# Euro area heads for slump as Draghi steps down as central bank chief

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The governing council of the European Central Bank (ECB), meeting in Frankfurt on Thursday, has reaffirmed its controversial decision in September to lower the base interest rate further into negative territory and resume its asset purchasing program to the tune of €20 billion a month.

The decision will further expand the ECB's holdings of €2.6 trillion worth of financial assets. It sparked considerable criticism both from within the governing council, leading to the resignation of the German representative, and also from several European central bankers past and present.

Speaking at his final press conference before former International Monetary Fund chief Christine Lagarde takes over next month, outgoing ECB president Mario Draghi noted the support for the policy shift at the governing council meeting, saying there was a "general call" for unity. But it is not clear whether the critics have shifted their position or whether they will resume their opposition when Lagarde takes the reins.

Addressing the decision at the press conference, Draghi said that "unfortunately" everything that had happened since the September meeting showed the need for the ECB to act in the way it had.

In his introductory remarks, he said: "Incoming data since the last governing council meeting in early September confirm our previous assessment of a protracted weakness in euro area growth dynamics, the persistence of prominent downside risks and muted inflation pressures."

The slowdown in growth mainly reflected "the ongoing weakness of international trade in an environment of persistent global uncertainties, which continue to weigh on the euro area manufacturing sector and are dampening investment."

In response to questions, he noted the ECB had been preparing to exit from its expansionary monetary policy in 2017 but conditions had changed since then and the central bank had to shift course.

Draghi was referring to the pronounced downward shift in global economic conditions over the past 18 months. In 2017 the world economy was experiencing an upturn, prompting the view that the world economy was finally recovering from the 2008 financial crisis and central banks could start to "normalise" monetary policy.

The "recovery" proved to be short-lived and by the middle of last year the global economy had entered what the IMF called at its meeting earlier this month a "synchronised" slowdown.

Draghi said the main take-out from the IMF meeting was what he called a shift in the "paradigm of reference." Previously the view had been that interest rates were low and would remain low for some time but that they would go up.

Now the sense was that interest rates would stay low and remain there for a long time.

Commenting directly on the situation in the euro area, he said the latest purchasing managers' index (PMI) for manufacturing—an indicator of future activity—was at its lowest level since 2012. The services sector had continued to hold up but now there were indications that PMIs in this area were starting to turn down.

Data released in advance of the ECB meeting pointed to the worsening economic outlook for Europe. Eurozone inflation fell to its lowest level in almost three years. Prices rose by only 0.8 percent in September from a year earlier, compared to 1 percent for August, and below estimates of a 0.9 percent rise.

The mandate of the ECB is that it should conduct monetary policy with the aim of maintaining inflation at close to 2 percent.

However, as one financial analyst commented to the *Financial Times*: “Almost every time Eurostat has published inflation data so far this year, the result has been disappointing for the ECB.”

France, at 1.1 percent, was the only country among the larger member states to record an inflation rate above 1 percent, while in Germany the inflation rate dropped from 2.2 percent a year ago to 0.9 percent.

The euro area is being heavily impacted by the slowdown in global trade. Figures released on Wednesday showed eurozone exports to the rest of the world fell in August by 2.2 percent compared to a year ago, while intra-eurozone exports were down by 5.5 percent. International trade was hit by the 5.7 percent fall in exports of machinery and transport equipment, reflecting the contraction of global investment.

Earlier this week, Germany’s central bank warned that the country’s economy may have contracted in the third quarter, following a decline of 0.1 percent in the June, putting it at risk of a technical recession, defined as two consecutive quarters of negative growth.

The Bundesbank said while a recession “in the sense of a clear broad-based decline” with underutilised capacity “had not yet been apparent,” the export-oriented manufacturing industry “continued to weaken” in the third quarter. Car production was “greatly reduced” in July and August while production of intermediate and consumer goods “fell sharply.”

Other reports on the German and eurozone economy indicate the same trends.

A report from the survey firm IHS Markit said that, according to its composite index covering manufacturing and services, employment levels in Germany had contracted this month for the first time in six years.

Speaking on the overall situation in the eurozone, the firm’s chief business economist, Chris Williamson, said the composite index showed the eurozone economy grew by only 0.1 percent in the September quarter, down from the 0.2 percent in the second quarter and well below trend levels.

“The eurozone economy started the fourth quarter mired close to stagnation, with the flash PMI pointing to a quarterly GDP growth rate of just under 1 percent. The manufacturing downturn remains the fiercest since 2012 and continues to infect the service sector, where October saw the smallest increase in new work for almost five years,” he said.

Williamson said the labour market was being hit as firms retrenched amid signs of excess capacity and a continued decline in jobs growth. This would add to risks that the trade-led downturn could spread to the household sector and further dampen growth by the end of the year.

“The survey indicates that Mario Draghi’s tenure at the helm of the ECB ends on a note of near-stalled GDP, slower jobs growth, near-stagnant prices and growing pessimism about the outlook, piling pressure on Christine Lagarde to drive new solutions to the eurozone’s renewed malaise.”

Draghi, once described by *New York Times* economics columnist Paul Krugman as arguably the “greatest central banker of modern times,” is leaving his presidency of the ECB hailed as the man who “saved the euro” with his pledge in 2012 to do “whatever it takes.” What that meant in practice was a massive bailout of the banks, paid for through austerity policies imposed on the European working class, above all in Greece, where living standards and social conditions were reduced to levels not seen since the 1930s.

As for the so-called “unconventional monetary policies” he espoused and implemented, together with other major central bankers, the record shows that they have failed to bring any real economic revival and only created the conditions for a renewed economic and financial crisis.