Snap | 2 February 2023

ECB press conference brings more fog than clarity

During the Q&A session, European Central Bank president Christine Lagarde confirmed the ECB's hawkish stance, while probably also confusing some market participants

Christine Lagarde at today's ECB press conference

The facts are straight: the ECB hikes interest rates by 50bp today, gave a quasi pre-commitment to hike again by 50bp in March and kept the door open for further rate hikes beyond the March meeting. A very clear message if the ECB had limited its communication to the 1:15pm CET press release but it didn't.

More and not less confusion

We know that it is easy to criticise politicians and policymakers if you are just an observer and not in the driver's seat, but if anything, today's ECB press conference created more and not less confusion about the ECB's reaction function and the path beyond the March meeting. With phrases like "continuity in a steady state", it is doubtful that market participants really understand the ECB's plans. And the logic behind a "data dependent" and "meeting by meeting" approach combined with a pre-commitment to hike by 50bp in March is not comprehensive to everyone. Just trying to look through the fog of most parts of the press conference, what remains are remarks like a "disinflationary process is not already at play" and "we know that we have ground to cover". Probably the best hints that the ECB will not stop after the March meeting but will rather slow down the size and pace of rate hikes. At the same time, ECB president Christine Lagarde made clear that staying the course implied keeping interest rates in restrictive territory for a sufficiently long period.

Not done, yet

It took the ECB a while, but it seems to have got the hang of it: hiking interest rates. And as long as core inflation remains stubbornly high and core inflation forecasts remain above 2%, the ECB will continue hiking rates. The increasing probability that a recession will be avoided in the first half of the year also gives companies more pricing power as illustrated by still high selling price expectations remain elevated.

More generally speaking, we are currently witnessing a mirror image of the ECB up until 2019. Back then, the Bank had a clear easing bias and was chasing disinflation with all means possible, even though the root causes for disinflation lay outside of the ECB's realm. Now, the ECB has a clear tightening bias and is chasing inflation, which arguably also has its root cause in something the ECB cannot tackle. This is why the ECB is obviously shifting its focus on core instead of headline inflation. More generally speaking, it looks as the current generation of ECB policymakers will only back down once they are fully convinced that inflation is no longer an issue. In this regard, the slight improvement of the eurozone's growth prospects as well as abundant fiscal stimulus have given the Bank even more reason to continue with its hawkish mission.

The celebrated fiscal stimulus, which has eased recession fears, is indeed an additional concern for the ECB as it could transform a supply-side inflation issue into demand-side inflation. These are two factors that could extend inflationary pressures in the eurozone, albeit at a lower level than we see at the moment. As a consequence, we expect the ECB not only to continue hiking into late spring but also to keep interest rates high for longer than markets have currently pencilled in. Even after today's exciting press conference.

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