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ECB leaves repo rate on hold at 4%, as expected

In a highly predictable fashion, **the ECB confirmed a wait and see approach to monetary policy in February**, with the main marginal lending, repo and deposit rates left on hold for the ninth consecutive month, at 5%, 4% and 3% respectively.

The overall policy language endorsed by the ECB President at today's press reinforces our view that the policy of wait and see endorsed by the monetary authorities over the past nine months will most likely continue in the coming months, but the mere fact that a more uncertain world has been highlighted by Mr Trichet throughout the press confirms suggests that **the Council has now moved away from the one last rate hike scenario, into a neutral stance and arguably a step closer to a rate cut scenario.**

Indeed, Mr Trichet mentioned that *'uncertainty about the prospect for economic growth is unusually high and the risk surrounding the outlook for economic activity has been confirmed to lie to the downside.'* The *'unusually high uncertainty'* has been referred to on several occasions at today's press conference while on growth, Mr Trichet suggested that *'The latest information on economic activity around the turn of the year points to a more moderate pace of growth in the euro area... The fundamentals of the euro area remain sound'*, so it is not all doom and gloom just yet.

Inflation remains a concern: *'The current short term upward pressure on inflation must not spill over into the medium-term. The firm anchoring of inflation expectations over the medium and long term is of the highest priority'*. The ECB also reiterated concern over second round effects and the materialisation of upside risks to price stability over the medium term.

This press conference is in line with our view **that rate hikes are definitely off the agenda at this stage** and by bringing a greater degree of uncertainty over the growth assessment, **the ECB may be getting ready for a shift towards a more dovish policy language.** Indeed, inflation clearly remains a prime concern, but the greater degree of uncertainty on the growth outlook **opens the door for a change in language within the next few months. This is probably enough for the market to buy into an ECB rate cut scenario, even if this does not materialise for quite some time.** All positive for the bond market (see more curve steepening) but a **euro negative.**

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