

ECB Watcher

Small step on the horizon

HCOB Economics
December 6, 2024

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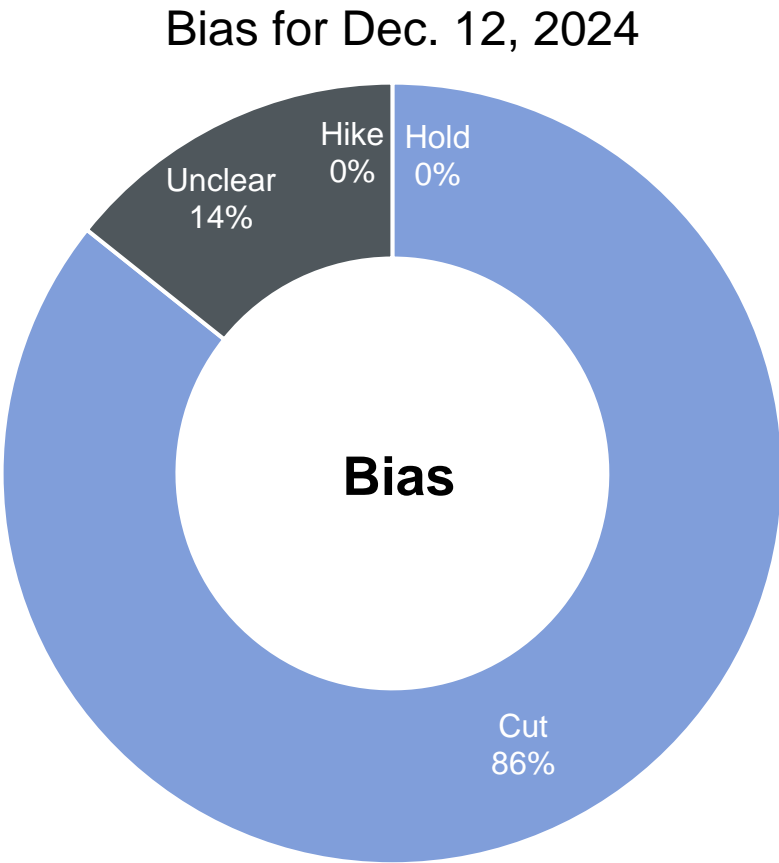
Executive Summary: Small step on the horizon (I)

- At their final meeting of the year on December 12, the European Central Bank (ECB) is expected to lower interest rates. Approximately 86% of the voting ECB Governing Council members are likely to support this measure, according to our analysis of their speeches and interviews. This would mark the fourth rate cut by the ECB this year, following decisions in June, September, and October.
- We expect the ECB to maintain its gradual approach and implement a 25 basis point (bp) cut. This would lower the deposit facility rate (currently at 3.25%) to 3.00% and the main refinancing rate (currently at 3.40%) to 3.15%.
- Additionally, we anticipate that the ECB will cut rates by another 25bp in both January and March 2025, maintaining the then reached rate level of 2.50% until the end of 2025. We believe the ECB will likely not continue the rate-cutting cycle beyond this point because we expect the average annual inflation rate in the eurozone to rise above 2.5% next year, significantly exceeding the ECB's target of 2%. Factors we consider contributing to rising inflation include a persistently weaker euro, potential retaliatory tariffs by the EU against the US, and continued above-average increases in unit labor costs. Higher natural gas prices and food prices, driven by new extreme weather events, are additional factors that could contribute to rising inflation.
- In November, the overall inflation rate (YoY) in the eurozone rose to 2.3%, up from 2.0% in October. Our nowcasting model forecasts a further increase to 2.5% in December.
- Although some ECB Governing Council members have not ruled out a larger 50bp cut, there have been clear coordinated efforts by the majority of ECB members in recent weeks to temper expectations of a larger rate cut next week. Most Council members seem to support a smaller 25bp step.
- Particularly the “hawkish” members of the ECB Governing Council, such as Bundesbank President Joachim Nagel, have advocated for “a gradual and cautious approach to rate cuts,” as he stated in early December. Similar statements have been made by Pierre Wunsch (Belgium), Gabriel Makhoul (Ireland), Robert Holzmann (Austria), and Executive Board member Isabel Schnabel.

Executive Summary: Small step on the horizon (II)

- Holzmann justified his stance in late November by stating that “price pressures in services are still high, some of the latest wage deals still aren’t in line with our goal and geopolitics pose additional risks.” Financial markets currently price in a moderate 25bp rate cut with about 93% probability, while a 50bp cut is priced in at only about 8%.
- We count François Villeroy de Galhau (France), Fabio Panetta (Italy), Yannis Stournaras (Greece), Mário Centeno (Portugal) and Mārtiņš Kazāks (Latvia) among the potential supporters of a 50bp reduction. The Greek representative on the ECB Governing Council, Stournaras, stated on behalf of this group: “A policy-rate path that remains too restrictive for too long could induce an undershooting of our inflation target over the medium term and impede growth. Should that occur, we would risk damaging our credibility.”
- The potential consequences of the US elections, such as tariffs or even a trade war between the US and the export-dependent eurozone, were also discussed by Governing Council members in their speeches. ECB President Christine Lagarde emphasized: “This can be in nobody’s interest, neither for the United States nor for Europe, or anyone for that matter. This would induce a global reduction in GDP.”
- Our favorite quote comes from Croatian Central Bank President Boris Vujčić: “When the road is slippery, you make small steps and this is what we are doing.”

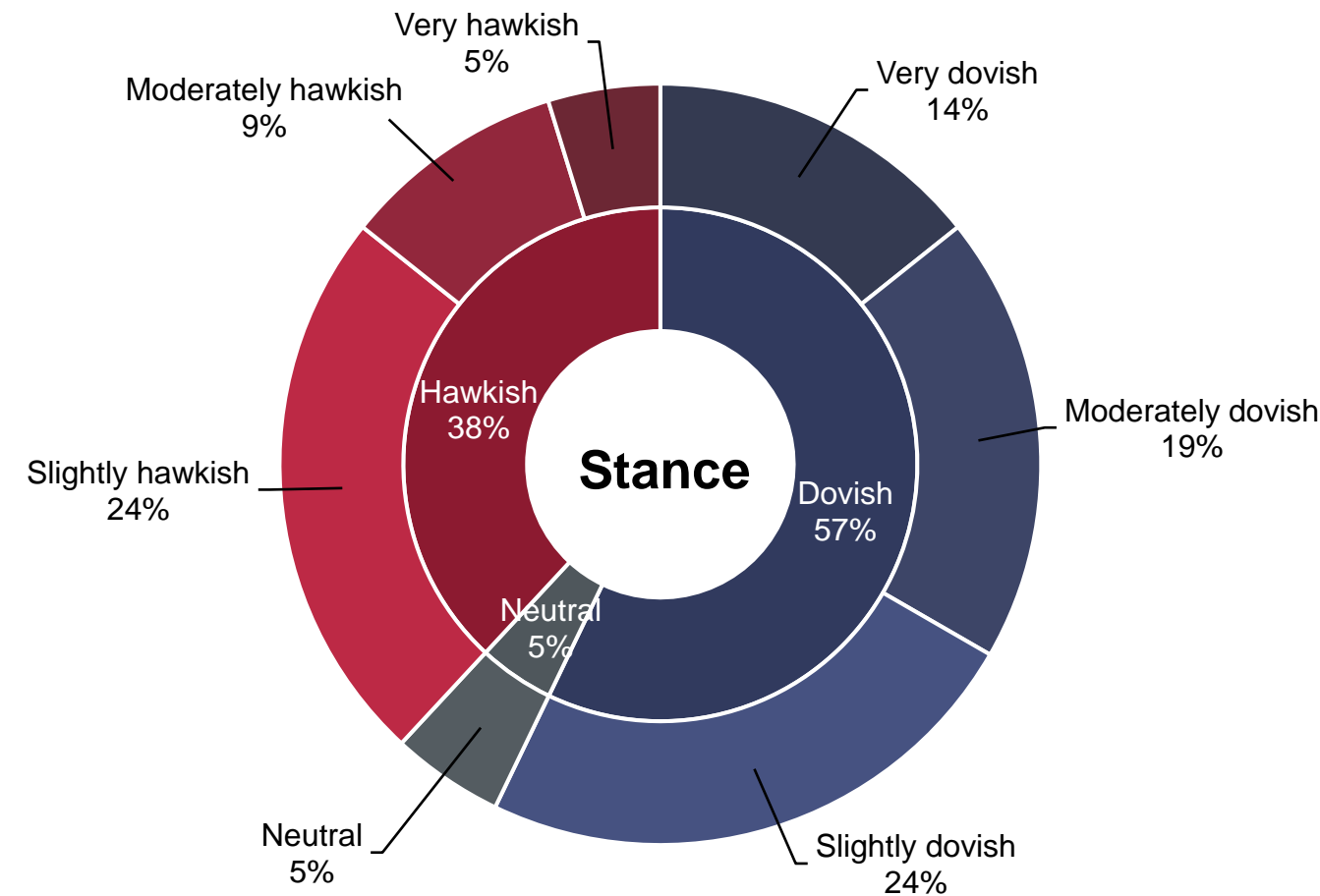
Around 86% of the ECB Governing Council (with voting rights) are likely to support a rate cut at the meeting on December 12.



Source: HCOB Economics
Note: We take the following into account when assessing a Governing Council member's bias: Statements since the last Governing Council meeting, previous statements, general stance, group dynamics, and the current economic situation of the eurozone and the respective country that the member represents. Only members with a voting right are considered.

More voting ECB members with a “dovish” than a “hawkish” stance will attend the December meeting.

Doves and Hawks in the ECB Governing Council



Source: HCOB Economics

Definition of „dovish“: certain tolerance when exceeding the inflation target.

Definition of „hawkish“: very limited tolerance when exceeding the inflation target.

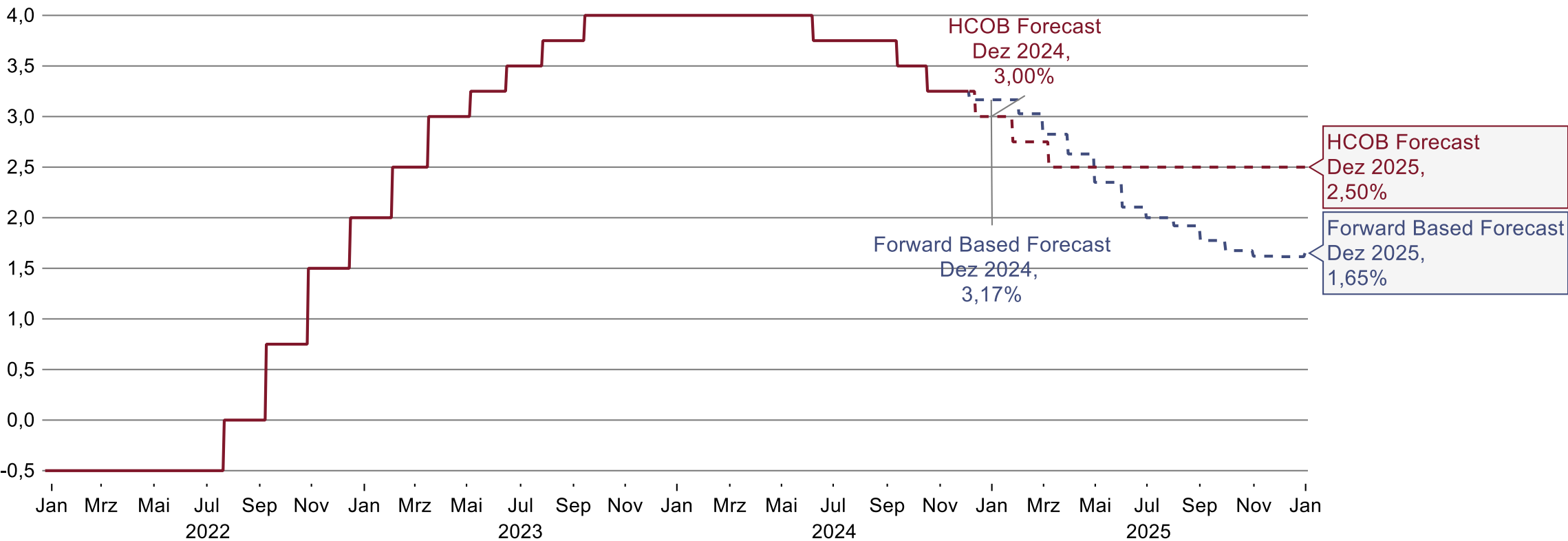
Note: With “stance” we mean a member’s general stance, which is rather static and likely not to change that much from meeting to meeting. The categorization of each ECB Governing Council member is based on an subjective qualitative judgement from HCOB Economics. Only members with a voting right are considered in this figure.

Overview of the Governing Council: Some ECB members have not made a clear statement on an interest rate decision, which is why we classify them as “Unclear”.

ECB Council Member	Position	Voting on Dec. 12, 2024	Bias for Dec. 12, 2024	General stance	Inflation (HICP, YoY, latest)	GDP (share of EZ in %)
Christine Lagarde	ECB President	Yes	Cut	Slightly hawkish	2,3	100
Luis de Guindos	ECB Vice-President	Yes	Cut	Moderately dovish	2,3	100
Isabel Schnabel	ECB Board Member	Yes	Cut	Moderately hawkish	2,3	100
Piero Cipollone	ECB Board Member	Yes	Cut	Very dovish	2,3	100
Philip R. Lane	ECB Board Member	Yes	Cut	Slightly dovish	2,3	100
Frank Elderson	ECB Board Member	Yes	Cut	Slightly hawkish	2,3	100
NCB Official of						
Joachim Nagel	Germany	No	Cut	Very hawkish	2,4	26,9
François Villeroy de Galhau	France	Yes	Cut	Moderately dovish	1,7	20,5
Fabio Panetta	Italy	Yes	Cut	Very dovish	1,6	15
José Luis Escrivá	Spain	Yes	Cut	Moderately dovish	2,4	11,3
Klaas Knot	The Netherlands	Yes	Cut	Slightly hawkish	3,8	7,1
Pierre Wunsch	Belgium	No	Cut	Very hawkish	5	3,9
Gabriel Makhlouf	Ireland	No	Unclear	Slightly hawkish	0,5	3,3
Robert Holzmann	Austria	Yes	Unclear	Very hawkish	2	3
Olli Rehn	Finland	Yes	Cut	Slightly dovish	1,9	1,8
Yannis Stournaras	Greece	No	Cut	Very dovish	3	1,8
Mário Centeno	Portugal	Yes	Cut	Very dovish	2,7	1,8
Peter Kažimír	Slovakia	Yes	Unclear	Slightly hawkish	3,6	0,8
Boris Vujčić	Croatia	Yes	Cut	Slightly dovish	4	0,5
Gaston Reinesch	Luxembourg	Yes	Unclear	Neutral	1,1	0,5
Boštjan Vasle	Slovenia	Yes	Cut	Slightly hawkish	1,6	0,4
Gediminas Šimkus	Lithuania	Yes	Cut	Slightly dovish	1,1	0,4
Christodoulos Patsalides	Cyprus	Yes	Cut	Moderately dovish	2,4	0,2
Mārtiņš Kazāks	Latvia	Yes	Cut	Moderately hawkish	2,3	0,2
Madis Müller	Estonia	No	Cut	Slightly hawkish	3,8	0,2
Alexander Demarco	Malta	Yes	Cut	Slightly dovish	2,3	0,1

Interest rate forecast from HCOB Economics: We expect the ECB to end its easing cycle with a terminal interest rate of 2.50% in March 2025.

ECB Deposit Facility Rate Forecast of HCOB Economics and Forecast based on ESTR Futures

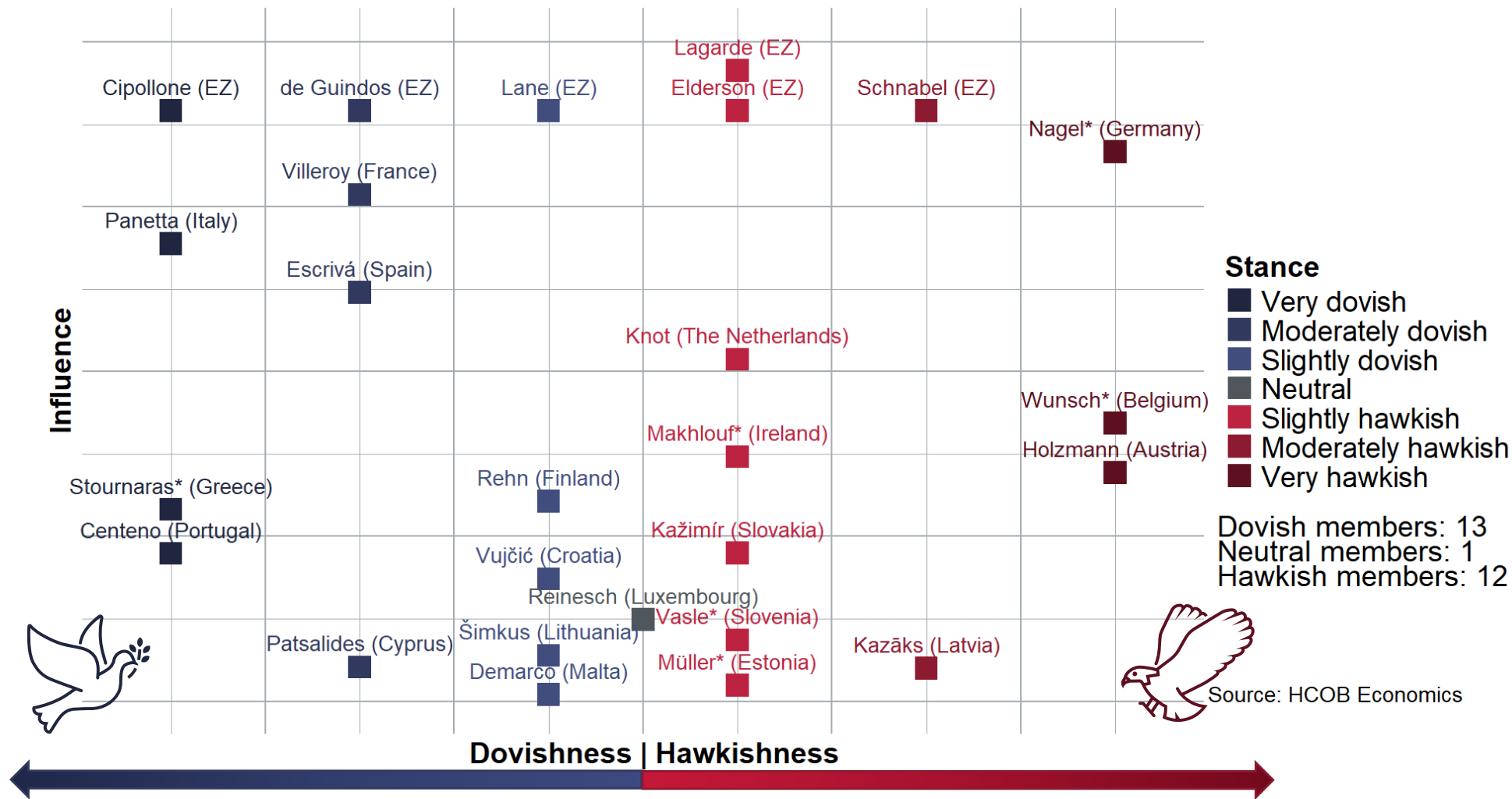


Source: Macrobond, HCOB Economics

Appendix

- **Influence and stance**
- **“One person, one quote”**

Influence and stance: In total, we classify 13 members as “dovish”, 12 as “hawkish” and one as “neutral”.



Note 1: Influence gauge is based on share of eurozone GDP. Governing Council members with no voting rights for the next meeting are marked with a superscript star.

Note 2: With “stance” we mean a member’s general stance, which is rather static and likely not to change that much from meeting to meeting. The categorization of each ECB Governing Council member is based on an subjective qualitative judgement from HCOB Economics.

“One person, one quote”: Quotes made since the last Governing Council meeting on Oct. 17, 2024 (I)

- **Christine Lagarde (ECB President):** “If anything, maybe it’s [a trade war with the US] a little net inflationary in the short term. But you could argue both ways; it depends what the tariffs are, what they are applied on and over what period of time.”
- **Luis de Guindos (ECB Vice-President):** “The balance of macro-risks has shifted from concerns about high inflation to fears over economic growth. [...] Inflation has moved closer to our 2% target.”
- **Isabel Schnabel (ECB Board Member):** “I’m not going to comment on the next monetary policy meeting. But given the inflation outlook, I think we can gradually move towards neutral if the incoming data continue to confirm our baseline. [...] we may not be so far from the neutral rate, which I would put into a range between 2% and 3%.”
- **Piero Cipollone (ECB Board Member):** “The current balance of risks suggests that we can and should reduce further the current level of monetary policy restriction. [...] The pace and extent of this reduction will depend on the incoming data.”
- **Philip R. Lane (ECB Board Member):** “We do not pre-commit to a particular speed but, over time, rates will have to be reduced. Monetary policy should not remain too restrictive for too long. Otherwise, the economy will not grow sufficiently and inflation will, I believe, fall below the target.”
- **Frank Elderson (ECB Board Member):** “We cannot pre-empt exactly what the appropriate policy response to an emerging bottleneck would be. Therefore, the flexibility and data-dependency that we have applied in navigating the challenges of the past few years will remain crucial in the years to come.”

“One person, one quote”: Quotes made since the last Governing Council meeting on Oct. 17, 2024 (II)

- **Joachim Nagel (NCB Official of Germany):** “Since inflation in services should gradually decline as wage pressures decrease, the point at which we can expect a sustained return to the 2% mark is approaching. It would therefore be too late to wait until the targeted inflation rate has been reached to ease policy. [...] It is important to remain cautious and to loosen monetary policy only gradually and not too quickly.”
- **François Villeroy de Galhau (NCB Official of France):** “Seen from today, there is every reason to cut on Dec. 12. Optionality should remain open on the size of the cut, depending on incoming data, economic projections and our risk assessment.”
- **Fabio Panetta (NCB Official of Italy):** “Restrictive monetary conditions are no longer necessary. We need to normalize our monetary-policy stance and move to neutral – or even expansionary territory, if necessary. The analysis, discussion and fresh forecast still lie ahead. But I think it is likely that we can again reduce interest rates in December.”
- **José Luis Escrivá (NCB Official of Spain):** “At the moment, the data suggests that we are approaching the inflation target broadly in line with the path envisaged in the September macroeconomic projections.”
- **Klaas Knot (NCB Official of the Netherlands):** “[The ECB’s data-dependent approach led to] a remarkably fast and, to date, relatively painless process of disinflation. As such, monetary policy today is gradually winding down some of the restrictions, based on the same data-dependent approach.”

“One person, one quote”: Quotes made since the last Governing Council meeting on Oct. 17, 2024 (III)

- **Pierre Wunsch (NCB Official of Belgium):** “My expectation is that the likelihood of a 50bp cut in December is very low. [...] Risks may even be tilted to the downside on inflation, and the likelihood that we remove restriction based on the new forecast in December is significant.”
- **Gabriel Makhoul (NCB Official of Ireland):** “It is clear that policy remains restrictive and, shocks aside, rates are on a downward trajectory. Given the volatility and the data and the substantial uncertainty regarding economic policy in trade partners, I remain open-minded on the slope of this downward trajectory.”
- **Robert Holzmann (NCB Official of Austria):** “As things currently stand, the possibility [of a December cut] exists, there’s nothing at the moment that would speak against it, but that doesn’t mean that it will automatically happen.”
- **Olli Rehn (NCB Official of Finland):** “If the latest statistical data and the new broad forecast update support the current inflation and growth outlook, further rate cuts are warranted at the December meeting.”
- **Yannis Stournaras (NCB Official of Greece):** “As inflation develops now and as the real economy develops now, I think yes we should have a cut in every meeting from now on until we get to what we call the neutral rate.”
- **Mário Centeno (NCB Official of Portugal):** “Interest rates now have to normalize — this means taking them back to neutral territory. Where is neutral territory? Well something around 2%, maybe slightly below, maybe 2%. Inflation has converged. It is as close to 2% as it can be.”

“One person, one quote”: Quotes made since the last Governing Council meeting on Oct. 17, 2024 (IV)

- **Peter Kažimír (NCB Official of Slovakia):** “Our decision to lower rates in October leaves the December meeting wide open. All options are on the table.”
- **Boris Vujčić (NCB Official of Croatia):** “Certainly the risk of undershooting the target has now increased compared to six months ago.”
- **Boštjan Vasle (NCB Official of Slovenia):** “We should keep going to neutral in measured steps. There is no urgency in discussing undershooting the target or going below the neutral rate. These are not current issues. By lowering interest rates further, we’ll be at the upper limit of the neutral rate estimates.”
- **Gediminas Šimkus (NCB Official of Lithuania):** “I can’t yet tell what will the decision be in December. But the direction is clear — down.”
- **Mārtiņš Kazāks (NCB Official of Latvia):** “We’ll definitely discuss this [a bigger-than-usual rate cut]. [...] We see that the inflation problem will soon end, and that means that we can lower rates.”
- **Madis Müller (NCB Official of Estonia):** “[The slow pace of economic recovery, especially in Germany and France] confirms the belief that the central bank no longer needs to keep interest rates at their current levels to permanently slow the rise in prices.”

“One person, one quote”: Quotes made since the last Governing Council meeting on Oct. 17, 2024 (V)

- **Christodoulos Patsalides (NCB Official of Cyprus):** “If there are no upside surprises to inflation, then we could and should continue lowering our interest rates. December is an important month because a lot more data will be available, including new projections. So, we will be in a better position to assess our stance.”
- **The following ECB Governing Council members made no public statement since the last Governing Council meeting:**
 - Gaston Reinesch (NCB Official of Luxembourg)
 - Alexander Demarco (NCB Official of Malta)

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