Foreign trade and payments

Foreign trade and current account

Export trends

Since the beginning of this year the gradual return of a more favourable world economic climate has had a positive impact on Germany's export markets. The fairly pronounced weakness in foreign demand until the turn of the year and German entrepreneurs' consequent pessimism about future export prospects have now been replaced by an improvement in exporters' order books and in their assessment of future business trends. For example, the orders received by German industry from abroad rose by 4½% between the first and second quarters of 1999 after stagnating in the period before. Since the early summer the majority of enterprises surveyed by the ifo Institute have once again become positive in their expectations about export trends.

Exports

It is true that the upturn in export business has not been fully seen in export deliveries, which generally take a certain length of time before they reflect the trend in orders. Nevertheless, German exports grew by a further 3% in the second quarter, both in value and in real terms, compared with only a slight rise of approximately 1% in the first quarter over the previous quarter. However, this means that real exports were still slightly below their level in the corresponding period last year.

Regional breakdown

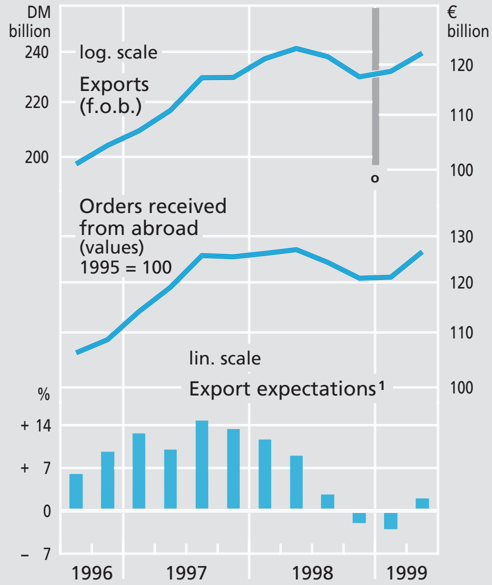
As already mentioned, the more buoyant export business in the course of the year so far is primarily the result of the more favourable world economic environment, which has been reflected in a correspondingly faster rate of market growth. This is particularly true of German exports to countries outside EMU, especially as in these countries suppliers from within EMU also enjoyed the exchange-rate-related competitive advantages provided by the weakness of the euro.

This is especially evident in the export success of German enterprises in the US market; deliveries to the United States were almost 6 % greater in the first five months of this year than in the previous five-month period (August-December 1998). Sharp increases in sales were also recorded in Asian export markets after the general situation there had largely stabilised and the economies of some of these countries had begun to grow again. German exports to the emerging markets in South-East Asia alone, where the largest losses in export business had been sustained, rose by 6½ %. German exporters recorded double-digit growth rates in their trade with Japan (14 %) and China (19 %). Taken together, these two countries are more or less as important for German export business as the group of emerging markets in South-East Asia.

By contrast, there were initially no particularly dynamic stimuli from trade with Germany's partner countries in the European Union and in the euro area. A certain revival did not emerge here until recently. Sales of German products were particularly sluggish in the countries in transition in central and eastern Europe where demand had been increasing particularly fast for quite some time. The difficult problems confronting Russia and the effects of these on Russia's east European neighbours probably had as much to do with

Export trend

Seasonally adjusted, quarterly



1 Values are taken from the ifo business survey. Balances are from positive and negative company reports. — o From 1999 on all data in euro.

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this as the crisis in Kosovo and the consequent detrimental impact on the neighbouring Balkan countries.

Import trends

The revival in exports was paralleled by a sharp increase in imports of goods since the beginning of the year. In terms of value, imports in the second quarter exceeded their level in the previous quarter by a seasonally adjusted 5 %. However, price increases in connection with the rise in the cost of energy imports and the depreciation of the euro accounted for part of the nominal growth in turnover. The upshot was a rise of just under 2 %, seasonally adjusted, in import prices in the second quarter of the year compared with the previous quarter. This means, however, that at approximately 3 % in real terms the increase in imported goods was similar to

Regional breakdown of foreign trade

January–May 1999, seasonally adjusted

Group of countries/ Country	Exports € billion	Exports Change from Aug. – Dec. 1998 in %	Imports € billion	Imports Change from Aug. – Dec. 1998 in %
Industrial countries	154.3	+ 1.1	130.4	+ 0.0
EU countries	114.0	+ 0.5	93.2	– 0.8
EMU countries	86.9	+ 0.2	74.7	– 1.0
Austria	10.6	– 1.9	7.1	+ 1.3
Belgium/ Luxembourg	11.0	– 4.7	8.8	– 10.8
Finland	2.2	+ 5.8	1.9	+ 7.3
France	19.6	+ 0.2	17.2	– 0.8
Ireland	1.2	+ 13.1	3.4	+ 69.7
Italy	15.0	+ 2.6	13.3	– 2.8
Netherlands	13.1	– 3.0	13.6	– 1.4
Portugal	2.2	– 1.8	1.9	– 2.1
Spain	8.6	+ 2.5	5.9	+ 0.9
Other EU countries				
Denmark	3.4	– 1.4	2.7	+ 3.4
Greece	1.5	– 1.4	0.7	– 1.5
Sweden	4.6	+ 2.7	3.3	– 0.3
United Kingdom	17.0	– 1.3	11.4	– 4.7
Other industrial countries				
of which				
United States	19.8	+ 5.8	14.7	+ 1.2
Japan	4.2	+ 13.9	8.7	+ 3.5
Countries in transition	22.5	– 2.6	24.0	+ 2.0
of which				
Countries in central and eastern Europe	19.4	– 4.4	18.8	+ 3.2
China 2	2.9	+ 19.2	5.1	+ 4.9
Developing countries	22.3	– 1.6	18.6	+ 0.8
of which				
OPEC countries	3.8	– 5.5	2.2	– 3.5
Emerging markets in South-East Asia	7.4	+ 6.3	8.6	+ 0.6
All countries 1	200.2	+ 0.7	174.1	+ 0.4

1 The totals include revisions which are not yet available in a regional breakdown. — **2** Excluding Hong Kong.

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the increase in exports. As a result of the high degree of corporate integration in European industry, the more favourable export performance in conjunction with greater domestic demand is leading more or less directly to increased imports not only of raw materials but also of semi-finished and finished products which are then used as inputs in the manufacturing process.

Breakdown of imports

Imports have grown correspondingly sharply recently, especially from other EMU countries and from the EU in general. If the first five months of the year are taken together, however, this trend is hardly detectable. According to the figures thereby obtained, the imports arising in trade with non-European industrial countries, notably Japan and the United States, rose at above-average rates. Imports by German firms from trading partners in the countries in transition and in the emerging markets in South-East Asia were also relatively buoyant. By contrast, the value of imports from the OPEC countries declined slightly, despite the increases in the price of petroleum since about the beginning of this year. A year earlier the rapid fall in the price of oil had led to an unusually sharp rise in imports and in stocks.

Trade balance

Owing to the relatively rapid growth in imports, the value of Germany's trade surplus, despite the increase in exports, was somewhat lower in the second quarter than in the first quarter of the year. In seasonally adjusted terms it amounted to € 15 ½ billion compared with € 17 billion in the first three months of the year.

Current account

By contrast, the invisible current transactions with non-residents, which generally show a considerable deficit, ran a smaller deficit in the second quarter of this year than in the previous quarter. In seasonally adjusted terms the deficit fell by € 3½ billion to just over € 15 billion. If the supplementary trade items are included, the seasonally adjusted current account had a slight deficit overall of € ½ billion in the period under review compared with one of over € 2 billion in the first quarter. The main reason for the improvement in the case of invisibles was an increase in investment income, which is recorded in the sub-account Factor income. The net income received from non-residents for direct investment was greater in the second quarter than previously. The rise in the dollar exchange rate could also have played a part here. The appreciation in the dollar meant that German investment income denominated in the US currency was worth appreciably more after conversion into euro.

Current account

€ billion; seasonally adjusted

Item	1998	1999	
	4th qtr	1st qtr	2nd qtr
1. Foreign trade			
Exports (f.o.b.)	118.1	119.2	123.1
Imports (c.i.f.)	103.3	102.3	107.5
Balance	14.8	17.0	15.6
2. Services (balance)	– 8.4	– 9.2	– 9.3
Receipts	18.5	18.0	19.2
Expenditure	26.9	27.2	28.5
of which Foreign travel (balance)	– 7.2	– 7.3	– 7.6
3. Factor income (balance)	– 3.0	– 3.8	– 0.1
Receipts	17.0	16.9	22.9
Expenditure	20.0	20.7	23.0
of which Investment income (balance)	– 2.8	– 3.6	0.2
4. Current transfers (balance)	– 7.2	– 5.6	– 5.7
By foreigners to Germany	3.4	3.5	4.2
By German residents to other countries	10.5	9.1	10.0
Balance on current account 1	– 3.7	– 2.2	– 0.4

1 Includes supplementary trade items.

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Financial transactions

Portfolio trends

The trend in financial operations with non-residents continued to be influenced in the second quarter of 1999 by the advancing integration of the capital markets in the euro area. However, the shifts in the interest rate differentials and exchange rates which have been under way between the large currency blocs since the beginning of this year and the recent improvement in the cyclical prospects for Germany have left their mark. The large capital exports which were observed in portfolio transactions at the beginning of the year became less significant again during the period under review. The foreign currency investments of German residents in foreign bond markets probably came off worst in view of the ever increasing currency risks assessed while the integration of the capital markets with the euro area advanced further. In the process considerable amounts of foreign capital flowed on to the German share market during the period under review. The net inflows in securities transactions as a whole amounted to € 3 billion in the second quarter compared with net capital outflows of € 38 billion in the three months earlier.

Foreign investment in German ...

It was particularly the renewed interest of non-residents in German securities that contributed to the swing. A total of € 45 billion in foreign funds accrued to the German mar-

Major items of the balance of payments

€ billion

Item	1998 2nd qtr	1999 1st qtr	1999 2nd qtr
I. Current account			
1. Foreign trade			
Exports (f.o.b.)	124.7	117.5	124.9
Imports (c.i.f.)	107.4	101.7	108.7
Balance	+ 17.3	+ 15.9	+ 16.2
2. Services (balance)	– 7.8	– 8.4	– 9.1
3. Factor income (balance)	– 2.0	– 4.5	+ 0.4
4. Current transfers (balance)	– 4.8	– 5.5	– 5.3
Balance on current account 1	+ 2.0	– 3.0	+ 1.5
II. Balance of capital transfers	– 0.1	+ 0.2	– 0.1
III. Financial account 2			
Direct investment	– 2.6	– 37.8	+ 3.2
Portfolio investment	– 39.8	– 58.3	– 41.6
German investment abroad	+ 37.2	+ 20.6	+ 44.8
Foreign investment in Germany	– 3.8	+ 1.5	– 0.1
Financial derivatives	– 2.2	– 2.2	+ 1.1
Credit transactions 3	+ 14.2	+ 4.2	+ 23.5
Overall balance on financial account	+ 2.3	– 42.7	+ 14.2
IV. Change in the monetary reserves at transaction values (increase: –) 4	– 1.1	+ 13.3	– 0.3
V. Balance of unclassifiable transactions	– 3.1	+ 32.2	– 15.3

1 Includes supplementary trade items. — 2 Net capital exports: –. — 3 Including Bundesbank investment and other public and private investment. — 4 Excluding allocation of SDRs and changes due to value adjustments.

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ket between April and June; this was more than twice as much as in the previous quarter (€ 20½ billion).

... shares

The main reason for this development was the large foreign investment in the German share market. As a result of the improved economic outlook, international investors had evidently also reassessed the potential of German equities and invested more heavily again in Germany. Another factor was that, with the increase in the capitalisation of Deutsche Telekom, an asset which had been highly prized internationally in the past attracted considerable interest. Foreign investors acquired German shares worth a total of € 21½ billion whereas in the previous quarter they had sold shares in German enterprises worth € 15 billion. In comparison with the other countries participating in EMU, Germany therefore appears to have benefited particularly well from the shifts in international portfolios during the quarter under review. Accordingly, the DAX rose by almost 11% in this period whereas the Euro Stoxx 50 index increased by only 6% and the New York stock exchange, as indicated by the Dow Jones index, was able to record no more than a rise of just under 2%. Since then the DAX and the other share indices mentioned have declined significantly again. However, there are still no statistics on the corresponding changes in investor behaviour.

... bonds and notes

In contrast to their demand for shares, foreign investors' demand for German fixed-interest securities was limited. They purchased German bonds and notes worth € 18½ billion net after investing € 32½ billion in the German bond market in the three months earlier. Bank bonds, which at the long end of the market have a somewhat better yield than public bonds, were at the centre of buyers' attention. The funds raised from the international placing of this paper amounted to € 16 billion between April and June although that was still much less than at the beginning of the year (€ 26 billion). Foreign demand for public bonds also weakened further (€ 3 billion). The weighting of these bonds in the portfolios of international investors under the changed circumstances since the introduction of the euro and in the light of the yield differential between them and the public bonds of other EMU countries had apparently been considered to be somewhat too high.

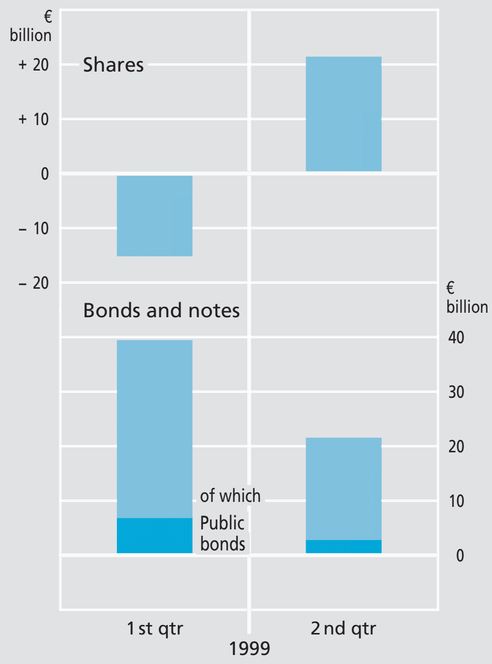
German investment in foreign ...

German investors have been making similar portfolio adjustments since last year. Their total investment in foreign financial centres between April and June amounted to € 41½ billion compared with € 58½ billion in the first three months of the year.

... bonds and notes

At approximately € 29 billion, bonds and notes accounted for the lion's share of German investors' securities purchases abroad in the second quarter of 1999. The paper concerned was exclusively euro-denominated bonds, just over 60 % of which was issued in other EMU countries. This means that the integration of the financial markets advanced further within the single currency area in the sense that public bonds issued by the EMU countries are being regarded as close substitutes for one another. Even slight changes in the interest rate differential between Federal (German) bonds, which are the benchmark for the euro capital market, and the euro bonds of other EMU countries may play a significant role in investors' decisions. From the end of March until the end of the period under review the interest rate spread between long-term Federal (German) bonds and comparable bonds issued by the governments of other EMU countries slightly increased by five basis points to 22. This may be an explanation for the persistently strong preference of German investors for these foreign issues. Foreign currency bonds, by contrast, were returned on balance by German savers. This cutting back is remarkable in that the yield advantages of US and UK bonds during the three months from April to June increased further. It is possible that, following the extent of the euro's depreciation against the other international investment currencies,

Foreign investment in German securities



Financial transactions

€ billion, net capital exports: –

Item	1998 2nd qtr	1999 1st qtr	1999 2nd qtr
1. Direct investment	– 5.5	– 10.7	– 12.3
German investment abroad	– 11.3	– 21.0	– 25.1
Foreign investment in Germany	+ 5.7	+ 10.3	+ 12.8
2. Portfolio investment	– 2.6	– 37.8	+ 3.2
German investment abroad	– 39.8	– 58.3	– 41.6
Shares	– 16.8	– 17.6	– 8.6
Investment fund certificates	– 4.0	– 4.5	– 3.3
Bonds and notes	– 19.0	– 35.7	– 29.2
Money market paper	+ 0.1	– 0.5	– 0.5
Foreign investment in Germany	+ 37.2	+ 20.6	+ 44.8
Shares	+ 25.2	– 15.2	+ 21.4
Investment fund certificates	– 0.6	+ 1.6	– 1.5
Bonds and notes	+ 11.0	+ 32.6	+ 18.7
Money market paper	+ 1.5	+ 1.5	+ 6.1
3. Financial derivatives [1]	– 3.8	+ 1.5	– 0.1
4. Credit transactions	+ 14.9	+ 4.4	+ 23.9
Credit institutions	+ 18.6	+ 21.6	+ 14.2
Long-term	+ 2.5	+ 4.0	– 6.0
Short-term	+ 16.1	+ 17.6	+ 20.1
Enterprises and individuals	– 0.9	+ 13.4	+ 1.6
Long-term	+ 3.0	+ 1.9	– 2.0
Short-term	– 3.9	+ 11.6	+ 3.6
General government	– 2.7	– 1.0	+ 0.5
Long-term	– 0.9	– 2.4	– 1.2
Short-term	– 1.8	+ 1.4	+ 1.7
Bundesbank	– 0.1	– 29.5	+ 7.6
5. Other investment	– 0.7	– 0.2	– 0.4
6. Balance of all statistically recorded capital flows	+ 2.3	– 42.7	+ 14.2
Memo item Change in the monetary reserves at transaction values (increase: –) [2]	– 1.1	+ 13.3	– 0.3

1 Securitised and non-securitised options and financial futures contracts. — **2** Excluding allocation of SDRs and changes due to value adjustments.

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a corresponding increase in the expected currency risks involved curbed any further expansion in foreign currency positions.

... shares

German investor interest in shares of foreign enterprises also declined discernibly in the period under review (€ 8½ billion compared with € 17½ billion in the previous quarter). The observed restraint, which involved the shares of enterprises in other euro countries for the most part, was possibly due to shifts in favour of German equities after the improvement in German enterprises' business prospects in the spring.

Deficit in direct investment

Outside the field of securities, there were net capital exports of € 12½ billion as a result of direct investment. One factor accounting for this result was the acquisition of a foreign financial institution by a German bank, a transaction which was reflected in the balance sheet of German direct investment abroad. Even if this significant transaction is disregarded, however, German firms still continued to increase their foreign investment further. All in all, German direct investment abroad amounted to € 25 billion, and countries outside EMU – notably the United States – were the preferred investment targets. By contrast, the provision of funds by foreign owners for their subsidiaries operating in Germany was relatively small (€ 13 billion). This was essentially in line with the general trend observed in the euro area as a whole. There, too, interest in investment in third countries was decidedly keen in the spring. For example, in April and May – more recent data on the balance of payments for the euro area are not yet available – direct investment accounted for outflows of € 48 billion from the single currency area whereas investors from non-EMU countries spent no more than € 17 billion on direct investment in the single currency area during the same period.

Credit transactions

In the quarter under review there was a slight surplus (of € 2 billion) in the unsecuritised credit transactions between non-residents, on the one hand, and enterprises, individuals and the state, on the other. German non-banks, in particular, reduced slightly further the short-term balances that they held with foreign banks and that they had already reduced significantly in the run-up to monetary union.

Banks' external position still in deficit

The changes in the net external position of the entire banking system essentially provide the counterpart to the transactions already mentioned in current and financial transactions with non-residents. For example, the German credit institutions again recorded a decline in their unsecuritised net external assets in the second quarter (€ 14 billion in all). At the short end of the market German banks raised foreign funds amounting to € 20 billion while at the long end they experienced net outflows of € 6 billion.

External transactions by the Bundesbank

As in the case of the credit institutions the short-term external transactions by the Bundesbank, which are not shown under monetary reserves, resulted in net inflows (of € 7 ½ billion) in the second quarter.[1] These essentially concern liabilities to other EU central banks in connection with the payment system TARGET, which ultimately are the result of settling private payment transactions.

Monetary reserves

The monetary reserves of the Bundesbank increased by just under € ½ billion as a result of transactions during the period under review. They also rose by just over € ½ billion as a result of the revaluation uniformly undertaken in the Eurosystem at the end of June. This means that between the end of March and the end of June German monetary reserves valued at current market prices – and excluding the euro claims on the ECB arising from the transfer of reserves at the beginning of the year – rose by € 1 billion to € 87 billion.

1 In line with international practice the changes in the Bundesbank's external position that do not count towards the monetary reserves have been shown under the relevant instruments of the financial account since the beginning of this year. The transactions concerned are essentially those entered under credit transactions.