EUROPEAN CENTRAL BANK
EUROSYSTEM

Combined monetary policy decisions and statement

25 January 2024

Monetary policy decisions

The Governing Council today decided to keep the three key ECB interest rates unchanged. The incoming information has broadly confirmed its previous assessment of the medium-term inflation outlook. Aside from an energy-related upward base effect on headline inflation, the declining trend in underlying inflation has continued, and the past interest rate increases keep being transmitted forcefully into financing conditions. Tight financing conditions are dampening demand, and this is helping to push down inflation.

The Governing Council is determined to ensure that inflation returns to its 2% medium-term target in a timely manner. Based on its current assessment, the Governing Council considers that the key ECB interest rates are at levels that, maintained for a sufficiently long duration, will make a substantial contribution to this goal. The Governing Council's future decisions will ensure that its policy rates will be set at sufficiently restrictive levels for as long as necessary.

The Governing Council will continue to follow a data-dependent approach to determining the appropriate level and duration of restriction. 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.

Key ECB interest rates

The interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility will remain unchanged at 4.50%, 4.75% and 4.00% respectively.

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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 Governing Council intends to continue to reinvest, in full, the principal payments from maturing securities purchased under the PEPP during the first half of 2024. Over the second half of the year, it intends to reduce the PEPP portfolio by €7.5 billion per month on average. The Governing Council intends to discontinue reinvestments under the PEPP at the end of 2024.

The Governing Council will continue applying flexibility in reinvesting redemptions coming due in the PEPP portfolio, with a view to countering risks to the monetary policy transmission mechanism related to the pandemic.

Refinancing operations

As banks are repaying the amounts borrowed under the targeted longer-term refinancing operations, the Governing Council will regularly assess how targeted lending operations and their ongoing repayment are contributing to its monetary policy stance.

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The Governing Council stands ready to adjust all of its instruments within its mandate to ensure that inflation returns to 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 keep the three key ECB interest rates unchanged. The incoming information has broadly confirmed our previous assessment of the medium-term inflation outlook. Aside from an energy-related upward base effect on headline inflation, the declining trend in underlying inflation has continued, and our past interest rate increases keep being transmitted forcefully into financing conditions. Tight financing conditions are dampening demand, and this is helping to push down inflation.

We are determined to ensure that inflation returns to our two per cent medium-term target in a timely manner. Based on our current assessment, we consider that the key ECB interest rates are at levels that, maintained for a sufficiently long duration, will make a substantial contribution to this goal. Our future decisions will ensure that our policy rates will be set at sufficiently restrictive levels for as long as necessary.

We will continue to follow a data-dependent approach to determining the appropriate level and duration of restriction. 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.

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 euro area economy is likely to have stagnated in the final quarter of 2023. The incoming data continue to signal weakness in the near term. However, some forward-looking survey indicators point to a pick-up in growth further ahead.

The labour market has remained robust. The unemployment rate, at 6.4 per cent in November, has fallen back to its lowest level since the start of the euro and more workers have entered the labour force. At the same time, demand for labour is slowing, with fewer vacancies being advertised.

Governments should continue to roll back energy-related support measures to avoid driving up medium-term inflationary pressures. Fiscal and structural policies should be designed to make our economy more productive and competitive, as well as to gradually bring down high public debt ratios. Structural reforms and investments to enhance the euro area’s supply capacity – which would be supported by the full implementation of the Next Generation EU programme – can help reduce price pressures in the medium term, while supporting the green and digital transitions. Following the recent ECOFIN Council agreement on the reform of the EU’s economic governance framework, the legislative process should be concluded swiftly so that the new rules can be implemented without delay. Moreover, it is imperative that progress towards Capital Markets Union and the completion of Banking Union be accelerated.

Inflation

Inflation rose to 2.9 per cent in December as some of the past fiscal measures to cushion the impact of high energy prices dropped out of the annual inflation rate, although the rebound was weaker than expected. Aside from this base effect, the overall trend of declining inflation continued. Food price inflation dropped to 6.1 per cent in December. Inflation excluding energy and food also declined again, to 3.4 per cent, due to a fall in goods inflation to 2.5 per cent. Services inflation was stable at 4.0 per cent.

Inflation is expected to ease further over the course of this year as the effects of past energy shocks, supply bottlenecks and the post-pandemic reopening of the economy fade, and tighter monetary policy continues to weigh on demand.

Almost all measures of underlying inflation declined further in December. The elevated rate of wage increases and falling labour productivity are keeping domestic price pressures high, although these too have started to ease. At the same time, lower unit profits have started to moderate the inflationary effect of rising unit labour costs. Measures of shorter-term inflation expectations have come down markedly, while those of longer-term inflation expectations mostly stand around 2 per cent.

Risk assessment

The risks to economic growth remain tilted to the downside. Growth could be lower if the effects of monetary policy turn out stronger than expected. A weaker world economy or a further slowdown in global trade would also weigh on euro area growth. Russia's unjustified war against Ukraine and the tragic conflict in the Middle East are key sources of geopolitical risk. This may result in firms and households becoming less confident about the future and global trade being disrupted. Growth could be higher if rising real incomes mean spending increases by more than anticipated, or if the world economy grows more strongly than expected.

Upside risks to inflation include the heightened geopolitical tensions, especially in the Middle East, which could push energy prices and freight costs higher in the near term and hamper global trade. Inflation could also turn out higher than anticipated if wages increase by more than expected or profit margins prove more resilient. By contrast, inflation may surprise on the downside if monetary policy dampens demand by more than expected, or if the economic environment in the rest of the world worsens unexpectedly. Moreover, inflation could decline more quickly in the near term if energy prices evolve in line with the recent downward shift in market expectations of the future path for oil and gas prices.

Financial and monetary conditions

Market interest rates have moved broadly sideways since our last meeting. Our restrictive monetary policy continues to transmit strongly into broader financing conditions. Lending rates on business loans declined slightly, to 5.2 per cent in November, while mortgage rates increased further to 4.0 per cent.

High borrowing rates, with the associated cutbacks in investment plans and house purchases, led to a further drop in credit demand in the fourth quarter, as reported in our latest bank lending survey. While the tightening of credit standards for loans to firms and households moderated, they remained tight, with banks concerned about the risks faced by their customers.

Against this background, credit dynamics have improved somewhat but overall remain weak. Loans to firms stagnated in November compared with a year earlier – after contracting in October – as the monthly flow of short-term loans rebounded. Loans to households grew at a subdued annual rate of 0.5 per cent.

Conclusion

The Governing Council today decided to keep the three key ECB interest rates unchanged. We are determined to ensure that inflation returns to our two per cent medium-term target in a timely manner. Based on our current assessment, we consider that the key ECB interest rates are at levels that, maintained for a sufficiently long duration, will make a substantial contribution to this goal. Our future decisions will ensure that our policy rates will be set at sufficiently restrictive levels for as long as necessary. We will continue to follow a data-dependent approach to determining the appropriate level and duration of restriction.

In any case, we stand ready to adjust all of our instruments within our mandate to ensure that inflation returns to our medium-term target and to preserve the smooth functioning of monetary policy transmission.

We are now ready to take your questions.