

TRENDMACRO LIVE!

## On the July ECB and BOE Policy Decisions

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**The BOE provides forward forward guidance, and the ECB provides no guidance guidance.**

As expected, there were no rate changes from either [the Bank of England](#) -- following its first Monetary Policy Committee meeting under new governor Mark Carney -- nor from [the European Central Bank](#) today. But significantly, both central banks have adopted forward guidance on interest rates as a new monetary policy tool.

- While both central banks are adopting forward guidance, they are taking different paths. The ECB started its forward guidance today, while the BOE promised to start forward guidance with thresholds next month.
- [The BOE said](#) that "The latest remit letter ... from the Chancellor had requested that the Committee provide an assessment... of the case for adopting some form of forward guidance, including the possible use of intermediate thresholds."
- [The ECB said](#), "The Governing Council expects the key ECB interest rates to remain at present or lower levels for an extended period of time."
- While the BOE promised to look at setting thresholds to help the market interpret when it would change its stance -- much like the US Federal Reserve has done with its so-called "[Evan's Rule](#)" thresholds (see "[On the December FOMC](#)" December 12, 2012), the ECB has neither given nor committed to give any thresholds.
- We are certainly not going to declare the ECB's apparent move to a more dovish footing today a failure -- initial market reaction has been very positive.
- But at the May meeting the ECB had already committed to maintaining liquidity operations until at least mid-2014 (see "[On the May ECB Policy Decision](#)" May 2, 2013), and [last month's statement](#) committed to maintaining the monetary policy stance as accommodative for as long as necessary (see "[On the June ECB Policy Decision](#)" June 6, 2013). While the change of language today from "as long as necessary" in June to "for an extended period of time" is technically forward guidance -- Draghi described it as such in [the Q&A after](#) the statement -- without a target or threshold, it does not seem to be telling us anything really new.
- The market seems to have interpreted it as a sign of a more dovish ECB, and this may well be right. After all, when the US Federal Reserve first used forward guidance way [back in March of 2009](#), it

### Update to strategic view

**ECB, BOE:** The ECB and the BOE offer forward guidance -- or the promise of it -- indicating to the markets that their present policy will remain in place for the foreseeable future, and imparting a dovish bias. Technically the BOE has promised to provide guidance next month, along with thresholds presumably like the Fed's Evan's Rule. The ECB's forward guidance was here and now, but did not commit to thresholds. The market reaction has been positive. But for these moves to be credible, the BOE will have to deliver next month on today's promises, and the ECB's forward guidance will have to introduce thresholds soon.

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said "economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period." Today's ECB language perfectly mirrors where the Fed was over four years ago -- and since then the Fed has certainly gotten more dovish. But then again, perhaps the Fed did so because, in the end, forward guidance is never enough.

- It would certainly be a leap to think that the ECB is going to follow in the Fed's footsteps towards outright quantitative easing, but without a threshold, the ECB will likely find it will have to provide at least some clarification of what an "extended period" actually means in Frankfurt.

Aside from the ECB's forward guidance, Draghi again defended the Outright Monetary Transactions (OMT) sovereign backstop, saying it has produced "universally acknowledged benefits." He added that some governments have used the gift of time provided by the OMT's easing of sovereign bond pressure better than others. He then went on to praise how well -- [under pressure](#) -- Portugal has implemented its adjustment program. So perhaps a hint there, amidst rising political instability that has seen the resignations of two key cabinet ministers in the last ten days, that the ECB would take a favorable view of a Portuguese OMT application.

On interest rates, Draghi did reiterate several times during the press conference that the 0.5% current ECB interest rate is not the lower bound of possible ECB rates, and that he still has an open mind on negative rates. We still do not see another rate cut as likely in the short term. If Draghi gets the hang of his forward guidance tool -- it should not be necessary as market sentiment improves.

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## Bottom line

The ECB and the BOE offer forward guidance -- or the promise of it -- indicating to the markets that their present policy will remain in place for the foreseeable future, and imparting a dovish bias. Technically the BOE has promised to provide guidance next month, along with thresholds presumably like the Fed's Evan's Rule. The ECB's forward guidance was here and now, but did not commit to thresholds. The market reaction has been positive. But for these moves to be credible, the BOE will have to deliver next month on today's promises, and the ECB's forward guidance will have to introduce thresholds soon. ▶

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