German balance of payments in 2009

The sharp and synchronous downturn in the global economy in the latter part of 2008 and early part of 2009 had a profound impact on Germany's external balance sheet. While the underlying conditions for German exporters improved steadily in the course of 2009 overall, German exports of goods shrank by almost one-fifth over the year as a whole. As German imports, in terms of value, declined less sharply, the trade surplus narrowed considerably. In addition, inbound cross-border income fell by a much larger margin than outbound income. On balance, the current account surplus contracted by more than one-quarter to €119 billion or 5% of nominal GDP.

This lower current account surplus was accompanied by a significant fall in net capital exports. The main reason for this was a massive reduction in the German banking sector's external assets in response to the crisis. But other cross-border financial operations, too, continued to feel the effects of the financial and economic crisis, particularly during the first half of 2009. On balance, outflows of funds from Germany occurred mainly in the form of portfolio investment and unsecuritised lending.

Current account

Global economic recovery following trough at start of 2009

At the beginning of 2009, German exporters had to contend with highly unfavourable underlying conditions. The global shock to confidence which resulted from the escalating financial crisis led to a worldwide collapse in trade flows. German industry's volume of orders received from abroad fell by nearly one-third over the course of two quarters. Comprehensive support measures for the financial markets and massive monetary and fiscal policy stimuli sparked a rapid rebound from the global paralysis. The economic recovery commenced already in the second quarter of 2009, causing cross-border trade in goods to pick up again. Nevertheless, with global economic output down by just under 1%, the volume of world trade slumped by around 12% on an annual average. The global recession thus brought about a sharp correction of the trade intensity that had increased markedly in preceding years, with strong export nations like Germany particularly hard hit.

The global economic recovery also triggered a renewed rise in the prices of oil and other commodities which, however, came nowhere near to matching their peak levels of mid-2008. For 2009 as a whole, therefore, a sharp decline was recorded in commodity prices. These were down by one-third for Brent crude oil measured in euro and by one-fifth and almost one-sixth respectively for other important industrial and agricultural commodities. This bolstered the purchasing power of commodity-importing countries. The lower commodity prices barely impacted bilateral competitive positions, however, as most industrial trading partners benefited from them on a similar scale. While encountering modest losses in price competitiveness vis-à-vis their euro-area competitors on an annual average, German enterprises enjoyed an improvement in their competitive position vis-à-vis non-euro-area countries, largely on account of exchange rate movements. All in all, the German economy's price competitiveness rose by ½% compared with 2008.[1]

Marked rise in demand for German goods in the course of the year

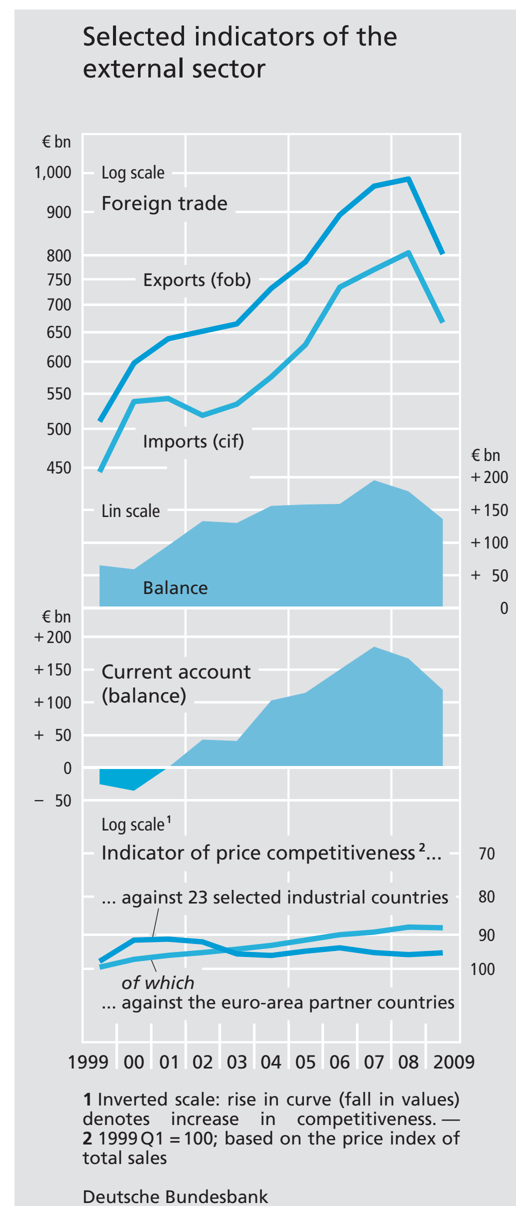
Starting from the cyclical low in the first quarter of 2009, the inflow of orders from abroad increased by one-fifth up to the fourth quarter. German firms benefited from the fact that Asian economies, led by China, started regaining momentum already in the second quarter of the year and that, in addition, economic activity started to pick up in most of the major industrial countries from the middle of the year onwards. This paved the way for an expansion of German exports, first to China and South-East Asia and later to the euro area and other EU countries as well as to Japan. At the end of the year demand for German goods also picked up noticeably in the USA, the OPEC countries and the Russian Federation. Despite this recovery in the course of the year, German enterprises' exports in 2009 were still 18½% lower on an annual average than in 2008. Since German exporters were forced to grant price concessions in the past year, this decrease was somewhat smaller in real terms (16½%). Even so, the decline in exports by German manufacturers was far greater than the over-

1 Calculated on the basis of the deflators of total sales against a group of 23 industrial countries.

all contraction in global trade. A major factor in this was that the demand for capital goods, which accounts for around two-fifths of German exports, was not yet able to fully benefit from the nascent recovery following its initial collapse in the wake of the crisis.

Breakdown of exports by goods

On an annual average, exports of capital goods fell by just over one-fifth in nominal terms. This fall was in large part due to an almost 30% drop in earnings from exported motor vehicles, which make up more than one-third of this segment. However, the statistical definition of this item includes earnings from the sale of new cars to non-resident households which, owing to the car scrappage incentives offered by many industrial countries, generated positive stimuli again from the beginning of the second quarter. In addition, enterprises abroad curbed their demand for German machinery – which accounts for more than one-third of the German capital goods industry's exports – by one-quarter. There was a decline of one-fifth in foreign sales of computer, electronic and optical products and electrical equipment which, however, are only partly classifiable as industrial machinery and equipment. The German consumer product sector, which accounts for almost 20% of total exports, likewise suffered a significant fall in exports of one-sixth. By contrast, the decline in export revenue from the intermediate sector can largely be explained by lower prices. The value of deliveries by the iron and steel industry fell particularly sharply by nearly a third. This resulted from the downturn in the automotive industry, meaning the loss of a major demand segment, coupled with the abrupt end to the construction boom in a number of countries. In price-adjusted terms, the decline amounted to one-fifth. This contrasted with the lower losses posted by the chemical and pharmaceutical industry, which saw foreign sales contract by just over one-eighth.



1 Inverted scale: rise in curve (fall in values) denotes increase in competitiveness. — 2 1999 Q1 = 100; based on the price index of total sales

Breakdown of exports by region

None of the German export markets escaped the effects of the contraction in world trade. In 2009, deliveries to the euro area were

Structure and development of regional foreign trade in 2009

Country/group of countries	Percentage share	Annual percentage change
Exports		
All countries	100.0	– 17.9
of which		
Euro-area countries	43.1	– 17.1
Other EU countries	19.9	– 21.0
of which		
Eight new member states 1	9.7	– 24.0
United States	6.7	– 24.6
Russian Federation	2.5	– 36.6
Japan	1.3	– 15.3
South-East Asian countries 2	3.5	– 13.1
China	4.5	7.0
OPEC	2.8	– 13.5
Developing countries excluding OPEC	9.3	– 14.6
Imports		
All countries	100.0	– 16.4
of which		
Euro-area countries	39.8	– 14.9
Other EU countries	18.5	– 14.7
of which		
Eight new member states 1	10.4	– 10.4
United States	5.9	– 14.1
Russian Federation	3.7	– 33.0
Japan	2.7	– 21.7
South-East Asian countries 2	4.1	– 16.3
China	8.2	– 8.8
OPEC	1.2	– 42.2
Developing countries excluding OPEC	9.9	– 17.1

1 Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania. — **2** Brunei Darussalam, Hong Kong, Indonesia, Malaysia, Philippines, Singapore, South Korea, Taiwan, Thailand.

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17% down on the year in nominal terms and 14% down in real terms. In particular, there was an above-average drop in sales to Ireland (-33%) and Spain (-26½%) whose economies were hit especially hard by the financial and economic crisis. By contrast, the German economy posted smaller losses of around one-eighth in exports to Austria and France.

On balance, the non-euro-area countries generated even more contractionary stimuli. Thus deliveries to markets outside the euro area went down by 18½% in terms of value and by 17½% in real terms. This said, developments differed greatly from country to country. Fortified by far-reaching monetary and fiscal policy measures, China was quickly able to return to its steep medium-term growth path in 2009, enabling the German economy to expand its export earnings there by as much as 7%. The South-East Asian countries also managed to exit the economic recession relatively quickly. Irrespective of this, German exporters still experienced a drop in sales of 13% in this region. Similarly, Japan benefited from the economic recovery in neighbouring countries. This factor, together with the depreciation of the euro vis-à-vis the yen on average during the year, worked to the advantage of German suppliers of goods to this region. Even so, their revenue from business with Japan went down by 15½%.

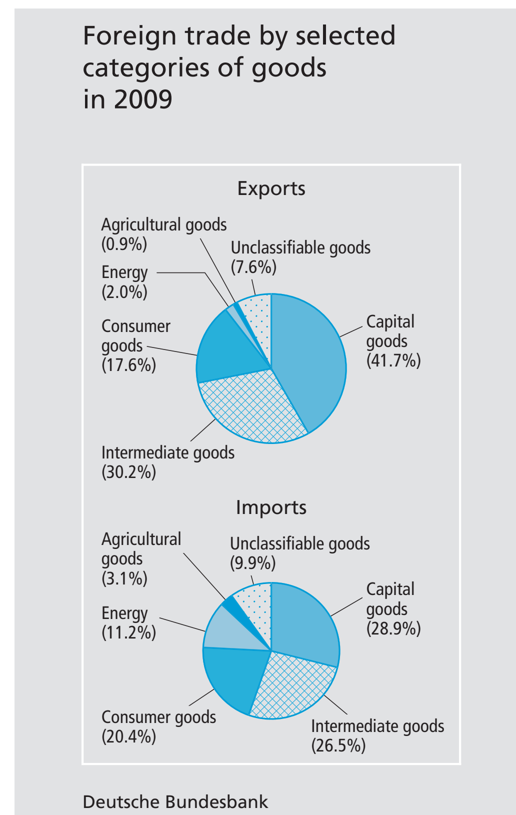
In the new EU member states, the demand for German exports fell by one-quarter. Worsened external financing conditions as well as the extremely close production links to Germany existing in some branches of

industry, for example the car sector, played a part in this. Likewise, at minus one-quarter, the sharp fall in exports to the USA was largely the result of reduced motor vehicle exports. The OPEC countries, which experienced a considerable decline in revenue from oil and gas exports, reduced their imports from Germany by 13½%. German producers' export sales to the Russian Federation decreased by a particularly large margin (-36½%). Here again, reduced receipts from commodity exports are likely to have played a key role.

Imports

German imports likewise recorded a marked decline in 2009. The main reason for this was the sharp slump in global trade during the latter part of 2008 and early part of 2009, which prompted German enterprises to cut production, reduce investment and run down their inventories. Imports of intermediate goods, in particular, increased in the second half of the year in line with the typical pattern in the early phase of a cyclical recovery. During the second and third quarters of 2009, the volume of imported motor vehicles also temporarily jumped on account of the German government's environmental premium encouraging the purchase of new cars. By contrast, imports of other major categories of capital goods had not picked up by the end of the year.

Nominal imports of goods fell by 17½% overall and – in percentage terms – almost as sharply as exports. However, owing to the 8½% decline in import prices across the year as a whole, imports only went down by around half as much as exports in price-



adjusted terms. The fall by one-quarter in the prices of imported raw materials and semi-finished goods was particularly pronounced, whereas there was only a slight fall in the prices of finished goods.

Breakdown of imports by goods

The price effect had a major impact on energy imports, the value of which fell by just over one-third, although in real terms this represented a decline of merely 6%. The lower prices of imported, price-inelastic energy boosted the German economy's purchasing power by almost €26 billion, which is the equivalent of 1.1% of nominal GDP. In terms of value, imports of intermediate goods likewise fell well short of their 2008 level (-27½%). This was primarily due to the fact that, in real terms, German buyers reduced their imports of metal and metal

products by almost one-quarter. As a result of the sharp fall in prices, their expenditure on such products went down by as much as 38½% overall. Conversely, the value of imported chemical and pharmaceutical products decreased by a below-average degree (-13½%). Foreign manufacturers were obliged to make considerable price concessions in this sector as well. Measured by volume, their sales to Germany decreased only by half as much.

Imports of capital goods receded by a nominal 14½%. One contributory factor was the recession-induced fall-off in investment, which caused expenditure on imported machinery to decrease by just over one-quarter. There was a sharp nominal fall in the sales of imported computer, electronic and optical products and electrical equipment (-17%) as well. In addition, foreign motor vehicle exporters saw their sales to the German market decline by just over one-sixth on an annual average. German imports of consumer goods went down by almost 15% overall in 2009.

Breakdown of imports by region

Imports from euro-area countries decreased by 15% in nominal terms. Around half of this decline was attributable to the price component. French and Italian producers, for example, whose deliveries account for a fairly large share of one-fifth and one-sixth each of Germany's imports from the euro area, sustained sales losses in the order of 14% and 15½% respectively. The value of imports from non-euro-area countries was down on the year by 17½%. Here again, the decline in real terms was half that figure. The revenue losses posted in connection with deliveries to Germany by major oil and gas-producing countries such as the OPEC states (down by two-fifths) and the Russian Federation (down by one-third) were in large part caused by the sharp fall in the cost of energy and raw materials. Japanese suppliers had to contend with sales losses of one-fifth in the German market, with the yen's strong appreciation against the euro on an annual average contributing to this effect. The decline in imports from South-East Asian countries was only a little less pronounced. US manufacturers, whose products had become noticeably dearer in Germany on an annual average following the distinct appreciation of the US dollar against the euro, recorded a 14% drop in turnover. Furthermore, imports from the newly acceded EU member states went down by just over one-tenth. Exporters from China, whose share of total German imports now amounts to 8%, were unable to buck the general downward trend and were obliged to reduce their deliveries to German buyers by 9%.

Trade and current account balances

As revenue from cross-border merchandise trade fell much more markedly than expenditure in 2009 in absolute terms, the trade surplus plummeted by €42½ billion to €136 billion, thereby falling below its 2004 level. The deficit on "invisible" current transactions amounted to €7½ billion. The overall current account surplus, which includes supplementary trade items, narrowed by €48 billion to €119 billion, or 5% of nominal GDP.

Invisibles

The balance on the invisibles account, which comprises services, income and current

transfers, reversed from a surplus of €1½ billion to a deficit of €7½ billion. This stemmed from the smaller surplus in the income account and a larger deficit on services, which more than offset lower net expenditure on current transfers.

Services

The deficit on the services sub-account expanded by €2½ billion to €9½ billion in 2009. Here, a prominent contributory factor was declining receipts from merchanting trade – which denotes net reported income from transactions of residents with non-residents involving goods that do not enter the economic territory – which fell from €11½ billion to €8½ billion. Moreover, the surpluses resulting from transportation services went down by €1½ billion to €7 billion. This decline, mirroring the trend in overall merchandise flows, affected exports more than imports. Conversely, the net surplus resulting from insurance services rose by €1 billion to €1½ billion. This mainly reflected the fact that German reinsurers saw a decline in their claims payments to non-residents relative to their receipts from premiums, whereas the reverse development applied to business operations of foreign reinsurers in Germany. Net earnings from financial services almost equalled the previous year's level. In the category of other services, net income likewise changed very little amid substantial movements in individual segments. Thus while, on balance, earnings from research and development declined and expenditure on business-related services increased appreciably, payments for foreign patents and licences were reduced considerably.

Travel

In the field of foreign travel, which is the largest item in cross-border services, the deficit decreased by €1½ billion to €33 billion. Although the percentage fall in revenue (-8½%) was greater than the reduction in expenditure (-6½%), in absolute terms the former amounts to no more than about two-fifths of payments. Expenditure on trips to other euro-area countries, which accounts for around half of all German travel expenditure, fell by 9½%. The decline in spending on journeys made to non-euro-area countries was much smaller (-3%). However, more money was spent on trips to the United Kingdom as well as on travel to Bulgaria, Tunisia and America (excluding the USA).

Income

The surplus on the cross-border income account declined by €9 billion to €34 billion in 2009. This was primarily due to a reduced positive outturn of investment income as, despite an improved net external position, receipts from investment (-€52½ billion) contracted more substantially than the corresponding expenditure (-€44½ billion). Three-quarters of the decline in investment income from the rest of the world was attributable to reduced interest earnings, which mainly relate to interbank transactions. The worldwide reduction of interest rates to a record low and the substantial cutback in lending both contributed to this development. Resident investors' receipts from international portfolio investment were also lower. Income from principal repayments of foreign bonds and notes rose. However, this was more than offset by reduced receipts from money market instruments, mutual fund shares and dividends. This was influenced by shifts in invest-

Major items of the balance of payments

€ billion

Item	2007	2008	2009
I Current account			
1 Foreign trade 1			
Exports (fob)	965.2	984.1	802.7
Imports (cif)	769.9	805.8	666.8
Balance	+ 195.3	+ 178.3	+ 135.9
Supplementary trade items 2	– 9.9	– 12.6	– 9.2
2 Services (balance)	– 11.6	– 7.0	– 9.4
of which Travel (balance)	– 34.3	– 34.6	– 33.1
3 Income (balance)	+ 43.5	+ 42.6	+ 33.8
of which Investment income (balance)	+ 43.2	+ 42.1	+ 34.1
4 Current transfers (balance)	– 32.2	– 34.3	– 32.0
Balance on current account	+ 185.1	+ 167.0	+ 119.1
II Balance of capital transfers 3	+ 0.1	– 0.2	– 0.2
III Financial account 4			
1 Direct investment	– 62.8	– 75.2	– 19.5
2 Portfolio investment	+ 142.7	+ 35.0	– 90.8
3 Financial derivatives	– 85.2	– 25.4	+ 20.4
4 Other investment 5	– 213.3	– 131.1	– 51.1
5 Change in the reserve assets at transaction values (increase: –) 6	– 1.0	– 2.0	+ 3.2
Balance on financial account	– 219.5	– 198.7	– 137.8
IV Errors and omissions	+ 34.3	+ 32.0	+ 18.9

1 Special trade according to the official foreign trade statistics (source: Federal Statistical Office). From January 2007, excluding supplies of goods for or after repair/maintenance, which up to December 2006 were deducted via supplementary trade items. — **2** Including warehouse transactions for the account of residents and the deduction of goods returned. — **3** Including the acquisition/disposal of non-produced non-financial assets. — **4** Net capital exports: –. For details see the table "Financial transactions" on page 27. — **5** Includes financial and trade credits, bank deposits and other assets. — **6** Excluding allocation of SDRs and excluding changes due to value adjustments.

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ment patterns and the poorer profitability of foreign enterprises. This also affected the foreign subsidiaries of German enterprises, with the result that, in addition to lower interest payments because of redeemed claims, direct investment income likewise declined considerably (see also page 29).

The development of investment payments to non-residents was likewise influenced by the decline in interest rates as well as by the deterioration in corporate profitability. This resulted in a reduction in interest payments on loans and securities along with lower dividends. As on the income side, the large-scale downturn in bank loans led to a substantial reduction in their debt service, with the result that spending on this item went down considerably. This was reinforced by a sharp decline in outflows related to the servicing of securities. Non-residents' receipts from direct investment in Germany were likewise well below the level one year previously.

Current transfers

The net deficit arising from current transfers lessened by €2½ billion to €32 billion, mainly on account of the decline in private transfers to the rest of the world. While German transfers to the EU budget went down, the same was also true of income received, especially from investment income tax on the assets of non-residents in Germany and from EU payments to Germany in connection with structural policy. For this reason, the deficit from public transfers decreased only marginally.

Financial transactions

Determinants of financial transactions

In 2009, the current account surplus was accompanied by German net capital exports in the amount of €138 billion. These outflows, however, were around one-third below their level of 2008, when they had already shrunk by around €20 billion. This further decline was in part brought about by heavy deleveraging in the financial sector, which led to a substantial lowering of the banking sector's unsecuritised cross-border lending positions. By contrast, international investors responded very cautiously to the improved sentiment in the international financial markets from the second quarter onwards as well as to the burgeoning recovery of the world economy in the course of 2009. Hence, Germany continued to benefit from large safe-haven inflows of portfolio investment, particularly in the first half of the year. Nevertheless, these inflows progressively waned with market participants' growing optimism and the reversal of the yield spread of ten-year government bonds vis-à-vis US Treasuries as well as the widening of spreads within the euro area, while residents concurrently stepped up their cross-border investment activity.

Net capital exports in portfolio investment

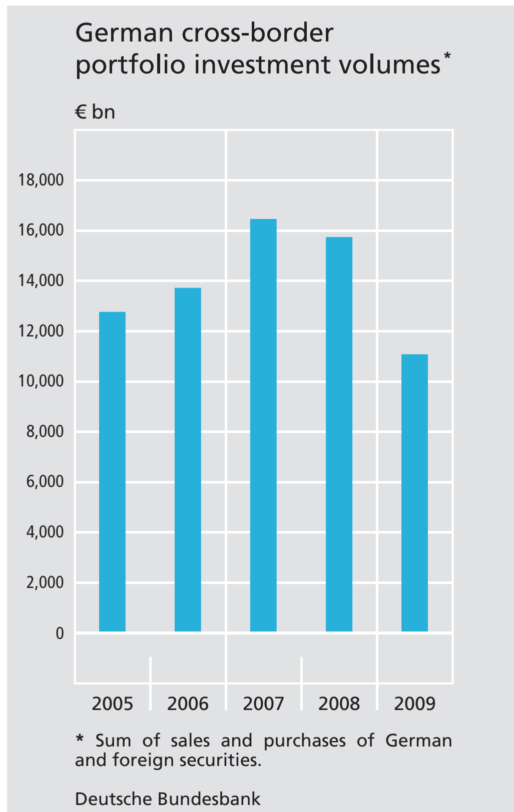
Against the backdrop of a sharp decline in transaction volumes, portfolio investment closed the year with net capital outflows of €91 billion, compared with inflows of €35 billion in 2008, when crisis-related behaviour in the wake of the collapse of the US investment bank Lehman Brothers led to a sharp reduction in cross-border portfolio positions. The demand for foreign securities picked up in the second quarter as the financial sector stabilised following massive government and central bank intervention and the global economy slowly got back on track.

German investment in foreign securities

In 2009, German investors again purchased foreign securities on balance, acquiring foreign instruments worth a net €72½ billion, compared with disposals amounting to €25 billion in the preceding year. With their interest mainly focused on debt securities (€71 billion), they steered clear of exchange rate risks and instead invested in – principally euro-denominated – bonds and notes (€83½ billion).[2] Bonds issued by other euro-area countries are traditionally very popular with German investors owing to their interest rate advantage over German federal bonds (Bunds). On an annual average for 2009 this spread amounted to 81 basis points. Such exposures do, however, entail greater price and liquidity risks. Foreign government bonds purchased in 2009 included Italian (€7½ billion) and Greek (€6 billion) issues. As a rule, the aim of acquiring private bonds and notes issued outside Germany is likewise to achieve a higher return, although this may entail a poorer credit quality of the non-resident issuer. The demand for foreign bank debt securities (€30 billion) remained slightly above that for government paper (€29½ billion). Additionally, German investors considered corporate bonds issued abroad an attractive option (€24½ billion), although in the majority of cases the actual borrowers were domestic firms. Against the backdrop of a reluctance by banks to grant credit and

Bonds and notes

2 Given high interest rate and exchange rate uncertainty, overall investment by German investors in foreign currency bonds dropped slightly (-€½ billion).



improved underlying conditions in the capital market, German enterprises made greater use of bonds and notes as a financing instrument. In the main, such bond issues are effected indirectly through specialist affiliates located abroad, particularly in the Netherlands. If bought by residents, this kind of debt security is recorded in the balance of payments under capital exports, even though it is the German enterprise which indirectly benefits from these financial resources[3].

Money market instruments

By contrast, during 2009 resident investors offloaded foreign money market instruments (€12½ billion) which, prior to the crisis, had proved a popular financing instrument with special-purpose vehicles. In particular, the banking sector reduced its exposure to this type of short-dated instrument. Following the marked decline in their yield in line with central bank key interest rates, money market instruments became less attractive compared with longer-term assets offering significantly higher returns.

Equities

Resident investors were slow to warm to foreign equities in 2009. Even so, they ended up buying paper of this kind for €2 billion, after reducing their foreign equities holdings by a total of €60½ billion in the two preceding years. The massive slump in share prices which persisted until March 2009 evidently dampened investors' risk appetite, although the major stock exchanges subsequently enjoyed a clear rally.

Mutual fund shares

German residents may also have invested in the international equity markets to a small extent indirectly via foreign mutual funds. While they redeemed foreign mutual fund shares in the amount of €½ billion net, after purchasing €8½ billion worth of these in 2008, this mainly related to money market funds (€5 billion), which, like money market instruments, were deemed not very attractive in the capital market environment outlined above. By contrast, funds with a different investment focus were indeed able to attract investors.

Foreign investment in domestic securities

Despite an increasingly optimistic mood in the financial markets as the year wore on, foreign portfolio investors reduced their investment in German securities by €18 billion

3 As a rule, financing affiliates pass on the proceeds from these issues to their parent companies in Germany. These financial flows are listed under direct investment as intra-group loans (see p 29).

in 2009, following net purchases in the amount of €10 billion in 2008. However, these asset disposals can be attributed to particular developments in the area of private debt securities and so should not be seen as a general shift out of the German market.

Private debt securities

Foreign investors sold a record volume of private debt securities with an original maturity of more than one year (€98½ billion). This was mainly due to the exceptionally high level of net redemptions of Pfandbriefe. The volume of public Pfandbriefe outstanding, in particular, has been falling for some years, recording a decline of around €80 billion in 2009 alone. Among other factors, this is explained by the public sector's growing propensity to tap the capital market directly and by changes in banks' wholesale funding behaviour. Moreover, the issuance of German Pfandbriefe did not pick up until after the Eurosystem had announced its purchase programme for covered bonds in May 2009 and tensions on the international financial markets had begun to ease.

At the same time, foreign investors sold debt securities issued by resident non-banks (€13½ billion). This primarily involved the redemption of previously issued structured securities. The corresponding hedging transactions were the main factor behind the high net capital imports in the financial derivatives category (€20½ billion).[4]

4 See also Deutsche Bundesbank, Certificates and warrants in the balance of payments, Monthly Report, March 2008, pp 26-27.

Financial transactions

€ billion, net capital exports: –

Item	2007	2008	2009
Direct investment	– 62.8	– 75.2	– 19.5
German investment abroad	– 118.7	– 91.9	– 45.1
Foreign investment in Germany	+ 55.9	+ 16.7	+ 25.6
Portfolio investment	+ 142.7	+ 35.0	– 90.8
German investment abroad	– 148.7	+ 25.0	– 72.6
Equities	+ 21.1	+ 39.6	– 2.2
Mutual fund shares	– 42.3	– 8.4	+ 0.6
Bonds and notes [1]	– 101.2	– 23.9	– 83.5
Money market instruments	– 26.4	+ 17.7	+ 12.5
Foreign investment in Germany	+ 291.5	+ 10.1	– 18.2
Equities	+ 40.0	– 32.6	+ 7.8
Mutual fund shares	+ 4.8	– 8.6	+ 0.2
Bonds and notes [1]	+ 199.2	+ 13.9	– 75.4
Money market instruments	+ 47.5	+ 37.4	+ 49.2
Financial derivatives [2]	– 85.2	– 25.4	+ 20.4
Other investment [3]	– 213.3	– 131.1	– 51.1
Monetary financial institutions [4]	– 153.7	– 130.1	+ 61.2
Long-term	– 113.0	– 130.4	+ 1.4
Short-term	– 40.6	+ 0.3	+ 59.8
Enterprises and households	– 10.2	+ 20.1	– 26.0
Long-term	– 27.6	+ 1.8	– 16.6
Short-term	+ 17.3	+ 18.3	– 9.4
General government	+ 4.9	+ 9.2	– 3.2
Long-term	– 2.9	– 1.4	– 2.6
Short-term	+ 7.8	+ 10.5	– 0.6
Bundesbank	– 54.4	– 30.2	– 83.0
Change in the reserve assets at transaction values (increase: –) [5]	– 1.0	– 2.0	+ 3.2
Balance on financial account	– 219.5	– 198.7	– 137.8

1 Original maturity of more than one year. — **2** Securitised and non-securitised options and financial futures contracts. — **3** Includes financial and trade credits, bank deposits and other assets. — **4** Excluding Bundesbank. — **5** Excluding allocation of SDRs and excluding changes due to value adjustments.

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Public debt securities

By contrast, foreign demand for debt securities issued by the German public sector remained very robust in 2009, totalling €79½ billion. Of this, €56½ billion was invested in money market instruments with a maturity of up to one year,[5] mostly in the form of Bubills, which have recently been used more intensively by central government as a means of funding.[6] In addition, foreign investors purchased longer-dated German government bonds worth €23½ billion. Especially in times of crisis, foreign investors value the high credit rating and liquidity offered by German Bunds. Foreign demand for Bunds was consequently concentrated on the first half of the year when risk aversion was still very high. Such purchases are likely to have been chiefly motivated by the increased need for security felt by buyers. An additional consideration during this period was that German Bunds continued to offer an interest rate spread over US Treasuries, which likewise usually serve as a safe haven. Furthermore, the net issuance of debt securities by the German public sector rose substantially in 2009 to €103½ billion, compared with €28½ billion in 2008. Within the euro area, however, German Bunds, as mentioned above, were at a high negative spread vis-à-vis government bonds in other euro-area countries which widened as the year progressed.

Equities

The resurgence of confidence in the cyclical recovery of the German economy was reflected in the return of foreign investors to the German equity market. Following large sales in 2008 (€32½ billion), 2009 saw purchases of equities in the amount of €8 billion. Thus investors participated in the German share price rally which, in turn, was bolstered by higher investment from abroad. Overall, the broad CDAX index rose by 20% last year.

Mutual fund shares

In 2009, the German mutual fund industry managed to halt the outflows of foreign investment, which had totalled €8½ billion in the previous year. The overall break-even position masked certain portfolio shifts, however. For instance, foreign investors divested from German money market funds and instead acquired other mutual fund products.

Direct investment worldwide ...

The financial crisis had a dampening effect on cross-border direct investment in 2009. According to initial UNCTAD estimates,[7] global direct investment flows in 2009 fell by roughly two-fifths to around US$1 trillion. The decline thus accelerated compared with 2008. The key reason for this was that the further plummeting in direct investment in the developed economies was accompanied by reduced investment in emerging market economies (EMEs) and developing countries, following a sharp rise in direct investment in these countries one year before. This decrease is likely to have been generated not just by cyclical factors – reflected, *inter alia*, in the slump in global trade and reduced corporate profits – but also by changes in longer-term investment strategies and options. This is suggested by the fact that, in response to the tense financial market setting, there was a further sharp decrease in

5 By contrast, foreign investors sold money market paper issued by the private sector worth around €7 billion.
6 See Deutsche Bundesbank, The current economic situation in Germany, Monthly Report, August 2009, p 41.
7 See UNCTAD, Global Investment Trends Monitor, No.2, 19 January 2010.

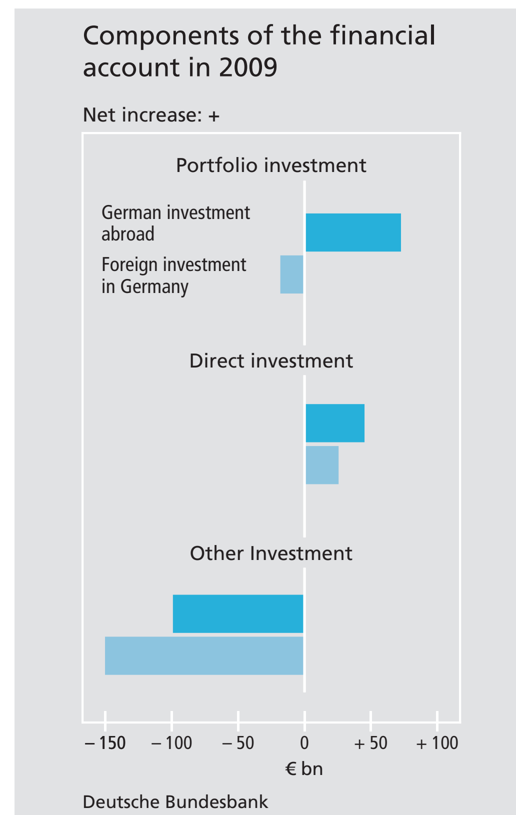
the number of cross-border mergers and acquisitions.

... and in Germany

The unfavourable global conditions also affected German inward and outward direct investment. Contrary to the general trend, foreign direct investment inflows into Germany actually increased. German foreign investment outflows, on the other hand, declined steeply. All in all, the year closed with a distinctly lower level of net capital exports (€19½ billion) than in the preceding years.

German direct investment abroad

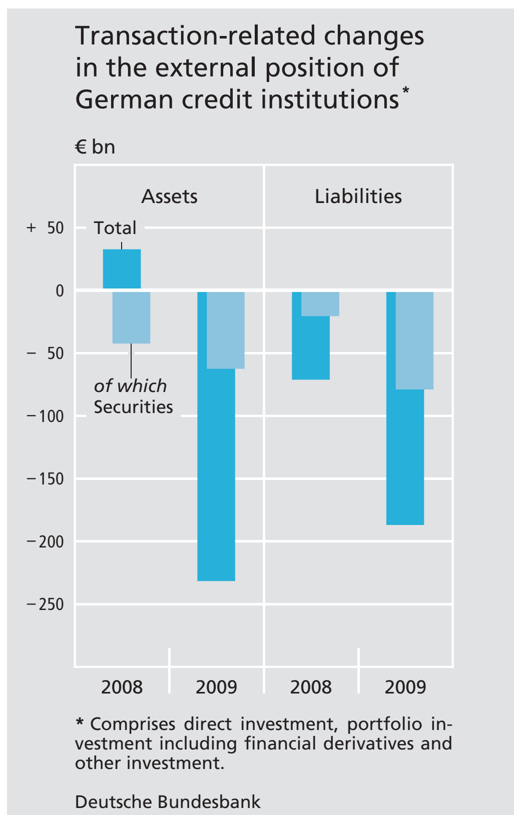
In 2009, the volume of resources invested abroad by German enterprises amounted to €45 billion, which was less than half as much as in 2008. Resident companies primarily focused on providing their foreign affiliates with more equity capital, although, at €47½ billion, this amount was perceptibly lower than in 2008 (€61 billion). Furthermore, despite an ongoing crisis-induced decline in earnings, German direct investors reinvested more earnings in their affiliates (€14½ billion) than in 2008. The main reason for this was that dividend payments by affiliates shrank more than their profits. By contrast, intra-group credit transactions were used to channel funds back to Germany (€17 billion). This was achieved, firstly, in the form of financial loans by foreign affiliates to their parent companies (€26 billion). As explained above, the requisite funding largely stemmed from the issuance of debt securities by financing affiliates, the majority of which are located in the Netherlands. These funds were channelled to the parent companies in the form of long-term financial loans worth €28 billion net. Secondly, with regard to trade credit



relationships with affiliates abroad, in a development matching the decline in foreign trade transactions, loan repayment by affiliates in the reporting year outstripped the granting of new trade credits; this meant that, overall, inflows of funds (€5 billion) were also recorded in this category.

Regional and sectoral breakdown

Providers of financial intermediation, insurance companies and holding companies were prominent among the German direct investors abroad. As in 2008, measures to offset the losses of German banks' foreign affiliates played a key role in this. In regional terms, the bulk of German direct investment in 2009 was concentrated on EU countries, with Luxembourg (€12½ billion), the United Kingdom (€9 billion) and Italy (€6½ billion) the principal investment targets.



* Comprises direct investment, portfolio investment including financial derivatives and other investment.

Deutsche Bundesbank

Foreign direct investment in Germany

Contrary to the international trend, foreign direct investment in Germany rose in the crisis-stricken year 2009. Indeed, at €25½ billion, it was noticeably up on the year (€16½ billion). This increase was largely the result of higher direct investment loans and additional equity capital provided by foreign proprietors to their German affiliates. At the same time, domestic enterprises were actively looking for and in some cases specifically targeting new investors in order to strengthen their capital base.

Regional and sectoral breakdown

Almost three-quarters of the inflows originated from EU partner countries, with Luxembourg (€7 billion) and Italy (€5 billion) to the fore. The Gulf states (€5 billion) were also major investors. Foreign investors showed a particular interest in the German automobile industry.

Other investment ...

Like direct investment, other investment – which comprises financial and trade credits (where not allocated to direct investment) as well as bank deposits and other assets – recorded net capital exports in 2009. These amounted to €51 billion and ultimately resulted from the fact that German external liabilities (€150 billion) fell more steeply than claims on non-residents, which were down by €99 billion.

... of non-banks ...

Non-banks' unsecuritised financial transactions contributed to capital exports in the amount of €29 billion net. The bulk of this amount related to transactions by enterprises and households (€26 billion), which primarily increased their foreign bank deposits. The cross-border activities of general government led to capital outflows totalling €3 billion. This was mainly due to the repayment of financial loans from foreign banks.

... and the banking system

The unsecuritised transactions in the banking system recorded in the balance of payments led to net outflows of €22 billion in the reporting year. Contrary to the overall development, however, credit institutions recorded inflows of funds (€61 billion). Banks significantly reduced their financial credit to foreign counterparties (-€176½ billion) while their unsecuritised external liabilities (including other assets and deposits of non-banks) likewise fell (-€115½ billion). This massive reduction in external transactions on both sides of the balance sheet is part of the adjustment processes in the banking system

which were triggered by the financial crisis. Consequently, the main factor driving the overall development in other investment was the transaction-related increase in the Bundesbank's net external position, amounting to €83 billion. Much of this was due to the increase in claims within the TARGET2 large-value payment system (€62½ billion). At the same time, the Bundesbank's external liabilities went down (-€22 billion). These consist *inter alia* of foreign central bank deposits, which were drawn down during 2009.

Reserve assets: transactions ...

The transaction-related changes in the Bundesbank's foreign reserves are shown in a separate item in the balance of payments. In 2009, this item exhibited a decrease of just over €3 billion which, in net terms, was solely attributable to the reduction in foreign currency reserves.

... and other adjustments

Aside from the transaction-related changes shown in the balance of payments, further adjustments were made to the reserve assets during 2009 which are not specified in the balance of payments according to the international standards. For instance, the Bundesbank's reserve assets gained considerably in value (€18 billion) through the customary practice of marking to market. This was mainly driven by the upward valuation of the Bundesbank's gold holdings by €15½ billion to the current level of €84 billion. Moreover, during the third quarter of 2009, the G20 summit that was held in April in London resulted in a non-BOP-relevant reallocation of special drawing rights by the International Monetary Fund (IMF) equivalent to almost €12 billion. All in all, the reserve assets rose by €26½ billion in balance sheet terms to reach € 125½ billion at the end of 2009.