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Special: Long-term impacts of climate change on economic growth and inflation

Analysts: Valentin Jansen // Constantin Lürer

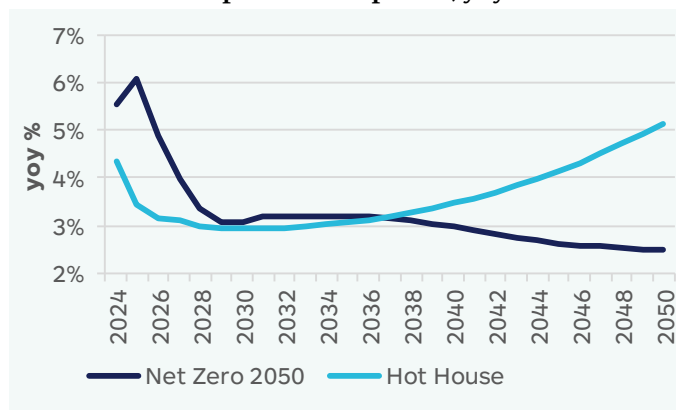
Sobering COP28 stocktake: same goal, less time!

The discussion on how to deal with the global consequences of climate change is becoming increasingly prevalent, not only in private but also and above all in state forums. One of the most important of these is undoubtedly the annual UN climate conference entitled "Conference of Parties" (COP), the 28th edition of which took place last December. In preparation for the conference, a "global stocktake" was conducted for the first time, within the framework of which the progress in the implementation of the Paris climate goals was the focus of critical evaluation. The result is not exactly a surprise on the upside. Too little has happened across all areas of activity, from the reduction of CO₂ emissions to the strengthening of resilience to climate change, right through to the provision of financial and technological support to countries that are particularly vulnerable to the impacts of climate change. The résumé of COP28 therefore focuses primarily on progress-accelerating measures for implementation by 2030, for example in the key area of transition. Specifically, a tripling of capacities in the area of renewable energies by 2030 is intended to make for a certain degree of compensation of the identified shortcomings. The global stocktaking is based on the work of the "Network of Central Banks and Supervisors for Greening the Financial System" (NGFS), which is regarded as fundamentally consensual in the ESG context. The NGFS constantly develops scenarios that, from the current starting point, sketch out possible development paths depending on the current or rather future success in climate change mitigation.

NGFS scenario landscape: from net zero to status quo

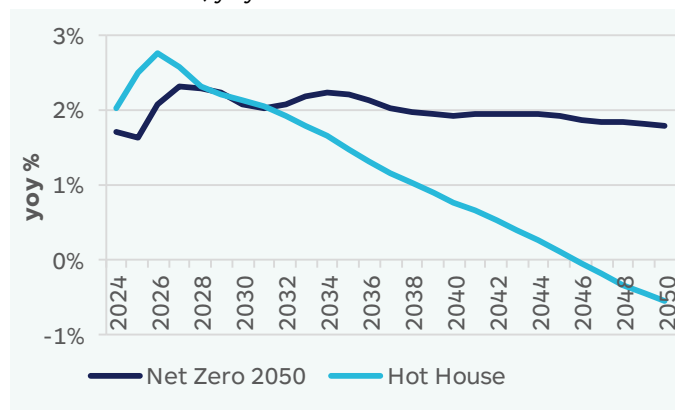
Starting out from the current baseline situation, the NGFS is currently mapping out seven scenarios. These differ in varying degrees of transition risks (negative effects due to the transition to a low-carbon economy) and the physical effects of rising average temperatures, for example extreme weather events or rising sea levels. They are based on socio-economic assumptions and trends, climate system development paths, technological developments and political measures. Owing to their diametrical development paths, the two scenarios "Net Zero 2050" and "Current Policies" are particularly relevant. The former assumes net zero CO₂ emissions by 2050 (limitation of average global warming to 1.4°C). To this end, adequate climate policy measures must be implemented without delay and decarbonization also needs to be accelerated. The physical risks, which show clear effects in the course of the 2030s, are the lowest in this case, while transition risks have the strongest impact on the economy in the short term. The contrasting Current Policies scenario assumes that the status quo of current global climate policy will be maintained until 2060. Following this path, the CO₂ emissions peak would not be reached until 2080 and an average global warming level of about 3°C would be in place as early as mid-century. These climate changes are irreversible, with effects such as sharply rising sea levels. This is where the physical risks are highest in the NGFS scenario landscape, while the transition risk is the lowest (no low-carbon realignment of the global economy). While the "Net Zero 2050" scenario is assigned to the superordinate category "Orderly", the 3°C scenario falls under the "Hot house world" category. The other five scenarios basically differ in terms of the effectiveness and speed of economic transformation, alongside political effectiveness.

Global consumer price development, yoy



Sources: Oxford Economics, NORD/LB Research

Global real GDP, yoy



Impacts of climate change on economic growth and inflation

The NGFS scenarios are generally regarded as a consensual working basis, and are used and further developed for more extensive macroeconomic analyses. CO₂ prices are a key lever in this context. In the Net Zero 2050 scenario it can, for example, be assumed that politically driven CO₂ price increases will prompt a sensitive reaction from, in particular, those inflation measurement components that are still strongly based on fossil fuels. This effect will likely diminish with the decreasing significance and use of fossil fuels. Thus, there is likely to be an increased price surge in the short and medium term, particularly in countries intensively using fossil fuels for energy, affecting them more severely than others. In the long term, however, the upward price pressures will decrease as the economy's transition progresses, and return to lowest inflation trajectory within the recognized climate scenarios. In contrast, supply shocks make for massive increases in terms of production factors and food prices if there is no reduction in CO₂ emissions whatsoever and global average temperatures rise by about 3°C. As regards GDP, the inflation upswing within the Net Zero 2050 framework reduces real economic output at the beginning of the forecast period. Towards mid-century, this effect diminishes and the productivity-related benefits of high investment activity become evident. In the Hot house scenario, the economic damage resulting from physical and chronic climate damage – such as the destruction of habitat, production areas and work productivity – becomes increasingly evident. In addition to impacts on economic growth and inflation, the scenarios also imply country-specific increases in the risk premiums of financing instruments – a development that would, in turn, bring additional actors into play within the framework of monetary policy reactions.

"Green Monetary Policy": ECB takes a pioneering role, the Fed focuses on its mandate

Central banks, too, can no longer avoid addressing the relationship between climate change and price stability within the scope of their mandate. The ECB has recognized the significance of climate change in relation to price stability, and now takes account of climate change mitigation considerations in its monetary policy framework – even if not all members of the ECB Executive Board are pulling in the same direction. The measures already implemented include the EU-wide climate stress test in risk management and the aim of aligning the Eurosystem's carbon footprint with the Paris climate protection goals. In contrast to the ECB, the US Federal Reserve is taking a more cautious stance – under the motto that the central bankers are not "climate politicians". Fed Chairman Jerome Powell sees his task primarily in fulfilling the dual mandate in terms of price stability and a healthy labour market. Nevertheless, the Fed, too, is increasingly taking climate risks into account and giving supervised financial institutions structured sets of guidelines on how potential risk exposures can be managed.

USA: Labour market data remain a grab bag of surprises

Analysts: Tobias Basse // Constantin Lüer

Labour market data from the USA continue to surprise

The recently reported US labour market data remain a veritable grab bag of surprises for market participants. This is reflected in the fact that while the preliminary data reported on non-farm payroll growth – expressed in concrete figures, 275,000 new jobs – in February as month under review were unexpectedly pleasing, there was at the same time a downward revision of the figures reported for January. The latter news ought not to have made for any great amazement, however. In addition, the official US statisticians reported an upturn in the separately calculated unemployment rate to 3.9 percent for February. The data on wage growth rather surprised on the downside, too, with an increase of just 0.1 percent mom in February. Against this background, optimists and pessimists alike thus find confirmation in the current figures to bolster their respective assessments regarding the state of the US economy. That said, it nevertheless has to be emphasized that the employment situation in the United States can still be described as rather positive. In this context, attention should also be paid to the annual rate of development in hourly wages; at 4.3 percent, this is markedly outpacing the rise in consumer prices at the present time, which should give households additional scope for more consumption, at least in the short term. The prospects are therefore not (yet?) unfriendly.

Chart: US interest rates



Sources: Macrobond, NORD/LB Macro Research

The economic environment remains difficult for the FOMC to interpret

The situation on the US labour market thus remains rather pleasing for now. Moreover, it now looks as if the mood in the US real estate industry is steadily improving. Generally a very reliable leading indicator for the development of real estate prices, the NAHB Housing Market Index rose to 51 points in March. This signals a preponderance of optimistic feedback again. Furthermore, the latest US price data have provided no indication of the easing tendencies coming to an end. Given this environment, the Fed ought not to feel any great urge to take action for the time being. Though an appreciable slowdown in economic growth in the USA is still to be reckoned with, the currently very high degree of uncertainty regarding further trends ought to nevertheless prompt the US central bankers to continue taking a cautious approach for the time being, as was the case in their last meeting in March.

The Fed pauses – but the decision has positive side effects

It could be said that the Fed is in a comfortable position. Tighter monetary policy as a result of fighting inflation typically puts pressure on the labour market; however, as already noted, the labour market is proving quite robust. The Fed can therefore afford to avoid rushing ahead too aggressively, and instead can carefully assess the situation before taking calm and appropriate action. For example, after its most recent meeting in March, the FOMC decided to hold its key rate at the 5.25 - 5.50 percent band. This had been widely expected. Of particular interest to the capital markets this time were the central bankers' individual projections – the so-called "dot plots" – which are only updated four times a year. These were given an update in the course of last week's decision announcement, and can be interpreted such that, on average, there could be three rate cuts over the course of this year. It goes without saying that this figure is not set in stone, however, and that this viewpoint is not shared by all central bankers. Indeed, two of the 19 FOMC members actually expect no rate cut this year, and another two anticipate just one downward adjustment. It is therefore essential to at all times take account of the fact that the opinions among the FOMC's members are in a state of flux and can change from time to time in line with fresh economic findings. However, it is not the case that the US economy is free of problematic issues. The commercial real estate sector is likely to be most pleased about falling interest rates.

Fundamental forecasts, USA

	2023	2024	2025
GDP	2.5	1.8	1.9
Private consumption	2.2	1.6	1.5
Govt. consumption	2.7	1.9	1.1
Fixed investment	2.0	1.8	2.6
Exports	2.7	1.6	2.6
Imports	-1.6	1.2	2.2
Inflation	4.1	2.7	2.3
Unemployment rate ¹	3.6	4.1	4.2
Budget balance ²	-6.5	-6.0	-6.2
Current acct. balance ²	-3.0	-3.1	-3.0

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

	II/23	III/23	IV/23	I/24	II/24
GDP qoq ann.	7.0	4.9	3.2	0.8	0.0
GDP yoy	2.4	2.9	3.1	2.2	1.0
Inflation yoy	4.0	3.5	3.2	0.0	3.0

Change as percentage

Sources: Feri, NORD/LB Macro Research

Interest and exchange rates, USA

	21.03.	3M	6M	12M
Fed funds target rate	5.50	5.50	5.25	5.00
3M rate	5.32	5.20	5.00	4.70
10Y Treasuries	4.27	3.90	3.70	3.50
Spread 10Y Bund	186	160	150	130
EUR in USD	1.09	1.06	1.07	1.08

Sources: Bloomberg, NORD/LB Macro Research

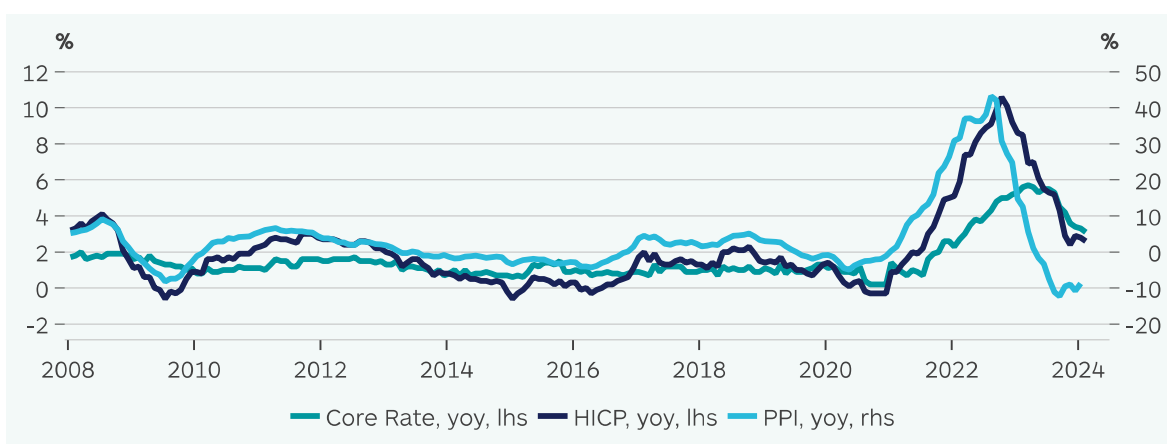
Euroland: ECB heading towards a first rate cut in June

Analysts: Christian Lips, Chief Economist // Christian Reuter

Disinflation trend continues – distortions in March and April will complicate interpretation

The downward inflation trend remains ongoing in the eurozone. February saw the annual HICP rate fall to 2.6 percent yoy. The core rate remains slightly higher than that, at 3.1 percent yoy, but likewise lower than in January. The decline in energy prices continues to have a dampening effect, even though the annual rate stands at just -3.7 percent yoy after previously -6.1 percent yoy. As the relieving base effects fade out, the focus is increasingly shifting towards underlying inflation. Given the persistently high price dynamics in services (+4.0 percent yoy), an all-clear cannot yet be given. That said, some price increases of late were of a one-off nature, for which reason the momentum here too can be expected to soon point downwards. Due to the timing of the Easter holidays this year and corresponding distortions, however, the data in March and April will make interpretation difficult. Another good reason for the ECB to wait a bit longer before starting to lower interest rates.

Chart: Disinflationary trend continues – timing of the Easter holidays distorts annual rate



Sources: Eurostat, Macrobond, NORD/LB Macro Research

ECB prepares for an initial rate cut in June – renewed “dovish” adjustment of projections

The ECB remains clearly on track for an initial rate cut in June. March saw no major surprises in terms of monetary policy decisions. This also applies to the lowering of projections, as many economists had already pointed out the need for adjustment in advance. The ECB lowered its growth forecast for 2024 to 0.6 percent, but sees the two following years in a quite optimistic light (+1.5 and +1.6 percent respectively). At 2.3 percent, the inflation rate in 2024 is now expected to be significantly lower than had been expected in December, besides which the central bankers expect a return to the inflation target of 2.0 percent in 2025, followed by 1.9 percent in 2026.

Much like the devil with holy water, the ECB's Governing Council still steers clear of any explicit pre-determination of the future interest rate path. Mainly in light of the even more persistent domestic price pressure currently prevailing, the Council is not looking to give any further guidance, but instead continues to emphasize the data-dependent approach. This cautious stance is due to the relatively high rate of nominal wage growth in the eurozone and the associated concerns as to second-round effects. Christine Lagarde pointed out that the decisions were taken unanimously. She added that rate cuts had not been discussed at the Governing Council's meeting in March, and that the members had instead only just begun to discuss dialling back the ECB's restrictive stance. This cautious communication is the preparation for the preparation in April, and is easy to translate: the central bankers are still playing for time. Despite the recent progress, inflation has not yet been defeated, especially since domestic price pressure is still too high. In this respect, the ECB is waiting for the next wage data, with the

recent strikes being symbolic of the new balance of power on the labour market. Overall, however, there are growing indications of an initial rate cut by the ECB in June, however.

As regards to the pace of adjustment after a first rate cut, there is still a lot to be said for a gradual approach. While not wishing to commit herself in this respect, Christine Lagarde always points out that it is a matter of "normalization". The projected growth rates for 2025 and 2026 above its trend restrict the potential for lowering interest rates as well, in light of which the Governing Council will more likely aim for a neutral orientation of its monetary policy. We continue to see an initial rate cut in June and a total of four downward adjustments this year as the most likely scenario.

New monetary policy framework changes little for the time being

Moreover, the ECB answered structural questions concerning monetary policy in March. First, the deposit rate will remain the relevant key rate. The spread to the rate for main refinancing operations will be narrowed from 50 to 15 basis points starting in September – and this will be done by technically lowering the mro rate (and in tow the marginal lending rate) by 35 basis points. Apart from this technical adjustment of the key-rate band, there is no need for any changes to our interest rate forecast in this respect. The ECB also aims to provide longer-term liquidity and build up a structural portfolio of securities over the medium term. The council has not yet presented any details, however.

Ultimately, in the current environment of falling, but still very high excess liquidity for the foreseeable future, the floor system will remain in place over the near term, with money market rates anchored to the deposit facility rate. In the medium term, the money market rates could be allowed somewhat more leeway again (demand-driven), but the central bankers have not yet ventured more than a "soft corridor system" with a few basis points of additional volatility – and that also only in the medium term.

Fundamental forecasts, Euroland

	2023	2024	2025
GDP	0.5	0.5	1.4
Private consumption	0.6	1.1	1.6
Govt. consumption	0.7	1.3	0.7
Fixed investment	1.4	1.0	2.6
Net exports ¹	0.2	-0.4	-0.1
Inflation	5.4	2.2	2.0
Unemployment rate ²	6.5	6.4	6.3
Budget balance ³	-3.2	-2.8	-2.6
Current account balance ³	1.9	1.9	1.7

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

	II/23	III/23	IV/23	I/24	II/24
GDP sa qoq	0.1	-0.1	0.0	0.1	0.2
GDP sa yoy	0.6	0.1	0.1	0.1	0.2
Inflation yoy	6.2	5.0	2.7	2.8	2.3

Change as percentage

Sources: Feri, NORD/LB Macro Research

Interest rates, Euroland

	21.03.	3M	6M	12M
Repo rate ECB	4.50	4.25	3.65	2.90
3M rate	3.93	3.70	3.30	2.70
10Y Bund	2.41	2.30	2.20	2.20

Sources: Bloomberg, NORD/LB Macro Research

Germany: Economy to remain weak for now

Analysts: Christian Lips, Chief Economist // Valentin Jansen

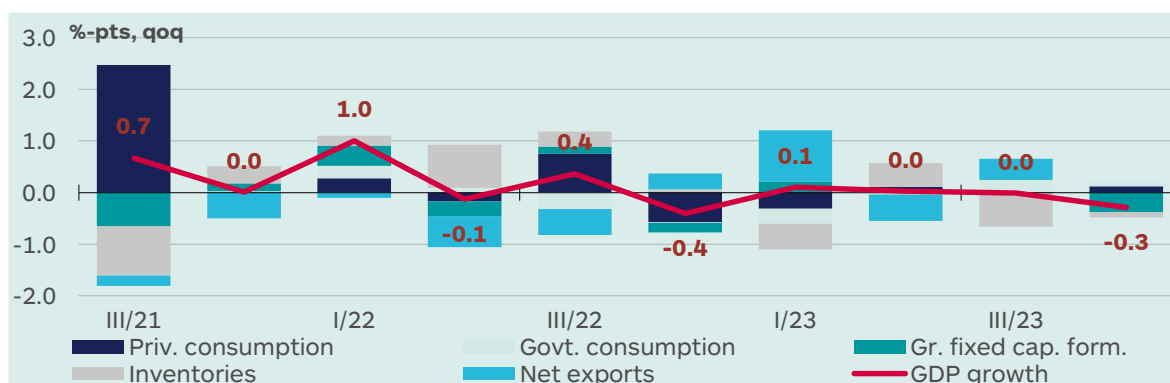
Economic indicators paint a mixed picture – slight GDP decline expected for Q1 as well

Germany has been in a state of economic weakness for almost two years, and this will remain the case for now. The economic policy uncertainty remains heightened, in both historical and international comparison. Along with tighter financing conditions, this is increasingly weighing on the investment climate. Indeed, there had already been a significant downturn in investment back in Q4/2023. Besides the construction investments that have been under pressure for some time, investments in machinery and equipment were now also more severely hit. The minimal growth contributions from consumption were insufficient to compensate for these burdens; real GDP, seasonally and calendar adjusted, contracted by 0.3 percent qoq (see chart).

As measured by the hard economic indicators, the start into 2024 was modest. While January as month under review saw industrial output register appreciable growth for the first time since February 2023, with a figure of +1.0 percent mom, the construction industry's month-on-month upsurge of 2.7 percent is largely to be seen in relation to December's weather-induced slump (-3.1 percent mom). Three trends are particularly worthy of note where the manufacturing sector (+1.1 percent mom) is concerned: first, the overall increase was solely accounted for by the main groups of consumer and intermediate goods (+4.0 percent and +4.4 percent mom respectively), while output in capital goods declined once again (-2.1 percent mom). Second, after a lengthy period of time the energy-intensive industries were at last able to register a more substantial upturn in their output (+2.8 percent mom) again, though overall output remains well short of the levels reported in early 2022. And third, the downturn in vehicle construction accelerated once again in January (-7.3 percent mom), contrasting to the general trend and indeed making for a double-digit decline of -11.7 percent in year-on-year comparison.

The previous month's upsurge in order intake due to a wave of large-scale orders was considerably corrected (-11.3 percent mom). And real retail sales started the year with their third month-on-month decline in a row. All in all, therefore, Q1 will likely have seen a slight contraction in GDP again.

Chart: Contributions to GDP growth (real, swda)



Sources: Destatis, Feri, NORD/LB Macro Research

Downward inflation trend continues – Easter-related distortion of March and April data

Inflation continued its downward trend in February as expected, with the annual rate of the national CPI standing at 2.5 percent and the HICP slightly higher at 2.7 percent yoy. The slight year-on-year decline in energy prices (-2.4 percent yoy) continues to have a dampening effect – despite the higher CO₂ price in place since January and the simultaneous removal of the energy price brakes. Moreover, the downward trend in food prices continued. As regards the two coming months under review, account

should be taken of the fact that the early timing of Easter this year will make for considerable distortions in the annual rate. Especially the movable Easter season, and consequently the Easter holidays as well, often make interpreting the inflation rate difficult in spring. The traditional "Easter effect" is now likely to fully kick in in March rather than April, particularly in the case of package holiday and fuel prices. This means we can expect the rate of inflation to rise in March slightly, followed by a disproportionate decline in April. From May onward, the levels will then be free of distortion again, and can be expected to confirm a continuation of the disinflationary trend as against February.

Marked improvement in the ifo Business Climate Index fuels hopes of recovery

The latest data from the sentiment indicators fuel hopes of an imminent economic recovery, with, for example, ZEW's economic expectations improving significantly to 31.7 points in March. The ifo Business Climate Index's strong upsurge to 87.8 points in March came as a big surprise on the upside. This key leading indicator for Germany's economic development last registered a higher level in June 2023. The expectations component improved by more than three index points to 87.5 points and, at 88.1 points, the current business situation was also rated as having significantly improved. The upswing in sentiment is broadly endorsed by all sectors under review.

After many negative reports that had severely impacted sentiment in recent months, there has been some positive news for the German economy of late. For example, there are signs of an agreement in the long-running labour dispute between Deutsche Bahn and the German Train Drivers' Union (GDL), thus averting any further strikes for now. Moreover, the economic activities in key foreign markets appear to be running better than expected, which ought to boost export business. The Federal Council's approval of the Growth Opportunities Act involving billions of euros in relief for the German economy was likely anticipated by the companies. And, due to the recent mild weather and declining workforce sickness rates, some of the burdens from the previous months finally appear to be subsiding. One swallow doesn't make a summer, however, and confirmation of a trend reversal remains to be seen. That said, there are at least indications of the winter half-year having seen a bottoming out and that a moderate economic upturn could likely begin in the spring.

Fundamental forecasts, Germany

	2023	2024	2025
GDP	-0.3	0.0	1.2
Private consumption	-0.7	1.1	1.6
Govt. consumption	-1.5	1.2	1.2
Fixed investment	-0.7	-1.7	2.5
Exports	-2.1	-1.1	3.9
Imports	-3.4	-0.7	5.0
Net exports ¹	0.6	-0.2	-0.3
Inflation ²	6.0	2.4	2.2
Unemployment rate ³	5.7	5.9	5.7
Budget balance ⁴	-2.0	-1.7	-1.0
Current account balance ⁴	6.0	6.7	6.1

Change vs previous year as percentage, ¹as contribution to GDP growth; ²HICP; ³as percentage of the civil labour force (Federal Employment Office definition); ⁴as percentage of GDP

Sources: Feri, NORD/LB Macro Research

Quarterly forecasts, Germany

	II/23	III/23	IV/23	I/24	II/24
GDP sa qoq	0.0	0.0	-0.3	-0.2	0.3
GDP nsa yoy	-0.4	-0.7	-0.4	-1.2	0.3
Inflation yoy	6.9	5.7	3.0	2.9	2.4

Change as percentage

Sources: Feri, NORD/LB Macro Research

Switzerland: Bold move – SNB lowers key interest rate

Analyst: Christian Reuter

Economy with trend towards stability – growth remains moderate

Q4/2023 saw real GDP – adjusted for seasonal, calendar and sporting events – register moderate growth of 0.3 percent yoy, thus closing the year as a whole with a plus of 1.3 percent. The service sector once again proved to be a mainstay of the economy, also continuing to drive employment. The hospitality sector was once more a key growth driver. The industrial sector at least showed signs of a bottoming out, with value added in the manufacturing sector – excluding chemicals and pharmaceuticals – rising again for the first time after two quarters in the negative zone. Domestic demand, however, declined slightly in the past quarter, primarily owing to the sharp downward trend in investment in plant and equipment. February saw the economic barometers continue to deliver a consistent picture, showing a continuation of the moderate growth trend with signs of recovery in the manufacturing sector and slowing momentum in the service sectors. The Industry PMI climbed by 1.1 points to 44.0, though continuing to signal a contraction of the sector, albeit somewhat slower than in the previous month. The gap to the Services PMI remained substantial. The latter fell by 1.6 points but, at 53.0 points, continues to point in the direction of healthy growth. Worthy of note at this point is the fact the service sector accounts for three quarters of Switzerland's GDP. Downward interest rates and a weakening currency will likely give stimulus to the manufacturing industry. The exchange rate ought to benefit the service sector, too, since international tourism has gained growing importance after COVID-19. Overall, however, we expect growth to remain rather moderate due to the weakness of the global economy.

Rate hike not completely unexpected – inflation below the 2.0-percent target mark since May 2023

22 March saw the SNB become the first major central bank to lower its key interest, doing so from 1.75 to 1.50 percent and pointing out a marked slowdown in inflation. At 1.2 percent yoy, the price increase rate was again lower than expected by observers and indeed the SNB itself. The core rate also declined further, meaning that the central bank's fears of another rebound at the beginning of the year have failed to materialize. The SNB lowered its inflation expectations again, and its current conditional forecast anticipates that inflation will now remain below 2 percent for the foreseeable future. Immediately after the decision, the euro appreciated by 1 percent against the Swiss franc to 0.978 EUR/CHF. On the forex market the Swiss currency had already moved away from its all-time high of 0.927 EUR/CHF recorded in December 2023 since the beginning of the year. This was probably not an unwelcome development from the central bankers' point of view, given the weak industrial economy in Switzerland and the favourable inflation trend, and they had let the exchange rate fluctuate freely of late. In its communication, however, the SNB retained the passage on its commitment to intervene in the forex market if need be. No mention was made of the announced change at the helm of the institute – SNB Chairman Thomas Jordan will be stepping down in September this year.

Fundamental forecasts*, Switzerland	2023			2024			2025		
	2023	2024	2025	21.03.	3M	6M	12M		
GDP	0.7	1.3	1.8	SNB policy rate	1.50	1.25	1.00	1.00	
Inflation (CPI)	2.1	1.3	1.2	3M rate	1.43	1.10	0.90	0.90	
Unemployment rate ¹	2.0	2.2	2.1	10Y	0.65	0.70	0.70	0.70	
Budget balance ²	0.5	0.6	0.5	Spread 10Y Bund	-176	-160	-150	-150	
Current account balance ²	8.2	8.0	7.5	EUR in CHF	0.97	0.96	0.97	0.97	

* 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: Wage demands prompt central bank reaction

Analyst: Tobias Basse

End of an era

The central bankers in Tokyo have finally scrapped their negative interest rate policy. This marks the end of an era in the Land of the Rising Sun. The Bank of Japan now plans to keep the traditional policy rate level in the range of 0.00 to 0.10 percent. In addition, the central bankers in Tokyo have ended their yield control measures, meaning that the target yield on Japanese government bonds, which in any case had merely symbolic significance of late, no longer officially exists. The central bank's ETF purchases are also set to be terminated.

High wage demands prompt central bank reaction

The monetary policymakers in Tokyo are thus showing an almost unusually high degree of activity. While measures of this nature were to have been expected, the timing of the rate hike can nevertheless be described as rather bold by its standards. It is therefore not surprising that this interest rate decision was not taken unanimously in the Land of the Rising Sun – a country in which decision-making is usually based on consensus. Two central bankers, namely Toyooki Nakamura and Asahi Noguchi, voted against the upward adjustment. In this context, the former emphasized that he would have preferred to wait for clearer indications of rising wages, also where SMEs are concerned, before raising interest rates. However, the comments on the part of BoJ governor Kazuo Ueda, show that recent wage demands in particular were likely the deciding factor behind the rate hike. The central bank in Tokyo didn't want to give clear signals in the direction of further key-rate hikes. In our view, adjustments to Japan's monetary policy will only be made with the greatest of caution in the months ahead – against which background a veritable sequence of rate hikes is hardly likely. The virtually collective fear of deflation in Japan will likely continue having a marked impact on future monetary policy in Tokyo.

Yen not yet able to benefit from the new monetary policy orientation

The forex market also appears to share this view, as reflected in the fact that the yen depreciated against the US dollar immediately after the interest rate decision in Tokyo and the statement on the part of BoJ governor Ueda, subsequently stabilizing above the psychologically important mark of JPY 150 per USD. It goes without saying that this is merely a momentary snapshot, however. In principle, higher interest rates in Japan will certainly benefit the country's currency in the future – especially as other currency areas appear to be leaning towards near-term rate cuts. Lower US key interest rates in particular ought to give the yen a fairly clear prospect of appreciation against the US currency in the course of 2024. However, every positive development ends at some point – so both central banks will be looking to act more cautiously in the months ahead!

Fundamental forecasts*, Japan

	2023	2024	2025
GDP	1.9	0.8	1.3
Inflation	3.3	2.2	1.8
Unemployment rate ¹	2.6	2.5	2.4
Budget balance ²	-5.2	-4.2	-3.7
Current account balance ²	3.5	3.5	3.5

* 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

	21.03.	3M	6M	12M
Key rate	0.10	0.10	0.10	0.20
3M rate	0.25	0.20	0.25	0.30
10Y	0.66	0.80	1.00	1.10
Spread 10Y Bund	-175	-150	-120	-110
EUR in JPY	165	157	153	148
USD in JPY	152	148	143	137

China: Ambitious growth target and Beijing's role

Analyst: Valentin Jansen

Ambitious 5-percent growth target likely only feasible with Beijing's support

Against a background of simmering economic problems, the messages delivered by the central government at this year's National People's Congress were the subject of particularly close attention among market participants. The planned growth target of 5 percent is certainly quite ambitious, seeing as the crisis-ridden real estate sector had traditionally accounted for around one quarter of China's GDP, and this now needs to be generated elsewhere. In addition, there are computationally favourable base effects that will no longer apply this year, as Premier Li Qiang acknowledged. A certain degree of hope therefore rests on private consumption, though there too, the outlook remains cautiously optimistic. Many market participants had therefore hoped for clearer signals in terms of fiscal and monetary policy. Although the issuance of government bonds is set to be slightly scaled up, the officially planned budget deficit of 3 percent remains short of expectations. The leeway available here is also limited, however, given the high levels of debt held by local government bodies as result of Beijing's zero-COVID policy. Overall, China's economy will likely be accompanied this year by a moderately supportive fiscal policy, including readjustments. Beijing is endeavouring to start up the actual medium- and long-term growth engine with "new productive forces" (artificial intelligence, big data, electromobility, renewable energies). In the long term, this is certainly good news in terms of potential growth, but in the short term its impetus will probably not be enough to overcome the prevailing economic weakness. In Addition, conflicts are already brewing now with China's key trading partners, as recently evidenced by the examination by the EU on the imposition of import tariffs on EVs from the Middle Kingdom.

China's stock markets reacted with volatility

China's stock markets reacted to the messages of the People's Congress with volatility; for example the Hang Seng Index temporarily registering a drop of -3 percent shortly after the growth target's announcement. On a three-month horizon, however, there are, all in all, signs of upward trends after the new local lows shortly after the turn of the year. That said, the economic indicators traditionally reported cumulatively for January and February in the context of the People's Congress will have likely contributed to this development, with for example, those for industrial output (+7.0 percent yoy) and foreign trade (exports: +7.1 percent; imports: +3.5 percent) sending out unexpectedly positive signals.

Renminbi's stability a priority; PBOC's leeway currently (still) limited, however

Unsurprisingly, the issue of the renminbi's stability was given high priority in the government's plans. The leeway available to the PBOC in terms of further easing is likely limited at present, at least until the two most important central banks on the left and right sides of the Atlantic start rolling back their restrictive monetary policy. Increased interest rate differentials would make for heightened pressure on the renminbi. Against this background, it will not be until the second half of the year that any significant monetary and fiscal stimulus can be expected from the PBOC.

Fundamental forecasts*, China

	2023	2024	2025
GDP	5.2	4.6	4.5
Inflation	0.3	1.0	1.6
Unemployment rate ¹	5.2	5.2	5.2
Budget balance ²	-6.0	-5.0	-5.0
Current account bal. ²	1.5	1.2	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

	21.03.	3M	6M	12M
Deposit rate	1.50	1.50	1.50	1.50
3M SHIBOR	2.16	2.25	2.25	2.25
10Y	2.29	2.50	2.50	2.50
Spread 10Y Bund	-12	20	30	30
EUR in CNY	7.82	7.58	7.60	7.61
USD in CNY	7.20	7.15	7.10	7.05

Britain: BoE irresolute – despite recession

Analyst: Constantin Lüer

Central bank remains in wait-and-see mode

At its last meeting in March the Bank of England's MPC resolved to hold the Bank Rate at 5.25 percent as had been widely expected. The committee had always stressed that they first wanted to see sustainable progress in disinflation before considering interest rate cuts. At any rate, there was no support for more hikes, with one member (again) voting for a cut of 25 basis points. This meant the MPC voted this time by a majority of 8-1 to pause rate adjustments. It was made clear that monetary policy will need to be kept restrictive for sufficiently long until the risk of inflation becoming embedded above the targeted level of 2 percent target dissipates. There are, naturally, upside risks to be contended with in this context, especially considering various conflicts and associated restrictions in goods transport. That said, the headline inflation rate in the UK has made progress of late and now stands at 3.4 percent yoy. While this represents a further step in the right direction, it was evidently not pronounced enough for the MPC. While there are no limits to the imagination, the likelihood of rate cuts should only then be seriously considered when inflation stands well below the mark of 3 percent.

The inflation trend creates a bit of leeway for the central bank

Along with the headline inflation rate, the CPIHs, i.e. the consumer prices indices including owner occupiers' housing costs, also registered a downward trend. These fell from 4.2 to 3.8 percent yoy in February, and in month-on-month comparison to just 0.6 percent from January's level of 1.0 percent. The largest contributions to this downward movement in both the CPI and CPIH indices came from food and restaurant / cafe prices. The former registered a welcome decline of 2.0 ppts to 5.0 percent yoy, and the cost of eating out likewise fell, by 1.1 ppts to 6.0 percent yoy. This relative relief is likely to be very much to the liking of British consumers. The biggest upward price drivers were similarly direct goods, however, namely housing costs (e.g. rent) with a year-on-year change rate of 2.9 percent (from 2.5 percent), and motor fuels. Year-on-year motor fuel inflation has now been negative for 12 consecutive months and, according to the latest data, fell by 6.5 percent yoy in February, though picking up by 2.7 ppts yoy compared to the previous month.

UK Manufacturing PMI surprises on the upside

The purchasing managers' indices are slowly converging. The PMI for the service sector fell by 0.4 points to a – still satisfactory – level of 53.4 points. The Manufacturing PMI surprised on the upside, on the other hand, narrowly missing the 50-point mark with a level of 49.9 points. The purchasing managers are thus seeing the future in a more positive light for the first time since July 2022.

Fundamental forecasts*, Britain

	2023	2024	2025
GDP	0.1	0.5	1.2
Inflation (CPI)	7.3	2.9	2.2
Unemployment rate ¹	4.0	4.7	4.7
Budget balance ²	-5.0	-3.6	-3.0
Current account bal. ²	-2.8	-2.5	-2.4

* Change vs previous year as percentage

¹ as percentage of the labour force as per ILO concept

Sources: Feri, Bloomberg, NORD/LB Macro Research

Interest and exchange rates, Britain

	21.03.	3M	6M	12M
Repo rate	5.25	5.25	5.00	4.75
3M rate	5.32	5.20	4.95	4.50
10Y	4.00	3.90	3.85	3.65
Spread 10Y Bund	159	160	165	145
EUR in GBP	0.86	0.87	0.88	0.87
GBP in USD	1.27	1.22	1.22	1.24

Portfolio strategies

Yield curve, Euroland

Yields and forecasts (Bunds/Swap)

	Yields (in %)	NORD/LB forecasts for horizons		
	21.03.2024	3M	6M	12M
3M	3.93	3.70	3.30	2.70
1Y	3.39	3.00	2.60	2.20
2Y	2.88	2.60	2.30	2.00
3Y	2.56	2.36	2.17	2.00
4Y	2.46	2.26	2.10	2.04
5Y	2.41	2.20	2.10	2.10
6Y	2.38	2.21	2.13	2.13
7Y	2.37	2.23	2.15	2.15
8Y	2.34	2.25	2.17	2.17
9Y	2.37	2.27	2.19	2.19
10Y	2.41	2.30	2.20	2.20
2Y (Swap)	3.19	2.95	2.65	2.40
5Y (Swap)	2.75	2.55	2.45	2.50
10Y (Swap)	2.69	2.65	2.55	2.60

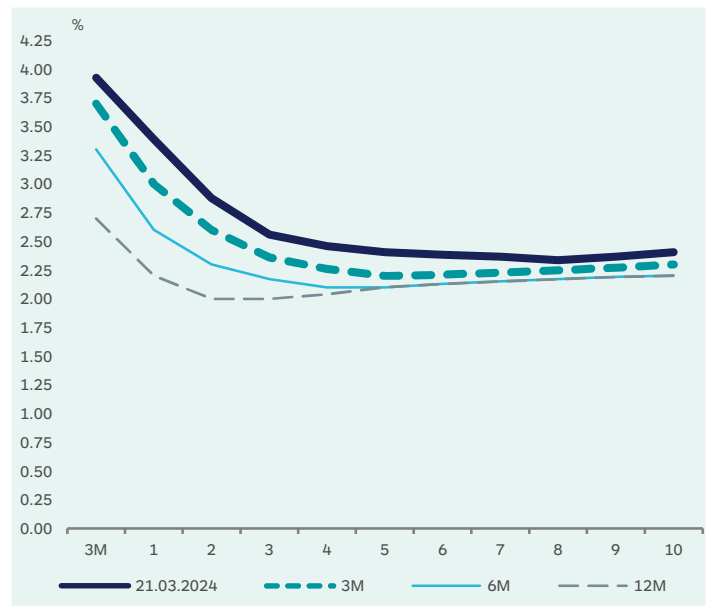
Sources: Bloomberg, NORD/LB Macro Research

Forecasts and total returns

	Total returns (in %) for horizons...		
	3M	6M	12M
3M	0.98	1.92	3.53
1Y	1.15	2.10	3.42
2Y	1.12	2.17	3.65
3Y	1.14	0.86	3.82
4Y	1.39	2.48	3.97
5Y	1.66	2.74	4.06
6Y	1.77	2.84	4.02
7Y	1.73	2.84	4.01
8Y	1.50	2.71	3.88
9Y	1.68	2.95	4.15
10Y	1.87	3.31	4.50

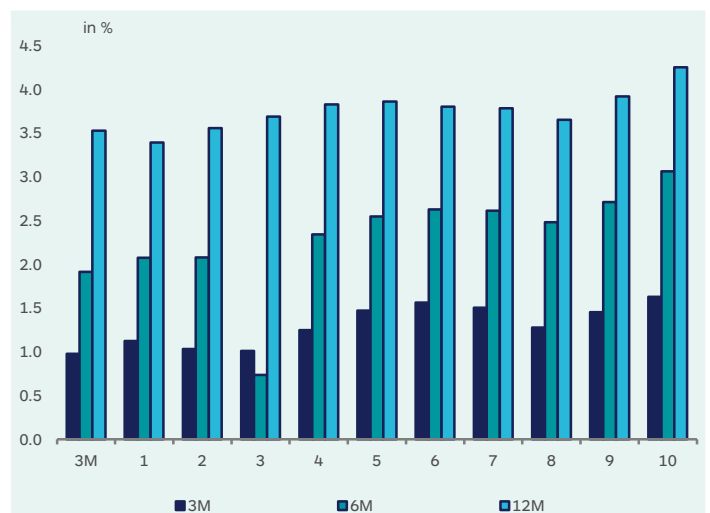
Sources: Bloomberg, NORD/LB Macro Research

Yield curve forecasts (Bunds)



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	1.2	3.6	-0.7	4.9	1.8
2Y	1.1	3.1	-1.7	5.0	1.7
3Y	1.1	3.3	-2.9	4.8	1.6
4Y	1.4	3.5	-3.2	4.9	1.6
5Y	1.7	3.4	-4.2	5.2	1.3
6Y	1.8	4.5	-4.7	5.1	0.9
7Y	1.7	3.1	-4.6	5.2	1.0
8Y	1.5	3.1	-3.9	5.1	0.8
9Y	1.7	3.1	-3.1	4.9	1.1
10Y	1.9	3.2	-1.2	4.7	1.2

Sources: Bloomberg, NORD/LB Macro Research

Expected total returns (as percentage) in national currencies				
	USD	GBP	JPY	CHF
1Y	1.1	0.7	0.0	0.2
2Y	0.6	-0.3	-0.1	0.1
3Y	0.9	-1.5	-0.1	0.1
4Y	1.0	-1.9	0.0	0.0
5Y	0.9	-2.8	0.3	-0.3
6Y	2.0	-3.4	0.2	-0.6
7Y	0.7	-3.3	0.3	-0.5
8Y	0.6	-2.6	0.3	-0.7
9Y	0.7	-1.7	0.0	-0.4
10Y	0.7	0.2	-0.1	-0.4

Sources: Bloomberg, NORD/LB Macro Research

12-month horizon

Expected total returns (as percentage) in euro					
	EUR	USD	GBP	JPY	CHF
1Y	3.4	5.4	3.1	11.3	1.5
2Y	3.6	4.5	2.4	11.5	1.4
3Y	3.8	5.2	1.7	11.3	1.4
4Y	4.0	5.5	1.5	11.3	1.3
5Y	4.1	5.7	0.9	11.6	1.2
6Y	4.0	7.3	0.5	11.5	1.0
7Y	4.0	5.8	0.5	11.6	0.9
8Y	3.9	6.0	0.9	11.4	0.7
9Y	4.2	6.3	1.5	10.9	0.1
10Y	4.5	6.9	2.6	10.2	-0.3

Sources: Bloomberg, NORD/LB Macro Research

Expected total returns (as percentage) in national currencies				
	USD	GBP	JPY	CHF
1Y	4.8	4.5	0.1	1.0
2Y	3.9	3.9	0.2	0.9
3Y	4.6	3.1	0.1	0.9
4Y	4.9	2.9	0.0	0.8
5Y	5.1	2.3	0.3	0.7
6Y	6.7	1.9	0.2	0.5
7Y	5.3	1.9	0.3	0.4
8Y	5.4	2.3	0.1	0.2
9Y	5.8	2.9	-0.4	-0.4
10Y	6.3	4.1	-0.9	-0.7

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		Status		Performance since	
	as at		Start of year	Prev. month	Start of year	Prev. month
	21.03.2024	Prev. month				
DAX	18,179.25	17,678.19	16,751.64	2.83%	8.52%	
MDAX	26,473.05	25,824.65	27,137.30	2.51%	-2.45%	
EuroSTOXX50	5,052.31	4,877.77	4,521.44	3.58%	11.74%	
STOXX50	4,402.37	4,277.81	4,093.37	2.91%	7.55%	
STOXX600	509.77	494.61	478.99	3.07%	6.43%	
Dow Jones	39,781.37	38,996.39	37,689.54	2.01%	5.55%	
S&P 500	5,241.53	5,096.27	4,769.83	2.85%	9.89%	
Nikkei	40,815.66	39,166.19	33,464.17	4.21%	21.97%	

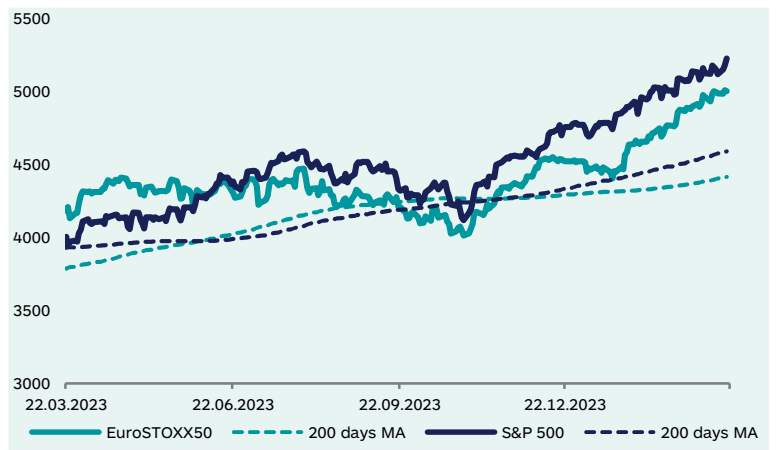
Sources: Bloomberg, NORD/LB Macro Research

Index forecasts

Index	NORD/LB forecast		
	for horizons ...		
	3M	6M	12M
DAX	17,200	16,800	17,500
MDAX	26,100	25,500	26,800
EuroSTOXX50	4,800	4,650	4,850
STOXX50	4,300	4,100	4,300
STOXX600	490	480	490
Dow Jones	38,500	37,000	37,500
S&P 500	4,950	4,750	4,850
Nikkei	38,000	36,500	37,000

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 22 March 2024**

The next English issue of Economic Adviser will be appearing on **29 April 2024**.

Overview of forecasts

Fundamental forecasts

in %	GDP growth			Rate of inflation			Unemployment rate ¹			Budgetary balance ²		
	2023	2024	2025	2023	2024	2025	2023	2024	2025	2023	2024	2025
USA	2.5	1.8	1.9	4.1	2.7	2.3	3.6	4.1	4.2	-6.5	-6.0	-6.2
Euroland	0.5	0.5	1.4	5.4	2.2	2.0	6.5	6.4	6.3	-3.2	-2.8	-2.6
Germany	-0.3	0.0	1.2	6.0	2.4	2.2	5.7	5.9	5.7	-2.0	-1.7	-1.0
Japan	1.9	0.8	1.3	3.3	2.2	1.8	2.6	2.5	2.4	-5.2	-4.2	-3.7
Britain	0.1	0.5	1.2	7.3	2.9	2.2	4.0	4.7	4.7	-5.0	-3.6	-3.0
Switzerland	0.7	1.3	1.8	2.1	1.3	1.2	2.0	2.2	2.1	0.5	0.6	0.5
China	5.2	4.6	4.5	0.3	1.0	1.6	5.2	5.2	5.2	-6.0	-5.0	-5.0

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 interest rates

In %	21.03.24	3M	6M	12M
USD	5.50	5.50	5.25	5.00
EUR	4.50	4.25	3.65	2.90
JPY	0.10	0.10	0.10	0.20
GBP	5.25	5.25	5.00	4.75
CHF	1.50	1.25	1.00	1.00
CNY	1.50	1.50	1.50	1.50

Sources: Bloomberg, NORD/LB Macro Research

Exchange rates

EUR in...	21.03.24	3M	6M	12M
USD	1.09	1.06	1.07	1.08
JPY	165	157	153	148
GBP	0.86	0.87	0.88	0.87
CHF	0.97	0.96	0.97	0.97
CNY	7.82	7.58	7.60	7.61

Interest rates (government bonds)

	3M rates				Yields 2Y				Yields 5Y				Yields 10Y			
	21.03.	3M	6M	12M	21.03.	3M	6M	12M	21.03.	3M	6M	12M	21.03.	3M	6M	12M
USD	5.32	5.20	5.00	4.70	4.64	4.25	3.90	3.60	4.25	3.85	3.60	3.50	4.27	3.90	3.70	3.50
EUR	3.93	3.70	3.30	2.70	2.88	2.60	2.30	2.00	2.41	2.20	2.10	2.10	2.41	2.30	2.20	2.20
JPY	0.25	0.20	0.25	0.30	0.06	0.20	0.25	0.30	0.26	0.35	0.40	0.45	0.66	0.80	1.00	1.10
GBP	5.32	5.20	4.95	4.50	4.18	4.98	4.89	4.38	3.88	4.70	4.70	4.22	4.00	3.90	3.85	3.65
CHF	1.43	1.10	0.90	0.90	0.86	0.80	0.75	0.75	0.69	0.75	0.75	0.70	0.65	0.70	0.70	0.70

Sources: Bloomberg, NORD/LB Macro Research

Spreads (bp)

	3M EURIBOR				2Y Bunds				5Y Bunds				10Y Bunds			
	21.03.	3M	6M	12M	21.03.	3M	6M	12M	21.03.	3M	6M	12M	21.03.	3M	6M	12M
USD	139	150	170	200	176	165	160	160	185	165	150	140	186	160	150	130
JPY	-368	-350	-305	-240	-282	-240	-205	-170	-215	-185	-170	-165	-175	-150	-120	-110
GBP	139	150	165	180	130	238	259	238	147	250	260	212	159	160	165	145
CHF	-249	-260	-240	-180	-201	-180	-155	-125	-171	-145	-135	-140	-176	-160	-150	-150

Sources: Bloomberg, NORD/LB Macro Research

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