Joachim Nagel: European monetary policy challenges in the new geopolitical environment

Dinner speech by Dr Joachim Nagel, President of the Deutsche Bundesbank, at the Euro50 Group meeting, London, 12 February 2026.

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1 Introduction

Ladies and gentlemen,

Some years ago, Dario Caldara and Matteo Iacoviello, economists at the Federal Reserve, proposed a news-based measure of adverse geopolitical events and risks –a metric that they dubbed the geopolitical risk index.[1] Technically, the index is based on the share of articles mentioning adverse geopolitical events in leading newspapers in the United States, the United Kingdom and Canada. According to this index –and unsurprisingly –we are currently living in a period of high geopolitical risk. For example, last year, the index recorded an average level of 145, which is only slightly lower than the reading of 158 we saw in 2022 –the year when Russia launched its full-scale invasion of Ukraine. For comparison, back in the pandemic year 2020, the average level was 78. And in the first month of this year, the index hit 164 already. This is almost as high as the average for 2001.[2] In recent decades, the index reached its peak in 2001, driven by the 9/11 terrorist attacks.

We all know that geopolitical events and risks affect the economic activities of households and enterprises, particularly investment.[3] However, in my speech, I would like to touch on the potential challenges that the new geopolitical reality poses for European monetary policy. In doing so, I will discuss three points: inflation volatility, central bank independence and the rise of stablecoins.

2 Inflation volatility

Let me begin with the first one –inflation volatility. Adverse geopolitical shocks can elevate inflation volatility. We observed this soon after Russia invaded Ukraine. At that time, energy prices saw a remarkable spike. We observed disruptions in some supply chains, especially for food products. This came on top of economic disruptions caused by the pandemic and led to the largest inflation wave since the 1970s. Fortunately, despite significant trade conflicts last year, we have successfully brought inflation under control. However, there is no guarantee that similar shocks won't occur again in the future.

In light of developments since the pandemic, the Eurosystem updated it monetary policy strategy last year. It acknowledges that geopolitical and economic fragmentation can lead to more volatile inflation dynamics. Being able to respond to new shocks in an agile way is important. The revised strategy takes this need into account.

In particular, it proposes forceful or persistent measures in response to strong or sustained deviations from our inflation target in both positive and negative directions. This point emphasises the symmetry of our inflation target and addresses the criticism that our monetary policy strategy placed more emphasis on target undershooting in the past. Last but not least, I believe it is crucial that we continue to reduce our balance sheet size since that increases leeway to take monetary policy action in unexpected scenarios.

Moreover, the Eurosystem's newly revised strategy states that we will make more use of scenario analysis in our forecasting exercises instead of focusing on a single, most probable baseline scenario. This approach will allow us to account for risks and uncertainty in a more comprehensive and systematic way.

3 Central bank independence

Let me move to the next item on my agenda: central bank independence. As we all know, central bank independence is crucial for price stability. The theoretical basis for this claim can be traced back to the seminal work of Kydland and Prescott, published almost fifty years ago.[4] Empirical studies reveal a negative relationship between the degree of central bank independence and inflation levels as well: the more independent a central bank is, the lower inflation will be –all other things being equal.[5]

However, increasing geopolitical competition between countries may increase the pressure on independent central banks to prioritise fiscal objectives over containing inflation. Currently, we are observing considerable political pressure being exerted on the Federal Reserve. If this political pressure succeeds, it could be taken as a blueprint for politicians in other countries to pursue similar policies. If that were to happen, inflation levels could increase all over the world.

Since the world economy is interconnected, political pressure in one country could make pursuing price stability more difficult for the Eurosystem as well. That is one of the reasons why, for me, it is so important to clearly commit to the independence of central banks. Well, in the Eurosystem's case, independence is enshrined in the primary law of the European Union. However, we must not become overly self-confident. We will always remain vigilant with regard to our own independence.

4 The rise of stablecoins

The last issue I would like to touch on concerns the rise of stablecoins. You have surely heard that the US administration is officially promoting the market for crypto-assets, specifically the market for stablecoins, denominated in US dollars. Stablecoins are crypto-assets designed to maintain a stable value relative to a specified asset, which is typically a national currency, a commodity or a financial asset. While stablecoins make up only a small share of the market compared with other "money-like" assets such as deposits, they have seen strong growth recently. Currently, depending on the definition, their market volume amounts to just over 300 billion US dollars.[6]

To be clear, stablecoins have benefits. For example, they open the door for programmable transactions, which, by the way, are not an option in central bank money just yet. Furthermore, stablecoins could facilitate cross-border payments by reducing transaction costs and payment duration. However, the rise of stablecoins could entail risks for the euro area if stablecoins, particularly those denominated in a foreign currency, were widely used as means of payment and store of value in the euro area.

Currently, the share of stablecoins denominated in euros does not even amount to 1 percent. In contrast, the vast majority of stablecoins are denominated in US dollars. Thus, if this market composition persists, a hypothetical replacement of a domestic currency with stablecoins would be equivalent to a dollarisation of the corresponding economy. In this scenario, the effectiveness of domestic monetary policy could be severely impaired, not to mention that European sovereignty could be weakened.

To be fair, the euro is a stable currency supported by a secure financial system and an attractive payment infrastructure. As a result, the risk of this scenario materialising is small. However, to further reduce the likelihood of this scenario, we are considering how to leverage new technological opportunities to best effect.

First, in my view, this involves introducing a wholesale central bank digital currency –CBDC. This would allow institutional actors on financial markets to execute programmable transactions in central bank money. Moreover, the introduction of a European wholesale CBDC would make our financial system more efficient and resilient. The Eurosystem has already done the necessary exploratory work in this field and is pushing ahead with two projects. The aim of one of these projects is to introduce a wholesale CBDC interoperability solution in the current year. Second, the Eurosystem could support DLT-based payment instruments not directly related to central bank money, in particular, tokenised deposits and euro-denominated stablecoins.

These measures will allow us to utilise cutting-edge digital technologies to maintain our monetary policy effectiveness in an uncertain geopolitical future. Additionally, they will increase our sovereignty.

5 Concluding remarks

Ladies and gentlemen,

Let me conclude. What will the average be for Caldara and Iacoviello's geopolitical risk index this year? Will it exceed its 2001 level? Only time will tell. Should we take comfort in the fact that we are well below the levels recorded during the world wars? I very much hope that we do not reach those levels again.

What can central banks do? In my view, we should be strictly fulfilling our mandate even in times of fundamental change. To do so, we need to focus on price stability, preserve our independence and counteract any risks that may arise in the context of new digital technologies.

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[1] Caldara, D. and M. Iacoviello (2022), Measuring Geopolitical Risk, American Economic Review, Vol. 112 No 4, pp. 1194-1225.

[2] https://www.matteoiacoviello.com/gpr.htm

[3] See Caldara and Iacoviello (2022); Bondarenko et al. (2025), Geopolitical Risk in the Euro Area: Measurement and Transmission, mimeo.

[4] Kydland, F. E. und E. C. Prescott (1977), Rules Rather than Discretion: The Inconsistency of Optimal Plans, Journal of Political Economy, Vol. 85, pp. 473-492.

[5] Cukierman, A., Webb, S. B. and B. Neyapti, (1992), Measuring the Independence of Central Banks and Its Effect on Policy Outcomes, World Bank Economic Review, Vol. 6 No 3, pp. 353-398.

[6] Stablecoin Market Opens 2026 at a New $310B Record –Crypto News Bitcoin News