

# Monetary Measures by European Central Bank under Covid Periods

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## ABSTRACT

To run the euro-region economy easily (saving from the awful impacts of crown), the European Central Bank (ECB) has reported countless measures since the start of the COVID-19 emergency. This reaction has set off apprehensions of a future expansion in swelling. We presume that the measures presented by the ECB during the emergency and the subsequent expansion in the size of its asset report, regardless of whether it were to be lasting, may prompt inflation. Central banks have found a way to keep their economies above water during the COVID-19 lockdowns. In the euro region, the European Central Bank (ECB) has facilitated essentially the states of its renegotiating activities and has reported another resource buy program to guarantee that its financial approach keeps on being very much communicated to all nations of the money related association. The European Central Bank worked by making cash and proficiently supplanting the credit framework by subbing cash for credit which may get terrible impacts the since quite a while ago run.

**Keywords--** COVID-19, ECB, Monetary Policy, Lockdown, Money Supply, Deflation, Inflation

bad socio-economic impacts. It is expected that the European Union will contract by 7.5 per cent in 2020 and grow by around 6 per cent in 2021.

World Economic Outlook projects global growth in 2020 to fall to 3 per cent. This is a downgrade of 6.3 per cent percentage points from January 2020, a major revision over a very short period. This makes the Great Lockdown the worst recession since the Great Depression, and far worse than the Global Financial crisis (IMF blog). COVID-19 is a different type of crisis, different from the Great Depression and the 1970s stagflation. Workers have left their jobs without even thinking about their future financial conditions. Reverse migration has taken place in crores of numbers, national as well as international as it is still not known when the world will be free from this virus. Also, the 2008 crisis was a financial crisis, but this Pandemic has affected the income of the people, while the 2008 crisis brought a big drop in credit. There is no economic policy, the tools of which can be used to control the prevailing abnormality.

## II. COVID-19 AND ECB

### I. INTRODUCTION

COVID-19, which has become a household name now, had its origin in Wuhan in China, and then travelled to Europe, the USA, and Asian countries. In the beginning, the people of Europe did not take it seriously, but later on, sensing its horrendousness, governments and Central Banks of these countries started taking actions to flatten the upward curve of the virus.

Various lockdowns across the world restricted millions of citizens to their homes, shutting down their businesses and put a stop to almost all economic activities, leading to the most severe economic contraction since the Great Depression of the 1930s, and Global Financial crisis of 2008. Incomes of all categories of the economy whether it's a household, corporation, financial, non-financial, and government and the asset markets took a large share of the hit. Although the government and Central Bank of all affected countries have responded to this crisis by bringing alternation and taking steps under fiscal and monetary policies which are unprecedented in size and scope, this pandemic has come as a shock for the EU economies with

When COVID-19 started, most of the countries went for lockdown in their respective countries, restricted the mobility of the people. The Economies were almost shut down. Income has fallen due to the shutdown of businesses. Fall in income has affected the spending capacity of the populace. It creates a spiral as when income falls, consumption falls, and when consumption falls, income falls; one man's spending becomes another's income. When consumption falls, or if consumption is restricted to very essential items, production activities are also shut down partly due to lockdown and restricted mobility.

Over the entire global economy, going company by company, the total hit to revenue is about \$27 Trillion and about \$7 Trillion to profits. (Stagflation: How it occurs and building a 'Stagflation Portfolio, July 10, 2020, "Day Trading.com"). When the government shuts down its economy, under such conditions it has to ensure its people that the government will take all such economic and reformative actions to fulfill their needs. These reformative activities will help the country to come out of this bad phase due to the pandemic. For this, policymakers are

providing unprecedented support to households, firms, and financial markets, including credit guarantees, liquidity facilities, loan forbearance, enhanced benefits, and relief in taxes. However, it was fairly straightforward for the Central Bank to come forward and handle the situation. Being the lender for the last resort, a Central Bank can fix the situation by backstopping credit. COVID-19 shuts down businesses, hits earnings and jobs, and had knocked on effects in the Global Credit.

During the COVID-19 period, the Central Banks of almost all the countries have pushed a lot of liquidity either through the selling of bonds or providing loans at easy terms into the market. It has brought up the financial economy by raising the prices of financial assets at the cost of the real economy. It is a nominal growth which is made up of real growth and inflation.

In the euro areas, the European Central Bank (ECB) has eased significantly the conditions of its refinancing operations and has announced a new asset purchase programme to ensure that benefits its monetary policy are well transmitted to all countries of the monetary union. This response has triggered fears of a significant increase in inflation, and concerns about whether the ECB measures are compatible with its price stability mandate and with the limits set by the EU Treaty.

Europe has a central bank, European Central Bank (ECB) which is quite a bit smaller than the US Federal Reserve. The ECB's and the Euro system's primary objective is spelled out in the EU treaty. The ECB's Governing Council intends to maintain price stability and inflation below but close to 2 per cent over the medium terms. Although, it is difficult to predict what will happen, how this virus is further going to affect the different aspects of human beings, (because of the high uncertainty and the exceptional nature of the current shock), yet there might be the risk that the Eurozone may experience in the coming years. The ECB's forecasts (Battistini and Stoevsky, 2020) predict that even in their more optimistic scenario, the output is not going to reach its pre-crisis trend before the end of 2022.

Since the beginning of the COVID-19, ECB has been very actively announcing a large number of measures, such as launching of a new temporary asset purchase program of securities issued by private and public sectors to meet the problems posed by the outbreak and escalating diffusion of COVID-19. The ECB's Governing Council announced on Wednesday, 18 March 2020, a new Pandemic Emergency Purchase Program (PEPP) with an envelope of €750 billion until the end of the year, in addition to the €120 billion decided on 12 March. Together this amounts to 7.3 per cent of euro area GDP. (Report by KPMG, "European Central Bank (ECB), 20/05/2020) A temporary programme was designed to address the unprecedented situation which the monetary

union was facing. It was made available to all jurisdictions. It aims to support the liquidity and the financial condition of all sectors of the Euro Zone economy. ([https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr.200318\\_1~3949d6f266.en.html](https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr.200318_1~3949d6f266.en.html)) It will remain in place until ECB assesses that the coronavirus crisis phase is over. PEPP will be terminated once the governing Council judges that the COVID-19 crisis phase is over. (The European Central Bank in the COVID-19 crisis: Whatever it takes, within its mandate By Gregory Claeys).

The main aim of this program by ECB is to provide relief to banks so that they can increase loans to businesses and SMEs to support production as well as employment. The Monetary program undertaken by ECB depicts similar concern to those motivating the Fed, which slashed short-term interest rates to near zero. It also includes the purchase of \$500 billion in T-bills and \$200 billion in mortgage-backed securities so that the credit market keeps on functioning. Under the pandemic support program, the ECB buys corporate and government bonds and other financial assets from banks and pay them newly created money. This lowers down the longer-term interest rates; and thereby banks keep funding the borrowers. (MINT, "European Central Bank nearly doubles COVID19 Pandemic support Scheme)

In March, it provided liquidity through eased conditions on its targeted longer-term refinancing operations (TLTRO). Also, it announced that ECB was ready to provide US Dollars to the Banks located in the euro area. The rate at which the ECB lends to banks is zero. Its rate on deposits left overnight by commercial banks is now minus 0.5 per cent, so that banks do not leave their deposits with the central bank but rather lend it to corporate and others to increase the money supply in the economy. The bank has also offered long term credits to banks at even lower rates if they show they are further lending to companies.

The bank is siphoning 1.35 Trillion Euros (\$1.6 trillion) in recently printed cash into the economy through acquisition of government and corporate securities, on top of 20 billion euro in month to month security buys from an upgrade exertion dispatched before the flare-up. This new improvement goes ahead top of added spending by European governments and comparative boost endeavors by the U.S. Central bank, the Bank of England, the Bank of Japan, and other national banks around the planet as the world attempts to adapt to a sharp, synchronous hit to both creating and rich economies. (Viewpoint, THE NEWSCROLL, "European Central Bank keeps improvement approaches on hold", 10/09/2020) (Money Control, "European Central Bank almost pairs Covid pandemic help plot" 04/06/2020), (The Economic Times, "European Central Bank gives out 1.3 trillion Euros in credits", 18/06/2020).

Further, in June 2020, with the aim of supporting funding conditions in the real economy, especially for businesses and households, the Governing Council of ECB, decided to increase the envelop for the PEPP by 600 EUROs and thereby taking the total amount to 1350 Billion EUROs. The time for net purchases under PEPP will be extended to the end of June 2021 or till coronavirus is over. And of course, the net purchases under Asset Purchase Programme (APP) will remain at the same monthly pace of 20 Billion EUROs, along with the additional purchases of 120 billion EUROs temporary envelop till the end of the 2020. (The ECB's (APP) which was initiated in mid-2014, is a part of non-standard monetary policy which includes targeted longer-term refinancing operations).

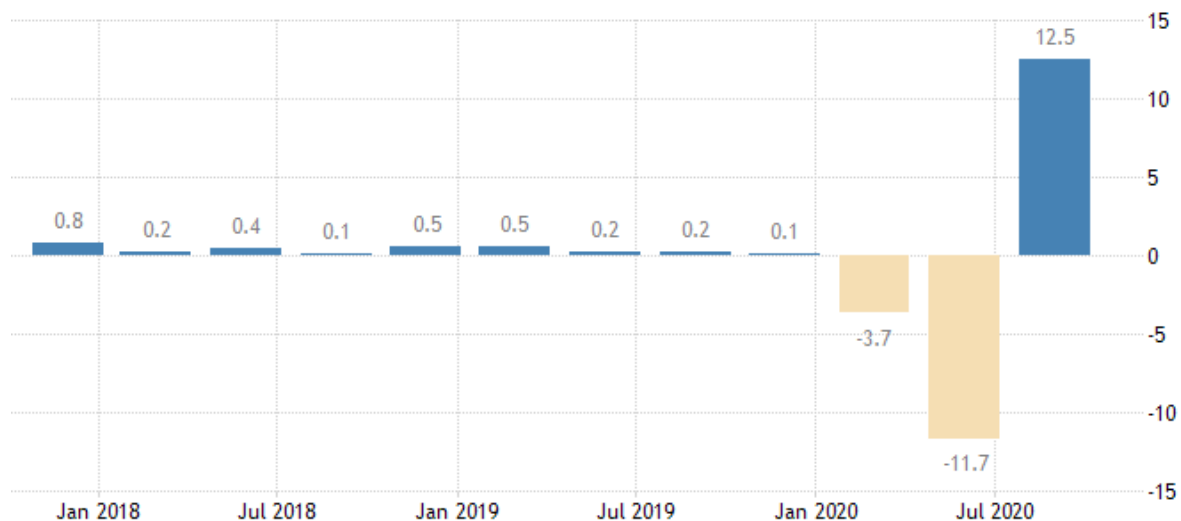
It will not affect the interest rate on the main refinancing operations and on the marginal lending facility including the deposit facility at 0.00%, 0.25% and -0.50% respectively. (-0.5 % , a negative rate penalty on deposits which are left overnight by commercial banks as an incentive to lend the money rather than getting piled up at the Central Bank).

On 10<sup>th</sup> December 2020, the biggest announcement was made by ECB on its Monetary Policy, was to boost its PEPP by an unexpectedly large amount of 500 Billion EUROs, thereby making the total amount to 1,850 Trillion EUROs. The objective was to keep affordable credit flowing to the economy during the steep downturn caused by the virus outbreak. It also extended the time limit for the net purchases at least the end of March 2022.

To support the flow of credit to all sectors and underpinning economic activity to maintain price stability, ECB also announced some more liquidity infusion measures and extended the time limit of other programs so that financing takes place in a favorable conditions over the pandemic period,

Such historic stimulus steps adopted by ECB through its Monetary Policy not only strengthen the European Economy but also led to growth of the Euro Zone Economy by 12.5 percent in three months to September 2020, recovering a record slump of 11.7 percent in the previous quarter and compared with a second estimate of a 12.6 percent advance.

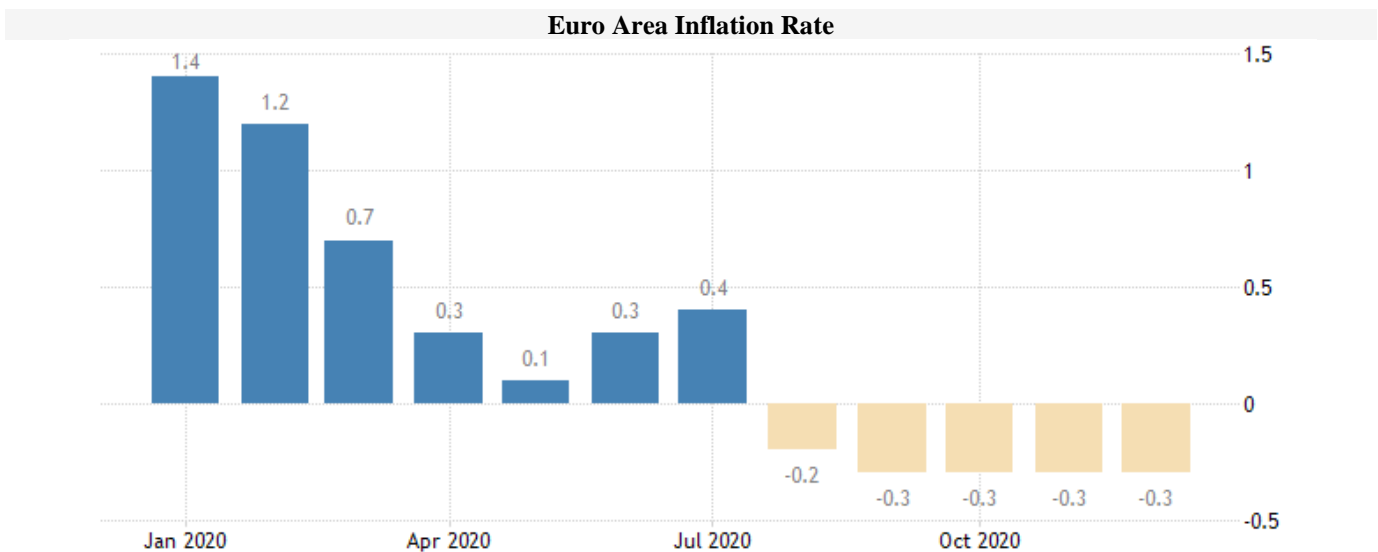
**Euro Area GDP Growth Rate**



**Source:** Tradingeconomics.com / World Bank

Besides above, there was a steep drop in inflation. According to "The European Economy Union's Euro Stat Data Agency", the inflation rate measured by the Harmonized index of consumer prices (HICP) came down to -0.2 percent in August 2020, and (-0.3% in each of the

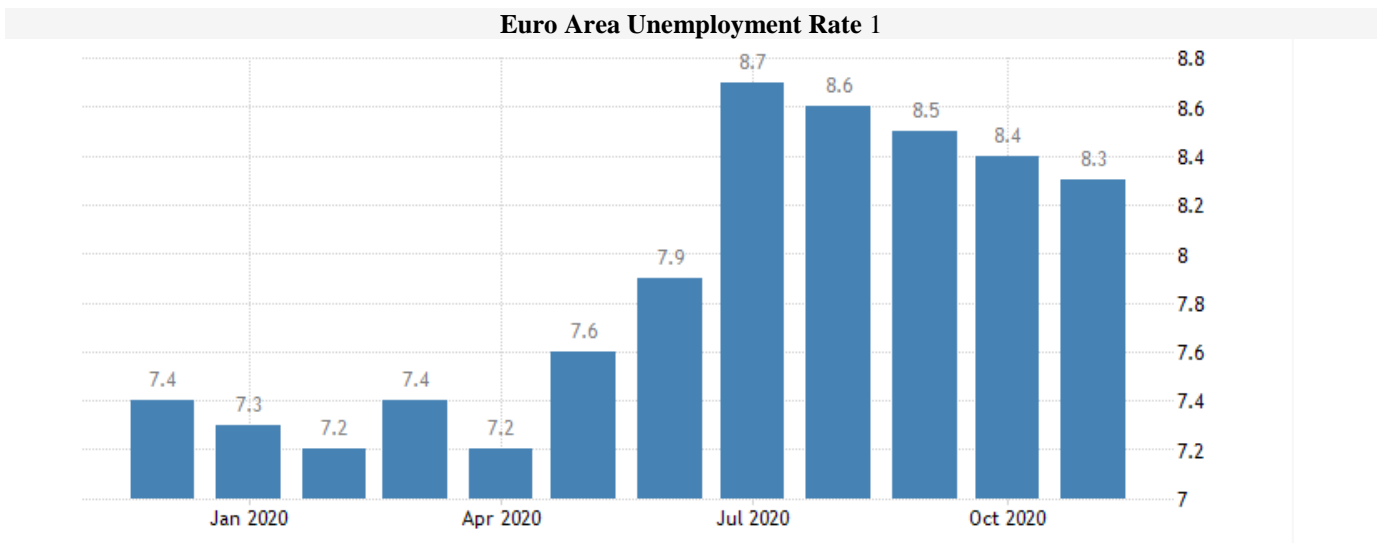
last 4 months till December 2020, i.e the price level had gone down into a steep descent. (Inflation fell to -0.3 percent in December 2020). Thereby inflation remained below the European Central Bank's target rate of near, but under 2%.



**Source:** Tradingeconomics.Com: Eurostat

Even at such a low inflation rate, The European Central Bank has decided to keep its stimulus policies unchanged on September 10, with almost a trillion Euros (dollars) still in the pipeline to bolster the eurozone economy's rebound from the severe coronavirus recession.

The European government has made big economic efforts at the national level, paying companies to keep workers on and extending loans. This has kept unemployment in the eurozone at 8.3 per cent, moving further away from an 8.7 percent in July of this year.



**Source:** Tradingeconomic.com | EURO STAT

European governments have made big economic efforts at the national level, paying companies to keep workers on and extending loans. That has kept unemployment in the euro zone down at 8.3 per cent, though the rate is likely to rise after those programs expire. Moreover, the reverse migrant when comes back to join back their jobs may also lead to an increase in unemployment. And to compensate for their losses,

corporate may not be in a position to hire more people. Under such a situation, the unemployment rate may increase further in the country. That has kept unemployment in the euro zone down at 8.3 per cent; though the rate is likely to rise after those programmes expire.

### III. REFORMS AND INFLATION

The ECB's major increase in the monetary base (similarly to other major central banks around the world) has raised fears about the acceleration of inflation in the future. In the euro-area, the European Central Bank (ECB) has eased significantly the conditions of its refinancing operations and has announced a new asset purchase programme. This response has triggered fears of a significant increase in inflation, and concerns about whether the ECB measures are compatible with its price stability mandate and with the limits set by the EU Treaties.

Annual inflation is projected at 0.2% in 2020, 1% in 2021, 1.1% in 2022 and 1.4% in 2023.

On the one hand, a drop off in consumer demand would serve to keep prices low, but at the same time, shutting down of business/ reducing scale of production and disruption of trade could limit supply, putting upward pressure on prices.

Initially, the pandemic took the form of a supply shock, as domestically and globally, the supply chain got disturbed because of small manufacturers shutting their businesses. In India, the trucks were not able to supply in time as whenever their vehicle even needs a tire puncturing service, they were not able to find a tire repairing shop on the road. Their effects have now generated a massive aggregate supply shock. At the same time, the corporate investments will be probably trend lower due to lockdown, reverse migration, and a large increase in corporate debt during lockdown and fall in aggregate demand. "Manufacturing is currently being buoyed by a wave of pent-up demand, but capacity is being scaled back," said HIS Markit's Chris Williamson. Households' demand, he major consumer of goods and services, will probably subside due to precautionary savings and unemployment and loss of jobs. A drop off in consumer demand due to lockdown and disruption to trade could limit supply, putting upward pressure on prices.

During the lockdown, people have curtailed their consumption because of two factors. First, a reduction in Income. Some of them have lost their job completely and some are working at half of their pay during the lockdown period. Secondly, their demand was restricted to food and other very essential goods. Demand for luxury, entertainment had become completely zero. Now, since the money supply got increased (Due to measures taken by ECB, people have started increasing their demand), it may lead to increase in Demand.

The most intuitive argument brought forward against having a large balance sheet is the classical monetarist argument. Since, ECB's measures have made its Balance-Sheet, a healthy one, by almost Euro 700 Billions in only 2 Months; it may lead to too much credit

and inflation in the economy, in the long run. A high level of central bank liquidity could result in rapid credit creation by the banking sector and ultimately in an acceleration of inflation above target, which would endanger the price-stability mandate of the ECB.

However accelerating inflation may not be an immediate threat, as the euro area had experienced in 2020, its deepest recession period ever recorded in 2020. HICP estimates for March and April 2020 already point towards a decrease in overall inflation in the EURO area. Price growth in the Euro zone slid to 0.1 per cent year on year in May, due to a sharp drop in energy prices. The cost of food in the Euro Area increased by 1.20 per cent in August of 2020 over the same month in the previous year. (Euro Area Food Inflation, Trading Economics).

Buyer costs in the Euro Area dropped 0.3 percent from a year sooner in December 2020, a fifth back to back month of decrease. In any case, this drop was because of a descending pressing factor coming from energy (- 6.9 percent versus - 8.3 percent in November) and non-energy modern products (- 0.5 percent versus - 0.3 percent). Simultaneously, food, liquor and tobacco swelling eased back to 1.3 percent from 1.9 percent, while cost for administrations rose 0.7 percent, and contrasted and 0.6 percent in November. The yearly center swelling, which avoids unpredictable costs of energy, food, liquor and tobacco and at which the ECB glances in its approach choices, was unaltered at 0.2 percent in December, the least on record. (EUROSTAT). source: EUROSTAT. In any case, second-round impacts have now created a huge total interest stun. Besides, supply won't increment in a similar extent. As such it might prompt a value ascend in the economy, however gradually once life gets typical.

The general effect on costs will rely upon which of these two stuns overwhelms. Going into the post-Covid-19 contributing period, we will be in a circumstance where the national bank has driven a great deal of liquidity into the business sectors and raised the monetary economy (i.e., costs of monetary resources) while the genuine economy (i.e., total exchanges volume in merchandise and ventures) stays feeble.

### IV. CONCLUSION

Fiscal and monetary policy stimulus "in and of itself has a very, very important inflationary dynamic to it," said Jeffrey Rosenberg, a portfolio manager of Black Rock's Systematic Multi-Strategy Fund. He sees inflation as a risk starting in about six months, and one that's will be marked by a steepening curve. "The Covid crisis is first and foremost a massive, massive supply shock" which then "had morphed into a massive, massive demand shock," he said. Forward inflation swap rates in the U.S. and the euro-zone, favored by policymakers for long-run inflation



expectations, have also rebounded yet remain below long-term averages.

Easing significantly the conditions of refinancing operations and purchase of new assets by ECB is not a short-term scenario, but that's the scary long term one. The result would be equities remaining on the front foot initially as the economy reflates, then heading lower, bond prices falling, commodities rising. Growth may take place, but inflation can also take place due to the clogging of the global supply chain.

Fiscal policymakers across the world tried to step in to fill in that income and spending gap by getting cash to households, credit, and liquidity support programs to corporations. Many households and corporations had holes blown in their balance sheets and that will be difficult to correct going forward. Households and corporations were in financial crisis as they had lost income but still have a fixed expense base to varying extents. Tapping savings (usually in the form of financial assets) is the easiest way to immediately fill that gap. The question remains whether the measures taken by ECB are enough? Will these measures be able to bring back the same position which was prior to COVID-19?

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