ECONSTOR
Make Your Publications Visible.

A Service of
ZBW
Leibniz-Informationszentrum Wirtschaft
Leibniz Information Centre for Economics

Siekmann, Helmut; Wieland, Volker

Working Paper

The ruling of the Federal Constitutional Court concerning the public sector purchase program: A practical way forward

IMFS Working Paper Series, No. 140

Provided in Cooperation with:
Institute for Monetary and Financial Stability (IMFS), Goethe University Frankfurt am Main

Suggested Citation: Siekmann, Helmut; Wieland, Volker (2020) : The ruling of the Federal Constitutional Court concerning the public sector purchase program: A practical way forward, IMFS Working Paper Series, No. 140, Goethe University Frankfurt, Institute for Monetary and Financial Stability (IMFS), Frankfurt a. M., https://nbn-resolving.de/urn:nbn:de:hebis:30:3-542710

This Version is available at:
https://hdl.handle.net/10419/217232

Standard-Nutzungsbedingungen:

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

Terms of use:

Documents in EconStor may be saved and copied for your personal and scholarly purposes.

You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.

WWW.ECONSTOR.EU

Mitglied der Leibniz-Gemeinschaft

HELMUT SIEKMANN
VOLKER WIELAND

The Ruling of the Federal Constitutional Court concerning the Public Sector Purchase Program: A Practical Way Forward

Institute for Monetary and Financial Stability
GOETHE UNIVERSITY FRANKFURT

WORKING PAPER SERIES NO. 140 (2020)

This Working Paper is issued under the auspices of the Institute for Monetary and Financial Stability (IMFS). Any opinions expressed here are those of the author(s) and not those of the IMFS. Research disseminated by the IMFS may include views on policy, but the IMFS itself takes no institutional policy positions.

The IMFS aims at raising public awareness of the importance of monetary and financial stability. Its main objective is the implementation of the "Project Monetary and Financial Stability" that is supported by the Foundation of Monetary and Financial Stability. The foundation was established on January 1, 2002 by federal law. Its endowment funds come from the sale of 1 DM gold coins in 2001 that were issued at the occasion of the euro cash introduction in memory of the D-Mark.

The IMFS Working Papers often represent preliminary or incomplete work, circulated to encourage discussion and comment. Citation and use of such a paper should take account of its provisional character.

Institute for Monetary and Financial Stability
Goethe University Frankfurt
House of Finance
Theodor-W.-Adorno-Platz 3
D-60629 Frankfurt am Main
www.imfs-frankfurt.de | info@imfs-frankfurt.de

The Ruling of the German Federal Constitutional Court concerning the Public Sector Purchase Program of the European Central Bank: A Practical Way Forward

Helmut Siekmann and Volker Wieland

Institute for Monetary and Financial Stability

Goethe University Frankfurt

8 May 2020

Abstract

This paper summarizes key elements of the German Federal Constitutional Court's decision on the European Central Bank's Public Sector Asset Purchase Programme. It briefly explains how it is possible for the German Court to disagree with the ruling of the Court of Justice of the European Union. Finally, it makes suggestions concerning a practical way forward for the Governing Council of the European Central Bank in light of these developments.

Siekmann: siekmann@imfs-frankfurt.de, Goethe University Distinguished Professor of Money, Currency and Central Bank Law; Wieland: wieland@imfs-frankfurt.de, IMFS Endowed Chair of Monetary Economics, Institute for Monetary and Financial Stability, Goethe-Universität Frankfurt, House of Finance, Theodor-W.-Adorno-Platz 3, 60323 Frankfurt am Main.

Introduction

On 5 May 2020, the German Federal Constitutional Court (GFCC) pronounced a seminal decision which might jar the very foundations of the judicial set-up of the European Union (EU). In effect, it partially contradicts a judgment of the Court of Justice of the European Union (CJEU). By doing so, it might result in shockwaves to the whole architecture of the Union, which is basically a legal construct.

The judgment concerns the Public Sector Purchase Programme (PSPP) of the European Central Bank (ECB), which was started in March 2015 and is still ongoing. The Court's decision concludes a long judicial process following constitutional complaints of several groups of citizens. This process involved the GFCC submitting a number of questions to the CJEU, which pronounced its judgment on those questions on 11 December 2018. The GFCC then held a public oral hearing on July 30th and 31st of 2019. Now, it has pronounced its final ruling.

First, it is important to notice that the GFCC emphasizes up front in its press release that the decision published on 5 May 2020 does not concern financial assistance measures taken by the European Union or the ECB in the context of the current coronavirus crisis, e.g. the Pandemic Emergency Purchase Programme (PEPP). Thus, it does not intend to interfere directly with measures taken to mitigate the economic recession caused by the coronavirus pandemic. The program concerned, that is the PSPP, has been running for many years and resulted in a large increase of government debt holdings by the European System of Central Banks (ESCB) during the years prior to this crisis when economic activity was close to potential output as estimated by the European Commission, and inflation was not far below the numerical objective defined by the European Central Bank. Even so, this ruling might indicate how the Court may decide on possible future complaints about other ongoing programmes.

The purpose of this paper is to explain how the GFCC comes to decide differently than the CJEU on a matter of EU law by employing its "*ultra vires*" approach. While this paper does not aim to contribute directly to the scholarly debate on this approach, it rather explains the judgment of the GFCC including its implications for the German authorities and proceeds to make some suggestions on a practical way forward for the Governing Council of the European Central Bank.

The sentence

In its final judgment on the Public Sector Purchase Program of the ECB, the Court found that the Federal Government of Germany and the German Bundestag violated the complainants' rights under Article 38(1) first sentence in conjunction with Article 20(1) and (2), and Article 79(3) of the German Federal Constitution, the Basic Law (*Grundgesetz* – GG). In the Court's opinion, the German authorities failed to question the lack of an examination of the proportionality of the PSPP by the ECB. The GFCC states that the German authorities also bear responsibility for the process of European integration, and therefore ought to take steps to ensure that the principle of proportionality be observed. This principle is fundamental in delineating the competences of the authorities of the EU. Specifically, the Court argues that the decisions of the ECB, that is, the statements explaining the decisions of the Governing Council, failed to include an assessment and substantiation of the proportionality of its measures. The European Court should have included this aspect in its review, but according to the GFCC it did not do so in a convincing manner.

How can the German Court decide on a question of EU Law? The *Ultra Vires* Approach

Since it is the exclusive competence of the European Court to control the compatibility of acts of institutions and organs of the EU with the law of the EU, the German Court had to invoke the *ultra vires* control developed in a long series of prior decisions. By creating this instrument, the GFCC has reserved the right to control whether a European institution has transgressed its competences; but limited to *manifest* and *structurally significant* infractions. Now, it identifies such a severe and manifest act in the context of the PSPP. Thus, by its nature, the *ultra vires* approach requires that the German Court expresses its evaluation of the deficits of the European Courts' judgment in stark terms. Otherwise, the German Court would not be consistent with its persistently stated cooperative and pro-European basic attitude.

In several preceding decisions, the German Court had clearly expressed that – despite its repeated acknowledgment of the priority of the European Court and its keen desire to solve controversies in a truly cooperative manner with mutual respect (BVerfGE 140, 317 (338 margin-no 44) – it reserves the right to have the "last word" in extreme cases; mainly when the acts in question would in effect imply an extension of competences which is reserved to the

amending procedures. With its judgment of 5 May the GFCC has activated this reservation for the *first time*. In this respect, it is a genuinely seminal legal event in the course of the European Communities and Union.

The GFCC qualifies the CJEU's judgment of 11 December 2018 of the CJEU, which considered the PSPP appropriate and proportional in its response to the GFCC request for a preliminary ruling, as *not understandable*; to this extent, it assesses the CJEU judgment also *ultra vires*. Regarding the proportionality of the ECB's decision, the CJEU's judgment had simply stated "It is *clear* that the ESCB weighed up the various interests involved so as to actually prevent disadvantages which are *manifestly* disproportionate to the PSPP's objective from arising on implementation of the programme." The response of the GFCC is – phrased in simple terms – how can this be clear if the ECB Governing Council has not weighed up the benefits and drawbacks in its own decisions as they are published in the form of Council statements. The argument proceeds as follows:

- While the CJEU considered the programme "within the ambit of the ECB's competences", the GFCC expressed the opinion that the CJEU's approach "manifestly fails to give consideration to the importance and scope of the principle of proportionality which applies to the division of competences between the European Union and the Member States – and is simply untenable from a methodological perspective given that it completely disregards the actual economic policy effects of the programme."

- The main deficit is seen in that the CJEU refrains from conducting an overall assessment and appraisal concerning the actual effects of the PSPP on economic policy and the principle of proportionality. To the German Court's opinion, it does not satisfy the requirements of a complete and understandable review as to whether the European System of Central Banks (ESCB) and the ECB observe the limits of their monetary policy mandate. This way the *principle of conferral* (Art. 5(1) first sentence and Art. 5(2) TEU), which guarantees that the EU acts only within the limits of the competences that EU Member States have conferred upon it in the Treaties, would be rendered meaningless.

- Furthermore, the GFCC criticizes that the CJEU restricts its judicial control to "manifest" errors in the ECB's assessment of benefits and damages or to the ECB

manifestly exceeding what is necessary to achieve its goals. This way, the legal rules on the distribution of competences, namely the confinement of the ESCB to *monetary policy*, would in effect run *void*.

The judicial review of proportionality by the German Court

On the basis of these arguments, the German Court concludes that it is its task to control the compatibility of the acts of the ECB in regard of the PSPP with EU law. The GFCC states that the ECB has failed to conduct the necessary balancing of the monetary policy objective against the potentially negative side effects in areas of economic policy arising from the programme: "Therefore, the decisions at issue violate Art. 5(1) second sentence and Art. 5(4) TEU and, in consequence, exceed the monetary policy mandate of the ECB."

Specifically, it is admonished that the direct consequences of the programme are not captured sufficiently and aptly weighed against the aspired benefits. In particular, the GFCC refers to the easing effect on the refinancing conditions of the Member States. Thereby, the PSPP has important effects on fiscal conditions in Member States that can be compared to financial support measures pursuant to Art. 12 et seq. ESM Treaty. The GFCC concludes that the CJEU is handling the delineation between (general) economic policy pursuant Art. 119 and 127 TFEU in an inconsistent manner. Whereas in the *Pringle* case it advocated a narrow interpretation of monetary policy in order to be able to uphold the establishment of the European support mechanism as economic policy, it advocates a very wide interpretation of the same term in *Gauweiler* (on OMT) and *Heinrich Weiss* (on PSPP) to justify these programmes as monetary policy. Even more, in the latter case it almost completely refrained from any control.

Other considerations of proportionality raised by the GFCC concern the consequences of the government bond purchases for the economic situation of banks and the economic and social impact on citizens. It notes that virtually all citizens are at least indirectly affected, *inter alia* as shareholders, tenants, real estate owners, savers or insurance policy holders. For instance, there is the risk of considerable losses for private savings. Furthermore, by lowering the general level of interest rates, the programme may keep companies in business that would otherwise not be viable. Finally, it is pointed out that the longer the programme continues and the more its total volume increases, the greater the risk that the Eurosystem becomes dependent on Member State

politics as it can no longer simply terminate and undo the programme without jeopardising the stability of the monetary union.

The German Court argues that the ECB should have weighed these and other economic policy effects against the predicted advantages in achieving its monetary policy objective. Without documentation whether and how this balancing was done, the lawful pursuit of the mandate cannot be effectively controlled by the courts.

The question of the prohibition of monetary financing and other concerns

The GFCC repeated its "considerable" concerns that PSPP may be circumventing the prohibition of monetary financing of government debt pursuant Art. 123(1) TFEU. In particular, it did not see the necessary closer scrutiny of the "safeguards" developed in the *Gauweiler* Judgment by the CJEU. Nevertheless, the GFCC accepted insofar the assessment of the PSPP by the European Court since a "manifest" violation of Art. 123(1) TFEU could not be ascertained. The main reasons why the GFCC concludes that PSPP does not violate the prohibition of monetary financing are listed as follows:

- The volume of the purchases is limited in advance;
- Only aggregate information on the purchases carried out by the Eurosystem is published;
- A purchase limit of 33% per international securities identification number (ISIN) is observed;
- Purchases are carried out according to the ECB's capital key;
- Bonds of public authorities may only be purchased if the issuer has a minimum credit quality assessment that provides access to the bond markets; and
- Purchases must be restricted or discontinued, and purchased securities sold on the markets, if continuing the intervention on the markets is no longer necessary to achieve the inflation target.

Even if the GFCC did not see an *ultra vires* act in this regard at present, these caveats are of importance for other programmes that might possibly relax some of these conditions. The

statements of the Court suggest that these features could play a key role in future Court cases regarding those programmes.

Another issue discussed in prior decisions was a possible violation of the constitutional identity of the Basic Law, the German Federal Constitution. In its recent judicature, the GFCC has differentiated this aspect from the *ultra vires* control discussed above. In particular, it attributed a significant role to the question of overall budgetary responsibility of the German *Bundestag* in the context of the legal assessment of the asset purchase programmes of the ESCB. The GFCC reiterated that the limits set by the overall budgetary responsibility of the German *Bundestag* could be affected by aspects of the bond purchases under the PSPP and the risk-sharing regime, for example, if the risk-sharing regime would be subject to (retroactive) changes. It concludes that the PSPP does not transgress these constitutional limits at this time but might consider a change "impermissible".

Implications for the German institutions

The GFCC had already made clear in earlier decisions that the German constitutional organs, administrative authorities and courts would break the law if they participated in the development, implementation, execution or operationalisation of *ultra vires* measures. Moreover, they would even have to "work towards the rescission of acts not covered by the integration agenda. This would especially affect the *Deutsche Bundesbank* as an integral part of the Eurosystem. Concretely, the GFCC states that the Deutsche Bundesbank may not continue to participate in the PSPP programme unless the ESCB provides an assessment that the monetary policy goals it aims to achieve with the PSPP are in proportion to the consequences this programme has for economic and fiscal policies. A deadline of three months is set in this regard. Furthermore, the Bundesbank is obliged to work towards a reduction of the government debt holdings in the long term and in coordination with the Eurosystem.

Thus, the GFCC did not yet definitely determine whether the German Federal Government and the *Bundestag* did actually violate their responsibility with regard to European integration. As a consequence, it did not yet grant the statement the complainants had petitioned for: that the failure to actively advocate for the termination of the PSPP was an infraction of a constitutional obligation. The Court made it contingent upon the – so far lacking – proportionality assessment

by the ECB Governing Council. To the opinion of the GFCC it would be up to the Governing Council to mitigate the legal dispute. It could still mend the admonished deficits by delivering a proportionality assessment that also addresses the issues raised by the Court. In effect, the final assessment whether the PSPP, in substance, is compatible with the delineation of the ESCB's competences in Art. 127(1) TFEU has been partially deferred.

The required assessment would have to demonstrate in a "substantiated and comprehensible manner" the ECB Governing Council's weighing of the considerable economic policy effects and balance them, based on proportionality considerations, against the expected positive contributions of the PSPP towards achieving its monetary policy objectives.

What Next? The Potential for Conflict

One option for the Governing Council of the ECB is to ignore the ruling of the German Court. It could take the position that as an EU Institution it is subject to EU law and that judicial control regarding its adherence to EU law is exercised by the CJEU. Thus, it could refer to the judgment of the CJEU concerning the questions the GFCC had conferred to the CJEU, and underline that the CJEU had not seen any need for further justifications by the ECB. It might even argue that in order to protect its institutional independence enshrined in Art 130 TFEU, it would need to ignore such interference. EU law states that "neither the European Central Bank, nor a national central bank, nor any member of their decision-making bodies shall seek or take instructions from Union institutions, bodies, offices or agencies, from any government of a Member State or from any other body."

In the meantime, the *Deutsche Bundesbank* would not be allowed to continue with its sovereign debt purchases. However, the primary law of the EU considers it as an integral part of the ESCB and demands that all national central banks shall act in accordance with the guidelines and instructions of the ECB, Art. 14.3 Sentence 1 Statute of the ESCB and ECB. Moreover, Sentence 2 states that the Governing Council shall take the necessary steps to ensure compliance with the guidelines and instructions of the ECB, and shall require that any necessary information be given to it. As a result, the Governing Council would have the power to demand full compliance from the *Deutsche Bundesbank*.

In case of conflict, a special judicial procedure is foreseen in Art. 271 lit. d. TFEU. The CJEU is explicitly given jurisdiction in disputes concerning "(d) the fulfilment by national central banks of obligations under the Treaties and the Statute of the ESCB and of the ECB. In this connection the powers of the Governing Council of the European Central Bank in respect of national central banks shall be the same as those conferred upon the Commission in respect of Member States by Article 258. If the Court finds that a national central bank has failed to fulfil an obligation under the Treaties, that bank shall be required to take the necessary measures to comply with the judgment of the Court."

If the required actions were not compatible with German constitutional law, an open conflict between the Courts would arise. This may well have many very negative consequences which bears asking the question: Is there no other way?

A Practical Way Forward

The final judgment of the GFCC on the PSPP does not come as a total surprise. The Court has expressed its legal concerns in prior decisions. Granted, the *ultra vires* approach that the Court has developed is discussed controversially in the German legal literature. In the context of this academic debate, the admissibility of these constitutional complaints could be questioned with good reasons, but there are respectable arguments in favour of the merits of the case. However, with this paper we do not aim to contribute to this academic debate but rather propose a practical way forward for the Governing Council of the European Central Bank.

First, Art 130 TFEU protects the independence of the ECB and ECSB "when exercising the powers and carrying out the tasks and duties conferred upon them by the Treaties and the Statute of the ESCB and of the ECB". It does not protect the ECB from judicial control that certainly extends to the proportionality of its actions. The argument is about whether the GFCC's role of as guardian of a Member State's constitution allows it to make judgments in this regard. The GFCC's view is that "if the Member States were to completely refrain from conducting any kind of *ultra vires* review, they would grant EU organs exclusive authority over the Treaties even in cases where the EU adopts a legal interpretation that would essentially amount to a treaty amendment or an expansion of its competences". Thus, it is a judicial conflict between the European and Member State Courts.

The Governing Council of the European Central Bank would be well advised, in our view, to side-step the issue of the conflict between the GFCC and the CJEU. Rather, it could consider the option of explicitly discussing proportionality in the published statements that announce the Council decisions on its own merits.

In fact, the Governing Council is already evaluating its monetary policy strategy including all aspects of communication in the *ongoing Strategy Review*. This review has been launched and publicly announced by the Governing Council on 23 January 2020. Furthermore, as stated by ECB President *Christine Lagarde*, this review includes soliciting a wide range of views from European citizens. At the start of the Questions and Answers segment of her first ECB press conference on 12 December 2019, she explained: "The strategic review, it will be reaching out to not just the usual suspects, but it will also include consulting with Members of Parliament and I've committed to that with the European Parliament. It will reach out to the academic community, of course. It will *reach out to civil society representatives* and it will aim at *not just preaching the gospel* that we think we master, *but also listening* to the views of those to whom we reach out."

The judges of constitutional courts are members of civil society. More importantly in this case, the role of the GFCC is to address constitutional complaints by citizens. Thus, there is ample reason for the ECB to listen and take these complaints into account in its strategy review.

Furthermore, an evaluation of the cost and benefits of policy measures deployed to achieve the objectives of the ECB is a natural part of a broad review of the policy strategy. It actually forms the basis for checking whether there is a need to change the strategy, and to change how different policy instruments are used within this strategy. As the ECB strategy review also covers the communication of its strategy and particular policy decisions, it would be natural to explore how the ECB Governing Council could communicate on the costs and benefits and the trade-offs involved in its regular policy statements.

As mentioned by President *Lagarde* in her remarks at the December 2019 press conference, such strategy reviews have also been carried out by other central banks. Thus, a feature of the review could be to take a look at practices of other central banks in terms of communicating the proportionality of their measures within their policy statements and reports.

By making the question of proportionality part of its strategy review, the Governing Council could discuss all issues involved in an open and effective manner. In this context, it could consider making a check of proportionality part of its strategy and regular policy statements. To this end, it may be useful to explore whether there exist already elements of the strategy that can play a role in such a check of proportionality. Furthermore, there would be room to consider whether elements of other central banks' strategies could help conducting and communicating such an *explicit proportionality check*. Checking proportionality involves evaluating trade-offs. Specifically, the question is how effectively certain policy instruments and measures contribute to the main objective of the central bank, what – and if which – negative side effects they may have, and what any trade-offs look like.

In the following, we list some examples of strategy elements that, in our view, would be worth closer inspection in this regard. In this paper, we keep this part brief and postpone further, more detailed analysis of such examples to follow-up work.

The medium-term. A key element of the strategy that the ECB has developed itself at the start of monetary union is that the inflation objective is to be reached only in the medium term. Embedded in this view is the idea of a possible trade-off at certain times between achieving the inflation objective and mitigating fluctuations in economic activity and employment. The ECB does not need to do everything within its power at a given moment in time to achieve the numerical inflation objective as soon as possible if this would negatively affect economic activity. Instead, it simply pursues the inflation objective over the medium term. Such consideration could be extended to the type of negative side effects of certain policy measures that are alluded to by the GFCC judgment and others. For example, often discussed side-effects of long periods of very low, long-term interest rates include the potential for risks to financial stability. This includes greater interest rate risk on bank balance sheets or increased risk of reversals of asset price booms. There are different views on how to best handle that, whether by adjusting monetary policy or macro-prudential policy. The Governing Council could include such balancing of costs and benefits in a proportionality check. This applies in particular to asset purchase programs because they are instrumental in lowering long-term interest rates by dampening term and risk premia.

The monetary pillar. The ECB strategy is unique in that it distinguishes two types of analysis by the Governing Council in its deliberations. Its economic analysis looks at short- to medium-

term determinants of price stability. The monetary analysis cross-checks these findings against the long-run link between money and prices. In the years prior to the financial crisis, the ECB made use of a quantitative reference value for broad money growth. This check may also serve to take into account risks to financial stability that emanate from excessive growth of credit, which is the flip-side of money. In a set of press interviews on 18 July 2008, the then-ECB President Trichet credited the monetary pillar for triggering the 2005 tightening of policy in response to the credit boom that eventually culminated in the global financial crisis of 2008/2009. He said, "When we raised interest rates in December 2005, (…) we did it, because our monetary analysis strongly suggested that we should". Nevertheless, the reference value fell into disuse. The ECB could re-emphasize the monetary pillar and reference values in the context of an explicit proportionality check. In particular, this could be relevant to possible risks for long-term financial stability due to lasting ECB balance sheet expansion. Interestingly, broad money growth has been moderate in recent years.

Policy rules. Policy rules provide a very natural way for assessing the proportionality of policy measures including the decision when and how much to resort to large-scale asset purchases. Such rules link the policy instrument, for example the level of the short-term central bank rate, to economic conditions and deviations from policy objectives. Response coefficients in such rules or reaction functions implicitly embody already an assessment of the costs and benefits of the magnitude of policy reactions. Macroeconomists at central banks and elsewhere regularly evaluate the performance of such rules on the basis of macroeconomic models and historical experience. For a few years now, the U.S. Federal Reserve has published a menu of interest rate rules in its regular monetary policy reports. Whenever they decline into negative territory, these rules provide a strong signal of the need for large-scale asset purchases. The reason is the existence of cash, which offers a zero-interest alternative to savers and makes it difficult for central banks to drive nominal interest rates far below zero. Instead, asset purchases are typically used in order to boost asset prices and reduce premia. While this can help enhancing demand and raising inflation, it may have side effects that may need checking.

Economic forecasts. Central banks, such as the Bank of Norway or the Bank of Sweden, publish official forecasts of the respective central bank board. They include forecasts of inflation and other macroeconomic and financial aggregates as well as forecasts of the policy instrument, i.e. the anticipated path of the central bank rate. Such forecasts are computed either on the basis of policy rules or policy objective functions that consider trade-offs and cost and

benefits from such policy paths. Such forecasts can also be used to balance the benefits from policy measures with potential costs in terms of negative side-effects.

Exit strategies. Policy rules as well as official policy forecasts also provide indications when to stop balance sheet expansion and when to reduce balance sheets. Thus, they can help in defining a possible state-dependent exit strategy from asset purchase programmes. Such an exit strategy would induce policy actions, once the crisis that the euro area economy is currently experiencing has subsided, the economy has recovered and price stability has been secured. The judgment of the GFCC calls for reducing sovereign debt holdings at the central bank in the longer run. The U.S. Federal Reserve, for example, has developed such a strategy. It has published its "Balance sheet normalization principles and plans" and acted upon them in a phase when the economy was doing well and inflation was close to its objective.

Fiscal policy effects. Interest rate policy and sovereign debt purchases by central banks in particular have implications for the financing conditions of fiscal authorities. These effects are especially important in a heterogeneous monetary union. The judgment of the GFCC refers to several decisions of the ECB in the context of the PSPP such as capital-weighting of purchases and 33% issue limits to justify its conclusion that the PSPP does not violate the prohibition of monetary financing of sovereign debt. Large-scale sovereign debt purchases by the ECB may have effects similar to the effects of ESM programs or credit lines, in particular, when the purchases deviate far from the above-mentioned constraints and may appear to be *de facto* Outright Monetary Transactions (OMT). This might become an issue with ongoing programmes such as the PEPP at some point in the future. When assessing potential questions of proportionality and how far the ECB is reaching into the domain of fiscal policies of Member States, it may therefore be of interest to recall former ECB President Mario Draghi's statement in the ECB press conference of 4 October 2012: "We view conditionality (of an ESM program) as an essential part of the activation of the OMT. I have made this point since the very beginning. Conditionality will actually have several roles. First of all it will reduce the moral hazard by governments. The second role it will have is that it protects the independence of the ECB. Without conditionality you would certainly have what people call fiscal dominance. With conditionality the independence of the ECB is protected."

Some relevant web links:

The Judgment of the German Federal Constitutional Court

The Judgment of the Court of Justice of the European Union

The ECB's Strategy Review

IMFS WORKING PAPER SERIES

Recent Issues

139 / 2020	Volker Wieland	Verfahren zum Anleihekaufprogramm der EZB
138 / 2020	Francisco Gomes Michael Haliassos Tarun Ramadorai	Household Finance
137 / 2019	Martin Kliem Alexander Meyer-Gohde	(Un)expected Monetary Policy Shocks and Term Premia
136 / 2019	Luc Arrondel Hector Calvo-Pardo Chryssi Giannitsarou Michael Haliassos	Informative Social Interactions
135 / 2019	Tiziana Assenza Alberto Cardaci Domenico Delli Gatti	Perceived wealth, cognitive sophistication and behavioral inattention
134 / 2019	Helmut Siekmann	The Asset Purchase Programmes of the ESCB – an interdisciplinary evaluation
133 / 2019	Josefine Quast Maik H. Wolters	Reliable Real-time Output Gap Estimates Based on a Modified Hamilton Filter
132 / 2019	Galina Potjagailo Maik Wolters	Global Financial Cycles since 1880
131 / 2019	Philipp Lieberknecht Volker Wieland	On the Macroeconomic and Fiscal Effects of the Tax Cuts and Jobs Act
130 / 2019	Eduard Hofert	Regulating Virtual Currencies
129 / 2018	Olga Goldfayn-Frank Johannes Wohlfart	How Do Consumers Adapt to a New Environment in their Economic Forecasting? Evidence from the German Reunification
128 / 2018	Christopher Roth Johannes Wohlfart	How Do Expectations About the Macroeconomy Affect Personal Expectations and Behavior?
127 / 2018	Michael Haliassos Thomas Jansson Yigitcan Karabulut	Financial Literacy Externalities
126 / 2018	Felix Strobel	The Government Spending Multiplier, Fiscal Stress and the Zero Lower Bound

125 / 2018	Alexander Meyer-Gohde Daniel Neuhoff	Generalized Exogenous Processes in DSGE: A Bayesian Approach
124 / 2018	Athanasios Orphanides	The Boundaries of Central Bank Independence: Lessons from Unconventional Times
123 / 2018	Karl-Heinz Tödter Gerhard Ziebarth	Zinsen, Effektivpreise und Lebenskosten – Ein Beitrag zur Konstruktion eines intertemporalen Preisindex
122 / 2018	Helmut Siekmann	Legal Tender in the Euro Area
121 / 2018	Maik H. Wolters	How the Baby Boomers' Retirement Wave Distorts Model-Based Output Gap Estimates
120 / 2017	Helmut Siekmann	Die Einstandspflicht der Bundesrepublik Deutschland für die Deutsche Bundesbank und die Europäische Zentralbank
119 / 2017	Gregor Boehl	Monetary Policy and Speculative Stock Markets
118 / 2017	Gregor Boehl Thomas Fischer	Can Taxation Predict US Top-Wealth Share Dynamics?
117 / 2017	Tobias H. Tröger	Why MREL Won't Help Much
116 / 2017	Tobias H. Tröger	Too Complex to Work – A Critical Assessment of the Bail-in Tool under the European Bank Recovery and Resolution Regime
115 / 2017	Guenter W. Beck Volker Wieland	How to Normalize Monetary Policy in the Euro Area
114 / 2017	Michael Binder Jorge Quintana Philipp Lieberknecht Volker Wieland	Model Uncertainty in Macroeconomics: On the Implications of Financial Frictions
113 / 2017	Mewael F. Tesfaselassie Maik Wolters	The Impact of Growth on Unemployment in a Low vs. a High Inflation Environment
112 / 2017	Gerhard Rösl Franz Seitz Karl-Heinz Tödter	Doing away with cash? The welfare costs of abolishing cash
111 / 2017	Jinhyuk Yoo	Capital Injection to Banks versus Debt Relief to Households
110 / 2017	Robert C. M. Beyer Volker Wieland	Instability, imprecision and inconsistent use of equilibrium real interest rate estimates