SPEECH

The monetary agenda at the ECB

Remarks by Philip R. Lane, Member of the Executive Board of the ECB, at the House of the Euro

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My goal today in these remarks is to outline the current monetary agenda at the ECB.[1] I will start with the monetary policy stance before turning to our updated monetary policy strategy. I will then briefly discuss the euro area bond market before concluding with a monetary perspective on the digital euro project.

The monetary policy stance

In a recent speech, I assessed that the challenge of returning inflation to the target after the 2021-2022 inflation surges can be considered to be largely complete.[2] The orientation now for the monetary policy stance is to make sure that the current shocks and prospective new shocks hitting the economy do not lead to medium-term deviations of inflation from our two per cent target.

In terms of significant data developments in recent months, there has been a marked drop in energy prices and a substantial appreciation of the euro. These forces played an important role in the June 2025 Eurosystem staff macroeconomic projections. In addition, the fiscal outlook has materially changed for the coming years, with the overall fiscal deficit looking set to remain above three per cent over the projection horizon.

Guarding against the risk of temporary deviations from target turning into longer-term deviations was an important factor in our June decision to cut rates by 25 basis points. By supporting the pricing pressure needed to generate target-consistent inflation in the medium term, this cut helps ensure that the projected negative inflation deviation over the next eighteen months remains temporary and does not convert into a longer-term deviation of inflation from the target.

Currently, there is high uncertainty about the future of the international trade system. This uncertainty extends beyond the calibration of new tariff regimes and includes the possibility of a broader set of non-tariff barriers, a deeper intertwining of economic policies and security policies and possible revisions to the treatment of foreign portfolio investors and foreign direct investors.

Especially under current conditions of high uncertainty, it is essential to remain data dependent and take a meeting-by-meeting approach in making monetary policy decisions, with no pre-commitment to any particular future rate path. In addition to observing how activity and inflation are actually behaving, data dependence also extends to the incoming data on policy settings outside the monetary domain, since shifts in international and domestic policy regimes are highly relevant for future inflation dynamics.

Our updated monetary policy strategy

The emphasis on two-sided uncertainty about inflation dynamics very much reflects the analysis that underpins the recently announced update to our monetary policy strategy.[3] In addition to the geopolitical tensions outlined above, our updated monetary policy strategy statement also identified ongoing structural shifts related to digitalisation, artificial intelligence, demography, the threat to environmental sustainability and changes in the international financial system as suggesting that the inflation environment will remain uncertain and potentially more volatile, with larger target deviations in both directions, posing challenges for the conduct of monetary policy.

In terms of the implications for monetary policy, our assessment is that the symmetric two per cent medium-term inflation target – which has served us well and remains unchanged - is best protected by appropriately forceful or persistent monetary policy action in response to large, sustained deviations of inflation from the target in either direction, to avoid deviations becoming entrenched through de-anchored inflation expectations. In the event of significant disinflationary shocks, the effective lower bound on nominal interest rates needs to be taken into account. In the event of significant inflationary shocks, possible non-linearities in price and wage-setting need to be taken into account.

The flexibility of the medium-term orientation recognises that the appropriate monetary policy response to a deviation of inflation from the target is context-specific and depends on the origin, magnitude and persistence of the deviation. Subject to maintaining anchored inflation expectations, it also allows the Governing Council in its monetary policy decisions to cater for other considerations relevant to the pursuit of price stability.

The Governing Council bases its monetary policy decisions, including the evaluation of the proportionality of its decisions and potential side effects, on an integrated assessment of all relevant factors. Our updated strategy makes explicit that our monetary policy decisions incorporate not only the most likely path for inflation and the economy but also surrounding risks and uncertainty, including through the appropriate use of scenario and sensitivity analyses.

A systematic but context-specific approach to incorporating the surrounding risks and uncertainty can include, in addition to conducting a regular risk assessment, analysing the sensitivity of projections and policy choices to changes in the underlying technical assumptions and model parameters as well as exploring a range of alternative scenarios, especially in relation to specific risk events.

In the internal preparation of monetary policy decisions, ECB staff have conducted sensitivity and scenario analyses for many years.[4] In recent years, some of this analysis has been published: this includes scenarios related to the pandemic, the unjustified Russian invasion of Ukraine, the conflicts in the Middle East and trade policy uncertainty. As we implement the updated monetary policy strategy, the incorporation of risks and uncertainty will be enhanced both in the internal preparation of monetary policy decisions and, where appropriate, in the communication of our decisions.

While our primary instrument is the setting of our policy rates, the Governing Council may also employ other instruments, as appropriate, to steer the monetary policy stance when the policy rates are close to the lower bound or to preserve the smooth functioning of monetary policy transmission. The list of "unconventional" instruments includes longer-term refinancing operations, asset purchases, negative interest rates and forward guidance. The incorporation of risks and uncertainty into monetary policy decisions also has implications for the use of such instruments. In particular, the choice, design and implementation of instruments will enable an agile response to new shocks and will appropriately reflect the intended aims, whether the calibration of the monetary policy stance or the protection of monetary policy transmission, subject to a comprehensive proportionality assessment.[5]

A more resilient euro area financial architecture

Our updated monetary policy strategy statement also assesses that: "A more resilient financial architecture – supported by progress on the savings and investments union, the completion of banking union and the introduction of a digital euro – would also support the effectiveness of monetary policy in this evolving environment".

It is beyond the scope of these remarks to review the full policy agenda in relation to the savings and investments union and the completion of banking union. Of course, the net gains from improving financial intermediation and financial integration depend on the scale of progress in implementing the pro-growth economic reform agenda, as laid out in the Draghi and Letta report. The European Commission's Competitiveness Compass provides a concrete roadmap for action, and its proposals, including on simplification, should be swiftly adopted.

Let me pick up on an important dimension of improving the euro area financial architecture by briefly discussing the potential value of an expanded pool of euro-denominated safe assets in making the euro area capital market more attractive for both European and global investors.[6]

The bund is the highest-rated large-country national bond in the euro area. However, the stock of bunds is too small relative to the size of the euro area or the global financial system. Especially in the context of much smaller and less volatile spreads, other national bonds also directionally contribute to the stock of safe assets. While the residual potential volatility in spreads and the lower liquidity of these bonds ultimately put a ceiling on their contribution to the supply of safe asset supply, the overall attractiveness of the euro area bond market ultimately depends on each member state ensuring fiscal sustainability, including through the shared commitment to implement the European fiscal framework in a rigorous manner.

In principle, common bonds backed by the combined fiscal capacity of the EU member states should constitute a high-grade category of safe assets. However, the current stock of such bonds is simply too small to foster the necessary liquidity and risk management services (e.g. derivative markets and repo markets) that are part and parcel of serving as a safe asset. Moreover, as it stands, the stock of supranational euro bonds is currently projected to shrink over time, in view of the scheduled repayment of the NGEU bonds and, over time, the retirement of ESM bonds as the ESM loans get repaid.

There are several ways to expand the stock of common bonds. For instance, the member countries could decide to finance investment in European public goods through more common debt. From a public finance perspective, it is natural to match European public goods with common debt in order to align the financing with the area-wide benefits of such public goods. In addition to EU-wide initiatives, there could also be scope for common issuance by sub-groups of member countries in the context of possible "coalition of the willing" shared investment projects.

Furthermore, in order to meet the rising global demand for euro-denominated safe assets more quickly, there are a number of ways to generate a larger stock of safe assets from the current stock of national bonds.[7] For instance, Olivier Blanchard and Ángel Ubide have proposed that the "blue bond/red bond" scheme (which was originally floated in 2010) be re-examined.[8]

Under the Blanchard-Ubide proposal, each member country would ringfence a dedicated revenue stream (for example, a certain amount of indirect tax revenues) that could be used to service commonly issued bonds. In turn, the proceeds of issuing common bonds (blue bonds) would be deployed to purchase a given amount of the national bonds (red bonds) of each participating Member State. This mechanism would result in a larger stock of blue bonds and a lower stock of red bonds. While this type of financial reform was originally proposed during the euro area sovereign debt crisis, the conditions today are far more favourable, especially if the scale of blue bond issuance were to be calibrated in a prudent manner in order to mitigate some of the identified concerns.

In particular, the Blanchard-Ubide proposal gives the example of a stock of blue bonds corresponding to 25 per cent of GDP. Just to illustrate the scale of the required fiscal resources to back this level of issuance: if bond yields were in the range of 2 to 4 per cent on average, the servicing of blue bond debt would require ringfenced tax revenues in the range of 0.5 to 1 per cent of GDP. While this would constitute a significant shift in the current allocation of tax revenues between national and EU levels, it would still leave tax revenues predominantly at the national level (the ratio of tax revenues to GDP in the euro area ranges from around 20 to 40 per cent). The shared payoff would be the reduction in debt servicing costs generated by the safe asset services provided by an expanded stock of common debt.

An alternative and possibly complementary approach that could also deliver a larger stock of safe assets from the pool of national bonds is provided by the sovereign bond-backed securities (SBBS) proposal. This proposal envisages that financial intermediaries (whether public or private) could bundle a portfolio of national bonds and issue tranched securities, with the senior slice constituting a highly safe asset. The SBBS proposal has been studied extensively (I chaired an ESRB report on it) and draft enabling legislation has been prepared by the European Commission.[9]Just as with the blue bond/red bond proposal, sufficient issuance scale would be required in order to foster the market liquidity needed for the senior bonds to act as highly liquid safe assets.

Finally, in relation to the digital euro, our updated monetary policy strategy statement also states that introducing a digital euro would support the effectiveness of monetary policy. In particular, as I outlined in a recent speech, a digital euro could help maintain the monetary autonomy of the euro area by ensuring a direct retail role for central bank digital currency can help maintain the monetary autonomy of the euro area.[10] By supplementing physical cash with digital cash, this would improve resilience by modernising the traditional two-tier monetary system whereby both cash and bank deposits can be used as a medium of exchange. This modernised system would best protect the euro's capacity to serve as the medium of exchange and unit of account.[11]

According to some advocates, an alternative approach to adapting the monetary system to a digital age would be to promote stablecoins, issued and operated by private sector intermediaries. There may be some potentially valid use cases for stablecoins, especially in relation to improving the efficiency of cross-border payments, at least compared to the incumbent global payments infrastructure. However, stablecoins lack key attributes of central bank money. Among other limitations, as highlighted in the recent Annual Economic Report, by the Bank for International Settlements, the supply of stablecoins is not elastic (unlike central bank money) since their issuance is driven by upfront purchases by customers. In contrast, central bank money can be issued elastically (especially during a crisis) by lending to counterparties or through open market operations. Additionally, one-to-one parity between the value of a stablecoin and the value of a currency cannot be guaranteed under all circumstances, such that stablecoins do not protect the singleness of money.

An effective medium of exchange requires that the monetary system and the payments system form a symbiotic ecosystem. Currently, the euro area payments system is highly fragmented along national lines and many customers are dependent on non-European card or e-wallet providers to make payments across the euro area. By mandating acceptance of the digital euro, instant network effects would help to unify the currently-fragmented market, reducing costs for merchants and indirectly also for households. Such an area-wide fast payment system is unlikely to develop in the absence of the area-wide payment rails provided by the digital euro infrastructure.

For these reasons, the digital euro is a high priority project for the Eurosystem, subject to the enabling legislation being adopted by the European Parliament and the Council of the European Union.

1.

The views expressed in these remarks are personal and should not be interpreted as representing the collective view of the ECB Governing Council.

2.

See Lane, P.R. (2025), "Monetary policy: new challenges", speech at the Barclays-CEPR Monetary Policy Forum 2025, London, 24 June.

3.

The monetary policy strategy statement, the accompanying overview note and the two occasional papers containing the Eurosystem staff analysis that supported the assessment exercise are available on the ECB's website.

4.

See also Lagarde, C. (2025), “Strategy assessment: lessons learned”, introductory speech at the opening reception of the ECB Forum on Central Banking 2025 on “Adapting to change: macroeconomic shifts and policy responses”, Sintra, 30 June; Lane, P.R. (2024), “Monetary policy under uncertainty”, keynote speech at the Bank of England Watchers’ Conference 2024, London, 25 November; and Lane, P.R. (2025), “The communication of monetary policy decisions: incorporating risks and uncertainty”, remarks at the Second Thomas Laubach Research Conference, Washington, D.C., 16 May.

5.

See also paragraph 8 of the monetary policy strategy statement and section 3.3 of the overview note.

6.

This section draws on a recent speech. See Lane, P.R. (2025), “The euro area bond market”, keynote speech at the Government Borrowers Forum 2025, Dublin, 11 June.

7.

For a discussion of alternative models for a European Debt Agency that would issue common bonds, see L.Bottazzi, C. Favero, R. Fernandez Fuertes, F. Giavazzi, V. Guerrieri, G. Lorenzoni and T. Monacelli (2025), “The conduct of ECB monetary policy under uncertainty,” Monetary Dialogue Papers June 2025, ECON committee of the European Parliament.

8.

Blanchard, O. and Ubide, Á. (2025), “Now is the time for Eurobonds: A specific proposal”, *Realtime Economics*, Peterson Institute for International Economics, 30 May; Leandro, Á. and Zettelmeyer, J. (2019), “Creating a euro area safe asset without mutualizing risk (much)”, *Capital Markets Law Journal*, Vol. 14, No 4, pp. 488-517.

9.

The SBBS proposal originated in the European Safe Bonds (ESBies) proposal. See Brunnermeier, M.K. et al. (2011), “European Safe Bonds (ESBies)”, *Euro-nomics*, 30 September; Brunnermeier, M.K. et al. (2016), “The Sovereign-Bank Diabolic Loop and ESBies”, *American Economic Review*, Vol. 106, No 5, pp. 508-512; and Brunnermeier, M.K. et al. (2017), “ESBies: safety in the tranches”, *Economic Policy*, Vol. 32, No 90, pp. 175-219. See also Volumes I and II of the Report of the ESRB High-Level Task Force on Safe Assets and European Commission (2018), “Proposal for a regulation on sovereign bond-backed securities”, 24 May.

10.

Lane, P.R. (2025), "The digital euro: maintaining the autonomy of the monetary system," speech at the University College Cork Economics Society Conference 2025, Cork, 20 March. For a complete guide to the digital euro project (including its crucial role in delivering a euro area-wide point-of-interaction fast payments system), see the ECB's dedicated web page.

11.

While it can be theorised that the euro area monetary system could probably remain functional even without a retail digital euro, the ECB is tasked with safeguarding monetary stability in all circumstances. Prudence calls for a monetary architecture that is resilient.