Monetary policy and banking business

Interest rate policy and the money market

Main refinancing rate remains at 1%

As expected, economic activity in the euro area slowed in the fourth quarter of 2009. Against this backdrop and given the prospect of a gradual economic recovery, Eurosystem projections indicate that consumer prices will remain within the range of stability over the time horizon relevant to monetary policy, although uncertainty regarding the outlook remains high due to the fallout from the financial crisis. Likewise, market participants' medium to long-term inflation expectations remain well anchored in the euro area. Monetary growth slowed in the reporting quarter, not least in view of the fact that lending to the private sector was virtually stagnant. Monetary developments consequently present no medium-term inflation risks at present. Based on these framework conditions, the Governing Council of the ECB left the Eurosystem's key policy rates on hold between October 2009 and January 2010. Throughout the fourth quarter of 2009, the main refinancing operations were again conducted as fixed-rate tenders with full allotment at an interest rate of 1%. Commercial banks still have to pay 1.75% to use the marginal refinancing facility, while credit balances under the deposit facility are remunerated at 0.25%.

Last one-year tender interest-indexed

On 17 December 2009, the ECB conducted its third and last supplementary Eurosystem refinancing operation with a maturity of one year. The tender was conducted on an interest-indexed basis. Banks participating in this transaction are not charged a pre-defined

Money market management and liquidity needs

During the three reserve maintenance periods from 14 October 2009 to 19 January 2010, euro-area credit institutions' need for central bank liquidity determined by autonomous liquidity factors remained practically unchanged; it decreased slightly by €1.8 billion in net terms. Although the demand for liquidity from banknotes in circulation increased markedly by €28.0 billion – primarily owing to the usual seasonal increase around Christmas – the developments in the remaining autonomous factors during the period under review resulted in a slight reduction in the need for central bank liquidity in net terms. First, there was a decrease of €19.2 billion in general government deposits with the Eurosystem over the three periods and, second, if the net foreign reserves and the other factors are taken together, a move which eliminates liquidity-neutral valuation effects, there was a decrease in the liquidity needs of €10.6 billion. The decline in the demand for liquidity arising from autonomous factors was strengthened by the decline in the minimum reserve requirement of €3.6 billion net.

As was the case in previous months, the period under review was defined by the generous supply of liquidity by the Eurosystem which had the aim of supporting the functioning of the money market and satisfying credit institutions' demand for central bank liquidity, even above the regular demand. Liquidity-providing open-market operations continued to be carried out as fixed-rate tenders with full allotment meaning that liquidity provision was determined by the demand from credit institutions. Primarily as a result of the additional liquidity provided by the 12-month tenders, the last of which was carried out on 17 December 2009 with a volume of €97 billion, in the three periods under review, the emphasis shifted further from main refinancing operations to longer-term refinancing operations. In net terms, the volume of the main refinancing operations decreased by around €19 billion, while the volume of the longer-term operations increased by just under €32 billion. Additionally, the Eurosystem continued to pursue its purchase programme for covered bonds and was able to increase its holdings by €13 billion to €31 billion during the period under review. At the same time, owing to the increase in liquidity provision, recourse to the deposit facility increased by around €37 billion net, while the marginal lending facility remained largely unused.

EONIA was recorded at around 0.35% throughout almost the entire period and thus was primarily oriented to the deposit facility rate of 0.25%. Only on the final day of each reserve period when the Eurosystem withdrew liquidity through liquidity-absorbing quick tenders did the EONIA fixings increase noticeably, to a maximum rate of 0.69%.

On 3 December 2009, the ECB Governing Council decided on initial steps to facilitate a move away from its liquidity policy characterised by non-standard measures. For instance, the Governing Council agreed to discontinue the supplementary 3-month tenders and the 12-month operations as of the beginning of 2010 and to allot just one final 6-month tender in 2010, at the end of March. Parallel to this, market participants were guaranteed that, until the beginning of April 2010, all main and longer-term refinancing operations would continue to be carried out as fixed-rate tenders with full allotment.

During the October-November 2009 reserve maintenance period, the outstanding refinancing volume decreased steadily, mainly due to declining demand from credit institutions in the weekly main refinancing operations, the volume of which decreased from €62 billion to €46 billion. Almost entirely unaffected by this, however, was the fact that significantly more liquidity remained available than was necessary to meet the regular liquidity needs arising from autonomous factors and the reserve requirement. The excess liquidity (on the basis of the benchmark amount) was around €135 billion on average over the period. EONIA turnover was €38.7 billion on average over the period, representing a slight increase on the previous period (€35.9 billion).

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In the November-December 2009 reserve period, the outstanding refinancing volume was around €650 billion on most days. The excess liquidity stood at around €109 billion on average, somewhat lower than in the previous period, and recourse to the deposit facility declined further (€66 billion on average compared with €86 billion and €110 billion in the previous periods). EONIA remained close to the deposit rate. At the same time, EONIA turnover, at €38.1 billion on average over the period, changed very little compared with the preceding period.

The December 2009-January 2010 reserve period, which lasted a total of 43 days, was determined by the allotment of the third and final 12-month tender. In its meeting on 3 December 2009, the ECB Governing Council agreed that the interest rate of this tender would correspond to the average minimum bid rate of the main refinancing operations carried out during the maturity of this tender. Under these changed conditions – both of the previous 12-month tenders were allotted at a fixed rate of 1.00% – 224 credit institutions participated in this tender in mid-December in the Eurosystem; they bid and received €97 billion, in line with market expectations. Even though the bid volume was higher than the €75 billion allotment volume of the second 12-month tender at the end of September, the number of bidders decreased by more than half in comparison. As a result of this additional inflow of just under €100 billion, the excess liquidity went up again (€228 billion on average over the period), causing a sharp increase in average recourse to the deposit facility to €147 billion. Owing to the even more comfortable liquidity conditions, turnover in the (short-term) money market decreased as credit institutions were even less dependent on trade in the secondary market. Hence, unsecured EONIA turnover fell to €29.1 billion on average over the period (€9 billion less than in the preceding period). Additionally, turnover on Eurex Repo's Euro GC Pooling for secured overnight money decreased to €7.1 billion per day on average, after being recorded at €10.0 billion and €11.0 billion respectively in the two preceding periods. This meant that the Eurosystem again played a more prominent role as an intermediary in the money market.

In the subsequent January-February 2010 reserve period, Eurosystem counterparties were offered liquidity-providing operations in US dollar and Swiss francs for the last time; the ECB had announced in January that these operations, which were limited until the end of January 2010, would not be extended.

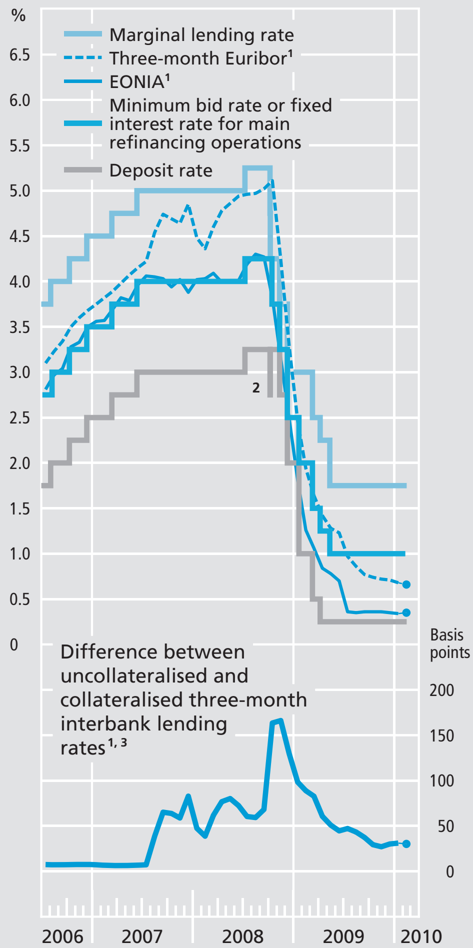
Factors determining bank liquidity [1]

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

Item	2009 14 Oct to 10 Nov	2009 11 Nov to 7 Dec	2010 8 Dec to 19 Jan
I Provision (+) or absorption (–) of central bank balances due to changes in autonomous factors			
1 Banknotes in circulation (increase: –)	– 1.9	– 4.5	– 21.6
2 General government deposits with the Eurosystem (increase: –)	– 9.7	– 1.4	+ 30.3
3 Net foreign reserves [2]	– 8.4	– 5.4	+ 5.4
4 Other factors [2]	+ 5.8	+ 11.3	+ 1.9
Total	– 14.2	+ 0.0	+ 16.0
II Monetary policy operations of the Eurosystem			
1 Open market operations			
(a) Main refinancing operations	– 26.8	+ 3.5	+ 4.7
(b) Longer-term refinancing operations	+ 9.2	– 32.7	+ 55.0
(c) Other operations	+ 6.7	+ 6.6	+ 5.6
2 Standing facilities			
(a) Marginal lending facility	– 0.0	+ 0.4	– 0.3
(b) Deposit facility (increase: –)	+ 23.1	+ 20.8	– 81.3
Total	+ 12.2	– 1.4	– 16.3
III Change in credit institutions' current accounts (I + II)	– 1.9	– 1.4	– 0.2
IV Change in the minimum reserve requirement (increase: –)	+ 1.8	+ 1.6	+ 0.2

1 For longer-term trends and the Deutsche Bundesbank's contribution, see pages 14* and 15* of the Statistical Section of this Monthly Report. — **2** Including end-of-quarter valuation adjustments with no impact on liquidity.

Money market interest rates in the euro area



1 Monthly averages. — 2 Only on 8 October 2008 2.75%. — 3 Three-month Euribor less three-month Eurepo. — ● Average from 1 to 15 February 2010.

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interest rate for the provision of central bank liquidity; instead, upon maturity of the transaction, they are charged the average main refinancing or minimum bid rate over the term. Although banks took advantage of this last opportunity to gain a one-year loan and, at a volume of €96.9 billion in December, borrowed more liquidity from the Eurosystem than during the second 12-month tender at the end of September (€75.2 billion), the allotment volume in the third one-year operation was significantly down on the first transaction of this kind in June 2009 (€442.2 billion) owing to the extremely favourable liquidity situation in the European banking sector. At the same time, the number of banks participating in the tender fell again. Only 224 credit institutions participated in the December tender compared with 1,121 in the first and 589 in the second 12-month operations.

Gradual phasing-out of supplementary monetary policy measures announced

In light of the recent drop in demand, the Eurosystem and the US Federal Reserve agreed to discontinue 84-day foreign currency operations in US dollars after 6 October 2009. The Eurosystem stopped conducting one-week US-dollar swap operations and refinancing operations for Swiss francs from 1 February 2010. Furthermore, supplementary three-month tenders were discontinued at the end of 2009. The Governing Council announced that it will conduct its last special tender with a maturity of six months at the end of March 2010. In addition, the Governing Council announced that it will decide at the start of March 2010 whether to continue gradually phasing out the supplementary non-standard liquidity measures adopted in response to the financial crisis.

Overnight interest rate just above interest rate on deposit facility

Euro-area money market rates barely reacted to the announcement that non-standard monetary policy measures are to be gradually phased out. As in the third quarter of 2009, the overnight interest rate (EONIA) was fluctuating slightly around the 0.35% mark between October and January, which was around 0.1 percentage point above the inter-

Open market operations of the Eurosystem *

Value date	Type of transaction [1]	Maturity in days	Actual allotment in € billion	Deviation from the benchmark [2] in € billion	Marginal rate/fixed rate %	Allotment ratio %	Weighted rate %	Cover ratio [3]	Number of bidders
14.10.09	MRO (FRT)	7	61.6	105.6	1.00	100.00	–	1.00	218
14.10.09	S-LTRO (FRT)	28	7.7	–	1.00	100.00	–	1.00	19
21.10.09	MRO (FRT)	7	49.8	142.8	1.00	100.00	–	1.00	224
28.10.09	MRO (FRT)	7	48.7	138.7	1.00	100.00	–	1.00	188
29.10.09	LTRO (FRT)	91	3.3	–	1.00	100.00	–	1.00	25
04.11.09	MRO (FRT)	7	46.2	141.2	1.00	100.00	–	1.00	170
10.11.09	FTO (–)	1	– 191.4	–	0.80	100.00	0.76	1.00	165
11.11.09	MRO (FRT)	7	51.3	68.8	1.00	100.00	–	1.00	160
11.11.09	S-LTRO (FRT)	27	2.5	–	1.00	100.00	–	1.00	12
12.11.09	S-LTRO (FRT)	91	10.8	–	1.00	100.00	–	1.00	9
12.11.09	S-LTRO (FRT)	182	0.8	–	1.00	100.00	–	1.00	21
18.11.09	MRO (FRT)	7	52.6	99.6	1.00	100.00	–	1.00	177
25.11.09	MRO (FRT)	7	59.1	114.1	1.00	100.00	–	1.00	168
26.11.09	LTRO (FRT)	91	2.1	–	1.00	100.00	–	1.00	19
02.12.09	MRO (FRT)	6	58.1	138.1	1.00	100.00	–	1.00	137
07.12.09	FTO (–)	1	– 129.7	–	0.80	100.00	0.76	1.00	147
08.12.09	MRO (FRT)	8	55.8	58.3	1.00	100.00	–	1.00	111
08.12.09	S-LTRO (FRT)	43	2.7	–	1.00	100.00	–	1.00	8
10.12.09	S-LTRO (FRT)	91	2.9	–	1.00	100.00	–	1.00	9
10.12.09	S-LTRO (FRT)	182	1.7	–	1.00	100.00	–	1.00	21
16.12.09	MRO (FRT)	7	52.9	109.4	1.00	100.00	–	1.00	125
17.12.09	S-LTRO (FRT)	371	96.9	–	[4] ...	100.00	–	1.00	224
17.12.09	LTRO (FRT)	105	2.6	–	1.00	100.00	–	1.00	21
23.12.09	MRO (FRT)	7	58.6	253.1	1.00	100.00	–	1.00	109
30.12.09	MRO (FRT)	7	78.6	288.6	1.00	100.00	–	1.00	132
06.01.10	MRO (FRT)	7	54.0	292.5	1.00	100.00	–	1.00	100
13.01.10	MRO (FRT)	7	60.1	277.1	1.00	100.00	–	1.00	102
19.01.10	FTO (–)	1	– 258.9	–	0.80	100.00	0.75	1.00	188

***** For more information on the Eurosystem's operations from 8 July 2009 to 13 October 2009, see Deutsche Bundesbank, Monthly Report, November 2009, p 28. — **1** MRO: main refinancing operation, LTRO: longer-term refinancing operation, S-LTRO: supplementary longer-term refinancing operation, FTO: fine-tuning operation (+: liquidity providing operation, –: liquidity absorbing operation). FRT: fixed-rate tender. — **2** Excluding (S-)LTROs allotted in the same week. — **3** Ratio of total bids to the allotment amount. — **4** The interest rate is the average minimum bid rate of the MROs over the life of this operation.

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est rate on the Eurosystem deposit facility. Any significant increases in the overnight rate occurred almost exclusively on the last days of each of the maintenance periods, when the Eurosystem absorbed surplus liquidity through fine-tuning operations.

Sideways trend in longer-term money market interest rates

A predominantly sideways trend was also observed in longer-term money market interest rates in the final quarter of 2009, especially at the long end of the money market curve. Conversely, towards the end of the year, in particular, shorter-term unsecured interbank interest rates with maturities of up to six months fell slightly and are, at present, consistently being quoted below the Eurosystem's main refinancing rate. The uncollateralised three-month rate (3M Euribor) currently stands at 0.66% and its collateralised counterpart (3M Eurepo) at 0.35%. The risk premium on the euro money market, which is determined on the basis of their yield spread, is currently 0.3 percentage point and thus only marginally below the level at the end of the previous quarter. The announcement of the gradual phasing-out of non-standard monetary policy measures in December did not lead to any discernible rise in this risk premium either.

Monetary developments in the euro area

Further deceleration of monetary expansion

Monetary expansion in the euro area continued to slow in the reporting quarter. In seasonally adjusted and annualised terms, the growth rate of the broad monetary aggregate M3 was more than -1% in the fourth quarter of 2009 and was thus well down on the already weak rate of 0% recorded in the third quarter. The three-month average of the annual rates of growth of M3 over the period from October to December also fell to -0.1% on the back of growth of 2.4% in the preceding quarter. It thus fell into negative territory for the first time since the launch of monetary union.

Demand for highly liquid M3 components still buoyant

The interest rate environment, characterised by assets with a maturity of up to two years having a comparatively small interest rate advantage over overnight deposits and by a steep yield curve for maturities of over two years, had a major impact on monetary growth in the reporting quarter, too. However, the shifts from short-term time deposits (with an agreed maturity of up to two years) remunerated at close to market rates to the most liquid components of M3, as witnessed in the three preceding quarters, steadily diminished throughout the reporting quarter. At a seasonally adjusted and annualised three-month rate of 8% in the fourth quarter, the rise in overnight deposits remained well below the very high rate of 16½% in the previous quarter. At the same time, growth in currency in circulation slowed in annualised terms from just under 7½% to just short of 4%. Overall, the still buoyant growth of the narrow monetary aggregate M1 decelerated to just over 7% between October and December on the back of 15% between July and September.

Net reduction in short-term deposits other than overnight deposits ...

At the same time, the decline in holdings of other short-term deposits in the reporting quarter was almost just as equally marked as in the past three quarters, at a seasonally adjusted and annualised three-month rate of just over 9½%. This was due mainly to persistently strong outflows of short-term time deposits. Households, in particular, contributed to the 25% seasonally adjusted and annualised decline in these deposits, compared with -27% in the previous quarter. The uptake of shorter-term savings deposits (redeemable at notice of up to three months) did not come close to compensating for this development; in the period under review, it was down somewhat on the preceding three quarters.

... and marketable instruments

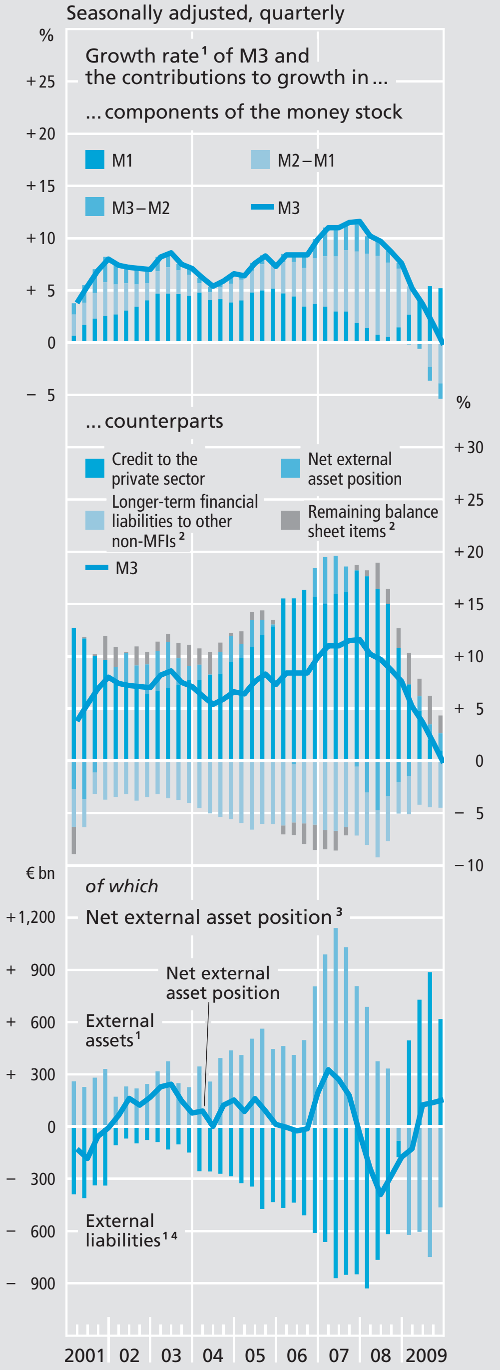
There were also net outflows of marketable financial instruments. After shrinking by more than 15% in the previous quarter, the decline slowed to just under 2½% in annualised terms between October and December 2009. Repo transactions, which are highly volatile and originate largely from securitised interbank operations, were the only sub-component to show a sharply positive trend in the reporting quarter. There were significant outflows of money market fund shares/units in the last quarter of 2009. These account for the largest share of marketable instruments and had experienced positive growth between July and September. By contrast, in December, special factors played a role in the considerable slowing of the decline in short-term debt securities of monetary financial institutions held by non-banks (with a maturity of up to two years) compared with the previous four quarters.

Weak lending to the private sector

The slowdown in the underlying pace of monetary growth and the latterly weak lending to the private sector continued in the reporting quarter. Nonetheless, credit provided by banks in the euro area experienced an increase, albeit slight, in loans for the first time since the final quarter of 2008. Starting from the high level of the previous quarter, the acquisition of securitised assets was negative overall from October to December. Loans to domestic private non-banks, which had stood at an annualised and seasonally adjusted three-month rate of -1% in the third quarter, rose by just short of 1% in the period under review. The three-month lending rate to the domestic private sector, adjusted for credit institutions' securitisation activities and loan sales, also amounted to just under 1%. The parallel development of the adjusted and unadjusted three-month rates can be attributed to the fact that banks conducted only a small number of securitisation transactions in the fourth quarter of 2009, which meant that

Components and counterparts of the money stock in the euro area

Seasonally adjusted, quarterly



1 12-month flows. — **2** Taken in isolation, an increase curbs M3 growth. — **3** Not seasonally adjusted. — **4** Increase: –, decrease: +.

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there was no statistical underreporting of banks' actual lending.

Perceptible growth in loans to households, ...

The slight rise in loans to domestic private non-banks was the outcome of fairly heterogeneous sectoral developments. Lending to households expanded most, with the positive developments of the past two quarters consolidating further. This was again attributable to loans for house purchase, which make up the lion's share of households' borrowing. Other credit to households also rose sharply, while consumer credit virtually stagnated in the reporting quarter following slight growth in the previous quarter.

... but further decline in loans to non-financial corporations

In the fourth quarter of 2009, inflows of loans to households were accompanied by strong outflows of loans to non-financial corporations, which are to be seen in connection with the slowdown in economic activity. This was primarily caused by the persistently sharp drop in short-term loans with a maturity of up to one year. Nevertheless, the development of medium-term loans (with a maturity of over one and up to five years) was also identifiably negative again in the reporting quarter. By contrast, there was a further clear increase in long-term loans (with a maturity of over five years).

Discernible increase in loans to other financial intermediaries

There was a discernible increase in loans to other financial intermediaries between October and December, while these loans had a significant negative effect on credit growth in the third quarter. The volatility of these movements should be viewed in connection with reverse repo transactions. With these transactions, banks issue securitised credit to a financial service provider in the other financial intermediaries sector. The financial service provider then lends the liquidity raised to other banks against collateral. By nature, these transactions ultimately constitute indirect interbank operations. This type of lending is therefore not *per se* accompanied by lending to the private non-banking sector.

Slight drop in securities acquisitions by banks

Starting from a high level in the previous three months, the fourth quarter of 2009 saw a slight drop in the level of funds made available by banks in the euro area through securities acquisitions. There was only a small rise in holdings of securities from public sector issuers; their annualised and seasonally adjusted growth rate fell from 15½% in the previous quarter to almost 1½% in the period under review. Holdings of securities issued by the private sector in the euro area had been rising sharply since 2007, but, for the first time since then, fell at a corresponding rate of 7% between October and December 2009, compared with an increase of more than 6½% in the preceding quarter.

Perceptible rise in net external assets

In the fourth quarter of 2009, the net external assets of the euro-area MFI sector rose by €45.4 billion in seasonally adjusted terms and, thus, taken in isolation, had an expansionary effect on monetary growth. As in the two preceding quarters, the decline in domestic MFIs' liabilities to residents outside the euro area in connection with the restructuring of MFI balance sheets was more pronounced than the corresponding reduction in assets.

Noticeable rise in longer-term investment at banks

By contrast, monetary growth tended to be slowed by a weaker, but nonetheless perceptible, formation of MFI longer-term financial liabilities. Monetary capital in the euro area rose by 4% in seasonally adjusted and annualised terms in the fourth quarter of 2009, compared with just over 7% in the previous quarter. While banks topped up their capital and reserves noticeably in the reporting period, there was a decline on the quarter in the remaining components. Although the steep yield curve gave rise to a further uptake of longer-term time deposits, particularly by households, their growth was, however, simultaneously dampened by other financial intermediaries' low securitisation activity via banks' special-purpose financing vehicles. Consequently, the increase in long-term time deposits was significantly lower between October and December than in the previous four quarters. Domestic non-banks reduced their holdings of long-term savings deposits slightly in the reporting quarter. Credit institutions in the euro area also borrowed less from non-banks in the form of bank debt securities with longer maturities on the back of high issuance in the third quarter.

No pronounced risk to price stability from a monetary perspective

Overall, the underlying monetary dynamics – in other words, monetary growth which is ultimately relevant to inflation – slowed again in the reporting quarter. There was even a slight drop in M3 between October and December. Inflation projections based on monetary data, taken as a whole, therefore continue to indicate that there will be no pronounced risk to price stability in the euro area for the next three years. Nevertheless, the dispersion of these projections increased again slightly in comparison with the previous quarter. This highlights the fact that there is still a high degree of uncertainty associated with such an outlook.

Deposit and lending business of German banks with domestic customers

Significant reduction in domestic investors' balances at German banks

In the third quarter of 2009, domestic investors reduced their deposits held by German banks for the first time in four years, and this trend accelerated in the fourth quarter. Deposits shrank at a seasonally adjusted and annualised three-month rate of -1% between October and December, compared with -½% in the third quarter. This decline was once again driven mainly by the drop in short-term time deposits (with an agreed maturity of up to two years) remunerated at close to market rates. At just under -45%, their seasonally adjusted and annualised three-month rate was almost as sharply negative as in the preceding quarter. Households, in particular, reduced these balances extremely sharply for the fourth time in succession. Simultaneously, there was another sharp expansion in holdings of overnight deposits. At a seasonally adjusted and annualised three-month rate of 14½%, they were down on the previous quarter (22½%), although their growth rate was still well above the long-term average. Strong growth was recorded among non-financial corporations and households, in particular. The latter also built up a very large volume of short-term savings deposits (redeemable at notice of up to three months), which meant that the pace of growth of this type of deposit remained at a high level. In seasonally

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

€ billion

Item	2009 Oct to Dec	2008 Oct to Dec
Deposits of domestic non-MFIs 1		
Overnight	44.9	51.0
With agreed maturities		
of up to 2 years	– 41.5	23.2
of over 2 years	3.3	28.6
Redeemable at notice		
of up to 3 months	17.1	5.6
of over 3 months	2.3	10.4
Lending		
to domestic enterprises and households		
Loans	– 19.2	– 3.0
Securities	4.7	28.1
to domestic general government		
Loans	– 2.3	– 0.9
Securities	5.5	0.4

* As well as banks (including building and loan associations, but excluding the Bundesbank), monetary financial institutions (MFIs) here also include money market funds; see also Table IV.1 in the Statistical Section of the Monthly Report. — 1 Enterprises, households and general government excluding central government.

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adjusted and annualised terms, short-term savings deposits increased by more than 11% between October and December, compared with over 16% in the third quarter.

Keen interest in long-term time deposits

With regard to long-term deposit types, the strong decline in savings deposits (redeemable at notice of over three months) in December was the main contributor to the reduction in the total volume of domestic deposits in the reporting quarter. In seasonally adjusted and annualised terms, long-term savings deposits shrank by 3½% in the fourth quarter. In the same period, there was, by contrast, a clear rise in the quantitatively more significant long-term time deposits (with an agreed maturity of over two years). Even so, the corresponding three-month rate fell slightly from 3% to 2% as a result of an unusually strong reduction in these balances by insurance corporations and pension funds. Conversely, households continued to top up their long-term time deposits on an extremely large scale with a view to benefiting from the comparatively high yields on these instruments.

Weak credit provision by German banks

Granting of credit by domestic credit institutions to the private sector decreased by a seasonally adjusted and annualised three-month rate of just under 3½% between July and September. Growth was back in positive territory in the fourth quarter, however, with the counterbalancing development in the net credit supply to the individual sectors, which had began in the previous quarter, becoming more pronounced. While more credit was issued to financial corporations, there was a further decline in credit to non-financial corporations. Loans decreased on balance. Growth in total credit to the private sector in the fourth quarter was therefore solely attributable to a perceptible rise in securitised lending. Securitised lending rose by a seasonally adjusted and annualised 5%, after having decreased by 8½% in the previous quarter.

Further decline in unsecuritised lending to non-financial corporations

The reduction in loans to the private sector in the reporting quarter was, overall, less pronounced than in the prececing three-month period. The annualised and seasonally adjusted three-month rate went up from -2½% to ½%. The decline in lending to the private sector in the fourth quarter of 2009 was due solely to the further reduction in the supply of credit to non-financial corporations. Following marked net redemptions of credit issued by German banks to domestic non-financial corporations in the second and third quarters of 2009, there was a further 6% seasonally adjusted and annualised reduction in their volume in the fourth quarter. With regard to maturities, there was a continuation of the trend observed in previous quarters. The reduction in short-term loans that had taken place in the preceding three quarters gained momentum significantly in the reporting quarter, while there was considerable growth in medium-term and long-term loans with a maturity of more than one year.

Clear increase in loans to households

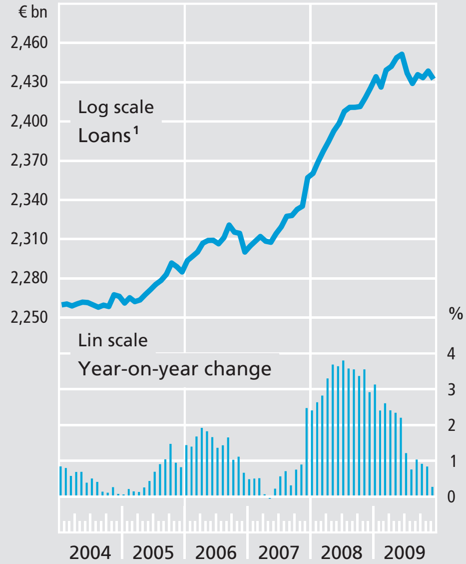
Unlike lending to non-financial corporations, lending to households continued to recover in the fourth quarter. Total loans to households again increased significantly in seasonally adjusted terms between October and December. Even so, the annualised three-month rate stood at just ½%, compared with not quite 1% between July and September. This growth was wholly due to loans for house purchase, which more than offset the decline in other credit and gave rise to a positive three-month rate for the third time in succession.

Less dynamic growth of credit to general government

Although the volume of credit issued to general government increased sharply in October due to the simultaneous rise in loans and securitised credit, credit growth in the fourth quarter was down overall on the two previous quarters. This was because of the considerable reduction in loans at the end of the quarter. However, for the first time in five years, the overall volume of loans to general government increased for three consecutive quarters. In seasonally adjusted and annualised terms, it increased by 2½%. Loans fell at

Loans of German banks to domestic enterprises and households

Seasonally adjusted



1 End of month; adjusted for statistical changes.

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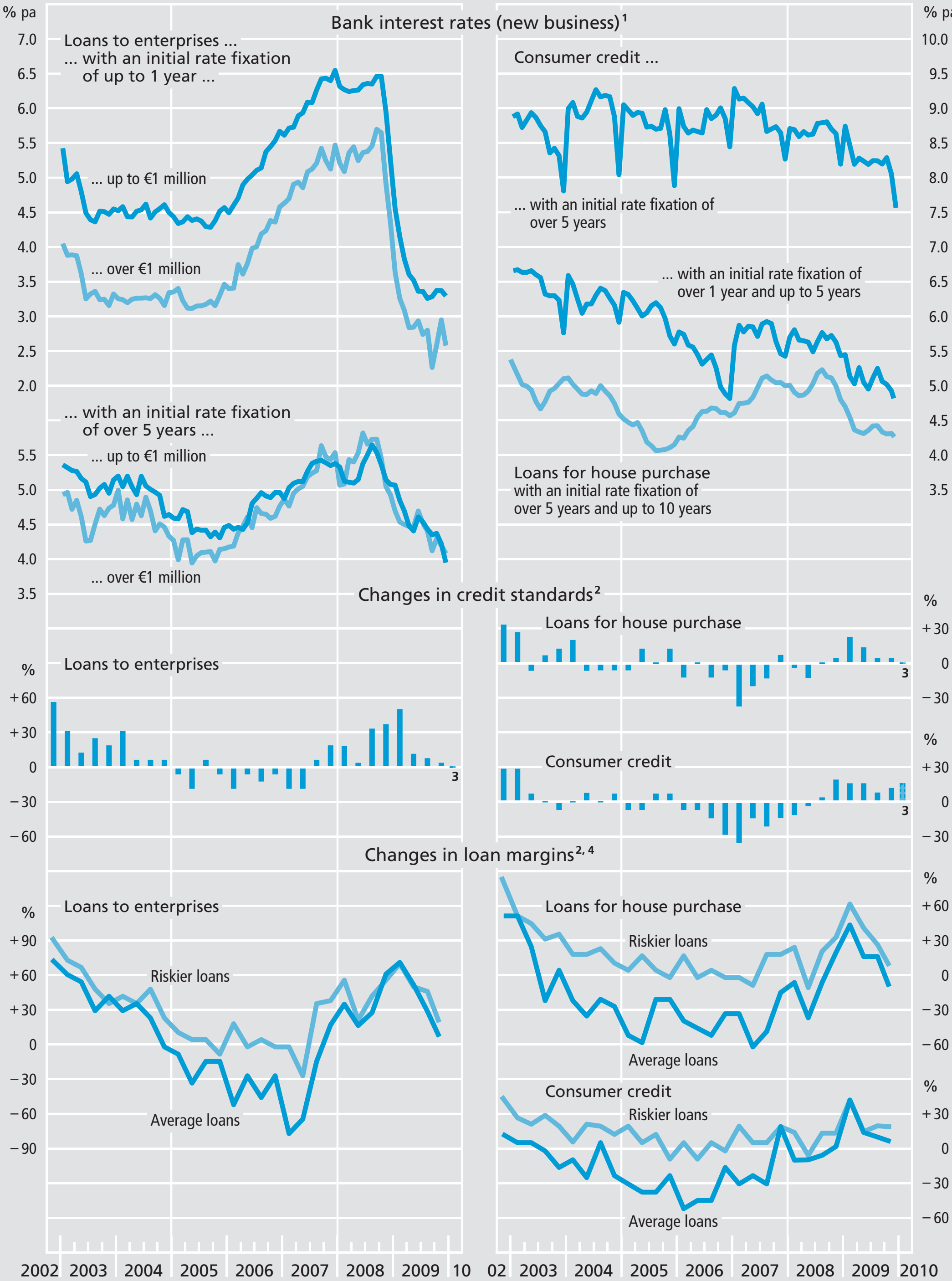
a seasonally adjusted and annualised three-month rate of just under 6% over the fourth quarter as a whole, while securitised credit grew by more than 22½%.

Credit standards barely change

In the closing quarter of 2009, banks participating in the Bank Lending Survey (BLS) barely changed their credit standards, thus confirming the impression gained in the previous quarter that a turning point had been reached in the credit cycle. In the area of loans to enterprises, industry-specific or firm-specific factors, in particular, again gave rise to more restrictive tendencies. As in the preceding quarters, lending to large enterprises was also affected by higher costs related to banks' capital position. This was countered, on the whole, by institutions' positive liquidity situation, however. Trends in margins became

Banking conditions in Germany



1 According to harmonised MFI interest rate statistics. — **2** According to the Bank Lending Survey, difference between the numbers of respondents reporting “tightened considerably” and “tightened somewhat” and the numbers of respondents reporting “eased somewhat” and “eased considerably” as a percentage of the responses given. — **3** Expectations for 2010 Q1. — **4** Reduced scale.

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calmer, with margins for average risks in corporate credit business being widened only slightly and adjustments for poorer credit ratings also declining significantly.

Credit supply conditions were therefore very largely in line with those in the euro area as a whole. By contrast, certain differences were once again evident with regard to reported funding needs. These increased in Germany, mainly as a result of debt rescheduling and caution on the part of other banks, while having decreased somewhat on balance in the euro area as a whole. For lending to households, as with loans to enterprises, it was chiefly institutions' perception of risk that led to a tightening of standards. For the first time since the third quarter of 2008, however, margins for average loans for house purchase narrowed again slightly. By contrast, riskier housing loans and lending to households for consumption purposes in both credit rating categories were again affected by expanded margins. At the same time, households' funding requirements remained unchanged on balance.

In the fourth quarter of 2009, the BLS was expanded to include a number of additional questions on the effects of the financial crisis on wholesale funding, capital costs and the lending of the participating banks as well as, for the first time, two questions on credit supply policy in 2010. The responses once again suggest that government aid measures had little influence on the funding of the surveyed German banks. Furthermore, the surveyees identified little change in access to wholesale funding via the money and capital markets. In the fourth quarter, too, half of the banks noted higher capital costs in the wake of the financial crisis, which was reflected partly in their lending. For 2010, the surveyed banks expect somewhat tighter standards, especially for credit to large enterprises and for household consumption purposes. According to the respondent institutions, this is attributable, above all, to the continuing deterioration of the perception of risk.

Little change in bank lending rates overall

According to reports for the interest rate statistics, bank lending rates, much like capital market rates, eased slightly on a broad front or remained very largely unchanged in the fourth quarter. At the end of the period under review, the reporting institutions were charging interest of 2.6% for large short-term loans to enterprises and 3.3% for small short-term loans to enterprises, and were charging 4.1% and 3.9%, respectively, for long-term loans to enterprises.[1] While bank lending rates for loans to households for house purchase remained virtually unchanged in the fourth quarter of 2009 and stood at 4.4% for long-term loans, interest rates for consumer credit fell again broadly at the end of the year in line with the seasonal pattern of recent years.

1 It should be noted that the recorded interest rate changes in December 2009 were also due to special factors.

Second special survey on German banks' lending to domestic enterprises

At the turn of 2009-10, the Bundesbank repeated the special survey which it first conducted among selected German banks and banking associations in July 2009.[1] The aim of this survey was to supplement the existing information on lending with the banks' assessments of their expected lending behaviour in the coming 12 months. In this connection, the participating institutions were also asked to forecast the development of their capital position.

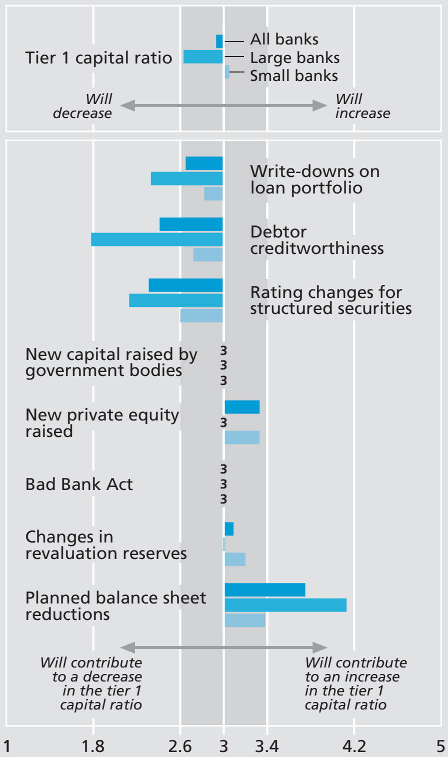
Like the first survey in the summer of 2009, the second survey provided little indication of an imminent, broad-based credit crunch in lending business with domestic enterprises. The banks' responses therefore do not bear out concerns that the German economy might be facing a shortage of credit as the upturn gets under way.

Overall, the survey participants take an optimistic view of their new lending in 2010, particularly to small and medium-sized enterprises. Even so, they do not anticipate that the total lending volume will increase significantly over the next 12 months as large write-downs are expected to have a dampening impact. On balance, the small banks surveyed expressed a somewhat more positive view of developments in their lending volume than the large institutions.

In the first survey, the participants still expected the poor outlook regarding general domestic activity as well as industry or firm-specific factors to have a dampening impact on their lending at least until the end of 2010. By contrast, in the latest survey they stated that these and other supply-side factors will probably no longer affect lending developments this year. They cited higher demand from enterprises as the only major factor driving lending in the coming 12 months; in their view, this increase in demand is likely to be reflected in a rising utilisation rate on existing credit lines and a larger overall volume of loan applications. Banks intend to respond to this by increasing their credit lines while keeping the rejection ratio constant.

While the banks taking part in the earlier survey had, on balance, expected their tier 1 capital ratio to decline in 2010, the institutions participating in the current special survey anticipate no major change over the next 12 months. They state that the need for write-downs, poorer borrower creditworthiness, and changes to the ratings of structured securities will have a negative impact on the tier 1 capital ratio. To counter this, some banks are planning to improve their tier 1 capital ratio by reducing their balance sheet, although they claim that this will not affect their lending behaviour.

Forecast of the tier 1 capital ratio for 2010, and key determinants[2]



1 See the detailed report on our website www.bundesbank.de/volkswirtschaft/vo_veroeffentlichungen.en.php. — 2 For this question, the possible responses range from "1 = will decrease considerably/will contribute considerably to a decrease of the tier 1 capital ratio" to "5 = will increase considerably /will contribute considerably to an increase of the tier 1 capital ratio". When this range is broken down into five intervals of equal width, there is an area of uncertainty between 2.6 and 3.4 (shaded in grey), which is interpreted as "will remain basically unchanged/will have basically no impact on the tier 1 capital ratio". — 3 At least 90% of the banks surveyed gave the response "not applicable" or "not stated" to this question.

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