

# ECB Watch: All is set to cut in June

April 11, 2024 15:31 CEST

For one last time, the ECB has kept key interest rates unchanged. At the next meeting in June, however, everything will be ready to kick-start the rate cutting cycle. Today's ECB meeting should be seen as a preparatory one, at which no additional impulses were given.

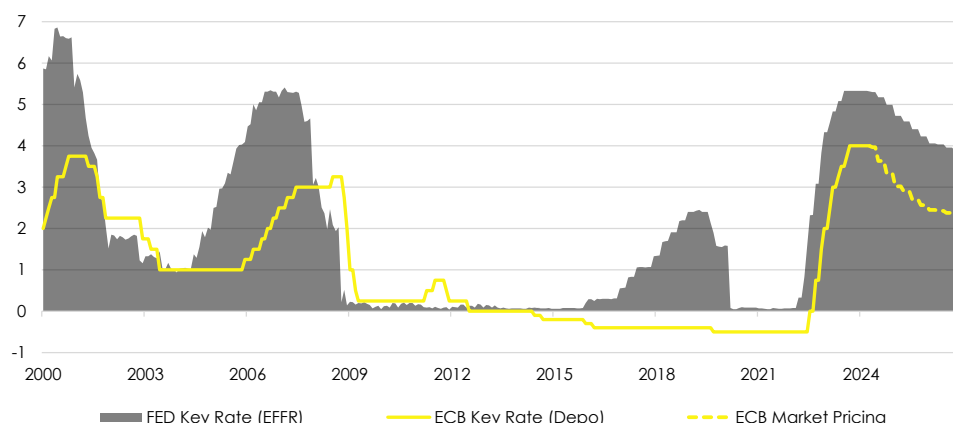


*In this rate cutting cycle the ECB seems to get a headstart vs the Fed* **1**

*Disclaimer* **3**

*Analyst* **6**

## In this rate cutting cycle the ECB seems to get a headstart vs the Fed



Market pricing is based on short-term forwards of respective OIS curve (ECB: €STR; Fed: EFFR).

Source: LSEG, RBI/Raiffeisen Research

"If the Governing Council's updated assessment of the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission were to **further increase its confidence** that inflation is converging to the target in a sustained manner, it would be **appropriate to reduce the current level of monetary policy restriction**."

That's the key sentence in today's monetary policy decision by the ECB. A reduction in the key interest rates will be appropriate should the ECB gain further confidence in its fight against inflation. The ECB's statement reads quite favourably on inflation. "Inflation continues to fall", "most measures of underlying inflation are easing" and "wage growth is gradually moderating". In March wage growth was still described as strong causing domestic price pressure to remain high. Confidence in the ECB's medium-term inflation outlook has clearly increased, which given the ECB's reaction function implies that a first rate cut is approaching. The ECB remains data-dependent but should the inflation releases for April and May be broadly in line with the ECB's expectations, **key interest rates will be lowered by 25 basis points in June**. The main refinancing rate will then move from 4.5 % to 4.25 % and the deposit rate from 4.0% to 3.75%.

The monetary policy statement also reads that the ECB "is not pre-committing to a particular rate path". Still, for the press conference our attention was directed towards

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any signals about the **pace of the rate cutting cycle**. Unfortunately, no signals were provided besides an emphasis on the ECB's data-dependency. Given our inflation outlook, which sees inflation to remain rather constant in 2024, we expect the ECB to follow a gradual approach of cutting interest rates by 25 basis points per quarter which allows the ECB to assess potentially volatile incoming information. During the press conference most questions were related to any **implications of a possible delay of the Fed's rate cutting cycle**. President Lagarde emphasized that the ECB is not directly influenced by the Fed, yet the ECB incorporates all available information in its economic projections. Thus, should spillovers from the Fed's decisions impact the ECB's inflation outlook, it could have implications for the ECB's setting of monetary policy. In our view, the euro would need to depreciate much further from current levels to have a noticable inflationary impact, which the ECB would act upon.

The **market reacted as expected**. Benchmark interest rates and Bund yields declined as a result of today's ECB decision. The decline was slightly more pronounced at the short-end of the curves. EUR/USD was broadly stable but it should be kept in mind that the US dollar appreciated sizeable the day before due to higher than expected US inflation data.

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Creation time of this publication: 11/04/2024 15:31 P.M. (CEST);  
First Dissemination of this publication: 11/04/2024 15:31 P.M. (CEST)

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