

# ECB Preview

## Time for a strategic review—not monetary policy messages

- **The December ECB meeting, which will be Lagarde’s first meeting as chair, is set to focus on the strategic review. With forward guidance and new QE purchases already set for the coming months, no change in monetary policy is expected for the near future.**
- **Markets are likely to trade sideways through the press conference. We doubt specific details of the strategic review will be announced but we hope for at least some scope. We do not expect a deadline to be announced.**
- **We recommend Bund ASW widenings and periphery spread tightening as main ECB QE trades next year. We do not expect next week’s meeting to ‘rock the boat’.**

### Strategic review – still within price stability

Lagarde’s EP hearing on Monday did not include any views or guidance on what the review may entail. We welcome the exercise as the previous review took effect in 2003. We have heard from many GC members that they welcome the review, but very few have been specific on what it may entail. Only Holzmann (Austria) has voiced concretely what a review may entail. In his view, it should lead to a lowering of the inflation target to 1.5%.

Generally, we argue that there are two ways to do it: a short and brief review or a large overhaul. ECB chief economist Lane said to Bloomberg that ‘the best type of review has a clear focus, knows its ambitions, and it’s not so extensive that it becomes impossible to conclude.’ We do see good arguments for a short and brief review, which could lead to a simple clarification of symmetry (e.g. deletion of ‘below’) or going back to the pre-2003 mandate (e.g. deletion of ‘close to’), but we favour a large overhaul. This is due to the scope, as it may also include which variables to target. For example, the increased volatility in the energy component in the inflation basket has resulted in the ECB’s reaction being dependent on core inflation, so targeting the core inflation (at a lower level than 2%) could be warranted.

### Focus on Green – but not for the central bank in our view

Undoubtedly, policy makers have picked up comments on the sustainability debate in recent weeks and months, of which Lagarde is a proponent. While we generally side with the Bundesbank president on the green QE debate (green / sustainability is a structural change and QE should be used to address a cyclical problem), we welcome the debate if it reflects a change in the underlying economy. Naturally, the central bank should be wary of structural changes to the economy, but as such the EU has a large number of institutions whose mandate is closer to climate effort than the ECB (such as EIB and most recently the EC that wants to create a fund that can facilitate up to EUR100bn of green investments). In our view, the ECB has only one mandate. That said, with Lagarde as president, we cannot rule out a more prominent role for green in the ECB going forward.

#### 12 December ECB meeting (CET)

- 13:45 Decision
- 14:30 Press conference
- 15:30 Technical document (exp)

#### All in scope?

- Change to price stability (‘below, but close to, 2%’)
- Precision of inflation level to target
- Price level targeting (allowing for over / undershooting)
- What metric to target (core, headline, super-core)
- Dot plot / framework discussion

#### Type of review

	Minor revision	Large overhaul
Strategy review	Changing mandate to pre-2003 definition of ‘below 2%’ HICP or clarification of symmetry	All ‘price stability’ definitions possible (Medium-term, average inflation, price level target). All target variable fulfilling ‘price stability’ (HICP, core, super-core)
Market impact	Unknown. Will depend on outcome of the	Unknown. Will depend on outcome of the
Time horizon	6-9 months	12-24 months

Source: Danske Bank

#### Senior ECB Strategist

Piet P. H. Christiansen  
+45 45 13 20 21  
[phai@danskebank.com](mailto:phai@danskebank.com)

#### Senior Analyst

Aila Mihr  
+45 45 12 85 35  
[amih@danskebank.com](mailto:amih@danskebank.com)

## Market impact and risks to review

The repercussions of a strategic review are set to affect markets. All things equal, a review might lead to higher volatility given the uncertainty related to it. Depending on the scope of the exercise, which we hope will be published next week, the review may last between 6-24 months.

At the same time, it is important to highlight the risk of the discussions being ‘hijacked’ by near-term monetary policy implications, as there is a risk that GC members may voice their opinion taking into account the near-term policy implications.

## Staff projections to underpin narrative for now

Since September, the clouds on the euro area macro outlook have started to lift. A no-deal Brexit has been avoided, further trade war escalations have not materialised and market-based inflation expectations have retraced somewhat from all-time lows. Q3 GDP growth has surprised on the upside (0.2% q/q versus 0.1% q/q projected by the ECB), which will be reflected in an upward revision of the ECB’s 2019 growth forecast to 1.2%. Similarly, a slightly higher oil price and a weaker effective EUR are likely to boost the HICP forecast for 2020 to 1.1%. With the ECB firmly on pause for now, **we expect the new forecasts to underpin the narrative that no further easing is warranted at the current stage and that the inflation outlook is still on track towards the medium-term aim.**

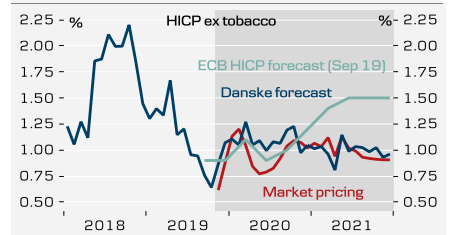
### Growth and inflation outlook to take a beating

ECB projections December 2019	2019	2020	2021	2022
GDP growth	1.2% (1.1%) ↗	1.2% (1.2%) →	1.4% (1.4%) →	1.4%
HICP inflation	1.2% (1.2%) →	1.1% (1.0%) ↗	1.5% (1.5%) →	1.6%
Core inflation	1.0% (1.1%) ↘	1.2% (1.2%) →	1.5% (1.5%) →	1.6%

Parenthesis are the old ECB projections (from September 2019)

Source: ECB, Danske Bank

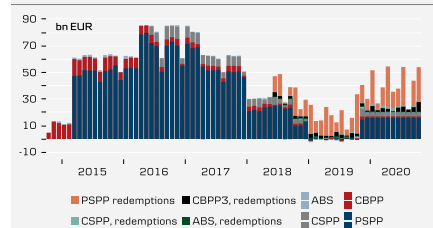
### ECB inflation target remains as elusive as ever



Source: ECB, Eurostat, Danske Bank

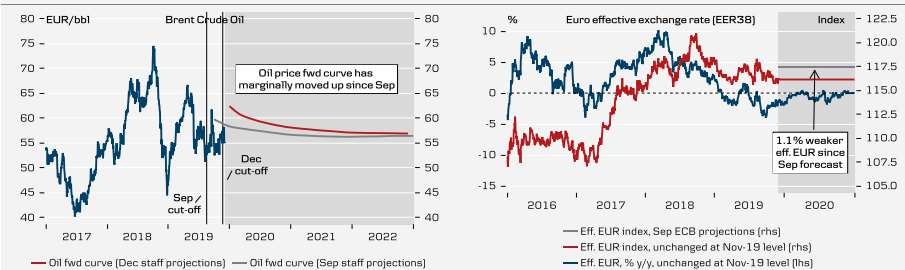
Past performance is not a reliable indicator of current or future results.

### ECB net purchases and reinvestments will be sizeable next year



Source: ECB, Maccrobond Financial, Danske Bank

### Higher oil price and weaker EUR provide tailwind for ECB's inflation forecast



Source: ECB, Macrobond Financial, Danske Bank

In light of the expected monetary strategy review, the new 2022 forecasts will also draw some attention at the December meeting. From tradition, we expect ECB to forecast HICP inflation ‘below, but close to, 2%’ and growth returning to potential. As discussed in *Euro Area Research - Measuring the euro area inflation pulse*, 29 November, **we remain more downbeat about a material pick-up in core inflation foreseeing it only at 1.1% in 2020 and 2021.** Especially, the subdued outlook for goods price inflation is rendering the ECB inflation target as elusive as ever in our view.

## ECB QE and monetary policy stance favour periphery and Bund ASW wideners

With its QE firmly setting the scene for the beginning of next year, we expect the ECB to be quite active with its monthly EUR20bn net purchases and on average EUR16bn reinvestments. As such, and as we outlined in our top trades for 2020, we expect periphery to perform against core bonds. We expect Bunds to trade in a 0% to -50bp range next year. We also favour Bund ASW spreads. See more in *EUR and Scandi Fixed Income Top Trades 2020*, 5 December.

## Disclosure

This research report has been prepared by Danske Bank A/S ('Danske Bank'). The authors of this research report are Piet P. H. Christiansen (Senior ECB Strategist) and Aila Mihr (Senior Analyst).

### Analyst certification

Each research analyst responsible for the content of this research report certifies that the views expressed in the research report accurately reflect the research analyst's personal view about the financial instruments and issuers covered by the research report. Each responsible research analyst further certifies that no part of the compensation of the research analyst was, is or will be, directly or indirectly, related to the specific recommendations expressed in the research report.

### Regulation

Danske Bank is authorised and subject to regulation by the Danish Financial Supervisory Authority and is subject to the rules and regulation of the relevant regulators in all other jurisdictions where it conducts business. Danske Bank is subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority (UK). Details on the extent of the regulation by the Financial Conduct Authority and the Prudential Regulation Authority are available from Danske Bank on request.

Danske Bank's research reports are prepared in accordance with the recommendations of the Danish Securities Dealers Association.

### Conflicts of interest

Danske Bank has established procedures to prevent conflicts of interest and to ensure the provision of high-quality research based on research objectivity and independence. These procedures are documented in Danske Bank's research policies. Employees within Danske Bank's Research Departments have been instructed that any request that might impair the objectivity and independence of research shall be referred to Research Management and the Compliance Department. Danske Bank's Research Departments are organised independently from, and do not report to, other business areas within Danske Bank.

Research analysts are remunerated in part based on the overall profitability of Danske Bank, which includes investment banking revenues, but do not receive bonuses or other remuneration linked to specific corporate finance or debt capital transactions.

### Financial models and/or methodology used in this research report

Calculations and presentations in this research report are based on standard econometric tools and methodology as well as publicly available statistics for each individual security, issuer and/or country. Documentation can be obtained from the authors on request.

### Risk warning

Major risks connected with recommendations or opinions in this research report, including as sensitivity analysis of relevant assumptions, are stated throughout the text.

### Expected updates

Ad hoc.

### Date of first publication

See the front page of this research report for the date of first publication.

## General disclaimer

This research report has been prepared by Danske Bank A/S. It is provided for informational purposes only and should not be considered investment advice. It does not constitute or form part of, and shall under no circumstances be considered as, an offer to sell or a solicitation of an offer to purchase or sell any relevant financial instruments (i.e. financial instruments mentioned herein or other financial instruments of any issuer mentioned herein and/or options, warrants, rights or other interests with respect to any such financial instruments) ('Relevant Financial Instruments').

The research report has been prepared independently and solely on the basis of publicly available information that Danske Bank considers to be reliable. While reasonable care has been taken to ensure that its contents are not untrue or misleading, no representation is made as to its accuracy or completeness and Danske Bank, its affiliates and subsidiaries accept no liability whatsoever for any direct or consequential loss, including without limitation any loss of profits, arising from reliance on this research report.

The opinions expressed herein are the opinions of the research analysts responsible for the research report and reflect their judgement as of the date hereof. These opinions are subject to change and Danske Bank does not undertake to notify any recipient of this research report of any such change nor of any other changes related to the information provided herein.

This research report is not intended for, and may not be redistributed to, retail customers in the United Kingdom or the United States.

This research report is protected by copyright and is intended solely for the designated addressee. It may not be reproduced or distributed, in whole or in part, by any recipient for any purpose without Danske Bank's prior written consent.

## Disclaimer related to distribution in the United States

This research report was created by Danske Bank A/S and is distributed in the United States by Danske Markets Inc., a U.S. registered broker-dealer and subsidiary of Danske Bank A/A, pursuant to SEC Rule 15a-6 and related interpretations issued by the U.S. Securities and Exchange Commission. The research report is intended for distribution in the United States solely to 'U.S. institutional investors' as defined in SEC Rule 15a-6. Danske Markets Inc. accepts responsibility for this research report in connection with distribution in the United States solely to 'U.S. institutional investors'.

Danske Bank is not subject to U.S. rules with regard to the preparation of research reports and the independence of research analysts. In addition, the research analysts of Danske Bank who have prepared this research report are not registered or qualified as research analysts with the NYSE or FINRA but satisfy the applicable requirements of a non-U.S. jurisdiction.

Any U.S. investor recipient of this research report who wishes to purchase or sell any Relevant Financial Instrument may do so only by contacting Danske Markets Inc. directly and should be aware that investing in non-U.S. financial instruments may entail certain risks. Financial instruments of non-U.S. issuers may not be registered with the U.S. Securities and Exchange Commission and may not be subject to the reporting and auditing standards of the U.S. Securities and Exchange Commission.

**Report completed:** 6 December 2019, 08:55 CET

**Report first disseminated:** 6 December 2019, 10:35 CET