

## What central banks are set to do next

We think the Federal Reserve has finished hiking rates, and the ECB and Bank of England aren't far behind



ECB President, Christine Lagarde's future options are somewhat limited

### Federal Reserve

At the recent Jackson Hole Fed symposium, Fed Chair Jerome Powell acknowledged that monetary policy is “restrictive” and that policymakers will “proceed carefully” in determining whether to hike interest rates further. September appears set for a pause given recent encouraging signals on inflation and labour costs, but robust activity data means the door remains ajar for a further potential hike. Markets see a 50-50 chance of a final hike while we think rates have most probably peaked.

Households are rapidly running down pandemic-era savings, and rising consumer loan delinquencies indicate growing stresses that will be intensified by the restart of student loan repayments. Amid weakening global activity, we are, unfortunately, in the camp that fears this is more of a downturn-delayed rather than recession-averted story. Fortunately, we think that inflation will continue to slow rapidly and this will afford the Federal Reserve the flexibility to respond swiftly to this challenging environment with interest rate cuts through 2024.

### European Central Bank

Macro developments over the summer have caused further complications for the ECB. While the

rapid worsening of the economy should come as a surprise, at least judging from overly optimistic ECB growth forecasts so far, the speed with which headline inflation is coming down should still leave the central bank uncomfortable.

Core inflation also remains too high and wage growth up until now signals that even without excessive wage settlements core inflation could stay higher for longer.

We still expect headline inflation to come down significantly after the summer, mainly on the back of German headline inflation falling. However, if the ECB sticks to its stance of putting more emphasis on actual data rather than on expected data, the current inflation picture still argues in favour of another rate hike.

After 425bp of rate hikes in slightly more than a year, a pause in the ECB's hiking cycle at the September meeting would make perfect sense. However, the worsening economy and our expectation of an acceleration of disinflationary risks after the summer could easily transform a pause into an actual full stop. The question is whether everyone at the ECB could live with a terminal rate of 3.75%. We think that the hawks would prefer 4% and will therefore push for one final rate hike at the September meeting. A last one for the road, even if it remains a very close call.

## Bank of England

The Bank of England looks poised to hike rates again in September, but November is less certain. Private sector wage growth is at a cycle high and looks unlikely to slow dramatically by the end of the year, and certainly not before November. Meanwhile, services inflation has risen higher again. And while we think the impact of lower gas prices should start to show through here with a lag, progress is likely to be limited by the time of the November meeting.

That said, the wider economy is showing signs of slowing amid higher interest rates, and the jobs market is also noticeably cooling. We're likely to see more evidence of this over the next couple of months. We're erring on the side of a pause in November, but we don't rule out another hike.

Bigger picture, the BoE is clear that it wants to keep rates high for a prolonged period. We've pencilled in the first cut for the second quarter of next year but we acknowledge that may end up being delayed.

## Authors

### James Knightley

Chief International Economist, US

[james.knightley@ing.com](mailto:james.knightley@ing.com)

### Carsten Brzeski

Global Head of Macro

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

### James Smith

Developed Markets Economist, UK

[james.smith@ing.com](mailto:james.smith@ing.com)

## 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>.