



**BERENBERG**

PARTNERSHIP SINCE 1590

## MACRO NEWS

07/03/19

Florian Hense, Economist | [florian.hense@berenberg.com](mailto:florian.hense@berenberg.com) | +44 20 3207 7859

### ECB GETS REAL AND LEAPFROGS AHEAD OF THE CURVE

#### Berenberg Macro Flash

**Getting real:** The ECB today reacted faster and more decisively to the weaker economic outlook than expected. To the surprise of markets and us, the ECB already announced today a new series of generous long-term liquidity injections (TLTROs) starting in September and pledged to keep all its rates at their current levels until the end of 2019 instead of just through this year's summer. We had forecast the ECB to prepare markets for such decisions today, but to wait for further data before acting in April or June. Moving now, we judge crucial a significant downgrade of the inflation projections over the entire 3-year horizon, including lowering both the headline and core inflation forecast for 2021 from 1.8% to 1.6%. The ECB also slashed its growth forecast for 2019 more than expected, moving all the way to our below-consensus growth call of 1.1% for this year (for the ECB's forecasts see Tables 1-3 and Charts 1-5).

**Effectively, the ECB has done what it could for this year, a little earlier than expected.** As a result, watching the ECB could be boring for the remainder of 2019. Previously, the ECB may have seen the glass half-full. With today's moves, it switched viewing the glass as half-empty. While there are some brighter spots (stabilising PMIs, rebounding consumer confidence and continued solid disposable income gains), the economic situation may easily get worse first. Worryingly, long-term inflation expectations have fallen significantly. Like the US Fed which had turned dovish earlier in January, the ECB wants to give the economy more breathing space. As underlying price pressures are still miles away from the 2% target, the ECB affords to act as the buffer and respond to weaker growth by extending its period of pronounced monetary accommodation.

**A new round of long-term liquidity for banks (TLTROs):** While the current TLTROs do not mature before June 2020, or even 2021, only funding with a maturity of at least one year fully counts as "available stable funding" for banks' "net stable funding ratios" (NSFR). Banks' funding costs will, therefore, be affected already from the end of June 2019 onwards. As TLTROs worth 710 billion euros mature over a period of three quarters, the ECB balance sheet – and banks' funding resources – could drop by 15% from its current level (see chart 6), leading to much tighter financial conditions – private creditors would struggle to offset the significant drop in due time and scale. As a comparison, the Fed cut its balance sheet by only about 10% since late 2017. With the new round of TLTROs the ECB relaxes the current policy stance and supports stronger credit growth instead of just extending the current level of liquidity provision. Still, the ECB intends to wean the banks off the cheap funding very gradually: the new round is shorter and (slightly) more expensive than the terms of the current TLTROs. The ECB will launch a series of 2-year TLTROs every quarter between September 2019 and March 2021 indexed at the main refinancing rate. Like the current TLTROs, the new round of TLTRO will feature "built-in incentives for credit conditions to remain favourable". The ECB will provide further details on the conditions.



## MACRO NEWS

### POLICY OUTLOOK

Today's decisions suggest that ECB policies may roughly take the following path:

- In September 2019, the ECB may update its current guidance of unchanged rates “at least through the end of 2019”, pointing markets to a first main refinancing rate hike in spring 2020 at the earliest.
- In December 2019, the ECB may announce a return to a symmetrical rate corridor by raising its deposit rate from -0.4% to -0.25% in Q1 2020 while still keeping the main refinancing rate and the marginal lending rate unchanged at 0% and 0.25%, respectively. Alternatively, the ECB may introduce a tiered system under which it will levy the full penalty on deposits held at the ECB only beyond some threshold.
- In Q2 and Q4 2020, the ECB may lift all rates by 25bp each, putting an end to a negative deposit rate and reaching a main refinancing rate of 0.5% by the end of 2020.
- Until at least the end of 2020, the ECB will fully reinvest the proceeds from maturing debt, keeping its bond portfolio constant for two years after the end of net asset purchases.

These calls rest on two assumptions: (1) by summer 2019, Eurozone growth returns to trend from the current slowdown and, (2) core inflation will edge up gradually throughout 2019.

**Table 1: Eurozone headline inflation (yoy, in %)**

	2018	2019	2020	2021
ECB new projections	1.7	1.2	1.5	1.6
ECB previous projections	1.8	1.6	1.7	1.8
Bloomberg consensus	1.8	1.4	1.5	1.7
Berenberg forecasts	1.8	1.3	1.6	-

*Bloomberg consensus taken as of today. Source: ECB, Bloomberg, Berenberg*

**Table 2: Eurozone core inflation (yoy, in %)**

	2018	2019	2020	2021
ECB new projections	1.0	1.2	1.4	1.6
ECB previous projections	1.0	1.4	1.6	1.8
Bloomberg consensus	-	-	-	-
Berenberg forecasts	1.0	1.2	1.5	-

*Bloomberg consensus taken as of today. Source: ECB, Bloomberg, Berenberg*

**Table 3: Eurozone real GDP (yoy, in %)**

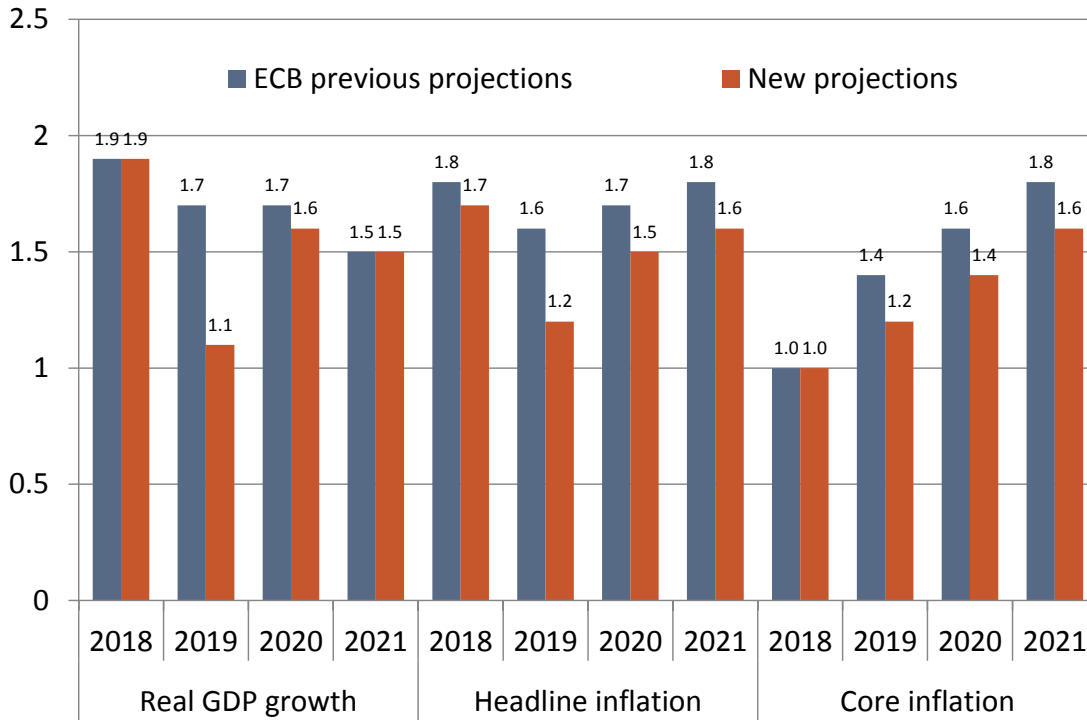
	2018	2019	2020	2021
ECB new projections	1.9	1.1	1.6	1.5
ECB previous projections	1.9	1.7	1.7	1.5
Bloomberg consensus	1.8	1.4	1.5	1.5
Berenberg forecasts	1.8	1.1	1.7	-

*Bloomberg consensus taken as of today. Source: ECB, Bloomberg, Berenberg*



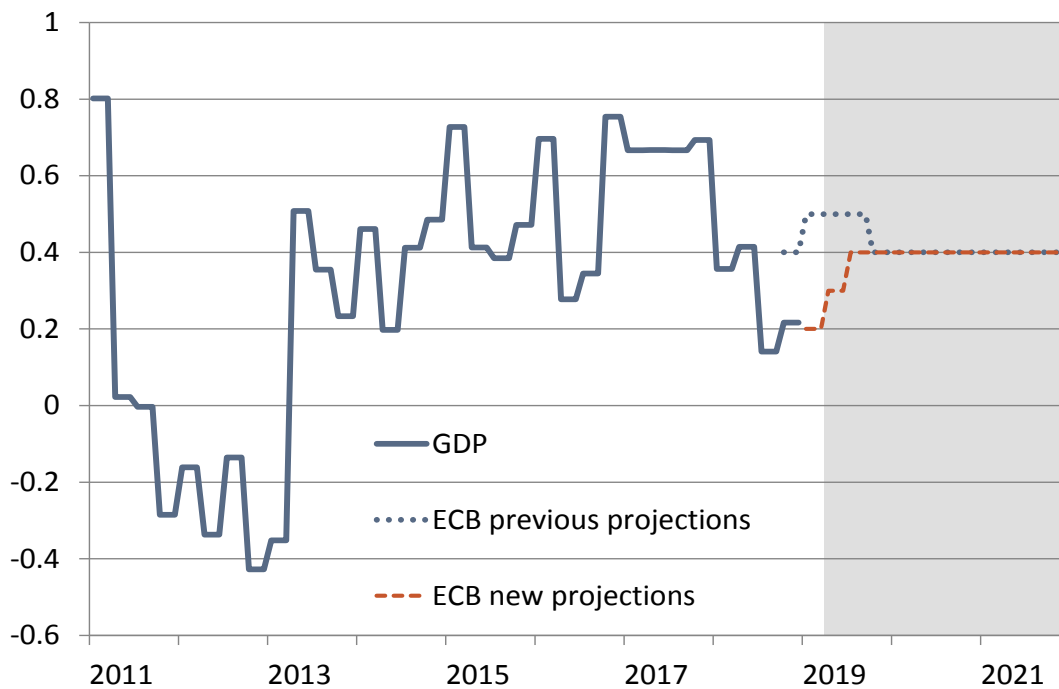
## MACRO NEWS

Chart 1: Main annual ECB projections (qoq, in %)



Source: ECB

Chart 2: Quarterly real GDP growth and ECB projections (qoq, in %)

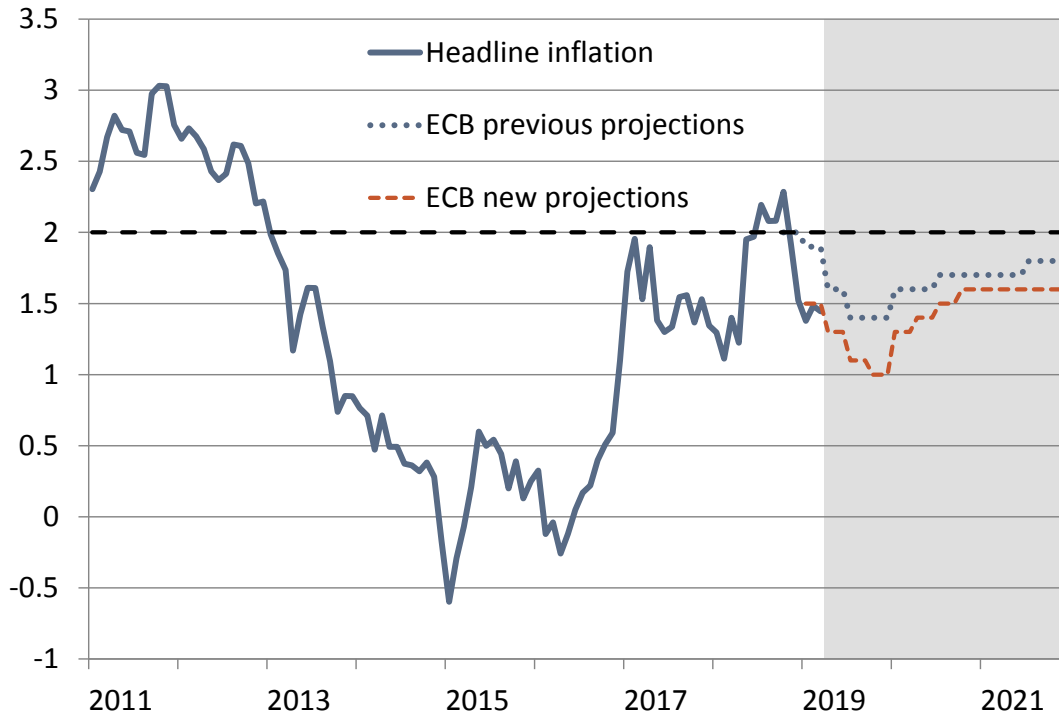


Sources: Eurostat, ECB



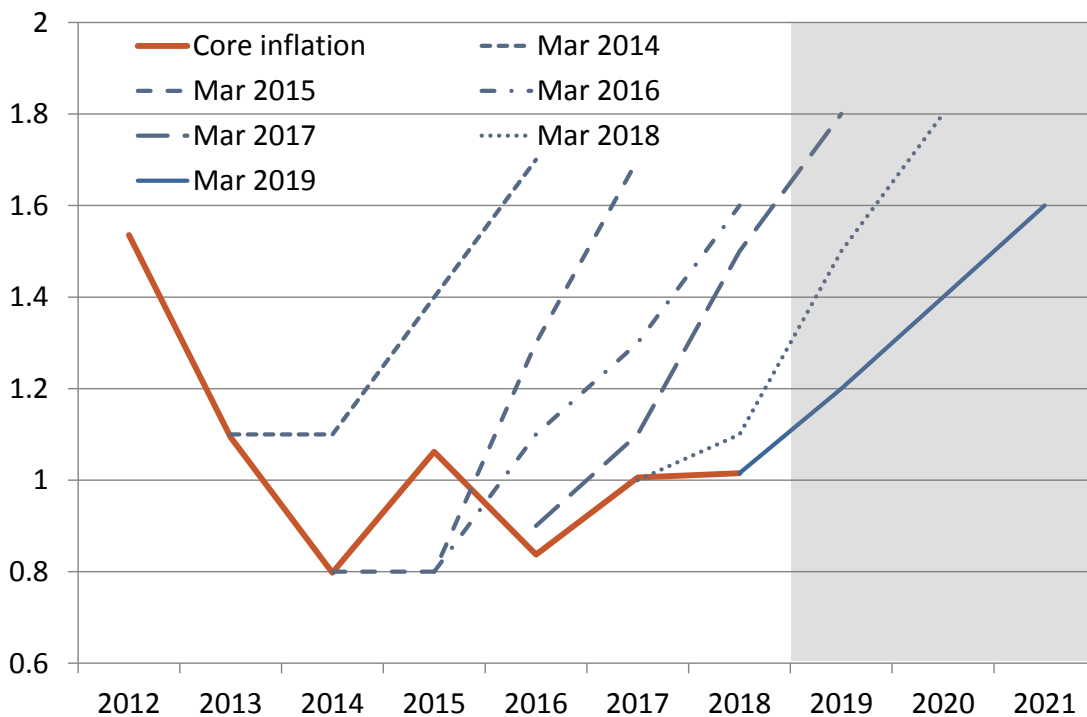
## MACRO NEWS

Chart 3: Monthly headline inflation and quarterly ECB projections (yoy, in %)



Sources: Eurostat, ECB

Chart 4: Core inflation and ECB projections (yoy, in %)

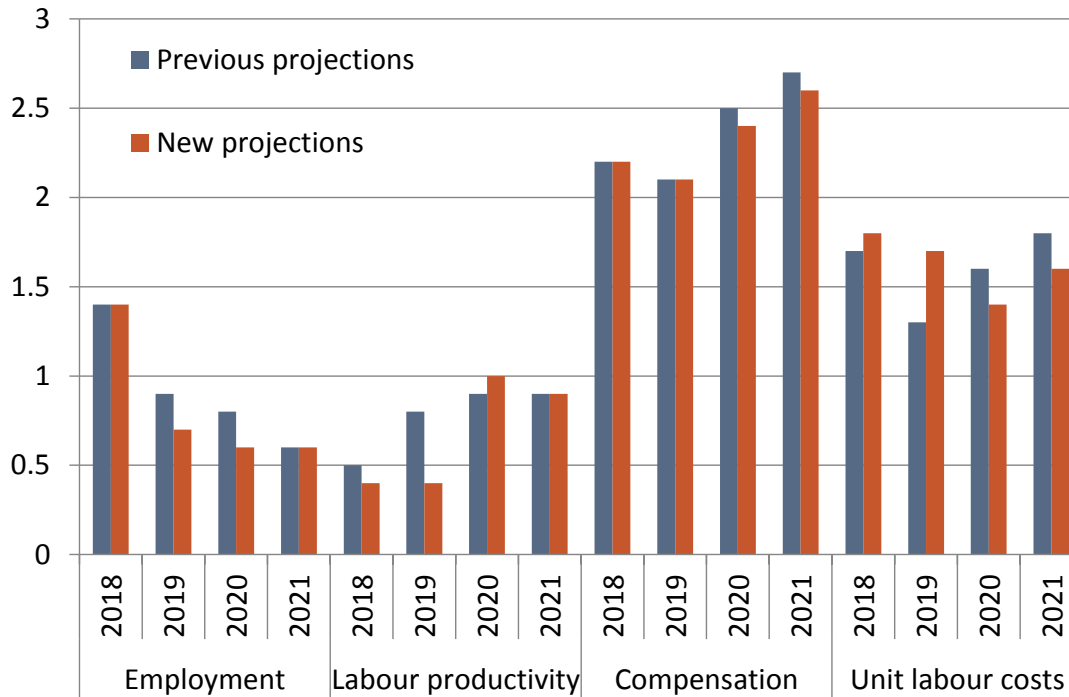


Sources: Eurostat, ECB



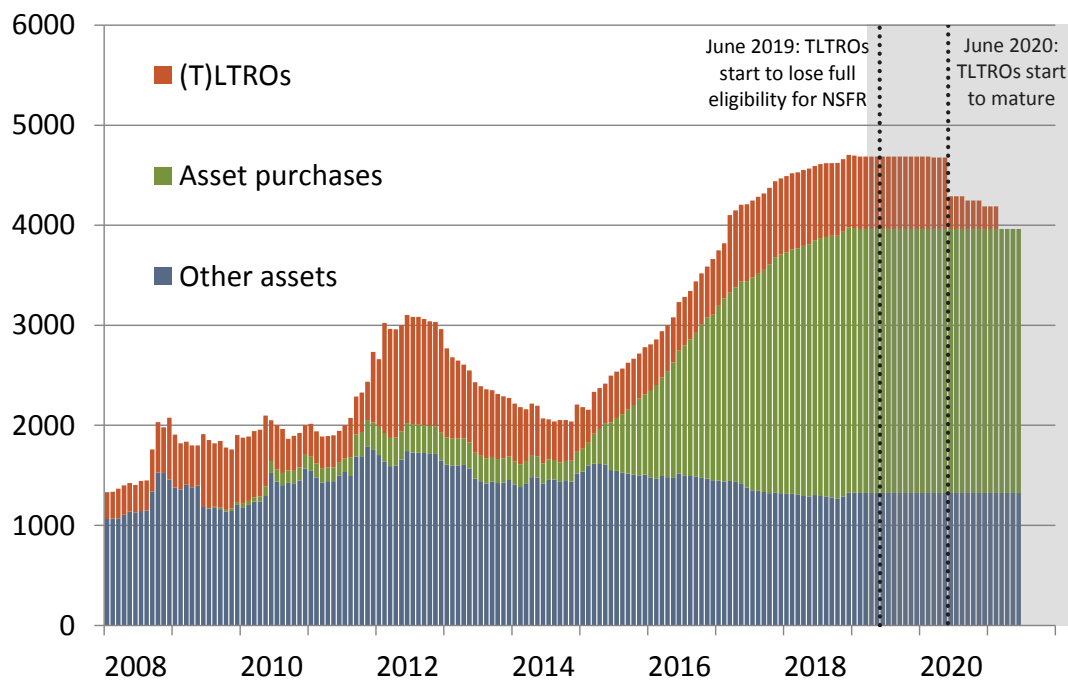
## MACRO NEWS

Chart 5: Further ECB projections (yoy, in %)



Sources: Eurostat, ECB

Chart 6: ECB balance sheet excluding the new round of TLTROs



In billion euros. Source: ECB