

## Box I

### Financing and financial investment of the non-financial sectors in the euro area up to the third quarter of 2001

The release of quarterly financial accounts for the non-financial sectors in the euro area for the second and third quarters of 2001 allows the financing and financial investment decisions of these sectors to be analysed. With this release, the publication time-lag for quarterly financial account data is reduced to slightly more than four months. This makes it possible to conduct a more timely analysis of developments in financing and financial investment, and hence to put recent monetary and financial market developments into a broader perspective. An overview of the financing and financial investment decisions of the non-financial sectors is presented in Tables A and B. For more details, see Table 6.1 in the "Euro area statistics" section of this issue of the Monthly Bulletin.

**Table A: Financial investment of non-financial sectors in the euro area <sup>1)</sup>**

	Financial investment										Memo item: M3
	Currency, deposits and short-term marketable instruments	Currency and deposits <sup>3)</sup>	Short-term securities other than shares	Money market fund shares	Long-term marketable instruments and insurance technical reserves	Long-term securities other than shares	Quoted shares	Mutual fund shares other than money market fund shares	Insurance technical reserves		
<b>Annual growth rates (end of period)<sup>2)</sup></b>											
1998	5.6	1.8	3.2	-22.8	-4.3	8.6	-5.1	6.3	31.2	8.7	4.9
1999	6.0	2.7	2.8	-5.8	7.4	8.2	1.9	7.2	13.6	9.4	5.5
2000 Q1	4.9	3.7	3.3	6.8	11.1	5.7	-2.4	4.2	8.3	9.7	5.5
Q2	5.1	3.5	3.4	15.7	-2.3	6.1	3.4	4.0	5.2	9.6	5.5
Q3	6.0	3.8	3.1	40.4	-3.0	7.4	6.3	8.5	3.1	9.3	4.5
Q4	6.8	3.1	2.9	18.4	-1.7	8.9	4.2	12.8	7.0	8.6	4.2
2001 Q1	8.0	4.6	3.2	50.1	4.5	9.9	9.7	14.5	6.7	7.4	3.9
Q2	7.6	5.0	4.1	35.5	6.0	9.0	8.0	13.7	5.7	7.0	4.3
Q3	6.6	5.6	4.7	25.0	12.0	7.1	7.4	8.1	6.1	6.5	6.0
<b>Ratio to total financial investment as at 2001 Q3 (amounts outstanding)</b>	100%	39%	36%	1%	2%	61%	11%	16%	10%	23%	37%

Source: ECB.

- 1) Non-financial sectors comprise general government, non-financial corporations and households including non-profit institutions serving households.
- 2) Growth rates of financial investment are based on non-seasonally adjusted transactions and therefore do not include valuation effects and reclassifications. The growth rate of M3 is a quarterly average annual growth rate adjusted for seasonal and calendar effects.
- 3) Excluding central government deposits with MFIs.

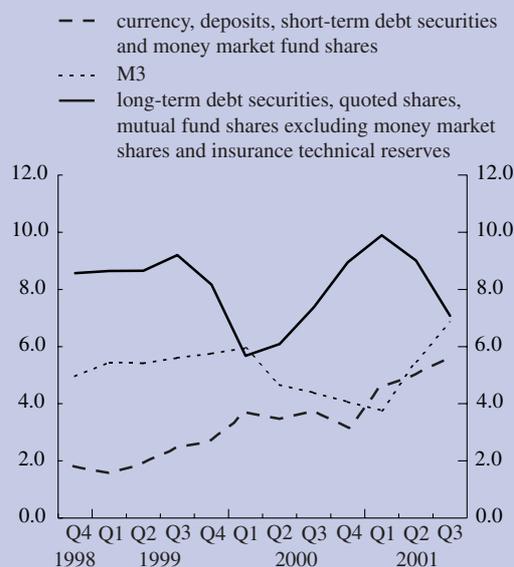
#### Financial investment –evidence of portfolio reallocations towards shorter-term financial instruments

The annual rate of growth of financial investment by the euro area non-financial sectors (excluding central government deposits with MFIs) declined to 6.6% in the third quarter of 2001, from 7.6% in the second quarter (see Table A). The decline in the annual rate of growth of financial investment was due entirely to a weakening in the annual growth of investment in longer-term financial assets (i.e. long-term debt securities, mutual fund shares excluding money market fund shares, quoted shares and insurance technical reserves) to 7.1% in the third quarter of 2001, down from a peak of 9.9% in the first quarter (see Chart A). Of the total annual (i.e. four-quarter flow) financial investment by the euro area non-financial sectors in the third quarter of 2001, around 70% was long-term investment, compared with 78% in the first quarter.

The pronounced decrease in the annual rate of growth of investment in longer-term financial assets resulted predominantly from lower investment in quoted shares. The annual rate of growth of investment by the non-financial sectors in quoted shares fell to 8.1% in the third quarter of 2001, from 13.7% in the second

**Chart A: Short-term and long-term financial investment of the non-financial sectors in the euro area**

(annual growth rates in percentages)



Source: ECB.

Note: Excluding central government deposits with MFIs. M3 refers to holdings of the non-MFI sector with euro area MFIs.

increased in the course of 2001, broadly in line with that of the monetary aggregate M3. This increased liquidity preference on the part of investors was probably related to a relatively flat yield curve up to August, the persistent decline in stock prices and the surge in financial market uncertainty following the events of 11 September. The financial account data thus support the assessment that the rise in M3 growth in the course of 2001 was driven to a significant extent by portfolio reallocations in favour of short-term financial instruments.

**Financing –changes in the maturity structure**

In the third quarter of 2001, the annual growth rate of financing of the euro area non-financial sectors decreased to 5.5%, from 6.1% in the second quarter (see Table B). Developments differed significantly across sectors, however. The annual rate of growth of financing of non-financial corporations fell to 7.1%, from 8.5% in the second quarter. The annual rate of growth of financing of households decreased to 5.8%, from 6.2% in the second quarter. The decline in both rates took place in an environment characterised by weakening economic activity and the fading away of a number of special factors, such as the strong merger and acquisition activity and the booming real estate markets in some euro area countries in 1999 and 2000. In contrast to the developments in the non-financial private sectors, the annual rate of growth of financing of general government increased to 2.5% in the third quarter of 2001, from 2.0% in the second quarter and 1.5% in the first. General government financing needs rose after the fading of the impact of the one-off UMTS revenues in autumn 2000 and as a result of the slowdown in euro area economic activity, which led to a rather subdued increase in general government taxes and social contributions accompanied by broadly stable growth of social benefits and government consumption.

An analysis of how the maturity structure of financing has developed may contain information about cyclical and structural changes in the financing behaviour of households, non-financial corporations and general

1 A breakdown of the investment of the euro area non-financial sectors into short-term and long-term deposits is not available so far.

quarter. This may be related to investors having experienced substantial capital losses owing to almost continuously falling stock prices between March 2000 and the third quarter of 2001; it also resulted from a decrease in merger and acquisition transactions by euro area corporations during 2001 after the exceptionally high level in 2000. The global economic slowdown and the decline in business confidence contributed to the weakening of merger and acquisition activity.

The fall in the annual rate of growth of financial investment was also, to some extent, due to lower investment in the so-called insurance technical reserves (mainly life insurance and pension fund reserves) and debt securities. The annual rate of growth of investment in mutual fund shares excluding money market fund shares (i.e. equity and bond-related mutual fund shares) remained at a level similar to that recorded in previous quarters.

By contrast, the annual rate of growth of shorter-term financial investment (i.e. currency, deposits,<sup>1</sup> money market fund shares and short-term debt securities)

**Table B: Financing of non-financial sectors in the euro area <sup>1)</sup>**

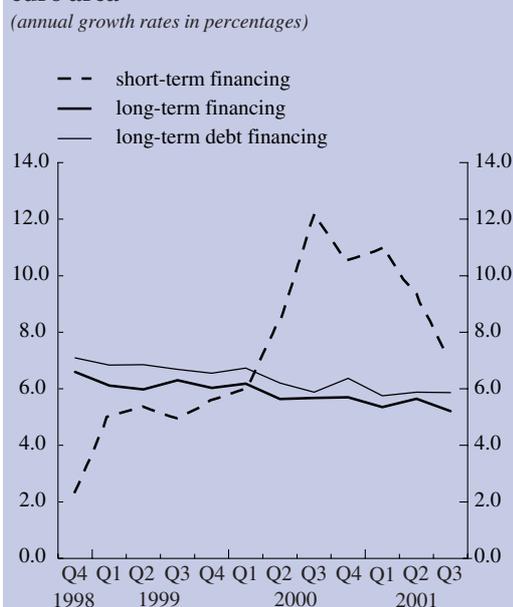
	Financing												
	Financing of general government						Financing of non-financial corporations					Financing of households <sup>3)</sup>	
	Loans	Taken from euro area MFIs		Securities other than shares	Held by euro area MFIs	Loans	Taken from euro area MFIs		Securities other than shares	Quoted shares	Loans taken from euro area MFIs <sup>3)</sup>		
<b>Annual growth rates (end of period)<sup>2)</sup></b>													
1998	6.0	3.1	-1.1	-0.4	4.3	3.2	7.0	8.8	8.5	8.6	5.0	8.9	9.1
1999	6.0	2.5	-1.2	0.4	3.3	2.4	6.7	8.2	7.0	13.8	4.6	10.3	10.7
2000 Q1	6.2	2.1	-1.4	0.0	3.1	-0.9	7.7	11.0	9.4	10.7	4.7	9.6	9.7
Q2	6.0	2.2	-1.6	-0.3	2.9	-4.6	7.7	11.4	9.3	12.2	4.2	8.6	8.7
Q3	6.6	1.9	-1.8	-1.2	2.6	-7.9	9.4	14.1	11.1	13.7	5.3	7.8	8.0
Q4	6.3	1.8	-1.4	-0.9	2.6	-10.6	8.7	14.4	10.9	16.0	4.4	7.3	7.4
2001 Q1	6.1	1.5	-1.1	-0.4	2.0	-11.9	8.6	13.2	10.0	24.6	4.7	6.4	6.6
Q2	6.1	2.0	-2.4	-1.8	3.0	-4.0	8.5	11.1	9.0	26.9	5.3	6.2	6.3
Q3	5.5	2.5	-1.4	-0.7	3.3	-1.6	7.1	9.5	7.4	23.8	3.8	5.8	6.0
<b>Ratio to total financing as at 2001 Q3 (amounts outstanding)</b>	100%	32%	6%	5%	26%	8%	46%	23%	19%	3%	18%	22%	20%

Source: ECB.

- 1) Non-financial sectors comprise general government, non-financial corporations and households including non-profit institutions serving households. Financing consists of loans, securities other than shares, quoted shares, pension fund reserves of non-financial corporations and deposit liabilities of central government.
- 2) Quarterly average annual growth rates are based on non-seasonally adjusted transactions and therefore do not include valuation effects and reclassifications.
- 3) Including non-profit institutions serving households.

government. The quarterly financial accounts for the euro area allow such an analysis, as they provide a split into short-term and long-term financing. The split between short-term and long-term financing is based on original maturities of up to one year and over one year.

**Chart B: Short-term and long-term financing of the non-financial sectors in the euro area**  
(annual growth rates in percentages)



Source: ECB.

Notes: Short-term financing consists of short-term loans and debt securities issued as well as government deposits; long-term financing consists of long-term loans and debt securities issued as well as quoted shares and pension fund reserves of non-financial corporations; debt financing consists of loans and debt securities issued.

As can be seen from Chart B, the annual rate of growth of financing of the euro area non-financial sectors via short-term financial instruments (short-term loans, short-term debt securities and deposit liabilities of central government) fell considerably, from 12.1% in the third quarter of 2000 to 7.0% in the third quarter of 2001. By contrast, the annual rate of growth of long-term financing (long-term loans, long-term debt securities, quoted shares and pension fund reserves) remained relatively stable, at 5.2% in the third quarter of 2001.

On average since the fourth quarter of 1997, 86% of the liabilities of the euro area non-financial sectors (loans, debt securities, quoted shares and pension fund reserves) were long-term. Broadly in line with this, between the fourth quarter of 2000 and the third quarter of 2001, 82% of the total financing of the non-financial sectors was raised through long-term instruments. In the four quarters up to the third quarter of 2000, by contrast, long-term financing accounted for only 75% of the total annual financing of the non-financial sectors. The fall in the annual rate of growth of short-term financing of the euro area non-financial sectors thus represents, to some extent, a return of the maturity structure to a ratio more in line with the past.

The overall financing development of the euro area non-financial sectors mainly reflects changes in the maturity structure of the financing of non-financial corporations. The annual growth rate of short-term financing of non-financial corporations dropped from a peak of 21.5% in the third quarter of 2000 to 9.0% in the third quarter of 2001. In the third quarter of 2001, short-term financing accounted for 20% of the total annual financing of non-financial corporations, in line with the ratio of short-term liabilities to total liabilities of non-financial corporations. In the third quarter of 2000, the corresponding figure had been 37%. This development presumably partly reflects the redemption by non-financial corporations of short-term bridge loans taken out earlier to finance mergers and acquisitions as well as the purchase of UMTS licences in the autumn of 2000 before switching in part to financing via the issuance of debt securities. Accordingly, the annual rate of change in financing via short-term loans declined continuously from the third quarter of 2000 until the third quarter of 2001.

By contrast, the annual rate of growth of long-term financing of non-financial corporations decreased less markedly, to 6.7% in the third quarter of 2001 from 7.5% in the second quarter. Partly as a result of the refinancing of short-term loans, long-term debt financing (long-term loans and long-term debt securities) remained relatively stable despite the slowdown in real economic activity. The annual growth in financing via the issuance of quoted shares, however, fell to 3.8% in the third quarter of 2001, from 5.3% in the second quarter. This decline is probably related to the fall in stock prices during 2001, which meant that financing via quoted shares became comparatively more expensive for corporations. In addition, lower merger and acquisition activity in the course of 2001 reduced the total financing needs of non-financial corporations. Overall, financing via debt securities gained further momentum in relation to other financing sources, accounting for 17% of the total annual financing of non-financial corporations at the end of the third quarter of 2001, though only about 7% of the amounts outstanding of financing instruments used by euro area non-financial corporations.

As regards the household sector, the annual rates of growth of both short-term and long-term loans continued to fall up to the third quarter of 2001, following the trend since 1999. The bulk of household debt (91% on average between the fourth quarter of 1997 and the third quarter of 2001) consists of long-term loans, mainly loans for house purchase. The decline in the annual growth rate of long-term loans is thus likely to be related to the slowdown in previously booming real estate markets in some euro area countries. The fall in lending rates for house purchase in the course of 2001 may, however, have prevented a steeper decline. The more pronounced decrease in the annual rate of growth of short-term loans, accounting for just 9% of total household debt and consisting to a considerable extent of consumer credit, is likely to reflect the adjustment of households to the slowdown in economic activity in the euro area. In addition, the decline in the retail interest rates for consumer credit was limited up to the third quarter of 2001, which might also explain the significant fall in short-term lending to households.

In contrast to the overall development of the financing of non-financial sectors and in particular to that of non-financial corporations, the annual rate of growth of short-term financing of general government increased considerably in the course of 2001, to 6.0% in the third quarter. Around two-thirds of the annual short-term financing of general government (short-term loans, short-term debt securities and deposit liabilities of central government) resulted from the issuance of short-term debt securities. Although the share of short-term debt in total general government debt was only 13% at the end of the third quarter of 2001, 32% of the total annual financing of general government at the end of the third quarter resulted from short-term financial instruments. Consequently, after a decline in recent years, the share of short-term debt in total general government debt increased slightly during 2001.

At the same time, the annual rate of change in longer-term general government financing rose only slightly in the course of 2001. While the demand of general government for long-term loans continued to decline up to the third quarter, it increased its issuance of longer-term debt securities during the year.