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ECB: REMOVING FURTHER STOPS

Berenberg Macro Flash

Pandemic update: The virus continues to spread rapidly on both sides of the Atlantic. In Europe, the total number of confirmed infections has risen by 27% within two days to 245k as of the morning of 26 March. This follows slightly faster increases of 28% between 23 and 25 March and 41% between 20 and 22 March, according to the [Johns Hopkins University](#). From a lower level, the US is following Europe with a 49% surge in the last two days to 69k (after 57% between 23 and 25 March and 88% in the two days to 22 March).

Whatever it takes: The European Central Bank last night removed some of the remaining stops, granting itself significantly more freedom to deploy its [additional €750bn asset purchases](#) in the most effective way. The move further strengthens our conviction that the ECB can and will ensure financial stability and contain the tail risk of any debt crisis in the face of an extreme health emergency.

ECB: MAXIMUM FLEXIBILITY FOR ASSET PURCHASES

In a [legal decision](#) providing details of its new temporary Pandemic Emergency Purchase Programme (PEPP), the ECB last night broke new ground. Clarifying that the PEPP's objectives are different from those of its other purchase programmes, the ECB announced a "high degree of flexibility in its design and implementation".

Key elements:

- the 33% limit on the share of a Eurozone member state's outstanding bonds which applies to the ECB's public sector purchase programme (PSPP) does NOT apply to the PEPP;
- the ECB can purchase shorter maturities than under its current programmes and therefore debt across the yield curve (under OMT the ECB can buy the 1-3 years maturities while under PSPP it can make purchases of debt instruments with maturities from 1-31 years);
- Greek bonds are eligible for purchases;
- the ECB will accept the so-called "pari passu" pledge and thus the same treatment as other investors in a hypothetical debt restructuring.

The ECB did not lift the "capital key" rule, that is the requirement to distribute bond purchases between member countries over time roughly according to their share in ECB capital. However, the ECB stressed that "a flexible approach to the composition of purchases under the PEPP is nonetheless essential".

The ECB's new purchase programme is now significantly more flexible than its standard programme. As the ECB had already emphasized on 18 March it can be scaled up if required.

The unprecedented ECB response to the pandemic further helps governments to prevent the severe liquidity crunch in the real economy from turning into a dangerous credit crunch. By deploying an instrument better suited to cope with the current shock, it reduces slightly the need that



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the ECB might also have to deploy its OMT programme, that is the „whatever it takes“ tool it had designed in 2012 to stop the euro crisis. The ECB can now lend even more support to hard-hit countries such as Italy without the stigma that an early use of the OMT tool may have implied. Of course, activating the OMT programme once a country has asked for and been granted support from the European Stability Mechanism (ESM) remains a powerful additional option.

While the Eurogroup of finance ministers dithers, shying away from sending an impressive signal of solidarity on Tuesday evening, the ECB continues to deliver. This shows once again that, once it comes to actions of a seriously impressive scale in the Eurozone, the ECB is the only institution capable of that, at least so far. Let us hope that EU leaders on their video summit today do better. Even after the ECB response, a decision for [corona bonds along the lines some observers including us](#) have proposed would still be a most valuable signal of solidarity within the Eurozone. If there ever was a time to send such a signal, it is now.

Incidentally, the ECB published its legal decision right after former President Mario Draghi had weighed in with a rare [intervention](#) that now should not be the time to worry about rising public debt levels. He stressed that the “The cost of hesitation may be irreversible. The memory of the sufferings of Europeans in the 1920s is enough of a cautionary tale.” In his own memorable words, Draghi thus emphasised one of our key political points, namely that the way in which Europe does or does not rise to the current challenge will shape attitudes to European integration for a long time to come, for better or worse.

For our overall take on the economic impact of the pandemic, see [macro essentials](#) and [preventing a credit crunch](#).

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