

ECB preview

Acknowledging downside weakness = A rate cut

- At next week's ECB meeting on 17 October we expect the ECB to deliver yet another rate cut of 25bp, bringing the deposit rate to 3.25%. Weaker-than-anticipated growth indicators, as well as a decline in inflation, support the case for another rate cut from the ECB.
- Since the US labour market report last week, markets have significantly repriced expectations for policy easing across central banks, not least the ECB. Markets are now discounting an additional 47bp of rate cuts this year, consistent with a rate cut next week and again in December, and 97bp of rate cuts next year, consistent with our baseline of quarterly rate cuts of 25bp each.
- We expect very limited forward guidance at the upcoming meeting, meaning the ECB should stick to the 'meeting by meeting' and 'data dependent' approach that it has been following in the past few quarters. Ahead of the December meeting, where it will give new staff projections, including the 2027 projection, we are set to see very important data points from the euro area (2x PMIs, 2x inflation, wage data, labour data).

Weaker growth and moderating labour market...

Since the latest ECB meeting five weeks ago on 12 September, the ECB has received only a very limited amount of new data. However, this data has showed convincing signs of weaker growth and moderating labour market dynamics in Q3, that may extent into the current and coming quarters. Since the September meeting, the composite PMI indicator fell to 49.6 from 51.0 in August. The decline was largely driven by services moving lower from 52.9 to 51.4, where a part of the move can be explained by the one-off boost to French activity from the Olympic games disappearing in September. Overall, the service sector remains in expansionary territory, but it has weakened during the past quarter due to Germany and France while Spain is experiencing higher activity. For details, see *Research euro area - Southern Europe to continue outperforming*, 23 September.

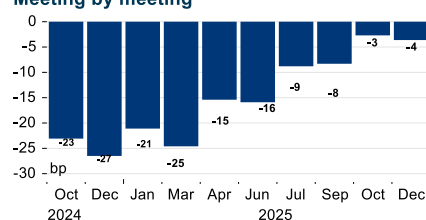
Outside services, the manufacturing sector continues to struggle, with, for example, PMIs declining from 45.8 to 45.0. Given the long period with declining production, the employment situation has also clearly deteriorated, with the employment PMI at 46.1. The weak employment situation in the manufacturing sector has impacted the aggregate euro area labour market, where survey data into Q3 shows cooling employment growth in the euro area. Please see *Research euro area - Moderating labour market with downside risks*, 3 October. The moderating labour market and weakening growth support our expectations for a cut by the ECB in October.

...combined with softer inflation supports October cut

Headline inflation fell below 2% for the first time in three years to 1.8% y/y in September, as expected. The decline was mainly due to energy inflation while core inflation was stickier at 2.7% y/y (prior: 2.8%) due to high services inflation at 4.0% y/y and low goods inflation at 0.4% y/y. Importantly, momentum in services inflation declined significantly

ECB pricing

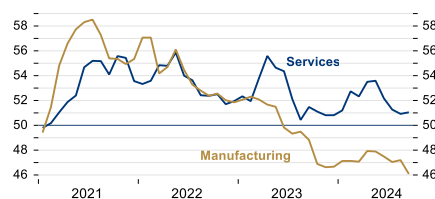
Meeting by meeting



Source: Macrobond Financial and Danske Bank

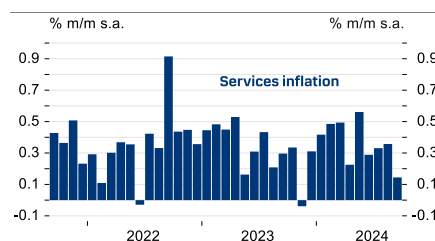
Labour market is moderating

PMI employment



Source: S&P Global, Macrobond Financial

Monthly services price increases fall to lowest rate this year



Source: ECB, Macrobond Financial

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as service prices rose only 0.1% m/m s.a., which was the lowest monthly rate this year. Headline inflation has averaged 2.17% in Q3, below the expectation of 2.3% in the latest ECB projections. Combined with the weakening of the services momentum, this should make the ECB more confident of inflation returning persistently to target.

Weak growth outlook risks the ECB

We see the good inflation news as welcome information for the ECB, albeit the weakness observed on the activity side may be viewed with some concern. If the near-term growth weakness extends into the months to come, and thus downside risks to growth materialise with domestic demand not picking up, we may consider a frontloading of the rate cuts next year – and potentially add a degree of ‘insurance cuts’, i.e. cutting the deposit rate below 2%. Markets have already priced this probability at 44%, see also *Reading the Markets EUR: Yield Outlook - From restrictive to neutral. Sell 15Y Finland*

Two weeks ago, when we pencilled in an October rate cut expectation following the weak PMIs and country inflation releases, we also noted that a reversal to the quarterly rate cut profile next year would be contingent on an improvement in the growth outlook. Admittedly it is an uncertain outlook, not least due to the impact from a stagnating labour market in Q3. Should the labour market soften significantly, that would constitute another catalyst for another revision. For now, we point to near-term downside risks to the profile and assign a 30% probability of a January rate cut as well.

Higher rates since the September meeting

Markets have recorded a high degree of volatility since the September meeting, with a low-to-high December €STR 2025 pricing range of 33bp. Looking at the rates pricing in isolation, the 10y GDP weighted yield is up 11bp since the September ECB meeting. Most recently the inflation pricing surge has led to a decline in real rates, to its average since this summer of around 40bp (measured on 5.5. real rate).

Looking ahead, less supportive rate differentials, instability in risk sentiment, geopolitical tensions, and US election tail risks suggest that EUR/USD could remain under pressure in the short term. The current divergence in economic activity – stronger in the US and weaker in the euro area – is weighing on the cross. This trend, along with several USD-positive factors currently in play, supports our overall narrative of a lower EUR/USD over the coming year, with a 12M target of 1.07.

Euro area data overview

Inflation (%)		Mar/24	Apr/24	May/24	Jun/24	Jul/24	Aug/24	Sep/24	Last 12 obs
Headline (YoY)		2.4	2.4	2.6	2.5	2.5	2.1	1.8**	
Core (YoY)		2.9	2.7	2.9	2.8	2.8	2.7	2.7**	
SuperCore (YoY)		3.1	2.9	2.9	2.9	2.7	2.9		
Services (YoY)		4.0	3.7	4.1	4.1	4.0	4.1	4.0**	
LIMI (Domestic inflation, YoY)		4.4	4.3	4.4	4.3	4.3	4.2		
Headline (MoM)		0.2	0.1	0.1	0.1	0.3	0.1	0.0**	
Core (MoM)		0.3	0.1	0.4	0.2	0.3	0.2	0.1**	
SuperCore (MoM)		0.2	0.2	0.3	0.3	0.3	0.3		
Services (MoM)		0.5	0.2	0.6	0.3	0.3	0.4	0.1**	
Economic Growth									
GDP ¹	... QoQ (%)	0.3	0.2	0.2	0.2				
PMI	... Composite	50.3	51.7	52.2	50.9	50.2	51.0	49.6	
	... Manufacturing	46.1	45.7	47.3	45.8	45.8	45.8	45.0	
	... Services	51.5	53.3	53.2	52.8	51.9	52.9	51.4	
IFO	... Current	88.1	88.9	88.3	88.3	87.1	86.4	84.4	
	... Expectations	87.6	89.7	90.3	88.8	87.0	86.8	86.3	
ESI	Index	96.3	95.6	96.2	96.0	96.0	96.5	96.2	
Eurocoin	...%	0.2	0.3	0.2	0.2	0.2	0.3	0.1	
	Consumer Confidence	-14.8	-14.7	-14.3	-14.0	-13.0	-13.4	-12.9	
Labour Market									
%	Employment	0.3	0.2	0.2	0.2				
QoQ (%)	Unemployment ¹	6.5	6.4	6.5	6.5	6.4	6.4		
	Labour Force ¹	0.0	0.4	0.4	0.4				
	Negotiated Wages ¹	4.8	3.5	3.5	3.5				
YoY (%)	Job Postings Wages	3.5	3.5	3.4	3.9	3.9	4.1		
	Comp per Employee ¹	4.8	4.3	4.3	4.3				
Labour Shortage	... Industrials ¹	19.7	19.3	19.3	19.3				
	... Services ¹	27.6	26.4	26.4	26.4				
	EC Employment Expectations Indicator	102.4	101.5	101.2	99.8	97.9	99.4	99.5	
Credit									
%	BLS credit standards ¹	3.3	2.5	2.5	2.5				
YoY (%) - loan growth	Non-Financial corporations	0.3	0.2	0.3	0.7	0.6	0.8		
	Households	0.2	0.2	0.3	0.3	0.5	0.6		
YoY (%)	Euro Area M1	-6.7	-5.9	-5.2	-3.5	-3.1	-1.9		
	Euro Area M3	0.9	1.4	1.6	2.4	2.5	3.2		
Financial indicators									
% (eom)	10y Bund	2.3	2.6	2.6	2.5	2.3	2.3	2.1	
	10y GDP weighted rate	2.8	3.1	3.1	3.1	2.9	2.9	2.7	
% (eom), HICP	10y GDP wght. real rate	36.3	37.7	37.6	43.6	44.3	44.7	48.1	
	10y GDP wght. real rate	59.5	77.3	86.7	91.4	76.8	84.1	75.5	
bp (eom)	BTP-Bund Spread	141.0	134.0	131.0	157.0	134.0	139.0	125.0	
YoY (%) (eom)	Stoxx600	12.0	8.2	14.7	10.7	9.9	14.6	16.1	
	Stoxx50	17.8	12.9	18.2	11.3	9.0	15.4	19.8	
Spot rates	EER (YoY %, eom)	3.0	1.9	3.5	0.7	0.9	1.2	2.3	
	REER (YoY %, eom)	2.0	0.3	1.2	0.3	-0.6	-0.4	0.1	
	EURUSD (YoY %, eom)	-0.6	-2.4	1.6	-1.5	-1.8	2.0	5.7	
Energy & commodities									
YoY (%) (eom)	Commodities index	11.1	13.3	18.4	15.0	0.2	-2.1	-6.1	
	Energy index	20.1	20.2	25.1	24.9	3.4	-3.7	-14.9	
EUR/MWh (eom)	TTF NatGas	27.1	29.0	34.1	34.1	35.1	38.8	39.0	
USD/bbl (eom)	Brent oil	87.5	87.9	81.6	86.4	80.7	78.8	71.8	

¹Indicates release is flash, and not final.
 Superscript with the number * 1 indicates data is released in quarterly intervals, hence the border marking new releases reflects this.
 Sources: ECB, Eurostat, Macrobond and Danske Bank.

Forward looking indicators

Inflation		Oct/24	Nov/24	Dec/24	Jan/25	Feb/25	Mar/25	Apr/25
YoY(%)	Inflation market pricing	1.7	2.0	2.2	2.1	1.8	1.8	1.8
SMA* and market pricing		Oct/24	Nov/24	Dec/24	Jan/25	Feb/25	Mar/25	Apr/25
%	Market priced deposit rate (€STR+10bp)	3.28		3.02	2.81		2.56	2.41
bp	- change	-23		-26	-21		-25	-15
	SMA DFR	3.50		3.25	3.25		3.00	3.00
	SMA TLTRO	29	29	29				
EURbn	SMA PEPP	1669	1669	1669	1624	1624	1624	1579
	SMA APP	2888	2888	2888	2804	2804	2804	2721
SPF*		2024	2025	2026	Long Term	Released since last ECB meeting		
	SPF HICP	2.4	2.0	2.0	2.0	No		
YoY%	SPF HICP, Core	2.6	2.1	2.0	2.0	No		
	SPF Real GDP	0.6	1.3	1.4	1.3	No		
Latest ECB Staff Projections		Q4/2024	Q1/2025	Q2/2025	Q3/2025	Q4/2025	Q1/2026	Q2/2026
	HICP	2.6	2.5	2.3	2.2	2.0	2.0	1.9
YoY%	HICP CORE	2.9	2.7	2.4	2.2	2.1	2.1	2.0
	GDP	0.2	0.3	0.4	0.4	0.4	0.4	0.4

*SMA is latest release, coinciding with latest ECB meeting. SPF is latest release.
 Blank cells under SMA and market pricing indicate no ECB GC meeting that month.
 Sources: ECB, Eurostat, Macrobond and Danske Bank.

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None

Date of first publication

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