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### Surprise ECB moves

# Busy, busy

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THE European Central Bank responded today to a flatlining economy and a fall in inflation to just 0.3% with two new measures. First, its governing council lowered the bank's main lending rate from 0.15% to a new low of 0.05%. It also brought down its deposit rate from minus 0.1% to minus 0.2%, in effect increasing the charge that banks must now pay for placing spare funds with the central bank. Second, it announced that in October it would start to purchase asset-based securities (ABS)—whose underlying claims are in the private non-financial sector—and that it would also start to buy covered bonds—bonds issued by banks that are backed by mortgages or public loans—again.

The first decision—lowering interest rates again—was a surprise because in June, when the ECB had previously cut rates, in particular pushing the deposit rate into negative territory for the first time, it had indicated that it would go no further. Speaking on that occasion, Mario Draghi, the bank's president, said that "for all practical purposes, we have reached the lower bound." (Technically, the lower bound refers to the fact that there is a limit in imposing negative interest rates since depositors can switch to cash instead.) Today he insisted that whatever he might have said in June the ECB had now definitely reached the lower bound.

The ECB had already paved the way towards the second new measure—the purchase of ABS—in June when the governing council said it was intensifying preparatory work towards making such purchases. But now it has set a firm date for when the programme will commence. The securities will include mortgages as well as commercial loans among the underlying assets.

On the face of it this looks like the first step towards quantitative easing (QE) since the ECB will pay for the assets by creating money. But the move sets less of a precedent than it might appear. The two previous programmes of covered-bond purchases, in 2009-10 and 2011-12, which together amounted to around €75 billion ($100 billion), were not "sterilised", ie the ECB did not mop up the money created by them. And in June, the ECB stopped sterilising its remaining holdings of peripheral government debt (then worth around €165 billion) acquired between May 2010 and February 2012 in an effort to quell panic in the bond markets. That decision could be regarded as retrospective QE.

In any case, the size of the ABS market in the euro zone is simply too small to permit the scale of QE—a purchase programme worth around €1 trillion—needed to boost growth and raise inflation. Research recently published by Bruegel (http://www.bruegel.org/publications/publication-detail/publication/842-asset-backed-securities-the-key-to-unlocking-europes-credit-markets/) , a think-tank in Brussels, estimated that the entire securitised market is worth only around €1 trillion, a good chunk of which the ECB would not want to touch either because the securities are not "simple and transparent" or because they are too risky. The likely size of possible purchases would be €100 billion to €150 billion, reckons Nick Kounis, an economist at ABN Amro, a Dutch bank —too small to make much of a difference. Only purchases of sovereign debt would enable the ECB to intervene on the scale that is required. But such an intervention would be bitterly opposed by the Bundesbank on the grounds that it would redistribute fiscal risks among the 18 member states that belong to the euro.

But if the ECB is still distant from QE—today's decisions were not taken unanimously by the 24-strong council—it is certainly going to be busy in the remaining months of the year. Later this month it will conduct the first of its new lending operations, announced in June. The aim is to boost credit to businesses by providing dirt-cheap funding to banks (the rate will now be just 0.15%) for as long as four years provided that they improve their lending performance. In October, along with the new ABS and covered-bond purchase programmes, it will announce the results of its year-long assessment of big euro-zone banks which has involved both an asset-quality review and a new round of stress tests; those banks found wanting will have to find new capital. And in November the ECB will formally take over the job of single supervisor within the euro zone. The ECB is expanding at breakneck speed: if only the businesses and workers in the single currency club were as busy.