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Postponed is not abandoned

Gerhard Winzer

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Bond yields were up last Friday, whereas equities recorded losses. Signs that the bull market with low volatility, which started after the Brexit vote, is drawing to an end are becoming more plentiful.

ECB assuming wait-and-see stance

The immediate reason for the losses was the fact that the president of the European Central Bank failed to indicate any further loosening of the monetary policy at last Thursday's press conference. The most recent measures taken in spring are in fact TOO recent for the effects on the economic activity and inflation to be sufficiently assessable. The projections of the ECB for real economic growth were revised downwards by only a minor degree. Growth rates of 1.7% for 2016 and 1.6% for 2017 are in line with the continuation of moderate yet constant growth. Also, while the risks are rather on the downside, they have not increased.

Inflation the decisive factor

The development of inflation is the decisive factor. The ECB expects a gradual rise of inflation (this year: 0.2%; 2017: 1.2%; 2018: 1.6%). If this development continues "not to come through", a monetary loosening is very likely.

Options evaluated

President Draghi hinted at further loosening at the press conference. The ECB Council has tasked committees with the evaluation of the options for a smooth implementation of the purchase programmes. They would become particularly relevant if the purchase programmes, which are due to expire at the end of March 2017, were to be extended.

Wait until December

Council member Ilmārs Rimšēvičs pointed out last Friday that the ECB was evaluating all three options for a change to the purchase programmes: change in volume, change in allocation, and change of minimum yield. But he also said that we would probably have to wait until December for a decision.

Events of this week

Until then, some events coming up this week hold the potential to cause elevated volatility. On Tuesday, a further weakening of the Chinese economic data for August (industrial production and investments) would trigger a renewed sense of worry with regard to the stability of growth. On Thursday, the central bank of the UK might disappoint the markets by reducing the likelihood of further monetary loosening. On Friday an acceleration of US inflation in August would cause the expectations of a rate hike to rise. And lastly, the only result of the informal conference of the 27 heads of state and governments (EU without UK) in Bratislava on Friday might be that no consensus for the future development of the EU has been reached.

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From July 1997 to June 2007, he worked in research at CAIB, Bank Austria Creditanstalt, and UniCredit Markets & Investment Banking. His last position was as Executive Director for Fixed Income / FX Research and Strategy. He was responsible for research on asset allocation at Raiffeisen Zentralbank (RZB) in Vienna from July 2007 to February 2008.