

Eurozone: Money growth figures offer some relief

Monetary growth comes out better than expected, alleviating some of the recession fears. That said, some further ECB action is still quite likely in September



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Lower opportunity costs for holding money

After all the disappointing economic data recently, monetary dynamics of the eurozone came out stronger than expected in July. The annual growth rate M3 - the measure of monetary supply, accelerated to 5.2% in July 2019 from 4.5% in June and this was well above the consensus expectation of 4.7% growth. Of course, the strong decline of bond yields further reduced the opportunity costs of holding M3, supporting money growth. The annual growth rate of narrow monetary aggregate M1 also increased to 7.8% in July from 7.2% in June.

Looking at the counterparts of M3, there was a strong contribution from net external assets. This reflects an increased interest in the euro area from foreign investors, but as the ECB indicated itself in the Economic Bulletin, this factor tends to be volatile and may therefore not be durable.

Loan growth is keeping up...for now

The annual growth rate of adjusted loans to households slightly accelerated to 3.4% in July, compared with 3.3% in June, while the annual growth rate of adjusted loans to non-financial corporations stood at 3.9% in July, unchanged from the previous month. While loan growth is keeping up for now, we shouldn't forget that according to the euro area bank lending survey, credit standards for loans to enterprises recently tightened amid concerns about the economic outlook.

Taking away the sense of panic

The decent growth in monetary aggregates should take away the sense of panic. M1, which has been a good leading indicator in the past, still signals GDP growth close to 1% in 2020. That doesn't take away the fact that the economy remains vulnerable, warranting some further ECB action.

The big question is whether the ECB can still put together a package that will support growth and inflation since the adverse side-effects of the negative interest regime are becoming important. We still believe the ECB will announce a rate cut and a restart of QE in September, but at the same time, an important set of measures will have to be introduced to avoid the negative side-effects on the banking sector clog the credit channel. At the same time, the ball is now probably rather in the camp of fiscal policy to ward off potential recession risk.

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