CENTRAL BANKS

ECB, the focus is on Greece

Sonsoles Castillo / Maria Martinez

- The ECB reiterates its focus on the full implementation of its measures and its readiness to do more, if needed.
- The asset purchase programme proceeds smoothly, despite recent developments in financial markets.
- On Greece, the ECB increases the ELA to Greek banks by EUR900mn euros as “several positive things that have happened”
- On the euro, Mr Draghi wants decisive steps on further integration

As expected, at today’s monetary policy meeting there were no changes in the ECB´s monetary policy stance, as the central bank left the key policy rate unchanged at 0.05% and took no additional steps on non-standard measures. Mr Draghi reiterated the bank’s commitment to the firm implementation of measures in place. Moreover, he reaffirmed its readiness to do more by using all instruments available within its mandate, if needed. Regarding the economic outlook, the view has not changed, despite "recent developments in financial markets, which partly reflect greater uncertainty". On inflation, the Governing Council (GC) will continue to monitor medium-term risks closely. Meanwhile, the risks surrounding the economic outlook remain on the downside, but have generally been contained as a result of the central bank´s measures and also due to oil price and exchange rate developments.

At the press conference, the (only) issue was Greece and, especially, the provision of emergency liquidity assistance (ELA). Regarding this, Mr Draghi announced that the central bank had decided to increase the ELA by EUR900mn for one week, as requested by the Greek central bank. The ELA funding for Greek banks had been frozen since 29 June at EUR89bn. Mr Draghi clarified that this decision had been taken because conditions to raise the ELA have been restored and because of "several positive things that have happened" in Greece's negotiations with its creditors on a third bailout programme. It should be taken into account that the ECB´s decision came after the Eurogroup released a statement (see) welcoming the Greek vote and launching the third bailout. Moreover, he took the opportunity to emphasise that the Greek banks are solvent and thus they qualify to receive the ELA. Moreover, he said that there was no decision on ELA collateral haircut today.

In response to a question about whether the ECB will be repaid by Greece on 20 July, Mr Draghi highlighted that he expects that the country will repay EUR3.5bneuros to central bank on that day. In this context, the European Commission today agreed (although it has yet to finalise) to use the EFSM for a EUR7bn bridging loan to Greece, until the country reaches an agreement on the third bailout programme.

Regarding capital controls in Greece, this increasing of the ELA is a first step for the normalisation of the Greek banks’ situation, but Mr Draghi highlighted that it is difficult to predict when capital controls could be lifted (they were imposed on 29 June after the breakdown of the bailout negotiations). Moreover, he added that any decision on capital controls rests with the Greek government, emphasising that “It’s clearly in the interest of the Greek economy to have these capital controls last as little as possible”.

On the Greek deal reached on Monday, Mr Draghi said that the agreement has an impressive list of planned reforms. He also stressed that the country needs a “strong, sustainable and fair programme”, and when asked about concerns on implementation, he admitted that there are “doubts and questions”. Regarding the possibility of any debt relief for the country, he stated that “it is uncontroversial that debt relief is necessary, and I think that nobody has ever disputed that." He also added that the question is how this could be achieved within the legal institutional framework.

Mr Draghi asked for further integration with the eurozone as the recent Greek debt crisis has shown that the current structure is fragile. "This union is imperfect, and being imperfect is fragile, vulnerable and doesn't deliver ... deliver all the benefits that it could if it were to be completed. The future now should see decisive steps on further integration."

Against this background, Mr. Draghi remained firm on the full implementation of the ECB's QE plan. In our view, the message from the ECB continues to be quite supportive. This is especially important in the current climate of heightened uncertainty, not just because of the Greek situation but also on account of other global risk factors.

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,

Frankfurt am Main, ~~3 June~~16 July 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.

Regarding **non-standard monetary policy measures**, the asset purchase programmes ~~are proceeding well.~~continue to proceed smoothly. As explained on previous occasions, our monthly asset purchases of €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 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 effects of these measures are working their way through to the economy and are contributing~~All in all, the information that has become available since the Governing Council meeting in early June has been broadly in line with our expectations. Recent developments in financial markets, which partly reflect greater uncertainty, have not changed the Governing Council's assessment of a broadening of the euro area's economic recovery and a gradual increase in inflation rates over the coming years. The ECB's monetary policy stance remains accommodative and market-based inflation expectations have, on balance, stabilised or recovered further since our meeting in early June. The latest information also remains consistent with a continued pass-through of our monetary policy measures to the cost and availability of credit for firms and households. Our measures thereby continue to contribute to economic growth, a reduction in economic slack, and money and credit 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 levels below, but close to, 2% 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**. In the first quarter of 2015, real GDP in the euro area rose by 0.4%, quarter on quarter, after 0.3% in the last quarter of 2014. In recent quarters, domestic demand and, particularly, private consumption were the main drivers behind the ongoing recovery.~~Looking ahead, we will continue to closely monitor the situation in financial markets, as well as the potential implications for the monetary policy stance and for the outlook for price stability. If any factors were to lead to an unwarranted tightening of monetary policy, or if the outlook for price stability were to materially change, the Governing Council would respond to such a situation by using all the instruments available within its mandate.
Let me now explain our assessment of the available information in greater detail, starting with the **economic analysis**. Euro area quarterly real GDP growth was confirmed at 0.4% in the first quarter of 2015, supported by contributions from private consumption and investment. The latest survey data, available up to ~~May~~June, remain consistent with a continuation of the ~~modest~~moderate growth trend in the second quarter. Looking ahead, we expect the economic recovery to broaden further. Domestic demand should be further supported by 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 level of the price of~~ recent decline in oil prices should ~~continue to~~provide additional support for 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, the ongoing slowdown in emerging market economies continues to weigh on the global outlook and economic growth in the euro area 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~~ The downside~~, the~~ risks surrounding the economic outlook for the euro area have ~~become more balanced on account~~generally been contained as a result of our monetary policy decisions~~ and~~ , as well as oil price and exchange rate developments.

Inflation bottomed out at the beginning of the year and has moved back into positive territory in recent months. According to Eurostat~~'s flash estimate~~, euro area annual HICP inflation was 0.~~3% in May 2015, up from 0.0~~2% in ~~April and compared with -0.6% in January.~~June 2015, slightly down from 0.3% in May. On the basis of the information available and current oil futures prices, annual HICP inflation is expected to remain low in the months ahead and to rise towards the end of the year, also on 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 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, energy and 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 increase in underlying~~robust growth in broad money (M3). The annual growth rate of M3 ~~increased to~~was 5.~~3~~0% in ~~April~~May 2015, ~~up from 4.6% in March.~~compared with 5.3% in April. Annual growth in M3 continues to be strongly supported by its most liquid components, with the narrow monetary aggregate M1 growing at an annual rate of ~~10.5~~11.2% in ~~April~~May.

Loan dynamics ~~gradually improved further.~~continued to improve. The annual rate of change of loans to non-financial corporations (adjusted for loan sales and securitisation) ~~was -0.1% in April, after -0.2% in March~~increased to 0.1% in May, up from -0.1% in April, continuing its gradual recovery from a trough of -3.2% in February 2014. This is consistent with the positive evidence from the bank lending survey for the second quarter of 2015. Banks reported a continued net easing of credit standards on loans to enterprises which was stronger than expected in the previous survey round. Net demand for loans to enterprises increased further, supported by demand for credit related to fixed investment. Fragmentation in terms of credit demand in individual countries decreased and the targeted longer-term refinancing operations helped to improve the terms and conditions for credit supply. Despite these improvements, the dynamics of loans to non-financial corporations remain subdued. 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.~~3~~4% in ~~April~~May 2015, after 1.~~1~~3% in ~~March. The~~ April. Overall, the monetary policy measures we have put in place ~~will~~since June 2014 provide clear support ~~further~~for improvements both in borrowing ~~costs~~conditions 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 maintain a steady monetary policy course, firmly implementing the Governing Council's monetary policy decisions. The full implementation of all our monetary policy measures will provide the necessary support to the economic recovery in the euro area and 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 **structural policies**. In particular, in order to increase investment, boost job creation and raise productivity, both the implementation ~~of~~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. ~~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.

DISCLAIMER