BANK FOR INTERNATIONAL SETTLEMENTS

THIRTY-SEVENTH ANNUAL REPORT

1st APRIL 1966 — 31st MARCH 1967

BASLE

12th June 1967

TABLE OF CONTENTS

LIST OF TABLES AND GRAPHS

(Graphs are indicated by an asterisk)

Page

Part I – Current Economic Trends and Policies 1966–67

Part II – Monetary and Economic Survey

I. Credit Developments and Policies

II. World Trade and Payments

Page

Part III - Activities of the Bank

THIRTY-SEVENTH ANNUAL REPORT

submitted to the

ANNUAL GENERAL MEETING

of the

BANK FOR INTERNATIONAL SETTLEMENTS

held in

Basle on 12th June 1967.

Gentlemen,

I have the honour to submit herewith the Annual Report of the Bank for International Settlements for the thirty-seventh financial year, which began on 1st April 1966 and ended on 31st March 1967.

After deduction of the transfers to provisions, the net profit amounted to 32,074,487 gold francs, compared with 22,578,751 gold francs for the preceding year. With the addition to the net profit of the balance of 9,842,787 gold francs brought forward from the previous financial year, there is a sum of 41,917,274 gold francs available.

The Board of Directors recommends that the present General Meeting should declare, as last year, a dividend of 112.50 gold francs per share, i.e. a total distribution of 22,500,000 gold francs. The dividend will consist of 37.50 gold francs in respect of the annual cumulative dividend of 6 per cent., 54.47 gold francs in respect of the remainder of the undeclared cumulative dividend and 20.53 gold francs representing an additional, non-cumulative dividend of 3.28 per cent. If the other recommendations of the Board of Directors are accepted, the sum of 9,409,310 gold francs will be transferred to the General Reserve Fund and the sum of 10,007,964 gold francs to a Special Dividend Reserve Fund.

Part I of this Report deals with economic developments and policies in Europe and the United States in 1966 and the early months of 1967, and examines the development of global reserves in the course of the last twelve years.

In Part II a survey is given of developments in the fields of credit, 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 activities of the Bank and gives details of the results of the year's business operations, together with an analysis of the balance sheet as at 31st March 1967. It also deals with the functions of the Bank on behalf of the High Authority of the European Coal and Steel Community and as Trustee and Fiscal Agent for international loans. Finally, it touches on the Bank's rôle in promoting co-operation between central banks as well as on its relations with other international institutions.

PART I

CURRENT ECONOMIC TRENDS AND POLICIES 1966–67.

In the past year a marked change has come over the economic situation in many of the principal industrial countries. In the early months of 1966 excess demand was exerting strong inflationary pressures on prices and the labour market. While official policies were directed to curbing the boom, they had not yet gathered the strength, or had the time, to show results. In the course of the year, however, the effect of policy restraint became more and more evident and by the first quarter of 1967 had produced a situation that ranged from marked slow-down or easing to mild recession.

The countries that dominated in giving this general cast to the international economic picture were the United States, Germany and the United Kingdom, not only because of their own size but because the change in their overall demand soon came to be felt beyond their borders. In greater or lesser degree, the development of the situation in the other countries of western Europe has been similar.

Italy and Japan have stood out as exceptions to the more general turn in the demand picture. As they had been obliged to impose stabilisation programmes in 1963–64, their economies were in a balanced phase of expansion by the beginning of last year, and this has continued to run on smoothly up to the present time.

There have also in the past year been substantial changes in balance-of-payments situations, particularly of the bigger countries. The large surplus position of France has turned to deficit and Italy's has been sharply curtailed. The United Kingdom's deficit has shifted into mild surplus and that of Germany into substantial surplus. For the United States, although tight money in the past year produced an exceptional shift in capital flows, the underlying payments position deteriorated. While swings in external positions are no doubt better than prolonged surpluses and deficits, the goal of equilibrium appears as elusive as ever and it is only in a few countries that a near-balanced position seems in prospect.

United States.

To tax or not to tax; that was the question. And the indecisive way it was answered gives the key to what happened to the US economy over the last eighteen months. On the one hand, it allowed the forces of excess demand to gather momentum and, on the other, it left the task of restraint to monetary policy.

The question posed itself in the wake of the announcement by the President on 28th July 1965 that the military forces in Vietnam and the draft call were to be substantially increased. This clearly implied a sharp rise in defence expenditure, with a multiplied effect on economic activity through its repercussions on major categories of private spending. And this jolt to total demand, coming in a situation of already strongly expanding demand and about full employment, was bound to lead to inflationary pressures on prices and the labour market. Within a matter of weeks these implications of the stepping-up of the Vietnam conflict became evident in the market-place and by the fourth quarter of 1965 a boom situation manifested itself.

The fever chart of the economy, given in the table below, shows gross national expenditure increasing at an average rate of $12.9 milliard in the

United States: Changes in demand factors, 1965–67.

Demand factors	Average quarterly changes			
	2nd and 3rd quarters 1965	4th quarter 1965 and 1st quarter 1966	2nd to 4th quarter 1966	1st quarter 1967
	in milliards of dollars, seasonally adjusted			
Personal consumption expenditure	+ 8.1	+ 10.3	+ 6.2	+ 5.8
Durable goods	+ 0.8	+ 1.8	− 0.2	− 1.2
Other	+ 7.3	+ 8.5	+ 6.4	+ 7.1
Government purchases of goods and services	+ 3.0	+ 3.7	+ 5.3	+ 8.0
National defence	+ 1.2	+ 2.0	+ 3.6	+ 4.2
Other	+ 1.8	+ 1.7	+ 1.7	+ 3.8
Gross private fixed investment	+ 1.8	+ 3.8	− 0.7	+ 0.2
Residential construction	—	+ 0.4	− 2.2	+ 0.2
Producers' plant and equipment	+ 1.8	+ 3.4	+ 1.5	—
Change in business inventories	− 0.4	+ 0.1	+ 2.5	− 10.8
Net exports of goods and services	+ 0.4	− 0.5	− 0.6	+ 1.3
Gross national expenditure	+ 12.9	+ 17.4	+ 12.7	+ 4.4

second and third quarters of 1965. At this rate the economy was continuing the balanced expansion of the previous few years, with reasonably stable prices and moderate wage increases. Then the rate of rise jumped to $17.4 milliard in the next two quarters. Defence spending rapidly increased and, what is more, orders were being placed that would make for a larger rise later on. Besides this direct stimulus, the spectre of war added a psychological factor which helped boost the quarterly increase in business plant and equipment outlays from $1.8 to 3.4 milliard and in consumer expenditure from $8.1 to 10.3 milliard in this short space of time.

The resulting strain on resources is indicated by the flatness of inventories; as raw materials and goods in process in the defence industries must have been rising, consumer and capital purchasing was running ahead of output. In the six months after September 1965 production in the group of equipment and defence goods industries rose at an annual rate of 23 per cent. There was pressure not only on capacity but also on the labour market, as unemployment declined to 4 per cent. by January and was further reduced thereafter. And prices started an accelerated rise that was to carry on throughout the year. From balanced growth, the atmosphere had become one of inflationary boom.

With much public discussion of the pros and cons of the matter, the government hesitated all through 1966 over the advisability of curbing private demand by a strong tax increase. It did, however, introduce several fiscal measures in March which cancelled reductions in excise taxes that had come into force in January and increased the withholding tax on individual income. In April an appeal was made to business to reduce capital spending plans and in September the 7 per cent. tax credit on investment in machinery and equipment and the provision for accelerated depreciation on new buildings were suspended.

In the Federal Reserve System the policy requirements of the situation were more clearly evaluated as the demand for credit became excessive and other signs of booming demand appeared, and monetary policy was soon directed to the task of restraint. In December 1965 the discount rate was raised from 4 to 4½ per cent. and the ceilings under Regulation Q from 4–4½ to 5½ per cent. on deposits of thirty days or more. As this measure aroused some controversy in Washington circles, it was not followed up immediately by other restraining actions. But gradually the grip of tight money became apparent in financial markets, reaching real stringency by the late summer, and interest rates went up to levels that had not been seen for decades.

While the monetary measures were being intensified, business demand for bank loans remained high, partly anticipating future needs. But, none the less, monetary policy attained its objective of dampening total demand as the year wore on. The sharply lowered rate of demand increase in the second quarter must be attributed to a natural settling-down of the buying wave that had occurred during the previous six months. However, the continuation of more moderate demand after that and the real easing towards the end of the year and in the first quarter of 1967 were due to monetary restraint. As mortgage funds became more expensive and harder to get, residential construction dropped sharply; automobile sales declined, and the rise in business investment outlays was greatly reduced. These developments are indicative of the ways in which room was made in the economy for growing defence expenditure with a lessening of inflationary pressures. In fact, by late 1966 the easing of demand led to substantial involuntary inventory accumulation.

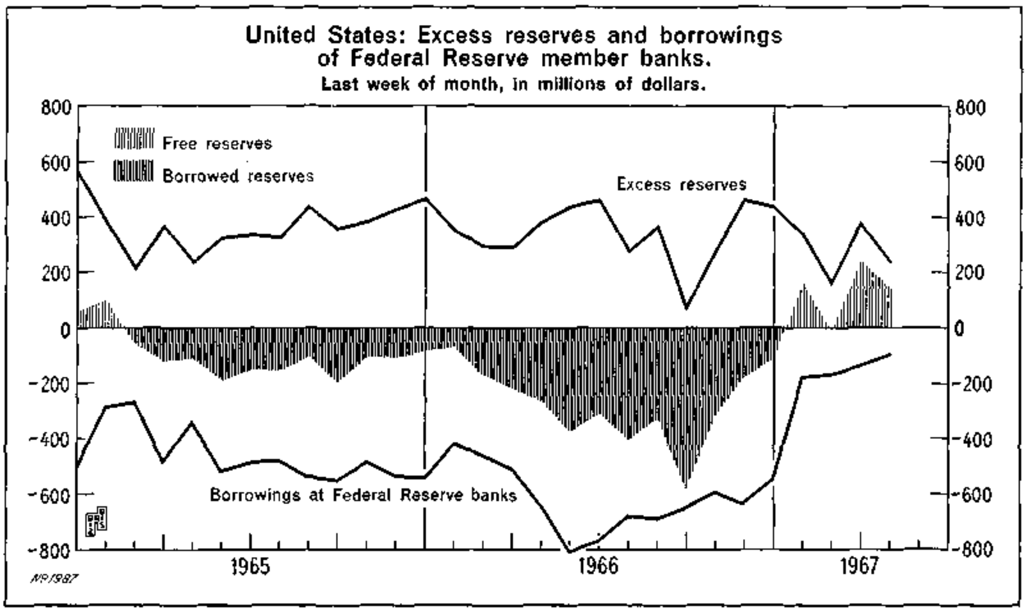
Excess demand inevitably led to rising prices. Consumer prices went up by 3.7 per cent. over the twelve months to October 1966 and wholesale prices by 3 per cent.; while the gross national product in real terms increased by 5.4 per cent. in 1966, the rise in nominal terms was 8.6 per cent. Furthermore, the wage guide-lines that had been closely adhered to for several years did not hold after the middle of the year, and the wage round at higher rates has continued in 1967 despite the change in the labour-market situation.

The forces operating in the domestic economy also led to a significant deterioration in the US external payments position. Directly linked to the war in Vietnam, military expenditure abroad increased by about $1 milliard at an annual rate from mid-1965 to the last quarter of 1966. In addition, the spurt in demand spilled over into imports, which increased by 19 per cent. in 1966, the major upsurge taking place in the first three quarters. The rise was concentrated on manufactured goods, both consumer and capital, as domestic capacity was strained and delivery schedules lengthened. In fact, capital goods imports advanced by 65 per cent. Even though exports were doing well, the trade surplus, exclusive of government-financed exports, declined to $730 million — down $1.3 milliard from the year before. As demand slackened towards the end of the year, the growth of imports began to subside and was quite small in the early months of 1967. Exports continued to show strength, however, so that the adverse movement of the trade balance was partially reversed.

The worsening trade position and larger overseas military costs were partly offset by a significant improvement in the balance on long-term capital account in 1966. The main factors contributing to this were the high interest rates prevailing in the United States and the voluntary restraint of capital exports. Thus, there was a $2 milliard inflow of foreign longer-term funds in 1966, compared with practical balance in 1965. This included a large shift into longer-term certificates of deposit and government agency securities, a good part of which was placed by international institutions and foreign monetary authorities. In addition, the outflow of US private long-term capital was reduced by $0.9 milliard from the figure of some $4.4 milliard in 1965. US firms financed a larger proportion of their foreign investments through new security issues in Europe and the resultant long-term inflow partly offset the $3.4 milliard direct investment outflow. Owing to the strong domestic demand for credit there was also a moderate reduction in long-term US bank loans to foreigners, and net purchases of foreign securities by US residents declined slightly.

As a result of these varying influences the balance-of-payments deficit increased on the liquidity basis from $1.3 milliard in 1965 to $1.4 milliard last year. However, the deterioration would have been sharper had it not been for the shift from liquid to non-liquid investments by foreign official institutions. In addition, net military prepayments by Germany contributed to the inflow of official funds, and $0.4 milliard of debt prepayments was received from France, Italy and Germany.

In the domestic economy inflationary demand pressures had clearly abated towards the end of 1966. While the Federal Reserve had acted to relieve the stringency in financial markets in the autumn, it definitely shifted to a policy of monetary ease in December through large open-market operations. Non-borrowed reserves resumed their growth in November and December,

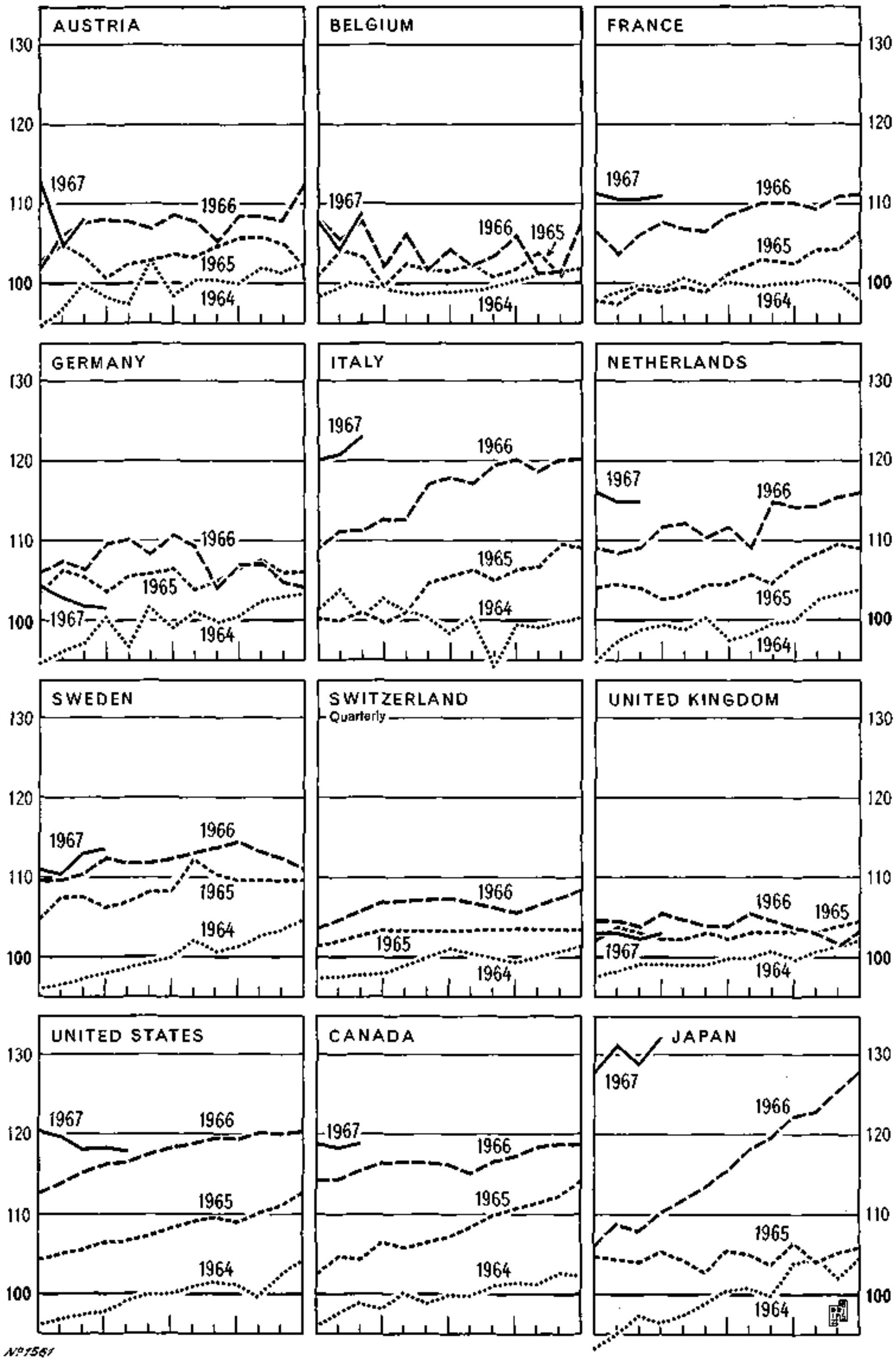


and just before the year-end the Federal Reserve rescinded the request addressed to banks in September to restrict business loans. The policy towards easier money was continued in early 1967. In March member-bank reserve requirements on savings deposits and, in part, on time deposits were reduced from 4 to 3 per cent., and early in April the discount rate was lowered from 4½ to 4 per cent. With US interest rates declining, the programme to curb capital outflows in the coming year was strengthened in December. With effect from January 1967, the interest equalisation tax was raised from an equivalent of 1 to 1½ per cent. and extended for another two years.

When the Federal budget was presented in January, the government had to make a difficult assessment of the emphasis to be given to fiscal policy. On the one hand, demand for the time being had stopped expanding and there was no immediate need for it to be restrained further. On the other, a very large budget deficit was in prospect. Besides this, easier money was likely to bring some revival to sectors like housing, wages were rising and a further increase in defence expenditure seemed probable. On balance, it was considered that a revival of demand was likely by the second half of 1967, so that a tax increase was called for. The proposals were for a 6 per cent. surcharge on individual and corporate income taxes with effect from 1st July and a rise in social security taxes as from 1st January 1968. As total demand continued to flag in the spring months, however, the 7 per cent. tax credit on investment in equipment and the provision for accelerated depreciation on industrial and commercial buildings were restored. There was also a release of some previously frozen Federal budgetary funds for highways and other projects. It was not yet evident what action Congress would take on the proposed tax increases.

To sum up, the situation in the United States echoes a familiar refrain: the boom has ended, but the wage-push lingers on. So does the external deficit!

Industrial production.
Adjusted monthly indexes: 1964 = 100.



Germany.

The situation in Germany has been somewhat similar to that of the United States in that severe monetary tightness was the main instrument used to combat an inflationary boom. Of course, the process extended over a longer time span in Germany, but in both countries excess demand was brought under control. In Germany, however, there was not rising defence expenditure to put a floor under the reaction, and policy has had to be shifted more deliberately to promote recovery.

As far back as 1964 the expansion in Germany led to over-full employment and inflationary strains in the economy. With the fiscal position strongly expansionary, it was the Bundesbank that applied the brakes. A first move was made in the summer of 1964 by increasing minimum reserve requirements. Subsequently, monetary policy was tightened step by step by all possible means. As a result, bank liquidity came under considerable pressure, bank credit and capital-market funds became scarce and interest rates went up to almost prohibitive levels. However, as government spending remained expansionary until well into 1966, it took some time for the central bank's restraint measures to bite. Nevertheless, by the spring of 1966 their effect was making itself felt, the upswing came to a halt and soon a decline set in.

This reversal was clearly reflected in the fall in new domestic orders, which, after reaching a peak in March and April, had contracted roughly 10 per cent. by the end of the year. Even more pronounced was the decline of 17½ per cent. in the value of building projects over the same period. Industrial output decreased, too, although as there was a considerable backlog of orders in the spring of 1966 the fall between then and the end of the year was only 4½ per cent. Once the backlog had been worked off, the decline accelerated.

The cyclical change was also evident in labour-market developments, though unemployment did not begin to rise until the autumn. By February 1967, however, the total of persons out of work had risen to 674,000, against only 236,000 in February 1966. In addition, short-time working, almost unknown for some years, had increased considerably and the number of foreign workers fell between September 1966 and January 1967 by almost 20 per cent. This was partly seasonal, but it is expected that a substantial proportion of those at present in their home countries will not obtain fresh contracts. The turn in the cycle is shown also in the unusually sharp decrease in vacancies from 622,000 in March 1966 to 275,000 in February 1967.

On the demand side, the main factor in the cyclical downturn was the weakening of investment activity in both the private and the public sectors, and it was, in fact, the capital goods industries, together with the building sector, that suffered the strongest setback. The national accounts show that gross fixed investment in money terms was actually 1.1 per cent. lower in the second half of 1966 than in the corresponding period of 1965. This contrasts sharply with the 7.4 per cent. increase for the January–June period. The divergence was more marked in purchases of equipment: in the first half of 1966 they showed a 4.6 per cent. rise on the level a year earlier, but in the second half of the year they recorded a 5 per cent. fall. Household demand, too, tapered off in the summer and growth rates for private consumption fell — in line with income developments — from 9 per cent. in the first half of the year to 4 per cent. in the fourth quarter, both compared with the same period of 1965.

The advance of prices began to slow down in the middle of the year. Industrial goods prices, which had climbed steadily throughout 1965 and had risen even more sharply in the early months of 1966, have remained more or less unchanged since last summer. The cost of living, on the other hand, continued to go up until recently — mainly owing to the persistent rise in rents and a fresh upswing in food prices — but the increase was more moderate than before. The rise of wages, which had previously averaged about 9 per cent., did not ease up until late in 1966.

The recessionary trend at home was counteracted, though only to a small extent, by foreign trade developments. As delivery schedules shortened in Germany, exporters intensified their sales efforts abroad, where demand was still active. Consequently exports rose sharply in 1966, with a 12.5 per cent. gain for the year. At the same time — also owing to cyclical factors — imports levelled off and eventually decreased. With these divergent developments, the external current account shifted back from a substantial deficit in the period January–June to an even higher surplus in the latter half of 1966. For the year as a whole a surplus of DM 0.4 milliard was recorded, against a deficit of DM 6.1 milliard in 1965. However, the effect on the liquidity of the economy of this large shift was to some extent weakened by a decrease in the net inflow of capital (excluding special government transactions) and a change in leads and lags of DM 2.8 milliard.

As the easing tendencies in the economy strengthened, the Bundesbank had to take account of the fact that wages were continuing to mount and fiscal developments — the most expansionary factor in the previous upswing — were still obscure. Initially, therefore, the policy of monetary restraint was maintained, although the effects of the increasing external surplus on bank liquidity were accepted.

Around the turn of the year the situation was clearly different: wages and prices had almost ceased to rise, a solution to the fiscal problems seemed in sight, and, above all, unemployment was rising. In view of these developments, the Bundesbank adjusted its policy drastically. From December onwards minimum reserve regulations were amended and requirements cut in three stages, the discount rate was brought down gradually and selling prices for money-market paper were lowered accordingly. While the effect of easier money on domestic interest rates was somewhat limited by an outflow of funds, rates have receded. This has been more pronounced in the short-term area than in bond-market yields — which are still around 7 per cent. Credit demand, on the other hand, has not reacted accordingly, and so far only the public sector has taken advantage of the banks' increased credit facilities.

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	Plant and equipment	Dwellings			
		in percentages							
Austria	1964	3.9	6.3	9.0	9.4	7.2	7.7	7.7	6.8
	1965	5.1	− 1.1	4.7	4.8	4.0	6.5	9.2	2.4
	1966	5.1	4.5	7.3	.	.	6.3	10.4	4.3
Belgium	1964	4.1	4.2	12.9	5.3	46.2	12.7	11.2	6.6
	1965	3.5	5.2	1.2	1.6	0.1	8.8	7.7	3.3
	1966	3.0	4.0	4.0	6.0	− 2.5	7.0	9.5	3.5
Denmark[1]	1964	6.6	8.0	19.2	17.4	28.3	8.8	19.9	8.0
	1965	4.6	3.7	6.9	7.0	6.3	8.0	7.1	4.6
	1966	4.1	4.3	4.6	4.8	3.8	2.7	5.7	2.4
Finland	1964	5.9	6.7	3.3	7.6	− 9.3	5.7	19.1	6.7
	1965	4.7	3.6	8.5	8.1	10.0	4.6	6.5	5.5
	1966	4.0	4.0	2.0	2.5	1.0	5.0	3.0	2.0
France	1964	4.7	4.6	10.1	7.8	16.9	7.7	12.4	5.9
	1965	3.9	3.9	5.2	1.8	14.9	11.3	3.6	4.2
	1966	4.7	3.3	7.4	10.4	0.0	7.1	11.1	4.8
Germany	1964	5.4	− 1.2	12.0	13.0	8.4	10.4	10.9	6.6
	1965	6.1	6.6	6.9	8.7	− 0.6	7.1	14.8	4.8
	1966	3.2	0.3	0.5	0.0	2.6	10.3	2.1	2.6
Italy	1964	2.5	3.4	− 6.5	−11.9	6.0	11.6	− 5.1	2.8
	1965	2.2	3.6	− 8.4	− 9.6	− 6.0	20.8	1.9	3.5
	1966	5.7	3.6	3.7	6.1	− 0.9	12.5	13.4	5.5
Netherlands	1964	6.1	2.8	16.9	14.7	28.8	12.1	14.3	9.3
	1965	7.8	0.9	5.1	3.6	12.1	9.1	7.3	5.4
	1966	3.9	2.6	7.6	7.5	8.1	5.5	8.0	4.3
Norway[1]	1964	4.0	4.6	1.5	1.0	4.5	10.7	8.1	4.9
	1965	3.2	8.8	8.7	9.6	3.6	7.3	9.6	5.7
	1966	4.6	3.8	4.8	5.6	− 0.6	7.6	7.9	4.3
Sweden[1]	1964	5.3	5.1	7.0	5.8	11.1	10.6	10.0	7.6
	1965	4.4	6.5	4.0	4.1	3.7	4.0	11.0	3.5
	1966	1.5	4.4	3.5	6.0	− 4.0	5.1	2.9	2.6
Switzerland	1964	4.8	4.1	8.9	8.4	10.6	6.8	8.7	5.1
	1965	3.5	0.8	− 1.4	− 1.3	− 2.1	12.0	3.1	4.2
	1966	2.2	5.8	− 0.7	− 0.4	− 1.8	5.8	4.1	2.3
Total for above countries	1964	4.7	2.7	8.4	7.3	12.8	10.0	9.9	6.0
	1965	4.5	4.7	4.1	4.3	3.4	10.0	8.4	4.3
	1966	4.0	3.0	3.3	4.1	1.1	8.1	6.9	3.8
United Kingdom	1964	3.8	1.9	17.0	14.7	26.8	3.9	8.6	5.8
	1965	1.7	3.5	3.5	3.8	2.4	5.3	2.0	2.2
	1966	1.6	3.2	0.8	1.8	− 2.9	3.0	2.6	1.4
United States	1964	5.8	1.1	6.3[2]	8.9	− 0.8	13.4	5.3	5.3
	1965	6.0	2.1	8.0[2]	11.3	− 2.0	2.5	10.7	5.9
	1966	4.9	8.4	5.1[2]	9.7	−10.2	10.2	17.4	5.4

[1] In the case of Denmark, Norway and Sweden the official data for domestic investment include maintenance and repairs; these are excluded from the above figures. [2] Private investment and new civil public construction.

In government policy, too, account had finally to be taken of the change in economic conditions. In the autumn, when the first fiscal estimates for 1967 were made, attention was focused on budget-balancing. Earlier investment programmes and appropriations for current expenditure pointed to an automatic increase in 1967 budgetary outlays which it seemed impossible to cover in the light of revenue forecasts and the tight situation on the financial markets. The authorities therefore tried to cut down expenditure and raise revenue.

The original budget, presented in September, foresaw an increase in Federal expenditure of over 7 per cent., so that changes in fiscal legislation were proposed to reduce the deficit by DM 3.5 to 0.5 milliard. But, as the economic downswing made itself felt and had repercussions on tax receipts, the expected deficit tended to grow at the same time as the recessionary trends limited the scope for deflationary action. The budget, as modified up to the end of January, proposed to augment revenue mainly by increasing taxes on consumption, abolishing tax concessions and speeding up tax collection. On the expenditure side, cuts were envisaged in subsidies and social expenditure, but there was also to be a shifting of burdens onto other bodies or into the future.

While the budget deficit was not very large as presented, the estimates did not take into account further cyclical declines in receipts already considered likely. In departing from the previous aim of running a roughly balanced budget, the government has turned for the first time in many years to an anti-cyclical approach to fiscal policy, which in the circumstances called for deficit-spending.

Besides the regular budget, this policy was implemented by a "contingency budget" announced in January, which provided for credit-financed investment expenditure of up to DM 2.5 milliard. DM 850 million of this sum was already appropriated by March, mainly for additional capital outlays by the Federal Railways and the Postal Administration and for road construction. In addition, in order to stimulate private investment, special depreciation allowances were granted to industry for a period of nine months.

As of the late spring the fiscal stimulus had had little time to make itself felt and monetary ease had not yet brought down the level of long-term interest rates to a point that was encouraging a general upturn in investment. On the other hand, exports were still a sustaining factor and the recession was not deepening. It was reasonable, therefore, to expect economic activity to begin a revival without too much delay. In any case, the authorities announced their intention to take further stimulating steps later in the year if they should be needed.

United Kingdom.

The experiment conducted in the United Kingdom to test the novel theory that forced-draught expansion of the economy would itself eventually right the balance-of-payments deficit was abandoned last July, after more than two years of negative results.

The various measures of monetary and fiscal restraint imposed in late 1964 and in 1965 had slowed down the real rate of expansion but had failed to eliminate the excessive demand, which was still intense in the first quarter of 1966. By that time, too, the balance of payments was no longer showing improvement, as it had in 1965. To meet the situation, the budget of May 1966 introduced new taxes, calculated to yield £386 million in 1966–67, and made a further direct attack on the external problem by means of voluntary restraint on investment in the more developed sterling-area countries and steps to cut back government expenditure overseas.

Of the new revenue that would result from the budget, over 80 per cent. was to come from a new selective tax on employment. As time was required to bring this tax into operation, it was not to become effective before September and had, therefore, no immediate impact upon domestic demand. Productive capacity consequently remained overstretched in the second quarter. Consumer expenditure showed some reaction from pre-budget buying, but was held up partly because the existing prices and incomes policy proved to be more successful in limiting price increases than in restraining the rise in wages. Private investment, financed by heavy capital issues during the first half-year, also remained at a relatively high level and there was steady growth of public current and capital spending. On balance, total final expenditure was a little lower in real terms, but the labour market remained as tight as ever, with unemployment at 1.2 per cent. of total employees — less than a year earlier — and vacancies increasing. Moreover, although the external position was blurred by the seamen's strike in May and June, the trade deficit was seen to be expanding.

Besides these adverse domestic forces, the rise of interest rates in the United States attracted a substantial volume of short-term funds away from London during the first half of the year, which intensified the pressure in the sterling exchange market. This combination of factors caused a weakening of confidence in the pound and in July a major crisis developed. Immediate support of the currency could be met only through heavy borrowing against facilities provided by overseas monetary institutions.

In the face of this crisis, decisive action to ensure a balance-of-payments adjustment became the absolute priority for policy and, more than ever, this implied a substantial cut in internal demand. On 20th July measures were announced which aimed to reduce expected domestic expenditure by over £500 million and, in addition, to cut spending overseas directly by some £150 million. Private demand at home was to be reduced by £350 million by further restrictions on consumer credit, increases in indirect taxes and in surtax, higher post-office charges and the further direct limitation of less essential building. Tighter exchange restrictions were to make a direct contribution of £50 million to the balance of payments. Public expenditure, too, was to be curtailed by cuts of £150 million in domestic investment, mainly by public enterprises, and of at least £100 million in spending overseas, though these were not to be effective until 1967–68.

In addition, a rigid standstill was imposed on incomes and prices until the end of the year, to be followed by a further six months of severe restraint. These direct controls and fiscal measures were supplemented by further monetary action. Some days earlier Bank rate had been raised to 7 per cent. and additional special deposits requested from the banks. At about the same time it was announced that no easing of the ceiling on bank credit would be permitted to offset the squeeze on company liquidity expected later in the year. With the impact of the selective employment tax still to come, the scope and stringency of this programme demonstrated the resolution of the UK authorities.

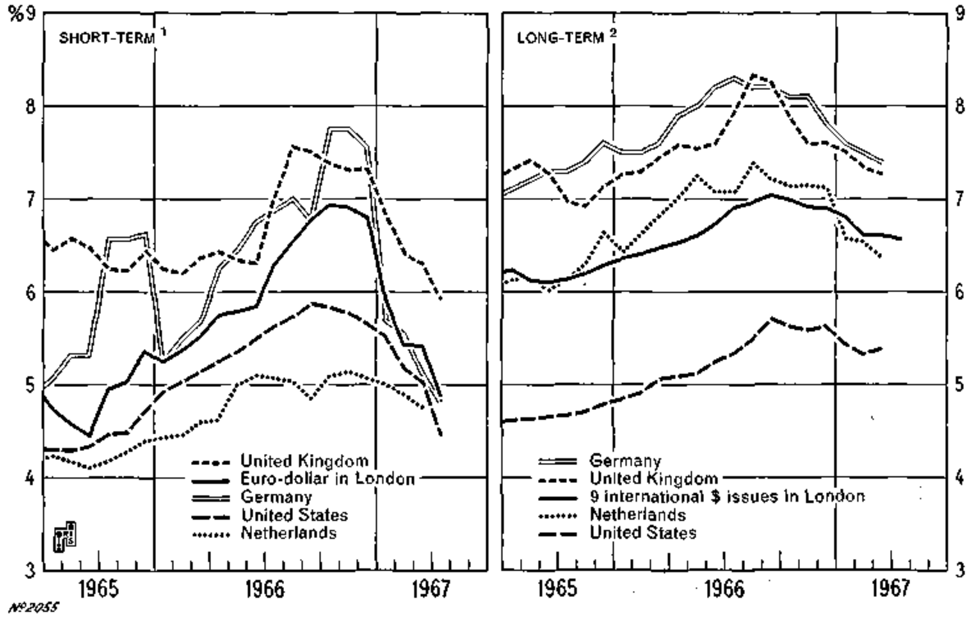
The measures rapidly affected private spending. Consumption in the second half of the year was 2½ per cent. lower than in the first, despite a decline in the savings ratio. The impact was especially heavy on sales of durable goods, with new car sales dropping by about one-third. Private investment, too, declined progressively towards the end of the year. There was, however, some offset from rising public-sector expenditure and higher exports. Although industrial production fell rather sharply after August, total output did not contract significantly but stagnated.

As demand receded, there was a marked decline in business confidence, which had remained so buoyant in the face of earlier restrictive measures. This showed in a prompt falling-off in the demand for finance as investment programmes were curtailed. Many prospective capital issues which had threatened to overburden the market were withdrawn or postponed and long-term interest rates began to decline. Demand for bank advances also fell away and the banks, which had expected difficulty in keeping within their credit ceilings, found themselves with room to spare for priority borrowers.

There was also a rapid adjustment of work forces to the lower level of production — in contrast to the earlier labour hoarding. By the end of the year the number of unemployed had risen to nearly 450,000, 1.9 per cent. of total employees, and reported vacancies showed a comparable fall. This change in the labour-market situation gave support to the incomes freeze, which many had initially suspected of being unrealistic. Hourly wage rates in industry rose at an annual rate of 8 per cent. between January and June but were virtually unchanged after July and the tendency to shorter normal working hours was halted. Retail prices rose by 2.6 per cent. in the first six months of 1966 but by only 1.0 per cent. in the latter half of the year, and even this increase was largely attributable to the tax changes and to seasonal factors.

With quite a short time-lag, the easing in the domestic economy brought an improvement in the balance of payments. Over the year as a whole the current-account deficit was nearly halved, to £61 million, but this improvement was entirely due to a substantial surplus of £135 million (seasonally adjusted) in the fourth quarter. This result was affected by an unusual number of special factors, but the strength of exports at the end of the year and a decline in imports not affected by the removal of the import surcharge in

Interest rates.



[1] United Kingdom: three-month deposits with local authorities; Germany: three-month money-market loans; United States: three-month certificates of deposit (secondary market); Netherlands: three-month Treasury bills.
[2] Germany: industrial bonds; United Kingdom: 20-year debenture and loan stocks; Netherlands: three private bonds (4½—4¾ per cent.); United States: industrial bonds.

November clearly reflected the dampening of domestic demand. The long-term capital account also showed an improvement of £111 million, spread more evenly through the year and almost entirely on private account. The basic balance registered a deficit of £189 million for the year, against one of £348 million in 1965, and a surplus of £121 million in the fourth quarter, despite the resumption of service on the North American post-war loans.

Pressure in the exchange market continued for a time and further drawing on foreign short-term assistance was required in August. The change began later in September, however, and in October a start was made in repaying central-bank assistance. With the substantial easing of monetary conditions in the United States in December, which was coupled with a renewal of confidence in sterling, short-term funds returned to London on a large scale. Furthermore, the balance of payments was in more than seasonal surplus in the first quarter of 1967. These factors together put a large volume of foreign exchange into official hands, enabling the bulk of short-term assistance to be liquidated by the end of March.

The broad picture from 1964 to that time can be summed up as follows. The demands on sterling had come from balance-of-payments deficits in the years 1964–66 and from confidence movements of funds out of London. These had been financed by medium-term borrowing from the IMF and Switzerland of £900 million, by the transfer of £316 million from the Treasury's portfolio to the reserves and by heavy drawings on monetary assistance from abroad. By the end of March sterling balances had been for the most part reconstituted and short-term assistance largely paid off, while the medium-term debt outstanding plus the transfer from the portfolio to the reserves about equalled the previous external deficits — moderately offset by recent surpluses.

On 25th May the United Kingdom repaid to the IMF $405 million of the $1 milliard that it had drawn in December 1964. The sum repaid corresponded to the total of GAB credits granted to the IMF in connection with the 1964 UK drawing. At the same time the $80 million credit granted by Switzerland to the United Kingdom in December 1964 was also repaid.

By the end of 1966 the UK economy had absorbed the initial shock of the July measures. After November industrial production stabilised; similarly, both the rise in unemployment and the drop in the number of vacancies moderated around the turn of the year. The decline in consumer spending appeared to level off and some rise in wage rates was to be expected. Although private investment continued to fall, it had been given a mild stimulus by an increase in grants on investment expenditure incurred over the next two years, and by the accelerated payment of such grants. Interest rates were well below their peak and, with short-term rates abroad declining, Bank rate was reduced to 6 per cent. by mid-March. Moreover, although the July programme had foreshadowed a reduction in public-sector expenditure for the coming fiscal year, the official estimates showed that public investment in particular would continue to be an expansionary factor. And, although sterling had recovered in the first quarter, it was essential not to jeopardise the improvement on external account.

The budget of April 1967 was based on the expectation that output during the calendar year 1967 would rise by 3 per cent., or at about the

United Kingdom: The budget.

Items	Financial years			
	1965–66	1966–67		1967–68
	Results	*Estimates*[1]	*Results*[2]	*Estimates*[1]
	in millions of £ sterling			
Revenue				
Tax revenue	8,324	9,626	9,371	10,679
Other receipts	821	893	908	1,025
Total revenue	9,145	10,519	10,279	11,704
Expenditure				
Supply services	7,140	8,023	8,108	9,507
Consolidated Fund standing services	1,316	1,449	1,433	1,560
Total expenditure	8,456	9,472	9,541	11,067
Surplus	689	1,047	738	637
Consolidated Fund loans (net)	− 1,265	− 1,334	− 1,478	− 1,580
Overall deficit (—)	− 576	− 287	− 740	− 943

[1] After budget changes. [2] Preliminary.

underlying rate of growth of productive capacity. As this outlook was consistent with the current objectives of policy, the budget made only minor tax changes.

As presented, the budget anticipated an increase in revenues of £1,425 million as against a rise in expenditure of £1,526 million. Consolidated Fund lending, especially to the nationalised industries, was expected to increase by £102 million, so that the overall deficit would rise from £740 to 943 million. This fiscal stimulus, in conjunction with the large size of the deficit, was not without risk and required restraint of possible renewed inflationary forces from the private sector.

Borrowing on this scale could clearly generate excessive monetary liquidity. To meet this danger, the budget amended the terms of issue of certain forms of non-marketable government debt in order to promote saving, and, although the credit ceiling was abolished for the clearing and Scottish banks, these banks are to continue to be controlled through the more flexible use of special deposits. For other banks and finance houses direct restriction is retained for the time being.

Continued restraint will also be applied to prices and incomes, although some relaxation of the criteria against which proposed increases will be measured is in view. The government is to retain statutory powers to delay increases but expects that the lower pressure of demand will reduce the necessity for official intervention.

A feature of the past two years has been the resistance of the UK economy to restraint and the severity of the measures eventually necessary to create the conditions required for external recovery. Besides the excessive rise of wages, a fundamental factor in this has been the expansionary rôle of public-sector expenditure, which, however desirable in itself, has not been accommodated to short-term demand management. A major share of the adjustment has consequently fallen on private investment. Since longer-term easing of the balance-of-payments constraint is directly linked with such investment, it is important that when business spending recovers the demands on the economy from the public sector be tailored to make room for it.

France.

With economic policy directed to expansion, the recovery in France which began in the spring of 1965 continued at a rapid pace until the end of the summer of 1966. Since then the increase in activity has slowed down as a result mainly of some slackening in consumer demand and of a weakening in exports, primarily in those to Germany and the United Kingdom. By the spring of this year activity was in a sideways movement, not too different from that in other countries of the Continent. For 1966 as a whole, however, the increase in the gross national product reached 4.8 per cent., compared with 4.2 per cent. the year before, and industrial output was more than 6 per cent. higher than in 1965.

The main forces behind this increase were the continued rapid advance of public investment outlays and a satisfactory revival of private productive investment; the latter was stimulated by a 10 per cent. tax credit introduced in February 1966 and applicable up to the end of the year. In contrast to 1965, private demand for housing weakened and led to a decline in building-sector activity.

With important elements of the 1963 stabilisation programme — namely budgetary strictness and a prohibition on price increases — remaining in force, economic growth has not been accompanied by significant inflationary pressure. Indeed, the price rise of 2.8 per cent. at the retail level and near-stability at the wholesale level was equal to or lower than that recorded in 1965, while wage increases tended to slow down somewhat. Apart from price controls and public-sector incomes policy, other factors, such as more intense competition from abroad, which was encouraged to some extent by the removal of some import restrictions, and a progressive easing of the labour market, also played a rôle.

As regards the balance of payments, while 1966 as a whole showed a surplus, a reversal occurred in the course of the year. The previous large surplus was maintained in the first half of the year but has given way since the autumn to a deficit. Most of the deterioration was in the basic balance, both long-term capital and current transactions. Imports continued to rise with domestic activity, whereas exports tapered off as the boom in neighbouring countries faded. Net invisible receipts were smaller, and the previous inflow of long-term capital was much reduced by tight money and high interest rates abroad.

In the monetary sphere, while quasi-money and liquid savings kept growing rapidly, the increase in the money supply was moderate and, in contrast to preceding years, not higher than that in the gross national product in current terms. Following the balance-of-payments developments, the flow of domestic liquidity arising from the external factor steadily declined in the course of the year and has shifted to liquidity absorption since the autumn. For 1966 as a whole the flow of savings to the Treasury was more than enough to cover the budget deficit of some Fr.fr. 2 milliard and permitted the draining-off of some liquidity. Consequently, bank credits to the economy, which in 1966 rose by 15 per cent., have become the only source of liquidity. In view of this development and of the flagging condition of the economy, the Bank of France completely removed credit restraints in February 1967.

With the economy in a reasonably balanced position, the authorities have taken the opportunity to make further progress in financial reforms. Freedom in financial relations between France and foreign countries was re-established as from 31st January 1967. This involved the abolition of all exchange control regulations and the introduction of full convertibility of the franc and complete freedom for transfers into or out of France of all means of payment, securities and gold. In addition, a flexible system of reserve requirements for the banks was introduced to replace the former "coefficient de trésorerie" and the scope of activity of both banks and savings institutions was enlarged. Although certain transactions — especially those concerning direct foreign investment and foreign securities issued in France — are kept subject to control, these liberalisation measures represent a basic change, which should have a lasting effect on the French economy.

While the new freedom in financial relations will give wider scope for initiative to the private sector, which is indeed its purpose, it implies less latitude in the conduct of official policy. The monetary authorities have already had to take account of the increased influence of interest rate levels abroad. Open-market operations have had to be broadened and the authorities have intervened for the first time as a seller on the market to maintain internal rates at levels necessary to avoid large outflows of funds. And, in the future, the need to maintain sound budgetary policies and to avoid significant acceleration in prices and wages will be reinforced.

Netherlands.

In the Netherlands the wage explosion of late 1963 had propelled the economy into a roaring boom which led the central bank to adopt a tight monetary policy to bring the situation under control. Although real expansion and overall monetary demand were much smaller in 1965 than the year before, this was due more to physical limitations than to a firm grip of policy on market forces. Hence, at the beginning of 1966 the Netherlands economy was entering another year with over-full employment and strong inflationary pressures.

Given this situation, the restrictive monetary policy was maintained. It was directed also that long-term lending be kept in line with the accrual of long-term funds. In addition, the government's policy, which had previously been an expansionary influence, was modified somewhat. Tax increases and other fiscal measures were planned to reduce the budget deficit in 1966 to substantially less than in 1965. Against this background, fairly balanced growth was anticipated for 1966 and an external surplus seemed in prospect.

Actual developments early in the year, however, pointed to a new strengthening of inflationary pressures. Bank credit in the first four months was growing at an annual rate about twice as high as had been laid down in the restrictive measures. In addition, it became apparent by the spring that central-government expenditure — mainly on transfers and salaries — was increasing more than estimated and that a budget deficit in excess of that for 1965 was to be expected. At the same time the price rise was accelerating and the trade deficit widened considerably.

In view of the situation, new corrective measures were initiated. The central bank raised the discount rate on 2nd May and lowered the permissible annual rate of expansion of short-term bank credit. The government introduced a new programme under which wage rises were to be limited to 7 per cent.

in 1966 and prices were generally to be kept at their end-May level. In addition, government investment projects were postponed and the recruitment of new civil servants was prohibited. Finally, financing through the Bank for Netherlands Municipalities, introduced in 1965 to protect the capital market, was restricted to really urgent requirements.

These measures were fairly successful, although the government's deficit remained quite large. Between April and December the banks absorbed the excess over the norm in short-term lending. The directive on long-term lending was also respected. A side-effect, however, was that banks shifted away from portfolio investment and thus curtailed the supply of funds to the bond market. On the capital market, existing tensions increased and, with demand still high, interest rates went up to 7 per cent. for new government loans and to almost 8 per cent. for mortgage loans. The very tight market induced the public sector to cover its financial needs to a greater extent by short-term borrowing. After the middle of the year, however, capital-market rates became stable and towards the end of the year they even turned down somewhat.

These financial strains, together with slackening foreign demand and some curtailment of public investment, exercised a retarding influence on economic activity. Industrial production rose more slowly after August, new orders in the metal industries remained virtually stationary and, above all, labour-market strains diminished. The number of vacancies on an adjusted basis dropped from about 85,000 in the late spring of 1966 to 47,000 in March 1967; the rate of unemployment increased over the same period from slightly more than 1 per cent. to 2.5 per cent.

In 1966 as a whole the real gross national product increased by 4.3 per cent., against 5.4 per cent. in 1965, though, with the balance of payments shifting from surplus to deficit, the percentage rises in real national expenditure were the other way round. The main forces behind the increase were sharp rises in private productive and public investment and in government consumption. In contrast, the growth rates for household consumption, residential building and exports decreased. It was, none the less, a year of greater price inflation; consumer prices were up by 6 per cent. (partly because of excise taxes), compared with 5 per cent. in 1965, and investment goods prices were 5.5 per cent. higher, as against 4 per cent. in the previous year.

As already indicated, however, the pressure of inflation was at full strength only in the first half of the year and waned in the second half. By the early months of 1967 prices were reasonably stable and overall economic activity was making little headway. Imports had lost momentum more than six months before and the balance of payments was close to equilibrium. Permissible wage increases had been fixed at 4 per cent. for the first half of the year and 1.5 per cent. for the second.

At the start of 1967 the prospects for the year were judged to be reasonably good. But more recent developments have indicated a further slackening of business activity. Unemployment, in particular, continued to increase, and in certain structurally weak regions it rose to high levels. This induced the government as early as January and February to provide special assistance by granting investment incentives and releasing funds to create employment in the areas in question. Monetary policy, too, has been adjusted; in March the discount rate was reduced and it was announced that banks exceeding the lending ceiling would not have to make penal deposits with the Nederlandsche Bank.

Belgium.

The change in trend which occurred last year in most industrial countries was quite marked in Belgium. Recovery strengthened considerably in the early months of 1966 and, while capacity was not hard pressed, the expansion was accompanied by accentuation of inflationary strains. Hence, in April and May the authorities again took stabilisation measures; steps were initiated to slow down the increase in public expenditure and to impose a three-month freeze on the prices of goods and services. In addition, bank credit was restrained by a rise in the discount rate in June.

Although these mild measures may have had some effect, they probably played only a small part in the shift to a declining rate of expansion that emerged during the summer and still prevailed in the spring of this year. Other factors, such as the weakening of exports and the flagging of domestic private demand, were the main forces at work.

As in neighbouring countries, the export decline was mainly in shipments to Germany; it explains the current-account deficit as well as the bulk of the overall deficit in the balance of payments, which came to B.fr. 5.9 milliard, in contrast to a surplus of B.fr. 8.5 milliard in 1965.

As a result of the various dampening influences, industrial production last year was weak after its early upswing, and in December 1966 it was back at the same level as twelve months earlier. There were fair margins of idle capacity and the number of unemployed rose. The gross national product increased over the year by about 3.5 per cent. in volume terms, or only slightly more than in 1965, the improvement being due to the upswing during the first quarter.

Although price pressures were strong early in the year, the abatement of demand after the first quarter served to dampen them and in December the retail price index was at about the same level as in June. The total increase for the year was 3.2 per cent., compared with 4.1 per cent. in 1965. Since January 1967 prices have been freed altogether, except for the obligation to give advance notice of increases. While price pressures weakened in 1966, wages, despite the easing in the labour market, continued their rapid rise, gross hourly earnings going up by 10 per cent. over the year, compared with 7.6 per cent. in 1965.

In view of continued inflationary pressures, now of the cost-push variety, the authorities have eased the monetary situation only moderately. While the official discount rate was reduced in February, in March and again in May 1967, partly in line with developments abroad, the limitations on the expansion of credit introduced in April 1966 were extended for the first six months of this year. However, on the basis of a new law granting the government special powers to revive the economy and ensure budget equilibrium, several measures were taken in April 1967. They aimed to promote investment through a Fund for Economic Expansion and Regional Reorganisation of B.fr. 5 milliard and by granting fiscal advantages for new investment. They provided also for increased taxes to yield B.fr. 1.5 milliard in 1967.

Switzerland.

During the past year the Swiss authorities succeeded in combining full employment with balance-of-payments equilibrium, but the problem of a rather high rate of price increase has remained. While the growth of the gross national product in real terms declined from 4.2 to 2.3 per cent., the slowdown in current prices was only from 7.8 to 7.2 per cent. At the end of 1966 the consumer-price index stood 4.6 per cent. above its level a year earlier.

The anti-inflationary measures which had been taken in 1964 were quite effective in slowing down the growth of private domestic demand. Total investment, which in constant prices advanced at a rate of 8.9 per cent. in 1964, declined by 3.5 per cent. in 1965 and by another 0.9 per cent. in 1966. The situation of chronic excess demand in the building sector has been remedied and private consumption has continued to expand at a lower rate than gross national expenditure.

The stabilising effects of the various anti-inflationary measures were, however, largely offset by the continued buoyancy of current public expenditure and exports. In 1966 public consumption advanced at a rate of 11.5 per cent. in current prices and exports went up by 9.8 per cent.

A second reason for the failure of economic policy to show major results in the field of prices was that inflation has been taking on much more of a cost-push character. The government's restrictive policy with respect to foreign labour has tended to increase the tensions in the labour market. The upward adjustment of the Swiss interest rate level, which had been rendered inevitable by the rise in interest rates abroad, has, in view of the high mortgage indebtedness of the Swiss economy, contributed to the upward movement of rents. A third autonomous factor behind the upward trend of prices has been the principle of granting agriculture a certain income parity with earnings in industry. As long as wage increases completely absorb industrial productivity gains, and thus rule out any offsetting downturn of industrial prices, this policy inevitably leads to some wage/price spiral, which does not readily lend itself to the conventional treatment of restricting aggregate demand.

Apart from its price record, the Swiss economy's performance in the past year was an impressive one. The slower growth of the gross national product was partly due to government policy, which prescribed another 5 per cent. reduction in the foreign labour force between March 1966 and January 1967. In fact, at 3.3 per cent., the rate of increase in gross national product per person employed was about as high as during the preceding boom years. Industrial production, despite a 1.3 per cent. decline in the industrial labour force, stood in the fourth quarter of 1966 4.4 per cent. above its level a year earlier. Even after its recent slow-down, investment still accounts for over a fourth of the gross national product, which is one of the highest proportions recorded in the industrial countries. In addition, after five years of deficits, the Swiss economy in 1966 achieved a substantial current-account surplus in its balance of payments.

Sweden.

The momentum of overall demand in the Swedish economy, which had been strong since 1963, abated in the course of 1966. This change was due firstly to policy restraint carried over from the previous year and secondly to the lowering of tensions in other countries, particularly Germany. Since the easing was moderate, merely dampening the earlier tendency to overheating, there was no let-up in pressure on commercial-bank liquidity in the first half of the year, and in June the official discount rate was increased to 6 per cent. and the penalty rate to 12 per cent.

The slackening of demand last year was evident in the case of both households and firms. Private consumption increased at only about one-third of its 1965 rate, owing in part to protracted wage negotiations and delayed payments. The tight credit situation, combined with stricter building controls introduced in the spring, led to a decline in housing activity. And with a substantial reduction in the accumulation of stocks, total private investment showed little change over the year, compared with an 11 per cent. increase in 1965. This resulted partly from lower profitability and self-financing ability, but credit tightness was also an important restraining influence.

Compared with the reduced rate of growth in the private sector, public expenditure showed less change in 1966. The central government's direct demand for goods and services slackened, partly as a result of the transfer of certain activities to the local level, and for the public sector as a whole growth was somewhat slower than in 1965, owing to measures taken to limit the expansion of local-authority investment. Because of such action and a marked rise in income, the financial position of the local authorities improved in 1966. The budget results of the central government, on the other hand, shifted from a surplus in 1965 to a deficit exceeding S.kr. 1 milliard, primarily owing to an increase in lending and a slower rise in revenue.

With an easing in the labour market, there was a somewhat smaller increase in wage costs. However, this had little immediate effect on the behaviour of prices; consumer prices, excluding the effects of indirect taxes and subsidies, went up by about 5 per cent., or a little more than in 1965, and, while the gross national product rose by 8.8 per cent. in current prices, the real gain amounted to only about 3 per cent.

As after mid-year the slow-down in activity became apparent, central-bank policy was relaxed somewhat. The adjustment of credit policy to market trends was continued early in 1967 and the discount rate was lowered to 5½ per cent. in February and to 5 per cent. in March. While the easier monetary policy was designed to stimulate productive investment, a fee was introduced to discourage certain types of non-priority construction and the turnover tax was increased from 10 to 11 per cent. in March to dampen private consumption.

This combination of measures shows that there is little concern about a significant contraction and, in fact, demand is expected to pick up later in the year. Renewed overheating of the economy this year is not anticipated, however, and reducing the current-account external deficit, which was still considerable in 1966, and slowing down price increases continue to be important objectives of economic policy.

Canada.

After several years of rapid expansion, the slack in the Canadian economy had been progressively taken up. By the end of 1965 gross output was one-third greater than in 1961 and unemployment had been reduced to 3½ per cent., its lowest level since 1956. By that time, however, definite signs of inflationary pressures had appeared; expenditure by the public sector was continuing to rise rapidly and business fixed investment was expanding at boom proportions. To limit the excess overall demand, with its accompanying cost and price pressures, and to maintain the country's external financial position, monetary policy began to be tightened.

A clear shift to restraint was made in the March 1966 budget; government construction expenditure was cut, some depreciation allowances were reduced sharply, and a 5 per cent. refundable tax was levied on after-tax corporation profits. As an incentive to defer investment expenditure, the sales tax on production machinery was to be lowered in April 1967 and abolished a year later. To reduce spending for consumption, personal income tax, except for the lower brackets, was raised as from June 1966, thus reversing the 1965 tax cut. Later in the year these budget restraints were reinforced by some additional measures, including withdrawal of the winter house-building incentive programme, and in a supplementary budget in December the Federal sales tax and the old-age social security tax were raised.

As a result of the various monetary and fiscal measures the investment boom began to taper off in the second half of the year and, although the 16 per cent. annual increase in capital outlays was still large, it was substantially smaller than the 23 per cent. rise indicated by the mid-year review of investment intentions. On the other hand, expenditure on goods and services by the Federal Government rose by 19 per cent., against 11 per cent. in 1965, and, despite the March measures, its net position on a national accounts basis weakened by Can.$ 444 million. Expenditure by provincial and municipal governments rose as usual more rapidly than their revenues.

As in the United States, the extreme tightness of credit had a very uneven effect on different sectors of the Canadian economy, the impact on mortgage borrowers being particularly severe. The lack of mortgage funds had already caused a slow-down in house-building in late 1965 and this trend was intensified last year. Tighter credit conditions and higher taxes also acted as a dampening influence on domestic sales of motor-cars and other durable consumer goods, the steep decline in the stock market serving as a further discouraging factor.

As demand pressures moderated in the summer and early autumn, the Bank of Canada switched to a policy of greater ease. Economic activity was again stronger in the final quarter of the year but there seemed little prospect of renewed overheating. In fact, the survey of investment intentions for 1967 showed total planned outlays on plant and equipment to be about the same as in 1966. The Bank of Canada moved towards easier money, a step which was facilitated by similar action in the United States. Late in 1966 and early in 1967 the government also announced a number of measures designed to stimulate house-building activity and in April there was a lifting of some of the earlier tax restraints on business investment. The estimated increase in government spending should also provide considerable stimulus this year.

Although demand pressures abated after mid-1966, prices and wages rose sharply and about two-fifths of the 11 per cent. increase in the gross national product last year was accounted for by higher prices. Tight labour-market conditions coincided with a large number of contract negotiations and the 6.9 per cent. increase in wages and salaries in the non-farm sector considerably exceeded the productivity improvement. An important objective of economic policy in 1967 will be to arrest the price and wage rise while maintaining a satisfactory rate of growth to employ the rapidly increasing labour force.

Despite the strong expansion last year, the external trade balance improved. On capital account, direct investment inflows increased sharply and new issues floated in the United States rose, but large net purchases were made of US common stocks and there was a substantial outflow of funds through the banking system.

Italy.

Having weathered a serious setback in 1964, the Italian economy last year was an exception to the general recessionary tendency in western Europe; a 5.5 per cent. increase in the real gross national product was successfully combined with a continuing current-account surplus and a high degree of price stability.

The economic recovery, which had begun hesitantly in the spring of 1965, was at first led by an increase in public expenditure and a strong export performance, while the easing of monetary conditions and fiscal incentives to investment were not very successful in reviving private investment demand. In the course of 1966, however, the recovery became more broadly based. Exports remained a dynamic element but, with the gradual reconstitution of profit margins and higher rates of capacity utilisation, private investment also showed signs of improvement. This is reflected in the rise of 6.1 per cent. in total investment, after declines of 8.2 and 7.5 per cent. in 1964 and 1965. Investment in industry went up by nearly 10 per cent. and public-sector investment by 5.4 per cent. Private consumption expenditure, after lagging behind in 1965, expanded at a slightly higher rate than the total gross national product, whereas the increase in current public expenditure (in current prices) slowed down from 12.8 to 6.9 per cent. The growth rate of imports jumped from 2.7 to 16 per cent.

Reflecting the continuing strength of exports, the recovery was most pronounced in the industrial sector (excluding building), which accounted for about two-thirds of the increase in the gross national product. Industrial production advanced by about 11 per cent. between the fourth quarters of 1965 and 1966 and exceeded its pre-recession peak by 18 per cent. Nevertheless, certain branches, such as the textile and building-materials industries, have not yet regained their previous highs. The building sector has remained the chief weak spot in an otherwise fairly bright picture, but here, too, there are indications of an improvement. Thus dwellings completed during 1966 were 25 per cent. down on 1965, but new building permits issued were nearly 10 per cent. up.

The recovery of economic activity was mainly reflected in a return from part to full-time employment. Overall employment actually declined slightly, owing primarily to the weakness of the building sector and a renewed shift of labour from agriculture. The data thus far in 1967, however, point to an improvement in the employment situation.

The continued ease of the labour market has contributed towards moderating the upward trend of wages. Contractual minimum wage rates at the end of December exceeded their level a year earlier by only 4.7 per cent. The decline in the rate of wage increases was in itself one of the major factors behind the slow-down of the upward movement of the automatic wage scale from 10 points in 1964 to 6 points in 1965 and only 3 points in 1966. The cost-of-living index at the end of 1966 stood only 1.8 per cent. above its level a year earlier, while the wholesale-price index showed virtually no increase over the year.

Monetary policy throughout 1966 was directed towards keeping liquidity in ample supply, the main object being to encourage the upswing in investment. This policy also succeeded in insulating the Italian credit market from the interest rate advance abroad and led to a substantial increase in net capital exports, which offset about two-thirds of the total current-account surplus. At the same time net issues of fixed-interest securities on the capital market showed a spectacular rise from about Lit. 2,000 to 2,800 milliard.

The budget was less expansionary than in 1965. The central administration's overall national-income deficit declined from Lit. 819 to 689 milliard. At the same time, however, the Treasury's net financing requirement rose by Lit. 324 milliard to Lit. 1,867 milliard owing to increased government lending for investment purposes. Favourable capital-market conditions enabled the Treasury to finance a larger proportion of its needs by long-term borrowing.

The need for relief, reconstruction and river-control expenditure following the flood disasters led to large tax increases in November. Income tax was raised by 10 per cent. for one year and taxes on petrol, alcoholic beverages and tobacco were increased for two years.

Despite these charges, the outlook for the Italian economy remains favourable. As a result of cyclical developments abroad the growth of exports has slackened but, with the absorption of excess capacity, aggregate demand is likely to receive increasing stimulus from domestic investment.

Japan.

Under the stimulus of an easy monetary policy and expansionary fiscal measures the Japanese economy began early in 1966 to recover from the previous year's recession and the upward movement gathered momentum as the year progressed. A crucial factor in the recovery and its speed was the favourable international environment for Japanese exports, particularly those going to the United States and to neighbouring countries in the Far East. But consumer spending picked up after a period of stagnation, inventories started to be rebuilt, and private equipment investment also soon began to rise, showing a gain for the full year of about 8 per cent.

Under these influences the gross national product, which had registered a gain of 10 per cent. in 1965, went up by another 15 per cent. last year. In 1965, however, about 6 per cent. of the increase had reflected higher prices, compared with 5 per cent. in 1966.

The monetary ease initiated in the previous year was continued throughout 1966 and early 1967. However, credit demand took some time to recover and in the first half of the year bank loans grew at a slower pace than in the same period of 1965. This changed in the second half as the revival of private-sector activity gained momentum, and bank loans then went up more quickly. As to fiscal policy, the new practice of floating government bonds was stepped up in 1966 and there was considerable stimulus from rising government expenditure.

As a result of the situation of monetary ease prevailing in Japan in 1966, domestic interest rates, which had previously been high in comparison with overseas rates, declined relative to the latter. This development led Japanese traders to switch borrowing from overseas to domestic banks. Later in the year and in early 1967 the relationship between overseas interest rates and Japanese rates became more normal, as the former declined from their autumn peaks and the latter tended to rise slightly.

Despite higher economic activity, the trade balance showed a surplus of \$2.3 milliard in 1966, compared with one of \$1.9 milliard in the previous year, as exports rose by 15.7 per cent., while imports grew by 14.4 per cent. This more than covered the substantial deficit on services and transfers, amounting to \$1 milliard, and a deficit on capital account of over \$900 million, leaving an overall balance-of-payments surplus of \$320 million.

In late 1966 and early 1967 there was an acceleration in economic activity and a marked tightening of the labour market. Thus the policy problem began to shift from that of counteracting recessionary tendencies to one of keeping the new expansion under control in order to avoid a cost/price spiral and deterioration in the country's external position. The business recovery being stronger than expected, the government early this year reduced its planned increase in expenditure, at the same time curtailing the scheduled amount of government bond flotations. Central-bank policy has remained one of general ease.

Eastern Europe.

In their plans for last year the eastern European countries anticipated an improved agricultural performance but slower industrial expansion. In the event, output targets in both these key sectors were surpassed almost everywhere, so that the rate of growth of the net material product was generally faster than expected and compared very favourably with the average for the five preceding years. In quantitative terms, therefore, 1966 was clearly successful.

More emphasis has recently been placed on improving efficiency and on adapting output, in terms both of quality and of product mix, more closely to the pattern of demand. It is too early as yet to judge the results in this regard; however, the new approach has produced changes in agricultural policy. Over recent years purchase prices for agricultural products have been selectively raised and consequently also the sector's share in distributed income. This has brought both a relative improvement in rural consumption standards and a rise in agricultural investment, which has also been encouraged by state capital grants and credits. Moreover, industry has been better orientated to supplying the farms with essential inputs, particularly of chemical fertilisers and farm machinery. These policies, together with favourable weather conditions, contributed to the better results in 1966. In the countries where agriculture is proportionately most important global production rose very strongly, by some 15 per cent. in Albania and Bulgaria and by over 11 per cent. in Rumania. After a fall in 1965, output went up by 10 per cent. in Czechoslovakia, and a similar result was achieved in the USSR, where growth has averaged over 8 per cent. a year since the shortfall of 1962–63. In Poland, where farming remains largely in private hands, production increased by 5½ per cent. after a growth of 7½ per cent. in 1965. Only in Hungary, where the losses of the previous year were scarcely made good, were results disappointing.

In the region as a whole the longer-term trend towards slower industrial expansion was expected to continue last year, with a growth target of less than 7 per cent. compared with the 8.6 per cent. achieved in 1965. But plans were exceeded, and production in fact expanded by just under 8½ per cent. These figures are heavily influenced by the performance of the USSR, where overfulfilment of the target by the capital goods sector in particular resulted in an 8.6 per cent. rise in total output — well above the planned 6.7 per cent. and only slightly less than in the previous year.

Eastern European economies:
National income, industrial and agricultural production.

Countries	Net material product			Global industrial output			Global agricultural output		
	1961–65	1966	1966–70 Plan	1961–65	1966	1966–70 Plan	1961–65	1966	1966–70 Plan
	annual increases, in percentages								
Albania	5.7	.	7.4–8.2	6.8	12.0	8.7	5.2	15.0	6.2–7.0
Bulgaria	6.5	11.0	8.5	11.7	12.2	11.2	3.2	15.0	5.4
Czechoslovakia .	1.8	7.0	4.1–4.4	5.3	7.4	5.1–5.4	−0.4	10.0	2.8
Eastern Germany	3.5	4.5	.	5.8[1]	6.5[1]	.	.	.	.
Hungary	4.7	6.0	3.5–3.9	7.9	6.6	5.7–6.3	1.3	5.0–6.0	2.5–2.8
Poland	6.0	6.0	6.0	8.5	7.4	7.6	2.8	5.5	2.4
Rumania	9.1	7.9	7.0	13.8	11.7	10.6–11.6	2.5	11.2	4.7–5.7
USSR.	6.8	7.5	6.6–7.1	8.6	8.6	8.0–8.5	2.3	10.0	4.5
Yugoslavia . . .	7.5[2]	9.0[2]	7.5–8.5[2]	10.8	4.3	9.0–10.0	1.6	16.0	4.6

[1] "Commodity production" after 1964 (i.e. excluding work in progress). [2] Gross material product.

In other countries the difference between output plans and performance was less striking. Faster expansion in mining, in engineering and in the processing industries dependent upon agricultural requirements led to exceptional growth in Albania, Bulgaria and Rumania, where industrial output rose by 12 per cent. Expansion also continued in Czechoslovakia, where the recovery since 1963 is now being consolidated, and in Poland, although here the growth rate declined. Even so, in both these countries production increased by nearly 7½ per cent. Although slower than elsewhere, the industrial growth rate of 6½ per cent. recorded in Hungary and eastern Germany was, in both cases, faster than in 1965. The improvement was particularly marked in Hungary, where activity had been restrained in the previous year as part of a programme to correct the country's adverse balance of payments.

A change to more intensive development is an important aim of the current reforms, which made limited progress last year. In the USSR and Bulgaria new decentralised control techniques were extended to broader sectors of industry, but elsewhere implementation was slow. The need to establish an up-to-date system of wholesale prices, based on full costs, accounts for the delay. These prices will be introduced in Czechoslovakia, eastern Germany, the USSR and Bulgaria during the current year, and are a necessary condition of the wider use of profits as the criterion of enterprise efficiency, to which material incentives will be geared. In several countries this is viewed as a first step towards a situation in which the pattern of demand will exert a direct influence on production decisions through its effect on profits, and in which central planning will operate more through fiscal, credit and interest rate policies and less through statutory directives.

In the longer term these changes may also result in a more flexible management of foreign trade. At present, through the foreign purchasing monopolies, imports are kept within the bounds set by earnings from exports and the availability of foreign credit. Reserves are drawn upon essentially to ease bottlenecks. This policy gave the region as a whole a surplus in external trade over the years 1961–65, although the cumulative surplus during the period was less than $1 milliard on a trade turnover averaging over $34 milliard a year.

The decentralisation process in eastern Europe is similar to that which has been taking place over a much longer period in Yugoslavia. The latest stage in this process came in 1965 with sweeping structural reforms designed to establish market forces as the basis for resource allocation. These changes came at a time when the Yugoslav economy was subject to excess demand, and were therefore accompanied by a policy of credit restraint. Added to the reorientation of output, this policy halved the rate of growth of industrial production in 1965 and again last year, when output rose by only 4.3 per cent. At the same time, record agricultural production, with an expansion of 16 per cent. in 1966, made for a sharp upturn in the gross material product, which went up by 9 per cent. against only 3 per cent. the year before. Despite this improvement, a strong recovery of investment spending in the second half of the year, added to the renewed growth of consumption, caused a return of demand pressure and further restraint was imposed towards the end of 1966.

Under the impact of the reform, which included a 40 per cent. devaluation of the dinar, and of domestic restraint, the balance of payments improved in 1965, when the current account was in equilibrium. Last year saw a further 12 per cent. rise in exports, but the trade balance nevertheless worsened as the result of a 22 per cent. increase in imports. The deterioration on current account, to a $30 million deficit, was less marked, however, thanks to increased earnings from tourism and other services.

The development of global reserves.

The discussions on the reform of the international monetary system in the past few years have been dealing with three basic problems: (1) the means of assuring an adequate growth of global reserves, (2) the improvement of the adjustment process, and (3) the implications for reserve composition of the shortage of new monetary gold. As the various countries put different emphasis on these problems, a coherent conception of the future system has not been arrived at.

To take here only the matter of reserve growth, the problem being discussed may be formulated as follows. Given that fixed exchange rates are a high-priority policy objective, monetary authorities must hold official reserves to defend their rates in the face of shifting market conditions. Moreover, these reserves must grow over time in some relation to the growth of international transactions. At its established price, new gold alone does not meet this need. Nor can reserve growth be met by increased dollar holdings to the same extent as formerly, because the disproportionate rise of dollars relative to gold would itself threaten the stability of the system. Hence, a sound and acceptable means of assuring the growth of reserves is being sought. This need relates to the aggregate of reserves since, if their rise were reasonably adequate, all countries that followed appropriate economic and monetary policies should be able to participate in it.

As the shortage of new monetary gold and the over-abundance of dollars have been evident for some years now, one may analyse how global reserves have developed under these conditions. First, the scope of global reserves must be indicated.

Reserves consist of international assets held by the monetary authorities which are readily available to support the par value of the currency in the exchange market. Traditionally, reserves have been held in gold and in foreign currency assets, primarily dollars and sterling. As countries have placed large resources with the IMF, however, and as the corresponding unconditional claims on the Fund serve the function of reserves, "IMF reserve positions" (as they are increasingly referred to) must also be counted in global reserves. Thus, global reserves are taken as the sum of gold, foreign exchange and IMF reserve positions held officially by all countries. Reserves are here taken on a gross basis, i.e. without netting out liabilities; this is essential for US and UK reserves, in view of their position as reserve currencies, while for other countries liabilities are too small to matter.

The table on the next page shows the cumulative changes in reserves for the years 1955–60 and 1961–66.

The two periods are divided between 1960 and 1961 because the problem of new monetary gold and the over-abundance of dollars became evident at about that time. The eruption of the gold price on the London market in October 1960 was a signal of the changed situation. Since then the system has operated quite differently from the way it did before; through co-operation among the principal countries, management of official financing has played a large rôle and new instruments have been used on an ad hoc basis to meet the greater pressures that have often been present. This contrast between the two periods is profoundly reflected in the development of global reserves.

It may be seen first that the increment to global reserves since 1961 was more than 50 per cent. larger than in the previous period and that the annual rate of increase averaged 2.8 per cent., as against 2.1 per cent. This larger gain was accounted for wholly by countries outside the Group of Ten.

Changes in global reserves, 1955–66
(in milliards of US dollars and average annual percentage increases).

Areas and years	Gold		IMF reserve position	Foreign exchange		Total	
	Amount	%	Amount	Amount	%	Amount	%
All countries							
1955–60	+ 3.1	1.4	+ 1.7	+ 2.1	2.0	+ 6.9	2.1
1961–66	+ 2.9	1.2	+ 2.8	+ 5.2	4.2	+10.8	2.8
Group of Ten							
1955–60	+ 3.1	1.7	+ 1.4	+ 2.8	6.3	+ 7.3	2.9
1961–66	+ 1.3	0.6	+ 2.0	+ 2.2	3.6	+ 5.5	1.9
Other developed countries							
1955–60	+ 0.4	4.6	+ 0.2	+ 0.0	—	+ 0.6	2.1
1961–66	+ 1.6	11.2	+ 0.5	+ 1.3	6.2	+ 3.4	8.9
Less-developed countries							
1955–60	— 0.4	—	+ 0.2	— 0.7	—	— 1.0	—
1961–66	— 0.1	—	+ 0.3	+ 1.7	4.0	+ 1.9	3.2
Group of Ten excluding US and UK							
1955–60	+ 6.8	13.2	+ 0.8	+ 2.6	6.3	+10.2	10.5
1961–66	+ 6.7	7.2	+ 3.7	+ 0.1	0.2	+10.5	6.6
United States							
1955–60	— 4.0	—	+ 0.4	—	—	— 3.6	—
1961–66	— 4.6	—	— 1.2	+ 1.3	—	— 4.5	—
United Kingdom							
1955–60	+ 0.3	1.7	+ 0.3	+ 0.2	8.2	+ 0.7	3.5
1961–66	— 0.9	—	— 0.5	+ 0.7	18.0	— 0.6	—

Source: *International Financial Statistics*. The "less-developed countries" group is the same as in the IMF reserve statistics. "Other developed countries" is the same, with the addition of Austria, Denmark and Norway. Figures may not add up to totals because of rounding.

The record of the less-developed countries was particularly improved, as their reserves increased by $1.9 milliard, in contrast to a loss of $1 milliard in the earlier period — a turn-round of almost $3 milliard. In the 1950s these countries were adversely affected by the aftermath of the Korean war; they have evidently benefited also from the strong expansion of the US economy since 1961. However, the increase in their reserves over the last six years can hardly be considered excessive.

The developed countries outside the Group of Ten also had a much improved position, with a gain of almost $3 milliard more in the second period than in the first. The rate of increase, at almost 9 per cent., was very high, and even over the whole twelve years the average rate was 5.4 per cent.

The Group of Ten countries gained $1.8 milliard less reserves in the second period and their rate of increase was sharply lower. More important, however, was the contrast between the two reserve centres and the other countries of the Group. The non-reserve countries gained more than $10 milliard in both periods, and their rate of increase averaged 8.5 per cent. over the whole twelve years. The United States and the United Kingdom together lost reserves in both periods; the loss of $3 milliard in the first was more than accounted for by the United States, while the United Kingdom accounted for $600 million of the $5 milliard combined loss in the second period.

So far as participation in global reserve growth is concerned, therefore, the countries outside the Group of Ten have fared much better since 1961, while the non-reserve countries of the Group had more than adequate increases in both periods. The reserve centres did not share in the rise in global reserves; in fact, UK reserves at the end of the twelve years were about the same as at the beginning, while the US reserves were lower by $8.1 milliard.

This picture reflects, of course, the greater disequilibrium in international payments in the period since 1961. But it is the asset composition of the increase in reserves which shows the change in the operation of the system. Broadly speaking, new gold contributed less to reserve creation, while IMF reserve positions and foreign exchange assets became much more important sources.

The decrease in additions to countries' gold reserves occurred in spite of substantially larger new supplies. Gold production and Russian sales increased from $7.5 milliard in 1955–60 to $10.2 milliard in 1961–66, but the sharper rise in private demand left less gold for monetary purposes. In the recent period, in fact, there were net transfers of $195 million of gold from international institutions (IMF and BIS) to countries' reserves, whereas in the earlier years these institutions had added $505 million to their gold holdings. Thus, the gold stocks of countries plus the international institutions rose by $2.7 milliard during 1961–66, as against $3.6 milliard in the earlier period.

For the Group of Ten, excluding the United States and the United Kingdom, the proportion of gold in their total reserve increase was much the same in the two periods, at about two-thirds; as there was less new monetary gold in the second period, however, and as the additions to gold stocks of non-Group of Ten countries went up from roughly zero to $1.5 milliard, this meant drawing a larger volume of gold from the two reserve centres.

With regard to the larger increase in IMF reserve positions since 1961, the difference being $1.1 milliard, this reflects credit-tranche drawings on the Fund — in particular the drawing by the United Kingdom. Global reserves are not changed in their total by countries' payments of gold subscriptions to the Fund, as these only shift the form of assets. Similarly, drawings on Fund reserve positions merely shift these assets from one country to another. However, credit-tranche drawings do add to global reserves, since they set up Fund reserve positions to the account of the countries whose currencies are drawn. It will be seen that it was the non-reserve members of the Group of Ten that financed the bulk of the Fund's requirements in the years 1961–66.

To turn now to foreign exchange assets, the increase in the growth of these holdings in the second period was accounted for entirely by countries outside the Group of Ten; the Group of Ten countries actually accumulated a somewhat smaller volume than previously. Again, however, there was a significant change within the Group of Ten. The two reserve centres, which traditionally held only gold in their reserves, acquired \$2 milliard of foreign exchange assets in the second period; the other countries of the Group, which increased their exchange holdings by \$2.6 milliard in the first period, showed virtually no increase after 1961. While this outcome reflects a reluctance to accumulate dollars, it occurred also because, in addition to maintaining a high level of gold acquisition, the non-reserve countries of the Group put \$3 milliard more of resources into the IMF. The increased foreign exchange holdings of the two reserve centres, on the other hand, are explained largely by special transactions which have become important in the operation of the system in the last six years.

During the years 1955–60 the growth of reserves took place through the accumulation of new gold stocks and the acquisition of ordinary foreign exchange assets, mostly in dollars, such as Treasury bills, deposits with banks, etc. The amount stemming from credit operations of the IMF was small and there were very few special operations which affected reserves. One such was the liquidation of the European Payments Union, which, because current positions were consolidated into longer-term debt, reduced the foreign exchange reserves of the countries concerned by some \$550 million. Another was the purchase by the United States of \$800 million's worth of gold from the IMF against special Treasury securities, which increased its reserves by that amount. As these operations were largely offsetting in their effect on global reserves, it may be said that the growth of reserves came about quasi-automatically in this earlier period.

In the years 1961–66, however, there were special transactions involving ad hoc liquidity creation which played a major rôle in the growth of global reserves. These transactions were confined almost entirely to the Group of Ten countries. They may be explained partly by: (1) the efforts of the United States to limit the drain of gold reserves arising mainly from its own deficit but at times also from the shifts of dollar reserves among other countries; and (2) the United Kingdom's need for resources to protect the exchange rate in the face of an external deficit and confidence movements against sterling. Partly also, they may be seen as providing acceptable assets to European countries in surplus that did not want to add unduly to their ordinary dollar exchange holdings or to exert greater pressure on the US gold stock.

Special transactions that accounted for increased reserves include the issue of US Treasury foreign currency securities (Roosa bonds), the use of central-bank facilities, primarily swaps, and the transfer to the UK reserves of assets out of its Treasury dollar portfolio. In general, the statistical effect of these transactions on reserves is equal to the amount of the assets that are put into reserves. With regard to central-bank swaps, this is the case also when the creditor country advances resources out of its reserves. A swap of dollars against sterling drawn by the Bank of England on the Bundesbank, for example, adds to the reserves of the United Kingdom and leaves the

German reserves unchanged — sterling having replaced the dollars put up. But, when neither party puts up resources from its reserves, as is the case, for example, in a swap of dollars against sterling drawn by the Bank of England on the Federal Reserve, the reserves of both countries increase, so that double the amount of the swap is added to global reserves.

Figures for the reserves accounted for by special transactions as at the end of 1966 are shown in the following table. Together, these special transactions account for more than a third of the increase in global reserves from 1961 to 1966 and three-quarters of the increase in foreign exchange reserves. Inside the Group of Ten they account for 69 per cent. of the increase in total reserves and for more than the whole of the increase in foreign exchange reserves, \$3.8 milliard as against \$2.2 milliard. Excluding special transactions, non-reserve members of the Group of Ten had a decline of \$0.7 milliard in their foreign exchange reserves during this period.

Sources of increases in global reserves.

	1955–60	1961–66
	in millions of US dollars	
Gold	3,115	2,860
Ordinary foreign exchange assets	2,075	1,385
IMF reserve positions arising out of		
Gold subscriptions	1,515	1,410
Members' credit-tranche drawings	210	1,350
US Government non-marketable bonds	—	430
Central-bank facilities	—	2,470
UK dollar security portfolio	—	885
Total	6,915	10,790

While the special transactions just described had the effect of increasing reserves, the Group of Ten countries also used special transactions in ways that had a reverse effect; that is, they limited the rise in reserves. Firstly, there was the prepayment of official debt, largely to the United States. Over the 1961–66 period this amounted to some \$2.1 milliard, excluding payments which would have fallen due during this period anyway. Secondly, monetary authorities acquired foreign assets which have not been counted as reserves. While this partly depended on the particular country's definition of reserves, most of these assets, which in all amounted to some \$1.3 milliard at the end of 1966, are less liquid than those included in reserves; they often represent longer-term investment of balances not needed as reserves.

Without these special transactions, taken together, the statistical rise of global reserves would be \$3.4 milliard larger during 1961–66 than it was in fact.

The calculated effects of special transactions on reserves are, of course, statistical; had they not been undertaken, both the international payments situation and the movement of global reserves would have been very different.

* * *

The growth of global reserves has been reviewed here in some detail because its significance lies to a large degree in the kinds of assets accumulated and their distribution among countries. Even so, the conclusions that can be drawn from the record and their implications for the future are subject to considerable latitude.

With the importance of special transactions, global reserves are a less homogeneous and meaningful aggregate than they used to be; as the assets that arise from official credit arrangements are to some extent not readily marketable, they do not provide the same degree of "liquidity" as traditional reserves. This may not be important so long as the volume of such assets is relatively small, but a problem could arise if they were relied upon for the continuous growth of global reserves.

It will be evident, also, that the record of the past six years cannot be taken as evidence of the "need" for global reserves, particularly in view of the volume of special transactions undertaken to limit reserve accumulation. The actual growth of reserves was much influenced by the balance-of-payments deficits of the two reserve-currency countries and, as these deficits could have been considerably smaller, the growth of global reserves could have been smaller also and still been in conformity with the "need".

None the less, gold supplies and ordinary foreign exchange assets provided only a quite small increment to global reserves in this period; the growth rate from these two sources alone was 1.1 per cent., so that the actual growth of 2.8 per cent. depended on IMF facilities and special reserve-creating transactions. It is difficult to envisage the system operating smoothly for any length of time with reserves growing only at the smaller figure, and it therefore seems not unreasonable to say that official credit transactions to some extent reflected global reserve needs.

While the existence of a sufficient global stock of reserves is obviously one aspect of reserve "needs", history indicates that the system has a need also of a fairly continuous increase in that aggregate. This may happen not so much because countries direct their policies to increasing their reserves, but simply to avoiding deficits and losing reserves. On balance, therefore, total reserves tend to go up. The dilemma of the system is that, with new monetary gold so limited, this supply of reserves has depended on a persistent deficit in the external accounts of the United States. Although the redistribution of reserves that occurred in the 1950s had its favourable side in strengthening the world payments system, no way has been found to correct the disequilibrium in the 1960s when further redistribution has been undesirable.

It is significant also that the problems of the system, and the measures they have called forth, have centred on the Group of Ten. Other countries, taken together, have obtained a satisfactory increase in reserves without engaging in special transactions. If global reserves stopped rising, however, it is likely that many of these countries would be adversely affected.

In assessing the future, it seems clear that, as the supply of new gold for monetary purposes is declining and as the willingness to hold ordinary foreign exchange is linked to the availability of gold, the growth of global reserves from these sources is likely to be less than in the past. It is apparent too that the drain of gold from the United States cannot for long continue on its former scale. To what extent it will be reduced by a smaller imbalance in payments, however, and to what extent by use of special transactions remains to be seen.

As regards the effect on reserves of official credit operations, the future is also not so clear. Official credits all have repayment obligations and when there is net liquidation global reserves are reduced. This has happened on a large scale in the first quarter of 1967 with the repayment of central-bank assistance by the United Kingdom. The associated decline in global reserves is obviously of little importance as such and the situation has certainly been strengthened by these debts being paid off. The ups and downs of official credits are illustrated by the operation of the Federal Reserve swap network; total drawings on the network by various countries have been $7.7 milliard, but none were outstanding at the end of March 1967. Yet, over time, the system has operated to make the growth of reserves a persistent force and, despite the ups and downs and shifts among countries from one type of credit to another, total borrowed reserves outstanding have tended to rise. There is some prospect of this in the rest of 1967.

Finally, it seems rather misleading to contrast the present state of affairs with a possible future one in which additions to reserves from traditional sources might not be enough. Supplementing these sources has been going on for six years already and the outlook is that this process will continue.

PART II

MONETARY AND ECONOMIC SURVEY.

I. CREDIT DEVELOPMENTS AND POLICIES.

The dramatic tightening of monetary conditions, on both international and key domestic markets, carried interest rates to historically high levels by the late summer of 1966. Although in some ways interrelated, these movements derived primarily from a coincidence of largely autonomous developments in the United States, the United Kingdom and Germany. Each of these countries had experienced domestic inflationary strains side by side with external deficits, and each of them placed heavy reliance on monetary policy to bring the situation under control. In various neighbouring countries, including Canada, the Netherlands, Sweden and Switzerland, developments moved along fairly similar lines.

Domestic money-market rates, and with them Euro-currency rates, moved upwards in close parallel from late 1965 up to the summer of 1966. Discount rate adjustments in the United States and Canada at the turn of the year were followed by a round of increases on the Continent in the spring and by a rise to 7 per cent. in the United Kingdom in July. Moreover, long-term yields in the United States, which had begun to rise sharply after the middle of 1965, reached by August 1966 their highest levels for decades. In many western European countries, however, the increase in long-term rates had started earlier and went even further.

The easing of credit markets since last autumn has been almost as striking as their previous tightening. Short and long-term interest levels have come down substantially in the countries where they had previously recorded the largest increases. In the Euro-currency market the tone has been set by the large reflux of funds borrowed last year by the United States. Long-term interest levels within western Europe have generally moved closer together, but the differentials vis-à-vis the United States remain wide.

* * *

Bank credit and liquid-asset formation.

In 1965 and a large part of 1966 the rate of credit expansion, relative to the growth of the gross national product, was clearly running to excess in North America and much of western Europe. The following table gives

The banking system: Monetary survey.

Countries	Years	Annual changes in main assets: Net foreign assets	Annual changes in main assets: Credit to public sector	Annual changes in main assets: Credit to private sector	Annual changes in main liabilities: Money	Annual changes in main liabilities: Quasi-money	Gross national product, at market prices	Money and quasi-money,[1] as percentages of GNP
		in milliards of national currency units						
Austria	1964	2.51	2.38	11.38	3.08	10.42	222.77	*50.6*
	1965	− 1.66	2.15	15.03	4.19	10.72	241.70	*52.8*
	1966	− 2.30[2]	2.46[2]	15.41[2]	2.42	11.20	260.50	*54.4*
Belgium	1964	8.80	8.00	10.70	19.70	6.10	773.82	*45.7*
	1965	6.80	16.10	13.90	21.10	11.60	836.96	*46.0*
	1966	− 5.60	18.30	22.50	21.00	12.90	902.00	*46.1*
Denmark	1964	0.82	− 0.98	3.42	1.40	1.53	61.91	*48.2*
	1965	0.12	0.88	2.36	1.70	1.19	69.47	*47.4*
	1966	0.22	0.14	4.47	2.23	2.04	76.67	*48.2*
Finland[3]	1964	126	− 48	1,130	56	949	23,433	39.7
	1965	− 282	69	1,167	45	1,022	25,819	40.5
	1966	− 457	215	1,378	126	1,218	27,591	*42.0*
France	1964	3.60	− 0.32	10.66	12.21	2.61	431.90	*39.5*
	1965	3.33	1.28	12.04	15.27	2.77	461.40	*40.6*
	1966	1.83	1.03	14.40	13.64	5.05	497.50	*41.6*
Germany	1964	2.00	8.40	21.70	5.40	13.90	413.80	*38.6*
	1965	− 0.20	8.80	25.30	5.10	17.30	449.60	*40.3*
	1966	3.10	6.00	19.40	1.30	19.90	477.90	42.3
Italy	1964	483	548	1,104	908	870	33,077	*61.9*
	1965	992	922	1,470	1,871	1,490	35,575	*65.3*
	1966	418	821	2,646	2,080	1,690	38,397	*69.9*
Netherlands	1964	0.11	0.17	1.08	1.15	2.42	61.83	*58.8*
	1965	0.06	0.89	1.47	1.70	2.50	68.65	*59.4*
	1966	− 0.27	1.17	1.09	1.18	2.43	75.88	*58.4*
Norway	1964	0.27	0.20	1.39	0.57	1.23	45.18	*53.2*
	1965	1.13	0.34	1.23	0.77	1.76	50.10	*52.0*
	1966	0.07	0.48	1.98	0.84	1.45	54.17	52.3
Spain	1964	21.00	28.10	90.00	60.30	78.00	1,062.90	*67.4*
	1965	− 3.60	32.80	125.50	62.30	82.40	1,287.40	*66.4*
	1966	− 14.60	49.00	112.50	50.90	79.90	1,474.20	*66.9*
Sweden	1964	1.06	− 0.36	4.82	1.27	3.83	92.97	*67.3*
	1965	0.12	− 0.67	3.92	1.08	1.64	102.15	*65.4*
	1966	0.56	1.57	5.19	1.44	4.81	110.80	*64.7*
Switzerland	1964	0.85[4]	0.61	3.92	1.72	4.30	55.54	*124.8*
	1965	0.56[4]	0.86	4.46	1.09	4.73	59.88	*125.8*
	1966	0.41[4]	0.79	4.50	1.12	4.16	64.17	*125.8*
United Kingdom[3]	1964	− 578[5]	− 200	967	585	—	33,066	*34.3*
	1965	− 304[5]	550	570	909	—	35,426	34.3
	1966	− 10[5]	99	308	554	—	37,424	*34.5*
United States	1964	− 0.10[6]	6.40	17.80	6.80	13.20	631.70	*42.8*
	1965	− 1.20[6]	8.90	26.40	7.30	19.40	681.20	*43.1*
	1966	− 0.60[6]	4.10	16.80	− 1.30	11.10	739.60	42.5
Canada	1964	0.35	− 0.26	1.02	0.71	0.50	47.40	*35.4*
	1965	0.16	0.04	1.67	1.20	0.78	52.11	*35.9*
	1966	0.34	0.65	0.75	0.80	0.53	57.78	*34.8*
Japan	1964	− 274	727	3,791	1,012	2,503	27,645	*90.4*
	1965	154	745	2,774	1,611	2,908	30,441	*95.1*
	1966	133	912	4,656	1,459	3,697	35,190	*96.3*

[1] Annual averages (based on quarterly data). [2] Twelve months to October. [3] In millions of national currency units. [4] National Bank only. [5] Includes the Exchange Equalisation Account's assets (other than transfer from US dollar portfolio), net IMF position and deposit banks' net assets. [6] *Official assets plus net IMF position.*

Source: IMF, *International Financial Statistics.*

a comparative survey of liquid-asset formation via the banking system and the corresponding changes in claims on the public, private and foreign sectors. It thus reflects in part the composition of domestic credit demand and the extent to which economic policy — not only monetary policy but also budgetary and incomes policy — was successful in influencing bank credit and liquidity formation. As in many countries credit demand eased late in the year, the annual data shown in the table present a somewhat mixed picture.

In a number of countries the granting of bank credit to the public sector, which had become an increasingly important source of monetary expansion in 1965, fell away somewhat in 1966. In certain of them, including Denmark, Germany and Italy, the public sector's reduced recourse to bank credit in 1966 was attributable partly to the achievement of better budgetary results. On the other hand, in Belgium the budget also improved but, in order to ease capital-market strains, the government borrowed more from the banking system than in 1965 and began again to take up funds from abroad.

In some countries the slower growth in bank credit to the government was due partly to a shift in the pattern of borrowing. In Switzerland and Italy the public authorities raised a larger proportion of funds through net capital issues and in Germany at short term outside the banking system. In France the central government's budget shifted from overall balance to a small deficit last year. However, Treasury borrowing, mainly for purposes of re-lending to the economy, was more than covered outside the banking system, thus permitting some repayment to the banks. But in the Netherlands not only did the central government's budget position deteriorate further but its financing via the banking system, including the central bank, also increased.

In the United States and the United Kingdom the expansion in bank credit to the public sector was smaller last year, although the US budget deficit increased and that in the United Kingdom remained large. In the United States the banks curtailed their acquisition of public-sector securities, while the amount held by the non-bank public increased. In the United Kingdom the Treasury's financing needs were met mostly by an increase in overseas purchases of Treasury bills and by the sterling that became available through the Exchange Equalisation Account.

In Canada, on the other hand, the central government's budget position, excluding the operations of the new national pension fund, deteriorated in 1966, as also did that of the provinces and municipalities. Part of the public sector's larger cash requirements were met via the banks and the central bank. In Sweden developments followed similar lines. In Japan, as part of a deliberate effort to stimulate activity, the budget deficit was increased and financed mainly via the sale of bonds to the banking system.

Bank credit to the private sector rose more slowly in a number of countries last year, at first because of tighter money, later because of an easing of demand. The deceleration was quite marked in the United States, Canada, the United Kingdom, Germany and the Netherlands, while in Switzerland and Austria the increase in absolute terms was not much more than in 1965. In some of these countries — the United Kingdom, the Netherlands and Switzerland — credit to the private sector was restricted by a quantitative ceiling.

In contrast, lending to the private sector accelerated in countries where activity had been cyclically depressed — Belgium, France, Italy and Japan — as well as in the Scandinavian countries and Finland.

Bank credit expansion and liquid-asset formation constitute an interrelated process. At the margin it is limited by central-bank policy to influence bank liquidity, taking account of the effects of the balance of payments, Treasury operations and other factors. Normally, monetary restraint expresses itself in a slowing-down in the growth of liquid assets relative to the gross national product and in a rise in long-term interest rates, and for monetary ease the reverse is true. The inverse relationship between liquidity trends and long-term interest rates is generally borne out in the results for most of the countries last year. But in Germany, for example, liquidity preference in 1966 was such that a sharp rise in long-term interest yields went hand in hand with an increase in money and quasi-money relative to the gross national product. In Denmark, too, a larger proportion of funds was placed with the banks despite the high level of interest rates.

Comparative interest rate movements.

In the United States the rise in short-term interest rates in 1966 marked the continuation, under changed circumstances, of an upward adjustment in progress since 1962. Over this period the official discount rate was raised in three steps, the last in December 1965, from 3 to 4½ per cent. The maximum rates payable on time deposits under Regulation Q were increased much more, those on 3–6 month deposits being brought up from 2½ to 5½ per cent. The need favourably to influence short-term capital movements played a prominent rôle in these adjustments, although by December 1965 domestic considerations had become of decisive importance.

The movement of US long-term interest rates, on the other hand, followed a somewhat different course. The yields on long-term government bonds, after rising moderately between the end of 1962 and the spring of 1964, then remained very stable. However, from the summer of 1965 onwards, as demand pressures became excessive, they began to rise steeply and continued to move upwards until August 1966.

The gap between short and long-term interest rates in the United States gradually closed between 1962 and 1966. In the latter part of the period, in fact, short-term yields went appreciably above those at long term.

In the United Kingdom the rise in interest rates, both short and long-term, began in late 1963 as a domestic upswing got under way. Thereafter, until the late summer of 1966, the trend remained upward, though it was marked by a particularly steep rise during the crisis of late 1964 and early 1965 and a subsequent easing of rates later in 1965.

Comparative interest rate movements, 1962–67.[1]

Country	Money-market rates[2]					Yields on long-term government bonds				
	End-1962	Mid-1965	August 1966	March 1967	Change from 1962 to March 1967	End-1962	Mid-1965	August 1966	March 1967	Change from 1962 to March 1967
	in percentages				in percentage points	in percentages				in percentage points
Netherlands	2.02	4.18	5.03	4.76	+ 2.74	4.19	5.24	6.53	5.83	+ 1.64
Denmark	.	.	.	.	.	6.45	7.61	8.05	8.05	+ 1.60
Switzerland	2.88	3.73	4.21	4.50	+ 1.62	3.12	3.92	4.24	4.72	+ 1.60
Germany	4.37	4.87	7.00	5.12	+ 0.75	6.10	7.10	8.60	7.20	+ 1.10
Belgium	2.73	3.57	3.95	3.45	+ 0.72	4.96	5.59	5.81	5.88	+ 0.92
Sweden	.	.	.	.	.	4.35	5.00	6.10	5.23	+ 0.88
United Kingdom	3.64	5.59	6.70	5.69	+ 2.05	5.61	6.65	7.17	6.39	+ 0.78
France	3.51	4.41	4.77	5.00	+ 1.49	5.31	5.47	5.98	6.08	+ 0.77
Italy	.	.	.	.	.	4.88	5.46	5.55	5.56	+ 0.68
United States	2.86	3.81	4.93	4.29	+ 1.43	3.87	4.14	4.80	4.45	+ 0.58
Canada	3.87	3.95	5.07	4.26	+ 0.39	5.07	5.16	5.91	5.45	+ 0.38

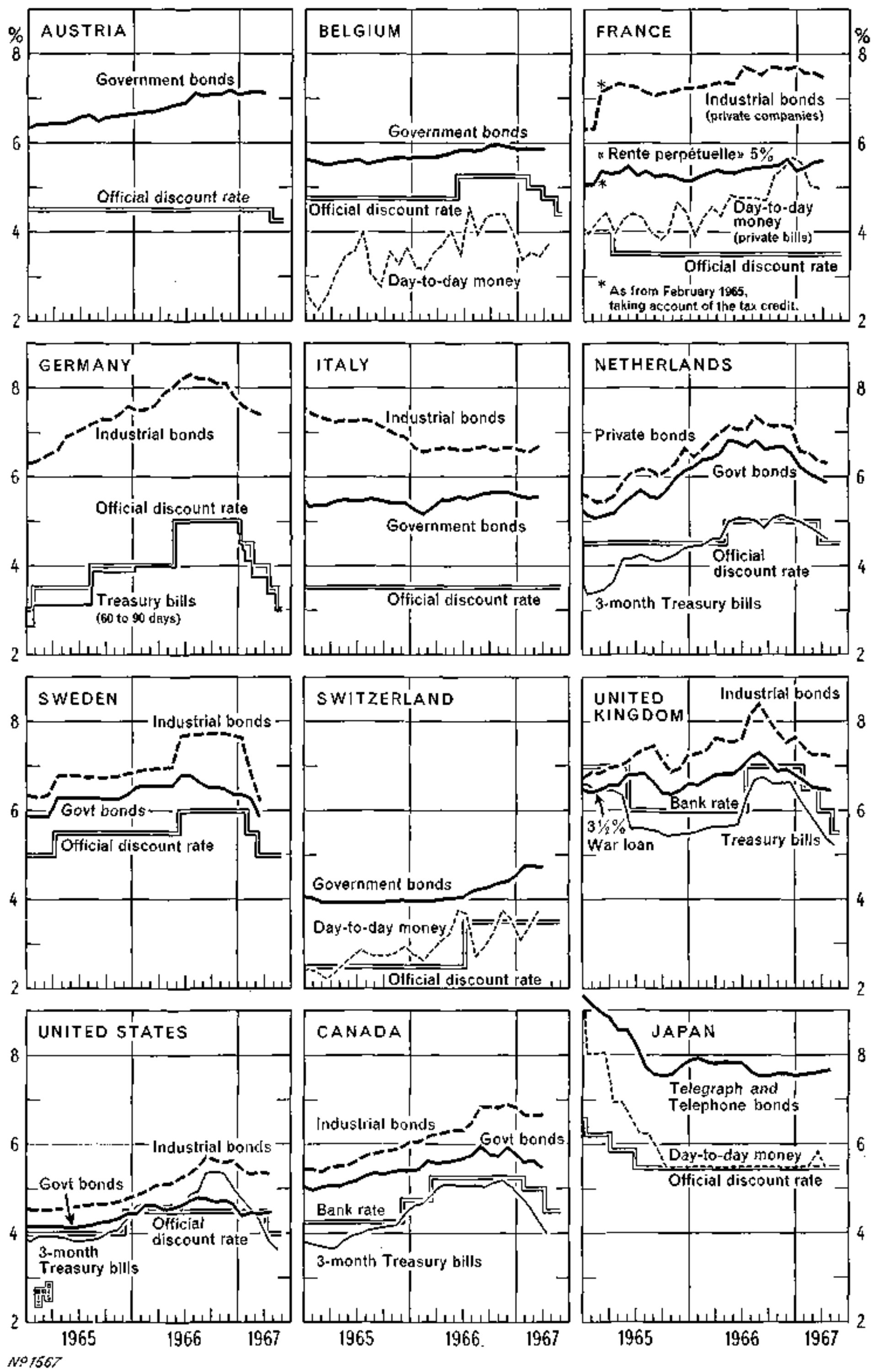
[1] The international comparability of interest rates is very limited, lying more in relative movements over time than in absolute differences. [2] Belgium, France: call-money rates; Netherlands, United Kingdom, United States, Canada: three-month Treasury bills; Germany, Switzerland: three-month deposit rates.

On the Continent short-term market rates generally moved upwards from 1962 to 1966 and kept more or less in line with those in the United States and in the Euro-currency market. One reason for the fairly close correspondence between short-term interest rate movements lies in the linkages, both direct and through the Euro-currency market, that have come to exist among the national money markets. Another is that, as reserve-currency countries, the United States and the United Kingdom have on balance-of-payments grounds had to keep their short-term rates closely attuned to economic conditions elsewhere.

On the other hand, long-term interest differentials between the United States and virtually all western European countries have widened over recent years. In the period from 1962 up to the middle of 1965, in which yields on long-term government bonds in the United States showed little rise, large increases occurred in Denmark, Germany, the Netherlands and the United Kingdom. Smaller rises, but still greater than in the United States, took place in Belgium, Italy and Sweden. The long-term yield in Switzerland, though starting at a much lower level than in the United States, rose by nearly the same amount as in Germany and the Netherlands. Only in France was the increase no greater than in the United States.

Between the middle of 1965 and August 1966 the yield in the United States on long-term government bonds moved up sharply from 4.14 to 4.80 per cent. Yet, even during this period, the yields in some of the continental countries — Germany, the Netherlands and Sweden — showed an even greater increase, while in France, the United Kingdom and Denmark the rise was more or less comparable. But in other countries — Belgium, Italy and Switzerland — the yields advanced appreciably less than in the United

Interest rates.



Changes in official discount rates since 1964.

Country and date of change	Official discount rate in %
Austria	
27th June 1963	4½
18th April 1967	*4¼*
Belgium	
31st October 1963	4¼
3rd July 1964	4¾
2nd June 1966	*5¼*
2nd February 1967	*5*
23rd March 1967	*4¾*
11th May 1967	*4½*
Canada	
12th August 1963	4
24th November 1964	4¼
6th December 1965	4¾
14th March 1966	*5¼*
30th January 1967	*5*
7th April 1967	*4½*
Denmark	
13th November 1963	5½
11th June 1964	6½
France	
14th November 1963	4
8th April 1965	3½
Germany	
5th May 1961	3
22nd January 1965	3½
Germany (contd.)	
13th August 1965	4
27th May 1966	*5*
6th January 1967	*4½*
17th February 1967	*4*
14th April 1967	*3½*
12th May 1967	*3*
Iceland	
29th December 1960	9
1st January 1965	8
1st January 1966	*9*
Japan	
20th April 1963	5.84
18th March 1964	6.57
9th January 1965	6.205
3rd April 1965	5.84
26th June 1965	5.475
Netherlands	
8th January 1963	3½
6th January 1964	4
4th June 1964	4½
2nd May 1966	*5*
15th March 1967	*4½*
Portugal	
12th January 1944	2½
1st September 1965	3
Sweden	
14th June 1963	4
31st January 1964	4½
6th November 1964	5
9th April 1965	5½
10th June 1966	*6*
3rd February 1967	*5½*
10th March 1967	*5*
Switzerland	
26th February 1959	2
3rd July 1964	2½
6th July 1966	*3½*
United Kingdom	
3rd January 1963	4
27th February 1964	5
23rd November 1964	7
3rd June 1965	6
14th July 1966	*7*
26th January 1967	*6½*
16th March 1967	*6*
4th May 1967	*5½*
United States	
17th July 1963	3½
24th November 1964	4
6th December 1965	4½
7th April 1967	*4*

States. Thus, impressive though it was, the rise in long-term yields in the United States fell into about the middle of the spectrum of international movements generally.

In the most recent phase, from about August 1966 up to the spring of 1967, long-term yields have fallen in the United States and a number of western European countries. In Germany, Sweden, the Netherlands and the United Kingdom the decline was quite steep, much more so than that in the United States. However, in Switzerland, where yields had remained low by European standards, they continued to rise over this period. At the same time, in Belgium, France and Italy, where long-term interest levels were already high relative to those in the United States, yields were maintained or went up somewhat further.

One reason for the relatively large increases in long-term interest rates in western Europe since 1962 is that rapid increases in public expenditure, together with wage adjustments in excess of productivity gains, have made inroads on national saving ratios. Related to this, long-persisting inflation has strengthened liquidity preference. Another reason lies in the direct measures taken by the United States to improve its balance of payments. Under the voluntary programme US business firms, by borrowing in Europe, may exceed the prescribed direct investment ceilings and also improve their individual payments positions as requested. Moreover, the interest equalisation tax, which with effect from January 1967 was raised in terms of its interest equivalent from 1 to 1½ per cent., encourages US residents to invest at home and potential foreign borrowers to turn to European international and domestic markets.

It is noteworthy, on the other hand, that long-term interest differentials within western Europe are now narrower than at any time in recent years. This reflects, on the one hand, the substantial upward adjustments in the Netherlands, Sweden and Switzerland, where by international standards yields had been low, and, on the other hand, the relatively easy cyclical situation in Belgium, France, Germany and Italy. In France budget restraint has also helped to limit the rise in yields, and since last summer there has also been an improvement in the underlying budget position in Belgium, Germany and Italy.

Capital markets: domestic and international.

Under conditions of monetary restraint, the proportion of total credit that is channelled via the banking system normally tends to decline. Potential borrowers find it necessary to turn more to the capital market, and the banks themselves, in trying to sustain their ordinary lending, tend to cut back their net security acquisitions. At the same time, as security prices fall and yields rise, non-bank investors, particularly institutional investors, move in increasingly to take advantage of buying opportunities in the long-term market. The slower rate of deposit formation limits the banks' scope for multiple credit creation and thus helps to curb credit expansion by the financial system as a whole.

Developments along these lines were clearly reflected last year in the rise of new issues in countries such as the United States, the United Kingdom and Canada. In the first two countries the increase was ascribable largely to private borrowing, while in Canada the public sector, particularly the provinces and municipalities, became more prominent.

Where monetary restraint was applied on the Continent, shifts in the flow of funds often tended to be more towards time and savings deposits than towards new capital issues. This was particularly true in Germany, owing to strong liquidity preference and limited institutional support for the market. In Switzerland capital issues were kept down by a system of quotas and in Denmark by agreement among the mortgage institutions. In the Netherlands, on the other hand, relatively more funds passed through the capital market last year, but the bulk of these were in the form of private loans rather than new issues. In Sweden the larger volume of issues was facilitated by institutional buying, particularly by the public insurance institutions.

In Italy and Japan, where monetary ease prevailed, a marked increase in public issues was facilitated by further large bank purchases of securities. In France new-issue activity was about the same as in 1965, but a relatively

Domestic capital markets: Net Issues.

Countries	Years	Public: State	Public: Local authorities and public bodies	Private[1]: Shares	Private[1]: Bonds	Foreign issues	Total	Private and foreign issues	Total new issues
		in milliards of national currency units						as percentages of GNP	
Belgium	1964	7.89	12.82	11.98	5.66	0.17	38.52	*2.3*	*5.0*
	1965	17.21	12.27	11.41	15.25	0.26	56.40	*3.2*	*6.7*
	1966	12.96	13.94	11.96	15.47	.	54.33	*3.0*	*6.0*
Denmark	1964	−0.18	—	0.24	3.49	—	3.55	*6.0*	*5.7*
	1965	−0.14	—	0.30	4.82	—	4.99	*7.4*	*7.2*
	1966	−0.16	—	0.23	4.20	—	4.27	*5.8*	*5.6*
France	1964	0.55	0.47	5.01	5.14	0.15	11.32	*2.5*	*2.6*
	1965	0.00	0.68	5.02	6.34	0.12	12.16	*2.5*	*2.6*
	1966	0.00	0.84	3.66	7.66	0.20	12.36	*2.3*	*2.5*
Germany	1964	1.51[2]	1.76	2.24	10.24	0.89[3]	16.64	*3.2*	*4.0*
	1965	1.15[2]	1.96	3.96	9.36	1.36[3]	17.79	*3.3*	*4.0*
	1966	0.36[2]	0.06	2.69	5.10	0.62[3]	8.83	*1.8*	*1.9*
Italy	1964	70	159[4]	555	1,221	—	2,005	*5.4*	*6.1*
	1965	161	501[4]	406	1,295	14	2,377	*4.8*	*6.7*
	1966	1,551[4]		470	1,197	72	3,290	*4.5*	*8.6*
Netherlands	1964	0.20	0.29	0.21	0.14	−0.05	0.78	*0.5*	*1.3*
	1965	−0.03	0.59	0.11	0.71	0.04	1.41	*1.2*	*2.1*
	1966	−0.02	0.66	0.06	0.80	−0.07	1.43	*1.0*	*1.9*
Spain	1964	15.00	8.33	20.12	19.93	—	63.38	*3.8*	*6.0*
	1965	27.51	9.10	34.76	25.93	—	97.30	*5.4*	*8.7*
	1966	24.44	9.00	40.08	26.19	—	99.71	*5.2*	*7.8*
Sweden	1964	0.11	0.37	0.49	3.15	—	4.11	*3.9*	*4.4*
	1965	−0.29	0.20	0.93	2.81	—	3.66	*3.7*	*3.6*
	1966	−0.14	0.16	0.72	4.83	—	5.55	*5.0*	*5.0*
Switzerland[5]	1964	−0.16	0.66	1.54	2.12	0.28	4.44	*7.1*	*8.0*
	1965	−0.22	0.75	1.54	1.81	0.26	4.14	*6.0*	*6.9*
	1966	0.00	0.90	1.21	1.59	0.42	4.12	*5.0*	*6.4*
United Kingdom	1964	−0.11[6]	0.09	0.23	0.29	0.06	0.56	*1.8*	*1.7*
	1965	0.22[6]	0.21	0.07	0.37	0.02	0.89	*1.3*	*2.5*
	1966	0.23[6]	0.19	0.19	0.50	−0.02	1.09	*1.8*	*2.9*
United States[7]	1964	0.80[8]	5.10	3.30	6.60	1.20[9]	17.00	*1.8*	*2.7*
	1965	−4.70[8]	6.10	3.10	8.10	1.50[9]	14.10	*1.9*	*2.1*
	1966	−1.20[8]	5.50	4.40	11.30	1.30[9]	21.30	*2.3*	*2.9*
Canada	1964	0.56	0.88	0.33	0.56	—	2.32	*1.9*	*4.9*
	1965	−0.06	0.67	0.45	0.92	—	1.99	*2.6*	*3.8*
	1966	0.42	1.32	0.53	0.51	—	2.77	*1.8*	*4.8*
Japan	1964	−17	69	860	904[10]	—	1,816	*6.4*	*6.6*
	1965	−10	151	277	1,391[10]	—	1,809	*5.5*	*5.9*
	1966	797	217	433	1,575[10]	—	3,022	*5.7*	*8.6*

[1] Includes issues of semi-public credit institutions and nationalised industries. [2] Change in market holdings of bonded loans and medium-term notes. [3] Includes issues sold to foreigners; however, see footnote 2 to table on page 48. The 1966 figure above excludes US company issues in exchange for shares of German companies. [4] Includes indirect Treasury borrowing. [5] Includes privately-placed issues. [6] Change in marketable debt (excluding Treasury bills) in public hands. [7] Based on Federal Reserve flow-of-funds data, excluding mortgage loans. [8] Change in public holdings of marketable debt having a maturity of one year or more. [9] Gross. [10] Includes public corporation bonds.

bigger volume of funds was placed outside the banking system in other forms, including housing savings. In Belgium the decline in new issues was the result largely of a reduction in central-government flotations, which was offset to only a small extent by greater private and other borrowing.

With the exception of rises in Italy and Japan early in the year, share prices declined steeply in 1966 in most countries. The common cause was monetary tightness and the rise in long-term interest rates. But whereas in the United States, the United Kingdom and Canada the decline was associated in part with a larger volume of share issues, new share flotations dropped off considerably in most continental countries. From the viewpoint of the borrowers, one reason for this was no doubt the depth that share prices had reached after several years of decline. From the viewpoint of lenders, one special factor on the Continent was the large volume of international bond issues, which drew long-term funds from domestic markets. Late in 1966, as monetary conditions eased and interest rates declined, share prices staged a recovery, especially in the United States, Canada and the United Kingdom.

The volume of foreign issues on domestic capital markets is shown for individual countries in the table on page 46 on a net basis and in the broader context of international issues as a whole in the table on page 48. The only markets, apart from that of the United States, where issues of this conventional type have at times reached significant proportions are Switzerland, the Netherlands and Germany. Throughout western Europe, apart from Germany, such issues generally require official approval, while in the United States they are subject, with certain exceptions, to the interest equalisation tax. In recent years the authorities in both Switzerland and the Netherlands have restricted foreign issues in order to ease strains on their domestic capital markets. In Germany the volume of issues has been limited more by the high prevailing rates of interest. Foreign issues on continental markets and in the United Kingdom rose to $531 million in 1966. Apart from a large issue by a US international company in Germany, there was a small increase in Switzerland, while in Italy and France approval was given for certain issues by international institutions.

Foreign issues in the United States in 1966 totalled $1,317 million, i.e. about $100 million less than in 1963, when the interest equalisation tax was introduced. Issues in the United States by continental Europe and the United Kingdom, which in 1963 had amounted to $347 million, were only $9 million last year. On the other hand, Canadian issues, which are conditionally exempt from the tax, accounted for 82 per cent. of the total in 1966, as against 54 per cent. in 1963. Up to a certain borrowing limit Japan is also exempt from the interest equalisation tax; however, in view of its external surplus last year, it borrowed neither in the United States nor elsewhere.

International issues, after rising steeply from $120 million in 1963 to $1,192 million in 1965, fell away somewhat to $1,155 million last year. In contrast to "foreign" issues on individual markets, these are organised by international underwriting syndicates for sale in a number of countries. They require no special consent in the main issuing centres, are denominated in various key currencies or currency combinations, and depend for their sale primarily on the freedom of various countries' residents to buy foreign securities. Within the 1966 total, issues by industrial and commercial companies increased considerably, and those by governments and international institutions declined, having shifted partly to domestic markets. Issues denominated in US dollars accounted for about two-thirds of the total, while the others were expressed in various currencies, particularly Deutsche Mark. As the effective yield on new issues continued to rise until the early autumn, companies increasingly shortened the term of borrowing in order to avoid long-term commitments at high rates. By September new private issues of five years' maturity gave an effective yield of over 7 per cent., while those at longer term offered 6¾ per cent. or more. In the spring of 1967 new five-year bond issues carried yields of 6–6¼ per cent., while those at long term were typically 6¼–6½ per cent.

Foreign and international bond issues.[1]

Borrowers	Years	Foreign issues on domestic markets: Continental Europe[2]	United Kingdom	Canada	United States	Total	International issues[2]	Total issues abroad
		in millions of US dollars						
Continental Europe	1963	149	—	—	192	341	93	434
	1964	74	4	—	45	123	406	529
	1965	66	4	—	25	95	441	535
	1966	75	14	—	9	98	413	512
United Kingdom	1963	16		—	155	171	—	171
	1964	15		—	5	20	—	20
	1965	23		—	80	103	25	128
	1966	12		—	—	12	40	52
Canada	1963	—	—		762	762	—	762
	1964	—	—		767	767	—	767
	1965	—	—		959	959	—	959
	1966	—	—		1,081	1,081	—	1,081
United States	1963	—	—	—		—	—	—
	1964	—	—	—		—	—	—
	1965	10	—	—		10	296	306
	1966	192[3]	—	—		192	474	666
Japan	1963	25	19	—	136	180	22	202
	1964	36	—	—	—	36	162	198
	1965	—	—	—	63	63	35	98
	1966	—	—	—	—	—	—	—
Rest of the world	1963	6	129	—	163	298	—	298
	1964	—	55	—	219	274	5	279
	1965	—	59	—	205	264	110	374
	1966	—	42	—	143	185	126	311
International institutions	1963	81	—	—	5	86	5	91
	1964	70	8	—	155	233	266	499
	1965	79	—	23	200	302	286	588
	1966	196	—	18	85	299	101	400
Total issues placed	1963	277	148	—	1,413	1,838	120	1,958
	1964	195	68	—	1,191	1,454	838	2,292
	1965	178	63	23	1,532	1,796	1,192	2,988
	1966	475	56	18	1,317	1,866	1,155	3,021

[1] Including private placements. Company borrowing through foreign subsidiaries is normally treated as borrowing by the country of the parent company. [2] Non-resident loans issued in Germany after the announcement of the 25 per cent. coupon tax in March 1964 are generally treated as international issues. Since such issues are exempt from the tax, they were issued at interest rates below those prevailing on the domestic market for sale mainly to foreigners. [3] Consists of US company issues in exchange for shares of German companies (principally by Texaco for shares of Deutsche Erdöl).

US companies and their foreign affiliates substantially increased their issues abroad last year. In view of their extensive direct investment plans, and given the US balance-of-payments guide-lines, these companies' international issues rose to $474 million from $296 million in 1965. Thus, borrowing by US companies and their affiliates accounted for over two-fifths of total international issues in 1966, as against about one-quarter in 1965. Issues by Scandinavian countries, which in 1964 had reached a high level, declined in 1965 and again last year. On the other hand, issues by borrowers from the EEC countries, after rising substantially in 1965, dropped off slightly.

Together, foreign and international issues amounted to over $3,020 million in 1966. This figure, though only marginally above that for 1965, was over half as much again as the $1,960 million recorded in 1963. Almost all the growth over this three-year period was in international issues, which rose from about 6 per cent. of the total in 1963 to 38 per cent. in 1966. Moreover, of the overall increase of about $1,065 million, the United States and Canada accounted for well over 90 per cent. Continental borrowers, restricted by both the interest equalisation tax and tighter conditions in the principal continental centres, shifted over from 1964 onwards largely to international issues. In 1966 borrowing by the United Kingdom was negligible, while Japan was out of the market altogether. The rest of the world has shared to some extent in the recent growth of the market by larger recourse to international issues and indirectly through the activities of international institutions.

In the first four months of 1967 issues of the international type totalled $623 million, compared with $529 million in the corresponding period of 1966. Within these totals, issues by US companies and affiliates declined to $130 million from $261 million, while those by western European borrowers rose to $338 million from $188 million.

Credit developments in individual countries.

United States. The Federal Government's growing budget deficit, combined with a further strengthening of private credit demand, set the stage late in 1965 for a decisive turn towards monetary restraint. In the second half of the year, according to flow-of-funds data, the private sector's holdings of currency and demand deposits rose at an annual adjusted rate of $12.8 milliard, as against one of only $2.9 milliard in the first six months. Most of this change was due to the emerging budget deficit, which the Treasury financed from cash balances and by short-term borrowing. Moreover, bank loans to business began to advance sharply in the fourth quarter.

In December 1965, after market interest rates had risen appreciably in the autumn, the Federal Reserve authorities raised the discount rate from 4 to 4½ per cent. At the same time the maximum rates payable on time deposits under Regulation Q were increased by 1–1½ per cent. to a new high of 5½ per cent. Over the first eight months of 1966 the Federal Reserve authorities gradually intensified the restraint, mainly by limiting their acquisition of government securities. The tightening was reflected in a rise in

United States: Total net funds supplied to the credit markets.

By sectors and financial instruments	1964	1965 1st half	1965 2nd half	1966 1st half	1966 2nd half
	in milliards of US dollars, at annual adjusted rates				
Increases in assets					
Private sector[1]					
Currency and demand deposits	6.5	2.9	12.8	3.2	2.5
Time and savings accounts					
at commercial banks	13.0	19.2	19.8	17.0	7.6
at savings institutions.	15.8	12.8	13.4	7.3	7.3
Securities and other credit-market claims . .	8.4	10.2	9.3	20.7	21.5
Private insurance and pension funds	11.1	11.5	11.9	12.1	13.5
Other[2]	12.0	15.5	6.9	19.3	9.1
Total	66.8	72.1	74.1	79.6	61.5
Credit supplied to borrowers via					
Commercial banks and Federal Reserve System	24.9	28.5	37.9	27.7	16.7
Other financial institutions	28.9	27.6	26.7	21.0	22.4
Direct financial investment	13.0	16.0	9.5	30.9	22.4
Total	66.8	72.1	74.1	79.6	61.5
Increases in borrowers' liabilities					
Private sector[1]					
Bank and other loans	10.7	17.9	18.6	20.0	15.3
Consumer credit	8.0	9.8	9.1	8.1	5.7
Mortgages	25.7	24.9	26.0	21.7	17.6
Corporate securities	5.4	5.7	5.1	13.6	9.3
State and local obligations	5.9	7.4	7.4	6.3	5.5
US Government					
Short-term securities	4.0	4.6	2.4	— 6.6	4.6
Other securities	3.0	0.7	— 0.6	15.5	
Cash balances (increase —).	— 0.2	— 2.2	4.2	— 1.9	2.9
Foreign borrowers	4.4	3.3	1.9	2.4	1.2
Total	66.9	72.1	74.1	79.6	61.5

[1] Excluding financial institutions. [2] Including government, foreign and miscellaneous claims.

member banks' net borrowed reserves from only $2 million in December 1965 to $390 million in August 1966.

Concurrently, despite the increase in Regulation Q ceilings, the commercial banks began to experience competition for funds as a result of rising market interest rates, especially long-term ones. The corporate sector more than doubled its recourse to new capital issues while continuing to increase its bank loans at about the same rate. Moreover, the Federal Government, partly to improve its budget, arranged that Federal agencies should rely less on budgetary funds and more on the sale of new issues and participation certificates. As a result of these developments, the proportion of financial funds invested directly in the credit markets as an alternative to placement with financial institutions rose from 13 per cent. in the second half of 1965 to 39 per cent. in the first half of 1966.

None the less, the commercial banks succeeded in continuing to expand their loans rapidly during this period. Competing more aggressively for funds, the banks quickly raised the rates payable on certificates of deposit to their ceilings and began to offer such certificates in small denominations. Moreover, the banks with overseas branches borrowed large amounts of foreign-owned dollar balances. To help meet loan demand, the banks cut back their holdings of government securities and slowed down their purchases of State and local-government issues, thus contributing to market pressures making for higher interest rates. They also stiffened their own lending terms, increasing the prime loan rate four times — from 4½ to 6 per cent. — between December 1965 and mid-August 1966. As late as July, however, business loans were still advancing at an annual rate of about 20 per cent.

Higher market interest rates, together with the competition of commercial banks for deposits, fell particularly hard on the savings institutions and the mortgage market. In the United States, unlike some countries, these institutions do not have the possibility of periodically adjusting debtor interest rates on outstanding mortgage contracts to changes in market conditions. Hence they had little scope for putting up effective resistance to the competition for funds from other quarters by raising their deposit rates. The rate of formation of time and savings deposits at savings institutions declined from $15.8 milliard in 1964 to $13.1 milliard in 1965 and then plummeted to an annual rate of $7.3 milliard in 1966.

During the summer the Federal Reserve took various steps to redress the balance between the commercial banks and the savings institutions. In July the Regulation Q ceiling on new multiple-maturity time deposits was reduced to 5 per cent. for deposits at 90 days or more, and to 4 per cent. for those at shorter term. Between July and September reserve requirements on time deposits in excess of $5 million (consisting mainly of certificates of deposit held by business firms) were raised in two steps from 4 to 6 per cent. Bank issues of promissory notes maturing in less than two years were also brought under reserve-requirement and interest-ceiling regulations.

Credit-market strains approached crisis proportions in the late summer. Fiscal action remained uncertain, while business firms' continued anticipatory borrowing, together with sales of Federal agency securities, weighed heavily on the market. In addition, the banks were faced with a possible run-off of certificates of deposit owing to September tax payments. At about this time, too, the commercial banks' loan/deposit ratio touched a post-war high of almost 67 per cent., while that for the New York banks went to almost 80 per cent. Against this background, the Federal Reserve authorities on 1st September requested the member banks to slow down the expansion of their loans, particularly to business firms. It was indicated, moreover, that adherence to this objective would be kept in mind by the Federal Reserve authorities when member banks came to the discount window.

Other measures quickly followed. Early in September the Administration announced the suspension of tax benefits on new investment outlays on plant and equipment, as well as a curtailment of agency issues until the end of the year. In late September Congress enacted temporary legislation permitting greater differentiation in the establishment of interest ceilings on time and savings deposits. The Federal Reserve promptly reduced from 5½ to 5 per cent. the maximum rate payable on time deposits of less than $100,000, thus putting the commercial banks in a less favourable competitive position vis-à-vis savings institutions.

As much of the growth of demand for funds had been based on inflationary expectations, the September measures produced a sharp reaction in the credit markets. From the beginning of September 1966 to the end of March 1967 business loans by the Federal Reserve's weekly-reporting member banks increased by only $3.7 milliard, as against a rise of $5.9 milliard a year earlier. Over the same period, aided by a progressive easing of monetary policy, the banks acquired $5.2 milliard of securities, whereas in the corresponding months of 1965–66 they had reduced their portfolio by $1.8 milliard.

Just before the end of 1966 the Federal Reserve authorities announced that their September statement on business loans and discount administration was no longer applicable. In March 1967 reserve requirements were reduced from 4 to 3 per cent. for savings deposits and for time deposits of up to $5 million. Over the whole six-month period, moreover, open-market operations were geared to ease the banks' liquidity position, which shifted from net borrowed reserves of about $400 million in the August-October period to net free reserves of about $300 million in early April 1967. In addition, the banks repaid to their overseas branches a substantial volume of foreign-owned dollars borrowed in earlier months.

From about November 1966 onwards short-term market interest rates declined sharply. Towards the end of January 1967 the banks began to adjust their prime loan rate, in most cases from 6 to 5¾ per cent., and in late March a rate of 5½ per cent. was generally adopted. On 7th April 1967 the official discount rate was lowered from 4½ to 4 per cent. By May the yield on long-term government securities, which after rising to 4.80 per cent. in August 1966 had by mid-March dropped to below 4.45 per cent., had risen again to around 4¾ per cent. The recent increase was occasioned by a heavy volume of security issues, reflecting both corporate demand and a resumption of Federal agency issues. In general, however, long-term funds have been relatively plentiful, particularly in the mortgage market, and residential housing has shown signs of upturn. The tax benefits on new business investment were restored as from early March, and investment plans may now be upgraded as a result of the temporary postponement of the 6 per cent. tax surcharge.

Canada. A further intensification of monetary restraint in early 1966, combined with an impressive package of fiscal and budget measures in March, helped to slow down the growth of credit in the first half of the year. In this period the increase in the chartered banks' domestic assets dropped to an annual rate of 3 per cent. from 12 per cent. in 1965. In December 1965, concurrently with the US discount rate increase, Bank rate was raised from 4¼ to 4¾ per cent. But, unlike in the United States, it was increased again to 5¼ per cent. in early March prior to the new budget. During these months, moreover, bank liquidity was kept under pressure by debt-management

Gross national saving and investment.

Countries	Years	Gross national saving			Total saving and investment	Gross national investment			
						Gross domestic fixed capital formation		Change in stocks	Net external balance
		Households	Enterprises	Public authorities		Housing	Plant and equipment		
		as percentages of gross national product at market prices							
Belgium	1964	8.2	11.4	2.2	21.8[1]	5.8	15.4	0.4	0.1
	1965	9.2	11.3	1.3	21.8[1]	5.7	15.0	0.1	0.9
	1966	9.2	10.7	1.1	21.0	5.7	15.2	0.5	− 0.4
Denmark	1964	16.0		5.7	21.7	4.2	17.7	2.1	− 2.3
	1965	16.0		5.5	21.5	4.3	17.6	1.6	− 2.0
	1966	.		.	21.6	4.4	17.3	1.2	− 1.3
Finland	1964	7.6	11.9	7.4	26.9	5.3	19.3	4.6	− 2.4
	1965	8.2	11.4	7.4	27.0	5.6	19.8	3.9	− 2.3
	1966	7.0	11.4	7.2	25.6	5.5	19.7	2.4	− 2.0
France	1964	9.3	8.1	4.0	21.4	5.8	14.9	1.9	− 1.1
	1965	9.6	8.2	4.0	21.8	6.6	15.0	0.4	− 0.1
	1966	9.5	8.3	4.1	21.9	6.3	15.4	1.0	− 0.7
Germany	1964	8.3[2]	11.8	7.7	27.8	6.3	20.1	1.1	0.3
	1965	9.2[2]	11.3	6.2	26.7	6.0	20.5	1.5	− 1.3
	1966	8.7[2]	11.2	6.3	26.2	6.0	19.6	0.2	0.4
Italy	1964	19.8		3.8	23.6	7.7	14.1	0.6	1.2
	1965	22.6		0.9	23.5	6.8	12.1	0.7	3.9
	1966	22.5		0.7	23.2	6.2	12.2	1.2	3.6
Netherlands . . .	1964	9.8	12.7	4.0	26.5	4.5	20.4	2.7	− 1.1
	1965	9.8	11.9	4.2	25.9	4.9	19.6	1.3	0.1
	1966	9.7	12.0	4.2	25.9	5.0	20.0	2.0	− 1.1
Norway	1964	20.7		6.4	27.1	4.1	23.8	0.4	− 1.2
	1965	22.4		6.1	28.5	4.0	24.6	1.4	− 1.5
	1966	21.9		6.4	28.3	3.9	24.6	1.5	− 1.7
Sweden	1964	8.4	6.6	9.1	24.1	5.7	17.3	1.2	− 0.1
	1965	7.0	6.1	10.4	23.5	5.8	17.3	1.9	− 1.5
	1966	6.8	15.9		22.7	5.3	17.6	0.9	− 1.1
Switzerland . . .	1964	8.9	13.1	5.5	27.5	7.6	21.9	1.4	− 3.4
	1965	9.7	13.2	5.1	28.0	7.1	20.6	0.8	− 0.5
	1966	9.0	18.9		27.9	6.7	20.0	0.7	0.5
United Kingdom .	1964	5.8	10.7	2.5	18.4[1]	3.7	14.0	1.9	− 1.2
	1965	5.7	10.4	3.4	18.6[1]	3.7	14.1	1.1	− 0.3
	1966	5.1	9.2	4.4	18.1[1]	3.5	14.1	0.7	− 0.2
United States . .	1964	7.4	8.7	2.8[3]	18.7[1]	4.5[3]	12.6[3]	0.7	0.9
	1965	7.2	8.8	3.6[3]	19.4[1]	4.2[3]	13.3[3]	1.3	0.6
	1966	7.0	8.7	3.6[3]	19.2[1]	3.6[3]	13.8[3]	1.6	0.2
Canada	1964	4.3	14.9	3.8	23.0[1]	4.3	18.8	0.8	− 0.9
	1965	5.6	14.0	4.7	24.3[1]	4.1	20.6	1.8	− 2.2
	1966	6.0	13.4	5.1	25.0[1]	3.8	22.0	1.7	− 1.9
Japan	1964	11.9	16.4	7.7	36.2[1]	5.6	27.2	4.0	− 0.6
	1965	12.6	15.5	7.6	34.4[1]	6.0	25.3	2.0	1.1
	1966[4]	8.3	16.7	8.4	33.3[1]	6.4	26.6	− 0.8	1.1

[1] Including a residual error. [2] Includes depreciation charged on residential buildings. [3] Including, as an element of both saving and investment, new civil public construction. [4] January–September.

and open-market operations, and there was an increase in the volume of longer-term government bonds in the hands of non-bank residents, excluding government accounts. The chartered banks' liquid assets ratio, which had been declining since late 1963, continued to fall until June 1966.

Towards the middle of the year aggregate demand showed signs of moderating. Over the summer months, however, international financial developments were such that monetary conditions in Canada continued to tighten. The Bank of Canada sought to mitigate these tendencies, though on external grounds it could not counteract them altogether, by giving strong support to the bond market in July and August. The average yield on long-term government bonds rose to a peak of nearly 6 per cent. in late August, which was a full percentage point above the level of January 1965, when the uptrend began.

At all events, the monetary authorities' actions served to ease bank liquidity and credit availability from the middle of 1966 onwards. Credit expansion was resumed, even in the face of higher interest charges, and the chartered banks' total loans expanded at an annual rate of 9 per cent. in the second half of the year. Bank liquidity also improved, partly as a result of an increase in the central government's financing requirement, which was met to some extent by central-bank purchases of government securities in this period. Bank lending to both the private sector and local authorities picked up speed and industrial production showed a new advance from the late summer onwards. This development was strengthened by the September reversal in market conditions in the United States and Canada, though the long-term interest differential in favour of Canada tended to widen up to the end of the year.

Both the chartered banks and other financial institutions experienced somewhat slower deposit growth in 1966, reflecting their difficulty in competing for funds as capital-market interest rates rose. As in the United States, credit restraint bore with particular severity on the housing sector, and mortgage approvals in the second half of the year were almost one-third lower than in 1965. Over the year as a whole the non-financial corporate sector substantially reduced its net recourse to bank and other loans — and to a lesser extent to new capital issues — but this reduced flow of funds was compensated partly by a marked rise in direct investment by foreigners. The decline in new corporate issues was more than offset by a large increase in flotations by the central and local governments, so that net capital issues rose by almost $750 million to over $2.7 milliard in 1966. Another feature last year was the coming into force of the national pensions scheme. The amount contributed totalled almost $530 million and was largely lent on to the provinces to finance their rapidly expanding outlays.

Towards the close of the year and early in 1967 credit conditions eased further as interest rates declined in international markets. With private investment showing weakness, both in plant and equipment and in housing, the Bank of Canada acted so as to increase bank liquidity. At the end of January 1967 Bank rate was reduced from 5¼ to 5 per cent. and in April, coincident with the US reduction, it was lowered to 4½ per cent. To stimulate investment activity some of the restrictions introduced in the March 1966 budget were lifted later in the spring. In May the new Bank Act came into force, the effect of which is likely to be an increase in competition between financial institutions and greater bank participation in mortgage lending.

United Kingdom. As broadly conceived in the spring of 1966, government policy implied a continued need, at least until the autumn, for heavy reliance on monetary restraint. The May budget, though designed to yield a substantially larger revenue surplus, was not to have its main impact until later in the year, when the selective employment tax was to take effect. Moreover, incomes policy, still based on voluntary restraint under conditions of high demand, was not producing the necessary results.

In February 1966 quantitative restrictions on sterling lending to the private sector were further tightened. Whereas in the year to March 1966 the clearing banks had been asked to limit the growth in their advances to 5 per cent., they were now requested to regard the level set for March as a ceiling, seasonal movements apart, until further review. As on earlier occasions, and in more general terms, other banking and financial institutions were also asked to exercise restraint. Furthermore, priority to credit for exports and productive investment was again recommended. About the same time hire-purchase terms were stiffened, the maximum payment period being put for cars at twenty-seven months and for most other goods at twenty-four months and the minimum down-payment requirements generally at 25 per cent.

As a result of these measures, consumer borrowing showed a further modest decline over the first half of 1966. Any effect this might have had on consumption, however, was swamped by the continuing rapid growth in personal disposable income. Moreover, private-sector investment, although it appeared to taper off somewhat, remained at a high level. This was facilitated in part by the utilisation of the remaining margin of expansion for bank credit. Between November 1965 and May 1966 advances to manufacturing industry, building and contracting, and retail trade rose on an adjusted basis by nearly 5 per cent. In addition, business firms turned increasingly to the capital market, where net issues by public companies grew to nearly £400 million in the first six months of 1966 from under £300 million in the preceding six months. In view of the buoyancy of public-sector expenditure — much of it for productive investment by public enterprises, on which credit policy could exert no real influence — business confidence remained high.

Thus, while monetary policy helped to contain the expansion of private-sector demand, it could do little actually to reduce it — and even less to curb overall demand.

The monetary measures taken as part of the July emergency programme aimed at both reinforcing domestic credit restraint and counteracting the previous rise in interest rates abroad. First the authorities announced that the existing ceiling on bank credit would remain unchanged up to March 1967 and until further notice thereafter. It was added that no special credit arrangements would be made to facilitate payment of the selective employment tax beginning in September. Shortly after, on 14th July, Bank rate was raised from 6 to 7 per cent. and the special deposits required from London clearing banks and Scottish banks were doubled. Moreover, hire-purchase terms were again tightened, mainly by a sharp increase in minimum down-payment requirements.

More significant, in terms of longer-run objectives, were the measures of fiscal, budgetary and incomes policy (see page 13). These measures, together with the selective employment tax, were designed to halt cost inflation, increase productivity and, by curbing consumption, raise the rate of national saving. Hence they offered the prospect that any resulting decline in private investment would be temporary and less pronounced than if reliance were placed on credit restraint alone.

The impact on the structure of savings and investment implicit in these policies may be seen in the wider context of developments during the past three years. From 1963 to 1966 public-sector fixed investment rose in money terms by over 45 per cent. to reach £3,115 million, while that in the private sector went up by 25 per cent. to £3,485 million. Within the private sector the increase by companies was about 30 per cent. and by the personal sector some 10 per cent. It may be observed that public-sector saving has shown even more rapid growth, rising from the equivalent of 48 per cent. of public-sector fixed investment in 1963 to 73 per cent. in 1966. The growth in public saving took place more at the expense of private consumption than of private saving, with public and private saving combined rising from 18.8 to 21.4 per cent. of the gross domestic product between 1963 and 1966. Despite the large expansion in public investment, fixed outlays by private companies increased over the same period from 7.2 to 7.9 per cent. of the gross domestic product.

These developments do not gainsay the fact that for most of the period 1963–66 gross domestic investment (including inventory investment) was permitted to rise too rapidly relative to the improvement in national saving. The

United Kingdom: Saving and fixed investment, by sectors.

Items	Years	Private sector			Public sector				Grand total
		Personal	Companies	Total	Public corporations	Central government	Local authorities	Total	
		in millions of £ sterling, at market prices							
Saving	1963	1,590	2,410	4,000	530	225	265	1,020	5,020
	1964	1,815	2,640	4,455	590	485	330	1,405	5,860
	1965	1,880	3,190	5,070	660	890	310	1,860	6,930
	1966	1,890	2,675	4,565	640	1,190	455	2,285	6,850
Fixed investment	1963	860	1,915	2,775	1,025	225	880	2,130	4,905
	1964	900	2,365	3,265	1,190	280	1,115	2,585	5,850
	1965	1,010	2,475	3,485	1,295	305	1,205	2,805	6,290
	1966	955	2,530	3,485	1,450	340	1,325	3,115	6,600
		as percentages of gross domestic product at factor cost							
Saving	1963	6.0	9.0	15.0	2.0	0.8	1.0	3.8	18.8
	1964	6.3	9.2	15.5	2.1	1.7	1.1	4.9	20.4
	1965	6.1	10.5	16.6	2.2	2.9	1.0	6.1	22.7
	1966	5.9	8.4	14.3	2.0	3.7	1.4	7.1	21.4
Fixed investment	1963	3.2	7.2	10.4	3.8	0.9	3.3	8.0	18.4
	1964	3.1	8.3	11.4	4.1	1.0	3.9	9.0	20.4
	1965	3.3	8.1	11.4	4.2	1.0	4.0	9.2	20.6
	1966	3.0	7.9	10.9	4.5	1.1	4.1	9.7	20.6

result was domestic inflation and a deterioration in net foreign investment. Thus, when the present downtrend in private investment is reversed, it will be important for public investment to be adjusted so as to avoid renewed strain on productive capacity.

In the more restrained domestic atmosphere which prevailed after July, credit policy remained generally unchanged. However, with the burden of restraint now shifted more to other instruments and with private demand receding, the programme of direct credit control ceased to be restrictive for priority borrowers. Its continued selective application, however, helped to ensure that the productive capacity released was not promptly reabsorbed in less essential activity. In addition, as the gilt-edged market gathered strength, the authorities made heavy sales of securities while allowing interest yields to decline gradually.

In 1966 as a whole the banking sector's advances (in all currencies) to UK residents rose by only £22 million, against an increase of £425 million, or 6½ per cent., in 1965. The direction of lending was broadly consistent with the official recommendation. The expansion of resident deposits was only 3 per cent., against 7½ per cent. in 1965, but it was still large compared with the rise in advances. The difference expressed itself mainly in a reduction of some £260 million in the banking sector's net liabilities to non-residents, reflecting the attraction of short-term dollar interest rates for much of the year and the lack of confidence in sterling.

The Exchequer returns for the calendar year 1966 show a substantial improvement on revenue account, largely offset by a further rise in Consolidated Fund lending, notably for investment by public enterprises and local authorities. The total financing requirement declined by £66 million to £531 million. However, the Exchequer's external transactions, predominantly official sales of foreign exchange and short-term assistance from overseas monetary authorities, covered £462 million of this deficit, compared with £118 million in 1965. Domestic borrowing was, therefore, very sharply reduced to only £69 million, against £479 million the year before. Domestic holdings of all forms of government debt outside the banking sector actually declined by £52 million, after a rise of £171 million in 1965. Net withdrawals of national savings, despite more generous terms, were particularly heavy. Recourse to the banking sector was reduced from £308 million in 1965 to £121 million in 1966. Moreover, this borrowing was very largely in non-liquid form: the further call for special deposits raised £100 million and the banking sector took up £119 million of government stocks and £85 million of tax reserve certificates. The banks' Treasury bill portfolio declined by £209 million. These changes helped to offset the sharp increase in bank liquidity resulting from the contraction of advances after July.

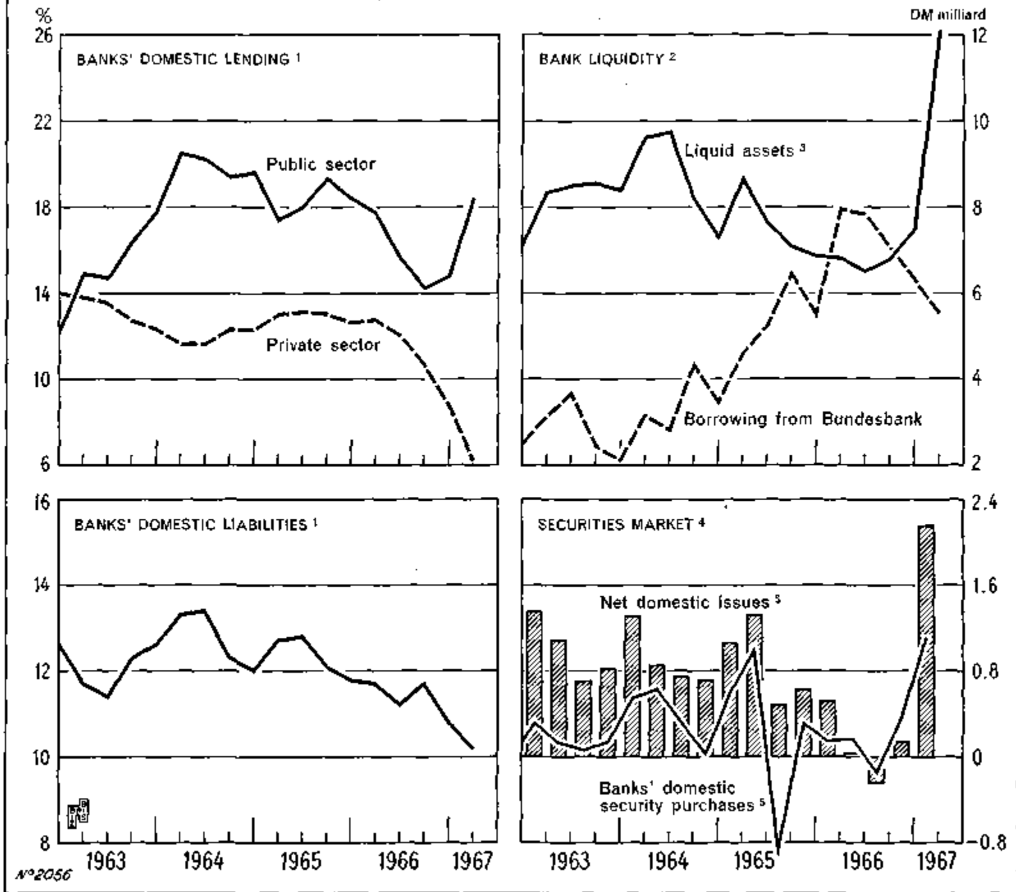
The course of Exchequer financing was influenced to a marked extent by developments in the capital market. Net issues by non-financial companies in 1966 rose by 40 per cent. to £566 million, including an increase of over 60 per cent. in issues by manufacturing industry, notably in the chemicals sector. Financial institutions raised £120 million, after only £38 million in 1965, and local-authority issues, at £189 million, although 10 per cent. less than in the previous year, were still very large. Within the total of net issues of £859 million, nearly 40 per cent. was concentrated in the first three months, which tended to depress the government bond market. By the end of the year, however, with less pressure from other borrowers, gilt-edged securities had recovered strongly and net sales to the public reached £410 million in the final quarter, bringing total Exchequer borrowing in this form for the year to £229 million.

The relaxation of US monetary policy at the end of 1966 and the related trend towards lower short-term interest rates in Europe made possible a reduction of 1½ per cent. in the UK Bank rate in the course of the first five months of the current year. This action added to the buoyancy of the gilt-edged market, which, if it is sustained, will go some way towards easing the sizable financing problem posed by the recent budget for the fiscal year 1967. With no net increase in revenue from new taxes, the expected decline of £100 million in the surplus of revenue over expenditure, and a comparable rise in central-government lending, would give an Exchequer borrowing requirement of £943 million, against £740 million in 1966–67. Moreover, the anticipated surplus on the UK balance of payments, together with the scheduled repayment of the IMF and Swiss loans, suggests that the Exchequer will need substantially to increase its borrowing from domestic sources. Efforts may be necessary, therefore, to avoid excessive government recourse to the banking system. At all events, the impact of Exchequer borrowing on monetary expansion will be mitigated by the continuation of credit control through official guidance on the direction of lending and the use of the special-deposits mechanism in the case of the clearing and Scottish banks, which as from 12th April were released from the obligation to observe a ceiling on advances. Other banks and the finance houses will continue to be subject to the ceiling (while other arrangements are being worked out) and to lending guidance.

Germany. The gradual intensification of monetary restraint from the summer of 1964 onwards did not create the same policy conflict as on earlier occasions. Inasmuch as domestic inflationary pressures were accompanied by an external payments deficit, there was not the same danger that capital inflows would be disequilibrating. Yet, dilemma there was. Public-sector budgets, instead of compensating for excess private demand, were themselves contributing to demand pressures and, indirectly, cost inflation. Inevitably, moreover, the effects of credit restraint were to some extent circumvented through recourse by domestic borrowers to loans from abroad. In these circumstances the containment of inflation by monetary policy led to increasingly high interest rates, carrying with it the usual risk of an abrupt shift in expectations concerning the profitability of investment.

In the early months of 1966 the demand for funds continued strong and the credit markets tightened further. On several occasions the Bundesbank

Germany: Selected monetary indicators.



¹ Percentage changes over corresponding quarter of preceding year. ² End of quarter, in milliards of DM. ³ Domestic money-market paper and foreign liquid assets. ⁴ Quarterly, in milliards of DM. ⁵ Excluding issues and purchases of bank bonds.

raised the rate on its transactions in money-market paper. In May, after both foreign and domestic interest yields had risen considerably, it increased the official discount rate from 4 to 5 per cent. and the rate on secured advances from 5 to 6¼ per cent. Also in May, the second phase of a reduction in rediscount quotas, absorbing about DM 1.3 milliard of unused facilities, became effective.

Deposit formation and bank credit expansion slowed down noticeably in the first six months of 1966. In this period the credit institutions' total deposit liabilities rose by only DM 9.4 milliard, as against DM 12.6 milliard a year earlier, reflecting mainly a curtailment in the expansion of sight deposits. Moreover, owing to very unfavourable capital-market conditions, the credit institutions cut back their bond issues to about DM 3.0 milliard from DM 6.1 milliard in the same period of 1965. To some extent the slower growth of resources was associated with a more moderate expansion in their lending, which declined to DM 14.7 milliard from DM 16.5 milliard in the first six months of 1965. Within this total, however, lending to the private sector continued strong and the increase, at DM 12.5 milliard, was much the same as in 1965. On the other hand, credit-granting to the public sector declined in the first half of 1966, falling to DM 1.8 milliard from DM 2.6 milliard in the corresponding period of 1965, owing mainly to an improvement in the cash budget position of the central government and the Länder. While this may have been partly due to deliberate budget restraint, it also appears that the limited accessibility and high cost of credit served to keep down public expenditure. Finally, in view of growing liquidity strains, the credit institutions cut back their acquisitions of securities to less than DM 300 million, whereas in the first half of 1965 they had bought DM 1,580 million.

As a result of autonomous forces, together with the growth of minimum reserve requirements, the absorption of bank liquidity in the first half of 1966 was almost DM 3.1 milliard, after having already amounted to over DM 6.1 milliard in the preceding eighteen months. The most important liquidity drain came from the external deficit, which was still large in the first quarter, and from an increase in the public authorities' deposits with the central bank. The credit institutions met their liquidity needs mainly from domestic sources, by borrowing from the central bank some DM 2.6 milliard and by selling to it money-market paper in the amount of almost DM 0.5 milliard.

The new-issues market, after weakening substantially in 1965, showed signs of a developing crisis in the first half of 1966. The yield on public-authority bonds, after rising from an average of 6.2 per cent. in 1964 to 7.7 per cent. by the end of 1965, moved steadily upwards to reach 8.4 per cent. by June 1966. New domestic bond issues in the January–June period totalled only DM 3.2 milliard, as against DM 7.8 milliard in the corresponding period of 1965. The banks' smaller acquisitions go some way towards explaining this smaller volume, as does also their reluctance to go to the market with their own issues. To some extent, too, the figures do not give the full picture, because medium and long-term direct lending by insurance companies and other non-bank institutions increased markedly, taking the place of previous bond purchases in the market. Moreover, the public authorities, through a self-imposed scheme of rationing, limited their own recourse to security flotations. Last but not least, the general public stood aside from the market, partly because of lower household savings and partly because interest rates were expected to go higher.

In terms of final demand, the decisive change appears to have come in the early summer of 1966, by which time tight credit conditions had initiated a decline in private fixed investment. In subsequent months the marked shift to an external surplus, together with an easing in the demand for bank credit, produced a complete reversal in the trend of bank liquidity. Since, however, the banks used their liquidity accruals largely to repay indebtedness to the central bank, conditions in the credit and capital markets were somewhat slow to change.

The private sector's demand for bank credit sagged in the second half of 1966 to DM 6.6 milliard, scarcely more than one-half the DM 12.4 milliard borrowed in the same period of 1965. The public authorities, on the other hand, increased their borrowing to DM 4.7 milliard from DM 4.3 milliard in the earlier period. However, the 1966 figure reflects in part the DM 1.0 milliard raised around the turn of the year in order to finance foreign exchange payments to the United States as an offset to military expenditure in Germany. Deposits with the credit institutions rose in the second half-year by DM 19.1 milliard, or slightly more than a year earlier. The banks' security portfolio increased by DM 220 million, whereas it had declined by DM 580 million in the last half of 1965. On balance, bank liquidity increased through autonomous market forces by DM 2,850 million in the second half of 1966. Some DM 1,850 million was used to repay indebtedness to the central bank, while most of the rest was employed abroad.

New bond issues in the July–December period came to only DM 2.3 milliard, or one-half as much as in the same period of 1965. The demand for funds was held in check by procedures governing the timing of issues and by mutual agreement among the public authorities. On the supply side, bond acquisitions by the banks remained small, while the general public, given the prevailing uncertainties, continued to show a high degree of liquidity preference. The yield on public-authority bonds rose further to 8.6 per cent. in July/August, but thereafter edged slowly downwards until November and then dropped by half a percentage point to 7.7 per cent. in December.

Towards the turn of the year demand had eased considerably, the underlying budget position was better and the external surplus was large and threatening to become larger. In these circumstances the Bundesbank moved towards a policy of active monetary ease. At the beginning of December, at first as a temporary end-year move, minimum reserve requirements for sight and time deposits were reduced by 9 per cent. At about the same time, in order to attract more funds to the domestic market, the Bundesbank suspended with effect from 1st January the regulation exempting from minimum reserve requirements the banks' deposit liabilities to foreigners in so far as they are offset by short-term foreign assets. To compensate for this, the reduction in reserve requirements was made permanent. On 6th January 1967 the official discount rate was lowered from 5 to 4½ per cent. and the rate on secured advances from 6¼ to 5½ per cent. With effect from 1st February the special reserve ratios for liabilities vis-à-vis non-residents were reduced from the legal maximum to the ratios in force for liabilities towards residents. On 17th February the official discount rate was again lowered by ½ per cent. to 4 per cent. and minimum reserve ratios were cut by 10 per cent. across the board. Following the April reduction in the US discount rate, the Bundesbank lowered its rate once again to 3½ per cent. With effect from May the minimum reserve requirements were cut by a further 5 per cent. Finally, the discount rate was reduced on 12th May to 3 per cent.

The return to monetary ease, and particularly the lowering of interest rates, has been carried out in harmony with developments abroad. Since interest levels elsewhere act as a constraint on the Bundesbank's actions, it proceeded cautiously in bringing rates down. As a structural measure, the Bundesbank agreed in March to abolish completely the fixing of maximum interest rates for bank credits and deposits. On the bond market yields declined further in the first few months of 1967, and in April the authorities shifted over from a nominal rate of 7 per cent. to one of 6½ per cent. To some extent a revival of demand will be stimulated by the anti-cyclical measures described on page 12, including increases in government expenditure financed by short-term credit. More generally, given the background of credit ease, it is expected that there will also be some autonomous recovery of demand later in the year.

Netherlands. In the years 1963–66 the Netherlands experienced a marked upward adjustment of costs and prices, accompanied by a fairly moderate deterioration in the balance of payments but also last year by difficulties in structurally weak industrial sectors. Sharp advances in wages, central and local-government expenditure, and investment in housing and industry provided the fuel for this inflationary movement. The strength of the emerging demand for funds, against the background of the central bank's efforts to restrict credit availability, may be seen in the course of interest rates. The yield on industrial bonds, which between 1959 and 1963 had fluctuated narrowly within a range of 3¾–4½ per cent., thereafter climbed steeply to reach 7½ per cent. by the summer of 1966. This movement, of course, reflects also the influence of rising rates abroad.

The central government's net financial requirement, after expanding from Fl. 310 million in 1963 to Fl. 1,040 million in 1965, went up further to Fl. 1,620 million in 1966. Within the year, however, the government was able to improve its position, largely as a result of the curbs on expenditure, particularly public investment, introduced in May. In the second half of 1966, for the first time since 1963, the growth of revenue outstripped that of expenditure. Over 1966 as a whole the government increased its recourse to long-term borrowing, but the proportion of its net financial requirement met in this way dropped from 74 to 66 per cent. To avoid subjecting the capital market to further strain, it borrowed relatively more at short term. After rising by Fl. 570 million in 1965, bank credit taken up by the central government went up in 1966 by Fl. 800 million, of which an appreciable part was reflected in an increase in floating debt vis-à-vis the Nederlandsche Bank.

After a sharp ascent to a peak of Fl. 2,220 million in 1964, the local authorities' net financial requirement declined for two years in succession, falling in 1966 to Fl. 1,760 million. This decline is attributable largely to the placing of quantitative limits on borrowing by public bodies. Last year, moreover, the local authorities were permitted to have access to the capital market only via central public-borrowing institutions, mainly the Bank for Netherlands Municipalities. The proportion of the sector's net financial requirement that was met by long-term borrowing dropped much more than in the case of the central government, viz. from over 95 per cent. in 1965 to

61 per cent. in 1966. However, recourse to bank credit and other short-term borrowing was confined mostly to the first half of the year. By the second half the sector's financial needs had been reduced further and were almost fully covered by long-term resources.

In the early part of 1966 the private sector's demand for bank credit was strong. Although the Nederlandsche Bank had fixed the ceiling for short-term credit-granting to this sector for the months January–April at 5 per cent., equivalent to three-quarters of the actual growth in the corresponding period of 1965, loans in fact increased by about 10 per cent. This led to a further tightening of monetary policy in May, when the discount rate was raised from 4½ to 5 per cent. and the lending ceiling was brought down, partly on seasonal grounds, to 4 per cent. for the period January–August as a whole. Shortly after, an easing of domestic demand set in. By late summer the demand for short-term bank credit had fallen off, and it did not show its usual seasonal recovery later in the year. On the other hand, longer-term bank lending, which at the request of the central bank was to be kept in line with the availability of longer-term resources, picked up in the latter half of the year.

In 1966, even more than in 1965, deposit formation lagged behind the expansion of bank credit, partly because of the balance-of-payments deficit and partly because of high yields in the capital market. The commercial banks' total loans rose by Fl. 1,520 million, or 12½ per cent., while their total deposits went up by only Fl. 690 million, or 6 per cent. In these circumstances the banks cut back their holdings of securities somewhat, particularly in the early months of the year, and borrowed rather more than usual from the central bank. What is more important, they further reduced their net foreign position by about Fl. 380 million. One may also note that increased recourse by Dutch firms to trade credit from abroad not only helped them to circumvent domestic credit restrictions but also mitigated liquidity pressures on the banks.

At Fl. 7,130 million, the net funds raised by domestic borrowers on the capital market in 1966, mostly in the form of private and mortgage loans, recorded an increase of 2 per cent., compared with one of 10 per cent. in 1965. However, because of the restraint shown by the public authorities, whose borrowing dropped by 21 per cent. to Fl. 2,140 million, the private sector was able to take up long-term funds to a total of Fl. 4,990 million, or 17 per cent. more than in 1965. The supply of funds from the banks and savings institutions contracted by 28 per cent. to Fl. 1,660 million, but this was more than offset by the growth of funds from institutional investors and a somewhat larger net inflow of foreign portfolio capital. The availability of new funds from business and households, at Fl. 1,200 million, was slightly less than in 1965 but still one-third greater than in 1964.

The combination of budget and monetary restraint applied in 1966 appears to have produced an easing of inflationary pressures without seriously impeding the continued expansion of industrial production. Long-term bond yields remained high until November, but they have since declined appreciably. On 15th March the Nederlandsche Bank reduced its discount rate from 5 to 4½ per cent. and for the time being exempted the banks from the obligation to make non-interest-bearing deposits with the central bank in the event of lending in excess of the prescribed ceiling. The ceiling itself was fixed for January–April 1967 at 4 per cent. of the amount outstanding in the last quarter of 1965. The central government expects a financing deficit in 1967 of about the same size as in 1966; it will in fact be more appropriate than last year's because of the present easier demand situation. The local authorities have been asked to limit until further notice their short-term borrowing to 105 per cent. of the amount outstanding in July 1966, and they will continue in 1967 to be obliged to centralise their borrowing on the capital market.

Belgium. In late 1965 and early 1966 a renewed economic upswing appeared to be taking firm hold. As a precautionary measure, designed to keep credit expansion within non-inflationary bounds, the National Bank in April requested the banks to limit the growth of their lending in 1966 to 12 per cent. of the end–1965 level. Within this limit the banks were also asked to give priority to loans for productive investment and to observe moderation in lending for building, consumption and speculative stock accumulation. In addition, it was recommended that the banks should finance medium and long-term lending only with resources of suitable maturity. The savings banks, life assurance companies and public credit institutions continued to be associated with the programme of credit restraint.

In the event the expansion proved short-lived. Under the influence of a weakening in exports, caused mainly by disinflationary measures taken in neighbouring countries, economic activity began to slow down in the spring. Cost inflation, however, continued to go ahead, leading in May to the imposition of a temporary price freeze. In order further to counteract rising costs, but also to help keep domestic interest rates in line with those abroad, the National Bank raised its discount rate from 4¾ to 5¼ per cent. on 2nd June.

The shift into external basic deficit in 1966 had a restrictive effect on the formation of liquid assets via the banking system. However, domestic bank credit expansion worked in the opposite direction. The Treasury had greater recourse to monetary financing, partly through borrowing abroad, and bank credit to the private sector accelerated. Thus, at B.fr. 34 milliard, the increase in money and quasi-money came to 8½ per cent., almost equalling the 9 per cent. rise in 1965.

The Treasury's net financial requirement fell from B.fr. 22.1 milliard in 1965 to B.fr. 17.1 milliard last year, thanks partly to an increase in indirect taxation as from the beginning of 1966 and partly to the restraint exercised over expenditure. In 1965 the Treasury had borrowed B.fr. 26.9 milliard on the domestic market, of which about two-thirds was at medium and long term, and had used B.fr. 4.8 milliard of the proceeds to reduce its foreign indebtedness. But last year, in view of the strains on the domestic credit markets, the Treasury turned once again to borrowing abroad, while continuing to have recourse to monetary financing for a considerable part of its reduced domestic borrowing.

Bank credit to the private sector, in so far as it was subject to the ceiling, went up by 4.4 per cent. in the first half of 1966 and by 15.4 per cent. for the year as a whole, as against 17 per cent. in 1965. Although the ceiling introduced in April remained in effect, the National Bank indicated at the end of June that it would agree to an overstepping of the limit in cases where this was due to investment credits enjoying a government guarantee or subsidy. The banking system's total credits to the private sector increased in 1966 by B.fr. 22.4 milliard, or 20 per cent., compared with 14½ per cent. in 1965. The strength of credit demand was largely a result of the squeeze on profits caused by the weakening of final demand and by the continued upward push of wages.

At the end of 1966 the National Bank prolonged the credit ceiling until mid-1967, at which time bank lending should not exceed 118 per cent. of the end-1965 level. Now explicitly excluded from the ceiling, however, are investment credits guaranteed or subsidised by the government and also export credits in the form of bank acceptances. As a move towards greater ease and in order to align rates with those prevailing internationally, the official discount rate was reduced in three steps between February and early May from 5¼ to 4½ per cent.

France. In 1966 the aim of policy was to encourage the renewed upswing of economic activity without jeopardising the degree of price and cost stability achieved in recent years under the stabilisation programme. This result was obtained by moderately expansionary budget and credit policies tempered by continued restraint on public-sector incomes as well as on liquid-asset formation. During the year controls over industrial prices were somewhat relaxed and the prices of certain agricultural goods and public services were adjusted upwards.

The central government's budget, after having been brought from a large deficit into balance over the years 1964–65, moved back into moderate deficit last year. At Fr.fr. 2 milliard, however, the deficit was more or less consistent with the need to promote economic expansion. In considerable part it was the result of larger outlays in favour of the nationalised industries and the social security system. It also reflected a 10 per cent. tax credit granted on investment goods purchased or ordered during the year and increased lending to the Fund for Economic and Social Development.

Although it helped to augment final demand, the budget was financed so as to limit the growth of money and quasi-money. This result was achieved partly through the issue of another National Equipment Loan — for Fr.fr. 1.5 milliard, as against Fr.fr. 1.0 milliard in 1965 — the proceeds of which were mainly used for re-lending to industry. But more important were the funds which accrued to the Treasury from postal and correspondents' accounts. In 1966 Treasury operations exercised a restrictive effect on liquid-asset creation of the order of Fr.fr. 1.7 milliard, whereas in 1965 they contributed to monetary expansion to the extent of Fr.fr. 0.5 milliard.

The deteriorating external payments position also tended to limit the growth of liquid assets. The banking system's net foreign position, after improving by Fr.fr. 5.58 milliard in 1965, recorded a gain (including debt repayment) of Fr.fr. 2.13 milliard for 1966 as a whole, although from the late summer onwards the position was one of deficit. On the other hand, credits to the private sector by the banking system (including the central bank) expanded by Fr.fr. 15.3 milliard, or 12.6 per cent., compared with 11 per cent. in 1965. This was attributable primarily to the further upswing in economic activity. Thus, as restrained by debt-management operations and the external position, the growth of money and quasi-money via the banking system came to Fr.fr. 19.1 milliard, or 9.7 per cent., which was slightly below the 10 per cent. rise recorded in the previous year.

Owing partly to a slowing-down in the expansion of the currency circulation, total bank deposits, including those at longer term, increased by Fr.fr. 13.8 milliard, thus showing a rise of 12.9 per cent., compared with 11.8 per cent. in 1965. Within this total, quasi-monetary assets with the banks went up by 26.5 per cent. This was the result of measures put into effect in early 1966 to give the banks greater opportunity to attract savings, both on booklet accounts and under a new housing-savings scheme, in competition with savings banks. On the other hand, the Treasury, by borrowing more from other sources, reduced its net indebtedness with the banks by some Fr.fr. 3.9 milliard. This, together with the high rate of deposit formation, helped the banks to increase their credits granted to the economy by Fr.fr. 16.9 milliard. This expansion amounted to 15.5 per cent., as against 13.4 per cent. in 1965. Medium-term credits for construction and, in a lesser degree, for equipment recorded substantial gains. The banks had recourse to rediscounting with the central bank and other institutions, but the total came to only Fr.fr. 1.8 milliard, or about Fr.fr. 1 milliard less than in 1965.

Total credit-granting by other financial institutions, including special credit institutions and the Treasury, went up in 1966 by Fr.fr. 18.4 milliard, or 15.2 per cent., compared with 13.8 per cent. in 1965. This was made possible by a larger supply of public funds from the Treasury, a faster growth of deposits with the savings banks and greater recourse to the capital market by the special credit institutions.

Net capital issues increased slightly, to Fr.fr. 12.4 milliard from Fr.fr. 12.2 milliard in 1965. Within this total, share issues dropped off appreciably, reflecting a further deterioration in conditions on the share market. However, the financing needs of industry were met to a larger extent through the intermediary of the specialised credit institutions and the Treasury. Combined, their gross bond issues went up from Fr.fr. 4.7 milliard in 1965 to Fr.fr. 6.5 milliard in 1966, the lending counterpart of which is reflected in the figures given in the preceding paragraph. About the middle of the year, in order to encourage a greater flow of capital, the authorities raised the nominal interest rate on new bond issues by ½ per cent.

Money-market interest rates, which were more under the influence of external developments, went up considerably, day-to-day rates rising by more than 1 per cent. to an average of 5.7 per cent. in December 1966. Throughout the year the discount rate was kept unchanged at 3½ per cent., and the authorities acted at times to ease market pressures, mainly through several reductions in the "coefficient de trésorerie". However, in the second half of the year, by which time an external deficit had emerged, the central bank provided funds to the market only at rising rates, thus helping to limit the outflow of capital. By early 1967 the rate on day-to-day money had fallen back to about 5 per cent.

Against the background of continued monetary stability, the authorities introduced further measures to broaden the activity of financial institutions and to spur competition between them. For instance, institutions specialising in financing investment, such as the Crédit National, and private housing, such as the Crédit Foncier, were granted permission to issue marketable medium-term bonds suitable for placement with banks. In addition, the banks were permitted to introduce long-term savings contracts carrying fiscal privileges. With a view to reducing the cost of housing loans and extending their term, efforts were also initiated to promote a mortgage market, principally through the agency of the Crédit Foncier.

With regard to monetary policy instruments, an important change came in January 1967 with the introduction of a system of compulsory reserves for all banks and statutory deposit institutions. Under this system the banks must place interest-free deposits with the Bank of France proportionate to the main items of their short-term French franc liabilities at up to three years. Introduced gradually, the system is to be fully operative by 21st October 1967, by which time the reserve ratios will be 4½ per cent. for sight deposits and 2 per cent. for other accounts. The limit to which these ratios may be raised by decision of the central bank is 10 per cent., as established for the time being by the National Credit Council. At the same time the "coefficient de trésorerie" was abolished but, as an interim measure, a minimum ratio in respect of securities representing medium-term credits was laid down. In addition, the banks' minimum Treasury bill ratio, which was part of the overall "coefficient", is to be progressively lowered from 5 per cent. to nil between January and 1st September 1967. In view of the introduction of virtually full capital-account convertibility early this year, the system of variable reserve requirements, combined with the greater use of open-market operations, provides the authorities with an additional element of flexibility in monetary management. For the immediate future, the deterioration in the balance of payments, the adherence to budgetary orthodoxy revealed in the estimates for 1967, and the more hesitant advance of economic activity should minimise the danger of any excessive growth of domestic liquidity.

Italy. The primary objective of economic policy in 1966 and early 1967 was to encourage the upswing in economic activity, especially in investment. Budgetary, debt-management and monetary policies contributed in unison towards this goal, against a background of relatively stable prices and wages and a declining external surplus.

So far as the government's rôle is concerned, the central administration's current-account surplus, expressed in national-income terms, increased from Lit. 186 milliard in 1965 to Lit. 433 milliard in 1966. Thus, after the central administration's own investment expenditure and capital transfers, its overall national-income deficit declined from Lit. 819 to 689 milliard. On the other hand, as a result mainly of government lending for investment purposes, the net requirement of the Treasury (including the Postal Savings Fund) rose from Lit. 1,543 milliard in 1965 to Lit. 1,867 milliard last year.

The Treasury's new borrowing from the credit institutions amounted in 1966 to about Lit. 800 milliard, compared with Lit. 600 milliard in 1965. But, whereas in 1965 about one-third of this borrowing was through sales of Treasury bills, in 1966 it derived almost exclusively from the banks' purchases of long-term government securities. Furthermore, the Treasury's net security sales to the general public rose from about Lit. 195 milliard in 1965 to Lit. 668 milliard in 1966. In these ways, together with postal savings and other borrowings, the Treasury was able through longer-term borrowing to meet about three-quarters of its net cash requirement, as against about two-fifths in 1965. Its position vis-à-vis the central bank, after having deteriorated by Lit. 293 milliard in 1965, showed a net improvement of Lit. 78 milliard in 1966.

The credit institutions' lending to the domestic economy went up by 14.6 per cent., against 7.2 per cent. in 1965, the rate of increase in private and public-sector credit being about the same. The rise in deposit liabilities, at 15.3 per cent., was even greater, though less than the 17.7 per cent. increase in the preceding year. The banks' loan/deposit ratio, which had been as high as 78.6 per cent. at the end of 1963, thus dropped in 1966 from 67.7 to 67.3 per cent. Besides accelerating their lending, the credit institutions again made heavy purchases of securities. Excluding their holdings of Treasury bills, which dropped off last year, the addition to their security holdings amounted to Lit. 1,340 milliard, representing an increase of 32 per cent., following one of 38 per cent. in 1965. The bulk of these acquisitions were government or government-guaranteed issues, and some Lit. 300 milliard, of which Lit. 200 milliard consisted of mortgage bonds, was used under existing regulations to meet compulsory reserve requirements. Another part, some Lit. 500 milliard, was used as collateral with the central bank. Hence the credit institutions' free portfolio of securities rose by less than Lit. 525 milliard, or just over 20 per cent.

Among the factors adding to bank liquidity, the Treasury's deficit operations in 1966 provided Lit. 1,867 milliard, while liquidity creation via the external surplus declined to Lit. 418 milliard from Lit. 994 milliard in

1965. On the other hand, bank liquidity was absorbed to the extent of Lit. 1,392 milliard through the growth of the currency circulation and minimum reserve requirements. Thus, the net increase in liquidity resulting from these autonomous factors came in 1966 to Lit. 809 milliard, as against Lit. 1,066 milliard in 1965. As to the effects of policy, the authorities' net sales of securities as the result of debt-management and open-market operations absorbed liquidity in the amount of Lit. 1,370 milliard, though this absorption was mitigated by the already-mentioned use of Lit. 300 milliard of securities to meet reserve requirements. Moreover, in accordance with existing instructions, the banks used part of their liquid resources to bring their net foreign position into equilibrium. On balance, these policy factors drained away more liquidity than was created by autonomous forces, thus constraining the banks to increase their borrowing at the Bank of Italy by almost Lit. 535 milliard, as against only Lit. 35 milliard in 1965.

The loans of the special credit institutions increased by 14 per cent. to reach almost Lit. 9,310 milliard at the end of 1966. At this level these institutions' loans, which are mainly at longer term for investment in industry, construction and agriculture, are about three-fifths as large as those of the other credit institutions. Last year the special credit institutions, for their own account, issued new bonds totalling Lit. 945 milliard, representing an increase of 12 per cent. In addition, they issued Lit. 887 milliard for the account of the Treasury (including railway bonds).

The capital market was very receptive in 1966, net issues advancing from Lit. 2,377 to 3,290 milliard. Although the absolute amount taken by the banking sector increased, its share in the total declined appreciably, reflecting a strong interest on the part of the general public and institutional investors for fixed-interest securities. The relative stability of consumer prices and interest rates over a sustained period helps to explain this, but a reluctance to invest in housing and shares also played a significant part. The share market remained under the shadow of fiscal deliberations, which culminated in February 1967 in the withdrawal of the option to pay tax at a flat rate of 30 per cent. on dividends instead of declaring the dividend receipts for income-tax assessment.

In early 1967 the economy continued to advance buoyantly. In March the yield on industrial bonds, at 6.7 per cent., was at about the same level as a year earlier.

Switzerland. Despite a constantly high savings ratio, a further decline in real investment and a slow-down in the growth of the real national product, credit markets remained tight throughout 1966. To some extent this was the result of cost inflation, which pushed up the economy's credit needs. More important, however, Swiss credit-market developments in 1966 were influenced to a large extent by the tightening of capital and credit markets abroad. Despite a further upward adjustment of domestic interest rates — industrial bond by ¾ per cent. and mortgage by ¼ per cent. — identified net long-term capital exports increased from Sw.fr. 260 to almost 750 million in 1966.

Owing to the attraction of higher interest rates abroad, any efforts by the monetary authorities to prevent a rise in domestic rates through liquidity creation would have run counter to the primary goal of containing domestic inflation. So far as interest rates are concerned, therefore, the National Bank's policy was essentially limited to smoothing out and keeping in check the upward movement. Thus the increase in the official discount rate from 2.5 to 3.5 per cent. in July 1966 represented primarily an adjustment to the higher call-money rates, which had risen from a monthly average of 2.75 per cent. in January to 3.75 per cent. in June.

Capital exports last year were largely covered by the current-account surplus and, apart from temporary fluctuations, the balance of payments did not have a restrictive impact on the domestic money supply. In fact the National Bank's gold and foreign exchange holdings went up by Sw.fr. 340 million on a December-to-December basis. The note circulation rose by Sw.fr. 610 million, or 6.1 per cent., while the increase in the total money supply amounted to only 3.8 per cent. and was thus considerably smaller than the 7.2 per cent. rise in the nominal gross national product.

The tightness of monetary conditions abroad was also reflected in the slower growth of the banks' resources, which expanded by only Sw.fr. 5,025 million, or 7.3 per cent., compared with Sw.fr. 5,480 million, or 8.7 per cent., in 1965. Demand deposits showed virtually no increase, whereas time deposits went up by 12½ per cent. This development was partly the result of the higher interest rates which the banks, in view of the lending possibilities on the Euro-currency markets, were able to offer on fixed-term deposits. To some extent it also reflected the reserved attitude of Swiss investors, who owing to the upward trend of interest rates were reluctant to buy medium-term cash certificates and other longer-term bank paper. In fact, the rate of increase of cash certificates outstanding dropped from 13.6 to 4.0 per cent. The growth of savings deposits, at just over 8 per cent., was much the same as in 1965.

In contrast to the banks' reduced intake of funds, their rate of credit expansion accelerated from 8.8 per cent. in 1965 to 9.3 per cent., leading to a reduction in their liquidity position. The increase in foreign credits was particularly pronounced, but lending to residents, which in the case of some banks ran up against the official credit ceilings, also advanced at a rate of about 8 per cent. The system of statutory ceilings on credit expansion, which was due to expire in March 1967, was replaced as from January 1967 by a central-bank guide-line which (with certain exceptions) puts the maximum rate at which banks may expand their credits to residents in 1967 at 7 per cent. of the end-1966 totals, and which thus tries to bring the rate of credit creation rather more into line with the actual growth possibilities of the economy. This limit must also be seen against the background of an anticipated considerable growth in the public sector's financial requirements in 1967.

The capital markets in 1966 were characterised by a situation of excess demand. The Swiss Banking Commission continued to ration new issues rather stringently but, with a ¾ per cent. rise in bond yields, total net placements, at Sw.fr. 2,810 million, were about Sw.fr. 250 million higher than in 1965. Within this total, a larger proportion was accorded to foreign issues, which increased from Sw.fr. 260 to 425 million. In addition, in March 1966 the Swiss banks were authorised to participate with a share of up to 10–15 per cent. in issuing consortia for certain international loans. Moreover, the Swiss authorities gradually rescinded in the course of 1966 the restrictions which had been imposed in the spring of 1964 on the investment of foreign capital in Swiss bonds, shares and other types of securities. The prohibition of the payment of interest on foreigners' Swiss franc deposits and the banks' obligation to offset any net increase in such deposits by investing abroad or by making a non-interest-bearing deposit with the National Bank expired in March 1967.

Austria. Economic activity remained stable at a high level in 1966. Partly owing to the slowing-down of growth in other countries, exports showed weakness. Industrial earnings advanced by 12 per cent. but the cost of living went up by only 2 per cent. The expansion of consumption contributed to a marked rise in imports and a widening of the external payments deficit. Industrial investment, on the other hand, was only marginally higher than in 1965.

The demand for credit remained keen, particularly in the first half of the year, and the credit institutions came under liquidity pressure, partly on account of the balance-of-payments deficit. In view of the wage and price trend, and of the external imbalance, monetary policy steered a cautious course. To discourage borrowing from the central bank, the rate for secured advances was raised around mid-year by ½ per cent. to 5½ per cent. On the other hand, the banks' credit ceiling was raised from 68 to 70 per cent. of their liabilities, thus permitting increased lending by banks in a liquid position. In August, moreover, the central bank redeemed Sch. 1 milliard of money-market Treasury certificates issued in July 1965 to absorb liquidity. On the average the credit institutions' indebtedness to the central bank amounted in 1966 to Sch. 2.4 milliard as against Sch. 535 million in 1965, though in December it was back near the level of a year earlier. More important, the credit institutions had substantial recourse to short-term borrowing abroad, their overall foreign position shifting from net assets of Sch. 240 million at the end of 1965 to net liabilities of Sch. 1.6 milliard at the end of 1966. In consequence, despite the external deficit, the official reserves increased by over Sch. 500 million.

The credit institutions' loans rose in 1966 by Sch. 14.7 milliard, or 16 per cent., compared with a growth of about 18 per cent. in 1965. At Sch. 2.1 milliard, their net purchases of domestic securities were almost the same as in the preceding year. The expansion of their deposits, on the other hand, was only Sch. 11.2 milliard, representing an increase of 10.8 per cent., compared with 13.3 per cent. in 1965. Thus, besides reducing their holdings of Treasury certificates and having recourse to central-bank credit and foreign borrowing, the credit institutions also increased their own bond issues, which went up by Sch. 2.4 milliard, as against Sch. 1.5 milliard the year before.

In early 1967, with industrial activity below its level of a year earlier, industrial investment was expected to show a decline of about 7 per cent. for the year as a whole. Public expenditure, on the other hand, is to increase markedly, and the government, in order to leave the capital market free for the private sector, plans to meet part of its financing requirements by borrowing abroad. Early in 1967 monetary policy shifted towards greater ease, and on 18th April the National Bank reduced its discount rate from 4½ to 4¼ per cent.

Denmark. Demand pressures, which had been strong throughout most of 1965, were more moderate in the early months of 1966, reflecting mainly a slowing-down in the growth of industrial investment and exports. This easing was partly the result of monetary and fiscal measures taken in 1965 but it was also attributable to stabilisation efforts by other countries and the continuing rise of Danish costs. Led by residential construction, economic activity gathered force again from the spring onwards. Industrial investment and exports remained weak, however, and consumer prices, though rising less than in 1965, went up by about 5 per cent. over the year as a whole.

The government's budget helped significantly to restrain consumption and enlarge saving. In 1966 the cash budget surplus rose to D.kr. 1,215 million from D.kr. 685 million in 1965. For the most part, except for scheduled debt redemption, the surplus went to improve the government's accounts with the central bank. In turn, the Nationalbank put a roughly equivalent amount of funds into the capital market through the purchase of long-term government bonds.

In 1966 the central bank's government security purchases plus government debt redemption came to D.kr. 1.0 milliard, whereas in 1965 this total had reached D.kr. 1.5 milliard. In 1965, however, the central bank's intervention in the market had been designed to ease even greater strains on the capital market, as mortgage bond and other issues had risen by 37½ per cent. to D.kr. 5.1 milliard. But in 1966, largely in consequence of the ceilings imposed on mortgage lending as from the middle of 1965, such issues dropped back by 14 per cent. to a level of D.kr. 4.4 milliard. The interest rate on first mortgage bonds, after rising from about 6¾ per cent. in early 1964 to above 9 per cent. in the spring of 1965, remained relatively stable until late in 1966, when it moved to above 9¼ per cent.

The commercial banks' activity expanded sharply in 1966, their loans having increased by 15½ per cent., as against 9½ per cent. in 1965. Reflecting partly the public's liquidity preference, demand and time deposits rose in about the same proportion, providing scope for the banks to increase their investments. Their purchases of bonds and shares, amounting to D.kr. 535 million in 1966 compared with D.kr. 180 million in 1965, gave added support to the capital market.

The credit measures in force in 1966 remained basically the same as those introduced in 1965. In February 1965 the commercial banks, in a voluntary arrangement with the Nationalbank, had agreed to place 20 per cent. of any increase in their deposits in a special account with the Nationalbank or, alternatively, to utilise it to improve their net foreign position. In March a similar agreement was reached with the savings banks. Subsequently, in January 1967, it was laid down that banks may cover special deposit commitments arising from December 1966 onwards by depositing bonds of under ten years' maturity with the Nationalbank.

These measures were effective in limiting the banks' access to liquid funds from abroad. In fact, the commercial banks reduced their net foreign liabilities from D.kr. 305 million in December 1965 to D.kr. 180 million in December 1966. The measures were also effective in sterilising about D.kr. 100 million in special deposits over the year. They did not, however, prevent the banks from turning to central-bank credit in the form of discounts and advances, which rose from D.kr. 895 million in December 1965 to D.kr. 1,615 million in December 1966. The official discount rate remained unchanged at 6½ per cent., the level to which it had been raised in June 1964.

Norway. With activity already at a high level, a strong new advance in demand, led by exports and investment, brought productive capacity under strain in 1966. Wages and consumer prices increased substantially, and the contribution of the external overall surplus to domestic liquidity contracted sharply.

According to the official recommendation at the outset of 1966, bank loan expansion was to be kept down to 6–6½ per cent. Early in the year, operating under the new Monetary and Credit Act, the authorities directed the commercial banks to maintain liquid reserves corresponding to 5 per cent. of their total assets. In June, after an acceleration of bank lending, this reserve requirement was raised to 8 per cent. However, special domestic factors and difficulties met in raising funds abroad kept credit demand high. By August outstanding credits at commercial banks were about N.kr. 1.1 milliard higher than a year earlier and were running about N.kr. 500 million above the recommended ceilings. Consequently, at the end of September those banks which in the preceding twelve months had increased their lending by more than 10 per cent. were instructed to hold an extra reserve corresponding to 50 per cent. of the excess amount. Under new official recommendations, the maximum permissible increase over a twelve-month period was fixed at 9 per cent. at the end of October and 8 per cent. at the end of November until March 1967, when the extra reserve requirements were discontinued. Construction loans for residential housing were not included. By the end of 1966 the commercial banks' domestic loans, other than those for house-building, were about 9 per cent. higher than a year before.

Early in 1967 resources continued to be under strain, with considerable increases expected in both private and public spending. The planned growth in public expenditure, at 9.7 per cent., was much above the increase in 1966 and the expected growth of the real national product. With the aim of further tightening credit, the authorities recommended that the increase in commercial-bank loans in 1967 be kept to no more than N.kr. 700 million (about 7 per cent.) and those of the savings banks to N.kr. 550 million (about 6½ per cent.). In the spring, moreover, additional measures were taken to curb consumption and investment, including a tightening of hire-purchase terms, a spacing-out of lending by the state banks and a selective curtailment of new building.

Sweden. In view of the continuing strong demand for credit, monetary policy was tightened further in early 1966. In the first five months of the year commercial-bank loans increased by S.kr. 2.2 milliard, against S.kr. 1.8 milliard in the same period of 1965. In order to meet this demand the commercial banks curtailed their holdings of government securities and borrowed more from the central bank. Thus in May their net indebtedness to the Riksbank reached S.kr. 800 million, compared with S.kr. 590 million a year earlier. On 10th June, so as to increase the flow of longer-term funds, the central bank raised its discount rate from 5½ to 6 per cent., the highest level for thirty-five years. Accordingly, the banks put up their deposit and lending rates, and the nominal interest rate moved up by ½ per cent. to 6¾ per cent. for housing bonds and 7 per cent. for industrial bonds.

Final demand eased perceptibly towards the middle of the year. Inventory accumulation, which in 1965 and early 1966 had largely caused the external deficit, returned to normal, and companies' fixed investment grew more slowly. Concurrently, the expansion of bank credit to the private sector slowed down and, partly in conjunction with an improvement in the external accounts, deposit formation and bank liquidity began to rise. Another factor of major importance was the emergence of a substantial central-government budget deficit, stemming largely from a loss of buoyancy in revenue combined with an increase in housing loans and in income transfers to the local authorities. By financing this deficit partly via the Riksbank, the authorities gave an additional fillip to monetary expansion and bank liquidity. For 1966 as a whole the banks' liquid assets rose by almost S.kr. 2.0 milliard, after declining by S.kr. 350 million in 1965. With effect from July, banks adhering strictly to the liquidity ratios laid down by the Riksbank were released from paying the penalty rate for borrowing over certain limits.

The net increase in lending for the credit system as a whole came in 1966 to S.kr. 12.6 milliard, compared with S.kr. 10.6 milliard in 1965 and S.kr. 9.4 milliard in 1964. At S.kr. 4.7 milliard, the funds raised by the private sector, excluding housing, were no greater than in 1965, although an appreciably larger proportion was raised on the capital market. On the other hand, the central government, which in 1965 had repaid S.kr. 250 million to the credit institutions and the general public, had a net financing requirement in 1966 of almost S.kr. 1.3 milliard. Of this total, S.kr. 880 million was financed at the Riksbank, while the commercial and other banks reduced their claims on the government by nearly S.kr. 200 million. The difference —

S.kr. 570 million — was taken up by capital-market institutions and the general public. The local authorities' net financing requirement remained about the same as in the previous year, partly because of greater revenue but partly also because building controls limited their investment activity. Lending to the housing sector expanded more rapidly in 1966, particularly since financing became easier in the second half of the year. Thanks mainly to the mortgage institutions, which, with higher interest rates, were able to attract more funds, total credit to this sector expanded by S.kr. 5.5 milliard in 1966, compared with a little under S.kr. 5.0 milliard in 1965.

Reflecting the budget deficit and its financing partly via the Riksbank, a somewhat bigger proportion of total credit was channelled through the banking system last year. However, capital-market activity also increased quite substantially; the number of mortgage issues, in particular, was greater after the rise in interest rates in June. As in previous years, the public credit institutions, mainly the National Pensions Fund, were chiefly responsible for the increased flow of long-term funds.

The signs of weakness that had appeared in some sectors in the course of 1966 continued in early 1967. The monetary authorities, though remaining cautious on both domestic and external grounds, lowered the discount rate to 5½ per cent. in February and to 5 per cent. in March.

Finland. Under the influence of a restrictive monetary policy the slow-down that began towards the end of 1965 continued last year, the decline in private capital formation being particularly marked. However, government expenditure continued to rise rapidly and, although some taxes and charges were raised in the middle of the year, the Treasury's cash difficulties reached major proportions, culminating in a F.mk. 300 million credit facility from the central bank in December. In the absence of any major fiscal measures, and with a continued rapid rise in incomes, private consumption also showed a considerable increase, contributing to a continuation of the trade deficit and the drain on official reserves.

Despite the slow-down in economic activity, credit demand remained strong in 1966, partly reflecting the pressure of costs and the squeeze on profits. Credit granted by all credit institutions increased by 11½ per cent. to F.mk. 12.1 milliard, while commercial-bank lending, which depended largely on central-bank credit, went up by 14 per cent. to F.mk. 4.9 milliard. To help curb this growth the Bank of Finland laid down quantitative restrictions on bank advances until the end of October, when such credits were to amount to no more than 115 per cent. of their end-1964 level. The central bank also set new rediscounting quotas from the beginning of May, which could be exceeded by a maximum of 25 per cent. but only at steeply progressive penalty rates. Because of the weakening foreign exchange position, still tighter directives were issued at the end of October, giving banks certain levels to which they had to reduce their rediscounts by January and June 1967. The weekly average of rediscounts amounted to F.mk. 725 million in 1966, i.e. F.mk. 150 million more than in 1965. Towards the end of the year, in connection with the loan to the Treasury, a special cash reserve agreement was concluded with the banks. Under this the banks make special deposits with the Bank of Finland depending on the growth of their deposits in 1967, the combined maximum being F.mk. 300 million.

Although the tight monetary policy helped reduce overall demand pressures in 1966, it was less effective against cost/price inflation. Consumer prices rose by nearly 5 per cent., wages went up about 9 per cent., and the balance of payments recorded a deficit of about F.mk. 500 million. Consequently, monetary policy was reinforced by various fiscal measures in the 1967 budget. Among other things, the purchase tax was raised from 10 to 11 per cent. from the beginning of the year and the personal income and property taxes and the company tax were increased. These measures are, on the one hand, designed to achieve equilibrium in the government finances and, on the other, to restrict the growth of consumption and import demand. The relaxation in the international capital market may also make it easier to raise funds abroad. In the meantime Finland has been granted a F.mk. 300 million IMF stand-by credit to support the country's official reserve position.

Spain. Economic activity rose sharply once again in 1966, led by an 18 per cent. expansion in industrial investment and a 21 per cent. advance in public-sector outlays. On the supply side, thanks to a better-than-average agricultural year and a big increase in industrial production, the real national product went up by over 8 per cent. However, price and wage pressures were strong, contributing to a further steep rise in imports.

Various new stabilisation measures were introduced in 1966. Early in the year credit ceilings were imposed for the first time, setting the permissible limit for bank credit expansion to the private sector at 17 per cent. of the end-1965 level. In March the interest rates on secured advances from the central bank were increased by 1 per cent. to a range of 5–6 per cent. In the second half of 1966 the proportion of deposits that the banks must invest in government securities was twice raised, each time by one percentage point, bringing it to 17 per cent. In October new legislation was passed restricting public expenditure in 1966 and provisionally limiting public investment in 1967 to the previous year's level. In addition, hire-purchase terms were tightened and measures taken to encourage savings and exports.

The credit institutions' lending to the private sector, including their holdings of securities, increased by Pesetas 112 milliard, corresponding to the ceiling of 17 per cent., whereas in 1965 the rise had been 24 per cent. The expansion of credit to the public sector, on the other hand, at Pesetas 47 milliard, came to 20 per cent., compared with 19 per cent. in 1965. The central administration, it may be observed, reduced its cash deficit from Pesetas 33.3 milliard in 1965 to Pesetas 30.6 milliard last year, but this improvement had its counterpart mainly in a curtailment of new issues. Moreover, the measures to contain public expenditure were taken too late in the year to affect materially the 1966 outcome. Under the influence of the external deficit, deposit formation with the credit institutions increased by only Pesetas 106 milliard, or

13.6 per cent., as against 19.3 per cent. in 1965. Again in 1966, therefore, the banks' lending activity necessitated borrowing from the central bank, which rose by nearly Pesetas 23 milliard.

The restraint programme had a dampening influence on demand in the course of the year and this, combined with rising labour costs and falling profitability, led to a slower growth of investment. There was also a deceleration in the price rise, and the increase in the cost of living, at 5.3 per cent., was considerably less than the 9.4 per cent. recorded in 1965. None the less, the external situation and wage/price trends still give cause for concern, necessitating a continuation of the restraint policy. In March 1967 the percentage of deposits which the banks must invest in government securities was increased to 18 per cent.

Japan. In overcoming the economy's first acute post-war recession, the authorities brought to bear a strong combination of fiscal and monetary measures. In its special action of July 1965, and again in its budget for the fiscal year 1966–67, the government adopted a broad reflationary budget programme, concentrating on public investment. The emerging deficit was financed through bond issues, which were placed mainly with the banks and other financial institutions. In the monetary sphere, the Bank of Japan lowered its discount rate in three stages in the first half of 1965 from 6.57 to 5.48 per cent., where it subsequently remained. In addition, with the widening of the government bond market, the central bank also used open-market operations to create greater monetary ease.

In the first half of 1966 production turned buoyantly upwards under the influence of rising public expenditure and a faster growth in exports. In these circumstances the private sector's demand for credit did not gather force until the second half of the year, by which time investment outlays had accelerated. Throughout most of the year, moreover, as credit abroad became relatively dearer, Japanese traders turned increasingly to domestic sources of funds, while granting more credit to their customers abroad. Towards the end of the year, as overseas rates declined and Japanese rates remained stable, this situation began to reverse itself. A final factor associated with higher credit demand was the slower growth of exports and continued rise in imports in late 1966 and early 1967.

In 1966 total deposits with the commercial, postal savings and co-operative banks went up by Yen 4,830 milliard, or almost 17 per cent., compared with 10 per cent. in 1965. At over Yen 4,650 milliard, the increase in lending to the private sector came to 15 per cent., as against 10 per cent. in 1965. Net lending to the public sector was Yen 910 milliard, compared with Yen 745 milliard in 1965. With monetary policy easy and domestic money-market rates low, the banks also improved their net foreign position by about Yen 150 milliard, through both an increase in foreign assets and a reduction in foreign liabilities. Altogether, the liquidity supplied by the Bank of Japan by means of advances and purchases of bills and securities amounted in 1966 to almost Yen 560 milliard, as against less than Yen 55 milliard in 1965. For the most part, however, this went to offset the liquidity drain associated with the growth of the currency circulation and an improvement in the Treasury's account with the central bank.

Employed for the first time as a flexible policy instrument, the budget for the fiscal year 1966–67 made an important contribution to the economic upswing. General-account expenditure rose by over 20 per cent. to reach Yen 4,477 milliard, while government bond flotations increased from Yen 197 milliard in the year 1965–66, when this practice started, to Yen 730 milliard in 1966–67. Of this amount 11 per cent. was taken up by individuals and 89 per cent. by the banking system and other financial institutions.

In early 1967, as demand pressures became stronger, the policy problem changed from counteracting recession to keeping the new expansion under control. To moderate the business recovery, which was better than expected, the government curtailed its planned general-account expenditure for the fiscal year 1967–68, which is now budgeted to rise by 15.9 per cent. The increase in the Treasury's investment and loan programmes is 17.8 per cent., the lowest for five years. Government bond issues are expected not to exceed Yen 800 milliard.

II. WORLD TRADE AND PAYMENTS.

The expansion of world trade, which had slowed down somewhat in 1965, accelerated slightly last year. World exports measured in current values rose by 9.5 per cent., against 8.5 per cent. in the previous year. This fairly even rate of progress conceals two divergent movements — a rapid acceleration of exports from Canada and western Europe to the United States, and a further deceleration of intra-European trade growth, reflecting chiefly the effect of the levelling-off of economic activity in Germany.

International trade.

Areas	Exports			Imports			Changes in volume of	
	1964	1965	1966	1964	1965	1966	exports 1966	imports 1966
	in milliards of US dollars						in percentages	
Developed areas								
Western Europe								
EEC	42.6	47.9	52.7	45.1	49.1	53.7	+ 8.0	+ 8.1
EFTA	24.5	26.6	28.5	30.7	32.2	33.9	+ 5.3	+ 6.0
Other countries	4.6	5.1	5.7	7.5	8.9	10.0	+ 9.1	+ 11.4
Total for western Europe	71.7	79.6	86.9	83.3	90.2	97.6	+ 7.2	+ 7.7
United States	26.6	27.5	30.5	20.3	23.2	27.7	+ 14.1[1]	+ 19.1[1]
Canada	8.1	8.5	10.0	7.6	8.7	10.0	+ 12.3	+ 12.5
Japan	6.7	8.5	9.8	7.9	8.2	9.5	+ 16.2	+ 17.9
Other areas[2]	5.5	5.5	5.8	6.6	7.5	7.3	+ 4.3	− 6.3
Total for developed areas	118.6	129.6	143.0	125.7	137.8	152.1	+ 8.1	+ 9.7
Developing areas								
Latin America	9.9	10.4	11.1[3]	8.6	8.8	9.3[3]	+ 6.0[3]	+ 5.3[3]
Other areas	24.1	25.6	27.0[3]	26.6	28.4	30.5[3]	+ 5.0[3]	+ 4.2[3]
Total for developing areas	34.0	36.0	38.1[3]	35.2	37.2	39.8[3]	+ 5.3[3]	+ 4.5[3]
Grand total[4]	152.6	165.6	181.1	160.9	175.0	191.9	+ 7.8	+ 8.8

[1] First half of 1965 to first half of 1966. [2] Australia, New Zealand and South Africa. [3] Preliminary.
[4] Represents roughly 90 per cent. of world trade, as the trade of centrally-planned economies is included only to the extent that it is reflected in the imports and exports of their partners in the West.

In the first quarter of 1966 world exports were 13 per cent. higher than in the comparable period of 1965, when they were affected by a prolonged strike in US ports. The rate of increase slackened in the second quarter and dropped to 7 per cent. in the fourth quarter.

As in 1965, the increase in the value of international trade was almost entirely due to an expansion in volume, unit values having risen by only 1 per cent. In developed countries the volume of imports expanded more than that of exports, viz. by nearly 10 as against 8 per cent. The reverse was the case in developing countries, where exports rose by 5.5 per cent. and imports by 4.5 per cent. On an average, the terms of trade of the developed countries remained unchanged last year and those of developing countries deteriorated marginally.

Export prices of primary commodities, which on a year-to-year comparison had fallen in 1965, increased by 1 per cent. last year. Those of commodities from developing countries, which had been worst affected the previous year, remained stable, while those of products from developed countries went up by 2 per cent., largely because of higher quotations for cereals and wool. Export prices of non-ferrous base metals rose by 15 per cent., owing entirely to the advance of copper prices. In the past three years prices of non-ferrous metals have gone up by 60 per cent., a trend which has benefited, inter alia, some developing countries, such as Chile, Malaysia and Zambia.

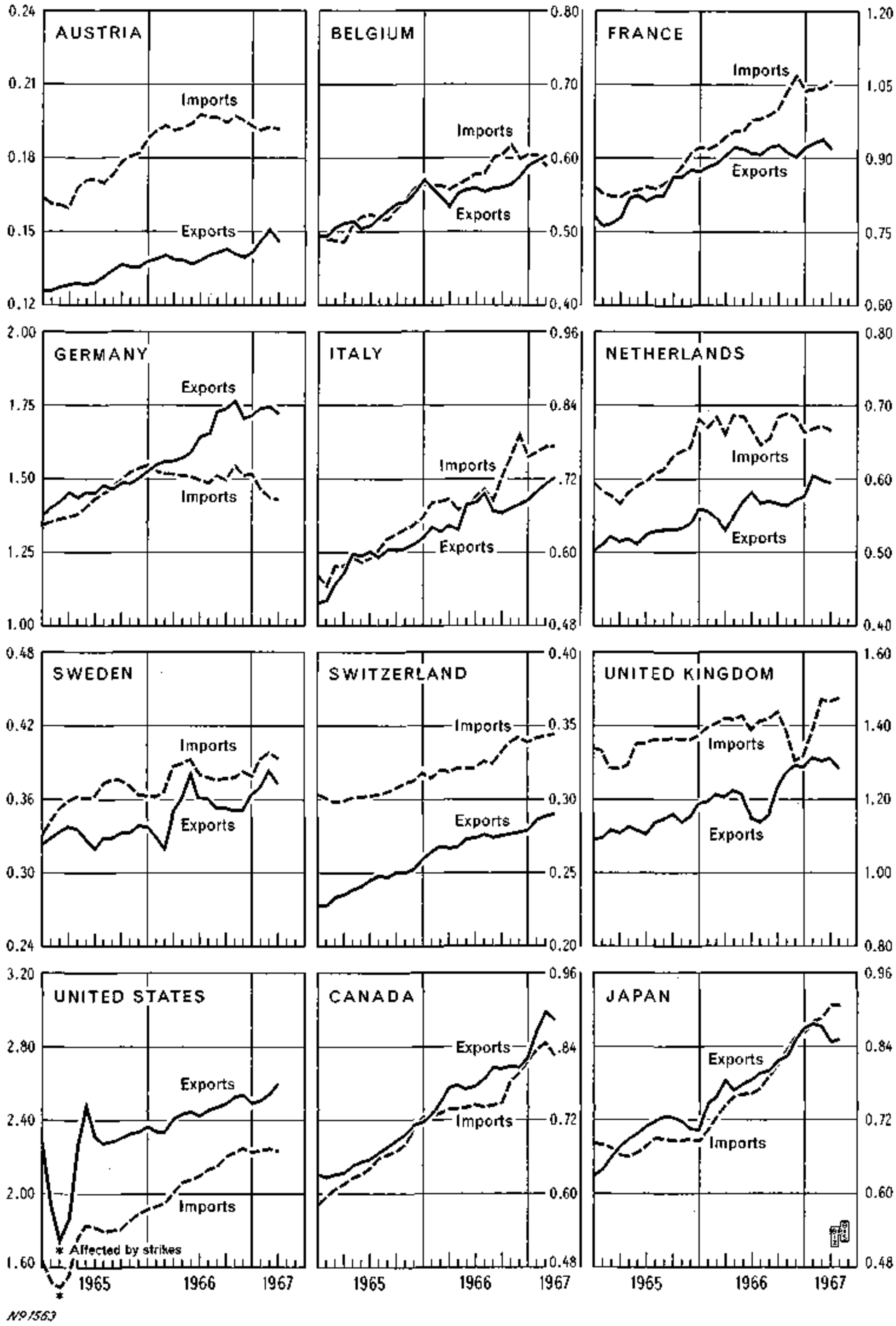
As regards the more recent trend of world commodity prices, a rise from mid-1965 to the first quarter of 1966 was followed by a substantial decline in the next two quarters, which affected almost all commodities except cocoa and wheat. Prices levelled out towards the end of the year and remained steady in the first quarter of 1967, when they were some 5 per cent. down on the corresponding quarter of 1966.

In terms of value, the rates of expansion of trade among developed countries were much higher last year in North America and Japan than in western Europe. US imports rose by nearly 20 per cent., partly as a result of the war in Vietnam, and since exports increased only half as much the trade surplus was reduced from $4.3 to 2.8 milliard. The counterpart of the growth in US imports was a substantial increase in western European, Canadian and Japanese exports, which went up by 25, 24 and 20 per cent. respectively in regard to the United States and by 9, 18 and 15.5 per cent. altogether. The EEC countries' imports and exports both increased by about 9 per cent., whereas in the EFTA group exports went up by 7 per cent. and imports by 5 per cent. (the latter figure mainly reflects the very moderate rise in UK imports). Exports of the group comprising Australia, New Zealand and South Africa expanded by 8 per cent., while imports actually declined by 3 per cent., chiefly owing to a substantial fall in South African imports. In the case of developing countries as a whole, imports seem to have expanded in line with exports.

Trade developments in the EEC countries reflected primarily changes in German trade. In 1965, when the German economy was buoyant, imports from its EEC partners shot up by 31 per cent., while exports to them rose by only 7 per cent., owing to shortage of productive capacity in Germany and also to low demand in France and Italy. The opposite situation prevailed in 1966, when, owing to a slackening of domestic demand, German imports from the other EEC countries rose by only 4 per cent., whereas exports to them expanded by 16 per cent., mainly in response to the recovery in Italy and France.

Foreign trade.

Uncentred moving averages of adjusted monthly figures, in milliards of US dollars.



The development of services.

One of the outstanding developments of the period since the end of the second world war has been the increasing economic interdependence of the various countries and areas of the world. This has found its expression not only in the field of trade but also in that of invisible transactions, i.e. services and unilateral transfers.

Between 1955 and 1965 the aggregate invisible receipts of western Europe, North America and Japan went up from $22.4 to 49.0 milliard, or by 119 per cent. Over the same period their aggregate invisible expenditures rose from $22.2 to 47.8 milliard, or by 116 per cent. As their exports and imports increased by 120 and 116 per cent. respectively, the share of invisibles in their current-account total declined a little.

Western Europe, North America and Japan: Balance of invisible transactions.

Areas	Years	Transportation[1]	Investment income	Tourism	Remittances[2]	Government transactions[3]	Other	Total
		in millions of US dollars						
Western Europe . . .	1955	+ 450	+ 620	+ 570	+ 210	+ 1,230	+ 805	+ 3,885
	1960	+ 850	+ 825	+ 1,275	+ 410	− 390	+ 870	+ 3,840
	1965	+ 1,300	+ 1,110	+ 1,925	+ 510	− 1,325	+ 550	+ 4,070
United States	1955	+ 200	+ 1,955	− 500	− 455	− 4,835	+ 395	− 3,240
	1960	− 165	+ 2,350	− 855	− 485	− 4,770	+ 850	− 3,075
	1965	− 275	+ 4,255	− 1,190	− 630	− 4,465	+ 1,680	− 625
Canada . . .	1955	− 15	− 330	− 120	− 70	+ 40	− 155	− 650
	1960	− 95	− 495	− 215	− 155	− 100	− 235	− 1,295
	1965	− 75	− 705	− 30	—[4]	—[5]	− 430	− 1,240
Japan	1955	− 160	− 40	+ 5	—[5]	+ 500	− 30	+ 275
	1960	− 285	− 35	—	—[5]	+ 325	− 130	− 125
	1965	− 550	− 190	− 20	—[5]	+ 215	− 425	− 970

[1] Including merchandise insurance. [2] Earnings of workers temporarily employed abroad and emigrants' remittances. [3] Services and transfers, both civilian and military. [4] Migrants' funds only; personal and institutional remittances included under "Other". [5] Not available separately; included under "Other".

Note: Discrepancies between figures in the above table and those in western Europe's consolidated balance and in the country tables are explained by differences in method. The above data are based for nearly all countries on their transactions balance and they exclude processing and merchanting, which are considered to belong to trade, whereas in the other tables the cash balance had to be used in some cases and processing and merchanting transactions were counted as invisibles. As regards the United States the difference is due to the inclusion of government grants in the above table and their exclusion from services on page 88.

The break-down of invisible transactions by area shows a net surplus for western Europe and net deficits for North America and Japan. In the period 1955–65 Europe's invisible surplus, to which all the main categories of invisible transactions except government expenditure contributed, was fairly stable at around $4 milliard a year. As regards North America, the United States' invisible deficit shrank from $3.2 to 0.6 milliard thanks to the dynamic growth of investment income, its only major invisible item to yield a surplus, whereas concurrently Canada's deficit rose from $0.7 to 1.2 milliard. Japan's invisible account has also deteriorated considerably in recent years, from a surplus of $0.3 milliard in 1955 to a deficit of just under $1 milliard ten years later.

Among the five major categories of invisible transactions, *transportation* is still the most important one for the countries concerned, having accounted in 1965 for one-quarter of their combined receipts and expenditure. Western Europe's net surplus on transport nearly trebled between 1955 and 1965, to $1.3 milliard. Amongst the traditionally sea-faring countries, Greece and the northern countries did best during this period. Their shipping tonnage more than doubled and their net transportation receipts went up from $0.6 to 1.4 milliard. In the case of the United Kingdom, the share of whose merchant fleet in the overall total declined from 20 to 14 per cent., the improvement — from a net deficit of $0.1 milliard in 1955 to a net surplus of the same size in 1965 — was much less marked. The Netherlands' surplus on transportation increased over these ten years from $145 to 350 million, the volume of goods loaded and unloaded at Dutch ports having doubled.

Western Europe, North America and Japan: Aggregate invisible transactions.

Items	Receipts			Expenditure			Balance		
	1955	1960	1965	1955	1960	1965	1955	1960	1965
	in millions of US dollars								
Transportation[1] . .	6,580	8,840	12,900	6,105	8,535	12,500	+ 475	+ 305	+ 400
Investment income	4,925	6,940	11,570	2,720	4,295	7,100	+2,205	+2,645	+4,470
Tourism	2,780	5,010	9,075	2,825	4,805	8,390	— 45	+ 205	+ 685
Remittances[2] . . .	515	1,075	2,095	830	1,305	2,215	— 315	— 230	— 120
Government[3] . . .	3,550	3,225	3,600	6,615	8,160	9,175	—3,065	—4,935	—5,575
Other	4,075	6,275	9,765	3,060	4,920	8,390	+1,015	+1,355	+1,375
Total	22,425	31,365	49,005	22,155	32,020	47,770	+ 270	— 655	+1,235
Foreign trade . . .	53,725	77,620	118,110	53,700	74,745	115,885	+ 25	+2,875	+2,225
Services and transfers as a percentage of trade . .	*42*	*40*	*41*	*41*	*43*	*41*	—	—	—

[1] Including merchandise insurance. [2] Earnings of workers temporarily employed abroad and emigrants' remittances. [3] Services and transfers, both civilian and military.

In the case of the United States, the share of whose merchant fleet in the world total has shrunk since the war from about 50 per cent. to only 12 per cent., the transportation account has steadily deteriorated. The post-war surpluses came to an end in 1957, and in 1965 a deficit of $275 million was recorded. Japan's transportation account has been consistently unfavourable despite a considerable increase in the size of the merchant fleet, with the net deficit increasing from $160 million in 1955 to $550 million ten years later.

Total net *investment income* of western Europe, North America and Japan rose from $2.2 to 4.5 milliard between 1955 and 1965, most of the increase occurring in the 1960s.

US net receipts went up from $2.0 to 4.3 milliard and those of western Europe from $0.6 to 1.1 milliard, reflecting chiefly the rise in UK net income from \$0.5 to 1.3 milliard. Other countries in Europe with a surplus of receipts over out-payments in 1965 were, in decreasing order, Switzerland, the Netherlands, France, Ireland, Sweden and the BLEU. Germany was the only large European deficit country, with net out-payments totalling nearly \$500 million in 1965. Outside Europe, Canada and Japan registered mounting net out-payments.

The United States' gross income from its investments abroad went up between 1955 and 1965 from \$2.4 to 5.9 milliard and its total assets from \$45 to 106 milliard, whilst foreigners' income from investments in the United States grew from \$0.5 to 1.6 milliard, their assets having risen from \$30 to 59 milliard. About half of all foreign assets in the United States are in the form of short-term claims, compared with some 10–15 per cent. in the case of US foreign assets abroad. Up to 1957 income from direct investment accounted for roughly 80 per cent. of total US investment income from abroad. This proportion has since declined to about two-thirds, owing chiefly to the expansion of foreign borrowing in the United States in the form of security issues.

Western Europe, North America and Japan: Investment income.

Countries	Receipts			Expenditure			Balance		
	1955	1960	1965	1955	1960	1965	1955	1960	1965
	in millions of US dollars								
Western Europe									
Austria	5	20	40	5	25	65	—	− 5	− 25
BLEU	130	180	245	90	130	240	+ 40	+ 50	+ 5
Denmark	10	25	40	20	20	50	− 10	+ 5	− 10
Finland	5	10	10	15	15	55	− 10	− 5	− 45
France	150	190	365	80	110	280	+ 70	+ 80	+ 85
Germany	50	200	330	195	395	795	− 145	− 195	− 465
Greece	—	10	10	5	5	20	− 5	+ 5	− 10
Iceland	—	—	—	—	5	5	—	− 5	− 5
Ireland	70	85	120	45	50	65	+ 25	+ 35	+ 55
Italy	25	85	200	45	115	285	− 20	− 30	− 85
Netherlands . . .	195	320	560	110	215	360	+ 85	+ 105	+ 200
Norway	10	20	40	25	60	110	− 15	− 40	− 70
Portugal	10	10	20	5	5	30	+ 5	+ 5	− 10
Spain	—	10	30	10	25	65	− 10	− 15	− 35
Sweden	30	45	85	15	20	40	+ 15	+ 25	+ 45
Switzerland . . .	170	215	320	50	55	60	+ 120	+ 160	+ 260
Turkey	—	—	—	10	30	45	− 10	− 30	− 45
United Kingdom .	1,445	1,905	2,770	960	1,225	1,505	+ 485	+ 680	+1,265
Total for western Europe . . .	2,305	3,330	5,185	1,685	2,505	4,075	+ 620	+ 825	+1,110
Canada	160	180	285	490	675	990	− 330	− 495	− 705
United States . . .	2,445	3,350	5,900	490	1,000	1,645	+1,955	+2,350	+4,255
Japan	15	80	200	55	115	390	− 40	− 35	− 190

Canada's investment-income deficit, which increased from \$330 to 700 million over the period, is largely vis-à-vis the United States, which accounts for about three-quarters of total foreign investment in the country.

The United Kingdom's foreign assets, which declined from \$14 to 8 milliard between 1938 and 1948, have since been reconstituted, despite controls on investment outside the sterling area. At the end of 1964 the United Kingdom had long-term foreign investments amounting to \$28.7 milliard, against long-term foreign liabilities of \$16.7 milliard. UK receipts from interest and dividends doubled between 1955 and 1965 to \$2.8 milliard. On the other hand, the corresponding out-payments went up from \$1.0 to 1.5 milliard. Net investment income is by far the biggest surplus item on invisible account and during the period under review it has been about equal to the net deficit on government services and transfers.

In Switzerland net investment income, which ranks second after tourism, increased steadily during the period under review from \$120 to 260 million. At the end of 1965 Switzerland's total foreign assets were estimated at \$18.5 milliard and its total liabilities at \$8.5 milliard. Its long-term assets and liabilities totalled \$10.7 and 4.5 milliard respectively, whilst the banks' foreign assets and liabilities stood at \$4.3 and 3.9 milliard respectively.

In the Netherlands receipts and payments in respect of investment income roughly trebled between 1955 and 1965. Receipts went up from \$195 to 560 million and payments from \$110 to 360 million. In most years there was a net capital outflow, security transactions being the most important item in the capital-account balance. Except in 1961, foreign purchases of Dutch securities exceeded purchases of foreign securities by Netherlands residents throughout the 1955–65 period.

Germany is the only country in western Europe with a large deficit in respect of investment income, despite the fact that in nearly all the years under review the net outflow of official capital exceeded the net inflow of private capital. Up to 1961 the former consisted for the most part of contractual repayments under the London Debt Agreement; later on, it represented loans and credits to developing countries, which amounted in the 1960s to about \$280 million a year. As yields on foreign investment in Germany were much higher than those on German official lending, net out-payments on this item increased from \$145 million in 1955 to \$465 million in 1965.

In recent years *tourism* has become one of western Europe's major export industries. Gross receipts from this service item rose during the period under review from \$1.8 milliard to about \$7 milliard. France, Italy and Spain accounted for more than half of this rise, with increased receipts of \$0.7, 1.1 and 1.0 milliard respectively. In addition, gross tourist receipts of Austria and Switzerland went up by about \$0.5 milliard each during this period. Gross European expenditure on foreign travel also rose sharply during the period under review, from \$1.2 to 4.9 milliard. Two-thirds of the increase was accounted for by France, Germany and the United Kingdom, with increases of \$0.8, 1.2 and 0.5 milliard respectively.

Western Europe's net surplus on tourist account therefore rose from $0.6 milliard to nearly $2 milliard between 1955 and 1965. Italy and Spain both had net surpluses of $1 milliard in 1965, and they were followed by Austria and Switzerland with $0.4 milliard each. Germany's tourist deficit in that year amounted to $660 million, and those of Sweden and the United Kingdom to $115 and 270 million respectively.

US expenditure on and receipts from foreign travel both approximately doubled between 1955 and 1965, to stand at $2.4 and 1.2 milliard respectively in the latter year. The net deficit thus increased from $0.5 to 1.2 milliard. The Canadian deficit, on the other hand, owing mainly to increased receipts from US visitors, narrowed from $120 to 30 million.

Remittances, covering earnings of workers temporarily employed abroad and emigrants' remittances, have grown with the increase of labour migration both within and to Europe. The peak number of foreign workers employed in European countries is estimated to have risen from 2.5 to 5.4 million between 1962 and 1965. The principal European employers of foreign labour in the latter year were Germany with 1.1 million, France with 1 million, Switzerland with 800,000 and the United Kingdom with 700,000 workers. The main supplying countries were Italy with 1.5 million, Spain with 675,000 and Ireland with 600,000 workers.

Western European countries' aggregate gross receipts from workers' remittances went up from $400 million in 1955 to $1,900 million in 1965 and their net receipts from $200 to 500 million. The aggregate gross receipts of Mediterranean European countries expanded during this period from $225 to 1,430 million, those of Italy alone increasing from $125 to 800 million. In 1965 the Mediterranean countries' net receipts from this source came to $1,350 million and were the next largest invisible-income item after tourism.

As Europe's economic recovery proceeded in the 1950s, its net receipts from *government transactions,* representing chiefly US aid, diminished. However, in 1955, owing to large-scale US payments to France to help finance the war in Indo-China, overall net receipts amounted to $1.2 milliard. Thereafter the balance on government transactions reflected chiefly the net UK deficit, which grew from less than $400 million in 1955 to about $1,250 million in 1965. Germany's government transactions showed only a small surplus in most years, large receipts from foreign military agencies having been nearly offset by German payments on reparations and indemnities. In 1965 receipts and expenditure were practically balanced, at nearly $1,100 million in each case.

Outside Europe, the net outflow of US Government funds remained very large at between $4 and 5 milliard a year, about half of which represented military expenditure, while in Japan the net inflow of official funds — mostly US military aid — declined from $500 million in 1955 to $200 million in 1965.

Balances of payments.

United States. US balance-of-payments developments in 1966 were dominated by two factors: the escalation of the war in Vietnam and the domestic investment boom. The former produced a $0.7 milliard rise in net overseas military expenditure, whilst the latter was mixed in its effects. On the one hand, increasing strains on domestic resources led to a $1.1 milliard decline in the trade surplus; on the other hand, the related tightening of domestic credit conditions contributed towards a $1.9 milliard reduction in the net outflow of private capital. The improvement in the capital account, which also owed something to the voluntary restraint programme, as well as to special conversions of certain foreign official dollar holdings from liquid to non-liquid form, practically offset the deterioration on current account, so that the deficit, measured on the liquidity basis, only edged up from $1.3 to 1.4 milliard. On the official-settlements basis, however, there was a shift from a deficit of $1.3 milliard to a surplus of $0.2 milliard, owing mainly to the $2.7 milliard increase in liquid liabilities to foreign commercial banks.

The narrowing of the trade surplus from $4.8 to 3.7 milliard was the result not of a slow-down in exports but of the exceptional strength of imports. After a 15 per cent. increase in 1965, they went up by a further 19 per cent. last year to a level more than 75 per cent. above their 1961 cyclical low. The pressure of domestic demand was most clearly reflected in the increase in imports of manufactured goods. Imports of consumer goods other than food and beverages, after a $0.7 milliard rise in 1965, went up by $1.3 milliard, or 30 per cent., in 1966. The predominant item here was motor-cars, imports of which — mainly from Canada and Germany — practically doubled, from $670 to 1,245 million. Imports of capital equipment, which had gone up by $450 million in 1965, rose further by $1 milliard, or 60 per cent. And purchases of industrial materials, which expanded at about the same pace as industrial production, showed a rise of $1.1 milliard.

The growth of commercial exports, despite increasing capacity strains, accelerated from 3 to 11 per cent. (on a Bureau of Census basis). Part of the higher growth rate may be explained by the 1965 dock strike. There was a recovery of agricultural exports following their decline in 1965, but the rate of growth of non-agricultural exports also quickened, from 5 to 10 per cent. Exports of machine tools, however, for which domestic demand was particularly strong, declined.

With regard to the geographical distribution of exports, the greatest increases were in those to Canada (+20 per cent.) and Japan (+14 per cent.); together, these two countries accounted for about half of the $2.7 milliard expansion of US exports. Sales to western European countries, on the other hand, went up by 8 per cent.

The recent slackening of the pace of US economic activity has already begun to show through in the trade accounts. The increase in imports began to slow down in the fourth quarter of last year and continued to in the first

United States: Balance of payments.

Items	1965	1966 Year	1966 1st quarter	1966 2nd quarter	1966 3rd quarter	1966 4th quarter	1967 1st quarter[1]
	in millions of dollars[2]						
Goods and services							
Exports (f.o.b.)							
Government-financed	2,765	2,945	715	805	665	760	.
Commercial	23,510	26,235	6,360	6,565	6,305	7,005	.
Total exports	26,275	29,180	7,155	7,100	7,425	7,500	7,730
Imports (f.o.b.)	21,485	25,505	5,980	6,220	6,640	6,665	6,700
Trade balance	+ 4,790	+ 3,675	+ 1,175	+ 880	+ 785	+ 835	+ 1,030
Investment income, including fees and royalties	+ 5,165	+ 5,360	+ 1,330	+ 1,395	+ 1,360	+ 1,275	.
Military expenditure less receipts	− 2,035	− 2,740	− 655	− 640	− 720	− 725	.
Pensions and remittances	− 995	− 990	− 235	− 235	− 275	− 245	.
Other services	− 960	− 1,000	− 270	− 250	− 220	− 260	.
Total services	+ 1,175[3]	+ 630	+ 170	+ 270	+ 145	+ 45	.
Balance on goods and services	+ 5,965	+ 4,305	+ 1,345	+ 1,150	+ 930	+ 880	.
Private capital movements							
US capital							
Long-term							
Direct investment	− 3,370	− 3,365	− 690	− 975	− 735	− 965	.
Portfolio	− 760	− 425	− 320	+ 5	− 70	− 40	− 260
Bank loans	− 230	+ 330	+ 120	− 30	+ 85	+ 155	+ 150
Other	− 90	− 115	− 15	− 55	− 30	− 15	.
Total long-term	− 4,450	− 3,575	− 905	− 1,055	− 750	− 865	.
Short-term							
Banks	+ 325	− 70	+ 140	− 90	+ 20	− 140	− 85
Non-banks	+ 435	− 265	− 165	+ 50	− 15	− 135	.
Total short-term	+ 760	− 335	− 25	− 40	+ 5	− 275	.
Total private US capital	− 3,690	− 3,910	− 930	− 1,095	− 745	− 1,140	.
Foreign non-liquid capital[4]							
Purchases of US corporate securities	− 445	+ 880	+ 175	+ 505	+ 110	+ 90	+ 75
Other	+ 440	+ 1,275	+ 160	+ 540	+ 75	+ 500	.
Total foreign non-liquid capital	− 5	+ 2,155	+ 335	+ 1,045	+ 185	+ 590	.
Balance on private capital account	− 3,695	− 1,755	− 595	− 50	− 560	− 550	.
Government grants and loans, net of repayments, and miscellaneous non-liquid capital transactions	− 3,175	− 3,385	− 1,005	− 1,025	− 740	− 615	.
Errors and omissions	− 430	− 590	− 290	− 195	+ 170	− 275	.
Balance of payments on a liquidity basis, seasonally adjusted	− 1,335	− 1,425	− 545	− 120	− 200	− 560	.
Balance of payments on a liquidity basis, revised but not seasonally adjusted[5]	− 1,335	− 1,365	− 50	− 145	− 700	− 470	− 230

[1] Preliminary. [2] Quarterly figures are seasonally adjusted, except export sub-totals. [3] See note to table on page 82. [4] Foreign private and official investments in US private non-liquid instruments. [5] As at mid-May revised figures were not available for all items.

quarter of 1967, when, owing also to a marked rise in exports, the trade surplus went up to over $1 milliard.

The other principal deterioration in the balance of payments was the increase from $2.0 to 2.7 milliard in net military expenditure. This was entirely due to the war in Vietnam. As far as the other main items of the current-account balance are concerned, net receipts from interest and dividends (including fees and royalties) continued to expand, although considerably less fast than in preceding years. Between 1960 and 1965 the yearly increase had averaged $480 million, while in 1966 it amounted to only $195 million. Income from direct investment, which had gone up by $290 million in 1965, showed hardly any increase. The balance on other service items (including private remittances) showed virtually no change, both receipts and expenditures rising by about $0.5 milliard. The current-account surplus therefore declined by $1.7 to 4.3 milliard.

The deficit on private capital account, which had already receded from its peak level of $6.3 milliard in 1964 to $3.7 milliard in 1965, narrowed further to $1.75 milliard. The pattern of development, however, was quite different in 1966 from the previous year. In 1965 the balance on short-term capital movements improved by $2.9 milliard, while the long-term capital outflow increased by $0.3 milliard; in 1966, in contrast, the short-term capital account deteriorated from a $0.9 milliard surplus to a $0.1 milliard deficit, while the long-term capital outflow was reduced from $4.6 to 1.7 milliard. Moreover, whereas in 1965, owing to the voluntary restraint programme, the smaller capital-account deficit had been the result of a decline in the net outflow of US capital, in 1966 it was almost wholly due to an increase in the net inflow of foreign capital.

Net exports of private US capital, which had declined from $6.5 to 3.7 milliard in 1965, edged up to $3.9 milliard. Direct investment, after increasing to $3.4 milliard in 1965, remained at this high level last year. Investment in continental western Europe and in Canada rose by $210 and 175 million respectively, but investment in Asian and African countries (excluding Japan and South Africa) was reduced by $300 to 250 million.

Net new foreign issues on the US capital market fell from $1.0 to 0.7 milliard last year, mostly owing to larger redemptions. In addition, US residents continued, under the influence of the interest equalisation tax, to draw down their foreign security portfolios, net sales amounting to $275 million — $50 million more than in 1965. In the banking sector, US longer-term claims fell by $330 million while short-term loans expanded by $70 million, so that total bank loans to foreigners were reduced by $260 million and at the end of the year stood $865 million below the ceiling set under the voluntary restraint programme. On the other hand, the foreign short-term claims of non-bank US residents, after a $435 million decline in 1965, went up by $265 million. Deposits in the Euro-dollar market of funds raised by US corporations in the European capital market seem to have been the main cause of this increase.

The net flow of foreign non-liquid capital to the United States expanded from zero in 1965 to about $2.2 milliard. Over half of this increase was accounted for by foreign holdings of US securities (other than those issued by the Treasury), which, following a decline of $445 million in 1965 when the UK Treasury was liquidating its dollar security portfolio, rose by $880 million. A major part of the increase in 1966 came from foreign purchases of securities issued by US corporations in the European capital markets. In addition, there were substantial foreign official purchases of US Government agency securities.

Foreign long-term claims on US banks, which had already gone up by $205 million in 1965, advanced by a further $930 million. Virtually the whole of this increase took the form of long-term time deposits and purchases of long-term certificates of deposit by Asian and Latin American countries and international institutions.

Despite an increase from $220 to 430 million in advance debt payments, net government grants and loans (including miscellaneous non-liquid capital transactions) rose a little from $3.2 to 3.4 milliard. Grants increased by just over $100 million and there was a rise of almost $250 million in official holdings of foreign currencies not included in the reserves.

Canada. Despite an increase in the level of domestic economic activity, Canada's export surplus, including non-monetary gold, increased in 1966 from $235 to 465 million. Furthermore, net capital inflows were $315 million higher than in 1965, so that the overall balance of payments shifted from a deficit of $260 million to a surplus of $145 million.

Exports, on a balance-of-payments basis, rose by $1,400 million, or 17 per cent. Sales to the United States, which account for three-fifths of the total, went up by 24 per cent. Half of this increase was accounted for by a rise from $340 to 900 million in deliveries of motor-cars, trucks and spare parts, which, under the 1965 US–Canadian automotive agreement, are duty-free in either direction. There was a small decline in exports to the United Kingdom, but sales to all other countries increased by $300 million, or 13 per cent. More than two-thirds of this was accounted for by larger shipments of wheat and flour, in particular to the USSR and India.

For the third year in succession Canadian imports rose by 14.5 per cent. Purchases of goods subject to the US–Canadian automotive agreement went up by 41 per cent. and other imports by 10.5 per cent. — about the same rise as in 1965.

Owing mainly to larger interest and dividend payments, the deficit on services account increased by $140 million. This item was also affected by an increase in Canadian Government aid, predominantly for the financing of the wheat shipments to India.

The net inflow of long-term capital, at $880 million, was the largest since 1959 and $220 million above the level of the previous year. Net direct investment in fact went up by $360 million. Foreign direct investment in

Canada: Balance of payments.

Items	1965	1966 Year	1966 1st quarter	1966 2nd quarter	1966 3rd quarter	1966 4th quarter
	in millions of US dollars[1]					
Merchandise trade (f.o.b.)						
Exports	8,215	9,615	2,340	2,335	2,450	2,490
Imports	7,980	9,150	2,205	2,240	2,310	2,395
Trade balance	+ 235	+ 465	+ 135	+ 95	+ 140	+ 95
Services						
Investment income	— 705	— 815	— 185	— 190	— 210	— 230
Other	— 530	— 560	— 140	— 120	— 165	— 135
Total	— 1,235	— 1,375	— 325	— 310	— 375	— 365
Current balance	— 1,000	— 910	— 190	— 215	— 235	— 270
Long-term capital						
Net new Canadian issues abroad	+ 765	+ 875	+ 435	+ 190	+ 185	+ 65
Transactions in outstanding Canadian securities	— 185	— 215	— 20	— 60	— 80	— 55
Transactions in foreign securities	— 80	— 330	— 65	— 85	— 105	— 75
Direct investment	+ 260	+ 620	+ 95	+ 140	+ 220	+ 165
Other	— 100	— 70	— 30	+ 15	— 40	— 15
Total	+ 660	+ 880	+ 415	+ 200	+ 180	+ 85
Balance on current and long-term capital account	— 340	— 30	+ 225	— 15	— 55	— 185
Short-term capital[2]	+ 80	+ 175	— 215	— 105	+ 250	+ 245
Total balance (= changes in monetary items)	— 260	+ 145	+ 10	— 120	+ 195	+ 60

[1] Quarterly data in the current balance are seasonally adjusted. [2] Including the balancing item.

Canada rose very sharply, from \$375 to 610 million, mostly coming from the United States. In addition, for the first time since 1950 there was on balance no direct Canadian investment abroad, owing to the sale by a Canadian petroleum company of its foreign subsidiary.

Net new issues of Canadian securities abroad also increased, from \$765 to 875 million. Half of the inflow from this item occurred in the first quarter of the year on account of the transfer, which had been deferred from the previous quarter, of the proceeds of large Canadian issues placed in the New York market in late 1965. On the other hand, net Canadian purchases of foreign, mostly US, securities rose from \$80 to 330 million, while net short-term inflows of capital, excluding Canadian bank funds, went up from \$80 to 175 million and thus also contributed to the turn-round in the balance of payments.

Western European countries. The combined current-account deficit of western European countries was reduced from \$1.3 milliard in 1965 to \$0.7 milliard last year. The surplus of the EEC countries increased from \$0.8 to 1.3 milliard, while the deficit of the EFTA countries was reduced from \$1.1 to 0.8 milliard.

Western European 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	
		in millions of US dollars					
Belgium-Luxemburg. . .	1965	− 90	+ 240	+ 150	+ 50	− 65	+ 135
	1966	− 350	+ 250	− 100	− 10		− 110
France	1965	+ 390	+ 130	+ 520	+ 110[4]	+ 330[5]	+ 960
	1966	− 45	+ 80	+ 35	+ 10[4]	+ 295[5]	+ 340
Germany	1965	+ 1,275	− 2,795	− 1,520	+ 205	+ 1,035	− 280
	1966	+ 2,915	− 2,810	+ 105	− 250[4]	+ 595	+ 450
Italy	1965	− 475[6]	+ 2,110	+ 1,635	− 45	− 15	+ 1,575
	1966	− 995[6]	+ 2,380	+ 1,385	− 805[4]	− 20	+ 560
Netherlands	1965	− 670	+ 650	− 20	− 45	+ 65	—
	1966	− 605	+ 515	− 90	+ 55	− 5	− 40
Total EEC	1965	+ 430	+ 335	+ 765	+ 275	+ 1,350	+ 2,390
	1966	+ 920	+ 415	+ 1,335	− 135		+ 1,200
Austria.	1965	− 525[6]	+ 490	− 35	− 55	+ 35	− 55
	1966	− 670[6]	+ 480	− 190	− 30	+ 155	− 65
Denmark	1965	− 285	+ 175	− 110	+ 130		+ 20
	1966	− 265	+ 205	− 60	+ 90		+ 30
Norway.	1965	− 780[6]	+ 670	− 110	+ 200	+ 70	+ 160
	1966	− 850[6]	+ 685	− 165	+ 135	+ 35	+ 5
Portugal	1965	− 295	+ 170	− 125	+ 65	+ 145[7]	+ 85
	1966	− 325	+ 300	− 25	+ 110	+ 30[7]	+ 115
Sweden	1965	− 405[6]	+ 105	− 300	+ 325		+ 25
	1966	− 300[6]	+ 65	− 235	+ 330		+ 95
Switzerland.	1965	− 710[6]	+ 640	− 70	+ 130		+ 60[8]
	1966	− 650[6]	+ 730	+ 80	− 95		− 15[8]
United Kingdom	1965	− 755	+ 450	− 305	− 670	+ 280	− 695
	1966	− 385	+ 215	− 170	− 360	+ 30	− 500
Total EFTA . . .	1965	− 3,755	+ 2,700	− 1,055	+ 655		− 400
	1966	− 3,445	+ 2,680	− 765	+ 430		− 335
Finland.	1965	− 225[6]	+ 35	− 190	+ 35	+ 70	− 85
	1966	− 230[6]	+ 25	− 205	+ 50	+ 10	− 145
Greece.	1965	− 700[6]	+ 435	− 265	+ 205	+ 30	− 30
	1966	− 725[6]	+ 490	− 235	+ 220	+ 40	+ 25
Iceland.	1965	+ 5	+ 0	+ 5	—		+ 5
	1966	− 10	+ 0	− 10	+ 10		+ 0
Ireland	1965	− 415[6]	+ 300	− 115	+ 65		− 50
	1966	− 365[6]	+ 320	− 45	+ 120		+ 75
Spain	1965	− 1,670	+ 1,280	− 390	+ 195	+ 90	− 105[8]
	1966	− 2,000	+ 1,420	− 580	+ 360	+ 15	− 205[8]
Turkey	1965	− 115[6]	+ 40	− 75	+ 100		+ 25[8]
	1966	− 235[6]	+ 65	− 170	+ 135		− 35[8]
Total "Other" . .	1965	− 3,120	+ 2,090	− 1,030	+ 790		− 240
	1966	− 3,565	+ 2,320	− 1,245	+ 960		− 285
Grand total. . . .	1965	− 6,445	+ 5,125[9]	− 1,320	+ 3,070		+ 1,750
	1966	− 6,090	+ 5,415	− 675	+ 1,255		+ 580

[1] Including unilateral transfers. [2] Calculated as the difference between the current balance and the overall balance. Long-term capital movements are shown separately where possible. Total figures or figures for short-term capital movements include errors and omissions. [3] Equal to changes in net official assets and the net foreign position of commercial banks. [4] Including official debt prepayments. [5] Including the balance of French overseas territories vis-à-vis the non-franc area. [6] Imports c.i.f. [7] Including the balance of Portuguese overseas territories vis-à-vis the non-escudo area. [8] Net official assets only. [9] See note to table on page 82.

The outstanding change in 1966 was a turn-round in the German balance from a deficit of \$1.5 milliard to a surplus of \$0.1 milliard, entirely owing to a rise in the export surplus. The current balances of other EEC countries deteriorated, as there was a decline in the French and Italian surpluses, a shift from surplus to deficit in the case of Belgium and a rise in the Netherlands' deficit. With the exception of Austria and Norway, the current-account balances of all EFTA countries improved.

The combined deficit of the six countries outside the EEC and EFTA groups increased by over \$200 million, chiefly owing to larger deficits in Spain and Turkey.

United Kingdom. Owing largely to the measures taken in July 1966, the balance-of-payments deficit on current and long-term capital account was again substantially reduced, from \$975 to 530 million. If account is taken of the effect of the resumption of service on the post-war North American loans, the real improvement in the basic position was of the order of \$625 million. Both the merchandise and long-term capital accounts contributed substantially to the improvement, the trade deficit declining by \$370 million and the net capital outflow by \$310 million. On the other hand, net receipts from services fell by \$235 million. As the surplus on the balancing item was also sharply reduced, the overall deficit declined only from \$695 to 500 million. Despite some deterioration of the trade balance, the overall balance probably continued in surplus in the first quarter of 1967.

Exports, on a trade-account basis, went up by 6.5 per cent., compared with 7 per cent. in 1965. Much of the 1966 rise was attributable to a 25 per cent. increase in sales to the United States, which followed almost as large a gain in the previous year. Exports to EFTA countries rose by 11 per cent. and those to EEC countries by 5.5 per cent., assisted by an impressive revival in sales to Italy and France. Exports to eastern Europe and the USSR continued their rapid growth, whereas those to the sterling area (excluding Rhodesia), which had risen by 7 per cent. in 1965, fell by 1.5 per cent.

Imports increased by 3.5 per cent., compared with only 1 per cent. in 1965; 1 per cent. of the rise represented higher prices and 2.5 per cent. a growth in volume. Despite the continuation of the import surcharge until almost the end of the year, imports in categories largely subject to it, i.e. all except food, fuels and basic materials, went up by 9.5 per cent. in 1966, whilst food imports remained at their 1965 level and those of basic materials fell by 4 per cent. Imports of capital goods were up by 13 per cent. (machinery imports by 17 per cent.), whereas those of consumer goods increased by 11 per cent. Imports of semi-manufactured goods rose by 8 per cent. — to a large extent reflecting the higher copper price, although in volume copper imports declined.

The trade balance improved considerably during the course of the year, from a deficit of \$505 million in the first half to a surplus of \$120 million in the second half. To some extent this reflected two special factors: the

United Kingdom: Balance of payments.[1]

Items	1964	1965	1966 Year	1966 1st quarter	1966 2nd quarter	1966 3rd quarter	1966 4th quarter
	in millions of US dollars						
Merchandise trade (f.o.b.)[2]							
Imports	14,040	14,150	14,695	3,750	3,665	3,810	3,470
Exports and re-exports	12,520	13,395	14,310	3,540	3,370	3,615	3,785
Trade balance	−1,520	− 755	− 385	− 210	− 295	− 195	+ 315
Services[2]	+ 420	+ 450	+ 215	+ 90	+ 5	+ 55	+ 65
Current balance[2]	—	—	—	− 120	− 290	− 140	+ 380
Current balance before adjustment	−1,100	− 305	− 170	− 95	− 205	− 310	+ 440
Long-term capital							
Official	− 325	− 235	− 220	− 70	+ 50	− 40	− 160
Private							
UK	−1,135	− 995	− 885	− 255	− 280	− 175	− 175
Foreign	+ 430	+ 560	+ 745	+ 120	+ 255	+ 135	+ 235
Total private	− 705	− 435	− 140	− 135	− 25	− 40	+ 60
Total long-term	−1,030	− 670	− 360	− 205	+ 25	− 80	− 100
Balance on current and long-term capital account	−2,130	− 975	− 530	− 300	− 180	− 390	+ 340
Errors and omissions	+ 75	+ 280	+ 30	+ 180	− 75	+ 100	− 175
Total balance (= changes in monetary items)	−2,055	− 695	− 500	− 120	− 255	− 290	+ 165

[1] On a transactions basis. [2] Quarterly data are seasonally adjusted.

seamen's strike, which shifted some exports from the second to the third quarter of the year (a similar effect on imports was less marked), and a temporary reduction of imports immediately preceding the removal of the surcharge at the end of November. In the main, however, the improvement was attributable to the disinflationary July measures. Moreover, although the backwash of the removal of the surcharge makes the early 1967 trade figures hard to interpret, exports in the first four months were 7 per cent. above the level of a year earlier, whilst imports, on average, were at the same level in the seven months October 1966–April 1967 as in January–September 1966.

The surplus on invisible transactions declined sharply in 1966, from $450 to 215 million. This was mainly the result of a number of special factors, such as the resumption of the full service on the North American post-war loans, a fall in oil companies' earnings connected with accelerated tax payments to producing countries, and the seamen's strike.

On long-term capital account the net outflow fell from $670 to 360 million, almost all of the decline being on private account. Net private investment abroad contracted by $110 million, largely as a result of portfolio disinvestment following the exchange control measures of April 1965, which require residents to surrender at the official exchange rate 25 per cent. of the proceeds of their sales of foreign securities. Direct investment was prevented from rising through various restrictive measures, including those announced in

May 1966 concerning outflows to the developed countries of the sterling area. There was also a fall in overseas investment by oil companies.

The net inflow of foreign private capital into the United Kingdom, on the other hand, rose by $185 million to a total of $745 million. Direct investment increased by nearly $100 million, reflecting several large transactions involving the acquisition of a majority interest in UK companies by US concerns. There was also an increase in investments by foreign oil companies, including outlays by companies prospecting for natural gas in the North Sea. Overseas holdings of UK securities again contracted, with net disinvestment, at $145 million, $10 million higher than in the previous year.

At $220 million, the net outflow of official capital was somewhat smaller than in 1965. Loans granted by the United Kingdom, at $265 million, were $55 million up, more than offsetting the decline in government economic grants to developing countries entered on current account. Some $145 million was drawn during the year from the Export-Import Bank to pay for US military aircraft and missiles, and these drawings brought the official capital account into net surplus in the second quarter; in the fourth quarter, on the other hand, payment of the first full instalments since 1963 on the North American loans contributed to a net outflow of $160 million.

The balancing item, representing partly time-lags between the recording of transactions in the balance of payments and the settling of accounts, which had been positive to the extent of $280 million in 1965 and had averaged $175 million in the period 1958–65, fell to $30 million last year. The decline was accounted for entirely by an exceptionally large negative figure in the fourth quarter, when the removal of the import surcharge meant that for a time arrivals of goods from abroad lagged behind payments for imports.

Germany. The main feature of Germany's balance of payments in 1966 was the continued improvement in the trade balance, which had begun in the last quarter of 1965 and which brought the trade surplus for the year up to just on $2 milliard, compared with a figure of $300 million in 1965. There was a partly offsetting movement of $450 million in the long-term capital account, nearly half of which was due to a debt prepayment to the United States of $195 million. The basic balance of payments therefore improved from a deficit of $1,315 million in 1965 to one of only $145 million in 1966, or to a surplus of $50 million if the debt prepayment is excluded. The trade surplus continued to expand in the first quarter of 1967, in which it amounted to $1,080 million, the highest quarterly figure ever attained. As other items of the balance of payments showed a net deficit of $160 million, there was an overall surplus of $920 million.

Most of the improvement in the trade balance resulted from the fact that imports rose by only $0.5 milliard, or 3 per cent., compared with an increase of nearly $3 milliard in 1965. In the first half of 1966 imports were 8 per cent. higher than in the corresponding period of 1965, while in the second half they fell slightly below the corresponding 1965 level. Three

Germany: Balance of payments.[1]

Items	1965	1966 Year	1966 1st quarter	1966 2nd quarter	1966 3rd quarter	1966 4th quarter	1967 1st quarter
	in millions of US dollars						
Merchandise trade							
Exports (f.o.b.)	17,910	20,155	4,740	4,905	4,970	5,540	5,190
Imports (c.i.f.)	17,610	18,165	4,530	4,560	4,405	4,670	4,110
Trade balance	+ 300	+ 1,990	+ 210	+ 345	+ 565	+ 870	+ 1,080
Services	— 355	— 410	— 75	— 120	— 190	— 25	— 40
Unilateral transfers	— 1,465	— 1,475	— 385	— 350	— 335	— 405	— 320
Current balance	— 1,520	+ 105	— 250	— 125	+ 40	+ 440	+ 720
Long-term capital							
Net German investment abroad	— 480	— 610	— 160	— 230	— 100	— 120	— 190
Net foreign investment in Germany	+ 1,005	+ 980	+ 295	+ 350	+ 190	+ 145	+ 115
Total private	+ 525	+ 370	+ 135	+ 120	+ 90	+ 25	— 75
Official	— 320	— 620[2]	— 85	— 150	— 85	— 300[2]	— 50
Total	+ 205	— 250	+ 50	— 30	+ 5	— 275	— 125
Balance on current and long-term capital account	— 1,315	— 145	— 200	— 155	+ 45	+ 165	+ 595
Short-term capital							
Private	+ 205	+ 425	+ 125	+ 100	+ 200	—	+ 155
Official	+ 350	— 35	— 40	+ 115	—	— 110	— 25
Total	+ 555	+ 390	+ 85	+ 215	+ 200	— 110	+ 130
Errors and omissions	+ 480	+ 205	+ 175	+ 100	+ 55	— 125	+ 195
Total balance (= changes in monetary items)	— 280	+ 450	+ 60	+ 160	+ 300	— 70	+ 920

[1] On a transactions basis. [2] Including a debt prepayment of $195 million to the United States.

main factors contributed to this development. First and foremost was the slackening of domestic demand, which mainly affected imports of manufactured goods for civilian use. These had expanded by 29 per cent. in 1965, and by 24 per cent. in the first quarter of 1966. Thereafter the rate of increase slowed down to 13 and 5 per cent. respectively in the second and third quarters of the year, whilst in the fourth quarter there was a decline of 2 per cent. compared with the corresponding period of 1965. Secondly, good domestic crops reduced the increase in food imports from 20 to 3.5 per cent.; and thirdly, imports of defence equipment fell by about one-third.

Exports rose during 1966 to $20.2 milliard, or by 12.5 per cent., compared with a 10.5 per cent. rise in the previous year. This was mainly in response to strong demand in France, Italy and the United States. Sales to these countries, which account for about one-quarter of total exports, went up by 18, 26 and 25 per cent. respectively. The expansion of exports quickened in the second half of the year, with a strong upward trend in sales of machinery and motor-cars.

As regards the area pattern of the trade balance, the net position vis-à-vis other EEC countries turned from a deficit of $360 million to a surplus of $380 million, whilst the deficit with regard to North America was reduced from $900 to 500 million and the surplus vis-à-vis all other countries rose from $1.6 to 2.1 milliard.

The deficit on services account (excluding freight and insurance on imports, which are included in the trade balance) rose from $355 to 410 million. Net expenditure on foreign travel showed a further increase of $160 million and expenditure on "miscellaneous services" went up by $185 million, over 25 per cent. of which represented higher spending for the promotion of exports. On the other hand, net receipts from foreign troops stationed in Germany were $200 million higher than in 1965.

On long-term capital account there were marked changes in 1966 both in the private and the official sector. In the private sector, net German investment abroad rose from $480 to 610 million, chiefly through an increase in portfolio investment. In particular, what has come to be known as the Texaco transaction, i.e. the conversion of $180 million's worth of shares in a German oil company into convertible bonds of a US subsidiary company, showed up in this item of the balance of payments as an increase in German portfolio investment abroad. This transaction did not, however, have any net effect on the overall long-term capital account, since the sale of the shares in the German oil company was recorded as direct foreign investment in Germany. Despite this, net new foreign investment in the Federal Republic was lower in 1966, so that the total inflow of private long-term capital was reduced from $525 to 370 million.

At the same time the net outflow of official long-term capital rose considerably in 1966, from $320 to 620 million. Most of this is accounted for by the $195 million debt prepayment to the US Government in December 1966. Taking the private and official sectors together, the long-term capital account showed an outflow of $250 million, or $55 million excluding the debt prepayment.

In the short-term capital account, official transactions recorded an outflow of $35 million, compared with an inflow of $350 million the year before. This change was mainly the result of the fact that in 1966 advance payments for defence equipment exceeded actual deliveries. In the private sector, on the other hand, increased short-term borrowing by German enterprises (which, however, ceased in the fourth quarter) raised the inflow from $205 to 425 million. Finally, the slackening of imports, coupled with the faster rise of exports, reduced the positive balancing item from $480 to 205 million. The overall balance of payments therefore showed a surplus of $450 million, compared with a deficit of $280 million the year before.

Italy. A rising trade deficit, together with a record outflow of capital, reduced the Italian external surplus from $1.6 milliard in 1965 to $0.6 milliard. The deficits on trade and capital account increased by $0.5 and 0.8 milliard respectively, but at the same time there was a further growth of $0.3 milliard in net service receipts.

Italy: Balance of payments.[1]

Items	1965	1966					1967
		Year	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter
	in millions of US dollars						
Merchandise trade							
Imports (c.i.f.)	7,130	8,600	1,965	2,080	2,240	2,315	2,280
Exports (f.o.b.)	6,655	7,600	1,840	1,815	1,975	1,970	1,960
Trade balance	− 475	− 1,000	− 125	− 265	− 265	− 345	− 320
Services							
Travel	+ 1,060	+ 1,200	+ 135	+ 285	+ 565	+ 215	+ 145
Remittances	+ 675	+ 730	+ 135	+ 185	+ 210	+ 200	+ 140
Transport	+ 360	+ 410	+ 95	+ 100	+ 120	+ 95	+ 95
Other	+ 15	+ 45	+ 5	—	+ 20	+ 20	− 50
Total	+ 2,110	+ 2,385	+ 370	+ 570	+ 915	+ 530	+ 330
Current balance	+ 1,635	+ 1,385	+ 245	+ 305	+ 650	+ 185	+ 10
Capital movements							
Repatriated bank-notes	− 315	− 560	− 175	− 105	− 105	− 175	− 255
Investment and loans by non-residents	+ 390	+ 260	+ 45	+ 15	+ 175	+ 25	
Investment and loans by residents	− 160	− 425	− 20	− 55	− 205	− 145	
Other (including official capital)	+ 25	− 100[2]	− 20	+ 25	− 105[2]	—	
Total	− 60	− 825	− 170	− 120	− 240	− 295	− 255
Total balance (= changes in monetary items)	+ 1,575	+ 560	+ 75	+ 185	+ 410	− 110	− 245

[1] On a cash basis. [2] Including a debt prepayment of $145 million to the United States.

The factors behind the deterioration of the trade balance were on the one hand the sharp recovery of economic activity in Italy and on the other hand less favourable conditions in certain export markets, notably Germany.

Imports, which had remained almost stationary in 1965, rose by 16 per cent. last year. In particular, purchases of semi-manufactured goods went up by 30 per cent., of which steel and copper accounted for half. Imports of finished goods, which had declined in 1965, went up by 17 per cent. and those of raw materials by 15 per cent. The expansion of food imports, on the other hand, slowed down from 20 to 10 per cent. because of increased domestic supplies.

The growth of exports dropped from 21 to 12 per cent. in 1966, the rate of expansion declining in the second half of the year. Sales to Germany rose by only 6 per cent., after 35 per cent. in 1965; and this accounted for three-quarters of the slower growth in total exports. There was also some slackening in the expansion of exports to countries outside Europe — with the exception of the United States, sales to which continued to grow at a rate of about 20 per cent.

The net surplus from services showed a further increase of $275 million, nearly as much as in 1965. Half of this was due to larger net receipts from tourism and a fifth each to net receipts from transportation and higher workers' remittances. The number of emigrants to EEC and other European countries, in particular Switzerland, was some 7 per cent. less than in the previous year. As, however, emigration to overseas countries rose steeply, the total number of persons going abroad increased by 3 per cent.

The other dominant factor in 1966 was the net capital outflow. It amounted to $825 million for the whole year — over 35 per cent. of which was in the fourth quarter — compared with only $60 million in 1965. Italian savings were attracted abroad by higher interest rates, which also caused Italian debtors to make anticipatory repayments of loans. Direct Italian investment abroad rose by $75 million, and net foreign loans taken up on the Italian market increased by $190 million. Foreign investment in Italy, on the other hand, declined by $130 million. The capital outflow in the form of bank-notes expanded by $245 million, reflecting uncertainties concerning the coupon tax, which were brought to an end by a decree of February 1967 subjecting all dividends payable to Italian residents to a 5 per cent. withholding tax. "Other" capital movements include the debt prepayment of $145 million to the United States in September 1966.

In the first quarter of 1967 the current account was in equilibrium, whereas the net capital outflow continued at a high level, exceeding $250 million.

France. The overall surplus on France's balance of payments, which had fluctuated between $600 and 1,200 million in the previous five years, dropped to $340 million in 1966, its lowest level since 1958. The trade surplus of $390 million in 1965 shifted to a deficit of $45 million and there was a decline of $205 million in net private foreign investment in France. The basic balance was still in surplus in the first half of the year, but moved into deficit in the second half.

Stimulated by the recovery of economic activity, imports from outside the franc area (as measured by customs statistics) went up from $8.8 to 10.3 milliard, or by 17 per cent., compared with only 4.5 per cent. in 1965. Semi-manufactured goods showed the fastest advance; consumer and equipment goods increased by 24 and 18 per cent. respectively. Purchases of raw materials — excluding fuel imports, which rose very moderately — went up by 13 per cent., largely owing to the need to replenish stocks.

Exports to countries outside the franc area rose to $9.4 milliard, or by 11 per cent., compared with approximately 14 per cent. in the two preceding years. The slower overall rate of expansion was largely due to a slackening in the growth rate of exports of semi-manufactured products. The trade deficit vis-à-vis the non-franc area thus grew by $580 million. The balance vis-à-vis EEC countries shifted from a surplus of $100 million to a deficit of $245 million, nearly two-thirds of the deterioration representing a fall in exports to Germany. The surplus in relation to EFTA countries was reduced from $420 to 280 million, chiefly because of a larger deficit vis-à-vis Sweden and a smaller surplus in trade with Switzerland. As for trade with the French

France: Balance of payments.[1]

Items	1965	1966 Year[2]	1966 1st quarter	1966 2nd quarter	1966 3rd quarter	1966 4th quarter
	in millions of US dollars					
Merchandise trade (f.o.b.)						
Exports	8,600	9,485	2,310	2,420	2,330	2,330
Imports	8,210	9,530	2,280	2,385	2,300	2,530
Trade balance	+ 390	— 45	+ 30	+ 35	+ 30	— 200
Services						
Transportation	+ 40	+ 55	— 10	+ 10	+ 40	+ 15
Travel	— 30	+ 30	+ 30	+ 80	— 120	+ 35
Workers' remittances	— 275	— 330	— 70	— 75	— 85	— 95
Other	+ 395	+ 325	+ 95	+ 75	+ 20	+ 105
Total	+ 130	+ 80	+ 45	+ 90	— 145	+ 60
Current balance	+ 520	+ 35	+ 75	+ 125	— 115	— 140
Long-term capital						
Official	— 250[3]	— 145[4]	— 15	—	— 105[4]	— 25
Private	+ 360	+ 155	+ 65	+ 80	— 50	+ 50
Total	+ 110	+ 10	+ 50	+ 80	— 155	+ 25
Balance on current and long-term capital account	+ 630	+ 45	+ 125	+ 205	— 270	— 115
Short-term capital and adjustments	+ 60	+ 45	— 15	+ 85	+ 105	— 20
Rest of French franc area	+ 270	+ 250	+ 95	+ 55	+ 50	+ 45
Total balance (= changes in monetary items)	+ 960	+ 340	+ 205	+ 345	— 115	— 90

[1] On a cash basis. [2] The sum of the quarters does not tally with the annual figure, as revisions are included in the yearly total but not in the quarterly figures. [3] Including a debt prepayment of $179 million to the US Export-Import Bank. [4] Including a debt prepayment of $71 million to the United States.

franc area, the 1965 surplus was converted into a deficit in 1966, mainly as a result of a sharp drop in exports to Algeria.

Net receipts from services and transfers showed a further contraction last year, declining from $130 to 80 million. Remittances abroad by foreign workers increased by $55 million and income from royalties and other services fell off. On the other hand, there was an improvement of $60 million on travel account.

Policy measures both in France and elsewhere (e.g. US Government pressure on enterprises to limit direct investment abroad) and the relatively low level of French interest rates combined to reduce the net inflow of private long-term capital from $360 to 155 million. Owing to the depressed state of the French stock exchange, foreign interest in French securities fell off, while at the same time French residents became net purchasers of foreign securities; thus, whereas in 1965 there had been a net inflow of $175 million in respect of security transactions, in 1966 this was reduced to $25 million. The net outflow of official long-term capital declined from $250 to 145 million, entirely owing to smaller prepayments of debt to the United States.

At \$250 million, net receipts from overseas countries of the franc area were slightly below their 1965 level; they declined substantially towards the end of the year.

Belgium-Luxemburg Economic Union. In 1966 the overall balance of the BLEU swung round from a surplus of \$135 million to a deficit of \$110 million owing to a rise in the import surplus from \$90 to 350 million.

The principal change in the trade accounts was the slowing-down of the expansion of exports from 14 per cent. in 1965 to 7 per cent. To a considerable extent this reflected the less favourable conditions prevailing in the German market, which takes about one-fifth of all Belgian exports. While sales of non-ferrous metals went up by 26 per cent., reflecting the rise in the price of copper, and those of textile products by 10 per cent., iron and steel exports declined by 4 per cent., and those of coal by one-third. Imports increased by 10.5 per cent., compared with 9 per cent. in 1965; those of equipment goods went up by some 10 per cent., twice as fast as those of consumer goods.

Last year the public sector reduced its net foreign indebtedness by \$50 million, compared with \$110 million the year before, but this reduction in the outflow was more than offset by the increase in purchases of foreign securities by BLEU residents.

Netherlands. On a cash basis, the Netherlands' deficit on current account, which had contracted in 1965, widened again last year as a result of a deterioration on services account.

The growth of imports on a customs statistics basis had fallen from 18 to 6 per cent. in 1965. Last year imports increased by 7 per cent., reflecting the pressure of demand which prevailed in the greater part of the year. As far as consumer goods are concerned, there was a rise of 17 per cent., nearly as much as in the previous year. Exports rose by 6 per cent., compared with 10 per cent. in 1965. There were certain exceptional factors that adversely affected the trade balance in the first quarter of 1966. An abnormal increase in imports for stock-building coincided with a decline in agricultural exports due to the ban by foreign countries on meat and cattle from the Netherlands in view of an outbreak of foot-and-mouth disease. This decline may have represented a loss of about \$50 million in export earnings. Exports to EEC countries went up by 5 per cent. over the year (those to France and Germany by 12 and 2 per cent. respectively) and those to EFTA countries by 1 per cent., owing to the stagnation of sales to the United Kingdom, while those to North and Latin America expanded by 19 and 25 per cent. respectively.

For the year as a whole the import surplus amounted to \$605 million, compared with \$670 million in 1965. This reduction in the trade deficit was more than offset by the fall in net receipts on services account from \$650 to 515 million. Income from investment was \$50 million less than in 1965, mainly because of lower dividends paid by foreign subsidiaries of Dutch

Netherlands: Balance of payments.*

Items	1965	1966 Year	1966 1st quarter	1966 2nd quarter	1966 3rd quarter	1966 4th quarter	1967 1st quarter
	in millions of US dollars						
Merchandise trade (f.o.b.)							
Imports	6,655	7,045	1,720	1,755	1,755	1,815	1,755
Exports	5,985	6,440	1,500	1,585	1,625	1,730	1,635
Trade balance	− 670	− 605	− 220	− 170	− 130	− 85	− 120
Services							
Investment income	+ 200	+ 150	+ 10	− 5	+ 80	+ 65	+ 45
Other	+ 450	+ 365	+ 75	+ 100	+ 95	+ 95	+ 50
Total	+ 650	+ 515	+ 85	+ 95	+ 175	+ 160	+ 95
Current balance	− 20	− 90	− 135	− 75	+ 45	+ 75	− 25
Capital movements							
Long-term							
Private							
Dutch	− 290	− 275	− 130	− 10	− 85	− 50	− 15
Foreign	+ 305	+ 355	+ 95	+ 55	+ 90	+ 115	
Banks	− 25	—	− 20	+ 15	—	+ 5	− 5
Official	− 35	− 25	− 5	− 10	− 5	− 5	− 5
Total long-term	− 45	+ 55	− 60	+ 50	—	+ 65	− 25
Short-term	+ 65	− 5	+ 30	+ 10	+ 5	− 50	− 10
Balance on capital account	+ 20	+ 50	− 30	+ 60	+ 5	+ 15	− 35
Total balance (= changes in monetary items)	—	− 40	− 165	− 15	+ 50	+ 90	− 60

* On a cash basis.

companies; expenditure by Dutch tourists abroad increased by $60 million; and unilateral transfers, which had yielded a net inflow of $30 million in 1965, when the last instalment was paid under the Netherlands–German Financial Treaty, resulted in a net outflow of $20 million.

In 1966 long-term capital movements shifted from a net outflow of $45 million to a net inflow of $55 million, nearly three-quarters of the change being due to securities transactions. In particular, net new loan issues abroad yielded $75 million, compared with only $5 million in 1965. No foreign issues were authorised on the Dutch market last year.

Austria. Because of a rise from $525 to 670 million in the trade deficit, the basic balance of payments deteriorated in 1966 from a deficit of $90 million to one of $220 million. This deterioration was largely offset, however, by a rise in short-term capital inflows (including errors and omissions) from $35 to 155 million, so that the overall deficit of $65 million was little greater than in 1965.

Imports rose by 11 per cent.; the biggest increase was in semi-manufactured and manufactured goods, impelled by the strong demand for machinery and motor-cars. After rising sharply in 1965, imports of foodstuffs remained practically stable last year. Exports went up by only 5 per cent., against 11 per cent. in 1965. Those of raw materials and foodstuffs actually declined, while exports of manufactured and semi-manufactured goods increased by 7.5 per cent., although the sub-group of machinery and vehicles showed a rise of only 4 per cent. While the slower rate of expansion was mainly the result of a weakening of demand in Germany, the growing discrimination on EEC markets and the fact that Austrian exporters cannot grant as favourable credit terms as many of their competitors also played a rôle.

The uninterrupted growth of net tourist receipts, which account for almost the entire surplus on services, practically came to a halt last year. At $425 million, they were barely $5 million higher than in 1965. Growing competition from other countries, rising Austrian travel expenditure abroad and bad weather contributed to this result. As net receipts from other services and unilateral transfers fell off somewhat, total net invisible receipts declined from $490 to 480 million.

The net outflow of long-term capital was reduced from $55 to 30 million last year, mainly as a result of increased borrowing by Austrian enterprises. Net long-term credits taken up abroad rose from $10 to 70 million. At the same time Austrian long-term credits granted expanded from $70 to 95 million, export credits accounting for $45 and 65 million respectively in the two years. The net inflow of short-term capital went up from $10 to 65 million and the positive errors and omissions item from $25 to 90 million.

Switzerland. The continued slowing-down in domestic economic expansion, together with interest rate developments abroad, resulted in the pattern of Switzerland's balance of payments being rather different in 1966 from what it had been in other recent years. The current account moved from deficit into surplus and the capital account from surplus into deficit. The overall balance, measured by the changes in net official assets, showed a small deficit of $15 million.

The trade deficit was reduced from $710 to 650 million. Imports, which had started to expand towards the end of 1965, increased by 7 per cent. in 1966, compared with 2.5 per cent. in the previous year. There was strong demand for investment and consumer goods, whereas the cooling-down in the building sector led to a decline in imports of iron and semi-finished iron products. Exports rose by 10.5 per cent., slightly less than in 1965, and in the course of 1966 their growth slackened because of cyclical developments in some other European countries. Exports to overseas countries, above all the United States, Brazil and Japan, expanded by as much as 15 per cent., while those to EFTA and EEC countries rose by 9 and 5.5 per cent. respectively.

Net receipts from invisible items are estimated to have increased from $640 to 730 million, reflecting a rise in investment income and tourist receipts and a decrease in workers' remittances due to the reduction in foreign labour. The current-account balance, therefore, shifted from a deficit of $70 million to a surplus of $80 million — the first since 1960.

Owing mainly to rising interest rates abroad, the total capital account, including errors and omissions, showed an outflow of $95 million in 1966, the first for some years. The outflow from identified transactions rose from $85 to 185 million. Net new foreign issues in Switzerland went up from $50 to 75 million and authorised bank credits to foreigners from $35 to 110 million. At the same time the inflow from unidentified capital transactions, including the change in the banks' net foreign position as well as errors and omissions, came down from $215 to 90 million.

Denmark. The improvement both in the trade and invisible accounts reduced the current deficit from $110 to 60 million. At the same time the net inflow of capital declined from $130 to 90 million and the overall balance again showed a small surplus.

Both imports and exports rose by about 6 per cent., reducing the trade deficit from $285 to 265 million. There was, however, some increase in the deficit between the first and second halves of the year, as imports began to go up faster with the pick-up in domestic economic activity while the rate of growth of exports slackened. The rise in exports during 1966 included a 5 per cent. increase in export prices, mainly of agricultural products. Exports of manufactured products, excluding ships, rose by 8.5 per cent., after increases of 17.5 per cent. in 1964 and 12.5 per cent. in 1965. The slackening of their growth reflects a certain loss of competitiveness due to rapidly rising costs, as well as weakening demand last year in Germany, Sweden and the United Kingdom.

Since 1960 Denmark has been a large importer of capital, on both official and private account. Last year the net inflow was reduced from $130 to 90 million, since repayments exceeded new borrowing in the public sector and net receipts from commercial credits declined. Borrowing by private enterprises, which was not permitted in 1965, was resumed last year on a limited scale.

Finland. The growth rate of the Finnish economy accelerated in the second half of 1966 and, at the same time, imports were stepped up. Over the year as a whole, however, imports rose by only 5 per cent., against 9 per cent. in the previous year. There was a similar drop in the growth rate of exports, viz. from 10.5 to 5.5 per cent., so that the import surplus, at $230 million, was about the same as in 1965. The trade deficit vis-à-vis western countries was reduced by $45 million, but that vis-à-vis bilateral-agreement countries expanded by a like amount. The terms of trade deteriorated by 3 per cent., as import prices increased over the year while those of exports, taken as a whole, remained stable. Although the deficit in respect of tourism narrowed in 1966, the surplus on invisible items contracted somewhat, owing chiefly to heavier interest payments on the growing external debt.

In 1966 the net capital inflow was reduced from $105 to 60 million. The net inflow of long-term capital was kept down by long-term debt repayments, whereas the net inflow of short-term capital fell off. Towards the end of the year and early in 1967 several specific measures were taken to reduce the balance-of-payments deficit.

Norway. Continued economic expansion in Norway led to a 9 per cent. increase in imports in 1966. Exports rose by 8 per cent. — mainly metals and engineering products — and the deficit on merchandise and ships account went up from $780 to 850 million. The net surplus on invisible items expanded by $15 million, leaving the current-account deficit, at $165 million, considerably higher than in 1965. Nearly the whole of this deficit occurred in the last quarter of the year, when imports of both merchandise and ships showed a sharp increase while receipts from invisibles shrank.

Throughout the post-war period the authorities have encouraged capital imports. In 1966, however, owing to the high interest rates on the international capital market, no Norwegian Government loans were issued abroad. Net borrowing abroad by public authorities, which had amounted to $40 million in 1965, was replaced by net repayments of $10 million. Shipping companies also reduced their borrowing abroad. On the other hand, direct foreign investment in Norway increased somewhat. On balance the net long-term capital inflow declined from $200 to 135 million, so that the basic balance showed a deficit of $30 million — the first for a number of years. This was just covered by a $35 million inflow of short-term capital.

Sweden. The balance on current account, which had been in approximate equilibrium in the early 1960s, showed deficits of $300 and 235 million respectively in the last two years. The improvement in 1966 was due to a $105 million reduction in the import surplus. As economic activity in Sweden levelled off in the course of the year, the growth in the volume of imports, which had amounted to 12 per cent. in 1965, slowed down to 4.5 per cent. in the first half of 1966 and ceased almost entirely in the second half. However, since import prices were higher than in 1965, the value of imports for the year as a whole was up by 4.5 per cent. Exports increased at about the same rate as in 1965, viz. by 6 per cent. in volume and 7.5 per cent. in value. Sales of machinery went up by 20 per cent., while those of iron ore, timber and transport equipment declined.

Net receipts from services continued to shrink, as the increase in shipping earnings fell short of the rise in expenditure on other invisible items, including tourism. As usual, the net identified capital inflow was not sufficient to offset the current deficit, but the positive balancing item closed the gap. At $210 million, it was almost as large as in the previous year, while the identified capital inflow increased from $95 to 110 million, despite the fact that its major net component, private long-term loans, was reduced by $40 million.

Spain. Excess demand in the first half of 1966 caused imports to rise very steeply. As investment slackened and plentiful crops came onto the market, the import rise slowed down considerably in the second half-year and the trade deficit contracted from $1,035 to 965 million. Owing to the seasonal large surplus from tourism and to a substantial capital inflow, the balance on current and long-term capital account, which had shown a deficit of $285 million in the first half, moved into surplus in the latter part of the year.

Imports, as measured by customs statistics, which had shot up by 34 per cent. in 1965, continued to expand at the same rate in the first half of 1966 but the increase slowed down to 6 per cent. in the second half. While imports of foodstuffs and semi-manufactured products, which had risen by 36 and 28 per cent. respectively in the first half-year, actually declined by 9 and 5 per cent. in the second, in the case of investment goods the increase merely slowed down, from 36 to 8 per cent. On the other hand, imports of consumer goods went up by another 26 per cent. in the second half of 1966, compared with 44 per cent. in the first half, and those of raw materials rose by 20 per cent., compared with 50 per cent. in the first half.

Exports, which had stagnated in 1965 because of a decline in sales of agricultural products, not only recorded a 30 per cent. gain last year but showed a more favourable composition, as it was the more sophisticated products which registered the highest rates of increase. Thus, over the year as a whole exports of investment goods more than doubled, those of consumer goods went up by a third and those of foodstuffs by a fifth.

Receipts from unilateral transfers, chiefly workers' remittances, went up from $300 to 480 million in 1966 but those from tourism, which had increased by leaps and bounds since 1959, rose by only 8 per cent. The number of tourists went up by a fifth to 17.3 million, but the average receipts per visitor declined from $81 to 72.

Spain: Balance of payments.[1]

Items	1965 Year	1965 1st half	1965 2nd half	1966 Year	1966 1st half	1966 2nd half
	in millions of US dollars					
Merchandise trade (f.o.b.)						
Imports	2,715	1,235	1,480	3,260	1,725	1,535
Exports	1,045	560	485	1,260	690	570
Trade balance	−1,670	− 675	− 995	−2,000	−1,035	− 965
Services	+ 980	+ 325	+ 655	+ 940	+ 375	+ 565
Unilateral transfers[2]	+ 300	+ 155	+ 145	+ 480	+ 220	+ 260
Current balance	− 390	− 195	− 195	− 580	− 440	− 140
Long-term capital	+ 195	+ 90	+ 105	+ 360	+ 155	+ 205
Balance on current and long-term capital account	− 195	− 105	− 90	− 220	− 285	+ 65
Short-term capital	+ 90	+ 45	+ 45	+ 15	+ 70	− 55
Overall balance (= changes in official reserves)	− 105	− 60	− 45	− 205	− 215	+ 10

[1] On a cash basis. [2] Chiefly workers' remittances.

Although the net long and short-term capital inflow increased from \$285 to 375 million, it was not sufficient to offset the large current deficit, and for the second year in succession the official reserves fell.

Japan. Despite the sharp recovery of domestic economic activity, the large trade surplus which had emerged as a result of the 1965 recession increased in 1966. Imports, after remaining fairly stagnant in 1965, advanced by 14.5 per cent., while exports went up by 15.5 per cent. Their continued buoyancy was partly a reflection of the war in Vietnam and boom conditions in the United States. Thus, on a customs statistics basis, exports to a group of countries in the Far East went up by 46 per cent. and those to the United States by 20 per cent.

The deficit on invisible items increased from \$970 million in 1965 to \$1,030 million in 1966 but even so the current-account surplus widened from \$930 to 1,250 million. In the first quarter of 1967, however, the current balance turned to a deficit of \$170 million, as owing to a very strong growth of imports the trade surplus was reduced to \$150 million.

The combination of domestic credit ease and mounting capital-market tensions abroad resulted in a further sharp rise in long-term capital exports, which doubled to \$820 million. These represented mainly yen credits to India and other Asian countries, private debt repayments and commercial credits connected with the rise in exports of the chemical and iron and steel industries.

Japan: Balance of payments.[1]

Items	1965			1966		
	Year	1st half	2nd half	Year	1st half	2nd half
	in millions of US dollars					
Merchandise trade (f.o.b.)						
Exports	8,330	3,875	4,455	9,640	4,380	5,260
Imports	6,430	3,290	3,140	7,360	3,560	3,800
Trade balance	+ 1,900	+ 585	+ 1,315	+ 2,280	+ 820	+ 1,460
Services						
Transportation	− 525	− 230	− 295	− 610	− 320	− 290
Investment income	− 190	− 100	− 90	− 185	− 95	− 90
Government[2]	+ 310	+ 125	+ 185	+ 440	+ 195	+ 245
Other	− 565	− 275	− 290	− 675	− 325	− 350
Total	− 970	− 480	− 490	− 1,030	− 545	− 485
Current balance	+ 930	+ 105	+ 825	+ 1,250	+ 275	+ 975
Long-term capital account	− 415	− 125	− 290	− 820	− 285	− 535
Balance on current and long-term capital account	+ 515	− 20	+ 535	+ 430	− 10	+ 440
Short-term capital account	− 60	+ 30	− 90	− 55	—	− 55
Errors and omissions	− 45	+ 20	− 65	− 55	+ 45	− 100
Total balance (= changes in monetary items)	+ 410	+ 30	+ 380	+ 320	+ 35	+ 285

[1] On a transactions basis. [2] Mainly military transactions.

Commercial policy.

Today, ten years after its inception, the European Economic Community is about half-way towards the goals laid down in the Rome Treaty. Realisation of the common market is in sight but the integration of the six national economies into a single economy is still a long way off. The merger of the executive bodies of the EEC, the ECSC and Euratom, which was agreed upon by the member countries under a treaty dated 8th April 1965, is to take place on 1st July 1967.

On 26th July 1966 the Council of Ministers decided that a 5 per cent. reduction in the Community's internal tariffs for industrial goods would be made on 1st July 1967 and that the remaining 15 per cent. would be abolished a year later, at which date the common external tariff would also come into force. With regard to agricultural policy, the Council decided on 26th July to set up marketing organisations for fruit and vegetables, sugar and fats, and fixed the prices for milk, beef, sugar, rice, oilseeds and olive oil. In fact, olive oil was the first agricultural product to reach the stage of a common market, on 10th November 1966, without a transitional period. Important steps towards the unification of economic policies were taken in February 1967. On 8th February the Council accepted the medium-term economic policy programme for the period 1966–70 and on the following day it approved the guide-lines for the harmonisation of turnover taxes, which involves the introduction of an added-value tax to come into operation on 1st January 1970 at the latest.

Negotiations with Austria for a possible link with the EEC continued throughout 1966 and the first half of 1967, but have not yet been completed. On 11th May 1967 the UK Government, with strong parliamentary support, made a formal application for membership of the three Communities. Almost simultaneously, Ireland and Denmark submitted their applications, while other EFTA countries expressed their readiness to negotiate.

On 1st January 1967 — three years ahead of schedule — the EFTA countries abolished the remaining 20 per cent. customs duties on industrial products. Finland lowered its duties to 10 per cent. and the remainder will be eliminated by the end of 1967. Some exceptions — of limited duration — have been granted to Austria, Finland, Norway and Switzerland, while every country except Denmark, which has no such duties, is maintaining revenue duties on certain goods. In the near future emphasis will be placed on the removal of barriers other than tariffs and on the enforcement of rules of fair competition.

After four years of arduous negotiations the Kennedy Round was completed on 15th May 1967. Some fifty countries, representing about 80 per cent. of world trade, took part in the negotiations. The most difficult problems to be solved affected the EEC, the United Kingdom and the United States. Much detailed work remains to be done before the full implications of the agreement are clear. Although the main target of a 50 per cent. linear reduction in the tariffs for industrial products has not been entirely achieved, tariff cuts of between 30 and 40 per cent. were made. It is estimated that these reductions apply to some \$40 milliard's worth of goods, or roughly a third of world trade in manufactured products. As regards agricultural products, the minimum price for wheat was fixed at \$1.725 per bushel and it was agreed to grant 4.5 million metric tons of cereals annually as aid to developing countries. Certain developed countries reduced their tariffs on tropical products, in some cases with immediate effect. Although the tariff reductions would normally be implemented over a five-year period, it was decided to examine, before signature of the agreement on 30th June 1967, the possibility of making cuts in advance for the benefit of developing countries.

III. GOLD, RESERVES AND FOREIGN EXCHANGE.

Gold production, markets and reserves.

In 1966 world gold production (excluding the USSR, other eastern European countries, mainland China and North Korea) is estimated to have amounted to 41.1 million ounces, the same as in the preceding year. As usual, the combined output of all producing countries other than South Africa continued to decline. Canadian output in particular, which is the next largest after that of South Africa, registered a marked drop of over 300,000 ounces, or nearly 9 per cent. On the other hand, production expanded a little in the United States, Australia, Japan and the Philippines. The outstanding feature of the year, however, was the slow-down in the rate of growth of South African output, from 1.4 to only 0.3 million ounces. During the preceding twelve years South African output had grown from 11.9 to 30.5 million ounces, outpacing by far the gradual downward trend of production elsewhere and enabling total production to rise, in round figures, from 24 to 41 million ounces. This phase of expansion in the gold-mining industry would appear now to have ended.

World gold production.

Countries	1929	1940	1946	1953	1963	1964	1965	1966
	weight, in thousands of fine ounces							
South Africa	10,412	14,046	11,927	11,941	27,432	29,137	30,540	30,869
Canada	1,929	5,333	2,849	4,056	4,003	3,799	3,587	3,274
United States	2,059	4,870	1,575	1,958	1,454	1,456	1,705	1,790
Australia	427	1,644	824	1,075	1,024	964	878	905
Ghana	208	886	586	731	921	865	755	684
Japan	335	867	40	258	433	460	519	555
Philippines	163	1,121	1	481	376	426	436	445
Colombia	137	632	437	437	325	365	319	280
Mexico	655	883	420	483	238	210	216	212
Total listed	16,324	30,282	18,659	21,420	36,206	37,682	38,955	39,014
Other countries[1]	2,276	6,718	3,041	2,680	2,494	2,418	2,145	2,086
Estimated world total[1]	18,600	37,000	21,700	24,100	38,700	40,100	41,100	41,100
	in millions of US dollars							
Value of estimated world total at $35 per fine ounce	650[2]	1,295	760	845	1,355	1,405	1,440	1,440

[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, $385 million.

The huge expansion of South African gold output was due to the development of new mines. Production in these new gold-fields between 1953 and 1966 went up from 2.5 to 25.1 million ounces, whereas the production of the older mining areas declined from 9.4 to 5.8 million ounces. The opening-up of the new gold-fields reached its climax in 1961–62; since then the growth of South African gold production has tended to slow down and in the course of 1966 seems to have come to a halt. Although strikes around the year-end may have contributed somewhat to the poor out-turn for 1966, the basic factors behind this trend in South African gold production are the lack of new gold discoveries and the effect on profits of rising wages and material costs. In the older mines that belong to the Transvaal and Orange Free State Chamber of Mines, where output declined by 0.5 to 5.3 million ounces in 1966, the cost per ton of ore milled has gone up by 22 per cent. since 1958 and, notwithstanding a shift to higher-yielding ores, average profits per ounce have been reduced by 44 per cent.

Valued at the official parity of $35 an ounce, total 1966 gold output was worth $1,440 million. And, as there were no offerings of gold by the USSR, this was also the total of fresh gold supplies that became available during the year. Total demand for gold other than from western official sources, although considerably below the 1965 peak of $1,750 million, did not shrink as much as supplies did, with the result that total official western gold stocks had to be drawn on during the year to the extent of $95 million in order to maintain the balance between demand and supply.

Estimated sources and uses of gold.

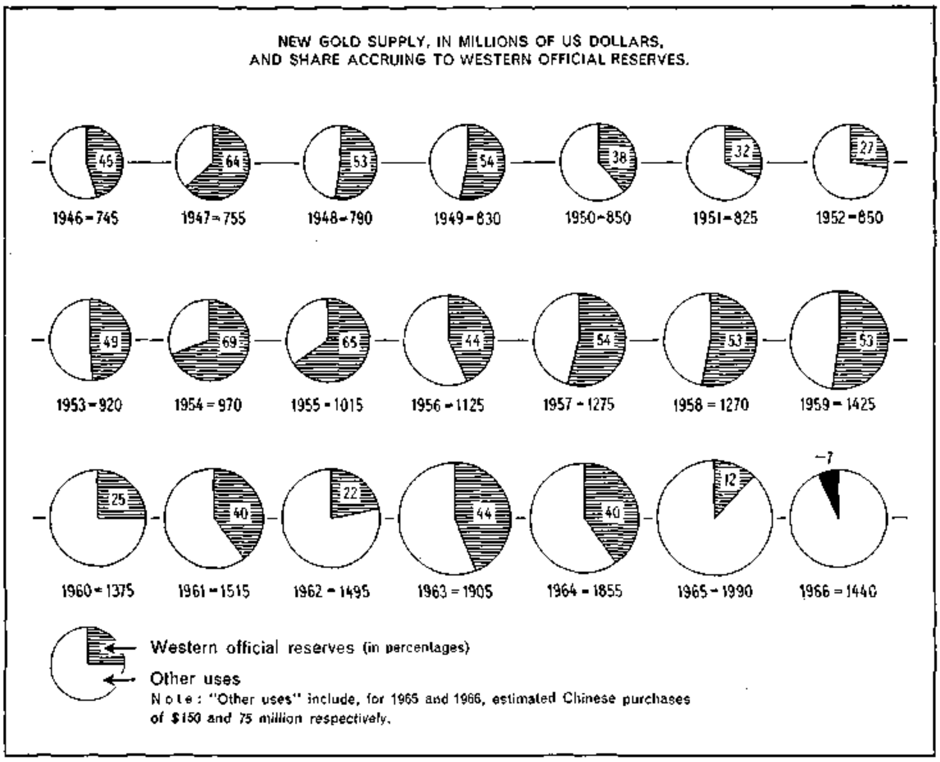
	1962	1963	1964	1965	1966
	in millions of US dollars				
Gold production[1]	1,295	1,355	1,405	1,440	1,440
Sales by the USSR	200	550	450	550	—
Total	1,495	1,905	1,855	1,990	1,440
Change in western official gold stocks	330	840	750	240	− 95
Other uses[2]	1,165	1,065	1,105	1,750	1,535

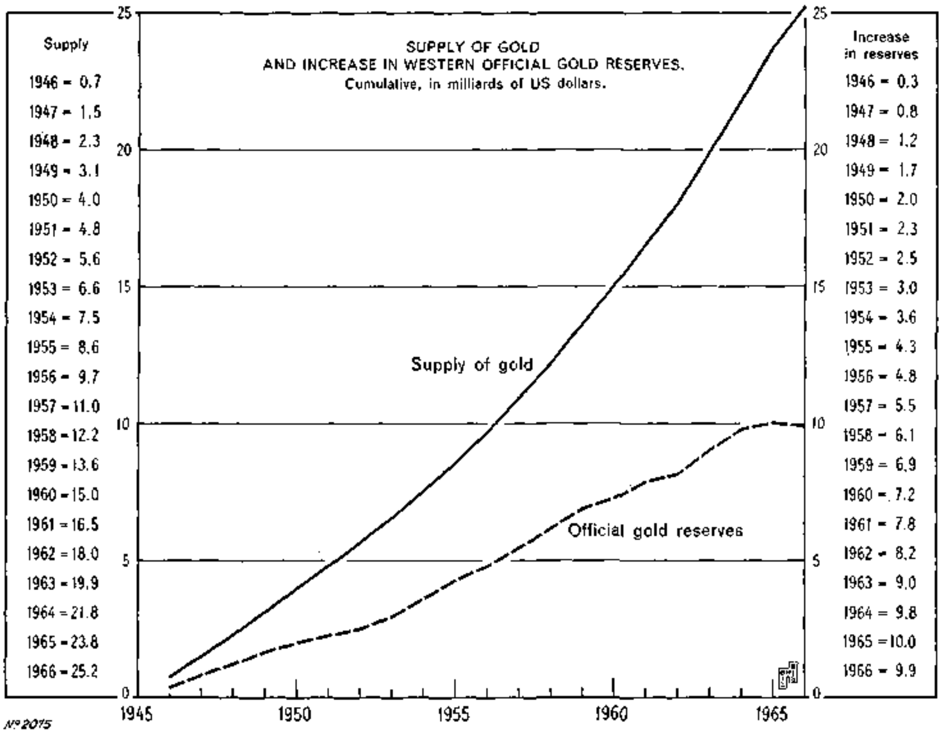
[1] Excluding the USSR, eastern Europe, mainland China and North Korea. [2] Residual figures. Includes estimated purchases by China of about $150 million in 1965 and $75 million in 1966.

Chinese purchases of gold, which had been estimated at about $150 million for the year 1965, may be put at some $75 million for 1966. Non-monetary demand for gold, therefore, was of the order of $1,450 million, roughly $150 million less than it had been in 1965, but substantially above the 1962–64 average of about $1,100 million. This is to a large extent accounted for by the upward trend in industrial and traditional hoarding demand for gold, though in addition there was certainly some speculative buying in 1966.

1966 was the first year since the war in which official gold stocks failed to register any increase. Altogether, in the twenty-one years since the end of the second world war, out of total fresh gold supplies of $25.2 milliard a cumulative amount of $9.9 milliard was added to western official stocks. The graphs on the following page show the year-by-year relationship over this period between monetary and non-monetary demand for gold, as well as the cumulative development of supplies and official reserves.

Supply and uses of gold, 1946-66.





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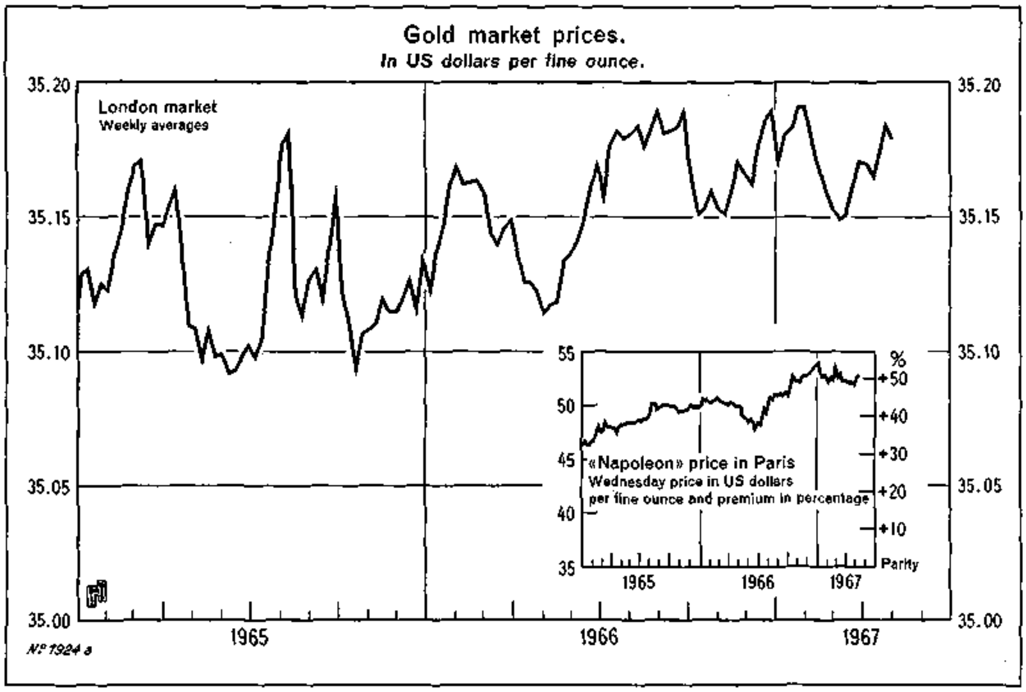
Turning to developments on the London gold market, there were two important factors that held down market supplies during the period under review and that contributed to the net drain which, for the first full year since it came into existence, the central-bank gold pool experienced in 1966. One was the absence, already mentioned, of Russian sales; and the other was the low level of South African sales until late in 1966, owing to that country's balance-of-payments surplus. The easing of private demand in the earlier part of 1966 brought the London fixing price down from over \$35.17 at the end of January to below \$35.11, its lowest level for the year, in early May. The emergence of another acute phase of the sterling crisis, however, led to a strengthening of demand in June and thereafter buying pressure remained heavy until after the annual meeting of the IMF early in October. Accordingly, the fixing price gradually increased to a peak of \$35.18 in mid-July and then fluctuated rather sharply around this level until early October, when it fell to \$35.15. Towards the end of the year conjecture about the possibility of South Africa becoming involved in the Rhodesian crisis and about an increase in the gold price contributed to a renewed emergence of tensions. In the second half of December the fixing price came close to \$35.19½. Quotations eased early in the new year, but then strengthened again to \$35.19½ in late January. Despite the fact that during the first quarter of 1967 South African gold sales were considerably in excess of current production, the fixing price was mostly above \$35.15 and in mid-May it stood at around \$35.18. Following the suspension of silver sales by the US Treasury (see next page), and also partly in connection with events in the Middle East, demand for gold increased sharply later in the month and on 25th May the fixing price reached \$35.19¾, its highest level since October 1962.



The market price of gold coins increased appreciably during 1966, for the second year in succession. Expressed in terms of dollars per fine ounce, the Paris market quotation for the "napoleon", after easing during the earlier months of 1966, rose from $48.25 at the end of May to a fourteen-year peak of $53.75 around the turn of the year. Early in 1967 it receded to about $52.50 but in late May it went up to $54 for the same reasons that caused the rise in the price of gold bullion. Within their general programme of exchange liberalisation the French authorities lifted as from 31st January 1967 the ban on private gold imports and exports. While this move has rendered the Paris market an integral part of the international gold market, there is so far no evidence that it has increased the turnover on the Paris gold market.

Acting under powers conferred on it by the Coinage Act of 1965, on 18th May 1967 the US Treasury suspended all sales of silver except those to "legitimate domestic concerns which use silver in their business". In addition, it introduced a ban on the melting-down, treatment and export of silver coins. This development came after more than eight years in which world demand for silver consistently exceeded fresh supplies. During this period the US Treasury acted as a residual seller of the metal to the market at a fixed price (which since September 1963 had been $1.293 per fine ounce) with the result that between the end of 1958 and the suspension of sales the Treasury's silver stock was reduced from 2,100 to some 500 million ounces — the latter figure being just about the amount of Treasury silver certificates outstanding. The immediate result of the suspension of the Treasury's sales was the emergence of a market price higher than the official US selling price. At the end of May 1967 this market price stood at $1.55 per fine ounce.

World supply and uses of silver.

Year	Supply			Uses[1]			Excess of demand over supply	Change in US Treasury's silver stock
	New production[1]	Other[2]	Total	Coinage	Industrial	Total		
	in millions of fine ounces							
1959	189	35	224	86	213	299	− 75	− 47
1960	208	53	261	104	225	329	− 68	− 68
1961	203	55	258	137	240	377	− 119	− 130
1962	209	99	308	128	259	387	− 79	− 96
1963	215	75	290	166	261	427	− 137	− 184
1964	217	—	217	267	304	571	− 354	− 369
1965	223	98	321	376	347	723	− 402	− 418
1966	231	37	268	107	357	464	− 196	− 202

[1] Excluding the USSR, eastern Europe, mainland China and North Korea. [2] Scrap, demonetised coins, changes in inventories and sales by China and the USSR.

As already mentioned, world gold reserves (excluding those of the USSR, other eastern European countries, mainland China and North Korea) declined by $95 million in 1966 to a total of $43,205 million at the end of the year. Apart from this, the main feature of official gold movements during the year

World gold reserves.

Countries or areas	Changes in 1965	Changes in 1966	Amounts outstanding end-1966
	in millions of US dollars		
United States	− 1,665	− 570	13,235
Canada	+ 125	− 105	1,045
Western Europe	+ 2,435	− 125	22,835
of which			
Austria	*+ 100*	*—*	*700*
Belgium-Luxemburg	*+ 105*	*− 35*	*1,525*
France	*+ 975*	*+ 530*	*5,240*
Germany	*+ 160*	*− 120*	*4,290*
Italy	*+ 300*	*+ 10*	*2,415*
Netherlands	*+ 70*	*− 25*	*1,730*
Portugal	*+ 55*	*+ 70*	*645*
Spain	*+ 195*	*− 25*	*785*
Switzerland	*+ 315*	*− 200*	*2,840*
United Kingdom	*+ 130*	*− 325*	*1,940*
Other	*+ 30*	*− 5*	*725*
Latin American republics	− 80	− 70	985
of which			
Brazil	*− 30*	*− 15*	*45*
Colombia	*− 25*	*− 10*	*25*
Mexico	*− 10*	*− 50*	*110*
Other	*− 15*	*+ 5*	*805*
Asia	+ 75	− 30	1,690
Africa	− 115	+ 165	880
of which			
South Africa	*− 150*	*+ 210*	*640*
Other	*+ 35*	*− 45*	*240*
Other countries	− 5	+ 5	250
Total for all countries	+ 770	− 730	40,920
International institutions	− 530	+ 635	2,285
of which			
BIS	*− 510*	*+ 135*	*− 425*
European Fund	*+ 20*	*− 15*	*50*
IMF	*− 40*	*+ 515*	*2,650*
Other	—	—	*10*
Grand total	+ 240	− 95	43,205

was the transfer of metal from countries' reserves to the international monetary institutions owing mainly to the payment of gold subscriptions in connection with the general increase in IMF quotas.

The gold stocks of the international monetary institutions rose by $635 million during 1966. Most of this went to the IMF, whose holdings grew by $515 million. Gold subscriptions paid to the Fund in 1966 totalled $853 million; the effect of these payments on countries' gold reserves was, however, partly mitigated through gold deposits of $254 million which the Fund made with the United States and the United Kingdom as well as by its gold sales of $148 million to member countries. There was also an improvement during 1966 in the spot gold position of the BIS. Mainly because the end-1966 gold swaps between the BIS and the Swiss National Bank were $220 million lower than those of end-1965, the negative spot gold position of the BIS was $135 million less at the end of 1966 than it had been a year earlier.

Turning to countries' gold reserves, the biggest losses in 1966 were recorded by the two reserve centres. The United States' gold loss amounted to $570 million, which was very much below the 1965 figure of $1,665 million. The principal reason for the much smaller loss was, of course, a reduction in other countries' conversions of dollars into gold. Total net US sales to other countries in 1966 came to $610 million, as against $1,320 million the year before. Sales to western Europe were $660 million, France taking $600 million and Italy $60 million. These were virtually the only European gold purchases of any note in 1966, whereas during 1965 most European countries had made substantial conversions at the US Treasury. The 1966 gold loss was also held down by the fact that $177 million of sales to other countries was "mitigated" by the IMF, while the 1965 loss had been increased by the payment of the $259 million US gold subscription to the Fund.

The gold reserves of the United Kingdom declined by $325 million in 1966. Other western European countries taken together added $200 million to their official gold stocks. France, with $530 million, and Portugal, with $70 million, were the only European countries to record substantial gains, whilst, apart from the United Kingdom, Switzerland, with $200 million, and Germany, with $120 million, were the only substantial losers. And, as has been explained above, the Swiss "loss" was fictitious, since it was largely the result of a change in end-year window-dressing arrangements. Except in the case of the United Kingdom and Switzerland, European gold losses in 1966 were mostly due to gold payments to the IMF.

In the rest of the world there were only two changes of any note in gold reserves. Canada's reserve declined by $105 million, accruals from domestic production being more than offset by sales of $200 million to the United States. And South Africa's gold reserve rose by $210 million. In fact, it went up by $250 million during the first seven months of the year, but was subsequently reduced somewhat when government stockpiling programmes turned the balance of payments into deficit.

International Monetary Fund.

1966 saw a considerable expansion in the total resources of the IMF. The 25 per cent. general increase in quotas decided on in 1964 came into effect in February and together with special increases in the quotas of sixteen member countries it raised the total of all Fund quotas from $16 to about 21 milliard. The operations of the Fund were again on a large scale in 1966, though drawings were considerably less than in 1965. Member countries' gross drawings totalled $1,448 million, compared with $2,433 million the year before. Repurchases, at $721 million, were slightly greater than in 1965, and total net drawings declined from $1,732 to 727 million.

Gross drawings by the United States amounted to $680 million, compared with $435 million in 1965. Other members drew a total of $159 million in

International Monetary Fund: Drawings and repurchases in 1966.

Countries or areas	Drawings	Repurchases	Net drawings
	in millions of US dollars		
United States	680	159*	521
United Kingdom	122	82*	40
Other Europe	83	63	20
of which			
Yugoslavia	*38*	*40*	*— 2*
Latin America	174	220	— 46
of which			
Argentina	*48*	*76*	*— 28*
Brazil	*—*	*39*	*— 39*
Chile	*30*	*45*	*— 15*
Colombia	*38*	*34*	*4*
Others	389	197	192
of which			
Ceylon	*30*	*11*	*19*
Ghana	*52*	*2*	*50*
India	*225*	*125*	*100*
Total	1,448	721	727

* Repurchases by other members' drawings.

US dollars during the year, so that net US drawings were $521 million. Technical drawings by the United States, the object of which is to provide other Fund members with currencies that they can use for repurchases, amounted to $430 million, of which $400 million was in Canadian dollars and the rest in Deutsche Mark. In addition, the United States drew $250 million of lire in August 1966 and used the proceeds to absorb dollars held by the Italian monetary authorities. By the end of 1966 cumulative gross drawings by the United States since February 1964 amounted to $1,640 million, of which $1,090 million were technical drawings. As other countries' US dollar drawings during this period amounted to $719 million, total net US drawings were $921 million. This represents just over 70 per cent. of the US gold tranche of $1,290 million.

The United Kingdom made a further drawing, of $122 million, in 1966. However, as other countries drew $82 million of sterling during the year, the net UK position declined by only $40 million. The British drawing was equal to the increase in the gold tranche of the UK quota and was made in order to mitigate the burden on the British reserves of the gold subscription payment. The drawing was in Deutsche Mark, which were used to purchase gold from the Deutsche Bundesbank. The Fund then sold a corresponding amount of gold to the Bundesbank, thus replenishing its own Deutsche Mark balances and at the same time compensating the Bundesbank for its gold sale to the Bank of England.

Other European countries' net drawings totalled only $20 million in 1966. The largest single drawing was one of $38 million by Yugoslavia, which was, however, more than offset by repurchases of $40 million. Other transactions of European countries included net drawings of $21 million by Ireland and gross drawings and repurchases of $21 million by Turkey.

Latin American countries on balance reduced their Fund indebtedness by $46 million. Elsewhere in the world Fund members drew a net amount of $192 million, of which India accounted for $100 million and Ghana for $50 million.

Fourteen different currencies were drawn on the Fund during the year. Heading the list for the first time was the Canadian dollar, with $460 million. $400 million of these drawings, however, was used by other members for repurchases and the net use of Canadian dollars was only $48 million. On a net basis the most used currency was the lira, with $304 million, followed by the Deutsche Mark, with $225 million.

Out of total gross drawings of $1,448 million, $1,050 million was financed out of member countries' currency subscriptions, $148 million from Fund gold sales and $250 million from a five-year loan in lire which the Fund obtained from Italy in August 1966. The latter transaction was the first in which a member country had made a loan to the Fund outside the framework of the General Arrangements to Borrow. The terms of the Italian loan are similar to those applied under the GAB.

During 1966 and the first quarter of 1967 the Fund deposited $272 million in gold with the two reserve centres to mitigate the effect on their gold reserves of other countries' purchases of gold from them for gold subscription payments to the Fund. Altogether, between September 1965 and March 1967 the Fund made gold "mitigation" deposits totalling $315 million, of which $228 million with the United States and $87 million with the United Kingdom. Out of a total of $1,177 million paid into the Fund in gold since February 1965 in connection with the increase in quotas, $463 million had, by the end of March 1967, been returned to members by the Fund through sales and deposits of gold.

A feature of the year was the revision and extension of the Fund's special facilities, introduced in 1963, for the compensatory financing of primary-producing member countries' payments deficits arising out of export shortfalls. Under the new facilities the ceiling on members' outstanding compensatory drawings has been raised from 25 to 50 per cent. of the quota. This means that if eligible Fund members use this facility, as well as their ordinary Fund drawing rights, to the full the Fund's holdings of their currencies could rise to 250 per cent. of the quotas, as against 225 per cent. previously.

Total net drawings on the Fund in the first quarter of 1967 were $100 million, the principal transaction being a drawing of $166 million by Spain. Another feature of the quarter was that the currency principally used for drawings was the pound sterling, with $72 million. These drawings of sterling by other Fund members of course produced a corresponding improvement in the net UK position. Then on 25th May the United Kingdom repaid to the Fund $405 million out of the $1 milliard that it had drawn in December 1964. The Fund used this amount to repay the sums made available to it on that occasion under the General Arrangements to Borrow.

Official reserves and other monetary movements.

United States. Measured according to the liquidity concept, the US balance-of-payments deficit was about the same in 1966 as it had been the year before — $1,370 million as against $1,335 million. The pattern of its financing, however, was quite different. In 1965 it had been covered as to 90 per cent. by official financing, while in 1966 there was a surplus of $245 million on the official-settlements basis, and, within this, an improvement of $1,020 million in the net balance of liquid liabilities and assets in the official sector.

United States: External monetary movements.

Items	1965	1966					1967
		Year	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter
	in millions of US dollars (+ = increase in assets, decrease in liabilities)						
Reserves	−1,220	− 570	− 425	− 70	− 80	+ 5	−1,025
of which							
Gold	*−1,665*	*− 570*	*− 70*	*− 210*	*− 170*	*− 120*	*− 50*
Foreign exchange . . .	*+ 350*	*+ 540*	*− 220*	*+ 165*	*+ 425*	*+ 170*	*−1,005*
IMF gold tranche position	*+ 95*	*− 540*	*− 135*	*− 25*	*− 335*	*− 45*	*+ 30*
Liabilities to official foreigners	− 85	+ 815	+ 825	− 315	+ 490	− 185	− 255
of which							
Liquid	*+ 15*	*+1,590*	*+ 850*	*− 55*	*+ 600*	*+ 195*	*+ 85*
Non-liquid	*− 100*	*− 775*	*− 25*	*− 260*	*− 110*	*− 380*	*− 340*
Balance on official-settlements basis	−1,305	+ 245	+ 400	− 385	+ 410	− 180	−1,280
less Non-liquid liabilities to official foreigners	+ 100	+ 775	+ 25	+ 260	+ 110	+ 380	+ 340
Total change in official liquid position	−1,205	+1,020	+ 425	− 125	+ 520	+ 200	− 940
plus Liabilities to non-official foreigners. .	− 130	−2,390	− 475	− 25	−1,220	− 670	+ 710
Balance on liquidity basis .	−1,335	−1,370	− 50	− 150	− 700	− 470	− 230

The outstanding feature of US monetary movements in 1966 was the increase of $2,390 million in liabilities to non-official foreigners. This development, which was most marked in the second half of the year, came about as a result of the tightening of monetary conditions in the United States. In particular, banks in the United States were attracting deposits through the operations of their foreign branches in the Euro-dollar market. Some of these deposits may have come from official sources, although they are recorded in the statistics as being owed to non-official institutions. This is because, when foreign monetary authorities shift the employment of their dollars from the United States to the Euro-dollar market, or when they decide to employ newly-received dollars in that market, the US statistics show an increase in liabilities to foreign commercial banks, not to official holders. It is probable, therefore, that the US statistics exaggerate the real increase that took place in non-official holdings of dollars, as well as the real decline in official holdings.

Although the inflow of short-term funds through the banking system more than covered the liquidity deficit, this did not mean that the US authorities had no external financing problems in 1966. On the contrary, the gold stock fell by a further $570 million, net sales of gold to foreign countries amounting to $610 million. In addition, the IMF gold tranche position deteriorated by $540 million. The effect of these reserve losses on the net official position was, however, more than offset by the changes that occurred in official holdings of foreign exchange and in liabilities to official foreigners.

US official holdings of convertible foreign exchange, which had already risen by $350 million during 1965, went up by a further $540 million in 1966 and at the end of the year stood at the record figure of $1,320 million. Nearly half of the 1966 increase came from the sterling counterpart of assistance given to the Bank of England, while most of the rest represented the proceeds of a $200 million Deutsche Mark/dollar swap between the Federal Reserve System and the BIS in December 1966, the purpose of which was to enable the BIS to moderate the end-of-year rise in Euro-dollar interest rates. The increase in US official exchange holdings then had as a counterpart an increase in foreign holdings of dollars.

As regards liabilities to official foreigners, these declined by $815 million during 1966. Liquid liabilities were reduced by $1,590 million, whilst there was an increase of $775 million in certain non-liquid liabilities to foreign official agencies, which, while they do not affect the overall balance on the liquidity basis, are included in the official-settlements balance. Part of the decline in liquid liabilities was simply the counterpart of the rise in non-liquid liabilities; and another part will have been reflected in the recorded increase of liabilities to non-official foreigners, although, as was pointed out above, some of this shift may not have represented a real transfer of dollars from official to private hands. In addition, the liquid liabilities to official foreigners were affected by the debt prepayments which foreign governments made during the course of the year. These totalled $410 million, of which Germany accounted for $195 million, Italy for $145 million and France for $70 million. In 1965 the only debt prepayment had been one of $180 million by France. If these prepayments were considered as financing items and added to the liquidity deficit, then the overall deficit for 1966 would go up to $1,780 million, compared with $1,515 million in 1965.

Liabilities to official foreigners also include foreign holdings of US Government non-marketable bonds, mostly denominated in the holder's currency and usually known as Roosa bonds. The total of Roosa bonds outstanding declined by $450 million in 1966. Germany's holdings went down by $250 million, Canada's by $125 million, Austria's by $50 million and Switzerland's by $45 million. On the other hand, Italy's Roosa bond holdings rose by $25 million. In addition, a further $515 million was converted from non-liquid to liquid form, $300 million in Germany, $190 million in Switzerland and $25 million in Austria. These conversions involved corresponding shifts between non-liquid and liquid liabilities to official foreigners.

The liquidity deficit for the first quarter of 1967, before seasonal adjustment, was $230 million. On the official-settlements basis, however, the deficit was $1,280 million. The difference between these two figures is accounted for by two factors. The first, and most important, was an outflow of $710 million through the banking system in the form of a reduction in liabilities to non-official foreigners, caused by the repayment of funds which banks in the United States had borrowed in the Euro-dollar market during 1966. The second was a further increase of $340 million in non-liquid liabilities to official foreigners. Apart from this latter increase, the official-settlements deficit was essentially financed through a reduction of $1,005 million in official holdings of convertible foreign exchange, mostly sterling.

United Kingdom. The principal feature of UK monetary movements in 1966 was that despite a marked improvement in the overall balance of payments there was an outflow of funds from London on a scale such that the total of official financing was considerably greater than it had been in 1965. More precisely, there was a substantial outflow during the summer months of both years, but in 1966 the autumn reflux was much smaller than it had been in 1965, owing to a decline in the sterling holdings of overseas sterling-area countries, and to the adverse covered differential on the comparison with dollar interest rates.

Thanks to the measures which the British authorities took in July 1966, the payments deficit declined from $695 to 500 million. And the real improvement was greater than this, since the 1966 deficit included some $200 million for the servicing of the post-war loans obtained from the United States and Canada; corresponding payments in 1964 and 1965 had been mostly deferred. The exact composition of monetary movements in 1966 cannot be precisely measured, owing to lack of information about the amount of central-bank assistance taken by the Bank of England. A rough idea of what happened can, however, be obtained if it is assumed that movements in official holdings of sterling outside the sterling area were by and large due to the taking or reimbursement of central-bank assistance.

Using this assumption, it can be deduced that total official financing requirements for 1966 may have exceeded the payments deficit by something of the order of $1 milliard. This figure therefore measures very roughly the extent of the adverse monetary movements that occurred during the year. There were two main factors behind these movements: the renewed crisis of confidence in sterling during the summer of 1966 and the attraction of high dollar interest rates. The effects of these two factors for the year 1966 as a whole show up mainly in the reduction of $420 million in the item "Other sterling liabilities (net)" (which measures the change in all sterling liabilities except those to official holders outside the sterling area and which includes a decline of $475 million in liabilities to non-official holders outside the sterling area) and in the decrease of $455 million in net foreign currency liabilities of UK banks.

United Kingdom: External monetary movements.

Items	1965	1966 Year	1966 1st quarter	1966 2nd quarter	1966 3rd quarter	1966 4th quarter
	in millions of US dollars (+ = increase in assets, decrease in liabilities)					
Official assets	+ 690	− 790	− 320	− 295	− 115	− 60
of which						
Reserves	*+ 690*	*+ 95*	*+ 565*	*− 295*	*− 115*	*− 60*
Use of dollar portfolio	—	*− 885*	*− 885*	—	—	—
Account with IMF	−1,400	+ 5	− 10	+ 20	− 10	+ 5
Sterling liabilities to official holders in non-sterling area (net)	− 290	− 810	+ 350	− 40	−1,110	− 10
Official deposits in foreign currencies by overseas central banks (net)	+ 200	− 40	—	—	− 50	+ 10
Other sterling liabilities (net)	+ 80	+ 420	− 325	− 275	+ 885	+ 135
of which						
to sterling-area holders	*− 25*	*− 15*	*− 255*	*− 485*	*+ 470*	*+ 255*
to non-official non-sterling-area holders	*+ 90*	*+ 475*	*− 60*	*+ 210*	*+ 405*	*− 80*
to international organisations	*+ 15*	*− 40*	*− 10*	—	*+ 10*	*− 40*
Liabilities of UK banks in foreign currencies (net)	+ 185	+ 455	+ 150	+ 185	− 20	+ 140
Liabilities in overseas sterling-area currencies (net)	− 20	+ 125	− 65	+ 50	+ 125	+ 15
Miscellaneous capital	− 140	+ 135	+ 100	+ 100	+ 5	− 70
Overall balance	− 695	− 500	− 120	− 255	− 290	+ 165

In addition to these two main items, there were also during the year declines of $125 million in the net liabilities in overseas sterling-area currencies and of $135 million in miscellaneous liabilities. The change in the UK banks' position in overseas sterling-area currencies reflected transactions of a book-keeping nature, which were offset in overseas sterling-area countries' sterling holdings, whilst the miscellaneous capital outflow was due, to the extent of $105 million, to reductions of advance deposits against future export orders which had been made by western Germany.

So far as official monetary movements are concerned, the largest financing item was the use of $885 million from the Treasury's dollar portfolio. In addition, the $810 million increase in sterling liabilities to official holders outside the sterling area must have reflected mainly the taking of central-bank assistance, as did the net increase of $40 million in official deposits in foreign currencies by overseas central banks. Published reserves rose by $95 million over the year.

Looking at the course of events during the year, the pressure on sterling reached its peak in the third quarter. The main factors at that time were the seasonally high payments deficit of $290 million, including the balancing item, and the reduction of $885 million in sterling liabilities to holders other than official holders outside the sterling area. More than half of the reduction in this item, or $470 million, was in the balances of the outer sterling area and reflected its largely seasonal payments deficit rather than lack of confidence in sterling. By contrast, during the first six months of the year the outer sterling area's payments surplus had produced a rise of $740 million in its sterling balances, thus considerably easing the burden of UK official financing.

In the last quarter of 1966 the balance of payments turned into surplus. The reserves went down by $60 million but some repayments of assistance were made. At the same time, the sterling balances of the non-sterling area began to be rebuilt. Officially-held balances, excluding assistance, must have shown a significant rise, since even including repayments of assistance they went up by $10 million during the quarter. And privately-held non-sterling-area balances also increased, by $80 million. The potential effect on the reserves of these inflows, as well as of miscellaneous capital receipts of $70 million, was, however, nullified by a renewed outflow of $140 million arising from changes in the banks' net foreign currency position and by a further reduction of $255 million in the outer sterling area's sterling balances.

During the first quarter of 1967 there was a substantial inflow of funds to London, particularly at the beginning of the year. This took the form partly of a further rebuilding of sterling balances by the non-sterling area and partly of a reflux of funds from the United States following the easing of dollar interest rates. Details of first-quarter developments are not yet available, but it is known that the reserves went up by $160 million and that most of the outstanding central-bank assistance was repaid.

Continental western Europe. The main features of the external monetary movements of continental western European countries for 1966 show a considerable contrast with those for 1965. Firstly, the total external monetary surplus, at $1,080 million, was less than half what it had been the year before. To a considerable extent this reflected the decline of the French and Italian surpluses. In addition, it may be mentioned that debt prepayments from this group of countries to the United States rose from $180 to 410 million. Secondly, the improvement in the net foreign positions of those continental banking systems for which data are available amounted to only 10 per cent. of the overall surplus, as against 40 per cent. in 1965. Here, too, the difference is accounted for chiefly by France and Italy. Thirdly, the growth of official assets slowed down from $1,495 to 975 million. Fourthly, whereas the $335 million increase in official gold and exchange holdings recorded in 1965 was the net result of a reduction of $1,980 million in exchange holdings and a rise of $2,315 million in gold reserves, in 1966 neither of these items showed much movement, gold reserves going up by $200 million and exchange holdings declining by $85 million.

So far as the gold reserves of continental Europe are concerned, more than half of the difference between the 1965 and 1966 increases can be accounted for by transactions between these countries and the international monetary institutions. Thus in 1965 continental European countries received $350 million of gold from the IMF in connection with the $1.4 milliard UK drawing; in 1966, on the other hand, they made gold subscriptions of $365 million to the Fund. Furthermore, the Swiss National Bank's end-year gold swaps with the BIS increased by $330 million in 1965, but decreased by $220 million in 1966. Nevertheless the fact remains that in 1965, even excluding these transactions with the international institutions, the increase in

Continental European countries, Canada and Japan: External monetary positions.

Countries	End of year	Gold and foreign exchange	Net IMF and GAB position	Total official assets	Commercial banks (net)	Total foreign assets	Changes (+ = increase in assets, decrease in liabilities): Total official assets	Changes (+ = increase in assets, decrease in liabilities): Commercial banks
		in millions of US dollars						
Austria	1965	1,235	70	1,305	— 60	1,245	— 10	— 45
	1966	1,225	100	1,325	— 145	1,180	+ 20	— 85
Belgium-Luxemburg	1965	2,145	310	2,455	— 560	1,895	+ 160	— 25
	1966	2,120	370	2,490	— 705	1,785	+ 35	— 145
Denmark	1965	510	60	570	— 45	525	— 60	+ 80
	1966	510	70	580	— 25	555	+ 10	+ 20
Finland	1965	275	15	290	— 65	225	— 70	— 15
	1966	140	30	170	— 90	80	— 120	— 25
France	1965	5,370	885	6,255	— 110	6,145	+ 705	+ 255
	1966	5,655	985	6,640	— 155	6,485	+ 385	— 45
Germany	1965	7,070	1,075	8,145	— 680	7,465	— 325	+ 45[1]
	1966	7,240	1,255	8,495	— 580	7,915	+ 350	+ 100
Greece	1965	235	15	250	5	255	— 30	—
	1966	250	25	275	5	280	+ 25	—
Iceland	1965	45	5	50	— 5	45	+ 5	—
	1966	50	5	55	— 10	45	+ 5	— 5
Ireland	1965	395	10	405	250	655	— 40	— 10
	1966	490	—	490	240	730	+ 85	— 10
Italy	1965	4,400	550	4,950	— 195	4,755	+ 955	+ 620
	1966	4,235	885	5,120	195	5,315	+ 170	+ 390
Netherlands	1965	2,045	360	2,405	35	2,440	+ 75	— 75
	1966	2,030	415	2,445	— 45	2,400	+ 40	— 80
Norway	1965	445	25	470	10	480	+ 90	+ 70
	1966	480	45	525	— 40	485	+ 55	— 50
Portugal	1965	990	15	1,005	110	1,115	+ 55	+ 30
	1966	1,100	20	1,120	110	1,230	+ 115	—
Spain	1965	1,270	140	1,410	—	1,410	— 105	—
	1966	1,040	165	1,205	—	1,205	— 205	—
Sweden	1965	815	140	955	95	1,050	+ 5	+ 20
	1966	845	165	1,010	135	1,145	+ 55	+ 40
Switzerland	1965	3,700	—	3,700	.	.	+ 60	.
	1966	3,685	—	3,685	.	.	— 15	.
Turkey	1965	60	— 20	40	.	.	+ 25	.
	1966	25	— 20	5	.	.	— 35	.
Total	1965	31,005	3,655	34,660	—1,215[2]	29,705[2]	+ 1,495	+ 950[2]
	1966	31,120	4,515	35,635	—1,110[2]	30,835[2]	+ 975	+ 105[2]
Canada	1965	2,605	355	2,960	— 70	2,890	+ 140	— 400
	1966	2,230	450	2,680	355	3,035	— 280	+ 425
Japan	1965	1,865	255	2,120	— 900	1,220	+ 130	+ 280
	1966	1,735	320	2,055	— 515	1,540	— 65	+ 385

[1] After elimination of statistical changes. [2] Fifteen countries only.

Note: For Group of Ten countries, plus Switzerland, the figures for official assets are those used for multilateral surveillance. They do not in most cases correspond to published reserve figures.

continental European gold reserves was somewhat larger than the total of official financing, whereas in 1966 it was somewhat smaller.

As regards the difference between 1965 and 1966 in the movement of continental official exchange holdings, much of the explanation of the large drop that occurred in 1965 is to be found in the extent to which these countries lent their currencies through the IMF and the large increase in their commercial banks' net foreign positions. In addition, there were in 1965 some exceptional conversions into gold of exchange reserves that had accrued in earlier years.

With regard to the geographical distribution of continental European reserve increases in 1966, the largest rises were recorded in France ($385 million) and Germany ($350 million). Italy's official assets went up by $170 million, their rise having been limited by transfers of dollars to the banking system through special swap arrangements. In relation to their economic rôle, rather large reserve gains were shown by Portugal ($115 million), Ireland ($85 million) and Norway ($55 million).

Three countries accounted for virtually the whole advance in continental gold reserves, viz. France ($530 million), Portugal ($70 million) and Greece ($40 million). France also showed the largest decline in exchange reserves ($250 million), but Spain's holdings fell substantially, by $205 million, and Italy's by $175 million. Germany's foreign exchange assets, on the other hand, went up by $285 million. The $860 million increase in continental net IMF positions was fairly broadly distributed, though Italy, with $335 million, had much the largest individual rise. This included the $250 million special loan to the Fund in August 1966.

During the first quarter of 1967 the net official assets of continental countries declined by $545 million, their gold and exchange holdings going down by $435 million and their net IMF and GAB positions by $110 million. On the other hand, the net foreign liabilities of the commercial banks in those countries for which data are available fell by $740 million, the German banks alone having increased their foreign position by $820 million.

Germany. For Germany the main influence on monetary movements during 1966 was the pronounced improvement in the balance of payments from a deficit of $280 million to a surplus of $450 million. If the debt prepayment of $195 million made to the United States in December 1966 is counted as an official financing item, the 1966 surplus becomes $645 million. As there was not much change in the banks' net positions, the improvement in the balance of payments showed up mainly in a turn-round of the net official position from a loss of $325 million to a gain of $350 million, or $545 million if the debt prepayment is included.

It was not until May 1966 that the external position moved decisively into surplus. During the first four months of the year, in fact, there was a slight deficit of $5 million. The commercial banks recorded a seasonal improvement

Germany: External monetary movements.

Items	1965	1966	January–April 1966	May 1966–March 1967
	in millions of US dollars (+ = increase in assets, decrease in liabilities)			
Net official assets	— 325	+ 350	— 365	+ 815
of which				
Gold	*+ 160*	*— 115*	*— 5*	*— 110*
Convertible foreign exchange	*— 700*	*+ 785*	*— 125*	*+ 895*
Other reserve assets	*+ 35*	*— 390*	*— 220*	*— 170*
Net IMF and GAB position	*+ 165*	*+ 180*	*+ 35*	*+ 150*
Other (net)	*+ 15*	*— 110*	*— 50*	*+ 50*
Banks' net position	+ 45	+ 100	+ 360	+ 560
Overall balance	— 280	+ 450	— 5	+ 1,375

of $360 million in their net foreign position, which was offset partly by a decline of $125 million in the exchange reserves and partly by a fall of $220 million in the item "Other reserve assets". The volume of outstanding Deutsche Mark Roosa bonds was reduced by $150 million and official holdings of sterling, which had been built up in 1965 under the terms of the Anglo-German agreement on the equalisation of defence costs, fell by $70 million.

Since May 1966 the balance of payments has been consistently favourable and the rate of surplus increased steadily into the first quarter of 1967. The pattern of monetary movements during this period can be seen most clearly if it is taken as a whole, so as to eliminate the effects of the end-year operations of the commercial banks. Between the end of April 1966 and the end of March 1967 the cumulative surplus was $1,375 million. Of this amount, $560 million was added to the banks' net foreign position, leaving $815 million to be financed by the official sector. The essential element of official financing during this period was the increase of $895 million in the exchange reserves. The gold reserve, on the other hand, declined by $110 million, owing to a gold subscription payment of $103 million to the IMF; and this accounted for most of the $150 million increase in the net IMF position. Other reserve assets showed a further fall of $170 million, of which $100 million came from repayments of Deutsche Mark Roosa bonds, $50 million from a reduction of official holdings of sterling and the remaining $20 million from repayment of EPU debts.

France. Monetary movements in France during 1966 show the fundamental change that occurred in the balance of payments in the course of the year. During the first eight months of 1966 there was a surplus of $610 million, and this was reflected in a rise of $505 million in the gold reserve, together with an increase of $95 million in the net IMF position, of which $50 million came from the gold subscription payment. The external position turned into deficit in September and for the last four months of the year the deficit amounted to $270 million. As there was a debt prepayment of $70 million to the United States in September, total financing requirements for these four months were $340 million. These were mostly met through drawing $245 million on the exchange reserves, and there was a decline of $45 million in the banks' net foreign position. During the first quarter of 1967 there was a further moderate deficit of $50 million. As this was accompanied by an inflow of $60 million through the banks, net official assets rose slightly.

Italy. As in France, the balance of payments became markedly less favourable in 1966. The long period of surplus, which had begun in the second quarter of 1964, came to an end in the third quarter of 1966 and gave way to a deficit of $110 million in the last quarter of the year. As a result, the annual surplus was reduced from $1,575 million in 1965 to $560 million in 1966. These figures, however, overstate the deterioration that occurred between the two years, since there was a debt prepayment of $145 million to the US Government in September 1966 which may be considered as a sort of financing item.

During the first three quarters of 1966 the Italian commercial banks continued to absorb part of the balance-of-payments surplus and thus helped to moderate the need for official financing. Within this general framework, however, the pattern of monetary movements varied considerably from quarter to quarter.

In the first quarter there were no problems of official financing, since the overall surplus of $75 million was more than covered by an increase, partly seasonal, of $220 million in the banks' net foreign position. Net reserves fell by $275 million, which was considerably more than the banks' external surplus for the quarter. There were two reasons for this. One was the gold subscription payment of just over $30 million to the IMF and the other was the increase of $90 million in the item "Other official assets", representing a shift from first-line reserves into longer-term assets.

Italy: External monetary movements.

Items	1965	1966 Year	1966 1st quarter	1966 2nd quarter	1966 3rd quarter	1966 4th quarter	1967 1st quarter
	in millions of US dollars (+ = increase in assets, decrease in liabilities)						
Net reserves	+ 400	− 220	− 275	+ 175	− 35	− 85	− 170
of which							
Gold	*+ 295*	*+ 10*	*− 35*	*—*	*− 10*	*+ 55*	*—*
Foreign exchange	*− 110*	*− 175*	*− 190*	*+ 185*	*− 105*	*− 65*	*− 150*
Other reserve assets	*+ 225*	*− 85*	*− 50*	*− 10*	*+ 60*	*− 85*	*− 15*
Short-term liabilities	*− 10*	*+ 30*	*—*	*—*	*+ 20*	*+ 10*	*− 5*
Net IMF and GAB position and other loans to IMF	+ 405	+ 335	+ 40	+ 30	+ 255	+ 10	+ 25
Other official assets	+ 150	+ 55	+ 90	− 30	+ 5	− 10	+ 5
Net official position	+ 955	+ 170	− 145	+ 175	+ 225	− 85	− 140
Banks' net position	+ 620	+ 390	+ 220	+ 10	+ 185	− 25	− 105
Overall balance	+ 1,575	+ 560	+ 75	+ 185	+ 410	− 110	− 245

During the second quarter the surplus rose to $185 million, the monetary counterpart of which was an increase of $175 million in net reserves. In the third quarter, when the surplus reached its seasonal peak, the banks' net foreign position showed a substantial rise of $185 million, leaving $225 million to be financed by the official sector. In July the Federal Reserve activated its lira swap facility to the extent of $225 million in order to absorb the influx of dollars into Italy's reserves. But in the following month this swap was liquidated by means of a $250 million lira drawing by the United States on the IMF. This drawing was financed by a special lira loan to the Fund, which essentially accounts for the third-quarter increase in Italy's net IMF position.

The last-quarter deficit was mostly reflected in a decline of $85 million in the net official position. More precisely, it was financed by a reduction of that amount in dollars held under swaps with the Federal Reserve, which are included in the item "Other reserve assets". The exchange reserves declined by $65 million, almost entirely as a result of gold purchases from the US Treasury.

Owing partly to fiscally-motivated outflows of capital, the overall deficit increased to $245 million in the first quarter of 1967. The exchange reserves fell by $150 million and the banks' net foreign position declined by $105 million. The deficit was concentrated in January and February, after which March showed a surplus of $40 million.

Italian policy as regards the financing of the payments surplus can be clearly seen by adding together the monetary items for 1965 and 1966. Out of a total surplus of $2,135 million, $1,010 million was financed through the banks and a further $740 million through the IMF. The first-line reserves of gold and foreign exchange showed a rise of only $20 million.

Netherlands. In 1966 the balance of payments showed a deficit of $40 million. The banking system, however, reduced its net foreign position by twice that amount, so that net official monetary assets were able to rise by $40 million. In fact there was an increase of $55 million in the net IMF position, accompanied by a decline of $15 million in the gold and exchange reserves. The increase in the Netherlands' net Fund position was due as to $25 million to the payment of its gold subscription to the Fund and for the rest to other members' drawings of florins on the Fund. These transactions produced a corresponding reduction in the gold and exchange reserves respectively, but, so far as the exchange reserves are concerned, they were more than offset by the effects of the reduction in the banks' net foreign position, so that the exchange reserves actually rose during the year by $10 million.

There was a considerable contrast between the two halves of 1966 as regards both the pattern and direction of external monetary movements. During the first six months of the year there was a balance-of-payments deficit of $180 million, which was reflected in a $105 million reduction in the banks' net foreign assets and a decline of $75 million in net official assets.

In the second half of the year, however, when the balance of payments moved into surplus on a cash basis, the banks' foreign position increased by only \$25 million, whilst net official assets rose by \$115 million.

The cash balance of payments showed a further deficit of \$60 million during the first quarter of 1967, the counterpart to which was a decline in the net external position of both the official and banking sectors. The exchange reserves fell by \$50 million, partly through a rise of some \$20 million in other official assets; and the banks' net foreign liabilities went up by \$35 million.

Belgium. In Belgium the pattern of monetary movements for 1966 as a whole was somewhat similar to that in the Netherlands. The balance of payments showed a deficit of \$110 million, but owing to a reduction of \$145 million in the banks' net foreign position there was a rise of \$35 million in net official assets. As in the Netherlands, the net IMF position increased more than the total of official assets, namely by \$60 million, whilst the gold and exchange reserves declined by \$25 million. In the first quarter of 1967 there was a payments surplus of \$35 million. Net official monetary assets, however, fell by \$10 million, since the banks' net foreign liabilities, which had risen by \$185 million during the three preceding quarters, were reduced by \$45 million.

Austria. In Austria, too, a payments deficit was accompanied in 1966 by an increase in net official assets. The overall external deficit was \$65 million, but this was more than covered by a reduction of \$85 million in the banks' foreign position, nearly all of which occurred during the last quarter of the year, when the deficit reached \$90 million. The increase of \$20 million in total net official assets was, as in the Netherlands and Belgium, more than accounted for by a rise of \$30 million in the net IMF position, of which \$25 million resulted from the payment of Austria's gold subscription to the Fund. There was no change in the gold reserve during the year, whilst the exchange reserves decreased by \$10 million.

Switzerland. Switzerland's net official monetary assets fell by \$15 million in 1966. The gold and exchange reserves went up by \$75 million, whilst other official assets declined by \$90 million. During the first four months of the year the reserves were reduced by \$450 million, partly for seasonal reasons and partly because of the attraction of rising interest rates abroad. In May the Swiss money and capital markets began to tighten and this, combined with mid-year window-dressing, led to an increase of \$200 million in reserves by the end of June. The effects of the reversal of the window-dressing operations in July were to a considerable extent offset by the repercussions of the sterling crisis, but the reserves declined gradually between end-June and end-October by a total of \$110 million before rising again by \$435 million by the end of the year. The gold reserve was \$200 million lower at the end of 1966 than it had been a year earlier, essentially because of smaller end-year swaps with the BIS. The exchange reserves, on the other hand, went up during the year by \$275 million. As regards the decline of \$90 million in other official assets, \$45 million came about through a reduction in the Swiss Confederation's holdings of non-marketable US Government securities denominated in Swiss francs.

During the early months of 1967 there were considerable further fluctuations in the reserves. Following a seasonal decline of \$415 million in January, there were, for the first time, window-dressing operations by the banks at the end of the first quarter, which produced a rise of \$210 million in the reserves during March. The reversal of these operations contributed largely to the decline of \$280 million in the reserves during April.

Of the northern countries, Denmark and Norway were about in balance for 1966, whilst Sweden recorded a surplus and Finland a deficit.

Sweden. The overall balance of payments showed a surplus of \$95 million. Net official assets went up by \$55 million, of which the exchange reserves accounted for \$30 million and the net IMF position for \$25 million. The banks' net foreign assets rose by \$40 million, a decline of \$40 million in the first half of the year being followed by an increase of \$80 million in the following six months.

Finland. The balance-of-payments deficit increased between 1965 and 1966 from \$85 to 145 million, over half of the rise being recorded in the final quarter of the year. Most of the 1966 deficit was financed by a reduction of \$120 million in net official assets. The gold reserve declined by \$40 million, of which \$15 million was paid to the IMF and was reflected in an increase in Finland's net Fund position, and the exchange reserves fell by \$80 million.

Spain. The balance-of-payments deficit increased to \$205 million in 1966. During the first six months net official assets declined by \$215 million, the gold and exchange reserves falling by \$240 million whilst the net IMF position, owing to the payment of the Fund gold subscription, went up by \$25 million. Then, during the third quarter, the reserves rose seasonally by \$85 million and, although they declined again during the last quarter, at the end of the year they stood \$15 million above the mid-year figure. During the first quarter of 1967 there was a further deficit of \$170 million, virtually all of which was financed by drawing \$165 million, the whole of Spain's gold tranche position, from the IMF.

Canada. The balance of payments, measured as the sum of changes in net official monetary assets and in the net foreign position of the banks, improved between 1965 and 1966 from a deficit of \$260 million to a surplus of \$145 million. At the same time there was a complete reversal not only of the direction but also of the pattern of monetary movements. In 1965 the deficit had been more than covered by a \$400 million net reduction in the banks' short-term foreign position, so that net official monetary assets rose by \$140 million. In 1966, on the other hand, the banks' net foreign position increased by \$425 million, whilst net official assets were reduced by \$280 million.

The 1966 increase in the banks' foreign position resulted essentially from the pull of higher interest rates in the United States. More than half of the rise took place in the third quarter of the year, when monetary conditions in the United States were particularly tight. So far as the change in net official assets is concerned, the main item was a fall of $430 million in the gold and exchange reserves. The gold reserve went down by $105 million, including gold sales of $200 million to the US Treasury; and the exchange reserves were reduced by $325 million during the year, $145 million of which resulted from repurchases by the Canadian Government of its own US dollar obligations held in the United States. The exchange reserves were also affected by certain transactions which led to increases in non-reserve monetary assets. On the one hand, Canada's net IMF position went up by $95 million during the year and, on the other hand, the Canadian Government purchased $25 million of IBRD securities from US residents. By the end of 1966 Canada's gold and US dollar reserves plus its net creditor position in the IMF had fallen to about $2,500 million, somewhat below the figure which had been agreed on with the US authorities in return for Canadian exemption from the US interest equalisation tax.

In the first quarter of 1967 there was a balance-of-payments deficit of $315 million, nearly all of which was financed by a $280 million decline in the banks' net foreign position. The reserves fell by $35 million, official exchange balances decreasing by $70 million, whilst the gold reserve rose by $35 million.

Japan. The overall balance showed a surplus of $320 million in 1966, compared with one of $410 million the year before. The surplus was more than financed, as in the case of Canada, by an increase of $385 million in the banks' net foreign position. Since interest rates abroad, particularly in the United States, were higher than those in Japan, the banks' yen liabilities fell by $215 million and their net foreign exchange liabilities by $170 million. Japan's net official monetary assets declined over the year by $65 million, the principal changes being a fall of $100 million in the exchange reserves and an increase of $65 million in the net IMF position.

During the first quarter of 1967 there was a deficit of $285 million, which was more than covered by a decline of $300 million in the banks' net foreign position.

Foreign exchange markets.

Two important sets of factors affected exchange-market developments during the period under review. On the one hand, there was the influence of US monetary policy and, on the other, the evolution of the basic balance of payments in certain important European countries. So far as the former is concerned, the period under review falls into two distinct phases. During the first of these, which lasted for most of 1966, tight monetary conditions were attracting funds to the United States. This, despite the continuing US balance-of-payments deficit, created a strong underlying demand for dollars and contributed, except in large surplus countries, to some weakening of European currencies against the dollar. During the second phase, which began in December 1966 and was still continuing in the early months of 1967, US monetary policy was being progressively relaxed. Partly as a result of this, and although policies in some European countries were eased, to some extent in sympathy with US developments, most European currencies were at or above par on the US dollar by early May 1967.

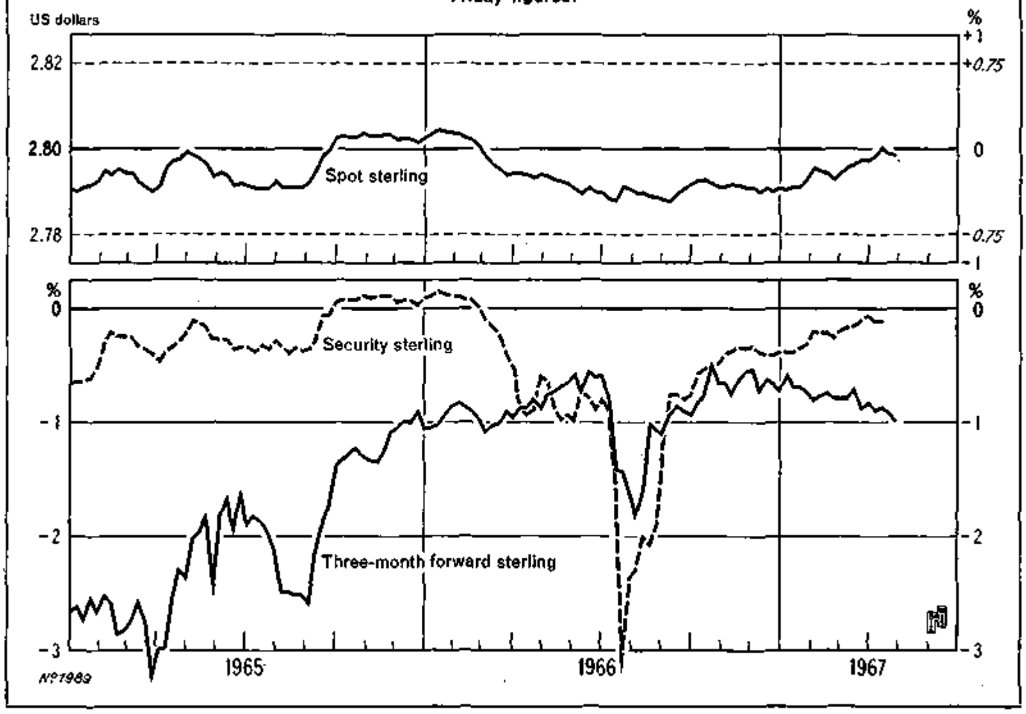
So far as the exchange-market effects of European balance-of-payments developments are concerned, these are most clearly seen in the weakness of sterling in the spring and summer of 1966, followed by its recovery from late September onwards, in the weakening of the French franc and the Italian lira during the last quarter of 1966, and in the progressive strengthening of the Deutsche Mark from May 1966 onwards.

Sterling. At the beginning of 1966 the outlook for the pound appeared encouraging. A steady inflow of funds since September 1965 had, despite large official purchases of dollars, most of which were used for the repayment of assistance and for the reduction of the authorities' outstanding forward exchange commitments, brought the spot rate by mid-January up to \$2.80½. Over the same period the three-month forward discount on the dollar had narrowed from 2½ to 1 per cent. per annum.

From mid-February onwards, however, the situation began to deteriorate again. Doubts about the underlying trend of the balance of payments began to reappear and this, followed by the announcement of the general election date, brought the spot rate down to par by the end of the month. At the same time the upward movement of interest rates in other countries, particularly the United States, began to put pressure on sterling. By the end of March the spot rate was not much above \$2.79¼, at or around which level it then remained until mid-May.

Pressure on sterling increased further when the seamen's strike began on 16th May. By the end of that month the spot rate had fallen to \$2.79⅛ and the devaluation of the Indian rupee in early June was an added source of general unease. The announcement on 13th June of new central-bank support arrangements for sterling brought momentary relief but this was soon followed by a further tightening of monetary conditions abroad as mid-year approached, and despite official support the spot rate went below \$2.79. During the second quarter, however, there was little change in the authorities' forward exchange commitments, and the three-month forward discount on the dollar in fact declined from 1 to 0.6 per cent. per annum, largely as a result of the swapping of sterling into dollars.

In July continuing tight monetary conditions abroad, coupled with the publication of unfavourable balance-of-payments figures for the first quarter of the year and a substantial loss of reserves for June, caused the situation to deteriorate rather drastically. During the first half of the month there was heavy selling of sterling, both spot and forward. At considerable cost to the



Sterling/dollar exchange rates.*
Friday figures.

* The spot dollar rate for sterling is shown both in dollars and, as is also the case for the security sterling rate, as a percentage of the parity. The three-month forward rate for sterling is shown as a discount on the spot rate, on a percentage per annum basis.

reserves, which were supplemented by substantial external assistance, the spot rate was not allowed to fall below $2.78\frac{5}{16}$, but the three-month forward discount widened to over 1 per cent. by mid-month. Indicators of the abrupt decline of confidence in sterling included a widening of the discount on security sterling to over 3 per cent. and a rise in three-month Euro-sterling interest rates to over 8 per cent. Strong measures were then taken to correct the situation, but sterling continued to be under some pressure until well into September, although from about the middle of August onwards this seemed to be due as much to a general shortage of dollars overseas as to confidence factors. The spot rate, after recovering to about $2.79 at the end of July, weakened again in August and remained below that level until the second half of September, whilst the forward rate weakened considerably in late July and early August, to a discount of 1¾ per cent. per annum.

The announcement on 13th September of further central-bank support arrangements, made at a time when the dollar shortage was already becoming less acute and it was becoming apparent that sterling itself was in short supply, at last brought a reversal of the situation. Sterling strengthened, both spot and forward, later in the month and the improvement was generally maintained for the rest of the year. Though the spot rate did not go much above $2.79, the three-month forward discount on the dollar had come down to less than ¾ per cent. per annum by the end of October.

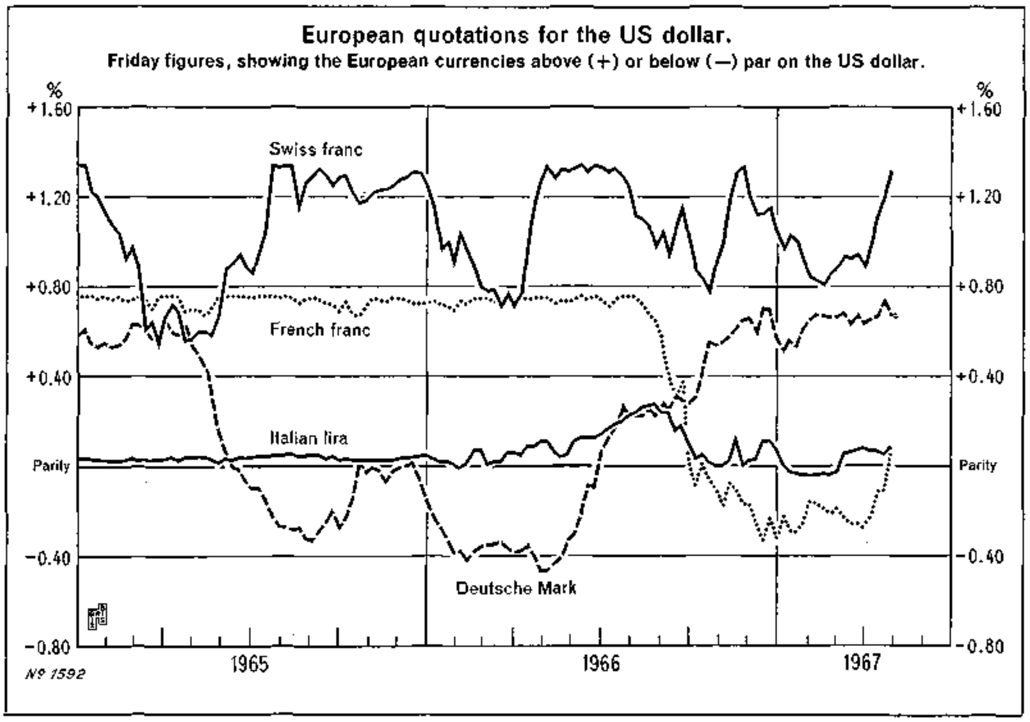
A decline in dollar interest rates from December 1966 onwards moved interest-arbitrage margins in favour of sterling. This, together with growing expectations of a reduction in sterling interest rates, accentuated the normal seasonal return of funds after the end of the year. With the basic balance of payments back in surplus, there was, therefore, a very large inflow of foreign exchange during January 1967, which allowed the authorities to make substantial repayments of assistance whilst also letting the spot rate rise to about \$2.79½. After easing somewhat in February, quotations strengthened again during March, and in mid-April, by which time the bulk of the assistance had been paid off, the spot rate reached parity for the first time for over a year. In May, however, a number of factors combined to produce an easing of the rate to about \$2.79½ at the end of the month.

Swiss franc. During the early months of 1966 there was a considerable outflow of funds from Switzerland, partly for the usual seasonal reasons and partly because of rising interest rates in the Euro-dollar market. As a result the spot rate for the Swiss franc against the dollar eased progressively from Sw.fr. 4.31⅞ at the end of 1965 to Sw.fr. 4.34⅜ three months later. In April a tightening of the Swiss money market caused the Swiss franc to become firmer and by early May the spot dollar rate had reached the official intervention point of Sw.fr. 4.31½. An equally sharp fall in the forward premium on the dollar, which ran off completely during April, suggests that this tightness was not expected to last beyond mid-year. In the event, however, the sterling crisis kept the spot rate for the dollar very close to the intervention point until late July.

In August, after the height of the sterling crisis was passed, funds began to flow out of Switzerland again as interest rates abroad reached their peak, and the spot rate for the dollar eased to Sw.fr. 4.33. Following a further weakening to almost Sw.fr. 4.34 in October, it hardened during November to Sw.fr. 4.31½, as end-year liquidity preparations were put in hand, but then eased to below Sw.fr. 4.32 in December when the end-year tightness of the market was moderated by official intervention.

Early in 1967 the spot rate for the dollar eased further, in accordance with the usual seasonal pattern. But as domestic interest rates remained firm, in contrast with the general downward trend apparent elsewhere, demand for francs brought the spot rate up to the official intervention point in late April 1967.

Deutsche Mark. The striking improvement that occurred in Germany's balance of payments during the period under review was reflected in the exchange-market quotations for the Deutsche Mark. This improvement, however, did not begin to make itself felt until May 1966. In fact, during the first four months of the year the Deutsche Mark remained well below par on the dollar, partly because of a seasonal outflow of funds through the banks in January and partly because the overall external position continued in deficit during February, March and April. Indeed, had the US authorities not



been purchasing Deutsche Mark during these months in the market, the spot rate against the dollar might have fallen even further.

From the end of April onwards spot quotations improved almost continuously and the Deutsche Mark reached its upper limit on the dollar by December. Although the swing into very large balance-of-payments surplus explains the strength of the upward movement in the exchange rate, other factors influenced its rate of appreciation. The acute sterling crisis certainly contributed to the sharpness of the rise in mid-year, whereas subsequently the upward trend of quotations was moderated by the attraction of Euro-dollar interest rates. Despite an easing of liquidity requirements for the banks, tight domestic monetary conditions in connection with the year-end finally carried the rate to its ceiling.

A substantial, more-than-seasonal outflow of funds in the new year caused the Deutsche Mark to ease in January, but, although this outflow continued, under the weight of the external surplus the exchange rate soon recovered to just below its ceiling.

French franc. The long series of external surpluses which had begun as soon as the franc was stabilised in December 1958 came to an end in the late summer of 1966, and the spot rate for the French franc against the dollar, which had remained consistently at or very close to the upper intervention point, began to ease rather rapidly. It went below par at the end of September 1966 and by the end of the year stood at a discount of some 0.3 per cent. Although the balance of payments continued in moderate deficit, the franc became a little firmer in the new year. Quotations then eased again in February and March, only to become much firmer in April, and by late May the spot rate for the franc was well above par.

Italian lira. The most striking feature of exchange-market quotations for the lira during the period under review was their greater flexibility. From March 1964 until early in 1966 the spot rate against the dollar had been held by the authorities just above the parity of Lit. 625. From there it rose to Lit. 623¼ in August 1966, reflecting the seasonal strengthening of the balance of payments, and subsequently declined to just below par in January 1967 as the external position turned into deficit. When the balance of payments reverted to surplus in March 1967 the lira went above par on the dollar again, and at the end of April it stood at Lit. 624½.

Other exchange developments.

There were further changes during the year both in foreign exchange controls in the strict sense as well as in certain less formal arrangements limiting the freedom of international monetary flows. The reserve-currency countries both had recourse to further restraints on outward transfers, while in France there were substantial relaxations of administrative regulations.

In the United States the balance-of-payments guide-lines for 1967 followed their earlier pattern. Non-financial corporations were asked to limit direct investment abroad during 1966–67 to an annual average 20 per cent. above that for 1962–64. The existing ceiling on commercial-bank foreign lending of 109 per cent. of the end-1964 level has been retained until the end of 1967, and the banks have been requested to phase their lending within this ceiling evenly over the period. Finally, non-bank financial institutions were asked to keep the growth in their foreign assets down to 5 per cent. between October 1966 and the end of 1967. In addition, there were a number of changes affecting the interest equalisation tax, which was prolonged until July 1969. The rate of tax, in terms of interest equivalent, was raised to 1½ per cent., and the President of the United States was authorised to vary the tax between 1 and 1½ per cent. In February 1967 exemption was extended to lending by foreign branches of US banks for periods of over one year.

The outward movement of long-term capital was already heavily circumscribed in the United Kingdom, and the exchange control aspects of the July 1966 programme consequently concentrated rather on tightening existing restrictions on current transfers. The basic annual holiday travel allowance was cut to £50 per person, and the limit on cash gifts from UK residents to residents outside the sterling area was similarly reduced. At the same time, control over outward transfers by UK emigrants was tightened. A month later, to reduce the scope for switching between sterling and foreign currencies by the UK banking sector, the individual limits imposed upon authorised foreign exchange dealers' open positions and their spot against forward positions were reduced. A change of a rather different kind was announced with the April 1967 budget, when it was decided that all non-resident transactions in sterling securities would be settled at the official rate of exchange, thereby abolishing the market in security sterling.

On the Continent the most important development was the French move to virtually complete convertibility. From the end of January 1967 almost all the remaining exchange control regulations were rescinded and the general freedom of transfer of all means of payment, securities and gold was restored. This broad liberalisation had been foreshadowed, in 1966, by the general permission granted to banks to open foreign currency accounts for their customers, and by the extension to one year of the time-limit on forward exchange operations and on French franc credits to non-residents. Permission is still required, however, for foreign direct investment in France (including portfolio investment resulting in the acquisition of a 20 per cent. interest in a French quoted company) or for direct French investment abroad. Equally, the introduction of foreign securities on the French capital market and French non-bank borrowing abroad in excess of Fr.fr. 2 million still require advance authorisation.

Outside Europe and North America, perhaps the most significant exchange developments were the currency devaluations in India, Brazil and Argentina. From 6th June 1966 the declared par value of the rupee was reduced by some 36 per cent. from Rupees 4.76 to Rupees 7.5 = US $1. As part of a wider currency reform, the free rate for the new Brazilian cruzeiro (equal to 1,000 old cruzeiros) was devalued by 18 per cent. from Cruz. 2.22 to Cruz. 2.72 = US $1 from 13th February 1967; and a month later, after a series of smaller devaluations, the Argentine peso was devalued by 29 per cent. from Pesos 250 to Pesos 350 = US $1, a rate which applies to all operations.

IV. THE EURO-CURRENCY MARKET.

In 1966 the Euro-currency market experienced its largest annual increase, in both liabilities and assets. For the reporting European countries the dollar volume in the market, net of redeposits between banks, may be estimated to have risen from about $10 to 13 milliard.

The main expansionary factor was the tightening of credit in the United States, which, among other things, led to heavy Euro-dollar borrowing by US banks. In addition, demand was kept high by the reduced foreign access to bank credit in the United States and by credit-market tensions in Germany and the Netherlands. The resultant strengthening of the demand for Euro-dollars led to a sharp rise in Euro-dollar deposit rates that was apparently quite successful in attracting new funds to the market. In addition, the supply of Euro-dollars received support from a further increase in the Italian Exchange Office's dollar swaps, from the depositing in the Euro-dollar market of part of the proceeds of US issues in the Euro-capital market and from the sterling crisis in the summer of 1966, which partly took the form of switches of foreign London-held sterling balances into Euro-dollars.

The external dollar liabilities of the banks of the eight reporting European countries went up by $3.4 milliard, or about 30 per cent., in 1966 and their assets by $4.5 milliard, or nearly 40 per cent. The $1.1 milliard increase in their net dollar asset position reflected mainly larger placements in the United States. This demand for Euro-dollars tended to shift the banks' new lending away from their own area and to cause them to convert increased amounts of other currencies into dollars. This latter point is confirmed by the $480 million deterioration in the banks' net foreign position in reported currencies other than dollars.

Changes in the banks' external foreign currency positions.

Items	Dollars			Other reported currencies[1]		
	Liabilities	Assets	Net position	Liabilities	Assets	Net position
	in millions of US dollars					
Eight reporting European countries[2]						
1965	+ 1,710	+ 2,590	+ 880	+ 250	+ 520	+ 270
1966	+ 3,370	+ 4,470	+ 1,100	+ 770	+ 290	— 480
Amount outstanding at end of 1966[3]	*14,720*	*16,060*	*+ 1,340*	*3,590*	*3,850*	*+ 260*
Canada and Japan						
1965	— 50	— 100	— 50	+ 20	— 110	— 130
1966	— 220	+ 470	+ 690	— 80	— 30	+ 50
Amount outstanding at end of 1966[3]	*4,700*	*5,760*	*+ 1,060*	*310*	*460*	*+ 150*

[1] Sterling, Swiss francs, Deutsche Mark, French francs, Dutch florins, Italian lire. [2] Belgium-Luxemburg, France, Germany, Italy, Netherlands, Sweden, Switzerland, United Kingdom. [3] For full series see tables on pages 147–152.

Liabilities and assets in these other currencies went up by $770 and 290 million respectively, or at a considerably lower average rate than the positions in dollars. As in preceding years, their relative importance thus tended to decline. Whereas in comparison with September 1963, the earliest date for which reasonably complete data are available, the banks' total gross positions in dollars more than doubled, those in the other reported currencies went up by only about one-third. The development differed markedly, however, from currency to currency. In 1966 reported liabilities in French francs expanded from $100 to 570 million, those in Swiss francs from $930 to 1,220 million and those in Deutsche Mark from $870 to 970 million, whereas liabilities in Dutch florins declined from $170 to 70 million and those in sterling from $730 to 710 million.

The external gross foreign currency positions of the Canadian and Japanese banks, which are, however, only partly related to developments in the Euro-currency market, showed comparatively little overall change in 1966. Liabilities in dollars declined by $220 to 4,700 million, whereas assets went up by $470 to 5,760 million; the net asset position thus widened sharply from $370 to 1,060 million. Reflecting the voluntary restraint programme and the tightening of US credit conditions, the whole of this rise was vis-à-vis the United States, whereas the net position vis-à-vis the rest of the world declined by $150 million. The Japanese and Canadian banks' external positions in foreign currencies other than dollars are of relatively minor importance and have, if anything, tended to decline.

Geographical distribution of the reporting European banks' external dollar positions. Only $1,270 million, or about 38 per cent., of the $3,370 million increase in the reporting European banks' dollar liabilities in 1966 was vis-à-vis countries outside the reporting group. Liabilities towards US residents, despite the voluntary restraint programme, went up by $320 million. A factor behind this movement was the depositing in the Euro-dollar market of part of the $475 million raised by US corporations through their security issues in the Euro-capital market.

The reporting banks' liabilities to outside countries other than the United States, after edging up by only $160 million in 1965, advanced by $950 million last year. The main causes of this were the highly attractive interest rates offered in the Euro-dollar market and the flight out of sterling. Liabilities to "Other western Europe" went up by $240 million and those to Latin America, the Middle East and "Other" by $540 million.

The banks' liabilities vis-à-vis countries within the reporting group, after showing a $1.4 milliard increase in 1965, mounted by another $2.1 milliard last year. A substantial part of this advance consisted of funds flowing to the United Kingdom on their way to the United States. Liabilities vis-à-vis Switzerland went up by $850 million and those vis-à-vis Belgium by $300 million; the rest of the $2.1 milliard increase was fairly broadly distributed.

The geographical break-down of the rise in assets was quite different from that of liabilities, claims on countries outside the reporting group accounting for about two-thirds of the total $4,470 million increase. Assets

Dollar positions of reporting European banks vis-à-vis non-residents.

Positions vis-à-vis	1964 December	1965 December	1966 March	1966 June	1966 September	1966 December
	in millions of US dollars					
Liabilities						
Other western Europe	800	850	770	870	1,020	1,090
Eastern Europe	260	290	220	190	280	360
Canada	880	560	490	510	610	660
Japan	40	50	60	60	50	50
Latin America	610	720	710	740	760	840
Middle East	680	850	860	960	1,090	1,000
Other	740	850	860	950	1,060	1,120
Total	4,010	4,170	3,970	4,280	4,870	5,120
United States	1,260	1,370	1,450	1,680	1,800	1,690
Total outside own area	5,270	5,540	5,420	5,960	6,670	6,810
Position inside own area	4,370	5,810	5,060	5,550	6,400	7,910
of which vis-à-vis						
Belgium	*270*	*340*	*390*	*450*	*520*	*640*
France	*550*	*840*	*720*	*880*	*960*	*1,040*
Germany	*140*	*190*	*250*	*220*	*340*	*240*
Italy	*620*	*1,240*	*850*	*880*	*1,300*	*1,510*
Netherlands	*260*	*290*	*260*	*300*	*320*	*410*
Sweden	*110*	*130*	*80*	*130*	*110*	*150*
Switzerland	*1,240*	*1,730*	*1,790*	*1,750*	*1,880*	*2,580*
United Kingdom	*1,180*	*1,050*	*720*	*940*	*970*	*1,340*
Grand total	9,640	11,350	10,480	11,510	13,070	14,720
Assets						
Other western Europe	380	670	620	780	760	890
Eastern Europe	460	540	580	720	690	670
Canada	420	670	480	420	360	620
Japan	440	510	530	610	620	670
Latin America	290	380	400	470	420	450
Middle East	110	170	150	150	170	190
Other	120	270	310	350	390	390
Total	2,220	3,210	3,070	3,500	3,410	3,880
United States	2,820	3,010	3,530	3,900	4,720	5,270
Total outside own area	5,040	6,220	6,600	7,400	8,130	9,150
Position inside own area	3,960	5,370	4,800	4,860	5,930	6,910
of which vis-à-vis						
Belgium	*320*	*370*	*400*	*380*	*390*	*460*
France	*540*	*710*	*520*	*550*	*780*	*900*
Germany	*370*	*370*	*340*	*410*	*480*	*480*
Italy	*880*	*1,070*	*650*	*600*	*890*	*1,190*
Netherlands	*230*	*370*	*400*	*470*	*520*	*570*
Sweden	*90*	*160*	*150*	*180*	*160*	*180*
Switzerland	*330*	*460*	*570*	*580*	*570*	*670*
United Kingdom	*1,200*	*1,860*	*1,770*	*1,690*	*2,140*	*2,460*
Grand total	9,000	11,590	11,400	12,260	14,060	16,060

vis-à-vis US residents, after edging up by only $190 million in 1965, advanced by $2,260 million, or about 75 per cent., and undoubtedly represented the most dynamic market element in 1966. The bulk of this rise was in the form of increased Euro-dollar borrowing by US banks through their branches in Europe, mainly in London. This activity seems to have continued up to the middle of December 1966, but was apparently greatest during the third quarter, when claims on the United States shot up by $820 million.

The increase in the banks' assets vis-à-vis outside countries other than the United States slowed down from $990 to 670 million. The explanation for the smaller rise may largely be that, whereas in 1965 the enactment of the US voluntary restraint programme tended to increase these countries' dependence on Euro-dollar borrowing, in 1966 the greater competition for Euro-dollar funds from US banks left less room for other kinds of borrowers. The $670 million gain was fairly broadly distributed; only claims on Canada declined. Assets vis-à-vis Japanese residents — reflecting the economic upswing and the diminished availability of US credit — went up by $160 million, or nearly one-third.

At $1,540 million, the increase in claims on countries within the reporting group was on about the same scale as in 1965. Claims on the United Kingdom rose by $600 million, or about one-third.

As regards the geographical break-down of the reporting banks' net position, the $1.1 milliard addition to their net assets was in the form of a $1,940 million rise in net claims on the United States and of $280 and 560 million increases in net liabilities to other outside countries and within their own area. The biggest change vis-à-vis countries outside the reporting area other than the United States was the $160 million rise in net claims on Japan. The net position vis-à-vis Canada, on the other hand, which owing to the US voluntary restraint programme had shown a $570 million improvement in 1965, declined by $150 million.

Within the reporting area the banks' net position deteriorated by $640 million vis-à-vis Switzerland, $210 million vis-à-vis Belgium and $150 million vis-à-vis Italy. On the other hand, their net position improved by $310 million vis-à-vis the United Kingdom and by $80 and 60 million respectively vis-à-vis the Netherlands and Germany. The increase in their net claims on the United Kingdom was a counterpart to the sharp rise in the UK banks' claims on the United States, whereas the larger borrowing by Dutch and German residents reflected mainly the tightness of the domestic credit markets.

The net size of the Euro-dollar market. To obtain a truer picture of the net amount of credit channelled through the Euro-dollar market, several factors have to be taken into account in considering the data in the table on page 140. On the one hand, the figures are inflated both by a substantial amount of redepositing between banks and by certain positions which are not related to Euro-dollar market transactions. On the other hand, they do not include positions vis-à-vis residents and cannot show the intake or the placement of dollars in the form of swaps. The table on the next page tries to make allowance for these various factors, using the methods described on pages 145–147 of the BIS's Thirty-Sixth Annual Report.

These estimates suggest that the net size of the Euro-dollar market increased in 1966 from about $10 to 13 milliard. Liabilities towards the United States rose by $0.3 milliard and those towards other outside countries by $0.9 milliard, while the increase in the supply of funds from within the reporting area may be put at about $1.8 milliard.

Estimated net size of the Euro-dollar market.

Items	Sources			Uses			Net		
	1964	1965	1966	1964	1965	1966	1964	1965	1966
	end-year figures, in milliards of US dollars								
Outside area									
United States . .	0.7	0.8	1.1	1.5	1.8	4.1	+ 0.8	+ 1.0	+ 3.0
Other countries .	4.0	4.2	5.1	2.2	3.2	3.9	− 1.8	− 1.0	− 1.2
Total	4.7	5.0	6.2	3.7	5.0	8.0	− 1.0	—	+ 1.8
Inside area									
Official monetary institutions . .	0.8	2.2	2.8	—	—	—	− 0.8	− 2.2	− 2.8
Non-residents other than banks	0.8	1.0	1.5	0.5	0.6	0.8	− 0.3	− 0.4	− 0.7
Non-bank residents, plus swaps from or into the domestic or third currencies* . .	1.7	1.8	2.5	3.8	4.4	4.2	+ 2.1	+ 2.6	+ 1.7
Total	3.3	5.0	6.8	4.3	5.0	5.0	+ 1.0	—	− 1.8
Total net size of the market .	8.0	10.0	13.0	8.0	10.0	13.0	—	—	—

* Excluding swaps carried out under special arrangements with official monetary institutions but including, under "Uses", the reporting banks' own use of Euro-dollars for liquidity purposes and window-dressing operations (temporary switching out of dollars into the domestic currency).

The changes in the positions vis-à-vis outside countries are the same as result from the data on page 140. As regards the \$1.8 milliard increase in the supply from within the reporting area, funds received from official monetary institutions were up by about \$0.6 milliard. \$350 million of this change was due to a further rise in the amount of dollars obtained by the Italian banks through swaps with the Italian Exchange Office and about \$310 million to end-of-year Euro-dollar placements by the Swiss National Bank. Liabilities to non-residents other than banks went up by \$0.5 milliard; about \$0.2 milliard of this movement seems to have been due to an increase in Swiss (non-bank) residents' deposits with UK banks and reflected the attraction of the high Euro-dollar deposit rates. The increase in the supply of Euro-dollars from non-bank residents and through swaps might be estimated at about \$0.7 milliard. The \$480 million deterioration in the banks' net position in foreign currencies other than dollars shown in the table on page 138 would seem to point to a substantial increase in the amount of switching from other foreign currencies into dollars. Moreover, the available evidence suggests that there was an increase both in outright dollar liabilities to domestic non-bank residents and in the banks' switching out of their domestic currencies into dollars.

As regards uses, the whole increase in lending seems to have been vis-à-vis outside countries. As already indicated by the figures in the table on page 140, claims on the United States went up by about \$2.3 milliard and those vis-à-vis the rest of the outside world by $0.7 milliard. Placements within the reporting area seem to have changed little. Owing mainly to a $0.2 milliard rise in the UK banks' claims on German non-banks, assets vis-à-vis non-residents other than banks went up from $0.6 to 0.8 milliard, but this increase seems to have been roughly offset by a decline in lending to residents. The main factor behind the estimated decline of about $0.2 milliard in this latter item was the reduction in the UK banks' lending to local authorities. On the other hand, the Italian banks continued to swap dollars into other currencies in order to lend them to residents.

Changes in the external foreign currency positions of banks in individual countries. At $2,330 and 2,760 million respectively, the expansion of the UK banks' dollar positions accounted for about 70 per cent. of the total increase in the reporting European banks' dollar liabilities and about 60 per cent. of the increase in their assets. As a result the UK banks' share in total outstanding positions went up by 6 per cent. to 48 per cent. Their dominant rôle in the 1966 expansion of the market reflected above all the sharp rise in the US banks' Euro-dollar borrowing, which was mainly channelled through their branches in London. Thus the UK banks' claims on US residents advanced by $1.9 milliard and their liabilities towards the rest of the world by about the same amount, $650 million of this latter increase being vis-à-vis Switzerland. Liabilities vis-à-vis the United States went up by $400 million. The $430 million reduction in the UK banks' net debtor position, which reflected the increased demand for Euro-dollars from the United States, was facilitated by the domestic credit ceilings and the smaller market financing requirements of UK local authorities.

The Italian banks' foreign currency assets vis-à-vis non-residents went up by $690 to 2,730 million and those vis-à-vis residents by $160 to 1,980 million. Their net external position in foreign currencies, which had already recorded a $590 million improvement in 1965, strengthened by another

External positions in foreign currencies of the reporting European banks.

Banks of	Liabilities		Assets		Net position	
	Dollars	Other reported currencies*	Dollars	Other reported currencies*	Dollars	Other reported currencies*
	changes from end-1965 to end-1966, in millions of US dollars					
Belgium-Luxemburg	+ 110	+ 340	+ 270	+ 60	+ 160	— 280
France	+ 260	+ 100	+ 640	— 40	+ 380	— 140
Germany	— 40	— 20	— 40	— 50	—	— 30
Italy	+ 220	+ 150	+ 520	+ 170	+ 300	+ 20
Netherlands	+ 260	+ 140	+ 130	+ 110	— 130	— 30
Sweden	+ 40	+ 70	+ 70	+ 40	+ 30	— 30
Switzerland	+ 190	— 150	+ 120	— 110	— 70	+ 40
United Kingdom	+ 2,330	+ 140	+ 2,760	+ 110	+ 430	— 30
Total change	+ 3,370	+ 770	+ 4,470	+ 290	+ 1,100	— 480

* Sterling, Swiss francs, Deutsche Mark, French francs, Dutch florins, Italian lire.

$320 million. Within the space of two years the Italian banks' net position thus shifted from $700 million of liabilities to $210 million of assets. The main reasons for the improvement in 1966 were a further $350 million increase in the banks' use of the Italian Exchange Office's special swap facilities and the domestic credit ease, which contrasted with rising interest rates abroad.

The relative ease of domestic credit conditions, together with the gradual liberalisation of French foreign exchange policy, was also one of the major factors behind the $380 million increase in the French banks' external net dollar assets. About one-third of this seems to have been due to switches out of third currencies into dollars. Claims on US residents went up from $200 to 590 million.

The main features in the development of the Belgian–Luxemburg banks' foreign currency position were a $360 million rise in French franc liabilities and a $270 million increase in dollar assets. About two-thirds of the French francs seems to have been re-lent to residents. The largest individual change in dollar claims was a $90 million increase vis-à-vis the Netherlands. On a net basis, the Belgian–Luxemburg banks' position improved by $160 million in dollars but deteriorated by $280 million in the other reported currencies.

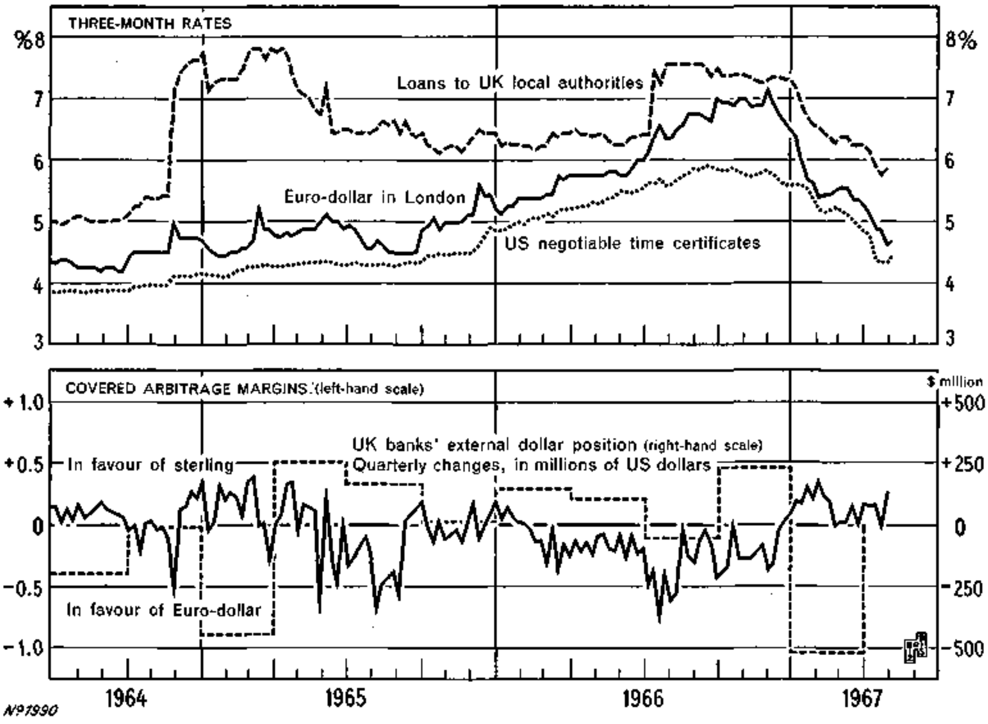
The Dutch banks' net foreign currency position shifted from $80 million of assets to $80 million of liabilities. The main cause of this turn-round was the tightening of domestic credit. The German, Swedish and Swiss banks' foreign currency positions showed little overall change.

Towards the end of 1966 several central banks took action to ease the tensions arising from the commercial banks' end-year operations. Direct support given to the Euro-dollar market amounted to about $800 million. The Swiss National Bank channelled back approximately $470 million acquired from its banks, of which $310 million directly and the remainder through the BIS. The BIS, for its part, placed an additional $275 million in the Euro-dollar market; of this amount, $200 million was obtained by activating the swap facility with the US Federal Reserve and the rest came from the BIS's own resources. The Nederlandsche Bank placed dollars on a swap basis with its commercial banks, while the Deutsche Bundesbank and the Bank of Italy took measures to limit their banks' end-year repatriations.

* * *

Interest rate developments. In 1966 the tightening of some of the key national credit markets and the ensuing strengthening of demand for Euro-dollar credits led to a sharp increase in Euro-dollar interest rates. The rate on three-month deposits in London, which had already shown a strong upward momentum in the last quarter of 1965, continued its rising trend throughout the first nine months of 1966 and by early September it stood at 6¾ per cent., or 2¼ per cent. above its level a year earlier. The usual seasonal tightening pushed the rate up further to 7 per cent. in October and

Rates of interest in London and New York and arbitrage margins in London.
Weekly, in percentages per annum.



at one point early in December it even exceeded that level by $^1/_8$ per cent. This seasonal peak coincided, however, with the turning-point in the international credit situation and was immediately followed by a sharp decline, which carried the three-month rate to below 5½ per cent. early in February. After a short pause the downward movement resumed in March, and by the end of April the rate had fallen to $4^5/_8$ per cent. In May the rate strengthened, to reach $5^1/_8$ per cent. by the end of the month.

The yield on US negotiable certificates of deposit, which are in some ways a competitor of Euro-dollar deposits, also went up, but not quite as much as that on Euro-dollars. As a result the margin between the two rates widened from its past average of about $^3/_8$ per cent. to reach $1^1/_8$ per cent. during the fourth quarter of 1966. This rather high margin in favour of Euro-dollar deposits was one of the reasons why US corporations deposited a major part of the proceeds of their Euro-bond issues in the Euro-dollar market in 1966. At the same time the much higher rates on Euro-dollar deposits did not deter the US banks from borrowing through their European branches in the Euro-dollar market. The explanation is that the rates paid on certificates of deposit were held down by Regulation Q and thus did not fully reflect the actual scarcity of credit in the United States; moreover, the US banks' taking of deposits from their foreign subsidiaries is not subject to reserve requirements and is therefore less costly than the nominal rates suggest.

With the decline in Euro-dollar rates, their margin over the yields on certificates of deposit tended to narrow. By the end of April 1967 it had fallen to ¼ per cent., but it widened to ½ per cent. in the course of May.

The climb of the Euro-dollar rate in 1966 was also reflected in the covered interest-arbitrage margins between Euro-dollar and UK local-authority deposits. Apart from January and the second half of December, this margin stood throughout most of 1966 in favour of Euro-dollars and thus tended to discourage the UK banks from switching Euro-dollar funds into sterling. This was undoubtedly the main factor behind the \$430 million improvement in the UK banks' net external dollar position. In the third quarter, however, when owing to the weakness of forward sterling the covered interest-arbitrage margins in favour of Euro-dollar deposits were at their highest, the UK banks' net dollar liabilities expanded. The reason for this paradoxical situation was the renewed outbreak of the sterling crisis, which led to substantial switches of foreign London-held balances out of sterling into Euro-dollars. Although the UK banks' external dollar assets went up by \$760 million, this growth was not quite large enough to offset the whole of the \$810 million rise in their dollar liabilities. By the fourth quarter, however, the UK banks had caught up with the situation; their assets showed a record increase of \$930 million and their net position improved by \$230 million.

The sharp decline in the Euro-dollar rate from the second half of December onwards shifted the covered interest-arbitrage margins back in favour of UK local-authority deposits. In the first quarter of 1967 the UK banks' net dollar liabilities went up by \$520 million, thus more than offsetting their decline in 1966.

* * *

Complete figures for the changes in the banks' Euro-dollar positions during the first quarter of 1967 are not yet available. Nevertheless there can be little doubt that the winding-up of end-year operations caused the total volume of outstanding credit to decline. Apart from this seasonal factor, the development of the Euro-dollar market was dominated by the easing of monetary conditions in the United States and Germany. Easier credit within the United States led to a reduction in the US banks' borrowing in the Euro-dollar market; as a result, the claims of UK banks on the United States, after rising by \$1,880 million in the course of 1966, decreased by \$230 million. Although there was also some decline in the demand from German residents, the main impact of Germany's return to monetary ease was on the supply side of the Euro-dollar market. The German banks' external dollar assets shot up by \$360 to 760 million, about \$240 million of this increase being vis-à-vis the United Kingdom and another \$100 million vis-à-vis France, whereas claims on the United States declined slightly. The change in the relationship between the supply and demand for Euro-dollars, which had already become discernible in the course of December, was reflected in a pronounced easing of market conditions that continued until May, when interest rates began to strengthen again.

Short-term liabilities and assets of ten countries' commercial banks in certain foreign currencies vis-à-vis non-residents.

Countries	End of month	US dollars		Other currencies[1]		Total		
		Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Net
		in millions of US dollars						
Belgium-Luxemburg . . .	1963 September	360	260	280	230	640	490	— 150
	1964 March	380	310	370	210	750	520	— 230
	September	290	310	540	270	830	580	— 250
	December	420	360	520	320	940	680	— 260
	1965 March	400	440	570	280	970	720	— 250
	June	400	440	680	360	1,080	800	— 280
	September	480	460	630	330	1,110	790	— 320
	December	560	470	600	380	1,160	850	— 310
	1966 March	560	530	770	490	1,330	1,020	— 310
	June	530	520	790	470	1,320	990	— 330
	September	570	590	810	410	1,380	1,000	— 380
	December	670	740	940	440	1,610	1,180	— 430
France[2]	1963 September	650	670	630	660	1,280	1,330	50
	1964 March	610	710	590	560	1,200	1,270	70
	September	620	720	540	560	1,160	1,280	120
	December	810	860	560	660	1,370	1,520	150
	1965 March	730	890	550	590	1,280	1,480	200
	June	770	830	550	700	1,320	1,530	210
	September	920	980	510	680	1,430	1,660	230
	December	1,070	1,220	530	640	1,600	1,860	260
	1966 March	770	1,160	750	740	1,520	1,900	380
	June	810	1,280	710	650	1,520	1,930	410
	September	1,100	1,570	710	610	1,810	2,180	370
	December	1,330	1,860	630	600	1,960	2,460	500
Germany	1963 September	270	510	100	170	370	680	310
	1964 March	220	510	110	130	330	640	310
	September	290	420	80	150	370	570	200
	December	440	440	80	120	520	560	40
	1965 March	230	510	60	120	290	630	340
	June	250	460	70	120	320	580	260
	September	270	400	70	120	340	520	180
	December	370	440	70	170	440	610	170
	1966 March	290	440	50	100	340	540	200
	June	300	470	50	110	350	580	230
	September	330	660	60	100	390	760	370
	December	330	400	50	120	380	520	140
Italy	1963 September	1,540	950	750	410	2,290	1,360	— 930
	1964 March	1,240	780	580	300	1,820	1,080	— 740
	September	1,250	810	360	270	1,610	1,080	— 530
	December	1,530	870	360	320	1,890	1,190	— 700
	1965 March	1,340	800	450	260	1,790	1,060	— 730
	June	1,280	900	460	320	1,740	1,220	— 520
	September	1,230	1,340	460	380	1,690	1,720	30
	December	1,710	1,570	440	470	2,150	2,040	— 110
	1966 March	1,220	1,280	500	560	1,720	1,840	120
	June	1,230	1,330	460	480	1,690	1,810	120
	September	1,630	1,880	490	630	2,120	2,510	390
	December	1,930	2,090	590	640	2,520	2,730	210

[1] Sterling, Swiss francs, Deutsche Mark, Dutch florins, French francs, Italian lire. [2] Positions vis-à-vis banks only.

Short-term liabilities and assets of ten countries' commercial banks in certain foreign currencies vis-à-vis non-residents (continued).

Countries	End of month	US dollars		Other currencies[1]		Total		
		Liabil-ities	Assets	Liabil-ities	Assets	Liabil-ities	Assets	Net
		in millions of US dollars						
Netherlands. . . .	1963 September	270	360	100[2]	280[2]	370	640	270
	1964 March	280	330	80[2]	220[2]	360	550	190
	September	310	280	150[2]	260[2]	460	540	80
	December	360	390	150[2]	290[2]	510	680	170
	1965 March	360	420	150[2]	300[2]	510	720	210
	June	400	380	180[2]	340[2]	580	720	140
	September	400	360	200[2]	400[2]	600	760	160
	December	530	420	210[2]	400[2]	740	820	80
	1966 March	570	360	290[2]	500[2]	860	860	—
	June	650	450	310[2]	520[2]	960	970	10
	September	670	440	310[2]	450[2]	980	890	— 90
	December	790	550	350[2]	510[2]	1,140	1,060	— 80
Sweden.	1963 September	80	150	40	100	120	250	130
	1964 March	80	180	50	140	130	320	190
	September	110	200	80	170	190	370	180
	December	110	230	50	110	160	340	180
	1965 March	130	180	70	110	200	290	90
	June	150	220	100	130	250	350	100
	September	130	220	100	130	230	350	120
	December	150	260	70	160	220	420	200
	1966 March	140	230	100	150	240	380	140
	June	150	220	100	160	250	380	130
	September	150	230	100	170	250	400	150
	December	190	330	140	200	330	530	200
Switzerland[3] . . .	1963 September	1,060	1,660	290[4]	500[4]	1,350[4]	2,160[4]	810[4]
	1964 March	1,220	1,960	300[4]	500[4]	1,520[4]	2,460[4]	940[4]
	September	1,370	2,110	360	560	1,730	2,670	940
	December	1,590	2,180	330	560	1,920	2,740	820
	1965 March	1,450	2,270	340	510	1,790	2,780	990
	June	1,480	2,360	330	520	1,810	2,880	1,070
	September	1,580	2,380	320	440	1,900	2,820	920
	December	1,700	2,660	360	550	2,060	3,210	1,150
	1966 March	1,490	2,520	360	560	1,850	3,080	1,230
	June	1,760	2,370	260	550	2,020	2,920	900
	September	1,730	2,310	210	470	1,940	2,780	840
	December	1,890	2,780	210	440	2,100	3,220	1,120
United Kingdom. .	1963 September	3,160	2,970	490	510	3,650	3,480	— 170
	1964 March	3,100	2,810	490	540	3,590	3,350	— 240
	September	3,890	3,190	490	640	4,380	3,830	— 550
	December	4,380	3,670	520	660	4,900	4,330	— 570
	1965 March	4,560	3,410	550	720	5,110	4,130	— 980
	June	4,410	3,520	480	690	4,890	4,210	— 680
	September	4,750	4,000	510	740	5,260	4,740	— 520
	December	5,260	4,550	540	790	5,800	5,340	— 460
	1966 March	5,440	4,880	620	850	6,060	5,730	— 330
	June	6,080	5,620	640	900	6,720	6,520	— 200
	September	6,890	6,380	640	930	7,530	7,310	— 220
	December	7,590	7,310	680	900	8,270	8,210	— 60

[1] Sterling, Swiss francs, Deutsche Mark, Dutch florins, French francs, Italian lire. [2] Sterling, Swiss francs and Deutsche Mark only. [3] Including Euro-currency assets of the BIS. [4] Estimates.

Short-term liabilities and assets of ten countries' commercial banks in certain foreign currencies vis-à-vis non-residents (continued).

Countries	End of month	US dollars		Other currencies[1]		Total		
		Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Net
		in millions of US dollars						
Sub-total, eight European countries . . .	1963 September	7,390	7,530	2,680[2]	2,860[2]	10,070[2]	10,390[2]	320[2]
	1964 March	7,130	7,590	2,570[2]	2,600[2]	9,700[2]	10,190[2]	490[2]
	September	8,130	8,040	2,600	2,880	10,730	10,920	190
	December	9,640	9,000	2,570	3,040	12,210	12,040	− 170
	1965 March	9,200	8,920	2,740	2,890	11,940	11,810	− 130
	June	9,140	9,110	2,850	3,180	11,990	12,290	300
	September	9,760	10,140	2,800	3,220	12,560	13,360	800
	December	11,350	11,590	2,820	3,560	14,170	15,150	980
	1966 March	10,480	11,400	3,440	3,950	13,920	15,350	1,430
	June	11,510	12,260	3,320	3,840	14,830	16,100	1,270
	September	13,070	14,060	3,330	3,770	16,400	17,830	1,430
	December	14,720	16,060	3,590	3,850	18,310	19,910	1,600
Canada	1963 September	2,350	2,790	20[3]	130[3]	2,370	2,920	550
	1964 March	2,170	2,360	10[3]	170[3]	2,180	2,530	350
	September	2,440	2,780	40[3]	230[3]	2,480	3,010	530
	December	2,590	3,180	20[3]	200[3]	2,610	3,380	770
	1965 March	2,370	2,770	30[3]	190[3]	2,400	2,960	560
	June	2,220	2,440	30[3]	150[3]	2,250	2,590	340
	September	2,470	2,740	30[3]	120[3]	2,500	2,860	360
	December	2,370	2,670	30[3]	110[3]	2,400	2,780	380
	1966 March	2,040	2,440	30[3]	120[3]	2,070	2,560	490
	June	1,960	2,360	10[3]	90[3]	1,970	2,450	480
	September	1,830	2,490	10[3]	80[3]	1,840	2,570	730
	December	2,150	2,890	10[3]	80[3]	2,160	2,970	810
Japan.	1963 September	1,820	1,660	370	230	2,190	1,890	− 300
	1964 March	2,110	1,780	330	300	2,440	2,080	− 360
	September	2,230	2,020	390	380	2,620	2,400	− 220
	December	2,380	2,210	350	400	2,730	2,610	− 120
	1965 March	2,500	2,290	370	400	2,870	2,690	− 180
	June	2,540	2,470	380	370	2,920	2,840	− 80
	September	2,460	2,600	370	360	2,830	2,960	130
	December	2,550	2,620	360	380	2,910	3,000	90
	1966 March	2,570	2,600	340	340	2,910	2,940	30
	June	2,590	2,640	350	330	2,940	2,970	30
	September	2,460	2,840	340	350	2,800	3,190	390
	December	2,550	2,870	300	380	2,850	3,250	400
Grand total .	1963 September	11,560	11,980	3,070[2]	3,220[2]	14,630[2]	15,200[2]	570[2]
	1964 March	11,410	11,730	2,910[2]	3,070[2]	14,320[2]	14,800[2]	480[2]
	September	12,800	12,840	3,030	3,490	15,830	16,330	500
	December	14,610	14,390	2,940	3,640	17,550	18,030	480
	1965 March	14,070	13,980	3,140	3,480	17,210	17,460	250
	June	13,900	14,020	3,260	3,700	17,160	17,720	560
	September	14,690	15,480	3,200	3,700	17,890	19,180	1,290
	December	16,270	16,880	3,210	4,050	19,480	20,930	1,450
	1966 March	15,090	16,440	3,810	4,410	18,900	20,850	1,950
	June	16,060	17,260	3,680	4,260	19,740	21,520	1,780
	September	17,360	19,390	3,680	4,200	21,040	23,590	2,550
	December	19,420	21,820	3,900	4,310	23,320	26,130	2,810

[1] Sterling, Swiss francs, Deutsche Mark, Dutch florins, French francs, Italian lire. [2] Estimates. [3] All other currencies, but mainly sterling.

Short-term liabilities and assets of ten countries' commercial banks in certain foreign currencies vis-à-vis non-residents, excluding positions vis-à-vis the country of issue of the currency in question.

Countries	End of month	US dollars		Other currencies[1]		Total		
		Liabil-ities	Assets	Liabil-ities	Assets	Liabil-ities	Assets	Net
		in millions of US dollars						
Belgium-Luxemburg . . .	1963 September	280[2]	190[2]	.	.	.	.	.
	1964 March	290[2]	220[2]	.	.	.	.	.
	September	220[2]	230[2]	.	.	.	.	.
	December	330	260	380	60	710	320	− 390
	1965 March	350	310	300	60	650	370	− 280
	June	330	290	400	70	730	360	− 370
	September	420	280	400	60	820	340	− 480
	December	460	350	410	100	870	450	− 420
	1966 March	460	420	460	110	920	530	− 390
	June	410	360	490	110	900	470	− 430
	September	470	430	560	120	1,030	550	− 480
	December	560	560	620	110	1,180	670	− 510
France[3]	1963 September	600	550	350	360	950	930	− 20
	1964 March	590	540	350	320	940	860	− 80
	September	590	530	310	330	900	860	− 40
	December	730	660	400	340	1,130	1,000	− 130
	1965 March	660	660	330	350	990	1,010	20
	June	650	620	310	360	960	980	20
	September	760	740	340	360	1,100	1,100	—
	December	940	1,010	360	370	1,300	1,380	80
	1966 March	680	910	430	410	1,110	1,320	210
	June	680	1,050	420	360	1,100	1,410	310
	September	940	1,150	450	380	1,390	1,530	140
	December	1,230	1,270	430	360	1,660	1,630	− 30
Germany	1963 September	220	300	50	20	270	320	50
	1964 March	190	290	50	20	240	310	70
	September	260	190	50	20	310	210	− 100
	December	390	160	40	10	430	170	− 260
	1965 March	190	160	20	20	210	180	− 30
	June	200	190	30	10	230	200	− 30
	September	220	190	30	10	250	200	− 50
	December	310	230	30	10	340	240	− 100
	1966 March	240	290	20	10	260	300	40
	June	260	310	20	10	280	320	40
	September	290	470	20	10	310	480	170
	December	260	260	20	10	280	270	− 10
Italy	1963 September	1,420	570	440	230	1,860	800	−1,060
	1964 March	1,060	450	330	140	1,390	590	− 800
	September	1,010	460	200	120	1,210	580	− 630
	December	1,250	600	210	150	1,460	750	− 710
	1965 March	1,030	640	250	110	1,280	750	− 530
	June	990	760	260	160	1,250	920	− 330
	September	940	1,200	260	190	1,200	1,390	190
	December	1,420	1,370	250	200	1,670	1,570	− 100
	1966 March	960	1,110	280	270	1,240	1,380	140
	June	980	1,140	260	280	1,240	1,420	180
	September	1,380	1,670	340	310	1,720	1,980	260
	December	1,700	1,870	390	390	2,090	2,260	170

[1] Sterling, Swiss francs, Deutsche Mark, Dutch florins, French francs, Italian lire. [2] Estimates. [3] Positions vis-à-vis banks only.

Short-term liabilities and assets of ten countries' commercial banks in certain foreign currencies vis-à-vis non-residents, excluding positions vis-à-vis the country of issue of the currency in question (continued).

Countries	End of month	US dollars		Other currencies[1]		Total		
		Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Net
		in millions of US dollars						
Netherlands	1963 September	230	250	40[2]	50[2]	270	300	30
	1964 March	240	230	40[2]	40[2]	280	270	— 10
	September	270	190	60[2]	50[2]	330	240	— 90
	December	320	300	100[2]	100[2]	420	400	— 20
	1965 March	300	340	100[2]	110[2]	400	450	50
	June	360	300	100[2]	120[2]	460	420	— 40
	September	370	270	130[2]	110[2]	500	380	— 120
	December	470	340	140[2]	90[2]	610	430	— 180
	1966 March	480	280	190[2]	140[2]	670	420	— 250
	June	570	350	190[2]	150[2]	760	500	— 260
	September	600	350	190[2]	160[2]	790	510	— 280
	December	720	470	220[2]	170[2]	940	640	— 300
Sweden	1963 September	70	100	10	20	80	120	40
	1964 March	70	90	10	30	80	120	40
	September	80	120	10	30	90	150	60
	December	80	140	30	20	110	160	50
	1965 March	90	110	40	30	130	140	10
	June	110	140	50	40	160	180	20
	September	110	120	50	40	160	160	—
	December	120	170	50	40	170	210	40
	1966 March	120	130	50	30	170	160	— 10
	June	120	140	50	30	170	170	—
	September	130	170	60	30	190	200	10
	December	160	240	60	50	220	290	70
Switzerland[3] . . .	1963 September	920	1,330	.	.	.	.	.
	1964 March	1,060	1,530	.	.	.	.	.
	September	1,210	1,710	200	90	1,410	1,800	390
	December	1,440	1,610	180	120	1,620	1,730	110
	1965 March	1,290	1,800	150	70	1,440	1,870	430
	June	1,310	1,850	140	80	1,450	1,930	480
	September	1,420	1,840	160	110	1,580	1,950	370
	December	1,550	2,160	170	90	1,720	2,250	530
	1966 March	1,320	2,070	160	110	1,480	2,180	700
	June	1,590	1,850	170	150	1,760	2,000	240
	September	1,570	1,830	120	130	1,690	1,960	270
	December	1,750	2,300	130	140	1,880	2,440	560
United Kingdom .	1963 September	2,800	1,970	.	.	.	.	.
	1964 March	2,780	1,740	.	.	.	.	.
	September	3,400	2,010	.	.	.	.	.
	December	3,840	2,460	.	.	.	.	.
	1965 March	4,080	1,950	.	.	.	.	.
	June	3,910	2,090	.	.	.	.	.
	September	4,230	2,320	.	.	.	.	.
	December	4,710	2,950	.	.	.	.	.
	1966 March	4,770	2,660	.	.	.	.	.
	June	5,210	3,150	.	.	.	.	.
	September	5,890	3,280	.	.	.	.	.
	December	6,640	3,830	.	.	.	.	.

[1] Sterling, Swiss francs, Deutsche Mark, Dutch florins, French francs, Italian lire. [2] Sterling, Swiss francs and Deutsche Mark only. [3] Including Euro-currency assets of the BIS.

Short-term liabilities and assets of ten countries' commercial banks in certain foreign currencies vis-à-vis non-residents, excluding positions vis-à-vis the country of issue of the currency in question (continued).

Countries	End of month	US dollars		Other currencies[1]		Total		
		Liabil-ities	Assets	Liabil-ities	Assets	Liabil-ities	Assets	Net
		in millions of US dollars						
Sub-total, eight European countries . . .	1963 September	6,540[2]	5,260[2]	.	.	.	.	.
	1964 March	6,280[2]	5,090[2]	.	.	.	.	.
	September	7,040[2]	5,440[2]	.	.	.	.	.
	December	8,380	6,190	.	.	.	.	.
	1965 March	7,970	5,970	.	.	.	.	.
	June	7,860	6,240	.	.	.	.	.
	September	8,470	6,960	.	.	.	.	.
	December	9,980	8,580	.	.	.	.	.
	1966 March	9,030	7,870	.	.	.	.	.
	June	9,820	8,350	.	.	.	.	.
	September	11,270	9,350	.	.	.	.	.
	December	13,020	10,800	.	.	.	.	.
Canada	1963 September	890	760	10[3]	40[3]	900	800	— 100
	1964 March	860	620	10[3]	30[3]	870	650	— 220
	September	860	890	10[3]	40[3]	870	930	60
	December	910	1,210	20[3]	30[3]	930	1,240	310
	1965 March	1,010	1,010	30[3]	30[3]	1,040	1,040	—
	June	1,110	760	20[3]	30[3]	1,130	790	— 340
	September	1,380	810	20[3]	30[3]	1,400	840	— 560
	December	1,390	900	30[3]	40[3]	1,420	940	— 480
	1966 March	1,190	840	30[3]	40[3]	1,220	880	— 340
	June	1,180	830	10[3]	40[3]	1,190	870	— 320
	September	1,120	800	—[3]	40[3]	1,120	840	— 280
	December	1,450	930	—[3]	40[3]	1,450	970	— 480
Japan	1963 September	300	300	.	.	.	.	.
	1964 March	250	340	.	.	.	.	.
	September	330	510	100	240	430	750	320
	December	350	550	100	260	450	810	360
	1965 March	380	550	100	230	480	780	300
	June	360	570	120	220	480	790	310
	September	380	690	120	220	500	910	410
	December	390	690	100	230	490	920	430
	1966 March	430	680	100	210	530	890	360
	June	480	720	80	190	560	910	350
	September	560	780	70	210	630	990	360
	December	610	790	70	230	680	1,020	340
Grand total .	1963 September	7,730[2]	6,320[2]	.	.	.	.	.
	1964 March	7,390[2]	6,050[2]	.	.	.	.	.
	September	8,230[2]	6,840[2]	.	.	.	.	.
	December	9,640	7,950	.	.	.	.	.
	1965 March	9,360	7,530	.	.	.	.	.
	June	9,330	7,570	.	.	.	.	.
	September	10,230	8,460	.	.	.	.	.
	December	11,760	10,170	.	.	.	.	.
	1966 March	10,650	9,390	.	.	.	.	.
	June	11,480	9,900	.	.	.	.	.
	September	12,950	10,930	.	.	.	.	.
	December	15,080	12,520	.	.	.	.	.

[1] Sterling, Swiss francs, Deutsche Mark, Dutch florins, French francs, Italian lire. [2] Estimates. [3] All other currencies, but mainly sterling.

V. THE EUROPEAN MONETARY AGREEMENT.

The European Monetary Agreement (EMA), which came into force on 27th December 1958, serves as a framework for co-operation between the monetary authorities of Contracting Parties, with the broad objective of encouraging multilateralism in international trade and currency convertibility. Its two principal operational aspects are: the European Fund, from which members may receive short or medium-term balance-of-payments assistance, and the Multilateral System of Settlements, under which each member country's central bank is assured of obtaining settlement in dollars of its holdings of other members' currencies at an exchange rate known in advance. The Agreement is operated by the Council of the Organisation for Economic Co-operation and Development (OECD) and a Board of Management. The Bank for International Settlements, acting as Agent, is entrusted with the execution of all financial operations under the Agreement.

Modification of the Agreement.

Following a comprehensive review during 1965, the Agreement was renewed for a period of three years until the end of 1968. A number of amendments to the Agreement, described in last year's Annual Report, arose out of this review, including provision for an alternative and more rapid procedure for the granting of credits from the European Fund through delegation to the Board of Management of authority to grant credits of not more than $50 million* each for periods of up to one year.

Particularly in the light of this new facility, it is desirable that the European Fund should have ready access to additional funds when existing liquid assets are temporarily inadequate to meet a drawing on a credit granted by the Board. Supplementary finance would normally be obtained by a general call-up of unpaid capital contributions from Contracting Parties and by drawing upon the capital of the former European Payments Union (EPU). An additional method of financing was provided for in 1960, when the articles of the Agreement were amended to permit the European Fund to receive special credits from Contracting Parties. In practice it has proved unnecessary to raise additional finance by this alternative method, but it has more recently been felt that, should the occasion arise, it might involve protracted negotiation. Accordingly, in May 1967, the Board of Management proposed to the Council further amendments to the Agreement which would allow the European Fund to obtain short-term credits from international financial institutions situated within the territory of a Contracting Party. It was further proposed that authority to obtain such credits, to a total outstanding of up to

* 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.

$50 million and for a maximum period of one year, be delegated to the Board of Management. The Bank for International Settlements, having been approached by the Secretary General of the OECD, has indicated its readiness in principle to co-operate in such financing subject to agreement being reached in each particular case. At the end of May 1967 the proposals were still before the Council.

Operations under the Agreement.

European Fund. The table below sets out the credits granted from the European Fund which were outstanding during the year April 1966 to March 1967, together with the rates of interest and service charges applied to them. No new credits were granted during this period.

EMA: Credits granted from the European Fund in the fiscal year ended March 1967.

Credits	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 since 31st March 1966				
Turkey (4th credit; balance) . . .	10.0	15th March 1963 to dates below*	3.50	0.25
	15.0	30th June 1963 to dates below*		
Credits available at 31st March 1967				
Turkey (6th credit)	20.0	31st March 1965 to dates below*	3.75	0.25
	25.0	30th July 1965 to dates below*		
	5.0	29th October 1965 to dates below*		
	15.0	15th March 1966 to dates below*		
	5.0	31st October 1966 to dates below*		
Greece	30.0	8th February 1966 to dates below*	*3.875*	*0.25*

* The balance of the fourth credit to Turkey was repayable as follows: 15 million on 31st October 1966 and 10 million on 15th March 1967. The sixth credit to Turkey is repayable as follows: ten instalments of 5 million each on 30th June and 31st December 1968, 31st March, 30th June, 30th September and 31st December 1969, and 31st March, 31st May, 29th July and 28th October 1970; one instalment of 15 million on 14th March 1971; and one instalment of 5 million on 30th October 1971. The credit to Greece is repayable as follows: 5 million on 7th February 1969, 10 million on 7th February 1970 and 15 million on 7th February 1971.

At the end of March 1966 credits totalling $120 million were outstanding. Of this amount, $90 million represented the balance of the fourth credit and the first four tranches of the sixth credit to Turkey, and the remaining $30 million represented the credit to Greece granted in February 1966 and fully drawn since 9th March 1966.

With effect from 31st October 1966, the Board of Management released the final tranche of $5 million of the sixth credit to Turkey. This amount was promptly drawn and used to refinance a part of the $15 million third instalment of the fourth credit which was due for repayment on the same date. On 15th March 1967 Turkey repaid the final instalment of $10 million of the fourth credit in cash. These transactions reduced Turkey's indebtedness to the European Fund in respect of credits to $70 million by the end of March 1967 and the total of credits outstanding to $100 million.

In the light of an anticipated balance-of-payments deficit in 1967 and of the critically low level of Turkey's official reserves the Council on 23rd May 1967 decided to grant a further credit to that country with effect from 1st June 1967, for an amount of $25 million. The conditions governing the repayment of this new credit are closely comparable with those accorded to Greece in February 1966. A sum of $5 million is repayable at the end of the third year, a further $5 million at the end of the fourth year, and the balance of $15 million at the end of the fifth year. These terms represent the maximum period allowable under the Agreement.

The table on the utilisation of credits granted shows the position at the value date for multilateral settlements (the fifth working day of the following month) for February 1959, when the first credits were granted, for the end

EMA: Utilisation of credits granted from the European Fund.

At value date for settlements for month	Greece		Iceland		Spain		Turkey		Totals		
	Available and undrawn	Drawings outstanding	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
December. . . .	—	—	—	—	51.0	24.0	0.5	21.0	51.5	45.0	96.5
1960											
December. . . .	—	—	5.0	7.0	76.0	24.0	15.0	21.5	96.0	52.5	148.5
1961											
December. . . .	—	—	7.0	5.0	—	—	—	50.0	7.0	55.0	62.0
1962											
December. . . .	—	—	5.0	—	—	—	—	80.0	5.0	80.0	85.0
1963											
December. . . .	—	—	—	—	—	—	—	95.0	—	95.0	95.0
1964											
December. . . .	—	—	—	—	—	—	—	105.0	—	105.0	105.0
1965											
January	—	—	—	—	—	—	—	100.0	—	100.0	100.0
February	—	—	—	—	—	—	—	95.0	—	95.0	95.0
October	—	—	—	—	—	—	—	90.0	—	90.0	90.0
1966											
February	25.0	5.0	—	—	—	—	—	90.0	25.0	95.0	120.0
March	—	30.0	—	—	—	—	—	90.0	—	120.0	120.0
October	—	30.0	—	—	—	—	—	80.0	—	110.0	110.0
1967											
March	—	30.0	—	—	—	—	—	70.0	—	100.0	100.0

of each year from 1959 to 1964, and for each month from end-1964 to March 1967 in which changes occurred.

There was no call-up of capital in the period under review, so that the amount of contributions paid in remained unchanged at $38 million. Together with $148 million from the former EPU capital, this leaves the active capital of the Fund at $186 million, while uncalled capital remains at $421 million.

Multilateral System of Settlements. No amounts of interim finance were drawn during the year under review. Buying and selling rates notified by member countries for their currencies remained unchanged and no balances were brought into the Multilateral System of Settlements.

Since the coming into force of the EMA, payments to or by the European Fund in respect of the multilateral settlements have totalled $37.8 million.

Management of the European Monetary Agreement.

The Board of Management of the EMA supervises the execution of the Agreement and advises the Council of the OECD on all related matters. The Board also follows the economic and financial situation in member countries on the basis of reports made by the Secretariat or by the various committees of the Organisation and, on occasion, by special missions. In discharging these functions the Board meets when necessary, recently about six times a year. In December 1966 the Council re-appointed M. Hay as Chairman of the Board for a further year.

The Bank for International Settlements, as Agent, presents monthly reports on the operations carried out under the Agreement and on the investments of the European Fund, and also provides the Board with monthly statistical material on the international gold and foreign exchange markets and on the evolution of the external monetary position of OECD countries.

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 amounted at the beginning of operations to $35 million, representing long-term claims on Norway and Turkey transferred from the EPU, stood at a peak of $143.1 million at end-March 1966, of which $120 million represented credits drawn and outstanding and $23.1 million the balance of the long-term claims on Norway and Turkey. The total was unchanged until the end of October, when it fell to $133.1 million as the result of the net repayment by Turkey described above. In December the sixth amortisation payment of the long-term claims on Norway and Turkey reduced the total by a further $2.6 million, and with the repayment by Turkey in March of the final $10 million outstanding from the fourth credit the sum of credits and claims outstanding declined to $120.5 million.

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

At value date for settlements 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 December	82.1	123.5	297.9	123.1	626.6	607.5	19.1
1964 December	79.3	123.5	297.9	130.6	631.4	607.5	23.9
1965 December	101.3	123.5	297.9	113.1	635.8	607.5	28.3
1966 January	100.9	123.5	297.9	113.1	635.4	607.5	27.9
February	96.0	123.5	297.9	118.1	635.5	607.5	28.0
March	71.1	123.5	297.9	143.1	635.6	607.5	28.1
April	71.2	123.5	297.9	143.1	635.8	607.5	28.3
May	71.3	123.5	297.9	143.1	635.9	607.5	28.4
June	73.4	123.5	297.9	143.1	638.0	607.5	30.5
July	73.1	123.5	297.9	143.1	637.7	607.5	30.2
August	73.2	123.5	297.9	143.1	637.8	607.5	30.3
September	73.4	123.5	297.9	143.1	638.0	607.5	30.5
October	83.7	123.5	297.9	133.1	638.3	607.5	30.8
November	83.9	123.5	297.9	133.1	638.4	607.5	30.9
December	89.4	123.5	297.9	130.5	641.3	607.5	33.8
1967 January	88.9	123.5	297.9	130.5	640.9	607.5	33.4
February	89.1	123.5	297.9	130.5	641.1	607.5	33.6
March	99.2	123.5	297.9	120.5	641.2	607.5	33.7

This decline of $22.6 million in the Fund's non-liquid assets during the year to end-March 1967 was more than matched by the growth in liquid resources from a level of $71.1 million at the end of March 1966 to $99.2 million a year later. The balance of $5.5 million of the increase in liquid assets reflects the further rise in undistributed net income.

The calculation of interest payable on paid-up contributions to the Fund's capital was again based on the principle adopted in previous years, whereby the cumulative amount of interest paid to each member country represents 90 per cent. of its share in the Fund's net income which the country would have received if the Fund had been liquidated at the end of the period in respect of which interest is paid. Net income during 1966 was the highest for any year since the Fund was established, partly because of the high level of credits outstanding and partly reflecting higher yields on the Fund's short-term dollar investments. As a result, the interest on contributions for the year as a whole reached $1.0 million, bringing the cumulative amount of interest so far paid to member countries to $6.4 million.

PART III

ACTIVITIES OF THE BANK.

1. Operations of the Banking Department.

The balance sheet of the Bank as at 31st March 1967, certified by the auditors, is reproduced at the end of the present Report. The following two changes have been made in the presentation.

On the one hand, in connection with the settlement of the Bank's investments in Germany two temporary items appeared in the balance sheet as at 31st March 1966: "Claim in respect of the Arrangement dated 29th November 1965 with the Federal Republic of Germany" on the assets side and "Claims of Governments in respect of the Annuity Trust Account" on the liabilities side. The settlement having been effected in April 1966, these items immediately lapsed and hence do not figure in the balance sheet as at 31st March 1967.

On the other hand, the item "Provision for contingencies" has been split into two following the creation of a "Provision for building purposes", which will be discussed in Section 6 below: "Net profits and their distribution".

* * *

The balance-sheet total as at 31st March 1967 amounted to 8,231,996,517 francs,* against 7,881,659,477 on 31st March 1966, showing an increase of 350,337,040 francs. The total of the monthly statement of account fluctuated fairly widely during the financial year; thus, at the end of May 1966 it declined to 7,282 million and at the end of December 1966, at 9,098 million, it for the first time exceeded the 9 milliard level.

BIS: Development of the balance-sheet total.

Financial years ended 31st March	Total of balance sheet	Movement
	in millions of francs	
1963	4,950[1]	+ 218
1964	5,778[1]	+ 828
1965	7,850[1]	+ 2,072
1966	7,882	+ 32
1967	8,232	+ 350

[1] First section.

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

* 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.

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 1966, 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 below.

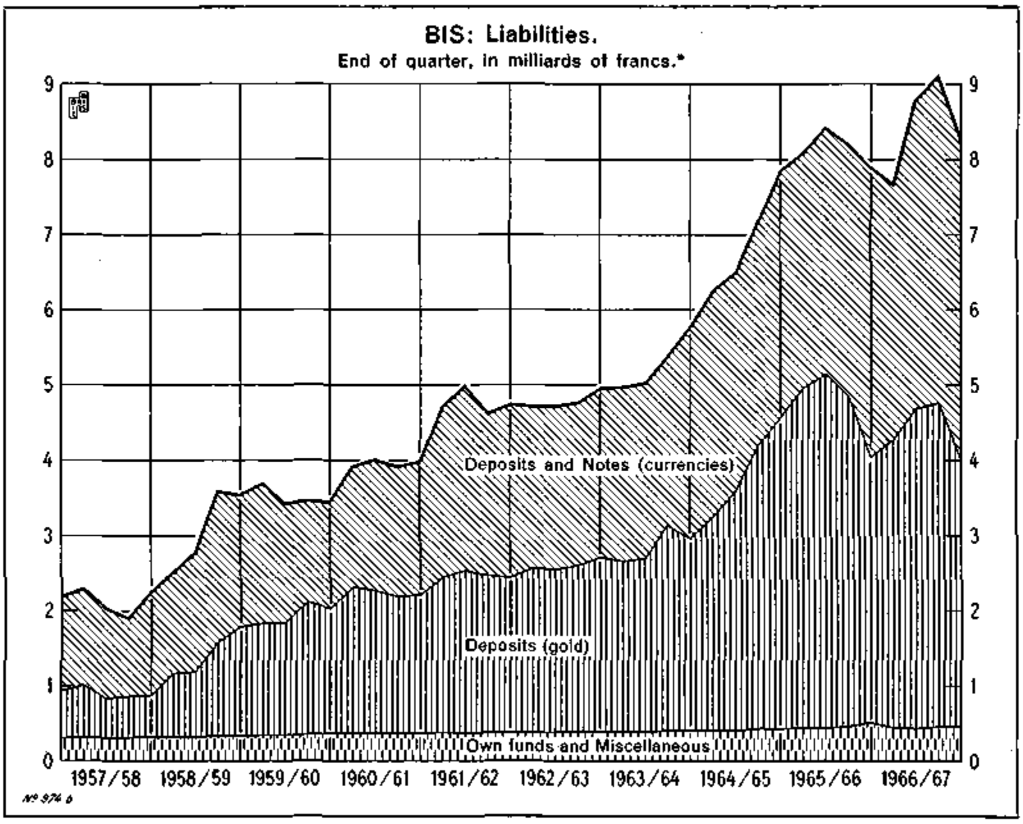
BIS: Memorandum accounts (b).

Items	Financial years ended 31st March 1966	1967
	in millions of francs	
Earmarked gold	1,145	1,233
Bank balances	32	26
Bills and other securities	715	678
Total of items not included in the balance sheet	1,892	1,937

Composition of resources (liabilities).

A. Own funds.

The "Capital authorised and issued" remained unchanged at 500 million francs, of which 125 million was paid up.



* Total of first part of statement of account up to and including 31st December 1965; thereafter total of statement of account.

The Bank's reserves, at 25.8 million, also showed no change, the Legal Reserve Fund and the General Reserve Fund remaining unaltered.

The balance of the Profit and Loss Account, which comprises the net profit for the financial year ended 31st March 1967 and the balance brought forward from the preceding year, amounted to 41.9 million on 31st March 1967, against 32.3 million a year earlier. The "Provision for contingencies", which had stood at 216.2 million on 31st March 1966, was replaced as at 31st March 1967 by a "Provision" consisting of two sub-items, which together totalled 231 million. The figures just given are commented on in Section 6: "Net profits and their distribution".

The item "Miscellaneous" rose from 33.3 million on 31st March 1966 to 44.1 million on 31st March 1967.

At the end of March 1967 the Bank's own funds ("Miscellaneous" included) amounted to 468 million francs, i.e. 6 per cent. of its borrowed funds (7,764 million) and 5.7 per cent. of the balance-sheet total (8,232 million). If the non-paid-up capital (375 million) were included in the Bank's own funds, the ratios would be roughly 11 per cent. and 10 per cent. respectively.

The following table gives a break-down of the Bank's resources (not including the non-paid-up capital), in absolute terms and in percentages, as 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	Ratio of own funds to balance-sheet total
	in millions of francs			in percentages	
1963	389	4,561	4,950*	8.5	7.9
1964	408	5,370	5,778*	7.6	7.1
1965	433	7,417	7,850*	5.8	5.5
1966	433	7,449	7,882	5.8	5.5
1967	468	7,764	8,232	6.0	5.7

* First section of the balance sheet.

B. Borrowed funds.

The following tables show the origin, nature and term of the Bank's resources.

BIS: Resources, by origin.

Origin	Financial years ended 31st March 1966*	1967	Movement
	in millions of francs		
Central banks	6,104	6,602	+ 498
Other depositors	901	869	— 32
Notes	362	293	— 69
Total	7,367	7,764	+ 397

* Not including "Claims of Governments in respect of the Annuity Trust Account".

The deposits of central banks showed a moderate increase of about 8 per cent.; those of other depositors decreased very slightly. The item "Notes", which represents notes issued by the Bank in currencies in favour of commercial banks, showed a reduction of some 20 per cent., since the monetary policy aims underlying the issue of such paper on certain markets were no longer applicable.

BIS: Resources, by nature and term.

Term	Deposits in gold			Deposits in currencies			Notes		
	Financial years ended 31st March		Movement	Financial years ended 31st March		Movement	Financial years ended 31st March		Movement
	1966	1967		1966*	1967		1966	1967	
	in millions of francs								
Sight	2,484	2,593	+ 109	184	240	+ 56	—	—	—
Not exceeding 3 months	591	325	— 266	2,816	3,282	+ 466	346	291	— 55
Between 3 and 6 months	102	164	+ 62	380	309	— 71	16	2	— 14
Between 6 and 9 months	272	338	+ 66	17	53	+ 36	—	—	—
Between 9 and 12 months	90	141	+ 51	45	10	— 35	—	—	—
Over 1 year	—	—	—	24	16	— 8	—	—	—
Total	3,539	3,561	+ 22	3,466	3,910	+ 444	362	293	— 69

* Not including "Claims of Governments in respect of the Annuity Trust Account".

Deposits in gold remained practically unchanged over the financial year, whereas those in currencies rose by 13 per cent.

As far as gold deposits are concerned, sight accounts showed little variation during the year; at the end of the year they were slightly higher than at the beginning. Time deposits, in contrast, were a little lower at the year-end and had fluctuated sharply at various times in the course of the year; between the end of February and the end of March 1967, for example, they fell by almost half. These fluctuations were attributable in particular to the conclusion of swaps under which gold sold spot and purchased forward by the Bank was left on deposit with it for the duration of the operations. At the same time there was a shift in the distribution of deposits according to term, about two-thirds of the decrease in accounts at less than three months being offset by an increase in funds at longer term — between three and twelve months. The ratio of time accounts to total gold deposits was a little lower at the end of the financial year than at the beginning — 27 per cent. against 30 per cent.

With regard to resources in currencies, the rise in deposits was the result of an increase in funds at not exceeding three months. The movements during the year in this category of deposit were largely connected with swaps under which currency sold spot by the Bank was sometimes entrusted to it for short periods. These operations included swaps carried out under the arrangement concluded in June 1966 in which a number of central banks and the Bank participated. This arrangement, which was renewed in March 1967, had as its object the further strengthening of sterling. Other deposits in currencies underwent little change, at least in absolute figures: rises occurred in sight accounts and in funds at between six and nine months and declines in deposits at between three and six months and at over nine months. It should be noted, however, that sight deposits fluctuated very sharply during the year (the minimum was 32 million and the maximum 1,268 million, the latter figure having been reached as a result of various swaps concluded by the Bank of which the countervalue was credited to sight accounts in its books).

At the beginning of the financial year the Bank's resources were almost evenly divided between gold deposits (48 per cent.) and currency deposits (47 per cent.), while the remaining 5 per cent. consisted of notes; on 31st March 1967 these percentages were 46, 50 and 4 respectively.

EMPLOYMENT OF RESOURCES (assets).

BIS: Distribution by nature of total cash holdings and investments.

Nature	Financial years ended 31st March 1966		1967		Movement	
	in millions of francs					
Cash						
Gold	3,025		3,096		+ 71	
Currencies	381	3,406	156	3,252	— 225	— 154
Investments						
Gold	423		420		— 3	
Currencies*	3,924	4,347	4,559	4,979	+ 635	+ 632
Total						
Gold	3,448		3,516		+ 68	
Currencies*	4,305	7,753	4,715	8,231	+ 410	+ 478

* Not including the "Claim in respect of the Arrangement dated 29th November 1965 with the Federal Republic of Germany".

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.

BIS: Gold position.

End of month	Spot position: Gold in bars and coins	Spot position: Investments in gold	Spot position: Deposits in gold	Spot position: Net balance	Forward operations: Net balance	Final net gold position
	in millions of francs					
1966						
March	3,025	423	3,539	— 91	+ 439 (min.)	348 (min.)
May	2,824	424	3,360 (min.)	— 112	+ 479	367
July	2,527	426 (max.)	4,181	—1,228	+1,607	379
August	2,520 (min.)	426	4,133	—1,187	+1,576	389
December	2,583	422	4,303	—1,298 (min.)	+1,712 (max.)	414
1967						
January	3,095	419 (min.)	4,353	— 839	+1,257	418
February	3,053	420	4,359 (max.)	— 886	+1,308	422
March	3,096 (max.)	420	3,561	— 45 (max.)	+ 472	427 (max.)
Movement: 31st March 1966 to 31st March 1967	+ 71	— 3	+ 22	+ 46	+ 33	+ 79

The figures at the end of the financial year for the various items constituting the Bank's gold position were little changed from those at the end of the previous financial year.

The increase in spot assets in the form of cash gold holdings and investments — 68 million — would have been even greater had not the balance of forward operations risen at the same time by 33 million.

The final net gold position was affected in particular by the conversion into gold of the funds accruing to the Bank as a result of the settlement of the investments made by it in Germany under the Hague Agreements of 1930.

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 item "Gold in bars and coins" (which consisted mainly of gold in bars) has been commented upon above.

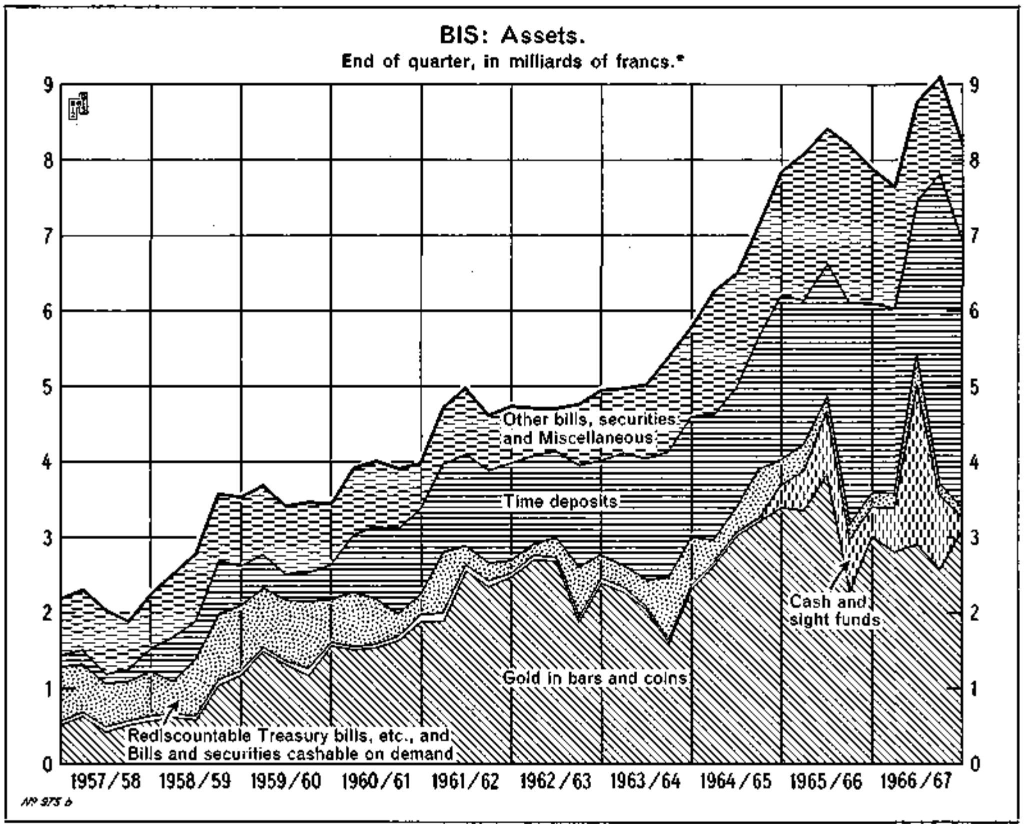
At the beginning of the financial year the figure for the item "Cash on hand and on sight account with banks" stood at 381 million. It then registered very wide fluctuations, declining to 76 million on 31st May, rising to 2,104 million on 30th September 1966 (the maximum for the financial year) and then falling back to 156 million on 31st March 1967. These movements were almost entirely connected with various swaps, some against gold and others against currencies, which furnished the Bank with very substantial sight funds.

On 31st March 1967 total cash holdings (gold and currencies) represented 39.5 per cent. of the total of the Bank's balance sheet, compared with 43 per cent. a year earlier.

The figure for the item "Rediscountable Treasury bills" was almost the same at the end of the financial year as it had been at the beginning, the respective totals being 70 million and 68 million. On two occasions during the financial year the figure for this item rose to nearly 300 million following the investment of funds obtained through the swap network set up among central banks, in which the Bank participates.

The item "Bills and securities cashable on demand" declined from 124 to 74 million.

At the beginning of the financial year the total of the Bank's sight funds and rediscountable investments, comprising the asset items so far analysed, was thus 3,598 million francs and represented 46 per cent. of the total of the balance sheet; on 31st March 1967 the corresponding figures were 3,396 million and 41 per cent. Over the same period the percentage of sight deposits on the liabilities side remained unchanged at 34 per cent. Thus, the Bank's liquidity ratio, although slightly lower, was still at a high level.



* Total of first part of statement of account up to and including 31st December 1965; thereafter total of statement of account.

B. Time deposits and investments.

Very wide fluctuations occurred in the figure for the item "Time deposits and advances". From its level of 2,507 million at the beginning of the financial year the total gradually declined until the end of September 1966, when it stood at 2,030 million, its lowest level for the year, and then rose again, reaching its maximum of 4,108 million on 31st December 1966. By the end of January 1967 it had fallen back to 3,449 million, and it closed the financial year at the level — still a high one — of 3,551 million, 1,044 million above that of a year earlier.

These wide-scale movements were due firstly to the fact that the Bank obtained large amounts of funds at certain times during the year as a result of operations carried out within the framework of central-bank co-operation or of spot gold sales covered by corresponding forward purchases; secondly, to the transfer of sight investments to "Time deposits and advances" as and when deposits placed with the Bank were switched from sight accounts to time accounts; and thirdly, to the reduction in the total of the item "Other bills and securities".

Indeed, in contrast to what had often been the pattern in previous years, the movements in the item "Other bills and securities" frequently diverged from and were less marked than those in "Time deposits and advances". From 1,648 million at the beginning of the financial year, which was nearly its maximum, the total gradually fell to 1,187 million on 30th November, but then from the end of December onwards it remained fairly steady at the level at which it closed the financial year, viz. 1,284 million. The decline over the year thus amounted to 364 million.

The following table shows the composition according to term of the Bank's time investments as at the end of the last two financial years.

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

Periods	Financial years ended 31st March 1966	1967	Movement
	in millions of francs		
Not exceeding 3 months	3,062	3,805	+ 743
Between 3 and 6 months	576	499	− 77
Between 6 and 9 months	228	254	+ 26
Between 9 and 12 months	147	248	+ 101
Over 1 year	142	29	− 113
Total	4,155	4,835	+ 680

The overall increase in investments in the form of time deposits and advances and other bills and securities was more than accounted for by the rise in funds invested at less than three months. The total of the funds invested at more than six months remained practically unchanged; the almost complete liquidation of investments at over one year was roughly offset by the increase in investments at between six and twelve months. Hence there was a shortening of the average term of the Bank's time investments taken as a whole. Finally, it should be noted that, as in the past few years, a substantial proportion of these funds was in fact mobilisable at very short notice.

* * *

Apart from the increase in time deposits in currencies entrusted to the Bank by central banks, there was no fundamental change during the financial year in the volume or composition of borrowed resources.

As in preceding years, the main feature of the Bank's activity was the growing volume of swaps — of gold against currencies or of currencies against currencies — concluded with central banks.

These swaps, carried out within the framework of monetary co-operation between central banks, enabled the Bank to play an active and increasing part in the development of such co-operation, particularly in connection with the arrangement concluded in June 1966.

Furthermore, the Bank obtained by some of these swaps the necessary resources to serve as an intermediary between the monetary authorities and the market. It was thereby able to help to a certain extent and at certain times (especially at the end of December) to relieve tension caused by the large-scale repatriation of funds by commercial banks and by so doing damped down the rise in interest rates on the Euro-dollar market.

The total volume of the Bank's operations reached a new record level, amounting to 110 milliard in 1966–67, against 86 milliard in 1965–66 and 72 milliard in 1964–65.

The net profit for the past financial year was appreciably higher than that for the previous financial year. While partly attributable to the rise in the funds received in the form of deposits, the increase was due even more to the larger volume of resources obtained by way of swaps and the widening of profit margins resulting from the development of interest rates on the markets in the first nine months of the financial year.

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

In conformity with the agreements in force, the Bank continued in the year under review 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 1966–67 ended for the Dawes Loan on 15th April 1967 and for the Young Loan on 1st June 1967. The interest in respect of the financial year 1966–67 amounted to the equivalent of about 11.5 million francs for the Dawes Loan and of about 35.7 million francs for the Young Loan; it was duly paid to the Bank and distributed by the latter among the Paying Agents. Redemption of the Dawes Loan was effected in respect of the financial year 1966–67 partly by purchases of bonds on the market and partly by drawings; redemption of the Young Loan was effected entirely by purchases of bonds on the market.

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 in 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 as 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 1958-59 to 1965-66	1966-67	Balance after redemption
		Conversion bonds			
American . . .	$	44,107,000	13,084,000	2,045,000	28,978,000
Belgian	£	583,200	123,600	18,400	441,200
British	£	8,277,200	1,752,400	264,300	6,260,500
Dutch.	£	1,323,000	262,100	42,200	1,018,700
French	£	1,929,600	403,500	61,200	1,464,900
Swedish . . .	S.kr.	14,209,000	2,782,000	428,000	10,999,000
Swiss	£	1,130,500	235,300	36,800	858,400
Swiss	Sw.fr.	8,251,000	1,581,000	244,000	6,426,000
		Funding bonds			
American . . .	$	8,206,000	1,886,000	244,000	6,076,000
Belgian	£	157,800	37,700	5,000	115,100
British	£	2,232,000	525,700	70,700	1,635,600
Dutch.	£	291,400	61,400	9,000	221,000
French	£	498,900	118,700	15,800	364,400
Swiss	£	115,000	26,600	3,600	84,800
Swiss	Sw.fr.	415,000	90,000	11,000	314,000

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 1958-59 to 1965-66	1966-67	Balance after redemption
		Conversion bonds			
American . . .	$	55,466,000	5,326,000	824,000	49,316,000
Belgian	B.fr.	202,769,000	19,371,000	2,924,000	180,474,000
British	£	17,703,000	1,676,300	254,700	15,772,000
Dutch.	Fl.	52,487,000	4,875,000	755,000	46,857,000
French	Fr.fr.	445,555,000	42,160,000	6,442,000	396,953,000
German	DM	14,504,000	1,363,000	210,000	12,931,000
Swedish . . .	S.kr.	92,763,000	8,824,000	1,341,000	82,598,000
Swiss	Sw.fr.	58,383,000	5,566,000	841,000	51,976,000
		Funding bonds			
American . . .	$	9,004,000	855,000	127,000	8,022,000
Belgian	B.fr.	45,662,000	4,402,000	657,000	40,603,000
British	£	4,223,900	402,500	59,200	3,762,200
Dutch.	Fl.	8,488,000	800,000	124,000	7,564,000
French	Fr.fr.	98,140,000	9,160,000	1,401,000	87,579,000
German	DM	416,000	39,000	6,000	371,000
Swedish . . .	S.kr.	6,014,000	580,000	86,000	5,348,000
Swiss	Sw.fr.	1,405,000	133,000	19,000	1,253,000

* Nominal value on 1st May 1967 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 and for those coupons of the loan which the Federal Republic of Germany has undertaken to pay to the extent of 75 per cent. of the nominal value. In both cases the service was carried out in conformity with the relevant agreements.

The following table shows the position as regards the assented bonds of the loan and their redemption.

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 1965	1966	
American . . .	$	1,667,000	459,000	79,000	1,129,000
Anglo-Dutch .	£	856,600	231,200	38,600	586,800
Swiss	Sw.fr.	7,102,000	1,610,000	276,000	5,216,000

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

The total amount of these secured loans was originally equivalent to about 817 million francs. Repayments by the High Authority up to 1st April 1967 amounted to the equivalent of about 289 million francs, so that the total amount outstanding was reduced to the equivalent of about 528 million francs. Further particulars of these loans are given in the table on the next page.

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 1966-67 the Bank received from the borrowers and distributed among the Paying Agents the equivalent of about 27 million francs in respect of interest and the equivalent of about 35 million francs in respect of redemption.

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.

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 1967	Rates of interest %	Year of final maturity
1st	1954	United States	US Government	$	100,000,000	68,900,000	3⅞	1979
2nd	1955	Belgium	Caisse Générale d'Epargne et de Retraite, Brussels	B.fr.	200,000,000	147,800,000	3½	1982
3rd	1955	Germany	Rheinische Girozentrale und Provinzialbank, Düsseldorf	DM	25,000,000	16,884,850	3¾	1981
			Landesbank für Westfalen (Girozentrale), Münster	DM	25,000,000	16,884,850	3¾	1981
4th	1955	Luxemburg	Caisse d'Epargne de l'Etat, Luxemburg	B.fr. L.fr.	20,000,000 5,000,000	14,780,000 —	3½ —	1982 —
5th	1956	Saar	Landesbank und Girozentrale Saar, Saarbrücken	DM	2,977,450[1]	1,932,365	4¼	1977
6th	1956	Switzerland	Public issue	Sw.fr.	50,000,000	31,250,000	4¼	1974
7th[2]	1957	United States	Public issue	$	25,000,000	15,500,000	5½	1975
10th	1957	Luxemburg	Etablissement d'Assurance contre la Vieillesse et l'Invalidité, Luxemburg	L.fr.	100,000,000	85,057,222	5⅜	1982
11th[2]	1958	United States	Public issue	$	35,000,000	28,100,000	5	1978
13th[2]	1960	United States	Public issue	$	25,000,000	23,350,000	5⅜	1980
15th	1961	Luxemburg	Etablissement d'Assurance contre la Vieillesse et l'Invalidité, Luxemburg	L.fr.	100,000,000	94,412,804	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, 12th and 14th Series have been entirely redeemed.

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

The Bank's activities in its continuing capacity as Agent for the execution of the financial operations of the EMA under the Organisation for Economic Co-operation and Development have been described in Chapter V of Part II of the present Report. The Bank has received in this connection, as last year, a contribution of Sw.fr. 500,000 towards its administrative expenses, together with the reimbursement of its out-of-pocket expenses; these amounts have been credited to "Costs of administration" in the Bank's Profit and Loss Account, but are not shown, as in the past, as a separate item.

5. Development of co-operation between central banks and international organisations.

Co-operation between central banks, the promotion of which is one of the primary functions of the Bank and which it has constantly endeavoured to further over the years, has become closer and been intensified during the last year.

Prominent among operations within this framework is the arrangement set up in Basle last June by a group of major central banks and the Bank with the object of providing facilities for the Bank of England in order to relieve the pressure on the official reserves of the United Kingdom arising from fluctuations in the sterling balances of overseas countries and thus to strengthen the sterling system. These central-bank facilities were channelled through the Bank, and their usefulness has been clearly borne out. Furthermore, in close co-operation with certain central banks, the Bank has contributed effectively to co-ordinated efforts to alleviate undesirable seasonal strains on markets, in particular the Euro-dollar market. This has been partly achieved, in agreement with the Federal Reserve Bank of New York, by the utilisation of the swap arrangements concluded between the latter and the Bank for International Settlements. The total of these swap lines amounts to US $400 million, half of which is against Swiss francs and half against other European currencies.

The Bank's activity in the field of research and exchanges of information has been continued. A number of meetings of central-bank experts have been organised — in addition to the regular meetings of the Board of Directors — either to study economic and monetary problems of general interest or to examine specific questions such as the development of the gold and Euro-currency markets. The Bank's services have assisted in the work of these groups.

The Bank has continued to perform the task entrusted to it in August 1964 by the Ministers of the Group of Ten of collecting and distributing to all participants of the Group and to Working Party No. 3 of the OECD statistical data relevant to the means used to finance surpluses and deficits on external account. These data provide the essential basis for multilateral surveillance of international liquidity creation. The Governors of the central banks of the Group, when they meet at the Bank, also exchange information at the earliest possible stage on arrangements entered into between members of the Group for new or enlarged credit facilities and the evolution of such credits. Co-operation in this field has proved to be of great value.

The Bank has continued to be associated in the work carried out by the Deputies of the Group of Ten and its Study Groups on the international liquidity problem, the creation of a new reserve instrument and the adjustment process. The Bank's services have also assisted in this work.

The continued co-operation between central banks has strengthened relations between the Bank, on the one hand, and the OECD and the IMF, on the other.

6. Net profits and their distribution.

The accounts for the thirty-seventh financial year ended 31st March 1967 showed a surplus of 47,074,487 francs. The surplus for 1965-66 was 38,578,751 francs.

The Board of Directors has decided to continue to build up the provision for exceptional costs of administration and the provision for contingencies, to the extent of 200,000 francs and 3,800,000 francs respectively. In 1966 transfers to these provisions had amounted to 1 million and 15 million francs respectively.

In addition, it has become necessary to constitute a provision for building purposes. In view of the large profit for the financial year 1966-67, the Board of Directors has decided to pay into this new provision an amount of 11 million francs. At present the Bank's offices are spread over six buildings; the premises date from the beginning of the century and are no longer in line with modern requirements. Four of these buildings, including the main one, are owned by the Bank. The other two are adjoining, but the Bank is only the lessee of a number of rooms in them. Since this is not a rational situation, the Bank is studying the possibility of constructing a new building either on the land it owns or on a site in the neighbourhood that has been offered to it.

After deduction of the transfers to the provisions, the net profit amounts to 32,074,487 francs, to which must be added the sum of 9,842,787 francs carried forward from the previous financial year. The profit available for distribution thus amounts to 41,917,274 francs. This makes it possible not only to pay the cumulative dividend of 6 per cent. per annum on the paid-up capital and the balance of the undeclared cumulative dividend but also to make other distributions provided for under Article 53 of the Bank's Statutes.

The cumulative dividend amounts to 37.50 francs and the balance of the undeclared cumulative dividend to 54.47 francs per share. After appropriation of the sums required for the distribution of these two dividends, i.e. 7,500,000 and 10,894,000 francs respectively, totalling 18,394,000 francs, an amount of 23,523,274 francs remains to be distributed.

Under the provisions of sub-clause (c) of Article 53 of the Statutes, 20 per cent. of this sum, viz. 4,704,655 francs, can be utilised to pay a supplementary dividend or to build up a Special Dividend Reserve Fund. The Board of Directors recommends to the General Meeting that 4,106,000 francs be used to pay a supplementary dividend of 20.53 francs per share. As regards the remaining 598,655 francs, the Board of Directors, exercising the powers vested in it by sub-clause (c) of Article 53 and basing itself on the policy pursued by the Bank in the early years of its existence, has decided to appropriate this to a reconstituted Special Dividend Reserve Fund.

The appropriation of the balance of the available profit, namely 18,818,619 francs, is regulated by sub-clauses (d) et seq. of Article 53 of the Statutes.

Until the General Reserve Fund reaches an amount equal to that of the paid-up capital, half of this balance must be transferred to that Fund, which will go up from 13,342,650 to 22,751,960 francs. The last transfer to this Reserve was made in 1940.

Following the settlement of the assets and liabilities of the Bank appertaining to the Hague Agreements of 1930 (Young Plan), to which reference was made in the Bank's Thirty-Sixth Annual Report, the appropriation of the other half is now subject to the provisions of sub-clause (f) of Article 53. On the basis of that clause, the Board of Directors recommends to the General Meeting that the whole of this sum, viz. 9,409,309 francs, be paid into the Special Dividend Reserve Fund. If this proposal is accepted, this Fund will amount to 10,007,964 francs, which approximately corresponds to the sum brought forward from the previous financial year, which can no longer be carried forward since this would be contrary to the provisions of Article 53.

Under the proposals of the Board of Directors, the total distribution will amount to 112.50 francs per share, the same sum as that paid in 1966. It will be payable on 1st July 1967 in the amount of 160.75 Swiss francs per share. In the case of dividends which cannot be paid on that date, the conversion into Swiss francs will take place on the day of their payment at the then prevailing rate of exchange.

The Balance Sheet, the Profit and Loss Account and the Appropriation Account will be found at the end of this Report.

The accounts of the Bank have been duly audited by Messrs. Price Waterhouse & Co., Zurich, who have confirmed that the Balance Sheet and the Profit and Loss Account give a true and correct view of the state of the Bank's affairs as at 31st March 1967 and of its profit for the year ended on that date. Messrs. Price Waterhouse & Co.'s certificate is appended at the foot of the Balance Sheet.

7. Changes in the Board of Directors.

The Earl of Cromer, who, as Governor of the Bank of England, had been an ex officio Director of the Bank for International Settlements since 1961, resigned as Governor of the Bank of England at the end of June 1966, at the same time ceasing to be an ex officio Director of the Bank. The Chairman, at the meeting held on 13th June 1966, expressed the Board's sincere thanks for the outstanding services which Lord Cromer had rendered to the Bank.

Sir Leslie O'Brien, who succeeded Lord Cromer as Governor of the Bank of England on 1st July 1966, became an ex officio Director of the Bank for International Settlements on the same date. He was welcomed by the Chairman at the first Board meeting which he attended on 11th July 1966.

At the meeting of the Board held on 11th July 1966, the Chairman announced that Sir Leslie O'Brien had appointed Mr. C. J. Morse, Director of the Bank of England, as his Alternate on the Board of Directors in place of Sir Maurice Parsons and that Mr. R. G. Raw would continue to act as Sir Leslie O'Brien's Alternate in the absence of Mr. Morse. The Bank is grateful to Sir Maurice Parsons for his valuable services.

At the meeting of the Board held on 11th July 1966 the Chairman announced that Dr. W. Schwegler, who had been a member of the Board since 1956, had decided to resign from his office as a member of the Board of Directors of the Bank for International Settlements on 31st August 1966, when he would retire from his post as President of the Direktorium of the Swiss National Bank. He thanked Dr. Schwegler in the name of the Board for the eminent services he had rendered to the Bank over many years.

At its meeting on 11th July 1966 the Board elected, under Articles 28(3) and 29 of the Statutes, Dr. Edwin Stopper, who had been appointed President of the Direktorium of the Swiss National Bank as from 1st September 1966, to be a member of the Board of Directors for the unexpired period of Dr. Schwegler's term of office ending on 31st March 1968. At the meeting on 5th September 1966 the Chairman welcomed Dr. Stopper, who was attending his first meeting as a member of the Board of Directors.

The mandate of M. Maurice Frère as a member of the Board was due to expire on 7th August 1966 and he was re-appointed under Article 28(2) of the Statutes by M. Ansiaux, Governor of the National Bank of Belgium, in July 1966 for a further period of three years ending on 7th August 1969.

The mandate of Dr. Donato Menichella as a member of the Board was due to expire on 7th November 1966 and he was re-appointed under Article 28(2) of the Statutes by Dr. Carli, Governor of the Bank of Italy, in September 1966 for a further period of three years ending on 7th November 1969.

The mandate as a member of the Board of Dr. M. W. Holtrop being due to expire on 31st March 1967, he was re-elected under Article 28(3) of the Statutes at the meeting of the Board held on 13th March 1967 for a further period of three years ending on 31st March 1970.

At the meeting of the Board held on 8th May 1967 the Chairman announced that M. Brunet had appointed M. Marcel Théron, General Manager of the Foreign Department of the Bank of France, as his second Alternate in place of M. Gilbert Bouchet. The Bank is grateful to M. Bouchet for the valuable services he has rendered to the Bank since his appointment more than two years ago.

CONCLUSION.

Whereas a year ago excess demand and rising prices was the prevailing situation in most of the industrial countries, the general economic climate today ranges from lack of expansionary momentum to mild recession. Three countries have been dominant in bringing about this change in the conjuncture — the United States, Germany and the United Kingdom — both because of their own size and because the easing of activity in them has had repercussions on the export demand over a wider area. Expansion of output is continuing only in Italy and Japan.

Excess demand emerged suddenly in the United States with the intensification of the Vietnam war, while in Germany it built up more slowly over many months. But the situation in both countries was similar in that rising public-sector expenditure was the major factor in forcing boom conditions. Also, adequate fiscal restraint to curb inflationary pressures was not forthcoming and the containment of excess demand was left to central-bank policy. To counteract the stimulus from the budget deficit, very severe monetary restriction was required in both countries, which sent interest rates well above previous post-war levels. In the end, this policy succeeded in overcoming inflation, though the process was slower and involved more sectoral difficulties than what could have been achieved with a better policy mix.

In the United Kingdom large negotiated wage increases had added to the strong expansionary impulse from public expenditure to produce excess demand by early in 1964. After vain hopes that the situation would correct itself with the help of mild restraints, the authorities tried to impose a strong curb on demand in the budget a year ago. The means used, however, were not immediately effective or convincing. Hence, there was a substantial flight from sterling in the early summer of 1966 which necessitated a further package of restrictive measures in July. The freeze on wages and prices and the new tax increases imposed at that time very soon brought a better balance in both the domestic and external spheres.

While there has not yet been a clear shift to renewed expansion, the present situation does not show any of the characteristic signs of a deflationary spiral. With regard to the economic outlook, also, it is important that the easing of demand did not reflect an autonomous business cycle — such as might come from an overexpansion of productive capacity. Rather, it came about through anti-inflationary policy and, with inflation having subsided, there is little reason to expect protracted stagnation. Monetary policy has been relaxed in all countries and positive steps to stimulate activity have been taken in Germany and several other countries. In both the United States and the United Kingdom the rates of overall budget deficit are very large and, if they are financed through monetary expansion, the danger of excess domestic liquidity is just as real as that of stagnant demand — particularly in view of the external payments problems of both countries. In general, official policy must guard against reactivation of excess demand; hence, expansion is likely to be renewed at a more moderate pace than in the 1962–65 period.

Restrictive measures in the end gained their objective; but the impression that remains from recent experience is one of groping towards stabilisation. The situation was not obscure from an analytical standpoint and the policy remedies required were not very difficult to formulate. Thus, nothing was wrong with the "new economics", as sometimes charged; the trouble was failure to act promptly and effectively. In particular, fiscal policy was too inflexible, which meant that monetary restrictions had to be pushed close to the limit. As this process came near to producing a monetary crisis and, indeed, contributed to the intense strains in the foreign exchange market, the case for a better policy mix in the future cannot be brushed aside.

The problem of more effective use of the whole range of policy instruments, to help prevent imbalance in the first place and to correct it more quickly when it comes, is not one for governments and parliaments alone. There is no doubt that public opinion relishes tax cuts more than tax increases, and that "full employment" has greater support than this less tangible goal of monetary stability. It is significant that several governments fell in the process of seeking budgetary restraint. Therefore, it is vital that the public become better informed on these matters. One must say, for the time being, that in quite a few countries control of the opinion cycle is more difficult than control of the business cycle.

The cyclical movement over the past year has produced significant changes in the balance-of-payments situation of the main countries. In Italy the large surplus of the two previous years has been sharply curtailed; imports have increased substantially with continued domestic expansion and net capital exports were induced by higher interest rates abroad. In France, also, where the dampening of internal demand was milder than in most other countries, the external surplus has shifted to a small deficit due to higher imports and to a much reduced capital inflow. In the United Kingdom, on the other hand, the previous balance-of-payments deficit has been corrected by restraint of domestic demand and further limitations on capital exports. Similarly, in Germany the deficit has disappeared but, with the recession in domestic demand causing a rise in exports and a fall in imports, it has given way to a large surplus.

The significant exception to generally better balance in international payments, however, is the United States. The upsurge of home demand led to soaring imports, so that the trade surplus, excluding government-financed exports, fell to only a little over $700 million. To this deterioration was added a large rise in military expenditure abroad because of the war in Vietnam. As the tight monetary conditions of last year attracted unusually large capital imports, the overall external deficit did not rise very much. However, the prospect this year is that the underlying deterioration will become more evident, which would pose problems for monetary policy.

Official discussions on reform of the international monetary system in the past year have concentrated on plans for deliberate creation of a new reserve asset to supplement gold in the growth of global reserves over the longer term. While it has been agreed that the increment of gold and dollars is likely to be insufficient in the future, there has not been agreement on how to make good this deficiency. Many countries believe the new asset should have the character of an owned reserve so that it might, at least in time, serve as an international money in its own right. Other countries believe such a course to be too dangerous and would limit contingency planning to provision of an additional element of credit in the system, part of which could be automatic. Perhaps more importantly, the two views are quite divergent on how much supplement to gold may be needed for global reserves and how soon. The deterioration of the US balance of payments, and the unlikelihood of equilibrium being restored in the next year or two, has had a strong influence on the views of the hard money school. Given the persistence of that deficit, these countries are reluctant to separate the problem of reform of the means of reserve creation in the system from the problem of stricter implementation of the adjustment process.

It is too early to know what proposals for strengthening the IMF might be presented at the coming meeting in Rio de Janeiro. While such a step would be welcome, it is hardly likely that it will go very far to resolve the problem of the future growth of reserves. Where the matter stands is that an alternative to the present gold-exchange standard has not been found; nor is there a clear view about how to operate that system with a very limited flow of new monetary gold.

Meanwhile, it seems likely that, in the practical task of managing the flows of payments, there will be continued recourse to the expedients of ad hoc credit transactions and direct controls.

Gabriel Ferras

General Manager

BALANCE SHEET AND PROFIT AND LOSS ACCOUNT

AS AT 31st MARCH 1967

BALANCE SHEET

ASSETS

IN GOLD FRANCS (UNITS OF 0.290 322 58...

			%
Gold in bars and coins		3,095,928,425	37.6
Cash on hand and on sight account with banks		155,533,515	1.9
Rediscountable Treasury bills		70,473,519	0.9
Bills and securities cashable on demand		74,223,807	0.9
Time deposits and advances			
Not exceeding 3 months	2,905,993,888		35.3
Between 3 and 6 months	272,963,858		3.3
Between 6 and 9 months	160,440,341		1.9
Between 9 and 12 months...	211,658,614		2.6
		3,551,056,701	
Other bills and securities			
Gold			
Not exceeding 3 months	282,673,089		3.4
Between 3 and 6 months	95,114,787		1.2
Between 6 and 9 months	23,346,085		0.3
Between 9 and 12 months...	19,012,096		0.2
Currencies			
Not exceeding 3 months	616,621,496		7.5
Between 3 and 6 months	130,732,607		1.6
Between 6 and 9 months	69,640,555		0.8
Between 9 and 12 months...	17,314,479		0.2
Over 1 year	29,275,240		0.4
		1,283,730,434	
Miscellaneous assets		1,050,115	0.0
Buildings and equipment		1	0.0
		8,231,996,517	100

MEMORANDUM ACCOUNTS

a. Forward gold operations:

Net balance: gold receivable (currencies to be delivered)	471,594,422

b. Funds, bills and other securities administered or held by the Bank for account of third parties:

Earmarked gold	1,233,031,174
Bank balances	26,288,404
Bills and other securities	677,697,186

AS AT 31st MARCH 1967

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	1.5
Reserves			
Legal Reserve Fund	12,500,000		
General Reserve Fund	13,342,650		
		25,842,650	0.3
Deposits (gold)			
Central banks			
Between 9 and 12 months...	141,164,686		1.7
Between 6 and 9 months	237,859,991		2.9
Between 3 and 6 months	74,864,788		0.9
Not exceeding 3 months	221,537,433		2.7
Sight	2,326,306,125		28.3
Other depositors			
Between 6 and 9 months	99,949,256		1.2
Between 3 and 6 months	89,601,231		1.1
Not exceeding 3 months	103,436,255		1.3
Sight	266,489,919		3.3
		3,561,209,684	
Deposits (currencies)			
Central banks			
Over 1 year	16,220,264		0.2
Between 9 and 12 months...	9,581,924		0.1
Between 6 and 9 months	52,408,796		0.7
Between 3 and 6 months	309,190,996		3.8
Not exceeding 3 months	2,991,199,828		36.3
Sight	221,336,672		2.7
Other depositors			
Not exceeding 3 months	290,699,118		3.5
Sight	18,942,037		0.2
		3,909,579,635	
Notes			
Between 3 and 6 months	2,327,358		0.0
Not exceeding 3 months	291,067,560		3.5
		293,394,918	
Miscellaneous		44,052,356	0.5
Profit and Loss Account		41,917,274	0.5
Provisions			
Provision for contingencies	220,000,000		
Provision for building purposes	11,000,000		
		231,000,000	2.8
		8,231,996,517	100

REPORT OF THE AUDITORS TO THE BOARD OF DIRECTORS AND THE SHAREHOLDERS OF THE BANK FOR INTERNATIONAL SETTLEMENTS, BASLE.

In our opinion the foregoing Balance Sheet and the annexed Profit and Loss Account give a true and correct view of the state of the Bank's affairs as at 31st March 1967 and of its profit for the year ended on that date.

We have obtained all the information and explanations which we considered necessary. In our opinion the Bank has kept proper books and the said accounts are in agreement with them and with the said information and explanations.

ZURICH, 3rd May 1967. PRICE WATERHOUSE & CO.

PROFIT AND LOSS ACCOUNT
for the financial year ended 31st March 1967

		Gold Francs
Net interest and other income		55,949,014
Less: Costs of administration:		
Board of Directors	141,428	
Executives and Staff	7,101,620	
Office and other expenses	1,631,479	8,874,527
Net operating surplus		47,074,487
Less: Amounts appropriated to the following provisions:		
Exceptional costs of administration	200,000	
Contingencies	3,800,000	
Building purposes	11,000,000	15,000,000
NET PROFIT for the financial year ended 31st March 1967		32,074,487
Add: Balance brought forward from the preceding year		9,842,787
TOTAL PROFITS AVAILABLE		41,917,274

APPROPRIATION ACCOUNT

		Gold Francs
TOTAL PROFITS AVAILABLE, as above		41,917,274
Applied in accordance with Article 53 of the Statutes, as follows:		
Sub-clause (b)		
Cumulative dividend of 37.50 gold francs per share ...	7,500,000	
Balance of undeclared cumulative dividend of 54.47 gold francs per share	10,894,000	18,394,000
		23,523,274
Sub-clause (c) – 20% of 23,523,274		
Additional non-cumulative dividend of 20.53 gold francs per share	4,106,000	
Transfer to Special Dividend Reserve Fund	598,655	4,704,655
		18,818,619
Sub-clause (d) – 50% of 18,818,619		
Transfer to General Reserve Fund		9,409,310
		9,409,309
Sub-clause (f) – 50% of 18,818,619		
Transfer to Special Dividend Reserve Fund		9,409,309
		—

BOARD OF DIRECTORS

Dr. M. W. Holtrop, Amsterdam	Chairman of the Board of Directors, President of the Bank
Maurice Frère, Brussels	Vice-Chairman

Hubert Ansiaux, Brussels
M. J. Babington Smith, London
Karl Blessing, Frankfurt a/M.
Dr. Rudolf Brinckmann, Hamburg
Jacques Brunet, Paris
Dr. Guido Carli, Rome
Henri Deroy, Paris
Dr. Donato Menichella, Rome
Sir Leslie O'Brien, London
Dr. Edwin Stopper, Zurich
Per Åsbrink, Stockholm

Alternates

Dr. Paolo Baffi, Rome, or
Prof. Pietro Stoppani, Rome
Bernard Clappier, Paris, or
Marcel Théron, Paris
C. J. Morse, London, or
R. G. Raw, London
Cecil de Strycker, Brussels

MANAGEMENT

Gabriel Ferras	General Manager
Dr. Milton Gilbert	Economic Adviser, Head of the Monetary and Economic Department
Dr. Antonio d'Aroma	Secretary General, Head of Department
Dr. Hans H. Mandel	Head of the Banking Department
D. H. Macdonald	Manager
Georges Janson	Manager
Henri Guisan	Legal Adviser
Dr. Antonio Rainoni	Manager

Jan Knap	Assistant Manager