

The ECB's dashboard and implications for asset markets

The cautious ECB tone this Thursday in the currently USD-supportive environment suggests a modest downside to EUR/USD. We reiterate our 1- to 3-month EUR/USD forecast of 1.1200. The upside to bund yields remains limited



Source: Shutterstock

The ECB's Dashboard: How to position for Draghi's alternatives

	Inflation outlook	Growth outlook	Forward rate guidance	TLTRO discussion			
Current stance	"Underlying inflation is expected to increase over the medium term"	"The risks... to growth outlook have moved to the downside"	Rates to remain "at their present levels at least through the summer of 2019"	None at this point. Potential TLTRO liquidity bottleneck by June this year	EUR/USD	2-year Schatz	10-year Bund
Dovish	Downward revision to 2020/21 CPI forecast	Risks to the growth outlook to the downside	Rates to remain "at their present levels until end-2019"	Announcement of new round of TLTROs	1.11	-5 bp	-5bp
ING Base Case	Unchanged CPI forecasts for 2019/20/21	Downgrade to GDP forecasts for 2019/20/21	No change to forward guidance (at this meeting)	Committees have been tasked to look into options	1.13	+2.5 bp	+5 bp
Hawkish	Upward revision by 0.2 pp or more of 2020 CPI forecast	Upward revision of 2019/20 growth forecasts	The council doesn't envisage extension of forward guidance	No discussions about options to deal with liquidity bottlenecks	1.15	+5 bp	+10 bp

Source: ING

EUR: Still very limited near term upside

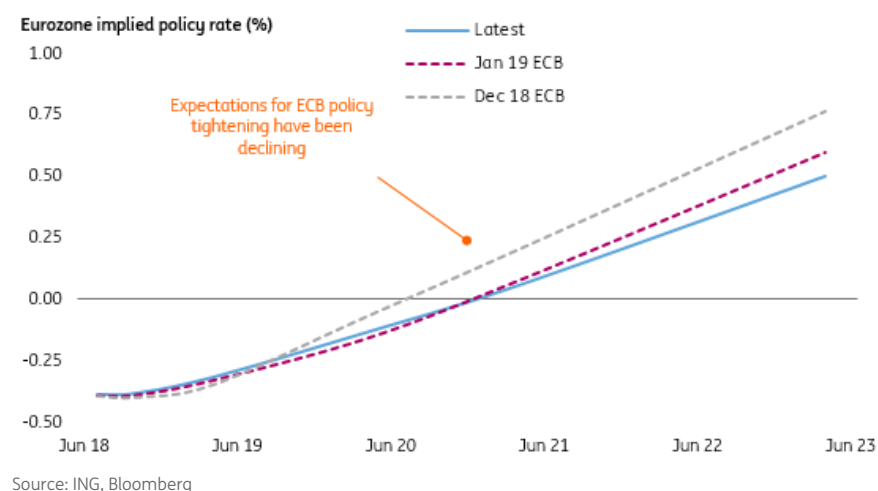
We don't expect the euro to get much of a boost from the ECB meeting this week. The general message should remain cautious with the ECB attempting to avoid unintentional tightening of monetary conditions. Here a potential hint at further TLTROs should reinforce such a message.

With the ECB remaining cautious and the rate differential between the USD and EUR intact (if anything, it should widen again as markets start pricing in a 3Q19 Federal Reserve hike, cementing the dollar's status of one of the high yielders in the G10 FX space), the upside to EUR/USD looks very limited in the coming months. We reiterate our forecast for EUR/USD 1.12 for one and three-month time horizons.

Indeed, the lack of catalysts for a more meaningful reversal in the dovish ECB stance (as per Fig 2, the market is assigning a fairly low probability to any meaningful ECB tightening in coming quarters) as well as the non-negligible costs of shorting USD vs EUR have been some of the factors behind why the speculative community has been reducing EUR longs or increasing EUR shorts over recent weeks (Fig 3).

[Read our ECB preview: Trying not to get lost in the transition](#)

Market assigning low probability to any meaningful ECB tightening



While Eurozone data may improve, this is unlikely to translate into a hawkish ECB stance

While we see a lack of near-term catalysts for EUR/USD upside, we also think the downside to the cross is limited, particularly if Eurozone data improves. The February Eurozone PMI displayed the first tentative signs of Eurozone data bottoming out.

However, we note that unless any positive data surprise translates into a shift in the ECB stance (from the current cautious tone to a more hawkish stance), the scope for an idiosyncratic EUR rally (as was the case in 2017, when the market started pricing in ECB QE tapering) is fairly limited. Indeed, the data surprise index increased modestly in February while the US index fell sharply (in

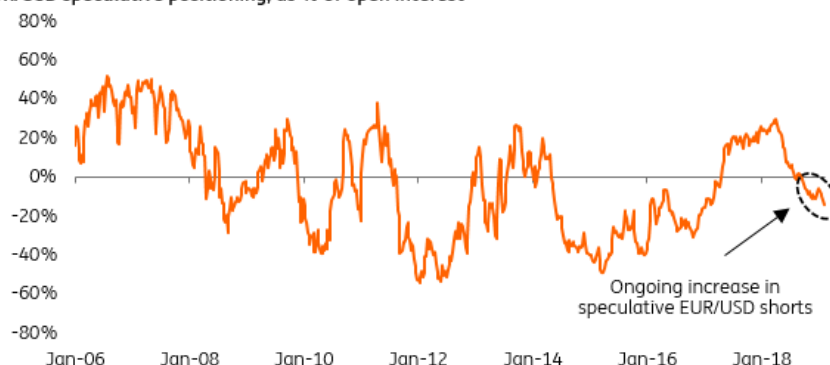
large part due to poor December US retail sales). EUR/USD remained flat and didn't benefit from the relative reversal in the data surprises.

We see it unlikely that the ECB will deliver a meaningful tightening during this cycle (as CPI will remain below the target) meaning that any meaningful EUR/USD upside should be a function of the peak in the USD cycle (and subsequent across-the-board USD softness) rather than ECB generated euro strength.

Eurozone PMI: Early signs of an economy pulling through

Speculative EUR/USD shorts rising modestly

EUR/USD speculative positioning, as % of open interest*



* As of 19th February 2019 (data are reported with a lag)

Source: CFTC

Bond markets: Fairly limited upside to bund yields

Our base case looks for yields being biased slightly higher as a wait-and-see stance might not be enough to live up to market expectations. More clarity on a potential new round of TLTROs seems to be the base case, where "tasking committees" would be the bare minimum.

If hints emerge of the new operations being conducted at less generous terms, the bias higher in rates could be felt even more in Eurozone periphery bond yields, though. Still, ECB reluctance to act now should not lead markets to price out a lower-for-longer scenario, meaning the upside in yields should be limited.

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