BETTER FINANCE
The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

PRESS RELEASE

Financial Repression | Low ECB Interest Rates & High Inflation generate a Loss of €1 Trillion in Purchasing Power for European Savers in 2022 alone

8 September 2022 | In a late bid to address soaring inflation in the Euro area, the European Central Bank (ECB) increased interest rates for the first time in 11 years in July 2022, raising its main rate to 0 percent after eight years of negative rates, and reaching 0,75% today. Notwithstanding, Eurozone inflation hit a new record high of 9.1% in August, further deepening Europe's cost-of-living crisis.

As inflation continues to hit new records, these timid increases in interest rates seem more like small concessions than effective measures, only slightly deviating policymakers from their overarching policy of 'debt relief through inflation'.

Financial Repression or Debt Relief through Inflation | Since the financial crises of 2008 and 2009, 'Financial Repression' has been the only game in town. With government debt in many cases close to (and in some cases over) 100 per cent of gross domestic product, European governments desperately need to get the lowest interest rates possible. To achieve this, policymakers implement policies to redirect funds to the states' coffers that in a free-market environment would go elsewhere, or would become much more expensive.

By providing financing at negative interest rates in real terms (after inflation) with sovereign bonds as collateral, and having central banks buy sovereign bonds directly on the markets, policymakers create a captive domestic market for government debt.

To complete the picture, inflation is kept alive and eventually unleashed through these "quantitative easing" policies, obliterating the real value of financial savings, since these are for the main part directly or indirectly linked to the level of real interest rates (bank savings, capital guaranteed life insurance, pension funds, bond and money market investment funds, etc.)

A Grey Future for Retirees | These public policy-induced very negative real interest rates represent what economists call "financial repression", since the main designated victims are the long-term savers. Financial Repression also exploits the cognitive bias of "money illusion" - the tendency of people to think of money in nominal, rather than real, terms. Despite posting slightly positive nominal returns, Financial Repression generates comparatively higher price increases. As a result the real value of debts decreases and so does the real value of savings, with net real short-term interest rates now hovering at around minus 8% (nominal ECB rate of 0,75% minus inflation rate of 9,1%), a historical record for many decades.

Research by BETTER FINANCE over the last 10 years has shown that the real returns (after costs and inflation) from private pension funds have been negative in several EU Member States. Add a soaring inflation since 2021 into the equation, and the symbolic interest rate hikes will barely make a difference, with the purchasing power (real value) of EU citizens' savings further plummeting.

European savers are now looking at a real loss of value of about € 1 trillion or more for 2022 alone!

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