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Europe Hints That It May Raise Rates

By [MARK LANDLER](#)

FRANKFURT, Feb. 2 — The European Central Bank laid the groundwork for a rate increase next month, its second in five years, saying that Europe was continuing to grow and that inflation remained a threat.

The central bank opted to keep interest rates unchanged at 2.25 percent at its meeting Thursday, but its president, [Jean-Claude Trichet](#), said at a news conference here that the bank would "exercise vigilance" in monitoring prices — a code phrase for an imminent tightening of monetary policy.

"There's not much standing between now and a rate hike," said Thomas Mayer, the chief European economist at [Deutsche Bank](#). "The only thing that could dissuade them from acting would be new economic data that suggests something bad is happening in Europe."

He and other economists expect the bank to raise rates by a quarter-point in March. Mr. Trichet, who has sought to telegraph such changes in advance, did nothing to discourage them. "What I see in the short-term expectations of moves seems to be reasonable," he said.

Mr. Trichet, however, reiterated that the bank would not embark on a cycle of rate increases like that being pursued by the Federal Reserve. He sought to distinguish the European Central Bank from the Fed, even as he heaped praise on [Alan Greenspan](#), who retired this week as Fed chairman.

Jörg Krämer, the chief economist at the HVB Group in Munich, said, "The E.C.B. is not on autopilot, which is what you've had at the Fed since June 2004."

The Fed has been raising rates regularly, "whatever the economic statistics," Mr. Krämer said. "It would be very difficult to do that at the E.C.B., given the divisions on the board."

Those divisions bubbled to the surface on Thursday when Mr. Trichet pointedly reminded financial markets that he alone speaks for the bank's 18-member governing council on monetary policy. He was referring to remarks made by an Italian member of the council, Lorenzo Bini Smaghi, who has publicly expressed his reluctance to raise rates further in an economically fragile Europe.

"He doesn't speak on behalf of the governing council. Full stop," Mr. Trichet said, in an uncharacteristically sharp tone.

Several analysts applauded Mr. Trichet's drive to impose discipline on the bank's communications. Remarks by Mr. Bini Smaghi and other board members, they said, had muddied the bank's message and could weaken its resolve at a time when it faces heavy political pressure. When the bank raised rates by a quarter-point in December, it provoked a storm of protest from European leaders, who said a tighter money supply could choke off the recovery of their economies.

They continue to apply pressure, if less directly. At the World Economic Forum conference in Davos, Switzerland, last week, the French finance minister, Thierry Breton, said inflation posed no problem in France — undermining a central justification for the bank to tighten policy.

The bank faces similar doubts on its economic analysis. In December, it forecast that Europe's economy would expand about 1.9 percent this year, compared with 1.4 percent in 2005. Recent statistics, though, paint a more mixed picture of the Continent's health. In Germany, investor confidence is soaring, yet retail sales continue to be weak and unemployment rose in January. In France, manufacturing production slowed markedly in the most recent survey.

Mr. Trichet, however, said he was confident that the general trend in Europe was one of steady economic growth. He noted that inflation, which has moderated in recent months but still hovers above the bank's threshold of 2 percent, might rise again if the price of oil jumped.

"You could argue that he downplayed the weakness in the recent data," said Elga Bartsch, an economist at [Morgan Stanley](#). "But the forward-looking indicators suggest that this was just a bump in the road."

Ms. Bartsch said the bank was all but certain to raise rates next month, but wanted to leave its options open thereafter. Like most economists, she says she believes the equilibrium interest rate for the 12 nations that use the euro is about 3.25 percent, which would imply a few more increases.