Monetary policy in the euro area and the path towards a “new normal”

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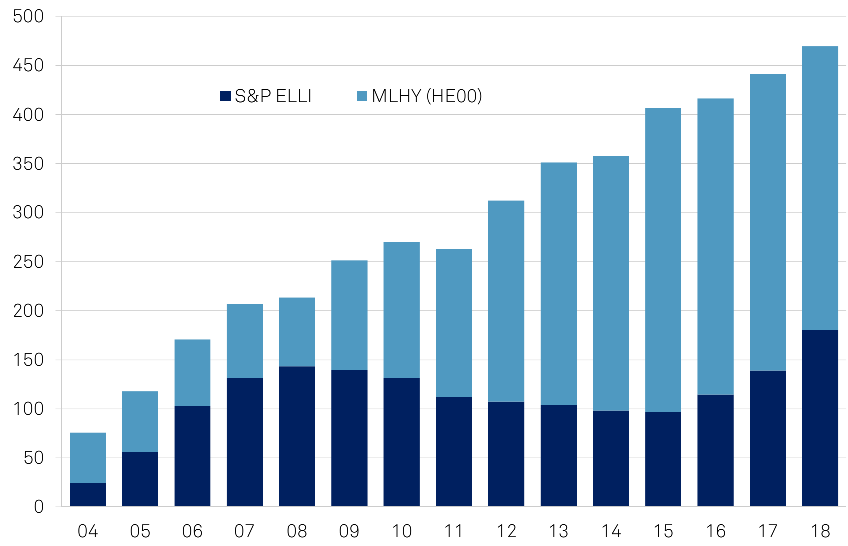
The return to one-dimensional monetary policy has become impossible

- **Deal with the Zero Lower Bound**
  - ➢ Transmission of monetary policy instruments
  - ➢ Downward bias in interest rates policy (preemptive easing in MPR is easier than leaning against the wind)
- **Global debt is higher and in many cases riskier than a decade ago**
  - ➢ „Benign Neglect“ approach by large asset prices movements is no more an option
  - ➢ Fiscal dominance is more than ever a risk to CB's independence
- **Externalities are on the rise**
  - ➢ Macro-prudential measures cannot tackle financial stability issues on their own
  - ➢ Cross-border dependencies (FX, capital flows, …)
  - ➢ Climate risk, …

European Leverage Finance and High Yield market outstanding in EUR bn



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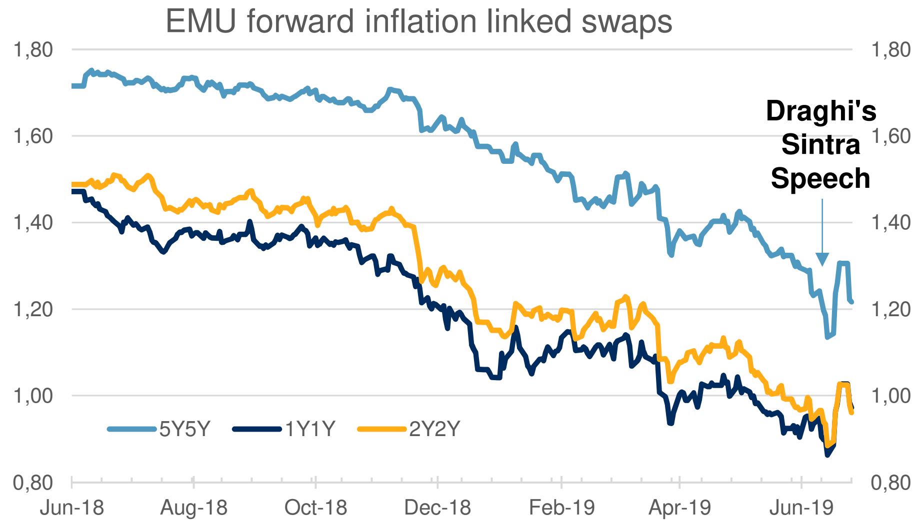
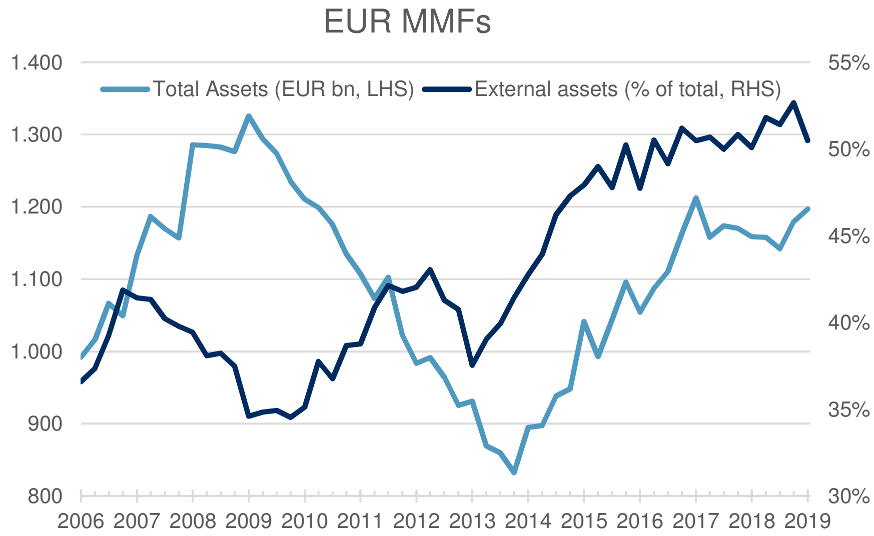
Redefining a framework for ECB policy

- **It is not much about price stability**
  - ECB's strategy of price stability with 2-legs forward guidance offers a lot of flexibility
  - Alternatives to flexible inflation targeting are no cure
- **It is about the consistency of the "order of rules" and the "order of actions"**
  - Protect Monetary policy from overburdening and fiscal dominance in a context where the euro area framework will never be complete
  - Enshrine the role of LoLR in the statutes of the Eurosystem
  - System analysis of the new monetary policy practices
- **It is about strengthening the international role of the euro**
  - Not only to serve the purpose of the EC addressing the extraterritorial effects of US laws
  - But also to ensure the good transmission of monetary policy while private digital stable coins are challenging public fiat currencies
- **It is about no longer thinking of the NIRP as an "eccentricity"**
  - cash vs. digital; existence of a corporate finance channel
  - Critical assessment of the allocative effects of the APP and the disincentive effects of the PSPP on fiscal discipline

What does all this mean in terms of policy instruments ?

- **Primarily use of NIRP to steer inflation expectations** in a context of undershooting the price stability target
- **Permanent but restricted use of QE** to address the risk of debt unsustainability (r-g as trigger?)
- **Provision of short term safe assets** (RRP, debt certificates) to a large set of financial counterparties (banks, MMFs)
- **Standing LoLR facility** to prevent liquidity crisis
- **Standing swap lines or list of collateral extended to FX assets**
- **Definitively: larger balance sheets**





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