MARKET COMMENTARY

ECB starts frontloading policy easing with a 25 bps cut

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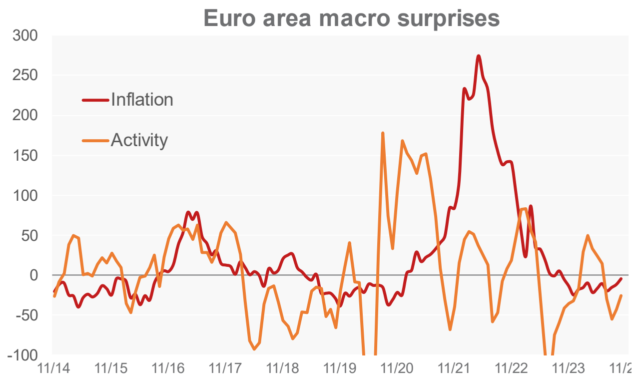
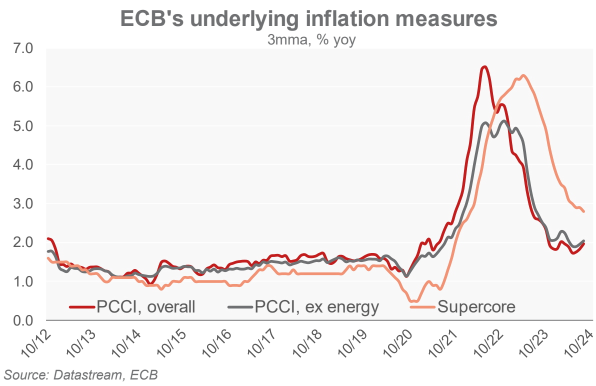
- **At today's meeting the ECB's Governing Council (GC) unanimously decided again to cut its key rate by 25 bps to 3.25%, in line with latest market expectations. The decision to cut again before updated macro projections was due to the combination of disappointing growth data and more favourable inflation reading.**
- **Overall, the ECB adopted a dovish tone seeing "*the disinflationary process well on track*". Still President Lagarde was very outspoken that data-dependency and the meeting-by-meeting approach will be maintained and that until the neck of inflation is broken a restrictive policy stance would still be needed.**
- **But with a higher emphasize of the growth risks and less concerns about inflation risks we foresee the ECB to continue cutting rates at the forthcoming meetings. We expect a series of 25 bps cuts at each meeting until April at a terminal rate of 2.25% thereby basically frontloading policy easing.**

ECB cut by 25 bps today: At today's meeting the GC again decided to cut its key rate, the deposit rate, to 3.25%. It continues with APP non-reinvestments and keeps on investing maturing securities purchased under the PEPP by only €7.5 billion per month on average. It intends to fully stop these reinvestments at the end of 2024.

Latest data show weak growth and surprisingly low inflation: At the previous policy meeting President Lagarde had stated that the October meeting was only six weeks away qualifying this as a rather short time period suggesting that a rate cut at today's meeting had not been on the Governing Council's mind. What changed its mind was a string of disappointing activity data (like the Sep. PMIs) in combination with a significantly weaker final September headline inflation reading of 1.7% yoy and core inflation down to 2.7% yoy.



Source: Datastream, GenAM



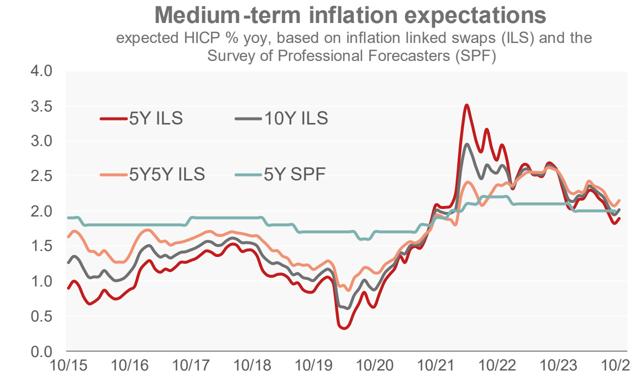
Source: Datastream, ECB

GC envisages lower growth and sees less inflation risks: Looking ahead, the GC assesses that the "*disinflationary process is well on track*" and that the inflation outlook was also affected by the recent downward surprises of activity indicators. While domestic inflation is still characterised as high, the ECB now sounds more confident on labour costs. These are now set "to continue easing gradually" while at the September meeting moderation had only been acknowledged. In the Q&A President Lagarde confirmed that activity data were a bit below expectation and that this also impacts on the inflation outlook. Activity risks are still seen as tilted to the downside. But at the same time, she was also very clear by stating that "*We* (the ECB) *certainly do not see a recession*". All in all, the ECB sounded much more confident bringing inflation down than before.

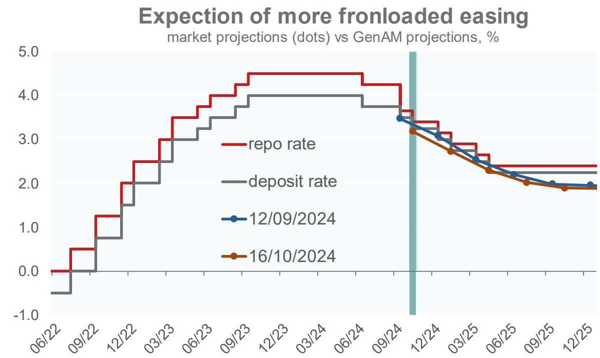
Neck of inflation not yet broken, December projections key: That said, during the press conference Mrs Lagarde also stated very clearly that the neck of inflation was not yet broken but that the process of doing this had started. Accordingly, the GC stuck to its intention to "*keep policy rates sufficiently restrictive for as long as necessary*". As also emphasized at the press conference, a thorough reassessment of the growth and inflation outlook will be conducted at the December meeting when updated staff projections will become available.

Meeting-by-meeting approach emphasized: Not surprisingly, President Lagarde was very outspoken in praising the ECB's data-dependence and meeting-by-meeting approach. Asked about whether the door for a further cut in December would be opened if data were continuing to hint in the same direction as recently, she replied that the ECB was not pre-committing and that she did not open the door for anything.

Frontloading of policy easing likely: Today's decision was met unanimously which signals to us that also the hawks see considerably less inflation risks now. At the December meeting we see the need for a downward adjustment of the ECB's macro projection, first of all the activity outlook. Especially the 2025 growth forecast of 1.3% looks too optimistic to us. We expect only 0.9% implying the need to adjust the inflation path downwards amid further reduced upside risks. We expect another 25 bps cut by December bringing the deposit rate down to 3.00% by then and look for meeting-by-meeting cuts until 2.25% will be reached in April. Depending on incoming data we see the risk tilted towards more cuts.



Source: Datastream, ECB, GenAM calculations



Source: Datastream, ECB, GenAM calculations