european community
BACKGROUND INFORMATION
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BACKGROUND NOTE

No. 21/1976

May 12, 1976

COMMISSION AUTHORIZES ITALY TO APPLY MONETARY CONTROLS

The Commission of the European Communities has authorized Italy to apply stringent new monetary controls on foreign transactions to protect its currency from speculation on the international exchange markets.

On May 6, the Italian Government began a system of compulsory deposits in foreign exchange operations. This measure applies to Community members and non-Community members alike. On May 9, the Bank of Italy in a further move to defend the lira ordered commercial banks to cut the conversion time of foreign credits received into lira from 15 to seven days.

Community Aid to Italy

Theoretically, medium- and short-term Community aid equivalent to $3 billion is available to Italy under the EEC Treaty clause pledging members to give "mutual monetary support" to another member having balance-of-payments difficulties. This aid, if granted, would be in addition to medium-term Community assistance of $1.4 billion given December 17, 1974, and a $1 billion Community loan granted on March 15, 1976.

The March loan was made under the conditions that the central government would limit spending, the budget deficit, the financing of the deficit by treasury transactions, and credit, and the rise of incomes. Although this loan was also made with the understanding that Italy would not unilaterally take any commercial or financial measure that would restrict imports or subsidize exports, the Commission felt that economic events had overtaken this commitment and, therefore, authorized Italy's new deposit system.

Non-Interest Bearing Cash Deposit System

According to Italy's deposit system, whenever foreign exchange is purchased and whenever lire are deposited on foreign account, a non-interest bearing cash deposit in lire must be made with the Bank of Italy. The only major foreign exchange transactions exempted are those relating to the import of wheat. The deposit is 50 per cent of the amount of foreign exchange involved in the transaction. The deposit is to be released three months after its lodging date. The system will end on August 5, 1976.

This system contrasts with the one applied in 1974. In 1974, an import deposit system operated for a while, but it applied only to part of Italy's merchandise imports, with raw materials, energy, and capital goods exempted. The present system is general in scope and applies not only to merchandise imports but to every transaction involving the purchase of foreign exchange or the transfer of lire to a foreign account. The system should increase the cost of foreign exchange by forcing the operator to borrow money or dip into his own cash balances.

Some Monetary Events and Italy's Exchange Rates

The recent aggravation of economic and political uncertainties quickened the flow of funds out of Italy, draining reserves and forcing Italy into heavy borrowing. Concommitantly, Italy's exchange rate dropped from 686 lit. to the dollar on January 20 (the day before the exchange market closed temporarily) to 914 lit. to the dollar on May 5, a depreciation of about 25 per cent over three months.

Since the announcement of the new controls, the lire has appreciated by 11 per cent against the dollar.

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CORRECTION

In Background Note No. 2, line one, put a period after "airport" and delete to "thrust" in line 3. We regret that the statement is incorrect.