

United in diversity – Challenges for monetary policy in a currency union

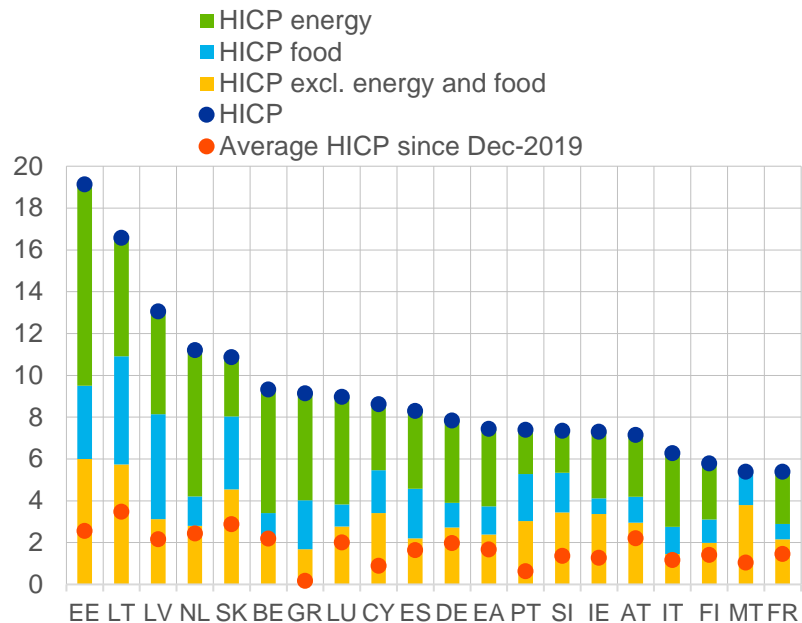
Isabel Schnabel, Member of the ECB's Executive Board

Commencement speech to the graduates of the Master's Programme in Money, Banking, Finance, and Insurance at the University Panthéon-Sorbonne, Paris, 14 June 2022

High divergence of inflation in the euro area

HICP inflation and components

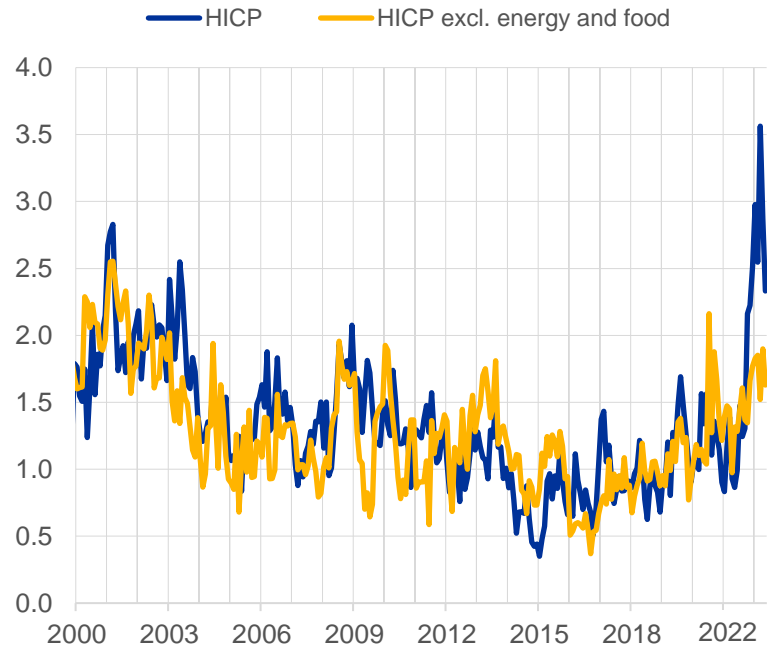
(annual percentage change)



Source: ECB and Eurostat.
Last observation: Apr 2022.

Inflation divergence

(percentage points)

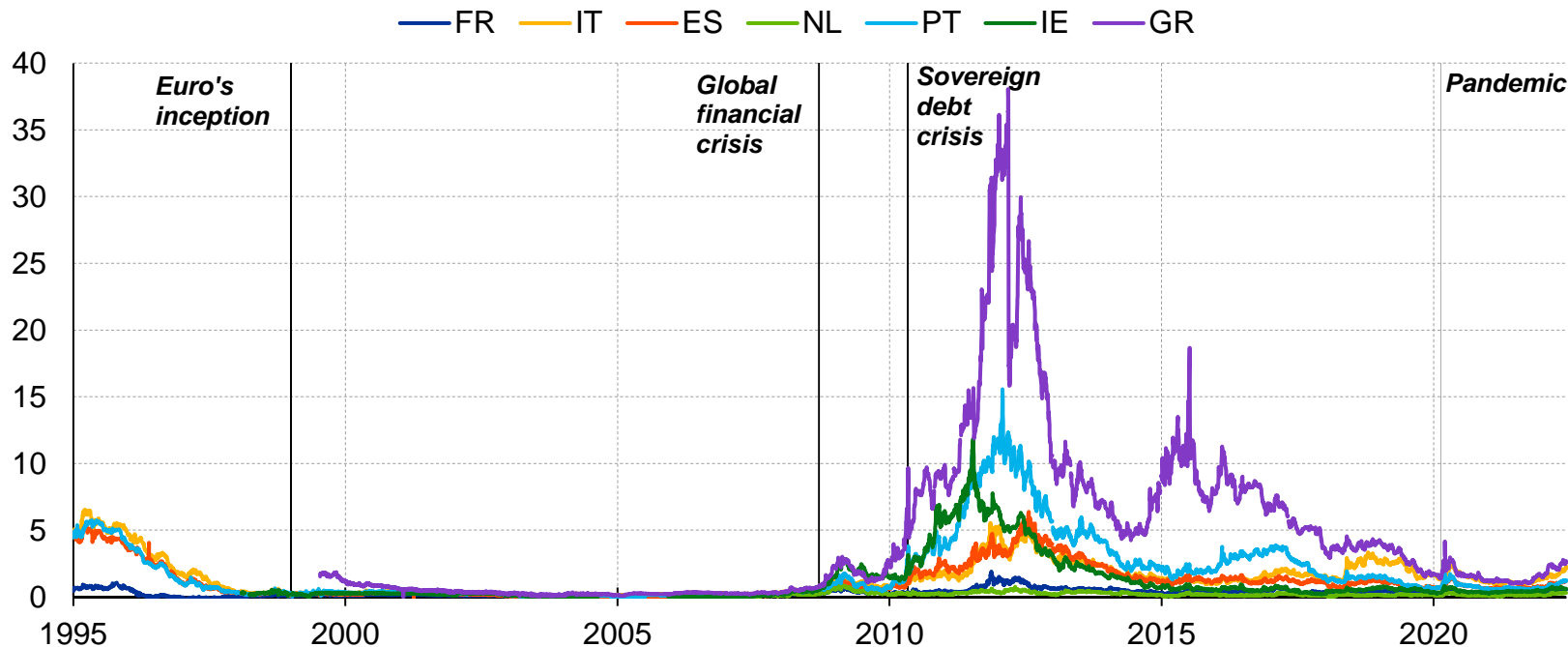


Sources: ECB and Eurostat.
Note: The chart shows the inter-quartile range, i.e. the difference between the 75th and 25th percentile of the cross-country distribution.
Last observation: May 2022.

Turbulent history of bond market fragmentation in the euro area

Euro area 10-year sovereign spreads

(percentage points)



Sources: Haver

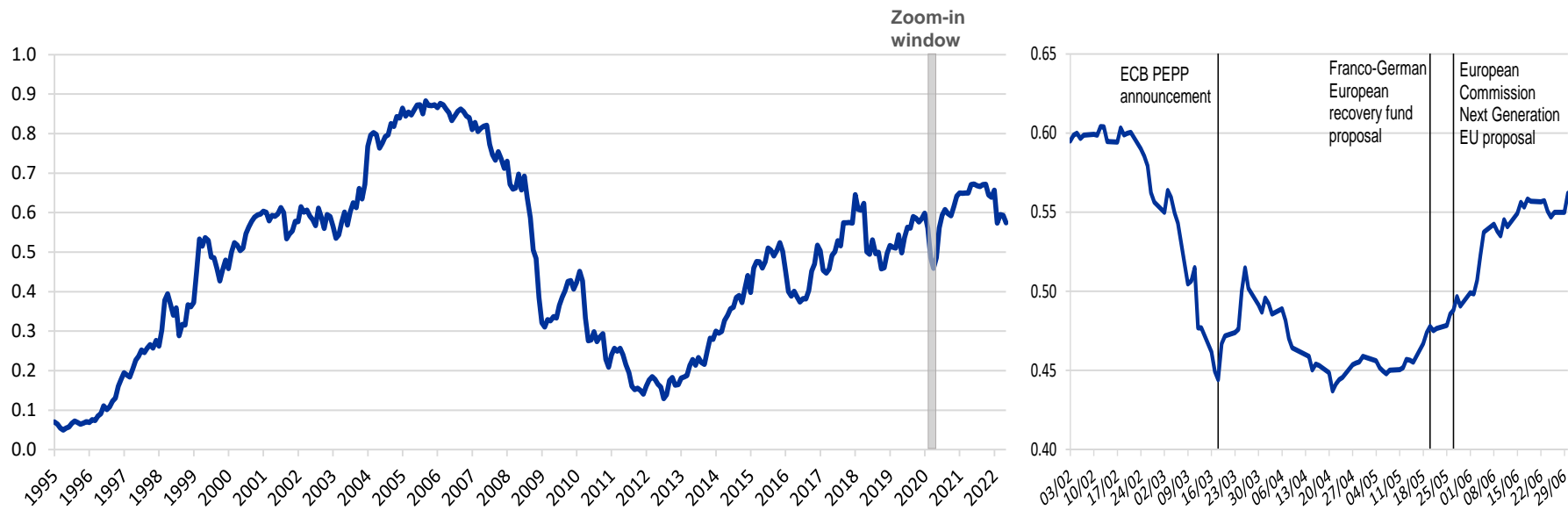
Notes: 10-year sovereign bond yields over 10-year German Bund. The vertical lines mark the beginning of each phase.

Latest observation: 10 June 2022.

Fiscal and monetary policy jointly halted and reversed fragmentation in the pandemic

Euro area price-based financial integration indicator

(monthly data, January 1995 – May 2022; zoom in window: daily data, 3 February 2020 – 30 June 2020)



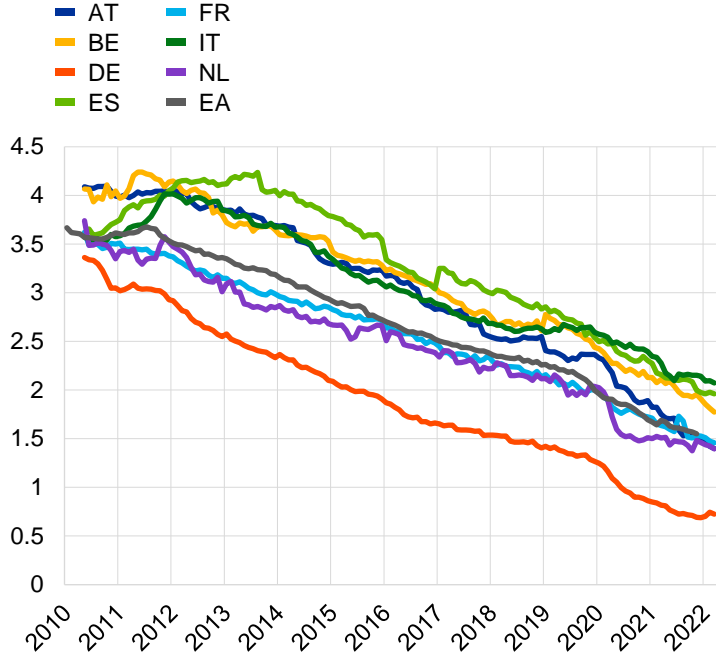
Sources: ECB Report on Financial Integration and Structure in the Euro Area, April 2022.

Notes: The price-based composite indicator of financial integration is a high-frequency version (daily readings) of the one by Hoffmann et al. (2019), described in Borgioli et al. (2020). The indicator is calibrated to vary between 0 and 1.

Borrowing costs for euro area sovereigns declined, while maturities increased

Average nominal sovereign yields on total government debt securities

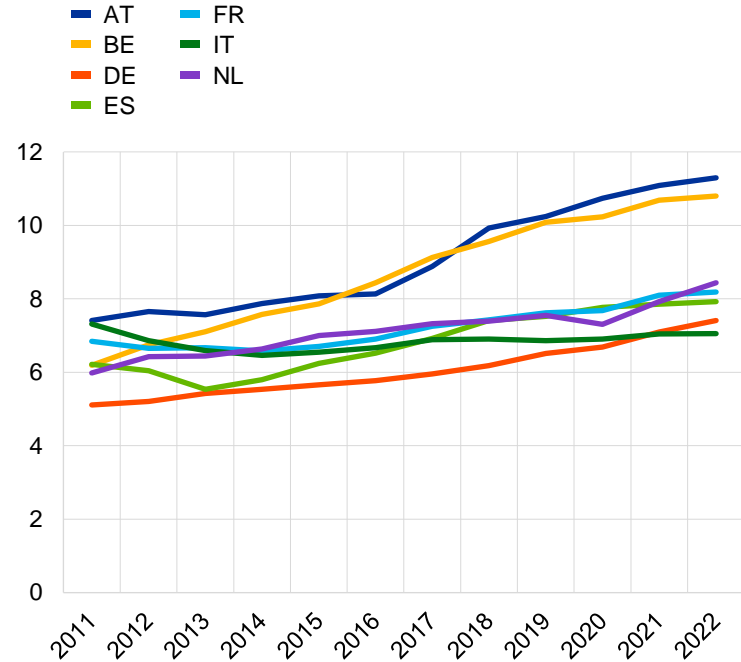
(percentage points)



Source: ECB and ECB calculations.
Note: Last observation: April 2022

Residual maturities

(years)

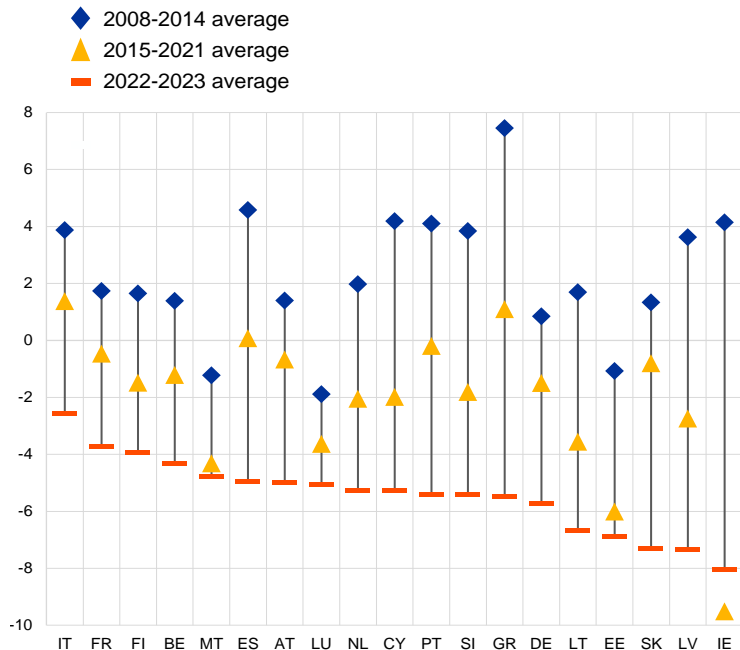


Source: ECB and ECB calculations.
Notes: All original maturities. Annual averages per year, for 2022 average over the period January – April.

Given favourable interest rate-growth differentials, public debt ratios likely to decline

Interest rate-growth differential

(percentage points, average over period)

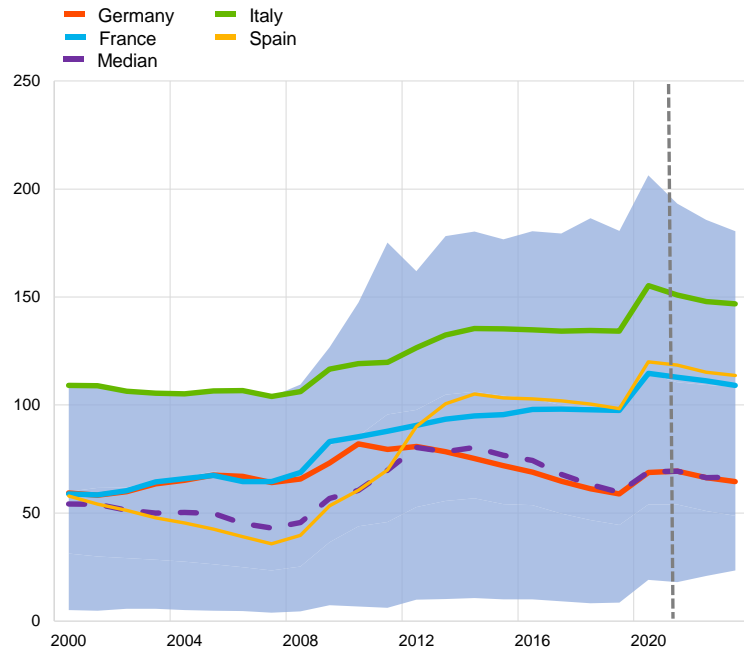


Sources: European Commission, ECB calculations.

Notes: The interest rate-growth differential is calculated using the implicit interest rate on government debt and the growth rate of nominal GDP. The implicit interest rate in year t is interest payments by the government in year t divided by government gross debt in t-1. Countries are sorted according to the 2022-2023 average interest rate-growth differential. Figures for 2022 and 2023 refer to the European Commission 2022 Spring forecast.

Government debt in selected countries

(percent of GDP)

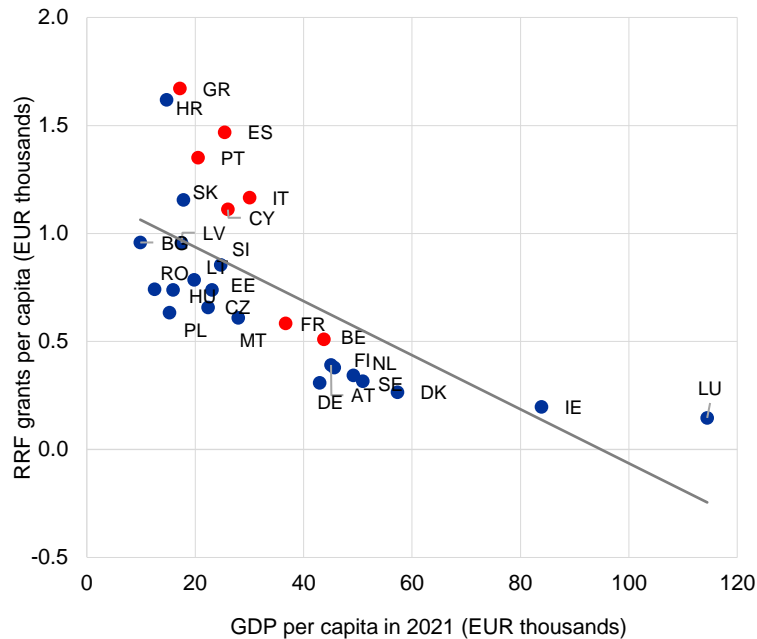


Sources: European Commission

Note: The range shows the min and the max of all euro area countries. Figures for 2022 and 2023 refer to the European Commission 2022 Spring forecast. Latest observation: 2023

NGEU allocations tilted towards countries with weaker GDP per capita and higher public debt

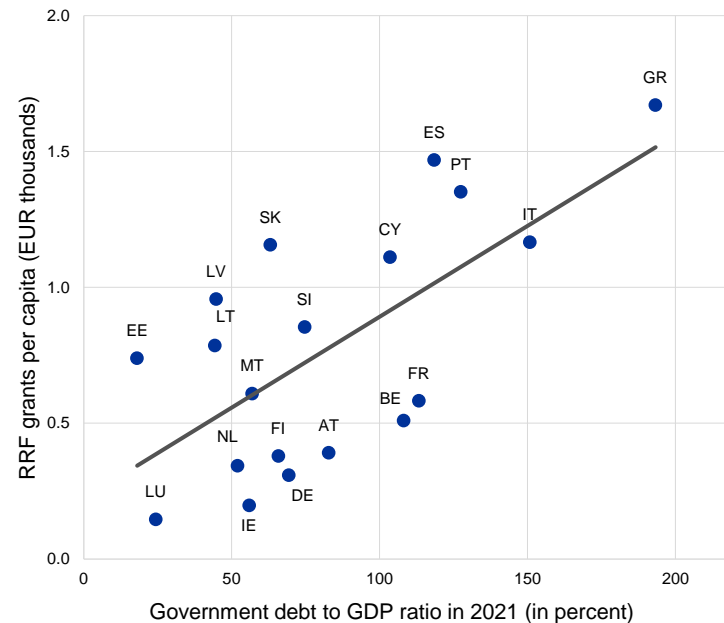
Recovery and Resilience Facility (RRF) grants per capita vs. GDP per capita



Sources: European Commission, ECB calculations.

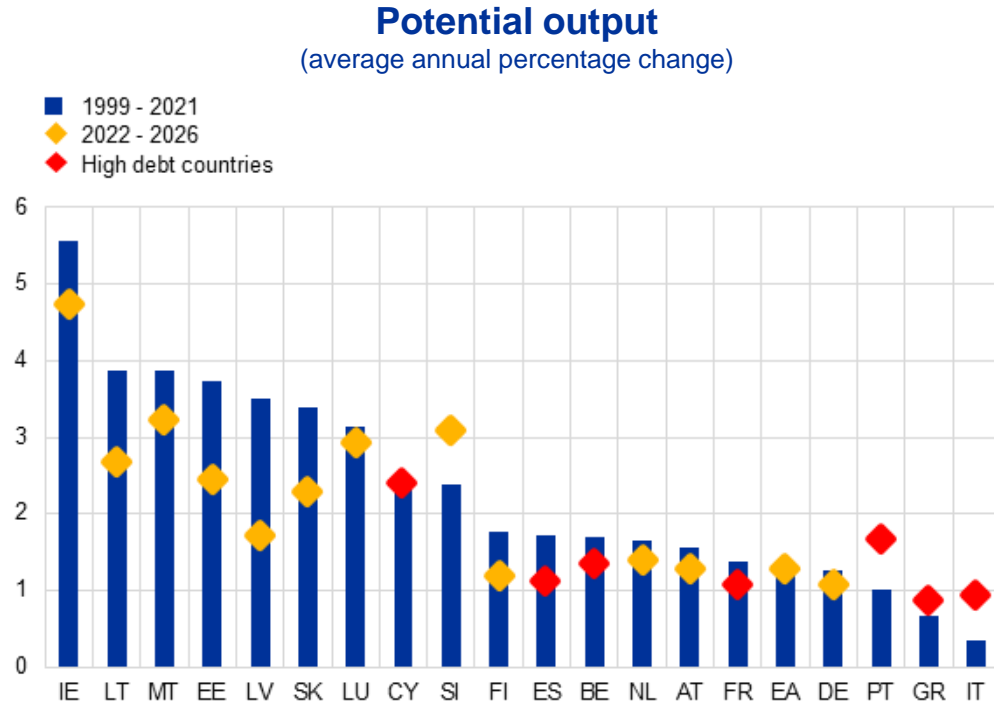
Note: Red dots indicate a country with a debt-to-GDP ratio exceeding 90%.

Recovery and Resilience Facility (RRF) grants per capita vs. government debt to GDP ratio



Sources: European Commission, ECB calculations.

Potential growth outlook above historical average for some high-debt countries

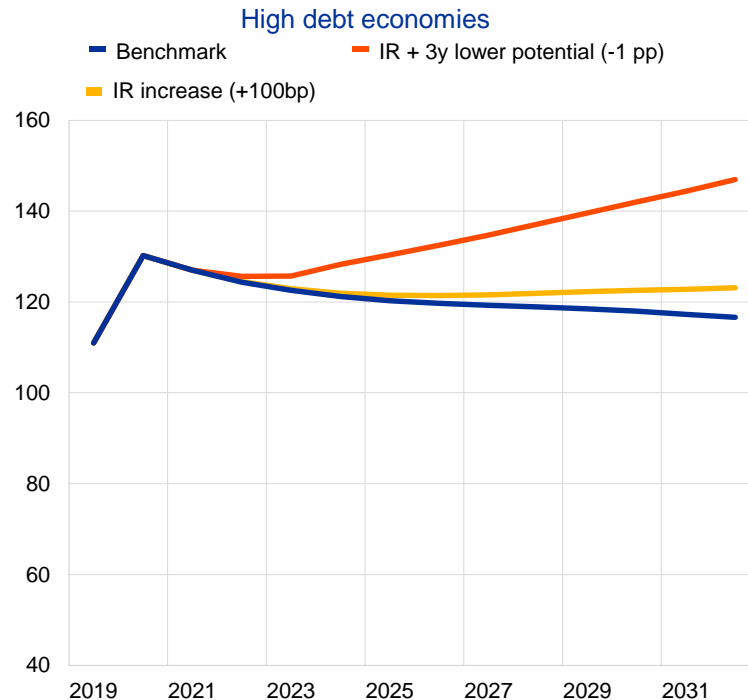
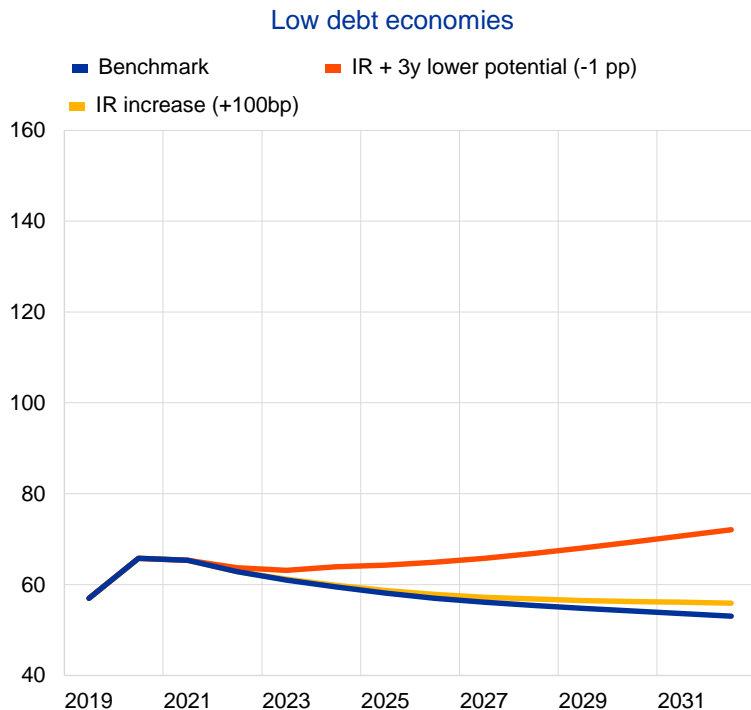


Source: European Commission, EPC Working Group on Output Gaps

Note: The definition of high debt countries is debt to GDP ratio of over 90% of GDP in 2019.

Potential growth matters more for sovereign finances than interest rates

Impact of an interest rate and GDP shock on sovereign gross financing needs (percent)



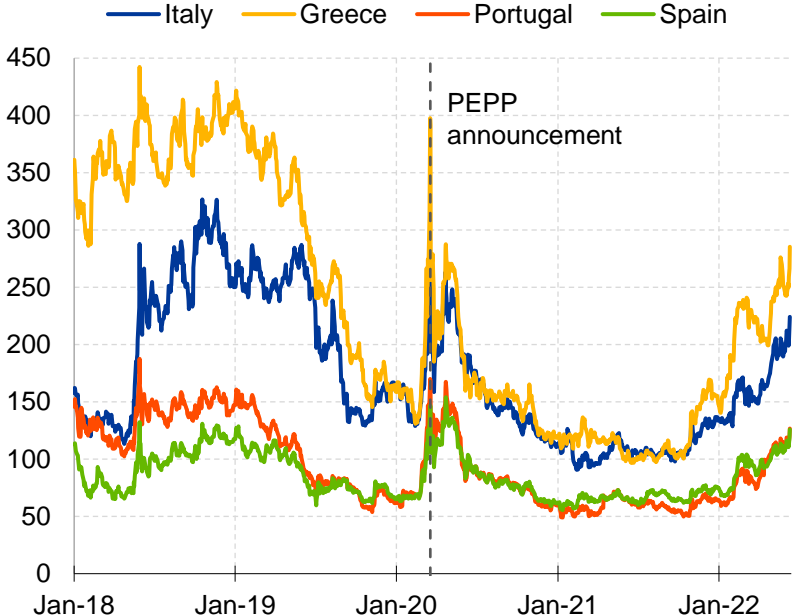
Sources: European Commission, ECB calculations.

Notes: High debt economies are countries with a debt-to-GDP ratio exceeding 90% in 2019; Interest rate shock assumes permanently higher interest rates by 1pp across countries and maturities; Potential growth shock assumes potential growth lower by 1 percentage point for 3 years, implying permanently lower potential output levels.

Sovereign spreads widen at accelerating speed amid global policy normalisation

Sovereign bond spreads

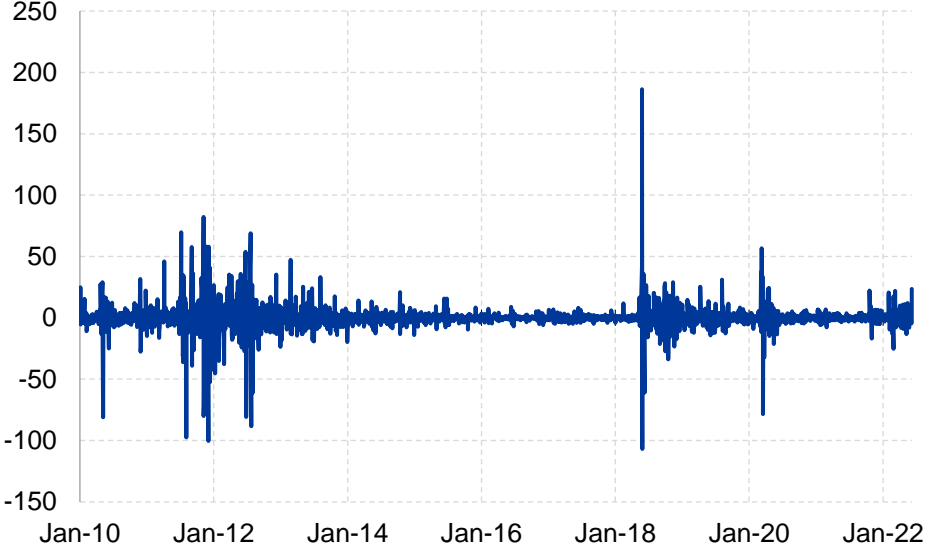
(basis points)



Source: Bloomberg.
Latest observation: 10 June 2022.
Note: The spreads show the difference between the 10Y sovereign bonds and the 10Y German government bond.

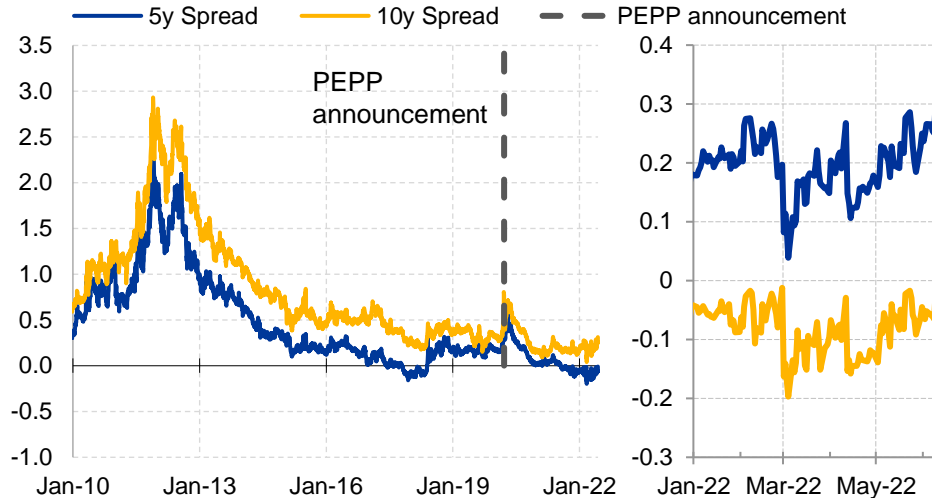
Daily change of 2-year Italian sovereign bond yield

(basis points)



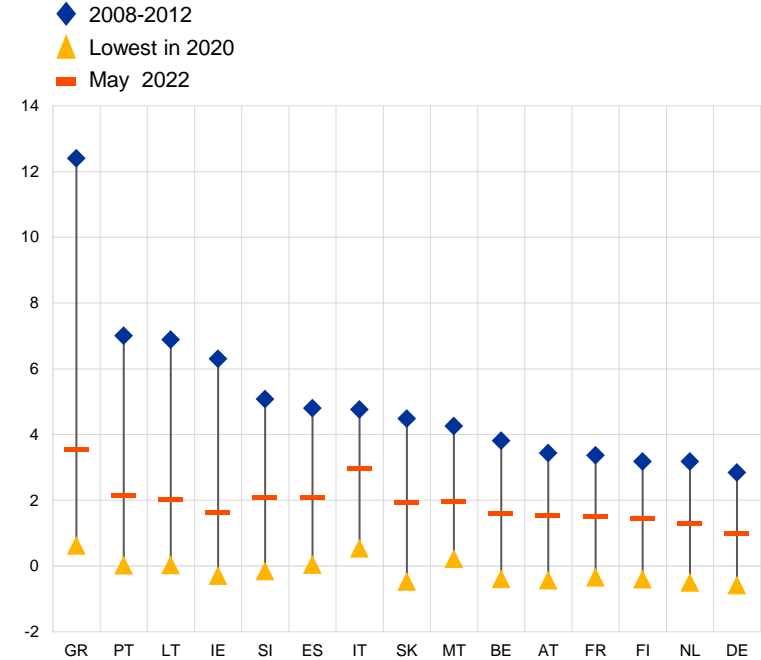
Source: Bloomberg.
Latest observation: 10 June 2022.

5-year and 10-year euro area GDP-weighted yield over the equivalent OIS rate (percentage points)



Source: SDW.
 Latest observation: 10 June 2022.
 Note: ESTR OIS mid of bid and ask is used, before 10/10/2019 EONIA OIS-8.5bps is used.

Sovereign bond 10-year yields (percent, average over period)



Source: ECB Financial Markets database.
 Notes: 'Lowest in 2020' displays the lowest average monthly sovereign bond 10-year yield in 2020. Countries are ranked according to the 2008-2012 average monthly sovereign 10-year yield.

Thank you for your attention!