on the European Monetary Cooperation Fund in connection with the European Monetary System		
ECU balances resulting from the provisional contribution of gold and dollar reserves 1	12,421.0	12,496.1
ECU balances resulting from transfers from other central banks	5,054.0	2,948.3
Other claims	2,120.8	—
Balances with foreign banks and money market investments abroad	38,955.7	37,794.1
Foreign notes and coins	25.0	24.7
External loans and other external assets		
Loans to the World Bank	2,455.7	2,455.7
Foreign bills of exchange	7,050.4	9,448.4
Domestic bills of exchange	46,688.8	46,586.5
Securities bought in open market transactions under repurchase agreements	9,103.4	16,168.4
Lombard loans	12,031.1	13,294.8
Cash advances (book credits)	1,395.4	901.5
Equalisation claims on the Federal Government and non-interest-bearing debt certificate in respect of Berlin	8,683.6	8,683.6
Securities	5,409.4	7,797.3
German coins	1,084.2	1,013.6
Balances on postal giro accounts	150.3	238.5
Land and buildings	1,267.0	1,386.7
Furniture and equipment	107.7	119.2
Items in course of settlement	2,970.4	3,487.1
Other assets	3,411.6	3,977.0
Prepaid expenses and deferred income	36.0	36.3
Balance sheet total	186,328.0	197,148.1
Contingent claims	1.2	0.1

Liabilities	December 31 1982	December 31 1983
Banknotes in circulation	88,574.7	96,073.0
Deposits of banks	51,875.1	52,702.0
Deposits of public authorities		
Federal Government	723.6	1,516.8
Equalisation of Burdens Fund and ERP Special Fund	162.2	19.1
Länder Governments	330.0	592.2
Other public depositors	42.3	31.9
Deposits of other domestic depositors		
Federal Railways	19.8	10.4
Federal Post Office	2,865.8	2,561.8
Other depositors	629.7	599.6
Liabilities arising from mobilisation and liquidity paper sold	4,651.6	6,296.0
Liabilities arising from external transactions	12,035.0	9,780.5
Counterpart of special drawing rights allocated	3,174.0	3,452.7
Provisions	4,306.0	6,192.2
Other liabilities	186.4	159.9
Deferred expenses and accrued income	675.7	380.8
Capital	290.0	290.0
Reserves	4,479.5	4,718.7
Unappropriated profit	11,306.6	11,770.5
Balance sheet total	186,328.0	197,148.1
Contingent liabilities	1.2	0.1

1 After deduction of the difference between the ECU value and the book value of the reserves contributed.

Assets

Gold

The gold holding at December 31, 1983, amounting to 95 million ounces of fine gold (excluding the gold reserves provisionally contributed to the European Monetary Cooperation Fund), at DM 13,687.5 million, was the same as at end-1982.

Reserve position in the International Monetary Fund and special drawing rights

Drawing rights within the reserve tranche

At December 31, 1983 the drawing rights within the reserve tranche in the IMF amounted to DM 7,705.0 million (= SDR 2,701.9 million) against DM 4,178.3 million (=SDR 1,593.8 million) at end-1982. Increases of SDR 1,718.5 million were accompanied by decreases of SDR 610.4 million. Of the increases, SDR 542.4 million was due to the raising of the German IMF quota, and SDR 1,176.1 million to Deutsche Mark drawings of other member countries and transactions of similar effect. The decreases were due to Deutsche Mark repayments and transactions of similar effect totalling SDR 278.5 million and to an IMF member country's subscription payment in Deutsche Mark equivalent to SDR 331.9 million. The level of drawing rights within the reserve tranche represents the difference between the German quota of SDR 5,403.7 million (previously: SDR 3,234.0 million) and the Deutsche Mark balances equivalent to SDR 2,701.8 million at the disposal of the IMF at the end of the year.

Loans under special borrowing arrangements

Loans under special borrowing arrangements amounted to DM 2,503.7 million at December 31, 1983 against DM 3,159.2 million at end-1982. The loans outstanding at the end of 1983 comprise exclusively claims of SDR 878.0 million on the IMF arising from the financing of other members' Deutsche Mark drawings under the Supplementary Financing Facility; in the year under review the IMF was granted loans totalling SDR 255.8 million under this Facility at the Deutsche Bundesbank. This Facility was thereby fully utilised. The claim of SDR 582.9 million on the IMF under the General Arrangements to Borrow (GAB) shown at end-1982 and arising from the financing of a Deutsche Mark drawing by the United States in 1978 was duly repaid by the IMF on maturity in November 1983.

Special drawing rights

The amount of special drawing rights (SDRs) held at December 31, 1983 is shown at DM 4,394.1 million against DM 4,881.5 million at end-1982. It consists of SDR 1,210.8 million of SDRs allocated, the counterpart of which is shown on the liabilities side, and SDR 330.1 million of SDRs purchased. Increases of SDR 1,264.8 million were accompanied by decreases of SDR 1,586.0 million. The increases resulted from the repayment of the GAB credit by the IMF (SDR 582.9 million), from designations (SDR 389.4 million), from a payment in the context of the settlement of balances in the EMS (SDR 84.8 million) and from interest payments and remunerations by the IMF (SDR 207.7 million). The decreases stemmed from sales in freely agreed SDR transactions (SDR 1,043.6 million), and the above-mentioned raising of the German quota in the IMF (SDR 542.4 million).

Claims on the European Monetary Cooperation Fund in connection with the European Monetary System

This item comprises the Bank's ECU balances and the claims arising from the use of the very short-term financing arrangement by other central banks.

ECU balances resulting from the provisional contribution of gold and dollar reserves

The ECU balances amounting to DM 39,427.5 million arose from the provisional contribution of 20% of the Bank's gold and dollar reserves to the European Monetary Cooperation Fund (EMCF) in the form of three-month swaps.

less Difference between the ECU value and the book value of the reserves contributed

The gold and dollar reserves provisionally contributed to the European Monetary Cooperation Fund in connection with the European Monetary System (EMS) against the crediting of ECUs were transferred at market prices and therefore at values higher than those shown in the balance sheet. The resulting difference of DM 26,931.4 million is deducted in this sub-item.

ECU balances resulting from transfers from other central banks

This sub-item comprises the reserve ECUs amounting to DM 2,948.3 million (end-1982: DM 5,054.0 million) transferred to the Bank by other central banks participating in the EMS.

Other claims

At end-1983 no other ECU claims arising from loans to other central banks under the very short-term financing arrangement were outstanding.

Balances with foreign banks and money market investments abroad

The balances with foreign banks and money market investments abroad, the great bulk of which are denominated in U.S. dollars and bear interest, amounted to DM 37,794.1 million at end-1983 against DM 38,955.7 million at December 31, 1982.

Foreign exchange deals

Mainly owing to larger dollar sales on the foreign exchange market, the Bank's turnover in foreign exchange spot deals (foreign currency against Deutsche Mark) rose to DM 44,284.5 million in 1983 against DM 29,031.1 million in 1982. Because of the increase in commercial transactions the number of deals climbed to 7,593 compared with 5,926 in the preceding year. These deals consisted of

	1982		1983	
	Number	DM million	Number	DM million
Purchases	2,635	9,725.1	2,786	12,445.2
Sales	3,291	19,306.0	4,807	31,839.3
	5,926	29,031.1	7,593	44,284.5.

The volume of cross deals (foreign currency against foreign currency) declined in the year under review, at 390 deals equivalent to DM 3,759.2 million against 474 deals equivalent to DM 3,836.5 million in 1982. By contrast, the volume of SDR/U.S. dollar and SDR/Deutsche Mark deals rose to 138 deals equivalent to DM 4,283.1 million compared with 130 deals equivalent to DM 2,546.2 million in 1982. In addition, 148 U.S. dollar inter-centre switch transactions totalling US$ 29.5 million were conducted against 123 transactions amounting to US$ 24.9 million in the preceding year.

49 forward ("outright") sales of U.S. dollars totalling US$ 600 million were effected, compared with 13 U.S. dollar sales totalling US$ 750 million and four U.S. dollar purchases totalling US$ 50 million in the previous year.

To regulate the money market, 63 dollar swaps totalling DM 12,967.1 million were conducted with domestic banks to increase liquidity during the year under review, against 65 such transactions amounting to DM 13,492.1 million in the preceding year. In addition, 43 foreign exchange transactions under repurchase agreements totalling DM 10,471.8 million were conducted in 1983 for the purpose of reducing liquidity.

External payments

The Bank executed the following payment orders in the context of external payments:

External payments

Number of orders

Year	in foreign currency	in Deutsche Mark	Total	of which: Processed by automated standing order procedure	of which: Processed automatically via S.W.I.F.T. 1
	Outgoing external payment orders				
1982	450,038	1,770,714	2,220,752	1,963,234	155,190
1983	437,084	1,988,267	2,425,351	2,161,779	168,565
	Incoming external payment orders			of which Payments received via S.W.I.F.T.	
1982	15,134	206,043	221,177		176,014
1983	14,294	201,719	216,013		182,935

1 S.W.I.F.T. (= Society for Worldwide Interbank Financial Telecommunication) is a Belgian society which transmits external payments messages by means of data telecommunication. The Bank is a member of the society and has been using the services provided by S.W.I.F.T. since the middle of 1978.

Sales of foreign cheques

During 1983 14,679 (1982: 11,949) foreign cheques payable to order totalling DM 726.1 million (1982: DM 898.8 million) were sold. In addition, the Bank sold 24,658 traveller's cheques amounting to DM 2.9 million against 31,298 traveller's cheques totalling DM 3.4 million in the preceding year.

Simplified collection procedure for foreign cheques

The number and amount of cheques received under the simplified collection procedure for foreign cheques continued to rise during the year under review. Details are given in Appendix 3 of the German original of this Report.

Foreign commission business

The Bank took in the following for realisation on a commission basis:

	1982 Number	1983 Number
Bills, cheques, etc.	49,885	41,795
Foreign notes and coins	6,518	5,439
	56,403	47,234.

Foreign notes and coins

The amount of foreign notes and coins held at December 31, 1983, at DM 24.7 million, was DM 0.3 million lower than at December 31, 1982. During the year under review, the Bank effected 21,320 purchases (1982: 21,448) and 41,171 sales (1982: 39,418) of foreign notes and coins.

External loans and other external assets

As in the preceding year, only loans to the World Bank are shown in this item. Loans under the EEC medium-term monetary assistance arrangement and other loans to foreign monetary authorities were not granted in the year under review.

Loans in connection with EEC medium-term monetary assistance

Other loans to foreign monetary authorities

Loans to the World Bank

As in preceding years, the loans to the World Bank were mainly granted against borrowers' notes denominated in Deutsche Mark.

Foreign bills of exchange

At the end of 1983 the portfolio of foreign bills accumulated through purchases in Germany amounted to DM 9,448.4 million compared with DM 7,050.4 million at December 31, 1982. The share of Deutsche Mark bills in the total value of the foreign bills purchased in 1983 averaged about 87 % (1982: about 90 %).

Purchases of foreign bills of exchange in the Land Central Bank areas

Land Central Bank	1982 Number	1982 DM million	1983 Number	1983 DM million
Baden-Württemberg	40,541	2,985.7	40,772	4,234.6
Bavaria	22,490	3,980.6	23,096	4,493.6
Berlin	1,326	2,113.4	1,581	2,545.6
Bremen	2,651	364.0	2,702	519.7
Hamburg	11,717	3,604.8	13,067	4,910.5
Hesse	24,312	8,634.1	23,690	12,674.7
Lower Saxony	4,506	597.7	4,534	895.3
North Rhine-Westphalia	39,164	6,918.7	38,302	10,007.1
Rhineland-Palatinate	7,829	894.1	7,288	1,028.1
Saarland	3,492	840.4	2,886	808.7
Schleswig-Holstein	1,588	444.0	1,642	606.3
Total	159,616	31,377.5	159,560	42,724.2

Domestic bills of exchange

At the end of 1983 the Bank's portfolio of domestic bills amounted to DM 46,586.5 million against DM 46,688.8 million at the end of 1982. The Bank's average portfolio of domestic bills on all return days, at DM 46,308 million, was slightly lower than in the preceding year (DM 46,525 million). As in previous years, most of these bills were presented by banks within their rediscount quotas.

The domestic bill portfolio comprised	Dec. 31, 1982 DM million	Dec. 31, 1983 DM million
Domestic bills discounted	43,453.3	42,826.1
Prime bankers' acceptances acquired in the course of open market operations	3,235.5	3,760.4
	46,688.8	46,586.5.

Purchases of domestic bills of exchange in the Land Central Bank areas

Land Central Bank	1982 Thousands	1982 DM million	1983 Thousands	1983 DM million
Baden-Württemberg	610	26,682.5	627	27,911.2
Bavaria	393	26,101.3	385	26,952.1
Berlin	28	5,860.9	24	5,009.5
Bremen	49	4,464.9	45	3,906.2
Hamburg	119	15,937.2	114	14,715.6
Hesse	373	47,101.1	344	41,030.3
Lower Saxony	179	13,437.7	178	13,719.6
North Rhine-Westphalia	625	49,539.2	612	48,454.7
Rhineland-Palatinate	101	6,070.3	104	6,368.3
Saarland	30	2,560.6	27	2,580.0
Schleswig-Holstein	46	3,862.9	41	3,571.6
Total	2,553	201,618.6	2,501	194,219.1

The average value of the bills purchased in the year under review was DM 77,700 compared with DM 79,000 in the preceding year.

Of the bills purchased, the following were returned and charged, in the absence of payment, to the parties presenting them for rediscounting:

	1982		1983	
	Number	DM million	Number	DM million
	15,139	222.8	13,904	232.5
as % of the total purchased	0.59	0.11	0.56	0.12.

Discount rate

During the year under review the Bank's discount rate for domestic and foreign bills was 5% until March 17 and 4% as from March 18.

Prime bankers' acceptances

The amount of prime bankers' acceptances which the Bank is prepared to purchase in the course of its open market operations was raised by another DM 500 million to DM 4 billion with effect from February 1, 1983. Throughout the year the Bank's buying rate for prime bankers' acceptances was below the discount rate; from March 18, 1983 onwards the difference was 0.5 percentage point. As a result, heavy recourse was had to this higher ceiling. The Bank's purchases of prime bankers' acceptances through the Privatdiskont-Aktiengesellschaft came to DM 17,290.1 million (1982: DM 13,794.9 million). There were no resales to the market via the broker in 1983.

The amount of prime bankers' acceptances that remained in the Bank's portfolio until payment on maturity, at DM 16,334.2 million, was therefore larger than in the previous year (DM 13,102.6 million). At December 31, 1983 the Bank held prime bankers' acceptances stemming from open market operations totalling DM 3,760.4 million (end-1982: DM 3,235.5 million).

Open market transactions in bills under repurchase agreements

The Bank conducted no open market transactions in bills under repurchase agreements in the year under review.

Securities bought in open market transactions under repurchase agreements

To provide liquidity for a limited period, the Bank offered the banks, by tender, open market transactions in securities under repurchase agreements on several occasions during the year under review. In these transactions the Bank bought bonds eligible as collateral for lombard loans on condition that the sellers repurchased them forward. The repurchase periods varied between 28 and 33 days, and the interest rates between 5.1% and 6.0%. At the end of the year the Bank held DM 16,168.4 million of securities deriving from such transactions.

Lombard loans

At the end of 1983 the Bank's outstanding lombard loans to banks amounted to DM 13,294.8 million against DM 12,031.1 million at end-1982. The average level of such loans on all return days of the year under review was DM 5,779 million compared with DM 4,552 million in the previous year. The outstanding amount of such loans was subject to marked fluctuations, as in preceding years, and was largest on September 2, 1983, at DM 23,545 million.

Lombard rate

During the year under review the lombard rate was 6% until March 17, 5% from March 18 to September 8, and 5½% from September 9.

Cash advances (book credits)

Section 20 (1) 1 of the Bundesbank Act lays down the following credit ceilings:

	DM million
for the Federal Government	6,000
for the Federal Railways	600
for the Federal Post Office	400
for the Equalisation of Burdens Fund	200
for the ERP Special Fund	50

for the Länder Governments DM 40 per inhabitant; for Berlin, Bremen and Hamburg DM 80 per inhabitant.

Besides book credits, Treasury bills which the Bank holds in its portfolio or has undertaken to purchase are to be counted against these credit ceilings.

Federal Government, Equalisation of Burdens Fund, Länder Governments

Cash advances (book credits) outstanding

DM million

Borrower	December 31, 1982	December 31, 1983
Federal Government	–	–
Länder Governments		
Baden-Württemberg	–	–
Bavaria	181.6	–
Berlin	–	–
Bremen	54.7	54.1
Hamburg	144.0	130.0
Hesse	186.1	150.0
Lower Saxony	192.2	–
North Rhine-Westphalia	517.0	438.6
Rhineland-Palatinate	–	–
Saarland	30.5	42.0
Schleswig-Holstein	89.3	86.8
Total	1,395.4	901.5

The Equalisation of Burdens Fund and the ERP Special Fund took up no cash advances during the year under review.

Federal Railways, Federal Post Office

No book credits to the Federal Railways or Federal Post Office were outstanding at December 31, 1983; such credits, together with claims arising from the purchase of Treasury bills and Treasury discount paper, are to be shown in the item "Loans to the Federal Railways and Federal Post Office" on the assets side of the balance sheet.

Throughout the year the rate of interest on book credits was identical with the Bank's discount rate.

Treasury bills and Treasury discount paper

In the issuing of Treasury discount paper the Bank again acted as the selling agent for the Federal Government and its Special Funds. This paper, which serves financing purposes, is distinct from the mobilisation and liquidity paper issued pursuant to sections 42 and 42 (a) of the Bundesbank Act, which is reported on below. No Treasury bills serving financing purposes were issued during the year under review.

Federal Government

To meet the credit requirements of the Federal Government, Treasury discount paper amounting to DM 8,167.8 million (1982: DM 10,497.6 million) was issued. A large part of this sum (DM 5,441.8 million) consisted of sales to domestic banks of Treasury discount paper type "BN", which is not returnable before maturity. Since May 1983 these securities have been issued only with certain uniform periods to maturity per sale as parts of a collective holding (and no longer in the form of individual certificates).

The total issue figure includes DM 2,476.0 million (1982: DM 4,006.2 million) of Treasury "financing" paper of the Federal Government. The residual DM 250.0 million, consisting of paper returnable prior to maturity (type "B"), was purchased by an institutional investor.

After the redemption of DM 10,217.0 million (1982: DM 2,966.8 million) of matured Treasury discount paper (including Treasury financing paper), the amount of Treasury discount paper types "B" and "BN" outstanding at December 31, 1983 was DM 16,180.8 million (end-1982: DM 18,230.0 million). Of this total, DM 1,090.0 million was repurchasable by the Bank (type "B").

Federal Railways

Of the (returnable) Treasury discount paper of the Federal Railways (type "Ba") which fell due in 1983 totalling DM 231.0 million, DM 131.0 million was reissued. In addition, the Federal Railways issued DM 100.0 million of (non-returnable) Treasury discount paper type "BaN" direct through the Deutsche Verkehrs-Kredit-Bank AG, so that the amount of Treasury discount paper of the Federal Railways outstanding at end-1983 was DM 231.0 million, as in the previous year.

Federal Post Office

In the year under review, the outstanding amount of (non-returnable) Treasury discount paper of the Federal Post Office type "PN" remained unchanged; at end-1983 it came to DM 524.9 million.

The total amount of money market paper issued for the account of the Federal Government and its Special Funds and outstanding at December 31, 1983 was DM 16,936.7 million (end-1982: DM 18,985.9 million).

Money market paper issued for the account of the Federal Government and its special funds

DM million

Type of paper	Outstanding at Dec. 31, 1982	1983 Issued	1983 Redeemed	Outstanding at Dec. 31, 1983
Treasury discount paper of the Federal Republic of Germany type "B" 1 and type "BN" 2	18,230.0	8,167.8	10,217.0	16,180.8
of which Treasury financing paper	(5,373.3)	(2,476.0)	(3,826.8)	(4,022.5)
Treasury discount paper of the Federal Railways types "Ba" and "BaN" 2	231.0	231.0	231.0	231.0
Treasury discount paper of the Federal Post Office type "PN" 2	524.9	—	—	524.9
Total	18,985.9	8,398.8	10,448.0	16,936.7

1 The letter "B" serves to distinguish these bonds from the mobilisation and liquidity paper dealt with below. — 2 The letters "BN", "BaN" and "PN" denote securities which may not be returned before maturity.

Länder Governments

Of the money market paper of the Länder Governments, DM 200 million of Treasury discount paper was redeemed in 1983 and, by agreement with the Bank, DM 978 million was newly issued. At end-1983 DM 1,578 million of Treasury discount paper of the Länder Governments was still outstanding (end-1982: DM 800 million). This paper is not included in the money market regulating arrangements.

Equalisation claims on the Federal Government and non-interest-bearing debt certificate in respect of Berlin

The Bank's equalisation claims on the Federal Government and the non-interest-bearing debt certificate in respect of Berlin remained unchanged during the year under review. Since January 1, 1983 the interest rate on the Bank's equalisation claims has no longer been 3% p. a. but 1% p. a. (Act Accompanying the 1983 Budget, Article 9).

Loans to the Federal Railways and Federal Post Office

No loans to the Federal Railways or Federal Post Office were outstanding at December 31, 1983, as in the previous year. See also the notes on the items "Cash advances (book credits)" and "Treasury bills and Treasury discount paper".

Securities

During the year under review the Bank's portfolio of securities — chiefly bonds of the Federal Republic of Germany, the Federal Railways and the Federal Post Office — rose by DM 2,387.9 million net to DM 7,797.3 million owing to open market operations.

Issue of bonds

In 1983 13 bond issues totalling DM 17,900 million (1982: 15 bond issues amounting to DM 20,000 million) were launched through the Federal Bond Consortium, which is under the direction of the Bank. The Consortium took over DM 13,650 million of this total; the remainder was reserved for price regulation purposes.

At the end of 1983 the outstanding amount of bonds of the Federal Republic of Germany was DM 66,047.1 million (end-1982: DM 55,882.5 million), that of the Federal Railways was DM 15,745.3 million (end-1982: DM 16,733.0 million) and that of the Federal Post Office was DM 10,708.3 million (end-1982: DM 9,930.6 million).

Bond issues of the Federal Republic of Germany, the Federal Railways and the Federal Post Office in 1983

Issuer	Amount issued (DM million)		Terms				
	Total	of which Sold through Federal Bond Consortium	Nominal interest rate (%)	Maturity (years)	Issue price (%)	Yield (%)	Start of sales
Federal Republic of Germany	1,600	1,200	7.50	10	99.25	7.61	Jan. 3
Federal Railways	850	700	7.75	10	99.50	7.82	Jan. 26
Federal Post Office	1,000	800	7.75	10	99.50	7.82	Feb. 11
Federal Republic of Germany	1,600	1,200	7.50	10	99.75	7.54	Mar. 1
Federal Republic of Germany	1,600	1,200	7.50	8	100	7.50	May 9
Federal Republic of Germany	1,600	1,200	8.25	10	99.50	8.33	June 7
Federal Republic of Germany	1,600	1,200	8	10	99.25	8.11	July 7
Federal Republic of Germany	1,600	1,200	8.25	10	99.50	8.33	Aug. 5
Federal Post Office	800	650	8.50	10	100.25	8.46	Sep. 8
Federal Republic of Germany	1,600	1,200	8.25	10	99.50	8.33	Oct. 3
Federal Railways	850	700	8.25	10	100	8.25	Oct. 17
Federal Republic of Germany	1,600	1,200	8.25	10	100.25	8.21	Nov. 1
Federal Republic of Germany	1,600	1,200	8.25	10	99.25	8.36	Dec. 7

Issue of Federal savings bonds

With the Bank assisting in the selling operation, DM 3,815.6 million (gross) of Federal savings bonds were sold to private investors in 1983 through banks and by the Bank itself (1982: DM 2,870.2 million).

During the year under review the rate of interest paid on Federal savings bonds was raised five times and lowered three times to bring it into line with market rates.

Gross sales, interest rates and yields of Federal savings bonds in 1983

Issue	Sales period 1983	Gross sales (DM million) Total	Federal savings bonds type A [1]	Federal savings bonds type B [2]	Interest rate (I) in, and yield (Y) after, ... year after issue (% p.a.)	1st	2nd	3rd	4th	5th	6th	7th
1982/ 13+14	[3] Jan. 3– Jan. 12	[4] 319.6	149.9		I	5.00	7.00	7.50	8.00	8.25	8.50	
					Y	5.00	5.97	6.45	6.80	7.05	7.25	
				169.7	I	5.00	7.00	7.50	8.00	8.25	8.50	8.50
					Y	5.00	6.00	6.49	6.87	7.14	7.37	7.53
1983/ 1+2	Jan. 13– Mar. 16	791.2	378.3		I	5.00	6.50	7.00	7.25	7.75	8.50	
					Y	5.00	5.73	6.13	6.38	6.62	6.88	
				412.9	I	5.00	6.50	7.00	7.25	7.75	8.50	8.50
					Y	5.00	5.75	6.16	6.43	6.70	6.99	7.21
1983/ 3+4	Mar. 22– Apr. 21	225.6	104.0		I	4.00	5.50	6.00	7.00	7.50	8.25	
					Y	4.00	4.73	5.13	5.56	5.90	6.23	
				121.6	I	4.00	5.50	6.00	7.00	7.50	8.25	8.25
					Y	4.00	4.75	5.16	5.62	5.99	6.37	6.63
1983/ 5+6	Apr. 22– May 17	112.6	55.4		I	4.00	5.50	6.50	7.50	8.00	8.50	
					Y	4.00	4.73	5.29	5.79	6.18	6.50	
				57.2	I	4.00	5.50	6.50	7.50	8.00	8.50	8.50
					Y	4.00	4.75	5.33	5.87	6.29	6.66	6.92
1983/ 7+8	May 18– June 9	71.1	30.9		I	4.00	6.00	7.00	7.50	8.00	9.00	
					Y	4.00	4.98	5.61	6.04	6.38	6.74	
				40.2	I	4.00	6.00	7.00	7.50	8.00	9.00	9.00
					Y	4.00	5.00	5.66	6.12	6.49	6.90	7.20
1983/ 9+10	June 10– July 19	139.8	54.1		I	4.00	6.00	7.50	8.50	9.00	9.50	
					Y	4.00	4.98	5.77	6.38	6.83	7.20	
				85.7	I	4.00	6.00	7.50	8.50	9.00	9.50	9.50
					Y	4.00	5.00	5.82	6.49	6.98	7.40	7.70
1983/ 11+12	July 20– Sep. 2	184.6	61.2		I	4.25	6.50	8.25	9.00	9.25	9.75	
					Y	4.25	5.35	6.25	6.87	7.27	7.61	
				123.4	I	4,25	6,50	8,25	9.00	9.25	9.75	9.75
					Y	4.25	5,37	6.32	6.98	7.43	7.82	8.09
1983/ 13+14	Sep. 5– Dec. 29	1,971.1	719.0		I	5.50	8.00	8.00	8.50	8.50	10.00	
					Y	5.50	6.71	7.11	7.42	7.60	7.93	
				1,252.1	I	5.50	8.00	8.00	8.50	8.50	10.00	10.00
					Y	5.50	6.74	7.16	7.49	7.69	8.08	8.35
1984/ 1+2	Dec. 30*	[5] –	[5] –		I	5.50	7.50	8.00	8.25	8.25	9.50	
					Y	5.50	6.47	6.94	7.24	7.41	7.69	
				[5] –	I	5.50	7.50	8.00	8.25	8.25	9.50	9.50
					Y	5.50	6.50	6.99	7.31	7.49	7.83	8.06
Total	Jan. 3– Dec. 31*	3,815.6	1,552.8	2,262.8								

1 With annual payment of interest. — 2 With accrual of interest. — 3 Sales started on December 7, 1982. — 4 Sales between December 7, 1982 and December 31, 1982: Federal savings bonds type A DM 39.6 million, Federal savings bonds type B DM 55.2 million = DM 94.8 million. — 5 On December 30, 1983 orders only accepted as per January 2, 1984. — * Sales not completed on December 31, 1983.

During 1983 DM 97.7 million (1982: DM 961.7 million) of Federal savings bonds from earlier tranches were returned to the issuer before maturity, and a further DM 1,225.5 million were redeemed on maturity. The amount of Federal savings bonds outstanding rose from DM 13,508.0 million (end-1982) to DM 16,000.4 million at December 31, 1983.

Issue of five-year special Federal bonds

With the assistance of the Bank, sales of five-year special Federal bonds (which are tap issues and are sold in consecutive series) through the banks and by the Bank itself continued during the year under review.

In the year under review, DM 12,101.9 million (1982: DM 13,133.8 million) of newly issued special Federal bonds were sold in the market. In addition, DM

1,050.8 million was reserved for market regulation purposes after the completion of the issue of the current series.

During the year under review the terms of issue of special Federal bonds were brought into line with market conditions on 26 occasions.

Sales and terms of issue of five-year special Federal bonds in 1983

Designation Series	Start of sales	Terms (%) Nominal interest rate	Issue price	Yield	Amount issued (DM million) Sales per issue price	Sales Total	Price regulation share	Total	Date of admission to stock exchange dealing
S. 35 of 1982 (1987)	[1] Jan. 3	7.50	100.00	7.50	1,520.4	[2] 1,520.4	182.3	2,200	Jan. 25
S. 36 of 1983 (1988)	Jan. 11	7.25	99.40	7.40	335.4				
	Jan. 13		100.00	7.25	444.7				
	Feb. 9		98.80	7.55	324.7				
	Feb. 15		99.60	7.35	247.4				
	Feb. 25		100.00	7.25	385.7				
	Mar. 4		100.40	7.15	976.1	2,714.0	136.0	2,850	Mar. 22
S. 37 of 1983 (1988)	Mar. 9	6.75	99.20	6.94	233.4				
	Mar. 17		99.80	6.80	304.8	538.2	61.8	600	May 3
S. 38 of 1983 (1988)	Apr. 22	7.00	99.60	7.10	78.0				
	May 2		99.20	7.20	260.8	338.8	61.2	400	May 30
S. 39 of 1983 (1988)	May 18	7.25	99.80	7.30	82.3	82.3	17.7	100	June 8
S. 40 of 1983 (1988)	May 27	7.50	99.60	7.60	49.9				
	June 1		99.00	7.75	113.9	163.8	36.2	200	June 21
S. 41 of 1983 (1988)	June 10	8.00	100.00	8.00	1,189.6				
	June 15		100.60	7.85	58.9				
	June 16		101.00	7.75	521.2				
	July 13		100.00	8.00	671.4				
	July 25		100.60	7.85	147.7				
	Aug. 3		100.00	8.00	793.4	3,382.2	217.8	3,600	Sep. 12
S. 42 of 1983 (1988)	Sep. 1	8.00	99.40	8.15	1,383.2				
	Oct. 5		100.00	8.00	285.3				
	Oct. 10		100.60	7.85	435.2	2,103.7	96.3	2,200	Dec. 15
S. 43 of 1983 (1988)	Nov. 30	8.00	99.80	8.05	371.7	371.7	128.3	500	Dec. 28
S. 44 of 1983 (1988)	Dec. 16	8.25	100.00	8.25	645.7				
	Dec. 23		100.60	8.10	241.1	886.8	113.2	1,000	Jan. 10, 1984
S. 45 of 1984 (1989)	[3] Dec.30	8.00	100.00	8.00	[4] —	[4] —	[3] —	[3] —	Mar. 15, 1984

1 Sales started on December 7, 1982. — 2 Sales between December 7, 1982 and December 31, 1982 = DM 497.3 million. — 3 Sales not completed on December 31, 1983. — 4 On December 30, 1983 orders only accepted as per January 2, 1984.

The amount of special Federal bonds outstanding at the end of 1983 was DM 48,403.8 million (end-1982: DM 35,417.4 million).

Issue of medium-term notes

Through the agency of the Bank, DM 4,511.8 million of Treasury bonds (medium-term notes) of the Federal Government were sold in six issues by four tenders in 1983 (1982: DM 3,234.8 million by three tenders).

Treasury bonds (medium-term notes) of the Federal Republic of Germany sold by tender in 1983

Issuer	Amount sold (DM million)	Nominal interest rate (%)	Maturity (years)	Selling price (%)	Yield on issue (%)	Month of sale
Federal Republic of Germany	1,307.4	7	3	99.70	7.11	January
Federal Republic of Germany	467.6	7.25	4	99.30	7.46	January
Federal Republic of Germany	770.8	6.75	4	99.20	6.99	March
Federal Republic of Germany	630.2	7.75	3	99.60	7.90	June
Federal Republic of Germany	329.5	8	4	100	8	June
Federal Republic of Germany	1,006.3	8	4	99.40	8.18	August

At the end of 1983 the outstanding amount of medium-term notes of the Federal Republic of Germany was DM 13,053.5 million (end-1982: DM 8,957.6 million), that of the Federal Railways was DM 1,543.4 million (end-1982: DM 933.4 million) and that of the Federal Post Office was DM 2,100.9 million (end-1982: DM 2,100.9 million).

Admission to stock exchange dealing

The Bank introduced the new bond issues of the Federal Republic of Germany, the Federal Railways, the Federal Post Office and the Reconstruction Loan Corporation, as well as the five-year special Federal bond series 35 to 43, to official dealing on all German stock exchanges; it also introduced eight issues of bearer bonds of the Equalisation of Burdens Bank to regulated unofficial dealing on the Düsseldorf stock exchange.

In addition, the Bank introduced the new issues of medium-term notes of the Federal Republic of Germany, the Federal Railways and the Reconstruction Loan Corporation to regulated unofficial dealing on the Frankfurt stock exchange.

Price regulation operations

In the year under review, as in preceding years, the Bank conducted price regulation operations for the account of the issuers on the eight German stock exchanges in respect of the bonds issued by the Federal Government and its Special Funds, five-year special Federal bonds, and the bonds issued by one Land Government, the Reconstruction Loan Corporation and the Equalisation of Burdens Bank.

The Bank as paying and collecting agent for bonds

As the paying and collecting agent for, in particular, bonds (including external bonds) of the Federal Government and its Special Funds, the Bank paid 731,700 interest coupons and matured bonds in the year under review (1982: 1,492,271).

German coins

The amount of German coins held by the Bank came to DM 1,013.6 million at end-1983 (end-1982: DM 1,084.2 million). In 1983 the Federal Government was credited with DM 437.4 million for coins taken over from the Mints and debited with DM 9.0 million for coins no longer fit for circulation or melted down. Between 1948 and 1983 the Bank — acting for the account of the Federal Government — took over coins amounting to DM 11,305.8 million and redeemed DM 1,672.9 million of coins which were no longer fit to circulate or had been called in.

The total amount of coins in circulation at the end of 1983 (DM 8,619.3 million) divided by the number of inhabitants of the Federal Republic of Germany, and Berlin (West) on September 30, 1983 (61.4 million) yields a coin circulation of DM 140.37 per head of population (1982: DM 131.81).

During the year under review the DM 5 commemorative coins "Karl Marx" and "Martin Luther" were put into circulation.

Balances on postal giro accounts

The postal giro account balances, including the branches' transfers in transit to the postal giro account of the Bank (Central Office) in Frankfurt am Main, amounted to DM 238.5 million at December 31, 1983 (December 31, 1982: DM 150.3 million). The Bank's credit balances on the latter account and on the postal giro account of the Land Central Bank in Berlin, other than those required for current payments, are offset daily, in rounded amounts, against the giro balances of the Central Cash Office of the Federal Post Office and the Berlin (West) Postal Giro Office.

Postal giro transactions with third parties

	1982				1983			
	Transfers received from third parties		Transfers made to third parties		Transfers received from third parties		Transfers made to third parties	
Area	Number	DM million	Number	DM million	Number	DM million	Number	DM million
Land Central Bank								
Baden-Württemberg	64,932	18,391.1	5,981	2,344.0	72,236	18,646.7	5,527	2,510.9
Bavaria	40,666	13,148.4	6,802	6,545.5	41,179	13,162.0	8,048	7,337.3
Berlin	17,842	2,963.8	2,305	977.8	17,082	3,049.0	2,147	1,560.4
Bremen	4,654	380.8	94	0.0	4,741	388.0	103	0.0
Hamburg	114,112	18,913.2	1,306	317.2	115,076	19,818.7	2,031	594.7
Hesse	75,927	8,605.3	3,660	7,392.0	85,565	8,584.6	3,593	6,855.8
Lower Saxony	50,597	8,215.3	3,218	2,314.6	50,597	8,877.8	3,783	2,842.0
North Rhine-Westphalia	141,715	22,885.4	10,789	7,202.3	141,105	23,852.3	10,454	7,909.3
Rhineland-Palatinate	18,858	1,278.3	4,161	825.6	18,771	1,194.6	3,943	820.6
Saarland	5,564	1,926.9	159	0.1	6,056	2,044.1	132	0.1
Schleswig-Holstein	4,768	84.9	723	0.5	5,088	72.3	638	7.7
Total	539,635	96,793.4	39,198	27,919.6	557,496	99,690.1	40,399	30,438.8
Bundesbank — Central Office —	5,169	1,912.1	828	3.3	4,991	2,249.2	842	3.8
Grand total	544,804	98,705.5	40,026	27,922.9	562,487	101,939.3	41,241	30,442.6

Land and buildings

After additions amounting to DM 231.8 million and depreciation totalling DM 112.1 million, land and buildings are shown at DM 1,386.7 million.

Furniture and equipment

The balance sheet value of furniture and equipment is DM 119.2 million after additions totalling DM 63.7 million and depreciation amounting to DM 52.2 million.

Items in course of settlement

The "Items in course of settlement" mainly comprise the intercity credit and debit transfers proceeding inside the Bank at the end of the year and the cheques and direct debits being cleared. At December 31, 1983 the balance of items in course of settlement stood at DM 3,487.1 million against DM 2,970.4 million at end-1982.

Other assets

In this item, other assets are shown at DM 3,977.0 million at end-1983 (end-1982: DM 3,411.6 million). This item primarily includes the interest due in 1984 but assignable to the profit and loss account for the year under review on funds invested abroad and securities (DM 3,079.3 million against DM 2,514.0 million at end-1982) and the balance arising from intra-German settlements (commercial payments under the "Berlin Agreement"), which amounted to DM 480.7 million (1982: DM 489.8 million). The regulations governing intra-German payments are outlined in Part A IV of the German original of this Report.

This item also contains the Bank's 30% share, amounting to DM 75 million, in the capital of the Liquidity Consortium Bank of Frankfurt am Main (set up as a private limited company). The provision included in the articles of association of that bank that, if necessary, further capital is to be paid up in proportion to the existing share entails for the Bank a maximum commitment of DM 225 million.

Prepaid expenses and deferred income

The prepaid expenses and deferred income almost entirely comprise salary and pension payments made in the year under review but relating to 1984.

Liabilities

Banknotes in circulation

The amount of banknotes in circulation at December 31, 1983, at DM 96,073.0 million, was DM 7,498.3 million larger than at end-1982.

Currency in circulation

DM million

End of	Bundesbank notes	Federal coins	Currency in circulation, total
1978	74,799.1	6,577.5	81,376.6
1979	79,385.6	6,988.7	86,374.3
1980	83,730.3	7,461.0	91,191.3
1981	83,790.3	7,816.6	91,606.9
1982	88,574.7	8,120.2	96,694.9
1983	96,073.0	8,619.3	104,692.3

The denominations of the Bundesbank notes and Federal coins in circulation are shown in Appendix 3 to the German original of this Report.

In the year under review the Bank again took over new Bundesbank notes of various denominations from the printing works and put them into circulation or made them ready for that purpose.

The banknotes (including monetary tokens) destroyed as being no longer fit for circulation or after having been called in amounted to:

	1978	1979	1980	1981	1982	1983
Number (millions)	560.9	505.9	466.4	662.3	834.5	582.9
Value (DM million)	22,682.1	20,829.6	18,495.1	28,793.9	39,604.0	24,938.5.

In the year under review the number and value of the counterfeit Bundesbank notes detained in payments in the Federal Republic of Germany and Berlin (West) dropped distinctly in comparison with the preceding year.

The further rise in the counterfeit coins detected is primarily due to the greater incidence of counterfeit DM 1 and DM 2 coins.

Counterfeits detected in payments

Year	Bundesbank notes		Federal coins	
	Number	DM thousand	Number	DM thousand
1978	6,341	586.4	9,835	35.5
1979	3,388	296.6	7,405	24.3
1980	2,421	183.4	9,428	25.1
1981	2,896	219.1	17,172	34.3
1982	3,317	250.7	19,975	43.3
1983	2,156	181.7	26,607	56.1

Deposits of banks

The banks' deposits on giro accounts are mainly composed of the minimum reserves to be held at the Bank. The sub-item "Other" contains the deposits of domestic banks on U.S. dollar accounts. At the end of the year, compared with end-1982, the deposits were made up as follows:

	Dec. 31, 1982 DM million	Dec. 31, 1983 DM million
Deposits on giro accounts	51,854.9	52,681.2
Other	20.2	20.8
	51,875.1	52,702.0.

Deposits of public authorities

In the item "Deposits of public authorities" the current balances of public authorities are shown as follows:

	Dec. 31, 1982 DM million	Dec. 31, 1983 DM million
Federal Government	723.6	1,516.8
Equalisation of Burdens Fund and ERP Special Fund	162.2	19.1
Länder Governments	330.0	592.2
Other public depositors	42.3	31.9
	1,258.1	2,160.0.

Deposits of other domestic depositors

The deposits of other domestic depositors were composed as follows:

	Dec. 31, 1982 DM million	Dec. 31, 1983 DM million
Federal Railways	19.8	10.4
Federal Post Office (including postal giro and postal savings bank offices)	2,865.8	2,561.8
Other depositors	629.7	599.6
	3,515.3	3,171.8.

Giro transactions, simplified cheque and direct debit collections

Almost 100% of the turnover on the giro accounts was settled on a cashless basis, in terms of both the number of transactions and the amount involved, as in the previous year.

Annual turnover on the giro accounts of the Bank

Type of turnover	1982 Number of transactions	1982 Total amount	1982 Average amount	1983 Number of transactions	1983 Total amount	1983 Average amount
	Thousands	DM million	DM thousand	Thousands	DM million	DM thousand
(a) Credits						
Cash payments	1,069	214,935	201.1	1,066	221,792	208.1
Clearings with account-holders	4,219	4,584,719	1,086.7	4,008	4,902,191	1,223.1
Local transfers	78,972	4,764,580	60.3	83,408	5,373,283	64.4
Intercity transfers	291,028	4,899,258	16.8	318,135	5,486,555	17.2
Cheque and direct debit collections (total presented)	1,097,794	2,041,085	1.9	1,158,858	2,153,736	1.9
Total	1,473,082	16,504,577	–	1,565,475	18,137,557	–
(b) Debits						
Cash payments	1,546	222,819	144.1	1,576	231,394	146.8
Clearings with account-holders	3,127	4,453,782	1,424.3	2,993	4,760,915	1,590.7
Local transfers	78,972	4,764,580	60.3	83,408	5,373,283	64.4
Intercity transfers	291,337	5,021,074	17.2	318,959	5,590,432	17.5
Cheque and direct debit collections (total paid)	1,098,323	2,038,695	1.9	1,158,833	2,150,089	1.9
Total	1,473,305	16,500,950	–	1,565,769	18,106,113	–
(c) Percentage of total turnover (credits and debits)						
Cash payments	0.09	1.33	–	0.08	1.25	–
Clearings with account-holders	0.25	27.38	–	0.22	26.66	–
Local transfers	5.36	28.87	–	5.33	29.65	–
Intercity transfers	19.76	30.06	–	20.35	30.56	–
Cheque and direct debit collections (total presented and paid)	74.54	12.36	–	74.02	11.88	–
Total	100.00	100.00	–	100.00	100.00	–

In 1983 the turnover on the giro accounts of the Bank increased over the previous year by 6 % in terms of the number of transactions and by 10 % in terms of the amount involved. The number of intercity transfers went up by 9 % (1982: 7 %).The number of items presented by the banks under the simplified collection procedure for cheques and direct debits grew by around 6 % (1982: 7 %). The number of cash outpayments (1.6 million) and cash inpayments (1.1 million) remained practically unchanged.

In the year under review 99 % of the 530 million vouchers presented for collection and about 98 % of the 207 million paper-based credit transfers, as well as 629 million direct debits (1982: 579 million) and 112 million credit transfers (1982: 105 million) recorded on magnetic tape, were processed by the Bank's computer centres. The volume of payments executed through the paperless exchange of data media was 8 % larger than in the preceding year. Such payments now account for more than half (50.5 %) of the payment items presented under the automated procedure. Altogether, 99 % of intercity transfers — paper-based as well as paperless — were processed automatically in the year under review.

Automation of intercity transfers

Year	Collection orders presented							Intercity credit transfers presented						
		processed							processed					
		in paper-based operations				through the paperless exchange of data media			in paper-based operations				through the paperless exchange of data media	
	Total	conventional		automated				Total	conventional		automated			
	millions	millions	%	millions	%	millions	%	millions	millions	%	millions	%	millions	%
1973	317	175	55	142	45	0	0	113	113	100	0	0	0	0
1974	374	142	38	232	62	0.2	0	123	75	61	48	39	0.1	0
1975	423	143	34	272	64	8	2	163	85	52	73	45	5	3
1976	501	83	17	313	62	105	21	174	62	36	83	48	29	16
1977	587	47	8	359	61	181	31	169	36	21	87	51	46	28
1978	694	31	5	412	59	251	36	183	26	14	89	49	68	37
1979	775	15	2	441	57	319	41	192	13	7	95	49	84	44
1980	873	11	1	473	54	389	45	230	7	3	125	54	98	43
1981	1,023	8	1	490	48	525	51	271	7	2	162	60	102	38
1982	1,098	7	1	512	46	579	53	291	6	2	180	62	105	36
1983	1,159	6	1	524	45	629	54	319	5	2	202	63	112	35

If local payments and clearing transactions — which, apart from local credit transfers in Hamburg, are not yet processed automatically — are also taken into account, 79% of cashless payments at the Bank are automated. It should be borne in mind in this connection that magnetic tapes containing payments are increasingly being exchanged locally between banks in clearing transactions, although only the total amounts are being cleared by this (conventional) procedure.

As a result of the progressive automation, the concentration of the incoming payment items continued in 1983. Since 1973 the number of items entered in giro accounts in intercity payments has fallen from 166 million to 29.3 million on the dispatch side, in spite of the simultaneous rise in the number of payments from 430 million to 1,478 million.

Liabilities arising from mobilisation and liquidity paper sold

In the year under review sales of mobilisation and liquidity paper pursuant to sections 42 and 42(a) of the Bundesbank Act, at DM 30,660.9 million, rose slightly against the preceding year (DM 29,165.4 million). Sales of these instruments consisted mostly of Treasury bills for the purpose of the revolving investment of funds of foreign institutions; there were no transactions with domestic banks in the year under review. Sales amounting to DM 30,519.7 million (1982: DM 29,004.6 million) were accompanied by redemptions totalling DM 28,950.7 million (1982: DM 29,361.9 million), so that the amount outstanding rose to DM 6,070.8 million (1982: DM 4,501.8 million).

The Bank sold DM 141.2 million of mobilisation and liquidity Treasury discount paper in 1983 (1982: DM 160.8 million), so that, after redemptions totalling DM 65.8 million, DM 225.2 million of such paper was outstanding at December 31, 1983 (end-1982: DM 149.8 million). The liabilities arising from mobilisation and liquidity paper outstanding amounted in all to DM 6,296.0 million at December 31, 1983 (end-1982: DM 4,651.6 million).

Mobilisation and liquidity paper sold and redeemed

DM million

Type of paper	1982 Outstanding at December 31	1983 Sold	Redeemed	Outstanding at December 31
Treasury bills (running for up to 90 days)	4,501.8	30,519.7	28,950.7	6,070.8
Treasury discount paper (running for 6 to 24 months)	149.8	141.2	65.8	225.2
Total	4,651.6	30,660.9	29,016.5	6,296.0

Liabilities arising from external transactions

The liabilities arising from external transactions fell to DM 9,780.5 million at end-1983 compared with DM 12,035.0 million at end-1982. In particular, the liabilities to foreign monetary authorities decreased. Specifically, the liabilities from external transactions were made up as follows:

		Dec. 31, 1982		Dec. 31, 1983
	DM million	DM million	DM million	DM million
Deposits of foreign depositors				
Banks	9,108.6		9,380.5	
Other depositors	401.4	9,510.0	383.1	9,763.6
Other				
Provision of cover for credits, etc.	11.3		12.0	
Miscellaneous liabilities	2,513.7	2,525.0	4.9	16.9
		12,035.0		9,780.5.

Counterpart of special drawing rights allocated

The counterpart of the special drawing rights allocated by the International Monetary Fund and shown on the assets side of the balance sheet in sub-item 2.3 corresponds to the allocations of SDRs to the Federal Republic of Germany between 1970 and 1972 and from 1979 to 1981, which totalled SDR 1,210.8 million.

Provisions
Provisions for pensions

DM 133.9 million was withdrawn from the provisions for pensions in order to pay retirement pensions and widows' and orphans' pensions. After an increase of DM 163.9 million, these provisions amounted to DM 2,066.0 million at December 31, 1983 against DM 2,036.0 million at end-1982.

Provisions for other purposes

DM 244.0 million was withdrawn from and DM 2,100.2 million was added to the provisions for other purposes. At end-1983 they totalled DM 4,126.2 million (end-1982: DM 2,270.0 million). They serve chiefly to meet the general hazards inherent in domestic and external transactions as well as risks arising from time commitments in course of settlement (see also the following notes on the receipts item "Receipts from purchases and sales of foreign currency and from the valuation of monetary reserves and other foreign currency positions").

Other liabilities

The other liabilities are shown at DM 159.9 million against DM 186.4 million at end-1982.

Deferred expenses and accrued income

Deferred expenses and accrued income amounted to DM 380.8 million at December 31, 1983 (end-1982: DM 675.7 million). As before, this item mainly comprised interest received in the year under review, but relating to the following year, on domestic and foreign bills and U.S. Treasury Notes.

Capital

The capital of the Bank amounts to DM 290 million; it is held by the Federal Government (section 2 of the Bundesbank Act).

Reserves

In accordance with the decision taken by the Central Bank Council on April 7, 1983, the legal reserves were increased by DM 239.2 million out of the unappropriated profit for 1982. After this increase the legal reserves totalled DM 4,428.7 million; they thus reached the maximum level permissible by law of 5% of the amount of banknotes in circulation, which came to DM 88,574.7 million at end-1982. The other reserves reached the statutory ceiling of DM 290 million at the end of 1980.

Unappropriated profit

See the notes on page 110 of this Report.

Contingent liabilities and claims

The contingent liabilities and claims amounted to DM 0.1 million against DM 1.2 million at end-1982.

Profit and loss account

Comparison of expenditure and receipts

DM million

Expenditure	1982	1983	Receipts	1982	1983
			Interest received		
Interest paid on foreign exchange transactions under repurchase agreements and swaps with domestic banks	14.0	20.0	Funds invested abroad	8,044.8	9,386.1
Interest paid on mobilisation and liquidity paper	360.1	248.1	Lending to domestic banks	5,011.9	2,922.2
Other interest paid	10.3	10.2	Equalisation claims	244.1	81.4
	384.4	278.3	Securities	407.0	594.0
Administrative expenditure			Cash advances (book credits)	173.9	90.7
Staff costs	700.3	719.8	Other interest received	3.5	8.3
Other	155.7	164.4		13,885.2	13,082.7
Note printing	139.5	153.9	Fees received	16.4	19.0
Depreciation	156.8	164.4	Receipts arising from purchases and sales of foreign currency and from the valuation of the monetary reserves and other foreign currency positions	–	2,140.1
Increases in provisions			Other receipts	103.5	99.1
for pensions	192.3	163.9			
for other purposes	594.0	1,856.2			
Pension payments in respect of the Reichsbank	30.9	28.9			
Other expenditure	33.9	40.6			
Write-downs of monetary reserves and other foreign currency positions	310.7	–			
Profit for the year (= unappropriated profit)	11,306.6	11,770.5			
Total	14,005.1	15,340.9	Total	14.005.1	15,340.9

Interest

	1982 DM million	1983 DM million
Interest received amounted to	13,885.2	13,082.7;
after deduction of interest paid, namely	384.4	278.3,
interest is shown in the profit and loss account at	13,500.8	12,804.4.

In the year under review, total interest income, at DM 13,082.7 million, was DM 802.5 million lower than in 1982. In spite of falling interest rates, the interest received from external transactions rose from DM 8,044.8 million to DM 9,386.1 million. As in 1982, this was mainly because the depreciation of the Deutsche Mark led to an increase in the Deutsche Mark equivalent of the interest income paid in dollars. By contrast, receipts from lending to domestic banks — domestic bills, security transactions under repurchase agreements, lombard loans and foreign bills bought in Germany — decreased by DM 2,089.7 million to DM 2,922.2 million, mainly on account of lower interest rates. The interest received from securities rose by DM 187.0 million to DM 594.0 million, the security portfolio being larger. The interest received from equalisation claims dropped by DM 162.7 million to DM 81.4 million as the interest rate on such claims has been 1% rather than 3% since January 1, 1983. Other interest income decreased from DM 177.4 million to DM 99.0 million, chiefly owing to the fall in interest received from cash advances.

The interest paid, at DM 278.3 million, declined by DM 106.1 million against the previous year. DM 248.1 million (1982: DM 360.1 million) was disbursed on Treasury bills and Treasury discount paper of the Federal Government (mobilisation and liquidity paper pursuant to sections 42 and 42 (a) of the Bundesbank Act); DM 20.0 million (1982: DM 14.0 million) was expended on foreign exchange transactions under repurchase agreements and swaps.

Fees

Fees totalling DM 19.0 million were received in the year under review (1982: DM 16.4 million).

Receipts from purchases and sales of foreign currency and from the valuation of the monetary reserves and other foreign currency positions

This item contains DM 2,140.1 million of receipts stemming from purchases and sales of foreign currency and, in particular, from the changes in the exchange rate of the Deutsche Mark vis-à-vis the special drawing right (SDR). The valuation gains included therein were retained among provisions. The valuation of claims denominated in U.S. dollars remained unchanged at DM 1,7275. (In 1982 write-downs of the monetary reserves and other foreign currency positions amounted to DM 310.7 million.)

Other receipts

The other receipts are shown at DM 99.1 million against DM 103.5 million in the preceding year.

Expenditure

Administrative expenditure
Staff costs

Administrative expenditure on personnel grew by DM 19.5 million to DM 719.8 million. This was chiefly attributable to statutory or negotiated pay rate increases for established employees ("officials") and unestablished wage and salary earners.

In 1983 the number of employees remained practically unchanged; it fell by 7 to 15,024. This figure includes 84 trainees who were recruited in the year under review and are employed in newly created trainee positions.

Staff of the Bank

Staff	Beginning of 1983					Beginning of 1984				
	Central Office	Land Central Banks	Total 1	of whom male	of whom female	Central Office	Land Central Banks	Total 1	of whom male	of whom female
Officials	880	5,419	6,299	5,832	467	905	5,484	6,389	5,894	495
Salary earners	1,600	6,054	7,654	3,568	4,086	1,575	5,984	7,559	3,534	4,025
Wage earners	237	841	1,078	217	861	225	851	1,076	200	876
Total	2,717	12,314	15,031	9,617	5,414	2,705	12,319	15,024	9,628	5,396

1 of whom	Beginning of 1983	Beginning of 1984
(a) Salaried staff working outside the Bank or released to work for international institutions	77	88
(b) Trainees	680	704
(c) Part-time staff		
Salaried staff	477	475
Wage earners	729	744

Payments to serving members of the Directorate of the Bank and the Central Bank Council amounted to DM 7,194,997.51 in the year under review. Former members of these bodies and of the Board of Directors and Board of Managers of the Bank deutscher Länder and the Managing Boards of the Land Central Banks, including their surviving dependants, received payments totalling DM 7,574,512.63.

Changes in staff regulations

In 1983 the Bank again entered into a number of pay agreements, thereby bringing the legal situation of its wage and salary earners into line with that of the wage and salary earners of the Federal Government.

Other

Other (non-staff) administrative expenditure increased by DM 8.7 million to DM 164.4 million during the year under review.

Note printing

Expenditure on note printing amounted to DM 153.9 million against DM 139.5 million in the previous year.

Depreciation and increases in provisions

Depreciation of land and buildings and of furniture and equipment was discussed in connection with the respective balance sheet items, as were increases in provisions.

Pension payments in respect of the Reichsbank

Payments to members of the former Deutsche Reichsbank and other persons to whom the Act concerning Article 131 of the Basic Law applies, for whom the Bank is required to provide in accordance with section 41 of the Bundesbank Act, at DM 28.9 million, declined slightly in the year under review.

Other expenditure

Other expenditure is shown at DM 40.6 million (1982: DM 33.9 million).

			DM
Unappropriated profit	The profit and loss account for 1983 shows a profit for the year of which is shown in the balance sheet as unappropriated profit (net profit).		11,770,539,360.98
Proposed distribution of profit	In accordance with section 27 of the Bundesbank Act, the Directorate proposes to the Central Bank Council that the following appropriations should be made:	DM	
	to the legal reserves	374,900,000.00	
	to the Fund for the purchase of Equalisation Claims	30,000,000.00	404,900,000.00.
	The balance of		11,365,639,360.98
	will be transferred to the Federal Government.		

After this appropriation, the legal reserves will amount to DM 4,803,600,000.00; as in the previous year, they will then come up to the statutory ceiling of 5% of the amount of banknotes in circulation, which totalled DM 96,073,021,755.00 at the end of 1983. The other reserves reached the statutory ceiling of DM 290,000,000.00 at the end of 1980.

Frankfurt am Main, April 1984

Deutsche Bundesbank
The Directorate
Pöhl Dr. Schlesinger
Dr. Emde Dr. Gleske Prof. Dr. Köhler Werthmöller

Part D: Report of the Central Bank Council

The annual accounts of the Deutsche Bundesbank for 1983 and the Report on the Fund for the Purchase of Equalisation Claims as at December 31, 1983, were audited by Treuarbeit Aktiengesellschaft Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft of Frankfurt am Main and Dr. Wollert — Dr. Elmendorff KG Wirtschaftsprüfungsgesellschaft of Düsseldorf, whom the Central Bank Council had appointed to be auditors in accordance with section 26 of the Bundesbank Act.

In their certificates of audit the auditors confirmed without qualifications that the annual accounts for 1983 and the bookkeeping as shown by the books at December 31, 1983, complied with German law and that the Fund for the Purchase of Equalisation Claims had been properly administered.

The Central Bank Council approved the annual accounts for 1983 on April 12, 1984, and accepted the Directorate's proposal in respect of the profit distribution. At the same time it approved the Report on the Fund for the Purchase of Equalisation Claims as at December 31, 1983.

Since the publication of the Report for the Year 1982 the following changes have taken place in the Central Bank Council and the Directorate of the Deutsche Bundesbank:

Retired
as at the close of December 31, 1983

the Vice-President of the Land Central Bank in Bremen
Joachim Treskow,

the Vice-President of the Land Central Bank in Saarland
Dr. Herwald Schmidt.

Reappointed
with effect from April 1, 1984

Dr. Leonhard Gleske
Member of the Directorate of the Deutsche Bundesbank,

Dr. Kurt Nemitz
President of the Land Central Bank in Bremen.

Appointed
with effect from January 1, 1984

Johannes Kremers
Vice-President of the Land Central Bank in Bremen,

Erhard Dauzenroth
Vice-President of the Land Central Bank in Saarland.

The Central Bank Council, acting also on behalf of the Directorate and of the Managing Boards of the Land Central Banks, expresses to the entire staff of the Deutsche Bundesbank its thanks for their loyal and understanding cooperation during 1983. The Council likewise wishes to record its appreciation of the excellent collaboration with the staff representative committees.

Frankfurt am Main, April 1984

Karl Otto Pöhl
President of the Deutsche Bundesbank

Appendix to Part B

Balance sheet of the Deutsche Bundesbank as at December 31, 1983

Assets

		DM	DM
1 Gold			13,687,518,821.70
2 Reserve position in the International Monetary Fund and special drawing rights			
2.1 Drawing rights within the reserve tranche		7,704,995,904.47	
2.2 Loans under special borrowing arrangements		2,503,753,315.47	
2.3 Special drawing rights		4,394,093,223.27	14,602,842,443.21
3 Claims on the European Monetary Cooperation Fund in connection with the European Monetary System			
3.1 ECU balances resulting from the provisional contribution of gold and dollar reserves	39,427,465,065.26		
less Difference between the ECU value and the book value of the reserves contributed	26,931,352,795.17	12,496,112,270.09	
3.2 ECU balances resulting from transfers from other central banks		2,948,265,202.61	
3.3 Other claims		—	15,444,377,472.70
4 Balances with foreign banks and money market investments abroad			37,794,134,872.01
5 Foreign notes and coins			24,702,660.28
6 External loans and other external assets			
6.1 Loans in connection with EEC medium-term monetary assistance		—	
6.2 Other loans to foreign monetary authorities		—	
6.3 Loans to the World Bank		2,455,698,000.—	2,455,698,000.—
7 Foreign bills of exchange			9,448,413,313.03
8 Domestic bills of exchange			46,586,494,032.07
9 Securities bought in open market transactions under repurchase agreements			16,168,428,764.19
10 Lombard loans			13,294,767,600.—
11 Cash advances (book credits)			
11.1 Federal Government		—	
11.2 Equalisation of Burdens Fund		—	
11.3 Länder Governments		901,461,161.—	901,461,161.—
12 Treasury bills and Treasury discount paper			
12.1 Federal Government		—	
12.2 Länder Governments		—	—
13 Equalisation claims on the Federal Government and non-interest-bearing debt certificate in respect of Berlin			8,683,585,988.93
14 Loans to the Federal Railways and Federal Post Office			
14.1 Cash advances (book credits)		—	
14.2 Treasury bills and Treasury discount paper		—	—
15 Securities			7,797,296,367.86
16 German coins			1,013,595,490.31
17 Balances on postal giro accounts			238,460,118.22
18 Land and buildings			1,386,734,046.63
19 Furniture and equipment			119,197,520.—
20 Items in course of settlement			3,487,067,278.42
21 Other assets			3,977,014,522.37
22 Prepaid expenses and deferred income			36,319,647.17
Rights of recourse in respect of contingent liabilities		120,915.41	
			197,148,110,120.10

	DM	DM
1 Banknotes in circulation		96,073,021,755.–
2 Deposits of banks		
2.1 Deposits on giro accounts	52,681,187,153.80	
2.2 Other	20,806,879.24	52,701,994,033.04
3 Deposits of public authorities		
3.1 Federal Government	1,516,855,097.56	
3.2 Equalisation of Burdens Fund and ERP Special Fund	19,061,434.78	
3.3 Länder Governments	592,170,986.02	
3.4 Other public depositors	31,895,018.28	2,159,982,536.64
4 Deposits of other domestic depositors		
4.1 Federal Railways	10,352,938.13	
4.2 Federal Post Office (including postal giro and postal savings bank offices)	2,561,795,993.95	
4.3 Other depositors	599,602,662.15	3,171,751,594.23
5 Liabilities arising from mobilisation and liquidity paper sold		6,296,000,000.–
6 Liabilities arising from external transactions		
6.1 Deposits of foreign depositors	9,763,614,339.73	
6.2 Other	16,888,193.45	9,780,502,533.18
7 Counterpart of special drawing rights allocated		3,452,712,184.40
8 Provisions		
8.1 Provisions for pensions	2,066,000,000.–	
8.2 Provisions for other purposes	4,126,200,000.–	6,192,200,000.–
9 Other liabilities		159,888,090.42
10 Deferred expenses and accrued income		380,818,032.21
11 Capital		290,000,000.–
12 Reserves		
12.1 Legal reserves	4,428,700,000.–	
12.2 Other reserves	290,000,000.–	4,718,700,000.–
13 Unappropriated profit		11,770,539,360.98
Contingent liabilities	120,915.41	
		197,148,110,120.10

Profit and loss account of the Deutsche Bundesbank for the year 1983

Expenditure

	DM	DM
1 Administrative expenditure		
1.1 Staff costs	719,779,045.37	
1.2 Other	164,355,275.02	884,134,320.39
2 Note printing		153,904,872.—
3 Depreciation		
3.1 of land and buildings	112,117,602.75	
3.2 of furniture and equipment	52,236,397.50	164,354,000.25
4 Increases in provisions		
4.1 for pensions	163,932,755.94	
4.2 for other purposes	1,856,200,000.—	2,020,132,755.94
5 Pension payments in respect of the Reichsbank		28,886,802.48
6 Other expenditure		40,628,365.03
7 Profit for the year (= unappropriated profit)		11,770,539,360.98
		15,062,580,477.07

Receipts

	DM
1 Interest	12,804,360,709.91
2 Fees	19,020,163.83
3 Receipts from purchases and sales of foreign currencies and from the valuation of the monetary reserves and other foreign currency positions	2,140,101,448.19
3 Other receipts	99,098,155.14
	15,062,580,477.07

Frankfurt am Main, February 8, 1984

Deutsche Bundesbank
The Directorate
Pöhl Dr. Schlesinger
Dr. Emde Dr. Gleske Prof. Dr. Köhler Werthmöller

According to the audit which we have duly carried out, the bookkeeping and annual accounts comply with German law and the Bank's by-laws.

Frankfurt am Main, March 12, 1984

Treuarbeit Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft

Dr. Scholz
Certified Auditor

Goldbach
Certified Auditor

Dr. Wollert — Dr. Elmendorff KG
Wirtschaftsprüfungsgesellschaft

Thoennes
Certified Auditor

Euskirchen
Certified Auditor