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EUROZONE: Even clearer monetary weakness?

More signs of credit crunch?

Coming in below expectations even more clearly this time around, December M3 money supply growth slowed by 0.4 percentage point to 1.6% Y/Y, thereby easing back to an 11-month low. This came on the back of a 0.5% M/M decline in adjusted M3, actually a third successive drop. In addition, the narrower money supply gauge (M1) saw its Y/Y growth rate weaken afresh to 1.6% (from 2.1%).

Weaker lending even clearer

More worrisome was the softer private sector lending growth picture (in adjusted terms). Indeed, the headline pace of growth slumped a further 0.7 percentage point to 1.2%, an 18-month low and a starker contrast to the cycle-high of 3.0% set in October. Furthermore, the weakness this time was little to do with base effects, instead being a reflection of a second and more sizeable M/M drop (the 0.7% fall actually being the steepest on record). Notably, the lending breakdown showed this weakness to be increasingly broad-based. Indeed, underlying Y/Y corporate lending growth slowed clearly to 1.2%. This came alongside a further fall in underlying household loans growth, down 0.4 percentage point to 1.9%, with broad based weakness across all sub-sectors.

Evidence of fragile banking sector

A familiar, but perhaps mote manifest, theme of fragility is evident in these numbers, the latter very much indicative of the on-going problems facing the Eurozone banking system that have become only too apparent in the last few months. Indeed, continued M3 weakness (down 4.5% annualized in the last three months) reflected not just sharp falls in repo activity but broader signs of fragility all very much consistent with financial market turmoil distortions as the root cause. Regardless, M3 growth is still very much negative in real terms as is that for M1. Indeed, the deeper weakness in M1 growth also corroborates the picture of a weak, if not, slowing economy evident in the business and consumer surveys as it is this aggregate which seems to be better than the broader M3 numbers in tracking the economy.

Perhaps more emphasis should be placed on the still increasingly soft private sector lending data, where the likes of the steeper M/M drop in consumer credit provide corroboration of the weaker consumer spending signals now being seen increasingly across the whole of the Eurozone. The question is the extent to which the softer consumer and company lending backdrop may be a reflection of a building credit crunch, a development that is being accentuated by financial market turmoil but which is manifesting itself ever-more adversely on real economic activity. Admittedly, this latest monetary data does not provide irrefutable evidence of a credit crunch, but clearly neither does it refute such a conclusion. Crucially, the ECB, under the direction of President Draghi, does seem to be more open to admitting such credit constraints risks, albeit so far willing to admit that no significant such effects are apparent. It will be interesting to see if the ECB Bank Lending Survey (due next Wednesday) provides more signs that the softening in credit is as much due to supply factors as demand

ECB will want more up-to-date numbers

All of which is crucial to markets looking for the ECB to step up its bond purchase. Especially as the ECB has explained that its existing bond purchase program is designed to ensure that the monetary policy transmission mechanism continues to work, clearer signs from this data that the latter may be in a deepening state of disrepair surely argue for possibly more sizeable bond purchases. However, from the ECB perspective, the weakness in December monetary data may be of no great surprise, with hints of such softness possibly being the rationale for the alternative policy-course that the ECB chose, namely the extraordinary large and long-term lending that the ECB provided via the € 490 bln 3-year loans it provided just before Xmas. Given that this liquidity injection has seemingly had some clear successes in shoring up banks in the last month, the ECB may want more data pertaining to January and beyond before the Council accepts that a credit crunch is biting more sizeable and durably.