

WEEKLY ANALYSIS

Number 781, June 13, 2022

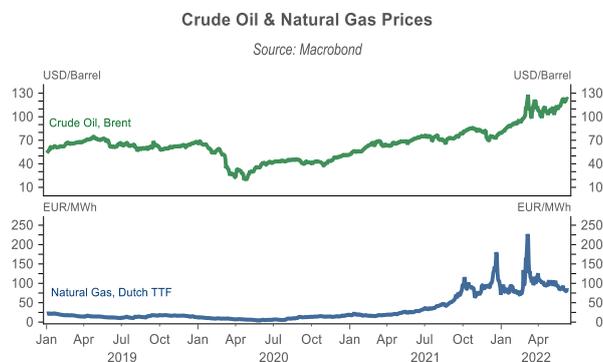
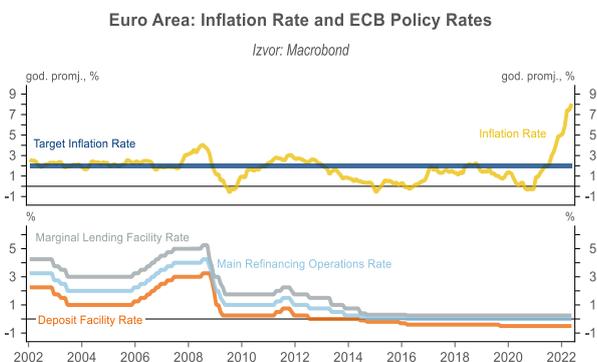
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ECB announces interest rate hike in July

Eurozone inflation rate in May reached a record 8.1% year-on-year according to a flash estimate. Details for last month are not yet available, but April data reveal that food prices have skyrocketed by 7.7%, housing by 15.9% and fuels by 29.4% year-on-year. At the end of May, the price of Brent crude oil was up by almost 80% year-on-year and the price of TTF natural gas by more than 270%. In the face of such strong inflationary pressures, it was evident that this year the ECB's March inflation forecast for the eurozone would be exceeded in both the baseline and the adverse scenario (5.1% and 5.9% year-on-year respectively) and that in the current circumstances the level of key interest rates is inadequate. The deposit facility rate is also negative in nominal terms, with all three of the key ECB interest rates in real terms deep in negative territory. Members of the ECB's Governing Council, including the leader Lagarde, had already before the June meeting openly announced an interest rate hike in the near term, but there were disagreements about whether it should start in July, as soon as net purchases are completed, or in September. There was also controversy over the pace of the increase, namely whether to start with a slightly bolder 50 b.b. or a moderate 25 b.b.

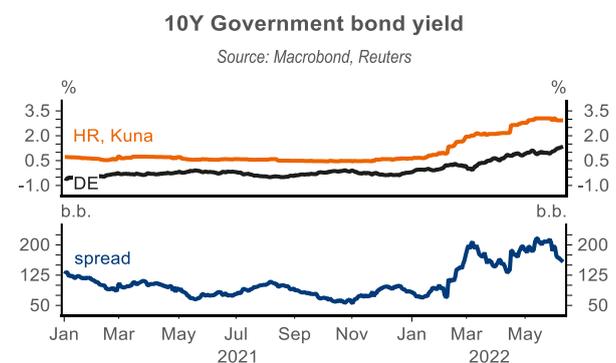
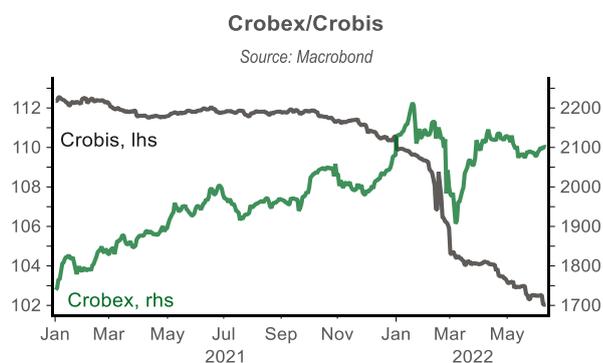
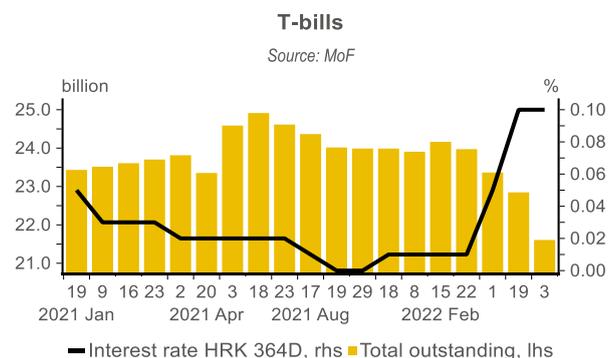
The dilemmas were resolved by last week's meeting of the Governing Council, which announced that key interest rates would be raised by 25 b.b. in July, as well as a further increase in September. Neither the possibility of a stronger hike of 50 b.b. in September has been ruled out, which will depend on the evolution of inflation: "If the medium-term inflation outlook persists or deteriorates, a larger increment will be appropriate at the September meeting." As regards the programmes of net purchases and reinvestment of maturing principal payments, it has been reaffirmed that the APP ends as of 1 July and reinvestment continues for as long as necessary (while the reinvestment of PEPP principal payments is planned at least until the end of 2024). So far, there is also no word on any new instrument to prevent the widening of bond spreads of peripheral EZ member states, other than to stress that the ECB knows "how to design and how to deploy new instruments if and when necessary".

In line with expectations, in the June macroeconomic projections, the European Central Bank cut the forecasted real GDP growth of the eurozone in 2022 and 2023 to 2.8% and 2.1%, respectively, while for 2024 it raised it to 2.1% year-on-year. At the same time, it revised its inflation projections up significantly, to 6.8% year-on-year in 2022, 3.5% in 2023 and 2.3% in 2024. It was clarified that inflationary pressures in the shorter term are expected to remain strong due to high oil and gas prices, and surging food prices pressured by the war in Ukraine, reopening of the economy and global supply-side constraints. At this point, it is very likely that in the next three months we will see a rate increase of 75 b.b., considering that the medium-term forecast of the inflation rate stands above 2% year-on-year. The cycle of increasing key interest rates has only just begun, as the ECB states that after September it will continue pursuing a "gradual but sustained path of further increases", and it is also possible for the difference in their respective levels to be reduced, which is currently 75 b.b. between the deposit facility and marginal lending facility rate.



Weekly overview

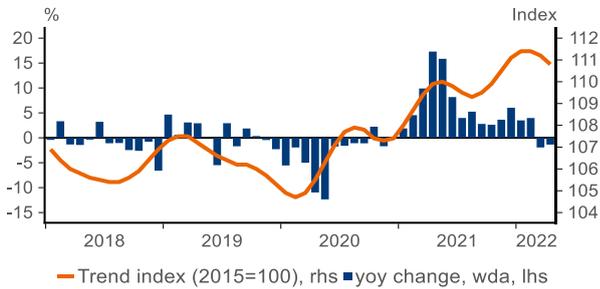
- Total exports of goods grew by 31.3% year-on-year in March, while imports simultaneously increased by 47.9%. The foreign trade deficit in the trade of goods thereby reached a record level of HRK 11.5 billion, which is also up by 79.6% year-on-year, while the coverage rate amounted to 58.4% (65.7% in March 2021).
- Last week, the kuna continued to appreciate slightly against the euro, and at the end of the week the mid-point exchange rate was down by 0.1% w-o-w at HRK 7.5181 per euro. Against the dollar, the kuna weakened by 1.3% and the exchange rate rose to HRK 7.0959 per dollar. This week we see the continuation of trading in the range of HRK 7.51-7.53 per euro.
- Excess liquidity rose from the level of HRK 67bn at the beginning of the week to HRK 73bn at the end of the week. Interest rates mostly stagnated w-o-w, and there was no interest at the CNB's repo auction.
- The Crobex Index closed last Friday at 2,100.59 points, up by 0.4% w-o-w, while Crobis was down by 0.4% (102.04 points) at the same time. As for sector indices, CROBEXconstruct decreased by 1.3% (to 454.35 points), while CROBEXindustry and CROBEXtourist increased by 5.1% and 0.1% respectively (1,223.83 and 3,581.41). Total ZSE turnover in the last week reached HRK 51.5 million, up by 6.3% w-o-w, owing to 6.3 times higher turnover in bonds (reaching HRK 24.3 million), while turnover in shares decreased by 39.1% (HRK 27.1 million).



Statistics

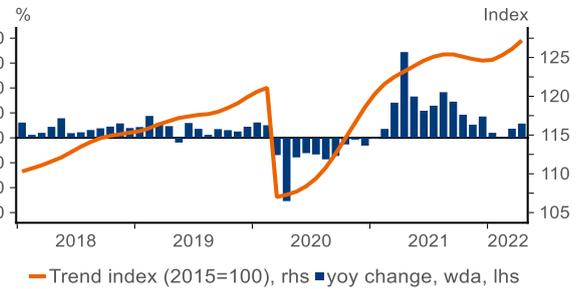
Industrial production

Source: Macrobond



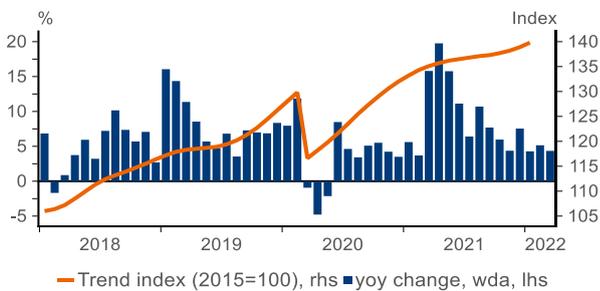
Retail trade, real

Source: Macrobond



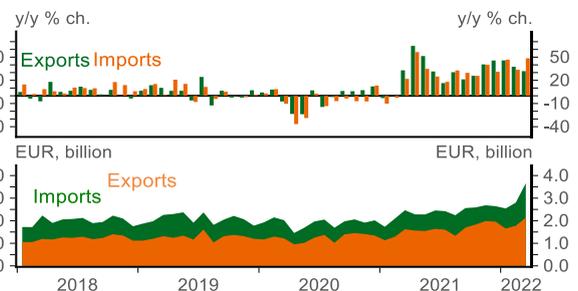
Construction works

Source: Macrobond



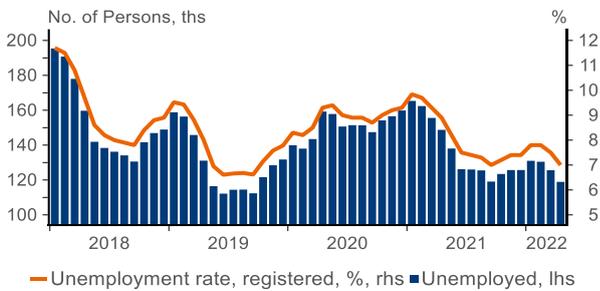
Goods exports and imports

Source: Macrobond



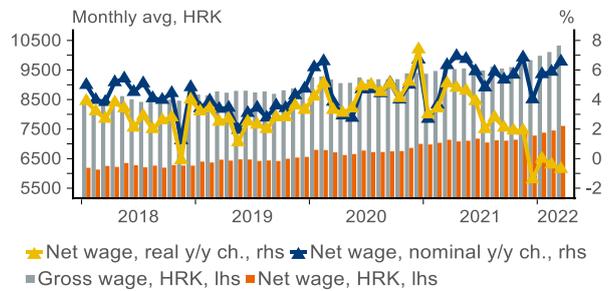
Unemployment

Source: Macrobond



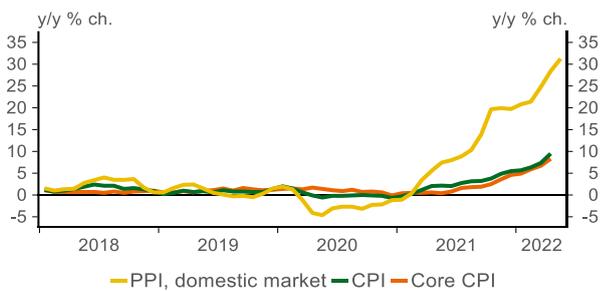
Wages

Source: Macrobond, CBS



Prices

Source: Macrobond



Economic Sentiment Indicator (ESI)

Source: Macrobond

