

Contributors

Juan Manuel Herrera

Senior Economist/Strategist

Scotiabank GBM

+44.207.826.5654

juanmanuel.herrera@scotiabank.com

ECB: Unsurprising Hold with Unchanged Guidance

The ECB did not surprise anyone in today's policy announcement. This is somewhat surprising in a way, as policymakers around the globe have often startled markets during the current tightening cycle; maybe it's just late/end-cycle dynamics. This is not a thrilling write-up, unfortunately. All settings, be it policy rates or balance sheet reduction policy, were left unchanged, and outside of minor inconsequential adjustments (and no discussion of forecasts), the decision statement is practically identical to September's.

All economists surveyed by Bloomberg were on board with a rate hold, and the 3bps that markets had priced in for today represented a widely-shared view among traders that there would be no increase. According to Lagarde, the decision to hold rates was unanimous. After getting a 'win' at the September decision with a 25bps hike to 4.00%, the hawks in the Governing Council agreed with the doves that they should at least watch data a bit longer.

The main unknown going into today's announcement was whether the ECB would announce a change to its PEPP reinvestments timetable, or even adjust minimum reserve requirements. But, the ECB still intends to continue the full reinvestment of proceeds from maturing assets under its PEPP "until at least the end of 2024." At the post-statement presser, Lagarde even went as far as saying that PEPP parameters and minimum reserve requirements were not discussed at this meeting and did not elaborate on when these items may be addressed. The 'status quo' maintenance was the highlight for markets, welcomed by a rally in European debt (more below).

Usually, with a carbon copy statement, Lagarde and de Guindos's press conference tends to deliver key quotes that shake markets up. Again, no fireworks here aside from Lagarde noting PEPP/MRR was not discussed. The ECB President highlighted the weakening of the services sector, with a slowdown in job creation in this industry, a decline in measures of underlying inflation, and increasing funding costs for banks among a series of headwinds or evidence that shows their policy tightening is being "transmitted forcefully". She also said that external tightening (read run-up in US/global yields) is not due to the Eurozone's economic fundamentals but it does spill over and has a tightening impact that needs to be taken into account.

Today's ECB decision was a placeholder. External developments like geopolitical risks or the steep climb in yields (or periphery-core widening) of the past few months may have stayed the bank's hand from tinkering with some settings or even letting something more hawkish slip-out in the press conference. On PEPP and reserves, the ECB may also be waiting for the discussion on its framework review to pick up, which is a late-2023/early-2024 matter.

Overall, inflation and economic data have evolved in line with what the ECB had projected in September (if not worse, in some cases). But it's only been six weeks since they rolled out these forecasts. The Governing Council can't be too confident that the current stance is adequate, leaving the door open to more hikes (though barely ajar), but the economy also looks fairly weak and piling on with faster/sooner QT or measures that tighten bank lending further would not have been appropriate.

A huge collection of data between now and the December 14th meeting awaits: Q3 GDP, Oct/Nov CPI, two ECB consumer surveys, and one PMI release among others. We expect the ECB to begin lowering rates in late-Q2, to end 2024 with a 3.25% deposit rate (75bps in cuts).

Market reaction (vs pre-statement, 10ET/15UK at writing):

- The ECB's statement came out at 8.15ET/13.15UK, followed by US data (namely Q3 GDP) at 8.30ET/13/30UK, and then Lagarde's presser starting at 8.45ET/13.45ET, so it's a tricky read of the reaction in markets, which when set against the moves in US markets looks relatively muted.
- Briefly, European government bonds and short-term rates markets rallied, and the EUR held vs the USD but weakened versus the GBP. The bulk of these moves took place after the release of US GDP, jobless claims, and durable goods data.
- EURUSD is practically unchanged at 1.0535/40 and EURGBP is down about 0.2% to 0.8700. German 2s are down 5/6bps and 10s are down about 4bps, compared to USTs down 6/7bps and 5bps, respectively. The spread between German and Italian 10-yr yields narrowed slightly, by 2/3bps to just around 200bps. Market pricing for the December meeting is practically unchanged around 3bps, but end-2024 ECB rates are seen 7bps lower on the day, to 68bps or somewhat about two and a two-thirds cuts from the current peak.

This report has been prepared by Scotiabank Economics as a resource for the clients of Scotiabank. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Scotiabank nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

These reports are provided to you for informational purposes only. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap or trading strategy involving a swap or any other transaction. The information contained in this report is not intended to be, and does not constitute, a recommendation of a swap or trading strategy involving a swap within the meaning of U.S. Commodity Futures Trading Commission Regulation 23.434 and Appendix A thereto. This material is not intended to be individually tailored to your needs or characteristics and should not be viewed as a “call to action” or suggestion that you enter into a swap or trading strategy involving a swap or any other transaction. Scotiabank may engage in transactions in a manner inconsistent with the views discussed this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

Scotiabank, its affiliates and any of their respective officers, directors and employees may from time to time take positions in currencies, act as managers, co-managers or underwriters of a public offering or act as principals or agents, deal in, own or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to securities or related derivatives. As a result of these actions, Scotiabank may receive remuneration. All Scotiabank products and services are subject to the terms of applicable agreements and local regulations. Officers, directors and employees of Scotiabank and its affiliates may serve as directors of corporations.

Any securities discussed in this report may not be suitable for all investors. Scotiabank recommends that investors independently evaluate any issuer and security discussed in this report, and consult with any advisors they deem necessary prior to making any investment.

This report and all information, opinions and conclusions contained in it are protected by copyright. This information may not be reproduced without the prior express written consent of Scotiabank.

[™] Trademark of The Bank of Nova Scotia. Used under license, where applicable.

Scotiabank, together with “Global Banking and Markets”, is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including: Scotiabank Europe plc; Scotiabank (Ireland) Designated Activity Company; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Derivados S.A. de C.V. – all members of the Scotiabank group and authorized users of the Scotiabank mark. The Bank of Nova Scotia is incorporated in Canada with limited liability and is authorised and regulated by the Office of the Superintendent of Financial Institutions Canada. The Bank of Nova Scotia is authorized by the UK Prudential Regulation Authority and is subject to regulation by the UK Financial Conduct Authority and limited regulation by the UK Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia's regulation by the UK Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorized by the UK Prudential Regulation Authority and regulated by the UK Financial Conduct Authority and the UK Prudential Regulation Authority.

Scotiabank Inverlat, S.A., Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, and Scotia Inverlat Derivados, S.A. de C.V., are each authorized and regulated by the Mexican financial authorities.

Not all products and services are offered in all jurisdictions. Services described are available in jurisdictions where permitted by law.