Further rate hikes flagged in latest ECB minutes

The minutes of the European Central Bank's July meeting underline its new approach to normalisation: we can do whatever we want, whenever we want

ECB President, Christine Lagarde at a news conference after July's meeting

In these fast-moving times, it is always hard to extract any hints for future ECB decisions from a meeting that took place four weeks ago. Still, the just-released minutes of the bank's July meeting reveal some interesting insights. Here are our top picks:

- The discussion on the Transmission Protection Instrument (TPI) actually took place before the discussion on hiking interest rates. The TPI was agreed upon unanimously.
- Concerns about the weak euro came on top of the policy-relevant discussion, with "*Members widely noted that the depreciation of the euro constituted an important change in the external environment and implied greater inflationary pressures for the euro area…*"
- Recession is still a forbidden word in the ECB's dictionary as it was only used nine times. However, there were many phrases like *downturn* or *contraction*, pointing to the same direction.
- Wage growth remains key for the ECB to identify second-round effects as "*Members agreed that the persistence of inflation depended, to a large extent, on the behaviour of wages. Wage growth, also according to forward-looking indicators, had continued to increase*

gradually over the last few months but still remained contained overall."

- The rate hikes by 50bp were broadly supported, with few ECB members calling for the initially almost pre-committed 25bp. The fact that many ECB officials, including ECB president Christine Lagarde, had publicly consistently repeated the intention to hike by 25bp since the June meeting was explained by "*The Governing Council thereby took a larger first step on its policy rate normalisation path than signalled at its previous meeting, applying the stated principles of data-dependence and optionality. This was seen as providing a clear signal of its determination to act and to fulfil its mandate.*"

All in all, the minutes illustrate how the momentum within the European Central Bank changed between the June and the July meeting and also stress its determination to continue hiking rates as the minutes repeatedly underline that the ECB is on a path of normalisation.

What to expect at the ECB's September meeting

ECB officials are returning from their holidays and are only gradually starting to become talkative again. Official comments which could hint at the next steps are still scarce. The discussion at the July meeting shows that growth concerns are mounting but that the ECB in our view is still too benign on the risk of an outright recession in the eurozone.

Looking ahead, we still think that the ECB is currently pursuing two main goals: anchoring inflation expectations and normalising monetary policy. As for inflation expectations, only business inflation expectations have come down somewhat. The US example, however, shows that even more aggressive rate hikes are less potent in bringing down survey-based inflation expectations than global commodity prices. The latest drop in US inflation expectations seems to be the result of falling gasoline prices and not so much of the latest Fed rate hikes. This could be a hint for the ECB that a series of more aggressive rate hikes might be too much of a good thing. This leaves it with at least normalising monetary policy. And here, we know that any neutral level of a policy rate also depends on the state of the economy. In a robust growth environment, the neutral rate will be higher than in a low growth or even recessionary environment.

Consequently, we still expect the ECB to take a less aggressive approach than the Fed and what markets are currently pricing in. We expect the bank to hike rates by another 50bp at the September meeting and then pause until spring next year. A recession, a winter energy crisis, and an ongoing war simply argue against overly aggressive rate hikes.

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