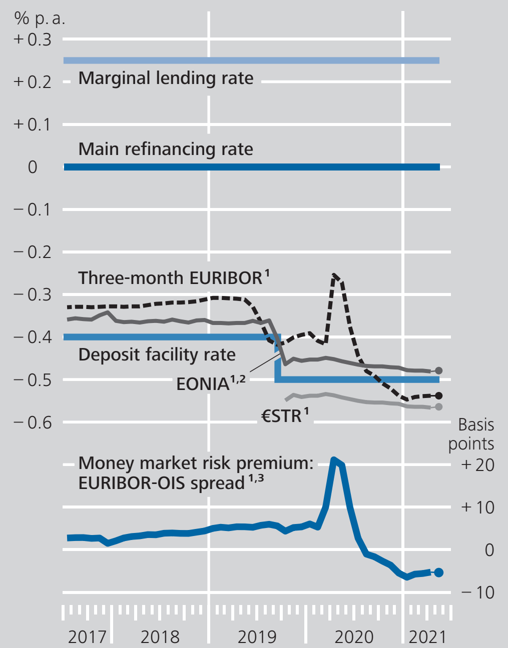
Monetary policy and banking business

Monetary policy and money market developments

ECB Governing Council expects higher monthly PEPP purchases for the second quarter

At its monetary policy meeting in March, the ECB Governing Council reaffirmed its decision taken in December 2020 to continue to conduct net asset purchases under the pandemic emergency purchase programme (PEPP) with a total envelope of €1,850 billion until at least the end of March 2022 and, in any case, until it judges that the coronavirus crisis phase is over. Purchases will continue to be conducted flexibly according to market conditions and with a view to preventing a tightening of financing conditions that is inconsistent with countering the downward impact of the pandemic on the projected path of inflation. If favourable financing conditions can be maintained with lower overall purchase volumes, the envelope of €1,850 billion need not be used in full. Equally, the total envelope can also be increased if necessary. In March, based on a joint assessment of financing conditions and the inflation outlook, the Governing Council expected purchases under the PEPP to be conducted at a significantly higher pace over the next quarter than during the first months of the year. It also confirmed this assessment following its monetary policy meeting in April.

Money market interest rates in the euro area



Sources: ECB and Bloomberg. **1** Monthly averages. **2** From 1 October 2019, EONIA calculated as €STR + 8.5 basis points. **3** Three-month EURIBOR less three-month EONIA swap rate. • Average 1 to 18 May 2021.
Deutsche Bundesbank

Preserving favourable financing conditions essential

While the macroeconomic projections published by the ECB in March envisaged a gradual increase in underlying inflation pressures, they confirmed that the medium-term inflation outlook was broadly unchanged compared with December 2020 and remained below the Eurosystem's inflation aim. In this context, the ECB Governing Council is of the view that preserving favourable financing conditions over the pandemic period remains essential. At the same time, it believes that the rise in market rates observed since the start of the year posed a risk to wider financing conditions.

APP and key interest rates unchanged

The ECB Governing Council left the asset purchase programme (APP) and the key interest rates unchanged. Net purchases under the APP will continue at a pace of €20 billion per month. The main refinancing rate remains at 0%, while the rate on the marginal lending facility stands at 0.25% and the deposit facility rate at -0.5%. The Governing Council reaffirmed its decisions on its other monetary policy measures from December and left them unchanged.

Continued increase in APP and PEPP securities holdings

APP holdings recorded on the balance sheet rose by €59.7 billion during the reporting period. On 14 May 2021, the Eurosystem as a whole held assets totalling €2,999.7 billion as part of the APP (see the box on pp. 27 ff. for a breakdown of the holdings by individual programme). The holdings are furthermore being influenced by the smoothing over time of reinvestments in line with the technical parameters agreed upon in December 2018 and by

Money market management and liquidity needs

In the two reserve maintenance periods under review running from 27 January 2021 to 27 April 2021, liquidity needs stemming from autonomous factors rose in the euro area by a total of €19.4 billion to €1,909 billion (see the table below).[1] This was mainly attributable to the rise in government deposits and growth in banknote demand (see the chart on p. 28). Government deposits totalled €644.5 billion on average for the March-April 2021 period, an increase of €114.2 billion on the average for the December 2020-January 2021 period. The Bundesbank accounted for €187.4 billion of these deposits in the March-April 2021 period. The volume of banknotes in circulation rose in the two reserve maintenance periods under review, climbing during the ongoing pandemic situation by €18.3 billion to an average of €1,447.7 billion in the March-April 2021 period. Net banknote demand at the Bundesbank rose by €10.4 billion, raising cumulative net banknote issuance in Germany to an average of €829.9 billion in the March-April 2021 period. The combined total of net foreign assets and other factors, which are considered together owing to liquidity-neutral valuation effects, saw a significant increase of €113.1 billion and reduced liquidity needs accordingly. The main reason for this development was a considerable decline in liabilities to non-euro area residents denominated in euro. This came about largely due to a reduction in deposits from foreign central banks, which had previously increased sharply up to the end of 2020. The minimum reserve requirement in the March-April 2021 reserve period stood at €147.4 billion, its increase of €2.0 billion adding to the calculated liquidity needs of the banking system in the Eurosystem.

1 Average of the second reserve maintenance period of 2021 (March-April 2021) compared with the average of the eighth reserve maintenance period of 2020 (December 2020-January 2021), which was covered in the February 2021 issue of the Monthly Report.

Factors determining banks' liquidity*

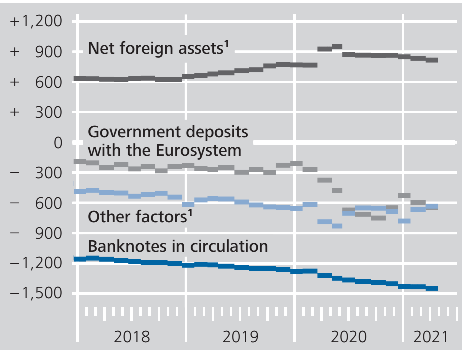
€ billion; changes in the daily averages of the reserve maintenance periods vis-à-vis the previous period

Item	2021: 27 January to 16 March	2021: 17 March to 27 April
I. Provision (+) or absorption (–) of central bank balances due to changes in autonomous factors		
1. Banknotes in circulation (increase: –)	– 4.0	– 14.3
2. Government deposits with the Eurosystem (increase: –)	– 65.5	– 48.7
3. Net foreign assets[1]	– 13.7	– 18.2
4. Other factors[1]	+ 110.5	+ 34.5
Total	+ 27.3	– 46.7
II. Monetary policy operations of the Eurosystem		
1. Open market operations		
a) Main refinancing operations	+ 0.1	– 0.1
b) Longer-term refinancing operations	– 0.2	+ 262.2
c) Other operations	+ 112.2	+ 126.3
2. Standing facilities		
a) Marginal lending facility	+ 0.0	+ 0.0
b) Deposit facility (increase: –)	– 11.1	– 78.4
Total	+ 101.0	+ 310.0
III. Change in credit institutions' current accounts (I. + II.)	+ 128.3	+ 263.4
IV. Change in the minimum reserve requirement (increase: –)	– 1.0	– 1.0

* 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.
Deutsche Bundesbank

Autonomous factors in the Eurosystem*

€ billion, mean values for the relevant reserve maintenance period



Sources: ECB and Bundesbank calculations. * Liquidity-providing (liquidity-absorbing) factors are preceded by a positive (negative) sign. 1 Including end-of-quarter liquidity-neutral valuation adjustments.
Deutsche Bundesbank

Eurosystem purchase programmes

€ billion

Programme	Change across the two reserve periods	Balance sheet holdings as at 14 May 2021
Active programmes[1]		
PSPP	+ 36.8	2,404.3
CBPP3	+ 2.2	291.6
CSPP	+ 15.1	275.0
ABSPP	− 0.2	28.8
PEPP	+ 206.0	1,053.1
Completed programmes		
SMP	− 5.2	17.1
CBPP1	0	0.4
CBPP2	− 0.3	2.4

1 Changes due to net purchases, maturities, reinvestments and amortisation adjustments.
Deutsche Bundesbank

In the period under review, additional central bank liquidity was provided both by purchase programmes, in particular the pandemic emergency purchase programme (PEPP), and by refinancing operations (see the chart on p. 30). Bids in the seventh operation of the third series of targeted longer-term refinancing operations (TLTRO-III) came in at a high €330.5 billion, probably because the TLTRO-III modalities were adjusted in December 2020, which made participation, particularly in the March 2021 operation, attractive for banks. Relative to the other operations still outstanding under the third TLTRO programme, the March operation allows participating banks to benefit longest from the special interest rate conditions of as low as -1.0% (one year and three months). On balance, the seventh TLTRO-III operation and maturities from the final TLTRO-II operation on 24 March 2021 resulted in a net liquidity injection of €314.8 billion. At €0.4 billion in total, there was hardly any demand for the eighth pandemic emergency longer-term refinancing operation (PELTRO). Uptake of the regular main refinancing operations and three-month tenders likewise remained subdued. Total tender volume in the Eurosystem amounted to an average of €2,055 billion in the March-April 2021 period. In Germany, the outstanding volume of longer-term operations – which include TLTROs, PELTROs and three-month tenders – rose by €66 billion to an average of €407.3 billion in the period under review, which represented a share of around 20% of the outstanding volume of long-term tenders in the Eurosystem.

At an average of €3,951 billion, balance sheet holdings of the asset purchase programmes in the March-April 2021 period were around €239 billion above the average for the period under comparison (see the adjacent table).

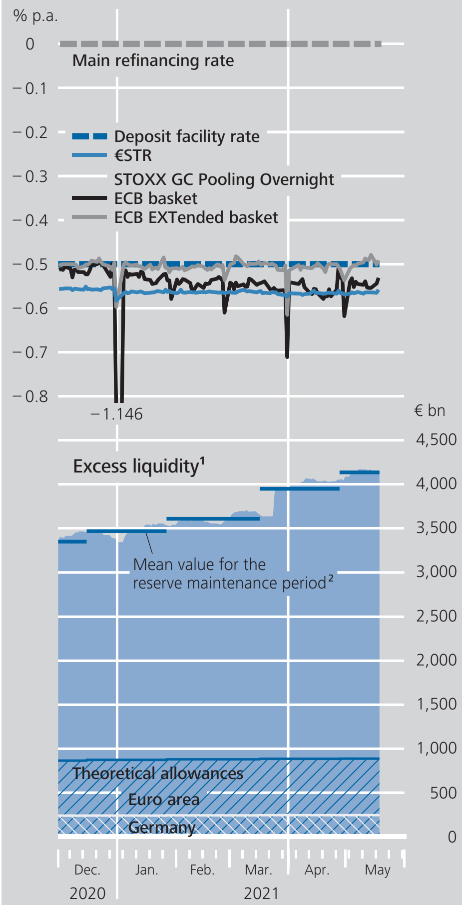
In net terms, there was a considerable increase of €479 billion overall in excess liquidity in the period under review to an average of €3,950 billion. Excess liquidity rose by €138 billion in the January-March 2021 period and increased by a further €341 billion in the subsequent March-April 2021 period. The stronger increase in the second period was primarily due to the TLTRO-III allotment and increased purchase volumes in monetary policy programmes. The higher government deposits in particular had an absorbing effect and prevented excess liquidity from rising even more strongly.

At 99.1%, Eurosystem banks made roughly the same use of the exemption allowances under the two-tier system for remunerating excess reserve holdings in the March-April 2021 period as in the December 2020-January 2021 period (98.9%). In Germany, utilisation of the exemption allowances was very close to the Eurosystem average at 99.0%. The increase in the minimum reserve requirement caused absolute exemption allowances to rise; however, given the much stronger growth in excess liquidity, excess reserves remunerated at -0.50% grew once again (see the adjacent chart). This meant that, on average, around 22% of excess liquidity in the Eurosystem was exempted from remuneration at negative interest rates in the March-April 2021 period, compared to around 24% in the January-March 2021 period, and 25% in the December 2020-January 2021 period (in Germany: 21%, 22% and around 23%, respectively).

In the money market, interest rates remained stable during the period under review, with the exception of the usual volatility around and at the end of the month and quarter in March 2021. As a result, the continued increase in excess liquidity did not lead to any notable downward pressure on overnight interest rates (see the adjacent chart). In the secured market, overnight rates in GC Pooling for the ECB basket were -0.55% on average, dipping to -0.71% for a time at the end of the quarter in March 2021. The rate for the ECB EXTended basket, which contains an extended pool of collateral, was higher, at -0.51% on average, though fluctuations around the reporting dates were milder than they were for the ECB basket. The decline in rates for the ECB basket left the spread between the two rates at 5 basis points on average during the period under review, compared to 3 basis points in the preceding period under review. The backdrop to this was a slight reduction in turnover on the GC Pooling platform for secured transactions with maturities of one day (ON, TN, SN; combined in the Deferred Funding Rate). While turnover after allotment of the seventh TLTRO-III operation at the end of March 2021 mostly hovered below €8 billion, it had generally been above that figure previously. The unsecured euro short-term rate (€STR) stood mostly at -0.57% after allotment of the TLTRO operation, slightly lower than in February and March 2021. €STR turnover remained broadly stable, averaging €44 billion in the period under review.

Central bank interest rates, money market rates and excess liquidity

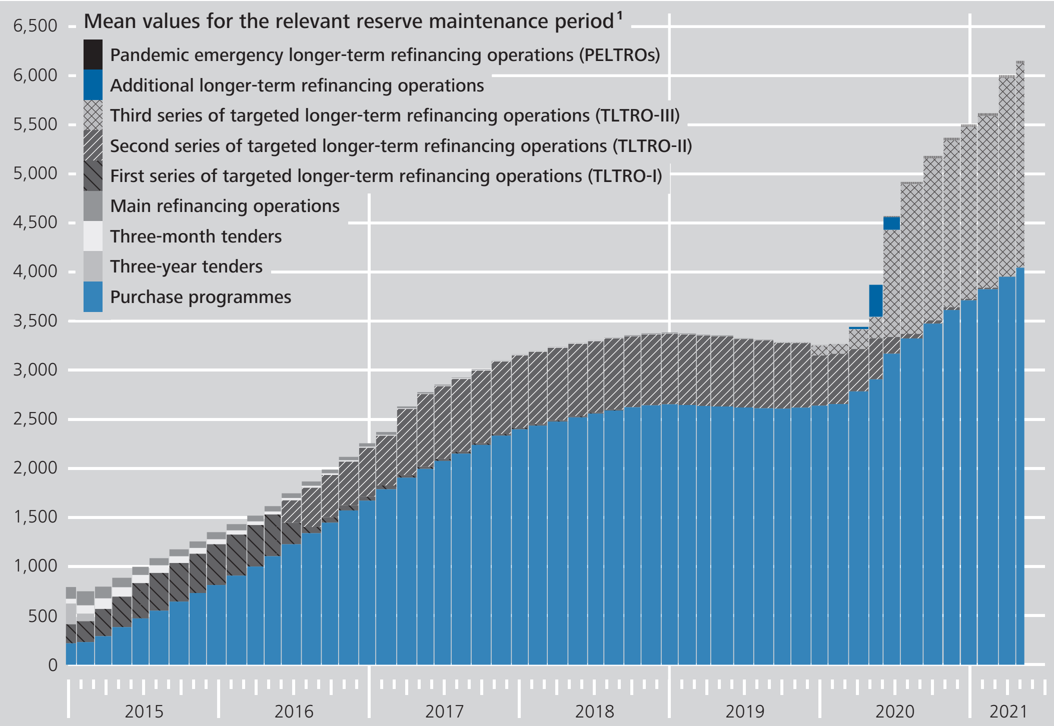
Daily data



Sources: ECB, Eurex Repo and Bundesbank calculations. **1** Central bank balance minus the minimum reserve requirement plus the deposit facility. **2** The last period displayed is still ongoing.
Deutsche Bundesbank

Outstanding liquidity broken down by open market operation 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.
Deutsche Bundesbank

the use of amortised cost accounting.[1] On 14 May, the securities holdings reported under the PEPP amounted to €1,053.1 billion, up by €215.7 billion.

Seventh TLTRO-III sees banks take up €330.5 billion

On 24 March 2021, the seventh operation of the third series of targeted longer-term refinancing operations (TLTRO-III) was settled. In total, 425 banks were allotted €330.5 billion, which significantly exceeded the two preceding operations and represented the second-highest level of demand seen for a TLTRO-III operation. Overall, a combined volume of €2,079.8 billion is currently outstanding for all TLTRO-III operations. The changes to the TLTRO-III conditions in December are likely to be the main reason behind the distinct increase in demand. The ECB Governing Council extended the particularly favourable interest rate terms by one year and raised the maximum amount that TLTRO-III counterparties are entitled to borrow from 50% to 55% of their stock of eligible loans. At €0.4 billion, demand for pandemic emergency longer-term refinancing operations (PELTROs) remained very subdued for the operation that was settled on 25 March 2021.

Excess liquidity exceeds €4 trillion for the first time

The trend increase in excess liquidity continued on account of the ongoing net asset purchases and the allotment of the seventh TLTRO-III operation. As this report went to press, the volume of excess liquidity had exceeded €4 trillion for the first time and stood at €4,146.6 billion, which corresponds to an increase of around €571.1 billion (see the box on pp. 27 ff.).

Short-term money market rates move sideways

Short-term money market rates largely moved sideways over the past few months. At the end of the reporting period, the unsecured euro overnight index average rate (EONIA), which is computed by applying a fixed spread to the euro short-term rate (€STR), was virtually un-

1 In particular, the difference between the acquisition and redemption value is amortised over the security's residual maturity, treated as part of interest income and measured at amortised cost.

changed at -0.48%. The three-month EURIBOR also registered only very limited movements, closing the period at -0.53%.

Slight rise in money market forward rates

Money market forward rates have increased slightly since the ECB Governing Council's monetary policy meeting in March. On balance, however, the rise remained limited when compared with the significant increases seen in the first few months of 2021, particularly in the short-term and medium-term maturity segments. As this report went to press, the forward curve was virtually flat and only very marginally inverted in these maturity segments, meaning that further interest rate cuts are no longer priced in. A very large majority of respondents to surveys conducted in March and April ahead of the Governing Council's monetary policy meetings likewise do not expect to see any further cut in interest rates. There was a somewhat stronger increase in forward rates with longer maturities, which was probably mainly due to a further improvement in market participants' assessment of the medium-term economic outlook. At the same time, the current slope of the money market forward curve indicates that an increase in the Eurosystem's deposit facility rate by 10 basis points is not priced in before mid-2023.

Monetary developments in the euro area

Monetary dynamics still strong due to coronavirus pandemic

In the first quarter of 2021, the broad monetary aggregate M3 once again went up steeply on account of the impact of the coronavirus pandemic. However, growth momentum slowed significantly overall compared with the situation at the outbreak of the coronavirus crisis a year ago. As a result, the annual growth rate of M3 declined markedly during the quarter, but still stood at 10.1% at the end of March. Precautionary considerations on the part of households and enterprises as well as the persistently low level of interest rates were the main factors behind this monetary growth, which led to both sectors continuing to accumulate highly liquid deposits in particular. On the counterparts side, the Eurosystem's continued asset purchases boosted monetary growth. Moreover, banks' lending to the domestic private sector once again registered significant inflows on balance. It was loans to non-financial corporations which picked up substantially in some member countries in the quarter under review. Loans to households remained on an upward path due to households' persistently brisk demand for housing loans. At the same time, however, the banks participating in the Bank Lending Survey (BLS) reported mostly tightening their credit standards due to elevated risk relating to the pandemic.

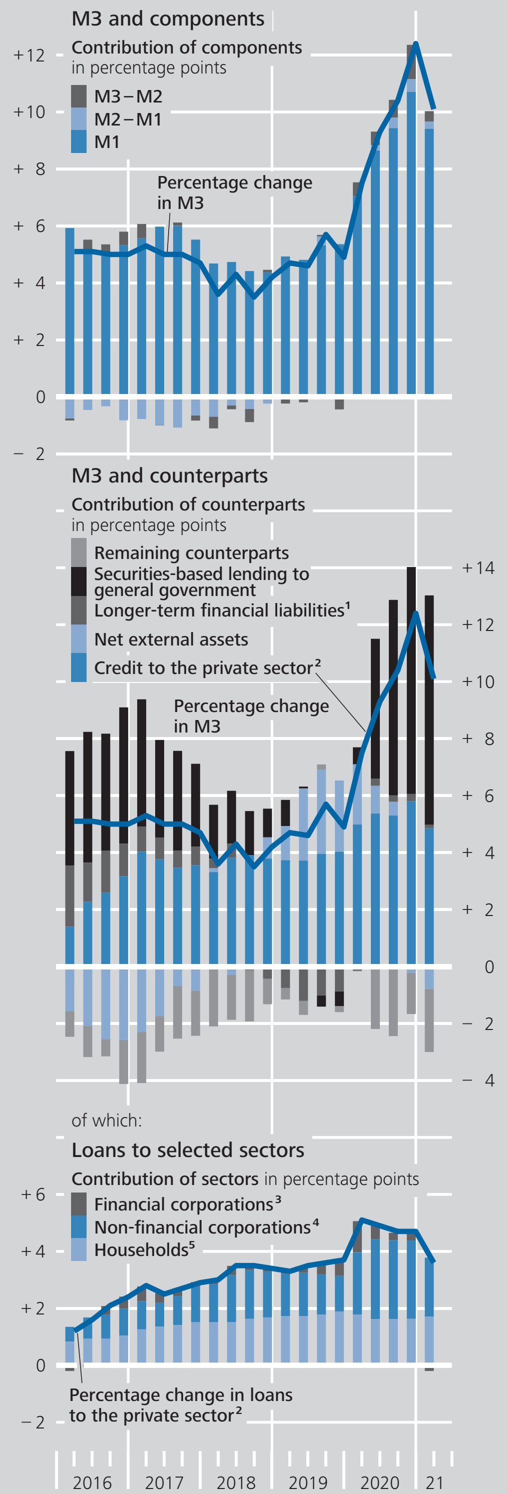
Monetary inflows still mainly driven by overnight deposits

Among the components of M3, overnight deposits once again made by far the largest contribution to monetary growth. The strong growth in household deposits observed in the previous quarters picked up slightly further in the first quarter of 2021; non-financial corporations also increasingly accumulated overnight deposits again. In addition, increased inflows of currency were recorded compared with the pre-pandemic period. This means that households and non-financial corporations continue to exhibit a strong preference for liquidity. In the case of households, the high inflows to short-term deposits are an expression of "forced saving", as the measures taken to combat the pandemic markedly restricted their consumption opportunities across the euro area. Inflows to non-financial corporations' deposits were distributed more heterogeneously among the member countries, depending on the liquidity and income situation of enterprises and the scope of government support measures in each country.

The continued strong inflow to M3 in the first quarter of 2021 was considerably smaller than in the preceding quarters, and that was because financial corporations and other general government did not accumulate any more overnight deposits on balance. Furthermore, non-banks reduced their short-term time deposits and marketable instruments, especially

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 and quasi-corporations. **4** Non-financial corporations and quasi-corporations. **5** Including non-profit institutions serving households.

Deutsche Bundesbank

money market fund shares, to a greater extent during the reporting period. The search for yield in conjunction with the upbeat sentiment in the international financial markets is likely to have reinforced this tendency.

Build-up of securitised lending mainly driven by Eurosystem net purchases

On the counterparts side, monetary growth was once again driven primarily by domestic lending. Though this item, like others, was down again on previous quarters, it remained significantly above pre-pandemic levels, with loans to general government and the private sector increasing in roughly equal measure. Loans to general government were mainly buoyed by the Eurosystem's ongoing net purchases under the APP and PEPP. These loans may have diminished since the onset of the coronavirus pandemic, but, in a persistently challenging environment, they are continuing to help preserve favourable liquidity and funding conditions in the euro area. Credit institutions likewise purchased government bonds in net terms in the first quarter of 2021. Furthermore, they again added to their holdings of corporate bonds and shares on balance, though net growth was significantly weaker than in the previous quarters. Loans to the private sector accounted for the bulk of their exposure, however.

Loans to non-financial corporations continue to grow at a decelerated pace

Loans to non-financial corporations in the euro area registered significant inflows in the first quarter, with longer-term loans in particular posting sizeable gains. Another factor was that the previously high net redemptions of short-term loans weakened significantly. Taken together, net inflows significantly exceeded those seen in the previous two quarters but fell short of the high figures registered in the first two quarters of 2020. The high overall rate of net growth was attributable to a heterogeneous set of developments at the country level. Net lending was up strongly on the two weak previous quarters in Germany and other core countries but lagged behind earlier growth rates in most other countries. One major reason for this is likely to have been the dampening effect on credit demand for investment

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

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

Assets	Q4 2020	Q1 2021	Liabilities	Q4 2020	Q1 2021
Credit to private non-MFIs			Holdings against central government[2]	– 57.1	– 50.2
in the euro area	191.4	138.0			
of which:			Monetary aggregate M3	377.8	208.9
Loans[1]	120.1	117.0	of which components:		
Securities	71.3	21.0	Currency in circulation and		
			overnight deposits (M1)	324.3	267.0
Credit to general government			Other short-term deposits		
in the euro area	176.4	173.6	(M2-M1)	– 11.0	– 18.3
of which:			Marketable instruments (M3-M2)	64.5	– 39.8
Loans	– 1.9	– 1.7			
Securities	178.3	175.3	Longer-term financial liabilities	1.2	– 28.0
			of which:		
Net external assets	– 95.3	– 8.4	Capital and reserves	51.1	26.7
			Other longer-term financial		
Other counterparts of M3	49.4	– 172.5	liabilities	– 50.0	– 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.

Deutsche Bundesbank

purposes that resulted from the third wave of the pandemic and the sluggish rollout of vaccinations. Another is that government grants and reduced-rate loans had caused stocks of short-term bank deposits to swell in the corporate sector over the course of 2020, which also softened demand for further funding overall. There are a number of reasons why demand for bank loans in Germany (and other core countries) increased strongly in the first quarter in spite of these adverse factors. One is the robust growth observed in the construction and real estate sector. Another is that the upswing in global industry has had a positive impact on the propensity to invest amongst export-oriented sectors. In addition, the end of March 2021 saw the expiry of a reference period that determined whether the banks participating in the TLTRO-III operations met the credit growth targets and thus qualified for very favourable funding conditions. This led to a situation where banks located mainly in Germany, Austria and the Netherlands offered loans at very favourable conditions and thus managed to partially make up for their weaker lending activity, by country standards, in the second half of 2020.

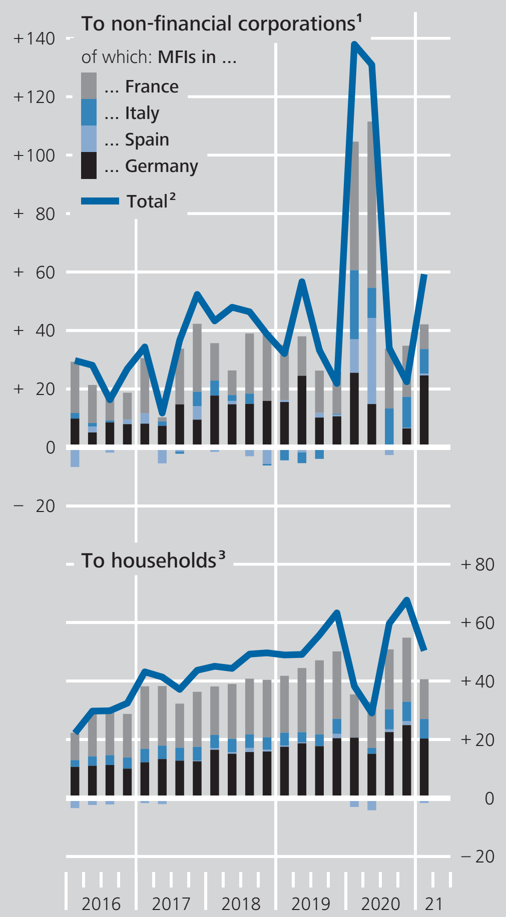
BLS banks report drop in corporate credit demand and tighten standards

The bank managers interviewed as part of the BLS reported a net decline in credit demand amongst euro area non-financial corporations in the first quarter, attributing it primarily to enterprises' persistent reluctance to invest. At the same time, the surveyed banks reported a further tightening of their corporate credit standards overall in the first quarter, though they had stated in the previous round of the survey that far more severe restrictions had been planned for the first quarter. Furthermore, this tightening was significantly milder than that implemented in the previous two quarters. As before, banks mainly attributed their more restrictive policies to a downturn in their risk assessments. First, euro area banks were more pessimistic about the situations of individual sectors and enterprises and about borrowers' creditworthiness than they had been one quarter earlier. Second, they reported tightening their standards on the basis of the depressed economic situation and general economic outlook at present, and also in response to a decline in the underlying value of collateral and their lower risk tolerance. By contrast, the competitive situation, particularly competition from other banks, had an easing effect on standards. Overall terms and conditions in the euro area remained unchanged in the first quarter of the year.

Lending business with households saw euro area banks once again register significant net inflows in the first quarter of 2021. While these

MFI loans to the non-financial private sector in the euro area*

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



Sources: ECB and Bundesbank calculations. * Adjusted for loan sales and securitisation. **1** Non-financial corporations and quasi-corporations. **2** Also adjusted for positions arising from notional cash pooling services provided by MFIs. **3** Including non-profit institutions serving households.
Deutsche Bundesbank

Loans to households on upward path, but lose momentum

were somewhat lower overall than in the two very strong previous quarters, inflows to loans for house purchase, which account for the bulk of activity in this credit segment, continued to grow at above pre-pandemic rates. At the end of the quarter, their annual growth rate increased to 5%, the highest rate seen since 2008. The most significant contributions came from banks in Germany and France, which had already been recording the strongest growth prior to the outbreak of the pandemic. Consumer credit business, on the other hand, contracted significantly in the first quarter owing to the limited opportunities for consumption. However, the decline in this market segment was again smaller than it had been during the first phase of pandemic-related restrictions in the spring of 2020. Other lending, which mainly comprises loans to self-employed persons, showed essentially no change.

BLS banks report decline in demand for housing loans against marginal easing of standards

Data provided by banks responding to the BLS reveal that the first quarter of 2021 saw a net decline in demand for loans for house purchase in the euro area, following the fairly strong increases registered in the previous two quarters. Respondents mainly put this down to the decrease in consumer confidence. The bank managers surveyed by the BLS also identified households' use of their own savings and lending by other banks as additional factors that dampened demand for loans. On the supply side, the banks participating in the survey reported marginally easing their standards for housing loans for the first time again in the first quarter of the year, after tightening them in the previous four quarters. They mainly cited the intense competition as the reason for easing their standards. Banks' poorer assessment of borrowers' creditworthiness as well as their lower risk tolerance, meanwhile, led standards to be made more restrictive.

BLS banks report considerable decrease in demand for consumer credit and other lending

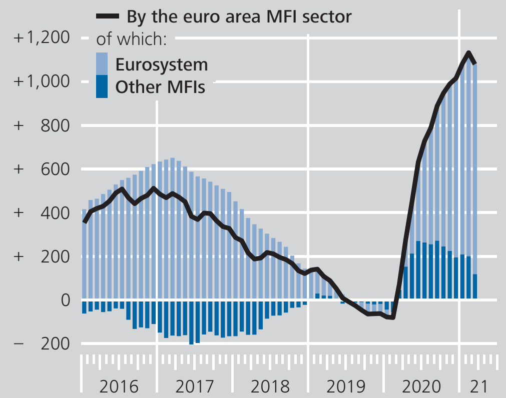
For the second time during the coronavirus crisis, the banks surveyed by the BLS reported a considerable decrease in household demand for consumer credit and other lending. Like in the second quarter of 2020, the current decline in demand can be attributed in particular to a significant deterioration in consumer confidence and a sharp fall in the need for funds to finance durable consumer goods. This reflects the limited opportunities for consumption and the precautionary saving due to the measures taken to contain the pandemic as well as the uncertainty surrounding its economic fallout. Compared to the second quarter of 2020, the banks also highlighted the increased significance of households making use of their own savings. The surveyed banks continued to tighten their credit standards on balance in the first quarter of 2021. The rejection rate rose yet again and is likely to be relatively high at present.

Net external position has no noticeable influence on monetary growth

The net external position of the MFI sector did not noticeably influence monetary growth in the first quarter of 2021. Non-seasonally adjusted balance of payments data, which are currently only available for January and February, indicate that the euro area's persistent current account surplus buoyed the net external position as usual. However, a countervailing effect – one that led to capital exports – was generated by the negative balance of cross-border securities transactions: in an upbeat setting and with the US economy picking up pace, domestic investors showed perceptibly brisker demand on balance for foreign securities than non-resident investors did for equivalent domestic assets. Unlike in the fourth quarter of 2020, when non-resident investors offloaded government bonds on a large scale, the first quarter of 2021 saw investors, including foreign ones, purchase domestic securities in net terms, focusing their attention on equity shares and investment fund shares.

Securities-based lending to general government in the euro area

€ billion, 12-month accumulated flows



Sources: ECB and Bundesbank calculations.
Deutsche Bundesbank

German banks' deposit and lending business with domestic customers

Overnight deposits cause huge increase in deposit business

German banks significantly expanded their deposit business with domestic customers in the first quarter of 2021 as resident money holding sectors once again showed a very strong preference for overnight bank deposits. This coincided with these sectors making further distinct reductions to their short-term time deposits and all of their long-term deposits. The ongoing accumulation of overnight deposits at an even brisker pace should also be seen against the backdrop of the persistently high uncertainty surrounding the path of economic recovery given the renewed uptick in the number of coronavirus infections. The low general level of interest rates and the narrow spread between short-term and long-term deposits provided additional tailwinds for this development (see the chart on p. 36).

Households and non-financial corporations behind biggest build-up of deposits

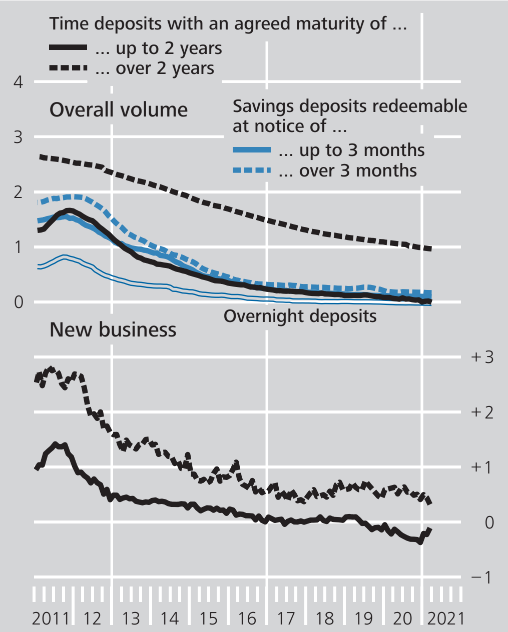
Alongside households, it was mainly non-financial corporations that added significantly to their holdings of overnight deposits. There are two aspects to this development. First, it was a reflection of the high level of corporate borrowing in the reporting quarter. Second, the disbursement of the government coronavirus assistance funds, some of which had been agreed upon back in the autumn, also picked up significantly in the reporting quarter. Another factor fuelling the substantial accumulation of overnight deposits by households was the absence of major consumption expenditure, including on items such as travel, due to the coronavirus-related restrictions. Moreover, the expiry of the VAT rate reductions at the end of 2020 gave households an incentive to make any planned major purchases before the end of the year.

Lending business with non-banks very dynamic

Lending business conducted by banks in Germany with domestic non-banks in the first quarter of 2021 was as lively as their deposit business, with loans to non-financial corporations in particular gaining significant momentum compared with the third and fourth quarters of last year. Household demand for loans for house purchase remained consistently strong as well. In addition to stepping up their loan volumes, banks in Germany also significantly expanded their holdings of securities

Interest rates on bank deposits in Germany*

% p.a., monthly data



* Deposits of households and non-financial corporations according to the harmonised MFI interest rate statistics (volume-weighted interest rates). Interest rate levels for overnight and savings deposits may also be interpreted as new business due to potential daily changes in interest rates.

Deutsche Bundesbank

issued by the private sector, focusing their purchases primarily on shares issued by domestic enterprises. By contrast, their lending business with the public sector increased only marginally overall, with the perceptible increase in securitised lending to general government offsetting a similarly sized reduction in loans.

Households register strongest inflow, driven by loans for house purchase

Loans to households once again saw the largest net inflows in the first quarter of 2021. In net terms, current lending business with this sector was driven by housing loans alone, the growth of which fell just short of the strong increase observed in the previous quarter. This is consistent with data reported by banks surveyed as part of the BLS, which indicate that demand for housing loans remained consistently high in the first quarter. As before, the BLS banks cited the low general level of interest rates, the positive outlook on the residential real estate market and the prospective rise in prices for residential real estate as the main factors propelling demand. The expiry of the home buyers' child benefit programme, for which house purchasers could apply if they purchased a home on or before 31 March 2021, and refinancing, debt restructuring and renegotiation were also reported to have stimulated demand. On balance, the growth rate of loans taken out for house purchase rose to 6.7% on the year, representing its highest value since 2000.

BLS standards, terms and conditions unchanged overall

Credit standards for housing loans remained unchanged on balance in the first quarter of the year for the second time in succession. Unlike the first wave of the pandemic, the second and third waves have therefore not yet had a material impact on housing loan standards. The rejection rate remained unchanged on the quarter after increasing over the each of three previous quarters, leaving it still at what is likely to be an elevated level at present. Terms and conditions agreed in loan contracts likewise remained unchanged overall after being persistently tightened since spring 2019.

Coronavirus restrictions lead to consumer credit being scaled back

Unlike loans for house purchase, the supply of consumer credit to households was scaled back discernibly in the first quarter of 2021, though the decline was considerably smaller than it had been in spring 2020. This probably comes mainly as a result of the ongoing restrictions that are still curbing many forms of economic and social activity. That observation is largely supported by the BLS survey data, with bank managers highlighting the lower level of consumer confidence and the reduced expenditure on durable consumer goods as having negative effects on demand. They also reported that consumers utilising their savings as a source of equity finance was another factor that dampened demand for bank loans.

Lending policies eased in consumer credit business

Credit standards in the consumer credit segment were eased marginally on balance in the first quarter. The rejection rate remained steady in the reporting quarter after rising significantly in the second and third quarters of 2020 and declining in the final three months of that year. Terms and conditions agreed in loan contracts were unchanged in this credit segment for the second time in succession.

Sharp uptick in demand for bank loans among non-financial corporations

Besides registering robust growth in their lending business with households, banks in Germany also significantly expanded their supply of loans to non-financial corporations in the first quarter of 2021. After two weak previous quarters, demand for bank funding among non-financial corporations bounced back strongly and was broadly distributed across the different maturity segments. Medium-term and long-term loans met with lively interest from investors, while loans with agreed maturities of up to one year saw demand pick up again for the first time since March 2020.

Rising funding requirements amongst enterprises not directly negatively impacted by COVID-19

Much of the stronger demand for loans was accounted for by enterprises from the construction and real estate sector, service providers operating in the field of digitalisation and research and development activities, and export-oriented industry. Their well-filled order books and the favourable outlook suggest that their funding requirements have probably increased. By contrast, the financing needs of sectors particularly affected by the coronavirus-related restrictions during the reporting quarter were covered at least in part by the disbursement of government grants, which grew substantially in size on the quarter.

Credit supply given an additional boost by bank motives

At the same time, the current supply of loans to non-financial corporations was given an additional boost by bank motives. In an effort to meet their net lending benchmarks before the TLTRO-III reference period expired at the end of March, some banks participating in these refinancing operations granted loans at very favourable conditions.

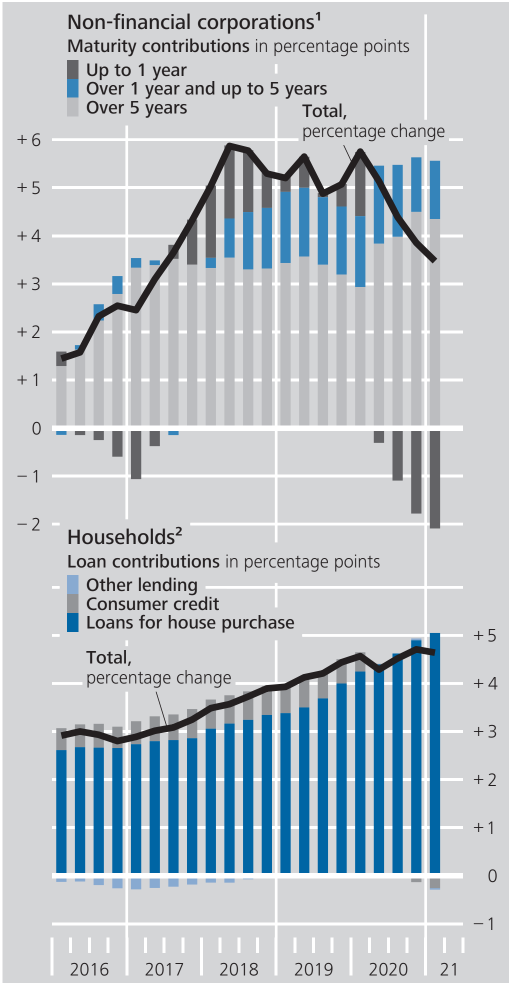
BLS data consistent with aggregate developments

Evidence of further factors can be found in the latest BLS data. Reporting banks once again identified refinancing, debt restructuring and renegotiation and increased financing needs for inventories and working capital as major factors driving the observed increase in credit demand. The delivery bottlenecks that materialised during the reporting quarter and the price increases for intermediate goods are also likely to have contributed to this development. According to the BLS data, funding requirements for fixed investment also added marginally to the livelier demand for the first time since the fourth quarter of 2019. Meanwhile, enterprises' scope for internal financing combined with the uncertainty triggered by COVID-19 over the prospects for the economy dampened demand for loans, all other things being equal.

At the same time, BLS banks reported that they had again made their lending policies in cor-

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

Year-on-year change, 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.

Deutsche Bundesbank

MFI* lending and deposits in Germany

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

Item	2020 Q4	2021 Q1
Deposits of domestic non-MFIs[1]		
Overnight	54.9	88.4
With an agreed maturity of		
up to 2 years	– 20.9	– 21.2
over 2 years	– 5.9	– 8.1
Redeemable at notice of		
up to 3 months	– 0.9	4.1
over 3 months	– 0.9	– 1.1
Lending		
to domestic general government		
Loans	– 3.0	– 3.7
Securities	– 9.0	4.4
to domestic enterprises and households		
Loans[2]	34.0	38.7
of which: to households[3]	24.7	20.2
to non-financial corporations[4]	5.7	16.3
Securities	0.2	9.3

* As well as banks (including building and loan associations, but excluding the Bundesbank), monetary financial institutions (MFIs) here also include money market funds. 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.

Deutsche Bundesbank

Credit lines in corporate banking more restrictive overall

porate banking more restrictive in response to the economic fallout from the coronavirus pandemic, tightening their credit standards for corporate financing somewhat on balance in the first quarter of 2021. This marked a continuation of the steady tightening of lending standards since COVID-19 first emerged in Germany in the first quarter of 2020, albeit to a lesser extent than during the financial crisis. Institutions attributed the tightening of standards to their more pessimistic assessments of both the situations of individual sectors and enterprises as well as of borrowers' creditworthiness, and cited the depressed general economic situation and the economic outlook as similarly important factors. In addition, the decline in the underlying value of collateral and in banks' risk tolerance had a slightly restrictive effect on standards. Marginally expansionary effects, on the other hand, were produced by competition with other banks and by an improved funding situation in the money and bond market. The proportion of rejected loan applications remained unchanged over the previous quarter during the reporting period. Following the rises observed last year, the rejection rate is probably still at an elevated level. In the case of borrowers from sectors particularly affected by the pandemic (such as hotel and restaurant services, tourism and retail), BLS banks reported that some did not even go as far as to submit formal loan applications because their informal enquiries had already been rejected out of hand. Unlike credit standards, overall terms and conditions were not tightened further on balance.

Virtually no change in German banks' funding environment

Against the backdrop of the situation in the financial markets, German banks, in response to the ad hoc questions in the April BLS, reported little change overall in their funding situation in the first quarter compared with the previous quarter. Only as regards funding through medium-term to long-term debt instruments did the positive development observed in the two previous quarters persist into the reporting period.

Eurosystem purchase programmes improve banks' liquidity position and market funding conditions

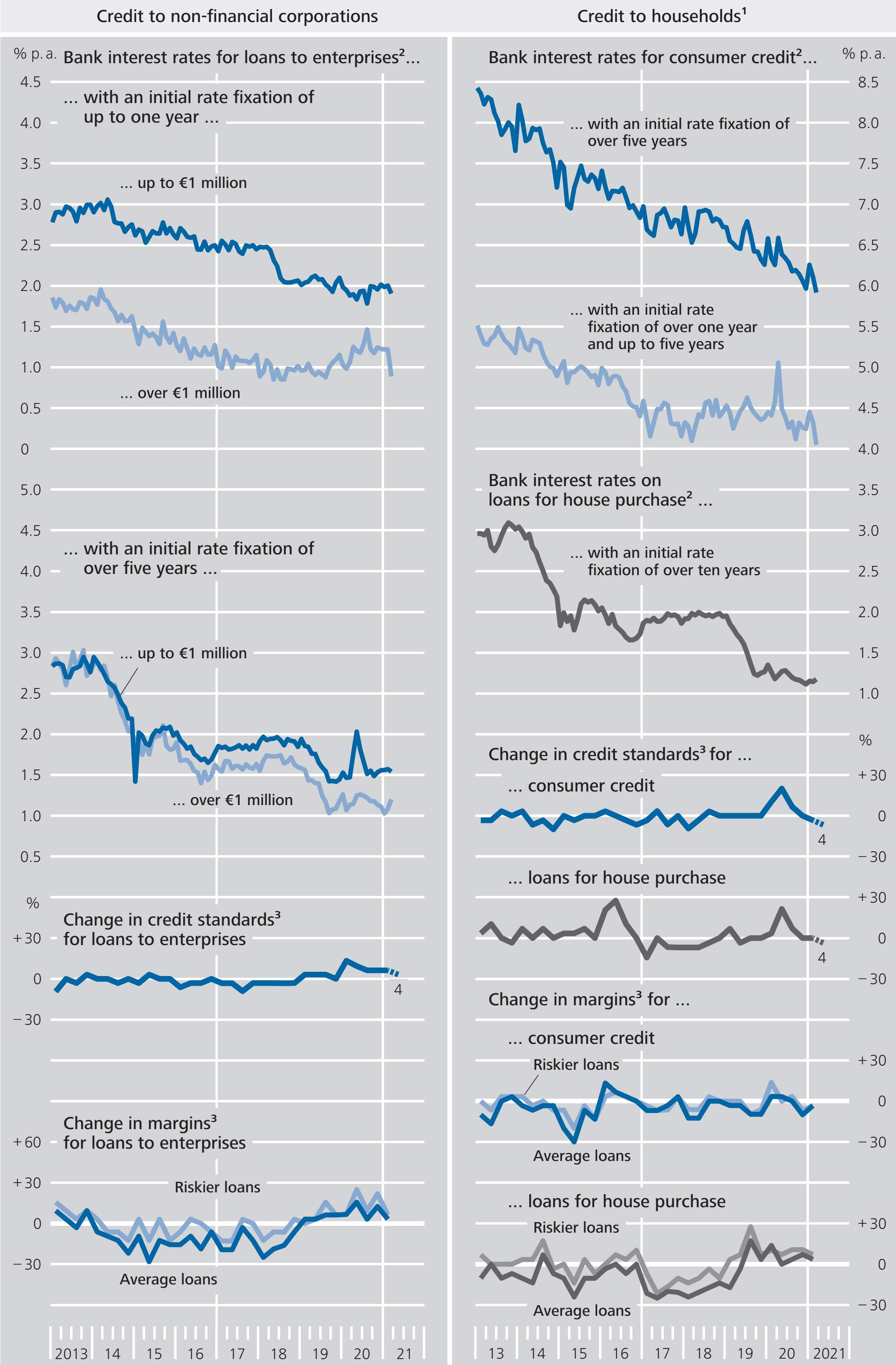
Over the past six months, the Eurosystem purchase programmes (APP and PEPP) helped improve the liquidity position of commercial banks and their market funding conditions, but continued to impact negatively on bank profitability through net interest income. The purchase programmes did not contribute to credit growth over the past six months.

Two-tier system for excess liquidity softens adverse impact on profitability

In addition, the negative interest rate on the deposit facility squeezed banks' net interest income once again, depressing lending and deposit rates and pushing up fees for deposits. Banks singled out loans for house purchase as the only category in which the negative deposit facility interest rate had increased volumes to any notable degree. The two-tier system for remunerating excess liquidity holdings did, however, soften the adverse impact on profitability.

Twelve banks from the German sample took part in the TLTRO-III operation in December 2020, while 17 participated in the March 2021

Banking conditions in Germany



1 Including non-profit institutions serving households. 2 New business. According to the harmonised MFI interest rate statistics. 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 Q2 2021.

Deutsche Bundesbank

TLTRO-III funds used primarily for loans and as a substitute for TLTRO-II funds

operation, mainly on account of the attractive conditions of these operations. Banks reported using the uptake in funds primarily for lending to the private non-financial sector and as a substitute for TLTRO-II funds and maturing debt instruments. They stated that they would also be participating in future operations mainly because of the TLTRO-III operations' attractive conditions. The TLTRO-III operations had barely any impact on banks' lending policies.