

## ECB President's remarks more dovish than expected, signaling further monetary policy easing ahead

**Olga Kosma**  
 Economic Analyst  
[okosma@eurobank.gr](mailto:okosma@eurobank.gr)

- At its regular monetary policy meeting on Thursday 22 October, the ECB Governing Council (GC) decided to keep QE operational modalities unchanged, as well as the interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility stable at 0.05%, 0.30% and -0.20% respectively, as expected. At a press conference that followed the conclusion of the meeting, President Mario Draghi adopted a more dovish than expected tone, highlighting the downside risks to growth and inflation outlook from the slowdown in emerging market economies and developments in financial and commodity markets. Despite the negative impact from weak foreign demand on real GDP growth, the GC expects the euro area economic recovery to continue, supported by robust domestic demand capitalizing on lower oil prices and ECB's monetary policy easing stance.
- Taking into consideration the above, President Draghi effectively paved the way for more quantitative easing, emphasizing that the degree of monetary policy accommodation will have to be re-examined at the ECB's December monetary policy meeting, when the GC is scheduled to publish an updated set of macroeconomic projections that is a key input to the ECB's policy decisions.
- As far as the monetary policy tools are concerned, the President added that the GC is willing to use all instruments available within its mandate if necessary so as to preserve an appropriate degree of monetary accommodation including a deposit rate cut if necessary, whereas he had previously underlined that the ECB had reached the lower bound on interest rates following a technical adjustment in September 2014.
- Reacting to the more dovish than expected tone the ECB President adopted, global equity markets were firmer today, while German Bunds edged higher with the 2-yr bond yield hitting a fresh record low of ca. -0.35%. In FX markets, the EUR weakened against its major currency peers, with the EUR/USD hovering around 1.1090/1.1091 in European trade on Friday, within distance from a two-month trough near 1.1070 earlier in Asian trade.
- Following ECB President's remarks, we expect the ECB to announce more quantitative easing in its December meeting by extending its Public Sector Purchase Programme (PSPP) beyond September 2016. Nevertheless, a further reduction in the deposit facility rate cannot be ruled out, as Mr. Draghi made it clear that the GC discussed this monetary policy tool in order to assess the advantages and disadvantages of its implementation. Adding to this, the ECB-dated Eonia forward curve is currently pricing in a probability of ca. 90% (from 50% before Mr. Draghi's comments) for a rate cut of 10bps in the deposit facility by mid-2016. A likely trigger for a deposit rate cut would probably be a significant EUR appreciation from current levels, potentially in case the Fed shifts to a more dovish stance reducing expectations for an interest rate hike before year-end.

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## Eurobank Economic Analysis and Financial Markets Research

Dr. Platon Monokroussos: Group Chief Economist  
pmonokroussos@eurobank.gr, + 30 210 37 18 903

### Research Team

**Anna Dimitriadou:** Economic Analyst  
andimitriadou@eurobank.gr, + 30 210 37 18 793

**Ioannis Gkionis:** Research Economist  
igkionis@eurobank.gr + 30 210 33 71 225

**Stylios Gogos:** Economic Analyst  
sgogos@eurobank.gr + 30 210 33 71 226

**Olga Kosma:** Economic Analyst  
okosma@eurobank.gr + 30 210 33 71 227

**Arkadia Konstantopoulou:** Research Assistant  
arkonstantopoulou@eurobank.gr + 30 210 33 71 224

**Paraskevi Petropoulou:** G10 Markets Analyst  
ppetropoulou@eurobank.gr, + 30 210 37 18 991

**Galatia Phoka:** Research Economist  
gphoka@eurobank.gr, + 30 210 37 18 922

**Theodoros Stamatou:** Senior Economist  
tstamatou@eurobank.gr, + 30 210 33 71 228

### Global Markets Sales

**Nikos Laios:** Head of Global Markets Trading, Sales & Structuring, nlaios@eurobank.gr, + 30 210 37 18 910

**John Seimenis:** Head of Treasury Sales  
yseimenis@eurobank.gr, +30 210 37 18 909

**Alexandra Papathanasiou:** Head of Institutional Sales  
apapathanasiou@eurobank.gr, +30 210 37 18 996

**Achilleas Stogioglou:** Head of Private Banking Sales  
astogioglou@eurobank.gr, +30 210 37 18 904

**Vassilis Gioulbaxiotis:** Head Global Markets International  
vgioulbaxiotis@eurobank.gr, +30 210 3 718 995

**Stefanos Togoussidis:** Head of Retail Sales  
stogoussidis@eurobank.gr, +30 210 3718917

Eurobank Ergasias S.A, 8 Othonos Str, 105 57 Athens, tel: +30 210 33 37 000, fax: +30 210 33 37 190, email: [EurobankGlobalMarketsResearch@eurobank.gr](mailto:EurobankGlobalMarketsResearch@eurobank.gr)

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