

ECB: October Minutes Bequeath Heavy Agenda to Lagarde

- The minutes of the October 23–24 meeting of the European Central Bank’s (ECB) Governing Council confirm that consensus eluded Mario Draghi’s last meeting as President.
- The minutes also underscore the heavy agenda ahead for Pres. Lagarde to build consensus amongst the Governing Council’s members and to press member states to deploy fiscal policy more concertedly to support the Eurozone economy in preparation for the start of the ECB’s strategic review in early-2020.
- If the Eurozone economy continues to develop in line with our forecasts presented in Scotiabank Economics’ Q4 *Global Outlook*, which it remains on track to do, we would anticipate that the ECB will keep rates on hold through to end- 2021.

DRAGHI’S LAST WALTZ WAS A DIFFICULT DANCE

The October minutes highlighted worries that the economic outlook may prove to be a shade darker than the ECB had previously forecast owing to some soft data prints between the September and October meetings. Participants noted concerns that the hoped-for recovery in inflation may be slower to materialize than projected, owing to a longer-than-expected economic trough that would extend beyond the pick-up anticipated in late-2020.

Despite this marginally more pessimistic shift of the ECB’s economic outlook from September to October, support for the package of exceptional monetary-policy measures agreed in September didn’t appear to firm up. Hawks who were opposed to Pres. Draghi’s push to restart quantitative easing appear to have remained unmoved. If anything, the respective camps seem to have become more entrenched in their views.

While there was a shared understanding in the October minutes that the new monetary policy initiatives decided in September offered enough substance and flexibility to deal with more negative developments in the outlook, this only underscored that some Governing Council members would still prefer to see a more modest package of measures. Observations that patience would be required to allow the effects of these measures to filter through the economy could be read as warnings to doves that they shouldn’t try to add to September’s suite of policy changes any time soon.

Repeated calls in the October minutes for the “unity of the Governing Council” and a strong commitment “to fully implement the September monetary-policy decisions” and to “remain prepared to act by using [the ECB’s] full set of instruments” all underscore that September’s closed-door battles and ensuing public fallout have not been resolved.

For balance, the October minutes stressed that even proponents of the September package remain mindful of its possible negative side effects. In this,

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the minutes indirectly foreshadowed cautions about excessive risk-taking in Wednesday's *Financial Stability Report* and in Vice-President de Guindos presentation of the *FSR*.

In a useful hand-off to incoming Pres. Lagarde, the minutes again called for other policymakers to shoulder more of the burden of stabilizing the Eurozone economy. The minutes repeated previous requests that governments that have fiscal space should use it. The minutes observed that the Eurozone's fiscal stance is already mildly expansionary. However, this stance may not be sustained owing to constraints under the monetary union's stability and growth pact, which imply a need in some large member states—even in Italy and Spain—to tighten fiscal policy.

SEEDS OF DOUBT ON WHATEVER, AS LONG AS, IT TAKES

So far, newly-minted ECB Pres. Lagarde has remained publicly mute on monetary policy, which has left a vacuum that more hawkish Governing Council members have filled. As a result, the pleas for unity, commitment, and patience detailed in the October minutes have not been realized.

Over the last few weeks, some of the same Governing Council members who dissented from the package of measures agreed in September have voiced their views that policy rates should not and even cannot go much lower, noting that they may have already lost effectiveness. Others have reiterated their wariness of unconventional policy measures in general, and their reluctance to implement any further action. ECB Chief Economist Philip Lane provided a lone public pushback yesterday in an interview on the *FSR* in which he argued that the limit on exceptional measures hasn't been reached yet.

The dissension before, during, and after the September and October meetings has put a sharp point on the need to make good on the October minutes' call for consensus and unity. At present, the ECB is neither providing clear forward guidance nor an indication of the ways in which it is data dependent. The recent and much-tweeted offsite retreat taken by Pres. Lagarde and the Governing Council may have provided a first step on this path.

ECB EXPECTED TO REMAIN ON HOLD

Given this lack of direction since the November 1st passing of the baton from Pres. Draghi to Pres. Lagarde, markets have cut back the implied probability of a cut at some point during the next year from around 60% to just above 40%. Data have also improved since the October meeting recounted in the minutes and are in line with our forecasts presented in Scotiabank Economics' Q4 [Global Outlook](#).

Purchasing-managers' indices and real GDP growth have come in a bit better than previously expected, owing largely to improved economic activity in Germany that was underpinned by strong export growth to the United States. US consumers and businesses continue to exhibit early-cycle indicators that imply they have substantial room to sustain demand over coming quarters. Ballooning US fiscal deficits and a strong US dollars are also stoking demand for imports. In contrast, German exports to China have been nearly flat. Even marginal further easing in global trade uncertainty would help to sustain this performance going forward. Still, price pressures remain muted, even though tighter labour markets are fuelling some Eurozone wage increases that are running well ahead of inflation.

If the Eurozone economy remains on its current trajectory, we continue to anticipate that we would not foresee a change in rates by the ECB before end-2021. September's package of measures should see the ECB through Brexit, the November 2020 US elections, and even a slightly-slower than forecast gentle rebound in the Eurozone economy.

WHAT'S AHEAD FROM PRES. LAGARDE: IT'S MAINLY FISCAL

Pres. Lagarde's speech on Friday (tomorrow) in Frankfurt provides an opportunity to sketch out some preliminary visions for the future. Although some commentators anticipate an expression of a few initial views on monetary policy, we think it unlikely that she would first raise her colours in this forum rather than with the Governing Council and in its related communications. Instead, we expect her to stick to issues on which consensus already exists, such as the need for more fiscal stimulus in the Eurozone. She may also look ahead to the ECB's strategic review that begins in 2020 and outline issues for consideration. The review could provide a rallying point for the Governing Council even as it confronts difficult points such as the need to raise the public-issuer limits on its asset purchases programme and attempts to follow through on Pres. Draghi's push to move the inflation target from "below, but close to 2%" to a symmetric target around 2%.

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