

Economic conditions

International environment

Developments in the global economy in 1998 were heavily influenced by the turbulence in the international financial and foreign exchange markets as well as by the crises in a number of countries. According to the December 1998 figures of the IMF (some of which are still estimates), growth in world trade decelerated in terms of volume from 10% in 1997 to 3½% last year. Global output increased by no more than 2¼%, compared with 4¼% in each of the two preceding years. The slowdown in the pace of expansion was particularly marked in the developing countries, being down from 5¾% in 1997 to 2¾% in 1998. At the same time, growth in the advanced economies, which account for the major part of global output, declined by just over 1 percentage point to 2%. In this group of countries, the United States (+4%) and the EMU member states (+3%) performed comparatively well. By contrast, the East Asian emerging economies as a whole, as well as Japan, suffered large losses in output. Despite the clear basic trend, the overall picture presented by the global economy currently comprises a quite heterogeneous range of countries and regions with marked differences in terms of their cyclical situation, the overall state of their economy as well as their specific, predominantly structural problems. Generalised statements all too easily obscure the fact that particularised responses are called for precisely where obviously difficult conditions exist.

*Growth in the
global economy
in 1998*

The hopes that the situation in the international financial markets would stabilise,

*New turbulence
in the financial
markets*

which had emerged last autumn, suffered a setback at the turn of 1998-9. This was mainly due to developments in Brazil, which also affected some other economies in Latin America. Furthermore, the collapse of an investment company in China led to a considerable unsettling of investors. The situation in the Russian economy, which has once again been undergoing a sharp contractionary process since summer 1998, is decidedly critical.

*First signs of
improvement
in East Asia*

By contrast, the central and east European countries in transition are in a remarkably robust condition. Also, in a number of East Asian countries the signs of improvement are now clearer than before. For instance, in Japan – which has a key role in overcoming the crises in East Asia – the reorganisation of the banking system is now gathering pace. In addition, the stimulus packages adopted in 1998 are now building up an initial expansionary impact. According to official sources, the South Korean economy is already pulling out of its trough and might achieve a growth in real GDP again in 1999. In other countries of this region, too, the economic outlook has brightened somewhat recently.

*Dampened
global outlook
for 1999*

Nevertheless, the events in Latin America and in China will not be without an impact on the volume of world trade and global output. All in all, 1999 will be a difficult year for the global economy. Even so, there is so far little to suggest that the entire global economy might slide into recession – as feared by some commentators. Firstly, despite the accumulation of risks and strains, the global dangers of contagion have not been virulent up to now. Secondly, the western industrial countries are

generating significant stabilising effects. These primarily include the continuing positive economic trend in North America and, with some qualifications, in western Europe, too. Moreover, the underlying monetary conditions in both regions are decidedly favourable. In addition, the international financial system as a whole seems to be much more robust at present than it was a year ago or at the outbreak of the crisis in Russia in summer 1998. Another factor is that the problems in Latin America do not appear to be as severe as they were in South-East Asia.

In Japan, the pace of the downturn appears to have slowed down recently. Seasonally adjusted industrial output in the fourth quarter was “only” slightly less than ½% below its level in spring, when it had been cut back very sharply. First of all, further progress has now been made in matching stockkeeping to lower final demand. Secondly, following a period of sharp decline, real exports picked up again slightly in the second half of the year. Above and beyond that, public investment expanded sharply in the final quarter of the year in connection with the extensive economic policy programmes adopted by the Japanese government last year. By contrast, private domestic demand was again on a downward trend. Private consumers’ propensity to consume was curbed, not least, by a further rise in unemployment, which – at a seasonally adjusted rate of 4.3% – reached a new all-time high in autumn of last year. The continuing decline in industrial fixed capital formation is due to the considerable under-utilisation of production capacities, the significant deterioration in enterprises’ profit-

Japan

ability and the lending restrictions (which have still not been overcome) on the part of the weakened banking system. Furthermore, the expected cyclical recovery is being made more difficult by the firming of the Japanese yen in the foreign exchange markets since the summer and the marked rise in capital market rates.

United States

In 1998, too, the US economy remained on a path of growth. According to initial estimates, real GDP increased in the fourth quarter of 1998 by 1½% in seasonally adjusted terms, and was 4% up on the year. A powerful stimulus was again imparted by private consumption, which benefited in turn from unbroken growth in employment, sharply rising real incomes (not least owing to the improvement in the terms of trade) and considerable price gains in the securities markets. The shortfalls in output due to the strikes in the motor industry in the summer of last year were subsequently made good, which likewise played a role as a special factor. Towards the end of the year, this led to correspondingly larger deliveries to customers. Expansionary impulses were also generated by private spending on housing construction, which was 12½% up on the year in the period of October to December. Furthermore, industrial firms' propensity to invest, which had slackened perceptibly in summer, picked up again. This is noteworthy in that the US export industry was severely affected by the decline in absorption in the regions in crisis.

However, the generally favourable picture presented by the US economy is clouded by the high foreign trade deficit which rose

again in the fourth quarter in terms of the real balance. Taken over the year as a whole, this is equivalent to a deficit of US\$ 241½ billion, or 3¼% of real GDP. A foreign trade situation of this kind, a large part of which is structural, harbours some problems insofar as it may lead to rigidities in the long run even in a strong economy like that of the United States. In the short term, however, accepting the high deficit in foreign trade has assisted the necessary restructuring in the countries in crisis and had a positive impact on the US price trend. Inflation at the consumer level, at 1.6% on an average of 1998, was at its lowest since the mid-sixties.

In contrast to the situation in the United States, there was a further slowdown in the pace of growth in the British economy in autumn. According to initial estimates, real GDP in the fourth quarter of 1998 rose by no more than ¼% in seasonally adjusted terms compared with the preceding period, and was hence 1½% higher than a year before. In autumn of last year there was a continuation of the downward trend in the real value added of British industry, which – on account of the high exchange rate of the pound sterling – had to cope with even sharper falls in foreign demand than, say, its competitors in the EMU member countries. However, this contrasted with contributions to growth by the services sectors which were again positive.

*United
Kingdom*

According to the revised figures of Eurostat, total output in EMU expanded quite sharply in the summer quarter (aggregate data for EMU are available up to that period) by a seasonally adjusted ¾% compared with the pre-

EMU

Capacity utilisation in the manufacturing sector in selected industrial countries

Seasonally adjusted figures in %

Country	Annual average for 1989–98	1997		1998			1999
		Total	Total	April	July	October	January
EMU ¹	81.7	81.3	83.2	83.4	83.7	82.8	81.9
of which							
Belgium	79.5	81.4	82.7	82.9	83.0	82.3	79.6
France	84.3	83.5	85.0	85.4	85.7	84.9	85.2
Germany	84.2	83.2	85.5	85.5	85.8	85.4	84.3
Italy	77.0	76.4	78.5	78.6	79.3	77.3	76.1
Netherlands	84.0	84.4	85.3	85.9	85.1	84.6	84.1
Spain	77.8	78.3	80.3	80.6	81.0	80.6	80.8
United Kingdom ¹	82.2	83.8	83.7	84.4	83.4	82.1	79.5
United States ²	81.2	82.0	80.8	81.7	79.8	80.4	...

¹ Source: EU business survey; weighted overall result of the country figures. — ² Source: Federal Reserve Bulletin.

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vious quarter, and by 2¾% compared with the corresponding period of 1997. During the autumn, the expansionary forces became noticeably weaker, however. This is suggested, at any rate, by a number of major indicators. Industrial output in October and November of last year, for example, was almost 1% down on the third quarter in seasonally adjusted terms. In addition, there was a further decline in capacity utilisation in manufacturing in January 1999; in seasonally adjusted terms, it was just under 2 percentage points below its peak of July 1998 and only slightly above its multi-year average. The business climate in industry has clouded over considerably in almost all the member countries. At least at first glance, this appears inconsistent with the fact that consumer confidence in autumn was still on an upward trend. The striking dis-

crepancy in these two confidence indicators is likely to be due, firstly, to the assessment of the global economic outlook, in particular, having a greater weight in the surveys of industry than it does in surveys of households. Secondly, the strains in the real economy, which the various regions in crisis are exerting on the euro area, have been felt so far mainly in industry. By contrast, the sentiment of households up to the end of the period under review is likely to have been influenced more strongly by the favourable effects on income owing, for example, to the sharp fall in prices for crude oil and the positive trend in employment in many parts of the EMU – the latter being made evident, above all, by a further decline in the seasonally adjusted number of unemployed in the euro area in autumn and by the fact that the standardised unemploy-

Expenditure of gross domestic product (GDP)

Adjusted for seasonal and working-day variations *								Germany	
Period	GDP	Domestic expenditure	of which			Net exports	Exports	Imports	
			Private consumption	Government consumption	Machinery and equipment				
at 1991 prices in DM billion									
1998 1st qtr	793.5	788.3	447.6	154.7	73.7	96.1	5.2	239.8	234.6
2nd qtr	793.8	785.7	445.8	154.0	72.1	90.0	8.1	246.1	237.9
3rd qtr	800.7	790.3	450.0	153.8	73.7	91.8	10.5	247.0	236.5
4th qtr	797.1	792.9	454.5	152.0	73.6	90.5	4.2	238.7	234.4
Change from previous quarter in %									
1998 1st qtr	1.4	1.8	0.8	3.8	7.3	-0.6	.	0.2	1.4
2nd qtr	0.0	-0.3	-0.4	-0.5	-2.2	-6.3	.	2.6	1.4
3rd qtr	0.9	0.6	0.9	-0.1	2.2	2.0	.	0.4	-0.6
4th qtr	-0.4	0.3	1.0	-1.2	-0.1	-1.4	.	-3.4	-0.9
at current prices in DM billion									
1998 1st qtr	933.5	917.2	533.6	177.8	76.3	109.8	16.3	253.7	237.4
2nd qtr	936.5	915.6	534.3	177.7	74.5	102.6	20.9	259.9	239.0
3rd qtr	945.1	923.0	540.4	177.5	76.3	104.7	22.1	259.9	237.8
4th qtr	941.7	923.3	545.3	175.0	76.1	103.1	18.4	251.8	233.3
Change from previous quarter in %									
1998 1st qtr	2.0	1.9	0.9	3.9	7.0	-0.8	.	0.2	-0.3
2nd qtr	0.3	-0.2	0.1	-0.1	-2.4	-6.6	.	2.4	0.7
3rd qtr	0.9	0.8	1.1	-0.1	2.4	2.0	.	0.0	-0.5
4th qtr	-0.4	0.0	0.9	-1.4	-0.3	-1.5	.	-3.1	-1.9

* Provisional figures. Fourth qtr 1998: Bundesbank's own calculations, some figures are estimated.

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ment rate was below 11% for the first time since the middle of 1993. The pace of inflation in the euro area decelerated further towards the end of the year. HICP inflation in December amounted to 0.8%. On an annual average, prices in 1998 were no more than 1.1% higher than in 1997.

Germany

Output and labour market

Overall growth

The German economy has lost momentum over the past few months, following a trend which had been positive for large parts of 1998 and – according to an initial calculation by the Federal Statistical Office – had led to a fairly large average annual growth in total

output of 2.8% compared with 1997. In autumn 1998, real GDP is unlikely to have matched its high level in the preceding three-month period; after adjustment for seasonal and working-day variations, the still-incomplete figures suggest a decline of ½% in the fourth quarter (see the explanatory notes on page 57). This was nearly 2% up on the figure for the corresponding period of 1997, i.e. much less than in the summer quarter, which had produced a growth of 2¾%. A similar picture is revealed if the first and third quarters (which were characterised by surges in growth) are combined with the periods of calm which followed each of them to form six-month periods. The resulting annualised rate of growth declined from just over 3% in the first half of the year to slightly less than 1½% in the second half.

*Retarding
factors*

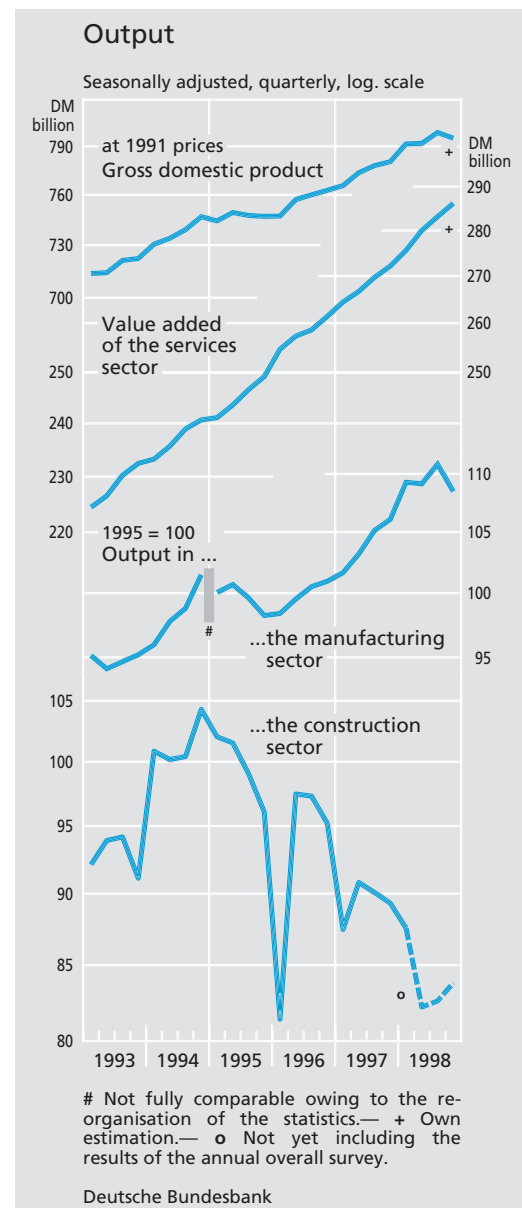
The slowdown was mainly due to the dampening effects on the international economy emanating, in particular, from the various regions in crisis around the world. It reflects not only the sharp downturn in demand in the countries affected but also their improved exporting ability. The fact that the situation is still unclear in some places probably likewise had an adverse impact on the general economic climate. German enterprises were less and less able to escape the shifts in the global current account structure and the influences dampening expectations. Furthermore, in Germany itself, a degree of uncertainty about how the underlying economic policy conditions will be set for the future and which course pay policy will take may have constituted an additional retarding factor.

*Industrial
output*

There was a perceptible fall in industrial output during the last few months of 1998. On an average of October to December, the decline in manufacturing amounted to a good 2%, seasonally adjusted, compared with the summer quarter. Growth in output when compared with the corresponding period of 1997 went down to just under 3%, having been nearly 5½% before.

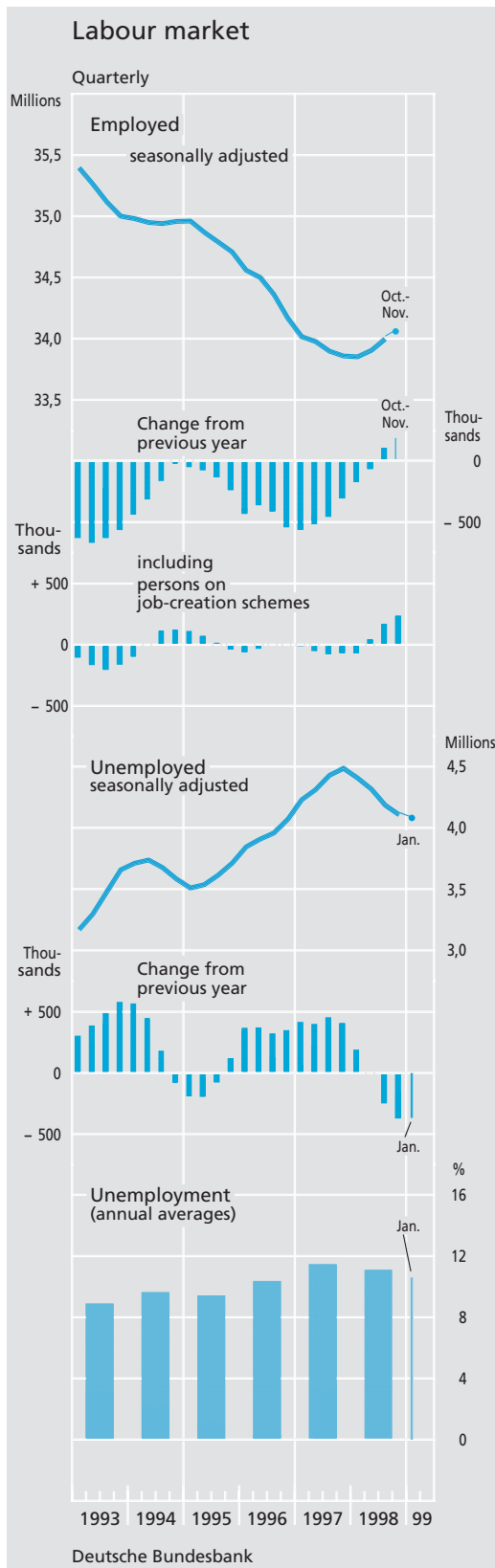
*Capacity
utilisation*

There was a simultaneous decline in the utilisation of available production capacity, which – according to the surveys of the ifo institute – was just over 1 percentage point lower in December 1998 than it had been three months previously. This likewise noticeably undershot the previous year's level. At the same time, an increasing number of firms assessed reserves of orders as being too low, whereas stocks of finished products were



often regarded as too large. This did not fail to have an impact on sentiment in industry. At the end of the period under review, both the assessment of the current situation and business expectations for the near future were more pessimistic than they had been in summer.

In the construction sector, the assessment of those enterprises surveyed about the situ-



ation and outlook was recently no longer as unfavourable as it had been, for example, in the past year. Even so, construction output was latterly well below its earlier level. In the fourth quarter as a whole, the decline amounted to around 6%. At present, there are no identifiable signs of this trough being overcome. By contrast, growth in the services sector is likely to have continued in autumn 1998, thus forming a powerful counterweight to the adverse trend in the producing sector and alleviating the decline in total output.

So far, the slowdown in overall growth has not had a perceptible impact on the labour market. Instead, according to the figures of the Federal Statistical Office, employment was, in fact, rising well into the autumn. In November – more recent data are not available at present – the seasonally adjusted number of employed was 34.1 million, i.e. 50,000 more than on an average of the third quarter, and around 175,000, or 0.5%, more than twelve months earlier. The increase in employment is likely to have continued especially in the labour-intensive services sector. This more than made up for restraint in recruitment in industry and shedding of labour in the construction sector.

Unemployment at the turn of 1998-9 was heavily influenced by differing weather conditions. The rise in November and December was due to the sharp onset of winter weather which resulted in many employees in outdoor occupations having to cease work earlier than would have otherwise been the case. Another factor was that the alleviating effects

Employment

Unemployment

Introduction of the new European System of National and Regional Accounts 1995 (1995 ESA)

As is customary in the Monthly Report for February, the present analysis is again based on the Bundesbank's own estimations of the national accounts for the final quarter of the preceding year. However, this is the last time that the concept of the accounts will follow the German system of national accounts based on the old 1979 ESA. At the end of April 1999 the Federal Statistical Office will, for the first time, publish quarterly figures for the national accounts in accordance with the rules of the 1995 ESA. These rules are binding for all EU member states. They were drawn up in close agreement with the 1993 System of National Accounts (SNA) of the United Nations and represent a far-reaching methodological revision of the previous framework.

The main aim of the 1995 ESA is to improve the comparability of key data within the EU and to make important statistical information available to the economic policy players more quickly than before. The new base year for prices will be 1995.

The new Europe-wide harmonised classifications prescribed in the 1995 ESA and the reorganisation of the sectors mean that there are major differences from the old concept in analytical terms. The corporate sector in Germany, for example, is defined less comprehensively than hitherto. In future, it will comprise only incorporated enterprises and quasi-corporations (such as limited partnerships (Kommanditgesellschaft, KG) and general partnerships (Offene Handelsgesellschaft, OHG)), whereas sole proprietorships, self-employed craftspersons and others are allocated with their entrepreneurial activities to the extended households sector. The previous special position of housing in Germany as a separate subsector of the corporate sector will no longer apply either. Residential building activities will now be allocated as a matter of policy to the respective domestic investors.

One of the reasons for the changes in the 1995 ESA is the extension of the concept of fixed capital formation. In future this will also comprise expenditure on intangible assets such as copyright and software that has either been acquired, or produced in-house. Furthermore, military installations which can be used for civilian purposes will no longer be recorded as intermediate consumption but as fixed capital formation, and – in contrast to the previous practice – consumption of public civil engineering projects is included. As a result of these changes, public consumption is increased on balance owing to additional consumption of public fixed capital formation.

A further adjustment concerns the calculation of households' savings. Savings is no longer the outcome of the difference between disposable income and consumption. Instead, company pension rights of households are also included – as in the approach already adopted by the Bundesbank. Moreover, the new definition of the households sector will probably lead to a saving ratio which tends to be lower.

Owing to these reclassifications and further changes in the 1995 ESA, it may be assumed that the level of German gross domestic product according to the new method of calculation will, in all cases, be shown as somewhat higher than hitherto. According to Article 8 of the ESA Regulation, however, national accounts data according to the old 1979 ESA will initially continue to be used for calculating both the own resources of the EU and the fiscal convergence criteria. A decision by the EU Council is needed for any amendment to the calculation of own resources. The deadline for determining the convergence criteria according to the old model is up to and including autumn 1999. As far as is ascertainable at present, the deficit ratio in accordance with the Maastricht Treaty is unlikely to change significantly in level under the 1995 ESA.

of labour market policy measures at the turn of the year were no longer as strong as they had been before, especially in eastern Germany. In January, when the weather was comparatively mild, seasonally adjusted unemployment went back down to 4.09 million. This was equivalent to a rate of 10.6%, and around 370,000 lower than the level in the corresponding period of 1998. At the end of January, 465,000 persons were on job-creation schemes and 375,000 were participating in vocational training courses. Together, this was almost 80,000 fewer than in autumn 1998.

Trends in demand

Manufacturing orders received

Demand for German manufacturing products slackened again perceptibly in the autumn months – it already having been the case in summer that not quite as many orders were received as before. In seasonally adjusted terms, there was a decline in the fourth quarter of around 3½% compared with the preceding period. This was the first time since early 1996 that the previous year's level had been undershot, in this case by just over 2%. By contrast, there had been an expansion of 2% in the third quarter of 1998 compared with 1997, and even one of slightly more than 7½% at the beginning of the year.

Foreign demand

Once again, foreign orders, too, showed a perceptible fall. After eliminating seasonal fluctuations, the decline in the last three months of 1998 came to just over 3½% when compared with the previous quarter. The figure was more than 4% below the

level of orders in the corresponding period of 1997.

The important group of capital goods producers, who generally have a strong international customer base and transact nearly 50% of their sales with other countries, were disproportionately affected by the further decline in demand. In autumn, seasonally adjusted orders for capital goods were 4½% down on the summer. When compared with the most recent peak in spring 1998, the decrease amounted to as much as almost one-tenth. Specifically, manufacturers of machinery and equipment (the part of the capital goods sector with the highest turnover) suffered a marked setback. By contrast, German cars continued to meet with a great deal of interest abroad, with the willingness to purchase them rising up to the end of the period under review. In the fourth quarter, orders placed for cars were slightly more than one-fifth up on the year.

The shifts in the structure of demand indicate that the international turbulence has mainly affected the propensity to invest abroad. Besides cuts in investment, a good part of this is likely to involve deferring the implementation of projects. Given that investment is generally fixed for long periods and the fact that fixed capital formation is irreversible, it appears that the increasing uncertainty is causing a number of enterprises abroad to take a cautious, waiting attitude. Even outstanding product quality and the fact that products remain competitive in terms of price (despite the adjustments that have occurred) cannot fully compensate for a situation of that kind.

Orders received in the manufacturing sector *

Change from previous year in %

Item	1997	1998	1998	
			3rd qtr	4th qtr
Total	6.4	3.0	2.1	-2.2
Domestic orders	2.0	3.6	4.2	-0.8
Producers of				
Intermediate goods	5.4	2.8	2.0	-2.2
Capital goods	-1.2	7.1	9.5	1.9
Consumer goods	-1.7	0.1	0.7	-1.6
Foreign orders	13.7	2.2	-0.9	-4.2
Producers of				
Intermediate goods	15.2	-1.7	-4.5	-8.1
Capital goods	15.8	4.4	-0.7	-4.8
Consumer goods	5.4	6.8	8.2	8.3

* Volume, adjusted for working-day variations.

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Domestic orders

In the last few months of 1998, domestic demand was no longer able to offset the decline in international business. In the fourth quarter, domestic orders declined, in fact, by a seasonally adjusted 3½%, having largely held up in spring and summer. The previous year's level was undershot slightly. In summer, however, domestic orders had been around 4% higher than a year before.

The slowdown was especially marked in durable and non-durable consumer goods; in addition to business in consumer electronics (which had been sluggish for some time), orders placed with motor vehicle manufacturers also flagged – at least for a while. Orders received by the producers of non-durables, which principally include food, drink and tobacco as well as the clothing industry, had

already been showing a year-on-year decline for some time.

The capital goods sector was likewise feeling the current slowdown in domestic demand. Global economic risks and home-made uncertainties in Germany played a part in this, although it still remains to be seen how long the retarding elements will have an impact. The gloomier climate for investment has already been reflected in deliveries to domestic customers. Although investment in machinery and equipment, which includes imported goods, rose by 7% over 12 months according to the Bundesbank's own calculations, it virtually stagnated at the level of the previous quarter in seasonally adjusted terms.

The increase in demand for construction work since early 1998 did not continue in autumn. Seasonally adjusted, orders received by the construction sector on an average of October and November – more recent data are not available at present – were more than 4% below the average of the preceding quarter. They were just under 3% up on the year.

Demand for construction work

The main reason for the recent renewed downturn in the overall trend was the perceptible restraint of many investors in the area of housing. Orders fell in the first two autumn months by just over one-tenth compared with the level in the summer. The year-on-year fall increased to around 5½%, having been no more than 1½% in the third quarter. The market continued to be depressed by an oversupply of apartment housing which meant that rent discounts tended

Housing construction



to be given to first-time tenants. Furthermore, the planned changes in the promotion of housing construction might have unsettled potential housebuilders. In eastern Germany, the cutback in tax concessions which came into force at the beginning of 1999 has evidently already had a retarding impact. At least, the seasonally adjusted 16% fall in orders in east Germany during the period under review was sharper than average.

In eastern Germany, there were also fewer contracts awarded for industrial construction than before. By contrast, building firms in western Germany benefited from orders commissioned by the railways and post office. For that reason, the trend in this sector was positive overall up to the end of the period under review. In the two autumn months, no stimuli were imparted by orders from the public sector, which fell to their lowest level in 1998.

Industrial and public construction

Households' consumption, income and saving

On balance, the level of consumption generated expansionary stimuli for the domestic economy. Overall, real consumption by households in the fourth quarter went up by 1% compared with the preceding three-month period after adjustment for seasonal and working-day variations. This was 2½% higher than the level in the corresponding period of 1997. In real terms, households spent virtually just as much on purchases from specialist dealers (excluding motor vehicles) in the period from October to November as they had done in the third quarter. Computer equipment was especially popular with buyers. In the fourth quarter, new registrations of private motor vehicles which originated from dealers' stocks likewise matched the very high level of the summer months. Services were in greater demand and there was a sharp increase particularly in budgets for holiday travel abroad. The fact that there was a further improvement in consumer expectations – in contrast to sentiment in some

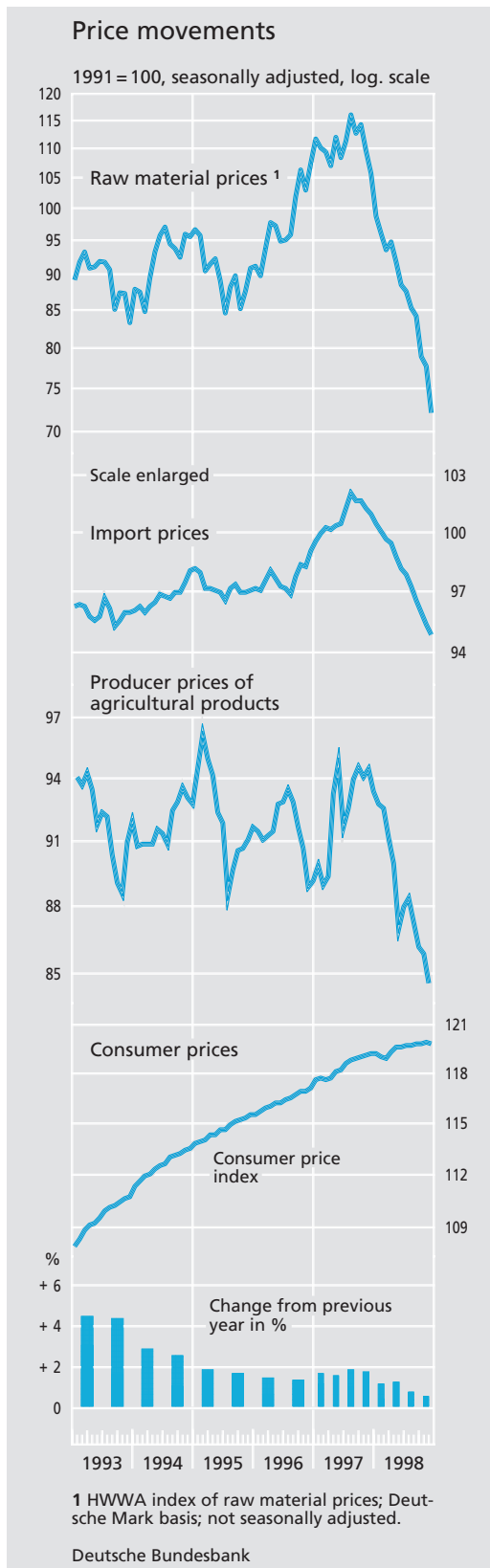
areas of business – is consistent with this picture.

The trend in income over the past few months has been marked by contrasting developments. In the last quarter of 1998, for example, there was a slight seasonally adjusted fall in total gross wages and salaries compared with the preceding quarter. The main reason for this was that less overtime was worked and remunerated recently. This was in contrast to the summer months when the motor vehicle industry, in particular, had shortened – or dispensed entirely with – the usual works holidays. Net labour income (i. e. after deduction of wage tax and employees' social security contributions) was $\frac{1}{2}$ % down on the third quarter in seasonally adjusted terms. At the end of the year, however, households were receiving somewhat higher payments than before from public cash offices. Including other income, which – in addition to property income – comprises self-employed persons' private withdrawals from entrepreneurial income (which have probably risen), households' disposable income went up by a seasonally adjusted $\frac{3}{4}$ % in the fourth quarter compared with the preceding three-month period. This was just over $2\frac{1}{2}$ % higher than in the corresponding period of 1997. The share of income that was saved was somewhat lower than in the summer months. Seasonally adjusted, the saving ratio – at $11\frac{1}{2}$ %, as it had been at the end of 1997 – was at quite a low level compared with earlier years.

That figure is also consistent with the private saving ratio on an annual average. Last year,

there was evidently a further slight decline in households' propensity to save. Admittedly, there were factors which acted as a strain on income, such as the increase in value added tax at the beginning of April 1998. On the whole, however, these were outweighed by the alleviating influences resulting from the lowering of the solidarity surcharge, the raising of the income tax payment threshold, and the positive effect of the terms of trade – in particular, the fall in oil prices. Furthermore, expectations with regard to an improvement in the labour market and income-supporting measures by the new Federal government are also likely to have encouraged a greater preference to consume.

The disparate pattern of private saving across the various groups of households, which had been discernible for some time, was also characteristic of their investment behaviour in 1998. Well to the fore were the acquisition of residential property and – in terms of financial investment – primarily assets with a potential for capital appreciation. So far, the stock market turmoil in the summer of 1998 does not appear to have had a strong overall adverse impact on the growing preference for shares. An estimated one-quarter of private funds might thus have flowed directly or indirectly into equities last year. However, the uncertainties triggered throughout the year by the various price fluctuations led to significantly higher private liquidity-holding at the end of the year.



Prices

The price climate in Germany remained very favourable at the turn of 1998–9. The year-on-year rate of increase in the consumer price index, which is usually regarded as a yardstick of general inflation, was no more than 0.5 % in December. The inflation rate is likely to have been the same in January 1999, judging by the results for a number of west German Länder.¹

Consumer prices

The rates of price increases are thus still within the range set by the stability policy-oriented objectives of the Eurosystem. There are no discernible inflationary dangers at present. At the same time, there are also no identifiable risks of deflation, even allowing for the fact that the official statistics probably overstate price increases somewhat. Although Bundesbank studies have indicated an average margin of error of up to $\frac{3}{4}$ percentage point, this should not be equated with a figure which is to be simply deducted automatically from the current rate of inflation.

The continuing fall in prices for mineral oil products had a significant dampening effect on the consumer price level well into December. The reduction in some prescription charges and a marked lowering of charges for telephone calls were the main factors in January. This contributed to what is likely to have been a smaller year-on-year difference

¹ For January, the Federal Statistical Office will not be publishing any figures using the current price index (1991 = 100). Instead, the introduction of a new index based on 1995 = 100 is planned for the end of February.

Consumer price index

Change from previous year in %

Item	1997	1998	1998	
			3rd qtr	4th qtr
Manufactured products	0.8	1.3	1.1	1.3
Energy sources	2.2	-3.2	-3.5	-4.8
of which Mineral oil products	2.7	-7.2	-7.8	-9.8
Services	2.3	1.3	1.0	1.1
Rents	2.7	1.7	1.6	1.6
Food	1.3	0.9	0.6	0
Total	1.8	0.9	0.8	0.6

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in the prices of services and of manufactured goods. Price rises in the case of industrial products remained at around 1%, one factor in this being the increase in the standard rate of value added tax on April 1, 1998. Accommodation costs were latterly about 1¼% higher than a year before. By contrast, the situation was eased by food being no more expensive at the turn of 1998-9 than it had been twelve months earlier. This was due, not least, to lower prices for pork, of which there was an abundant supply.

The dramatic slump in price in the international markets for crude oil, which also influenced prices for other sources of energy, was a major factor determining the recent trend in German import prices, too. Almost two-thirds of the 6% year-on-year decline in import prices in December was due to the energy component. But it was also only in a few cases – such as printed matter and glassware – that other imported goods were more expensive than a year before.

Import prices

At the end of 1998, German industrial producer prices undershot the previous year's level by a total of 1¾%. A large part of this was likewise due to "imported" price reductions, either because cheaper intermediates were bought in or because competitive pressure necessitated domestic price adjustments. It was only the capital goods sector that was still able to push through price increases in some cases. However, these were kept within narrow bounds and scarcely exceeded 1% in a year-on-year comparison.

Industrial producer prices

Construction work was no more expensive in autumn than it had been in the preceding months. The overall year-on-year construction price level – including value added tax – remained stable, too. Excluding the increase in value added tax on April 1, 1998, the previous year's level was undershot by ¾%.

Construction prices