ING

Economic and Financial Analysis

ECB Crib Sheet

6 March 2018

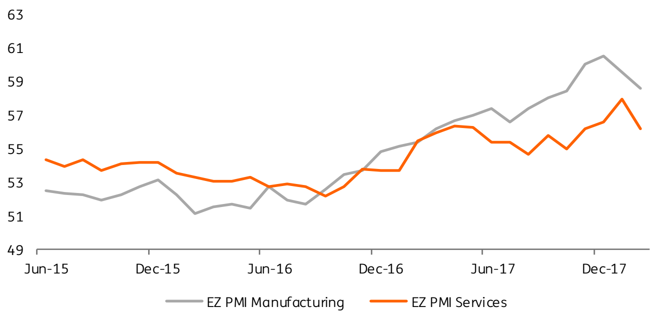
The ECB's Dashboard: Angry birds

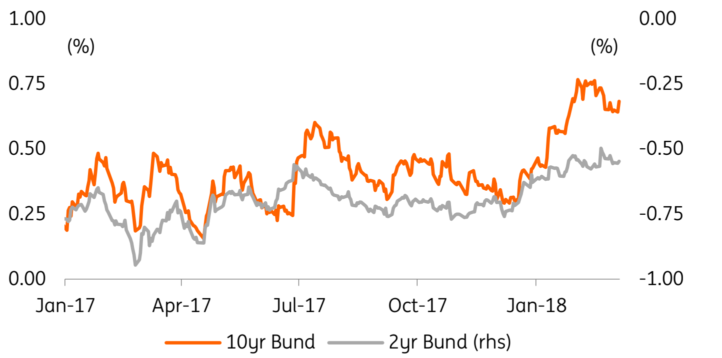
The market rout of recent weeks should not impact the ECB's assessment. The oil price and the euro developments (which interest the Eurozone's monetary policymakers more than the volatility in the stock market) suggest unchanged CPI forecast. The 2018 GDP forecast should be revised upwards.

Despite little inflationary pressure, the end of QE is getting closer. The risk of deflation is clearly behind us, and the only question is how to moderate and implement this exit.

All eyes are on the ECB's forward guidance**.** We don't expect a hint at when QE could end, but look for subtle change in the language that signals it is already en route to the exit.

The ECB's readiness to increase QE "in size and/or the duration" may be dropped and replaced by the readiness "to use all tools available", which would be a very mild form of dropping the QE easing bias. This should for now satisfy the growing dissent among the ECB hawks within the in-house bird fight.





Source: ING

What this means for markets

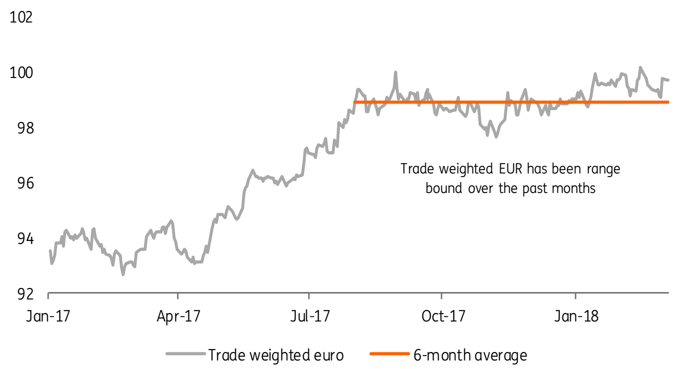
FX market: One step closer to the end of QE = higher EUR/USD

Our base case of (a) a modest shift in the ECB forward guidance, (b) no clear ECB attempts to talk down the EUR (as the euro is in fact not strong); and (c) an upward revision to the growth forecast, point to higher EUR/USD, with the cross likely to break above the 1.25 level.

The expected path of ECB policy stance holds the key towards a more pronounced EUR upside. We look through the Italian politics as the EUR sensitivity to Eurozone political uncertainty has diminished considerably.

Bond markets: Minor upside to yields

Heading into the Italian elections rates were depressed by the associated uncertainty and Trump's push for tariffs potentially triggering a trade war. Although concerns have eased somewhat, and rates have risen, markets may still be expecting a cautious ECB. Tweaking the guidance thus holds some minor upside risks to yields.



Source: ING

Scenario analysis: How to position for Draghi's alternatives

	Inflation outlook	Growth outlook	Reference to the EUR level	QE taper guidance	EUR/USD	2-year Schatz	10-year Bund
Current stance	"Underlying inflation is expected to rise gradually"	"The risks... to growth outlook are broadly balanced"	"Volatility in exchange rate is source of uncertainty ..."	ECB "stands ready to increase" QE "in size and/or the duration"			
Very dovish	**Downward revision** to (medium-term) 2020 CPI forecast	Risks to the growth outlook **to the downside**	**Unwarranted tightening** of monetary conditions	The **"size and/or the duration"** reference unchanged	1.21	-5 bp	-10bp
ING Base Case	**Unchanged CPI** forecast for 2018/19/20	**Upward revision to** 2018 GDP to 2.4%; 2019/20 unchanged	Volatility in the exchange rate represents **a source of uncertainty**	Ready to **use all tools available** (i.e., the QE ref. omitted)	1.26	+0 bp	+5 bp
Hawkish	**Upward revision** by 0.1% for 2018/19/20 CPI	2019/20 growth forecasts also **revised higher**	The EUR level is a **full reflection of fundamentals**	**No reference** to QE purchases or **available tools**	1.27	+5 bp	+10 bp
Very hawkish	**"Upside risks"** to the inflation outlook	Risks to growth outlook are to the **"upside"**	The EUR level **not a concern** to the Governing Council	**Asset purchases to end** by Sep 2018	1.29	+10 bp	+15 bp

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