

BANK FOR INTERNATIONAL SETTLEMENTS

THIRTY-FOURTH ANNUAL REPORT

1st APRIL 1963 — 31st MARCH 1964

BASLE

8th June 1964

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THIRTY-FOURTH ANNUAL REPORT

submitted to the

ANNUAL GENERAL MEETING

of the

BANK FOR INTERNATIONAL SETTLEMENTS

held in

Basle on 8th June 1964.

Gentlemen,

I have the honour to submit herewith the Annual Report of the Bank for International Settlements for the thirty-fourth financial year, which began on 1st April 1963 and ended on 31st March 1964. Details of the results of the year's business operations are given in Part III, together with an analysis of the balance sheet as at 31st March 1964.

The accounts for the thirty-fourth financial year closed with a surplus of 27,417,055 gold francs, against 21,210,271 gold francs for the previous year. After the writing-off of the cost of a building purchased during the year and the deduction of 2,000,000 gold francs transferred to the provision for exceptional costs of administration and of 7,500,000 gold francs transferred to the provision for contingencies, the net profit amounted to 17,517,055 gold francs, compared with 13,710,271 gold francs for the preceding year.

The Board of Directors recommends that the present General Meeting should decide to distribute, as last year, a dividend of 37.50 gold francs per share. The Board also proposes that, as an exceptional measure, a lump sum should be applied to the reduction of the amount of the undeclared cumulative dividend. This sum, which has been fixed at 8,500,000 gold francs, will represent an extraordinary distribution of 42.50 gold francs per share. The total distribution will thus amount this year to 80 gold francs, payable in Swiss francs in the amount of 114.30 Swiss francs per share.

Part I of this Report deals with economic developments and policies in Europe and the United States in 1963 and the early months of 1964. In

Part II a survey is given of developments in the fields of credit, prices, external payments and reserves and in the foreign exchange and Euro-currency markets; an outline is also given of the working of the European Monetary Agreement. Part III deals with the operations of the Bank and the functions it performs on behalf of the High Authority of the European Coal and Steel Community and as Trustee and Fiscal Agent for international loans.

The Bank has continued to co-operate with other international institutions.

PART I
CURRENT ECONOMIC TRENDS AND POLICIES
1963-64

Developments over the past twelve months have helped to resolve favourably some of the uncertainties about the economic situation which were still prominent a year ago.

The expansion of economic activity in the United States has been a vigorous one, without signs of the distortions or tensions of an unsound boom. As the stimulus to demand from the reduction in taxes is just beginning, the outlook for continued growth is favourable. But in addition there has been a major improvement in the balance of payments. While the near-balance of the external accounts in the first quarter of 1964 partly reflects temporary factors, it holds the promise that a sound external position can be restored in a reasonable time.

In the United Kingdom also, demand and output have moved ahead strongly, under the incentive of the measures taken a year ago. Although some steps have been initiated recently to keep the expansion in line with available resources, the prospects are for the growth of production to continue. While the balance-of-payments position is less favourable than it was a year ago, the situation should be manageable if the rise of incomes is kept within the limits set by incomes policy.

Another favourable aspect of the situation has been the improvement in the position of the less industrialised countries, brought about by increased demand for raw materials and some rise in their prices. Although the problems of economic development present innumerable difficulties, and the needs of these countries for outside capital and technical assistance remain as great as ever, the rise in export earnings should materially assist in making sound progress.

Following the signs that were evident a year ago, the trouble spot in the economic picture shifted to continental western Europe during the past twelve months. This has not been because demand and economic expansion have faltered but rather because excessive demand has produced inevitable inflationary consequences. The situation has been aggravated in some countries by very large negotiated wage increases, but more broadly it reflects a general pressure of demand on available resources. The result has been rising prices in most countries and a serious balance-of-payments deficit in one. Under the circumstances, economic and financial policy has definitely been turned to restraint. While some favourable results have been achieved, the situation has not yet been brought fully under control. It is, however, a hopeful sign that the Council of Ministers of the European Economic Community agreed in April 1964 on a co-ordinated anti-inflationary policy.

Developments in western Europe.

Output and demand. While the rate of economic expansion was fairly similar among most countries in western Europe in the past year, the cyclical situation was quite different on the Continent from that in the United Kingdom. For the United Kingdom it was the first year of a new expansionary movement. As the rise in total demand quickened it could be met in the main by higher output. Clearly, the margin for expansion was less by the spring of 1964 than a year before, but the situation still remains free of significant distortions.

Industrial production.¹

Countries	1962				1963				1964
	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter
adjusted quarterly changes, in percentages									
Austria	+ 1.6	— 1.6	+ 2.1	0.0	+ 1.6	+ 1.5	+ 1.5	+ 3.0	+ 3.4 ²
Belgium	+ 0.1	+ 2.0	+ 1.8	— 0.3	— 0.8	+ 7.3	— 0.5	+ 2.4	+ 1.1
France	+ 2.1	+ 1.2	+ 1.4	+ 1.0	— 3.6	+ 7.6	— 0.6	+ 4.5	+ 1.6
Germany	+ 0.4	+ 3.0	+ 1.1	+ 0.4	— 0.7	+ 3.2	+ 0.7	+ 1.7	+ 4.8
Italy	+ 2.0	0.0	+ 0.1	+ 4.5	+ 1.2	+ 4.7	— 1.5	+ 4.7	— 0.6
Netherlands	0.0	— 2.3	+ 1.6	+ 5.3	— 2.2	+ 1.5	0.0	+ 7.3	+ 1.0
Norway	— 1.2	+ 2.4	0.0	+ 2.4	+ 0.6	+ 1.7	+ 2.3	+ 2.2	— 0.5
Sweden	+ 0.7	+ 2.1	+ 1.0	— 1.3	— 1.4	+ 4.5	— 0.7	+ 2.0	+ 2.3
United Kingdom	+ 0.9	+ 0.9	+ 0.9	— 1.7	— 0.9	+ 4.4	+ 1.7	+ 3.3	+ 2.4

¹ Excluding construction. ² January-February.

For continental Europe, on the other hand, it was the fifth year of an expansion which had got under way early in 1959. By this time a year ago the margin of available labour and capacity was already negligible and the general situation was one of demand outrunning supply. This imbalance was accentuated over the past year and turned policy in many of the countries to corrective action.

In most respects the development of output and the pattern of demand in the past year were similar to those in 1962. Aggregate gross national product rose less than in 1962 — 3.9 per cent. as against 4.9 per cent. — reflecting the fuller use of resources and the severe winter of 1962-63. Among the individual countries growth was larger than in 1962 only in Austria, the Netherlands, Finland and Norway; in Sweden and Belgium it was about the same, while in the other countries it declined. Thus, after the peak of 7.5 per cent. in 1960, the rate of expansion on the Continent steadily fell. This movement was reversed to some extent in late 1963 and early 1964, however, as output picked up in several countries.

As to the increase of total demand, private consumption has remained far and away the dominant factor. Not only has consumer-goods output risen under this stimulus but intra-European trade in such goods has leaped ahead and imports have been drawn in from the outside world. Durable consumer-goods output rose particularly sharply, as indicated by a 15 per cent. increase in the motor-car industry, while even the textile industry expanded by 5 per

cent. For the first time for several years exports to countries outside continental Europe showed a fairly marked gain. In addition, public-sector investment advanced more than the year before, but public consumption expenditure was generally a less active factor. Housing demand was strong in most countries but output expanded little because of supply limitations. Plant and equipment outlays were generally a less dynamic demand element, but in more recent months demand in this sector has been stronger and has led to a revival in the steel and machinery industries.

Thus the picture on the Continent has been one of expansion being maintained primarily by consumption demand.

Inflationary pressures. The European economy has been subject to severe tensions over the past year to a degree that has made inflation the key problem. This was manifested in rising prices at both the wholesale and the retail levels, large wage increases and soaring imports. If anything, the pressure was intensified in 1963-64, but at the same time it was more concentrated in particular countries than the year before.

In a few countries the situation in 1963 was relatively satisfactory. This was the case in the United Kingdom, Germany, Denmark, Sweden and Norway; for Germany and Denmark there was a clear lessening in the tensions of the preceding year. But more recently it has become evident that forces have been building up which could make reasonable monetary stability more difficult to maintain in the current year. The growth of aggregate demand picked up markedly towards the end of 1963, and in Germany and the United Kingdom — rather in contrast to developments elsewhere — there was a sharp recovery in industrial profits and prospects for increased industrial investment. In Germany this was associated with a large rise in the external surplus, whereas in the United Kingdom the balance of payments tended to deteriorate.

As to the focal points of European inflation in 1963, Italy was the most severe case, though the pressure was also quite strong in France, particularly up to the time measures were taken at the end of the summer. These countries had the largest increases in costs and prices as well as a very sizable deterioration in the external balance on current account. Inflationary pressure persisted in Switzerland, where the price rise tended to quicken and the current-account deficit grew further. In the Netherlands the tensions seemed to be held in check during most of 1963, but towards the year-end there was an inflationary eruption in the shape of a big negotiated wage increase. In several other countries also, such as Austria and Belgium, inflationary tendencies became more apparent during the year.

While the pressures have been unequal as between the various countries, the overall menace of inflation certainly seemed greater last year than in 1962. The continuation of rising prices and excessive wage increases for another year itself set up an inflationary psychology which tended to develop its own momentum. Besides this, the price rise of a year earlier was more concen-

Changes in the gross national product and its components,
at constant prices.

Countries	Years	Sources of demand						Resources	
		Consumption		Gross fixed domestic investment			Exports of goods and services	Imports of goods and services	Gross national product
		Private	Public	Total	of which in				
					plant and equipment	dwellings			
Austria	1961	4.9	1.1	6.3	6.3	6.6	7.5	4.2	4.8
	1962	5.2	2.2	— 2.0	— 2.8	1.9	7.4	9.3	1.5
	1963	5.1	5.2	1.5	1.0	3.6	8.8	4.0	4.4
Belgium.	1961	3.1	1.1	3.1	2.2	4.9	7.6	6.6	3.2
	1962	4.0	6.1	1.5	3.7	— 3.2	9.2	8.2	3.9
	1963	4.0	5.5	3.1	5.6	— 3.0	9.0	9.5	4.0
Denmark ¹	1961	6.9	7.1	11.4	10.2	18.3	4.1	4.5	5.4
	1962	6.6	7.1	7.8	8.1	5.8	5.5	13.1	4.9
	1963	0.1	5.6	— 2.5	— 2.4	— 2.9	11.1	0.0	1.8
Finland ¹	1961	7.3	8.1	9.9	8.0	17.0	6.0	8.2	7.6
	1962	3.8	6.9	— 0.4	— 4.3	13.2	7.0	5.9	3.1
	1963	2.9	7.1	1.0	— 2.4	12.1	0.6	— 2.6	3.8
France	1961	5.9	3.4	10.5	11.8	6.7	5.4	7.2	4.5
	1962	7.0	4.3	7.5	8.3	4.9	2.5	9.2	6.6
	1963	6.3	1.9	5.9	5.2	8.1	7.4	12.0	4.3
Germany	1961	6.9	8.2	9.4	10.7	4.6	3.3	7.7	5.4
	1962	5.8	11.9	5.5	6.4	2.2	4.2	11.4	4.2
	1963	2.7	6.3	1.8	2.0	1.4	9.8	8.3	3.2
Italy	1961	7.7	4.3	12.4	13.5	9.0	17.2	15.4	8.6
	1962	7.7	4.9	9.1	7.2	15.4	10.7	14.9	6.7
	1963	9.2	5.2	5.5	4.5	8.4	6.8	19.7	4.8
Netherlands . . .	1961	4.7	3.8	6.1	7.6	— 1.1	4.4	7.1	3.1
	1962	4.2	6.3	4.2	6.2	— 5.5	6.6	6.6	2.7
	1963	6.0	3.0	4.4	4.1	6.0	7.0	9.0	4.3
Norway ¹	1961	5.7	4.2	11.5	12.1	7.8	7.2	9.6	5.7
	1962	3.8	5.4	6.5	7.0	3.1	5.4	7.0	2.9
	1963	4.4	6.0	7.1	7.9	2.0	11.3	9.7	4.9
Sweden ¹	1961	5.0	3.6	6.9	6.3	8.9	4.5 ²	0.6 ³	5.6
	1962	3.7	8.0	4.5	3.6	7.4	6.4 ²	6.2 ³	3.6
	1963	4.2	5.3	5.3	5.2	5.8	6.9 ²	7.1 ³	3.7
Switzerland . . .	1961	9.6	4.0	24.0	29.2	12.0	7.2	20.6	9.1
	1962	6.5	12.2	12.4	17.6	— 1.5	5.7	9.7	6.1
	1963	5.4	9.6	2.6	3.0	1.2	4.3	5.6	4.2
Total for above countries . . .	1961	6.6	5.4	10.2	11.2	6.8	6.2	8.5	5.6
	1962	6.0	7.8	6.3	6.7	4.9	5.9	10.0	4.9
	1963	5.0	5.2	3.6	3.4	4.6	8.2	9.5	3.9
United Kingdom .	1961	2.1	4.0	8.7	9.3	6.0	1.7	— 1.0	3.0
	1962	1.7	2.7	— 1.1	— 1.9	2.6	2.6	1.8	0.8
	1963	3.8	3.1	1.3	1.2	1.9	4.6	3.7	3.6
United States . .	1961	1.8	5.0	— 0.4 ⁴	— 0.8	0.5	2.4	0.4	1.8
	1962	4.6	8.3	6.6 ⁴	5.8	9.0	5.9	8.2	6.1
	1963	3.6	3.9	4.6 ⁴	4.5	4.9	6.7	4.0	3.8

¹ In the case of Denmark, Finland, Norway and Sweden the official figures for domestic investment include maintenance and repairs; these are excluded from the above figures. ² Exports of goods and net income on services. ³ Imports of goods only. ⁴ Private investment and new civil public construction.

trated on foodstuffs, which in large measure reflected unusually adverse weather conditions; with increased agricultural imports and more favourable weather over the past year, however, this excuse has not been applicable. In addition, there has been a progressive upturn in world-market prices for a number of commodities over the past eighteen months which has begun to affect Europe's import bill for raw materials and tropical foodstuffs.

What, then, has been the fundamental cause of the continued inflationary pressures? In a period of full employment and rapidly growing incomes there is often a mixture of excessive demand and large negotiated wage increases which makes judgment difficult. In the present instance one might be tempted to put the major emphasis on the force of the wage-push in view of the fact that the strength of the business investment boom definitely weakened after 1961. There are, however, several signs that point to excess demand, sustained by excessive credit expansion and the balance-of-payments surplus, as the basic explanation. For one thing, the building sector has almost everywhere remained under intense demand pressure and a centre of the inflationary impulse through the competitive bidding-up of wages and prices. More generally, there has been extreme tightness on the labour market — with declining unemployment even in countries where its level was already minimal. Under such conditions excessive wage increases are to be expected, although the strong bargaining power of organised labour adds its own contribution to the size of the pay rise.

If one looks at individual countries, it would seem fair to say that continued pressure of demand was the basic inflationary factor in France, Switzerland, the Netherlands and Sweden. In Italy, however, the emphasis would appear to fall on wage-push, not only because investment demand weakened markedly in 1962 but also because the abruptly higher rate of wage increase at the start of 1963 cannot plausibly be ascribed to any sudden change in the Italian labour market. Of course, the large pay increases were themselves bound to have a major effect on demand. In addition, however, it may be said that in both Italy and the Netherlands the existence of a wage level appreciably below that of their partners in the Common Market may help to explain the large size of the wage rises in a period when labour has generally been in short supply and more than ever free to move.

A contributory factor in the development of inflationary pressures in the continental countries has been the substantial balance-of-payments surplus since 1958, with its counterpart until recently in the deficit of the United States. However, as there has often been inflation not caused by an external surplus and an external surplus not resulting in inflation, a causal relation between the two is not an inevitable one.

A direct relation may arise from a current-account surplus due to higher exports than imports, as this means an addition to aggregate demand (this may happen also as a result of direct foreign investment). If it occurs when the economy is fully employed, it contributes directly to inflationary pressures. This can be the case even if imports rise correspondingly, when the increase

in imports is being induced by the strain on productive resources emanating from export demand.

For continental Europe as a whole, the sharp rise in exports to outside areas occurred in 1959-60 and was an important factor in the renewal of expansion. At that time, however, productive resources were available to absorb the rising demand without inflationary pressures. As Europe's exports to outside areas ceased to expand after 1960, the emergence of inflation in 1962-63 cannot be attributed to the direct influence of the overall current-account surplus. In fact, the substantial deterioration of the current account over the past two years, due to growing imports, has been a factor absorbing excess demand and limiting the rise in prices. It is rather within Europe that inflation has been transmitted from one country to another in this period through the effect of excessive demand in some countries on the resources of others.

The other mechanism by which the balance-of-payments surplus may exert an expansionary influence on the domestic economy is mainly of an indirect nature, resulting from its effect in expanding internal monetary liquidity and reducing interest rates. This has been a continuous influence in the European economy since 1959, with the help of an inflow of capital, particularly of portfolio capital and transfers of liquid funds. But whether such an increase in liquidity leads in fact to demand pressure and inflationary tensions depends on the extent of potential demand seeking to be financed and on the extent to which the authorities can curb expansion of bank credit and offset the inflow of funds to the capital market. Demand conditions in Europe were ripe for this influence to play a rôle and in some cases the authorities, while wishing to exert counter-pressure, did not have adequate policy instruments to do this. In the main, however, the credit expansion in Europe has exceeded what can be attributed to the inevitable consequence of the external surplus. It must be said in addition that in some countries capital imports were part of official policy, while in some others there was more scope for offsetting the inflow by allowing bigger capital exports.

It is therefore principally through its influence on money and capital-market conditions, rather than by directly adding very much to aggregate demand, that Europe's continued external surplus has contributed to inflationary pressures. The surplus has been an obstacle to monetary restraint and has encouraged expansionary policies; given the growing tightness of the labour market, a resultant increase in inflationary tensions was just about inevitable. Of course, up to a point the expansionary policy contributed to reducing the disequilibrium in international payments; the danger comes in overshooting the mark.

Denmark. As in the 1953-57 boom, Denmark was the first country in the present period of expansion to experience severe inflationary pressures and to be forced to take strong restraining measures. And again the problem arose essentially because of excessive increases in incomes after a position of full use of resources had been reached and the rise in output was slowing down

owing to supply limitations. By early 1960 unemployment was already minimal and signs of tension were evident even earlier, though prices remained relatively stable. Then, in 1961, the situation was aggravated. After extensive strikes, a new two-year wage agreement was negotiated providing for an immediate 8 per cent. rise in industrial wages, which was augmented by subsequent wage drift and automatic cost-of-living increases. Civil servants' salaries were increased by 13-14 per cent. (after having remained unchanged for three years) and there was a re-alignment of agricultural incomes to keep pace with other earnings. In the two years 1961 and 1962 wages rose by about 25 per cent. There followed a sharp renewal of rising prices and a deterioration in the balance of payments.

Efforts to contain the pressures by monetary policy, with the discount rate being raised from 4.5 per cent. in 1959 to 6.5 per cent. in the spring of 1961, had been unavailing in the face of a rising budget deficit. By the middle of 1962 a situation of inflationary crisis had developed. The problem was dealt with by a series of restrictive fiscal and incomes measures enacted in August 1962 and March 1963.

The important features of the policy programme of the summer of 1962 were a general purchase tax of 9 per cent. (excluding food, fuel and services), a reduction in public and private building starts, the imposition of a ceiling on government expenditure and the exclusion of direct and indirect taxes from escalator-clause adjustments of wages.

Although these measures exerted a stabilising influence, the inflationary process had by this time gained such momentum that the necessity for additional measures soon became apparent. Hence in March 1963 legislation was enacted to limit average wage increases over the coming year to 1.25 per cent. and to 2.5 per cent. in the succeeding year, to prohibit an increase in dividends, to restrict subsidies to agriculture essentially to their 1962-63 level, to introduce a price/profits stop and to impose a compulsory savings scheme as an offset to a reduction in direct taxes previously provided for.

These measures were effective in restoring better balance. Price increases levelled off in the second quarter of 1963 and, notwithstanding the lifting of the freeze in October, prices have since remained almost stable. Imports in 1963 remained at their 1962 level, while rising exports helped to eliminate the deficit on current account. These gains have necessitated a marked slow-down in gross investment, but the notable thing is that full employment has been maintained and total output was almost 2 per cent. higher in 1963 than in 1962.

The easing of the inflationary pressures permitted a lowering of the discount rate to 6 per cent. in August and to 5.5 per cent. in November 1963. More recently there have been signs of a larger increase in demand. In January 1964 the Nationalbank warned the banks against over-expansion of credit, while in February the government raised taxes on cigarettes, beer and petrol and decided to postpone all new public-sector building starts until 1st September of this year.

Italy. Early in 1962 the growth of the Italian economy had begun to level off somewhat and, with the balance of payments and external reserve position favourable, the authorities considered a shift to more expansionary fiscal and monetary policies appropriate. Industrial output did, indeed, continue to rise at an annual rate of around 9 per cent. throughout 1963. But at the same time inflationary tensions of unexpected severity emerged and obliged the authorities increasingly to turn to measures of restraint.

The main thing which upset official calculations as to the likely course of the economy was the wage eruption that came towards the end of 1962. Partly this arose out of a general feeling that, in view of the rapid growth of output and somewhat slower trend of wages over the preceding three years, the time was ripe for an extraordinary, once-for-all increase in workers' incomes. Partly also it was encouraged by the steady absorption of manpower reserves, unemployment being brought down to about 2 per cent. of the labour force in 1963. Be that as it may, wages in industry, agriculture and the public service have been rising at a rate of 15 per cent. or more per annum — three times as fast as productivity — for at least eighteen months.

The effects of such increases on labour costs and on consumer demand could not fail to be reflected in both prices and the balance of payments. Consumer prices have been rising by some 8 per cent. per annum and wholesale prices by 5.5 per cent. In 1963 the current balance of payments showed a deficit of \$900 million, compared with a \$250 million surplus in 1962.

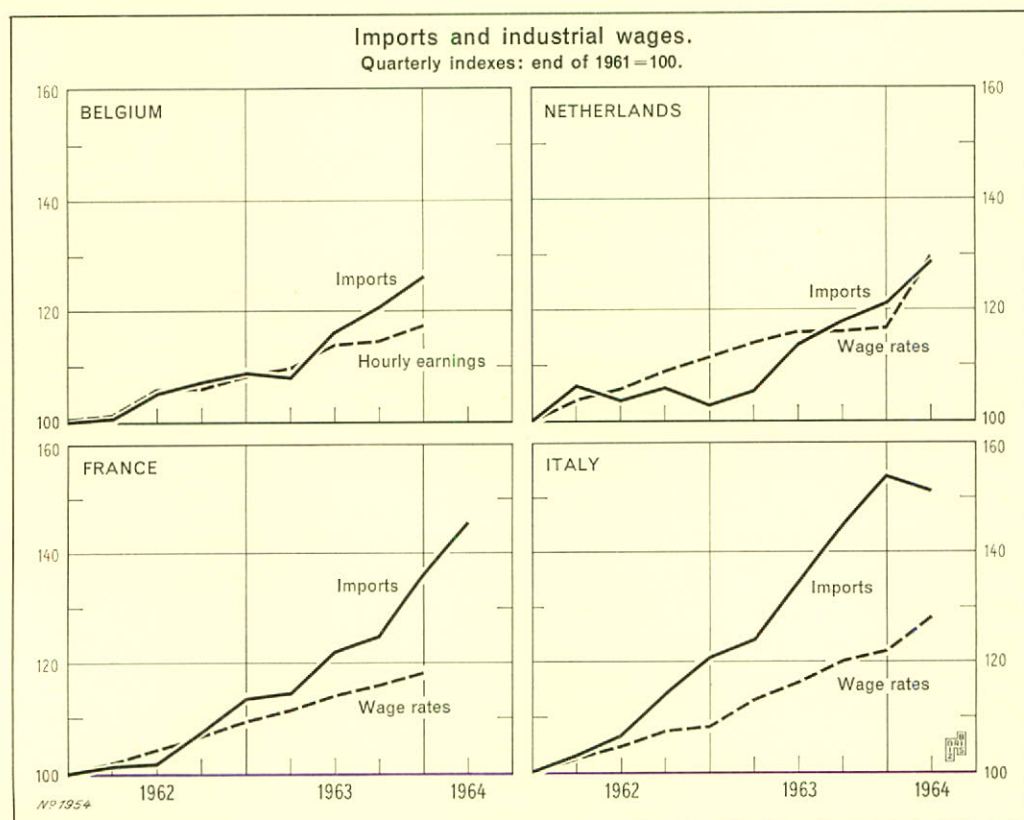
On the demand side, there was not only a huge rise in total consumers' expenditure but also an acceleration of structural shifts towards more expensive foodstuffs, such as meat and dairy products, and towards motor-cars and other durable goods. Car sales increased by two-thirds in one year and domestic producers were, not surprisingly, unable to keep abreast of demand. With agricultural output static since 1961, trade in foodstuffs accounted for \$500 million of last year's deterioration in the balance of payments. Trade in motor vehicles accounted for another \$300 million. In addition, the large movement of labour from agriculture to industrial centres was increasing the demand for urban housing.

Up to September 1963 the authorities allowed the balance-of-payments deficit to be financed by an increase in the commercial banks' net borrowing abroad, which permitted the continued expansion of bank lending, both directly and through the otherwise unreceptive capital market, thus offsetting the domestic deflationary effects of the deficit. As the magnitude and persistence of the inflation became evident, monetary policy in the second half of 1963 shifted gradually to restraint. In September the banks were asked to stop increasing, and if possible to reduce, their net indebtedness to non-residents. Thereafter, most of the deficit's deflationary impact was allowed to make itself felt, though the authorities continued to create liquidity sufficient to maintain orderly conditions in the capital market and to finance the

Treasury's 1963 cash deficit, which itself resulted largely from the civil-service pay increases. The expansion of the money supply slowed down and the banks' liquidity was brought under increasing pressure.

Parallel to this monetary tightening, fiscal and other measures were announced in September 1963 and early 1964 designed to bring a better balance between domestic supply and demand without, as far as possible, sacrificing the continued growth of output. Not all the measures adopted were of equal significance. Probably the most important were those to slow down consumption demand — particularly for motor-cars — and to improve the budget balance. After projected steps to reduce the budget deficit had been announced and the sales tax on certain luxury goods raised in September, February saw the introduction of a special purchase tax of from 7 to 15 per cent. on motor-cars and boats, as well as a 14 per cent. increase in the petrol tax. This was supplemented by restrictions on consumer credit.

Also significant were a number of measures aimed at improving the capital-market situation. Bond issues are now to be restricted to the amount of new long-term savings available, the 15 per cent. withholding tax on dividends has been replaced by a system giving taxpayers the choice between a 5 per cent. withholding tax and a flat 30 per cent. tax on dividends received, and stamp duties on share and bond transfers have been substantially cut. Finally, some direct action was taken to help check the rise in consumer



prices. In particular, house rents were blocked for two years, while special supplementary imports of meat and butter were authorised.

By the spring of 1964 the various measures of restraint were beginning to make themselves felt. The slow-down in credit expansion was maintained and the price rise also tapered off somewhat, while certain sectors of industry experienced a perceptible lessening of demand pressure and some easing of the labour situation. On the other hand, wages were still rising — partly because of indexation — and there was little sign of recovery in the capital market.

What must be seen over the near future is whether inflation has been decisively checked and the balance of payments put on the road to recovery. The favourable aspect of the situation is that exports have maintained a steady upward trend, so that improvement can be expected if the precipitous rise of imports is stopped and the economy is given a breathing-space during which the trade gap can be narrowed. In order to assure this result two things are necessary. First, the government's measures of restraint must succeed in putting a significant damper on the expansion of demand. And secondly, all concerned must co-operate to bring the rate of increase of wages back from the realm of fantasy to something which is in reasonable relation to productivity gains.

France. After some setback to production caused by bad weather and by the strikes in the public sector in the first quarter of 1963, the French economy advanced strongly throughout the following twelve months. The farming sector could not match its unusually good results for 1962, so that the increase in gross national product in 1963 was just under 4½ per cent. With private consumption demand buoyant and public investment and housing also showing a good increase, industrial output has been running about 6 per cent. higher than a year earlier.

This was accompanied, however, by a large price rise. During most of 1963 the retail-price index rose at an annual rate of 6 per cent. or more and the wholesale-price index by 4 per cent. Part of the inflationary pressure was absorbed by a deterioration in the current account of the balance of payments, and the trade surplus on a f.o.b. basis had disappeared by the beginning of 1964.

The main source of tension was the generally rapid expansion of demand, especially consumption, and the continued pressure of this on the labour market. The rise in consumption came partly from repatriation of population from Algeria; it was also due to wage increases obtained over the past year or two, so that something of a self-sustaining inflationary spiral appeared to have emerged. Despite another large increase in the working population during 1963, the manpower situation was not perceptibly eased and wages continued to rise at a fast pace. Total income from employment in 1963 went up by 13 per cent. — three times as much as output, and more also than the national product measured at current prices.

In the first half of 1963 the authorities strengthened the policy of moderating the expansion of the money supply and liquid assets both by ensuring restraint on the part of the credit institutions and by drawing the public's savings more into the capital market. This was really a new turn to the policy of the authorities, which now became to keep the increase of internal liquidity more or less in line with the rise of real output. In the course of the summer, however, it became apparent that stronger action would be needed to redress the situation, as the rate of price increase was accelerating rather sharply.

Accordingly a stabilisation programme was introduced during the autumn, the principal aim of which was to check the price rise and skim off the inflationary surfeit of demand without materially affecting the growth of output. The measures adopted fall into three main groups: first, intensified credit restraint, with restrictions on hire-purchase as well as on bank credit, and also an increase in the discount rate from $3\frac{1}{2}$ to 4 per cent.; secondly, measures in the sphere of public finance, a reduction in the planned budget deficit for 1964 and larger financing by long-term borrowing; and thirdly, direct action on the price front, including selective tariff cuts, a postponement of controlled rent increases and a general prohibition on price increases in manufacturing without authorisation by the Ministry of Finance.

By the end of 1963 and during the first quarter of 1964 this programme appeared to be having a certain measure of success. The rise of the retail-price index slowed down to around 2 per cent. per annum, while output continued to expand steadily. The money supply also grew less fast than before, partly because of the reduction in the external surplus and partly because of a slower rise in bank advances. It was too early to judge, however, to what extent there had been a fundamental improvement in the situation. In the first place, the measures of price control might to some extent simply be repressing inflation for a time, so that an acceleration of price increases later in the year could not be ruled out. Secondly, the early months of 1964 saw some renewal of labour unrest in the public sector. The authorities, however, have taken a firm stand to keep the rise in wages moderate and also to resist demands for higher prices from the agricultural sector.

In any event the labour market has remained under great strain and the test of the stabilisation effort may lie in whether the proposed reduction in the budget deficit is realised.

Netherlands. At the beginning of 1963 the prevailing impression in the Netherlands was that the economy was slowing down more than was desirable. As a consequence, and particularly in view of the easier labour-market situation and the levelling-off of credit expansion, monetary restrictions were suspended.

However, private consumption picked up again and expanded over the year as a whole at a rate close to that recorded in the boom year 1960. Fixed investment also grew more than in the previous year and demand for

building continued to exceed production capacity. Exports increased as before and the only slackening was in government consumption. On the supply side, output showed a much larger gain than in the preceding two years. Imports, too, rose more than in 1962 and 1961, and, as they grew faster than exports in 1963, the current surplus on a transactions basis was trimmed to a size considered appropriate for the Netherlands economy.

The rise in demand converged on the labour market, which came under increasing pressure, the more so as external demand for manpower was attracting workers abroad. This tension led finally to a breakdown of the general wage agreement, on the initiative of a few employers. In October an agreement was reached on a 10 per cent. rise in official wage rates in 1964. The actual increase in wages, however, is expected to be about 15 per cent., and for government employees a rise of 20 per cent. has been granted. Productivity, on the other hand, is expected to improve by 4.5 per cent. in 1964.

However desirable some adaptation of the Dutch wage and price levels to those in neighbouring countries may have been, a wage rise of that magnitude was bound to entail a serious risk of over-adjustment. This danger appeared all the more probable for two reasons: first, the pronounced growth of consumer demand seemed likely to coincide with a big rise in private investment and, secondly, the economy was liquid enough to finance quite a substantial additional demand.

In view of these circumstances the authorities imposed a variety of restrictive measures from the autumn onwards with the aim of reducing demand and the inflationary impact of the wage increase.

In October credit ceilings were reintroduced by the Nederlandsche Bank and in January 1964 the discount rate was raised from 3½ to 4 per cent. and hire-purchase regulations were tightened. As a measure of price control, a limit was set on the extent to which higher wage costs could be passed on in prices. Taxes on cigarettes and petrol were substantially raised to dampen consumer demand. Steps were also taken with the object of reducing investment demand: public investment plans were scaled down and private investment was discouraged by the suspension of advance amortisation and of investment allowances for new building. Finally, in order to drain liquidity from the economy, a government loan was issued for an amount in excess of actual needs.

The effect of the measures introduced will be to limit the rise in economic activity. Nevertheless, in 1964 a fairly substantial excess demand must be expected, combined with a rise in prices and a deterioration in the balance of payments. The situation is expected to ease, however, in the latter part of the year.

Switzerland. The Swiss economy has continued to show signs of strain. Owing to a smaller increase in employment, the 4.2 per cent. growth in the real gross national product was considerably below the 6.1 per cent. rate of 1962. Private consumption and public expenditure were the strongest expansionary factors. Business investment increased at a lower rate, but with the

large rise in public investment and the continuing strength of residential construction, the gap between supply and demand in the building sector was if anything wider. The trade balance has continued to deteriorate.

Since available evidence pointed towards a further aggravation of the prevailing disequilibria, the Federal Government in January 1964 proposed legislation designed to increase its powers of control over inflationary developments.

In the field of credit policy the new legislation, passed by Parliament in March, makes mandatory provisions previously embodied in voluntary agreements between the National Bank and the commercial banks; thus it gives the government power to prohibit the payment of interest on new foreign deposits and to make them subject to a period of notice, to prevent the investment of foreign funds in Swiss securities, real estate or mortgages, to limit the increase in bank credit and to ensure the control of new issues. Furthermore, these regulations are now extended to other financial intermediaries and the banks may be required to deposit the countervalue of their new foreign liabilities (in so far as they are not invested abroad in foreign currencies) with the National Bank. This latter measure came into effect on 31st March 1964.

The new legislation also provides for regulations designed to restrict building activity. With certain exceptions, building is subject to prior authorisation and a ceiling on the granting of new building permits is to be fixed. Certain types of non-essential building are to be prohibited completely for one year. Furthermore, the restrictive regulations laid down in March 1963 concerning the admission of foreign labour are to be retained for another six to nine months and are then to be replaced by a more comprehensive system.

Another important development which represented some change of policy was the upward movement of interest rates. Hitherto the National Bank had tried to maintain interest rates at a relatively low level; this was not only for balance-of-payments reasons but also because of the high degree of mortgage indebtedness and hence the effect that a rise in the interest rate level might have on rents, agricultural prices and wages. While this policy helped to hold down cost inflation, it stimulated economic expansion and aggravated the pressure in the building sector. However, when demand for credit intensified towards the middle of 1963 while at the same time the banks were no longer able to compete for medium-term funds, the National Bank agreed to a rise in the rate offered on the banks' medium-term bonds, which has been followed by a more general rise in rates. Swiss interest rates are still not very high, but their upward movement has continued and the National Bank has indicated that it does not intend to interfere with this development; their ultimate level will depend on the success of the stabilisation programme itself.

Belgium. After two years of balanced expansion, signs of strain became evident after mid-1963. Unemployment has fallen to a record low level, while the expansion of aggregate demand has continued to accelerate.

Demand for consumer durables remained strong over the past year and expansion of business investment quickened. But these factors were over-

shadowed by the rise in government expenditure, particularly for investment. Residential construction declined and, despite a rapid increase in exports, there was some deterioration of the current external balance.

A large rise in the Treasury's overall deficit increased the government's financial requirements at a time when the credit needs of the business sector were also expanding and when the new withholding tax had reduced public interest in new domestic issues. The Treasury financed a large part of its needs abroad with a resulting rise in commercial-bank liquidity. This permitted a large expansion of credit to enterprises and led to a rapid increase in the money supply, the impact of which was, for the time being, partly offset by the increase in the public's liquidity preference. Excluding government capital transactions, the balance of payments shifted from surplus to deficit and did not contribute to domestic liquidity formation.

In view of these developments, the National Bank moved away from its easy credit policy and raised the discount rate in two steps by October 1963 from 3.50 to 4.25 per cent. However, wage and price increases somewhat accelerated in the second half of 1963 and made the danger of inflation more imminent. Consequently, the following measures have been taken: first, the government is intending to spread its investment programme over a longer period of time; secondly, in February 1964 consumer credit conditions were tightened; thirdly, the National Bank has reached an agreement with the credit institutions to limit the expansion of credit.

The success of these measures will depend to a large extent on the Treasury itself. The overall budget deficit is expected to remain high in 1964 and the way it is financed will exert an influence on the future course of events. In recent months the financing has been by long-term borrowing. While this is an improvement, the high level of the private sector's liquidity itself constitutes a danger for monetary stability; even if it were employed to finance the government's deficit this would represent more an increase in the velocity of money than new savings.

Sweden. The past year has been one of satisfactory performance for the Swedish economy. With prospects in January 1963 not altogether favourable, the discount rate was lowered from 4 to 3.5 per cent. and public investment accelerated. By June 1963 a rapid expansion of bank credit and the inflationary pressures emanating from the building sector caused the Riksbank to restore the cut in the discount rate, and a further rise to 4.5 per cent. was announced in January 1964. At the same time bank liquidity was reduced through public-debt operations and the imposition of a penal rate on excessive recourse to the Riksbank served the same purpose.

The change in the budget position from a surplus of S.kr. 600 million in 1962 to a deficit of S.kr. 200 million in 1963 put the task of containing the economic expansion within non-inflationary limits on monetary policy. Credit extension to the building sector continued high, however, while credits to industry had to be accommodated to the policy change.

Gross national product at constant prices rose by 3.7 per cent. in 1963, but owing to the unusually severe winter and poor harvest this figure understates the expansionary forces. Partly because of the recovery of exports, the sectors which had earlier been subject to recessionary tendencies, that is, pulp, paper, iron and steel, showed the greatest improvement. A further reduction in unemployment reflected the increasing labour shortage, which was particularly pronounced in the building sector. Whereas consumer prices rose less than in 1962, wholesale prices rose somewhat more owing to the recovery of raw-material prices.

The strongest expansionary factors were private and public consumption, the rapid growth of exports and investment by local authorities. Industrial investment continued to decline, although less than expected.

In view of the decline in profit margins, employers' resistance to new wage increases has been particularly strong. With the help of a government-appointed arbitration committee, a new agreement with the trade unions was finally reached in April 1964 providing for wage increases of 1.4 and 3.4 per cent. in 1964 and 1965 respectively. However, increased fringe benefits and wage drift are expected to inflate the actual increase in hourly wage costs to almost what it had been in preceding years.

Austria. The Austrian economy has over the past year progressively recovered from the weakness apparent in 1962. In the first quarter of 1963 real gross national product was only 1 per cent. above a year earlier but by the fourth quarter it was 7 per cent. higher. Private consumption, public expenditure and exports were the strongest expansionary factors. Business investment and exports of steel and other basic materials have been lagging, but since the fourth quarter of 1963 there have been signs of improvement also in these demand factors. There was in 1963 on the whole no intensification of the pressures on the labour market; the 4.4 per cent. rise in real gross national product was achieved with little increase in employment, but the transfer of labour from the stagnating to the expanding sectors has contributed very much to the growth of output.

The continuing balance-of-payments surplus has led to a further increase in the banks' liquidity and a consequent downward pressure on interest rates — a development which the monetary authorities did not try to counteract. On the contrary, in order to stimulate investment the discount rate was lowered from 5 to 4.5 per cent. in June 1963. Credit expanded more rapidly, largely to the benefit of building activity.

The rise in prices has continued to be a problem. After the standstill agreement on wages and prices expired in January 1963, a new wave of wage increases in the second half of 1963 and its repercussions on prices led to the appointment of a group of experts to draft a stabilisation programme. This programme, which has already been approved by the representatives of business and labour, recommends among other things the active use of temporary tariff reductions and freer admission of foreign labour as tools of anti-inflationary policy. The first steps in this direction were taken in April 1964.

Germany. The economic climate in Germany underwent an abrupt change after the middle of 1963. Up to that time inflationary pressure had eased. The industrial investment boom had tapered off during 1962, and this was followed in 1963 by a smaller increase in private consumption as wages rose somewhat less fast than before and personal saving picked up. While construction demand was still very strong, the labour market appeared to be in better balance, prices were not going up much and altogether, with output increasing by around 3 per cent. per annum, a period of stable, less hectic expansion seemed in prospect.

Since then, however, the picture has been radically altered and 1964 seems bound to be a year of increased growth and probably renewed strain on resources. The main cause of the change was an accelerated increase in exports and, even more, export orders, due to the pressure of demand in other European countries. At the same time the rise in imports levelled off and the deficit on invisible items declined, so that the current account, which was in deficit up to the third quarter of 1963, moved into surplus at an annual rate of about \$2 milliard. In addition, the inflow of long-term capital to the bond market — due partly to interest rate inducements but more to fiscal and other factors — continued to boost the balance-of-payments surplus. All this led to an upward revision of investment plans and to a renewed rise in the commercial banks' liquidity.

The German authorities are thus once more faced with inflationary dangers at home due to an external surplus. In these circumstances it has seemed increasingly risky to continue with the policy, followed since 1961, of allowing market forces to work themselves out more or less fully in the banking system and the economy as a whole. Since the external position is also making general monetary restraint inappropriate, a number of selective measures have been taken to discourage the inflow of capital and give the banks an incentive to invest more of their liquid funds abroad.

Early in 1964 the banks were asked to give precedence to residents in subscriptions to public-sector bond issues. In March the government announced proposals to put a 25 per cent. withholding tax on interest from German bonds held by non-residents and to abolish the 2½ per cent. tax on new security issues, thus encouraging foreign borrowers to raise capital in Germany. At the same time the Bundesbank reintroduced special swap arrangements below market rates in order to stimulate the acquisition of US Treasury bills by the banks. Also, the banks' minimum reserve ratios on deposits of non-residents were raised to the statutory maximum to give a further incentive to money exports, as the reserve requirements do not apply to deposits that are offset by short-term foreign assets. Finally, the ban on interest payments to foreigners was once more extended from sight to time deposits.

It is easy to see that these measures do not go to the root of the problem. But, since the roots lie mostly in other countries, a suitable remedy for the German authorities does not suggest itself. After the rather sudden substantial rise in exports, however, it may be hoped that a rise in imports

will help to moderate the strain on the economy over the coming year; some tariff cuts have been proposed to assist this process. In addition, measures have been taken by other countries to check their excessive upsurge of demand.

United Kingdom. Following the pause of 1961-62, production in the United Kingdom has been going up rapidly since the spring of 1963, in response to various policy measures and to an increase in exports. In the fourth quarter of 1963 output was around 8 per cent. above the level of a year earlier; expansion continued in the first quarter of 1964, at a slightly slower rate, but unemployment continued to decline and the margin of unused capacity had clearly become small.

Expansionary fiscal and monetary policies had been initiated in the autumn of 1962 and were pursued in the April 1963 budget, which provided for an estimated increase of £620 million in the overall deficit. (The actual figure turned out to be £200 million less than this.) Public investment, notably in electricity and housing, was steeply increased, while tax reductions helped to stimulate consumer spending, particularly on motor-cars. Meanwhile, the rate of increase in exports of 10 per cent. (or 8 per cent. in volume terms) since the start of 1963 seems satisfactory but not exceptional in the light of the buoyant demand conditions in nearly all major markets. In fact, Britain's share of world exports of manufactures continued to decline slightly.

As the upswing proceeded, the decline in fixed capital formation in manufacturing, which had been in progress since mid-1961, levelled off and there was some rise before the end of the year. The prospect is for a sizable increase during 1964. More prominent, however, was the turn-round of nearly £200 million in stock-building between the third and fourth quarters of last year, which helped to boost imports to record levels. With the current external account deteriorating, and exports of long-term capital also moving to rather higher levels, the basic balance of payments shifted into deficit. From March 1963 onwards, the authorities aimed to discourage the outflow of liquid funds by keeping short-term interest rates well up relative to the 4 per cent. Bank rate.

Last year's rapid expansion and declining wage costs reflected an initial under-utilisation of resources. Hence in the early months of 1964 the authorities were faced with a twofold task: to bring the growth of the economy down to a rate that would be sustainable in the longer run, and to forestall any tendency for wage costs again to get out of hand and impair the international competitiveness of industry. The tactic adopted was a shift to mild restraint. Bank rate was raised from 4 to 5 per cent. at the end of February, but the banks' liquidity — the minimum ratio now at 28 per cent. — was not severely squeezed. In April the budget provided for an increase of approximately 10 per cent. in the taxes on tobacco and alcoholic drinks, expected to yield an extra £100 million of revenue. Some additional incentives were also given to personal saving. However, below the line net payments were expected to go up by some £300 million over the outturn of the previous fiscal year —

though this overstates the rise, as approximately £165 million represents a shift of local-authority borrowing from the market to the Exchequer.

Thus far in the upswing the rise in wages has conformed rather well with incomes policy. However, the increase has been exceeding the 3½ per cent. "guiding light" established in connection with the 4 per cent. annual growth target, and the fact that cyclical recovery enabled this to be absorbed without inflation last year is not evidence that the problem has been solved. The real test in respect of both labour costs and the balance of payments is still to come.

But the overall situation gives grounds for cautious optimism in that the outlook for exports, notwithstanding the EEC's anti-inflation programme, remains rather favourable — provided domestic demand does not move ahead too fast.

Improved situation in the United States.

An outstanding change in the US economy over the past year was the thaw in official policy — both monetary and fiscal. After the external deficit worsened in the first half of 1963 owing to a much enlarged outflow of private capital funds, three important monetary measures were taken in July: the discount rate was raised from 3.0 to 3.5 per cent. to slow up the outflow of liquid funds; Regulation Q was relaxed to enable the banks to compete more effectively with foreign rates for time deposits; and an interest equalisation tax on new purchases of foreign securities was proposed by the President to Congress to discourage the outflow of portfolio capital. Largely in consequence there was an impressive reduction in the balance-of-payments deficit in the second half of the year; with the help of other factors there was a near-balance in the first quarter of 1964.

On the fiscal side, the income-tax reduction was enacted in February 1964, providing for a decrease in collections from individuals of \$8 milliard in this calendar year and one in corporate-tax liabilities of \$1.5 milliard. Anticipation of this measure may have affected demand to some extent prior to its passage, but the main stimulus from it will come in the months ahead. The tax cut was essentially not an anti-cyclical measure but an effort to reduce the persistently high under-utilisation of productive resources of the past six years. With good reason, it supported an optimistic tone in views about the economic outlook even though the goal of full employment was not likely to be achieved in a short time.

Following the slow-down of expansion in the second half of 1962, the development of economic activity over the past year was favourable and exceeded what was expected at the beginning of 1963. While the increase in aggregate demand was rather broadly diffused, the accelerated expansion was stimulated by heavy demand for motor-cars, large increases in residential construction and business fixed investment and a more normal rate of inventory increase. The rises in Federal Government outlays and in personal consumption were less important than the year before.

Thus the economy has confounded the pessimists by continuing the expansion phase of the business cycle longer than in previous post-war cycles, and no signs of a reversal are in sight. In general, the reason for this is that the expansion has not developed the characteristic distortions of a boom which so often has either destroyed itself or has had to be tamed by official restrictive measures. Rising monetary demand has not been dissipated through an over-eager raising of prices, and wage increases have in the main been limited to a rate which has not generated a wage/price spiral. There has not been an outburst of business investment like that in 1956-57 or a rush of inventory accumulation as in 1959, either of which would have produced an inevitable reaction. Mortgage credit has remained readily available and there has been a decline, rather than an increase, in its cost. Finally, the impetus from the Federal budget has been fairly evenly maintained, in contrast to the drastic contraction of the stimulus from 1954 to 1956 and from 1958 to 1960. In other words, business, labour and the authorities have all contributed to keep the cyclical expansion a balanced one.

With the demand stimulus of the tax cut still to come in the months ahead, and with the pace of business investment quickening, the outlook for economic activity is one of substantial growth. In the assessment of the prospects there has been some controversy about the problems that may emerge and their policy implications. One of these is whether inflationary tendencies will show themselves at an early stage. Regarding this possibility it would seem that there is ample margin in the economy to absorb the prospective increase in demand without excessive pressure on productive resources; indeed, with the labour force rising rapidly, it may be that unemployment will decline only moderately. A renewed rise of prices in such circumstances would be likely to reflect pressures from wage demands or price action in specific industries. This, however, would not make it any less essential for the authorities to take strong steps to maintain monetary stability.

A related controversy concerns the question whether the high rate of unemployment is structural rather than a reflection of inadequate demand. While only time will answer this definitely, there is surely no immediate prospect of general tightness in the labour market. And, whether the crucial point in the labour market turns out to be nearer to 4 per cent. or to 5 per cent. in unemployment statistics, any structural problem can be resolved more easily when demand for labour is active than when it is inactive.

Finally, there is the question whether the balance-of-payments problem will require further tightening of monetary policy. The opponents of monetary restraint tend to present the alternatives as either maintenance of the present monetary ease or drastic restraint which would largely counteract the stimulus from the tax cut. A more balanced view, however, is that continued outflow of funds and the upward tendency of market rates in Europe may have to be allowed to be reflected in interest rates in the United States. It is difficult to believe that the expansion is so fragile that there is no room for manoeuvring of this sort.

Developments in eastern Europe.

The unsatisfactory results of agriculture in most eastern European countries (including the USSR) in the two years 1962-63 was in large part attributable to the particularly adverse weather conditions that also had a bearing on developments in many western European countries.

In addition, however, there were other factors which the authorities have begun to correct, although it will be some time before their full benefits are realised. Thus, while in some countries measures have been taken to raise farmers' incomes by adjusting upwards the prices paid by the state for their deliveries, in others the plans for 1964 provide for increased investment in agricultural equipment and in artificial fertiliser production.

As regards agricultural output in 1963, it was much higher than in 1959 (which was a good crop year) in Albania and Poland (by 20 and 10 per cent. respectively); in Bulgaria, Czechoslovakia and Rumania it was around 5 per cent. higher, while for Hungary and the USSR the statistics show little or no improvement. Moreover, this situation is to be seen against the background not only of the expanding urban population but also of the increasing demand for higher-quality food connected with the growth of consumers' incomes.

Centrally-planned economies: National income, industrial production and productivity.

Countries	Annual increase					
	National income		Gross industrial output		Output per worker in industry	
	1962	1963	1962	1963	1962	1963
	in percentages					
Bulgaria	6.2	6.0	11.0	10.0	7.8	4.6
Czechoslovakia	1.0	— 4.0	6.2	— 0.6	3.1	— 1.0
Eastern Germany	4.2	2.5	6.2	4.9	6.6	6.5
Hungary	4.7	5.0	8.4	7.0	4.4	3.2
Poland	2.0	6.0	8.4	5.3	3.2	2.7
Rumania	4.5	7.0	14.8	12.5	6.5	7.2
USSR	6.0	4.0	9.7	8.5	6.2	5.0
Yugoslavia	4.0	12.0	7.4	14.9	6.0	10.0

With the exception of Poland, the growth rate of the national income in eastern European countries fell short of planned targets in 1963. In Czechoslovakia national income actually declined by 4 per cent., after rising by only 1 per cent. the year before.

In Czechoslovakia it was industrial output — especially of investment goods — that declined; this was because the slight increase in the labour force was more than offset by the fall in productivity. At the moment a reorientation of priorities for investments and production seems to be taking place towards the manufacture of final products in great demand and of

higher quality; efforts are also being directed towards the elimination of serious bottlenecks that have developed over the years within industry itself.

In 1963 the largest rises in industrial output were recorded in Rumania and Bulgaria (12.5 and 10 per cent. respectively); results were also satisfactory in the USSR (8.5 per cent.) and Hungary (7 per cent.), although lower than in most preceding years. In these four countries the industrial labour force has been expanding substantially year by year, but labour productivity has been rising equally fast or even faster.

Eastern Germany continues to suffer from labour shortages and industry can expand its output only by dint of steady and substantial improvements in productivity.

The various plans for 1964 provide for an expansion of output more or less in line with that achieved last year, except for Czechoslovakia, where it is hoped to attain an increase of 3.5 per cent. in industrial output after the negative results of 1963. Although the qualitative adjustment of production to demand by means of a redirection of investment will be continued, it is generally believed that this can take place only gradually. This adjustment will be assisted by the steady efforts to increase foreign trade both within the area and with countries outside.

The establishment in Moscow on 1st January 1964 of the "Bank for International Economic Co-operation" is intended to help in this direction. This bank, in which the USSR and the other eastern European countries are participating, has been assigned the task of operating a multilateral clearing system, in free roubles, among the member countries and of granting credit in connection with the clearing itself and also in the event of temporary payments difficulties.

In Yugoslavia the economic recovery which set in in the second half of 1962 continued last year, supported as it was by a 20 per cent. rise in fixed investment and strong consumer demand. Government consumption, however, did not rise. Industrial production went up by 15 per cent. (7 per cent. in 1962) and agricultural output by 6 per cent., so that the gross national product rose, in terms of volume, by 12 per cent., compared with 4 per cent. in 1961 and 1962.

Although exports continued to expand, imports rose even more and the trade balance deteriorated by some \$70 million. This was partly offset by an improvement in invisible receipts, and the overall deficit on current account was smaller than the volume of capital imports; the reserves consequently rose by some \$20 million in the course of the year to a total of \$130 million.

Monetary policy was geared to support expansion without giving rise to inflation. Special attention has been paid to avoiding government borrowing from the central bank and also to some flexible bank lending to profitable enterprises at short term while restraining bank lending at long term.

The international payments situation.

The shifting disequilibrium in payments. With the large and opposing changes in the balance-of-payments positions that have occurred over the past year, there is no easy answer to the question of whether or not the international payments situation as a whole has become more favourable. While a better balance has been achieved among the broad regions of North America, western Europe and third areas, serious imbalances within Europe have re-emerged.

The sharp reduction in the US external deficit after the middle of 1963 is a solid gain for international financial stability; given the key rôle of the dollar as a trading and reserve currency, this development has undoubtedly imparted a firmer tone to the system as a whole. While it seems too early to say that the improvement represents a real break-through towards equilibrium for the dollar after the five-year stretch of heavy deficits, it is a big step on the way.

Given the practical possibilities of the situation, the measures taken to reduce the outflow of capital have made a good contribution to regaining equilibrium, but less impressive have been the efforts of the government in cutting expenditure abroad on its own account. This was recognised in the balance-of-payments programme of July 1963, in which a further reduction of \$1 milliard by the end of 1964 was scheduled in government foreign expenditure. Full implementation of this target seems likely to be needed. With the domestic economy continuing to expand under the stimulus of the tax reduction, a significant gain in the trade balance is not expected; in fact, with the prospect of some falling-off of the recently high level of agricultural exports and the restraints being put on the boom in Europe, imports are likely to increase more than exports over the coming year. In addition, there is bound to be an increase in long-term capital exports once the interest equalisation tax is enacted, though this may be partly offset by reduced bank lending abroad. In sum, while future policy will have to see to it that the improved balance on private capital account is retained, reduction in government outlays abroad will be a necessary element to bring the dollar to a sound position.

The improvement in the balance-of-payments position has considerably increased confidence in the dollar. This was helped by the measures taken in July 1963, which showed that the authorities fully intended to maintain control over the situation. It cannot be assumed, however, that the external problem in the longer term will take care of itself. The interest equalisation tax must be seen as an expedient to cover an underlying disequilibrium between the United States and the outside world. This expresses itself in the tendency for excessive financial resources to flow abroad without a corresponding outflow of real resources in the form of exports. It matters little whether one considers that the economy is not competitive enough with respect to goods or too competitive with respect to money; on one side or the other the adjustment process must continue in the years ahead.

On balance, there has been improvement also in the position of the less industrialised countries of the western world. Strong expansion in the industrial areas has brought increased demand for raw materials, with a beneficial effect on prices and volumes. In a broad way, the strengthened position is indicated by the rise in the reserves of these countries by some \$1.5 milliard in 1963, as against \$0.5 milliard in 1962.

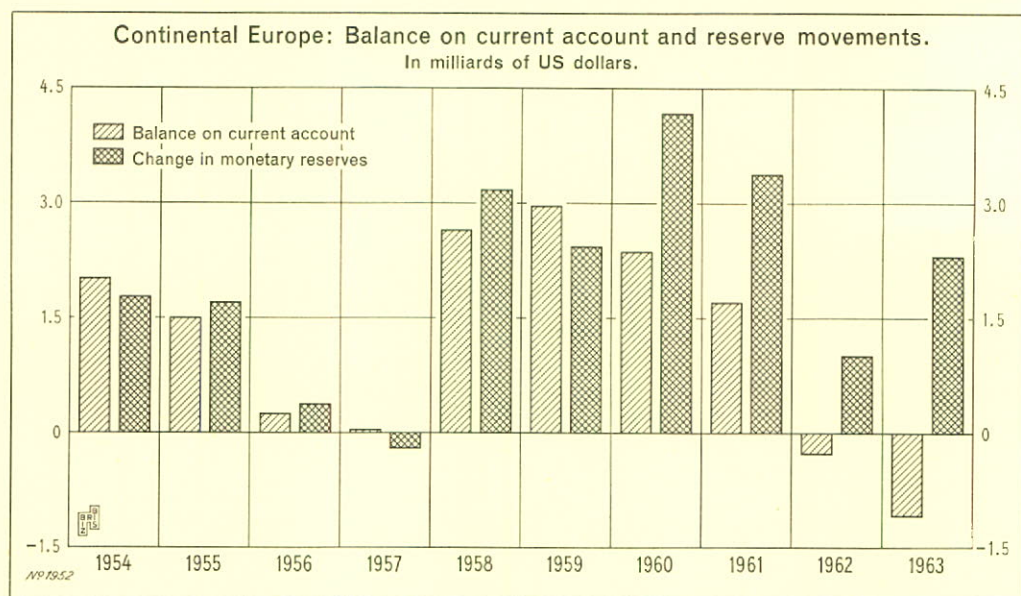
Developments in foreign trade of these countries have been generally favourable during the last two years thanks to a larger increase in export proceeds than in outlays for imports. The improvement was particularly marked in 1963, when the combined trade deficit of these countries declined by \$1 milliard thanks also to the higher prices received for some of their basic products, e.g. sugar, cocoa and wool. Australia was able to turn a trade deficit of over \$200 million in 1962 into a small surplus in 1963 and the shift from deficit to surplus in the case of Argentina amounted to about \$500 million, but in this case the decline in imports played a bigger part than the increase in exports. Much the same can be said of India's trade, its deficit having declined from over \$900 million to less than \$700 million. A substantial improvement seems to have occurred in the already positive trade balance of the oil-producing countries.

On the other hand, among the non-European industrial countries Japan shows a large deterioration of over \$500 million in its trade balance.

For western Europe changes in the balance-of-payments position over the past year resulted from conflicting developments in which disequilibria among the countries overshadowed the aggregate change. In the main these concerned the European Economic Community countries, as the changes for the other countries were largely offsetting.

In 1963 the current-account position of the Community countries moved into deficit because of a further large deterioration on trade account. The current balance worsened by about \$700 million, following an adverse movement of \$1,650 million the year before. But, whereas in 1962 the decline in the current surplus was spread among the countries and was an equilibrating factor in the world payments situation, there were in 1963 large adverse movements, mainly for Italy but also for France, at the same time as a large favourable movement for Germany. The disequilibrium was accentuated in the course of the year, so that by the fourth quarter the German current surplus was at an annual rate of about \$2 milliard, while the other countries of the Community were in deficit by about \$1.5 milliard, largely accounted for by Italy.

The balance-of-payments position of continental Europe was made more anomalous by the fact that while there was a deficit on current account there was a large overall surplus due to an inflow of funds from abroad. The rise of \$2.2 milliard in official reserves in 1963 exaggerates this movement, as the net foreign position of the banks deteriorated by about \$1.3 milliard. However, the fact remains that, instead of being a net exporter of capital,



which would seem the appropriate structural position, Europe was a large net importer of capital — which in the main has been flowing into reserves. In this respect 1963 was worse than the previous year, as the rise in reserves was larger despite the bigger current-account deficit.

Thus, policy has the double task of restoring balance within Europe and of encouraging the necessary shift from importing to exporting capital vis-à-vis the outside world.

Looking at changes in the world balance-of-payments situation between 1961 and 1963, the following table shows three interesting developments. The export of capital from the United States increased by over \$1 milliard without any rise in the net capital receipts of countries outside Europe taken together; western Europe's official reserve position improved in 1963 by not much less than in 1961, despite the deterioration of over \$2 milliard on current account; and the rest of the world, benefiting from a rise in Europe's imports, improved its current balance vis-à-vis Europe (excluding monetary gold sales) by more than \$1.5 milliard, so that its unchanged capital receipts were enough to cover its trading deficit and to allow an improvement in its reserve position.

The rest of the world, as given in the table, divides fairly conveniently into five developed countries — Australia, Canada, Japan, New Zealand and South Africa — and the less-developed world. The improvement of \$2 milliard in the rest of the world's current account between 1961 and 1963 was shared almost equally between the two groups. On capital account most of the net receipts of the rest of the world went to the five richer countries — \$2.4 out of 2.7 milliard in 1961 and \$2 milliard out of about the same total in 1963; the less-developed countries as a group were still only moderate net importers of capital in 1963.

World balance of payments.

1961	Balance of		
	United States	Western Europe	Rest of the world
	in milliards of dollars		
Current account with United States	—	— 0.6	— 1.8
western Europe	+ 0.6	—	— 1.9
rest of the world	+ 1.8	+ 1.9	—
Total	+ 2.4	+ 1.3	— 3.7
Monetary gold sales	—	—	+ 0.6
Total current account	+ 2.4	+ 1.3	— 3.1
Capital account, errors and omissions	— 3.7	+ 0.9	+ 2.7
Overall balance, corresponding to change in official gold and foreign exchange holdings and net IMF position	— 1.3	+ 2.2	— 0.4
1962			
Current account with United States	—	— 0.9	— 1.3
western Europe	+ 0.9	—	— 0.9
rest of the world	+ 1.3	+ 0.9	—
Total	+ 2.2	—	— 2.2
Monetary gold sales	—	—	+ 0.3
Total current account	+ 2.2	—	— 1.9
Capital account, errors and omissions	— 4.1	+ 1.9	+ 2.3
Overall balance, corresponding to change in official gold and foreign exchange holdings and net IMF position	— 1.9	+ 1.9	+ 0.4
1963			
Current account with United States	—	— 1.1	— 1.7
western Europe	+ 1.1	—	— 0.3
rest of the world	+ 1.7	+ 0.3	—
Total	+ 2.8	— 0.8	— 2.0
Monetary gold sales	—	—	+ 0.8
Total current account	+ 2.8	— 0.8	— 1.2
Capital account, errors and omissions	— 4.9	+ 2.6	+ 2.9
Overall balance, corresponding to change in official gold and foreign exchange holdings and net IMF position	— 2.1	+ 1.8	+ 1.7

Note: The overall balances for the different areas correspond to the changes in countries' official gold and exchange holdings and in their net IMF positions. They are affected by differences in statistical presentation and by movements of official dollar reserves into or out of the Euro-dollar market. If the overall balance figures are added across, a positive net result is obtained. In the absence of inconsistencies in the statistics of exchange holdings, this figure would equal the rise in monetary gold stocks for the year in question.

Taking the world pattern of capital movements, there was not a great change between 1961 and 1963. However, the share of Europe in net capital receipts, by no means insignificant in 1961, had by 1963 equalled that of the rest of the world. Moreover, in both years it would appear that on balance Europe was a substantial net importer of capital from non-US sources, particularly the less-developed countries.

Two things point to this. The first is that the net capital imports of the less-developed group of countries — \$0.3 milliard in 1961 and \$0.9 milliard in 1963 — were surely much less than the gross amount of foreign capital they received during those two years. There must therefore have been a considerable gross outflow of funds from these countries. The second factor is that, on the basis of US balance-of-payments figures, not more than about half of Europe's net capital receipts in 1961 and 1963 can be attributed directly to US sources. Hence, it would appear that the inflow of capital into the less-developed countries, mostly from the United States, has been to a significant extent offset by an outflow from them, mostly to Europe.

Management of exchange markets and reserves. Continued active co-operation among the monetary authorities of the principal financial centres has been required over the past year to meet shifting pressures in the exchange markets and to supplement official reserves. The need for it arose, first of all, out of the basic deficit and surplus positions, which had to be financed in a way to minimise exchange instability, but also out of temporary pressures due to political and financial uncertainties. The examples of sterling, the dollar and the lira show the nature of the problems and the instruments used in dealing with them.

In the case of sterling, selling pressure in the exchange market early in 1963 was caused by a withdrawal of liquid funds from London. It reflected an uneasiness about the longer-term prospects of the balance of payments rather than an immediate external deficit and was the sort of movement that tends to be cumulative until the public sees clearly that the authorities have the resources and the intention to meet the situation. The adverse sentiment induced by the failure of the negotiations for British entry into the Common Market led to an outflow in January 1963 and there was a more substantial movement in March with the anticipation of an expansionary budget. Official intervention in the market was required on both occasions to meet the heavy demand for foreign exchange. The Bank of England offset its sales to the market by taking deposits totalling \$250 million from four continental central banks, thus avoiding a decline in official reserves. With the underlying external position sound, these doubts soon evaporated and the reflux of funds allowed the central-bank deposits to be repaid by June.

In the case of the dollar, the basic deficit in the balance of payments has been the crux of the difficulty. But this was not essentially because of the deficit of any one year, for the meeting of which the United States has had a huge gold stock as well as large possibilities of financing with credit. It was rather because of the persistence of the deficit, which weakened the liquidity position of and confidence in the dollar. However, the problem of managing the situation was complicated by the extensive use of the dollar as the medium of international settlement. This meant that temporary shifts of funds and other imbalances among foreign countries could increase the drain on US gold reserves in circumstances where there was a preference for adding gold rather than dollars to official reserves.

Operations over the past year were concentrated on the Deutsche Mark, the Swiss franc and the guilder. The strength of these currencies vis-à-vis the dollar reflected largely transfers of dollars from reserves of other countries rather than imbalance in direct transactions with the United States. For the Deutsche Mark and the Swiss franc the periods of excess offering of dollars did not tend to be subsequently offset by a reverse flow of funds, while the pressures on the guilder were more short-lived. To meet the situation the US authorities used the instruments that had been developed during the previous two years: (1) intervention in the forward exchange markets for Swiss francs and guilders to provide cover at reasonable cost for foreigners to hold funds in dollars; (2) drawing on the swap facilities, in all three cases, to absorb an immediate over-supply of dollars; it may be noted that the network of swap facilities between the Federal Reserve and foreign central banks, including the BIS, was increased to over \$2 milliard; (3) the swapping of holdings of certain European currencies through the intermediary of the BIS to meet temporary needs for other currencies, namely Swiss francs and guilders; (4) the issuing of Treasury securities denominated in foreign currencies to the Bundesbank and the Swiss Confederation to absorb excess accumulation of dollars by Germany and Switzerland and in one case to help liquidate a swap drawing.

In addition, the United States made two drawings of \$125 million each, chiefly in Deutsche Mark and French francs, on the International Monetary Fund in February and May 1964. The proceeds were sold to other countries for use in making repayments to the Fund. As dollars could not be used for such repayments because the United States was no longer a net lender through the Fund, the alternative for the Treasury would have been a loss of gold reserves, either directly to countries requiring gold for repurchase of their currencies from the Fund or indirectly as a result of these countries buying European currencies against dollars for the same purpose.

Thus, the objective of US exchange operations has been to prevent temporary pressures, and even enduring accumulations of dollars, from making too large a call on gold reserves. Concern about the level of reserves, however, has had the more fundamental motive of warding off any significant flight from the dollar, which, while it could be met by emergency policy measures, would endanger internal economic expansion.

In the case of the lira, the primary difficulty has been the rapid emergence of a large current balance-of-payments deficit. Added to this has been a heavy outflow of Italian capital funds seeking safety from possible exchange instability and, in part, fiscal advantages. The problem for the authorities has been to finance the deficit during the time needed to formulate and reap the benefits of a remedial policy programme and to do so in a way that minimised the weakening of confidence. That the difficulty started with Italian reserves at a level of over \$3.5 milliard, plus a holding of \$200 million of US Treasury securities denominated in lire, is a reminder that ample international liquidity does not in itself assure the proper functioning of the international monetary system.

In the first phase, which started in the second half of 1962, the emerging deficit was financed by lifting the prohibition on the banks to run an unbalanced foreign position. This measure was conceived at the time primarily as a convenient way of supplying the economy with necessary domestic liquidity. In the course of a year (by September 1963) the banks had drawn in about \$1 milliard from abroad in various currencies — largely from the Euro-dollar market.

When the Bank of Italy limited the banks' access to foreign funds, the continuing deficit began to be reflected in a decline of official reserves. During this phase, from October 1963 to February 1964, two facilities for limiting the direct loss of reserves were utilised. The Bank of Italy drew on its reciprocal swap facility with the Federal Reserve System and sold lire direct to the US Treasury, thereby providing itself with further resources for market intervention. The accumulation of lire by the US Treasury was in anticipation of the repayment of its debt to Italy in lira-denominated securities, which was effected by April 1964.

In March a new phase had begun with arrangements for substantial liquid resources and other credits from abroad. The aim was to stop the capital flight as well as to limit the drain on reserves. By this time a firm start had been made on a policy of restraint, so that improvement of the situation seemed in prospect. Access to substantial liquidity was obtained from European central banks and the US Treasury; Italy's gold tranche in the IMF of \$225 million was drawn; and intermediate-term credits of \$450 million were arranged with the US Export-Import Bank and the Commodity Credit Corporation. In addition, negotiations were undertaken with the IBRD for a longer-term credit. Thus, the variety and volume of international financial resources, including private liquid funds, that were secured to help bridge the gap also showed the flexibility of the international financial system.

The details of these three cases give an insight into the operational meaning of the need for international liquidity. In practice, the need arises when there is selling pressure in the exchange market on one or more currencies, and liquidity — whether from official reserves or from borrowed resources — is the means that can be mobilised to contain the pressure. Of course, the more quickly and firmly steps are taken to restore equilibrium, the less need will there be to intervene in the exchange market. In any case the world total of international liquidity, however measured statistically, is only remotely related to the practical problems that both the deficit and the surplus countries must meet in managing the exchange markets. However large total reserves might be, their distribution is never likely to be ideal; and even ample reserves of a country in deficit may often have to be supplemented by outside resources to prevent deterioration of confidence and flight from the currency. The arrangements being made from month to month to meet these practical problems are giving a pragmatic demonstration of the rôle of co-operation among monetary authorities in the management of the international financial system.

PART II

MONETARY AND ECONOMIC SURVEY.

I. CREDIT DEVELOPMENTS AND POLICIES.

In the monetary sphere the past year has seen considerable progress towards the solution of certain problems, but also the emergence of some new ones.

In the United States the adoption of expansionary fiscal measures has, besides giving promise of sustained domestic growth, provided more freedom to adapt monetary policy to external ends. On the other hand, in western Europe and Japan, where little more than a year ago the tempo of activity had flagged, excessively rising demand has led to widespread recourse to measures of credit restraint. This has meant a renewed widening of interest rate differentials vis-à-vis the United States.

Among the continental European countries the problem of monetary policy has been further complicated by different degrees of demand pressure and the emergence of external payments imbalances. Within the Common Market, in particular, the requisites of integration have made it especially difficult for a surplus country, such as Germany, to use monetary restraint as a means of combating "imported" inflation. By the same token, it has become more important for a deficit country, such as Italy, to take all the necessary steps, including credit restrictions, to stop inflation at its origins.

Inflation has also accentuated the problem of developing and integrating Europe's capital markets. The progressive squeeze on profit margins in recent years, mitigated only by price inflation itself, has reduced industry's self-financing capacity, while the prospect of relatively low profit margins and further rising prices has made investors more reluctant to place funds at longer term.

In principle, the broad policy implications of these developments are fairly clear, and the authorities concerned have generally been moving in the appropriate directions. In countries with inflationary pressures it is important that fiscal restraint, leading to an increase in government saving, be given adequate emphasis. From the domestic point of view this has the advantage of facilitating a readier availability of both bank credit and capital-market funds for investment purposes, thus lessening the danger of provoking a slowing-down of growth. From the external point of view fiscal restraint helps to limit the rise in interest rates, thereby reducing the incentive for

further inflows of capital into Europe. To the extent that recourse to credit restrictions is necessary, the measures used should be designed so far as possible to avoid excessive capital inflows.

With regard to the United States, the implication for policy is rather that there may need to be a greater willingness to accept a somewhat higher structure of interest rates. The tax reduction of February 1964 has laid a firm basis for this, while greater caution in the credit field may also prove warranted on domestic grounds.

Comparative credit and capital-market developments.

New patterns of saving and investment. Underlying the strong demand for credit in continental Europe in recent years have been significant developments affecting both the sources and uses of investible funds. As regards the demand for funds, fixed capital investment continued to rise relative to gross national product up to 1962. Although industrial investment in plant and equipment weakened perceptibly in 1962 and early 1963, it remained high, and more recently it has shown signs of renewed advance. Almost everywhere the demand for housing has continued at inflationary levels. Inventory investment, on the other hand, was moderate in 1963 and much below the 1960-61 average — a fact that makes the external adjustment of these countries all the more notable.

With respect to the supply of funds, the central feature of recent years has been the decline in national saving ratios. In most cases this has been due primarily to a relative drop in gross business saving. The growth of international competition has kept industrial prices under considerable pressure, while the rise in wage and salary incomes has tended to run ahead of productivity gains. In 1963 rising commodity prices also contributed to the squeeze on profit margins.

Since the largest part of household income goes regularly into consumption, its relative increase at the expense of profits did not result in a compensating rise in personal saving. Nor was there any offset after 1961 from the side of public-sector saving, which instead tended to decline relative to gross national product.

For individual countries the behaviour of saving and investment components in relation to the gross national product is shown in the table on the next page.

Up to a point the trends just described were not unwelcome. For the continental countries with external surpluses the adjustment of saving to a level more in keeping with domestic investment contributed to an improved payments balance with the rest of the world. No doubt it has also made potentially for a better relation between profits and wages, provided that a stabilisation of the situation can be achieved. However, the adjustment forces tended last year to get out of hand, leading in some countries to excessive domestic demand and external deficits, actual or threatened.

Gross national saving and investment.

Countries	Years	Gross national saving			Total saving and investment	Gross national investment			
		House-holds	Enter-prises	Public author-ities		Gross domestic fixed capital formation		Change in stocks	Net external balance
						Housing	Plant and equip-ment		
as percentages of gross national product at market prices									
Belgium.	1960	9.5	10.2	— 0.2	19.5	5.8	12.8	0.7	0.2
	1961	8.2	10.5	0.8	19.5	6.0	12.8	0.7	0.0
	1962	8.4	10.4	1.0	19.8	5.7	13.1	0.5	0.5
	1963	.	.	.	19.2	5.6	13.3	0.6	— 0.3
Denmark	1960	15.6		6.0	21.6	3.2	16.2	3.4	— 1.2
	1961	16.8		3.5	20.3	3.6	17.0	1.5	— 1.8
	1962	14.3		5.1	19.4	3.6	17.0	2.3	— 3.5
	1963	.		.	19.8	3.4	16.2	0.2	0.0
Finland	1960	7.9	9.7	11.4	29.0	5.7	23.3	0.9	— 0.9
	1961	10.6	9.9	9.4	29.9	6.3	23.1	1.8	— 1.3
	1962	9.6	9.4	9.5	28.5	6.9	22.4	0.9	— 1.7
	1963	10.5	9.8	7.0	27.3	7.6	21.0	.	— 1.3
France	1960	8.9	8.8	5.1	22.8	4.7	14.0	2.4	1.7
	1961	8.1	8.5	5.4	22.0	4.8	14.8	0.9	1.5
	1962	9.2	8.3	4.4	21.9	4.7	14.9	1.6	0.7
	1963	8.5	7.9	4.6	21.0	5.0	14.8	1.1	0.1
Germany	1960	4.9	16.5	6.6	28.0	5.8	18.0	2.9	1.3
	1961	5.0	15.3	6.5	26.8	5.9	18.8	1.8	0.3
	1962	5.0	15.0	6.3	26.3	6.0	19.4	1.2	— 0.3
	1963	5.5	15.0	5.8	26.3	6.1	19.0	1.2	0.0
Italy	1960	22.4		3.6	26.0	5.8	17.5	1.6	1.1
	1961	22.8		4.3	27.1	5.9	18.3	1.4	1.5
	1962	22.2		4.4	26.6	6.5	18.1	1.3	0.7
	1963	19.6		4.1	23.7	6.8	17.5	0.9	— 1.5
Netherlands . . .	1960	9.5	14.4	5.9	29.8	4.2	19.4	3.3	2.9
	1961	8.2	13.6	6.8	28.6	4.1	20.1	2.9	1.5
	1962	8.0	12.8	6.1	26.9	3.9	20.4	1.2	1.4
	1963	8.2	12.7	5.4	26.3	4.0	20.4	0.9	1.0
Norway	1960	16.8		9.9	26.7	3.9	23.9	1.3	— 2.4
	1961	16.6		10.1	26.7	4.1	25.1	1.3	— 3.8
	1962	15.5		10.2	25.7	4.2	24.6	0.2	— 3.3
	1963	15.8		9.6	25.4	4.1	25.8	— 0.9	— 3.6
Sweden	1960	4.3	12.7	6.5	23.5	5.2	17.0	2.2	— 0.9
	1961	4.5	11.7	8.0	24.2	5.3	17.2	1.6	0.1
	1962	5.1	9.0	8.9	23.0	5.5	17.1	0.6	— 0.2
	1963	5.0	17.4		22.4	5.7	17.3	— 0.2	— 0.4
Switzerland . . .	1960	4.6	7.6	13.9	26.1	6.9	15.9	2.6	0.7
	1961	5.4	7.5	14.0	26.9	7.4	18.9	3.2	— 2.6
	1962	4.0	7.4	14.9	26.3	7.0	20.7	2.1	— 3.4
	1963	.	.	.	25.7	7.0	20.8	1.5	— 3.6
United Kingdom .	1960	5.2	11.2	2.3	17.5 ¹	3.0	13.2	2.3	— 1.0
	1961	6.3	9.4	2.5	18.0 ¹	3.0	13.9	1.1	— 0.0
	1962	5.4	8.8	3.6	17.2 ¹	3.1	13.4	0.3	0.4
	1963	5.8	9.5	2.3	17.0 ¹	3.1	13.0	0.5	0.4
United States . .	1960	4.3	10.1	3.7 ²	17.4 ¹	4.3 ²	12.1 ²	0.7	0.3
	1961	5.3	9.8	2.1 ²	16.9 ¹	4.2 ²	11.8 ²	0.3	0.6
	1962	5.2	10.4	2.2 ²	17.5 ¹	4.3 ²	11.8 ²	1.0	0.4
	1963	5.0	10.4	2.7 ²	17.5 ¹	4.4 ²	11.8 ²	0.8	0.5
Japan.	1960	17.1	13.2	8.2	36.9 ¹	2.3	29.2	5.0	0.4
	1961	18.0	14.1	9.8	41.4 ¹	2.5	32.2	8.8	— 2.1
	1962	17.8	12.4	9.6	38.3 ¹	2.7	32.0	3.7	— 0.1
	1963 ³	.	.	.	34.2 ¹	3.4	28.9	3.5	— 1.6

¹ Including a residual error. ² Including, as an element of both saving and investment, new civil public construction. ³ January-September.

Although the proportionate decline in total saving had been going on for some time, most continental countries early in 1963 were still pursuing relatively easy credit policies. This was partly because of their still strong external positions, but partly also because of their desire to sustain private investment, the profitable opportunities for which had declined in some sectors. In addition, there was a separate, but related, need to accommodate the shift by business firms from internal to external sources of finance. During 1963, however, the cumulative rise of wages and consumption contributed to domestic inflation and its transmission internationally via import demand. Fiscal policy, already tilted in the wrong direction in some countries in response to the earlier weakening of private investment, could not be readily reversed. In these circumstances credit policy had to be shifted quickly in many countries from relative ease to substantial restraint.

In the United States and the United Kingdom events have moved along different lines. At the turn of 1962-63 overall saving propensities were clearly in excess of domestic investment demand. But instead of being associated with an external surplus, as had earlier been the case on the Continent, the saving potential was running to waste in the form of idle domestic resources. Since that time growth has accelerated in both countries, partly as a result of expansionary fiscal policies, and has led to a buoyant recovery in business saving.

Bank credit and liquid-asset formation. A striking feature of the cyclical phase 1958-63 was the large expansion of bank credit. Total bank credit rose in absolute terms during this period two or three times as much as in the expansion of 1952-57, and the increases were usually also much bigger in percentage terms. In some countries, such as France, Italy and Finland, the large 1958-63 increase was proportionately about the same as earlier. It was also impressive in Germany, even against the exceptional rise in 1952-57.

The growth of bank credit in 1958-63, and with it the banks' deposit liabilities, was linked with the imbalance in international payments. In the United States the monetary authorities, with a view to promoting a fuller utilisation of resources, more than offset the effects of the steady gold outflow on the credit base. In the western European countries rising net foreign assets of the banking system formed an important counterpart to the growth of domestic liquid assets of the public. Thus not only was the total expansion of bank credit in 1958-63 generally larger than in 1952-57 but the proportion of the increase that was based on the acquisition of net foreign assets was often much bigger than in the earlier period. As shown in the table, this proportion ranged from around 10 per cent. (Finland, Germany, Italy, Norway and Sweden) to 30 per cent. or more (Austria, France and the Netherlands).

The influence of foreign exchange gains is seen in sharper focus if one looks only at the rise in official reserve holdings compared with the increase in the domestic money supply. In all the continental countries except

The expansion of bank assets.

Countries	Periods	Overall increase		Proportion of increase due to change in		
		in milliards of national currency units	in per- centages	net foreign assets	credit to government sector	credit to private sector
Austria	1958-1963	62.2	109.4	29.2	22.0	48.8
Belgium	1952-1957	45.9	24.2	22.6	38.6	38.8
	1958-1963	125.0	53.0	17.1	50.5	32.4
Denmark	1952-1957	3.8	27.5	6.3	3.6	90.1
	1958-1963	13.7	77.2	17.5	— 5.3	87.8
Finland	1952-1957	2.3	83.7	— 1.7	2.7	99.0
	1958-1963	4.4	88.7	10.8	— 2.6	91.8
France	1952-1957	38.4	103.1	— 7.0	37.4	69.6
	1958-1963	88.4	116.9	27.7	12.8	59.5
Germany	1952-1957	78.2	189.8	25.3	5.8	68.9
	1958-1963	124.5	104.3	11.7	9.8	78.5
Italy	1952-1957	4,668	110.0	4.0	26.3	69.7
	1958-1963	12,150	128.4	7.5	13.8	78.7
Netherlands	1952-1957	1.9	15.5	121.5	—146.6	125.1
	1958-1963	11.3	79.3	44.0	6.1	49.9
Norway	1952-1957	3.6	26.4	12.9	5.0	82.1
	1958-1963	7.1	41.4	12.7	3.9	83.4
Spain	1954-1957	129.6	79.8	— 5.1	44.7	60.4
	1958-1963	380.3	130.2	20.0	10.5	69.5
Sweden	1952-1957	12.3	42.8	9.1	30.2	60.7
	1958-1963	22.7	55.4	7.0	8.0	85.0
Switzerland	1952-1957	11.3	41.0	9.7	15.8	74.5
	1958-1963	29.1	74.7	18.3	9.1	72.6
United Kingdom . . .	1952-1957	0.9	10.1	— 11.7	122.7	— 11.0
	1958-1963	2.4	23.9	16.5	— 34.9	118.4
United States	1952-1957	38.9	21.7	1.0	6.2	92.8
	1958-1963	81.4	37.3	— 11.1	37.1	74.0
Canada	1952-1957	2.9	34.5	—	— 5.9	105.9
	1958-1963	4.7	41.8	18.5	13.7	67.8
Japan	1953-1957	3,814	93.2	— 1.8	10.6	91.2
	1958-1963	17,956	227.1	1.8	3.4	94.8

Source: IMF, *International Financial Statistics*, "Monetary Survey".

Germany the increase in the central bank's foreign exchange assets was much greater in 1958-63 than in 1952-57, and the same was true of the percentage growth in the money supply. In France, it is true, the money supply increased almost as much in the earlier period, when the net change in foreign assets was negligible; this reflects the inflation of the years 1956-57.

As the next table shows, there has been in practice a connection, though a rather loose one, between reserve gains and the increases in the money supply of most continental countries. This connection arises, of course, from the fact that the central bank must create domestic money to acquire the foreign exchange assets and this money in turn makes possible a multiple expansion of bank deposits and credit. The monetary authorities may offset all or part of the impact of the exchange inflow, and some countries did this to better effect than others.

Changes in official holdings
of foreign assets and in money supply.

Countries	Change in official foreign assets		Increase in currency and sight deposits			
	1952-57	1958-63	1952-57	1958-63	1952-57	1958-63
	in milliards of national currency units				in percentages	
Belgium	6.10	43.70	29.40	80.90	17	41
Denmark	0.37	2.10	1.06	6.09	15	77
Finland	0.06	0.56	0.18	0.82	18	70
France	0.34	21.23	34.42	78.26	93	110
Germany	21.50	10.10	15.90	27.10	83	77
Italy*	0.19	1.77	2.31	6.46	79	123
Netherlands	1.64	3.59	2.03	5.26	29	58
Norway	0.24	1.25	1.25	2.42	22	35
Sweden	— 0.14	1.54	1.64	5.62	20	56
Switzerland	1.93	5.36	3.08	11.46	26	76

* In thousands of milliards.

It must be recognised, on the other hand, that under convertibility the extent to which exchange inflows can be offset is circumscribed by monetary conditions elsewhere. Germany's unsuccessful efforts at monetary restraint in 1959-60 are a vivid reminder of this. Still, it would be going too far to say that present inflationary tendencies in Europe have been the inevitable outgrowth of previous inflows of exchange. Clearly, in a number of countries greater budget and monetary restraint, particularly during the last two years, would have helped to limit excessive demand.

To put this matter in its proper perspective, however, it should be noted that total bank credit expansion in most western European countries in 1958-63 was not to any great extent ascribable to the growth of credit to the public sector. Generally speaking, budget positions were stronger than in the years 1952-57. In many countries — Denmark, Finland, France, Italy, Norway, Sweden, Switzerland and the United Kingdom — public-sector net recourse to bank credit in 1958-63 was substantially below that in 1952-57 and in some cases was even negative (see page 35). Though this was not true of Germany and the Netherlands, the 1958-63 increase in these two countries was modest and it partly reflected credit to local authorities. Only in Belgium was bank credit to the public sector large — in fact, greater than in 1952-57. Public-debt funding operations also helped to keep down bank claims against the public sector in some countries, notably the Netherlands, Sweden and the United Kingdom.

Rather, it was the growth of bank credit to the private sector that, together with the increase in foreign assets, accounted for the large creation of liquid assets in 1958-63. Although its basis was provided by the foreign exchange inflows, the rapid expansion of private credit did not get under way until late 1959 with the resumption of heavy investment outlays. Subsequently, the business sector's demand for credit continued to grow as

investible funds from internal sources declined relative to overall requirements. Heavy credit demands were also widely associated with the boom in housing and land values, the steep upward trend in durable consumer goods expenditure and the financing of a growing volume of trade turnover at gradually higher prices.

These credit trends are reflected in the graph on the next page, which compares the actual percentage rates of increase of the banking system's deposit liabilities with their implicit increase in so far as associated with the expansion of private-sector credit alone. Thus the gap between the two lines indicates the extent to which the expansion of money and quasi-money is linked with the growth of the banks' foreign assets and of their claims on the public sector.

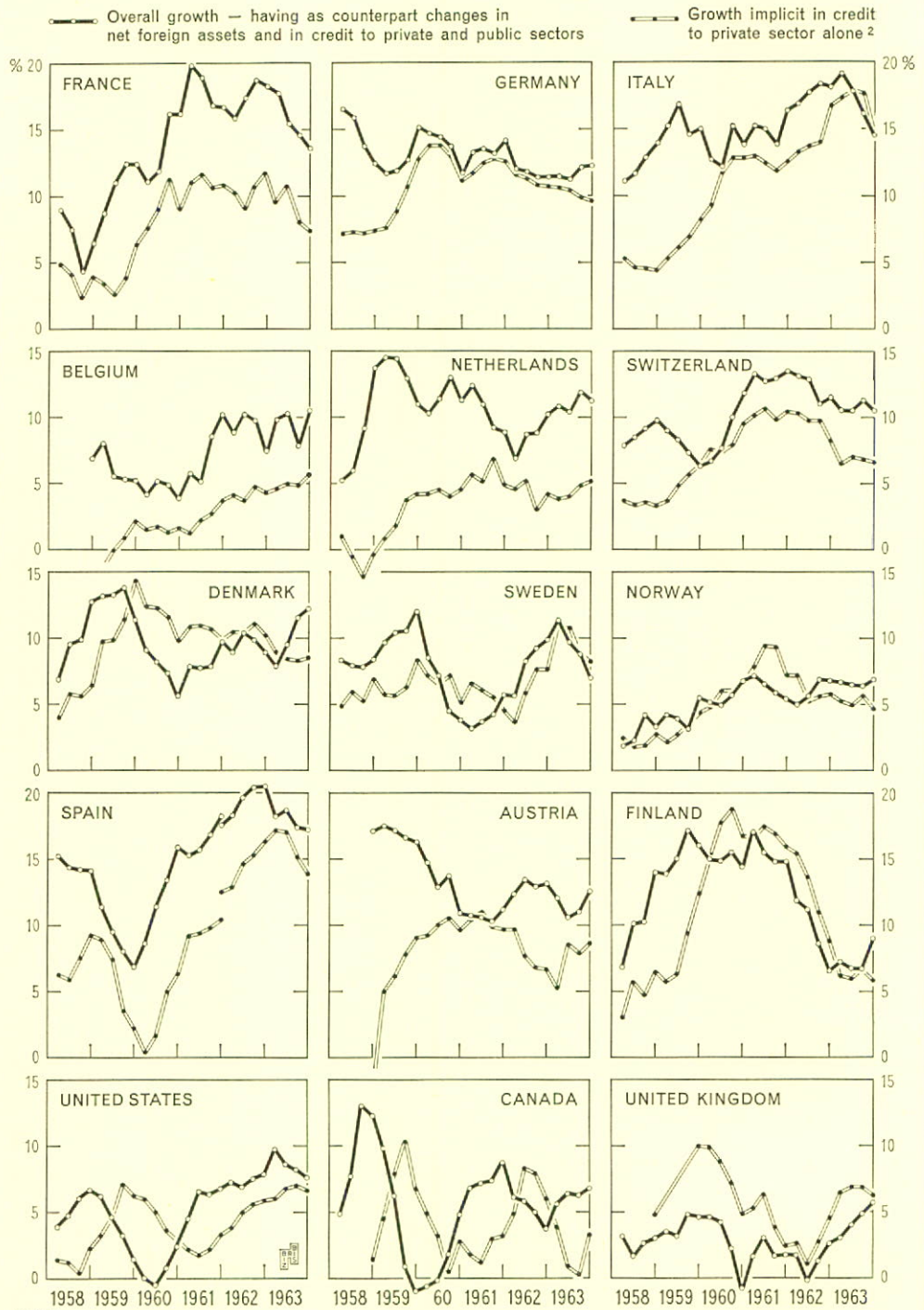
Largely owing to the inflow of foreign exchange, the rate of liquid-asset formation was already quite high in a number of countries in the years 1958-59. From late 1959 onwards, however, liquid-asset formation came to depend increasingly upon the marked growth in credit to the private sector. In some countries the uptrend in private credit, combined with the recurrence of exchange inflows, brought the rate of growth of liquid assets to new peak levels (France, Italy, Belgium, Switzerland and Spain).

The experience of individual countries over these years reflects wide differences of policy and circumstance, which cannot be gone into in detail. However, it is of interest to note that in Germany, where through its budget the central government absorbed funds domestically and used them mostly to make net payments abroad, the growth rate of liquid assets has in recent years been closely related to that of credit to the private sector. In France, with the help of a new compulsory assets ratio (the "coefficient de trésorerie") introduced in January 1961, the growth of liquid assets ascribable to private-sector bank credit was kept to about 10 per cent. a year. In Italy, on the other hand, this percentage generally ran higher and rose to upwards of 17 per cent.

Looking at more recent trends, liquid-asset formation has now slowed down in France, Italy, Switzerland, Sweden, Spain and Finland. Switzerland in April 1962 and France in March 1963 imposed ceilings on the permissible rate of bank credit expansion, and these ceilings were subsequently lowered. In Spain reserve requirements were introduced in the spring of 1963. In Italy, where there was some delay before the introduction of credit restraint, the authorities began in the late summer of 1963 to allow the external deficit to have some effect on the credit base. In Sweden both external reserve losses and public debt management operations have curtailed the growth of liquidity. In Finland the squeeze has been primarily associated with government deficit financing outside the banking system.

In Belgium from early 1961 and in the Netherlands from the spring of 1963 liquid-asset formation accelerated in conjunction with a speeding-up of credit to the private sector. In the autumn the Netherlands authorities reintroduced a ceiling on the permissible rate of credit expansion to the

Rate of growth of monetary and quasi-monetary liabilities.¹



¹ By quarters, as percentage change over corresponding quarter of preceding year. ² Lending to the private sector is assumed to have a counterpart only in monetary and quasi-monetary liabilities. In the case of Germany, however, where long-term liabilities are especially important, these have been included as a quasi-monetary liability.

private economy, and in Belgium a gentleman's agreement was worked out along similar lines early in 1964.

In three other countries — Germany, Austria and Denmark — liquid-asset formation also speeded up during 1963. Whereas in Germany and Denmark this was ascribable mainly to the renewed influx of foreign exchange, in Austria both exchange gains and an acceleration of private credit were involved.

In the United States deliberate policy actions have kept domestic liquidity creation rather independent of the external deficit. Monetary restraint was applied for domestic reasons in 1959, but since the adoption of credit ease in early 1960 liquid-asset formation has been very substantial. The contractive effects of the gold losses have been offset by a combination of open-market security purchases and reductions in reserve requirements. During 1963, however, bank liquidity tended to tighten under the influence of a slightly less easy credit policy.

In the United Kingdom, given the offsetting operations of the Exchange Equalisation Account, the link between the external position and domestic liquidity creation is less automatic than in most continental countries. In practice, however, the alternating periods of monetary tightness and ease during 1958-63 were closely related to deterioration and improvement in the external accounts. During much of this period, moreover, a continuing official objective was to fund public debt, which also served to restrain the growth of liquid assets. Thus deposit formation at the banks was less than the growth of private credit, leading the banks to run down their security holdings. In the course of 1962-63, as the external position improved, credit policy was eased and both bank advances and deposit formation accelerated. Following the Bank rate increase in February 1964, there was some slowing-down in the growth of advances, but, with larger government expenditure not wholly offset by greater sales of public debt, deposits went on rising.

Although liquid-asset formation has begun to slow down in some countries in response to credit restraint measures, the very scale on which these assets have been created in recent years represents a potential source of inflation. Thus, in most countries last year liquid assets continued to grow, or at least hold steady, relative to the gross national product, despite the rise in prices. Since the figures in the following table are annual averages, and since most restrictive measures were taken after the middle of the year, these ratios do not reflect more recent trends. They do tend to show, however, that credit remained relatively easy in many countries during much of 1963, leading also to a declining or stable trend of interest rates (France, Germany, the Netherlands, Sweden, Switzerland, Canada and the United Kingdom) up to about the middle of the year (see graph on page 50). Indeed, during the entire expansionary phase, except for isolated periods of monetary restraint such as that in Germany in 1959-60 and that in Belgium and Sweden in 1960-61, interest rates in most continental countries remained

near, or even below, the 1958 recession level. After the middle of 1963, however, the upsurge of demand, combined in many continental countries with recourse to monetary restraint measures, led to a rising trend of long-term interest rates. In the United Kingdom, where monetary restrictions were

Money supply, quasi-money and gross national product.¹

Countries	Years	Money supply			Quasi-money ²	Money and quasi-money	Gross national product (at market prices)	Money supply	Quasi-money
		Currency	Demand deposits	Total					
		in milliards of national currency units						as percentages of GNP	
Austria	1961	19.8	15.2	35.0	42.2	77.3	177.9	19.7	23.7
	1962	21.6	16.9	38.5	48.9	87.4	186.9	20.6	26.1
	1963	23.3	18.3	41.6	55.9	97.5	199.3	20.9	28.0
Belgium.	1961	128.7	100.2	228.9	48.2	277.1	601.2	38.1	8.0
	1962	136.2	109.4	245.6	56.5	302.1	637.2	38.5	8.9
	1963	149.3	121.4	270.7	60.8	331.5	683.5	39.6	8.9
Denmark	1961	2.8	8.1	10.9	11.4	22.3	45.3	24.2	25.1
	1962	3.1	9.0	12.1	12.4	24.5	50.9	23.7	24.3
	1963	3.3	10.0	13.3	13.6	26.9	54.3	24.5	25.1
Finland	1961	0.7	0.8	1.5	5.6	7.1	15.9	9.6	34.9
	1962	0.7	0.9	1.6	6.2	7.8	17.0	9.5	36.4
	1963	0.8	1.0	1.8	6.5	8.3	18.4	9.8	35.7
France	1961	42.2	59.4	101.6	10.9	112.5	319.7	31.8	3.4
	1962	47.6	71.1	118.7	13.0	131.7	356.3	33.3	3.7
	1963	53.7	84.5	138.2	14.5	152.7	391.8	35.3	3.7
Germany	1961	21.9	27.0	48.9	64.8	113.7	326.2	15.0	19.9
	1962	23.7	30.5	54.2	72.6	126.8	354.8	15.3	20.5
	1963	25.2	32.7	57.9	83.2	141.1	376.8	15.4	22.1
Italy	1961	2,466	5,286	7,753	6,021	13,774	21,083	36.8	28.6
	1962	2,813	6,331	9,144	7,082	16,226	23,754	38.5	29.8
	1963	3,310	7,500	10,810	8,140	18,950	26,930	40.1	30.2
Netherlands . . .	1961	5.2	6.6	11.8	14.6	26.4	44.9	26.3	32.6
	1962	5.6	6.9	12.5	16.3	28.8	47.7	26.2	34.1
	1963	6.2	7.6	13.8	18.2	32.0	51.6	26.6	35.2
Norway	1961	3.6	3.9	7.5	11.9	19.4	34.9	21.5	34.1
	1962	3.9	4.2	8.1	12.6	20.7	37.5	21.5	33.5
	1963	4.1	4.4	8.5	13.4	21.9	40.0	21.2	33.6
Sweden	1961	6.5	5.3	11.8	37.4	49.2	68.6	17.2	54.5
	1962	6.8	6.0	12.8	40.4	53.2	74.2	17.3	54.4
	1963	7.3	6.5	13.8	44.3	58.1	79.5	17.4	55.7
Switzerland . . .	1961	7.3	12.8	20.1	30.0	50.1	41.5	48.6	72.2
	1962	8.1	14.6	22.7	33.6	56.3	46.3	48.8	72.6
	1963	8.7	15.9	24.6	37.7	62.3	50.5	48.7	74.6
United Kingdom .	1961	2.1	6.9	9.0	.	.	27.1	33.4	.
	1962	2.1	7.0	9.1	.	.	28.3	32.3	.
	1963	2.2	7.3	9.5	.	.	29.8	31.9	.
Canada	1961	1.9	4.5	6.4	7.6	14.0	37.4	17.1	20.2
	1962	2.0	4.7	6.7	8.0	14.7	40.3	16.7	19.8
	1963	2.0	5.2	7.2	8.4	15.6	43.0	16.9	19.4
United States . .	1961	29.1	114.0	143.1	78.5	221.6	518.2	27.6	15.1
	1962	30.1	115.9	146.0	91.0	237.0	554.9	26.3	16.4
	1963	31.5	119.0	150.5	105.3	255.8	585.1	25.7	18.0

¹ The figures for the money supply and quasi-money are annual averages. ² Includes only the quasi-monetary liabilities of the deposit banks as defined in the IMF's "Monetary Survey" data. In the United Kingdom time deposits, which are at seven days' notice, are included under demand deposits.

not a factor, the yield on industrial bonds, after reaching a low in the autumn, increased markedly in subsequent months, while in the United States there was a more gradual upward trend over the year as a whole.

Capital-market problems and policies. In the light of the trends described in the preceding pages, the growing preoccupation on the Continent with the need to promote the flow of funds into longer-term channels is readily understandable. The reduced scale of self-financing, the public's preference for liquid financial assets and, in some cases, the public sector's greater recourse to the credit markets have all impinged upon the supply of industrial growth capital. Because inflation has helped to sustain profit margins, the problem has not yet been seen in its full dimensions. Moreover, inflation itself tends to undermine a vital prerequisite for a healthy capital market: a consistent, convincing record of price stability. In this respect 1963 was a setback.

In view of the major differences in national financial structures, inter-country comparisons of capital-market activity are hazardous. In the table on the next page, for instance, mortgage financing is not included for the United States and some European countries, whereas in a number of other countries bond issues to raise mortgage funds often play an important rôle. In addition, in some countries, such as France, Italy and Belgium, semi-public credit institutions, which borrow under favourable conditions and re-lend the proceeds mostly to private industry, are a significant factor in the capital market. For countries individually, however, it may be seen that by 1962 net new issues, expressed as a percentage of the gross national product, were quite substantial, and in some countries well above the average for the years 1956-58.

Over the past year the forces bearing on various capital markets, though diverse, were generally constrictive in their implications. In some cases monetary restraint was itself an overriding consideration. Thus in France the Treasury, after having refrained for four years from capital-market borrowing, issued two loans in 1963 for a total of Fr.fr. 3 milliard, primarily in order to reduce liquidity. Similarly, in Sweden the government issued several loans in late 1963 and early 1964, partly in order to reduce bank liquidity. In the Netherlands the Treasury also withdrew liquidity from the market in 1963 with an autumn loan in excess of its needs.

In some countries the public sector's greater financial needs curtailed the availability of capital-market funds. This was true in Germany and Sweden and also of local authorities in Switzerland. In Switzerland, too, there was a reduction in the Confederation's budget surplus last year and a smaller return flow of funds to the market via debt redemption. In Belgium the Treasury was faced with a double burden: a large deficit and the necessity of financing it mainly through short-term foreign credits channelled via the banks. Throughout the year the capital market was under the shadow of the fiscal reform of late 1962, which imposed withholding taxes on income from new issues, but the situation improved in the early months of 1964.

Capital market: Net issues.

Countries	Annual averages or years	Public		Private ¹		Foreign issues	Total	Private issues	Total new issues
		State	Local authorities and public bodies	Shares	Bonds				
Belgium	1956-58	6.5 ²	7.3	6.7	10.5	—	31.0	3.4	6.1
	1959-61	11.0 ²	7.4	6.2	10.3	—	34.9	2.9	6.1
	1962	17.9 ²	11.5	7.7	10.1	—	47.2	2.8	7.4
	1963	2.9 ²	7.2	5.3	10.3	—	25.7	2.3	3.8
Denmark	1956-58	0.08	—	0.10	0.84	—	1.03	2.9	3.1
	1959-61	— 0.18	—	0.15	1.78	—	1.75	4.6	4.1
	1962	— 0.18	—	0.13	2.92	—	2.87	6.0	5.6
	1963	— 0.19	—	0.13	3.80	—	3.74	7.2	6.9
France	1956-58	2.02	— 0.01	2.02	2.60	—	6.63	2.1	3.1
	1959-61	— 0.94	— 0.01	2.95	3.77	—	5.77	2.3	2.0
	1962	— 0.86	0.03	3.99	4.22	—	7.38	2.3	2.1
	1963	2.09	0.15	4.18	4.92	0.06	11.40	2.3	2.9
Germany	1956-58	— 0.18 ³	0.80	1.54	3.71	0.04	5.90	2.4	2.7
	1959-61	0.42 ³	0.91	1.82	5.12	0.13	8.41	2.5	3.1
	1962	0.66 ³	1.81	1.51	7.06	0.10	11.14	2.6	3.4
	1963	1.80 ³	1.78	1.02	8.48	0.11	13.19	2.7	3.7
Italy	1956-58	87	— 6	190	292	—	563	3.1	3.7
	1959-61	134	83	379	587	5	1,189	5.0	6.2
	1962	— 108	170	608	942	30	1,642	6.5	6.9
	1963	— 200	128	252	1,152	15	1,347	5.2	5.0
Netherlands . . .	1956-58	0.01 ⁴	0.42	0.37	0.25	— 0.04	1.00	1.7	2.8
	1959-61	0.46 ⁴	0.52	0.13	0.11	0.13	1.34	0.6	3.2
	1962	— 0.09 ⁴	0.20	0.46	0.30	0.14	1.01	1.6	2.1
	1963	0.60 ⁴	0.40	0.07	— 0.02	— 0.12	0.93	0.1	1.8
Sweden	1956-58	0.58 ⁵	0.04	0.28	0.68	—	1.58	1.8	3.0
	1959-61	0.45 ⁵	0.02	0.52	1.07	—	2.06	2.5	3.2
	1962	— 0.51 ⁵	0.23	0.80	3.03	—	3.55	5.2	4.8
	1963	0.87 ⁵	0.43	0.55	1.75	—	3.60	2.9	4.2
Switzerland . . .	1956-58	— 0.41	0.18 ⁶	0.25 ⁶	0.85 ⁶	0.14	1.01	3.5	3.2
	1959-61	— 0.21	0.10 ⁶	1.05 ⁶	0.99 ⁶	0.63	2.57	5.4	6.8
	1962	— 0.26	0.18 ⁶	1.81 ⁶	1.11 ⁶	0.44	3.28	6.3	7.1
	1963	— 0.08	0.26 ⁶	1.53 ⁶	2.19 ⁶	0.53	4.43	7.4	8.9
United Kingdom .	1956-58	0.06 ⁷	0.04	0.14	0.19	0.01	0.37	1.2	1.7
	1959-61	— 0.22 ⁷	0.04	0.35	0.12	0.01	0.29	1.8	1.1
	1962	0.57 ⁷	0.14	0.26	0.17	—	1.14	1.5	4.0
	1963	— 0.13 ⁷	0.09	0.20	0.23	0.02	0.41	1.4	1.4
United States . .	1956-58	— 1.0 ⁸	4.2	3.6	5.9	0.7	13.4	2.1	3.0
	1959-61	0.4 ⁸	4.2	4.0	4.7	0.7	14.1	1.7	2.8
	1962	1.5 ⁸	4.7	2.4	5.0	1.0	14.6	1.3	2.6
	1963	2.5 ⁸	6.2	1.0	5.6	1.1	16.4	1.1	2.8
Canada	1956-58	0.21 ⁹	0.84	0.51	0.81	—	2.36	4.1	7.4
	1959-61	0.95 ⁹	0.91	0.29	0.27	—	2.42	1.5	6.7
	1962	0.77 ⁹	0.88	0.34	0.42	—	2.41	1.9	6.0
	1963	0.98 ⁹	1.15	— 0.10	0.58	—	2.61	1.1	6.1

¹ Includes issues of semi-public credit institutions and nationalised industries. ² Change in medium and long-term direct debt. ³ Change in market holdings of bonded loans and premium Treasury bonds. ⁴ Excludes payments into pre-subscription accounts. ⁵ Change in funded debt. ⁶ Includes privately-placed issues. ⁷ Change in marketable debt (excluding Treasury bills) in public hands. ⁸ Change in public holdings of marketable debt having a maturity of one year or more. ⁹ Held outside government accounts.

In Italy new issues declined substantially in 1963, partly as a reaction to the previous year's decisions to nationalise the electricity sector and to impose a coupon tax on dividends. In January 1963, as in 1962, the Treasury redeemed long-term debt, while up to about the middle of 1963 credit ease permitted the banks to make large security purchases. Since that time, however, bank support to the market has been reduced. In Germany the ease with which the market absorbed a substantial rise in new issues in the years 1962-63 partly reflected the large influx of foreign capital. In Switzerland the increase in new issue activity last year was accounted for largely by banks' bond flotations — a new development which became necessary as a means of attracting loanable funds.

In the United States 1963 saw an increase in net new issues, mostly by State and local governments, finance companies and, in the first six months, foreign borrowers. From the demand side the main support, apart from insurance and pension fund buying, came from the commercial banks, which through higher creditor rates attracted an exceptional increase in time and savings deposits. In the United Kingdom the authorities made net purchases of longer-term government securities from the market last year, after having been large net sellers in 1962.

As regards foreign issues in domestic markets, developments in 1963 were of a mixed character. In the United States the New York market dried up following the proposal of the interest equalisation tax in July 1963, but when this proposal is enacted some revival of foreign issues is expected. In Switzerland the excessive domestic demand for capital led the authorities to adopt a stricter attitude towards foreign issues on the Swiss market. The same was true in the Netherlands — the third main country that had previously allowed significant scope for foreign issues. In these circumstances various experiments were made in Europe last year with issues expressed in foreign currencies and units of account. The best reception has so far been accorded to dollar loans; approximately \$200 million's worth was floated in London between the autumn of 1963 and April 1964.

Viewed from the domestic angle, it is clearly in their own interests for European countries to strengthen their capital markets. However, capital-market activity is not an end in itself. More fundamental to rapid, stable growth is the overall level and composition of saving and investment, and on this score European countries had an enviable record during most of the post-war period. Many of the basic techniques employed to increase total saving have as a by-product tended to restrict individuals' placements of funds on the capital market. For instance, large current-account budget surpluses have limited private saving potential and hence security purchases, though they have also meant higher aggregate saving. Various techniques used to increase the availability of funds for self-financing — accelerated depreciation schedules, investment allowances and relatively low profits taxes — also tended to promote saving. Finally, personal saving incentive schemes in some cases increased the total of such saving while reducing the share placed directly on the capital market.

In view of these considerations, the pressing problem for many countries is to find ways to bring about a better equilibrium between saving and investment. The most important means to this end is a return to larger current-account budget surpluses, which may be combined also with a spacing-out of public investment programmes. This approach, already being followed in a number of countries, frees the capital market for private borrowers and — what may also be helpful on international grounds — puts downward pressure on interest rates. A second requisite for the strengthening of capital markets is the maintenance of adequate differentials between short and long-term interest rates — though on equilibrium grounds this might imply a higher effective level of long-term rates than has recently prevailed in some countries.

Beyond this there are, of course, a number of technical possibilities for improving the breadth and efficiency of capital markets in different countries. The granting of more freedom with respect to institutional investment portfolios, the provision of more competitive underwriting facilities, the removal of heavy special taxes on new issues, the introduction of new capital-market instruments suited to the needs of borrower and lender alike, all provide opportunities for further progress.

The extent to which the strengthening of national capital markets leads to their closer integration with each other is still another matter. While there is already a high degree of freedom in Europe with respect to most forms of international capital movements, individual countries (except Germany) continue to regulate foreign new issues on their domestic capital markets. This is done partly for domestic reasons — to ensure the priority of domestic over foreign borrowers — and partly for external reasons — to ensure that foreign lending is compensatory with respect to other items in the balance of payments. However, assuming that present European stabilisation efforts are successful, it is reasonable to hope that national capital-market objectives will become increasingly leavened with those of an international character. In the past European countries have shown considerable resourcefulness in generating high levels of saving, and they may expect to derive mutual benefits from any concerted effort to broaden the pool of international capital.

Credit policies in individual countries.

United States. The buoyant domestic expansion of the past year has made it easier to adapt monetary policy to the requirements of the balance of payments. Already in December 1962 the Federal Reserve authorities had decided slightly to reduce credit ease, and their subsequent actions were reflected in a decline in member banks' free reserves (i.e. excess reserves minus borrowing) from about \$400 to 300 million during the early months of 1963. Coincident with the sharp second-quarter deterioration in the balance of payments, the authorities promoted a further tightening of bank reserves, which was soon followed by the raising of the discount rate from 3 to 3½ per cent. on 17th July. At the same time, the interest ceilings under

Regulation Q were further relaxed so as to permit the payment of up to 4 per cent. on time deposits at three to twelve months, instead of $2\frac{1}{2}$ – $3\frac{1}{2}$ per cent. as before. Finally, in early November the Federal Reserve Board raised the cash margin requirement for security purchases from 50 to 70 per cent. Reflecting the moderate firming-up of policy, the banks' free reserves dropped to about \$100 million in August 1963 and have since fluctuated around that level.

To deal more directly with the persisting conflict of domestic and external objectives, the authorities introduced in July 1963 their proposal for an interest equalisation tax. This measure is to be regarded primarily as a monetary expedient, since its purpose is to limit the outflow of capital by means other than a rise in long-term rates of interest, which has been viewed as being undesirable on domestic grounds. The levy is to apply retroactively from August 1963 until the end of 1965 on US purchases from foreigners of new or outstanding foreign securities. It would range from $2\frac{3}{4}$ to 15 per cent. on debt obligations maturing in from 3 to $28\frac{1}{2}$ years and would increase by approximately 1 per cent. the annual cost to foreigners of new issues in the United States. The tax would not apply to securities of underdeveloped countries, to US direct investments abroad or to short-term lending at up to three years.

Largely in consequence of 1963 policy developments, the picture as regards interest rates has altered considerably. The yield on three-month Treasury bills, which had stood at $2\frac{3}{4}$ per cent. in October 1962, generally remained above $3\frac{1}{2}$ per cent. in late 1963 and early 1964. The yield on long-term government securities, which was about 3.9 per cent. at the beginning of 1963, edged upwards throughout the year, but held steady at about 4.15 per cent. early in 1964. As regards bank loans, the prime lending rate remained unchanged at $4\frac{1}{2}$ per cent., the level to which it had been reduced in 1960. In short, while the placement of short-term funds was made more attractive for foreign and domestic financial investors alike, and foreign new issue costs were made subject to an impending rise, the cost of bank loans and long-term funds for domestic borrowers changed relatively little.

Nor was the availability of domestic credit impaired by last year's policy measures. Net funds raised by non-financial sectors in the credit and equity markets totalled \$62 milliard, compared with \$58 milliard in 1962 and a previous peak of \$53 milliard in 1959. Of this total, only a small part was accounted for by the financing of the Federal Government's cash deficit, which declined to \$4.6 milliard in 1963 from \$5.7 milliard in 1962. Most of the financing of the deficit fell indirectly to the Federal Reserve System, which increased its government security holdings by \$3.2 milliard in 1963 in order to compensate the gold outflow and provide the additional margin of bank reserves needed to support last year's credit growth.

Commercial banks increased their total loans and investments in 1963 by \$18.6 milliard, or 8 per cent., approximately the same rate as in

1962 and 1961. A large growth of time and savings deposits facilitated this increase, which, in conjunction with the higher rates paid on these deposits, encouraged the banks to shift towards higher-yielding assets. The bulk of new lending went into mortgage loans, tax-exempt State and local government securities, loans to public utilities and consumer credit. Because of rising profits, combined with the benefits arising from the new investment credit facility and revised depreciation rules introduced in 1962, business demand for bank credit remained modest. The stress laid on more profitable, longer-term lending led the banks to reduce their holdings of Treasury bills and other government securities by \$3.1 milliard. At the end of 1963 their holdings of short-term Federal Government securities were down to 7.5 per cent. of total deposits, compared with 11.2 per cent. two years earlier.

Although individuals and companies showed a greater preference for time and savings deposits in 1963, capital-market activity increased, thanks to the longer-term lending operations of financial institutions. Mortgage loans expanded by \$28.1 milliard, against \$24.8 milliard in 1962 and \$18.6 milliard in 1961. State and local obligations rose by \$6.7 milliard, compared with \$5.1 milliard in the preceding year. However, in view of the greater availability of internal funds, corporations borrowed less from the capital market. Foreign

Changes in official discount rates since 1961.

Country and date of change	Official discount rate in %	Country and date of change	Official discount rate in %	Country and date of change	Official discount rate in %
Austria		France		Spain	
17th March 1960	5	6th October 1960	3½	11th April 1960	5½
27th June 1963	4½	14th November 1963	4	9th June 1961	5
Belgium		Germany		Sweden	
4th August 1960	5	11th November 1960	4	15th January 1960	5
24th August 1961	4¾	20th January 1961	3½	6th April 1962	4½
28th December 1961	4½	5th May 1961	3	8th June 1962	4
18th January 1962	4¼			18th January 1963	3½
22nd March 1962	4	Greece		14th June 1963	4
9th August 1962	3¾	1st November 1960	6	31st January 1964	4½
6th December 1962	3½	17th January 1963	5½		
18th July 1963	4			Turkey	
31st October 1963	4¼			29th November 1960	9
Canada		Japan		1st July 1961	7½
24th June 1962 ¹	6	24th August 1960	6.94		
8th September 1962	5½	26th January 1961	6.57	United Kingdom	
12th October 1962	5	22nd July 1961	6.94	8th December 1960	5
13th November 1962	4	29th September 1961	7.30	26th July 1961	7
6th May 1963	3½	27th October 1962	6.93	5th October 1961	6½
12th August 1963	4	27th November 1962	6.57	2nd November 1961	6
Denmark		20th March 1963	6.21	8th March 1962	5½
26th January 1960	5½	20th April 1963	5.84	22nd March 1962	5
23rd May 1961	6½	18th March 1964	6.57	26th April 1962	4½
19th August 1963	6			3rd January 1963	4
13th November 1963	5½	Netherlands		27th February 1964	5
Finland ²		16th November 1959	3½		
1st April 1959	6¾	25th April 1962	4	United States	
30th March 1962	8	8th January 1963	3½	12th August 1960	3
28th April 1962	7	6th January 1964	4	17th July 1963	3½

¹ Prior to this date Bank rate was fixed each Thursday at ¼ per cent. above the latest average tender rate for Treasury bills. ² Basic rediscount rate.

issues, although dropping to nil after the interest equalisation tax was proposed, amounted for the year as a whole to \$1.1 milliard, or slightly more than in 1962. There was some resumption of foreign issues early in 1964, mainly by borrowers exempt from the proposed tax.

Since the February tax reduction the monetary authorities have made no perceptible shift in the direction of tighter credit, though the decline in bank liquidity over the past year puts them in a stronger position to do so if it should be thought necessary.

United Kingdom. The expansionary budget of April 1963 was the culmination of a series of fiscal measures initiated the preceding autumn with the aim of putting the economy firmly on the path to growth. With the same end in view, all remaining monetary restrictions had been removed during the later months of 1962 and Bank rate had been brought down to 4 per cent. in January 1963. As regards its implications for monetary policy, it is worth noting that, though the April budget involved both a substantial decline in the central government's saving and a rise in public investment, it was designed to compensate several trends of an opposite nature. Personal saving had been high, the self-financing capacity of the public corporations had grown and, finally, companies' fixed capital investment appeared still to be on a downward slope. Against this background, the immediate object of monetary policy was to promote domestic credit ease while keeping short-term market rates at a level — high relative to Bank rate — such as would discourage inward or outward movements of funds. The pursuit of this aim required some novel applications of policy during the year.

Developments early in 1963 had already foreshadowed liquidity strains for the banks, whose advances/deposits ratio rose to a new post-war high of close to 50 per cent. Advances increased sharply, partly because of severe weather and an adverse shift in external "leads and lags", while deposits declined under the influence of the Exchequer's seasonal cash surplus. During this phase the banks' position was eased somewhat by the authorities' net purchases of gilt-edged securities. As another alternative, however, the Bank of England informed the banks in the early spring that there would be no objection to their observing a 29 per cent. liquidity ratio for the time being instead of the customary one of 30 per cent. Around the same time the gilt-edged market had begun to strengthen and it continued to do so after the budget, particularly when it was announced that no conversion offer would be made with respect to maturing stocks and that only £400 million of a new 5 per cent. Exchequer stock (1976-78) would be issued. The yield on long-dated Treasury stock, which stood at 5.64 per cent. at the middle of March, fell steadily thereafter to reach 5.13 per cent. by the end of June. In these circumstances bank deposits rose only slowly, but the growth of advances had also become more moderate, partly perhaps because of the high rate of repayments.

As regards external considerations, there was from the beginning of the year, when Bank rate was lowered, a certain conflict with the policy of

domestic credit ease. In order to help sustain short-term market rates a monetary technique long in disuse was at that time revived. The Bank of England announced that it might occasionally in future make advances to the discount market at rates in excess of Bank rate. Although this technique was used only once — in March — its effect was sufficient to keep the Treasury bill rate within $\frac{1}{4}$ per cent. below Bank rate for the rest of 1963. Up to that time the yield on Treasury bills had normally fluctuated at $\frac{1}{2}$ – $\frac{3}{4}$ per cent. below Bank rate.

During the summer months the economy advanced steadily, but the strength of the upswing did not yet carry conviction. The yield on long-dated Treasury stock edged further downwards and in September it fluctuated around 5.05 per cent. The monetary authorities, believing the situation to be temporary and therefore not wishing to see an excessive decline in long-term rates, sold a moderate amount of stock during the third quarter, which was mostly taken up by domestic banks and overseas banks and official institutions. They also began during this period to encourage local authorities and others to enter the new issues market. In the meantime bank advances continued to rise, while the growth of deposits, though now relatively faster, was insufficient to bring bank liquidity to a comfortable level. The planned Exchequer deficit, which had been expected not only to stimulate the economy but also to feed bank liquidity, did not materialise on the expected scale. In September, therefore, the banks were once again informed that they might work to a lower liquidity ratio, i.e. 28 per cent., between that time and April 1964. At this level, which continues to apply for the time being, the ratio is now closer to what, under present-day conditions, is generally considered to be in accordance with sound banking practice.

In the autumn, as the upswing quickly gathered momentum, the gilt-edged market weakened. The rising tendency of longer-term interest rates was accentuated by a growing volume of new issues by local authorities and industry, as well as by the announcement of a substantial public investment programme for the next few years. The yield on longer-dated Treasury stock rose sharply during November, then fluctuated around 5.5 per cent. in December and January. In this situation Exchequer financing was shifted more to the banking system, thus contributing to a faster rise in deposits. As, moreover, the increase in bank advances was small, the banks' liquid-asset ratio remained comfortably above the 28 per cent. minimum. During this period official policy did not oppose the rise in longer-term rates, though on occasion some support was given to the market.

Early in 1964 it became apparent that domestic demand was growing at a rate that was not sustainable. As a precautionary measure, intended to slow down the pace of advance but not to cause a net inflow of foreign funds, Bank rate was raised on 27th February from 4 to 5 per cent. The yield on Treasury bills, however, at first rose by only about $\frac{1}{2}$ per cent., thus returning to a more normal level in relation to Bank rate. Subsequently, the budget of April 1964, bringing with it an increase in certain indirect taxes, injected a further element of caution.

The overall Exchequer deficit for 1964-65, after allowing for changes in taxation, is estimated at £791 million, of which £165 million represents net funds to be raised on behalf of the local authorities as an alternative to their borrowing in the market. The difference between these two figures, i.e. £626 million, compares with an estimated deficit of £687 million in the 1963-64 budget, the outturn of which, however, proved to be some £200 million lower. Thus the prospect is for an appreciably larger Exchequer financing requirement in the coming fiscal year. Since the February increase in Bank rate, the yield on long-dated Treasury stock has been fluctuating at around 5.9 per cent., and the gilt-edged market is unlikely to be strong during a period of rising activity. This suggests the possibility of a rather large volume of Treasury bill financing via the banks, which may therefore look ahead to comfortable liquidity margins. On the other hand, if the need arises, pressure can be exerted on bank liquidity by a call for special deposits.

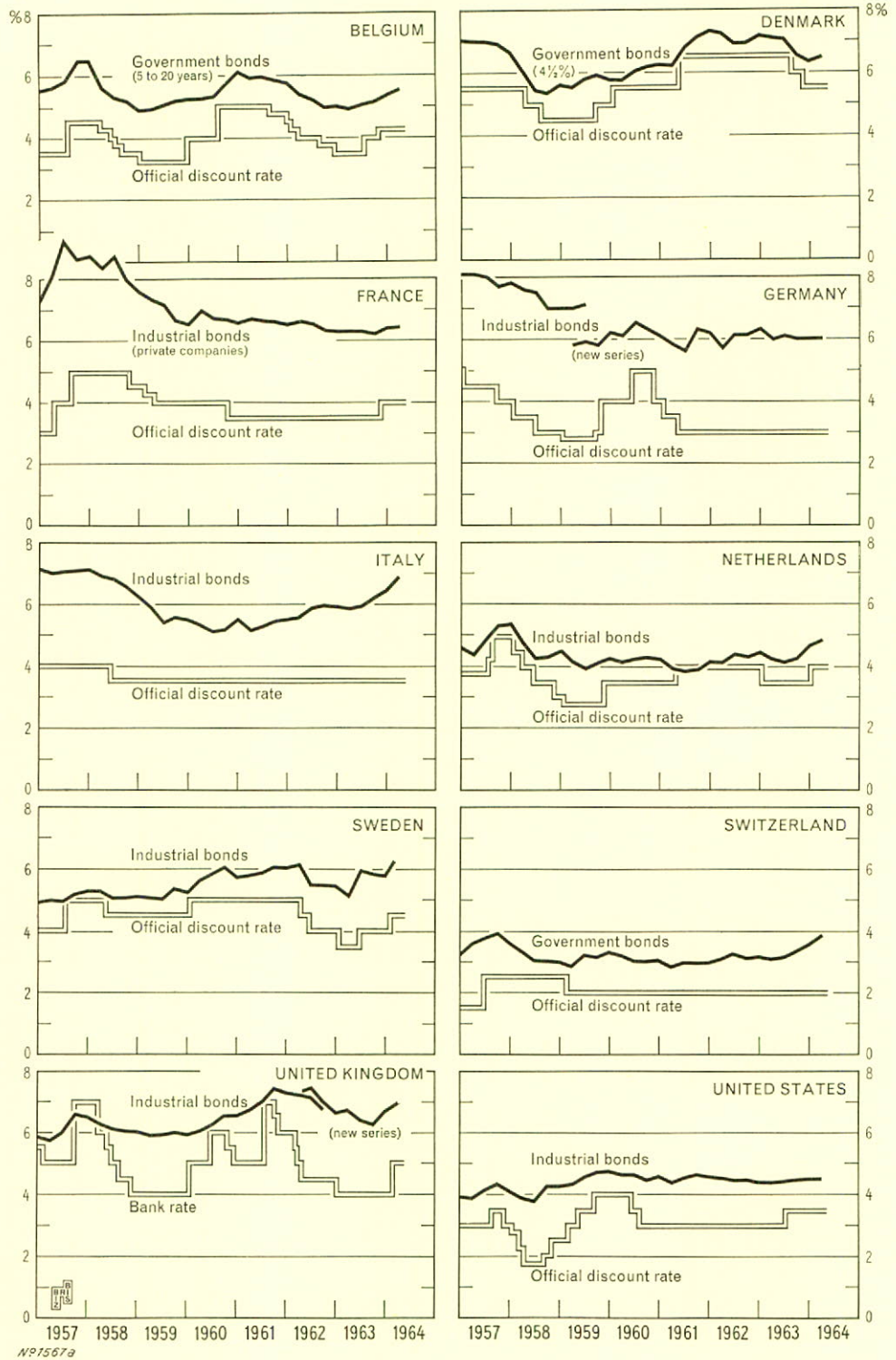
France. Efforts to restrain the growth of liquidity began early in 1962, when in conjunction with a continuing large external surplus the banks' lending to the private sector accelerated. Within this context, however, the measures taken were designed to favour the availability of longer-term funds to industry and to reduce the Treasury's recourse to bank credit. With the same twofold objective in view, further steps were taken later in the year, and these were considerably reinforced in 1963 and early 1964.

During 1962, the compulsory assets ratio ("coefficient de trésorerie") was increased from 30 to 32 per cent. of deposit liabilities, while the portion that must be held in Treasury bills (now designated as "certificats de trésorerie") was reduced from 17½ to 15 per cent. Thus the scope for compulsory holdings of other types of paper — mostly rediscountable equipment credits subject to the prior approval of the Bank of France — increased from 12½ to 17 per cent. of deposit liabilities. Moreover, beginning in 1962 the interest rates on time deposits, Treasury bills and medium-term Treasury bonds were progressively reduced.

Although in consequence of these measures the rate of increase of bank deposits slowed down after the middle of 1962, the creation of new liquidity was still substantial. As a more decisive step, therefore, the monetary authorities imposed a direct ceiling of 12 per cent. on the growth of bank credit for a period of one year as from the end of February 1963. In addition, the "coefficient de trésorerie" was raised from 32 to 36 per cent. between March and May. In April, with a view to reducing the banks' incentives to hold Treasury paper, Treasury bills sold to the banks in excess of their minimum compulsory requirements were made subject to tender. Finally, in May the Treasury, for the first time for about five years, launched a fifteen-year 4¼ per cent. loan, free of personal income tax and carrying reimbursement premiums, for Fr.fr. 1 milliard.

Following the intensification of inflationary pressures in the late summer, the autumn stabilisation programme brought with it a number of new credit measures. The Treasury issued a second loan, this time for Fr.fr. 2 milliard,

Interest rates.



with a maturity of twenty years, yielding $4\frac{1}{4}$ - $4\frac{3}{4}$ per cent. In addition, the 12 per cent. ceiling on bank credit for the year up to the end of February 1964 was reduced to 10 per cent. and hire-purchase terms were tightened, especially for motor-cars.

In November these measures were completed by an increase in the Bank of France's discount rate, unchanged since 1960, which was raised from $3\frac{1}{2}$ to 4 per cent. Previously the authorities had refrained from this action because it was inappropriate on external grounds. Now, with the external surplus declining and domestic inflation an overriding problem, the situation was different. Moreover, measures had already been taken which reduced the scope for international movements of short-term funds. In April the banks were prohibited from paying interest on non-resident franc accounts, and in August stricter terms were imposed on foreign borrowing by franc-area residents. The domestic effects of the discount rate adjustment were also circumscribed. It was decided to keep Treasury bill rates and those for export bills unchanged and to limit the increase in the minimum rates for bank credits to $\frac{1}{4}$ per cent. Thus the impact of the higher discount rate was primarily on the cost of recourse to the central bank — the more so because the penalty rate for borrowing was also increased.

In 1963 the banking system's monetary and quasi-monetary liabilities increased by Fr.fr. 19.7 milliard, i.e. 13.6 per cent., against 18.2 per cent. in 1962. The rate of growth of short-term credits to the private sector and the nationalised industries declined even more, from about 20 per cent. in 1962 to 12 per cent. last year. Since the external surplus continued to feed bank liquidity, there was no perceptible increase in recourse to the Bank of France in 1963 as a whole. During this period, however, the banks' margin of excess liquidity remained narrow, and there were times, especially in the spring and towards the end of the year, when the money market was especially tight.

In the early months of 1964, with the external accounts more in balance, money and quasi-money expanded much more slowly still. However, since existing liquid-asset holdings remain high, the object of policy has continued to be that of restricting their further growth. In January the ceiling on the permissible expansion of bank credit was prolonged, on the same basis as before, to the end of September 1964. In addition, the minimum requirement for "certificats de trésorerie" held by the banks within the 36 per cent. "coefficient" was further reduced from 15 to 13 per cent. Finally, the interest rate on short-term Treasury bills reimbursable upon demand was slightly reduced, and the banks' mobilisation of Treasury paper with less than three months to run was made subject to market rates instead of the central bank's discount rate as before. Subsequently, in March the Treasury launched another long-term loan, on the same terms as the one in September 1963, for Fr.fr. 1.5 milliard. Moreover, with effect from 1st June 1964, the authorities lowered the banks' requirement as regards "certificats de trésorerie" to 10 per cent., while keeping the overall compulsory assets coefficient unchanged. There is the prospect, too, that liquid-asset formation will be

further affected by the planned reduction in the 1964 budget deficit and the flotation of a new public loan later this year.

Italy. In 1962 and early 1963 bank credit to the economy advanced at an accelerated pace. During this period the progressive shift in income distribution from profits to wages was making domestic investment increasingly dependent on the availability of credit. With a view to avoiding a halt to growth, the monetary authorities sought to accommodate the demand for credit, particularly as external reserves were large and the balance of payments still not in an unsound position. Thus, when the external deficit first emerged towards the end of 1962, the banks were permitted to meet the resulting drain on their liquidity largely by borrowing at short term from abroad, while also increasing their direct recourse to the Bank of Italy. In early 1963, moreover, the Treasury did not renew a maturing nine-year bond issue, thereby lending assistance to both bank liquidity and the capital market.

In the summer and autumn, however, it became evident that the external situation was turning worse rather than better, and prospects were further dimmed by the gradual emergence of a substantial deficit in the central government's cash budget, which was financed largely by drawings on the central bank. In these circumstances credit restraint measures had to be brought strongly to bear, though clearly the situation called equally for budgetary action. In the early summer the authorities asked the banks to moderate their short-term borrowing abroad, and in September they formally requested the banks not to increase further, and if possible to reduce, their net foreign liability positions. In consequence, bank credit to the private sector rose in the second half of the year by 11 per cent., which was substantially below the 16 per cent. growth in the corresponding period of 1962. Bank deposits rose by 9 per cent. in the June-December period, compared with an increase of 12 per cent. in the same period of 1962. The banks' loan/deposit ratio, which stood at 74.4 per cent. at the end of December 1962, had risen a year later to 79.8 per cent. Early in January 1964 the banks were formally instructed not to let their net foreign indebtedness go above the level of the previous November or December, whichever was the lower.

Net capital-market issues dropped back from Lit. 1,640 milliard in 1962 to Lit. 1,350 milliard in 1963, although the availability of longer-term funds was somewhat increased by a net redemption of debt by the Treasury. Public credit institutions and enterprises floated a substantially larger volume of new issues in 1963, but the bond and share issues of private industry declined to Lit. 430 milliard from over Lit. 900 milliard in 1962. Thus, although in 1962 and early 1963 interest rates on short-term financial assets had been reduced as a means of encouraging the placement of funds at longer term, the advantages for investors were outweighed by the adverse influence of the nationalisation of the electricity sector, the coupon tax on dividends and general economic developments. In framing credit policy, therefore, the authorities took account of the public's increased liquidity preference and made it possible for the banks to give some support to the

capital market. However, the banks' securities portfolio (excluding Treasury bills), after having increased by Lit. 430 milliard in 1962, rose in 1963 by only Lit. 280 milliard.

In the first quarter of 1964 credit restraint made itself felt much more strongly, as reflected in a reduction in the credit institutions' loans by about Lit. 185 milliard, compared with a rise of Lit. 325 milliard in the corresponding period of 1963.

But whether the situation can be stabilised without impairing growth will depend very largely on steps to curb consumption and restore a strong Treasury position. The budget measures of late 1963 and early 1964 represent steps in the right direction.

Netherlands. In recent years the monetary authorities have been comparatively successful, even in the face of large foreign exchange inflows, in controlling the rate of domestic liquidity creation. Largely by means of debt-management techniques and the imposition of ceilings on the rate of private credit expansion, private-sector holdings of liquid assets (excluding savings deposits) have been kept in the neighbourhood of 40 per cent. of national income. In 1962, with the external accounts in approximate equilibrium and the demand for credit weakening, these efforts were relaxed, and by January 1963 credit restrictions had been removed altogether. By the late summer, however, the situation was rapidly being reversed again. At that time, when bank credit had already been accelerating for some months, wage inflation was becoming a distinct threat and there was also a resumption of foreign exchange inflows.

Responding quickly in October, the authorities turned primarily to measures of fiscal restraint (higher indirect taxation and a slowing-down of public investment), but moved also along accustomed lines in the credit field. The Nederlandsche Bank reintroduced a ceiling on the permissible growth of bank credit to the private sector, this time limiting the monthly expansion to 1 per cent. of the average level of credit outstanding in the first half of 1963. Under this arrangement, when the ceiling for all banks is exceeded the individual banks responsible are required to deposit specified sums in non-interest-bearing accounts with the central bank. As towards the end of the year the banks had already gone beyond these limits, they were required early in 1964 to place funds with the Nederlandsche Bank. This development was a factor leading the authorities to reinforce credit policy with an increase in the discount rate in January from $3\frac{1}{2}$ to 4 per cent.

Debt-management operations were also used with a view to reducing liquidity. In October the government issued a thirty-year $4\frac{1}{2}$ per cent. loan for Fl. 400 million. With the bond market already weakening, the loan yielded little more than Fl. 300 million, but this was still in excess of current Treasury needs. When shortly thereafter tax receipts accelerated unexpectedly, a further sterilisation of funds became possible. For 1963 as a whole the central government's borrowing at long term came to over Fl. 900 million,

as against its cash deficit of less than Fl. 300 million, with the difference going largely to improve its position vis-à-vis the central bank.

The local authorities, whose net financing requirement rose by over Fl. 400 million to reach almost Fl. 1.5 milliard in 1963, went to the capital market for nearly Fl. 1.2 milliard. According to new legislation effective as from November 1963, the government is now empowered to regulate the total borrowing of the local authorities. It was decided that for the year from the beginning of November the municipalities' borrowing would be limited to 91 per cent. of the amount they had taken up during the twelve months up to the middle of 1963.

Although the funds raised on the capital market rose from Fl. 4.9 milliard in 1962 to Fl. 5.4 milliard in 1963, the heavier borrowing by the central government and the local authorities necessarily curtailed the scope for private and foreign borrowing, which together declined over the same period from about Fl. 4.0 to 3.3 milliard. This was no doubt one factor underlying the private sector's greater recourse to bank credit last year.

In 1963 the central bank's net acquisitions of foreign exchange increased bank liquidity by over Fl. 615 million, but this effect was largely offset by the government's debt-management operations. To help the banks with their liquidity needs, associated with the growth of both the note circulation and credit to the private sector, the Nederlandsche Bank reduced the banks' cash reserve requirement in stages from 5 per cent. to nil in the course of 1963. The banks also found it necessary to draw upon their free cash reserves. Looking ahead, the authorities are expecting a substantial deterioration on external account in 1964 and hence an intensification of liquidity pressures on the banks.

Belgium. An acceleration of both private and public credit demand, coinciding with a particularly unreceptive capital market, led in 1963 to a big increase in bank credit and the money supply. Conditions on the capital market reflected in large measure the adverse response of investors to the fiscal reform of late 1962. Among other things this reform introduced an income withholding tax of 15 per cent. on earnings from fixed-interest securities and certain other financial assets (including time deposits, sight deposits and, with some exceptions, savings deposits).

In 1963 the central government's budget deficit increased substantially, mostly because of an acceleration in public investment, and the Treasury's net financing requirement rose to B.fr. 24.5 milliard from B.fr. 12.9 milliard in the previous year. But, whereas in 1962 the Treasury had raised B.fr. 20.1 milliard on the domestic credit market and reduced its indebtedness in foreign currencies by B.fr. 7.2 milliard, in 1963 it was able to place only B.fr. 10.8 milliard on the Belgian market while increasing its external indebtedness by B.fr. 13.7 milliard. Its foreign borrowing was largely accomplished indirectly via the commercial banks, which borrowed abroad and used the proceeds mostly to take up Treasury paper denominated in foreign currencies.

In the private sector the strength of credit demand reflected the continuing rapid economic expansion, the buoyant demand for durable consumer goods and the narrowing of profit margins in certain branches. Commercial-bank lending to this sector rose in 1963 by B.fr. 18.4 milliard, or 26 per cent., as against 17 per cent. in 1962. The banks' deposit and longer-term liabilities increased by a similar amount in absolute terms, i.e. B.fr. 17.7 milliard, representing a rise of 13 per cent., against 9 per cent. in 1962. The relatively large growth in credit to the private sector was facilitated by the abolition in January 1963 of the former "cover ratio" as regards government security holdings.

The first move towards credit restraint came in July 1963, when the National Bank raised its discount rate from $3\frac{1}{2}$ to 4 per cent. This was followed in October by a further increase to $4\frac{1}{4}$ per cent. By the turn of the year, however, inflationary strains had become rather more pronounced, leading the monetary authorities early in 1964 to conclude a credit agreement with all lending institutions and also to tighten hire-purchase terms. As a result the commercial banks, for example, will be expected to limit the growth of their lending to the private sector in 1964 to 10-12 per cent. During the first few months of 1964 there was some recovery in the demand for fixed-yield securities, and long-term interest rates appear to have stabilised at a higher level.

Germany. From late 1961 onwards the overall growth of lending by commercial banks and other credit institutions slowed down slightly. This was a reflection, however, not of credit restraint but of the more moderate rate of economic expansion. In 1962 and early 1963, it is true, the "passive" attitude adopted by the monetary authorities led, in combination with market developments, to a decline in bank liquidity. But, since the banks' liquid assets were quite large at the outset, this policy had the effect of making the credit situation tauter but not tight. In the later months of 1963 conditions of relative credit ease continued to prevail when, under the influence of the substantial influx of foreign exchange and a deterioration in the public authorities' budget positions, bank liquidity began to increase again.

The credit institutions' total loans rose in 1963 by DM 25.6 milliard, or 13.2 per cent., compared with 14.1 and 16.3 per cent. in 1962 and 1961 respectively. Within the total there was again a relatively big increase in long-term loans, reflecting to a large extent the growth of mortgage lending. On the liabilities side, the credit institutions benefited from a notable rise in savings deposits and greatly enlarged their own bond issues.

Net capital issues rose substantially once again in 1963, reaching DM 13.2 milliard, compared with DM 11.1 milliard in 1962. The increase was partly attributable to the afore-mentioned growth in credit institutions' issues, a good proportion of which found a counterpart in lending to local authorities, but it was also due to larger borrowing by the Federal Government. In this connection it is worth noting that the cash budget of the combined public authorities changed from a surplus of DM 2.3 milliard in

1961 to a deficit of DM 1.6 milliard in 1962 and one of DM 5.0 milliard in 1963. The increased recourse by public authorities to longer-term funds was a factor tending to keep interest rates relatively high in 1963 despite the large purchases of German securities by foreigners. It may also have contributed to the decline that occurred in new issues of industrial bonds and shares, though another underlying factor was the marked recovery in business profits in the second half of the year.

In late 1963 and early 1964, with the emergence of a large external surplus and an accompanying threat of domestic inflationary strains, the monetary authorities were once again faced with a conflict between domestic and external objectives. Any attempt to restrict credit by general monetary means would entail the strong risk that additional funds would flow in from abroad, thus nullifying the effects of restraint and accentuating the external surplus. Hence in early 1964 the authorities introduced or proposed various selective measures, already described on page 18, designed to discourage the entry and encourage the re-export of foreign money and capital and to stimulate foreign borrowing on the German capital market. These measures have helped to reduce simultaneously both the external surplus and domestic liquidity. It is noteworthy, on the other hand, that the monetary authorities have not increased the banks' reserve requirements against domestic deposit liabilities nor reduced their rediscount margins with the central bank. Since late 1963, to be sure, the banks have increased their holdings of open-market paper, but this represents primarily the investment of excess liquid funds. Furthermore, the Bundesbank's discount rate, fixed at 3 per cent. in May 1961, has been kept unchanged.

Switzerland. Until last year it was possible for interest rates to be kept both low and relatively stable. This was largely because foreign exchange inflows more than offset the liquidity-reducing effects of the external current-account deficit. But it was also ascribable partly to the authorities' efforts to limit directly both the rate of growth of bank credit and the volume of foreign issues on the Swiss capital market. In 1963, however, a situation was reached in which a general rise in interest rates could no longer be avoided. The reasons lay mainly in a decline in private and public saving relative to a continuing high rate of domestic investment.

The expansion of bank credit, after having slowed down about the middle of 1962, gathered speed again in 1963. Already early in the year, however, the banks began to encounter liquidity pressures, partly because of a net outflow of foreign exchange, but largely because new funds were not being attracted into the banks' medium-term bonds ("bons de caisse") at prevailing interest rates. At the end of July the National Bank gave its consent to an increase of $\frac{1}{4}$ per cent. in the rates paid on medium-term bank bonds running for five years or more. Subsequently, in January and May 1964, the interest rates paid on medium-term bonds were raised again, which brought the rate to $4\frac{1}{4}$ per cent., as against $3\frac{1}{2}$ per cent. one year earlier. As an alternative source of funds, however, the banks have been

impelled to resort increasingly to placing their own bonds in the capital market, where they accounted for most of the rise in new bond issues last year.

The yield on long-term bonds of the Confederation rose from 3.1 per cent. at the end of April 1963 to about 3.9 per cent. a year later. An effort has been made, however, to limit the rise in interest rates on first mortgages, which now as a rule bear a rate of 4 per cent., compared with $3\frac{3}{4}$ per cent. last year.

The intensification of inflationary pressures in the second half of 1963, accompanied by a resumption of foreign exchange inflows, led to the adoption in March 1964 of the broad set of legislative measures already described on page 15. In the credit field these measures follow along much the same lines as previously. Increased emphasis is being placed, however, on techniques aimed at discouraging the entry and encouraging the re-export of short-term funds. In addition, the banks' permissible rate of credit expansion has been reduced from 82 to 79 per cent. of the relevant 1960 or 1961 base for the year 1964 as a whole. The corresponding rate for mortgage credit is fixed at 108 per cent. in order to facilitate the consolidation of outstanding building loans (which are included in the lower ceiling). To the extent that these limits are exceeded, the banks concerned will be required to put an equivalent amount on special deposit with the Swiss National Bank. Finally, new domestic capital-market issues are to be more closely regulated. Since then, with effect from 1st June 1964, hire-purchase regulations have been made more stringent in respect of both minimum down-payments and maximum repayment periods.

These measures, together with the restrictions imposed on building and the intake of foreign labour, are designed to bring about a better equilibrium between domestic saving and investment, while at the same time easing upward pressures on interest rates. The scope for inflows of foreign capital is now considerably reduced; however, since the measures do not prevent the repatriation of Swiss capital held abroad, the influx of such capital in response to tight domestic credit and high interest rates could weaken the intended effect of the new restraint measures. At the same time the central government's cash budget deteriorated last year, declining from a surplus of Sw.fr. 430 million in 1962 to one of Sw.fr. 125 million. Viewed as a whole, therefore, the present situation would seem to call for as much budget restraint as possible as a means of keeping down interest rates and thus inhibiting the repatriation of funds from abroad. This would be in accordance with both domestic and international policy considerations.

Austria. For the third consecutive year financial developments in 1963 were influenced by a large inflow of foreign exchange, to no small extent reflecting public-sector borrowing abroad. The banking system's monetary and quasi-monetary liabilities increased by over 11 per cent.; this rise, which was somewhat smaller than in 1962, found over two-fifths of its counterpart in the growth of net foreign assets. In view of the weaker trend of business investment early in 1963, the foreign exchange inflow was permitted to

act on bank liquidity and credit, and the National Bank lowered its discount rate in June from 5 to $4\frac{1}{2}$ per cent. At the same time the banks were given freedom to borrow and invest short and medium-term funds abroad. They were thus led to build up their net foreign assets, which in the twelve months up to the end of March 1964 rose by about Sch. 1.9 milliard. They also further reduced their indebtedness to the central bank. Both these factors have helped temporarily to bring down the banks' high level of domestic liquidity.

On the capital market the volume of new issues in 1963 was considerably above that of recent years, reflecting increased borrowing both by mortgage institutions and by the Federal Government, whose larger budget deficit was financed mainly in this way. However, as a result of strong domestic and foreign buying, long-term yields have fallen appreciably; in March 1964 a Federal Government issue, offering an effective return of 6.5 per cent., was successfully placed. With long-term yields having risen in other countries, it is possible that the public authorities and enterprises will now have less incentive than earlier to place long-term loans abroad.

In January 1964 the authorities abolished the regulation, introduced in August 1962, limiting the banks' credit expansion to 40 per cent. of the growth of their deposit liabilities. At the same time the credit ceilings based on total deposit liabilities were made more stringent, and it was stipulated that foreign deposits received after the end of 1963 could not be counted among the liabilities determining these ceilings. In practice, however, the credit regulations in force in 1963 had virtually no restrictive effect, and the modifications of last January were primarily of a structural character, not intended to represent a change in credit policy. In the same vein, but with a view primarily to creating a functioning money market, the government in April converted Sch. 1.0 milliard of the credit institutions' non-negotiable Treasury bills into long-term bonds and in May made Sch. 560 million of their remaining holdings fully negotiable.

Sweden. When aggregate demand weakened at the turn of 1962-63, the authorities introduced a broad range of compensatory measures, including an easing of credit policy, a relaxation of licensing controls on house-building and an acceleration of public consumption and investment. During the spring, however, it became evident that the domestic demand stimulus was proving all too effective, and this was further confirmed in the summer when exports began to rise strongly. The authorities' initial response was in the credit sphere, where bank lending was expanding very rapidly. Already in April the Riksbank requested the banks to curb their lending activity, and this was followed up by increases in certain short-term interest rates. In June the discount rate itself was raised from $3\frac{1}{2}$ to 4 per cent. During this period, moreover, seasonal factors and an outflow of foreign exchange limited the growth of bank deposits. Hence the banks were compelled to reduce their holdings of government securities, and this led to an appreciable rise in long-term interest rates.

In the autumn steps were taken to space out public investment expenditure, but the need for overall monetary restraint remained insistent. Although the growth of commercial-bank credit slowed down after the middle of the year, its rate of increase was still substantial, and the credit activity of other financial institutions was very buoyant. The Riksbank therefore made further requests for a moderation of lending, and the emphasis of public-debt management continued to be on the placing of securities outside the commercial banks.

For 1963 as a whole the net flow of funds to the credit and share markets came to S.kr. 8.6 milliard, i.e. almost one-quarter more than in 1962 and about double that in 1961. Of this total, commercial banks accounted for only S.kr. 2.4 milliard, as against S.kr. 3.3 milliard in 1962. However, by reducing their holdings of government securities by over S.kr. 800 million, the commercial banks were able to increase their loans to the economy by S.kr. 3.2 milliard. A larger proportion of the increase in lending to the private sector last year went to housing.

The central government's cash budget changed from a surplus of S.kr. 600 million in 1962 to a deficit of S.kr. 200 million in 1963 and is expected to deteriorate further this year, thereby putting a considerable additional burden on monetary policy. In the last quarter of 1963, coincident with the emergence of the budget deficit, inflationary strains became more intense, and at the end of January the Riksbank raised the discount rate from 4 to 4½ per cent. This move was accompanied by the issue of a sixteen-year government loan for S.kr. 100 million, the yield of which, at 5¾ per cent., was the highest offered for a loan of this type since 1921. In addition, the National Debt Office issued a three-year 6 per cent. tap loan, which brought in some S.kr. 450 million. Finally, a penal rate of 9 per cent. was introduced for that part of a bank's borrowing from the Riksbank in excess of half its own capital.

Denmark. The heavy stress laid on fiscal and incomes measures in 1962-63, combined with long-term public and private borrowing abroad, proved effective in restoring a sound external position without halting domestic growth. External borrowing helped both to strengthen the reserves, especially in early 1963, and to avoid too sharp a curb on investment. The central government's budget, after having already moved back into surplus in 1962, improved further in 1963, contributing together with incomes restraint to the emergence of an external current-account surplus in the second half of the year.

Bank credit to the private sector, rising more slowly from the middle of 1962 onwards, increased in 1963 by about 10 per cent. In conjunction with the foreign exchange inflow, however, the public's holdings of monetary and quasi-monetary assets rose by over 12 per cent., as against less than 9 per cent. in 1962. This increase, as well as the accompanying rise in bank liquidity, would have been bigger but for the central government's cash surplus, which was sterilised with the Nationalbank to the extent of D.kr. 575 million,

compared with D.kr. 170 million in 1962. Even so, the commercial banks' liquidity improved last year by D.kr. 825 million, of which D.kr. 170 million was employed to reduce their net foreign indebtedness, while the remainder went to strengthen their net position vis-à-vis the central bank.

In August 1963 the Nationalbank reduced the discount rate from $6\frac{1}{2}$ to 6 per cent. and then lowered it further in November to $5\frac{1}{2}$ per cent., the level at which it had stood in the spring of 1961 prior to the outburst of inflation. The commercial banks followed suit with respect to the rates charged on their advances, but they lowered their deposit rates by only $\frac{1}{2}$ – $\frac{3}{4}$ per cent. The yield on long-term government bonds, which had stood at something above $6\frac{1}{2}$ per cent. about the middle of 1963, fluctuated around 6 per cent. early in 1964. With the market for fixed-yield securities strengthening in 1963, there was a notable rise in new issues, particularly of mortgage bonds, which, at D.kr. 3.5 milliard, were about one-third larger in 1963 than in the previous year.

Recently there have been indications of an acceleration in economic activity and bank lending. Continuing its emphasis on budget restraint, the government raised certain indirect taxes in February 1964 and in March postponed new public building starts for six months. Furthermore, in view of the comparatively high level of bank liquidity, the Nationalbank in January requested lending institutions to avoid a major expansion in their credit operations.

Norway. The credit control agreement for 1963, concluded at the end of 1962, was restrictive in character, requiring the commercial and savings banks not to increase their domestic lending by more than 6–7 per cent. To ensure that this policy would not be undermined by short-term borrowing abroad, as had been the case in 1962, the commercial banks were requested not to allow their foreign currency lending to increase by more than N.kr. 175 million above its level at the end of 1962. The banks observed these limitations, increasing their domestic loans by approximately the prescribed maximum and their loans in foreign currencies hardly at all. Credit restraint appears to have contributed to a damping-down of investment demand — particularly for inventories, which actually declined in 1963.

In the spring of 1963 a strong upswing in external demand imparted renewed momentum to domestic expansion and contributed also to an improvement in the current external balance (excluding net imports of ships) for the year as a whole. Developments in the public sector were also expansionary, largely because the public authorities' investment outlays continued to grow while their saving remained stable. Together, the central government, mainly owing to the deterioration in its budget, and Norges Bank, mostly through its net purchases of foreign exchange, supplied the banks with N.kr. 326 million of liquidity in 1963, as against N.kr. 188 million in 1962. Although most of this gain was offset by a rise in the currency circulation, the banks were able to increase their liquid-asset holdings in 1963.

At the turn of 1963-64 the weakened budget position, combined with the prospect of a further rise in money incomes, led to continued emphasis on monetary restraint. In the credit control agreement of 1964 it was laid down that the commercial and savings banks should not expand their lending by more than 5-6 per cent. and their lending in foreign currency by more than N.kr. 100 million. Particular restraint is to be exercised with respect to consumer credits and loans for extending plant capacity.

Finland. The slackening in the growth of demand early in 1963, mainly in investment expenditure, contributed along with a recovery in exports to an improved external position and an inflow of foreign exchange. On the other hand, the central government's budget position underwent a substantial further deterioration, leading the authorities to increase certain indirect taxes and prices of government services. Moreover, in December the government decided to increase the tax on company profits from 38 to 45 per cent., and in January 1964 a revised turnover-tax system, one effect of which is to increase total revenue, was introduced. In 1963 the government's borrowing requirement, which must be satisfied outside the banking system, rose to NFM 650 million from NFM 415 million in 1962, thus tending to limit the formation of deposits at the banks. Of this total, NFM 100 million was raised by means of special bond loans utilisable for income-tax payments in the years 1964-65.

The credit institutions' lending to the private sector rose in 1963 by only 6 per cent., against more than 10 per cent. in 1962, and the banks were able to repay some of their indebtedness to the central bank. In order to keep the reins of monetary policy fairly tight, however, the authorities took advantage of this development by reducing rediscount ceilings in April 1963 from NFM 700 to 545 million. A new interest rate agreement in June provided for greater differentiation in favour of longer-term deposits, but it did not raise the average level of rates; in addition, 100 per cent. index-tied accounts, suspended in 1958, were reintroduced. In February 1964, consequent upon a large negotiated increase in wages, monetary policy was tightened through the promulgation of detailed lending instructions to the credit institutions, which were asked to limit their lending for the financing of consumption, large investment undertakings and stock-building. In addition, personal income and property taxes were raised with effect from April.

Spain. In late 1962 and early 1963 excessive demand pressures, concentrated largely on foodstuffs and housing, led the authorities to take measures to slow down the growth of demand and ease upward pressures on prices. Imports of basic foodstuffs were increased, customs duties were slightly reduced and building licences for higher-cost dwellings were restricted. In the credit field a new compulsory minimum liquidity ratio, variable within a range of 10 to 20 per cent., was established at 12 per cent. as from 1st April 1963 and was put up to 13 per cent. at the end of May. Under the influence of these and other measures the economy momentarily slackened the pace of its advance in the spring and summer, and the rising trend of

prices was halted. The exchange reserves, which had for some months remained relatively stable, began to rise again about the middle of the year. Although still rapid, the growth of imports tapered off somewhat in 1963, while receipts from tourism, emigrants' remittances and capital imports continued to mount. Moreover, in recent months exports have benefited from the exceptionally good winter yields of citrus fruit and olives.

In 1963 the credit institutions' monetary and quasi-monetary liabilities increased by Pesetas 95.5 milliard, i.e. by 17 per cent., compared with a rise of over 20 per cent. in 1962. The reduced rate of increase partly reflected a smaller net inflow of foreign exchange, but it was also associated with a slowing-down in the growth of credit to the private sector, which went up by Pesetas 76.9 milliard (22 per cent., compared with 27 per cent. in 1962). At the same time, whereas in 1962 about 7 per cent. of the increase in the credit institutions' credits to the private sector consisted of acquisitions of industrial securities, the proportion rose in 1963 to 14 per cent. This reflects primarily the greater freedom enjoyed by the savings banks since August 1962 to invest in securities other than those of the public sector. Thus, the banks' purchases facilitated the large rise in 1963 in private-sector capital-market issues, which came to Pesetas 39.7 milliard, compared with Pesetas 24.2 milliard in 1962. The savings banks also took a big proportion of new public-sector issues, which rose in 1963 to Pesetas 13.9 milliard from Pesetas 6.7 milliard in 1962. Most of the public issues represented securities of the National Institute for Industry (INI), but there was also a Treasury issue in December for Pesetas 5.0 milliard which went to finance government transfers of funds to the public credit institutions.

At the beginning of 1964 Spain embarked on a four-year development programme, the main emphasis of which is to be placed on a high rate of public investment, accompanied by "indicative planning" designed to achieve similar results in the private sector. The accelerated rate of investment in the public sector is expected to be financed mostly by a growth in the sector's own saving, which is to be accomplished by holding the rate of increase of public consumption expenditure to about half that of budget revenue. With exchange reserves rising and prices stable, the programme was launched under favourable conditions. As the scheme is an ambitious one, however, its successful realisation will depend upon continuous attention being given also to the maintenance of domestic and external equilibrium.

Canada. Once the foreign exchange crisis of the early summer had been surmounted, the authorities began in the autumn of 1962 to move quickly back towards monetary ease, and by May 1963 Bank rate had been brought down to 3½ per cent. In July, however, the US announcement of the proposed interest equalisation tax, which followed closely upon the increase in the Federal Reserve System's discount rate, threatened to lead to a substantial general rise in interest rates. When subsequent negotiations made it clear that Canadian new issues in the United States would enjoy conditional exemption privileges in respect of the tax, the financial markets settled down

somewhat, though in August the Bank of Canada found it necessary to adjust to the new situation by raising Bank rate to 4 per cent. It was pointed out, however, that this change was not intended to signal a tightening of monetary policy. Then, with the news in September that large sales of wheat and flour were to be made to the Soviet Union, the markets strengthened and interest rates declined. At the end of 1963 credit conditions, as reflected in short and long-term market interest rates, were much the same as at the beginning of the year. Vis-à-vis the United States, moreover, interest rate differentials had significantly narrowed.

The total assets of the chartered banks increased in 1963 by 9½ per cent., compared with a rise of only 2½ per cent. in 1962 when stringent credit measures had been in force. Bank loans, although they accelerated late in 1963, rose for the year as a whole by less than in 1962, i.e. Can.\$515 against 840 million. Thus, whereas in 1962 the banks had been impelled to draw down their liquid assets by almost Can.\$500 million, they were able in 1963 to rebuild such holdings by over Can.\$800 million, of which Can.\$650 million took the form of government securities. At this figure the increase in the chartered banks' government security holdings was approximately the same as the government's cash borrowing requirement of Can.\$630 million.

Japan. Between the autumn of 1962 and the spring of 1963 existing monetary restrictions were gradually lifted as the growth of industrial production slackened and official reserves steadily rose. The Bank of Japan's discount rate was lowered in four steps from 7.30 to 5.84 per cent. From the spring onwards output advanced anew, stimulated largely by consumption and inventory demand. Exports also rose buoyantly, though not as much as imports. Around the turn of the year, with some suddenness, exports weakened and imports accelerated, causing a decline in monetary reserves to set in. Consumer prices, which had continued their upward trend even during the phase of eased demand pressure, have gone on rising at an annual rate of about 7 per cent.

In line with continental European experience, the strength of demand for bank credit last year was associated partly with rising expenditure on housing and durable consumer goods, but even more with mounting production costs and the squeeze on company profit margins. This demand, together with the prevalence of easy credit conditions throughout most of the year and a marked preference by individuals and business firms for liquid assets, led to a big expansion of bank loans and deposits. The corporate sector, in particular, appears to have borrowed, both domestically and abroad, considerably in excess of its net financial requirements, using the proceeds to build up liquid assets and extend larger trade credits to the rest of the economy. The commercial banks' lending to the private sector rose in 1963 by Yen 3,250 milliard, i.e. more than 25 per cent., as against an increase of about 16 per cent. in 1962. With the accompanying big growth of Yen 2,830 milliard (30 per cent.) in deposit liabilities, the banks' recourse to the Bank of Japan (Yen 130 milliard) was kept to small proportions.

Late in 1963 the monetary authorities began to move gradually back to a policy of restriction. One of the first steps was a tightening of the city banks' credit ceilings with the Bank of Japan. Then, in December, minimum reserve requirements in respect of demand deposits were raised, while those for savings deposits were left unchanged. More important, in January 1964 the Bank of Japan requested the commercial banks to limit their credit expansion in the first quarter to 90 per cent., and in the second quarter to 88 per cent., of the increase in the corresponding period of 1963. Finally, in March the Bank of Japan raised its discount rate from 5.84 to 6.57 per cent., and at the same time the advance deposit required on imports of producer goods was raised from 1 to 5 per cent. and that on imports of consumer goods from 5 to 35 per cent.

The policy problems facing the Japanese authorities are now more complex than those which on previous occasions called for restraint. For one thing, the principal source of excess demand in the past was investment expenditure, which as a rule responded quickly to the application of monetary measures. However, investment demand, particularly for plant and equipment, was relatively weak last year, while tight labour-market conditions — a new development in Japan — led to sharply rising wages and consumption. For another thing, several developments of an external character have increased the need for a flexible and broadly-based set of policy instruments. In April 1964 the yen was formally made convertible, and Japan has also become a member of the OECD. At the same time, the narrowness of overseas capital markets has made it increasingly difficult to raise long-term capital abroad, and the balance-of-payments invisible account has tended gradually to deteriorate. Thus, while the restrictive measures already taken appear now to be having some effect, a more active use of monetary and budget policy, in combination, may be expedient in future.

II. DOMESTIC AND INTERNATIONAL PRICES.

Domestic prices and wages.

The general picture of price changes in the western industrial countries over the past twelve months has remained much the same as in preceding years. While prices have been relatively stable in North America, and also in the United Kingdom, they have continued to rise sharply in a number of continental countries. Extraordinary increases in food prices due to bad weather have played a smaller rôle since the spring of 1963 than in the previous twelve months; high demand and extreme tightness in the labour market were clearly the principal cause of the persistent inflation. A new factor contributing to rising prices was the firmer trend in world commodity markets.

Consumer prices. Consumer prices continued to rise in all industrial countries in 1963. The increase in western Europe as a whole worked out at about 4 per cent., roughly the same as in the preceding year.

Italy and France experienced the largest increases last year, with index gains of 7 and 6 per cent. respectively. They were followed by Finland and Spain, with rises of 5 per cent. In Austria, Belgium, Switzerland and the Netherlands consumer prices went up by about 4 per cent., in Germany and Sweden by 3½ per cent. and in Denmark by a little under 3 per cent.

The situation was more satisfactory in Norway, the United Kingdom, the United States and Canada, where increases of less than 2 per cent. were recorded.

With few exceptions, the contribution of food prices to the general price rise over the past year was smaller than in 1962-63, when they were affected by exceptionally bad weather. Only in Belgium and the Netherlands was most of the rise in 1963 due to food prices. In Sweden, Austria, Italy and Finland food prices accounted for about one-half of the overall increase, in France, Germany and the United Kingdom for roughly two-fifths, and in Switzerland, Denmark, Canada and the United States for approximately one-third. In Norway prices were kept steady in 1963 by means of subsidies on foodstuffs, but with their removal at the beginning of this year the price level has begun to move upwards again.

Services again played a major rôle in pushing up consumer prices, accounting for 20-25 per cent. of the rise in the index in France, the Netherlands, Italy and Canada and over 40 per cent. of the comparatively small increase in the United States. Another source of price pressure in 1963 was the further relaxation of rent control and the higher cost of new housing. In Italy controlled rents were raised again by 20 per cent. on 1st January 1963.

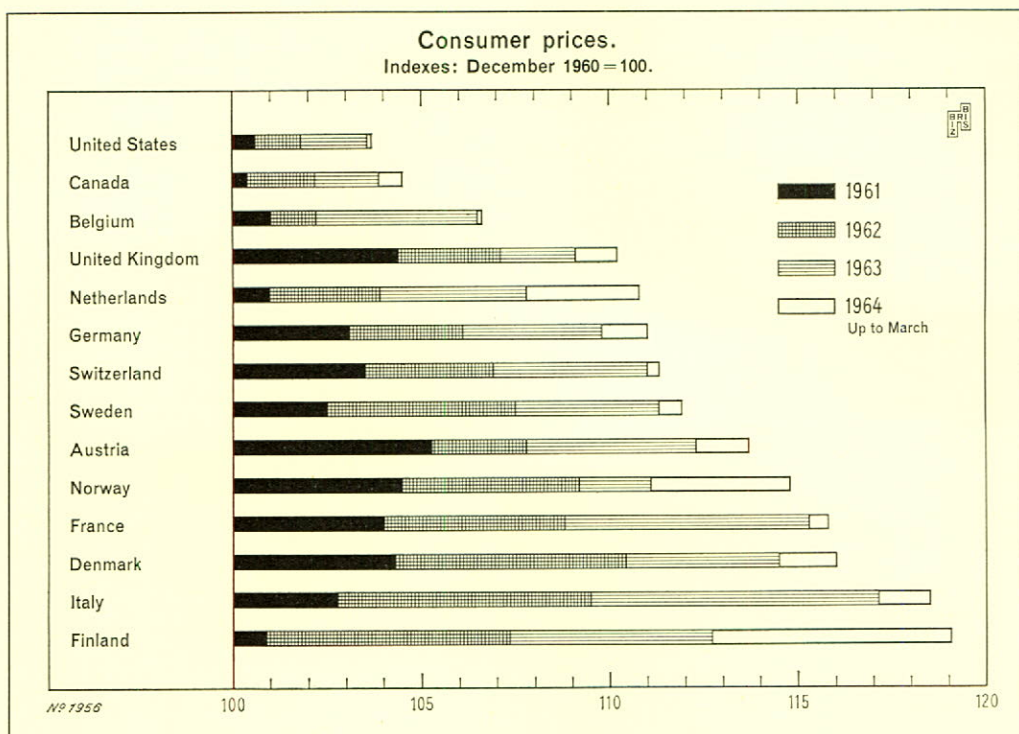
Consumer prices.

Countries	Total index, 1962	Total index and components, 1963				
		Total	Food	Rent	Light and fuel	Clothing
		percentage changes, December to December				
Austria	2.3	4.2	4.7	5.1	3.5	2.5
Belgium	1.2	4.2	5.7	.	.	.
Denmark	6.8	2.8	2.5	4.4	4.7	0.9
Finland	6.3	5.1	6.0	3.9	3.9	2.6
France	4.6	6.0	5.7	13.7	2.9	3.6
Germany	2.9	3.5	3.6	7.3	3.4	2.1
Italy	6.5	6.9	6.8	9.6	5.1	6.1
Netherlands	4.0	3.8	5.8	0.8	4.8	2.9
Norway	4.6	1.7	0.0	1.8	4.6	2.8
Spain	10.6	5.0	2.9	3.9	.	10.7
Sweden	4.9	3.5	6.1	1.2	2.0	0.7
Switzerland	3.2	3.9	3.3	7.2	3.5	3.1
United Kingdom	2.6	1.9	2.2	4.8	3.4	0.7
Canada	1.8	1.7	1.9	0.3	-2.8	2.6
United States	1.2	1.7	1.8	1.0	0.4	1.5

It was decided, however, not to proceed with the next stage of the progressive decontrol, and on 31st October, as part of the government's anti-inflation programme, rents of non-luxury dwellings were blocked for two years. In Switzerland permission was granted for controlled rents to be raised by 7 per cent. as from 1st October 1963. In Germany the decisive step was taken last year towards complete decontrol of rents: since 1st November rents have been freed on roughly 45 per cent. of the dwellings previously subject to control. Rents may not be increased by more than 20-25 per cent. in the first year, but after that they will be decontrolled altogether. Limited control still remains in those districts where demand exceeds 3 per cent. of the existing dwellings. As a result, rents in Germany went up by an average of 3 per cent. in the first four months of 1964, after rising by 7½ per cent. in 1963. In France and the Netherlands, it may be added, increases in controlled rents are scheduled for July 1964.

Over the past three years or so the cost of living has risen by somewhat more than 10 per cent. in Germany, the Netherlands, Sweden, Switzerland and the United Kingdom and by some 7 per cent. in Belgium. In Italy and France, as well as in Austria, Denmark, Finland and Norway, the increase was sharper, while in the United States and Canada, it was smaller.

The longer-run price trend for services, including rents, has been steeper than that for other retail prices, because, as living standards rise, demand for services and housing tends to increase more than proportionately, while productivity gains in these sectors are below the average. So far as rents are concerned, there is also the fact that a measure of control is still exercised in most European countries, so that, whenever rents have been allowed to move closer to their market level, increases have been substantial.



Examination of the consumer-price indexes for the eight-year period 1956-63 shows that prices of services rose appreciably more than the total index in all countries. The rent index, on the other hand, rose distinctly less than the total consumer-price index in the United States and Canada, where rents have long been decontrolled. In Europe, however, with the exception of Sweden, rents increased much more than the overall index — about twice as much in the Netherlands, the United Kingdom, Denmark, Germany and Switzerland, nearly three times as much in France and five times in Italy.

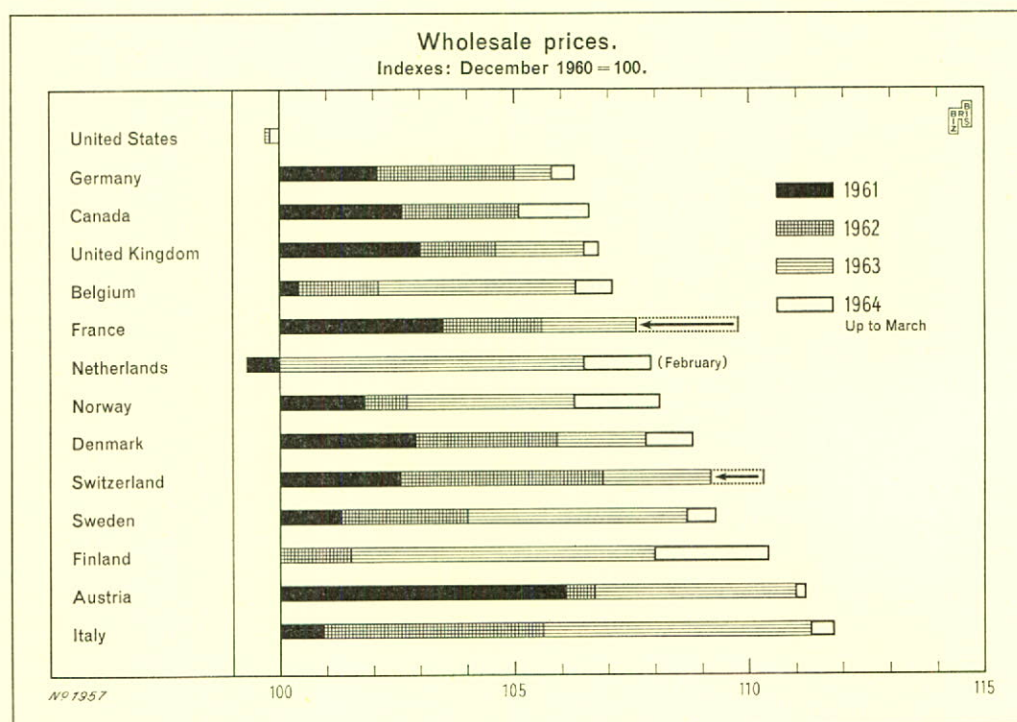
Wholesale prices and building costs. Wholesale prices in western Europe rose broadly in line with consumer prices in 1963, whereas in earlier years they had often tended to lag behind. For the area as a whole the increase came to over 4 per cent., compared with less than 3 per cent. in 1962. The biggest advances occurred in the Netherlands and Finland (6½ per cent.), Italy (5½ per cent.) and Sweden (4½ per cent.). An increase of 4 per cent. was recorded in Austria, Belgium and France. In Spain the overall index did not rise much, thanks to a fall in agricultural prices in the second half of the year resulting mainly from improved harvests. Wholesale prices fell slightly in the United States, where there has now been price stability for six years.

In most cases wholesale prices of manufactured goods rose less last year than those of foodstuffs and raw materials. In the three countries that account for two-thirds of western industrial production — the United States,

Wholesale prices.

Countries	Total index, 1962	Total index and components, 1963			
		Total	Agricultural products	Raw materials	Manufactured goods
		percentage changes, December to December			
Austria	0.5	4.0	4.6	3.5	.
Belgium	1.7	4.1	7.5	4.4	2.3
Denmark	2.9	1.9	0.9	5.3	1.9
Finland	1.5	6.4	9.0	10.7	2.1
France	2.1	3.9	4.5	5.8	2.8
Germany	.	.	5.4	2.9	0.7
Italy	4.6	5.5	3.7	5.9	.
Netherlands	0.7	6.5	15.0	1.9	3.5
Norway	0.9	3.5	4.8	3.4	0.9
Spain	5.7	0.9	— 1.4	1.6	2.0
Sweden	2.6	4.5	10.1	2.6	5.5
Switzerland	4.3	3.1	5.8	2.0	.
United Kingdom	.	.	6.1	4.7	1.8
Canada	2.4	1.4	— 7.0	0.8	1.6
United States	0.0	— 0.1	— 4.1	— 4.3	— 0.2

Germany and the United Kingdom — they rose moderately or even declined. Prices of agricultural products, on the other hand, increased by about 5½ per cent. (mostly concentrated in the first half-year), against a little over 4 per cent. in the previous year. And there was a marked turn-round in the price trend for raw materials, from near-stability to a 4 per cent. rise. In the last



month or two prices of foodstuffs and certain raw materials have again been showing a weaker tendency; in Canada and the United States, where developments often foreshadow the general trend, they have been declining.

Wholesale prices have generally risen less than consumer prices over the past three years. Most of the difference reflects services (including rents). The largest increase in wholesale prices during this period has been in Italy — 12 per cent. Elsewhere in Europe the rises have generally been within the range of 6–10 per cent. In the case of the Netherlands the whole of this increase occurred in 1963.

In the construction sector, demand pressure has remained very high, skilled labour has been in particularly short supply and productivity gains, particularly in house-building, are still limited. The rise in building costs accelerated in most countries last year, though not in Germany, the United Kingdom or the Scandinavian countries.

Building costs.

Countries	1961	1962	1963	1961–63
	percentage increases, December to December			
Austria	6.3	1.1	7.5	15.5
Denmark	8.0	7.4	2.3	18.6
Finland	3.2	4.7	7.4	16.0
France	3.5	6.1	9.6	20.4
Germany	9.0	7.9	4.6	23.0
Italy*	3.0	8.1	9.0	21.3
Netherlands*	2.4	1.4	6.5	10.7
Norway	6.7	3.9	2.3	13.4
Sweden	4.3	4.1	3.9	12.8
Switzerland	7.4	7.1	8.9	25.2
United Kingdom	5.3	2.5	2.4	10.5
United States	1.6	2.4	3.2	7.4

* Annual average changes, compiled from GNP deflator for dwellings.

Over the period 1961–63 building costs went up least — by 7½ per cent. — in the United States, where rationalisation of this sector is most advanced. In western Europe the increase has ranged from about 10 to 25 per cent. These figures are generally greater than the movement in either consumer or wholesale prices.

Wages. The broad geographical pattern of money wage increases is essentially the same as that of prices. In North America earnings have continued to rise by 3 or 4 per cent. per annum — slightly less than productivity. Much the same can be said, so far as 1963 is concerned, of the United Kingdom; but it remains to be seen whether wages will accelerate now that the UK economy has regained a higher level of activity.

The continental countries, on the other hand, have continued to show wage rises greatly in excess of productivity gains. The size of the advance over the past year has again been of the order of 7 or 8 per cent. in most

countries. By comparison with the previous year this represented an increase in Austria, Finland and Switzerland, but some easing in Germany and — towards the end of the period — France and Sweden. The situation was also healthier in Norway, where the rate of wage increase has been cut to around 5 per cent.

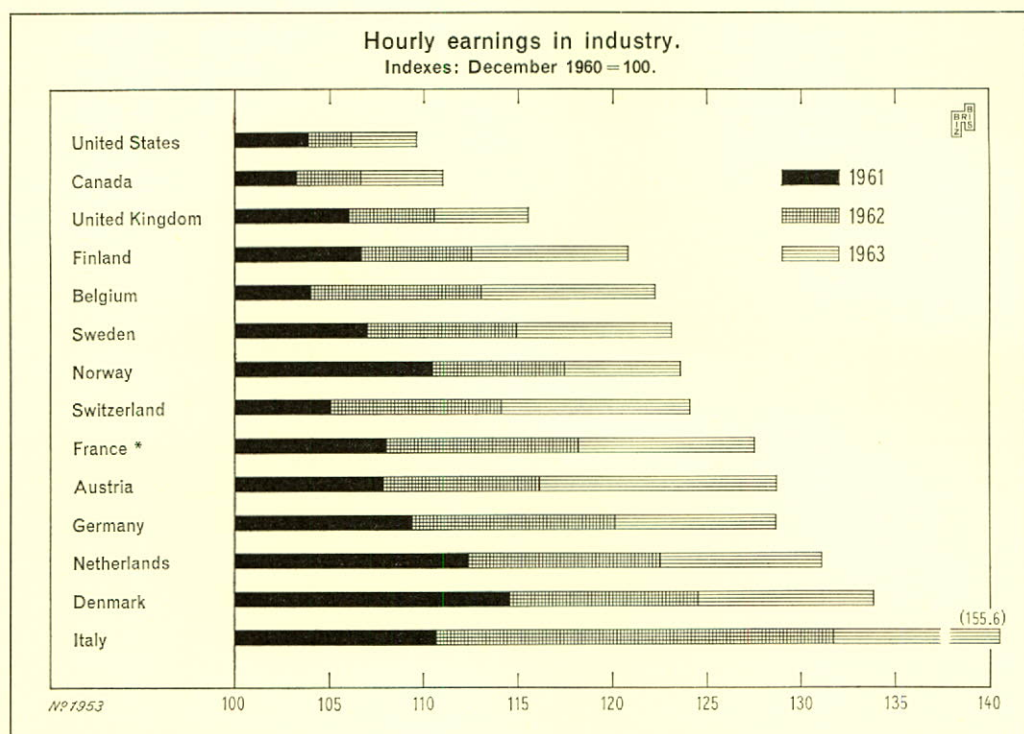
The most serious problem of wage inflation over the past year was in Italy, with a rise of between 15 and 20 per cent. for the second year running. This trend, which originally emerged from contractual wage negotiations, has persisted very largely because of the automatic links with the cost-of-living index. In the Netherlands the wage increase remained within relatively narrow bounds until late in 1963; as a result of the new pay agreements, however, earnings are expected to go up by about 15 per cent. in 1964.

Wages in industry.

Countries	Wages	Nominal				Real	
		1961	1962	1963	1961—63	1963	1961—63
		percentage increases, December to December					
Austria	Rates	7.6	3.5	9.9	22.4	5.4	9.0
	Earnings	7.9	7.6	10.9	28.7	6.4	14.6
Belgium	Earnings	4.0	8.7	8.2	22.2	3.8	14.8
Finland	Earnings	6.7	5.5	7.4	20.8	2.2	7.2
France	Rates	8.0	9.5	7.9	27.5	1.8	10.5
	Rates	8.4	8.5	5.8	24.4	2.3	13.3
Germany	Earnings	9.4	9.8	7.1	28.7	3.5	17.2
	Rates	7.6	6.0	15.8	32.1	8.3	12.8
Italy	Earnings	10.6	19.1	18.2	55.6	10.5	32.9
Netherlands	Rates	6.2	11.6	4.6	24.0	0.8	15.0
	Earnings	12.4	8.9	7.0	31.1	3.1	21.6
Norway	Earnings	10.5	6.3	5.2	23.6	3.5	11.2
Sweden	Earnings	7.0	7.4	7.1	23.1	3.5	10.7
Switzerland	Rates	4.6	5.5	6.3	17.3	2.3	5.7
	Earnings	5.1	8.5	8.8	24.1	4.7	11.8
United Kingdom	Rates	2.9	4.0	4.2	11.5	2.3	2.2
	Earnings	6.1	4.2	4.5	15.5	2.6	5.8
Canada	Earnings	3.3	3.2	4.1	11.0	2.4	6.9
	Earnings	3.9	2.1	3.3	9.6	1.6	5.8
United States	Earnings						

Inter-country differences in the movement of real wages have largely followed those of money wages. The rise in prices has been such, however, that only in the Benelux and the North American countries has the increase in real wages since 1961 amounted to more than half of the increase in nominal wages.

The climate of industrial relations, which had tended to worsen during 1962-63, has generally been more satisfactory in recent months. In some cases, for instance Germany, this may partly reflect the fact that no major wage agreements have recently fallen due for renewal. Elsewhere, however, particularly in the Scandinavian countries and the United Kingdom, policies appear to have exerted greater influence in helping to keep the rise in incomes in line with the trend of productivity. In the United States the



* Wage rates.

authorities were successful in the spring of 1964 in settling the four-year dispute between the railway unions and employers.

Prices and production of raw materials.

For a whole decade, until 1962, raw-material prices had been weakening. Then, in the autumn of that year, the tide began to turn. This change was attributable to the improvement in business activity in the United States, western Europe and Japan. But, in addition to the underlying cyclical forces of expansion, other factors, such as crop failures and a sudden strong demand from eastern-bloc countries, played a part in the price rise. The USSR had to import large quantities of wheat, whereas before it had been a net exporter. Mainland China, too, has again become a heavy importer of wheat. The position is similar with regard to textiles, the USSR having begun to make extensive purchases of wool in Australia and New Zealand, possibly owing to the decimation of its own flocks during the severe winter of 1962-63, and to buy substantial amounts of long-staple cotton. Finally, it may be noted that the USSR has reduced, or in some cases ceased, its exports of non-ferrous metals.

At first, from October 1962 to March 1963, the rise in the average price level was due to price increases for a few products — principally sugar, cocoa, sisal and steel scrap. In the spring of 1963, however, the recovery spread to a wider range of products. Notable exceptions were raw materials with "administered" prices.

The expansion of raw-material production capacity was initiated immediately after the war and during and after the Korea boom. Output, however, could be raised only slowly and over a long period and could not be rapidly cut back when prices began to recede. Despite the growth of consumption, therefore, supply exceeded demand. This situation led to the ten-year erosion of raw-material prices, which eventually discouraged further investment designed to expand output, until in 1962 some kind of balance was at last achieved. The change in the price trend coincided with the Cuba episode and the Sino-Indian dispute. The subsequent acceleration of demand for raw materials took producers by surprise. In view of the previous steady decrease in prices, restrictions had been placed on output and they could not be readily lifted in order to adapt supply to the increase in demand. These supply difficulties gave rise to concern about possible shortages, which pushed up demand still further and led to a renewed advance of prices.

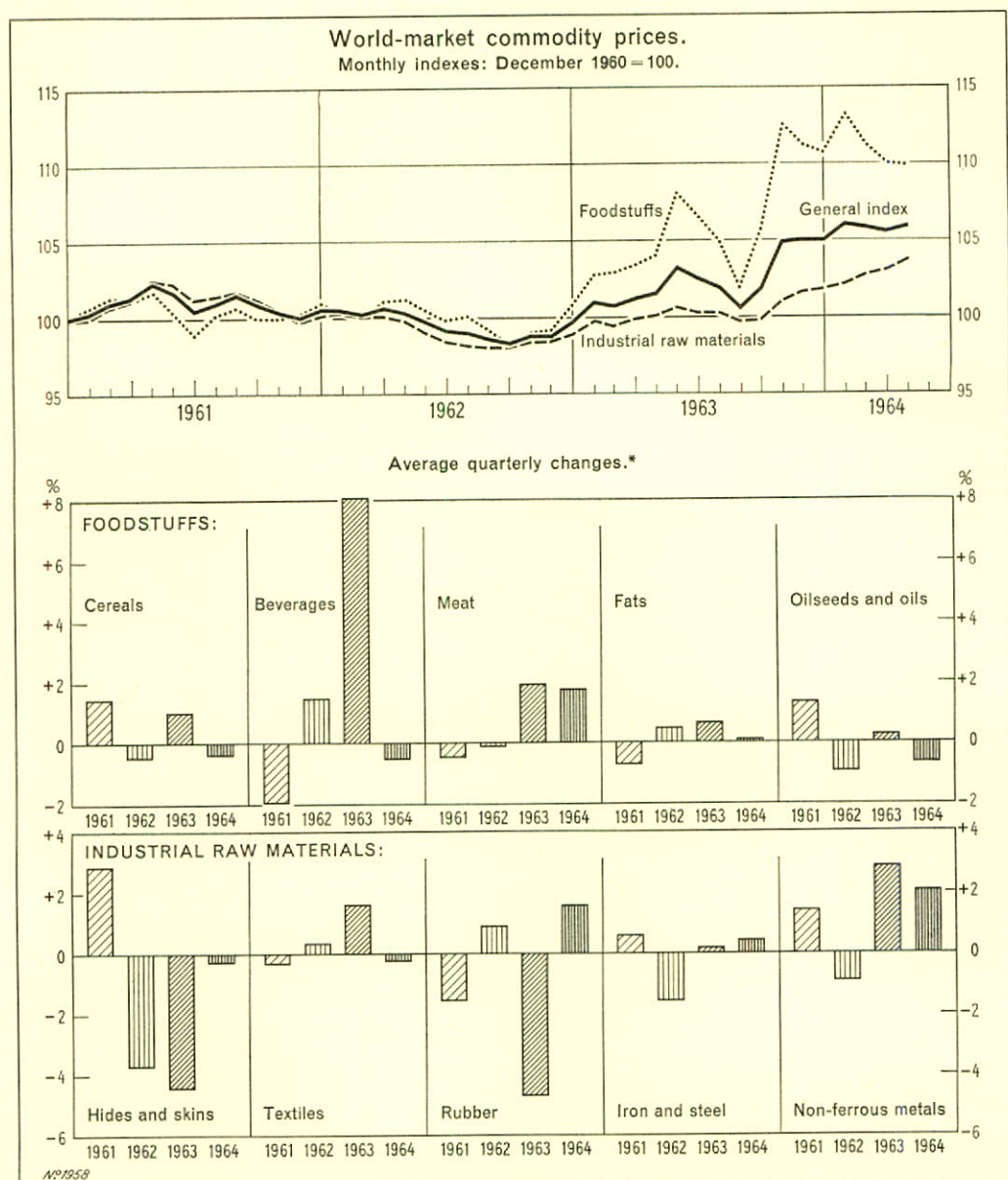
Though the 1963 harvests were not at all bad in the world as a whole, crop failures in some regions resulted in keen demand for agricultural products, and especially for foodstuffs. Consequently a larger proportion of all crops was exported. Wheat exports, for example, reached a record level in 1963.

* * *

In the six years from the end of 1956 to the autumn of 1962 sterling prices of raw materials on British markets fell by about 20 per cent. The price indexes of Reuter and the Financial Times have since then advanced by nearly 20 per cent., so that the lost ground has been recovered. According to Moody's Index, quotations on US markets also declined by an average of some 20 per cent. during the six-year period. The subsequent gain until the beginning of May 1964, however, worked out at only just 5 per cent.

The trend in world-market prices is perhaps best indicated by Schulze's Index, which covers a larger number of commodities and markets than other indexes. It shows an overall rise of 5 per cent. from the low in autumn 1962 until May 1963. Foodstuffs, which climbed by 10 per cent., made a greater contribution to this improvement than industrial raw materials, which went up by only 2½ per cent. In the following three months the index declined somewhat, without, however, returning to the low starting-point of the autumn of 1962. After this break an even stronger upward movement set in, and by the beginning of 1964 the general index was 8 per cent. above the level in the autumn of 1962, industrial raw materials having gone up by 4 per cent. and foodstuffs by 15 per cent.

Among foodstuffs, prices of cereals did not rise much, although they were in the limelight in the second half of 1963 when the USSR entered the market to purchase considerable quantities of wheat. Prices for beverages and sugar rose by 50 per cent. between September 1962 and January 1964; they have since fallen, however, by some 10 per cent. During the last twelve months prices of meat and meat products have gone up by a good 20 per cent., while fats and oils have remained quite stable.



* 1964: first quarter.

The rise in industrial raw-material prices was fairly moderate; it was attributable partly to textile fibres and to iron and steel, but chiefly to non-ferrous metals, prices of which have increased by some 15 per cent. since the autumn of 1962. The index figures for the rubber group and, especially, for hides and skins have dropped appreciably; supplies of hides and skins are abundant, as meat consumption has recently been at a high level, while demand is relatively weak, as the shoe industry is making increasing use of synthetic materials.

Thus, the improved price conditions for raw materials as a whole have been due to the movements of a few groups of products and are by no

Prices of major commodities.

Commodities	Markets	Changes during			
		1961	1962	1963	1964 to April
		in percentages			
Materials of industrial origin					
Crude oil	Bradford, Pa.	— 3.5	0.0	0.0	— 3.2
Crude oil	Venezuela	0.0	0.0	0.0	0.0
Coal	USA	— 0.9	— 2.0	— 3.4	— 0.4*
Copper	London	— 0.5	+ 1.8	+ 0.7	+ 32.5
Tin	London	+ 19.3	— 9.5	+ 17.6	+ 3.3
Lead	London	— 6.9	— 8.3	+ 34.1	+ 10.7
Zinc	London	— 13.8	— 6.1	+ 41.3	+ 14.4
Aluminium ingots .	USA	— 7.7	— 6.3	+ 2.2	+ 2.2
Mercury	New York	— 9.1	— 1.8	+ 16.8	+ 21.3
Steel bars	ECSC	— 9.9	— 12.1	+ 6.0	+ 11.6
Steel, section	USA	— 4.2	0.0	+ 3.5	0.0
Steel scrap	Pittsburgh	+ 32.5	— 26.6	— 0.3	+ 19.9
Rubber, synthetic . .	New York	0.0	0.0	0.0	.
Rayon yarn	USA	0.0	0.0	0.0	0.0*
Rayon staple	USA	— 3.6	0.0	+ 3.7	0.0*
Materials of agricultural origin					
Wool	Melbourne	+ 19.8	+ 5.8	+ 36.3	— 5.4
Cotton	New York	+ 8.3	— 0.2	+ 0.9	+ 0.7
Cotton	Alexandria	— 5.6	+ 7.5	+ 7.0	+ 14.2
Jute	London	— 28.4	— 7.9	— 8.7	— 2.3
Sisal	London	— 15.9	+ 43.0	+ 19.4	0.0
Hides	Chicago	+ 17.6	— 6.3	— 32.2	— 16.6*
Rubber, natural . . .	Singapore	— 9.5	+ 3.8	— 18.9	+ 5.5
Wood-pulp	Sweden	— 3.7	— 3.7	— 1.5	.
Foodstuffs					
Wheat	Winnipeg	+ 13.3	+ 3.7	+ 4.6	+ 1.5
Maize	New York	+ 4.5	+ 2.4	+ 5.3	+ 2.1
Sugar	New York	— 18.5	+ 74.1	+ 129.1	— 22.1
Cocoa	New York	+ 2.4	— 16.6	+ 21.7	— 16.6
Coffee	New York	— 5.8	— 1.3	+ 11.1	+ 31.2
Copra	London	— 6.1	+ 15.6	+ 5.3	— 1.9
Soya beans	Chicago	+ 10.6	+ 1.0	+ 11.7	— 7.1
Cotton-seed oil . . .	New York	+ 18.9	— 17.1	— 7.6	— 1.4
Lard	New York	— 12.6	— 12.9	+ 15.3	+ 4.2

* Up to March.

means general or uniform. Increased demand has led in some cases and in some sectors, but not throughout, to price increases. This differentiated development is best illustrated by grouping together the more important products in which the main changes have occurred. Four groups are discernible. From September 1962 to December 1963 prices

- (i) fell for rice, cotton-seed oil, natural rubber and, in particular, hides and skins;
- (ii) were practically stable for cotton, copper, steel, steel scrap (which is particularly sensitive to cyclical fluctuations) and wheat;
- (iii) rose for a fairly large number of commodities, namely maize, copra, soya beans and coffee (the latter only during the last quarter of 1963), and for certain non-ferrous metals — tin, mercury and silver;

- (iv) recorded a sharp rise in the case of sugar, cocoa, sisal, wool, zinc and lead.

Agricultural products were thus mainly responsible for the upward movement of raw-material prices from the autumn of 1962 until the end of 1963. In 1964 the situation changed. In the first four months of 1964

- (i) prices fell, in certain cases substantially, for sugar, cocoa, copra, soya beans, wool and hides and skins;
- (ii) prices of other foodstuffs, namely rice, wheat, maize and cotton-seed oil, remained stable, as did those of cotton, sisal and silver;
- (iii) an appreciable increase occurred in the case of natural rubber, lead, tin, copper, zinc, mercury, steel and steel scrap, and the price of coffee also began to rise sharply.

This renewed partial price boom for raw materials so far in 1964 is mainly based on metals and, in particular, non-ferrous metals, for which the industrial upswing has created a corresponding demand.

Tin. The restrictive policy pursued by the tin industry since before the war has been reflected over the past three years in a shortfall of supplies. At present output is lagging behind consumption by some 18,000 tons per annum. Last year half of this shortfall was covered by releases from the US surplus reserve (which then amounted to some 165,000 tons) and one-sixth by sales by the buffer pool; for the remainder producers, dealers and consumers had to run down their stocks.

In the middle of May 1963 the price of tin, at £908 per long ton, had come close to the level at which, under the International Tin Agreement, the buffer pool may sell. In fact its stock was only just 3,000 tons, so that it had to retire from the market. On 5th December the International Tin Council raised the ceiling price at which the buffer pool must sell from £965 to £1,000 per ton.

The upswing, however, continued: at the end of the year the £1,000 mark was passed and in February 1964 the price reached £1,250 a ton, the highest recorded since 1951. On 20th March the US Administration agreed to a new liquidation programme enabling 20,000 tons to be sold over the coming twelve months at prices consistent with the prevailing market level. After this demand quietened down and the price fell to £1,052 per ton at the end of March and £1,038 by the beginning of May 1964.

Zinc. The price of zinc has gone up far more than that of tin. At the beginning of 1963 the London settlement price for zinc was £65⁷/₈ per long ton; by the end of the year it had climbed to £97³/₈ and on 11th May 1964, at £128, it reached its highest level since the resumption of trading in zinc on the London Metal Exchange on 2nd January 1953. As with other metals, immediately available supplies are very short. Leading producers, fearing that aluminium or synthetic materials might be substituted for their

product, have tried to keep prices down by means of periodic sales, but they have not succeeded in the face of rising demand due to the continuing boom in the motor-car industry in the United States and Europe and also to the high level of building activity.

Copper. From March 1962 onwards the leading producers and exporters succeeded in keeping the price of copper stable. They fixed a selling price of £234¹/₈ a long ton for regular customers and maintained it by constant intervention. At the end of 1963, however, prices came under pressure and in the middle of January 1964 producers withdrew from the market. On 24th February the settlement price for copper wire bars on the London Metal Exchange was £277 a ton; thereafter it continued to rise, reaching £319 a ton on 13th April 1964, the highest quotation since 1956. The producers' efforts to keep prices stable were thus thwarted, as copper consumers wished to build up their stocks, while disputes and strike threats in North and South America and political unrest in East Africa strengthened the climate for a price rise. All restrictions on output and sales were lifted quickly, but it was too late. Production of copper is, however, large enough to preclude any genuine shortage and to meet further increases in demand.

Rubber. The position of natural rubber has been rather weak for a long time, notwithstanding the boom in the motor-car industry. As a result of competition from the synthetic product, prices of natural rubber tended downwards throughout 1963. They declined from 24³/₄d. to 19³/₈d. per lb. (reaching on 9th September, at 18³/₄d. per lb., their lowest level since 1954). In March 1964 quotations picked up somewhat under the impact of Soviet purchases, and at the beginning of May 1964 the price stood at 20¹/₂d. In 1963 the share of natural rubber in total rubber consumption in the West was for the first time less than one-half (in the United States, the chief consumer country, it is already less than one-quarter).

Wool. Although synthetic fibres have made further progress and cotton consumption has been sustained, demand for wool rose markedly in 1963 and has continued to do so in 1964. Exports from New Zealand and Australia in 1963-64 increased by nearly 10 per cent. compared with a year earlier. Production has risen steadily since the end of the war, but recently it has lagged behind the growth of consumption. Although the gap was covered last year from stocks in producing countries and from former strategic reserves, prices were affected. In the middle of November 1963 quotations for Australian merino were about 30 per cent. higher than a year before and in fact the highest for six years, while crossbreds from New Zealand were at their highest for twelve years.

Sugar. The decline in world sugar crops caused sugar quotations to soar in 1962-63. In that year the crop amounted to only 50 million tons, compared with 55 million tons in 1960-61. In 1963-64, however, world production is expected to reach 53 million tons. Meanwhile, prices, though lower than they

were last year, can still be regarded as being favourable for producers. In May 1963, at 12.60 cents per lb., the highest quotation since 1920 was registered. The price subsequently declined sharply until August 1963, but even then, at 5.62 cents, it was well above the former trough of little more than 2 cents a lb. It then recovered once more and after some ups and downs stood late in May 1964 at 6.32 cents.

Wheat. Prices of wheat and other cereals have strengthened somewhat over the last twelve months, although crops proved to be better than had been expected. The supply difficulties that have arisen during the current crop year have been due not to any overall shortage but more to geographical differences. On the one hand, the four traditional exporting countries (Argentina, Australia, Canada and the United States) increased their crop from 58.5 million tons in 1962-63 to 67.1 million in 1963-64; of this Canada accounted for nearly 20 million — the largest crop in its history. On the other hand, there were shortfalls in other regions, which forced former net exporters to arrange temporarily for substantial imports. The USSR had suddenly to contract for imports of over 10 million tons from western countries, including 6.6 million tons from Canada, 1.6 million tons from Australia and about 1 million tons from the United States.

Cocoa. The price of cocoa had reached its highest level for three years early in May 1963 at 29.17 cents a lb. At that time nearly all of Ghana's and Brazil's crops had been sold and the marketing boards in Ghana and Nigeria had withdrawn from the market. The UN Cocoa Conference, which took place in Geneva from 26th September to 24th October 1963 and which it was hoped would result in an agreement to ensure fair prices and to eliminate excessive swings in quotations for this commodity, failed. At the beginning of 1964, however, the price began to decline and by 10th April it had fallen to 22 cents. By this time it was known that west African crops in 1963-64 would be much larger than was expected at the end of last year, while the increase in consumption has lately been much slower than in the past.

World output of basic commodities. The growth of nearly 5 per cent. in industrial output in western Europe and North America last year led to an increase in demand for industrial raw materials, world production of which in general expanded, though at a slower rate than in the preceding year.

Considerable increases in output were recorded for fuels (including mineral oil) and man-made fibres. World steel production, too, increased by about 7 per cent. Output of non-ferrous metals went up by less than the average for industrial raw materials, with the effects already described on prices. Output of tin (which is below its pre-war level) remained stationary last year, whereas that of aluminium expanded by a further 9 per cent. and is now eleven times as high as in 1937.

In terms of volume, production of raw materials of industrial origin was over 6 per cent. greater in 1963 than in the preceding year. That of raw

Estimates of world production of basic commodities.

Commodities	Units (metric)	1937 ¹	1962	1963 preliminary	Percentage change		
					1962 over 1961	1963 over 1962	1963 over 1937
Aluminium ²	1000 tons	493	5,002	5,466	+ 9	+ 9	+ 1,009
Natural gas	milliard m ³	78	557	590	+ 9	+ 7	+ 658
Rubber, natural	1000 tons	986	2,139	2,096	+ 7	+ 3	+ 426
Rubber, synthetic	1000 tons	63	3,200	3,420	+ 12	+ 10	+ 422
Man-made fibres	1000 tons	834	3,948	4,350	+ 8	+ 7	+ 366
Crude oil	million tons	280	1,214	1,305	+ 6	+ 4	+ 352
Hydro-electricity	milliard kWh	177	768	800	+ 7	+ 4	+ 351
Cement	million tons	83	358	373	+ 3	+ 4	+ 184
Brown coal	million tons	252	686	715	+ 2	+ 7	+ 183
Steel	million tons	136	361	385	— 2	— 8	+ 173
Nickel ³	1000 tons	119	352	325	— 2	+ 3	+ 153
Soya beans	million tons	12	31	31	+ 3	+ 2	+ 140
Manganese ore	million tons	6	14	14	+ 4	+ 3	+ 116
Zinc ²	1000 tons	1,636	3,423	3,530	+ 2	+ 1	+ 110
Copper ⁴	1000 tons	2,534	5,281	5,325	— 2	+ 5	+ 109
Sugar	million tons	25	50	53	+ 1	+ 8	+ 104
Maize	million tons	115	217	235	— 2	+ 4	+ 100
Mercury	tons	4,590	8,837	9,200	+ 3	+ 1	+ 78
Fats and oils ⁵	million tons	19	33	33	+ 8	+ 5	+ 70
Hard coal	million tons	1,291	2,100	2,200	— 1	+ 4	+ 69
Lead ⁴	1000 tons	1,692	2,751	2,860	— 4	0	+ 66
Tungsten	1000 tons	39	65	65	+ 6	+ 3	+ 64
Cotton	1000 tons	6,661	10,607	10,895	— 7	— 2	+ 63
Coffee, green	1000 tons	2,420	4,020	3,955	+ 1	— 1	+ 61
Rice, rough	million tons	152	247	245	— 3	+ 3	+ 59
Cocoa	1000 tons	732	1,134	1,165	— 18	+ 7	+ 55
Jute	1000 tons	1,965	2,900	3,100	— 1	+ 2	+ 53
Wool	1000 tons	1,718	2,578	2,626	+ 11	— 5	+ 49
Wheat	million tons	167	263	249	+ 1	— 2	+ 41
Hard fibres	1000 tons	640	920	900	— 1	0	— 3
Tin ²	1000 tons	205	199	199			

¹ 1934-38 averages for agricultural products. ² Smelter production. ³ Metal content of mine production. ⁴ Refinery production. ⁵ Oil equivalent.

materials of agricultural origin (textile fibres and natural rubber), on the other hand, went up by 2 per cent. Output of all raw materials — of both agricultural and industrial origin — rose by 4 per cent., compared with 5 per cent. last year. Production of foodstuffs remained at about the same level as in the preceding year: the maize crop was larger than in 1962, while the rice crop remained more or less stable and the wheat harvest was smaller.

Since before the war production of foodstuffs and agricultural commodities has risen by about two-thirds, while that of industrial raw materials has more than trebled. Output of all the basic commodities shown in the table has risen two and a half times.

III. WORLD TRADE AND PAYMENTS.

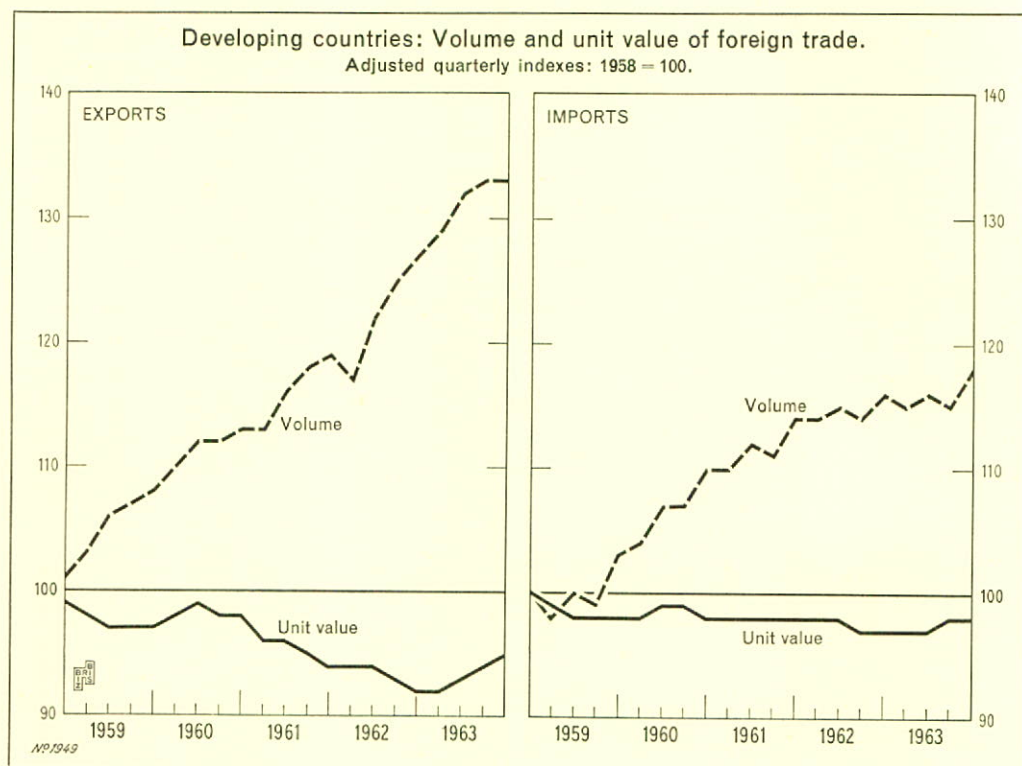
Since 1961 the expansion of world trade has been gathering momentum and in 1963 it amounted to 8.4 per cent. in value, against 5.7 per cent. the year before. As in 1962, western Europe's imports increased faster than its exports; the counterpart of this movement is to be found, generally speaking, in a bigger US export surplus and decreasing deficits in the developing areas.

International trade, by areas.

Areas	Exports (f.o.b.)			Imports (c.i.f.)			Changes in volume of trade 1961-63	
	1961	1962	1963	1961	1962	1963	Exports	Imports
	in milliards of US dollars						in percentages	
Developed areas								
Western Europe								
EEC	32.3	34.2	37.5	32.1	35.8	40.4	+ 16	+ 26
EFTA	19.5	20.5	22.2	23.6	24.6	26.4	+ 12	+ 11
Other countries	3.5	3.7	4.0	5.2	5.9	6.7	+ 5	+ 28
Total for western Europe . . .	55.3	58.4	63.7	60.9	66.3	73.5	+ 14	+ 20
United States and Canada	27.1	27.9	30.0	22.3	24.1	25.2	+ 12	+ 13
Other developed areas*	8.7	9.5	10.6	10.6	10.5	12.3	+ 15	+ 17
Total for developed areas . . .	91.1	95.8	104.3	93.8	100.9	111.0	+ 13	+ 18
Developing areas								
Latin America	9.6	10.2	10.8	10.0	10.1	9.9	+ 10	+ 4
Other areas	17.8	18.6	20.4	20.5	21.0	21.8	+ 14	+ 2
Total for developing areas . . .	27.4	28.8	31.2	30.5	31.1	31.7	+ 13	+ 3
World total	118.5	124.6	135.5	124.3	132.0	142.7	+ 13	+ 14

* Australia, Japan, New Zealand and South Africa.

Over the period 1953-61 the value of developing countries' exports rose by 3.1 per cent., while their imports increased by 4.5 per cent. per annum. A change for the better occurred in 1962, when export earnings began to rise faster than import expenditure. This improvement (which was accompanied, however, by a slowing-down of domestic production) was due, on the export side, to a rise in volume, prices having continued to decline until the end of the year. The increase in exports reflected chiefly the recovery in import demand in the United States but also the continuing, though slower, growth of sales to Europe. In 1963, on the other hand, the additional demand for primary products came mainly from western Europe and Japan. The 8 per cent. rise in developing countries' exports (against one of 5.3 per cent. in 1962) reflected an increase in both volume and prices. As measured by quarterly figures, the falling trend of export prices was reversed at the



beginning of 1963, and in the last quarter unit values were 4.5 per cent. higher than in the corresponding period of 1962.

Developing countries' imports were kept under control by a wide range of restrictive measures, which had been tightened after the decline in foreign exchange reserves in 1960-61. They increased in volume by some 1 per cent. in both 1962 and 1963. Thanks to the rise in their exports and the virtual stability of their imports the trade deficit of these countries was reduced by \$800 million in 1962 and \$1,800 million last year.

In the group of countries comprising Australia, Japan, New Zealand and South Africa imports remained stable in 1962, while exports showed a rise which was almost entirely accounted for by Japan. In 1963 imports increased by 17 per cent. and exports by 12 per cent., so that the balance of trade of the group as a whole deteriorated by some \$650 million. This change conceals, however, widely divergent movements. While Australia improved its balance by \$200 million, the balances of Japan, South Africa and New Zealand deteriorated by roughly \$550, 250 and 50 million respectively.

As regards western Europe, OECD countries' exports to other OECD countries rose, as in previous years, more than their exports to the rest of the world, namely by 12 per cent., compared with only 4 per cent. Their imports from the rest of the world went up by 9 per cent.

The expansion of intra-European OECD trade reflects chiefly a 17 per cent. growth of trade among EEC countries. In Italy and France, where

inflationary pressures were prevalent, there was an increase in purchases from EEC partners of 31 and 24 per cent. respectively, the counterpart of which is to be found in steep rises in the exports of Germany, Belgium and the Netherlands.

In all areas the 1963 expansion of trade began in the second quarter. In western Europe it continued at a fairly steady rate until the end of the year and accelerated in the early months of 1964. In the United States trade expanded at a lower rate after the middle of 1963 and this continued into the first quarter of 1964. In other developed countries, as well as in the developing countries, the expansion gathered speed throughout 1963, except in the third quarter.

Balances of payments.

European OECD countries. In 1963 the combined current account of the European OECD countries deteriorated by \$800 million in relation to the previous year. This deterioration was essentially due to a worsening of the trade position of the EEC countries, that of the EFTA countries having improved somewhat.

The balance on current account of the EEC countries shifted from a surplus of \$680 million in 1962 to a deficit of \$30 million last year. There were three big changes: a rise of over \$1 milliard in the Italian import surplus, a fall of \$365 million in the French export surplus and an increase of \$740 million in the German export surplus, the latter resulting chiefly from an upsurge of exports in the last quarter of 1963 while imports remained stable.

The combined current deficit of the EFTA countries was reduced from \$435 million in 1962 to \$260 million last year. The overall improvement resulted from substantial rises in Danish and UK exports. Portugal trimmed its current deficit with an increase in net receipts from services — mainly tourist receipts and workers' remittances. The current position of the four other EFTA countries weakened: import surpluses expanded in Austria, Norway and Switzerland, while in Sweden there was a fall in the net return on invisible transactions. For the EFTA group as a whole net invisible receipts remained practically unchanged in 1963.

With the exception of Greece, the current balance of the five remaining OECD countries worsened in 1963. In Iceland and Ireland imports grew faster than exports. In Spain increased economic activity and further liberalisation pushed imports up by \$400 million, while exports did not expand. In Turkey exports actually declined and imports rose substantially. In Greece and Spain net tourist receipts and emigrants' remittances continued to go up in 1963. In the case of Spain, however, the increase was not sufficient to offset the rise in imports and the current surplus of \$55 million achieved in 1962 gave way to a deficit of \$130 million.

European OECD countries: Balances of payments.

Countries	Years	Trade balance (f.o.b.)	Services ¹	Current balance	Net capital movements (inflow+) ²		Overall balance ³
					Long-term	Short-term	
Belgium-Luxemburg . . .	1962	— 130	+ 210 ⁴	+ 80	— 140		— 60
	1963	— 110	+ 10 ⁴	— 100	+ 325		+ 225
France	1962	+ 485	+ 345	+ 830	— 320	+ 175 ⁵	+ 685
	1963	+ 120	+ 320	+ 440	+ 70	+ 350 ⁵	+ 860
Germany	1962	+ 1,600	— 2,155	— 555	+ 40	+ 295	— 220
	1963	+ 2,340	— 2,090	+ 250	+ 535	— 65	+ 720
Italy	1962	— 1,425 ⁶	+ 1,675	+ 250	— 200	— 20	+ 30
	1963	— 2,495 ⁶	+ 1,605	— 890	— 355	+ 835	— 410
Netherlands	1962	— 415	+ 490	+ 75	— 80	— 10	— 15
	1963	— 360	+ 630	+ 270	— 115	+ 15	+ 170
Total for EEC	1962	+ 115	+ 565	+ 680	— 260		+ 420
	1963	— 505	+ 475	— 30	+ 1,595		+ 1,565
Austria	1962	— 280	+ 365	+ 85	+ 150		+ 235
	1963	— 340	+ 365	+ 25	+ 120		+ 145
Denmark	1962	— 290	+ 100	— 190	+ 80	+ 85	— 25
	1963	— 65	+ 115	+ 50	+ 155	+ 15	+ 220
Norway	1962	— 690 ⁶	+ 515	— 175	+ 170		— 5
	1963	— 750 ⁶	+ 555	— 195	+ 245		+ 50
Portugal	1962	— 215	+ 145	— 70	+ 170		+ 100
	1963	— 240	+ 180	— 60	+ 95		+ 35
Sweden	1962	— 200 ⁶	+ 170	— 30	+ 40	+ 80	+ 90
	1963	— 185 ⁶	+ 145	— 40	+ 20	— 25	— 45
Switzerland	1962	— 790 ⁶	+ 450	— 340	+ 455		+ 115
	1963	— 820 ⁶	+ 440	— 380	+ 580		+ 200
United Kingdom	1962	— 190	+ 475	+ 285	— 250	+ 515	+ 550
	1963	— 120	+ 460	+ 340	— 410	— 90	— 160
Total for EFTA	1962	— 2,655	+ 2,220	— 435	+ 1,495		+ 1,060
	1963	— 2,520	+ 2,260	— 260	+ 705		+ 445
Greece	1962	— 450 ⁶	+ 370	— 80	+ 95	+ 5	+ 20
	1963	— 450 ⁶	+ 400	— 50	+ 100	— 35	+ 15
Iceland	1962	0	+ 5	+ 5	+ 5		+ 10
	1963	— 10	+ 5	— 5	+ 10		+ 5
Ireland	1962	— 280 ⁶	+ 245	— 35	+ 50		+ 15
	1963	— 310 ⁶	+ 255	— 55	+ 100		+ 45
Spain	1962	— 535	+ 590	+ 55	+ 125	— 20	+ 160
	1963	— 935	+ 805	— 130	+ 210	+ 20	+ 100
Turkey	1962	— 220 ⁶	+ 70	— 150	+ 125		— 25
	1963	— 270 ⁶	+ 55	— 215	+ 165		— 50
Grand total	1962	— 4,025	+ 4,065	+ 40	+ 1,620		+ 1,660
	1963	— 5,000	+ 4,255	— 745	+ 2,870		+ 2,125

¹ Including unilateral transfers. ² Calculated as the difference between the current account on the one hand and the overall balance on the other. Long-term capital movements are shown separately where possible. Global figures or figures for short-term capital movements include errors and omissions and non-reserve monetary items. ³ Equal to changes in official reserves and the net IMF position (see Chapter IV of Part II). ⁴ Including processing, merchanting trade and monetary gold. ⁵ Including the balance of French overseas territories vis-à-vis the non-franc area. ⁶ Imports c.i.f.

The net capital inflow (including non-reserve monetary items and errors and omissions) into European OECD countries amounted to \$2.9 milliard in 1963. As the ascertained long-term movements (net inflows for France, Germany, Denmark, Sweden, Greece and Spain and net outflows for Italy, the Netherlands and the United Kingdom) showed a net surplus, and considering that Austria, Norway and Turkey are net borrowers on long-term account, one may assume that European OECD countries as a whole were substantial net recipients of both long and short-term capital in 1963.

France. For the first time since the stabilisation measures of 1957-58 the French current-account surplus, although still substantial, was greatly reduced in 1963. Though exports went up by 15 per cent., they were out-paced by imports, which rose by 23 per cent., partly owing to exceptionally large imports of fuel. The export surplus consequently fell to \$120 million, i.e. one-quarter of the previous year's figure.

As registered by customs statistics, the deterioration in the trade account with countries outside the franc area (which alone is relevant for the balance of payments) began in mid-1962.

France: Foreign trade.

Periods	Trade with countries outside the franc area			Trade with the franc area			Total balance of trade
	Exports (f.o.b.)	Imports (c.i.f.)	Balance	Exports (f.o.b.)	Imports (c.i.f.)	Balance	
	in millions of US dollars						
1962 1st quarter	1,465	1,420	+ 45	430	375	+ 55	+ 100
2nd quarter	1,490	1,435	+ 55	335	440	— 105	— 50
3rd quarter	1,350	1,375	— 25	300	340	— 40	— 65
4th quarter	1,585	1,615	— 30	415	370	+ 45	+ 15
1963 1st quarter	1,495	1,655	— 160	395	395	+ 0	— 160
2nd quarter	1,705	1,860	— 155	405	420	— 15	— 170
3rd quarter	1,535	1,645	— 110	345	330	+ 15	— 95
4th quarter	1,810	2,040	— 230	400	390	+ 10	— 220
1964 1st quarter	1,830	2,170	— 340	420	420	+ 0	— 340

In 1963 as a whole imports from outside the franc area rose by \$1,350 million. Processed consumer goods, semi-manufactured products and fuel each accounted for about \$250 million of the increase, while investment goods, foodstuffs and raw materials contributed roughly \$150 million each. In addition to the impact of strong domestic demand imports were encouraged by policy measures. For instance, in order to curb the rise in prices, import duties on industrial products were repeatedly lowered during 1963.

In recent years additional demand for fuel has been met by supplies from the franc area, which increased from less than 2 million tons in 1959 to 14 million in 1962, while imports from outside the area have been fairly stable at around 43 million tons a year during the same period. In 1963, mostly as a result of the harsh winter and of the French miners' strike in

March, purchases from outside the franc area rose to 54 million tons. Fuel imports from the franc area increased by 13 per cent. in value. As, however, purchases of foodstuffs declined and French exports to the area rose, France's balance vis-à-vis the rest of the franc area moved back into surplus after having shown — exceptionally — a deficit in 1962.

Net receipts from services fell slightly in 1963. A drop of \$85 million in earnings from tourist trade, larger remittances by foreign workers and the disappearance of the small surplus on transportation account were partly offset by rising receipts from unilateral transfers and foreign governments. With an export surplus of \$120 million and net receipts from invisibles amounting to \$320 million, the surplus on current account totalled \$440 million in 1963, against \$830 million in the previous year.

In the public sector advance debt repayments included the repurchase of instalments worth \$119 million of the 1947 IBRD loan to the Crédit National and advance repayments to the US Export-Import Bank to the amount of

France: Balance of payments.¹

Items	1961	1962	1963
	in millions of US dollars		
France			
Merchandise trade (f.o.b.)			
Exports	5,190	5,850	6,695
Imports	4,775	5,365	6,575
Trade balance	+ 415	+ 485	+ 120
Services (net)			
Travel	+ 215	+ 200	+ 115
Foreign labour	— 125	— 150	— 190
Others	+ 445	+ 295	+ 395
Total	+ 535	+ 345	+ 320
Current balance	+ 950	+ 830	+ 440
Long-term capital			
Official: Prepayments ²	— 320	— 585	— 280
Other	— 120	— 135	— 150
Private	+ 370	+ 400	+ 500
Total	— 70	— 320	+ 70
Balance on current and long-term capital account	+ 880	+ 510	+ 510
Short-term capital	— 85	— 115	— 75
Rest of French franc area	+ 90	+ 150	+ 140
Errors and omissions	+ 30	+ 55	+ 80
Total balance (= changes in monetary items)	+ 915	+ 600	+ 655
of which changes in reserves and IMF position	+ 1,095	+ 685	+ 860

¹ On a cash basis. ² In 1962 \$469 million to the United States, \$55 million to Canada and \$60 million to the IBRD; in 1963 \$119 million to the IBRD and \$161 million to the United States.

\$161 million. The net capital outflow on official account was reduced from \$720 to 430 million.

Owing mainly to sales of foreign securities by French residents, the net inflow of private long-term capital in 1963 was \$100 million more than in 1962. While net foreign investment by French residents amounted to \$60 million in 1962, net disinvestment to a total of \$50 million took place last year. In all, the balance on long-term capital account changed from a deficit of \$320 million to a surplus of \$70 million. Private short-term capital movements, which in 1962 had resulted in a deficit of \$115 million, were in equilibrium in the first half of 1963 and in the second half showed a net deficit of \$75 million.

Excluding debt prepayments, the overall balance showed in 1963 a surplus of \$935 million, or \$250 million less than in the previous year.

Italy. The balance of payments on a transactions basis and seasonally adjusted showed its largest surplus in the last quarter of 1961, after which surpluses became gradually smaller, until at the turn of 1962-63 a deficit was recorded. In 1963 the deficits increased from quarter to quarter. The overall balance of payments on a cash basis, which was practically in equilibrium the year before, registered a deficit of \$1,245 million in 1963, this being almost entirely due to a rise of over \$1 milliard in the import surplus, although a slight fall in net invisible receipts and a larger net capital outflow contributed to the total deterioration.

Imports, which had risen very steeply in the second half of 1962, continued to do so until nearly the end of 1963. For 1963 as a whole they stood 24 per cent. above the previous year's level, the quarterly increases amounting to 18, 30, 29 and 20 per cent. respectively. In the first quarter of 1964 the rate of increase fell further to 18 per cent. The import surplus of \$680 million was thus somewhat smaller than in the preceding quarter but still \$170 million larger than in the first quarter of 1963.

On the basis of customs statistics, imports totalled \$7,540 million in 1963, \$1,470 million more than in 1962; over one-third of the increase was accounted for by larger imports of food, in particular meat, and almost a tenth by cars and parts for assembly in Italy. In absolute figures meat and cattle imports amounted to \$400 million in 1963, or two and a half times their 1962 level, and cars and parts to \$320 million, or 75 per cent. more than in the previous year. The rising demand for food imports reflects three main factors: (1) a deficiency in domestic agricultural production, (2) higher consumption standards and (3) specific policy measures taken to check rising food prices. Thus, in February 1963 additional import quotas were established for meat and butter and import duties on fresh fruit, vegetables and olive oil were suspended. The steep growth of car imports was facilitated by the lowering of tariffs within the European Economic Community and even more by the substantial enlargement of quotas for imports from other areas.

For the first time since 1956, net invisible receipts fell somewhat in 1963; they were insufficient to cover the trade gap, and the current account

Italy: Balance of payments.*

Items	1962	1963	1963				1964 1st quarter
			1st quarter	2nd quarter	3rd quarter	4th quarter	
in millions of US dollars							
Merchandise trade							
Imports (c.i.f.)	5,885	7,255	1,640	1,820	1,830	1,965	1,930
Exports (f.o.b.)	4,460	4,760	1,130	1,175	1,205	1,250	1,250
Trade balance	— 1,425	— 2,495	— 510	— 645	— 625	— 715	— 680
Services (net)							
Travel	+ 725	+ 750	+ 95	+ 190	+ 325	+ 140	+ 90
Emigrants' remittances	+ 510	+ 520	+ 100	+ 130	+ 155	+ 135	+ 100
Transport	+ 300	+ 305	+ 65	+ 80	+ 80	+ 80	+ 80
Others	+ 140	+ 30	+ 40	— 30	— 15	+ 35	— 15
Total	+ 1,675	+ 1,605	+ 300	+ 370	+ 545	+ 390	+ 255
Current balance	+ 250	— 890	— 210	— 275	— 80	— 325	— 425
Capital movements							
Repatriated bank-notes	— 765	— 1,470	— 525	— 490	— 170	— 285	— 260
Investment by non-residents	+ 845	+ 1,290	+ 475	+ 320	+ 115	+ 380	+ 250
Investment by residents	— 175	— 75	— 20	— 30	— 15	— 10	
Others	— 105	— 100	+ 15	+ 65	+ 40	— 220	
Total	— 200	— 355	— 55	— 135	— 30	— 135	— 10
Total balance (= changes in monetary items)	+ 50	— 1,245	— 265	— 410	— 110	— 460	— 435
of which changes in reserves and IMF position	+ 30	— 410	— 165	— 10	+ 130	— 365	— 460

* On a cash basis.

registered a deficit of \$890 million, against a surplus of \$250 million the year before.

The export of capital in the form of bank-notes, calculated on the basis of bank-notes repatriated and credited to non-residents' capital lira accounts, was particularly large in the first half of 1963, when it amounted to over \$1 milliard. In the second half it fell to less than \$500 million. A substantial part of the outflowing capital, however, was reinvested in Italy in the form of portfolio investment under foreign cover. The total net outflow of capital amounted to \$355 million in 1963 — against \$200 million the year before — and it brought the overall deficit to \$1,245 million. In the first quarter of 1964 the overall deficit amounted to \$435 million and the deficit on current account to \$425 million. The latter was twice as large as in the corresponding quarter of 1963, 80 per cent. of the deterioration being attributable to the worsening in the trade balance.

Germany. A considerable export surplus in the fourth quarter of 1963 more than offset the current-account deficit of the previous nine months, so that 1963, in contrast to 1962, yielded a surplus on current account. In

addition, there was a very large inflow of long-term capital and the overall balance of payments moved from deficit to surplus, with a swing of over \$700 million.

In 1963 as a whole exports rose by 10 per cent., with substantial increases in the second and fourth quarters. Of the total export rise of \$1,335 million in 1963, 70 per cent. was accounted for by EEC countries, mainly Italy and France, and over a third represented larger sales of motor-cars. At \$1,980 million, these amounted to nearly one-seventh of all exports last year. Imports rose sharply in the second quarter of 1963 and then remained almost stationary until the end of the year. In 1963 as a whole they increased by 6 per cent. Their relatively slow growth was attributable to a fall in purchases of armaments and food.

The net deficit on invisible account declined by \$65 million to \$360 million, mainly because net tourist expenditure, which had increased by leaps and bounds since 1957 and represented the largest single deficit item in recent years, fell by \$50 million in 1963.

Germany: Balance of payments.¹

Items	1962	1963	1963				1964 1st quarter
			1st quarter	2nd quarter	3rd quarter	4th quarter	
in millions of US dollars							
Merchandise trade							
Exports (f.o.b.)	13,245	14,580	3,230	3,630	3,660	4,060	3,890
Imports (c.i.f.)	12,375	13,070	3,040	3,335	3,345	3,350	3,295
Trade balance . . .	+ 870	+ 1,510	+ 190	+ 295	+ 315	+ 710	+ 595
Services (net)	— 425	— 360	— 0	— 120	— 225	— 15	— 65
Unilateral transfers . .	— 1,000	— 900	— 255	— 245	— 230	— 170	— 205
Current balance	— 555	+ 250	— 65	— 70	— 140	+ 525	+ 325
Long-term capital							
Private	+ 285	+ 795	+ 185	+ 245	+ 205	+ 160	+ 90
Official	— 245	— 260	— 25	— 70	— 50	— 115	— 50
Total	+ 40	+ 535	+ 160	+ 175	+ 155	+ 45	+ 40
Short-term capital							
Private ²	+ 105	+ 10	+ 180	— 5	+ 15	— 180	+ 170
Official ³	+ 30	— 80	+ 30	+ 65	+ 145	— 320	— 90
Total	+ 135	— 70	+ 210	+ 60	+ 160	— 500	+ 80
Balance on capital account	+ 175	+ 465	+ 370	+ 235	+ 315	— 455	+ 120
Errors and omissions . . .	+ 160	— 210	+ 60	+ 60	+ 45	— 375	+ 205
Total balance (= changes in monetary items) . .	— 220	+ 505	+ 365	+ 225	+ 220	— 305	+ 650
of which changes in reserves and IMF position	— 220	+ 720	+ 445	+ 250	— 230	+ 255	+ 100

¹ On a transactions basis.
transactions with the IMF.

² Excludes changes in the net foreign position of the commercial banks.

³ Excludes

Government receipts on account of foreign troops stationed in Germany amounted to \$1,070 million, the same as in 1962. For some years, in order to alleviate the balance-of-payments burden of these contributions on other NATO countries, Germany has been placing armaments orders in these countries and has made advance payments for them. In 1963, for the first time, payments for armaments (which come under current items) together with advance payments (which figure in the capital account) exceeded the government's receipts in respect of foreign troops.

In 1960-62 Germany recorded a net inflow of private long-term capital of between \$200 and 300 million a year. In 1963 the total soared to \$800 million, of which three-quarters represented security transactions. Net purchases of German securities by foreigners rose from \$380 million in 1962 to \$715 million last year, while the share of bonds in the total increased from under 50 to 70 per cent. It is estimated that non-residents hold some \$1.5 milliard of German bonds. The growing foreign demand for them seems to have reflected not only the interest rate differential but also political and fiscal considerations.

On short-term capital account (excluding transactions with the IMF and those of the banking system) a net outflow of \$70 million was recorded in 1963. From the second quarter of 1962 onwards the net balance on official short-term capital account began to show a surplus. This is explained mainly by the fact that payments for armaments were smaller than actual imports. (In terms of capital movements this corresponds to the amortisation of credits previously granted by Germany.) Thus, in the first three quarters of 1963 there was a net inflow on official short-term capital account amounting to \$240 million. In the last quarter the situation was reversed. Defence payments were made on a large scale, particularly in December, and far exceeded imports of armaments.

In the first quarter of 1964, owing to a considerable rise in exports, the surplus on trade account amounted to nearly \$600 million, more than three times as much as in the corresponding quarter of 1963. The balance on current account consequently shifted from a deficit of \$65 million to a surplus of \$325 million.

This large surplus may be reduced in future if the tariff reductions announced on 13th May as part of the stabilisation programme help to raise imports. In relation to EEC countries all duties below 4 per cent. are expected to be brought down to zero on 1st July 1964, and it is planned to put the 10 per cent. reductions on industrial products which were due to take place on 1st January 1965 and 1966 into effect at the same time. In relation to non-EEC countries, Germany intends to lower duties on some 300 items to the level of the future common external tariff of the EEC.

Netherlands. An increase in receipts from invisible items and a contraction in the trade deficit combined to raise the surplus on current account (on a cash basis) from \$75 million in 1962 to \$270 million last year. If, however,

the balance on a transactions basis is considered, there is found to have been a deterioration of some \$40 million. The spread of \$230 million between the two types of balance is mainly accounted for by the fact that the sharp rise of imports towards the end of the year brought with it an increase in import credits.

Netherlands: Balance of payments.¹

Items	1962	1963	1963			
			1st quarter	2nd quarter	3rd quarter	4th quarter
			in millions of US dollars			
Merchandise trade (f.o.b.)						
Imports	4,795	5,210	1,170	1,270	1,305	1,465
Exports	4,380	4,850	1,110	1,185	1,210	1,345
Trade balance	— 415	— 360	— 60	— 85	— 95	— 120
Services (net)						
Investment income	+ 100	+ 175	+ 60	— 45	+ 65	+ 95
Others ²	+ 390	+ 455	+ 70	+ 110	+ 150	+ 125
Total	+ 490	+ 630	+ 130	+ 65	+ 215	+ 220
Current balance	+ 75	+ 270	+ 70	— 20	+ 120	+ 100
Capital movements						
Official ³	— 70	— 100	— 5	— 10	— 75	— 10
Private						
Long-term	— 10	— 15	— 10	+ 65	— 5	— 65
Short-term ⁴	— 30	— 15	— 45	— 25	+ 40	+ 15
Total	— 110	— 130	— 60	+ 30	— 40	— 60
Total balance (= changes in monetary items)	— 35	+ 140	+ 10	+ 10	+ 80	+ 40
of which changes in reserves and IMF position	— 15	+ 170	+ 10	+ 70	+ 20	+ 70

¹ On a cash basis. ² Including unilateral transfers. ³ Of which prepayments amounting to \$30 million in 1962 and \$70 million in 1963. ⁴ Including banks.

In 1963 on a cash basis imports expanded by 9 and exports by 11 per cent. — about twice the rate of increase in the previous year — so that the import surplus for the year as a whole was reduced by \$55 million. In the course of the year, however, the import surplus rose steadily and in the fourth quarter it reached \$120 million. Net invisible receipts went up by \$140 million in 1963 as a result of rises of \$75 million in investment income and \$65 million in revenue from other services. Nearly all of the increase took place in the second half of the year.

The net outflow of long-term capital expanded from \$80 million in 1962 to \$115 million last year on account of a rise in advance public-debt repayments from \$30 to 70 million, the latter representing a single payment to the United States in July.

As regards private capital movements, the long-term account was practically in equilibrium in 1962 and 1963. In both years the net outflow of Dutch capital and the net inflow of foreign capital each totalled some \$300 million. In 1963, however, direct investment on both sides went up while port-

folio investment declined. This fall reflected the absence of any major foreign issues on the Dutch market or of Dutch issues abroad. There was some growth in stock exchange transactions with Switzerland, which became the chief buyer of Dutch securities in 1963, while US purchases declined sharply following the announcement of the interest equalisation tax. Although the banks' net capital exports (excluding their foreign exchange operations) rose from \$15 to 40 million, the net total outflow of short-term capital decreased from \$30 to 15 million.

Belgium. The current account of the balance of payments, which in recent years had always shown a surplus, moved into deficit in 1963. The deterioration of \$180 million was due entirely to a dwindling of the surplus on invisible items, which fell from \$210 million in 1962 to practically nil last year. Judging from the results for the first nine months, this was ascribable for the most part to an increase in government expenditure and a fall in investment income. But net receipts from merchanting and processing also declined and government transfers were larger than in 1962, mainly because of a payment in the first quarter to the EEC Development Fund.

The \$100 million deficit on current account was practically offset by a net inflow of capital. The Treasury was obliged to borrow heavily abroad last year and to some extent this was reflected in the net inflow of official capital, which amounted to \$50 million — against a net outflow of \$65 million in 1962. Private capital, together with errors and omissions, accounted for another \$50 million. The rise of \$225 million in official reserves, as indicated in the table on page 82, was entirely attributable to an increase in the commercial banks' foreign liabilities.

United Kingdom. Three main points emerge from the UK balance-of-payments statistics for 1963. On current account the surplus was a little larger than in 1962 and (after adjustment for seasonal factors) was mainly concentrated in the first half of the year; the export of long-term capital, after a two-year break, returned to the level of the late 1950s; and there was a reversal of the balance on unrecorded transactions. The first two points partly offset each other, so that the identified current and long-term capital account was only in moderate deficit for the year as a whole. The adverse movement of \$435 million in the monetary items, therefore, was largely the result of a shift from plus to minus in the "balancing item".

Though the trade deficit was rather smaller in 1963 than 1962, there was a steady worsening throughout the year. This was mainly because imports grew faster than exports after the first quarter, with larger purchases of industrial materials at rising prices. On a seasonally adjusted basis the change in the balance of trade between the first and second halves of the year was not as great as the unadjusted figures in the next table would indicate, the deterioration being from a surplus of over \$40 million in the first half (the best result since 1958) to a deficit of \$165 million in the second half of the year.

United Kingdom: Balance of payments.*

Items	1961	1962	1963	1963	
				1st half	2nd half
	in millions of US dollars				
Merchandise trade (f.o.b.)					
Imports	11,235	11,365	12,090	5,885	6,205
Exports and re-exports	10,870	11,175	11,970	5,985	5,985
Trade balance.	— 365	— 190	— 120	+ 100	— 220
Services (net)	+ 335	+ 475	+ 460	+ 310	+ 150
Current balance	— 30	+ 285	+ 340	+ 410	— 70
Long-term capital					
Official	— 125	— 295	— 295	— 55	— 240
UK private	— 915	— 725	— 925	— 480	— 445
Foreign private	+ 1,165	+ 770	+ 805	+ 405	+ 400
Total	+ 125	— 250	— 415	— 130	— 285
Balance on identified current and long-term capital account	+ 95	+ 35	— 75	+ 280	— 355
Errors and omissions	— 40	+ 240	— 360	— 140	— 220
Total balance (= changes in monetary items)	+ 55	+ 275	— 435	+ 140	— 575

* On a transactions basis.

Customs figures show that exports rose by 8 per cent. in 1963 to \$11,425 million; the increase in volume was 5 per cent. and the rest was the result of higher prices. The levelling-off of the upward trend is shown by the fact that the fourth-quarter figures on an adjusted basis were 1 per cent. above the third quarter but 10 per cent. better than the fourth quarter of 1962. Much the same applies to exports of manufactured goods, which account for 85 per cent. of total exports. Looked at according to their principal destinations, sales to Europe and the sterling area rose in the first three quarters of the year and fell off slightly in the final quarter; sales to North America, though still rising in the fourth quarter, were doing so more slowly than earlier.

Imports, at \$13,500 million c.i.f., were 7 per cent. up on 1962. The rise in the world sugar price caused purchases of raw sugar, as measured in the trade accounts, to go up by \$285 million in value. As, however, imports of sugar were paid for at fixed prices which were generally higher than world prices in 1962 and lower in 1963, this increase greatly overstates the extra balance-of-payments costs of sugar in 1963. Other food imports taken together were a little lower because purchases of cereals and feeding stuffs for animals fell away. Imports of industrial materials began to increase in the second quarter and rose by 7 per cent. in both the third and fourth quarters. The largest increases were in chemicals, iron and steel, wool and timber. For the year as a whole the increase in this category was \$395 million. Imports of finished manufactures went up by \$120 million and fuel imports by \$85 million.

The balance on invisible account was practically the same in 1963 as in 1962. Government spending abroad and net travel expenditure were both a

little higher, and so was net investment income. The changes in the latter item were biggest on the payments side. Foreign earnings from direct and portfolio investment went up by \$100 million, while "other" investment income debits fell from \$615 to 485 million. This largely reflected lower rates of interest on sterling balances.

On long-term capital account the main feature of 1963 was the increase in private outflows from the United Kingdom. Direct outward investment rose by about \$60 million — as did also direct foreign investment in the United Kingdom — and other types of investment more than doubled to \$270 million.

Taken together, the current and long-term capital accounts showed a deficit of \$75 million for 1963 as a whole and \$355 million for the second half of the year. The balancing item was conspicuously negative, to the tune of \$360 million for the year as a whole, after having been substantially positive in 1962. While there may have been some unidentified outflow of funds, the movement of sterling balances held outside the sterling area — a decline of about \$100 million — does not suggest that this factor could account for a very large part of the turn-round of the balancing item. Rising exports will have led to an increase in export credits, and the terms may have been lengthened. Moreover, since exports are entered in the balance of payments at the date of shipment, recorded exports, in a period of export expansion, will tend to run ahead of export receipts. This, too, will have as its counterpart a negative entry in the balancing item.

The customs figures for the first four months of 1964 show, on a seasonally adjusted basis, a slight increase in exports over the previous four months. Imports c.i.f. were up by $7\frac{1}{2}$ per cent. and the trade deficit increased by over \$300 million. However, manufacturers' export order-books are fuller now than a year ago and stock-building may already have reached its peak. Thus, for the rest of the year exports may expand as fast as imports. Nevertheless, with long-term capital outflows, in particular the oil industry's investments, also expected to rise further, the prospects are for a substantial deficit on current and long-term capital account. The behaviour of the balancing item will, therefore, be of more than usual importance in 1964.

Scandinavian countries. The three Scandinavian countries taken together had a current-account deficit of nearly \$200 million in 1963, against one of \$400 million the previous year.

From 1960 to 1962 Denmark's deficit on current account had risen from \$50 to 190 million, as exports expanded only about half as fast as imports. From the fourth quarter of 1962 onwards, however, the trend was reversed, and exports rose vigorously while imports, under the influence of anti-inflationary measures (see pages 8-9), tended to level out. In 1963 exports went up by 14 per cent. as a result of an 11 per cent. rise in sales of farm products and one of 19 per cent. in exports of industrial goods, the balance

on current account showing a surplus of \$50 million. The net inflow of foreign capital went up from \$100 to 190 million, chiefly as a result of larger net borrowing by the public sector.

Norway increased its reserves by \$50 million in 1963, entirely owing to the fact that its foreign indebtedness rose more than its current-account deficit. The deficit in the trade balance went up by \$60 million, mostly, however, as a result of a net rise in imports of ships bearing little relation to fluctuations in domestic demand. An increase of \$45 million in freights, following a rise in rates, swelled net receipts from invisible items. However, this was not sufficient to cover the larger import surplus and the mounting interest burden on the foreign debt, so that the current deficit rose from \$175 to 195 million. The net capital inflow, at \$245 million last year, was one and a half times as large as in 1962, owing mainly to a rise of some \$80 million in net borrowing to finance shipbuilding and ship imports, the shipping industry being engaged in a programme of replacement of the present fleet by larger units, though its average age is only seven and a half years. Borrowing by the government and local authorities was \$45 million higher than in 1962. It included the issue of loans in Sweden, Switzerland and the United States.

The recorded items in the Swedish balance of payments showed little change in 1963. As exports rose by 9.5 and imports by 8.5 per cent., there was a small decline in the trade deficit to \$185 million — one of the lowest figures in recent years. Net income from shipping remained stable at \$280 million, but net expenditure on other invisibles rose somewhat, mainly as a result of higher net tourist expenditure abroad. The current deficit consequently increased from \$30 to 40 million. Capital transactions are of only minor importance in the Swedish balance of payments. The errors and omissions item, however, is generally positive and shows wide fluctuations. Together, capital movements and unrecorded transactions yielded only \$20 million last year, compared with \$110 million in 1962, this shrinkage probably being connected with changes in trade credit.

Switzerland. In 1963, for the third year in succession, Switzerland ran a larger deficit on current account while at the same time, owing to a substantial influx of capital, it added to its reserves. The accumulated current deficit over these three years amounted to \$930 million and the increase in reserves to \$750 million.

The current deficit went up from \$340 million in 1962 to an estimated \$380 million last year. With an increase of 8 per cent., imports rose more slowly than in 1962, whereas exports expanded by a further 9 per cent. The import surplus amounted to \$820 million. Net receipts from invisible items, at \$440 million, were slightly below their 1962 level, whereas they had risen in most previous years. Remittances from the growing body of foreign workers, which came to close on \$300 million in 1962, are likely to have been bigger still last year.

The net inflow of capital, calculated as the difference between the rise in reserves and the current deficit, amounted to \$580 million in 1963, compared with \$455 million in the previous year.

In the first quarter of 1964 there was a reversal in short-term capital movements in connection with the end-year operations of the banks. The trade balance in the first quarter of 1964, compared with that in the corresponding period of 1963, deteriorated by \$75 million, since imports were 17 per cent. higher while exports rose by 9 per cent.

United States. US balance-of-payments developments in 1963 were dominated by the capital account. In the first half of the year the seasonally adjusted overall deficit, excluding special transactions, was \$2.3 milliard — and the identified outflow of private US capital amounted to no less than \$2.7 milliard. After the measures taken in July (see page 20), the overall deficit before special transactions declined to \$1 milliard in the second half of the year, the outflow of US capital falling correspondingly to \$1.4 milliard. In the first quarter of 1964 the deficit was only \$135 million.

In 1963 exports increased by \$1,400 million, of which \$1 milliard was in respect of commercial exports and \$400 million in respect of government-financed exports. As imports rose by \$800 million, the commercial balance of trade improved by \$200 million. This improvement occurred entirely in the fourth quarter of the year (on a seasonally adjusted basis), when the export surplus amounted to \$790 million, against \$290 million in the corresponding period of 1962 and \$405 million in the first quarter of 1963. It should be noted that exports to the rest of the industrialised world were rising very fast last year while US imports went up just about in line with domestic activity.

Agricultural exports increased by \$560 million, poor weather conditions in large parts of Europe and Asia having helped to raise demand for cereals in these areas. Altogether, it may be estimated that 20–25 per cent. of the rise in US agricultural exports was due to temporary conditions, while a further 25 per cent. of the increase was in government-financed exports. Sales of non-agricultural materials and of finished manufactures rose in response to the acceleration of business activity in Europe, Japan and Canada. Total US exports to Europe went up by \$500 million, those to Japan by \$300 million and those to Canada by \$200 million.

Imports rose in the second and third quarters of 1963 and levelled out thereafter. The increase of \$800 million for the year as a whole derived chiefly from larger purchases of manufactured goods — motor-cars and capital equipment together accounted for 40 per cent. of the rise.

Net investment income, which had risen by about \$500 million in 1961 and 1962, increased by only \$40 million last year. Income from private investments, which represents 90 per cent. of the total, went up from \$3,850 million in 1962 to \$4,065 million in 1963, while payments increased

United States: Balance of payments¹.

Items	1962	1963	1963				1964 1st quarter
			1st quarter	2nd quarter	3rd quarter	4th quarter	
			seasonally adjusted, in millions of dollars				
Commercial transactions							
Exports (f.o.b.)	18,135	19,170	4,420	4,665	4,920	5,165	5,345
Imports (f.o.b.)	16,145	16,960	4,015	4,180	4,390	4,375	4,340
Trade balance	+ 1,990	+ 2,210	+ 405	+ 485	+ 530	+ 790	+ 1,005
Investment income (net) ²	+ 3,325	+ 3,370	+ 905	+ 805	+ 810	+ 850	n.a.
Services and remittances ³	- 1,205	- 1,390	- 360	- 360	- 330	- 340	n.a.
Balance of trade and services .	+ 4,110	+ 4,190	+ 950	+ 930	+ 1,010	+ 1,300	n.a.
Government transactions							
Exports	+ 2,345	+ 2,735	+ 590	+ 830	+ 640	+ 675	+ 730
Military expenditure less receipts .	- 2,370	- 2,250	- 570	- 520	- 615	- 545	n.a.
Grants and loans	- 3,515	- 3,790	- 870	- 1,200	- 785	- 935	n.a.
Total	- 3,540	- 3,305	- 850	- 890	- 760	- 805	n.a.
Private capital movements	- 3,120	- 3,690	- 955	- 1,465	- 340	- 930	n.a.
Errors and omissions	- 1,025	- 495	- 135	+ 120	- 385	- 95	n.a.
Balance on regular transactions	- 3,575	- 3,300	- 990	- 1,305	- 475	- 530	- 135
Seasonal adjustment item	-	-	+ 180	+ 95	- 365	+ 90	+ 245
Special government transactions ⁴	+ 1,385	+ 1,340	+ 455	+ 170	+ 425	+ 290	+ 95
Total balance on regular and special transactions ⁵	- 2,190	- 1,960	- 355	- 1,040	- 415	- 150	+ 205

¹ On a transactions basis. ² Including income from government loans. ³ Including government pensions.
⁴ Including sales of non-marketable medium-term convertible and non-convertible securities. ⁵ Corresponding to increase (—) in liquid liabilities and decrease (—) in gold and foreign currencies.

from \$655 to 795 million, reflecting the rise in interest rates on time deposits and government securities which took place in July 1963. Partial data seem to indicate that profits from the petroleum and mining industries grew at a steady rate but that those from manufacturing industries — which have received the most new capital in recent years — ceased to expand and may have diminished.

The improvement in the balance of commercial trade and investment income was partly cancelled out by a rise in net expenditure on services, so that the balance of trade and services was only \$80 million larger than in 1962.

The outflow of funds from regular government transactions declined by \$235 million in 1963. Government-financed exports rose substantially more than the total of government grants and loans, and there was a slight fall in net military expenditure.

The rise in the net export of US private capital had begun during the latter half of 1962. Between the third and fourth quarters of that year the outflow went up from \$0.5 to 1.1 milliard and there was a further sharp

United States: Private capital movements.

Items	1962	1963	1963			
			1st quarter	2nd quarter	3rd quarter	4th quarter
	seasonally adjusted, in millions of dollars					
US capital						
Long-term						
Direct investment	-1,555	-1,800	- 500	- 500	- 155	- 645
New issues of foreign securities	-1,075	-1,295	- 505	- 520	- 185	- 85
Redemptions	+ 170	+ 150	+ 30	+ 50	+ 25	+ 45
Transactions in outstanding foreign securities	- 55	+ 45	- 50	- 60	+ 55	+ 100
Other	- 250	- 540	- 10	- 125	- 120	- 285
Total	-2,765	-3,440	-1,035	-1,155	- 380	- 870
Short-term	- 510	- 640	+ 60	- 530	+ 130	- 300
Total US capital outflow . . .	-3,275	-4,080	- 975	-1,685	- 250	-1,170
Foreign capital						
Long-term	+ 270	+ 385	- 10	+ 205	+ 110	+ 80
Short-term	- 115	+ 5	- 20	+ 65	+ 25	- 65
Total foreign capital inflow . .	+ 155	+ 390	- 30	+ 270	+ 135	+ 15
Total private capital outflow .	-3,120	-3,690	-1,005	-1,415	- 115	-1,155

rise to \$1.7 milliard in the second quarter of 1963. For the first half of the year the total outflow was at an annual rate of \$5.3 milliard.

While US direct investment abroad and short-term lending had both contributed to the rise, it was portfolio investment that was singled out for special attention. About \$1 milliard out of a total US private capital outflow of \$2.7 milliard during the first half of 1963 was due to new issues of foreign securities in New York — Canada accounting for 60, western Europe for 20 and Japan for 10 per cent.

During the period October 1962 to June 1963 net new Canadian issues in the United States had averaged \$350 million per quarter. The two biggest issues were for \$250 million by the Canadian Government, to reinforce Canada's official exchange reserves, and for \$300 million by the Quebec Hydro-Electric Commission, though transfers of the latter were spread over fifteen months beginning in the first quarter of 1963.

The temporary interest equalisation tax proposed to Congress on 18th July 1963, and not yet enacted, is to be calculated so as to increase portfolio borrowing costs in the United States by about 1 per cent. It is anticipated that the tax will be levied only until the end of 1965 and will not apply to developing countries or to international organisations to which the United States belongs. It is also envisaged that new Canadian issues will be exempt from the tax.

Following the President's proposals, net new issues of foreign securities fell to \$200 million in the second half of 1963. Transactions in outstanding

securities (to which the tax would equally apply) shifted from net US purchases of \$110 million in the first half to net sales of \$155 million in the second half of the year. The latter change probably also reflected the growing attraction of the US stock market. In all, therefore, US portfolio investment abroad during July–December 1963 came to only \$45 million.

Direct investment, which had amounted to \$500 million in both the first and the second quarters of 1963, contracted sharply in the third but rose again steeply in the fourth quarter. The overall increase in 1963 tallied with the plant and equipment expenditure plans reported early in the year by the US parent companies. It therefore seems unlikely that a shift from portfolio to direct investment has been taking place.

Bank credits to non-residents amounted to \$1,280 million in 1963, roughly \$900 million more than in the previous year. About \$580 million represented medium-term loans. The rise began in the second quarter (before the interest equalisation tax was proposed) but accelerated during the latter half of the year. It is estimated that total bank lending to foreigners rose from \$500 to 780 million between the first and second halves of 1963. It may be, therefore, that some foreign borrowing was shifted in this period from the capital market to the banks. Furthermore, the adverse change of some \$500 million in the balance of unidentified transactions between the second and third quarters of the year may also be connected with the virtual cessation of foreign issues in New York.

Rather more than half of the increase in bank foreign lending was offset by reduced lending on the part of non-financial concerns. In all, the net outflow of both long and short-term US private capital amounted to over \$4 milliard in 1963 and was \$800 million larger than in the previous year.

The net inflow of foreign capital into the United States for investment other than in liquid assets was close on \$400 million in 1963, against \$150 million a year earlier, and was mainly a consequence of the rising trend on the US stock market.

The total US balance-of-payments deficit on regular transactions in 1963 was only \$275 million smaller than in 1962. As special government transactions, including sales of non-marketable convertible securities, were nearly as large as in 1962, the deficit remaining to be financed by drawing on reserve assets and adding to ordinary liquid liabilities was roughly \$200 million less than in 1962.

In the first quarter of 1964 regular transactions, on a seasonally adjusted basis, yielded a small deficit of \$135 million. Partly because of cereal shipments to the USSR, merchandise exports rose by about \$180 million. Security transactions again yielded a small surplus and bank credit to foreigners, at \$700 million, was also the same as in the preceding quarter. There were improvements on other items amounting in all to about \$200 million. Partly these resulted from temporary capital inflows that were reversed in April.

Canada. Owing to the rapid growth of exports in 1963, the current deficit contracted from \$780 million in 1962 to \$480 million last year. Since at the same time the net capital inflow fell by \$310 million, an overall surplus of some \$140 million was achieved in both years.

Exports, as adjusted for balance-of-payments purposes, expanded by \$650 million, or 11 per cent., of which some \$200 million represented sales of wheat to the USSR and certain eastern European countries. Larger exports of manufactured products, as well as gains in those of primary products, accounted for the remaining \$450 million.

Imports went up by \$345 million. They rose less than in former periods of economic expansion, as there has been a marked shift towards replacing imports by Canadian products, favoured by the Canadian devaluation and by policy measures, such as the import surcharges, which were still in force in the early months of 1963.

The net long-term capital inflow, which had dried up in the first half of 1962, resumed in mid-year after the implementation of the stabilisation programme. It amounted to \$645 million in the second half of 1962 and to \$530 million in the first half of 1963. The announcement of tax measures in

Canada: Balance of payments.

Items	1962	1963	1963			
			1st quarter	2nd quarter	3rd quarter	4th quarter
			in millions of US dollars			
Merchandise trade (f.o.b.)						
Exports	5,885	6,535	1,370	1,640	1,665	1,860
Imports	5,740	6,085	1,305	1,575	1,530	1,675
Trade balance.	+ 145	+ 450	+ 65	+ 65	+ 135	+ 185
Services						
Interest and dividends	- 525	- 570	- 145	- 125	- 125	- 175
Travel	- 45	+ 15	- 60	- 25	+ 105	- 5
Others	- 355	- 375	- 80	- 90	- 100	- 105
Total	- 925	- 930	- 285	- 240	- 120	- 285
Current balance	- 780	- 480	- 220	- 175	+ 15	- 100
Long-term capital account						
New issues of Canadian securities	+ 665	+ 890	+ 380	+ 360	+ 100	+ 50
Other security transactions	- 410	- 405	- 80	- 155	- 65	- 105
Direct investment	+ 395	+ 120	+ 45	+ 15	+ 30	+ 30
Other	- 30	- 65	± 0	- 35	- 35	+ 5
Total	+ 620	+ 540	+ 345	+ 185	+ 30	- 20
Balance on current and long-term capital account	- 160	+ 60	+ 125	+ 10	+ 45	- 120
Short-term capital account	+ 305	+ 75	- 65	+ 90	- 100	+ 150
Total balance (= changes in monetary items)	+ 145	+ 135	+ 60	+ 100	- 55	+ 30

the United States in July 1963 practically stopped the inflow of funds, in particular those in respect of security transactions.

On short-term account the net inflow of \$305 million in 1962 was reduced to \$75 million last year, reflecting, among other factors, a narrowing of the differential in favour of Canada in Treasury bill yields.

Japan. Over the last three years the balance of payments has shown violent swings, having turned from a very large deficit on current account in 1961 to a small surplus in 1962 and back again to a substantial deficit last year.

Japan: Balance of payments.

Items	1962	1963
	in millions of US dollars	
Merchandise trade (f.o.b.)		
Imports	4,545	5,565
Exports	4,785	5,360
Trade balance	+ 240	— 205
Services		
Transportation	— 215	— 240
Fees, royalties, capital income	— 230	— 290
Others	— 125	— 180
Total	— 570	— 710
Foreign military expenditure	+ 365	+ 345
Current balance	+ 35	— 570
Long-term capital account	+ 260	+ 470
Balance on current and long-term capital account	+ 295	— 100
Short-term capital account	+ 170	+ 185
Errors and omissions	— 110	— 45
Total balance (= changes in monetary items)	+ 355	+ 40

From the beginning of 1963, as the economy entered a new phase of faster expansion, imports increased by over \$1 milliard, or 22 per cent., reflecting chiefly larger purchases of raw materials. The growth rate of exports, which had amounted to 20 per cent. in 1962, slowed down to 12 per cent., corresponding to an increase of \$575 million. The balance of trade consequently switched from a surplus of \$240 million to a deficit of approximately the same size.

The balance on services is structurally in deficit on account of all main items, and it shows a long-term trend of increasing deficits. Foreign military expenditure in Japan, on the other hand, is tending to diminish, so that the invisible gap is widening. Last year it nearly doubled.

Net long-term borrowing increased substantially in 1963, when it amounted to \$470 million. It continued to increase in the early months of 1964, with the issues of a DM 100 million loan on the German market and a Sw.fr. 50 million loan on the Swiss market.

Commercial policy.

Tariff barriers inside the European Economic Community were cut by a further 10 per cent. on 1st July 1963, bringing tariffs for industrial goods down to 40 per cent. of their initial level. At the same time the second step towards the establishment of the common external tariff was taken. According to the programme of action formulated by the Commission in October 1962, customs duties between the Six should be abolished completely by the end of 1966, at which time the common external tariff should also come into force. As part of its common agricultural policy, the Council of Ministers adopted in December 1963 joint marketing rules for dairy produce, beef and rice.

As regards the Community's relations with the outside world, a five-year convention of association was signed in July 1963 with eighteen African states, which provides for financial assistance amounting to \$730 million. The convention came into effect on 1st June 1964. In September 1963 the Community signed a treaty of association with Turkey, akin to the agreement previously concluded with Greece.

Tariff reductions among EFTA countries continued to keep in line with those within the EEC. In May 1963 the EFTA Council of Ministers decided that all duties should be eliminated by the end of 1966, and on 31st December 1963 a 10 per cent. reduction brought tariffs down to 40 per cent. of their initial level.

Within the framework of the General Agreement on Tariffs and Trade (GATT), which is at present adhered to by sixty-two contracting parties and to which six countries have acceded provisionally, negotiations started in Geneva on 4th May 1964. These aim at a 50 per cent. linear tariff reduction on industrial products, at reducing non-tariff barriers to trade and at facilitating trade in agricultural products.

The United Nations Conference on Trade and Development, which opened in Geneva on 23rd March 1964 and in which some 120 countries are participating, is chiefly concerned with finding ways and means of helping the developing countries to speed up their economic growth.

IV. GOLD, RESERVES AND FOREIGN EXCHANGE.

Since the end of 1962 there have been substantial further additions to official gold reserves and to official and private holdings of foreign exchange. Mainly because of larger supplies, official gold reserves rose by \$0.8 milliard during 1963 to a total of \$42.3 milliard — and the rise has continued into 1964. Countries' holdings of short-term dollars and sterling went up by \$1.4 and 0.7 to 21.3 and 11.3 milliard respectively at the end of the year. There was also an increase during 1963 of \$0.7 milliard in special, quasi-liquid US government obligations held by foreign countries.

Balance-of-payments developments in 1963 and early 1964 have brought about considerable changes in the pattern of official reserve movements. In the United States all components of the reserve position have benefited from the shrinking of the payments deficit. The decline in the US gold stock has slowed down and the loss for the seven months to March 1964 was only \$83 million; during the same seven months US official holdings of convertible currencies went up by \$348 million, while short-term liabilities to foreigners reported by US banks have shown little further rise since the third quarter of 1963.

The developing countries have improved their reserve position considerably since the end of 1962. In particular, short-term dollar balances of Latin America and Asia (excluding Japan) rose by just on \$1 milliard in 1963.

Europe's monetary reserves increased by a further \$2 milliard in 1963 and then declined by \$0.6 milliard in the first three months of 1964. Both movements were associated with opposite changes of the same general order of magnitude in the foreign positions of European commercial banks. The same sort of thing had occurred in 1962, but in that year Europe had also improved its net IMF position by \$850 million.

Under the influence of larger supplies of metal and of the gold pool's operations, gold prices have fluctuated no more than 3 or 4 US cents on either side of \$35.08 per fine ounce. There have been no major disturbances in the foreign exchange markets during the period under review. The Deutsche Mark has strengthened considerably while the lira and, to a lesser extent, the pound sterling have eased.

There was little net borrowing from the IMF during 1963, but in the first five months of 1964 Italy drew \$225 million and the United States twice \$125 million. The purpose of the latter operations was to provide other Fund members with a means of repaying earlier drawings that would avoid strain, direct or indirect, on the US gold stock. In April 1964 Japan accepted the obligations of Article VIII of the Fund's Articles of Agreement and the yen was made convertible in current transactions with other countries.

Gold production and markets.

In this field there have been two notable features since the end of 1962: a better balance between the supply of and the demand for gold, taking the period as a whole, and very stable prices on the gold bullion market despite wide fluctuations in gold supplies.

The clearest indication of this better balance is that during 1963 monetary authorities were able to add an estimated \$845 million to their published gold reserves — the highest figure for any year since the war and some \$500 million more than they bought in 1962. This change in the situation had two causes. The main one was the 25 per cent. increase, mostly from the USSR, in fresh gold supplies, to a total of \$1.9 milliard; in addition, there was some falling-away of private demand from the very high levels of 1962. Roughly 55 per cent. of new production and Russian sales was required to meet private demand in 1963; the year before, when supplies totalled \$1.5 milliard, it had been over 75 per cent. On the other hand, the 1963 situation was, from this point of view, less satisfactory than that of, say, 1959, when private demand absorbed a little more than 45 per cent. of total fresh supplies estimated at \$1.4 milliard.

The amount of gold coming onto the market fluctuated very considerably from about \$300 million in the second quarter of 1963 to more than double that amount in the final quarter of the year. This was largely a matter of the size and pattern of Russian sales. Despite it, the range of fluctuation of the London market "fixing" price since the end of 1962 has been no more than 3 or 4 US cents on either side of \$35.08 — the greatest degree of

World gold production.

Countries	1929	1940	1946	1953	1960	1961	1962	1963
weight in thousands of fine ounces								
South Africa	10,412	14,046	11,927	11,941	21,383	22,942	25,492	27,432
Canada	1,928	5,333	2,849	4,056	4,629	4,474	4,158	3,972
United States	2,059	4,870	1,575	1,958	1,667	1,548	1,535	1,440
Australia	427	1,644	824	1,075	1,087	1,076	1,073	1,020
Ghana	208	886	586	731	893	834	888	921
Southern Rhodesia	561	826	545	501	563	570	555	566
Japan	335	867	40	258	336	379	421	433
Philippines	163	1,121	1	481	411	424	423	377
Colombia	137	632	437	437	434	401	397	326
Mexico	655	883	421	483	300	269	234	237
Total listed	16,885	31,108	19,205	21,921	31,703	32,917	35,176	36,724
Other countries ¹	1,715	5,892	2,495	2,179	1,897	1,783	1,724	1,876
Estimated world total ¹ .	18,600	37,000	21,700	24,100	33,600	34,700	36,900	38,600
in millions of US dollars								
Value of estimated world total at \$35 per fine ounce	650 ²	1,295	760	845	1,175	1,215	1,290	1,350

¹ Excluding the USSR, eastern Europe, mainland China and North Korea. ² At the official price of \$20.67 per fine ounce then in effect, \$382 million.

stability experienced since the market reopened in March 1954 and one that resulted from the operations of the gold pool. This stability in the spot market, together with the forward gold operations of the Bank for International Settlements, has undoubtedly provided favourable conditions for marketing the very considerable quantities of metal that have come on offer since August 1963.

World gold production (excluding that of the USSR, eastern Europe, mainland China and North Korea) continued to rise during 1963 and is estimated to have amounted for the year as a whole to 38.6 million ounces, worth \$1,350 million at the official dollar parity. The increase over 1962 was 1.7 million ounces; this was rather less than the rise in South African output, as other countries' production again declined a little.

1963 was another good year for South Africa's gold-mines, whose output rose by a further $7\frac{1}{2}$ per cent. to 27.4 million ounces — worth nearly \$1 milliard. There was a further drop of 11,000, to 381,000, in the average native labour force employed by the industry and the quantity of ore milled was $3\frac{1}{2}$ per cent. greater than in 1962, so that the yield of gold per ton milled went up by $4\frac{1}{2}$ per cent., from \$11½ to \$12. With average costs only 3 per cent. higher, the industry's profits before tax were nearly 6 per cent. more than in 1962.

Output from the mines on the old Witwatersrand declined again in 1963, to 24 per cent. of the total compared with 83 per cent. in 1952. The South African budget for 1964-65 contained proposals designed to lengthen the lives of marginal mines. Such mines will be granted government loans to cover working losses of up to 10 per cent. of revenue and to meet approved capital expenditure. In addition, the government is continuing to assist certain mines which were threatened with premature closure because of the heavy cost of pumping out water flowing into them from adjoining mines which have already closed down. As well as helping marginal mines in these ways, the government granted the industry other tax reliefs in 1963 designed to encourage exploration for new mines and the development of deep-level mining.

While the rise in the total amount of gold newly mined was of the same order of magnitude as in other recent years, the volume of Russian sales was far higher. Offerings were concentrated in the last four months of the year, when the USSR required to finance large imports of wheat, and it may be estimated that for 1963 as a whole they were worth some \$550 million. After an interval of three months, heavy Russian selling was resumed in mid-March 1964 and by the end of April sales had already comfortably exceeded the annual average of the years 1959-62.

Concurrently with this sharp rise in gold supplies, there was some decline in private demand for the metal to a level of about \$1 milliard. It is a safe assumption that industrial use of gold has continued to expand. The decline in what may be called the hoarding demand between 1962 and 1963 therefore looks to have been rather greater than the estimated drop of \$100 million in total non-monetary demand.

Estimated sources and uses of gold.

Items	1959	1960	1961	1962	1963
	in millions of US dollars				
Gold production ¹	1,125	1,175	1,215	1,290	1,350
Sales by the USSR	300	200	300	200	550
Total	1,425	1,375	1,515	1,490	1,900
Increase in official gold stocks ¹	750	310	600	335	845
Other uses ²	675	1,065	915	1,155	1,055

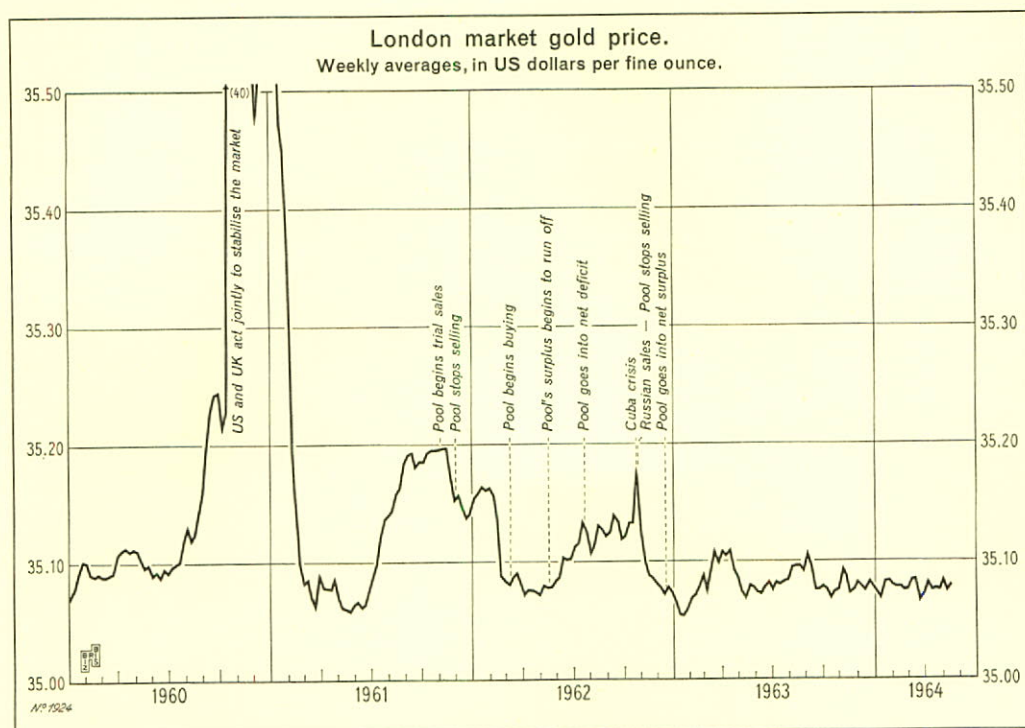
¹ Excluding the USSR, eastern Europe, mainland China and North Korea. ² Residual figures.

One important absorber of non-monetary gold is India. In an attempt to reduce the country's offtake of the metal, Gold Control Rules were introduced by the Indian authorities in January 1963. The possession of undeclared non-ornament gold, except in very small quantities, was made illegal; the activities of gold dealers were brought under strict official supervision; and, except by conversion from existing ornaments, no new ornament could have a gold content higher than 14 carats. At first these measures had a distinct effect on the amount of gold going to India, but it would seem that before the end of the year the country's offtake had probably regained the pre-control level.

Turning to the course of prices on the London gold market, the graph shows their very limited range by comparison with other recent years. 1963 opened with quotations around \$35.06½ and by 10th January — under the influence of Russian sales and the Indian measures mentioned above — they had fallen to \$35.05, the lowest "fixing" price for the year. Soon afterwards the market became firmer and this trend continued, with minor interruptions, until the "fixing" price on 11th April — just before the Easter week-end — reached nearly \$35.12, the highest figure recorded during the year. Russian sales had fallen away to practically nothing; South Africa, which had sold \$23 million of gold during December 1962 and January 1963 out of its reserves (i.e. in addition to current production) added \$105 million's worth to them in February–May 1963; and the first impact of the Indian measures was wearing off. On top of these factors, there was an increase in speculative demand just before the Easter break. This was reversed immediately afterwards. By the end of April prices had fallen below \$35.08, around which level they then remained for the next two or three months.

At the end of July, immediately after the announcement of proposals for curbing the outflow of capital from the United States, the price rose to about \$35.10 and private demand remained active throughout the next few months. The effect of the heavy Russian selling, however, overshadowed this and from over \$35.11 at the end of August 1963 quotations were down below \$35.07 a month later.

Prices were virtually unaffected either by the assassination of President Kennedy or by the cessation of Russian selling in mid-December. They



remained — despite some increase in private demand from Italy and Greece — mostly around the \$35.08 level until renewed sales by the USSR brought them down below \$35.06 again in late March 1964.

Gold and exchange holdings.

The next table shows the total gross ascertainable holdings at the end of 1963 (together with the changes that occurred in 1962 and 1963), by countries and by international institutions, of gold, short-term dollars and sterling. It also includes the official US holdings of convertible currencies and the official franc balances of the French franc area. Measured in this admittedly approximate fashion, there was a very large increase of \$3 milliard during 1963 in countries' gross holdings of international liquid assets. Roughly half of this increase was in dollar assets, with the remainder about equally divided between gold and sterling. International institutions, by contrast, showed slightly lower holdings at the end of 1963 than a year earlier.

Gold. The estimated rise of \$845 million in published official gold holdings during 1963 brought them by the end of the year to a total of \$42.3 milliard. Taking the whole year 1963, the gold figures indicate a familiar pattern — the absorption by Europe of surplus new gold plus gold from the official US stock. During the last four months of the year, however, the United States was able to cover almost all of its net gold sales to foreign countries out of

International liquidity, 1962-63.

Holders	Years and end of years	Gold	Short-term US dollars	£ sterling	Other currencies	Total	Net IMF position	Grand total	Memo-randum item ¹
in milliards of US dollars									
United States	1962, change	- 0.9			- 0.0	- 0.9	- 0.6	- 1.5	
	1963, change	- 0.5			+ 0.1	- 0.3	- 0.0	- 0.4	
	End-1963, total	15.6			0.2	15.8	0.2	16.0	
United Kingdom	1962, change	+ 0.3	- 0.6			- 0.3	+ 1.1	+ 0.8	
	1963, change	- 0.1	- 0.1			- 0.2	- 0.0	- 0.2	
	End-1963, total	2.5	1.5			4.0	0.5	4.5	
Continental western Europe	1962, change	+ 0.9	+ 0.5	- 0.1		+ 1.2	- 0.2	+ 1.0	
	1963, change	+ 1.0	+ 0.7	- 0.0		+ 1.7	+ 0.1	+ 1.8	+ 0.6
	End-1963, total	17.2	9.3	1.8		28.2	1.7	30.0	0.6
Total	1962, change	+ 0.3	- 0.2	- 0.1	- 0.0	- 0.0	+ 0.2	+ 0.2	
	1963, change	+ 0.5	+ 0.6	- 0.0	+ 0.1	+ 1.2	+ 0.0	+ 1.2	
	End-1963, total	35.3	10.8	1.8	0.2	48.0	2.4	50.5	
Other countries	1962, change	- 0.1	+ 1.3	+ 0.0	+ 0.0	+ 1.2	- 0.2	+ 1.0	
	1963, change	+ 0.3	+ 0.8	+ 0.7	+ 0.0 ²	+ 1.8	+ 0.0	+ 1.8	+ 0.1
	End-1963, total	4.7	10.5	9.5	0.5 ²	25.3	- 0.3	24.9	0.1
All countries	1962, change	+ 0.2	+ 1.1	- 0.1	+ 0.0	+ 1.2	+ 0.1	+ 1.3	
	1963, change	+ 0.7	+ 1.4	+ 0.7	+ 0.1	+ 3.0	+ 0.1	+ 3.0	+ 0.7
	End-1963, total	40.0	21.3	11.3	0.7	73.3	2.1	75.4	0.7
International institutions	1962, change	+ 0.1	+ 1.4	- 1.0		+ 0.5		+ 0.5	
	1963, change	+ 0.1	- 0.5	+ 0.1		- 0.3		- 0.3	
	End-1963, total	2.3	4.6	1.8		8.7		8.7	
Grand total	1962, change	+ 0.3	+ 2.5	- 1.1	+ 0.0	+ 1.7	+ 0.1	+ 1.8	
	1963, change	+ 0.8	+ 0.9	+ 0.8	+ 0.1	+ 2.7	+ 0.1	+ 2.7	+ 0.7
	End-1963, total	42.3	25.9	13.0	0.7	82.0	2.1	84.1	0.7
Grand total, official holders	1962, change	+ 0.3	+ 2.4 ³	- 1.3	+ 0.0	+ 1.5	+ 0.1	+ 1.5	
	1963, change	+ 0.8	- 0.0 ³	+ 0.4	+ 0.1	+ 1.3	+ 0.1	+ 1.4	+ 0.7
	End-1963, total	42.3	17.1 ³	8.3	0.7	68.4	2.1	70.5	0.7

¹ US Government non-marketable, medium-term convertible securities. ² Estimated.

³ These figures are reported by banks in the United States. As some officially-owned foreign dollar balances are held with commercial banks outside the United States they will be reported as belonging to those banks. The total of official foreign dollar balances at the end of 1963 is, therefore, certainly understated and the changes in 1962 and 1963 are also affected.

Note: The figures for short-term dollars are taken from the Federal Reserve Bulletin. Those for sterling balances are net in 1962 and gross in 1963. North American sterling balances have been allocated to "Other countries", since it was not possible to separate the United States from the rest of North America. "Other currencies" consist of US official holdings of convertible currencies (including sterling) and of official franc balances of the French franc area, the latter as reported by the International Monetary Fund. Figures may not add to totals because of rounding.

its "share" of available market supplies and the same was virtually true during the first quarter of 1964. Between the end of September 1963 and the end of March 1964 the US gold stock declined by only \$84 million and in April it rose by \$178 million.

The US gold loss for 1963, at \$461 million, was easily the smallest since 1958. It was the outcome of three main movements: net sales of \$729 million to continental western Europe; purchases of \$329 million from the United Kingdom, corresponding roughly in size to the American share of the gold pool's surplus; and net sales to domestic users of \$69 million. The latter figure has been increasing steadily of recent years; in 1958, for instance, the US Treasury had been able on balance to buy \$19 million of gold from resident sources.

European countries' published gold reserves rose during 1963 by \$1,151 million. Continental countries' holdings (excluding the BIS and the European Fund) went up by \$1,249 million, while the UK reserve dropped by \$98 million. The spot gold position of the BIS fell by \$229 million to a net minus figure of \$279 million.

As already mentioned, the Continent bought \$729 million of gold from the US Treasury — France accounting for \$518, Spain for \$130 and Austria for \$82 million. The remaining \$520 million came from the Continent's share of the gold pool's surplus, from UK sales and from gold swaps between the BIS and the Swiss National Bank, which brought the latter's gold reserves to a figure \$153 million above their end-1962 level. Elsewhere in Europe, Germany's gold reserve rose by \$165 million and that of Italy by \$100 million during 1963.

The negative spot gold position of the BIS at the end of 1963 was, of course, covered by forward gold assets. A good part of these consisted of gold due under the swaps with the Swiss National Bank. In addition, there were some outstanding Russian contracts. During the first quarter of 1964 there was a turn-round of \$302 million in the BIS spot gold position, to a positive figure of \$23 million, while Switzerland's gold reserve declined by \$278 million. Altogether, continental countries' gold reserves showed a decline of some \$200 million during these three months.

The other countries in the table added \$275 million to their gold reserves in 1963. Most of this can be accounted for by South Africa and Canada, the two main western gold producers, who added \$131 and 109 million respectively to their holdings. Altogether, countries' published official gold reserves, plus those of the BIS and the European Fund, showed a rise of \$727 million — after only \$218 million in 1962. The IMF's gold stock went up by \$117 million, almost the same as the year before.

Exchange. Countries' holdings, both of short-term dollars and of sterling, rose substantially during 1963. There were considerable increases in official and private holdings of both currencies, the most notable feature perhaps being the improvement in the exchange position of the developing countries.

Foreign countries' short-term dollar assets, as reported by the US banking system, went up by \$1.4 milliard. The statistics show this increase as about equally distributed between official, commercial-bank and other holdings. Proportionately the biggest rise was in private non-bank balances, which increased by \$0.5 milliard, or 20 per cent., to a total of \$3.0 milliard at the end of the year. Latin American non-bank holders alone added \$340 million to their balances.

Foreign countries' sterling balances rose by \$0.7 milliard to a total of \$11.3 milliard at the end of the year. Here, too, private holders accounted for more of the rise than official ones, with \$0.4 against 0.3 milliard. \$240 million of the increase in private holdings was outside the sterling area. In particular, Middle and Far Eastern, as well as eastern European, balances

were higher; at the same time, UK sterling claims on these countries went up by slightly more.

The combined short-term dollar and sterling balances of the group of "other countries" rose by \$1.5 milliard in 1963, after an increase of \$1.3 milliard the previous year. If, however, four developed countries in this group which are substantial holders of exchange are taken separately, a big improvement is visible between the two years in the exchange position of developing countries. Thus, Canada, Japan and Australia accounted for all but \$0.1 milliard of the 1962 increase in short-term dollars, whilst in 1963 their balances showed a slight fall. Developing countries therefore added \$0.9 milliard to their short-term dollars in 1963, compared with only \$0.1 milliard the year before. Latin American dollar balances went up by \$0.7 milliard and those of Asia (excluding Japan) by \$0.3 milliard. So far as sterling balances are concerned, those of developing countries, after showing little change in 1962, rose by about \$0.3 milliard last year. Altogether, then, exchange balances of developing countries were up by \$1.2 milliard in 1963, after only \$0.1 milliard in 1962.

International institutions' holdings of sterling showed little change in 1963; their short-term dollar balances, despite a small rise in IMF balances, fell by \$0.5 milliard. This was partly offset by additions of \$0.3 milliard to their holdings of marketable US Government bonds and notes with original maturities of over one year. Canada's holdings of such paper also increased by a similar amount. Taking the change in total US liquid liabilities to foreigners at \$1.6 milliard, as recorded in the official balance-of-payments statistics, nearly \$1 milliard was accounted for by short-term liabilities and \$0.7 milliard by higher foreign holdings of marketable bonds and notes.

The US international liquidity position.

With a deficit of \$3.3 milliard on "regular" transactions to be financed, the US monetary authorities took steps during 1963, as they had in the two preceding years, to minimise the calls made on the country's gold reserve. In the event the 1963 gold loss was 14 per cent. of the deficit, as compared with 25 per cent. of the larger deficit in 1962.

During the past four years five main factors have contributed to lessening the impact of the balance-of-payments deficit on the US gold stock: official compensatory transactions (non-scheduled receipts on government loans and advances on military exports) to reduce the effective deficit; reduction of the US gold tranche position at the IMF, largely through repayment of former US lending through the Fund and in February and May 1964 through modest US drawings on the Fund; official US intervention in the forward exchange market; use of the Federal Reserve System's swap network; and the issue by the US Treasury of special non-marketable securities, mostly denominated in foreign currencies.

Leaving aside forward exchange operations, which are discussed on pages 123-4, the contribution in 1963 of the other four factors amounted to \$1.5 milliard, or almost one-half of the "regular" balance-of-payments deficit. The year before, the corresponding figure had been \$2.3 milliard, nearly two-thirds of a rather bigger deficit. Larger issues of non-marketable securities in 1963 were more than offset by the fact that there was hardly any further reduction in the US gold tranche position at the Fund, as well as by smaller debt prepayments from abroad.

Financing of the US balance-of-payments deficit, 1962-63.

Items	1962	1963		
		Total	1st half	2nd half
		in millions of US dollars		
Deficit on regular transactions	3,573	3,301	2,023	1,278
Financed by				
1. Advance receipts	1,136	684	74	610
<i>Non-scheduled receipts on</i>				
government loans	666	325	59	266
Advances on military exports	470	359	15	344
2. Changes in US liabilities to foreigners (decrease —)	904	2,239	1,793	446
(a) Official				
Non-marketable securities	299	641	532	109
Dollars held under swaps	265	175	—	175
Other	140	820	725	95
Sub-total	704	1,636	1,257	379
(b) Private				
Commercial banks	— 147	434	459	— 25
Other	347	169	77	92
Sub-total	200	603	536	67
3. Changes in US monetary reserve assets (increase —)	1,533	378	156	222
of which				
Gold	890	461	227	234
Convertible currencies	17	— 113	— 27	— 86
IMF position	626	30	— 44	74

Thus, after taking into account a rise of \$113 million in official US holdings of convertible currencies, there remained an amount of \$1.9 milliard to be covered by a reduction in gold reserves and an increase in ordinary liquid liabilities. This was considerably more than the corresponding 1962 figure of \$1.2 milliard. In the event the reduction in the gold stock was the smallest since 1958, while foreign countries' outright holdings of short-term dollars went up by \$1.4 milliard. The moderate decline in the gold stock may be attributed partly to the larger supplies of and the reduced non-monetary demand for the metal. The substantial increase in dollar balances reflects some revival of confidence in the dollar, as well as the improved position of a number of developing countries that traditionally hold their monetary reserves in dollars and, probably, the temporary retention by Russia of the dollar proceeds of some gold sales. (Short-term claims on foreigners reported by US banks, treated as a capital outflow and therefore as part of

the deficit on regular transactions, went up by about \$750 million, more than twice as much as in 1962. Japan accounted for \$400 million, mostly towards the end of the year.)

During 1963 the swap network was increased from \$900 to \$2,050 million. In addition, several of the arrangements were placed on a six-month or one-year basis, instead of, as previously, only three months. US use of swaps in 1963 was concentrated on three currencies — the Deutsche Mark, the florin and the Swiss franc. The circumstances in which these operations took place differed considerably from case to case. Firstly, mention may be made of the increasing strength of the German balance of payments during the first half of 1963 which led the Federal Reserve System to disburse nearly \$150 million from its DM swap facility during May and June in order to moderate market pressures and to mop up excess dollars. In August it was deemed prudent to fund \$50 million of this by the issue of a DM bond to the Bundesbank and the rest of the swap commitment was paid off by October 1963, mostly with the proceeds of German defence payments to the United States.

US Federal Reserve System swap arrangements.

Facilities with	End 1962	March 1964
	in millions of US dollars	
Austria	50	50
Belgium	50	50
BIS	100	150
Canada	250	250
France	50	100
Germany	50	250
Italy	150	250
Japan	—	150
Netherlands	50	100
Sweden	—	50
Switzerland	100	150
United Kingdom	50	500
Total	900	2,050

Secondly, there were two instances of the US authorities making use of swap facilities to dampen down speculative movements of funds that were unfavourably affecting the dollar. The first was in connection with the rumours that began circulating about the Dutch florin in September 1963. In order to absorb the inflow of dollars to the Netherlands that resulted, the Federal drew \$100 million of florins under its swap facility, the greater part of which was used to mop up excess dollar balances at the Nederlandsche Bank and the rest to buy dollars in the market. This situation had, by the end of February 1964, reversed itself sufficiently for the drawings to have been reduced to \$25 million. Another case of this sort was the movement of funds to Switzerland in September and October 1963, partly arising out of market gossip at the time of the IMF's annual meeting and partly out of a

flight of capital from Italy. During these two months the Federal disbursed \$160 million out of its Swiss franc swap facilities to absorb Swiss receipts of dollars.

A third type of use of swap facilities by the United States has been in connection with temporary shortages of liquidity in foreign money markets. These, typically, result in the banking system of the country concerned repatriating liquidity held abroad. Such a movement of funds took place into the Netherlands in April-May 1963, leading the Federal to use \$44 million of its florin swap facility to mop up the dollars concerned. In June the Dutch money market became more liquid again and by the end of July (partly with the aid of florins obtained by swapping DM with the BIS) the swap had been put back on a stand-by basis. Analogous situations arose out of the end-year operations of the German and Swiss banking systems. In Germany the Federal had by mid-December 1963 used \$136 million of its DM swap facilities in this connection; a reversal of these operations, together with further German defence payments to the United States, enabled the Federal to liquidate this swap in full by early January 1964. In the Swiss case, swap drawings occasioned by the end-year operations of the banks amounted to the equivalent of \$70 million. Altogether the US debtor position under its Swiss franc swap lines was \$220 million at the end of 1963 and three months later only small progress had been made in reducing it.

Three other countries made use of the swap network in 1963 and early 1964. The excess of foreign currencies used by the United States under the swap lines over foreign countries' use of swap dollars fell from \$216 million at the beginning of 1963 to a low point of only \$20 million in late September. After rising to \$324 million at the end of the year, the US net debtor position declined again to \$145 million at end-February 1964.

Net sales of US Government non-marketable securities to foreign countries amounted to \$641 million in 1963, more than double the previous year's figure. Of this amount, \$181 million were special dollar securities. In January 1963 \$125 million of the proceeds of a Government of Canada bond issue in New York was placed in a fifteen-month non-marketable US Treasury bond and during the same month Italy subscribed to a \$58 million five-year non-marketable bond, the amortisation of which was timed to coincide with payments due to the US Government from Italy in 1968. In view of the Italian payments deficit, and as the bond carried a mobilisation clause, all but \$13 million of it had been redeemed in advance by the end of 1963. Sweden subscribed to a \$25 million twenty-seven-month non-marketable dollar bond in July 1963; and lastly the Export-Import Bank sold \$18 million of certificates to European countries during the year.

Issues of US Government non-marketable bonds denominated in foreign currencies amounted in 1963 to \$460 million. The Swiss Confederation's holdings of such paper went up by \$105 million, the whole of this sum being used by the US Treasury to pay off maturing exchange contracts in Swiss francs and to provide the Swiss Government with an intermediate-term

investment — the bonds issued ranged from twelve to eighteen months — for surplus funds which it did not wish to put into the Swiss financial circuit.

German holdings of DM bonds went up by \$275 million during 1963. \$200 million of these, issued for periods of between fifteen months and two years in January and February 1963, were a kind of funding of dollars previously accumulated in the Deutsche Bundesbank's reserves. In July 1963 a further \$25 million DM bond with a life of two years was issued to procure funds for mopping up dollars flowing into Germany, after the Federal Reserve System's DM swap facilities had been fully used for this purpose. In the following month another two-year DM bond, this time for the equivalent of \$50 million, was issued to provide funds for reducing the Federal Reserve's outstanding DM swap commitment. This was the first example of a swap borrowing being funded by the issue of a foreign currency bond.

Also during 1963 there were small issues of such bonds to Belgium and Austria. In May 1963 twenty-four-month Belgian franc bonds for the equivalent of \$30 million were issued to prevent the dollar balances of the National Bank of Belgium being increased by the proceeds of Belgian Government borrowings in New York and London which took place at that time. On two occasions, in April and December 1963, the US Treasury issued eighteen-month Austrian schilling bonds for the equivalent of \$25 million each and used the proceeds to absorb some of the growth in Austria's official dollar balances.

In March and April 1964 there occurred the first redemption of foreign currency securities, as well as a substantial issue of new ones. When the Italian balance of payments turned into deficit in 1963 Italy was holding amongst its second-line reserves lira bonds issued by the US Treasury in 1962 to the equivalent of \$200 million. Between October 1963 and March 1964 the United States authorities bought \$200 million of lire from the Bank of Italy and placed the money on deposit there. When the earliest-dated of the lira bonds matured, in March 1964, it was paid off out of these balances; and the remaining \$150 million was redeemed in advance by the same method on 1st April 1964.

On the same day Germany subscribed to a further two-year DM bond for the equivalent of \$200 million, bringing the Bundesbank's holdings of US Government foreign currency securities up to \$475 million out of a total of \$760 million outstanding in April 1964.

For the first quarter of 1964 the US balance of payments on regular transactions showed a surplus of \$110 million. Receipts from special transactions amounted to \$95 million, leaving a surplus of \$205 million to be reflected in monetary movements. The gold reserve declined by \$45 million and the net IMF position by \$130 million; on the other hand, official holdings of convertible currencies rose by \$230 million. Reserve assets, therefore, went up by \$50 million, and liquid liabilities to foreigners declined by \$155 million.

European monetary reserves.

Western European countries' official holdings of gold and exchange, as shown in the next table, went up by \$2 milliard in 1963. Continental reserves rose by a little more than that figure and there was a moderate decline in those of the United Kingdom. These substantial further additions to monetary reserves were associated with a large increase in foreign liabilities of these countries' banking systems taken as a group. Excluding Switzerland, where no figures for the commercial banks' foreign situation are available, what happened was as follows: official gold and exchange reserves rose by \$1.8 milliard and commercial-bank net foreign liabilities by \$1.5 milliard. This was to a large extent a repetition of 1962 when (again leaving out Switzerland) official European reserves had gone up by \$0.6 milliard and the banks' net foreign liabilities by \$1 milliard. In 1962, however, Europe had improved its net IMF position by \$850 million, through UK repayments of its 1961 drawing; last year net European lending through the Fund amounted to less than \$100 million.

During the first quarter of 1964 western European countries' reserves declined by \$0.6 milliard. There was no change in their net IMF positions taken together, while the foreign position of their commercial-banking systems almost certainly improved by more than the fall in official reserves. For ten continental countries (excluding Switzerland) the improvement was \$0.6 milliard and the fall of over \$0.3 milliard in Switzerland's reserves during the first quarter of 1964 was associated with a large re-export of funds by the Swiss banks.

Eight European countries showed substantial increases in their monetary reserves during 1963. In one, Belgium, the rise reflected and was entirely offset by a deterioration in the foreign position of the banking system. In four others, France, Germany, the Netherlands and (probably, though it cannot be proved statistically) Switzerland, there was a partial offset of this sort. In Austria and Denmark, however, the external position of the banks improved somewhat, so that official reserves went up by less than the overall balance-of-payments surplus.

France. For the third successive year, France was the biggest gainer of reserves in Europe. The overall surplus from regular transactions was \$935 million, \$280 million of which was used to prepay external public debt. Monetary movements, therefore, were positive to the extent of \$655 million. Official holdings of gold and convertible currencies went up by \$845 million, to a total of \$4,457 million at the end of the year. On the other hand, the banking system's foreign position, following the pattern of other recent years, showed a further rise of \$200 million in net liabilities. Non-residents' franc balances increased by \$50 million. This occurred almost entirely during the first quarter, and in April 1963 French banks were forbidden to pay interest on deposits owned by persons and institutions resident outside the franc area. Residents' net foreign exchange holdings were drawn down by a further \$150 million.

European countries: Reserve positions.

Countries	End of year	Net reserves			Net IMF position	Net reserves plus or minus net IMF position
		Gold	Foreign exchange	Total		
		in millions of US dollars				
Austria	1961	303	520	823	19	842
	1962	454	597	1,051	26	1,077
	1963	536	650	1,186	37	1,223
Belgium-Luxemburg. . .	1961	1,248	389	1,637	157	1,794
	1962	1,365	237	1,602	133	1,735
	1963	1,371	445	1,816	141	1,957
Denmark	1961	31	205	236	33	269
	1962	31	179	210	33	243
	1963	31	397	428	33	461
Finland	1961	47	258	305	14	319
	1962	61	206	267	14	281
	1963	61	239	300	14	314
France	1961	2,121	818	2,939	427	3,366
	1962	2,587	1,023	3,610	439	4,049
	1963	3,175	1,282	4,457	450	4,907
Germany	1961	3,664	2,793	6,457	637	7,094
	1962	3,679	2,679	6,358	517	6,875
	1963	3,844	3,199	7,043	552	7,595
Greece	1961	87	164	251	15	266
	1962	77	193	270	15	285
	1963	77	201	278	15	293
Italy	1961	2,225	1,194	3,419	243	3,662
	1962	2,243	1,248	3,491	203	3,694
	1963	2,343	714	3,057	226	3,283
Netherlands	1961	1,574	102	1,676	243	1,919
	1962	1,574	128	1,702	203	1,905
	1963	1,594	277	1,871	203	2,074
Norway	1961	29	240	269	25	294
	1962	29	237	266	25	291
	1963	29	289	318	25	343
Portugal	1961	443	248	691	15	706
	1962	471	321	792	15	807
	1963	497	330	827	15	842
Spain	1961	316	547	863	23	886
	1962	446	561	1,007	38	1,045
	1963	573	520	1,093	54	1,147
Sweden	1961	180	461	641	63	704
	1962	181	567	748	48	796
	1963	182	518	700	53	753
Switzerland	1961	2,560	194	2,754	—	2,754
	1962	2,667	201	2,868	—	2,868
	1963	2,820	250	3,070	—	3,070
Turkey	1961	140	— 44	96	— 21	75
	1962	140	— 61	79	— 27	52
	1963	115	— 83	32	— 31	1
United Kingdom	1961	2,268	1,050	3,318	— 559	2,759
	1962	2,582	224	2,806	502	3,308
	1963	2,484	173	2,657	489	3,146

Note: 1. Net reserves consist of central-bank and/or other official holdings of gold and foreign exchange, excluding IMF positions and claims or debts arising out of the liquidation of the EPU. The figures are also net of any other foreign exchange liabilities shown in the central-bank returns or other official sources, except for the UK sterling liabilities. For France, Italy, Spain, Switzerland and the United Kingdom the net reserves consist of gold and convertible currencies only. For Germany they exclude non-freely-usable balances which (ignoring claims arising out of the liquidation of the EPU) amounted at the end of 1961, 1962 and 1963 to \$353, 351 and 345 million respectively. 2. Net IMF position is gold subscription, plus repurchases of currency subscription, minus the member's net drawings or plus the Fund's net sales of its currency, plus or minus the Fund's administrative and operational expenditure or receipts in its currency.

With the foreign trade position deteriorating during the course of the year, the overall balance of payments had moved nearer to equilibrium by the end of 1963. During the first four months of 1964, in fact, official gold and exchange reserves went up by only \$76 million. At the same time France's net IMF position improved by \$50 million.

Germany. Two years after the revaluation of the Deutsche Mark Germany's monetary reserves began to increase again and by the end of 1963 they stood at \$7,043 million — some \$40 million above the high point reached at the end of March 1961.

The overall 1963 payments surplus resulted in total monetary movements of \$505 million. The central bank's holdings of gold and freely-usable currencies rose by \$685 million and Germany's net IMF position improved by \$35 million. Partially offsetting these movements were a further reduction of \$35 million in Germany's claims arising out of the liquidation of the EPU and an increase of \$175 million in the net external liabilities of the banking system. The foreign assets of German banks at the end of 1963 (a year in which the Bundesbank offered no special facilities for money exports) were rather higher than they had been a year earlier; non-residents' DM balances, however, went up by as much as \$215 million.

During the early part of 1964 Germany's official monetary reserves continued to rise, despite the reversal of end-year operations by the banking system, and on 10th March the Bundesbank resumed offering the banks special dollar swap facilities, limiting them to money employed in US Treasury bills. Between then and the end of March the Bundesbank sold \$95 million in this way and its reserves — also under the influence of DM drawings on the IMF — fell by \$90 million during the month. For the first quarter of 1964 as a whole the Bundesbank's reserves showed a small rise of \$6 million and Germany's net IMF position improved by \$92 million. In addition, the banking system's net external liabilities declined by \$555 million. The two most important factors contributing to this decline were money exports by the banks which, including some increase in credits to non-residents, amounted to \$277 million and the withdrawal of \$167 million of non-resident deposits from German banks.

Switzerland. The Swiss National Bank's external reserves stood at \$3,070 million on the last day of 1963, a rise of \$202 million on the year. End-year operations of the Swiss banks increased them by \$316 million in December 1963 and this was reversed the following month. If, however, November 1963 is compared with November 1962 or January 1964 with January 1963, there is still a rise — of \$146 and 118 million respectively.

No figures are available for the Swiss commercial banks' foreign position, but it would seem not unlikely that a part of the 1963 capital inflow into Switzerland affected them. The banks are known to have repatriated funds from abroad to replenish their liquidity, quite apart from their mid-year and end-year operations, and some of the influx of money from Italy during

the latter months of the year may well have gone to increase non-resident franc balances.

Following a drop of over \$200 million in January 1963, when end-1962 operations were reversed, the National Bank's external reserves were rather stable until the end of July. Indeed, they were only prevented from falling during this period by the fact that the US monetary authorities paid off in cash some \$140 million of short-term Swiss franc indebtedness.

The proposed interest equalisation tax in the United States and the decreasing liquidity of the Swiss money market produced an influx during the third quarter, on top of which was superimposed a flight of capital from Italy in October. Between the end of July and the end of October 1963 the National Bank's reserves increased by \$140 million. The rise would have been much larger but for forward sales of Swiss francs in the market by the US Treasury, amounting to about \$120 million by the end of October.

At the end of the first quarter of 1964 the National Bank's reserves stood at \$2,740 million, rather more than \$100 million above the March 1963 figure. At that time the Federal Reserve Bank of New York and the US Treasury still had sizable short-term Swiss franc commitments outstanding.

Netherlands. The fourth country where transactions of the banking system affected the size, though not the direction, of changes in the monetary reserves was the Netherlands. After two years of virtual stability, the Nederlandsche Bank's holdings of gold and foreign currencies began to go up again during the second quarter of 1963 and by the end of the year they were \$1,871 million — \$169 million higher than in December 1962. The rise was due to an improvement of nearly \$200 million on current external account which, after allowing for some outflow of capital, produced a surplus on regular transactions of \$210 million. \$70 million of debt owed to the US Government was repaid in advance, so that monetary movements totalled \$140 million. Partly offsetting the rise in official reserves was a decline of some \$30 million in the substantial net foreign assets of the banking system.

Towards the end of the year the balance of payments began to deteriorate considerably, though the reserves went on rising until the end of November. After the turn of the year, however, they began to reflect the change in the trade balance and by the end of March 1964 had declined to \$1,791 million — a loss of \$80 million for the quarter.

Belgium. If all four of the countries so far discussed owed a part of the rise in their official reserves to the effect of commercial-bank transactions, of Belgium in 1963 it can be said that the increase of \$214 million in the National Bank's gold and exchange holdings was almost exactly matched by a deterioration in the foreign position of the credit institutions. The overall balance of payments was in almost perfect equilibrium for the year as a whole — though during its course there was a pronounced change from surplus to deficit. This turn-round, as well as the opposite movements in

official holdings and those of the credit institutions, can be seen from the fact that during the first half of the year the National Bank's monetary reserves rose by \$152 million and the net external liabilities of the credit institutions by \$74 million, while the corresponding figures for the period July–December 1963 were \$72 and 154 million. The main cause of both movements was government borrowing abroad through the banking system. The whole of the 1963 increase of \$174 million in the National Bank's convertible currency balances was matched by larger forward commitments to sell exchange to the government and the banking system.

Denmark. Denmark's monetary reserves doubled during 1963, from \$210 million to a record level of \$428 million. The banking system, whose position had deteriorated by \$80 million during the 1961–62 crisis, showed an improvement of \$25 million, so that the overall balance-of-payments surplus was \$240 million, 80 per cent. of which was attributable to capital imports.

Austria. Austria added a further \$135 million to its monetary reserves in 1963, bringing them to \$1,186 million at the end of the year. The increase was taken as to \$80 million in gold — virtually all the rest is accounted for by \$50 million of non-marketable US Government securities denominated in schillings and subscribed to in April and December 1963. As in Denmark, the surplus was by and large on capital account and the banking system's foreign position also improved — by \$43 million.

Spain. The uninterrupted rise in Spain's monetary reserves since 1959 continued during 1963 and into the first months of 1964. For the first time since the stabilisation of the peseta, however, net invisible receipts did not cover the external trade deficit and there was a current-account deficit of \$130 million. As at the same time net capital receipts rose from \$105 to 230 million, mostly at long term, \$86 million was added to the official reserves during 1963 and, in addition, Spain's net IMF position went up by \$16 million.

Italy. Italy's balance of payments shifted from a surplus of \$50 million to a deficit of \$1,245 million in 1963. Yet the country's official gold and convertible currency holdings fell by no more than \$435 million. Indeed, after nine months of the year, which saw an overall deficit of \$790 million, the reserves were only \$60 million lower than in December 1962. Details of monetary movements in Italy are shown in the following table.

Broadly speaking, what happened was that the deficit was almost entirely financed by commercial-bank borrowing during the first nine months, and by changes in official monetary assets and liabilities for the rest of the year. On 1st November 1962 the banks had been dispensed from the obligation, imposed in 1960, to maintain a balanced position in foreign currencies vis-à-vis non-residents, and their net foreign liabilities increased from \$150 million at the end of October 1962 to a peak of \$1,370 million the following

Italy: Monetary movements.

Items	1962	1963	1963		1964 January- March
			January- September	October- December	
in millions of US dollars					
Official gold and exchange reserves . .	+ 70	— 435	— 60	— 375	— 235
Other monetary movements (increase in assets +)	— 20	— 810	— 730	— 80	— 200
of which					
Italian Exchange Office	+ 445	+ 10	+ 30	— 20	— 40
Bank of Italy	— 35	— 170	— 20	— 150	— 360
Commercial banks	— 430	— 650	— 740	+ 90	+ 200
Total (= balance-of-payments surplus/deficit)	+ 50	—1,245	— 790	— 455	— 435

August. The whole of this change was in the banks' position in convertible currencies. During the last quarter of the year the banks' net liabilities declined by \$90 million and the movement continued into the first quarter of 1964. The fall in reserves after September 1963 was nevertheless not as great as the balance-of-payments deficit, since the Bank of Italy's foreign indebtedness increased by \$150 million. One-third of this represented the use by Italy of \$50 million of its swap facility with the Federal Reserve Bank of New York; the remaining \$100 million were lire purchased against dollars by the US authorities and placed on account at the Bank of Italy for later repayment of US Government lira-denominated securities purchased by Italy in 1962.

During the first quarter of 1964 the first-line reserves fell by a further \$235 million to \$2,824 million. At the same time the Bank of Italy's foreign liabilities went up by \$360 million, the causes of this being the \$225 million drawing on the IMF, further purchases of lire by the US authorities totalling \$83 million and a second \$50 million drawing by Italy on its swap facility with the Federal Reserve Bank of New York. On the other hand, the further reduction of the banking system's net indebtedness was nearly \$200 million. In April the banks continued to improve their position and the official gold and convertible currency reserves fell by only \$10 million.

United Kingdom. The official gold and convertible currency holdings of the United Kingdom declined by \$149 million in 1963. The loss was nearly twice as large as the deficit on identified current and long-term capital account, but moderate in view of the large negative balancing item. In fact, to the decline in reserve assets must be added a rise of \$425 million in net external sterling liabilities.

The year can be divided into two halves. During the first, when the basic accounts were in surplus and sterling-area sterling balances went up by \$320 million, reserves fell by nearly \$100 million. On two occasions during the first quarter sterling came under heavy pressure in the exchange market, for reasons unconnected with the balance-of-payments situation, and by the end of March 1963 sterling balances held outside the sterling area had declined by \$400 million. An immediate drop in the reserves was

prevented by the authorities taking \$250 million of deposits from continental central banks, but when these were repaid in June a part of the earlier outflow showed up in the reserves.

The second half of the year saw a recovery of \$360 million in the level of sterling balances held outside the sterling area, as well as a further increase of \$140 million in sterling-area balances. This was almost enough to cover the deficit on identified and unidentified transactions, so that the fall for the six-month period was only \$55 million, entirely concentrated in the last month of the year when the North American debt payments led to a decline of \$115 million. During the first quarter of 1964 the reserves showed, on balance, no change while sterling balances increased by a further \$145 million.

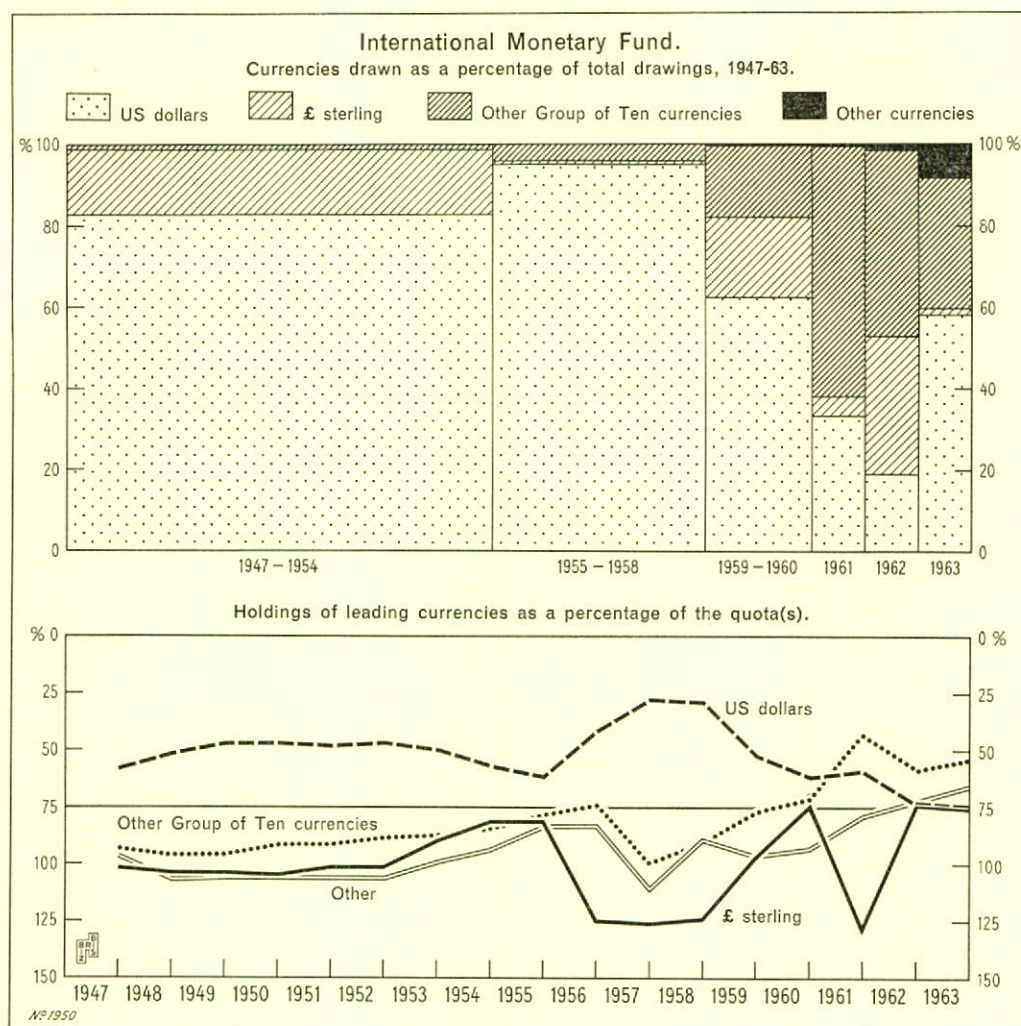
Sweden. The rise in Sweden's monetary reserves, which had begun in 1960, came to a stop during 1963. By the end of the year the central bank's holdings of gold and exchange stood at \$700 million, \$48 million below the level of a year earlier. In part this was offset by a rise of \$20 million in the net assets of the banking system. In 1962, however, the central bank and banks combined had added about \$100 million to their net foreign assets.

International Monetary Fund.

Following the large reduction of \$0.9 milliard in member countries' use of its resources during 1962, the Fund resumed net lending in 1963, though on a very modest scale. Drawings were \$333 million and repayments \$267 million, so that the net amount drawn rose by \$66 million.

Reversing the trend of recent years, nearly 60 per cent. of gross IMF drawings in 1963 were in US dollars and another one-third in other Group of Ten currencies. From the beginning of Fund operations in 1947 until the re-establishment of European convertibility at the end of 1958, total gross drawings on the Fund were \$3.2 milliard, 90 per cent. in US dollars. In 1959-60 the dollar element fell to about 60 per cent., in 1961 to one-third and in 1962 below 20 per cent. As, concurrently with this, the dollar was the main currency used by members repurchasing their currency, net drawings of dollars fell from \$1.9 milliard at the end of 1958 to virtually zero by the end of 1962. Other Group of Ten countries, on the other hand, moved from a net debtor position of \$1 milliard immediately before convertibility to a net creditor position of \$650 million at the end of 1962.

With IMF holdings of US dollars back to 75 per cent. of the US quota by the end of 1962, there was no further room for net repayments of dollars to the Fund. Such repayments had contributed substantially to financing the US payments deficit since 1958, not least during 1962 when the Fund's holdings of dollars were increased by over \$600 million. The danger arose that Fund members wishing to repurchase their currencies would put



pressure on the US gold stock, either directly by buying gold from the US Treasury or indirectly by selling dollars for other convertible currencies. The US authorities therefore arranged a \$500 million stand-by at the Fund in July 1963, and two drawings of \$125 million each, mainly in French francs and Deutsche Mark, were made in February and May 1964. The amounts drawn were sold, against dollars, to Fund members for repurchase of their currencies from the Fund.

Another substantial drawing that occurred during the first quarter was one of \$225 million by Italy in March 1964. This corresponded to Italy's \$68 million gold subscription plus the net amounts of lire previously borrowed through the Fund by other members. Altogether there were drawings of \$387 million and repayments of \$162 million during the first quarter of 1964. The main net drawings, by currencies, were \$92 million of Deutsche Mark and \$50 million of French francs.

During the period under review, developing countries began to take advantage of the new facilities established by the Fund in February 1963

for compensatory financing of export fluctuations and under which the Fund may hold a member's currency in amounts of up to 225 per cent. of the quota. The first drawing under these arrangements was one of \$60 million by Brazil in June 1963, and this was followed by a drawing of \$16 million in October 1963 by the United Arab Republic. The latter was the first instance of the Fund's holdings of a member's currency exceeding 200 per cent. of the member's quota.

During 1963 twenty new members, with quotas totalling \$325 million, joined the Fund, bringing the total membership up to 102 and the total of all quotas to \$15.6 milliard. Cuba withdrew from the Fund in April 1964.

In the course of the 1963 annual meeting of the Fund, the finance ministers and central-bank governors of Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden, the United Kingdom and the United States — that is, the representatives of the countries that are parties to the General Arrangements to Borrow in the IMF — met with the Managing Director of the Fund to discuss the international payments situation and to review the functioning of the international monetary system. They agreed that the underlying structure of the present monetary system — based on fixed exchange rates and the established price of gold — had proved its value as the foundation for present and future arrangements. At the same time, however, they decided to undertake a thorough examination of the present system and of future needs for liquidity. The ministers instructed their deputies to examine these questions in close working relations with the IMF and other international monetary institutions. The results of this study, together with further independent investigation of these topics by the IMF, are expected to be discussed at the Fund's next annual meeting in September 1964.

Foreign exchange.

There were no major disturbances in the exchange markets during the period under review. The main changes were the much greater strength of the Deutsche Mark and the weakening of the lira and, to a lesser extent, the pound. Despite the considerable reduction in the US balance-of-payments deficit, none of the major European currencies were below par on the dollar at the beginning of May 1964.

In the forward markets there was official US intervention during the autumn of 1963 to support the dollar against the Dutch florin and the Swiss franc. In both cases the dollar's weakness reflected its position as an international currency rather than any new development in the US balance of payments. In the early part of 1964 the Italian lira weakened considerably on the forward exchange market and the Deutsche Mark became very firm.

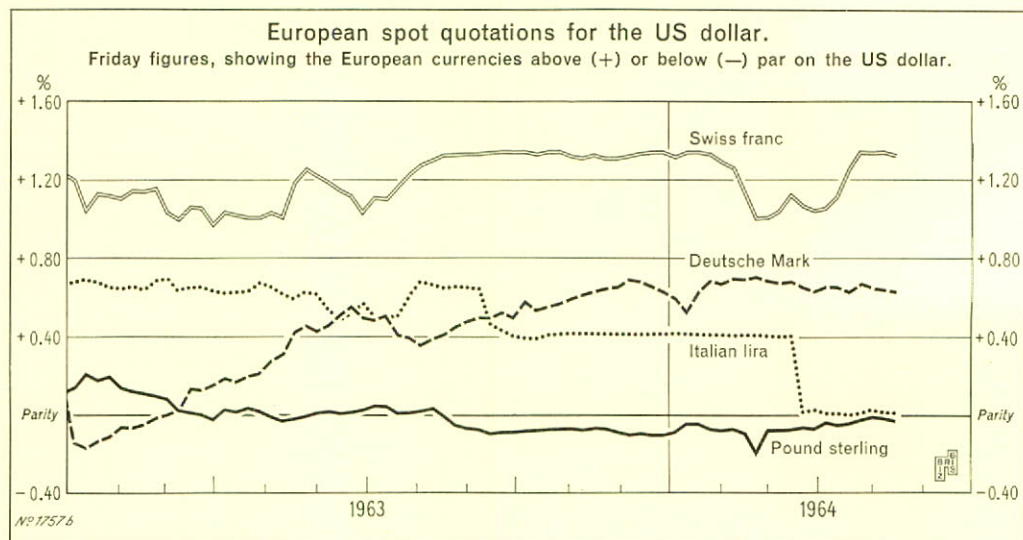
Spot markets. The Deutsche Mark strengthened fairly consistently throughout 1963 as the German balance of payments returned to surplus. From somewhat below par on the dollar in January 1963 — when the banks were

re-exporting funds they had repatriated temporarily at the end of 1962 — the spot rate climbed to a premium of 0.7 per cent., near its upper limit, in December 1963. After easing slightly in early January 1964, the DM has since been very firm again.

The lira, on the other hand, has been under considerable pressure since the summer of 1963. Until then, the serious balance-of-payments situation was masked by the large foreign currency borrowings of Italian banks, and the spot rate vis-à-vis the dollar, though no longer consistently at its upper limit as in the balance-of-payments surplus period, was very firm. When the banks stopped borrowing in this way, the reserves and the exchange rate were at once affected. In September 1963 the premium of the lira on the spot dollar was reduced from 0.65 to 0.4 per cent., at which point the authorities then held the rate fixed for six months during which the country's official gold and convertible currency holdings declined by over \$600 million. In March 1964 the authorities lowered the effective support point again, to approximately the parity.

The exchange rate for the pound sterling has during the period under review remained very close to par on the dollar. At the beginning of 1963 the spot rate was \$2.80½ and there was even some intervention by the Federal Reserve Bank of New York to support the dollar. Then came the two periods of pressure on the pound, met essentially by short-term borrowing from continental central banks. The pound weakened to just below \$2.80 by mid-March, subsequently becoming rather firmer in the second quarter, though movements in the rate were very small.

The latter part of the year, as well as being seasonally less favourable for sterling, saw imports rising strongly and an upward movement of interest rates in New York; there was also the beginning of what may be called the pre-election period in the United Kingdom. The pound went below par on the dollar in August 1963 and remained there until the end of April 1964.



Given the domestic situation in the United Kingdom, the behaviour of the spot dollar rate in recent months has been by no means unfavourable, probably in large measure because of balance-of-payments developments in the outer sterling area. And security sterling has been quoted very little below the official rate during the whole period. The investment dollar rate — the price which UK residents pay for exchange with which to buy foreign securities and to make direct investments outside the sterling area — rose between August 1963 and January 1964 from a premium over the official rate of rather more than 7 per cent. to one of nearly 14 per cent. It would appear that there was some increase in direct investment through this channel and, in addition, portfolio investment demand was strong for two reasons: the firmness of the US stock market and the approach of the British general election. In mid-May 1964 the investment dollar premium was about 11 per cent.

The Swiss franc/dollar exchange rate followed in 1963 a pattern not dissimilar to that of the previous year. During the first months of the year the spot premium of the franc was 1 per cent. or only a little more, so that the dollar was well away from the lower point at which the Swiss National Bank intervenes. But the inflow of funds in the latter half of the year brought the rate by the beginning of August to the National Bank's buying price of Sw.fr. 4.3150 and the dollar was weak for the rest of the year. In the early months of 1964, as the underlying balance-of-payments position began to exercise more influence on the situation, and with the Swiss authorities taking various measures to try and prevent fresh capital inflows, the dollar strengthened again.

So far as the spot quotations for other European currencies are concerned, the French franc has remained very firm during the whole of the period under review, mostly at its upper limit against the dollar. In July and again in October the Federal Reserve Bank of New York sold small quantities of francs to test the market, but without effect on the rates. Movements in the florin/dollar rate have continued mainly to reflect variations in Dutch bank liquidity; the florin was, however, exceptionally firm in late September and early October 1963, on rumours of a second revaluation. The Belgian franc has fluctuated narrowly, remaining somewhat above par on the dollar.

Forward markets. Such disturbances as occurred in the exchange markets during the period under review naturally affected forward quotations for currencies more than spot, particularly as movements in the latter were, in some cases, kept to a minimum. So far as the dollar is concerned, there were two episodes that led to official intervention in the forward markets. The first arose out of the short-lived florin revaluation rumours that pushed down the spot dollar rate in the Netherlands in September 1963; to encourage a continuation at that time of the Dutch banks' money exports, as well as to avoid repatriation of funds to the Netherlands, the US Treasury sold some \$40 million of florins one month forward. The rumours evaporated in October and the Treasury was able to meet more than half of its commitments by

spot purchases of florins in the market, the remainder coming from a DM/florin swap with the BIS.

The other episode that affected the forward dollar was the inflow of funds to Switzerland between July and October 1963. In July and August the US Treasury sold \$33 million of Swiss francs forward, in September a further \$72 million and in the first half of October \$44 million more. \$30 million of the earliest-maturing contracts were paid off in late October with the proceeds of a Swiss franc certificate of indebtedness issued by the US Treasury to the Swiss Confederation. The remainder was still outstanding in March 1964. After rising above $\frac{1}{2}$ per cent. in August and September 1963, the forward premium of the Swiss franc on the dollar was subsequently lower for the rest of the year. The re-export of money by the banks in early 1964 caused the premium to rise again, but in April 1964, unusually, it ran off altogether.

A decline in UK Treasury bill rates, together with pressure on the pound, pushed the discount on three-months forward sterling vis-à-vis the dollar out from $\frac{1}{2}$ to nearly $1\frac{1}{2}$ per cent. by mid-March 1963. A net interest advantage (on a covered basis) of nearly 1 per cent. emerged, which was met by the authorities forcing the market to borrow at $\frac{1}{2}$ per cent. above Bank rate. The forward rates subsequently came more into line with interest rate differentials and, with the rise in US money rates during the second half of the year, the forward discount on sterling disappeared for a short period in September 1963. A small discount reappeared in October and this began to widen early in 1964, as the pound came under pressure again, until it stood at nearly $\frac{1}{2}$ per cent. per annum just before the rise in Bank rate from 4 to 5 per cent. on 27th February 1964. After this change the forward discount only moved out another $\frac{1}{4}$ per cent. or so, thus eliminating the covered interest differential in favour of New York that had been re-emerging.

Under the influence of Germany's substantial balance-of-payments surplus, the three-months forward premium of the Deutsche Mark on the dollar widened early in 1964 from $\frac{1}{2}$ to about 1 per cent. This led the Bundesbank to reinstitute on 10th March 1964 the system of special swap facilities for the banks' money exports. By the end of April 1964 the market premium of the Deutsche Mark had fallen to less than $\frac{1}{2}$ per cent.

Pressure on the lira in March 1964, just before the arrangement by Italy of various foreign credit lines, pushed the forward lira to a discount on the dollar equivalent to an interest rate of $7\frac{1}{2}$ per cent. per annum. By the end of April the discount was just below 2 per cent.

Other exchange developments. Since the spring of 1963 there have been no changes of major importance in European exchange control regulations. Three countries — France, Germany and Switzerland — have introduced, or reinforced, measures against unwelcome inflows of funds. These have mostly been described elsewhere in this Report and in any case none of them were exchange control measures in the usual sense of that phrase. It

may, however, be mentioned here that France, as well as banning the payment of interest on non-resident franc deposits in April 1963, restricted further in August 1963 the freedom of French residents to take credits from non-residents.

In Italy during the period under review the authorities took two steps which, though adopted for reasons of credit policy, impinged directly on the foreign exchange field. The first was the prohibition, in September 1963, of further borrowing abroad by the Italian commercial banks, and in fact the banks reduced their net foreign liabilities by about \$300 million during the following six months. The second step, taken in April 1964, was to limit the time allowed for payment of durable-goods imports to a period of thirty days on either side of the date of their arrival in Italy. Previously payments could take place at any time within one year of the arrival of the goods in question.

In Austria, on the other hand, capital movements were further liberalised during 1963. In June the banks were given the widest facilities for attracting short or medium-term foreign funds and for investing abroad their own funds. In November 1963 Austrian residents were given greater freedom to take up investment and trade credits abroad.

Elsewhere in the world, on 1st April 1964 Japan formally introduced convertibility of the yen in current external transactions. At the same time Japan undertook to meet the obligations set out in Article VIII of the Articles of Agreement of the International Monetary Fund. In conjunction with this, the Fund established on 11th March 1964 a twelve-month stand-by arrangement in favour of Japan for an amount of \$305 million.

* * *

International monetary developments in 1963 and the first months of 1964 have been characterised on the one hand by substantial additions to countries' external liquid assets (without a corresponding reduction in those of international monetary organisations) and on the other hand by generally stable conditions in the markets for gold and exchange. The size of the increase in liquidity was mainly the result of three factors: larger gold supplies, better balances of payments in a number of less-developed countries and further subscriptions by certain monetary authorities to non-marketable obligations of the US Government. Stability in the gold and exchange markets, too, was a matter partly of the situation as it developed and partly of deliberate official action, national or international. In the gold market the operations of the gold pool have reinforced the effect of larger supplies of metal; while in the markets for the principal currencies the situation of better balance showed up in the generally firmer rates for the dollar, though there were occasions — for some European currencies as well as for the dollar — when official intervention helped importantly to maintain orderly conditions.

All in all, it can be said that the international monetary system — the object, during recent months, of special study by the member countries of the IMF's General Borrowing Arrangements (The Group of Ten) as well as by the staff of the Fund itself — worked not unsatisfactorily during the period under review. As to the future, the workings of the system will continue to depend primarily on the individual countries. International monetary co-operation, useful as it undoubtedly is, cannot relieve them of their own direct responsibilities.

V. THE EURO-CURRENCY MARKET.

Since the mid-1950s, and especially since Europe's return to external convertibility at the end of 1958, the foreign currency business of banks in Europe and elsewhere has undergone a very considerable expansion. Such business is not in itself new. But banks have been taking deposits and making loans in currencies other than their local currency on a much larger scale than before; and in the process there has also emerged an efficient interbank market in US dollar and other foreign currency deposits, helping to channel short-term funds internationally from lenders to borrowers. While this mass of operations has come to be called the Euro-dollar or, more broadly, the Euro-currency market, other countries, particularly Canada and Japan, play a prominent part in it.

Early on, the availability of European-owned dollars arising from the US balance-of-payments deficit was a factor in the development of the market. This factor was not essential, however. The basic causes were, first, the relaxation of exchange controls, which allowed business to be done in foreign currency, and, secondly, the existence of interest rate differentials, national and international, which gave the opportunity for such business to be profitable to both borrowers and lenders.

Problem of defining Euro-currencies.

There are several difficulties involved in trying to say precisely what a Euro-currency is. A Euro-dollar, for example, can be defined as a dollar that has been acquired by a bank outside the United States and used directly or after conversion into another currency for lending to a non-bank customer, perhaps after one or more redeposits from one bank to another. Three aspects of this definition may be expanded upon to clarify its meaning. In the first place, the definition implies that not all the dollar liabilities of the banks, nor all their dollar assets, can be regarded as Euro-dollars. On the liabilities side, banks may draw on lines of credit with their US correspondents for reasons quite unconnected with their Euro-dollar activities. Similarly, on the assets side, banks often place dollars in the US money market for reasons independent of Euro-dollar business. However, it is not possible to say that such liabilities or assets can be excluded as a class from the total of Euro-currency funds; according to circumstances they may or may not be connected with Euro-dollar activities.

Secondly, the dollar holdings of the banks may have been acquired not through dollar deposits but through conversion of deposits in another currency; likewise, the banks' dollar funds may be invested not only in dollar loans but in loans in other currencies obtained through conversion.

Gross short-term liabilities and assets in certain foreign currencies of commercial banks.¹
As at end-September 1963.

Countries	US dollars		Swiss francs		Sterling		Deutsche Mark		Dutch florins		Total	
	Liabil- ities	Assets	Liabil- ities	Assets	Liabil- ities	Assets	Liabil- ities	Assets	Liabil- ities	Assets	Liabil- ities	Assets
	in millions of US dollars											
Belgium-Luxemburg	360	480	130	130	30	60	70	100	50	40	640	810
France ²	650	670	190	180	250	260	120	140	60	70	1,270	1,320
Germany	270	570	40	70	40	80	///	///	10	10	360	730
Italy												
vis-à-vis non-residents	1,540	950	400	180	200	80	90	90	50	50	2,280	1,350
vis-à-vis non-bank residents	210	710	10	750	30	10	10	50	0	260	260	1,780
Netherlands												
vis-à-vis non-residents	270	440	30	30	40	100	20	150	///	///	360	720
vis-à-vis non-bank residents	20	10	0	—	10	10	20	0	///	///	50	20
Sweden	80	150	20	20	10	50	0	20	10	10	120	250
Switzerland	1,060	1,280	///	///	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	(1,060)	(1,280)
United Kingdom ³	3,200	3,000	200	200	///	///	200	200	50	50	3,650	3,450
Japan ³												
vis-à-vis non-residents	1,770	1,250	20	0	300	210	40	20	10	0	2,140	1,490
vis-à-vis non-bank residents	560	1,270	0	10	20	290	0	10	0	0	580	1,580
Total	9,990	10,790	1,040	1,570	930	1,150	570	780	240	490	12,770	14,780

¹ Vis-à-vis non-residents only, except for Italy, Netherlands and Japan. ² Vis-à-vis banks only. ³ Estimated.

Such possible discrepancies between dollar liabilities and assets would disappear if all foreign currencies were taken together — except when conversion from and to local currencies is involved.

Thirdly, it follows from the two preceding points that Euro-dollars cannot be defined exclusively either as dollar deposits in banks outside the United States or as dollar assets; both sides of the balance sheet must be considered.

It will be evident, therefore, that a precise statistical picture of the Euro-currency market is not feasible. The best that can be done is to present data on the banks' foreign currency liabilities and assets and then to arrive at some reasonable approximation of the most likely volume of funds in the Euro-currency market.

Present size of the market.

The preceding table of banks' short-term liabilities and assets in foreign currency at the end of September 1963 includes most of the countries whose commercial banks play a significant rôle in the Euro-currency market. The figures are gross in the sense that they include interbank deposits between countries; however, they do not include interbank deposits within each country or, for a majority of countries, liabilities and claims vis-à-vis non-bank residents. If estimates for these omissions were added, as well as for the other countries with banks in the market, particularly Canada, the gross total of foreign currency liabilities would exceed \$15 milliard (with assets rather larger).

This total, however, is not particularly significant, because of the duplication due to the large volume of interbank deposits. Interbank dealings are chiefly confined to the main western European countries and Canada ("the market area"), with London the largest individual centre. On the assumption that all inter-commercial-bank deposits in the market area can be excluded as duplication, the following figures have been obtained as a rough estimate of the net volume of the banks' foreign currency liabilities and assets.

These totals are underestimates, mainly because no allowance has been made for unavailable figures in respect of residents, and because the assumption that all inter-commercial-bank transactions in the market area represent duplication is an overstatement.

The table gives US dollar figures exclusive and inclusive of the banks' position vis-à-vis the United States, and similarly for the other currencies vis-à-vis their countries of issue. This means that the figures in the first column are too small as a measure of the Euro-currency phenomenon, since some transactions vis-à-vis the home countries of the respective currencies should be included. On the other hand, the second column is evidently too large, as it includes a sizable volume of transactions vis-à-vis these countries which

Estimated net volume of short-term foreign currency liabilities
and assets of commercial banks.

As at end-September 1963.

Items	Excluding items vis-à-vis countries of issue*	Including items vis-à-vis countries of issue*
	in millions of US dollars	
US dollars		
Liabilities	4,450	6,700
Assets	3,350	7,800
Net	— 1,100	+ 1,100
Other main currencies combined (£, Sw.fr., DM, Fl.)		
Liabilities	950	1,800
Assets	1,950	3,200
Net	+ 1,000	+ 1,400
Total above currencies		
Liabilities	5,400	8,500
Assets	5,300	11,000
Net	— 100	+ 2,500

* Items arising out of Japanese net dollar borrowings from the United States and net sterling borrowings from the United Kingdom are excluded.

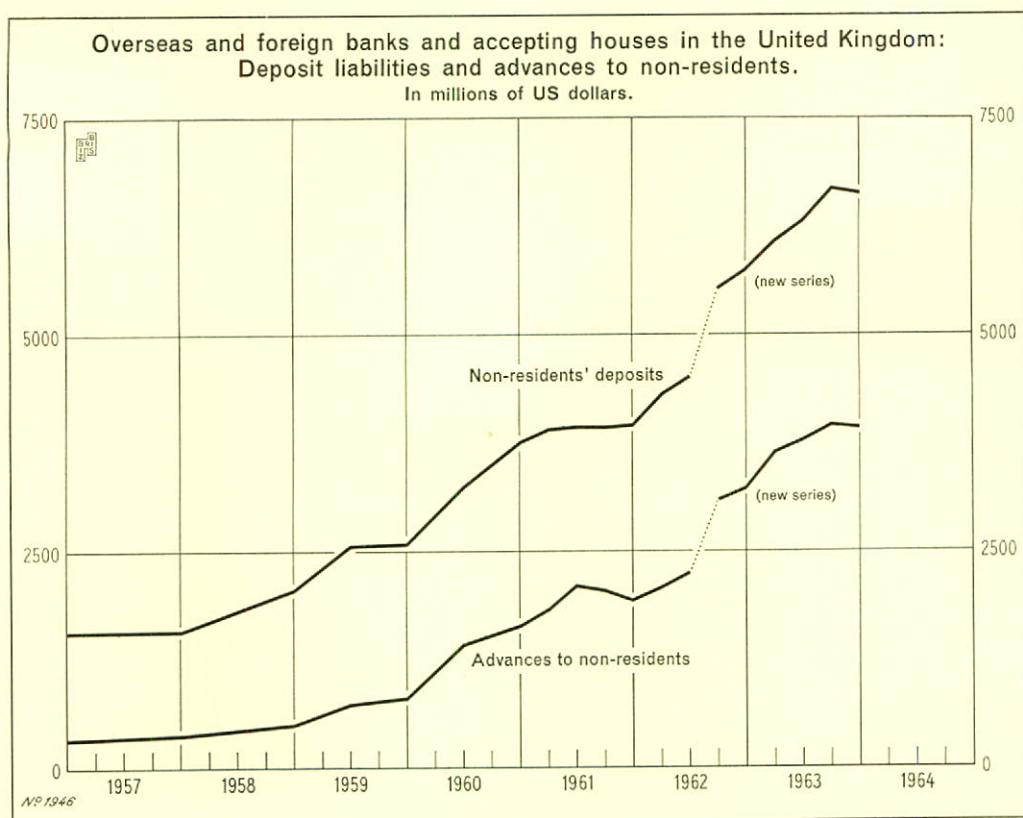
cannot be considered as part of the Euro-market. All in all, a figure of about \$7 milliard — of which some \$5 milliard actually in US dollars — would seem to be a reasonable estimate of the net volume of Euro-currencies at the end of September 1963.

Development of the market since the late 1950s.

Comparable statistical information on the Euro-currency market prior to 1963 is not available. There is, however, a useful indicator of its general growth since 1957, namely, the liabilities and claims on non-residents of the overseas and foreign banks and accepting houses in London. These institutions do the bulk of London's Euro-currency business and thus form the core of the whole market. Most of the striking growth of their deposit liabilities and advances to non-residents over the past six years, which is shown in the following graph, has been in foreign currencies, particularly dollars.

The statistical series up to September 1962 is not entirely comprehensive. However, making some allowance for the omissions, one may say that between 1957 and the last quarter of 1963 non-residents' deposits (including those in sterling) increased by over \$4,000 million. As the banks' liabilities in foreign currency were small in 1957, this figure corresponds fairly closely with the estimated \$3,650 million to which they had risen by September 1963.

Since UK banks' gross foreign currency liabilities to non-residents are only about half as large as the total net volume of Euro-currency funds, these data obviously do not allow any detailed conclusions to be drawn about the market as a whole. They suggest, however, that 1960 may have been its year of fastest growth, and that, after somewhat less rapid expansion during 1961-62, there was a certain re-acceleration until the autumn of 1963.



On this last point some independent confirmation is available: between March and September 1963 the net size of the Euro-market is estimated to have gone up by \$500 million, about half of this increase being accounted for by funds from outside the OECD area. Since then, the indications are that the market has not grown any further.

Sources and uses of Euro-currencies.

Of major interest is the question where the banks as a whole obtain their foreign currency balances and what they ultimately do with them. Given the preponderant rôle of the dollar in the Euro-market, the discussion may be concentrated primarily on that currency. The net sources and uses of funds, corresponding respectively to the liabilities and assets sides of the commercial-banking sector's balance sheet, can be classified in the following way.

Sources of dollar balances to commercial banks outside the United States:

1. Official institutions: central banks, governments, international organisations.
2. Commercial banks.
3. Non-banks: business and individuals.

Uses of dollar balances by commercial banks outside the United States:

1. Lending to non-banks in dollars.
2. Lending to non-banks after conversion into another foreign currency or into local currency.
3. Placing funds with US banks and in the US money market.

Sources of Euro-dollars. The flow of funds from official sources to the Euro-dollar market has taken place both directly and indirectly. Under the first head, some central banks in western Europe and elsewhere are believed to have placed dollars from their reserves — in a few cases perhaps as much as \$200 or 300 million — with banks outside the United States, presumably to obtain higher earnings on these funds. The central banks of the main financial centres have not made use of this investment outlet. There are indications that much of the money was placed in the Euro-market during 1960-61, when US money-market rates were low and the gap between them and Euro-dollar rates rather wide. Besides central banks, funds have been deposited in the Euro-market by international organisations, particularly the Bank for International Settlements. In addition, a sizable volume of eastern European countries' working balances in convertible currency is held with banks in western Europe.

So far as indirect official sources are concerned, certain central banks have facilitated the holding of dollars by their commercial banks — by way of swaps or deposits — for reasons connected with monetary policy. The commercial banks in turn have employed some of these dollars in the Euro-market. Thus, the Deutsche Bundesbank during the greater part of 1961 and 1962 helped the German banks to hold dollars by offering them special swap terms, the amount involved reaching a high of about \$1 milliard at the beginning of 1962; as the balance-of-payments position changed, these special terms were gradually withdrawn and by the end of the first quarter of 1963 the Bundesbank's swap commitment had fallen to zero. In March 1964, when the external surplus had again become large, the Bundesbank reintroduced its special swap arrangements; this time they were not available for periods of less than three months and banks making use of them were required to invest the dollars in US Treasury bills.

Again, the Italian Exchange Office has during the past four years held varying amounts of dollars — up to nearly \$1 milliard in 1962 — with the Italian banks, partly by way of swaps and partly as deposits. After the end of 1962, however, when the banks were permitted to be net borrowers abroad of foreign currency, they used part of the borrowings to reduce their foreign currency liabilities to the Exchange Office; these had accordingly declined to a much lower level by early 1964.

Elsewhere, the Japanese authorities have been holding substantial dollar balances with Japanese commercial banks in order to facilitate the expansion of bank lending. Finally, on a somewhat smaller scale, the Swiss National

Bank has periodically arranged forward cover to enable the Swiss commercial banks to hold dollars as part of its policy of offsetting unwanted inflows of liquid funds into Switzerland — for instance, after the sharp fall on Wall Street and the speculation against the Canadian dollar in the summer of 1962, and again following the outbreak of the Cuba crisis in the autumn.

It is evident that when the German, Italian or other authorities make dollars available to their commercial banks in this way, it may well be profitable for the banks to invest some of the funds in US money-market assets similar to those that the authorities would themselves have held had they retained the dollars in their own hands. In other words, the authorities' swap commitments with their own banks do not necessarily mean that an equivalent amount of dollars is being placed in the Euro-market. What can be said, however, is that this supply of official funds to the banks, and hence indirectly also to the Euro-market, has declined, and that official sources altogether have therefore become somewhat less prominent, relatively and absolutely, than they were two or three years ago. They may now amount to between \$1.5 and 2 milliard.

As for commercial banks, banks outside the United States — for instance in Germany and the Netherlands — have contributed to the net Euro-dollar supply with dollars acquired in the market against local currency from, for example, resident exporters. Banks in the United States may supply the Euro-dollar market by placing deposits with banks overseas, largely their own foreign branches, or by granting credit to overseas correspondents. The latter would not ordinarily involve the Euro-currency market. But it is impossible to draw a precise boundary, since European banks may draw on credit lines in New York to bridge temporary liquidity shortages in their Euro-dollar position.

The quantitative significance of commercial banks as an original source of supply is thus particularly hard to estimate. So far as Euro-dollars are concerned, however, the banks' contribution appears to have been smaller than those of non-banks and official institutions.

Non-banks have now probably become the most important source of Euro-dollar funds. Business and individuals have been choosing for reasons of both profitability and convenience to hold growing amounts of dollars outside rather than inside the United States. In addition, the existence of the Euro-dollar market has constituted an incentive for non-American firms engaged in foreign trade to retain larger dollar working balances altogether, thus saving the cost of conversion to and from local currency.

The dollar being a widely used international trading currency, it is to be expected that non-US firms involved in international trade should hold part of their liquidity in dollar form. It is probable, however, although detailed evidence is limited, that the rôle of American firms in supplying funds to the Euro-dollar market is larger and that it has increased appreciably over the past two or three years. Corporations resident in the United States have

placed some dollars directly in Europe, and a certain amount has been reaching European banks via Canada. More significant, however, has been the activity of overseas affiliates of US firms, partly in Europe but more especially in Latin America and the Middle East. The movement of US liquid funds to banks abroad has, of course, been reflected in the deficit shown by US balance-of-payments statistics for recent years.

In summary, all the sources listed have helped to supply the Euro-dollar market, but over the past two years there has been some shift of accent from central-bank to non-bank sources. Geographically, official institutions supplying funds to the Euro-dollar market have been located mostly in Europe (including eastern Europe), whereas non-bank funds have to a larger extent come from other regions.

Sources of other Euro-currencies. Much less can be said about currencies other than the dollar. So far as sterling is concerned, the main sources of funds to banks in Paris (the centre of Euro-sterling operations) and elsewhere appear to lie outside the OECD area. This would be in line with the fact that the importance of sterling as a trading and reserve currency is also greatest in other regions. For Swiss francs, Dutch florins and Deutsche Mark, however, the sources are to a large extent European, and notably commercial banks. On the one hand, Swiss, Dutch and German banks have given loans or deposits in their own currencies to banks abroad. On the other hand, banks have obtained foreign currencies by means of swaps; Dutch banks, for instance, appear to have moved into Deutsche Mark this way, while Italian banks have swapped dollars and sterling into Swiss francs and florins.

Uses of Euro-currencies. Final uses of Euro-currencies involve lending to a non-bank borrower. This covers the first two types of use in the schema on page 132. However, while the market is dependent on profitable final uses of this kind, banks also employ dollars (and other currencies) in money-market assets in order to obtain greater scope and flexibility in their operations. A special use of this type occurs when overseas branches of American banks channel dollar deposits back to their head office in the United States — which they have done on a rather large scale.

Final users of Euro-currencies employ them mostly to finance foreign trade. In the case of Euro-dollars, this applies not only to the many borrowers outside the United States who use the dollar as a trading currency but also to some of the US concerns that have been borrowing in the Euro-market rather than in New York, e.g. cotton and wheat exporters. But if interest rates, or shortage of domestic credit, are such as to give an incentive for firms to borrow foreign rather than local currency, it becomes impossible to specify what transactions the funds are really financing. In addition, some lending of Euro-currencies has clearly had nothing to do with international trade; for instance, some US security dealers and brokers have been borrowing in the Euro-dollar market instead of from banks in New York. Incidentally, European branches of US banks have recently been shifting less of their Euro-dollar

deposits back to head office than a few years ago and have been lending more to local borrowers, particularly foreign branches and affiliates of US firms.

Over 30 per cent. of recent final borrowers of Euro-dollars (considerably less in the case of other Euro-currencies) appear to have been resident outside western Europe and North America. Little more can be said about the geographical distribution in general. But further light is shed on the question of where Euro-currency funds have been flowing by the net foreign borrowing that has occurred at different times in four particular countries — the United Kingdom, Japan, Italy and Belgium.

The United Kingdom has been a net borrower of Euro-currencies since the early stages of the market's development. Net borrowing has resulted from banks converting into sterling (on a covered basis) for the purpose of short-term lending to certain UK borrowers, notably local authorities and finance houses. The amount converted has fluctuated but has remained modest in relation to the banks' total foreign currency liabilities, being of the order of a few hundred million dollars. During 1963 this type of business became less attractive and tended to decline.

In Japan Euro-currencies made up a part of the substantial foreign borrowing by Japanese banks in 1961 and have continued to be a source of credit, particularly for the financing of Japanese foreign trade. The amounts involved appear to have run into several hundred million dollars. In addition, the Japanese banks have used the dollars deposited with them by the Japanese authorities to make loans to customers.

In the case of Italy the banks' net indebtedness to non-residents rose between November 1962 and September 1963 by about \$1 milliard. The greater part of this was in Euro-currencies and the corresponding assets of the banks are foreign currency claims on residents. These claims in 1963 constituted the largest single item on the uses side of the Euro-market. At one time more than half of them were in Swiss francs; besides Swiss francs and dollars there has also been sizable lending in Dutch florins and Deutsche Mark.

In Belgium the Treasury during 1960-61 and again in 1963 financed part of the budget deficit by running a floating debt in foreign exchange, which at the end of 1963 totalled over \$200 million. In addition, the banks have financed holdings of Treasury paper denominated in Belgian francs by borrowing foreign currencies abroad and swapping. A part of these various funds has come from the Euro-currency market. During 1963 the Belgian authorities also obtained funds from the Euro-dollar market at medium term, two three-year loans of \$20 million having been floated in London.

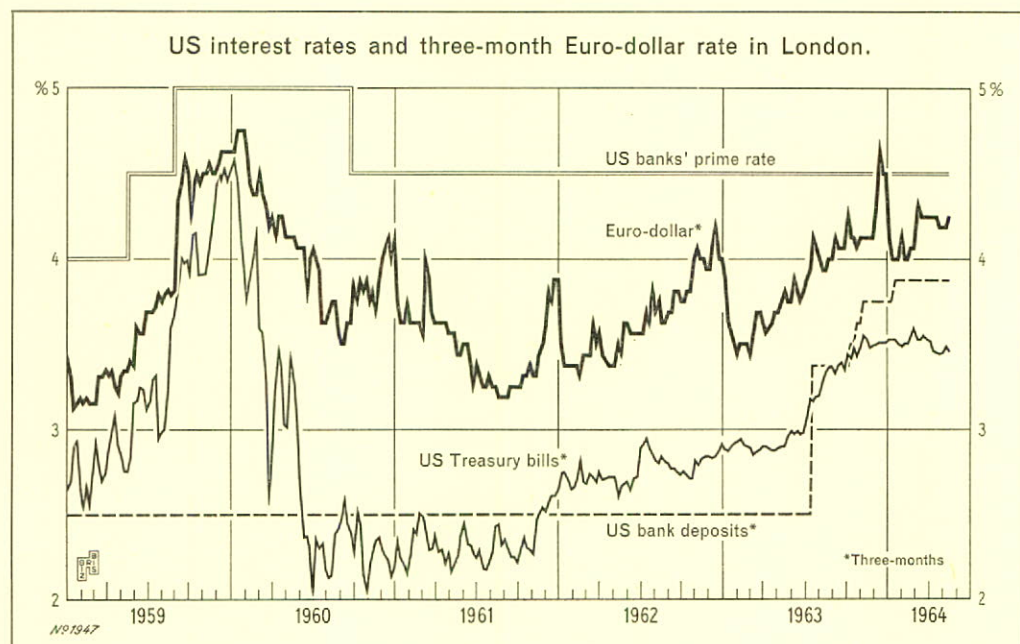
Euro-dollar interest rates.

While the cost of credit is of prime significance in any financial market, for Euro-currencies its importance is critical. In effect, the opportunity to operate profitably inside existing interest rate spreads, national and international,

has been the basic incentive for the banks to develop the Euro-currency business.

So far as Euro-dollars and their sources are concerned, some dollars have evidently been deposited outside the United States for reasons other than interest rate inducements — such as convenience, fiscal advantages, and so forth. But for the most part banks have been able to attract dollar deposits by paying rates higher than those on comparable placements in New York. When it comes to the profitable employment of these funds, the banks have been making dollar advances to final customers at inclusive rates competitive with those charged by New York banks or — in the case of borrowers who do not have access to the New York market — with lending rates in local currency. Alternatively, where rate differentials (and exchange control regulations) have been favourable, banks have swapped dollars into some other currency, possibly but not necessarily local currency, before lending to a non-bank customer. In fact, some banks offer customers a variety of currencies at different rates of interest depending on the cost of forward cover.

The ceiling on deposit rates in the United States fixed under Regulation Q was a factor which encouraged the growth of dollar deposits in foreign banks. Moreover, foreign banks pay interest on call and on the shortest time deposits, which is illegal in the United States. Apart from this, however, it is a fact that Euro-currency operations are considered a rather marginal type of business by many banks and are conducted on a narrower spread between borrowing and lending rates than that prevailing on banks' traditional business in their own currency. This is particularly the case with the large-scale transactions that take place in the interbank market.



This new element of international competition in banking has had a significant influence on the development of interest rates in various countries. In Europe, notably in Italy, there appears to have been downward pressure on banks' lending rates.

In the United States the maximum rate payable under Regulation Q on time deposits at three months or longer was raised in July 1963 to 4 per cent. New York banks have been paying 4 per cent. for six-month money, which, if placed in the form of deposit certificates, is liquid for the holder. Treasury bill rates in New York have also gone up, though to a somewhat lesser extent. At the same time, however, there has been no general increase in New York banks' lending rates; in other words, the spread between borrowing and lending rates in New York has narrowed. Consequently, while the rate for three-month Euro-dollar deposits is now above 4 per cent., the differentials between Euro-dollar and New York rates have been appreciably smaller for the past few months than they were a year or two ago.

Other Euro-currency interest rates.

Interest rates on deposits in other Euro-currencies tend to correspond to the net yield obtainable from a swap into dollars. For example, if the three-month forward rate on the Deutsche Mark or the Swiss franc against the dollar is at an annual premium of $\frac{1}{2}$ per cent., then the rate of interest on three-month Deutsche Mark or Swiss franc deposits in London will tend to be around $\frac{1}{2}$ per cent. below that on three-month dollar deposits. In effect, the market deals in liquid funds, however denominated, and interest rates on different currencies must reflect the cost of forward cover.

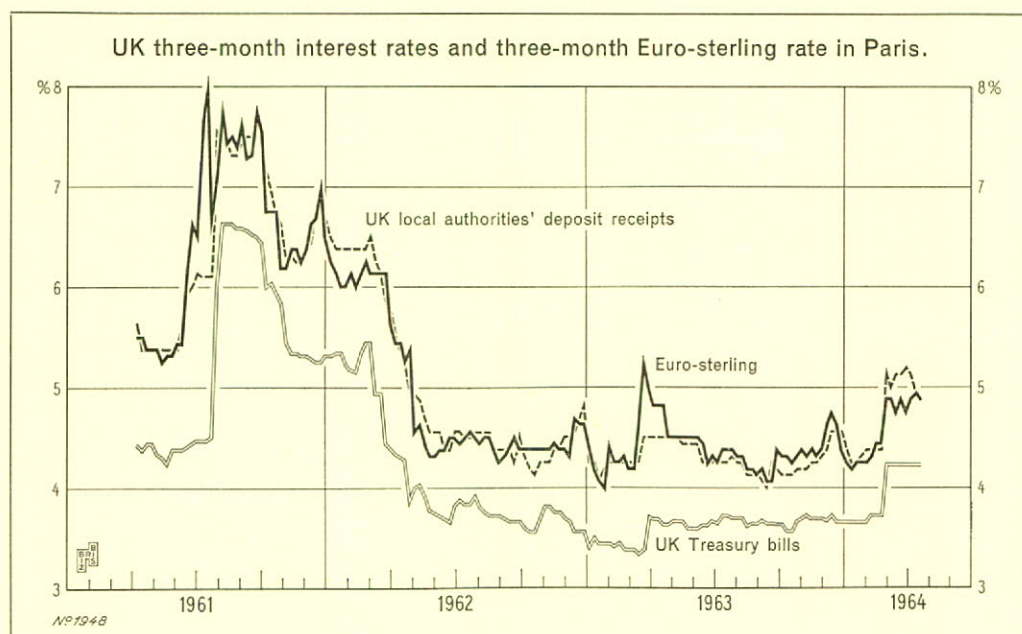
An illustration of how Euro-rates may be independent of domestic money-market rates is provided by the Euro-Deutsche Mark during the years 1960-61. Over the first three quarters of 1960 interest rates on the German money market rose quite sharply (the discount rate being put up from 4 to 5 per cent.); the three-month Euro-Deutsche Mark rate in London, however, declined from a high of $4\frac{1}{2}$ per cent. at the start of the year to around $2\frac{1}{2}$ per cent. in the autumn, because dollar interest rates both in New York and in London fell and at the same time the forward Deutsche Mark was strengthening, while the German money market was not freely accessible to non-residents.

After mid-1961, at a time when interest rates in Germany were declining gently, Euro-rates for the Deutsche Mark (together with those for the Swiss franc and the florin) began to increase and in fact went up by two full percentage points, from 1 to 3 per cent. This happened partly because Euro-dollar rates turned round and started to rise — the swap into sterling having become more attractive since the increase in UK Bank rate — but mainly because the forward discount on the dollar against the continental currencies was narrowed, in the case of the Mark from $2\frac{1}{2}$ to just over $\frac{1}{2}$ per cent.

In the case of sterling the UK money market offers a particularly wide range of investment possibilities. Hence, Euro-sterling rates are not determined

simply by Euro-dollar rates and the cost of the sterling-dollar swap. This is, no doubt, the most important factor. But in addition Euro-sterling rates must be competitive with rates obtainable on comparable investments in the United Kingdom; and the cost of the swap will in turn be influenced by whatever these rates are. The causation thus runs both ways. The graph shows how very closely the three-month Euro-sterling rate and the rate for three-month local-authority money in the United Kingdom have moved together. The relation between them is twofold: they are directly competitive with each other (for foreign holders of sterling) and they are linked through the cost of the dollar swap.

The Euro-sterling rate has been appreciably above the local-authority loan rate only at times of speculation against sterling — July 1961 and part of the first quarter of 1963.



Exchange regulations, banking controls and the Euro-currency market.

Apart from interest rate differentials, the development of Euro-currency activity has been dependent upon banks having a considerable measure of freedom to do business in foreign currencies. Such freedom has been widely granted over the past decade, generally before western Europe's return to external convertibility at the end of 1958. In most European countries, however, certain exchange restrictions on both banks and non-banks have been retained, and other controls have also been applied to influence the banks' net position vis-à-vis non-residents.

In the United Kingdom the banks' foreign currency activity received an important stimulus in the late summer of 1957, when temporary restrictions

were placed on overseas lending in sterling, particularly for transactions between non-residents. Foreign currency business was developed chiefly by the overseas banks and accepting houses, which have traditionally played the major rôle in the City's international banking business. It is perhaps also relevant that these banks are not subject to the liquidity requirements which apply to the London clearing banks.

As already mentioned, UK net borrowing of Euro-currencies has resulted from swapping into sterling by banks for lending to local authorities and others. UK non-bank residents may not borrow abroad directly without authorisation. It was announced in the autumn of 1963 that local authorities are to be able in future to obtain part of their financing requirements from the Treasury and that there is to be a ceiling on the proportion of their outstanding debt at less than one year; this will tend to narrow the scope for future expansion of this type of short-term lending business.

In Switzerland an incentive to foreign currency deposits was given by the gentleman's agreement between the Swiss National Bank and the banks, dating originally from August 1960, which forbade the payment of interest on new non-residents' deposits in Swiss francs. This measure also tended to stimulate Euro-Swiss franc business abroad. In the spring of 1964 the government's anti-inflation programme included a measure requiring the banks to place the counterpart of new non-residents' Swiss franc deposits abroad in foreign currency or to sterilise it at the central bank.

In Germany and the Netherlands banks are not legally restricted in the conduct of their foreign business. On the other hand, measures of official monetary policy have at different times in the last few years led the banks to put funds in the Euro-market (and also in the United States). From the end of 1959 until about mid-1962 the German authorities were anxious to encourage the outflow and discourage the inflow of liquid funds, and since early 1964 policy has again been directed to this objective. Besides its special swap arrangements, the Bundesbank has employed two main kinds of measures: first, a prohibition of interest payments on non-residents' deposits; and secondly, increases in the minimum reserves that banks are required to hold against foreign liabilities.

In the Netherlands the authorities in 1961 and again in 1963-64 restrained domestic lending by putting a ceiling on the desirable monthly expansion of total bank credit to Dutch residents. If this limit is exceeded, individual banks are obliged to hold non-interest-bearing balances equal to their particular excess with the central bank. This encourages the banks to maintain liquidity abroad.

In Italy the banks were required to balance their foreign currency position vis-à-vis non-residents as from January 1961, but this regulation was lifted in November 1962. The banks may not ordinarily convert foreign currency into lire; and non-banks are not free to borrow foreign currency from abroad directly. Also relevant in this context is the fact that Italian

banks' minimum reserve requirements do not apply to foreign currency liabilities.

Finally, in France the present state of exchange regulations is broadly similar to what it is in Italy. Banks — but not non-banks — may be net borrowers of foreign exchange abroad, but may not convert such borrowings into domestic currency. Foreign exchange may be advanced to residents for foreign trade finance; there has, however, been no unusual expansion of such lending in recent years. The French system of minimum reserves — the "coefficient de trésorerie" — applies to all the banks' liabilities. In April 1963 the French authorities followed the example of Switzerland and Germany by forbidding the payment of interest on non-residents' French franc deposits; but Euro-franc activity has so far remained very limited.

Euro-dollars and the US balance of payments.

At first, the basic deficit in the US balance of payments contributed to the development of the Euro-dollar market by putting large amounts of dollars into foreign hands. At a later stage, however, the market directly or indirectly attracted additional resources from US firms and their foreign affiliates. This gave rise (in so far as it did not finance additional US exports) to an increase in US liquid liabilities to foreigners, which under the existing statistical presentation means an increase in the US balance-of-payments deficit. It is not clear, however, to what extent there was an additional external financing problem for the United States.

To begin with, when US funds are placed in the Euro-dollar market, the resulting increase in US liquid liabilities is merely the counterpart of an increase in US liquid claims. So long as the dollars stay in the market, that is to say, so long as the US liability is to a non-official foreigner, the US gold stock cannot be affected. It obviously may be affected, however, if the dollars end up in some other country's official reserves. On the other hand, the Euro-market also facilitates the employment of foreign-owned dollars and thereby tends to keep down the amount of such dollars that are sold to the authorities. In addition, to some extent the Euro-dollar market has simply taken over the financing of international trade from New York banks and to that extent the US balance of payments is not affected.

Thus, it is not possible to say what has been the net effect of these factors. The Euro-dollar market may have aggravated the US balance-of-payments problem; but its influence cannot have been a major one relative to the problem that existed in any case.

* * *

The Euro-currency market has developed rapidly in the space of a few years and is today a substantial source of international credit. It has taken in its stride major shifts in the sources and uses of its funds. It brings many

lenders and borrowers together on more favourable terms to both than would otherwise be the case, and the impetus which it has given towards equalisation of money rates has been useful also in the broader context of international monetary equilibrium.

At the same time certain criticisms have been made of the market, in particular that it hampers efforts to control inflation and that it leads to unsound banking practices which could prove dangerous in the event of a large withdrawal of funds by depositors. So far as inflation is concerned, borrowing in the Euro-market by a country may enable the private sector to circumvent a domestic credit squeeze, or may allow the authorities to delay corrective action against an external deficit. As to unsound banking, some banks may have regarded Euro-currencies essentially as foreign exchange business and may not always have given sufficient study to the status and credit-worthiness of individual borrowers. A few bad debts encountered by certain banks in their foreign currency business in 1963 focused attention on this aspect. In addition, it is claimed that long chains of interbank transactions may result in excessive stretching of the periods for which ultimate borrowers obtain funds as compared with the maturities for which original depositors place them, partly because narrow interest rate spreads may push the banks to seek higher yields through longer-term lending.

While such arguments have their element of truth, this may easily be exaggerated. In particular, there is no evidence that Euro-currency business has occasioned widespread departures from the canons of prudent banking. Moreover, arguments about the control of inflation and the possibility of bad debts would for the most part apply not to Euro-currency lending as such but to international credit in general. Some of the comment which the market has attracted no doubt reflects the element of novelty as well as the growing prominence of Euro-currencies in short-term capital movements during recent years. So far, in fact, the market does not seem to have given rise to policy problems of a different order from those of other movements of short-term funds.

VI. THE EUROPEAN MONETARY AGREEMENT.

The European Monetary Agreement came into force on 27th December 1958. It is operated within the framework of the Organisation for Economic Co-operation and Development, which succeeded in September 1961 the Organisation for European Economic Co-operation. The Agreement has two principal features: the European Fund and the Multilateral System of Settlements.

In carrying out its review of the Agreement prescribed by Article 32, the Board of Management felt that it would be inopportune to make substantial changes in the EMA at the present time. Following recommendations made by the Board, the Council decided at the end of 1963 to prolong the Agreement until 31st December 1964 and to make a further review of the Agreement during 1964.

The few changes in the conditions under which the Agreement is operated in 1964 are described in the first part of this chapter; the second and third parts deal with the operations and management of the European Fund and Multilateral System of Settlements up to March 1964.

1. Continuation of the Agreement.

The only change which took place in the provisions of the Agreement on the occasion of its renewal concerns the number of the members of the Board, which was increased from seven to eight; a consequential modification of the majority rule was made to the effect that decisions will be taken by a majority of five members, or of four including the Chairman.

Shortly after the renewal of the Agreement the Council, upon the recommendation of the Board of Management, introduced a new method of calculating the half-yearly interest payments on contributions. The new method, the adoption of which entailed no change in the text of the Agreement, was applied for the first time to the interest payment in respect of the second half of 1963. Under the former system interest payments were based on a uniform rate per annum for the half-year in question. This method had the disadvantage that unequal parts of the various countries' total share were paid whenever their relative capital participation fluctuated, for instance as a result of adjustments made to contributions or of the call-up of a contribution which had previously been deferred. In order to avoid these inconsistencies in future the half-yearly interest payments will be determined in such a way that the cumulative amount of interest paid to each country represents a uniform percentage of its total income share if the Fund were liquidated at the end of the respective half-year.

2. Operations under the Agreement.

European Fund.

A. GRANTING AND UTILISATION OF CREDITS. A summary of the credits granted from the European Fund, showing interest rates and service charges, is contained in the following table. All amounts actually drawn are paid out and are repayable in gold.

EMA: Credits granted from the European Fund.

	Amount granted	Period available	Interest on amounts drawn	Service charge on amounts undrawn
	in millions of units of account		in percentages per annum	
Credits repaid or cancelled				
Greece	15.0	16th February 1959 to 16th December 1959	3.50	0.25
Turkey (1st credit)	21.5	16th February 1959 to 15th February 1961	3.50	0.25
Spain	75.0	1st August 1959 to 16th February 1961	3.75	0.25
	25.0	15th February 1960 to 9th August 1961		
Iceland (1st credit)	7.0	20th February 1960 to 19th February 1962	4.00	0.25
	5.0	1st August 1960 to 1st April 1962		
Turkey (2nd credit)	15.0	1st January 1961 to 31st December 1962	3.75	0.25
	20.0	15th February 1961 to 14th February 1963		
Iceland (2nd credit)	15.0	1st July 1961 to 30th June 1963	3.75	0.25
	5.0	1st April 1962 to 1st April 1963		
Credits available	20.0	1st April 1962 to 31st March 1965	3.75	0.25
	25.0	1st August 1962 to 31st July 1965		
Turkey (4th credit)	35.0	15th March 1963 to dates below*	3.50	0.25
	15.0	30th June 1963 to dates below*		
Credits granted and not available at end of March 1964				
Turkey (5th credit)	20.0	10th April 1964 to dates below*	3.00	0.25

* The fourth credit is repayable as follows: 10 million on 31st October 1964, 15 million on 15th March 1966, 15 million on 31st October 1966 and 10 million on 15th March 1967. The fifth credit is repayable in four instalments of 5 million each, falling due on 30th November 1964, 31st December 1964, 31st January 1965 and 28th February 1965.

At the end of March 1963 credits totalling \$100 million* were available to two countries; of this total \$95 million had been drawn.

* For convenience the dollar sign (\$) is used throughout the text of this chapter, whether the amount referred to is in US dollars, gold or EMA units of account.

The credit of \$5 million granted to Iceland from 1st April 1962 was cancelled with effect from 1st April 1963; no drawings were made on this credit.

Turkey repaid to the European Fund at maturity the third and last tranche of \$15 million of its second credit on 30th June 1963. On the same date Turkey drew the second tranche of \$15 million of the fourth credit, leaving the total amount of credit drawn and outstanding at \$95 million, at which level it has remained since March 1963. The third credit of \$45 million, granted in March 1962, was made available in two tranches, each for a period of three years. The first tranche (\$20 million available from 1st April 1962) was drawn in full on 12th June 1962, and the second tranche (\$25 million available from 1st August 1962) was drawn in full on 9th October 1962.

EMA: Utilisation of credits granted.

After operations for month	Greece	Turkey		Spain		Iceland		Totals		
	Available and undrawn	Available and undrawn	Drawings outstanding	Available and undrawn	Drawings outstanding	Available and undrawn	Drawings outstanding	Available and undrawn	Drawings outstanding	Total credit granted
in millions of units of account										
1959										
February . .	15.0	21.5	—	—	—	—	—	36.5	—	36.5
June	15.0	20.5	1.0	—	—	—	—	35.5	1.0	36.5
July	15.0	19.5	2.0	51.0	24.0	—	—	85.5	26.0	111.5
August . . .	15.0	13.5	8.0	51.0	24.0	—	—	79.5	32.0	111.5
October . . .	15.0	2.5	19.0	51.0	24.0	—	—	68.5	43.0	111.5
November . .	15.0	1.5	20.0	51.0	24.0	—	—	67.5	44.0	111.5
December . .	—	0.5	21.0	51.0	24.0	—	—	51.5	45.0	96.5
1960										
February . .	—	0.5	21.0	76.0	24.0	2.0	5.0	78.5	50.0	128.5
March	—	—	21.5	76.0	24.0	2.0	5.0	78.0	50.5	128.5
June	—	—	21.5	76.0	24.0	—	7.0	76.0	52.5	128.5
July	—	—	21.5	76.0	24.0	5.0	7.0	81.0	52.5	133.5
December . .	—	15.0	21.5	76.0	24.0	5.0	7.0	96.0	52.5	148.5
1961										
January . . .	—	15.0	21.5	100.0	—	5.0	7.0	120.0	28.5	148.5
February . .	—	13.0	22.0	25.0	—	5.0	7.0	43.0	29.0	72.0
June	—	15.0	35.0	25.0	—	5.0	7.0	45.0	42.0	87.0
July	—	—	50.0	25.0	—	5.0	7.0	30.0	57.0	87.0
August . . .	—	—	50.0	—	—	5.0	7.0	5.0	57.0	62.0
December . .	—	—	50.0	—	—	7.0	5.0	7.0	55.0	62.0
1962										
January . . .	—	—	50.0	—	—	9.5	2.5	9.5	52.5	62.0
February . .	—	—	50.0	—	—	5.0	—	5.0	50.0	55.0
March	—	20.0	50.0	—	—	5.0	—	25.0	50.0	75.0
June	—	—	70.0	—	—	5.0	—	5.0	70.0	75.0
July	—	25.0	70.0	—	—	5.0	—	30.0	70.0	100.0
October . . .	—	—	95.0	—	—	5.0	—	5.0	95.0	100.0
December . .	—	—	80.0	—	—	5.0	—	5.0	80.0	85.0
1963										
February . .	—	—	60.0	—	—	5.0	—	5.0	60.0	65.0
March	—	—	95.0	—	—	—	—	—	95.0	95.0
1964										
March	—	—	95.0	—	—	—	—	—	95.0	95.0

The fourth credit of \$50 million, granted in March 1963, was also made available in two tranches: the first of \$35 million from 15th March 1963, drawn in full on 21st March 1963, and the second of \$15 million from 30th June 1963, drawn in full on the same date. The fourth credit is to be repaid in four instalments: \$10 million on 31st October 1964, \$15 million each on 15th March and 31st October 1966 and \$10 million on 15th March 1967. Except for the repayment of \$10 million to be made in October 1964, each tranche is available for drawings for three years.

On the various credits granted from the European Fund, between June 1959 (when the first drawing was made) and March 1964 there were eighteen drawings totalling \$199.5 million; of this amount \$104.5 million had been repaid. The net amount drawn and outstanding after the operations for March 1964 was, therefore, \$95.0 million. A new credit of \$20 million was granted to Turkey with effect from 10th April 1964.

The table on the utilisation of credits granted shows the position after the operations for each month in which changes occurred.

B. CALLING-UP OF THE CAPITAL. Since January 1962 the Agent has no longer been required automatically to call up the capital of the European Fund as soon as the liquid assets fall below \$100 million. The call-up is now subject to variation at the discretion of the Board of Management.

The call-up mechanism was first brought into operation on 3rd August 1959 and has been used three times since then, most recently on 7th March 1960; a total of \$38 million has been called up from member countries with non-deferred contributions.

Multilateral System of Settlements.

In five and a quarter years payments to or by the European Fund in respect of the multilateral settlements have totalled \$37.1 million. The settlement for each month takes place on the fifth working day of the following month.

No amounts of interim finance have been brought into the settlements, since all amounts drawn have been repaid by the end of the month. Only one country has made extensive use of the right to obtain interim finance from other members and this country last used the facility in March 1963. The current rate of interest charged on drawings is 3 per cent. (until February 1960 it was 2½ per cent. and before July 1959 2 per cent.).

The balances reported for settlement, with the three exceptions noted below, have arisen entirely under bilateral payments agreements between member countries; of the seven agreements originally notified only one remained in force in March 1964.

On three occasions balances on accounts between central banks have been brought into the settlements. Such balances may be notified by their owner either at the end of the month or — as was the case in these three instances — when a change occurs in the buying or selling rates for the currency in which the account is denominated. The balances in question, reported as a result of modifications in the Swedish exchange margins in November 1959 and the Icelandic devaluations of February 1960 and August 1961, were settled at the old selling rates of the two currencies for the US dollar; in each case the amounts were small.

EMA: Payments made under the Multilateral System of Settlements,
January 1959 to March 1964.

Accounting period	Payments made by the Fund to (+) or to the Fund by (—)									Total payments by and to the Fund
	Austria	Denmark	Greece	Iceland	Italy	Netherlands	Norway	Sweden	Turkey	
	in thousands of US dollars									
1959 first financial year	+ 10,527	+ 10	—	—	+ 243	+ 1,400	+ 44	—	+ 2,350	14,574
	—	— 67	— 10,707	—	—	— 1,378	— 876	— 243	— 1,304	
1960 second financial year	+ 8,676	+ 207	—	—	—	—	+ 343	—	+ 2,202	11,428
	—	— 83	— 9,283	— 1	—	—	— 1,045	—	— 1,016	
1961 third financial year	+ 5,880	+ 23	+ 262	—	—	—	+ 274	—	+ 654	7,093
	—	—	— 4,924	— 23	—	—	— 251	—	— 1,895	
1962 fourth financial year	—	—	—	—	—	—	+ 97	—	+ 2,539	2,636
	—	—	— 2,314	—	—	—	— 323	—	—	
1963										
January . . .	—	—	— 4	—	—	—	+ 4	—	— 0	4
February . . .	—	—	+ 116	—	—	—	— 10	—	— 105	116
March	—	—	+ 18	—	—	—	+ 19	—	— 37	37
April	—	—	— 65	—	—	—	+ 108	—	— 42	108
May	—	—	— 55	—	—	—	—	—	+ 55	55
June	—	—	— 35	—	—	—	—	—	+ 35	35
July	—	—	+ 152	—	—	—	—	—	— 152	152
August	—	—	— 32	—	—	—	—	—	+ 32	32
September . .	—	—	— 89	—	—	—	—	—	+ 89	89
October	—	—	— 158	—	—	—	—	—	+ 158	158
November . . .	—	—	— 211	—	—	—	—	—	+ 211	211
December . . .	—	—	— 88	—	—	—	—	—	+ 88	88
1964										
January	—	—	— 133	—	—	—	—	—	+ 133	133
February . . .	—	—	— 121	—	—	—	—	—	+ 121	121
March	—	—	— 57	—	—	—	—	—	+ 57	57
Total payments by the Fund (+)	+ 25,083	+ 240	+ 547	—	+ 243	+ 1,400	+ 889	—	+ 8,723	37,126
or to the Fund (—)	—	— 150	— 28,274	— 24	—	— 1,378	— 2,505	— 243	— 4,552	
Net amount of settlements	+ 25,083	+ 90	— 27,727	— 24	+ 243	+ 22	— 1,616	— 243	+ 4,171	—

3. Management of the European Fund and the Multilateral System of Settlements.

The Board of Management of EMA supervises the execution of the Agreement and advises the Council of OECD on all related matters. The Board also follows closely the general economic and financial situation of member countries on the basis of reports made by the Secretariat, by the various committees of the Organisation and, on occasion, by special missions. In discharging these functions the Board meets when necessary, recently about seven times a year. M. Hay, who succeeded Dr. von Mangoldt in January 1962, remains Chairman of the Board.

The Agent presents monthly reports on the operations and the investments of the European Fund and on the working of the System of Settlements; the Bank for International Settlements also provides the Board with monthly material on the international gold, foreign exchange and capital markets and on the evolution of central-bank reserves in relation to balances of payments.

The operations of the Fund as described in the previous pages are reflected in the following summary of the Statement of Account.

Credits and claims outstanding, which at the opening of business amounted to \$35 million representing loans to Norway and Turkey transferred from EPU, stood at \$87.8 million at the end of 1961 as a result of drawings

EMA: Summary of the Statement of Account of the European Fund.

After operations for month	Assets				Total of Statement	Liabilities	
	Liquid resources	US Treasury account	Uncalled capital of member countries	Credits and claims out- standing		Capital Fund	Income and expendi- ture account
in millions of units of account							
Opening	113.0	123.5	328.4	35.0	600.0	600.0	—
1959 December	104.4	123.5	302.9	80.0	610.9	607.5	3.4
1960 December	106.4	123.5	297.9	87.5	615.3	607.5	7.8
1961 December	109.2	123.5	297.9	87.8	618.4	607.5	10.9
1962 December	90.4	123.5	297.9	110.5	622.3	607.5	14.8
1963 January	90.5	123.5	297.9	110.5	622.4	607.5	14.9
February	110.1	123.5	297.9	90.5	622.0	607.5	14.5
March	75.2	123.5	297.9	125.5	622.1	607.5	14.6
April	75.3	123.5	297.9	125.5	622.2	607.5	14.7
May	75.4	123.5	297.9	125.5	622.3	607.5	14.8
June	76.9	123.5	297.9	125.5	623.8	607.5	16.3
July	76.6	123.5	297.9	125.5	623.5	607.5	16.0
August	76.7	123.5	297.9	125.5	623.6	607.5	16.1
September	76.8	123.5	297.9	125.5	623.7	607.5	16.2
October	76.9	123.5	297.9	125.5	623.8	607.5	16.3
November	76.9	123.5	297.9	125.5	623.8	607.5	16.3
December	82.1	123.5	297.9	123.1	626.6	607.5	19.1
1964 January	82.2	123.5	297.9	123.1	626.7	607.5	19.2
February	82.1	123.5	297.9	123.1	626.6	607.5	19.1
March	81.6	123.5	297.9	123.1	626.2	607.5	18.7

on credits granted. The total declined slightly following repayments by Iceland in January and February 1962 but later rose to a high point of \$127.8 million in October 1962 after Turkey drew the full amount of its third credit. Repayments by Turkey of the second credit and the second amortisation payment by Norway and Turkey in respect of the loans mentioned above reduced the total again, but the drawing by Turkey of the first tranche of the fourth credit brought the total at end-March 1963 to \$125.5 million. The drawing by Turkey of the second tranche of the fourth credit in June 1963 merely replaced the maturing third tranche of \$15 million of the second credit, and the total at end-March 1964 after the third amortisation payment by Norway and Turkey was \$123.1 million.

Drawings were met in the first place out of the liquid resources transferred from EPU until these were brought down to approximately \$100 million in July 1959. From then until January 1962 this level was maintained through the calling-up of member countries' contributions, as recorded by the decline in uncalled capital. Since that date, the call-up being no longer automatic, the liquid resources have been allowed to fall below the level of \$100 million.

In the course of the year to March 1964 the increase in the total of the Statement by \$4.1 million was entirely due to a further rise in undistributed income.

Contributions called up from member countries have so far borne interest paid out of the income of the European Fund at rates decided half-yearly. There have been nine distributions, eight of which covering the period from January 1959 to June 1963, at the rate of 2 per cent. per annum. For the ninth distribution, relating to the second half of 1963, the new method of interest calculation as described in Section 1 of this chapter was applied for the first time, and in accordance with a Decision of the Board of Management the interest distributed in respect of this half-year brought the cumulative amount of interest paid to \$3.5 million, representing 90 per cent. of member countries' total income share as at the end of the half-year in question.

* * *

The European Monetary Agreement is now in the sixth year of its existence; the 1963 review led to no substantial change in its provisions. In the field of international monetary co-operation the procedure instituted early in 1963 regarding the notification of support operations concluded between member central banks has been put into effect, thus reinforcing the rôle of the Board of Management of EMA as a centre for consultation and exchange of information between member countries.

PART III

ACTIVITIES OF THE BANK.

1. Operations of the Banking Department.

The balance sheet of the Bank as at 31st March 1964, certified by the auditors, is reproduced at the end of the present Report. There has been no change in the presentation of the various items.

* * *

BIS: Annual balance-sheet totals
(first section).

Financial years ended 31st March	Total of balance sheet	Movement
	in millions of francs	
1960	3,430	— 98
1961	3,973	+ 543
1962	4,732	+ 759
1963	4,950	+ 218
1964	5,778	+ 828

The total of the first section of the balance sheet as at 31st March 1964 amounted to 5,777,990,295 francs,* against 4,950,068,854 on 31st March 1963.

The table shows the development of the end-of-year balance-sheet totals over the past five years.

The following items are not included in the balance sheet: gold under earmark, bills and other securities held in custody for the account of central banks and other depositors; the assets (gold under earmark, bank balances, bills and other securities) held by the Bank as Agent for the Organisation for Economic Co-operation and Development in connection with the European Monetary Agreement, as Depositary under the Act of Pledge concluded with the High Authority of the European Coal and Steel Community and as Trustee or Fiscal Agent for international government loans. As was done in the case of the balance sheet as at 31st March 1963, the amounts in question are shown at the foot of the assets column under the heading "Memorandum accounts (b)". The figures are given in the table on the next page.

The total of the first part of the monthly statement declined between 31st March and 30th April 1963 from 4,950 million francs to 4,890 million, its lowest level in the financial year. After topping the 5 milliard mark on

* Except where otherwise indicated, the term "francs" in this Part signifies *gold francs*. The method of conversion into gold francs (units of 0.290 322 58... grammes fine gold — Article 5 of the Statutes) of the various currencies included in the balance sheet is the same as that adopted in preceding years; the conversion is based on the exchange rates quoted for the various currencies against dollars and on the US Treasury's selling price for gold at the end of the financial year.

BIS: Memorandum accounts (b).

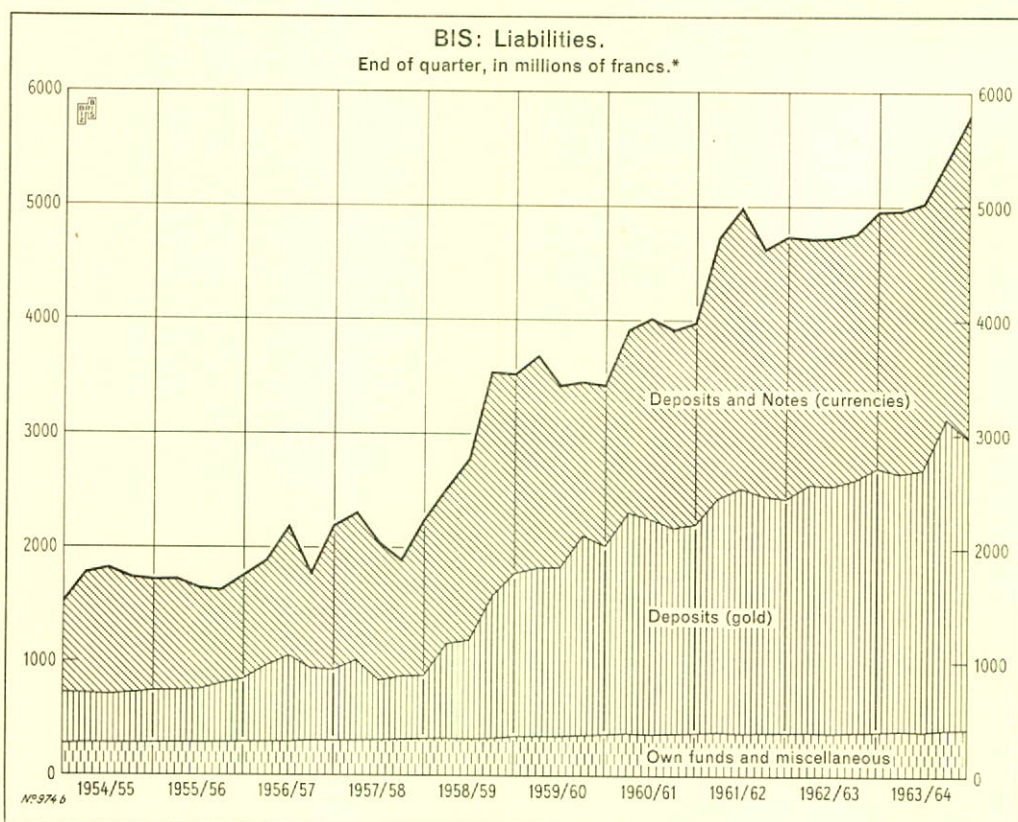
Items	Financial years ended 31st March	
	1963	1964
	in millions of francs	
Earmarked gold	1,338	1,370
Bank balances	33	36
Bills and other securities	1,086	901
Total of items not included in the balance sheet	2,457	2,307

31st August it went up to 5,536 million on 30th November, falling to 5,398 million on 31st December and then rising again to a peak on 31st March 1964 of 5,778 million, the highest figure since the foundation of the Bank.

COMPOSITION OF RESOURCES (liabilities).

A. Own funds.

The Bank's Share Capital remained unchanged at 500 million francs, of which 125 million was paid up.



* Not including liabilities connected with the execution of the Hague Agreements.

The reserves in the form of the Legal Reserve Fund and the General Reserve Fund rose from 24.8 million francs on 31st March 1963 to 25.4 million on 31st March 1964. As a result of the operations of the year (see below, Section 5, "Financial results") the balance of the Profit and Loss Account, which comprises the profit for the financial year ended 31st March 1964 and the balance brought forward from the preceding year, amounted to 25.1 million on 31st March 1964, against 21.3 million a year earlier. The amount of the item "Provision for contingencies" rose from 196.5 million on 31st March 1963 to 204 million on 31st March 1964. For the item "Miscellaneous" the figure was 21.4 million at the beginning of the year and 28.8 million at the end.

Thus, at the end of March 1964 the Bank's own funds (miscellaneous included) amounted to 408 million francs, i.e. about 8 per cent. of its borrowed funds (5,370 million) and about 7 per cent. of the total of the balance sheet on the same date (5,778 million).

The following table shows the composition of the Bank's resources at the end of each of the last five financial years.

BIS: Composition of resources.

Financial years ended 31st March	Own funds	Borrowed funds	Total	Ratio of own funds to	
				borrowed funds	balance-sheet total
	in millions of francs			in percentages	
1960	361	3,069	3,430	12	11
1961	370	3,603	3,973	10	9
1962	379	4,353	4,732	9	8
1963	389	4,561	4,950	9	8
1964	408	5,370	5,778	8	7

B. Borrowed funds.

The following tables show the origin, nature and term of the deposits received by the Bank.

BIS: Deposits, by origin.

Origin	Financial years ended 31st March		Movement
	1963	1964	
	in millions of francs		
Central banks	4,057	4,590	+ 533
Other depositors	504	780	+ 276
Total	4,561	5,370	+ 809

The deposits of central banks increased by nearly 13 per cent., while those of other depositors rose by some 55 per cent. The ratio of the latter to total deposits was higher at the end of March 1964 than at the end of March 1963.

BIS: Deposits, by nature and term.

Term	Deposits in gold			Deposits in currencies		
	Financial years ended 31st March		Movement	Financial years ended 31st March		Movement
	1963	1964		1963	1964	
	in millions of francs					
Sight	1,976	1,938	— 38	42	44	+ 2
Not exceeding 3 months	302	583	+ 281	1,512	2,243	+ 731
Between 3 and 6 months	—	—	—	525	455	— 70
Between 6 and 9 months	38	21	— 17	79	—	— 79
Between 9 and 12 months	—	20	+ 20	3	21	+ 18
Over one year	—	—	—	84	45	— 39
Total	2,316	2,562	+ 246	2,245	2,808	+ 563

Over the financial year deposits in gold rose by more than 10 per cent. and those in currencies by about 25 per cent. In both cases there was a pronounced increase in deposits at not exceeding three months, while those at more than six months (accounted for by gold and currencies to the extent of 41 and 66 million respectively) represented only a very small proportion of the total. In all, deposits in gold constituted 51 per cent. of total deposits at the beginning of the financial year and deposits in currencies 49 per cent. On 31st March 1964 the position was the reverse, the ratios being 48 and 52 per cent. respectively.

As regards deposits in gold in particular, there was a small decline in sight accounts, whereas accounts at not exceeding three months represented a distinctly higher proportion of the total at the end of the financial year than at the beginning: 23 per cent. instead of 13 per cent. Indeed, on several occasions during the year sight deposits were converted into time deposits, sometimes on the Bank's initiative in order to give it fixed-term resources suitable for the financing of forward operations against currencies. As and when such transactions were wound up, there was less reason for time accounts, and unutilised gold was retransferred to sight accounts which could be reconverted if need be into time accounts.

The development of deposits in currencies may be summed up quite simply: sight accounts — which were proportionately of little significance — remained stable, deposits at not exceeding three months increased by nearly one-half, while, with the exception of an increase in the small volume of deposits at between nine and twelve months, the other categories of deposits declined appreciably — deposits at between six and nine months, indeed, being reduced to zero.

The liabilities side of the Bank's balance sheet at the beginning and end of the financial year shows deposits as the only form of borrowed resources. However, from the end of June 1963 until the end of February 1964 the Bank's monthly statement of account included an item "Notes at not exceeding three months", which stood at 104 million on the former date and 78 million on the latter and reached a maximum of 140 million at the

end of November. These notes were issued to important banks with the agreement of the central bank concerned to assist it in its monetary policy. The purpose of the operation was to reduce the liquidity of the market in question. This was the first time that the Bank had undertaken an operation of this nature.

EMPLOYMENT OF RESOURCES (assets).

The following table shows the distribution of the Bank's assets according to their nature.

BIS: Total cash and investments.

Nature	Financial years ended 31st March				Movement	
	1963		1964			
	in millions of francs					
Cash						
Gold	2,396		2,318		— 78	
Currencies	56	2,452	48	2,366	— 8	— 86
Investments						
Gold	247		313		+ 66	
Currencies	2,182	2,429	3,030	3,343	+ 848	+ 914
Total						
Gold	2,643		2,631		— 12	
Currencies	2,238	4,881	3,078	5,709	+ 840	+ 828

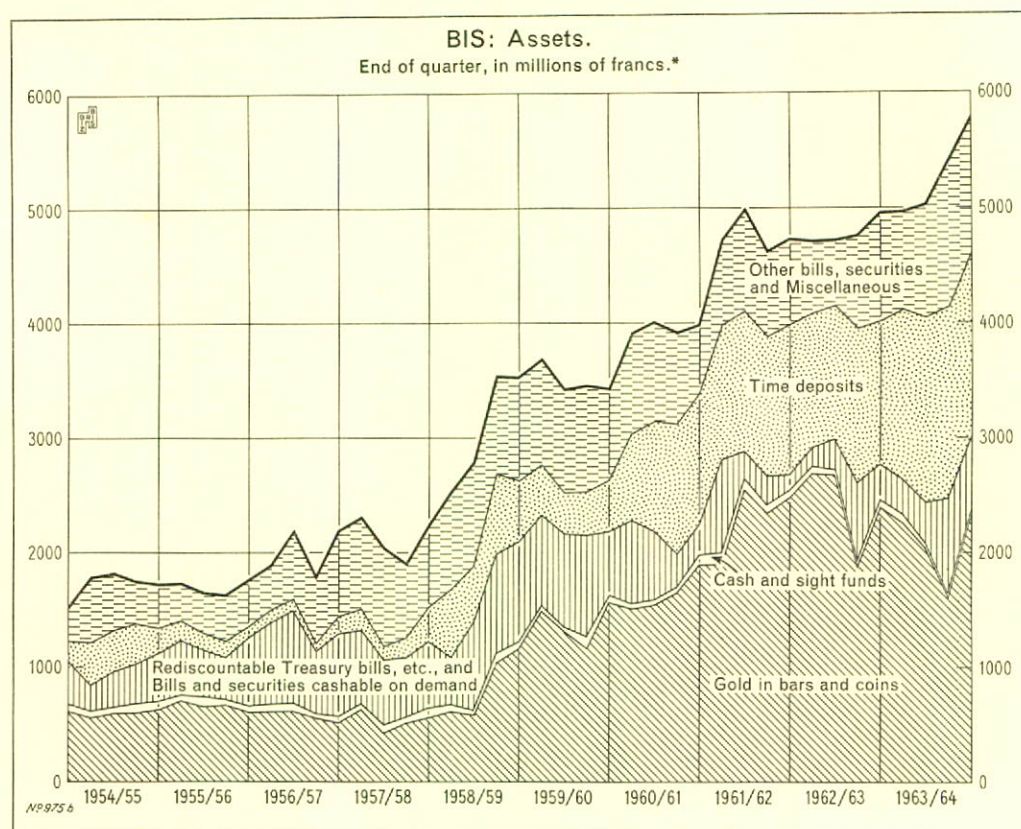
The development of the Bank's gold position is shown in the following table, which gives the maximum and minimum figures for the financial year for each item with the relevant dates.

BIS: Gold position.

End of month	Spot position				Forward operations (net balance)	Final net gold position
	Gold in bars and coins	Investments in gold	Deposits in a weight of gold	Net gold assets		
	in millions of francs					
1963						
March . . .	2,396	247	2,316	327	— 27	300
June	2,259	248	2,267 (min.)	240	53	293 (min.)
July	2,519 (max.)	242 (min.)	2,286	475 (max.)	— 179 (min.)	296
November . .	1,998	275	2,510	— 237	545	308
December . .	1,603 (min.)	275	2,733	— 855 (min.)	1,162 (max.)	307
1964						
February . .	2,489	313 (max.)	2,822 (max.)	— 20	332	312
March . . .	2,318	313	2,562	69	245	314 (max.)

The Bank's bullion holdings decreased in the course of the financial year by 78 million francs. Since its investments in gold rose by 66 million, assets in gold (bullion and investments) declined on balance by 12 million.

It can be seen from the table showing the development of the gold position that at certain times of the year, mainly in the second half of 1963



and at the beginning of 1964, wide fluctuations occurred both in the Bank's bullion holdings and in the net balance of forward operations. On 31st July, for example, when bullion holdings stood at their maximum of 2,519 million, forward operations showed a negative balance (gold to be delivered) of 179 million — the minimum for the financial year; on 31st December the situation was reversed, with bullion holdings standing at their minimum of 1,603 million and the balance of forward operations showing its maximum of 1,162 million (gold receivable). These two components of the Bank's gold position normally moved in opposite directions in accordance with the winding-up and maturity schedule of forward gold operations.

The distribution of the Bank's assets according to their term calls for the following observations.

A. Sight funds, rediscountable investments and investments cashable on demand.

The movements in the item "Gold in bars and coins" (which consisted entirely of gold in bars) have already been commented upon in the analysis of the table showing the Bank's gold position.

The figure for the item "Cash on hand and on sight account with banks" was 56 million francs at the beginning of the financial year and 48 million on 31st March 1964. Its lowest point was 36 million and its highest 77 million. The average balance shown under this heading was 49 million, compared with 50 million for the previous financial year.

On 31st March 1964 total gold and currency holdings represented 41 per cent. of the total of the first part of the Bank's balance sheet, compared with 50 per cent. a year earlier.

There were large fluctuations in the Bank's holdings of "Rediscountable Treasury bills". At the beginning of the financial year they stood at 306 million gold francs. In subsequent months the total was consistently below this level, reaching its lowest point for the financial year — 198 million — on 31st July. Thereafter it rose steadily to reach 729 million, its peak for the financial year, on 31st December; at the end of the financial year it was down to 573 million. These movements were due in most cases to investments effected after swap or exchange operations carried out by the Bank with central banks.

The item "Bills and securities cashable on demand" showed even greater fluctuations than the preceding item. After standing at 9 million at the beginning of the financial year, the figure for this item recorded its minimum of 6 million on 30th September 1963 and reached its maximum of 99 million on 30th November; at the end of the financial year it amounted to 69 million. Under this heading are entered investments, other than rediscountable Treasury bills, that can be mobilised at sight.

At the beginning of the financial year the total of the Bank's sight funds and rediscountable investments, comprising the assets items so far analysed, was thus 2,767 million francs and represented 56 per cent. of the first part of the balance sheet. On 31st March 1964 the corresponding figures were 3,009 million francs and 52 per cent. During this period the percentage of sight deposits on the liabilities side declined from 41 to 34. The Bank's liquidity ratio thus remains particularly high.

B. Time deposits and investments.

In general, a substantial part of the currency balances created by the Bank's gold swaps against currencies and its forward gold purchases was invested in the form of time deposits and advances or other bills and securities, which items fluctuated in consequence.

The total of the item "Time deposits and advances", which stood at 1,245 million francs on 31st March 1963, had declined to 1,205 million by the end of the following month. It rose to 1,666 million on 31st December; on 31st March 1964 it still stood as high as 1,594 million.

The total of the item "Other bills and securities" fluctuated to a more or less corresponding extent; from 869 million on 31st March 1963 it

reached its minimum of 782 million on 31st May and its maximum of 1,194 million on 31st December, standing at the end of the financial year at 1,106 million.

The following table shows the distribution of the Bank's time investments according to their term and compares their composition at the beginning and end of the financial year.

BIS: Time deposits and advances and other bills and securities.

Periods	Financial years ended 31st March		Movement
	1963	1964	
	in millions of francs		
Not exceeding 3 months	1,313	1,774	+ 461
Between 3 and 6 months	567	742	+ 175
Between 6 and 9 months	126	63	— 63
Between 9 and 12 months	34	57	+ 23
Over 1 year	74	64	— 10
Total	2,114	2,700	+ 586

As in the case of deposits entrusted to the Bank, there was a substantial increase in the Bank's investments at not exceeding three months. A rise was also registered in investments at between three and six months; it should be noted, however, that the maturity schedule of the investments just referred to is such as to give them a high degree of liquidity. The investments entered under the headings "not exceeding three months" and "between three and six months" include, in fact, funds which can be mobilised at very short notice.

There was a decline, on the other hand, in investments at over six months, not only in volume but also as a proportion of the total shown in the preceding table; on 31st March 1964 they represented only 7 per cent. of the total, compared with 11 per cent. on 31st March 1963.

* * *

Apart from the large increase in the funds entrusted to the Bank by central banks and other depositors, the main feature of the financial year was the steady development of swap transactions in currencies and in gold against currencies. This development was facilitated by the increase in deposits in gold received by the Bank.

The object of a number of the swap operations effected between the Bank and central banks was, at certain times of the year, to channel back funds to those markets from which funds had been withdrawn through the commercial banks.

The Bank's activity in the field of gold transactions, which had been resumed in the course of the previous financial year, subsequently developed

considerably. Apart from its current routine spot purchases and sales, exchanges and transfers, the Bank effected, as has already been noted a number of times in this Report, fairly substantial forward purchases of gold and other transactions involving forward sales of currencies against gold. As in the past, all these operations were carried out in conformity with the aims and the monetary policy of the central banks.

Finally, it is to be noted that the total volume of the Bank's operations for the last financial year exceeded that for the financial year 1962-63 by more than half.

As far as the financial results are concerned, the increase in the surplus is due to various factors, the main ones being the rise in deposits entrusted to the Bank, the development of forward gold transactions and increased recourse by central banks to the facilities that the Bank is able to offer in the matter of short-term international financial settlements.

As in previous years, the second section of the balance sheet consists solely of the assets and liabilities connected with the execution of the Hague Agreements of 1930. The total for the section remains unchanged at 297,200,598 francs.

2. The Bank as Trustee and Fiscal Agent for international government loans.

In conformity with the agreements in force the Bank continued to perform the functions of Fiscal Agent of the Trustees for the new bonds of the German External Loan 1924 (Dawes Loan) and of Trustee for the new bonds of the German Government International Loan 1930 (Young Loan) which were issued by the Government of the Federal Republic of Germany in accordance with the London Agreement on German External Debts of 27th February 1953.

The financial year 1963-64 ended for the Dawes Loan on 15th April 1964 and for the Young Loan on 1st June 1964. The interest in respect of the financial year 1963-64 amounted to the equivalent of about 13.2 million francs for the Dawes Loan and to the equivalent of about 37.8 million francs for the Young Loan; it was duly paid to the Bank, which distributed it among the Paying Agents. Redemption of both loans was effected in respect of the financial year 1963-64 partly by purchases of bonds on the market and partly by drawings.

The question whether the exchange guarantee attached to the Young Loan under the terms of the London Agreement is applicable in the case of the revaluation of the Deutsche Mark of March 1961 has not yet been settled. The matter is in the hands of the governments of the countries in which issues of the Loan were made.

The position as regards the Dawes and Young Loans is shown in the following tables.

German External Loan 1924
(Dawes Loan).

Issue	Currency	Nominal value			
		Bonds issued	Bonds purchased or drawn for redemption in respect of the financial years		Balance after redemption
			1958-59 to 1962-63	1963-64	
Conversion bonds					
American . . .	\$	44,073,000	7,564,000	1,743,000	34,766,000
Belgian . . .	£	583,100	74,200	15,300	493,600
British	£	8,275,800	1,054,100	218,500	7,003,200
Dutch	£	1,308,700	147,400	36,000	1,125,300
French	£	1,927,200	241,900	50,500	1,634,800
Swedish . . .	S.kr.	14,209,000	1,630,000	364,000	12,215,000
Swiss	£	1,130,500	140,200	29,500	960,800
Swiss	Sw.fr.	8,251,000	916,000	211,000	7,124,000
Funding bonds					
American . . .	\$	8,199,000	1,215,000	214,000	6,770,000
Belgian	£	157,700	24,400	4,100	129,200
British	£	2,231,600	338,600	58,700	1,834,300
Dutch	£	288,300	36,500	7,900	243,900
French	£	498,300	76,500	13,200	408,600
Swiss	£	115,000	16,800	3,000	95,200
Swiss	Sw.fr.	415,000	57,000	11,000	347,000

German Government International Loan 1930
(Young Loan).

Issue	Currency	Nominal value*			
		Bonds issued	Bonds purchased or drawn for redemption in respect of the financial years		Balance after redemption
			1958-59 to 1962-63	1963-64	
Conversion bonds					
American . . .	\$	55,388,000	3,087,000	709,000	51,592,000
Belgian	B.fr.	202,603,000	11,387,000	2,539,000	188,677,000
British	£	17,700,000	982,100	221,500	16,496,400
Dutch	Fl.	51,981,000	2,729,000	718,000	48,534,000
French	Fr.fr.	444,636,000	24,645,000	5,573,000	414,418,000
German	DM	14,458,000	795,000	181,000	13,482,000
Swedish	S.kr.	92,763,000	5,182,000	1,160,000	86,421,000
Swiss	Sw.fr.	58,375,000	3,270,000	733,000	54,372,000
Funding bonds					
American . . .	\$	8,989,000	519,000	108,000	8,362,000
Belgian	B.fr.	45,622,000	2,666,000	554,000	42,402,000
British	£	4,223,100	244,700	50,800	3,927,600
Dutch	Fl.	8,360,000	452,000	120,000	7,788,000
French	Fr.fr.	97,970,000	5,515,000	1,172,000	91,283,000
German	DM	411,000	24,000	5,000	382,000
Swedish	S.kr.	6,014,000	350,000	72,000	5,592,000
Swiss	Sw.fr.	1,405,000	81,000	17,000	1,307,000

* Nominal value on 1st May 1964 established in accordance with the provisions of the London Agreement on German External Debts of 27th February 1953 but without taking account of the revaluation of the Deutsche Mark in March 1961.

The Bank is also Trustee for the assented bonds of the Austrian Government International Loan 1930. The amount of interest due in respect of the financial year which ended on 31st December 1963 was the equivalent of about 0.7 million francs; this was duly paid to the Bank, which distributed it among the Paying Agents. Redemption in respect of the financial year 1963 was carried out by purchases of bonds on the market and by way of drawing. The position as regards this loan is shown in the following table.

Austrian Government International Loan 1930.

Issue	Currency	Nominal value			
		Bonds assented	Bonds purchased or drawn for redemption in respect of the financial years		Balance after redemption
			1959 to 1962	1963	
American . . .	\$	1,667,000	261,000	55,000	1,351,000
Anglo-Dutch .	£	856,600	125,600	33,100	697,900
Swiss	Sw.fr.	7,102,000	870,000	238,000	5,994,000

The coupons of the Austrian Government International Loan 1930 which the Federal Republic of Germany has undertaken to pay to the extent of 75 per cent. of the nominal value have now all matured and can be presented for payment up to 1st July 1967. In the year under review the payments made in respect of these coupons were negligible.

3. The Bank as Depositary under the terms of the Act of Pledge concluded with the High Authority of the European Coal and Steel Community.

The Bank has continued, in conformity with an Act of Pledge concluded between it and the High Authority of the European Coal and Steel Community on 28th November 1954, to perform the functions of Depositary in respect of the loans of the High Authority which are secured in accordance with the provisions of that Act.

The total amount of these secured loans was originally equivalent to about 817 million francs. Repayments by the High Authority up to 1st April 1964 amounted to the equivalent of about 174 million francs, so that the total amount now outstanding is the equivalent of about 643 million francs. Further particulars of these loans are given in the following table.

The High Authority has used the proceeds of these loans to grant credits in the member countries of the European Coal and Steel Community.

During the financial year 1963-64 the Bank received and distributed among the Paying Agents the equivalent of about 34 million francs in respect of interest and the equivalent of about 47 million francs in respect of redemption.

Secured loans of the High Authority
of the European Coal and Steel Community.

Series of Secured Notes of the High Authority	Dates of issue	Countries of issue	Lenders	Original amounts of loans	Amounts unredeemed on 1st April 1964	Rates of interest %	Year of final maturity
1st	1954	United States	US Government	\$ 100,000,000	80,500,000	3%	1979
2nd	1955	Belgium	Caisse Générale d'Epargne et de Retraite, Brussels	B.fr. 200,000,000	167,000,000	3½	1982
3rd	1955	Germany	Rheinische Girozentrale und Provinzialbank, Düsseldorf	DM 25,000,000	19,714,000	3¼	1981
			Landesbank für Westfalen (Girozentrale), Münster	DM 25,000,000	19,714,000	3¼	1981
4th	1955	Luxemburg	Caisse d'Epargne de l'Etat, Luxembourg	B.fr. 20,000,000 L.fr. 5,000,000	16,700,000 —	3½	1982
5th	1956	Saar	Landesbank und Girozentrale Saar, Saarbrücken	DM 2,977,450 ¹	2,334,321	4¼	1977
6th	1956	Switzerland	Public issue	Sw.fr. 50,000,000	42,500,000	4¼	1974
7th ²	1957	United States	Public issue	\$ 25,000,000	21,200,000	5½	1975
10th	1957	Luxemburg	Etablissement d'Assurance contre la Vieillesse et l'Invalidité, Luxembourg	L.fr. 100,000,000	94,487,558	5%	1982
11th ²	1958	United States	Public issue	\$ 35,000,000	35,000,000	5	1978
13th } 14th }	1960	United States	Public issue	\$ 25,000,000	25,000,000	5%	1980
			Public issue	\$ 3,300,000	—	—	—
				\$ 3,300,000	3,300,000	4%	1964
				\$ 3,400,000	3,400,000	5	1965
15th	1961	Luxemburg	Etablissement d'Assurance contre la Vieillesse et l'Invalidité, Luxembourg	L.fr. 100,000,000	100,000,000	5¼	1986
16th	1961	Netherlands	Public issue	Fl. 50,000,000	50,000,000	4½	1981

¹ This loan, which was contracted in French francs, was converted into Deutsche Mark in 1959. The original amount was 350,000,000 old French francs. ² The Secured Notes of the 8th, 9th and 12th Series have been entirely redeemed.

The High Authority has also raised loans which are not secured in accordance with the Act of Pledge, but the Bank has no function in connection with such loans.

4. The Bank as Agent for the Organisation for Economic Co-operation and Development (European Monetary Agreement).

The introduction and working of the European Monetary Agreement have been described in previous Annual Reports of the Bank and the description is brought up to date in Chapter VI of Part II of the present Report.

The Bank continued to act as Agent for the execution of the financial operations of the EMA under the Organisation for Economic Co-operation

and Development. The expenses of the Bank in this capacity amounted to 378,966 francs in the twelve months to March 1964; this amount has been duly reimbursed by the Organisation (as shown in the Profit and Loss Account for the financial year ended 31st March 1964).

5. Financial results.

The accounts for the thirty-fourth financial year ended 31st March 1964 showed a surplus of 27,417,055 francs. The comparable figure for the preceding financial year was 21,210,271 francs.

From the year's surplus the Board of Directors has decided to deduct a sum of 400,000 francs in order to write off the purchase price of a building acquired during the year. It has further decided that it is necessary to transfer 2,000,000 francs to the provision for exceptional costs of administration and 7,500,000 francs to the provision for contingencies; the net profit for the year thus amounts to 17,517,055 francs.

After providing 402,141 francs for the Legal Reserve Fund, i.e. the proportion of 5 per cent. of the net profit required to bring it up to an amount equal to 10 per cent. of the amount of the paid-up capital, as required by the Statutes, and with the addition of the balance of 7,629,978 francs brought forward from the previous year, there is a sum of 24,744,892 francs available.

The Board of Directors recommends that the present General Meeting should distribute, as last year, a dividend of 37.50 francs per share, involving a distribution of 7,500,000 francs. The Board also proposes that, as an exceptional measure, a lump sum should again be applied to the reduction of the amount of the undeclared cumulative dividend. This sum, which has been fixed at 8,500,000 francs, will represent an extraordinary distribution of 42.50 francs per share. The total distribution will thus amount this year to 80 francs, payable on 1st July 1964 in the amount of 114.30 Swiss francs per share. As regards the shares in respect of which the dividend cannot be paid on that date, the conversion to Swiss francs will be effected on the day of payment. The balance carried forward will be 8,744,892 francs.

The amount of the undeclared cumulative dividend will, as a result of this distribution, be reduced from 241.97 to 199.47 francs per share. It is recalled that the provisions of the Statutes relating to the cumulative dividend give shareholders the assurance that no remuneration will be paid in respect of the long-term deposits made under the Hague Agreements of 1930 by the Creditor Governments and by the German Government unless the shareholders have received in full the dividend permitted by Article 53(b) and (c) of the Statutes.

The accounts of the Bank and its thirty-fourth Annual Balance Sheet have been duly audited by Messrs. Price Waterhouse & Co., Zurich. The Balance Sheet, the Report of the Auditors and the Profit and Loss Account will be found at the end of this Report.

6. Changes in the Board of Directors.

The mandate as a member of the Board of M. Maurice Frère being due to expire on 7th August 1963, he was re-appointed under Article 28(2) of the Statutes by M. Hubert Ansiaux, the Governor of the National Bank of Belgium, in July 1963 for a further period of three years to end on 7th August 1966.

The mandate of Dr. Donato Menichella as a member of the Board was due to expire on 7th November 1963 and he was re-appointed under Article 28(2) of the Statutes by Dr. Guido Carli, Governor of the Bank of Italy, in October 1963 for a further period of three years to end on 7th November 1966.

The mandate as a member of the Board of Dr. M. W. Holtrop being due to expire on 31st March 1964, he was re-elected under Article 28(3) of the Statutes at the meeting of the Board held on 9th March 1964 for a further period of three years ending on 31st March 1967.

During the course of the year Lord Cromer, Governor of the Bank of England, appointed Mr. M. H. Parsons and, should the latter be absent, Mr. R. G. Raw as his Alternates in the place of Mr. J. M. Stevens and Mr. J. St. J. Rootham respectively.

In January 1964 M. Jacques Brunet, Governor of the Bank of France, appointed M. Bernard Clappier as his Alternate in the place of M. Pierre Calvet.

The Bank is grateful to Mr. Stevens, Mr. Rootham and M. Calvet for their valuable services extending over several years.

CONCLUSION.

For the first time in some years, a major change has taken place in the international economic picture over the past twelve months. In essence, the economic trouble spot has shifted from the United States to continental western Europe and the conflict between domestic and external considerations, which has complicated policy-making in both Europe and the United States for several years, has been significantly reduced.

In the United States there are firmer grounds for confidence with regard to both the domestic economic growth and the restoration of equilibrium in the balance of payments. On both fronts more vigorous policy measures in the year just past have made a major contribution to the improvement.

The pace of economic expansion accelerated from the beginning of 1963 and the upswing has continued without significant distortions in the pattern of demand. Reasonable wage increases and the maintenance of price stability have contributed to making the current expansion phase of the business cycle unusually long. The substantial tax reduction enacted earlier this year should provide the demand stimulus for prolonging this advance and promises to help in reducing excessive unemployment. While inflationary tensions have not been in evidence, the authorities are alert to this possibility.

Following the measures taken in July 1963, there has been a welcome improvement in the balance-of-payments position and increased confidence in the dollar. While the near-balance of the external accounts in the first quarter of 1964 has been achieved with the help of some temporary factors, the outcome for the year should show a large reduction in the 1963 deficit. However, a firm equilibrium has not yet been secured and hence efforts to achieve it cannot be relaxed. The immediate need is to meet the objective of reducing government expenditure abroad, which was announced in last July's programme; in addition, active support to the process of gradual adjustment to conditions of external equilibrium must be continued to allow such temporary measures as the pending interest equalisation tax to be dispensed with in a reasonable time.

In the United Kingdom demand and output have expanded strongly over the past year. Although there was no major disturbance to equilibrium, measures were taken in the spring of 1964 to keep the increase in demand in line with the growth of the productive potential of the economy. The rise in wages was fairly moderate, and it is encouraging that the need for incomes policy appears to be finding wider acceptance. While the margin of unused capacity in the economy has been much reduced and some external deficit is to be expected, the outlook for the months ahead does not seem to present severe difficulties.

On a longer view, however, the fact that some restraint on demand was called for after little more than a year of expansion suggests that a more dynamic attitude by both business and labour towards productivity increase is required to enable the economy to match the gains in other countries.

On the continent of Europe, while there has been a reasonably balanced position in a number of countries, the situation more broadly has been that the signs of pressure evident a year ago have worsened and that potential disequilibrium has become actual disequilibrium. The evidence of this has been rising prices, soaring imports, deterioration of the current external balance and, in the case of Italy, a large balance-of-payments deficit. The cause has generally been excessive total demand, with resultant tightness on the labour market, stemming not so much from investment or government outlays as from higher consumer incomes and spending. The rapid inter-reaction of the impulses among the countries has led in the case of Germany to a large, unwanted surplus in the balance of payments.

In these circumstances most countries have shifted the emphasis in policy to restraint. The measures taken have been fairly forceful in a few cases, but it may be said that policy generally seems designed to remove the inflationary excess without slowing down too much the underlying expansion in real output. While such a happy result may be attainable, the risks are more on the side of too mild restraint than of too strong. In particular, as monetary measures could be more quickly brought to bear on the situation, there is danger of insufficiently limiting consumer spending by fiscal restraint.

For a country where a severe external deficit has emerged, as in Italy, the need is that the situation should show improvement without extended delay. Experience has proved that adequate measures produce prompt results; the test will be whether there is a quick levelling-off in the rise in imports. Wage restraint must be an essential element in restoring monetary stability; in addition, it is evident that the system used in Italy for automatic cost-of-living adjustments has contributed strongly to the wage-price spiral and remains an obstacle to monetary stability.

Besides disequilibrium among countries, the Continent's aggregate balance of payments has been showing increased net capital imports. As circumstances differ considerably from country to country in this respect, there is no general prescription for resolving the problem. Recent actions in a few countries have been helpful, but there is still need for persistent efforts to make capital-market facilities and conditions more conducive to capital exports.

A welcome gain in the past year has been the rise in export earnings of the less developed countries, which have benefited from higher demand and prices for raw materials. This should provide a firmer basis for constructive development from these countries' own resources and even better opportunities for using capital from abroad. None the less, the need for capital assistance as well as for easier access to markets in the industrial

countries remains great, and it is to be hoped that progress on these matters can be achieved at the Geneva Conference on Trade and Development. In a few countries, however, internal policies have generated inflation to such an extent as to make an excessive balance-of-payments gap a permanent feature. Under such circumstances a useful rôle for outside assistance is difficult to find; it is evident that the continuous inflation not only makes development planning almost impossible but threatens political stability as well.

In the past year serious study has been undertaken of the functioning of the international monetary system and the possible needs for increased liquidity. While it is difficult to anticipate the longer-term evolution of the system, recent experience has highlighted two important points; one is that co-operation among the monetary authorities can contribute substantially to maintaining orderly conditions on the exchange markets; the other is that the disturbances that arise from inflation cannot be resolved by illusions about liquidity creation but only by acting on inflation itself.

Respectfully submitted,

GABRIEL FERRAS

General Manager.

BALANCE SHEET AND PROFIT AND LOSS ACCOUNT

AS AT 31st MARCH 1964

BALANCE SHEET

ASSETS

IN GOLD FRANCS (UNITS OF 0.290 322 58...)

		%
Gold in bars and coins	2,318,123,181	40.1
Cash on hand and on sight account with banks	47,659,507	0.8
Rediscountable Treasury bills	573,365,062	9.9
Bills and securities cashable on demand	68,831,905	1.2
Time deposits and advances		
Not exceeding 3 months	1,173,460,865	20.3
» » » (gold)	3,405,463	0.1
Between 3 and 6 months	401,826,881	6.9
Between 9 and 12 months	15,419,903	0.3
	<u>1,594,113,112</u>	
Other bills and securities		
Gold		
Not exceeding 3 months	146,445,240	2.5
Between 3 and 6 months	88,317,811	1.5
Between 6 and 9 months	42,450,607	0.7
Between 9 and 12 months	32,158,343	0.6
Currencies		
Not exceeding 3 months	450,195,417	7.8
Between 3 and 6 months	252,222,817	4.4
Between 6 and 9 months	20,751,028	0.4
Between 9 and 12 months	9,922,397	0.2
Over 1 year	63,819,930	1.1
	<u>1,106,283,590</u>	
Miscellaneous assets	1,322,714	0.0
Buildings and equipment	1	0.0
Own funds employed in execution of the Hague Agreements of 1930 for investment in Germany (see below)	68,291,223	1.2
	<u>5,777,990,295</u>	<u>100</u>
Execution of Hague		
Funds invested in Germany (see Note 2)		
Claims on Reichsbank and Golddiskontbank; bills of Golddiskontbank and Railway Administration and bonds of Postal Administration (matured)	221,019,558	
German Treasury bills and bonds (matured)	76,181,040	
	<u>297,200,598</u>	
MEMORANDUM ACCOUNTS		
a. Forward gold operations:		
Net balance: gold receivable (currencies to be delivered)	245,380,187	
b. Funds, bills and other securities administered or held by the Bank for account of third parties:		
Earmarked gold	1,370,111,521	
Bank balances	35,527,862	
Bills and other securities	901,062,622	

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS

OF THE BANK FOR INTERNATIONAL SETTLEMENTS, BASLE.

In conformity with Article 52 of the Bank's Statutes, we have examined the books and accounts of the and explanations we have required. Subject to the value of the funds invested in Germany, we report that in drawn up so as to exhibit a true and correct view of the state of the Bank's affairs according to the best of above-described gold franc equivalents of the currencies concerned.

ZURICH, 5th May 1964.

AS AT 31st MARCH 1964

GRAMMES FINE GOLD — ART. 5 OF THE STATUTES)

LIABILITIES

			%
Capital			
Authorised and issued 200,000 shares, each of 2,500 gold francs	500,000,000		
of which 25% paid up	125,000,000	2.2	
Reserves			
Legal Reserve Fund	12,097,859		
General Reserve Fund	13,342,650		
	25,440,509	0.4	
Deposits (gold)			
Central banks			
Between 9 and 12 months	20,670,682	0.4	
Between 6 and 9 months	20,777,510	0.4	
Not exceeding 3 months	513,990,491	8.9	
Sight	1,819,747,478	31.5	
Other depositors			
Not exceeding 3 months	68,890,913	1.2	
Sight	118,010,389	2.0	
	2,562,087,463		
Deposits (currencies)			
Central banks			
Over 1 year	45,006,175	0.8	
Between 9 and 12 months	20,572,755	0.4	
Between 3 and 6 months	411,897,593	7.1	
Not exceeding 3 months	1,720,223,327	29.8	
Sight	16,564,092	0.3	
Other depositors			
Between 3 and 6 months	43,475,112	0.7	
Not exceeding 3 months	522,276,408	9.0	
Sight	27,454,401	0.5	
	2,807,469,863		
Miscellaneous	28,845,427	0.5	
Profit and Loss Account			
Balance brought forward from the financial year ended			
31st March 1963	7,629,978		
Profit for the financial year ended 31st March 1964	17,517,055		
	25,147,033	0.4	
Provision for contingencies	204,000,000	3.5	
	5,777,990,295	100	
Agreements of 1930			
Long-term deposits			
Annuity Trust Account deposits of Creditor Governments (see Note 3)	152,606,250		
German Government deposit	76,303,125		
	228,909,375		
Own funds employed in execution of the Agreements (see above)	68,291,223		
	297,200,598		
NOTE 1 — For Balance Sheet purposes the currency amounts of the assets and liabilities have been converted into gold francs on the basis of quoted or official rates of exchange or in accordance with special agreements applicable to the respective currencies.			
NOTE 2 — Under an Arrangement dated 9th January 1953 between the Government of the Federal Republic of Germany and the Bank, which forms a part of the Agreement on German External Debts of 27th February 1953, it has been agreed that the Bank will not demand prior to 1st April 1966 the reimbursement of the principal of its investments in Germany described above, including arrears of interest thereon at 31st December 1952.			
NOTE 3 — The Bank has received confirmation from Governments whose deposits amount to the equivalent of 149,920,380 gold francs that they cannot demand from the Bank, in respect of their claims on the Annuity Trust Account, the transfer of amounts greater than those of which the Bank can itself obtain reimbursement and transfer by Germany in currencies approved by the Bank.			

Bank for the financial year ended 31st March 1964, and we report that we have obtained all the information our opinion the above Balance Sheet and Memorandum accounts, together with the Notes thereon, are properly our information and the explanations given to us and as shown by the books of the Bank, as expressed in the

PRICE WATERHOUSE & CO.

PROFIT AND LOSS ACCOUNT

for the financial year ended 31st March 1964

		Gold francs
Net income from the use of the Bank's own funds and the deposits entrusted to it		33,115,350
Commission earned as Trustee, etc.		711,691
		<u>33,827,041</u>
Costs of administration:		
Board of Directors — fees and travelling expenses ...	230,498	
Executives and staff — salaries, pension contributions and travelling expenses	5,535,150	
Rent, insurance, heating, electricity	40,496	
Renewals and repairs of buildings and equipment ...	80,113	
Office supplies, books, publications, printing	262,058	
Telephone, telegraph and postage	166,220	
Experts' fees (auditors, interpreters, economists, etc.)	56,168	
Cantonal taxation	35,295	
Contribution to the Per Jacobsson Foundation ...	97,696	
Miscellaneous	285,258	
	<u>6,788,952</u>	
Less: Amounts recoverable for expenses as Agent of the Organisation for Economic Co-operation and Development (European Monetary Agreement) ...	378,966	6,409,986
		<u>27,417,055</u>
The Board of Directors has decided that it is necessary to transfer		
to the provision for depreciation on buildings	400,000	
to the provision for exceptional costs of administration	2,000,000	
to the provision for contingencies	7,500,000	9,900,000
NET PROFIT for the financial year ended 31st March 1964		17,517,055
Add: Balance brought forward from the preceding year		7,629,978
Total profits available		<u>25,147,033</u>
which the Board of Directors recommends to the Annual General Meeting called for 8th June 1964 should be dealt with as follows:		
Transfer to the Legal Reserve Fund		402,141
Dividend of 37.50 gold francs, plus an amount of 42.50 gold francs, which increases the distribution to 80.— gold francs per share and reduces the amount of the undeclared cumulative dividend from 241.97 gold francs to 199.47 gold francs per share		16,000,000
Balance to be carried forward		8,744,892
		<u>25,147,033</u>

