Rates Spark: Don't rock the boat

The speedup of ECB asset purchases was announced at the March meeting, so today's press conference should be more about biding time until June when the purchase pace is up for reassessment. We think risks are skewed towards higher rates, as it might not take much to confirm the markets more bullish views on the economy

Source: Shutterstock

No pressure to act for the ECB

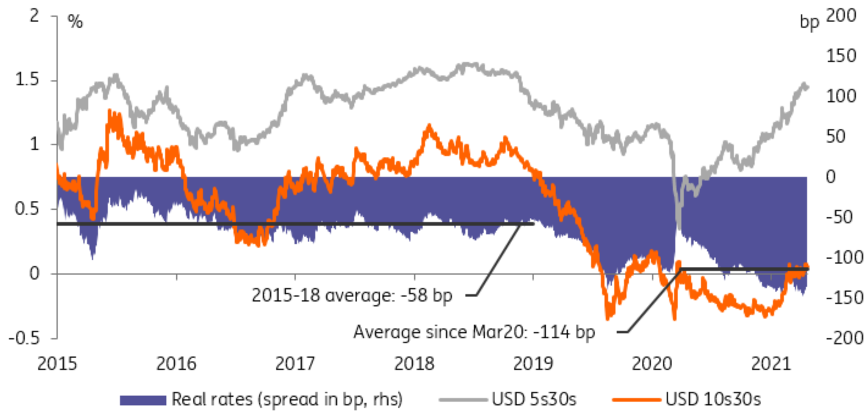
On the face of it, the ECB should feel little pressure to do anything today.

Market rates are slightly higher, but more importantly – as this measure for policy accommodation has been given more prominence by the likes of ECB's Isabel Schnabel - real yields are still close to their historic lows. In Germany, the constitutional court rejected the legal challenge of the EU recovery fund, paving the way for ratification. If anything, the outlook has brightened somewhat as the vaccine roll-out in Europe finally gains momentum. And herein lie the risks of today's meeting.

For financial markets, the acceleration of European vaccination programs so far this quarter, and the resilient confidence surveys in the face of tighter restrictions, are strong enough a rationale to price the start of an economic recovery. In the world of central banks, they are welcome but too tenuous to drive a change of policy.

Our economics team rightly stresses that the ECB should remain coy on the future of asset purchases. In the context of building optimism around the block's economic prospects, we think it would not take much for markets to see a confirmation of their bullish view in the central bank's discourse.

Little pressure on the ECB to act as real yields are close to their lows



Source: Refinitiv, ING

The PEPP discussion could spill into the open

In the background, the tug of war between hawks and doves, north and south, over the future of the pandemic emergency purchase programme (PEPP) beyond its current slated end date after March 2022 appears to be in full swing already. And not without reason as along these divides, our economists highlight the uneven recovery.

Governing Council members have already expressed widely different opinions about its future, ranging from tapering as soon as 3Q21 to a possible increase in the asset purchase programme (APP) to accompany the decrease in PEPP purchases.

Hints of tapering could open more upside for EUR rates

Overall, we see the rates market's potential reaction to comments on the future of PEPP as asymmetric: warnings that purchases could continue at a higher pace beyond Q2 would be met with scepticism. At the same time, hints of tapering could open more upside for EUR rates. It has not helped that the effective increase in net purchases has already been less impressive than expected.

Surely ECB President Christine Lagarde will try to dispel any notion of disappointment by pointing to larger redemptions and admittedly higher gross purchases as a result.

Today's events and market view

The ECB meeting and press conference will have the markets full attention, with no notable other events featuring in the calendars today.

As much as the ECB might want to avoid rocking the boat today, we think that the risks from this meeting are skewed towards higher rates. It might not take much for markets to see a confirmation of their bullish view around the economic prospects.

Today, the primary market will be busier, with France issuing up to €11bn in three bonds out to eight years of maturity, including a new bond coming due in 2027. In linkers, France will sell another €2bn. Spain will also be active selling up to €6bn in bonds out to 10 years.

Authors

Benjamin Schroeder
Senior Rates Strategist
benjamin.schroder@ing.com

Padhraic Garvey, CFA
Regional Head of Research, Americas
padhraic.garvey@ing.com