CENTRAL BANKS

The ECB remains patient

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- As widely expected, the ECB has remained on hold and has not changed its communication
- ECB signalled that, despite the recent improvement, the risk surrounding the economic outlook is biased to the downside mainly due to global factors. On inflation, also as expected, the ECB has put the focus on underlying inflation -that remains subdued- instead of headline inflation, thus trying to dampen any concerns on inflation.
- Draghi remarked that the tapering issue was not discussed and he wanted to avoid any speculation on this issue.

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%. Regarding non-standard monetary policy measures, the Governing Council confirmed the measures taken last December, i.e. intended to continue the asset purchase programme at a monthly pace of EUR 80 bn until March 2017 and at a monthly pace of EUR 60 bn since April 2017 until December 2017.

In the statement, the **ECB highlighted the recent improvement in euro area economic outlook**, with "the **survey data pointing to a somewhat stronger growth**" in 4Q16. However, the ECB still sees the risk to the euro area growth **tilted to the downside and related with global factors**. Mr. Draghi stated that "it is too early" to know what will be the impact of Brexit negotiations or the ongoing US administration policies.

The key issue in this meeting was the ECB's view on the **recent upward trend in headline inflation**. For Draghi, recent increasing headline inflation **reflects the sharp rebound in the energy component, while he does not see a convincing improvement in core inflation**. Draghi also admitted that higher than expected headline inflation combined with higher oil prices put an upward bias to the December Staff macroeconomic projections, but the pick in the near term should be transitory without implications for the medium-run. **He remarked that inflation improvement should be durable, non-transient, self-sustained** *"it has to stay there even when the extraordinary monetary policy will not be there."*, **and** it should also be **for the whole eurozone** beyond the heterogeneity across member states (in reference to German critics). In addition, Draghi stressed that deflation risk "largely disappeared". Furthermore, in the statement, they make some changes, removing the previous wording *"will closely monitor the evolution of inflation outlook"* while adding *"the Governing Council will continue to look through changes in HICP inflation if judged to be transient and to have no implication for the medium-term outlook for price stability".*

Regarding tapering talks, Draghi remarked that the issue was not discussed because *"we are still not there"* and insisted that December's decision to reduce the monthly amount of purchases was a recalibration process but not tapering, Furthermore he did not give any clue about the future tapering process. Definitely he wanted to avoid any speculation on this issue.

The Governing Council **showed confident about the smooth implementation of current asset purchase programme** despite recent time extension of ECB program (until Dec-17) and provided details on AAPP with **yields below deposit facility rate** (DFR): the option to buy **below the depo rate only applies to PSPP program** and the ECB will give a clear priority to purchases of assets above the DFR. Consequently the amount of purchases that have to be made at yields below the DFR could vary among jurisdictions and over time.

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, ~~8 December 2016~~19 January 2017

Ladies and gentlemen, ~~the~~first of all let me wish you a Happy New Year. 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, we ~~today conducted a comprehensive assessment~~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 ~~the economic~~time, and ~~inflation outlook and our monetary policy stance. As a result,~~well past the ~~Governing Council took the following decisions in the pursuit~~horizon of ~~its price stability objective:~~

~~As regards~~our net asset purchases. Regarding non-standard monetary policy measures, we confirm that we will continue to make purchases under the asset purchase programme (APP) at the current monthly pace of €80 billion until the end of March 2017~~. From~~ and that, from April 2017, our net asset purchases are intended to continue at a monthly pace of €60 billion until the end of December 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. ~~If, in the meantime, the outlook becomes less favourable, or if financial conditions become inconsistent with further progress towards a sustained adjustment of the path of inflation, the Governing Council intends to increase the programme in terms of size and/or duration.~~ The net purchases will be made alongside reinvestments of the principal payments from maturing securities purchased under the APP.

~~To ensure the continued smooth implementation of the Eurosystem's asset purchases, the~~The Governing Council today also decided ~~to adjust the parameters of the APP as of January 2017 as follows. First, the maturity range of the public sector purchase programme will be broadened by decreasing the minimum remaining maturity for eligible securities from two years to one year. Second, purchases of securities under the APP with a yield to maturity~~on further details of how the Eurosystem will buy assets with yields below the interest rate on the ~~ECB's~~ deposit facility ~~will be permitted to the extent necessary.~~

~~The key ECB interest rates were kept unchanged and we continue to expect them to remain~~ under its public sector purchase programme. These decisions will be published in a separate press release at ~~present or lower levels for an extended period of time, and well past the horizon of our net asset purchases.~~ 15.30 CET.

~~Today's extension of the asset purchase programme has been calibrated to preserve~~The monetary policy decisions taken in December 2016 have succeeded in preserving the very ~~substantial degree of monetary accommodation~~ favourable financing conditions that are necessary to secure a sustained convergence of inflation rates towards levels below, but close to, 2% over the medium term. ~~Together with the sizeable volume of past purchases and forthcoming reinvestments, it ensures that financial conditions in the euro area will remain very favourable, which continues to be crucial to achieve our objective. In particular, the extension of our purchases over a longer horizon allows for a more sustained market presence and, therefore, a more lasting transmission of our stimulus~~ Borrowing conditions for firms and households continue to benefit from the pass-through of our measures. ~~This calibration reflects the moderate~~As expected, headline inflation has increased lately, largely owing to base effects in energy prices, but ~~firming recovery of the euro area economy and still subdued~~ underlying ~~inflationary~~inflation pressures~~.~~ remain subdued. The Governing Council will ~~closely monitor the evolution of the~~continue to look through changes in HICP inflation if judged to be transient and to have no implication for the medium-term outlook for price stability~~ and, if~~.

A very substantial degree of monetary accommodation is needed for euro area inflation pressures to build up and support headline inflation in the medium term. If warranted to achieve its objective, the Governing Council will act by using all the instruments available within its mandate. In particular, if the outlook becomes less favourable, or if financial conditions become inconsistent with further progress towards a sustained adjustment in the path of inflation, we stand ready to increase our asset purchase programme in terms of size and/or duration.

Let me now explain our assessment in greater detail, starting with the~~-~~ economic analysis. ~~Real GDP in the euro~~Euro area real GDP increased by 0.3%, quarter on quarter, in the third quarter of 2016, ~~following~~ after recording a similar pace of growth in the second quarter. Incoming data, notably survey results, point to ~~a continuation of the~~somewhat stronger growth ~~trend~~ in the ~~fourth~~last quarter of 2016. Looking ~~further~~ ahead, we expect the economic expansion to ~~proceed at a moderate but firming pace.~~firm further. The pass-through of our monetary policy measures ~~to the real economy~~ is supporting domestic demand and ~~has facilitated~~facilitating the ongoing deleveraging~~. Improvements in corporate profitability and~~ process. The very favourable financing conditions and improvements in corporate profitability continue to promote ~~a~~the recovery in investment. Moreover, sustained employment gains, which are also benefiting from past structural reforms, provide support for private consumption via increases in households' real disposable income~~ and private consumption.~~. At the same time, there are ~~indications~~signs of a somewhat stronger global recovery. However, economic growth in the euro area is expected to be dampened by a sluggish pace of implementation of structural reforms and remaining balance sheet adjustments in a number of sectors. The risks surrounding the euro area growth outlook remain tilted to the downside and relate predominantly to global factors.

~~This assessment is broadly reflected in the December 2016 Eurosystem staff macroeconomic projections for the euro area, which foresee annual real GDP increasing by 1.7% in 2016 and 2017, and by 1.6% in 2018 and 2019. Compared with the September 2016 ECB staff macroeconomic projections, the outlook for real GDP growth is broadly unchanged. The risks surrounding the euro area growth outlook remain tilted to the downside.~~

According to ~~Eurostat's flash estimate~~Eurostat, euro area annual HICP inflation ~~in~~ increased markedly from 0.6% in November 2016 ~~was 0.6%, up further from 0.5~~to 1.1% in ~~October and 0.4% in September.~~December. This reflected ~~to~~mainly a ~~large extent an~~strong increase in annual energy inflation, while there are no signs yet of a convincing upward trend in underlying inflation. Looking ahead, on the basis of current oil futures prices, headline inflation ~~rates are~~is likely to pick up ~~significantly~~ further ~~at the turn of the year, mainly owing to base effects~~in the near term, largely reflecting movements in the annual rate of change of energy prices. ~~Supported~~However, measures of underlying inflation are expected to rise more gradually over the medium term, supported by our monetary policy measures, the expected economic recovery and the corresponding gradual absorption of slack~~, inflation rates should increase further in 2018 and 2019.~~.

~~This pattern is also reflected in the December 2016 Eurosystem staff macroeconomic projections for the euro area, which foresee annual HICP inflation at 0.2% in 2016, 1.3% in 2017, 1.5% in 2018 and 1.7% in 2019. By comparison with the September 2016 ECB staff macroeconomic projections, the outlook for headline HICP inflation is broadly unchanged.~~

Turning to the monetary analysis, broad money (M3) ~~growth moderated in October 2016~~continues to expand at a robust pace, with its annual rate of growth ~~decreasing~~increasing to 4.8% in November 2016, up from 4~~%, after 5.1~~.4% in ~~September~~October. As in previous months, annual growth in M3 was mainly supported by its most liquid components, with the narrow monetary aggregate M1 expanding at an annual rate of 8.7~~.9~~% in November, up from 8.0% in October~~, after 8.4% in September~~.

Loan dynamics followed the path of gradual recovery observed since the beginning of 2014. The annual growth rate of ~~change of~~ loans to non-financial corporations ~~increased to~~was 2.2% in November 2016, after 2.1% in ~~October 2016, from 2.0% in~~ the previous month. The annual growth rate of loans to households ~~remained at~~was 1.9% in November, after 1.8~~%.~~% in October. Although developments in bank credit 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 monetary policy measures put in place since June 2014 are significantly supporting borrowing conditions for firms and households and thereby credit flows across the euro area. The euro area bank lending survey for the fourth quarter of 2016 indicates that credit standards for loans to enterprises are broadly stabilising, while loan demand has continued to expand at a robust pace across all loan categories.

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 take today's monetary policy decisions so as to preserve the~~for a continued very substantial ~~amount~~degree of monetary ~~support that is necessary in order~~accommodation to secure a sustained 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, in~~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 level. The implementation of structural reforms ~~in particular~~ needs to be substantially stepped up to increase resilience, reduce structural unemployment and boost investment, productivity and potential output growth in the euro area. Structural reforms are necessary in all euro area countries. ~~The focus should be on actions to raise productivity and~~In particular, reforms are needed to improve the business environment, including the provision of an adequate public infrastructure~~, which are vital to increase investment and boost job creation. The~~. In addition, the enhancement of current investment initiatives, progress on the capital markets union and reforms that will improve the resolution of non-performing loans~~ will also contribute positively to this objective. In an environment of accommodative monetary policy, the swift and effective implementation of structural reforms will also make the euro area more resilient to global shocks. Fiscal policies~~, are a priority. **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 remains crucial to ensure confidence in the fiscal framework. At the same time, it is essential that all countries intensify efforts towards achieving a more growth-friendly composition of fiscal policies.

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