

# ECB: "We Are In a Good Place"

A Publication of BMO Capital Markets Economic Research • Douglas Porter, CFA, Chief Economist, BMO Financial Group

The **ECB's June 5 rate cut of 25 bps** brought the deposit rate down to a 29-month low of 2.00%. The move was widely expected, so the market's focus was on the tone and there, the less dovish leaning came as a bit of a surprise. According to President Lagarde, after the latest move and the level of rates, *"I think we are getting to the end of a monetary policy cycle..."*

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Yes, despite all the uncertainty that Europe still faces (described as *"high"* and *"exceptional"*), the Governing Council feels that it is *"in a good position"* to deal with whatever comes its way. It was no surprise that there would be at least one dissenter to the latest rate cut (Austria's Robert Holzmann's announcement on Friday that *"I dissented in this week's rate decision"* was likely met with a yawn), but reports that a *"clear majority"* of voters said that they want to hold rates steady in July—and that *"a few"* are thinking of holding beyond July—supports BMO's view that **there will be one more cut... 25 bps in September** to land at 1.75%.

Now, we wait to see how the **trade talks** progress and if the EU will need to roll out its retaliatory tariffs. Meantime, **Europe is not sitting around** to see how things pan out. There are plenty of **fiscal stimulus** plans in the works, which President Lagarde pointed to. Given the uncertain environment, *"it is even more urgent for fiscal and structural policies to make the euro area economy more productive, more competitive. Recently announced measures to step up defence and infrastructure investment should also bolster growth in the present geopolitical environment"*. This includes the EU's €150 bln loan for its weapons fund and Germany's €500 bln defence/infrastructure fund, along with Chancellor Merz's new plan for €46 bln worth of tax breaks that will help support Germany until 2029, just in time for the next election. The tax package includes corporate tax cuts, a 30% deduction for companies who buy new M&E, and a generous 75% depreciation of new EVs.

The data we've seen so far this week certainly do not scream for more rate cuts. Yes, headline Euro Area inflation is below target for the first time since last September, and core and services CPI are also at their lowest levels in about three years. The jobless rate is at a record-low 6.2%, which supported a mild gain in retail sales. The Euro Area composite PMI has shown expansion for five straight months, although it is hovering at a 5-month low in May.

But, the **broader Euro Area economy started the year on a far stronger footing** than originally estimated. **Real GDP** grew 0.6% q/q in Q1, 2x that of the prior estimate, thanks to Ireland and Germany. (Just remember: President Lagarde said that she would not be surprised to see Q1 revised up.) On an annualized basis, that works out to 2.5%, beating Canada's 2.2% rate but still below Britain's 2.9%. But take it with a grain of salt as it is another example of how the trade war and tariff uncertainty have changed firms' behaviour... lots of front-running of tariffs, loading up on goods while they're available and at a reasonable cost. We may see more of that in Q2, with all the pauses in play (particularly between the U.S. and China). All will come at the expense of the second half of 2025.

In other words, we can groove with the ECB's stance.

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