

ECB Watcher

Not yet the all-clear

HCOB Economics

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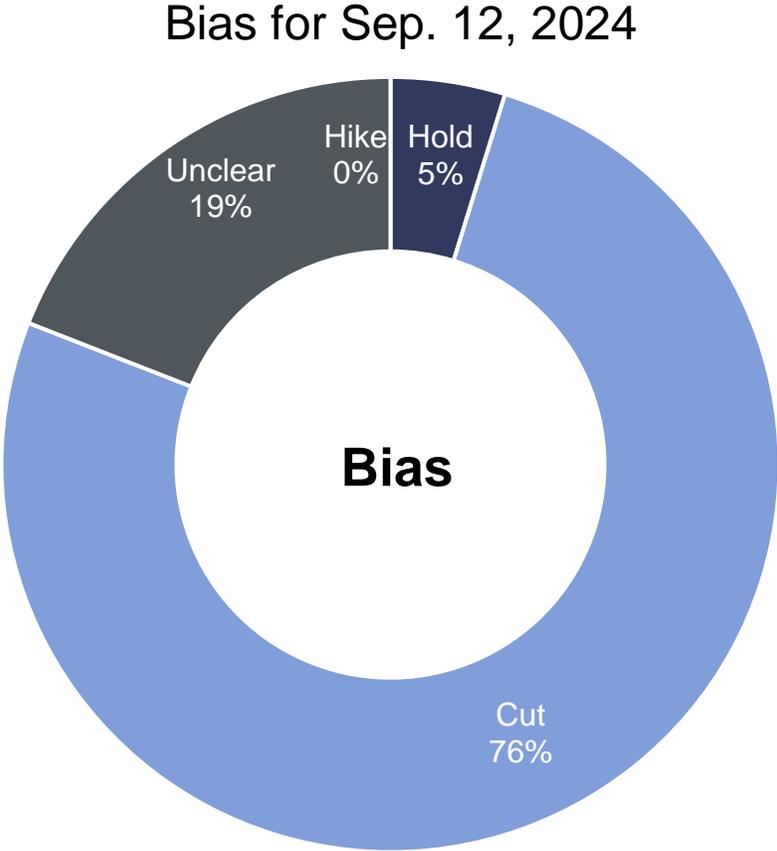
Executive Summary: Not yet the all-clear (I)

- In recent weeks, the members of the ECB Governing Council have been much more reluctant to advocate an easing of monetary policy than before the meeting in June. Nevertheless, we expect a majority of Council members to advocate a reduction in key interest rates at the upcoming meeting on September 12. Our analysis of Council members' speeches and interviews has shown that around 76% of voting Council members could be in favor of cutting interest rates.
- The ECB's key interest rates are currently 4.25% (main refinancing rate) and 3.75% (deposit facility rate). According to our forecast, which has remained unchanged since December last year, the ECB will cut interest rates by 25 basis points at the upcoming meeting and then leave them constant for the rest of the year. This time, the main refinancing rate will be lowered more sharply because the gap to the deposit rate will be reduced to 15 basis points in accordance with the ECB's decision.
- Our assessment is based not only on the statements of the Council members but also on the current data situation, which should make it easier for the ECB to lower interest rates in September. In particular, inflation in the eurozone was only just above the ECB's target of 2% in August at 2.18% (headline, YoY). In addition, economic indicators such as the HCOB Composite PMIs for the eurozone, which stood at 51 points in August, pointed to stagnating growth momentum. YoY growth in negotiated wages has also slowed and amounted to 3.55% in the second quarter, compared to 4.47% in the previous quarter.
- However, it is important to note that these data only represent snapshots. Inflation is likely to rise again in the coming months, partly due to base effects, meaning that 3% could be within sight again by the end of the year. For September, e.g., our in-house nowcasting model is already forecasting a figure of 2.3% for the headline inflation rate.
- Wage growth could also pick up again in the second half of the year. ECB Chief Economist Philip Lane, e.g., argued at the end of August that, according to the 'ECB Wage Tracker', further wage increases could still be expected in the second half of 2024. At the same time, however, he reassured that the race to catch up wages had then reached its peak and that the pace was likely to slow significantly over the next two years.

Executive Summary: Not yet the all-clear (II)

- The Governing Council of the ECB is still largely ‘hawkish’. The head of the Bundesbank, Joachim Nagel, who belongs to the ‘hawkish’ camp, has warned in recent weeks that “a timely return to price stability cannot be taken for granted” and that the ECB should therefore “be careful and must not lower policy rates too quickly.” He was particularly concerned about core inflation, especially in the services sector, which remains high and “a matter of concern.” Nagel also sees the risk that “a somewhat stronger economic recovery could further delay the return [to the 2% target].”
- In contrast to the more restrictive voices, the head of the Finnish central bank, Olli Rehn, was more ‘dovish’. Rehn emphasized that there are downside risks to the growth outlook and that the process of disinflation is already underway. “At the same time, the growth forecast is more subdued,” which in his opinion “reinforces the case for a rate cut in September.” He furthermore added that “this is how I see the monetary policy situation given the data and analysis currently available,” underlining his support for a looser monetary policy stance.
- Our favorite quote comes from Austrian central bank president Robert Holzmann: “For some, the impression is widespread that the fight is won. To a large extent it probably is, but definitely there are some areas where inflation is still lingering, and these are the ones that can become dangerous.”

The majority of the ECB Governing Council (with voting rights) is likely to be in favor of lowering key interest rates at the meeting on September 12.

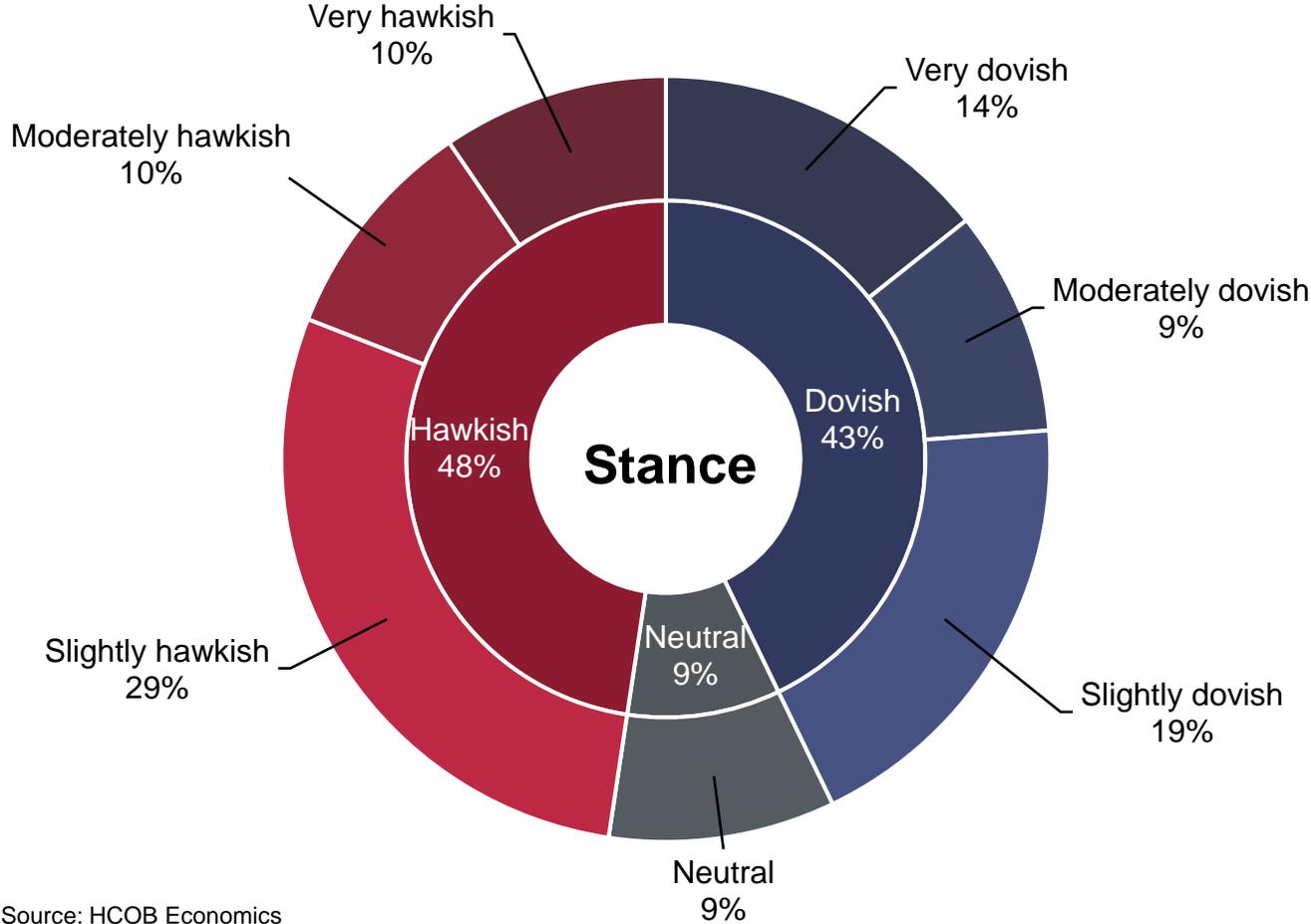


Source: HCOB Economics

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.

The Council remains predominantly 'hawkish', but members like Rehn have recently switched camps, slowly shifting the balance towards 'dovish'.

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.

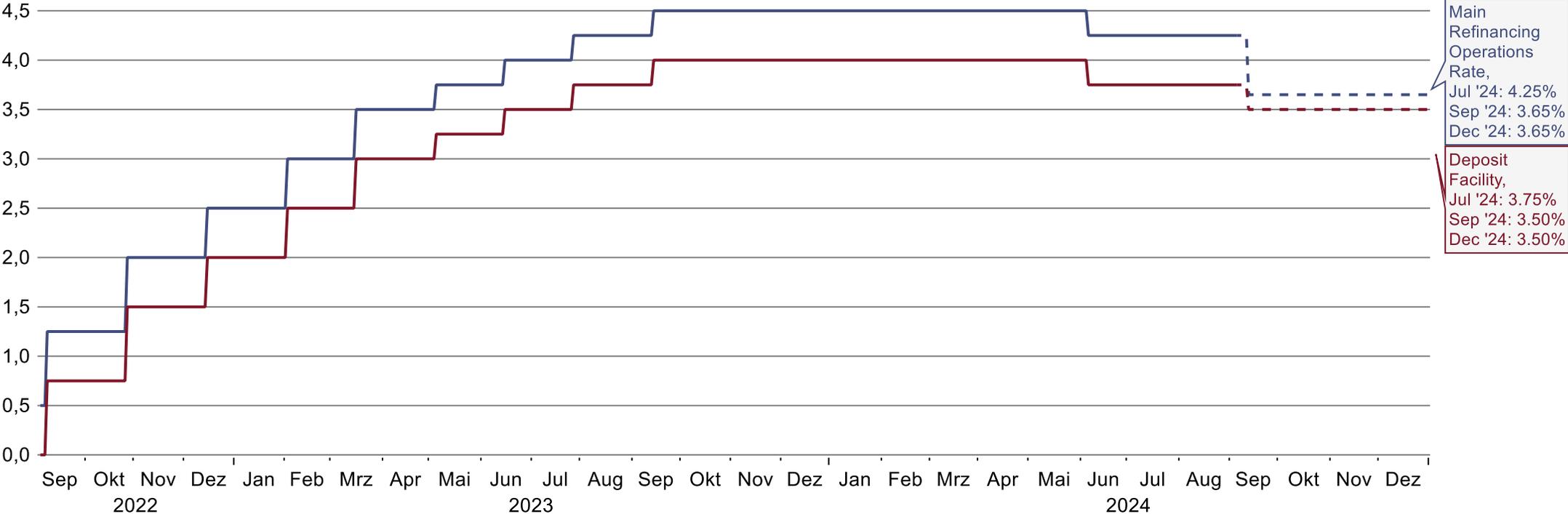
Note: With “stance” we mean a member’s general stance, which is rather static and likely not to change that much from meeting to meeting. The categorization of each ECB Governing Council member is based on an subjective qualitative judgement from HCOB Economics. Only members with a voting right are considered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

Overview of the Governing Council: Escrivá is the new Central Bank Governor in Spain and Demarco currently steps in for Malta's Scicluna.

ECB Council Member	Position	Voting on Sep. 12, 2024	Bias for Sep. 12, 2024	General stance	Inflation (HICP, YoY, latest)	GDP (share of EZ in %)
Christine Lagarde	ECB President	Yes	Cut	Slightly hawkish	2,2	100
Luis de Guindos	ECB Vice-President	Yes	Cut	Moderately dovish	2,2	100
Isabel Schnabel	ECB Board Member	Yes	Cut	Moderately hawkish	2,2	100
Piero Cipollone	ECB Board Member	Yes	Cut	Very dovish	2,2	100
Philip R. Lane	ECB Board Member	Yes	Cut	Slightly dovish	2,2	100
Frank Elderson	ECB Board Member	Yes	Unclear	Slightly hawkish	2,2	100
NCB Official of						
Joachim Nagel	Germany	Yes	Hold	Very hawkish	2	27,3
François Villeroy de Galhau	France	No	Cut	Moderately dovish	2,2	20,7
Fabio Panetta	Italy	Yes	Cut	Very dovish	1,3	15,1
José Luis Escrivá	Spain	Yes	Unclear	Neutral	2,4	11,1
Klaas Knot	The Netherlands	Yes	Cut	Slightly hawkish	3,3	7,1
Pierre Wunsch	Belgium	Yes	Cut	Very hawkish	4,5	3,9
Gabriel Makhlouf	Ireland	Yes	Cut	Slightly hawkish	1,1	3,3
Robert Holzmann	Austria	No	Hold	Very hawkish	2,5	3
Olli Rehn	Finland	Yes	Cut	Slightly dovish	1,1	1,8
Yannis Stournaras	Greece	Yes	Cut	Very dovish	3,1	1,8
Mário Centeno	Portugal	No	Cut	Very dovish	1,8	1,8
Peter Kažimír	Slovakia	Yes	Cut	Slightly hawkish	3,2	0,8
Boris Vujčić	Croatia	Yes	Cut	Slightly dovish	3	0,5
Gaston Reinesch	Luxembourg	Yes	Unclear	Neutral	1,7	0,5
Boštjan Vasle	Slovenia	No	Cut	Slightly hawkish	1,1	0,4
Gediminas Šimkus	Lithuania	Yes	Cut	Slightly dovish	0,7	0,4
Christodoulos Patsalides	Cyprus	Yes	Cut	Moderately dovish	2,2	0,2
Mārtiņš Kazāks	Latvia	Yes	Cut	Moderately hawkish	0,9	0,2
Madis Müller	Estonia	Yes	Unclear	Slightly hawkish	3,4	0,2
Alexander Demarco	Malta	No	Unclear	Neutral	2,5	0,1

Interest rate forecast from HCOB Economics: Due to rising inflation in the eurozone, we do not expect any further interest rate cuts this year after September.

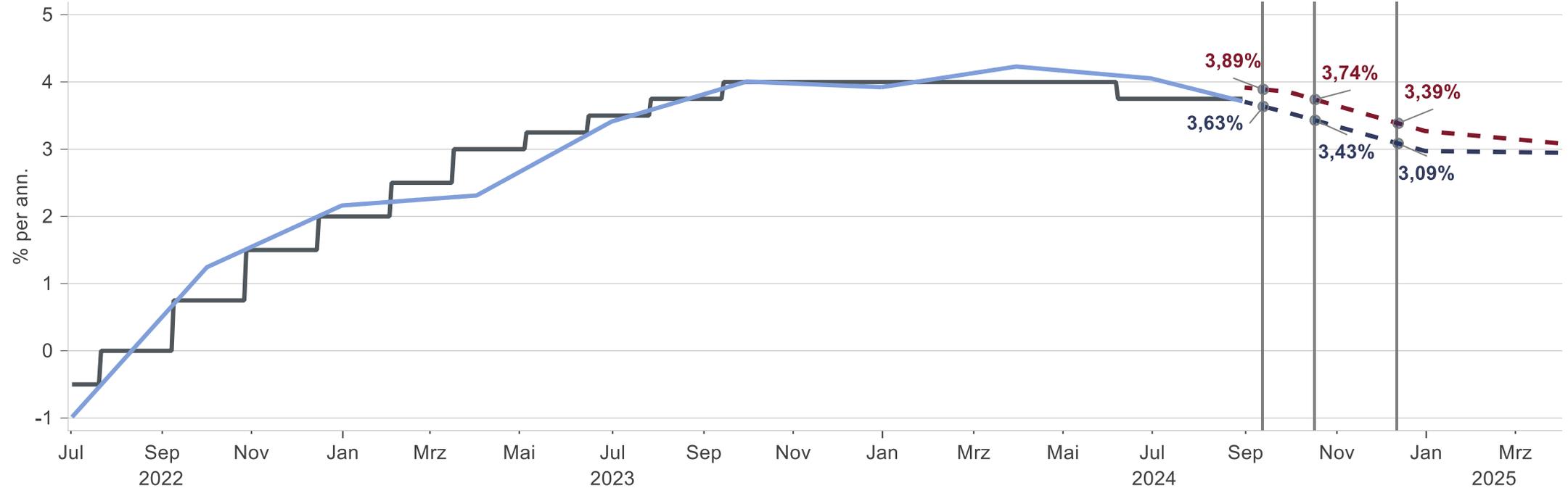
ECB policy rates and forecasts of HCOB Economics



Source: Macrobond, HCOB Economics. *The difference between the Main Refinancing Rate (MRF) and the Deposit Facility Rate (DFR) will be reduced from 0.5 pp to 0.15 pp by September 18. This is considered in the September forecast.

Hypothetical ECB interest rate path: According to our calculations, the ECB could keep interest rates high for longer if inflation rises at the end of the year.

ECB deposit facility rate (actual and predicted)



— Predicted ECB deposit facility rate (based on eurozone HICP headline inflation & real GDP growth forecasts of HCOB Economics)
 — Estimated ECB deposit facility rate
- - - Predicted ECB deposit facility rate (based on eurozone HICP headline inflation & real GDP growth projections of ECB Staff)
 — Actual ECB deposit facility rate

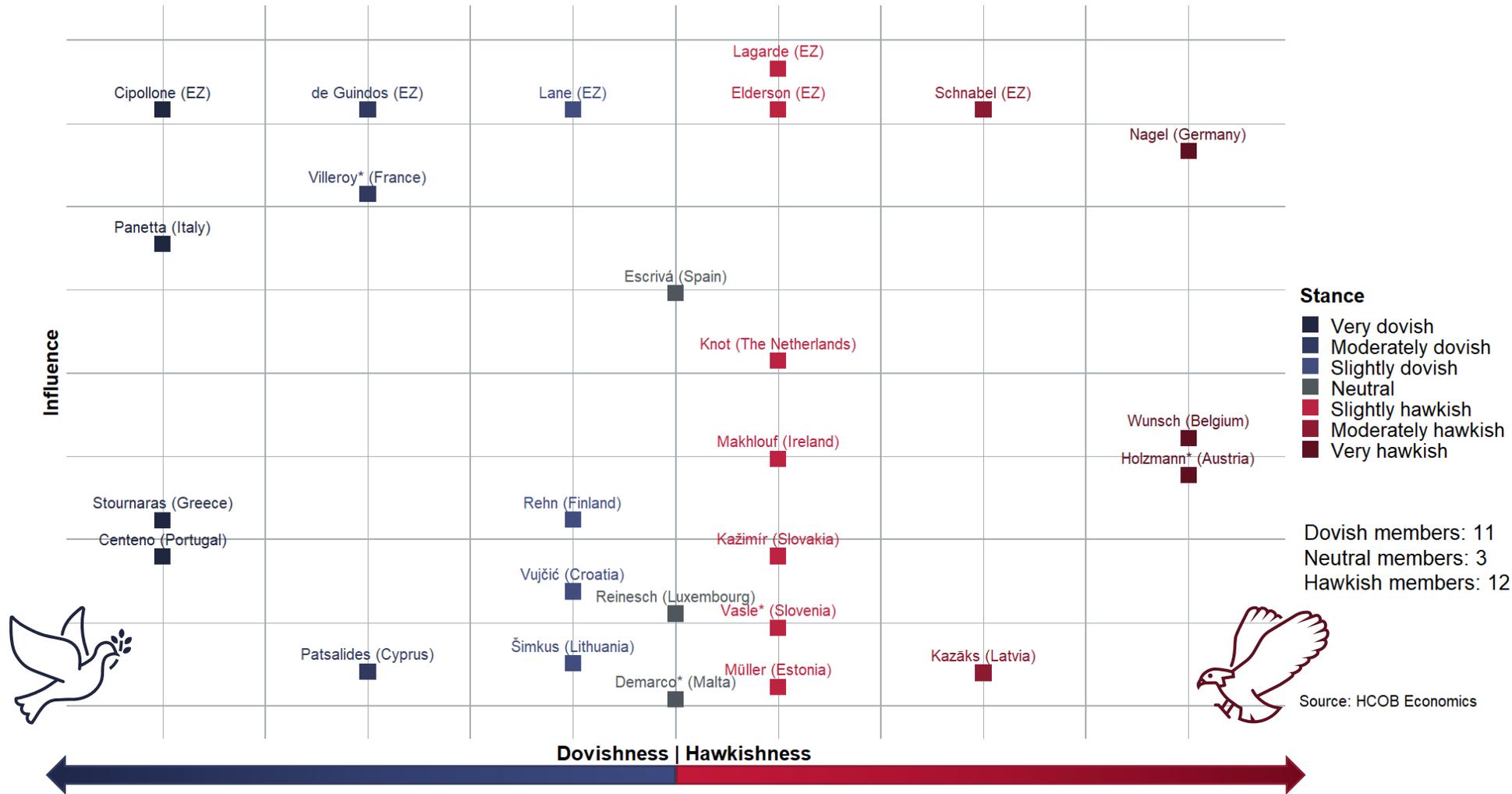
Source: Macrobond, HCOB Economics, ECB (European Central Bank). Note: Vertical lines indicate upcoming ECB Governing Council meetings in September, October, and December.

Note: We estimate a Taylor-type interest rate rule for the ECB, assuming that the ECB sets its policy rate in reaction to eurozone HICP inflation and real GDP growth. The dashed lines represent predictions of the ECB deposit facility rate, using forecasted values of these variables. Particularly, we use forecasts from HCOB Economics and the latest ECB Staff projections to calculate the counterfactual future rate path. Further note that these predictions do not necessarily represent the expected future rate path anticipated by HCOB Economics, but rather serve as a hypothetical scenario based on the given data. Our actual prediction remains the one presented in the previous slide.

Appendix

- Influence and stance
- 'One person, one quote'

Influence and stance: For the time being, we classified Escrivá and Demarco as 'neutral', as we did not yet have any speeches from them to analyze.



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 a subjective qualitative judgement from HCOB Economics.

‘One person, one quote’: Quotes made since the last Governing Council meeting on July 18, 2024 (I)

- **Christine Lagarde (ECB President):** “So, with additional data, if that data actually confirms the disinflationary process that is at work at the moment, it will reinforce our confidence.”
- **Luis de Guindos (ECB Vice-President):** “[...] we decided to keep interest rates unchanged because we will have more information in September, and especially new macroeconomic projections, so we will be able to better reassess the monetary policy stance.”
- **Isabel Schnabel (ECB Board Member):** “Along with signs of a potential decline in economic momentum in other parts of the world, there is less risk that a further moderate and gradual dialling back of policy restraint could derail the path back to price stability.”
- **Piero Cipollone (ECB Board Member):** “Yes, there is a real risk that our stance could become too restrictive. We must ensure that inflation converges to our target without holding back the economy unnecessarily, because we desperately need investment and growth in Europe. Every delay in this area puts us at a serious disadvantage.”
- **Philip R. Lane (ECB Board Member):** “[...] the return to target needs to be sustainable: a rate path that is too high for too long would deliver chronically below-target inflation over the medium term and would be inefficient in terms of minimising the side effects on output and employment.”
- **Joachim Nagel (NCB Official of Germany):** “[...] a timely return to price stability cannot be taken for granted. Therefore, we need to be careful and must not lower policy rates too quickly.”

‘One person, one quote’: Quotes made since the last Governing Council meeting on July 18, 2024 (II)

- **François Villeroy de Galhau (NCB Official of France):** “It would be fair and wise to decide in favour of a new rate cut.”
- **Fabio Panetta (NCB Official of Italy):** “I think it is reasonable to expect that from now on we will enter a phase of easing monetary conditions as inflation falls and the global economy slows down.”
- **Klaas Knot (NCB Official of the Netherlands):** “As long as our disinflation path still converges toward the return of 2 percent inflation before the end of 2025, then of course I’m comfortable with gradually taking our foot off the brake — because then we need less restriction.”
- **Gabriel Makhlouf (NCB Official of Ireland):** “We’ve got no predetermined rate path. We’re adopting a meeting-by-meeting approach.”
- **Robert Holzmann (NCB Official of Austria):** “I think we have to look more carefully at the data. I hope we can do it, I am not against cutting, only I am afraid that I don’t want to cut too early.”
- **Olli Rehn (NCB Official of Finland):** “And there are risks to the downside to our growth outlook. So, disinflation is in the process. At the same time, the growth outlook is more subdued. In my eyes, this reinforces the case for a rate cut in in September, and that’s how I see the monetary policy stance in light of all this data and analysis we have for the moment.”

‘One person, one quote’: Quotes made since the last Governing Council meeting on July 18, 2024 (III)

- **Yannis Stournaras (NCB Official of Greece):** “I still expect two rate cuts this year if disinflation continues as expected. In addition, growth is weaker than expected, which also speaks in favour of interest rate cuts.”
- **Mário Centeno (NCB Official of Portugal):** “Of course the most likely move in terms of monetary policy is to continue cutting rates. September — it’s easy. October is going to be a funny meeting. It’s always dependent on data. But it’s not on data points, it’s on data trajectories. We don’t look at data points, we look at data trends.”
- **Peter Kažimír (NCB Official of Slovakia):** “Enjoy the summer lull and wait for the much-anticipated September ‘health check’. The upcoming data, combined with fresh forecasts, will set the stage for any necessary decisions.”
- **Boštjan Vasle (NCB Official of Slovenia):** “Financial indicators show that the monetary policy transmission is working smoothly and homogeneously and supporting the return of inflation to the medium-term target level of 2%.”
- **Gediminas Šimkus (NCB Official of Lithuania):** “If there are no surprises or black swans and inflation converges as expected, further monetary-policy easing will undoubtedly be on the table in the next meetings. I have no doubt that the issue of cutting will be put up for discussion in September.”
- **Mārtiņš Kazāks (NCB Official of Latvia):** “As for monetary policy, I fully agree with Isabel [Schnabel]’s storyline that we can ease up monetary policy [in a gradual and data-dependent manner].”

‘One person, one quote’: Quotes made since the last Governing Council meeting on July 18, 2024 (IV)

- **Madis Müller (NCB Official of Estonia):** “[For the] next ECB Governing Council meeting [...] in September [...] we [cannot] promise too much in advance. At least one more cut [this year is reasonable, but I cannot say that with certainty.]”
- **The following ECB Governing Council members made no public statement since the last Governing Council meeting:**
 - Frank Elderson (ECB Board Member)
 - José Luis Escrivá (NCB Official of Spain)
 - Pierre Wunsch (NCB Official of Belgium)
 - Boris Vujčić (NCB Official of Croatia)
 - Gaston Reinesch (NCB Official of Luxembourg)
 - Christodoulos Patsalides (NCB Official of Cyprus)
 - Alexander Demarco (NCB Official of Malta)

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