WEEKLY ANALYSIS

NUMBER 807, FEBRUARY 6, 2023

ECB increased interest rates by 50 bps

- In line with the ECB accounts published last month, at last week's meeting the ECB increased all three key interest rates by 50 bps. Interest rate for deposits (DFR) will be 2.50% from 8 February, for main refinancing operations (MRO) 3.00% and for overnight credits (MLR) 3.25%.

ESB plans in March to raise interest rates again by 50 bps

- The ECB announced it plans to raise, again, interest rates by 50 bps at its next meeting in March, but the trajectory afterwards is unclear. The ECB stands by its not overly clear formulation in „raising interest rates significantly at a steady pace and in keeping them at levels that are sufficiently restrictive to ensure a timely return of inflation to its 2% medium-term target “. Inflationary pressures continue to wane according to Eurostat's flash estimate for January showing that the total inflation rate in the Eurozone is lower y-o-y for the third consecutive month (January 8.5%) and took a negative turn m-o-m (January: -0.4%), but the trajectory of the core inflation is not so unambiguous due to pronounced pressures on the demand side backed by strong labour market. The ECB is thus carefully tracking salary trends for which it expects it will be a significant inflationary pressure generator in the upcoming period. Inflation is still far higher than the level acceptable for the central bank and shall remain increased for a long time still, so it is very probable that the March increase will not be the last one. Rather, we expect that following this, key rates will be raised by additional 50 bps, 25 bps in May and 25 bps in June, thus making the deposit rate reach 3.50%. We see it as the final point where interest rates will hold for a longer period, until inflation starts a permanent downward trend and draws close to the desired level.

After March, we expect interest rate increase by further 50 bps

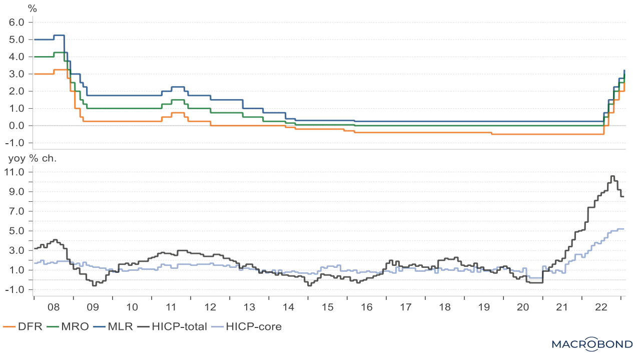
- As to quantitative tightening, there were no changes and it was repeated that the reduction of reinvestment of principal of maturing securities from March to the end of June will be € 15 billion per month, and with time, a decision on the reduction dynamic after June will be made. Regarding purchases of corporate bonds, the novelty is that the remaining reinvestment will mostly be focused on investors who are “greener”, i.e., more climate neutral, in line with ECB climate plan for promoting sustainable financing so as to support an orderly transition towards low-carbon economy.

- The ECB assessed the current economic outlook as more favourable than in December due to GDP growth in the Eurozone in Q4 2022 and the decline of energy prices. This is one of the reasons why Mrs Lagarde stated at the press conference it is possible that member states will be advised to adjust fiscal support measures in line with lower energy prices, to prevent from stoking the flames of demand.

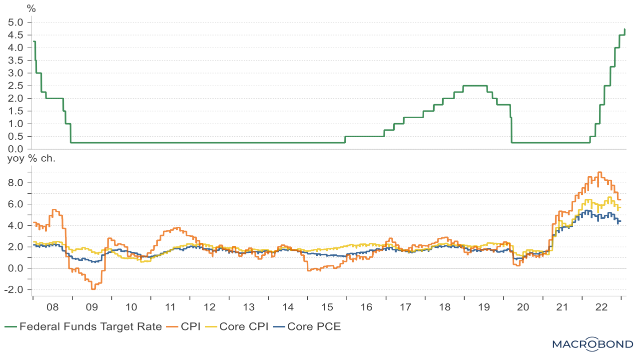
Fed raises the rate by 25 bps to 4.50-4.75%

- A day before ECB's meeting, Fed held a meeting at which, after the initial easing of the pace of interest rate hike in December to 50 bps, further slowdown occurred so the target range for fed funds rate was hiked by 25 bps (to 4.50% up to 4.75%). Fed announced further interest rate hikes which imply that the easing of monetary policy hoped for by the markets is still not in sight neither in the Eurozone nor in the U.S.

Euro Area: ECB interest rates and inflation



USA: Federal funds rate and inflation

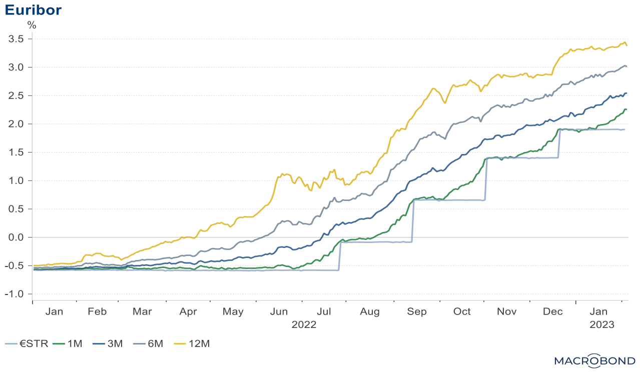


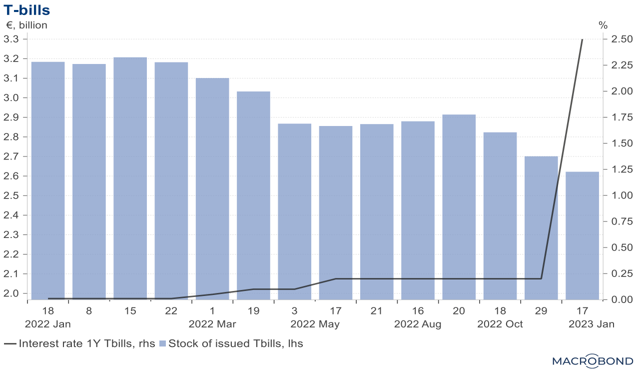
- First inflation assessment for January points to prices stagnating m-o-m (considering that estimated price growth for food products and services was offset by price decline for industrial products i.e., non-food products and energy), which reduced the annual inflation rate to 12.7% (from 13.1% recorded in December).

- After the Fed and ECB's meetings where interest rates were raised in line with expectations, EUR/USD exchange rate continued its mild increase. On Friday it was 1.0937 dollar to the euro, up by 0.7% w-o-w.

- Euribor changed only slightly last week, up to 10 bps w-o-w, so on Friday 3M rate was 2.5%, and 6M rate 3.0%. This week € 234 million of T-bills is due and an auction is announced in the amount of € 220 million.

- Crobex dived again and finished the week down by 0.5% w-o-w, i.e., at 2,112.7 points due to decline of all the most important indices (CROBEXindustry -0.2% to 1,171.5, CROBEXnutris -0.7% to 797.7, CROBEXtourist -0.5% to 3,546.5). Crobis slightly increased by 0.1% to 94.8 points.





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