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COMMITTEE ON ECONOMIC AND MONETARY AFFAIRS**MONETARY DIALOGUE WITH CHRISTINE LAGARDE,
PRESIDENT OF THE EUROPEAN CENTRAL BANK
(pursuant to Article 284(3) TFEU)****BRUSSELS,
MONDAY, 27 NOVEMBER 2023**

1-002-0000

IN THE CHAIR: IRENE TINAGLI
*Chair of the Committee on Economic and Monetary Affairs**(The Monetary Dialogue opened at 15.10.)*

1-003-0000

Chair. – Good afternoon, everyone. So let's get started with our committee meeting. As usual, we start with the adoption of the agenda. If there are no objections, the agenda is adopted. We also have to approve the minutes of the meetings of 23 and 24 October 2023 and of 7 November 2023. If there are no objections, they are considered approved.

I take the liberty of postponing all the announcements to tomorrow morning so we can jump to the core of our meeting today, which is the monetary dialogue with Christine Lagarde, the President of the European Central Bank. So, welcome, President Lagarde.

This is the fourth and last monetary dialogue in 2023. The previous one took place on 25 September. Today, the dialogue is taking place in a still challenging environment, which is marked by uncertainty. Since the last monetary dialogue in September, headline inflation in the euro area declined markedly to 2.9 % in October, down from 4.3 % in September. This is the lowest level since July 2021, and at the same time, core inflation has been high and persistent, exceeding 5 % throughout the year, but now also showing a downward trend at 4.5 % in September and 4.2 % in October.

So, after ten consecutive rate hikes in a row, the ECB Governing Council left interest rates unchanged in its last meeting on 26 October. The ECB has raised interest rates by a cumulative 450 basis points between July last year and now, making it the most aggressive monetary policy tightening since the start of the Economic and Monetary Union.

In parallel, the Eurosystem's balance sheet is being reduced through a first-ever quantitative tightening operation under the APP and through large TLTRO III repayments. Reinvestments under the PEPP are set to continue at least until the end of 2024.

In this context, two topics were chosen by the ECON Committee coordinators for today's meeting. The first one is 'A comparative analysis of monetary policy and inflation dynamics in the euro area and the United States'. The second one is 'The climate change considerations in monetary policy implementation'. As usual, all briefing papers prepared by the Parliament's panel of experts are available on the ECON Committee's website.

A few practical considerations before starting. The following procedure will be applied. There will be introductory remarks by President Lagarde of 10 minutes, followed by the first round

of questions, and then a second round. I ask to all of you to respect the time given to you. President Lagarde, before I choke, I give you the floor.

1-004-0000

Christine Lagarde, *President of the European Central Bank*. – Thank you very much, Chair, but I'm afraid I suffer from the same deficiency in terms of throat, and I might choke again, in which case I'll give you the floor. But we are fully equipped with water and a few mints around, courtesy of the European Central Bank, actually – here we are for the mints.

So, good afternoon to all of you. Let me just start with my preliminary comments. So, as I just mentioned, the world has continued this period marked by compounding challenges.

This new political and geopolitical landscape is emerging, fuelled by mounting tensions that are fragmenting the global economy. This has direct economic consequences, as it is fostering uncertainty and economic volatility.

In parallel to this geopolitical turmoil, the climate crisis is accelerating, resulting in more frequent and unprecedented natural disasters. These extreme weather events trigger supply shocks that reverberate through the global economy, further exacerbating the existing challenges.

To navigate this shifting environment, policymakers must be open-minded. At the same time, it is critical that central banks provide an anchor of stability by delivering on their price stability mandates.

In my short remarks today, I would like to briefly discuss our current assessment of the economic outlook and our efforts to bring inflation back to target. Then I will explain how the ECB incorporates climate change considerations in its monetary policy – one of the topics, the two topics, that you have chosen for today's hearing.

So, let's first have a look at the situation of the euro area economy. The activity has stagnated in recent quarters and is likely to remain weak for the rest of the year. Real GDP contracted by 0.1 % in the third quarter, reflecting a broadening impact of higher interest rates, weak foreign demand and the fading impetus from the reopening of the economy after the pandemic.

You must have received the one-pager, which is recto-verso actually – yes, thank you so much – plenty now. Okay, I'll take one.

So, I will refer to this one-pager. You have on the top of the front page, to the left, you have a good description of how GDP is evolving, using also PMI indicators.

So, manufacturing output has continued to fall and activity in the services sector is weakening further. Despite the slowdown in activity, the labour market remains resilient overall, although there are now some signs that job growth may lose momentum towards the end of this year.

While the short-term outlook remains subdued, the economy is set to strengthen again over the coming years as inflation falls further, household real incomes recover, and the demand for euro area exports picks up.

Turning now to inflation, which – as you said, Chair – fell further to 2.9 % in October – that's the latest headline reading that we have. This fall reflected a general decline in inflation, but was also helped by what we call the base effects. These effects were particularly visible in the low rate of energy inflation, which stood at -11.2 %. Food inflation has also declined, but is likely to remain strong for the rest of the year.

This contrasts with inflation developments in the United States – the first topic chosen for today’s hearing – where food inflation has been more contained, while core inflation picked up faster after the pandemic.

I encourage you to look on the back of that one-pager, which is called ‘Topic 1’. It gives you a nice graph of how inflation looks like in Europe and in the United States. I know it’s a bit counter-intuitive, but the numbers that we have in terms of latest readings is: headline 2.9 % in the euro area, headline 3.2 % in the United States.

There is that conventional wisdom that the US is faring a lot better in its fight against inflation. I’m not sure that this is exactly accurate. If we look at core, we are at 4.2 %, the US is at 4 %, but it peaked earlier than we had ourselves.

Inflation excluding energy and food, often called ‘core inflation’, has continued to moderate. It fell to 4.2 % in October owing to declines in both goods and services inflation. Most other measures of underlying inflation have also come down. At the same time, the ECB’s indicator of domestic inflation – which excludes items with a high import content – has not come down by much, reflecting the fact that inflation is now driven more by domestic sources than by external sources. That you will find on the first page in the right-hand graph, which shows in yellow what is actually high – which is high domestic sources.

Wage pressures, meanwhile, remain strong. Our current assessment is that this mainly reflects ‘catch-up’ effects related to past inflation, rather than a self-fulfilling dynamic. We expect wages – and again, that’s on the first page at the bottom left, where you have wage contribution in green, and red for profits – so, wages will continue to be a key factor driving domestic inflation.

But at the same time, the contribution of profits – as I said, in red in that graph – which accounted for much of the strong domestic price pressures seen recently, is now weakening.

Looking ahead, we expect the weakening of inflationary pressures to continue, even though headline inflation may rise again slightly in the coming months, mainly owing to some base effects. However, the medium-term outlook for inflation remains, of course, surrounded by considerable uncertainty.

So, turning to monetary policy, we remain determined to ensure the timely return of inflation to our 2 % medium-term target. In October, as you indicated, we decided to keep the key interest rates unchanged, and we expect that maintaining interest rates at current levels for a sufficiently long duration will make a substantial contribution to restoring price stability.

Our future decisions will ensure that policy rates are set at sufficiently restrictive levels for as long as necessary. The appropriate level and duration of restriction will continue to be determined in a data-dependent manner, assessing the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission.

The Governing Council will reassess its monetary policy stance in mid-December, in two weeks’ time, informed by new data and updated projections, including for 2026.

Let me now turn briefly to the other topic you have selected for today’s hearing. That is climate change in monetary policy implementation.

Climate-related disasters are becoming more frequent and more severe. This year’s catastrophic floods in Slovenia, Italy, Greece and France are a stark reminder of this.

At the same time, the warming of our climate continues. July and August 2023 were the two warmest months on record globally, and the planet is now on track to reach average warming of 1.5°C by the 2030s.

In today's challenging geopolitical environment, it is easy to lose sight of this unfolding climate crisis. But we remain committed to supporting the green transition.

European governments are primarily responsible for addressing climate change. They have the authority, the tools and the ability to implement the appropriate policies to tackle this crisis.

That said, climate change and the protection of the environment are also relevant for the ECB – from the perspective of both our primary and secondary objectives. The ECB therefore remains committed, within its mandate, to playing its part, first and foremost by ensuring that we fulfil our primary objective of price stability.

Large investments in green technologies are needed to support the transition, and a stable inflation outlook gives firms visibility on investment costs, which is particularly important for green projects in light of their mostly long-term planning horizon.

Price stability also supports the relative price signal from policies such as carbon pricing, thereby making those policies more efficient.

Over the past years, we have enhanced our understanding of the economic and financial ramifications of climate change. We published a set of climate-related indicators to improve the quality and quantity of climate-related data. As climate-related data improve, we are also working to further enhance our macroeconomic models, scenario analyses and risk assessment. This helps us better account for climate risks, and the implication for the transition to a carbon-neutral economy may have.

As it is relevant to our primary mandate, we are also working to better take into account climate-related financial risk in the Eurosystem's balance sheet. In doing so, we are also following our secondary objective, by supporting the green transition of the economy, in line with the EU's climate neutrality objectives.

In the implementation of our monetary policy, for instance, our tilting activities have helped decarbonise our corporate bond holdings, and we continue to tilt our reinvestments under the Pandemic Emergency Purchase Programme. You have a reference to that on the back of the one-pager.

We recently concluded our one-year review of the tilting framework, and we expect the decarbonisation of our corporate sector portfolios to continue throughout 2023 and 2024 on a path that supports the goal of the Paris Agreement.

There are three main factors driving this decarbonisation process. First, the effectiveness of our tilting approach. Second, redemption of bonds with a relatively high carbon impact. And third, we see that issuers of the bonds we hold are actively working to reduce their carbon footprint, with benefits for society at large.

Looking beyond 2024, the Governing Council is committed to considering ways to ensure the further decarbonisation of our corporate portfolio on a path that supports the Paris Agreement objectives, without prejudice to our price stability objective. We will continue to review our climate actions to ensure that they remain fit for purpose, focusing on the areas where the risks are greatest and our work contributes to the most.

So, as we enter in this new era of heightened geopolitical tensions and an unfolding climate crisis, we need to step up our efforts to make our economies more resilient. Progress on the green transition, including to accelerate Europe's energy independence, is essential, as it will reduce the likelihood of higher and more volatile energy prices.

Deepening the capital markets union, reaching an agreement on a sound fiscal framework, and addressing regulatory barriers are equally crucial to foster investment and speed up the development of renewables. The ECB will play its part, first and foremost by ensuring that inflation returns to our 2 % medium-term target.

This is not yet the time for us to declare victory. We need to remain attentive to the different forces affecting inflation and firmly focused on our mandate of price stability.

1-005-0000

Markus Ferber (EPP). – Madam Lagarde, I would like to speak in my mother tongue. In the recent Financial Stability Review, the European Central Bank stressed that the effectiveness of monetary policy was largely dependent on good fiscal policy choices. You yourself have already mentioned once or twice in this monetary dialogue that many of the programmes put in place by the Member States, for example during the energy crisis, were not sufficiently targeted and thus ended up undermining the central bank's monetary policy. Given that average budget deficits will be well above 3 % in the euro area and almost 5 % in France, what is your current assessment of the interplay between monetary and fiscal policy? And what does this mean for the ECB's further measures?

And secondly: In addition to interest rates, you of course have a second monetary policy lever – the management of the bond portfolio. With regard to reversing the bond-buying programmes, you are taking a very cautious approach, if I may say so. Only due earnings will not be reinvested under the APP. Under the PEPP, all maturities are still due to be reinvested until the end of 2024. Do you not think that decreasing the size of the portfolio more quickly could also help reduce inflation?

1-006-0000

Christine Lagarde, President of the European Central Bank. – Thank you very much, Mr Ferber. It's nice to see you again. I've missed you a bit in the last few meetings.

So, your first question relates to the fiscal measures. You're right, we had – in 2021 in particular, and in 2022 as well – we had specifically asked that measures that were taken by governments in the Member States be 'triple T': targeted, temporary, tailored. As we all know, and as was acknowledged by the Commission in its review of the measures, not that many of them were both tailored, targeted and temporary.

What we are saying now – that a lot of the circumstances that caused and justified those measures are fading away; in particular energy prices, which have reduced significantly, and bottlenecks that are fading out as well. We are now asking for what we call the rollback of energy support measures, in particular, in order to restore public finance, and to make sure that that is on a sustainable trend. That's the first thing that we ask for.

The second thing that we hope for, and that we expect finance ministers will work hard on – as well as, of course, you Members of Parliament – is the framework within which fiscal policies will be deployed by Member States in the years to come. We are particularly concerned that this fiscal framework be agreed as quickly as possible, in order to reduce the uncertainty in which we are likely to be in 2024 if nothing is agreed.

Your second question deals with the asset purchase programme. You are right. We started announcing that we would gradually reduce the reinvestment; that we would then stop the reinvestment in net asset purchases under the asset purchase programme; and we have done so. We are – as a result of this stop of the net asset purchase programme and letting the securities that we have on a run-off basis – the balance sheet of the ECB is reducing by about 23 billion, an average of 23 billion, per month. That continues to be the case.

In terms of other purchase programmes that we have undertaken, particularly as a result of the pandemic, we have indicated that we would continue reinvesting until at least 2024. This is a matter which will come probably for discussion and consideration within the Governing Council in the not-too-distant future, and we will re-examine, possibly, this proposal.

1-007-0000

Jonás Fernández (S&D). – I will confine myself to today’s debate on the effects of climate change and monetary policy. As you said, the effects of climate change, which we are already experiencing, present us with a likely prospect of greater volatility in the evolution of inflation and inflationary events probably linked to climate effects.

The issue is that some of the measures to combat climate change from a fiscal or budgetary point of view probably involve, among other things, the implementation of, for example, the Energy Taxation Directive. In other words, in the medium term, energy costs should encompass environmental costs, CO₂ costs, but currently, due to the effects of the war and the tensions in energy prices, political negotiation in both the Council and the Parliament is dragging on.

My question is, how to reconcile this trade off? At what point should we introduce such measures as tax increases to combat climate change, bearing in mind that they would have an inflationary effect in the short term, but would hopefully, in the medium term, contribute to climate change being fought efficiently?

What I am trying to say is that there is a clear trade off between raising energy prices in the short term with regard to inflation and the fact that such a tax increase will help to reduce inflation over the medium term. And, taking into account the current scenario as regards inflation and the actual inflation forecasts themselves, what is your assessment of this trade off between adopting measures in the short-term, which may have an inflationary effect and not adopting such measures now, but face higher and more volatile inflation in the future, all linked to climate change?

1-008-0000

Christine Lagarde, President of the European Central Bank. – We can only operate, each of us – you, us, governments, Commission, Council – in the areas and with the competence and within the mandate that were given to us.

But I would agree with your characterisation of the fact that externalities are not actually included in prices in many instances, and that it would be a prerequisite to insert externalities, by way of either a tax or a price signal of some sort – ETS comes to mind, for instance, as another example of how you can include the externalities back into the prices of energy and every other product that includes energy components.

Now, as far as we are concerned, we have to, of course, take into account these climate-change related impacts in the assessment that we make of the economy, in the price expectations that we have. I would also agree – and this is not something where there is complete agreement, and I think economists tend to not completely rally around one single assessment of the situation – but there is a large number of those who will say that, at least in the short term, there is an inflationary aspect of the fight against climate change – not in a very significant amount, if I

look into the accounts that have been provided by our researchers and by our economists, but slightly increasing over the next three to five years. And then, in the medium term, a disinflationary effect, as, of course, the marginal unit of energy and prices related to them are cheaper than what they would otherwise be.

But that's what we have to take into account in the models that we use, in the macroeconomic assessment that we form. It's not for us to make any kind of decision concerning the tax that would eventually apply, or the price embedding that would be required if we want to take into account all externalities.

1-009-0000

Jonás Fernández (S&D). – I have just one additional question. You have spoken about the need to improve the resilience of the European economy and, as you know, the EU is in a process of redefining its industrial policy, based on strategic autonomy in light of the war in Ukraine and the effects of COVID.

My question relates to the potential inflationary effect of this new industrial policy. I do not know whether the European Central Bank has any assessment, opinion or evaluation of the extent to which the revival of European industrial policy could have an effect on prices due to reduced competition, increased public deficits, sectoral subsidies... I do not know to what extent the ECB considers that this new industrial policy could or could not complicate the management of monetary policy.

1-010-0000

Christine Lagarde, President of the European Central Bank. – I think the honest answer to your question is 'no,' because we don't really know what the industrial policy will look like, how much subsidies it will imply, what kind of inflation reduction act will be proposed.

I understand that you will be hearing from the Commissioner in charge of those issues after me, so it's a good occasion to better understand exactly what it will be about.

From our vantage point and participating in Eurogroup on an extensive basis, there is certainly one aspect that is in our view critically important, and that is the capital markets union. Because it's clear that the EUR 650 billion needed per annum in order to accomplish the green transition, and the EUR 125 billion necessary to accomplish the digital transition, that the combination of these two will not be provided on public finances. Whether it's on a regional compounded basis, whether it's at the national level, it simply will not be enough, given the other priorities that prevail as well.

That's the reason why I very strongly believe that the capital markets union has to proceed, has to move forward, and has to do so as quickly as possible, including with a slightly different approach that I have called the 'Kantian shift' to capital markets union, really focusing on those areas that will deliver something, both from a regulatory, from a supervision and from an infrastructure standpoint.

Those are a critically important financing mechanism, calling on the private-sector financing and, in that case, which will hopefully improve the competitiveness and the delivery of the green and digital plans for Europe.

1-011-0000

Stéphanie Yon-Courtin (Renew). – Madam President, dear Christine, thank you for being here today. Against a background of rampant inflation, the ECB's efforts to ensure financial stability and reduce inflation to its 2 % target are to be welcomed. Nevertheless, there is no doubt that these measures have an impact on the daily lives of our citizens, in particular the reduction in the purchasing power of households and the difficulties involved in accessing finance at a time when it is vital for some people. So what can we do and what do you think

we should do to respond to inflation while maintaining citizens' purchasing power, if the current monetary policy continues for some time?

And I have another question. We can now see that monetary policy is necessary but that it has its limits, for it alone will not be able to finance our priorities for the future. And the current revision of the fiscal rules could be one means of reconciling investment capacity and sustainable debt, which are the two targets, despite having different time frames. Can you confirm that debt sustainability and sustainability are compatible objectives?

1-012-0000

Christine Lagarde, President of the European Central Bank. – Thank you for your two-fold question. I am going to continue in French because I want to refer to an expression you used. We do not have rampant inflation at present. We have moved past the period of rampant inflation. I would remind you that when inflation in October – just over a year ago – stood at 10.6 %, which it was, we were dealing with very serious figures, which obviously had a huge impact on our fellow Europeans.

We are now down to 2.9 %. I'm not at all ready to claim a victory – I think that would be very premature – but we have brought inflation down from those very high figures to figures that are much closer to our target.

Of course, that has an impact and we are well aware that it is painful for many citizens as the price of products, especially food – both processed and unprocessed – remains high. Energy prices have fallen but food prices continue to rise. The rate at which they are rising has slowed slightly, but it is still over 7 %, which is in itself an interesting aspect because, in the United States in particular, food prices are increasing at a slower rate. We can come back to this question.

But there is no doubt that this weighs heavily on our citizens. Our goal in the European Central Bank is to ensure price stability and get back down to 2 % in a sustainable manner. That is the task entrusted to us by the Treaties. This is what we have to do, and I believe that sometimes we have to think of the alternative and the fact that if we were not to make such efforts and if we were not to bring inflation down to the 2 % target, our citizens would be in a much tougher situation, with uncontrolled inflation and, above all, the risk of inflation expectations becoming de-anchored.

You are right to point out that this makes it difficult to access to finance, and it is proof that the monetary policy we have put in place to reduce inflation – and which is delivering results – is also being transmitted to the financing of the economy. Borrowing rates have risen for both businesses and households, and the number of loans to businesses and households has fallen. And it is with that in mind that we are obviously trying to reduce inflation by slowing down and increasing the cost of borrowing.

Debt sustainability, sustainability of these measures – our goal is obviously to reduce inflation to the target of 2 %, and of course public finances need to adjust to achieve sustainable debt and restore discipline.

1-013-0000

Michiel Hoogeveen (ECR). – Thank you, President Lagarde, for being here again.

I would like to ask you a question on the climate change aspect. In a recent blog you wrote – together with Fatih Birol, President of the International Energy Agency, and Werner Hoyer, President of the European Investment Bank – you wrote, and I quote, 'Europe must accelerate the green transition to remain globally competitive,' and you added, 'If Europe fails to join the global energy revolution, its competitiveness will be irreparably damaged'.

In addition, your colleague, board member Frank Elderson, recently stated – actually during a period of national campaigning in the Netherlands – that he was glad with the European Climate Law, glad with the Fit for 55 package, and that he was glad with the EU Nature Restoration Law, even before it was voted in the European Parliament, so – and he added that, and I quote, ‘We need to go faster and pull out all the stops to stop climate change.’

Now, I think – obviously what you said in your introductory statement – I think that indeed climate change could have an effect on financial and macroeconomic risks. I agree with that. But don’t you think these are quite strong statements, and you risk of being pulled into what is called the political debate, and something outside your mandate?

1-014-0000

Christine Lagarde, *President of the European Central Bank*. – Thank you, Mr Hoogeveen, for this question. It gives me a chance to clarify without any doubt that our primary objective, our mandate, is price stability, and it prevails over any other objectives of any type.

But we still have within the primary objective the requirements to include all components that will help us determine what is the macroeconomic situation; to use our models in the most efficient way in order to prepare for monetary policy decisions.

We also have – without prejudice to the first objective, which remains the prevailing one – we have the secondary objective, which is to accompany and support the economic policies that is decided by other institutions than ours.

So, it’s very simple for us. It’s primary objective – that embeds in its technicalities and complexity elements of climate change, no question about that – and secondary objectives, which is only without prejudice to the first objective.

I don’t think that I have ever given a speech that I have ever written, anything in relation to climate change and monetary policy, without having prefaced always – as I have actually in the remarks that I just gave – that for us, it is very clear. It is the responsibility of governments, of parliaments, potentially of the judicial powers, but certainly not that of the ECB, as primarily responsible for climate change. It’s a tangential obligation that we have both under the primary and the secondary objectives of our mandate relating to price stability.

But in doing so, we try to identify where we can act, within which parameters, involving other actors, and whether it is the tilting of our portfolio, whether it will be in 2024 the assessment of the collateral that we receive, whether it is the supervision that acts under the auspices of the SSM, whether it is the improvement of our models – we always try to be as comprehensive and as accurate as possible.

I’m using the term ‘accurate’, because I’m especially attentive to the availability and quality of the data on which we can base our considerations. That is something which hopefully will continue to improve, but which is not yet at a stage where we can sufficiently rely on them in order to move in certain directions.

So, I call on you, actually, to help us in relation to quality and quantity of the data available, in order to include, both in our risk management as well as in our portfolio management, the appropriate climate-change considerations.

1-015-0000

Michiel Hoogeveen (ECR). – A short follow-up, and thank you for your answer. I understand what you’re saying. At the same time, the energy transition – as you put in your blog, and as was put forward by your colleague Frank Elderson – is about the energy transition, and about

accelerating the energy transition, and doing more on climate policies. Isn't that fundamentally a political discussion, the way in which we stipulate and form our energy transition?

So, for example, my group is very much of the opinion that the current way, the direction we are going, will actually be a risk to competitiveness of the European economy. If we look at, for example, the investments in wind turbines, we recently saw that Siemens decided to stop using wind energy after the group lost EUR 4.5 billion in its wind businesses.

So, wouldn't it be more – well, 'wise' is a bit of a suggestive term – but wouldn't it be more careful, as central bankers, to refrain from engaging into what we believe is a highly politicised debate, and focus more, actually, on the core aspects of your mandate – and that is indeed the price stability – and try to stay away from pushing for a certain direction of the policies and the political debate?

1-016-0000

Christine Lagarde, *President of the European Central Bank*. – Again, price stability is our compass. It's our goal, it's our target, and I will not repeat that enough.

But it's not for us to debate decisions that have been made in trilogue or otherwise. And if the green transition is something which has been approved and agreed at the highest level of other institutions within the European Union, as has the digital transition been as well, I cannot argue with that.

It has been decided and it belongs to the public good policies, if you will. And as a result, we have to pay attention to them and include that in our secondary objectives.

1-017-0000

France Jamet (ID). – Ms Lagarde, I would like to discuss two points with you, which will lead to two questions. Firstly, you announced at previous monetary dialogues that the European Central Bank's goal was to reach a neutral rate for its key interest rates, but it is now clear that they have reached around 4 % as a result of a series of unprecedented increases.

To determine a monetary policy, the nature of inflation must be clearly identified. According to Eurostat, inflation was 2.9 % for October 2023 in the euro area. You yourself spoke about it and gave us these figures. We are therefore above the neutral rate. The core inflation you just referred to, i.e. excluding energy and food expenditure, has remained at 5.5 % since the beginning of the year. On that basis, we can see that the ECB is very far from the neutral rate.

The second point is that the US Federal Reserve's rates remain higher than those of the ECB, which could pose a risk to the value of our currency. Of course, for the time being, the euro seems to be holding up quite simply because of a highly expansionary US fiscal and budgetary policy.

Now to my two questions. The first is this: do you believe that you have reached the neutral rate that you have mentioned several times during our various discussions? And secondly, are you not worried that the euro's slight recovery against the dollar might just be cyclical? And on that basis, what is our outlook as regards exchange rates in the medium term in a geopolitical context where producer countries could decide at any moment to cause a spike in oil prices, notably by limiting production.

1-018-0000

Christine Lagarde, *President of the European Central Bank*. – Thank you very much for your questions. Let me first of all clarify what I mean by a 'neutral rate', which economists sometimes also call the 'R-star' rate. In fact, this neutral rate is the rate where we have a perfect balance in which the factors of production provide, there is no imbalance, inflation is

at the target rate – that is the principle of a perfectly balanced system. That is, for us, the ‘neutral rate’.

Today – and I will talk about the latest figures we have – what we see is inflation at 2.9 % in the euro area, with core inflation, excluding food and petroleum products, at 4.2 %. So we are really in a period of slowing inflation, disinflation, which can be seen at both core and headline levels. At the same time, we have interest rates that we have gradually increased over the last 15 months from -0.5 % – minus 50 basis points – to + 4 % for the main reference rate, pushing up our rates by 450 basis points in the space of 14 or 15 months. Such acceleration and movement are unprecedented and have helped to reduce inflation, as I just mentioned.

We firmly believe that that measure has played a part in lowering inflation. We also believe that we have to stick to those rates for as long as it takes to get to the 2 % target, which we haven’t yet reached: inflation is still too high today and has been for too long. We need to maintain this interest rate, and if we do so for long enough, it will help us to get back to the 2 % target in the medium term. We will do that. And we will deliver on the basis of the data we receive in each economic forecast and on the basis of the three specific elements we have indicated to explain how monetary policy is determined, i.e. the inflation forecast, core inflation, and the speed at which our monetary policy is transmitted to the economy and to the financing of the economy.

This is the framework for our approach. I believe that, in this context, we need to be both patient and alert. Why patient? Because a huge effort has been made in the past 15 months and we need to be sure that inflation is falling, that there is transmission, that all the monetary policy measures are being passed on and bearing fruit in our economic systems. We need to be alert because there are a number of factors that contribute to inflation at present, in particular the unit rate of the unit of work and the profit unit. These elements and the way in which they interact will be crucial in particular when observing inflation trends in the services sector, which is the sector that currently has the biggest impact on inflation rates.

Now to your third question: the difference between the Fed rate and the ECB rate. It seems from memory – though I did not check the figure – that there is roughly one point between the rates. We have a headline rate of 4 % and the various US rates are between 5 % and 5.25 %. This is also due to different fundamentals, and the United States having different and stronger growth, which is an area in which I believe monetary policy should play a more assertive and undoubtedly a more robust role.

However, as you said, there are no particular observations to make on the exchange rate between the euro and the dollar – other than its contribution to inflation – and the euro has risen in recent weeks. So I would refrain from offering any exchange rate forecasts. We are obviously watching it very closely because it contributes to inflation, imported or not, depending on whether or not the euro depreciates, but this difference is caused by a number of factors.

1-019-0000

Lídia Pereira (PPE). – Statements by President Lagarde or any other member of the ECB Governing Council naturally have an impact on the markets and the value of the single currency. And there is a reason for that: it is called ‘credibility’. Credibility resulting from authority and authority resulting from independence. And that is why I would like to ask you about the flagrant breach of the Code of Conduct by a member of your Governing Council, Mário Centeno. Mário Centeno is Governor of the Bank of Portugal, after going through the ‘revolving door’ following his government position as Minister for Finance. And he’s gone further: from President of the Eurogroup to member of the European Central Bank. In 37 days. He has now agreed to the Portuguese Prime Minister’s proposal that he replace him,

going back through the ‘revolving door’ in the other direction and posing a threat to his independence, which has been irrevocably compromised. Some colleagues have already asked you in writing, but I would like to ask you here: will the European Central Bank ignore this breach of its Code of Conduct or will it take action?

1-020-0000

Christine Lagarde, *President of the European Central Bank*. – Thank you very much, Ms Pereira, for your specific question.

Let me make that point very clearly. The independence of the ECB decision-making bodies is essential for achieving its mandate. Being truly independent requires all ECB policymakers to abide by the highest ethical standards. The ECB has in place for its high-level officials a strong code of conduct and a dedicated Ethics Committee to ensure that the ethical rules are implemented adequately, coherently, in a level playing field.

So, I have received letters on the matter from Members of this Parliament. I have asked the ECB Ethics Committee to look into it, and will answer after receiving the assessment from the Ethics Committee.

1-021-0000

Pedro Marques (S&D). – President Lagarde, I must begin by expressing my disappointment that the PSD has once again brought national matters to the European Parliament. The Bank of Portugal and its Governor have not failed to fulfil any of their duties. Their ability to perform those duties in an independent manner is not disputed. The EU should not be the stage for a national election campaign. A party that is responsible and wishes to govern casting aspersions on an institution as important as the central bank of its own country for electioneering purposes will certainly not help the PSD, but unfortunately we are used to it. In my opinion, the limits of decency and defence of national interests have once again been crossed.

That said, President Lagarde, let us move on to what really matters and not linger on the episodes that the honourable Member wished to discuss here. You recently said that a person close to you lost money due to cryptocurrencies and called for more regulation in the sector. I would like to ask you: you must also have close family and friends who are suffering a great deal as a result of higher interest rates on mortgages. The ECB is focused on cutting inflation – and rightly so. But I would like to ask you how we can explain to people suffering as a result of interest rate hikes that, at the same time, banks are making record profits and distributing record dividends to shareholders.

What measures and tools can you use? Can you guarantee that the deposit facility, remuneration from the deposit facility, is not contributing to an upsurge in profits in the banking sector and, furthermore, causing central banks to make losses? And, given the likely development of non-performing loans, shouldn't the SSM immediately start requiring banks to boost their balance sheets, rather than carry on paying out dividends without restraint?

1-022-0000

Christine Lagarde, *President of the European Central Bank*. – Thank you very much, Mr Marques. I think what you're referring to is the impact that interest rate hikes have been having on the financing conditions of households in particular and those that have taken out mortgages.

Let me first observe that we have quite a lot of heterogeneity in Europe and in the euro area. There are quite a few countries where households have borrowed under mortgage at fixed rate, and for those, obviously – for the borrowers at fixed rate – the current situation is not totally uncomfortable, quite to the contrary.

But there are also countries – and I think Portugal is one, but Finland is another one, the Baltic countries as well – where there is a predominance of variable interest rate mortgages, and for those, of course, the burden of the debt service has increased as the interest rate has been hiked over the last year. So that is clearly the case.

In a way, we, as a central bank, are observing that, monitoring that, and we draw the conclusion that there is good transmission of our monetary policy. Because as we increase the DFR, for instance – or other interest rates, but this one is the most relevant one – we are keen to see that it is transmitted throughout the system in the financing terms that are offered to corporates and to households.

We also observed that in the last few months – for term deposits, certainly, and a bit more now for deposits – we are seeing a slight increase of the interest rate that is served – certainly in different proportions, much higher for term deposits, and still very low for sight deposits. We very much hope that our monetary policy is transmitted not just in the mortgage rates, but also in the deposit remuneration.

So, that's what I can tell you at this point in time, in terms of the burden that applies to mortgage holders. I know that there are countries where terms and conditions of those loans provide for a specific suspension for a period of time, particularly if households go through a difficult economic situation. I know that many banks have actually offered to extend those terms and conditions while interest rates are still high and continue to be high.

1-023-0000

Georgios Kyrtos (Renew). – I would like to thank President Lagarde for her presentation.

I have a question concerning the coordination between major central banks in an effort to reduce inflation. Are you satisfied by the level of coordination? Are some things that could be improved between the Federal Bank, for instance, the ECB, the Bank of England? Or is everything covered by professional secrets, so you don't have to tell us anything? This is my first question.

The second question has to do with what Mr Ferber said about the fiscal policy, because in the European Union, we have two schools of thought. One school supports, let's say, an expansionary fiscal policy. The other wants to apply some kind of fiscal brake. But what about other major Western countries? For instance, the USA has a budget deficit of more than 6 % of GDP, if I'm not mistaken, and we have a similar evolution in Japan and the United Kingdom.

So, how do you think we can reconcile getting our house in order, our fiscal house in order – which, I agree, is necessary – with the fact that other Western powers, which are competing with us in any way, have even bigger deficits?

1-024-0000

Christine Lagarde, President of the European Central Bank. – Thank you very much, Mr Kyrtos.

On your first question, which is the coordination between central banks around the world, we do compare notes. We do exchange views. We don't coordinate monetary policies. On a regular basis, all central bankers who are members of the club meet in Basel.

That's where we look at financial stability. That's where we look at the state of the global economy and the spillovers between the various economies. So, we try to have as much of an intake of economic measures, economic policies, change in the geopolitical landscape.

So, we discuss all these matters, but we never coordinate our monetary policy. While we can meet a few days before a monetary policy meeting, either in Washington or in Brussels, or in Tokyo or in London, we never, ever share what our expectations are going to be or what decision we will propose. It stays within the Governing Council, from my perspective as ECB, and within the FOMC at the Fed, and it's not something that I would even think of sharing, let alone ask in terms of information.

But of course we are focused on price stability. All of us. And some of us – I think of the Fed, for instance – have a dual mandate and is also concerned about growth and will decide its monetary policy on the dual basis of its dual mandate.

Fiscal policy, you're right, is very different in terms of fiscal support, in particular between the United States and Europe, between Europe and Japan. It's a factor of our different economies. It's a factor of the different strength of our currencies as well. It's a factor of political preference.

From our perspective, I would say two things. One is, please, both governments, Parliament and all institutions concerned, deliver some fiscal framework within which fiscal policies can be decided, with common criteria, with common understanding of what is intended and expected, in terms of competitiveness, in terms of investment, in terms of public finance.

Second, let's make sure that there is enough investment in order to improve the competitiveness of Europe in all sectors where we have competitive advantage or where we can develop competitive advantage.

1-025-0000

Danuta Maria Hübner (PPE). – Madam President, as usual, pleasure, but I would also like to thank you very much for your recent speech on the capital market union, because, as you know, we have been – Irene would confirm – for the last years, actually, we have been fighting for the truly single capital market union.

But, as you know very well as well, we are often facing, especially in the trilogues, just narrow-minded defending of national interests, and so I hope that your speech will strengthen our position also in the upcoming trilogues. So thank you very much for this.

I would have two questions. One is a request to you to update us on the Transmission Protection Instrument, because I understand that since it was launched in July 2022, it has never been used. But then if you look at the spreads, if you compare the spread between Italian and German bonds, you can see that in this year, the situation of Italian bonds improved strongly. So maybe we don't need this instrument to be applied, because it is enough that it is somewhere hanging in the air and is working as a kind of risk instrument, or just impacting without being used. So that's my one question.

My second question is related to what you said about the fiscal rules in response to Markus Ferber's question. You said that those new ones on which we are working with the Council, or maybe still separately, that they should come as soon as possible, because we bring the reduction of uncertainty.

But in this context, I would like to ask you, because my understanding is that the Commission proposal would lead to substantial tightening of the fiscal stance in the medium term. So it will not just come overnight. It will take for some time this process of tightening the fiscal policies, and this continued fiscal consolidation under this new fiscal framework might result in an overly tight fiscal stance.

The question to you is – I don't know when you will finally reach the target inflation, but you can reach a moment where your implementation of the new fiscal rules will collide with the logic of monetary policy. Do you see this risk that this process of implementing this rule – which will be monitored, and we will be very tough on it – can somehow be in collision with your logic of monetary policy that might ... – so do you see this risk? Do you worry or you think that you will just cope with it once it's come?

1-026-0000

Christine Lagarde, *President of the European Central Bank*. – Count on me, on capital markets union. I will repeat if necessary, and it's really, really important, and I agree exactly with your characterisation of the approach that is taken occasionally by Member States, which I think calls for a higher imperative than the pure domestic perspective.

So, on your first question on the Transmission Protection Instrument that we outlined and announced in July 2022. It was intended to safeguard the smooth transmission of our monetary policy throughout the entire euro area market and to all countries, and it was certainly not intended to cushion the worsening of country-specific fundamentals. That's very clearly stated.

So it has a set of criteria that apply to countries that would eventually fall under the benefit of that Transmission Protection Instrument, that would benefit from the Transmission Protection Instrument. I can list them for you.

It's number one: compliance with the EU fiscal framework. Number two: the absence of severe macroeconomic imbalances. Number three: fiscal sustainability. Number four: sound and sustainable macroeconomic policies.

Of course, before those criteria are applied to any potential candidate country, we have to determine that the TPI is actually appropriate and proportional in order to deal with the situation. In particular, we need to make sure that it's intended for the purpose for which it was created.

It was intended for a temporary period of time and without prejudice to our monetary policy. I think it's a good instrument. We have not had to use it and it's not the only instrument that is in the toolbox and which we haven't used, but it's there, and if and when it is necessary to use it, of course we will use it.

So your second question related to the response that I gave to Markus Ferber concerning the fiscal governance and the economic dialogue that is ongoing at the moment, for which I encouraged very much the parties to the agreement to reach a conclusion as quickly as is possible, for one primary reason: it would help us eliminate the uncertainty and the vagueness of the parameters within which Member States are deciding their budgets at the moment.

They have guidelines. They have some recommendations. The Commission has to scrutinise their proposed budget, as it normally does, but without reference to a framework, or with reference to an old framework which everybody seems to agree is not adequate in order to deal with the current situation.

We have transmitted our comments, and we have given an opinion which was agreed by the whole Governing Council in response to the draft Commission plan, which has now been revised under the Spanish Presidency, which has come up with some new proposals.

But those comments included in particular: one, a realistic and gradual and sustained adjustment of public debt – so that coincides with what you said – which is not a brutal effort which is frontloaded, but over the course of time, for seven years. This is something that is much in

debate, as I understand – a public debt that comes back to a more realistic and good adjustment that makes it sustainable.

Second, we have encouraged policies that promote growth and investment; and third, we have encouraged the announcement of countercyclicality; and we have also added that the enforcement mechanism should be efficient, should be enforceable – which we have not always seen – and that the whole new framework should hopefully be more simple to understand and to implement.

So, we hope that this will be the case. I'm a little bit sceptical about the simplicity aspect of what is being negotiated at the moment – and not that it would require a brain surgeon to actually understand how it applies – but it would certainly require a lot of thorough knowledge of all the criteria, the parameters, and the various alternatives in the tree of decision that the Commission will have to apply.

But, first and foremost, we would like to have some certainty about what framework will apply. Thank you.

1-027-0000

Lefteris Nikolaou-Alavanos (NI) – Madam President, Ms Lagarde, as is evident from the data coming from the EU, the US, as well as from China, the key factor that is shaping the present period, is inflation and the looming capitalist crisis. Naturally, when this crisis does emerge it will be on the back of the great hardship endured by workers who are unable to make ends meet because their income has been slashed as a result of inflation, which you yourself described as persistent inflation. And, of course, the resulting price hikes will persist for many years to come, along with rising electricity prices. Despite the rise in prices, wages/salaries remain frozen, as instructed by the European Union and the Central Bank, because you consider salary increases to be inflationary. Meanwhile, tough measures are being taken, with Greece for instance introducing a new tax bill that penalises the self-employed while business groups continue to receive tax breaks.

Neither of the two basic approaches taken, i.e. the contractionary fiscal policy chosen by the EU in the last crisis 10 years ago, followed by the expansionary fiscal policy adopted recently – both of which favoured big business – succeeded in addressing inflation and the crisis because it is a crisis of overaccumulation of capital and a lower than desired profit margin. Instead, these approaches deepened divisions within society, with 1 % of the population holding 50 % of the wealth, that is, a 10 % increase compared to 10 years ago, and one in four workers in the EU today is at risk of poverty.

In light of all this, how do you respond to current demands from workers and working-class people not to be the ones who pay for the looming crisis as they did for growth? In other words, demands for income increases for the ordinary working people, pay and pension increases above the rate of inflation, abolition of unpopular excise duties, a 40 % tax increase on business group profits, and tax cuts for the working classes.

1-028-0000

Christine Lagarde, *President of the European Central Bank*. – Thank you very much for your question.

Two things that I would like to mention in response to your various points. One is: I believe that in delivering on our mandate of price stability, we reduce the inequality that is produced by high inflation. That's point number one.

Point number two: we are observing at the moment a balancing act between the contribution of profit versus the contribution of wages. While, of course, as you know, we remain very attentive

that we don't go into the second-round effect and the spiralling of inflation out of control, we also assume in our baseline that wage increases – which are continuing, because of the catch-up, because of the tight labour market – will entail a reduction of the profit margin, which have themselves contributed in 2022 significantly to inflation.

But we are seeing – and that's the graph that you have here at the bottom of page one – the contributions to GDP deflator, where you see that the contribution of wages has increased, and we are now seeing a reduction of the contribution of profits measured by unit, both for labour and profit. Thank you.

1-029-0000

Gunnar Beck (ID). – Good afternoon, *Madame la Présidente*.

In 2015, your predecessor went to very great lengths to assure us that multi-trillion bond purchases were not monetary financing, and that the ECB's purchases were merely temporary. The German Federal Constitutional Court subsequently took up that point and stated very clearly that if ever bond purchases became permanent, that would be a clear proof that the ECB is engaging in monetary state financing.

Now, on 9 November, your chief economist, Philip Lane, announced the ECB thought that, quote, 'a durable level of central bank reserves was required' and – I'm still quoting – 'that a structural bond portfolio was most suitable, as this would provide longer-term liquidity to the banking system'. In other words, a portfolio would permanently include APP and PEPP purchases.

So, was Mr Draghi not altogether honest all along, or can you assure us, contrary to Mr Lane's musings, you will eventually liquidate all bond holdings?

1-030-0000

Christine Lagarde, President of the European Central Bank. – Thank you, Mr Beck. I'll tell you something, I would be remiss to pass any kind of final judgment and to give you final consideration as to how these reserves will be constituted.

As you probably know, given the pertinence of your question, we are undergoing a review of what we call the operational framework, which is the way in which we try to monitor interest rates, the way in which we provide liquidity to banks.

This is an extremely complicated matter, where we have to study in depth many consequences of the various options, which include financing, refinancing; which include structural portfolio; which includes the volume of liquidity that is necessary and the way in which banks will access that liquidity. It's a complicated matter which will give rise to multiple trade-offs review, and we are in the middle of this work.

So this is very much work in progress. There will be many views expressed in the next few months. There will be in-depth examination of options, and it will be for the Governing Council at the end of the day to actually determine what will be the operational framework.

It may well include several components. That is a possibility. What I can imagine is that it will produce a balance sheet, the size of which will be definitely smaller than the peak that we have observed in the last couple of years; where I would imagine it will also be higher than what it was before the great financial crisis.

The third observation that I would make is that even when the Governing Council of the ECB has made its decision – on the basis of, as I said, multiple observations and opinions – when it

does so, there will be experimentation, because of the highly sophisticated nature of this operational framework.

But we will do that taking the appropriate time to review all the options. The one that you have mentioned is certainly a very informed consideration, but there will be more, and the ultimate decision will belong to the Governing Council of the ECB. Thank you.

1-031-0000

Chair. – Thank you very much. I have no further requests for the floor, so we can thank President Lagarde for her availability as usual.

Also I take the opportunity to highlight that the next, and also last, monetary dialogue of this legislative term is expected to take place on February 2024, and this will happen just after the 25th anniversary of the introduction of the euro, which took place on the 1 January 1999.

In this context, the ECON Committee coordinators have decided to focus on one topic: ‘Euro at 25 – what’s next for the EMU?’, which will allow to take stock of the first 25 years of the common currency, while assessing future challenges for the Economic and Monetary Union.

So, thank you very much. We will meet again in February. Thank you. Happy New Year.

Yes, we suspend for half an hour and we resume at 17:00 with the hearing with the Commissioner Breton.

(The Monetary Dialogue closed at 16.32.)