

Monetary policy and banking business

Monetary policy and money market developments

ECB Governing Council announces moderately lower pace for PEPP purchases compared with the preceding two quarters

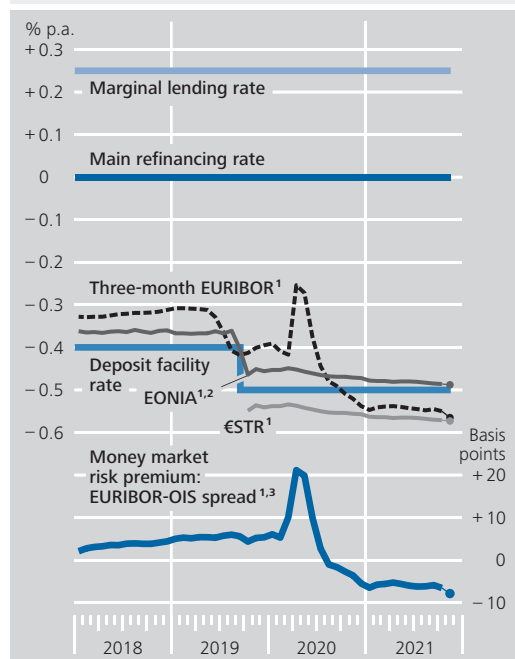
In September 2021, based on a joint assessment of financing conditions and the inflation outlook, the Governing Council of the ECB judged that favourable financing conditions could be maintained with a moderately lower pace of net asset purchases under the pandemic emergency purchase programme (PEPP) than in the previous two quarters. Moreover, net asset purchases will continue with an unchanged anticipated total envelope of €1,850 billion until at least the end of March 2022 and, in any case, until the Governing Council judges that the coronavirus crisis phase is over. If favourable financing conditions can be maintained with smaller asset purchase flows overall, the envelope of €1,850 billion need not be used in full. Equally, the total envelope can also

be increased if necessary. The Governing Council also confirmed its other measures, namely the level of the key ECB interest rates, its forward guidance on their likely future evolution, and its purchases under the asset purchase programme (APP) at a monthly pace of €20 billion.

At the beginning of September, compared to the last quarterly assessment in June, the ECB Governing Council judged that financing conditions for firms, households and the public sector had remained favourable. Moreover, the inflation outlook in the new macroeconomic projections has been revised upwards again. The ECB staff projections expect the current rise in inflation to be largely temporary, however, and for inflation to remain well below 2% over the medium term. Against this backdrop, the Governing Council remains of the opinion that favourable financing conditions are essential for the economy to continue its recovery and to offset the negative impact of the pandemic on inflation. However, it also sees upside risks to inflation. If supply bottlenecks last longer and feed through into higher than anticipated wage rises, price pressures could be more persistent.

Recovery of growth and inflation still depends on favourable financing conditions

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 November 2021.

In October, the Governing Council of the ECB confirmed its September assessment of financing conditions. Despite a rise in market interest rates since its meeting in early September, overall financing conditions remained favourable for firms, households and the public sector. In terms of inflation, the Governing Council noted that, while the current phase of higher inflation will last longer than originally anticipated, it still expects inflation to decline in the course of next year. At the same time, if persistent supply bottlenecks feed through into higher than anticipated wage rises or if the economy returns more quickly to full capacity, price pressures could become stronger.

ECB Governing Council confirms assessment of financing conditions in October

Money market management and liquidity needs

In the period under review from July to November 2021,¹ excess liquidity in the Euro-system rose by a total of €151.9 billion to an average of €4,391.3 billion. Of this overall rise in excess liquidity, €101.6 billion was attributable to the fifth reserve maintenance period of 2021 (July-September) and €50.3 billion was attributable to the sixth reserve maintenance period of 2021 (September-November), even though similarly large volumes were purchased as part of the liquidity-providing purchase programmes in both of these reserve maintenance periods. Developments in the liquidity-absorbing autonomous factors were the main reason for this difference.

In the period under review, additional central bank liquidity was provided primarily through a total of €267.8 billion worth of net asset purchases conducted as part of

the purchase programmes. The majority of these purchases were attributable to the pandemic emergency purchase programme (PEPP). As at 12 November 2021, the balance sheet holdings of the asset purchase programmes amounted to €4,611.2 billion (see the table on p. 30). During the period under review, the average outstanding tender volume in the euro area also grew by €14.0 billion to €2,210.0 billion. The allotment volume of €97.6 billion for the ninth targeted longer-term refinancing operation (TLTRO-III) in September exceeded the first voluntary repayments for the first to fifth TLTRO-III operations, which resulted in a net provision of liquidity overall. At €1.3 billion in total, there was little demand for the

¹ Here, the averages of the sixth reserve maintenance period of 2021 (September-November) are compared with the averages of the fourth reserve maintenance period of 2021 (June-July).

Factors determining banks' liquidity*

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

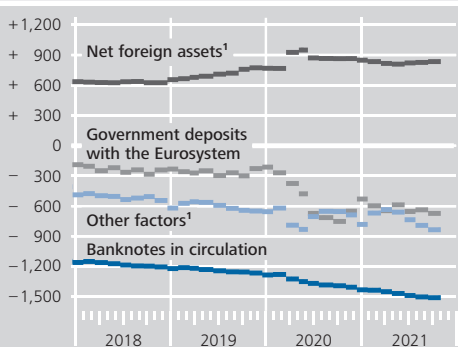
Item	2021	
	28 July to 14 Sep.	15 Sep. to 2 Nov.
I. Provision (+) or absorption (–) of central bank balances due to changes in autonomous factors		
1. Banknotes in circulation (increase: –)	– 14.1	– 7.5
2. Government deposits with the Eurosystem (increase: –)	+ 16.6	– 35.6
3. Net foreign assets ¹	+ 5.0	+ 8.4
4. Other factors ¹	– 55.9	– 43.3
Total	– 48.4	– 78.0
II. Monetary policy operations of the Eurosystem		
1. Open market operations		
a) Main refinancing operations	+ 0.1	+ 0.0
b) Longer-term refinancing operations	+ 17.2	– 3.3
c) Other operations	+ 134.4	+ 133.4
2. Standing facilities		
a) Marginal lending facility	+ 0.0	+ 0.0
b) Deposit facility (increase: –)	– 30.0	+ 28.1
Total	+ 121.7	+ 158.2
III. Change in credit institutions' current accounts (I. + II.)	+ 73.1	+ 80.3
IV. Change in the minimum reserve requirement (increase: –)	– 0.7	– 1.9

* 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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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.

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Eurosystem purchase programmes

€ billion

Programme	Change across the two reserve periods	Balance sheet holdings as at 12 Nov. 2021
Active programmes¹		
PSPP	+ 34.7	2,470.4
CBPP3	+ 4.6	296.5
CSPP	+ 15.3	305.4
ABSPP	- 1.7	28.2
PEPP	+ 225.6	1,501.4
Completed programmes		
SMP	- 10.6	6.5
CBPP1	+ 0.0	0.4
CBPP2	+ 0.0	2.4

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

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tenth pandemic emergency longer-term refinancing operation (PELTRO) in September (previous operation in June 2021: €0.5 billion). At the same time, three PELTROs amounting to €22.1 billion were repaid, leading to a net absorption of liquidity from the PELTROs. Uptake of the regular main refinancing operations and three-month tenders likewise remained very subdued. In Germany, the outstanding volume of all refinancing operations rose by €4.9 billion to an average of €439.3 billion. As a result, Germany's share of the outstanding tender volume in the Eurosystem remained unchanged at around 20%.

In the sixth reserve maintenance period of 2021, liquidity needs stemming from autonomous factors rose by €126.4 billion compared to the fourth reserve maintenance period of 2021 (June-July), reaching a new record high of €2,177.4 billion (see the table on p. 29).² The main driver of this growth was the combined total of net foreign assets and other factors, which are considered together owing to liquidity-neutral valuation effects. The resulting liquidity needs rose by €85.8 billion, which was attributable chiefly to increased non-monetary policy deposits, such as deposits of foreign central banks. Other major liquidity-absorbing effects originated from the sharp rise in banknotes in circulation, which grew by €21.6 billion to €1,507.4 billion, and the increase in government deposits, which rose by €19.0 billion to €671.3 billion. In Germany, net banknote issuance went up by €17.0 billion to €863.8 billion, and government deposits grew by €10.9 billion to €217.7 billion. Over the reporting period, the minimum reserve requirement climbed by an average of €2.6 billion to €152.8 billion in the sixth reserve maintenance period of 2021, which led to an additional need for central bank liquidity. In Germany, the reserve requirement went up by €0.3 billion to €41.6 billion.

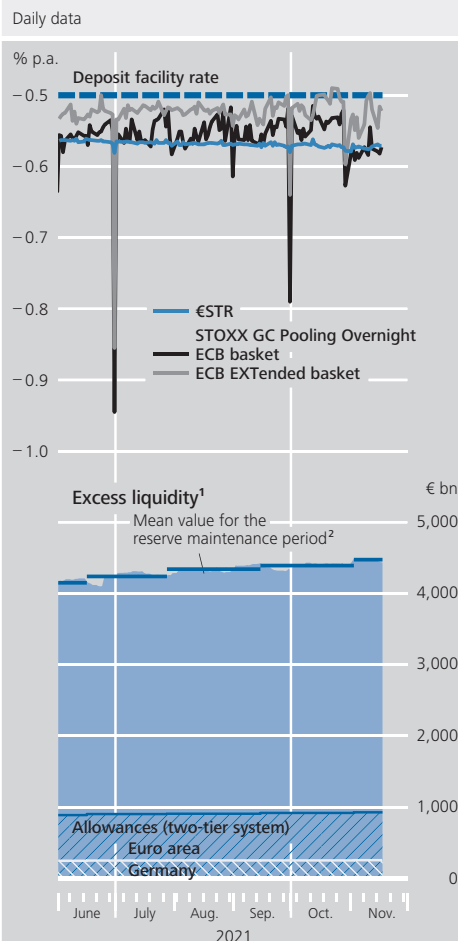
The use of exemption allowances under the two-tier system for remunerating excess reserve holdings increased over the reporting period from 99.2% to 99.3%. In Germany, use of these exemption allowances remained steady at 99.2%. The increase in the minimum reserve requirement caused absolute exemption allowances to rise. However, given the stronger growth in excess liquidity, excess liquidity holdings re-

² Average of the sixth reserve maintenance period of 2021 (September-November 2021) compared with the average of the fourth reserve maintenance period of 2021 (June-July 2021).

munerated at -0.50% grew once again (see the adjacent chart). As a result, an average of 20.7% (as in the previous period) of excess liquidity in the Eurosystem was exempted from negative remuneration during the sixth reserve maintenance period of 2021 (Germany: 20.2%; previous period: 20.4%).

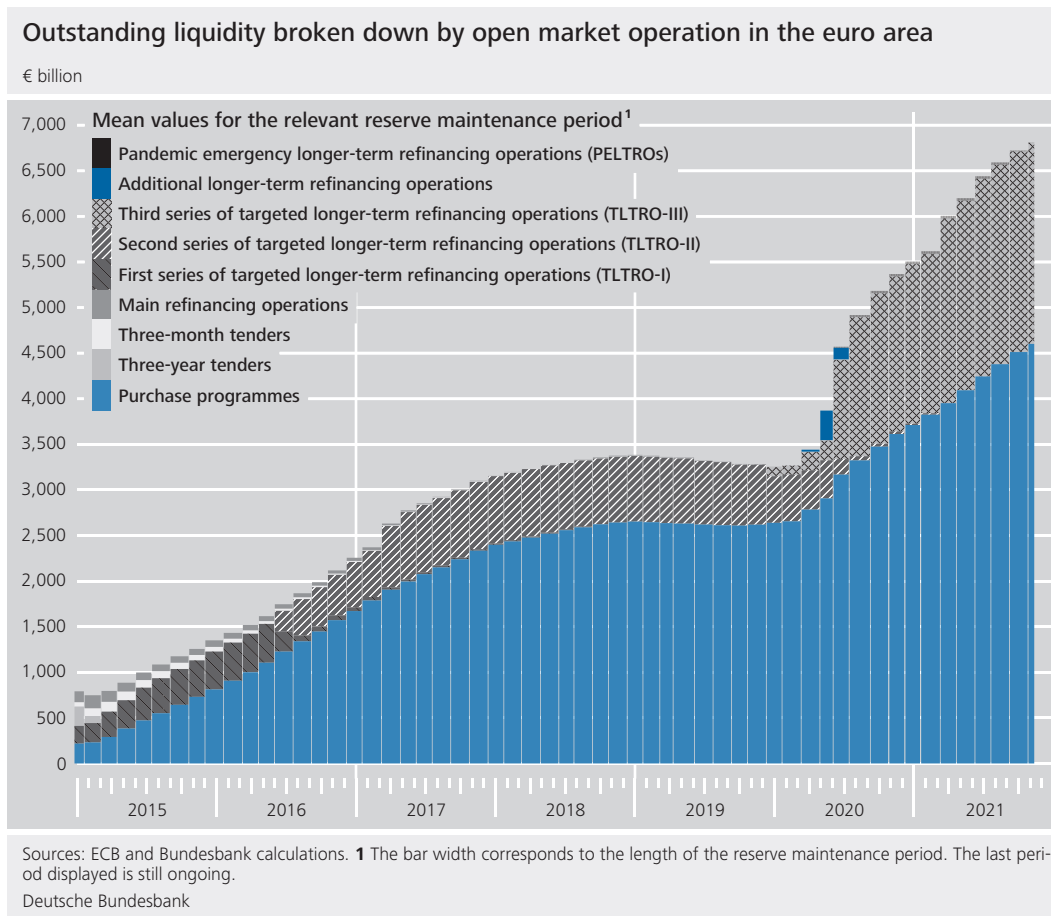
During the reporting period, overnight interest rates on the euro money market continued to move in line with the deposit facility rate (see the adjacent chart). In this context, the unsecured euro short-term rate (€STR) was set at -0.57% on average during the sixth reserve maintenance period of 2021 and thus stood 7 basis points below the deposit facility rate, as it had in the preceding period. On average, turnovers remained essentially unchanged in both of the periods under review, at €48.5 billion and €48.6 billion respectively. During the sixth reserve maintenance period of 2021, secured overnight money on the GC Pooling trading platform was traded at -0.55% on average in the ECB basket, which was 5 basis points below the deposit facility rate; the spread thus remained almost unchanged compared with the previous period. In the ECB EXTended basket, with its larger pool of securities, overnight money transactions were conducted at an average rate of -0.52% in both periods. By contrast, overnight rates in both baskets were around 1 basis point lower on average during the fourth reserve maintenance period of 2021. The aggregate overnight volume of the ECB and ECB EXTended baskets declined from an average of €3.6 billion per day in the fifth reserve maintenance period of 2021 to €3.0 billion in the subsequent period. Rates were lower at end-September 2021, as is typical for the end of a quarter. The €STR fell by just under 1 basis point to -0.58% compared with the previous day. For a period of time on this day,

Deposit facility rate, money market rates and excess liquidity



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.
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the price of secured overnight money in the ECB basket decreased significantly for very low volumes, falling by around 27 basis points to -0.79%. In the ECB EXTended basket, the overnight rate dropped by 14 basis points to -0.64%. On the whole over the reporting period, GC Pooling overnight interest rates remained considerably more volatile than the €STR. For example, the overnight rate in the ECB EXTended basket also exceeded the deposit facility rate for a short period of time in October 2021.



APP and PEPP securities holdings recorded on balance sheet see further expansion

The APP holdings recorded on the balance sheet have risen by €50.9 billion since mid-August. On 12 November, the Eurosystem held assets totalling €3,100.4 billion as part of the APP (see the box on pp. 29 ff. for a breakdown of the holdings by individual programme). The reported holdings continue to be influenced by the smoothing over time of reinvestments in line with the technical parameters agreed upon in December 2018 and by the use of amortised cost accounting.¹ Securities holdings reported under the PEPP amounted to €1,501.4 billion on 12 November, up by €204.5 billion.

Ninth TLTRO-III sees banks take up €97.6 billion

On 29 September 2021, the ninth operation of the third series of targeted longer-term refinancing operations (TLTRO-III) was settled, with 152 banks taking up a total of €97.6 billion. At the same time, there were voluntary repayments of funds provided under earlier TLTRO-III operations in the amount of €79.2 billion. Overall, a combined volume of €2,206.3 billion is thus outstanding for all TLTRO-III operations.

Uptake of the pandemic emergency longer-term refinancing operation (PELTRO) concluded one day later, at €1.3 billion, was once again very low. A total of just €2.3 billion is currently outstanding in the PELTROs.

The trend increase in excess liquidity continued on the back of the Eurosystem's ongoing net asset purchases under the APP and the PEPP. As this report went to press, the volume of excess liquidity stood at €4,448.5 billion, which corresponds to an increase of around €113.4 billion since mid-August (see the box on pp. 29 ff.).

Excess liquidity continues to rise

Short-term money market rates have moved within a narrow corridor since August, but have fallen slightly at the current end. At the end of the reporting period, the unsecured euro overnight index average rate (EONIA),

Short-term money market interest rates down slightly

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.

which is computed by applying a fixed spread to the euro short-term rate (€STR), was down by one basis point to -0.49%. The three-month EURIBOR fell somewhat more sharply compared to August, standing most recently at -0.57%.

Money market forward rates significantly higher

Money market forward rates have risen significantly since the ECB Governing Council's monetary policy meeting in September, with market participants increasingly pricing in an earlier date for the first Eurosystem interest rate hike. On the one hand, this was due to the perception of rising inflation risks in light of unexpected upside developments and more persistent inflation trends. On the other hand, developments in the international environment are also likely to have played a role, with several major central banks signalling an upcoming tightening of monetary policy. An initial interest rate increase at the end of 2022 is therefore already priced into the money market forward rates at present. However, this is probably mainly due to risk premia, which distort the informative content of the forward rates with regard to the expected interest rate path. The ECB Survey of Monetary Analysts prior to the October meeting also lends weight to this interpretation. Although the time at which survey participants are expecting the first interest rate hike also shifted forward slightly in comparison to the September survey round, respondents still anticipate that it will take place in the second quarter of 2024.

Monetary developments in the euro area

Gradual normalisation of monetary growth

The broad monetary aggregate M3 showed considerable growth in the third quarter of 2021, too, driven as before by highly liquid overnight deposits. Although inflows were slightly more extensive than in the previous quarter, they were still considerably lower than last year's high coronavirus-related net inflows. In this context, the annual growth rate of M3

sank by just over 1 percentage point to 7.4%. However, the pace of normalisation slackened.

On the counterparts side, the Eurosystem's continued asset purchases boosted monetary growth. Banks' lending to the domestic private sector also saw a significant increase. For one thing, non-financial corporations' demand for loans picked up momentum on the back of their increased funding needs for investment purposes. For another, household demand for loans for house purchase remained consistently strong. At the same time, the banks participating in the Bank Lending Survey (BLS) reported that, in the third quarter, they had tightened their credit standards only for loans for house purchase.

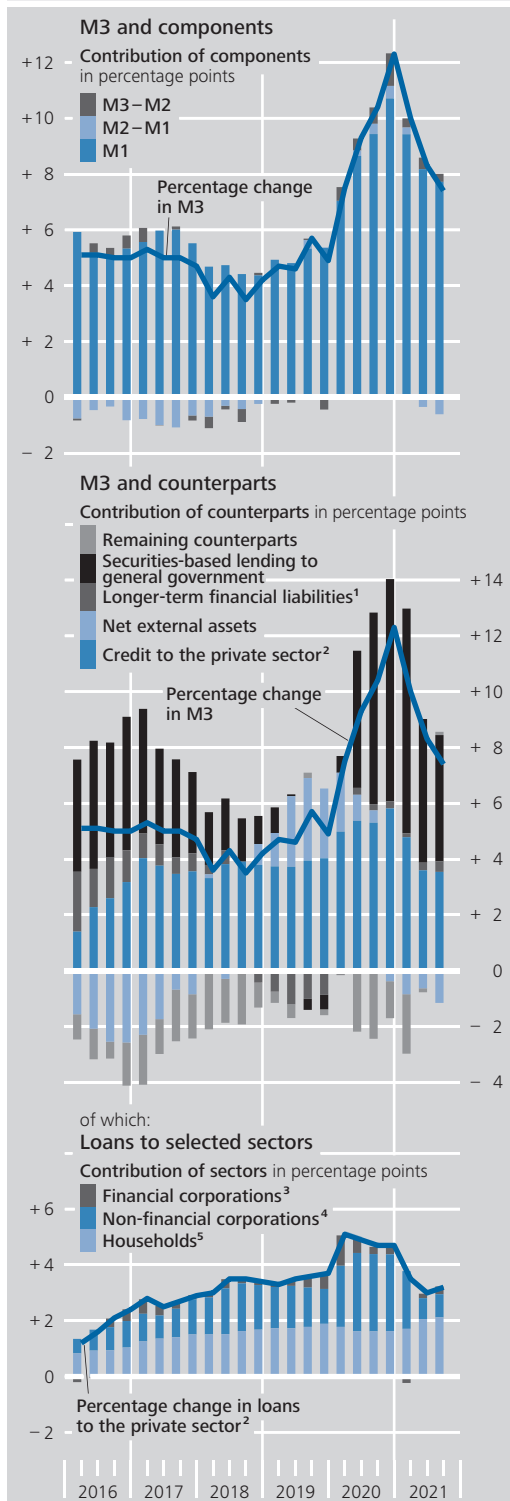
Overnight deposits were once again the M3 component that made the most significant contribution to annual growth. The low interest rate level means that their opportunity costs remain low. As in the preceding quarters, households accounted for the largest net inflows. Although net inflows were slightly up on the quarter, they were considerably lower than the high inflows observed during the first three waves of the pandemic. Households' short-term savings deposits followed a very similar pattern. There are thus signs that the accumulation of deposits is normalising as households' options for consumption have improved after pandemic-related containment measures were eased further.

M3 growth still driven by overnight deposits

Non-financial corporations also recorded relatively large inflows to their overnight deposits. These inflows were somewhat more substantial compared to the previous quarter, which is likely also connected to the ongoing bottlenecks in the supply of intermediate goods that is currently hampering production and investment in many sectors. This aggregate picture, however, masks fairly heterogeneous developments in the individual euro area countries brought about by differences in the degrees to which they have been affected by the pan-

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.

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demical and the ways in which they are dealing with it.

On the counterparts side, monetary growth was once again driven by the expansion in lending to domestic non-banks, which, after a weaker preceding quarter, returned to the high level recorded in the first quarter of 2021. Again, securities-based lending to general government made the largest contribution (see the lower chart on p. 36). This is due to the persistently high monthly net purchases of government bonds by the Eurosystem under the APP and the PEPP. At the same time, commercial banks reduced their government bond holdings to a lesser extent on balance than they had in the previous quarter. In addition, lending to the domestic private sector registered substantial growth, particularly in the area of loans. Securitised lending to the private sector recorded only moderate inflows, on balance.

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

Loans to non-financial corporations increased perceptibly on balance in the third quarter, after having fluctuated strongly in the first half of the year as a result of efforts to meet the credit growth targets under TLTRO-III.² The annual growth rate rose to a moderate 2.1% by the end of September. Loans in the long-term maturity segment, in particular, saw an increase, but short-term loans also rose slightly on balance (see the upper chart on p. 36). Across Member States, lending to non-financial corporations was as heterogeneous as it had been before the outbreak of the coronavirus pandemic, with the bulk of the net inflows stemming from banks in Germany and France. By contrast, banks in Italy and Spain scaled back their loans to non-financial corporations slightly in net terms, as they had done in the previous quarter.

Marked recovery in lending to non-financial corporations ...

Lending was supported, on the one hand, by factors including the ongoing economic recovery in the euro area and the associated increase in enterprises' propensity to invest. On the

... bolstered by economic recovery and low bank lending rates

² See Deutsche Bundesbank (2021a, 2021b).

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

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

Assets	Q2 2021	Q3 2021	Liabilities	Q2 2021	Q3 2021
Credit to private non-MFIs in the euro area	47.2	134.2	Holdings against central government ²	- 41.8	46.0
of which:			Monetary aggregate M3	208.7	251.9
Loans ¹	38.4	121.5	of which components:		
Securities	8.7	12.7	Currency in circulation and overnight deposits (M1)	245.7	254.0
Credit to general government in the euro area	109.2	182.6	Other short-term deposits (M2-M1)	- 46.0	- 9.4
of which:			Marketable instruments (M3-M2)	9.0	7.4
Loans	11.9	- 8.2	Longer-term financial liabilities of which:	- 19.3	- 4.3
Securities	97.2	190.8	Capital and reserves	30.0	2.6
Net external assets	- 7.3	- 49.0	Other longer-term financial liabilities	- 49.3	- 6.9
Other counterparts of M3	- 1.4	25.8			

* 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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other, demand for credit was bolstered by bank lending rates that remained close to all-time lows. However, the dampening factors seen in the previous quarters continued to have an impact. The generous liquidity buffers grew once again, for instance, due to the improved earnings situations of many enterprises. This was accompanied by additional government grants to enterprises affected by the pandemic. Moreover, it is likely that some enterprises that were hit hard by the pandemic were already highly indebted, leading to a certain reluctance to take out new loans.

BLS banks saw an increase in demand for loans to enterprises ...

The bank managers surveyed as part of the BLS reported that demand for loans among non-financial corporations nonetheless rose marginally overall compared with the previous quarter; this was the second increase in succession. According to the survey, it was primarily large enterprises that required financing. The surveyed banks cited financing needs for inventories and working capital as a factor boosting demand again for the first time in 2021. Financing needs for fixed investment, which the BLS banks had reported as curbing demand for loans for several quarters, also contributed to the rise in demand, as in the previous quarter. However, a few bank managers noted that, viewed in isolation, supply constraints were dampening credit demand.

At the same time, the banks surveyed as part of the BLS kept credit standards for loans to enterprises essentially unchanged on balance, as in the quarter before. According to the responses from the surveyed banks, this was the result of contrasting factors. The general economic situation and the economic outlook were conducive to looser credit standards, as were the greater competitive pressure with other banks and the improved liquidity position of the banking industry. By contrast, sector-specific and firm-specific factors as well as a decline in borrowers' creditworthiness continued to have a restrictive effect.

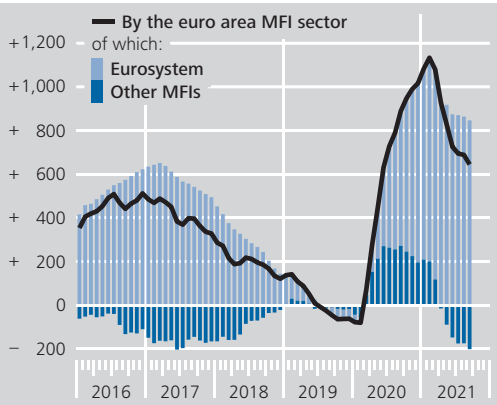
... and kept credit standards essentially unchanged

Loans to households showed further strong expansion in the third quarter of 2021. As with corporate loans, banks in Germany and France made the most significant contributions. A rather strong stimulus also came from Italy once again. Overall, net inflows to this segment are considerably higher than they were before the pandemic. These were predominantly driven by housing loans, which make up the most significant portion of loans to households. Their annual growth rate has increased steadily in recent years, standing at 5.5% at the end of September. The dynamic developments over the last few quarters should also be viewed against the backdrop of material shortages and other supply-side bottlenecks driving up prices for

Further sharp increase in housing loans to households ...

Securities-based lending to general government in the euro area

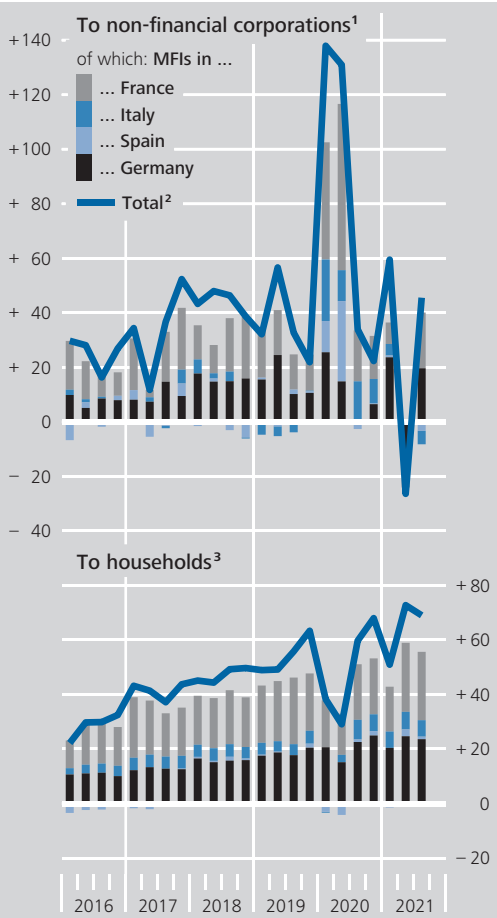
€ billion, 12-month accumulated flows



Sources: ECB and Bundesbank calculations.
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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.

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construction work, which, taken by itself, further increased the financing needs of households for house purchase.

Data from the BLS indicate the reasons behind the brisk demand for loans for house purchase. The banks surveyed repeatedly cited the low general interest rate level, the positive outlook on the residential real estate market and the renewed improvement in consumer confidence as key factors. On the supply side, banks participating in the BLS were revealed to be more cautious, tightening their standards for housing loans in the third quarter following slight relaxations in the preceding two quarters. The primary reasons named by banks were lower risk tolerance as well as higher costs of funds and balance sheet constraints. Some banks explicitly cited restrictive macroprudential policy.

... credit standards tightened according to BLS

Consumer loans to households increased perceptibly for the second quarter in succession. One of the reasons for this is likely to have been the lifting of coronavirus-related restrictions in the areas of transport, hospitality and culture. This was also accompanied by pandemic-related catch-up effects. Nevertheless, inflows in consumer credit remained far below their level prior to the outbreak of the pandemic. The banks responding to the BLS reported another moderate rise in demand for consumer and other loans. The main reasons they gave for this increase were improved consumer confidence and a greater propensity to purchase durable consumer goods. Furthermore, the banks surveyed as part of the BLS indicated that they had left their standards for consumer and other loans essentially unchanged, as they had in the preceding quarter.

Perceptible inflows in consumer credit as well

Unlike lending, the net external position of the MFI sector had a noticeable dampening influence on monetary growth in the third quarter of 2021. While the euro area's ongoing current account surplus resulted in inflows of funds as usual, this positive factor was offset by the negative balance in cross-border securities transactions according to the balance of pay-

Net external position with noticeable dampening effect on monetary growth due to negative balance in cross-border securities transactions

ments data available to date. The outflows in investment were attributable to the persistent differences in yield between bonds issued by other currency areas and those issued by the euro area. Against this backdrop, domestic non-banks continued to expand their holdings of foreign securities on balance, while non-residents sold bonds issued by domestic non-banks in net terms. Although they once again purchased larger volumes of shares and mutual fund shares issued in the euro area at the same time, this was, on the whole, far outweighed by the outflows of funds owing to bond transactions.

German banks' deposit and lending business with domestic customers

Accumulation of overnight deposits continues to dominate deposit growth

Despite interest rates falling deeper into negative territory in some cases, domestic customers increased their overnight deposits significantly again and continued to reduce all other deposits. Unlike in preceding quarters, the corporate sector recorded the highest inflows into overnight deposits in the current quarter.

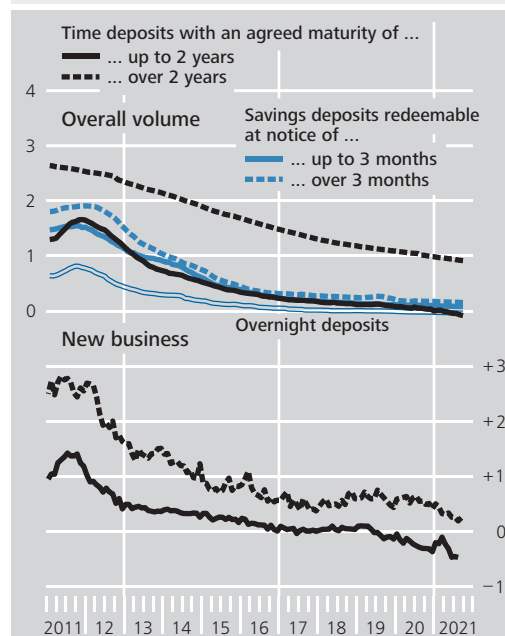
High propensity to consume dampening households' build-up of deposits

By contrast, domestic households built up their deposits to a limited extent in the third quarter of 2021. This development should be viewed against the background that the easing of pandemic-related restrictions has increased households' propensity to consume. Catch-up effects are likely to have played a role here as well. Furthermore, survey data indicate that some households purchased durable consumer goods earlier than planned in anticipation of further price increases.

Unlike households, non-financial corporations' accumulation of deposits in the third quarter of 2021 was again slightly above the pre-pandemic level. One reason for this is likely to have been the improved income situation of the sectors that were hit especially hard by the pandemic. Financial enterprises also expanded their overnight deposits to a greater extent in

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.

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the reporting quarter. It seems that the uncertainty surrounding the path of economic recovery has prompted enterprises in this sector to temporarily park their inflows of funds in overnight deposits. This decision was obviously encouraged by the fact that the interest rate disadvantage of overnight deposits compared to other types of bank deposits continues to be minor (see the chart above).

Compared with the previous quarter, banks' lending business with the domestic non-bank sector regained a considerable amount of momentum in the third quarter of 2021. This was mainly due to the sharp growth in lending to the domestic private sector. In addition, banks markedly increased their holdings of securities issued by the private sector once more, acquiring mainly shares and other variable-yield securities. By contrast, their lending to the public sector grew only marginally in net terms.

Credit business with non-banks regained momentum owing to loans to the private sector

MFI* lending and deposits in Germany

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

Item	2021	
	Q2	Q3
Deposits of domestic non-MFIs ¹		
Overnight	22.7	35.3
With an agreed maturity of up to 2 years	- 11.3	- 6.5
over 2 years	- 7.2	- 5.8
Redeemable at notice of up to 3 months	1.5	- 0.1
over 3 months	- 0.8	- 0.8
Lending		
to domestic general government		
Loans	0.7	- 0.7
Securities	- 13.1	1.7
to domestic enterprises and households		
Loans ²	14.8	38.8
of which: to households ³	24.6	23.5
to non-financial corporations ⁴	- 13.0	14.9
Securities	2.6	3.8

* 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.

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Continuing high demand for housing loans among households

In terms of lending to the private sector, loans to households once again recorded the largest net inflows. This was again primarily due to households' high demand for loans for house purchase, the growth rate of which initially picked up on the year and then stabilised at 7.2% towards the end of the third quarter. In addition to loans for house purchase, the current rise in loans to households was also attributable to consumer credit, which, unlike in the preceding three quarters, saw slightly positive growth again. Alongside the positive labour market and income situation, households' overall high demand for bank loans in the third quarter was encouraged by financing terms that remain exceptionally favourable. According to MFI interest rate statistics, the interest rate on long-term loans for house purchase was 1.3% at the end of the third quarter and thus only slightly above the historical low of 1.1% recorded at the end of December 2020.

The latest results of the BLS suggest that other factors were at play as well. The banks reported that the low general level of interest rates and improved consumer confidence as well as the good outlook for the residential real estate market and expected price developments were key factors driving the uptick in demand for housing loans. Another explanatory factor provided by the surveyed banks regarding the increase in demand for consumer credit was the increased propensity to purchase durable consumer goods.

Demand boosted by improved consumer confidence and good outlook, amongst other factors

Credit standards for loans to households for house purchase were tightened marginally in net terms in the third quarter. After easing lending standards in the previous quarter, the phase of tightening these standards that began at the outbreak of the coronavirus pandemic in Germany in the first quarter of 2020 resumed. One of the reasons for tightening these standards was an elevated level of credit risk according to banks' assessments. Another reason was that banks exhibited a lower tolerance of risk. The rejection rate rose slightly compared with the previous quarter. After the increases in the second, third and fourth quarters of 2020, this rate is likely to persist at an elevated level.

Standards for housing loans tightened slightly owing to elevated credit risk and lower risk tolerance

Credit terms and conditions were also tightened on balance, continuing the tightening that has been ongoing since the second quarter of 2019, with a brief interruption in the second quarter of 2021. This tightening was reflected solely in an expansion of margins irrespective of credit ratings, which banks justified on the basis of balance sheet constraints and lower competitive pressure.

Credit terms and conditions tightened irrespective of credit ratings

By contrast, standards for consumer and other loans to households were eased marginally by the surveyed banks in the third quarter of 2021.

In addition to lending to households, banks' lending business was also boosted by loans to non-financial corporations, which picked up substantially in comparison to the overall weak first half of the year. This was mainly a result of

Non-financial corporations exhibit high demand for credit ...

the continued recovery in economic activity in the third quarter, which was associated with an increase in financing needs, especially in domestically oriented sectors such as the construction and real estate sectors.

... across all maturities and driven by different demand motives

The current expansion covered all maturities. However, long-term loans recorded the most prominent gains. In addition to refinancing, restructuring and renegotiations, the banks surveyed in the BLS listed the funding of fixed investment as the key reason for the rise in demand. The latter funding is usually obtained through long-term loans. According to the BLS, other factors boosting demand stemmed from financial requirements for inventories and working capital, which non-financial corporations typically finance via short-term loans. The low general interest rate level also continued to boost demand. The MFI interest rate statistics show that, at the end of September, domestic enterprises paid interest amounting to 1.5% for small-volume loans and 1.1% for large-volume loans in the long-term segment, whilst interest rates on short-term loans most recently stood at 1.8% and 1.3%, respectively (see the chart on p. 40). By contrast, the results of the BLS suggest that enterprises' internal financing options, when viewed in isolation, had a dampening effect on demand.

Credit standards tightened only marginally in commercial banking

At the same time, the latest BLS results indicate that banks tightened their lending policies for corporate loans only marginally. Credit terms and conditions were not adjusted in their entirety in the third quarter. Banks marginally expanded their margins only for riskier loans and based this increase on lower competitive pressure.

German banks' funding environment somewhat improved ...

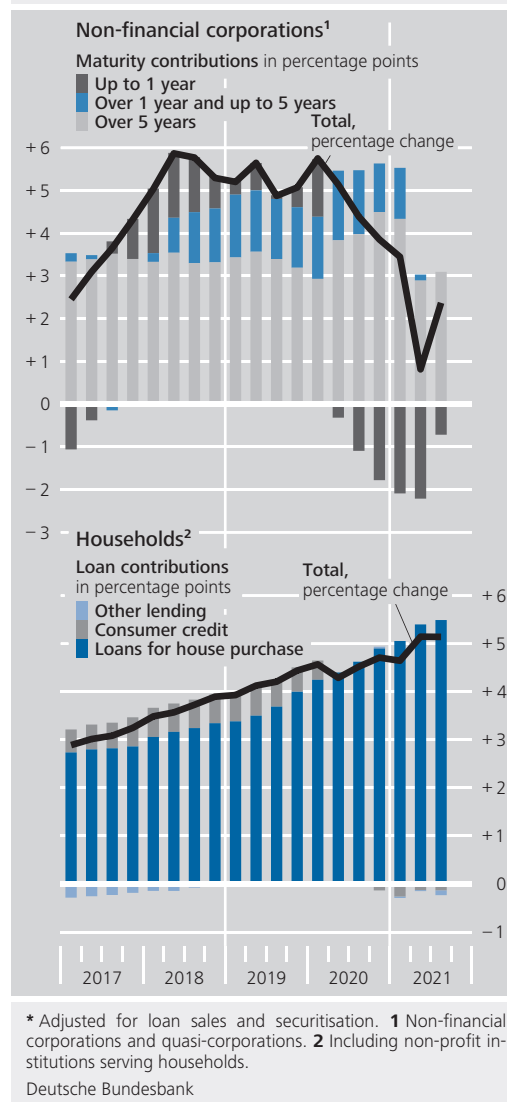
In response to the ad hoc questions in the October survey, German banks reported that their funding conditions had improved somewhat compared with the previous quarter.

... also helped by Eurosystem purchase programmes

According to the surveyed banks, the Eurosystem purchase programmes (APP, PEPP) have helped to improve the liquidity position of com-

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

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



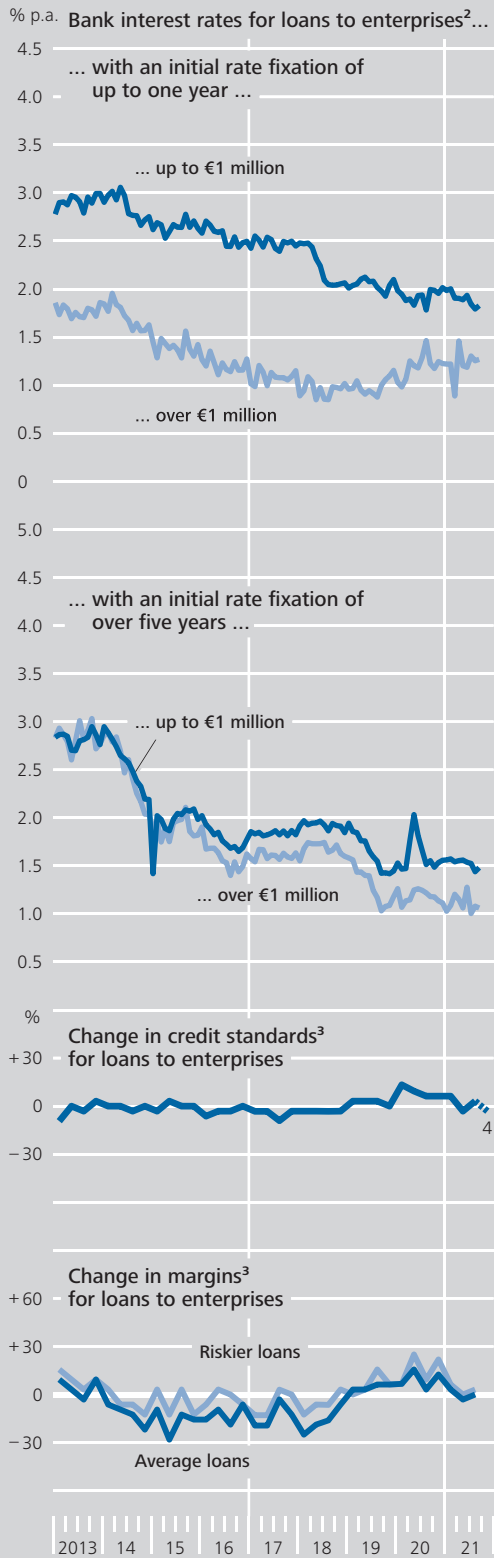
mercial banks and their market funding conditions over the past six months, but they were still having a negative impact on bank profitability through net interest income. The purchase programmes did not contribute to credit growth over the past six months.

Data from the BLS showed that the negative interest rate on the deposit facility depressed lending and deposit rates and also pushed up fees for deposits, squeezing banks' net interest income overall once again. The two-tier system for remunerating excess liquidity holdings did, however, soften the adverse impact on earnings.

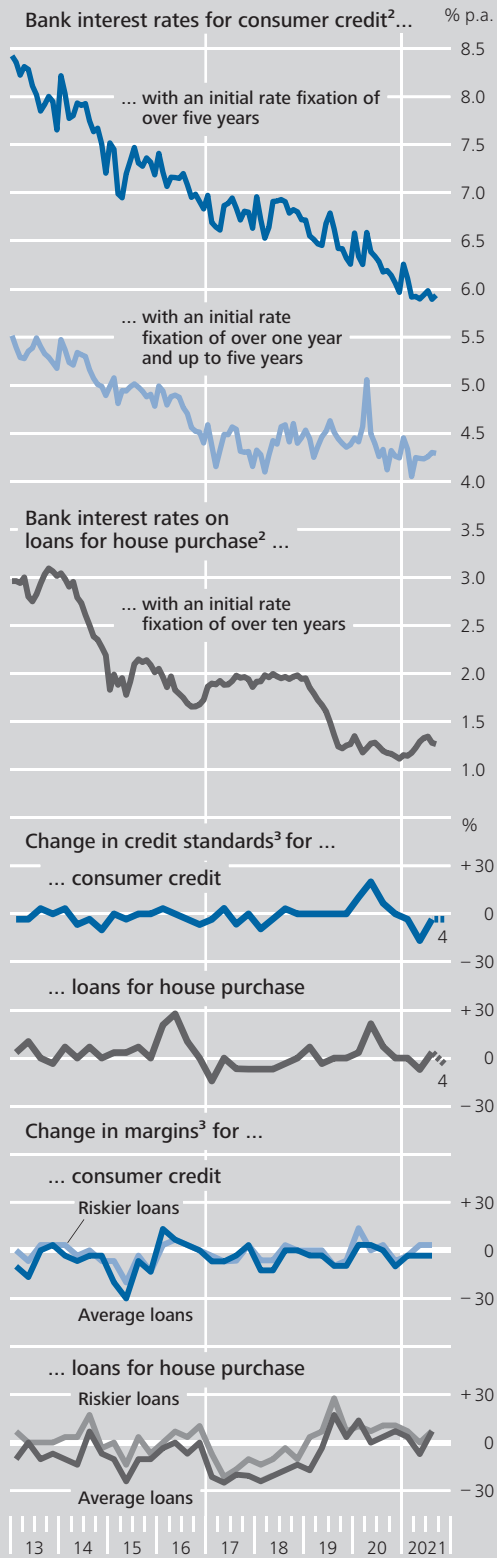
Two-tier system for excess liquidity softens adverse impact on profitability

Banking conditions in Germany

Credit to non-financial corporations



Credit to households¹



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 Q4 2021.

Use of TLTRO-III funds for lending, inter alia

Twelve banks from the German sample took part in the TLTRO-III operations in June, and eight in September 2021, mainly on account of the attractive conditions. Banks reported using the obtained funds primarily for lending and as a substitute for maturing debt securities and interbank loans. The surveyed banks would

participate in future TLTRO-III operations mainly due to the attractive conditions, provided that they had not yet reached their credit limits. The TLTRO-III operations caused banks to ease their lending policies and contributed to a rise in lending, particularly to enterprises.

■ List of references

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