

Governing Council meeting, ECB. 10/03/2022

ECB to taper the APP as well as ending PEPP at the end of March

At its meeting on 10th March, the Governing Council of European Central Bank announced a revision to the increase in the amount of assets purchased under the 2019 Asset Purchase Scheme. Initially, the monthly purchases were to be increased from €20b. to €40b. for three months starting in April to offset the termination of the Pandemic Emergency Purchase Programme at the end of March. Now the plan is for the rise to €40b. to last for just one month, followed by €30b. in May and then back to €20b. in June, with the possibility of terminating this asset purchase programme too if inflationary pressures have not eased, The assets will be reinvested - in the case of those purchased through the PEPP scheme until at least the end of 2024. (No date was mentioned as far as the APP assets are concerned.) There are currently no plans to increase interest rates. At the press conference after the meeting, ECB President Christine Lagarde stated any rise in interest rates would not take place for “some time” after the end of the asset purchases.

Mme Lagarde also stressed that the current inflationary pressures have continued to “surprise on the upside because of unexpectedly high energy costs.” If she and her colleagues had been paying attention to the growth in the quantity of broad money over the last two years, perhaps they would not have been so surprised. In every month between March 2020 and February 2021, the annualised quarterly growth rate of Eurozone M3 never fell below 6.6% and rose as high as 21%. For an economy with a modest trend growth rate such as the Eurozone, broad money growth should ideally rise no higher than 5% if the inflation target is 2%. Given that the usual lag between a surge in broad money growth and the resultant inflation is normally between 18 and 24 months, consumer price inflation of 5.8% in the year to February is therefore no surprise. This is the highest reading since the launch of the single currency.

Annualised broad money growth fell to 5.4% in the three months to January, the lowest reading since May 2021. The ECB’s expectation of a slow decline in inflation is therefore likely to be realised, but broad money growth of over 7% for much of the second half of 2021 suggests that the decline may not happen anything like as soon nor be as sharp as the ECB currently expects. Indeed, with producer prices rising by no less than 30.6% in the year to January, inflation may well rise higher before it starts to fall back.

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