Monetary policy and banking business

Monetary policy and money market developments

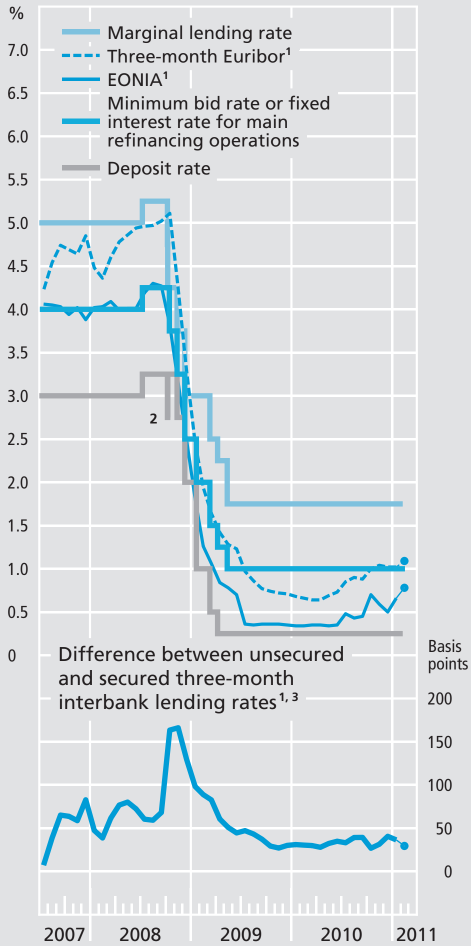
ECB Governing Council leaves key rates unchanged

The economic recovery in the euro area continued during the autumn months of 2010, spurred on by robust global economic activity and the extremely expansionary monetary policy being pursued across the world. Nevertheless, the rate of growth remained muted overall and unevenly distributed across the euro-area member states. Against this backdrop, and given muted monetary and credit growth, the Governing Council of the ECB concluded that inflation in the euro area would remain in line with price stability over the policy-relevant medium-term horizon. However, it stressed the need to monitor developments very closely, as several factors, in particular a continued upwards movement of commodity prices, could result in the risks to price stability, currently still balanced, moving to the upside in the medium term. As a result, the Governing Council decided to keep the policy rates unchanged at their historically low levels. The Eurosystem therefore remunerated balances held in the deposit facility at ¼% throughout and charged 1¾% for recourse to the marginal lending facility. The main refinancing rate remained unchanged at 1%.

Overnight rate moved away from historically low level

The final quarter of 2010 saw an upward tendency in euro money market interest rates, which can mainly be attributed to banks once again considerably reducing their excess liquidity as the last outstanding 6 and 12-month tenders expired. In addition, the pattern of the euro overnight rate (EONIA) over a minimum reserve maintenance period

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 16 February 2010.

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shifted at the start of the quarter. Whereas overnight rates had, up until then, fallen back sharply after rising briefly on the last day of a maintenance period as a result of the liquidity-absorbing fine-tuning operation, during the last quarter of 2010, EONIA sometimes remained elevated for considerably longer than previously. This meant that the spread between the overnight rate and the main refinancing rate fell from almost 60 basis points on average in the previous quarter to just over 40 basis points in the final quarter. Following the first meeting of the ECB Governing Council in January, EONIA rose very sharply after having declined continuously during the last maintenance period of 2010, and at times was noticeably above the main refinancing rate for several consecutive days.

Exit from non-standard monetary policy measures still delayed

Given the renewed intensification of the sovereign debt crisis in several euro-area countries during the fourth quarter, the Governing Council at the start of December decided to maintain its policy of full allotment in all liquidity-providing operations at least until the end of the first quarter of 2011. The interest rate indexation of its regular longer-term refinancing operations with a maturity of three months, which has been applied since October, was also extended for the first quarter of the new year. Full allotment at the fixed rate of 1% was continued for the main refinancing operations and for refinancing operations with a maturity of one maintenance period.

Securities purchase programme continued

The Eurosystem's purchase programme for public and private debt securities (Securities Market Programme, SMP) was also continued, but the liquidity it supplied was regularly absorbed. With the exception of two liquidity-absorbing operations at the end of December and start of February, every operation of this type was oversubscribed. The first of the two undersubscribed liquidity-absorbing operations was overshadowed by the imminent turn of the year, whereas the

Open market operations of the Eurosystem*

Value date	Type of transaction[1]	Maturity in days	Actual allotment in € billion	Deviation from the benchmark in € billion[2]	Marginal rate/fixed rate %	Allotment ratio %	Weighted rate %	Cover ratio[3]	Number of bidders
13.10.10	MRO (FRT)	7	186.0	– 9.0	1.00	100.00	–	1.00	145
13.10.10	S-LTRO (FRT)	28	52.2	–	1.00	100.00	–	1.00	34
13.10.10	FTO (–)	7	– 63.5	–	0.75	22.30	0.60	1.62	59
20.10.10	MRO (FRT)	7	184.0	55.0	1.00	100.00	–	1.00	151
20.10.10	FTO (–)	7	– 63.5	–	0.75	25.16	0.66	1.64	67
27.10.10	MRO (FRT)	7	183.4	43.9	1.00	100.00	–	1.00	190
27.10.10	FTO (–)	7	– 63.5	–	0.74	18.58	0.67	1.43	53
28.10.10	LTRO (FRT)	91	42.5	–	[4] 1.00	100.00	–	1.00	132
03.11.10	MRO (FRT)	7	178.4	97.4	1.00	100.00	–	1.00	144
03.11.10	FTO (–)	7	– 63.5	–	0.62	57.15	0.57	1.43	61
09.11.10	FTO (–)	1	– 148.4	–	0.80	100.00	0.78	1.00	147
10.11.10	MRO (FRT)	7	175.0	– 22.0	1.00	100.00	–	1.00	146
10.11.10	S-LTRO (FRT)	28	63.6	–	1.00	100.00	–	1.00	44
10.11.10	FTO (–)	7	– 64.0	–	0.80	92.70	0.68	1.14	50
11.11.10	FTO (+)	6	12.6	–	1.00	100.00	–	1.00	23
17.11.10	MRO (FRT)	7	186.0	73.0	1.00	100.00	–	1.00	177
17.11.10	FTO (–)	7	– 65.0	–	0.73	5.55	0.63	1.24	61
24.11.10	MRO (FRT)	7	177.1	53.6	1.00	100.00	–	1.00	165
24.11.10	FTO (–)	7	– 66.0	–	0.51	92.29	0.45	1.39	60
25.11.10	LTRO (FRT)	91	38.2	–	[4] ...	100.00	–	1.00	189
01.12.10	MRO (FRT)	7	179.7	101.2	1.00	100.00	–	1.00	163
01.12.10	FTO (–)	7	– 67.0	–	0.48	22.65	0.41	1.16	52
07.12.10	FTO (–)	1	– 147.0	–	0.80	100.00	0.79	1.00	139
08.12.10	MRO (FRT)	7	197.3	– 2.7	1.00	100.00	–	1.00	155
08.12.10	S-LTRO (FRT)	42	68.1	–	1.00	100.00	–	1.00	56
08.12.10	FTO (–)	7	– 69.0	–	0.72	39.91	0.65	1.43	56
15.12.10	MRO (FRT)	7	187.8	151.3	1.00	100.00	–	1.00	159
15.12.10	FTO (–)	7	– 72.0	–	0.55	60.25	0.49	1.34	57
22.12.10	MRO (FRT)	7	193.5	26.0	1.00	100.00	–	1.00	160
22.12.10	FTO (–)	7	– 72.5	–	0.60	97.33	0.42	1.12	44
23.12.10	LTRO (FRT)	98	149.5	–	[4] ...	100.00	–	1.00	270
23.12.10	FTO (+)	13	20.6	–	1.00	100.00	–	1.00	32
29.12.10	MRO (FRT)	7	227.9	208.4	1.00	100.00	–	1.00	233
29.12.10	FTO (–)	7	– 60.8	–	1.00	100.00	0.66	1.00	41
05.01.11	MRO (FRT)	7	195.7	184.2	1.00	100.00	–	1.00	179
05.01.11	FTO (–)	7	– 73.5	–	0.45	93.04	0.38	1.25	68
12.01.11	MRO (FRT)	7	180.1	132.1	1.00	100.00	–	1.00	169
12.01.11	FTO (–)	7	– 74.0	–	0.45	32.73	0.41	1.34	65
18.01.11	FTO (–)	1	– 135.0	–	0.80	100.00	0.79	1.00	142

* For more information on the Eurosystem's operations from 14 July 2010 to 12 October 2010, see Deutsche Bundesbank, Monthly Report, November 2010, p 25. — **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** Calculation according to publication after MRO allotment. — **3** Ratio of total bids to the allotment amount. — **4** The interest rate corresponds to the average minimum bid rate of the MROs conducted over the life of this operation.

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second was presumably attributable to the noticeable reduction in excess liquidity.

Longer-term money market rates continue upward trend

Between October and January, longer-term unsecured euro-area money market rates continued the upward tendency they had begun in the second quarter. After a noticeable increase at the beginning of October, prices did fall slightly until year-end. As with the overnight rate, however, the increase picked up again after the Governing Council's first monetary policy meeting in 2011. As this publication went to press, the interest rate on unsecured interbank liquidity with a three-month maturity (three-month Euribor) stood at around 1.10% – its highest level since mid-2009. Secured money market rates (Eurepo) showed a similar development but with markedly greater volatility than their unsecured counterparts. Central bank liquidity

Money market management and liquidity needs

During the three maintenance periods from 13 October 2010 to 18 January 2011, euro-area credit institutions' need for central bank liquidity as determined by autonomous liquidity factors fell by €36.8 billion in net terms. A decline in government deposits with the Eurosystem was a contributory factor, lowering credit institutions' liquidity needs by a total of €15.1 billion in the period under review. The combined analysis of net foreign assets and other factors, a move which eliminates valuation effects with no impact on liquidity, shows that net liquidity of €41.5 billion was provided over the three periods. This was mainly the result of emergency liquidity assistance measures in individual countries as well as the fact that several national central banks of the Eurosystem increased their holdings of euro-denominated securities not related to monetary policy. While these factors provided liquidity, the increased volume of banknotes in circulation had an absorbing effect. Banknotes in circulation rose – chiefly owing to the usual seasonal increase around Christmas – by €19.8 billion net in the period under review. On 24 December 2010, banknotes in circulation in the Eurosystem reached a new high of €842 billion. The minimum reserve requirement dropped by a total of €1.3 billion during the three maintenance periods and thereby amplified the effect of reduced liquidity needs arising from autonomous factors.

This period under review was also characterised by a generous supply of liquidity, with which the Eurosystem's liquidity management met credit institutions' demand for central bank liquidity – over and above the benchmark amount – and helped ensure the smooth functioning of the money market. Liquidity-providing open-market operations continued to be carried out as fixed-rate tenders with full allotment of the submitted bids, which meant that liquidity provision was determined by demand from credit institutions (see table on page 25). At its meeting on 2 December 2010, the Governing Council of the ECB decided to continue the full allotment policy both in main and longer-term refinancing operations at least until the end of the March-April 2011 maintenance period. The three-month refinancing operations will again be allotted at the fixed rate, which is indexed to the average of the minimum bid rates of the main refinancing operations over the life of this operation.

Aided by the expiry of the last outstanding six-month tender in mid-November 2010 and of the third 12-month tender at the end of December 2010, a further shift occurred during the three maintenance periods away from longer-term towards shorter-term central bank refinancing. Comparing period averages, the volume of main refinancing operations grew by roughly €33 billion (net) in the observation period, while the volume of longer-term refinancing operations fell by €76 billion. Furthermore, the recovery of the interbank market, which had commenced after the first one-year tender expired at the beginning of July 2010, continued in the period under review, with money market turnover and interest rates in some cases considerably exceeding the averages of the first half of the year.

Moreover, the Eurosystem continued to purchase bonds under the Securities Markets Programme (launched in May 2010) and increased its holdings throughout the three maintenance periods by around €13 billion to €76.5 billion. However, the weekly liquidity-absorbing fine-tuning operations taking place at the same time almost fully re-absorbed the liquidity provided by these purchases. Only in the last liquidity-absorbing operation in December did absorption fall slightly short of the intended amount, due to special factors at year-end. Independently of these weekly quick tenders, the Eurosystem continued to conduct a liquidity-absorbing fine-tuning operation on the last day of every maintenance period throughout the period under review in order to withdraw excess central bank liquidity.

The October-November 2010 maintenance period was marked by reduced central bank liquidity compared with the previous period after the second 12-month tender had expired at the end of September and credit institutions had only rolled over part of the amount due into other tenders. The associated decline in excess liquidity, ie the central bank liquidity exceeding the benchmark amount, led to perceptibly lower average recourse to the deposit facility of €42 billion (previous period €69 billion). Simultaneously, the EONIA rose significantly to average 0.71% over the period (after 0.48% in the previous period), while underlying turnover remained virtually unchanged at €46.2 billion.

At the beginning of the November-December 2010 maintenance period, the Eurosystem conducted an additional six-day liquidity-providing fine-tuning operation in order to bridge the gap between the last expiring six-month

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tender (repayment of €36 billion) and the next main refinancing operation. However, as demand was only just under €13 billion in this six-day tender, the outstanding tender volume declined to €514 billion and rose only slightly to up to €525 billion by the end of the period. Nevertheless, the EONIA fixings gradually decreased during the period and were – at an average of 0.58% – noticeably lower than in the previous period. Underlying unsecured turnover also declined to an average of €41.1 billion. By contrast, turnover of secured overnight money on Eurex Repo's GC Pooling trading platform rose to €12.4 billion on average over the period after it had already increased to an average of €9.7 billion in the previous period (period before that: €8.0 billion). Recourse to the deposit facility averaged €45 billion over the period, whereas the marginal lending facility was used perceptibly more in this period (€1.9 billion on average) than in the two other maintenance periods of the period under review (only €0.8 billion and €0.5 billion respectively).

The six-week long maintenance period December 2010-January 2011 included the expiry of the last 12-month tender, which resulted in a total of €97 billion maturing shortly before Christmas. In order to mitigate the liquidity outflow and to prevent possible tensions around the Christmas holiday period and the end of the year, the Eurosystem conducted a liquidity-providing thirteen-day bridge operation in addition to the regular three-month tender. This tender settled on the maturity date of the 12-month tender and also covered the year end. Of the total of €201 billion maturing on 23 December, around €170 billion was ultimately rolled over into the bridge tender (€21 billion) and the three-month tender (€149 billion). Furthermore, credit institutions noticeably raised demand for liquidity in the last main refinancing operation of the year by over €34 billion, which meant that the turn of the year passed off smoothly from a liquidity management point of view. Owing to the somewhat higher liquidity supply, recourse to the deposit facility also increased in this maintenance period to €66 billion on average. The EONIA, which had stood at 0.72% at the beginning of the period, subsequently steadily decreased to as little as 0.36%. In addition to the comfortable liquidity conditions, the high level of credit institutions' current accounts in the first days of the maintenance period, which allowed reserve requirements to be met early (frontloading), led to falling overnight rates. Only at the end of the year and the end of the maintenance period was the EONIA – in line with seasonal patterns – fixed distinctly higher at 0.82% and 0.81% respectively. At the same time, on average over the period, unsecured EONIA turnover (€40.4 billion) as well as secured overnight turnover on GC Pooling (€12.4 billion) were virtually unchanged compared to the previous period.

In the subsequent maintenance period (January-February 2011), the EONIA rose markedly and on several occasions exceeded the main refinancing rate of 1.00% as a result of perceptibly lower excess liquidity.

Factors determining bank liquidity[1]

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

Item	2010		2011
	13 Oct to 9 Nov	10 Nov to 7 Dec	8 Dec to 18 Jan
I Provision (+) or absorption (–) of central bank balances due to changes in autonomous factors			
1 Banknotes in circulation (increase: –)	+ 0.6	– 2.4	– 18.0
2 Government deposits with the Eurosystem (increase: –)	+ 4.3	– 2.3	+ 13.1
3 Net foreign assets[2]	– 20.0	– 0.2	+ 16.4
4 Other factors[2]	+ 32.2	+ 7.1	+ 6.0
Total	+ 17.1	+ 2.2	+ 17.5
II Monetary policy operations of the Eurosystem			
1 Open market operations			
(a) Main refinancing operations	+ 18.5	– 3.5	+ 17.5
(b) Longer-term refinancing operations	– 52.6	– 3.7	– 19.7
(c) Other operations	– 7.8	+ 3.9	+ 7.8
2 Standing facilities			
(a) Marginal lending facility	+ 0.1	+ 1.1	– 1.4
(b) Deposit facility (increase: –)	+ 26.9	– 2.8	– 21.8
Total	– 14.9	– 5.0	– 17.6
III Change in credit institutions' current accounts (I + II)	+ 2.1	– 2.7	– 0.1
IV Change in the minimum reserve requirement (increase: –)	– 2.1	+ 2.2	+ 1.2

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.

with a three-month maturity was trading at just under 0.8% on the secured money market as this report went to press, which is just under 30 basis points higher than at the end of the third quarter. The yield spread between the unsecured and secured money market rate (depo-repo spread), which can be interpreted as a risk premium, also experienced strong volatility in the fourth quarter. Due to a marked rise in the secured interest rate following the expiry of the second 12-month tender, the interest rate spread on the three-month maturity narrowed to around 23 basis points – its lowest level since the start of the financial market turmoil in August 2007. By the turn of the year, the risk premium had doubled to just under 46 basis points, but narrowed once again to around 30 basis points by mid-February.

Monetary developments in the euro area

Muted monetary developments in fourth quarter of 2010

Monetary expansion in the euro area weakened perceptibly in the last quarter of 2010 after having accelerated noticeably during the two previous quarters. In seasonally adjusted and annualised terms, the three-month rate of the broad monetary aggregate M3 amounted to just under 1% in the final quarter of 2010, and was therefore almost 3 percentage points below the corresponding value for the months July to September. The annual growth rate of M3 rose from 1.1% to 1.7% during the same period, which was, in part, attributable to a base effect, however.

Demand for highly liquid M3 components still declining

Looking at monetary assets, growth in overnight deposits was again less in the reporting period than in the preceding quarters. As currency in circulation was simultaneously even reduced slightly from October to December, the seasonally adjusted and annualised three-month rate for the narrow monetary aggregate M1 fell to 1½% in this period, its lowest level since mid-2008.

Net reduction of other short-term deposits

Furthermore, monetary growth during the reporting quarter was also weakened by developments in other short-term deposits, where holdings fell slightly on the quarter. Their seasonally adjusted and annualised three-month rate of -1½% was noticeably below that of the previous quarter. A determining factor in this development may be the fact that, in the fourth quarter, interest rates at the long end of the yield curve rose more sharply than at the short end. The increasing interest rate disadvantage of short-term deposits could have caused investors to shift into longer-term investments.

Marketable instruments see inflows

M3 growth was strengthened by positive developments in marketable instruments during the reporting period, which was chiefly due to sharp growth in repo transactions. Although these transactions were, as usual, undertaken mainly by other financial intermediaries, there was also clear demand for this investment from non-financial corporations again for the first time since mid-2009. This growth went a long way towards compensating for the ongoing reduction in money market fund shares and short-term bank debt securities, particularly as this had slowed overall in comparison to the first half of 2010.

Expansion of lending business with domestic non-banks ...

Among the counterparts of M3, lending by banks resident in the euro area to domestic non-banks was again of particular significance for monetary expansion in the final quarter of 2010. The extraordinarily sharp rise in MFI loans to government during the reporting period is particularly striking. The rise was, however, largely attributable to transactions conducted between the Hypo Real Estate (HRE) Group and the FMS Wertmanagement resolution agency. The latter operates as a public-law entity for the HRE group and is for statistical purposes classified as part of the government sector.

... with divergent sectoral developments

By contrast, lending by banks to the domestic private sector weakened significantly during the reporting quarter, which on balance was solely the result of lower securitised lending, however. Yet unlike securitised lending, unsecuritised loans with a seasonally adjusted and annualised three-month rate of just under 2½% grew virtually just as fast as during the third quarter. In sectoral terms, loans were primarily granted to households, where strong growth was once again driven by loans for house purchase, which make up the lion's share of household borrowing and continue to benefit from historically favourable financing conditions. By contrast, loans to non-financial corporations decreased noticeably during the period under review with a seasonally adjusted and annualised three-month rate of just over -2%, after having recorded noticeable growth in the previous quarter for the first time in six quarters. Judging by the results of the quarterly bank lending survey for the euro area, the subdued underlying demand for loans was primarily attributable to the good availability of internal funds for non-financial corporations. Furthermore, euro-area banks' lending operations to the domestic private sector in the months October to December were characterised by a strong rise in loans to other financial intermediaries. However, as such loans mainly constitute indirect interbank business, they are not *per se* accompanied by lending to the private non-banking sector.

Monetary developments in the euro area

Changes in € billion, seasonally adjusted

Monetary aggregate in a balance sheet context	2010 Q3	2010 Q4
Monetary aggregate M3 (=1+2-3-4-5)	86,767	19,235
of which Components:		
Currency in circulation and overnight deposits (M1)	35,286	16,622
Other short-term deposits (M2-M1)	66,712	– 14,148
Marketable instruments (M3-M2)	– 15,231	16,761
Counterparts		
1. Total credit to non-MFI in the euro area	178,106	190,696
of which		
Credit to general government	31,779	151,567
Credit to private-sector non-MFIs in the euro area	146,327	39,129
2. Net external assets	– 21,776	– 49,604
3. Central government deposits	– 9,947	54,304
4. Longer-term financial liabilities to other non-MFIs in the euro area	110,256	67,105
5. Other counterparts of M3 (residual)	30,746	– 448

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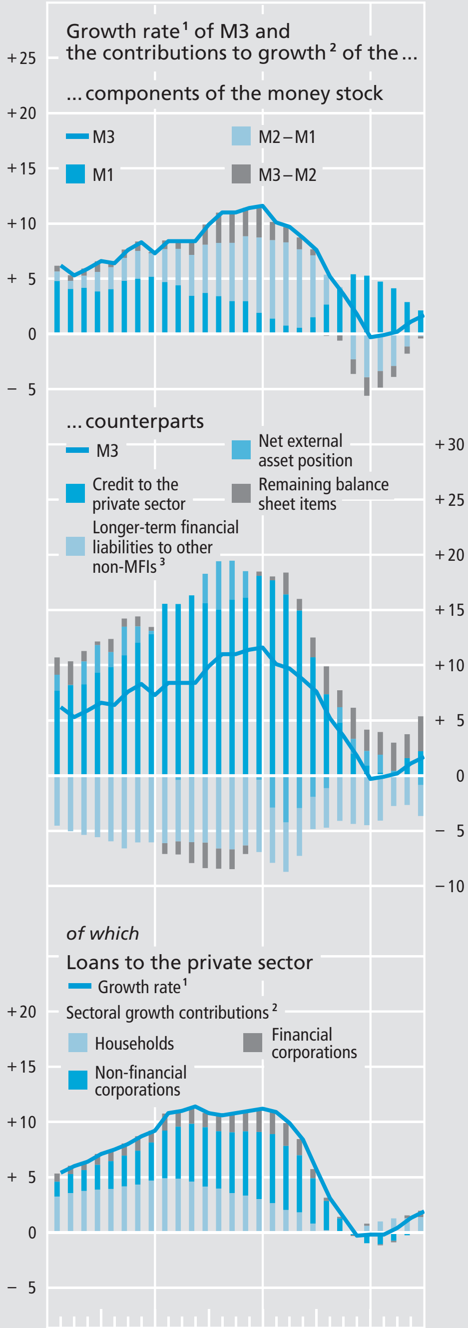
Clear monetary capital formation with noticeable fall in net external asset position

Finally, M3 growth in the final quarter of 2010 was again restrained by a significant rise in monetary capital, meaning longer-term deposits, bank debt securities and banks' capital (which are not part of M3), increased by a seasonally adjusted and annualised three-month rate of just under 4% as this report went to press. There were additionally

Components and counterparts of the money stock in the euro area

Seasonally adjusted, quarterly



1 In percent, 12-month flows. — **2** In percentage points. — **3** Taken in isolation, an increase curbs M3 growth.

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noticeable outflows of funds from net external assets of banks (MFIs) vis-à-vis non-euro-area residents. This factor, which also subdues M3 growth, must partly be seen in connection with the transfer of HRE Group assets to their resolution agency, however.

No pronounced risks to price stability from a monetary perspective

Considered as a whole, the underlying monetary dynamics – in other words, that monetary growth that is ultimately relevant to inflation – remained muted in the fourth quarter of 2010. In line with this, inflation risk indicators based on monetary data continue to indicate that there is no pronounced risk to price stability in the euro area over the policy-relevant horizon. However, the high degree of uncertainty associated with these indicators at present should not be overlooked.

German banks' deposit and lending business with domestic customers

Less demand for short-term bank deposits of late

The upward trend in deposit growth among German banks, which has been observed since the start of 2010, did not continue in the final quarter. In fact, the seasonally adjusted and annualised three-month rate for bank deposits fell to 1% compared with 3½% in the previous quarter. This was fuelled by waning momentum in short-term bank deposits, which in turn was presumably mainly attributable to the recent rise in the remuneration of longer-term investments. As in the euro area as a whole, highly liquid overnight deposits received fewer net inflows again on the quarter, which is likely due to their comparatively low remuneration. By contrast, inflows to short-term savings deposits (redeemable at notice of up to three months), especially from households, were on a par with the preceding quarters. Short-term time deposits (with an agreed maturity of up to two years) declined again in the final quarter of 2010 after recording slight net inflows in the previous quarter, albeit at a significantly reduced pace than in the preceding quarters.

Slowdown in reduction of longer-term deposit types

Longer-term bank deposits were reduced further overall in Germany in the last quarter of 2010, but at a slower rate than in the previous quarter. The general upward tendency observed for yields in Germany was not matched by interest rates for longer-term deposits. Longer-term time deposits (with an agreed maturity of over two years) were therefore reduced further by insurance companies and pension funds, which traditionally represent the most important investor group in this area. These deposits stagnated across all sectors in the final quarter. Moreover, households reduced their holdings of long-term savings deposits (redeemable at notice of over three months) more or less as strongly as in the two preceding quarters.

Banks' lending business driven strongly by special factors

Domestic banks' lending business with domestic customers enjoyed an extraordinarily strong revival in the final quarter of 2010. This increase, which was stronger than that for the euro area as a whole, was reflected in a rise in the seasonally adjusted and annualised three-month rate from just over -2½% in the third quarter to 13% in the reporting period. This revival is, however, mainly explained by transfers between the banking and government sectors in connection with the establishment of the FMS Wertmanagement resolution agency by the HRE Group. Credit to the domestic private sector also increased strongly in the reporting period, however. This was due to German banks acquiring securities from private issuers and, more significantly in terms of volume, by them increasing their holdings of private sector loans with a seasonally-adjusted and annualised three-month rate of just under 4% in the fourth quarter, after just under -3% in the previous quarter. But the vast majority of these holdings are loans to financial corporations, which had decreased sharply in the previous quarter and have been exceptionally volatile on the whole since the financial crisis intensified in the autumn of 2008.

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

Changes in € billion, seasonally adjusted

Item	2010 Q3	2010 Q4
Deposits of domestic non-MFIs [1]		
Overnight	15.3	13.5
With agreed maturities		
of up to 2 years	1.1	– 11.9
of over 2 years	1.1	0.0
Redeemable at notice		
of up to 3 months	11.8	8.7
of over 3 months	– 5.9	– 3.7
Lending		
to domestic enterprises and households		
Loans	– 16.8	21.9
of which: to households [2]	2.5	5.1
to non-financial corporations [3]	– 3.4	– 1.6
Securities	– 9.4	3.3
to domestic general government		
Loans	– 3.2	69.9
Securities	6.9	3.9

* 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 Including non-profit institutions serving households. — 3 Including non-financial quasi-corporations.

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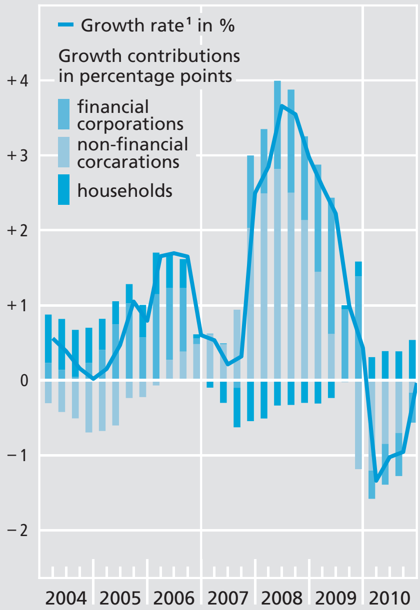
Loans of German banks to selected domestic sectors

seasonally adjusted, quarterly



1 Year-on-year rate of change.

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Lending to non-financial corporations sees outflows

In addition, domestic households also increased their debt levels further. But growth in lending to households, at a seasonally adjusted and annualised three-month rate of 1½%, compared with just over ½% in the previous quarter, was still weaker than in the euro area as a whole. The growth in Germany stemmed both from loans for house purchase and consumer loans, with the former likely to have benefited from favourable mortgage rates and the latter from households' optimistic expectations regarding the economy. Domestic non-financial corporations slightly reduced their net borrowing/loans from domestic banks again in the final quarter of 2010, particularly in the short-term segment. Although the annualised and seasonally adjusted three-month rate rose from just over -1½% to just under -1%, it could not match the positive growth observed in the second quarter of 2010. Therefore, looking at 2010 as a whole, the level of corporate exposure stagnated with fluctuating monthly changes. The German economy's sharp upward movement in 2010 has therefore not yet led to accelerated lending to the corporate sector. One factor was probably that the economic upswing provided non-financial corporations with better access to alternative sources of funding, particularly internally generated financial resources.

Credit supply conditions in Germany slightly relaxed

The results of the latest Bank Lending Survey (BLS) indicate slightly more relaxed credit supply conditions in Germany during the last quarter of 2010. The positive risk assessment by the participating banks, especially the good expectations regarding general economic activity, was the main reason for the somewhat eased credit standards for loans to small and medium-sized enterprises and in the consumer credit business. The margins for average-risk loans contracted in almost all business areas, whereas higher-risk loan margins expanded – except for loans for consumption purposes. In this credit segment, demand also stagnated, while there was a noticeable increase in interest from households in loans for house purchase and from enterprises for funds for fixed investment as well as inventories and working capital. Banks expect credit standards to ease further in the first quarter of 2011, and as usual appear optimistic as regards demand expectations.

For the first time since the outbreak of the financial crisis, there were on balance no fur-

Fourth special survey on German banks' lending to domestic enterprises

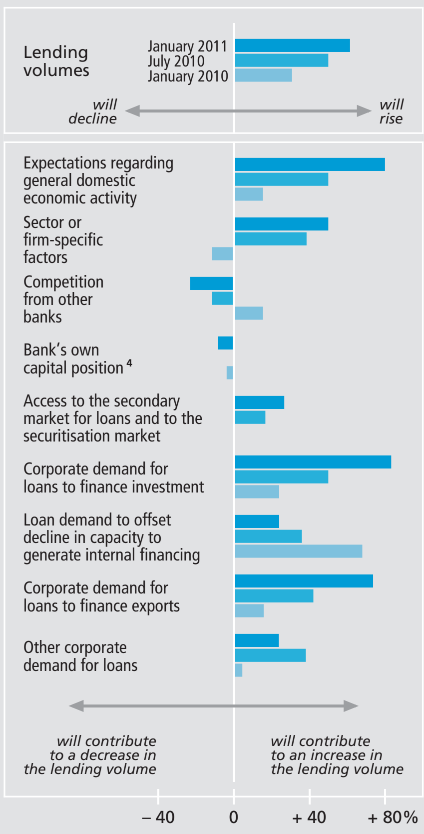
In January 2011, the Deutsche Bundesbank conducted its fourth special survey among selected German banks.[1] The main aim of this survey is to gauge how banks expect their lending business with domestic non-financial corporations to develop over the next twelve months. This time, the banks were also asked what measures they are likely to take in response to the tighter regulations in the context of Basel III.[2]

Like the previous surveys, the current round does not indicate any bottlenecks in relation to bank loans to enterprises. The survey participants expect loan volume to rise significantly in 2011, predominantly due to loans to small and medium-sized enterprises (SMEs). A contributory factor in the strong growth in new lending is the increased use of existing credit lines. Repayments, particularly by large enterprises, continue to have a dampening effect on the credit aggregate. Write-downs are now virtually negligible.

The surveyed banks believe that the expected rise in the loan volume will, as before, be attributable in particular to the economic upturn as well as to increased corporate demand for loans to finance investment and exports (see adjacent chart). This development will also be supported by banks' increasing willingness to grant syndicated loans, by their good liquidity position, increasing access to the secondary market for loans and to the securitisation market, as well as higher demand for loans as a replacement for internal financing. Thus the expected growth in lending stands on a considerably broader base than a year ago. According to the respondents, greater competition from other banks, the increased importance of the capital market as an alternative source of funding as well as higher capital costs for the surveyed institutions in the case of loans to large enterprises will have a dampening effect in 2011.

Despite growth in lending and the strains from the euro-area sovereign debt crisis, the surveyed banks forecast rising capital ratios for 2011. They aim to achieve this predominantly by retaining profits, raising new equity and reducing other risk-weighted assets. In the wake of "Basel III", the institutions currently plan in particular to raise their regulatory capital.

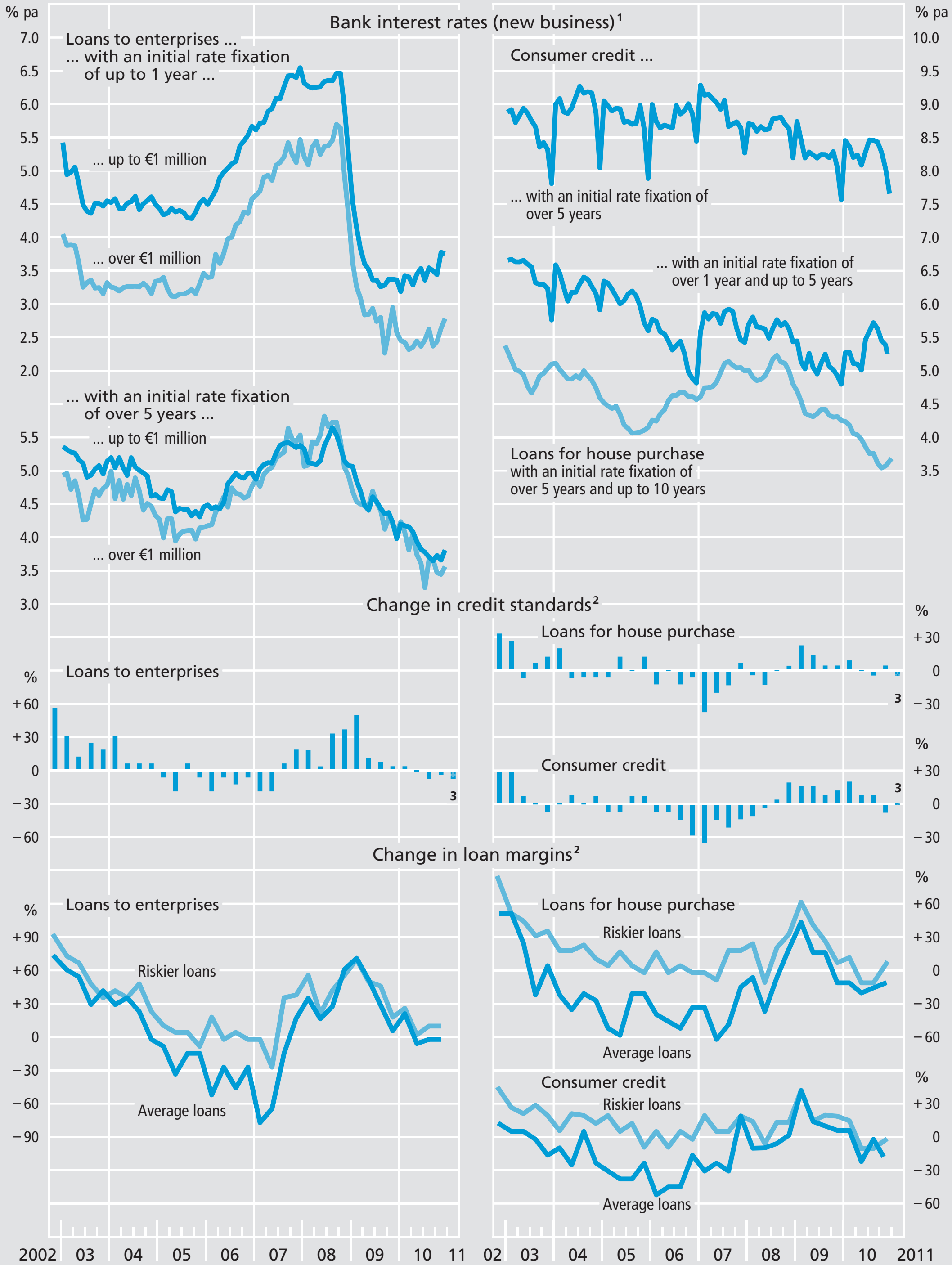
Lending volumes and selected explanatory factors, net percentages[3]



1 See the detailed report: Deutsche Bundesbank, Fourth special survey on German banks' lending to domestic enterprises, http://www.bundesbank.de/volkswirtschaft/vo_veroeffentlichungen.en.php. — 2 See Basel Committee on Banking Supervision, Bank for International Settlements, Basel Committee on Banking Supervision, Basel III: A global regulatory framework for more resilient banks and banking systems, http://www.bis.org/publ/bcbs189.htm. — 3 Difference between the sum of the percentages for "will increase considerably/will contribute considerably to an increase in the tier 1 capital ratio" and "will increase somewhat/will contribute somewhat to an increase in the tier 1 capital ratio" and the sum of the percentages for "will decrease somewhat/will contribute somewhat to a decrease in the tier 1 capital ratio" and "will decrease considerably/will contribute considerably to a decrease in the tier 1 capital ratio" (as a percentage of the given answers). — 4 Includes total regulatory capital.

Deutsche Bundesbank

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 2011 Q1.

Deutsche Bundesbank

Uneven developments in the euro area

ther adjustments in credit standards in the corporate business in the euro area as a whole, whereas retail customers faced tighter credit standards again. The margin policy was similar in both reference areas: the margins for higher-risk loans were increased, in some cases noticeably, as in Germany, whereas they remained virtually unchanged for the average borrower. Net demand rose noticeably in the euro area as a whole but still less than in Germany.

German banks' access to money market somewhat improved

The survey round for the fourth quarter of 2010 again contained *ad hoc* questions on the impact of the financial crisis on wholesale funding, capital costs and the willingness of the participating banks to lend. They indicated that access to wholesale funding had not changed, and only conditions for accessing the money market had improved on the quarter. At the same time, over one-third of the German bank managers surveyed said capital costs were higher in the wake of the financial crisis, while one-quarter of them spoke of some impact on their willingness to lend. The European survey participants said they had difficulties in bond market financing and once again said their capital position had constrained lending more than did German institutions.

Bank lending rates increase slightly in final quarter

In the final quarter of 2010, German bank lending rates developed unevenly but did rise slightly overall. Rates for long-term loans for house purchase increased to 3.8%. Rates for long-term, small-scale loans to non-financial corporations grew at a similar pace, whereas large-scale loans with long rate fixation cheapened somewhat to 3.6%. Conditions for short-term enterprise loans also edged upwards and stood at 3.8% and 2.8% respectively at the end of the year, depending on the size of the loan.