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What to look for from the European Central Bank as QE winds down

Bond purchases may stop but reinvestments* will still need to be made

The eurozone´s era of quantitative easing is drawing to a close. Mario Draghi is today almost certain to end the European Central Bank´s experiment in bloating its balance sheet through a mass bond-buying scheme – but a downturn in growth and increasing economic risks mean the central bank´s president wants to assure markets that other elements of the ECB´s stimulus will remain in place for some time.

The ECB will publish its monetary policy statement at 1.45pm local time in Frankfurt and Mr Draghi will meet the press at 2.30pm. Here is a guide to the three most important parts of what is likely to be a dovish message.

Reinvestments

The ECB´s governing council is expected to confirm what policymakers have said since the summer – they will stop expanding QE at the end of December, when bond purchases will fall from €15bn a month to zero.

That does not mean the effects of the programme will disappear entirely. The bank wants to keep the €2.6tn in bonds accumulated under QE on its balance sheet. With some of the bonds bought under the four-year programme maturing, eurozone central bankers will need to reinvest the proceeds in fresh asset purchases.

Thursday´s meeting will focus on what the bank should say about those reinvestments – whether to commit to remaining active in bond markets for a specific timeframe or link any removal of support to the strength of the economy.

So far, the bank has said in its monetary policy statement that it predicts that it will continue to reinvest maturing bonds "for an extended period of time" after the end of QE. It has already in effect committed to continue reinvestments until November by publishing a schedule of €190bn worth of purchases for the first 11 months of next year.

Mr Draghi will face a battle to persuade the council´s hawks to adopt a more dovish message on keeping the balance sheet bloated. But a new round of economic projections, which are expected to show risks are now tilted to the downside, should help his case for the bank to commit to reinvestments for two or three years.

Interest rate guidance

The ECB has said it expects to keep its key interest rates at record lows “through the summer” of 2019. However, poor data has led an increasing number of ECB watchers to bet that rates will remain on hold for all of next year.

One question for tomorrow is whether the bank updates its guidance to reflect the shift in markets´ expectations. The council could well focus its efforts on changing its message on reinvestments, however, and leave the guidance on interest rates unchanged.

The central bank´s benchmark main refinancing rate has been at zero and the deposit rate at minus 0.4 per cent since the spring of 2016.

Cheap cash

Investors fear there is little the ECB could do to boost the economy should those downside risks to growth and inflation begin to materialise. […]

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