

Italian Economic Developments in 1952 as Reported by the Bank of Italy

by
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The principal developments in Italy's economic situation in 1952, some of which have been mentioned in an earlier account (1) of the Report of the Minister of the Treasury, and which are much more fully documented in the Report of the Bank of Italy (2), present a picture which contrasts in a number of ways from that of the preceding years. It is marked by several symptoms of growing strain which may perhaps be said to render 1952 the most critical year in Italy's post-war economic development since 1947.

We have already commented (3) on the slowing down of the rate of increase in production and in investment shown by the 1952 statistics in comparison with those for the previous years. According to those statistics the increase in gross national income in money terms from 1951 to 1952 was only 5 per cent (4) as against an increase of 16 per cent from 1950 to 1951, and the increment in real terms between 2 and 3 per cent as against 6 per cent. Gross investment was estimated to have increased in money terms by less than 3 per cent from 1951 to 1952, compared with an increase of 26 per cent from 1950 to 1951. The increase in 1952 is attributed entirely to

fixed assets (5); it is supposed that the year closed with a level of stocks about equal to that with which it opened, thus contrasting with the previous year when a heavy increase took place in physical volume and still more in value terms.

A second sign of increasing strain was the slight upward pressure on the price level which did not reflect this time, as it had done on earlier occasions, an international movement. Thus it is noticed that after June, 1952 (see Table I) the internal wholesale price level, which had previously followed closely the level of prices of raw materials on the international market, began to diverge from the latter. Up until June, 1952 the internal wholesale price level had gone on falling, in continuation of the movement that had been evident most of the time since February, 1951; after June, 1952 it showed a gentle rising movement not apparent in the international indices, which either continued to fall or remained stable. Thus the Italian price level after the middle of 1952 showed an upward movement « of its own ». The increase was due mainly to a rise in the prices of consumers' goods (especially food products) which was more than sufficient to compensate for the fall in the prices of textile products. The cost of living index — which had followed the upward movement of wholesale prices

(5) Taken alone these increased in money terms by 15.5 per cent and in real terms by 13 per cent, the percentage increase in real terms being larger than in either of the two preceding years.

after June, 1950 with a lag, and went on rising after the latter had fallen — continued its upward movement through 1952. Over the twelve months it rose by 3.6 per cent. The increased pressure of spending on the consumers' market, nourished especially by higher wage rates and by the incomes generated by the government investment programme, was regarded by the Bank of Italy as a warning of the need for added watchfulness on the part of the monetary authorities in their effort to prevent a renewal of inflationary pressure.

TABLE I
MOVEMENTS IN PRICES AND MONEY WAGES
(ISTAT indices, 1938=1)

	Wholesale prices	Cost of living	Money Wages (a)	
			Industrial workers	Agricultural workers
1950 June	46.7	48.2	58.1	69.5
Dec.	54.1	50.1	59.6	69.9
1951 Feb.	57.4	51.7	59.7	70.0
June	55.9	53.9	63.3	70.8
Dec.	54.5	54.2	66.8	72.2
1952 June	51.3	55.6	70.5	73.1
Dec.	52.9	56.1	74.3	80.0
1953 Mar.	52.6	56.1	75.2	80.0

(a) Including family allowances for married man with three children

Source: Monthly Bulletins of the Central Institute of Statistics.

The increase in wage rates, which was mostly due to the raising of family allowances during the second half of the year, brought the indices of nominal wage rates for married industrial and agricultural workers in December, 1952 to over 10 per cent above the level of a year earlier (see Table I). The real increase (allowing for the rise in the cost of living) was between 7 and 8 per cent. Thus, the upward movement in real wage rates of the principal categories of employed, which had shown a pause in the first half of 1951 after the substantial gains made in the preceding years, was resumed. The fear was expressed that the pressure of continually rising wage rates on costs might seriously affect Italy's already difficult export position.

The increase in wage rates was accompanied by a fall in profits. The balance sheet data drawn up by the Bank of Italy for a sample of 221 joint stock companies selected from the principal branches of industrial activity indicate that net profits fell sharply in the textile industry, but that they increased in most other sectors (though not by the large amount by which they had increased from 1950 to 1951), and that for the sample taken as a whole they declined slightly. For the three years 1950 to 1952 the total moved as follows:

1950	1951	1952
45.4	60.8	58.7

(Milliards of lire)

The Bank of Italy adds, however, that since the amount of capital of the companies was increased through new issues from 511 milliards in 1950 to 545 milliards in 1951, and 570 milliards in 1952, the increase in the profit level *relative to the capital base* from 1950 to 1951 was smaller, and the decrease from 1951 to 1952 larger, than the above figures indicate.

The dominant symptom of increased strain was, however, the pressure on the balance of payments, which has been amply documented in the previous number of the « Quarterly Review » (6), and of which the most striking reflection was the reversal of Italy's position in the European Payments Union from one of continual accumulation of credit balances to one of decumulation. This development was attributed partly to the effects of the world textile crisis and of the quantitative import restrictions imposed by other countries in reducing Italian exports, but partly also to the effect of the domestic investment programme in increasing Italian imports, especially of equipment. The rise in the balance of payments deficit, by augmenting the supplies of goods on the domestic market more than in proportion to the growth of the national product (7), served temporarily as an

(6) January-March, 1953, pp. 44 ff.

(7) As we pointed out in the previous number of the « Quarterly Review », the increase in disposable income in 1952 as compared with the previous year was calculated by the Bank of Italy to be 144 milliard lire more than the increase (of 482 milliards) in the gross national product.

(1) See the previous number (January-March) of the « Quarterly Review ».

(2) Bank of Italy, *Assemblea generale ordinaria dei partecipanti*, 1952 (Rome, 1953).

(3) See the « Quarterly Review », *loc. cit.*

(4) According to the index of industrial production compiled by the Central Institute of Statistics, the increase in the level of activity took place almost entirely in the second half of the year.

anti-inflationary element helping to offset the inflationary effect of the increased domestic spending. The drawing on foreign exchange reserves which it implied was, however, a source of relief that could not continue indefinitely. This development was also, therefore, a cause for concern that had not existed in the previous years.

Another development which drew attention was the heavy increase in the volume of bank lending, not only to the government but also to the private sector of the economy. The expansion of lending to the private sector affected in greater or lesser degree all branches of activity, in spite of the considerable increase in private capital issues and in lending by special credit institutions, and it seemed to be at variance with the relatively small increase in production and investment. There was a slight suggestion also that the credit reins had been a little less firmly held by the authorities than in previous years.

Finally, all the developments we have mentioned served to underline the dangers inherent in the continuation of the heavy budget deficit, which is very largely conditioned by the financing of the government investment programme.

The general conclusion to be drawn from the years's events seemed to be that even if the degree of strain had not yet reached the point where it gave cause for actual alarm, it was sufficient to foreshadow some of the dif-

ficulties that would face the new government in maintaining on its present scale, or still more in expanding, the development programme aimed at decreasing unemployment and raising the real income levels of the poorest classes of the population. Indeed it seemed probable that total expenditures had already been pushed just beyond, rather than held just short of, the critical point on which the Minister of the Treasury and the Governor of the Bank of Italy has insisted in earlier years in reply to those critics who had pressed for a more expansive policy.

The remainder of this article will be devoted to summarizing some of the statistics relating to the budget deficit as they have been set out for us by the Bank of Italy, and finally, to analysing the year's monetary and credit developments.

The Budget Deficit.

The Treasury returns provide statements of the administrative budget (*gestione di competenza*), i.e. of appropriations and accruals, and of the cash budget, i.e. of payments actually made and revenues received, each being divided into two parts, the ordinary account (*parte effettiva*) and the capital account (*movimenti di capitale*). Since, however, the capital account includes not only investment expenditures but also receipts from medium-

BUDGET DEFICITS
(Milliards of lire)

TABLE 2

	Treasury figures						Bank of Italy figures			
	Administrative budget			Cash budget			Administrative budget (adjusted) Total	Cash budget (adjusted) Total		
	Ordinary account	Capital account	Total	Ordinary account	Capital account	Total				
1947-48	- 844	- 71	- 915	- 416	- 89	- 505	} n. a.	} n. a.		
1948-49	- 496	- 57	- 553	- 370	- 50	- 420				
1949-50	- 295	+ 121	- 174	- 200	+ 116	- 84				
1950-51	- 169	- 44	- 213	- 211	+ 52	- 159				
1951-52 (a)	- 410	+ 37	- 373	- 320	- 15	- 335			- 340	- 229
1952-53 (b)	- 443	- 53	- 496						- 496	- 307
1953-54 (c)	- 366	- 51	- 417				- 537	- 393		
							- 411			

- (a) Provisional results.
(b) Revised estimates.
(c) Initial estimates.

TABLE 3
ADJUSTED CASH BUDGET: SUMMARY
(Milliards of lire)

	Financial years		Calendar years	
	1950-1951	1951-1952	1951	1952
1. Ordinary account:				
Expenditures (a) . . .	1,668	1,995	1,807	2,038
Revenues	1,477	1,687	1,576	1,778
Deficit on ordinary account	- 191	- 308	- 231	- 260
2. Capital account:				
Deficit	- 70	- 65	- 51	- 113
3. Total deficit on ordinary and capital account	- 261	- 373	- 282	- 373
4. Minor cash items relating to budget . . .	- 46	- 20	+ 16	- 71
5. Total (3)+(4) . . .	- 307	- 393	- 266	- 444

(a) Including allocations to the *Cassa per il Mezzogiorno* amounting to 75, 125, 100 and 115 respectively. The *Cassa* itself, however, deposited with the Treasury or invested in Treasury certificates sums amounting in the respective periods to 23, 96, 69 and 28. The net drawings of funds by the *Cassa* were thus only 52, 29, 31 and 87, respectively.

and long-term security issues minus payments for debt redemption, these returns do not suffice to give us a measure of the real pressure of the deficit on the economy.

The Bank of Italy has therefore drawn up *adjusted statements* of the administrative budget results for each of the last three financial years, and of the estimates for the coming financial year (1953-54), eliminating these debt items. Similarly it has calculated for several years past the figures for the *adjusted cash budget*, the principal adjustments being the elimination of the debt items and the inclusion of certain cash items relating to the capital account which the Treasury statements exclude. All four sets of figures are reproduced in so far as they are available in Table 2.

Since neither set of adjusted figures is available for many years we are obliged to fall back on the Treasury figures for the ordinary account to give us an approximate idea of the movement of the deficit over a longer period: the fall up to 1949-50 in the cash deficit, or up to 1950-51 in the administrative deficit, and the sharp increase afterwards. A summary of the main items in the adjusted cash budget, calculated both for the last two financial years and for the last two calendar years, is reproduced in Table 3.

For an itemized account of revenues and expenditures over the last few years we have to rely on the adjusted administrative budget, since it is not possible to draw up the adjusted cash budget in the same detail. The Bank of Italy in drawing up this adjusted statement, besides excluding the debt movements to which we have already referred, has regrouped the items so as to give a truer division between « revenue » and « capital » items, since in the Treasury returns the ordinary account as well as the capital account includes some investment expenditures.

This regrouping allows us to judge the weight of the public investment expenditure. The adjusted administrative budget figures (see Table 4) show that the total revenues (on ordinary and capital accounts combined) were more than sufficient in 1951-52, and almost sufficient in 1952-53, to cover the expenditures on ordinary account, and that they

should be almost sufficient also, according to the initial estimates, in 1953-54. The investment programme, which according to the preliminary figures was responsible for 23 per cent of the total appropriations in 1951-52, for 21 per cent in 1952-53 and for 18 per cent in the 1953-54 estimates, has been either more than, or not far from sufficient to account for the entire deficit in the administrative budget for these years. Although the initial total appropriations for investment purposes in the coming financial year (1953-54) are considerably lower than in the two previous years, and it is almost entirely from this source that the attempt to reduce the deficit in the coming year derives, it is not expected that actual cash expenditures on investment will be correspondingly lower. For the investment expenditures are likely to be swollen by the faster spending of the balances of the *Cassa per il Mezzogiorno* (evidenced by the rapid increase in the rate of withdrawals in the second half of 1952) (8) and by the use of other appropria-

(8) Cf. footnote to Table 3.

ADJUSTED ADMINISTRATIVE BUDGET, ITEMIZED
(Milliards of lire)

TABLE 4

	Financial years				Financial years		
	1951-1952 (a)	1952-1953 (b)	1953-1954 (c)		1951-1952 (a)	1952-1953 (b)	1953-1954 (c)
A. Ordinary account:				B. Capital account:			
<i>Expenditures</i>				<i>Expenditures</i>			
1. Current goods and services				1. Investments			
Civil	683	718 ^(b)	707	(a) Extraordinary public works (g)	168	200	154
Military	407	475	427	(b) <i>Cassa per il Mezzogiorno</i>	118	80	90
2. Public debt service	117	146	159	(c) Agriculture, land improvement and fishing	55	65	61
3. Relief and welfare	108	126	132	(d) Industry and mining	87	59	23
4. Subsidies	91	80	95	(e) Workers' training, and reforestation projects	48	28	10
of which:				(f) Others	44	59	48
« political prices » of cereals	(—)	(17)	(25)	<i>Total</i>	520	491	386
operating losses of <i>amministrazioni autonome</i> (e)	(91)	(63)	(70)	2. Others items	48	19	17
5. Other transfer payments (war pensions and indemnities)	103	108	115	<i>Total</i> (1)+(2)	568	510	403
6. Grants to provincial and local authorities	127	119	130				
7. Transfers abroad	32	43	19	<i>Revenues</i>			
<i>Total</i>	1,668	1,815	1,784	1. Transfers (sales of goods, loan repayments, etc.)	51	15	22
<i>Revenues</i>				2. Foreign governments grants	118	123	50
1. Direct taxes	483	553	538	<i>Total</i>	169	138	72
of which:				<i>Total expenditures</i>	2,236	2,325	2,187
income and surtaxes	(228)	(233)	(254)	<i>Total revenues</i>	1,740	1,788	1,776
2. Indirect taxes on business turnover and on consumption	736	761	810	TOTAL DEFICIT	496	537	411
3. State monopolies	254	270	281				
4. <i>Total</i> (1)+(2)+(3)	1,473	1,584	1,629				
5. <i>Less</i> refunds and reimbursements	26	32	22				
6. <i>Total</i> (4)-(5)	1,447	1,552	1,607				
7. Others (f)	124	98	97				
<i>Total</i>	1,571	1,650	1,704				

(a) Provisional results.

(b) Revised estimates.

(c) Initial estimates.

(d) Includes 9 milliards for election expenses.

(e) For a description of these bodies, see G. Cosmo, *State Participation in Business Concerns in Italy*, Vol. IV, No. 19 of the « Quarterly Review » (October-December, 1951).(f) Including lotteries and net income from public services and *amministrazioni autonome*.

(g) These were particularly high in 1951-52 and 1952-53 because of works undertaken as a result of the floods of the winter of 1951-52.

tions made in previous years and not yet used (*conti residui*).

Monetary and Credit Developments.

Our final and principal task is to examine the main developments in the money and credit situation in 1952 as they emerge from the wealth of statistics and analysis given us in the Bank's Report.

The total volume of currency (9) increased between the two year ends by rather less than in 1951 (not quite 8 per cent as compared with 10 per cent). The total deposits of banks and savings banks increased by rather more than in 1951 (24 per cent as compared with

(9) Defined as including the note circulation of the Bank of Italy, Treasury notes and coin (net of amounts held by the Bank of Italy) and circular cheques of the Bank of Italy and of the commercial banks.

20 per cent). The current accounts, which are usually assumed to represent « deposit money » (10), taken separately increased in about the same proportion as the total. The volume of money (currency *plus* current accounts) in-

creased by 12 per cent: this increase represented a marked change from the situation of the previous year when total borrowing by the Government from the banking system had remained almost constant.

TABLE 5

MOVEMENTS OF CURRENCY IN CIRCULATION, AND OF DEPOSITS AT BANKS AND SAVINGS BANKS
(Milliards of lire)

End of :	(1) Currency in circulation	(2) Current accounts	(3) Savings deposits	(4) Total deposits (2)+(3)	(5) Total volume of money (1)+(2)	(6) Ratio (2)÷(1)	(7) Ratio (4)÷(1)
Dec. 1938	24.5	21.3	34.2	55.5	45.8	0.87	2.27
Dec. 1947	928	599	415	1,014	1,527	0.65	1.09
June 1948	944	743	518	1,261	1,687	0.79	1.34
Dec. 1948	1,122	869	651	1,520	1,991	0.77	1.35
June 1949	1,030	965	707	1,672	1,995	0.94	1.62
Dec. 1949	1,194	1,107	842	1,949	2,301	0.93	1.63
June 1950	1,112	1,115	890	2,005	2,226	1.00	1.80
Dec. 1950	1,326	1,246	989	2,235	2,571	0.94	1.69
June 1951	1,226	1,269	1,009	2,278	2,495	1.04	1.86
Dec. 1951	1,459	1,527	1,161	2,688	2,987	1.05	1.84
June 1952	1,358	1,643	1,247	2,890	3,001	1.21	2.13
Dec. 1952	1,573	1,883	1,452	3,335	3,456	1.20	2.12

Note: The sources of the figures used to construct this and the following tables are the tables given in the Report of the Bank of Italy, supplemented where necessary by the Bank's Monthly Bulletins of Statistics.

increased by 16 per cent (*i.e.* by very much more than the volume of currency taken alone); this rate of increase was about the same as that registered in 1951 (see Table 5).

The credit situation was relatively easy, especially when compared with the stringency which had prevailed late in 1950 and in the first half of 1951. The figures given in Table 6, which makes a rough division between lending by the banking system to the government and private sectors respectively, indicate that the volume of lending by the banks and savings banks to the private sector increased by 26 per cent (as compared with 18 per cent the year before). The increase affected all sectors of the economy in greater or less de-

increased by 12 per cent: this increase represented a marked change from the situation of the previous year when total borrowing by the Government from the banking system had remained almost constant.

(11) The attribution of the total to the Bank of Italy on the one hand and the banks and savings banks on the other is obscured by the compulsory reserves of the banks. We have here included the amounts which are invested by the Bank of Italy in Treasury certificates (*buoni del Tesoro ordinari*) out of the compulsory reserves of the banks under lending to the Government by the Bank of Italy.

From the point of view of the system as a whole it is, of course, unimportant whether the compulsory reserves are invested directly by the banks themselves in government securities or whether they are so invested by the Bank of Italy. And in the case that the banks deposit their reserves with the Bank in the form of cash, it makes no difference whether the Bank keeps them in that form, and at the same time allocates an equivalent amount to investments in government securities, or to other forms of lending to the Treasury, out of its « own funds », or whether it invests them and lends so much less out of its « own funds ». The difference is purely of an accounting nature, and what matters is the net intake, or release of funds by the Bank of Italy from, or to the economic system resulting from these operations.

(10) The division of deposits which is usually adopted in Italy distinguishes between the *depositi fiduciari liberi a risparmio* plus the *depositi fiduciari vincolati* as broadly representing savings deposits on the one hand, and the *conti correnti di corrispondenza con clienti* plus the *depositi fiduciari in conto corrente* (*i.e.* the current accounts) as broadly representing deposit money on the other.

TABLE 6

LENDING TO GOVERNMENT AND TO PRIVATE SECTOR
BY BANKING SYSTEM
(Milliards of lire)

Bank of Italy (a)	Banks and Savings Banks		(4) Total lending to government (1) + (2)
(1)	(2)	(3)	
Advances to Treasury, and investments in government securities (b)	Investments in government and government guaranteed securities (c)	Lending to private sector (d)	
End of Dec.—			
1950 798 (160)	535 (168)	1,614	1,333
1951 732 (152)	605 (203)	1,899	1,337
1952 823 (218)	678 (267)	2,390	1,501

(a) Lending by the Bank of Italy to private customers amounted at the successive dates to 16, 18 and 17 milliardi respectively.

(b) The figures in brackets indicate the amounts (included in the totals) that were financed by the Bank of Italy out of the compulsory reserves of the banks deposited with the former in the form of cash.

(c) The figures in brackets indicate the amounts (included in the totals) that represented compulsory reserves of the banks invested directly by them in government securities.

(d) These figures include bills rediscounted by the banks and savings banks at the Bank of Italy and amounting at the successive dates to 86, 84 and 96 milliardi respectively. They do not include investments by the banks and savings banks in private securities. These amounted at the successive dates to 85, 124 and 200 milliardi respectively. Also excluded are funds lent abroad.

Interest Rates.

The easier credit conditions were reflected to some extent also in lower interest rates (see Table 7). No change was made by the Bank of Italy in the official rediscount and advance rates which had stood at 4 per cent since April, 1950 and April, 1949 respectively. On the whole, however, borrowing rates showed a downward tendency partly produced by the deliberate action of the Treasury in reducing the rate on its short-term paper (Treasury certificates) by roughly ½ per cent in May, 1952 (the first change since April, 1949) and partly by market forces. The average yield on medium and long-term government securities dropped from 6.23 per cent at the end of 1951 to 5.71 at the end of August, 1952, after which it bounced back, reaching 6.03 per cent at the end of the year or, that is, about the same level as had prevailed before the rise that took place in 1951. The gap be-

INTEREST RATES (End-of-year figures)

TABLE 7

	1950	1951	1952
	(Per cent)		
Rediscount rate of Bank of Italy	4.00	4.00	4.00
Advance rate of Bank of Italy . . .	4.00	4.00	4.00
Rate paid by Bank of Italy on compulsory reserves of banks deposited in cash (a)	4.75	4.75	4.25
Treasury certificates (10 mths.) (b)	4.71	4.71	4.17
Average yield on medium- and long-term government securities	6.04	6.23	6.03
Banks and savings banks (cartel rates):			
Sight deposits		0.50	
Ordinary time deposits (3-6 months)		1.50-2.00	
Special time deposits (12 months) (c)		3.00	
Unsecured credits		6.00-7.50	
Loans		4.75-7.00	
Discounts		5.25-6.75	

(a) In January, 1953 the Bank also lowered the rates paid on « free » deposits held with it by the banks and savings banks and other institutions, this being the first change in these rates since 1943. The rate paid on sight deposits remained unchanged at 0.50 per cent, but the rates on term deposits for 8 and 15 days were lowered by 1 per cent (from 2.50 to 1.50 and from 3 to 2 per cent, respectively), and 4 and 6 month term deposits which previously carried 3.50 and 4 per cent were abolished.

(b) The rates on certificates for shorter terms than 10 months were likewise lowered by about 0.50 per cent in May, 1952. The amounts of such certificates outstanding are, however, small.

(c) For longer periods the rate rises by 0.25 per cent for every additional 6 months up to a maximum of 3.50 for savings banks and 4.75 for certain special institutions.

tween the short-term rate fixed by the Treasury and the medium- and long-term rates set by the market was thus considerably widened, and it appeared from this and other evidence to which we shall refer immediately that the Treasury had fixed the short rate somewhat lower than the market would bear.

The rate paid by the Bank of Italy on compulsory reserves of the banks deposited with it in the form of cash was reduced (in May 1952) in proportion to the reduction in the Treasury certificate rate; and, in January, 1953, the Bank reduced, more drastically, the rates paid on « free » deposits (12). As in previous years the banks constituted more than half the increment in their com-

(12) See footnote (a) to Table 7.

pulsory reserves in the form of cash deposits (13) notwithstanding the slightly higher effective rate yielded by those constituted in the form of Treasury certificates (14). As a result of the subscription in the form of Treasury certificates to the issue, at the beginning of 1952, of medium-term (nine-year) government securities, and of the reduction later in the rate on the former, private and non-bank investors in Treasury certificates decreased their holdings of these in 1952, and the banks and savings banks increased theirs very little. The entire amount of the increase in the volume outstanding was accounted for by investments by the Bank of Italy of the compulsory reserves of the banks deposited with it in the form of cash. The Bank (15) invested the whole of the increment of compulsory reserves in this way in 1952, whereas in 1951 it had actually disinvested to a small extent. The distribution of Treasury certificates outstanding between the main groups of holders over the last three years was as follows:

	End of —		
	Dec. 1950	Dec. 1951	Dec. 1952
	(Milliards of lire)		
Private and non-banking	296	290	283
Banks and savings banks	391	460	463
Bank of Italy	160	152	218
T o t a l	847	902	964

We may probably infer that it was this unwillingness of the market to take up larger quantities of the short-term, relatively low-interest government paper that induced the step taken by the authorities in January, 1953 towards a tightening of the reserve requirements against deposits; the rules determining the ratios remained unchanged (the effective level now being about 23 per cent) but henceforth the reserves constituted in the form of

(13) See Table 9 below.

(14) The nominal rate on Treasury certificates is 4.00 per cent; those deposited as compulsory reserves earn a premium of 0.25 per cent, making the total rate equivalent to that paid on reserves deposited in the form of cash. Since, however, the nominal rate on certificates is « earned » at the beginning of the period, it is equivalent to a higher effective rate received at the end of the period. Treasury certificates deposited as compulsory reserves also carry the additional advantage of being tax exempt.

(15) See Table 8 below.

securities were to consist exclusively of Treasury certificates (16). It may be noted that in the previous year (1952), when all types of government securities were still eligible, the increment in compulsory reserves constituted in the form of securities had consisted of Treasury certificates to the extent of only just over 40 per cent.

So far as rates applied by the commercial banks were concerned, the cartel rates (the minimum rates chargeable to borrowers and the maximum rates payable to depositors) remained unchanged at the levels established in April, 1950. The Bank of Italy reports, however, that the banks' lending rates moved down closer to the minimum cartel rates, and that so far as deposit rates were concerned the situation of the two previous years continued to prevail. That is to say, keen competition among the banks for deposits, and the absence of action on the part of the authorities to enforce the cartel agreement, led to the payment of rates to important customers and on large sums that were far above those fixed by the cartel. (According to information obtained from other sources they sometimes reached 5 per cent on relatively short-term deposits). The writers of the Report content themselves with recording these facts and do not take any position on the very much discussed subject of the partial breakdown of the cartel agreement.

Cash Movements.

The cash resources which supported the heavy credit expansion in 1952 came from three sides.

The first was the Central Bank which, as in previous years, considerably increased the cash base of the economic system by net additional lending. This is analysed in Table 8 in terms of the principal items in the Bank's balance sheet leading to releases or with-

(16) The regulations concerning the cover required against circular cheques were also tightened. After December, 1952, the increase in circular cheques had to be covered to the extent of 100 per cent by government securities (instead of 60 per cent as previously), and from the middle of January, 1953 on the securities must consist exclusively of Treasury certificates.

Circular cheques are a relatively small item: the total volume outstanding at banks and savings banks at the end of 1952 was 136 milliard lire.

drawals of funds to or from the system. The analysis shows that additional financing by the Bank of the Treasury (91 milliards) to help cover the budget deficit was alone sufficient to take up the slack left by the deflationary effect of the running down of foreign balances (leading to decreased financing by the Bank to the extent of 25 milliards) plus the increase in the cash deposits (in respect of com-

policy of the commercial banks to which we shall come later. The total is in any case considerably less than the increment of new cash (127 milliards) provided by the Bank in the previous year.

At the same time, however, a *second* very important factor was at work, causing the cash inflow to the banks to rise more than in proportion to the addition to the cash base

BANK OF ITALY: FACTORS AFFECTING THE VOLUME OF CURRENCY IN CIRCULATION TABLE 8
(Milliards of lire)

	End of:			Variations: sources of increase (+) or decrease (-) in circulation	
	1950	1951	1952	1950-51	1951-52
I. Sources of release of funds by Bank of Italy:					
1. Lending to Government	638.5	580.1	604.9	- 58.4	+ 24.8
2. Investment of compulsory reserves	160.0	152.0	218.0	- 8.0	+ 66.0
<i>Total (1)+(2)</i>	<i>798.5</i>	<i>732.1</i>	<i>822.9</i>	<i>- 66.4</i>	<i>+ 90.8</i>
3. Foreign exchange and gold reserves	535.1	756.9	731.9	+ 221.8	- 25.0
4. Accommodation to banks, savings banks and special credit institutions (of which « crop collection » bills)	269.6 (152.3)	258.3 (151.6)	316.8 (180.9)	- 11.3 (- 0.7)	+ 58.5 (+ 29.3)
II. Sources of withdrawal of funds by Bank of Italy:					
1. Counterpart funds of American aid	- 119.1	- 54.3	- 12.3	+ 64.8	+ 42.0
2. Deposits held by banks in respect of com- pulsory reserves	- 238.0	- 285.4	- 352.1	- 47.4	- 66.7
3. Other deposits (of which banks and savings banks)	- 53.5 (- 33.5)	- 80.3 (- 60.5)	- 67.6 (- 46.9)	- 26.8 (- 27.0)	+ 12.7 (+ 13.6)
III. Other items (release +, withdrawal -)	- 27.4	- 35.5	- 58.1	- 8.1	- 22.6
<i>Total sources of release minus sources of withdrawal = currency in circulation</i>	<i>1,165.2</i>	<i>1,291.8</i>	<i>1,381.5</i>	<i>+ 126.6</i>	<i>+ 89.7</i>

pulsory reserves) of the banks (67 milliards). At the same time the counterpart funds of American aid — also a Treasury account — were decumulated (to the extent of 47 milliards). The Bank also discounted additional crop collection bills, and lent additional funds to the banks and saving banks in the form of advances and discounts of other than crop collection bills. The net result of all the movements of funds in and out of the Bank was to release additional cash to the extent of 90 milliards. This total includes, however, withdrawals from the Bank of private deposits, mostly of banks, which are more properly considered under the separate heading of the

of the economic system provided by the Central Bank. It came from the side of the public, and expressed itself in the very sharp decrease in the ratio of currency to deposits held by the public. In the earlier post-war years, there had also been a tendency towards such a decrease (see Table 5), reflecting the gradual return to more normal proportions after the distortions that had been caused by the effects of the war and the inflation. The movement had affected both savings deposits, which were slowly being reconstituted after their destruction by the inflation, and current accounts which we take as roughly equivalent to « deposit money ». The

rate of growth of total deposits had, however, slowed down in 1950 and the first half of 1951. Moreover, by the end of 1950 it had seemed that the upward movement in the ratio of current accounts to currency held by the public (roughly representing the propor-

sits to slow down, and a resumption of the tendency towards the holding, by the public, of a higher ratio of current accounts to currency. The ratio of current accounts to currency rose in the one year (from December, 1951 to December, 1952) from 1.05 to 1.20,

COMPULSORY RESERVES OF BANKS (a); AND PRIMARY (FREE) RESERVES,
AND INDEBTEDNESS TO BANK OF ITALY, OF BANKS AND SAVINGS BANKS
(End-of-year data)

TABLE 9

	1949	1950	1951	1952
1. Compulsory reserves (milliards of lire):				
Cash	239.2	238.0	285.4	352.1
of which: invested in securities by Bank of Italy	(193.1)	(156.8)	(149.0)	(213.6)
Securities	139.7	171.8	203.3	267.4
<i>Total</i>	<i>378.9</i>	<i>409.8</i>	<i>488.7</i>	<i>619.5</i>
<i>Ratio to deposits of banks (per cent)</i>	<i>22.9</i>	<i>23.1</i>	<i>22.8</i>	<i>23.1</i>
2. Primary (free) reserves (milliards of lire):				
Cash in hand	40.3	52.6	65.8	66.8
Deposits at Bank of Italy (b)	40.8	33.5	60.5	46.9
Deposits at other institutions (c)	42.6	18.2	29.8	36.8
<i>Total cash reserves</i>	<i>123.7</i>	<i>104.3</i>	<i>156.1</i>	<i>150.5</i>
Unutilized lines of credit at Bank of Italy (d)	82.9	105.9	136.3	131.8
Treasury certificates (e) in portfolio	49.3	48.7	72.0	48.9
<i>Total primary reserves</i>	<i>255.9</i>	<i>258.9</i>	<i>364.4</i>	<i>331.2</i>
<i>Ratio of cash to deposits of banks and savings banks (per cent)</i>	<i>6.3</i>	<i>4.7</i>	<i>5.8</i>	<i>4.5</i>
<i>Ratio of primary reserves to deposits of banks and savings banks (per cent)</i>	<i>13.1</i>	<i>11.6</i>	<i>13.6</i>	<i>9.9</i>
3. Indebtedness to Bank of Italy (milliards of lire) (f) .	59.3	97.3	86.7	113.5
of which: rediscounts	(8.4)	(21.5)	(11.9)	(7.7)
advances (g)	(45.9)	(70.9)	(71.7)	(100.7)

(a) The compulsory reserve requirements do not apply to savings banks.

(b) Excluding compulsory reserves.

(c) Treasury, *Cassa Depositi e Prestiti*, Postal Administration.

(d) Equals difference between amount of credit opened (against deposits of government securities) and amount utilized.

(e) *Buoni del Tesoro ordinari*, of which maturities do not exceed 12 months.

(f) Excluding rediscounts of crop collection bills.

(g) The remainder of the total consists of advances for covering adverse balances in the clearings (*prorogati pagamenti*).

Note: The figures in this table do not always exactly coincide with those given in other tables owing to discrepancies between the times of registering items in the accounts.

tions in which the public holds its « cash balances » in the form of bank deposits and currency respectively) might have come to a halt. The 1952 movement, or more accurately the movement after the middle of 1951, thus represented both a break in the tendency for the rate of growth of total depo-

and the ratio of total deposits to currency from 1.84 to 2.12 (17).

(17) The ratios are slightly understated, and the changes in the ratios from year to year may be slightly under- or over-stated, by reason of the fact that the figures for currency in circulation include « cash in hand » of the banks and other credit institutions. The error on this account is, however, very small.

This source of cash inflow to the banks would have had to be counteracted by a correspondingly smaller creation of new cash by the Central Bank if the latter had considered it necessary to keep the volume of credit from expanding as much as it did.

The *third* factor aiding the expansion of bank lending in 1952 derived from the policy of the commercial banks themselves — their willingness, not only to increase their indebtedness to the Bank of Italy, but also to diminish the ratio of their free cash and near-cash reserves to deposits (see Table 9). The running down of their free cash reserves at the same time as deposits were increasing caused the free cash ratio to fall from 5.8 per cent at the end of 1951 to 4.5 per cent at the end of 1952. And if we take the ratio to deposits of free cash *plus* the resources that are most nearly equivalent to cash (*i.e.* the unutilized margins of lines of credit at the Bank of Italy which represent the extent to which the banks can draw additional advances from the latter, and short-term government paper (18) in portfolio), or what the Bank of Italy takes as roughly definable as « primary reserves », we find that this fell over the one year from 13.6 per cent to 9.9 per cent, this latter figure being almost as low as the figure (9.1) reached in June, 1951 (19) when the credit situation was generally regarded as being very tight and the banks were evidently under considerable pressure. The fall in 1952 was largely concentrated in the last quarter of the year, which was also the period when loans increased most rapidly; at the end of the third quarter the « primary » reserve ratio had stood at 14 per cent.

In its analysis of the developments we have just described the Bank of Italy seeks to answer three interconnected questions:

(18) Both the short-term, and the medium- and long-term government securities held by the banks in portfolio are eligible for deposit at the Bank of Italy against the opening of additional lines of credit. Since, however, both types serve also as guarantees for various other types of operation, and up until recently both were eligible as compulsory reserves against deposits, it is not possible to draw a clear dividing line between the part that should be included in « primary » reserves and the part that should not. The line drawn by the Bank of Italy is admitted to be a somewhat arbitrary one.

(19) At that date the free cash reserve ratio was only 2.9 per cent.

1. Why did bank deposits expand so rapidly between mid-1951 and the end of 1952?

2. How is it that the volume of deposits, and the total volume of money, could increase so much in 1952 without affecting the price level more markedly given the relatively small increase in production (or in disposable income? (20).

3. How is it that such a heavy increase in bank lending could take place without being reflected in the investment figures?

Causes of the High Rate of Growth of Deposits.

The Bank of Italy in its attempt to explain the development of deposits over the last few years speaks of the « formation of liquid balances » by the public being greater at one period than at another. Thus it suggests (21) that « the speculative activity of the first half of 1951 had worked against the formation of liquid balances in favour of the accumulation of stocks of goods both by firms and by individuals », and (by implication) that in 1952, since there was no such accumulation of stocks, the available « liquid resources » became deposits instead of being spent on stocks of goods.

Since the currency and the bank deposits outstanding in the system must always be in somebody's liquid balances, *i.e.* what is released from one person's balance always appears in somebody else's, unless it is extinguished by being used to repay a bank loan, the heavier formation of liquid balances by the public in 1952 can only refer to a change in the *form* in which the public held its balances. That is to say it must mean *either* a shift from one form of « active balance » to another (from currency to current accounts at the banks), *or* a transformation of « active balances » into « idle balances » (held in the form of savings deposits). If the « formation of liquid balances » was of this latter kind in 1952 we should expect it to be reflected predominantly in the figures for savings deposits.

(20) See footnote (7), p. 98, above.

(21) *Cf. op. cit.*, p. 314.

In actual fact savings deposits and current accounts increased in roughly the same proportion. The writers of the Report believe, however, that one reason for the rapid growth of current accounts in 1952 was that in that year a larger part of these accounts was in the nature of savings deposits (22). This would mean too that the statistics overstate the growth in the volume of money, and would thus be a partial answer also to our second question.

An explanation of the way in which « genuine » current accounts may have been affected by stock movements must be sought in the possible influence of such movements on the proportions between the two types of cash balance held by the public: the possibility, for instance, that the accumulation of stocks causes a shift of funds away from people who normally hold the bulk of their cash balances in the form of bank deposits towards people who hold them in the form of currency, and *vice versa*, for a decumulation of stocks. Such shifts may indeed quite well occur in a country where not all groups of the population are equally in the habit of using the banks. As, however, it is supposed that there was no net decumulation of stocks in 1952, the role of stock movements in this particular case can only have been that the movement in the opposite direction (*i.e.* the net accumulation) in 1950 and 1951 had served in those years to neutralise the effect of other factors which were working in the direction of increasing the ratio of current accounts to currency, and that no such neutralising influence was present in 1952. The Bank of Italy does not indicate that there are any grounds for assuming the presence in 1952 of other special factors (*i.e.* other than stock movements) that might account for marked shifts of funds in that year from groups that hold their cash balances predominantly in the form of currency to groups that hold them predominantly in the form of bank deposits: it is not, for example, indicated that there was on balance for the year a shift from the

(22) *i.e.* that they were not balances « held for satisfying the usual requirements of business turnover » but « balances awaiting investment » (p. 356).

agricultural to the industrial sector (23) or from wages to profits (indeed the movement in respect of the latter seems to have been in the opposite direction).

Since, however, there are good reasons for expecting a trend factor, working in the direction of raising the ratio of current accounts to currency held by the public, to exist, it is a highly plausible explanation that this factor was temporarily masked by the special events (as reflected in stock accumulation) of 1950 and 1951.

This long run tendency for the ratio of current accounts to currency to rise is associated with the effect of increased industrialisation and urbanisation in causing a higher proportion of total cash balances to be held in the form of banks deposits rather than in the form of currency, with the growing importance in total expenditures of heavy single items (such as durable goods and rents) that are more likely to be paid for by cheque than in cash, and finally with the general spread of the cheque using habit to wider sections of the population. As may be seen from Table 5 (Column 6) the ratio, after recovering from the diminution which it had undergone in Italy as elsewhere, during the war and the inflation, is now considerably above the level of 1938. Italy is, however, far from having reached the situation which prevails, for example, in the United Kingdom, where the ratio of bank deposits to currency held by the public is nearly 5:1, and where — what is more significant — this ratio shows a very high degree of stability from year to year.

The tendency towards a continual increase in the ratio merits attention also in terms of its consequences for monetary policy. Since it is a source of a cash inflow to the banks, and therefore of additional lending power, which is not immediately under the control of the monetary authorities, it has to be taken into account by the latter as a factor influencing the amount of cash they themselves can release to the system (or the amount they must withdraw from it) in the effort to avoid

(23) The role of such shifts, towards agriculture in the summer months and away from it later, is examined in regard to its seasonal effects on the circulation.

inflationary pressure. This is the more so since the increase in the public's ratio of deposits to currency also increases the « coefficient of expansion » of deposits with respect to Central Bank cash, *i.e.* the volume of new deposits that the banks can create on the basis of a given increment of new cash provided by the Central Bank.

To some extent the process of economic development itself provides a compensating force. It is one on which the Bank of Italy comments in its present Report (p. 354-5); *i.e.* the tendency for economic development to cause the holding of larger cash balances relative to income, partly because more emphasis is placed on the need for « liquidity », and partly because more transactions are carried out in money form (owing for example to the decreasing importance of independent workers, of auto-consumption in agriculture, and of economic activity in the home). This provides at least part of the answer to our second question of why, not only in 1952 but also in previous years, the volume of money could increase much more than the real national income without causing pressure on the price level.

Since there is, however, no reason for expecting that this second effect of economic development will always automatically offset the first, it remains true that a high rate of growth of deposits — which has been welcomed by the Bank of Italy as a very favourable sign in its Reports of previous years — may be the source in the future of a need for added watchfulness on the part of the monetary authorities.

Sources of the Increased Demand for Bank Credit.

The third problem is that raised by the fact that there was such a heavy increase in bank lending to the private sector of the economy in spite of the relatively small increase in production and investment. As we have already seen, bank lending to the private sector increased by 26 per cent in 1952 as compared with an increase of 18 per cent in 1951. The increase took place almost entirely in the last three quarters of the year and was particularly marked in the last quarter; and the statistics

of bank lending by branches of activity show increases in all branches. In money terms (which are what are relevant here) the gross national income is estimated to have risen by only 5 per cent and gross investment by less than 3 per cent from 1951 to 1952, as compared with increases of 16 per cent and 26 per cent respectively from 1950 to 1951. As the Bank of Italy remarks (24), the growth in investment in plant and equipment, the additional investment in stocks (which was on balance for the system as a whole believed to be nil), and the increase in the general level of activity, is, according to these figures, insufficient alone to explain such a heavy increase in borrowing from the banks. It does not appear, either, that the increase was offset by a diminution in the volume of new funds drawn from other sources. A synthesis of the volume of funds borrowed from the banks and savings banks, the « special credit institutions », the securities market, and certain other institutions (25) shows that the increment of new funds drawn from all those sources together amounted to 957 milliard lire (of which 491 came from the banks and savings banks) in 1952, compared with an increment of only 656 milliard (of which 285 came from the banks and savings banks) in 1951 (26).

The Bank of Italy points, therefore, especially to two other factors that it presumes to have been responsible for part of the increase in bank lending to the private sector (27). The first is the reduction in self-finance due to the lower profits. According to the Bank's sample taken from balance sheets, however, profits were only slightly lower in 1952 than in 1951 (28), when the level was exceptionally high, and they were still far above those for 1950; and yet 1950 was a year both of greater expansion in investment and general activity, and of a smaller increase in bank loans, than took place in 1952. It seems rather

(24) *Op. cit.*, pp. 339-40.

(25) The *istituti di categoria* (central organisations of the savings banks and « people's banks »), certain minor credit institutions, the *Istituto per la Ricostruzione Industriale*, and the *Cassa Depositi e Prestiti*.

(26) *Op. cit.*, p. 350.

(27) *Op. cit.*, pp. 340 ff.

(28) See p. 93 above.

unlikely, therefore, that this factor can have been of more than modest significance.

The second factor is an increase in the volume of credit given by firms to their customers. It is admitted that, except in special circumstances to which we shall refer presently, the additional credit, in order to lead to a net increase in borrowing from the banks, must be extended to units which do not have recourse to bank credit — since otherwise its effect in increasing bank borrowing by those who give the credit would be compensated by its effect in decreasing bank borrowing by those who receive it. The Report lists three cases in which it is clear that no such compensation takes place: the granting of credit to consumers, the granting of trade credit to foreign buyers of Italian goods, and the granting of trade credit to the Government. Although no direct statistics are available, it is believed that consumers' credit due to instalment buying increased very considerably in 1952; and credit to foreign buyers is said to have been given especially by exporters of capital goods. It is also supposed that government purchases not accompanied by immediate cash payments gave rise to additional need for credit in the sectors of naval construction, electrical materials, munitions and textile products; this would mean that part of the new lending to the private sector went indirectly into financing the government.

Partly as an extension of the foregoing argument, the Bank goes on to describe one, or perhaps two, further ways in which the volume of bank lending may have been increased. It says that, in spite of giving additional credit to consumers, traders, « either by reducing their stocks or by shifting part of the financing of those stocks to the producers » (29), may have accumulated « liquid balances » which they deposited with the banking system — a factor which has already been mentioned above in connection with the development of deposits — and which were in turn lent by the banks to the producers. The argument concerning the trade credit element (we shall come to the stock liquidation element later) follows a general thesis propounded by the writers of the Report that

at some times, when little recourse is had to trade credit, traders « invest their liquid balances directly » with the result that producers have a correspondingly smaller need to borrow from the banks, while at other times, when more recourse is had to trade credit, the traders who receive the credit « accumulate larger liquid balances which are deposited with the banks and redistributed by the latter to the producers », the banks being thus « inserted in the credit circuit ». In this way both sides of the bank balance sheets are lengthened by a process which does not imply any increase in investment. The explanation of how a marked lengthening or shortening can occur within a relatively short period rests on the assumption that trade credit tends to increase when demand and prices are stable or falling, and to decrease when demand and prices are rising — this being the element which is supposed to have distinguished conditions in 1952 from those in 1951.

More broadly, it would seem to us that the situation in which both sides of bank balance sheets are swollen from one year to the next by forces which do not derive from any increase in the level of productive or investment activity may occur under the following conditions — and we are here incorporating the stock liquidation factor which the Report mentions but does not consider further (30):

(a) That the volume of trade credit expands in the manner described, and that the additional trade credit is taken by those who do not borrow from the banks and is given by those who do, or is taken by those who have borrowed only to a small extent in relation to their total financial needs, and is given by those who borrow to a larger extent.

(b) That in the year concerned there are sharply contrasting movements — *more* sharply contrasting than in the previous year — in the levels of activity as between different firms so that some are contracting (decumulating stocks, or failing to reinvest depreciation allowances), and consequently accumulate liquid balances, while others are expanding and are consequently in need of more funds; and again either that

(29) *Op. cit.*, p. 341. The italics are ours.

(30) Cf. the quotation above (first column of this page).

the contraction process affects firms that do not borrow from the banks while the expansion process affects those that do, or that the contraction process in the firms concerned goes so far that the proceeds of their stock liquidation, etc., exceed the amounts that they can absorb by repaying their bank loans, so that they accumulate bank deposits in addition (31).

(31) A more advanced stage of recession — which was surely not reached in Italy in 1952 — would be that where, over the system as a whole, such heavy losses were made that they more than absorbed the proceeds of stock liquidation, etc., so that bank loans increased rather than decreased.

It is still questionable whether these conditions were sufficiently widespread over the Italian economy in 1952 to contribute much towards the explanation of the phenomenon under discussion.

On the whole, even when we allow for the contributions that each and all of the factors mentioned by the Bank of Italy may have made towards increasing the volume of bank lending in 1952, we are left wondering whether the expansion in economic activity can really have been so modest, and the increase in investment so small, as the official national income statistics indicate.