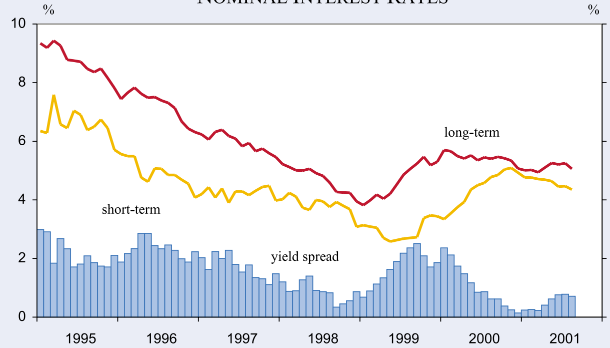
Monetary Conditions in the Euro-Area

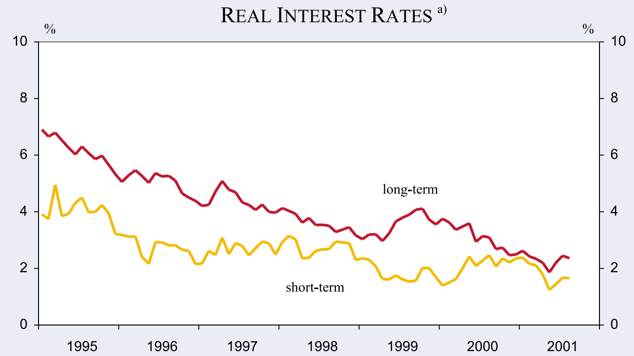
Nominal Interest Rates a)



a) Weighted averages (GDP weights).

Sources: European Central Bank.

Real Interest Rates a)



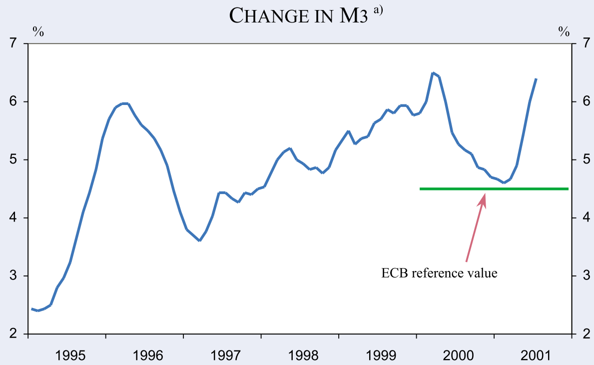
a) Real interest rate = nominal interest rate minus inflation rate.

Sources: European Central Bank.

Money market rates continued to decline, reflecting increased expectations among market participants of reductions in the key ECB interest rates. In the aftermath of the terrorist attacks in the United States, the ECB did decide to lower its key rates by 50 basis points. Long-term bond yields have also fallen over the summer to levels last seen in March 2001. On 10 September the average euro area ten-year government bond yield stood at close to 5.1% which was about 20 basis points lower than at the end of June. As a result, the yield spread, which had widened until July, narrowed a bit again.

Euro-area real interest rates, which had come down sharply during the first half of the year, especially for short-term assets, rose again as inflation subsided, but have recently flattened out. They have now reached a comfortable level, at about 2%.

Change in M3 a)

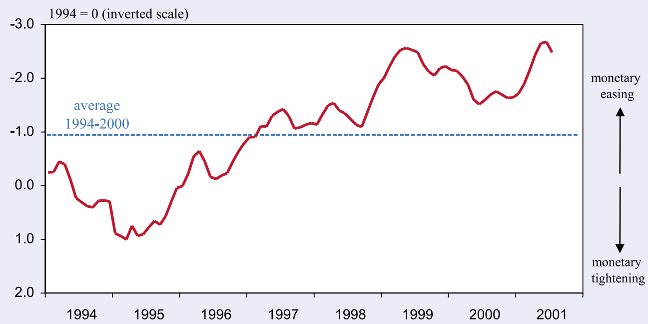


a) Annual percentage change (3-month moving average).

Sources: European Central Bank.

The annual rate of growth of M3 was 6.7% in August, up from 6.4% in July. The three-month moving average of the annual growth rates of M3 over the period June to August 2001 increased to 6.4% from 5.9% during the previous three-month period. According to the ECB, these developments reflect partly the relatively flat yield curve up to August and the weakness of the stock markets, which made the holdings of short-term deposits and marketable instruments included in M3 more attractive.

Euro Area: Monetary Conditions Index



Note: MCI index is calculated as a (smoothed) weighted average of real short-term interest rates (nominal rate minus core inflation rate HCPI) and the real effective exchange rate of the euro.

Sources: European Central Bank, calculations by the Ifo Institute.

The monetary conditions index for September signaled some monetary tightening, reversing the easing throughout the earlier part of the year. While short-term real interest rates declined, the index was dominated by the rise of the effective real exchange rate of the euro.