

# Investment Strategy Bulletin

## ECB dovish guidance: a game changer for the euro

Investment Solutions

8 March 2019

**The European Central Bank's policy communication on 7 March was a game changer for the EUR. We revise substantially lower our EURUSD forecast for 2019: near-term we see better-than-even odds for a convergence towards the 1.10 level and anticipate a modest recovery only in the second half of this year. Our year-end target now stands at 1.14 (1.20 previously).**

Yesterday, the ECB delivered "shock and awe" by abruptly turning controlled cautiousness into full-blown dovishness. We will first summarise the key points from the ECB's policy meeting and then elaborate on EUR implications (including changes to our forecasts). We conclude with our view on the broader implications for the FX universe.

### Four key points on policy changes

1. Real GDP growth expectations for 2019 were revised substantially lower, from 1.7% to 1.1%. The lower growth trajectory now means it will take longer to meet the inflation target. Inflation for 2019 is now seen at 1.2% (1.6% previously), and is not expected to exceed 1.6% over the next three years.
2. The ECB significantly changed its forward guidance, with rates now seen on hold at least through the end of 2019 (the previous guidance was "at least through the summer of 2019").
3. The ECB announced a third round of Targeted Long Term Refinancing Operations (TLTRO III) which will avoid the cliff-edge expiry of the second round of TLTROs at the end of June and ensure fluid lending conditions. These TLTROs will be conducted every quarter from September 2019 through March 2021, with a 2-year maturity.
4. Finally, reinvestments of maturing debt (approximately EUR 20 billion per month) will last longer than planned to keep the ECB's balance sheet constant.

### EUR implications

The TLTRO announcement was not really a surprise, although we expected the formal communication to come a little later (potentially at the April meeting). However, the ECB turned the tide on the currency with its substantial downgrade of growth/inflation forecasts and its altered forward guidance. We view this as game-changing for the EUR (at least for the next six months or so) as it opens the door to the current negative interest rate policy remaining in place for longer than initially expected. EURUSD sold-off on the news, diving from 1.1320 to 1.1180 before stabilising around the 1.12 level.

We have long argued that EURUSD upside (until now our central scenario) was more about dollar weakness than strong idiosyncratic euro area factors. Of course, slackening external headwinds (such as trade) would also help by allowing the euro area's economic data to normalise. Although our broader dollar view of a slow depreciation throughout 2019 remains unchanged, we now believe that the ECB's policy shift represents a huge hurdle for the common currency to find its footing. Importantly, past experience suggests that Mr Draghi's well-articulated dovishness has had a noticeable and lasting negative impact on the currency.

As such, we now think that chances are more than even that EURUSD will converge lower towards 1.10 by the end of this quarter and potentially stabilise around 1.12 at the end of Q2 19 (compared with 1.16 previously). We still expect the external headwinds of weaker trade to normalise over the next few quarters (and so we think the ECB's new growth forecast is too pessimistic) but any euro recovery is unlikely before the second

**Important information: Please read the important information at the end of the document.**

Publication of Lombard Odier – Contacts: Investment Solutions, [investment-solutions@lombardodier.com](mailto:investment-solutions@lombardodier.com)

Data as of 8 March 2019 unless otherwise stated.

Lombard Odier · Investment Strategy Bulletin · 8 March 2019

Page 1/4

half of this year. We pencil-in 1.13 for Q3 19 (1.18 previously) and 1.14 for Q4 19 (1.20 previously). By that time, we judge that the modest improvement in global trade and continuing sound domestic fundamentals will be enough to allow the ECB to start unwinding some of its recent dovishness. Of course, we do not now expect a deposit rate hike this year. Inevitably, any failure in global trade data to stabilise would put these forecasts under significant downside pressure.

### **Broader FX implications**

More broadly, it is hard to ignore this new wave of major central bank dovishness from the Federal Reserve, the ECB, the Bank of Canada, and to a certain extent, the Bank of Japan. This is bound to have implications for risk and risk currencies, although through different and potentially offsetting channels.

On one hand, this renewed and broad-based dovish stance implies that monetary policies will remain accommodative for longer. This should be good for risk and emerging market FX more widely. On the other hand, the increased pessimism communicated by central banks is sending alarm signals to the investment community about global growth prospects and could weigh on risk sentiment (for example following the ECB policy communication and the disappointing overnight Chinese trade figures, USDJPY fell from 111.86 to 110.95).

There seems to be a battle between liquidity remaining plentiful for longer (which is risk positive) and concerns over global trade and growth (which is risk negative). In our view, recent developments in the US-China trade discussions have increased the chances of data normalisation followed by a modest recovery. If we are right, then the effect on risk should be a net positive and maintain the recent pickup in portfolio flows towards emerging markets. The latter should bode well for emerging market FX carry trades. That said, with the ECB communicating that rates will remain negative for longer, it now makes more sense to chase higher-yielding EM currencies through funding of euros.

Finally, the ECB's (indirect) blow to the exchange rate has implications for EURGBP given the upcoming developments on Brexit. Our new EURUSD trajectory implies that EURGBP will reach 0.82 around the middle of the year with risks skewed to the downside. Of course, this is under our working assumption that there will be an extension of article 50 agreed in the UK parliament next week (and approved by the EU) and eventually, negotiations over the next three or four months that lead to a sort of a 'soft Brexit'. If correct, this would allow sterling to appreciate by pricing-out the 'hard Brexit' risk premia while the EUR continues to remain under pressure from the ECB's newly dovish forward guidance.

*Vasileios Gkionakis,  
PhD Global Head of FX Strategy*

## Important information

This is a marketing communication issued by Bank Lombard Odier & Co Ltd (hereinafter “Lombard Odier”).

It is not intended for distribution, publication, or use in any jurisdiction where such distribution, publication, or use would be unlawful, nor is it aimed at any person or entity to whom it would be unlawful to address such a marketing communication.

This marketing communication is provided for information purposes only. It does not constitute an offer or a recommendation to subscribe, to purchase, sell or hold any security or financial instrument. It contains the opinions of Lombard Odier, as at the date of issue. These opinions and the information contained herein do not take into account an individual’s specific circumstances, objectives, or needs. No representation is made that any investment or strategy is suitable or appropriate to individual circumstances or that any investment or strategy constitutes personalised investment advice to any investor. Tax treatment depends on the individual circumstances of each person and may be subject to change in the future. Lombard Odier does not provide tax advice. Therefore, you must verify the above and all other information provided in the marketing communication or otherwise review it with your external tax advisors. Some investment products and services, including custody may be subject to legal restrictions or may not be available worldwide on an unrestricted basis. The information and analysis contained herein are based on sources considered to be reliable. Lombard Odier makes its best efforts to ensure the timeliness, accuracy, and completeness of the information contained in this marketing communication. Nevertheless, all information and opinions as well as the prices, market valuations and calculations indicated herein may change without notice. **Investments are subject to a variety of risks.** Before entering into any transaction, an investor should consult his/her investment advisor and, where necessary, obtain independent professional advice in respect of risks, as well as any legal, regulatory, credit, tax, and accounting consequences. **Past performance is no guarantee of current or future returns, and the investor may receive back less than he/she invested.** The value of any investment in a currency other than the base currency of a portfolio is subject to foreign exchange rate risk. These rates may fluctuate and adversely affect the value of the investment when it is realised and converted back into the investor’s base currency. The liquidity of an investment is subject to supply and demand. Some products may not have a well-established secondary market or in extreme market conditions may be difficult to value, resulting in price volatility and making it difficult to obtain a price to dispose of the asset.

**European Union Members:** This marketing communication has been approved for use by Lombard Odier (Europe) S.A in Luxembourg and by each of its branches operating in the following territories: **Belgium:** Lombard Odier (Europe) S.A. Luxembourg · Belgium branch; **France:** Lombard Odier (Europe) S.A. · Succursale en France; **Italy:** Lombard Odier (Europe) S.A. · Italian Branch; **Spain:** Lombard Odier (Europe) S.A. · Sucursal en España; and **United Kingdom:** Lombard Odier (Europe) S.A. · UK Branch. Lombard Odier (Europe) S.A. is a credit institution authorised and regulated by the Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg. **Notice to investors in the United Kingdom:** Lombard Odier (Europe) S.A. · UK Branch is authorised in the UK by the Prudential Regulation Authorities (PRA) and is subject to limited regulation by the Financial Conduct Authority (‘FCA’) and the Prudential Regulation Authority (‘PRA’). **Details of the extent of our authorisation and regulation by the PRA and regulation by the FCA are available from us on request. UK regulation for the protection of retail clients in the UK and the compensation available under the UK Financial Services Compensation Scheme does not apply in respect of any investment or services provided by an overseas person.** In addition, this marketing communication has also been approved for use by the following entities domiciled within the European Union: **Gibraltar:** Lombard Odier & Cie (Gibraltar) Limited, a firm which is authorised and regulated by the Financial Services Commission, Gibraltar (FSC) to conduct banking and investment services business; **Spain:** Lombard Odier Gestión (España) S.G.I.I.C., S.A.U., an investment management company authorised and regulated by the Comisión Nacional del Mercado de Valores (CNMV), Spain.

**Israel:** This marketing communication has been approved for use in Israel by the Israel Representative Office of Bank Lombard Odier & Co Ltd, an entity not supervised by the Supervisor of Banks in the Bank of Israel, but by Swiss Financial Market Supervisory Authority which supervises the activities of Bank Lombard Odier & Co Ltd.

**South Africa:** This marketing communication has been approved for use in South Africa by the South Africa Representative Office of Bank Lombard Odier & Co Ltd, an authorised financial services provider Registration number 48505.

**Panama:** This marketing communication has been approved for use in Panamá by Lombard Odier (Panamá) Inc., an entity authorised and regulated by la Superintendencia del Mercado de Valores de Panamá. License to operate as an Investment Adviser. Res. SMV No.528-2013

**Switzerland:** This marketing communication has been approved for use in Switzerland by Bank Lombard Odier & Co Ltd, a bank and securities dealer authorised and regulated by the Swiss Financial Market Supervisory Authority (FINMA).

**United States:** Neither this document nor any copy thereof may be sent, taken into, or distributed in the United States of America, any of its territories or possessions or areas subject to its jurisdiction, or to or for the benefit of a United States Person. For this purpose, the term “United States Person” shall mean any citizen, national or resident of the United States of America, partnership organized or existing in any state, territory or possession of the United States of America, a corporation organized under the laws of the United States or of any state, territory or possession thereof, or any estate or trust that is subject to United States Federal income tax regardless of the source of its income.

**Media:** Lombard Odier would like to offer you for your information the enclosed Investment Strategy Bulletin.

In connection with the use of the enclosed document Lombard Odier kindly draws your attention to certain particular items/conditions. The information sent is for your personal use only. In case of quoting please cite Lombard Odier in no other capacity than as source of information only. For the sake of good order Lombard Odier would like to remind you that responsibility regarding quoted content and compliance with applicable regulations rests with you. The information provided does not constitute the provision of investment advice or an offer of any financial services especially not to the public. Lombard Odier kindly reminds you that further distribution of the received document to third parties without its prior written consent is prohibited.

This marketing communication may not be reproduced (in whole or in part), transmitted, modified, or used for any public or commercial purpose without the prior written permission of Lombard Odier.

**Data protection:** You might be receiving this because you have provided us with your contact details. If this is the case, note that we may process your personal data for direct marketing purposes. If you wish to object to this processing, please address your objection to the Group’s Data Protection Officer: Bank Lombard Odier & Co Ltd, Group Data Protection Officer, 11, Rue de la Corrairie, 1204 Geneva, Switzerland. E-Mail: [group-dataprotection@lombardodier.com](mailto:group-dataprotection@lombardodier.com). For more information on Lombard Odier’s data protection policy, please refer to [www.lombardodier.com/privacy-policy](http://www.lombardodier.com/privacy-policy).

## SWITZERLAND

### GENEVA

#### **Bank Lombard Odier & Co Ltd<sup>1</sup>**

Rue de la Corraterie 11 · 1204 Genève · Suisse  
geneva@lombardodier.com

#### **Lombard Odier Asset Management (Switzerland) SA**

Avenue des Morgines 6 · 1213 Petit-Lancy · Suisse  
Support-Client-LOIM@lombardodier.com  
Management Company regulated by the FINMA.

### FRIBOURG

#### **Banque Lombard Odier & Cie SA · Bureau de Fribourg<sup>1</sup>**

Rue de la Banque 3 · 1700 Fribourg · Suisse  
fribourg@lombardodier.com

### LAUSANNE

#### **Bank Lombard Odier & Co Ltd<sup>1</sup>**

Place St-François 11 · 1003 Lausanne · Suisse  
lausanne@lombardodier.com

### VEVEY

#### **Banque Lombard Odier & Cie SA · Agence de Vevey<sup>1</sup>**

Rue Jean-Jacques Rousseau 5 · 1800 Vevey · Suisse  
vevey@lombardodier.com

### ZURICH

#### **Bank Lombard Odier & Co Ltd<sup>1</sup>**

Utoschloss · Utoquai 29-31 · 8008 Zürich · Schweiz  
zurich@lombardodier.com

## EUROPE

### BRUSSELS

#### **Lombard Odier (Europe) S.A. Luxembourg · Belgium branch<sup>2</sup>**

Avenue Louise 81 · Box 12 · 1050 Brussels · Belgium  
brussels@lombardodier.com  
Credit institution supervised in Belgium by the Banque nationale de Belgique (BNB) and the Financial Services and Markets Authority (FSMA).

### GIBRALTAR

#### **Lombard Odier & Cie (Gibraltar) Limited**

Suite 921 Europort · P.O. Box 407 · Gibraltar  
gibraltar@lombardodier.com  
Authorised and regulated by the Gibraltar Financial Services Commission (FSC) to conduct banking and investment services business.

### LONDON

#### **Lombard Odier (Europe) S.A.<sup>2</sup>**

Queensberry House · 3 Old Burlington Street · London  
W1S 3AB · United Kingdom · london@lombardodier.com

The Bank is authorised and regulated in the UK by the Prudential Regulation Authority (PRA) and subject to limited regulation by the Financial Conduct Authority (FCA) and the PRA. Details of the extent of our authorisation and regulation by the PRA and regulation by the FCA are available from us on request. Registered in Luxembourg No. B169 907.

#### **Lombard Odier Asset Management (Europe) Limited**

Queensberry House · 3 Old Burlington Street · London  
W1S 3AB · United Kingdom · london@lombardodier.com

Investment firm authorised and regulated by the Financial Conduct Authority (FCA register No. 515393).

<sup>1</sup> Private bank and securities dealer authorised and regulated by the Swiss Financial Market Supervisory Authority (FINMA).

<sup>2</sup> Branch of Lombard Odier (Europe) S.A., a credit institution based in Luxembourg, authorised and regulated by the Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg.

## LUXEMBOURG

#### **Lombard Odier (Europe) S.A.**

291, route d'Arlon · 1150 · Luxembourg · Luxembourg  
luxembourg@lombardodier.com

Credit institution authorised and regulated by the Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg.

#### **Lombard Odier Funds (Europe) S.A.**

291, route d'Arlon · 1150 · Luxembourg · Luxembourg  
luxembourg@lombardodier.com

### MADRID

#### **Lombard Odier (Europe) S.A. · Sucursal en España<sup>2</sup>**

Paseo de la Castellana 66 · 4<sup>a</sup> Pl. · 28046 Madrid · España · madrid@lombardodier.com  
Credit institution supervised in Spain, by the Banco de España and the Comisión Nacional del Mercado de Valores (CNMV).

#### **Lombard Odier Gestión (España) S.G.I.I.C, S.A.U.**

Paseo de la Castellana 66, 4<sup>a</sup> Pl. · 28046 Madrid · España · madrid@lombardodier.com  
Management Company supervised by the Comisión Nacional del Mercado de Valores (CNMV).

### MILAN

#### **Lombard Odier (Europe) S.A. · Succursale in Italia<sup>2</sup>**

Via Santa Margherita 6 · 20121 Milano · Italia  
milano-cp@lombardodier.com  
Credit institution supervised in Italy by the Commissione Nazionale per le Società e la Borsa (CONSOB) and la Banca d'Italia.

### MOSCOW

#### **Bank Lombard Odier & Co Ltd · Representative Office Moscow**

2 Letnikovskaya st.2, bld.1 · 115114 Moscow · Russian Federation · moscow@lombardodier.com  
Under the supervisory authority of the Central Bank of the Russian Federation.

### PARIS

#### **Lombard Odier (Europe) S.A. · Succursale en France<sup>2</sup>**

8, rue Royale · 75008 Paris · France.  
RCS PARIS B 803 905 157 · paris@lombardodier.com  
Credit institution supervised in France by the Autorité de contrôle prudentiel et de résolution (ACPR) and by the Autorité des Marchés Financiers (AMF) in respect of its investment services activities. Business permit No.23/12. Registered in Luxembourg - No. B169 907.  
Insurance intermediary authorised by the Commissariat aux Assurances (CAA) No.2014 CM002. The registration with the CAA can be verified at [www.orias.fr](http://www.orias.fr).

## AFRICA | AMERICAS | ASIA - PACIFIC | MIDDLE EAST

### BERMUDA

#### **Lombard Odier Trust (Bermuda) Limited**

3rd Floor, Victoria Place · 31 Victoria Street · Hamilton  
HM 10 · Bermuda · bermuda@lombardodier.com  
Licensed to conduct Trust, Investment and Corporate Service Provider Business by the Bermuda Monetary Authority.

### DUBAI

#### **Bank Lombard Odier & Co Ltd · Representative Office Dubai**

Conrad Business Tower · 12th Floor · Sheikh Zayed Road · P.O. Box 212240 · Dubai · UAE  
dubai@lombardodier.com  
Under the supervisory authority of the Central Bank of the UAE.

### HONG KONG

#### **Lombard Odier (Hong Kong) Limited**

3901, Two Exchange Square · 8 Connaught Place · Central · Hong Kong · hongkong@lombardodier.com  
A licensed entity regulated and supervised by the Securities and Futures Commission in Hong Kong.

## ISRAEL

#### **Israel Representative Office · Bank Lombard Odier & Co Ltd**

Alrov Tower 11<sup>th</sup> floor · 46 Rothschild Blvd. · Tel Aviv  
6688312 · Israel · telaviv@lombardodier.com  
Not supervised by the Supervisor of Banks in the Bank of Israel, but by Swiss Financial Market Supervisory Authority which supervises the activities of Bank Lombard Odier & Co Ltd.

### JOHANNESBURG

#### **South Africa Representative Office · Bank Lombard Odier & Co Ltd**

140 West Street · Sandton  
Johannesburg 2196 · South Africa  
johannesburg@lombardodier.com  
Authorised financial services provider Registration number 48505.

### MONTEVIDEO

#### **Lombard Odier (Uruguay) SA**

Luis Alberto de Herrera · Torre 2 · Oficina 2305  
11300 Montevideo · Uruguay  
montevideo@lombardodier.com  
Supervised by Banco Central del Uruguay.

### MONTREAL

#### **Lombard Odier & Cie (Canada), Limited Partnership**

1000 Sherbrooke Street West · Suite 2200 · Montreal (Quebec) · Canada H3A 3R7  
montreal@lombardodier.com  
Regulated by the Autorité des Marchés Financiers du Québec.

### NASSAU

#### **Lombard Odier & Cie (Bahamas) Limited**

Goodman's Bay Corporate Centre · West Bay Street · P.O. Box N-4938 · Nassau · Bahamas  
nassau@lombardodier.com  
Supervised by the Central Bank of the Bahamas and the Securities Commission of the Bahamas.

### PANAMA

#### **Lombard Odier & Cie (Bahamas) Limited · Representative Office in Panama**

Oceania Business Plaza Torre 2000 · Oficina 38-D · Blvd. Pacifica · Urb. Punta Pacifica · Corregimiento de San Francisco · Panamá · panama@lombardodier.com  
Supervised by the Central Bank of the Bahamas and the Superintendencia de Bancos de Panamá.

#### **Lombard Odier (Panama) Inc.**

Oceania Business Plaza Torre 2000 · Oficina 38-D · Blvd. Pacifica · Urb. Punta Pacifica · Corregimiento de San Francisco · Panamá · panama@lombardodier.com  
Supervised by the Superintendencia del Mercado de valores de Panamá. Licensed to operate as an Investment Advisor. Res. SMV No.528-2013.

### SINGAPORE

#### **Lombard Odier (Singapore) Ltd.**

9 Raffles Place · Republic Plaza #46-02 · Singapore  
048619 · singapore@lombardodier.com  
A merchant bank regulated and supervised by the Monetary Authority of Singapore.

### TOKYO

#### **Lombard Odier Trust (Japan) Limited**

Izumi Garden Tower 41F · 1-6-1 Roppongi, Minato-ku · Tokyo 106-6041 · Japan · tokyo@lombardodier.com  
Regulated and supervised by the Financial Services Agency (FSA) in Japan. It holds a trust business license (FSA No.208) and is registered with Kanto Local Finance Bureau for Financial Instruments Business Operator (No.470).