

## Eurozone: It's the end of QE as we know it...

...and we will be fine as the European Central Bank is gradually shelving the controversial bond-buying programme



ECB headquarters,  
Frankfurt

The ECB meeting next week will not only be the last meeting of the year but will also be a historic meeting. It should mark an important step in returning monetary policy to normality. Only, hardly anyone seems to be interested. Thanks to changes in the communication back in June, market participants and ECB watchers have been well prepared for the gradual end of the ECB's net asset purchases. Anything else than the announcement to bring these purchases down to zero by year-end at Thursday's meeting would be a great surprise.

### **New macro projections: how low will they go?**

The biggest unknown at next week's meeting should be the ECB's latest staff projections and the Governing Council's assessment of the economic situation. Up to now, ECB senior officials have maintained their relatively upbeat take on the eurozone economy, despite a recent and more subtle shift towards putting more emphasis on downside risks. Back in September, the ECB saw GDP growth at 2.0% this year, 1.8% in 2019 and 1.7% in 2020. Headline inflation was expected to

come in at 1.7% in all three years. In the meantime, the market consensus has clearly shifted to the downside.

When analysing the ECB's projections, keep in mind that compared with the September projections, the external assumptions have changed significantly. In particular, the sharp drop in oil prices, in terms of both spot and forward prices, should have boosted GDP growth and lowered the headline inflation forecasts. While the trade-weighted exchange rate has remained broadly stable, long-term interest rates have come down, also inserting some stimulus to GDP growth. Taken together, all changes in the external assumptions could add some 10 basis points to GDP growth and shave off 10 basis points from headline inflation. As regards growth, however, this should be too little to offset the impact from a weak 3Q on 2018 and 2019 growth. Any downward revisions to below 1.6% for 2019 and beyond would, in our view, signal a clear shift towards more pessimism. Finally, the forecast horizon will be extended to 2021. Keep a close eye on the inflation projections for 2021.

## Details on reinvestments and liquidity

During the press conference, ECB President Mario Draghi will probably also be asked questions about details of the reinvestment programme and possible new liquidity injections. The changes to the capital key do not necessarily have to affect the reinvestment programme. As regards new targeted long-term refinancing operations, the discussion within the ECB has already started with an aim to avoid any liquidity shortages. A new TLTRO in the summer of 2019 with a variable interest rate could be a way out but currently comes too early, as it could be perceived as direct support to Italian banks.

## One done but not a lot more to come

With the end of the net asset purchases, at least one unconventional measure should be shelved now. Expectations that the end of QE would lead to surges in bond yields have – so far – been proven wrong. However, let's not forget that there is still a reinvestment programme in place. The ECB's balance sheet will hardly shrink in the coming months. As successful as the transition has been, there will be little time for the ECB to relax. As of next week, all eyes will be on what is coming next.

For the time being, the ECB should keep all its cards close to its chest and stick to the current forward guidance on rates and the reinvestment horizon of at least one year. This keeps all options open for further normalisation and a first rate hike at the end of next year but also for keeping rates at their current level for much longer. However, if things really get nasty, next year's discussions on the timing of the first rate hike could easily morph into discussions on whether the second unconventional measure (negative deposit rates) should be shelved or whether to hike rates at all.

### Author

**Carsten Brzeski**

Global Head of Macro

[carsten.brzeski@ing.de](mailto: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>.