

ECB slows rate hike pace but ratchets up hawkishness

All good things come in threes...after the Federal Reserve and Bank of England, the European Central Bank has followed with a rate hike of 50bp. The ECB also announced it would start to reduce its bond portfolio, aka quantitative tightening, from March 2023 onwards



Ahead of today's meeting, the question was whether the ECB would opt for a larger-sized rate hike with a dovish message or for a smaller-sized rate hike with a hawkish message. The answer is clear: a smaller hike with a very hawkish message. In particular, the following phrases were surprisingly hawkish: "interest rates will still have to rise significantly at a steady pace to reach levels that are sufficiently restrictive to ensure a timely return of inflation to the 2% medium-term target. Keeping interest rates at restrictive levels will over time reduce inflation by dampening demand and will also guard against the risk of a persistent upward shift".

As regards the reduction of the ECB's bond holdings, the reinvestments of maturing bonds under the asset purchase programme (APP) portfolio will decline to €15 billion per month on average until the end of the second quarter of 2023 "and its subsequent pace will be determined over time".

The ECB also already published the results of its latest macroeconomic projections, expecting inflation to come down to 3.4% in 2024 and 2.3% in 2025. The 2024 number was revised upwards significantly. At the same time, the ECB expects only a short and shallow recession, forecasting eurozone growth to come in at 0.5% in 2023 and 1.9% in 2024. This is much more optimistic than our own growth forecast.

All in all, the ECB's crusade to not only fight inflation but to fight against any deterioration in its reputation and credibility continues. There is still very little the ECB can do to bring down actual inflation but it can contribute to re-anchoring inflation expectations. With today's announcement, it is clear that the ECB wants to first fully exploit interest rates as the main instrument to fight inflation and that the balance sheet reduction will stay on the back burner. Needless to say that with the still relatively optimistic growth outlook, the risk increases that the ECB pushes the eurozone economy further into recession with every new rate hike.

Author

Carsten Brzeski

Global Head of Macro

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>.