WEEKLY ANALYSIS

Number 770, March 14, 2022

PRIVREDNA BANKA ZAGREB
Bank of INTESA SANPAOLO

ECB accelerated the reduction of net purchases, highlighted the uncertainty

ECB March meeting was highly awaited ever since the previous meeting in February because it was believed ECB would change its rhetoric on raising interest rates due to increased inflationary pressures threatening to significantly exceed ECB December prognoses for inflation trends. In the meantime, Russian invasion of Ukraine started and the situation has dramatically escalated with the introduction of sanctions to Russia and a strong growth of uncertainty.

At last week's meeting the ECB confirmed its decision to end the PEPP programme by the end of March, emphasizing that the principal payments from maturing securities will be reinvested until at least the end of 2024, while deciding to accelerate the reduction of net purchases under the APP. Thus, instead of gradual reduction to the level of 20 billion euro till October, monthly net purchases will be cut from 40 billion euro in April to 30 billion euro in May and 20 billion euro in June, while the net purchase amounts in Q3 will be subsequently calibrated, in line with economic developments. The principal payments from maturing securities purchased under the APP will be fully reinvested during a longer period after ECB starts raising key interest rates. Interest rates were maintained at current levels at this meeting, with the ECB emphasizing that their possible adjustment will take place “some time after the end of net purchases under the APP” (and not “shortly after” as emphasized before) and that the adjustment will be gradual. Also highlighted was that the key interest rates’ trends depend on forward guidance, and therefore “ the key ECB interest rates will remain at their present levels until it sees inflation reaching 2% well ahead of the end of its projection horizon and durably for the rest of the projection horizon, and until the Governing Council judges that realised progress in underlying inflation is sufficiently advanced to be consistent with inflation stabilising at 2% over the medium term”. Markets continue to expect interest rate increase in the second part of the year, most probably in Q4.

New ECB macroeconomic projections point to lower GDP growth in the eurozone in the current and the following year and higher inflation and unemployment. Thus, expectations for 2022 are the growth of eurozone GDP by 3.7% y-o-y, and for 2023 by 2.8% (which is 0.5, i.e., 0.1 p.p. lower than December prognoses), while for 2024 the prognosis is maintained at 1.6%. Inflation projection for 2022 has been significantly elevated to 5.1% y-o-y, (+1.9 p.p. compared to December), while for 2023 and 2024 it has been slightly elevated to 2.1% and 1.9% (+0.3, i.e., +0.1 p.p.), because it is expected that energy price increase will be significantly mitigated towards the end of period covered by the projections. The ECB emphasizes that economic prospects are currently uncertain and mostly depend on the developments in Ukraine, the impact of current sanctions as well as possible further measures, so along with the baseline, adverse and severe scenarios were also presented, with milder and stronger impact, depending on the level of imposed sanctions and the reaction of energy prices.

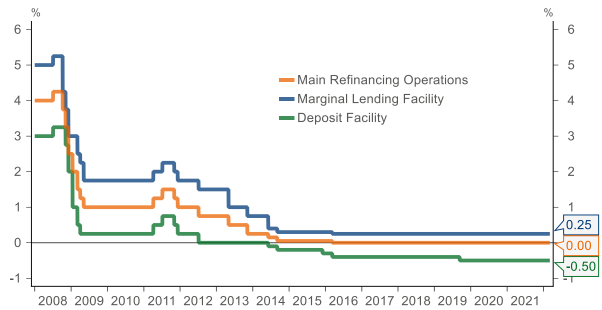
Growth and inflation projections for the euro area

(annual percentage changes)

	March 2022 projections				Adverse scenario				Severe scenario			
	2021	2022	2023	2024	2021	2022	2023	2024	2021	2022	2023	2024
Real GDP	5.4	3.7	2.8	1.6	5.4	2.5	2.7	2.1	5.4	2.3	2.3	1.9
HICP inflation	2.6	5.1	2.1	1.9	2.6	5.9	2.0	1.6	2.6	7.1	2.7	1.9

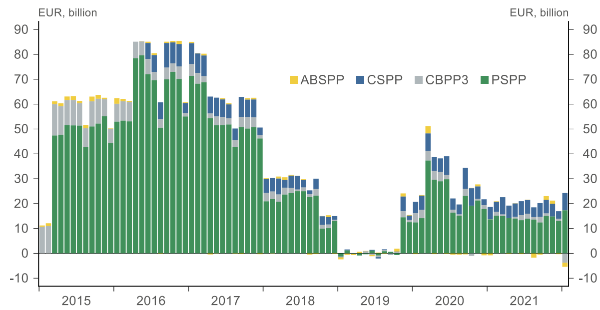
ECB policy rates

Source: Macrobond



APP Net Purchases by programme

Source: Macrobond

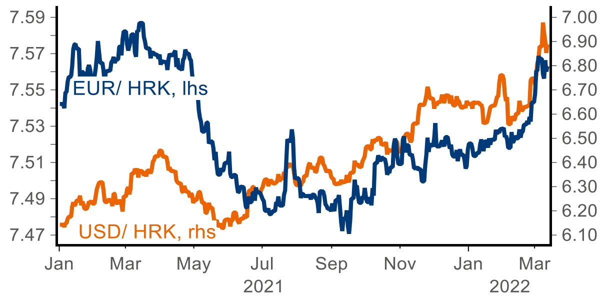


Weekly overview

- In January 2022 y-o-y growth of retail trade turnover in real terms slightly decreased to 2.0%. Observing the most important categories by gross, non-adjusted indices, sale of automotive fuels and lubricants slowed to 25.8%, and sales in non-specialised stores with food, beverages and tobacco predominating to 3.5%.
- Exchange rate retained its somewhat higher levels and trading was in the range of 7.56-7.58 kuna to the euro, with somewhat higher corporate demand for foreign currencies and calm interbank market. On Friday, mid-point exchange rate was down by 0.1% w-o-w and amounted to 7.5630 kuna to the euro. Kuna slightly weakened against the dollar, by 0.1% w-o-w, so the exchange rate increased to 6.8880 kuna to the dollar.
- Excess liquidity rose to 79 billion kuna, and interest rates stagnated w-o-w. At the CNB's repo auction a somewhat lower amount was placed compared to previous week, in the amount of 255 million kuna, with an interest rate of 0.05%.
- The Crobex Index closed last Friday at 1,975.12 points, up by 1.5% w-o-w, while Crobis simultaneously decreased by 0.2% (104.41). Sector indices ended in the black, whereas CROBEXconstruct was up by 3.9% (to 425.20 points), CROBEXtourist by 2.0% (3,424.43), and CROBEXindustry by 1.9% (1,094.88). Total ZSE turnover last week reached 304.0 million kuna, down by 51.3% w-o-w, owing to 57.7% lower turnover in bonds (reaching 211.3 million kuna) and 25.9% lower turnover in shares (92.7 million kuna).

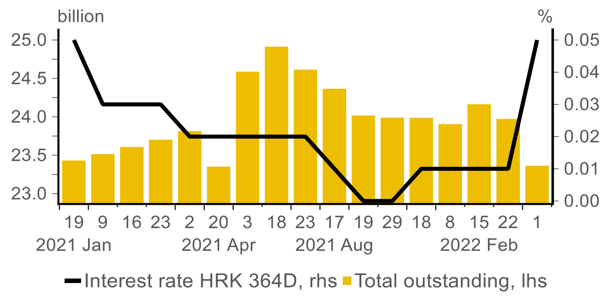
EUR/HRK and USD/HRK

Source: Macrobond



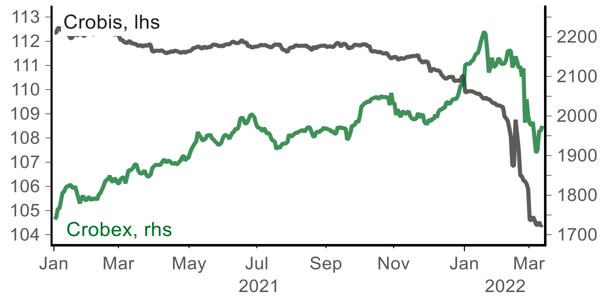
T-bills

Source: MoF



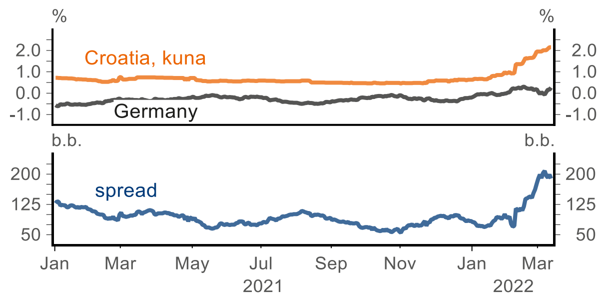
Crobex/Crobis

Source: Macrobond



10Y Government bond yield

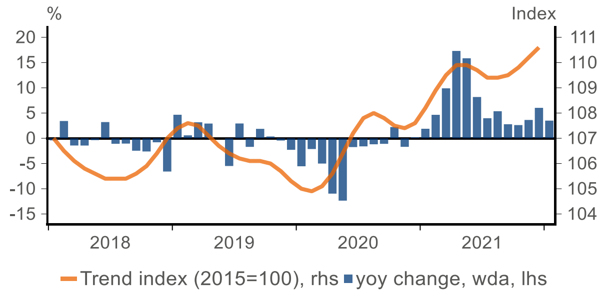
Source: Macrobond, Reuters



Statistics

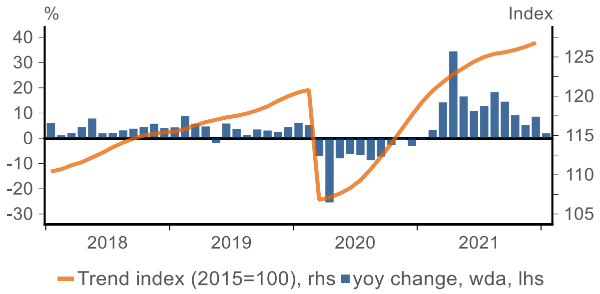
Industrial production

Source: Macrobond



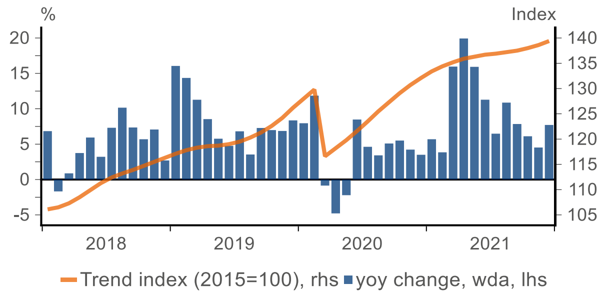
Retail trade, real

Source: Macrobond



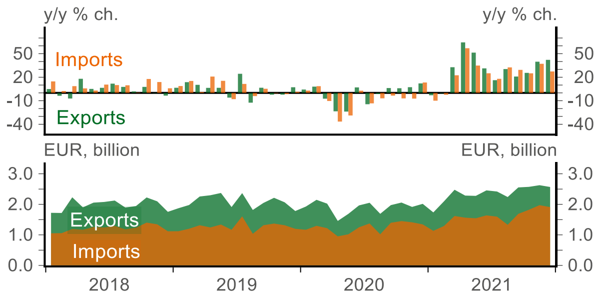
Construction works

Source: Macrobond



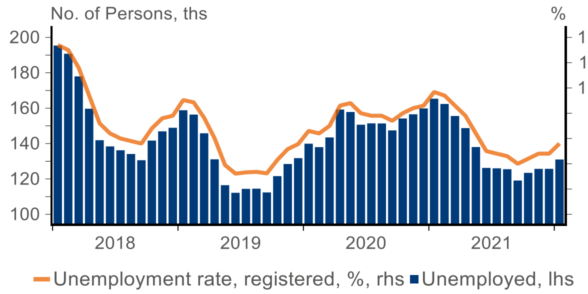
Goods exports and imports

Source: Macrobond



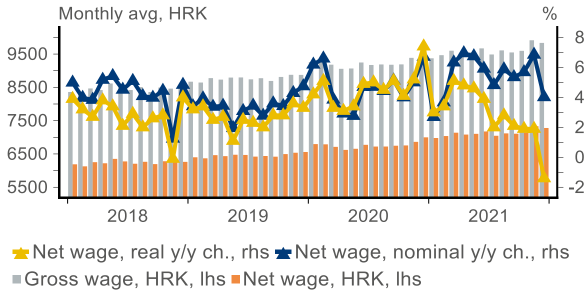
Unemployment

Source: Macrobond



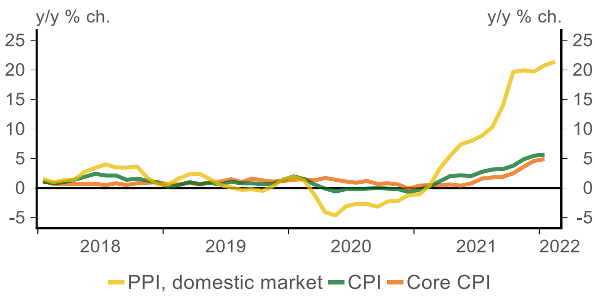
Wages

Source: Macrobond, CBS



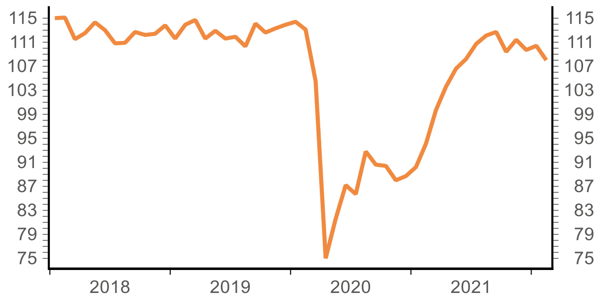
Prices

Source: Macrobond



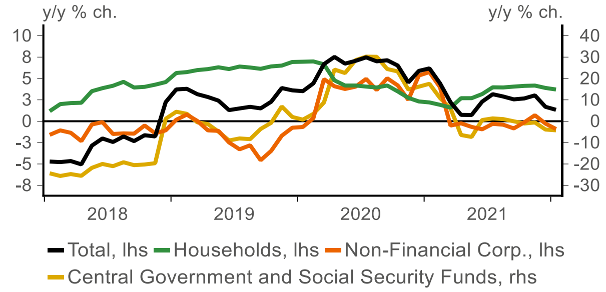
Economic Sentiment Indicator (ESI)

Source: Macrobond



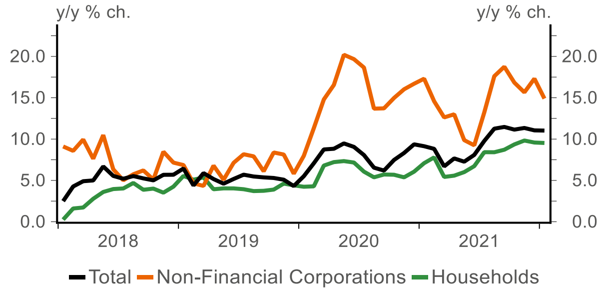
Loans

Source: Macrobond



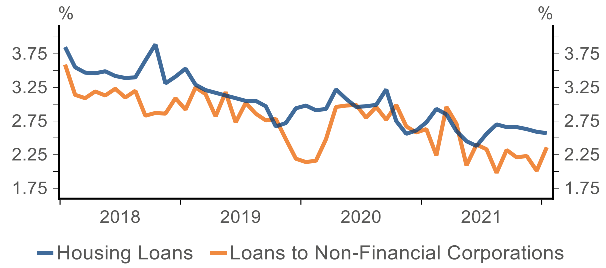
Deposits

Source: Macrobond



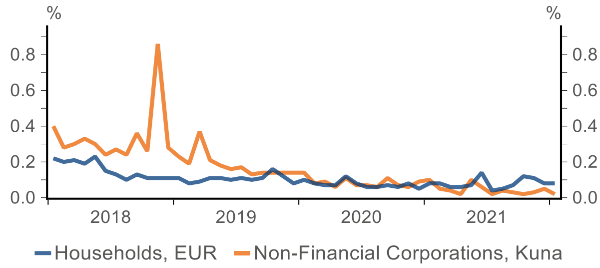
Interest rates on long-term loans indexed to € (new business)

Source: Macrobond



Interest rates on short-term time deposits (new business)

Source: Macrobond



RESEARCH OFFICE

Ivana Jović

Ana Lokin

Ivan Odrčić

TREASURY

Eugen Bulat

TRANSLATION

Ana Biloš

Jelena Marinović

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