



Leibniz Institute for Financial Research SAFE  
Sustainable Architecture for Finance in Europe (<https://safe-frankfurt.de/>)

## SAFE Finance Blog

### What Effect would an Extension of ECB's Asset Purchase Program Have?

04/28/2017

Jan Pieter Krahenen warns about negative outcome on investments



After the meeting of the ECB Governing Council on 27 April, President Mario Draghi stated that the ECB would be prepared to expand its asset purchase program (APP) in volume and towards additional asset classes if the economic outlook becomes gloomy again. This statement comes at a time when the Eurozone economy is taking up speed again and, over the last months, a persistent trend in core inflation is not discernible.

Among economists however, there is quite a lot of skepticism that the policy of quantitative easing would sustain or even increase its impact on market liquidity and credit supply. According to Jan Pieter Krahenen (<https://safe-frankfurt.de/research/researchers/researchers-details/showauthor/14-krahenen.html>), Director

of SAFE, the ECB's officials should take into account that an extension of the APP may actually have the opposite effect than expected: "By fostering market expectations towards unsustainable debt burden of states and financial institutions, the induced reduction in the level of interest rates may lead to lower investment levels rather than higher ones." Krahen assumes that market participants will postpone their investments if they interpret the ECB's action as a reaction to a poor and gloomy economic situation. "The macroeconomic investment curve may actually be backward bending, rather than simply monotonically rising", Krahen states. In this "backward bending" scenario, an extension of the APP as a response to a poor economic outlook would exacerbate the negative investment trend.

Given this view, which effect would a – currently not foreseeable – revision of the ECB's present course of monetary policy have? "A signal of the ECB's officials to start exiting easy-money policy might even have a positive impact on investments", Krahen states. "However one has to take into account", he reminds, "that the APP is not targeted to stimulate growth as, in general, it is not the ECB's task to boost growth but to manage inflation."

The question of how the euro area's economic growth would respond to an increase of the ECB's APP if the economic outlook became less favorable was also subject to a recent survey of the European IGM Economic Experts Panel (<http://www.igmchicago.org/surveys/ecb-asset-purchases>) (University of Chicago Booth). The panel displays the uncertainty among European economists about the success of an APP extension. Merely 16 percent of the 50 panelists said that they expect an extension of the APP to substantially increase the euro area's economic growth over the following five years. 18 percent, among them Jan Pieter Krahen, believe the opposite and 42 percent are uncertain. The European IGM Economic Experts Panel explores the views of distinguished European economists on vital public policy issues on a regular basis.


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