Erste Group Research
Week Ahead | Major Markets | Eurozone, US
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Week Ahead

Focus: EZ – bank lending survey, new ECB key rates and EURUSD forecasts

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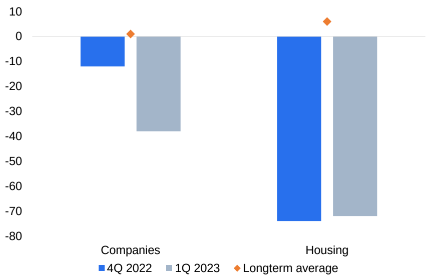
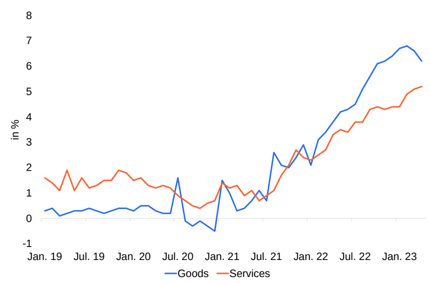
EZ – Loan demand companies and for housing



Source: ECB, Erste Group Research

EZ – core inflation: goods vs. services



Source: Eurostat, Erste Group Research

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Note: Past performance is not necessarily indicative of future results

EZ – demand for credit collapses sharply

According to the ECB's latest bank lending survey, banks in the Eurozone continued to significantly tighten their credit standards for granting loans and credit lines in 1Q23. The main reasons for the tightening are increased risks for the economic outlook and the banks' reduced risk appetite. For 2Q23, banks expect a further moderate tightening of credit standards. At the same time, corporate demand for credit has also fallen significantly. The generally high interest rate level was cited by businesses as a major factor for the lower demand. The demand for property loans from households has also fallen sharply. This was caused by higher interest rates, an uncertain outlook for the property market and weak consumer confidence. Since the start of the data, there has been no comparable sharp drop in demand for housing loans as in 4Q22 and 1Q23.

Based on this survey data, a significant decline in lending across all sectors and areas is expected over the medium term. This will have a particularly dampening effect on the growth prospects for investments by companies and households. The real estate sector in particular will be strongly affected, and a noticeable slowdown in activity has already been observed. Since the current interest rate level is cited as a major dampening factor for the demand for credit by companies and households, the ECB's future interest rate steps play a major role in the outlook for credit demand. In turn, the focus is on the outlook for core inflation. In April, for the first time in a long time, core inflation lost some of its momentum compared to the previous year and fell to 5.6% y/y. In line with the current strong divergence in sentiment between industry (weak) and service providers (strong), core inflation has developed differently by segment. While price dynamics for goods have continued to decline, inflation for services, on the other hand, rose slightly again in April.This is due to catch-up effects on the one hand and rising wages on the other.

However, we expect that the price dynamics for services should also weaken in the coming months. Nevertheless, there are upside risks to the inflation outlook if companies keep their profit margins high in view of higher wage payments. The extent to which lower lending will affect the real economy and thus inflation remains to be seen.

ECB should also raise interest rates in July, dollar weaker faster

As expected, the Governing Council decided this week to raise key interest rates by 25bp. Two of the three criteria defined by the Governing Council itself were in favor of the move. The inflation outlook for the next year was seen as largely unchanged and thus inflation as too high for too long. The underlying inflation dynamics were also still (too) strong. Only the transmission of monetary policy presented a mixed picture. The effects of the interest rate hikes on financial conditions are clearly visible, but they cannot yet be assessed for the real economy. The ECB's statements together with the latest data now lead us to expect another interest rate hike in July, in addition to June. However, the decision is close. Ultimately, the decisive factor is that core inflation is likely to be more sticky than originally expected. At the same time, the latest survey of banks (see above) has highlighted the downside risks to the economy. In our view, however, economic stagnation in the second quarter is still the most likely scenario, and that will not be enough to prevent the Governing Council from raising interest rates in July. The environment still suggests that core inflation will eventually weaken and we therefore do not expect another rate hike in September.

An increase in the ECB's key rate forecasts also has implications for our EURUSD forecast. The interest rate advantage of the US dollar will thus decline faster than originally assumed, which argues for an earlier and stronger weakening of the dollar against the euro. The ongoing turmoil in the US banking sector as well as the dispute over raising the debt limit are also potential further burdening factors for the dollar.

Economic calendar

Ctry	Date	Time	Release	Period	Consens	Prior
Eurozone						
USA						
	10-May	14:30	Inflation y/y	Apr	5.0%	5.0%
China						
	11-May	3:30	Inflation y/y	Apr	0.3%	0.7%

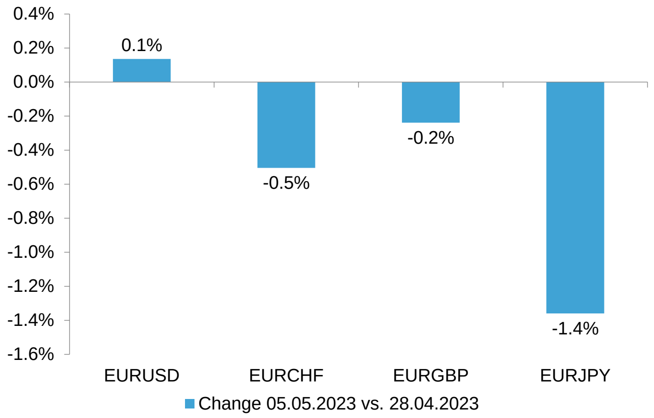
Central bank events

	Date	Time	Representative	Forum	Location
ECB	8-May	16:00	Philip Lane	Speech	Forum New Economy
	9-May	10:00	Philip Lane	Panel discussion	IMF
	9-May	19:00	Isabel Schnabel	Lecture	Hessischer Kreis
	11-May	14:00	Isabel Schnabel	Talk	Federal Minstery of Finance
	11-May	19:30	Luis de Guindos	Panel discussion	Cercle d'Economia Barcelona
	12-May	10:00	Luis de Guindos	Lecture	Academia Europea Leadership
Fed	13-May	01:45	Philip Jefferson	Panel discussion	Stanford University

Source: Market Data Provider, ECB, Federal Reserve, Erste Group Research

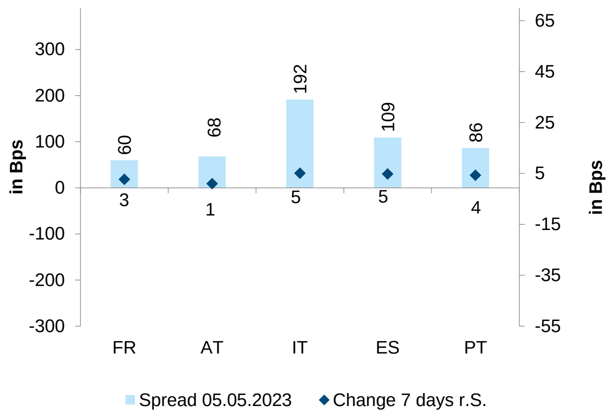
Forex and government bond markets

Exchange rates EUR: USD, CHF, GBP and JPY
Changes compared to last week



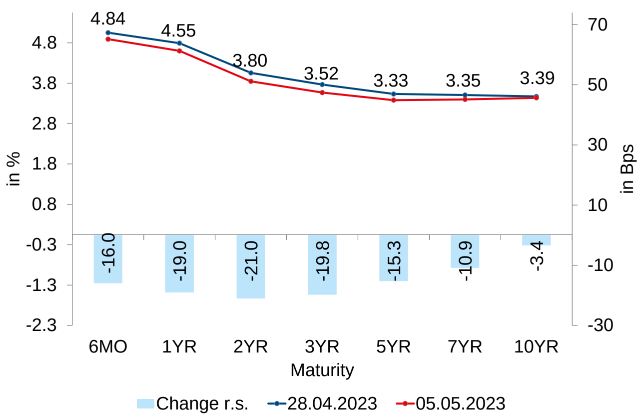
Source: Market Data Provider, Erste Group Research

Eurozone spreads vs. Germany
10Y government bonds



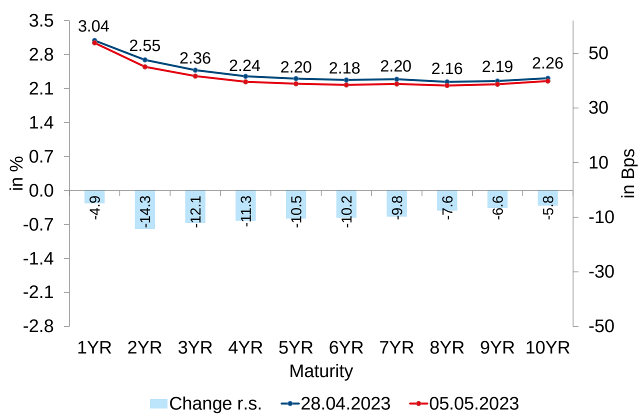
Source: Market Data Provider, Erste Group Research

US Treasuries yield curve
Changes compared to last week



Source: Market Data Provider, Erste Group Research

DE Bund yield curve
Changes compared to last week



Source: Market Data Provider, Erste Group Research

Forecasts[1]

GDP	2021	2022	2023	2024
Eurozone	5.3	3.5	0.6	1.2
US	5.7	2.0	1.4	1.1

Inflation	2021	2022	2023	2024
Eurozone	2.6	8.4	5.7	2.7
US	4.7	8.0	4.0	1.9

Interest rates	current	Jun.23	Sep.23	Dec.23	Mar.24
ECB MRR	3.75	4.00	4.25 ↑	4.25 ↑	4.25 ↑
ECB Deposit Rate	3.25	3.50	3.75 ↑	3.75 ↑	3.75 ↑
3M Euribor	3.28	3.70 ↑	3.72 ↑	3.75 ↑	3.69 ↑
Germany Govt. 10Y	2.25	2.20	2.20	2.20	2.20
Swap 10Y	2.94	2.70	2.70	2.70	2.70

Interest rates	current	Jun.23	Sep.23	Dec.23	Mar.24
Fed Funds Target Rate*	4.83	5.13	5.13	4.88	4.63
3M Libor	5.33	5.21	5.21	4.96	4.71
US Govt. 10Y	3.39	3.30	3.10	2.90	2.90
EURUSD	1.10	1.12 ↑	1.14 ↑	1.16 ↑	1.18 ↑

*Mid of target range

In case of changes to our forecasts compared to the previous issue, arrows show the direction of the change.

Source: Market Data Provider, Erste Group Research

[1] Note: In accordance with regulations, we are obliged to issue the following statement: Forecasts are not a reliable indicator of future performance.

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