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EUROPEAN CENTRAL BANK

MONTHLY BULLETIN January 1999

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Foreword

The Monthly Bulletin of the European Central Bank (ECB), the first issue of which you now have at hand, is one of the most important means of written communication for the ECB. In its Monthly Bulletin the ECB will explain to the public the monetary policy decisions taken by the Governing Council of the ECB. Through a comprehensive economic analysis, it will aim at enhancing the transparency of monetary policy. It will thus constitute an indispensable form of support for a successful single monetary policy of the "Eurosystem", comprising the ECB and the national central banks (NCBs) of the 11 EU Member States which have adopted the euro from the start of Stage Three of Economic and Monetary Union. The Monthly Bulletin will be translated by the NCBs. The publication of the Monthly Bulletin will also fulfil the ECB's obligation to publish at least quarterly reports on the activities of the European System of Central Banks (ESCB) (Article 15.1 of the Statute of the ESCB).

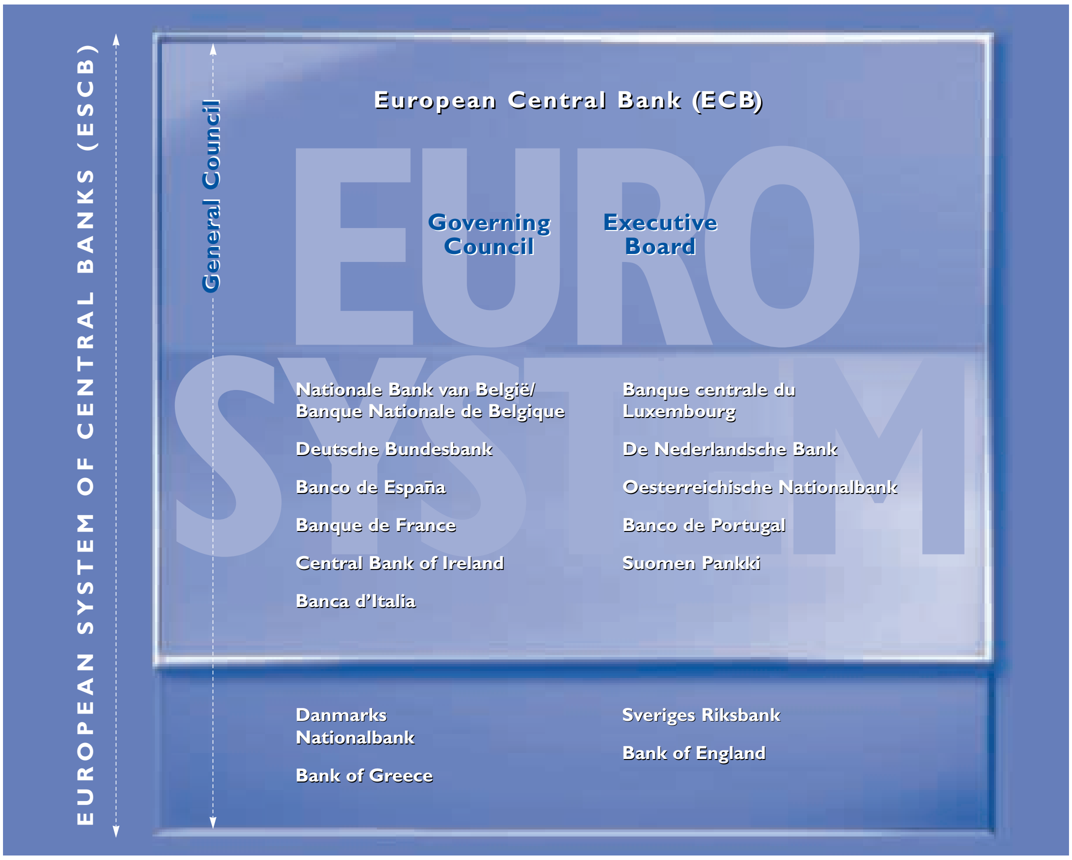
While being subject to further development and improvement, the contents of this first issue of the Monthly Bulletin should set a standard for future issues. The "Editorial" will summarise the aspects on which monetary policy decisions are based, explaining these from the point of view of the stability-oriented monetary policy strategy of the Eurosystem, whether or not the Governing Council of the ECB decides to change the ECB interest rates. These aspects will be further expounded in the section on "Economic developments in the euro area". In the quarterly version of the Monthly Bulletin – to be published in March, June, September and December every year – this section will be more extensive and will also cover developments in fiscal policies. The third standard component of the Monthly Bulletin is a section on "Euro area statistics", which will contain a comprehensive set of tables and charts supplying important economic information on the euro area. Furthermore, the Monthly Bulletin will include a chronology of monetary policy measures, as well as material informing readers about the ECB's publications. We shall also publish articles on various matters related to the design and conduct of monetary policy and on other matters relevant for the ECB in the Monthly Bulletin. In particular, issues which are relevant for the success of the single monetary policy and the stability of the euro will be addressed, including such themes as wage and labour market developments, fiscal policies and structural rigidities. Other central banking themes will also be addressed.

With all these efforts aimed at providing comprehensive information, our intention is to demonstrate that the ECB will do its utmost to perform its task of maintaining price stability for the benefit of all European citizens to ensure that their confidence in their new currency is well founded.

Frankfurt am Main, January 1999

Willem F. Duisenberg
President

The Eurosystem and the European System of Central Banks (ESCB)



The Treaty establishing the European Community and the Statute of the European System of Central Banks and of the European Central Bank confer several tasks upon the European System of Central Banks (ESCB) which have to be carried out by the European Central Bank (ECB) and the national central banks (NCBs). To enhance transparency and enable the public to grasp more easily the very complex structure of European central banking, the Governing Council of the ECB has decided to adopt the term "Eurosystem" as a user-friendly expression denoting the composition in which the ESCB performs its basic tasks.

The Eurosystem

The Eurosystem comprises the ECB and the NCBs of the Member States which have adopted the euro in Stage Three of Economic and Monetary Union (EMU). There are currently 11 NCBs in the Eurosystem (see the chart above). If and when all 15 Member States participate in the euro area, the term "Eurosystem" will become a synonym for the ESCB.

The Eurosystem is governed by the Governing Council and the Executive Board of the ECB.

The ***Governing Council*** comprises all the members of the Executive Board and the governors of the NCBs of the Member States which have adopted the euro.

The ***Executive Board*** comprises the President, the Vice-President and four other members appointed by the Heads of State or Government of the Member States which have adopted the euro.

The European System of Central Banks (ESCB)

The ESCB is composed of the ECB and the NCBs of all 15 Member States, i.e. it includes, in addition to the members of the Eurosystem, the NCBs of the Member States which have not adopted the euro from the start of Stage Three of EMU.

The ESCB is governed by the Governing Council and the Executive Board of the ECB and, as a third decision-making body of the ECB, by the General Council.

The ***General Council*** comprises the President, the Vice-President and the governors of all 15 NCBs.

Editorial

The Eurosystem – comprising the European Central Bank (ECB) and the national central banks of the 11 Member States which adopted the euro on 1 January 1999 – has assumed the task of conducting the single monetary policy for the euro area. On 22 December 1998 the Governing Council of the ECB announced the ECB interest rates to be applied under the new regime and indicated that it regarded these rates as appropriate for the foreseeable future. This announcement was deemed important to eliminate uncertainties about the monetary policy stance of the Eurosystem at the start of Stage Three and to contribute to a smooth changeover to Monetary Union. Three decisions were adopted in this context on 22 December 1998 and confirmed on 7 January 1999 by the Governing Council.

First, it was decided that the initial main refinancing operations would be conducted as fixed rate tenders at a rate of 3%. Already in early December 1998 the Governing Council had judged this level to be compatible with the maintenance of price stability in the euro area over the medium term. The arguments leading to the decision are summarised below and are elaborated in more detail in the section on "Economic developments in the euro area" in this Bulletin.

Second, the interest rate for the marginal lending facility was set at 4.5% and the interest rate for the deposit facility was set at 2% at the start of Stage Three, i.e. 1 January 1999. The asymmetric character of this corridor around the main refinancing rate underlines the intention expressed by the Governing Council to continue to apply a level of 3% for the main refinancing rate, which is very low by historical standards, for the foreseeable future.

Third, the Governing Council decided to narrow temporarily the corridor between the interest rates on the two standing facilities to 50 basis points. This was achieved by setting the marginal lending rate at 3.25% and the deposit facility rate at 2.75% for the period from 4 to 21 January 1999. The purpose of this measure was to smooth the adaptation of market participants to the integrated money market in the euro area during the initial days of Monetary Union. However, since the maintenance of such a narrow corridor over a prolonged period of time may hamper the development of an efficient euro area money market, the Governing Council has also announced that it intends to terminate this transitional measure following its meeting on 21 January 1999.

The aforementioned decisions on the levels of the ECB interest rates were taken in accordance with the announced monetary policy strategy, which is presented in detail in this Bulletin in the article entitled "The stability-oriented monetary policy strategy of the Eurosystem". This strategy is based on a quantitative definition of price stability, namely that an annual increase in the Harmonised Index of Consumer Prices (HICP) of below 2% can be considered as being compatible with this primary objective of monetary policy. Furthermore, to achieve this objective, the strategy is based on two pillars. The first consists in a prominent role for money, as signalled by the announcement of a quantitative reference value of 4½% for the growth rate of the broad monetary aggregate M3 which is regarded as being compatible with price stability. The second comprises a broadly based assessment of the outlook for price developments and the risks to price stability using financial and other economic indicators.

For almost two years now HICP increases have been in line with the Eurosystem's definition of price stability. In November 1998 the 12-month rise in the HICP was 0.9%. Taking a forward-looking perspective, the environment for price developments is determined by the following factors. With regard to monetary growth, the first pillar of the strategy, it can be observed that M3 showed a stable trend in 1998. The three-month moving average of the 12-month growth rate of M3 up to November 1998 stood at around 4.7%. This rate of monetary expansion is very close to the reference value of 4½%.

With regard to other economic indicators, the second pillar, financial indicators support the view that market participants expect the current climate of price stability to continue in the medium to longer term. At the start of Stage

Three nominal short-term and long-term interest rates in the euro area have reached levels which are very low by historical standards. Real interest rates are also significantly below their long-term averages.

With regard to indicators for real economic activity in the euro area, many uncertainties surround the outlook for the world economy at the start of Stage Three. These uncertainties have tended to have a negative impact on industrial confidence and have contributed to a less optimistic view of future economic growth in the euro area. More recently a decline has also been observed in outstanding orders and, to a lesser extent, in capacity utilisation. Furthermore, Eurostat's first estimate of real GDP growth in the third quarter of 1998 was 2.4% on an annual basis, following an increase of around 3% in the first half of last year. All this has fostered expectations of a slowdown in the growth of economic activity in the short term.

At the same time, however, consumer confidence resumed its earlier increase and the annual increase in retail sales showed an acceleration in the months up to September 1998. Furthermore, the increase in employment led to a further small reduction in the unemployment rate (from 11.0% in the summer months to 10.8% in November). Subdued wage growth in the first half of 1998 may have supported this. Low wage growth was also a major factor underpinning the low rate of increase in the HICP. Another key – though possibly temporary – factor which has contributed to bringing down HICP inflation to its current levels was the falling trend in energy and other commodity prices.

On balance, the evidence suggests that there are no indications of significant upward or downward pressures on price developments at this juncture. Some risks to price stability can nonetheless be identified. On the downward side, the possibility cannot be ruled out that the negative repercussions of recent global developments on economic growth in the euro area could turn out to be more serious than is currently anticipated. This might also have a further dampening effect on import and domestic prices. On the upward side, wage demands in excess of labour productivity growth and a relaxation of the fiscal stance in the euro area could represent sources of inflationary risk in the future. Overall, however, the outlook for price developments in the euro area can be regarded as being broadly balanced.

Against this background, the Governing Council confirmed at its meeting on 7 January 1999 that a level of 3% for the Eurosystem's main refinancing rate should, for the foreseeable future, be appropriate in order to maintain the current climate of price stability in the euro area, in line with the Eurosystem's primary objective.

As is also observed in this Bulletin in the article entitled "The euro area at the start of Stage Three", the euro area enjoys, in many respects, a favourable starting position, and price stability is one aspect of this. At the same time, there is also ample evidence to suggest that the euro area faces many structural challenges, first and foremost the problem of high unemployment. These challenges will need to be addressed by means of determined structural adjustment measures taken in other areas of economic policy. This will also be vital for ensuring the stability of the euro over the longer term. The contribution of monetary policy consists in maintaining price stability and establishing confidence in the continuation of its efforts, thereby creating the conditions necessary for the sustained, non-inflationary growth of output and employment.

The euro area at the start of Stage Three

The start of the single monetary policy of the Eurosystem for the euro area marked the beginning of a new era in the process of European economic integration. While important fields of economic policy, including fiscal policy, will remain primarily the responsibility of the 11 participating Member States, monetary policy is now determined at the euro area level. When deciding on monetary policy, the Governing Council of the European Central Bank (ECB) will focus on euro area-wide economic data within the framework of its monetary policy strategy adopted in late 1998 (see "The stability-oriented monetary policy strategy of the Eurosystem" in this Bulletin). Many of the key features of the euro area as a whole, such as the size and openness of the economy and the financial structure, are quite different from those of the individual Member States and should rather be compared with those of the United States and Japan. These characteristics should be borne in mind when undertaking economic analyses of the euro area. In order to familiarise the public at large with the euro area economy, this article highlights its key features. In addition, it describes the macroeconomic situation prevailing at the start of Stage Three, so as to provide a starting-point for the first, more detailed commentary on recent developments in the euro area (see "Economic developments in the euro area" in this Bulletin).

1 Key features of the euro area

The euro area: a large economy with a significant weight in the world economy

Putting the euro area into perspective (see Table 1), the most striking feature is that it comprises formerly small and medium-sized economies, which have joined together to form an economy with a large internal market. Indeed, with a share of world GDP of 15%, the euro area is one of the largest economies in the world, possessing a significant purchasing power which is matched only by that of the United States. In comparison, the largest Member State in the euro area accounts for only just over 4% of world GDP, while the individual shares of the smaller ones do not exceed 1%.

Being a large economy, the "degree of openness" of the euro area is much smaller than that of the individual Member States. With a ratio of exports of goods to euro area-wide GDP standing at around 14% (after adjusting for intra-euro area trade), the euro area's degree of openness is by and large comparable to that of the United States and Japan. This contrasts with the position of individual euro area countries, which were previously seen as "small or medium-sized open economies", with, for example, export ratios (including intra-euro area trade) ranging from 19% to 62%, thus giving an average for the countries in the euro area as a whole of around 35%. The share of the euro area in total world exports (of goods) amounts to almost 16%, which substantially exceeds the shares of both the United States and Japan. Machinery and transport equipment, other manufactured articles and chemicals accounted for the bulk of trade effected with, in order of their share of trade, the United Kingdom, the United States, Switzerland and Japan, which together account for a large part of euro area external trade. For the euro area as a whole, trade in services is less significant and it is estimated not to have exceeded 4% of GDP in 1997.

Similarities to and differences from the United States and Japan

When considering other features of the euro area, it may be more appropriate to make comparisons with the United States and Japan rather than with the individual Member States, and to point to areas of similarity and differences. Patterns of production are broadly similar to those of the United States and Japan. Primary production, such as agriculture, fishing and forestry, accounts for around 2% of total output in all three economies. The services sector in the euro area accounts for about 67% of total production, which is a smaller share than in the United States (72%) but larger than in Japan (59%). The industrial sector (including construction) accounts for 31% of total production in the euro area, which in turn is more than in the United States but less than in Japan.

In terms of size and structure, the government sector in the euro area differs significantly from those of the United States and Japan. As represented by the share of government expenditure in GDP, the government sector is significantly larger in the euro area (49%) than in either Japan (39%) or the United States (35%). To a large extent, this can be explained by the

Table 1

Key characteristics of the euro area

	Reporting period	Unit	Euro area	United States	Japan
Population	1998	mn	292	270	127
GDP (share of world GDP) [1]	1997	%	15.0	20.2	7.7
Sectors of production					
Agriculture, fishing, forestry	1993	% of GDP	2.4	1.7	2.1
Industry (including construction)	1993	% of GDP	30.9	26.0	39.2
Services	1993	% of GDP	66.7	72.3	58.7
General government					
Receipts	1998	% of GDP	46.7	35.9	33.0
Social security contributions	1998	% of GDP	17.0	9.4	11.1
Expenditure	1998	% of GDP	49.1	34.5	38.6
Current transfers to households	1998	% of GDP	20.2	13.7	15.7
Exports of goods [2]	1997	% of GDP	13.6	8.5	10.0
Imports of goods [2]	1997	% of GDP	12.0	11.1	8.1
Exports (% of world exports) [2]	1997	%	15.7	12.6	7.7
Bank deposits [3] [4]	End-1997	ECU bn	4,657.9	3,953.4	3,663.4
	End-1997	% of GDP	83.9	55.3	98.8
Domestic credit [4] [5]	End-1997	ECU bn	7,128.5	5,881.5	4,710.8
	End-1997	% of GDP	128.5	82.2	127.1
Claims on the private sector	End-1997	ECU bn	5,125.9	4,931.1	4,033.6
Claims on the general government	End-1997	ECU bn	2,002.6	950.4	677.1
Domestic debt securities	End-1997	ECU bn	5,002.4	11,364.0	4,015.2
	End-1997	% of GDP	90.2	164.7	108.5
Issued by the private sector	End-1997	ECU bn	1,897.9	4,729.3	1,192.4
Issued by the public sector	End-1997	ECU bn	3,104.4	6,634.7	2,822.9
Stock market capitalisation [6]	Oct. 1998	ECU bn	3,190.9	9,679.7	3,300.9
Real GDP growth	1998	%	3.0	3.3	-2.5
CPI inflation [7]	Nov. 1998	%	0.9	1.5	0.8
Unemployment rate (% of labour force)	Nov. 1998	%	10.8	4.4	4.4
Broad money growth [8]	Q3 1998	%	4.4	7.4	3.3
Three-month interest rate	End-1998	%	3.25	5.00	0.18
10-year government bond yield	End-1998	%	3.94	4.70	2.02
General government					
Surplus (+) or deficit (-)	1998	% of GDP	-2.3	1.4	-5.5
Gross debt	1998	% of GDP	73.8	59.3	115.6
Current account balance [9]	1997	% of GDP	1.1	-1.7	2.3

Sources: Eurostat (population, stock market capitalisation, real GDP, euro area data for exports, imports, inflation (HICP), unemployment and current account balance), European Commission - autumn 1998 forecasts (shares of world GDP, general government data (calendar year basis)), OECD (sectors of production), IMF (exports, imports, bank deposits, domestic credit, gross debt for the United States and Japan), BIS (domestic debt securities), national data (for the United States and Japan: CPI inflation, unemployment, broad money growth, three-month interest rate, 10-year government bond yield, current account balance) and ECB (for the euro area: broad money growth, three-month interest rate, 10-year government bond yield).

1) *At constant prices and purchasing power standards in 1997; euro area: 1990 prices.*
2) *Excluding intra-euro area trade; exports: f.o.b.; imports: c.i.f.*
3) *Euro area: total deposits with MFIs; United States: demand, time and savings deposits in banking institutions; Japan: demand and time deposits in deposit money banks.*
4) *Euro area data for bank deposits and domestic credit are calculated on the basis of the irrevocable euro conversion rates announced on 31 December 1998.*
5) *Euro area: MFI loans to and holdings of securities of euro area residents; United States and Japan: domestic credit.*
6) *United States: the New York exchanges (NYSE and Nasdaq); Japan: Tokyo and Osaka exchanges.*
7) *HICP for the euro area; national data for the United States and Japan.*
8) *Euro area: M3 aggregate; United States: M2 aggregate; Japan: M2 and CDs.*
9) *Provisional data for the euro area.*

existence of different social security systems. Government current transfers to households in euro area countries, as a share of GDP, are relatively high compared with the United States and Japan. Another noticeable difference is that the proportion of GDP devoted to the provision of collective services by the government sector is also higher in the euro area than in either the United States or Japan. Also, with respect to the structure of government receipts, in the euro area and in Japan social security contributions represent about one-third of the government's current revenue, compared with only one-quarter in the United States. As regards tax income, the governments of both the United States and Japan rely more on direct taxation, whereas in the euro area indirect taxes represent a higher share of tax revenue.

Turning to a number of key monetary and financial indicators, several structural differences between the euro area's financial system and the financial systems of the United States and Japan may be noted. The key difference, in particular from the United States, lies in the relative roles played by banks and securities markets. Whereas the euro area's financial system is predominantly based on banking products and equity financing plays only a limited role, in the United States equity and debt securities markets provide the principal means of financing and saving.

This general picture of the financial structure of the euro area can be illustrated by reference to various indicators (see Table 1). Bank deposits, if measured relative to GDP, are more significant in the euro area (84%) than in the United States (55%), but less important than in Japan (99%). Similarly, the outstanding amount of domestic bank credit, both in absolute terms and relative to GDP, is far larger in the euro area than in the United States, although it is comparable, as a share of GDP, to that in Japan. In the euro area a relatively large amount of bank credit is extended to general government. By contrast, the amount of domestic debt securities relative to GDP in the United States far exceeds the amounts in either the euro area or Japan. In absolute terms, the outstanding amount of domestic debt securities in the United States, at ECU 11,364 billion, was more than twice that in the euro area at the end of 1997, and the difference is even more pronounced in terms of securities issued by the private sector. Finally, stock market capitalisation is also far higher in the United States than in the euro area and Japan.

Labour market characteristics also differ substantially between the euro area and the two other economies. The latest overall unemployment rate in the euro area (10.8%) is far higher than that in the United States (4.4%), and differences are accounted for by a host of factors, including structural features of the two labour markets, such as wage and non-wage labour costs, employment protection legislation and the scale and duration of unemployment benefits. From a medium-term perspective, experience also suggests that, for a comparable level of real GDP growth, the euro area has experienced much weaker employment growth than the United States. Also, by contrast with the United States, there has been a clear asymmetric response to fluctuations in economic activity, such that each downturn has brought about a higher level of unemployment in the euro area. However, labour markets are notoriously difficult to compare by referring to measured unemployment rates alone. This is particularly true in the case of Japan, where, despite persistent weakness of the economy, the official unemployment rate is also only 4.4%.

2 The economic situation in the euro area at the start of Stage Three

Monetary and financial developments reflect an environment of price stability

The broad monetary aggregate M3 has followed a rather smooth path, with growth rates of between 3.5% and 5% over the past two years. This monetary trend can be regarded as compatible with ongoing price stability and sustainable economic growth in the euro area. At the same time, interest rates declined all along the maturity spectrum, on account of the improvement in the price environment. The euro area average three-month interbank rate has shown a trend decline from a level of more than 7% in spring 1995 to 3.25% at the end of 1998. This decline reflects the achievement of price stability in the euro area and the increasing stability of intra-euro area exchange rates before the start of Stage Three. The euro area long-term interest rate (as measured by the average of 10-year government bond yields) has declined from more than 9½% in early 1995 to just below 4% at the end of December 1998. In real terms, i.e. corrected for the decline in inflation, the long-term interest rate has fallen by around 3½ percentage points since early 1995 to around 3% at end-1998. Within the euro area, the gradual disappearance of exchange rate risk premia, the reduction in inflation risk premia, the closing of short-term interest rate differentials and the progress towards fiscal consolidation which have taken place over the past few years have all played a positive role in this respect.

Increase in consumer prices at around 1%

Focusing on more recent trends, price increases as measured by the Harmonised Index of Consumer Prices (HICP) have declined from around 1.6% in mid-1997 to a level of 0.9% in November 1998. This was mainly due to a lower rate of increase in goods prices, of 0.3%, whereas the price increase for services remained broadly unchanged in 1998 at around 2%. An important factor underlying lower goods price increases in the recent past has been the considerable decline in oil and other commodity prices since their 1997 peak. Moreover, growth in compensation per employee slowed further in 1998 and unit labour costs declined slightly over the most recent quarters for which data are available.

Robust output growth in 1998, but slowdown in the course of the year

Following a recovery in 1997, real GDP growth in the euro area accelerated further in 1998 as a whole, being increasingly driven by domestic demand rather than by net exports. Private consumption has accounted for the largest single contribution to GDP growth in recent quarters, while fixed investment has expanded less strongly. However, against the background of a worsening of the external environment, the risk increased during the course of 1998 that the expansion in the euro area would not continue at its recent pace, and real GDP growth slowed after the summer months, falling from 3% in the first half of 1998 to 2.4% in the third quarter, compared with the corresponding period in the previous year. This coincided with a deterioration in industrial confidence, while consumer confidence remained at historically high levels.

Unemployment rate declines gradually as employment recovers

Notwithstanding the cyclical improvement in economic activity, unemployment in the euro area as a whole remains high. However, it declined slightly in 1998, following a pick-up in employment growth that started in early 1997. According to Eurostat, the standardised unemployment rate in the euro area declined to 10.8% in autumn 1998, i.e. to the lowest level in five years.

Improvements in fiscal positions have stalled

Compared with the progress in fiscal consolidation achieved in previous years, only a small further reduction in budgetary deficits across the euro area was achieved in 1998. The average deficit-to-GDP ratio in the euro area is estimated by the European Commission to have declined to 2.3% in 1998 from 2.5% in the previous year. This reduction, however, was the effect of favourable cyclical influences and lower interest payments. According to the European Commission, adjusting the deficit ratio for cyclical effects shows that the remaining "structural deficit" in the euro area in fact deteriorated slightly in 1998, rather than having improved. This would be the first deterioration in the cyclically adjusted deficit ratio since 1991, which contrasts with the commitment enshrined in the Stability and Growth Pact to respect the medium-term budgetary objective of achieving fiscal positions "close to balance or in surplus". Moreover, the primary balance ratio is also estimated to have worsened in 1998 for the first time in several years. While the share of government expenditure in GDP appears to be on a declining trend after reaching a peak in 1993, the ratio of euro area government revenue to GDP declined in 1998 after increasing in the period 1995-97. In the euro area as a whole taxes increased slightly in 1998, whereas social security contributions were lower.

On average, the euro area general government debt is estimated by the European Commission to have been 73.8% of GDP in 1998, 1.2 percentage points less than in 1997. Government debt ratios in the euro area have been falling since 1996, not only because of the reduction in deficits, but also on account of the benefits accruing from a number of financial transactions, including, most notably, privatisation. However, debt ratios in the euro area as a whole are still far above the reference level of 60% of GDP laid down in Protocol No. 5 to the Treaty establishing the European Community, thus limiting substantially the budgetary room for manoeuvre in Member States. At the same time, deficit ratios are still too high to set debt ratios on a rapidly declining path.

Euro area currencies appreciated slightly

In 1998 euro area currencies appreciated by about 2.1% on average in nominal terms and by about 1.5% in real terms against their major trading partner currencies, compared with a year earlier. However, this appreciation - due mainly to a weakening of the US dollar and the pound sterling in the second and third quarters of 1998 - took place against the background of a marked depreciation in 1997, when, driven by the exceptional strengthening of the US dollar and the pound sterling, euro area currencies had fallen by about 9% vis-à-vis their trading partner currencies. As a result, on the eve of Stage Three, euro area currencies stood, in effective terms, still somewhat below their average levels of the past few years.

On 31 December 1998, in accordance with Article 109l (4) of the Treaty establishing the European Community, the irrevocable conversion rates for the euro were adopted by the EU Council (see Table 2), upon a proposal from the European Commission and after consultation of the ECB. In compliance with the legal framework for the use of the euro, the irrevocable conversion rate for the euro vis-à-vis each participating currency is the only rate to be used for conversion either way between

Table 2

Irrevocable euro conversion rates

	EUR 1 =	
Belgium	BEF	40.3399
Germany	DEM	1.95583
Spain	ESP	166.386
France	FRF	6.55957
Ireland	IEP	.787564
Italy	ITL	1936.27
Luxembourg	LUF	40.3399
Netherlands	NLG	2.20371
Austria	ATS	13.7603
Portugal	PTE	200.482
Finland	FIM	5.94573

the euro and the national currency unit and also for conversions between national currency units. The last official ECU (and first euro) rate against the US dollar was set at USD 1.168 on 31 December 1998. The euro opened trading in Australia on 4 January 1999 at USD 1.175. In Europe the euro started trading at USD 1.1855.

External accounts recently affected by the deterioration in the global environment

Over recent years both the euro area trade and current account balances with the rest of the world have shown rising surpluses (on the basis of provisional data), from 1.2% and 0.5% of GDP respectively in 1995 to 1.6% and 1.1% of GDP in 1997. However, from mid-1998 onwards, the worsening in the global economy, whose origins lay in the Asian crisis, had a delayed impact on external accounts. Falling foreign demand caused a deceleration of export growth, which was also adversely affected by the currency appreciation. At the same time, while the growth of import volumes rose, as domestic demand remained strong, import prices declined, reflecting the fall in commodity prices.

3 Final considerations

Overall, the euro area, as one of the largest economies in the world, will play a significant role in shaping global macroeconomic conditions. Equally, it will be open vis-à-vis its trading partners, although developments in the domestic economy will by far outweigh external factors. Residents of the euro area will undoubtedly benefit from the enhanced growth and employment opportunities which are afforded by a large internal market.

However, important challenges remain. These include, in particular, a high level of unemployment and fiscal imbalances, as reflected in both current deficit and debt levels in relation to GDP. In order to address these challenges, a large economy such as the euro area has to rely primarily on maintaining a sound and sustainable policy framework "at home", thereby also contributing to a stable world economy. This framework is characterised by fiscal policies that are consistent with the Stability and Growth Pact, on the one hand, and ongoing structural reform in the labour and product markets accompanied by moderate wage developments, on the other. Maintaining this policy framework will help to foster competitiveness and profitability in the corporate sector, thereby promoting investment. Equally, it will help to sustain and foster the employment growth that has been seen recently, which will in turn support private consumption.

Monetary policy will play its part by pursuing its primary objective of price stability, thereby keeping inflationary expectations and risk premia in long-term interest rates low and hence contributing to an environment conducive to growth in economic activity and employment in the euro area.

Economic developments in the euro area

1 Monetary and financial developments

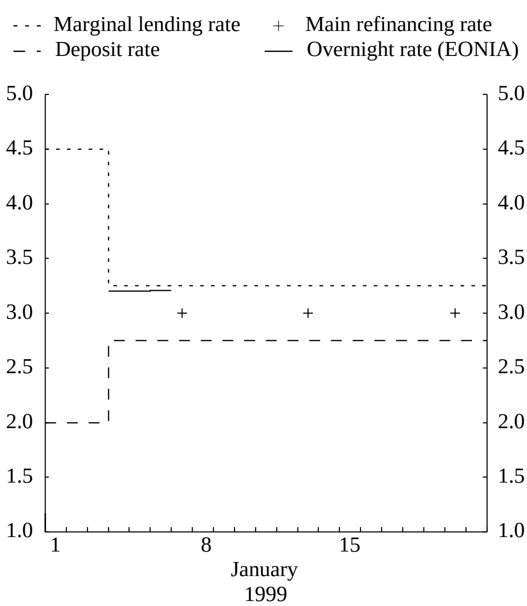
Monetary policy decisions by the Governing Council of the ECB

On 22 December 1998 the Governing Council of the ECB announced the interest rates for the first monetary policy operations of the Eurosystem. The interest rate applicable to the first main refinancing operation, offered in the form of a fixed rate tender and settled on 7 January 1999, was set at a level of 3%. In addition, the interest rate for the marginal lending facility was set at a level of 4.5% and the interest rate for the deposit facility at a level of 2% at the start of Stage Three (i.e. 1 January 1999). However, as a transitional measure between 4 and 21 January 1999, the interest rate for the marginal lending facility was set at a level of 3.25% and the interest rate for the deposit facility at a level of 2.75%. At its meeting on 7 January 1999 the Governing Council decided that the main refinancing operations to be settled on 13 and 20 January 1999 would also be conducted as a fixed rate tender at a rate of 3% (see Chart 1 and the "Chronology of monetary policy measures of the Eurosystem" at the end of this Bulletin).

Chart 1

ECB interest rates and the overnight rate

(percentages per annum; daily data)



Source: ECB.

The interest rate on the main refinancing operation, i.e. the weekly tender, is the main interest rate with which the Eurosystem steers movements in short-term market rates, whereas the interest rates on the two standing facilities provide a corridor for movements of the overnight money market rate (see Box 1). The aforementioned decisions on the interest rate applicable to the first three main refinancing operations reflected the view of the Governing Council, based on its assessment of the economic, monetary and financial situation in the euro area, that a level of 3% is appropriate for the foreseeable future as it best serves the maintenance of price stability over the medium term.

With regard to the first interest rates on the standing facilities of the Eurosystem, the Governing Council had to consider two aspects. First, it needed to signal clearly its monetary policy intentions. These were expressed by setting the rate for the marginal lending facility at 4.5% and the rate for the deposit facility at 2% for the start of Stage Three. Hence the corridor for movements in short-term interest rates, relative to the 3% main refinancing rate, is asymmetric towards the upper boundary. Determining these rates was also necessary in order to provide successors to the official national central bank rates previously used as reference rates in certain legislation and contracts in some Member States. Second, the Governing Council had to consider the possibility that market participants may need some time to get used to the new environment for monetary policy. By setting a relatively narrow interest rate corridor of 50 basis points on the standing facilities between 4 and 21 January 1999, the Governing Council aimed at smoothing the adaptation of market participants to the new environment of the euro area money market during the initial days of Monetary Union. The Governing Council also announced that the chosen narrow width of the corridor represented a temporary and exceptional measure which would only be applied during the first three weeks of Stage Three.

Given the many novelties associated with the move to the new monetary policy environment in Stage Three, it was regarded as important to contain the volatility of interest rates at the beginning of Stage Three by means of a narrow corridor. A narrow corridor has the effect, in particular, of limiting the costs for those credit institutions which, owing to technical problems or insufficient information, would have been unable to receive or place funds in the interbank market at the start of Stage Three. Such a narrow corridor is, however, not a desirable feature for the longer term, since it may hamper the development of an efficiently functioning euro area money market, limits incentives for credit institutions to carefully plan the fulfilment of their reserve requirements and complicates the liquidity management of the Eurosystem. For this reason, the Governing Council already announced on 22 December 1998 that it intended to terminate this measure following its meeting on 21 January 1999.

On 5 January 1999 the Eurosystem announced the allotment of its first main refinancing operation. A total amount of €75.0 billion was allotted, which was spread across 944 bidding credit institutions in proportion to the bids they had submitted. The allotment decision was made on the basis of the liquidity needs of the euro area as a whole, so as to relatively rapidly provide the amounts needed by the credit institutions to fulfil their reserve requirements within the first reserve maintenance period, while paying due attention to the uncertainties connected to the phasing-in of the new system.

Box 1

The monetary policy operational framework of the Eurosystem: a brief introduction

In order to achieve its monetary policy objectives, the Eurosystem conducts open market operations, offers standing facilities and requires credit institutions to hold minimum reserves on accounts with the national central banks. Open market operations play an important role in the monetary policy of the Eurosystem for the purposes of steering short-term interest rates, managing the liquidity situation in the money market and signalling the stance of monetary policy. Standing facilities are aimed at providing and absorbing overnight liquidity and at providing a general signal regarding monetary policy intentions over the medium term. The minimum reserve system primarily serves the purpose of stabilising money market interest rates and creating (or enlarging) a structural liquidity shortage.

Among the open market operations, the “main refinancing operation”, i.e. a weekly tender with a two-week maturity, plays a pivotal role in the Eurosystem’s monetary policy framework. Indeed, it is mainly through this operation that the Eurosystem steers movements in short-term market interest rates and refinances the banking system. In addition, the Eurosystem also regularly conducts “longer-term refinancing operations”. These are monthly tender operations which have a three-month maturity. By contrast with the weekly tender, in the monthly tender the Eurosystem does not, as a rule, intend to send signals to the market. Other types of open market operations which the Eurosystem could conduct, when deemed necessary, include fine-tuning operations, which are aimed, in particular, at smoothing the effects of unexpected liquidity fluctuations in the market. Furthermore, the Eurosystem has the possibility of using open market operations (such as the issuance of ECB debt certificates) to adjust the structural position of the Eurosystem vis-à-vis the financial sector. Since the start of Stage Three the ECB has not, however, seen any need to carry out such “structural” operations.

While open market operations are conducted on the initiative of the Eurosystem, in the case of the standing facilities the initiative lies with those credit institutions which are the Eurosystem’s counterparties. Eligible counterparties have access to two standing facilities of the Eurosystem: the marginal lending facility allows them to obtain overnight liquidity from the national central banks and the deposit facility allows them to make overnight deposits at the national central banks. Under normal circumstances there is no limit on access to the standing facilities (with the exception that access to the marginal lending facility, as for all credit operations of the Eurosystem, has to be backed by sufficient eligible collateral). As a consequence, fluctuations in the overnight market interest rate are bounded by the corridor set by the interest rates applied to these standing facilities.

In addition, each credit institution located in the euro area is subject to a reserve requirement. This requirement is determined by applying a reserve ratio to selected liabilities of the balance sheet of credit institutions. The reserve ratio was set at a level of 2% as from the start of Stage Three. A credit institution complies with its obligations under the Eurosystem's minimum reserve system if its average daily reserve holdings, as computed over a reserve maintenance period normally running from the 24th day of each month to the 23rd day of the following month, is at least equal to its reserve requirement. Holdings of required reserves are remunerated at the rate of the Eurosystem's main refinancing operation. The mechanism for the fulfilment of the reserve requirement over a period longer than one day – a period of precisely one month in the case of the Eurosystem's minimum reserve system – is known as the averaging provision. As the averaging provision provides flexibility in the banking system's management of its liquidity, credit institutions will be able to accommodate day-to-day changes in the provision of liquidity and to exploit short-term arbitrage possibilities in the money market. In this way, the averaging provision can be expected to contribute to a stabilisation of the overnight rate over the course of the maintenance period.

Finally, as regards the inception of the Eurosystem's operations, the standing facilities have been accessible to credit institutions as from 4 January 1999, the first business day of Stage Three. The first weekly tender was settled on 7 January 1999 and the settlement date of the first monthly tender was 14 January 1999. With a view to contributing to a smooth transition to the Eurosystem's monetary policy framework, participating national central banks agreed to let the open market operations they conducted towards the end of Stage Two mature gradually in the course of the first half of January 1999. Furthermore, as a transitional provision for the Eurosystem's minimum reserve system, the first maintenance period will run from 1 January 1999 until 23 February 1999.

A detailed description of the Eurosystem's monetary policy framework is presented in the ECB report entitled "The single monetary policy in Stage Three: General documentation on ESCB monetary policy instruments and procedures" (September 1998).

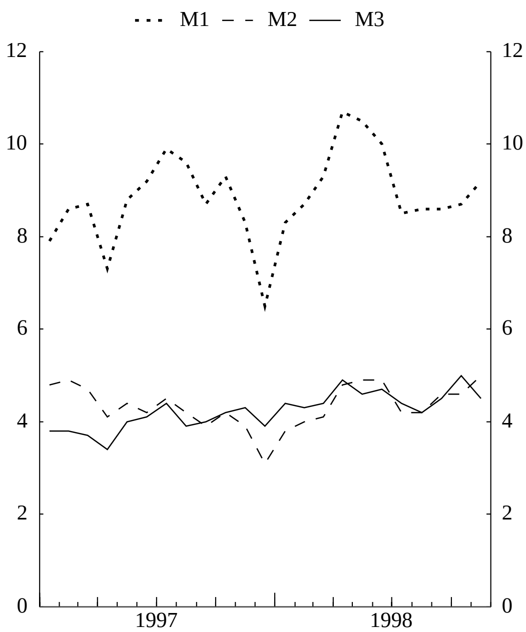
Monetary growth compatible with price stability

The stability-oriented monetary policy strategy of the Eurosystem assigns a prominent role to money, founded on the essentially monetary nature of inflation in a medium and long-run perspective (see the article entitled "The stability-oriented monetary policy strategy of the Eurosystem" in this issue of the Bulletin). The Governing Council of the ECB decided on 1 December 1998 to set the first reference rate for the annual growth of a broad monetary aggregate M3 in the euro area at 4½%. Monetary developments will be monitored against this reference value on the basis of the three-month moving average of the 12-month growth rate of M3, in order to prevent erratic monthly outturns from unduly distorting the information contained in the data. In addition to M3, attention will be paid to narrower definitions of money (M1 and M2) and to the counterparts of M3, particularly lending to the private sector (see Box 2 for an overview of definitions of monetary aggregates for the euro area).

The data available show that M3 grew at a pace of between 3.5% and 5.0% over the past two years. This was broadly compatible with price stability and sustainable economic growth in the euro area. During this period, the pace of growth of the narrow aggregate M1 was significantly higher than that of M3 (see Chart 2); this reflected entirely the high rate of growth of overnight deposits. Shifts towards this component of narrow money in the course of 1998 were stimulated by the decline in interest rates in the euro area, which reduced the opportunity cost of holding overnight deposits. Furthermore, investment in this component of narrow money benefited from the fall in inflation rates in several countries as well as from the expected establishment of Monetary Union and a stable single currency. Moreover, in some countries overnight deposits may have played a buffer role in a portfolio reallocation process leading to significant shifts toward mutual funds and equities during 1998. On the whole, it therefore appears that, apart from reflecting the pace of economic expansion, most of the strong growth of narrow money results from the adjustments to low inflation rates in some euro area countries or portfolio shifts which do not signal any inflationary risks.

Chart 2

Monetary aggregates in the euro area
(annual percentage changes)



Source: ECB.

Looking at more recent monetary developments, the data for November 1998 show that M3 grew at an annual pace of 4.5%, which was 0.5 percentage point lower than the 12-month growth rate recorded in the previous month. The three-month moving average of the 12-month growth rate of M3 (covering the period from September to November 1998) was broadly stable at 4.7%, a level which is very close to the reference value set by the Governing Council of the ECB. The annual rate of growth of M1 increased from 8.7% in October 1998 to 9.2% in November, while that of M2 accelerated to 5.0% in November 1998, from 4.6% in October 1998.

The decline in the rate of growth of M3 between October and November 1998 mainly reflected a slower pace of growth in marketable instruments included in M3. In particular, the demand for repurchase agreements contracted substantially, and that for debt securities issued with a maturity of up to two years decelerated. The subdued demand for marketable instruments in November reversed a movement observed in October and must be seen against the background of an exceptionally high degree of volatility in financial markets in October, which was followed by a gradual return to normality in November.

Overnight deposits grew at an annual rate of 11.5% in November, compared with 10.7% in October. Deposits redeemable at notice of up to three months grew at an annual pace of 6.3% in November, while deposits with an agreed maturity of up to two years contracted by 3.8% on a 12-month basis.

Counterparts of M3 support the monetary analysis

In the context of the monetary policy strategy of the Eurosystem, an analysis of the so-called counterpart items of M3 in the consolidated balance sheet of the MFI sector contributes to a deeper understanding of monetary developments. These counterparts belong to the wide range of economic variables that are monitored and analysed mainly in terms of their leading indicator properties regarding future price developments.

On the assets side of the balance sheet the total amount of credit to the private sector (defined as the sum of MFI loans to the private sector and holdings of securities issued by euro area residents other than general government) has been growing at a considerably faster pace than M3 during recent months. On an annual basis it increased by 8.8% and 9.2% in October and November respectively. According to recent MFI balance sheet data, the 12-month increase in the outstanding stock of loans to households and non-financial enterprises (which

Box 2

Definitions of monetary aggregates for the euro area

In the course of Stage Two of Economic and Monetary Union (EMU) the national central banks, the European Monetary Institute (EMI) and, subsequently, the ECB have devoted considerable effort to developing harmonised euro area monetary statistics. This has resulted in the compilation of a consolidated balance sheet of the Monetary Financial Institutions sector (MFI sector), on the basis of which the monetary aggregates for the euro area are derived. The MFI sector comprises those institutions whose liabilities may be of a monetary nature: they include the national central banks, the ECB, credit institutions and other financial institutions, mainly money market funds (MMFs). The MFIs resident in the euro area are collectively defined as the "money-issuing" sector in the euro area.

For the purpose of defining monetary aggregates, the "money-holding" sector comprises all non-MFI euro area residents, excluding central government. This sector principally includes households, non-financial corporations, insurance corporations and pension funds and other non-MFIs located in the euro area, as well as state and local government authorities and social security funds in the euro area. Central governments are considered to be a "money-neutral" sector, with one exception: central government deposit liabilities with a monetary character (post office accounts, national savings accounts and treasury accounts) are included in the definition of the monetary aggregates of the Eurosystem.

Different types of MFI liabilities are included in the monetary aggregates for the euro area. Currency in circulation and overnight deposits are the most liquid instruments and form the narrow definition of money, referred to as M1. Adding other short-term deposits to M1 (namely deposits with an agreed maturity of up to two years and deposits redeemable at notice of up to three months) gives the monetary aggregate M2. Finally, the broad monetary aggregate M3 is obtained by summing M2 with specific marketable liabilities of the MFI sector (repurchase agreements, money market fund shares/units and money market paper, together with debt securities issued with an original maturity of less than two years).

In quantitative terms, M1 accounted for around 39% of M3 in November 1998, with currency representing 7% and overnight deposits 32%. Deposits redeemable at notice of up to three months and deposits with an agreed maturity of up to two years accounted for around 27% and 20% respectively; thus the aggregate M2 accounted for 86% of M3. Marketable instruments accounted for the remaining 14% (with money market fund shares/units and money market paper at 7%, repurchase agreements at 5% and debt securities issued with an original maturity of up to two years at 2%).

Data on the consolidated balance sheet of the MFI sector and the monetary aggregates for the euro area (covering all 11 euro area countries) have been compiled as from September 1997. This has made it possible to obtain 12-month growth rates for all balance sheet items from September 1998 onwards. For monetary aggregates, however, longer-term series have been estimated. Statistics on month-to-month flows representing actual financial transactions are not available as yet; consequently, growth rates are calculated on the basis of statistics for stocks. This method of calculation may neglect the influence of distorting factors, such as the variation of market prices (for securities included in M3 for which there is a secondary market), exchange rate movements and reclassifications. Furthermore, the data are to some extent still based on estimates as some changes to the reporting systems in individual euro area countries have yet to be completed. However, at this point in time these data represent the most comprehensive and reliable source of monetary information in the euro area. This notwithstanding, some caution should be exercised when evaluating monetary statistics for monetary policy purposes.

Conceptual and empirical aspects of the euro area monetary aggregates will be discussed in more detail in an article which is to appear in the February 1999 Monthly Bulletin.

accounts for around 91% of total MFI credit to the private sector) was 8.5% in November (compared with 8.2% in October 1998). Securitised MFI lending to the private sector expanded at a relatively high 12-month growth rate of 16.2% in November, although this development should not be overstated since this item accounts for less than 10% of total MFI credit to the private sector. The strong rate of growth of MFI financing to the private sector appears to be related to the economic expansion in the euro area in 1998 and to favourable financing conditions for non-financial corporations and households, given the current low level of retail bank lending interest rates (see Table 2.8 in the "Euro area statistics" section).

MFI credit to general government, by contrast, increased at a very slow pace in November 1998; in particular, loans extended to general government declined at a 12-month rate of 1.5%. The annual rate of growth of MFI holdings of general government debt securities was 3.8% in November.

On the liabilities side of the balance sheet the longer-term financial liabilities of MFIs (comprising longer-term deposits and debt securities issued plus MFIs' capital and reserves), are financial instruments outside the scope of the definition of broad money. Under certain circumstances, they may provide alternative investment opportunities to the instruments included in M3. In November 1998 longer-term financial liabilities accounted for around 30% of total MFI liabilities (for comparison, components of M3 accounted for some 41% of total MFI liabilities). This counterpart item grew at an annual rate of around 3% in November 1998, which was slightly less than in October 1998 (3.4%). The subdued growth of this component may have been influenced by the falling spread between long-term and short-term interest rates in recent months (see Box 4 below).

The net external position of MFIs in the euro area tended to deteriorate in 1998. The 12-month growth of external liabilities reached 14.9% in November, compared with a corresponding growth rate of 4.6% for external assets.

Money market rates on a declining trend in recent months

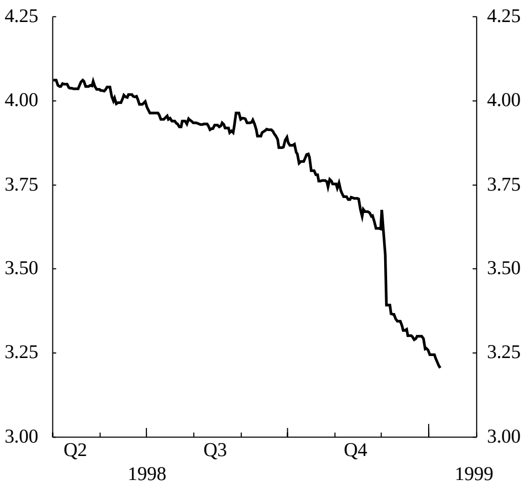
While the average three-month interest rate for the euro area was still just above 4% in May 1998, when the euro area countries were selected, it gradually declined during the course of the year. To a large extent, this reduction in short-term interest rates reflected the process of convergence in interest rates recorded in the euro area in 1998. While significant differentials in money market rates existed across euro area countries in early 1998, these spreads narrowed over time through the reduction of central bank interest rates in those countries with relatively high short-term interest rates. This resulted in a process of convergence towards the levels prevailing in the euro area countries with the lowest interest rates. By the end of November 1998 the average three-month market rate had reached a level of 3.6%.

A further pronounced fall in the euro area average of three-month interest rates took place immediately after 3 December 1998 when all the national central banks of the 11 Member States adopting the euro as from the start of Stage Three decided in a co-ordinated manner to lower their key central bank rates to 3% (with the exception of one central bank, which initially only reduced its key rate to 3.5%, subsequently reducing it to 3% on 23 December 1998). As explained by the ECB at the time, this joint reduction in interest rates had to be seen as a de facto decision on the starting level of the corresponding ECB interest rate. At end-December 1998 the level of the euro area three-month interest rate was equal to 3.25%, i.e. around 35 basis points lower than at end-November 1998 and about 80 basis points below the level of May 1998 (see Chart 3).

Chart 3

Short-term interest rate in the euro area

(percentages per annum; daily data)



Source: ECB.

Note: Euro area average of national three-month interbank rates until 29 December 1998; three-month EURIBOR from 30 December 1998 onwards.

In the first week of January 1999 the overall conditions prevailing in the euro area money market were stable. The one-month and three-month interest rates were both quoted at levels of around 3.2%. The overnight rate, as measured by the EONIA ("euro overnight index average", i.e. the weighted average of the rates on unsecured overnight contracts reported by a panel of major banks in the euro area) was also close to 3.2% between 4 and 7 January 1999.

Although some minor problems of a technical nature could not be avoided, the changeover to the euro and the experience of the functioning of the ESCB's payment system (TARGET) and the euro area money market in the first few days of Monetary Union were generally encouraging (see Box 3). Short-term interest rate differentials across participating countries narrowed quickly. This indicates that credit institutions throughout the euro area appear to be adapting rapidly to the new environment by engaging in cross-border business in order to make use of arbitrage possibilities in the single money market. At the same time, the Eurosystem observed relatively intensive recourse by credit institutions not only to its marginal lending facility, but also to its deposit facility in the first few days of Monetary Union. While the recourse to the marginal lending facility has to be seen in the light of the fact that the spread between the rate on this facility and the overnight market rate was relatively small during those first few days, implying a low opportunity cost for banks to use the marginal lending facility, the significant level of recourse to the deposit facility indicates that, at the start of Stage Three, not all banks used excess liquidity to place loans in the money market. With the envisaged widening of the corridor between the rates on the Eurosystem's standing facilities, however, there will be noticeably greater incentives for all credit institutions to participate in the money market.

Box 3

The changeover to the euro

Financial markets and payment and settlement systems opened in the morning of 31 December 1998 with low liquidity and only few transactions, as expected, while all stock exchanges in the euro area were closed. In the early afternoon, after the Council of the European Union had adopted the irrevocable conversion rates of the euro against the participating currencies, the changeover activities of the public and private financial sectors got under way. During the following three and a half days (known as the "changeover weekend"), the bulk of the public debt of the participating Member States was redenominated in euro, databases containing billions of electronic records were converted from the national currencies to the euro, and systems and procedures were adapted to function in the new currency. Conversion activities were practically concluded by late afternoon on 3 January 1999. The global financial and foreign exchange market opened in euro in Sydney at 6 p.m. C.E.T. on 3 January, while all segments of the financial markets in the euro area opened in euro on 4 January. The TARGET system closed at 7.30 p.m. on 4 January, after the financial community in the euro area had operated in the new currency for a full day. This allowed the Eurosystem to announce its first main refinancing operation in an environment fully operational in the new currency on the same day. Only five days had passed between the opening of the markets in national currencies on 31 December 1998 and the close of business in euro on 4 January 1999.

The changeover weekend went smoothly, without any serious incident affecting the launch of the single currency, thanks to the commitment and hard work of a very large number of institutions. Sources in the media reported that a workforce of 50,000 was directly involved in the changeover during the weekend – not only in the euro area, but also in other major financial centres.

Within the Eurosystem preparations had been ongoing for some time. The first plan of action for the changeover weekend had already been approved by the Council of the European Monetary Institute in March 1998. After the establishment of the ECB, the Governing Council of the ECB examined reports on the changeover at four of its meetings. During the changeover weekend several thousand staff members were at work or on call at the ECB and at the national central banks.

The Eurosystem played a key role. It helped to compute, promulgate and publish the irrevocable conversion rates of the euro vis-à-vis the participating currencies; it co-ordinated the orderly transition to the new currency at the ECB and at the national central banks; it conducted final tests, when required, of the new infrastructure; it launched the new infrastructure for payment and securities settlement, including TARGET; it issued recommendations to credit institutions and securities settlement systems; and it participated in working groups and tests at the local level, together with representatives of the banking community. The Eurosystem also identified a number of systems and players – defined as the "core infrastructure" – with which it created ad hoc links for the exchange of information during the changeover weekend; these included payment systems, securities settlement systems, stock exchanges, global custodians and financial data providers. A "Changeover Weekend Committee" and a network of "central communication points" were created to gather and share information. A mechanism was set up to monitor 240 relevant steps in the conversion process which might impinge upon the smooth launch of the euro and the functioning of the monetary system (the so-called "milestones"). Contact was established with the central banks of the non-participating countries, of the G-10 countries and of other nations, with the European Commission and with a parallel network of institutions organised by the Banking Supervision Committee. The decision-making bodies of the ECB stood ready to gather in extraordinary teleconference meetings, if necessary. Information was exchanged continuously, both prior to and during the weekend; in particular, the state of advancement of the conversion activities was discussed during three teleconferences before the weekend and eight during the weekend among the central communication points at the ECB and at the national central banks.

The major concern of the Eurosystem was to avoid a breakdown in the transition to the euro – at the ECB, at any national central bank or within any of the systems of the above-mentioned "core infrastructure" – hampering the functioning of the monetary system, perpetuating the pre-existing segmentation of money markets or confronting the monetary authorities with risks for financial stability at the very start of Monetary Union.

The conversion of the national currencies to the euro during the changeover weekend had all the features of a major engineering endeavour. It imposed a unique co-ordination effort upon the Eurosystem as well as upon the banking and financial community of the euro area and beyond. It was a test of the capacity of the European financial industry to work under extreme pressure. The satisfactory outcome of the changeover process is a sign of the quality of the preparatory work conducted over the past two years by the banking community and by other financial market operators in the euro area.

Long-term government bond yields at historically low levels

Towards the end of December 1998 long-term government bond yields in the euro area reached historically low levels of well below 4% (see Chart 4). This represented a significant decline of around 150 basis points, compared with the situation at end-1997, and may be seen as a continuation of the longer-term trend of declining long-term interest rates in the euro area which has been firmly in place since early 1995. This favourable development in euro area bond markets is a reflection of the more or less continuous decline in euro area rates of inflation since early 1995, as well as of a corresponding decline in longer-term inflation expectations. Furthermore, it reflects the efforts made towards fiscal consolidation in the euro area in preparation for the move to Stage Three and the gradual disappearance of exchange rate risk premia.

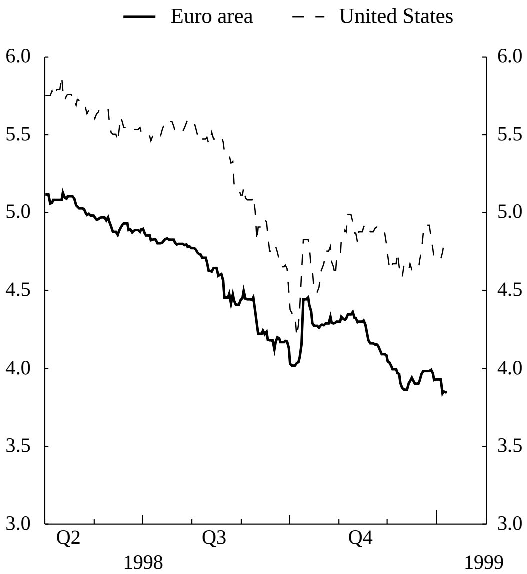
In the course of 1998 this process of declining long-term bond yields accelerated in an environment of exceptional turbulence in international financial markets which saw "safe-haven" flows from emerging markets to the capital markets of industrialised countries as well as a shift in investors' attitudes towards risk. This shift in risk attitudes prompted a generalised "flight to safety" in global financial markets, from stock markets to the bond markets of industrialised countries. All in all, this resulted in an increased volatility in bond, stock and foreign exchange markets in the autumn. However, as volatility subsequently returned to normal levels, long-term government bond yields in the euro area continued to decline. This was a notable development, which indicated that the "flight to safety" was not the only source of the decline in bond yields and that domestic factors, such as a further decline in inflation and an easing of risks for price stability, had also played a key role.

The co-ordinated round of central bank interest rate cuts in the euro area on 3 December 1998 was reflected in an immediate further decline in long-term bond yields, while the differential between 10-year bond yields in the United States and comparable yields in the euro area widened slightly. Overall, despite a temporary upturn related to a sharp increase in Japanese bond yields, 10-year bond yields in the euro area declined by almost 20 basis points in the course of December, while further declines were observed in early January. This compares with a slight increase in comparable yields in the United States and a substantial increase of more than 70 basis points in Japanese yields in the period between 3 December 1998 and 7 January 1999. These developments, together with a euro area yield curve downward shift at all maturities (see Box 4) following both the cuts in central bank rates and the announcement concerning the standing facilities corridor, indicate that the single monetary policy has already achieved a high degree of credibility in the eyes of the financial markets.

Chart 4

Long-term government bond yields in the euro area and the United States

(percentages per annum; daily data)



Sources: ECB and BIS.

Note: Long-term government bond yields refer to 10-year bonds or closest available bond maturity.

Box 4

Yield curve developments since July 1998

The yield curve can, under certain assumptions, reflect market participants' expectations regarding the future direction of short-term interest rates. At the same time, it can provide useful information on market participants' expectations with regard to future developments in inflation and the pace of real economic activity. The following analysis considers developments in the yield curve, as measured using the interest rates observed on the fixed side of interest rate swap contracts. An interest rate swap is an agreement to exchange a flow of fixed interest payments in return for a variable rate of interest.

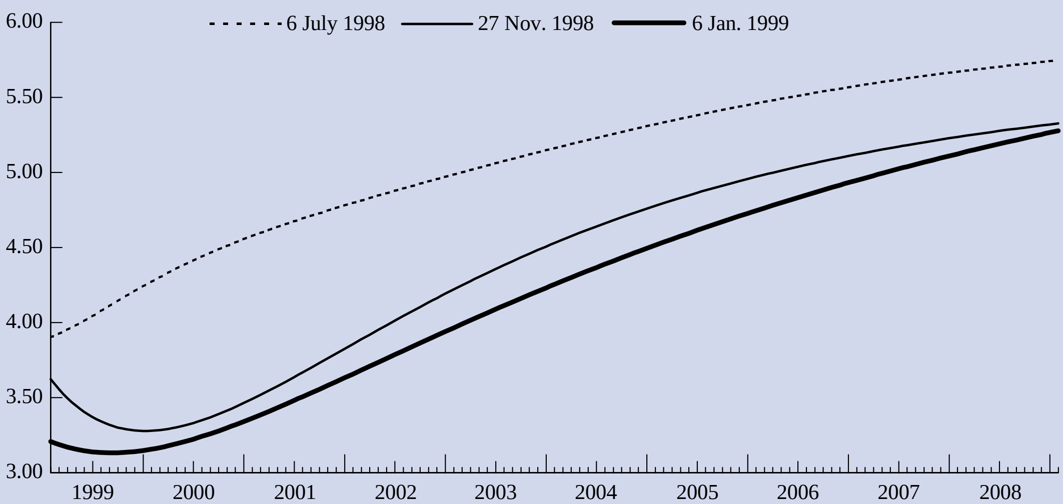
The shape of the euro area swap yield curve has changed significantly over the course of the past six months. Reflecting the decline in both short-term and long-term interest rates, the euro area yield curve has shifted downwards along the entire maturity spectrum. In addition, since these declines were slightly larger at the long end of the maturity spectrum than at the very short end, a slight flattening of the spot yield curve was observed, with the spread of 10-year swap yields over three-month money market interest rates narrowing slightly. Although safe-haven flows related to the turbulence in international markets may at times have played a role in developments in long-term interest rates, this levelling-off of the yield curve slope might also indicate a reduction in the long-term outlook for inflation in the euro area.

The chart below shows how the pattern of implied forward euro area overnight interest rates derived from the term structure of interest rates has changed over the past six months. As may be seen from the chart, abstracting from risk premia considerations related to the term to maturity, in early July 1998 financial markets expected overnight interest rates in the euro area to be at a level just below 4% at the beginning of 1999, and to increase gradually thereafter. The configuration of implied forward overnight interest rates observed in early January 1999, by contrast, shows a change in these expectations, which partly reflects the convergence of short-term interest rates within the euro area to below the levels of those countries which previously had the lowest short-term interest rates.

In early January 1999 market participants expected a very slight decline in overnight rates in the months to come. Subsequently, overnight rates were expected to rise again. This pattern in the yield curve could also be observed in futures markets. In early January 1999 the three-month interest rates implicit in the futures contracts on euro deposits maturing in mid-March and mid-June 1999 were slightly lower than the three-month spot interest rate.

Implied forward euro area overnight interest rates

(percentages per annum; daily data)



Source: ECB estimation using the method outlined in the article entitled "Estimating and interpreting forward interest rates: Sweden 1992-94" by L. E. O. Svensson (1994), IMF WP/94/114, Washington, DC. The data used in the estimation are derived from swap contracts.

Heightened levels of volatility in stock markets

In recent months stock prices in the euro area have been significantly influenced by the turbulence in international financial markets. As measured by the Dow Jones EURO STOXX index, they showed a substantial decline of almost 35% from their peak in mid-July 1998 to a trough in early October, before climbing again by more than 35% until end-1998. Yet, reflecting the strength of euro area stock markets during the first half of 1998, by end-December stock prices were 30% above levels observed at the end of 1997. In early January stock prices in the euro area continued to show increases.

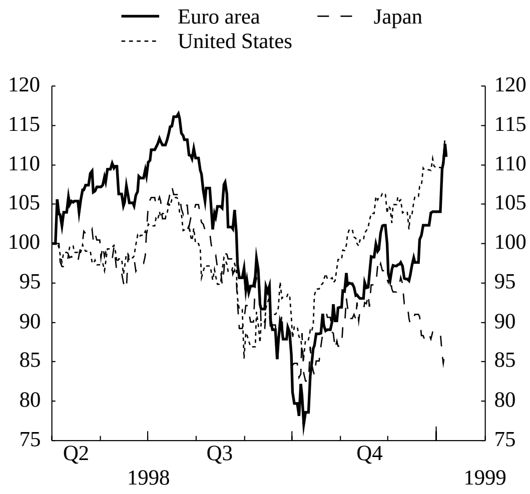
The recent high level of volatility in euro area stock markets, which was also apparent in the stock markets of both the United States and Japan (see Chart 5), appeared to reflect two main factors. First, concern about the economic situation in Russia, Asia and Latin America led to a downward reassessment of the prospects for global economic growth. This, in turn, appeared to lead to downward revisions of expectations for exports and corporate earnings. A second factor was a heightened level of uncertainty, which saw volatility in stock markets reach exceptionally high levels. This may, in part, have reflected a reassessment by market participants of the risks inherent in equity market investment generally. Nonetheless, as markets may subsequently have considered this reassessment of the global economic outlook to be unduly pessimistic, stock markets in the euro area recovered. This recovery was also linked to a recovery in stock markets in the United States. However, volatility in euro area stock markets has yet to return fully to the lower levels observed in early 1998, prior to the outbreak of financial market turbulence.

Turning to sectoral developments in euro area stock markets, considerable differences in performances have been observed in recent months. When stock market values declined in the autumn months, the largest downturns, of more than 40%, were observed in the automobile, banking and technology sectors. In the case of the euro area banking sector the key factors in this development, apart from global stock market influences, appeared to be concerns about the exposure of euro area financial institutions to emerging markets. Nonetheless, in line with the general trend, some recovery was later seen in these three sectors, where prices at end-1998 were only 20-25% below previous peaks, but still significantly above their end-1997 levels. Other sectors, such as the retail and utilities sectors, remained remarkably resilient throughout the stock market turbulence, with prices at end-1998 close to their earlier peaks in mid-July 1998. These sectoral developments show that, although sectors which were exposed to the international environment tended to perform adversely, those which depended to a larger extent on the strength of domestic demand remained relatively buoyant.

Chart 5

Stock price indices in the euro area, the United States and Japan

(1 May 1998 = 100; daily data)



Sources: Reuters for euro area; BIS for United States and Japan.
Note: Dow Jones EURO STOXX broad (stock price) index for the euro area, Standard and Poor's 500 for the United States and Nikkei 225 for Japan.

2 Price developments

Consumer price increases edged downwards

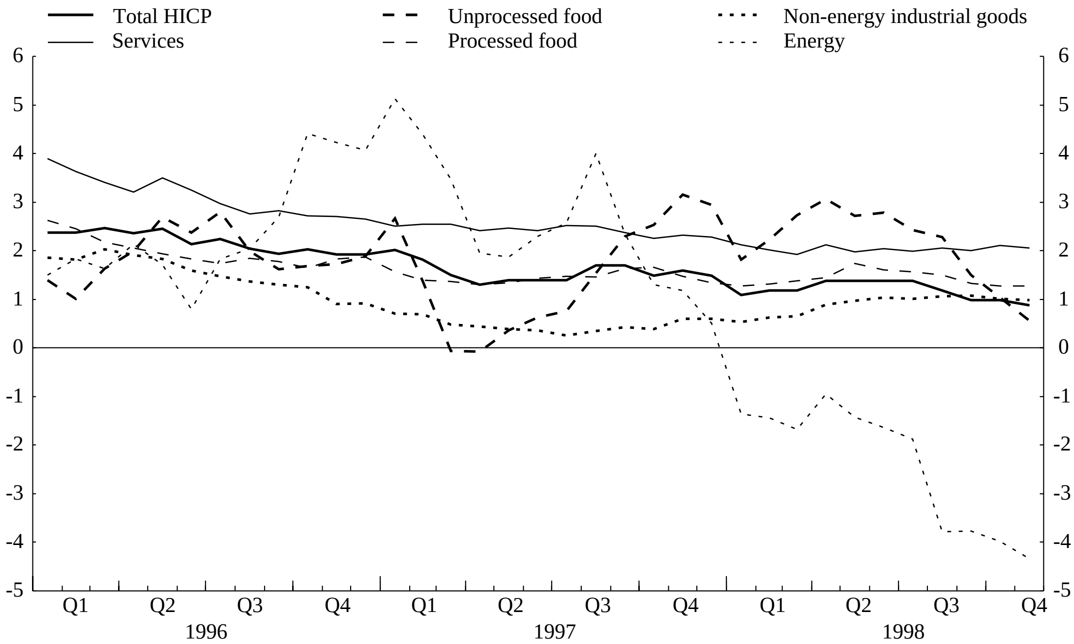
Recent consumer price increases in the euro area edged downwards further, while remaining in line with the quantitative definition of price stability adopted by the Eurosystem. As measured by the Harmonised Index of Consumer Prices (HICP), the annual percentage change in consumer prices in the euro area was 0.9% in November 1998, i.e. 0.1 percentage point lower than in September and October. Since the second quarter of 1998, when the annual increase in the HICP for the euro area reached 1.4%, it has decreased by 0.5 percentage point.

A breakdown of developments in the HICP for the euro area shows that the trends which were mainly accountable for the decrease in recent months continued in November. In particular, unprocessed food price increases moderated further to 0.6% and the fall in energy prices accelerated to -4.3% (see Table 1). With regard to unprocessed food prices, which generally show a fair degree of volatility, increases have moderated since April 1998 as the upward effects resulting from temporary supply shortages in the course of 1997 dropped out of the 12-month rates. The further reduction in energy prices reflected a continued fall in oil prices, which, in ECU terms, reached a level in December of around 45% below that recorded at the end of 1997. Moreover, commodity prices (excluding energy) remained considerably below the levels recorded in 1997. With regard to the other sub-indices, modest price increases continued in the case of processed food and non-energy industrial goods price increases were broadly unchanged at 1.0%, while services prices continued to increase by around 2%.

Chart 6

Breakdown of HICP inflation in the euro area by components

(annual percentage changes)



Source: Eurostat.

Note: For further information on the data used, see the respective tables and charts in the "Euro area statistics" section of this Bulletin. Latest observation: Total HICP: 0.9% (Nov. 1998); services: 2.1% (Nov. 1998); unprocessed food: 0.6% (Nov. 1998); processed food: 1.3% (Nov. 1998); non-energy industrial goods: 1.0% (Nov. 1998); energy: -4.3% (Nov. 1998).

Table 1

Price and cost developments in the euro area

(annual percentage changes, unless otherwise indicated)

	1996	1997	1998	1998 Q1	1998 Q2	1998 Q3	1998 Q4	1998 July	1998 Aug.	1998 Sep.	1998 Oct.	1998 Nov.	1998 Dec.
Harmonised Index of Consumer Prices (HICP) and its components													
HICP	2.2	1.6	.	1.2	1.4	1.2	.	1.4	1.2	1.0	1.0	0.9	.
of which:													
Processed food	2.0	1.5	.	1.3	1.6	1.5	.	1.6	1.5	1.3	1.3	1.3	.
Unprocessed food	1.9	1.5	.	2.3	2.9	2.1	.	2.4	2.3	1.5	1.0	0.6	.
Non-energy industrial goods	1.5	0.5	.	0.6	1.0	1.1	.	1.0	1.1	1.1	1.0	1.0	.
Energy	2.4	2.6	.	-1.5	-1.3	-3.2	.	-1.9	-3.8	-3.8	-4.0	-4.3	.
Services	3.1	2.4	.	2.0	2.0	2.0	.	2.0	2.1	2.0	2.1	2.1	.
Other price and cost indicators													
Industrial producer prices 1)	0.7	1.1	.	0.5	-0.2	-1.3	.	-0.8	-1.4	-1.6	-1.9	.	.
Unit labour costs 2)	1.8	0.6	.	-2.3	-0.5	.	.	-	-	-	-	-	-
Compensation per employee 2)	3.4	2.6	.	1.0	1.2	.	.	-	-	-	-	-	-
Labour productivity 2)	1.6	2.1	.	3.4	1.7	.	.	-	-	-	-	-	-
Oil prices (ECU per barrel) 3)	15.9	17.1	12.0	13.6	12.8	11.7	10.0	11.9	11.3	11.9	11.1	10.2	8.7
Commodity prices (ECU) 4)	-6.9	13.0	-12.5	-0.1	-10.7	-18.1	-20.5	-14.4	-19.0	-20.9	-23.6	-18.4	-19.5

Sources: Eurostat, national data, HWWA and ECB calculations.
Note: For further information on the data used, see the respective tables and charts in the "Euro area statistics" section of this Bulletin.
1) Excluding construction.
2) Whole economy.
3) Brent Blend (for one-month forward delivery).
4) Excluding energy.

A number of other cost and price indicators support the general picture of price stability in the euro area (see Table 1; for methodological remarks concerning price and cost statistics, see Box 5). Notably, producer price increases have slowed down gradually since the end of 1997 – mainly as a result of falling intermediate goods prices – and, after turning negative in May, producer prices were 1.9% lower in October 1998 than a year earlier. In addition, labour cost increases appear to have remained subdued throughout the first half of 1998. In particular in the first quarter of the year, growth in unit labour costs was negative as stronger economic activity led to higher productivity growth and the increase in compensation per employee slowed. Thereafter, as lower productivity growth was matched by continued wage moderation, unit labour costs remained broadly unchanged in the second quarter compared with a year earlier.

Box 5

Non-financial statistics supporting the analysis of euro area-wide economic developments

To assess macroeconomic developments in the euro area, a comprehensive set of reliable and up-to-date euro area-wide statistics is needed. In particular, these statistics must have a sufficient coverage of euro area-wide developments and country data should, to a high degree, be comparable. However, at this juncture much of the data, particularly longer time series, are available only on a non-harmonised basis. The definition and collection of statistics has been the responsibility of individual countries and, in the past, the need for harmonised data was limited. International definitions and standards have been developed over time, while only recently have more systematic efforts been made, not least in response to certain legal obligations, to work towards a harmonised statistical base within Europe. This box briefly describes the set of euro area-wide statistics on prices and costs, on output and demand and on the labour market that are currently available and indicates where improvements are likely in the near future (see also the "Euro area statistics" section in this Bulletin).

The ECB and its predecessor, the European Monetary Institute (EMI), have strongly supported initiatives at the European level which have aimed at providing the statistical basis for the single monetary policy. While an important impetus in this process was the provision of comparable statistics for the purpose of assessing convergence, the ECB data requirements are broader and at the same time more detailed. Moreover, the timeliness of the euro area results is crucial for their use for monetary policy purposes. These issues were recognised in a number of EU Regulations on statistics which have been enacted by the Council of the European Union on the proposal of the European Commission over the past few years (see below). Moreover, there are supplementary initiatives which will contribute to the euro area-wide statistical basis, such as the agreement between the Statistical Office of the European Communities (Eurostat) and all EU national statistical institutes (NSIs) to provide a set of existing key variables in a very timely fashion. The result of these initiatives is that the data situation has improved significantly and further improvements are expected in some areas in the course of 1999.

However, where harmonised data are not yet available in a timely fashion, it is necessary to use the best estimates which can be derived from national sources. These estimates are generally compiled on the basis of data for most, but not all, countries.

Price and cost statistics

For the conduct of monetary policy the Harmonised Index of Consumer Prices (HICP) for the euro area is of crucial importance. Eurostat provides, on a timely basis, the HICP and its sub-components on the basis of harmonised measures with respect to coverage, standards for the procedures for quality adjustment and numerous technical details. Further harmonisation and broadening of the coverage, for example to include expenditures on education and health services, are planned for the next two years. However, these series are considered to already meet the requirements of the ECB for policy analysis in terms of reliability, timeliness and comparability.

National accounts deflators, producer price statistics and labour costs are other indicators used for the analysis of price developments. They are not yet based on fully harmonised data and have a varying degree of coverage and comparability. Most of the data used in this context are provided by Eurostat and improvements can be expected as a result of the Regulation on the European System of National and Regional Accounts 1995 (ESA 95) in the second quarter of 1999 and of the Regulation on short-term statistics from 1999 onwards. In addition, a further initiative was launched to harmonise measures of real GDP in the context of the Stability and Growth Pact. Concerning the current situation, while national accounts deflators at the aggregate level provide a reasonable basis for analysis, they contain data which are estimated for several smaller countries that do not yet report quarterly national accounts. Producer price statistics vary to some degree in terms of the definitions used. Standardised labour cost measures are currently not available for all countries at a quarterly frequency, but are expected to be available as from spring 1999.

Output and demand statistics

Data on euro area GDP and its expenditure components are published by Eurostat. The quarterly statistics include an estimate for those Member States which do not yet produce quarterly accounts. Euro area-wide estimates of GDP are also constructed by the ECB on the basis of national data (not presented in the section on "Euro area statistics"). Differences between aggregates published by Eurostat and estimates based on national data can occur owing to the treatment of working days and seasonal adjustment in the respective sources, notably for German data. As mentioned above, the implementation of the ESA 95 will broaden the availability of national accounts data during 1999.

In addition, both quantitative and qualitative short-term indicators, namely industrial production and survey data (for example, on confidence in the consumer, industrial and construction sectors) are available on a monthly basis in all Member States. Many of the quantitative data examined by the ECB are covered by the EU Regulation on short-term statistics, and improvements in data provision at the euro area level are expected. The coverage of countries, the comparability of the data and the timeliness of data releases in the Member States are the main concerns in respect of the industrial output data. This is also the case for retail trade turnover and other kinds of information on activity in the services sector. Thus national data currently provide valuable supplementary information.

Labour market statistics

As regards employment statistics, quarterly and sometimes monthly data are available for most countries. The data are derived from different sources (surveys, registers) and are therefore not yet fully comparable. A reliable, timely and high frequency sectoral breakdown of employment is not yet available. Data on unemployment are published by Eurostat on a standardised basis, and may therefore differ from results quoted at the national level. A breakdown of short-term and long-term unemployment on a standardised basis at monthly frequency, though desirable, is not currently possible. Besides the two EU Regulations mentioned above, the results of the new regular labour force surveys, also introduced by EU Regulations, will improve the data available in the near future.

3 Output, demand and labour market developments

Slower output growth in the third quarter

Data available at this juncture suggest slower euro area-wide output growth in the second half of 1998, following robust growth throughout the first half of the year. (For methodological remarks on the data used for analysing output, demand and the labour market, see Box 5.) This is consistent with expectations that the deterioration in the external environment would eventually also have some effect on activity in the euro area. A first estimate by Eurostat for the third quarter of 1998 indicates a rise in euro area-wide real GDP of 2.4%, compared with the same period a year earlier (see Table 2). This compares with an average rate of year-on-year growth of 3.1% in the first half of 1998. The first half of 1998 as a whole may serve as the most appropriate point of reference, rather than the quarterly profile of GDP growth, as it takes into account the fact that the first two quarters were heavily influenced by calendar effects related to the timing of Easter. As the published quarterly data are not corrected for the effect of the different number of working days, they suggest, prima facie, a substantial decrease in GDP growth to 2.5% in the second quarter, and thus only a marginal further slowdown in the third quarter.

The pattern of a more moderate economic expansion since the spring of 1998 is reflected in slower growth in industrial production. Compared with a year earlier, the overall index of industrial production increased by 4.0% in the third quarter of 1998, following increases of 4.4% in the second quarter and 6.3% in the first quarter. Figures released by national authorities are in some cases available up to October and point to a further deceleration in production growth. Output in manufacturing, in which conjunctural variations are typically most strongly reflected, saw a decline in growth from 7.3% in the first quarter of 1998 to 5.0% in the second and 4.3% in the third quarter, primarily owing to a slowdown in industries producing intermediate goods. Industries producing capital goods also saw lower growth rates after the strong first quarter. However, they maintained robust production growth of around 7%, most of which was due to vehicle production. Judging from the average increase in new passenger car registrations in October

Table 2

Output, demand and labour market developments in the euro area

(annual percentage changes, unless otherwise indicated)

	1995	1996	1997	1997 Q4	1998 Q1	1998 Q2	1998 Q3	1998 May	1998 June	1998 July	1998 Aug.	1998 Sep.	1998 Oct.
								3-month centred moving averages					
Real gross domestic product	2.2	1.6	2.5	3.2	3.8	2.5	2.4	-	-	-	-	-	-
Industrial production excl. construction	3.4	0.0	4.1	5.7	6.3	4.4	4.0	4.4	4.7	4.0	4.0	.	.
of which:													
Manufacturing	3.5	-0.2	4.7	6.4	7.3	5.0	4.3	5.0	5.3	4.4	4.3	.	.
by main industrial groupings:													
Intermediate goods	2.5	-0.6	5.4	7.2	7.3	4.3	3.3	4.3	4.3	3.6	3.3	.	.
Capital goods	7.3	1.7	4.2	6.1	9.2	6.6	7.0	6.6	7.5	6.7	7.0	.	.
Consumer goods	1.0	-0.6	1.9	3.0	3.4	3.8	3.5	3.8	4.4	3.5	3.5	.	.
Construction	0.0	-2.3	-1.2	-0.1	3.0	0.0	-1.9	0.0	0.7	-0.6	-1.9	.	.
Capacity utilisation (%) 1)	82.6	80.3	81.6	82.7	83.1	83.6	83.3	-	-	-	-	-	-
Economic sentiment index	0.6	-2.5	2.7	3.7	3.9	4.5	3.1	4.5	4.3	3.7	3.1	2.2	1.9
Consumer confidence indicator 2)	-1	-8	-3	1	4	7	7	7	7	7	7	8	9
Industrial confidence indicator 2)	6	-8	3	8	10	10	7	10	9	8	7	5	3
Construction confidence indicator 2)	-3	-13	-10	-8	-1	2	10	2	4	7	10	9	9
Retail sales, constant prices	2.0	1.1	0.9	2.2	2.7	1.8	3.0	1.8	2.7	2.9	3.0	.	.
New passenger car registrations	0.3	6.6	3.9	11.2	12.6	3.3	7.5	3.3	6.5	6.6	7.5	5.1	7.8
Employment (whole economy)	0.4	0.2	0.3	0.5	1.0	1.1	1.4	-	-	-	-	-	-
Unemployment (annual change in 000s)	-306	422	105	-28	-417	-699	-901	-699	-797	-864	-901	-961	-1008
Unemployment (% of labour force)	11.4	11.6	11.7	11.6	11.3	11.1	11.0	11.1	11.1	11.0	11.0	10.9	10.9

Sources: Eurostat, European Commission Business and Consumer Surveys, ACEA/A.A.A., national data and ECB calculations.
Note: For further information on the data used, see the respective tables and charts in the "Euro area statistics" section of this Bulletin. All data are seasonally adjusted, apart from industrial production (working day adjusted), retail sales and new passenger car registrations.
1) Data are collected in January, April, July and October of each year. The quarterly figures shown are the average of two successive surveys, i.e. the surveys conducted at the beginning of the quarter in question and at the beginning of the following quarter.
2) Percentage balances; data shown are calculated as deviations from the average over the period since January 1985.

and November, this positive influence may have continued in the fourth quarter. Finally, production in consumer goods also expanded at a fairly stable rate of around 3.5% over the past three quarters.

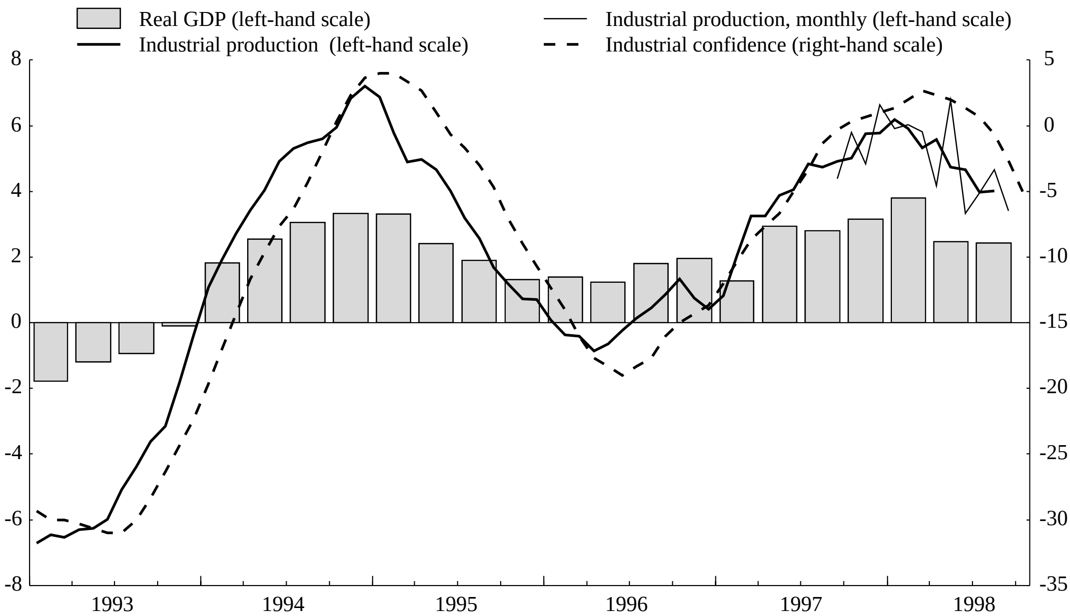
Variations in the indicator of industrial confidence, as reported in the European Commission survey, are largely due to changes in the assessments for order books and changing production expectations. In the manufacturing sector, in line with the deterioration in the global environment, assessments of order books successively worsened in the months from August to November after having remained broadly unchanged during the first half of 1998. The deterioration was slightly more pronounced in the case of export orders than in that of domestic orders. In addition, production expectations became more pessimistic. Overall, this led to a worsening in industrial confidence which, when measured on the basis of a three-month centred moving average, declined significantly towards the end of the year to a level close to its average over the past ten years. As developments in industrial confidence have typically provided a fairly reliable guide to near-term developments in production and business fixed investment, recent trends would suggest that there may have been a further reduction in the growth rate of real GDP towards the end of 1998 (see Chart 7).

On a seasonally adjusted basis, capacity utilisation declined by 0.3 percentage point in the third quarter of last year but, at 83.3%,

Chart 7

Output and industrial confidence in the euro area

(annual percentage changes; percentage balances for industrial confidence)



Sources: Eurostat and European Commission Business and Consumer Surveys.
Note: For further information on the data used, see the respective tables and charts in the "Euro area statistics" section of this Bulletin. All data are seasonally adjusted; data for industrial production (total, excluding construction) and industrial confidence are three-month centred moving averages.
Latest observation: Real GDP: 2.4% (Q3 1998); industrial production (three-month centred moving average): 4.0% (Aug. 1998); industrial production (monthly): 3.4% (Sep. 1998); industrial confidence (three-month centred moving average): -5 (Oct. 1998).

remained 1½ percentage points above its long-term average and also above the peak level recorded in mid-1995. Up to the third quarter of 1998 equipment had been run at above-average levels of capacity for a year without inducing a strong pick-up in fixed capital formation in order to ease capacity constraints. The explanation may be that expectations about the order position and about production related more to the immediate future, while investment decisions are typically taken on the basis of considerations that take a longer time horizon into account.

Concerning the construction sector, production growth declined noticeably in the second quarter of 1998 and turned negative in the third. However, confidence in the construction sector started to increase in early 1998 and in the second half of the year exceeded somewhat the levels seen during the short-lived recovery at the end of 1994. While output developments over the first half of the year, taking into account weather conditions, appeared to be in line with a continuation of the gradual recovery that started in the second half of 1997, third-quarter data seem to indicate renewed weakness. Nevertheless, given sustained confidence, the most recent output data in this sector might contain temporary components.

An encouraging sign is that there has been no evidence as yet of a slowdown in consumption demand. Following a period of broadly unchanged consumer confidence during the summer months of last year, there was a renewed increase in optimism up to November, with confidence reaching a level that was only marginally below the highest level reached in the past ten years. Actual and expected increases in employment as well as increases in purchasing power owing to the fall in energy prices may have contributed to continued improvements in consumer confidence, as reported in recent European Commission surveys. Also, after taking into account the effects of an increase in indirect taxes on the quarterly pattern in the first and second quarters of 1998, retail sales volumes appear to have expanded at a fairly stable rate of over 2% during the first half of the year. When measured on the basis of three-month moving averages, latest data available for 1998 point to an acceleration.

Employment continued to increase

Notwithstanding recent signs of a weakening in economic activity, euro area employment continued to improve during the autumn. Using national data, total employment in the euro area is estimated to have risen by 0.4% in the third quarter of 1998 compared with the previous quarter. Thus the rise in employment observed from spring 1997 onwards was consolidated over the first three quarters of 1998, with yearly growth rates rising above 1% (see Table 2). Employment in the manufacturing sector, which represents around one-fifth of total employment, also continued to increase in the third quarter, albeit at a slower pace (0.4% quarter-on-quarter, compared with 0.8% and 1.2% in the second and first quarters respectively), reflecting the slowdown in activity in this sector. In turn, employment growth in other sectors, notably the services sector, appears to have accelerated somewhat.

Unemployment declined at a gradual pace

Reflecting recent increases in employment, unemployment in the euro area has declined since October 1997. However, the decline in the standardised unemployment rate has been very gradual and the reduction, as measured by published data, has repeatedly stalled. This was again the case in November 1998, when the unemployment rate was estimated by Eurostat to have remained unchanged from the previous month at 10.8%, compared with 10.9% in September and 11.6% a year earlier. One possible explanation for the slow pace of decline in the unemployment rate is that more people may have been registering with labour offices as a result of a growing perception that job prospects have been improving.

In terms of absolute levels, the number of jobless in the euro area is estimated to have fallen by just over 1 million in the 12 months to November 1998. This is approximately twice as much as the fall in unemployment observed during the short-lived upturn in 1994-95. According to Eurostat data on unemployment by age, the recovery in net job creation appears to have been to the benefit of, in particular, people under 25 years of age.

4 Exchange rate and balance of payments developments

Foreign exchange market developments reflect global uncertainties

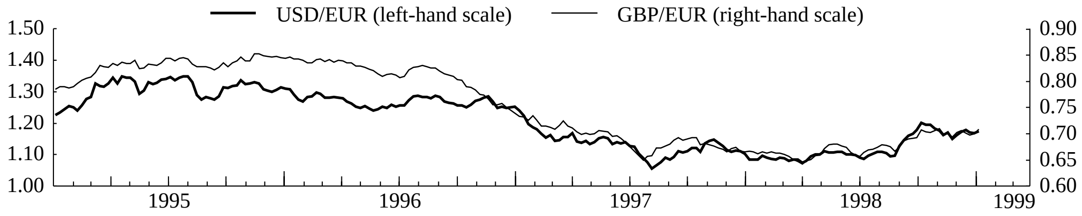
Even though financial markets in most parts of the world recovered towards the end of 1998, indicators of global economic conditions remained mixed, and the risks associated with growth in world output and trade continued to be predominantly on the downside. As a result, foreign exchange markets remained relatively volatile in December.

Starting from a level of USD 1.15 at end-November, the ECU appreciated against the dollar in the first half of December to reach a level of USD 1.18, inter alia amid some leading indicators and corporate profit developments pointing to a slowdown in the US economy. However, subsequent data releases showed solid growth of the US economy in the third quarter of 1998 and a number of indicators suggested continued strong consumer expenditures. As a result, later in December the ECU depreciated somewhat and, at USD 1.17, ended the month slightly above its end-November level. The euro, after the first few days of trading, stood at USD 1.16 at the end of the reporting period, i.e. on 7 January 1999.

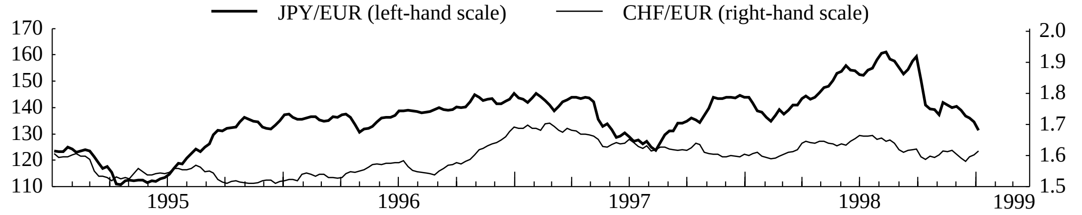
Chart 8

Patterns in exchange rates [1]

(weekly averages)



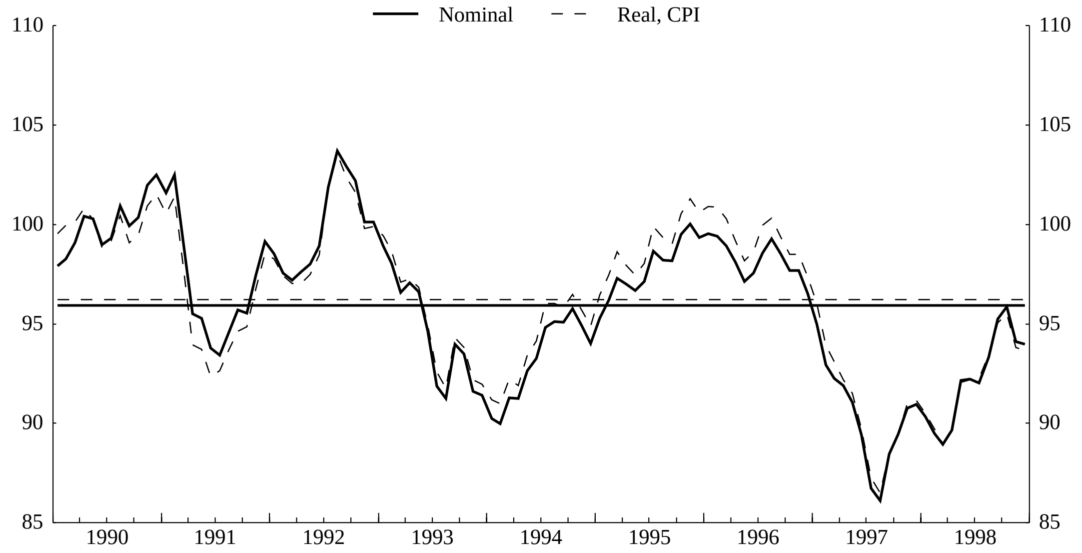
Latest observation: USD/EUR: 1.17 (4 Jan. to 7 Jan. 1999); GBP/EUR: 0.71 (4 Jan. to 7 Jan. 1999).



Latest observation: JPY/EUR: 131.39 (4 Jan. to 7 Jan. 1999); CHF/EUR: 1.61 (4 Jan. to 7 Jan. 1999).

Effective exchange rates of the euro area; index 1990 = 100 [2]

(monthly averages)



Latest observation: Nominal effective: 94.0 (Dec. 1998); real effective: 93.6 (Dec. 1998).

Source: BIS.

1) *Data shown are bilateral exchange rates against the ECU up to the end of 1998. From the start of 1999 data are euro exchange rates. For the first week of January 1999, data are the average values for the period from 4 to 7 January 1999.*

2) *BIS calculations; data are weighted averages of euro area countries' effective exchange rates against the euro area's trading partners (see Table 10 in the "Euro area statistics" section of this Bulletin). An upward movement of the index represents a currency appreciation for the euro area. Horizontal lines are averages over the period shown.*

Against the Japanese yen the ECU depreciated significantly during December, falling from JPY 142 at end-November to a level of JPY 133 at end-December. This primarily reflected the strong appreciation of the yen against the dollar, which was seen by the markets as mainly related to repatriation flows to Japan rather than to fundamental improvements in the economic outlook for the Japanese economy. According to the Bank of Japan's quarterly "Tankan" survey, business sentiment actually worsened slightly in December, compared with the situation three months earlier. On 7 January 1999 the euro was quoted at JPY 129.

Vis-à-vis the currencies of the other major trading partners, the United Kingdom and Switzerland, the ECU closely followed the pattern vis-à-vis the US dollar in the case of the pound sterling, while remaining broadly unchanged against the Swiss franc. At the end of the reporting period, the euro exchange rate against the pound sterling was GBP 0.71. Against the Swiss franc, the euro stood at CHF 1.62.

Euro area effective exchange rate stable

Owing to roughly offsetting movements vis-à-vis the US dollar and the pound sterling, on the one hand, and the yen, on the other, the nominal effective exchange rate of the euro area currencies, as measured by the Bank for International Settlements (BIS), remained broadly unchanged in December from the month before (see Chart 8). Its December 1998 average level was, however, around 4% higher than that recorded on average in the first half of 1998. It thereby made up ground lost in the course of 1997, while remaining somewhat below the average level observed during the 1990s. In real terms, deflated by the relative CPIs, the effective exchange rate of the euro area in December 1998 was estimated at around 3.5% above its average level in the first half of 1998, while also remaining below its long-term average level. During the first few days of January 1999 the nominal effective exchange rate of the euro area remained broadly unchanged.

Cumulative trade balance surplus almost unchanged

Little information is available as yet on overall balance of payments developments for the euro area (see Box 6). Against this background, remarks are made only on external trade data produced by Eurostat, based on gross data for exports and imports between the euro area and the rest of the world, excluding intra-euro area transactions. Balance of payments data will become available in the course of 1999.

In summary, the trade balance surplus for the euro area in September 1998 (the latest month for which data are available) was ECU 5.2 billion, i.e. ECU 1.6 billion lower than in the

Table 3

Trade in goods of the euro area

	1996	1997	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2	1998 Q3	1998 Aug.	1998 Sep.
Exports											
ECU billions	663.9	754.4	168.6	189.7	191.7	204.4	192.6	202.6	193.5	55.8	65.6
Annual percentage changes	7.3	13.6	7.3	15.1	18.6	13.4	14.3	6.8	1.0	1.8	-3.2
Imports											
ECU billions	590.5	666.8	156.7	166.2	165.7	178.3	180.1	178.3	168.7	49.5	60.4
Annual percentage changes	5.7	12.9	6.3	13.3	18.0	14.3	15.0	7.3	1.8	1.7	-1.0
Trade balance											
ECU billions	73.5	87.6	11.9	23.6	26.0	26.1	12.5	24.3	24.8	6.3	5.2
ECU billions, cumulative [1]	73.5	87.6	11.9	35.5	61.5	87.6	12.5	36.9	61.7	56.5	61.7

Source: Eurostat.
1) In the year to date.

Box 6

The balance of payments for the euro area: methodological issues

The production of overall balance of payments figures for the euro area is undergoing a major methodological revision. Euro area balance of payments aggregates could be compiled, in principle, by adding up the net balances of payments of the individual Member States involved. In theory, such a method should yield accurate estimates of the net balance of payments of the 11 participating countries vis-à-vis the rest of the world, since the addition of national data would imply the netting-out of intra-euro area transactions. In practice, however, bilateral data do not fully match, resulting in discrepancies at the euro area level.

In order to overcome such problems, for data starting from January 1999 onwards, and for historical data, each Member State will provide balance of payments data which are compiled using an alternative common methodology. The euro area balance of payments statistics will be compiled by aggregating – on a gross basis – the extra-euro area balance of payments data reported by the 11 participating countries. As from April 1999 the ECB will publish monthly balance of payments figures using this methodology.

As from July 1999 the ECB will also publish, in co-operation with the Statistical office of the European Commission (Eurostat), a quarterly balance of payments for the euro area with a more detailed breakdown of the main items of the financial account (direct investment, portfolio investment, financial derivatives, other investment and reserve assets) as well as investment income.

corresponding month in 1997. Focusing on the third quarter of 1998, the value of exports, at ECU 194 billion, was only marginally higher than in the third quarter of 1997. Imports of goods likewise increased only modestly, from ECU 166 billion to ECU 169 billion, over the same period. This contrasts sharply with the high growth rates seen for imports and exports in the period up to early 1998, i.e. before the world economy was adversely affected by developments in Asia and Russia. Over the first nine months of the year the cumulative surplus in the trade balance reached ECU 61.7 billion, a figure virtually unchanged in nominal terms from that for the same period in 1997. Underlying these developments were declining commodity prices, on the one hand, and weaker demand for exports, on the other.

The stability-oriented monetary policy strategy of the Eurosystem

In October and December 1998, the Governing Council of the European Central Bank (ECB) announced the main elements of its stability-oriented monetary policy strategy to the public. This strategy is designed to maintain price stability in the euro area, thereby fulfilling the mandate given to the European System of Central Banks (ESCB) by the Treaty establishing the European Community (the "Treaty"). The strategy will guide the single monetary policy of the Eurosystem, i.e. the ECB and the national central banks (NCBs) of the 11 Member States which adopted the euro from the start of Stage Three of Economic and Monetary Union (EMU) (see "The Eurosystem and the European System of Central Banks (ESCB)" in this Bulletin). The stability-oriented strategy of the Eurosystem consists of three main elements: a quantitative definition of the Eurosystem's primary objective, namely price stability, and the "two pillars" of the strategy used to achieve this objective. These pillars are a prominent role for money, as signalled by the announcement of a quantitative reference value for the growth rate of a broad monetary aggregate, and a broadly based assessment of the outlook for price developments and risks to price stability in the euro area as a whole.

1 Price stability and its importance

The Treaty states that "*the primary objective of the ESCB shall be to maintain price stability*" (see Box 1: The Eurosystem's mandate: Key excerpts from the Treaty). In order to fulfil this clearly defined mandate, the Treaty accords the ESCB and, by implication, the Eurosystem a considerable degree of institutional independence, albeit supplemented by extensive obligations concerning transparency and accountability.

The logic of the Treaty is clear. By unambiguously assigning the primary objective of price stability to an independent central bank, the Treaty recognises that focusing monetary policy on the maintenance of price stability in the euro area ensures that it will make the best possible contribution to the broader economic objectives of the European Union and its citizens. This view is rooted in the belief – confirmed by decades of practical experience and a substantial body of empirical economic research – that a monetary policy that maintains price stability in a credible and lasting way will make the best overall contribution to improving

Box 1

The Eurosystem's mandate: Key excerpts from the Treaty

Article 105 (1)

The primary objective of the ESCB shall be to maintain price stability. Without prejudice to the objective of price stability, the ESCB shall support the general economic policies in the Community with a view to contributing to the objectives of the Community as laid down in Article 2.

Article 2

The Community shall have as its task … to promote throughout the Community a harmonious and balanced development of economic activities, sustainable and non-inflationary growth respecting the environment, a high degree of convergence of economic performance, a high level of employment and of social protection, the raising of the standard of living and quality of life, and economic and social cohesion and solidarity among Member States.

Article 3a

For the purposes set out in Article 2, the activities of the Member States and the Community shall include … the definition and conduct of a single monetary policy and exchange-rate policy the primary objective of both of which shall be to maintain price stability and, without prejudice to this objective, to support the general economic policies in the Community.

Box 2

The benefits of price stability

A large number of economic arguments point to the benefits of price stability. This box focuses specifically on the benefits of price stability for real economic growth and employment prospects. Among the main arguments are:

1. Price stability improves the transparency of the *relative price mechanism*, thereby *avoiding distortions* and helping to ensure that the market will *allocate real resources efficiently* both across uses and across time. A more efficient allocation will raise the productive potential of the economy. In this sense, price stability creates an environment in which the necessary structural reforms implemented by national governments to increase the flexibility and efficiency of markets can be most effective.

2. As discussed in the main text, stable prices *minimise the inflation risk premium* in long-term interest rates, thereby lowering long-term rates and helping to stimulate investment and growth.

3. If the *future price level is uncertain, real resources are diverted to hedging* against inflation or deflation, rather than being put to productive use. Credibly maintaining price stability avoids these costs and provides the environment for efficient real investment decisions. Price stability also eliminates the real costs entailed when *inflation or deflation exacerbates the distortionary effects of the tax and welfare system* on economic behaviour.

4. Maintaining price stability *avoids the large and arbitrary redistribution of wealth and incomes* that arises in inflationary as well as deflationary environments, and therefore helps to maintain social cohesion and stability.

These arguments collectively suggest that maintaining price stability in itself contributes to the achievement of output or employment goals. The logic underlying both the Treaty and the Eurosystem's stability-oriented monetary policy strategy is therefore that output and employment goals are best served by a monetary policy that focuses on price stability.

In addition, the empirical evidence strongly suggests that the benefits of price stability for real economic performance are significant. Several studies have shown that, across a large number of countries, nations with lower inflation appear, on average, to grow more rapidly (for example, Robert J. Barro demonstrates this in *Determinants of economic growth,* MIT Press, 1997). Furthermore, empirical estimates of the benefits of price stability can be very substantial. A number of studies have shown that the costs incurred when inflation exacerbates the distortions inherent in tax and benefit systems are considerable (see, for example, Martin S. Feldstein, *Costs and benefits of price stability*, Chicago University Press, to be published in 1999). Extension of this analysis to several euro area countries suggests that the benefits of maintaining price stability in these contexts may be even higher than in the United States.

economic prospects and raising living standards. Box 2 reviews the main arguments why the benefits of price stability for growth and employment are substantial.

The Treaty also recognises that the Eurosystem's single monetary policy will interact with policies implemented by other institutions in the European Union. Given the potential risk of political intervention in the design and implementation of the single monetary policy, the Treaty made the ECB and the national central banks (NCBs) independent of national governments and political interference. This institutional independence allows the Eurosystem to pursue price stability in an appropriate medium-term framework and thereby significantly enhances the credibility of monetary policy. It is widely recognised that a central bank lacking independence is susceptible to short-term pressures that may be prejudicial to the maintenance of price stability. The Eurosystem's institutional independence, as guaranteed in the Treaty, therefore serves the interests of the public, which benefits from the resulting environment of stable prices.

Price stability and the exchange rate

However, institutional independence does not mean isolation. The Eurosystem will interact with other policy-makers, for example with regard to exchange rate policy. Since exchange rate policy must be consistent with monetary policy, the Treaty states that the primary objective of the Community's exchange rate policy is the maintenance of price stability. In this context, the Treaty assigns the Eurosystem the "basic task" of conducting "foreign exchange operations consistent with the provisions of Article 109". Article 109 foresees that the Council of Ministers (in the composition of the Ministers of Finance), acting with unanimity, may conclude "formal agreements on an exchange rate system for the euro in relation to non-Community currencies". In addition, it notes that, acting with a qualified majority, the Council of Ministers can also issue "general orientations" to the Eurosystem concerning exchange rate policy. Regarding the former issue, the Council of Ministers clarified in a report to the European Council in December 1997 that, in all likelihood, a formal exchange rate system of this type will not be established in the foreseeable future. In the same report, the Council of Ministers announced, albeit in a not legally binding form, that they will only issue "orientations" in exceptional circumstances, for example in the case of a clear misalignment.

In the present circumstances – in which there is neither a formal exchange rate agreement nor a general orientation – the euro exchange rate is the outcome of current and expected monetary and other policies in both the euro area and elsewhere, and of the perception of these policies by market participants. As the Eurosystem's monetary policy strategy does not embody an exchange rate target for the euro, the task of focusing on the maintenance of price stability in the euro area is facilitated.

Monetary policy and support for general economic policies

Reflecting the broad need for mutual co-operation and dialogue among policy-makers in an interdependent environment, the Treaty requires the Eurosystem to *"support the general economic policies in the Community with a view to contributing to the objectives of the Community laid down in Article 2"*. At the same time, in further recognition of the dangers of political interference in monetary policy, the Treaty states that the Eurosystem's actions must be *"without prejudice to the objective of price stability"*. Both the logic of the Treaty and the argumentation in Box 2 strongly suggest that the best contribution the single monetary policy can make in this supportive role is to focus unambiguously on maintaining price stability over the medium term and thereby creating the stable environment in which other policies can be most effective. In the absence of such recognition, the danger exists that the public would come to doubt the Eurosystem's commitment to maintaining price stability. Inflation expectations and risk premia would rise, increasing longer-term interest rates and raising the cost of investment required to produce sustainable and lasting increases in the standard of living.

In this respect, the Governing Council of the ECB is highly concerned about the current high level of unemployment in the euro area. However, this problem is overwhelmingly structural in origin. It is caused mainly by the inflexibility of euro area labour and goods markets resulting, in part, from excessive or inappropriate regulation in these markets. Structural economic reforms aimed at reducing these inflexibilities are the appropriate policy response. In those euro area countries where such reforms have been implemented, unemployment has fallen substantially. Effective euro area-wide structural policies would lead

Box 3

Transparency and accountability of the Eurosystem

In general, central banks should be open, transparent and accountable, reporting fully to the public on their activities, including their conduct of monetary policy. A transparent and accountable central bank reinforces its credibility by communicating clearly with the public and thereby signalling that its monetary policy is appropriately oriented to the maintenance of price stability. In this regard, the Eurosystem meets or exceeds the best practices of any central bank.

The President of the ECB will hold a press conference immediately after the first Governing Council meeting of every month. On these occasions, the President will present an extensive statement of the Council's view of the economic situation and the outlook for price developments, followed by a question and answer session. The schedule for these meetings and conferences has already been announced for 1999. This regular statement will be supplemented by the publication of a Monthly Bulletin. The Monthly Bulletin is intended to provide the general public and financial markets with a thorough assessment of the economic environment, as well as with articles about the economy's structure and topical issues important for the single monetary policy.

Furthermore, the Eurosystem's balance sheet will be published weekly. An annual report on the activities of the Eurosystem must be produced, supplemented by the production of quarterly reports. These reports are to be submitted to the European Parliament, the Council of Ministers and the Commission of the European Communities. The European Parliament will hold a general debate on the reports that it receives. The ECB President and Executive Board members have to answer questions posed by the European Parliament's committees. The President will appear before the parliamentary committee five times each year, following the submission of the quarterly and annual reports mentioned above.

In speeches, members of the Governing Council will also inform the public about monetary policy and the economy. Working papers and technical analysis by ECB staff will be published for professional review and scientific assessment. These articles and other presentations will address not only the central issue of monetary policy and the monetary transmission mechanism, but also the major economic problems facing Europe, not least the problem of the high level of unemployment.

Through all these media, the ECB is committed to communicating with the public in a clear and transparent manner. Against this background, the Eurosystem clearly demonstrates high levels of transparency and accountability.

to higher trend real growth. Within its monetary policy strategy, the Eurosystem would naturally take account of such higher growth. However, attempting to reduce unemployment by implementing an inflationary monetary policy would ultimately be self-defeating, since such a policy would only undermine price stability over the medium term, which is the basis for lasting and sustainable employment growth.

Transparency and accountability

All central banks operate in a certain social, political and institutional environment. In a democratic context, it is vital that an independent central bank is open, transparent and clear about the reasoning for its actions, and accountable for its performance. Recognising the importance of these issues in the euro area, the Treaty imposes on the Eurosystem some of the most stringent reporting obligations required of any central bank. In practice, the Eurosystem has already committed itself to exceeding even these stringent requirements (see Box 3: Transparency and accountability of the Eurosystem).

2 The role of a monetary policy strategy

The primary objective of the single monetary policy is the maintenance of price stability. However, the Eurosystem, like all central banks, cannot control the price level directly by using the monetary policy instruments at its disposal. Instead, central banks face a complex transmission process from their own monetary policy actions to changes in the general price level. This transmission mechanism of monetary policy is characterised by the existence of several distinct channels, each with long, variable and not fully predictable lags. Moreover, the transmission mechanism itself is continuously evolving in response to changes in economic behaviour and institutional structure.

Because the transmission mechanism is complex, the preparation, discussion and presentation of monetary policy decisions must be placed in a coherent clarifying framework. This is the role of the monetary policy strategy. The strategy fulfils two crucial tasks.

- *First*, the strategy imposes a clear structure on the policy-making process itself. The strategy must ensure that the Governing Council has the information and analysis it requires to take effective monetary policy decisions that will maintain price stability. The Governing Council must work within a coherent analytical framework that allows developments in the economic environment to be mapped into appropriate decisions on the terms offered in the Eurosystem's open market operations and on its standing facilities. Using these instruments, the Eurosystem can exercise considerable operational control over short-term market interest rates, which then feed through to other economic variables and, ultimately, the price level.

- *Second*, the Eurosystem's monetary policy strategy is a vehicle for communicating with the public. Monetary policy is most effective when it is credible – that is, when the public is completely confident that monetary policy is fully committed to the objective of price stability and is being implemented in a manner that will effectively achieve this goal. Therefore, the monetary policy strategy must not only signal the overriding objective of monetary policy, but must also convince the public that this objective will be achieved.

In designing a monetary policy strategy to fulfil these two complementary roles, knowledge about how the economy works is essential. In particular, an awareness is required regarding the information about future threats to price stability that can be extracted from observing current developments in the economic situation; that is, the *indicator properties* of monetary, financial and other economic variables for price developments must be analysed.

Moreover, it is vital to understand broadly how monetary policy, through short-term nominal interest rates, will affect the economy in general and, ultimately, the price level. Understanding the transmission mechanism will help to allow judgements to be formed about whether the policy measures taken are appropriate to address the threats to price stability revealed by the indicator variables.

A monetary policy strategy is therefore a coherent and structured description of how monetary policy decisions will be made in the light of the behaviour of economic indicators, in order to achieve the overriding objective of price stability.

3 Criteria for selecting the monetary policy strategy of the Eurosystem

General criteria

In order to fulfil the aims described above, the Eurosystem's monetary policy strategy must satisfy certain general criteria. Foremost among these criteria is the principle of *effectiveness*. The best monetary policy strategy for the Eurosystem is the one which best ensures the achievement of, and signals a credible and realistic commitment to, the primary objective of price stability.

As discussed above, for a monetary policy strategy to be effective, it must be credible. In other words, the public in general, and the financial markets in particular, must be convinced that the Governing Council of the ECB is committed to maintaining price stability, has the instruments and expertise to do so, and is implementing monetary policy with this objective in mind.

In order to build a good reputation, and thereby the necessary credibility to implement the single monetary policy successfully and effectively, the Eurosystem's monetary policy strategy has to satisfy a number of other criteria.

- The strategy must be *clear* and *understandable*. If there is ambiguity about the objective of monetary policy or how this objective will be achieved, unnecessary uncertainty will be created in the minds of the public.
- Furthermore, the strategy must be *transparent*. The public must be presented ex ante with information about how monetary policy decisions are being made by the Governing Council and the economic rationale on which they are based.
- The strategy must ensure that the Eurosystem is *accountable* both for its policy actions and for its performance in achieving the primary objective of price stability. In the view of the Governing Council, this entails the publication of a quantified objective against which the public can sensibly judge the performance of the Eurosystem and its single monetary policy.
- Finally, the strategy must be *consistent with the Eurosystem's institutional independence*.

The specific environment at the start of Monetary Union

In addition to the general criteria outlined above, certain important characteristics of the specific environment faced by the Eurosystem at the start, and in the early years, of Stage Three have also had to be taken into account.

Building credibility is particularly important for the ECB at the outset of Stage Three since it is a new institution, lacking an independent track record or reputation of its own. The participating NCBs that are components of the Eurosystem have, over the years, built up a strong reputation for maintaining price stability. By ensuring as much continuity as possible with the objectives and successful performance of the NCBs prior to Monetary Union, the Eurosystem can inherit this reputation, to the benefit of its credibility in the future.

However, the Eurosystem faces a unique situation at the start of Monetary Union. Of particular concern to the Eurosystem in these special circumstances are those uncertainties that inevitably arise as a result of the move to Stage Three itself. These relate, in particular, to the way in which the transition to Stage Three of EMU will affect economic behaviour, institutional structures and statistical series in the euro area.

The adoption of the single monetary policy marks a significant *regime shift*. The transformation of the institutional arrangements for deciding and implementing monetary policy will change the structure of important sectors of the economy, especially the financial system. Moreover, the regime shift is likely to change the way expectations are formed in the euro area. This may already have been seen in recent years in many countries, where the adoption of a credible and lasting commitment to price stability has been stabilising longer-term inflation expectations at new, low levels.

As a consequence, empirical relationships between economic variables that have been estimated using data from the past may become unstable should behaviour change in this new environment. These changes may complicate the Eurosystem's assessment of economic conditions because the indicator properties of monetary, financial and other economic variables for future price developments may be altered.

As regards the structure of the euro area economy, behavioural changes at the outset of Stage Three might be particularly pronounced in the financial sector, where the impact of Monetary Union may be most immediate. For example, the behaviour of monetary aggregates – which consist largely of bank deposits – might be affected by the transition to Stage Three. The introduction of the euro could also lead to changes in the banking system and to private portfolio shifts between monetary and non-monetary assets.

However, structural and institutional change will not be limited to the financial system. In conjunction with the single market programme, the elimination of currency risk in the euro area will increase the transparency of pricing in goods and labour markets and thereby probably raise the intensity of competition and innovation. More generally, consumption and investment behaviour may be affected by the regime shift to an environment of stable prices. In these circumstances, conducting macroeconomic analyses and forecasts will also be complicated, since the historical empirical relationships on which they are largely based may begin to break down.

These uncertainties – arising directly from the transition to Stage Three itself – will be both compounded by and inter-related with the broader economic context in which Monetary Union will be established. The increasing internationalisation of the global economy, and the current rapid pace of technological change, have affected all sectors of the economy. All these effects may change the properties of key indicator variables, which will therefore have to be interpreted with special caution and care.

Furthermore, in many respects, Monetary Union has created an entirely new economic area for which comprehensive and harmonised data have not been collected in the past. A number of fully, or almost fully, harmonised series are now available. These include the euro area monetary data, the balance of payments data and the Harmonised Index of Consumer Prices (HICP). However, these euro area-wide statistics are based, in part, on new concepts, and the properties of the series are not yet well known. Therefore, the uncertainty facing policy-makers concerning the indicator properties of the available euro area statistics is larger than has typically been the case in national contexts in the past.

4 The stability-oriented monetary policy strategy of the Eurosystem

Having considered various options on the basis of the criteria and considerations outlined above, the Governing Council of the ECB announced the Eurosystem's stability-oriented monetary policy strategy to guide its monetary policy decisions in Stage Three of EMU. The main elements of this strategy were presented to the public on 13 October 1998, and have subsequently been elaborated in speeches and statements by the President of the ECB and other members of the Governing Council. The strategy consists of three main elements:

- ♦ a quantitative definition of the primary objective of the single monetary policy, namely price stability; and

- the "two pillars" of the strategy used to achieve this objective:
  - a prominent role for money, as signalled by the announcement of a reference value for the growth of a broad monetary aggregate; and
  - a broadly based assessment of the outlook for future price developments and the risks to price stability in the euro area as a whole.

The quantitative definition of price stability

The definition

The Governing Council has decided to publish a quantitative definition of price stability. A published definition gives clear guidance to expectations of future price developments, helping to build up the credibility of the new strategy. The publication of the Eurosystem's definition of price stability also provides the public with a clear indication for making its assessment of the success of the single monetary policy, thereby making the Eurosystem and its stability-oriented monetary policy strategy transparent and accountable.

Against this background, the Governing Council of the ECB has adopted the following definition: *"price stability shall be defined as a year-on-year increase in the Harmonised Index of Consumer Prices (HICP) for the euro area of below 2%"*. Price stability according to this definition *"is to be maintained over the medium term"*.

The phrase *"below 2%"* clearly delineates the upper bound for the rate of measured inflation in the HICP which is consistent with price stability. At the same time, the use of the word *"increase"* in the definition clearly signals that deflation, i.e. prolonged declines in the level of the HICP index, would not be deemed consistent with price stability.

It should be noted that the Eurosystem's definition of price stability is in line with the definitions used by most NCBs in the euro area prior to the transition to Monetary Union, ensuring an important element of continuity with their successful monetary policy strategies.

The HICP index

The chosen definition identifies the HICP as the price index that should be used in the assessment of whether price stability has been achieved and maintained. This index was initially created for the assessment of price convergence in Stage Two and is largely harmonised across the various countries in the euro area. Use of the HICP is also consistent with the public's usual focus on consumer prices in its assessment of developments in the price level.

Among economists in academic, financial and central banking circles, there is a broad consensus that various forms of so-called "measurement bias" can exist in consumer price indices (CPIs). These biases arise mainly from changing spending patterns and quality improvements in those goods and services that are included in the basket used to define a specific price index. Such biases cannot always be fully corrected in the construction of price indices. The measurement bias typically causes CPIs to overstate slightly the "true" rate of inflation.

The HICP for the euro area is a relatively new concept and long runs of back data do not exist. Therefore, studies of the magnitude of the HICP measurement bias are preliminary and inconclusive. Eurostat has expended considerable effort to reduce or eliminate the measurement bias in the HICP. It is therefore probable that the bias in the HICP is smaller than that observed in national CPIs of the countries comprising the euro area. Moreover, the available empirical evidence suggests that the measurement bias in national CPIs for euro area countries is smaller than that which has been estimated in a number of prominent studies of consumer price indices in other countries.

The success of these attempts to minimise the measurement bias in the HICP is as yet unknown. Furthermore, the size of the measurement bias is likely to change over time as the structure of the economy evolves and statistical methods change, partly in response to these changes in economic structure. Therefore, the definition has avoided explicitly embodying specific estimates of the HICP measurement bias, while allowing for such bias by not setting the lower bound for measured price level increases at zero.

Finally, the Governing Council explained that, by defining price stability in terms of the HICP *for the euro area*, it has made clear that its decisions will be based on an assessment of developments in the euro area as a whole. With a unified monetary policy, policy decisions must be made in a manner that reflects conditions across the euro area in its entirety, rather than specific regional or national developments.

Medium-term orientation

The statement that "*price stability is to be maintained over the medium term*" reflects the need for monetary policy to have a forward-looking, medium-term orientation. It also acknowledges the existence of short-term volatility in prices, resulting from non-monetary shocks to the price level that cannot be controlled by monetary policy. The effects of indirect tax changes or variations in international commodity prices are good examples. The Eurosystem cannot be held responsible for these short-term shocks to the price level, over which it has little control. Rather, assessing the performance of the Eurosystem's single monetary policy over the medium term ensures genuine and meaningful accountability.

Furthermore, in response to some types of unforeseen economic disturbance with an impact on the price level that may threaten price stability, a medium-term orientation of monetary policy is important in order to permit a gradualist and measured response. Such a central bank response will not introduce unnecessary and possibly self-sustaining uncertainty into short-term interest rates or the real economy, while nevertheless ensuring that price stability – and the benefits that it brings – is maintained over the medium term.

The two pillars of the strategy

The reference value – a prominent role for money

Inflation is ultimately a monetary phenomenon. The Governing Council therefore recognised that giving money a prominent role in the Eurosystem's strategy was important. Money constitutes a natural, firm and reliable "nominal anchor" for monetary policy aiming at the maintenance of price stability. The important role played by money in the overall stability-oriented strategy also emphasises the responsibility of the Eurosystem for the monetary impulses to inflation, which a central bank can control more readily than inflation itself.

To signal the prominent role it has assigned to money, the Governing Council has announced a quantitative reference value for monetary growth as one pillar of the overall stability-oriented strategy. The reference value is intended to help the Governing Council analyse and present the information contained in the monetary aggregates in a manner that offers a coherent and credible guide for monetary policy aimed at price stability.

Two characteristics of the quantitative reference value for monetary growth should be emphasised.

- *First*, the reference value was derived in a manner that is consistent with – and serves the achievement of – price stability. To ensure that the reference value is consistent with the maintenance of price stability over the medium term, money must have a *stable* relationship with the euro area price level at this horizon. The stability of this relationship is typically assessed in the context of a money demand function, where a specific monetary aggregate is related to the price level and other macroeconomic variables, such as real income and interest rates.

- *Second*, substantial or prolonged deviations of monetary growth from the reference value would, under normal circumstances, signal risks to price stability over the medium term. This feature requires both that a stable relationship between money and the price level exists and that monetary growth is a *leading indicator* of developments in the price level.

However, the concept of a reference value does not entail a commitment on the part of the Eurosystem to correct deviations of monetary growth from the reference value over the short term. Interest rates will not be changed "mechanistically" in response to such deviations in an attempt to return monetary growth to the reference value. Therefore, the euro area monetary aggregate for which the reference value is announced does not need to be *controllable* in the short run, using a short-term nominal interest rate influenced closely by the Eurosystem. This is one of the main differences between setting a reference value and announcing an intermediate monetary target.

The available empirical evidence suggests that broad monetary aggregates (i.e. measures of money that include a wide spectrum of deposits, embracing time and savings deposits, as well as close substitutes for them, such as marketable short-term bank liabilities) exhibit the properties required for the announcement of a reference value. In the past, the demand for euro area broad money has been stable over the long run. Broad aggregates have been leading indicators of developments in the price level. This contrasts with the empirical properties of euro area narrow money, which, although controllable using short-term nominal interest rates, exhibited neither stability with nor significant indicator properties for the price level. Of course, this evidence has to be treated with some caution, given the statistical and economic uncertainties highlighted above. Nevertheless, the empirical evidence has been judged strong and robust enough for a reference value to be announced for a broad monetary aggregate. The Governing Council has chosen to announce a reference value for the aggregate M3, defined in an encompassing manner to include not only currency in circulation and the conventional deposit components of broad money, but also both the shares/units of money market funds (MMFs) and debt securities issued by monetary financial institutions (MFIs). Conceptual and empirical aspects of the euro area monetary aggregates are discussed in more detail in an article to appear in the February 1999 Monthly Bulletin.

Against this background, the reference value for monetary growth has been derived using the well-known relationship between money, on the one hand, and prices, real gross domestic product (GDP) and the velocity of circulation, on the other. For prices, the derivation of the reference value has to be based on the Eurosystem's published definition of price stability. Furthermore, in view of the medium-term orientation of monetary policy, it is appropriate to base the derivation of the reference value on assumptions about medium-term developments in both real GDP and the velocity of circulation. In this respect, assuming trend growth for real GDP would tend to impart a counter-cyclical property to monetary policy, as GDP growth below trend would normally be associated with lower monetary growth relative to a reference value derived using trend output.

On 1 December 1998 the Governing Council announced its reference value for M3 growth. The derivation of the reference value was based on the following medium-term assumptions.

- Price stability must be maintained according to the Eurosystem's published definition, so that year-on-year increases in the HICP for the euro area are below 2%.

- The trend of real gross domestic product (GDP) growth lies in the range 2-2½% per annum.

- Over the medium term, the decline in the velocity of circulation of M3 is in the approximate range ½-1% each year.

In setting the reference value for monetary growth, the Governing Council emphasised that the Eurosystem's published definition of price stability limits increases in the HICP for the euro area to "*below* 2%". Furthermore, the actual trend decline in velocity is likely to lie somewhat below the upper bound of its ½-1% range. Taking account of these two factors, the Governing Council decided to set its reference value for M3 growth at 4½% per annum.

The Governing Council decided to announce a specific reference rate for monetary growth, rather than a reference range, on the basis that announcing a reference range might be falsely interpreted by the public as implying that interest rates would be changed automatically if monetary growth were to move outside the boundaries of the range, something that would be contrary to the role of the reference value in the overall strategy.

The reference value will help to inform and present interest rate decisions aimed at maintaining price stability over the medium term. Therefore, in the first instance, a deviation of monetary growth from the reference value will prompt further analysis to identify and interpret the economic disturbance that caused the deviation. If this analysis suggests that the disturbance identified indeed points to a threat to price stability, monetary policy would respond in a manner appropriate to counter this risk. The relationship between actual monetary growth and the reference value will therefore be regularly and thoroughly analysed by the Governing Council. The results of this analysis and its impact on monetary policy decisions will be explained to the public. Through this process monetary policy decision-making will be made both clearer and more transparent.

While the presentation of monetary analysis to the public will naturally focus on developments in the "key" broad monetary aggregate M3 in relation to the published reference value for monetary growth, developments in other monetary aggregates, in the various components of M3, and in the counterparts to all these aggregates in the consolidated MFI balance sheet will also be thoroughly assessed on an ongoing basis. Such analysis provides useful background information that helps the assessment of developments in M3.

A broadly based assessment of the outlook for price developments

Although the monetary data contain information vital to informed monetary policy-making, on their own they will not constitute a complete summary of all the information about the economy required to set an appropriate monetary policy for the maintenance of price stability. Therefore, in parallel with the analysis of monetary growth in relation to the reference value, a broadly based assessment of the outlook for price developments and the risks to price stability in the euro area will play a major role in the Eurosystem's strategy. This assessment will be made using a wide range of economic indicators.

This wide range of indicators will include many variables that have leading indicator properties for future price developments. These variables include, inter alia, wages, the exchange rate, bond prices and the yield curve, various measures of real activity, fiscal policy indicators, price and cost indices and business and consumer surveys. Obviously, it will also be useful to look at inflation forecasts derived using all these variables when assessing whether the monetary policy stance is appropriate. In this respect, the Eurosystem will evaluate the full range of inflation forecasts produced by international organisations, other authorities, market participants, etc., and will also produce its own assessment of the future inflation outlook.

However, given behavioural, institutional and structural uncertainties, forecasting price developments in the euro area is inevitably difficult. Inflation forecasts will have to be interpreted with caution and care. Moreover, a forecast cannot encompass all the indicator variables that are important for monetary policy. Nor can it always incorporate indicators in a timely manner. Therefore, a thorough analysis of individual indicator variables plays an important role in the overall broadly based assessment of the outlook for price developments, in addition to any role these variables may have in the forecast. Both forecasts and the analysis of individual indicators will help to inform the Governing Council about the specific nature of the macroeconomic environment and the disturbances to the economy, on which monetary policy decisions would normally depend.

Based on its strategy, the Governing Council has undertaken to offer full and prompt explanations of its assessment of overall economic conditions, including the economic rationale on which it is based. This will present the public with a transparent view of monetary policy-making.

5 Concluding remarks

The Eurosystem's stability-oriented monetary policy strategy, as described above, is a new and distinct strategy, which reflects the unique circumstances and institutional environment that will face the Eurosystem.

The stability-oriented strategy emphasises the overriding priority attached to the maintenance of price stability according to a quantitative definition published by the Eurosystem. The strategy aims to identify those economic disturbances that threaten price stability, and to prompt a monetary policy response which addresses these threats and which is appropriate to both the prevailing economic circumstances and the nature of the threat. The strategy recognises that reliance on a single indicator variable or intermediate target is unlikely to prompt the appropriate response in all circumstances. In particular, mechanical responses to a small number of indicators or forecasts at the start of Stage Three may be especially misguided, given the inevitable uncertainties about economic relationships prompted by the regime shift associated with the transition to Monetary Union.

The stability-oriented monetary policy strategy therefore eschews "mechanistic" monetary policy responses to deviations from a specific target or developments in a specific indicator variable. Instead, a thorough analysis of the monetary data in relation to the quantitative reference value for monetary growth and a broadly based assessment of other economic data will be conducted, with the aim of identifying the economic developments and disturbances that pose a threat to price stability. This analysis will then inform the selection of an appropriate monetary policy response geared to the maintenance of price stability over the medium term.

This strategy requires considerable effort on the part of the Eurosystem to explain its assessment of the economic situation. The Governing Council is committed to exceeding the reporting and communication requirements outlined in the Treaty, which are already among the most stringent imposed on any central bank.

Against this background, the Eurosystem's stability-oriented monetary policy strategy will ensure that price stability over the medium term is maintained in a credible and lasting manner throughout the euro area. This is the best contribution that the single monetary policy can make to raising the standard of living of Europe's citizens.

Euro area statistics

Contents

Statistics

1 Monetary policy statistics

Table 1.1

Consolidated financial statement of the Eurosystem

(EUR millions)

1. Assets

	Gold and gold receivables	Claims on non-euro area residents in foreign currency	Claims on euro area residents in foreign currency	Claims on non-euro area residents in euro	Lending to financial sector counterparties in the euro area			
						Main refinancing operations	Longer-term refinancing operations	Fine-tuning reverse operations
	1	2	3	4	5	6	7	8
1999 1 Jan.	99,598	230,342	6,704	8,939	185,120	144,924	24,698	6,680

2. Liabilities

	Banknotes in circulation	Liabilities to financial sector counterparties in the euro area in euro						Debt certificates issued
			Current accounts (covering the minimum reserve system)	Deposit facility	Fixed-term deposits	Fine-tuning reverse operations	Deposits related to margin calls	
	1	2	3	4	5	6	7	8
1999 1 Jan.	341,708	87,308	84,437	973	1,886	0	12	13,835

Source: ECB.

							Total assets	
				Securities of euro area residents in euro	General government debt in euro	Other assets		
Structural reverse operations	Marginal lending facility	Credits related to margin calls	Other lending					
9	10	11	12	13	14	15	16	
0	6,372	26	2,420	21,650	60,125	84,683	697,160	1999 1 Jan.

							Total liabilities	
Liabilities to other euro area residents in euro	Liabilities to non-euro area residents in euro	Liabilities to euro area residents in foreign currency	Liabilities to non-euro area residents in foreign currency	Counterpart of special drawing rights allocated by the IMF	Capital and reserves	Other liabilities		
9	10	11	12	13	14	15	16	
61,477	9,969	595	3,314	5,765	112,498	60,690	697,160	1999 1 Jan.

Table 1.2

ECB interest rates on standing facilities

(levels in percentages per annum; changes in percentage points)

	Deposit facility		Marginal lending facility	
	Level	Change	Level	Change
	1	2	3	4
1999 1 Jan.	2.00	-	4.50	-
4 Jan. [1]	2.75	0.75	3.25	-1.25

Source: ECB.

1) *On 22 December 1998 the ECB announced that, as an exceptional measure between 4 and 21 January 1999, a narrow corridor of 50 basis points would be applied between the interest rates for the marginal lending facility and the deposit facility, aimed at facilitating the transition to the new regime by market participants.*

Table 1.3

Eurosystem monetary policy operations executed through tenders

(EUR millions; interest rates in percentages per annum)

Main refinancing operations

Date of settlement	Type of operation	Bids (amount)	Allotment (amount)	Fixed rate tenders: Fixed rate	Variable rate tenders: Marginal rate	Variable rate tenders: Weighted average rate	Running for [...] days
	1	2	3	4	5	6	7
1999 7 Jan.	Fixed rate	481,625	75,000	3.00			13

Longer-term refinancing operations

Date of settlement	Type of operation	Bids (amount)	Allotment (amount)	Fixed rate tenders: Fixed rate	Variable rate tenders: Marginal rate	Variable rate tenders: Weighted average rate	Running for [...] days
	1	2	3	4	5	6	7
1999							

Other tender operations

Date of settlement	Type of operation	Bids (amount)	Allotment (amount)	Fixed rate tenders: Fixed rate	Variable rate tenders: Marginal rate	Variable rate tenders: Weighted average rate	Running for [...] days
	1	2	3	4	5	6	7
1999							

Source: ECB.

Table 1.4

Minimum reserve statistics

1. Reserve base of credit institutions subject to reserve requirements [1) 2)]

(EUR millions)

Reserve base as at:	Total	Liabilities to which a 2% reserve coefficient is applied			Liabilities to which a 0% reserve coefficient is applied		
		Deposits (overnight, up to 2 years agreed maturity and notice period)	Debt securities up to 2 years agreed maturity	Money market paper	Deposits (over 2 years agreed maturity and notice period)	Repos	Debt securities over 2 years agreed maturity
	1	2	3	4	5	6	7
1999 1 Jan.	.	.	.	.	.	.	.

Source: ECB.

1) *Liabilities vis-à-vis other credit institutions subject to the minimum reserve system, the ECB and participating national central banks are excluded from the reserve base. If a credit institution cannot provide evidence of the amount of its issues of debt securities with a maturity of up to 2 years and of money market paper held by the institutions mentioned above, it may deduct 10% of these liabilities from its reserve base.*

2) *The reserve base of credit institutions as at 1 January 1999 is used to calculate the minimum reserves for the maintenance period starting on 1 January 1999 and ending on 23 February 1999. The relevant aggregated data will be reported to the ECB by the end of February 1999.*

2. Reserve maintenance [1)]

(EUR millions; interest rates as annual percentages)

Maintenance period ending in:	Required reserves [2)]	Actual reserves [3)]	Excess reserves [4)]	Deficiencies [5)]	Interest rate on minimum reserves [6)]
	1	2	3	4	5
1999 Feb.	.	.	.	.	.

Source: ECB.

1) *This table will contain data for completed maintenance periods. The first maintenance period of the minimum reserve system ends on 23 February 1999.*

2) *The amount of reserve requirement of each individual credit institution is first calculated by applying the reserve ratio for the corresponding categories of liabilities to the eligible liabilities, using the balance sheet data as at the end of each calendar month; subsequently, each credit institution deducts from this figure a lump-sum allowance of EUR 100,000. The resulting reserve requirements for each credit institution are then aggregated at the euro area-wide level.*

3) *Aggregate average daily holdings of credit institutions subject to minimum reserve requirements on their reserve accounts over the maintenance period.*

4) *Average actual reserve holdings over the maintenance period in excess of the required reserves, computed on the basis of those credit institutions that have fulfilled the reserve requirement.*

5) *Average shortfalls of actual reserve holdings from required reserves over the maintenance period, computed on the basis of those credit institutions that have not fulfilled the reserve requirement.*

6) *This rate equals the average, over the maintenance period, of the ECB's rate (weighted according to the number of calendar days) on the Eurosystem's main refinancing operations (see Table 1.3).*

2 Monetary and financial developments in the euro area

Table 2.1

Aggregated balance sheet of the Eurosystem [1]

(EUR billions (not seasonally adjusted; end-of-period stocks))

1. Assets

		Loans to euro area residents				Holdings of securities other than shares issued by euro area residents				Holdings of shares/ other equity issued by euro area residents			External assets	Fixed assets	Remaining assets	**Total assets**
			MFIs	General govern- ment	Other euro area residents		MFIs	General govern- ment	Other euro area residents		MFIs	Other euro area residents				
		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1997	Sep.	245.1	222.6	21.8	0.6	115.8	0.9	113.7	1.2	2.9	0.5	2.4	278.9	7.1	44.7	694.5
	Oct.	250.7	228.2	21.8	0.6	114.0	0.8	112.0	1.2	2.9	0.5	2.4	278.3	7.2	43.1	696.1
	Nov.	242.1	219.7	21.8	0.6	113.9	0.8	111.7	1.5	2.9	0.5	2.4	280.3	7.2	53.9	700.2
	Dec.	254.3	232.5	21.1	0.6	114.3	0.8	112.1	1.4	2.9	0.5	2.4	288.9	7.0	52.1	719.5
1998	Jan.	238.1	216.5	21.2	0.4	111.9	1.0	109.5	1.5	2.9	0.5	2.5	291.0	7.2	41.1	692.3
	Feb.	261.0	239.2	21.2	0.7	108.3	1.0	105.9	1.5	2.9	0.6	2.4	291.4	7.3	42.3	713.3
	Mar.	246.7	225.3	21.2	0.2	106.7	2.3	103.1	1.2	3.0	0.6	2.5	290.3	7.5	39.4	693.5
	Apr.	241.0	219.4	21.2	0.4	102.5	2.5	99.2	0.8	3.0	0.6	2.5	294.9	7.6	43.8	692.8
	May	243.0	221.6	21.2	0.3	101.9	2.9	98.2	0.8	3.1	0.6	2.5	298.2	7.7	46.9	700.7
	June	325.4	304.1	21.1	0.2	105.4	6.6	98.0	0.8	3.3	0.8	2.5	288.4	7.8	47.9	778.2
	July	338.5	317.2	21.1	0.2	87.8	3.2	83.8	0.8	4.7	2.1	2.6	292.6	8.0	49.9	781.6
	Aug.	339.9	318.5	21.1	0.2	88.1	2.8	84.5	0.9	4.7	2.0	2.7	290.7	8.0	54.9	786.3
	Sep.	326.7	305.4	21.1	0.2	82.7	1.0	81.0	0.7	4.7	2.0	2.7	288.4	8.0	50.2	760.7
	Oct.	326.9	305.6	21.1	0.2	73.3	0.9	71.7	0.7	4.7	2.0	2.7	297.8	8.1	49.7	760.5
	Nov. (p)	322.5	301.0	21.1	0.4	78.0	1.0	76.3	0.6	4.7	2.0	2.7	304.9	8.1	51.5	769.7

2. Liabilities

		Currency in circulation	Deposits of euro area residents				Money market paper	Debt securities issued	Capital and reserves	External liabilities	Remaining liabilities	**Total liabilities**
				MFIs	Central government	Other general government/ other euro area residents						
		1	2	3	4	5	6	7	8	9	10	11
1997	Sep.	337.1	139.6	80.4	55.8	3.3	17.3	16.8	100.8	15.9	67.0	694.5
	Oct.	337.2	144.0	88.6	51.9	3.5	17.0	16.6	99.9	15.7	65.6	696.1
	Nov.	340.7	141.6	82.3	54.5	4.8	13.3	15.6	100.9	15.9	72.3	700.2
	Dec.	352.8	147.0	91.9	52.2	2.9	13.2	15.0	105.6	16.1	69.8	719.5
1998	Jan.	338.7	136.3	83.4	50.7	2.2	13.9	16.3	107.4	16.1	63.5	692.3
	Feb.	338.7	159.2	93.7	61.5	4.0	13.3	16.5	105.6	15.1	64.9	713.3
	Mar.	339.2	138.1	88.4	47.0	2.7	11.3	17.2	104.8	15.3	67.5	693.5
	Apr.	342.6	131.4	84.8	44.5	2.2	12.0	16.9	103.7	16.4	69.6	692.8
	May	344.9	142.0	90.9	47.1	4.0	13.1	15.3	103.5	15.9	66.1	700.7
	June	344.2	208.3	149.3	54.5	4.5	13.5	14.1	111.6	20.8	65.6	778.2
	July	349.2	200.1	132.8	64.2	3.0	13.9	14.3	110.3	24.0	69.9	781.6
	Aug.	343.4	209.0	135.5	69.9	3.5	12.4	13.5	110.2	21.6	76.2	786.3
	Sep.	340.2	196.1	124.4	67.2	4.5	11.2	12.8	106.4	23.2	70.8	760.7
	Oct.	341.1	198.2	129.2	64.8	4.3	11.7	11.8	106.6	22.6	68.4	760.5
	Nov. (p)	342.8	210.6	147.3	56.9	6.4	12.5	11.6	103.3	20.0	68.9	769.7

Source: ECB.

1) The ECB was established on 1 June 1998. The data shown for the Eurosystem relate to the ECB (as from June 1998) and the national central banks of Member States in the euro area.

Table 2.2

Aggregated balance sheet of the other euro area MFIs (excluding the Eurosystem)

(EUR billions (not seasonally adjusted; end-of-period stocks))

1. Assets

		Loans to euro area residents	MFIs	General government	Other euro area residents	Holdings of securities other than shares issued by euro area residents	MFIs	General government	Other euro area residents	Money market paper	Holdings of shares/ other equity issued by euro area residents	MFIs	Other euro area residents	External assets	Fixed assets	Remaining assets	**Total assets**
		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
1997	Sep.	8,132.5	2,730.0	813.4	4,589.1	1,879.1	625.7	1,067.2	186.2	102.0	307.0	90.5	216.5	1,571.8	234.8	751.1	12,978.4
	Oct.	8,199.6	2,766.6	817.9	4,615.2	1,882.1	630.2	1,066.4	185.6	102.9	311.8	91.7	220.1	1,578.7	237.7	764.5	13,077.3
	Nov.	8,297.8	2,826.4	830.1	4,641.3	1,894.0	634.4	1,071.7	187.9	100.7	316.6	92.5	224.1	1,633.3	240.2	797.5	13,280.1
	Dec.	8,426.6	2,899.3	820.7	4,706.5	1,856.5	628.5	1,048.6	179.4	95.6	329.8	94.2	235.6	1,617.1	235.1	765.3	13,325.9
1998	Jan.	8,475.5	2,950.5	806.5	4,718.5	1,900.2	641.4	1,072.7	186.1	101.0	351.1	102.2	248.9	1,631.7	232.4	801.8	13,493.7
	Feb.	8,513.9	2,967.7	805.6	4,740.6	1,921.1	644.9	1,084.9	191.2	102.5	363.6	104.6	259.0	1,656.0	232.7	807.5	13,597.3
	Mar.	8,552.8	2,973.9	804.8	4,774.1	1,946.4	648.1	1,102.7	195.7	101.2	384.4	108.9	275.4	1,693.7	234.2	785.6	13,698.2
	Apr.	8,593.8	2,980.4	807.9	4,805.6	1,967.1	657.7	1,113.5	195.9	102.2	396.0	112.1	284.0	1,665.6	234.3	803.4	13,762.5
	May	8,602.8	2,982.8	799.2	4,820.8	1,988.6	664.4	1,125.0	199.2	102.7	403.9	114.4	289.5	1,656.3	243.1	817.9	13,815.2
	June	8,736.7	3,056.9	805.5	4,874.4	1,992.6	673.5	1,126.8	192.3	101.5	401.5	115.2	286.4	1,691.8	240.1	824.6	13,988.7
	July	8,714.1	2,994.7	801.8	4,917.6	2,007.1	687.6	1,124.7	194.8	101.7	393.2	115.1	278.0	1,650.4	235.0	814.5	13,916.0
	Aug.	8,737.1	3,019.1	803.9	4,914.1	2,026.4	698.8	1,132.3	195.3	100.5	387.6	116.1	271.5	1,650.7	236.1	761.7	13,899.9
	Sep.	8,807.5	3,039.6	806.4	4,961.5	2,027.9	702.3	1,131.2	194.5	99.9	381.4	107.9	273.5	1,641.6	236.9	780.9	13,976.1
	Oct.	8,925.8	3,119.6	813.5	4,992.7	2,051.7	704.9	1,148.1	198.7	99.6	387.0	112.3	274.7	1,635.4	238.8	792.5	14,130.7
	Nov. (p)	9,057.4	3,201.3	818.4	5,037.7	2,069.0	722.5	1,152.0	194.5	109.4	400.3	115.0	285.3	1,697.0	241.2	750.1	14,324.5

2. Liabilities

		Currency in circulation	Deposits of euro area residents	MFIs	Central government	Other general government/ other euro area residents	Overnight	With agreed maturity	Redeemable at notice	Repurchase agreements	Money market fund shares/ units	Debt securities issued	Money market paper	Capital and reserves	External liabilities	Remaining liabilities	**Total liabilities**
		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
1997	Sep.	0.4	7,467.0	2,843.8	96.0	4,527.2	1,137.1	1,895.4	1,287.4	207.3	226.9	1,906.8	143.6	677.1	1,331.2	1,225.4	12,978.4
	Oct.	0.4	7,533.1	2,894.1	99.9	4,539.1	1,139.3	1,904.2	1,288.5	207.2	222.1	1,913.2	146.6	675.5	1,344.1	1,242.3	13,077.3
	Nov.	0.4	7,627.8	2,966.5	88.9	4,572.3	1,165.4	1,899.3	1,291.8	215.8	224.4	1,923.9	145.6	677.7	1,393.2	1,287.2	13,280.1
	Dec.	0.4	7,749.7	2,992.3	102.4	4,655.0	1,224.3	1,897.0	1,328.4	205.3	215.3	1,925.1	138.8	687.5	1,391.3	1,217.8	13,325.9
1998	Jan.	0.4	7,777.9	3,029.6	95.6	4,652.7	1,178.0	1,915.3	1,341.9	217.5	220.2	1,944.5	145.2	690.8	1,434.5	1,280.1	13,493.7
	Feb.	0.4	7,825.4	3,066.3	98.4	4,660.7	1,179.8	1,919.4	1,345.2	216.3	221.3	1,967.8	147.2	696.0	1,468.7	1,270.5	13,597.3
	Mar.	0.4	7,832.1	3,076.9	92.8	4,662.4	1,208.8	1,894.8	1,346.5	212.3	221.2	1,985.1	149.5	710.3	1,520.0	1,279.5	13,698.2
	Apr.	0.4	7,862.6	3,079.7	97.2	4,685.7	1,223.2	1,909.9	1,346.1	206.6	223.9	1,999.4	156.3	702.6	1,491.3	1,325.9	13,762.5
	May	0.4	7,885.7	3,092.8	88.2	4,704.8	1,240.0	1,908.6	1,348.0	208.2	226.4	2,012.1	150.9	712.2	1,483.8	1,343.6	13,815.2
	June	0.4	7,989.6	3,167.2	94.4	4,728.0	1,287.7	1,889.6	1,347.1	203.6	225.0	2,042.4	145.9	718.9	1,494.2	1,372.3	13,988.7
	July	0.4	7,946.0	3,147.5	92.2	4,706.3	1,248.5	1,894.8	1,346.8	216.2	225.3	2,062.9	152.8	720.3	1,470.1	1,338.1	13,916.0
	Aug.	0.4	7,973.3	3,175.7	95.5	4,702.1	1,239.2	1,905.7	1,348.7	208.5	228.1	2,072.4	152.9	719.8	1,469.6	1,283.5	13,899.9
	Sep.	0.4	8,010.0	3,210.9	96.4	4,702.7	1,264.0	1,883.6	1,347.0	208.2	224.9	2,073.9	153.2	718.3	1,481.1	1,314.2	13,976.1
	Oct.	0.4	8,097.2	3,281.0	96.2	4,720.1	1,268.3	1,884.7	1,350.4	216.7	223.8	2,074.9	160.2	720.2	1,523.3	1,330.8	14,130.7
	Nov. (p)	0.4	8,207.2	3,367.8	97.4	4,742.1	1,309.9	1,881.0	1,352.3	198.8	255.5	2,087.7	168.6	724.2	1,599.3	1,281.6	14,324.5

Source: ECB.

Table 2.3

Consolidated balance sheet of the euro area MFIs (including the Eurosystem [1])

(EUR billions (not seasonally adjusted; end-of-period stocks))

1. Assets

		Loans to euro area residents	General government	Other euro area residents	Holdings of securities other than shares issued by euro area residents	General government	Other euro area residents	Holdings of shares/other equity issued by other euro area residents	External assets	Fixed assets	Remaining assets	**Total assets**
		1	2	3	4	5	6	7	8	9	10	11
1997	Sep.	5,425.0	835.2	4,589.7	1,368.3	1,180.9	187.5	218.9	1,822.6	242.0	795.8	9,872.5
	Oct.	5,455.5	839.7	4,615.8	1,365.1	1,178.3	186.8	222.5	1,829.2	244.9	807.5	9,924.7
	Nov.	5,493.8	851.9	4,641.9	1,372.8	1,183.4	189.4	226.5	1,885.4	247.3	851.4	10,077.2
	Dec.	5,549.0	841.9	4,707.1	1,341.5	1,160.7	180.8	238.0	1,871.2	242.1	817.4	10,059.2
1998	Jan.	5,546.6	827.6	4,719.0	1,369.7	1,182.2	187.5	251.4	1,893.8	239.6	842.8	10,143.9
	Feb.	5,568.0	826.7	4,741.3	1,383.5	1,190.8	192.7	261.4	1,918.8	240.0	849.8	10,221.6
	Mar.	5,600.3	826.0	4,774.3	1,402.6	1,205.7	196.9	277.9	1,954.8	241.7	825.0	10,302.3
	Apr.	5,635.0	829.0	4,806.0	1,409.4	1,212.7	196.7	286.4	1,931.1	241.9	847.1	10,350.9
	May	5,641.4	820.4	4,821.0	1,423.2	1,223.3	199.9	292.0	1,925.2	250.8	864.7	10,397.3
	June	5,701.1	826.5	4,874.6	1,417.9	1,224.8	193.0	288.9	1,949.8	247.9	872.5	10,478.0
	July	5,740.7	822.8	4,917.9	1,404.1	1,208.5	195.6	280.7	1,912.9	243.0	864.4	10,445.8
	Aug.	5,739.3	825.0	4,914.3	1,412.9	1,216.8	196.1	274.2	1,911.2	244.1	816.6	10,398.3
	Sep.	5,789.2	827.5	4,961.7	1,407.3	1,212.1	195.1	276.2	1,900.0	244.9	831.1	10,448.7
	Oct.	5,827.5	834.6	4,992.9	1,419.1	1,219.8	199.4	277.4	1,903.9	246.8	842.1	10,516.9
	Nov. (p)	5,877.6	839.5	5,038.1	1,423.5	1,228.3	195.2	288.0	1,972.1	249.3	801.4	10,611.9

2. Liabilities

		Currency in circulation	Deposits of central government	Deposits of other general government/other euro area residents	Overnight	With agreed maturity	Redeemable at notice	Repurchase agreements	Money market fund shares/units and money market paper	Debt securities issued	Capital and reserves	External liabilities	Remaining liabilities	Excess of inter-MFI liabilities	**Total liabilities**
		1	2	3	4	5	6	7	8	9	10	11	12	13	14
1997	Sep.	309.3	151.8	4,530.5	1,140.3	1,895.4	1,287.4	207.4	285.8	1,297.1	687.0	1,347.1	1,292.4	-28.4	9,872.5
	Oct.	309.8	151.8	4,542.6	1,142.6	1,904.3	1,288.5	207.2	282.8	1,298.9	683.3	1,359.8	1,307.9	-12.2	9,924.7
	Nov.	312.9	143.4	4,577.1	1,170.0	1,899.5	1,291.8	215.8	282.5	1,304.3	685.6	1,409.0	1,359.5	2.9	10,077.2
	Dec.	318.4	154.7	4,657.9	1,227.3	1,897.0	1,328.4	205.3	271.7	1,310.8	698.4	1,407.4	1,287.6	-47.7	10,059.2
1998	Jan.	310.2	146.3	4,654.9	1,180.2	1,915.3	1,341.9	217.5	278.2	1,318.4	695.6	1,450.6	1,343.6	-53.9	10,143.9
	Feb.	310.5	160.0	4,664.7	1,183.7	1,919.4	1,345.2	216.3	279.3	1,338.4	696.5	1,483.8	1,335.4	-47.0	10,221.6
	Mar.	310.6	139.8	4,665.1	1,211.5	1,894.8	1,346.5	212.3	280.8	1,351.9	705.6	1,535.3	1,347.0	-33.8	10,302.3
	Apr.	313.6	141.7	4,687.9	1,225.4	1,909.9	1,346.1	206.6	290.0	1,356.0	693.7	1,507.7	1,395.6	-35.3	10,350.9
	May	315.9	135.3	4,708.8	1,244.0	1,908.6	1,348.0	208.2	287.7	1,360.2	700.7	1,499.7	1,409.7	-20.7	10,397.3
	June	314.2	148.9	4,732.5	1,292.2	1,889.6	1,347.1	203.6	283.0	1,376.4	714.5	1,515.0	1,437.9	-44.5	10,478.0
	July	319.4	156.4	4,709.3	1,251.5	1,894.8	1,346.8	216.2	290.2	1,386.4	713.4	1,494.1	1,408.0	-31.5	10,445.8
	Aug.	313.7	165.4	4,705.6	1,242.7	1,905.7	1,348.7	208.5	292.9	1,384.3	711.9	1,491.2	1,359.7	-26.3	10,398.3
	Sep.	310.6	163.6	4,707.3	1,268.5	1,883.6	1,347.0	208.2	289.4	1,383.4	714.8	1,504.3	1,385.0	-9.7	10,448.7
	Oct.	312.1	160.9	4,724.4	1,272.5	1,884.7	1,350.4	216.7	296.2	1,380.9	712.5	1,545.9	1,399.0	-15.1	10,516.9
	Nov. (p)	313.4	154.3	4,748.4	1,316.2	1,881.0	1,352.3	198.9	327.2	1,375.7	710.4	1,619.4	1,350.4	12.7	10,611.9

Source: ECB.

1) *The ECB was established on 1 June 1998. The data shown for the Eurosystem relate to the ECB (as from June 1998) and the national central banks of Member States in the euro area.*

Table 2.4

Monetary aggregates [1]

(EUR billions (not seasonally adjusted; end-of-period stocks) and annual percentage changes)

		M2								Repurchase agreements	Money market fund shares/units and money market paper	Debt securities up to 2 years
		M1				Deposits with agreed maturity up to 2 years	Deposits redeemable at notice up to 3 months	Total	Annual percentage change [2]			
		Currency in circulation	Overnight deposits	Total	Annual percentage change [2]							
		1	2	3	4	5	6	7	8	9	10	11
1997	Sep.	309.3	1,204.8	1,514.1	8.7	898.7	1,121.9	3,534.7	3.9	207.4	285.8	70.4
	Oct.	309.8	1,208.7	1,518.5	9.3	905.1	1,123.8	3,547.4	4.2	207.2	282.8	72.1
	Nov.	312.9	1,238.6	1,551.5	8.3	899.5	1,127.4	3,578.4	3.9	215.8	282.5	69.5
	Dec.	318.4	1,296.8	1,615.2	6.5	890.3	1,161.7	3,667.2	3.1	205.3	271.7	73.3
1998	Jan.	310.2	1,251.3	1,561.5	8.3	902.4	1,177.6	3,641.5	3.8	217.5	278.2	74.5
	Feb.	310.5	1,251.8	1,562.4	8.7	898.4	1,181.7	3,642.4	4.0	216.3	279.3	79.3
	Mar.	310.6	1,281.4	1,592.0	9.3	872.5	1,183.5	3,648.0	4.1	212.3	280.8	85.5
	Apr.	313.6	1,293.4	1,607.0	10.7	886.3	1,185.3	3,678.5	4.8	206.6	290.0	86.0
	May	315.9	1,310.4	1,626.3	10.5	882.6	1,189.3	3,698.3	4.9	208.2	287.7	89.1
	June	314.2	1,359.3	1,673.5	10.0	863.8	1,189.6	3,726.8	4.9	203.6	283.0	88.7
	July	319.4	1,319.0	1,638.4	8.5	866.8	1,190.4	3,695.6	4.2	216.2	290.2	94.1
	Aug.	313.7	1,309.7	1,623.4	8.6	873.4	1,193.5	3,690.3	4.2	208.5	292.9	88.9
	Sep.	310.6	1,334.1	1,644.7	8.6	861.5	1,192.6	3,698.7	4.6	208.2	289.4	85.3
	Oct.	312.1	1,337.9	1,650.0	8.7	865.9	1,196.3	3,712.2	4.6	216.7	296.2	89.1
	Nov. (p)	313.4	1,381.2	1,694.6	9.2	865.2	1,198.0	3,757.8	5.0	198.9	327.2	80.4

Source: ECB.

1) *Monetary aggregates comprise monetary liabilities of MFIs and central government (Post Office, Treasury) vis-à-vis non-MFI euro area residents, excluding central government.*

2) *Calculated in this issue from amounts outstanding adjusted for incomplete coverage of the data before September 1997. In the near future, the difference in levels will be adjusted for reclassifications, other revaluations and any other changes which do not arise from transactions.*

3) *The growth rate of M3 for November 1998 has been adjusted to reflect the fact that at present data on money market funds in one Member State are available only for that month.*

M3			Memo: Non-monetary liabilities of MFIs							
Total	Annual percentage change 2) 3)	3-month moving average (centered)	Deposits	With agreed maturity over 2 years	Redeemable at notice over 3 months	Debt securities over 2 years	Capital and reserves	Total		
12	13	14	15	16	17	18	19	20		
4,098.3	4.0	4.1	1,214.0	997.3	216.6	1,226.7	687.0	3,127.6	1997	Sep.
4,109.6	4.2	4.2	1,215.8	999.8	216.0	1,226.7	683.3	3,125.8		Oct.
4,146.2	4.3	4.1	1,216.6	1,000.5	216.1	1,234.8	685.6	3,137.1		Nov.
4,217.5	3.9	4.2	1,227.0	1,007.3	219.8	1,237.5	698.4	3,162.9		Dec.
4,211.6	4.4	4.3	1,231.3	1,013.6	217.7	1,244.0	695.6	3,170.9	1998	Jan.
4,217.4	4.3	4.4	1,239.2	1,021.7	217.5	1,259.1	696.5	3,194.7		Feb.
4,226.6	4.4	4.5	1,239.7	1,022.9	216.8	1,266.4	705.6	3,211.7		Mar.
4,261.2	4.9	4.6	1,239.0	1,024.3	214.7	1,270.0	693.7	3,202.8		Apr.
4,283.3	4.6	4.7	1,239.5	1,026.5	213.0	1,271.0	700.7	3,211.3		May
4,302.1	4.7	4.6	1,238.5	1,026.5	212.0	1,287.7	714.5	3,240.7		June
4,296.1	4.4	4.5	1,239.2	1,028.4	210.8	1,292.3	713.4	3,244.9		July
4,280.7	4.2	4.4	1,242.7	1,032.8	209.9	1,295.3	711.9	3,249.9		Aug.
4,281.6	4.5	4.6	1,231.9	1,022.6	209.3	1,298.1	714.8	3,244.9		Sep.
4,314.2	5.0	4.7	1,228.4	1,019.3	209.1	1,291.8	712.5	3,232.6		Oct.
4,364.3	4.5	.	1,225.7	1,016.2	209.5	1,295.3	710.4	3,231.4	(p)	Nov.

Table 2.5

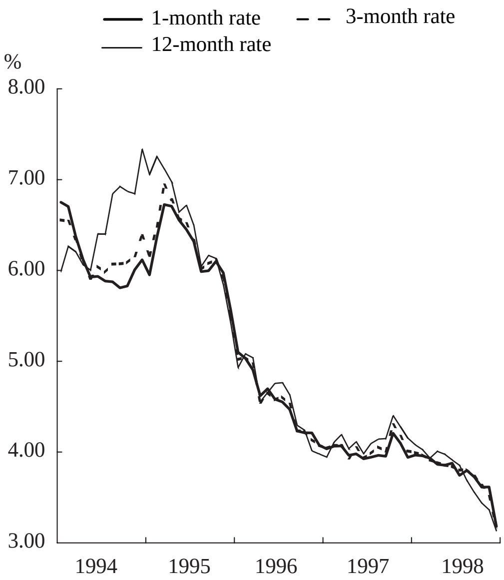
Money market interest rates[1]

(percentages per annum; end of period)

		Euro area [2]					United States	Japan
		Overnight deposits	1-month deposits	3-month deposits	6-month deposits	12-month deposits	3-month deposits	3-month deposits
		1	2	3	4	5	6	7
1994		5.24	6.12	6.38	6.83	7.34	6.37	2.34
1995		5.62	5.57	5.49	5.62	5.42	5.44	0.50
1996		4.04	4.08	4.08	4.06	3.98	5.43	0.31
1997		3.98	3.94	4.01	4.05	4.15	5.62	0.36
1998		3.09	3.18	3.17	3.14	3.13	5.00	0.18
1997	Dec.	3.98	3.94	4.01	4.05	4.15	5.62	0.36
1998	Jan.	3.89	3.97	4.00	4.08	4.08	5.50	0.41
	Feb.	4.22	3.96	3.97	3.98	4.02	5.55	0.48
	Mar.	3.83	3.93	3.92	3.89	3.93	5.59	0.50
	Apr.	3.76	3.86	3.89	3.93	4.01	5.60	0.45
	May	3.79	3.85	3.86	3.89	3.98	5.59	0.37
	June	3.76	3.88	3.84	3.85	3.91	5.59	0.43
	July	3.77	3.74	3.80	3.82	3.85	5.56	0.34
	Aug.	3.78	3.80	3.81	3.72	3.69	5.50	0.37
	Sep.	3.81	3.73	3.73	3.64	3.55	5.20	0.12
	Oct.	3.66	3.61	3.63	3.53	3.44	5.12	0.68
	Nov.	3.40	3.62	3.51	3.43	3.36	5.12	0.68
	Dec.	3.09	3.18	3.17	3.14	3.13	5.00	0.18
	4 Dec.	3.10	3.33	3.29	3.22	3.14	5.09	0.20
	11	3.13	3.32	3.23	3.14	3.16	5.14	0.12
	18	2.93	3.27	3.21	3.13	3.14	5.56	0.56
	25	2.81	3.27	3.14	3.19	3.06	5.18	0.28
1999	1 Jan.	3.09	3.18	3.17	3.14	3.13	5.00	0.18

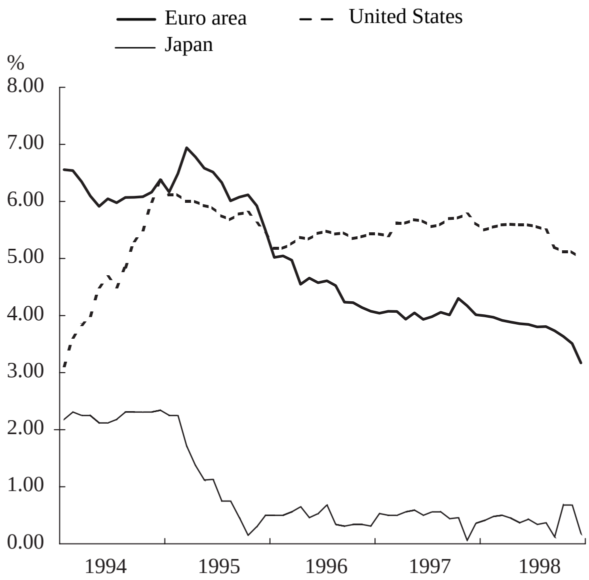
Euro area money market rates

(1, 3 and 12-month rates)



3-month money market rates

(euro area, United States and Japan)



Sources: Reuters and ECB.
1) *Interbank deposit bid rates.*
2) *Prior to 4 January 1999, synthetic euro area rates were calculated on the basis of national rates weighted by GDP.*

Table 2.6

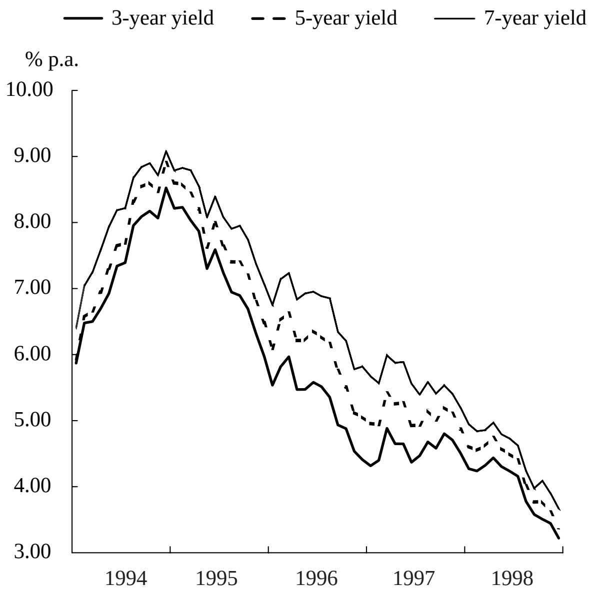
Government bond yields [1)]

(percentages per annum)

	Euro area [2)] 2 years	3 years	5 years	7 years	10 years	United States 10 years	Japan 10 years
	1	2	3	4	5	6	7
1994	8.08	8.52	8.91	9.08	8.18	7.21	4.24
1995	5.69	5.97	6.48	7.06	8.73	6.69	3.32
1996	4.17	4.41	5.06	5.82	7.23	6.54	3.03
1997	4.33	4.51	4.87	5.20	5.99	6.45	2.15
1998	3.16	3.22	3.38	3.67	4.71	5.33	1.30
1997 Dec.	4.33	4.51	4.87	5.20	5.46	5.89	1.65
1998 Jan.	4.11	4.27	4.61	4.95	5.22	5.63	1.69
Feb.	4.08	4.24	4.55	4.84	5.12	5.65	1.71
Mar.	4.17	4.32	4.61	4.86	5.01	5.73	1.56
Apr.	4.26	4.44	4.75	4.97	5.00	5.72	1.57
May	4.13	4.30	4.58	4.79	5.06	5.73	1.30
June	4.08	4.24	4.50	4.73	4.91	5.58	1.22
July	4.04	4.16	4.41	4.62	4.82	5.53	1.36
Aug.	3.68	3.78	4.01	4.24	4.59	5.41	1.17
Sep.	3.55	3.58	3.77	3.98	4.27	4.87	0.88
Oct.	3.39	3.51	3.77	4.09	4.25	4.58	0.82
Nov.	3.33	3.44	3.62	3.90	4.24	4.89	0.89
Dec.	3.16	3.22	3.38	3.67	3.95	4.69	1.39
4 Dec.	3.25	3.31	3.50	3.76	4.00	4.67	1.06
11	3.18	3.23	3.39	3.62	3.86	4.66	1.17
18	3.20	3.15	3.35	3.63	3.90	4.63	1.32
25	3.20	3.23	3.39	3.67	3.98	4.92	1.77
1999 1 Jan.	3.16	3.22	3.38	3.67	3.94	4.70	2.02

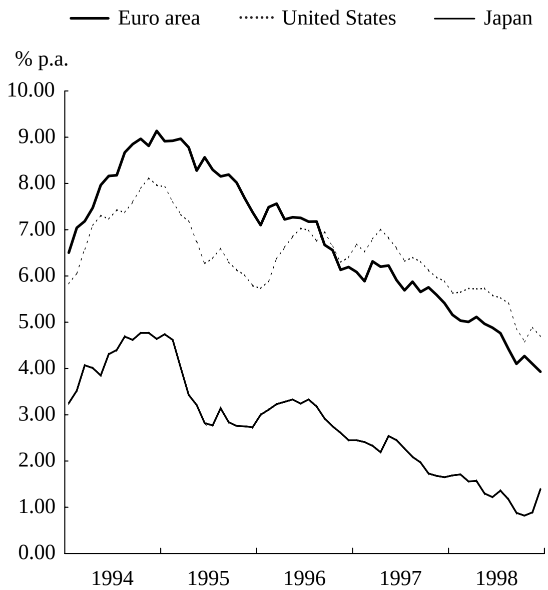
Euro area government bond yields

(3, 5 and 7-year yields)



10-year government bond yields

(euro area, United States and Japan)



Sources: Reuters, ECB, Federal Reserve and Bank of Japan.

1) 2, 3, 5 and 7-year euro area yields are end-of-period values; 10-year yields are period averages.

2) Euro area yields are calculated on the basis of harmonised national government bond yields weighted by GDP.

Table 2.7

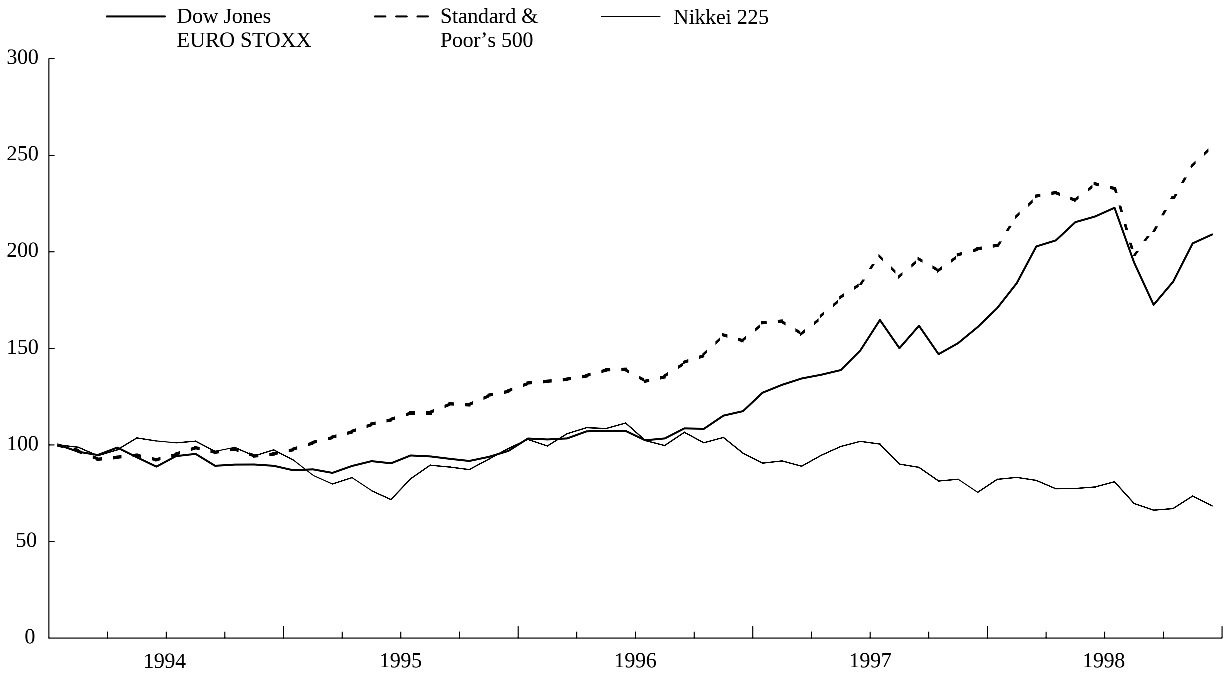
Stock market indices

(index levels in points; end of period)

		Dow Jones EURO STOXX indices											United States	Japan
		Benchmark		Main economic sectors										
		Broad	50	Basic materials	Consumer cyclical	Consumer non-cyclical	Energy	Financial	Conglom-erates	Industrial	Techno-logy	Utilities	Standard & Poor's 500	Nikkei 225
		1	2	3	4	5	6	7	8	9	10	11	12	13
1994		127.33	1,320.59	145.88	107.82	143.90	125.92	109.29	125.91	132.31	128.66	122.60	455.19	19,299.47
1995		138.37	1,506.82	137.78	111.06	181.13	145.46	117.66	133.05	136.18	145.57	152.09	614.57	19,417.95
1996		167.75	1,850.32	145.11	120.25	274.94	180.64	137.84	156.11	171.05	153.17	192.40	743.25	20,147.27
1997		229.86	2,531.99	166.33	159.82	324.06	249.22	188.87	210.33	204.75	248.37	225.11	962.37	15,917.07
1998		298.37	3,342.32	147.10	156.74	485.39	232.87	250.29	218.78	283.76	353.38	329.50	1,229.23	13,842.17
1997	Dec.	229.86	2,531.99	166.33	159.82	324.06	249.22	188.87	210.33	204.75	248.37	225.11	962.37	15,917.07
1998	Jan.	243.93	2,676.03	173.71	167.26	338.43	247.28	203.90	220.86	218.99	275.99	242.74	963.36	15,929.69
	Feb.	262.29	2,878.04	185.29	179.88	367.60	252.05	225.29	222.68	234.57	303.85	247.81	1,023.74	16,797.69
	Mar.	289.46	3,153.32	196.69	197.27	390.26	278.01	249.55	239.23	270.77	335.91	268.38	1,076.83	16,840.31
	Apr.	293.96	3,195.43	204.90	202.37	386.70	270.47	266.59	238.17	276.74	354.64	275.98	1,112.20	15,941.29
	May	307.44	3,357.77	211.08	207.22	401.14	280.40	276.07	248.87	302.71	378.82	285.79	1,108.42	15,514.28
	June	311.58	3,406.82	198.55	204.62	430.65	275.47	270.69	244.59	299.67	387.80	294.99	1,108.39	15,231.29
	July	318.06	3,480.63	182.52	195.81	436.13	255.90	291.41	226.39	301.26	417.31	305.08	1,156.58	16,370.17
	Aug.	277.73	3,050.59	151.13	167.11	413.58	217.55	240.10	194.28	262.30	360.33	279.30	1,074.62	15,243.98
	Sep.	246.31	2,670.97	131.62	137.37	379.55	230.22	187.86	182.29	240.51	279.90	277.86	1,020.64	14,140.69
	Oct.	263.49	2,887.11	138.21	147.48	419.19	223.71	206.17	197.45	250.98	300.39	295.80	1,098.67	13,564.51
	Nov.	291.73	3,232.44	147.95	153.01	442.91	237.51	236.66	208.39	270.40	339.22	306.30	1,176.46	14,883.70
	Dec.	298.37	3,342.32	147.10	156.74	485.39	232.87	250.29	218.78	283.76	353.38	329.50	1,229.23	13,842.17
	4 Dec.	278.59	3,048.73	143.19	148.42	435.12	220.10	224.89	199.48	266.43	335.76	300.50	1,150.14	14,639.97
	11	273.85	3,044.56	141.25	143.08	446.41	218.90	227.98	197.59	261.65	321.45	301.58	1,165.02	14,405.64
	18	279.91	3,134.19	141.16	146.19	462.56	222.79	235.00	197.42	275.32	331.46	312.63	1,179.98	14,194.29
	25	294.21	3,301.32	147.53	151.85	477.04	231.32	244.25	208.97	282.58	350.20	320.76	1,226.27	13,797.95
1999	1 Jan.	298.37	3,342.32	147.10	156.74	485.39	232.87	250.29	218.78	283.76	353.38	329.50	1,229.23	13,842.17

Dow Jones EURO STOXX Broad, Standard & Poor's 500 and Nikkei 225 re-based

(base month: January 1994 = 100)



Source: Reuters.

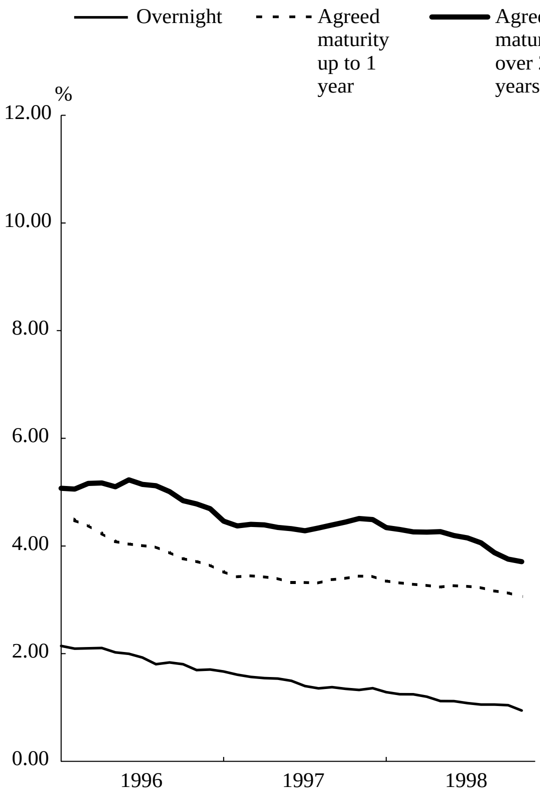
Table 2.8

Retail bank interest rates

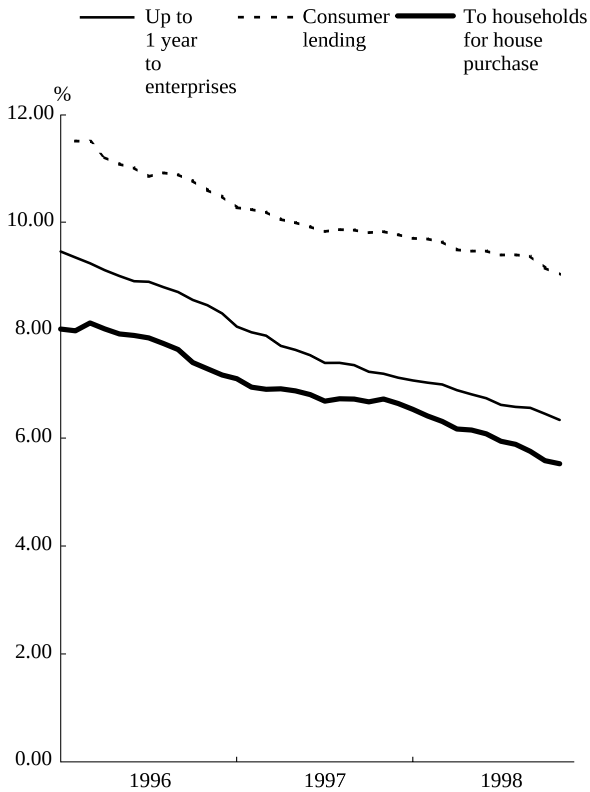
(percentages per annum; lending interest rates are provisional)

		Deposit interest rates						Lending interest rates			
		Overnight	With agreed maturity			Redeemable at notice		To enterprises		To households	
			Up to 1 year	Up to 2 years	Over 2 years	Up to 3 months	Over 3 months	Up to 1 year	Over 1 year	Consumer lending	For house purchase
		1	2	3	4	5	6	7	8	9	10
1996		1.94	4.07	4.68	5.03	3.01	3.16	8.90	.	11.03	7.76
1997		1.47	3.40	3.62	4.40	2.80	3.09	7.54	6.69	9.97	6.81
1997	Nov.	1.33	3.44	3.54	4.51	2.79	3.33	7.19	6.60	9.83	6.72
	Dec.	1.36	3.44	3.52	4.49	2.79	3.39	7.12	6.42	9.77	6.64
1998	Jan.	1.29	3.35	3.40	4.34	2.77	3.35	7.07	6.36	9.70	6.53
	Feb.	1.25	3.32	3.35	4.31	2.78	3.30	7.03	6.30	9.69	6.41
	Mar.	1.25	3.29	3.32	4.26	2.75	3.32	6.99	6.19	9.63	6.31
	Apr.	1.20	3.27	3.30	4.26	2.74	3.30	6.89	6.12	9.49	6.17
	May	1.12	3.24	3.25	4.27	2.73	3.33	6.81	6.09	9.46	6.15
	June	1.12	3.26	3.27	4.19	2.61	3.34	6.74	6.04	9.47	6.08
	July	1.08	3.25	3.26	4.15	2.58	3.29	6.61	6.00	9.39	5.94
	Aug.	1.05	3.23	3.23	4.06	2.56	3.30	6.58	5.91	9.40	5.88
	Sep.	1.05	3.17	3.17	3.88	2.54	3.21	6.56	5.78	9.37	5.75
	Oct.	1.04	3.13	3.13	3.76	2.52	3.14	6.45	5.65	9.15	5.58
	Nov.	0.94	3.06	3.06	3.71	2.52	3.12	6.34	5.57	9.03	5.52

Deposit interest rates



Lending interest rates



Source: ECB.
These euro area retail bank interest rates should be used with caution and for statistical purposes only, primarily for analysing their development over time rather than their level. They are calculated as the weighted average of national interest rates provided by the national central banks. The national rates represent those rates that are currently available from national sources and which are judged to fit the standard categories. These national rates have been aggregated to derive information for the euro area, in some cases relying on proxies and working assumptions due to the heterogeneity observed in the national financial instruments across MU Member States. Furthermore, the national interest rates are not harmonised in terms of their coverage (new business and/or outstanding amounts), the nature of the data (nominal or effective) or the compilation method. The country weights for the euro area retail bank interest rates are derived from the monthly MFI balance sheet statistics or close proxies. The weights reflect the country-specific proportions of the relevant instruments within the euro area, measured as outstanding amounts. The weights are adjusted monthly, so that interest rates and weights always refer to the same month.

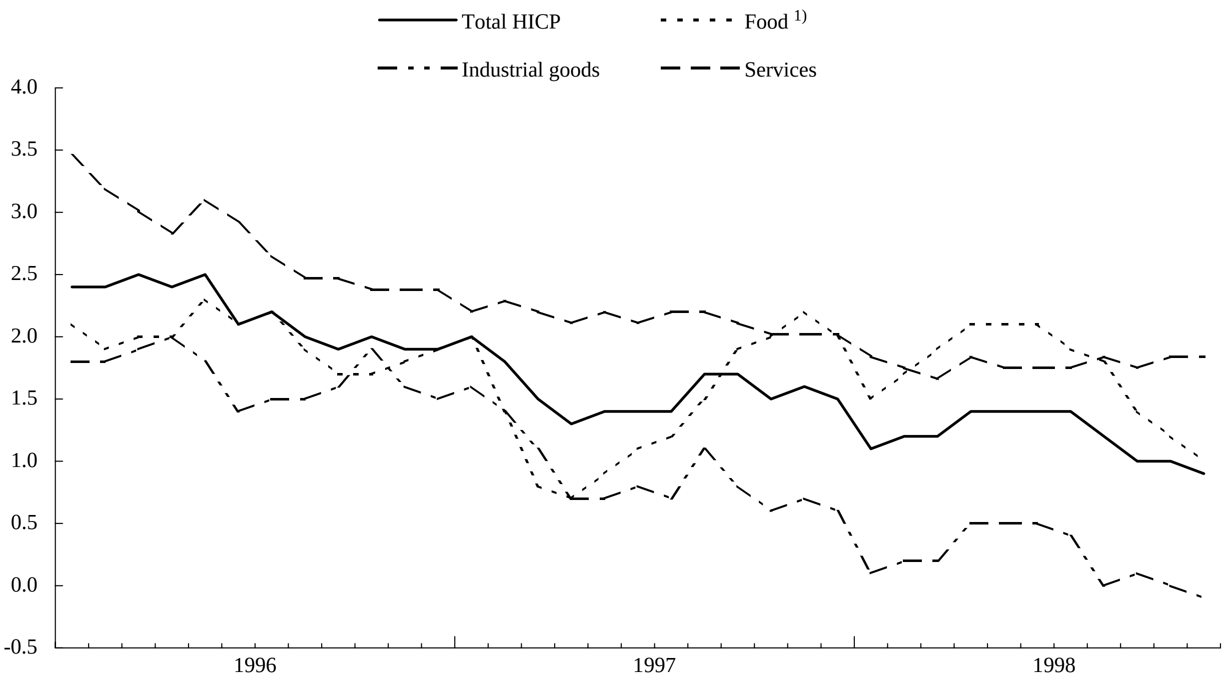
4 HICP and other prices in the euro area

Table 4.1

Harmonised Index of Consumer Prices

(annual percentage changes, unless otherwise indicated)

		Total 1996 = 100	Total	Goods	Food [1]	Processed food [1]	Unprocessed food	Industrial goods	Non-energy industrial goods	Energy	Services
Weight in the total (%) [2]		100.0	100.0	65.4	22.9	13.5	9.4	42.5	33.7	8.8	34.6
		1	2	3	4	5	6	7	8	9	10
1995		97.9	-	-	-	-	-	-	-	-	-
1996 [3]		100.0	2.2	1.8	2.0	2.0	1.9	1.7	1.5	2.4	3.1
1997		101.6	1.6	1.1	1.5	1.5	1.5	0.9	0.5	2.6	2.4
1997	Q2	101.4	1.4	0.8	0.9	1.4	0.3	0.7	0.4	2.0	2.4
	Q3	101.8	1.6	1.1	1.5	1.5	1.5	0.9	0.3	3.0	2.5
	Q4	102.0	1.5	1.1	2.1	1.5	2.9	0.6	0.5	1.0	2.3
1998	Q1	102.2	1.2	0.7	1.7	1.3	2.3	0.2	0.6	-1.5	2.0
	Q2	102.8	1.4	1.1	2.1	1.6	2.9	0.5	1.0	-1.3	2.0
	Q3	103.0	1.2	0.7	1.7	1.5	2.1	0.2	1.1	-3.2	2.0
1997	Nov.	102.0	1.6	1.2	2.2	1.5	3.2	0.7	0.6	1.2	2.3
	Dec.	102.1	1.5	1.1	2.0	1.3	2.9	0.6	0.6	0.5	2.3
1998	Jan.	102.0	1.1	0.6	1.5	1.3	1.8	0.1	0.5	-1.4	2.1
	Feb.	102.3	1.2	0.7	1.7	1.3	2.2	0.2	0.6	-1.4	2.0
	Mar.	102.4	1.2	0.8	1.9	1.4	2.7	0.2	0.7	-1.7	1.9
	Apr.	102.6	1.4	1.1	2.1	1.4	3.1	0.5	0.9	-0.9	2.1
	May	102.9	1.4	1.1	2.1	1.7	2.7	0.5	1.0	-1.4	2.0
	June	102.9	1.4	1.1	2.1	1.6	2.8	0.5	1.0	-1.6	2.0
	July	103.0	1.4	0.9	1.9	1.6	2.4	0.4	1.0	-1.9	2.0
	Aug.	103.0	1.2	0.7	1.8	1.5	2.3	0.0	1.1	-3.8	2.1
	Sep.	102.9	1.0	0.5	1.4	1.3	1.5	0.1	1.1	-3.8	2.0
	Oct.	102.9	1.0	0.4	1.2	1.3	1.0	0.0	1.0	-4.0	2.1
	Nov.	102.9	0.9	0.3	1.0	1.3	0.6	-0.1	1.0	-4.3	2.1



Source: Eurostat.
1) Including alcoholic beverages and tobacco.
2) Referring to index period 1998.
3) Annual percentage changes in 1996 include France for the overall index, but do not cover France for all components of the HICP.

Table 4.2

Selected other price and cost indicators

(annual percentage changes, unless otherwise indicated)

1. Industry and commodity prices

		Industrial producer prices									World market prices of raw materials (ECU)	
		Total industry excluding con-struction 1995 = 100	Total industry excluding con-struction	Manu-facturing	Inter-mediate goods	Capital goods	Consumer goods	Durable consumer goods	Non-durable consumer goods	Con-struction [1]	Total	Total excluding energy
		1	2	3	4	5	6	7	8	9	10	11
1995		100.0	3.7	3.9	5.2	1.8	2.1	1.4	2.5	.	0.2	2.1
1996		100.7	0.7	1.0	-0.6	1.3	1.7	1.3	1.8	1.2	6.5	-6.9
1997		101.7	1.1	0.6	1.1	0.2	1.0	0.2	1.4	1.4	10.0	13.0
1998		.	.	.	.	.	.	.	.	.	-21.2	-12.5
1997	Q3	102.0	1.4	1.0	1.9	0.0	0.9	-0.2	1.4	1.7	12.3	19.7
	Q4	102.1	1.1	1.0	1.1	0.3	1.3	0.1	1.8	1.4	1.8	14.1
1998	Q1	101.7	0.5	0.6	-0.1	0.3	1.0	-0.2	1.6	0.4	-13.8	-0.1
	Q2	101.3	-0.2	0.0	-0.9	0.3	.	.	1.0	0.2	-16.6	-10.7
	Q3	100.7	-1.3	-1.0	-2.6	0.5	.	.	0.3	.	-24.3	-18.1
	Q4	.	.	.	.	.	.	.	.	.	-30.0	-20.5
1997	Dec.	102.0	1.0	1.0	0.7	0.3	1.3	0.1	1.8	-	-3.7	12.3
1998	Jan.	101.9	0.6	0.8	0.1	0.3	1.2	-0.2	1.8	-	-12.7	5.4
	Feb.	101.8	0.5	0.6	-0.1	0.2	1.0	-0.3	1.6	-	-12.8	-0.5
	Mar.	101.6	0.3	0.5	-0.3	0.3	0.9	-0.2	1.4	-	-15.9	-4.8
	Apr.	101.5	0.1	0.4	-0.4	0.2	0.8	-0.2	1.2	-	-12.2	-6.0
	May	101.3	-0.2	-0.1	-0.9	0.3	0.6	0.0	0.8	-	-18.6	-12.8
	June	101.1	-0.5	-0.3	-1.3	0.3	.	.	0.8	-	-18.9	-13.3
	July	100.9	-0.8	-0.6	-1.9	0.5	.	.	0.6	-	-21.1	-14.4
	Aug.	100.7	-1.4	-1.2	-2.8	0.5	.	.	0.3	-	-26.3	-19.0
	Sep.	100.5	-1.6	-1.4	-2.9	0.4	.	.	-0.1	-	-25.4	-20.9
	Oct.	100.3	-1.9	-1.7	-3.5	0.4	.	.	-0.3	-	-30.6	-23.6
	Nov.	.	.	.	.	.	.	.	.	-	-28.6	-18.4
	Dec.	.	.	.	.	.	.	.	.	-	-30.8	-19.5

2. Deflators of gross domestic product and indicators of labour costs

		Deflators of GDP (s.a.)					Unit labour costs in whole economy	Compensation per employee in whole economy	Earnings per employee in manufacturing
		GDP 1995 = 100	GDP	Private consumption	Government consumption	Gross fixed capital formation			
		12	13	14	15	16	17	18	19
1995		100.0	2.7	2.6	3.0	2.1	1.7	3.5	3.7
1996		102.0	2.0	2.4	2.4	0.7	1.8	3.4	3.5
1997		103.4	1.4	1.8	2.0	0.9	0.6	2.6	3.0
1996	Q1	101.4	2.5	2.5	3.2	1.2	2.6	3.6	4.1
	Q2	101.7	2.0	2.6	1.9	0.7	2.0	3.3	3.2
	Q3	102.2	1.8	2.2	1.9	0.4	1.7	3.5	3.7
	Q4	102.6	1.6	2.1	2.0	0.4	1.5	3.3	2.8
1997	Q1	102.9	1.5	2.0	1.7	0.6	1.8	2.9	3.1
	Q2	103.3	1.5	1.6	2.1	0.8	0.3	2.9	3.4
	Q3	103.4	1.2	1.9	1.7	1.0	-0.1	2.4	2.7
	Q4	103.9	1.3	1.7	1.7	1.0	-0.4	2.1	2.8
1998	Q1	104.4	1.4	1.4	1.3	0.6	-2.3	1.0	2.2
	Q2	104.9	1.5	1.5	1.2	0.2	-0.5	1.2	2.8

Sources: Eurostat, except columns 10 and 11 (HWWA-Institut für Wirtschaftsforschung, Hamburg), columns 12 to 16 (ECB calculations based on deflators in national currency) and columns 17 to 19 (ECB calculations based on non-harmonised national data).

1) Residential buildings, based on non-harmonised data.

5 Real economy indicators in the euro area

Table 5.1

Output and demand indicators

1. Gross domestic product and its components

(ECU billions, seasonally adjusted, at 1990 prices) [1]

		GDP	Domestic demand	Private consumption	Government consumption	Gross fixed capital formation	Exports [2]	Imports [2]
		1	2	3	4	5	6	7
1995		4,495.9	4,401.3	2,761.3	708.2	907.9	1,443.5	1,348.9
1996		4,567.9	4,450.2	2,812.7	720.1	912.1	1,509.8	1,392.1
1997		4,684.1	4,538.3	2,854.1	721.8	929.7	1,663.3	1,517.5
1997	Q3	1,177.6	1,137.6	714.5	180.7	233.2	428.7	388.6
	Q4	1,185.4	1,147.7	720.3	179.7	235.8	432.4	394.8
1998	Q1	1,195.1	1,162.9	725.2	181.2	239.9	434.3	402.0
	Q2	1,198.6	1,165.0	728.2	181.5	236.2	441.2	407.5
	Q3 (p)	1,206.3	1,170.8	733.3	180.3	237.7	444.3	408.8

(annual percentage changes) [1]

		GDP	Domestic demand	Private consumption	Government consumption	Gross fixed capital formation	Exports [2]	Imports [2]
		8	9	10	11	12	13	14
1995		2.2	1.9	1.9	0.1	3.3	8.1	7.5
1996		1.6	1.1	1.9	1.7	0.5	4.6	3.2
1997		2.5	2.0	1.5	0.2	1.9	10.2	9.0
1997	Q3	2.8	2.1	1.3	0.3	1.7	13.0	11.7
	Q4	3.2	2.6	2.0	-0.5	2.7	11.4	10.4
1998	Q1	3.8	4.0	2.6	0.3	5.2	11.1	12.2
	Q2	2.5	2.7	2.2	0.4	1.5	7.3	8.4
	Q3 (p)	2.4	2.9	2.6	-0.2	1.9	3.6	5.2

2. Selected other real economy indicators

(annual percentage changes, unless otherwise indicated)

		Industrial production [3]								Retail sales at constant prices	New passenger car registrations
		Total excluding construction 1995 = 100 (s.a.)	Total excluding construction	Manu-facturing	Intermediate goods	Capital goods	Durable consumer goods	Non-durable consumer goods	Construction		
		15	16	17	18	19	20	21	22	23	24
1995		100.0	3.4	3.5	2.5	7.3	-0.7	1.7	0.0	2.0	0.3
1996		100.1	0.0	-0.2	-0.6	1.7	0.0	-0.8	-2.3	1.1	6.6
1997		104.2	4.1	4.7	5.4	4.2	1.0	2.2	-1.2	0.9	3.9
1997	Q3	105.2	4.9	5.4	6.3	5.7	1.4	2.1	-2.3	0.9	6.0
	Q4	106.5	5.7	6.4	7.2	6.1	3.5	2.8	-0.1	2.2	11.2
1998	Q1	107.6	6.3	7.3	7.3	9.2	8.6	1.3	3.0	2.7	12.6
	Q2	108.5	4.4	5.0	4.3	6.6	7.9	2.1	0.0	1.8	3.3
	Q3	109.4	4.0	4.3	3.3	7.0	7.7	1.9	-1.9	3.0	7.5
1997	Nov.	106.1	4.8	5.3	6.2	5.2	2.8	1.3	0.6	-0.8	9.9
	Dec.	106.9	6.5	7.8	8.4	6.4	4.6	4.4	-1.0	3.8	13.6
1998	Jan.	107.0	5.8	7.6	7.7	8.0	5.9	2.2	10.2	2.9	10.7
	Feb.	107.7	6.0	6.9	7.1	8.0	8.6	1.1	0.0	2.2	9.8
	Mar.	108.1	6.9	7.3	7.2	11.2	11.1	0.8	-0.2	3.1	16.5
	Apr.	108.2	3.2	3.7	3.5	4.9	5.5	0.8	-3.0	0.8	-1.8
	May	109.1	6.8	7.7	6.1	10.4	12.3	4.2	2.8	1.9	6.9
	June	108.2	3.3	3.7	3.3	4.7	6.3	1.5	0.3	2.7	5.3
	July	109.7	4.2	4.6	3.6	7.8	8.0	2.4	-0.9	3.6	7.3
	Aug.	109.7	4.8	5.2	4.0	8.0	8.9	2.4	-1.3	2.5	7.3
	Sep.	108.9	3.2	3.5	2.5	5.7	6.9	1.1	-3.3	2.8	7.9
	Oct.	.	.	.	.	.	.	.	.	.	1.3
	Nov.	.	.	.	.	.	.	.	.	.	15.5

Sources: Eurostat, except column 23 (ECB calculation based on non-harmonised national data) and column 24 (ACEA/A.A.A.).

1) Components exclude changes in inventories.

2) Exports and imports cover goods and services and include internal cross-border trade in the euro area.

3) Adjusted for variations in the number of working days.

Table 5.2

Labour market indicators

(seasonally adjusted)

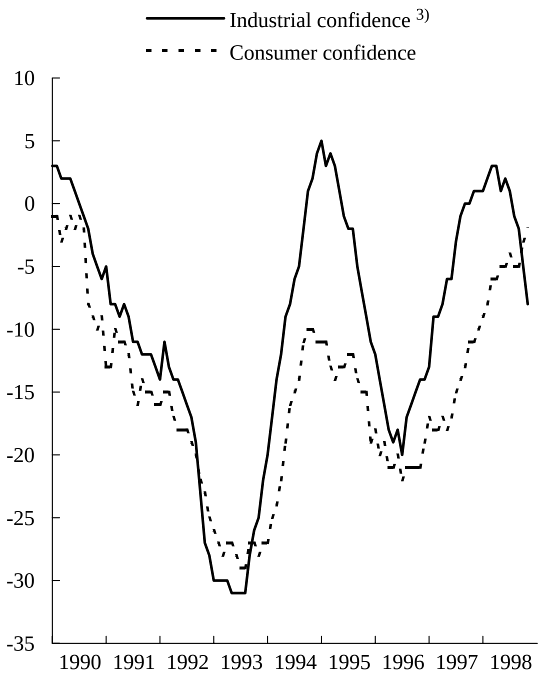
	Employment [1]				Unemployment [2]		Labour productivity [1]	
	Whole economy		Manufacturing		Millions	% of labour force	Whole economy annual percentage changes	Manufacturing annual percentage changes
	1995 = 100	Annual percentage changes	1995 = 100	Annual percentage changes				
	1	2	3	4	5	6	7	8
1995	100.0	0.4	100.0	-0.8	14.400	11.4	1.8	4.4
1996	100.2	0.2	98.6	-1.4	14.822	11.6	1.6	1.2
1997	100.5	0.3	97.9	-0.8	14.927	11.7	2.1	5.6
1997 Q3	100.6	0.3	98.0	-0.3	14.962	11.7	2.5	5.6
Q4	100.8	0.5	98.4	0.5	14.842	11.6	2.6	5.9
1998 Q1	101.1	1.0	99.6	2.2	14.523	11.3	3.4	4.8
Q2	101.5	1.1	100.4	2.9	14.265	11.1	1.7	2.0
Q3	102.0	1.4	100.9	2.9	14.061	11.0	.	.
1997 Nov.	-	-	-	-	14.832	11.6	-	-
Dec.	-	-	-	-	14.775	11.5	-	-
1998 Jan.	-	-	-	-	14.573	11.4	-	-
Feb.	-	-	-	-	14.537	11.3	-	-
Mar.	-	-	-	-	14.459	11.3	-	-
Apr.	-	-	-	-	14.336	11.2	-	-
May	-	-	-	-	14.279	11.2	-	-
June	-	-	-	-	14.179	11.1	-	-
July	-	-	-	-	14.108	11.0	-	-
Aug.	-	-	-	-	14.080	11.0	-	-
Sep.	-	-	-	-	13.994	10.9	-	-
Oct.	-	-	-	-	13.868	10.8	-	-
Nov.	-	-	-	-	13.802	10.8	-	-

Chart 5.3

Opinion surveys

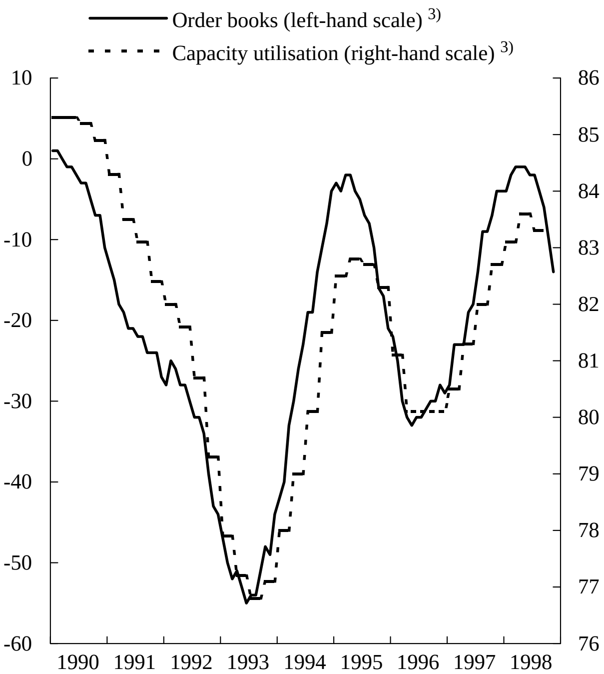
Consumer and industrial confidence indicators

(percentage balances; seasonally adjusted)



Capacity utilisation and order books

(capacity utilisation, percentages; order books, percentage balances; seasonally adjusted)



Sources: ECB calculations based on available national non-harmonised data (columns 1 to 4 and 7 to 8), Eurostat (columns 5 to 6) and European Commission Business and Consumer Surveys (chart data).

1) Quarterly results are based on available data from those countries which compile monthly or quarterly statistics.

2) Calculated according to ILO recommendations.

3) Manufacturing; data on capacity utilisation are collected in January, April, July and October and are shown as 2-quarter moving averages.

6 Saving, investment and financing in the euro area

Table 6

Saving, investment and financing

(as a percentage of GDP, unless otherwise indicated)

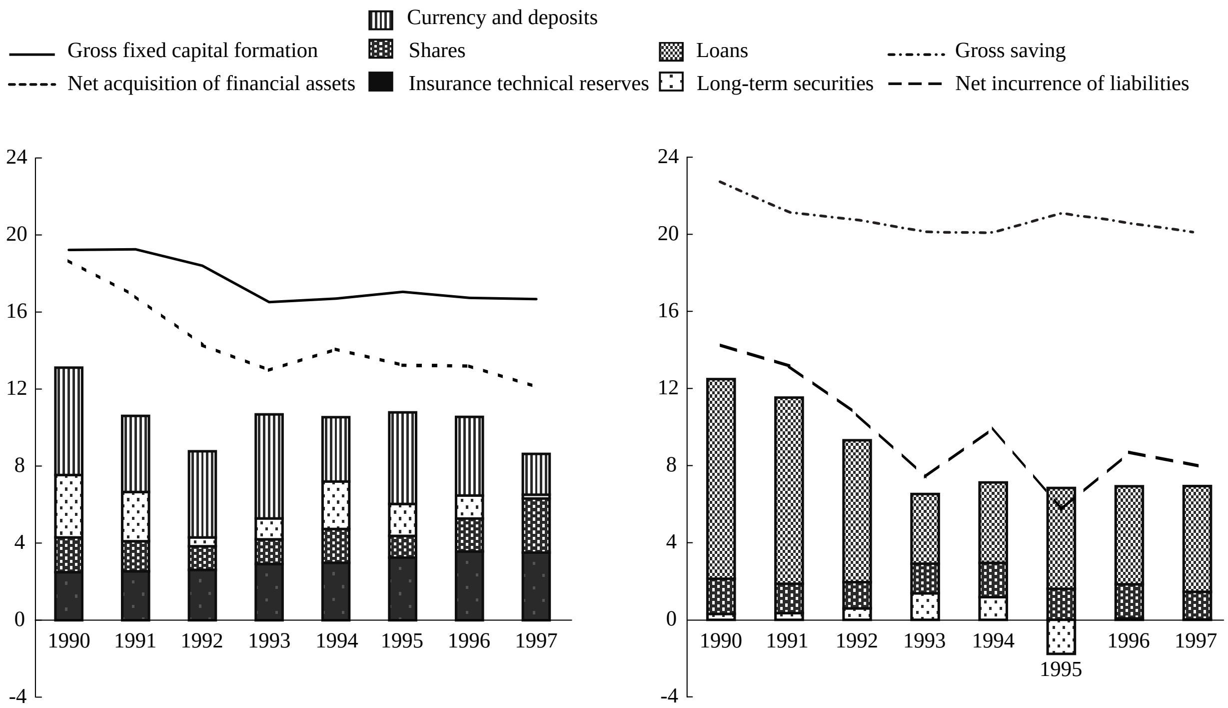
	Euro area saving and investment [1]			Investment of private non-financial sectors [1) 2)]							
	Gross saving	Gross fixed capital formation	Net lending to the rest of the world	Gross fixed capital formation	Non-financial corporations	Net acquisition of financial assets	Currency and deposits	Securities other than shares	Long-term securities	Shares	Insurance technical reserves
	1	2	3	4	5	6	7	8	9	10	11
1990	23.5	22.8	0.1	19.2	14.4	18.7	5.6	4.4	3.2	1.8	2.5
1991	21.9	22.9	-1.2	19.3	14.9	16.8	4.0	3.0	2.6	1.6	2.5
1992	20.9	22.1	-1.0	18.4	14.1	14.3	4.5	1.7	0.5	1.2	2.6
1993	20.0	20.2	0.5	16.5	12.7	13.0	5.4	0.6	1.1	1.3	2.9
1994	20.4	19.8	0.3	16.7	13.0	14.1	3.3	2.3	2.5	1.8	3.0
1995	21.3	20.0	1.0	17.0	13.3	13.2	4.8	1.9	1.7	1.1	3.2
1996	20.8	19.6	1.4	16.7	13.0	13.2	4.1	0.3	1.2	1.7	3.6
1997	21.4	19.0	2.1	16.7	12.9	12.1	2.1	-0.2	0.2	2.8	3.5

	Financing of private non-financial sectors [1) 2)]								Net financial investment	Financial investment as a % of gross investment	Net incurrence of liabilities as a % of financing
	Gross saving	Households	Net incurrence of liabilities	Securities other than shares	Long-term securities	Shares	Loans	Long-term loans	(col. 6 - 14)	(col. 6 / (4+6))	(col. 14 / (12+14))
	12	13	14	15	16	17	18	19	20	21	22
1990	22.7	12.9	14.2	0.6	0.3	1.8	10.4	3.8	4.4	49.3	38.5
1991	21.1	13.1	13.2	0.4	0.3	1.5	9.7	4.1	3.6	46.6	38.4
1992	20.8	13.1	10.7	0.7	0.6	1.4	7.4	4.1	3.6	43.7	33.9
1993	20.1	12.6	7.4	1.3	1.4	1.5	3.6	4.1	5.6	44.0	26.9
1994	20.1	11.7	10.0	1.1	1.2	1.8	4.2	3.5	4.1	45.7	33.1
1995	21.1	11.9	5.7	-1.7	-1.8	1.6	5.2	2.7	7.5	43.7	21.3
1996	20.6	11.7	8.7	0.2	0.1	1.8	5.1	3.2	4.5	44.1	29.7
1997	20.1	11.1	8.0	0.1	0.0	1.4	5.5	2.5	4.1	42.1	28.5

Investment and financing of private non-financial sectors [1) 2)]

(as a percentage of GDP)

Investment **Financing**



Source: ECB.
1) Selected items of financing and investment.
2) Private non-financial sectors comprise non-financial corporations, households and non-profit institutions serving households.

7 General government fiscal position in the euro area and in the euro area countries

Table 7.1

General government fiscal position

(as a percentage of GDP)

1. Euro area [1] - receipts and expenditure

	Current receipts [2]	Direct taxes	Indirect taxes	Social contributions	**Current expenditure** [2]	Public consumption	Interest	Transfers to households	**Net capital expenditure** [2]	Investment	**Deficit (-) / surplus (+)**
	1	2	3	4	5	6	7	8	9	10	11
1990	45.0	12.0	12.9	16.7	45.0	17.5	4.8	18.5	4.1	3.0	-4.1
1991	45.9	12.3	12.9	17.3	46.2	18.1	4.9	19.2	4.2	3.1	-4.4
1992	46.7	12.3	13.0	17.7	47.7	18.5	5.5	19.9	3.6	3.1	-4.6
1993	47.6	12.5	13.2	18.1	49.4	18.8	5.7	20.8	3.9	2.9	-5.6
1994	47.0	12.0	13.4	18.0	48.5	18.5	5.5	20.7	3.6	2.8	-5.1
1995	46.8	12.1	13.3	18.0	48.2	18.2	5.8	20.6	3.6	2.6	-5.0
1996	47.1	12.1	13.4	18.2	48.2	18.3	5.5	20.6	3.2	2.5	-4.2
1997	47.3	12.2	13.5	18.2	47.1	17.9	5.1	20.5	2.7	2.4	-2.5

2. Euro area [1] - deficit and debt

	Primary deficit (-) / surplus (+)	**Cyclically adjusted deficit (-) / surplus (+)** [2]	**Deficit/ debt adjust- ment** [3]	**Change in debt** [4]				**Gross nominal consolidated debt**			
				Total	Currency, deposits and loans	Short-term securities	Medium/ long-term securities	Total	Currency, deposits and loans	Short-term securities	Medium/ long-term securities
	12	13	14	15	16	17	18	19	20	21	22
1990	0.7	-5.7	1.5	5.6	1.3	1.0	3.3	58.4	18.8	9.4	30.2
1991	0.5	-5.9	0.7	5.2	1.2	0.0	4.0	58.3	18.4	8.5	31.4
1992	0.9	-5.6	2.2	6.8	1.7	0.8	4.2	61.8	19.0	8.9	33.9
1993	0.2	-4.9	2.5	8.0	1.5	-0.3	6.9	68.3	20.0	8.3	39.9
1994	0.4	-4.7	0.8	5.9	0.2	0.6	5.1	70.7	19.2	8.5	43.1
1995	0.8	-4.6	2.3	7.2	2.0	-0.2	5.5	74.6	20.3	7.8	46.5
1996	1.4	-3.5	-0.2	3.9	0.3	0.0	3.6	76.0	19.9	7.6	48.5
1997	2.6	-1.9	-0.3	2.2	0.0	-1.0	3.2	75.3	19.1	6.3	49.9

3. Euro area countries - deficit (-) / surplus (+)

	BE	DE	ES	FR	IE	IT	LU	NL	AT	PT	FI
	1	2	3	4	5	6	7	8	9	10	11
1990	-5.5	-2.1	-4.3	-1.6	-2.3	-11.1	5.0	-5.1	-2.4	-5.1	5.4
1991	-6.3	-3.1	-4.5	-2.1	-2.3	-10.1	1.9	-2.9	-3.0	-6.0	-1.5
1992	-6.9	-2.6	-4.1	-3.9	-2.5	-9.6	0.8	-3.9	-2.0	-3.0	-5.9
1993	-7.1	-3.2	-7.0	-5.8	-2.4	-9.5	1.7	-3.2	-4.2	-6.1	-8.0
1994	-4.9	-2.4	-6.3	-5.8	-1.7	-9.2	2.8	-3.8	-5.0	-6.0	-6.4
1995	-3.9	-3.3	-7.3	-4.9	-2.2	-7.7	1.9	-4.0	-5.1	-5.7	-4.7
1996	-3.2	-3.4	-4.7	-4.1	-0.4	-6.7	2.9	-2.0	-3.7	-3.3	-3.5
1997	-2.0	-2.7	-2.6	-3.0	0.9	-2.7	3.0	-0.9	-1.9	-2.5	-1.1

4. Euro area countries - gross nominal consolidated debt

	BE	DE	ES	FR	IE	IT	LU	NL	AT	PT	FI
	12	13	14	15	16	17	18	19	20	21	22
1990	125.7	43.8	44.8	35.5	96.0	98.0	4.7	79.1	57.9	65.3	14.5
1991	127.5	41.5	45.5	35.8	95.3	101.5	4.2	78.9	58.1	67.3	23.0
1992	129.0	44.1	48.0	39.8	92.3	108.7	5.1	79.9	58.0	60.1	41.5
1993	135.2	48.0	60.0	45.3	96.3	119.1	6.1	81.1	62.7	63.1	58.0
1994	133.2	50.2	62.6	48.5	88.2	124.9	5.7	77.9	65.4	63.8	59.6
1995	131.0	58.3	65.6	52.7	80.9	124.2	5.9	79.2	69.2	65.9	58.1
1996	126.8	60.8	70.2	55.7	71.4	124.0	6.6	77.1	69.6	64.9	57.8
1997	121.9	61.5	68.9	58.1	63.4	121.6	6.7	71.4	64.3	61.5	55.1

Sources: European Commission (DG II and Eurostat) and ECB.

1) *The transactions among the euro area countries are not consolidated.*
2) *Euro area excluding Luxembourg for 1990-95.*
3) *Difference between the annual change in nominal gross consolidated debt and the deficit as a percentage of GDP.*
4) *Annual change in nominal gross consolidated debt expressed as a percentage of GDP: [debt(t)-debt(t-1)] / GDP(t).*

Chart 7.2

General government deficit [1)]

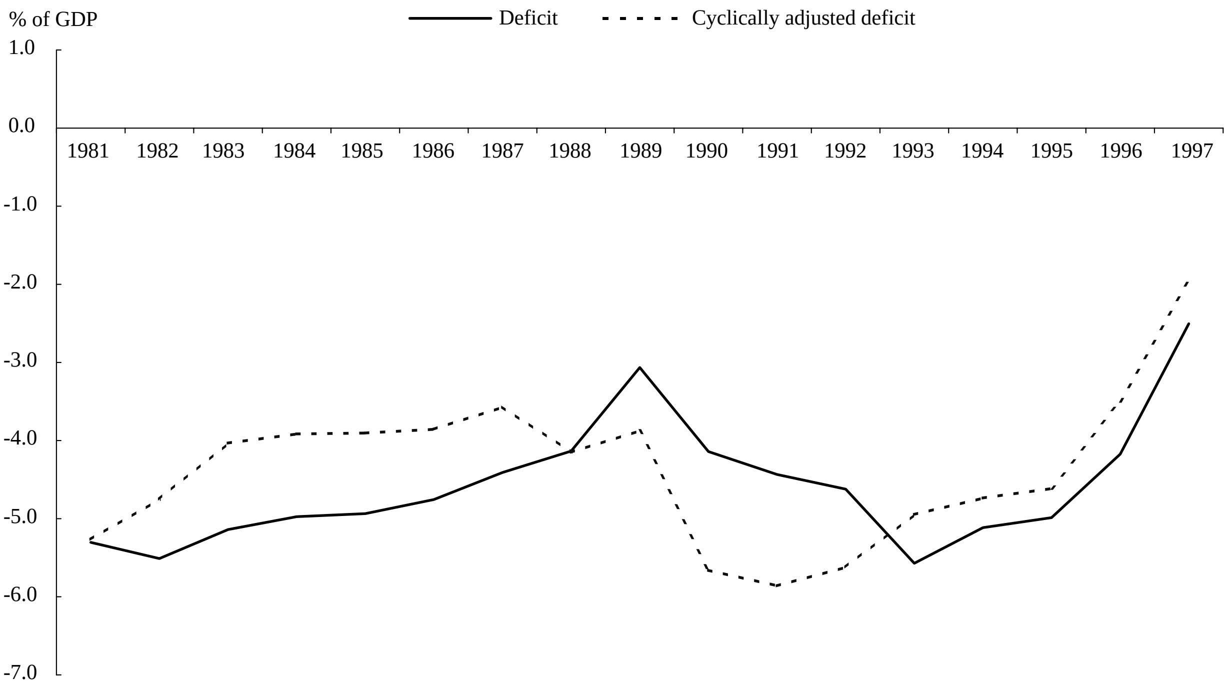
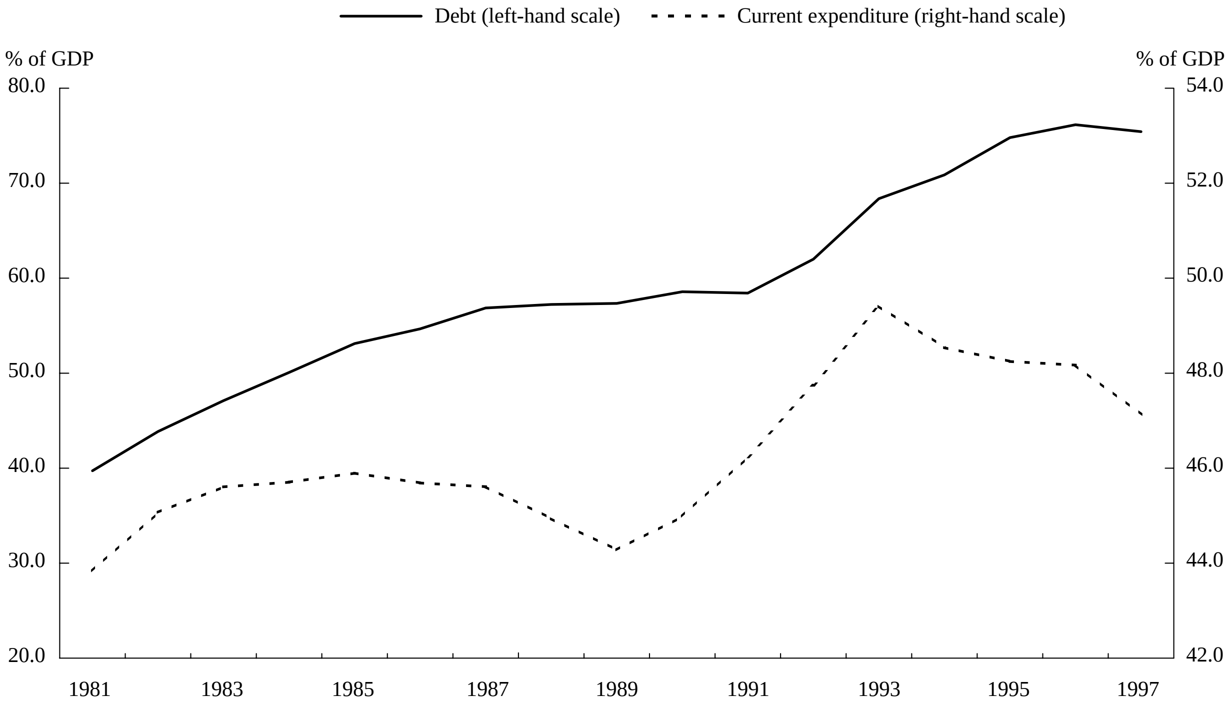


Chart 7.3

General government debt and current expenditure [1)]



Sources: European Commission (DG II and Eurostat) and ECB.
1) Euro area excluding Luxembourg.

9 Trade in goods of the euro area

Table 9.1

Exports

(ECU billions; f.o.b. value)

		Total	Food, drink, tobacco	Raw materials	Energy	Chemicals	Other manufactured articles	Machinery, transport equipment	Other
		1	2	3	4	5	6	7	8
1995		618.56	46.79	14.53	11.14	79.50	182.75	271.31	12.55
1996		663.94	48.65	13.71	12.97	85.08	194.25	293.46	15.82
1997		754.39	52.58	16.23	14.35	98.75	215.77	341.60	15.12
1996	Q1	157.17	11.48	3.43	3.08	20.46	46.11	68.71	3.91
	Q2	164.88	11.94	3.43	3.24	21.26	47.73	73.38	3.89
	Q3	161.58	11.92	3.25	3.15	21.69	48.39	69.34	3.84
	Q4	180.32	13.31	3.60	3.50	21.67	52.03	82.02	4.18
1997	Q1	168.57	11.93	3.80	3.63	22.53	48.56	74.37	3.75
	Q2	189.74	13.28	4.07	3.61	25.08	53.72	86.06	3.92
	Q3	191.67	12.99	4.15	3.42	25.60	55.54	86.29	3.68
	Q4	204.41	14.37	4.21	3.70	25.54	57.95	94.87	3.77
1998	Q1	192.64	13.13	4.12	3.40	26.52	54.29	87.37	3.81
	Q2	202.65	13.92	3.89	3.30	26.93	55.96	94.65	4.01
	Q3	193.49	.	.	.	.	.	.	.
1997	Aug.	54.85	3.94	1.28	1.09	7.89	15.63	23.90	1.10
	Sep.	67.76	4.71	1.49	1.15	8.78	19.54	30.81	1.28
	Oct.	72.54	5.23	1.54	1.26	9.27	21.22	32.65	1.36
	Nov.	65.62	4.63	1.34	1.18	8.20	18.71	30.33	1.23
	Dec.	66.25	4.51	1.33	1.25	8.07	18.02	31.89	1.18
1998	Jan.	57.93	4.04	1.25	1.17	8.36	16.16	25.77	1.18
	Feb.	63.27	4.30	1.36	1.01	8.59	17.99	28.76	1.25
	Mar.	71.44	4.79	1.51	1.21	9.57	20.15	32.84	1.38
	Apr.	67.52	4.68	1.31	1.11	9.16	18.82	30.97	1.47
	May	65.46	4.55	1.26	1.06	8.69	18.06	30.53	1.31
	June	69.67	4.70	1.32	1.12	9.08	19.08	33.14	1.23
	July	72.06	4.49	1.33	1.06	9.26	20.87	33.83	1.22
	Aug.	55.83	3.95	1.23	0.91	7.74	15.43	25.47	1.10
	Sep.	65.60	.	.	.	.	.	.	.
Percentage change compared with the corresponding period in the previous year									
Aug. 1998		1.8	0.2	-4.2	-16.5	-1.9	-1.3	6.6	-0.2
Cumulative Jan.-Aug. 1998		8.5	6.0	0.4	-8.9	9.3	6.0	11.8	0.7

Source: Eurostat; the commodity breakdown is in accordance with the SITC Rev. 3.

Table 9.2

Imports

(ECU billions; c.i.f. value)

		Total	Food, drink, tobacco	Raw materials	Energy	Chemicals	Other manufactured articles	Machinery, transport equipment	Other
		1	2	3	4	5	6	7	8
1995		558.78	46.03	39.81	62.09	52.13	163.71	177.36	17.65
1996		590.45	46.68	36.45	73.85	53.75	166.12	191.34	22.26
1997		666.79	49.42	41.19	80.91	61.59	187.01	226.90	19.76
1996	Q1	147.41	11.72	9.70	16.35	13.60	42.71	47.81	5.52
	Q2	146.66	11.64	9.42	17.53	13.75	40.22	48.69	5.42
	Q3	140.38	11.18	8.29	17.81	12.69	41.75	43.51	5.14
	Q4	156.00	12.13	9.04	22.16	13.71	41.44	51.32	6.19
1997	Q1	156.66	11.29	9.59	20.88	14.51	44.31	51.23	4.85
	Q2	166.17	12.57	11.01	18.62	15.92	46.27	56.98	4.79
	Q3	165.68	12.14	10.01	19.98	15.13	48.62	55.27	4.54
	Q4	178.27	13.43	10.59	21.42	16.03	47.81	63.42	5.57
1998	Q1	180.12	12.64	10.83	17.49	17.58	51.18	64.48	5.92
	Q2	178.32	12.54	11.12	15.87	17.21	50.03	65.76	5.80
	Q3	168.69	.	.	.	.	.	.	.
1997	Aug.	48.65	3.64	2.85	6.78	4.35	14.20	15.60	1.23
	Sep.	60.99	4.26	3.70	6.63	5.57	17.93	21.21	1.69
	Oct.	62.95	4.81	3.68	7.53	5.79	17.33	21.91	1.91
	Nov.	57.42	4.21	3.47	6.84	5.19	15.30	20.65	1.76
	Dec.	57.91	4.41	3.43	7.06	5.06	15.18	20.86	1.91
1998	Jan.	57.77	4.12	3.51	6.16	5.59	16.39	20.10	1.90
	Feb.	58.11	3.95	3.53	5.74	5.53	16.58	20.69	2.10
	Mar.	64.24	4.57	3.80	5.60	6.46	18.21	23.69	1.92
	Apr.	59.84	4.33	3.66	5.42	5.74	16.62	22.24	1.84
	May	56.98	4.03	3.55	5.52	5.56	15.74	20.88	1.71
	June	61.50	4.19	3.91	4.93	5.91	17.67	22.64	2.25
	July	58.78	4.29	3.56	4.91	5.86	17.65	20.75	1.75
	Aug.	49.49	3.68	2.78	4.69	4.66	14.72	17.54	1.43
	Sep.	60.42	.	.	.	.	.	.	.
Percentage change compared with the corresponding period in the previous year									
Aug. 1998		1.7	1.1	-2.3	-30.8	7.0	3.6	12.4	16.2
Cumulative Jan.-Aug. 1998		9.2	4.5	5.2	-18.7	13.3	10.1	18.5	19.3

Source: Eurostat; the commodity breakdown is in accordance with the SITC Rev. 3.

Table 9.3

Trade balance

(ECU billions; exports (f.o.b.) - imports (c.i.f.))

		Total	Food, drink, tobacco	Raw materials	Energy	Chemicals	Other manufactured articles	Machinery, transport equipment	Other
		1	2	3	4	5	6	7	8
1995		59.77	0.76	-25.29	-50.96	27.37	19.04	93.95	-5.11
1996		73.49	1.97	-22.74	-60.88	31.33	28.13	102.12	-6.44
1997		87.60	3.15	-24.96	-66.56	37.16	28.76	114.70	-4.64
1996	Q1	9.76	-0.25	-6.26	-13.27	6.86	3.40	20.89	-1.61
	Q2	18.21	0.30	-5.99	-14.29	7.51	7.50	24.69	-1.52
	Q3	21.19	0.74	-5.04	-14.66	8.99	6.63	25.83	-1.30
	Q4	24.32	1.18	-5.45	-18.66	7.96	10.59	30.70	-2.01
1997	Q1	11.91	0.64	-5.79	-17.26	8.02	4.25	23.14	-1.09
	Q2	23.57	0.72	-6.94	-15.01	9.16	7.45	29.07	-0.88
	Q3	25.99	0.86	-5.86	-16.57	10.47	6.92	31.03	-0.86
	Q4	26.14	0.94	-6.37	-17.72	9.50	10.14	31.45	-1.81
1998	Q1	12.52	0.49	-6.71	-14.10	8.94	3.11	22.89	-2.11
	Q2	24.33	1.38	-7.23	-12.58	9.72	5.93	28.89	-1.79
	Q3	24.80	.	.	.	.	.	.	.
1997	Aug.	6.19	0.31	-1.56	-5.69	3.54	1.42	8.30	-0.13
	Sep.	6.77	0.45	-2.21	-5.48	3.21	1.61	9.60	-0.41
	Oct.	9.59	0.43	-2.14	-6.26	3.48	3.89	10.74	-0.55
	Nov.	8.20	0.42	-2.13	-5.65	3.01	3.41	9.68	-0.53
	Dec.	8.34	0.10	-2.11	-5.81	3.02	2.83	11.03	-0.73
1998	Jan.	0.16	-0.08	-2.25	-4.98	2.77	-0.24	5.67	-0.73
	Feb.	5.16	0.35	-2.17	-4.73	3.07	1.41	8.07	-0.84
	Mar.	7.20	0.22	-2.29	-4.38	3.10	1.94	9.15	-0.53
	Apr.	7.68	0.35	-2.35	-4.31	3.42	2.20	8.73	-0.37
	May	8.48	0.52	-2.28	-4.46	3.13	2.32	9.66	-0.40
	June	8.17	0.51	-2.59	-3.81	3.17	1.41	10.50	-1.02
	July	13.28	0.20	-2.23	-3.85	3.39	3.23	13.08	-0.53
	Aug.	6.34	0.28	-1.55	-3.78	3.08	0.71	7.93	-0.33
	Sep.	5.18	.	.	.	.	.	.	.
Absolute change compared with the corresponding period in the previous year									
Aug. 1998		0.1	0.0	0.0	1.9	-0.5	-0.7	-0.4	-0.2
Cumulative Jan.-Aug. 1998		1.8	0.6	-1.3	9.0	0.7	-4.0	-0.9	-2.3

Source: Eurostat; the commodity breakdown is in accordance with the SITC Rev. 3.

10 Exchange rates

Table 10

Exchange rates [1)]

(period averages; units of national currency per ECU (bilateral); index 1990 = 100 (effective))

		Bilateral ECU exchange rates								
		US dollar	Japanese yen	Swiss franc	Pound sterling	Swedish krona	Danish krone	Greek drachma	Norwegian krone	Canadian dollar
		1	2	3	4	5	6	7	8	9
1994		1.190	121.3	1.621	0.776	9.16	7.54	288.0	8.37	1.625
1995		1.308	123.0	1.546	0.829	9.33	7.33	303.0	8.29	1.795
1996		1.270	138.1	1.568	0.814	8.51	7.36	305.5	8.20	1.731
1997		1.134	137.1	1.644	0.692	8.65	7.48	309.3	8.02	1.569
1997	Q4	1.123	140.5	1.610	0.677	8.58	7.51	310.2	8.01	1.581
1998	Q1	1.087	139.2	1.604	0.660	8.71	7.53	319.1	8.20	1.554
	Q2	1.100	149.5	1.643	0.665	8.60	7.52	339.9	8.28	1.592
	Q3	1.118	156.3	1.642	0.676	8.95	7.50	332.7	8.54	1.690
	Q4	1.177	140.6	1.600	0.702	9.38	7.44	331.5	8.82	1.814
1997	Dec.	1.112	143.9	1.599	0.669	8.66	7.53	310.9	8.06	1.585
1998	Jan.	1.088	140.8	1.604	0.665	8.72	7.53	312.3	8.16	1.566
	Feb.	1.088	136.8	1.593	0.664	8.80	7.53	312.4	8.23	1.561
	Mar.	1.084	139.9	1.614	0.653	8.64	7.55	331.6	8.22	1.536
	Apr.	1.091	144.1	1.643	0.653	8.53	7.55	345.0	8.22	1.560
	May	1.109	149.7	1.639	0.677	8.54	7.50	340.3	8.26	1.603
	June	1.101	154.4	1.645	0.667	8.71	7.52	334.8	8.34	1.613
	July	1.098	154.3	1.661	0.668	8.77	7.52	328.7	8.37	1.630
	Aug.	1.102	159.4	1.646	0.675	8.96	7.50	331.6	8.51	1.688
	Sep.	1.154	155.3	1.617	0.687	9.12	7.48	337.9	8.74	1.756
	Oct.	1.194	144.2	1.596	0.705	9.37	7.44	336.5	8.88	1.842
	Nov.	1.164	140.1	1.612	0.701	9.31	7.44	329.1	8.68	1.793
	Dec.	1.172	137.4	1.594	0.702	9.45	7.45	328.8	8.91	1.807
% ch. vs. [2)]	prev. month	0.7	-2.0	-1.1	0.2	1.6	0.0	-0.1	2.7	0.8
	prev. year	5.4	-4.6	-0.3	4.9	9.2	-1.0	5.8	10.5	14.0

		Bilateral ECU exchange rates							Effective exchange rate (EER) of the euro area [3)]	
		Australian dollar	New Zealand dollar	Hong Kong dollar	Korean won	Singapore dollar	Taiwan dollar	Mexican peso	Nominal	Real
		10	11	12	13	14	15	16	17	18
1994		1.625	2.002	9.17	957.0	1.810	31.44	4.02	93.2	94.1
1995		1.765	1.993	10.01	999.7	1.833	34.28	8.35	97.8	98.9
1996		1.623	1.847	9.68	1,007.9	1.765	34.39	9.52	98.2	99.3
1997		1.528	1.715	8.75	1,073.2	1.678	32.50	8.95	90.4	90.8
1997	Q4	1.621	1.820	8.69	1,291.1	1.795	35.15	9.07	90.4	90.5
1998	Q1	1.630	1.879	8.42	1,745.8	1.817	36.07	9.17	89.6	89.7
	Q2	1.754	2.063	8.53	1,537.0	1.810	37.09	9.55	91.4	91.3
	Q3	1.867	2.199	8.67	1,486.8	1.935	38.71	10.62	93.5	93.6
	Q4	1.887	2.236	9.16	1,516.6	1.942	38.64	11.84	94.6	94.3
1997	Dec.	1.677	1.878	8.61	1,660.6	1.837	36.14	9.04	91.0	91.2
1998	Jan.	1.656	1.876	8.42	1,855.8	1.900	37.08	8.94	90.3	90.5
	Feb.	1.615	1.867	8.43	1,773.8	1.798	35.89	9.26	89.5	89.7
	Mar.	1.619	1.892	8.41	1,615.8	1.757	35.30	9.30	88.9	89.0
	Apr.	1.673	1.971	8.47	1,520.2	1.749	36.07	9.29	89.6	89.5
	May	1.762	2.062	8.60	1,552.4	1.817	37.13	9.53	92.2	92.1
	June	1.824	2.151	8.53	1,539.8	1.866	38.06	9.83	92.2	92.2
	July	1.776	2.116	8.51	1,423.6	1.878	37.79	9.78	92.0	92.2
	Aug.	1.868	2.196	8.55	1,450.4	1.939	38.33	10.34	93.3	93.5
	Sep.	1.962	2.289	8.97	1,592.4	1.994	40.10	11.83	95.2	95.1
	Oct.	1.932	2.284	9.31	1,615.7	1.969	39.81	12.21	95.9	95.5
	Nov.	1.834	2.180	9.05	1,511.9	1.913	38.08	11.64	94.1	93.8
	Dec.	1.893	2.241	9.11	1,426.3	1.941	38.02	11.65	94.0	93.6
% ch. vs. [2)]	prev. month	3.2	2.8	0.7	-5.7	1.5	-0.2	0.0	-0.2	-0.2
	prev. year	12.9	19.3	5.8	-14.1	5.7	5.2	28.9	3.3	2.7

Source: BIS.

1) *From January 1999 onwards the table will continue with bilateral and effective exchange rates for the euro.*

2) *A percentage change of the latest monthly observation is shown compared with the previous month and the same month of the previous year, respectively. A positive change denotes an appreciation of the ECU.*

3) *BIS calculations; based on weighted averages of the euro area countries' effective exchange rates against the trading partners whose currencies are shown in the table. Weights are based on 1990 manufactured goods trade and capture third market effects. Real rates are calculated using national CPIs. Where CPI data are not yet available, estimates are used.*

11 Economic and financial developments in the other EU Member States

Table 11

Economic and financial developments

(annual percentage changes, unless otherwise indicated)

		HICP	General government deficit (-) / surplus (+) as a % of GDP	General government gross debt as a % of GDP	Long-term government bond yield [1] as a % per annum	Exchange rate [2] as national currency per ECU	Current and new capital account [3] as a % of GDP	Unit labour costs [4]	Real GDP	Industrial production index [5]	Standardised unemployment rate as a % of labour force (s.a.)	Broad money [6] [7]	3-month interest rate [7] as a % per annum
		1	2	3	4	5	6	7	8	9	10	11	12
Denmark													
1995		-	-2.4	73.1	8.27	7.33	1.1	1.7	3.0	4.4	7.2	4.1	4.60
1996		2.1	-0.7	68.4	7.19	7.36	1.7	1.0	3.3	1.4	6.8	7.2	3.56
1997		1.9	0.5	64.1	6.26	7.48	0.9	2.8	3.1	4.5	5.5	5.2	3.83
1998		.	.	.	.	7.50	.	.	.	.	.	.	4.00
1997	Q4	1.6	-	-	5.96	7.51	-1.3	3.1	3.3	6.8	5.1	5.2	3.83
1998	Q1	1.6	-	-	5.30	7.53	-0.7	2.2	4.0	5.6	5.0	2.9	3.75
	Q2	1.4	-	-	5.12	7.52	.	2.0	1.1	-1.1	4.6	3.5	4.00
	Q3	1.2	-	-	4.82	7.50	.	3.5	3.4	2.4	4.5	8.4	4.62
	Q4	.	-	-	.	7.44	.	.	.	.	.	.	4.00
1998	June	1.2	-	-	4.99	7.52	-	-	-	5.0	4.5	3.5	4.00
	July	1.4	-	-	4.91	7.52	-	-	-	3.1	4.6	5.3	4.06
	Aug.	1.1	-	-	4.81	7.50	-	-	-	4.9	4.5	6.2	4.25
	Sep.	1.1	-	-	4.74	7.48	-	-	-	-0.8	4.3	8.4	4.62
	Oct.	1.1	-	-	4.67	7.44	-	-	-	1.6	4.2	4.0	4.43
	Nov.	1.1	-	-	4.59	7.44	-	-	-	.	.	4.1	4.12
	Dec.	.	-	-	.	7.45	-	-	-	.	.	.	4.00
Greece													
1995		-	-10.6	110.1	.	303.0	-2.5	11.6	2.1	2.1	7.1	10.2	14.70
1996		7.9	-7.5	112.2	.	305.5	-3.7	10.6	2.7	0.6	7.5	9.2	12.20
1997		5.4	-4.0	109.5	9.92	309.3	.	7.1	3.5	1.0	7.9	9.7	12.50
1998		.	.	.	8.48	330.7	.	.	.	.	.	.	11.40
1997	Q4	4.7	-	-	10.18	310.2	.	.	.	2.8	7.9	9.7	12.50
1998	Q1	4.2	-	-	10.45	319.1	.	.	.	2.9	8.1	4.8	10.85
	Q2	5.0	-	-	7.90	339.9	.	.	.	6.0	10.3	2.7	12.20
	Q3	4.8	-	-	7.83	332.7	.	.	.	3.1	11.7	1.1	12.25
	Q4	.	-	-	7.76	331.5	.	.	.	.	.	.	11.40
1998	June	4.9	-	-	7.74	334.8	-	-	-	6.6	11.1	2.7	12.20
	July	4.8	-	-	7.67	328.7	-	-	-	8.3	11.2	2.3	12.00
	Aug.	4.7	-	-	7.56	331.6	-	-	-	3.2	12.1	2.2	14.00
	Sep.	5.0	-	-	8.25	337.9	-	-	-	-1.4	11.9	1.1	12.25
	Oct.	4.5	-	-	8.45	336.5	-	-	-	1.0	10.4	2.4	11.70
	Nov.	3.9	-	-	7.65	329.1	-	-	-	.	.	5.4	11.45
	Dec.	.	-	-	7.17	328.8	-	-	-	.	.	.	11.40
Sweden													
1995		-	-7.0	78.0	10.24	9.33	.	.	3.9	12.6	8.8	2.7	8.37
1996		0.8	-3.5	77.2	8.02	8.51	.	.	1.3	3.1	9.6	11.4	3.93
1997		1.8	-0.8	76.9	6.62	8.65	2.7	.	1.8	8.1	9.9	1.3	4.68
1998		.	.	.	4.99	8.92	.	.	.	.	.	.	3.42
1997	Q4	2.7	-	-	6.18	8.58	2.1	.	3.3	9.1	9.1	1.3	4.68
1998	Q1	1.9	-	-	5.51	8.71	3.1	.	2.9	4.2	8.7	-0.6	4.50
	Q2	1.4	-	-	5.13	8.60	1.2	.	2.3	6.6	8.6	2.8	4.12
	Q3	0.6	-	-	4.82	8.95	2.4	.	3.5	4.5	8.1	4.8	4.12
	Q4	.	-	-	4.50	9.38	.	.	.	.	.	.	3.42
1998	June	1.4	-	-	4.97	8.71	-	-	-	7.5	8.0	2.8	4.12
	July	1.3	-	-	4.88	8.77	-	-	-	7.2	8.5	5.5	4.12
	Aug.	0.6	-	-	4.80	8.96	-	-	-	6.3	8.2	3.9	4.19
	Sep.	-0.1	-	-	4.79	9.12	-	-	-	1.2	7.6	4.8	4.12
	Oct.	0.1	-	-	4.72	9.37	-	-	-	4.3	7.5	5.9	3.93
	Nov.	0.1	-	-	4.55	9.31	-	-	-	.	7.6	.	3.50
	Dec.	.	-	-	4.22	9.45	-	-	-	.	.	.	3.42
United Kingdom													
1995		-	-5.5	53.9	8.32	0.829	-0.5	1.7	2.8	1.7	8.7	9.9	6.56
1996		2.5	-4.7	54.7	7.94	0.814	-0.2	2.0	2.6	0.3	8.2	9.5	6.56
1997		1.8	-2.1	53.5	7.13	0.692	0.6	3.3	3.5	1.5	7.0	11.8	7.48
1998		.	.	.	5.58	0.676	.	.	.	.	.	.	6.12
1997	Q4	1.9	-	-	6.57	0.677	0.0	3.5	4.0	0.9	6.6	11.8	7.48
1998	Q1	1.5	-	-	6.10	0.660	-1.6	3.1	3.7	0.3	6.4	9.7	7.47
	Q2	1.8	-	-	5.89	0.665	.	.	3.0	0.2	6.3	9.2	7.59
	Q3	1.4	-	-	5.57	0.676	.	.	2.3	.	6.2	9.1	7.27
	Q4	.	-	-	4.75	0.702	.	.	.	.	.	.	6.12
1998	June	1.7	-	-	5.87	0.667	-	-	-	0.0	6.2	9.2	7.59
	July	1.5	-	-	5.92	0.668	-	-	-	-0.6	6.3	10.2	7.65
	Aug.	1.3	-	-	5.63	0.675	-	-	-	.	6.2	8.8	7.50
	Sep.	1.5	-	-	5.16	0.687	-	-	-	.	6.2	9.1	7.27
	Oct.	1.3	-	-	4.99	0.705	-	-	-	.	.	9.1	7.12
	Nov.	1.4	-	-	4.93	0.701	-	-	-	.	.	.	6.62
	Dec.	.	-	-	4.33	0.702	-	-	-	.	.	.	6.12

Sources: Eurostat (columns 1, 8 and 10 (except Greece)); European Commission (DG II and Eurostat) (columns 2 and 3); Reuters (column 12); national data (columns 4, 5, 6, 7, 9, 10 (Greece) and 11).

1) *Average-of-period values.*
2) *For more information, see Table 10.*
3) *BPM4; BPM5 for Sweden.*
4) *Whole economy; data for the United Kingdom exclude employers' contribution to social security.*
5) *Manufacturing; adjusted for working days.*
6) *M3; M4 for the United Kingdom.*
7) *End-of-period values.*

12 Economic and financial developments outside the EU

Table 12.1

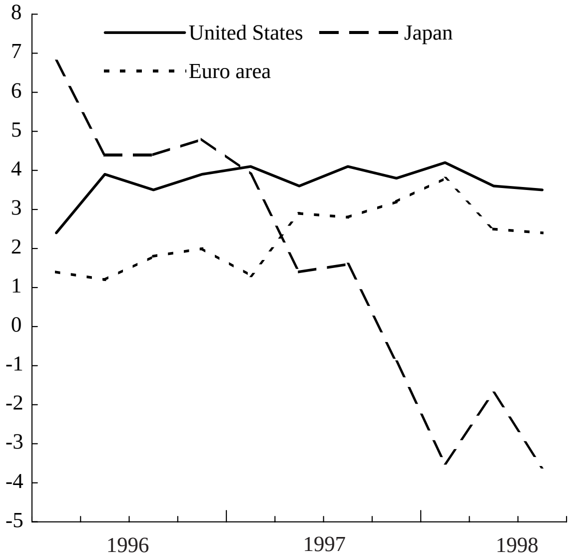
Economic and financial developments

(annual percentage changes, unless otherwise indicated)

		Consumer price index	Unit labour costs [1]	Real GDP	Industrial production index [1]	Standardised unemployment rate as a % of labour force (s.a.)	M2 [2]	3-month interbank deposit bid rate [3] as a % per annum	10-year government bond yield [3] as a % per annum	Exchange rate [4] as national currency per ECU	Fiscal deficit (-) / surplus (+) as a % of GDP	Gross public debt [5] as a % of GDP
		1	2	3	4	5	6	7	8	9	10	11
United States												
1995		2.8	-1.6	2.3	5.4	5.6	2.1	5.44	6.69	1.308	-2.3	60.8
1996		2.9	-2.3	3.4	4.8	5.4	4.9	5.43	6.54	1.270	-1.2	59.9
1997		2.3	0.0	3.9	6.7	4.9	5.0	5.62	6.45	1.134	0.1	57.8
1998		.	.	.	.	.	.	5.00	5.33	1.121	.	.
1997	Q4	1.9	0.7	3.8	7.3	4.7	5.7	5.62	5.99	1.123	.	57.8
1998	Q1	1.5	1.1	4.2	6.0	4.7	6.5	5.59	5.67	1.087	.	57.7
	Q2	1.6	1.0	3.6	5.0	4.4	7.2	5.59	5.67	1.100	.	56.1
	Q3	1.6	1.4	3.5	3.2	4.6	7.4	5.20	5.27	1.118	.	55.2
	Q4	.	.	.	.	.	.	5.00	4.72	1.177	.	.
1998	June	1.7	-	-	3.6	4.5	7.2	5.59	5.58	1.101	-	-
	July	1.7	-	-	2.9	4.5	7.3	5.56	5.53	1.098	-	-
	Aug.	1.6	-	-	3.7	4.5	7.2	5.50	5.41	1.102	-	-
	Sep.	1.5	-	-	2.9	4.6	7.9	5.20	4.87	1.154	-	-
	Oct.	1.5	-	-	2.9	4.5	8.5	5.12	4.58	1.194	-	-
	Nov.	1.5	-	-	2.0	.	8.8	5.12	4.89	1.164	-	-
	Dec.	.	-	-	.	.	.	5.00	4.69	1.172	-	-
Japan												
1995		-0.1	-2.5	1.5	3.4	3.1	3.0	0.50	3.32	123.0	-3.6	.
1996		0.1	-1.7	5.1	2.3	3.4	3.3	0.31	3.03	138.1	-4.3	.
1997		1.7	-1.8	1.4	3.6	3.4	3.1	0.36	2.15	137.1	-3.3	.
1998		.	.	.	.	.	.	0.18	1.30	146.4	.	.
1997	Q4	2.1	1.8	-0.9	-0.7	3.4	3.3	0.36	1.68	140.5	.	.
1998	Q1	2.0	3.7	-3.5	-4.0	3.7	4.7	0.50	1.65	139.2	.	.
	Q2	0.3	7.1	-1.7	-8.5	4.2	3.7	0.43	1.36	149.5	.	.
	Q3	-0.2	.	-3.6	-8.6	4.3	3.7	0.12	1.14	156.3	.	.
	Q4	.	.	.	.	.	.	0.18	1.04	140.6	.	.
1998	June	0.1	5.4	-	-7.6	4.2	3.4	0.43	1.22	154.4	-	-
	July	-0.1	8.5	-	-9.2	4.2	3.5	0.34	1.36	154.3	-	-
	Aug.	-0.3	8.3	-	-9.1	4.3	3.8	0.37	1.17	159.4	-	-
	Sep.	-0.2	.	-	-7.6	4.3	3.8	0.12	0.88	155.3	-	-
	Oct.	0.2	.	-	-7.9	.	3.9	0.68	0.82	144.2	-	-
	Nov.	0.8	.	-	-5.5	.	4.4	0.68	0.89	140.1	-	-
	Dec.	.	.	-	.	.	.	0.18	1.39	137.4	-	-

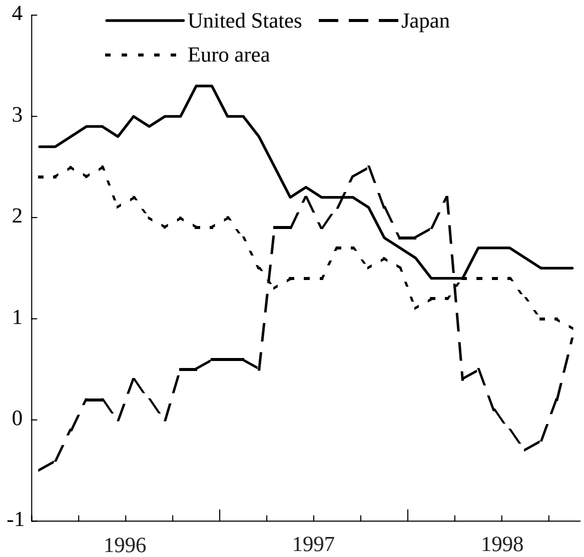
Real gross domestic product

(annual percentage changes)



Consumer price indices

(annual percentage changes)



Sources: National data (columns 1, 2 (United States), 3, 4, 6, 9 and 11); OECD (column 2 (Japan)); Eurostat (column 5 and euro area chart data), Reuters (column 7); European Commission (DG II) (column 10).

1) *Manufacturing.*
2) *Average-of-period values, M2 and CDs for Japan.*
3) *For more information, see Tables 2.5 and 2.6.*
4) *For more information, see Table 10.*
5) *Gross consolidated debt for the general government (end of period).*

Table 12.2

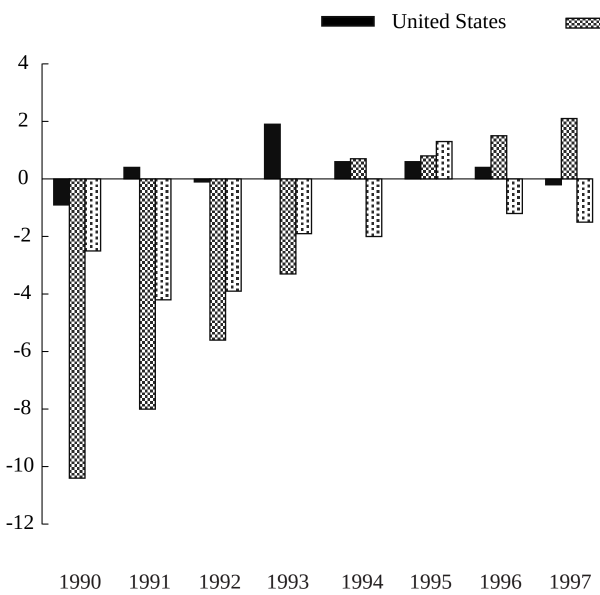
Saving, investment and financing

(as a percentage of GDP)

	National saving and investment			Investment and financing of non-financial corporations						Investment and financing of households [1]			
	Gross saving	Gross capital formation	Net lending to the rest of the world	Gross capital formation	Gross fixed capital formation	Net acquisition of financial assets	Gross saving	Net incurrence of liabilities	Securities and shares	Capital expenditure	Net acquisition of financial assets	Gross saving	Net incurrence of liabilities
	1	2	3	4	5	6	7	8	9	10	11	12	13
United States													
1994	15.5	17.5	-1.7	7.4	6.7	4.1	7.9	3.5	1.4	12.4	7.6	13.7	4.5
1995	16.3	17.4	-1.4	7.8	7.2	6.0	8.3	5.4	2.5	12.2	6.7	13.4	4.9
1996	16.6	17.8	-1.6	7.8	7.5	5.2	8.2	4.8	1.4	12.4	5.7	13.3	5.1
1997	17.3	18.4	-1.7	8.4	7.6	4.2	8.2	4.4	1.9	12.3	4.8	12.7	4.9
1997 Q1	17.0	18.1	-1.6	8.2	7.4	6.1	8.1	5.9	1.5	12.4	3.0	12.7	4.5
Q2	17.6	18.5	-1.5	8.8	7.5	2.4	8.3	2.9	1.4	12.2	5.7	13.2	4.7
Q3	17.5	18.4	-1.7	8.3	7.7	4.8	8.4	5.2	2.0	12.3	5.7	12.8	5.4
Q4	17.3	18.5	-2.0	8.4	7.7	3.7	8.1	3.6	2.5	12.3	4.8	12.1	4.9
1998 Q1	17.7	19.1	-2.1	8.9	7.9	5.9	8.2	7.2	2.3	12.5	4.3	11.5	5.6
Q2	17.2	18.7	-2.5	8.4	8.0	4.4	8.1	5.1	2.7	12.8	6.5	11.5	5.6
Q3	17.2	18.8	-2.7	8.6	7.9	4.1	8.1	4.8	2.1	12.8	3.8	11.0	5.5
Japan													
1994	31.3	28.7	2.7	12.8	14.5	1.6	12.3	1.0	0.8	7.2	10.3	12.6	1.5
1995	30.8	28.6	2.1	14.9	14.9	3.1	13.5	2.3	0.5	5.3	10.3	13.1	1.9
1996	31.5	30.0	1.4	14.6	15.3	1.7	15.2	0.3	1.0	6.7	6.4	12.7	1.1
1997	30.9	28.7	2.2	15.5	16.1	3.3	15.2	1.2	0.1	5.6	7.1	12.3	0.7
1997 Q1	33.4	29.4	1.5	.	.	0.6	.	-8.1	-1.0	.	-3.3	.	-0.9
Q2	31.2	26.6	2.3	.	.	2.6	.	-1.9	1.4	.	10.7	.	0.7
Q3	30.2	30.0	2.2	.	.	3.0	.	3.1	0.4	.	-0.3	.	1.5
Q4	29.0	29.3	2.6	.	.	6.6	.	10.7	-0.3	.	19.8	.	1.5
1998 Q1	33.2	27.9	2.4	.	.	0.6	.	-15.3	-2.6	.	-5.4	.	-2.3
Q2	.	24.1	.	.	.	-0.6	.	1.3	2.2	.	12.2	.	0.0
Q3	.	26.7	.	.	.	3.7	.	-2.2	0.5	.	-2.6	.	0.5

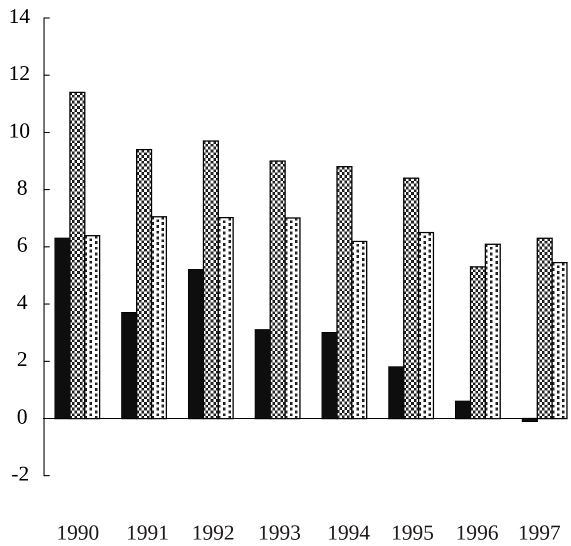
Net lending of non-financial corporations

(as a percentage of GDP)



Net lending of households [1]

(as a percentage of GDP)



Sources: ECB, Federal Reserve Board, Bank of Japan and Economic Planning Agency.

1) *Households including non-profit institutions serving households. For Japan, saving of non-profit institutions serving households is included under saving of non-financial corporations.*

General notes

The basis for the statistics compiled and published by the European Central Bank (ECB) was laid down in the document entitled the "Statistical requirements for Stage Three of Monetary Union (Implementation Package)" which was made available to banking associations and others involved in statistical preparations for Stage Three by the European Monetary Institute (EMI) and the national central banks (NCBs) in July 1996. The Implementation Package covers money and banking statistics, balance of payments statistics, international investment position statistics, financial accounts statistics, price and cost and other economic statistics.[1)]

The focus of these statistics is the euro area as a whole. More detailed and longer runs of data, with further explanatory notes, are to be published on the ECB's Web site (http://www.ecb.int), and new or expanded data will appear in the ECB Monthly Bulletin as they become available.

Because the composition of the ECU does not coincide with the currencies of the Member States adopting the single currency, amounts expressed in ECU are influenced by the market behaviour of the other currencies. To avoid this effect in the monetary statistics, the pre-1999 data in Tables 2.1 to 2.4 are expressed in units converted from national currencies at the irrevocable fixed exchange rates announced on 31 December 1998. Unless indicated otherwise, price and cost statistics before 1999 are based on the data expressed in national currency terms.

Methods of aggregation and/or consolidation (including cross-country consolidation) have been used as appropriate.

The cut-off date for the statistics included in this issue was 7 January 1999.

Monetary policy and financial statistics

Tables 1.1 to 1.4 show the consolidated financial statement of the Eurosystem, data on Eurosystem operations and statistics relating to minimum reserves (not available for this first issue). Monetary data relating to Monetary Financial Institutions (MFIs), including the Eurosystem, are shown in Tables 2.1 to 2.3. Table 2.4 sets out monetary aggregates drawn from the consolidated MFI balance sheet. Fuller quarterly data relating to the MFI balance sheet and monetary statistics are planned for the March issue. A complete list of MFIs is published on the ECB's Web site. Details of the sector definitions are set out in the "Money and Banking Statistics Sector Manual – Guidance for the statistical classification of customers" (EMI, April 1998). The "Money and Banking Statistics Compilation Guide" (EMI, April 1998) explains recommended practices to be followed by the NCBs. From 1 January 1999 the statistical information is collected and compiled on the basis of the ECB Regulation concerning the consolidated balance sheet of the Monetary Financial Institutions sector (ECB/1998/16).

Statistics on money market interest rates, long-term government bond yields and stock market indices (Tables 2.5 to 2.7) are produced by the ECB from wire services. For details concerning the statistics on retail bank interest rates (Table 2.8), see the footnote at the bottom of the relevant page.

Statistics on securities market issues and redemptions (Table 3) are expected to be available in spring 1999.

Prices and real economy indicators

The data presented in the ECB Monthly Bulletin are, with a few exceptions, produced by the European Commission (mainly Eurostat) and national statistical authorities. Euro area results are obtained by aggregating data for individual countries. As far as possible, the data are harmonised and comparable. However, the availability of comparable data differs among the statistics and is, as a general rule, better for the more recent periods than for earlier data. The seasonally adjusted data are produced by Eurostat or national sources.

The Harmonised Index of Consumer Prices (HICP) for the euro area (Table 4.1) is available from 1995 onwards. It is based on national HICPs that follow the same methods in all euro area countries. The implementation of the 1998 EU Council Regulation on short-term statistics will enlarge the range of available

1) *Money and banking statistics are the responsibility of the ECB at the European level; responsibility for balance of payments, international investment position and financial accounts statistics is shared with the European Commission (Eurostat); price and cost and other economic statistics are the responsibility of the European Commission (Eurostat).*

euro area data, including timely and comparable data for retail trade turnover, for which, at present, an estimate based on national data is used (Table 5.1).

With regard to statistics on national accounts (Tables 4.2 and 5.1), the implementation of the European System of National and Regional Accounts 1995 (ESA 95) during 1999 and thereafter will pave the way for fully comparable data, including quarterly summary accounts, across the euro area.

Unemployment rates conform to International Labour Organisation (ILO) guidelines. Data on employment are derived from the most recent national sources using similar, but not fully comparable definitions of employment (Table 5.2).

Opinion survey data (Chart 5.3) draw on the business and consumer surveys of the European Commission.

Financial accounts statistics

The Implementation Package foresaw a need for detailed information covering the financial transactions and balance sheets for the euro area in order to complement monetary analysis and policy research. The aim is to provide a fairly full, though not complete, set of financial accounts for the euro area based on money and banking, balance of payments, capital market, non-MFI financial corporation and government finance statistics, and drawing also on the ESA 95 national accounts. Table 6 shows euro area aggregates based on national capital and financial accounts.

A more detailed and further harmonised set of statistics presenting financial accounts for the euro area is expected to appear in the ECB Monthly Bulletin during the course of 1999.

General government fiscal position

Table 7.1 shows the euro area general government fiscal position as a percentage of GDP. This is compatible with the data notified by the Member States in the framework of the Excessive Deficit Procedure as laid down in the Treaty establishing the European Community. In addition, government deficit and debt data are shown for individual euro area countries due to their importance in the framework of the Stability and Growth Pact.

Euro area receipts and expenditure, and the cyclically adjusted deficit, are compiled on the basis of country data provided by the European Commission (DG II). The aggregation is carried out by the ECB. While the data on the deficit/surplus are harmonised, data on receipts and expenditure are not. The breakdown of debt is compiled from data provided by NCBs.

Balance of payments, trade and exchange rate statistics

Balance of payments data for the euro area will be published for the first time in the April issue, and international investment position statistics in the autumn, conforming to the 5th edition of the IMF Balance of Payments Manual (October 1993) and the ECB Guideline of 1 December 1998 on the statistical reporting requirements of the European Central Bank (ECB/1998/17). Meanwhile, Tables 9.1 to 9.3 present data on euro area trade in goods only.

From January 1999 onwards, statistics on exchange rates (Table 10) will be produced on the basis of the daily reference rates published by the ECB.

Other statistics

Statistics on other EU Member States (Table 11) follow the same principles as those for data relating to the euro area. Data for the United States and Japan (Tables/Charts 12.1 and 12.2) are obtained from national sources. Saving, investment and financing data for the United States and Japan (Table/Chart 12.2) are structured in the same way as the capital and financial flows data shown for the euro area in Table/Chart 6.

Conventions used in the tables

"-"	not applicable
"."	not available
"…"	nil or negligible
"billion"	10^9
(p)	provisional
s.a.	seasonally adjusted

Abbreviations

Countries

BE	Belgium
DK	Denmark
DE	Germany
GR	Greece
ES	Spain
FR	France
IE	Ireland
IT	Italy
LU	Luxembourg
NL	Netherlands
AT	Austria
PT	Portugal
FI	Finland
SE	Sweden
UK	United Kingdom
JP	Japan
US	United States

Others

ACEA/A.A.A.	European Automobile Manufacturers' Association
BIS	Bank for International Settlements
BPM4	IMF Balance of Payments Manual (4th edition)
BPM5	IMF Balance of Payments Manual (5th edition)
CDs	Certificates of deposit
C.i.f.	Cost, insurance and freight at the importer's border
CPI	Consumer Price Index
ECB	European Central Bank
ECU	European Currency Unit
EMI	European Monetary Institute
ESA 95	European System of National and Regional Accounts 1995
ESCB	European System of Central Banks
EU	European Union
EUR	Euro
F.o.b.	Free on board at the exporter's border
GDP	Gross domestic product
HICP	Harmonised Index of Consumer Prices
ILO	International Labour Organisation
IMF	International Monetary Fund
MFIs	Monetary Financial Institutions
NCBs	National central banks
Repos	Repurchase agreements
SITC Rev. 3	Standard International Trade Classification (revision 3)

In accordance with Community practice, the EU countries are listed in this report using the alphabetical order of the country names in the national languages.

Chronology of monetary policy measures of the Eurosystem

The monetary policy measures recorded below for the period up to 1 January 1999 refer to decisions involving the Governing Council of the ECB with regard to the preparation of the monetary policy framework of the Eurosystem (comprising the ECB and the national central banks of the 11 Member States that have adopted the euro as from the start of Stage Three).

1 June 1998

Establishment of the European Central Bank (ECB) and the European System of Central Banks (ESCB).

7 July 1998

The Governing Council of the ECB adopts a Recommendation for a Council Regulation (EC) concerning the application of minimum reserves by the European Central Bank in Stage Three of Economic and Monetary Union. The main provisions of the recommended Council Regulation define the basis for the minimum amount of reserves which the ECB may require credit institutions to hold on their accounts with the national central banks. In addition, they provide the ECB with specific regulatory powers and specify the sanctions to be imposed in the event of non-compliance. This ECB Recommendation was published in the Official Journal of the European Communities No. C 246 of 6 August 1998, page 6 ff.

The Governing Council further agrees on some of the key features of the minimum reserve system to be applied as from the start of Stage Three: the minimum reserve holdings are defined to be within a range of 1.5-2.5% of the relevant liability base (after deducting a lump-sum allowance); interbank liabilities and liabilities vis-à-vis the Eurosystem will not be subject to reserve requirements; holdings of required reserves will be remunerated at the average, over the maintenance period, of the interest rate (weighted according to the number of calendar days) corresponding to that of the Eurosystem's main refinancing operations.

1 September 1998

The ECB and the national central banks of the Member States outside the euro area (Denmark, Greece, Sweden and the United Kingdom) agree to lay down the operating procedures for an exchange rate mechanism in Stage Three of Economic and Monetary Union (the ERM II Agreement). The ERM II Agreement specifies the procedure of intervention on the basis of the EU Council Resolution of 16 June 1997 setting up an exchange rate mechanism as from 1 January 1999. The ERM II Agreement was published in the Official Journal of the European Communities No. C 345 of 13 November 1998, page 6.

11 September 1998

The Governing Council of the ECB endorses the Report entitled "The single monetary policy in Stage Three: General documentation on ESCB monetary policy instruments and procedures". The Report contains a detailed description of the monetary policy instruments and procedures to be applied by the ESCB (Eurosystem) in Stage Three of Economic and Monetary Union. The Report was published on 18 September 1998.

26 September 1998

The ministers of the euro area Member States, the ECB and the ministers and central bank governors of Denmark and Greece, in a common procedure involving the European Commission and after consultation of the Monetary Committee, welcome the decision of the governments of Denmark and Greece to extend their participation in the exchange rate mechanism from ERM I to ERM II, linking their currencies to the euro. They agree that the Danish krone will participate in ERM II with a fluctuation band around its central rate against the euro of ±2.25% and that the Greek drachma will participate in ERM II with the standard fluctuation band around its central rate against the euro of ±15%. These agreements became effective from the opening of foreign exchange markets on 4 January 1999 (see also the ERM II Agreement of 1 September 1998).

13 October 1998

The Governing Council of the ECB announces the main features of the stability-oriented monetary policy strategy that the Eurosystem will pursue in Stage Three of Economic and Monetary Union: the primary objective of price stability shall be defined as a year-on-year increase in the Harmonised Index of Consumer Prices (HICP) for the euro area of below 2% and is to be maintained over the medium term; a prominent role shall be assigned to money, with a reference value for the growth of a broad monetary aggregate; in parallel, a broadly based assessment of the outlook for price developments shall play a major role in the monetary policy strategy.

Further to its decision on 7 July 1998, the Governing Council announces the application of a minimum reserve ratio of 2% to a credit institution's liability base of overnight deposits, deposits with an agreed maturity of up to two years, deposits redeemable at notice up to two years, debt securities issued with an agreed maturity of up to two years and money market paper. A reserve ratio of 0% will apply to repurchase agreements, deposits with an agreed maturity of more than two years and debt securities issued with an agreed maturity of more than two years. The lump-sum allowance to be deducted from the reserve requirement of each institution is set at €100,000. If a credit institution cannot provide evidence of its interbank liabilities in the form of debt securities with a maturity of up to two years and money market paper, it will be allowed to deduct a standardised 10% of these liabilities from its liability base.

3 November 1998

The Governing Council of the ECB adopts two Guidelines: one specifying general principles to be followed by the national central banks when carrying out operations in their domestic assets and liabilities outside the scope of the single monetary policy; and one establishing the thresholds above which national central banks must obtain the ECB's approval for operations in their remaining foreign reserve assets, including gold. In addition, the Governing Council adopts a Guideline according to which the participating Member States will have to give advance notice to the ECB of any transactions with their foreign exchange working balances which exceed a certain amount. These legal acts are based on provisions of the Statute of the ESCB and are aimed at ensuring the singleness of monetary policy and the consistency of such transactions with the Community's monetary and exchange rate policies.

1 December 1998

The Governing Council of the ECB agrees on the remaining issues regarding the monetary policy strategy of the Eurosystem. The first reference value for monetary growth is set at 4½% and refers to the broad monetary aggregate M3. The derivation of the reference value is based on the contributions to monetary growth resulting from assumptions made for prices (year-on-year increases in the HICP of below 2%), the medium-term trend in real GDP growth (of 2-2½% per annum) and the medium-term trend decline in the velocity of circulation of M3 (in the approximate range of ½-1% each year). Monetary developments against this reference value will be monitored on the basis of three-month moving averages of the monthly 12-month growth rates for M3. In December 1999 the Governing Council will review the reference value for monetary growth (see also the announcement of the Governing Council on 13 October 1998).

Further to its decisions on 7 July and 13 October 1998, the Governing Council adopts a Regulation on the application of minimum reserves. This ECB Regulation follows the Council Regulation (EC) No. 2531/98 of 23 November 1998 concerning the application of minimum reserves by the European Central Bank and establishes minimum reserve requirements for credit institutions in the euro area in the pursuance of monetary policy objectives. The ECB Regulation entered into force on 1 January 1999 and was published in the Official Journal of the European Communities No. L 356 of 30 December 1998, page 1.

22 December 1998

The Governing Council of the ECB decides that the first main refinancing operation of the Eurosystem will be a fixed rate tender offered at an interest rate of 3%. This operation will be initiated on 4 January 1999, while the allotment decision will be taken on 5 January 1999 and settlement will take place on 7 January 1999. In addition, the first longer-term refinancing operation will be announced on 12 January 1999 (with a settlement date of 14 January 1999) and will be conducted through a variable rate tender using the single rate allotment procedure.

The Governing Council furthermore decides that the interest rate for the marginal lending facility will be set at a level of 4.5% and the interest rate for the deposit facility at a level of 2% for the start of Stage Three, i.e. 1 January 1999. As a transitional measure, between 4 and 21 January 1999, the interest rate for the marginal lending facility will be set at a level of 3.25% and the interest rate for the deposit facility at a level of 2.75%. The Governing Council intends to terminate this transitional measure following its meeting on 21 January 1999.

31 December 1998

In accordance with Article 109l (4) of the Treaty establishing the European Community, the EU Council, acting with the unanimity of the Member States of the European Community without a derogation, upon a proposal from the European Commission and after consultation of the ECB, adopts the irrevocable conversion rates for the euro, with effect from 1 January 1999, 0.00 a.m. (local time).

The ministers of the euro area Member States, the ECB and the ministers and central bank governors of Denmark and Greece decide, in a common procedure involving the European Commission and after consultation of the Monetary Committee, to fix the central rates against the euro for the currencies participating in the exchange rate mechanism which comes into operation on 1 January 1999. Further to this decision on the euro central rates, the ECB, Danmarks Nationalbank and the Bank of Greece establish by common accord the compulsory intervention rates for the Danish krone and the Greek drachma. A fluctuation band of ±2.25% will be observed around the euro central rate for the Danish krone. The standard fluctuation band of ±15% will be observed around the euro central rate for the Greek drachma (see also the ERM II Agreement of 1 September 1998 and the agreement of 26 September 1998).

7 January 1999

The Governing Council of the ECB decides that for the two main refinancing operations to be announced on 11 and 18 January 1999 respectively the same conditions will apply as for the first such operation, which was settled on 7 January 1999, i.e. they will be fixed rate tenders conducted at an interest rate of 3%. The Governing Council confirmed its intention to maintain the main refinancing rate at this level for the foreseeable future.

Documents published by the European Central Bank (ECB)

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Monthly Bulletin
Articles published from January 1999 onwards:
"The euro area at the start of Stage Three", January 1999.
"The stability-oriented monetary policy strategy of the Eurosystem", January 1999.

Monetary policy
"The single monetary policy in Stage Three: General documentation on ESCB monetary policy instruments and procedures", September 1998.

"Report on electronic money", August 1998.

Payment systems
TARGET brochure, July 1998.
"The TARGET service level", July 1998.

"Assessment of EU securities settlement systems against the standards for their use in ESCB credit operations", September 1998.