Monetary policy and banking business

Monetary policy and money market developments

ECB Governing Council leaves policy rates unchanged

Based on its economic and monetary analysis, the ECB Governing Council decided to keep key interest rates unchanged in the reporting period. The main refinancing rate thus remains at 0%, while the marginal lending rate stands at 0.25% and the deposit facility rate at -0.40%. The Governing Council continues to expect the key interest rates to remain at their present levels for an extended period of time, and well past the horizon of its net asset purchases. Furthermore, as agreed in October 2017, the Governing Council confirmed that purchases under the expanded asset purchase programme (APP) will be made at the reduced monthly pace of €30 billion net until the end of September 2018, or beyond, if necessary, and in any case until the Governing Council sees a sustained adjustment in the path of inflation consistent with its inflation aim. Redemption amounts will be reinvested alongside the net purchases. The Eurosystem will reinvest the principal payments from maturing securities for an extended period of time after ending net asset purchases, and in any case for as long as necessary.

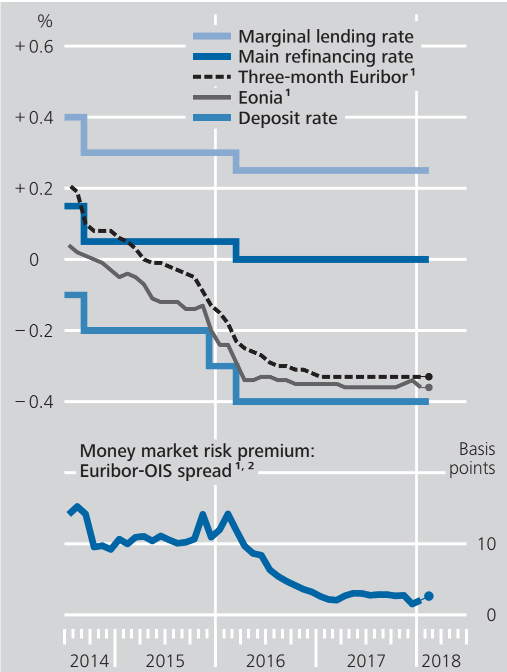
Pace of economic expansion higher than expected

In the view of the Governing Council, information which became available in the reporting period confirmed that the economy was expanding at a robust pace that had increased more strongly in the second half of 2017 than expected. The strong cyclical momentum, the ongoing reduction of economic slack and increasing capacity utilisation further strengthened the Governing Council's confidence that inflation will converge towards its inflation aim of below, but close to, 2%. However, domestic price pressures remain subdued and the Governing Council has not yet identified any convincing signs of a permanent, self-sustaining upward trend. Overall, the Governing Council therefore concluded that a high degree of monetary policy accommodation remains necessary to ensure a sustained return of inflation rates towards a level of below, but close to, 2%.

Purchase volumes still in line with announced target

On 9 February 2018, the Eurosystem held assets in the amount of €1,919.1 billion under the public sector purchase programme (PSPP). The average residual maturity of the PSPP portfolio fell yet again slightly to 7.7 years from previously 7.9 years. The outstanding amounts acquired to date under the third covered bond purchase programme (CBPP3) and the asset-backed securities purchase programme (ABSPP) came to €246.1 billion and €25.3 billion respectively. As for the corporate sector purchase programme (CSPP), asset purchases totalled €139.1 billion by 9 February.

Money market interest rates in the euro area



Sources: ECB and Bloomberg. **1** Monthly averages. **2** Three-month Euribor less three-month Eonia swap rate. • Average 1 to 14 February 2018.

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Money market management and liquidity needs

The two reserve maintenance periods between 1 November 2017 and 30 January 2018 saw another overall increase in euro area liquidity needs stemming from autonomous factors (see the table below). They averaged €1,197.6 billion in the December 2017-January 2018 reserve period, which was €87.6 billion more than the average for the September-October 2017 reserve period, ie the last one prior to the period under review. At the end of 2017, the sum of the autonomous factors reached a new all-time high of €1,268.7 billion. A crucial factor behind the higher liquidity needs was the aggregate decline in net foreign assets and other factors, which are considered together because of liquidity-neutral valuation effects. Combined, they fell by €102.4 billion. This very considerable decrease was attributable, in particular, to non-euro area residents' higher deposits with the Eurosystem. One reason for this could be the fact that, towards the close of the year, investing funds in the market was difficult or was possible only under unattractive conditions. This category of deposits was also up at the end of 2016, albeit to a lesser degree. Furthermore, the seasonal increase in banknotes in circulation during the observation period, to the tune of €15.4 billion net, contributed to higher liquidity needs. The previous year's two corresponding reserve maintenance periods saw the volume of banknotes in circulation rise by an average of €24.4 billion. By contrast, the decline in government deposits with the Eurosystem provided more liquidity. Compared with the average for the September-October 2017 reserve period, these decreased by €30.2 billion to €188.1 billion in the December 2017-January 2018 period. The minimum reserve requirement rose across the two reserve maintenance periods by a total of €1.5 billion, thus additionally increasing the calculated liquidity needs.

The total outstanding tender volume fell slightly in the period under review. In the

Factors determining banks' liquidity*

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

Item	2017/2018 1 November to 19 December	2017/2018 20 December to 30 January
I Provision (+) or absorption (–) of central bank balances due to changes in autonomous factors		
1 Banknotes in circulation (increase: –)	– 3.8	– 11.6
2 Government deposits with the Eurosystem (increase: –)	+ 29.8	+ 0.4
3 Net foreign assets[1]	– 0.5	+ 1.2
4 Other factors[1]	– 23.7	– 79.4
Total	+ 1.8	– 89.4
II Monetary policy operations of the Eurosystem		
1 Open market operations		
(a) Main refinancing operations	– 3.7	– 0.1
(b) Longer-term refinancing operations	– 1.6	– 3.1
(c) Other operations	+ 94.3	+ 64.7
2 Standing facilities		
(a) Marginal lending facility	+ 0.0	+ 0.0
(b) Deposit facility (increase: –)	– 34.4	– 6.7
Total	+ 54.6	+ 54.8
III Change in credit institutions' current accounts (I + II)	+ 56.4	– 34.5
IV Change in the minimum reserve requirement (increase: –)	– 0.6	– 0.9

* For longer-term trends and the Bundesbank's contribution, see pp 14• and 15• of the Statistical Section of this Monthly Report. 1 Including end-of-quarter liquidity-neutral valuation adjustments.
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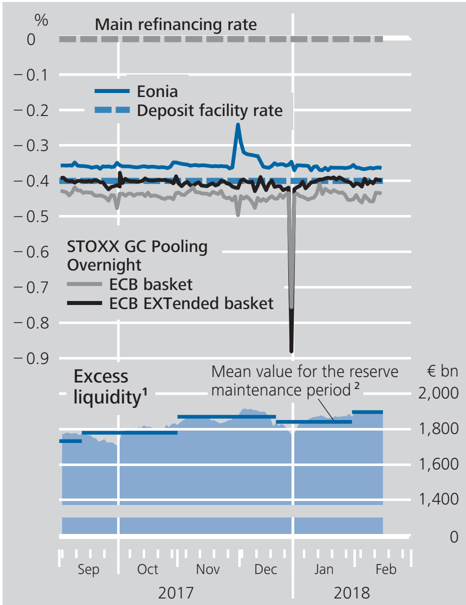
December 2017-January 2018 reserve period, it averaged €764 billion, which was just over €8 billion less than in the September-October 2017 reserve period (see the chart on page 25). Both the main refinancing operations and the longer-term refinancing operations contributed to the slight drop. The volume of main refinancing operations fell by €3.8 billion in the same period, to an average of just €2.9 billion. The increase in demand seen in the final main refinancing operation of 2017 – which, by way of exception, lasted two weeks and thus coincided with both the Christmas public holidays and the end of the year – was relatively modest at €1.5 billion. Demand rose to €3.4 billion. The decline in the volume of longer-term refinancing operations resulted primarily from early voluntary repayments of funds borrowed under the first series of targeted longer-term refinancing operations (TLTRO I), with a total of €2.7 billion being repaid in December 2017 for the second, fourth and sixth TLTRO I operations. This brought the TLTRO I volume down to just over €13 billion, placing it still further behind the TLTRO II in terms of magnitude, with the latter's outstanding volume still standing at around €740 billion (see the chart on page 24). In the December 2017-January 2018 reserve period, the already low volume of the three-month tenders fell slightly against the average for the September-October 2017 reserve period, dropping by €0.5 billion to €7.8 billion.

The Eurosystem continued to provide the bulk of central bank liquidity through the monetary policy asset purchase programmes (see the adjacent table). At an average of €2,398 billion in the December 2017-January 2018 reserve period, the APP balance sheet holdings were up on the average for the September-October 2017 reserve period by approximately €159 billion. Pursuant to the decision taken by the ECB Governing Council in October 2017, January 2018 saw the pace of net asset purchases under the APP scaled back from €60 billion to €30 billion per month.

Against the backdrop of asset purchases for monetary policy purposes, excess liquidity continued to climb in the period under review overall, averaging €1,841 billion in the December 2017-January 2018 reserve period. However, comparing each reserve period average with its respective previous period reveals that excess liquidity increased only in the November-December 2017 reserve period (up €90 billion), while the December 2017-January 2018 reserve period saw a decrease of €29 billion. This decline was caused by the signifi-

Central bank interest rates, money market rates and excess liquidity

Daily data



Sources: ECB, Eurex Repo and Bundesbank calculations. **1** Current account holdings minus the minimum reserve requirement plus the deposit facility. **2** The last period displayed is still ongoing.
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Eurosystem purchase programmes

€ billion

Programme	Change across the two reserve periods	Balance sheet holdings as at 9 February 2018
Active programmes		
PSPP	+ 111.6	1,919.1
CBPP3	+ 8.1	246.1
CSPP	+ 15.4	139.1
ABSPP	+ 0.7	25.3
Completed programmes		
SMP	1 + 0.2	85.0
CBPP1	− 0.1	6.0
CBPP2	− 0.0	4.6

1 Increase due to use of amortised cost accounting at end of quarter.
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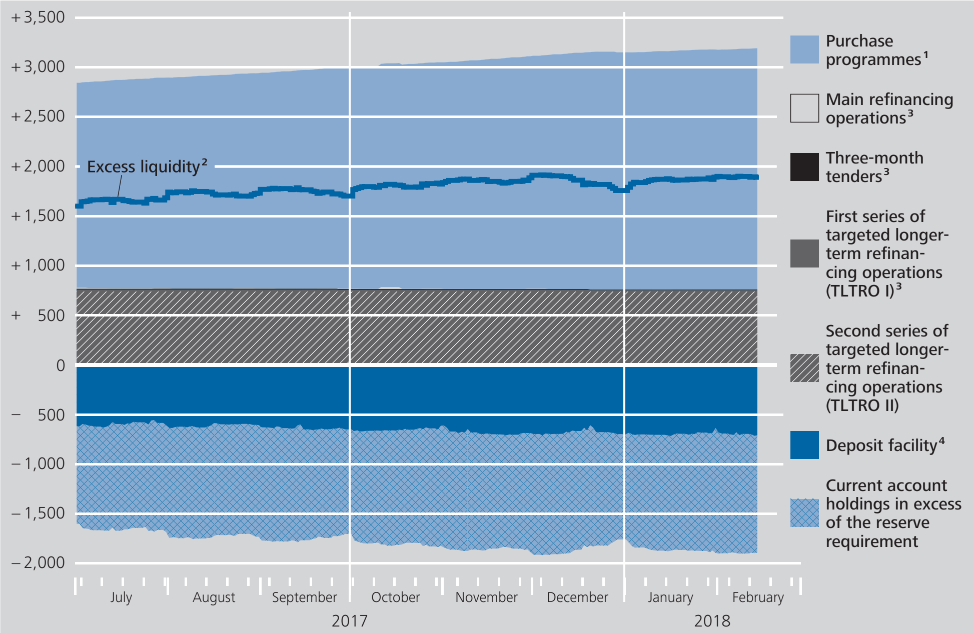
Liquidity provision and use

€ billion, daily data



Sources: ECB and Bundesbank calculations. **1** Securities markets programme (SMP), covered bond purchase programmes (CBPP1, CBPP2 and CBPP3), asset-backed securities purchase programme (ABSPP), public sector purchase programme (PSPP) and corporate sector purchase programme (CSPP). **2** Current account holdings minus the minimum reserve requirement plus the deposit facility. **3** Volume so small it is hardly visible. **4** The marginal lending facility is not shown in this chart owing to its very low volume.

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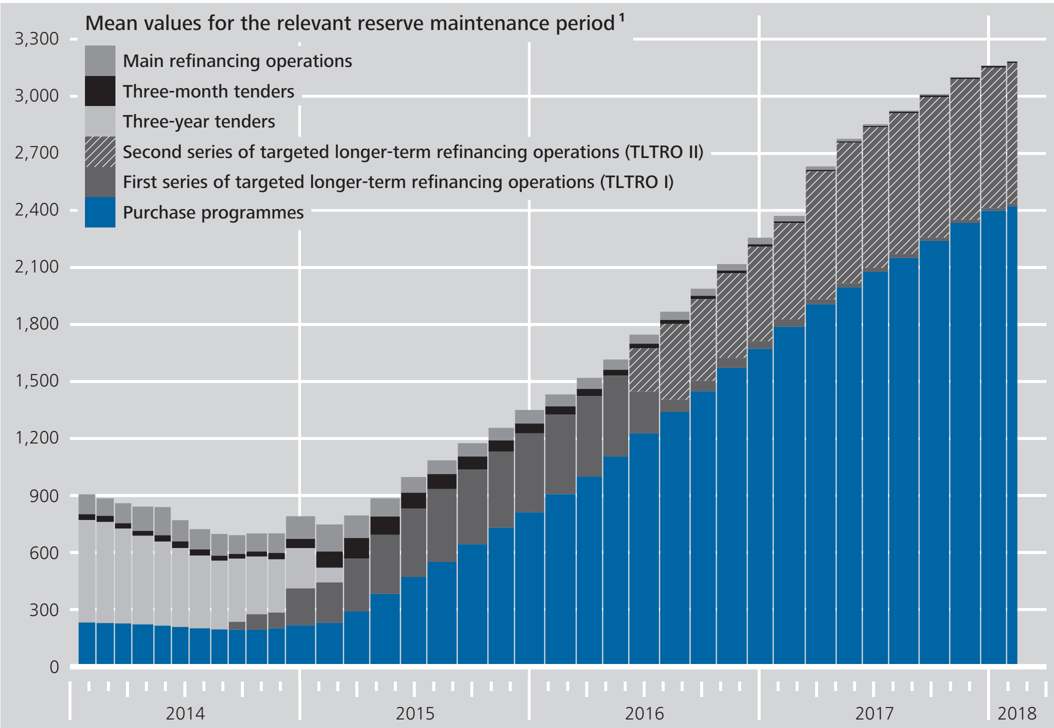
cantly higher liquidity needs stemming from autonomous factors, which exceeded the injection of liquidity from the purchases under the APP.

With the exception of the year-end figure and against the backdrop of high excess liquidity, overnight rates in the period under review continued to move in line with the deposit facility rate (see the chart on page 23). Notwithstanding a temporary rise, the unsecured overnight rate in the money market (Eonia) averaged -0.35% in the November-December 2017 reserve period, ie 1 basis point higher than in the subsequent December 2017-January 2018 reserve period, when it averaged -0.36%. At the end of November, Eonia was significantly higher at -0.24% and remained at elevated levels over the following days, too. In the absence of a general increase in overnight rates, for instance in the secured market, the increase in Eonia should be considered in the light of the limited number of panel banks and the low turnovers reported. With an average daily turnover of €5.3 billion in the period under review, the reported volumes of unsecured overnight money continued on a downward trend. On the GC Pooling platform, secured overnight money traded in the ECB basket at an average of -0.45% in the December 2017-January 2018 reserve period, ie 1 basis point lower than in the previous period. Overnight money in the ECB EXTended basket (which contains a larger set of eligible securities) traded at an average of -0.42%, which was 2 basis points lower than the deposit facility rate. Totalling €5.2 billion and €5.8 billion respectively, the associated overnight turnovers in the ECB and ECB EXTended baskets in both reserve maintenance periods under review had again risen compared with the previous observation period, despite low turnovers at year-end. As in previous years, the end of the year saw a fall in Eonia turnovers, although this time the reference rate hardly changed. Also with low turnovers, the turn of the year saw considerable declines in the case of secured overnight money, to -0.76% in the ECB basket and -0.88% in the ECB EXTended basket.

Outstanding liquidity broken down by open market operations in the euro area

€ billion



Sources: ECB and Bundesbank calculations. **1** The bar width corresponds to the length of the reserve maintenance period. The last period displayed is still ongoing.
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Upward trend in excess liquidity slows down

The upward trend in excess liquidity flattened slightly in the period under review as a result of the lower purchase volumes under the APP since January 2018. Overall, excess liquidity grew by €40 billion to €1,890 billion. This increase continued to be propelled mainly by the continued asset purchases, while volumes in the standard tender operations deflated again slightly. Bearing in mind the planned purchases under the APP up until September 2018, a further rise in the level of excess liquidity can be expected.

Money market rates largely unchanged on the whole

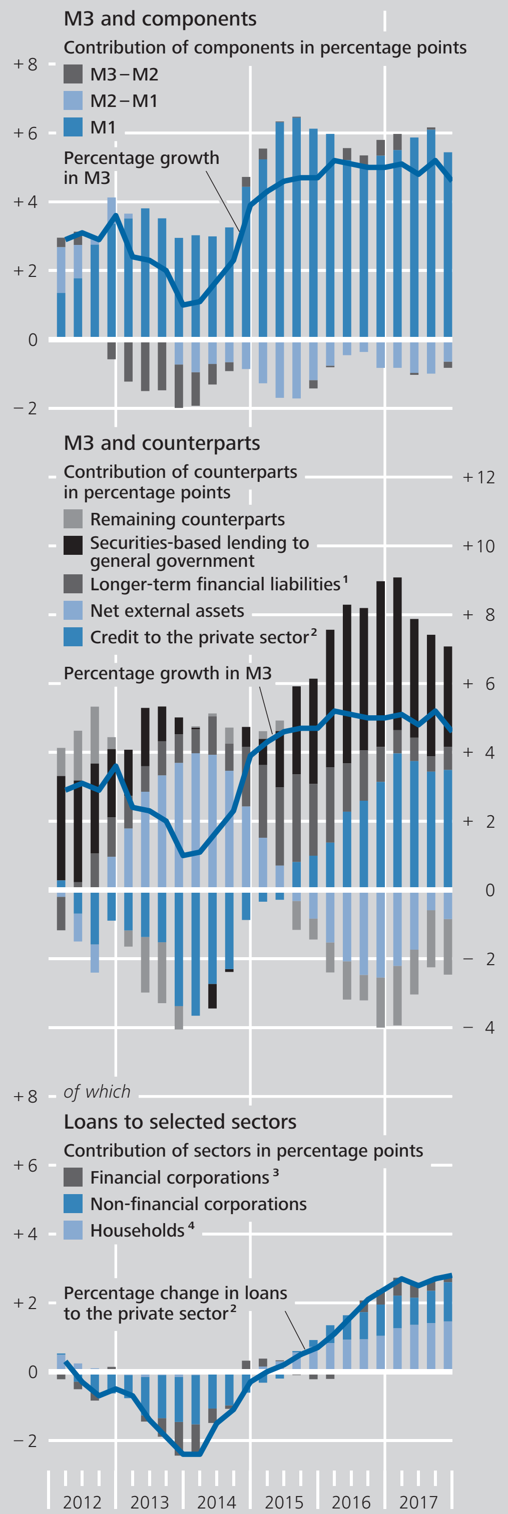
The unsecured overnight rate in the money market (Eonia) moved within a range of between -0.24% and -0.37% in the reporting period, ie above the deposit facility rate of -0.40%. At the end of November, Eonia increased perceptibly for a number of days. Given that total turnover was very low, this increase was probably caused by individual transactions reported in the Eonia panel. As a consequence, Eonia a few days later returned to a lower level of between -0.35% and -0.37%. The secured overnight rate (STOXX GC Pooling) remained slightly below the deposit facility rate in the reporting period. Due to end-of-year effects, the secured overnight rate temporarily saw a substantial drop to -0.76%. By contrast, three-month Euribor was largely unchanged throughout the reporting period, standing at -0.33% at last report. Despite the intermediate one-off effects, money market rates on the whole remain at essentially the same level observed for several months now.

Market participants expect first policy rate increases in 2019

Forward rates recorded considerable increases in the reporting period. These were, for the most part, related to the positive economic data which became available in December. To some extent, the summary of the monetary policy meeting of the ECB Governing Council in December, which was published at the beginning of January, contributed to this rise as well. Thus, the markets are currently pricing in an initial interest rate hike in the first quarter of 2019.

Monetary aggregates and counterparts in the euro area

Year-on-year change, end-of-quarter data, seasonally adjusted



Source: ECB. **1** Denoted with a negative sign because, per se, an increase curbs M3 growth. **2** Adjusted for loan sales and securitisation as well as for positions arising from notional cash pooling services provided by MFIs. **3** Non-monetary financial corporations. **4** Including non-profit institutions serving households.

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Monetary developments in the euro area

Credit growth reflected in monetary dynamics

In the fourth quarter of 2017, the perceptible expansion in the broad monetary aggregate M3 continued on balance, with a 4.6% annual growth rate at the end of the quarter, ie only slightly below the level observed since April 2015. The sustained expansion of the money stock continued to be shaped by the money-holding sector's strong preference for overnight deposits against the backdrop of low opportunity costs. Of the counterparts, MFI lending to non-banks in the euro area – including by the Eurosystem – was once again the main driver of monetary growth. On the one hand, monetary growth was supported by the Eurosystem's continued purchases of bonds issued by general government and private non-banks. On the other hand, in the context of the still very low interest rate setting and the economy's broad-based growth path, bank loans to private non-banks, in particular, continued their upward trajectory; the picture for the year shows that their contribution to the M3 growth rate in the reporting quarter exceeded that of loans to general government for the first time since 2011. The positive development in lending is also reflected in the assessments of the banks surveyed as part of the Bank Lending Survey (BLS). Thus, against the backdrop of virtually unchanged or only slightly changed credit standards, the growth of loans to enterprises and households was primarily fuelled by a lively demand for credit.

Overnight deposits still dominant force behind M3 growth

Given the persistently low yield spread between long-term government bonds and monetary components, money holdings remained attractive in the period under review, especially for risk-averse investors. In this setting, monetary growth in the reporting quarter was again characterised by strong inflows in overnight deposits, received, in particular, from households but also from financial and non-financial corporations. The shifts within the monetary aggregate M3 from short-term time deposits to short-term savings and, in particular, to over-

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

Quarter-on-quarter change in € billion, seasonally adjusted

Assets	2017 Q4	2017 Q3	Liabilities	2017 Q4	2017 Q3
Credit to private non-MFIs in the euro area	82.5	77.3	Holdings against central government[2]	– 9.5	64.9
Loans	64.6	78.9	Monetary aggregate M3	91.5	163.9
Loans, adjusted[1]	81.6	86.7	*of which* Components		
Securities	17.9	– 1.7	Currency in circulation and overnight deposits (M1)	114.4	166.9
Credit to general government in the euro area	88.9	88.7	Other short-term deposits (M2-M1)	– 11.2	– 21.7
Loans	– 16.3	– 10.8	Marketable instruments (M3-M2)	– 11.8	18.6
Securities	105.1	99.6	Longer-term financial liabilities	– 32.9	– 20.0
Net external assets	– 73.1	24.1	*of which* Capital and reserves	0.2	34.7
Other counterparts of M3	– 49.1	18.7	Other longer-term financial liabilities	– 33.1	– 54.8

* Adjusted for statistical changes and revaluations. **1** Adjusted for loan sales and securitisation as well as for positions arising from notional cash pooling services provided by MFIs. **2** Including central government deposits with the MFI sector and securities issued by the MFI sector held by central governments.
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night deposits continued. Given the low level of interest rate spreads between these types of deposit, the incentives for building up time deposits are currently low.

Lending to private non-banks again key driver of monetary growth

Monetary growth in the fourth quarter was again mainly supported by MFI lending to non-banks in the euro area. A key driver of this development were once again the loans to private non-banks adjusted for securitisation and other one-off effects; in the reporting quarter, the annual growth rate of these loans recorded a further slight increase to 2.8%. Consequently, the gap narrowed further between monetary growth and loan growth in the euro area, having widened in 2011 and 2012 as a result of weak loan dynamics in parts of the currency union.

Significant rise in lending to non-financial corporations

The largest contribution to loan growth came from lending to non-financial corporations in the euro area regaining momentum in the fourth quarter. Medium and long-term loans again recorded the most significant gains. Adjusted for securitisation and other one-off effects, the annual growth rate of loans to non-financial corporations climbed from 2.4% at the end of September to 2.9% at the end of December. The ongoing expansion in loans to enterprises reflects the continued favourable underlying conditions in the euro area; the solid economic growth is broad-based across member states and sectors, lending rates in the euro area as a whole remain close to historical lows and the business of lending to corporate customers is highly competitive.

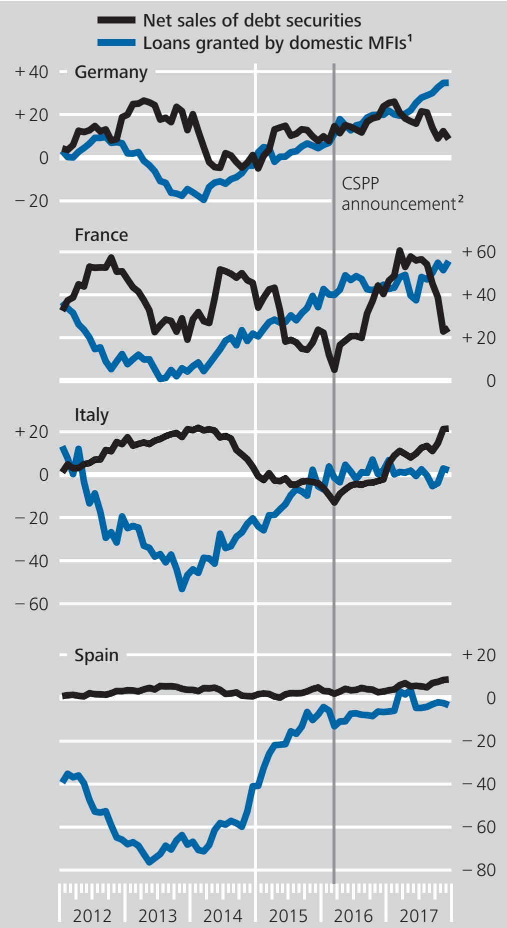
According to BLS, demand for credit increasingly fuelled by funding needs for fixed investment

This is consistent with the fact that the banks surveyed in the BLS perceived a considerable rise in the demand for credit by non-financial corporations in the fourth quarter of 2017, which meant that credit demand was even somewhat more dynamic than in the preceding quarters. The credit institutions attributed these gains, above all, to greater funding needs for fixed investment. However, demand-boosting impulses also stemmed from the low general interest rate level and the financing needs for inventories and working capital as well as for mergers, acquisitions and corporate restructuring. By contrast, enterprises' scope for internal financing, *per se,* had a stifling effect on demand. No headwinds were caused by lending policies in the reporting quarter. The surveyed institutions left their credit standards for lending to enterprises unchanged on balance and continued to ease their credit terms and conditions, as previously reported in the preceding months.

More so than in the preceding quarters, the growth of loans to non-financial corporations

Selected components of the external financing of non-financial corporations in the four large euro area countries

€ billion, 12-month accumulated flows



Sources: ECB and Bundesbank calculations. **1** Adjusted for loan sales and securitisation. **2** The vertical line depicts the ECB Governing Council's announcement of the corporate sector purchase programme (CSPP) on 10 March 2016.
Deutsche Bundesbank

Internal financing particularly relevant in Spain and Germany

in the euro area in the reporting quarter was driven by positive impetus not only from France and Germany, but also from Italy and a number of smaller core euro area countries; muted positive contributions emanated from Spain. Country-specific differences in the demand for loans to enterprises can, in part, be explained by the varying degrees of relevance of alternative sources of funding.[1] In Germany and Spain, for instance, internal financing of non-financial enterprises has risen considerably as a result of the favourable development in gross value added since the financial and economic crisis; but whereas internal financing declined in Germany of late, it remained at a high level in Spain. The slower pace of internal financing could explain why the growth of loans to non-financial corporations in Germany recently rebounded.

Higher net sales of debt securities of late, especially in Italy and Spain

In addition, since the announcement of the CSPP in March 2016, net issuance of debt securities by non-financial corporations has picked up in the euro area as a whole. This is especially true of France, the Netherlands and, to a lesser extent, of Italy and Spain (see the adjacent chart). In France, however, net issuance by enterprises which were previously highly active in the capital market weakened noticeably at the end of the reporting period. By contrast, net issuance of debt securities by non-financial corporations in Italy and Spain accelerated in recent quarters, which meant that their volumes even exceeded net inflows in corresponding loans. Conversely, growth in net issuance in Germany was perceptibly lower than the net increase in loans to enterprises. Projections drawn up *ex post* regarding the CSPP period provide no indication of any markedly dampening effects on German loan growth stemming from the purchase programme.

Loans to households – especially for house purchase – providing further support to lending growth

Loans to households continued on their steady growth path and were thus the second major mainstay of credit to the euro area private sector in the fourth quarter. The largest contributions came from banks in Germany and France, followed by Italy. Drivers of growth in the euro area as a whole were once again loans for house purchase, the annual growth rate of which stood at 3.3% at the end of the year; this was roughly the same level as in the two preceding quarters. According to the banks surveyed in the BLS, household demand for loans for house purchase rose again in the fourth quarter. At the same time, the pace of growth continued to slow compared with the previous quarters. Viewed in isolation, the posi-

1 See also Deutsche Bundesbank, Developments in corporate financing in the euro area since the financial and economic crisis, Monthly Report, January 2018, pp 53-71.

tive outlook on the housing market and anticipated price changes supported demand just as much as robust consumer confidence and the low general interest rate level. Demand-curbing effects mainly resulted from households' use of their own savings to help fund house purchases. On balance, credit standards in this segment were eased slightly.

Continued steep growth in consumer credit

Consumer credit showed further substantial growth in the reporting period, probably reflecting the ongoing expansionary underlying trend in private consumption. This is consistent with the fact that households' need for consumer credit recorded another marked increase in the fourth quarter of 2017, according to the results of the BLS. Respondents put the higher demand down to stable consumer confidence, the low general level of interest rates and the high propensity to purchase. On balance, credit standards in this segment remained virtually unchanged.

Securities-based lending to private sector records net inflows

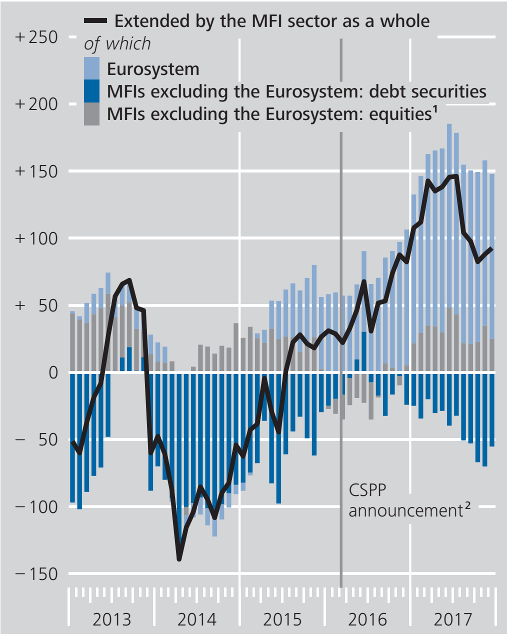
MFIs noticeably expanded their securities-based lending to the private sector from October to December, thus also making a positive contribution to monetary growth. This expansion was supported, in particular, by the ongoing Eurosystem purchases of debt securities issued by private non-banks under the APP. In net terms, other MFIs continued to buy shares issued by private enterprises in the reporting quarter while at the same time reducing their net holdings of debt securities issued by the private sector (see the adjacent chart). Securities-based lending to general government was also strongly influenced in the last quarter of 2017 by the Eurosystem purchases under the APP and contributed significantly to monetary growth. Other MFIs, by contrast, further reduced their holdings on balance.

Further net outflows from longer-term financial liabilities due to interest rate levels

The supportive impact of longer-term financial liabilities vis-à-vis other euro area residents on the money supply, which has been observed since the end of 2011, also continued in the quarter under review. The money-holding sector again significantly reduced its stock of longer-term time deposits and savings deposits as well as longer-term bank debt securities. It is likely that this was largely encouraged by the interest rate levels and the persistently high inflows of funds to short-term deposits.

Securities-based lending* to private non-banks in the euro area

€ billion, 12-month accumulated flows



Sources: ECB and Bundesbank calculations. * Eurosystem: debt securities only; other MFIs: debt securities and equities. **1** Shares and other equities. **2** The vertical line depicts the ECB Governing Council's announcement of the corporate sector purchase programme (CSPP) on 10 March 2016.
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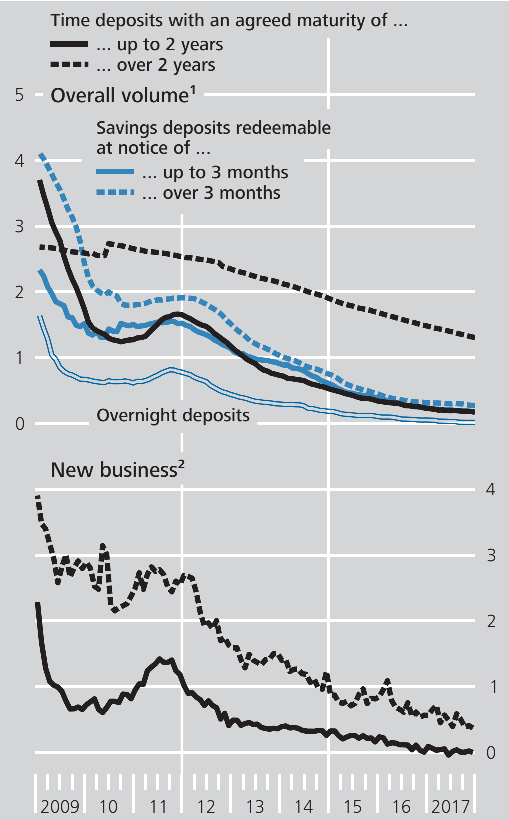
Net external asset position dampening M3 growth

The previously observed upward trend in the net external asset position of the MFI sector did not continue in the reporting period. Instead, the fourth quarter saw further substantial outflows of funds to non-euro area countries, which curbed monetary growth *per se*. The balance of payments data available so far for October and November 2017 suggest that this can be attributed to euro area investors' extensive net purchases of foreign securities, especially longer-term bonds issued by the non-MFI private sector. This development was aided by the persistently negative yield spread for the euro area relative to most other economic areas. On balance, the resulting outflows from portfolio transactions outweighed the continued marked interest of non-resident invest-

Interest rates on bank deposits in Germany*

% pa, monthly data



* Deposits of households and non-financial corporations. **1** According to the harmonised MFI interest rate statistics. Volume-weighted interest rates across sectors. Interest rate levels for overnight and savings deposits may also be interpreted as new business due to potential daily changes in interest rates. **2** According to the harmonised MFI interest rate statistics. Volume-weighted interest rates across sectors and maturities. Unlike the overall volume of contracts (ie deposit contracts on the balance sheet at the end of the month), the volume of new business (ie all contracts concluded in the course of a month) is explicitly recorded for time deposits only.

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ors in euro area equities and investment fund shares and the high current account surpluses.

German banks' deposit and lending business with domestic customers

Build-up of households' overnight deposits still dominating deposit growth

German banks' deposit business with domestic customers recorded another distinct increase in the final quarter of 2017. Given the low interest rates and the flat yield curve (see the chart above), the ongoing build-up of overnight deposits, which began in autumn 2008, continued whilst all other deposit types recorded net outflows. From a sectoral perspective, households once again made the greatest contribution to the sustained build-up of overnight deposits, although this growth again slowed slightly on the quarter. Overall, the investment behaviour of households – despite signs of a small increase in yield awareness – was still characterised by a preference for highly liquid and less risky investment forms, however.

Further build-up of non-financial corporations' bank deposits

At the same time, non-financial corporations markedly stocked up their holdings of overnight deposits, despite the fact that interest rates had fallen further. In addition, the enterprises included in this sector showed greater interest in long-term time deposits in the reporting quarter, as they had also done in the preceding months. This development is likely to be attributable to the now negative average interest rates on short-term bank deposits and other safe forms of investment, amongst other things. The sustained increase in this sector's bank deposits was also assisted by the fact that non-financial corporations in Germany were still generating high surpluses.

Investment behaviour within the financial corporate sector remains very heterogeneous

Furthermore, for the first time in around four years, a positive contribution from financial corporations characterised domestic banks' deposit business in the reporting quarter. However, the investment behaviour of the individual financial market players remained heterogeneous in the fourth quarter: whilst insurers and pension funds continued to reduce both their long-term and – to a lesser extent – their short-term deposits, other financial corporations built up their bank deposits further.

Further expansion in lending to domestic non-banks

German banks' lending to the domestic non-bank sector rose markedly again in the fourth quarter of 2017. As in the preceding eight quarters, loans to general government were the sole exception here. In view of the very favourable budgetary situation overall, this is likely to reflect, not least, the public sector's low financing needs. By contrast, loans to the domestic private sector saw distinct growth again. In addition, banks in Germany markedly increased their holdings of securities issued by the private sector once more, acquiring mainly shares and other variable-yield securities.

Loans to households still driven by housing loans, …

Loans to households again recorded the largest net inflows in loans to the private sector, closely followed by non-financial corporations. Once more, loans for house purchase were a decisive driver of households' ongoing brisk demand for bank loans, growing at a similarly strong rate in the reporting quarter as in the preceding quarters. On balance, the year-on-year growth rate of this credit segment remained unchanged again at 3.9%. It was thus the fourth consecutive quarter that this rate moved sideways.

… aided by low borrowing costs and by favourable income and asset situation

In addition to the extremely favourable income and asset situation of households in Germany, the continued high demand for housing loans in the quarter under review was also spurred on by the still exceptionally supportive financing conditions. According to the MFI interest rate statistics, the interest rate on long-term loans for house purchase was 1.9% at the end of the fourth quarter, thus remaining close to the trough it reached in September 2016.

The results of the latest BLS provide evidence of further factors influencing these developments. For instance, in addition to the low general level of interest rates, the respondent banks indicated that good prospects for the housing market and robust consumer confidence *per se* were also having an expansionary effect on demand. This impact was neutralised on balance, however, by influences stifling demand, such as households' increased use of their own savings, banks having lost market share to competitors, lower funding needs for refinancing, restructuring and renegotiation purposes, and more restrictive legal and tax conditions in the housing market.

No restrictive stimulus from lending policies

According to the BLS, banks' lending policies provided no restrictive stimulus during the reporting period. In fact, credit standards for loans to households for house purchase eased slightly in net terms. After the expansionary adjustments to the standards in the first and third quarters, this was the third time credit standards were loosened in the past year. However, neither the scale of these adjustments nor the proportion of banks in the sample easing their standards suggests that the standards were reduced across the board. For the first quarter of 2018, the surveyed banks do not expect any further changes to credit standards.

Fresh inflows for consumer credit

Unlike for housing loans, growth in consumer credit accelerated markedly over the course of 2017, although the banks surveyed in the BLS reported more subdued loan demand growth

Lending and deposits of monetary financial institutions in Germany*

€ billion, 3-month accumulated flows, end-of-quarter data, seasonally adjusted

Item	2017 Q3	2017 Q4
Deposits of domestic non-MFIs1		
Overnight	23.2	30.7
With an agreed maturity of		
up to 2 years	− 5.0	− 7.8
over 2 years	− 2.2	− 1.7
Redeemable at notice of		
up to 3 months	0.4	− 0.1
over 3 months	− 2.1	− 2.5
Lending		
to domestic general government		
Loans	− 7.5	− 1.4
Securities	− 5.1	− 6.9
to domestic enterprises and households		
Loans2	26.1	22.6
of which to households3	12.3	12.6
to non-financial corporations4	11.0	9.6
Securities	2.1	5.4

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

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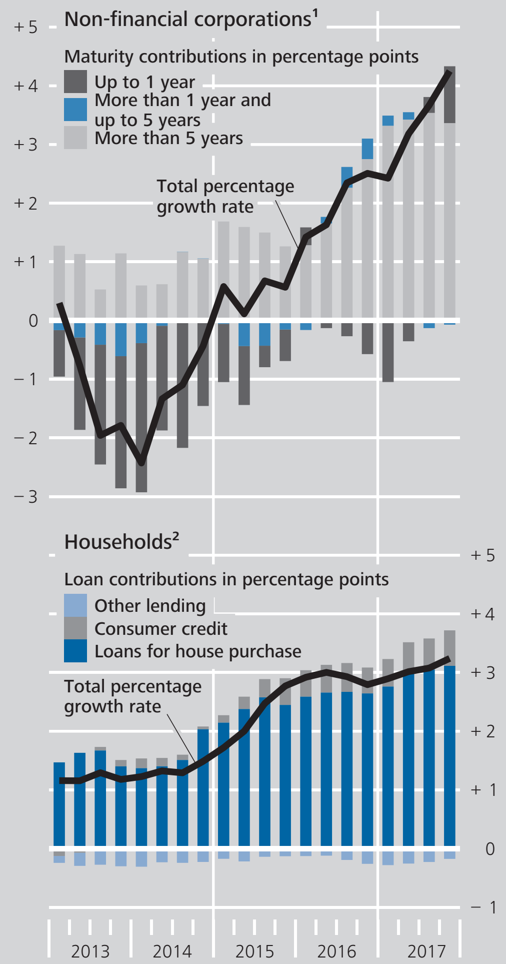
Loans* by German banks to the domestic private non-financial sector

Year-on-year changes, end-of-quarter data, seasonally adjusted



* Adjusted for loan sales and securitisation. **1** Non-financial corporations and quasi-corporations. **2** Including non-profit institutions serving households.
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in this segment. Compared with the dynamic developments of the three preceding quarters, for example, the respondent banks reported marginal growth in demand for the fourth quarter of 2017. As in the past, the banks mainly attributed the rise in demand to households' stable propensity to purchase, robust consumer confidence and the low general interest rate level. On balance, credit standards in this segment remained unchanged in the reporting quarter.

Growth in German banks' lending business was largely supported by loans to non-financial corporations. In line with the persistently strong upturn in the German economy, domestic enterprises once again showed great interest in bank loans during the quarter under review. With an annual growth rate of 4.3% at the end of the quarter, the growth momentum in this credit segment is now distinctly higher than in the case of loans to households, which grew by 3.2% last year.

Another distinct increase in lending to non-financial corporations with unchanged credit standards …

… and greater preference for longer-term loans

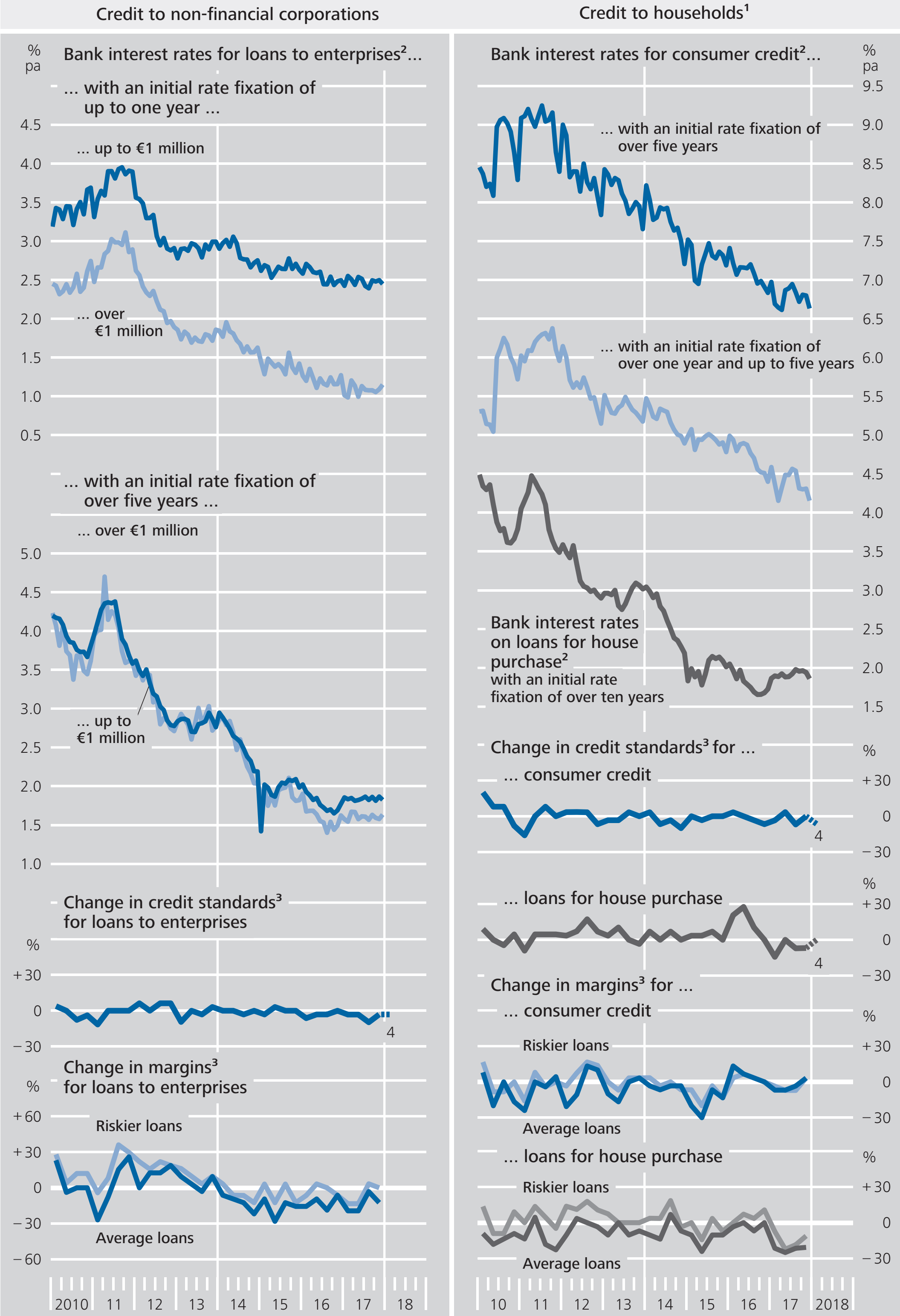
In terms of maturities, non-financial corporations continued to show a preference for long-term loans in the reporting quarter. Besides the exceptionally low interest rates, German enterprises' interest in long-term loan contracts can probably also be explained by the strong sentiment and enterprises' upbeat business expectations. The latest BLS results underpin this assessment: according to the surveyed bank managers, the high level of funds needed for fixed investment was decisive for the increase in demand for bank loans while, when viewed in isolation, enterprises' use of internal financing was the main factor dampening demand.

Banks' lending policies also supported enterprises' demand for bank loans in the reporting quarter. Whereas credit standards remained broadly unchanged, on balance, according to the responses provided by the banks surveyed in the BLS, banks eased the credit terms and conditions agreed in the loan contracts markedly on the whole, although the easing only related to the margins on average-risk loans.

German banks increase risk-weighted assets and strengthen their capital position

The BLS conducted in January contained additional questions on banks' funding conditions and on the impact on banks' lending policies of the new regulatory and supervisory activities relating to requirements for capital adequacy, leverage ceilings, liquidity and loss provisioning. The German banks reported that, given the situation in the financial markets, their funding situation showed little change overall compared with the preceding quarter. With regard to the new regulatory and supervisory activities, the respondents reported – for the first time since the *ad hoc* question was introduced

Banking conditions in Germany



1 Including non-profit institutions serving households. **2** New business. According to the harmonised MFI interest rate statistics. Until May 2010, the aggregate interest rate was calculated as the average rate weighted by the reported volume of new business. As of June 2010, an interest rate weighted by the reported volume of new business is first calculated for each level. The aggregate interest rate is calculated by weighting the interest rates for the levels by the extrapolated volumes. **3** According to the Bank Lending Survey; for credit standards: difference between the number of respondents reporting "tightened considerably" and "tightened somewhat" and the number of respondents reporting "eased somewhat" and "eased considerably" as a percentage of the responses given; for margins: difference between the number of respondents reporting "widened considerably" and "widened somewhat" and the number of respondents reporting "narrowed somewhat" and "narrowed considerably" as a percentage of the responses given. **4** Expectations for 2018 Q1.

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in 2011 – having increased their risk-weighted assets slightly on balance in the wake of the new regulatory and supervisory activities, particularly as a result of the rise in average-risk loans. In addition, credit institutions strengthened their capital position again.