MIRABAUD Asset Management

FLASH NOTE

12 March 2020

ECB ACTS VIA BANK LIQUIDITY CHANNEL

STRATEGY TEAM

- In an unanimous decision, the ECB has left its main policy rates unchanged (refinancing rate at 0.00%; deposit facility rate at -0.50%);
- **Three main decisions** were announced: 1/ further liquidity measures for the financial system, including additional LTROs; 2/ relaxed rules for the TLTRO III operations at a lower rate; and 3/ supplementary purchases worth €120 billion through the end of the year;
- This decision will not bring a strong support to real economy, but will help avoid liquidity shortages, without putting further pressure on banks.

The Decision. The ECB decided in an unanimous decision to maintain unchanged its deposit facility rate, at -0.50%, but it reinforced its expansionary stance in announcing pre-emptive measures to support the financial system and avoid liquidity shortage:

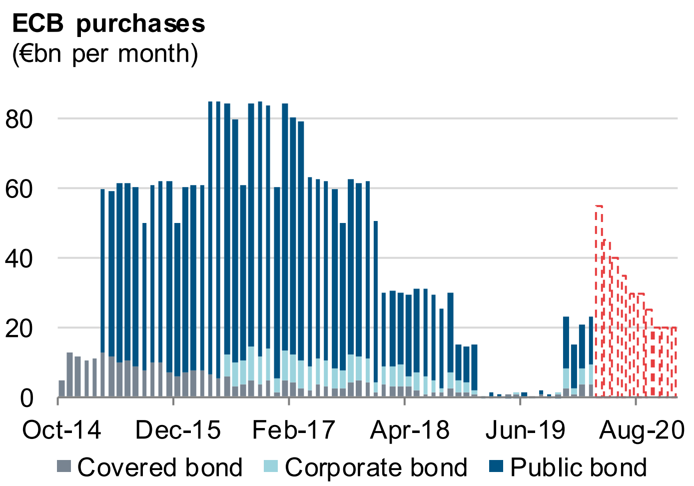
- Additional LTRO will be conducted to bridge the period until the next TLTRO III operation in June 2020;
- TLTRO III conditions will be relaxed until June 2021, and their amount will substantially be raised. The interest rate will be cut to a maximum of 25 basis points below the deposit facility rate, i.e. -0.75% (previously, operations were conducted at the deposit facility rate);
- On top of the €20 billion monthly asset purchases, the ECB will conduct supplementary purchases worth €120 billion through the end of the year. These purchases will mostly focus on private sector corporate bonds;
- Finally, banks will benefit from temporary capital and operational relief.

The Rationale. The spreading of the coronavirus is a major shock on growth prospects. It will have significant impact on activity through supply chain disruptions, and it will also reduce global demand. Thus, the ECB has revised down its growth and inflation forecasts. These forecasts could substantially be revised downward once again because of the recent drop in oil price and supplementary containment measures taken in several countries. Finally, the ECB is calling upon governments to settle ambitious and coordinate fiscal policies.

Our take. This decision will not provide a strong support to real economy. But it will allow the ECB to provide supplementary liquidity and to avoid further tightening of financing conditions, without cutting again its deposit facility rate. Thus, it will alleviate the pressure on the banking system. On top of that, the new envelope of purchases with no monthly predetermined amount will enable the ECB to be very flexible. It will manage the timing of the purchases in order to avoid further credit spread widening. Finally, we maintain our scenario regarding the SNB, expecting status quo at its next meeting on March 19.

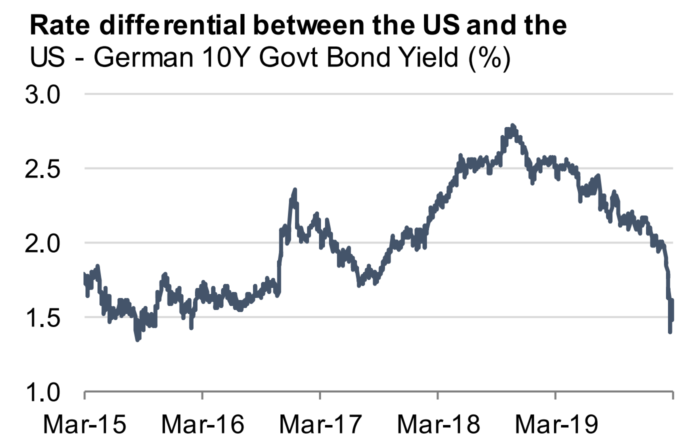
Asset Allocation. We are maintaining our 50% hedges on US and European equities, including Swiss and UK stocks. We continue to anticipate a moderation in the dollar against euro, considering the reduction in rate differential between the two areas.

ADDITIONAL PURCHASES WORTH €120 BILLION



Sources: ECB, Datastream, Mirabaud Asset Management

FALL IN RATE DIFFERENTIAL BETWEEN THE US AND THE EZ



Sources: Datastream, Mirabaud Asset Management

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