CENTRAL BANKS

Wait-and-see stance

Soncoles Castillo / Agustín García / Maria Martinez

- The ECB has left interest rates unchanged
- Macroeconomic projections remain mostly unchanged
- The focus is on the implementation of the measures announced in March

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 0.0% and the deposit rate at -0.4%. The ECB reiterated that if warranted to achieve its objective, it will act using all the instruments in its mandate. "It is quite clear we will not hesitate to act." However, during the press conference, Mr Draghi stressed that the focus is on the implementation of the measures taken in March. Regarding the outlook for growth and inflation, the Governing Council (GC) highlighted that for both, the balance of risks has improved on the back of the monetary policy measures taken. Nonetheless, risk continue to relate to developments in the global economy, to the upcoming British referendum (mentioned in the statement for the first time) and to other geopolitical risks.

The central bank announced today that it would start its corporate bond purchase programme (CSPP) on 8 June (remaining details have also been released, see) and would conduct its first TLTROII on 22 June.

At the press conference, the dovish tone was retained, reiterating that the GC will closely monitor the evolution of the outlook for price stability, with a special focus on second-round effects. "We still see no substantial pressures on the wage and price-setting mechanisms, with the possible exception of Germany." However, Mr Draghi made clear that the central bank is determined to act if second-round effects did appear.

The ECB's Staff macroeconomic projections barely changed over the forecast horizon, beyond the slight upward revision this year due to better than expected incoming data (+0.2pp to 1.6% for GDP and +0.1pp to 0.2% for inflation), but the balance of risks for growth has improved (still tilted to the downside). Slightly more surprising to analysts were the unchanged inflation forecasts for 2017 and 2018 (1.3% and 1.6%, respectively) after the increase in oil prices in the last three months. This should be partly offset by a marginally stronger euro path but especially by the downward revision of core inflation over the forecast horizon (-0.1pp each year to 1%, 1.2% and 1.5%). This reflects weaker figures than expected three months ago, raising doubts about potential second-round effects of lower oil prices, except for Germany. Finally, GDP growth forecast for 2016 remains unchanged at 1.7% in 2017, while it was revised downwards slightly for 2018, probably due to the slightly stronger euro and weaker foreign demand.

At this meeting, Greece has returned to the forefront at the press conference, as euro zone ministers reached a deal on Greece debt relief last week. Mr Draghi clarified that the GC did not take a decision on the restoration of the waiver for Greek government bonds that could allow banks access to normal refinancing operations. He stated that they have to see what ESM will decide, highlighting that this decision will require more progress and another monetary policy meeting. This means that Greek sovereign debt will not be eligible at the first TLTRO II (next monetary policy meeting will be held on 21, July)

On the upcoming Brexit referendum, Mr Draghi said that the UK and the euro zone are "mutually beneficial", highlighting that the UK should stay in the European Union. On the question whether the ECB is ready for any outcome, Mr Draghi said that the ECB is ready for all contingencies.

At today´s meeting, as expected Mr Draghi confirmed the ECB´s pledge to maintain a steady monetary policy course. We expect the ECB to remain on hold, monitoring the impact of the measures announced in March.

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, 21 April~~Vienna, 2 June 2016

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~~ I would like to thank Governor Nowotny for his kind hospitality and express our special gratitude to his staff for the excellent organisation of today's meeting of the Governing Council~~, which was also attended by the Commission Vice-President, Mr Dombrovskis~~. We will now report on the outcome of our meeting.

Based on our regular economic and monetary analyses, we decided to keep the **key ECB interest rates** unchanged. We continue to expect them to remain at present or lower levels for an extended period of time, and well past the horizon of our net asset purchases. Regarding **non-standard monetary policy measures**, ~~as decided on 10 March 2016,~~ we ~~have started to expand our~~ confirm that the monthly asset purchases ~~under the asset purchase programme to €~~of €80 billion~~, from the previous amount of €60 billion. As stated before, these purchases~~ are intended to run until the end of March 2017, or beyond, if necessary, and in any case until the Governing Council sees a sustained adjustment in the path of inflation consistent with its inflation aim. As a next step, on 8 June we will start making purchases under our **corporate sector purchase programme (CSPP)**. Moreover, ~~in~~starting on 22 June, we will conduct the first operation ~~of~~in our new series of **targeted longer-term refinancing operations** ~~(TLTRO II) and we will commence purchases under our corporate sector purchase programme (CSPP).~~. Further information on ~~the~~ implementation aspects of the CSPP will be released after the press conference on the ECB's website.

~~Following our~~The comprehensive package of decisions taken in early March~~, broad financing conditions in the euro area have improved. The pass-through of the monetary policy stimulus to firms and households, notably through the banking system, is strengthening. However, global uncertainties persist.~~

~~Looking forward, it is essential to preserve an appropriate degree of monetary accommodation as long as needed in order to underpin~~ underpins the momentum of the euro area's economic recovery and ~~in order to accelerate~~fosters the return of inflation to levels below, but close to, 2%. ~~The Governing Council will~~ In particular, our measures continue to ~~monitor closely~~ease the cost of credit and contribute to a strengthening in credit creation. The economic recovery is gradually proceeding. Additional stimulus, beyond the impetus already taken into account, is expected from the monetary policy measures still to be implemented and will contribute to further rebalancing the ~~evolution of~~risks to the outlook for ~~price stability and, if warranted to achieve its objective, will act by using all the instruments available within its mandate~~growth and inflation. In the current context, it is crucial to ensure that the very low inflation environment does not become entrenched in second-round effects on wage and price setting. The Governing Council will closely monitor the evolution of the outlook for price stability and, if warranted to achieve its objective, will act by using all the instruments available within its mandate.

Let me now explain our assessment in greater detail, starting with the **economic analysis**. Euro area real GDP increased by 0.~~3~~5%, quarter on quarter, in the ~~fourth~~first quarter of 2016, after 0.3% in the last quarter of 2015~~,~~. Growth continues to be supported by domestic demand, while being dampened by ~~relatively~~ weak ~~export trends. Incoming~~exports. The latest data ~~for the first quarter of 2016~~ point to ongoing ~~output~~ growth~~, at a pace broadly similar to that~~ in the ~~final~~second quarter ~~of 2015.~~, though possibly at a lower rate than in the first quarter. Looking ahead, we expect the economic recovery to proceed~~.~~ at a moderate but steady pace. Domestic demand~~, in particular, continues to be~~ remains supported by the pass-through of our monetary policy measures~~. Their favourable impact on~~ to the real economy. Favourable financing conditions~~, together with~~ and improvements in corporate profitability~~, is benefiting~~ continue to promote investment. Moreover, ~~our accommodative monetary policy stance, continued~~sustained employment gains ~~resulting~~, which are also benefiting from past structural reforms, and ~~the~~ still relatively low ~~price of~~ oil ~~should~~prices provide ~~ongoing~~additional support for households' real disposable income and private consumption. In addition, the fiscal stance in the euro area is slightly expansionary. ~~At the same time~~However, the economic recovery in the euro area ~~is still~~continues to be dampened by ~~the ongoing~~subdued growth prospects in emerging markets, the necessary balance sheet adjustments in a number of sectors~~, the insufficient~~ and a sluggish pace of implementation of structural reforms ~~and subdued growth prospects in emerging markets~~.

This outlook is broadly reflected in the June 2016 Eurosystem staff macroeconomic projections for the euro area, which foresee annual real GDP increasing by 1.6% in 2016 and 1.7% in 2017 and 2018. Compared with the March 2016 ECB staff macroeconomic projections, the outlook for real GDP growth has been revised up for 2016 and has remained broadly unchanged for 2017 and 2018.

The risks to the euro area growth outlook ~~still~~ remain tilted to the downside~~. Our recent~~, but the balance of risks has improved on the back of the monetary policy ~~decisions have improved overall financing conditions, which should support the outlook for consumption and investment. However, uncertainties persist and~~ measures taken and the stimulus still in the pipeline. Downside risks continue to relate~~, in particular,~~ to developments in the global economy, to the upcoming British referendum and to other geopolitical risks.

According to ~~Eurostat~~Eurostat's flash estimate, euro area annual HICP inflation in ~~March~~May 2016 was -0.~~0%, compared with~~ 1%, up from -0.2% in ~~February,~~ April, mainly reflecting ~~mainly a rise in~~higher energy and services price inflation. Looking ahead, on the basis of current futures prices for ~~energy~~oil, inflation rates ~~could turn~~are likely to remain very low or negative ~~again~~ in the ~~coming~~next few months before picking up in the second half of 2016~~.~~ ~~Thereafter, supported~~, in large part owing to base effects in the annual rate of change of energy prices. Supported by our monetary policy measures and the expected economic recovery, inflation rates should recover further in 2017 and 2018.

This broad pattern is also reflected in the June 2016 Eurosystem staff macroeconomic projections for the euro area, which foresee annual HICP inflation at 0.2% in 2016, 1.3% in 2017 and 1.6% in 2018. In comparison with the March 2016 ECB staff macroeconomic projections, the outlook for HICP inflation has been revised slightly up for 2016, reflecting recent oil price increases, and has remained unchanged for 2017 and 2018.

Turning to the **monetary analysis**, broad money (M3) continued to grow at a robust pace in ~~February~~April 2016, with its annual rate of growth ~~remaining unchanged~~standing at 4.6%, after 5.0~~%.~~% in March. As in previous months, annual growth in M3 is mainly supported by its most liquid components, with the narrow monetary aggregate M1 growing at an annual rate of ~~10.3~~9.7% in ~~February~~April, after 10.~~5~~1% in ~~January~~March.

Loan dynamics followed the path of gradual recovery observed since the beginning of 2014. The annual rate of change of loans to non-financial corporations (adjusted for loan sales and securitisation) ~~increased to 0.9~~stood at 1.2% in ~~February~~April 2016, ~~up from 0.6~~compared with 1.1% in ~~January~~March. Developments in loans to enterprises continue to reflect the lagged relationship with the business cycle, credit risk 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~~remained broadly stable at 1.5% in April, after 1.6% in ~~February 2016, from 1.4% in January~~March.

~~The euro area bank lending survey for the first quarter of 2016 indicates further improvements in loan supply conditions for enterprises and in loan demand across all loan categories. Improvements in the demand for bank loans were supported by the low level of interest rates, financing needs for investment purposes and housing market prospects.~~

~~Overall, the~~The monetary policy measures in place since June 2014 have clearly improved borrowing conditions for firms and households, as well as credit flows across the euro area. The comprehensive package of new monetary policy measures adopted in March this year underpins the ongoing upturn in loan growth, thereby supporting the recovery of the real economy.

To sum up, a **cross-check** of the outcome of the economic analysis with the signals coming from the monetary analysis confirmed the need to preserve an appropriate degree of monetary accommodation in order to secure a return of inflation rates towards levels that are below, but close to, 2% without undue delay.

Monetary policy is focused on maintaining price stability over the medium term and its accommodative stance supports economic activity. As emphasised repeatedly by the Governing Council, and as again strongly echoed in both European and international policy discussions, in order to reap the full benefits from our monetary policy measures, other policy areas must contribute much more decisively, both at the national and at the European levels. **Structural policies** are essential, given continued high structural unemployment and low potential output growth in the euro area. ~~In particular,~~Structural reforms are necessary in all euro area countries, although specific reform needs differ across the individual economies. At this stage, the focus should be on actions to raise productivity and improve the business environment, including the provision of an adequate public infrastructure, which are vital to increase investment and boost job creation. ~~The~~The enhancement of current investment initiatives, including the extension of the Juncker plan, and progress on the capital markets union will also contribute positively to this objective. In an environment of accommodative monetary policy, the swift and effective implementation of structural reforms, in ~~an environment of accommodative monetary policy~~line with the country-specific recommendations recently published by the European Commission, will not only lead to higher sustainable economic growth in the euro area but will also make the euro area more resilient to global shocks. **Fiscal policies** should also support the economic recovery, while remaining in compliance with the fiscal rules of the European Union. Full and consistent implementation of the Stability and Growth Pact over time and across countries is crucial to maintain confidence in the fiscal framework. At the same time, all countries should strive for a more growth-friendly composition of fiscal policies.

DISCLAIMER