Retail bank rates, bank lending and monetary policy in the euro area

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Abstract

This paper studies the developments in retail bank lending rates and the amount of bank lending in the euro area as well as the effectiveness of the European Central Bank (ECB) monetary policy, taking special consideration to the impact of the global financial and sovereign debt crises. The extent to which monetary policy rate is reflected in retail bank interest rates and is able to affect the amount of bank lending is crucial for the efficient transmission of monetary policy measures to real economy. It is especially important in the euro area where a majority of external funds supplied to non-financial corporations comes from the banks. Furthermore, any cross-country dispersions in retail bank rates in the euro area imply a lack of uniformity in the cost of funds for the non-financial sector which in turn might contribute to the widening of the macroeconomic gaps and threaten the price and financial stability goals of the ECB. The main observations show that, after the outbreak of the global financial crisis, there was general fall in level of retail bank lending and deposit rates in the euro area, followed by considerable increase in variation in interest rates across euro area countries. At the same time, impact of monetary policy on retail bank lending rates and bank lending became considerably weaker while retail bank lending rates kept significant impact on the amount of bank loans in euro area. Taken together, the results point at monetary policy losing important channel through which it might affect real economy and achieve the price stability goal, and at the danger of higher diversity in bank lending rates across euro area countries, leading to more diverse loan growths and economic situation. While the situation seems to be improving from 2016 on, it is important that new financial market regulations and the currently implemented banking union project are designed so as to secure uniform transmission of monetary policy in case of future financial market tensions, thereby contributing to higher economic convergence in the euro area.