

5 June 2020



THEMATIC

In this report:

Euro – ECB goes big

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Euro

ECB goes big

The European Central Bank (ECB) increased its Pandemic Emergency Purchase programme by a further €600 billion (US\$676 billion). The new package takes the ECB's total announced monetary stimulus to €1.35 trillion (US\$1.52 trillion). The ECB left key interest rates unchanged. The central bank also extended its horizon for net purchases until at least June 2021.

What can be seen here is that the ECB, just like many others, is not in any better position in getting the grasp of the full depth and breadth of the economic crisis and the pace of the recovery. In our view, the announcement, however, details what the ECB will do to support the economy.

The policy support is likely to keep markets happy, particularly as some of the economic data is improving as lockdowns are being relaxed. And in our view, the emphasis on inflation means that the good old one-needed compass is back. It also means that with the inflation forecast clearly below 2% in 2022, more monetary stimulus should not be excluded as we move ahead.

- The European Central Bank (ECB) added more fireworks into the eurozone policy. It increased the size of its Pandemic Emergency Purchase programme (PEPP) by €600bil to a total of €1,350bil. The purchases will last at least until the end of June 2021, and in any case, until the central bank's Governing Council judges that the corona crisis is over.
- Also, the ECB will reinvest the proceeds from the PEPP purchases until at least 2022. The asset purchase programme (APP) and reinvestments, as well as low-interest rates and forward guidance, remain unchanged.
- But the ECB left key interest rates unchanged. The main refinancing operations stood at 0.00%, rates of marginal lending facility were 0.25% and the deposit facility stood at -0.5%.
- The ECB said: "The Governing Council expects the key ECB interest rates to remain at their present or lower levels until it has seen the inflation outlook robustly converge to a level sufficiently close to, but below, 2% within its projection horizon."
- What can be seen here is that the ECB, just like many others, is not in any better position in getting the grasp of the full depth and breadth of the economic crisis and the pace of the recovery. In our view, however, the announcement details what the ECB will do to support the economy.
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- In its base-case scenario, the ECB projected the eurozone economy to contract by 8.7% this year, and then rebound by 5.2% in 2021 and 3.3% in 2022. This is a significant downward revision for 2020 compared with the March projections. The ECB also added the typical risk assessment to the growth outlook, which had disappeared in the April communication. The balance of risk is tilted to the downside. In two alternative scenarios, the economy would contract by 5.9% or 12.6% this year.
- With regards to inflation, the ECB predicted headline inflation to come in at 0.3% in 2020, 0.8% in 2021 and 1.3% in 2022. This muted inflation forecast was the main driver behind the decision to increase the size of the PEPP. Not too long ago, one of the executive board members called the inflation outlook as the single most important factor.
- In our view the emphasis on inflation means that the good old one-needed compass is back. It also means that with inflation forecast clearly below 2% in 2022, more monetary stimulus should not be excluded as we move ahead.

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