Meeting of 18 March 2020

Account of the monetary policy meeting of the Governing Council of the European Central Bank held by means of a teleconference on Wednesday, 18 March 2020

1. Review of financial and economic developments and policy options

The President started the meeting by observing that, while the policy measures taken by the Governing Council at its monetary policy meeting on 11-12 March 2020 had been well calibrated at the time, the scale of the challenges faced had been highly uncertain. Meanwhile, the situation had deteriorated significantly, with nearly all euro area countries in full containment mode owing to the rapid spread of the coronavirus (COVID-19). The situation was unprecedented and the repercussions were also impossible to forecast accurately. Uncertainty on the economic front was creating severe strains in the financial markets, while the message that, first and foremost, fiscal support was required had been well understood, and many governments had already responded. Faced with the risk of the ECB's monetary policy transmission becoming significantly impaired, there was an urgent need for the Governing Council to reassess its policy stance and instruments to address the economic consequences of the evolving coronavirus pandemic.

Financial market developments

Ms Schnabel reviewed the latest financial market developments.

Since the Governing Council's regular monetary policy meeting on 11-12 March 2020, Europe had become the epicentre of the global coronavirus pandemic. To date, almost as many cases had been confirmed in the euro area as in China. As a result, losses in euro area stock markets had been larger than in most other jurisdictions. The EURO STOXX 50 was down by nearly 40% since 20 February 2020, when the coronavirus epidemic had started to turn into a global pandemic. Stock markets in the United States, Japan and emerging markets were all down by around 25% over the same period. The euro area banking sector had been one of the sectors most severely affected by the pandemic-related crisis and bank stocks were down by close to 50% over the period. Implied volatility had continuously trended upwards and, over the two days prior to the current meeting, had reached levels last seen during the global financial crisis in 2008.

In euro area fixed income markets a significant deterioration in market liquidity had been observed over recent days. Counterparties had reported an absence of buyers for several types of assets. In this environment of thin liquidity, there had been a remarkable degree of price volatility, in particular in the US Treasury market. High volatility had also been observed in the German Bund market, with ten-year bond yields up by more than 40 basis points since Monday, 9 March. A main factor that had contributed to the rise in the yields of safe assets was likely related to the fiscal response to the coronavirus pandemic. Governments worldwide had announced a number of initiatives, resulting in expectations of an increased supply of government bonds and, ultimately, higher levels of duration risk that needed to be absorbed by investors, which had likely led to a rise in term premia. All in all, ten-year German government bond yields were now back at the levels observed just before the outbreak of the coronavirus, reflecting the broadly offsetting effects of a weaker growth outlook and the expected increase in bond supply.

At the same time, bond yields in other higher-rated euro area jurisdictions were currently well above their pre-coronavirus levels.

Whereas part of the widening of spreads could reflect differences in the impact of the coronavirus crisis on growth and debt across euro area jurisdictions, part of the rise could also reflect a flight to quality that even affected euro area sovereign issuers with higher credit ratings. Flight to safety had been clearly visible in the government bond markets of lower-rated jurisdictions, with spreads widening measurably and persistently, although there had been a considerable improvement on 18 March 2020. This likely reflected both expectations of further policy actions and the Eurosystem's increased presence in the market, as portfolio managers had started to implement the additional €120 billion purchase envelope approved by the Governing Council at its meeting of 11-12 March 2020.

Ms Schnabel concluded her presentation by noting that, as in sovereign bond markets, there had been a significant widening of spreads in euro area private credit markets, which threatened the orderly transmission of the ECB's monetary policy. The widening had been most pronounced in, but by no means confined to, high-yield corporate bonds. The widening of spreads in credit markets had been accompanied by significant net outflows from credit issued by non-financial corporates, with €2 billion having been withdrawn from euro area corporate bond markets in a matter of a few days. Market intelligence suggested that the Eurosystem's increased presence in the market had helped to prevent an even greater widening of sovereign and credit spreads.

Economic outlook and monetary policy options

Mr Lane observed that the coronavirus pandemic represented a collective public health emergency with few precedents in recent history. It was also an extreme economic shock that required an ambitious, coordinated and urgent policy reaction on all policy fronts to support those businesses and workers at risk. It was clear that economic activity across the euro area would decline considerably, especially as more countries would face the need to intensify containment measures. These measures would exert acute strains on the cash flows of companies and employees. It was also clear that it would add severe downside risks to the Governing Council's inflation outlook.

The Governing Council had taken carefully calibrated measures at its monetary policy meeting on 11-12 March 2020, but in conditions in which the scale of the challenges faced had not been sufficiently clear. At this juncture, the Governing Council needed to reassess the situation, which had rapidly evolved and was still evolving, and needed to judge whether the stance of monetary policy remained commensurate with the risk to the outlook.

While the outlook had worsened, indicators of financial conditions had tightened markedly, since financial markets had become severely dislocated and fragmented. The risk-free curve had shifted up and sovereign curves – key to the pricing of other assets in the economy – had become steeper and more dispersed. This tightened financial conditions at a time when the economy needed more support.

Against this background, Mr Lane proposed the following monetary policy measures to address the coronavirus crisis:

(a) first, to launch a new temporary asset purchase programme of private and public sector securities to counter the serious risks to the monetary policy transmission mechanism and the outlook for the euro area posed by the outbreak and escalating diffusion of the coronavirus (COVID-19): (i) this new pandemic emergency purchase programme (PEPP) would have an overall envelope of €750 billion, with purchases conducted for the rest of 2020, and would target all asset categories eligible under the current asset purchase programme (APP). For the fraction of purchases that would target eligible government bonds under the new programme, the benchmark allocation across jurisdictions would continue to be the capital key of the Eurosystem's national central banks. However, in deciding the modalities of intervention, the Executive Board should be able to adjust the operations under the new programme to allow for temporary fluctuations in the distribution of purchase flows both across asset classes and across jurisdictions. This flexible approach to the composition of purchases was essential in preventing the current dislocations in the aggregate euro area sovereign curve from translating into further distortions in the euro area risk-free curve, while also ensuring that the overall orientation of the programme covered all jurisdictions of the euro area; (ii) in line with modalities on the APP, the programme would be risk-shared for the part targeting private securities. For the public securities part, the same risk-sharing rule as under the PSPP would apply; (iii) furthermore, a waiver of the eligibility requirements for securities issued by the Greek government should apply under the PEPP; and (iv) the Governing Council would make the decision to terminate the new purchase programme once it was assessed that the coronavirus crisis phase was over;

(b) second, to expand the range of eligible assets under the corporate sector purchase programme (CSPP) to non-financial commercial paper, making all commercial paper of sufficient credit quality eligible for purchase under this programme; and

(c) third, to ease the collateral standards by adjusting the main risk parameters of the Eurosystem's collateral framework. In particular, the Governing Council would expand the scope of the framework in place for additional credit claims to include claims related to the financing of the corporate sector. This would ensure that counterparties could continue to make full use of the ECB's refinancing operations. The Governing Council should also signal that it stood ready to ease its collateral standards further, if needed.

As regards public communication, Mr Lane remarked that the Governing Council needed to: (a) stress that the ECB was committed to protecting all citizens of the euro area through this extremely challenging time. To that end, the ECB would ensure that all sectors of the economy could benefit from supportive financing conditions that enabled them to absorb this shock. This applied equally to families, firms, banks and governments; (b) pledge that it would do everything necessary within its mandate to deliver on this promise. This included being fully prepared to increase the size of the asset purchase programmes and adjust their composition by as much as necessary and for as long as needed, within the ECB's mandate. The Governing Council would explore all options and all contingencies to support the economy through this shock; (c) emphasise that, to the extent that some self-imposed limits might hamper action required to fulfil its mandate, the Governing Council would consider revising these to the extent necessary to make its action proportionate to the risks faced. This also applied to the terms and conditions put in place for the ECB's tools. The Governing Council would not tolerate any risks to the smooth transmission of its monetary policy across all jurisdictions in the euro area; and (d) make clear that it would terminate the programme once it assessed that the coronavirus crisis phase was over, but in any case not before the end of the year.

2. Governing Council's discussion and monetary policy decisions

In their subsequent exchange of views, members widely agreed with the assessment made by Ms Schnabel and Mr Lane with respect to the prevailing financial and economic situation. Since the monetary policy decisions taken at the 11-12 March Governing Council meeting, financial markets had been exhibiting extreme volatility, with signs of severe dislocation and rising fragmentation. Overall, financial conditions had continued to tighten as risk-free interest rates further increased across all maturities and sovereign and corporate spreads widened significantly, while equity markets had slumped. Moreover, the likely deterioration in the outlook for economic activity and inflation and the accompanying drop in inflation expectations could lead to an increase in real interest rates, running the risk that financial conditions would tighten in a procyclical manner at a time when the economy required easier conditions to cope with the current shock.

Similarly, the economic situation was seen to be deteriorating rapidly. The strict containment measures being put in place throughout the euro area were leaving a profound mark on the economy as firms and households scaled back production and spending. This was evidenced by some of the latest economic indicators, which were starting to signal material declines in economic activity and employment. Hence, it was judged that economic growth across the euro area would decline considerably. While the full extent and duration of the consequences of the coronavirus for the economy were difficult to predict at this juncture and would only gradually become clear over time, there was a significant risk of a major recession in the euro area. The worsening economic outlook, together with lower oil prices and declining inflation expectations, also introduced significant downside risks to the euro area inflation outlook.

In view of the rapid deterioration in the environment since the 11-12 March Governing Council meeting, all members agreed that a further forceful monetary policy response was warranted. Broad support was expressed for the package of measures proposed by Mr Lane, with some nuances of views regarding specific elements of the proposal.

There was unanimous agreement that bold and decisive action was needed to counter the serious risks posed by the rapidly spreading coronavirus for the monetary policy transmission mechanism, the outlook for the euro area economy and, hence, ultimately the ECB's price stability objective. Since the Governing Council's meeting on 11-12 March it had become evident that the euro area was facing a common shock that severely affected economic outcomes across all euro area jurisdictions. This clearly justified a forceful monetary policy response and required additional policy stimulus and support to monetary policy transmission to be provided only a week after the Governing Council's decision on the previous policy package. A strong response was also seen to underline the credibility of the ECB's commitment to use all of its monetary policy instruments to prevent destabilising and self-perpetuating spirals that could disrupt financial markets and put financial and price stability at risk.

A large majority of members supported the proposal by Mr Lane to launch a new pandemic emergency purchase programme (PEPP) for private and public sector securities with an envelope of €750 billion until the end of the year. Such a temporary programme, targeting the specific consequences of the spread of the coronavirus, was seen as the most appropriate response to address a severe and common shock of unprecedented proportions that affected the euro area economy as a whole. The amount of €750 billion would add to the envelope of €120 billion decided at the 11-12 March meeting and, hence, provide a powerful response to counter the serious risks to the monetary policy transmission mechanism and the outlook for the euro area. The size and duration of the new programme was seen to be proportionate to the risks that the Governing Council was facing, in full respect of its price stability mandate. It was also noted that the additional asset purchases would effectively complement actions by euro area governments, while respecting the Treaty provision on the separation between monetary policy and fiscal policy.

Members broadly supported the proposal that purchases would be conducted in a flexible manner, while the benchmark allocation for public securities across jurisdictions would continue to be the capital key of the Eurosystem's national central banks. A flexible purchase strategy would allow for fluctuations in the distribution of purchase flows over time, across asset classes and among jurisdictions to address financial fragmentation and market distortions, while also enabling purchases to be tailored to the ramifications of the coronavirus pandemic. In this context, it was also seen as welcome that the eligibility requirements for securities issued by the Greek government would be waived under the PEPP. Given the common nature of the shock, this was seen as an important measure to support the effective transmission of monetary policy in all segments of euro area bond markets. The granting of the waiver was also considered to reflect the compliance of the Greek government with the commitments made under the enhanced surveillance framework monitored by the EU institutions.

Reservations were expressed by some members about the necessity of launching a new, dedicated asset purchase programme. While these members concurred with the clear need for action, they expressed a preference for employing the existing toolkit of the Governing Council, such as scaling up the current APP or considering Outright Monetary Transactions (OMTs).

However, overall it was widely felt that the APP would be less suitable, given the large-scale and common, but temporary, nature of the shock. Regarding the OMTs, the programme had been designed to address a fundamentally different contingency, that of safeguarding the singleness of the ECB's monetary policy in the event of severe tensions in the government bond markets of one or several euro area countries which originated, in particular, from unfounded fears over the reversibility of the euro.

The current situation was generally seen to be rather different. The coronavirus represented a global and common shock that affected financing conditions and the macroeconomic outlook throughout the euro area. The situation thus called for monetary policy action that would, first, provide immediate support to stabilise market conditions and, second, ensure an appropriate stance of monetary policy across the euro area.

In this context a remark was made that, alternatively, consideration could be given to a cut in official interest rates as part of the policy package, since part of the tightening of financial conditions was due to an upward move in the risk-free curve. Furthermore, a suggestion was made that the Governing Council could flag that additional asset classes could in the future be accommodated within the scope of the proposed purchase programme, beyond the inclusion of commercial paper, or that rating thresholds could be lowered for private paper in order to expand the eligible universe.

Members widely agreed with the proposal made by Mr Lane to expand the eligible purchase space in the CSPP, as well as under the PEPP, to allow for purchases of commercial paper of sufficient credit quality. Enlarging the set of purchasable bonds issued by corporates was viewed as a measure that would directly support the funding situation of companies, thereby providing crucial assistance to the part of the economy that was being hit hard by the containment measures designed to halt the spread of the coronavirus. There was also broad agreement on easing the collateral standards for the Eurosystem's refinancing operations. In particular, the scope of the additional credit claims could be expanded to include claims related to the financing of the corporate sector. This was seen as a way of ensuring that counterparties had sufficient collateral and could make full use of the Eurosystem's credit operations, while providing incentives to banks to extend credit to the real economy.

As regards communication, members broadly supported the lines of communication suggested by Mr Lane in his introduction. It had to be underlined that the ECB was acting in pursuit of its price stability mandate, as the deterioration in the economic outlook, falling inflation expectations and tightening financing conditions across asset classes and maturities posed a serious risk to the Governing Council's medium-term price stability objective. It needed to be highlighted that the coronavirus pandemic represented a severe and exceptional shock to the euro area economy that warranted an equally exceptional and resolute policy response. In this context, the PEPP, which was temporary in nature and targeted to the specific shock and contingency at hand, was seen as an appropriate course of policy action, proportionate to the risks faced. A powerful policy response was indeed warranted to address dislocations in financial markets, supporting the transmission of monetary policy to ease funding conditions for the euro area real economy. At the same time, acknowledging the ultimately temporary nature of the coronavirus-related shock, it had to be highlighted that – in compliance with the proportionality principle – the Governing Council would end net asset purchases under the PEPP once it judged that the coronavirus crisis phase was over, but in any case not before the end of the year.

Members stressed that the ECB was fully committed to playing its role in supporting all euro area citizens through this extremely challenging time. To that end, the ECB would ensure that all sectors of the economy could benefit from supportive financing conditions that enabled them to absorb this shock. Against that background, it had to be reiterated that the Governing Council would do everything necessary within its mandate. This included the Governing Council being fully prepared to increase the size of its asset purchase programmes and adjust their composition, by as much as necessary and for as long as needed. This also included the Governing Council's commitment to adjust all of its other instruments, as appropriate, including adjusting its policy rates in line with its forward guidance.

Members largely supported the proposal by Mr Lane to signal that, to the extent that self-imposed limits might hamper action that was needed to fulfil its mandate, the Governing Council would consider revising the limits to the extent necessary to make its action proportionate to the risks faced. It had to be stressed that the Governing Council would support the smooth transmission of its monetary policy in all jurisdictions of the euro area. At the same time, it was underlined that the Governing Council's policy actions had to remain clearly within its remit and fully proportionate to the risks to the ECB's price stability mandate. It was also noted that new debt issuance by euro area governments, agencies and European institutions in view of increased financing needs to support the economy was likely to alleviate potential feasibility constraints implied by the current purchase parameters set for the APP.

Reservations were, however, expressed by some members with regard to the proposed communication on the issue share and issuer limits. It was recalled that these limits were one of the safeguards to ensure that the Governing Council acted within its mandate. Moreover, at present there appeared to be sufficient scope in the evolution of the purchasable universe to avoid a premature discussion on a possible lifting of these limits, which could imply incurring a higher risk of being perceived as getting closer to monetary financing. However, notwithstanding the hesitation, readiness was also expressed to go along with the carefully phrased communication, in the light of the scale of the market disruptions and challenges faced in the pursuit of the ECB's mandate.

Finally, other policy actors, including fiscal authorities and other policy institutions, were called upon to act in an ambitious and coordinated fashion to effectively complement the Governing Council's policy measures in combating the coronavirus crisis. While it was welcome that fiscal measures had been announced and taken at the national level, joint and concerted action at the euro area level was still lacking. Coordinated and timely policy action by governments and European institutions, including banking supervision, was needed to address the public health challenge of containing the spread of the coronavirus and mitigate its economic impact, supporting businesses and workers at risk. This also comprised further specific and decisive steps to strengthen the institutional framework of Economic and Monetary Union, including through more unified fiscal measures.

Taking into account the foregoing discussion among the members, the Governing Council decided on the following comprehensive package of monetary policy measures:

1. To launch a new temporary asset purchase programme of private and public sector securities to counter the serious risks to the monetary policy transmission mechanism and the outlook for the euro area posed by the outbreak and escalating diffusion of the coronavirus (COVID-19).This new pandemic emergency purchase programme (PEPP) would have an overall envelope of €750 billion. Purchases would be conducted until the end of 2020 and would include all the asset

categories eligible under the existing APP.For the purchases of public sector securities, the benchmark allocation across jurisdictions would continue to be the capital key of the Eurosystem's national central banks. At the same time, purchases under the new PEPP would be conducted in a flexible manner. This would allow for fluctuations in the distribution of purchase flows over time, across asset classes and among jurisdictions.A waiver of the eligibility requirements for securities issued by the Greek government would be granted for purchases under the PEPP.The Governing Council would terminate net asset purchases under the PEPP once it judged that the coronavirus crisis phase was over, but in any case not before the end of the year.

2. To expand the range of eligible assets under the CSPP to non-financial commercial paper, making all commercial paper of sufficient credit quality eligible for purchase under the CSPP.

3. To ease the collateral standards by adjusting the main risk parameters of the collateral framework. In particular, the scope of the framework in place for additional credit claims would be expanded to include claims related to the financing of the corporate sector. This would ensure that counterparties could continue to make full use of the Eurosystem's refinancing operations.

Press release

https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200318_1~3949d6f266.en.html

Meeting of the ECB's Governing Council, 18 March 2020

Members

- Ms Lagarde, President
- Mr de Guindos, Vice-President
- Mr Costa
- Mr Hernández de Cos
- Mr Herodotou
- Mr Holzmann *

- Mr Kazāks
- Mr Kažimír
- Mr Knot
- Mr Lane
- Mr Makhlouf
- Mr Mersch
- Mr Müller
- Mr Panetta
- Mr Rehn
- Mr Reinesch *
- Ms Schnabel
- Mr Stournaras
- Mr Vasiliauskas
- Mr Vasle
- Mr Vella *
- Mr Villeroy de Galhau
- Mr Visco *
- Mr Weidmann
- Mr Wunsch

* Members not holding a voting right in March 2020 under Article 10.2 of the ESCB Statute.

Other attendees

- Ms Senkovic, Secretary, Director General Secretariat

- Mr Smets, Secretary for monetary policy, Director General Economics

Other ECB staff

- Ms Graeff, Director General Communications
- Mr Straub, Counsellor to the President
- Ms Rahmouni-Rousseau, Director General Market Operations
- Mr Rostagno, Director General Monetary Policy

CONTACT

European Central Bank

Directorate General Communications

- Sonnemannstrasse 20
- 60314 Frankfurt am Main, Germany
- +49 69 1344 7455
- media@ecb.europa.eu

Media contacts