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An analysis of the latest economic data June 14, 2018, 8:30 am

ECB Announcement and Press Conference

ECB's APP Ends at Dec's End

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The June 14th ECB announcement was fully in line with our expectations although the details were released a little sooner than anticipated. But that's ok. The baby steps are no longer baby steps……more like long strides. The ECB not only discussed the nearing end of its bond buying program, it pulled out some calculators, did the math and made a unanimously-agreed upon decision to:

1) taper its monthly purchases after September from €30 bln to €15 bln and let those purchases run until the end of December 2018, subject to incoming data

2) call it quits on asset purchases at year-end 2018 (but the APP is now part of the tool box, "it is not disappearing"), and

3) leave the refi rate at 0.00%, the marginal lending facility at 0.25%, and the deposit facility at -0.40% "at least through the summer of 2019".

And by the way, when asked if the timing on rates includes September, President Draghi retorted "*If it includes September, we would have said September*". Still, the rate guidance supports our call for a September 2019 rate hike. That is still over a year away, but there are plenty of risks around that call, with the sequencing still a question mark (refi rate first?).

This decision, which was taken after "careful review", gives a nod to the hawks and doves on the Governing Council. Winding down the APP makes a lot of sense given that the Euro Area is on track for its 5th consecutive year of economic growth, and inflation is starting to move—albeit somewhat unsteadily— towards its target. But given that unsteady move in inflation, policy rates will stay at super-low levels at least through next summer, or "as long as necessary" to ensure inflation is aligned with the target. The warning to "Hold up….rates are staying low for a while!" helped rein in the EUR.

The press conference was not as upbeat as the FOMC's; President Draghi noted the moderation of growth of late, or the soft patch, and warned that for some countries, it may extend into the second quarter. The moderation is partly due to temporary factors, weaker external trade, and uncertainty relating to global factors, which are becoming more prominent. Wonder which factors they are thinking of? Hence, the downgrade to the 2018 growth forecast to 2.1% from 2.4% three months ago. However, there is some anticipation of positive surprises from U.S. fiscal expansion and very likely fiscal expansion in several countries in the Euro Area.

The ECB expects inflation to hover around the current level (as of May, +1.9% y/y) for the remainder of the year. Although underlying inflation remains muted, uncertainty around inflation is receding and inflation is anticipated to increase gradually over the medium term, supported by the ECB's monetary policy. In any event, inflation forecasts were revised up "*notably*" this year and next, reflecting mainly oil prices. And, when assessing whether or not inflation was durable and self-sustained, "*the answer was positive*".

Bottom Line: Stronger economic growth trends, and '*substantial'* improvement in the progress of inflation, have allowed the ECB to declare an end date for bond purchases. However, rate hikes are not anticipated until after next summer (we continue to see a September 2019 hike), and patience, persistence and prudence still holds. The ECB is now firmly on the path to normalization. Next stop: raising rates. After the bond buying ends, of course.