Economic Adviser

Macro Research

May 2023♦ Date of issue: 2 May 2023

Finanzgruppe

Contents

Special: ECB enters the home stretch of its rate-hike cycle

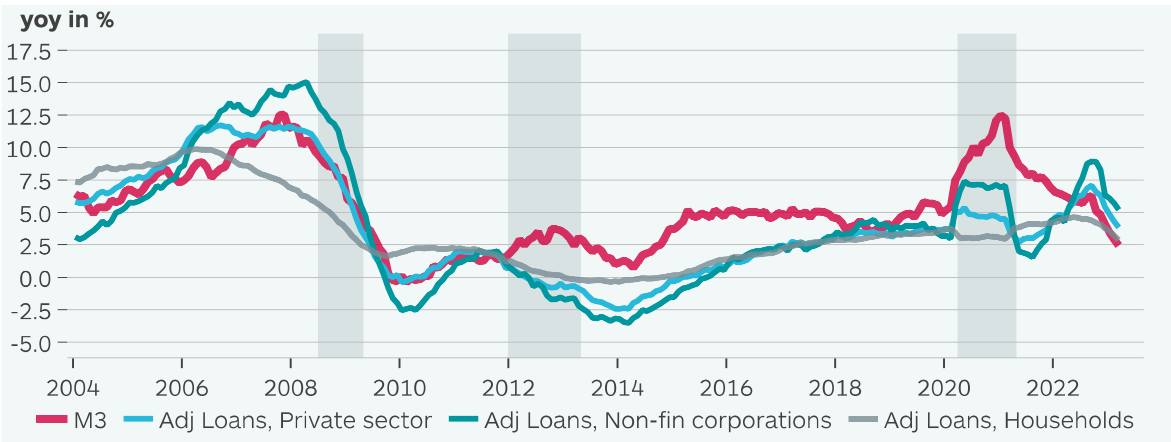
Analyst: Christian Lips, Chief Economist

ECB interest rate path: May looks certain to see a slowdown in the pace of hikes

In concert with many other central banks worldwide, the ECB has responded to the massive inflationary pressures with significant interest rate hikes since July last year. Over that period the central bankers in Frankfurt have raised the key rates by an aggregate of 350 basis points, doing so at a hitherto unprecedented pace. The end of the line has not yet been reached in the rate-hike cycle but, after the most recently published macro data, it now looks quite certain that the ECB will resolve to scale back the pace of its increases at its meeting in May.

This is also indicated by the recent remarks on the part of the central bank's chief economist Philip Lane and François Villeroy de Galhau in an interview with Le Figaro, in which the possibility of a few further rate hikes proving necessary was mentioned though, according to Villeroy, these ought to be limited in size and number. Villeroy's viewpoint is of great importance, as he has on many occasions in the past represented the majority or compromise-oriented stance among the members of the ECB's Governing Council. It goes without saying that there are also members from the hawk camp who can imagine a further rate hike of 50 basis points, besides which all monetary policymakers naturally stress that further decisions will depend on the incoming data. Until the May session, however, there is hardly any likelihood of unexpected events or data that could after all swing the pendulum towards an upward rate adjustment of 50 basis points.

Chart: Lending dynamics and M3 money supply growth



Sources: ECB, Macrobond, NORD/LB Macro Research

Important decision-making parameters for the central bankers

When assessing the ECB's further monetary policy stance, account must first be taken of the fact that the rate hikes implemented up to now are already having an effect but, due to customary time lags, have not yet fully arrived in the real economy. But which decision-making parameters will the Governing Council members use to guide their decisions in the coming months?

The answer lies in the following triad:

- Assessment of the inflation outlook on the basis of current economic and financial data,
- assessment of the underlying inflation and
- strength of monetary policy transmission.

Inflation data remain crucial – statistical "noise" complicates interpretation
The ECB will therefore first check, on the basis of the latest economic data, whether the baseline scenario updated in March is in principle still valid. In light of the data published in late April there is much to suggest that this is indeed the case since the slight economic recovery now emerging is consistent with the baseline scenario in the ECB's projections. As regards the HICP inflation rate, the available data from the member states more or less point to a sideways trend in April. The easing of input costs, at least for food and goods, provides indication of a further decline. This trend is not so clear where services are concerned, and the further development in that sector very much depends on the future wage settlements. After several years of real wage loss, the wage settlements arrived at to date are rather to be seen as a catch-up effect, whereby the normalization process is prolonged but there is no recognizable de-anchoring of inflation expectations.
We see no signs of any so-called "greedflation". If companies have adjusted their sales prices in anticipation of higher input cost increases, surprises on the upside such as, for example, the recent decline in energy prices, make for higher profit margins. Furthermore, the easing in supply bottlenecks will likely lead to a normalization in those areas in which supply was artificially limited over a longer period of time for pandemic-induced reasons. Problems would only then arise if high margins, strong inflationary pressures and wage developments were to mutually fuel each other.
The development of underlying inflation is probably the central bankers' biggest headache at the present time. However, core inflation likely peaked in March with a year-on-year level of 5.7 percent. The easing in supply bottlenecks and falling energy prices will, with a time lag, have a dampening effect on the core rate as well, and the inflation in services in Germany has already fallen very slightly again in April.

Effects of market turmoil are so far manageable
The strength of monetary policy transmission has acquired particular significance against the backdrop of the market tensions in March. Indeed, market developments could possibly lead to an additional tightening of financing conditions. That eventuality would necessitate a lesser degree of monetary tightening to bring inflation back into the target range. Against this background, the results of the ECB's new bank lending survey will be a focus of attention in the first week of May.
That said, it may be difficult to identify whether changes are actually a result of the recent market tensions or part of the “normal” and desired transmission of the rate hikes. The survey three months ago had already shown significant effects of the rising interest rates on credit demand and conditions. In recent months, bank loans to companies and households have also become more expensive, and credit growth has accordingly been slowed by both reduced demand and the tightening of lending conditions (see chart on page 1). This was accompanied by a marked slowdown in money supply growth – a trend that will likely continue. As regards transmission, however, it is above all positive to note that there are so far no signs of any fragmentation. We therefore consider a pause by the ECB to be just as unlikely as a 50bp rate hike.

Further decisions to be taken when the rate-hike cycle ends
The ECB is facing a number of important decisions this year. In the short term, May and June will see intensive discussions on the interest rate path, though this should not be construed as meaning a fundamental conflict: the next interest rate decisions are more a matter of "fine-tuning" on the last few meters of the rate-hike cycle. We currently expect three small hikes, with the hawk camp possibly foregoing the third one in return for an earlier termination of the APP reinvestment phase. The ECB will without doubt maintain its restrictive stance for some time to come, however, and an initial rate cut is not likely to be on the agenda until well over a year from now. But even after the rate-hike cycle has ended, there will be some far-reaching decisions to be taken, with implications for liquidity supply and/or market rates. These include, for example, the long-term handling of the high volume of asset holdings (keyword: PEPP reinvestments), the design of a digital euro and the question as to whether the ECB should return to using an interest rate corridor system. Suspense is thus guaranteed!

USA: Rougher times ahead for the economy

Analysts: Tobias Basse // Bernd Krampen

Rougher times ahead for the economy

The initial data published on the development of real US economic growth in Q1/2023 came with a slight surprise – namely that the economy grew by 1.1 percent (ann.). However, the figures are still highly susceptible to revision, so considerable caution is advisable when interpreting them in any great detail. That said, a look at the recent retail sales data reveals that Q1 kicked off with a veritable surge in consumption. Published monthly, this time series registered impressive month-on-month growth of 3.1 percent. The data reported for February and March were already less encouraging, however. The figures available for March are still of a provisional nature but, with a decline of 1.0 percent mom, indeed already reveal rather marked weakness. High interest rates and the general uncertainty as to the further development of the US economy appear to be weighing on consumption to a more sustained degree. While the positive employment situation is still helping consumers in the United States and the rate of unemployment currently stands at just 3.5 percent, the fact is that, at the same time, initial signs of a slowdown in the US labour market are gradually emerging. The pent-up demand for personnel among the companies in the recent past will likely ensure that the pressure on employees ought not to become extreme, but no further positive news from the US labour market is to be expected for the time being. All in all, the risk of recession in the USA has increased of late, though a real catastrophe is not to be expected. The crucial question now is likely whether a mild recession can still be averted.

Chart: Interest rates in the USA

Sources: Macrobond, NORD/LB Macro Research

What's next on the US real estate market?

The situation on the real estate market is set to remain rather difficult for the time being. Basically, at least in macroeconomic terms, a further downward trend in house prices is to be reckoned with, with the likelihood of considerable regional differences. Still, the NAHB Housing Market Index (HMI), did improve to 45 points in April. This important sentiment indicator, which can be helpful in forecasting US real estate prices, thus remains below the "magical" mark of 50 points, meaning that the time series is increasingly points in the direction of a slowdown to the decline of house prices. At any rate, a close eye still needs to be kept on the US real estate market. Should new problems emerge here in the future, further challenges would arise for some of the more traditional – as opposed to Silicon Valley Bank – regional financial institutions which are, for example, more active in construction financing. In this respect, the NAHB Housing Market Index remains of great importance from the point of view of the international financial markets.

Monetary policy and the US dollar

The FOMC's policy on interest rates is no longer of any great help to the US currency. With the further stance of the central bankers in Washington in mind, the FX market is most probably pricing in a further key-rate hike of 25bp in total. After that, the Fed will likely go into wait-and-see mode. The developments in inflation could also allow for this hesitation on the part of US central bankers, especially since the now more difficult economic environment already appears to provide a sound argument against any further raising of the Fed funds target rate. Against this background, some market participants in the FX segment already appear to be expecting initial rate cuts by the central bank in Washington in the course of 2023. In the absence of negative news of a really lasting nature from the North American economy, however, we consider this scenario unlikely. Nonetheless, any marked concern about a deeper recession in the USA could lead to an interim overshooting of the euro/dollar exchange rate, which could even put the fundamentally justified level off the radar in the short term. Additionally, the discussions currently taking place in Washington about raising the debt ceiling are not of any help to the US currency either. Moreover, the ECB is currently under greater pressure than the Fed in terms of monetary policy. This environment is in principle a favourable one for the euro. However, the FX segment in the meantime already ought to price in a relatively high degree of pressure on the greenback.

Fundamental forecasts, USA

	2022	**2023**	**2024**
GDP	2.1	1.1	1.2
Private consumption	2.7	1.6	1.5
Govt. consumption	-0.2	0.5	1.0
Fixed investment	-0.5	2.0	2.5
Exports	7.1	2.0	3.0
Imports	8.1	4.0	3.0
Inflation	8.0	3.9	2.4
Unemployment rate[1]	3.6	3.8	4.0
Budget balance[2]	-4.1	-3.7	-3.7
Current acct. balance[2]	-3.7	-3.4	-3.4

Change vs previous year as percentage; [1] as percentage of the labour force; [2] as percentage of GDP

Sources: Feri, NORD/LB Macro Research

Quarterly forecasts, USA

	III/22	**IV/22**	**I/23**	**II/23**	**III/23**
GDP qoq ann.	7.0	2.6	1.1	-0.1	0.0
GDP yoy	1.9	0.9	1.6	1.7	0.9
Inflation yoy	8.3	7.1	5.8	3.9	3.2

Change as percentage

Sources: Feri, NORD/LB Macro Research

Interest and exchange rates, USA

	27.04.	**3M**	**6M**	**12M**
Fed funds target rate	5.00	5.25	5.25	5.00
3M rate	5.30	5.10	5.10	4.70
10Y Treasuries	3.52	3.50	3.40	3.30
Spread 10Y Bund	106	100	80	80
EUR in USD	1.10	1.08	1.08	1.09

Sources: Bloomberg, NORD/LB Macro Research

Euroland: Higher growth momentum from Q2 onwards

Analysts: Christian Lips, Chief Economist // Christian Reuter

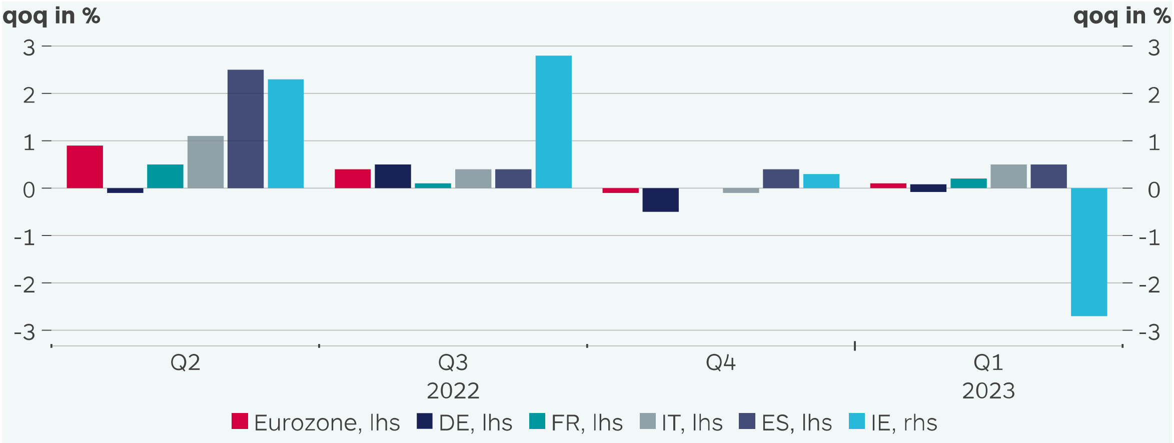
Merely moderate GDP growth in Q1

Q1 saw the eurozone back on a modest growth path, with real GDP 0.1 percent – adjusted for calendar effects – up on the preceding quarter. The corresponding annual rate fell slightly to 1.3 yoy. Investments and net exports made positive growth contributions, while consumption again proved an inflation-induced brake on growth.

The good news is that there has been no GDP shrinkage in any of Euroland's major economies (see chart). Germany's real GDP stagnated, while economic output in France registered moderate expansion (+0.2 percent) despite onerous strikes. Italy and Spain reported impressive GDP growth of no less than +0.5 percent each. Indeed, the growth reported for the eurozone as a whole would have been even more pronounced, had it not been for a strong braking effect from Ireland – where GDP nosedived by 2.7 percent qoq! The growth figures among the other member states were predominantly preceded by plus signs, with Belgium (+0.4 percent) and Portugal (+1.5 percent) both registering a disproportionately high pace of momentum.

In retrospect, the economic trend was subdued in the winter half-year, but the outlook for the economy has at any rate brightened of late. At 99.3 points in April, economic confidence is only slightly below the long-term average. The sentiment among the service providers has brightened to a particularly pronounced degree of late, as confirmed by the relevant PMI. Moreover, the industrial sector is benefiting from both the declining energy prices as well as from the marked easing in supply bottlenecks. Inflation must now fall even further, then consumption will also be able to contribute to growth again.

Chart: GDP growth in the eurozone up to Q1/2023



Sources: Macrobond, NORD/LB Macro Research

After the previous month's significant decline – inflation likely not fallen further in April

March saw inflation in the eurozone plummet to 6.9 percent yoy. As expected, this decline was primarily a result of falling energy prices, with a particularly strong base effect dampening the annual rate in March. The energy index component fell again in year-on-year comparison for the first time since February 2022, by 0.9 percent. At the same time, inflation continued to broaden its impact, with the annual rates for foodstuffs (+17.5 percent yoy), alcohol and tobacco (+7.3 percent yoy) rising further to long-term highs. While the price pressure on industrial goods excluding energy eased slightly for the first time in a good year, the inflation rate for services climbed to an all-time year-on-year high of 5.1 percent. The core inflation rate accordingly continued upwards to hit a new historical year-on-year peak of 5.7 percent.

We are not reckoning with any further decline in the inflation rate in April as month under review. While the annual rate for food will likely fall due to a favourable base effect, the prices for package holidays and overnight stays customarily rise sharply in April as a seasonal effect, however. This effect can be expected to have a stronger impact on overall inflation due to the significantly higher weighting compared to the previous year, but will be reversed again in May, however. On the basis of the consumer price data from the member states reported by the date of going to press, the HICP flash estimate for April, which is due in the first week of May, can at best be expected to register a sideway or even slight upward movement. As regards the core rate, there can be no guarantee of a trend reversal – with corresponding implications for the upcoming discussions among the members of the ECB's Governing Council.

ECB: Markets pricing in a more realistic interest path – restrictive strategy to be maintained
Following the immense uncertainty in March, the markets are pricing in a more realistic interest rate path for the ECB again. The fluctuating key-rate expectations had once again led to a high degree of volatility among the capital market rates. While a further key-rate hike of 50 basis points in May could certainly be justified, the recent market turmoil makes a somewhat more cautious approach advisable. We therefore expect the ECB to raise its key rates in May and June by 25 basis points in each case, likely followed by a concluding hike in July. Moreover, it is becoming clear that the central bankers will have to maintain their restrictive stance for longer than some currently hope. Rate cuts are not likely to be on the agenda until mid-2024. Against this background, long-term government bond yields ought to rise slightly but not sustainably exceed the annual highs seen in early March anymore.

Fundamental forecasts, Euroland

	2022	**2023**	**2024**
GDP	3.5	1.0	1.7
Private consumption	4.3	0.0	1.5
Govt. consumption	1.4	2.2	1.0
Fixed investment	3.8	1.2	3.1
Net exports[1]	-0.1	0.4	0.0
Inflation	8.4	5.7	2.9
Unemployment rate[2]	6.7	6.7	6.7
Budget balance[3]	-3.6	-3.3	-2.6
Current account balance[3]	-1.0	1.4	1.5

Change vs previous year as percentage, [1] as contribution to GDP growth; [2] as percentage of the labour force; [3] as percentage of GDP

Sources: Feri, NORD/LB Macro Research

Quarterly forecasts, Euroland

	III/22	**IV/22**	**I/23**	**II/23**	**III/23**
GDP sa qoq	0.4	0.0	0.1	0.3	0.4
GDP sa yoy	2.5	1.8	1.3	0.8	0.8
Inflation yoy	9.3	10.0	8.0	6.4	5.0

Change as percentage

Sources: Feri, NORD/LB Macro Research

Interest rates, Euroland

	27.04.	**3M**	**6M**	**12M**
Repo rate ECB	3.50	4.25	4.25	4.25
3M rate	3.25	3.90	3.90	3.80
10Y Bund	2.46	2.50	2.60	2.50

Sources: Bloomberg, NORD/LB Macro Research

Germany: Recession averted, but momentum to remain subdued in 2023

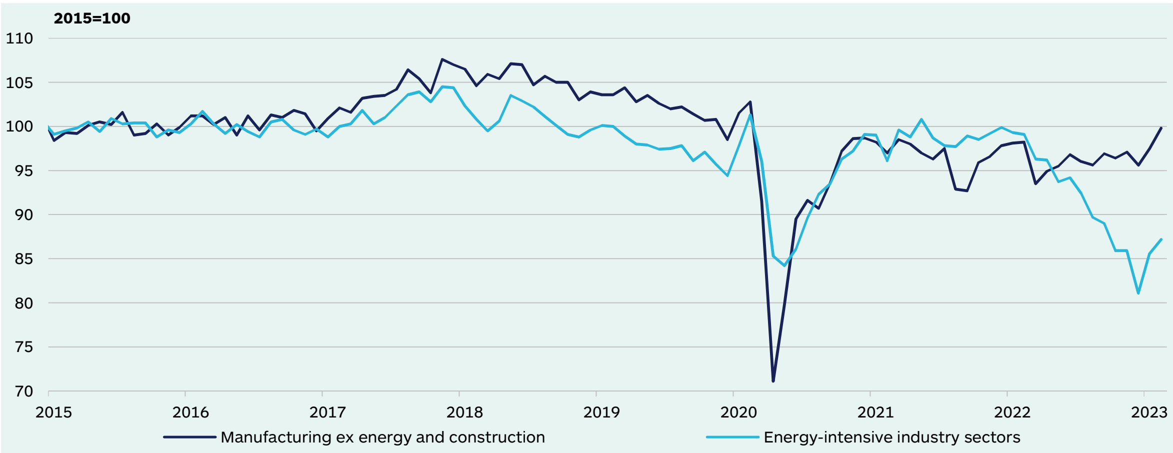
Analysts: Christian Lips, Chief Economist // Christian Reuter

GDP stagnation in Q1 – technical recession averted

The German economy made a weak start to 2023, but at least narrowly averted a technical recession. Real gross domestic product stagnated in Q1. Net exports and investment made positive contributions to growth while, on the other hand, private and public consumption registered a price-adjusted decline and slowed the German economy's development. Given gradually receding inflation, private consumption will likely recover, step by step, over the course of the year. It looks as if the marked decrease in inflation in March has already contributed to the improvement in consumer confidence of late, in which respect it is encouraging that an initial assessment suggests that the inflationary pressures somewhat unexpectedly continued to recede in April.

The hard economic data released recently had actually indicated a good start to the year. The first two months saw industrial output 3.1 percent up on the average for the preceding quarter, new orders up by 3.3 percent and orders from abroad up by no less than 5.5 percent. Construction output registered particularly strong growth in the first two months, with a quarter-on-quarter figure of +7.9 percent. At first glance this might seem surprising in light of the highly negative impacts of rising interest rates and building material costs. However, this development is likely due to the unusually mild weather rather than indicating a general revival of the construction industry. Be that as it may, the early spring upturn in the construction sector constitutes a burdening factor for Q2.

Chart: Substantial production cutbacks in energy-intensive sectors of the economy in 2022



Sources: Destatis, NORD/LB Macro Research

Output in energy-intensive sectors of the economy remains subdued

The German economy has so remained relatively unscathed by the at times dramatic surge in energy prices ensuing from Russia's invasion of Ukraine. That said, this does not apply to the particularly energy-intensive sectors, which over the past year have been very clearly decoupled from the other developments in the manufacturing sector. Output in the energy-intensive sectors (including chemicals, metal production and processing, manufacture of glass, ceramics, processing of stone and earth, production of cardboard and paper as well as coking and mineral oil processing) declined by up to 20 percent over the course of 2022, and in December slumped practically to the low registered during the global financial and economic crisis in 2009.

Production in the non-energy-intensive sectors, on the other hand, developed along significantly more stable lines, with output across the entire manufacturing sector merely suffering a relatively small damper in the spring of 2022 and subsequently being able to recover in the direction of the pre-invasion levels. This is to a large extent due to the high flexibility of Germany's industrial enterprises, which evidently adapted their supply chains very quickly to the surging energy prices.
The question as to whether the companies in the energy-intensive industries have permanently or merely temporarily scaled back their domestic production cannot yet be answered on the basis of the current data. Still, the past few months have seen energy prices fall significantly. It is an encouraging sign that there was a marked recovery in output in the energy-intensive sectors as well during the same period, with an increase of 7.5 percent since December which was significantly stronger than the 4.4 percent registered by the manufacturing industry as a whole.

Leading indicators paint a mixed picture – but overall brightening in sentiment
The leading indicators have painted a mixed picture of late. While ZEW's economic expectations fell anew in April, the same month saw the ifo Business Climate Index continue its upward trend, mainly thanks to higher business expectations. One possible explanation is that the recent market turmoil likely resonated more strongly among the financial experts surveyed by ZEW.
There is also a positive interpretation for the strongly contrasting PMI trends in recent times. While the services PMI leapt to 55.7 points and thus stands well inside the expansion zone, the industry PMI fell anew in April to 44.0 points, which would normally signal a contraction. However, this development is largely due to reduced delivery times and indicates a significant easing in supply bottlenecks – much like to other global indicators as well. In other words the glass is, in terms of the economic outlook, half full rather than half empty. For 2023 as a whole, however, we expect GDP growth of just 0.2 percent as result of the weak start to the year.

Fundamental forecasts, Germany

	2022	**2023**	**2024**
GDP	1.8	0.2	1.4
Private consumption	4.3	-0.6	1.5
Govt. consumption	1.2	0.4	2.1
Fixed investment	0.4	1.2	2.3
Exports	2.9	2.3	3.5
Imports	6.0	2.5	4.3
Net exports[1]	-1.3	0.0	-0.2
Inflation[2]	8.7	6.0	3.0
Unemployment rate[3]	5.3	5.5	5.3
Budget balance[4]	-2.6	-3.9	-2.6
Current account balance[4]	4.3	5.6	6.0

Change vs previous year as percentage, [1]as contribution to GDP growth; [2]HICP; [3]as perc. of the civil labour force (BA); [4] as perc. of GDP
Sources: Feri, NORD/LB Macro Research

Quarterly forecasts, Germany

	III/22	**IV/22**	**I/23**	**II/23**	**III/23**
GDP sa qoq	0.5	-0.5	0.0	0.4	0.4
GDP nsa yoy	1.3	0.2	0.2	0.0	-0.1
Inflation yoy	9.4	10.8	8.7	7.0	5.2

Change as percentage
Sources: Feri, NORD/LB Macro Research

Switzerland: Sentiment stable – SNB rate hike in June

Analyst: Christian Lips, Chief Economist

Economy: sentiment just slightly clouded after market turmoil – boom in the service sector

The Swiss economy has been on a positive path since the beginning of the year after the phase of GDP stagnation in the closing quarter of 2022. The manufacturing PMI fell to 47.0 points in March, but it should be noted that this was due to a shortening of delivery times, which first and foremost indicates an easing of the supply chain disruptions. Output, on the other hand, registered further slight upward movement. The momentum in the services sector was particularly strong, with the PMI business activity component averaging almost 60 points in Q1.

The KOF Economic Barometer fell slightly to 98.2 points in March, attributable to negative signals from the construction and manufacturing industries (in particular the electrical and wood industries) and the service sector. Seeing as the order situation and availability of intermediate products have improved, the biggest barriers to output lie in problems in recruiting personnel. On the other hand, positive signals came from the indicators for the export economy. April saw the KOF Economic Barometer continue its decline, dropping to 96.4 points.

The sentix economic index dropped to -1.2 points as result of a significant deterioration in future expectations. At 17.3 points, the current situation is still considered to be comparatively stable, however. All told, it can be said that the market turmoil has so far been reflected only to a very limited extent in the key sentiment indicators.

Unexpected decline in inflation pressure in March

After rising prices for electricity, tourism services and food in particular caused inflation to climb to 3.4 percent yoy in February, the price pressure already fell unexpectedly sharply in March to 2.9 percent yoy. The positive trend is likely to have continued in April according to our estimate. Developments upstream of consumer prices, too, suggest a gradual disinflationary trend, with Switzerland's Producer and Import Price Index having dropped to 2.1 percent, year on year, in March – its lowest level in almost two years.

SNB set for a further rate hike in June – Swiss franc to remain below euro parity

Nevertheless, we expect inflation to remain above the SNB's inflation target for some time to come. There is great uncertainty as to the extent of the impact of the recent tensions in the financial sector on the economy and price developments. In our baseline scenario, however, we expect an additional slight tightening of monetary policy, with a further rate hike, at least in June, and a continuation of the foreign currency sales. However, whether the SNB raises its policy rate to 2.00 percent will largely depend on the extent of any additional tightening of financing conditions as result of the market tensions. In this environment, the Swiss franc will likely remain below euro parity for the time being.

Fundamental forecasts*, Switzerland

	2022	2023	2024
GDP	2.1	0.7	1.8
Inflation (CPI)	2.8	2.7	1.3
Unemployment rate[1]	2.2	1.9	1.8
Budget balance[2]	-0.2	0.4	0.6
Current account bal.[2]	9.9	9.0	8.8

Interest and exchange rates, Switzerland

	27.04.	3M	6M	12M
SNB policy rate	1.50	1.75	2.00	2.00
3M rate	1.55	1.80	2.00	2.00
10Y	1.09	1.40	1.60	1.50
Spread 10Y Bund	-137	-110	-100	-100
EUR in CHF	0.99	0.99	0.99	1.00

* Change vs previous year as percentage; [1] as percentage of the labour force, [2] as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

Japan: Inflation needs to be kept an eye on

Analysts: Tobias Basse // Bernd Krampen

Kazuo Ueda takes over at the helm of Japan's central bank

Kazuo Ueda is now in office at the helm of the Bank of Japan as successor to Haruhiko Kuroda. The new governor was in no rush to make any great changes at the central bank's meeting in April, evidently preferring a rather cautious approach. This news comes as no great surprise. Continuity is the keyword in Tokyo, and the central bankers left the traditional key interest rate and the target yield on 10-year government bonds at their existing levels. Even so, the BoJ did not remain completely inactive. In its verbal communication, the Bank of Japan has now dispensed with clear indications in the direction of ultra-low interest rates even over the long term. Moreover, it was decided to review Japan's monetary policy strategy. This process will take up to eighteen months.

Playing for time

This shows that the central bankers in Tokyo are continuing to play for time. In our view, an upward adjustment of the traditional key rate before the completion of the central bank's monetary policy review is quite unlikely. At the press conference following the BoJ’s last meeting, however, Kazuo Ueda stressed that tweaks to Japan's monetary policy could well also be made more quickly. We are therefore maintaining our view that changes will be made to the BoJ's yield control (YCC) policy by the end of the year. However, the current signals from the central bank in Tokyo point more in the direction of merely cautious adjustments to begin with. The announcement of a complete termination of this policy is probably not to be expected before the end of 2023 at the earliest. This assessment fits well with the most recent comments by Kazuo Ueda to the effect that the YCC policy could only then be dispensed with when there is clear evidence to conclude that inflation would sustainably achieve the BoJ's target level of 2 percent. While basically positive for the yen, this news probably disappointed the FX market which had up to then banked on a more near-term end to the yield curve control measures. The Japanese currency has accordingly found itself under added pressure of late.

Inflation trend needs to be kept a close eye on

In this context the inflation trend also needs to be kept an eye on. The year-on-year rate of change in consumer prices in Tokyo rose further to +3.5 percent in April, so that the central bank has had to slightly adjust its inflation projections. While the central bankers are maintaining their conviction that the upward price movement will slow down soon, the current inflation trend nevertheless ought to dampen deflation fears and thus permit near-term adjustments to the BoJ's YCC policy.

Fundamental forecasts*, Japan

	2022	2023	2024
GDP	1.0	1.0	1.1
Inflation	2.5	2.4	1.4
Unemployment rate[1]	2.6	2.5	2.4
Budget balance[2]	-6.8	-5.3	-4.0
Current account bal.[2]	1.9	1.7	2.1

* Change vs previous year as percentage;

[1] as percentage of the labour force; [2] as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

Interest and exchange rates, Japan

	27.04.	3M	6M	12M
Key rate	-0.10	-0.10	-0.10	-0.10
3M rate	0.07	0.05	0.05	0.10
10Y	0.46	0.45	0.50	0.70
Spread 10Y Bund	-200	-205	-210	-180
EUR in JPY	148	140	138	136
USD in JPY	134	130	128	125

China: Beijing reports return to solid growth

Analysts: Tobias Basse // Bernd Krampen

Back on the growth path – at least for now!

The economic momentum in China appears to be picking up again at the start of this year: the disappointing quarter-on-quarter stagnation at 0.00 percent in Q4/2022 was followed in the opening quarter of this year by a welcome increase of 2.2 qoq and a year-on-year upsurge from 2.9 to 4.5 percent. With 2022 having seen the Chinese economy on a zig-zag growth path due to the government's zero-Covid restrictions and the ensuing second-lowest annual growth rate since the 1970s, the statisticians in Beijing found themselves able to publish encouraging growth figures again. The ending of the Covid-related constraints, the easing of domestic supply bottlenecks and solid global economic demand were contributory factors in this context. The other indicators for March were also more encouraging, with industrial output registering solid growth of 3.9 percent yoy while retail sales indeed surprised on the upside with an even more marked year-on-year upsurge of 10.6 percent. That said, the slight easing of the restrictions on lending appears to be helping the real estate market and construction investment only in part and to a very moderate extent.

Sentiment surveys indicate continuation of this tendency in the months ahead

The overall improved tendencies had already been indicated by the forward-looking business surveys, which documented fresh optimism just in time for spring: the values registered by the CFLP and Caixin indices for the manufacturing industry rose to 51.9 and 50.0 points respectively. However, the actual reason for the pick-up in economic activity lies in the markedly improved situation in the services sector, for which the two surveys registered results of 58.2 and 57.8 points respectively – after levels well below the expansion threshold of 50 points in winter. The revival can be expected to continue for the time being. Government measures and the economy's stabilization have made for a slight easing of the risks in – and thus some breathing space for – the real estate market.

Fiscal and monetary policymakers prepared for intervention – but can hold back for now

The fiscal policymakers are likely inclined to favour pulling out a couple more stops. The policymakers on the monetary side prefer merely to ensure sufficient liquidity on the money market, although the PBoC could have more leeway in light of the unexpectedly more pronounced disinflationary trend of late. China's gradual population shrinkage , its dependence on raw materials and technology as well as the international concerns as to the country's military intentions will have a braking effect on the economy in the long term: private investment in the Middle Kingdom will certainly be questioned more critically. Depending on the severity of the feared weakening of its main customer regions North America and Europe, China too will feel the effects of this in the second half of 2023. The prospects of steady US interest rates in the near term stabilized the US dollar at 6.90 CNY.

Fundamental forecasts*, China

	2022	2023	2024
GDP	3.0	5.5	5.0
Inflation	1.9	2.2	2.3
Unemployment rate[1]	4.4	4.1	4.1
Budget balance[2]	-7.5	-4.9	-4.6
Current account bal.[2]	2.2	1.4	1.1

* Change vs previous year as percentage

[1] as percentage of the labour force; [2] as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

Interest and exchange rates, China

	27.04.	3M	6M	12M
Deposit rate	1.50	1.50	1.50	1.50
3M SHIBOR	2.43	2.50	2.40	2.20
10Y	2.79	2.90	2.80	2.60
Spread 10Y Bund	33	40	20	10
EUR in CNY	7.64	7.34	7.13	7.09
USD in CNY	6.92	6.80	6.60	6.50

Britain: Central bank needs to stay on the ball

Analysts: Tobias Basse // Bernd Krampen

Inflation remains a problem

March as month under review saw Britain's rate of inflation fall just slightly, from 10.4 to 10.1 percent year-on-year. The declining fuel prices played a particularly helpful role in this development. Many observers (and probably the Bank of England as well) had expected somewhat more movement. Moreover, the core rate remained unchanged compared to February, at 6.2 percent yoy. Here, too, the majority of interested market participants had probably hoped for a clearer signal in the direction of diminishing inflation problems. Thus, the macroeconomic price environment clearly remains a problem for monetary policymakers in London for the time being.

The Bank of England needs to stay on the ball

Indeed, the Bank of England will have to stay on the ball for now in light of these figures. Recent comments by high-ranking central bankers also show that at least some officials appear to be more concerned about excessively generous wage settlements. This environment has prompted us to adjust our forecasts to the effect that we now expect a further Bank Rate hike of 25bp in the very near term. This, however, will likely have no great implications in terms of the capital market rate levels in the UK.

Inflation and toothpaste – Karl Otto Pöhl's insight revisited!

Having at least not remained behind the expectations among the majority of the interested observers, the current economic trend ought to permit corresponding action on the part of the Bank of England. Nevertheless, there will certainly be controversial discussions among the members of the BoE's Monetary Policy Committee as to the necessity of a further Bank Rate hike, so a unanimous decision on the future course of Britain’s interest rate policy is again unlikely to be possible. In a recent panel discussion in Washington, MPC member Silvana Tenreyro said that interest rate rises take time to have an impact on the economy, and stressed the need for more patience among the central banks. She can therefore be expected to vote against the imminent renewed rate hike – and it could well be that she will not be alone in doing so. That said, the majority of the central bankers in London currently appear to be more concerned that in the absence of further monetary policy action by the Bank of England inflation expectations among private economic entities could stabilize at a worryingly high level. In this context an insight on the part of the former Bundesbank president Karl Otto Pöhl could well be of significant relevance. He had famously emphasized that inflation is like toothpaste – once it's out of the tube, you can hardly get it back in again!

Fundamental forecasts*, Britain

	2022	2023	2024
GDP	4.1	-0.2	0.9
Inflation (CPI)	9.1	6.5	2.4
Unemployment rate[1]	3.7	4.2	4.4
Budget balance[2]	-6.4	-5.3	-3.7
Current account bal.[2]	-3.8	-3.8	-3.5

* Change vs previous year as percentage

Interest and exchange rates, Britain

	27.04.	3M	6M	12M
Repo rate	4.25	4.50	4.50	4.50
3M rate	4.61	4.60	4.50	4.40
10Y	3.79	3.50	3.30	3.20
Spread 10Y Bund	133	100	70	70
EUR in GBP	0.88	0.88	0.87	0.86
GBP in USD	1.25	1.23	1.24	1.27

[1] as percentage of the labour force as per ILO concept; [2] as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

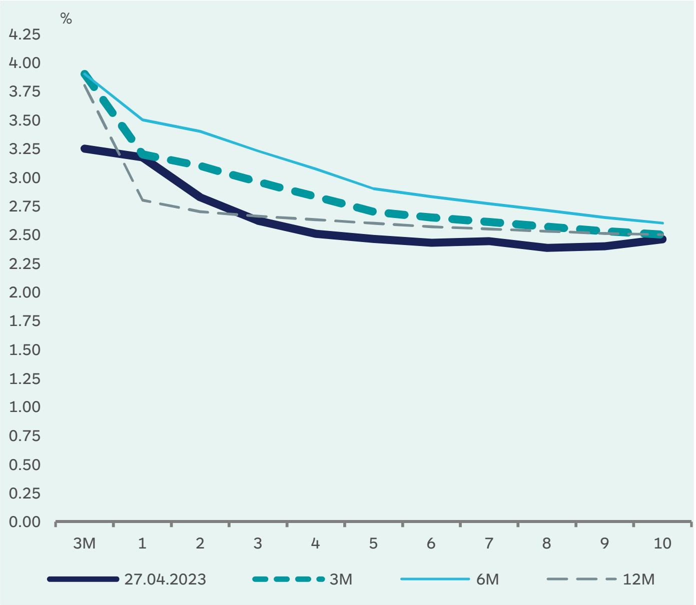
Portfolio strategies
Yield curve, Euroland

Yields and forecasts (Bunds/Swap)

	Yields (in %)	NORD/LB forecasts for horizons		
	27.04.2023	**3M**	**6M**	**12M**
3M	3.25	3.90	3.90	3.80
1Y	3.18	3.20	3.50	2.80
2Y	2.83	3.10	3.40	2.70
3Y	2.62	2.96	3.23	2.66
4Y	2.51	2.83	3.07	2.63
5Y	2.46	2.70	2.90	2.60
6Y	2.43	2.65	2.83	2.57
7Y	2.44	2.61	2.77	2.55
8Y	2.39	2.57	2.71	2.53
9Y	2.40	2.53	2.65	2.51
10Y	2.46	2.50	2.60	2.50
2Y (Swap)	3.56	3.75	4.00	3.25
5Y (Swap)	3.17	3.35	3.50	3.15
10Y (Swap)	3.10	3.15	3.20	3.05

Sources: Bloomberg, NORD/LB Macro Research

Yield curve forecasts (Bunds)



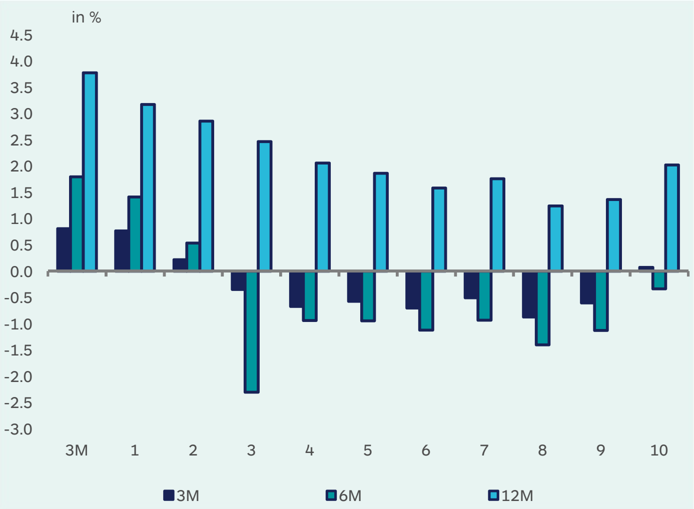
Sources: Bloomberg, NORD/LB Macro Research

Forecasts and total returns

	Total returns (in %) for horizons...		
	3M	**6M**	**12M**
3M	0.81	1.80	3.78
1Y	0.77	1.42	3.17
2Y	0.22	0.54	2.86
3Y	-0.35	-2.30	2.47
4Y	-0.67	-0.94	2.06
5Y	-0.58	-0.95	1.86
6Y	-0.70	-1.12	1.58
7Y	-0.51	-0.93	1.76
8Y	-0.87	-1.40	1.25
9Y	-0.60	-1.13	1.37
10Y	0.07	-0.33	2.02

Sources: Bloomberg, NORD/LB Macro Research

Expected total returns



Sources: Bloomberg, NORD/LB Macro Research

A total return is the absolute profit from an investment in the time period under consideration, with account being taken of the pro-rata yields plus the price gains or losses to be anticipated on the basis of the forecast yield curve change.

Portfolio strategies International yield curve: 3-month & 12-month horizons

3-month horizon

Expected total returns (as percentage) in euro

	EUR	USD	GBP	JPY	CHF
1Y	0.8	3.2	1.5	5.4	-0.2
2Y	0.2	2.1	1.4	5.4	-0.7
3Y	-0.3	1.5	1.6	5.3	-0.9
4Y	-0.7	1.6	1.6	5.2	-1.2
5Y	-0.6	1.9	1.5	5.3	-1.5
6Y	-0.7	5.1	2.4	5.2	-2.0
7Y	-0.5	2.1	1.8	5.2	-2.2
8Y	-0.9	2.1	2.4	5.3	-2.5
9Y	-0.6	2.3	2.2	5.0	-2.9
10Y	0.1	2.5	3.2	5.2	-2.9

Sources: Bloomberg, NORD/LB Macro Research

Expected total returns (as percentage) in national currencies

	USD	GBP	JPY	CHF
1Y	1.0	1.2	-0.1	0.1
2Y	0.0	1.1	-0.3	-0.6
3Y	-0.6	1.3	-0.3	-0.6
4Y	-0.5	1.3	-0.3	-0.8
5Y	-0.2	1.3	-0.2	-1.1
6Y	2.9	2.1	-0.4	-1.6
7Y	0.0	1.5	-0.3	-1.8
8Y	0.0	2.1	-0.3	-2.1
9Y	0.2	1.9	-0.5	-2.6
10Y	0.3	2.9	-0.4	-2.5

Sources: Bloomberg, NORD/LB Macro Research

12-month horizon

Expected total returns (as percentage) in euro

	EUR	USD	GBP	JPY	CHF
1Y	3.2	5.9	7.0	8.5	-0.1
2Y	2.9	4.9	6.5	8.5	-0.6
3Y	2.5	4.3	7.6	8.5	-1.0
4Y	2.1	4.1	7.9	8.4	-1.3
5Y	1.9	4.4	8.1	8.5	-1.8
6Y	1.6	8.2	9.3	8.2	-2.3
7Y	1.8	5.1	9.0	8.0	-2.7
8Y	1.2	5.2	9.9	7.8	-3.0
9Y	1.4	5.3	9.6	7.2	-3.5
10Y	2.0	5.8	10.9	7.0	-3.5

Sources: Bloomberg, NORD/LB Macro Research

Expected total returns (as percentage) in national currencies

	USD	GBP	JPY	CHF
1Y	4.7	4.3	-0.1	1.3
2Y	3.6	3.8	-0.1	0.8
3Y	3.1	4.8	-0.1	0.4
4Y	2.9	5.2	-0.2	0.0
5Y	3.2	5.4	-0.2	-0.4
6Y	7.0	6.6	-0.5	-1.0
7Y	3.9	6.3	-0.6	-1.3
8Y	4.0	7.1	-0.8	-1.6
9Y	4.1	6.8	-1.4	-2.2
10Y	4.6	8.1	-1.6	-2.2

Sources: Bloomberg, NORD/LB Macro Research

A total return is the absolute profit from an investment in the time period under consideration, with account being taken of the pro-rata yields plus the price gains or losses to be anticipated on the basis of the forecast yield curve and exchange rate change.

Portfolio strategies
Stock market strategy; 3-month, 6-month & 12-month horizons

Levels and performance

Index	Level as at	Status		Performance since	
	27.04.2023	**Prev. month**	**Start of year**	**Prev. month**	**Start of year**
DAX	15,800.45	15,628.84	13,923.59	1.10%	13.48%
MDAX	27,608.19	27,662.94	25,117.57	-0.20%	9.92%
EuroSTOXX50	4,358.05	4,315.05	3,793.62	1.00%	14.88%
STOXX50	4,029.96	3,941.10	3,651.83	2.25%	10.35%
STOXX600	464.03	457.84	424.89	1.35%	9.21%
Dow Jones	33,826.16	33,274.15	33,147.25	0.08%	0.47%
S&P 500	4,135.35	4,109.31	3,839.50	-1.30%	5.64%
Nikkei	28,457.68	28,041.48	26,094.50	1.48%	9.06%

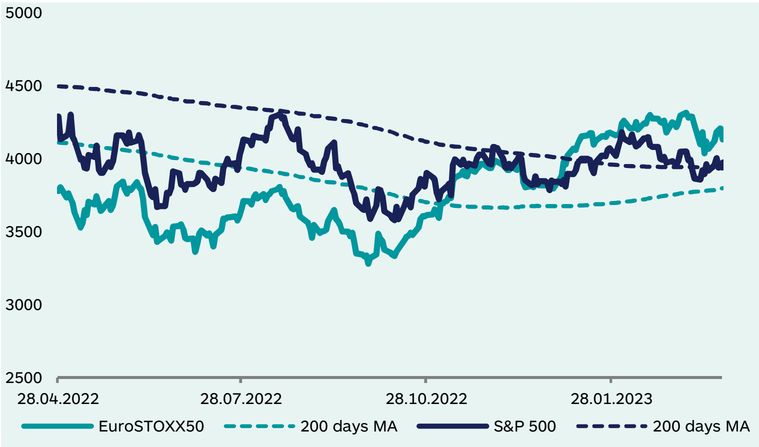
Sources: Bloomberg, NORD/LB Macro Research

Index forecasts

Index	NORD/LB forecast for horizons ...		
	3M	**6M**	**12M**
DAX	15,200	15,900	16,500
MDAX	26,300	27,600	29,000
EuroSTOXX50	4,100	4,300	4,500
STOXX50	3,825	4,000	4,175
STOXX600	435	460	480
Dow Jones	32,500	33,750	35,000
S&P 500	3,950	4,100	4,250
Nikkei	27,500	28,000	29,500

Sources: Bloomberg, NORD/LB Macro Research

EuroSTOXX50 and S&P500



Sources: Bloomberg, NORD/LB Macro Research

Date of going to press for data, forecasts and texts was **Friday, 28 April 2023.**
The next English issue of Economic Adviser will be appearing on **29 May 2023**.

Overview of forecasts

Fundamental forecasts

in %	GDP growth			Rate of inflation			Unemployment rate[1]			Budgetary balance[2]		
	2022	2023	2024	2022	2023	2024	2022	2023	2024	2022	2023	2024
USA	2.1	1.1	1.2	8.0	3.9	2.4	3.6	3.8	4.0	-4.1	-3.7	-3.7
Euroland	3.5	1.0	1.7	8.4	5.7	2.9	6.7	6.7	6.7	-3.6	-3.3	-2.6
Germany	1.8	0.2	1.4	8.7	6.0	3.0	5.3	5.5	5.3	-2.6	-3.9	-2.6
Japan	1.0	1.0	1.1	2.5	2.4	1.4	2.6	2.5	2.4	-6.8	-5.3	-4.0
Britain	4.1	-0.2	0.9	9.1	6.5	2.4	3.7	4.2	4.4	-6.4	-5.3	-3.7
Switzerland	2.1	0.7	1.8	2.8	2.7	1.3	2.2	1.9	1.8	-0.2	0.4	0.6
China	3.0	5.5	5.0	1.9	2.2	2.3	4.0	4.1	4.1	-7.5	-4.9	-4.6

Change vs previous year as percentage; [1] as percentage of the labour force (Germany: as per Federal Employment Office definition); [2] as percentage of GDP
Sources: Feri, NORD/LB Macro Research

Key rates

In %	27.04.23	3M	6M	12M
USD	5.00	5.25	5.25	5.00
EUR	3.50	4.25	4.25	4.25
JPY	-0.10	-0.10	-0.10	-0.10
GBP	4.25	4.50	4.50	4.50
CHF	1.50	1.75	2.00	2.00
CNY	1.50	1.50	1.50	1.50

Sources: Bloomberg, NORD/LB Macro Research

Exchange rates

EUR in...	27.04.23	3M	6M	12M
USD	1.10	1.08	1.08	1.09
JPY	148	140	138	136
GBP	0.88	0.88	0.87	0.86
CHF	0.99	0.99	0.99	1.00
CNY	7.64	7.34	7.13	7.09

Interest rates (government bonds)

	3M rates				Yields 2Y				Yields 5Y				Yields 10Y			
	27.04.	3M	6M	12M	27.04.	3M	6M	12M	27.04.	3M	6M	12M	27.04.	3M	6M	12M
USD	5.30	5.10	5.10	4.70	4.07	4.50	4.40	4.00	3.59	3.70	3.60	3.40	3.52	3.50	3.40	3.30
EUR	3.25	3.90	3.90	3.80	2.83	3.10	3.40	2.70	2.46	2.70	2.90	2.60	2.46	2.50	2.60	2.50
JPY	0.07	0.05	0.05	0.10	-0.05	0.00	0.00	0.00	0.14	0.17	0.19	0.26	0.46	0.45	0.50	**0.70**
GBP	4.61	4.60	4.50	4.40	3.82	3.60	3.40	3.20	3.67	3.56	3.36	3.20	3.79	3.50	3.30	3.20
CHF	1.55	1.80	2.00	2.00	1.06	1.30	1.60	1.30	1.02	1.30	1.60	1.40	1.09	1.40	1.60	1.50

Sources: Bloomberg, NORD/LB Macro Research

Spreads (bp)

	3M EURIBOR				2Y Bunds				5Y Bunds				10Y Bunds			
	27.04.	3M	6M	12M	27.04.	3M	6M	12M	27.04.	3M	6M	12M	27.04.	3M	6M	12M
USD	205	120	120	90	124	140	100	130	113	100	70	80	106	100	80	80
JPY	-318	-385	-385	-370	-287	-310	-340	-270	-232	-253	-271	-234	-200	-205	-210	-180
GBP	136	70	60	60	99	50	0	50	120	86	46	60	133	100	70	70
CHF	-170	-210	-190	-180	-177	-180	-180	-140	-144	-140	-130	-120	-137	-110	-100	-100

Sources: Bloomberg, NORD/LB Macro Research

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Time of going to press:
Tuesday, 02 May 2023 4:06 PM CET