

Governing Council meeting, ECB. 14/04/2022

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

Bucking the trend of most central banks in advanced Western economies, the Governing Council of European Central Bank voted to keep interest rates at 0% at its meeting on 14h April. The ECB confirmed that the 2019 Asset Purchase Scheme is likely to be terminated in the third quarter of the year and that the monthly purchases will be increased from €20b. to €40b. in April, with €30b. to be purchased in May and €20b. in June. The Pandemic Emergency Purchase Programme has now ceased, but reinvestment of assets acquired under this scheme will continue until at least the end of 2024. The press release following the meeting stressed that uncertainties created by the Russian invasion of Ukraine has influenced its decision not to tighten monetary policy, even though inflationary pressures continue to build. Overall inflation in the Eurozone hit a record 7.5% in the year to March and producer prices rose by a remarkable 31.4% in the same period, strongly indicative of higher consumer prices to follow. Some individual Eurozone member states are seeing significantly higher inflation, with Lithuania, where prices rose by 15.7%, the worst affected. Nonetheless, a number of influential ECB policymakers, including chief economist Philip Lane, are worried that raising interest rates at this stage could provoke a severe downturn.

The dramatic increase in broad money, especially in the spring of 2020, is the principal culprit for these high levels of inflation, not the war in Ukraine, although this has unquestionably affected energy prices. Broad money grew at an annualised rate of 5.7% in the three months to February, a modest increase in comparison with over 20% in June 2020, but still somewhat too high to be compatible with the ECB's 2% inflation target and strongly indicative that high inflation is going to last for some time, regardless of the outcome of events in Ukraine.

The ECB's tardiness in responding to rising inflation has attracted criticism from Otmar Issing, one of the architects of the single currency. He called recent ECB policy "misguided" and claimed that the ECB would "pay the price for not heeding countless warnings and halting its ultra-expansionary monetary policy long ago", while Thomas Mayer, the chief economist at Deutsche Bank claimed that "the Euro has become the successor to the Italian Lira, not the Deutschmark, just as we feared." From a monetarist perspective, these criticisms are justified.

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