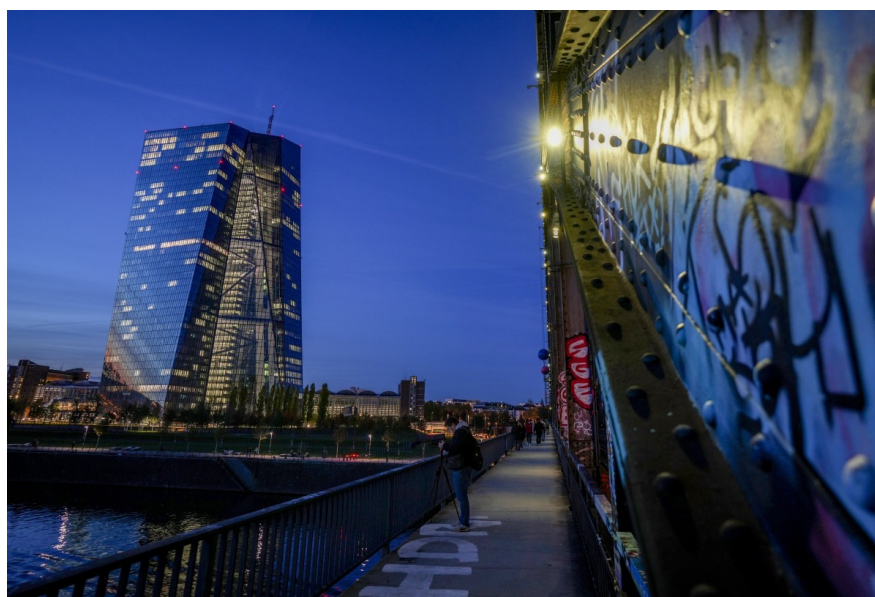


## March staff projections will be another argument for ECB hawks

The European Central Bank staff is currently working hard on the March macro projections. As the cut-off date for the technical assumptions has been reached, we take a look at how these assumptions alone will give the hawks enough support to get the ECB to announce the end of QE at the March meeting



European Central Bank, Frankfurt, Germany

Source: Shutterstock

“It’s difficult to make predictions, especially about the future”. Every professional forecaster knows this humorous saying and it nicely illustrates the difficulty every forecaster is facing. Everyone knows how uncertain forecasts are, but still there has always been high demand for predictions of all kinds. Be it about the weather, sport games, financial markets or the economy. For ECB staff members, the demand for their next round of economic forecasts has never been higher. The heat is almost unbearably on for ECB staff as the outcome of the forecasts will have direct policy implications.

The ECB excitement continues. Last week, ECB President Christine Lagarde tried to return the [hawkish genie back into the bottle](#) and Chief Economist Philip Lane felt urged to publish another

blog entry on the ECB site, explaining the inflation differences between the US and the eurozone. This was not an attempt to fully reverse the main messages of the ECB press conference. Don't forget that the new hawkishness with 'risks to the inflation outlook are tilted to the upside' and the disappearance of the phrase that 'monetary accommodation was still needed for inflation to stabilise at the 2% inflation target' was agreed and prepared by the entire ECB Governing Council. However, the ECB had clearly not expected such an aggressive reaction by financial markets, pricing in two rate hikes already this year. We expect more calming interventions by ECB officials in the coming weeks, without taking away the hawkish twist.

## What to expect from the ECB's March inflation projections

The next ECB showdown will be the 10 March meeting. This will be the moment to alter its asset purchase programme and this will also be the moment to possibly give clearer guidance on future rate changes. All these decisions will be closely linked to the ECB's staff projections.

A lot of pressure has been on these staff projections as they have structurally underestimated recent inflation dynamics, as much as they structurally overestimated inflation dynamics in the decade before the pandemic. Though formally correct, it is remarkable that several ECB officials recently commented that the staff projections were not the Governing Council's forecasts and that the Governing Council was not bound by these forecasts. Let's not forget that these so-called staff projections twice a year are the result of joint forecasts by the national central banks and twice by ECB staff in Frankfurt. Enough to have sufficient buy-in also from national central bank governors one would think.

In any case, the March projections will be ECB staff projections and if the past is of any guidance, the cut-off date for these projections must have been any of the last days. As any inflation projection is currently highly dependent on the underlying energy price assumption, we have a brief look at the technical assumptions the ECB uses and how they have changed since the December meeting.

The ECB uses so-called technical assumptions for the euro exchange rate, oil prices and interest rates. For the exchange rate, this assumption is simply a continuation of the values of the last two weeks before the cut-off date, for interest rates and oil prices, the ECB uses future prices.

- **Bond yields.** The hawkish tone at the ECB press conference pushed up bond yields and widened spreads by some 50 basis points compared with the December projections. At first glance, the irony is that the strong reaction by financial markets could actually undermine any ECB normalisation plans. However, at second glance, changes in bond yields with these magnitudes have hardly had any impact on its inflation forecasts
- **Exchange rate.** Compared with the December projections, the change in the euro exchange rate has been too small to have a direct impact on the ECB's inflation forecasts.
- **Oil prices.** Again the main driver of the ECB's inflation forecasts. Compared with the futures applied in the December projections, oil price futures were up by another 10% across the curve. This alone could push up headline inflation by 0.1 to 0.2 percentage points.

Back in December, the ECB projections predicted headline inflation to come in at 3.2% in 2022 and 1.8% in both 2023 and 2024. Simply applying what we expect the next technical assumptions to be should push the inflation projections for 2023 and 2024 already very close if not exactly to 2%. And there will be more: the pass-through of higher energy and commodity prices has been structurally underestimated by the ECB's macro model and could be remodelled based on the

experiences of the last months, opening the door for further upward revisions of the inflation forecasts.

Given the rising criticism on the ECB forecasts voiced by several ECB officials, we expect a growing majority at the ECB to at least support a faster reduction of the asset purchases at the March meeting. For this, inflation doesn't have to be at 2.0% over the next years. Interestingly, if oil prices were to stay at their current level, headline inflation would have to be revised up by some 0.5 percentage points for 2023 and 2024. This is something that will also not have escaped the attention of ECB members.

It is hard to see how the March ECB inflation forecasts will not be higher than in December. Admittedly, it is still mainly an energy price story but another upward revision of the 2023 and 2024 forecasts will convince enough ECB members to support a faster reduction of the asset purchases and to bring them to an end by 3Q, opening the door to a rate hike in 4Q.

## Author

**Carsten Brzeski**

Global Head of Macro

[carsten.brzeski@ing.de](mailto:carsten.brzeski@ing.de)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.