

Snap | 21 July 2022

ECB hikes rates by 50bp and softens forward guidance

A historic day for the European Central Bank. For the first time since 2011, the Bank has hiked interest rates and did so with a bang. Hiking rates by 50bp and softening forward guidance shows that the ECB thinks the window for a series of rate hikes is closing quickly



What did the ECB just announce?

- All three key ECB interest rates were increased by 50bp.
- Forward guidance was changed to a “meeting-by-meeting” approach, which is a more dovish tweak compared with the aggressive forward guidance from the June meeting.
- A Transmission Protection Instrument (TPI) was introduced but without any details.

This decision shows that the hawks must have got cold feet, fearing that the promised higher-than-25bp rate hike in September would be washed away by the looming recession. The agreement on a TPI had to be paid for by the doves with a stronger rate hike.

We all know that today’s rate hike will not bring down inflation in the short run - not even on the demand side of the economy, which will react much more to the looming recession than to any

ECB action. The hike, as well as potential further hikes, are all aimed at bringing down inflation expectations and to restore the ECB's damaged reputation and credibility as an inflation fighter. Today's decision shows that the ECB is more concerned about this credibility than about being predictable. This matters more than forward guidance. Today's decision conforms with our previous view that the ECB will not be able to deliver as many rate hikes over the next 12 months as markets had priced in after the June meeting.

Today's press conference will start at 2.45pm CET and ECB President Christine Lagarde will definitely have a lot to explain.

Author

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

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