mni

All Signal, No Noise

MARKET ANALYSIS

ECB Preview: December 2021

Contents

Details:

Monetary policy decision: 12:45BST/13:45CET, Thursday 16 December 2021

Press conference: 13:30BST/14:30CET, Thursday 16 December 2021

Expected links:

Monetary Policy Decisions:
https://www.ecb.europa.eu/press/govcdec/mopo/2020/html/index.en.html

Interest Rate Announcements:
https://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html

ECB Press Conference Video:
https://www.ecb.europa.eu/press/tvservices/webcast/html/webcast_pc_youtube.en.html

Bloomberg: MEDI <Go>

MNI Point of View (POV):

A Recalibration Potentially Short on Details

- PEPP is likely to end in March, with a beefed-up APP smoothing the transition from the emergency phase to the recovery phase.
- How much of this will get announced in December is unclear given heightened uncertainty over growth and inflation, in both directions.
- It is a close call, but we err on the side of the ECB seeking to retain some optionality by pre-committing to ending PEPP and using the APP flexibly (perhaps by pursuing quarter-by-quarter decisions on purchase volumes), without specifying at this stage exact target volumes or potential envelope size.
- Whether or not the mechanics of the 'transition purchases' are unveiled in December or February, a monthly APP purchase rate of EUR30-40bn/month for six months, or a ~EUR60-120bn purchase envelope on top of the existing EUR20bn/month purchases would be in the right ball park.

As policymakers readily admit (see *"Reflation, Not Stagflation"*, Isabel Schnabel, 17 November) the ECB has had a particularly tough time forecasting inflation and meeting the price stability objective in the decade before the pandemic. The ECB now finds itself in a new predicament as the sudden burst of inflation coupled with the emergence of the Omicron variant has injected fresh uncertainty to the economic outlook and muddied the waters for monetary policy. Having conditioned the market since October to expect a recalibration of policy instruments at the December

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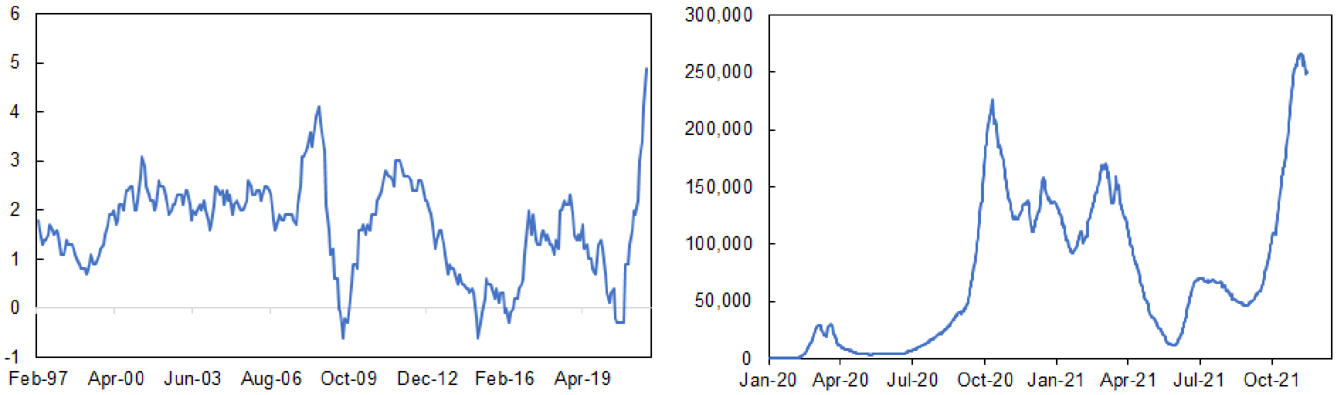
meeting, and clearly signalling that net purchases under PEPP are expected to end in March 2022, the ECB's efforts to guide the market have now potentially complicated the communication strategy in the coming months.

The uncertainty around inflation (transitory or persistent), and the sustainability of the recovery in the face of the Omicron variant and fresh mobility restrictions, make it more difficult to gauge where the consensus lies within the GC. Having poured over the communication since the last meeting, we would summarise sentiment in the following way:

- The surge in inflation has been driven by temporary factors which will subside, with inflation still projected to be below target over the medium term.
- For the time being, there are limited signs of wage pressure and second-round effects.
- Nonetheless, with inflation running hotter than expected, the risks to inflation are shifting to the upside.
- PEPP is likely to end in March 2022.
- Asset purchases, in some form, will continue after PEPP concludes in order to preserve favourable financing conditions and secure the recovery.
- The conditions will not be met for an interest rate rise in 2022.

Fig 1. Eurozone CPI, % Y/Y (LHS) & New Covid Cases In The EU, 7-Day Smoothed (RHS)



Source: MNI, Bloomberg, Our World In Data

Managing the transition from the emergency phase to the recovery phase of the pandemic will be tricky and made more complicated by the ECB repeatedly signalling that PEPP will be wound up in March. The ECB needs to balance the need to safeguard the recovery while also not jeopardising price stability. As such, a post-PEPP cliff edge for asset purchases would need to be avoided, as would an open-ended commitment to prolonged stimulus. Flexibility will be key. As Isabel Schnabel argued on November 17, in the face of considerable uncertainty a 'risk-management approach" to monetary policy, which considers the distribution of risks around the baseline scenario, and embeds a degree of optionality in monetary policy design to target different inflation outcomes, would be beneficial.

With that in mind, the ECB could opt to confirm at this week's meeting that PEPP will be wound down in March, that the APP would be used more flexibly during a transition period (but with no further specific details at this point), and that PEPP would still be in the toolbox and available for reactivation if the pandemic situation worsens. This would constitute a recalibration (in general terms) and provide some guidance to the market without having to pre-commit at this stage to specific purchase volumes and instead give the ECB time to assess the impact of Omicron and the inflation path.

The alternatives to this policy announcement in December appear less compelling to us. The ECB could extend PEPP beyond March, but would undermine its own communication strategy, especially given that as recently as November 26 President Lagarde strongly indicated in an interview with Frankfurter Allgemeine Sonntagszeitung that the programme will end on time. Moreover, should the Omicron wave subside in the early part of next year with growth and inflation both accelerating, it could become more difficult to justify using pandemic emergency purchases. The principal benefit of the PEPP over APP come down to flexibility and particularly the ability to diverge from the capital key, which can be used to defuse fragmentation risks. As such, unless there is a real risk of core-periphery spread widening, the APP can be deployed to maintain a sufficiently accommodative monetary stance rather than an extended or 'transition' PEPP.

The rationale for pre-committing to specific purchase volumes for the APP at this stage is also unclear. Doing so would require a degree of conviction on the outlook for the pandemic and inflation at a time of heightened uncertainty. The ECB could instead pre-commit at the December meeting to using the APP flexibly after PEPP ends, with specific details perhaps being announced at the February meeting. Flexibility in this case could mean deciding purchase volumes on a quarter-by-quarter basis within the context of a time-limited envelope, with the PEPP only reactivated in the event of fragmentation risks arising.

Regardless of whether or not the ECB goes all in at the December meeting and announces an enhanced APP with specific monthly volumes or a purchase envelope, or holds off until February to announce the specifics, a transition period involving monthly purchases in excess of the current APP run rate is likely in 2022.

It is also likely that the flexibility of the PEPP will be retained in one way or another over the longer term. Initially there was speculation that the APP could inherit some of this flexibility, although there are two reasons to discount this. First, allowing the regular asset purchase programme to deviate from the capital key would run the risk of future interventions from the German constitutional court. Although the ECB deftly dealt with the previous legal objections, the central bank would surely prefer to avoid having to publicly defend the legitimacy of its programmes. Second, various GC members including President Lagarde and Isabel Schnabel have made clear that even if PEPP is wound up in March, it will not disappear completely from the toolbox. The ECB could eventually decide to drop the first 'P' from PEPP and devise a new emergency purchase programme to deal with future crisis involving a severe demand or supply shock that risks triggering fragmentation in bonds markets. The introduction of PEPP in the first place has significantly lowered the hurdle for introducing a similar policy tool in the future – perhaps kept in permanent reserve as part of an extended monetary toolbox.

Baseline Scenario: The ECB announces that PEPP will end in March as initially planned and that the APP will be used to manage the transition from the emergency phase to the recovery phase. Although net purchases under PEPP will end, the policy tool will remain in reserve and can be reactivated if the trajectory of the pandemic worsens. While we believe that the ECB could delay until February announcing further specific details on asset purchases, this is a close call and could ultimately be unveiled at this week's meeting.

Dovish Scenario: The ECB reverses course on PEPP and delays a decision on when to end the current programme, with the possibility of even extending pandemic purchases beyond March. President Lagarde maintains that the current surge in inflation will prove temporary and that the ECB should be both patient and persistent given the new risks to the economic recovery.

Hawkish Scenario: The ECB announces that PEPP will end in March as initially planned, but delays any announcements on the APP. Furthermore, President Lagarde highlights that the risks to the inflation outlook have shifted to the upside and that the Omicron variant has not fundamentally altered the balance of risks around the growth outlook.

mni Central Bank Watch - ECB

09 December 2021

MNI ECB Data Watch List

Inflation		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
HICP	% y/y	4.9	3.0	↑	2.0	↑					2.53
Core Inflation	% y/y	2.6	1.6	↑	1.0	↑					1.67
Oil Prices	$	70.6	73.0	↓	69.3	↑					-0.68
5y/5y Inflation Swap	%	1.91	1.69	↑	1.60	↑					0.96
Economic Activity		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Eurozone PMI (Comp)	Index	55.4	59.0	↓	57.1	↓					0.57
Industrial Production	% y/y	5.2	10.6	↓	12.0	↓					-0.56
Business Climate Indicator	Index	1.80	1.72	↑	1.45	↑					0.68
Consumer Confidence	Index	-6.8	-5.3	↓	-5.1	↓					-1.02
Monetary Analysis		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Narrow Money (M1)	% y/y	10.7	11.0	↓	12.4	↓					-0.58
Broad Money (M3)	% y/y	7.7	7.7	→	9.4	↓					-0.79
Loans to Non-Fin Corps	% y/y	1.9	1.3	↑	2.6	↓					-0.08
Loans to Households	% y/y	4.3	4.5	↓	4.3	→					-0.05
Consumer / Labour Market		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Retail Sales	% y/y	1.4	3.3	↓	23.7	↓					-0.08
Unemployment Rate	%	7.3	7.6	↓	8.1	↓					-1.35
Labour Costs (Quarterly)	% y/y	-0.1	1.5	↓	2.4	↓					-1.71
Employment (Quarterly)	% y/y	2.1	-1.7	↑	0.5	↑					1.24
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Equity Market	Index	4236	4196	↑	4039	↑					1.06
Bund Yield	%	-0.34	-0.38	↑	-0.19	↓					-0.72
10y BTP Spreads	%	134.3	109.2	↑	109.6	↑					-1.76
EUR TWI	Index	121.07	123.52	↓	125.83	↓					-1.50

Source: MNI, Bloomberg

Summary of Analyst Views

- Analysts broadly expect the current round of net purchases under PEPP to end in March alongside a temporary increase in asset purchases under other programmes to avoid a cliff-edge.
- What form these ‘transition purchases’ take is wide open and range from raising the monthly purchases of APP, introducing a temporary APP envelope or even introducing a new recovery PEPP tool.
- Analysts are also split on whether the full details of the post-PEPP policy setting (in terms of volume of asset purchases) will be announced in December, or whether the ECB will opt to pre-commit in December to ending PEPP while waiting until February to provide specific details on how asset purchases will be used to avert a cliff edge.

Barclays

- The ECB will announce the end of PEPP in March 2022. Purchases of EUR60bn/month via PEPP are expected in Q122.
- The ECB will also indicate that the programme can be reactivated if needed and that reinvestments could be conducted flexibly across jurisdictions and asset classes.
- The APP will be scaled up with an additional envelope of EUR180bn to be used from April 2022 to September 2022 (revised from December 2022 previously). This will allow the ECB to add on average EUR30bn/month to the existing EUR20bn purchase rate during Q2 and Q3 of 2022.
- The ECB is expected to indicate that it is very unlikely that policy rates will be hiked in 2022 with Barclays expecting the first hike to come in 2024.

- An announcement on TLTROs is likely to be postponed until H122
- Expected economic forecast revisions:
    - GDP: 2021 Unchanged at 5.0%, 2022 -0.6pp to -0.4pp to 4.0-4.2%, 2023 +0.2pp to +0.4pp to 2.3-2.5%. Expected 2024 forecast: 1.5%.
    - Inflation: 2021 +0.3pp to +0.4pp to 2.5-2.6%, 2022: +1.0pp to 1.2pp to 2.7-2.9%. Expected Q424 forecast: 1.9-2.0%.

BNP Paribas

- While the ECB is expected to pivot from the PEPP to a more flexible APP next year, an announcement may be delayed until February with the December meeting looking more like a can-kicking exercise.
- Nonetheless, the GC is still likely to strongly hint at the December meeting that PEPP will end in March and that reinvestment will continue until at least December 2023.
- APP flexibility means varying purchases conditional on the inflation outlook and inflation conditions.
- The ECB is expected to increase the starting level of the APP to EUR40bn/month from April. This volume will be reduced over time with net purchases ending in Q123.
- Expected economic forecast revisions:
    - GDP: 2021 +0.1pp to 5.1%, -0.3pp to 4.3%, +0.2pp to 2.3%. Expected 2024 forecast: 1.4%.
    - Inflation: 2021 +0.3pp to 2.5%, 2022 +0.7pp to 2.4%, 2023 +0.1pp to 1.6%. Expected 2024 forecast: 1.8%.

Commerzbank

- The ECB is expected to announce that PEPP will end in March, although the current EUR1.85tn envelope is likely to be fully used.
- An announcement on a new fixed monthly APP volume is unlikely at the December meeting, with the ECB instead opting for a quarter-by-quarter decision on purchase volumes.

Danske

- The ECB will announce that net purchases under PEPP will end in March as originally planned.
- The APP will continue at EUR20bn/month with an additional envelope of EUR250bn. The envelope will provide a degree of implementation flexibility, although Danske expects the capital key and ISIN limits to remain unchanged.
- By scaling up the APP when PEPP ends, ECB bond buying will still match new net supply from European governments in 2022.
- The ECB will provide indications of TLTRO operations in 2022, with an actual announcement perhaps delayed until the February meeting.
- Although the ECB is likely to shutdown speculation of a rate hike in 2022, it is expected to open the door to a 2023 rate hike.
- Expected economic forecast revisions:
    - GDP: 2021 unchanged at 5.0%, 2022 -0.4pp to 4.2%, 2023 +0.1pp to 2.2%. Expected 2024 forecast: 1.6%.
    - Inflation: 2021 +0.3pp to 2.5%, 2022 +0.7pp to 2.4%, 2023 +0.2pp to 1.7%. Expected 2024 forecast: 1.8%.

Goldman Sachs

- The ECB will end PEPP purchases in March.
- The PEPP pace is expected to be stepped down to EUR50bn/month in Q122 followed by a temporary APP increase of EUR120bn on top of the underlying EUR20bn of monthly purchases.
- The GC will reserve the right to conduct PEPP reinvestments flexibly and freeze the remaining EUR100bn unused PEPP envelope for a future date if required.

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- In light of the risks to inflation, GS expects that the APP top-up will be spent by September 2022, three months earlier than previously expected.
- The ECB will defer decisions on other policy parameters to 2022 or even later.
- The emergency features of TLTRO-III – namely the 100bp discount – will be discontinued, while a decision on the tiering multiplier will depend on the health of the banking sector.
- The APP is expected to continue through 2023 with the first policy rate hike coming in 2024.
- Expected economic forecast revisions:
    - GDP: 2021 + 0.3pp to 5.3%, 2022 -0.3pp to 4.3%, 2022 +0.1pp to 2.2%. Expected 2024 forecast: 1.6%
    - Inflation: 2021 + 0.3pp to 2.5%, 2022: +1.0pp to 2.7%, 2023 + 0.1pp to 1.6%. Expected 2024 forecast: 1.8%.

HSBC:

- The ECB will stick with its plan to end PEPP in March with a more moderate pace of net purchases expected during Q122.
- However, the door could be left open for reactivating PEPP beyond March if Covid risks intensify.
- APP will be expanded to avoid a PEPP cliff edge, but HSBC no longer sees support as large as the EUR200bn buffer previously expected.
- There is also a risk that the ECB opts to delay a decision on PEPP until the February meeting.

J.P. Morgan

- JPM note that high uncertainty around the Omicron variant has underpinned a lack of clarity in recent ECB communication with the only firm indications being that PEPP is likely to end in March and that there will be no rate hikes in 2022.
- Total asset purchases (APP plus PEPP) are expected to slow to around EUR50bn/month during Q222 from around EUR90bn/month currently, slowing further thereafter.
- JPM continues to highlight the legal/institutional difficulties of transferring PEPP flexibility to the APP.
- Instead, JPM sees scope for a 'recovery PEPP' to replace the current 'emergency PEPP' with a duration of nine months, an envelope of EUR200-250bn and retention of PEPP's flexibilities but with a higher hurdle for deviating from the capital key.
- A decision on TLTROs is likely to be deferred until the February meeting.

Lloyds

- The PEPP is expected to end in March with the APP increased to partially compensate for the end of the pandemic purchases.
- Lloyds sees scope for the APP to be raised to EUR40bn/month for six months.
- Given the uncertainty around the Omicron variant, the ECB may delay a decision on this until the new year.

Morgan Stanley

- Given heightened uncertainty, there is a case to be made for a slower withdrawal of stimulus measures.
- MS assumes a steady EUR70bn/month PEPP pace in January and February with a modest decline to EUR60bn/month in March. This would imply almost full use of the current envelope by end-March.
- The ECB will confirm at the December meeting that asset purchases under PEPP will be concluded in March.
- MS note that it is not clear whether the preconditions for terminating PEPP – namely growth back to pre-pandemic levels and an end to the crisis phase of the pandemic – will have been unambiguously met by this point. The GC could decide to introduce a clause in the December meeting to allow a reactivation of PEPP if the pandemic deteriorates further.
- The ECB will also announce an enhanced and flexible APP running at EUR40bn/month on average through the remainder of 2022 following the conclusion of PEPP in March. As with PEPP, the purchase pace will be recalibrated at each forecast meeting.

- The limit on supra purchases will be removed, but the issuer limits will remain unchanged.
- Full reinvestment of PEPP and APP will be extended until end-2024.

Natixis

- The lack of broad consensus suggests that the GC may not announce a detailed plan or its policy actions in 2022 at the December meeting.
- Instead, the ECB is expected to announce that PEPP will end in March and that purchases under the APP will be conducted with a higher degree of flexibility.
- This could involve setting a total envelope for purchases under the APP in 2022 without predetermining monthly volumes.
- While a decision on additional refinancing operations may not be made at the December meeting, the GC could provide some colour on which way the ECB is leaning.
- Expected economic forecast revisions:
    - GDP: 2021 unchanged at 5.0%, 2021 -0.1pp to 4.5%, 2022 +0.4pp at 2.5%. Expected 2024 forecast: 1.5%
    - Inflation: 2021 + 0.4pp to 2.6%, 2022 + 0.6pp to 2.3%, 2023 unchanged at 1.5%. Expected 2024 forecast: 1.8%.

Nordea

- Net purchases under PEPP will likely end in March, but buying will still be notable in the coming months.
- The APP will take over when PEPP ends, but it is far from certain that the ECB will be ready to make a detailed decision at the December meeting.
- Nordea expects the ECB to opt for a EUR100-200bn APP envelope, with the decision potentially postponed until Q122.
- A decision on TLTROs will also be postponed until next year.
- PEPP reinvestments can be use flexibly to tackle fragmentation risks.
- Forward guidance on policy rates and asset purchases will remain unchanged.

Nomura

- The ECB will stick with its plan to end purchases under PEPP in March.
- To avoid an aggressive slowdown in purchases, the ECB will raise purchases under the APP to EUR40bn/month from EUR20bn/month starting in April.
- The risk to this view would be the ECB opting for a more discretionary approach involving a temporary APP envelope which could be deployed flexibly should the need arise.
- It is also possible that beyond confirming that PEPP will end in March, the ECB may decide to delay any further announcements until February when virus conditions could be clearer.

RBC

- The ECB is expected to announce that the PEPP will continue at the current pace and be terminated in March as planned.
- The ECB will also announce that the APP will inherit some of the PEPP flexibilities and will be expanded in April to avoid a PEPP cliff edge.
- RBC expects a EUR400-500bn envelope with a pace of around EUR50/bn month which will continue until the end of December 2022. RBC further stress that it is unclear whether all of these policy specifics will be announced at the December meeting.

Scotiabank

- The ECB is likely to end the PEPP in March and temporarily raise purchases under the APP.
- President Lagarde is also likely to repeat that it is very unlikely that policy rates will rise in 2022.

Swedbank

- No changes to the monetary policy stance or forward guidance are expected at the December meeting.
- Details of an increase in APP to prevent a post-PEPP cliff edge are unlikely to be announced just yet.
- The ECB is likely to signal its flexibility and readiness to adjust APP but will adopt a 'wait and see' approach before providing further details.

TD Securities

- The ECB will confirm that the PEPP will end in March alongside a temporary increase to the APP through Q222 of around EUR50bn/month. There will also be a commitment to revisit the APP at a later date.
- Expected 2024 inflation forecast: 1.8%.
- Over the course of 2022, TD Securities expects the following policies to be announced at some point in the future: APP to run at EUR50bn/month (through to early 2024), new and less generous refinancing operations and no change to key policy rates.

UniCredit

- Given that the GC does not seem to regard Omicron a serious downside risk, UniCredit expects the ECB to announce that purchases under PEPP will end in March alongside an increase in monthly purchases under the APP to EUR40bn/month.
- Any announcement of an APP envelope for 2022 would leave plenty of scope for the GC to recalibrate purchases conditional on financing conditions and the medium-term outlook.
- Some degree of PEPP flexibility could be retained through reinvestments and by reactivating the facility if needed.

Wells Fargo

- The ECB will end PEPP on schedule in March. Purchases will ultimately come in slightly below the EUR1.85tn envelope.
- The APP will be increased to EUR50bn/month from EUR20bn/month.

UBS

- Despite the emergence of the Omicron variant and new mobility restrictions across Europe, the ECB will announce an end to the PEPP in December alongside a beefed-up APP.
- PEPP purchases will be conducted at a moderately slower pace in Q122 with purchases terminated at the end of March. Reinvestments will continue until at least end-2023.
- The ECB will keep an open-ended commitment to continue the APP until the inflation target has been sustainably met.
- In addition to the current EUR20bn APP run rate, an additional envelope of EUR150-250bn for 6-9 months will be introduced to avoid a PEPP cliff edge.
- The issue/r limits for the APP are no expected to be raised and the capital key will continue to guide purchases.
- Decisions on new TLTROs and tiering will be deferred until H122.
- Expected economic forecast revisions:
    - GDP: 2021 unchanged at 5.0%, 2022 -0.3pp to 4.3%, 2023 + 0.1pp to 2.2%. Expected 2024 forecast: 1.6%.

- Inflation: 2021 +0.4pp to 2.6%, 2022 +1pp to 2.7%, 2023 +0.1bp to 1.6%. Expected 2024 forecast: 1.7%.
- The UBS base foresees accommodative ECB policy through 2022-2023 although there is a growing risk that the APP starts to wind down in early 2022 with rate hikes in 2023.

ECB Communication: The Detail

While the ECBs official stance on inflation (temporary rather than persistent) and the outlook for PEPP (likely to end in March) have not fundamentally changed, there are signs of diverging opinions within the GC. While some policymakers are still rigidly sticking to the script and argue that the recent inflation surge is driven by temporary impulses which will subside next year, others are starting to warn that risks are shifting to the upside.

Starting with the current state of economic conditions, various members have highlighted the slowdown in momentum following a strong growth spurt in the summer. Isabel Schnabel stated on November 17:

> "All in all, the pace of recovery over the summer was extraordinary and indeed much faster than many of us expected, thanks in large part to the marked rise in the number of people who are fully vaccinated."

> "Incoming data over the past few weeks, however, suggest that economic activity globally and in the euro area has started to moderate. This did not come as a surprise. Given the exceptional pace of expansion over the summer, a moderation was to be expected. Even a visible slowdown would still leave growth at historically high levels."

On the burning issue of inflation, Madis Muller stuck with the ECB's official stance on November 3, stating:

> "The factors that have currently increased the pace of inflation are largely, by their nature, temporary in relation to the fast rise of energy prices and also various supply chain difficulties, which have increased the prices of certain products"

With Pablo Hernández de Cos reiterating on November 29:

> "…this pick-up in actual inflation has, broadly speaking, been driven by specific and largely pandemic-related factors, whose impact can be expected to wane, or in some cases even disappear, over the course of next year."

And further:

> "…for now events remain consistent with a return to the situation of moderate inflationary pressure in the medium term that characterized the pre-pandemic period"

Isabel Schnabel offered a succinct assessment on November 17 of why supply bottlenecks mean that inflation is likely to subside, while also highlighting the uncertainty around this projection:

> "…supply bottlenecks, by their very nature, do not diminish growth potential. They merely shift activity over time. Port congestions cannot last indefinitely. In a competitive economy, supply will eventually catch up with demand, even if it takes longer than previously expected."

> "…contrary to the 1970s and much of the past decade, we are now facing a macroeconomic environment characterised mainly by deficient supply rather than deficient demand. Supply bottlenecks are tempering what has become one of the strongest demand shocks in recent history.

Companies operating at the earlier stages of the value-added chain are producing at full capacity, while firms at the final stages are facing an unprecedented wedge between the amount of orders on the one side and production activity on the other."

"There is broad agreement on the main factors that are currently pushing up inflation: rising energy prices, shortages of goods, equipment and labour, as well as statistical base effects."

"There is less agreement on the persistence of many of these price pressures, and what they mean for the appropriate response of monetary policy."

Regardless of which inflation scenario the Eurozone faces, there is no escaping the fact that inflation is running far hotter than the ECB was expecting as noted by Pablo Hernández de Cos on November 29:

"The upturn in inflation is proving more pronounced and longer-lasting than we anticipated some months ago".

A reality that Luis de Guindos similarly pointed out on November 15:

"…the current phase of higher inflation, reflecting in part the afore mentioned increase in energy prices and supply constraints, could last longer than expected only some months ago, as reflected in the European Commission's projections released last week."

And by Luis de Guindos on December 8:

"The current phase of higher inflation could last longer than expected only some months ago,"

For the time being many on the GC still point to the lack of wage pressure as evidence that second-round effects are not yet a prominent concern. With respect to wage negotiations, Philip Lane stated on November 3:

"We will look out for unsustainable patterns that might lead to pressures that are undesirable from an inflation perspective. But let me emphasise: we don't see this right now. It's more of a risk factor that we need to take a look at, rather than something where we see any evidence building"

Fabio Panetta argued on November 24:

"Typically, a sustained increase in wages requires the economy to be operating persistently above potential. This is not currently the case in the euro area. Estimates of the output gap suggest that it will take time before it is convincingly positive."

"Wage pressures could still emerge before the economy reaches full capacity if there are widespread matching inefficiencies in the labour market – for instance owing to structural changes triggered by the pandemic – or if the inflation spike impacts wage bargaining dynamics. But neither appears to be the case today."

And concluded that:

"…if the sources of higher inflation today do last longer, there is little or no evidence at this stage to suggest that they would feed into wage-price spirals or a de-anchoring of inflation expectations in the euro area. There are, instead, signs that they could weaken the recovery and reduce underlying inflation pressures."

Gabriel Makhlouf added on November 24:

> “Recent data for the euro area does not suggest, at least thus far, that higher inflation in 2021 is feeding into broad-based higher wage demands, although the upheaval in the labor market makes it more challenging than ever to extract timely and accurate insights from the data”

While Luis de Guindos stressed on December 8:

> “So far there is no evidence of second-round effects from high inflation when it comes to wages”

While also arguing that wage growth will be higher in 2022.

Speaking on November 23, Isabel Schnabel highlighted the current lack of wage pressures while similarly pointing to a pickup in wages next year.

> “On the wage side, so far we have not seen any broad-based wage pressures that could give rise to wage-price spirals. But we do see in our corporate telephone survey that firms expect wages to grow more strongly going forward. There is also no sign that inflation expectations are de-anchored to the upside.”

And, again, Luis de Guindos offered a similar assessment on November 15:

> “So far there is no evidence of second-round effects from higher inflation outcomes to wages and back to prices. But wage growth is expected to be somewhat higher in 2022 than in 2021.”

And, finally, President Lagarde argued on November 26:

> “Judging by what we know from surveys of employers and trade unions so far, no strong inflationary pressure is to be expected from that front for the time being. The negotiated wage settlements have been very moderate so far. For next year, somewhat higher wage demands are partly to be expected. But based on what we are seeing, the settlements should not be on a scale that might trigger a wage-price spiral.”

While still broadly holding firm on the ECB’s assessment for the inflation path, GC members have increasingly stated the risks are now shifting to the upside as reflected in comments made by Isabel Schnabel on November 23:

> “It’s plausible to assume that inflation is going to drop below our target of 2% in the medium term. However, the risks to inflation are skewed to the upside”

Madis Muller suggested on December 8 that longer-term inflation risks are:

> “..higher in general and they are tilted to the upside,”

And that although he believes that current higher inflation is being driven by temporary factors, there is

> “a risk that the longer inflation stays at such levels, the higher will also be the probability of second-round effects”

Luis de Guindos stated on November 29:

> “The European Central Bank is continuously pointing out that the inflation rebound in recent months is of a transitory nature,”

> “However, we have also seen how in recent months these supply factors are becoming more structural, more permanent.”

Klaas Knot offered a more emphatic warning on November 9:

> “We should not be complacent about upside risks to inflation,”

> “We cannot make long-lasting unconditional commitments that might end up being incompatible with how the inflation outlook develops.”

The uncertainty around the inflation risks and divergence of opinions across the GC complicate the ECB’s policy decision in December. The more dovish members of the GC continue to assert that monetary policy should help secure the recovery and that tightening now would be premature – a position stressed by President Lagarde on November 3:

> “Regarding asset purchases, for the time being, we continue to use the PEPP to safeguard favourable financing conditions and ensure that borrowing costs for all sectors of the economy do not unduly tighten. An undue tightening of financing conditions is not desirable at a time when purchasing power is already being squeezed by higher energy and fuel bills, and it would represent an unwarranted headwind for the recovery.
>
> As for the calibration of bond purchases in a post-pandemic world, we will announce our intentions in December. Even after the expected end of the pandemic emergency, it will be still important that monetary policy – including the appropriate calibration of asset purchases – supports the recovery and the sustainable return of inflation to our target of 2%.”

Klaas Knot has been unequivocal in supporting an end to PEPP even in the face of the fresh lockdowns:

> “I don’t think myself that it will have an impact on our intention to wind down the pandemic emergency purchase program”
>
> “After all, its dual objectives have already been accomplished.”

Others have stressed that even if PEPP is concluded in March, some degree of flexibility can be retained. Indeed, François Villeroy de Galhau stated on November 25:

> “We can end the PEPP net asset purchases in March, while keeping flexibility,”
>
> “The infrastructure of the program will remain in place, notably with the reinvestments; it could be mobilized again in the case of exceptional on some assets, or unjustified fragmentation between countries of the euro zone. It’s what I call our virtual toolbox”

A position supported by Madis Muller on December 7:

> “We need to have some flexibility in decision-making going forward but PEPP can end”

Isabel Schnabel also stressed that PEPP will not be permanently eradicated after March:

> “The PEPP will not disappear once net asset purchases have been reduced to zero. Sometimes people talk about ending the PEPP. The PEPP is not going to end in March. The net asset purchases probably, b but not the PEPP as such.”

While a decision on the future course for asset purchases is likely to be a thorny issue, GC policymakers are more aligned on the limited prospect of policy rates hikes in 2022. President Lagarde stressed on November 3:

> “In our forward guidance on interest rates, we have clearly articulated the three conditions that need to be satisfied before rates will start to rise. Despite the current inflation surge, the outlook for inflation over the medium term remains subdued, and thus these three conditions are very unlikely to be satisfied next year.“

Francois Villeroy stated on November 29:

> “The conditions for an increase in interest rates according to our forward guidance are very unlikely to be met in 2022”.

Similarly, Madis Muller argued on November 3:

> "On the question of when the ECB could first begin increasing interest rates, the ECB Council has publicly said this can happen once we see price increases have consistently reached 2%. According to the most recent forecasts, we're clearly not yet in this situation"

> "I'm not convinced we can say that we're consistently at a stable 2% level for consumer prices in the euro area as a whole"

Luis de Guindos stated on November 17:

> "My personal view is that we're not going to see a rate increase in 2022"

> "We're data dependent. We'll see what happens over the next months with the evolution of the economy, the evolution of inflation, but my personal view is that it's going to be quite unlikely."

Gabriel Makhlouf was even more emphatic:

> "On the evidence we see today increases in interest rates are absolutely not warranted"

With Philip Lane similarly unequivocal in arguing that rate rises are not on the table for now:

> "Given our assessment that the medium-term inflation trajectory remains below our two per cent target, it would be counter-productive to tighten monetary policy at the current juncture."

ECB Inter-Meeting Communication

Date	Time	Speaker	Event
29/10/2021	09:00		ECB Survey of Professional Forecasters
29/10/2021	11:00		G20 Joint Finance and Health Ministers Meeting
02/11/2021	11:20	Frank Elderson	Panel participation "Action on Forests and Land Use" at the UN Climate Change Conference UK 2021
02/11/2021	11:55	Pablo Hernández de Cos	Speech on banking regulation at the Santander International Banking Conference 2021
03/11/2021		Frank Elderson	Interview for Bloomberg TCV conducted by Francine Lacqua on 2 November https://www.ecb.europa.eu/press/inter/date/2021/html/ecb.in211103~e8bcb85b25.en.html
03/11/2021	08:00	Frank Elderson	Participation in an even for the UN Climate Change Conference UK 2021
03/11/2021	09:30	Christine Lagarde & Mário Centeno	Speech 'Learning from Lisbon: recovery and resilience in Europe' on the occasion of the 175th anniversary of Banco de Portugal in Lisbon https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211103~d0720ef27b.en.html
03/11/2021	10:00	Madis Müller	Speech at a Financial Stability Event https://www.youtube.com/watch?v=z8qLWgQATBk

03/11/2021	10:15	Frank Elderson	Keynote speech 'The NGFS Glasgow Declaration – From a coalition of the willing to a coalition of the committed' at the COP26 Finance Day Presidency Event on “A Financial System for Net Zero” https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211103_1~981d1ed885.en.html
03/11/2021	10:40	Pablo Hernández de Cos	Speech on the future of the European banking system
03/11/2021	13:00	François Villeroy de Galhau	Conference speech in Lyon
03/11/2021	14:30	Frank Elderson	Panel participation "In depth presentation of the NGFS achievements/strategy" for the UN Climate Change Conference UK 2021
04/11/2021	11:00	Pablo Hernández de Cos	Speech on the Spanish Economy at an economic summit in Galicia
04/11/2021	13:00	Christine Lagarde	Opening remarks at the ECB-CEPR Women In Economics Conference
04/11/2021	14:00	Frank Elderson	Panel contribution at the COP26 World Leaders’ Summit Presidency Event on “Action on Forest and Land Use” https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211104~701dd5f918.en.html
04/11/2021	18:15	Isabel Schnabel	Participation in the panel "Rebuilding After Covid: Central Banking In Support of Society and a New Social Contract" for the ECB-CEPR Women In Economics conference.
05/11/2021	08:30	Robert Holzmann	Speech at the Austrian Association of Business Journalists
05/11/2021	08:30	Luis de Guindos	Remarks made at an event organised by the Confederacion Mutualidades and Axon Partners Group
05/11/2021	09:00	Mário Centeno	Speech at a conference organised by the Portuguese securities regulator CMVM.
05/11/2021	11:00	Fabio Panetta	Speech 'Central bank digital currencies: a monetary anchor for digital innovation' at the Elcano Royal Institute, Madrid https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211105~08781cb638.en.html
05/11/2021	12:30		Speech at a money conference organised by Global Media
08/11/2021		Philip R. Lane	Interview with El Pais conducted by Lluís Pellícer on 3 November 2021 https://www.ecb.europa.eu/press/inter/date/2021/html/ecb.in211108~c270ad5bc6.en.html
08/11/2021	10:00	Gabriel Makhlouf	Speech on macroprudential policy at ESRI
08/11/2021	13:10	Philip R. Lane	Welcome address 'Inflation in the short term and in the medium term' at the ECB Conference on Money Markets https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211108~c915d47d4c.en.html

08/11/2021	14:00	Philip R. Lane	Speech at a Brookings Institute event on Fed and ECB monetary policy frameworks
09/11/2021	07:45	Fabio Panetta	Presentation 'Digital currencies around the world – what are the policy implications?' at the high-level panel on central bank digital currency, 30th Anniversary Conference of the Bank of Finland Institute for Emerging Economies (BOFIT) https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211109~058e03e806.en.pdf?b4ced0233e495b1ca10d51e85c350f25
09/11/2021	13:00	Christine Lagarde	Welcome address at the ECB Forum on Banking Supervision, 9 November 2021 https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211109_1~6cdc943638.en.html
09/11/2021	14:00	Klaas Knot	Speech at a UBS panel event.
09/11/2021	16:00	Isabel Schnabel	Speech 'Monetary policy and inequality' at a virtual conference on “Diversity and Inclusion in Economics, Finance, and Central Banking” https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211109_2~cca25b0a68.en.html
10/11/2021	08:00	Jens Weidmann	Speech at a Bundesbank conference on the Future of Cash
10/11/2021	09:30	Frank Elderson	Speech at the ECB Forum on Banking Supervision
11/11/2021	09:00		ECB Publishes Economic Bulletin
11/11/2021	09:00	Gabriel Makhlouf	Keynote speech at the 14th European SSM Roundtable
11/11/2021	12:15	Philip R. Lane	Introductory remarks 'Expectations surveys: a tool for research and monetary policy' at the Second joint European Central Bank – Federal Reserve Bank of New York conference https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211111~9177268ea9.en.pdf?31272b6ae07148d65fb1b8399440dd38
11/11/2021	16:00	Isabel Schnabel	Speech at an event organised by the Women In Economics Initiative and the Women In Business Program
12/11/2021	13:50	Philip R. Lane	Panel intervention 'The future of the EU fiscal governance framework: a macroeconomic perspective' at the European Commission webinar on “The future of the EU fiscal governance framework” https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211112~739d3447ab.en.html
15/11/2021	10:00	Christine Lagarde	Introductory statement at the Hearing of the Committee on Economic and Monetary Affairs of the European Parliament (by videoconference) https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211115~6fa9a12c1e.en.html
15/11/2021	15:45	Luis de Guindos	Speech 'Recovery from the pandemic crisis – challenges for the financial sector ' at the 24th Euro Finance Week https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211115_1~c86d858b33.en.html
16/11/2021	16:10	Christine Lagarde	Speech at the 10th Anniversary of Financi'Elles https://www.youtube.com/watch?v=s7w0AaZf1AY
17/11/2021	01:20	Christine Lagarde	Video message for the 'Female Leaders Video Series' for an event organised by Friends of IHES
17/11/2021	09:00		ECB Publishes Financial Stability Review

17/11/2021	14:00	Isabel Schnabel	Speech 'Reflation, not stagflation' at a virtual event organised by Goldman Sachs https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211117~78f0a1f435.en.html
18/11/2021	09:30	Mário Centeno	Speech for an online conference on banking organised by Jornal de Negocios
18/11/2021	10:00	Fabio Panetta	Introductory remarks 'Designing a digital euro for the retail payments landscape of tomorrow' at the ECON Committee of the European Parliament https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211118~b36013b7c5.en.html
18/11/2021	14:30	Philip R. Lane	Participation in the discussion "The New Federal Reserve and ECB Strategies - Implications for Monetary Policy" at the "Transatlantic Economic Policy Responses to the Pandemic and the Road to Recovery" conference organised by the EC, the Federal Reserve Bank of New York and the CEPR
19/11/2021	08:30	Christine Lagarde	Keynote speech 'Commitment and persistence: monetary policy in the economic recovery' at the 31st Frankfurt European Banking Congress 2021 "From Recovery to Strength" https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211119~3749d3556c.en.html
19/11/2021	13:00	Jens Weidmann	Keynote speech for the "From Recovery to Strength" event at the 31st Frankfurt European Banking Congress https://www.frankfurt-ebc.com/programme-2021/
22/11/2021	14:00	Robert Holzmann, Mārtiņš Kazāks & Peter Kažimír	Speech at a conference on CEE monetary policy
22/11/2021	17:00	Pablo Hernández de Cos	Introductory remarks at the Bernacer award ceremony
22/11/2021	17:30	Luis de Guindos	Remarks 'Ralph Koijen's contribution to research on the pricing of risk in equity and insurance markets' at the virtual ceremony awarding the 2020 Germán Bernácer Prize to Ralph Koijen https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211122~75b8a1488c.en.html
23/11/2021		Isabel Schnabel	Interview with Bloomberg conducted by Carolynn Look and Alexander Weber on 22 and published on 23 November 2021 https://www.ecb.europa.eu/press/inter/date/2021/html/ecb.in211123~484ab3aa81.en.html
23/11/2021	17:30	Gabriel Makhlouf	Speech for the Irish parliamentary committee
24/11/2021	10:10	Fabio Panetta	Speech 'Patient monetary policy amid a rocky recovery' at Sciences Po https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211124~a0bb243dfe.en.html
24/11/2021	16:00	Isabel Schnabel	Presentation 'A new strategy for a changing world' at a Youth Dialogue hosted by the University of Sofia https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211124_1~98461a44c7.en.pdf?08d7bf01f9e15d2eeba2e1b253e7b0cd

25/11/2021	08:00	François Villeroy de Galhau	Speech at an ACPR conference
25/11/2021	08:10	Frank Elderson	Speech 'When you need change to preserve continuity: climate emergency and the role of law' at the ECB Legal Conference 2021 https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211125~2da387f2ce.en.html
25/11/2021	09:00	Isabel Schnabel	Presentation 'Inflation im Euroraum: Ursachen und Ausblick' at a meeting organised by Wirtschaftsrat der CDU https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211125_1~af734cf52b.de.pdf?d9b05729b68e524727b5d145f65cf1bf
25/11/2021	10:00		Bundesbank presents Financial Stability Report
25/11/2021	12:30		ECB Publishes Account of October Policy Meeting
25/11/2021	13:30	Christine Lagarde	Speech at the ECB Legal Conference 2021 https://www.ecb.europa.eu/pub/conferences/html/20211125_4th_ECB_legal_conference.de.html
25/11/2021	17:15	François Villeroy de Galhau	Speech at a conference in Paris
26/11/2021		Christine Lagarde	Interview with Frankfurter Allgemeine Sonntagszeitung conducted by Gerald Braunberger, Dennis Kremer and Christian Siedenbiedel on 23 November and published on 26 November 2021 https://www.ecb.europa.eu/press/inter/date/2021/html/ecb.in211126~80dc9eeac7.en.html
26/11/2021	01:15	Luis de Guindos	Speech an an economic summit in S'Agaro
26/11/2021	08:00	Christine Lagarde	Keynote speech 'Change and continuity in law' at the ECB Legal Conference 2021 https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211126~6fe408acd1.en.html
26/11/2021	08:00	Ignazio Visco	Speech at a European Banking Association event
26/11/2021	08:30	Isabel Schnabel	Chairing a panel at the ECB Legal Conference 2021
26/11/2021	10:30	Fabio Panetta	Chairing a panel at the ECB Legal Conference 2021
26/11/2021	13:30	Philip R. Lane	Chairing a panel at the ECB Legal Conference 2021
26/11/2021	15:15	Pablo Hernández de Cos	Speech at an economic summit in S'Agaro on the eurozone's monetary and fiscal challenges
28/11/2021	10:40	Fabio Panetta	Interview at Festa dell'ottimismo 2021 organised by Il Foglio
29/11/2021		Isabel Schnabel	Interview with ZDF Morgenmagazin conducted by Mitri Sirin on 29 November 2021 https://www.ecb.europa.eu/press/inter/date/2021/html/ecb.in211129~da0141d2fa.en.html
29/11/2021	07:35	Isabel Schnabel	Presentation 'Inflation im Euroraum: Ursachen und Ausblick' at a meeting organised by Bundesverband der Deutschen Industrie (BDI) https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211129~3caf5f2922.de.pdf?32c30c17181b612c7c8801f4ff4a7f64

29/11/2021	08:15	François Villeroy de Galhau	Speech for an online conference
29/11/2021	08:15	Pablo Hernández de Cos	Speech at a banking event organised by El Economista
29/11/2021	08:30	Luis de Guindos	Speech
29/11/2021	09:30	Mário Centeno	Speech at a conference organised by the Bank of Portugal on the challenges facing the Portuguese economy following the pandemic https://www.bportugal.pt/evento/conferencia-expresso-e-banco-de-portugal-os-desafios-da-economia-portuguesa-no-pos-pandemia
29/11/2021	11:30	Isabel Schnabel	Participation in an event organised by BDI
29/11/2021	12:30	Pablo Hernández de Cos	Speech at a banking and economic event organised by Daily Expansion
29/11/2021	17:15	Christine Lagarde	Lectio Magistralis 'Dialogue in a changing world' at the Accademia Nazionale dei Lincei https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211129_1~12fc1248a8.en.html
30/11/2021		Luis de Guindos	Interview Les Echos conducted by Guillaume Benoit, Édouard Lederer and Thibaut Madelin on 24 November and published on 30 November https://www.ecb.europa.eu/press/inter/date/2021/html/ecb.in211130~887737ac79.en.html
30/11/2021	09:00	François Villeroy de Galhau	Speech at an online conference on capital markets union
30/11/2021	14:00	Pablo Hernández de Cos	Speech the Spanish Senate Budget Committee
02/12/2021	14:00	Fabio Panetta	Chairing a panel at the Fifth ECB biennial conference on Fiscal policy and EMU governance https://www.ecb.europa.eu/pub/conferences/html/20211202_5th_fiscal_policy_conference.en.html
03/12/2021	08:30	Christine Lagarde	Participation in an online Q&A organised by Reuters
03/12/2021	13:00	Philip R. Lane	Keynote lecture at the Fifth ECB biennial conference on Fiscal policy and EMU governance
07/12/2021		Christine Lagarde	Interview with Che Tempo Che Fa conducted by Fabio Fazio on 28 November and published on 7 December 2021 https://www.ecb.europa.eu/press/inter/date/2021/html/ecb.in211207~4a6bc318c1.en.html
08/12/2021	08:15	Christine Lagarde	Welcome remarks 'Macroprudential policy in Europe – the future depends on what we do today' at the fifth annual conference of the ESRB https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211208~e18612adce.en.html

08/12/2021	08:25	Luis de Guindos	Speech 'Macroprudential policy for non-bank financial intermediation' at the 5th ESRB Annual Conference https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211208_1~9a61c122f7.en.html
08/12/2021	10:00	Olli Rehn	Participation in a webinar
08/12/2021	11:30	Luis de Guindos	Participation in a panel discussion on non-bank financial intermediation fragilities at an ESRB Conference https://www.esrb.europa.eu/news/schedule/2021/html/20211208_5th_annual_conference.en.html
08/12/2021	13:10	Isabel Schnabel	Speech 'Monetary policy and financial stability' at the fifth annual conference of the European Systemic Risk Board https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp211208_2~97c82f5cfb.en.html
10/12/2021	09:05	Christine Lagarde	Participation in a panel discussion organised by the BIS
10/12/2021	09:05	Christine Lagarde, Jens Weidmann & François Villeroy de Galhau	Participation in a panel discussion organised by the BIS
10/12/2021	10:00	Fabio Panetta	Speech "Presente e futuro della moneta nell'era digitale. Le opportunità per il risparmio e lo sviluppo"
10/12/2021	14:40	Frank Elderson	Introductory remarks at the MCM-SARTTAC climate webinar
13/12/2021	11:30	Mário Centeno	Speech at a book presentation

MNI Policy Team

MNI SOURCES: ECB Seen Buying EUR40-60 Bln A Month After March 10 December 2020

MNI (London) - The European Central Bank is likely next week to open the way to a boost in its Asset Purchase Programme to up to a flexible EUR40-60 billion a month following the end of the active phase of its Pandemic Emergency Purchase Programme in March, several sources told MNI, though some governors are arguing that upscaling APP would be inappropriate given rising inflation.

“There are no firm numbers yet....... there is still a need to agree them, but I still believe that we will settle at a [net new] purchase level around 40 - 50 billion a month -- perhaps the lower end given the concern of many over current headline inflation rates, although we must avoid any severe cliff-edge effects,” one eurosystem official said, speaking ahead of next week's key Governing Council meeting.

ECB officials have long expected that the PEPP would be followed by an increase in the APP's EUR20 billion runrate, for perhaps 9-12 months, he said. Initial expectations had been for total purchases of EUR500 billion during this period, though this may now turn out to be lower.

"Of course, any agreement on size now can always be amended -- up or down -- as needed in future times," the official said, noting that the ability to amend the rate of purchases would not be the same as setting a maximum envelope with the intention of not using it all.

FLEXIBILITY

"We could say not all has to be used, but be symmetric saying more could be used if need be. That will fit nicely with a key thematic moving into 2022 of maximum flexibility."

Other sources roughly agreed with these numbers, with one eurosystem official pointing to somewhere in the region of EUR40-60 billion, a range which MNI first reported being considered in May. (See MNI SOURCES: ECB Seen Halving Asset Purchases After PEPP) A former official said he would guess the year's purchases would total EUR300-400 billion, with the rate calibrated according to financing conditions and inflation and flagged in speeches by policymakers.

"As it's Christmas time, there might be a small parcel under the tree," one of the officials said. "I'm not sure this would convince everybody, but it won't be necessary to convince everybody."

While the sources pointed to a bolstered APP as a likely outcome, some Governing Council members are likely to resist an increase in its purchase envelope at a time of rising inflation.

Other officials declined to specify likely purchase amounts as final agreement remains to be had not only on that but also on how purchases are made. Two officials said that extending the PEPP for a quarter or two beyond March remains an option, as Covid's Omicron variant adds to uncertainty. Others said this possibility was now unlikely.

PEPP "IN THE FRIDGE"

The ECB is though likely to point to the possibility that the PEPP, which will continue to make reinvestments, could be reactivated.

"You can take the PEPP and put it in the fridge," one official said. "You don't have to destroy it."

Another possibility has been highlighted by the ECB's former director general of market operations Francesco Papadia, who suggests that fixed APP purchases could remain at EUR20 billion a month, while an additional envelope would be available to spend if financial conditions deteriorate, effectively functioning like a form of yield curve control.

Other mooted options, including loosening the rules on APP bond buying or creating a new envelope for a "sleeper PEPP" only to be used in an emergency, may prove too controversial, officials said.

December's monetary meeting will be the last attended by outgoing Bundesbank president Jens Weidmann - a fact to be considered when weighing up the size of any additional stimulus package.

"Of course, it can't be too big, because otherwise the new Bundesbank present won't be very happy with his present," one source said. "Also for political reasons. It would be very hard messaging for the new government."

Current guidance for the ongoing rate of PEPP purchases, which specifies a “moderate” reduction in pace compared with last December, could be adjusted further downwards or left unchanged, sources said.

An ECB spokesperson declined to comment to MNI.

MNI INTERVIEW: ECB Needs Limited,Flexible PEPP Successor-Kazaks 24 November 2021

By Luke Heighton

MNI (Frankfurt) - The successor to the European Central Bank's Pandemic Emergency Purchase Programme should be limited in size and duration but used flexibly, Bank of Latvia Governor Martins Kazaks told MNI.

The PEPP's active phase can end as planned in March 2022, Kazaks said in an interview, with the worst of the economic impact of the Covid-19 pandemic beginning to fade and GDP growth set to continue at a decent rate at least over the medium-term forecast horizon, barring sudden macroeconomic shocks.

Inflation, continuing to beat earlier expectations in absolute terms and likely to stay higher for longer, will likely fall to a level just short of 2% by 2023-24, albeit with upside risks, Kazaks said, adding that he expects some upward revision to December's Eurosystem staff growth and inflation projections.

The ECB should not begin to consider raising key interest rates until labour market slack disappears and wages are pushed up on a sustainable basis, he said.

"The labour market is very much the missing link. There's growing indirect evidence that wage pressures are strengthening, and we also see that producer price increases are likely to be transferred into consumer prices. But we still do not see that in actual data. So, there's no need to overreact. There will be inflation projections in December, and again in the spring, and another in the summer. Let's take it step-by-step."

LOCKDOWNS

The reimposition of lockdown conditions in some European countries in response to rising infection rates is unlikely to seriously dent the recovery, he said.

"The question is, what's the sensitivity of the economy to these lockdowns?" Kazaks said. "Are we talking about significantly slower growth? I don't think that they are likely to derail the overall economic recovery, so in terms of PEPP the story is relatively clear."

Ongoing support offered through the reinvestment of principal payments from PEPP should not be underestimated, he said.

"Flexibility is not disappearing, at least in my view, during the reinvestment phase. The end of PEPP does not mean that we are finishing supporting the economy. By no means, we are not withdrawing support, we are just adding less."

December's Governing Council debate over how to cushion the landing once PEPP's net purchase phase is over should adopt a solution that is both cautious and flexible, Kazaks said. MNI has separately reported that debate over post-PEPP stimulus will focus on possibly adding flexibility to an pre-existing bond purchasing scheme or on the creation of a "sleeper" PEPP to be used only at times of market stress. (See MNI SOURCES: Hawks Emboldened As ECB Nears Crunch December)

"Do we see the necessity of a temporary instrument or an add-on to avoid the risk of unwanted too sharp tightening and market? Temporary meaning limited in time with a guideline in terms of the size. But, again, if such an instrument or add-on is eventually decided to be necessary, it should be used flexibly. And we do not need to spend all of it."

Removing from current forward guidance the reference to ending bond buying under the ECB's non-pandemic-specific asset purchase programme, APP, shortly before raising rates would further signal the Governing Council's commitment to flexibility, he said, and should not be taken as a sign of either a dovish or a hawkish shift. But it is not a priority next month.

By contrast, the tightening narrative becoming established in the U.S. would be inappropriate at the current juncture in Europe's recovery, he said.

"It is a communications challenge," he said. "There are some spill-overs, and some of them are unwarranted. The euro area economy, in terms of its business cycle, is lagging behind that of the U.S., and that very clearly puts a wedge between the decisions that are made by the Fed and the ECB. The Fed is removing support. We are about to reduce the support."

MNI INTERVIEW: Smaller Facility To Replace ECB's PEPP-Papadia 22 November 2021

By Jason Webb

The European Central Bank is likely to replace its Pandemic Emergency Purchase Programme with a similar, but significantly smaller, bond-buying facility once it expires in March, as it seeks to ensure its monetary policy firepower while the Covid pandemic drags on, the ECB's former director general of market operations Francesco Papadia told MNI.

Creating a smaller successor to the PEPP, which could be deployed if market conditions deteriorate and bond spreads widen, would be more attractive than expanding the ECB's Asset Purchase Programme, Papadia, who served as director general of market operations at the ECB until 2012 and is a former senior Bank of Italy official, said in an interview. Such a facility would offer flexibility at a time of continued Covid uncertainty, even if waves of infection are likely to be less severe than those seen earlier in the pandemic, and also rising inflation, he said.

"I think that they will rather opt for something closer to the PEPP than the APP, but of course much smaller in size and without commitment. I think this would at least address the need the ECB feels to behave with caution and its wish to keep its hands free," he said, referring to the Governing Council's upcoming December meeting.

Such a new facility would supplement the APP's existing EUR20 billion capacity, he said. MNI has previously cited Eurosystem sources saying the ECB was looking at creating a smaller "sleeper" PEPP, to be used only in an emergency. (See MNI SOURCES: Hawks Emboldened As ECB Nears Crunch December)

HIGH BAR

"I think the most likely outcome is that we have another amount, X, and the ECB will spend it as needed. I am thinking of an envelope that they could spend flexibly as needed in response to market conditions, whether those are a tightening in aggregate financial conditions, or changes in specific markets, like Italy, maybe Spain and Portugal etc."

But the bar for deploying the new tool will be high, he said.

"They will have some sensitivity to spreads, but my sense is that spreads would have to move more than aggregate financial conditions for them to react."

The ECB will be keen to ensure that any new ECB programme – like the current PEPP - continues to support Greece, Papadia said, adding that markets might read negative implications into any decision by the ECB not to do so.

"They would not want to rock the boat for Greece, and not just for Greece, because one could interpret what they could do to Greece as an indication of what they could do in the future to Italy, if there was a serious rating downgrade. They will find a way to keep purchasing Greek bonds."