German balance of payments in 2013

The German economy ran a current account surplus of €206 billion in 2013, which equates to 7½% of gross domestic product (GDP). This represents a moderate year-on-year rise of €7½ billion. A reduction in the current account surplus vis-à-vis euro-area partner countries was more than offset by a sharp increase in net receipts from non-European transactions, thereby continuing a tendency observed since 2010. Germany now no longer exhibits a major imbalance position within the euro area. The adjustment processes have already had a noticeable impact, with the German economy's contribution to that in the form of robust import growth showing up clearly during the reporting period, in contrast to 2012.

The increase in the current account surplus vis-à-vis non-euro-area countries in 2013 was caused by the fact that the economic upturn in Germany was accompanied by barely any rise in imports of goods from outside Europe. In addition, the German economy profited considerably from better terms of trade on the back of a considerable fall in prices for internationally traded commodities and semi-finished products. Export momentum was flat in 2013. This was mainly due to the fact that demand for German-made high-quality capital and consumer goods in the emerging market economies (EMEs) was more subdued during the reporting period than in the preceding years, during which it had shot up.

Germany's financial account with the rest of the world continued to be influenced by the financial and sovereign debt crisis. However, it also mirrored Germany's current account surplus. On balance, net capital exports in 2013 were high (€250½ billion). These were primarily attributable to German portfolio investment in other countries and to unsecuritised credit transactions by credit institutions. German banks noticeably recorded a strong decline in short-term financial credit liabilities to non-residents which in part had resulted from the trend to deposit funds in Germany at the height of the financial crisis. This was counterbalanced, inter alia, by the sharp decline in the Bundesbank's cross-border claims under the TARGET2 payment system. The direct investment sub-account – which is generally influenced by longer-term motives – likewise recorded capital outflows. This was chiefly prompted by German firms' desire to further expand their presence abroad.

Current account

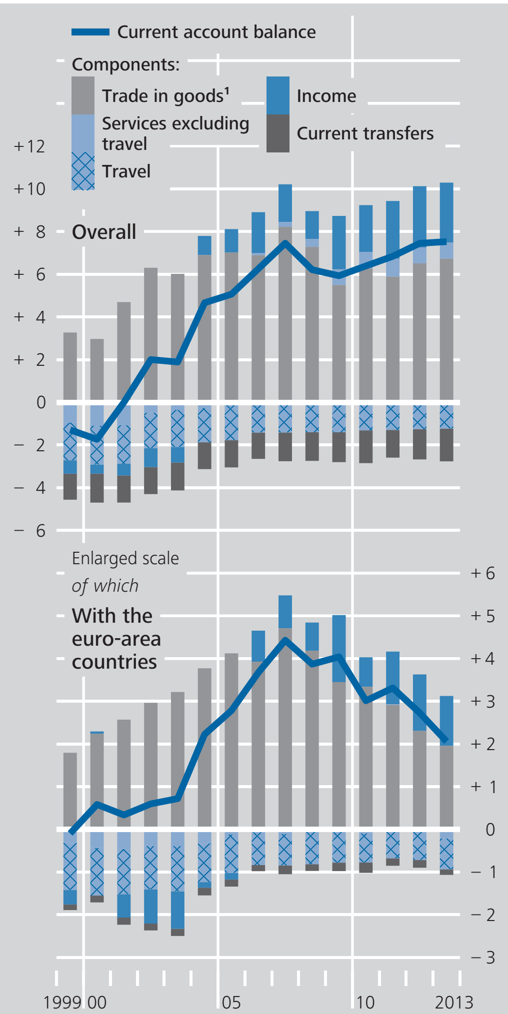
Underlying trends

Further rise in current account surplus in 2013

The German economy's current account surplus increased further in 2013, buoyed by improving national and international economic conditions and a calmer mood in the financial markets. The year-on-year growth of €7½ billion was, however, much smaller than in 2012 (+€20 billion), when the temporary intensification of the euro-area sovereign debt crisis had triggered widespread uncertainty in the euro area and led in Germany to the postponement of investment projects, in particular. Although global production and world trade started to pick up again over the course of 2013, this did not provide any additional stimuli for German goods exports. By contrast, imports were perceptibly boosted by domestic demand, which from mid-2013 onwards was bolstered by renewed business investment. Although the volume of imported goods went up significantly, expenditure on imports showed no year-on-year increase on balance owing to the marked fall in prices for internationally traded commodities and semi-finished products. The quantitative significance of the terms-of-trade gains (estimated at €14½ billion) is illustrated by the fact that they far outstripped the increase in the foreign trade surplus (+€8 billion).

Germany's current account

As a percentage of GDP



1 Special trade according to the official foreigen trade statistics, including supplementary trade items, excluding freight and insurance costs for import.

Deutsche Bundesbank

Surplus from trade and investment income, balanced result for services, deficit only from current transfers

Besides the structurally positive trade balance, investment income, too, has been recording an increasingly sizeable surplus for ten years now. This is broadly linked to the sharp expansion in net external assets, although in the reporting year yield effects were particularly significant. Moreover, the revised data indicate that the services sub-account (including travel) has been close to balance since 2010.[1] One reason for this is that the services offered by German enterprises in the international transport and logistics business and as providers of IT services and technical and financial services are also in demand outside of Germany. In comparison, foreign competitors are not meeting with as much demand in Germany. This has also been the case up to now for the construction sector, although utilisation of the production capacities of the German construction sector is currently extremely elevated owing to the high demand in Germany. The deficit recorded for current transfers rose comparatively sharply in 2013, as it had done one year previously.

Germany's current account surplus came to €206 billion in 2013, which equates to 7½% of GDP. The persistently high overall result masks

1 This is the case if freight and insurance costs for imports are excluded. If these components are included, the services sub-account recorded a small deficit during this period.

German surplus curtailed by euro-area adjustment mechanisms

two countervailing tendencies. On the one hand, further progress has been made towards reducing the current account surplus vis-à-vis the euro-area partner countries. Thus Germany's current account surplus vis-à-vis the euro area in relation to GDP has more than halved compared with the peak level recorded in 2007. Hence the adjustment processes underway in the euro-area countries are having a clear impact on the German economy's external transactions. On the other hand, the current account imbalance vis-à-vis non-euro-area countries has steadily widened over the past three years. In the year under review, this owed something to the fact that the non-European goods trade balance was heavily influenced by the import price reversal on account of the greater weight of energy and commodity supplies. Viewed over a longer period, however, Germany's growing trade surplus vis-à-vis this group of countries indicates that major trading partners outside the euro area have not yet achieved a notable correction of their domestic imbalances.

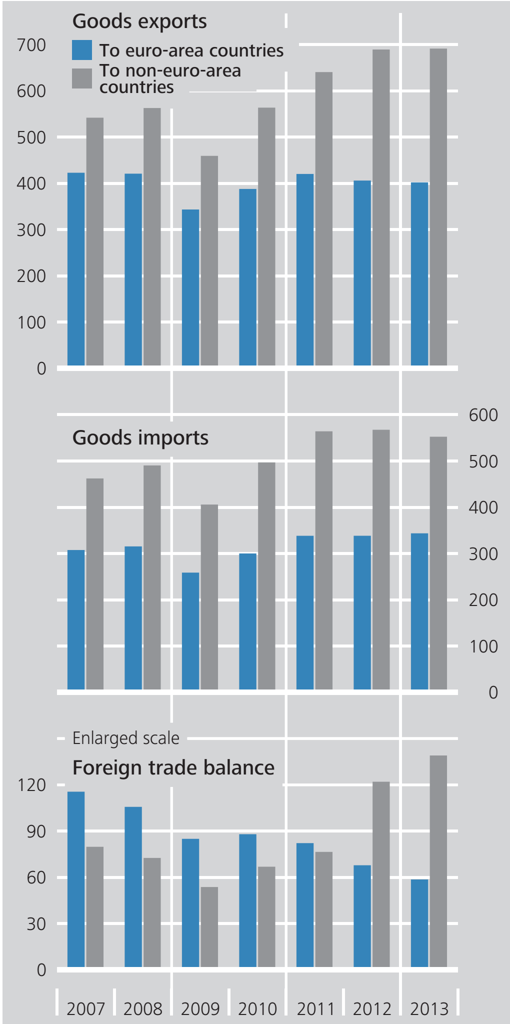
Goods flows and balance of trade

German foreign trade sluggish in 2013

For the first time since 2009, there was no year-on-year increase in German foreign trade in 2013. Nominal exports of goods fell slightly by ¼% after growing by 3¼% in 2012. Nominal imports of goods were 1% down on the year. In real terms, however, they rose by an estimated 1½%, as import prices eased significantly. This was due *inter alia* to the euro's appreciation against major currencies and to lower world market prices for commodities and semi-finished products. By contrast, export prices declined only marginally. During the period under review the terms of trade thus shifted in favour of the German economy for the first time since the recession year of 2009. Overall, Germany's positive trade balance increased by €8 billion to €197½ billion. In purely arithmetical terms, this increase was solely attributable to price effects; in terms of volume, net exports in 2013 were down on the year.

Germany's foreign trade within and outside the euro area

€ billion



Source of unadjusted figures: Federal Statistical Office.
Deutsche Bundesbank

High EME export volume not maintained, …

German exports stagnated overall in 2013, and the very pronounced differences in regional trends observed in 2012 were much less in evidence. While the volume of goods delivered to the euro area once again contracted, the year-on-year decrease of 1% was distinctly smaller than in 2012 (-3½%). Exports to non-European markets recorded an increase only for a few countries during the period under review. Whereas in 2011 and 2012, very high rates of growth had been recorded for exports to emerging market economies, the economic situ-

Foreign trade by region

%

Country/ group of countries	Percentage share 2013	Annual percentage change 2011	2012	2013
Exports				
Euro area (17)	36.8	8.4	– 3.4	– 1.0
Other EU countries	20.2	13.3	3.3	2.0
of which				
United Kingdom	6.9	11.8	11.8	3.3
Central and east European EU countries (8)[1]	9.9	15.5	0.1	1.5
Switzerland	4.3	14.9	2.2	– 3.3
Russia	3.3	30.8	10.6	– 5.2
USA	8.1	12.5	17.9	1.6
Japan	1.6	15.0	13.4	– 0.1
Newly industrialised economies in Asia[2]	3.0	8.8	4.5	2.2
China	6.1	20.6	2.9	0.4
South and east Asian emerging market economies[3]	2.3	12.3	11.7	– 6.2
OPEC	2.8	– 2.0	18.3	3.5
All countries	100.0	11.5	3.3	– 0.2
Imports				
Euro area (17)	37.7	12.7	0.0	1.6
Other EU countries	18.2	15.8	– 1.1	3.1
of which				
United Kingdom	4.8	18.0	– 4.3	– 1.3
Central and east European EU countries (8)[1]	10.5	15.9	1.4	5.4
Switzerland	4.1	13.8	2.1	1.1
Russia	4.0	28.4	4.6	– 5.5
USA	5.7	7.3	5.2	– 5.0
Japan	2.8	5.0	– 7.1	– 11.0
Newly industrialised economies in Asia[2]	3.0	– 4.5	– 6.0	– 3.8
China	9.7	2.9	– 1.3	– 6.6
South and east Asian emerging market economies[3]	3.1	13.8	– 0.5	1.2
OPEC	1.2	42.8	28.5	– 7.0
All countries	100.0	13.2	0.4	– 1.1

1 Bulgaria, Croatia, Czech Republic, Hungary, Latvia, Lithuania, Poland, Romania. **2** Hong Kong, Singapore, South Korea, Taiwan. **3** India, Indonesia, Malaysia, Philippines, Thailand, Vietnam.
Deutsche Bundesbank

ation in these countries has since changed to such an extent that it proved impossible to further lift the high levels already attained. This was probably attributable to lower orders for capital goods owing to waning investment dynamics and also, in part, to nearing saturation levels in the demand for high-quality motor vehicles. Fluctuations in demand for these two types of goods have a major impact on German foreign trade, as they account for a high proportion of exports, not least owing to German suppliers' strong market position. Thus the share of capital goods and cars in total exports was around 45% in 2013, while deliveries of these two product groups to G20 emerging-market countries made up over 57% of the total.

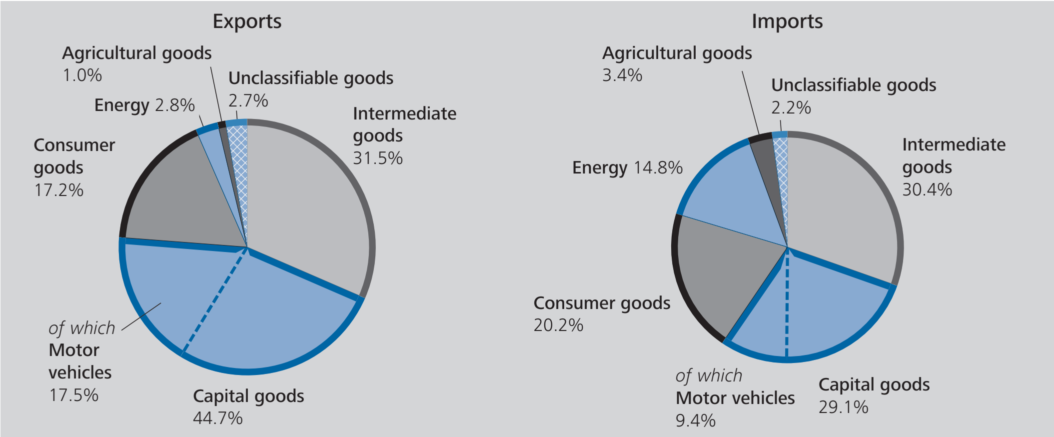
… but slight rise in deliveries to non-European industrial countries

Although the level of exports to non-European industrial countries continued to rise, there was a considerable loss in momentum. Deliveries to the United States went up by only 1½% in 2013 compared with 18% in 2012. There was a similarly marked slowdown for Japan, where exports stagnated during the period under review after having risen by 13½% in 2012. The euro's appreciation against the US dollar and especially against the yen may have played a role in this. Revenue from goods exported to the other Asian industrial countries picked up by a comparatively strong 2¼%. The impression that the industrial countries – with the exception of the euro area, Japan and Switzerland – bolstered German exports during the period under review and thereby helped to offset waning demand from the emerging markets is further supported by German exporters' business with the United Kingdom, which grew perceptibly (+3¼%). More goods were also exported to central and east European EU countries.

Fall in euro-area business in 2013 not as sharp as in 2012

Germany's export performance vis-à-vis euro-area countries last year reflects the marked easing of recessionary pressure in 2013 in the countries worst hit by the crisis. On an annual average, exports to Greece, Portugal and Spain stabilised vis-à-vis 2012, and in some cases ex-

Foreign trade by selected categories of goods in 2013



Source of unadjusted figures: Federal Statistical Office. Deviations from 100% due to rounding.
Deutsche Bundesbank

ports to these countries even tilted upwards again towards the end of the year. Exports to Ireland expanded considerably, not least because of the pick-up in investment there. German exporters' revenue from business in the euro area did not rise overall, however, owing to the shrinking demand for German goods in the two large countries of France and Italy.

No rise in international demand for German capital goods

German capital goods showed no marked year-on-year increase in export turnover in 2013. This was mainly due to a decline in orders of aircraft and spacecraft and of machinery and equipment, although orders of computers and electronic and optical products provided an export stimulus. Automotive exports also only increased marginally, although there were marked regional differences. While there was a clear rise in demand for German automobiles in the United States and the United Kingdom, cars sales fell in both China[2] and the euro area. Exports of intermediate goods rose only slightly owing to the relatively muted pace of global growth. By contrast, German consumer goods exports recorded another jump during the period under review, which is likely to have been chiefly fuelled by the high demand for pharmaceutical products.

Clear growth in imports thanks to German upturn

The distinct increase in real imports of goods in 2013 was attributable to the economic upturn in Germany, which has been driven by domestic demand. Germany's expanding industrial output particularly benefited deliveries of intermediate goods from central and east European countries. Close production links have been formed with this region over the past two decades. With regard to imports from the euro area, German enterprises and households primarily raised their demand for capital and consumer goods. The marked growth in the overall volume of capital goods imported by Germany during 2013, following a dip in 2012, indicates a resurging propensity to invest over the course of the year. Higher sales were recorded, in particular, for computers, electronic and optical products and electrical equipment, but also machinery produced abroad. The largest single contribution to import growth came, however, from consumer goods, which is consistent with German households' exceptionally high propensity to purchase.

Euro-states main beneficiaries of higher demand

European countries benefited to a far greater extent from German import demand in 2013 than did overseas manufacturers. Thus imports from the euro area went up by an estimated 3% on the year in real terms, whereas imports

2 See Deutsche Bundesbank, Reasons for the recent slump in German goods exports to China, Monthly Report, November 2013, pp 47-49.

from non-euro-area countries rose by only ½%. In 2012, deliveries of goods from both regions had declined in equal measure by 1¾%, while in the previous two years non-euro-area countries fared clearly better. One noteworthy feature was the downward trend in goods imported from east Asia. In 2013, the value of deliveries from China was 6½% down on 2012. Imports from the newly industrialised Asian economies dropped last year by 3¾%, having already fallen in the two previous years. Imports from Japan in 2013 were one-sixth lower than in 2011. One reason for this might be that during the last two years Japanese producers have focused on the strongly expanding domestic market. Moreover, the yen's sharp depreciation against the euro during the period under review – by around one-fifth on an annual average compared with 2012 – evidently led to a temporary fall in the value of Japanese imports.[3]

Breakdown of invisibles

Cross-border services business more muted

Germany's services business with the rest of the world expanded in 2013 at a slower pace than it had done in previous years. This was because most cross-border services are linked to manufacturing, which developed rather moderately in 2013 at both a national and an international level. Financial and insurance services similarly increased only slightly. By contrast, the exchange of business-related services in the technical and commercial areas, which are less cyclically sensitive, picked up. German residents' travel expenditure abroad once again rose only moderately year on year. Proceeds from non-residents' travel to Germany, which are far smaller, rose by a similar amount. Overall, Germany's services sub-account[4] recorded a surplus of €2½ billion, compared with €3½ billion in 2012. For cross-border travel – a major sub-item – the deficit was unchanged at €33½ billion.

Business-related services: surpluses remain high

German enterprises play a key role in the international freight and logistics business. Given the very intense competition and considerable price pressures, they are evidently managing to maintain market share at the expense of their profit margins. In 2013, cross-border transport – particularly sea freight[5] – once again recorded substantial net receipts, which, at €8½ billion, were only slightly down on the 2012 figure. With moderate turnover growth during the period under review, revenue and expenditure from engineer-related and other technical services roughly balanced out last year, as in 2012. By contrast, cross-border transactions connected with research and development (R&D) services, IT applications and commercial services continued to expand sharply, thereby perpetuating a trend that has been observed for some years. In these globally expanding lines of business, German enterprises are likewise well positioned overall. Whereas IT and R&D services tend to yield a clear surplus (€5 billion during the period under review), commercial services are sourced from abroad on balance. This sub-item posted a deficit of €5 billion in 2013. Furthermore, patents and licences accounted for sizeable receipts. Last year they shot up by three-tenths to €22 billion, the lion's share of which was due to rising usage fees for mail distribution networks. On balance, this sub-account recorded a surplus of €7 billion.

German construction firms refocus on Germany

For five years, German construction firms have been shifting the focus of their activities back to the domestic market. Revenue earned from construction work abroad fell by 11% in 2013 to €7½ billion; the cumulated fall in revenue from 2008 comes to more than one-quarter.[6] The activities of foreign construction firms in

3 This is because the value of the goods imported decreases simply as a result of being converted into euro if the selling prices are contractually stipulated in yen. Renegotiation of the delivery contracts can lead to a drop in the price of Japanese goods owing to the yen's depreciation, which generally results in growth in the volume of demand for these products in Germany.
4 Excluding freight and insurance costs for imports.
5 However, in the area of port services, expenditure far outweighs revenue.
6 Expenditure on goods and services purchased from local subcontractors must be deducted from this figure. This went up further in 2013, lowering net revenue by just over €1 billion.

Germany continue to play only a minor role. In 2013, they received €1½ billion for construction work, assembly and repairs. Expenditure was thus only slightly higher than the level recorded in 2012.[7]

Moderate rise in foreign travel spending

German residents' expenditure on foreign travel in 2013 rose only moderately, as in 2012, by 2¼%. This is attributable to private foreign travel, which, following two years of strong growth, recorded hardly any increase in expenditure in 2013 (+1½%). By contrast, business foreign travel expenses climbed by 8% during the period under review, following sometimes sizeable budget cuts in the preceding years (eg by one-eighth in 2012). Germany's euro-area partner countries benefited disproportionately from the additional expenditure of German business travellers and tourists. In particular, more German holidaymakers went to Spain and Greece again in 2013. However, travel expenditure in Italy and Portugal, as well as in Croatia, fell last year, after recording marked increases in previous years. Turkey and Bulgaria continued to gain in popularity as holiday destinations. But the number of tourists travelling to North Africa, especially to Egypt and Tunisia, plummeted in 2013 – as it had done in 2011 – after picking up in 2012. German residents' travel expenditure in Switzerland continued to dwindle in 2013 – having already dropped substantially during the two previous years – probably in response to the exchange rate adjustment. It is likely that travel destinations in Austria benefited from this. The higher level of spending in the United Kingdom may well be linked to the renewed rise in business travel budgets. Expenditure on trips to distant destinations stagnated overall in 2013 amid a minor shift from America to Asia.

Higher investment income surplus thanks to lower expenditure

Over the past ten years, Germany has seen a trend of rising net surpluses from cross-border investment income. In 2013 the surplus came to €75 billion, which was up by around €1 billion on the year. This was mainly due to continuously falling outlays on outbound foreign direct investment, portfolio investment and lending. At 8%, the expenditure drop was on a similar scale to 2012. All three investment categories had an equally dampening impact on the liabilities side of the investment income account, with interest payments on loans recording the highest relative decline, dropping by one-sixth. Safe-haven effects may have played a role in this. Income from German assets abroad likewise declined distinctly (by 4½%), after falling by only half as much in 2012. Given the ongoing asset accumulation, the result suggests that during the period under review the average return on Germany's external assets was comparatively low. The return on investment varied according to type. While revenue from international portfolio investment rose distinctly, receipts from direct investment dipped slightly. The biggest factor behind the poor rate of return is likely to have been the lower level of interest income from cross-border lending, which sank by more than one-fifth, not least because of the low-interest-rate environment.

Larger deficit on current transfers

Current transfers to the rest of the world went up sharply by 11½% in 2013 to €63½ billion, with both public and private-sector transfers recording growth. Payments to the EU posted the biggest year-on-year rise (climbing by one-sixth) and now account for more than half of all of Germany's current transfers to the rest of the world. The large influx of immigrants in recent years is presumably the main reason behind the increase in the level of cross-border transfers sent by foreign workers in Germany to eastern Europe and, to a lesser extent, to southern Europe. However, these payments have a quantitatively small weight as they make up only 5% of total current transfers. Transfers from the rest of the world to resident recipients likewise went up by 11½%. The net deficit from current transfers widened by €4½ billion to €42 billion in 2013. Just over three-fifths of this is attributable to net transfers to the EU budget.

7 The receipts of German suppliers and subcontractors working for foreign construction firms providing services in Germany increased, but are very low.

Financial transactions

Underlying trends

Signs of normalisation in the international capital markets

In 2013, Germany's current account surplus was again mirrored by high net capital exports (€250½ billion).[8] Two-thirds of this figure was attributable to portfolio investment. A key reason for the high share of portfolio investment in comparison to 2012 was the marked decline in non-residents' demand for German government bonds. This reflected the easing of tensions on the European capital markets, which in turn lessened foreign investors' urge to turn to Germany as a safe haven. Instead, both domestic and foreign investors refocused on the search for yield. Capital outflows were also recorded in the other investment and direct investment sub-accounts. By contrast, the Bundesbank's TARGET2 claims decreased on balance for the first time since the start of the financial crisis.

Positive signals for the international financial markets came, first, from the progress made last year towards overcoming the European debt crisis: the adjustment processes initiated by the countries most severely affected by the crisis have made significant headway in improving their economic performance.[9] Second, signals that policymakers would begin to phase out non-standard monetary policy measures became increasingly apparent in non-euro-area countries, especially the United States. The clearest such signal was the US Federal Reserve's announcement in May 2013 that it would cut back quantitative easing, followed by initial tapering measures at the beginning of 2014. Expectations that this would push up global interest rates likewise had an impact on international and German financial transactions during the reporting year, especially on portfolio investment.

Portfolio investment

Marked rise in capital exports through portfolio investment

Portfolio investment, which as a rule is particularly quick to react to mood swings on the financial markets, resulted in net capital exports of €165 billion last year amid slightly higher turnover, compared with €64½ billion in 2012. This marked rise is primarily due to a reversal of foreign demand for German securities. After acquiring large volumes of German securities in 2012, non-resident investors sold German portfolio paper on balance in 2013. This led to a transaction-related decline of €24 billion in foreigners' holdings of German securities.

Foreign investment in domestic public bonds and notes, …

Although the volume of domestic public bonds and notes purchased by foreign investors again exceeded the amount sold (€29½ billion), this represented a decrease on the year of over 60%. This reflects international investors' growing optimism and reduced interest in Germany's role as a safe haven compared with previous years. This is borne out by the successful placement of public debt securities in Ireland, Italy, Portugal and Spain.

… in domestic private bonds and notes, …

Cross-border trading in private debt securities, unlike public bonds and notes, resulted in net sales and redemptions over the year as a whole (€41½ billion). It should be noted, however, that the outstanding volume of bank debt securities issued by residents has itself been declining for years and fell by around €115 billion in the year under review. This is due, among other factors, to redemptions of covered bonds by the German Landesbanken, which no longer issue the same volume of these securities owing to a change in their business models. Moreover, credit institutions received substantial deposits from non-banks in the wake of the financial crisis, which reduced their need to raise funding through bonds. The decline in

8 The difference between the balances of the current account and the financial account is primarily attributable to errors and omissions (€43 billion).
9 See Deutsche Bundesbank, Adjustment processes in the member states of economic and monetary union, Monthly Report, January 2014, pp 13-78.

non-residents' holdings of German private debt securities is thus clearly due not only to waning demand, but also to a decreasing supply.

… in German money market instruments …

International investors also offloaded domestic money market instruments on balance (€23 billion). However, this was mainly paper issued by the public sector, which, following strong demand in 2012, was sold (or redeemed) on balance in 2013. Foreign investors reduced their holdings of private short-dated securities only marginally in 2013 following significant sell-offs in the two previous years.

… and in German equities and mutual fund shares

Cross-border turnover in German equities fell further in the reporting year. As sales fell more than purchases, share trading resulted in net capital imports of €5½ billion. By contrast, purchases of German mutual fund shares by non-residents rose substantially, leading to further inflows of €6 billion.

German investment in foreign bonds and notes, …

Conversely, German investors acquired larger volumes of foreign bonds and notes on balance (€141 billion, following €110 billion in 2012). There was particularly high demand for interest-bearing paper. Purchases of bonds and notes from the rest of the euro area were slightly down on 2012; this was partly due to the fact that public authorities (including the resolution agencies) reduced their holdings of debt securities from the European periphery countries (through redemptions or sales). Furthermore, German commercial banks' cross-border activities, in line with their lending behaviour, remained subdued, also in respect of portfolio investment. By contrast, non-banks – notably money market funds and other non-monetary financial institutions – stepped up their foreign investment in bonds from southern Europe (primarily Italy and Spain).

… in foreign currency bonds …

The net acquisition of foreign currency bonds also rose. In comparison to 2012, purchases of securities in foreign currencies more than tripled in 2013 (€22½ billion). Demand for securities denominated in US dollars, pounds

Major items of the balance of payments

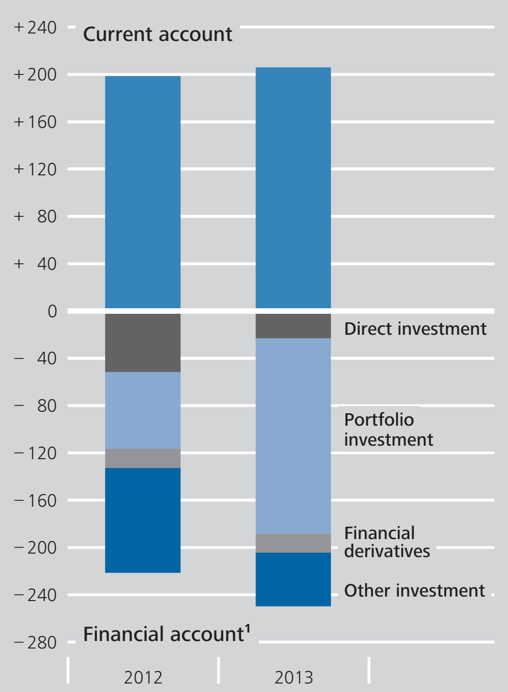
€ billion

Item	2011 r	2012 r	2013 r
I Current account			
1 Foreign trade[1]			
Exports (fob)	1,061.2	1,095.8	1,093.8
Imports (cif)	902.5	905.9	896.2
Balance	+ 158.7	+ 189.8	+ 197.7
Supplementary trade items[2]	− 20.3	− 33.2	− 29.0
2 Services (balance)	+ 3.4	+ 3.3	+ 2.4
of which Travel (balance)	− 33.8	− 33.6	− 33.6
3 Income (balance)	+ 70.5	+ 76.4	+ 76.9
of which Investment income (balance)	+ 68.7	+ 73.8	+ 74.8
4 Current transfers (balance)	− 33.9	− 37.7	− 42.0
Balance on current account	+ 178.4	+ 198.6	+ 206.0
II Balance of capital transfers[3]	+ 0.6	+ 0.0	+ 1.8
III Financial account[4]			
1 Direct investment	− 15.6	− 51.7	− 23.2
2 Portfolio investment	+ 28.0	− 64.7	− 165.0
3 Financial derivatives	− 27.7	− 16.3	− 16.1
4 Other investment[5]	− 156.5	− 88.7	− 45.5
5 Change in the reserve assets at transaction values (increase: –)[6]	− 2.8	− 1.3	− 0.8
Balance on financial account	− 174.7	− 222.7	− 250.6
IV Errors and omissions	− 4.3	+ 24.1	+ 42.8

1 Special trade according to the official foreign trade statistics (source: Federal Statistical Office). **2** Including warehouse transactions for the account of residents and the deduction of goods returned. **3** Including the acquisition/disposal of nonproduced non-financial assets. **4** Net capital exports: –. For details see the table "Financial transactions" on p 45. **5** Includes financial and trade credits, bank deposits and other assets. **6** Excluding allocation of SDRs and excluding changes due to value adjustments.
Deutsche Bundesbank

Major items of the German balance of payments

Balances in € billion



1 Excluding transaction-related change in reserve assets; net capital exports: –.

Deutsche Bundesbank

sterling and Danish krone was particularly strong.

… and in foreign equities and mutual fund shares

Prompted by declining risk aversion and a brighter outlook for the global economy over the course of the year, domestic investors also showed a growing interest in foreign shares. They purchased equities worth €19 billion net in 2013 on the back of higher turnover. Persistently low interest rate levels in the advanced economies, coupled with the expectation of rising long-term interest rates and accompanying price losses on government bonds, may have contributed to the pick-up in demand. On top of this, stock prices rose in many countries. The financial markets in Europe continued to grow calmer, which likewise encouraged investors to add equities to their portfolios. This is also underlined by the regional breakdown of share purchases. There was an above-average increase in purchases of equities issued by foreign enterprises in the euro area, but shares issued by Japanese and British companies were likewise in demand. By contrast, purchases of mutual fund units issued by US enterprises, which had played an important role during 2012, fell by almost half.

Indirect investment through foreign mutual fund companies had an even stronger impact than direct share purchases abroad. During 2013 as a whole, German investors purchased foreign mutual fund units totalling over €31½ billion; this was more than 40% higher than the already high levels of demand for this type of investment recorded in 2012.

Financial derivatives showing net capital exports

Financial derivatives (which are aggregated to form a single item in the balance of payments) showed net capital exports, as in the two preceding years. At €16 billion, the result was on a par with 2012.

Direct investment

Direct investment worldwide …

The international integration of the enterprise sector continues to make rapid progress. According to estimates made by the United Nations Conference on Trade and Development (UNCTAD), global foreign direct investment (FDI) rose by 11% last year to reach almost US$1½ trillion,[10] a level comparable to the pre-crisis average for the years 2005-07. As in 2012, emerging and developing economies accounted for the bulk of these direct investment inflows despite growing expectations in the course of the year that the US Fed would start tapering its bond buying programme. Direct investment thus proved relatively robust in this regard. Nonetheless, UNCTAD considers that the gradual rundown of quantitative easing could potentially dampen direct investment flows to some of the emerging markets most strongly affected. Inflows to developed countries also increased, although the picture was mixed. In 2013, foreign investors strongly favoured a number of EU countries, in particular,

10 See UNCTAD, Global Investment Trends Monitor, No 15, 28 January 2014.

including Germany, which significantly improved its position as a recipient of FDI inflows last year according to these data.

… and in Germany

While foreign firms significantly increased their direct investment in Germany in 2013 compared with 2012, German enterprises did not expand their foreign investment as strongly in the reporting year as in 2012. Foreign direct investment flows to and from Germany in 2013 nonetheless resulted in net capital outflows of €23 billion (compared with the prior-year figure of €51½ billion).

German direct investment abroad

At €43½ billion, German firms' outbound FDI was down on the previous year (€62 billion). Although German companies supplied their foreign subsidiaries with additional equity capital in 2013 (€13 billion), they mainly strengthened their capital base by reinvesting earnings (€30 billion). By contrast, flows in the form of intra-group credit transactions practically cancelled each other out: lending by domestic enterprises to their foreign affiliates roughly matched net borrowing by domestic companies from their foreign subsidiaries. In some cases, countervailing individual large-volume transactions were directly connected. For example, funds were raised from non-resident financial subsidiaries and passed on to subsidiaries in other countries.

Drivers of German outbound FDI

Though down on the year, outbound foreign direct investment remained robust, which underlines the ongoing importance that German firms attach to maintaining a presence abroad. In a survey of the Association of German Chambers of Commerce and Industry (DIHK),[11] 46% of the companies surveyed – more than ever before – said that they wished to expand their FDI. Strategic objectives were the main reason given. Almost half the companies gave "distribution and customer services" as their primary motive, while more than a third cited "market penetration". Only a fifth of the companies said that "cost savings" were the main factor behind their foreign direct investment. Ten years ago, this was industry's key reason for transferring production abroad. Since then, cost motives have become steadily less important, probably also due in large part to the significant improvement in Germany's price competitiveness.

An expansion in German firms' presence abroad does not necessarily imply lower levels of investment in Germany. This is shown, *inter alia*, in a study presented in the box on pages 46 and 47. According to this study, there is a positive relationship in the long run be-

Financial transactions

€ billion, net capital exports: –

Item	2011 r	2012 r	2013 r
1 Direct investment	– 15.6	– 51.7	– 23.2
German investment abroad	– 58.2	– 62.0	– 43.3
Foreign investment in Germany	+ 42.7	+ 10.3	+ 20.1
2 Portfolio investment	+ 28.0	– 64.7	– 165.0
German investment abroad	– 21.6	– 109.8	– 141.0
Equities	+ 2.7	– 11.7	– 19.2
Mutual fund shares	– 1.3	– 21.7	– 31.3
Bonds and notes 1	– 18.3	– 76.5	– 86.7
Money market instruments	– 4.8	+ 0.1	– 3.8
Foreign investment in Germany	+ 49.6	+ 45.1	– 24.0
Equities	– 11.3	+ 1.1	+ 5.3
Mutual fund shares	+ 7.1	– 3.8	+ 6.0
Bonds and notes 1	+ 51.1	+ 52.2	– 12.3
Money market instruments	+ 2.7	– 4.4	– 23.0
3 Financial derivatives 2	– 27.7	– 16.3	– 16.1
4 Other investment 3	– 156.5	– 88.7	– 45.5
Monetary financial institutions 4	– 52.6	+ 113.7	– 101.7
Long-term	– 31.3	+ 37.6	+ 33.6
Short-term	– 21.3	+ 76.1	– 135.3
Enterprises and households	+ 4.8	+ 10.7	– 29.3
Long-term	– 6.2	– 7.7	– 23.2
Short-term	+ 10.9	+ 18.4	– 6.0
General government	– 2.5	– 80.4	– 10.8
Long-term	+ 2.9	– 13.4	– 6.3
Short-term	– 5.4	– 67.0	– 4.4
Bundesbank	– 106.1	– 132.7	+ 96.2
5 Change in the reserve assets at transaction values (increase: –) 5	– 2.8	– 1.3	– 0.8
Balance on financial account	– 174.7	– 222.7	– 250.6

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.
Deutsche Bundesbank

11 See DIHK Survey, Auslandsinvestitionen in der Industrie, spring 2013.

Foreign direct investment and domestic investment

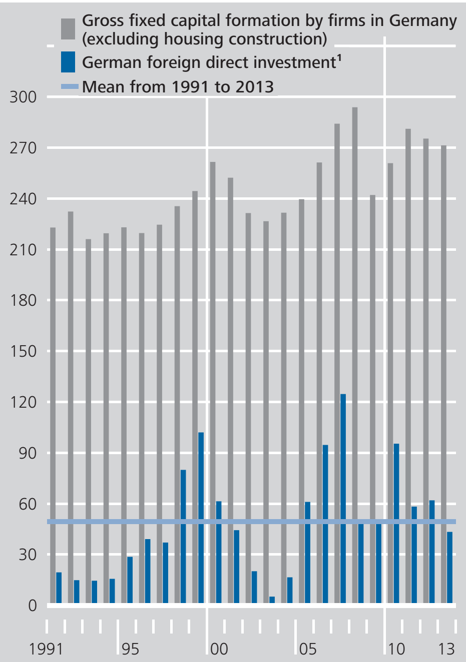
In the public debate, the relatively moderate level of investment in Germany is often linked with reports of German manufacturers' expanding output abroad. It is suggested, for example, that Germany's outbound foreign direct investment (FDI) means that German firms invest less in the domestic economy as this is rendered superfluous by the acquisition or expansion of foreign production capacity. In actual fact, however, the presumed substitutional relationship between corporate investment in Germany and German FDI cannot be empirically confirmed at the macroeconomic level.

Descriptive analysis

The data on German outbound FDI show no significant expansion in the recent past. Over the past two decades, the statistics on German FDI recorded an annual mean value of just under €50 billion. In 2012, Germany's FDI was just above and in 2013 just below the long-run average. These data provide no confirmation for a supposed increased investment shift to export markets at the current time. Nor do the data indicate any substitution effect between foreign and domestic investment. A comparison with the investment behaviour of firms in Germany suggests, rather, a co-movement between German foreign investment and investment in Germany driven by cyclical factors (see chart). This applies equally to gross fixed capital formation in the total economy and to business investment,[1] which is a more appropriate yardstick in this context.

Foreign direct investment and domestic investment

€ billion



1 Net capital exports: +.
Deutsche Bundesbank

Empirical analysis for Germany

A long-run complementary relationship between German outbound FDI and business investment in Germany was established in a study published back in 2006.[2] An updated estimation for the period from 1971 to 2013 confirms those previous findings.[3] In line with the 2006 study and with earlier analyses,[4] investment amounts were again normed to gross domestic product (GDP). Moreover, as in 2006, the measure chosen was direct investment in the form of equity stakes owing to the better comparability it affords with the gross fixed capital formation concept.[5]

1 Private non-residential investment.
2 See Deutsche Bundesbank, Direct investment and domestic investment, Monthly Report, September 2006, p 50.
3 A dummy was used to take account of the extraordinary period from 2008 (financial crisis).
4 See, for example, M S Feldstein (1995), The Effects of Outbound Foreign Direct Investment on the Domestic Capital Stock, in M S Feldstein, J. R. Hines and R. G. Hubbard (eds), The Effects of Taxation on Multinational Corporations, University of Chicago Press, pp 43-66.
5 A positive sign is used for net capital exports, contrary to the balance of payments notation.

For the analysis the equation

$$\beta_1 \frac{BI}{GDP} + \beta_2 \frac{FDI_{IN}}{GDP} + \beta_3 \frac{FDI_{OUT}}{GDP} + c = \varepsilon$$

has been estimated as a vector error correction model (VECM).[6] BI stands for business investment in Germany, FDI_{IN} for inbound FDI and FDI_{OUT} for outbound FDI (in each case in the form of equity stakes); c is a constant and ε the error term. The complementary relationship between German firms' domestic investment and outbound FDI is determined by the negative sign of β_3 (see table). Using causality tests,[7] it can additionally be shown that outbound FDI influences domestic investment. The figures indicate that, at least in the long run, German outbound FDI goes hand in hand with higher domestic investment. Increased foreign investment by German enterprises evidently leads to a rise in domestic investment needs.

Foreign direct investment and domestic business investment

Annual data, 1971-2013, t-values in brackets

Variable	Cointegration vector	Error correction equation	Loading coefficient
$\frac{BI}{GDP}$	β_1 = 1.00[1]	$\Delta\frac{BI}{GDP}$	– 0.41 (– 3.60)
$\frac{FDI_{IN}}{GDP}$	β_2 = 1.64 (5.28)	$\Delta\frac{FDI_{IN}}{GDP}$	– 0.50 (– 2.96)
$\frac{FDI_{OUT}}{GDP}$	β_3 = – 1.28 (– 4.34)	$\Delta\frac{FDI_{OUT}}{GDP}$	0.00[1] –
c	– 0.12 (– 47.70)		

1 Restricted.
Deutsche Bundesbank

G20 states

In order to give the study a broader base, the G20 countries[8] were analysed from 1993 to 2012 with a view to determining to what extent domestic gross fixed capital formation is dependent on inbound or outbound FDI (in relation to GDP).[9] In addition, the countries' economic growth and output gap – as indicators of the cyclical development and economic situation – and the level of and change in price competitiveness[10] were included as further explanatory variables. Overall, the estimation (as a country panel with fixed effects and robust standard errors) indicates that outbound FDI generally has a positive, and in any case non-negative, impact on the development of domestic gross fixed capital formation. The results suggest that domestic investment is mainly driven by cyclical factors.

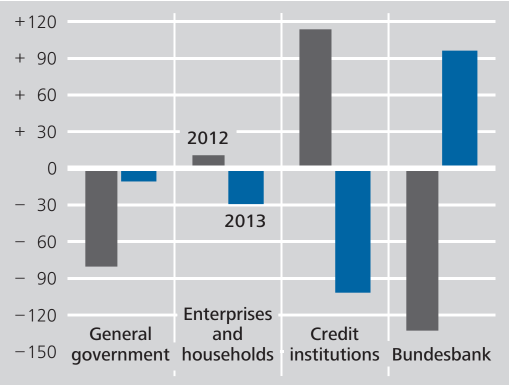
Conclusion

A relationship between outbound FDI and domestic investment can be confirmed empirically; however, it is not the frequently presumed negative, substitutional relationship but, rather, a positive, complementary one. However, caution is called for when performing and, in particular, interpreting such studies as, on the one hand, the investment definitions follow different methodological concepts and, on the other, the FDI data are unable to fully capture firms' foreign activity owing to the requisite statistical definitions. These include the reporting exemptions, but also the widespread phenomenon of production by foreign contracting parties or licencees, which – without a corresponding equity stake – is by definition not classified as FDI.[11]

6 The variables are integrated of order 1. A Johansen cointegration test suggests one cointegration relationship.
7 An LR test shows that the loading coefficient for outbound FDI can be restricted to 0. That is an indication of weak exogeneity. At the same time, the coefficients of the lags of $\Delta BI/GDP$ are not significant, which is a sign of strong exogeneity.
8 Excluding the European Union.
9 Norming to GDP mainly serves to facilitate comparability (scaling) of the values across the various countries.
10 Compared with 56 trading partners based on consumer prices.
11 Detailed information and methodological notes on FDI statistics are available on the Bundesbank's website at http://www.bundesbank.de/Navigation/EN/Statistics/External_sector/Direct_investments/direct_investments.html.

Other investment* broken down by sector

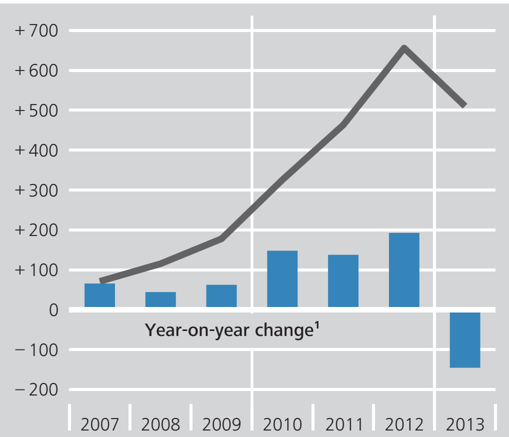
Balances in € billion



* Primarily financial and trade credits as well as bank deposits; net capital exports: –.
Deutsche Bundesbank

The Bundesbank's TARGET2 balance

€ billion, year-end levels



1 Net capital exports: +.
Deutsche Bundesbank

tween outbound FDI and business investment in Germany.

Regional and sectoral breakdown

As in 2012, German FDI flowed mainly into industrial countries in 2013. In Europe, investors focused primarily on the United Kingdom. Outside of Europe, Asian countries, particularly China, were popular investment locations. Sizeable funds flowed in addition to North and South America. The foremost domestic investors during the reporting period were German private equity companies and manufacturing enterprises, especially those in the mechanical engineering and chemical industries.

Foreign direct investment in Germany

Non-resident investors doubled their direct investment in Germany from just under €10½ billion in 2012 to just over €20 billion in 2013. This increase highlights both the aforementioned global strengthening of world FDI flows and Germany's attractiveness as an investment location; total inflows to the group of developed countries as a whole grew considerably less sharply. While equity stakes in foreign-owned German enterprises rose only marginally (€2½ billion), greater inflows came from the reinvestment of earnings generated in Germany (3½ billion) and, most of all, in the form of loans from foreign proprietors to their German affiliates (€14 billion).

Regional and sectoral breakdown

The funding received by German enterprises came mainly from affiliated enterprises in Europe, especially from the neighbouring countries of Belgium, Luxembourg, the Netherlands and Switzerland. In the case of the Benelux countries, which are major locations of international holding companies, this occurred almost exclusively on balance in the form of intra-group loans. By contrast, French proprietors withdrew substantial amounts of funds from Germany, also through the intra-company credit channel. While resident investment companies benefited considerably from fresh injections of foreign funds, the withdrawal of foreign capital mainly affected domestic subsidiaries and branches in the manufacturing sector, especially in the area of vehicle construction.

Other investment

Net capital exports of other investment

Other investment, comprising financial and trade credits (inasmuch as these do not constitute a part of direct investment) as well as bank deposits and other assets, resulted in net capital exports of €45½ billion in 2013. Both non-banks and the banking system recorded outflows of funds.

Capital outflows from non-banks …

The cross-border transactions of domestic non-banks generated net capital outflows amounting to €40 billion in 2013. The bulk of these capital exports was accounted for by enterprises and households (29½ billion). They paid down cross-border financial loans previously received – the majority of which were long-term – (€22½ billion) and also increased their bank deposits abroad (13½ billion). General government recorded additional net capital exports totalling €11 billion. These included, *inter alia*, the scheduled payment of two tranches to the European Stability Mechanism (ESM) in the amount of €8½ billion.

… and from the banking system

The banking system's cross-border activities resulted in an increase of €101½ billion in credit institutions' unsecuritised net external assets in 2013. Owing to the ongoing deleveraging process, German banks' cross-border liabilities decreased far more than their corresponding assets. As in 2012, the reduction in assets of €56½ billion mainly affected long-term financial credits. German banks' cross-border liabilities contracted by €158½ billion. A sharp drop in financial credits featured prominently in this case, too (€174½ billion), predominantly in the form of intra-group transactions. This should be partly seen as a natural rebound from the large influx of foreign cash to German banks in 2012, when tensions in the euro area resulted in a huge volume of safe-haven flows to Germany. Besides this, end-of-year window-dressing operations by the banking sector – particularly in the run-up to the ECB's asset quality review – may have played a role. The associated depletion of banks' balance sheet assets helped to temporarily improve their equity ratio.

Change in Bundesbank's external position due to fall in TARGET2 claims

In 2013, the Bundesbank's net external position recorded a decline of €96 billion caused chiefly by transactions under the TARGET2 payment system. In contrast to previous years, the TARGET2 balance in the reporting period dropped by €145½ billion; this was the first decrease in the Bundesbank's TARGET2 claims since the start of the financial crisis in 2007.[12] This was a reflection of the calmer mood on the international financial markets and the support provided by the international community to the euro-area member states worst affected by the crisis. By contrast, a decline in non-resident deposits with the Bundesbank led to capital outflows of €49½ billion. This mainly related to temporary deposits parked at the Bundesbank by other central banks and international organisations, including funds belonging to the European rescue packages.

Reserve assets

Transactions …

Transaction-related changes in the reserve assets are shown as a separate item in the balance of payments. In 2013, they amounted to just under €1 billion net. The increase of €1½ billion in the foreign currency reserves outweighed a slight decrease in the reserve position vis-à-vis the International Monetary Fund (IMF).

… and balance sheet adjustments

As in past years, the international reserve holdings were also influenced by balance sheet adjustments which, in line with internationally agreed accounting standards, are not recognised in the balance of payments. The end-of-year revaluation of the reserve assets at market prices resulted in a decline of €45½ billion in 2013. This was due mainly to downward valuation adjustments on the Bundesbank's gold holdings: the price of gold fell for the first time in years during the reporting period. In addition, small write-downs due to valuation changes were made on the foreign currency reserves and reserve position with the IMF. The upshot of all this was that Germany's reserve assets as recorded in the balance sheet fell by €45 billion to €144 billion at the cut-off date of 31 December 2013.

12 At the end of 2013, the Bundesbank's TARGET2 claims stood at €510 billion. They reached their highest end-of-month level in August 2012, at €751½ billion.