Combined monetary policy decisions and statement

12 December 2024

Monetary policy decisions

The Governing Council today decided to lower the three key ECB interest rates by 25 basis points. In particular, the decision to lower the deposit facility rate – the rate through which the Governing Council steers the monetary policy stance – is based on its updated assessment of the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission.

The disinflation process is well on track. Staff see headline inflation averaging 2.4% in 2024, 2.1% in 2025, 1.9% in 2026 and 2.1% in 2027 when the expanded EU Emissions Trading System becomes operational. For inflation excluding energy and food, staff project an average of 2.9% in 2024, 2.3% in 2025 and 1.9% in both 2026 and 2027.

Most measures of underlying inflation suggest that inflation will settle at around the Governing Council's 2% medium-term target on a sustained basis. Domestic inflation has edged down but remains high, mostly because wages and prices in certain sectors are still adjusting to the past inflation surge with a substantial delay.

Financing conditions are easing, as the Governing Council's recent interest rate cuts gradually make new borrowing less expensive for firms and households. But they continue to be tight because monetary policy remains restrictive and past interest rate hikes are still transmitting to the outstanding stock of credit.

Staff now expect a slower economic recovery than in the September projections. Although growth picked up in the third quarter of this year, survey indicators suggest it has slowed in the current quarter. Staff see the economy growing by 0.7% in 2024, 1.1% in 2025, 1.4% in 2026 and 1.3% in 2027. The projected recovery rests mainly on rising real incomes – which should allow households to consume more – and firms increasing investment. Over time, the gradually fading effects of restrictive monetary policy should support a pick-up in domestic demand.

The Governing Council is determined to ensure that inflation stabilises sustainably at its 2% medium-term target. It will follow a data-dependent and meeting-by-meeting approach to determining the appropriate monetary policy stance. In particular, the Governing Council's 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.

Key ECB interest rates

The Governing Council today decided to lower the three key ECB interest rates by 25 basis points. Accordingly, the interest rates on the deposit facility, the main refinancing operations and the marginal lending facility will be decreased to 3.00%, 3.15% and 3.40% respectively, with effect from 18 December 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 will discontinue reinvestments under the PEPP at the end of 2024.

Refinancing operations

Banks will repay the remaining amounts borrowed under the targeted longer-term refinancing operations this month, which concludes this part of the balance sheet normalisation process.

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The Governing Council stands ready to adjust all of its instruments within its mandate to ensure that inflation stabilises sustainably at 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 three key ECB interest rates by 25 basis points. In particular, the decision to lower the deposit facility rate – the rate through which we steer the monetary policy stance – is based on our updated assessment of the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission.

The disinflation process is well on track. Staff see headline inflation averaging 2.4 per cent in 2024, 2.1 per cent in 2025, 1.9 per cent in 2026 and 2.1 per cent in 2027 when the expanded EU Emissions Trading System becomes operational. For inflation excluding energy and food, staff project an average of 2.9 per cent in 2024, 2.3 per cent in 2025 and 1.9 per cent in both 2026 and 2027.

Most measures of underlying inflation suggest that inflation will settle at around our two per cent medium-term target on a sustained basis. Domestic inflation has edged down but remains high, mostly because wages and prices in certain sectors are still adjusting to the past inflation surge with a substantial delay.

Financing conditions are easing, as our recent interest rate cuts gradually make new borrowing less expensive for firms and households. But they continue to be tight because our monetary policy remains restrictive and past interest rate hikes are still transmitting to the outstanding stock of credit.

Staff now expect a slower economic recovery than in the September projections. Although growth picked up in the third quarter of this year, survey indicators suggest it has slowed in the current quarter. Staff see the economy growing by 0.7 per cent in 2024, 1.1 per cent in 2025, 1.4 per cent in 2026 and 1.3 per cent in 2027. The projected recovery rests mainly on rising real incomes – which should allow households to consume more – and firms increasing investment. Over time, the gradually fading effects of restrictive monetary policy should support a pick-up in domestic demand.

We are determined to ensure that inflation stabilises sustainably at our two per cent medium-term target. We will follow a data-dependent and meeting-by-meeting approach to determining the appropriate monetary policy stance. 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.

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 0.4 per cent in the third quarter, exceeding expectations. Growth was driven mainly by an increase in consumption, partly reflecting one-off factors that boosted tourism over the summer, and by firms building up inventories. But the latest information suggests it is losing momentum. Surveys indicate that manufacturing is still contracting and growth in services is slowing. Firms are holding back their investment spending in the face of weak demand and a highly uncertain outlook. Exports are also weak, with some European industries finding it challenging to remain competitive.

The labour market remains resilient. Employment grew by 0.2 per cent in the third quarter, again by more than expected. The unemployment rate remained at its historical low of 6.3 per cent in October. Meanwhile, demand for labour continues to weaken. The job vacancy rate declined to 2.5% in the third quarter, 0.8 percentage points below its peak, and surveys also point to fewer jobs being created in the current quarter.

The economy should strengthen over time, although more slowly than previously expected. The rise in real wages should strengthen household spending. More affordable credit should boost consumption and investment. Provided trade tensions do not escalate, exports should support the recovery as global demand rises.

Fiscal and structural policies should make the economy more productive, competitive and resilient. It is crucial to swiftly follow up, with concrete and ambitious structural policies, on Mario Draghi's proposals for enhancing European competitiveness and Enrico Letta's proposals for empowering the Single Market. We welcome the European Commission's assessment of governments' medium-term plans for fiscal and structural policies, as part of the EU's revised economic governance framework. Governments should now focus on implementing their commitments under this framework fully and without delay. This will help bring down budget deficits and debt ratios on a sustained basis, while prioritising growth-enhancing reforms and investment.

Inflation

Annual inflation increased to 2.3 per cent in November according to Eurostat's flash estimate, from 2.0 per cent in October. The increase was expected and primarily reflected an energy-related upward base effect. Food price inflation edged down to 2.8 per cent and services inflation to 3.9 per cent. Goods inflation went up to 0.7 per cent.

Domestic inflation, which closely tracks services inflation, again eased somewhat in October. But at 4.2%, it remains high. This reflects strong wage pressures and the fact that some services prices are still adjusting with a delay to the past inflation surge. That said, underlying inflation is overall developing in line with a sustained return of inflation to target.

The increase in compensation per employee moderated to 4.4 per cent in the third quarter from 4.7 per cent in the second. Amid stable productivity, this contributed to slower growth in unit labour costs. Staff expect labour costs to increase more slowly over the projection horizon as a result of lower wage growth and higher productivity growth. Moreover, profits should continue to partially offset the effects of higher labour costs on prices, especially in the near term.

We expect inflation to fluctuate around its current level in the near term, as previous sharp falls in energy prices continue to drop out of the annual rates. It should then settle sustainably at around the two per cent medium-term target. Easing labour cost pressures and the continuing impact of our past monetary policy tightening on consumer prices should help this process. Most measures of longer-term inflation expectations stand at around 2 per cent, and market-based indicators of medium to longer-term inflation compensation have decreased measurably since the Governing Council's October meeting.

Risk assessment

The risks to economic growth remain tilted to the downside. The risk of greater friction in global trade could weigh on euro area growth by dampening exports and weakening the global economy. Lower confidence could prevent consumption and investment from recovering as fast as expected. This could be amplified by geopolitical risks, such as Russia's unjustified war against Ukraine and the tragic conflict in the Middle East, which could disrupt energy supplies and global trade. Growth could also be lower if the lagged effects of monetary policy tightening last longer than expected. It could be higher if easier financing conditions and falling inflation allow domestic consumption and investment to rebound faster.

Inflation could turn out higher 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 more than expected. By contrast, inflation may surprise on the downside if low confidence and concerns about geopolitical events prevent consumption and investment from recovering as fast as expected, if monetary policy dampens demand more than expected, or if the economic environment in the rest of the world worsens unexpectedly. Greater friction in global trade would make the euro area inflation outlook more uncertain.

Financial and monetary conditions

Market interest rates in the euro area have declined further since our October meeting, reflecting the perceived worsening of the economic outlook. Although financing conditions remain restrictive, our interest rate cuts are gradually making it less expensive for firms and households to borrow.

The average interest rate on new loans to firms was 4.7 per cent in October, more than half a percentage point below its peak a year earlier. The cost of issuing market-based debt has fallen by more than a percentage point since its peak. The average rate on new mortgages, at 3.6 per cent in October, is about half a percentage point lower than at its highest point in 2023, even though the average rate on the outstanding stock of mortgages is still set to rise.

Bank lending to firms has gradually picked up from low levels, and increased by 1.2 per cent in October compared with a year earlier. Debt securities issued by firms were up 3.1% in annual terms, which was similar to the increase in the previous few months. Mortgage lending continued to rise gradually in October, with an annual growth rate of 0.8 per cent.

In line with our monetary policy strategy, the Governing Council thoroughly assessed the links between monetary policy and financial stability. Euro area banks remain resilient and there are few signs of financial market stress. Financial stability risks nonetheless remain elevated. Macroprudential policy remains the first line of defence against the build-up of financial vulnerabilities, enhancing resilience and preserving macroprudential space.

Conclusion

The Governing Council today decided to lower the three key ECB interest rates by 25 basis points. In particular, the decision to lower the deposit facility rate – the rate through which we steer the monetary policy stance – is based on our updated assessment of the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission. We are determined to ensure that inflation stabilises sustainably at our two per cent medium-term target. We will follow a data-dependent and meeting-by-meeting approach to determining the appropriate monetary policy stance. 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 stabilises sustainably at our medium-term target and to preserve the smooth functioning of monetary policy transmission.

We are now ready to take your questions.