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The euro area economic outlook and completion of EMU

CIO CFO Conference

Paris, 15 June 2018

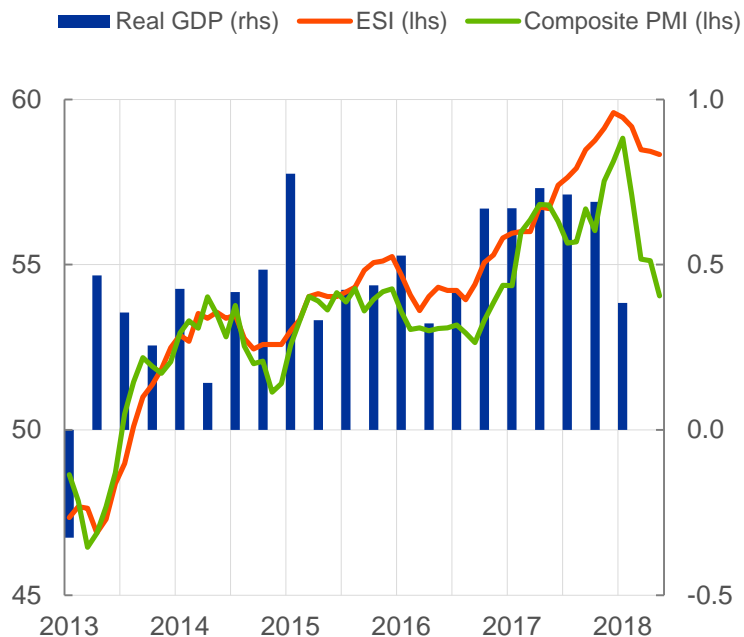**A**   **Euro area economic outlook**

B   Recent monetary policy measures

C   Completing economic and monetary union

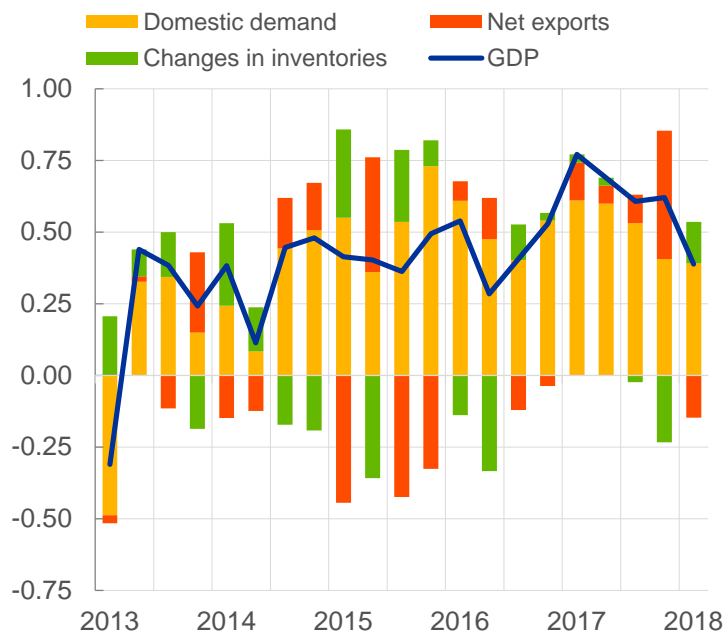# Solid economic expansion driven mainly by domestic demand

Real GDP growth and survey indicators
(lhs: diffusion index; rhs: q-o-q % change)

Legend: ■ Real GDP (rhs) — ESI (lhs) — Composite PMI (lhs)

Euro area real GDP composition
(q-o-q growth rate, q-o-q pp. contributions)

Legend: ■ Domestic demand ■ Net exports ■ Changes in inventories — GDP
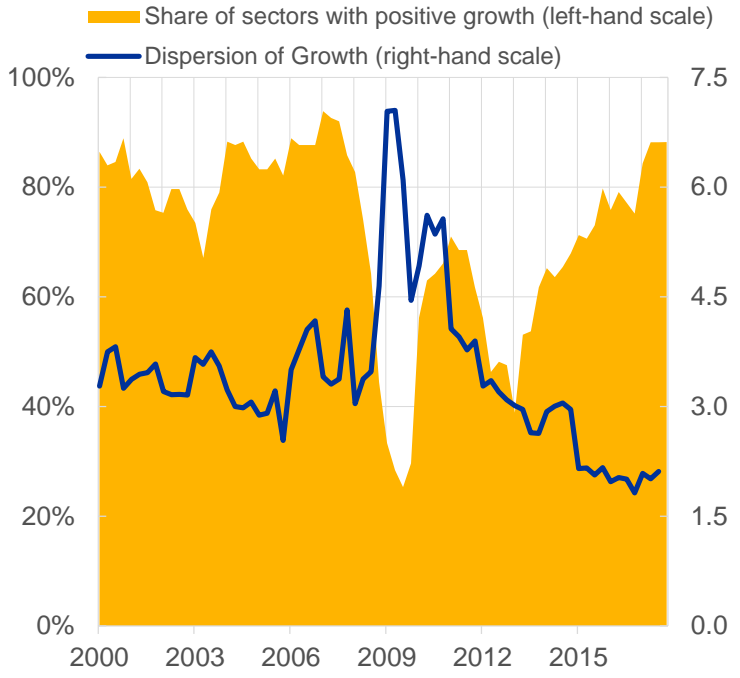
Sources: Eurostat, Markit, European Commission, ECB calculations.
Notes: ESI stands for European Commission Sentiment Indicator.
Latest observations: 2018Q1 for GDP, May 2018 for ESI and PMI.

Sources: Eurostat and ECB staff calculations.
Latest observation: 2018Q1.

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Broad-based expansion, both within the euro area and globally

Dispersion of euro area value-added growth
(lhs-axis: percentages, rhs-axis: percentage points)

Share of countries globally with real GDP growth exceeding past three-year average
(in percent)

Legend:
- Share of sectors with positive growth (left-hand scale)
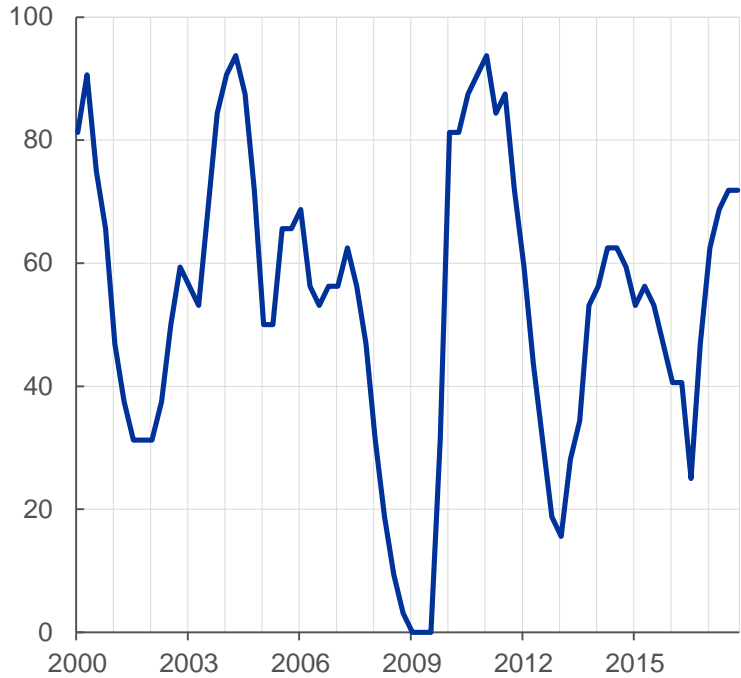- Dispersion of Growth (right-hand scale)

Sources: Eurostat and ECB calculations.
Notes: The share of sectors with positive growth is constructed as the percentage of the 162 country-sector pairs that reported positive year-on-year growth in value added. The dispersion of growth is measured as the weighted standard deviation of year-on-year growth in value added in the same 162 country-sector pairs. The latest observation is for 2017Q4.
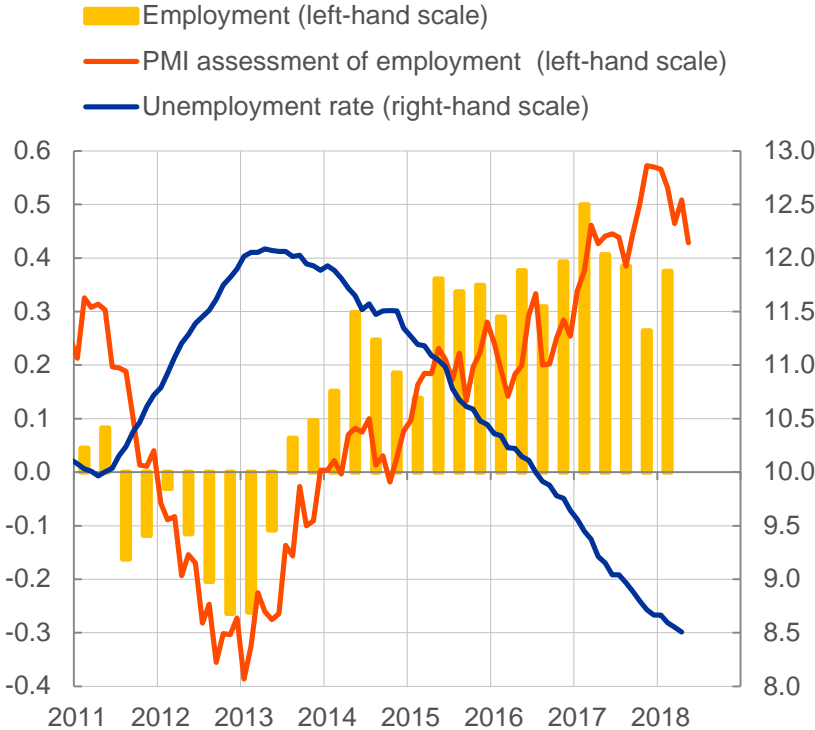
Source: ECB calculations.
Notes: Annual GDP growth rate is calculated for 31 countries and the euro area, accounting for 92% of global GDP in PPP. Last observation is 2017Q4.

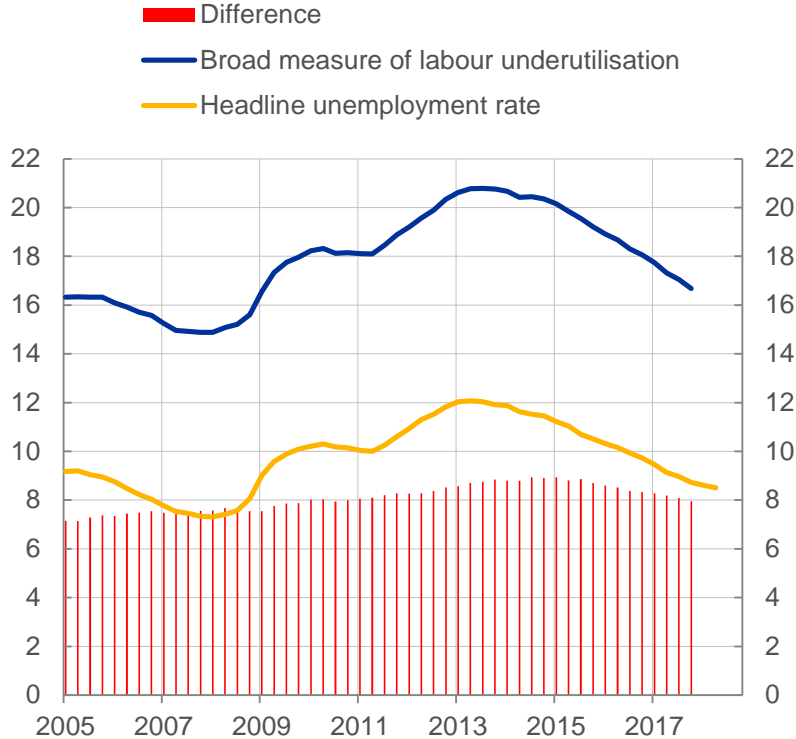# Strong employment growth but labour market slack remains

Employment growth, PMI assessment of employment and the unemployment rate
(quarter-on-quarter percentage changes; diffusion index; percentage of labour force)

- Employment (left-hand scale)
- PMI assessment of employment (left-hand scale)
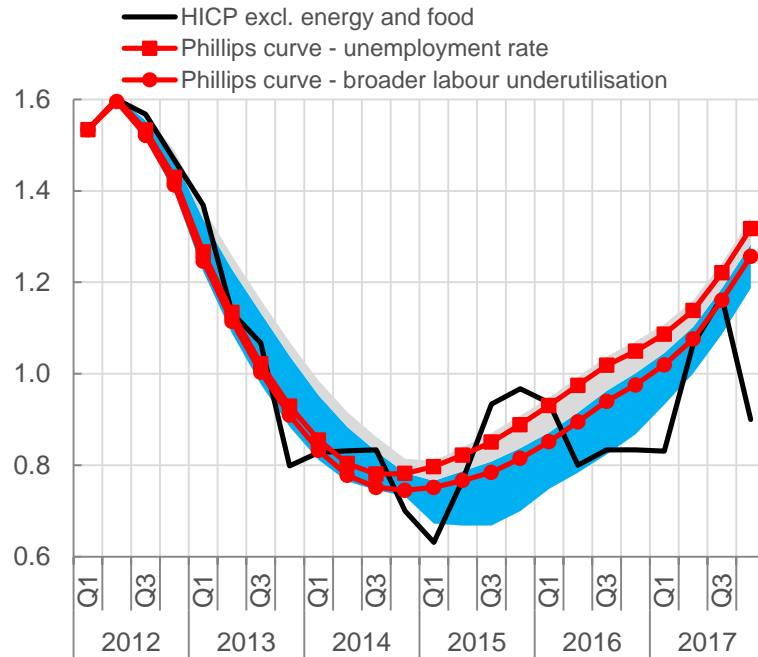- Unemployment rate (right-hand scale)

Sources: Eurostat, Markit and ECB staff calculations.
Note: The PMI index is expressed as a deviation from 50 and divided by 10. Last observations: 2018Q1 for employment, 2018 April for the unemployment rate and May 2018 for the PMI.
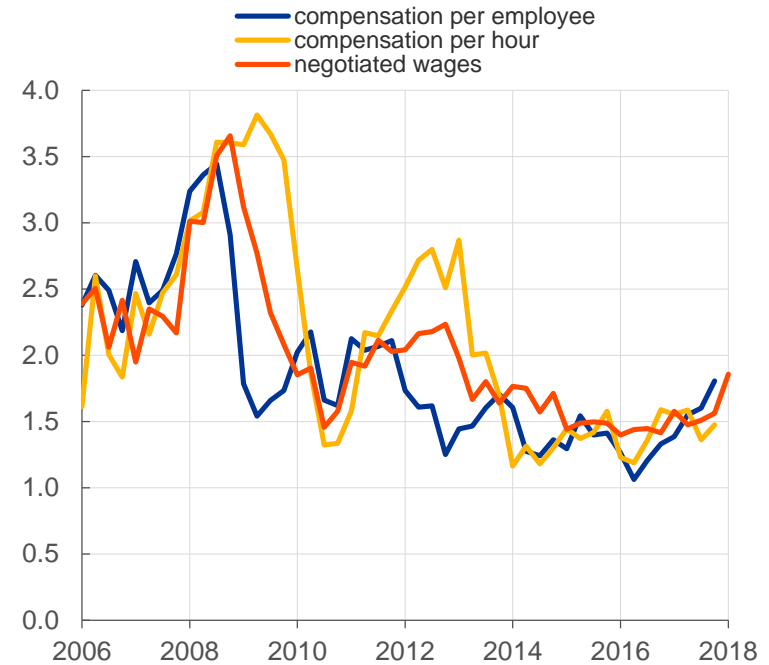
Unemployment rate and the broad measure of labour underutilisation
(percentages of the respective labour force)

- Difference
- Broad measure of labour underutilisation
- Headline unemployment rate

Source: Eurostat, LFS and ECB Staff calculations.
Latest observations: 2018 April for the unemployment rate and 2017Q4 for the broad measure of labour underutilisation.
Note: Seasonally adjusted data. The broad measure of labour underutilisation contains the unemployed, the underemployed part-time workers, those available to work but not seeking, and those seeking work, but not available and is expressed as a share of the extended labour force. Data have been corrected for methodological changes and backcast by ECB Staff. Age group 15-74.

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Broader slack measures more consistent with inflation and wage developments

Underlying inflation: actual and conditional out-of-sample projection
(annual percentage changes)

Sources: Eurostat, Consensus Economics, SPF and ECB calculations.
Notes: The parameters are estimated over the sample 1999Q1 to 2017Q4. The conditional out-of-sample forecast is done for 2012Q2 to 2017Q4. The grey (blue) range depicts forecasts for HICP excl. energy and food coming from Phillips curve specifications that are based on constant parameters and include permutations across the expectation formation either backward- or forward-looking and the unemployment rate (broader measure of labour underutilization) as slack measure. The red lines are all based on constant parameters and backward-looking expectation formation. The following inflation expectations measures are included: Consensus measures with a horizon from 2 to 7 quarters ahead, SPF 1 year ahead, SPF 2 years ahead and SPF 5 years ahead.

Wage developments in the euro area
(annual percentage changes)

Sources : Eurostat, National Accounts.
Latest Observations: 2018Q1 for negotiated wages, and 2017Q4 for all other.

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Inflation expected to convergence durably to levels closer to 2%

HICP and HICP excluding energy and food
(annual percentage changes)
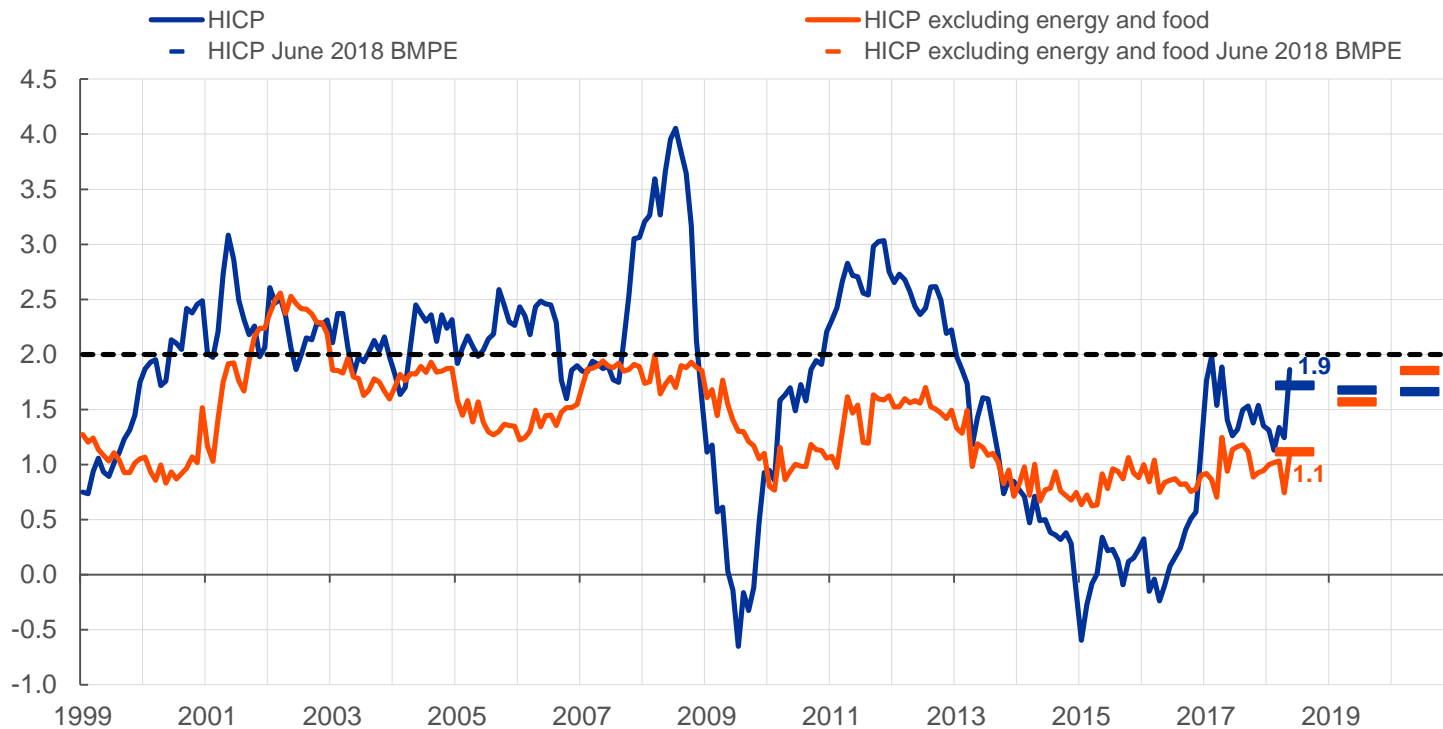
Source: Eurostat and June 2018 BMPE.
Latest observation: May 2018 (flash estimates) for HICP and HICP excluding energy and food.
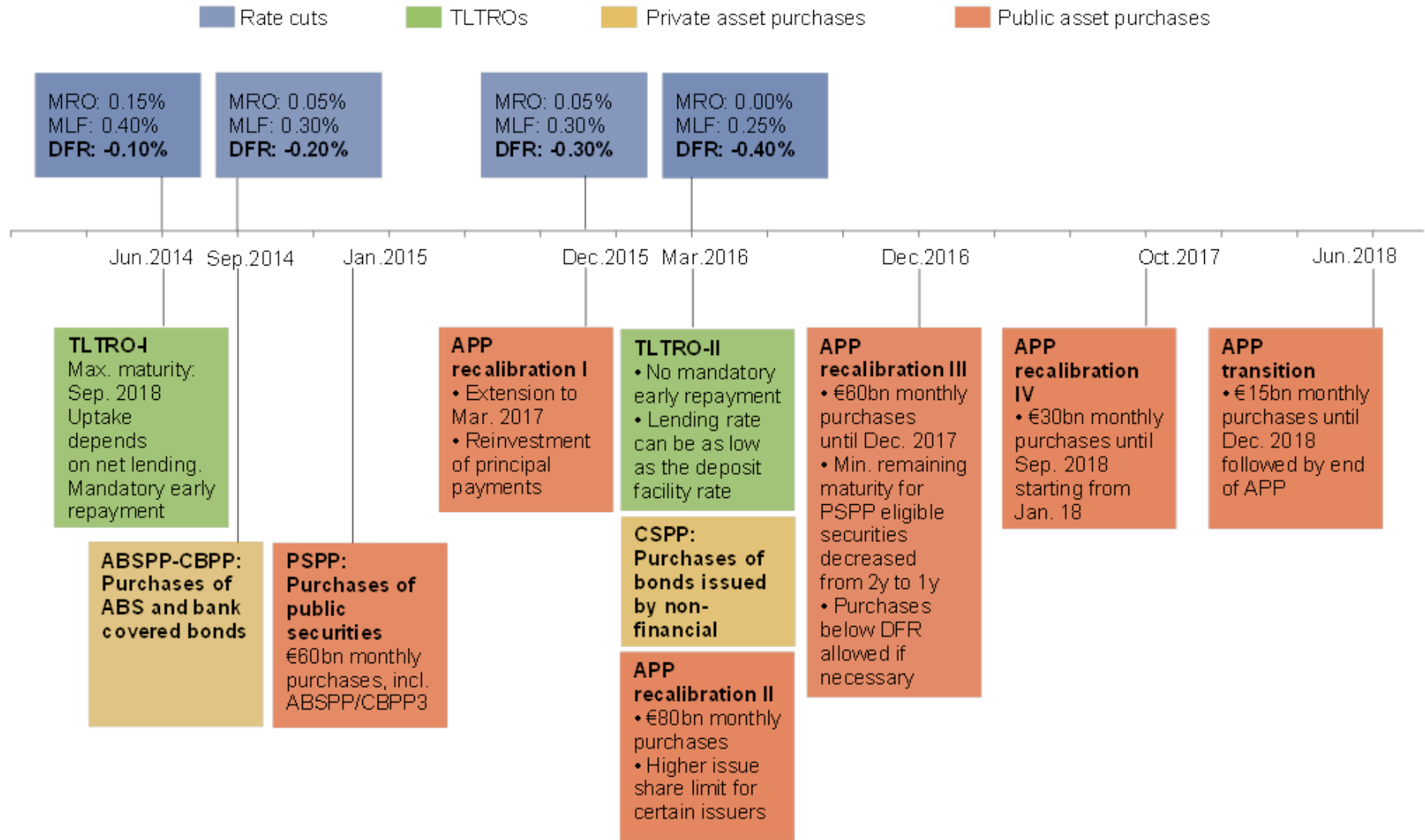
A	Euro area economic outlook
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Recent monetary policy measures (2014 – 2018)

Legend: Rate cuts — TLTROs — Private asset purchases — Public asset purchases

Rate cut boxes (above timeline):

- MRO: 0.15%
  MLF: 0.40%
  DFR: -0.10%

- MRO: 0.05%
  MLF: 0.30%
  DFR: -0.20%

- MRO: 0.05%
  MLF: 0.30%
  DFR: -0.30%

- MRO: 0.00%
  MLF: 0.25%
  DFR: -0.40%

Timeline: Jun.2014 — Sep.2014 — Jan.2015 — Dec.2015 — Mar.2016 — Dec.2016 — Oct.2017 — Jun.2018

TLTRO-I
Max. maturity:
Sep. 2018
Uptake
depends
on net lending.
Mandatory early
repayment

ABSPP-CBPP:
Purchases of
ABS and bank
covered bonds

PSPP:
Purchases of
public
securities
€60bn monthly
purchases, incl.
ABSPP/CBPP3

APP
recalibration I
• Extension to
Mar. 2017
• Reinvestment
of principal
payments

TLTRO-II
• No mandatory
early repayment
• Lending rate
can be as low
as the deposit
facility rate

CSPP:
Purchases of
bonds issued
by non-
financial

APP
recalibration II
• €80bn monthly
purchases
• Higher issue
share limit for
certain issuers

APP
recalibration III
• €60bn monthly
purchases
until Dec. 2017
• Min. remaining
maturity for
PSPP eligible
securities
decreased
from 2y to 1y
• Purchases
below DFR
allowed if
necessary

APP
recalibration
IV
• €30bn monthly
purchases until
Sep. 2018
starting from
Jan. 18

APP
transition
• €15bn monthly
purchases until
Dec. 2018
followed by end
of APP

Notes: MRO = Main refinancing operations, MLF = Marginal lending facility, DFR= Deposit facility rate

# Policy measures compressed borrowing rates and boosted bank lending

Composite indicator of the nominal cost of bank borrowing for NFCs
(percentage)

MFI loans to non-financial corporations
(annual percentage changes)
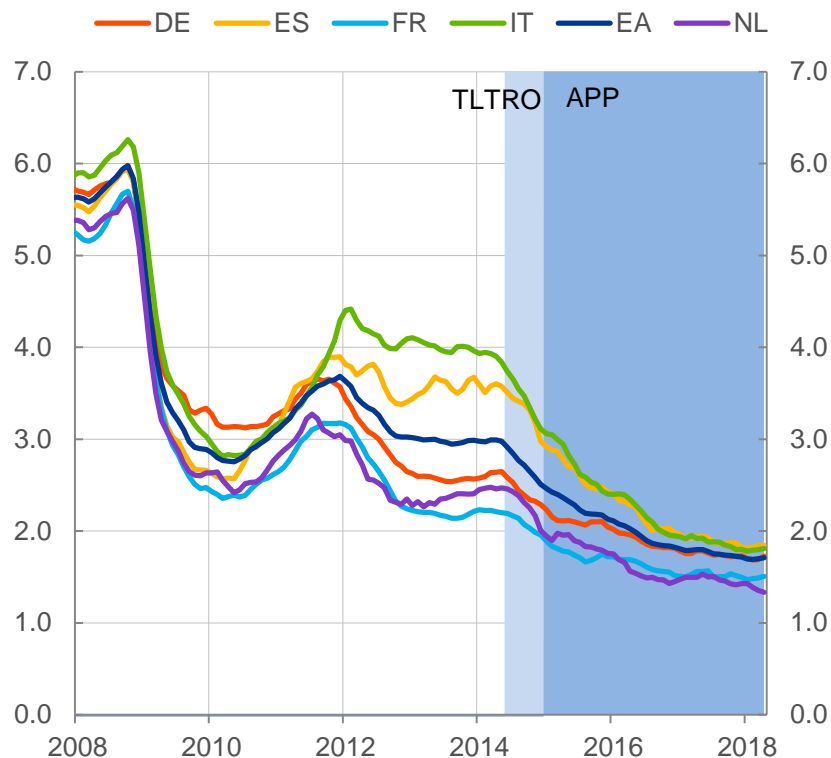
Source: ECB.
Notes: The indicator for the total cost of bank borrowing is calculated by aggregating short- and long-term rates using a 24-month moving average of new business volumes.
Latest observation: April 2018.
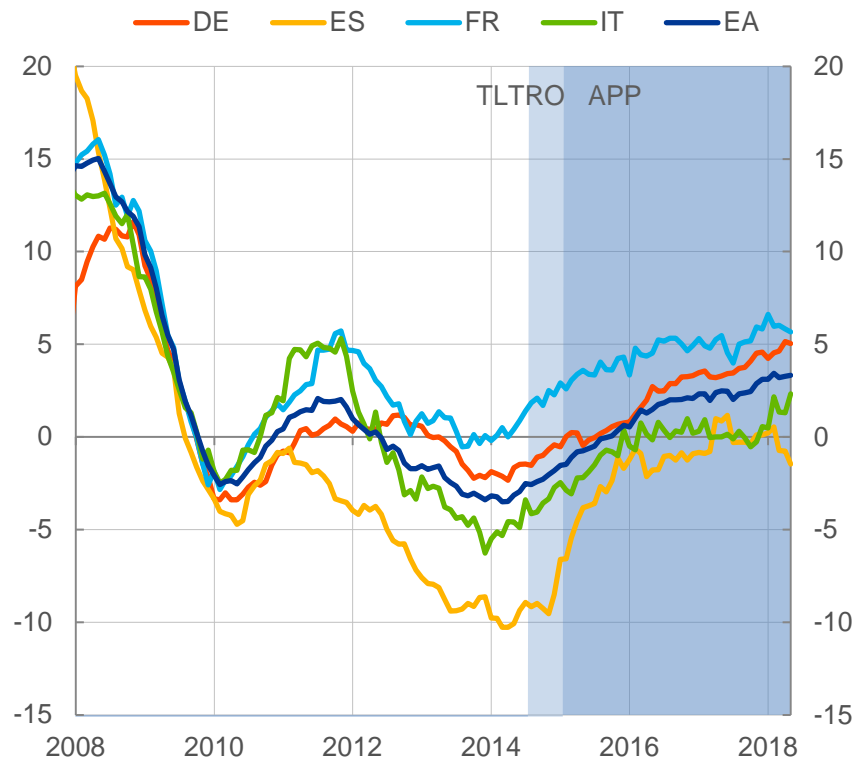
Source: ECB.
Notes: Adjusted loans (i.e. adjusted for sales, securitisation and cash pooling activities). Non-seasonally adjusted data.
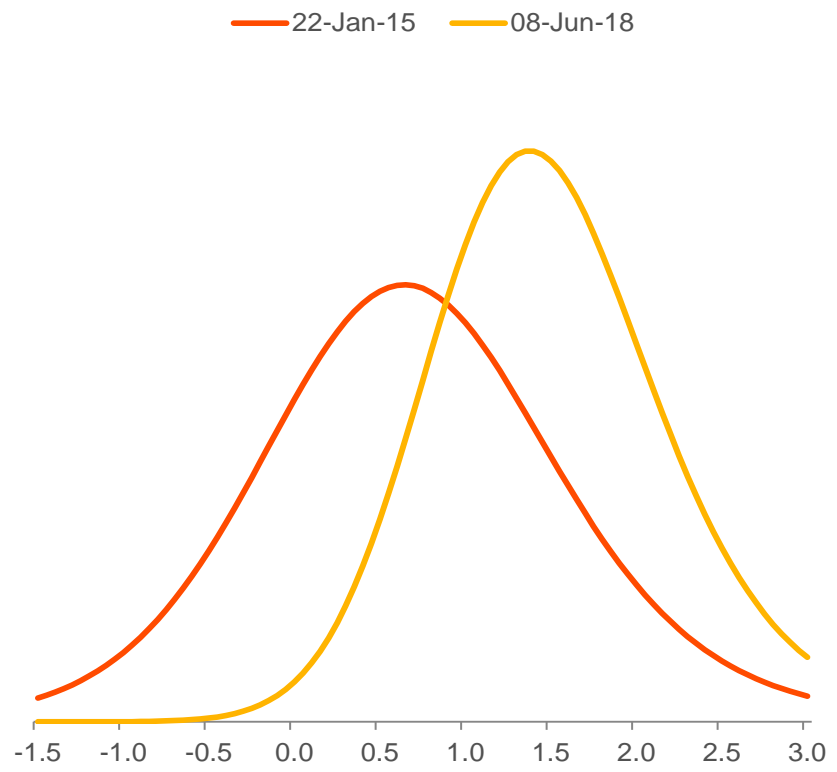Latest observation: April 2018.

Sizeable impact of policy on inflation prospects

Inflation, inflation projections and impact of measures on inflation
(annual percentage changes)

Legend:
- ⊢—⊣ max-min range w/o measures
- ◆ median w/o measures
- —— HICP annual
- ▬ HICP quarterly

Risk neutral density function of euro area inflation over next five years
(probability percentage)

Legend:
- —— 22-Jan-15
- —— 08-Jun-18

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Completing EMU: priorities for the short and long term

Priorities for the June Council

- **Complete Banking Union**
  - Establish a backstop for the SRF, both for solvency and liquidity support
  - Agree on a step-wise introduction of a fully mutualised EDIS
- **Reform the ESM**
  - Make it more agile and effective
- **Fiscal capacity**
  - Agree to continue working on the design of a euro area fiscal capacity

Priorities for the longer term

- **Complete Capital Markets Union**
- **Economic Union**
  - Initiate a more binding 'convergence process'
  - More effective use of the Macro-Economic Imbalance Procedure
- **Fiscal union**
  - Simplify fiscal rules and enhance their implementation
  - Work towards the introduction of a euro area fiscal capacity (which may include the joint financing of common public goods, steps towards coordinating/harmonising tax policies and a stabilisation capacity) under European democratic control

Thank you