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THE EUROPEAN CENTRAL BANK'S QUANTITATIVE EASING PROGRAMME: LIMITS AND RISKS

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Highlights

- The European Central Bank (ECB) has made a number of significant changes to the original guidelines of its quantitative easing (QE) programme since the programme started in January 2015. These changes are welcome because the original guidelines would have rapidly constrained the programme's implementation.

- The changes announced expand the universe of purchasable assets and give some flexibility to the ECB in the execution of its programme. However, this might not be enough to sustain QE throughout 2017, or if the E [illegible]

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EXECUTIVE SUMMARY

- The Eur

- The fear that the ECB will lose its credibility solely because it is currently buying a large amount of sovereign bonds appears to be largely unfounded. The primary risk to the ECB's credibility bcdWZGWG•daXXaü•fT_Ut i

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1. Draghi (2016) hinted at further easing during the press conference following the Governing Council of January 2016.

2. See for instance Baumeister and Benati (2010) or Kapetanios *et al* (2012).

cludes that QE programmes implemented around the world boosted inflation, output and employment.

For the euro area in particular, the effects of QE are even more difficult to pin down given that the programme only started in March 2015. However, there are already some indications that QE is having some impact on the euro-area economy. The effects on the exchange rate and on interest rates (and in particular on financial fragmentation in the euro area, with credit rates converging again) have been the most visible. In terms of inflation, monetary measures take time to materialise in prices and it is very difficult to know what programme was open-ended and that purchases would be conducted until the ECB would see “a sustained adjustment in the path of inflation which is consistent with the aim of achie[illegible] tha

3. A more extensi

7. The assumptions and method used can be found in the annex to Claeys *et al*

Reality will lie between these two extremes.

Figure 3 shows our projections for the monthly purchases, by country, in the scenario in which every debt security contains a CAC. Despite the increase in eligible debt (with the expanded list of agencies, and the new ability to buy regional and local debt), the limits are reached roughlyol a few million euros, while, were the programme to go on until then, they will be worth roughly €1.5 billion per month in March 2019, which is sizeable because it would increase the monthly purchases of German bonds by approximately 10 percent. This effectively means that, while the limits will be reached at roughly the same time as before the rules changed, the balance sheet of the Eurosystem will be bigger at that time thanks to the increase in eligible debt.

Figure 4 shows our projections for the second scenario, in which only central government debt securities issued after 1 January 2013 are assumed to contain CACs. The limits will be reached later than in scenario 1, as can be seen easily by comparing figures 2 and 3. For example, while in scenario 1, purchases in Germany are heavily constrained after April 2017, this is not the case until March 2018 in scenario 2.

On 21 January 2016, President Draghi hinted at further easing, given *"downside risks"* related to heightened uncertainty about the growth prospects of emerging economies, volatility in financial and commodity markets, and geopolitical risks. While this further easing could come in the form of a further reduction in the deposit rate, which would increase the amount of debt eligible for purchase (provided that the yields on these securities do not fall excessively in the meantime), the Governing Council might also decide to increase the amounts purchased each month under the PSPP. The Eurosystem is currently purchasing €44 billion of6OiPZü • _6OnPZü • v/WU_cdcZGWG • v/WUYWccZGWG • 6OoPZü • v/WU_aYcX • v/WU_abGWG • 6OvPü • vü • ve/WU_c

10. Data available at https://www.ecb.europa.eu/paym/coll/charts/html/index.en.html.

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