TrendMacro

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Data Insights: ECB and Euro Area Economy Monitor

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Today's monetary policy decision: how the language changed from prior meeting

~~27 July~~14 September 2023

Inflation continues to decline but is still expected to remain too high for too long. The Governing Council is determined to ensure that inflation returns to its 2% medium-term target in a timely manner. ~~It therefore~~In order to reinforce progress towards its target, the Governing Council today decided to raise the three key ECB interest rates by 25 basis points.

The rate increase today reflects the Governing Council's assessment of the inflation outlook in light of the incoming economic and financial data, the dynamics of underlying inflation, and the strength of monetary policy transmission. ~~The developments since the last meeting support~~ The September ECB staff macroeconomic projections for the ~~expectation that~~euro area see average inflation ~~will drop further over~~at 5.6% in 2023, 3.2% in 2024 and 2.1% in 2025. This is an upward revision for 2023 and 2024 and a downward revision for 2025. The upward revision for 2023 and 2024 mainly reflects a higher path for energy prices. Underlying price pressures remain high, even though most indicators have started to ease. ECB staff have slightly revised down the ~~remainder of the year but will stay above target for an extended period. While some measures show signs of easing, underlying~~projected path for inflation ~~remains high overall. The past~~excluding energy and food, to an average of 5.1% in 2023, 2.9% in 2024 and 2.2% in 2025. The Governing Council's past interest rate increases continue to be transmitted forcefully~~: financing~~. Financing conditions have tightened ~~again~~further and are increasingly dampening demand, which is an important factor in bringing inflation back to target. With the increasing impact of this tightening on domestic demand and the weakening international trade environment, ECB staff have lowered their economic growth projections significantly. They now expect the euro area economy to expand by 0.7% in 2023, 1.0% in 2024 and 1.5% in 2025.

Based on its current assessment, the Governing Council considers that the key ECB interest rates have reached levels that, maintained for a sufficiently long duration, will make a substantial contribution to the timely return of inflation to the target. The Governing Council's future decisions will ensure that the key ECB interest rates will be set at sufficiently restrictive levels for as long as necessary~~ to achieve a timely return of inflation to the 2% medium-term target.~~. The Governing Council will continue to follow a data-dependent approach to determining the appropriate level and duration of restriction. In particular, ~~its~~the Governing Council's interest rate decisions will~~ continue to~~ be based on its assessment of the inflation outlook in light of the incoming economic and financial data, the dynamics of underlying inflation, and the strength of monetary policy transmission.

~~The Governing Council also decided to set the remuneration of minimum reserves at 0%. This decision will preserve the effectiveness of monetary policy by maintaining the current degree of control over the monetary policy stance and ensuring the full pass-through of the interest rate decisions to money markets. At the same time, it will improve the efficiency of monetary policy by reducing the overall amount of interest that needs to be paid on reserves in order to implement the appropriate stance.~~

~~The details of the change to the remuneration of minimum reserves are provided in a separate press release to be published at 15:45 CET.~~

Key ECB interest rates

The Governing Council decided to raise the three key ECB interest rates by 25 basis points. Accordingly, the interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility will be increased to 4.~~25~~50%, 4.~~50~~75% and ~~3.75~~4.00% respectively, with effect from ~~2 August~~20 September 2023.

Asset purchase programme (APP) and pandemic emergency purchase programme (PEPP)

The APP portfolio is declining at a measured and predictable pace, as the Eurosystem no longer reinvests the principal payments from maturing securities.

As concerns the PEPP, the Governing Council intends to reinvest the principal payments from maturing securities purchased under the programme until at least the end of 2024. In any case, the future roll-off of the PEPP portfolio will be managed to avoid interference with the appropriate monetary policy stance.

The Governing Council will continue applying flexibility in reinvesting redemptions coming due in the PEPP portfolio, with a view to countering risks to the monetary policy transmission mechanism related to the pandemic.

Refinancing operations

As banks are repaying the amounts borrowed under the targeted longer-term refinancing operations, the Governing Council will regularly assess how targeted lending operations and their ongoing repayment are contributing to its monetary policy stance.

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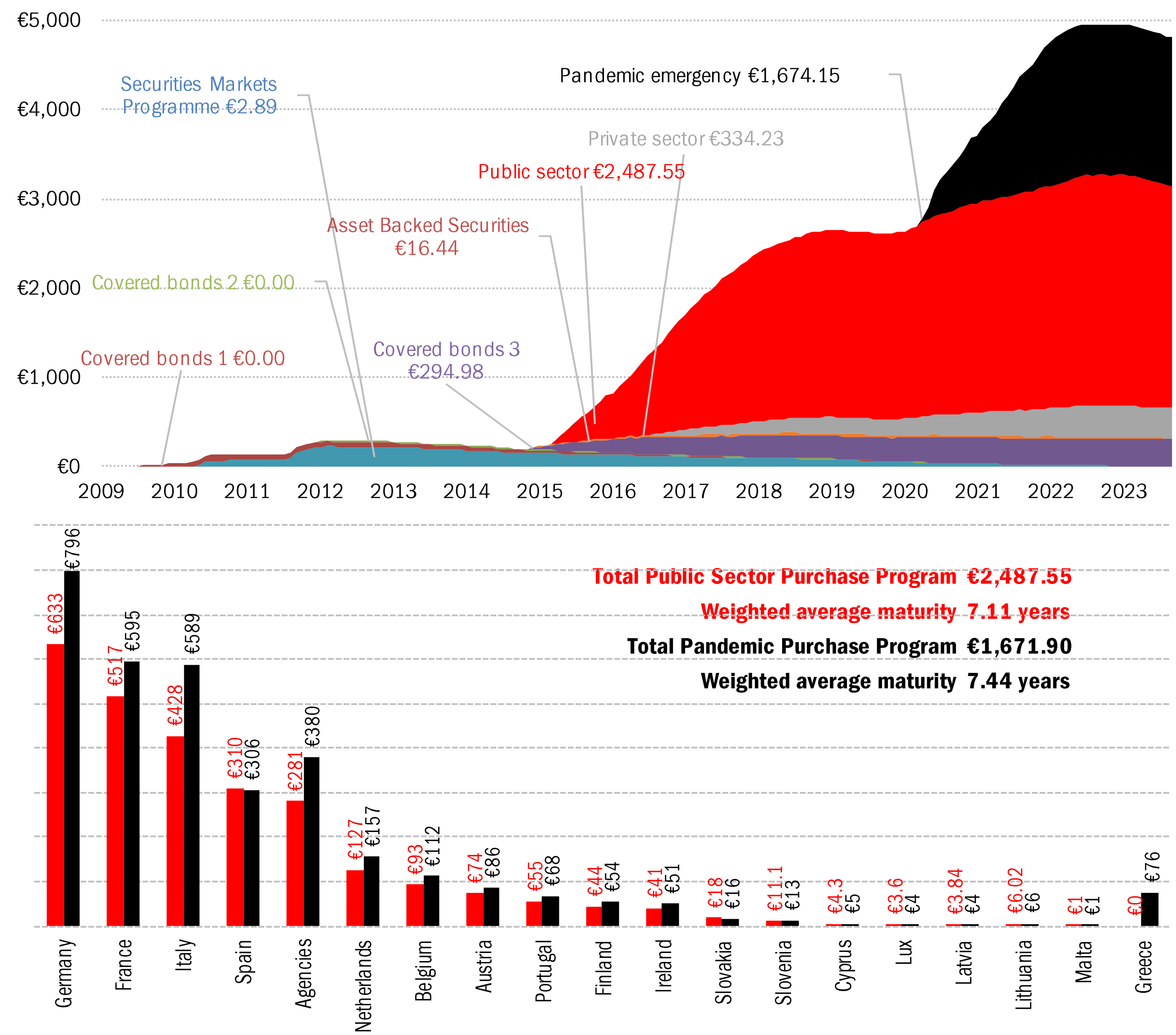
The Governing Council stands ready to adjust all of its instruments within its mandate to ensure that inflation returns to its 2% target over the medium term and to preserve the smooth functioning of monetary policy transmission. Moreover, the Transmission Protection Instrument is available to counter unwarranted, disorderly market dynamics that pose a serious threat to the transmission of monetary policy across all euro area countries, thus allowing the Governing Council to more effectively deliver on its price stability mandate.

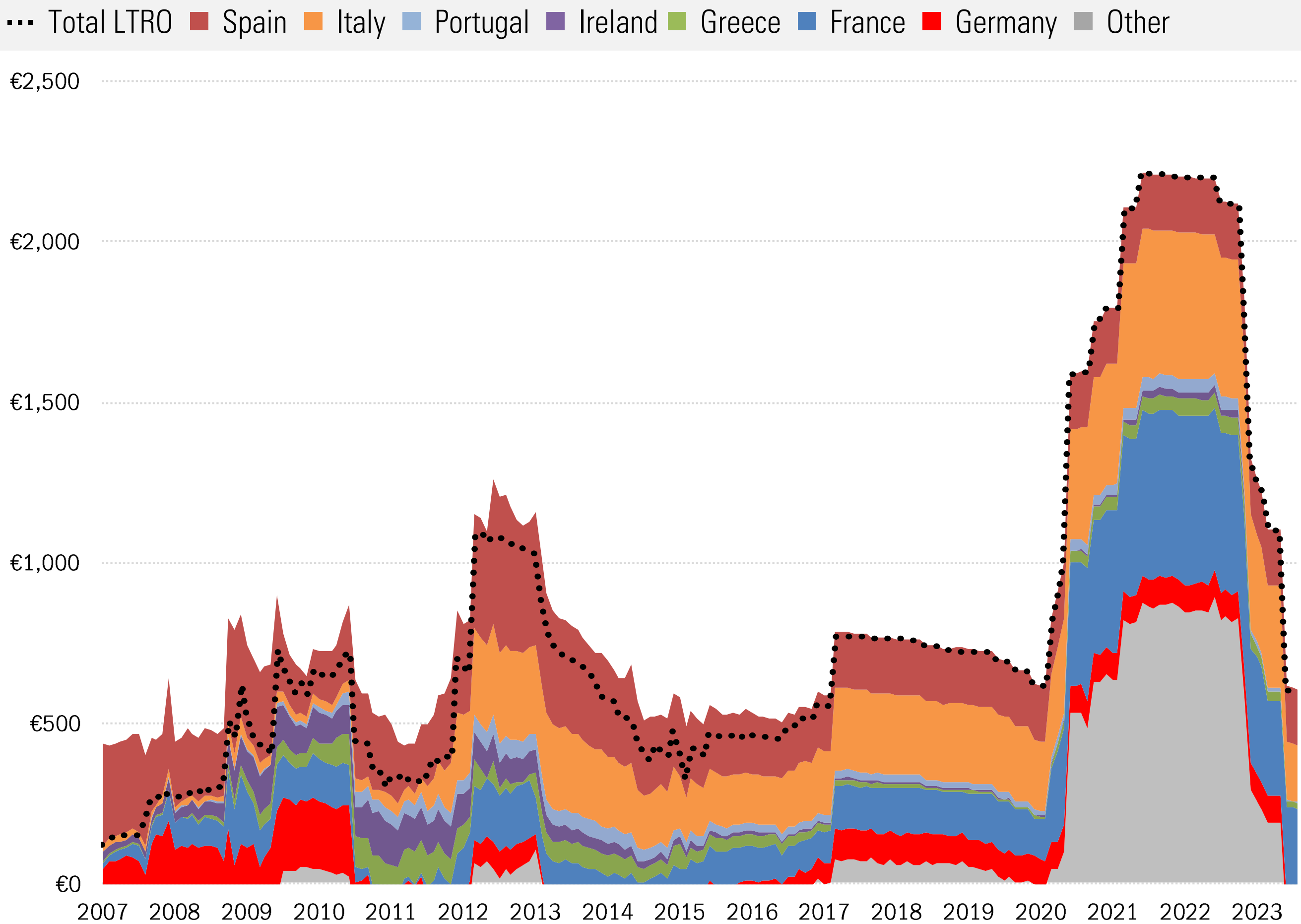
Source: FOMC, TrendMacro analysis

Euro-QE (€ billions)



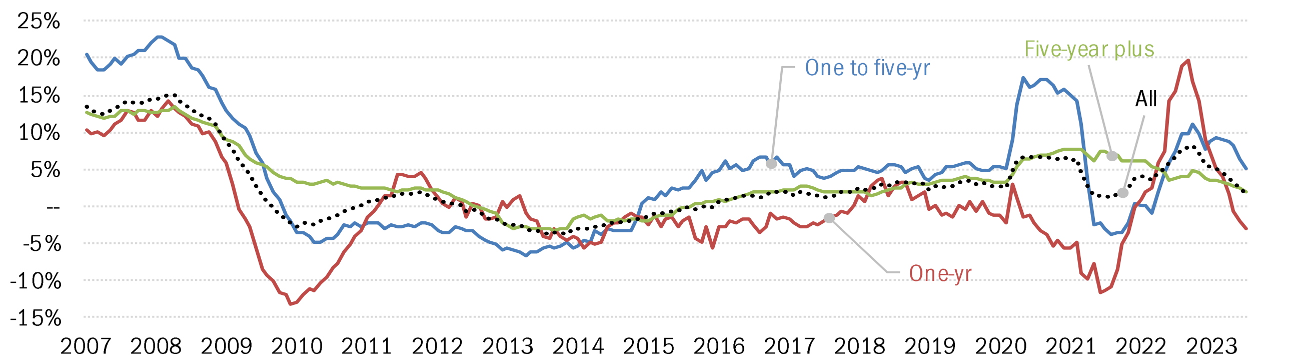
Source: ECB, TrendMacro calculations

Banking system dependency: borrowing from the ECB (€ billions)



Source: ECB, National central banks, TrendMacro calculations

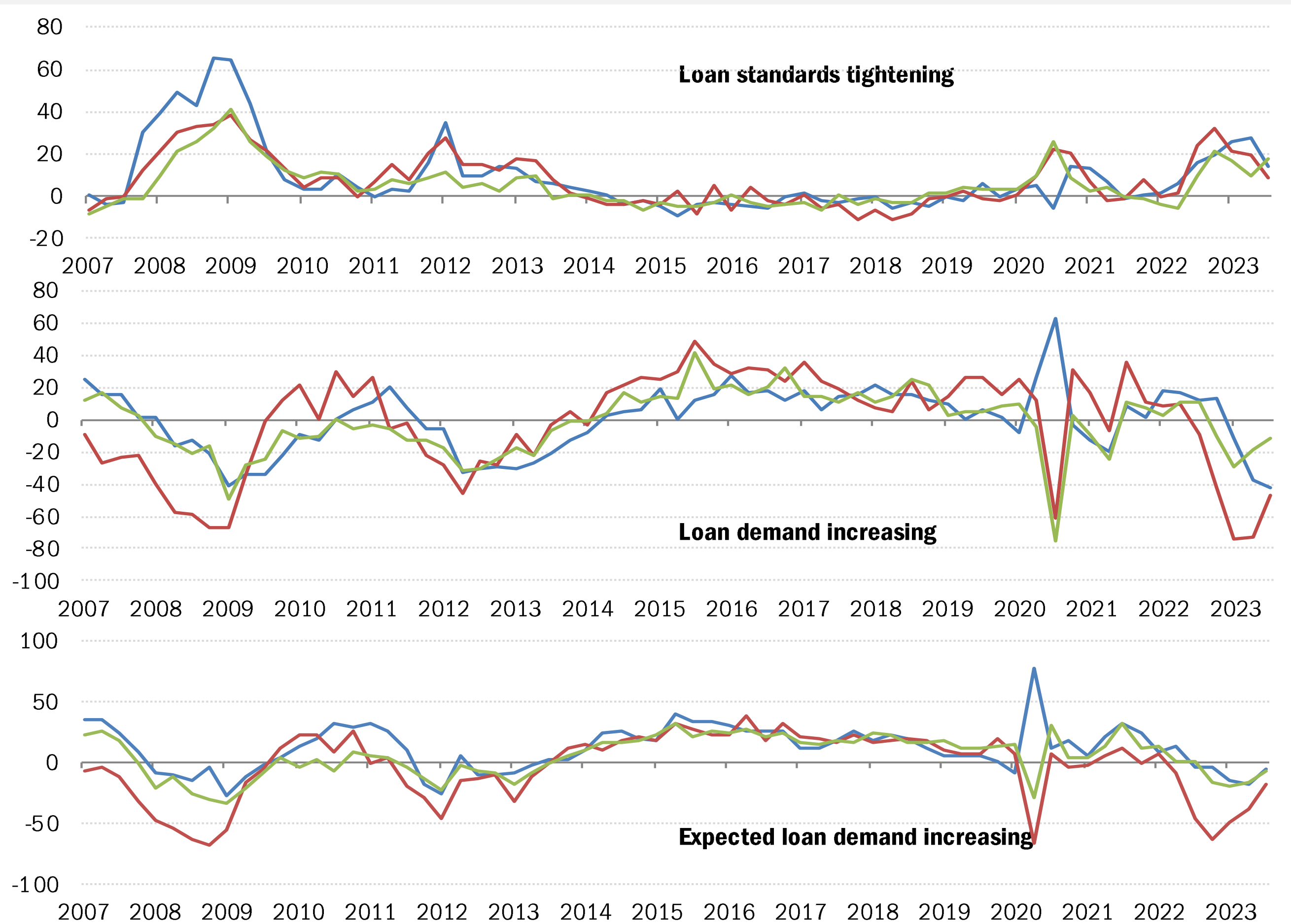
The credit drought: loans to non-financial businesses (YOY growth)



Source: ECB, TrendMacro calculations

Supply and demand for lending: ECB Bank Survey

Net number of banks reporting for: Enterprises, Home mortgage, Consumer

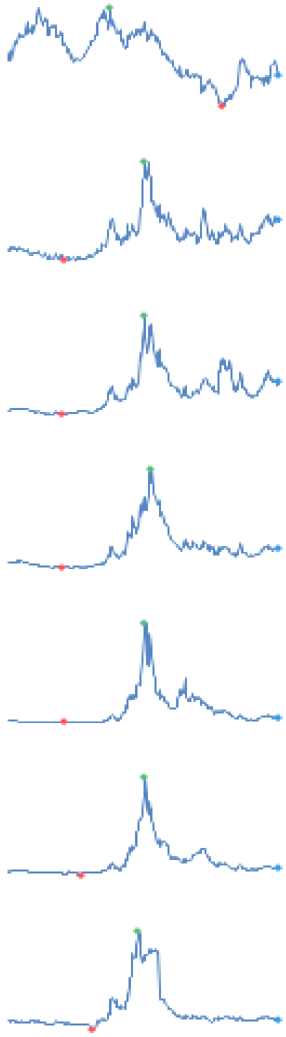


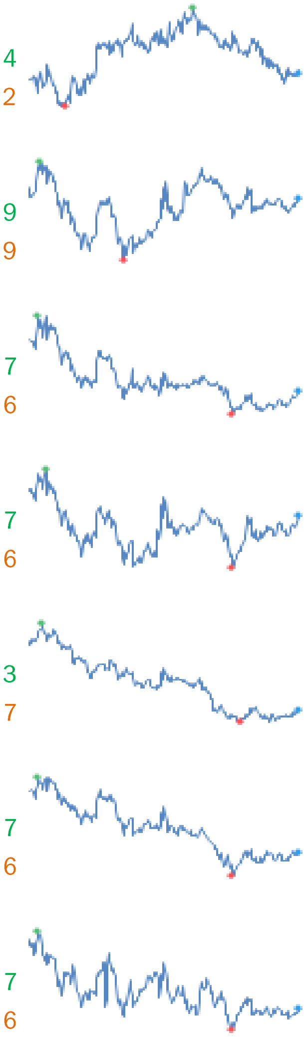
Source: ECB, TrendMacro calculations

Sovereign stress monitor: 10-year bond spreads

· High · Low · Last

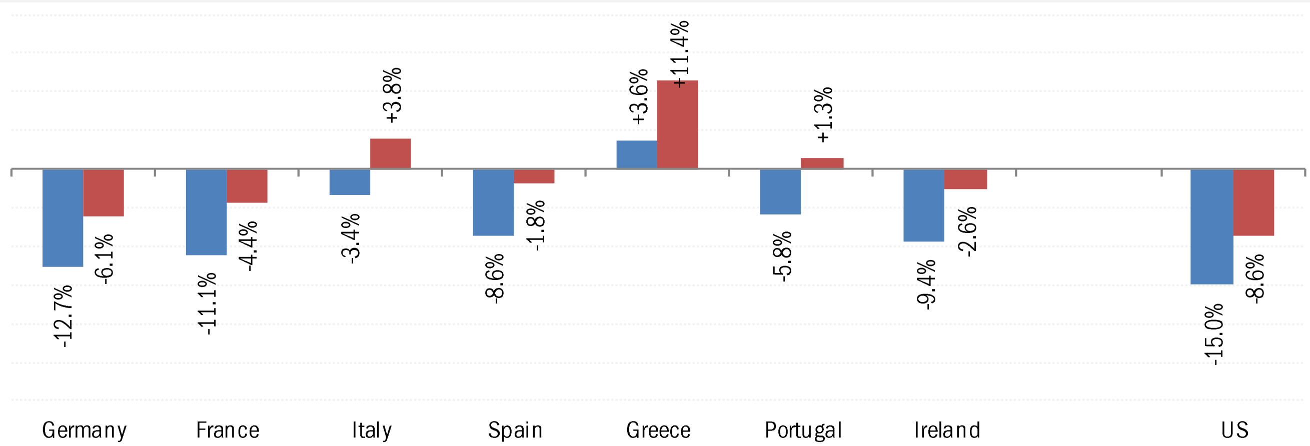
	2000 to present			Trailing 12m	
Germany					
Spread to US	High 0.74%	Dec '08		High -0.98%	Apr 24
Last -1.62%	Low -2.76%	Oct '18		Low -1.96%	Nov 2
France					
Spread to Germany	High 1.32%	Dec '11		High 0.62%	Sep 29
Last 0.54%	Low -0.01%	Jan '05		Low 0.42%	Jan 19
Italy					
Spread to Germany	High 5.28%	Dec '11		High 2.53%	Sep 27
Last 1.79%	Low 0.09%	Nov '04		Low 1.56%	Jun 16
Spain					
Spread to Germany	High 5.52%	Aug '12		High 1.22%	Oct 7
Last 1.07%	Low -0.05%	Nov '04		Low 0.91%	Jun 16
Greece					
Spread to Germany	High 33.13%	Dec '11		High 2.84%	Oct 3
Last 1.40%	Low 0.09%	Jan '05		Low 1.22%	Jun 27
Portugal					
Spread to Germany	High 14.61%	Jan '12		High 1.10%	Sep 27
Last 0.75%	Low -0.54%	Jun '06		Low 0.64%	Jun 16
Ireland					
Spread to Germany	High 8.67%	Jun '11		High 0.62%	Sep 27
Last 0.40%	Low -0.67%	Jun '07		Low 0.35%	Jun 16





10-year sovereign bond total returns, trailing 12-months

🟦 EUR 🟥 USD



Source: Bloomberg, TrendMacro calculations

Labor market in intensive care

ULC: Nominal, quarterly YOY UE: · High 12m pulse: monthly improvement or worsening in rate of change

Source: Eurostat, TrendMacro calculations

Purchasing Manager Indices

Manufacturing	Last	Prev	13-month history	***Services***	Last	Prev	13-month history
Eurozone Aug	43.5	42.7		Eurozone Aug	47.9	50.9	
UK Aug	43.0	45.3		UK Aug	49.5	51.5	
Germany Aug	39.1	38.8		Germany Aug	47.3	52.3	
France Aug	46.0	45.1		France Aug	46.0	47.1	
Italy Aug	45.4	44.5		Italy Aug	48.8	46.4	
Spain Aug	46.5	47.8		Spain Aug	49.3	52.8	
Ireland Aug	50.8	47.0		Ireland Aug	55.0	56.7	
Netherlands Aug	45.9	45.3					
Austria Aug	40.6	38.8					
Greece Aug	52.9	53.5					
Czech Rep Aug	42.9	41.4					

Source: Markit, TrendMacro calculations

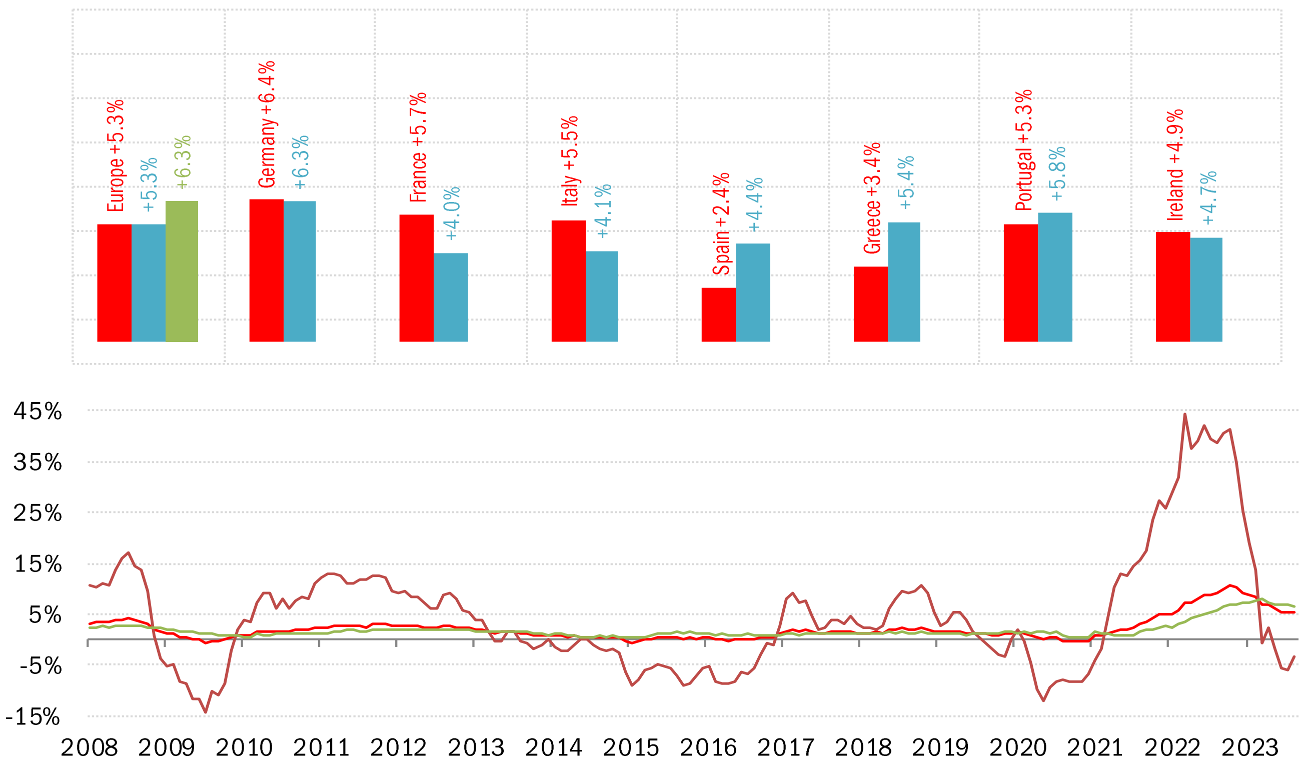
Regional currency flight

Euro vs Swiss franc   SNB FX reserves

Source: Bloomberg, TrendMacro calculations

Euro area consumer inflation, year on year

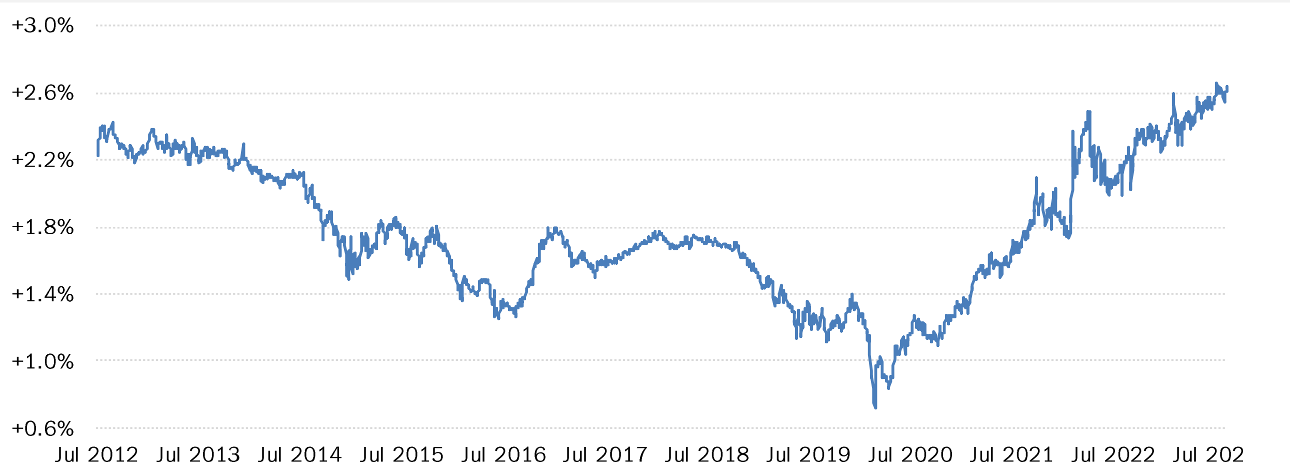
Country: Headline Ex-food and energy Ex-energy Euro area: Headline Energy Ex-energy



Source: Eurostat, TrendMacro calculations

Draghi's old dashboard:
Swap-implied inflation expectations since “Whatever it takes”

5-year inflation-swap rate, 5 years forward



Source: Bloomberg, TrendMacro calculations