CENTRAL BANKS

The ECB reaffirms its existing stance

Financial Scenarios Unit
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- The GC was unanimous on maintaining its prestated roadmap, “if anything, the central bank will actually add (new measures) to policy stance”
- Macroeconomic projections remained mostly unchanged
- Exit strategies were not discussed

At today’s As expected, at today’s monetary policy meeting there were no changes to the ECB´s monetary policy stance: the Governing Council (GC) left the key policy rate unchanged at 0.05% and took no additional steps on non-standard measures. Mr Draghi reaffirmed its commitment to the full implementation of current monetary policy measures. Moreover, he indicated that the GC was unanimous on keeping steady the current monetary policy stance and, if anything, , leaving open the door to further measures. “If anything, the central bank will actually add to policy stance.” On the inflation outlook, the GC will continue to closely monitor medium-term risks. Meanwhile, risks surrounding the economic outlook remain on the downside (but have become more balanced).

Mr Draghi remained cautious on the economic outlook. He stated that they continue to expect the economic recovery to broaden (this time strengthen gradually was dropped from the statement), but he recognized that they “had expected stronger (growth) numbers", confirming that the recovery has lost some momentum. On the question if recent inflation data have surprised the central bank, Mr Draghi stated that those figures have not beaten ECB´s expectations (but certainly the markets´).

As we expected, the updated staff macroeconomic projections for 2015-17 remain mostly unchanged. The main difference is the upward revision to the inflation forecast for 2015, now at 0.3% YoY (March: 0% YoY, BBVA:0.1% YoY), incorporating recent data and oil prices that signal marginally-higher inflation this year, while projections remain at 1.5% YoY for 2016 and 1.8% YoY for 2017. On GDP, there are no changes, as fundamentals remain broadly unchanged. Growth is expected to be 1.5% YoY in 2015, 1.9% in 2016 and 2.1% in 2017 (BBVA: 1.5% in 2015 and 2.2 in 2016). Overall, both the new projections and their risk assessment are in line with that envisaged in our scenario.

At the press conference, the attention was on Greece. In this context, Mr Draghi took the opportunity to make clear that the central bank wants Greece to remain in the eurozone. He stressed that there is a general will to find an agreement, but he remarked negotiations are in a “state of flux.” He added that there must be a “strong agreement” in terms of design and implementation. On the question about the possibility of raising the limit on Greece´s issuance of T-bills, he reiterated that the country should first achieve a credible perspective of the successful conclusion of the current review.

Regarding the recent surge in European bond yields (and to address questions to whether QE is adding volatility to the markets), Mr Draghi pointed to three possible explanations to current volatility: i) improvement in growth prospects, ii) higher inflation expectations and iii) technical market conditions (among others, poor market liquidity). He added that “one lesson is that we should get used to periods of higher volatility”.

Concerning the exit strategy, Mr Draghi stated that the GC has not discussed any QE exit plan, adding that there still a "long way to go" in terms of inflation, i.e. before the central bank reached its inflation target of close to 2%.

Against this background, Mr. Draghi remained firm with regard to the full implementation of the ECB´s QE plan. In our view, opening the window to speculation over an early tapering would had been both premature and risky. More now than ever, as the recent tightening of monetary conditions (due to the recent sell-off of Eurozone government bonds and the accompanying euro appreciation) should contribute to reaffirm the ECB´s commitment.

PLEASE NOTE: TRACKING CHANGES IN FOLLOWING STATEMENTS

in black, wording common to both the current and previous statements, in red and crossed, previous wording that was replaced by new wording, in blue and underlined (YES, TRACK CHANGES ARE THERE ON PURPOSE)

Mario Draghi, President of the ECB,
Vítor Constâncio, Vice-President of the ECB,
~~15 April~~ Frankfurt am Main, 3 June 2015

Ladies and gentlemen, the Vice-President and I are very pleased to welcome you to our press conference. We will now report on the outcome of today's meeting of the Governing Council, which was also attended by the Commission Vice-President, Mr Dombrovskis.

Based on our regular economic and monetary analyses, and in line with our forward guidance, we decided to keep the **key ECB interest rates** unchanged.

~~As regards~~Regarding **non-standard monetary policy measures**~~,~~, the asset purchase programmes are proceeding well. As explained on ~~9 March we started purchasing euro-denominated public sector securities as part of~~previous occasions, our ~~expanded~~ asset ~~purchase programme, which also comprises~~ purchases of ~~asset-backed securities and covered bonds. Purchases~~€60 billion per month are intended to run until the end of September 2016 and, in any case, until we see a sustained adjustment in the path of inflation that is consistent with our aim of achieving inflation rates below, but close to, 2% over the medium term. When carrying out its assessment, the Governing Council will follow its monetary policy strategy and concentrate on trends in inflation, looking through ~~unexpected outcomes~~fluctuations in measured inflation in either direction if judged to be transient and to have no implication for the medium-term outlook for price stability.

Our monetary policy measures have contributed to a broad-based easing in financial conditions, a recovery in inflation expectations and more favourable borrowing conditions for firms and households. The ~~implementation of our asset purchase programmes is proceeding smoothly, with volumes in line with the announced figure of €60 billion of securities per month. In addition, there is clear evidence that the monetary policy measures we have put in place are effective. Financial market conditions and the cost of external finance for the private sector have eased considerably over the past months~~ effects of these measures are working their way through to the economy and ~~borrowing conditions for firms and households have improved notably, with a pick-up in the demand for credit.~~

~~Looking ahead, our focus will be on the full implementation of our monetary policy measures. Through these measures, we will contribute to a further improvement in the~~ are contributing to economic ~~outlook~~growth, a reduction in economic slack, and ~~a recovery in~~ money and credit ~~growth. Together, such developments will~~expansion. The full implementation of all our monetary policy measures will provide the necessary support to the euro area economy, lead to a sustained return of inflation rates towards ~~a level~~levels below, but close to, 2% ~~over~~in the medium term, and ~~will~~ underpin the firm anchoring of medium to long-term inflation expectations.

Let me now explain our assessment in greater detail, starting with the **economic analysis**. ~~Real~~ In the first quarter of 2015, real GDP in the euro area rose by 0.~~3%, quarter on~~ 4%, quarter~~,~~ on quarter, after 0.3% in the last quarter of 2014. ~~Domestic demand, especially~~In recent quarters, domestic demand and, particularly, private consumption~~, continued to be~~ were the main ~~driver~~drivers behind the ongoing recovery. ~~The latest economic indicators, including survey data up to March, suggest that the euro area economy has gained further momentum since the end of 2014.~~ The latest survey data to May remain consistent with a continuation of the modest growth trend in the second quarter. Looking ahead, we expect the economic recovery to broaden ~~and strengthen gradually~~. Domestic demand should be further supported by ~~ongoing improvements in~~our monetary policy measures and their favourable impact on financial conditions, as well as by the progress made with fiscal consolidation and structural reforms. Moreover, the low~~er~~ level of the price of oil should continue to support households' real disposable income and corporate profitability and, therefore, private consumption and investment. Furthermore, demand for euro area exports should benefit from improvements in price competitiveness.

However, economic growth in the euro area ~~recovery~~ is likely to continue to be dampened by the necessary balance sheet adjustments in a number of sectors and the sluggish pace of implementation of structural reforms.

This assessment is also broadly reflected in the June 2015 Eurosystem staff macroeconomic projections for the euro area, which foresee annual real GDP increasing by 1.5% in 2015, 1.9% in 2016 and 2.0% in 2017. Compared with the March 2015 ECB staff macroeconomic projections, the projections for real GDP growth over the projection horizon remain virtually unchanged.

While remaining on the downside, the risks surrounding the economic outlook for the euro area have become more balanced on account of ~~the recent~~our monetary policy decisions~~, the fall in oil prices and the lower euro~~ and oil price and exchange rate developments.

Inflation bottomed out at the beginning of the year. According to Eurostat's flash estimate, euro area annual HICP inflation was ~~-~~0.~~1~~3% in ~~March~~May 2015, up from ~~-~~0.~~3~~0% in ~~February~~April and compared with -0.6% in January. ~~This pattern largely reflects an increase in oil prices in euro terms since mid-January.~~ On the basis of the information available and current oil futures prices, annual HICP inflation is expected to remain ~~very~~ low ~~or still negative~~ in the months ahead~~. Supported by the favourable impact of our monetary policy measures~~ and to rise towards the end of the year, also on ~~aggregate demand, the impact of the lower euro exchange rate and the assumption~~ account of base effects associated with the fall in oil prices in late 2014. Supported by the expected economic recovery, the impact of the lower euro exchange rate and the assumption embedded in oil futures markets of somewhat higher oil prices in the years ahead, inflation rates are expected to ~~increase later in 2015 and to~~ pick up further during 2016 and 2017.

This assessment is also broadly reflected in the June 2015 Eurosystem staff macroeconomic projections for the euro area, which foresee annual HICP inflation at 0.3% in 2015, 1.5% in 2016 and 1.8% in 2017. In comparison with the March 2015 ECB staff macroeconomic projections, the inflation projections have been revised upwards for 2015 and remain unchanged for 2016 and 2017.

The Governing Council will continue to monitor closely the risks to the outlook for price developments over the medium term. In this context, we will focus in particular on the pass-through of our monetary policy measures, as well as on geopolitical, exchange rate and energy price developments. We acknowledge that the staff projections are conditional on the full implementation of all our monetary policy measures in place. We also take into account that the degree of forecast uncertainty tends to increase with the length of the projection horizon.

Turning to the **monetary analysis**, recent data confirm the ~~gradual~~ increase in underlying growth in broad money (M3). The annual growth rate of M3 increased to ~~4.0~~5.3% in ~~February~~April 2015, up from ~~3.7~~4.6% in ~~January.~~March. Annual growth in M3 continues to be supported by its most liquid components, with the narrow monetary aggregate M1 growing at an annual rate of ~~9.1~~10.5% in ~~February~~April.

Loan dynamics ~~also~~ gradually improved further. The annual rate of change of loans to non-financial corporations (adjusted for loan sales and securitisation) was -0.4~~1~~% in ~~February~~April, after -0.~~9~~2% in ~~January~~March, continuing its gradual recovery from a trough of -3.2% in February 2014. ~~In this respect, the April 2015 bank lending survey confirms that improvements in lending conditions support a further recovery in loan growth, in particular for firms.~~ Despite these improvements, the dynamics of loans to non-financial corporations remain subdued ~~and~~. They continue to reflect the lagged relationship with the business cycle, credit risk, credit supply factors, and the ongoing adjustment of financial and non-financial sector balance sheets. The annual growth rate of loans to households (adjusted for loan sales and securitisation) increased further to 1.~~0~~3% in ~~February~~April 2015, after ~~0.9~~1.1% in ~~January.~~March. The monetary policy measures we have put in place ~~should~~ will support further improvements both in borrowing costs for firms and households and in credit flows across the euro area.

To sum up, a **cross-check** of the outcome of the economic analysis with the signals coming from the monetary analysis confirms the need to ~~implement~~maintain a steady monetary policy course, firmly implementing the Governing Council's ~~recent~~ monetary policy decisions. The full implementation of all our monetary policy measures will provide the necessary support to the ~~euro area~~ economic recovery in the euro area and ~~bring~~lead to a sustained return of inflation rates towards levels below, but close to, 2% in the medium term.

Monetary policy is focused on maintaining price stability over the medium term and its accommodative stance contributes to supporting economic activity. However, in order to reap the full benefits from our monetary policy measures, other policy areas must contribute decisively. Given continued high structural unemployment and low potential output growth in the euro area, the ongoing cyclical recovery should be supported by ~~effective supply-side measures.~~effective **structural policies**. In particular, in order to increase investment, boost job creation and raise productivity, both the implementation of **product and labour market reforms** and actions to improve the business environment for firms need to gain momentum in several countries. A swift and effective implementation of these reforms, in an environment of accommodative monetary policy, will not only lead to higher sustainable economic growth in the euro area but will also raise expectations of permanently higher incomes ~~and~~. Therefore, it will encourage both households to expand consumption and firms to increase investment today, thus reinforcing the current cyclical economic recovery. As concerns **fiscal developments**, reflecting mainly the cyclical recovery and the low level of interest rates, the aggregate euro area general government deficit ratio is projected to decline gradually from 2.1% of GDP this year to 1.5% in 2017. The general government debt ratio is projected to decline gradually from 91.5% of GDP this year to 88.4% in 2017. **Fiscal policies** should support the economic recovery while remaining in compliance with the Stability and Growth Pact. Full and consistent implementation of the Pact is key for confidence in our fiscal framework. ~~In view of the necessity to step up structural reform efforts in a number of countries, it is also important that the macroeconomic imbalance procedure is implemented effectively in order to address the excessive imbalances as identified in individual Member States.~~