

## German balance of payments in 1997

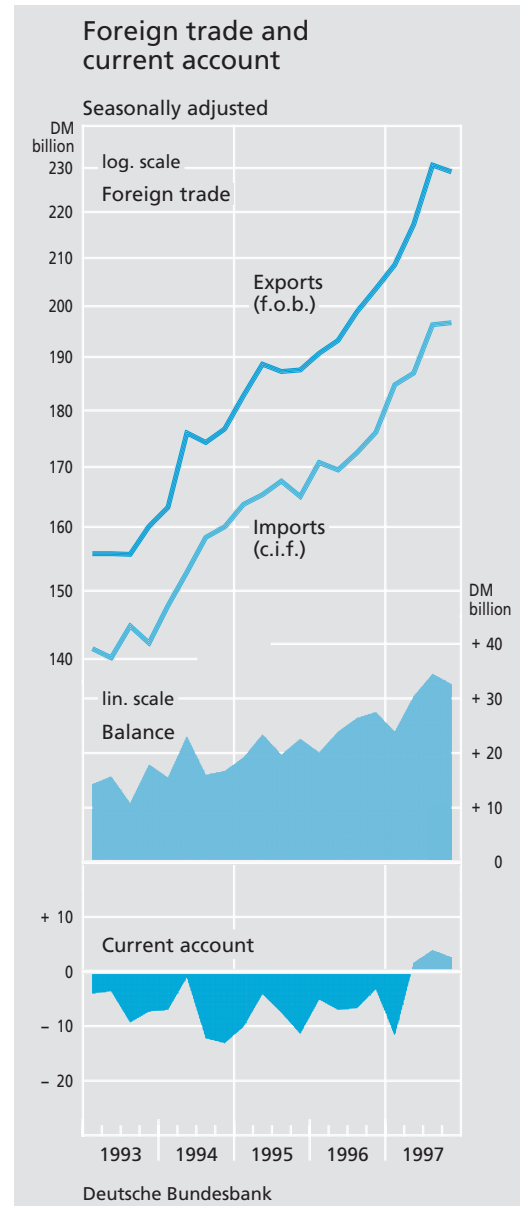
Exports exerted particularly dynamic growth stimuli on the German economy and that of its trading partners last year. On the one hand, exports of German goods grew at a rate in double figures, which was significantly above the growth rate of world trade in general. On the other hand, imports picked up more sharply than would have been expected in the light of the weak domestic demand alone. The unusually rapid growth in exports generated a trade surplus which, at DM 122 billion, almost matched the record levels produced during the export boom prior to German reunification. Fairly substantial deficits were again recorded in invisibles, however, with the result that the German current account as a whole ran a slight deficit of DM 1½ billion; this was still much smaller than in 1996 (DM 20½ billion). For most of last year cross-border financial transactions were marked by the boom in the international equity and bond markets. This encouraged German residents to build up their foreign investments sharply; at the same time foreign investors provided the German market with a new impetus by continuing to make substantial purchases of securities in Germany. These trends are presented and explained in detail below.

## Current account

### Exports

Following the distinct revival in German exports which had already begun in the course of 1996, the value of the goods Germany exported in 1997 rose by 12 ½ % to DM 887 ½ billion. Although part of this increase was due to the somewhat higher export prices, the rise in exports was still considerable even in real terms – that is to say, when calculated at constant prices. With an increase of 11%, the rise in exports clearly exceeded the simultaneous (real) growth in world trade, which, according to estimates by the International Monetary Fund, was probably about 9%. Two factors contributed to this favourable result. Firstly, the changing regional pattern of world trade growth benefited Germany's traditional export markets. Secondly, German enterprises were apparently also successful in 1997 in winning market shares.

The international competitiveness of German business improved considerably during the past two years. The "normalising" of exchange rate patterns played an important role in this. Another factor was the successful adjustment measures which enterprises had taken to lower costs and rationalise production and which had resulted in considerable improvements in productivity. These measures, together with the moderate wage policy, led to a significant decline in the unit labour costs of German business. The average real external value of the Deutsche Mark against the currencies of 18 industrial countries fell by almost 8 ½ % in 1997 compared with its level in 1995. The picture remains little changed even after taking into account



the depreciations of a number of South-East Asian currencies because the share of this region in Germany's foreign trade is relatively small.

However, the sales successes of German entrepreneurs have also to be seen not least in the light of the buoyancy of German export markets. Demand from the countries in transition in central and eastern Europe was

*Regional  
breakdown  
of exports*

particularly strong; exports to these countries, which currently absorb about one-tenth of total German exports, grew by 27 ½ % in the first 11 months of 1997 (more up-to-date figures are not yet available). High double-digit growth rates were also recorded in exports to the OPEC countries (18 ½ %) and to the other developing countries, notably those in Latin America (26 ½ %). Of the industrial countries, the United States was a particularly successful market for German exporters. This was partly due to the robust growth of the US market and partly to the favourable competitive position of German exporters following the appreciation of the dollar. German industry recorded a rise in turnover in the United States of no less than 26 %. By contrast, the annual result (according to the data already available) for the EU countries, which absorb more than one-half of Germany's exports and are thereby the country's most important market by far, likewise showed a sharp rise, at 8 ½ %, although this rise remained below average. However, sales by German firms in these markets accelerated in the course of the year.

*Breakdown of  
exported goods*

Almost all economic sectors benefited from the heavy demand from abroad. The manufacturers of basic and producer goods as well as of capital goods increased their export turnover (according to the figures available up to November) by approximately 12 %. Motor manufacturers were the most successful branch of the capital goods industry. Their exports during the first 11 months rose by 14 ½ % compared with the corresponding period in 1996. By contrast, the 6 ½ % growth in exports achieved by German

### Regional breakdown of foreign trade

January-November 1997

Group of countries/ Country	Exports		Imports	
	DM billion	Change from the pre- vious year in %	DM billion	Change from the pre- vious year in %
Industrial countries	608.1	10.1	520.6	7.4
EU countries	449.6	8.4	374.2	5.7
of which				
Austria	42.3	1.0	25.4	1.9
Belgium/ Luxembourg	47.3	4.1	42.4	5.6
France	86.5	8.3	72.9	7.8
Italy	59.1	8.3	54.1	1.5
Netherlands	56.9	3.0	58.6	6.4
Spain	30.3	15.4	22.9	11.3
United Kingdom	68.8	18.0	47.7	11.0
Other industrial countries	158.5	15.4	146.4	12.1
of which				
United States	69.7	26.1	53.7	18.0
Japan	18.9	- 3.5	33.6	5.8
Countries in transition	93.2	23.5	88.2	20.1
of which				
Countries in central and eastern Europe	81.8	27.7	67.7	20.1
China	9.6	- 2.2	19.7	18.5
Developing countries	105.9	13.5	81.3	11.9
of which				
OPEC countries	18.0	18.5	12.8	12.8
Emerging markets in South-East Asia	44.4	9.5	36.6	10.9
All countries <sup>1</sup>	809.9	12.0	700.5	10.9

<sup>1</sup> Totals here include figures which are not yet available in a regionally disaggregated form for 1997.

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manufacturers of mechanical engineering products was below average. Although they account for only a comparatively small percentage of German exports, the consumer goods sectors had to make do with relatively modest increases in export sales.

*Imports*

The rise in imports was almost on a par with the sharp growth in exports. In terms of value, at any rate, the growth in imports – at approximately 11% – was almost as rapid. However, import prices – which went up by just over 3% – rose twice as fast as export prices on a year-on-year comparison, with the result that the increase in imported goods, at 7½% in real terms, was much less steep than the rise in exports; however, the rise in imports was still remarkably strong compared with the moderate growth in real domestic demand.

*Imports broken down by category of goods and by region*

The fact that the growth in imports was concentrated mainly on semi-finished goods which are required as intermediate goods in the production process is consistent with the picture of greater dependence on exports. The rise in value of semi-manufactured goods amounted to 16½% from January to November 1997 compared with the corresponding period a year earlier. By contrast, total imports of finished goods rose by no more than 6½% notwithstanding the heavy demand for some categories of goods, notably data processing equipment and road vehicles. The fact that the increase in imports of raw materials (including energy) was below average, at 7%, is somewhat surprising, especially as the value of imports in this area was probably greatly distorted by the effects of the sharp

**Breakdown of foreign trade by category of goods**

in %; January – November 1997

Item	Change from previous year	Share of total exports or total imports
<b>Exports</b>		
Basic and producer goods <sup>1</sup>	12.4	23.2
of which		
Chemical products	12.5	13.2
Capital goods	12.0	56.4
of which		
Mechanical engineering products	6.5	14.7
Road vehicles	14.3	17.8
Electrical engineering products	11.7	13.1
Data processing equipment <sup>2</sup>	14.0	2.2
Consumer goods	7.1	10.6
Food, drink and tobacco <sup>3</sup>	1.5	5.0
<b>Total <sup>4</sup></b>	<b>12.0</b>	<b>100</b>
<b>Imports</b>		
Sources of energy	11.9	7.7
Basic and producer goods <sup>5</sup>		
(excluding sources of energy)	8.3	19.7
of which		
Chemical products	9.1	9.2
Capital goods	7.9	40.0
of which		
Mechanical engineering products	2.7	5.6
Road vehicles	8.0	10.8
Electrical engineering products	5.9	11.4
Data processing equipment <sup>2</sup>	8.9	4.3
Consumer goods	2.8	14.9
Food, drink and tobacco <sup>3</sup>	1.2	10.0
<b>Total <sup>4</sup></b>	<b>10.9</b>	<b>100</b>

<sup>1</sup> Including mining and energy. — <sup>2</sup> Including office machines. — <sup>3</sup> Including agricultural products. — <sup>4</sup> Including estimates not broken down by category of goods. — <sup>5</sup> Including mining.

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rises in the prices of energy and other raw materials in 1996 and at the beginning of 1997. Data on the volumes of raw materials imported are available only in the case of crude oil. In real terms imports of crude oil declined slightly last year although this could have been partly due to the existence of substantial stocks.

Despite this, the value of imports from the OPEC countries actually rose at an above-average rate (just under 13%), but this was due mainly to oil price increases, a trend which continued well into the spring of 1997. Much the same is true of imports from the countries in transition in central and eastern Europe. With a growth rate of 20% these imports rose even faster than those from the OPEC countries, but in the former case the proportion of energy involved was probably considerably lower. However, the increases in turnover which some industrial countries recorded in their trade with Germany were also remarkably strong. Imports from the United States alone grew by 18% last year compared with 1996 although, of course, the exchange-rate-related rise in prices probably contributed considerably to this increase. At all events, the average rate of the dollar in 1997 was 15% above its corresponding value in 1996. Seen in this light, the rise in the value of German imports from other EU countries was not inconsiderable, at just over 5½%, especially as hardly any exchange-rate-related distortions were involved, except in the case of the United Kingdom. This means that, in real terms, Germany's import requirements probably exerted quite a strong stimulus on the economic development of

European partner countries – an effect which reflects the growing integration of European production and the greater exchange of industrial goods that inevitably arises from this.

The fact that the German current account ran a slight deficit again in 1997 despite the large surplus on traded goods was largely due to the deficits in the area of invisible current transactions with non-residents, which comprise cross-border services, factor income and current transfers. The net negative balance on these items rose by a further DM 2 billion to DM 117 billion. The sharpest rise was recorded in the deficit on services account whereas (net) investment income payments to non-residents declined.

*Invisibles*

The traditionally large deficit on Germany's services account increased again last year – by just under DM 4 billion to DM 56½ billion – following a period of pronounced stability during the previous few years. However, it was not the structural deficit on foreign travel, which accounts for the bulk of the deficit on Germany's services account, that was the deciding factor in this renewed deterioration. Instead, it was greater expenditure on the other services that largely contributed to the rise. The deficit on other services increased from just over DM 2 billion in 1996 to almost DM 5 billion in 1997. The services involved were as varied as transport and financial services, building services of foreign firms in Germany, and patents and licences.

*Services*

By contrast, foreign travel, whose persistently rising deficits had impaired the performance of the German services account until two

*Foreign travel*

## Current account

DM billion

Item	1995	1996	1997
1. Foreign trade			
Exports (f.o.b.)	749.5	788.9	887.3
Imports (c.i.f.)	664.2	690.4	765.5
Balance	+ 85.3	+ 98.5	+ 121.7
2. Services (balance)	- 52.5	- 52.5	- 56.3
of which			
Foreign travel (balance)	- 49.1	- 50.3	- 51.5
3. Factor income (balance)	- 1.8	- 7.7	- 4.2
of which			
Investment income (balance)	- 0.4	- 5.9	- 2.4
4. Current transfers (balance)	- 58.7	- 54.8	- 56.4
Balance on current account 1	- 32.4	- 20.7	- 1.7

1 Includes supplementary trade items.

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years ago, ran a deficit, which, at DM 51½ billion, was little more than DM 1 billion up on the 1996 figure. This means that in real terms the (net) expenditure of German tourists and business travellers was actually lower than in the previous year. Owing to the appreciation of currencies in major countries of destination, it would appear that, at least in some cases, foreign travel became considerably more expensive. This is particularly true in the case of the United States and other non-European destinations. While (nominal) expenditure rose sharply here, it probably declined in real terms. The greater spending restraint in respect of foreign travel is more clearly illustrated in the lower expenditure by German tourists in the "classical" European holiday countries, such as Austria, Italy and

Spain, which were not affected by such exchange rate factors.

Net investment income payments made to non-residents declined last year from DM 7½ billion (1996) to just over DM 4 billion (including income from employment). For one thing, German investment income receipts rose far more sharply than the corresponding expenditure because the appreciation of the dollar had a positive impact on net German interest income in Deutsche Mark terms. The reason is that a relatively large proportion of Germany's external assets are denominated in dollars whereas the dollar plays a less significant role on the liabilities side of Germany's external assets and liabilities position.<sup>1</sup> For another thing, Germany's net receipts from direct investment rose (by DM 5½ billion to just over DM 13 billion).

*Investment  
income account*

Germany's large net transfer payments to non-residents account for almost one-half of the total deficit on invisibles. Current transfers to non-residents amounted to DM 56½ billion net last year. Although that was "only" DM 1½ billion more than in 1996, it means that Germany, in terms of its GDP, makes more unrequited payments to non-residents than any other industrial country. Germany's regular net contributions to the EU (DM 28 billion) account for approximately one-half of these payments. After taking account of payments received from the EU's regional and agricultural funds, which benefited eastern Germany in the main and which are recorded under capital transfers in the balance of pay-

*Current  
transfers*

<sup>1</sup> See also the article on the German external assets position on page 79ff. of this Report.

## Major items of the balance of payments

DM billion			
Item	1995	1996	1997
<b>I. Current account</b>			
1. Foreign trade			
Exports (f.o.b.)	749.5	788.9	887.3
Imports (c.i.f.)	664.2	690.4	765.5
Balance	+ 85.3	+ 98.5	+ 121.7
2. Balance of invisibles	- 113.0	- 115.0	- 116.9
Balance on current account <sup>1</sup>	- 32.4	- 20.7	- 1.7
<b>II. Balance of capital transfers</b>	- 0.9	- 0.0	+ 3.6
<b>III. Financial account <sup>2</sup></b>			
Direct investment	- 36.3	- 48.6	- 57.8
Portfolio investment <sup>3</sup>	+ 52.0	+ 86.7	- 10.6
German investment abroad	- 32.6	- 54.0	- 161.3
Foreign investment in Germany	+ 84.6	+ 140.8	+ 150.7
Credit transactions <sup>3, 4</sup>	+ 56.6	- 10.1	+ 55.9
Overall balance on financial account	+ 72.3	+ 28.1	- 12.6
<b>IV. Balance of unclassifiable transactions</b>	- 21.3	- 8.9	+ 2.3
<b>V. Change in the Bundesbank's net external assets at transaction values (increase: +) <sup>5</sup></b> (I plus II plus III plus IV)	+ 17.8	- 1.6	- 8.5

<sup>1</sup> Includes supplementary trade items. — <sup>2</sup> Net capital exports: -. — <sup>3</sup> Excluding direct investment. — <sup>4</sup> Including other public and private investment. — <sup>5</sup> Excluding allocation of SDRs and changes due to value adjustments.

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ments, Germany's net contributions to the EC budget came to DM 22 ½ billion last year.

Another important factor as far as its magnitude is concerned is the remittances of foreign workers in Germany to their home countries. These remittances amounted to approximately DM 7 ½ billion in 1997. A further total of just under DM 13 ½ billion net was transferred to other countries in the form of pensions and other maintenance payments to non-residents or to Germans living abroad. Payments of just over DM 3 billion were made under the government development aid scheme.

## Financial account

International financial transactions, which were long regarded as the "financial mirror image" of the balances in cross-border current transactions, have had their own determinants for some time now. This is a result of their extensive liberalisation in the industrial countries and, as globalisation increases, of the innovations in the exchange of information worldwide. Forecasts of the development prospects of major economic regions play a key role in this. Last year international capital flows were initially stimulated, among other things, by arbitrage transactions in view of the approaching European monetary union. The financial market crises in East Asia came to the fore in the second half of 1997; the renewed preference for quality paper had a dampening effect on financial transactions in certain areas. From the German standpoint there was a discernible increase in cross-

*Trends in  
financial  
transactions*

border portfolio investment in both directions in 1997. This increase occurred against a backdrop of generally favourable trends in the equity and bond markets, and the investment was many times greater than the corresponding balances of the financial transactions. In the end portfolio investment ran a deficit of DM 10½ billion in 1997 compared with net capital inflows of DM 86½ billion a year earlier. The substantial deficit on direct investment of the previous year was again exceeded, and in non-banks' credit transactions with non-residents there was likewise an outflow of funds in 1997. The net capital exports in these segments of the financial account and the deficit on current transactions were accompanied by large capital inflows through the external business of the banks. The net external assets of the Bundesbank declined discernibly, too.

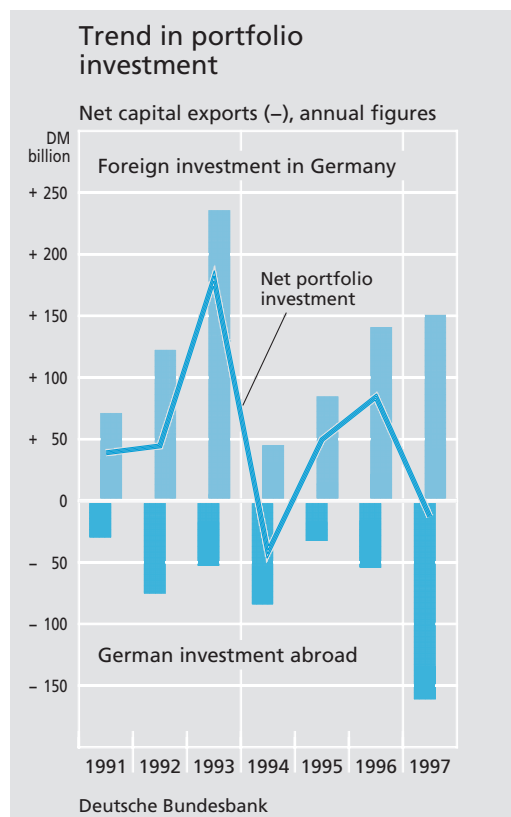
*Portfolio transactions*

The striking turnaround of almost DM 100 billion in portfolio transactions was mainly due to the behaviour of German investors. Despite the heightened risk-awareness of late, probably due in part to the crises in the East Asian countries, German residents tripled their investment in foreign securities over that of the previous year, with record purchases of DM 161½ billion.

*German investment in foreign ...*

*... bonds and notes*

Interest in foreign bonds and notes rose particularly sharply; compared with DM 22 billion in 1996, DM 77 billion was exported in this way last year. DM 64½ billion of this was invested in foreign currency bonds issued abroad (1996: DM 14½ billion). In view of the comparatively low "domestic" interest rate level, the search for more attractive



yields may have contributed to these substantial outflows. However, it was above all the widely expected convergence of interest rates – an expectation that was fulfilled in the course of the year – in the run-up to European monetary union which awakened the prospect of significant capital gains in various European bond markets in the minds of German investors. The significance of "convergence trading" in the annual data for 1997 can be seen from the currency breakdown of the foreign bonds purchased by German residents. Lira-denominated paper alone accounted for DM 26 billion of the purchases of bonds and notes. The interest rate differential between this paper and German paper declined at the long end of the market from 1½ percentage points to ½ percentage point in 1997. The popularity of the Italian currency



with German investors was on a par with that of the dollar (DM 26 billion) and ahead of the yen (DM 6 billion). The outflows of funds into the dollar area may have been stimulated – in addition to the remaining interest rate differentials – by expectations of making exchange rate gains from the US currency. German demand for Deutsche Mark paper issued abroad was appreciably lower than that for foreign currency bonds. Nevertheless, at DM 12 ½ billion, more funds flowed into this paper, which usually has an interest advantage over German bonds, than in 1996 (DM 7 ½ billion).

... money  
market paper

Sales of foreign money market paper in Germany likewise grew strongly (DM 6 ½ billion). The share of paper denominated in Deutsche Mark amounted to approximately one-quarter of this; here, too, German investors apparently preferred paper denominated in foreign currency.

... equities

German investors showed a lively interest in equities last year, purchasing foreign shares worth DM 52 ½ billion net. This was more than twice the figure recorded in 1996 (DM 21 ½ billion) when investment in foreign equities had likewise increased discernibly. There is no doubt that the macroeconomic environment, with low long-term interest rates and moderate inflation rates, created a favourable climate for investment in equities, especially as the prospects for the world economy – at least until the outbreak of the crises in East Asia – were fairly good. It is likely, however, that a large proportion of the foreign equities were acquired not by domestic savers direct but by German investment funds, which

## Financial transactions

DM billion, net capital exports: –

Item	1995	1996	1997
<b>1. Direct investment</b>	– 36.3	– 48.6	– 57.8
German investment abroad	– 55.6	– 44.5	– 57.5
Foreign investment in Germany	+ 19.3	– 4.1	– 0.3
<b>2. Portfolio investment</b>	+ 52.0	+ 86.7	– 10.6
German investment abroad	– 32.6	– 54.0	– 161.3
Equities	+ 1.7	– 21.3	– 52.3
Investment fund certificates	– 1.2	– 3.2	– 14.3
Bonds and notes	– 24.1	– 21.9	– 77.0
Money market paper	– 2.0	– 1.2	– 6.3
Financial derivatives <sup>1</sup>	– 7.0	– 6.4	– 11.4
Foreign investment in Germany	+ 84.6	+ 140.8	+ 150.7
Equities	– 1.7	+ 22.5	+ 27.2
Investment fund certificates	– 1.0	– 2.3	– 4.2
Bonds and notes	+ 86.0	+ 102.4	+ 121.8
Money market paper	– 4.1	+ 18.5	+ 10.5
Warrants	+ 5.5	– 0.3	– 4.6
<b>3. Credit transactions</b>	+ 61.7	– 6.1	+ 60.2
Credit institutions	+ 42.4	– 5.0	+ 63.4
Long-term	+ 38.9	+ 23.1	– 4.4
Short-term	+ 3.6	– 28.2	+ 67.8
Enterprises and individuals	+ 23.5	– 5.9	+ 13.5
Long-term	– 2.3	– 2.5	+ 1.8
Short-term	+ 25.8	– 3.4	+ 11.7
Public authorities	– 4.2	+ 4.9	– 16.7
Long-term	– 0.0	+ 0.8	– 10.6
Short-term	– 4.1	+ 4.0	– 6.2
<b>4. Other investment</b>	– 5.1	– 4.0	– 4.3
<b>5. Balance of all statistically recorded capital flows</b>	+ 72.3	+ 28.1	– 12.6
Memo item			
Change in the Bundesbank's net external assets at transaction values (increase: +) <sup>2</sup>	+ 17.8	– 1.6	– 8.5

<sup>1</sup> Securitised and unsecuritised options as well as financial futures contracts. — <sup>2</sup> Excluding allocation of SDRs and changes due to value adjustments.

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recorded substantial influxes of resources last year.

... investment  
fund  
certificates

The trend towards increased saving through investment funds can also be seen in the somewhat greater demand for foreign investment fund certificates. German residents invested DM 14½ billion in these certificates, which was DM 11 billion more than in 1996. Nevertheless, this form of investment did not regain the significance which it enjoyed for a time when the tax on interest income was introduced. The adjustments which have since taken place in tax legislation also make this unlikely.

Foreign  
investment  
in German ...

Non-residents likewise increased their investment in German securities in 1997 after already investing relatively heavily in the German market in 1996. However, the increase was not as great as the rise in the purchases of foreign paper by German investors. A total of DM 150½ billion flowed into the German capital market through foreign investment compared with DM 141 billion in 1996. That is the second-largest amount after the record year of 1993. Both the German equity market and the bond market benefited from the greater interest of non-residents. As usual, however, the lion's share of foreign investment flowed into bonds and notes (DM 122 billion), notably public sector bonds (DM 78 billion). With a share of more than one-third, the two-year Federal Treasury notes (*Schätze*) which the Federal Government has been issuing since September 1996 have now become firmly established in the portfolios of foreign investors. In contrast to issues of paper with longer maturities, such as special five-year

... bonds  
and notes

Federal bonds (*Bobls*) and Federal bonds (*Bunds*), new issues of the two-year Federal Treasury notes are usually placed, to a very large extent, with foreign investors.

By contrast, private sector bonds lost ground in 1997 compared with public sector bonds. After investing DM 58½ billion in German bank bonds in 1996, non-residents acquired such issues to the value of no more than DM 44 billion net in 1997. At DM 39½ billion, foreign currency bonds, which in the main were probably issued with special investor groups abroad in mind, predominated in this sector. German dollar-denominated paper was particularly in demand, accounting for approximately one-third of the foreign currency bonds originating in Germany and purchased by non-residents (DM 13½ billion). Somewhat smaller sums were invested in paper denominated in French francs (DM 4 billion), in Italian lire (DM 3½ billion), the pound sterling (DM 3½ billion), the Swiss franc (DM 3½ billion) and the yen (DM 3 billion). On the other hand, trade with non-residents in mortgage bonds (*Pfandbriefe*) denominated in Deutsche Mark contracted last year although they had been comparatively popular with foreign investors in 1996.

Foreign demand for German equities also

... equities

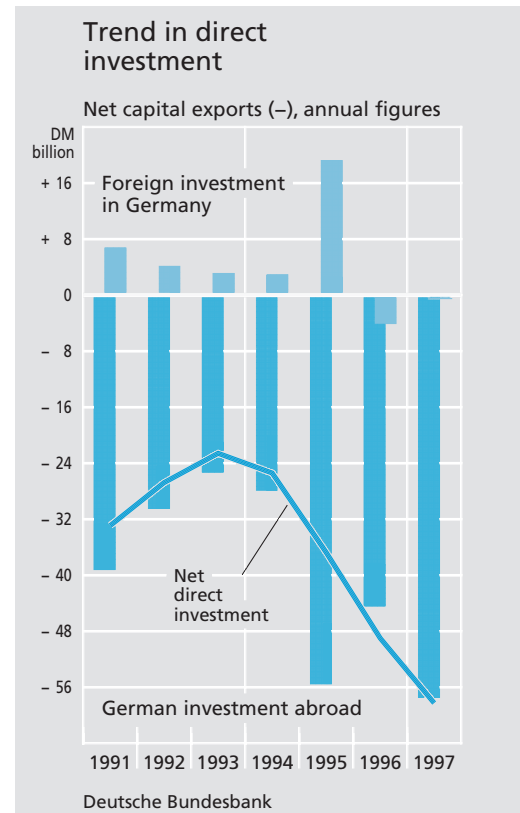
and summer when the profitability of German enterprises was being regarded in a particularly favourable light owing to the discernible improvement on the economic front. It was not least the uncertainty engendered by the crises in East Asia that probably led subsequently to a temporary change of mood among foreign investors and therefore to net sales of German equities.

*... investment  
fund certificates  
and money  
market paper*

Much the same is true of German investment fund certificates throughout 1997; foreign investors sold them on balance in the amount of DM 4 billion. Demand for German money market paper was likewise weaker (at DM 10 ½ billion) than in 1996. However, the market for this paper was fairly restricted while the total amount of public sector paper in circulation actually declined somewhat. Previously, foreign central banks in particular had shown considerable interest in it.

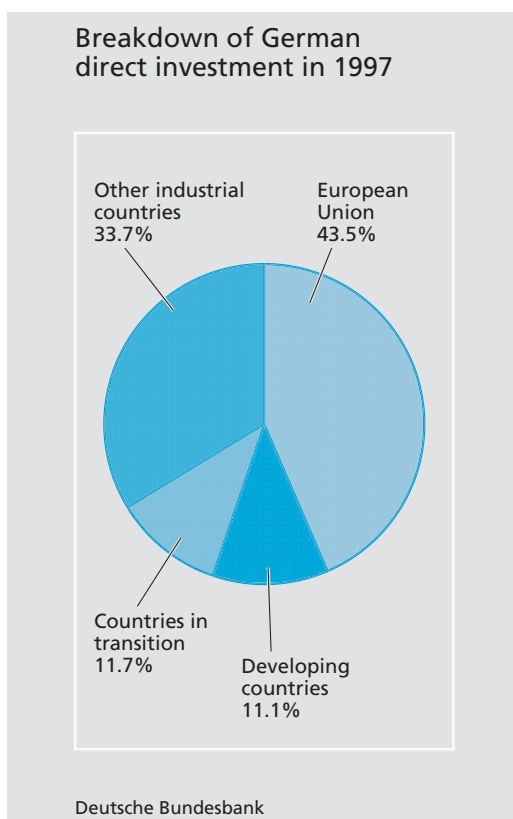
*Direct  
investment*

Substantial amounts of capital were again exported through direct investment in 1997. According to the German balance of payments statistics, German enterprises increased their foreign investment by DM 57 ½ billion compared with DM 44 ½ billion in 1996. This means that the 1995 record was broken. Experience has shown that trends in direct investment abroad are pro-cyclical. In other words, they move in line with the growth in major export markets and reflect the economic state and liquidity position of domestic enterprises. To that extent, the recent rise in German acquisitions of participating interests abroad is not surprising – quite apart from the frequently cited “wave of globalisation”.



The regional breakdown of German direct investment in 1997 basically confirms these considerations. Owing to the continued robustness of its economic growth, the United States, for example, increased its share of German outward investment, as it had done in 1996. Last year the United States accounted for just under one-quarter of Germany's acquisition of participating interests abroad. Investment in other industrial countries outside the EU also increased relatively sharply. By contrast, there was a decline in the share of outward investment in other EU countries although these countries still absorbed the bulk of this investment, accounting in total for more than 43%. Possibly as a result of the firmness of the pound, a downturn was discernible in German investors' interest in the United Kingdom, in particular.

*Regional  
breakdown of  
German direct  
investment*



Investment by German firms in the countries in transition likewise declined slightly compared with 1996 (share: 12 %); this may have been associated with the smaller number of major privatisations, which had previously had a marked effect on the figures relating to individual countries. On the other hand, German firms again invested somewhat more in the developing countries in 1997 (share: 11%).

*Foreign direct investment in Germany*

Compared with German investors and their direct investment abroad, foreign entrepreneurs continued to show very little inclination to invest in Germany. Although a limited amount of investment funds did flow into their subsidiaries domiciled in Germany, this was more than offset, as in 1996, by substantial profit distributions to the foreign owners,

a factor that was reflected in the negative balance on reinvested profits. Consequently, there were net outflows of funds amounting to DM ½ billion although actually a more positive result would have been expected given the cyclical and exchange rate trends. This, together with the generally modest level of investment in Germany, could be a sign of structural impediments to entrepreneurial activity in Germany.<sup>2</sup>

In addition to the capital exports through portfolio transactions and direct investment, there were also net outflows (of DM 3 billion) as a result of the non-securitized credit transactions of non-banks. The credit transactions of public authorities, which made large redemption payments on loans previously raised abroad, were the main reason for this. Net capital exports totalling DM 16 ½ billion through public sector operations were offset by inflows (of DM 13 ½ billion) in the case of enterprises and individuals. Part of this was attributable to the further reduction of Euro-deposits; intergroup liquidity management operations in multinational concerns did not play the same major role on the whole as they had done in 1996.

*Credit transactions of non-banks*

There were movements in both directions in the non-securitized credit transactions of domestic banks in 1997. On the one hand, out-

*Credit transactions of credit institutions*

<sup>2</sup> However, surveys have also shown that in the past the inward direct investment flows recorded in the German balance of payments have been significantly below the corresponding outward direct investment figures quoted by the countries of origin. See Deutsche Bundesbank, Problems of international comparisons of direct investment flows, Monthly Report, May 1997, page 77 ff. and Deutsche Bundesbank, Development and determinants of international direct investment, Monthly Report, August 1997, page 63 ff.

flows of funds (DM 4 ½ billion) predominated in the banks' long-term credit operations whereas in 1996 they had received DM 23 billion net in long-term credit. The reason for the about-turn was the exceptionally large loans granted by German issuing institutions to non-residents, a large part of which was probably connected with the substantial sales of foreign currency bonds by these institutions, mentioned above. Another part was probably refinanced, as usual, through the raising of long-term loans from foreign business partners – especially the foreign financing subsidiaries of German credit institutions.

On the other hand, and in contrast to the deficits mentioned in the other sectors of the financial and current account, there were considerable inflows of funds (DM 68 billion) through the short-term financial transactions of the credit institutions. In 1996, by contrast, short-term funds amounting to DM 28 billion had been exported. As a result, the non-securitised net external assets of the credit institutions declined by DM 63 ½ billion in 1997.

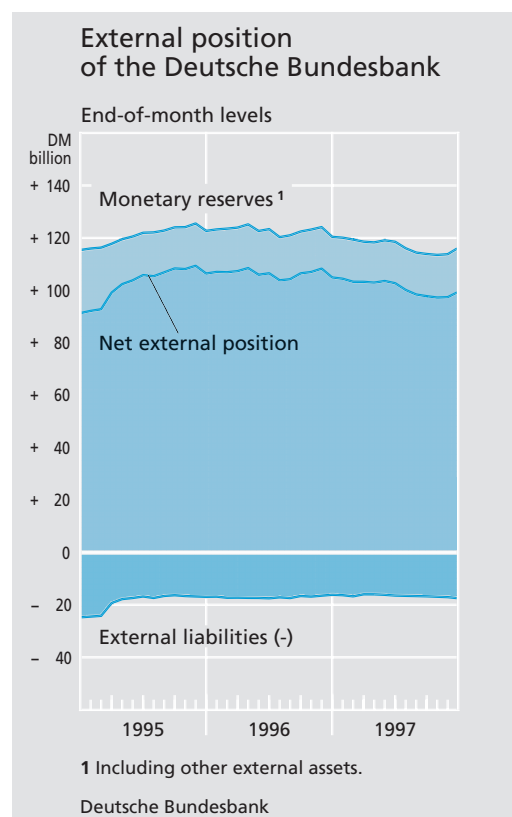
### External position of the Bundesbank

*Net external assets of the Bundesbank decline*

The net external assets of the Bundesbank also declined last year. At transaction values, net external assets fell by DM 8 ½ billion compared with a decline of DM 1 ½ billion in 1996.

*External assets*

The primary reason for the decline was the fall of just over DM 7 billion in external assets.



For example, the Bundesbank channelled foreign exchange assets that it had previously acquired in the course of commercial transactions back into the market. There was a corresponding decline in the Bundesbank's claims in respect of the reserves which it had transferred to the European Monetary Institute, which are linked to the gold and dollar reserves. By contrast, the reserve position in special drawing rights at the International Monetary Fund (including special drawing rights allocated) increased; a contributory factor here was the Bundesbank's participation in the IMF's aid programme for the countries in crisis in Asia although in the end this resulted only in shifts between the various asset items.

*External  
liabilities*

In contrast to its external assets the Bundesbank's liabilities stemming from external operations rose by approximately DM 1½ billion last year. The external liabilities largely consist of balances of foreign central banks and international organisations at the Bundesbank.

*External  
position at  
balance sheet  
rates*

At the end of 1997 the external assets calculated at balance sheet rates amounted to just under DM 117 billion; the external liabilities

amounted to DM 17 billion. In contrast to customary practice, no revaluation of US dollar holdings and ECU balances was undertaken at the end of 1997. The planned change to the valuation of foreign exchange reserves at rates closer to those obtaining in the markets will not be reflected in the balance sheet figures until the annual accounts for 1997 have been drawn up.