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ECB ON HOLD FOR SOME TIME AFTER DRAGH-ERA

Berenberg Macro Flash

On hold: After the Governing Council passed a comprehensive and highly controversial easing package at its 12 September meeting, we expect ECB policy to be on hold for the remainder of this year and for much of 2020. A divided ECB with a new President could maintain its current stance (deposit rate of -0.5%, €20bn in monthly net asset purchases and a forward guidance linked to expected and actual inflation) until 2021. At the press conference following his last Governing Council meeting this Thursday, ECB President Mario Draghi will likely downplay the serious divisions within the Governing Council. For what it is worth, he may stress that its members still sing from broadly the same hymn sheet. Christine Lagarde will likely do her best to bring all Governing Council members into line again when she takes over next month. To succeed, she will have to get the ECB's strategy review right.

Backdrop unchanged, some progress on trade and Brexit: The economic data has largely come in line with ECB and our expectations. The weakness in global trade, business investment and industrial production has broadened. Service sector surveys, employment growth and household confidence in the Eurozone are still relatively solid, but continue to soften. Price pressures remain [stuck at around 1%](#) and inflation expectations are at or close to their all-time lows. However, some recent developments suggest the Eurozone downturn could bottom out in a couple of months. While the [half-finished mini-agreement](#) between Washington and Beijing falls short of resolving the US-China tensions, it supports the hope that both sides may not want to escalate the trade war much further. With a [much lower risk of a hard Brexit](#), a further source of uncertainty for the Eurozone economy could be fading soon. A pick-up in real money growth suggests that businesses and households have the money to spend once the current pessimism gives way to a less downbeat outlook.

Draghi's last message: The ECB's September decisions to resume open-ended net asset purchases, cut the deposit rate further combined with a two-tiered system for bank reserves and strengthen the forward guidance were [highly controversial](#). Whether they will make any difference remains to be seen. That some factions within the ECB Governing Council have aired their opposition to the September decisions so forcefully and publicly could weigh on the efficacy of the package, though. Draghi will want to make the point that, despite some differences, the Governing Council members agree on many points. He will reiterate that all Governing Council members believe that the policy stance provides substantial stimulus, that the ECB stands ready to adjust its instruments and that fiscal policy should be more supportive. Markets and media may focus more on the divisions within the Governing Council, though.

Strategy review crucial to unite Governing Council: Christine Lagarde will be in listening mode when she attends the meeting this week. She takes over from Draghi on 1 November as ECB president and will chair her first Governing Council meeting on 12 December. Lagarde's most pressing job will be to bridge the divisions and ask all Governing Council members to focus on jointly ex-



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plaining the decision to the public rather than emphasising the differences. Easing US-China trade tensions and a path towards an orderly resolution of the Brexit saga would make life easier for her as it would lift pressure from the ECB to act as a buffer. But both is beyond her and the ECB's power. She will surely argue for a more balanced policy mix between the monetary and fiscal sphere. However, she may not have more success than Draghi had for the past five years on this count. The planned review of the ECB's monetary policy strategy could be of crucial importance for Lagarde to narrow the divisions within the Governing Council.

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