Global Economy

ECB, the real challenge is yet to come

El País (Spain)

Sonsoles Castillo

Last Thursday the European Central Bank (ECB) announced that it was ending its asset purchase programme or APP, better known as QE or quantitative easing, four years after it had come into effect. With the benefit of hindsight and the experience of the United States, here are some reflections brought about by the announcement,

In the first place, it is undoubtedly good news, in that the euro zone economy no longer needs this stimulus. In these past four years the ECB has bought €2.6 billion worth of debt (23% of GDP) through the APP, which has proved an effective instrument in avoiding the risk of deflation in the euro zone. Secondly, the announcement passed completely unnoticed by the markets, despite its marking a milestone in the process of monetary normalisation. This was thanks to the effective communication of the ECB, which has been carefully laying the groundwork for the past year. And thirdly, although this brings us a little nearer to a normal monetary situation, there is still a long way to go.

The end of QE is just the first step in a process that will be long drawn out. After all, the ECB still has to dismantle a raft of non-conventional measures rolled out during the crisis, encompassing in particular the policy of providing (long-term) liquidity to the financial system, and it also still has to increase interest rates, which are currently negative, not to mention shrinking its enormous balance sheet.

To give some idea of how much remains to be done, here are a few figures. As regards liquidity, the euro zone banking system responded to the last long-term auctions en masse, bidding for more than €700 billion (to be returned between 2020 and 2021, unless the ECB extends the auctions, which seems very likely). As for interest rates, let us not forget that the ECB cut them to less than zero (to as low as -0.40%). So there is a long way to go before rates return to “normal”.

To the extent that the policy of the US Federal Reserve can serve as a reference as to how long this process may last, although the situation there can certainly not be extrapolated to ours due to the differences between the two jurisdictions, we may be looking at four to five years, since the Fed brought an end to QE in October 2014 and it looks as though the top of the interest rate cycle will be reached in 2019. If this turns out to be the case, the challenge for the ECB will be a daunting one, because it will probably have to face the next phases of the monetary normalisation process just as the economy is slowing down. It will be interesting to see how the new president of the ECB and the new Governing Council manage this.

DISCLAIMER

This document has been prepared by BBVA Research Department. It is provided for information purposes only and expresses data, opinions and estimates at the date of issue of the report, prepared by BBVA or obtained from or based on sources we consider to be reliable, but not independently verified by BBVA. Therefore, BBVA offers no warranty, either express or implicit, regarding their accuracy, completeness or correctness.

Estimates this document may contain have been made in accordance with generally accepted methodologies and should be considered as forecasts or projections. Results obtained in the past, whether positive or negative, are no guarantee of future performance.

This document and its contents are subject to changes without prior notice depending on variables such as the economic context or market fluctuations. BBVA is not responsible for updating these contents or for giving notice of such changes.

BBVA accepts no liability for any loss, direct or indirect, that may result from the use of this document or its contents.

This document and its contents do not constitute an offer, invitation or solicitation to purchase, divest or enter into any interest in financial assets or instruments. Nor shall this document or its contents form the basis of any contract, commitment or decision of any kind.

With regard to investment in financial assets related to economic variables this document may cover, readers should be aware that in no circumstances should they base their investment decisions on the information contained in this document. Persons or entities offering investment products to these potential investors are legally required to provide the information needed for them to take an appropriate investment decision.

CONTACT DETAILS:
BBVA Research: Azul Street. 4. La Vela Building – 4th and 5th floor. 28050 Madrid (Spain). Tel.:+34 91 374 60 00 and +34 91 537 70 00 / Fax: +34 91 374 30 25 - bbvaresearch@bbva.com www.bbvaresearch.com