

Article | 4 June 2020

FX

EUR: ECB making EUR a well-behaved passenger vs USD and GBP

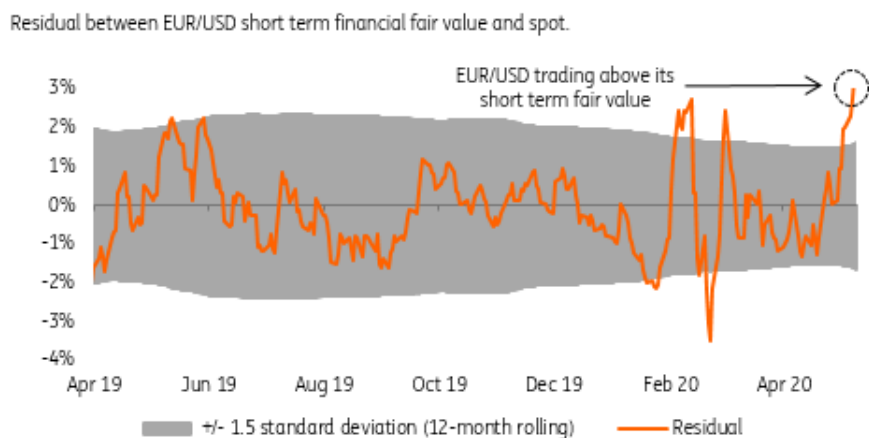
The ECB delivered and the €600bn PEPP expansion further helped to stabilise EUR. The euro risk premium is currently no longer an issue. If anything, EUR seems to be modestly front running its short-term fair value. The positive ECB effect on EUR now seems exhausted, with further EUR/USD and EUR/GBP gains to be driven by issues USD and GBP are to face



The ECB delivered and further stabilised the euro ...

The ECB delivered and increased the Pandemic Emergency Purchase Programme (PEPP). The top-up was modestly higher than expected (€600bn announced vs €500bn expected) and the announcement that PEPP reinvestments will run until at least end-2022 is also seen as positive (see [ECB Review](#) for more), as both ensured a limited scope for a risk premium to return into the euro and the euro-denominated assets. However, as the euro has already been trading rich vs its short-term fair value (Fig 1), we see scope for further ideosyncratic euro gains as limited. In our view, and as we argued in the [ECB Crib Sheet](#), the newly announced ECB measures are to have more of a stabilising effect on the common currency and should prevent euro weakness.

Figure 1: EUR/USD front running its short-term fair value



Source: ING

... but any further ECB induced EUR strength is unlikely any time soon

While the ECB is preventing an idiosyncratic EUR decline, its new set of forecasts also suggests that an ECB induced EUR strength is unlikely any time soon. The inflation forecast has been surprisingly downgraded throughout the forecast horizon and with the 2022 forecast pencilling CPI at 1.3% (well below the 2% target) the prospects of any monetary normalisation are almost non-existent at this point. Recall this was the key driver of EUR/USD in 2017 when the cross rallied largely on the back of the ECB QE tapering expectations.

Bearish USD and GBP prospects the key for more upside to EUR/USD and EUR/GBP

With the domestic induced EUR rally unlikely, we continue to see the continuation of the USD bear trend as the main driver of the expected EUR/USD upside. Indeed, the post ECB break in EUR/USD above 1.1300 coincided more with the renewed broad-based USD weakness rather than EUR strength (with the likes of NOK, SEK and CEE FX appreciating against EUR). We see EUR/USD above 1.15 this summer.

| We see EUR/USD above 1.15 this summer.

The same dynamics also apply to EUR/GBP where the GBP side of the cross should be the main driver of the pair. As per [Brexit returns as major headache for the pound](#), we target EUR/GBP 0.91 by end-June as the likely limited progress in the UK-EU trade negotiations and the no extension of the transition period should translate into further built up of risk premium into GBP.

THINK economic and financial analysis

For both EUR/USD and EUR/GBP near-term journeys, the euro shall remain a relatively well behaved passive passenger, more attractive than its more ugly two partners (USD and GBP), which are to actively decline.

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.