

Combined monetary policy decisions and statement

12 September 2024

Monetary policy decisions

The Governing Council today decided to lower the deposit facility rate – the rate through which it steers the monetary policy stance – by 25 basis points. Based on the Governing Council’s updated assessment of the inflation outlook, the dynamics of underlying inflation 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 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 higher wages on inflation. Financing conditions remain restrictive, 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 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 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 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. Accordingly, the deposit facility rate will be decreased to 3.50%. The interest rates on the main refinancing operations and 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.

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.

The President of the ECB will comment on the considerations underlying these decisions at a press conference starting at 14:45 CET today.

Monetary policy statement

Press conference

**Christine Lagarde, President of the ECB,
Luis de Guindos, Vice-President of the ECB**

Good afternoon, the Vice-President and I welcome you to our press conference.

The Governing Council today decided to lower the deposit facility rate – the rate through which we steer the monetary policy stance – by 25 basis points. Based on our updated assessment of the inflation outlook, the dynamics of underlying inflation 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 per cent in 2024, 2.2 per cent in 2025 and 1.9 per cent 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 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 per cent this year to 2.3 per cent in 2025 and 2.0 per cent 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 higher wages on inflation. Financing conditions remain restrictive, and economic activity is still subdued, reflecting weak private consumption and investment. Staff project that the economy will grow by 0.8 per cent in 2024, rising to 1.3 per cent in 2025 and 1.5 per cent in 2026. This is a slight downward revision compared with the June projections, mainly owing to a weaker contribution from domestic demand over the next few quarters.

We are determined to ensure that inflation returns to our two per cent medium-term target in a timely manner. We will keep policy rates sufficiently restrictive for as long as necessary to achieve this aim. We will continue to follow a data-dependent and meeting-by-meeting approach to determining the appropriate level and duration of restriction. In particular, our interest rate decisions will be based on our 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. We are not pre-committing to a particular rate path.

The decisions taken today are set out in a press release available on our website. 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.

I will now outline in more detail how we see the economy and inflation developing and will then explain our assessment of financial and monetary conditions.

Economic activity

The economy grew by 0.2 per cent in the second quarter, after 0.3 per cent in the first quarter, falling short of the latest staff projections. Growth stemmed mainly from net exports and government spending. Private domestic demand weakened, as households consumed less, firms cut down business investment and housing investment dropped. While services supported growth, industry and construction contributed negatively. According to survey indicators, the recovery is continuing to face some headwinds.

We expect the recovery to strengthen over time, as rising real incomes allow households to consume more. The gradually fading effects of restrictive monetary policy should support consumption and investment. Exports should also continue contributing to the recovery as global demand rises.

The labour market remains resilient. The unemployment rate was broadly unchanged in July, at 6.4 per cent. At the same time, employment growth slowed to 0.2 per cent in the second quarter, from 0.3 per cent in the first. Recent survey indicators point to a further moderation in demand for labour, and the job vacancy rate has fallen closer to pre-pandemic levels.

Fiscal and structural policies should be aimed at making the economy more productive and competitive, which would help to raise potential growth and reduce price pressures in the medium term. Mario Draghi's report on the future of European competitiveness and Enrico Letta's report on empowering the Single Market stress the urgent need for reform and provide concrete proposals to make this happen. Implementing the EU's revised economic governance framework fully, transparently and without delay will help governments bring down budget deficits and debt ratios on a sustained basis. Governments should now make a strong start in this direction in their medium-term plans for fiscal and structural policies.

Inflation

According to Eurostat's flash estimate, annual inflation dropped to 2.2 per cent in August, from 2.6 per cent in July. Energy prices fell at an annual rate of 3.0 per cent, after an increase of 1.2 per cent in the previous month. Food price inflation went up slightly, to 2.4 per cent in August. Goods inflation and services inflation moved in opposite directions. Goods inflation declined to 0.4 per cent, from 0.7 per cent in July, while services inflation rose, to 4.2 per cent from 4.0 per cent.

Most measures of underlying inflation were broadly unchanged in July. Domestic inflation edged down only slightly, to 4.4 per cent from 4.5 per cent in June, with strong price pressures coming especially from wages. Negotiated wage growth will remain high and volatile over the remainder of the year, given the significant role of one-off payments in some countries and the staggered nature of wage adjustments. At the same time, the overall growth in labour costs is moderating. The growth in compensation per employee fell further to 4.3 per cent in the second quarter, the fourth consecutive decline, and ECB staff project it to slow markedly again next year. Despite weak productivity, unit labour costs grew less strongly in the second quarter, by 4.6 per cent, after 5.2 per cent in the first quarter. Staff expect unit labour cost growth to continue declining over the projection horizon owing to lower wage growth and a recovery in productivity. Finally, profits are continuing to partially offset the inflationary effects of higher labour costs.

The disinflation process should be supported by receding labour cost pressures and the past monetary policy tightening gradually feeding through to consumer prices. Most measures of longer-term inflation expectations stand at around 2 per cent, and the market-based measures have fallen closer to that level since our July meeting.

Risk assessment

The risks to economic growth remain tilted to the downside. Lower demand for euro area exports, owing for instance to a weaker world economy or an escalation in trade tensions between major economies, would weigh on euro area growth. Russia's unjustified war against Ukraine and the tragic conflict in the Middle East are major sources of geopolitical risk. This may result in firms and households becoming less confident about the future and global trade being disrupted. Growth could also be lower if the lagged effects of monetary policy tightening turn out stronger than expected. Growth could be higher if inflation comes down more quickly than expected and rising confidence and real incomes mean that spending increases by more than anticipated, or if the world economy grows more strongly than expected.

Inflation could turn out higher than anticipated if wages or profits increase by more than expected. Upside risks to inflation also stem from the heightened geopolitical tensions, which could push energy prices and freight costs higher in the near term and disrupt global trade. Moreover, extreme weather events, and the unfolding climate crisis more broadly, could drive up food prices. By contrast, inflation may surprise on the downside if monetary policy dampens demand more than expected, or if the economic environment in the rest of the world worsens unexpectedly.

Financial and monetary conditions

Market interest rates have declined markedly since our July meeting, mostly owing to a weaker outlook for global growth and reduced concerns about inflation pressures. Tensions in global markets over the summer led to a temporary tightening of financial conditions in the riskier market segments.

Overall, financing costs remain restrictive as our past policy rate increases continue to work their way through the transmission chain. The average interest rates on new loans to firms and on new mortgages stayed high in July, at 5.1 and 3.8 per cent respectively.

Credit growth remains sluggish amid weak demand. Bank lending to firms grew at an annual rate of 0.6 per cent in July, down slightly from June, and growth in loans to households edged up to 0.5 per cent. Broad money – as measured by M3 – grew by 2.3 per cent in July, the same rate as in June.

Conclusion

The Governing Council today decided to lower the deposit facility rate by 25 basis points. We are determined to ensure that inflation returns to our two per cent medium-term target in a timely manner. We will keep policy rates sufficiently restrictive for as long as necessary to achieve this aim. We will continue to follow a data-dependent and meeting-by-meeting approach to determining the appropriate level and duration of restriction. In particular, our interest rate decisions will be based on our 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. We are not pre-committing to a particular rate path.

In any case, we stand ready to adjust all of our instruments within our mandate to ensure that inflation returns to our medium-term target and to preserve the smooth functioning of monetary policy transmission.

We are now ready to take your questions.