

**FAZ**

31 October 2016

## **Follow the Fed's plucky example**

*by Michael Heise*

The European Central Bank (ECB) will soon have to decide how to proceed with its bumper asset-purchasing program. It has already extended its purchases until March 2017 and upped the monthly volume to EUR 80bn. But what happens from next March? So far there have been no commitments in this regard nor is there any relevant experience in the eurozone.

US monetary policy could provide some guidance. In 2013 the Fed gradually abandoned its unconventional monetary policy. In the second quarter of that year, Ben Bernanke, Fed chairman at the time, dropped the first hints of a reduction in bond purchases. The financial markets took fright and asset prices plummeted. Up to mid-August 2013 US Treasuries tumbled by around 6.5%, with yields rising accordingly. But after only a few months the kerfuffle was over. Monthly purchases were wrapped up at the end of 2014, yields were back at low levels.

The same is likely to happen here too when the ECB one day announces that it would be buying fewer assets. Security prices will fall because the markets are likely to be miffed by the withdrawal of liquidity injections. But with ongoing moderate economic growth and low inflation the initial turmoil will swiftly fade again.

With business expectations currently upbeat, the ECB should start reining in its bond purchases from March 2017. In line with the US model, it could announce its intention to reduce purchases by EUR 10bn from meeting to meeting, with the result that no new bond holdings would be accumulated after around 10 months. The ECB will wish to preserve flexibility in the course of the exit process. But this needs to apply in both directions. Should inflation rise more swiftly than forecast by the ECB and market watchers, bond purchases would need to be reduced more quickly.

There is little point in delaying the exit any longer. Low, in some cases indeed negative, capital market rates are not helping the economy, but are in fact prompting savers to put even more aside, and are tearing huge holes in company pension schemes and forcing investors into more crowded and riskier financial segments. And hopes that governments are using the low interest rate environment to reduce their debt are also illusory. Quite the opposite: consolidation zeal is waning because savings are already being made on interest payments. And the soft euro, which goes hand-in-hand with the expansionary policy and gives eurozone countries a price advantage, also allows governments to put off growth-enhancing reforms. By returning policy to normal the ECB could lend considerable weight to its ever louder calls for structural reforms.

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