

Will ECB walk or just talk as rate circus comes to Europe?



BRUSSELS (Reuters) – The global march towards lower interest rates reaches Europe this week with the European Central Bank expected at least to signal easier monetary policy, while Turkey's new banking chief is seen taking an ax to the country's rates.

Slowing global growth, increased protectionism and in some cases weak domestic data have persuaded major central banks to loosen monetary policy, with a rate cut more or less inked in for the U.S. Federal Reserve at the end of the month.

The ECB, whose Governing Council meets on Wednesday and Thursday, said last month that euro zone interest rates would remain at present levels at least through the first half of 2020 – an extension from previous period of until the end of 2019.

Two-thirds of economists polled by Reuters expect the ECB next week simply to change its guidance, such as for rates to be at “present or lower levels” ahead, with a cut of the deposit rate to an all-time low of -0.50% at its September meeting.

“I think for now, they’ll only get to point where they consider a rate cut is on the table and then do it later. The ECB has a long history of moving very slowly,” said Capital Economics’ senior Europe economist Jack Allen-Reynolds.

But some economists believe the ECB will have to do more.

Carsten Brzeski, chief economist for Germany at ING, says he thinks of the chances of just words as 51%, versus 49% for action.

“Draghi has surprised us more often in terms of being ahead of the curve, of over-delivering, but it’s very hard to say. I think there will be a tough discussion,” he said.

If the Fed starts cutting rates and the ECB does not send out an extremely dovish message, the euro could strengthen, although at Friday’s level of \$1.12 it is hardly near the pain barrier for EU exporters.

Commerzbank is one bank that predicts the ECB will act, cutting by 20 basis points

“Maybe they want to prevent an appreciation (of the euro) and, like the U.S., they want to prolong the upswing. The data though is not as bad as you might think,” said economist Bernd Weidensteiner.

Unemployment in the euro zone is, at 7.5%, at its lowest level since July 2008, while industrial production and exports improved in May, albeit after declines in April.

In the United States, the case for a rate cut is ostensibly even thinner, with strong labor markets despite U.S.-China trade tensions and factory activity strong – at a year high in

the mid-Atlantic region.

Yet markets were by Thursday expecting a half percentage point cut in U.S. rates at the end of July, double the reduction they expected just a day earlier. The action has been sold as insurance against any negative development. U.S. economic growth is expected to have cooled in the second quarter, set to be confirmed in a first GDP estimate on Friday.

TURKISH AX, NEW BRITISH PM

In Turkey, the case for action is more clear-cut given a recession-hit economy. Economists polled by Reuters expect the central bank under new governor Murat Uysal to reduce the current 24% interest rate by an average 250 basis points.

It will follow Indonesian and South Korean rate cuts on Thursday and the Reserve Bank of Australia, which reduced interest rates in both June and July.

The trend leaves only the Bank of Canada, buoyed by higher oil exports and consumer spending, and the Bank of England as outliers, though the latter could change.

Arch-Brexiteer Boris Johnson is expected to be named as Britain's next Prime Minister on Tuesday, raising the chances of a 'no deal' Brexit and potentially lowering growth forecasts.

Only 27 of 76 economists polled now expect an increase to British interest rates before the end of next year, compared to 36 of 69 last month. On the flip side, nine of 76 were expecting a cut by end-2020 compared to five of 69 in June.

"We don't necessarily share the view that the UK economy will see a substantial pick-up in growth even in a smooth Brexit," Royal Bank of Canada, a primary dealer of British government bonds, said.

Reporting by Philip Blenkinsop; Editing by Toby Chopra

Our Standards: The Thomson Reuters Trust Principles.

<https://www.reuters.com/article/us-global-economy/will-ecb-walk-or-just-talk-as-rate-circus-comes-to-europe-idUSKCN1UE1LU>