CENTRAL BANKS

The ECB hints clearly at further stimuli in December

Sonsoles Castillo / Maria Martinez

- The ECB “will re-examine” the degree of stimulus in December.
- The GC had a “very rich discussion” about possible instruments. Some GC members wanted to act at today´s meeting.
- The GC showed concern about the slowing return of inflation to the target.

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%. As regards non-standard measures, the central bank unexpectedly hinted at an easing by the central bank as early as December. In this way, the dovish tone was reinforced and the easing bias was strengthened as the ECB stated that it “will re-examine the degree of the policy accommodation at the next monetary policy meeting”. In particular, Mr. Draghi stated that the governing council (GC) had "a very rich discussion" and was "open to a whole menu of monetary policy instruments.” Moreover, he said that some members had wanted to act at today´s meeting. On the outlook for inflation, the GC will continue to closely monitor renewed risks – those related to current developments in emerging economies as well as financial markets and commodity prices - as they could further slow down the gradual increase in inflation rates towards 2%. Besides, on the economic outlook the risks also remain to the downside.

Mr Draghi remained cautious on the economic outlook, and stressed that the downside risks remain to both economic growth and inflation, arising from slowing growth in emerging markets. On the recovery of the eurozone’s economy, he said that domestic demand seemed resilient, but that external demand due to weakness in emerging markets, and in particular in China, poses a risk for the recovery. On inflation, Mr Draghi highlighted that the strength and persistence of these factors are slowing down the return of inflation towards the ECB´s objective. Particularly, Draghi mentioned that the bank is currently more cautious about lower oil prices, as they seem to be driven more by demand than supply. In this regard, he stated that the central bank will remain “vigilant” on inflation.

At the press conference, the attention was focused on which way the ECB is ready to implement further measures. Mr Draghi highlighted that there was “a very rich discussion” about all the monetary policy instruments that could be used, but that no decision had been reached yet. On its readiness to do more, he said that the relevant committees had been tasked with examining all possible monetary policy tools. He stressed that the central bank´s stance was not one of “wait and see” but of “work and assess”. In particular, on the question whether one of the tools that was discussed was a further cut in the deposit rate, (this had not been done at the previous meeting, emphasising that the bank was currently at “zero lower bound”), he said that it is reassessing this possibility on the back on the experience of other central banks, and it is therefore now on the table. This haste in the need to re-examine the degree of monetary policy accommodation certainly contrasts with the latest statements from ECB members in which they judged that it was too early to judge whether more easing is needed.

All in all, after listening to Draghi today, we expect the ECB to act in December. It is difficult to foresee, in the coming months, a variation in the inflation outlook that would change its mind. While Draghi gave no clear hints on the choice of any particular measure, an extension of the asset purchase programme (APP) could be one of the preferred options (given the bank’s implicit commitment to keep rates low for longer). We will wait to see the details of the discussion, which will be revealed in the minutes of the meeting, to be published on 19 November.

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)

Introductory statement to the press conference

Mario Draghi, President of the ECB,

Vítor Constâncio, Vice-President of the ECB,

Malta, 22 October~~Frankfurt am Main, 3 September~~ 2015

Ladies and gentlemen, the Vice-President and I are very pleased to welcome you to our press conference. I would like to thank Governor Bonnici for his kind hospitality and express our special gratitude to his staff for the excellent organisation of ~~We will now report on the outcome of~~ today's meeting of the Governing Council. We will now report on the outcome of our meeting~~As usual, let me start with the decisions taken~~.

Based on our regular economic and monetary analyses~~analysis~~, and in line with our forward guidance, the Governing Council decided to keep the **key ECB interest rates**unchanged. As regards **non-standard monetary policy measures**, the asset purchases are proceeding smoothly and continue to have a favourable impact on the cost and availability of credit for firms and households.

The ~~Our asset purchase programme continues to proceed smoothly. Regarding **non-standard monetary policy measures**, following the announced review of the public sector purchase programme's issue share limit after the first six months of purchases, the~~ Governing Council has been closely monitoring incoming information since~~decided to increase the issue share limit from the initial limit of 25% to 33%, subject to a case-by-case verification that this would not create a situation whereby the Eurosystem would have blocking minority power, in which case the issue share limit would remain at 25%.~~

~~Underlying~~ our meeting in early September. While euro area domestic demand remains resilient, concerns over growth prospects~~monetary policy assessment was a review of recent data, new staff macroeconomic projections and an interim evaluation of recent market fluctuations. The information available indicates a continued though somewhat weaker economic recovery and a slower increase~~ in emerging markets and possible repercussions for the economy from developments in financial and commodity markets continue to signal~~inflation rates compared with earlier expectations. More recently, renewed~~ downside risks ~~have emerged~~ to the outlook for growth and inflation. Most notably, the strength and persistence of the factors that are currently slowing the return of inflation to levels below, but close to, 2% in the medium term require thorough analysis. In this context, the degree of monetary policy accommodation will need to be re-examined at our December monetary policy meeting, when the new Eurosystem staff macroeconomic projections will be available. The Governing Council is willing and able~~However, owing to sharp fluctuations in financial and commodity markets, the Governing Council judged it premature to conclude on whether these developments could have a lasting impact on the outlook for prices and on the achievement of a sustainable path of inflation towards our medium-term aim, or whether they should be considered to be mainly transitory.~~

~~Accordingly, the Governing Council will closely monitor all relevant incoming information. It emphasises its willingness and ability~~ to act~~, if warranted,~~ by using all the instruments available within its mandate if warranted in order to maintain an appropriate degree of monetary accommodation. In ~~and, in~~ particular, the Governing Council recalls that the asset purchase programme provides sufficient flexibility in terms of adjusting its~~the~~ size, composition and duration. ~~of the programme.~~

In the meantime, we will continue to fully implement the~~our~~ monthly asset purchases of €60 billion. These purchases ~~have a favourable impact on the cost and availability of credit for firms and households. They~~ are intended to run until the end of September 2016, or beyond, if necessary, 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.

Let me now explain our assessment of the available information in greater detail, starting with the **economic analysis**. Euro~~Real GDP in the euro~~ area real GDP increased~~rose~~ by 0.4%, quarter on quarter,~~3%~~ in the second quarter of 2015, following a rise of 0.5% in the previous quarter.~~which was somewhat lower than previously expected.~~ The outcome for the second quarter reflected positive contributions from both domestic demand and net exports. The most recent~~latest~~ survey indicators point to a broadly similar pace of real GDP growth in the third quarter~~second half~~ of the~~this~~ year. Overall, we expect the economic recovery to continue, albeit dampened,~~at a somewhat weaker pace than earlier expected, reflecting~~ in particular, by weaker than expected ~~the slowdown in emerging market economies, which is weighing on global growth and~~ foreign demand. ~~for euro area exports.~~ 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 decline in oil prices should provide support for households' real disposable income and corporate profitability and, therefore, private consumption and investment. However, the recovery in domestic demand~~economic growth~~ in the euro area continues~~is likely to continue~~ to be hampered~~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 September 2015 ECB staff macroeconomic projections for the euro area, which foresee annual real GDP increasing by 1.4% in 2015, 1.7% in 2016 and 1.8% in 2017. Compared with the June 2015 Eurosystem staff macroeconomic projections, the outlook for real GDP growth has been revised down, primarily due to lower external demand owing to weaker growth in emerging markets.~~

The risks to the euro area growth outlook remain on the downside, reflecting in particular the heightened uncertainties regarding~~related to the external environment. Notably, current~~ developments in emerging market economies, which have the potential to further weigh on~~affect~~ global growth ~~adversely via trade~~ and foreign demand for euro area exports.

Increased uncertainty has recently manifested itself in financial market developments, which may have negative repercussions for euro area domestic demand~~confidence effects~~.

According to Eurostat~~Eurostat's flash estimate~~, euro area annual HICP inflation was -0.1~~2~~% in September~~August~~ 2015, down~~unchanged~~ from 0.1% in August.~~June and July.~~ Compared with the previous month, this mainly reflects a further decline in energy price inflation~~, compensated for by higher price increases for food and industrial goods~~. On the basis of the information available and current oil futures prices, annual HICP inflation rates will remain very low in the near term. Annual HICP inflation is expected to rise at~~towards~~ the turn~~end~~ of the year, also on account of base effects associated with the fall in oil prices in late 2014. Inflation rates are foreseen to pick up further during 2016 and 2017, supported by the expected economic recovery, the pass-through of past declines in the euro exchange rate and the assumption of somewhat higher oil prices in the years ahead as currently reflected in oil futures markets. However, there are risks stemming from the economic outlook and from financial and commodity market developments which could further slow down the gradual~~this~~ increase in ~~annual~~ inflation rates towards levels closer~~is currently expected~~ to 2%. These risks are being closely monitored by the Governing Council~~materialise somewhat more slowly than anticipated thus far~~.

~~This assessment is also broadly reflected in the September 2015 ECB staff macroeconomic projections for the euro area, which foresee annual HICP inflation at 0.1% in 2015, 1.1% in 2016 and 1.7% in 2017. In comparison with the June 2015 Eurosystem staff macroeconomic projections, the outlook for HICP inflation has been revised down, largely owing to lower oil prices. Taking into account the most recent developments in oil prices and recent exchange rates, there are downside risks to the September staff inflation projections.~~

~~In this context, the Governing Council will closely monitor the risks to the outlook for price developments over the medium term. We will focus in particular on the pass-through of our monetary policy measures, as well as on global economic, financial, commodity price and exchange rate developments.~~

Turning to the **monetary analysis**, recent data confirm solid~~robust~~ growth in broad money (M3), notwithstanding a decline in the ~~). The~~ annual growth rate of M3 to 4.8% in August 2015 from~~was~~ 5.3% in July.~~ 2015, compared with 4.9% in June.~~ Annual growth in M3 continues to be mainly~~increasingly~~ supported by its most liquid components, with the narrow monetary aggregate M1 growing at an annual rate of 11.4% in August, after 12.2~~1~~% in July~~, compared with 11.7% in June~~.

Loan dynamics continued to improve. The annual rate of change of loans to non-financial corporations (adjusted for loan sales and securitisation) increased to 0.4% in August, up from 0.3~~9~~% in July, pursuing~~up from 0.2% in June, continuing~~ its gradual recovery since the beginning of 2014. Despite these improvements, developments in~~the dynamics of~~ loans to enterprises~~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 to 1.0% in August 2015, compared with 0.9% in July. The euro area bank lending survey for the third quarter of 2015 confirms the increase in demand for bank loans, supported by the general level of interest rates, financing needs for investment purposes and housing market prospects. In addition, credit standards eased further on loans to enterprises, notably due to increasing competitive pressures in retail banking, while tightening somewhat on loans to households for house purchase.~~9% in July~~

~~2015, after 1.7% in June.~~ Overall, the monetary policy measures we have put in place since June 2014 provide clear support for improvements both in borrowing 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 indicates the need to firmly implement the Governing Council's monetary policy decisions and to monitor closely all relevant incoming information as concerns their impact on the medium-term outlook for price stability.

Monetary policy is focused on maintaining price stability over the medium term and its accommodative stance supports~~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,~~Further product and labour market reforms, and particularly~~ actions to improve the business environment, including the provision of an adequate public infrastructure, are vital to increase productive investment, boost job creation and raise productivity. The swift and effective implementation of structural~~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 accelerate the benefits of reforms, thereby making the euro area more resilient to global shocks. **Fiscal policies** should support the economic recovery, while remaining in compliance with the EU's fiscal rules.~~Stability and Growth Pact.~~ Full and consistent implementation of the Stability and Growth Pact is crucial for confidence in our fiscal framework. At the same time, all countries should strive for a growth-friendly composition of fiscal policies.

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