



European Money-Supply Growth Holds Near 28-Year High (Update1)

By Simone Meier

Oct. 26 (Bloomberg) -- Money-supply growth in the euro region remained near a 28-year high in September, adding to signs inflation may accelerate.

M3 money supply, which the European Central Bank uses as a gauge of future inflation, rose 11.3 percent from a year earlier, after gaining 11.6 percent in August, the Frankfurt-based bank said today. The rate reached 11.7 in July, the highest since August 1979. Economists expected growth of 11.4 percent, the median of 30 forecasts in a Bloomberg News survey showed.

The ECB on Oct. 4 kept its main lending rate on hold after the collapse in U.S. subprime mortgages pushed up global credit costs. With inflation above the bank's 2 percent limit, some ECB council members have signaled they favor raising interest rates further even as the economy of the 13 nations sharing the euro shows signs of cooling.

"Liquidity is still at excessive levels," said Karsten Junius, a senior economist at Dekabank in Frankfurt. "The ECB can't be satisfied with it or sound the all clear."

The ECB has increased its key rate eight times since late 2005 to 4 percent, seeking to quell inflation pressures. President Jean-Claude Trichet on Oct. 4 said money and credit growth in the euro-region was "vigorous."

Elevated Level

M3 is the broadest gauge of money supply and includes cash-in-circulation, some forms of savings and money-market holdings. Its growth rate has exceeded 4.5 percent -- the level the ECB still deems non-inflationary -- every month since May 2001.

The three-month average of the annual M3 growth rate through September was 11.5 percent, up from 11.4 percent in the three months through August, the ECB said. Loans to the private sector rose 11 percent in September from a year earlier, down from 11.2 percent a month earlier.

"A lot of investors have shifted from risky assets to safe havens," boosting money growth, said Andreas Rees, chief German economist at UniCredit Markets & Investment Banking in Munich. "Overall, M3 is certainly distorted to some extent, but the ECB won't discount it because of inflation threats."

An 82 percent surge in oil prices since mid-January is adding to price pressures. Oil rose to a record \$92.22 a barrel today. Inflation accelerated past the ECB's 2 percent limit for the first time in over a year in September.

ECB council members including Axel Weber and Klaus Liebscher have signaled they're in favor of raising interest rates further. Weber said Oct. 20 that "inflation risks have increased recently" and Liebscher said Oct. 21 that "there is no relaxation concerning the risks to price stability."

Fed Rate Cut

While the ECB was forced to shelve a planned rate increase in September, the U.S. Federal Reserve on Sept. 18 cut its key rate by half a percentage point to 4.75 percent to prevent the world's largest economy from slipping into recession.

Rising defaults on U.S. mortgages aimed at people with a poor credit history have made banks reluctant to lend, pushing up global credit costs. The ECB offered banks extra cash in August and September to help restore

confidence.

European banks may make it harder for companies and consumers to borrow money in the next three months after market turmoil, the ECB's quarterly survey showed Oct. 5.

The annual rate of growth of M1, a measure of cash and equivalents, rose 6.1 percent, down from 6.7 percent in the previous month, the ECB said today.

``The positive message is that credit and money supply growth slowed down," said Thorsten Polleit, chief German economist at Barclays Capital in Frankfurt.

The euro-region economy is already losing momentum. European manufacturing growth slowed for a fourth straight month in October. In Germany, Europe's largest economy, business confidence dropped to a 20-month low and French executives also grew more pessimistic this month.

``We're in a phase of economic slowdown and that's why the ECB doesn't need to do anything" on rates, UniCredit's Rees said. ``Inflation will probably slow next year. We expect the ECB to keep interest rates at 4 percent far into 2008."

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