The horse is drinking, albeit reluctantly

Loan growth, although still positive, is not accelerating in the Eurozone, while money growth slowed to 4.6% year-on-year. Not an indication that the ECB should start reducing monetary stimulus in the short run

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Broad money growth lower-than-expected

Growth in broad money (M3) in the Eurozone was lower than expected at 4.6% year-on-year in December, a deceleration from November's 4.9% growth pace. At the same time, the annual growth rate of adjusted loans to households was unchanged at 2.8%, while the growth rate of adjusted loans to non-financial corporations decreased to 2.9% in December, from 3.1% in November.

The question is whether this makes us any wiser in terms of the inflation and growth outlook. In the early years, the ECB's Governing Council attached quite some importance to M3-growth, with 4.5% being seen as compatible with the ECB's inflation objective. However, because of the many potential distortions, this emphasis on money growth was later abandoned and the analysis of monetary developments became just one of the means to "cross-check" the outcome of the economic analysis in a medium to longer-term perspective.

Today, money growth is without any doubt influenced by portfolio shifts, with the low opportunity cost of holding the most liquid instruments in an environment of very low interest rates responsible for the still strong increase in M1 (+8.6% year-on-year). Of course, the continuing bond buying by the ECB is also shifting savings to shorter maturities. The velocity of money has therefore fallen dramatically over the last couple of years, which makes it hard to claim that inflation is going to converge rapidly towards the (below, but close to) 2% target, on the back of the current money growth figures. If anything, the slowdown of money growth points in the other direction.

Since 2003 the role of monetary aggregates has become slightly less important in the ECB's analysis

Monetary policy pass-through

That said, today's figures at least suggest that the ECB's monetary strategy is supporting growth. This is reflected in the evolution of credit growth. Even though it is not accelerating, there is indeed some pass-through of the monetary policy measures put in place since June 2014. The January Bank Lending Survey showed that credit standards remained broadly unchanged for enterprises and consumer credit, while they continued to ease for housing loans. At the same time, credit terms and conditions eased further for loans to enterprises and housing loans. We therefore still expect that credit growth will continue its recovery, helped by both generous financing conditions and loose credit standards, with the historically high business confidence underpinning investment growth.

Central bankers sometimes complain that creating favourable financing conditions isn't enough to foster a recovery. Just as you can lead a horse to the water, but cannot make it drink. Judging by the latest credit figures, the Eurozone horse seems to be drinking, albeit somewhat reluctantly. Today's figures don't give the ECB any reason to contemplate a change in its monetary policy in the short run.

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