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IMFC Statement by Mario Draghi
President
European Central Bank

Statement by Mario Draghi, President of the ECB, at the thirty-fifth meeting of the International Monetary and Financial Committee, Washington DC, 21 April 2017

Growth in the euro area economy, supported by the ECB's monetary policy measures, is firming and broadening, compared with the situation at the time of our last meeting six months ago. Risks to the growth outlook have somewhat diminished, but remain tilted to the downside and relate predominantly to global factors. While euro area headline inflation has increased markedly over the past year, underlying inflation is expected to continue to remain subdued. A very substantial degree of monetary accommodation is still needed to secure a sustained return of inflation rates towards levels below, but close to, 2% – in line with the ECB's mandate. In order to reap the full benefits of our monetary policy measures, actions in other economic policy areas are necessary to strengthen long-term growth and resilience in the euro area.

The euro area's ongoing economic expansion is being largely driven by domestic demand, with both private consumption and investment contributing to growth. Real GDP rose by 1.7% in 2016. There are signs that the recovery is broadening across countries and sectors. The pass-through of our monetary policy measures is supporting domestic demand. The recovery in investment continues to be promoted by very favourable financing conditions and improvements in corporate profitability. Private consumption should be further aided by continued employment gains. There are also signs of a somewhat brighter global recovery and increasing global trade. The latest ECB staff projections foresee annual real GDP increasing by 1.8% in 2017, 1.7% in 2018 and 1.6% in 2019.

Headline inflation in the euro area has increased over the past year, largely reflecting noticeably higher energy and food inflation. The risks of deflation, defined as generalised price declines that trigger a negative spiral of self-fulfilling expectations, have largely disappeared. At the same time, underlying inflation has not shown a convincing upward trend – domestic cost pressures remain subdued and recent increases in global price pressures have yet to filter through. In the coming months, headline inflation is likely to fluctuate around current levels, mainly reflecting movements in the annual rate of change of energy prices. Underlying inflation, however, is expected to rise only gradually over the medium term, supported by our monetary policy measures, the expected continuing economic recovery and the corresponding gradual absorption of slack. The latest ECB staff projections for the euro area point to annual headline inflation of 1.7% in 2017, 1.6% in 2018 and 1.7% in 2019.

The comprehensive monetary policy measures taken by the ECB since June 2014 have materially contributed to the economic upturn. Financing conditions and credit demand have improved. Lending volumes continue to rise, bank lending rates for households and companies have fallen to historically low levels; and there has been a decrease in their cross-country heterogeneity. Also, compared to six months ago, market-based inflation expectations have noticeably strengthened. At the same time, as underlying inflation remains subdued and the path of inflation crucially dependent on the prevailing very favourable financing conditions, we cannot yet have sufficient confidence that a sustained adjustment in inflation will materialise in a durable manner. Thus, a very substantial degree of monetary accommodation is still needed for underlying inflation pressures to build up and to support headline inflation in the medium term.

As the Governing Council affirmed at its last monetary policy meeting on 9 March, we continue to expect the key ECB interest rates to remain at present or lower levels for an extended period of time, and well past the horizon of the net asset purchases. Until the end of last month our monthly purchases of public and private sector securities under the asset purchase programme (APP) amounted to €80 billion on average. They are now intended to continue at a monthly pace of €60 billion until the end of December 2017, or beyond, if necessary, and in any case until the ECB's Governing Council sees a sustained adjustment in the path of inflation consistent with its inflation aim. The net purchases will be made alongside reinvestments of the principal payments from maturing securities purchased under the APP. If the outlook becomes less favourable, or if financial conditions become inconsistent with further progress towards a sustained adjustment in the path of inflation, we stand ready to increase our asset purchase programme in terms of size and/or duration.

Market sentiment towards the euro area banking sector has improved. The recent strengthening of the recovery is supporting banks' profitability and helping to reduce the stock of non-performing loans (NPLs). Euro area banks have improved their capital positions since the crisis and are now well capitalised at an aggregate level. Nevertheless, profitability remains weak in parts of the euro area banking sector and important vulnerabilities and structural challenges remain. These challenges include incomplete adjustment of bank business models, cost inefficiencies, overcapacity and still-large stocks of NPLs for parts of the euro area banking sector. First and foremost, it is up to the banks themselves to undertake the needed adjustment. But an effective reduction of NPLs will require action from all stakeholders, and will need to include legal and institutional reforms. In particular, active policies are needed to improve the efficiency of judicial systems, increase access to collateral, introduce swift out-of-court procedures and create liquid markets for distressed debt. Last month the ECB published its final guidance to banks on NPLs. Furthermore, it is crucial to complete the global regulatory reform agenda as soon as possible in order to significantly strengthen the regulatory framework for banks and ensure a period of regulatory stability and certainty for market participants.

While the economic recovery in the euro area is firming, the reform process needs to be reinvigorated to transform the cyclical pick-up into stronger and persistent long-term growth. To that end, structural reforms have to be implemented much more decisively, including reforms addressing key institutional weaknesses and improving private debt workout mechanisms which are necessary to improve the investment environment. In many cases, these reforms entail fairly low short-term economic cost. Given that national reform efforts remain limited in euro area countries, it is also important to foster the use of existing tools, most notably a full and consistent application of the EU's macroeconomic imbalance procedure. Likewise, full and consistent implementation of the Stability and Growth Pact remains crucial to ensure confidence in the EU's fiscal framework and to safeguard public debt sustainability. In the current environment of a firming economic recovery, a broadly neutral euro area fiscal stance strikes an appropriate balance between aggregate stabilisation and sustainability needs. However, the contribution of individual Member States to the area-wide stance is sub-optimal. Some Member States need to take additional measures to ensure compliance with the fiscal rules while others have scope to use available fiscal space. All euro area countries should strive for a more growth-friendly composition of fiscal policies.

More broadly, a stronger and more complete Economic and Monetary Union (EMU) is essential to ensuring the future resilience of the euro area economy. The European Commission started a general reflection on the future of the EU by publishing a white paper last month, which will be followed by a paper on EMU in May 2017. We need to make progress on completing the banking union by moving forwards in parallel on risk sharing and risk reduction, and we look forward to an ambitious mid-term review process of the capital markets union agenda. A more complete EMU is the foundation for a stable, flourishing and resilient euro area economy that will be the best contribution to global economic growth and financial stability. The ECB will continue to do its part by delivering on its mandate.