

## ECONOMIC PULSE

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## EUROZONE: ECB MEETING OF 10 MARCH: KEY POINTS TO WATCH

The launch of Russia's military invasion against Ukraine on Thursday, 24 February, puts further focus on the next ECB meeting on 10 March and further increases the difficulty of the task facing the central bank. First of all, we will pay particular attention to the extent of the upward revision of its inflation projections. We expect major revisions given the latest developments and the most recent inflation figures, which continue to rise (headline inflation hit 5.8% y/y in February, according to the Eurostat flash estimate, and core inflation was 2.7% y/y). In December 2021, the ECB was forecasting average annual inflation of 3.2% in 2022 and 1.8% in 2023 and 2024. It will also be interesting to see whether the ECB expects inflation to hold above its 2% target in 2024. This is a key point to watch since it will give an idea of the ECB's confidence in its capacity to reach this target, and whether the conditions have come together yet to begin raising key rates again.

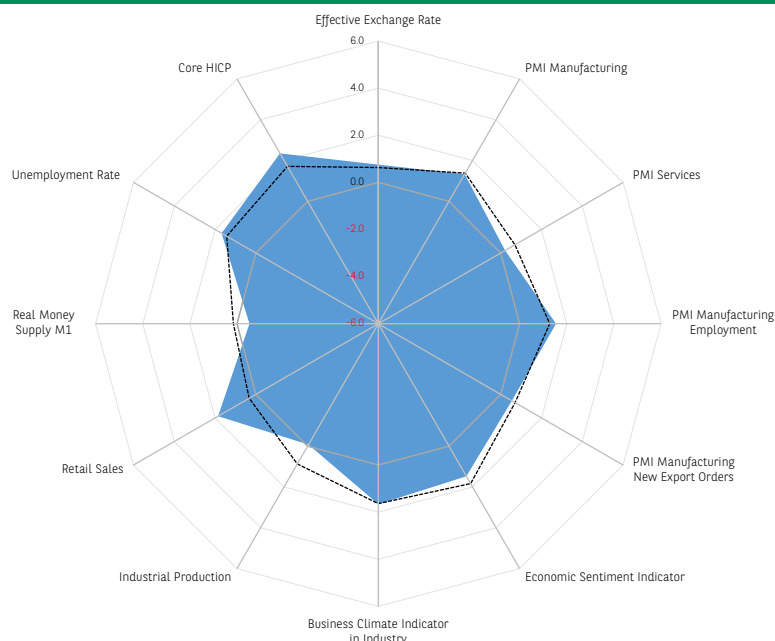
We will also pay attention to the extent of the ECB's downward revision of its growth forecasts. In December, the central bank was forecasting an average annual growth of 4.2% in 2022 followed by 2.9% in 2023 and 1.6% in 2024. For the time being, the Eurozone seems able to weather the economic shock of the war given its pre-existing economic momentum (as illustrated, for instance, by an unemployment rate at an all-time low of 6.8% in January and by the positive February figures for business confidence surveys) and the very probable implementation of new fiscal support measures to buffer the shock. The size of the shock is very uncertain and hard to evaluate. It will undoubtedly be negative, and one of its first repercussions is already to exacerbate the pressures on supply, the supply chain and prices that were at work. We cannot rule out the possibility that Eurozone GDP will contract for one or two quarters. According to very first estimates from Philip Lane, the ECB's chief economist, the war could slash between 0.5 and 1 points of growth from the Eurozone in 2022.

For the ECB, the conflict in Ukraine is a game changer. It should cool off the debate that was heating up prior to the invasion about an accelerated timetable for normalising monetary policy in response to inflationary risks (end date for the Asset Purchasing Programme (APP), timing of the first deposit rate hike and the number of rate increases in 2022). The inflationary shock is certainly growing, but so are its negative effects on growth. Fears about growth are winning out over inflationary concerns, and the balance between the downside risks to growth and the upside risks to inflation is shifting towards the first, and thus towards a wait-and-see stance of the ECB. Optionality and flexibility, caution and gradualism as well as data dependence will be the keywords again in the monetary policy setting. The ECB is not an adept of pre-commitments, but as Christine Lagarde said on 25 February, "the ECB stands ready to take whatever action necessary to ensure price stability and financial stability in the euro area."

According to our central scenario, the Pandemic Emergency Purchasing Programme (PEPP) will end as expected in March while the APP will take over with monthly asset purchases of EUR 40 bn in Q2 and EUR 20 bn per month open-ended thereafter. Our scenario calling for a preliminary 25 bp rate hike as of September now seems unlikely, although a rate increase by the end of the year is still on the table, especially if tensions were to abate.

Hélène Baudchon

## QUARTERLY CHANGES



SOURCE: REFINITIV, BNP PARIBAS

The indicators in the radar are all transformed into 'z-scores' (deviations from the long-term average, as standard deviations). These z-scores have mean zero and their values are between -6 and +6. In the radar chart, the blue area shows the actual conditions of economic activity. It is compared with the situation four months earlier (dotted-line). An expansion of the blue area compared to the dotted area signals an increase in the variable.



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