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# Lending to eurozone private sector slows

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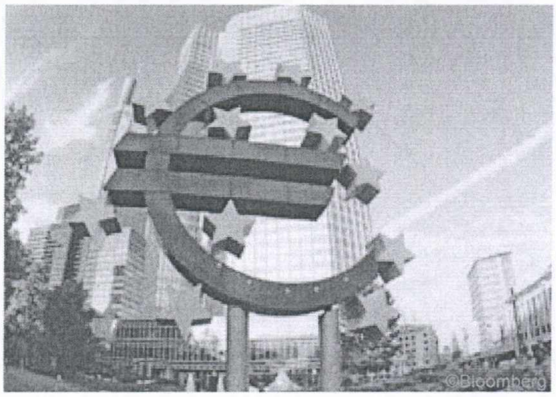
By Ralph Atkins and James Wilson in Frankfurt




The eurozone's economic fragility has been highlighted by the weakest growth in bank lending to the private sector in almost two years, while an unusually-sharp drop in overnight deposits added to worries of fresh banking sector stresses ahead.

In spite of exceptional steps taken by the European Central Bank to boost the supply of credit, lending to the private sector grew at an annual rate of just 0.3 per cent in April – the slowest since May 2010, according to ECB figures on Wednesday.

The ECB has injected more than €1tn of three-year loans into the eurozone banking system since December and hoped that some of the liquidity would find its way to small, job-creating businesses. However, its latest credit figures suggested lending was being held back by weak demand, especially in crisis-hit southern Europe.

The European Commission reported eurozone economic confidence had fallen sharply again in May, adding to evidence that uncertainty about Greece's future in Europe's monetary union was hitting the real economy. Its eurozone "economic sentiment" index dropped from 92.9 in April to 90.6 this month, the lowest since October 2009.

Mario Draghi, ECB president, has put the emphasis on eurozone governments taking action to restore investor confidence. But a significant weakening in economic prospects, or heightened tensions in the banking sector, would strengthen the case for a cut in ECB interest rates or further longer term liquidity offers – although it may await the outcome of Greece's June 17 election and the next European Union leaders' summit.

The ECB argues its liquidity action so far has averted possible disasters in the eurozone financial system. But Spain saw a near €32bn fall in deposits in April, one of the largest monthly falls since the launch of the euro. Analysts watching for signs of funds being withdrawn across the eurozone were struck by a €57bn fall in overnight deposits in April shown in Wednesday's ECB data – the largest month-on-month drop since the launch of the euro in 1999.

The reason for the drop was unclear – and may have reflected technical factors. Elga Bartsch, economist at Morgan Stanley, pointed out that the fall was accounted for by financial intermediaries, rather than households or non-financial businesses. Although the move "warrants close monitoring", it was not the result of "the average citizen pulling money out of the bank," she said.

But Peter Schaffrik at RBC Capital Markets, argued that on the basis of other evidence, "It seems likely that actual withdrawal has taken place and led to an outflow of funds from banks and potentially out of the euro area".

The ECB will also have been disappointed by slower growth in M3, the broad money supply measure, which is used as an indicator of economic activity as well as possible inflation pressures. M3, which had shown signs of re-accelerating this year, grew at an annual rate of 2.5 per cent in April, down from 3.1 per cent in March and the slowest since January.

Christoph Weil, economist at Commerzbank in Frankfurt, warned that "resurging uncertainty is paralysing economic activity in the eurozone." Concerns about Greece and Spain had returned economic sentiment to recession levels and "it is becoming increasingly likely that the eurozone economy will contract in the second quarter," he said.