Financial markets

Financial market setting

Financial markets shaped by divergent economic data and monetary policy stance

In the first few months of 2018, the international financial markets were influenced by a slightly more moderate global upturn and, in some cases, divergent expectations regarding the monetary policy stance in the major currency areas. The temporary rise in uncertainty did not do any lasting damage to sentiment in financial markets, however, and receded again fairly quickly. The threat of a trade dispute between the major currency areas had only a fleeting and fairly isolated impact on individual market segments, but still remains a risk. At the beginning of February, the sharp increase in interest rates observed since the start of the year sent equity markets distinctly lower; for the most part, however, this was largely regarded as a correction warranted by the fundamentals. Furthermore, it was at this time that the sentiment indicators began to portend a continued very substantial rate of growth for the United States and China and a slightly slower pace for the euro area and Japan. This slight overall divergence in the growth outlook was also reflected in market participants' monetary policy expectations. While the turbulence that emerged in February did nothing to shake their conviction that the Federal Reserve would stick to gradually normalising policy over the course of the year, expectations of when the first euro area interest rate hike would take place were shifted back to mid-2019. This widened the interest rate differential between US Treasuries and German Bunds across the entire maturity spectrum, taking the differential between ten-year US Treasuries and German Bunds with the same maturity to more than 250 basis points at last count. International equity markets saw bouts of strong volatility, but registered price gains on balance in the United States and the euro area. Measured in terms of the equity risk premium, investors are slightly less willing to invest in US enterprises (having been very keen to do so at the beginning of the year) and are displaying a slightly greater propensity to invest in euro area stocks. In the foreign exchange markets, the euro relinquished the gains it had run up against the US dollar in January by the end of the period under review.

Exchange rates

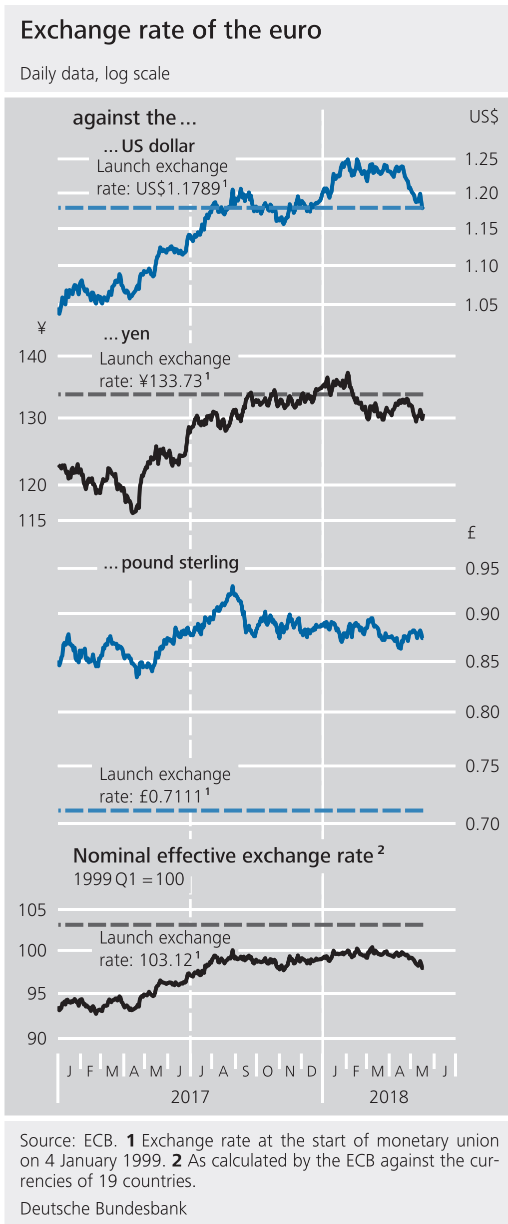
Low volatility in major foreign exchange rates

In the past few months, the foreign exchange markets, unlike the equity markets, have seen fairly little volatility in terms of the exchange rates between the major currencies. For example, the implied volatility of the EUR/USD currency pair, calculated from currency options with a maturity of three months, has stood at 7.2% on average since the beginning of the year, which is considerably lower than its long-term average of 10.2% since the introduction of the euro. The historical volatility for the EUR/USD exchange rate is currently very low, too, even though, in January, the euro continued to appreciate distinctly against the US dollar, reaching its highest level for more than three years in mid-February at US$1.25.

After a strong start to the year …

… euro depreciates against US dollar in the second half of February

However, in the second half of February, the euro surrendered some of these gains when, just a few days after the adoption of the US budget, which involved plans to increase net new borrowing in the market, debate about the risk of the US economy overheating intensified. One specific reason for this was the publication of higher-than-expected inflation figures from the United States, which was then followed by surprisingly positive leading indicators (eg for consumer confidence). Many market participants thus began to adjust their expectations towards a more rapid policy rate increase in the United States, which benefited the US dollar. Their confidence in these expectations was reinforced by optimistic comments made by the new Chairman of the Federal Open Market Committee (FOMC) about eco-



Source: ECB. **1** Exchange rate at the start of monetary union on 4 January 1999. **2** As calculated by the ECB against the currencies of 19 countries.
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nomic developments in the United States as well as the minutes of the FOMC meeting, which had already been published prior to this and which indicated the growing likelihood that further gradual increases would be warranted. On this side of the Atlantic, unexpectedly weak inflation and economic data from the euro area and Germany helped push the euro down to US$1.22.

A countermovement at the beginning of March …

At the beginning of March, the euro appreciated again after the President of the United States announced the imposition of protective tariffs on steel and aluminium imports. Even if higher import tariffs per se tend to improve a country's trade balance, thus potentially exerting upward pressure on its currency, in this case, market participants' concerns about increasing protectionism in the United States, possible countermeasures by trading partners and, ultimately, an impairment of the economic outlook for the US, seem to have predominated.

… was followed by further losses in the value of the euro from the end of April

For the next month and a half, the euro hovered fairly evenly at a level of around US $1.23 to US $1.24. This changed only towards the end of April when a series of surprisingly positive economic data was reported from the United States in areas such as retail sales, industrial production, capacity utilisation and data from the construction sector. Ultimately, the first estimate of economic growth in the United States in the first quarter of 2018 was also more favourable than projected on average. Prior to this, a further increase in consumer price inflation and the minutes of another FOMC meeting had already been published, which indicated that a steeper rise in policy rates than previously expected is likely to be appropriate for the next few years. All this put the euro under renewed downward pressure against the US dollar. In the first half of May, this was compounded by surprisingly weak economic data from the euro area. For instance, not only was euro area consumer price inflation lower than expected; retail sales and the Purchasing Managers' Index for the euro area as a whole as well as growth figures for Germany were also disappointing. As a result, the euro most recently stood at US$1.18, which was 1.6% down on its level at the beginning of the year.

Euro depreciates against yen …

In the second half of February, the euro continued to depreciate against the yen as it had done since the start of the month, prompted by corrections in the global stock markets and the uncertainty that ensued. In mid-February, this price movement gained fresh momentum when the Japanese finance minister announced that the appreciation of the yen did not mean that special intervention was needed. In addition to this, a surprisingly strong increase in

Japanese exports was reported for January. However, the euro-yen exchange rate stabilised at the beginning of March when the Japanese central bank stressed that it would continue its current policy of quantitative and qualitative easing. Afterwards, this currency pair showed no lasting price change until, at the beginning of May, the abovementioned data published for the euro area placed the euro under strain. At the end of the reporting period, this left the euro at ¥131, which was 3.2% lower than at the beginning of the year.

… and against pound sterling

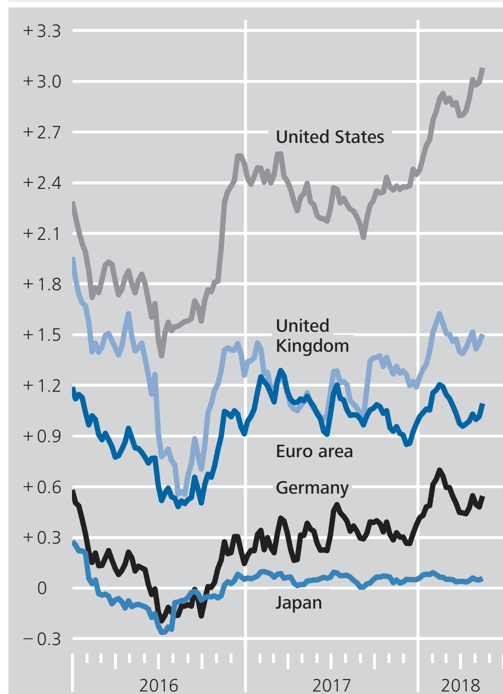
Following small fluctuations in the exchange rate between the euro and the pound sterling in the first part of the reporting period, the euro began to depreciate markedly as of mid-March. This was due, above all, to an agreement regarding transitional arrangements for the period after the planned withdrawal of the United Kingdom from the European Union, which, in the eyes of the market, improved the UK's economic prospects. However, mid-April brought news of an unexpected drop in UK consumer price inflation, which prompted some market participants to lower their expectations of future policy rate hikes. This temporarily benefited the euro, as did the subsequent publication of surprisingly weak growth in the British economy in the first quarter. Most recently, the euro stood at £0.88, which was 1.5% lower than at the beginning of the year.

Effective euro weaker on balance since beginning of the year

On a weighted average against 19 major trading partners, the euro depreciated on balance (-1.1%). The losses against the currencies mentioned above and the renminbi (-3.7%) were partly offset by marked price gains vis-à-vis the Swedish krona in particular (+4.6%). The euro temporarily reached its highest level against the krona in more than eight years. The main reason for the weakness of the krona was the continuation of the extremely expansionary monetary policy by the Swedish central bank, which disappointed some market participants' expectations of a tightening of policy. Outside the group of 19 partner currencies, the euro also recorded marked gains against the Argentine peso (+28.0%) and the Turkish lira (+15.5%).

Yields* in the euro area and selected countries

% pa, weekly averages



Source: Bloomberg. * Government bonds with a residual maturity of ten years.
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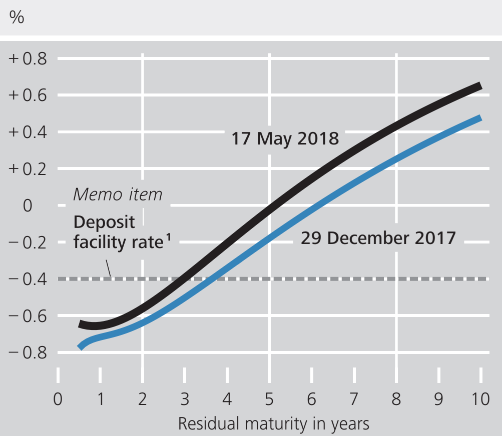
Securities markets and portfolio transactions

Mixed developments in the bond markets

Buoyed by market participants' confidence with respect to global economic activity at the beginning of the year, bond markets on both sides of the Atlantic also experienced a sharp rise in yields at first. As already mentioned, in the first half of February, expectations about future economic developments and the future monetary policy stance of both major currency areas then began to diverge somewhat more strongly, which was also reflected in different return patterns. For the first time since 2014, yields on ten-year US Treasuries temporarily rose to more than 3% (+72 basis points since the end of 2017) and also exceeded this figure as this report went to press. The fact that, according to estimates by the Congressional

Yield curve on the German bond market*

%



* Interest rates for (hypothetical) zero-coupon bonds (Svensson method), based on listed Federal securities. 1 Current interest rate on the deposit facility in place since 15 March 2016.

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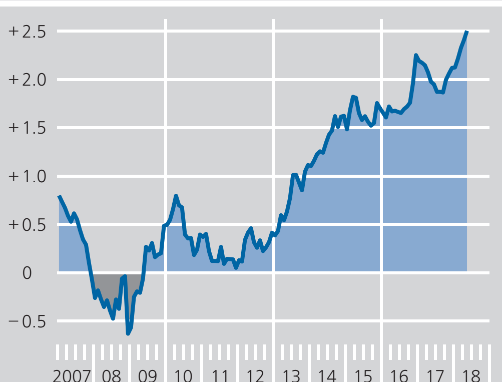
Budget Office (CBO), US government debt could grow considerably as a result of the tax reform probably also placed the price of US securities under strain.

Given the Eurosystem's continued accommodative monetary policy and the weaker economic data from Germany, yields on ten-year Bunds fell to 0.6% from mid-February after having climbed sharply at the beginning of the year. Compared to the yield level at the end of 2017, on the other hand, this represented an increase of 18 basis points.

Yield spread between US and German government bonds*

Percentage points, monthly data



1 Source: Bloomberg. * US Treasury yields less Bunds, each with a residual maturity of ten years.

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Term premiums up, especially in the United States

As a result, the yield spread between ten-year US Treasuries and ten-year German Bunds grew by 51 basis points to 250 basis points at last count – the highest level for the last 30 years. The uneven rise in interest rates on each side of the Atlantic is mainly due to differences in the growth of the term premiums, which are the premiums that remunerate investors' willingness to hold securities with longer residual maturities. This premium has risen sharply in the United States since the end of 2017 (+29 basis points); by contrast, it has climbed by a mere 6 basis points for German Bunds.[1]

Yield curve shifted upwards

While money market participants expected Eurosystem rate increases to start at a later date, the yield curve derived from yields on Federal securities shifted upwards somewhat and steepened slightly. With regard to unconventional monetary policy measures, this upward shift demonstrates that expectations of a normalisation have risen. The spread between ten-year and two-year bonds widened by 10 basis points. The yield spread between EONIA swaps and Bunds with an equivalent maturity narrowed further. This suggests that market participants perceive there to be fewer scarcity problems with regard to Federal securities until the Eurosystem's asset purchase programmes are potentially phased out.

Yield spreads in the euro area mostly narrower

At last report, the GDP-weighted yield on ten-year government bonds in the euro area was 13 basis points higher than at the start of the year. This reflected the countervailing trends of rising yields on ten-year Bunds and falling interest rates on ten-year government bonds issued by other euro area countries. The GDP-weighted average of yield spreads over Bunds has therefore fallen by 11 basis points to 70 basis points since the beginning of the year. Spreads on Spanish and Portuguese government bonds narrowed, in particular, doing so by more than 35 basis points each. The con-

1 At the same time, short-term interest rate expectations for the next ten years have gone up more sharply in the United States than in the euro area, reflecting increasingly different monetary policy stances.

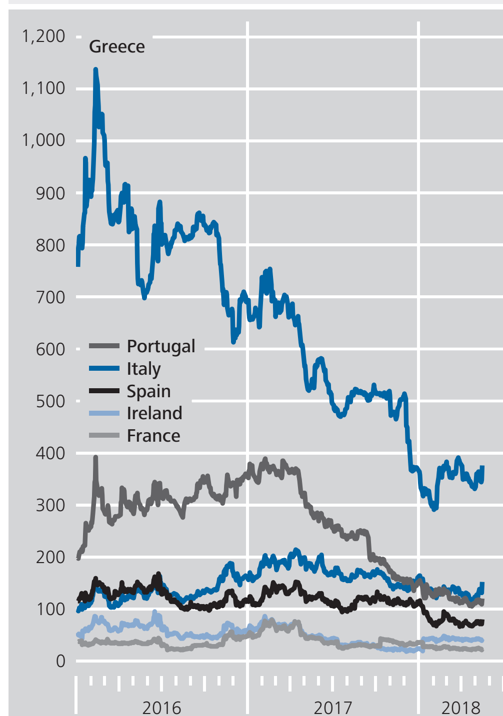
tinuing upward trend in economic activity in the euro area and ratings upgrades may have played a role here. Although the yield spread on ten-year Italian government bonds also decreased considerably for a time, plans by the potential new coalition government in Italy to lower taxes whilst ramping up public spending then led to a marked increase in spreads.

Yields up in the United Kingdom and largely unchanged in Japan

In the United Kingdom, yields have also gone up significantly since the beginning of the year. Ten-year gilts increased by 38 basis points to 1.6%. After the Bank of England raised its policy rates last November, market participants' expectations are currently fairly evenly split between a further interest rate hike and an unaltered interest rate level. In Japan, yields moved within a narrow corridor and, on balance, remained virtually unchanged at 0.06%. Yields on Japanese government bonds are still being heavily influenced by the Bank of Japan's yield curve control programme, which aims to maintain the yield on ten-year government bonds at close to 0%.

Spreads of ten-year government bonds over German Federal bonds

Basis points, daily data



Sources: Bloomberg and Bundesbank calculations.
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Forward inflation rates remain almost unchanged

The five-year forward inflation rates in five years derived from inflation swaps fluctuated only slightly by 1.7%. Currently standing at 1.9%, the inflation expectations for the euro area six to ten years ahead, as computed by Consensus Economics on the basis of surveys, likewise remained virtually unchanged. Hence, the difference between market-based and survey-based inflation expectations for the euro area continued to be negative. When interpreting the discrepancy between survey-based and market-based expectations, however, it is necessary to bear in mind possible liquidity and, above all, inflation risk premiums which can affect market-based measures. The probability of deflation over the next five years based on options data remained close to its level in January 2018, and thus at its lowest point since the end of 2009, the time when option quotations began to be available.

European corporate bond yields increase

Yields on European corporate bonds have increased since the beginning of the year, having started at very low levels. Bonds issued by financial corporations with a BBB rating and a residual maturity of seven to ten years were yielding 2.4% as this report went to press, 50 basis points up from the beginning of the year. Meanwhile, yields on non-financial corporate bonds with the same maturity were up by 1.8%, an increase of 33 basis points. The yield spreads of non-financial and financial corporate bonds over Bunds also went up on balance, rising by 29 basis points and 12 basis points respectively. For a while however (in early February), yield spreads in both corporate sectors hovered at veritably low levels of a kind not seen since before the onset of the financial crisis in July 2007. Against this background, the financing conditions for European enterprises should still be categorised as favourable, with the market conditions for corporate bonds still having been influenced by the prevailing accommodative monetary policy and the corporate sector purchase programme.

Investment activity in the German securities markets

€ billion

Item	2017 Q1	2017 Q4	2018 Q1
Debt securities			
Residents	59.5	38.8	40.6
Credit institutions	– 20.8	– 13.5	– 1.9
of which			
Foreign debt securities	– 10.1	– 0.3	3.3
Deutsche Bundesbank	52.6	35.6	19.1
Other sectors	27.6	16.7	23.4
of which			
Domestic debt securities	13.5	11.9	4.5
Non-residents	– 22.2	– 42.9	5.0
Shares			
Residents	18.6	19.2	18.2
Credit institutions	2.1	4.8	– 6.5
of which			
Domestic shares	– 0.1	2.9	– 3.9
Non-banks	16.4	14.4	24.7
of which			
Domestic shares	8.0	– 1.7	1.9
Non-residents	3.3	0.0	4.3
Mutual fund shares			
Investment in specialised funds	21.4	24.1	25.4
Investment in open-end funds	7.9	5.2	6.9
of which			
Equity funds	1.4	0.8	0.2

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Net sales in the bond market up

Gross issuance in the German bond market stood at €298½ billion in the first quarter of 2018, well up on the figure for the previous quarter (€240½ billion). After deducting redemptions and taking account of changes in issuers' holdings of their own bonds, net issuance came to €20 billion. In addition, foreign borrowers placed debt securities worth €25½ billion in the German market. Funds totalling €45½ billion net were consequently raised in the German bond market in the reporting period.

Significant rise in credit institutions' capital market debt

Domestic credit institutions issued new bonds totalling €25 billion net in the first quarter of 2018. Debt securities of specialised credit institutions (€21½ billion) constituted the lion's share of issues, followed on a smaller scale by mortgage Pfandbriefe (€5 billion). This contrasted with net redemptions of other bank debt securities that can be structured flexibly (€1 billion).

Net issuance of corporate bonds

In the quarter under review, domestic enterprises issued debt securities worth €3½ billion net. On balance, the vast majority of these were bonds with maturities of less than one year. Viewed in net terms, the issues were attributable solely to other financial intermediaries, while non-financial corporations redeemed bonds on balance.

Public sector capital market debt down

The public sector took advantage of the favourable fiscal situation and pared back its capital market debt by €8½ billion net in the first quarter of 2018. These figures include issues by resolution agencies set up for German banks, which are ascribed to the public sector for statistical purposes. Central government itself principally redeemed five-year Federal notes (Bobls; €10 billion) and Treasury discount paper (Bubills; €1 billion). This contrasted with net issuance of 10 and 30-year Federal bonds (Bunds) totalling €4 billion and €5½ billion respectively, as well as two-year Federal Treasury notes (Schätze) in the amount of €3 billion. In the quarter under review, state and local governments redeemed their own bonds to the tune of €10 billion net.

Purchases of debt securities

In the first quarter of 2018, domestic nonbanks, including mutual funds, were the principal buyers on the bond market; they added instruments worth €23½ billion to their portfolios, most of this paper being foreign. For its part, the Bundesbank added a net €19 billion worth of paper to its balance sheet, mainly under the Eurosystem's asset purchase programmes (compared with €35½ billion in the fourth quarter of 2017). This primarily entailed domestic public sector instruments. The lower quarter-on-quarter amounts reflect the reduced volume of monthly asset purchases that has been in evidence since the beginning of the year. Non-resident investors acquired bonds to the tune of €5 billion net, while domestic credit institutions parted with debt securities worth €2 billion net.

Equity market

Signs of stock market recovery following temporary slump

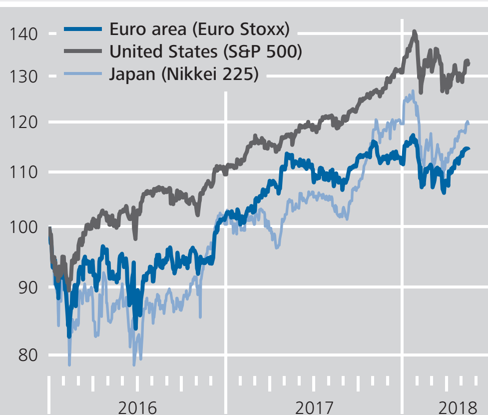
In the period under review, the international stock markets were influenced by a temporary spike in market uncertainty. During the first half of February, there was a worldwide dip in prices on the stock markets, compounded by heightened uncertainty, as measured by the implied volatility of equity indices calculated on the basis of options. This emanated from growing expectations that the Federal Reserve might raise interest rates sooner than previously anticipated and culminated in a sharp correction to the equity market. Over the months that followed, however, stock market investors' uncertainty about future price developments petered out. Their sense of uncertainty is still above its level at the beginning of the year, not least in the United States, but well below its level recorded in early February, which was the highest for several years. The higher volatility is partly attributable to the fact that predictions regarding the extent of trade disputes between the US and a number of other countries have varied, depending on individual news reports, thus fuelling uncertainty. Overall, prices listed on the broad equity indices listed for the United States and the euro area hovered around their current levels during the reporting period. The Euro Stoxx (+3.1%) performed slightly better than the S&P 500 (+1.7%), although the economic sentiment indicators for the euro area have recently worsened, down from their previously high level. The German equity market – as measured by the CDAX price index – was trading only slightly above levels at the beginning of 2018 (+0.2%), chiefly on account of the negative trajectory of bank shares.

Sectoral prices affected by higher oil prices and concerns about trade disputes

While German banks suffered losses of more than 24%, Italian, Greek and Portuguese bank shares made above-average gains of 9%, 3% and 11% respectively. Moreover, at the European level, energy companies, in particular, performed considerably better than the market as a whole during the period under review (+17.2%), mainly on the back of the recent sharp increase in the price of oil. By contrast, enterprises engaged in the steel industry – prompted by the US administration's threat that it might also impose tariffs on transatlantic trade – lost value compared with the beginning of the year, after delivering above-average performances in the final quarter of 2017.

Equity market

Beginning of 2016 = 100, log scale, daily data



Sources: Bloomberg, Thomson Reuters and Bundesbank calculations.
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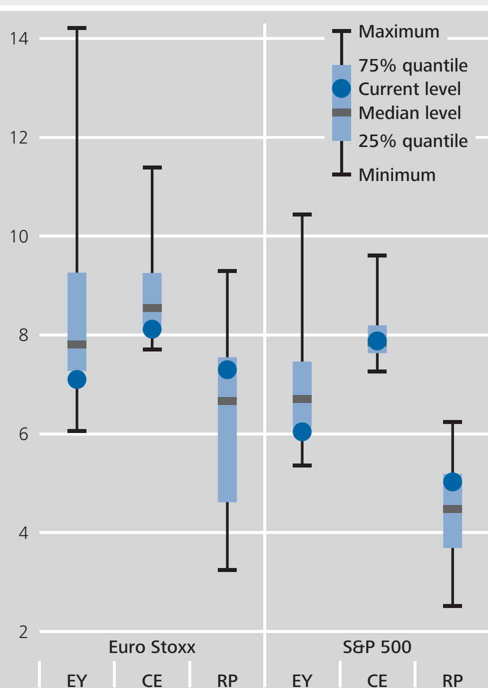
Stock market valuations

Data since January 2004



Sources: Thomson Reuters I/B/E/S, Bundesbank calculations. Earnings yields (EY) shown as an inverted price/earnings ratio; implied cost of equity (CE) and equity risk premium (RP) derived from the dividend discount model.
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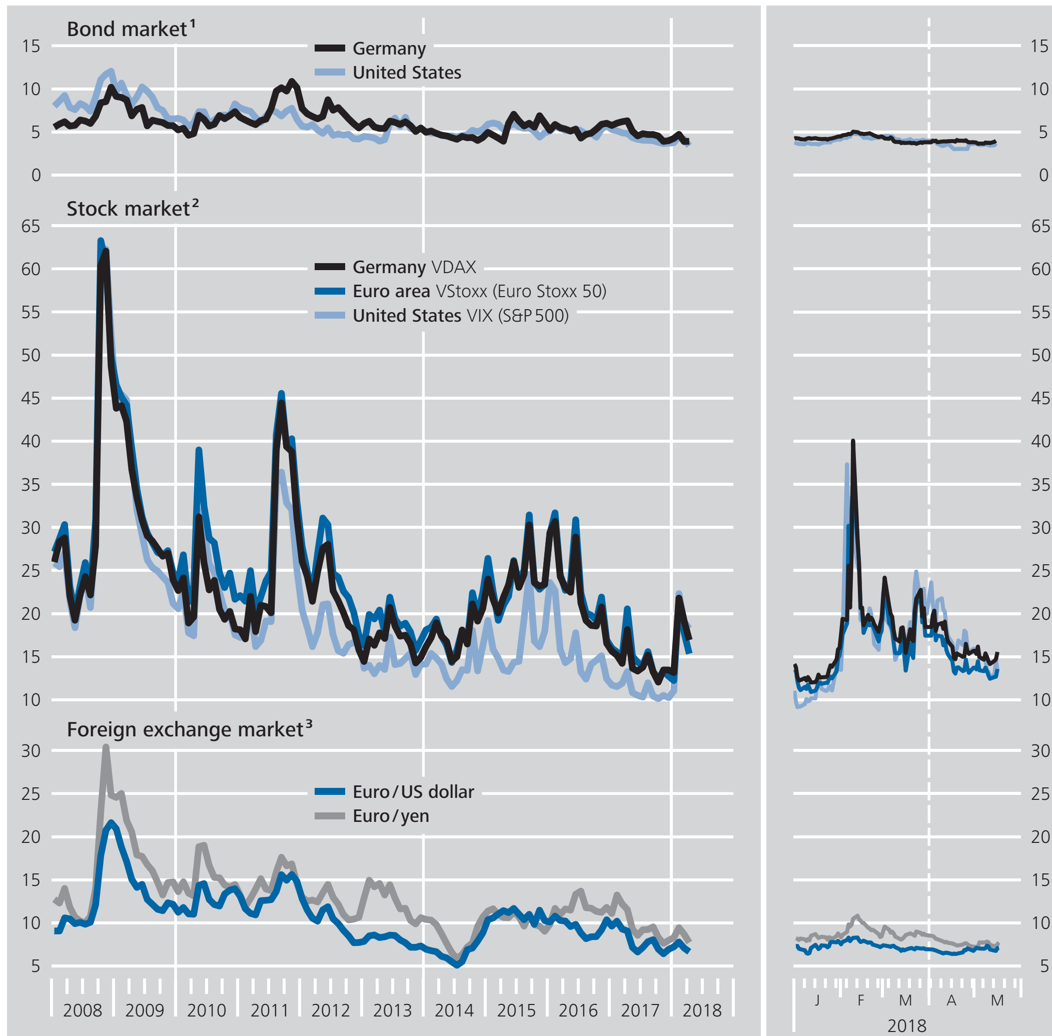

1 Implied volatility of options on the Bund future (Germany) or T-Note Future (USA) for a three-month horizon. 2 Calculated using the prices of index options with a maturity of 30 days. 3 Implied volatility of currency options with a maturity of three months.
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Slight price gains in the Japanese and UK equity markets

The Japanese and UK equity markets recently recouped the temporary losses sustained previously. On balance, the Nikkei 225 rose by 0.3%, having in the interim peaked at its highest level since 1991 before embarking on a sharp decline. The broad FTSE All-Share Index also saw gains (+1.3%).

Divergent earnings revisions

While estimates by IBES analysts of European enterprises' earnings in the year ahead were revised upwards, their estimates relating to medium-term earnings growth were revised downwards. Taking into account interest rate and share price movements, the equity risk premium, which arises from a multi-stage dividend discount model, fell slightly, indicating an increased valuation level. Conversely, during the reporting period, analysts substantially raised their projections regarding the future earnings trajectory of US enterprises, both for the short and medium term. These revisions to projected earnings in the US probably stem largely from the tax relief that companies can expect as a result of the US tax reforms adopted at the end of 2017. This is also reflected in the significant increase in profits experienced by enterprises belonging to the S&P 500 in the first quarter. Amid a sharp increase in interest rates and higher share prices overall, the equity risk premium applying to US enterprises only went up

slightly on balance. By this yardstick, US share prices remain at a high level, despite the lower price-earnings ratio.

Stock market funding and stock purchases

Issuing activity in the German equity market was moderate in the first quarter of 2018. Domestic enterprises issued €2½ billion worth of new shares in net terms. The outstanding volume of foreign shares in the German market rose by €20 billion over the same period. In the main, equities were purchased by German non-banks (€24½ billion) while non-resident investors bought shares worth €4½ billion net, and domestic credit institutions pared back their holdings by €6½ billion net.

Sales and purchases of mutual fund shares

During the reporting period, domestic investment companies recorded inflows of €32½ billion, after raising funds totalling €29½ billion in the previous three months. The fresh cash mainly accrued to specialised funds reserved for institutional investors (€25½ billion). Among the various asset classes, mixed securities funds were the chief sellers of new fund shares (€17 billion) but open-end real estate funds (€4 billion), funds of funds (€3½ billion), equity funds (€3 billion), and bond funds (€2½ billion) also engaged in sales, albeit to a lesser extent. Foreign funds operating in the German market attracted fresh funds totalling €8½ billion net in the first quarter of 2018. Domestic non-banks were the main buyers, adding mutual fund shares worth €41 billion to their portfolios. On balance, their focus was largely on German paper. Domestic credit institutions acquired mutual fund shares for €1½ billion net, while foreign investors scaled back their German fund portfolio by €2 billion net.

Direct investment

Direct investment sees capital exports

As with cross-border portfolio investment, which saw net outflows amounting to €35 billion in the first quarter of 2018, net capital exports were likewise recorded in the field of direct investment, where they came to €19½ billion.

Major items of the balance of payments

€ billion

Item	2017		2018
	Q1	Q4	Q1p
I Current account	+ 68.0	+ 75.3	+ 71.1
1 Goods[1]	+ 66.0	+ 64.2	+ 66.1
2 Services[2]	− 2.5	+ 0.4	− 0.7
3 Primary income	+ 21.3	+ 25.1	+ 19.9
4 Secondary income	− 16.8	− 14.5	− 14.2
II Capital account	+ 0.6	− 1.0	+ 0.1
III Financial account (increase: +)	+ 67.3	+ 81.4	+ 60.4
1 Direct investment	+ 15.2	+ 15.3	+ 19.7
Domestic investment abroad	+ 44.6	+ 27.4	+ 39.9
Foreign investment in the reporting country	+ 29.4	+ 12.0	+ 20.2
2 Portfolio investment	+ 51.6	+ 69.9	+ 34.9
Domestic investment in foreign securities	+ 31.4	+ 23.3	+ 42.4
Shares[3]	+ 5.6	+ 5.7	+ 8.2
Investment fund shares[4]	+ 17.6	+ 14.7	+ 8.6
of which Money market fund shares	+ 6.3	+ 1.8	− 1.1
Long-term debt securities[5]	+ 5.0	+ 7.6	+ 25.6
of which Denominated in euro[6]	+ 5.8	+ 4.3	+ 24.2
Short-term debt securities[7]	+ 3.2	− 4.7	0.0
Foreign investment in domestic securities	− 20.2	− 46.6	+ 7.5
Shares[3]	+ 1.9	− 0.8	+ 4.3
Investment fund shares	+ 0.1	− 2.9	− 1.8
Long-term debt securities[5]	− 12.1	− 40.4	+ 16.4
of which Issued by the public sector[8]	− 21.5	− 22.6	− 1.9
Short-term debt securities[7]	− 10.1	− 2.4	− 11.5
3 Financial derivatives[9]	+ 0.2	+ 4.0	+ 1.1
4 Other investment[10]	+ 0.7	− 6.5	+ 3.9
Monetary financial institutions[11]	− 35.2	+ 16.8	− 4.0
Enterprises and households[12]	− 7.7	− 17.0	+ 16.3
General government	− 2.2	+ 13.2	− 2.5
Bundesbank	+ 45.8	− 19.4	− 5.8
5 Reserve assets	− 0.4	− 1.4	+ 0.7
IV Errors and omissions[13]	− 1.3	+ 7.2	− 10.8

1 Excluding freight and insurance costs of foreign trade. **2** Including freight and insurance costs of foreign trade. **3** Including participation certificates. **4** Including reinvested earnings. **5** Long-term: original maturity of more than one year or unlimited. **6** Including outstanding foreign D-Mark bonds. **7** Short-term: original maturity up to one year. **8** Including bonds issued by the former Federal Railways, the former Federal Post Office and the former Treuhand agency. **9** Balance of transactions arising from options and financial futures contracts as well as employee stock options. **10** Includes in particular financial and trade credits as well as currency and deposits. **11** Excluding the Bundesbank. **12** Includes the following sectors: financial corporations (excluding monetary financial institutions) as well as non-financial corporations, households and non-profit institutions serving households. **13** Statistical errors and omissions, resulting from the difference between the balance on the financial account and the balances on the current account and the capital account.

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German direct investment abroad

Direct investment abroad by German enterprises totalled €40 billion net in the first three months of 2018. Domestic investors boosted their equity capital by €33 billion, with a clear emphasis on investment in equity capital in the narrower sense, with foreign earnings being reinvested as well. German enterprises also expanded their intra-group lending in the period under review (+€7 billion). Countries receiving substantial direct investments from Germany included the Netherlands (€4 billion) and Ireland (€2½ billion) within the euro area, as well as the United States (€11½ billion) and China (€4½ billion) beyond it.

Foreign direct investment in Germany

Foreign investors also increased their direct investment in Germany from January to March 2018 by €20 billion, mainly by means of intra-group credit transactions (€16½ billion). The number of financial credits saw a particular increase, facilitated by reverse flows which allow foreign subsidiaries to channel funds to their parent companies in Germany[2], whereas intra-group trade credits were mainly redeemed. On top of this, foreign investors also bolstered their equity stakes in German subsidiaries (€3½ billion), primarily by reinvesting net earnings. In regional terms, investors from the euro area, particularly from the Netherlands (€10½ billion) and Luxembourg (€5 billion), played a major role.

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2 Since the last set of methodological adjustments were made, these loans flowing in the opposite direction to the equity capital have been recorded in accordance with the "asset/liability principle" pursuant to the sixth edition of the IMF's Balance of Payments and International Investment Position Manual (BPM6). They are therefore classified as direct investment from the country in which the subsidiary is resident to the country in which the parent company is located. For a description of these and other data recording principles applying to the balance of payments and the international investment position, see Deutsche Bundesbank, Changes in the methodology and classifications of the balance of payments and the international investment position, Monthly Report, June 2014, pp 57-68.