

## COMMENTARY

04 SEPTEMBER 2014

### Hermes Group Chief Economist Neil Williams reacts to today's ECB meeting

"Today's ECB moves are a step in the right direction, but too little, too late to snuff out deflation-risk and kick-start growth. The further 10bp shavings off the refinancing and deposit rates are puny, and look more cosmetic than real. Any drop in the euro on the back of them would be welcome, but possibly short lived.

"The ECB hopes the negative deposit rate (-0.2%) will deter banks from parking cash at the ECB, instead passing it on to consumers and firms. But, this may be a red herring, given still tame credit demand, pressure for the banks to pass stress tests and the fact that the bulk of reserves still gets the (0.05%) refinancing rate.

"These rates may have to be cut again - especially if the unfortunate conflict to the east causes an increasingly direct macro hit on Germany's growth.

"The ECB's private asset purchases may help, but the amounts are small, and any benefit will fall more to the bigger, core members, Germany, France and Italy, than the periphery.

"Far more useful would've been the 'bazooka' of unlimited sovereign QE, which was not fired today. But, Dr Draghi's clearly leaving his powder dry. His hesitancy to use all bullets reflects how empty the policy tool box is. With demand subdued and the likelihood at some stage of rising bond yields, the ECB will have to capitulate on QE.

"The biggest test will be when global yields start to climb, probably in 2015. Given two-thirds of euro-zone activity is long, not short-rate, driven, this will sap demand. Otherwise, the zone's misery may be compounded by a stronger euro, doing nothing to allay fears that Japan is 'leading the way' in terms of deflation risk."

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#### Notes to Editors:

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