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Event Update

European Central Bank decides to discontinue PEPP...

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European Central Bank (ECB): The central bank's main objective is to maintain price stability (inflation) in the euro area. This, in turn, helps it support general EU economic policies aiming at full employment and economic growth. To do this the ECB uses various tools like interest rates, targeted longer term refinancing operations (TLTROs), asset purchase programme, etc/

Key Highlights:

- ECB kept its benchmark interest rate unchanged
- The central bank decided to temporarily raise monthly net asset purchases to €40 billion in the second quarter and €30 billion in the third quarter under the APP. From October 2022 onwards, the Governing Council will maintain net asset purchases under the APP at a monthly pace of €20 billion
- The central bank said it would conduct bond purchases under its emergency programme at a "lower pace" than in previous quarter and discontinue net asset purchases under the PEPP at the end of March 2022
- ECB President Lagarde said inflation is expected to remain elevated in the near term but should ease in the course of next year

Interest rates:

- The central bank maintained its main refinancing operations rates at 0.00% (rate at which banks can borrow liquidity from the central bank against collateral on a weekly basis)
- Marginal lending facility rates at 0.25% (rate at which banks can borrow money for overnight from the central bank)
- Deposit facility rate at -0.50% (rate which banks may use to make overnight deposits with the central bank)

Asset Purchase Programme:

- It is a non-standard monetary policy measure. In this the central bank purchases assets including government bonds, securities issued by European supranational institutions, corporate bonds, asset-backed securities and covered bonds
- In this monetary policy, the central bank decided to temporarily raise monthly net asset purchases to €40 billion in the second quarter and €30 billion in the third quarter under the APP. From October 2022 onwards, the bank will maintain net asset purchases under the APP at a monthly pace of €20 billion for as long as necessary to reinforce the accommodative impact of policy rates. ECB expects net purchases to end shortly before it starts raising key ECB interest rates

Pandemic emergency purchase programme (PEPP):

- ECB started this programme in March 2020 to counter the impact of the pandemic on the Euro Area economy. It is a temporary programme, which helps people and firms to get access to affordable funds
- The central bank said it will discontinue conducting net asset purchases with a total span of €1.85 trillion at the end of March 2022. Further, the central bank said it would conduct bond purchases under its emergency program at a “lower pace” than in previous quarter and decided to reinvest the principal payments from maturing securities purchased under the PEPP until at least the end of 2024

Guidance on inflation, economic activity:

- The bank expects key interest rates to remain at their present or lower levels until it sees inflation reaching 2% well ahead of the end of its projection horizon and durably for the rest of the projection horizon
- ECB President Lagarde said economic activity has been moderating over the final quarter of the year. This slower growth is likely to extend into the early part of next year. ECB now expects output to exceed its pre-pandemic level in the first quarter of 2022
- Ms Lagarde said inflation increased further to 4.9% in November and will remain above 2% for most of 2022. Inflation is expected to remain elevated in the near term but decline in the course of next year

Impact on EURUS\$:

EURUS\$ is likely depreciate further till 1.10 on strong dollar and divergence in monetary policy between US Federal Reserve and European Central Bank. US Federal Reserve accelerated the reduction of its monthly bond purchases, opening doors for earlier rate hike whereas, ECB decided to discontinue net asset purchases under PEPP but temporarily raise monthly net asset purchases and promised to hold down borrowing costs next year and keep doors open to restart emergency support if required. Further, the bank said economic activity has been moderating over the final quarter of the year. This slower growth is likely to extend into the early part of next year. Compared with September staff projections, the outlook has been revised down for 2022 and up for 2023. Additionally, investors fear that rising Covid-19 cases and imposition of new restrictions to curb the spread of new Omicron variant would delay in economic recovery.

Inflation v/s Interest rate chart



December 2021 Eurosystem macroeconomic projections

HICP Inflation Projections December 2021

	2021	2022	2023
HICP	2.60	3.20	1.80
Real GDP	5.10	4.20	2.90

September 2021 Eurosystem macroeconomic projections

HICP Inflation Projections September 2021

	2021	2022	2023
HICP	2.20	1.70	1.50
Real GDP	5.00	4.60	2.10



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ANALYST CERTIFICATION

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