

Where next for global central banks?

It's been a hectic few days in the central bank arena, and there's still more to come. Here's what we expect now from global monetary policy

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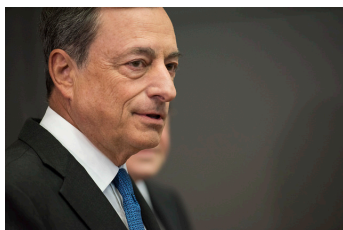


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A Dovish, but cautious shift from the Fed

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Source: Shutterstock

The Federal Reserve has opted to leave monetary policy unchanged, but as widely expected (and forewarned by Fed Chair Jerome Powell), has adopted a more dovish stance today. James Bullard, the St Louis Fed President, went further and voted for an immediate 25bp rate cut.

The market has taken this as a signal that a July 25bp rate cut is virtually a done deal with three more to come, but we are not so sure. The path of trade talks is critical and if there are some positive messages, if not actions, and the activity data holds up, the market will be disappointed. Moreover, the “dot” diagram of forecasters has a median of NO cuts this year and only one next year.

While the news in the near term is likely to get worse before it gets better, we think there are decent fundamentals. More importantly, we think President Trump’s desire to win re-election means that he will be wary of pushing too far for too long on trade, thereby damaging his own chances. We continue to look for two rate cuts in 2H19 and favour September and December.

A clear shift in language,

The big change in the accompanying statement is the dropping of the description of the Fed's stance as being "patient". Instead, the Fed believes "uncertainties about the outlook have increased" which mean the FOMC will be "closely monitoring the implications of incoming information... and will act as appropriate to sustain the expansion".

The current economic situation has also been downgraded from one that was "solid" in May to one that is "moderate" today. This is largely down to "soft" business investment, which is enough to offset the fact consumer spending "appears to have picked up". Yet they have actually revised up their 2020 GDP growth forecast to 2% and lowered their prediction for unemployment. Meanwhile, market-based measures of inflation "have declined" and they have lowered their near-term forecast profile, but have headline and core inflation returning to target next year.

But not in forecasts...

The tone of this statement is clearly suggesting that rate cuts are in the offing and markets are increasingly confident that the first move will be in July with three more probable over the next year. Yet the "dot" diagram of predictions from Fed officials warns markets they perhaps shouldn't get too far ahead of themselves. The median forecast is for NO rate change this year. Seven officials are looking for two 25bp rate cuts and one is looking for a single 25bp move. Eight expect no change while one individual is actually still penciling in a rate hike!

For end 2020, Fed officials are suggesting they may only need one rate cut thanks to the fact that one additional official is now looking for a single 25bp next year - no-one is looking for more than two rate cuts in total over the forecast period. The median then suggests that one cut is reversed in 2021 - returning the Fed funds target rate to its current level - with the longer run forecast for where the Fed funds rate settles has been lowered from 2.8% to 2.5%.

As such it's dovish, but certainly not that dovish.

Federal Reserve median forecasts

Variable	Median			
	2019	2020	2021	Longer Run
Change in real GDP (June FOMC)	2.1	2.0	1.8	1.9
(PREVIOUS)	2.1	1.9	1.8	1.9
Unemployment Rate (June FOMC)	3.6	3.7	3.8	4.2
(PREVIOUS)	3.7	3.8	3.9	4.3
PCE inflation (June FOMC)	1.5	1.9	2.0	2.0
(PREVIOUS)	1.8	2.0	2.0	2.0
Core PCE inflation (June FOMC)	1.8	1.9	2.0	-
(PREVIOUS)	2.0	2.0	2.0	-
Fed funds rate (June FOMC)	2.4	2.1	2.4	2.5
(PREVIOUS)	2.4	2.6	2.6	2.8

Source: Federal Reserve, ING

All to play for

The press conference has allowed Fed Chair Powell to put a bit more colour on the situation, suggesting that the Fed will learn a lot in the near term - next week's G20 and associated trade discussions - and that the Fed should not overreact to individual data points.

Nonetheless, even those officials that are forecasting no rate cuts acknowledge the case for

action has strengthened.

We are sticking to our recently revised forecast for now, but if the data deteriorates further and President Trump and President Xi's meeting next week goes badly, we are open to moving that to July and September

We recently switched to a view that the Fed would cut rates twice this year – once in September and once in December on the basis that trade tensions are likely to get worse before they get better. This will weigh on sentiment, which could see firms pull back on investment and hiring, thereby threatening a broader economic slowdown and justifying precautionary policy easing.

We are sticking with this for now, but should the data deteriorate and next week's meeting between President Trump and President Xi go badly, we are open to moving that to July and September. Should payrolls rebound to 250k next month, and trade discussions offer signals for encouragement it is the market that will have to move.

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Snap | 18 June 2019

ECB: Mario strikes again

ECB president Mario Draghi moves financial markets again, opening the door wide for new monetary stimulus. Today's speech marks a remarkable u-turn...



Source: ECB

After Benoit Coeure's rather dovish interview with the Financial Times, suggesting that “at some point during our next few meetings, we might very well be facing a situation where risks have materialised”, ECB president Mario Draghi went one step further with his speech in Sintra today.

There should be no more doubts about the ECB's determination to act. In fact, the major question is no longer what it would take the ECB to cut rates but rather what it would take the ECB not to cut rates. Next steps could follow as soon as at the July meeting.

In Draghi's Sintra speech, the economic assessment was a bit more downbeat than during the press conference after the June meeting. While less than two weeks ago, “the euro area expansion will continue to be supported by favourable financing conditions, the mildly expansionary euro area fiscal stance, further employment gains and rising wages, and the ongoing – albeit somewhat slower – growth in global activity”, Draghi today talked about indicators for the coming quarters pointing to lingering softness. From which follows that “In the absence of improvement, such that the sustained return of inflation to our aim is threatened, additional stimulus will be required”.

On top of that Draghi hinted that the ECB might interpret its medium-term inflation objective of below but close to 2% as an average, meaning that inflation would have to be above that level at

some time in the future.

Draghi's language on additional easing measures was also more explicit than two weeks ago. "Mentioned by some Governing Council members" rate cuts and a restart of QE were today confirmed as possible actions. While two weeks ago it sounded as if only some ECB members had started to dig back into the ECB's toolkit, Draghi today opened the toolkit, showcasing it to financial markets.

Rate cut coming - as early as July?

As already concluded after the last ECB meeting, the ECB is in our view only one economic slip away from further easing. After today's comments, it even looks as if it would require a clear positive surprise for the ECB not to act. Consequently and given the fast pace of communication changes, a rate cut in July can no longer be excluded. In a more normal world, the ECB would like to wait until the September meeting, when not only 2Q GDP will have been released but when also a fresh round of staff projections will be available. However, the world is not normal. In case of another batch of disappointing sentiment indicators next week, the Fed opening the door to a July rate cut and further escalation of the trade conflicts, a July cut looks likely. If one or more of these factors surprises to the upside, September looks more likely.

One might wonder why the ECB is so alarmed, in a situation when the economy is still growing and unemployment rates are at their lowest levels in a decade. The answer is that the ECB is completely focused on the inflation outlook. As long as the longer-term inflation outlook is significantly below 2%, the ECB in its current line-up will [continue doing whatever-it-takes](#).

The Sintra speech also made clear that the ECB is somewhat caught in its own success. Draghi today was very vocal, putting pressure on governments to step in with fiscal policy. Even though he would never admit it, before going where no European central bank has ever gone before, the ECB would like to see the fiscal stimulus, getting growth and inflation in the Eurozone higher

Today's speech also marks a remarkable U-turn for global central banks, which in less than half a year have moved from normalisation towards new easing prospects. This is unprecedented activism. Only time will tell whether this attempt to stay ahead of the curve was foresight or just panic.

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The Bank of England's June dashboard

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Source: Shutterstock

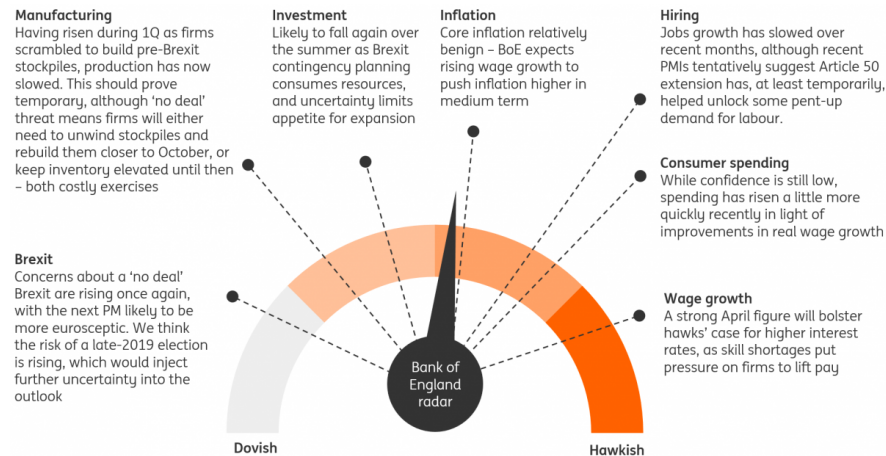
Will the Bank of England hike interest rates in 2019? Set against the prospect of both US and eurozone monetary easing, this may seem unlikely – and in fact, markets now think UK rates are marginally more likely to fall rather than rise over the next two years. However, this is in stark contrast to recent comments from BoE policymakers – most of which have signalled that rates may need to rise sooner than investors think. So who's right?

We think it's unlikely the Bank will get an opportunity to tighten further this year

Well, the growth story at least suggests caution. While the growth numbers are being thrown around by the effect of Brexit stockpiling – potentially resulting in a very poor second-quarter GDP figure – the underlying story is still fairly mixed.

Consumer spending has been performing a little better, given a gradual improvement in real wage growth. However, this is likely to be offset over the summer by a further fall in investment. Contingency activities for a possible 'no deal' exit in October will be both time and resource-intensive for firms, limiting appetite/scope for increased capital spending. Global growth risks have also risen amid President Trump's threat to impose further tariffs on Chinese imports.

ING's Bank of England radar



Source: ING

Solid wage data - a key focus for policymakers

It's worth noting though that a fair chunk of this uncertainty is already factored into the Bank's latest forecasts. At the same time, wage growth is continuing to perform solidly - a key ingredient in the BoE's rate hike rationale. Earnings growth excluding bonuses increased to 3.4% YoY in April, albeit some of this was down to a fairly sizeable pick-up in public sector pay ([reportedly centred within the health service](#)).

On balance though, this recent data should help to bolster the Bank's view that wage growth will continue to rise in the medium-term as skill shortages intensify.

Expect the BoE to continue talking up prospects of rate hikes

With that in mind, we expect policymakers to continue hinting that markets are underestimating the risk of further tightening. It's possible that the Bank says this more explicitly within either its statement or set of minutes (released simultaneously) this week, particularly given that market interest rate expectations have completely flattened since the May meeting.

There is also an outside chance that one or two policymakers vote for an immediate 25bp rate hike at this meeting - Michael Saunders, in particular, has taken a hawkish stance in public recently.

We don't expect a rate hike this year

Ultimately though, we think it's unlikely the Bank will get an opportunity to tighten further this year. While we think the probability of 'no deal' is still relatively low (around 20%), the [risk of a late-2019 election is rising](#), and this would inject another layer of uncertainty into the UK outlook.

Recent rhetoric from the BoE suggests a November move shouldn't be totally ruled out, but the fact that this meeting falls only a week after the October 31 Brexit deadline makes for challenging timing. Barring either a swift ratification of a Brexit deal, or a further six-month Article 50 extension, we think policymakers are more likely to keep policy on hold through 2019.

[Read our three scenarios for Brexit under Boris Johnson](#)

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Hawkish Norges Bank to hike rates and signal more to come

We expect the Norwegian central bank to increase interest rates on Thursday and signal another move later in the year. But in light of recent declines in...



Source: Shutterstock

Norges Bank is going against the tide of global central bank easing

The Norwegian central bank looks set to go firmly against the global rate cut tide on Thursday, where the stage is set for interest rates to increase by a quarter-point to 1.25%. This would mark the second rate hike so far in 2019.

But given that this move was clearly signposted by policymakers back at the May meeting, the bigger question is whether the bank will signal a third increase later in the year.

Expect the central bank to signal a further move later this year

When Norges Bank last released its interest rate projection back in March, policymakers had pencilled in roughly two further rate hikes in addition to the one expected this week. Back then, the next rate rise was expected to come in the early stages of 2020, but in light of recent developments, we think policymakers may look to bring forward the timing of this to later this

year.

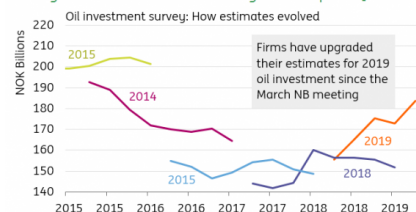
Domestically, the case for tightening continues to look fairly solid. The recovery in energy prices over the past couple of years has helped the economy, particularly given that the break-even cost for new Norwegian projects lies well below current market pricing (break-even is around \$10-35 per barrel, according to the central bank). This has incentivised investment in extraction/pipeline activities, and the latest survey data suggests the total investment in 2019 will be even higher than previously anticipated.

At the same time, the krone has weakened further, defying Norges Bank's forecast for around a 2% average appreciation in the trade-weighted krone across the second quarter.

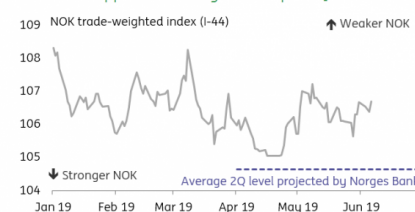
The combination of stronger near-term investment and the weaker krone should have the effect of boosting Norges Bank's rate path in the short-term.

How the latest interest rate projection could change compared to March

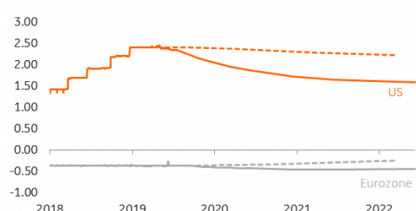
Stronger 2019 oil investment - Higher rate path ↑



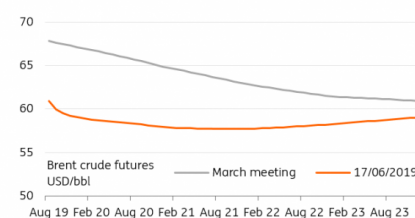
NOK hasn't appreciated - Higher rate path ↑



Lower foreign rates - Lower rate path ↓



Lower oil curve - Lower rate path ↓



Source: Macrobond, ING

The Bank may signal a lower path for interest rates further out

It's not all positive though, and there are question marks over how the projections will look further out. Oil prices have declined across the curve since March, while foreign interest rate expectations have fallen markedly as trade tensions have grown. The mechanical way the Bank formulates its interest rate projections mean both factors could translate into a lower rate path for 2020 and beyond.

We expect a December rate hike from Norges Bank

Wrapping all of this together, it looks pretty likely that the Bank will incorporate a further rate hike later this year into its projections. We think such a move is most likely to happen in December.

All this could support NOK in the short term and even deliver a lower USD/NOK – [please read our article on how the dollar could react to a Fed Dot adjustment](#). However, we doubt

Norges Bank policy will be enough to drive NOK persistently stronger against EUR in 3Q19, even if oil prices move higher. Like other high-beta currencies, NOK has been dragged down by concerns about trade wars and weaker global growth.

With a non-negligible risk of the US imposing broader tariffs on China this summer, a hawkish Norges Bank should instead translate into NOK outperformance against SEK (Swedish Krona) as opposed to EUR. Risks to EUR/NOK remain on the upside over coming months unless there are signs of a material improvement in trade tensions.

[Read how the dollar could react to a Fed dot adjustment](#)

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Emperor Draghi's not naked, the ECB has corporates (and banks) in CSPP2

Mario Draghi's hints at possible new monetary stimulus has got the market thinking: Has he still got the magic, or is he just an emperor trying to...



All dressed up. ECB President, Mario Draghi, receives an honorary degree in Bologna, Italy in February 2019

Targeting corporates will squeeze credit spreads

The talk in fixed income markets for a while now centres on the European Central Bank's readiness to restart new stimulus. We covered it [here](#) and discussed the various routes that could be taken, from rate cuts to renewed quantitative easing to buying stocks.

And we see ample reason to expect the ECB to target corporates again and that means credit markets are set to be supported. With the ECB only one economic slip away from another rate cut, speculation about what ammunition the ECB still has left will continue.

For the past eight years of his presidency, Mario Draghi has shown an impressive determination to act. Nothing is worse than a central bank admitting it has run out of options. In this regards, besides a possible rate cut, restarting QE looks as though it'll be the most likely option. Even though a restart of QE would fall into the category 'more of the same', we would be very cautious calling Draghi an emperor with new clothes.

In fact, in our view, the emperor is not naked at all; he has corporates, and banks, in CSPP2.

The ECB likes private sector programmes

The ECB has made no secret of its liking of private sector programmes. Apart from members' rhetoric, ECB publications particularly provide the greatest hint of a possible reinstatement. Take a look at the 2018 [report discussing the effect of CSPP on financing conditions for eurozone non-financial corporations](#) (NFCs). It provides plenty of proof of the excessive liking of the ECB to this private sector programme.

The ECB has made no secret of its liking of the private sector programmes

The report states 'An ample set of analytical studies attributes a sizeable part of these developments directly to the effects of the programme' and '..indirectly, the CSPP has also had positive knock-on effects on the wider financing environment for firms in the euro area'.

We view both comments as rather contentious but they do highlight how fond the European Central Bank is of CSPP. To strengthen that view, we went through [this report](#) from 2018 where the ECB discusses that, despite the absence of an explicit environmental target, the CSPP purchases have led to green corporate bond spreads steadily tightening, and they claim; 'a significant part of this effect can be attributed to the Eurosystem's purchases.'

We believe this comment is rather ambitious and self-praising to put it mildly. All spreads were tightening and the Green market was becoming mainstream with real money investors. CSPP, in essence, was nothing more than a vacuum cleaner hoovering all bonds in its wake, regardless of nationality, sector or Environmental, Social and Corporate Governance (ESG) status.

[Read the full ECB report on the effect of CSPP on financing conditions for eurozone NFCs](#)

Bank bonds 'clearly in the running'

Looking at the availability of assets, headroom in other purchasing programmes will be limited but this is not the case for corporate bonds, so in this regard, there are two reasons to be cheerful.

A new eligible asset class worth EUR 240bn is waiting for the ECB to target

Firstly, plenty of options remain in the corporate market. While the ISIN limit was set at 70%, CSPP has currently purchased only EUR 178bn (i.e. 25%) of the approximately EUR 700bn eligible non-financial corporate euro investment grade universe. And that's supplemented by an estimated gross supply of new eligible corporate bonds of EUR 150bn every year.

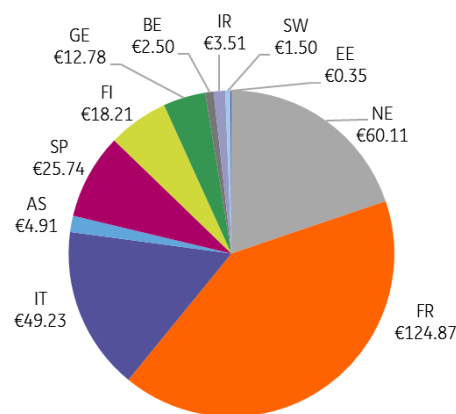
Secondly, this time, bank bonds are clearly in the running as the ECB seeks additional assets to target. And in the process, this will aid the financing cost of banks. The new sub-division of senior bank debt into preferred senior and bail-in senior (non-preferred or holding company) only helps to achieve this. Debt needs to be collateral eligible for the ECB to be able to purchase and since late December 2017, it's become clear that preferred senior bank debt will continue to fulfil this criterion.

Using that as a guide and looking at all bonds with a one year or longer maturity indicates a new eligible asset class worth EUR 305bn is waiting for the ECB to target. Added to this outstanding amount we expect an uptick in annual issuance (up to EUR 100bn) which can also be purchased.

For example, the Italian bank preferred supply would certainly increase. Looking at the charts, we see that most of the bank debt the ECB could buy would be short-dated and it's the French, Italian and Dutch banks that will benefit most from lower funding costs as 40%, 16% and 20% of the debt eligible is issued there.

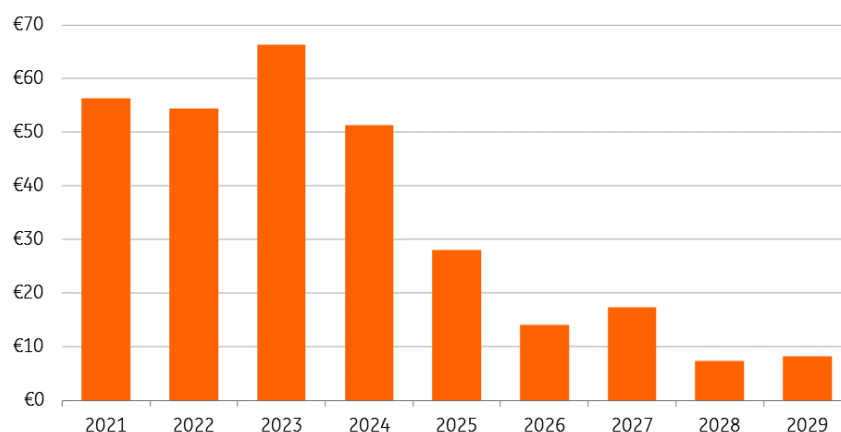
Outstanding amount of financial bonds per country (bln)

(The chart represents which countries the banks are in)



Source: ING, ECB, Bloomberg

Amount outstanding per maturity date (bln)



Source: ING, ECB, Bloomberg

ECB will enter an already crowded market

The net effect of this renewed and expanded foray into the credit markets means the ECB adds its considerable weight to a market that is already sought after. Demand is already at high levels in European credit to satisfy the need for quality yield that low rates have created.

To detractors suggesting there's little left in the ECB's arsenal, we think otherwise. The Bank clearly's got a taste for corporate bonds

In essence, as the ECB adds itself to this crowded trade, as it did in 2016, it creates a squeezed credit market. Credit spreads will be well bid, either due to the expectation of or announcement of CSPP2. Both investment grade corporate and preferred senior bank debt will benefit directly but the crowding out effect will lead to larger circles of tightening in European credit markets as yield is added but credit risk rises for real money investors. In the longer term, that could lead to a risk transfer to asset managers and pension funds.

So to detractors suggesting there's little left in the ECB's arsenal, we think otherwise. The Bank clearly's got a taste for corporate bonds and from we think CSPP will be top of its list.

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Opinion | 13 June 2019

ECB: About bazookas and water pistols

At last week's meeting in Vilnius, ECB president Mario Draghi sent a strong signal that the ECB was only one small economic slip away from new...



Source: Shutterstock

It was not so much the announced actions – new forward guidance and TLTRO pricing – which surprised financial markets last week but Draghi's comments during the Q&A session, stressing the ECB's readiness to act "if adverse contingencies were to materialise" (see our review of the ECB meeting [here](#)). The surprise moment was when Draghi actually reported that the ECB had discussed options such as rate cuts and restarting quantitative easing in such a scenario. According to Draghi, no one should have doubts about the ECB's policy space.

What could the ECB still do?

Since last week, many market participants are scratching their heads, wondering what the ECB actually still could do if it felt the need to act. Here are some thoughts:

- **Another cut of the deposit rate – the safe bet.** As long as the ECB believes that negative interest rates actually stimulate the economy and do not have significant negative effects (as suggested by a recent [ECB working paper](#) bank profitability is not affected by negative deposit rates) another rate cut looks like the easiest first option. Even without a tiering system. Combined with a tiering system, the ECB would shift away from the bank lending channel towards the fx channel, possibly bringing the Eurozone back on the US radar screen

- as a potential currency manipulator.
- **Restart QE – possible but only with some tweaks.** Another relatively easy-to-do option for the ECB. However, a valid question is how much “headroom”, as Draghi put it, the ECB really has to purchase bonds. According to [ECB estimates](#), the current reinvestments still absorb close to 30% of the planned new issuances in Germany in 2019 and 2020 but less than 15% in France, Spain and Italy. Don't forget that the 33% issuer limit was one of the main arguments used by the European Court of Justice in its ruling that QE was not monetary financing. As a result, headroom to significantly restart the sovereign bond purchases is rather limited, unless the ECB would be willing to deviate from the capital key. Instead, the ECB could either increase the issuer limit for EU supranationals (from currently 50% up to 100%) or step up its corporate bonds purchasing programme.
 - **Buying stocks – the bold option.** So far only a theoretical or rather hypothetical option but if the ECB really wanted to make a difference, buying equity – or going Japanese – would be the ultimate answer. Obviously, with many strings attached but just think of purchasing stocks, funds or baskets aimed at supporting investments into green technologies or linked to “green” ratings.

Bazooka or water pistols?

All in all, while further rate cuts and restarting QE look like the most likely policy options for the ECB in case it really feels the need to act, none of these options is a magic bullet. In fact, technical, legal or economic limitations to these two types of policy instruments bring back previous euro-crisis memories of wanna-be bazookas, which actually are rather water pistols.

Eventually, the entire discussion of whether monetary policy still can kick-start a stagnating economy in a zero-rate environment will get more attention. If bazookas turn out to be water pistols, the only resort left is fiscal policy. Probably, the only thing that could really work to fight a recession or a protracted stagnation would be fiscal stimulus backed by monetary policy. However, this would require either a Eurozone budget or loosening the fiscal rules. None looks likely in the short run.

Over the last few years, the ECB under Mario Draghi has frequently proven that no one should ever underestimate its willingness to act or simply do “whatever it takes”. At least as long as Mario Draghi is in office, there is nothing worse for the ECB than admitting it has run out of ammunition. The ECB will do everything it can to avoid such a confession. Secretly, most ECB officials will keep their fingers crossed that the ECB's determination to act will not be tested and that the Eurozone economy can avoid new slippages. If not, the next months will quickly show whether Draghi can once again overachieve or whether he has lost his magic touch.

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Australia's central bank hints at more rate cuts

The Reserve Bank of Australia's June meeting minutes describe domestic and overseas economic data as "mixed", but the outlook remained...



Source: Shutterstock

Reserve Bank of Australia Governor Philip Lowe

Key phrases of the minutes

If you've never had to comment on the minutes of a central bank before, the trick is to start at the end, with the discussion on the actual decision. The rest is usually fluff and padding. In the June meeting minutes, two key phrases in the last paragraph are:

1. Given the amount of spare capacity in the labour market and the economy more broadly, members agreed that it was more likely than not that a further easing in monetary policy would be appropriate in the period ahead. And:
2. However, lower interest rates were not the only policy option available to assist in lowering the rate of unemployment, consistent with the medium-term inflation target.

The final sentence went on to say that developments in the labour market would be of particular importance in determining future policy.

More rate cuts to come...but how much, and when?

The Australian central bank uses market rates in its modelling, and these are aggressively priced currently to show rates falling in total by somewhere between 50 and 75 basis points, which would at its extreme take the cash rate to 0.5%, which many have suggested marks the practical lower bound for the RBA.

Although we've only pencilled in a 25bp rate cut in August, we're certainly not ruling out more rate cuts in 2020, and this is where the risk to our forecast clearly lies

Even with these market rates plugged into their models (they use the market - not forecasts), the RBA's models point to only a small decline in the unemployment rate. As the RBA believes full employment now lies somewhere close to 4.5%, which implies that even aggressive easing won't enable them to meet their inflation target.

This can be interpreted in two ways. Either:

1. The only reasonable conclusion is that the RBA will have to cut quickly to 0.5% and hope that fiscal policy provides the shortfall of stimulus needed to get the unemployment rate to 4.5% and inflation moving back to target, or, and we prefer this,
2. Given rate cuts won't enable them to reach their target, and that they don't help everyone (savers for example, and pensioners on fixed interest incomes), a more cautious approach would be warranted - both slower, but also not cutting as far, whilst still looking for other policy measures (e.g. fiscal, macroprudential) to do more of the heavy lifting.

We think this interpretation is more consistent with the second key phrase we've mentioned in the RBA minutes. The text of the minutes elsewhere notes the mixed impact of rate cuts on different sections of the economy, backing up this view.

No change to our forecast for now

We have been a little less aggressive than the market with respect to our forecast over the rest of this year and next, looking only for a further 25bp of easing, probably in August after the next "Statement on Monetary Policy", which would take the cash rate to 1.0%.

The Australian economy is still in "reasonable" shape, with "mixed" rather than outright bad newsflow according to this latest assessment, so anything further would take policy into the emergency territory, and we clearly aren't in an emergency mode yet and nor do we expect to be, unless the trade war escalates another couple of notches.

That said, as 50bp of easing in total is unlikely to do more than have a very negligible impact on the unemployment rate, and hence wages and price inflation, we certainly aren't ruling out more cuts in 2020, and this is where the risk to our forecast clearly lies.

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ECB president succession: Nationality matters...sometimes

Our analysis of eurozone central bankers' communication shows nationality matters, but not really in the ECB's board. And once the appointment...



Source: Shutterstock

From L -H: Bundesbank President Jens Weidmann, former Governor of the Bank of Finland Erkki Liikanen and the Governor of the Bank of France Francois Villeroy de Galhau

When European leaders meet in Brussels this week, they won't only be discussing ways to further deepen the monetary union but also scratching their heads on how to best fill the top European jobs.

As [we've discussed](#) in detail before, an already complex musical chairs game has become even more convoluted as it also includes replacing the ECB president Mario Draghi. In the past, the ECB president was appointed in an exclusive process but due to the timing of Mario Draghi's term ending - 31 October, the position has been included in the bigger game. Nationalities, gender, political affiliations and previous jobs, everything matters.

As hard as it may be for market participants and ECB watchers to understand, leaders will first

choose the next president of the European Commission before appointing Draghi's successor.

[Read our detailed report on ECB Musical Chairs](#)

No real front runners as the presidency is part of horse trading

Given the deadlock in the talks up until now and particularly the increasing differences between France and Germany, chances have increased that this week's summit won't tell us 'who is who' in European politics.

We think it's very hard not seeing one of the Spitzenkandidaten as the next European Commission president. While the German politician Manfred Weber has the backing of the largest party in the European Parliament - the EPP, there is growing resistance against Weber. This could open the door for the Danish-born Competition Commissioner for the EU, Margrethe Vestager or the centre-left Dutch politician Frans Timmermans. If Weber doesn't get the job, chances of another German, Jens Weidmann, to take over Mario Draghi's seat increase.

In any case, while many observers believe this round of European musical chairs would bring both France and Germany a top job each, a scenario in which neither country gets one should no longer be excluded.

We think it's very hard not seeing one of the Spitzenkandidaten as the next European Commission president

Zooming in on the next ECB president, there is no real news on a front-runner. It still looks as if Draghi's successor will emerge from the group of Germany's Jens Weidmann, France's Francois Villeroy de Galhau or Finland's: Oli Rehn and Erkki Liikanen plus the outsider or compromise candidates including Klaas Knot, Ardo Hansson or Benoit Coeuré. While the European Treaties 'only' say that the ECB president (as well as all other Executive Board members) should have "recognised standing and professional experience in monetary or banking matters", it's hard to imagine any candidate without central bank experience.

[Watch our video on who'll be the next ECB president?](#)

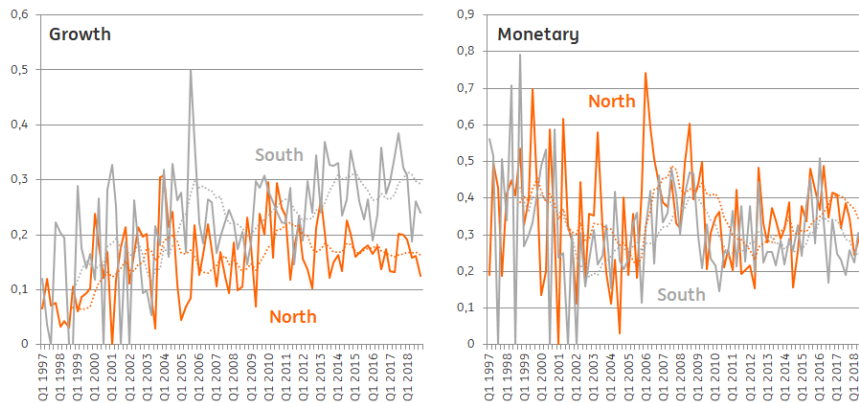
Does nationality really matter?

Officially, nationality shouldn't matter. However, given that the Draghi-succession has now become part of the bigger European horse trading, nationality will matter.

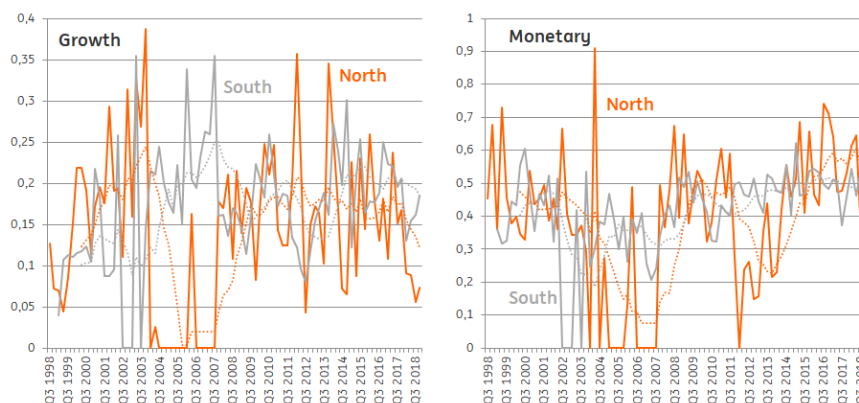
We all know of the prejudices about core European hawks and Southern European doves. To lift the issue of nationality out of the cocktail party sphere to a more analytical level, we find that that there is indeed a significant difference in terms of topics that central bankers discuss. Southern European Governing Council members are much more concerned with growth-related issues, while Northern European Governing Council members have more of a tendency to discuss monetary issues like inflation and price stability.

However, surprisingly, this national bias tends to disappear in the ECB's Executive Board, as our analysis finds that ECB board members discuss less diverging themes based on their background.

Governing council members see clear differences between South and North in terms of topical discussion in speeches



ECB executive board members have less clear divisions in terms of themes discussed in speeches



Leaving the national passport at the door

Even if the European musical chairs game currently looks set to continue after this week, giving all commentators more time and material to gossip and engage in tea-leaf-reading on who will get which job, the ECB presidency remains the most important nomination for markets.

The results of our analysis give hope that even though nationality will matter during the appointment process, the national bias won't be as significant as many ECB watchers think these days

Now that the ECB has moved towards a new easing bias, opening the door for rate cuts and other monetary action, any Draghi successor will not only be questioned and tested on “whatever it takes” but also on the continuation of the latest dovish shift. In this regards, we could see marginal differences between a more hawkish new president, let’s call him Jens Weidmann, and a more dovish president, let’s call him Benoit Coeure. This difference won't be apparent in the pace of normalisation but rather in the depth and determination of additional easing.

In the broader sense of things, the results of our analysis give hope that even though nationality will matter during the appointment process, the national bias won't be as significant as many ECB watchers think these days. Chances are much higher that the ECB president will be presidential, leaving his or her national passport behind at the security control of the EuroTower on 1 November this year.

Footnote

Our analysis of the ECB speeches is done using word count methodology based on Ernst and Merola (2018).

The vertical axis depicts the relative intensity of the topic in speeches where one means all of the speech were about a single topic. The thematic categories “monetary” and “growth” consist of five keywords central to the themes (for growth: expansion, recovery, productivity, GDP and economic growth, for monetary: inflation, interest rates, money, assets and quantitative).

The country grouping north includes Germany, Netherlands, Luxembourg, Ireland, Finland, Estonia, Lithuania, Latvia, Slovakia and Austria. The country grouping south includes Italy, Spain, France, Belgium, Portugal, Greece, Slovenia, Malta and Cyprus.

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