



ESSENTIALS OF MONETARY POLICY

European Central Bank (ECB) ECB Ends Era of Negative Interest Rates

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ACCORDING TO THE ECB

- ▶ The ECB increased the interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility by 50 basis points to 0.50%, 0.75% and 0.00% respectively.
- ▶ It also approved the Transmission Protection Instrument (TPI), which can be activated to counter unwarranted, disorderly market dynamics that pose a serious threat to the transmission of monetary policy across the euro area. The scale of TPI purchases will depend on the severity of the risks facing policy transmission, and purchases won't be restricted ex ante.
- ▶ The principal payments from maturing securities purchased under the asset purchase programme (APP) and the pandemic emergency purchase programme (PEPP) will be reinvested in full for an extended period of time. Maturing PEPP securities will be reinvested until at least the end of 2024.
- ▶ Flexibly reinvesting PEPP securities will remain the first line of defence against divergent interest rates in the eurozone.

COMMENTS

In June, the ECB signalled it would raise rates by 25 basis points. But with eurozone inflation recently hitting 8.6% and threatening to become entrenched, the ECB had to take more aggressive action. Today's move also ends eight years of negative interest rates. One of the main upside risks to inflation the ECB cited was highly uncertain natural gas supplies.

Fifty-point rate hikes aren't all that unusual these days. Since the beginning of July, the central banks of Australia, New Zealand and Korea have announced their own 50-point increases. But among advanced economies, Canada's central bank has gone the furthest yet, with a 100-basis point hike.

Today's ECB decision also makes sense given the announcement of the TPI, which will be used to limit interest rate spreads in the eurozone. As we understand it, the ECB will be able to use the TPI to purchase bonds from countries experiencing undue market stress. These purchases will be sterilized and won't affect monetary policy. But the ECB will rely first and foremost on flexibly reinvesting its securities to support countries that need it. Italy could soon be one of those countries. Italian bond yields have been rising much faster than German yields, and the current spread is about 225 basis points. The recent resignation of Prime Minister Mario Draghi has only widened the gap.

IMPLICATIONS

We've updated our forecast for future ECB rate hikes based on today's announcement. Additional 50-point hikes seem likely to keep high inflation from becoming entrenched. We now expect the refinancing rate to hit 2.25% in the first quarter of next year. We'll have to wait and see how well the TPI and other ECB tools can contain interest rate spreads in the eurozone. If major financial tensions emerge, the eurozone economy could cool faster than expected, possibly forcing the ECB to scale back monetary tightening.

Schedule 2022 of Central Bank Meetings

Date	Central banks	Decision	Rate
January			
13	Bank of Korea	+25 b.p.	1.25
17	Bank of Japan	s.q.	-0.10
20	Bank of Norway	s.q.	0.50
26	Bank of Canada*	s.q.	0.25
26	Federal Reserve	s.q.	0.25
31	Reserve Bank of Australia	s.q.	0.10
February			
2	Bank of Brazil	+150 b.p.	10.75
3	European Central Bank	s.q.	0.00
3	Bank of England	+25 b.p.	0.50
10	Bank of Sweden	s.q.	0.00
10	Bank of Mexico	+50 b.p.	6.00
22	Reserve Bank of New Zealand	+25 b.p.	1.00
23	Bank of Korea	s.q.	1.25
28	Reserve Bank of Australia	s.q.	0.10
March			
2	Bank of Canada	+25 b.p.	0.50
10	European Central Bank	s.q.	0.00
16	Bank of Brazil	+100 b.p.	11.75
16	Federal Reserve	+25 b.p.	0.50
17	Bank of England	+25 b.p.	0.75
17	Bank of Japan	s.q.	-0.10
24	Bank of Norway	+25 b.p.	0.75
24	Bank of Mexico	+50 b.p.	6.50
24	Swiss National Bank	s.q.	-0.75
April			
5	Reserve Bank of Australia	s.q.	0.10
12	Reserve Bank of New Zealand	+50 b.p.	1.50
13	Bank of Korea	+25 b.p.	1.50
13	Bank of Canada*	+50 b.p.	1.00
14	European Central Bank	s.q.	0.00
27	Bank of Japan	s.q.	-0.10
28	Bank of Sweden	+25 b.p.	0.25
May			
3	Reserve Bank of Australia	+25 b.p.	0.35
4	Bank of Brazil	+100 b.p.	12.75
4	Federal Reserve	+50 b.p.	1.00
5	Bank of England	+25 b.p.	1.00
5	Bank of Norway	s.q.	0.75
12	Bank of Mexico	+50 b.p.	7.00
24	Reserve Bank of New Zealand	+50 b.p.	2.00
25	Bank of Korea	+25 b.p.	1.75
June			
1	Bank of Canada	+50 b.p.	1.50
7	Reserve Bank of Australia	+50 b.p.	0.85
9	European Central Bank	s.q.	0.00
15	Bank of Brazil	+50 b.p.	13.25
15	Federal Reserve	+75 b.p.	1.75
16	Bank of England	+25 b.p.	1.25
16	Bank of Japan	s.q.	-0.10
16	Swiss National Bank	+50 b.p.	-0.25
23	Bank of Norway	+50 b.p.	1.25
23	Bank of Mexico	+75 b.p.	7.75
30	Bank of Sweden	+50 b.p.	0.75

Date	Central banks	Decision	Rate
July			
5	Reserve Bank of Australia	+50 b.p.	1.35
12	Reserve Bank of New Zealand	+50 b.p.	2.50
13	Bank of Korea	+50 b.p.	2.25
13	Bank of Canada*	+100 b.p.	2.50
20	Bank of Japan	s.q.	-0.10
21	European Central Bank	+50 b.p.	0.50
27	Federal Reserve		
August			
2	Reserve Bank of Australia		
3	Bank of Brazil		
4	Bank of England		
11	Bank of Mexico		
16	Reserve Bank of New Zealand		
18	Bank of Norway		
24	Bank of Korea		
September			
6	Reserve Bank of Australia		
7	Bank of Canada		
8	European Central Bank		
15	Bank of England		
20	Bank of Sweden		
21	Bank of Brazil		
21	Bank of Japan		
21	Federal Reserve		
22	Bank of Norway		
22	Swiss National Bank		
29	Bank of Mexico		
October			
3	Reserve Bank of Australia		
4	Reserve Bank of New Zealand		
13	Bank of Korea		
26	Bank of Brazil		
26	Bank of Canada*		
27	European Central Bank		
27	Bank of Japan		
31	Reserve Bank of Australia		
November			
2	Federal Reserve		
3	Bank of England		
3	Bank of Norway		
10	Bank of Mexico		
22	Reserve Bank of New Zealand		
23	Bank of Korea		
24	Bank of Sweden		
December			
5	Reserve Bank of Australia		
7	Bank of Brazil		
7	Bank of Canada		
14	Federal Reserve		
15	European Central Bank		
15	Bank of England		
15	Bank of Norway		
15	Bank of Mexico		
15	Swiss National Bank		
19	Bank of Japan		

NOTE: Certain banks may decide to change rates in-between the scheduled meetings. The abbreviations s.q. and b.p. correspond to status quo and basis points respectively. * Monetary Policy Report published.