ISSN: 2241-4851

Eurobank Research

EUROBANK

GLOBAL & REGIONAL MONTHLY

As evident in the latest global PMI surveys, economic growth slowed for a third successive month in August, underscoring the downside risks associated with the lagged effects of monetary policy tightening. Meanwhile, inflation continues to decelerate slowly, but further progress on disinflation may prove more difficult to achieve due to fading base effects and potential supply constraints. That said, amid concerns of inflation proving stickier than earlier expected, major CBs will likely retain a tightening bias and keep rates high for longer in order to ensure price stability on a sustained basis.

Macro Picture

USA: GDP growth continues to exhibit surprising resilience to tighter monetary conditions

EA: gloomy signals for economic growth dash ECB hopes for a recovery in H2

UK: activity data point to fast growth deceleration in Q3 after surprisingly strong Q2 GDP print

CESEE: dismal Q2 GDP prints tilt growth risks to the downside

Markets

FX: perceived rate differentials key drivers of FX pairs; USD index DXY about to break higher

Rates: EUR and USD rates trading range bound; "high for longer" scenario more likely in the near term

EM: sovereign bond spreads traded wider intra-month, still within the year's range

Credit: market to remain data-driven; focus on soft vs hard landing scenario

Policy Outlook

USA: resilient activity data support the case of further Fed rate tightening by year-end

EA: mounting growth concerns skew risks toward a pause at the 14 September ECB meeting, but inflation still too high for comfort

UK: elevated services inflation amid rising wage growth likely to force the BoE to hike rates further

CESEE: central banks about to start monetary easing amid falling inflation and slowing growth

Key Downside Risks

DM: high inflation persists for longer, requiring additional monetary tightening to tame; financial sector turmoil resumes

EM: growth deceleration in China continues; extreme weather events and geopolitical jitters inflate again commodity prices

Special Topic in this issue:

→ Trends in energy products prices in 2023 and medium-term outlook

Contributing Authors:

Paraskevi Petropoulou
Senior Economist
ppetropoulou@eurbank.gr

Maria Kasola
Research Economist
mkasola@eurobank.gr

Michail Vassileiadis
Research Economist
mvassileiadis@eurobank.gr

Dr.Dimitrios Exadaktylos
Economic Analyst
v-dexadaktylos@eurobank.gr

September 2023

Special thanks to the Global Markets team (Global_Markets_Trading@eurobank.gr)

Contents

Macro Views 3

World Economic Outlook 3

Developed Economies 4

Emerging Economies 5

Markets View 6

Special Topic 9

US 16

China 17

Japan 18

Euro area 19

Germany 20

France 21

UK 22

Cyprus 23

Bulgaria 24

Turkey 25

Eurobank Macro Forecasts 26

Eurobank Fixed Income Forecasts 27

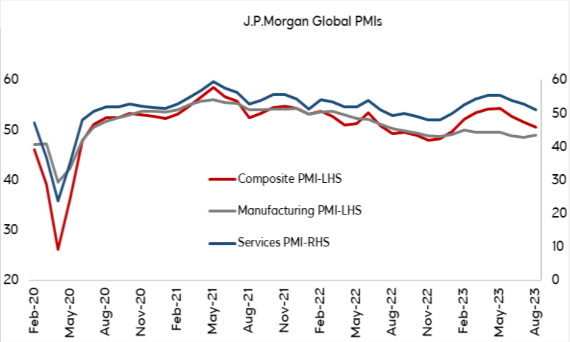
Research Team 28

Macro Views
Latest world economic & market developments

Global growth is slowing, but the risk of inflation remaining elevated for a protracted period will likely force major CBs to keep rates high for longer

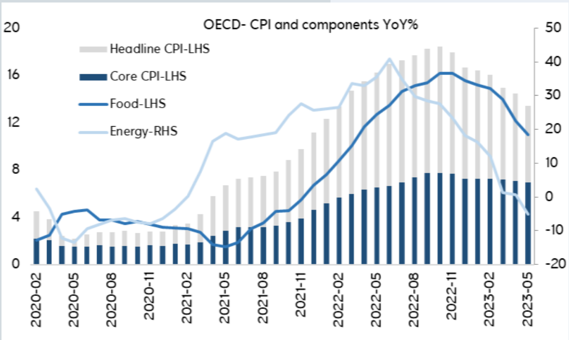
As evident in the latest global PMI surveys, economic growth slowed for a third successive month in August after holding at a solid pace through midyear, underscoring the downside risks associated with lagged effects of monetary policy tightening and the impact of tighter credit conditions. After dropping by a cumulative 2.8pts in June-July, the global composite PMI fell by another 1pts in August, coming in at 50.6, further below the survey's long-run average of 53.3. The slowdown was driven by the services PMI which recorded the third consecutive sizable monthly decline, down by 1.6pts to 51.1, its lowest level since January, as it catches down to manufacturing which edged up by 0.4pts to a three-month high of 49.0, though still in contraction territory. Besides a gloomy assessment of the global economy's near-term growth momentum, PMI surveys also confirmed that differential fundamental forces lead to divergent growth patterns across countries. That said, in contrast with the Eurozone and the UK where the composite PMI index dropped in August further below the 50 benchmark that separates expansion from contraction, the respective US index remained above that critical level. Admittedly, incoming US data continue to surprise to the upside over the last few months, suggesting that the economy will likely outperform several developed and developing economies, including the Eurozone, the UK and China, mainly supported by firm consumer spending — the key engine of growth for the world's largest economy —thanks to a still strong labor market and excess savings. However, while conditions are set for a global growth slowdown near-term amid material headwinds, the continued strength in consumer fundamentals, notably robust labor income growth, and healthy rates of fixed asset investment, have been encouraging, raising hopes for a soft landing scenario. On the inflation front, global headline CPI remains on a downward trend, but still above major CBs' target, and core inflation, though off recent highs, has proven to be sticky mainly due to services inflation which remains elevated amid sustained labor market tightness, while core goods inflation continues to decelerate driven by manufacturing sector weakness and easing supply chain bottlenecks. However, further disinflation progress

Figure 1: Global economic growth slowed in August for the third consecutive month



Source: Bloomberg, Eurobank Research

Figure 2: Inflation pressures have eased, but still above CBs' comfort zones



Source: OECD, Eurobank Research

may prove more difficult on fading base effect affect after the above 25% increase in brent crude oil prices from their late June lows and the risk of an increase in global food prices on weather-related supply shocks and geopolitical risks. That said, amid concerns about inflation to remain elevated for a protracted period, DM central banks will likely retain a tightening bias and keep rates at restrictive levels for longer, to ensure price stability on a sustained basis.

Developed Economies

US: According to the second estimate, Q2 GDP grew by an annualized rate of 2.1%QoQ saar, revised lower by 0.3ppts from the previous estimate after a lower re-assessment in private inventories and net exports. Nevertheless, this is still higher than initially expected after a GDP print of 2.0% in Q1 and slightly above the trend growth rate of the economy. Looking into Q3, defying soft indicators (e.g. PMI) which have been consistent with a slowdown in economic activity for some time now, incoming activity data continue to show a resilient tone to tighter monetary conditions (e.g., IP, retail sales, housing starts), implying another quarter of solid growth and proving wrong, thus far, earlier calls for recession by mid-2023. Though economic activity will likely slow in Q4 amid expectations for a further decline in personal consumption as excess savings are nearly depleted and banks are expected to tighten lending standards further US resilience so far prompts us to revise higher our 2023 GDP growth forecast to 2.0% from 1.3% previously. Meanwhile, the disinflationary process is progressing slowly, and the labor market, though still tight, is moderating, supporting the case of stable rates at the 20 September FOMC meeting. However, given the solid dataflow, the prospect of a further 25bps hike later this year, cannot be ruled out.

Euro area: GDP surprised to the upside in Q2, growing by 0.3%QoQ, after 0.0% in Q1 and a mild contraction of 0.1%QoQ in the last quarter of 2022, mainly supported by the volatile print of Ireland. However, beyond Q2, data suggest that the economy has been weakening sharply, as tightening monetary policy increasingly drags on domestic demand, fiscal support is becoming less supportive and external demand remains subdued. The composite PMI dropped in August for the fourth consecutive month led by a sharp slowdown in the services sector that joined manufacturing in contraction territory for the first time since December 2022. Adding to growth concerns, economic sentiment deteriorated in August for the fourth month in a row, while ECB monetary tightening continues to feed through the credit channel. Meanwhile, headline CPI stopped falling in August for the first time in five months, but core inflation declined for the first time since May, supporting expectations of a pause in rate tightening at the upcoming 14 September ECB policy meeting, especially as GDP is seen broadly stagnating in H2. However, we should not rush to conclude that core CPI has embarked on a sustained declining trend, as upward pressures on wages are unlikely to abate soon, suggesting that the ECB may also consider a final 25bps rate hike.

Emerging Economies

EM: the key development in the EM space since our last issue in early July was the two-day 15th BRICS summit held at the end of August in Johannesburg, where it was decided by the group of "5", consisting of Brazil, Russia, India, China and South Africa, the entry of 6 new countries, Saudi Arabia, the Iran, Ethiopia, Egypt, Argentina and the United Arab Emirates (UAE), marking the first expansion of the bloc in the last 13 years. The inclusion of the new members has a visible imprint both in terms of the world population and in terms of GDP the eleven countries in total represent. While the existing five countries account for about 42% of the world's population and slightly more than 23% of world GDP, the wider group will represent roughly 46.5% of the world's population and 30% of world GDP. Understandably, a coalition of these sizes attracts the interest and attention of markets and analysts, taking also into account the special weight that the group acquires on the global energy map, pointing it as the main driver of expansion, especially towards the countries of the Middle East. Based on 2022 data, the BRICS gather 20% of the daily oil barrels extracted, with the percentage doubling after the addition of Saudi Arabia, Iran and the UAE. The strengthening of the position of the enlarged group in terms of natural gas reserves is also important, with Russia, which stores 24% of the global reserves, primarily supported by the share of Iran (17%), followed by Saudi Arabia (4%) and the HEA (3%), resulting in the 4 states holding a total of almost half of the world's natural gas reserves. Finally, Argentina's invitation also covers strengthening its energy position in the shale gas and oil market, considering the country's dominant storage capacity in shale energy derivatives.

CESEE: the extensive monetary tightening adopted by local central banks for at least the past 20 months, has taken a toll on the region; indicatively, all CEE3 economies continued to post, either on quarterly, annually or in both terms, negative growth rates in Q2-2023. Nevertheless, the tightening cycle has started to bear fruits regarding its imprint on inflation as, based on the latest CPI prints that go up to July, most regional peers have returned to single-digit grounds. In Czechia, CPI inflation has eased substantially landing to 8.8%YoY in July from 9.7%YoY in June and 12.7%YoY three months earlier. In Romania, inflation slowed down quicker than expected coming in at 9.4%YoY compared to 10.25%YoY in June and 11.3%YoY in April. Poland's flash print for August came in at 10.1%YoY from 10.8% in June but Hungary, despite the marked progress, remains the laggard given the abidance of inflation on deep double-digit grounds for more than a year. CPI moderated to 17.6%YoY in July from 20.1%YoY in the previous month and January's peak of 25.7%YoY. Given the above landscape, the MPCs held by regional central banks in August point to a change of course as in Hungary, the one-day deposit rate was further cut by 100bps to 14.0%, following tantamount easing in all three previous policy meetings, with the key policy rate (KPR), however, kept unchanged at 13.0%. Central banks of Czechia and Romania retained a wait-and-see stance in both July's and August's MPC meetings by keeping the KPR at 7.0%. On the flipside, the central bank of Poland, following the disappointing Q2 GDP growth prints (-2.2%QoQ/-1.4YoY in Q2 from +1.6%QoQ/-0.6%YoY in Q1) cut the unchanged at 6.75% KPR since October 2022 by 75bps to 6.0%, beating market consensus to the downside as the latter pointed to a milder cut of 25bps. All said, while disinflation proceeds broadly in the region, opening the door to all regional central banks for some easing in order for financial conditions to become less tight and thus support the economy which remains in a soft patch, recent spiking commodity prices on the back of adverse climate changes or geopolitical jitters tilt inflationary risks to the upside and call again for close monitoring.

Markets View

Foreign Exchange

EUR/USD: the pair continued trending lower and is currently trading below 1.08, almost 4.5% lower from mid July's high at 1.1240. The pair has been mostly driven by the divergence between the ECB and the Fed rhetoric during August that led to a significant increase in perceived interest rate differentials in favour of the USD. The loss of economic steam in China which is one of the major EU trading partners has only added oil to the fire. For the next few weeks we anticipate the downward trend to continue and the pair to test the 1.06 area while on the upside first resistance stands at 1.0840.

EUR/GBP: the pair has been trading lower for the past two months, moving from the mid-July high of 1.3141 to 1.2550 currently. This move has also been driven by the decrease in the perceived interest rate differential between the UK and the US as the rhetoric of the Bank of England (BoE) has been extremely cautious. Technicals suggest that if 1.2550 is broken further downside towards 1.2422 opens up. It appears that the USD behaviour will determine much for both EUR and GBP in the near term.

Rates

EU: swap rates remained in a tight range during August, with the 10-year now trading around 315bps, having reached a high of 330bps. The yield curve has steepened, with the 5s30s spread trading at -40bps, a notable uptick from -50bps earlier in the month. Looking ahead, it is anticipated that rates will remain range bound and close to their peak. We expect the ECB to hike in September, one last time, despite August's core inflation drop and the weak economic numbers from EA countries, as inflation is still far above the 2% target. The stagflation narrative for the EU, however, persists.

US: swap rates ended the month higher following significant volatility. The 10yr SOFR is trading at 390bps, having traded as high as 400bps. The curve continued to steepen with 5s30s trading at -45bps, up from -60bps at the start of August. Going forward we expect rates to hover around current levels as it is expected that the Fed will pause in September and possibly remain on hold thereafter, although upcoming policy decisions will be data dependent. We do not anticipate any rate cuts in the near term, as the US economy remains strong, thus, we are looking into a "high for longer" scenario.

Emerging Markets Sovereign credit

Sovereign spreads ended the month wider driven by the rise in US yields, China's continuing poor growth prospects, as well as significantly reduced flows due to the summer holiday period. The EMBI Global Index is currently standing at 349bps, having moved 13bps wider since the beginning of August. Overall, the sharp bear-steepening of the Treasury curve, witnessed over the past few weeks, had a profoundly negative effect on EM total returns, yet spreads remained relatively resilient and close to the tight end of the last twelve months range. Asian and sovereign bond outperformed LatAm and EMEA. In China, intensified policy efforts to stimulate the world's second-largest economy, seem to have placed a short-term bottom in the negative sentiment for the region and the global outlook in general. Going forward total returns for the EM space will depend on the trajectory of US yields, which are expected to be range-bound from current levels, as rates are expected to remain higher for longer, signalling a negative tone for the EM space. Growth resilience about to be challenged by the expected slowdown in the US and Eurozone, alongside cyclical and structural growth challenges in China. Idiosyncratic stories are likely to continue to dominate spread performance (Turkey, Ukraine, Egypt etc).

Corporate credit

Following a largely positive July for most asset classes, risk-off prevailed in early August, triggered by both Fitch's move to downgrade the US credit rating from AAA+ to AAA as well as growing scepticism that the Fed was about to cut rates soon. Bonds and equities recovered some ground at the end of the month, as hopes about a soft landing scenario gathered pace once again amid a positive July CPI print in the US, a much less hawkish speech by Fed Chair Powell at this year's Jackson Hole compared to the year before and the JOLTS report survey for July that showed further easing in the labour market. Outside the US, sentiment remained somewhat downbeat amid mixed data (renewed concerns about the economy after the flash PMIs for August, fairly resilient inflation). In this environment, equities posted a slightly negative performance, following three consecutive positive quarters, with the Stoxx 600 -2.4% and the S&P 500 -1.6% in August, supported by a strong month for energy stocks. In credit, IG synthetics ended flattish while HY credit spreads ended mildly wider.

In Europe, Itraxx Main and Xover ended +0.9bps and +8.5bps wider respectively August-to-date. In corporate cash, performance was mixed, with IEAC ending +9bps wider and IHYG -9bps tighter since the beginning of August. Snr Financials outperformed among EU IG cash (Snr Financials -7.5bps) while Consumer Discretionary, Sub Financials and Comms lagged (+10-11bps each). In High Yield, Snr Financials massively outperformed (-317bps) while Consumer Discretionary and Utilities lagged behind (+22-25bps each). Activity in the EU Primary market remained muted in view of the summer lull, with August issuance at EUR75bn, of which almost a 20% consisted of ESG-related issues. In the US, CDX IG finished flat while CDX HY was +13bps wider.

Looking ahead, the market is expected to remain data-driven, with focus on inflation vs growth and rates expectations as investors continue to gauge the probability of a soft vs hard landing scenario. Markets now price in a 38% chance of an additional 25bps rate hike by the Fed in the next two meetings, down from 48% just before the release of the latest NFP print and 63% a week ago. Meanwhile, the chances of a September hike by the ECB are now priced at 23%, their lowest since early May and down from 55% last week, following encouraging EA inflation and less hawkish ECB commentary. The EU Primary market is set for a steady flow of deals in early September, following muted activity during the summer.

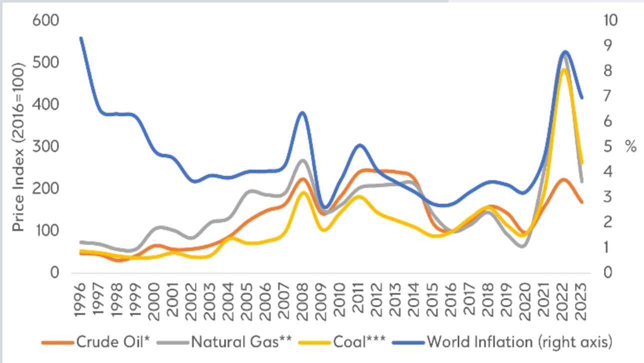
Special Topic: Trends in energy products prices in 2023 and medium-term outlook

Introduction

World inflation hit in 2022 a 27-year high of 8.7%, owed mainly to surging energy products prices in the aftermath of the Russian invasion to Ukraine, as prior to the war, Russia produced ca 11% and 17% of the global oil and natural gas consumption respectively. The high correlation between world inflation and trends in prices of the most consumed energy products, not only in 2022 but also in previous years (e.g., 2008-2011, 2018), is depicted in Figure 3.

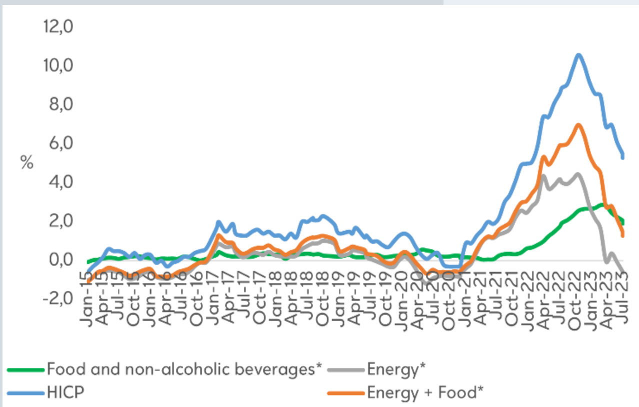
High correlation among inflation and energy prices is also evident at the Euro Area (EA) level. The steep rise of the harmonised price index for energy products accounts for the same trend in the overall harmonised index of consumer prices (HICP) in the January 2021-October 2022 period more than any other major HICP component, with the trend in the subindex of food and non-alcoholic beverages prices being the second most important determinant of the HICP inflation (Figure 4). On the other hand, energy inflation in the EA is sharply declining since October 2022 and in July 2023 it was negative for the third consecutive month (-6.1%YoY), against a multi-year high of 41.5%YoY in past October, having a major role to the HICP inflation weakening at the same period, from 11.5%YoY to 5.3%YoY (Figure 2).[1] Significant developments affecting the energy markets took place in 2023, such as the price cap on Russian petroleum products by the EU, the G7 members beyond the EU and Australia since February, further cuts in daily oil output by OPEC+ members since May 2023 until the end of the year (-1.66 million barrels per day (mb/d) from the April 2023 production level), and, more recently, the additional voluntary oil output reduction by Saudi Arabia (-

Figure 3: Strong correlation between world inflation and fluctuations in prices of the main energy products since the mid-'00s



* simple average of three spot prices; Dated Brent, West Texas Intermediate, and the Dubai Fateh
** includes European, Japanese, and American Natural Gas Price Indices
*** includes Australian and South African Coal
Source: WEO database (IMF), Eurobank Research

Figure 4: Energy prices were the most contributing factor to inflation rise in the EA up to October 2022, but also to its weakening from November 2022 onwards



* * contribution to overall HICP inflation
Source: Eurostat, Eurobank Research

[1] HICP declined by 5.1ppts, with the effect of the energy inflation slowdown at 4.8ppts

1mb/d), effective since July. These and other developments and potential changes affecting the energy markets could pose significant risks to energy prices. This is why, in the remainder of this special topic, developments so far in the prices of crude oil and natural gas in 2023 are first presented. Then, a medium-term prices outlook follows, based on information currently available.

Developments in crude oil prices

Recent developments

The most significant developments so far in 2023 affecting the crude oil and petroleum products markets were presented in the foreword. But, for their potential implications for prices to be fully appreciated, some other, closely related developments, which took place in Q4-2022 must be presented. Specifically, prior to the price cap on Russian petroleum products since February 2023, a price cap on Russian crude oil (so called Urals in the oil market) at $60/bbl was imposed since the beginning of December 2022, also by the EU countries and the rest, non-EU G7 members. The price caps on Russian crude oil and petroleum products could cause a reallocation of global demand towards other countries-producers, price increases from the new suppliers and accordingly, a fall in global demand. Also, prior to the daily oil output cut by OPEC+ members since May 2023, the coalition decided in October 2022 to reduce oil production by 2.0 mb/d since November 2022 from the August 2022 agreed production level. Thus, the overall scheduled cuts in OPEC+ daily production from November 2022 to May 2023, relative to its August 2022 level, amounted to 3.66 mb/d. If these cuts were applied, and non-OECD+ liquids supply remained unchanged, they would correspond to a 3.6% reduction of global production in August 2022. According to the latest data available, in May 2023, OPEC+ daily oil output had been reduced by 1.7 mb/d relative to August 2022, to 37.7 mb/d, thus the target was almost half-achieved, implying less than expected pressures on global crude oil supply.[2] The fall short of the reduction target up to May is probably one of the reasons that led Saudi Arabia to further voluntary output limitations of 1 mb/d since July. Another possible reason is that, according to the IMF, for Saudi Arabia to balance its fiscal budget an oil price of at least $80.9/bbl is needed and up to May crude oil was mostly trading above this level.

As can be seen in Figure 5, crude oil prices do not seem to have been affected for a long term after each of the above developments but the last one, i.e., the voluntary cuts by Saudi Arabia. Since they were announced on June 3rd, crude oil prices have increased up to end August from 13.2% (Brent) to 22.1% (Urals), in close distance to 4 (Brent, WTI) or 9-month highs (Dubai Fateh, Urals) in mid-August. Russian crude oil price has exceeded the $60 price cap since July 7 and was trading above $71/bbl in end August. On early August, Saudi Arabia announced the extension of the voluntary production limitation into September and one month later up to end 2023.

Although oil prices were not affected by almost all the developments concerning directly oil supply/demand, they have been under the impact of recent trends in global economy, such as the slowdown in economic growth, due to the implications of the war in Ukraine, aggressive monetary policy tightening etc., with GDP in the OECD economies increasing by 1.6%YoY in Q1-2023 and 1.5%YoY in Q2-2023, against rises of 4.6%YoY and 3.3%YoY a year earlier.[3] For the world economy in 2023, we project a 2.7% growth rate

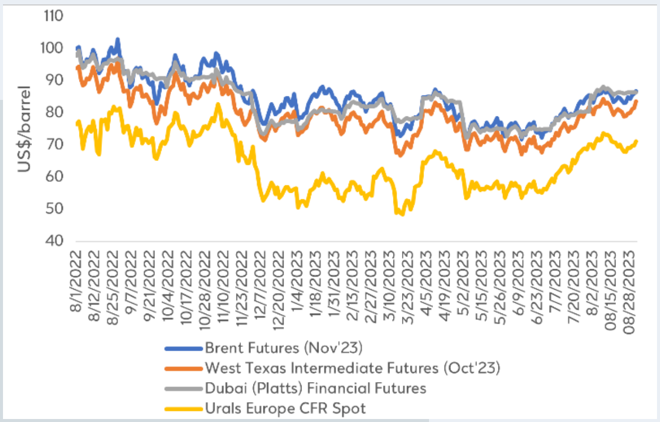
---

[2] OPEC Monthly Oil Market Report (MOMR), October 2022, November 2022, June 2023
[3] According to worldeconomics.com, OECD countries accounted for 42% of global GDP and 27% of global GDP growth in the period 2012-2022

after 3.5% in 2022, albeit stronger by 0.3ppts from our mid-spring (April) forecast. These weakened growth dynamics in the global economy already had an analogous impact on oil and other energy products demand.

On the oil supply side, in contrast to OPEC+ daily output cuts, non-OPEC+ crude production has increased by 1.1 mb/d during January-May 2023, to 20.8 mb/d, mainly from expansion in the US (+0.6 mb/d, to 12.7 mb/d) and China (+0.3 mb/d, to 4.3 mb/d), offsetting most of the supply cuts from the OPEC+ side.

Figure 5: Crude oil prices were not affected by any of the major supply and demand developments in 2023 but the Saudi Arabia voluntary production cuts



Source: investing.com, Eurobank Research

Under the above developments, average crude oil prices were down during January – May 2023 by 19.2%YoY (Dubai Fateh) to 23.7%YoY (WTI), with the fall in Urals being more pronounced (-33.4%), highlighting the implications of the war to demand from Russia. On a YtD basis, the price fall was much milder in January-May in UAE crude oil (Dubai Fateh -2.9%) and Urals (-4.8%), implying weak effects of the price caps for the latter, but the decline was strong for Brent and WTI oil (-15.4% in both cases). As mentioned earlier, oil prices increased during June-August, in the aftermath of Saudi Arabia's announcement for an additional production reduction, which also led to a YtD price increase up to end August in all the main crude petroleum varieties, ranging from 1.1% (Brent) to 26.4% (Urals).

Expected price defining factors and impact in the medium-term

Regarding the expected most defining factors of crude oil prices in the remainder of 2023 and 2024, they comprise the world economy growth dynamics, developments in OPEC+ production, especially in Saudi Arabia, and non-OPEC+ production trends, mainly in the US.

As mentioned earlier, we have revised slightly upwards our world output growth projection for this year compared to mid-spring, by 0.3ppts, to 2.7%. On the other hand, our projection for the next year was marginally downsized, also to 2.7% (-0.1ppts), remaining below the historical (2000–19) annual average of 3.8%. Advanced economies are expected to be the drivers of decelerating growth in 2023 and 2024 relative to the previous year, losing most of their steam in 2022. Indicatively, our growth projections for the US economy are 2.0% and 0.9% against 2.1% in 2022, for the UK 0.3% and 0.6% after 4.3%, for Germany -0.3% and 0.9%, following 1.8% last year and for Japan 1.6% and 1.1% after 1.0%. In view of persistent macroeconomic headwinds, the International Energy Agency (IEA) revised lower for the first time this year in its July 2023 Oil Market Report (OMR) the projection for global oil demand growth this year, by 220 kb/d, to 2.2 mb/d.

Turning to oil supply side expected developments, the recent extension by Saudi Arabia of the 1 mb/d voluntary output cut up to end 2023 pushed further upwards oil prices, at least in the short-term. Further, moderate pressures on OPEC+ supply are expected from Russia's announcement in early August of further cuts in its oil exports by 300 kb/d during September-December, after a fall by 600 kb/d in June, which limited the country's exports to the lowest level since March 2021 (7.3 mb/d) and another scheduled cut by 500 kb/d in August. Both the Saudi Arabia and Russia reductions, not reflected so far on the output data which do not go beyond June, will be partially offset by the expected small output increases in non-OPEC+ countries, such as Norway and the UK, according to recent OPEC projections.[4]

Concerning expected developments in 2024, as the 1.66 mb/d OPEC+ output cut since May 2023 is scheduled to end in December, its extension in the following year is not certain and will be decided most probably in the November 2023 OPEC+ ministerial meeting. The Saudi Arabia and Russia voluntary cuts will be reviewed by the end of the same month. An extension of these cuts, fully or partially, into early 2024, will obviously depend on the price levels oil will be trading at that time. Even if these reductions are extended to next year, they will be largely, yet not fully counterbalanced by higher production mainly in the US and, to a lesser extent, in Norway. The IEA expects oil supply from the Americas, especially its US share, to drive an immense increase in non-OPEC+ volumes over the 2023-2028 period (+5.1 mb/d).[5] Currently, a ca 0.5 mb/d widening is projected for the US in 2024.

Considering the recent and expected dynamics in crude oil demand and supply, average prices in H2-2023 are expected to stand higher than in H1-2023, due to OPEC+ production and exports cuts putting pressures on global supply and the resilience of the services sectors to headwinds in global economic activity. These effects are reflected at the upward revised average oil price projection for 2023 in the July WEO Update, to $76.43/bbl from $73.13/bbl in the April WEO, limiting the annual fall to 20.7% from 24.1%.[6] The expected subdued world economic growth in 2024 and output increases from non-OPEC+ producers will most probably avert a sharp hike in oil prices. On the other hand, risks concerning oil prices are tilted to the upside, e.g., from an escalation of the conflict in Ukraine resulting to additional sanctions from either side, a colder 2024 winter than the previous, very mild one. Indicatively regarding oil price developments in 2024, one-year-ahead (Sep-24) Brent futures are currently trading 7.9% below spot price, with the respective difference in one-year-ahead Dubai Fateh futures at -8.6%. Furthermore, the IMF projected in the July WEO Update that oil prices will decline further next year, by another 6.2%.

Developments in natural gas prices

Recent developments

Some important developments on natural gas demand and supply have taken place so far in 2023 and a significant agreement was reached in late 2022 at the EU level, about the conditions for imposing a price cap in natural gas. With this agreement, a temporary market correction mechanism (MCM) to limit excessive gas prices was established. The MCM will be activated if the following events occur simultaneously:

- The month-ahead price on the Title Transfer Facility (TTF) exceeds €180/MWh for three working days; and
- The month-ahead TTF price is 35€ higher than a reference price for liquified natural gas (LNG) on global markets for the same 3 working days.

[4] Monthly Oil Market Report (MOMR) – July, 2023, published in August
[5] Oil 2023 - Analysis and forecast to 2028, June 2023
[6] Simple average of prices of UK Brent, Dubai Fateh, and West Texas Intermediate crude oil

The MCM has been applicable as of 15 February 2023. When the mechanism is active, transactions concerning the natural gas futures that are within the scope of the MCM above a so-called 'dynamic bidding limit' will not be allowed to take place. The 'dynamic bidding limit' is the reference price for LNG on global markets according to an international basket of LNG transaction hubs, plus €35/MWh. Once activated, the dynamic bidding limit will apply for at least 20 working days. If the dynamic bidding limit is below €180/MWh for the last three consecutive working days, the MCM will be automatically deactivated.

Regarding significant developments so far this year, Freeport LNG's Texas plant, the second largest LNG export facility in the US, resumed processing and export operations in February after an eight-month outage caused by a fire on 8 June 2022, that took the plant's terminal fully offline. At the time, Freeport represented almost 20% of total US liquefaction capacity, and it had sent more than three-fifths of its output in the January-May 2022 period to Europe. By the end of 2022 total LNG exports from the US to the EU reached 55 billion cubic meters (bcm), a volume ca 150% higher than the respective 2021 level (almost 22 bcm). It was estimated that if Freeport had not blown up, US LNG exports to greater Europe could have topped 80 bcm last year. Nonetheless, the rise in EU total natural gas imports from the US in 2022 covered 85.7% of the decline from Russia, with the expansion in US inflows representing 1/3 of total 2021 Russian imports. Following the Freeport LNG terminal's return to service in past February, US LNG exports set a monthly record in April at 8.89 bcm, supported by high demand, particularly from Europe and declined slightly in May (8.41 bcm) and much more in June (7.57 bcm), because of maintenance at several US LNG export facilities, but spiked in July upon completion (10.1 bcm).[7] Europe took 71% of the April US LNG exports, 60% in May, 47% in June and 43% in July, strengthening diversification in energy supplies, which is among the targets of the REPowerEU Plan.

On 10 May 2023, the European Commission launched the first international tender for joint gas purchasing, under the EU Energy Platform. For the first tender, 63 companies submitted requests for a total natural gas volume of 11.6 bcm. Supplier bids amounted to 18.7 bcm and demand finally matched stood at 10.9 bcm (94.0% of requests), with deliveries spanning June 2023 to May 2024. On 7-10 July the second tender ran, with 49 companies submitting requests for a total volume of 15.9 bcm. On the part of suppliers, 15.2 bcm were offered, with agreements finally covering 12 bcm (75.5% of requests), to be delivered during August 2023-March 2025.[8] The prices agreed in the tendering process were not made known, however, with such gigantic collective purchases, much lower gas prices for Europe than those in 2022 could be achieved.

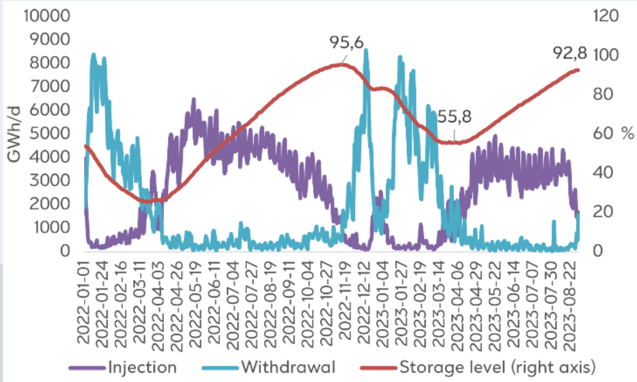
A critical factor that affected natural gas demand in Europe during H1-2023 was the mild weather conditions during winter. According to the EU's Copernicus Climate Change Service,[9] Europe has had this year its second-warmest recorded winter, which offered some relief amid gas prices and facilitated the built up of reserves, also for the next heating season (October 2023 – March 2024). Indicatively, by the end of the previous heating season (end March 2023), the EU gas storage filling level stood at 56%, a level more than

---

[7] Data collected from reuters.com articles
[8] https://energy.ec.europa.eu/system/files/2023-07/ENE%20-%20Joint%20gas%20purchasing%20_FS_final.pdf
[9] https://climate.copernicus.eu/copernicus-antarctic-sea-ice-extent-reaches-all-time-minimum

double that in the same period of 2022 (26%). Reserves accumulation afterwards resulted to a storage level of 92.8% in end August, above the 90% target level for 1 November and in small distance from the 95.7% maximum level of the previous heating season (Figure 6). This summer's extended heatwaves in Europe have not significantly increased natural gas consumption for cooling purposes, as depicted at withdrawals from storages, thus the filling process was not inhibited (Figure 6).

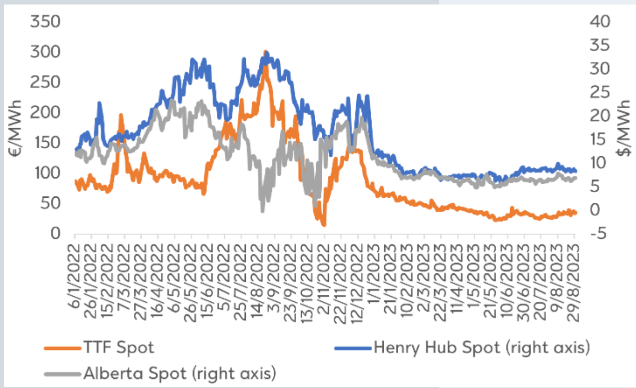
Figure 6: The 2nd warmest EU winter in 2023, kept storage filling at a high level until the end of the heating season and facilitated the built up of reserves for the next one



Source: Gas Infrastructure Europe - AGSI, Eurobank Research

As can be seen in natural gas spot price trends in the most significant trading hubs, the EU agreement about the market correction mechanism in late 2022 ended price fluctuations not only in Europe, but also in the most significant hubs in the US and Canada (Figure 7). In combination with the mild winter, especially in Europe, it sustained a gradual decline in natural gas prices up to end May 2023, to below pre-war levels, of May 2021 (≈€25/MWh at the TTF natural gas hub), from 67.7% (Alberta) to 82% (TTF) below the mid-December 2022 levels. The rise in prices in June is owed to idiosyncratic regional factors, such as the announcement of permanent shutdown of Europe's once one of the biggest gas fields in Groningen, Netherlands, whose production has been drastically reduced in previous years, as the country has been winding down onshore production because of the risk of earthquakes, and planned plant maintenance outages in Norway, EU's 6th most significant supplier in 2022. In the US, prices were underpinned by the reduction in US shale gas rigs, and a rise in speculation activity in the futures markets as traders flipped large amounts of short positions into long ones.

Figure 7: The EU agreement about the market correction mechanism ended price fluctuations not only in Europe and together with the mild winter, led gas prices below pre-war levels



Source: EIA, Bloomberg, Eurobank Research

Expected price defining factors and impact in the medium-term

Regarding price developments in the remainder of 2023 and 2024, the main determinants include the course of recovery of the global economy -crucial also for crude oil prices-, the degree of further progress in diversification of natural gas supplies and in EU joint gas purchasing, under the EU Energy Platform. The global economic outlook about 2023 and 2024 was presented in the price forecasting subsection about crude oil. In brief, after being more resilient in Q1-2023 than expected in the end of 2022, global economic activity showed signs of weakening in Q2, mainly in nonservices sectors (e.g., manufacturing), with GDP in the OECD economies increasing by 1.5%YoY in Q1-2023 after a 1.6%YoY rise in Q2-2023. Nonetheless, given the Q1 growth print, world GDP growth projections for 2023 were revised in July slightly upwards.[10] Global growth in 2024 is still projected to remain subdued, of the same magnitude as in the current year or marginally stronger. Thus, currently there are no signs of a potential sharp upward shift to global natural gas demand.

On the progress achieved in diversification of EU natural gas supplies and limiting dependence on imports from Russia, according to the latest data available, in the period January-April 2023, inflows from Russia accounted ca. for 14.2% of the total beyond-EU imports, against a share of 25.2% in the same period last year and 37.8% in 2021, implying a significant disengagement from Russia. The EU has also limited extra-territory imports from another significant partner, Algeria, from 22.7% in 2021 to 16.4%. Fewer imports from these two countries have been mainly covered from higher inflows from the US (63.8% of losses) and Norway (33.9%). Azerbaijan also saw its share to EU natural gas imports increasing considerably, from 3.6% in January-April 2021 to 6.0% two years later, based on the MoU signed with the EU in July 2022, in the context of the RePowerEU plan. This agreement has created space for much higher imports from Azerbaijan up to 2027, as it includes the doubling of the capacity of the Southern Gas Corridor (SGC)[11] to deliver at least 20 bcm to the EU annually by 2027, with EU imports from this corridor last year amounting to 11.4 bcm out of a total of 13.8 bcm imports from Azerbaijan.

Regarding EU joint gas purchasing, besides the two tendering processes already completed in May and July 2023, according to the European Commission, another three are already scheduled for this year. The schedule for 2024 is not known yet. Considering the delivery period for the already tendered volumes (June 2023-March 2025) and the forthcoming tenders, a significant part of natural gas demand in the EU during H2-2023-H1-2025 is expected to be covered from these tendering processes, at fixed, much lower than in 2022 prices.

The above developments have already strengthened the diversification of EU's natural gas supplies and have created significant potential for further improvement in the non-distant future. In combination with the mild 2023 winter, they have drastically contributed to achieving by end August a storage filling above the 90% target level for 1 November. Furthermore, the completed and scheduled ahead joint gas purchase tenders will secure a significant part of future EU supplies, at least up to mid-2025 at a relatively low cost. Accordingly, the probability of persistently high prices at least during 2023 fall and 2024 early winter, as happened in the period March 2022-January 2023, is considered small.

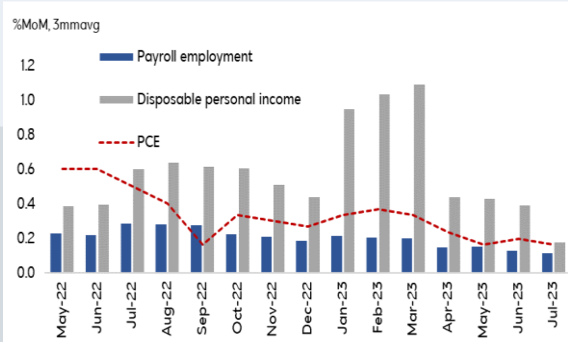
[10] World Economic Outlook Update, July 2023
[11] Starting from Baku in the Caspian Sea, the SGC passes through Azerbaijan, Georgia, Turkey to enter the EU from Greece (Trans Adriatic Pipeline-TAP) and Bulgaria (Nabucco pipeline)

US

Growth continues to exhibit surprising resilience to tighter monetary conditions

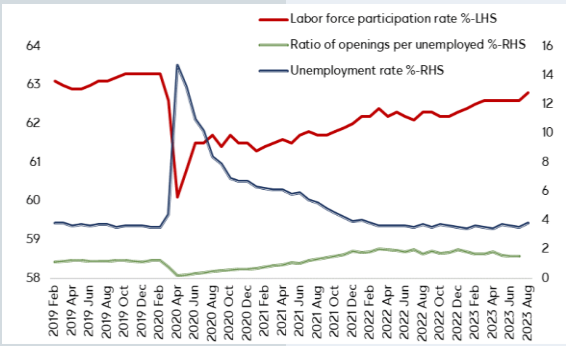
According to the second estimate, Q2 GDP grew by an annualized rate of 2.1%QoQ saar, revised lower by 0.3ppts from the previous estimate after a lower re-assessment in private inventories and net exports. Nevertheless, this is still higher than initially expected after a GDP print of 2.0% in Q1 and slightly above the trend growth rate of the economy. The main positive contribution to Q2 GDP came from personal consumption (+1.71ppts) which rose by a still healthy 1.7% annualized pace supported by firm disposable income that reflects a strong labor market, though slower from 4.2% in Q1 amid tighter bank lending standards for loans in general, and especially for consumer credit. Fixed investment was also a growth driver (+0.1ppts), rising by 3.9% after falling by 0.4% in Q1, driven by strong increases in spending on structures (presumably helped by the Inflation Reduction Act), though residential investment was a drag, recording the ninth consecutive quarter of contraction (-3.6%), despite signs that housing market activity may have already bottomed out in recent months. Looking into Q3, defying soft indicators (e.g., PMI) which have been consistent with a slowdown in economic activity for some time now, incoming activity data continue to show a resilient tone to tighter monetary conditions (e.g. IP, retail sales, housing starts), implying another quarter of solid growth and proving wrong, thus far, earlier calls for recession by mid-2023. Though economic activity will likely slow in Q4 amid expectations for a further decline in personal consumption — the key engine of growth — as excess savings are nearly depleted (personal saving rate down by 0.8ppts in July to an eight-month low of 3.5%, well below the 7-9% post-pandemic range) and banks are expected to tighten lending standards further (according to the Fed's latest SLOOS survey), US resilience so far prompts us to revise higher our 2023 GDP growth forecast to 2.0% from 1.3% previously. Meanwhile, the disinflationary process is progressing slowly, and the labor market, though still tight, is moderating. Core CPI fell in July for the fourth consecutive month, down by 0.1ppts to 4.7%YoY, while the unemployment rate rose by 0.3ppts in August to 3.8% and the ratio of openings to unemployment fell to 1.5%, moving further below the March 2022 peak of 2.0% and approaching its pre-pandemic average of 1.2%, supporting the case of stable rates at the 20 September FOMC meeting. However, given the robust dataflow, the prospect of a further 25bps hike later this year, cannot be ruled out.

Figure 8: Still firm PCE is among the main drivers behind the US economy's resilience



Source: BSL, Eurobank Research

Figure 9 : The labor market is gradually moderating



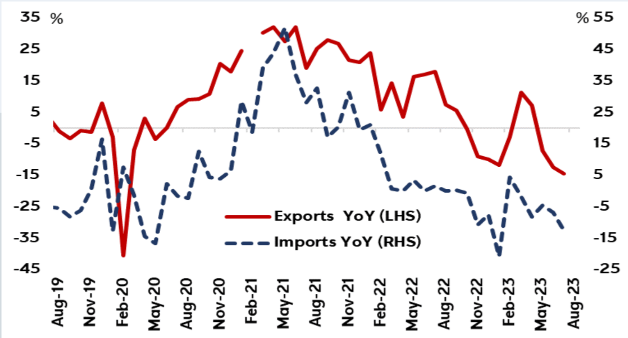
Source: BLS, Eurobank Research

China

After the alarming Q2 growth print, data call for firm policy response

The continuing loss of growth momentum since April was mirrored in Q2-2023 GDP growth data released in mid-July; growth rate was estimated at 6.3%YoY/0.8%QoQ from 4.5%YoY/2.2%QoQ in Q1-2023 translating into a H1-2023 growth rate of 5.4%YoY and poising risks over the accomplishment of this year's official growth target set at around 5.0%. Annual growth between April and June may appeared stronger compared to the first quarter but the Q2 growth print was inflated from low base effects routed in the respective period last year when the severe lockdown in Shanghai was in effect (Mar 2022-Aug 2022).

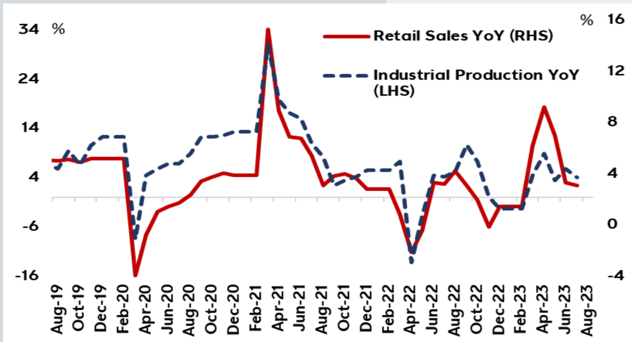
Figure 10: Pronounced deceleration in foreign trade...



Source: Bloomberg, Eurobank Research

Along these lines, the 6.3%YoY growth rate surprised to the downside and spurred expectations over more extensive policy support which is currently unfolding. Soft and hard data following the critical GDP announcement failed to provide markets with some comfort as they suggest at whole that no turnaround is yet in sight. Industrial production expanded in July by a slower pace compared to that in June, up by 3.7%YoY, beating market consensus to the downside. Retail sales growth kept shrinking for a third month in a row landing to a 2.5%YoY rate from 18.4%YoY in April. Imports and exports also plunged and came in below market expectations in July with the former shrinking by 12.4%YoY from 6.8%YoY and the latter diving by 14.5%YoY from 12.4%YoY in June. Finally, industrial profits continued to shrink by 6.7%YoY in July, albeit at a slowing pace during the last three months. Note that the backstop in the diminishing profits is not clear whether it has also intercepted the deferrals in new hirings. Official data release over youth unemployment has been suspended in July after June's jobless rate between 16 and 24 years old in urban areas hit a record high of 21.3% from 20.8% and 20.4% in May and April respectively. Meanwhile, real estate sector remains in a limbo with new home prices declining steeper in July compared to June, reflecting, thus, the prevailing uncertainty among consumers, also evident in services PMIs for August which also disappointed. Recent policy stimulus with cuts in existing and new mortgages is embraced positively in principle and remains to be seen which other measures will follow and how soon will all kick in.

Figure 11: ..along with firm indicators over subdued domestic supply and demand



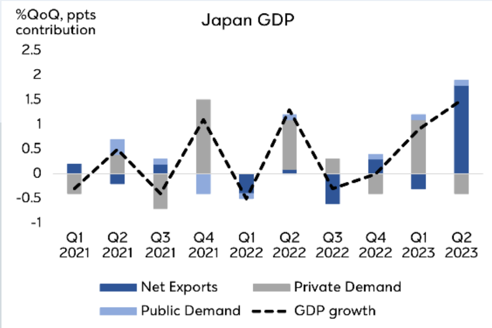
Source: Bloomberg, Eurobank Research

Japan

Rapid growth in Q2, while a somewhat slower pace is expected in H2

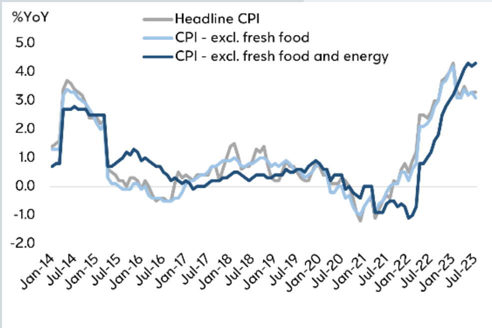
The first estimate for Q2 2023 real GDP growth came in at 1.5%QoQ, well above expectations, after an upwardly revised 0.9%QoQ in Q1. The annual rate stood at 2.0%, unchanged from the previous quarter. Growth was mainly driven by external demand with net exports having a positive contribution of 1.8ppts. Exports of goods increased after a sharp drop in Q1 (+3.3%QoQ from -6.1%QoQ) and exports of services rose for the fifth consecutive quarter (+2.9%QoQ), possibly thanks to the increasing inbound tourism. Imports dropped further (-4.3%QoQ from -2.3%QoQ), indicating a softer domestic demand (private consumption -0.5%QoQ) as pent-up demand from the pandemic is gradually weakening. Looking into Q3, incoming data for July and August were mixed, with a drop in July industrial production (-2.0%MoM), but also with improvements in July retail sales (+2.1%MoM), while consumer sentiment remains at high levels (36.2 in August, lower from July's 19-month high at 37.1, but equal to June's level which was the highest since January 2022), indicating a possible rebound in private consumption. Overall, Q3 growth will most likely decelerate marginally, as the economic slowdown overseas is expected to negatively affect external demand. This effect will be possibly offset to some extent by a further recovery in inbound tourism. Regarding Q4, growth is expected to further weaken, albeit modestly, compared to Q3 marking a somewhat slower pace for the whole H2 2023. All in all, given the unexpectedly rapid growth in Q2, we revise upwards our annual GDP forecast for 2023 to 1.8%. Meanwhile, price pressures persist, with the headline CPI inflation standing at 3.3%YoY in July, unchanged from the previous month. The data release followed the last monetary policy meeting in July, when the BoJ revised substantially its median forecasts for fiscal year 2023 to 2.5%YoY for CPI excl. fresh food and to 3.2%YoY for CPI excl. fresh food and energy, both 0.7ppts up from the previous projections in April. The revision was justified on the basis that the passthrough of higher import prices to consumer prices is larger than the BoJ's expectations. Notably, the BoJ also adjusted the yield curve control (YCC) policy, by raising the rate for daily fixed-rate purchase operations for 10yr JGBs to 1.0% from 0.5%, reflecting the BoJ's concerns about the rising inflation and the side effects of the policy, such as distortions in the functioning of bond markets. As a result, 10yr JGB yields exceeded 0.6% on July 31 for the first time since 2014 (currently at 0.66%).

Figure 12: Strong growth momentum in Q2 driven by external demand



Source: Cabinet Office Japan, Eurobank Research

Figure 13: The BoJ adjusted the YCC policy, as price pressures persist



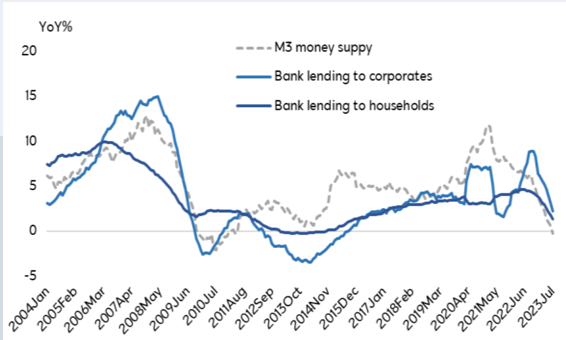
Source: Statistics Bureau Japan, Eurobank Research

Euro area

Gloomy signals for economic growth after a better-than-expected Q2

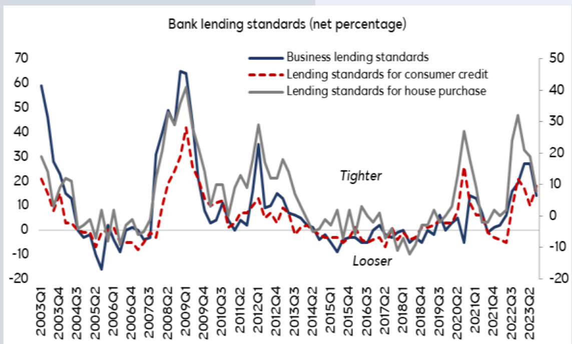
GDP surprised to the upside in Q2, growing by 0.3%QoQ, after 0.0%QoQ in Q1 and a mild contraction of 0.1%QoQ in the last quarter of 2022, mainly supported by the volatile print of Ireland (3.3%QoQ) that was boosted — as suggested by the Irish Central Statistics Office — by activities of multinationals (Eurozone Q2 GDP breakdown due on 7 September). However, beyond Q2, data suggest that the economy has been weakening sharply, as tightening monetary policy increasingly drags on domestic demand, fiscal support is becoming less supportive and external demand remains subdued. The composite PMI, which rose strongly through to April favored by fading energy drags, improving services and easing supply chain disruptions, dropped in August for the fourth consecutive month (-1.9pts to 46.7), led by a sharp slowdown in the services sector (-3.0pts to 47.9), joining manufacturing in contracting territory for the first time since December 2022. Adding to growth concerns, economic sentiment deteriorated in August for the fourth month in a row (-1.2pts to 93.3) amid broad weakness across sectors, while consumer confidence fell (-0.9pts to -16.0) after four consecutive improvements. Meanwhile, ECB monetary tightening continues to feed through the credit channel. Bank lending to both households and non-financials slowed further in July (-0.4ppts and -0.8ppts to 2.2%YoY and 1.3%YoY, respectively) amid weak loan demand and tightening lending standards, as suggested by the ECB's latest lending survey, while M3 money supply recorded an annual contraction (-0.4%) for the first time since 2010. In an encouraging note, though, the labor market remains strong, with the unemployment rate coming in at a record low of 6.4% in July for the second consecutive month, boding well for private consumption as inflation is decelerating, though slowly. Headline CPI stopped falling in August for the first time in five months (5.3%YoY) on the back of volatility in energy prices, but core inflation declined for the first time since May (-0.2pts to 5.3%YoY), supporting expectations of a pause at the upcoming 14 September ECB policy meeting, especially as GDP is seen broadly stagnating in H2. However, we should not rush into conclusion that core CPI has embarked on a sustained declining trend, as upward pressures on wages are unlikely to abate soon (negotiated wages up by 4.3%YoY in Q2), suggesting that the ECB may also consider a final 25bps rate hike.

Figure 14 : ECB monetary tightening continues to feed through the credit channel



Source: ECB, Eurobank Research

Figure 15 : Banks continued to tighten lending standards in Q2



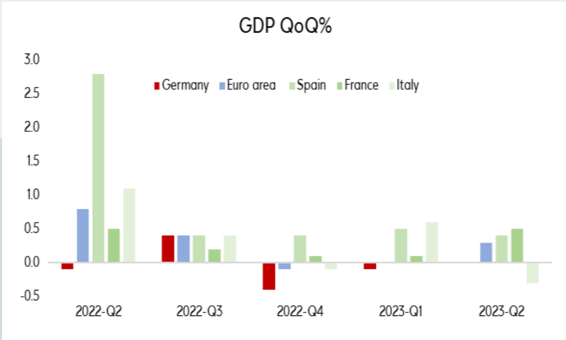
Source: ECB, Eurobank Research

Germany

Recession ended, but risks of protracted weakness remain

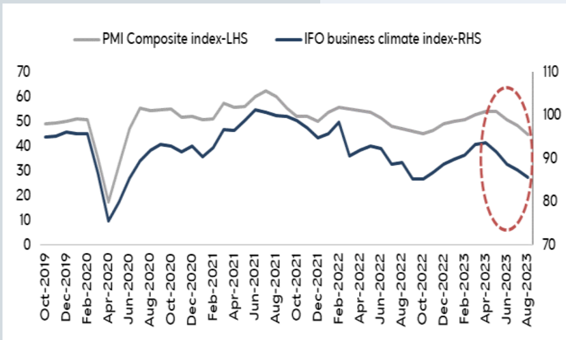
The economy escaped the technical recession it entered in Q4 2022, as GDP grew by an anemic 0.02%QoQ in Q2 2023, with inventories providing the only substantial support to economic activity (+0.4ppts). Though slightly lower than expected, the meagre Q2 GDP was accompanied with upward revisions to the previous two quarters, Q1 2023 and Q4 2022, from -0.3%QoQ and -0.5%QoQ to -0.1%QoQ and -0.4%QoQ, respectively. But even if the technical recession ended, a broad-based decline in leading indicators points to risks of protracted weakness. After a six-month expansion from November 2022 to April 2023 thanks to the absence of a natural gas shortage and lower energy prices, the Ifo business climate worsened in August for the fourth consecutive month, declining by 1.7pts to 85.7, the lowest reading since October 2022. Both expectations and current conditions deteriorated substantially, mainly driven by the services sector and construction, amid concerns about weak external demand, especially from China, higher interest rates and elevated inflation. Sending also clear downward signals, the composite PMI dropped from July's 48.5 to 44.6 in August, the lowest print since May 2020, pressured by a hefty fall of 5.0pts to 47.3 in the services index, the biggest monthly decline since April 2020, mirroring —along with the latest Ifo survey —the sudden deterioration in the sector sentiment as it catches down to manufacturing. Meanwhile, in terms of hard data, retail sales declined in July for the second consecutive month, down by -0.8%MoM, pointing to a lackluster start to Q3 for consumer spending, as persistently high inflation continued to erode households' purchasing power. Also reflecting the tough challenges the economy is facing, industrial output unexpectedly dropped by 1.5%MoM in June, with construction down by 2.8%MoM and manufacturing output falling by 1.2%MoM, leaving a negative carry-over effect of -1.1% for Q3 GDP. More worryingly, the trend of new industrial orders points clearly to the downside, despite June's 7.0%MoM gain thanks to one-off large orders. Against this backdrop, we continue to expect the economy to contract by 0.3% this year, as the upward revision for Q1 GDP was more or less offset from weaker than expected Q2 GDP growth, with risks skewed to the downside amid concerns that external headwinds will likely increase later this year, assuming that the US economy enters a recession by the end of the year.

Figure 16 : Germany continued to lag behind its major EA peers in Q2 2023



Source: Eurostat, Eurobank Research

Figure 17 : Leading indicators do not bode well for economic activity



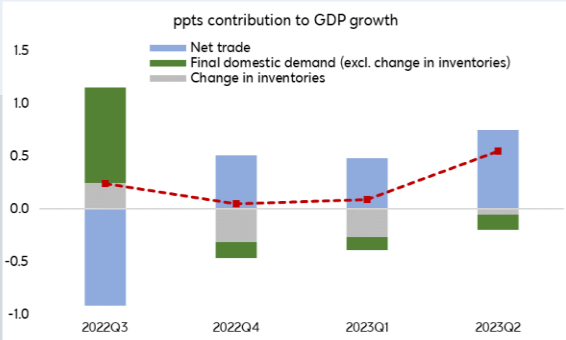
Source: IFO, Bloomberg, Eurobank Research

France

Strong GDP gain in Q2 unlikely to prove sustainable

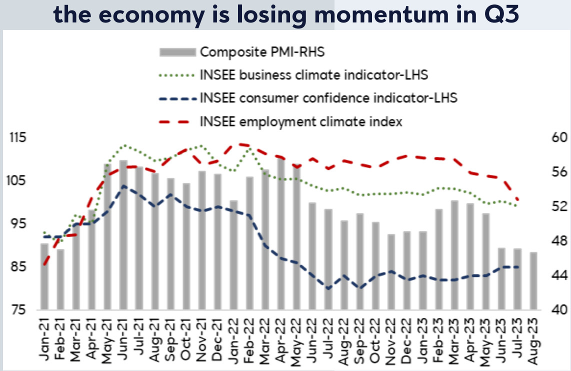
France's GDP rose by a sharply higher than expected 0.5%QoQ in Q2 following a downward revised 0.1%QoQ growth rate (-0.1ppts) in the prior quarter. However, the breakdown of the GDP report was less rosy than the headline, showing that the boost to economic activity came solely from net trade for the third consecutive quarter (+0.7pts). Exports bounced back sharply (2.6%QoQ after -0.8%QoQ in Q1) supported by one-offs, including the delivery of a cruise ship, while imports also recovered, though by a slower pace (0.4%QoQ after -2.0%QoQ). Worryingly, domestic demand had a negative contribution on GDP growth for the third quarter in a row (-0.1pts). Consumer spending remained weak (0.4%QoQ), while investment recovered modestly (0.1%QoQ after -0.4%QoQ) thanks to business investment (0.7%QoQ) and, to a lesser extent, public investment (0.5%QoQ), while household investment dropped for the fourth consecutive quarter (-1.6%QoQ). Looking into the remainder of the year, sentiment surveys and real activity data suggest that economic activity is losing steam, and the strong Q2 GDP gain is unlikely to prove sustainable. The good health of the tourism sector that continues to benefit from the post-pandemic recovery should provide a tailwind to growth in Q3 that is not likely, though, to exceed 0.1%-0.2%QoQ, before weaking further in Q4 amid slower global growth and persistently high interest rates. Led by a 2 ½-year high drop in the services print (to 46.0 from 47.1), the flash composite PMI came in at 46.0 in August, the lowest level since November 2020, confounding market expectations for a modest improvement, while the INSEE composite business confidence fell in August below the long-term average of 100 to a near two-year low of 99.2. In a similar gloomy note, consumer spending on goods fell by 0.8%MoM in July after a two-month rising streak, suggesting that consumption is unlikely to provide much support to growth in Q3, as persistently high inflation —that is decelerating but only slowly— continues to erode household purchasing power, while, perhaps more worryingly, unemployment edged up in Q2 for the first time in two years (+0.1ppts) albeit still close to Q1's three-year low of 7.1%. All in all, we have revised higher our annual GDP growth forecast for 2023 after the surprisingly strong Q2 print, though at a still low level of 0.7% from 2.5% in 2022.

Figure 18: GDP was again mainly supported by net trade in Q2



Source: INSEE, Eurobank Research

Figure 19: Sentiment surveys provide evidence that the economy is losing momentum in Q3



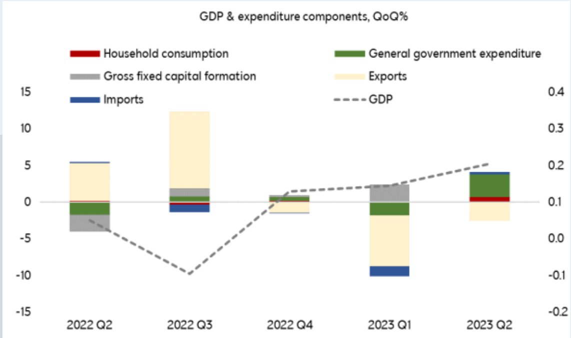
Source: INSEE, Bloomberg, Eurobank Research

UK

Broad decline in leading indicators point to protracted weakness

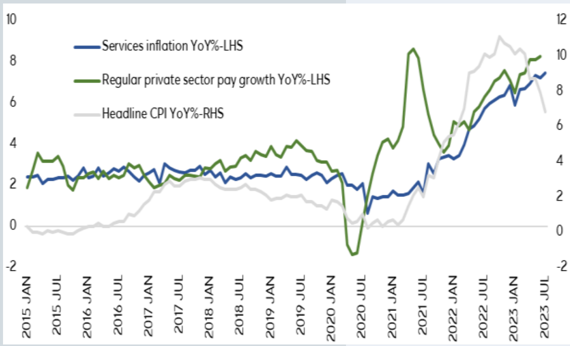
GDP surprised to the upside in June rising by 0.5%MoM amid a strong performance across all sectors, pointing to a more forceful than anticipated rebound from the extra bank holiday for the King's coronation that weighed on the May print (-0.1%MoM). As a result, the economy unexpectedly accelerated in Q2, with GDP growing by 0.2%QoQ after 0.1%QoQ in Q1. Public consumption was the main growth driver (3.7%QoQ, +0.65ppts), rebounding strongly after a strike-related contraction (-1.8%QoQ) in Q1. More surprisingly, private consumption showed decent growth (+0.7%QoQ, +0.45ppts), presumably supported by strong labor income gains and a decline in the housing savings rate. Investment was flat, while net trade was the main negative contributor (-1.14ppts), as exports declined sharply (-2.5%QoQ) and imports rose (1.0%QoQ). However, in a higher interest rate environment, the economy still faces a long road ahead to attain strong and sustainable growth. Sentiment surveys and hard data for Q3 suggest that growth is decelerating sharply as monetary tightening is being transmitted more forcefully on the real economy, allowing us to keep unchanged our projection for near flatline growth for the whole year 2023. The flash composite PMI dropped in August in contraction territory after a six-month period of expansion (48.6 from July's 50.8), annual housing price growth edged further into negative territory in July, according to the latest Nationwide release (-3.8%, the biggest drop in 14 years, after June's -3.5%), and GfK consumer confidence remained well below its long-run average, in spite of the August improvement (+5pts to -25). In a similar gloomy note, retail sales halted a three-month rising streak in July falling by 1.2%MoM on the back of the ongoing cost-of -living squeeze. Meanwhile, the labor market, though still tight, has started to loosen, with the unemployment rate rising in Q2 by a higher than expected 0.2ppts to 4.2% and vacancies, albeit still elevated, took another leg lower in June. Despite, though, markedly deteriorating employment data, wage growth continued to accelerate in June (regular private sector pay growth at a two-year high of 8.3%YoY in June), contributing to a further increase (+0.3ppts) in services inflation to a new multi-record high of 7.5%YoY and pointing to the risk of a longer BoE rate tightening cycle.

Figure 20: GDP surprised to the upside in Q2



Source: ONS, Eurobank Research

Figure 21: Headline CPI is falling, but core and wage growth still rising



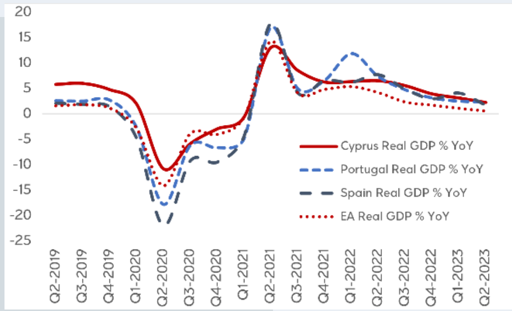
Source: ONS, Eurobank Research

Cyprus

Investment dynamics weakening, household consumption growth unabated

GDP growth weakened in Q2 2023 for the fourth consecutive quarter, to 2.3%YoY from 3.2%YoY in the previous quarter. On a quarterly basis GDP declined, by 0.4%, for the first time in the last three years, after an increase by 1.1% in Q1 2023. The annual slowdown is mainly due to a fall in gross capital formation by 5.1%YoY, against a steep rise of 84.2%YoY a quarter earlier, an increase mostly based on acquisition of ships that significantly weighed on external balance. However, new construction projects (+2.9%YoY) and investment in machinery excluding transports-ICT (+32.1%YoY) exhibited resilience. The decline in exports widened to 2.7%YoY from 1.9%YoY, exclusively from a fall in the goods component (-0.2%YoY), but the external balance improved, from less imports (-3.0%YoY). On the growth drivers' side, household consumption increased further (+4.7%YoY against 4.5%YoY), on the back of weakening inflation (3.4%YoY vs. 6.5%YoY), and support from public consumption to GDP continued, albeit slightly milder (+3.6%YoY after +4.3%YoY). Recent consumer prices dynamics could moderate the increase in household consumption, as inflation slowdown weakened in July (-0.4ppts, to 2.4%YoY), in contrast to expected base effects from its all-time high a year ago, and despite the imposition since May of a zero VAT rate on a list of basic goods. This development is linked to partial wage indexation from June onwards, at a higher rate than in previous years (66.7% instead of 50%), which, on the one hand will support private consumption in the remainder of 2023, but will also sustain high inflation. Regarding external balance, as 75% of exports of goods is channeled beyond the EU, largely to countries from developing regions (e.g., South-West Africa, Middle East, Asia), exports' prospects under the current regional growth risks are hard to trace. The solid rise in tourism revenue throughout Q2 (+27.4%YoY) did not avert the decline in real exports of services, at almost the same pace as in Q1 (≈-3.5%YoY), due to the deterioration in other tradable services (e.g., financial services, based on Q1 current account data). Thus, robust inbound tourism cannot solely boost services exports in the period ahead. Continuing credit contraction towards non-financial businesses in early Q3 from December 2022 onwards, at a fast pace (-3.1%YoY) will be the main drag on investment. In view of the GDP trend in Q2 2023 and the above recent developments, our growth forecast for 2023 was slightly revised downwards by 0.4ppts, to 2.2%.

Figure 22: Cyprus remained among the best performers in GDP growth terms in the EA in Q2 2023, only behind Ireland and Greece



Source: CYSTAT, Eurobank Research

Figure 23: Construction of new houses is positively correlated since Q1 2022 with house prices and is affected by credit expansion especially from Q3 2022 onwards

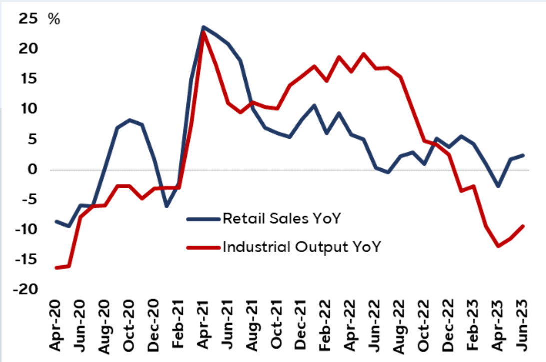
Source: Central Bank of Cyprus, Eurobank Research

Bulgaria

Modest growth in Q2, though firmer compared to its regional peers

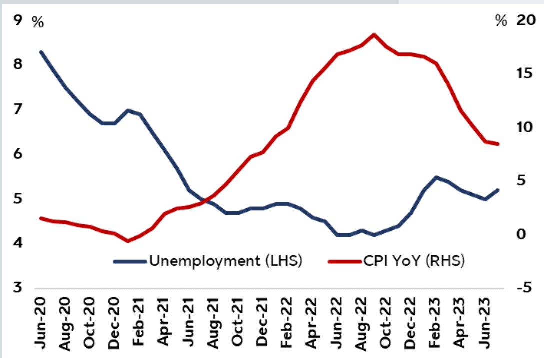
Q2-2023 GDP flash estimate, released in mid-August, came in at +1.8%YoY/+0.4%QoQ from +2.1%YoY/+0.4%QoQ in Q1. In anticipation of the final reading that comes with the breakdown of the GDP components and assuming that this will verify the flash figure, H1-2023 GDP growth is estimated at 1.95%YoY. Despite the slight cooling between the two first quarters in terms of the annual readings, the average GDP growth rate for the first six months ranks first once compared with the respective of all CEE3 plus Romania and Serbia. Additionally, the economy held steady in both Q1 and Q2 expanding by the modest rate of +0.4%QoQ, which, however, is higher compared to the negative prints of Poland (-2.2%QoQ) and Hungary (-0.3%QoQ) and the almost idle performance of Czechia (+0.1%QoQ) in Q2. Rest available economic data point to a broader resilience in the economy in the first half of 2023 with domestic demand strengthening further in June as mirrored in the retail sales growth which picked up to +2.4%YoY after May's +1.8%YoY and following April's -2.7%%YoY slump. On a parallel move, the contraction of industrial production was somewhat curbed in June as it came in at -9.3%YoY after most probably having bottomed out in April (-12.7%YoY). We read beneath the said improvement the deflation process which unfolds continuously since late 2022. Specifically, CPI came in at 8.5%YoY in July from 8.7%YoY in June, despite the uptick in the food prices component which spiked to 13.5%YoY from 13.3%YoY in the previous month, halting a seven-month declining streak (26.6%YoY in Nov-2022). The retreat of inflation along with the steadily firm labor market (unemployment hovering around 5% during the last two years) has given a breather to the disposable income and in our view, there is potential for these conditions to have held in Q3. In view of the above, we revise our FY2023 forecast from 1.5% to 1.7%, continuing to consider, though, the subdued external demand a crucial peril and rendering the overall growth risks balanced.

Figure 24: Broad resilience in the economy with demand strengthening and supply recovering ...



Source: National Statistical Institute of Bulgaria, Eurobank Research

Figure 25: ...on the back of deflation and steadily low unemployment



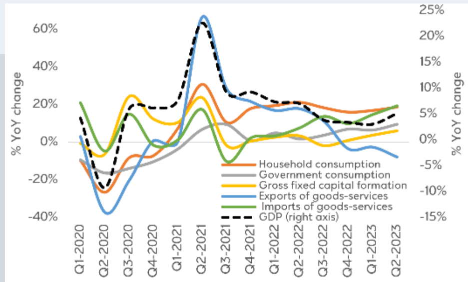
Source: National Bank of Bulgaria, National Statistical Institute of Bulgaria, Eurobank Research

Turkey

Firm monetary policy enhances credibility, albeit with potential implications for investment

Growth on a yearly basis accelerated in Turkey in Q2 2023, to 5.1% from 3.0% in the previous quarter, the strongest increase in the last four quarters. On a quarterly basis, GDP expanded by 3.5%, after a stabilizing -0.1% in Q1 2023. The boost to growth on an annual basis is attributed to all the components of domestic demand, as household consumption expanded by 18.6% against 16.8% a quarter earlier, backed by milder, albeit persisting inflationary pressures (40.5%YoY against 54.5%YoY), and public consumption widened by 9.5%, in the aftermath of the February earthquakes and ahead of the May presidential elections. Investment also expanded, by 6.1%YoY, a 2-year high, with the increase being more pronounced in machinery-equipment (+7.4%YoY). On the contrary, the drag to GDP from the external sector strengthened, both from a bigger fall in exports (-8.0%YoY against -2.7%YoY in Q1) and a stronger rise in imports (+19.3%YoY after +14.6%YoY). The strong rebound of inflation in July-August, at 58.9%YoY in the latter month against 38.2%YoY in June, mainly due to the initial negative effects on the lira (TRY) from the switch to the monetary policy stance and rising fuel prices globally, will weigh on private consumption growth in H2 2023. Inflationary pressures on household demand will be mitigated by the second minimum wage raise in 2023, up by 34% from July onwards, and base effects.

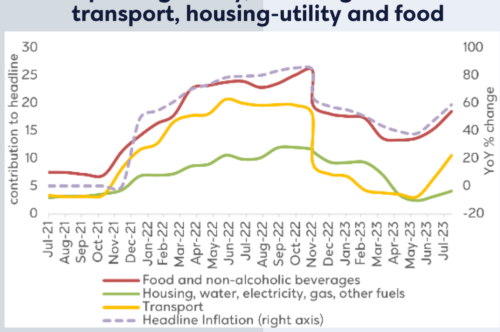
Figure 26: GDP growth at a 4-quarter high in Q2, boosted by all domestic demand components, especially household consumption



Source: Turkstat, Eurobank Research

Further monetary tightening of 1000bpts, through two hikes in July-August, bringing the main policy rate to 25%, above market expectations, improves confidence to overall economic policy, which is reflected at the stabilization of the TRY from July onwards, albeit close to all-time low levels (0.038), and the fast restoration of pre-elections losses to foreign exchange reserves, which have returned to February 2023 levels in the end of August ($75.9bn from $56.5bn in late May), not far from the December 2022 20-month highs ($85.6bn). Provided that these trends continue, external balance will improve through enhanced confidence. On the other hand, tight monetary policy will put a drag on investment, as the average interest rate for business loans has more than doubled during June-August, from 14.5% to 32.5%. The GDP surge in Q2 2023 and the expected dynamics in the economy, are reflected at the upward revision of our growth forecast for 2023 to 3.7% from 2.2%.

Figure 27: The inflation surge in July-August is mainly due to the lira devaluation and rising fuel prices globally, affecting the cost of transport, housing-utility and food



Source: Turkstat, Eurobank Research

Eurobank Macro Forecasts

	Real GDP (YoY%)			CPI (YoY%, avg)			Unemployment rate (% of total labor force)			Current Account (% of GDP)			General Budget Balance (% of GDP)		
	2022	2023f	2024f	2022	2023f	2024f	2022	2023f	2024f	2022	2023f	2024f	2022	2023f	2024f
World	3.5	2.7	2.7	8.7	6.0	4.1									
Advanced Economies															
USA	2.1	2.0	0.9	8.0	4.1	2.6	3.6	3.7	4.3	-3.8	-3.2	-3.2	-5.4	-5.8	-5.9
Eurozone	3.5	0.6	0.9	8.4	5.5	2.5	6.7	6.6	6.7	-0.7	1.5	1.7	-3.6	-3.4	-2.9
Germany	1.8	-0.3	0.9	8.6	6.1	2.8	5.3	5.6	5.5	4.2	5.5	5.4	-2.6	-2.3	-1.6
France	2.5	0.7	1.0	5.9	5.6	2.7	7.3	7.2	7.3	-2.0	-0.9	-0.7	-4.7	-4.7	-4.5
Periphery															
Cyprus	5.6	2.2	2.9	8.1	3.7	2.0	6.8	6.2	6.0	-9.1	-10.0	-6.0	2.3	2.5	2.1
Italy	3.7	0.9	0.8	8.7	6.3	2.4	8.1	7.9	7.9	-1.2	0.7	1.0	-8.0	-4.7	-3.9
Portugal	6.8	2.3	1.5	8.1	5.3	2.5	6.0	6.8	6.7	-1.2	-0.6	-0.5	-0.4	-0.4	-0.2
Spain	5.5	2.2	1.5	8.3	3.4	2.6	12.9	12.7	12.3	0.6	1.4	1.5	-4.8	-4.1	-3.5
UK	4.3	0.3	0.6	9.1	7.4	3.0	3.7	4.1	4.5	-4.9	-2.6	-2.7	-4.4	-5.2	-3.8
Japan	1.0	1.8	1.1	2.5	3.2	2.0	2.6	2.6	2.4	2.1	2.5	2.7	-6.7	-5.5	-4.0
Emerging Economies															
BRICs															
Brazil	2.9	2.4	1.5	9.3	4.8	4.0	9.5	8.3	8.6	-2.8	-2.0	-2.2	-4.6	-7.4	-6.7
China	3.0	5.2	4.6	2.0	0.8	2.0	4.9	5.3	5.0	2.2	1.5	1.2	-4.7	-5.5	-4.6
India	7.0	6.0	6.3	6.7	5.3	5.1		NA		-2.1	-1.5	-1.6	-6.4	-5.9	-5.3
Russia	-2.1	1.4	1.2	13.8	5.6	5.0	3.9	3.5	3.7	10.2	3.2	3.2	-2.2	-3.2	-1.8
CESEE															
Bulgaria	3.4	1.7	2.5	15.3	9.6	4.1	4.3	4.4	4.5	-0.7	-0.6	-0.3	-2.8	-3.0	-3.0
Turkey	5.4	3.7	3.3	72.0	49.5	23.6	10.5	11.5	11.0	-5.5	-6.8	-5.5	-0.9	-3.5	-2.3

Sources: European Commission, World Bank, IMF, OECD, Bureaus of National Statistics, Bloomberg, Eurobank Research

Eurobank Fixed Income Forecasts

	Current	September-23	December-23	March-24	June-24
USA					
Fed Funds Rate	5.25-5.50%	5.26-5.50%	5.27-5.50%	5.07-5.30%	4.67-4.90%
3m SOFR	5.40%	5.39%	5.39%	5.15%	4.78%
2yr Notes	5.50%	5.50%	5.50%	5.30%	4.90%
10yr Bonds	5.25%	5.26%	5.27%	5.07%	4.67%
Eurozone					
Refi Rate	4.25%	4.35%	4.35%	4.30%	4.15%
3m Euribor	3.80%	3.88%	3.87%	3.80%	3.62%
2yr Bunds	3.05%	2.92%	2.71%	2.51%	2.33%
10yr Bunds	2.61%	2.42%	2.31%	2.25%	2.19%
UK					
Repo Rate	5.25%	5.50%	5.60%	5.55%	5.30%
3m Sonia	5.45%	5.51%	5.62%	5.65%	5.51%
10-yr Gilt	4.53%	4.29%	4.09%	3.94%	3.77%
Switzerland					
3m Saron	1.79%	1.91%	1.93%	1.88%	1.78%
10-yr Bond	0.95%	1.16%	1.16%	1.12%	1.08%

Source: Bloomberg (market implied forecasts)

Eurobank Research

EUROBANK

Research Team

Dr. Tasos Anastasatos | Group Chief Economist
tanastasatos@eurobank.gr | + 30 214 40 59 706

Dr. Dimitrios Exadaktylos
Economic Analyst
v-dexadaktylos@eurobank.gr
+ 30 214 40 63 449

Dr. Stylianos Gogos
Research Economist
sgogos@eurobank.gr
+ 30 214 40 63 456

Maria Kasola
Research Economist
mkasola@eurobank.gr
+ 30 214 40 63 453

Paraskevi Petropoulou
Senior Economist
ppetropoulou@eurobank.gr
+ 30 214 40 63 455

Dr. Theodoros Rapanos
Research Economist
trapanos@eurobank.gr
+ 30 214 40 59 711

Symeoni – Eleni Soursou
Junior Economic Analyst
ssoursou@eurobank.gr
+ 30 214 40 65 120

Dr. Theodoros Stamatiou
Senior Economist
tstamatiou@eurobank.gr
+ 30 214 40 59 708

Michail Vassileiadis
Research Economist
mvassileiadis@eurobank.gr
+ 30 214 40 59 709

More available research at: https://www.eurobank.gr/en/group/economic-research
Subscribe electronically at: https://www.eurobank.gr/el/omilos/oikonomikes-analuseis/forma-ekdilosis-endiaferontos
Follow us on twitter: https://twitter.com/Eurobank_Group
Follow us on LinkedIn: https://www.linkedin.com/company/eurobank