ECB: Between hope and facts

The minutes of the ECB's December meeting show an upbeat assessment of the economic outlook but also reflect doubts about a pick-up in inflation

Source: iStock

The press conference after the ECB meeting was short and not very eventful. The just-released minutes of the meeting, however, show that the discussion behind closed doors must have been livelier and more exciting.

Highlights of the minutes

There were three interesting points emerging from a quick read through the minutes:

- Upbeat growth forecast. For the first time, ECB members use the term "upside risk" in connection with the growth outlook. At least in the near term, "some upside risk could result from the US tax reform".
- Inflation pick-up still more wishful thinking than reality. The wording of the inflation assessment reflects a very cautious stance by the ECB. Phrases like "the steady absorption of economic slack gave grounds for increased confidence that price pressures would gradually take hold" or "...increased the level of confidence in a sustained return of inflation towards the Governing Council's aim" in our view illustrate that the ECB is not convinced,

yet. This hesitance was also reflected by the statement that "measures of underlying inflation had weakened overall and had yet to show convincing signs of a sustained upward trend" and "Caution was expressed regarding the projected pick-up in underlying inflation over the projection horizon, in particular with respect to the assumed rebound in wage dynamics".

- Dissenting views remain. The statement that "a remark was made that a gap appeared to be emerging between favorable economic conditions and a policy stance that remained in a crisis configuration" clearly shows that not all ECB members are satisfied with the current stance.

Further steps towards the exit?

Against all of the above, it is not surprising that the ECB is not ignoring further steps in its tapering (or recalibration) process. Phrase like "the language pertaining to various dimensions of the monetary-policy stance and forward guidance could be revisited early in 2018" or "the view was widely shared among members that the Governing Council's communication would need to evolve gradually, without a change in sequencing, if the economy continued to expand and inflation converged further towards the Governing Council's aim" indicate a further adjustment but in our view no abrupt end.

First another 'lower for longer', then the end

We stick to our previous view that the ECB will not stop QE in September but will rather decide on another "lower for longer" beyond September, probably until the end of the year. Interestingly, the ECB is increasingly focused on growth and seems to regard inflation only as a derivative of growth developments. Judging from previous experiences, to get an inflation rate sustainably around 2%, the Eurozone economy needs to have a positive output gap. This could, but does not necessarily have to, happen in the course of 2018.

Also, it is obvious that the ECB's balancing act between uniting the Governing Council and not distorting markets on the way towards the exit is a difficult one. While the ECB had actually tried to hush speculation with the October decision for "lower for longer", some ECB officials' talks are clearly undermining this intention. In this regards, next week should be interesting when both Jens "the hawk" Weidmann and Benoit "first proponent now advocate for a September end" Coeure will have public appearances.

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