ISSN: 2241-4851

Eurobank Research

EUROBANK

GLOBAL & REGIONAL MONTHLY

Global economic momentum picked up pace at the start of 2024, according to the latest business survey data. Unemployment is low and workers are seeing strong wage gains. Inflation is still high for services, and missile attacks on ships passing through the Red Sea pose the risk of a quickening rate of price increases for goods too. Against this backdrop, the world's major central banks are reluctant to ease their tight monetary policy stances too soon. They are communicating their caution about early interest rate cuts, insisting they need more time to get confident that inflation is sustainably returning to target.

Macro Picture

USA: solid growth and easing inflation pressure suggest the economy is still on track for a soft landing

EA: GDP continued to stagnate, though economic activity has probably bottomed out

Japan: hopes are pinned on *shunto* pay negotiations to sustain a wage-price growth cycle

CESEE: the region's major economies shrank in 2023, but are poised for a rebound this year

Markets

FX: USD higher, EUR and GBP lower, on continuing strength of US economic activity

Rates: EU and US short-term rates likely to move higher as CBs seem reluctant to cut rates soon

EM: Sovereign spreads underperformed in early 2024, but pricing appears attractive

Credit: Investors focused on data for fresh signals over the speed and timing of rate cuts

Policy Outlook

USA: the Fed is in no rush to cut rates as it needs to gain "more confidence" on disinflation

EA: the ECB remains data dependent, but implicitly left the door open for a possible rate cut in Q2

Japan: the BoJ became more hawkish, hinting at a Q2 end to its negative interest rate policy

CESEE: further rate cuts, on the back of waning inflation, could stimulate growth in 2024

Key Downside Risks

DM: commodity prices spike as geopolitical tensions escalate, stickier inflation requires tighter monetary policy stance, political uncertainty ahead of elections in several countries

EM: sharper geopolitical fragmentation leads to risk repricing in countries with high-debt profiles and intensifies supply chain disruptions

Special Topic in this issue:
→ Red Sea missiles, central bank rate cycles

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February 2024

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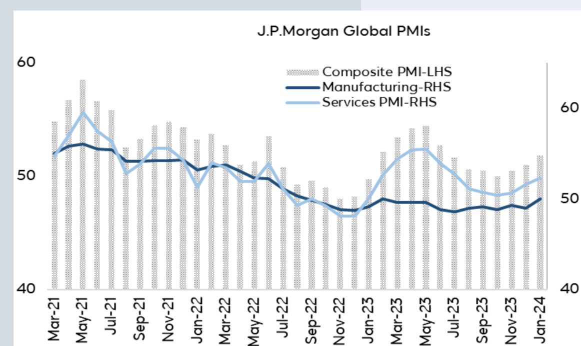
Macro Views
Latest world economic & market developments

Global GDP growth momentum gathered pace at the start of 2024; major CBs signaling caution over early rate cuts

Global composite PMI improved slightly further in January, indicating a third consecutive month of expanding economic output following five months of contraction before that. Robust private sector balance sheets, strong labour markets and the fading drag from inflation helped the index rise by 0.8pts to 51.8, its highest reading since June 2023. That gives some cause for optimism that the worst of the economic slowdown could be over with the global economy starting 2024 with some good momentum behind it. Both services and manufacturing business activity improved, though the former continued to perform better. Services PMI rose for the third straight month, reaching a six-month high of 52.3, up from 51.6 in December. The manufacturing PMI was lower but showed signs of stabilising after 16 months of continuous stagnation. The index rose by 1.0pt to 50.0, with improvements observed across key subindices, including new orders and new export orders. Geographically, Asian economies, led by India, fared relatively better than developed ones.

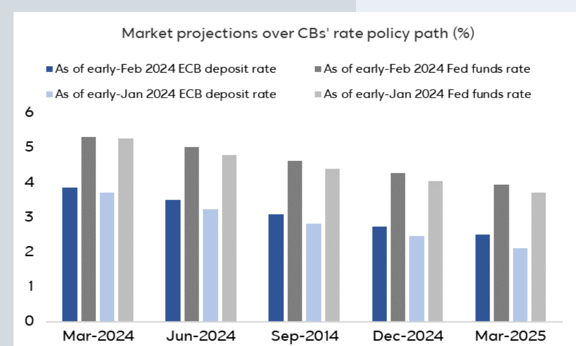
Figure 1: Global GDP growth gathered pace at the start of 2024



Source: Bloomberg, Eurobank Research

Despite these positive developments, January's global PMI survey pointed to increased risks of fresh supply chain shocks in the future due to recent global shipping disruptions in the Red Sea (see special topic on p. 9). Freight costs have increased significantly compared to November 2023 levels — though still remain well below pandemic highs — and supply delivery times have lengthened. As a result, global PMI manufacturing input prices rose in January to the highest level in three months, raising concerns that much of the deflationary momentum in goods prices — the main driver of core deflation last year — could potentially fade. This holds especially taking into consideration that stickiness in core services inflation looks likely to persist for some time given labour market tightness. Part of the

Figure 2: Investors have scaled back their rate easing expectations



Source: Bloomberg, Eurobank Research

January increase in input prices was passed on to clients, with output charges rising for the sixth straight month. Meanwhile, global headline CPI growth moved slightly higher to 3.6%YoY in December as energy base effects look to have largely played out for now. At the same time, global core inflation, which slowed sharply in the first three quarters of last year, continued to ease in December, though modestly, on the back of some disinflation in service prices and fading deflation in core goods prices. Given concerns about a renewed uptrend in core goods inflation in an environment where labour markets are still tight, major central banks are reluctant to say that the battle against inflation is at an end and that they can imminently ease monetary policy. They are signaling caution over early rate cuts, pushing back against near-term rate easing expectations and making it clear that they need time to gain more confidence that inflation is sustainably returning to target before they move.

Developed Economies

US: according to the advance estimate, US GDP expanded by a 3.3% annualized rate in Q4 2023, a slight deceleration from 4.9% in the prior quarter, but well above market consensus and the Fed's longer-run estimate. The upward surprise was mainly due to net exports and inventories. Setting those two volatile components aside, final sales to domestic purchasers still grew by a robust 2.7%, a decrease from 3.5% in Q3 2023 but high enough to suggest that underlying growth still has some hefty momentum behind it. Strong consumer spending provided the bulk of that heft, more than offsetting a sharper slowdown in private domestic investment. Looking to Q1 2024, economic activity is expected to lose some of its momentum, mainly due to the lagged effects of tighter monetary policy and the resumption of federal student loan payments. However, consumer spending remains resilient, suggesting that enough momentum will remain for it to be unlikely that GDP growth falls in Q1 2024 much below Q4 2023. But in such an environment of robust economic activity and labour market tightness, risks remain that there might be another uptick in inflation. As such, the Fed is in no rush to cut rates, as it will take some time for there to be enough convincing evidence that inflation's move towards levels consistent with its target will be sustained.

Euro area: a picture of two-speed economy is emerging in the euro area, with the region's two biggest economies driving stagnation in the currency bloc and countries on the periphery outperforming. For the eurozone as a whole, real GDP was flat in Q4 2023 after a 0.1%QoQ contraction in the previous quarter, meaning that a technical recession was narrowly avoided. Nevertheless, the flat print indicates that the economy has effectively been stagnant over the last five quarters. Activity data suggests that the economy will continue to be weak in the coming quarters. There was one encouraging note from a modest improvement in January's flash composite PMI, kindling hope that economic activity may be at or near its trough. Meanwhile, labour markets remain tight and wage growth elevated, while headline and core inflation decelerated further in January – though slightly less than expected. Against this backdrop, ECB President Lagarde said she wants to see stronger evidence that inflation is on a sustained path towards its 2% target before easing monetary policy. However, in her comments after the January policy meeting, she did implicitly leave open the possibility of a rate cut in Q2.

Emerging Economies

EM: the two fresh economic outlooks from the IMF and the OECD held no major surprises or revisions to the forecasts for developing economies. The IMF's World Economic Outlook estimates that emerging economies grew by 4.1% in 2023, the same rate as in 2022, and they are forecast to retain the same pace in 2024 with revisions in the forecast of 2024 considered negligible compared to the previous publication in October. Chinese growth is seen cooling to 4.6% from 5.2% in 2023, while India will remain the key growth engine in emerging markets, maintaining growth rates above 6% in both 2023 and 2024. The OECD's forecasts were in a similar vein, noting the diverse economic conditions among the G20's emerging-market economies, with the growth drivers varying widely. China continues to struggle with its real estate sector and successive waves of policy stimulus have not managed to improve consumer confidence. On the other hand, India and Indonesia are forecast to experience steady growth over the next two years, driven by strong investment growth, with GDP rising by more than 6% and 5% per annum respectively. On a market-oriented note, emerging market equities and currencies came under renewed pressure this month following signals from the Fed that rates will stay high for longer. Given that EM assets are highly sensitive to movements in the USD, which was strengthened by the Fed's communication, key gauges such as the MSCI EM equities and foreign currency indices extended their losses, which in January reached about 5% and 1% respectively.

CESEE: the majority of the region's countries are set to release Q4 2023 GDP flash estimates by mid-February. Among those that have already reported, the Czech economy contracted by 0.4% in 2023 after expanding by 2.4% in 2022, but we expect it to rebound and grow 1.6% this year. In Poland, the growth rate fell to 0.2% in 2023 after a vigorous 5.3% expansion the year before, but it is projected to recover to a pace of 2.8% in 2024. As we wait for Hungary's Q4 report next week, we estimate that economic output contracted by 0.6% in 2023, following 4.8% growth in 2022, and forecast a recovery to 2.7% for this year, following a similar trajectory to Poland. Examining the average consumer price growth in the CEE3 economies reveals that Hungary, which lagged the other economies in economic output, also faced more persistent inflation, with the average rate of HICP increases accelerating to 17% in 2023 from 15.3%, whereas in Czechia and Poland inflation was somewhat curbed. In Czechia, HICP growth decreased to 12% in 2023 from 14.8% in 2022, and in Poland it dropped to 10.9% from 13.2%. The level and persistence of inflation among these three economies explains quite straightforwardly the monetary policy stances their respective central banks in 2023, as the Hungarian central bank tightened more aggressively compared with its counterparts in Czechia and Poland. This year's outlook appears brighter as a general decline in inflation and subsequent monetary easing are expected to support growth dynamics.

Markets View

Foreign Exchange

EUR/USD: the market bias for EUR/USD, remains bearish. A break below 1.0743 could pave the way for a potential downward push towards 1.0641. Further bearish momentum could potentially target 52-week lows near 1.0448. Relative Strength Index below 30 (RSI <30) is currently at 44.257 indicating that the market is in bearish territory. The Moving Average Convergence Divergence (MACD) signal is currently at a bearish crossover, suggesting that downward momentum could be building. Support levels include 1.0636, 1.0582, and 1.0528, while resistance levels include 1.1029,1.1084, and 1.1138. 1M, 6M and 9M implied volatilities currently at 6.4575, 6.7725, and 6.8175%, respectively.

GBP/USD: same analysis for GBP/USD, suggests a bearish market bias, while a break below 1.255 could potentially target the 1.2353 territory. Currently RSI<30 shows 47.028 and indicates a technically set mid-term bearish area. MACD signal is on a neutral to bearish crossover territory suggesting a downward momentum, while support levels include 1.2425, 1.2362, and 1.2299 and resistance ones 1.2928,1.2992, and 1.3056. 1M, 6M and 9M implied volatilities currently at 6.75, 7.115, and 7.47%, respectively.

Rates

EU: EU rates increased in January, with the 10y swap rate trading at 270bps up from 250bps in the beginning of January. Additionally, the slope of the yield curve has flattened, with the 5s30s trading at -19bps, down from -11bps at the start of the year, though it did reach a low of -25bpsin mid-January. Looking ahead, we anticipate further upward movement in EU swap rates in the near term. This expectation is driven by the fact that markets are already pricing in five rate cuts for the year and the anticipation that the ECB will delay the first rate cut until June, due to still elevated inflation.

US: the US swap rates started the year significantly higher across all tenors. The 10-year SOFR Swap Rate is trading at 375bps, up from 347bps in the beginning of January. The curve remains inverted with the 5s-30s part at the same levels compared to early January, close to -20bps, but having traded as high as -7bps. Looking ahead, we expect short-term interest rates to move higher, boosted by forecast-crushing U.S. non-farm payrolls and average hourly earnings that led futures markets to scale back the total amount of monetary easing expected this year.

Emerging Markets Sovereign Credit

EM sovereign spreads underperformed other parts of the global credit market due to some geopolitical escalations and a lot of new issuance at the start of the year. This has left the EM sovereign/US credit spread at the widest level since early 2022. The EMBI Global Index widened by 16bps and is now at 335bps vs 319bps at the end of last year. In CEEMEA, Saudi Arabia sovereign spreads over Qatar and UAE modestly underperformed, while Israeli spreads remained elevated as new tensions emerged in the area. In Hungary, the central bank delivered a cautious, smaller than expected cut of 75bps bringing the key policy rate to 10%, probably due to recent headlines around EU funding. In Latam, both the central banks of Brazil and Chile cut their monetary policy rates by 50 and 100bps respectively, in line with market consensus. In Asia, Chinese economic data remains soft, while the recent policy intervention was less than expected with the CGB yields ending more than 10bps lower on the month. We remain interested in longer EM duration given the upcoming Fed easing cycle and attractive pricing of EM relative to US credit.

Corporate Credit

January was a mixed month, with risk assets seeing a fairly divergent performance. Hopes for a soft landing continued, albeit markets saw a greater chance of a "later but steeper" path with the first rate cuts materialising after May rather than in March. As economic data continues to surprise on the upside, equities maintained their positive momentum from late 2023. The S&P 500 reached a new all-time high (+4% on the month) while Stoxx 600 advanced for a third consecutive month (+1% January-to-date). US regional bank stocks lost ground in January after New York Community Bancorp, which bought most of Signature Bank last year, reported a loss and raised its expected loan losses on commercial real estate, sparking concerns that the full consequences from higher rates haven't fully unfolded yet. Geopolitical concerns persisted, following attacks from Houthi rebels on commercial ships in the Red Sea, which led to significant supply-chain disruptions (see special topic on p. 9). Freight costs soared and oil prices rose in January but retreated somewhat in the last days after strong results from US oil companies. Sovereign bonds lost ground as investors folded back the prospect of rate cuts in Q1, with Fed Chair Powell saying that the Fed will probably wait beyond March to cut rates, as policy makers need more data to be sure inflation is on a sustained path back to its 2% target. On the politics front, attention is on US elections, after former US President Donald Trump easily won the first primaries of his election year, which put him in a historically strong position to win the Republican nomination.

In credit, European spreads had a mixed performance, with Main flattish January-to-date (+0.5bps) and Xover widening slightly (+13bps). Both indices underperformed vs. US synthetics (CDX IG -2bps and CDX HY -5bps January-to-date). In EUR Corporate cash, IEAC continued to underperform vs. HY, ending +2bps, with IHYG -4bps since the beginning of January. Financials and Technology outperformed among EUR IG cash (Snr Fins -1bps, Sub Fins +4bps, Tech +2bps) while Consumer Discretionary lagged (+8bps January-to-date). In High Yield, Energy, Utilities and Consumer Staples outperformed (-35bps each) and Technology remained a notable underperformer (+484bps). January was a record-breaking month for the market with

total sales exceeding EUR350bn. Issuance was largely driven by sovereign, supranationals and agencies, which accounted for c. 55% of the deal flows, with sovereigns alone at 30%. ESG-labelled issuance accounted for c. 20% of total deals.

Looking ahead, attention remains on data, as investors seek fresh signs on the timing and speed of rate cuts, given the growing chances of a “later-but-steeper” path following January’s policy meetings and subsequent remarks. US politics and geopolitical developments will also remain in focus in the medium-term. Credit sentiment remains positive for issuance, with fresh mandates indicative of a busy week ahead.

Special Topic: Red Sea missile attacks, prices and central bank rate cycles

Heading into 2024, geopolitical risks were one of the top concerns over the global economic outlook, with an escalation in the missile attacks on Red Sea shipping by Yemen's Houthi rebels foremost among these. That danger materialised straight away, yet the signs so far suggest the macroeconomic impact may be small.

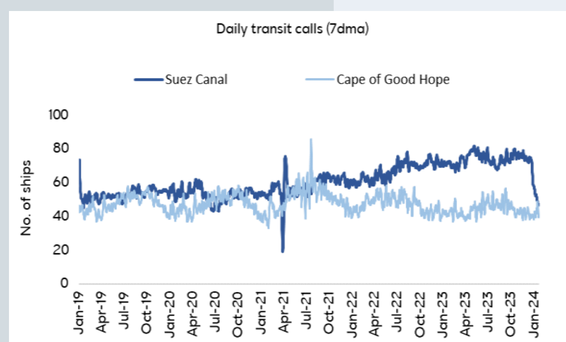
Figure 3: Increasing shipping costs due to Red Sea disruptions

Source: Bloomberg, Eurobank Research

Certainly, the cost to ship goods through the Red Sea, which is the gateway to the Suez Canal from Asia, has increased sharply in recent weeks. As of late January 2024, the Freightos Baltic Index which measures freight costs of so-called 40-foot containers (around 12-meter-long units) has tripled for the China to Europe route compared with late November 2023, rising to about $5,500. That is the highest since late 2022, but it's still around 60% below its peak during the Covid-19 pandemic. For the route between China and the west cost of the US, the equivalent index has surged by more than 50% to $3,000 but remains 86% lower than its pandemic heights.

And there's the nub: while shipping costs have increased, the impact is tiny compared to the supply-chain disruptions three years ago, which kicked off the largest global inflationary shock in decades. During the pandemic, many services were not available due to the lockdowns and as a result, demand from private households for durable goods had surged. This was boosted by government income support measures implemented to contain the impact from the crisis. In short, the irresistible force of extraordinary fiscal and monetary stimulus met the immovable object of supply constraints.

Figure 4: Transits via the Suez Canal are down



Source: IMF, Eurobank Research

Three years on, the fiscal expansion has run its course and monetary policy has cycled through loosening to tightening and is now poised to turn once more. That also hints at where the Houthi rebel attacks have the greatest likelihood of throwing sand in the gears of the global economy – by clouding the outlook on inflation, they could be another factor delaying the start of interest rate cuts this year.

Brief background

In support of the Palestinian militant group Hamas, which has been fighting Israel since October, the Iran-backed Houthis have been attacking dozens of western commercial ships navigating the Suez Canal since November 2023, with a marked step up in their attacks since early January around the Bab-el-Mandeb at the Southern end of the Red Sea. The Red Sea is one of the most important strategic trade routes for global shipping, and the shortest sea route from Asian to Europe, responsible for facilitating – according to the New Zealand Ministry of Foreign Affairs and Trade[1] – around 12% of global trade. That includes 30% of all global container traffic, an estimated 7-10% of the world's oil and 8% of global liquefied natural gas.

In response, the US, which in December 2023 formed the "Prosperity Guarding" coalition of 20 states, has repeatedly conducted, along with the UK, missile strikes on Houthi targets aimed at degrading their disruptive capabilities and to secure safe lanes for commercial shipping in the Red Sea. Since mid-December, several international shipping companies have announced that they are suspending passage through the Red Sea and re-route via the Cape of Good Hope around South Africa due to security concerns. That is more time-consuming and costly due to significantly higher fuel costs. The sailing time for a voyage from Asia to Europe will lengthen by around 10 days to 35. According to the IMF PortWatch tracking data[2], the Suez Canal seven-day moving average of shipping volumes dropped more than 37% in the second week of January, and the respective figure for the Cape of Good Hope increased by nearly 70% due to the re-routed shipping traffic.

Supply chain resilience

Re-routing of large part of shipping flows results in higher freight costs and affects supply chains for some companies, raising concerns about a possible reversal of the disinflationary process. Since mid-2022, a major factor behind declining price pressures has been the deflation in goods prices, as global supply chain that got gnarled up by the pandemic started to normalize. Renewed increases in global shipping costs could add to price pressure on goods.

For now, the New York Fed's Global Supply Chain Pressure Index has remained roughly at its historical average.[3] Meanwhile, another factor mitigating against freight costs increasing as much as they did during the pandemic is the sharp increase in the delivery of new container ships with 20-foot capacity in 2023, which was nearly double the average in recent years.

That said, it's worth bearing in mind that early in the post-pandemic inflation cycle, many underestimated the impact of supply-chain disruptions would have, including the European Central Bank, whose chief economist Philip Lane argued in an April 2021 blog that the impact of shipping costs on consumer prices "would be overall very limited".[4]

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[1] https://www.mfat.govt.nz/en/trade/mfat-market-reports/the-importance-of-the-suez-canal-to-global-trade-18-april-2021/
[2] https://portwatch.imf.org/pages/573013af3b6545deaeb50ed1cbaf9444
[3] https://www.newyorkfed.org/research/policy/gscpi#/overview
[4] https://www.ecb.europa.eu/press/blog/date/2021/html/ecb.blog210401~6407b23d87.en.html

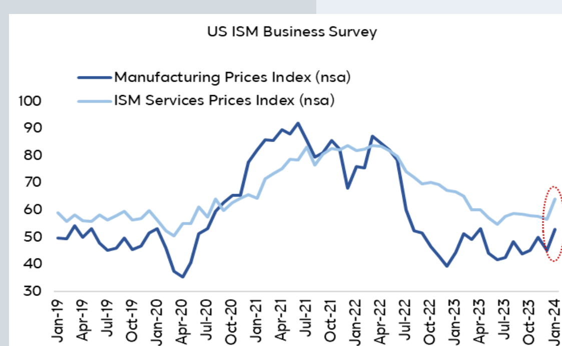
A 2022 IMF study argued that shocks to global shipping costs could have statistically significant and persistent effects on inflation, likely reflecting the impact of increased trade openness.[5] In detail, an increase in global shipping costs (as measured by the Baltic Dry Index)[6] by one-standard deviation (21.8%) typically pushes domestic inflation higher by around 0.2%, with the effect building up gradually before reaching its peak in 12 months and reverts in the subsequent six months.

Inflation risks and easing cycles

So far there have been clear examples where the disruptions are having an impact at the company level – such as production stoppages by Tesla and Volvo at car plants in Europe.[7] But the question is whether these will prove to be significant at a macroeconomic scale. A first hint at the answer to that comes from the various PMI reports for January. By and large, the PMI reports downplayed the impact of the disruptions on output levels – especially at global level – although lengthening supplier lead times was a recurring theme in the country-level reports, such as those for the UK, Spain and Italy. And the global survey did note that manufacturing input prices rose to the highest level in three months, reflecting increased supply chain pressures arising from the Red Sea disruption. Part of the increased input cost in January was passed to clients, with output charges rising for the sixth straight month.

The most significant reference so far was from the Institute for Supply Management, which references the Red Sea as one of the factors, among other, behind a spike in prices paid by businesses in both its manufacturing and services PMI reports for the US. The services report was particular important as the 7.3pt jump in the gauge to a one-year high is the biggest increase since 2012 – and is the kind of print that explains why members of the Federal Reserve Open Markets Committee have been pushing back against market expectations on the pace and timing of interest rate cuts.

Figure 5: ISM data showed a January spike in prices paid by US businesses



Source: ISM, Eurobank Research

To be sure, shipping was just one factor affecting the price gauge, and the Fed has been trying to tamper rate cut expectations regardless of what has been happening in the Red Sea. In fact, this is partly why it is so difficult to disentangle the shipping situation from other factors affecting policy makers' thinking. Nevertheless, the fact remains that at the end of 2023, markets were pricing in 158bps of Fed rate easing this year, with the first cut being fully priced in for March, and those expectations now stand at 120bps with the first one priced in for June.

[5] https://www.elibrary.imf.org/view/journals/001/2022/061/article-A001-en.xml
[6] The Baltic Dry Index (BDI) is a shipping cost measure for bulk goods, including metals, coal, etc.
[7] https://www.japantimes.co.jp/business/2024/01/23/companies/chaos-red-sea-companies-profits/

In Europe, the economy is running cooler than the US, but it is more affected by the smooth flow of traffic through the Suez Canal. In response to a question during the press conference at the conclusion of the latest policy meeting on January 25, ECB President Christine Lagarde said that disruptions in the Red Sea are expected to have “a moderate impact”, though she acknowledged upside risks to inflation from higher shipping costs.

Even if the ECB decides there is no significant direct impact on Eurozone consumer prices, there could still be knock-on effects on the currency bloc if the shipping disruption ends up being a factor delaying a Fed rate cut. Despite the weaker state of the euro area economy compared to the US, some members of the ECB’s governing council may be motivated by a reluctance to be the first to cut rates. And if the ECB does act first, that may lead to a weakening EUR/USD – which could itself be a channel for inflation.

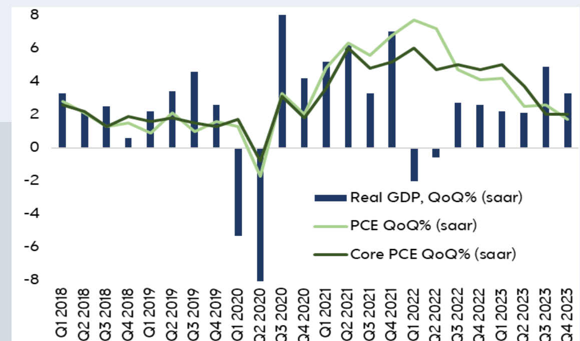
Pressures arising from higher shipping costs would generally be considered temporary and monetary authorities could potentially look through these transitory effects. However, this is all taking place at a time when major central banks are about to pivot to monetary easing after their unprecedented tightening. Even if the potential effect of higher shipping costs on inflation looks to be contained for now, central bankers could still see it as a meaningful policy risk given concerns that its full impact may take some time to bear out.

US

Economy remains strong despite slight slowdown in GDP growth

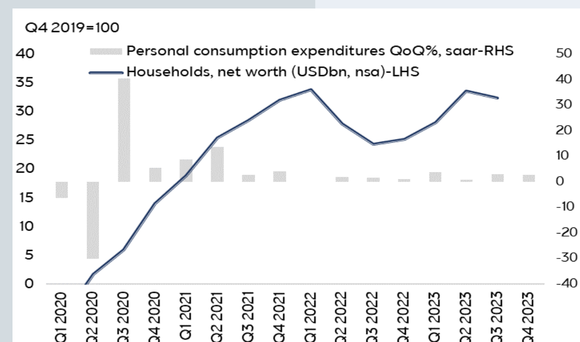
Elevated wage growth, healthy household balance sheets and a gradual decline in savings are continuing to power the US's gravity-defying economy. According to the advance estimate, GDP expanded by a 3.3% annualized rate in Q4 2023, a slight deceleration from 4.9% in the prior quarter, but well above market consensus for a growth rate of 2% and the Fed's longer-run estimate of 1.8%. The upward surprise was mainly due to net exports and inventories, which together had a combined positive contribution of about +0.5ppts to growth – confounding market expectations that they would be a material drag on economic growth. Setting those two volatile components aside, final sales to domestic purchasers still grew by a robust 2.7%, a decrease from 3.5% in Q3 2023 but high enough to suggest that underlying growth still has some hefty momentum behind it. Strong consumer spending provided the bulk of that heft, slowing only marginally in Q4 to an annualized rate of +2.8% from +3.1% in Q3. That more than offset a sharper slowdown in private domestic investment (to +2.1% from +10.1%) and contributed +1.91ppts to GDP growth. Looking to Q1 2024, economic activity is expected to lose some of its momentum, mainly due to the lagged effects of tighter monetary policy and the resumption of federal student loan payments. However, consumer spending remains resilient, as reflected in strong December prints for retail sales and real personal spending. That suggests that enough momentum will remain for it to be unlikely that GDP growth falls in Q1 2024 much below Q4 2023. Last quarter's solid GDP print was accompanied by a further moderation in price pressures, as reflected in core PCE — the Fed's preferred gauge for inflation — which increased by 2%, in line with the central bank's target, for the second consecutive quarter. But in such an environment of robust economic activity and labour market tightness, risks remain that there might be another uptick in inflation. The economy generated 353k jobs in January, the highest in a year, the unemployment rate was steady at 3.7%, against expectations for a modest increase, and average hourly earnings rose by 4.5%YoY after December's 4.3%YoY increase. As such, the Fed is in no rush to cut rates and it is not expected to start easing before Q2 2024, as it will take some time for there to be enough convincing evidence that inflation's move towards levels consistent with its target will be sustained.

Figure 6: Robust GDP growth and moderating price pressures support optimism for a soft landing



Source: BSL, Eurobank Research

Figure 7: Healthy households' balance sheets support consumer spending



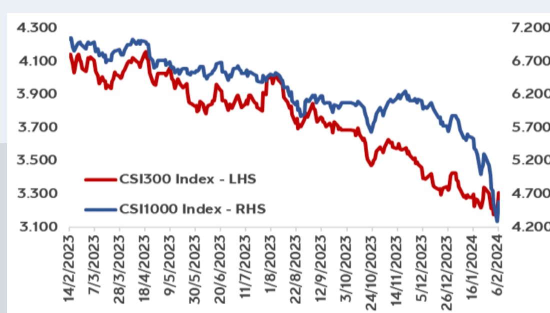
Source: Fed, BLS, Eurobank Research

China

Spooked markets are a reflection of loss of confidence in economy

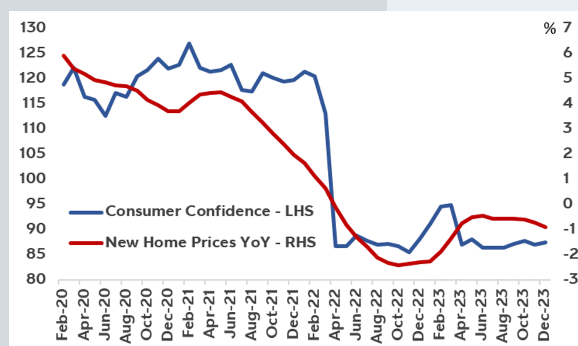
Over the past few days, the rout of China's equity markets has received much attention, adding yet another challenge to the growing list that policymakers must address. The economic difficulties range from structural issues, such as the declining growth rate over the past decade, an aging population and high levels of debt, to more recent concerns, including the economic slowdown following the repeal of the zero-tolerance COVID policy and the downturn in the pivotal real estate sector. These persistent and unresolved issues have markedly impacted consumer confidence, which sunk in mid-2022 and has failed to sustainably recover since. In our view, the weak economic sentiment, along with issues around housing affordability, significantly explains the sluggish dynamics of the housing market, despite the introduction of policy measures aimed at improving conditions. These measures, which include the planning and construction of affordable housing and the relaxation of residential housing loan rules implemented since last summer, have yet to produce the intended effects, with key residential market indicators neither signaling a turnaround nor showing any positive response, even temporarily. As of December, new home prices have continued their monthly decline since June, following a brief five-month period of increase. This trend is more pronounced in the annual data, with prices continuously decreasing since April 2022. A similar pattern is observed in annual residential property sales, which have been declining since August. This reflects the broader economic challenges, as evidenced by the performance of all the PMIs since last spring. Despite a few upticks, the general trend shows that after a peak in March 2023, coinciding with the end of the zero-COVID policy, both manufacturing and service sector PMIs have struggled to remain above the 50 threshold which separates expansion from contraction. By December 2023, the official manufacturing PMI stood at 49.2, a slight improvement of 0.2pts, and the Caixin services index was below market expectations and slightly worse than the previous month, although still above the 50. This suggests that the positive impact of the lunar new year festivities on the services sector may not be as strong as previously expected. In conclusion, the economy is at a crossroads, with market participants waiting for effective policy interventions.

Figure 8: The recent rout in equity markets ..



Source: Bloomberg, Eurobank Research

Figure 9: ..reflects the loss of consumers' confidence



Source: Bloomberg, Eurobank Research

Japan

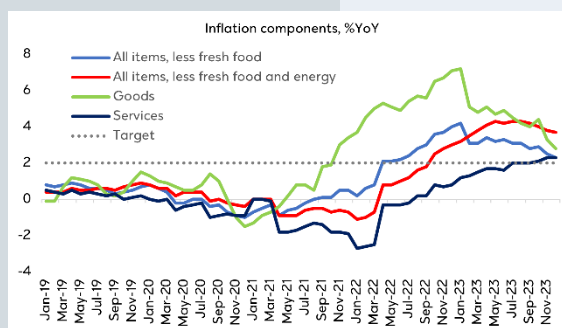
As shunto negotiations get underway, BoJ signals that rate hike is approaching

The Bank of Japan took a slightly more hawkish turn in January, signalling the strong likelihood that it will finally end its negative rate policy in the coming months. Ironically, the shift came as recent data underlined what a challenge it will be for Japan to achieve sustained, demand-led inflation at the target 2% level over the long-term. Headline CPI growth slowed 0.2ppts to 2.6%YoY in December, while core CPI inflation, which excludes fuel but includes energy, decelerated to 2.3%YoY from 2.5%YoY. Separately, the Tokyo headline CPI index – a leading indicator for nationwide data – increased 1.6%YoY January, down from 2.4%YoY the month before. Labour cash earnings increased 1.0%YoY in December after gaining 0.7%YoY the month before, with December's real earnings falling 1.9%YoY – marking 21 straight months of decline. Meanwhile, retail sales increased 2.1%YoY in December and actually shrank by 2.9%MoM, while industrial production fell 0.7%YoY. Apart from the national inflation releases, in each of these cases the data released came in lower than consensus estimates, highlighting that the Japanese economy is far from roaring on all cylinders. However, for Japan's central bank policy makers, the key variable seems to be that services inflation is on a steady uptrend. This was also reinforced by January's services PMI print, which increased 0.4ppts to 53.1, helping to boost the composite PMI by a similar amount to 51.5. Manufacturing PMI was unchanged at 48 – below the 50 threshold separating expansion and contraction. But the most important factor behind the BoJ's optimism that it can normalise monetary policy is the expectation that the *shunto* spring wage negotiations between the country's larger corporations and trade unions, which have just got underway, will secure larger pay increases than last year's historic rises, and that these will then set the trend for smaller companies. This expectation came through in the published summary of the BoJ's January meeting, where the governor also signalled that conditions for ending monetary stimulus were coming into place. One policy maker even remarked that failing to act soon may mean missing out on the chance to do so in this cycle, according to the summary. Derivatives markets currently imply a 77.1% chance of a hike by April's meeting, which would bring the policy rate to zero from -0.1%.

Figure 10: Recent economic data releases have mostly surprised to the downside

Source: Bloomberg, GS, Eurobank Research

Figure 11: Japanese services inflation remains on a steady uptrend



Source: Statistics Bureau of Japan, Eurobank Research

Euro area

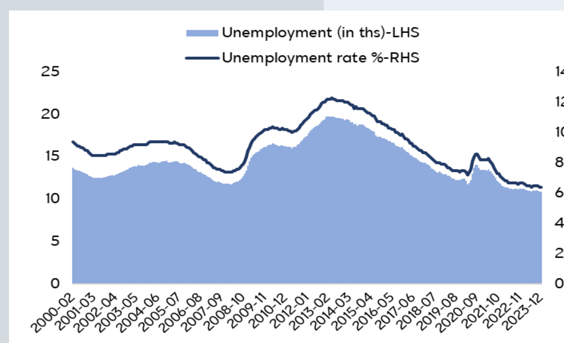
Struggles of region's ailing giants weigh on currency bloc's economy

A picture of two-speed economy is emerging in the euro area, with the region's two biggest economies driving stagnation in the currency bloc and countries on the periphery outperforming. For the eurozone as a whole, real GDP was flat in Q4 2023 after a 0.1%QoQ contraction in the previous quarter, meaning that a technical recession was narrowly avoided. Nevertheless, the flat print indicates that the economy has effectively been stagnant over the last five quarters. A breakdown by components is not yet available, but information from several countries points to weak domestic demand – probably driven by investment, reflecting the impact of tight monetary policy and subdued global industrial activity. Germany continued to be the biggest driver of economic weakness in the Eurozone, contracting 0.3%QoQ as French output was unchanged on a quarterly basis. The economies of the Iberian Peninsula were the strongest performers – partly thanks to the post-Covid normalization in tourism – with Portugal growing 0.8%QoQ in the last quarter of 2023 and Spain's GDP increasing 0.6%QoQ. Activity data suggests that the Eurozone economy will continue to be weak in the coming quarters. Industrial production dropped by 0.3%MoM in November, the third consecutive monthly drop, leaving the October-November average 1.3% below the Q3 average, while retail sales declined by 1.1%MoM in December. That was the biggest monthly drop since late last year and underlined the weakness in private sector domestic demand at the end of last year. There was one encouraging note from a modest improvement in January's flash composite PMI, kindling hope that economic activity may be at or near its trough. Meanwhile, labour markets remain tight and wage growth elevated. If disinflation continues, improved household purchasing power should help economic activity gain some momentum later this year. Both headline and core inflation decelerated further in January – though slightly less than expected – to 2.8%YoY and 3.3%YoY respectively. Unemployment fell by a further 17k in December to a record low of 10.909mn, and compensation per employee rose by 5.3%YoY in Q3 2023. Against this backdrop, ECB President Lagarde said she wants to see stronger evidence that inflation is on a sustained path towards its 2% target before easing monetary policy. However, in her comments after the January policy meeting, she did implicitly leave open the possibility of a rate cut in Q2.

Figure 12: Eurozone narrowly avoids recession, but big divergence between countries

Source: Eurostat, Eurobank Research

Figure 13: Tightness in labour markets persists despite economic stagnation



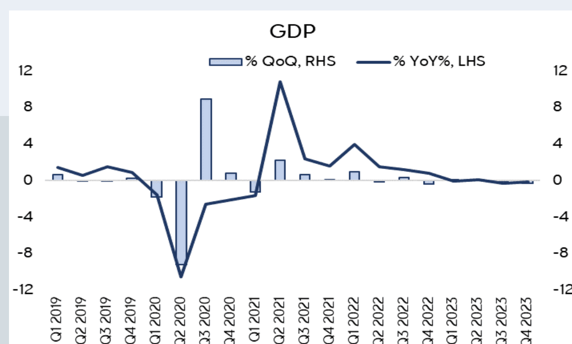
Source: Eurostat, Eurobank Research

Germany

No sustained near-term recovery in sight after Q4 2023 GDP contraction

Real GDP contracted by 0.3%QoQ in Q4 2023 according to the flash estimate, confirming the estimate implied by the Federal Statistical Office when it provided the flash GDP release for the full year 2023 in mid-January (a detailed expenditure and production breakdown for Q4 GDP is due on February 23). The economy avoided a technical recession, however, as the Q3 reading was revised up by 0.1ppts to 0.0%QoQ. Nevertheless, Germany's long spell of stagnation continues, with GDP having grown by an average 0.1%QoQ since autumn 2021 mainly on the back of high domestic energy costs, the still unfolding effects of past ECB rate tightening and subdued global industrial activity. Future growth prospects are gloomy and the risk of a further GDP growth contraction in Q1 2024 cannot be ruled out, as lacklustre sentiment indicators suggest. Both the composite PMI and the headline IFO business climate unexpectedly dropped in January (-0.4pts and -1.2pts respectively to 47 and 85.2), probably on the back of persistent uncertainty around fiscal budget cuts following the constitutional court's ruling late last year, farmer protests, a large-scale rail strike and manufacturer fears over input shortages due to Red Sea shipping disruptions. High-frequency indicators add to concerns that a strong recovery is still some way off.

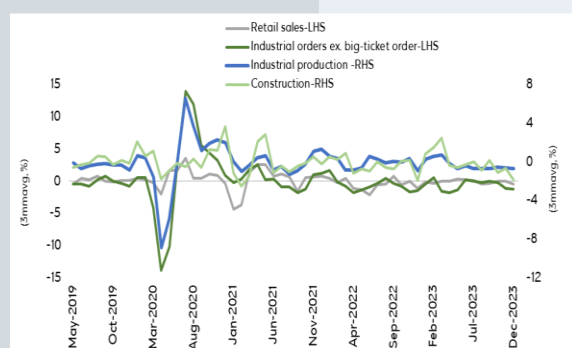
Figure 14: Quarterly GDP growth averages 0.1% since Q4 2021



Source: Destatis, Eurobank Research

New manufacturing orders — excluding volatile big-ticket orders — remained on a downward trend in December falling to the lowest level since early 2021. The slump in orders has weighed heavily on industrial production, declining by 1.6%MoM in December, the sixth drop in the last eight months, and 1.5% lower for the full year 2023. A similar gloomy picture emerges from construction amid tight financial conditions and a shrinking order backlog, with overall building permits down 3.6% in Q4 compared to the Q3 average. Meanwhile, retail sales fell by 1.6%MoM in December, the second straight monthly decline, and another strong hit in GfK consumer climate index, from -25.1 to -29.7 in January, does not bode well for hopes of a strong growth rebound soon. Overall, we expect only a marginal pickup in growth momentum in H2 on the back of easing financial conditions (the ECB is expected to start cutting rates in June), a modest improvement in global trade activity and increased real wage growth that would support private consumption (HICP inflation is seen more than halving in 2024, from 6.1% in 2023, while the Bundesbank projects a 5% pay growth in 2024, including one-off payments). For the full year 2024, GDP is seen contracting 0.1%.

Figure 15: No sustained near-term recovery in sight



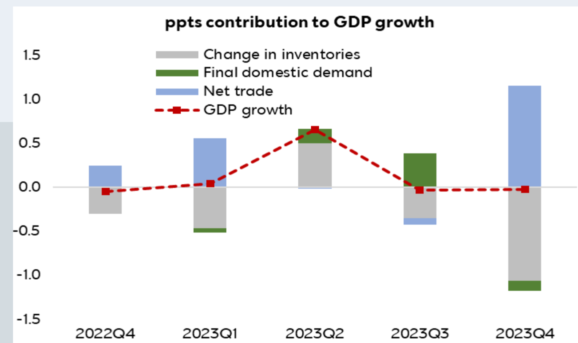
Source: Destatis, Eurobank Research

France

Indicators offer few hopes for an end soon to economy's malaise

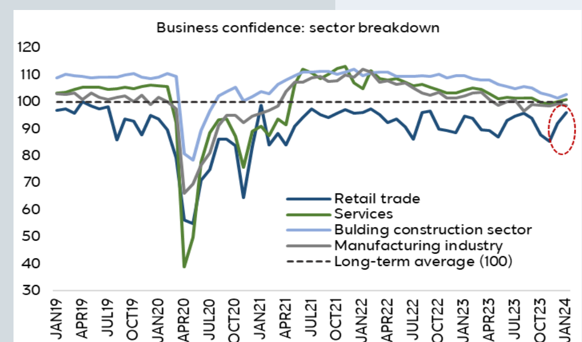
Weak domestic demand left the French economy in a deep funk in Q4 2023, even as it managed to narrowly escape a technical recession. Real GDP stagnated for a second quarter straight, after the Q3 figure was revised to flat from its previous reading of -0.1%QoQ. For the full year, the economy expanded 0.9%, with GDP stagnating in each quarter of the year except for Q2 2023, when it grew 0.7%QoQ. The expenditure breakdown for the latest GDP print reflected broad-based weakness across all the main components. Final domestic demand subtracted 0.1ppts from GDP growth due to a mild contraction in personal consumption (-0.1%QoQ compared with +0.5%QoQ in Q3) and a sharp fall in gross fixed investment (-0.7%QoQ compared with +0.2%QoQ in Q3). Inventories made a negative contribution for the second consecutive quarter (-1.1ppts). The only thing that prevented GDP from contracting was net trade, which added 1.2ppts to growth. However, this can also be traced back to the weak state of domestic demand, as the contraction in imports (-3.1%QoQ) outpaced that of exports (-0.1%QoQ). Looking to Q1 2024, economic stagnation will likely continue as lackluster forward-looking indicators provide little hope for an imminent strong recovery. The INSEE business climate indicator slightly improved in January, rising by 0.5pts to 98.4, along with household confidence, which increased 2pts to 91. However, both are still below their long-term average of 100, and the PMI surveys present an even worse picture. January's composite PMI remained below the 50 threshold, dropping by 0.2pts to a two-month low of 44.6. That is because an improvement in the manufacturing PMI, which increased 1pt to 43.1, was fully offset by a further decline in services PMI to 45.4 from 45.7. Economic activity is not expected to gain momentum before H2 2024, with full-year GDP growth projected at 0.8%, led by a rebound in household spending. This should be the result of slightly improving purchasing power as inflation declines, partially offsetting the stifling effects of tighter credit conditions on gross fixed capital formation. EU-harmonised inflation continued to slow in January, down to a lower-than-expected 3.4%YoY from 4.1%YoY the month before. Looking ahead, inflation is expected to decelerate further towards 2%YoY by year-end, though the downward path is likely to be bumpy due to less favourable base effects and the withdrawal of government support measures for energy bills.

Figure 16: Only reduced imports prevented GDP from contracting in the last quarter of 2023



Source: INSEE, Eurobank Research

Figure 17: Fragile retail sentiment improved in January, but still lags other sectors



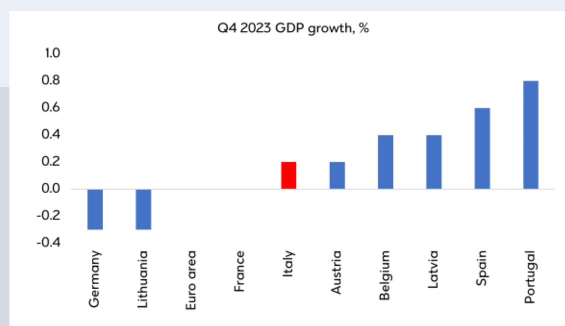
Source: INSEE, Eurobank Research

Italy

Economy shows resilience as unemployment rate falls to lowest since 2008

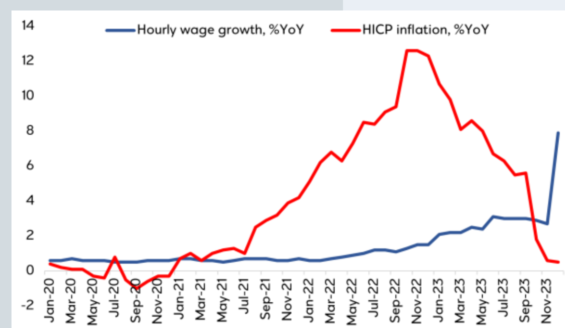
Surprise growth in the last quarter of 2023 showed that there is still some life in the Italian economy. It also helped set apart the euro area's third largest economy from those of Germany and France – the two bigger than Italy's – which are driving the currency bloc's current malaise. GDP grew 0.2%QoQ and 0.5%YoY in Q4, which brought the overall 2023 growth to 0.7%. The preliminary release did not give a breakdown by components, but noted there was a positive contribution to quarterly growth from the external sector. The positive quarterly growth in Q4 meant a carry-over effect of +0.1% going into 2024, leading us to revise up our estimate for this year's GDP growth to 0.6%. There is also positive news in Italy's labour market that gives cause for optimism that the expected slowdown this year will be mild. The unemployment rate dropped to 7.2% in December from a downwardly revised 7.4% the month before, bringing it down to its lowest level since 2008. There was also a 7.9%YoY spike in hourly wages, the most on record. However, that was largely due to a 22.2%YoY increase for government employees, which in turn was due to the advance payment of an allowance compensating them for a delay in the renewal of their national contract. That one-off element means that it is probably not indicative of sustained wage pressure – indeed, annual wage growth slowed in each of the previous two months, coming down to 2.7%YoY in November – and does not pose a threat to inflation remaining under control. EU-harmonised consumer prices increased 0.9%YoY in January compared with 0.5%YoY the month before, a slight upside surprise, while core inflation continued its downtrend as it slowed 0.2ppts to 2.8%YoY. The improving labour market and slowing inflation probably helped drive Italy's Q4 resilience. Household consumption was the main contribution to Q3 GDP growth, and retail sales increased 10%QoQ in the last quarter. The flip side is that industrial sector continues to be squeezed; although the manufacturing PMI did rise more than expected to 48.5 in January. That is still below the 50 level that separates expansion from contraction, but it was the highest reading in 10. Meanwhile, the services and composite PMI prints both crossed the 50 threshold in January. The services PMI increased to 51.2 from 49.8 and service providers reported that they hired additional staff. The composite print recorded its first output expansion in eight months as it increased to 50.7 from 48.6 in December.

Figure 18: Italy was among the euro-area countries reporting QoQ growth last quarter



Source: Eurostat, Eurobank Research

Figure 19: A December spike in hourly earnings was due to one-off factors



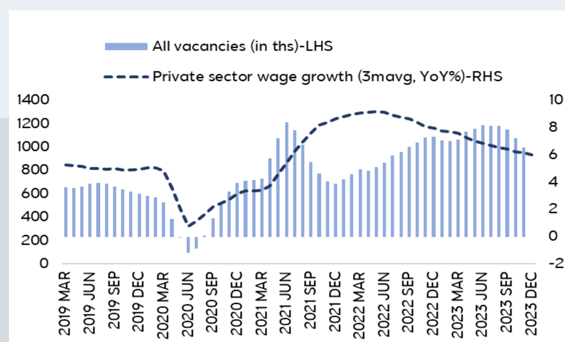
Source: Bloomberg, Eurobank Research

UK

Sentiment indicators suggest economy will improve in Q1

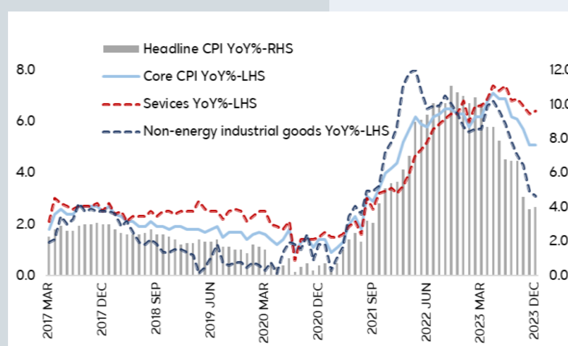
Supporting optimism for an acceleration in economic activity at the turn of the year, the January composite PMI moved further above the crucial level of 50. Boosted by a further strengthening in services activity (0.9ppts to 54.3), the composite index came in at an eight-month high of 52.9, up by 0.8ppts from December and 4.4ppts cumulatively from September 2023 lows. Adding to recent evidence flagging an improvement in growth momentum, GfK consumer confidence increased in January for the third straight month, +3ppts to -19, the highest level since December 2021. Undoubtedly, this contrasts sharply with the hefty -3.2%MoM drop in December's retail sales, following a 1.4%MoM gain in November. However, this was likely due to a fall in discretionary spending, as consumers probably brought forward some of their December spending to November to benefit from Black Friday sales. That said, December's fall in retail sales is anticipated to be reversed in the coming months, leaving unchanged our expectations for a modest positive GDP growth rate to the tune of 0.1%-0.2%QoQ in Q1 2024. Though still sub-trend, that pace of GDP growth would mark a clear improvement from the state of near stagnation in H2 2023 and the flat average quarterly growth rate between Q2 2022 and Q3 2023. Meanwhile, house prices are rising (the average price of residences increased up by a one-year-high of 4.6%QoQ in Q3 2023) and the labour market is still tight overall. Vacancies continued their downward trend in December (-17k to 934k), but still stand well above pre-pandemic levels. Private sector regular pay — the BoE's preferred gauge of the labour cost — dropped in November to a more than a year low of 6.5% 3mmavg/YoY from 7.2%YoY in October and a peak of 8.2%YoY in June 2023, though still far above the 3-4%YoY range consistent with inflation at 2.0%. Meanwhile, fueling worries that the road to the BoE's target will likely be bumpy, headline CPI unexpectedly accelerated in December from 3.9%YoY to 4.0%YoY and core was unchanged at 5.1%YoY, as services inflation rose from 6.3%YoY to 6.4%YoY, while non-energy industrial goods inflation continued to decline, from 3.3%YoY to 3.1%YoY. Against this backdrop, the BoE made clear at the February 1 policy meeting that it needs more evidence to gain confidence in the downward inflation and wage growth trajectory before it starts easing. Markets do not price-in fully the first rate cut before August 2024.

Figure 20: The labor market is loosening, but fairly gradually



Source: ONS, Eurobank Research

Figure 21: CPI inflation edged up unexpectedly in December, partially due to an uptick in services



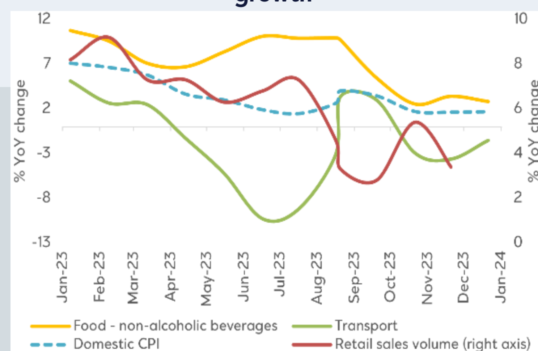
Source: ONS Eurobank Research

Cyprus

Improved investment prospects from RRF inflows and return to credit expansion

Domestic CPI increased annually in January by 1.7%, almost at the same pace as in December (1.6%), remaining for a third consecutive month below 2%, with the monthly decline accelerating to 1.2% from 1.0%. These weaker inflation dynamics on the back of the disinflationary measures in force since November/December support household consumption growth, as is reflected in the volume of retail sales that grew by 5.4%YoY and 3.4%YoY in these two months, respectively, exceeding the average increase in September-October (+3.0%YoY). However, retail sales growth weakened in Q4 2023 relative to the previous quarter, to 3.9%YoY from 5.1%YoY, which is expected to weigh on private consumption and GDP growth in the latest quarter.

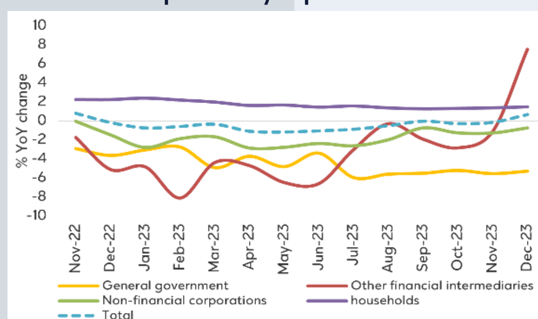
Figure 22: Weaker inflation dynamics on the back of the disinflationary measures in food and fuels items support household consumption growth



Source: CYSTAT, Eurobank Research

Nonetheless, the disinflationary policies that are withdrawn in May will sustain real disposable income and household consumption increases in H1 2024, which are expected to be supported throughout this year mainly by stronger partial wage indexation and a tighter labour market. Despite higher growth in tourist arrivals in December relative to November (+12.3%YoY from +6.5%YoY), the rise continues to lag the average increase in January-September last year (+23.4%YoY), mainly due to the change of trend in arrivals from Israel during the war in Gaza, which kept strongly falling in December (-40.9%YoY), in contrast to +77.7%YoY in 9M2023. The spike in tourist inflows from EU countries in December (+30.9%YoY vs. +19.0%YoY a month earlier), which accounted for most of the overall increase, rises the possibility of covering a significant part of the reduced arrivals from Israel in case the war continues. On the investment side, after the cooling of the RRF installments in 2023, the MinFin recently announced that up to April grants of €152.2mn will be disbursed (2nd-3rd RRF installment), while later this year two more requests will be submitted, for the disbursement of the 4th and 5th installment (in total €197mn). Another €20.9mn were channeled to Cyprus in the context of the REPowerEU plan, adding to the investment financing firepower.

Figure 23: Credit expansion in December after 13 months, raises hopes for improved financing conditions for businesses earlier in 2024 than previously expected



Source: Central Bank of Cyprus, Eurobank Research

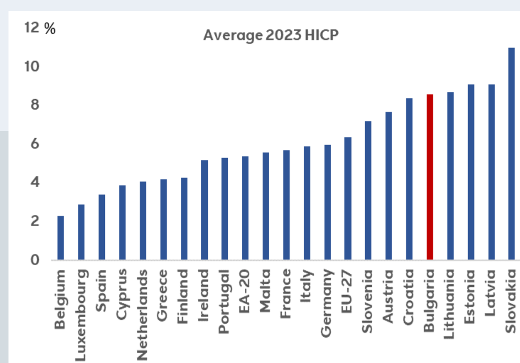
A return to credit expansion in December after 12 months, mainly from higher credit supply towards other financial intermediaries, as well as a milder credit contraction towards non-financial corporations (-0.7%YoY vs. -1.3%YoY a month earlier), could imply improved financing conditions for businesses earlier in 2024 than previously expected, provided this trend continues. Considering the above, our growth forecasts for 2023 and 2024 remain unchanged to 2.3% and 2.7%, respectively.

Bulgaria

Slow convergence on prices threatens country's timely adoption of the euro

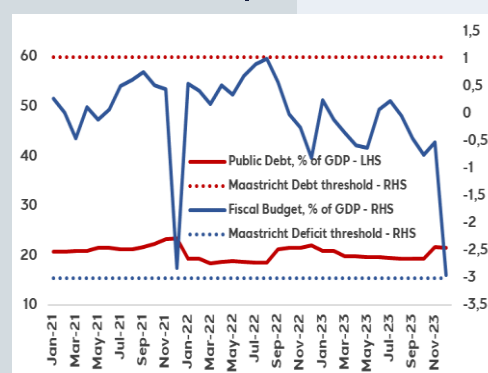
Data releases were without surprises in the past few weeks, meaning that the most significant economic development instead was Prime Minister Nikolay Denkov hinting that Bulgaria's entry into the euro area will probably be delayed. This was reported by local media late last month, with the implication being that entry would be delayed for about six months from the current timeline that sees the country joining the common currency in January 2025. The reason for the delay would be slow convergence with the rest of the eurozone in the rate of price growth – despite the impressive disinflation seen last year in Bulgaria. Overall, last year HICP grew at an average rate of 8.6%, compared with 13.0% in 2022, with the prospect of further disinflation this year bringing the rate below 4%. However, there is still a way to go to return to price stability or even approach the Eurozone average (8.4% in 2022, 5.4% in 2023, forecast for 2024 of 3.2%), which will determine to a crucial extent the country's entry into the Eurozone. That said, the inflation criterion is not fulfilled for 2023 as the 8.6% HICP FY2023 average is considerably higher, almost double in fact, than the ceiling of 4.4% that the average of the best three performers (average HICP of Belgium, Luxembourg and Spain at 2.9% plus the granted margin of 1.5%) imposes. Still, the fiscal performance both on the budget deficit and the public debt front is well anchored with the requirements of convergence and it is set to remain on track in 2024. The budget deficit target for 2024 is set at 2.9% of GDP, up from 2.2% in 2023 while public debt as percentage of GDP ended up to about 22% in 2023, with figures for at least the past five years hovering around these levels. In other data, retail trade growth cooled down to 0.7%YoY in December from 3.2%YoY in the previous month while industrial production data for December are about to be published. On a monthly basis the retail trade volume contracted by 0.6%, a bit more pronounced from the 0.2%YoY contraction in November. When the Q4 2023 GDP print is released in mid-February, it is expected to show that growth cooled to 1.9% last year from 3.9% in 2022. A mild rebound to 2.5% is anticipated in 2024, mainly driven by a sustained positive momentum in investment, which emerged in Q3 2023 and is expected to extend into Q4 2023 and this year. Overall, risks for 2024 continue to be balanced and the lack of recent surprises in the data means that we maintain our forecasts for 2024 unchanged.

Figure 24: Slow convergence on prices poses delays on the Euro adoption...



Source: Eurostat, Eurobank Research

Figure 25: ...despite the cemented fiscal discipline



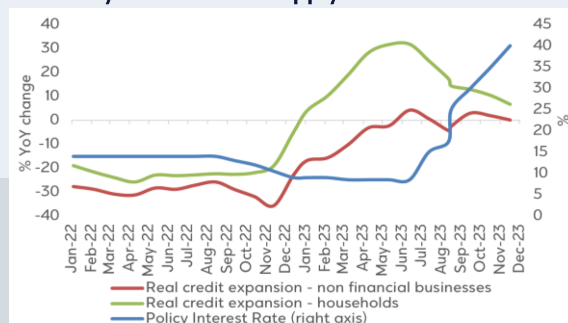
Source: NSI, Eurobank Research

Turkey

Inflation continues rising amid monetary tightening conclusion

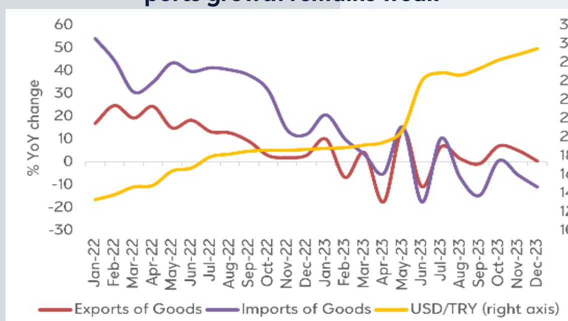
Despite aggressive monetary policy tightening since July 2023, headline annual inflation rose by a tad in January relative to December, to 64.9% from 64.8%, a 14-month high, with the monthly pace accelerating to 6.7% from 2.9%. The main factors sustaining rampant inflation are the lira devaluation, that accelerated further in January (-60%YoY vis-à-vis USD from -55.9%YoY in December) –an indication of the low market confidence to the ultra-tight monetary policy – but also the new private sector minimum wage and public sector salary raises as of January (+49.1% and +46.5%, respectively). The latter development is expected to only temporary mitigate the inflationary pressures on household consumption, as previous similar increases eventually fed into higher prices of goods and services. Indicatively, despite such rises in July 2023, as well as increases in pensions, growth in retail sales volume is weakening since August, falling to 12.8%YoY in November, a 12-month low. On the other hand, as mentioned in previous issues, labour market tightening, with the unemployment rate in 2023 expected at a 10-year low (ca 9.4%) and projected to move further lower in 2024, will provide a firmer support to household consumption. The conclusion of the monetary tightening cycle in January with another base rate hike by 250bps that brought it to 45.0%, and the central bank's (TCMB) accompanying statement that this level of monetary tightness will be maintained until there is a strong declining trend in the monthly inflation, could make monetary policy more reliable, provided the TCMB does not deviate from this line. The recent change in the TCMB governor is not expected to have an impact on the monetary policy stance, as her successor has already stated that he will maintain the necessary monetary tightness until inflation falls to levels consistent with the medium-term TCMB target (5%). Soaring lending rates are expected to weigh on investment and consumption, as credit growth towards non-financial businesses (PPI adjusted) was minimal in December (0.1%YoY) from 4.2%YoY in June, whereas towards households (CPI adjusted) it fell to 6.7%YoY from 31.8%YoY. On the flipside, the reconstruction process after the February 2023 earthquakes will continue significantly boosting investment and employment. Signals from the external sector of the economy remain mixed as to the effects of the lira devaluation, as annual growth in income from tourism decelerated further in Q4, whereas the goods trade balance improved in December, but mainly due to the strong fall in imports (-11.0%YoY) as exports expanded marginally (+0.4%YoY). Given the above, our growth forecasts for 2023 and 2024 remain unchanged to 4.2% and 3.2%, respectively.

Figure 26: Monetary policy tightening weighs mainly on real credit supply towards households



Source: Central Bank of Turkey, Eurobank Research

Figure 27: The lira devaluation improves the goods trade balance mainly through falling imports, as exports growth remains weak



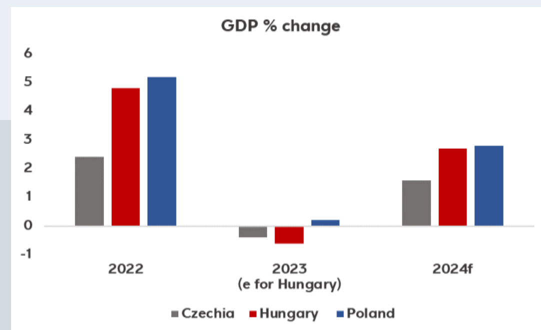
Source: Turkstat, Central Bank of Turkey, Eurobank Research

CESEE

Poland saves the day in the CEE3, achieving positive growth in 2023

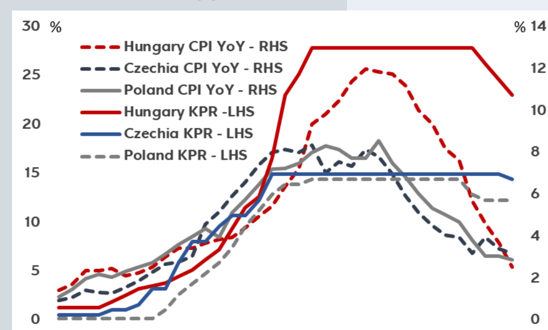
The majority of the region's countries are set to release Q4 2023 GDP flash estimates by mid-February. Among those that have already reported, the Czech economy contracted 0.4% in 2023 after expanding 2.4% in 2022 but we expect it to rebound and grow 1.6% this year, though, on a milder pace than its two closer peers, Poland and Hungary. Based on the first estimate for 2023 by the Polish statistics bureau, the growth rate fell to 0.2% in 2023 after a vigorous 5.3% expansion the year before, but it is projected to recover to a pace of 2.8% in 2024. As we wait for Hungary's Q4 report next week, we estimate that economic output contracted 0.6% in 2023, after 4.8% growth in 2022, and forecast a recovery to 2.7% for this year, following a similar trajectory to Poland. Examining the average consumer price growth in the CEE3 economies, Hungary — which lagged the other economies in economic output — also faced more persistent inflation, with the average rate of HICP increases accelerating to 17% in 2023 from 15.3%, whereas in Czechia and Poland inflation was somewhat curbed. In Czechia, inflation retreated to 12.0% in 2023 from 14.8% in 2022 and in Poland to 10.9% from 13.2% respectively. The level and persistence of inflation among these three economies explain quite straightforwardly the monetary policy stances adopted by their respective central banks in 2023. The Hungarian central bank tightened more aggressively compared with its two counterparts, having also paid a heavier economic toll in terms of growth. Key policy rate (KPR) in Hungary peaked to 13.0% in September 2022 from 0.6% in 2021 and has been gradually cut in the last quarter of 2023 to 10.0%. On the flipside, monetary tightening was not required to be that steep in Poland and Czechia with KPRs starting from levels below 1% back in 2021, peaking close to 7.0% in August and landing to 6.75% in Poland and 5.75% in Czechia currently. Following the retrospective narrative for 2023 which endeavors to link roughly the course of growth, inflation and monetary policy in the CEE3, prospects for 2024 may continue to be challenging, for the reasons outlined in our previous issue and the respective regional outlook for 2024 but appear brighter as the broadly waning inflation and the accommodative monetary easing to follow will foster growth dynamics.

Figure 28: Hungary's expected 2023 GDP contraction got deeper...



Source:Eurostat, Eurobank Research

Figure 29: ..on the back of stickier inflation and more aggressive monetary policy



Source: local statistics bureaus and central banks, 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)		
	2023e	2024f	2025f	2023	2024f	2025f	2023e	2024f	2025f	2023e	2024f	2025f	2023e	2024f	2025f
World	3.1	2.7	3.0	6.8	4.1	3.5									
Advanced Economies															
USA	2.5	1.5	1.7	4.1	2.7	2.3	3.6	4.1	4.2	-3.1	-3.0	-3.0	-6.5	-6.0	-6.2
Eurozone	0.5	0.5	1.4	5.5	2.3	2.1	6.5	6.8	6.7	1.7	1.7	1.8	-3.3	-3.0	-2.7
Germany	-0.3	-0.1	1.0	6.1	2.6	2.2	5.7	6.0	5.8	6.2	6.5	6.1	--2.3	-1.6	-1.4
France	0.9	0.8	1.3	5.7	2.6	2.0	7.3	7.4	7.4	-1.2	-1.0	-0.7	-4.9	-4.5	-4.3
Periphery															
Cyprus	2.3	2.7	3.0	3.9	1.8	1.2	6.2	5.8	5.5	-11.5	-8.0	-7.0	3.4	3.7	3.2
Italy	0.7	0.6	1.1	6.0	2.0	1.9	7.6	7.8	7.6	0.3	1.0	1.2	-5.4	-4.5	-4.0
Portugal	2.3	1.2	2.1	5.3	2.5	2.0	6.5	6.6	6.3	1.5	1.2	1.5	0.7	0.1	0.0
Spain	2.5	1.4	1.8	3.4	2.8	2.2	12.1	11.8	11.6	2.2	1.9	1.9	-4.0	-3.4	-3.1
UK	0.3	0.4	1.2	7.4	2.8	2.1	4.2	4.6	4.7	-2.8	-2.4	-2.5	-4.6	-3.6	-3.0
Japan	2.0	0.8	1.0	3.3	2.2	1.7	2.6	2.5	2.4	3.4	3.4	3.5	-5.2	-4.1	-3.4
Emerging Economies															
BRICs															
Brazil	3.0	1.6	2.0	4.6	3.9	3.5	8.0	8.2	8.4	-1.4	-1.6	-1.7	-7.9	-7.0	-6.3
China	5.2	4.6	4.4	0.2	1.1	1.7	5.2	5.1	5.1	1.7	1.2	1.1	-5.6	-5.0	-5.1
India	6.8	6.3	6.5	5.4	4.9	4.6		NA		-1.4	-1.5	-1.6	-5.9	-5.4	-5.1
Russia	3.1	1.6	1.0	6.0	6.3	4.5	3.2	3.1	3.2	3.4	3.5	3.1	-2.8	-2.2	-1.6
CESEE															
Bulgaria	1.9	2.5	2.9	9.6	3.7	3.1	4.3	4.5	4.4	-0.4	0.5	0.6	-2.2	-2.9	-2.9
Turkey	4.2	3.2	3.5	53.4	46.6	33.2	9.4	8.9	8.6	-5.4	-4.8	-4.0	-6.3	-5.6	-2.5

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

Eurobank Fixed Income Forecasts

	Current	March 2024	June 2024	September 2024	December 2024
USA					
Fed Funds Rate	5.25-5.50%	5.23-5.5%	4.92-5.15%	4.5-4.75%	4.11-4.35%
3m SOFR	5.32%	5.29%	5.00%	4.64%	4.27%
2yr Notes	5.5%	5.5%	5.15%	4.75%	4.35%
10yr Bonds	5.25%	5.23%	4.92%	4.5%	4.11%
Eurozone					
Refi Rate	4.50%	4.45%	4.2%	3.9%	3.6%
3m Euribor	3.92%	3.92%	3.67%	3.4%	3.16%
2yr Bunds	2.6%	2.64%	2.44%	2.31%	2.23%
10yr Bunds	2.31%	2.31%	2.2%	2.19%	2.21%
UK					
Repo Rate	5.25%	5.25%	5.05%	4.7%	4.3%
3m Sonia	5.21%	5.18%	4.88%	4.63%	4.35%
10-yr Gilt	4.01%	3.9%	3.81%	3.72%	3.62%
Switzerland					
3m Saron	1.65%	1.73%	1.61%	1.48%	1.36%
10-yr Bond	0.89%	0.87%	0.89%	0.87%	0.89%

Source: Bloomberg (market implied forecasts)

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