Jean-Claude Trichet: Hearing at the Committee on Economic and Monetary Affairs of the European Parliament

Introductory statement by Mr Jean-Claude Trichet, President of the European Central Bank, at a hearing at the Committee on Economic and Monetary Affairs of the European Parliament, Brussels, 29 August 2011.

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Dear Madam Chair,

Dear Honourable Members,

Thank you very much for the invitation to the exchange of views today. You asked me to begin with a brief overview of the main recent economic and monetary developments in the euro area and recent monetary policy decisions.

I. Economic and monetary developments

Incoming information since our last regular hearing in June continue to point towards ongoing growth in the euro area, although – as expected – at a slower pace. After a strong increase of 0.8% quarter-on-quarter in the first quarter of 2011, partly due to special factors, real GDP growth decelerated to 0.2% quarter-on-quarter in the second quarter. Looking ahead, we continue to see the euro area economy growing at a modest pace in a context of overall relatively sound economic fundamentals for the euro area as a whole. At the same time, not least because of the recently re-emerged tensions in financial markets, uncertainty remains particularly high. This mainly relates to ongoing fiscal and economic adjustment in a number of euro area countries and most other advanced economies, as well as the overall outlook for the global economy. In particular, the United States has been facing both fiscal and structural headwinds amidst weakened economic prospects.

Inflation in the euro area has remained elevated for some months, mainly driven by commodity prices. We expect to see inflation still above 2% over the months ahead. Risks to the medium-term outlook for price developments are under study in the context of the ECB staff projections that will be released early September.

Our monetary analysis indicates that the underlying pace of monetary expansion remains moderate but monetary liquidity remains ample, with the potential to accommodate price pressures. At the same time, monetary liquidity is likely to be held more for precautionary reasons rather than for spending purposes.

The Governing Council of the ECB is determined to ensure that inflation expectations continue to be firmly anchored in line with our aim of keeping inflation rates below, but close to, 2% over the medium term.

II. Recent measures taken in response to the intensification of the crisis early August

Let me turn to our response to the deterioration in financial markets in the second half of July and early August in the euro area and elsewhere. Notably, in the euro area the renewed intensification of financial market turbulence led to very high interest rates, potentially damaging volatility and very low trading volumes in some government bond markets that at times ceased to function appropriately. The tensions to some extent resembled those observed in May 2010, but in some aspects they were more broad-based than what we had seen at that time.

In view of these developments, the ECB decided earlier this month to continue conducting its refinancing operations as fixed-rate tender procedures with full allotment, at least until mid-January 2012. "Full allotment" means that the Eurosystem fulfils, against collateral, in full the liquidity demands by any participating bank in our refinancing operations. Currently, the outstanding Eurosystem credit in our refinancing operations amounts to about € 530 billion, which is provided in operations ranging from 1 week to 6 months. We decided in early August to conduct one refinancing operation with a maturity of approximately six months to help banks in their liquidity planning, and enhance support for their lending to households and corporations. Currently about 470 banks participate as counterparts in our refinancing operations; and over 6,000 banks are potentially eligible. The total value of marketable securities eligible for Eurosystem credit operations is about € 14,000 billion (as of 31 December 2010; source: ECB Annual Report). Therefore, there is no liquidity or collateral shortage for the European banking system.

The ECB resumed government bond market interventions within its Securities Markets Programme (SMP) in August. Via its securities interventions, the ECB Governing Council aims at helping to restore a more appropriate transmission of its monetary policy stance in an environment in which some market segments are dysfunctional. The interventions do not influence our monetary policy stance. In order to sterilise the impact of these interventions on the liquidity conditions in the banking system, we re-absorb the liquidity injected.

On the broader context of this programme, let me quote what I said in May 2010[1]: "Our actions are in full compliance with the prohibition of monetary financing and thus with our financial independence. The Treaty prohibits the direct purchase by the ECB of debt instruments from governments. We are buying bonds on the secondary market only, and we stick to the principles of the Treaty, which are price stability, our primary mandate, and central bank independence. We expect from governments strict respect for the principle of budgetary discipline and effective mutual surveillance.

The purchases made on the secondary market cannot be used to circumvent the fundamental principle of budgetary discipline. The Securities Markets Programme strictly aims at correcting malfunctioning of markets.

The prohibition of monetary financing underlines precisely the fact that budgetary discipline is of the utmost importance. We have taken note of the precise additional commitments taken by some euro area governments to accelerate fiscal consolidation and to ensure the sustainability of their public finances." I have nothing to withdraw from these remarks of May 2010. They remain fully valid.

We expect from governments strict respect for the principle of budgetary discipline and effective mutual surveillance. It is of utmost importance that these commitments are now implemented strictly and timely. They need to be backed by concrete measures. This applies to both the IMF/EU adjustment programmes and the renewed commitment of all euro area governments to the agreed fiscal targets. The full and timely implementation of the 21 July agreement between Heads of State or Government is of essence in this respect.

While a special arrangement for Greece has been launched, the inflexible determination of all other euro area governments to fully honour their own individual sovereign signature is key in returning to sustainable and healthy public finances and contribute to stable market conditions.

Thank you for your attention.

[1] Speech on "The ECB's response to the recent tensions in financial markets", Economic Conference of the Oesterreichische Nationalbank, Vienna, 31 May 2010.