CHAO & COMPANY
FIDUCIA PERPETUA

July 25, 2019, ECB Press Conference – What has changed from June 6, 2019?

Summary

- Keep ECB interest rates unchanged and expect them to remain at their present or lower levels at least through Q2 of 2020. (**unchanged**)
- Intends to continue reinvesting, in full, the principal payments from maturing securities purchased under the asset purchase programme for an extended period of time past the date when we start raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation. (**unchanged)**
- ECB underlined the need for a <u>highly accommodative stance</u> of monetary policy for <u>a prolonged period of time</u>, as <u>inflation rates</u>, both realised and projected, have been <u>persistently below levels that are in line with its aim</u>. If the medium-term inflation outlook continues to fall short of ECB's aim, it is determined to act, in line with its commitment to <u>symmetry</u> in the inflation aim. It stands ready to adjust all of its instruments to ensure that inflation moves towards its aim in a sustained manner. (**new**)
- Relevant Eurosystem Committees tasked with examining options, including ways to reinforce its forward guidance on policy rates, the design of a tiered system for reserve remuneration, and options for the size and composition of potential new net asset purchases. **(new)**
- The prolonged presence of uncertainties, related to geopolitical factors, the rising threat of protectionism and vulnerabilities in emerging markets, is dampening economic sentiment, notably in the manufacturing sector. Inflationary pressures remain muted and inflation expectations have declined. A significant degree of monetary stimulus continues to be necessary to ensure that financial conditions remain very favourable and support the euro area expansion. (**new)**
- In order to reap the full benefits from our monetary policy measures, other policy areas must contribute more decisively to raising the longer-term growth potential and reducing vulnerabilities. The implementation of **structural reforms** in euro area countries needs to be substantially stepped up to boost euro area productivity and growth potential, reduce structural unemployment and increase resilience. (**unchanged**)

8460 Tyco Road, Suite E, Vienna, Virginia 22182
T: 703.847.4380 F: 703.847.4384 www.ChaoCo.com

PRESS CONFERENCE

Mario Draghi, President of the ECB,

Luis de Guindos, Vice-President of the ECB,

Frankfurt am Main, 25 July ~~Vilnius, 6 June~~ 2019

INTRODUCTORY STATEMENT

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 Chairman of the Board Vasiliauskas 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 ~~have conducted a thorough assessment of the economic and inflation outlook, also taking into account the latest staff macroeconomic projections for the euro area. As a result, the Governing Council took the following decisions in the pursuit of its price stability objective.~~

~~First, we~~ decided to keep the **key ECB interest rates** unchanged. We ~~now~~ expect them to remain at their present **or lower** levels at least through the first half of 2020, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to **our aim** ~~levels that are below, but close to, 2%~~ over the medium term.

We ~~Second, we~~ intend to continue reinvesting, in full, the principal payments from maturing securities purchased under the asset purchase programme for an extended period of time past the date when we start raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation.

~~Third, regarding the modalities of the new series of quarterly targeted longer-term refinancing operations (TLTRO III), we decided that the interest rate in each operation will be set at a level that is 10 basis points above the~~

8460 Tyco Road, Suite E, Vienna, Virginia 22182
T: 703.847.4380 F: 703.847.4384 www.ChaoCo.com

~~average rate applied in the Eurosystem's main refinancing operations over the life of the respective TLTRO. For banks whose eligible net lending exceeds a benchmark, the rate applied in TLTRO III will be lower, and can be as low as the average interest rate on the deposit facility prevailing over the life of the operation plus 10 basis points.~~

~~A press release with further details of the terms of TLTRO III will be published at 15:30 CET today.~~

The Governing Council also **underlined the need for a highly** ~~assessed that, at this point in time, the positive contribution of negative interest rates to the~~ accommodative **stance of** monetary policy **for a prolonged period of time, as** ~~stance and to the sustained convergence of~~ inflation **rates, both realised and projected, have been persistently below** ~~is not undermined by possible side effects on bank-based intermediation. However, we will continue to monitor carefully the bank-based transmission channel of monetary policy and the case for mitigating measures.~~

~~Today's monetary policy decisions were taken to provide the monetary accommodation necessary for inflation to remain on a sustained path towards~~ levels that are **in line with its aim. Accordingly, if** ~~below, but close to, 2% over~~ the medium**-term inflation outlook continues to fall short of our aim, the Governing Council is determined to act, in line with its commitment to symmetry in the inflation aim. It therefore stands ready to adjust all of its instruments, as appropriate, to ensure that inflation moves towards its aim in a sustained manner.**

In this context, we have tasked the relevant Eurosystem Committees with examining options, including ways to reinforce our forward guidance on policy rates, mitigating measures, such as the design of a tiered system~~.~~ ~~Despite the somewhat better than expected data~~ **for reserve remuneration, and options for the size and composition of potential new net asset purchases**.

Incoming ~~the first quarter, the most recent~~ information **since the last Governing Council meeting in early June** indicates that **while further employment gains and increasing wages continue to underpin the resilience of the economy, softening global growth dynamics and weak international trade are still weighing** ~~global headwinds continue to weigh~~ on the euro area outlook. **Moreover, the** ~~The~~ prolonged presence

8460 Tyco Road, Suite E, Vienna, Virginia 22182
T: 703.847.4380 F: 703.847.4384 www.ChaoCo.com

of uncertainties, related to geopolitical factors, the rising threat of protectionism and vulnerabilities in emerging markets, is **dampening** ~~leaving its mark on~~ economic sentiment, **notably in**~~.~~

~~At~~ the **manufacturing sector. In this environment, inflationary pressures remain muted** ~~same time, further employment gains and increasing wages continue to underpin the resilience of the euro area economy and gradually rising~~ **and inflation expectations have declined Therefore, a significant degree of monetary stimulus continues to be necessary to** ~~. sector. In this environment, inflationary pressures remain mutedsame time, further employment gains and indicatorsincreasing wages continue to underpin the resilience of the euro area economy and gradually rising inflation expectations have declined. Therefore, a significant degree of monetary stimulus continues to be necessary to . Today's policy measures~~ ensure that financial conditions ~~will~~ remain very favourable **and support**~~,~~ ~~supporting~~ the euro area expansion, the ongoing build-up of domestic price pressures and, thus, headline inflation developments over the medium term. ~~Looking ahead, the Governing Council is determined to act in case of adverse contingencies and also stands ready to adjust all of its instruments, as appropriate, to ensure that inflation continues to move towards the Governing Council's inflation aim in a sustained manner.~~

Let me now explain our assessment in greater detail, starting with the **economic analysis**. **Following a rise of 0.2% in the fourth quarter of 2018, euro** ~~Euro~~ area real GDP **increased** ~~rose~~ by 0.4%, quarter on quarter, in the first quarter of 2019**. Incoming** ~~, following an increase of 0.2% in the fourth quarter of 2018. However, incoming~~ economic data and survey information **continue to** point to somewhat weaker growth in the second and third quarters of this year. This **mainly** reflects the ongoing weakness in international trade in an environment of prolonged global uncertainties, which are **particularly affecting** ~~weighing, in particular, on~~ the euro area manufacturing sector. At the same time, **activity levels in** the ~~euro area~~ services and construction sectors are **resilient** ~~showing resilience~~ and the labour market is **still improving** ~~continuing to improve~~. Looking ahead, the euro area expansion will continue to be supported by favourable financing conditions, **further employment gains and rising wages,** the mildly expansionary euro area fiscal stance~~, further employment gains and rising wages,~~ and the ongoing – albeit somewhat slower – growth in global activity.

8460 Tyco Road, Suite E, Vienna, Virginia 22182
T: 703.847.4380 F: 703.847.4384 www.ChaoCo.com

~~This assessment is broadly reflected in the June 2019 Eurosystem staff macroeconomic projections for the euro area. These projections foresee annual real GDP increasing by 1.2% in 2019, 1.4% in 2020 and 1.4% in 2021. Compared with the March 2019 ECB staff macroeconomic projections, the outlook for real GDP growth has been revised up by 0.1 percentage points for 2019 and has been revised down by 0.2 percentage points for 2020 and by 0.1 percentage points for 2021.~~

The risks surrounding the euro area growth outlook remain tilted to the downside, **reflecting** ~~on account of~~ the prolonged presence of uncertainties, related to geopolitical factors, the rising threat of protectionism and vulnerabilities in emerging markets.

Euro ~~According to Eurostat's flash estimate, euro~~ area annual HICP inflation **increased to 1.3% in June 2019, from** ~~was~~ 1.2% in May**, as higher HICP inflation excluding food and energy more than offset** ~~2019, after 1.7% in April, reflecting mainly~~ lower energy ~~and services~~ price inflation. On the basis of current futures prices for oil, headline inflation is likely to decline over the coming months, before rising again towards the end of **the** year. Looking through the recent volatility due to temporary factors, measures of underlying inflation remain generally muted, **Indicators of inflation expectations have declined. While** ~~but~~ labour cost pressures **have strengthened** ~~continue to strengthen~~ and **broadened** ~~broaden~~ amid high levels of capacity utilisation and tightening labour markets **the pass-through of cost pressures to inflation is taking longer than previously anticipated. Over the medium term**~~. Looking ahead,~~ underlying inflation is expected to increase ~~over the medium term~~, supported by our monetary policy measures, the ongoing economic expansion and stronger wage growth.

~~This assessment is also broadly reflected in the June 2019 Eurosystem staff macroeconomic projections for the euro area, which foresee annual HICP inflation at 1.3% in 2019, 1.4% in 2020 and 1.6% in 2021. Compared with the March 2019 ECB staff macroeconomic projections, the outlook for HICP inflation has been revised up by 0.1 percentage points for 2019 and revised down by 0.1 percentage points for 2020.~~

Turning to the **monetary analysis**, broad money (M3) growth stood at 4.**5**~~7~~% in **June** ~~April~~ 2019, after 4.**8**~~6%~~ in **May** ~~March~~. Sustained rates of broad money growth reflect ongoing bank credit creation for the private

8460 Tyco Road, Suite E, Vienna, Virginia 22182
T: 703.847.4380 F: 703.847.4384 www.ChaoCo.com

sector and low opportunity costs of holding M3. The narrow monetary aggregate M1 continues to be the main contributor to broad money growth on the components side.

The annual growth rate of loans to non-financial corporations **remained unchanged at** ~~increased to~~ 3.**8**~~9~~% in **June** ~~April~~ 2019**. Notwithstanding some moderation**~~,~~ from **the peak recorded** ~~3.6%~~ in September 2018, ~~March. Beyond short-term volatility,~~ the annual growth rate of loans to non-financial corporations **continues to be robust.** ~~has moderated somewhat in recent months from its peak in September 2018, reflecting the typical lagged reaction to the slowdown in economic growth observed over the course of 2018.~~ The annual growth rate of loans to households **also remained unchanged** ~~stood~~ at 3.**3**~~4~~% in **June**~~April~~, ~~compared with 3.3% in March~~, continuing its gradual improvement. **Overall, loan growth is still benefiting from historically low bank lending rates. The euro area bank lending survey for the second quarter of 2019 indicates that loan growth continued to be supported by increasing demand across all loan categories. At the same time, credit standards for loans to enterprises tightened in the second quarter amid concerns about the economic outlook, while they remained broadly unchanged for loans for house purchase.**

Our ~~The~~ monetary policy measures ~~taken today~~, including **the forthcoming new series of targeted longer-term refinancing operations** (TLTRO III)~~,~~ will help to safeguard favourable bank lending conditions and will continue to support access to financing, in particular for small and medium-sized enterprises.

To sum up, a **cross-check** of the outcome of the economic analysis with the signals coming from the monetary analysis confirmed that an ample degree of monetary accommodation is still necessary for the continued sustained convergence of inflation to levels that are below, but close to, 2% over the medium term.

In order to reap the full benefits from our monetary policy measures, other policy areas must contribute more decisively to raising the longer-term growth potential and reducing vulnerabilities. The implementation of **structural reforms** in euro area countries needs to be substantially stepped up to ~~increase resilience, reduce structural unemployment and~~ boost euro area productivity and growth potential~~.~~, **reduce structural**

unemployment and increase resilience. The 2019 country-specific recommendations should serve as the relevant signpost. Regarding **fiscal policies**, the mildly expansionary euro area fiscal stance is providing support to economic activity. At the same time, countries where government debt is high need to continue rebuilding fiscal buffers. All countries should reinforce their efforts to achieve a more growth-friendly composition of public finances. Likewise, the transparent and consistent implementation of the European Union's fiscal and economic governance framework over time and across countries remains essential to bolster the resilience of the euro area economy. Improving the functioning of Economic and Monetary Union remains a priority. The Governing Council welcomes the ongoing work and urges further specific and decisive steps to complete the banking union and the capital markets union.

We are now at your disposal for questions.

https://www.ecb.europa.eu/press/pressconf/2019/html/ecb.is190725~547f29c369.en.html

8460 Tyco Road, Suite E, Vienna, Virginia 22182
T: 703.847.4380 F: 703.847.4384 www.ChaoCo.com