European Central Bank: Press conference - introductory statement

Introductory statement by Mr Jean-Claude Trichet, President of the European Central Bank, Frankfurt am Main, 6 April 2006.

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Ladies and gentlemen, let me welcome you to our press conference and report on the outcome of today's meeting of the ECB's Governing Council. The meeting was also attended by Commissioner Almunia.

On the basis of our regular economic and monetary analyses, we have decided to keep the **key ECB interest rates** unchanged, following the increase of 25 basis points on 2 March 2006. The information which has become available since then confirms our assessment that a further adjustment of our accommodative monetary policy stance was warranted to address upside risks to price stability. It remains essential to ensure that medium to long-term inflation expectations in the euro area are kept solidly anchored at levels consistent with price stability. Such anchoring of inflation expectations is a prerequisite for monetary policy to make an ongoing contribution towards supporting economic growth and job creation in the euro area. With interest rates across the whole maturity spectrum still at very low levels in both nominal and real terms, and monetary and credit growth remaining strong and liquidity ample, our monetary policy remains accommodative. We will continue to monitor very closely all developments to ensure that risks to price stability over the medium term do not materialise.

Turning first to the **economic analysis**, recent information has confirmed our assessment of an improved outlook for economic growth in the euro area, following the more subdued developments in late 2005. On the basis of the latest data, survey releases and various indicator-based estimates, it appears that growth is strengthening and broadening in the first half of 2006. Indeed, the conditions remain in place for solid growth over the coming quarters. Activity in the world economy remains strong, providing support for euro area exports. Investment activity is expected to remain solid, benefiting from an extended period of very favourable financing conditions, balance sheet restructuring, and accumulated and ongoing gains in earnings and business efficiency. Consumption growth should also strengthen over time, in line with developments in real disposable income, as the labour market situation continues to gradually improve. This outlook for economic activity is also confirmed by available forecasts from international organisations and private sector institutions.

The risks to economic growth appear to be broadly balanced over the shorter term. Further ahead, downside risks still relate to potential increases in oil prices and concerns about global imbalances.

Turning to price developments, according to Eurostat's flash estimate, annual HICP inflation was 2.2% in March 2006, compared with 2.3% in February and 2.4% in January. In the short run, inflation rates are likely to remain above 2%, with the precise levels depending largely on developments in the more volatile components of the index. Beyond the short term, changes in administered prices and indirect taxes are expected to significantly affect inflation in 2006 and 2007, and an upward impact may also be expected from the indirect effects of past oil price increases. At the same time, wage dynamics in the euro area have remained moderate over recent quarters and growth in wages is expected to remain contained, partly reflecting strong global competitive pressures, particularly in the manufacturing sector. Over the recent past, moderate wage trends have helped to dampen domestic inflationary pressures; looking ahead, it is crucial that the social partners continue to meet their responsibilities in this regard, also in the context of a more favourable economic environment.

Risks to the outlook for price developments remain on the upside and include further increases in oil prices, a possibly stronger pass-through of oil price rises into consumer prices than currently anticipated, additional increases in administered prices and indirect taxes, and – more fundamentally – stronger wage and price developments than expected due to second-round effects of past oil price increases.

Turning to the **monetary analysis**, the latest developments confirm that the stimulative impact of the low level of interest rates remains the dominant factor behind the high trend rate of monetary expansion. Moreover, the annual growth rate of credit to the private sector has continued to increase over recent months, with borrowing by households – especially loans for house purchase – and non-financial corporations rising rapidly. Overall, strong monetary and credit growth in an environment of ample liquidity in the euro area continues to point to upside risks to price stability over the medium to longer term.

To sum up, annual inflation rates are projected to remain elevated in 2006 and 2007, and the economic analysis indicates that the risks to price stability remain on the upside. Given the strength of monetary growth and the ample liquidity situation in a context of improving economic activity, **cross-checking** the outcome of the economic analysis with that of the monetary analysis supports the assessment that upside risks to price stability over the medium to long term prevail. It is essential that medium-term inflation expectations remain firmly anchored at levels consistent with price stability. Accordingly, the Governing Council will continue to monitor very closely all developments to ensure that risks to price stability do not materialise, thereby making an ongoing contribution to sustainable economic growth and job creation.

As regards **fiscal policies**, while the budgetary results reported for 2005 are mostly better than anticipated a few months ago, the budget balances planned for 2006 imply no significant progress in fiscal consolidation for the euro area as a whole. Given the economic outlook, a faster pace of deficit reduction is necessary. Delaying fiscal consolidation in times of improving economic activity implies risks for the medium term, as has been observed in the past. Speeding up deficit reduction on the basis of credible and fully specified measures as part of a comprehensive reform programme would help to enhance confidence in the medium-term prospects of the euro area and prevent a repeat of past experiences, when complacency in good times contributed to persistent budgetary disequilibria.

As regards **structural reforms**, the Governing Council welcomes the call by the European Council, which met in Brussels on 23-24 March 2006, to maintain the momentum of the re-launched Lisbon strategy for growth and employment. As emphasised by the European Council, the focus should now be on ensuring the effective, timely and comprehensive implementation of the measures agreed in the national reform programmes presented by Member States and, if necessary, on strengthening them. These measures are designed to, among other things, enhance the sustainability and quality of public finances, promote flexible labour and product markets, support a favourable business environment, and ensure a fully operational EU internal market, including the markets for energy and services. Applying comprehensive structural reforms is of particular importance for the euro area countries, in order to increase wage and price flexibility and the resilience to shocks, facilitate structural adjustment, raise potential output growth and job creation, and reduce price pressures, thereby facilitating the task of the single monetary policy.

We are now at your disposal for questions.