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## Data Insights: ECB and Euro Area Economy Monitor

Thursday, September 12, 2024

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

*18 July 12 September 2024*

The Governing Council today decided to keep lower the ~~three key ECB interest rates unchanged~~. The incoming information broadly supports deposit facility rate – the rate through which it steers the monetary policy stance – by 25 basis points. Based on the Governing Council's previous updated assessment of the ~~medium-term~~ inflation outlook. ~~While some measures, the dynamics~~ of underlying inflation ~~tick~~ and the strength of monetary policy transmission, it is now appropriate to take another step in moderating the degree of monetary policy restriction.

Recent inflation data have come in broadly as expected, and the latest ECB staff projections confirm the previous inflation outlook. Staff see headline inflation averaging 2.5% in 2024, 2.2% in 2025 and 1.9% in 2026, as in the June projections. Inflation is expected to rise again in the latter part of this year, partly because previous sharp falls in energy prices will drop out of the annual rates. Inflation should then decline towards our target over the second half of next year. For core inflation, the projections for 2024 and 2025 have been revised up in May owing to one-off factors, most measures were either stable or edged down in June. In line with expectations, the inflationary slightly, as services inflation has been higher than expected. At the same time, staff continue to expect a rapid decline in core inflation, from 2.9% this year to 2.3% in 2025 and 2.0% in 2026.

Domestic inflation remains high as wages are still rising at an elevated pace. However, labour cost pressures are moderating, and profits are partially buffering the impact of high wage growth has been buffered by profits. Monetary policy is keeping financing higher wages on inflation. Financing conditions remain restrictive. At the same time, and economic activity is still subdued, reflecting weak private consumption and investment. Staff project that the economy will grow by 0.8% in 2024, rising to 1.3% in 2025 and 1.5% in 2026. This is a slight downward revision compared with the June projections, mainly owing to a weaker contribution from domestic price pressures are still high, services inflation is elevated and headline inflation is likely to remain above the target well into next year. demand over the next few quarters.

The Governing Council is determined to ensure that inflation returns to its 2% medium-term target in a timely manner. It will keep policy rates sufficiently restrictive for as long as necessary to achieve this aim. The Governing Council will continue to follow a data-dependent and meeting-by-meeting approach to determining the appropriate level and duration of restriction. In particular, its interest rate decisions will 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 is not pre-committing to a particular rate path.

As announced on 13 March 2024, some changes to the operational framework for implementing monetary policy will take effect from 18 September. In particular, the spread between the interest rate on the main refinancing operations and the deposit facility rate will be set at 15 basis points. The spread between the rate on the marginal lending facility and the rate on the main refinancing operations will remain unchanged at 25 basis points.

#### Key ECB interest rates

~~The~~The Governing Council decided to lower the deposit facility rate by 25 basis points. The deposit facility rate is the rate through which the Governing Council steers the monetary policy stance. In addition, as announced on 13 March 2024 following the operational framework review, the spread between the interest rate on the main refinancing operations and the ~~interest rates on the deposit facility rate~~ will be set at 15 basis points. The spread between the rate on the marginal lending facility and the ~~deposit facility rate on the main refinancing operations~~ will remain unchanged at 4.25%, 4.25 basis points. Accordingly, the deposit facility rate will be decreased to 3.50%. The interest rates on the main refinancing operations and 3.75% the marginal lending facility will be decreased to 3.65% and 3.90% respectively. The changes will take effect from 18 September 2024.

#### 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.

The Eurosystem no longer reinvests all of the principal payments from maturing securities purchased under the PEPP, reducing the PEPP portfolio by €7.5 billion per month on average. The Governing Council intends to discontinue reinvestments under the PEPP at the end of 2024.

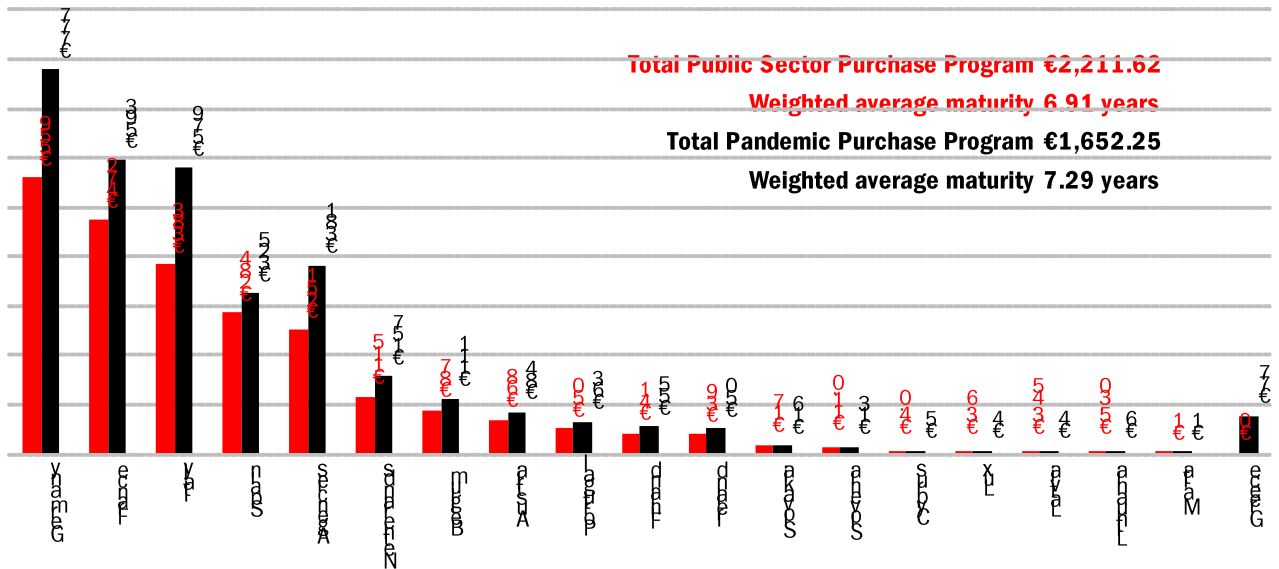
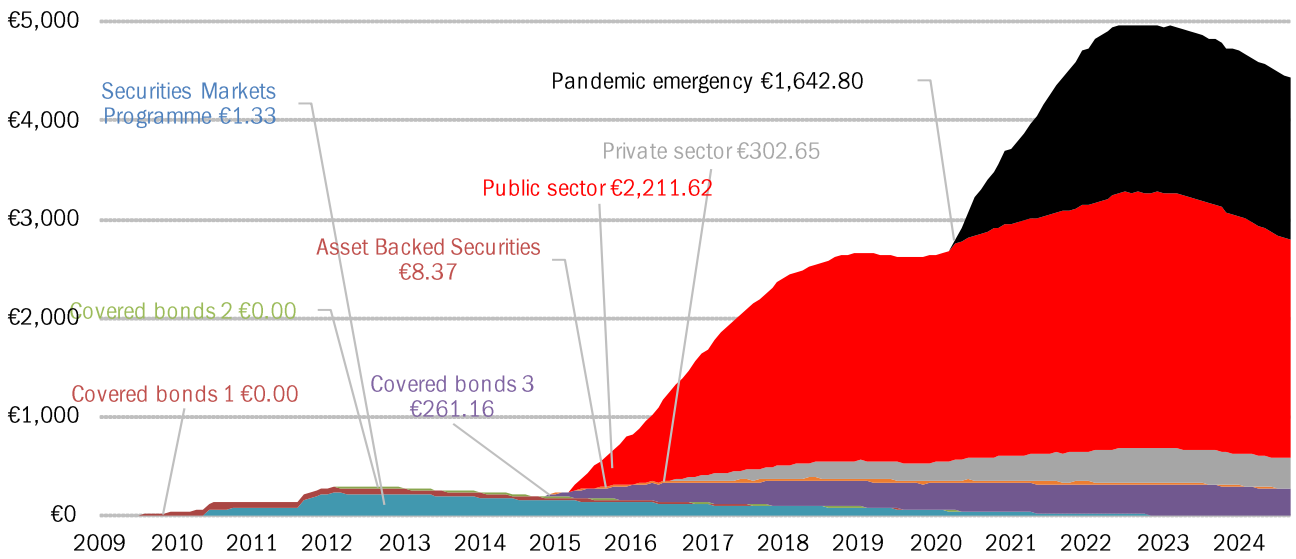
The Governing Council will continue applying flexibility in reinvesting redemptions coming due in the PEPP portfolio, with a view to countering risks to the monetary policy transmission mechanism related to the pandemic.

#### 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.

Source: ECB, TrendMacro analysis

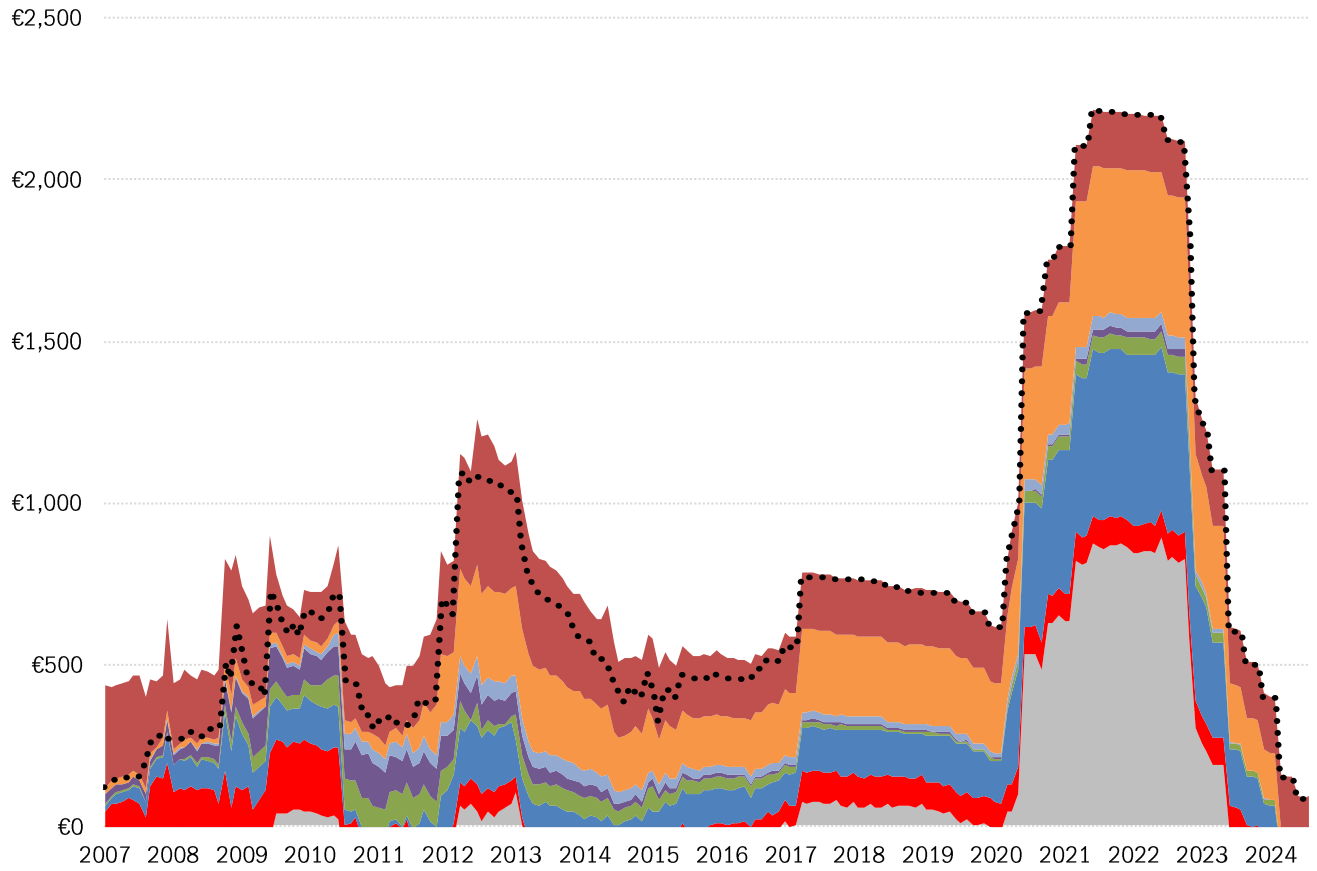
# Euro-QE (€ billions)



Source: ECB, TrendMacro calculations

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

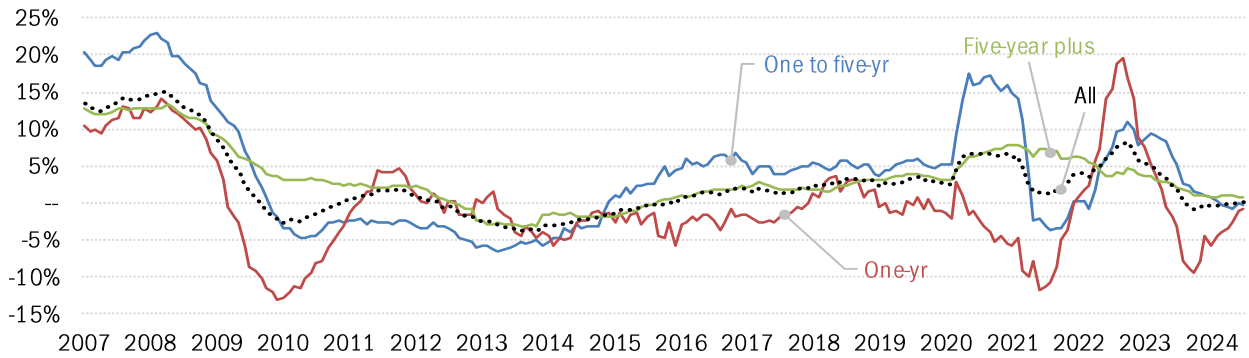
--- Total LTRO Spain Italy Portugal Ireland Greece France Germany Other



Source: ECB, National central banks, TrendMacro calculations

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

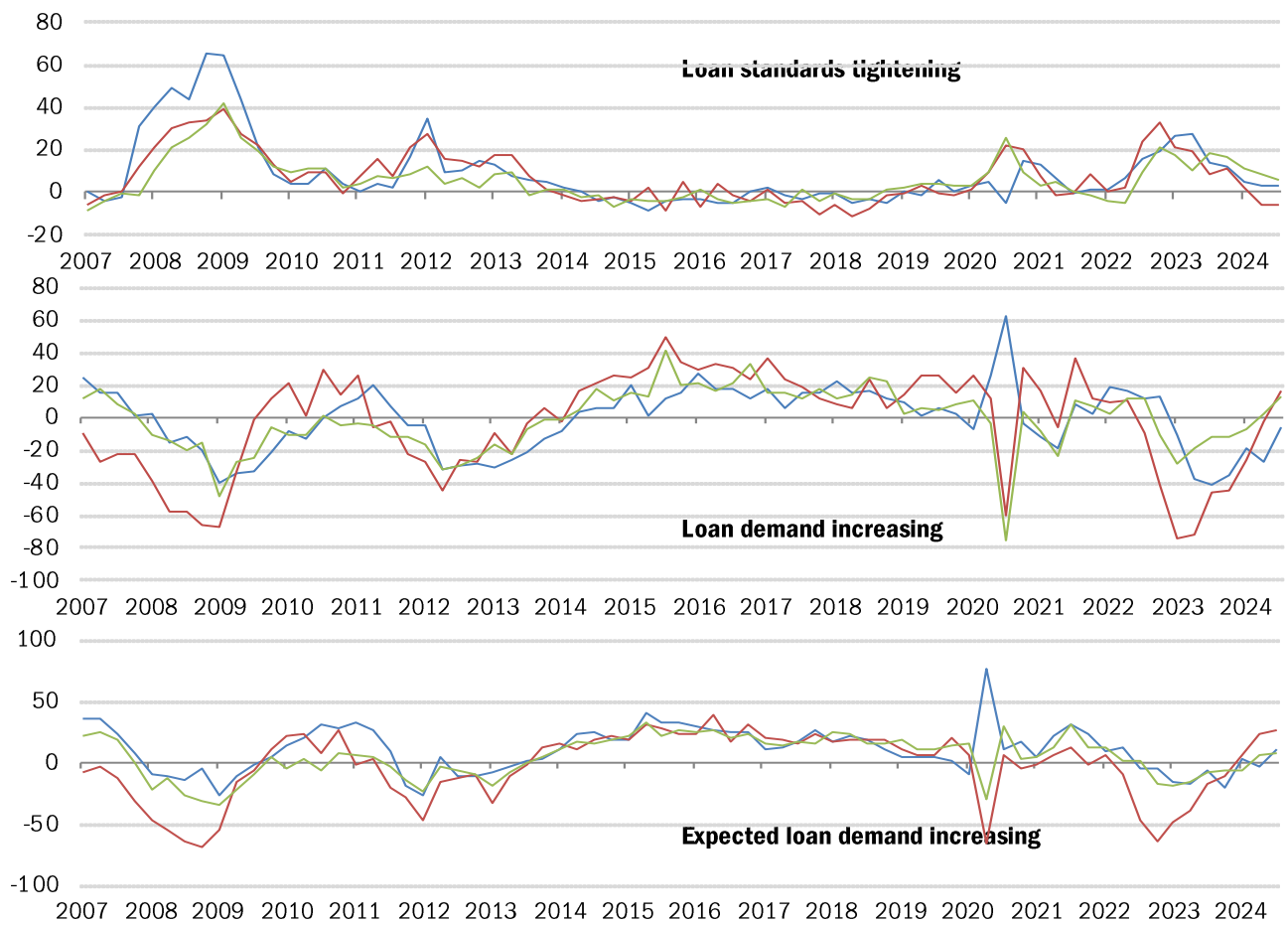
— Loans to 1 year — Loans 1-5 years — Loans 5 years plus ... Total



Source: ECB, TrendMacro calculations

## Supply and demand for lending: ECB Bank Survey

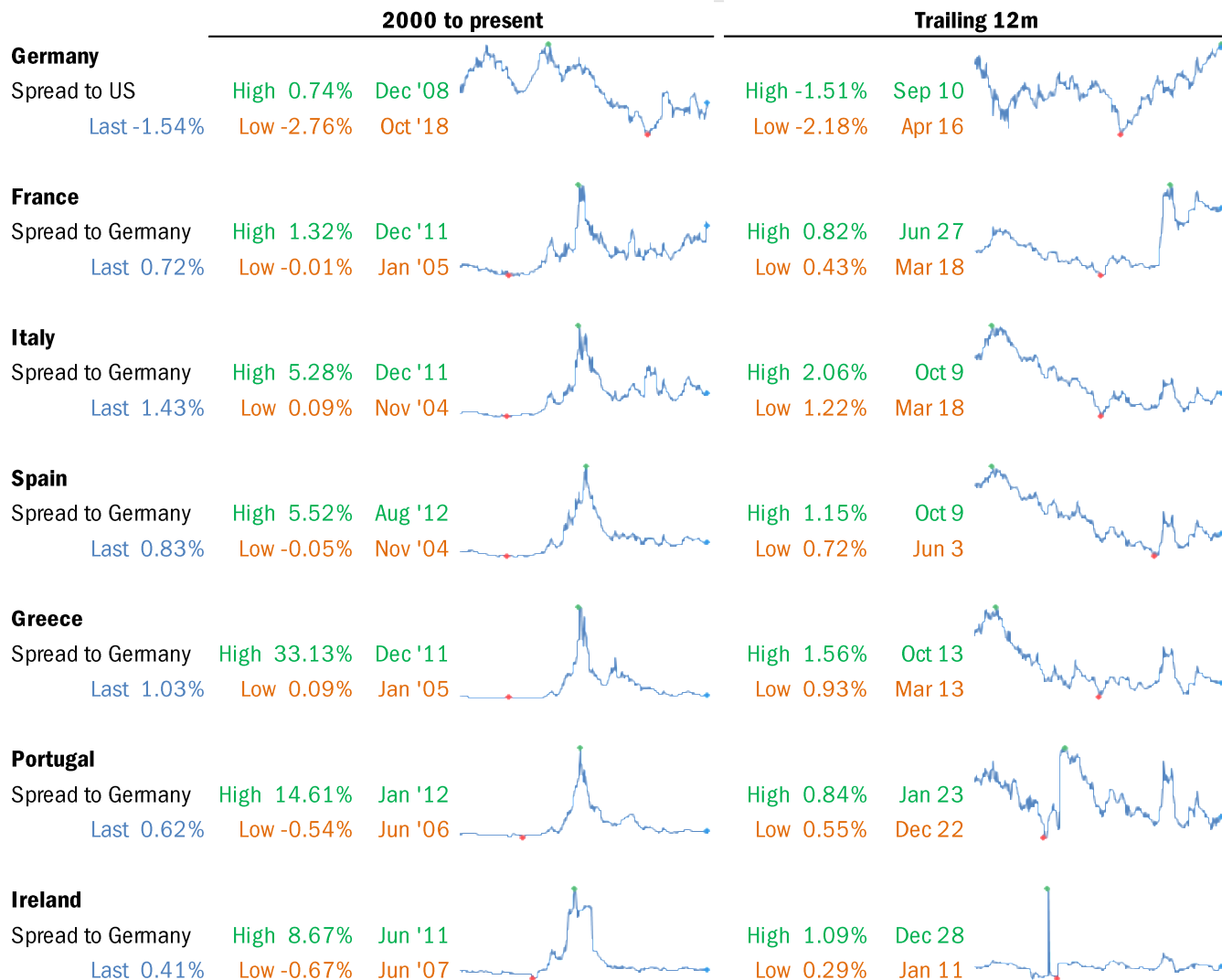
Net number of banks reporting for: — Enterprises — Home mortgage — Consumer



Source: ECB, TrendMacro calculations

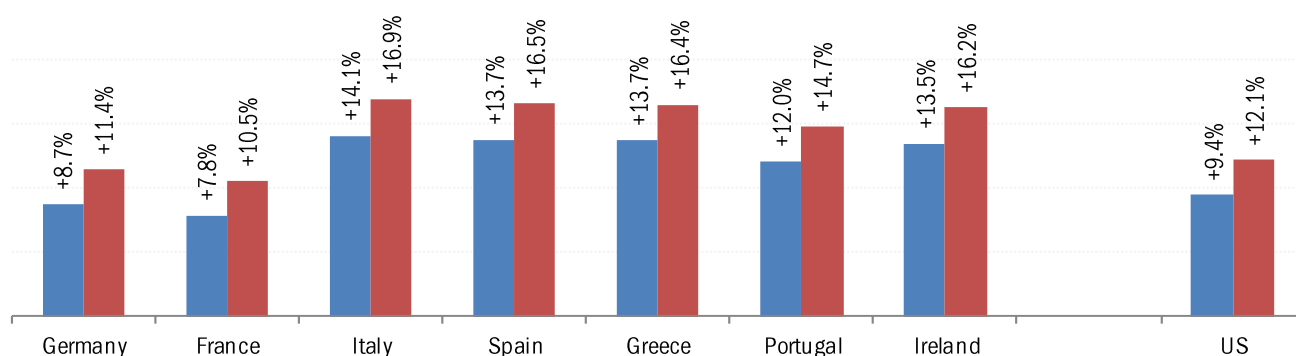
# Sovereign stress monitor: 10-year bond spreads

· High · Low · Last



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

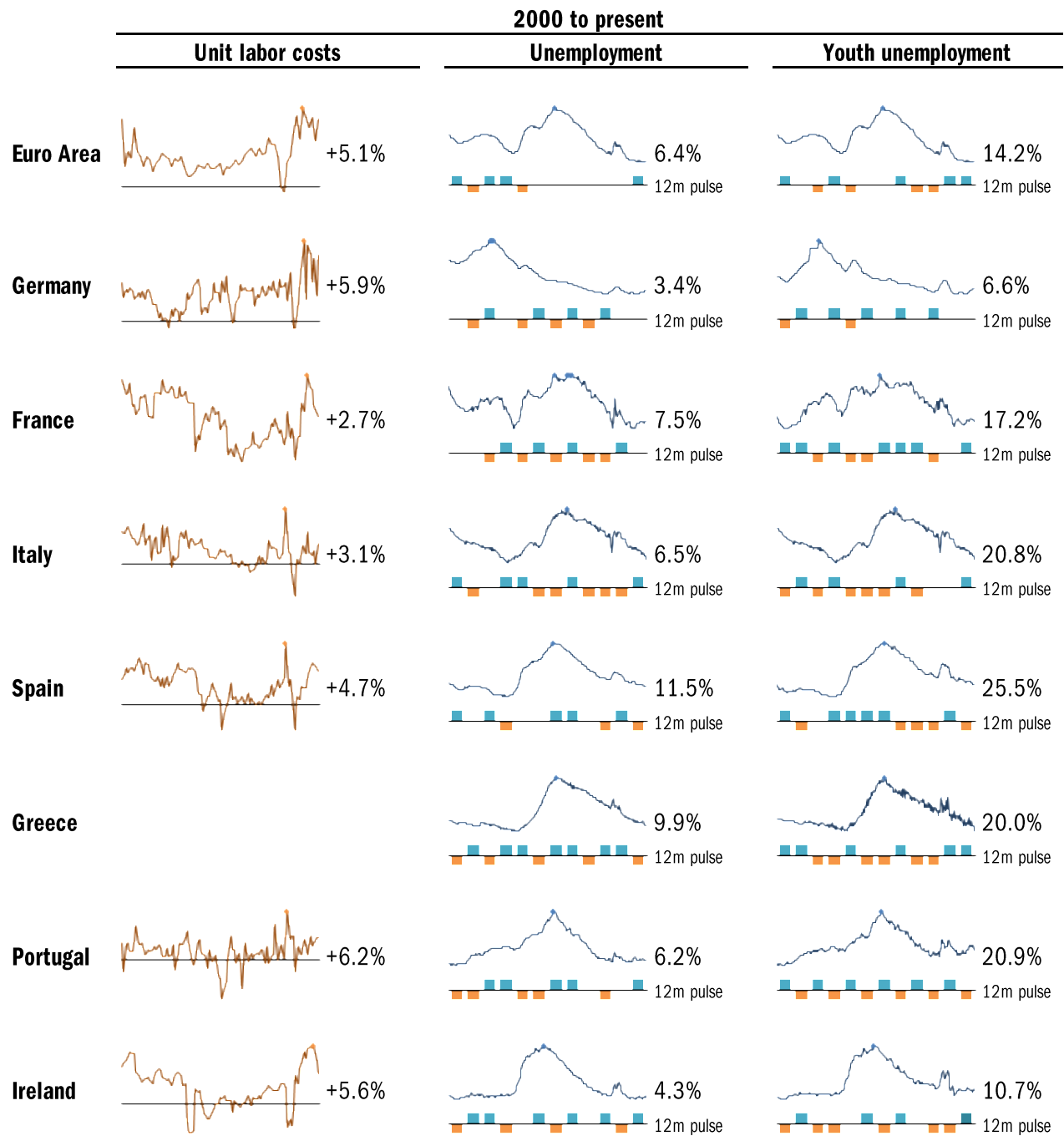
■ EUR ■ USD



Source: Bloomberg, TrendMacro calculations

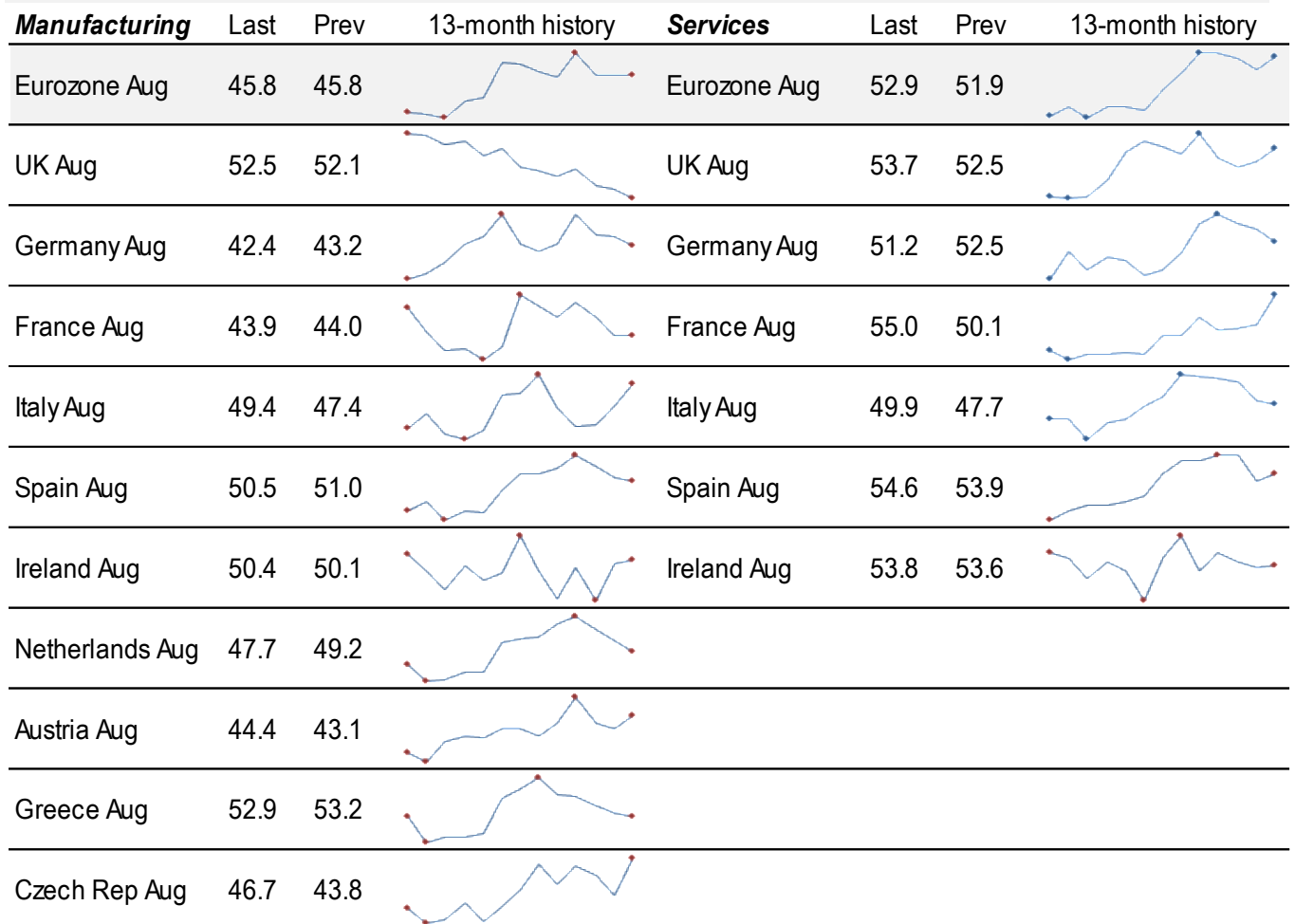
# Labor market in intensive care

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



Source: Eurostat, TrendMacro calculations

## Purchasing Manager Indices



Source: Markit, TrendMacro calculations

## Regional currency flight — Euro vs Swiss franc ■ SNB FX reserves

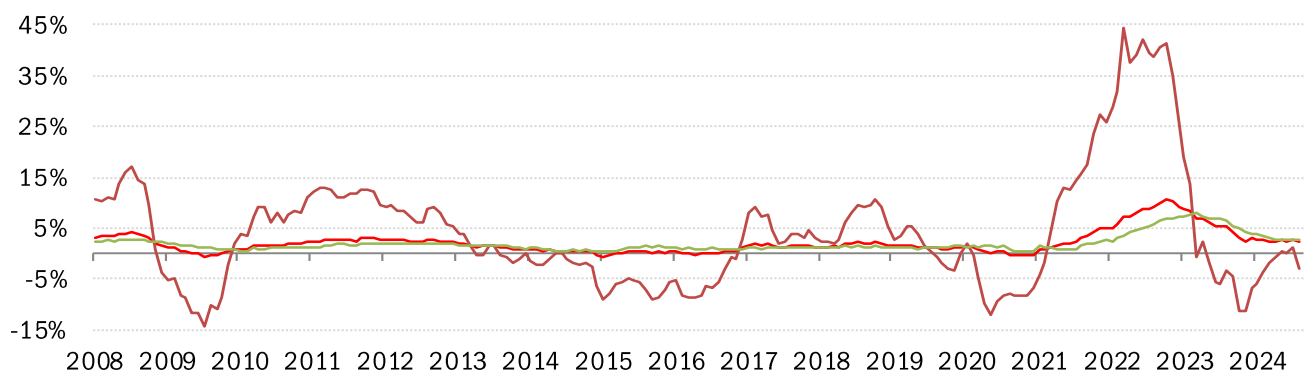
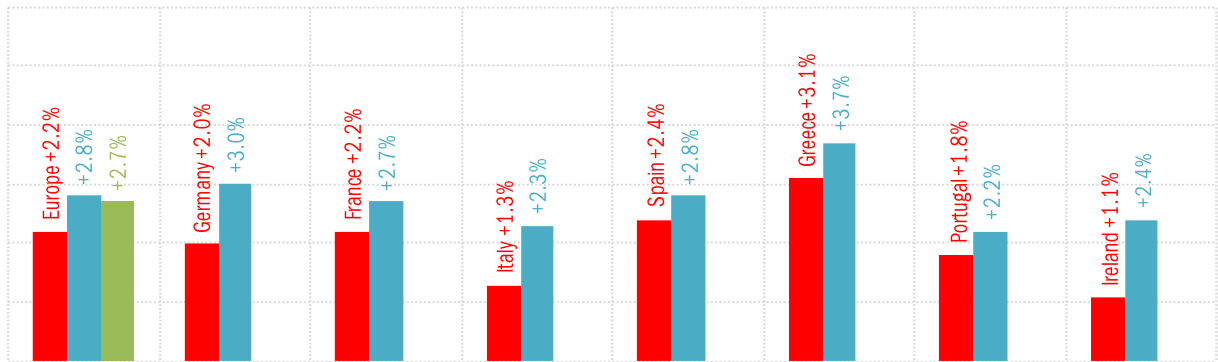


Source: Bloomberg, TrendMacro calculations



## 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