



## *Little by way of ECB rate hikes in next two years*

As expected, last week's meeting of the ECB Governing Council concluded with no changes to interest rates from their present levels of 0% for the refi rate and -0.4% for the deposit rate. However, the ECB did make some significant announcements on monetary policy, which point to rates remaining at very low levels for an even longer period of time.

In particular, the ECB pushed out the timing of its guidance on when interest rates might first start to rise. It is now guiding that rates are on hold "at least through the end of 2019" from its previous reference to until the end of summer 2019. Indeed, in the press conference, President Draghi noted that several members of the Governing Council wanted to change the guidance on rates staying unchanged until March 2020.

The other key decision from the ECB was the launch of a new round of targeted longer-term refinancing operations, or so called TLTROs. Starting in September 2019 and ending in March 2021, this repo liquidity facility will have a maturity of two years and provide funding to banks at very low interest rates.

The aim is to help preserve favourable bank lending conditions in an environment of increased bank funding requirements, owing to the maturing of existing TLTROs and other bank debt, as well as greater regulatory compliances that require increasing bond issuance by banks.

The rationale for the ECB's announcements is the weaker and more challenging economic backdrop for the Eurozone economy. Not surprising, this was evident in the updated set of macro forecasts published by the ECB last week, which saw it sharply revise down its 2019 growth forecast. It is now projecting GDP growth of 1.1% for this year, compared to 1.7% previously, with forecasts for moderate growth of 1.6% in 2020 and 1.5% in 2021. It noted that the risks to these forecasts remain tilted to the downside.

The March update of its inflation forecasts also saw downward revisions. HICP inflation is forecast at 1.2% in 2019, down from 1.6% previously, 1.5% in 2020 (from 1.7%) and 1.6% in 2021 (from 1.8%). Crucially, the updated projections show that the ECB now expects inflation to remain well below its 2% target over the next three years. President Draghi explained that the weaker economic momentum is slowing the upward movement of inflation towards target.

The market expectation now is that the ECB will not start to raise rates until September 2020, when a small hike of 0.1% (10bps) is being factored in. Rates are expected to rise at a snail's pace thereafter. Futures contracts suggest the market is not factoring in a full 25bps rate increase until mid-2021.

Over the medium term, futures contracts show that markets expect rates to remain low for an extended period. Three month rates are only expected to get back into positive territory around end 2021, and are envisaged to still be comfortably below 1% by end-2024, in nearly six years' time.



This low interest rate outlook is keeping the euro anchored at low levels against the dollar, with EUR/USD edging down to around the \$1.12 level after the ECB meeting.

Oliver Mangan,  
Chief Economist, AIB

\*\*\*\*\*

R:mrk-com/Mlt View/Mkt View2018/.doc

AIB Customer Treasury Services  
DUBLIN / CORK  
fxcentre.aib.ie

Customer Treasury Services NI  
BELFAST  
firsttrustbank.co.uk/fxcentre

Customer Treasury Services GB  
LONDON  
aibgb.co.uk/fxcentre

Customer Treasury Services US  
NEW YORK  
fxcentre.aib.ie

This publication is for information purposes and is not an invitation to deal. The information is believed to be reliable but is not guaranteed. Any expressions of opinions are subject to change without notice. This publication is not to be reproduced in whole or in part without prior permission. In the Republic of Ireland it is distributed by Allied Irish Banks, p.l.c. In the UK it is distributed by Allied Irish Banks, plc and Allied Irish Banks (GB). In Northern Ireland it is distributed by First Trust Bank. In the United States of America it is distributed by Allied Irish Banks, plc. Allied Irish Banks, p.l.c. is regulated by the Central Bank of Ireland. Allied Irish Bank (GB) and First Trust Bank are trademarks used under licence by AIB Group (UK) p.l.c. (a wholly owned subsidiary of Allied Irish Banks, p.l.c.), incorporated in Northern Ireland. Registered Office 92 Ann Street, Belfast BT1 3HH. Registered Number NI 018800. Authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. In the United States of America, Allied Irish Banks, p.l.c., New York Branch, is a branch licensed by the New York State Department of Financial Services. Deposits and other investment products are not FDIC insured, they are not guaranteed by any bank and they may lose value. Please note that telephone calls may be recorded in line with market practice.