

Central bank head defends rate hike



The Euro sculpture stands in front of the former headquarters of the European Central Bank (ECB) in Frankfurt, Germany, May 23, 2023. MICHAEL PROBST — THE ASSOCIATED PRESS FILE

BY DAVID MCHUGH

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FRANKFURT, Germany >> The head of the European Central Bank defended its June 11 rate hike as justified to ward off real inflationary pressures and said it wasn't just a mere "insurance hike."

ECB head Christine Lagarde said Monday that without the quarter percentage-point increase, inflation could have lingered above the bank's 2% target into 2028.

"Some have characterized our rate increase earlier this month as an 'insurance hike,'" Lagarde said. "I'm sorry to disappoint them. That is not an accurate description. We faced an outlook of rising headline and core inflation."

The central bank for the 21 countries that use the euro raised its benchmark rate earlier in June by a quarter point to 2.25%, the first rate move in a year. Even with higher rates, inflation is projected to return to 2% only in the last three months of 2027. Euro area annual inflation was 3.2% in May.

Lagarde said, however, that the bank wouldn't need the jumbo half-point and three-quarter-point increases that it used to squelch double-digit inflation after Russia cut off gas supplies over the war in Ukraine.

Note

Instead, better forecasting means the bank can go meeting to meeting and take a more measured approach as it confronts the fluctuating price pressures from the Iran war and the interruption of oil and gas supplies through the Strait of Hormuz. The bank has rate-setting meetings July 22-23 and Sept. 9-10.

The bank responded to the Russian gas cutoff with "the fastest tightening cycle in our history, raising rates in increments we had never used before," she said in the text of a speech at the bank's annual monetary policy conference in Sintra, Portugal.

"We no longer need to act with the same force," she said. "We can make measured adjustments to rates, calibrated to the shocks we face."

She said bank forecasters were now using scenarios of milder and harsher outcomes to geopolitical events so that the bank could make sure it doesn't over- or underreact.

Oil prices have fluctuated wildly during the Iran war, while the European economy has held up better than many expected against headwinds from U.S. President Donald Trump's imposition of new tariffs on European imports.