CENTRAL BANKS

Slight change in ECB wording

Agustín García / Juan Navarro / Cristina Varela

- **The ECB is more optimistic regarding the growth outlook.**
- **Inflation is revised significantly up this year to 1.7% YoY on increasing energy prices, but the ECB barely changes its broad view on core inflation.**
- **They still maintain a dovish bias, but they introduce a small tweak that could be the prelude of additional changes in the coming months.**

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 (GC) confirmed the measures taken last December, i.e. reducing the monthly purchases to EUR 60 bn as from next month until December 2017. Moreover, the GC did not discuss about another round of TLTROs, as they judge that at the current juncture it is not necessary.

The ECB is **more optimistic regarding the growth outlook than three months ago,** as they see a more broad-based recovery at a steady and robust pace. The **Staff macroeconomic projections do not substantially change the ECB assessment on the outlook for the eurozone** as compared to the previous one of three months ago. **GDP growth is revised slightly up** (by 0.1pp) in both 2017 to 1.8% and in 2018 to 1.7%, while the forecast for 2018 remains at 1.6%.

More importantly, **while risks** continue to be tilted to the downside and relate predominantly to global factors, they **are seen as less pronounced** than three months ago -a message that Mr. Draghi emphasized during the Q&A session.

However, **regarding inflation, the broad assessment remains unchanged**, as the underlying pressures remain subdued with **"no signs yet of a convincing upward trend"**. In this regard, Mr. Drahi reiterated that wage dynamics are the key variable to monitor. **Inflation is revised significantly up this year** (by 0.4pp to 1.7% YoY) **on account of increasing energy and food prices over recent months, but this does not change the ECB broad view on prices** as the rapid increase this year should be temporary and is consistent with minor changes in the projections over the forecast horizon, that remain below the ECB target (1.6% in 2018 and 1.7% in 2019). **Importantly**, t**he projection of a gradual increase in core inflation remains broadly unchanged** (1.1% in 2017, 1.5% in 2018 and 1.8% in 2019).

Regarding the forward guidance, **they still maintain a dovish bias**, as they "expect interest rates to remain at present or lower levels for an extended period of time, and well past the horizon of our net asset purchases". **However**, in line with a more benign growth outlook and the decreasing probability of negative scenarios, **a small tweak was introduced in the statement** as they drop the sentence *"If warranted to achieve its objective, the Governing Council will act by using all the instruments available within its mandate"* from the statement. In fact, Mr. Draghi argued that **the urgency to take further action has diminished.** In our view, **this could be a small step** or the prelude **to additional changes** in the ECB´s forward guidance **in the coming months.**

Regarding its **exit strategy and**, more specifically, the question if the ECB may increase interest rates before QE tapering ends, Mr. Draghi preferred do not speculate and he adhered to the statement.**The ECB recognized the existence of distortions at some bond market segments** (namely short-term German bonds) **that are being monitored closely.** Draghi pointed out three factors that could have been behind current distortions, i.e. the effect of safe-haven flows towards quality assets; the fact that short-term bonds are a highly liquid asset, similar to the deposit facility, for institutions that can not get access the facility and, finally, the Asset Purchases Programme.

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, ~~19 January~~9 March 2017

Ladies and gentlemen, ~~first of all let me wish you a Happy New Year. The~~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.
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, 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~~this month 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. The net purchases will be made alongside reinvestments of the principal payments from maturing securities purchased under the APP.

~~The Governing Council today also decided on further details of how the Eurosystem will buy assets with yields below the interest rate on the deposit facility under its public sector purchase programme. These decisions will be published in a separate press release at 15.30 CET.~~

~~The~~Our monetary policy ~~decisions taken in December 2016~~measures have ~~succeeded in preserving~~continued to preserve the very 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. ~~Borrowing~~Their ongoing pass-through to the borrowing conditions for firms and households ~~continue to benefit from the pass-through~~ benefits credit creation and supports the steadily firming recovery of ~~our measures. As expected, headline~~the euro area economy. Sentiment indicators suggest that the cyclical recovery may be gaining momentum. Headline inflation has again increased ~~lately~~, largely ~~owing to base effects in~~on account of rising energy ~~prices, but~~and food price inflation. However, underlying inflation pressures continue to remain subdued. 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.

A very substantial degree of monetary accommodation is still needed for ~~euro area~~underlying 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~~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. Euro area real GDP increased by 0.~~3~~4%, quarter on quarter, in the ~~third~~fourth quarter of 2016, ~~after recording~~following a similar pace of growth in the ~~second~~third quarter. Incoming data, notably survey results, ~~point to somewhat stronger growth in the last quarter of 2016. Looking ahead, we~~

~~expect the~~ increase our confidence that the ongoing economic expansion will continue to firm ~~further~~and broaden. The pass-through of our monetary policy measures is supporting domestic demand and ~~facilitating~~facilitates the ongoing deleveraging process. ~~The~~The recovery in investment continues to be promoted by very favourable financing conditions and improvements in corporate profitability ~~continue to promote the recovery in investment.~~. Moreover, ~~sustained~~rising employment ~~gains~~, which ~~are~~is also benefiting from past structural reforms, ~~provide support for private consumption via increases in~~ is having a positive impact on households' real disposable income~~. At the same time~~, thereby providing support for private consumption. Also, there are signs of a somewhat stronger global recovery~~.~~ and increasing global trade. 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~~adjustment needs in a number of sectors.

This assessment is broadly reflected in the March 2017 ECB staff macroeconomic projections for the euro area, which foresee annual real GDP increasing by 1.8% in 2017, by 1.7% in 2018 and by 1.6% in 2019. Compared with the December 2016 Eurosystem staff macroeconomic projections, the outlook for real GDP growth has been revised upwards slightly in 2017 and 2018. The risks surrounding the euro area growth outlook have become less pronounced, but remain tilted to the downside and relate predominantly to global factors.

According to ~~Eurostat~~Eurostat's flash estimate, euro area annual HICP inflation increased ~~markedly~~ further to 2.0% in February, up from ~~0.6% in November~~1.8% in January 2017 and 1.1% in December 2016 ~~to 1.1% in December.~~. This reflected mainly a strong increase in annual energy and unprocessed food price inflation, ~~while there are~~with no signs yet of a convincing upward trend in underlying inflation. ~~Looking ahead, on the basis of current oil futures prices, headline~~ Headline inflation is likely to ~~pick up further~~remain at levels close to 2% in the ~~near term~~coming months, largely reflecting movements in the annual rate of change of energy prices. ~~However, measures~~Measures of underlying inflation, however, have remained low and are expected to rise ~~more~~only gradually over the medium term, supported by our monetary policy measures, the expected continuing economic recovery and the corresponding gradual absorption of slack.

This pattern is also reflected in the March 2017 ECB staff macroeconomic projections for the euro area, which foresee annual HICP inflation at 1.7% in 2017, 1.6% in 2018 and 1.7% in 2019. By comparison with the December 2016 Eurosystem staff macroeconomic projections, the outlook for headline HICP inflation has been revised upwards significantly for 2017 and slightly for 2018, while remaining unchanged for 2019. The staff projections are conditional on the full implementation of all our monetary policy measures.

Turning to the ~~-~~ monetary analysis, broad money (M3) continues to expand at a robust pace, with ~~its~~an annual rate of growth ~~increasing to~~of 4.~~8~~9% in ~~November~~January 2017, after 5.0% in December 2016~~, up from 4.4% in 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~~4% in ~~November, up from~~January 2017, after 8.~~0~~8% in ~~October~~December 2016.

Loan dynamics followed the path of gradual recovery observed since the beginning of 2014. The annual growth rate of loans to non-financial corporations was 2.~~2~~3% in ~~November 2016, after 2.1%~~January 2017, as in the previous month. The annual growth rate of loans to households was ~~1.9~~2.2% in ~~November~~January 2017, after ~~1.8~~2.0% in ~~October~~December 2016. 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 for a continued very substantial degree of monetary 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.~~ 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.~~ to strengthening economic growth. The implementation of structural reforms~~-~~ needs to be substantially stepped up to increase resilience, reduce structural unemployment and boost ~~investment, productivity and~~ potential output growth~~ in~~. Against the ~~euro area. Structural reforms are~~ background of overall limited implementation of country-specific recommendations in 2016, greater reform effort is necessary in all euro area countries~~. In particular, reforms are needed to improve the business environment, including the provision of an adequate public infrastructure. 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, are a priority.~~ ~~**Fiscal**~~ in 2017. Regarding **fiscal** policies~~ should also support the economic recovery, while remaining in compliance with the fiscal rules of the European Union. Full~~, all countries should intensify efforts towards achieving a more growth-friendly composition of public finances. A full and consistent implementation of the Stability and Growth Pact and of the macroeconomic imbalances procedure over time and across countries remains crucial to ensure confidence in the ~~fiscal~~EU's governance 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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