PREVIEW - ECB Policy Announcement due Thursday 12th September 2024

- **ECB policy announcement due Thursday September 12th; rate decision at 13:15BST/08:15EDT, press conference from 13:45BST/08:45EDT**
- **The consensus firmly expects the ECB to cut the deposit rate by 25bps to 3.5%**
- **Focus will be on what signals the ECB offers over future easing**

OVERVIEW: The ECB is expected to resume its rate-cutting cycle after pausing in July. Such an outcome is virtually fully-priced in by markets, and therefore attention will turn on what clues (if any) Lagarde provides on future easing plans. Note, a recent Reuters report suggested that policymakers are torn over how they weigh gloomy growth prospects against concerns over lingering inflation.

PRIOR MEETING: As expected, the ECB opted to stand pat on rates following its 25bps reduction in June. In the accompanying policy statement, the Governing Council reaffirmed that it will keep policy rates sufficiently restrictive for as long as necessary to achieve its goals. Furthermore, policymakers will continue to maintain a data dependent approach and not pre-commit to a specific policy path. At the follow-up press conference, President Lagarde said incoming data points to the economy growing in Q2, though likely at a slower rate than in Q1. On the inflation front, this was expected to fluctuate around current levels for the remainder of the year before declining towards the target over H2-2025 owing to weaker unit labour costs and other factors. In the Q&A segment, Lagarde noted that the discussion on the Governing Council was very much a case of "on the one hand" and "on the other hand", with the ultimate policy decision being unanimous. Lagarde was also keen to stress that the ECB is data dependent, but not specific data point dependent. Regarding the path ahead, Lagarde kept her cards close to her chest, suggesting that the September meeting is "wide open".

RECENT ECONOMIC DEVELOPMENTS: Headline inflation in the Eurozone printed 2.2% Y/Y in August (vs the previous 2.6%) on a prelim basis, with the move lower driven by developments in the energy space. The super core measure pulled back to 2.8% Y/Y from 2.9%, and services inflation rose to 4.2% Y/Y from 4.0%, with some of the move attributed to the Paris Olympics. The ECB's Consumer Expectations Survey saw the 12-month inflation expectation hold steady at 2.8% Y/Y, whilst the 3-year metric ticked higher to 2.4% Y/Y from 2.3%. In terms of market gauges of inflation, the 5y5y forward has pulled back to circa 2.08% from around 2.31% at the time of the last meeting. From a growth perspective, Eurozone GDP was confirmed at 0.2% Q/Q in Q2, whilst more timely survey data from S&P Global showed the August manufacturing PMI held steady at 45.8, while services rose to 52.9 from 51.9. The accompanying release noted "the 'Olympic effect' is also set to ensure that the Eurozone's GDP will show growth in the third quarter". Unemployment in the Eurozone stands at a historic low of 6.4%.

RECENT COMMUNICATIONS: Since the prior meeting, President Lagarde hasn't offered much in the way of pertinent commentary. Chief Economist Lane has noted that "the return to the 2% inflation target is not yet secure", adding that "the monetary stance will have to remain in restrictive territory for as long as needed to shepherd the disinflation process towards a timely return to the target". Germany's Schnabel stated that "…the closer policy rates get to the upper band of estimates of the neutral rate of interest – that is, the less certain we are how restrictive our policy is…the more cautious we should be." Her German colleague Nagel, who sits at the hawkish end of the spectrum, has cautioned that the ECB must not "lower policy rates too quickly". Elsewhere within the hawk camp, Austria's Holzmann said that when considering rate cuts "one has to be careful, or one could be forced to take a step back". For the doves, Italy's Panetta is of the view that "it's reasonable to expect that from here on we will be going into a phase of easing monetary conditions because inflation is falling and the world economy is slowing down". Finally, Latvia's Kazaks remarked "our June projections assumed two more rate cuts this year and right now I don't see any reason why we shouldn't follow through."

RATES: After skipping a rate cut at the July meeting, the Governing Council is set to resume its easing campaign with a 25bps reduction in the deposit rate to 3.5%. The decision to lower rates is in-fitting with the Bank's cautious stance but ultimately one in which headline inflation is moving ever-closer to 2%. Such an outcome is priced at around 97% by markets and backed by all 77 economists surveyed by Reuters. As a reminder, the ECB is set to reduce the Main Refinancing and Deposit Rate spread to 15bps from 50bps (as announced in March); this would see the Main Refinancing Rate cut to 3.65% from 4.25%. ING notes "this narrowing of the spread could be interpreted as an easing of monetary conditions (though the main refinancing operations are hardly used nowadays). While this narrowing of the spread could theoretically be used by ECB hawks, for us it is not a very convincing argument to keep the deposit rate on hold". Looking beyond September, a total of 62bps of easing is seen by year-end, which implies one full 25bps cut and a 50% chance of another. Interestingly, a recent sources piece by Reuters suggested that policy decisions after September are likely to be more complicated as the Eurozone economy enters a more precarious state with some policymakers concerned by a potential recession and others more worried about lingering inflationary pressures. For now, Lagarde will likely reiterate the Bank's "meeting-by-meeting" and "data-dependent" approach.

MACRO PROJECTIONS: For the accompanying macro projections, Goldman Sachs expects headline inflation projections for 2024-2026 to be unchanged as the impacts of "lower oil prices and a stronger Euro are likely to be offset by lower rates and higher gas prices". For core inflation, GS looks for a 10bps upward revision to both the 2024 and 2025 forecasts, taking them to 2.9% and 2.3% respectively (2026 to be left unchanged). From a growth perspective, the bank looks for 2024 and 2025 projections to be lowered by 10bps a piece, taking them to 0.8% and 1.3% respectively.

HICP INFLATION:

2024: 2.5% 2025: 2.2% 2026: 1.9%

HICP CORE INFLATION (EX-ENERGY & FOOD) :

2024: 2.8% 2025: 2.2% 2026: 2.0%

GDP:

2024: 0.9% 2025: 1.4% 2026: 1.6%