ECB Preview: July 2022

Contents

Details:

Monetary policy decision: 13:15BST/14:15CET, Thursday 21 July 2022
Press conference: 13:45BST/14:45CET, Thursday 21 July 2022

Expected links:

Monetary Policy Decisions:
https://www.ecb.europa.eu/press/govcdec/mopo/html/index.en.html

Interest Rate Announcements:
https://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html

ECB Press Conference Video:
https://www.ecb.europa.eu/press/tvservices/webcast/html/webcast_pc_youtube.en.html

Bloomberg: MEDI <Go>

MNI Point of View (POV):

Tightening As Economic Headwinds Build

- The ECB is likely to hike policy rates by 25bp in July as already telegraphed. While there does not appear to be enough momentum behind a larger move for now, it should not be discounted entirely. Indeed, it may prove easier to hike aggressively now, than attempt to do so later in the year should economic activity abruptly deteriorate.
- The ability of the ECB to provide additional guidance on the path for policy rates from September onwards has become more challenging.
- The ECB needs to credibly signal its commitment to rein in inflation at a time when it has fallen far behind its peers in tightening policy. However, pre-committing now to specific policy outcomes at future meetings when there is a growing risk of outright recession, would be a risky play from a credibility perspective.
- We expect the ECB to reiterate that it anticipates a gradual but sustained path for further increases in policy rates, alongside being data dependent, while not providing any further specific rate guidance for now.
- A sufficiently large (likely limitless) and flexible anti-fragmentation tool is expected to be announced at the July meeting. Delaying the announcement would be risky for spreads given the previous market disappointment at the unscheduled mid-June meeting for discussing fragmentation risks.

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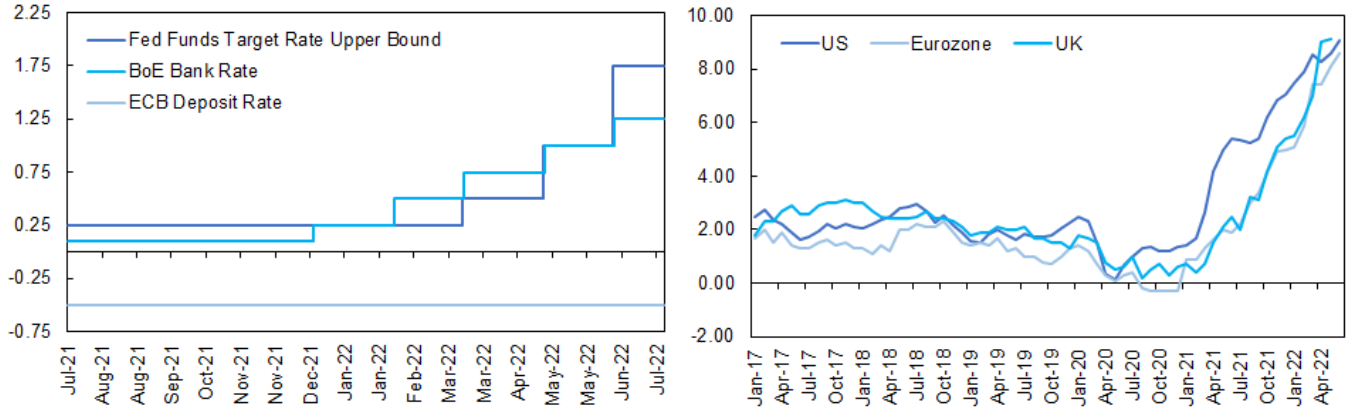
As has now been well telegraphed, the ECB is set to kick off the policy rate tightening cycle this week with an inaugural 25bp hike. Although there does not appear to be sufficient momentum behind a larger move, it should not be discounted entirely given how far the ECB has fallen behind its peers. Moreover, as we highlight below, with the euro area economy at risk of tipping into recession, it could prove easier to frontload rate hikes rather than trying to pursue a path of sustained tightening through end-year and heading into 2023. As such, we see a 25bp lift-off as the base case, with a non-trivial risk of a 50bp move.

Following the July hike, focus shifts to the September decision and the path for rates thereafter. The monetary policy statement from the June meeting indicated: "…the Governing Council expects to raise the key ECB interest rates again in September. The calibration of this rate increase will depend on the updated medium-term inflation outlook. If the medium-term inflation outlook persists or deteriorates, a larger increment will be appropriate at the September meeting." The latest headline inflation data showed a further acceleration to 8.6% Y/Y from 7.5% at the time of the June meeting, while concerns about an intensification of the gas supply crisis has further compounded the medium-term inflation outlook. Absent a marked deterioration in economic activity through the remainder of July and August, the ECB will hike policy rates by at least 50bp. We warn, however, that the ECB is entering choppy waters, which will constrain its ability to provide additional guidance on the specific policy rate path from September onward.

The ECB's reticence to start the hiking cycle sooner means that it has fallen far behind its peers. The Federal Reserve has delivered a cumulative 150bp of hikes this year and the Bank of England 115bp since December, while the ECB's main policy rate still remains in deeply negative territory (and will remain so after July assuming a 25bp hike at this week's meeting) despite inflation moving in tandem with the US and UK towards 10%. The widening differential between the policy rate paths suggests that the ECB has been falling behind the curve, while the carry erosion has driven the euro down towards parity against the dollar, further amplifying imported energy inflation. The Fed's willingness to consider bolder moves (hiking 75bp in June) has only upped the ante further on the ECB.

Fig 1. Central Bank Policy Rates, % (LHS) & Headline Inflation, % (RHS)



Source: MNI, Bloomberg, Central Bank & National Statistical Office Data

However, the ECB is also having to contend with the rising risk of a regional recession in H222/2023. Alongside the impact of the global shift towards policy tightening, the prospect of a further intensification of the gas supply crisis and a potential rationing of gas supplies, could prove the tipping point for the euro area economy. Policymakers could then be facing a situation of leading and coincident indicators turning contractionary while inflation remains considerably and persistently above target. Under this scenario the ECB would need to make a judgement call on whether weaker demand would be sufficient to outweigh the inflationary impulse coming from the supply side.

Given these conflicting challenges, we would be surprised if at this week's meeting the ECB provided the same level of clarity and specificity on the policy rate path after September as it has done for the July and September meetings. The ECB clearly needs to signal a strong and credible commitment to reining in inflation, but would want to avoid pre-committing to specific future policy decisions given the risk of the economic outlook abruptly deteriorating. As such, President Lagarde is likely to reaffirm the wording from the June meeting: "Beyond September, based on its current assessment, the Governing Council anticipates that a gradual but sustained path of further increases in interest rates will be appropriate", while stressing data dependence and highlighting the downside risks to economic growth.

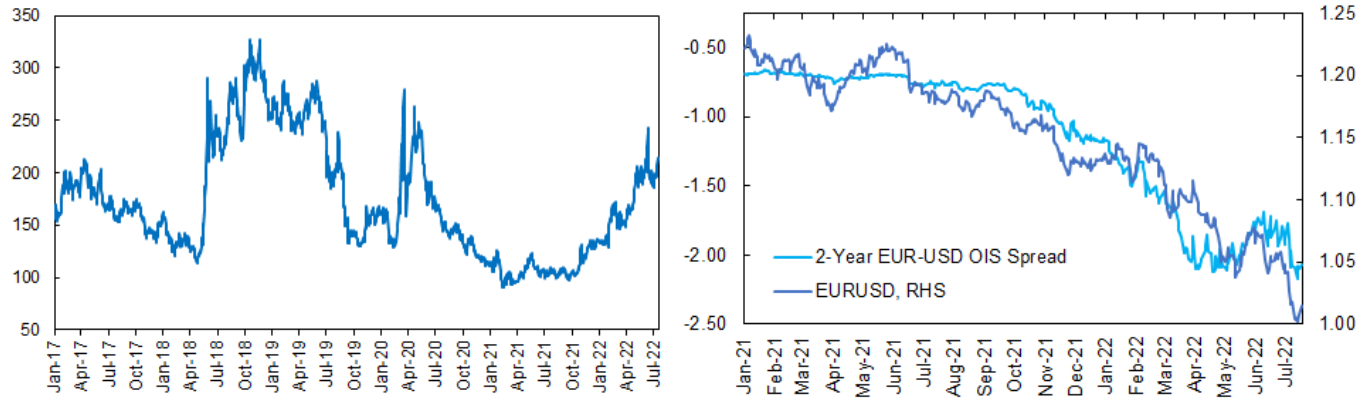
Transmission Protection Mechanism: Big, Vague, Conditional

Beyond the policy rate path, the other big ticket item markets will be looking for at the July meeting is the new anti-fragmentation tool, which is reportedly being called the Transmission Protection Mechanism (TPM). Given the degree to which regional spreads have already widened, and with markets left disappointed by the outcome of the unscheduled meeting in mid-June to discuss fragmentation risks, a failure to unveil the TPM now, or at least provide some indications on its basic parameters, would risk fuelling further spread stress. As such, we expect the ECB to at least provide some details of the TPM.

In order for the tool to be effective, it needs to be credible. To be credible, the tool needs to be large, and possibly limitless. We would concur with the sentiments of François Villeroy de Galhau who stated on July 7 "It is probable that the existence alone of this instrument allowing fast and massive intervention if needed is sufficient, without needing to activate it". Given the inherent difficulty of determining in real-time when spread widening is warranted or unwarranted by fundamentals (an argument made by Joachim Nagel), the ECB is unlikely to be too specific on the factors that would trigger intervention and will instead refer to a range of metrics that are being monitored.

A large programme with somewhat vague determinants for activation (in terms of a specific definition of 'fragmentation' or spread trigger levels) would raise the risk of this tool facing legal action as other policy innovations have in the past. To counter this (perhaps not fully) purchases would need to be sterilised and the programme would need to have conditions attached which force a degree of policy discipline at the national government level, while not being so onerous that it renders the programme unable to respond to emerging threats.

Fig 2. 10-Year BTP-Bund Spread, bp (LHS) & EURUSD vs 2-Year EUR-USD OIS Spread, % (RHS)



Source: MNI, Bloomberg

Baseline Scenario: The ECB delivers a 25bp hike and indicates that it will hike by a larger magnitude in September provided that the inflation outlook has not materially improved. The ECB will proceed to raise policy rates in a gradual manner thereafter, but President Lagarde does not provide any further specificity on the timing the size of future rate moves. Lagarde also stresses that the ECB will act in a data dependent manner and retains full flexibility and optionality to recalibrate the policy setting as required. A new anti-fragmentation tool (TPM) is unveiled, which will be limitless in size, flexible, conditional and with any potential purchases sterilised.

Hawkish Scenario: The ECB hikes by 50bp in July and indicates that the September rate hike need not be limited to 50bp. President Lagarde provides further specific guidance on the policy rate path beyond September, perhaps by indicating that the ECB will move in 25bp increments in the subsequent meetings in the first instance.

Dovish Scenario: The ECB delivers a 25bp hike in July and indicates that a larger move in September would be data dependent and contingent on downside risks to economic growth not materialising. The ECB not only steers clear of providing additional guidance on the policy rate path, but also highlights the mounting risk of a protracted slowdown in economic activity.

Note: We have intentionally excluded different outcomes for the TPM from our hawkish and dovish scenarios. In the event of the TPM overwhelming expectations, periphery EGBs would rally and regional spreads would narrow, but the tool would also provide scope for the ECB to pursue a more aggressive tightening path. The converse would be true if the TPM underwhelmed markets.

mni Central Bank Watch - ECB

18 July 2022

MNI ECB Data Watch List

Inflation		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
HICP	% y/y	8.6	7.5	↑	5.0	↑					1.90
Core Inflation	% y/y	3.7	3.0	↑	2.6	↑					1.18
Oil Prices	$	114.8	107.9	↑	77.8	↑					0.84
5y/5y Inflation Swap	%	2.11	2.21	↓	1.97	↑					0.04
Economic Activity		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Eurozone PMI (Comp)	Index	52.0	54.9	↓	53.3	↓					-0.42
Industrial Production	% y/y	1.6	1.6	→	-1.3	↑					1.05
Business Climate Indicator	Index	1.47	1.68	↓	1.77	↓					-0.94
Consumer Confidence	Index	-23.6	-21.6	↓	-9.3	↓					-1.14
Monetary Analysis		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Narrow Money (M1)	% y/y	7.8	9.1	↓	10.0	↓					-1.65
Broad Money (M3)	% y/y	5.6	6.4	↓	7.3	↓					-1.45
Loans to Non-Fin Corps	% y/y	5.0	3.9	↑	2.4	↑					1.37
Loans to Households	% y/y	4.5	4.4	↑	4.4	↑					1.32
Consumer / Labour Market		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Retail Sales	% y/y	0.2	5.2	↓	8.5	↓					-0.70
Unemployment Rate	%	6.6	6.8	↓	7.1	↓					-1.32
Labour Costs (Quarterly)	% y/y	3.8	-0.1	↑	1.6	↑					1.13
Employment (Quarterly)	% y/y	2.9	2.0	↑	-2.1	↑					1.17
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Equity Market	Index	3522	3903	↓	4298	↓					-0.86
Bund Yield	%	1.22	0.55	↑	-0.18	↑					1.41
10y BTP Spreads	%	216.0	149.1	↑	134.9	↑					-1.15
EUR TWI	Index	117.44	120.17	↓	120.77	↓					-0.28

Source: MNI, Bloomberg

Summary of Analyst Views

- Analysts broadly expect the ECB to hike by 25bp in July as explicitly stated by the ECB. While there is possibility of a 50bp, most analysts do not see sufficient evidence of momentum building behind a larger move.
- Similarly, most analysts expect the ECB to hike by 50bp in September, although there is more disagreement on the rate path thereafter, both in terms of the scale and pace of future tightening.
- Most analysts expect the details of a new anti-fragmentation tool to be announced in July. While there are a range of ideas on specific technical aspects of its design, most analysts agree that the programme needs to be large in scale with relatively light conditions and limited specific detail on spread level targets or definitions of 'unwarranted' tightening, in order for the tool to be effective.

Analyst Views

Barclays

- The ECB will hike by 25bp at the July meeting and will announce the broad guidelines of a new anti-fragmentation tool.
- While the possibility that Russia does not restart exporting gas to Europe via Nord Stream 1 on 21July will not affect the July policy rate decision, it could influence the ECB's September decision.
- Barclays expects the ECB to hike by 50bp in September, but there is a risk of less tightening if gas and electricity rationing becomes the base case.
- The new anti-fragmentation tool will be large, but not unlimited – the ECB will instead indicate limits to total purchases, albeit with a pledge to increase the limit if needed.

- Conditionality will be imposed, such as having a country receive a disbursement from the NGEU and having a budget draft incorporating the recommendation of the EU commission published in May.
- The ECB will not provide any indication of the rates, spreads, or rate of change that would trigger intervention.
- Barclays highlights the difficulty of distinguishing between warranted and unwarranted tightening in light of the unfolding political situation in Italy.

Commerzbank

- The ECB will hike policy rates by 25bp at the July meeting, paving the way for a larger 50bp move in September given that the inflation outlook has not improved.
- Commerzbank expects the ECB to raise the deposit rate to an estimated neutral rate of 1.50% by spring 2023. Furthermore, they suspect that all policy rates will be raised at each of the five meetings following the September meeting.
- The ECB is expected to outline at the July meeting plans for a new anti-fragmentation tool. The programme will likely be designed in such a way that markets do not doubt about its willingness to be used. It is unlikely that the ECB will want to commit itself to precise criteria which would determine when the facility is used and will want to sterilise purchases.

BNP Paribas

- The ECB will stick to the plan agreed on June 9 and hike the policy rate by 25bp at this week's meeting, as well as committing to a 50bp hike in September.
- While a 50bp July hike is not entirely ruled out, there has been limited sign of the GC converging in this direction.
- As long as inflation continues to exceed the ECB's forecasts and the bank's credibility continues to be challenged, there will be pressure for a steeper tightening cycle. As such, BNP Paribas notes that risks to the 50bp September hike are skewed to the upside.
- However, rather than having a 75bp September hike as a base case, BNP believes that 50bp back-to-back hikes in September and October are more likely.
- The ECB is expected to introduce a new anti-fragmentation tool and probably at the July meeting.
- Given the concerns raised by Bundesbank chief Joachim Nagel concerning the ability to determine in real-time whether spread widening is fundamentally justified or unwarranted, the ECB is likely to indicate that the new tool is ready to launch while deploying some constructive ambiguity on the conditions for launch.
- The need to be vague means that the new tool risks disappointing the market. Nonetheless, the ECB is expected to ultimately succeed in limiting spread widening.
- While the initial focus will be on government bonds, BNP believes that purchasing corporate bonds should be allowed to reduce fragmentation risks given that corporate debt is an important part of the transmission chain.
- The launch of a new anti-fragmentation tool would open the door for an end to APP reinvestments.

Danske

- The ECB will go ahead as planned and deliver the first 25bp policy rate hike in July.
- While some hawks have floated the idea of a 50bp move in July, there does not appear to be consensus for this.
- Additional guidance on the Q4 monetary policy outlook is not expected at this week's meeting.
- A 50bp hike in September is the base case and beyond that a sequence of gradual hikes through to Q123 will follow.
- A new anti-fragmentation tool will work primarily through a confidence channel, with the ECB expected to draw inspiration from previous bond buying programmes. Specifically:
    - There are likely to be 'loose conditions' attached to the programme which could be similar to those required to access NGEU funding.
    - There will be a vague definition of what constitutes fragmentation which would allow the ECB to implement the tool flexibly.
    - Purchases would be sterilised.
    - Focus will be on shorter-dated maturities and possibly an implicit intra-euro area spread target.
    - No predetermined capital key guidance.

- Unlimited in volume and size.

Goldman Sachs

- Despite recent euro weakness and central bank actions abroad raising the possibility of a 50bp hike in July, GS expects the ECB to stick to its planned 25bp hike. They note that the growth outlook has deteriorated and the ECB has not historically hiked rates that were less than 70% discounted.
- The ECB is expected to announce details of the new sovereign backstop, which is likely to be unlimited in size with associated macro conditionalities and sterilisation of purchases.
- There are several options for macro conditionality which could see the backstop connected to:
  - **EU-wide fiscal rules**. However, the Stability and Growth Pact is currently suspended.
  - **The ESM**. This would require countries to apply for a tailor-made programme. Although this would entail looser conditionality than the OMT, political impediments may prevent timely activation of the backstop.
  - **The Recovery Fund**. This would allow the ECB to purchase bonds from countries that are fulfilling conditions of the NGEU.
- GS believes that connecting the new anti-fragmentation tool to the NGEU and fiscal rules is most likely.
- In terms of deciding when purchases are to be activated and which indicator(s) to follow, a dashboard approach similar to that used for PEPP is likely, rather than focusing on a single indicator.
- GS expects a 50bp hike in September, followed by a 50bp hike in October and 25bp hike in December.
- The possibility of a complete stop to Russian gas flows skews the risks to the downside for the tightening pace.

HSBC

- The ECB is expected to raise policy rates by 25bp at the July meeting as planned.
- HSBC also expects the ECB to deliver a 50bp hike in September, but there will be no additional information on the path for rates beyond then.
- HSBC argue that managing government bond spreads is a key precondition for the ECB to raise policy rates and so a new anti-fragmentation tool is expected to be announced in July.
- The new tool is likely to be sizeable (at least EUR500bn), have similar flexibility to PEPP, time limited and with considerable involvement from the GC in terms of when it is to be activiated.
- Few details are likely to emerge with respect to what would trigger activation and what conditionalities would be attached.

ING

- A 25bp hike at the July meeting, followed by a 25bp or greater hike in September, is a 'no brainer' given the ECB's previous communication.
- There is a small chance that the ECB decides instead to hike by 50bp in July. The possibility of the ECB staring down a recession come September, coupled with the recent euro weakness, suggests that the hawks on the GC may try to frontload rate hikes.
- The ECB is expected to provide some guidelines on the new anti-fragmentation tool such as linking conditionality to NGEU reform programmes, vaguely defining what constitutes fragmentation and indicating that purchases would be sterilised.
- The hawks could even trade off frontloading rates against looser conditions on an anti-fragmentation tool.

J.P. Morgan

- The ECB will kick-off the tightening cycle this week, likely with a 25bp move, followed by a 50bp hike in September.
- Deviation from the planned 25bp hike this week are possible, but the ECB perceives a cost to this with even hawkish policymakers pointing to a 25bp hike.
- While a new anti-fragmentation tool will be considered, this will not necessarily be launched this week. Even if were announced, it would not be activated. Nonetheless, the ECB will signal a strong and credible commitment to tackling unwarranted fragmentation.

- A failure to launch the tool could lead to some market pressure, but JPM are not concerned by this as long as there is strong commitment to tackle unwarranted fragmentation.
- It is possible that President Lagarde will state that a new tool has been designed, that it can be launched at any time and that it would be effective. Lagarde could also hint at the size being "large enough", conditionality being "effective but not onerous" and that purchases would be sterilised via fixed-term deposits rather than asset sales.
- Specific details on trigger points for intervention are unlikely to be revealed.
- JPM also highlight that the tool's reported name ("Transmission Protection Mechanism") does not contain the word "pandemic" which suggests it could be more permanent in nature. However, linking the tool to the vulnerabilities created by the pandemic would make it easier to justify the tool from a legal perspective.

Lloyds

- The ECB is expected to raise all policy rates by 25bp in July, followed by a further hike in September – possibly in excess of 50bp.

NatWest

- As per the pre-set path, the ECB will hike by 25bp in July and 50bp in September.
- The new anti-fragmentation tool may or may not be announced at the July meeting. NatWest expects the new tool to be similar to the OMT albeit with lighter conditionality and greater flexibility.

Nomura

- The ECB will hike policy rates by 25bp in July, as explicitly intended.
- Thereafter Nomura expects a 50bp hike in September and then 25bp hikes at each meeting until the end of Q123 for a total of 175bp.
- By the end of Q123 the ECB will pause the tightening cycle, leading to modest easing in mid-2023. This is underpinned by Nomura's belief that policy rates will, at that point, lie in the 'neutral' range indicated by GC members, and that the economy will be entering a persistent recession lasting into the coming year.
- Nomura indicates that the most important risk to their rate forecast is that the ECB emulates the Fed by raising rates more aggressively in the short term, but then having to end the normalisation earlier than currently expected.
- A new anti-fragmentation tool is expected to be ready by the July meeting and, even if it is not, the ECB will give clues as to how the tool will operate.
- The ECB is unlikely to provide any specific information about the spread levels that could trigger intervention.
- For the tool to work, it would need to be sufficiently large and probably limitless. Conditionality is likely to be more limited than the OMT. Purchases would be sterilised, which could involve selling bonds of core countries or issuing debt.

RBC

- The ECB will hike by 25bp in July, with markets focused on how much guidance the ECB will give for September.
- RBC expects a 50bp hike in September and October, followed by 25bp increments towards 1.50% for the deposit rate.
- The ECB will either terminate straight away or pre-announce the termination of the tiering system for September as policy rates move back into positive territory.
- With respect to a new anti-fragmentation tool, RBC argue that the ECB would not want to be too specific on the aims of the programme beyond acting against fragmentation risks, lighter conditionality would have more of an impact on spreads, and purchases would likely be open ended. Furthermore, the ECB could sell some of the existing holdings in order to help struggling markets, or use absorbing tenders to sterilise any reserve creation.

Scotiabank

- The ECB is likely to stick to its plan to hike all policy rates by 25bp in July.
- Scotiabank argues that since such a move will be inconsequential for taming inflation, focus will be on the forward guidance around subsequent policy rate moves.

SEB

- The ECB will kick off the tightening cycle with a 25bp policy rate hike in July and a 50bp increase in September. There are minor risks of a 50bp hike in July.
- Specific signals concerning the size of the September hike are unlikely at this week's meeting with the focus instead being on the GC's risk assessments.
- The GC will stress concerns about inflation while also acknowledging headwinds to economic activity.
- SEB maintains their current policy call: a 25bp hike in July, 50bp in September and 25bp in October and December. A further two 25bp rate increases are expected in H123.
- The ECB is expected to define the parameters of the new anti-fragmentation tool quite vaguely by indicating a willingness to purchase as much as necessary in order to maintain monetary policy transmission across the euro area. Purchases will be fully sterilised so that the ECB can argue that it is not continuing QE.

Swedbank

- Although Swedbank maintains its call for the ECB to hike by 25bp at the July meeting, they stress that after a 'few more hikes' inflation will recede and the tightening cycle will end.
- The ECB is expected to unveil some details of the new anti-fragmentation tool this week, but warn that the instrument is likely to face legal, political and technical hurdles.

TD Securities

- The ECB will hike all three policy rates by 25bp at the July meeting.
- TD sees little chance of the ECB deviating from this plan with a 50bp hike and expect little change to the messaging around the planned September hike.
- After a 50bp hike in September, the ECB is expected to hike by 50bp again in October followed by additional hikes in 25bp increments until the deposit rate reaches a terminal/neutral rate of 1.50% in March 2023.
- TD believes that the ECB will not raise policy rates without having the new anti-fragmentation tool in place. As such, they expect the ECB to announce details of the new tool at the July meeting. The larger the tool, the more credible it will be and the least likely it will need to be used.

UBS

- The ECB will hike all three policy rates by 25bp as planned.
- The ECB will also present the key features of its new anti-fragmentation tool with implementation following at a later stage depending on market conditions.
- UBS looks for the following characteristics in the new tool:
    - Country-focused
    - Open-ended
    - Ad-hoc and without quantitative limits
    - Sterilised
    - Limited conditionality
    - Subject to risk-sharing
    - Potentially open to private sector securities
    - Designed to provide the ECB with sufficient flexibility and discretion.
- UBS expects the ECB to hike the deposit rate by a cumulative 125bp in 2022 (25bp in July, 50bp in September and 25bp in October and December).
- A further four 25bp hikes are expected in March, June, September and December 2023. This would take the terminal rate to 175bp.

- In the event of limited gas rationing the ECB would be expected to stop hiking rates after October and in a severe rationing scenario the ECB would stop after the September meeting.

UniCredit

- The ECB will hike policy rates by 25bp at the July meeting. The probability of a bolder move is low.
- Focus will be on the new anti-fragmentation tool. UniCredit expects the following parameters for the new tool:
    - Potentially unlimited purchases
    - Light conditionality
    - Short-end focus; probably up to 3-years.
    - Full sterilisation of purchases
- The conditionality component will be a thorny issue, but will also be important if the ECB wants to retain maximum flexibility with respect to the timing and size of any interventions.
- Given that requests for ESM support risk being politically toxic, UniCredit expects conditionality to be tied to reforms under NGEU and fulfilment of fiscal objectives under the Stability and Growth Pact.
- In terms of sterilising purchases, the ECB could use a similar strategy to the Security Market Programme whereby interest-bearing deposits are offered to banks to the same value as the government bonds purchased.
- UniCredit believes that the risks are skewed towards the ECB underdelivering, with two main sources of potential disappointment:
    - A split within the GC could result in a delay to the new anti-fragmentation tool being announced.
    - Hawks on the GC could insist on conditionality that goes beyond existing commitments. This would put the ECB in crisis-reaction mode rather than crisis-prevention mode.

ECB Communication: The Detail

The summer months typically mark a quiet spell for policy communication, which this time around has been further compounded by the ECB's well telegraphed plan for raising rates in July and September. However, there have been some notable developments, particularly with respect to indications around the potential cumulative increase in policy rates in the coming quarters and the parameters around a new anti-fragmentation tool.

Economic Outlook

The economic outlook has further deteriorated since the last GC meeting as reflected in the evolution of ECB commentary over this period. Speaking on June 20, President Lagarde highlighted the impact of higher energy costs on economic activity, while also striking a relatively optimistic note:

> "Euro area activity is being dampened by high energy costs, intensified supply disruptions and greater uncertainty, which affect the manufacturing sector in particular.
>
> At the same time, activity in the services sector is supporting growth and the recovery in this sector is expected to strengthen over the coming months. The lifting of pandemic-related restrictions and good prospects for the tourist season are driving stronger activity, particularly in contact-intensive services. Moreover, a strong labour market, with more people in jobs, will continue to support incomes and consumption.
>
> The headwinds from high energy costs, the deterioration in the terms of trade, greater uncertainty and the adverse impact of high inflation on disposable income are expected to gradually fade."

And further on June 28

> "We have markedly revised down our forecasts for growth in the next two years. But we are still expecting positive growth rates due to the domestic buffers against the loss of growth momentum"

Fabio Panetta, however, struck a more downbeat note on July 1:

> "This surge in prices does not reflect excess demand in the euro area. Consumption and investment remain below their pre-pandemic level and even further away from their pre-pandemic trend. With wages rising at a moderate pace, real incomes have been severely hit by the surge in import prices. Together with the war, this is further depressing consumption and confidence, despite the boost they have received from the reopening after the pandemic. Leading indicators of consumer confidence and business sentiment are deteriorating, and the growth outlook is being progressively revised downwards. Our projections now foresee activity remaining below its pre-pandemic trend throughout our projection horizon."

While Luis de Guindos stated on July 4:

> "Our projections foresee growth above 2% throughout the projection horizon. But the war and the risk of further disruption in the energy supply to the euro area continues to be a significant downside risk to growth. In fact, the downside scenario in our June projections reflects this risk and implies a contraction of activity in 2023, following weaker but positive growth in 2022."

Yannis Stournaras highlighted stagflation risks on July 10 and did not entirely quell the possibility of recession:

> "There are stagflationary winds blowing - there's no question about that"
>
> "But for the moment we don't expect negative growth this year or next year."

Madis Müller, meanwhile, downplayed the likelihood of stagflation on July 4:

> "For the euro-area economy, stagflation isn't the most likely scenario"
>
> "The outlook of growth has weakened in recent months, but we can still expect some positive economic growth in the euro area for the coming years, with questions around gas supply a significant risk."

Inflation

Speaking in Sintra on June 28, President Lagarde summarised the current state of play with respect to inflation:

> "Inflation in the euro area is undesirably high and it is projected to stay that way for some time to come. This is a great challenge for our monetary policy.
>
> We are not facing a straightforward situation of generalised excess demand or economic overheating, in which case the trajectory of medium-term inflation would have been clearer. Despite the bounceback in services, private consumption in the euro area is still more than 2% below its pre-pandemic level. And investment remains subdued.
>
> Although there have been some signs of above-target revisions in recent months, longer-term inflation expectations currently stand at around 2% across a range of measures. This supports our baseline projection for inflation to converge back towards our medium-term inflation target.
>
> At the same time, inflation pressures are intensifying and broadening through the domestic economy. Almost four-fifths of items in the consumption basket had annual price increases above 2% in April, and this is not only a reflection of high import prices. A new ECB indicator of domestic inflation – which removes items with a high import content – currently stands above 3%.

> In this environment, it is important to understand how persistent domestic price pressures are likely to become. There are several factors worth considering here.
>
> First, inflation is starting to take root in the services sector, which is the "stickiest" component of inflation and has a higher weight than goods.
>
> Second, unemployment in the euro area is at a record low, labour shortages are broad-based across sectors and indicators of labour demand remain strong. This tightening of the labour market, together with the catch-up effect triggered by the high inflation environment, suggests that wage growth will pick up We are also seeing signs that the supply shocks hitting the economy could linger for longer. While it is reasonable to assume that global supply chain disruptions will gradually be resolved, the outlook for energy and commodities remains clouded."

And went on to stress on June 29 that there has been a paradigm shift for inflation:

> "I don't think we are going to go back to that environment" that kept prices low over the past two decades, said Christine Lagarde, the president of the bank. That period of low inflation, predicated on increasing globalization, has now changed, though the extent of that is still being debated, she added. Meanwhile, inflation expectations, which policymakers watch carefully to see if elevated prices become uncontrollable, are rising for the region."
>
> "There are forces that have been unleashed as a result of the pandemic, as a result of this massive geopolitical shock that we are facing now, that are going to change the picture and the landscape within which we operate."

Luis de Guindos added on July 4:

> "Elevated inflation will remain with us for some time, declining to just above target only at the end of our projection horizon. We expect that moderating energy costs, the easing of supply disruptions related to the pandemic and the normalisation of monetary policy will be conducive to inflation returning to our 2% target over the medium term. But the risks surrounding inflation are on the upside."

Gediminas Simkus offered a stark assessment of the near-term trajectory for inflation on June 13

> "The key risk is inflation"
>
> "The balance of risks for inflation is to the upside. Inflation continues growing, it's pace keeps surprising again and again, it will surprise again next month."

Isabel Schnabel indicated in a presentation on July 2 Jul 2

> "No signs yet of a wage-price spiral, but risks are increasing"
>
> "Projections are pointing to a decline in inflation," but there's a "history of projection errors"
>
> "Monetary policy has dampened inflation expectations, but remaining risk of de-anchoring"

Peter Kažimír warned on June 13

> "Inflation in the euro area, even at home, is much, much higher than we would like, and will remain high for some time to come"

While Mārtiņš Kazāks stated simply on June 10:

> "Inflation is extremely high and it is unacceptably high"

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And on July 4

> "Inflation is very broad. We see that inflation is picking up. And the risks of further second round effects are increasing"

Policy Normalisation

On the need for policy normalisation, Olli Rehn state on June 21:

> "With inflation rising sharply, there has been good reason to expedite the normalization of monetary policy"

Mário José Gomes de Freitas Centeno stressed on June 20 that policy normalisation:

> "..will be done gradually, both at the level of interest rates and at the level of the purchase programs"

Fabio Panetta similarly stressed the need for gradualism on July 1

> "Given the prevailing uncertainty, normalisation should remain gradual. For now, our aim should be to avoid high near-term imported inflation becoming entrenched by feeding into higher inflation expectations. And this is why we are ending the policies that sought to fend off deflationary dynamics, such as net asset purchases and negative rates. But beyond this, further adjustments to our monetary policy stance will depend on the evolution of the outlook for inflation and the economy."
>
> "At this stage, inflation expectations stand at around 2% and wage increases remain moderate. We are closely monitoring these developments. And we need to see how the economy reacts to the tightening in financing conditions and the deterioration of the global and domestic economic outlook."

President Lagarde meanwhile indicated on June 28 a willingness to tighten more aggressively if needed:

> "If the inflation outlook does not improve, we will have sufficient information to move faster. This commitment is, however, data dependent"

Policy Rate Path

Although the ECB has laid out a clear baseline path for policy rate adjustments at upcoming meetings, some within the GC continue to dissent. The more hawkish GC members are still pushing the envelope in terms of ever larger and more frequent policy rate hikes, despite having managed to get a 50bp hike pencilled in for September. At the dovish end of the spectrum, some GC members who have accepted the need to normalise policy have nonetheless warned of the risk of overtightening in the face of a deteriorating economic outlook

Madis Müller confirmed on July 4 the previously agreed policy path:

> "Given the inflation outlook, it's appropriate to start raising interest rates in July"
>
> "We should continue with a further hike of 50 basis points in September."

Boštjan Vasle affirmed the post-September direction for rates on July 4

> "The dynamic of raising interest rates is expected to continue after September, in the fourth quarter and the beginning of next year"

President Lagarde stressed on June 28 that the ECB could move faster if needed:

> " If the inflation outlook does not improve, we will have sufficient Iinformation to move faster. This commitment is, however, data dependent."

Peter Kažimír stressed on June 13 the urgency to hike rates:

> "I can clearly see the need to accelerate the pace and deliver an increase of 0.5 percentage point"
>
> "The incoming data only confirm to me that there's no reason to hesitate."
>
> "It's more sensible to act preventively now than then to be sorry afterward if we were hesitating"

Joachim Nagel similarly argued on June 23 for an urgent response:

> "Central banks must not respond with too little, too late"
>
> "If monetary policy falls behind the curve, even stronger hikes in interest rates could become necessary to get inflation under control. This would create much higher economic costs."

Adding on June 27

> "History has shown that inflation expectations can become unanchored if central banks are too slow to tackle inflation, and we must do things better this time round"
>
> "Longer-term inflation expectations are still close to our target of 2%. We need to make sure that things stay this way"

Mārtiņš Kazāks indicated his willingness on June 28 to consider a larger than (25bp) planned hike in July:

> "If we see that the situation has worsened, that inflation is high and we see negative news in terms of inflation expectations, then in my view front-loading the increase would be a reasonable choice"

Although he had previously warned markets on June 20 about getting too far ahead:

> "..the market should not be carried away with the speed of re-pricing and jumping to much higher interest rate levels."

Gediminas Simkus also hinted on June 29 at the potential for a larger hike in July:

> "But if we see this change in data that points to the persistence of inflation, to its acceleration, 50 basis points should be a policy option for July."

Not to be outdone, Robert Holzmann argued on July 7

> "When the situation doesn't improve, a 0.75 percentage point increase may eventually become necessary"
>
> "The time has now come for clear rate steps, otherwise inflation will solidify."

Klaas Knot indicated on June 18 that successive 50bp hikes were possible:

> "If it continues to rise then we will continue to intensify, and there will be multiple interest rate hikes of 50 basis points."

And that the policy rate could get to 2%:

> "It will take a while to get the first two percentage points … I don't expect we'll be there before the beginning of 2023."

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Moreover, he previously indicated on June 14 that a larger than 50bp hike in September was possible:

> "If conditions stay the same as they are today, we should increase the rate by more than 0.25 percentage points. The following level is to go up again by 0.50 points, but our options are not necessarily limited to that"

Knot also suggested on July 7 that policy rates could be hiked even with economic growth slowing:

> "It may well be that while the economy is slowing in the coming months and quarters, we will increase interest rates"
>
> "In an ideal world, you'd want to stimulate the economy but bring inflation down at the same time"
>
> "Unfortunately that's not what we can do, we have to make a choice; in that case our mandate is very clear - we have to choose bringing inflation down."

Pierre Wunsch also explicitly stated a level for the policy rate on June 15:

> "My personal opinion is that the next 150-200 basis points hikes are no-brainers because then we would still be with negative real rates in the short term"
>
> "It's only when you go beyond that you really start being less expansionary in real terms."
>
> "The fact that we have more or less committed -- unless the situation improves -- to a more than 25 basis-point hike means that our understanding of gradualism doesn't exclude increases of that magnitude"

He also warned on June 29 that government efforts to soften the blow of higher energy costs could ultimately lead to further policy rate hikes:

> "If fiscal policy remains supportive, then we have to do more,"
>
> "The end game is higher deficits and higher interest rates, and therefore also a higher risk of fragmentation."

Finally, at the more dovish end, Luis de Guindos pushed back against a larger July hike, stating on June 24:

> "The communication is firm"

While Gaston Reinesch warned of the risk of recession if the ECB tightens

> "too much too fast"

Exchange Rate

While the ECB has repeatedly stressed that it does not target the exchange rate, the sharp depreciation towards parity against the US dollar has clearly been a concern, particularly given that a large proportion of euro area inflation has been imported.

François Villeroy de Galhau suggested on July 13 that the depreciation was:

> "…good news for activity as it supports exporters but unfortunately it raises inflation a bit"

And that:

> "The exchange rate isn't something we set but we follow it because it counts for inflation."

While President Lagarde stated on June 20 that the ECB needs to respond to the potential spillovers from a weaker exchange rate:

> "What is important is that with our monetary policy, we have to respond to the situation and make sure that we address these spillovers that we will be observing and that we should counteract in this particular market."

A New Anti-Fragmentation Tool

Fabio Panetta warned on July 1 that a failure to contain fragmentation risks would mean:

> "Monetary policy could otherwise be impaired by an excessive, self-fulfilling market reaction leading to an asymmetric tightening of financing conditions across the euro area."

And that:

> "Action to prevent fragmentation is therefore not at odds with the normalisation of monetary policy. On the contrary, it is a necessary condition for us to have the freedom to adjust our stance as needed to bring inflation back to 2%."

Luis de Guindos stressed on July 4:

> "Let me stress that, ever since the gradual process of policy normalisation was initiated in December 2021, the Governing Council has pledged to act against potential fragmentation risks."

And in addition to the commitment to flexible reinvesting PEPP redemptions:

> "We also tasked the Eurosystem committees, together with ECB staff, with accelerating the completion of a new anti-fragmentation instrument for consideration by the Governing Council. Fiscal policy should do its part by guaranteeing sound public finances in the medium term and delivering targeted and temporary support to vulnerable groups in the short run."

Lagarde stated on June 20:

> "Suffice to say that fragmentation will be addressed if the risk of it arises"
>
> "And it will be done so with the appropriate instruments, with the adequate flexibility, it will be effective, it will be proportionate, it will be within our mandate. And anybody who doubts that determination will be making a big mistake."

Isabel Schnabel highlighted on June 14:

> "These tools might again look different, with different conditions, duration and safeguards to remain firmly within our mandate"

Pablo Hernández de Cos stated on June 24

> 'We gave a very clear message about the commitment of the ECB's Governing Council to fight against financial fragmentation"
>
> "We are in the phase of defining the proposal. I won't go into the details. There are many things that need to be defined for this instrument"

Gediminas Simkus June 27 also indicated that the ECB is:

> "accelerating creation of the instrument to make sure monetary policy can achieve its target should fragmentation become an obstacle"

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While Mario Centeno hinted on June 24 that an announcement is drawing near:

> "We expect to have something to tell you, to tell the markets in the coming weeks."
>
> "We understand we need to react promptly in anticipation of materialization of risks"

Centeno suggested on June 20 that a well-designed tool may never need to be used:

> "There will be a new insurance that will only be used in case of need, and if it is well designed it will probably never be used. Its objective is not to act, its objective is to prevent a set of behaviors."

A possibility similarly highlighted by Yannis Stournaras on July 10:

> "I believe that there is a lot of truth in the idea that if we convince markets that this is going to be a strong tool, we might not need it"
>
> "We'll have it on the shelf. This is the good scenario."

And by François Villeroy de Galhau on July 7

> "It is probable that the existence alone of this instrument allowing fast and massive intervention if needed is sufficient, without needing to activate it".
>
> "It's an instrument, the very credibility of which is assured by the fact that it marks our limitless commitment to the euro. It will be a powerful instrument, but used only when necessary and in certain conditions"

Adding:

> "Work is advancing well, as fast as possible"

Centeno stressed on June 24:

> "There's no objective regarding specific spread values. The intensification of these fragmentation situations don't come down to one indicator."

While appearing to accept the need for a new anti-fragmentation tool, Pierre Wunsch struck a note of caution on June 15:

> "Most of us -- probably all of us, actually -- are very open to doing something if it's clear enough that there's a problem of markets overreacting or unwarranted fragmentation,"
>
> "But we should be careful not to give too much of an impression to authorities that we will immediately jump to their help in whichever uncomfortable situation they might find themselves"
>
> "In addition, if you are too specific about a new instrument, there's a concern that you're going to lose flexibility. So, we should not over-engineer before knowing what the circumstances are."

Adding on June 28

> "Flexibility means we do not want to impose conditions that would prevent us to act when there is a case to act"
>
> "I don't think there should be any automatic triggers based on the spreads because the spreads are related to the credibility of fiscal policy"

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And, finally, on July 7:

> "If the fragmentation in bond markets is unwarranted then we should be as unlimited as possible"
>
> "The case to act is strong when faced with unwarranted fragmentation."
>
> "The difficulty will be about the grey zone in between what is warranted and what is not and that is the area of moral hazard we have to navigate,"
>
> "We need countries to make an effort and come up with a credible fiscal plan"

Joachim Nagel echoed these sentiments by arguing on July 4:

> "..it would be fatal if governments were to assume that the eurosystem will ultimately be ready to assure favourable financing terms for the member states"

And warned against:

> "…using monetary policy instruments to limit risk premia, as it is virtually impossible to establish for sure whether or not a widened spread is fundamentally justified".

Which could otherwise result in policymakers finding themselves in:

> "dire straits"

He concluded with:

> "it is clear that unusual monetary policy measures to combat fragmentation can be justified only in exceptional circumstances and under narrowly defined conditions".

ECB Inter-Meeting Communication

Date	Time	Speaker	Event
10/06/2022	06:40	François Villeroy de Galhau	Discussion on BFM Business TV
10/06/2022	09:00	Robert Holzmann	Presentation of economic forecasts at a press conference organised by the Austrian National Bank.
10/06/2022	16:00	Joachim Nagel	Presentation "How Does Monetary Policy Work in the Euro System?"
11/06/2022		Frank Elderson	Keynote speech "Supervising banks' governance: structure, behaviour and culture" at the Florence School of Banking and Finance's Bank Board Academy "Sitting on Bank boards: Suitability and better governance" https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220611~01ae4a6b1c.en.html
13/06/2022	09:00	Robert Holzmann	Speech at the IMF Austria IV-Consultation in Vienna
13/06/2022	09:00	Gediminas Šimkus	Speech in Vilnius, Lithuania
14/06/2022	18:20	Isabel Schnabel	Commencement speech "United in diversity – Challenges for monetary policy in a currency union" to the graduates of the

			Master Program in Money, Banking, Finance and Insurance of the Panthéon-Sorbonne University https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220614~67eda62c44.en.html
15/06/2022	09:00	Robert Holzmann	Speech to coincide with the publication of the Austrian National Bank's Financial Stability Report
15/06/2022	09:00	Robert Holzmann	Speech to coincide with the publication of the Austrian National Bank's Financial Stability Report
15/06/2022	11:00	Madis Müller	Speech at the Estonian Chamber of Commerce
15/06/2022	12:00	Mário Centeno	Presentation of the Bank of Portugal's June Economic Bulletin
15/06/2022	13:30	Pablo Hernández de Cos	Speech
15/06/2022	14:00	Fabio Panetta	Introductory statement "The digital euro and the evolution of the financial system" at the Committee on Economic and Monetary Affairs of the European Parliament https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220615~0b859eb8bc.en.html
15/06/2022	14:15	Klaas Knot	Speech at the Young Factor web event
15/06/2022	15:15	Mário Centeno	Speech at the Young Factor web event
15/06/2022	17:20	Christine Lagarde	Discussion with José Viñals hosted by Baroness Minouche Shafik, London School of Economics, in London
16/06/2022	08:00	Ignazio Visco	Speech at the Young Factor web event
16/06/2022	08:45	François Villeroy de Galhau	Speech at the Young Factor web event
16/06/2022	08:50	Fabio Panetta	Keynote speech "Bringing European payments to the next stage: a public-private endeavour" at the European Payments Council's 20th anniversary conference https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220616~9f8d1e277b.en.html
16/06/2022	09:30	Luis de Guindos	Speech at the Young Factor web event
16/06/2022	10:30	Klaas Knot	Speech at the Young Factor web event
16/06/2022	10:30	Mário Centeno	Speech at the Young Factor web event
16/06/2022	10:30	Fabio Panetta	Speech at the Young Factor web event
16/06/2022	10:30	Fabio Panetta	Speech
16/06/2022	13:20	Gabriel Makhlouf	ECB Governing Council Member Gabriel Makhlouf speaks at Insurance Ireland launch
16/06/2022		Luis de Guindos	Interview with Ta Nea conducted by Maria Vasileiou https://www.ecb.europa.eu/press/inter/date/2022/html/ecb.in220616~a25cc9df1e.en.html
16/06/2022		Isabel Schnabel	Interview conducted by Dein Spiegel on 19 May 2022 https://www.ecb.europa.eu/press/inter/date/2022/html/ecb.in220616_1~84c741b1fb.en.html
17/06/2022	08:00	Gediminas Šimkus	Presentation of economic forecasts for Lithuania.
18/06/2022	21:40	Olli Rehn	Participation in a Federal Reserve Bank of Dallas policy panel concerning monetary policy in the US and euro area
20/06/2022	08:00	Madis Müller	Speech at Bank of Estonia event
20/06/2022	08:30	Ignazio Visco	Speech

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20/06/2022	09:15	Mário Centeno	Speech at the CNN Portugal Summit.
20/06/2022	13:45	Mārtiņš Kazāks	Participation in a panel discussion on investment, held in Riga.
20/06/2022	14:00	Christine Lagarde	Speech "Hearing of the Committee on Economic and Monetary Affairs of the European Parliament" at the Hearing of the Committee on Economic and Monetary Affairs of the European Parliament https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220620~b91bded4f1.en.html
20/06/2022	15:00	Mário Centeno	Speech at a conference marking 10 years of the Portuguese Public Finance Council.
20/06/2022	16:00	Christine Lagarde	Introductory statement before the Committee on Economic and Monetary Affairs of the European Parliament.
20/06/2022	20:30	Philip R. Lane	Presentation "Inflation and monetary policy in the euro area" at the Society of Professional Economists Annual Dinner https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220620_1~2f075cc2f5.en.pdf?429f9195875c0061d1d51ffb74922fb8
21/06/2022	09:00	Olli Rehn	Presentation of forecasts on the Finnish economy.
21/06/2022	09:00	Peter Kažimír	Presentation of forecasts on the Slovak economy.
22/06/2022		Frank Elderson	Keynote speech "Good, bad and hopeful news: the latest on the supervision of climate risks" at the 10th Annual Conference on Bank Steering & Bank Management at the Frankfurt School of Finance & Management https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220622~860a2aef6b.en.html
23/06/2022	09:00		ECB Publishes Economic Bulletin
23/06/2022	15:30	Joachim Nagel & François Villeroy de Galhau	Participation in Bundesbank event
23/06/2022	19:00	François Villeroy de Galhau	Participation in Banque Postale conference in Paris
24/06/2022	10:30	Mário Centeno	Presentation of the Bank of Portugal's financial stability report
24/06/2022	11:30	Fabio Panetta	Participation in event organized by the Association of Financial Journalists
24/06/2022	12:30	Luis de Guindos	Participation in panel discussion at UBS expert talk "Central Banks and Inflation" in Zurich
24/06/2022	15:15	Mário Centeno	Speech at the AFME/OMFIF's 2nd Annual European Financial Integration Conference https://www.afme.eu/events/detail?eventid=496ebaa0-64cc-ec11-a7b6-6045bd110b98 &utm_campaign=efi2022&utm_source=afme&utm_medium=email&dm_i=3TYX,1G3AV,5ECY6S, 5ANVK,1#event-agenda
27/06/2022	18:30	Christine Lagarde	Opening remarks at the ECB Forum on Central Banking 2022 `Challenges for monetary policy in a rapidly changing world' in Sintra, Portugal
27/06/2022			ECB Forum on Central Banking in Sintra

			https://www.ecb.europa.eu/pub/conferences/ecbforum/html/index.en.html
28/06/2022	09:00	Christine Lagarde	Speech "Price stability and policy transmission in the euro area" at the ECB Forum on Central Banking 2022 on "Challenges for monetary policy in a rapidly changing world" in Sintra, Portugal https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220628~754ac25107.en.html
28/06/2022	09:30	Philip R. Lane	Chairing a panel at the ECB Forum on Central Banking 2022 `Challenges for monetary policy in a rapidly changing world' in Sintra, Portugal
28/06/2022	10:30	Frank Elderson	Chairing a panel at the ECB Forum on Central Banking 2022 `Challenges for monetary policy in a rapidly changing world' in Sintra, Portugal
28/06/2022	12:00	Fabio Panetta	Chairing a panel at the ECB Forum on Central Banking 2022 `Challenges for monetary policy in a rapidly changing world' in Sintra, Portugal
29/06/2022	09:00	Luis de Guindos	Chairing a panel at the ECB Forum on Central Banking 2022 `Challenges for monetary policy in a rapidly changing world' in Sintra, Portugal
29/06/2022	11:00	Isabel Schnabel	Chairing a panel at the ECB Forum on Central Banking 2022 `Challenges for monetary policy in a rapidly changing world' in Sintra, Portugal
29/06/2022	14:00	Christine Lagarde	Speech in Sintra
29/06/2022	16:00	Christine Lagarde	Participation in a panel at the ECB Forum on Central Banking 2022 `Challenges for monetary policy in a rapidly changing world' in Sintra, Portugal
01/07/2022	11:30	Fabio Panetta	Keynote speech "Europe as a common shield: protecting the euro area economy from global shocks" at the European Parliament's Innovation Day "The EU in the world created by the Ukraine war" https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220701~254252d76e.en.html
01/07/2022	18:00	Fabio Panetta	Speech at a graduation ceremony at the Center for Monetary and Financial Studies (CEMFI) in Madrid.
02/07/2022		Isabel Schnabel	Presentation " Inflation in the euro area - past and future" at Petersberger Sommerdialog https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220702~ea05cea550.en.pdf?39e5da52e4cf028f65dac901fa110a93
04/07/2022	10:00	Boštjan Vasle	Speech at an OECD Event in Slovenia
04/07/2022	15:00	Joachim Nagel	Speech at the Frankfurt Euro Finance Summit organized by dfv Euro Finance Group GmbH
04/07/2022	16:00	Luis de Guindos	Remarks "Challenges for monetary policy" at the Frankfurt Euro Finance Summit https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220704~9f5fc26b43.en.html
06/07/2022	08:50	Olli Rehn	Speech on Finnish Foreign Policy

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07/07/2022	10:45	Philip R. Lane	Participation in a panel on the green transition following the Covid-19 panic at the 2022 Annual Conference of the OECD Global Forum on Productivity
07/07/2022	12:30		ECB Publishes Account of June Policy Meeting
07/07/2022	15:00	Klaas Knot	Speech on Dutch TV
07/07/2022	15:10	Yannis Stournaras & Mário Centeno	Participation in panel discussion on the role central banks can play in boosting economic growth.
08/07/2022	09:00	Ignazio Visco	Speech at an event in Rome
08/07/2022	11:00	Madis Müller	Speech at an event unveiling a new euro coin dedicated to Ukraine
08/07/2022	12:55	Christine Lagarde	Participation in the session `Que risque le monde?' at Les Rencontres Economiques d'Aix-en-Provence 2022 in Aix-en-Provence, France
08/07/2022	17:45	François Villeroy de Galhau	Speech at a conference in Aix-en-Provence, France
09/07/2022	14:30	Isabel Schnabel	Speech at a conference in Aix-en-Provence, France
10/07/2022	10:15	Yannis Stournaras	Speech in France
11/07/2022	14:00	Fabio Panetta	Speech at an event organized by IEFA in Montreal.
11/07/2022	17:30	Joachim Nagel	Speech on the digital euro
12/07/2022	11:15	François Villeroy de Galhau	Speech at a Europlace conference in Paris
15/07/2022	11:00	Olli Rehn	Speech on the economy and inflation at the SuomiAreena 2022 event.

MNI Policy Team

MNI SOURCES: ECB Focussing On Conditions For New Crisis Tool **29-06-2022**

By Jason Webb

Sintra, Portugal (MNI) - European Central Bank officials are likely to consider a range of possible new tools to address any blowout in eurozone spreads at its next meeting on July 21, with debate on committees now preparing the proposals focussing on how to make countries requiring assistance pledge to improve their finances and on how long bond purchases could continue, central bank sources told MNI.

While the ECB has said it will use reinvestments from its Pandemic Emergency Purchase Programme to cap spreads if necessary, officials acknowledged that a new tool with greater firepower could be necessary if the government bonds of a country like Italy were to come under sustained pressure.

But while any such tool would have to come with strict conditions in order to withstand possible scrutiny from Germany's constitutional court, the nature of these will be difficult to agree, with Italy's government in particular bridling at the requirements imposed by the ECB's existing facilities such as Outright Monetary Transactions. (See MNI SOURCES2:ECB Mulls Crisis Tool As Officials Debate Spreads)

Possibilities include conditioning use of the tool to targets agreed by member states to access the European Union's EUR723.8 billion Recovery and Resilience Facility, though that would be complicated by the fact that assessments are carried out only annually. Alternatively, tying it to the Excessive Debt Procedure could also be possible, one Eurosystem source said, adding that he expected up to three proposals from the Committees for tools aimed at preventing fragmentation of monetary policy transmission, even if only one is presented to the Governing Council.

DURATION

The other key conditionality is likely to be duration, the source, adding that approval for a tool may only come if it is time-limited. Agreement could require more than one meeting, the source said.

There is also debate over whether the conditions for the tool should be made public, another source said.

Any tool would only serve as a backstop after all else has failed, the source said, adding that there was significant divergence within the Governing Council regarding the conditions under which such a tool could be deployed, and that any decision on these would be likely to be fudged or put off until later.

Another source agreed that conditionality, likely be linked to a medium-term fiscal sustainability programme, will be crucial in gaining approval for a new tool.

FIREPOWER

Several sources agreed that the PEPP reinvestments, which ECB President Christine Lagarde has said can be flexibly deployed from as soon as Friday to cap spreads, would be the tool of first resort, even though they could be overwhelmed in a crisis.

"PEPP reinvestments don't have much firepower, their effect will therefore be quite limited," one official said. "The new tool - whatever it is, and there is a broad outline - will be the real backstop. With that in place, the monetary policy stance can be much more focused on ensuring price stability."

The new tool will be a "bazooka" which hopefully goes unused, one of the sources said. Although, as is the case with the PEPP, the new tool may not be constrained by the "capital key" capping purchases of individual countries' bonds under the ECB's older Asset Purchase Programme, it would not be practically possible to direct all of the new tool's reinvestment firepower only at debt suffering from market attack.

While the ECB's rate hikes flagged for July and September are not reliant on having a new backstop in place, this could allow a faster pace of rate hikes should that become necessary, a source said, adding that proposals to sterilise bond purchases under the tool were more of a "presentational" issue than something of real market significance.

In the meantime, as the ECB prepares to tighten, there are already signs that the economy is weakening, one of the sources said, adding that inflation could already be close to peaking and that the threat of a U.S. recession was rising.

An ECB spokesperson declined to comment on the matter.

MNI INTERVIEW: ECB's Simkus Says New Tool May Never Be Used **29-06-2022**

By Luke Heighton

(MNI) London - The European Central Bank should raise key interest rates by at least 50 basis points in September and possibly by the same amount in July, Bank of Lithuania Chairman Gediminas Simkus told MNI, adding that he hoped a proposed new tool aimed at capping yield spreads within the eurozone may never be used.

“A 50-basis-point rate rise might also become a policy option in July – but only if supported by incoming and substantially worsened data for inflation,” Gediminas Simkus said at the ECB Forum in Sintra,. “I think 50 basis points should be the baseline for September, assuming we don’t see any downward shocks to the inflation outlook by then, which I think is unlikely.”

But monetary policy will depend on how the economy performs and there is little point in speculating as to how high rates will eventually be raised in this cycle, Simkus said in an interview.

FRAGMENTATION FEARS

Simkus said there was still no sign that the transmission of monetary policy was being impeded by widening yield spreads within the eurozone. The ECB has said it is working on a tool to cap any unwarranted divergence in yields as it moves towards raising rates in July and September. (See MNI SOURCES2:ECB Mulls Crisis Tool As Officials Debate Spreads)

“The risk of market fragmentation does exist,” Simkus said, “therefore a new tool that can act as a backstop is appropriate. But we have not seen fragmentation yet, so any such tool is pre-emptive. Hopefully it won’t be needed to use.

“It’s important not to get bogged down in the details of [the new tool’s] design at the start of discussions. We should start first from principles. Above all, it should not interfere with the monetary policy stance.”

MNI INTERVIEW: Flexible ECB Bond Buys Risk Breaking German Law **05-07-2022**

By Luke Heighton

(MNI) London - Germany’s constitutional court may rule against any attempt by the European Central Bank to use proceeds from maturing German bonds bought under its Pandemic Emergency Purchase Programme to buy debt of fiscally weaker countries, advisor to the German finance minister and former chair of the Council of Economic Experts Lars Feld told MNI.

In an interview, Feld also criticised attempts by the ECB to design a new tool to limit any blow-out in peripheral bond spreads, saying it was unacceptable for countries such as Italy to refuse to accept conditions under the existing Outright Monetary Transactions facility. The EU needs to draw in fiscal stimulus as it battles high inflation and the danger of a wage-price spiral, even as Germany’s economy is already stagnating, he said.

“I'm not happy with the information we now have on the anti-fragmentation tool,” Feld, who was named an advisor to Finance Minister Christian Lindner in February and is also Walter Eucken Institut director and a professor at the University of Freiburg, said in an interview late last week. “I have the impression that the ECB is simply doing this particular type of monetary policy ambiguity in order to calm down markets, but I'm sceptical that it will finally work.”

The legal room to design a new tool -- which investors anticipate may be unveiled at the next Governing Council meeting on July 21 -- is limited given rules capping purchases of individual countries' bonds under other ECB programmes, Feld said. (MNI SOURCES2:ECB Mulls Crisis Tool As Officials Debate Spreads)

"We have an instrument in place called OMT which would be the right way to go," he said. "I find it unacceptable that countries simply refuse to accept conditionality. I don't think that the other member countries should give in in that regard."

CONSTITUTIONAL COURT

The ECB also hopes to use proceeds from maturing bonds acquired by PEPP to compress spreads if necessary, but Feld said that may violate German law.

"PEPP was an additional tool, and to say we will use PEPP, or the maturing PEPP bonds that we get from Germany, the Netherlands and others in order to reinvest them in countries where the spreads are going up may nevertheless be unconstitutional regarding the German case," Feld said.

Much internal EU discord stems from a fundamental disagreement over fiscal policy, according to Feld, who chaired the Council of Economic Experts from 2020 to 2021. Member states should now consolidate their fiscal stances, he said.

"We need to stay away from an expansionary fiscal policy in order not to increase inflationary pressures even more than we currently have," he said, "You have a divide in the assessment of what fiscal policy actually should do in the current situation. That's the basic problem. It's not the problem of the alignment between fiscal and monetary policy."

STAGFLATION

Even as prices surge, the growth outlook is weak, with Germany entering stagflation, Feld said.

"We have stagflation already, just because we have stagnation for the third quarter in a row together with high inflation. The outlook for the rest of the year is gloomy. But, overall, I would say that if it remains in a stagnation, it is one of the best outcomes we can hope for."

Inflation, though, may not have peaked in May, when it hit 7.9% before easing to 7.6% in June, he said.

"The pressure regarding oil producer prices has not relaxed yet, and once that finally translates into consumer price increases, this would mean that we either are on a plateau of high inflation rates, month by month, or we will have further increases and the peak is still waiting for us," he said, warning of a possible wage-price spiral.

Germany faces significant challenges as it weans itself of Russian gas, Feld said, and in the nearer term shutdown of Russian deliveries could prompt high-energy intensity industries such as glass and ceramic production to relocate to the U.S. or Sweden. The government should change the law to allow for earlier energy rationing for households if necessary, he said, in order to allow companies to grow.

"I know that in international discussions there's the fear that, given its dependence on Russian gas, the German economy will have huge difficulties. But when you look at the state of our firms and the resilience they have developed in these 10-12 good years, I'm not so negative on this outlook even if the worst scenarios materialise," Feld said.

MNI SOURCES: Divisions Remain Over ECB's New Crisis Tool **15-07-2022**

(MNI) London - Large remaining differences over the design of a new mechanism to contain any blow-out in peripheral bond spreads will be difficult to resolve by next week's European Central Bank meeting, but officials will aim to convince markets that the tool has major firepower even if some of its details are never made public, Eurosystem sources told MNI.

ECB staff are evaluating five proposals which they expect to whittle down for the Governing Council as they seek to incorporate binding conditions but avoid the stigma of the existing Outright Monetary Transaction programme, a senior central bank source said. Discussions have taken place between the ECB and national central banks, with Austria and Germany making the most demands on conditionality, though sources said there proposals to tie these to the EU's excessive deficit procedure have been dropped and there should be agreement by September or October.

Some aspects of the anti-fragmentation tool may be kept in reserve even once finalised, sources said, noting that it will be a backstop and that reinvesting maturing bonds acquired under the ECB's Pandemic Emergency Purchase Programme will remain the first line of defence against volatility.

"Details of the plan will not be disclosed – so size, scope, what size of spreads constitute – these will not be spelled out," said one source. "A key strength of the AFT will rest on its mystique."

ITALIAN BONDS

A key argument for the tool is that it is necessary to support peripheral bond markets as rates rise, and the crisis now engulfing the government in Italy, where Prime Minister Mario Draghi offered his resignation on Thursday, highlights both the need to get it into place and the importance that it comes with clear conditionality.

"Events in Italy in recent days have underlined our dilemma," one source said. "We must not have a tool that offers governments a free hand over fiscal policy in these very difficult times, but we must be able to stave off unjustified speculative moves by the bond markets."

Conditionality will be central to the tool, which is likely to face scrutiny by Germany's Constitutional Court, though it must also avoid the stigma attached to the OMT facility, whose use is contingent on agreeing programmes with the European Stability Mechanism.

Early proposals to tie the programme to the EU's excessive deficit procedure have been dropped, with an EU official telling MNI this would have put finance ministers in a difficult position and perhaps made them reluctant to enact the procedure.

"It would also have meant too much meddling by the ECB in fiscal policy," the EU source said.

The new tool's fiscal conditions are likely to look beyond headline metrics such as those specified in European Union debt rules, one of the eurosystem sources said.

"Rather than being dependent on Brussels, I would put it the other way around: we are actually setting conditions for countries in order to drive others toward what already should be in place. There's no free lunch, and we've always said that."

The ECB will make allowances for spending in support of structural reform, the source said, adding that it could also consider use of funds provided by the NextGenerationEU financial aid programme. "When the country is at least showing, or trying to, put in their share of work to tackle fragmentation, then the ECB is giving the other 50% share of the work, and then jointly, we will have a good outcome."

CALIBRATION

The tool could also be calibrated at short intervals, perhaps on a weekly basis.

"It will be a very sensitive tool that will be prone to very sensitive calibration, from meeting to meeting or week to week, especially in the beginning," the source said. "We also want to find the actual root cause of fragmentation, otherwise the tool was not effective, or we wouldn't need a tool."

Sources acknowledged the danger that markets might react with initial disappointment to a lack of detail, though they added that the ECB would convince investors of its firepower.

"On Thursday, whether we learn something or not, it will be a volatile couple of days. And the true reactions will only be visible the week after, when markets open again on Monday," one source said.

Another source agreed that Thursday's announcements were likely to include "constructive ambiguity -- in part because that is what is wanted, and part because the details may need still to be ironed out." But, the source added, the Governing Council is united in its aim of preventing fragmentation and accepts that any plan should convey the impression that it is unlimited in size.

"It will be difficult to agree on all the technicalities by next week as there are still some very large differences on the plan itself. However, there will be an embryonic outline with more than enough firepower already available if needed," the official said. An ECB spokesperson declined to comment to MNI.

MNI SOURCES: September Hikes From 25-75Bps On Table For ECB **15-07-2022**

(MNI) London - Anything from 25- to 75-basis-point hikes could be on the table when the European Central Bank in September, though next week's widely-expected 25-basis-point increase is now looking almost set in stone, Eurosystem sources told MNI.

Bar any downside surprises to incoming inflation datam a 50 basis-point hike in September remains the most probable outcome, one source said.

"I would not be surprised if the ambiguity over September will again point to 50 basis points," the source said, but added that either 25- or 75-basis-point moves could be considered.

"The risks are all too evident on both sides of the ledger, although price pressure will dominate for now. The weaker euro, gas prices, gas supply, airline disruption to the travel/tourism industry, political upheaval, supply chain disruption, further Covid lockdowns in China," the source said.

NEXT WEEK

But anything but a 25-basis-point hike next Thursday would be a major surprise, given the ECB's guidance, sources said, even if some Governing Council members may call for 50 points. All sources agreed that the ECB should be at at least at zero by the autumn.

"Even if we do face weak growth or other weakening circumstances, we will still see a higher rate hike if it is necessary to fulfill our price stability mandate," a Eurosystem official said. "Our primary mandate is our priority, and we will not sacrifice our mandate for German growth, for Italian growth."

An ECB spokesperson declined to comment.