

## **Governing Council meeting, ECB. 04/05/2023**

### **ECB raises rates by a further 0.25%**

The ECB's Governing Council raised all three of its key interest rates by a further 0.25% at its meeting on 4<sup>th</sup> May. The press release accompanying the announcement reiterated the ECB's commitment to bring inflation down to its 2% target prompting Christine Lagarde, ECB president, to comment "We are not pausing, that is extremely clear" while noting that some of the Governing Council had backed a bigger rise of 50bps., which implied that this may not be the last rate hike. Indeed, on Tuesday 9<sup>th</sup> May, Peter Kažimír, the governor of the Slovakian central bank (And thus a member of the ECB's Governing Council), stated that the spate of rate increases may have to be prolonged for longer than anticipated due to the persistence of above-target inflation. Prices rose by 7% in the year to April, only a slight increase on March's reading of 6.9%, but an unwelcome hiatus after five consecutive months of decline.

Since July 2022, there have been seven back-to-back increases in the cost of borrowing, with the main refinancing fixed rate having now risen by 375bps to 3.75% in total - an unprecedented cycle of tightening. Maturing assets purchased under the 2019 Asset Purchase Scheme that had been running off at a rate of €15b. per month since March 2023 will now be increased to €25b. a month from July 2023. after which there will be no further reinvestment at all, which may result in a larger run-off after this date. No assets purchased under the much larger 2020 Pandemic Emergency Purchase Programme will be run off before the end of 2024.

M3 in the Eurozone has now been on a downward path for most of the last six months. Even allowing for the entry of Croatia into the single currency bloc at the beginning of 2023, the quantity of money, broadly defined, has fallen by over €100b. since September. The annual rate of growth has fallen to 2.5%, the lowest level since late 2014, while the annualised quarterly growth rate has now been negative for four consecutive months. Strong growth in lending by Eurozone banks kept broad money growth buoyant for several months after the termination of the asset purchases but demand for credit is slowing, both from consumers and businesses. Mortgage lending was growing at an annual rate of over 5% at the start of 2022. The most recent figure (March 2023) is 3.3%. Growth in new loans to non-financial companies has declined from 5.3% at the start of the year to 4.4%. The recent bank failures in the USA and Europe have raised the prospect of further regulation, including demands for banks to set aside even more capital, leaving them with fewer resources available for new loans. The net result is that broad money growth is likely to fall still further.

Eurozone GDP increased by a very modest 0.1% in the first quarter of 2023. It did not grow at all at all in Germany, once the powerhouse of the Eurozone economy. The only positive prediction that can be made about the economy across the 20-nation currency bloc is that inflation will probably drop back to the 2% target by the end of the year. The money numbers strongly point to a recession, perhaps before the end of the year, and the likelihood of further increases in the cost of borrowing, especially in conjunction with more bank regulation, do not offer much hope of a swift rebound.

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