Central Banks

The direction is clear: more cuts to come

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- **ECB cuts rates by 25bps (depo rate to 2.75%), reinforcing the easing cycle**
- **Rates remain in restrictive territory, neutral rate discussion remains premature**
- **The macroeconomic outlook and the balance of risks remain unchanged**

As widely expected, **the ECB cut key interest rates by 25 basis points** today, marking the fourth consecutive reduction and the fifth since the current easing cycle began in June 2024. The deposit rate was lowered to 2.75%, while the rates for the main refinancing operations and the marginal lending facility were reduced to 2.90% and 3.15%, respectively. President Lagarde said that **the decision was unanimous**.

On the next steps to take, Lagarde emphasized that **the ECB remains on a clear downward path, but the pace and sequence of rate cuts will be determined by incoming data and decided on a meeting-by-meeting basis, as in previous meetings.** She ruled out providing firm forward guidance, stating that it would be "totally unrealistic" given the current high and potentially rising uncertainty. She reiterated that decisions will continue to be guided by three key factors: the inflation outlook, underlying inflation, and the transmission of monetary policy.

During the Q&A session, several questions were raised about the neutral rate. Lagarde said that the **ECB remains in restrictive territory and has not yet reached the neutral rate, calling any debate on the matter "entirely premature.**" She explained that once the ECB approaches that level, it will rely on staff research and analysis to assess how close it is and what monetary policy decisions should follow. At the December meeting, she indicated that the neutral rate was estimated to be between 1.75% and 2.5%, while recently at the WEF in Davos she suggested a slightly lower range of 1.75% to 2.25%—a mildly dovish signal. However, today she stressed that these are ECB staff projections, set to be published on February 7. She also emphasized that it is a conceptual benchmark derived from multiple models rather than a fixed policy guideline.

Regarding the macro outlook, ECB President Christine Lagarde stated that the **central bank's macroeconomic outlook remains largely unchanged from the December meeting.** On growth, **the euro area stagnated in Q4,** as confirmed by today's weaker-than-expected data from France and Germany, but **the ECB emphasized that the fundamentals for a gradual recovery remain in place. On inflation, Lagarde reaffirmed that the disinflation process is progressing as expected**, with the ECB confident that the 2% target will be reached this year and maintained sustainably. While wage growth remains elevated, it is moderating in line with expectations, with a normal lag. Additionally, corporate profits continue to absorb part of the impact, helping to contain inflationary pressures. The ECB's risk assessment on growth and inflation remains unchanged.

Regarding the question of whether Bitcoin could be included in the ECB's reserves, Lagarde firmly ruled out this possibility. She emphasized that euro area reserves must be liquid, secure, and free from risks related to money laundering or criminal activities. According to Lagarde, there is broad consensus within the Governing Council—and likely the General Council as well—that Bitcoin does not meet these criteria. She also stated that it is highly improbable that any EU country would choose to add Bitcoin to its monetary reserves.

Overall, **the ECB adopted a relatively dovish stance** today while implementing the widely expected rate cut, **signaling the possibility of further reductions without committing to a specific terminal level**. This approach aligns with the continued progress in disinflation and the subdued momentum of the Eurozone economy. Following the meeting, we maintain our expectation of three additional rate cuts in the first half of 2025, bringing the deposit rate down to 2%.

PLEASE NOTE: **TRACKING CHANGES IN FOLLOWING STATEMENTS**

in black, wording common to both the current and previous statements, in light grey and crossed, previous wording that was replaced by new wording, in blue and underlined (YES, TRACK CHANGES ARE THERE ON PURPOSE).

1.1. Christine Lagarde, President of the ECB, Luis de Guindos, Vice-President of the ECB

Frankfurt am Main, ~~12 December 2024~~30 January 2025

Good afternoon, the Vice-President and I welcome you to our press conference.

The Governing Council today decided to lower the three key ECB interest rates by 25 basis points. In particular, the decision to lower the deposit facility rate – the rate through which we steer the monetary policy stance – is based on our updated assessment of the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission.

The disinflation process is well on track. ~~Staff see headline inflation averaging 2.4 per cent~~Inflation has continued to develop broadly in ~~2024, 2.1 per cent in 2025, 1.9 per cent in 2026 and 2.1 per cent in 2027 when~~line with the ~~expanded EU Emissions Trading System becomes operational. For inflation excluding energy and food,~~ staff ~~project an average~~projections and is set to return to our two per cent medium-term target in the course of ~~2.9 per cent in 2024, 2.3 per cent in 2025 and 1.9 per cent in both 2026 and 2027.~~

this year. Most measures of underlying inflation suggest that inflation will settle at around our ~~two per cent medium-term~~ target on a sustained basis. Domestic inflation ~~has edged down but~~ remains high, mostly because wages and prices in certain sectors are still adjusting to the past inflation surge with a substantial delay. But wage growth is moderating as expected, and profits are partially buffering the impact on inflation.

~~Financing conditions are easing, as our~~Our recent interest rate cuts are gradually ~~make~~making new borrowing less expensive for firms and households. ~~But they~~ At the same time, financing conditions continue to tight, also because our monetary policy remains restrictive and past interest rate hikes are still transmitting to the ~~outstanding~~ stock of credit~~.~~

~~Staff now expect a slower economic recovery than in the September projections. Although growth picked up in the third quarter of this year, survey indicators suggest it has slowed in the current quarter. Staff see the~~ , with some maturing loans being rolled over at higher rates. The economy ~~growing by 0.7 per cent in 2024, 1.1 per cent in 2025, 1.4 per cent in 2026 and 1.3 per cent in 2027. The projected recovery rests mainly on~~is still facing headwinds but rising real incomes ~~– which should allow households to consume more – and firms increasing investment. Over time,~~and the gradually fading effects of restrictive monetary policy should support a pick-up in ~~domestic~~ demand over time.

We are determined to ensure that inflation stabilises sustainably at our two per cent medium-term target. We will follow a data-dependent and meeting-by-meeting approach to determining the appropriate monetary policy stance. In particular, our interest rate decisions will be based on our assessment of the inflation outlook in light of the incoming economic and financial data, the dynamics of underlying inflation and the strength of monetary policy transmission. We are not pre-committing to a particular rate path.

The decisions taken today are set out in a ~~press release~~press release available on our website.
I will now outline in more detail how we see the economy and inflation developing and will then explain our assessment of financial and monetary conditions.

1.2. Economic activity

The economy ~~grew by 0.4 per cent~~stagnated in the ~~third~~fourth quarter, ~~exceeding expectations. Growth was driven mainly by an increase in consumption, partly reflecting one-off factors that boosted tourism over the summer, and by firms building up inventories. But the latest information suggests it~~ according to Eurostat's preliminary flash estimate. It is ~~losing momentum.~~set to remain weak in the near term. Surveys indicate that manufacturing ~~is still contracting and growth in~~ continues to contract while services activity is expanding. Consumer confidence is ~~slowing. Firms are holding back~~ fragile, and households have not yet drawn sufficient encouragement from rising real incomes to significantly increase their ~~investment~~ spending ~~in~~.

Nevertheless, the conditions for a recovery remain in place. While the ~~face of weak demand and a highly uncertain outlook. Exports are also weak, with some European industries finding it challenging to remain competitive.~~

~~The~~ labour market ~~remains resilient. Employment grew by 0.2 per cent in~~ has softened over recent months it continues to be robust, with the ~~third quarter, again by more than expected. The~~ unemployment rate ~~remained at its historical~~staying low ~~of~~, at 6.3 per cent in ~~October. Meanwhile, demand for labour continues to weaken. The~~December. A solid job ~~vacancy rate declined to 2.5% in the third quarter, 0.8 percentage points below its peak, and surveys also point to fewer jobs being created in the current quarter.~~

~~The economy~~market and higher incomes should strengthen ~~over time, although more slowly than previously expected. The rise in real wages should strengthen household~~consumer confidence and allow spending to rise. More affordable credit should also boost consumption and investment over time. Provided trade tensions do not escalate, exports should support the recovery as global demand rises.

Fiscal and structural policies should make the economy more productive, competitive and resilient. We welcome the European Commission's Competitiveness Compass, which provides a concrete roadmap for action. It is crucial to ~~swiftly~~ follow up, with further concrete and ambitious structural policies, on Mario Draghi's proposals for enhancing European competitiveness and on Enrico Letta's proposals for empowering the Single Market. ~~We welcome the European Commission's assessment of governments' medium-term plans for fiscal and structural policies, as part of the EU's revised economic governance framework.~~ Governments should ~~now focus on implementing~~implement their commitments under ~~this~~the EU's economic governance framework fully and without delay. This will help bring down budget deficits and debt ratios on a sustained basis, while prioritising growth-enhancing reforms and investment.

1.3. Inflation

Annual inflation increased to 2.~~3~~4 per cent in December, up from 2.2 per cent in November~~ according to Eurostat's flash estimate, from 2.0 per cent in October. The ~~. As in the previous two months, the increase was expected and primarily reflected ~~an ~~past sharp drops in energy~~-related upward base effect.~~ prices falling out of the calculation. Along with a month-on-month increase in December, this led energy prices slightly higher on an annual basis, after four consecutive declines. Food price inflation edged down to 2.~~8~~6 per cent and ~~services~~goods inflation to ~~3.9~~0.5 per cent. ~~Goods~~Services inflation ~~went~~edged up to 4.0~~.7~~ per cent.

Most underlying inflation indicators have been developing in line with a sustained return of inflation to our medium-term target. Domestic inflation, which closely tracks services inflation, ~~again eased somewhat in October. But at 4.2%, it remains~~has remained high~~. This reflects strong wage pressures and the fact that ~~, as wages and some services prices are still adjusting ~~with a delay ~~to the past inflation surge~~. That said, underlying inflation is overall developing in line~~ with a ~~sustained return of inflation to target.~~

~~The increase in compensation per employee moderated to 4.4 per cent in~~substantial delay. At the ~~third quarter from 4.7 per cent in the second. Amid stable productivity, this contributed to slower growth in unit labour costs. Staff expect labour costs to increase more slowly over the projection horizon as a result of lower ~~same time, recent signals point to continued moderation in wage ~~growth~~pressures and ~~higher productivity growth. Moreover, ~~to the buffering role of profits~~ should continue to partially offset the effects of higher labour costs on prices, especially in the near term~~.

We expect inflation to fluctuate around its current level in the near term~~, as previous sharp falls in energy prices continue to drop out of the annual rates.~~. It should then settle sustainably at around the two per cent medium-term target. Easing labour cost pressures and the continuing impact of our past monetary policy tightening on consumer prices should help this process. ~~Most~~While market-based indicators of inflation compensation have largely reversed the declines observed in the autumn, most measures of longer-term inflation expectations continue to stand at around 2 per cent~~, and market-based indicators of medium to longer-term inflation compensation have decreased measurably since the Governing Council's October meeting~~.

1.4. Risk assessment

The risks to economic growth remain tilted to the downside. ~~The risk of greater~~Greater friction in global trade could weigh on euro area growth by dampening exports and weakening the global economy. Lower confidence could prevent consumption and investment from recovering as fast as expected. This could be amplified by geopolitical risks, such as Russia's unjustified war against Ukraine and the tragic conflict in the Middle East, which could disrupt energy supplies and further weigh on global trade. Growth could also be lower if the lagged effects of monetary policy tightening last longer than expected. It could be higher if easier financing conditions and falling inflation allow domestic consumption and investment to rebound faster.

Inflation could turn out higher if wages or profits increase by more than expected. Upside risks to inflation also stem from the heightened geopolitical tensions, which could push energy prices and freight costs higher in the near term and disrupt global trade. Moreover, extreme weather events, and the unfolding climate crisis more broadly, could drive up food prices by more than expected. By contrast, inflation may surprise on the downside if low confidence and concerns about geopolitical events prevent consumption and investment from recovering as fast as expected, if monetary policy dampens demand by more than expected, or if the economic environment in the rest of the world worsens unexpectedly. Greater friction in global trade would make the euro area inflation outlook more uncertain.

1.5. Financial and monetary conditions

Market interest rates in the euro area have ~~declined further~~risen since our ~~October~~December meeting, ~~reflecting the perceived worsening of the economic outlook. Although~~partly mirroring higher rates in global financial markets. While financing conditions remain ~~restrictive~~tight, our interest rate cuts are gradually making it less expensive for firms and households to borrow.

The average interest rate on new loans to firms ~~was~~declined to 4.~~7~~5 per cent in ~~October, more than half a percentage point below its peak a year earlier. The~~ November, while the cost of issuing market-based debt ~~has fallen by more than a percentage point since its peak.~~remained at 3.6 per cent. The average rate on new mortgages~~, at~~ edged down to 3.~~6~~5 per cent.

Growth in ~~October, is about half a percentage point lower than at its highest point in 2023, even though the average rate on the outstanding stock of mortgages is still set to rise.~~

~~Bank~~bank lending to firms ~~has gradually picked up from low levels, and increased by~~ rose to 1.~~2~~5 per cent in ~~October compared with~~December, up from 1.0 per cent in November, amid a ~~year earlier. Debt~~strong monthly flow. Growth in debt securities issued by firms ~~were up~~moderated to 3.~~1%~~2 per cent in annual terms~~, which was similar to the increase in the previous few months.~~. Mortgage lending continued to rise gradually ~~in October~~but remained muted overall, with an annual growth rate of ~~0.8~~1.1 per cent.

~~In line with our monetary policy strategy, the Governing Council thoroughly assessed the links between monetary policy and financial stability. Euro area banks remain resilient and there are few signs of financial market stress. Financial stability risks nonetheless remain elevated. Macroprudential policy remains the first line of defence against the build-up of financial vulnerabilities, enhancing resilience and preserving macroprudential space.~~

Credit standards for business loans tightened again in the fourth quarter of 2024, having broadly stabilised over the previous four quarters, as reported in our latest bank lending survey. The renewed tightening mainly reflected banks becoming more concerned about the risks faced by their customers and less willing to take on risks themselves. Demand for loans by firms increased slightly in the fourth quarter but remained weak overall. Credit standards for mortgages were broadly unchanged, after three quarters of easing, while the demand for mortgages again increased strongly, mainly because of more attractive interest rates.

1.6. Conclusion

The Governing Council today decided to lower the three key ECB interest rates by 25 basis points. In particular, the decision to lower the deposit facility rate – the rate through which we steer the monetary policy stance – is based on our updated assessment of the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission. We are determined to ensure that inflation stabilises sustainably at our two per cent medium-term target. We will follow a data-dependent and meeting-by-meeting approach to determining the appropriate monetary policy stance. In particular, our interest rate decisions will be based on our assessment of the inflation outlook in light of the incoming economic and financial data, the dynamics of underlying inflation and the strength of monetary policy transmission. We are not pre-committing to a particular rate path.

In any case, we stand ready to adjust all of our instruments within our mandate to ensure that inflation stabilises sustainably at our medium-term target and to preserve the smooth functioning of monetary policy transmission.

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