Monetary policy and banking business

Interest rate policy and the money market

Main refinancing rate down to 1% in second quarter

Against the backdrop of persistently poor economic performance, a projected gradual recovery and the considerable euro-area slowdown in monetary dynamics in the second quarter of 2009, low current and projected inflation rates as well as reliable inflation expectations gave the Governing Council of the ECB the leeway to reduce the key policy rates by a further 0.25 percentage point in April and again in May to a level of 1%. Furthermore, the Governing Council decided to narrow the corridor around the main refinancing rate to ensure that the money market, in which activity is still ailing, was not put under additional strain by the interest rate cuts. The Eurosystem now charges 1¾% for use of the marginal lending facility and pays interest of ¼% on account balances under the deposit facility.

High demand for 12-month tender

The reduction in the main refinancing rate was accompanied by the Governing Council's decision to develop a programme to buy €60 billion worth of euro-denominated covered bonds in order to stabilise the liquidity situation of the European banking system in the medium and long term. The ECB also decided to offer, by December 2009, a total of three additional 12-month fixed-rate refinancing operations. In the first of these longer-term refinancing operations, the Eurosystem allotted a total of €442.2 billion at an interest rate of one percent on 25 June 2009. 1,121 credit institutions took part in this transaction, considerably more than the average number of participating banks in previous refinancing operations in the past 12 months.

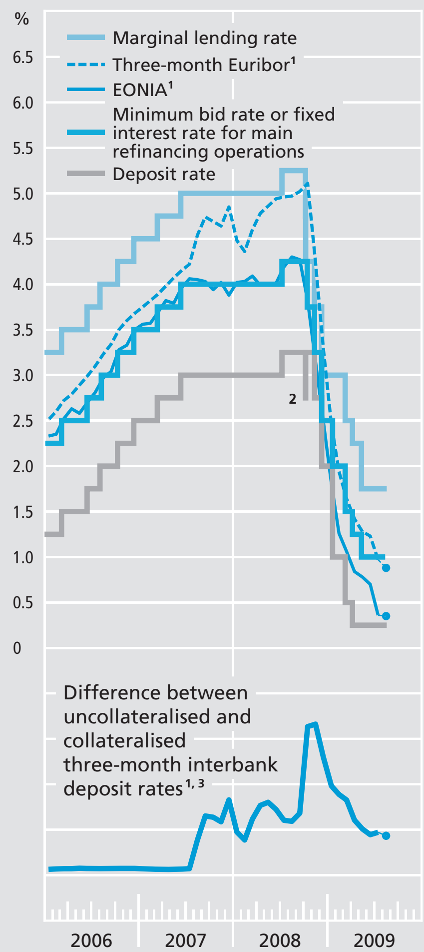
Overnight rate quoted at just over the deposit facility

As expected, the very good liquidity position of European credit institutions after the 12-month tender led to another significant drop in money market interest rates. The operation can therefore be considered an extraordinary success. The overnight rate (EONIA) fell by 0.4 percentage point and has remained relatively stable at around 0.1 percentage point above the interest rate on the Eurosystem's deposit facility. Although the trading volumes used to determine the EONIA interest rate fell sharply following the allotment of the long-term tender, activity on the overnight market recently showed signs of a slight recovery.

Longer-term money market rates down across the board

Longer-term money market rates also dipped noticeably again after the 12-month tender, in line with monetary policy. The uncollateralised three-month interest rate thus fell a further 0.3 percentage point plus, and the interest rate on uncollateralised 12-month liquidity also additionally shrank by more than 0.2 percentage point. At the same time, the money market continued to stabilise and key risk premiums continued to narrow, albeit at a slower pace. Since mid-May, the yield spread between the interest rate on uncollateralised three-month money (three-month Euribor) and its collateralised three-month counterpart (Eurepo) has fallen by around 0.1 percentage point to around 0.4 percentage point and has thus returned to the level of February 2008.

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 1-17 August 2009.

Deutsche Bundesbank

Monetary developments in the euro area

Continued deceleration of monetary expansion

Monetary expansion continued to decelerate in the euro area in the quarter under review, albeit at a slower pace. In seasonally adjusted and annualised terms, M3 increased by more than 2% in the second quarter after decreasing by a rate of just under 2½% between January and March. The three-month average of the annual growth rates for April to June

Money market management and liquidity needs

During the three reserve maintenance periods from 8 April to 7 July, euro-area credit institutions' need for central bank liquidity determined by autonomous liquidity factors fell by €12.8 billion in net terms. Although the volume of banknotes in circulation rose sharply, as is usual for the time of year, by a total of €15.8 billion (in particular due to a sharp increase of €10.2 billion in the April-May maintenance period), there was a net decrease in the liquidity requirement owing to the development of the remaining autonomous factors throughout the period under review. This resulted in general government deposits with the Eurosystem falling by a net total of €1.1 billion. In addition, if the net foreign reserves and the other factors are taken together, a move which eliminates liquidity-neutral valuation effects, an additional decline in the liquidity requirement of €27.5 billion is apparent. The demand for central bank liquidity resulting from the minimum reserve requirement also decreased in net terms, by €2.7 billion.

In the period under review, the Eurosystem's ample provision of liquidity with the aim of supporting the functioning of the money market continued to be of utmost importance. All refinancing operations continued to be carried out as fixed-rate tenders with full allotment with the same maturity structure and frequency (see table on page 29). Additionally, at its meeting on 7 May 2009, the ECB Governing Council decided to carry out additional longer-term refinancing operations with a maturity of 12 months, also in the form of fixed-rate tenders with full allotment. On this basis, the Eurosystem allotted a 12-month tender for the first time at the end of June. This had a major influence on the outstanding refinancing volume which is currently based solely on credit institutions' liquidity demand and on the shift in emphasis from main to longer-term refinancing operations. In the first two maintenance periods of the reporting period, the average volume of outstanding open market operations decreased by just over €30 billion in net terms whereas in the June-July period it increased once again, by just under €80 billion. Over the entire reporting period, the refinancing volume increased by approximately €155 billion to €835 billion in absolute terms. There was a similar trend with respect to recourse to the deposit facility which increased again very sharply after the 12-month tender, having decreased perceptibly in the April-May and May-June periods. The first-time execution of a 12-month tender also caused a clear shift in the maturity structure of the total outstanding refinancing volume, in that weekly main refinancing operations accounted for just 13% of the refinancing volume at the end of the reporting period compared with 36% at the beginning. On the last day of the maintenance periods under review, the ECB carried out fine-tuning operations to absorb excess liquidity as usual.

In the April-May reserve period, the main refinancing operations were carried out at the new fixed rate of 1.25% after the Governing Council of the ECB had approved an interest rate reduction of 25 basis points at its meeting on 2 April. The demand for liquidity from credit institutions changed very little on average compared to the previous period. The excess liquidity – measured against the autonomous factors and the reserve requirements – was approximately €90 billion on a daily average in both periods. Nevertheless, compared to the March-April period, average recourse to the deposit facility decreased by €15 billion to €43 billion. One reason for this is likely to have been the reduction in the interest rate on the deposit facility to 0.25% as a result of the cut in the key interest rate. The overnight rate did not fully mirror the reduction in the key interest rate, especially at the beginning of the maintenance period, meaning that EONIA fixings, which in the previous periods had tended to orientate more to the deposit rate, once again approached the fixed rate of the main refinancing operations (the EONIA rate was 51 basis points below the fixed rate on average over the period). However, as the market participants anticipated further cuts in the key interest rate, demand remained rather low in the longer-term refinancing operations. Consequently, the average share of total refinancing represented by main refinancing operations increased slightly to 36% compared with 34% in the previous period.

The May-June maintenance period began with the interest rate cut of 25 basis points to 1.00% which was approved by the ECB Governing Council at its meeting on 7 May and had been expected by the market participants. Simultaneously, the width of the standing facilities corridor was symmetrically reduced to 150 basis points in order to prevent the interest rate for the deposit facility from falling to 0.00%. Credit institutions' demand for central bank liquidity decreased noticeably again whereby the distribution of the demand between main and longer-term refinancing operations remained largely unchanged.

Deutsche Bundesbank

At the same time, the above-benchmark surplus in liquidity decreased markedly again to just over €30 billion on a daily average. As a result of this reduction in liquidity, recourse to the deposit facility in the Eurosystem also decreased to an average of €22 billion. A further consequence of the drop in excess liquidity was evidenced by the development of EONIA fixings. These again oriented themselves more strongly to the fixed rate of the main refinancing operations. On average over the maintenance period, they were 20 basis points below the main refinancing rate and, on four days in this period, the EONIA was even recorded above the main refinancing rate.

The June-July maintenance period was largely influenced by the introduction of the 12-month tender. Until the 12-month tender was carried out on 25 June, the total outstanding volume of longer-term refinancing operations reached its lowest levels since the introduction of the fixed-rate tender in October 2008. As the demand for liquidity in the main refinancing operations increased simultaneously, the share of total refinancing represented by main refinancing operations increased to 50%. This changed noticeably as a result of the allotment of the 12-month tender. In this tender, €442 billion was requested and allotted at a fixed rate of 1.00%. The number of bidders, at 1,121, also confirmed the credit institutions' exceptionally strong interest in this operation. As a result of the very high allotment volume, the share of total refinancing attributable to main refinancing operations decreased to an average of 16% until the end of the period and the outstanding refinancing volume temporarily reached a record high of almost €900 billion. The excess liquidity, which had fallen to an average of just over €12 billion in the maintenance period until the settlement of the 12-month operation, was €285 billion on average from the 25 June to the end of the period. After the 12-month tender had been carried out, average recourse to the deposit facility also recorded a corresponding very sharp increase to €245 billion on average until the end of the period compared to an average of €11 billion before the tender. As many credit institutions demanded significantly less liquidity in the main refinancing operation carried out on 24 June, instead switching to the 12-month tender, they experienced a one-day liquidity gap. This was bridged using, amongst other things, overnight credit with the Eurosystem. Thus, recourse to the marginal lending facility on 24 June was €29 billion. The clear effects of the new tender operation were also reflected by the development of EONIA fixings.

Factors determining bank liquidity [1]

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

Item	2009		
	8 Apr to 12 May	13 May to 9 June	10 June to 7 July
I Provision (+) or absorption (–) of central bank balances due to changes in autonomous factors			
1 Banknotes in circulation (increase: –)	– 10.2	– 2.3	– 3.3
2 General government deposits with the Eurosystem (increase: –)	– 2.9	+ 0.2	+ 3.8
3 Net foreign reserves [2]	+ 4.4	– 24.5	– 30.8
4 Other factors [2]	– 0.4	+ 29.5	+ 49.3
Total	– 9.1	+ 2.9	+ 19.0
II Monetary policy operations of the Eurosystem			
1 Open market operations			
(a) Main refinancing operations	+ 9.2	– 0.9	– 17.4
(b) Longer-term refinancing operations	– 16.2	– 26.3	+ 104.3
(c) Other operations	+ 0.6	+ 1.0	– 7.8
2 Standing facilities			
(a) Marginal lending facility	– 0.4	– 0.0	+ 0.6
(b) Deposit facility (increase: –)	+ 15.1	+ 20.4	– 97.4
Total	+ 8.3	– 5.8	– 17.7
III Change in credit institutions' current accounts (I + II)	– 0.8	– 2.9	+ 1.3
IV Change in the minimum reserve requirement (increase: –)	+ 1.1	+ 3.0	– 1.4

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.

From the beginning of the period until the allotment of the 12-month tender, the EONIA was again oriented more strongly to the fixed rate of the main refinancing operations (19 basis points lower on average). Owing to the increase in liquidity as a result of the 12-month tender, EONIA decreased noticeably. Subsequently, the spread vis-à-vis the main refinancing rate increased to an average of 63 basis points below the key interest rate.

In the July-August maintenance period, the Eurosystem began the purchase programme for covered bonds which had been agreed in the meeting of the ECB Governing Council on 7 May 2009.

fell further to 4.1% on the back of 5.6% in the previous quarter, and thus reached its lowest level in eight years.

Highly liquid M3 components in particular demand

As in the previous quarter, there were strong shifts towards the most liquid components of the monetary aggregate. Overall, the narrow monetary aggregate M1 grew in the reporting period by a seasonally adjusted and annualised 14% compared with 11% in the first three months of 2009. The growth of cash in circulation, at a seasonally adjusted and annualised rate of just under 4%, was relatively sluggish following growth of 9½% a quarter earlier. By contrast, overnight deposits rose extremely sharply, by more than 16%. They had already increased by just under 11½% in the first quarter.

Decline in marketable instruments and other short-term deposits on balance

Although the rise in overnight deposits affected almost all domestic sectors, it was particularly marked among households and other financial intermediaries. In the case of households, the growth in overnight deposits was to the detriment of short-term time deposits remunerated at market rates, in particular, which were sold in vast quantities, mainly due to ever-decreasing short-term interest rates. Overall, short-term time deposits fell by a seasonally adjusted and annualised rate of 19½% in the reporting period compared with -25% in the first quarter. Among households, in particular, short-term savings deposits were the main beneficiaries. As in the two previous quarters, they once again proved very popular. Overall, however, holdings of other short-term deposits diminished by a seasonally adjusted and annualised three-month rate of 6½% after having already shrunk by almost 9½% in the previous quarter.

Marketable instruments were once again battered by the financial crisis. They experienced a decline of 5½% between April and June on the back of -17% in the previous quarter. The significant reduction in short-term interest rates had a particular impact on demand for money market fund shares/units. However, short-term bank debt securities were also sold on balance by European non-banks, albeit to a much lesser extent than in the previous quarter. The decline in marketable instruments is attributable not just to interest rate movements but also to still existing uncertainty among investors with regard to the capital security and liquidity of these investment instruments. Monetary financial institutions in the euro area were thus once again unable to raise short-term marketable funds from domestic non-banks in the third quarter following the intensification of the financial crisis in September 2008.

Subdued lending to the private sector

As in the previous quarters, the weak underlying monetary dynamics during the reporting period has to be seen, in particular, in connection with continuing muted growth in lending. Although the growth of loans to domestic private non-banks was positive for the first time in two quarters, the seasonally adjusted and annualised three-month rate remained low at just under 1%. Even taking into account credit institutions' securitisation activities, which, in statistical terms, lead to the underreporting of banks' lending, loans to the private sector remained weak. Adjusted for the securitisation effect, loans to do-

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
08.04.09	MRO (FRT)	7	237.6	– 130.4	1.25	100.00	–	1.00	535
08.04.09	S-LTRO (FRT)	35	131.8	–	1.25	100.00	–	1.00	119
09.04.09	S-LTRO (FRT)	182	36.1	–	1.25	100.00	–	1.00	75
15.04.09	MRO (FRT)	7	249.4	67.9	1.25	100.00	–	1.00	557
16.04.09	SLTRO (FRT)	84	13.2	–	1.25	100.00	–	1.00	37
22.04.09	MRO (FRT)	7	244.1	118.6	1.25	100.00	–	1.00	563
29.04.09	MRO (FRT)	7	233.2	91.7	1.25	100.00	–	1.00	526
30.04.09	LTRO (FRT)	91	30.2	–	1.25	100.00	–	1.00	90
06.05.09	MRO (FRT)	7	234.2	89.7	1.25	100.00	–	1.00	503
12.05.09	FTO (–)	1	– 108.1	–	1.05	100.00	0.93	1.01	128
13.05.09	MRO (FRT)	7	229.6	– 136.4	1.00	100.00	–	1.00	512
13.05.09	S-LTRO (FRT)	28	116.1	–	1.00	100.00	–	1.00	113
14.05.09	S-LTRO (FRT)	91	33.7	–	1.00	100.00	–	1.00	56
14.05.09	S-LTRO (FRT)	182	20.7	–	1.00	100.00	–	1.00	97
20.05.09	MRO (FRT)	7	221.3	10.8	1.00	100.00	–	1.00	558
27.05.09	MRO (FRT)	7	276.8	23.3	1.00	100.00	–	1.00	709
28.05.09	LTRO (FRT)	91	27.5	–	1.00	100.00	–	1.00	104
03.06.09	MRO (FRT)	7	227.6	45.6	1.00	100.00	–	1.00	620
09.06.09	FTO (–)	1	– 57.9	–	0.80	100.00	0.77	1.58	101
10.06.09	MRO (FRT)	7	302.1	– 75.9	1.00	100.00	–	1.00	604
10.06.09	S-LTRO (FRT)	28	56.8	–	1.00	100.00	–	1.00	147
11.06.09	S-LTRO (FRT)	91	14.5	–	1.00	100.00	–	1.00	44
11.06.09	S-LTRO (FRT)	182	18.2	–	1.00	100.00	–	1.00	110
17.06.09	MRO (FRT)	7	309.6	16.1	1.00	100.00	–	1.00	670
24.06.09	MRO (FRT)	7	167.9	– 150.6	1.00	100.00	–	1.00	530
25.06.09	LTRO (FRT)	98	6.4	–	1.00	100.00	–	1.00	70
25.06.09	S-LTRO (FRT)	371	442.2	–	1.00	100.00	–	1.00	1,121
01.07.09	MRO (FRT)	7	105.9	335.4	1.00	100.00	–	1.00	405
07.07.09	FTO (–)	1	– 276.0	–	0.80	100.00	0.64	1.01	165

* For more information on the Eurosystem's operations from 21 January 2009 to 7 April 2009, see Deutsche Bundesbank, Monthly Report, May 2009, p 27. — **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.

Deutsche Bundesbank

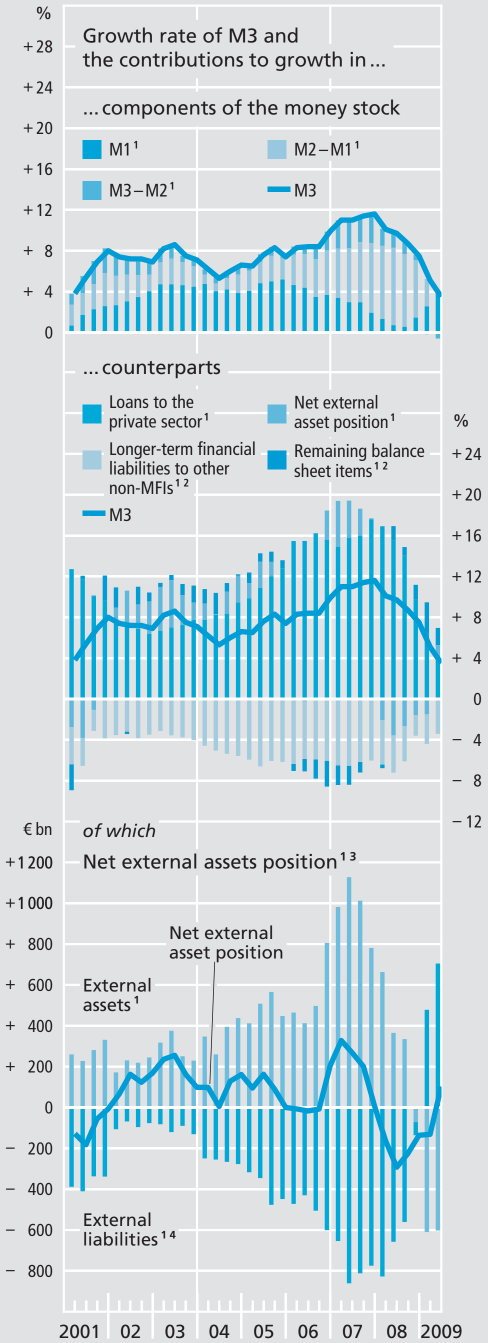
mestic private non-banks increased by a seasonally adjusted and annualised 1½% in the second quarter compared with just under ½% in the previous quarter.

Strong growth in unsecuritised loans to financial corporations...

At sectoral level, it is clear that lending growth in the second quarter was almost exclusively driven by lending to other financial intermediaries. These transactions seem to stand in direct correlation with the exceptional circumstances which still prevail in the financial markets, particularly the special role of financing and special purpose vehicles. In this respect, they do not constitute traditional lending to the private non-banking sector. In the quarter under review, loans to other financial intermediaries grew by a seasonally adjusted and annualised rate of just over 25½% compared with a decrease of more than 4½% between January and March.

Components and counterparts of the money stock in the euro area

Seasonally adjusted, quarterly



1 Calculated from the cumulative changes over 12 months. — 2 Taken in isolation, an increase curbs M3 growth. — 3 Not seasonally adjusted. — 4 Increase: –.

Deutsche Bundesbank

Credit to insurers and pension funds also increased significantly by 8% over the same three-month period after shrinking by just over 14% in the previous quarter.

... but decline in lending to non-financial corporations

By contrast, loans to non-financial corporations again decreased at an accelerated seasonally adjusted and annualised rate of 3½%. This was because of the sharp drop in unsecuritised loans with a maturity of up to one year, contrasting with a slight rise in medium-term to long-term loans. The weak borrowing was the result of both reduced demand from enterprises in the wake of a further drop in capacity utilisation and, to a certain extent, the tightening of credit supply conditions by banks. The recent increase in real financing costs and the cleanup of corporate balance sheets in some euro-area countries may have also had a negative effect on lending demand. Household borrowing was also weak in the quarter under review; unlike in the two previous quarters, however, a slight increase was recorded. This was especially true of quantitatively important housing loans, which, after falling by 1% in the previous quarter, rose by a seasonally adjusted and annualised three-month rate of almost ½%. Consumer credit, on the other hand, decreased by 3% in the period under review on the back of a slight increase in the previous quarter (1½%).

Large securities acquisitions by banks

Lending by banks in the euro area was, for the third consecutive quarter, funded to a greater extent by the purchase of securitised assets rather than the issue of loans. Banks purchased large quantities of securities issued by the public sector again in the quarter under review. This can be attributed to the rise in general government's financing requirements, but also to the fact that these securities benefit from the issuers' comparatively high credit rating and can be used as collateral for refinancing transactions in the Eurosystem. However, securities issued by the private sector in the euro area, which are generally considered riskier, also experienced an increase in the second quarter. Most of the bonds acquired by banks originate from securitisation transactions, however, and are therefore not classified as new lending to the private non-banking sector.

Significant increase in banks' net external position

Contrary to the previous quarter, more funds were provided on balance through foreign payment transactions by non-banks in the euro area in the period under review. As a result, the net external assets of the German MFI sector rose by more than €108 billion in seasonally adjusted terms in the second quarter of 2009 and, taken in isolation, thus had an expansionary effect on monetary developments.

Rise in longer-term investment at banks

By contrast, monetary growth was slowed by persistently strong monetary capital formation. Longer-term deposits in the euro area increased by a seasonally adjusted and annualised 7% in the second quarter of 2009 compared with more than 7½% in the first quarter. While banks strengthened their efforts to top up their capital and reserves, primarily through state recapitalisation measures, domestic non-banks bought large quantities of long-term time deposits, albeit at a slower rate than in the previous quarter. Most of this increased demand came from other financial intermediaries (OFIs) and thus resulted mainly from the securitisation activities of credit institutions, which usually accept long-term time deposits from their special purpose vehicles (SPVs) for securitisation. Purchases of long-term bank debt securities by domestic non-banks continued to be restrained; most new debt instruments were issued to the banking sector.

Medium-term price risks down considerably from monetary perspective

Underlying monetary dynamics – in other words, the growth relevant to inflation – slowed considerably in the reporting quarter. M3 growth was subdued in the quarter under review and bank lending to the non-financial private sector declined on balance. The inflation forecasts carried out using monetary data indicate that the price stability risks fell further in the second quarter. They hold that medium-term inflation growth is most likely to be below the 2% mark. The degree of uncertainty associated with such inflation forecasts remains high, however.

Deposit and lending business of German banks with domestic customers

Continued shifts from short-term time deposits to overnight deposits

Between April and June 2009, domestic investors topped up their deposits at German banks only slightly. In seasonally adjusted and annualised terms, investors' balances once again grew at a weakened three-month rate of 1½% after having increased at a rate of 6½% in the first quarter. There were, however, stark contrasts in the growth of the various types of short-term deposit. Domestic investors, for example, drastically reduced their holdings of short-term time deposits remu-

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

€ billion

Item	2009 Apr to Jun	2008 Apr to Jun
Deposits of domestic non-MFIs 1		
Overnight	+ 56.6	− 1.2
With agreed maturities		
of up to 2 years	− 70.8	+ 37.7
of over 2 years	+ 20.3	+ 0.7
Redeemable at notice		
of up to 3 months	+ 9.2	− 6.8
of over 3 months	+ 2.7	− 3.6
Lending		
to domestic enterprises and households		
Loans	+ 9.2	+ 19.1
Securities	+ 4.8	− 5.4
to domestic government		
Loans	− 1.6	− 1.7
Securities	+ 10.8	− 6.3

* 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 government excluding central government.

Deutsche Bundesbank

nerated at market rates (with an agreed maturity of up to two years) given the further reduction in short-term interest rates. At a seasonally adjusted and annualised rate of more than 45%, the quarter-on-quarter fall was greater than at any time since the introduction of monetary union. As in the previous quarter, highly liquid overnight deposits benefited from this development, despite their growth falling from a seasonally adjusted and annualised rate of 39% in the first quarter to 25½% in the second quarter. However, short-term savings deposits continued to grow at a positive rate, increasing by more than 10% between April and June on the back of just under 13% between January and March.

Long-term deposit business benefits from steep yield curve

Since the fourth quarter of 2008, German banks' long-term deposit business with domestic customers has benefited, in particular, from the ever-steeper yield curve. Holdings of long-term time deposits (with an agreed maturity of over two years) again rose by a strong seasonally adjusted and annualised rate of 11% in the second quarter. Long-term time deposits had already increased by respective three-month rates of more than 6% (2009 Q1) and 17% (2008 Q4). In the second quarter of 2009, too, the development of long-term time deposits was driven to a large extent by the activities of other financial intermediaries, which, following moderate expansion in the first quarter, began purchasing long-term time deposits to a greater extent between April and June. This reflects a renewed surge in securitisation activity. Long-term savings deposits (with an agreed period of notice of more than three months) also recovered in the second quarter after having slowed considerably in the first quarter. In seasonally adjusted and annualised terms, they increased by 18%. Once again, households were the main purchasers of long-term savings deposits.

Majority of lending again accounted for by financial corporations

Overall, lending between April and June was up considerably on the quarter, albeit primarily as a result of a sharp hike in securitised lending to the private sector at the end of the quarter. In seasonally adjusted and annualised terms, the total volume of outstanding loans rose by 5% in the quarter under review on the back of 1½% in the first quarter. Conversely, growth in loans to the domestic private sector was weak in the second quarter. The seasonally adjusted and annualised three-month growth rate for unsecuritised lending to domestic private debtors was just under 1½% between April and June and therefore slightly down from the previous quarter (in which the rate had been just over 2%). The majority of lending to the private sector was again accounted for by lending to financial corporations, however.

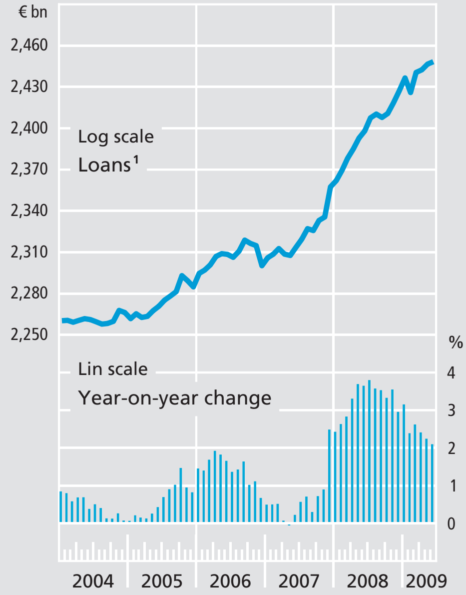
Significant drop in unsecuritised lending to non-financial corporations

By contrast, lending to non-financial corporations fell considerably by a seasonally adjusted and annualised three-month rate of -4%. This development was driven by short-term lending (with a maturity of up to and including one year) and five-year-plus loans, the growth rates of which (-21% and just under -1% respectively) were clearly negative. By contrast, there was an increase in medium-term loans (more than one and up to and including five years). In seasonally adjusted and annualised terms, these grew by a three-month rate of more than 12½%. The most important determinant of slow overall credit growth was again probably weak economic growth, which led, in particular, to lower demand for short-term loan financing for ongoing operating expenses, and is also characterised by reduced investment demand owing to severe capacity underutilisation. Furthermore, according to the Bank Lending Survey (BLS), bank lending conditions were tightened again in the second quarter, but to a lesser extent than in the two previous quarters. These data therefore provide no evidence of a widespread credit crunch in Germany at present.

Unlike unsecuritised loans to non-financial corporations, the decline in loans to house-

Loans to domestic enterprises and households

Seasonally adjusted



1 End of month; adjusted for statistical changes.

Deutsche Bundesbank

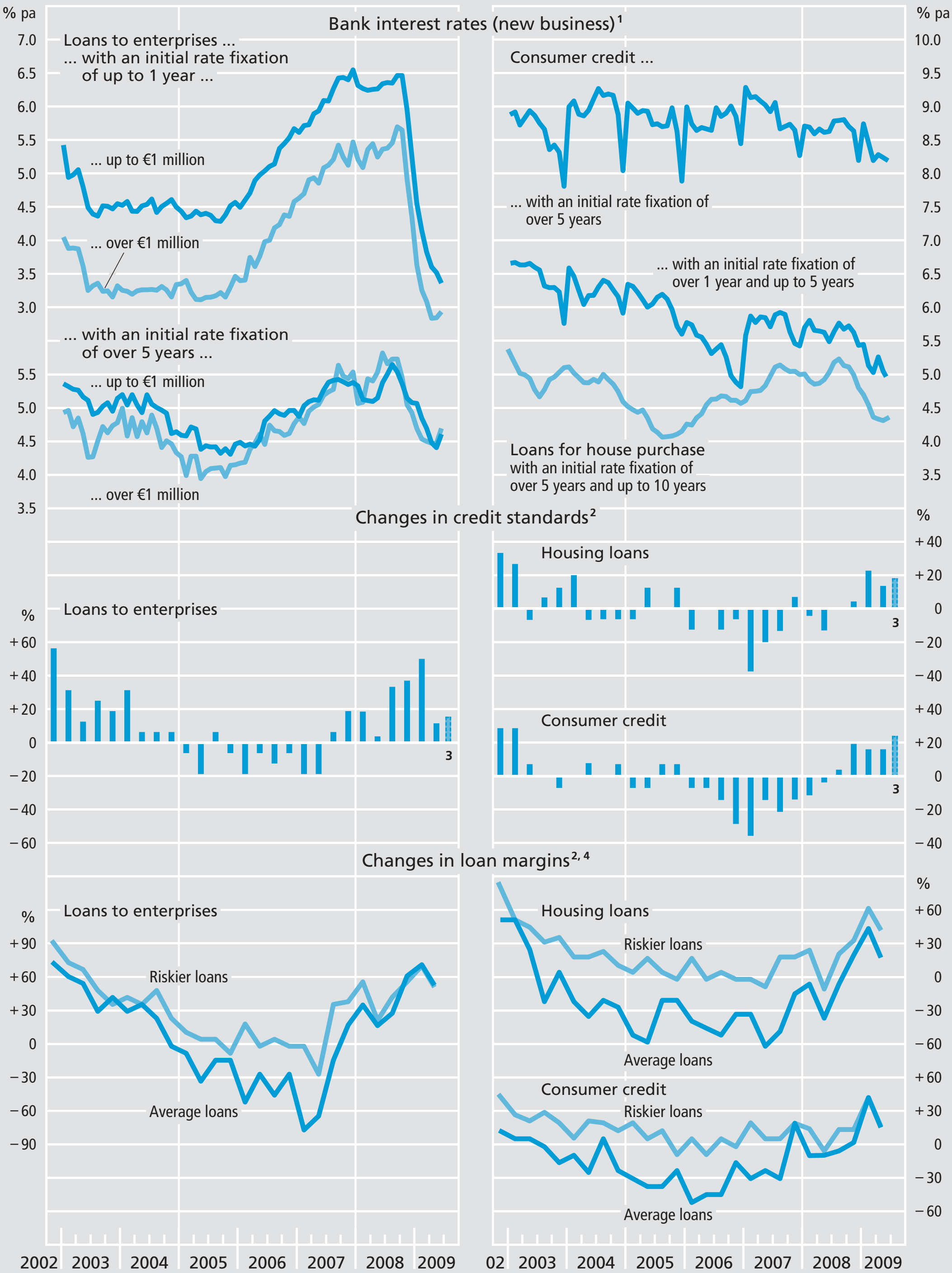
holds, which has been evident for some time, came to a standstill in the second quarter. For the first time since the third quarter of 2006, these loans increased slightly between April and June 2009, by a seasonally adjusted and annualised rate of almost ½%. The volume of outstanding housing loans and other unsecuritised loans to households both increased perceptibly.

Reduction of loans to households stopped for now

Increase in securities issued by the private sector

Most of the lending to the domestic private sector in the second quarter resulted from the sharp rise in securities issued by the domestic private sector in German banks' portfolios, however. While banks sold large quantities of these securities in April, domestic credit institutions topped up their holdings to an extremely high extent in June. On balance, the securitised lending of German banks to

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 2009 Q3. — 4 Reduced scale.

Deutsche Bundesbank

domestic private issuers rose by a seasonally adjusted and annualised three-month rate of more than 26% between April and June. Once again, however, credit institutions' securitisation activities were the main driving force behind this growth. Actual provision of funds to the domestic non-banking sector was therefore limited.

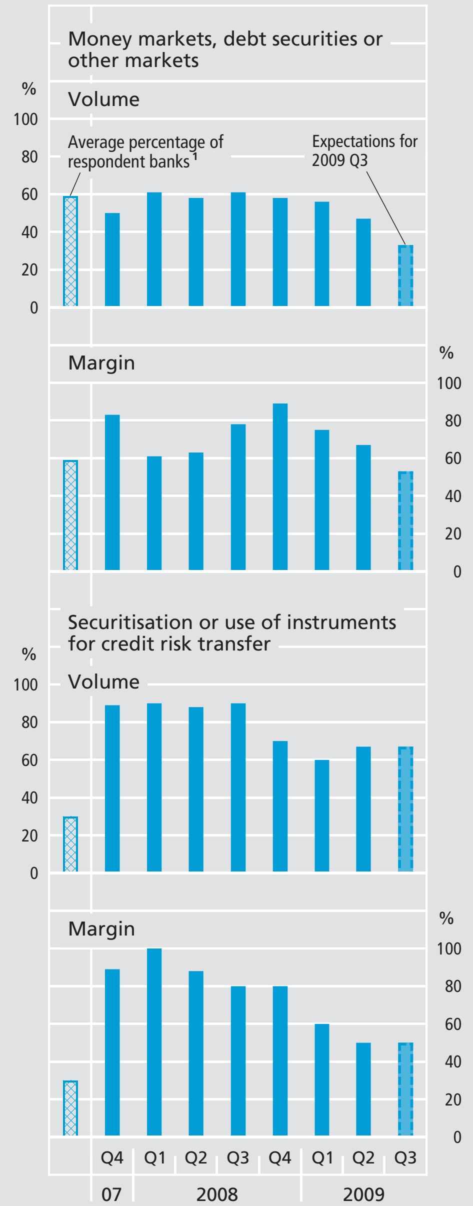
Dynamic growth of credit to general government

Credit to general government also experienced dynamic growth. In seasonally adjusted and annualised terms, it rose by 9½% in the second quarter. While loans stagnated, securitised loans were once again responsible for the increase in the provision of funds. They grew at a seasonally adjusted and annualised three-month rate of 36%, compared with just over 1% in the previous quarter.

Credit standards for enterprises only slightly more restrictive

The weak growth of domestic loans to the private sector can also be attributed to, among other things, banks' more restrictive lending policy. According to the German BLS results, the surveyed institutions tightened their credit standards for corporate business only slightly on balance in the second quarter of 2009 after having tightened them considerably in the three previous quarters. This quarter-on-quarter decline in the degree to which credit standards were tightened was the largest since the BLS was launched in 2003. The German banks surveyed stated that, besides the costs of holding capital reserves, the main reasons for the slight tightening of credit standards for corporate business were the negative influence of the general economic forecast as well as industry and firm-specific factors. At the same time, the banks surveyed again widened their margins

Funding options and lending of German BLS banks during the financial market crisis*



* Banks which reported significant or insignificant effects of the financial crisis on their credit standards as a percentage of all banks claiming to be active in the relevant market and to have been adversely affected in their wholesale funding. — **1** Banks claiming to be active in the relevant market and to have been adversely affected in their wholesale funding as a percentage of all German BLS banks; average from 2007 Q4 to 2009 Q2.

Deutsche Bundesbank

for corporate business – which is not unusual in times of interest rate cuts – considerably, more so than in the euro area.

In contrast, the lending conditions for loans to households for consumption or house purchase were only slightly more restrictive across the board. The exception to this rule was riskier loans for house purchase: the banks surveyed claimed to have increased margins significantly on balance in this business area. German results deviated most from European results in terms of demand trends. While demand for financing (with the exception of consumer credit) fell throughout the euro area, German BLS institutions observed greater demand for all types of credit under review. However, these BLS data may overstate the actual development of overall demand owing to multiple loan requests, especially from enterprises.

The survey round in the second quarter of 2009 again contained a set of additional questions on the isolated impact of the financial market crisis on the participating banks' lending policy. The responses indicated that the wholesale market refinancing problems have eased greatly since the previous quarter. However, a not insignificant number of surveyed banks still faced constraints owing to capital restrictions, impacting mainly on lending.

Drop in bank lending rates slow

By contrast, bank lending rates on new loans may have supported domestic lending to the private sector. In the wake of interest rate cuts by the Eurosystem, short-term loans to households and non-financial corporations, in particular, became much cheaper again, albeit at a significantly slower rate, despite the wider margins mentioned above. Conversely, interest rates on longer-term bank loans remained largely unchanged according to the interest rate statistics. Banks charged 3.4% or 2.9% for short-term loans to enterprises and 4.6% or 4.7% for long-term loans to enterprises depending on volume at the end of June. At 3.7% with short-term interest rate fixation, German banks were also charging much less for housing loans than at the end of March; by contrast, the interest rate on housing loans with interest rates locked in for more than five years and up to 10 years remained unchanged on the quarter at 4.4%.