Monetary policy and banking business

Monetary policy and money market developments

ECB Governing Council cuts key interest rates to new all-time low

Against the backdrop of the persistently weak inflation outlook, on 5 June 2014 the Governing Council of the ECB adopted a package of monetary policy measures designed to help the inflation rate return to levels closer to 2% in the medium term. As part of this package of decisions, the Governing Council reduced both the interest rate on main refinancing operations and the rate on the deposit facility by 10 basis points. The main refinancing rate is now only 0.15% and the deposit rate -0.10%. At the same time, the interest rate on the marginal lending facility was lowered by 35 basis points to 0.40%. This means that the interest rate corridor set by the marginal lending rate and the deposit rate became symmetrical again, with a width of ±25 basis points around the main refinancing rate.[1]

The ECB Governing Council's interest rate decision was based on the view that annual HICP inflation was again lower than expected in May 2014 and that it would remain at low levels over the coming months, before increasing only gradually until the end of 2016. This is also indicated by the persistently subdued underlying monetary growth and the weak loan dynamics. At the same time, the Governing Council reiterated that ECB key interest rates would remain at present levels for an extended period of time. Accordingly, the Governing Council maintained the key interest rates in July and August that had been agreed in June.

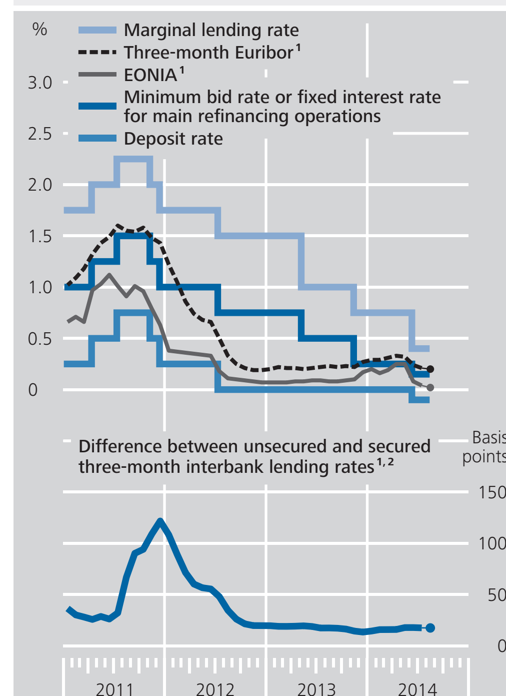
Negative rate on deposit facility for the first time

At -0.10%, the rate on the deposit facility became negative for the first time when key interest rates were lowered on 5 June. This interest rate also applies to banks' reserve holdings in excess of the minimum reserve requirements and certain other deposits held with the Eurosystem. The decision to forego a further reduction in the interest rate spread between the main refinancing rate and the deposit rate was intended to uphold the remaining incentives for money market activity, which have already been significantly reduced over the last few years through a gradual narrowing of the interest rate corridor.[2]

ECB Governing Council agrees on further unconventional measures

In addition to the interest rate cut, the ECB Governing Council agreed on a range of unconventional measures in June. In order to maintain a highly accommodative monetary policy stance and to keep possible fluctuations

Money market interest rates in the euro area



Source: ECB. 1 Monthly averages. 2 Three-month Euribor less three-month Eurepo. • Average 1 to 13 August 2014.
Deutsche Bundesbank

1 Traditionally, the width of the interest rate corridor in the euro area mostly stood at ±100 basis points around the main refinancing rate.
2 The width of the interest rate corridor determines the incentives for a horizontal distribution of liquidity among banks via the interbank money market; see also Deutsche Bundesbank, Implications of the Eurosystem's monetary operations during the financial crisis, Monthly Report, April 2014, pp 42-43.

Money market risk premia: indicators for the state of the interbank market

During the financial crisis, money market risk premia – measured as the spread between interest rates on risky, unsecured money market transactions between banks ("unsecured money market rates") and largely risk-free interest rates – came to be widely regarded as a barometer for the extremely tense atmosphere at times in the interbank money market. This article aims to shed greater light on both the different determinants behind risk premia and their dynamics over the course of different crises.

Money market risk premia: calculation and determinants

Normally, the three-month Euribor (Euro Interbank Offered Rate), a benchmark rate derived from survey responses from a panel of banks, is used as the unsecured money market rate for calculating money market risk premia in the euro area. Unsecured money market rates such as the Euribor include a credit risk component – if the borrowing institution is unable to repay the money market loan at the end of the agreed term, the creditor bank suffers a loss initially and can only hope to recoup at least some of the principal and interest payments in protracted insolvency proceedings. To aid panel banks in gauging the credit risk component involved in unsecured money market transactions, the European Money Markets Institute (EMMI; formerly Euribor-EBF), the body responsible for computing the Euribor, has specified that the quotes which panel banks submit in the daily survey of interbank deposit rates should be based on transactions between credit institutions of high creditworthiness (prime banks) for short-term liabilities.[1] So the Euribor is not a weighted average rate based on actual transactions but an average of assessments of the rates for typical transactions that the panel banks need not necessarily have entered into.

Usually, the money market risk premium is simply the difference between the three-month Euribor and an interest rate[2] that is largely risk-free (and thus considered safe) for the same term. This risk-free interest rate can be set in two different ways. The first is to use interest rates on secured money market transactions ("secured money market rates", or "repo rates"), with the Eurepo rate (which, like the Euribor, is survey-based and computed by EMMI) being a particularly common benchmark. The risk premium calculated using this particular reference rate is often referred to as the "depo-repo spread". Generally speaking, other available repo rates such as the Eurex Repo GC Pooling rate, which was introduced in October 2013, are equally suitable benchmarks for calculating risk premia. The second way to approximate the risk-free interest rate in the euro area is to use the EONIA swap rate[3] as the reference rate. Since the EONIA swap, by its very nature, can also be regarded as an overnight index swap (OIS), the risk premium thus calculated is often simply referred to as the "Euribor-OIS spread".

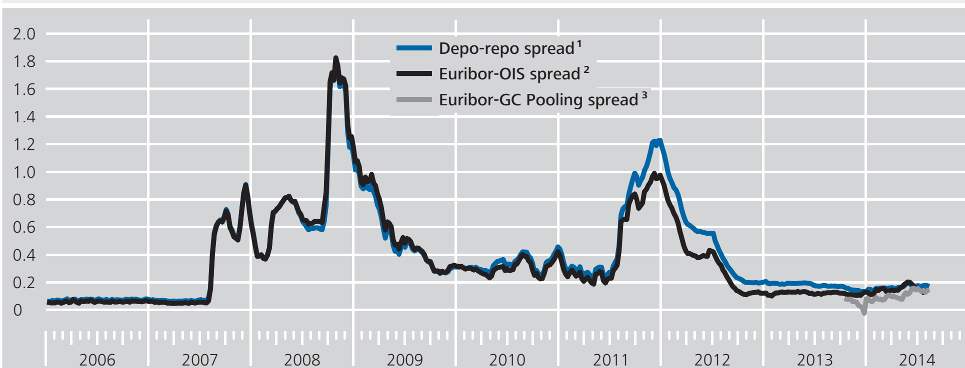
In a secured money market loan, the creditor has the option of realising the collateral provided if the debtor defaults. Should a default occur, the creditor only needs to assert its right of recourse against the debtor's insolvency estate if the proceeds from realising the collateral fall short of the interest and repayment. Credit risk is thus largely eliminated in transactions that are adequately collateralised. This explains why unsecured money market rates such as the Euribor are almost always higher than their secured counterparts.

Besides credit risk, money market risk premia also contain a liquidity risk component. The lending institution is exposed to liquidity risk in

1 See http://www.emmi-benchmarks.eu.
2 See also Deutsche Bundesbank, Interest rates in the repo market: approximation of short-term risk-free interest rates, Monthly Report, February 2014, pp 34-35.
3 EONIA swaps are hedging transactions in which a fixed interest rate (the swap rate) is "exchanged" for the unsecured interbank overnight rate EONIA for the term of the contract. No funds change hands, so credit risk is virtually non-existent. While it is true, in principle, that the EONIA rate used as the reference rate for the swap includes credit risk, this component can be disregarded for the most part.

Money market risk premia in the euro area

Percentage points, weekly averages



Sources: European Money Markets Institute (EMMI), Bloomberg, Eurex Repo; Bundesbank calculations. **1** Spread between the three-month Euribor and the three-month Eurepo. **2** Spread between the three-month Euribor and the three-month EONIA Swap Index (until 30 June 2014; from 1 July 2014: EONIA swap rate). **3** Spread between the three-month Euribor and the three-month repo rate.
Deutsche Bundesbank

as far as unexpected outflows of funds might force it to raise liquidity itself in the interbank money market and such liquidity might only be available at unfavourable conditions or not at all. This is why it makes sense for banks to add an interest rate premium to their loans if their own liquidity risk increases as a result. The liquidity risk component of secured money market transactions is likewise lower than it is for unsecured transactions because the lender has the option of using the collateral it receives as security when raising liquidity for its own purposes. In practice, it is virtually impossible to split the calculated money market risk premia into the two determinants credit risk and liquidity risk.

Money market risk premia over time

Before the onset of the liquidity crisis, money market risk premia normally amounted to just a handful of basis points. During this period, market players considered credit and liquidity risk in the interbank money market to be negligible. The outbreak of the liquidity crisis in August 2007 sent money market risk premia rocketing from their previous low levels, and they reached new highs when the financial crisis came to a head in autumn 2008. The raft of measures taken by central banks and governments throughout 2009 to tackle the crisis restored a degree of calm, but the spectre of renewed tension came back to haunt the money markets in 2010 when the sovereign debt crisis began to unfold. As it turned out, risk premia resumed their steep upward trajectory when the sovereign debt crisis flared up at the end of 2011 but fell short of the record levels posted in late 2008.

The decisions taken throughout this period by the ECB Governing Council to roll out additional monetary policy measures, the restructuring and recapitalisation of banks, most notably in the periphery of the euro area, the agreements of the European governments, and the first steps towards consolidating public finances in a number of euro-area member states are likely to have played a major role in the subsequent decline in money market risk premia, a process which continues to this day.

Even though a return to pre-summer 2007 levels appears unlikely at the current juncture, money market risk premia have been rather low of late compared with recent crisis years. Risk perceptions among market players still tend to vary, but the consensus view is that risk is much less pronounced, all the more so when the potential borrowing institutions of unsecured three-month funds conform with the EMMI’s definition of prime banks. However, unsecured transactions with a term of three months or more are still not quite as common as they were before the onset of the liquidity crisis. Those entered into at low rates comparable to the Euribor can be seen as indicating that the lender regards the borrower as highly creditworthy.

in the money markets in check, the ECB Governing Council extended full allotment in its monetary policy refinancing operations at least until the end of 2016. The latter objective is also served by the ECB Governing Council's decision to suspend the fine-tuning operations sterilising the liquidity injected under the Securities Markets Programme (SMP). The suspension of these operations will help to reduce fluctuations in the liquidity situation and thereby also in short-term money market rates.[3]

Targeted longer-term refinancing operations to strengthen lending to the private sector

In view of the continuously weak developments in loans to the private sector, the ECB Governing Council also decided to conduct a total of eight targeted longer-term refinancing operations (TLTROs). As banks used a large part of the funds they had borrowed at the end of 2011 and the beginning of 2012 in the two three-year longer-term refinancing operations (LTROs) to purchase government bonds,[4] the new operations are partly conditional on banks' past and future lending to the private sector.

In the first two auctions in September and December 2014, the participating banks will be entitled to borrow an amount equivalent to up to 7% of their outstanding volume of loans to the euro-area non-financial private sector as at 30 April 2014 (excluding loans to households for house purchase). Additional operations will be conducted between March 2015 and June 2016 on a quarterly basis, allowing counterparties to borrow up to three times the amount of their eligible net lending exceeding a benchmark. Different benchmarks apply depending on whether a bank exhibited positive or negative eligible net lending in the 12-month period to 30 April 2014.[5] As a result of this design, the refinancing volume obtained by banks in the TLTROs may exceed their positive eligible net lending. All TLTROs will mature in September 2018 and the interest rate for each operation lies ten basis points above the main refinancing rate applicable at the time of take-up.

Mandatory early repayments to strengthen lending incentives

To strengthen the incentive to expand lending activities, banks will be obliged to repay all borrowed funds in September 2016 if their total eligible net lending lies below the bank-specific benchmark in the period from 1 May 2014 to 30 April 2016. In effect, this mechanism sets certain incentives for banks to avoid negative net lending or lend in excess of their bank-specific benchmarks. However, it cannot entirely prevent the institutions from using some of the central bank liquidity that they have obtained to roll over market financing that is approaching maturity or purchase interest-bearing securities (including domestic government bonds), even though there are now fewer incentives to do so owing to the lower interest rates on such securities. The effects of the TLTROs must therefore be closely monitored so as to be able to counter unsound developments at an early stage and achieve the ECB Governing Council's objective of strengthening lending.

Preparatory work for potential ABS purchases intensifying

The ECB Governing Council also announced that it would preventively intensify preparatory work related to potential outright purchases of asset-backed securities (ABS). Under this initiative, the Eurosystem will consider purchasing simple and transparent ABS which are backed by claims on the euro-area non-financial private sector. The Eurosystem must ensure that such securities purchases do not mean that profits from lending business remain with the banks while risks and expected losses are shifted to the central banks, ultimately leaving the general public to shoulder the costs.

Given that the medium-run inflation outlook is currently appreciably below the Eurosystem's inflation target, the adopted package of measures is justifiable, on the whole. At the same time, there is a danger that the expansionary

3 See Deutsche Bundesbank, Monetary policy and banking business, Monthly Report, February 2014, pp 32-33.
4 See Deutsche Bundesbank, Substantial government bond purchases by Eurosystem and commercial banks, Monthly Report, May 2012, p 32; and Deutsche Bundesbank, Changes in bank holdings of domestic government bonds in the euro area, Monthly Report, November 2013, pp 31-32.
5 Additional details can be found in the ECB's press release of 3 July 2014.

Money market management and liquidity needs

The three reserve maintenance periods from 9 April to 8 July 2014 saw a marked increase in euro-area liquidity needs stemming from autonomous factors. Compared with the average figure for the March-April 2014 reserve period (€468.2 billion), the latter went up by €47.3 billion, to reach an average of €515.6 billion in the June-July 2014 reserve period. The autonomous factors were once again very volatile, ranging between €462 billion and €553 billion. The rise was attributable to higher general government deposits (on balance: +€36.2 billion) and an increased volume of banknotes in circulation in the euro area (on balance: +€19.7 billion). By contrast, the other autonomous factors (including net foreign assets) had a liquidity-providing effect overall (on balance: -€8.6 billion). The minimum reserve requirement had a slight liquidity-absorbing impact, increasing by €0.8 billion over the three reserve maintenance periods to €104.4 billion in the June-July reserve period (see table below).

The ECB Governing Council's monetary policy decisions of 5 June 2014 (see pages 29 to 48) had a marked impact on credit institutions' demand behaviour in the tender operations. In the June-July reserve period, during which the lowering of the key interest rates and suspension of the SMP liquidity-absorbing tender (Securities Markets Programme) became effective for the first time, a change in bidding behaviour could be observed. The maturity of the last SMP liquidity-absorbing operation resulted in inflows of funds to the banking system totalling around €109 billion (gross) on 18 June. This caused the banks to perceptibly reduce their demand in the main refinancing operations as well as their bids in the refinancing

Factors determining bank liquidity[1]

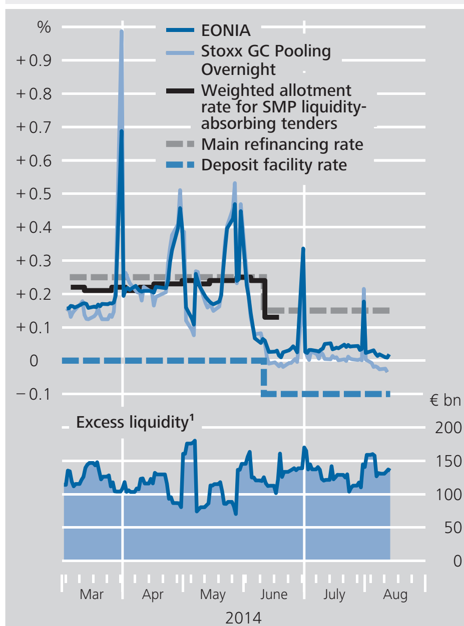
€ billion; changes in the daily averages of the reserve maintenance periods vis-à-vis the previous period

Item	2014		
	9 Apr to 13 May	14 May to 10 June	11 June to 8 July
I Provision (+) or absorption (–) of central bank balances due to changes in autonomous factors			
1 Banknotes in circulation (increase: –)	– 9.5	– 3.1	– 7.1
2 Government deposits with the Eurosystem (increase: –)	– 13.9	– 23.9	+ 1.6
3 Net foreign assets[2]	+ 17.5	+ 0.4	+ 3.2
4 Other factors[2]	– 22.9	– 1.6	+ 12.0
Total	– 28.8	– 28.2	+ 9.7
II Monetary policy operations of the Eurosystem			
1 Open market operations			
(a) Main refinancing operations	+ 22.7	+ 20.0	– 36.4
(b) Longer-term refinancing operations	– 15.0	– 11.8	– 47.7
(c) Other operations	+ 18.2	+ 19.7	+ 91.9
2 Standing facilities			
(a) Marginal lending facility	– 0.5	– 0.1	+ 0.0
(b) Deposit facility (increase: –)	– 0.5	+ 1.4	+ 4.4
Total	+ 24.9	+ 29.2	+ 12.2
III Change in credit institutions' current accounts (I + II)	– 4.0	+ 1.1	+ 22.0
IV Change in the minimum reserve requirement (increase: –)	+ 0.1	– 0.4	– 0.5

1 For longer-term trends and the Bundesbank's contribution, see pp 14• and 15• of the Statistical Section of this Monthly Report. 2 Including end-of-quarter liquidity-neutral valuation adjustments.
Deutsche Bundesbank

Central bank interest rates, money market rates and excess liquidity

Daily data



Sources: ECB, Eurex Repo and Bundesbank calculations. **1** Current account holdings minus the minimum reserve requirement plus the deposit facility.
Deutsche Bundesbank

operation with a maturity of one maintenance period which was conducted for the last time. Consequently, the net supply of liquidity was significantly lower, especially as, parallel to this, liquidity needs stemming from autonomous factors increased. Overall, the outstanding tender volume (excluding liquidity-absorbing fine-tuning operations) fell during the period under review, from an average of €640 billion in the March-April reserve period to €572 billion in the June-July reserve period, mainly on account of the early repayments of the liquidity provided in the three-year tenders (amounting to €81.7 billion). Following the general trend seen in previous reserve periods, the demand in the respective main refinancing operations increased just before the end of the month (reaching as much as €174 billion at the end of May), in order to prevent potential liquidity bottlenecks in the euro money market, which are associated with high funding costs. The propensity to lend to other banks at the end of each month seems to have tended to decline further owing to the greater priority attached to balance sheet policy.

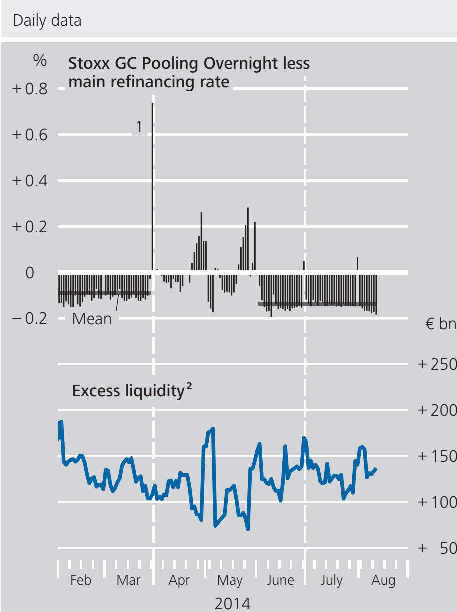
The balance sheet holdings of securities acquired through the purchase programmes fell further during the period under review in light of maturities and taking into account end-of-quarter revaluations. In the case of the two Covered Bond Purchase Programmes, CBPP1 and CBPP2, balance sheet holdings fell by €3.0 billion to €34.7 billion and by €0.4 billion to €14.1 billion, respectively. The balance sheet holdings of securities purchased under the SMP fell by €16.2 billion to €156.3 billion. The SMP liquidity-absorbing operations – which were conducted on a weekly basis until their suspension on 18 June 2014, and were intended to neutralise the impact of these purchase programmes on liquidity – consistently recorded underbidding from mid-April onwards. In addition to varying their demand in the main refinancing operations, credit institutions in the Eurosystem also used their level of participation in these fine-tuning operations to respond to the (expected) liquidity situation and manage their liquidity needs.

This behaviour was reflected in the level of excess liquidity. In the three reserve maintenance periods under review, the level of excess liquidity fluctuated greatly, ranging between €70 billion (end of May) and €180 billion (start of May), even though the respective averages for each reserve period (€117.4 billion, €116.6 billion and €133.7 billion) were relatively constant. Alongside the bidding behaviour in the tenders, major fluctuations in autonomous factors also impacted on the respective level of excess liquidity. The volatility of general government deposits played a particularly large role in this regard.

The correlation between overnight rates and the level of excess liquidity varied during the period under review. Although a distinct reduction in excess liquidity or a drop below €100 billion often resulted in an increase in the overnight rates, this phenomenon was less profound above all at the end of a reserve period. At the end of each month, the overnight rate was generally significantly higher than the main refinancing rate and increased by as much as 31 basis points (EONIA) or 20 basis points (GC Pooling Overnight, ECB Basket) compared with the previous day, even though credit institutions had in each case ensured that there would be substantially higher excess liquidity *ex ante* through their bidding behaviour in the tenders (see the chart on page 34). In the period prior to the lowering of the key interest rates, there had already been signs of a slight pick-up in the money market, such as a greater volume of longer-term repo transactions, which were also used to avoid negative interest rates. That the spread between the key policy rate and the secured money market rate has increased since 11 June, while the width of the corridor has remained unchanged (see adjacent chart), is also likely to be a consequence of the suspension of the SMP liquidity-absorbing tender. The average allotment rates of the latter (which in recent months have largely been close to the main refinancing rate) were a factor behind higher interest rates on overnight money.

Spread between Stoxx GC Pooling Overnight and the main refinancing rate, and excess liquidity

Daily data



Sources: ECB, Eurex Repo and Bundesbank calculations. **1** High spread on 31 March 2014 owing to end of quarter and quite low level of excess liquidity. **2** Current account holdings minus the minimum reserve requirement plus the deposit facility.
Deutsche Bundesbank

In the maintenance period July-August 2014, which followed the period under review, the money market rates were rather stable, with the exception of the month-end rate. While EONIA generally stood just a few basis points over 0.00%, the secured overnight money rate (GC Pooling, ECB Basket) was initially just above the zero percent mark, but dipped into negative territory towards the end of the reserve period. Thus excess liquidity – which also fluctuated greatly at times during this period, between €104 billion and €160 billion – hardly affected the overnight rates. It is also striking that daily use of the deposit facility almost never fell below €20 billion, despite these fluctuations in liquidity. Credit institutions' behaviour in terms of depositing money with the central bank followed a similar pattern during the three previous periods, too. Overall, the outstanding tender volume fell further to €521 billion on average (down by €50 billion on the previous period). In nominal terms, this was attributable not only to the early repayments of the liquidity provided in the three-year tenders (totalling €35.4 billion) and somewhat lower demand in the main refinancing operations, but also, *inter alia,* to the discontinuation of the maintenance period tender.

monetary policy will encourage excesses in the financial and real estate markets and reduce the pressure on fiscal policymakers to take action, which could cause euro-area member states' consolidation and reform efforts to flag.

ECB Governing Council decides to change monetary policy meeting schedule

The ECB Governing Council decided in July that its monetary policy meetings would be held in a new six-week cycle from January 2015. The reserve maintenance periods will also be extended to six weeks to match this new schedule. Starting with the January 2015 meeting, the ECB also intends to publish accounts of its monetary policy meetings. Meetings on topics other than monetary policy will continue to be held at least once a month.

Refinancing volume initially still trending downwards

From the beginning of the second quarter, the overall outstanding refinancing volume declined by just over €130 billion on balance to just over €500 billion at the current end. The reduction in the refinancing volume reflects, among other things, the above-mentioned decision to suspend the fine-tuning operations to sterilise the liquidity injected under the SMP. On balance, this decision enabled banks to scale back their demand for liquidity from the Eurosystem without this causing a strong decline in excess liquidity and an increase in money market rates. The falling demand for central bank loans was also reflected in continued repayments of the funds provided in the three-year LTROs in the amount of €120 billion. Through early repayments, institutions have thus already managed to redeem almost two-thirds of the just over €1 trillion which they originally borrowed in the two three-year LTROs a good few months before these operations mature.

Short-term money market rates show clear reaction to ECB Governing Council decisions

The fluctuations in short-term money market rates – which were already observed in the preceding months – due to the sometimes relatively volatile liquidity situation initially continued in May but eased considerably in June following the decisions of the ECB Governing Council. In particular, the decision to maintain the spread between the interest rates on the main refinancing operations and the deposit facility and to suspend the fine-tuning operations to sterilise liquidity injected under the SMP is likely to have played a major role in the fact that the key interest rate cut of ten basis points was reflected – in some cases to a slightly disproportionately large extent – in short-term money market rates. Whereas the EONIA – the overnight reference rate for unsecured lending transactions in the interbank market – has generally only just remained in positive territory since mid-June due to the rate on the Eurosystem deposit facility being negative for the first time, interest rates on secured overnight interbank transactions were slightly negative at times, depending on the individual banks' liquidity positions. On the whole, short-term money market rates have fallen back to levels further below the main refinancing rate since the measures were introduced.

Monetary developments in the euro area

Macroeconomic setting

The slight macroeconomic recovery in the euro area, which first took hold in the middle of last year, seems to be gradually having an effect on lending, although heterogeneity in the euro area remains high. One indication of this is that net lending to the euro-area private sector was slightly positive in the spring quarter for the first time in two years, with lending to non-financial corporations – while still negative – gaining some upward momentum compared with preceding quarters. Securitised lending to the private sector was also up somewhat, following sometimes strong outflows in the previous quarters. Against this backdrop, the slight upward trend in monetary and credit growth that could already be seen in the previous three-month period continued in the reporting quarter. However, it is too early to speak of a broad-based recovery in lending activities.

M3 growth still driven by overnight deposits

Supported by continuing inflows of funds from abroad and the upward trend in lending to the private sector, the pace of monetary growth accelerated markedly in the spring months.

Consolidated balance sheet of the MFI sector in the euro area*

Changes in € billion, seasonally adjusted

Assets	2014 Q2	2014 Q1
Credit to private non-MFIs in the euro area	– 34.9	– 28.2
Loans	– 41.4	– 10.0
Loans, adjusted 1	10.5	– 7.3
Securities	6.5	– 18.2
Credit to general government in the euro area	– 34.4	17.2
Loans	– 13.1	20.4
Securities	– 21.4	– 3.2
Net external assets	90.6	79.6
Other counterparts of M3	– 53.1	– 17.8

Liabilities	2014 Q2	2014 Q1
Central government deposits	16.1	1.1
Monetary aggregate M3	72.9	43.3
of which: Components		
Currency in circulation and overnight deposits (M1)	54.9	89.3
Other shorter-term bank deposits (M2-M1)	15.7	– 23.9
Marketable instruments (M3-M2)	2.3	– 22.1
Monetary capital	– 68.9	9.2
of which		
Capital and reserves	7.1	54.7
Other longer-term financial liabilities	– 76.0	– 45.5

***** Adjusted for statistical changes. **1** Adjusted for loan sales and securitisation.
Deutsche Bundesbank

This expansion again primarily affected overnight deposits, which benefited from the ongoing fall in interest rates on other deposits. However, unlike in the previous quarters, the other components of M3 also recorded slight inflows on balance in the reporting quarter.

Slight upward trend in monetary and credit growth

Against this backdrop, the slight upward trend in monetary growth that could already be observed in the previous three-month period continued in the reporting quarter. Annual M3 growth rose perceptibly from 1.0% at the end of March to 1.5% at the end of June, influenced in part by a base effect. At the same time, the annual growth rate (adjusted for loan sales and securitisation) for loans to the euro-area private sector, which had stood at -2.0% at the end of the previous quarter, increased clearly to -1.1%. Although the gap between monetary and loan growth has thus narrowed discernibly, it remains large by historical standards. Despite the tentative signs of recovery, underlying monetary dynamics continue to be very subdued.

Decline in loans to non-financial corporations slowed further

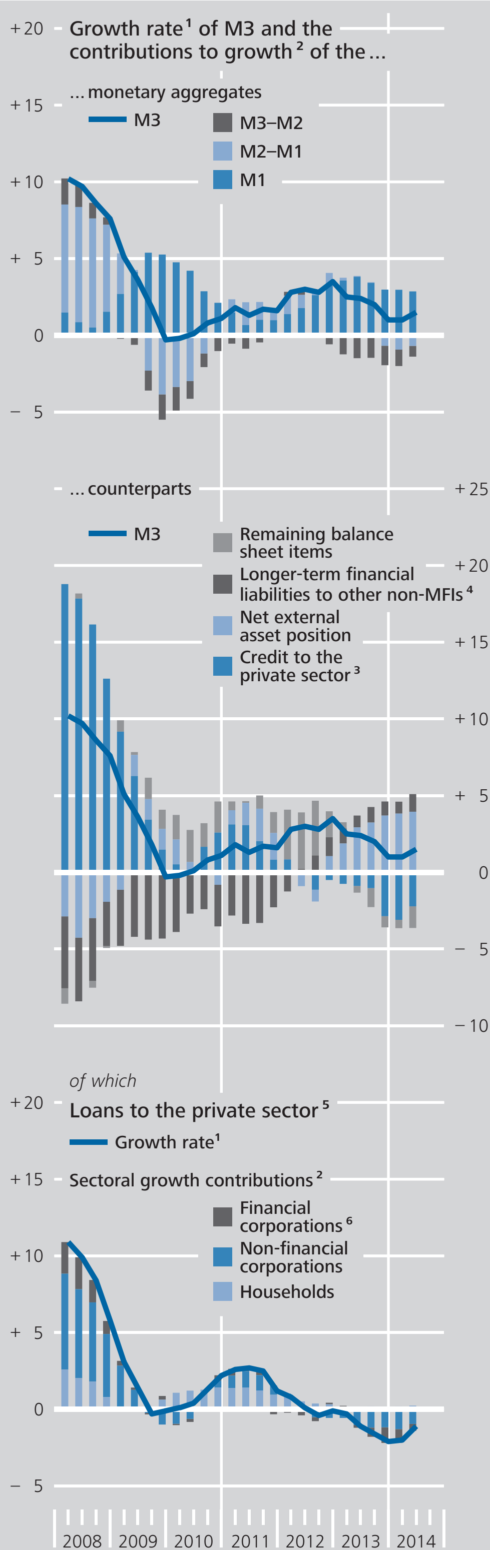
After their volumes had declined for two years, loans to the euro-area private sector were slightly up again for the first time on balance in the spring months. The improvement on the previous quarter was essentially attributable to the non-financial corporate sector, where the decline once again weakened considerably in the second quarter. The recovery in lending, which began in summer 2013, led to an increase in the annual growth rate for loans to non-financial corporations from -3.1% in March to -2.3% in June.

According to BLS, standards for loans to enterprises largely unchanged; the same applies to the demand for loans

The bank lending survey (BLS) conducted in the second quarter likewise provided indications of a gradual stabilisation in the non-financial corporate sector. As in the preceding quarter, the surveyed euro-area banks reported a virtually unchanged demand for loans to non-financial corporations. This meant that the decline in non-financial corporations' demand for bank loans recorded since the third quarter of 2011 had come to a halt. At the same time, the participating institutions largely kept credit standards for loans to enterprises at the level of the previous quarter in net terms.

Slight upward trend in credit growth despite heterogeneity in all four large euro-area countries

Whereas heterogeneity in the development of loans to non-financial corporations in the euro area remained high at country level, all four large member states recorded a slight upward trend in credit growth (see the chart on page 39). French and for the first time also German banks reported discernibly positive quarterly inflows. Although lending to non-financial corporations continued to decline on balance in Italy and, above all, Spain, the pace of reduction slowed



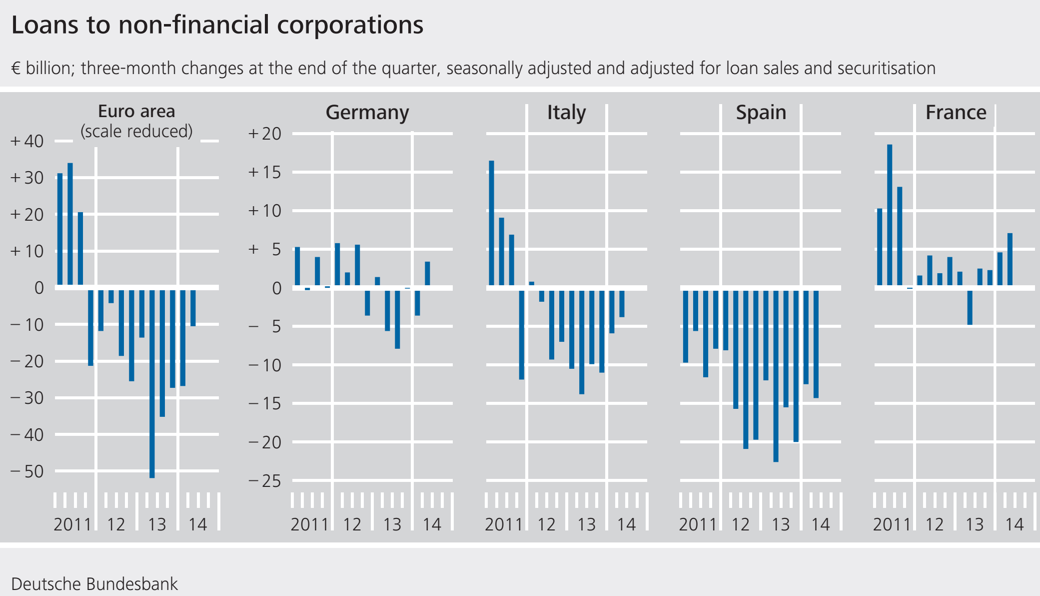
Source: ECB. **1** Year-on-year percentage change. **2** In percentage points. **3** Adjusted for loan sales and securitisation. **4** Denoted with a negative sign because, taken in isolation, an increase curbs M3 growth. **5** Adjusted for loan sales and securitisation from 2010 Q1. **6** Non-monetary financial corporations.
Deutsche Bundesbank

in the last four quarters. In the case of Germany and Spain – less so for France and Italy – this is attributable to the economic recovery, which – with a typical lag of a few quarters – ought to boost lending to non-financial corporations. The fact that Italy has slipped back into recession could represent a risk for its future loan growth; by contrast, in Spain the positive influence of the business cycle is tending to be overshadowed by the persistently high need for deleveraging in the non-financial corporate sector. In the four large member states (as in the euro area as a whole), the demand for loans may also have been dampened, as in the previous quarters, by the fact that non-financial corporations partially replaced bank loans by making greater use of internal financing or – in light of the favourable financing conditions for enterprises at present – by raising funding directly on the capital markets.

Slight increase in loans to households

Loan growth in the second quarter was mainly supported by loans to financial corporations, which continued the moderate rise registered in the previous quarter. Loans to households in the euro area continued to increase at a weak annual growth rate of 0.5%; the main drivers of growth in the second quarter were once again loans for house purchase.[6] Here, too, there was persistent heterogeneity across countries. The moderate increase in the euro-area aggregate masked a more pronounced increase in loans for house purchase in the euro-area core countries, while the periphery countries saw a further decline on account of the existing need for household deleveraging. For the euro area as a whole, the banks surveyed as part of the BLS reported a slight easing of credit standards for housing loans, which is likely to have supported lending across the euro area. At the same time, the surveyed

6 Unlike the aggregate of loans to households, the time series for housing loans to households is not adjusted for loan sales and securitisation. This explains why a large-volume securitisation operation in France in May created a downward bias in the figures on loans for house purchase in the euro area for the second quarter of the year, while the aggregate of loans to households exhibited no irregularities.



Loans to non-financial corporations

€ billion; three-month changes at the end of the quarter, seasonally adjusted and adjusted for loan sales and securitisation

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banks recorded a noticeable increase in the demand for loans to households for house purchase, which they perceived to be as strong as it last was at the end of 2010.

In keeping with the moderate increase in nominal private consumption expenses, consumer credit has been moving gradually upwards since the end of 2012, and this continued in the reporting quarter despite slight net outflows. The upward trend in this credit segment is reflected in the BLS. The surveyed banks reported that demand for consumer credit in the euro area had risen markedly in the second quarter for the first time since the beginning of 2007, while credit standards remained virtually unchanged.

Marked expansion in net external asset position

Besides the upward trend in loans to the private sector, monetary growth in the reporting quarter was again supported, above all, by the inflow of funds from abroad, which was reflected in a significant expansion in the MFI sector's net external asset position.[7] The available data suggest that this was attributable in equal measure to the persistent current account surpluses in the euro area and inflows from portfolio transactions with non-residents. As in the previous quarters, the latter are likely to have been driven primarily by foreign investors' strong demand for euro-area securities. The resulting inflow of deposits into the euro area was only partially counterbalanced by domestic non-MFIs' continued purchases of foreign securities.

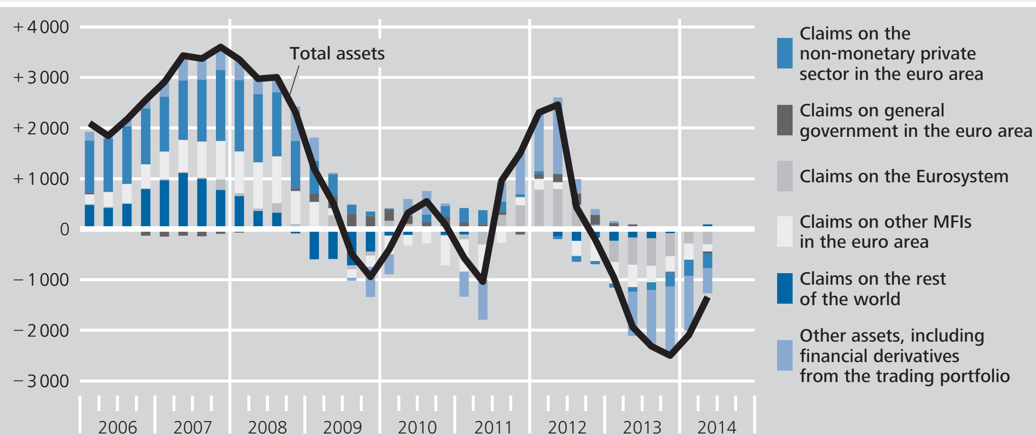
Monetary capital down considerably, but with only a partial influence on the monetary aggregate

Monetary growth in the reporting quarter was also supported by the decline in monetary capital. This was largely attributable to strong outflows from long-term time deposits. Given that these outflows were, to a large extent, the result of securitisation transactions in France being liquidated and that such transactions simultaneously lead to a corresponding decline in securitised lending to the private sector, they had no net impact on M3, however. Besides the liquidation of time deposits, the reduction in long-term bank debt securities with a maturity of over two years continued as well. Despite the – in some cases distinct – improvements in placing longer-term bank debt securities reported by institutions participating in the BLS, outflows were recorded in this area by Ger-

7 The reporting quarter was characterised by two large-scale special factors, which did not have an impact on M3 on balance and are therefore disregarded when interpreting M3 developments. In April, long-term time deposits and securitised lending to the domestic private sector (see also the next paragraph) experienced extensive declines as a result of the liquidation of credit securitisation transactions in France. In May, a securitisation transaction in France led to a sharp decline in loans to households for house purchase, while securitised lending to the domestic private sector posted an increase (see footnote 6).

Balance sheet assets of euro-area banks*

12-month changes[1] at the end of the quarter, in € billion



* Including money market funds. **1** Adjusted for statistical changes.
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man, Spanish and Italian banks in particular. This suggests that bank-side factors continue to play a role in this context, too. In addition to some credit institutions requiring little funding on account of deleveraging, a key bank-side factor is that banks have been substituting bank debt securities with alternative sources of financing, such as Eurosystem liquidity provided on favourable terms as well as deposits, which are continuing to grow. This is consistent with the fact that the banks surveyed in the BLS reported improved access to funding in the form of deposits and via the money market.

Net decline in asset items weakened considerably

The net decline in asset items on bank balance sheets observed in 2013 weakened significantly (measured in terms of 12-month changes) for the first time in the reporting quarter. This is generally consistent with the results of the latest BLS, in which the surveyed banks indicated that the reduction in risk-weighted assets owing to the new regulatory and supervisory actions had come to a halt in the first half of 2014. By contrast, banks continued to strengthen their capital position. The slowdown in deleveraging was mainly attributable to items which have little or no influence on monetary developments (see the chart above). In particular, the strong reduction in financial derivatives in the trading portfolio – which had emerged in 2013, notably because of the tightening of regulatory banking standards – weakened in all four large euro-area countries. Furthermore, there was a slowdown (with the exception of Italy) in the reduction in claims on other euro-area MFIs, which is likely to be linked to the improved level of confidence now placed in the periphery countries and the euro area as a whole again. Focusing only on the counterparts of M3 contained in the asset items, balance sheet reduction continued in Spain and Italy. In these two countries, claims on the rest of the world and the euro-area private sector decreased by a smaller margin than in the previous quarter, yet banks intensified their reduction of securitised lending to the public sector. By contrast, the counterparts of M3 contained in the asset items increased slightly in Germany and France towards the end of the second quarter, which was essentially attributable to claims on the rest of the world.

German banks' deposit and lending business with domestic customers

The increase in German banks' deposit business amidst a simultaneous shift towards shorter-term deposit types continued in the second quarter of 2014. As in the euro area, it is likely that the renewed overall decline in the

Deposit business continues growing and is almost entirely attributable to overnight deposits of households

interest rate spread between deposits of different maturities combined with the marked preference of investors for liquid assets contributed to this. The decline in longer-term deposits mainly affected long-term time deposits, while increases in the shorter-term segment were primarily driven by an increase in households' overnight deposits. Besides the low interest rates on alternative secure deposit types, the continued attractiveness of overnight deposits in the reporting quarter may have been encouraged by discussions about potential excesses in the stock markets and about the level of guaranteed returns in insurance policies. Compared with the increase in households' overnight deposits, the other movements in shorter-term deposits were almost negligible. Non-financial corporations increased their overnight deposits to a far lesser extent in the second quarter of 2014; short-term time deposits and savings deposits across all sectors rose only slightly at most.

Longer-term deposits again reduced mainly by financial corporations

The main factor behind the reduction in the longer-term maturity segment of domestic banks' deposit business in the reporting quarter was the renewed distinct decline in the long-term time deposits of financial corporations, especially insurance companies and pension funds. As in the previous quarters, these professional investors are likely to have shifted the freed-up funds towards less liquid and riskier assets outside M3 in search of higher yield. Moreover, households likewise continued to reduce their long-term deposits.

Bank loans to domestic non-banks clearly on the rise and driven by the non-financial private sector

Compared with previous quarters, German banks' lending business expanded significantly in the second quarter of 2014, although this was solely the result of an increase in loans to private non-banks. Banks in Germany upped their holdings of securities issued by private domestic entities and increased their private-sector lending, particularly to the non-financial private sector.

As regards loans to households, the positive development seen in the previous quarter continued. Loans for house purchase were once again the main driver of growth, with their rate of increase continuing to accelerate somewhat. This development is broadly consistent with the information provided by the institutions surveyed in the BLS, which indicates that demand for loans to households for house purchase again rose moderately in the second quarter of 2014, even though the rise in demand was perceptibly weaker than in the preceding quarter. According to the bank managers surveyed, this development was fuelled by both optimism on the part of borrowers regarding housing market prospects and consumer confidence, which had risen again slightly.

Growth in loans to households continues to be driven by loans for house purchase

Lending and deposits of monetary financial institutions (MFIs) in Germany*

Changes in € billion, seasonally adjusted

Item	2014 Q1	2014 Q2
Deposits of domestic non-MFIs[1]		
Overnight	20.4	22.2
With agreed maturities		
of up to 2 years	9.6	0.4
of over 2 years	− 7.6	− 9.1
Redeemable at notice		
of up to 3 months	− 3.2	1.6
of over 3 months	− 0.3	− 0.8
Lending		
to domestic general government		
Loans	− 1.2	− 6.5
Securitised lending	− 2.0	4.7
to domestic enterprises and households		
Loans[2]	2.9	9.3
of which to households[3]	5.6	5.8
to non-financial corporations[4]	− 4.8	4.0
Securitised lending	− 1.1	10.4

* As well as banks (including building and loan associations, but excluding the Bundesbank), monetary financial institutions (MFIs) here also include money market funds. End-of-quarter data, adjusted for statistical changes. 1 Enterprises, households and general government excluding central government. 2 Adjusted for loan sales and securitisation. 3 Including non-profit institutions serving households. 4 Corporations and quasi-corporations.

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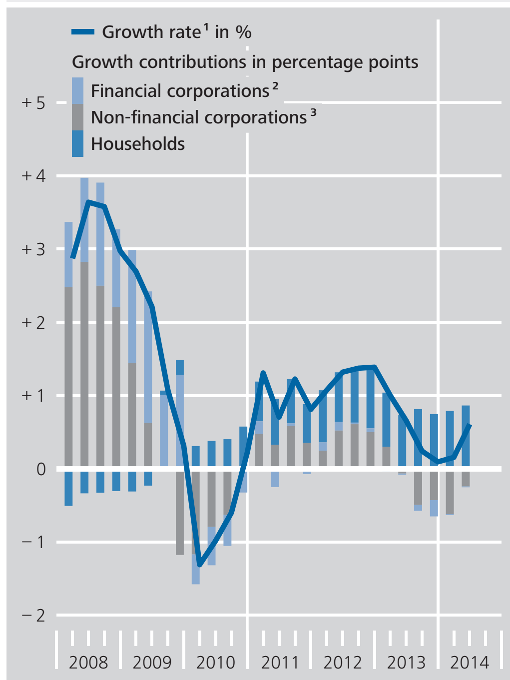
Credit standards for housing loans unchanged

The credit standards for housing loans remained unchanged according to the banks which participated in the BLS. The banks did not identify any specific factor that had a noteworthy impact on credit standards. In particular, banks again did not regard housing market prospects as having an easing effect on the

Loans of German banks to selected sectors

Seasonally adjusted and adjusted for loan sales and securitisation, end-of-quarter data



1 Year-on-year rate of change. **2** Non-monetary financial corporations. **3** Corporations and quasi-corporations.
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development of credit standards, whereas they perceived this factor to have an expansionary influence on demand-side developments. The banks adjusted their margins primarily on loans for house purchase carrying an average risk; the margins in this credit segment were narrowed markedly. However, the margins on riskier loans remained largely unchanged.

Consumer credit stalled

The margins on average loans were also narrowed somewhat for consumer credit in the reporting quarter, whereas they remained practically unchanged for riskier loans. In addition, the banks surveyed in the BLS perceived a slight easing of standards for consumer credit in the second quarter and reported a slight increase in demand for this credit category. The statistics for the month of June, which are based not only on information from the MFIs surveyed in the BLS but on data from all MFIs in Germany, do indeed show a significant increase in consumer credit. Given that this category of lending was still on the decline at the beginning of the three-month period, consumer loans stagnated across the second quarter as a whole. On the whole, loans to domestic households remained moderate in mid-2014. The 12-month rate of loans to households rose to 1.4% at the end of the quarter compared with 1.3% at the end of March, continuing the slight upward trend observed for some time now.

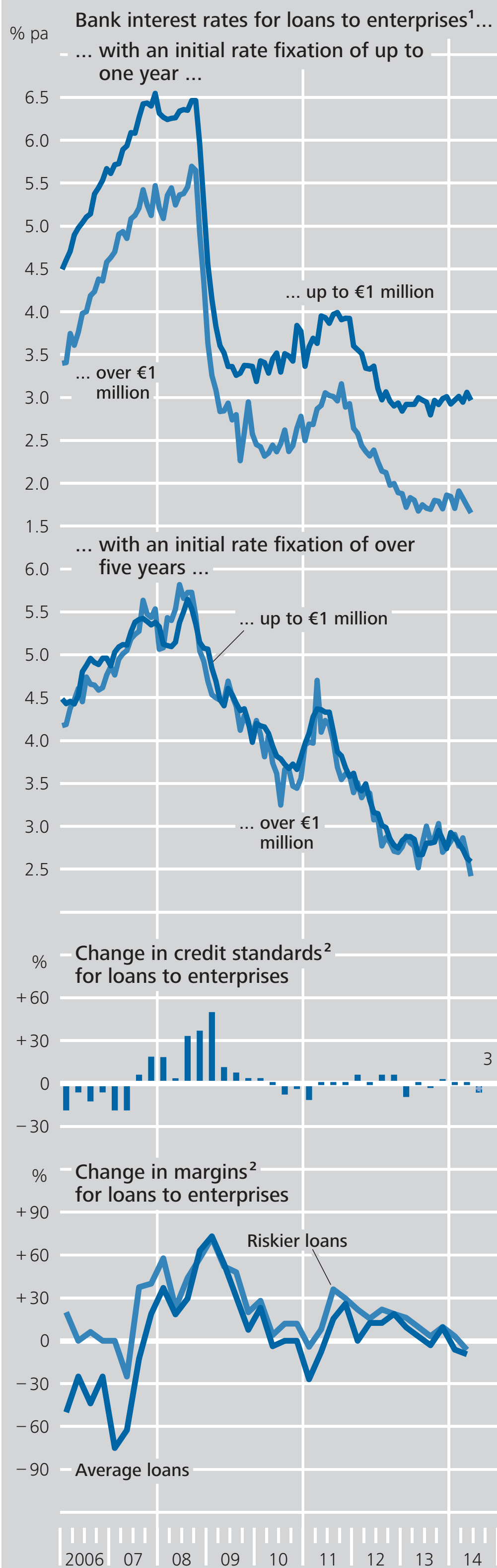
Marked increase in loans to non-financial corporations

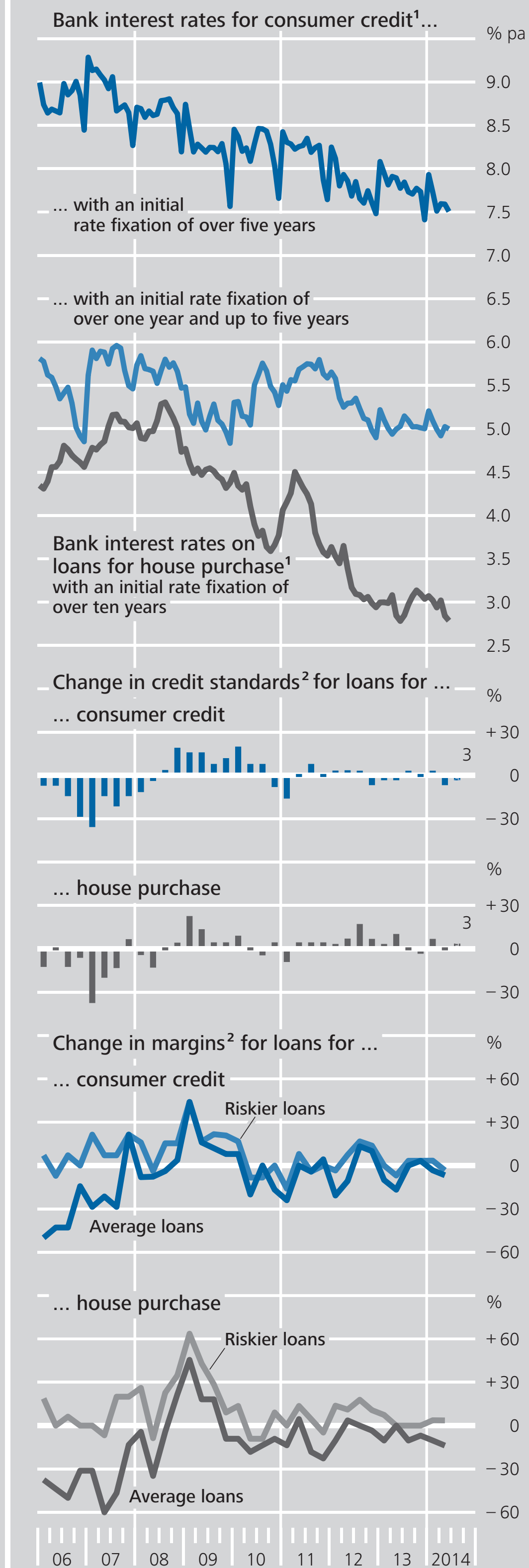
There was also an upturn in lending to domestic non-financial corporations, with marked growth in loans with short and intermediate maturities being recorded in the reporting quarter for the first time since summer 2012. However, this development came to a halt towards the end of the quarter as net inflows into short-term loans were somewhat lower than net outflows from longer maturities in June. This could be one of the reasons why, according to the German banks participating in the BLS, demand for loans to enterprises remained virtually unchanged on balance in the second quarter of 2014. As in the preceding quarters, BLS data suggest that demand was dampened by enterprises accessing alternative sources of funding, particularly internal financing. However, viewed over the 12-month period up to the end of the second quarter, the increase in the second quarter did not fully offset the net redemptions made in the preceding quarters. Although the annual growth rate rose by 1.1 percentage points, it remained in negative territory at -0.7%.

German banks' credit standards for enterprises unchanged

Surveys do not currently offer any indications of substantial supply-side impediments to lending, although in the previous BLS survey the German banks considered their credit standards for lending to enterprises to be relatively tight (see the box entitled The level of credit standards in the Bank Lending Survey on pages 44 to 47). According to the German results of the latest BLS for the second quarter, the surveyed institutions did not change their credit standards for loans to enterprises. This applies to loans to all firm sizes and of all maturities. None of the factors relevant to credit standards contained in the BLS questions

Banking conditions in Germany





1 New business. According to harmonised MFI interest rate statistics. **2** According to the Bank Lending Survey; for credit standards: difference between the number of respondents reporting "tightened considerably" and "tightened slightly" and the number of respondents reporting "eased somewhat" and "eased considerably" as a percentage of the responses given; for margins: difference between the number of respondents reporting "widened considerably" and "widened slightly" and the number of respondents reporting "narrowed somewhat" and "narrowed considerably" as a percentage of the responses given. **3** Expectations for 2014 Q3.

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The level of credit standards in the Bank Lending Survey

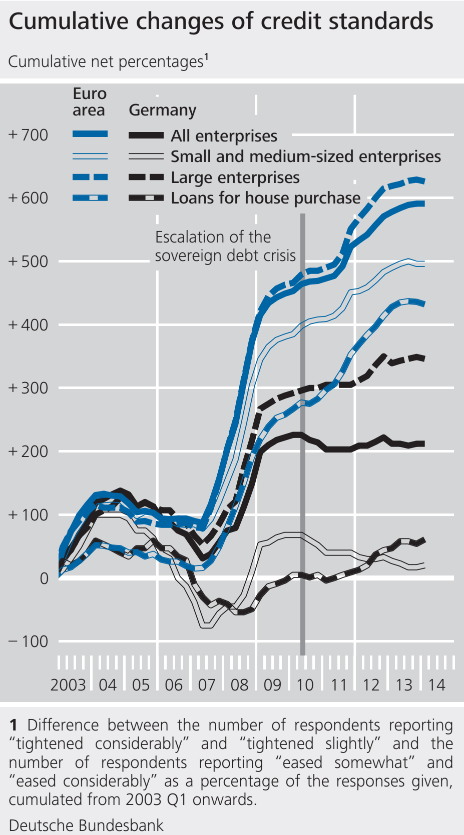
For the first time since the euro-area Bank Lending Survey (BLS) was launched in 2003, the respondent banks were asked in this year's April survey not only about the changes in their credit standards in the quarter ended but also, and explicitly, about the levels of their credit standards. To this end, the surveyed institutions were asked to assess the current level of their credit standards relative to the levels prevailing since the beginning of 2003 and the second quarter of 2010 respectively.[1]

In the past, levels of credit standards could only be approximated by cumulating the changes reported on a quarterly basis. For the longer period (since the beginning of 2003) this cumulation of the values reported by the surveyed banks indicates, for the euro area as a whole, a tendency towards more restrictive credit standards in all loan segments (amid fluctuations). Periods in which standards were tightened alternate with periods in which tightenings remained constant or were reduced, but were not (wholly) reversed. In Germany, this trend is less pronounced and is evident only with regard to credit standards for loans to large enterprises. By contrast, the cumulative credit standards for loans to small and medium-sized enterprises (SMEs) as well as for loans to households for house purchase fluctuate more or less around the 2003 initial value. For the period since the second quarter of 2010, the cumulative changes currently indicate that, in the euro area as a whole, banks have tightened their credit standards for both loans to enterprises and loans for house purchase. In Germany, by contrast, a tightening of standards is discernible only for loans to large enterprises and housing loans.

This cumulation method has one major drawback in that there is no information as to the point in time when credit standards were at a "neutral" level – the only truly suitable reference point for such a cumulation.[2] What is more, the reasons for the essentially euro-area trend towards more restrictive credit standards across the entire observation period cannot be unambiguously identified. This trend is probably due chiefly to the financial crisis, which largely overlaps the observation periods and led to

Cumulative changes of credit standards

Cumulative net percentages[1]



1 Difference between the number of respondents reporting "tightened considerably" and "tightened slightly" and the number of respondents reporting "eased somewhat" and "eased considerably" as a percentage of the responses given, cumulated from 2003 Q1 onwards.

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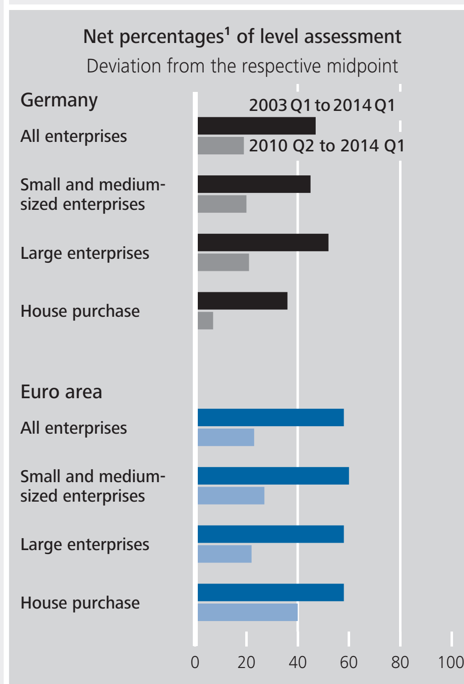
1 The period since the beginning of 2003 represents the longest possible observation period, as the BLS has been in existence since then. The second, shorter period was included in order to obtain an appraisal of the current level of credit standards compared with the period since the euro-area sovereign debt crisis intensified.
2 Moreover, this point in time is likely to vary across the different banks and countries of the euro area, thereby further impairing comparability.

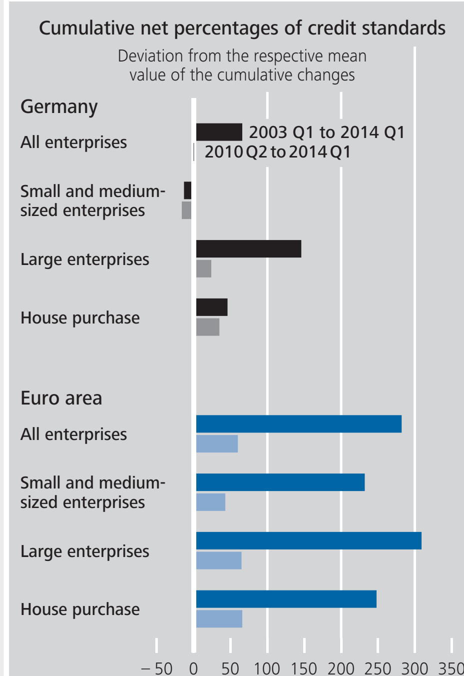
more restrictive lending in most countries. However, it cannot be ruled out that the banks' response behaviour is fundamentally biased towards a "tightened" assessment.[3] A bias of this kind could be attributed to an overly stringent response behaviour, either for strategic reasons or subconsciously.[4]

Because of these shortcomings, the banks participating in the latest April round of the BLS were asked directly and separately for each loan category how restrictive or expansive they considered their current credit standards to be compared with two reference periods, one from the launch of the BLS in 2003 to the first quarter of 2014 and the other from the escalation of the sovereign debt crisis in the second quarter of 2010 to the first quarter of 2014. Each bank was to use as its reference level the midpoint of the range of its responses, ie the midpoint between the tightest and loosest level of its credit standards in the respective periods.[5] The individual banks' responses to this *ad hoc* question were aggregated using the calculation method for net percentages,

Comparison of responses regarding the level* and of the current deviation from the mean value of the cumulative changes

As a percentage of the responses given





* Assessment of the current level of credit standards in relation to the midpoint of the range of standards implemented in two different time periods. **1** Difference between the number of respondents reporting "at the tightest level/considerably tighter/moderately tighter than the midpoint of the range" and "at the loosest level/moderately looser/considerably looser than the midpoint of the range" as a percentage of the responses given.

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3 The Senior Loan Officer Opinion Survey on Bank Lending Practices (SLOOS), which the US Federal Reserve System has used since 1967 to collect data on banks' lending behaviour, likewise indicates that, over time, banks have reported a tightening of their credit standards significantly more often than an easing of lending standards.
4 The results of the cumulation method may be distorted for other reasons, too. For instance, the respondents at many banks have changed over the years, meaning that a continuity of response behaviour was not always assured. Moreover, the net percentages ignore the gradations of the possible responses ("considerably" versus "slightly") in the changes to credit standards. In addition, a slight easing followed by a slight tightening does not necessarily mean a return to exactly the same level as before.
5 The banks were given eight possible answers to appraise the current level of their credit standards compared with the reference level. In addition to the five gradations (from "considerably tighter than the midpoint of the range" to "considerably looser than the midpoint of the range") modelled on the standard BLS questions, three further possible answers were provided which were designed to capture particularly noteworthy levels ("at the tightest/loosest level during this period") or developments ("levels have remained constant during this period").

which is also used to aggregate the responses to the standard questions in the BLS.[6] Given the way the *ad hoc* question was framed, it is not possible to reach any conclusions about the absolute levels of current credit standards when interpreting these net percentages. However, it is possible to gauge how great the deviations are currently estimated to be from the respective "historical" reference value in the individual countries or in the euro area as a whole. The aforementioned problem regarding the cumulation method, ie the fact that the "neutral" benchmark level of credit standards is unknown, cannot be entirely eliminated in respect of the *ad hoc* question either. However, the fact that the current level is compared with the range of the levels over an extended period rather than with the level at a fixed point in time (the beginning of 2003) significantly reduces the problem of working with a reference level that may be unsuitable.

The survey results show that the present level of credit standards for loans for enterprises and loans for house purchase, both in the euro area as a whole and in Germany, are significantly more restrictive on balance than the reference value for the longer observation period (since 2003). Differences relating to firm size are scarcely discernible. The extent of the restrictive deviations from the reference value is somewhat greater in the euro area as a whole than in Germany, and in addition is very heterogeneous across the individual countries of the euro area. It should be pointed out that large restrictive deviations from the midpoint of the range for this time period do not necessarily result (only) from a currently extremely restrictive level; they can also stem from the fact that the pre-crisis level was by no means "neutral", for example because credit standards were loose in some cases prior to the crisis. In that case, the large deviations evident at present may *(inter alia)* indicate a correction.

Compared with the reference value for the shorter time period (since the second quarter of 2010), the credit standards for loans to enterprises are also tighter at present. However, they exceed the reference value far less than do the results for the longer reference period. This is not surprising, as massive crisis-induced tightenings of credit standards occurred for the most part before 2010, meaning that the standards in most countries and loan segments were probably already at a fairly high level by the second quarter of 2010. The responses to the standard questions suggest that banks subsequently tightened their credit standards only slightly or left them unchanged. For the period beginning in the second quarter of 2010, the deviations from the reference value in loans to enterprises in the euro area as a whole and in Germany do not differ greatly. In the case of loans for house purchase, by contrast, credit standards in Germany are currently only slightly tighter than their reference value since the sovereign debt crisis intensified, while in the euro area as a whole they are considerably more restrictive than the corresponding reference value.

The responses to the *ad hoc* question regarding the levels can be compared with the deviations of the current levels from the mean values in each of the two reference periods as derived from the cumulative changes. In theory, the two methods could produce different results for various reasons. It may be, for example, that the time

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6 The difference between the total number of respondents reporting "at the tightest level/considerably tighter/moderately tighter than the midpoint of the range" and "at the loosest level/moderately looser/considerably looser than the midpoint of the range" was calculated for each country and for the euro area as a whole, and then the percentage share of this difference in all responses was computed.

series of the historical values was not available as a yardstick to the bank respondent who answered the question regarding the current level. If, on the other hand, the respondent had been able to consult this time series, he or she may have identified a distorted response pattern in the past and tried to correct it *ex post* when answering the question. Given these possible distorting factors, it is surprising that the results obtained using the two methods largely match. However, it is equally conceivable that respondents' answers regarding the level were coloured by a similar degree of tightening bias as that presumed in the cumulative changes; this could explain the high degree of consistency.

The two methods show that, both in Germany and in the euro area as a whole, the most pronounced changes in the credit standard level occurred before the sovereign debt crisis escalated, and that only comparatively minor adjustments were made thereafter. In addition, the same qualitative differences between the results for the euro area as a whole and Germany are revealed by both methods. The tightening is more pronounced in the euro area as a whole than in Germany. By contrast, the two methods come to different conclusions with regard to credit standards for loans to SMEs in Germany. Thus, the level of credit standards measured by cumulative changes is currently somewhat looser than the mean values of both comparable periods. Yet according to the responses to the *ad hoc* question regarding the level, German banks see the present level of their credit standards for loans to SMEs – like those for loans to large enterprises – as being markedly tighter than the respective reference value for the two observation periods.[7]

However, differences in the results obtained using the two methods with regard to the credit standards for loans to SMEs in Germany do not necessarily point to a contradiction. On the one hand, the cumulative changes imply that these standards were changed only relatively slightly over the entire time period. On the other hand, the response to the *ad hoc* question provided by many banks, to the effect that lending standards are at present moderately or considerably tighter than the midpoint of the range or that they are even at their tightest level, might also be true, namely within a narrow range.

The differences in the results obtained using the two methods with regard to credit standards for loans to SMEs in Germany also highlight the importance of the question regarding the level of credit standards. Only by comparing the results obtained using the two methods regarding the perceived level of credit standards is it possible to detect possible deviations between the levels as calculated using the cumulative net percentages and as reported by the banks. Since neither approach is clearly superior, divergences have to be evaluated against the backdrop of the advantages and disadvantages specific to each. In future, the *ad hoc* question regarding the level of credit standards is to be posed annually in the April BLS.

7 The discrepancy in the results obtained using the two methods could be attributable, amongst other things, to the differences in how the respondents appraise their credit standards for loans to large enterprises and loans to SMEs. Thus, in response to the *ad hoc* question regarding the level, banks appraised the current differences in credit standards for loans to enterprises of different sizes as being slight. However, occasional differentiations by firm size which were made in the course of credit standard changes may accumulate over time to become considerable, a phenomenon of which the respondent banks may have been unaware until they considered their reply to the *ad hoc* question regarding the level. Moreover, there were distinct discrepancies for a few banks between the results obtained using the two methods, which significantly magnify the differences at the aggregate level.

had a noteworthy impact when viewed in isolation. The surveyed banks moderately tightened their margins on loans to enterprises. However, this only benefited large enterprises; the margins on loans to small and medium-sized enterprises remained unchanged.

Risk-weighted assets reduced and capital position strengthened

The BLS in the second quarter contained a number of *ad hoc* questions on banks' funding conditions, the impact of the sovereign debt crisis and on the new regulatory and supervisory actions, which include the ECB's asset quality review. According to the institutions, the funding situation improved slightly in the second quarter of 2014. The institutions also stated that the sovereign debt crisis had not affected their lending policy and had only very marginal effects on their funding conditions in the period under review. In the wake of the new regulatory and supervisory actions, the banks reduced their risk-weighted assets in the first half of 2014, albeit to a lesser extent than in the second half of 2013. They also managed to strengthen their capital position through retained earnings and capital issuance. The institutions stated that the new regulatory requirements – taken in isolation – did not have any notable effects on their funding conditions. The changed regulatory and supervisory setting *per se* had an impact on lending business merely in the form of somewhat tighter credit standards for loans to enterprises.

Bank lending rates follow interest rate decline in the capital market

As the interest rate level was still very low, the development of bank lending rates in new business probably tended to support domestic lending to the private sector. The interest rate statistics suggest that bank interest rates in the second quarter largely followed the moderate interest rate decline in the money and capital markets across all reported segments, maturities and volumes. For example, the interest rates for small-scale loans to enterprises decreased slightly, whereas they fell discernibly for large-scale loans. For short-term funds, the reporting institutions were charging interest of 3.0% for small-scale and 1.7% for large-scale loans at the end of June. Interest rates on long-term loans to domestic non-financial corporations stood at 2.6% and 2.4% respectively at the end of the period under review.

Interest rates on loans for house purchase were also discernibly on the decline in the second quarter. At the end of June, the interest rate on long-term loans stood at 2.8%. Deposits of households and non-financial corporations again predominantly earned somewhat less interest than in the previous quarter.