

Snap | 14 December 2017

ECB meeting: Goldilocks can't do without QE

ECB closes the year without any surprises. In the ECB's eyes, strong growth and muted inflationary pressure give no reason to change its current stance anytime soon



No changes to rates, QE or forward guidance. No changes at all. This was the main outcome of today's ECB meeting. As expected, the ECB did not give any argument that would create doubts about its determination to fully implement its dovish tapering in 2018. If anything, ECB's macroeconomic outlook with strong growth but very little inflationary pressure currently confirms our view that we can see another 'lower for longer' beyond September 2018.

With regards to the macroeconomic outlook, the ECB acknowledged the strong growth momentum in the Eurozone economy. Already in October, the ECB stopped talking about an economic recovery. It is now an economic expansion.

2017 has been a year which many Eurozone policy-makers probably would never want to see end

Today, 'strong pace' and 'strong momentum' were the characteristics of the Eurozone economy. This was also reflected in a significant upward revision of the ECB's GDP growth forecasts to 2.4%, 2.3%, 1.9% and 1.7% for the years 2017 to 2020. Risks to this outlook remain balanced. It seems, however, as if the ECB still does not (yet) believe that strong growth will eventually translate into higher inflationary pressure. Here the new staff projections show an inflation forecast of 1.5%, 1.4%, 1.5% and 1.7% over the same period. Here, only the 2018 forecast was revised upwards, with ECB president Draghi also stating that while deflationary risks are largely gone, the risks to the inflation outlook are not balanced and remain to the downside for now.

2017 has been a year which many Eurozone policy-makers probably would never want to see end. Strong growth and low, but positive, inflation has created a Goldilocks moment in the Eurozone economy. A very comfortable situation for the ECB. However, looking into 2018, the ECB could face a more complicated world.

With central banks around the world hiking interest rates and trying to reduce monetary policy accommodation, pressure on the ECB to step up its tapering process could increase, from both the outside and the inside. Just imagine a situation in which the growth momentum strengthens further, core inflation gradually picks up and headline inflation breaches the 2%-level on the back of higher oil prices. In such a scenario, it could be hard to keep the ranks at the ECB closed.

For the time being, we stick to our base case scenario in which the ECB continues with its dovish tapering and will even announce another 'lower for longer' going beyond September 2018, ending QE by December 2018. Although Draghi commented that the ECB has not yet discussed the future of QE after September 2018. Having said this, if all of a sudden inflation, particularly core inflation was to pick up, some market participants could start doubting the ECB's sequencing and forward guidance. It is too early to tell how the ECB would then react.

Remember the metaphor of the Eurozone being the patient in intensive care? Over the last years, the ECB has been the chief physician, getting the patient into rehab and making him walk again with monetary crutches. Some ECB members have already suggested that the patient should be able to walk without crutches. Today, Draghi once again made clear that walking, even walking fast, without creating inflation was fine. A reasonable cure. Only once the patient can sprint an entire marathon will the crutches come off.

Author

Carsten Brzeski

Global Head of Macro

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 www.ing.com.