Christine Lagarde: Hearing of the Committee on Economic and Monetary Affairs of the European Parliament

Introductory statement by Ms Christine Lagarde, President of the European Central Bank, at the ECON committee of the European Parliament, Brussels, 2 December 2019.

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Madam Chair,

Honourable members of the Economic and Monetary Affairs Committee,

Ladies and gentlemen,

I am very happy to be back before this Committee for my first regular hearing as ECB President. I want to express my personal and sincere gratitude to this house for the support I received during the appointment process. And I look forward to a constructive and positive relationship between our two institutions going forward.

The connection between the ECB and the European Parliament is especially valuable today as a means to reinforce trust in European institutions.

In the euro area, support for the single currency has grown steadily in recent years, rising from a low of 62% in 2013 during the crisis to an all-time high of 76% today. Trust in the ECB has grown in that time as well – but its recovery after the crisis has been less dynamic.[1]

My predecessors at the ECB were alert to this and already acted to address the challenge. The ECB's accountability practices have evolved[2], as has its communication strategy. And the ECB's transparency, ethics and good governance frameworks have been harmonised, strengthened and extended to all members of the Governing Council and Supervisory Board.[3]

But it is important to me that our focus on connecting with the people we serve continues and grows stronger – in particular by improving the ways in which we communicate with the general public.

And this is why your role in the Parliament is so important: you make sure that the people's voice is heard by the ECB and the ECB's voice is heard by the people.

Communication is a two way street and it is vitally important for democracy, a founding principle of Europe. It is in this spirit that I will approach this hearing – and those we will have together in the future.

The current economic situation and monetary policy

Let me start by looking at the current economic situation in the euro area, before moving on to the longer-term questions for monetary policy about which you have enquired.

Euro area growth remains weak, with gross domestic product growing by only 0.2%, quarter on quarter, in the third quarter of 2019. This weakness has been mainly due to global factors.

The world economy outlook remains sluggish and uncertain. This lowers demand for euro area goods and services and also affects business sentiment and investment.

As the sector most directly exposed to these global developments, the manufacturing industry has been suffering the most. We are also seeing signs of spillovers to other parts of the economy, with recent survey data pointing to some moderation in the services sector.

Yet, consumption has held up fairly well: labour market conditions have continued to improve, encouraging consumers to remain confident and to continue to spend.

The prolonged slowdown in economic activity has nevertheless been affecting price developments, which remain subdued. According to Eurostat's flash estimate, inflation stood at 1.0% in November. Whether we look at surveys or market-based measures, inflation expectations are at or close to historical lows.

What can the ECB do in a weaker economic environment to fulfil its price stability mandate?

First of all, monetary policy can respond effectively even when growth is being dampened by external factors. And it can do so by ensuring favourable financing conditions for all sectors of the economy and providing visibility on those conditions into the future.

Backed by a steady flow of credit on affordable terms, households and firms can consume and invest more. Such support for internal demand reinforces the services sector in particular, which is the most labour-intensive part of the economy. That helps to protect jobs and incomes and thereby sustains consumption – partly offsetting the external shock.

We are seeing this mechanism in action today: the relative resilience of services so far is the key reason why employment has not been affected by the global manufacturing slowdown.

In response to the weaker outlook, the Governing Council took a series of decisions in September this year to ensure that financing conditions remain favourable.

It decided to lower the interest rate on the deposit facility to -0.5%, to restart net asset purchases, to strengthen forward guidance on both these tools, to make the conditions on the targeted longer-term refinancing operations (TLTROs) more attractive, and to introduce a new regime of remuneration for excess reserves held by banks with the Eurosystem.

These measures work together to keep interest rates at all maturities around levels consistent with very accommodative financing conditions.

The ECB's negative policy rates and forward guidance on their likely future path influence short to medium-term interest rates, which are used by banks to price loans to firms. In parallel, the net purchase of bonds eases medium- to long-term yields, which provide the benchmark for long-term loans to households. The more attractive conditions on the TLTROs help keep bank credit flowing to customers on affordable terms.

At the same time, the Governing Council's decisions in September showed that it was alert to the potential side effects of monetary policy.

The new two-tier regime of excess reserve remuneration exempts a share of banks' liquidity deposited with the Eurosystem from the negative interest rate applied on the deposit facility. This will also ensure that banks remain willing and able to pass on very accommodative financing conditions to the economy.

The ECB's accommodative policy stance has been a key driver of domestic demand during the recovery, and that stance remains in place. As laid out in the ECB's forward guidance, monetary policy will continue to support the economy and respond to future risks in line with our price stability mandate. And we will continuously monitor the side effects of our policies.

As I confirmed to you last time when I was here, the ECB remains resolute in its commitment to deliver on its mandate. This commitment is vital for the stability of the euro area economy and for the welfare of euro area citizens.

But you have also asked me to discuss more structural issues facing monetary policy, in particular the review of the ECB's monetary policy strategy, which will start in the near future.

Such strategic reviews are relatively common for central banks, although their scope and aims often vary. The US Federal Reserve is currently undertaking such a review; the Bank of Canada has one every five years. In the ECB's case, the last strategy review was completed in 2003. A lot has changed in the last 16 years.

The macroeconomic landscape has been marked by the Great Financial Crisis and the sovereign debt crisis, and more recently by a low inflation environment. At the same time, new challenges have emerged such as demographics, disruptive technology and climate change. Conventional wisdom has been challenged and monetary policy globally has explored unchartered territories.

This calls for us to review our strategy and to consider how our monetary policy can best deliver on our mandate.

Indeed, a question that is common to the entire community of central banks today is how to best define the medium-term objective of monetary policy, so as to ensure that expectations are firmly anchored. This could be particularly beneficial in conditions – like today's – in which the policy space to buffer the economy from adverse developments is more limited than it was prior to the crisis.

And, we are all trying to gain a better understanding of how the longer-term trends I mentioned might affect variables we monitor regularly and seek, to some extent, to control.

This being said, it is premature to venture here into debates about the precise scope, direction and timeline of our review, as the matter has not yet been discussed thoroughly by the Governing Council.

What I can confirm, however, is that the strategy review will be guided by two principles: thorough analysis and an open mind. This will require time for reflection and for wide consultation.

The Parliament, and this Committee in particular, have traditionally offered a unique forum for dialogue, which has been enriched by the expert reports prepared ahead of the hearings.[4] The ECB greatly benefitted from these debates 16 years ago when it undertook its last strategy review.

This time around, we will be seeking a dialogue which is even more intense and productive than in the past. And I see it as my responsibility, as the ECB President, to report back to you, and engage in further discussion, once the Governing Council moved forward on the content and timeline of our exercise. The two way street communication principle will apply.

Shaping the future of money

The other topic you have asked me to discuss today is the future of money. Indeed, as central banks navigate a complex and changing landscape, we should not only aim to anticipate future trends, but also seek to shape them. In doing so, we should be particularly attentive to risks and perform a thorough analysis of their costs and benefits.

The financial services environment is evolving as new entrants shake up the market. So are the public's needs and demands. The ongoing discussion around so-called stablecoins offers a glimpse of the changes that might come.

This phenomenon could disrupt the current payments landscape, with spillover effects for monetary policy transmission, financial stability and the international monetary system more broadly. But the ECB is not standing still in the face of these challenges.

Last year, the ECB launched TARGET Instant Payment Settlement (TIPS), an instant payment service that allows money to reach the recipient within seconds, 24 hours a day, 365 days a year. TIPS responds to the growing user demand for instant payments and helps ensure that any bank account holder in Europe can be reached. By offering settlement in central bank money, TIPS increases the speed and safety of customers' daily transactions.[5]

Since 2016, the ECB has also been exploring the application of new technologies, particularly distributed ledger technologies, to market infrastructures. Together with the Bank of Japan, the ECB is conducting a research project called "Stella" which is investigating innovations that can facilitate safer, faster and cheaper financial transactions.[6]

But driving change also means identifying and managing the risks that come with breaking new ground. Innovations – including stablecoins – will only be beneficial if the associated risks are mitigated through effective regulation and oversight. So I believe we should follow the golden rule of supervision: "same business, same risk, same rules".

We must ensure that stablecoins do not compromise the safety and efficiency of the payment system or the soundness and stability of the financial and monetary system. And this is all the more important for stablecoins with a global reach. The G7 Working Group chaired by my fellow Executive Board member Benoît Cœuré has made clear recommendations with a view to developing a globally consistent approach to their regulation and oversight.[7]

As it did for the General Data Protection Regulation, the European Union can show the way here. In line with international standards and recommendations, we – and here I count on you as co-legislator – should develop and enforce regulation that strikes the right balance between supporting innovation and addressing risks.

The ECB is ready to play its part and is already collaborating with other central banks and international authorities to that end. We are also reviewing our oversight framework to capture innovative payment solutions, including stablecoin arrangements. In doing so, we are following a risk-based and proportionate approach.

Looking ahead, the ECB will continue to act as a catalyst for change. We will go on engaging with European stakeholders to actively contribute to a pan-European payment solution.

We also play our part, in full independence, in assessing the value of central bank digital currencies for European citizens and the broader economy.

A central bank digital currency would allow citizens to use central bank money directly in their daily transactions. However, depending on its design, a central bank digital currency could pose risks. For instance, they could alter the way in which monetary policy is conducted and transmitted to the real economy. They could also carry implications for the functioning of the global financial system and its stability. The question of central bank digital currencies and their optimal design therefore warrants further analysis.

Our ultimate goal is to foster safer, innovative and integrated payments in euro. This will in turn benefit everyone in the euro area and strengthen the euro internationally.

Conclusion

Madam Chair, honourable members,

The last European Parliament elections highlighted that people expect ambitious responses from Europe. Matching these expectations by working together is the best way to strengthen people's confidence in the European project, the euro and the ECB.

Jean Monnet once said that “everyone is ambitious, the question is if one is ambitious to be or ambitious to do”. I can assure you that the ECB is ambitious to do, and to play its part in accordance with its mandate.

Thank you for your attention. I am now available for your questions.

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1 See Spring 2013 Standard Eurobarometer survey (EB 79) and Spring 2019 Standard Eurobarometer survey (EB 91).

2 See “The evolution of the ECB’s accountability practices during the crisis”, Economic Bulletin, Issue 5, ECB, 2018.

3 See, for example, the Single Code of Conduct for high-level officials adopted by the ECB in 2019, which includes the obligation to publish monthly appointment calendars.

4 All the reports are published on the European Parliament’s website.

5 See the ECB’s website.

6 See the ECB’s website.

7 See G7 Working Group on Stablecoins, Investigating the impact of global stablecoins.