

EUR & ECB crib sheet: Hawks can't lend their wings to the euro

Here are our four scenarios for the European Central Bank and their related implications for the currency and rates markets. A 75bp ECB hike is our call; it's what markets are expecting too. Attaching a hawkish tone to the hike should – like in previous instances – fail to offer substantial and long-lasting support to the euro

EUR and ECB crib sheet

	Inflation outlook	Growth outlook	Interest rates	Quantitative easing	EUR/USD (0.98)	10Y Bund (2.32%)
<i>Current stance</i>	Inflation far too high & likely to stay above target for an extended period	Economy expected to stagnate later in the year and in the first quarter of 2023	Depo at 0.75%. Future rate path will be data-dependent	APP and PEPP in reinvestment phase. TPI can be triggered but has conditionality		
Dovish	Upside risks in near term, but medium-term infl. may return to target	High risk of a much sharper/longer lasting economic slowdown	50bp hike Worsening outlook suggests slower pace of tightening	Increased probability of activating TPI	0.96	2.10%
ING Base Case (neutral)	Infl. to stay high, more hikes needed to bring medium term back to target	Risks to the downside, particularly in the near term	75bp hike Maintaining a fully data-dependent approach	Unchanged	0.97	2.25%
Moderately hawkish	Inflation will likely be higher than forecasted over medium term	Downside risks to the outlook slightly abated since September	75bp hike Hinting at more large hikes ahead	Hints that balance sheet reduction is being discussed	0.99	2.30%
Very hawkish	Inflation seen persistently above target in the projection period	Fiscal support and lower gas prices suggest quick economic rebound	100bp hike More hikes to come	Balance sheet reduction will start early in 2023	1.00	2.40%

Source: ING

We expect the ECB to hike by 75bp at the October meeting

This has become a consensus call in recent weeks, and markets are fully pricing in such a move. This means that – barring a surprise on the size of the hike – the market reaction will depend on the ECB's stance on:

- **Further rate rises:** any tweaks to the meeting-by-meeting data-dependent approach and/or references to the terminal rate
- **Changes in the inflation and growth outlook**
- **Discussion over quantitative tightening**

In our [ECB preview](#), we highlight what we expect to hear on those topics this week. Here you can see where we're coming from; it's our usual pre-meeting scenario analysis, where we look at implications for EUR/USD and the rates market to those different potential outcomes.

A 75bp hike will not be a game-changer for EUR/USD

As shown above, we see limited upside risks for EUR/USD in the aftermath of the ECB announcement. This is mainly due to the weakened correlation between short-term rates and currency dynamics in the eurozone. This means that additional tightening being priced into the EUR curve on the back of a hawkish statement still looks unlikely to offer a sizeable, and above all, sustainable support to the euro.

This was indeed the case in the past few meetings, where the ECB consistently surprised on the hawkish side but that did not avert a euro depreciation. A tightening-based FX protest (against the inflationary weak euro) is simply not working in the current market environment.

In line with our expectations of a stronger dollar, as the Fed keeps tightening policy and keeps risk sentiment weak into the new year, we expect a drop below 0.9500 in EUR/USD by the end of this quarter.

Authors

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.