

FOREIGN BANKING AND BUSINESS CONDITIONS

ANNUAL REPORT OF THE GERMAN REICHSBANK

The annual report of the German Reichsbank for 1926 contains the following account of economic conditions in Germany during the year:

During 1926 the German currency situation on the whole remained satisfactory, notwithstanding the continued difficulties of the economic situation. The Reichsbank throughout the year sold for its own notes or other means of payment any required amount of foreign exchange, and was able also to purchase to their full amount all foreign exchange bills offered to it. No demand was made on the Reichsbank for gold for payments abroad, but the bank will, of course, not hesitate to make gold available for such purposes if the exchange situation should require it.

In the economic crisis, which had reached its climax in Germany during 1926, the weeding-out process under way ever since the stabilization of the currency made still further progress during the year under review. The crisis reached its peak during the first third of the year, then moderated gradually, until toward the end of the year there was a slight business revival in various lines. The necessary measures for reconstruction and reorganization, as well as for adjustment to consumption demand, were carried through with decision and foresight—a fact which bears witness to the sustained vigor of the German people. A series of events, some transitory and some lasting, undoubtedly helped business to weather the severe crisis; most important of all was the English coal strike; there were also the continued support which German credit obtained from abroad; the decline, as a result of foreign currency reforms, in the dumping of commodities on the German market by countries with depreciated foreign exchanges; and the increased purchasing power of the world market. Mention should be made here of certain signs of progress in the restoration of friendly relations between European countries accompanied by international economic agreements. There were also the lower tax rates adopted during the year under review, the program of providing employment, other measures of assistance, and, finally, the progress made in meeting reparations payments out of the proceeds of taxation.

The passing of the economic crisis is clearly seen in the number of dishonored drafts at the Reichsbank during 1926; in comparison with the total domestic bills accepted by the bank, they stood at 4.25 per cent in January, as against an average of 0.72 per cent in 1913 and 2.23 per cent in 1925, and declined slowly to 3.07 per cent in March, 1.57 per cent in June, 0.91 per cent in September, and 0.82 per cent in December.

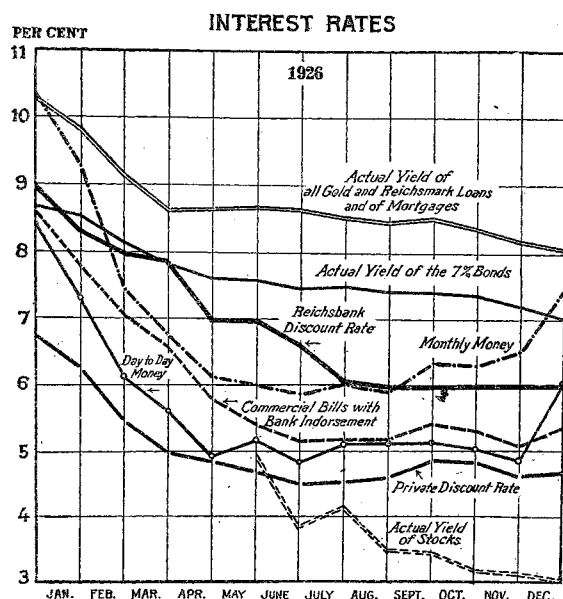
The price which had to be paid for the reorganization and reform of the German economic system was by no means small. The actual number of workers out of employment at the end of the year—2,000,000 as compared with 1,500,000 at the end of 1925—including those unemployed persons whose term of unemployment relief had expired, serves as a striking illustration of the seriousness of the difficulties, uncertainties, and dangers which have not yet been overcome. To one looking more deeply into the situation, the basic facts must still seem uncertain in spite of all the apparent progress, both because any disturbing factors growing out of the unsettled political situation affect the economic situation; and because the reconstruction of European trade, after 10 years' interruption, continues to be obstructed by the protective tariffs and the industrial nationalism of both old and new countries. Furthermore, there can be no doubt that the problem of reparations, which weigh heavily on German industry, and reparations payments and deliveries flowing out of Germany into the rest of the world, and directed not by economic considerations but by political motives, will inevitably be the source of increasingly serious disturbances to the free international exchange of commodities and to the prosperity, built thereupon, of economically interdependent nations.

The trend of economic development put upon the Reichsbank heavy tasks and responsible decisions in the matter of its credit and discount policy. The bank's constant concern was necessarily to encourage the tendency toward a further lowering of interest rates which was beginning to be apparent on the market, and thus to make it easier for the increasing supply of capital to provide a most effective stimulus to activity in agriculture, industry, and com-

merce. When, at the beginning of 1926, it became possible definitely to discard the temporary expedient of credit rationing, the Reichsbank, having due regard to the condition of the market, set about a further gradual reduction of its discount rate: on January 12, to 8 per cent; on March 27, to 7 per cent; on June 7, to 6½ per cent; on July 6, to 6 per cent. The rate for loans on collateral was reduced from 11 per cent to 7 per cent during the year; the rate for credit at the Gold Discount Bank from 6 per cent to 5 per cent. The interest and commission rates of the private banks and other financial institutions followed—at first, partly under pressure from the Reichsbank, which entered into negotiations

which still remained between rates in the money market and in the capital market showed that only partial success had been achieved in removing the difficulties which continued to obstruct the development of a rightly proportioned allocation of available funds to the long-term and the short-term credit market. The average rates were as follows:

	In 1913	In fourth quarter 1926
	Per cent	Per cent
Call money rate.....	4.12	5.30
Private discount rate.....	4.98	4.73
Reichsbank discount rate.....	5.88	6.0
Interest paid on mortgage and loans (about).....	4.50	8.20
Yield on stocks.....	3.97	3.11



to this end with the local institutions as well as with the various associations. With the exception of the rate on monthly money, money rates in the open market, which had continued to move in unison with the bank rate during 1925, declined sharply during the past year and at times reached rather low levels.

At the same time rates on long-term credits began to decline, as is indicated by the curve on the accompanying diagram of actual interest paid on mortgages and loans; and during the first quarter of the year, the yield of these securities declined by about one-sixth in the course of a few weeks. This decline continued during the entire year, although at a more moderate rate. Similarly, the rate on long-term money throughout the country showed a decline. Nevertheless, the considerable spread

The course of interest rates was closely connected with the great abundance of short-term money. This abundance was further increased during the first half of the year by the business depression; by the clearing out of stocks of commodities, which later on was aided by the English strike; the increase of reserves in the hands of industry; the accumulation of new capital; the continuous import of capital from abroad; and chiefly the increasingly large sums of public funds held by government institutions. Another important factor was that the majority of banking firms and other lenders, in view of the short maturity of the funds put at their disposal, especially of the still unused portions of the loans floated both abroad and at home, and being still under the influence of the recent crisis, were most eager to invest their funds at the shortest possible maturities. The abundance of short-term money was so great at times that considerable amounts, for lack of investment opportunities, sought employment abroad, especially on the London bill market. The decline of interest rates in the money market began to slow down only when, after the middle of the year, the depression was relieved by a moderate revival in various branches of industry. In connection with the raising of the redemption fund installment of 293,000,000 reichsmarks, which, in conformity with the law providing for the liquidation of the Rentenbank, was payable at the end of November for the liquidation of rentenmark circulation, there came a slight tightening of the money market toward the end of the year.

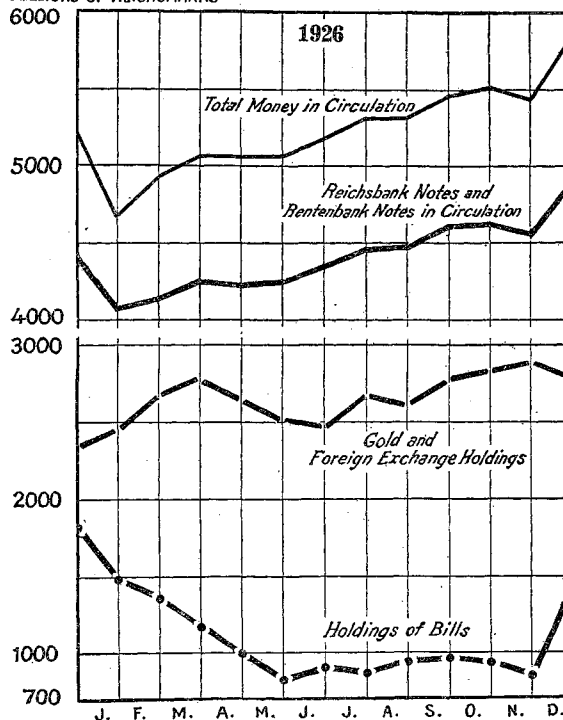
On the long-term capital market the Reichsbank intervened at the opportune moment at the beginning of the year to aid the latent tendency toward improvement by means of

carefully planned purchases of mortgage bonds for its own and for depositors' account, and by purchases of mortgage securities through the Gold Discount Bank. This was referred to in the report of last year and will be discussed further on. The easing of the tension hitherto prevailing on the capital market then began to show marked progress. Capital issues revived to a degree hardly anticipated; foreign capital also began to take an active part in the German security market. In spite, however, of the remarkable increase of capital issues, one must be careful not to overestimate either the actual power of absorption of the German capital market or the creation of new capital at home, all the more so because the reparations deliveries provided for in the Dawes plan continue to absorb a large part of the newly created savings. Large amounts of the new capital issues, as well as of securities purchased on the stock exchange, have been bought not for permanent investment but temporarily with funds available for only a short time, and generally with the expectation of being able by this means to make a profit on the market or to obtain a higher rate of interest. Certainly, the development of the capital market during the past year, influenced as it was by the abundance of funds on the money market, should not delude anyone as to the necessity of employing available long-term capital very sparingly for current business purposes; because, as developments show, the demands for capital by central governments, municipalities, and other public bodies are very large, and the assistance of foreign capital which at times is indispensable can not always be counted on. That the development of a sound consolidation of capital requirements is still far from being realized is clearly shown by the above-mentioned changes in the yield of stocks and securities which bear fixed rates of return, especially if one compares them with their pre-war conditions. While during 1913 the actual yield on capital invested in securities bearing a fixed rate of interest was about one-half of 1 per cent higher than the actual yield of stocks, which at that time stood at about 4 per cent, this difference at the end of 1926 was about 5 per cent, since the yield on stocks was about 3 per cent and the yield on securities bearing a fixed rate of interest was 8 per cent. Thus, although the nominal yield on stocks was considerably lower than in 1913, the average level of the yield on securities bearing a fixed rate of interest was considerably higher than the level at the end of 1913.

For the Reichsbank, the development of conditions on the money market and on the capital market brought about a progressive decrease in its domestic discount business. The steady, copious stream of foreign credits caused the bank to be called upon more for the purchase of foreign exchange bills than for rediscounts. The accompanying chart shows the increasing

GOLD AND FOREIGN EXCHANGE HOLDINGS AND MONEY IN CIRCULATION

MILLIONS OF REICHSMARKS



divergence, especially noticeable in the early months of the year, between the development of the domestic bill portfolio and that of the gold and foreign exchange holdings of the Reichsbank.

In this respect even the economic improvement which began in the last four months of the year, and from which a contraction of the money market might have been expected, brought no change. Not until December did the demand for rediscounts and loans on collateral show a passing accession of strength in connection with the above-mentioned tightening of the money market.

While the gold and foreign exchange holdings of the Reichsbank rose from 2,230,600,000 reichsmarks at the end of 1925 to 2,794,500,000

reichsmarks at the end of 1926, the total domestic rediscounts granted by the Reichsbank declined from 1,826,600,000 reichsmarks at the end of 1925 to 784,300,000 reichsmarks on August 23, then fluctuated between 800,000,000 and 950,000,000 reichsmarks until the middle of December, and at the end of the year showed a sharp temporary rise to 1,412,900,000 reichsmarks. The stream of foreign exchange bills flowing into the Reichsbank resulted in an expansion of the circulation; the circulation of Reichsbank notes and Rentenbank notes together rose from 4,436,200,000 reichsmarks at the end of 1925, with some fluctuations to 4,899,600,000 reichsmarks at the end of 1926. The total monetary circulation, including Reichsbank notes, Rentenbank notes, notes of the private banks of issue, and subsidiary currency, rose from 5,208,000,000 to 5,829,800,000 reichsmarks.

In the above-mentioned total of domestic rediscounts at the end of 1925 were included 473,100,000 reichsmarks, representing such amounts as had been rediscounted with public bodies in order to furnish them with interest-bearing investments for their liquid funds. This kind of rediscounting, since from the first it was a measure intended for only a short transition period, was discontinued in the course of the first half year, partly because the cash reserves available for investment by the public bodies concerned had declined, and also because with the reduction of the domestic bill portfolio that part of the note cover which, according to section 28b of the banking law, must consist of bills and checks, came on several occasions perilously near to its legal minimum. Moreover, the Reichsbank was continually obliged to employ a considerable part of the foreign exchange bills presented to it—so far as these were not converted into gold—for the purchase of bills on the foreign market in order to maintain the required note cover in bills and checks, either in domestic or in foreign bills. Not only did the supply of domestic bills eligible for note cover decline in amount, but the maturity of the paper offered for rediscount constantly became shorter; in the second half of the year it averaged only about 30 days as against 38 days at the beginning of the year; bills presented for rediscount by the financial houses, as a rule, ran scarcely more than 22 days, while those of the Berlin banks had a maturity of only about 13 days. Thus, a great part of the bill portfolio consisted of paper discounted shortly before its maturity.

In order to safeguard agriculture from a recurrence of the great injury which had resulted the year before from forced sales of the grain harvests and from the accompanying fall of prices on the grain market, the Reichsbank announced its willingness to extend credits for financing crops. This action enabled the farmer to pledge his crops as security for loans of six months' maturity at the agricultural cooperatives; the commercial bills resulting from these transactions could be sold by the cooperatives to the Prussian Central Cooperative Association, to which the Reichsbank had given an extensive rediscount privilege. The abundance of funds on the money market enabled cooperatives sometimes to retain these credits for their own account; furthermore, the large volume of mortgage loans made to agriculture during the year, the rise of grain prices, and the various measures of assistance taken by the Government improved the agricultural situation so much in comparison with the previous year that the Reichsbank was called upon for only the most moderate amounts in carrying out the above-mentioned policy.

Agriculture was also greatly benefited through purchases of agricultural mortgage bonds made by the Reichsbank during the year to a nominal value of 55,300,000 reichsmarks with resources provided out of the pension reserve, and to a nominal value of 113,800,000 reichsmarks in trust for public administrative bodies. These purchases contributed greatly to the revival of the mortgage-bond market. This revival was further strengthened by the announcement of the Gold Discount Bank that it was prepared to accept agricultural mortgage bonds of the Rentenbank Kreditanstalt, which were issued at a rate considerably lower than the customary interest rate—for example, at 7 per cent on their par value and at a maturity of from three to five years. The issue of these mortgage bonds brought about a general lowering of interest rates on the mortgage market. Moreover, this short-term interim form of credit made it possible for agriculture to defer the final satisfaction of its long-term capital requirements to a time when the progressive building of new capital would in all probability have made interest rates more normal and more bearable for the farmer. For reasons of currency policy, the possibility of attracting foreign capital to finance these interim credits was not considered. The distribution of credits to agriculture was carried on by the various private and public

mortgage credit banks, which granted credit to the ultimate borrower at a rate of interest slightly above $7\frac{1}{2}$ per cent. The actual payment of these credits to the borrower unfortunately suffered many delays because the land registry offices were too overburdened to be able always to record individual claims promptly in the register. This was the result of greater difficulties and a greater burden of work growing out of the legislation in respect to currency revaluation. At the end of the year altogether about 300,000,000 reichsmarks of mortgage bonds were issued, of which 200,700,000 reichsmarks were in the account of the Gold Discount Bank. It deserves to be mentioned in this connection that during the year under review, in the collateral loan business of the Reichsbank, the margin of lending¹ against the nominal value of reichsmark and gold mortgage bonds rose in rapid succession from 50 per cent to $66\frac{2}{3}$ per cent and again to 75 per cent, and an increasing number of securities new to the collateral loan business of the Reichsbank have been admitted to rediscount.

In the matter of influencing the relation between monetary supply and demand there were two highly important problems with which the Reichsbank had been deeply concerned, even during previous years; the complete lack of unity, the shortsightedness and mismanagement in the administration of the so-called public funds, and the excessive demands for foreign credits; both being primary causes of the unnatural and exaggerated liquidity of the money market. The amounts belonging in the strict sense to public funds, over which the Reich, the States, and the municipalities have control, and the revenues of the Reich administrations, such as the postal and railway systems and the funds arising out of social legislation, have been in very large volume since stabilization; they have constantly fed the money market and have tended to interfere with an accurate appraisal of the position of the market. In many cases the administration of these funds has been devoted to profitable investment for purely private industry. It is regrettable that through force of circumstances the great public departments, especially the State railways and postal system, should be separated financially from the Reich, and should thus have been compelled to create and maintain separate cash and working reserves. Whereas before the war there was perfect cooperation among the

various offices, and the management of their funds was centralized in the treasury of the Reich and of the various States respectively, so that it was possible to operate with a minimum of reserves, there is now to be observed an almost independent division of funds and of fiscal organizations. The centralization of funds and of fiscal agencies corresponding to the pre-war system would not only make their administration more consistent and more rational and avoid the existing disadvantages, but would also obviate the accumulation of such large cash holdings, and thereby would release more resources to productive business. It is especially desirable that the cash reserves of the Reich treasury—according to the principles of administration approved in pre-war times as well as according to the example of other great countries—should flow regularly through the local branches of the Reichsbank to the central treasury of the Reich, which should again be administered by the Reichsbank. Continuous streams from such great sources of accumulated wealth as the treasury of the financial administration and the public departments represent, permit a larger part of the circulating medium to return to the bank more quickly, by this means cause a general decline of notes in circulation, and thus increase the effective influence of the central bank of issue. Understood in this way, the coordination of public reserves in the giro account of the Reichsbank does not mean, as is often mistakenly asserted, a centralization of investment on the Berlin market; on the contrary, in the extensive network of Reichsbank branches throughout the country, the most complete decentralization and redistribution of funds is guaranteed.

If the financial administration of the Reich should, so far as possible, reduce its own large working capital, it must on the other hand be in a position to obtain temporary working credits in case of need. The authority which is granted the Reichsbank in section 25 of the bank law, to extend credit to the Reich, is inadequate because of its limitation to a maximum of 100,000,000 reichsmarks. The Reichsbank therefore suggested that the Reich, in case of emergency, might again resort to the sale of treasury bills on the open market. In order to facilitate the sale of these bills, the bank offered to admit them to rediscount at the Reichsbank in a limited amount. By the law of July 8, 1926, dealing with the revision of the bank statutes, it was provided that treasury bills issued by the Reich, which mature in three months at the latest, and for

¹ That is, the percentage of the par value which the Reichsbank lent.

which another guarantor of unquestioned financial standing besides the Reich has assumed responsibility, can be presented for rediscount, according to section 21, article 2; likewise, by section 21, article 3, their eligibility as collateral for loans has been established. The amount of treasury bills offered for rediscount and as collateral together can not exceed 400,000,000 reichsmarks. No occasion arose for the practical application of this regulation during the past year.

In regard to foreign credits, the Reichsbank found itself obliged during the period under review, as also during the preceding year, to issue emphatic warnings against the rapidity and the amount of foreign loans flowing into the country, and to do everything possible without injuring legitimate German business interests to check the too extensive and sharp demand for foreign credit. German loans during the year were negotiated abroad in a nominal value of almost 1,750,000,000 reichsmarks (against 1,250,000,000 reichsmarks in 1925); of this about 600,000,000 reichsmarks (as against 500,000,000 reichsmarks in 1925) represented public loans—loans issued by states and municipalities as well as those issued with state or municipal guaranty. Statistics for the corresponding amount of short-term foreign credits are not available.

Aside from the possible serious consequences to the currency and the economic situation, the extensive employment of foreign credits has a bearing also on the reparations situation. Foreign exchange bills arising out of foreign loans can not be regarded as the proceeds of an economic surplus resulting from the productivity of our country, as contemplated by the Dawes plan for the execution of reparations payments (I, V). Most certainly no conclusions as to the existence of funds available for transfer can be drawn from the gold and foreign exchange holdings of the Reichsbank so far as these holdings arise not from a surplus of production but from foreign credits. The suspension of foreign credits during the first months of 1927 and the consequent extensive decline in the foreign exchange holdings of the Reichsbank have proved this.

The gold and foreign exchange policy of the Reichsbank is, of course, strongly influenced by each phase of the foreign credit situation. The growth in gold and foreign exchange holdings is shown in the chart on page 336. This increase took place entirely in gold holdings, which have risen from 1,208,100,000 reichsmarks at the beginning of the year to 1,831,400,000 reichsmarks, while the foreign exchange

holdings have remained at about the level shown at the end of the year; according to the balance sheets, at the end of 1925 they amounted to 1,022,500,000 reichsmarks and at the end of 1926 to 963,100,000 reichsmarks. In accordance with the principles explained in last year's report, the Reichsbank, as a matter of currency policy, has endeavored to provide the gold and foreign exchange note cover required by the bank law not only for its own note circulation but for the circulation of the Rentenbank as well.

Beginning August 23, 1926, it was found possible to give up the policy regarded necessary by the Reichsbank up to that time, of binding the reichsmark closely to the currency of the United States of America through the purchase and sale of dollars at the fixed rate of 4.20 reichsmarks per dollar. The quotation of the reichsmark accordingly became independent of the dollar quotation; with some fluctuations between the gold points it showed a slight premium over the dollar until October, and during the next few weeks until toward the end of the year, it moved in a course slightly below dollar parity. Some time before this, by the edict of May 1, 1926, the legal restrictions still in force on foreign exchange operations were almost entirely removed. The last remaining provisions, which concerned the so-called foreign exchange banks, have meanwhile also been revoked by a decree of February 22, 1927. Toward the end of 1926 the Reichsbank established an international clearinghouse business with foreign banks of issue, which permits the direct transfer of funds between the offices of the Reichsbank and those of foreign note-issuing banks; by the end of the year relations of this kind were established with the Austrian National Bank, the National Bank of Czechoslovakia, the Hungarian National Bank, the Swiss National Bank, and the Bank of Danzig. This new arrangement came into effect at the beginning of 1927; our experience with this and its further development will have to be discussed in next year's report.

Gold imports, which accompanied the import of capital into Germany, amounted during 1926 to 586,300,000 reichsmarks, from which must be subtracted a small export of 9,700,000 reichsmarks, leaving a net import of 576,600,000 reichsmarks. Of this about 546,000,000 reichsmarks came into the Reichsbank; 274,200,000 reichsmarks, it is true, had their origin in gold deposits maintained abroad, where the bank had been in the habit of placing such amounts of gold as were ac-

quired outside the country; the remainder came for the most part directly from the hands of arbitrage dealers. The arbitrage purchases assumed considerable importance, especially during the last five months of the year. With the weakening of the exchange value of

sterling at that time, the quotation of the pound in relation to Germany declined repeatedly to the gold export point, so that gold exports from England became a profitable operation.

ANNUAL REPORT OF THE BANK OF POLAND

The annual report of the Bank of Poland, presented to the meeting of stockholders on February 10, 1927, contains the following account of economic and financial developments in Poland during the year 1926:

At the beginning of 1926 the crisis brought about by the depreciation of the zloty in the course of 1925 reached its culminating point. The year began under very difficult economic conditions. Unemployment, amounting to about 35 per cent of all industrial workers, continued as a disquieting symptom. The acute crisis had dissipated the general optimism which had grown up since the period of inflation, checked economic activity, and developed a spirit of economy which was imposed rigorously throughout every domain of life. The favorable harvest and the crisis in exchange furnished a check to importing and encouraged exporting. After September, 1925, the merchandise balance became favorable. This favorable balance strengthened the position of the Bank of Poland and aided in sustaining monetary stability, while it also furnished the money market with funds provided out of savings. These developments made it possible gradually to modify financial difficulties and to mobilize capital for industry, and they contributed to decrease unemployment and to increase fiscal receipts. After June the budget deficit, which had been considerable at the beginning of 1926, no longer appeared. For the first time since its independence, the Government was able to achieve a balanced budget.

Finances of the Government.—The budget had been too high during 1924 and 1925 and not proportioned to the actual resources of the country. The budget for 1924 showed a deficit of 12 per cent, that for 1925 of 13 per cent of the receipts, these deficits being occasioned by the issue of token currency and by loans which had not been provided for in the estimates. Through a series of measures taken by the Government toward the end of 1925 and during 1926, including a sharp reduction of governmental expenses, it has been possible to control this situation.

During 1926 not only was the increase in governmental expenses checked, but some

reduction was effected. The importance of the economies introduced in the budget appears clearly when one considers that the index of prices rose rapidly following the depreciation of the currency unit. It is true that the nominal amount of actual expenditures by the State during 1926 showed a slight increase over the year before, but the real value of these Government expenditures showed a considerable decrease, the level of prices on the market having risen during this period by 30 per cent. Expenditures during the first six months of the year exceeded receipts by 71,400,000 zlotys. Thereafter, beginning with July, receipts ran continuously in excess of expenditures.

One may attribute the more favorable situation of the treasury to improvement in general conditions, to the measures taken by the Government in respect to an increase of 10 per cent in taxation, to the rise in prices for monopoly products, and finally to the vigorous effort in the direction of reorganizing public enterprises. As a result, the budget of 1926 closed with a surplus of 53,600,000 zlotys, although for preceding years there were deficits amounting to 235,500,000 zlotys for 1925 and to 189,400,000 zlotys for 1924. The surplus of receipts made it possible for the treasury to repay outstanding foreign debts, to effect a considerable reduction in paper currency, to repay 25,000,000 zlotys of advances of the Bank of Poland, and finally to build up cash reserves, which are indispensable for a more rational management of finance in the future.

Agriculture.—After the difficulties caused by the poor harvest of 1924, the excellent harvest of 1925 had an exceedingly beneficial influence on the agricultural situation. This improvement coincided with the exchange crisis. The prices of grain were almost perfectly adjusted to the fluctuations of the dollar and to the level of international prices. This circumstance neutralized the disastrous effects on the Polish market of the fall in the world price of wheat during the second half of 1925—a price decline which resulted from abundant harvests. During 1926 the level of world prices for wheat

FOREIGN BANKING AND BUSINESS CONDITIONS

ANNUAL REPORT OF THE GERMAN REICHSBANK

The annual report of the German Reichsbank for 1927 was presented to the general meeting of shareholders on March 14, 1928. The full text of the report is given herewith.

General economic improvement.—In the German business situation the gradual improvement which began in the second half of 1926 became more and more marked until the second half of 1927, and thereafter for the remainder of the year maintained its level. It exhibited in general the character of a domestic development, and in all its phases was effected by extensive use of foreign capital loans. Although "rationalizing" of business enterprises was prosecuted with all possible energy, the number of employed persons continued to rise. Unfortunately the improvement achieved was not always consolidated; and it will not be consolidated so long as the restraints imposed by foreign politics create in German business circles that uncertainty which we now find everywhere. To enable her to live, Germany requires not only freedom from foreign political fetters but also, in consideration of her reparations obligations, a willingness on the part of foreign countries to receive relatively larger amounts of products and deliveries in kind from her than Germany receives from them.

Changes in Reichsbank discount rates.—Improvement in the general situation was a primary cause of the activity in the money market which began at the end of February, 1927. A superabundant inflow of foreign loans, under conditions of business depression and of a correspondingly moderate demand for capital, had brought about a very considerable lowering of interest rates during 1926 and had brought the Reichsbank out of touch with the money market in spite of successive reductions in the discount rate from 9 to 6 per cent. As early as November or December of 1926 it would have been possible to reduce the discount rate still further, except that it seemed advisable to wait until after the year-end settlements. As interest rates in the open market, after the usual tension at the end of the year, declined rapidly during the early days of January, and a strong return flow of funds to the Reichsbank set in during the first week of January, a reduction of the discount rate from 6 to 5 per cent was made effective on January 11, 1927. On this occasion the Reichsbank stated emphatically

that only actual developments could determine whether the new rate should be regarded as established for any considerable period. At the same time a lessening of the inflow of foreign funds was expected because of the decline of German interest rates. This expectation proved correct until the beginning of the second half of February. From that time on open-market interest rates advanced, the increase being induced by a rapidly growing demand on the domestic capital market arising out of the floating of public loans, particularly the surprisingly well received great loan of the Reich; induced, also, by continuous improvement of the business situation, and especially by a vigorous expansion of speculative business on the bourse financed largely by credit. Interest rates paid for funds on the bourse reached such a height that, with substantially lower rates prevailing at the same time in the bill market, foreign short-term funds flowed into the German banking and stock-exchange business in large amounts. This development showed that the level of the Reichsbank rate was effective in only one section of the money market, namely, that occupied with dealings in bills, and exerted no effective influence over the inflow or outflow of foreign funds. In order, therefore, to prevent undue extension of bank credit for various activities which escaped the normal influence of the Reichsbank rate, the Reichsbank repeatedly took occasion to impress upon the private banks the necessity of maintaining their assets in liquid condition. After this advice had been heeded to the extent of contracting stock-exchange credit operations in particular, an advance in the discount rate from 5 to 6 per cent followed on June 10. On October 4 the increasing demands of commerce and industry necessitated another advance to 7 per cent.

At the time of reduction of the discount rate on January 11, the Lombard rate was still maintained at 7 per cent in order to check the extensive borrowing on collateral which had taken the place of earlier month-end bill offerings. It was possible still to maintain the Lombard rate unchanged when the discount rate was raised on June 10, 1927, and not until October 4 was it raised to 8 per cent.

The money market.—The movement of interest rates in the open market in comparison

with the Reichsbank discount rate is shown in the accompanying chart. From this chart it may be seen that the rate for month-to-month money showed a rising tendency from the end of February throughout the year. For day-to-day money the same tendency is unmistakable, although sharp fluctuations are shown—for this reason among others, that very often as a result of large end-of-month settlements a temporary but great abundance of day-to-day money was created, the effect of which was that rates were depressed for a brief period. Funds available in the private discount market at no time reached any considerable amount. Acceptances of the Berlin "great banks," for example, amounted to 263,800,000 reichsmarks at the end of October, 1926, and to 386,600,000 reichsmarks at the end of October, 1927, as compared with 1,260,200,000 reichs-

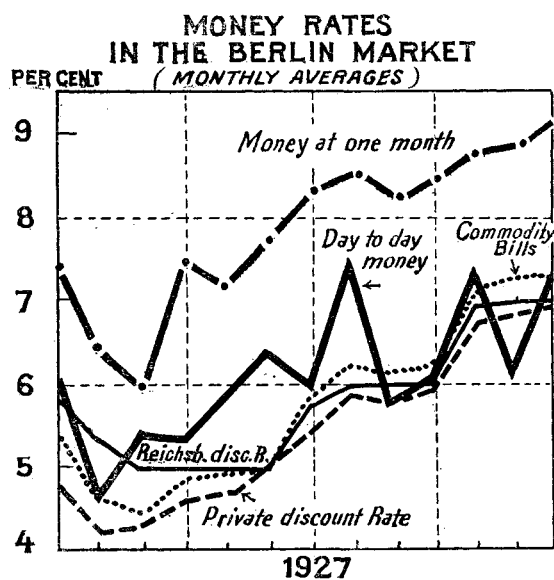


CHART I

marks on October 31, 1927. The demand for private discounts arose chiefly in connection with public funds administered by the Reichsbank. The rate fluctuated for the most part slightly below the Reichsbank rate, or now and then even reached that level for a short time. The rate for commodity bills with bank indorsement, which was often a merely nominal rate, was lower than the Reichsbank rate until about the middle of the year, and thereafter above it.

Domestic bill portfolio.—The volume of domestic bills, which during 1926 averaged 863,000,000 reichsmarks, rose considerably after February of last year, and since the end

of May amounted almost always to more than 2,000,000,000 reichsmarks; at the month's end in August, September, and October to more than 2,500,000,000 reichsmarks; and at the end of 1927 it had advanced to almost 3,000,000,000 reichsmarks. (Chart II.) Examination of the gross increase in domestic bills (Chart III) shows very clearly the extent of the demands made on the banks. The largest part of the

**MONEY IN CIRCULATION AND
REICHSBANK HOLDINGS OF GOLD AND FOREIGN EXCHANGE
AND DOMESTIC BILLS**

BILL. R.M. (END OF MONTH FIGURES)

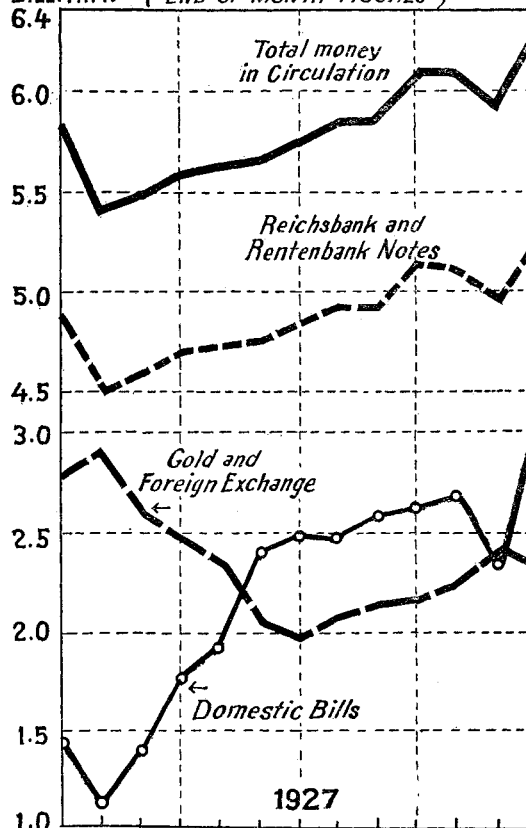


CHART II

bill offerings was made through the agency of banks and other financial institutions, while direct offerings by industry, handicrafts, commerce, agriculture, and other borrowers, in spite of a similar tendency to increase, declined in relative importance. The average maturities of discounted bills from the time of their purchase, moreover, were longer as compared with maturities of discounted bills in the year 1926.

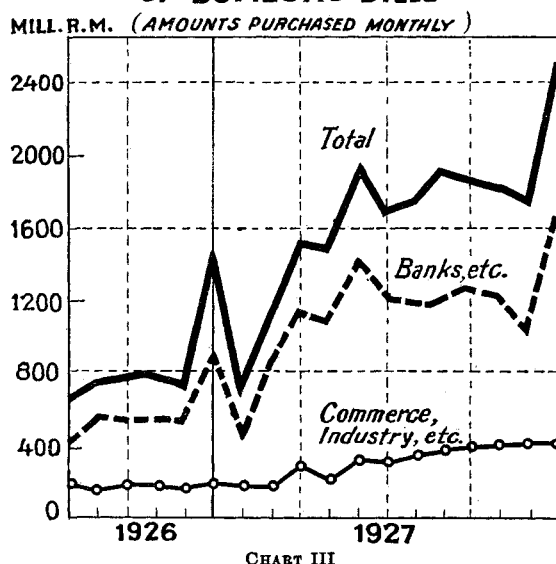
The credit operations of the Reichsbank were supplemented in a sense by the export

credits granted by the Gold Discount Bank. Since April, 1927, the latter bank has held bills in reichsmark currency as well as sterling and dollar bills. On the whole, however, the discount operations of the Gold Discount Bank were somewhat curtailed for the reason that the bank is gradually approaching its appointed end. It must also be borne in mind that the cooperation of the Gold Discount Bank in the administration of public funds will be discontinued within a measurable period of time after the plan of the Reichsbank to take over the management of these balances shall have received the general approval of the parties concerned. The business undertaken by the Gold Discount Bank at the beginning of

Nevertheless a unified management of all these balances for the benefit of the country as a whole continued to be essential. Unfortunately this matter is not yet seen by everyone in its true light. Short-term funds tend for the most part to seek investment in a central money market for the sake of the interest to be earned; the result is that even such important places as Frankfurt and Hamburg try with good reason to establish close relations with the Berlin money market. Only a central money market is in a position to distribute its available balances to all parts of the country. The Reichsbank has contributed to make this possible, especially through the establishment of clearing facilities by telegraph. By this means all unemployed balances are made available to the whole German business world; the entire administration of public funds is more rationally organized; and excessive hoarding and dissipation of reserves is avoided. This does not mean the withdrawal of funds from less important districts, but quite the reverse—namely, the possibility of placing at any time otherwise idle funds of the business world and of the Government wherever they are needed; in this way enabling local markets to participate in the advantages of the great central market. Germany is not rich enough to permit herself the luxury of uncoordinated employment of capital.

Foreign credit policy.—Considering the dearth of capital in Germany, the necessity of seeking foreign credits is admitted without further argument. So far as a satisfactory increase in production is the aim in seeking the assistance of foreign loans, no objections can be raised. This assumption can generally be accepted in the case of private business, which is faced with the necessity of calculating profits very closely. Naturally many objections arise in the case of private loans if they are employed to excess or in unproductive ways, especially in consideration of possible future changes in price levels and conditions of production. In the case of public organizations the same considerations do not always apply, owing to the special character of most of their operations and owing to the interplay of political factors. A most economical financial policy in general, and most careful management of public undertakings in particular, must therefore be constantly demanded. The effort which the *Beratungsstelle* (Loan Advisory Committee) under the direction of the Finance Minister of the Reich has been making in the direction of stern self-denial in respect to seeking new public loans abroad has strengthened the confidence

PURCHASES BY THE REICHSBANK OF DOMESTIC BILLS



1926—namely, the acceptance of 360,000,000 reichsmarks of agricultural 7 per cent mortgage bonds of the Rentenbank-Kreditanstalt with a maturity of three to five years—was almost completed at the close of the year under review, after a further sum of about 65,000,000 reichsmarks had been appropriated for agriculture in 1927, and the statutory limit had thus been almost reached. Of these mortgage bonds, 118,400,000 reichsmarks will mature on July 15, 1929; 118,600,000 reichsmarks on July 15, 1930; and 118,700,000 reichsmarks on July 15, 1931.

The volume of public funds declined considerably during the past year, and accordingly their importance for the money market and the discount policy of the Reichsbank diminished.

of foreign countries in Germany's financial policy. Self-discipline and self-denial in financial matters will be essential in the future also—all the more since the Agent General for Reparations in his latest report has revived the question of a precise definition of German reparation obligations. The close relationship which the solution of this problem bears to the currency question imposes new tasks of great difficulty and responsibility upon the Reichsbank.

Gold and foreign exchange policy.—The gold and foreign exchange policy of the Reichsbank was deeply influenced during 1927 by foreign credits. Rates of the dollar and of sterling fluctuated near the gold export point until the end of June. The causes for this lay especially in the temporary decline of the inflow of foreign capital and in the very unfavorable trade balance; the latter constitutes a problem of the greatest importance for the further economic development of Germany. The delivery by the Reichsbank of almost 1,000,000,000 reichsmarks in foreign exchange—and in gold also to a small amount—together with the inflow of short-term foreign credits, could not change the course of the exchanges. During the second half year the value abroad of the reichsmark rose again, especially as a result of the larger inflow of foreign loans. When, owing to this development the exchanges had declined almost to the gold import point, and the possibility emerged that foreign credits might come to Germany in the form of gold, the Reichsbank decided to reduce the purchasing price of gold to 2,784 reichsmarks.

Circulation and the price level.—A considerable increase in money in circulation, even though fully covered by gold, can not fail to have an unfavorable influence on the course of prices, which seems all the more serious because an advance in prices, even though it may have quite natural causes from the point of view of commodities and production, will be regarded generally among the population as a sign of inflation because of their previous experience. The situation of the reserves, therefore, can not and ought not to serve as the only standard for the guidance of the Reichsbank: in such case the Reichsbank would mislead business by the devious path of price advances and wage advances to a misconception of profits, and to unsound measures in the placing of their investments and the conduct of their business. The monetary circulation of any country should be maintained in well-balanced proportion to the volume of business

activity. It should be larger in periods of keen business activity than in quieter periods. For this reason the increase in the German monetary circulation which took place as a result of the improvement in economic conditions during 1927 is a case in point. The fact that the German price level showed a rising tendency during almost the whole of 1927—in direct contrast to the price movement in England, and except for the last month or two in the United States also—showed the need of checking any further expansion in circulation, and was a contributory cause of the autumn rise in the discount rate.

Gold imports.—Gold imports into Germany during 1927 amounted to 186,000,000 reichsmarks and gold exports to 9,000,000 reichsmarks, giving a net import of 177,000,000 reichsmarks. Of this amount, 133,700,000 reichsmarks came to the Reichsbank—45,000,000 reichsmarks being acquired by purchase during 1927, while the remainder was withdrawn from gold deposits held abroad and was therefore already in possession of the Reichsbank.

International clearing facilities.—The international clearing facilities arranged with certain foreign banks of issue toward the end of 1926 were extended to a larger number of foreign banks during the past year, so that by the end of 1927 similar arrangements were in force with 17 countries—Belgium, Denmark, Danzig, Estonia, Finland, France, Great Britain, Holland, Latvia, Lithuania, Norway, Austria, Sweden, Switzerland, Czechoslovakia, Hungary, and the United States of America. In practice the international clearance is used especially for the transfer of rather small individual accounts. During 1927 10,987 clearing operations were put through, in a total value of 39,000,000 reichsmarks.

Security and capital market.—After February the market for long-term securities with fixed yield showed increasing stringency. This was not only closely connected with the activity of the mortgage institutions and public organizations during preceding months—an activity which, being supported by an expansion in the volume of credit, had already to some extent anticipated future capital accumulation—but was also the result of the business revival. Even though figures for the issues for 1927, particularly for the first half of the year, indicate a fairly considerable supply of funds in the domestic capital market, they were nevertheless inadequate to meet the demand. Interest rates on the capital market continued to be unfavorable for borrowers. The 10 per

cent agricultural mortgage bonds of East Prussia, Saxony, and Schleswig-Holstein could, it is true, be converted at the beginning of the year at 7 per cent, but the average return of securities with fixed yield fluctuated almost continuously above 7 per cent; mortgage bonds with an interest rate below 8 per cent could scarcely be disposed of during the closing months of 1927. The demand on a great part of the savings of the German people for reparation deliveries is one of the chief causes of the higher level of interest in comparison with other countries which weighs so heavily upon German business.

On the security market the high level of prices prevailing until May was considerably influenced by the inflow of short-term foreign balances; but in addition the aftereffects of the inflation psychosis prevalent throughout the population and a temporary superabundance of credit facilities available for security purchases had the same effect.

Revision of balance sheets.—Negotiations between the Reichsbank and the banks and clearing houses with regard to improving and elaborating their published balance sheets led to the following result at the beginning of 1928: Instead of bimonthly, monthly condition statements are to be published; thus the interval between publications is shortened. The plan of the balance sheet has been revised in several particulars for the sake of more correct and more precise wording and form. The new form has been drawn up in such a way that it can be uniformly applied in the case of private credit banks, public banks, clearing houses, and mortgage banks. At the same time the Reichsbank came to an agreement with these institutions that a number of additional items should be included for the clearer interpretation of the entries shown on the condition statement.

ANNUAL REPORT OF THE BANK OF JAPAN

The annual report of the Bank of Japan for 1927, presented to the meeting of shareholders on February 18, 1928, contains the following sections dealing with financial and economic developments during the year:

General conditions.—The past year brought little improvement in general business conditions, which continued to be slack during the early months. Money had become easier since the preceding year with rates tending to decline still further, and the prospect seemed more favorable for proceeding with necessary business readjustments. Foreign-trade conditions proved less adverse than the year before. A marked recovery in the value of the yen brought exchange rates very near to par, while prices of some of the staple commodities were, if only slightly, upon the upward grade. The nation, however, had not fully recovered from the economic effects of the crisis of 1920 and the earthquake damage of 1923; and the persistent fall of commodity prices in 1925 and 1926, resulting from an improvement in the value of the yen, made itself keenly felt in our trade and industries. Although the probability of the removal of the embargo on gold exports had been increasing since the latter part of the preceding year, there were still disquieting factors of no little importance beneath the surface.

Banking panic.—Such was the state of affairs until March, when a deadlock in the debates in the Diet on the Government measures relating to the liquidation of the earthquake bills inci-

dentally disclosed the insecure position of a few banks. This was sufficient to arouse suspicion in the minds of depositors and to start a banking panic which resulted in the failure of such banks as the Tokyo Watanabe, the Nakai, the Murai, the Eighty-four, the Nakazawa, and the Soda. Some minor provincial banks also announced suspension of payment.

Meanwhile, the measures under discussion passed the legislature, and there was a temporary lull in developments; but the shock to the credit system was too great to pass so easily. Bankers became extremely cautious and were especially on their guard with such firms as Suzuki & Co. and affiliated concerns. On account of its close business relations with Suzuki & Co., the Bank of Taiwan was soon called upon to repay its short-term borrowings, while banks in the western Provinces suspected of similar relations suffered heavy withdrawals of deposits. As the Bank of Taiwan had no means of raising funds to meet its short-term loans, the Government, fearing serious credit disturbances as a consequence of the failure of this institution, drafted an emergency imperial ordinance authorizing the Bank of Japan to provide the Bank of Taiwan with such funds as it needed to tide over the situation. The Privy Council, however, rejected the plan on April 17—an action which was immediately followed by the closing of all branches of the Bank of Taiwan on the Main Island, and the subsequent failure of the Fifteenth Bank and the Omi

(as compared with 37,994,267 tons in 1927). Taking the franc value of imports and exports, total imports in 1928 amounted to 53,448,265,000 francs, an increase of 398,387,000 francs in comparison with the year before; exports, on the other hand, which amounted to 51,346,799,000 francs, showed a decline of 3,577,960,000 francs in comparison with 1927. This decline in the value of exports, which coincided with a considerable increase in the quantities exported, seems to be due to price reductions to which French producers who sell on international markets agreed for the sake of holding their own in markets which had been opened to them during preceding years. The increased value of exports is due chiefly to manufactured commodities.

It must, therefore, be regretfully admitted that the French trade balance was temporarily adverse in 1928; but it should be noted that since autumn our foreign trade has been making excellent progress, which has been uninterrupted during recent months.

Conclusion.—Gentlemen, we have tried before presenting detailed statistics of the opera-

tions of the bank, to explain as fully as the scope of this report would permit, the motives and the facts which justified the highly important monetary and financial decisions which we agreed to and promoted during the past year. We are fully convinced that these decisions were inescapable, and that they will benefit our entire national economy.

There is no way in which a nation can achieve permanent recovery and productive activity except by way of monetary security. Delivered from that uncertainty regarding tomorrow which paralyzes great initiative, discourages patient effort, creates the taste for speculation to the detriment of the spirit of enterprise—assured of being able, in short, to make either short-term or long-term contracts in francs with complete security, our country can face the future and prepare for it with confidence.

Our task at all times will be to make certain that the franc of 1928 shall remain, under the administration of the bank, a reliable instrument for the assistance of labor, production, and savings.

ANNUAL REPORT OF THE GERMAN REICHSBANK

The annual report of the German Reichsbank for 1928 was presented to the meeting of shareholders on February 4, 1929.¹ The portion of the report dealing with general economic and credit conditions follows:²

The halt which occurred toward the end of 1927 in the general economic improvement of Germany continued well into 1928, and then was succeeded by a gradual recession. The buying power of the domestic market was diminished by price increases, which in certain branches of industry were made with the primary purpose of holding down export prices. In spite of these and other measures tending to encourage exports, it was impossible, in the face of the unabated protectionism of other countries, to overcome the adverse German trade balance and achieve that substantial growth in exports which is so essential from the point of view of reparations policy. On several occasions wage disputes disturbed the labor situation and thereby interrupted the steady course of economic development; in November they reached their climax in the

lockout in the iron industry of northwestern Germany, which was finally ended through intervention by the Government. Once again for an entire year reparation payments have been discharged, not out of an economic surplus but out of borrowed funds, and the question becomes more and more serious how long this debt-incurring process can be continued and how far German business can bear up under credit conditions which in the course of the year have steadily become more unfavorable. The continuing high rates of interest cast their shadows over all German economic activity. They are among the principal causes of the difficult situation of agriculture. Furthermore, they have been an important factor in impairing credit conditions during the year, as reflected in the growing number of suspended payments and of protested bills, accompanied by extra-judicial settlements and reorganizations which to an increasing extent affect even the more important firms. If, on the whole, business has hitherto shown remarkable powers of resistance to adverse influences, that is primarily the effect of foreign credits, both long and short term, which have continued to flow into Germany in large volume.

Money rates.—The gradual recession of business activity was reflected but slowly in the condition of the money market. After the

¹ For earlier reports of the Reichsbank see FEDERAL RESERVE BULLETIN for May, 1928, 1927, 1926, etc.

² The full report contains, in addition, accounting details, several charts, and a brief discussion of changes of procedure in the Reichsbank transfer (Giro) system. The 1928 report has been issued in English, as well as in German. The official English version became available after the accompanying extract, translated from the German, was already in type, and was used in revising it.

heavy demands at the end of 1927 the customary dullness followed during the first six weeks of the new year. A subsequent revival carried interest rates to a high level, only slightly below that of the last quarter of 1927. Not until October did another period of inactivity set in. Chart I [omitted] illustrates the course of open-market rates in comparison with the Reichsbank discount rate. The general trend of the money market is reflected most clearly in the rate for month-to-month funds. This rate rose gradually from February until September and only during the last quarter showed a slight recession. The rate for day-to-day money also reflected the general tension of the money market, although subject to frequent fluctuations consequent upon influxes of short-term foreign funds. Throughout the year bank acceptances were in small volume. On these bills the rate was very close to the Reichsbank rate. From March to October the private discount rate fluctuated between $6\frac{1}{2}$ and $6\frac{7}{8}$ per cent; in November it declined somewhat, but remained above 6 per cent until the close of the year. To broaden the scope of the acceptance market, agreements which had already been in force for some time between the Reichsbank and a group of important acceptance houses in regard to the purchase and sale of acceptances and their rediscount by the Reichsbank were, at the suggestion of the Reichsbank, extended to a number of other first-class banking firms.

The more liquid condition of the bill market enabled the Reichsbank, acting for the Government, to place Treasury bills in the market from February, 1928, on. The rediscounting of these bills and their use as collateral for loans with the Reichsbank, as authorized by the bank-law amendment of July 8, 1926, was in very limited volume.

In contrast with the greater part of the previous year the Reichsbank, by maintaining its rate unchanged throughout the year at 7 per cent, found itself almost constantly in close relationship with the rate situation in the open market. The brief ease of the money market during January and February was very soon dispelled again by the customary spring demand for funds. The liquidity of the market, which became evident again after October, could not be regarded as adequate reason for a lowering of the Reichsbank rate, although this had been expected in many quarters. The demand upon the Reichsbank for credit, it is true, declined slightly; but total currency in circulation continued to show a gradual upward trend, since the decline in bill offerings

was more than compensated by accessions of gold and foreign exchange.

The Reichsbank rate for loans on securities remained unchanged throughout the year at 8 per cent.

The demand on the Reichsbank for discount of domestic bills was but slightly affected by the ease of the money market at the beginning of the year. The volume of domestic bills held by the Reichsbank was maintained with almost uniform monthly fluctuations at an average level of 2,000,000,000 reichsmarks. In the last quarter the volume declined and in November fell temporarily below the figure of 1,500,000,000 reichsmarks. The supply of bills brought to the Reichsbank originated for the most part with the banks and other financial institutions, which were responsible for the movement in the Reichsbank's holdings of domestic bills, while direct applications for discount accommodation from other sources—commerce, industry, agriculture, manufactures, and other applicants for credit—remained almost unchanged in respect to volume and maturity.

Public funds.—The so-called public moneys have become less disturbing as elements in bank policy by reason of the decline in volume of the funds involved. The departments concerned now manage with considerably smaller reserves, and have become convinced that the wishes repeatedly expressed by the Reichsbank regarding the investment of these funds are in every way to the interest of the public departments and accordingly of the public in general.

Reparations and foreign credits.—On August 31, 1928, the last of the four transition years under the experts' plan came to an end. The Agent General for Reparations has in each of his reports laid stress upon Germany's punctual and loyal execution of the plan. The Reichsbank also, to which special tasks were assigned in respect to reparations policy by the London Agreement, can claim on its part that during these four years it has done everything to facilitate the functioning of the plan without friction. During this period the German bank rate has at all times been higher than rates of other important banks of issue. Demands for foreign exchange made by the Agent General have in each case been satisfied by the Reichsbank in such manner that the open foreign exchange market has been in no way disturbed. Moreover, in general financial policy, the Reichsbank within its prescribed limitations has worked for economical administration. In particular it has insisted strenuously on the

employment of foreign funds in the most productive ways possible. During the transition years about 7,000,000,000 reichsmarks have come into Germany in the form of long-term foreign loans. Short-term foreign funds borrowed by German banking institutions are estimated at more than 6,000,000,000 reichsmarks. In addition, other branches of German industry have floated short-term foreign loans to obtain working capital. Finally, a very considerable volume of domestic shares, bonds, and other assets have been acquired in the course of these years by foreign purchasers. The effects of this foreign indebtedness have given a peculiar character to the development of German economy during these transition years. It would have been strange indeed if an artificially induced increase of capital in such considerable amount had not been reflected in expansion of plant and of consumption, in rising wages, in an increase of deposits with banks and savings institutions, and the like—expansions which are all the more striking if compared only with the years of extreme distress resulting from inflation, and not with normal years of peace. It is most urgent and important to determine whether this foreign indebtedness now and in future will contribute to the creation of an adequate German export surplus, from which not only the interest payments on outstanding foreign loans—amounting at present to about 1,000,000,000 reichsmarks per annum—but also the annuity payments under the experts' plan, can be made. Germany has every reason to be grateful to foreign countries for their assistance by means of credits. We are justified in adding that the credits which have been extended are, from the commercial standpoint, perfectly safe. A country possessed of such economic resources as those of Germany will always be able to make available a sum such as these credits represent—if necessary, through the sale of liquid assets. So long as the transfer protection provided in the experts' plan is continued, there need be no fear that private credits will be endangered. Transfer of previous annuities under the experts' plan, however, has been possible only with the help of foreign loans. It will, therefore, be necessary now that the four experimental years are past, to probe to the bottom of the question whether the situation will justify further transfers out of borrowed funds, in view of the fact that the experts' plan presupposed that transfers would be made in the long run entirely out of a surplus balance of payments.

The gold and foreign exchange situation during the year under review was also determined by the foreign credits. The dollar and the pound sterling were generally below parity as compared with the reichsmark; the sterling rate several times and for a considerable period even fell below the gold import point (to Germany). This situation led to substantial imports of gold, which the Reichsbank was obliged to take, inasmuch as the bank is legally obligated to convert gold bullion into reichsmarks at the rate of 2,784 reichsmarks per kilogram of fine gold.

The fundamental cause for the continued inflow of foreign capital is in last analysis the high level of German interest rates, which result from the disparity between domestic capital accumulation and capital demand. This disparity is made greater by the burden of yearly reparation payments in the amount of 2,500,000,000 reichsmarks. Germany, having lost her liquid capital during the inflation period, had no alternative but to float credits and loans as quickly as possible both at home and abroad if she wished to preserve her economic existence and at the same time discharge her heavy obligations toward her reparation creditors. This led to interest, amortization, and commission charges which for a country of such high cultural and economic development are without precedent, and will, if they grow in amount, become intolerable. These costs have already deprived large sections of industry of any opportunity for profit or for capital accumulation, and their payment up to the present time has been possible only because a constant influx of new foreign capital, accompanied by a steadily rising price level, has enabled current obligations to be met by new indebtedness. So long as it remains impossible to strengthen the productive capacity of industry, and at the same time reduce costs of production along all lines and lower prices, so that Germany can by increased exports and decreased imports discharge a reparation burden adjusted to her capacity to pay—after removal of the more onerous tariff barriers—the danger will still remain that capital charges will continue to rise in Germany, and will eventually reach a level far above any normal earning power of German industry.

The capital market.—The German capital market remained at high tension throughout the year. Complete exhaustion of the market was avoided by regular apportionment of demands over stated periods of time. De-

mands on the market so far exceeded its capacity that at times even first-class issues could be only partly absorbed. Only for mortgage bonds, which enjoy a traditional popularity, did the market show some absorptive capacity throughout the year. This, however, was undoubtedly due in considerable measure to foreign purchases, a statement which applies similarly to other domestic issues of the past year. Participation of foreign countries was especially marked in the issue of Reich railway shares, and later on also in a series of interim loans which were floated by German municipalities under very unfavorable conditions. The unsatisfactory situation of the market for securities bearing a fixed rate of interest is reflected in the actual yield, which has risen in comparison with the previous year, and terms of issue were considerably more unfavorable. Even borrowers of the highest standing had to pay 9 per cent or more for their long-term loans by reason of the discount at which the loan was issued.

The Reichsbank lent the market its support by means of various measures during 1928. In the case of loans against securities up to an amount of 50,000 reichsmarks, the Reichsbank removed the restrictions as to maturity which had been prescribed for credit institutions, so that loans of this character can now be placed with maturity up to the legal limit of three months. Some alleviation was afforded the market for Government securities by the creation of a banking consortium with the aid of the Reichsbank, the members of which pledged themselves to assume, without cost to the borrower, the guarantee required for the Reichsbank, under the bank law (section 21, subsection 3, last clause). Most important of all, it was possible for the Reichsbank, under authority of the law of December 21, 1927, to extend considerably the kinds of securities on which advances might be made, through the inclusion of a large part of the mortgage bonds and municipal bonds issued by semipublic credit institutions.