

Box I

Financing and financial investment of the non-financial sectors in the euro area up to the end of 2001

The release of quarterly financial accounts for the non-financial sectors in the euro area for the fourth quarter of 2001 makes it possible to analyse the financing and financial investment decisions of these sectors up to the end of 2001. An overview of the developments is presented in Tables A and B. For more details, see Table 6.1 of the "Euro area statistics" section of this issue of the Monthly Bulletin.

Overall, these data show a reduction in the annual growth rate of financing and financial investment of the non-financial sector in the fourth quarter of 2001, in line with the weak economic growth recorded at the time. The decrease in the annual growth of financing, to 4.7% in the fourth quarter of 2001, followed a period of relatively high and stable growth rates of around 6% between 1998 and the second quarter of 2001 (see Table A). In particular, the annual growth rate of short-term debt financing by non-financial corporations, which had been boosted by mergers and acquisitions as well as economic activity in 2000, declined substantially. The annual rate of growth of the issuance of quoted shares also went down significantly in the second half of 2001. Households reduced their short-term loans on a year-on-year basis, while the growth of long-term loans receded only moderately. Regarding financial investment of the euro area non-financial sectors, the annual rate of growth came down from a peak of nearly 8% in the first quarter of 2001 to 5.4% in the fourth quarter of 2001 (see Table B). Economic agents exhibited a marked preference for investment in liquid assets over equity in an environment of financial market uncertainty and concerns over corporate earnings and accounting practices. Significant holding losses over the past two years might also have contributed to such more cautious investment behaviour.

Table A: Financing of the non-financial sectors in the euro area ¹⁾

| | Financing | | | | | | | | | | | | |
|---|---------------------------------|-----|------------------------------|------|------------------------|-------|---|------|------------------------------|---------------|-----|---|------|
| | Financing of general government | | | | | | Financing of non-financial corporations | | | | | Financing of households ³⁾ | |
| | Loans | | Securities other than shares | | Held by euro area MFIs | | Loans | | Securities other than shares | Quoted shares | | Loans taken from euro area MFIs ³⁾ | |
| | | | Taken from euro area MFIs | | | | Taken from euro area MFIs | | | | | | |
| Annual growth rates (end of period) ²⁾ | | | | | | | | | | | | | |
| 1998 Q4 | 6.0 | 3.2 | -1.2 | -0.4 | 4.4 | 3.2 | 7.1 | 9.0 | 8.5 | 8.5 | 4.9 | 8.9 | 9.1 |
| 1999 Q4 | 6.0 | 2.3 | -1.2 | 0.4 | 3.0 | 2.4 | 6.8 | 8.3 | 7.0 | 14.3 | 4.7 | 10.7 | 10.7 |
| 2000 Q4 | 6.3 | 1.8 | -1.5 | -0.9 | 2.6 | -10.6 | 8.9 | 15.0 | 10.9 | 15.6 | 4.2 | 7.2 | 7.4 |
| 2001 Q1 | 6.1 | 1.5 | -1.1 | -0.4 | 2.0 | -11.9 | 8.7 | 13.4 | 10.1 | 25.2 | 4.6 | 6.3 | 6.5 |
| Q2 | 6.2 | 2.0 | -2.3 | -1.8 | 3.0 | -4.0 | 8.6 | 11.3 | 9.0 | 27.4 | 5.3 | 6.2 | 6.2 |
| Q3 | 5.5 | 2.4 | -1.2 | -0.7 | 3.1 | -1.6 | 7.2 | 9.5 | 7.5 | 24.7 | 4.1 | 5.7 | 5.9 |
| Q4 | 4.7 | 2.5 | -1.3 | -1.0 | 3.3 | 1.0 | 5.7 | 6.7 | 6.2 | 23.8 | 3.1 | 5.6 | 5.4 |
| Contribution to total annual financing (four-quarter flows) | | | | | | | | | | | | | |
| 1998 Q4 | 100% | 20% | -2% | 0% | 21% | 5% | 49% | 30% | 25% | 4% | 14% | 31% | 29% |
| 1999 Q4 | 100% | 13% | -1% | 0% | 14% | 4% | 50% | 27% | 20% | 6% | 16% | 37% | 33% |
| 2000 Q4 | 100% | 9% | -1% | -1% | 10% | -14% | 69% | 44% | 28% | 6% | 18% | 23% | 21% |
| 2001 Q4 | 100% | 16% | -2% | -1% | 16% | 2% | 60% | 29% | 23% | 14% | 16% | 24% | 21% |
| Ratio to total financial liabilities as at Q4 2001 (amounts outstanding) | | | | | | | | | | | | | |
| | 100% | 31% | 6% | 5% | 25% | 7% | 48% | 22% | 18% | 3% | 21% | 21% | 20% |

Source: ECB.

- 1) The 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.

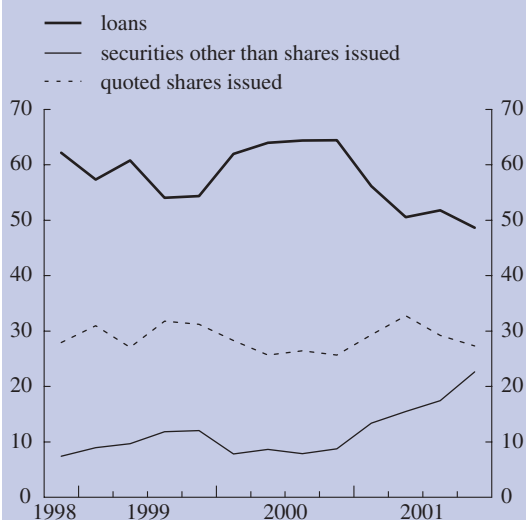
Financing of the non-financial sectors

For non-financial corporations, the annual growth of financing continued to fall in the fourth quarter of 2001, to 5.7%, from 7.2% in the third quarter. This sizeable decline was mainly related to the drop in the annual growth of loans, which declined to 6.7%, from 9.5% in the previous quarter. This reflects cyclical developments as well as a base effect, as the exceptionally high extension of loans in the fourth quarter of 2000, partly taken up for the financing of mergers and acquisitions and the UMTS licences, dropped from the calculation of the annual growth rate. The annual rate of growth of short-term loans (i.e. loans with an original maturity of up to one year) taken up by non-financial corporations decreased sharply to 2.2% in the fourth quarter of 2001, from 5.5% in the third quarter, while the annual rate of growth of long-term loans (i.e. loans with an original maturity of over one year) taken up by non-financial corporations fell to 9.3% in the fourth quarter of 2001, from 11.8% in the third quarter.

Issuance of quoted shares also contributed to slower growth in the financing of non-financial corporations. The annual growth of quoted shares issued fell to 3.1% in the fourth quarter of 2001, which was the lowest since the start of 1999. By contrast, the annual rate of growth of debt securities issued by non-financial corporations remained at a high level in the fourth quarter of 2001 (23.8%). In particular, the annual growth of long-term debt securities issued by non-financial corporations increased in the fourth quarter of 2001, to 20.5%, from 18.9% in the third quarter, in part probably reflecting a substitution of previous bridging loans taken up in the context of the financing of mergers and acquisitions and the UMTS licences. The annual growth of short-term debt securities issued by non-financial corporations also remained high in the fourth quarter of 2001 (34.5%), despite declining from 43.0% in the third quarter.

Chart A: Financing of non-financial corporations in the euro area

(share in annual financing of non-financial corporations, in percentages)



Source: ECB.

Note: Annual financing is defined as the sum of the four-quarter flows. Financing includes loans, securities other than shares, quoted shares and pension fund reserves of non-financial corporations.

Debt securities form a small part of total liabilities of non-financial corporations (only 6.9% at the end of 2001, compared with a share of loans of 46.1%). However, the annual financing (i.e. the sum of the four-quarter flows) of non-financial corporations via debt securities amounted to 22.6% of their total financing in 2001, compared with 8.7% in 2000 (see Chart A). By contrast, the share of annual financing via loans was 48.7%, compared with 64.5% in 2000. Quoted shares decreased only moderately as a proportion of total annual financing by non-financial corporations, to 27.3% in 2001. This mainly reflected the high issuance in the first half of the year, while issuance was exceptionally low in the second half. For 2001 as a whole, it was thus only slightly below its average proportion in total annual financing of non-financial corporations between 1998 and 2001 (28.7%). A noticeable feature observed over the past few years has been the continuously stronger growth of loans granted by financial intermediaries other than MFIs as compared with MFI loans. However, these diverging paths narrowed significantly in the last quarter of 2001.

The annual growth of loans extended by MFIs and other financial institutions to the household sector declined further in the fourth quarter of 2001 (to 5.6%). Since the third quarter of 1999, the rate of annual growth has declined uninterruptedly. Households even reduced their short-term loans, which mainly serve consumption

purposes, in the fourth quarter of 2001 (-0.5%). By contrast, the annual growth of long-term loans, which accounted for 91.6% of the amount outstanding of loans to households in the fourth quarter of 2001 and which are to a large extent loans for house purchase, remained stable compared with the previous quarter (6.2%). While the sharp decline of the annual rate of growth of short-term loans to households is largely linked to the weakening of economic activity in 2001, the developments in long-term loans reflect partly the decline in lending rates for house purchase in the course of 2001 and relatively steady housing markets in the euro area.

While loans to general government continued to decrease in the fourth quarter of 2001 (-1.3%), the annual growth of debt securities issued by general government increased further, to 3.3%. With regard to the maturity structure of financing, the annual growth of short-term financing of general government increased considerably in the fourth quarter of 2001 (to 8.1%), whereas the annual growth of long-term financing remained relatively low (1.7%). This reflects the increased financing needs of general government in the context of weak economic activity in 2001 and, presumably, a response to the steepening yield curve. The proportion of the outstanding amount of short-term debt of general government in total general government debt thus increased slightly to 13.1% at the end of 2001, from 12.7% one year earlier.

Financial investment of the non-financial sectors

The annual growth of financial investment of the euro area non-financial sectors continued to decrease in the fourth quarter of 2001, to 5.4%, from 6.8% in the third quarter (see Table B). Overall, there was a strong preference for liquid financial assets (except currency which was adversely affected by the cash changeover)

Table B: Financial investment of the non-financial sectors in the euro area¹⁾

| | Financial investment | | | | | | | | | | Memo item: M3 |
|---|--|-------------------------------------|---|--------------------------|---|--|---------------|--|------------------------------|-----|------------------|
| | Currency, deposits and short-term marketable instruments | Currency and deposits ³⁾ | 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 | | |
| Annual growth rates (end of period)²⁾ | | | | | | | | | | | |
| 1998 Q4 | 5.6 | 1.8 | 3.2 | -24.0 | -4.3 | 8.6 | -5.0 | 6.1 | 31.3 | 8.7 | 4.9 |
| 1999 Q4 | 5.9 | 2.5 | 2.8 | -10.1 | 7.3 | 8.2 | 2.5 | 7.2 | 13.5 | 9.4 | 5.6 |
| 2000 Q4 | 6.8 | 3.3 | 2.9 | 23.2 | -1.2 | 8.8 | 6.3 | 11.3 | 7.1 | 8.4 | 4.2 |
| 2001 Q1 | 7.8 | 4.8 | 3.2 | 56.3 | 4.3 | 9.5 | 10.8 | 13.3 | 5.4 | 7.5 | 3.8 |
| Q2 | 7.7 | 5.5 | 4.0 | 41.6 | 12.1 | 8.9 | 9.8 | 13.2 | 3.7 | 7.4 | 4.4 |
| Q3 | 6.8 | 6.3 | 4.7 | 30.0 | 22.7 | 7.0 | 7.7 | 8.7 | 3.3 | 7.1 | 6.0 |
| Q4 | 5.4 | 6.5 | 5.0 | 20.5 | 28.6 | 4.8 | 7.4 | 2.1 | 2.2 | 7.4 | 7.6 |
| Contribution to total annual financial investment (four-quarter flows) | | | | | | | | | | | |
| 1998 Q4 | 100% | 14% | 23% | -8% | -1% | 86% | -11% | 15% | 49% | 33% | 3% |
| 1999 Q4 | 100% | 17% | 18% | -2% | 2% | 83% | 5% | 20% | 25% | 34% | 3% |
| 2000 Q4 | 100% | 18% | 15% | 4% | 0% | 82% | 10% | 34% | 12% | 26% | 2% |
| 2001 Q4 | 100% | 43% | 31% | 5% | 7% | 57% | 15% | 8% | 5% | 30% | 5% |
| Ratio to total financial assets as at Q4 2001 (amounts outstanding) | | | | | | | | | | | |
| | 100% | 38% | 35% | 1% | 2% | 62% | 11% | 18% | 11% | 23% | 36% |

Source: ECB.

- 1) The 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.

and a declining demand for quoted shares, in both cases clearly related to the uncertainty prevailing in financial markets following the terrorist attacks in the United States on 11 September 2001. These developments support the assessment of a temporary strengthening of M3 growth as a result of considerable portfolio shifts at that time.¹

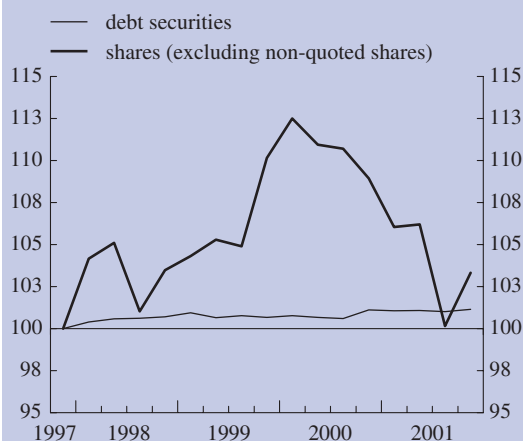
Overnight deposits and deposits redeemable at notice expanded strongly. In addition, the annual rate of growth of investment by the non-financial sectors in money market fund shares increased further, to 28.6% in the fourth quarter of 2001.

By contrast, the annual rate of growth of investment in quoted shares declined sharply to 2.1% in the fourth quarter of 2001, from 8.7% in the third quarter, partly owing to a base effect. Non-financial sectors even disinvested in quoted shares in the fourth quarter of 2001, reflecting a clear preference for short-term liquid assets. Investors' concerns with regard to prospects for corporate earnings and uncertainty about accounting practices have probably played a role. The annual growth of investment in mutual fund shares excluding money market fund shares also decreased in the fourth quarter of 2001, to 2.2%, from 3.3% in the third

quarter. The decline in the valuation of shares over the last two years (despite some recovery in the fourth quarter of 2001) has probably contributed to this more cautious behaviour of investors (see Chart B). In fact, most of the valuation gains on quoted shares and mutual fund shares since the end of 1997 were lost between the first quarter of 2000 and the end of 2001.

Chart B: Holdings gains of the euro area non-financial sectors –per instrument

(accumulated quarterly valuation changes, stock of financial assets in 1997 Q4 = 100)



Source: ECB.

Note: Holding gains (+) and losses (-) are calculated as the difference between the change in amounts outstanding and transactions. They may, however, in some cases, include other flows, in particular resulting from reclassifications.

The annual growth of investment in securities other than shares also decreased in the fourth quarter of 2001, to 8.8%, from 10.0% in the third quarter of 2001, although this decline was moderate by comparison with shares. The annual rate of growth of investment in short-term debt securities declined somewhat, but remained at high levels (20.5% in the fourth quarter of 2001). Despite the general preference for short-term assets by investors, investment in long-term debt securities also remained pronounced. The annual rate of growth of investment in long-term debt securities by the non-financial sectors was 7.4% in the fourth quarter of 2001, after 7.7% in the third quarter. This may reflect the higher issuance of debt securities by general government as

well as some impact of a steepening of the yield curve. Investment in insurance (included in the item “insurance technical reserves”) also remained strong, reflecting long-term investment decisions.

¹ This is in line with what has been observed in the monetary analysis of the non-MFI sector. The non-MFI sector encompasses euro area residents who do not belong to the Monetary Financial Institutions (MFIs, i.e. the Eurosystem, credit institutions and money market funds located in the euro area). Accordingly, the non-MFI sector includes non-monetary financial institutions (in particular, insurance corporations). By contrast, the non-financial sector only consists of households, non-financial corporations and general government.