

# MARKET COMMENTARY

ECB still in a good place, stronger euro no need to act (yet)

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- At today's meeting the ECB Governing Council (GC) unanimously decided to again keep its deposit rate unchanged at 2.0%.
- FX developments were discussed, with the stronger euro being seen as a burden the external environment and a downside risk to inflation. But in the Q&A President Lagarde played down latest developments finding that there has been no materially new appreciation in 2026 and that past appreciation was already in the baseline scenario.
- Analogously, she sounded relaxed on the latest inflation data that were below the ECB's expectation and constructive on growth.
- All in all, President Lagarde reconfirmed that the ECB was *"in a good place"* while stating that the sentiment in the GC was broadly balanced.
- We stick to our view that the ECB maintains its key rate at 2.0% but see the risk tilted towards a cut, especially if the euro were to rise significantly further.

**ECB kept key rate unchanged today:** Quite unspectacularly, at today's meeting the GC left its key rate, the deposit rate, at 2.00% for the fourth consecutive time. It continues with fully non-reinvestments of its APP and PEPP purchases.

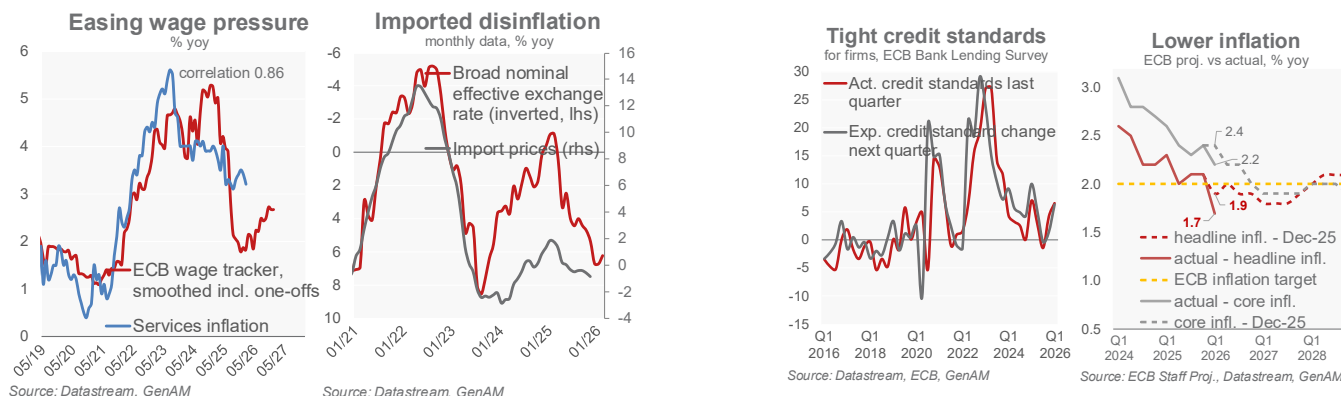
**A strong euro does not cause too much concern (yet).** The latest dataflow fuelled speculation that the ECB might be pushed out of its policy hibernation. Especially the euro's rise at the outset of the year was in focus, nurtured by concerns about imported disinflation and a further hit to European external competitiveness. Comments from GC members like de Galhau that the exchange rate has become a more explicit input to the reaction function contributed to speculations about when the ECB would need to act. Indeed, the stronger euro is seen as a burden on the external environment and a downside risk to inflation that the GC monitors closely and was discussed at today's meeting. But in the Q&A President Lagarde played down latest developments finding that there has been no materially new appreciation in 2026 and that past appreciation was already in the baseline scenario. It became clear that to trigger policy action the euro would need to leave its trading range to the upside.

**Low January inflation no reason of concern.** While the latest GDP data (+0.3% qoq vs. staff projection assumption of 0.2% qoq) surprised on the upside, January flash headline as well as core inflation came in below the expected average for the first quarter (see rh-graph). However, the GC sounded not only constructive on growth and again characterised the economy as resilient but continued to see inflation at target in the medium-term. In the Q&A Mrs Lagarde played down the low January inflation data by mentioning that undershooting in 2026 had long been forecast and that inflation was in a 'good place'.

**ECB still in a good place:** As before, monetary policy acts under huge uncertainty and the range of risks is not being reduced. In between the line it became clear that there was a debate within the GC about the course of monetary policy and we conjecture

from the wording that it was bigger than at the previous meetings. However, according to President Lagarde the sentiment in the GC was 'broadly balanced' and she found the ECB again in a 'good place'.

**What's next?** At the current level of 2.0% the policy rate is in the middle of the neutral range (of 1.75% to 2.25%) that ECB staff had derived. From today's press conference it became clear to us that it needs much for the ECB to act. Apart from a further significant euro appreciation President Lagarde mentioned services inflation and the ECB's proprietary wage tracker as key signposts. The latest ECB data (see rh-graph) suggest moderation but stabilisation afterwards, something monetary policy will likely look through. We expect the ECB to stay on hold for this and next year. That said, with core inflation now also approaching the 2% threshold and headline inflation even below it, we think that the monetary policy risks are skewed to the downside.



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