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Economic Research

Economic Briefing

ECB – Lagarde not impressed by Powell

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The ECB cut its deposit rate by 25 basis points to 2.75% today, as widely expected. Unlike the Fed, the ECB clearly suggested further rate cuts. We continue to expect three further rate cuts of 25 basis points each by the middle of the year, although there are also arguments in favour of a wait-and-see approach in the eurozone. For example, the ECB is likely to overestimate the decline in wage pressure in the second half of the year due to the construction of its forward-looking wage tracker.

It was a foregone conclusion that the ECB would cut its deposit rate from 3.0% to 2.75% today. Accordingly, what mattered most was what President Christine Lagarde would say about the future. By and large, there was no change compared to the last press conference in December. In its [statement](#), the ECB repeated the core statement that inflation would return to its 2% target on a sustainable basis in the course of this year. The ECB will decide from meeting to meeting depending on the data.

Asked by a journalist whether the rate cut process could be coming to an end after a total of five rate cuts, Lagarde pointed out that monetary policy was still "restrictive", i.e. dampening the economy and inflation. This is a clear hint that the ECB sees room for further interest rate cuts. Lagarde emphasised that any discussion about a possible end to interest rate cuts was "premature".

ECB deposit rate at 2.0% in the middle of the year

All in all, Lagarde's comments confirm our forecast that the ECB will cut its policy rates three more times by 25 basis points each time. The next step is likely to take place in March, when the ECB publishes its updated projections for inflation and GDP. We continue to expect the deposit rate to reach 2.0% in the middle of the year.

The ECB should pay more attention to the Fed

The ECB is easing its monetary policy more decisively than the Fed, which only yesterday adopted a wait-and-see stance. But there are also arguments in the eurozone that call for caution:

- Inflation, excluding the volatile prices for energy and food, has settled above the ECB's target of 2%. This is mainly due to the prices of mostly labour-intensive services, which have been rising by far too high a rate of 4% for more than a year.
- Wages are continuing to rise strongly – most recently by more than 5% in terms of collectively agreed wages. However, it is unclear whether wage pressure – as signalled

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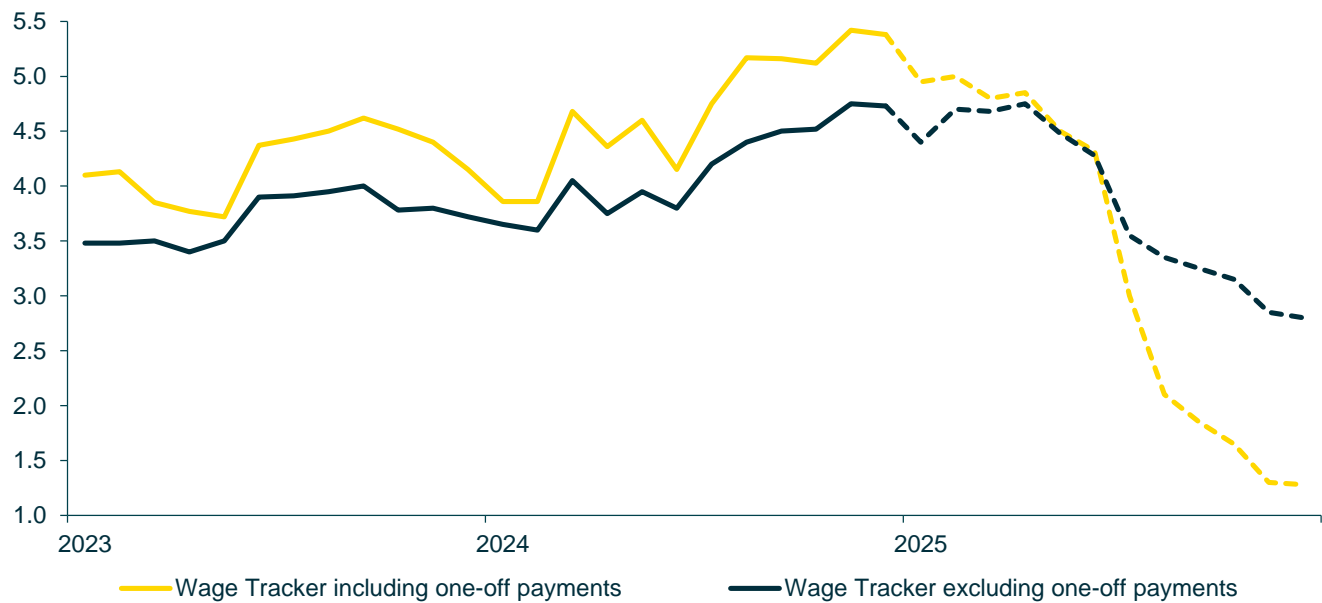


by the ECB Wage Tracker - will ease significantly in the second half of the year (chart). This is because the collective wage data available for the second half of the year often comes from the second half of two-year collective wage agreements, in which wages usually rise much more slowly than in the first half of the contract. However, if new collective agreements are added, the ECB Wage Tracker is likely to show higher increases again for the second half of the year. All in all, the ECB is probably underestimating wage trends (see our [study](#)).

- The recent recovery in the Purchasing Managers' Index (PMI) gives hope for a slightly better growth from the spring onward. However, when the PMI fell surprisingly sharply in autumn 2024, the ECB used this as an argument to cut interest rates again in October immediately after the September meeting. If the PMI now rises again, this should actually be an argument for the ECB against further rapid interest rate cuts.

Chart 1 - ECB Wage Tracker points to easing wage pressure in the second half of this year

ECB Wage Tracker, based on data on wage settlements in Germany, France, Greece, Italy, Austria, the Netherlands and Spain, in percent compared to previous year



Source: ECB, Commerzbank Research



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