

Governing Council meeting, ECB. 02/02/2023

All lending rates increased by a further 0.5%

The ECB's Governing Council held its first meeting of the year on 2nd February and, as widely expected, voted further to hike the cost of borrowing by a further 0.5%. Since June, the cost of borrowing has risen by 3% in total. In the press conference following the meeting, Christine Lagarde, the ECB's President stated that a further 0.5% increase is likely at the next meeting of the Governing Council, scheduled for 16th March. She also confirmed plans to shrink the ECB's balance sheet. Maturing assets purchased under the 2019 Asset Purchase Scheme will be run off at a rate of €15b. per month from March until June 2023 at which point the rate of run-off will be reviewed. No mention was made of the assets purchased under the much larger 2020 Pandemic Emergency Purchase Programme. Previous statements have stressed that no run-off of these assets is on the cards until at least the end of 2024.

Thus far, the ECB has not hiked the cost of borrowing as much as many other central banks. Indeed, it was one of the last major central banks to tighten monetary policy, out of concerns that the increase in bond yields which normally accompanies higher lending rates could be problematical. Thus far, there has not been anything like as wide a spread in bond yields as that which caused the Sovereign Debt crisis a decade ago, Italy, the most at-risk member of the Eurozone saw yields on its 10-year bonds fall below 4%., nowhere near the 15%+ yields for Greek government debt in 2015. Inflation still remains a serious worry, even though the overall figure for the single currency bloc has been declining since October's peak of 10.6%. January's reading was 8.5%. This is still considerably higher than the ECB's 2% target and with producer prices rising at an annual rate of 27.1% in November (the most recent month for which statistics are available), that target is unlikely to be reached any time soon.

The quantity of broad money (M3) fell by €55b. during December. This brought the annualised quarterly growth rate into negative territory for the first time since January 2014. Growth in the stock of new bank loans, which remained fairly robust for most of 2022, slowed in the final two months, with both the housing market and business lending showing signs of weakness. The ECB's actions are likely to exacerbate the slowdown in broad money growth. GDP grew by a mere 0.1% in the final quarter of 2022 and although the currency bloc gained a new member, Croatia, in January 2023, which may distort the figures slightly, a recession looks likely in late 2023 or 2024.

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