

FX Daily: ECB containing EUR risk premium

All eyes on the ECB today, as markets closely watch two aspects of the meeting today. The potential top-up of the PEPP programme and President Lagarde's communication

Scenario analysis: How to position for Lagarde's alternatives

	Inflation outlook	Growth outlook	Interest rate & QE decision	PEPP programme	EUR/USD
<i>Current stance</i>	Over the medium term inflation is expected to increase	"The risks... to growth outlook... are clearly to the downside"	Deposit rate at 0.50%, regular EUR 20bn QE pm & temporary EUR 120bn until year end	An overall envelope of EUR 750 billion until end-2020	
Rise in risk premium	Inflation pick up too slow to bring CPI to the target	Recent data don't suggest a sustained easing of risks	Downside risks still present, further depo cuts on cards	No PEPP top up intended as BTP-bund spread stable	1.070
ING Base Case	Recent data suggest the CPI pick up will take longer	Recent data suggest significant slowdown in activity	No change, forward guidance for lower rates for longer	Hints at increase of PEPP scale & scope in June meeting	1.090
Decline in risk premium	Confident that underlying inflation will pick up	Downside risks have started to disappear	No change, forward guidance for lower rates for longer	PEPP top up by EUR 500bn, ECB buying fallen angels	1.0950
Large decline in risk premium	Risks to the inflation outlook are balanced	Risks to the economic outlook are balanced	QE to stay beyond 2020 but lower bound for rates likely reached	EUR 750bn top up, bank bonds / fallen angels buying	1.110

Source: ING, Bloomberg

⬇️ USD: Further moving towards a soft USD environment

Markets are benefitting from the cautious Federal Reserve stance and the positive news on Covid-19 drug test results.

On the former, the [Fed struck a downbeat tone](#) on the economic outlook yesterday, sticking to its ultra-accommodative policy stance - with loose policy set to remain in place for longer. Support from central banks globally (today, the ECB should also reiterate its accommodative stance) and first European countries moving out of lockdown provide glimmers of hope for risk assets and should support higher beta FX today and keep USD soft.

⬆️ EUR: ECB containing EUR risk premium and avoiding miss-steps

Markets will be closely watching two aspects of the ECB meeting today: the potential top-up of the PEPP programme and President Lagarde's communication. On the former, we see a further increase in size (from the current EUR750bntoEUR1.25trn) and scope (adding fallen angels)as

likely, though the timing is uncertain. It may not happen today, but the ECB is likely to signal the eventual increase in purchases when it comes to its June meeting.

On the latter, following the unfortunate communication in March, we expect the ECB President to communicate a commitment to do 'whatever it takes' to help the eurozone economy and ensure financial stability. Both would be supportive of EUR. As EUR/USD trades with a modest ECB uncertainty risk premium, clear ECB communication should send it to 1.090. PEPP programme being extended already today would likely send EUR/USD to 1.095.

See [ECB Cribsheet](#) for details. April CPI is expected to fall to 0.2% but its explanatory power should be taken with a pinch of the salt given measurement issues (ie closed shops).

GBP: Helped by the general risk sentiment

The ECB message to do more on the PEPP programme should help GBP/USD to move above 1.2500 today. Supportive risk sentiment should put a downward pressure on EUR/GBP, with the cross continuing testing the 0.8700 level.

Oil FX: The worst may be over but still cautious outlook

Oil continues to recover, benefiting from the mix of the smallest increase in inventories in the US since March and Norway decision to reduce output (in line with the previous OPEC + decision). As our commodities team notes, if we see a continuation of this trend in the coming weeks, it could suggest the [worst might be behind the oil market](#).

We remain cautious on oil-related currencies as Brent is unlikely to move meaningfully above 25US\$/bbl this quarter while the risk of a steep decline in WTI in mid-May (due to storage-related issues) is still in place. In the EM FX space, RUB looks the most attractive among commodity exporters given its relatively solid fiscal position. In the G10 FX space, upside to NOK should be limited and EUR/NOK to stay above the 11.00 level.