

ECB: REVIEWING STRATEGY WHILST WAITING FOR INFLATION

The ECB remains cautious in its assessment of the economic situation characterised by risks still tilted to the downside, although less than before thanks to the US-China trade deal. The message is slightly better on underlying inflation where some signs of a moderate increase are noted. Between now and year-end, the strategy review, which has now been launched, will grab a lot of attention, with markets wondering how it could influence monetary policy. The review is also important from the perspective of climate change: will monetary policy operations take it on board as a risk factor or will ambition even be higher?

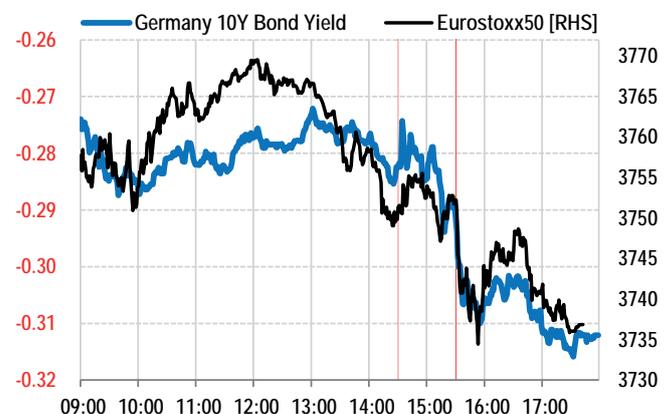
Judging by the market reaction, the ECB President's press conference this week was rather uneventful. The Euro Stoxx 50 equity index fluctuated in a narrow range of approximately 0.15% and 10 year Bund yields eased about 1 basis point. The absence of volatility is unsurprising. Firstly, monetary policy is set to remain unchanged for a long time and, secondly, the message about the economy remains cautious. At the December meeting, the assessment was that "incoming economic data and survey information, while remaining weak overall, point to some stabilisation in the slowdown of economic growth in the euro area". Now "[i]ncoming economic data and survey information point to some stabilisation in euro area growth dynamics, with near-term growth expected to be similar to rates observed in previous quarters." The change in the assessment is tiny – "while remaining weak overall" has been dropped – but, importantly, no pick-up in growth is expected in the near term. Moreover, risks remain tilted to the downside although they have become less pronounced as trade-related uncertainty is receding. The Governing Council of course welcomes that "there are some signs of a moderate increase in underlying inflation in line with expectations", although the inflation outlook remains subdued.

With monetary policy locked in a state-dependent forward guidance mode and data moving at a glacial pace, attention is shifting to the strategy review, which has now been formally launched. The scope is huge but in line with its importance. A key question is whether the mandate, whilst remaining narrow – i.e. achieving price stability – will be reformulated. One possibility would be to make it explicitly symmetric. This would require dropping the word "below" in the now well-known sentence "We expect them to remain at their present or lower levels until we have seen the inflation outlook robustly converge to a level sufficiently close to, but below, 2%". Another possibility would be to set a range within which inflation would be considered in line with the objective. Clearly, such a move would have a significant impact on policy rate expectations and bring the expected first hike forward.

Then there is the question of how climate change should be addressed by the central bank. The sheer number of questions on climate change during the press conference is in part related to the ambition that has been expressed by the ECB's President in recent statements and before the European Parliament. They also reflect an impatience of seeing how far the remit will reach: risk control in the context of financial stability or something more ambitious in the context of monetary policy decisions by steering the relative pricing of financial assets – green versus other – or even influencing the flow of credit?

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SOURCE: BLOOMBERG, BNP PARIBAS

“The large number of climate-related questions during the press conference reflect an impatience of learning how far the ECB's remit might be broadened: risk control in the context of financial stability, steering the relative pricing of 'green' versus other assets or even influencing the flow of credit.

