

EUR & ECB crib sheet

The April ECB meeting poses modest upside to EUR/USD. Compared to the March disappointment, the ECB is likely to do all it can to prevent a risk premium build-up. If the PEPP programme is not expanded this week, the ECB will likely signal a top-up in June. EUR/USD trades with a modest ECB uncertainty risk premium but clear communication should send it to 1.090

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

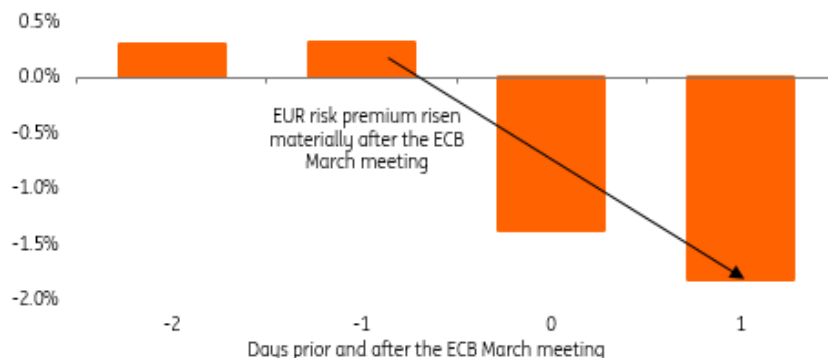
FX markets will be closely watching two aspects of the upcoming European Central Bank meeting this Thursday: the potential top up of the Pandemic Emergency Purchase Programme and President Christine Lagarde's communication, with both being closely tied to the perception of the euro risk premia.

PEPP programme: We see a further increase in size (from the current EUR 750 billion to EUR 1.250 trillion) and scope (adding fallen angels - high yield debt) as likely, though the timing is uncertain. It may already happen this week, but given that the new set of ECB staff forecasts is only delivered at the June meeting, the ECB may opt to wait (see [ECB Preview](#) for details), particularly as the BTP-Bund spread has narrowed in recent days and the 10-y BTP yield is back below 2%. However, even if the increase in PEPP is not announced this week, we think it likely that the ECB's communication will hint at an eventual increase in purchases at the June meeting, in turn preventing a disappointment induced sell-off in peripheral bonds and the euro. See the ECB cribsheet above for

details and various scenarios.

Figure 1: March ECB meeting led to euro risk premium built up

EUR/USD risk premium estimate (derived from ING Short-term Financial Fair Value model) around and after the March ECB meeting (shown as day 0 in the chart). Negative number means negative euro risk premium, positive number means positive euro risk premium

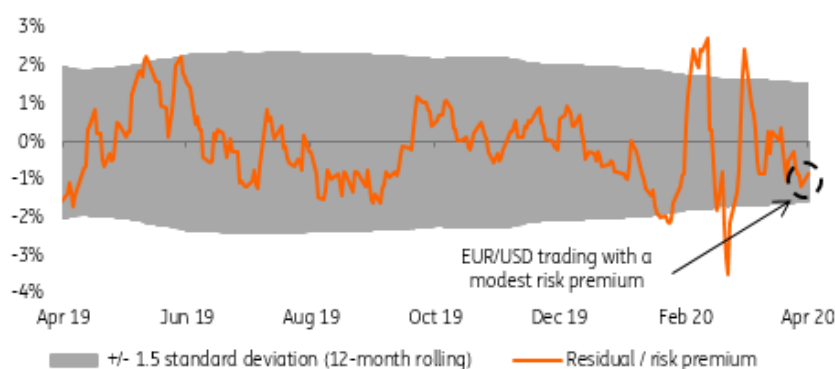


Source: ING

The press conference: This will be a closely watched factor following President Lagarde's unfortunate communication at the March meeting, which gave rise to fears of the risk premium being re-introduced to the common currency (as Figure 1 shows above, the euro risk premium increased substantially after the March meeting, by around 2%). We see it as unlikely that President Lagarde would want to repeat the mistakes of the past and communicating a commitment to do 'whatever it takes' to help the eurozone economy and ensure financial stability would be supportive of the euro this week.

Figure 2: Modest uncertainty premium priced into EUR ahead of the ECB meeting

Residual / measure of risk premia between EUR/USD short term financial fair value and spot.

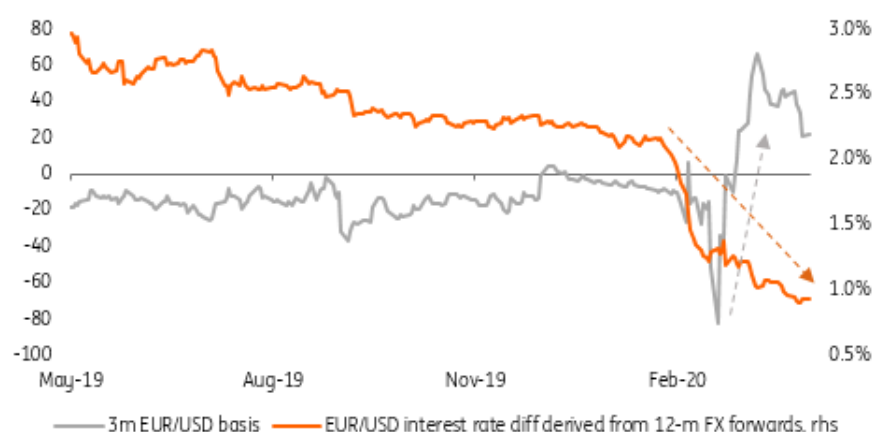


Source: ING

No ECB missteps to help EUR/USD to / above 1.0900 this week

Given that EUR/USD trades modestly below its short term fair value (Figure 2), meaning that some risk premium associated with the ECB communication looks to be partly priced in, positive signals from the ECB this week could bring EUR/USD to / above the 1.0900 level this week.

Figure 3: USD losing its tactical and strategic advantages



Source: ING, Bloomberg

EUR/USD 1.15 target for the summer

With the ECB preventing the euro risk premium from re-building and the US dollar no longer getting the indiscriminate support from the USD funding squeeze and a previously high interest rate differential (both in Figure 3, with the former being tactical and the latter strategic advantages - which have now faded) we expect EUR/USD to slowly grind higher, towards the 1.15 level this summer as the broader USD weakness unfolds.

Author

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 www.ing.com.