



CROATIAN NATIONAL BANK

EUROSYSTEM

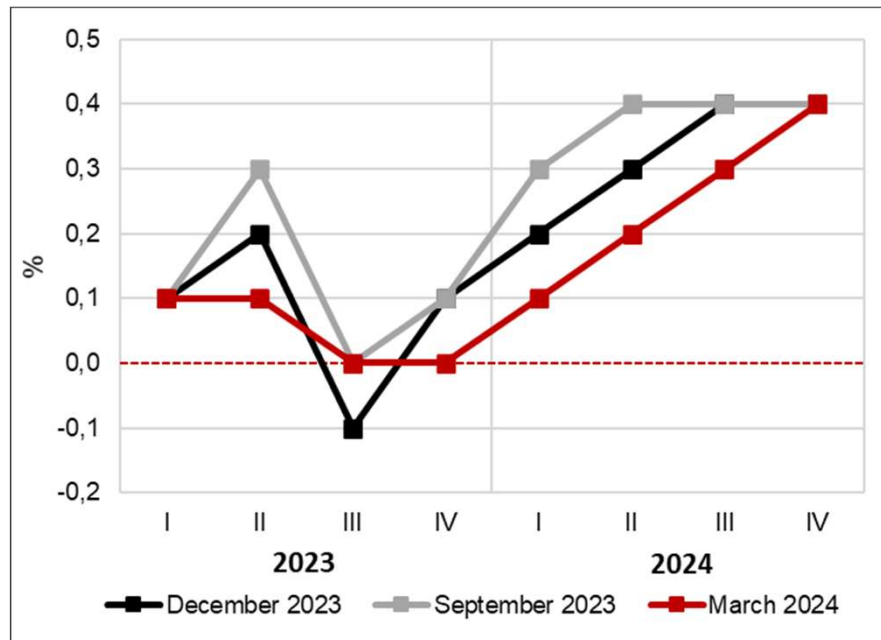
Disinflation and Markets in the Euro-area: Where Do We Stand?

Boris Vujčić, Governor
New York, April 2024



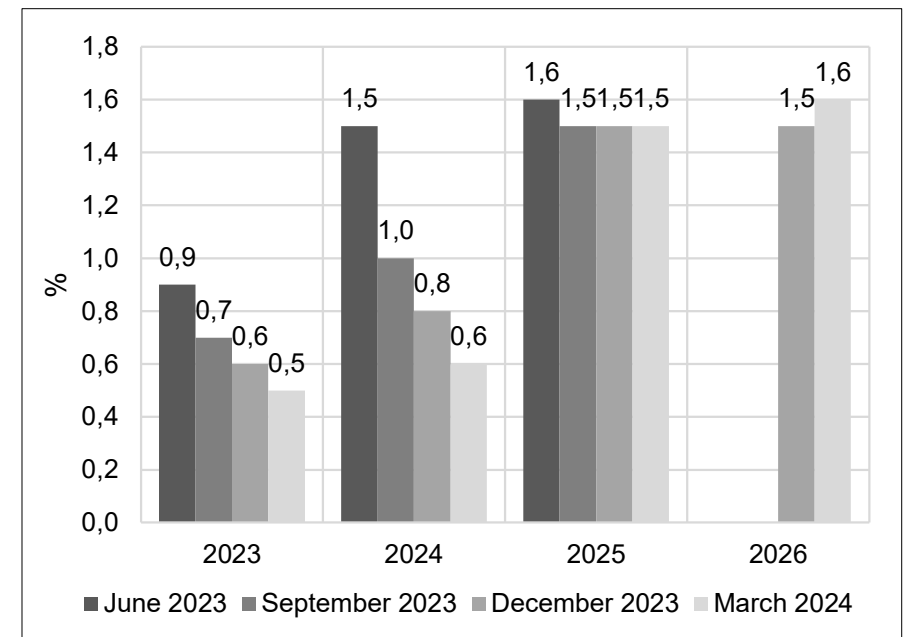
While recovery keeps being delayed, euro-area economy has so far proved more resilient than initially feared

Short term real GDP projections for EA
quarterly growth, %



Source: ECB.

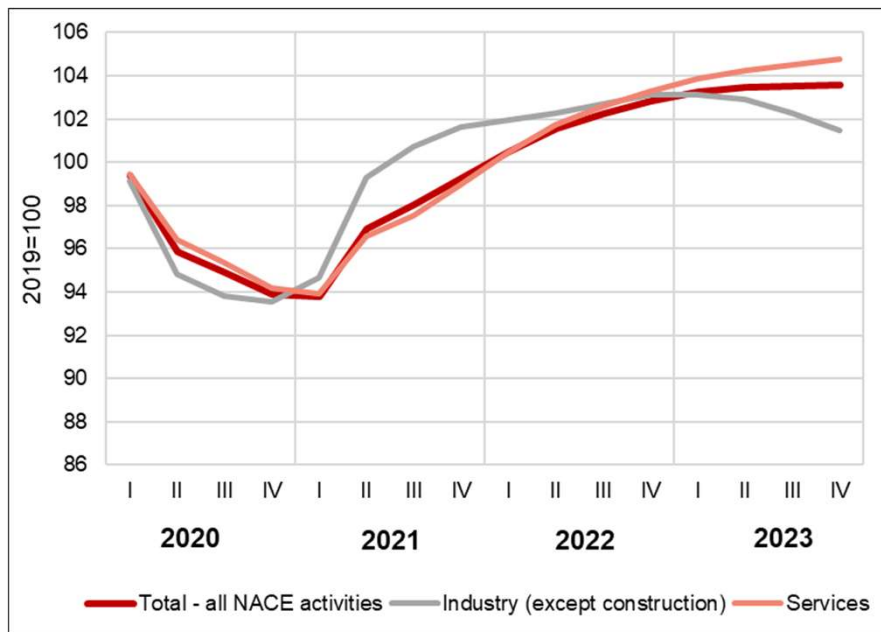
Long term real GDP forecast for EA
yoy growth, %



Source: ECB.

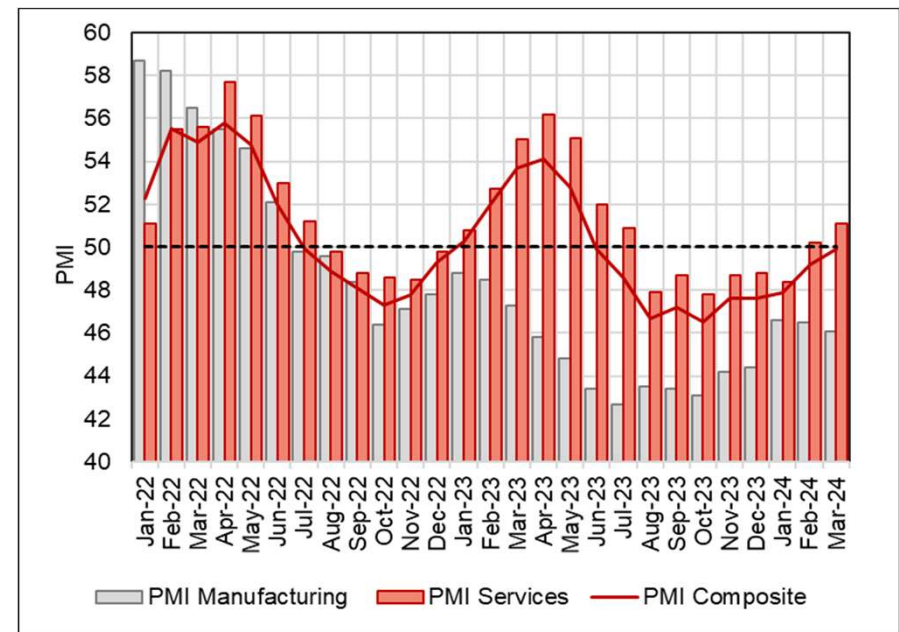
As outlook gradually improves, services activity stays ahead of manufacturing

Gross value added in EA
2019=100



Source: Eurostat.

EA Purchasing manager index

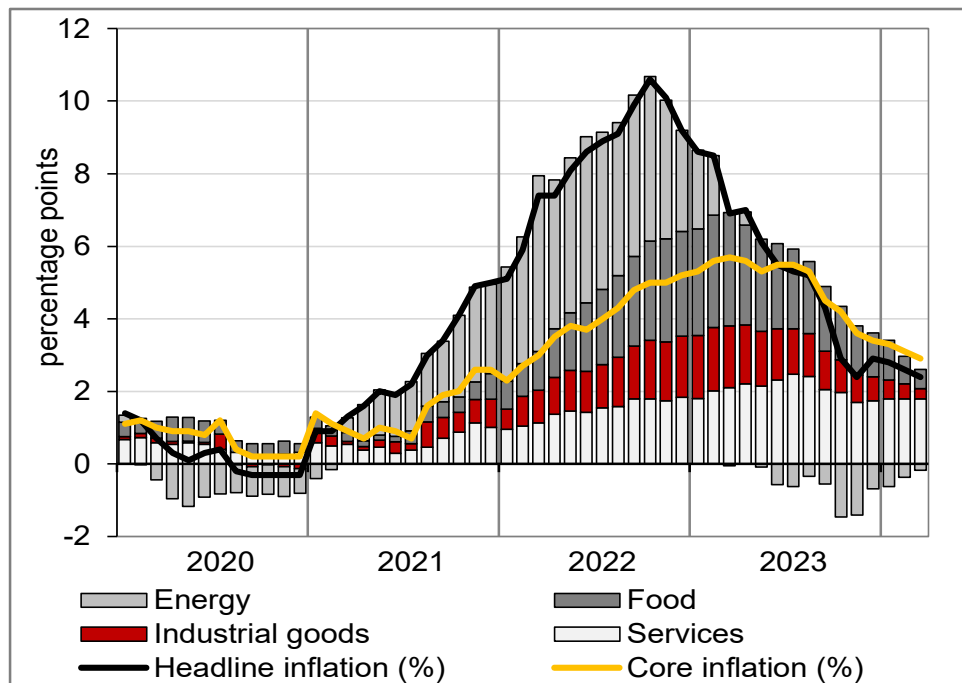


Note: PMI above 50 represents an expansion, while PMI under 50 represents a contraction relative to the previous month.

Source: S&P Global.

Headline inflation is coming down, but underlying pressures are still present

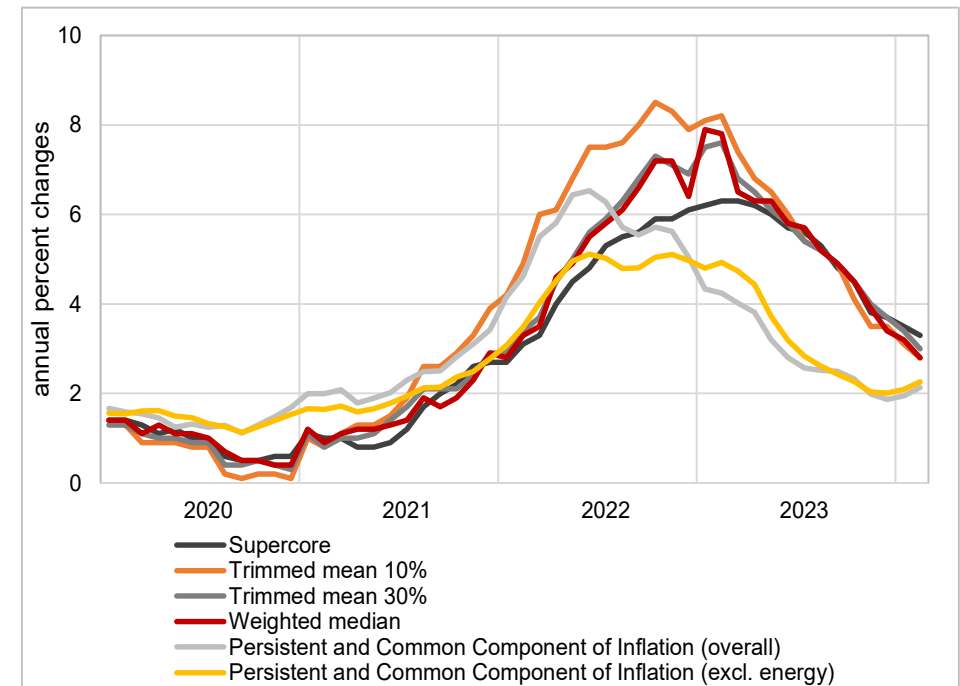
EA Inflation and contribution of main sub-components



Notes: Core inflation measured by the HICP excluding energy and food. Data up to March 2024.

Source: Eurostat.

EA Indicators of underlying inflation



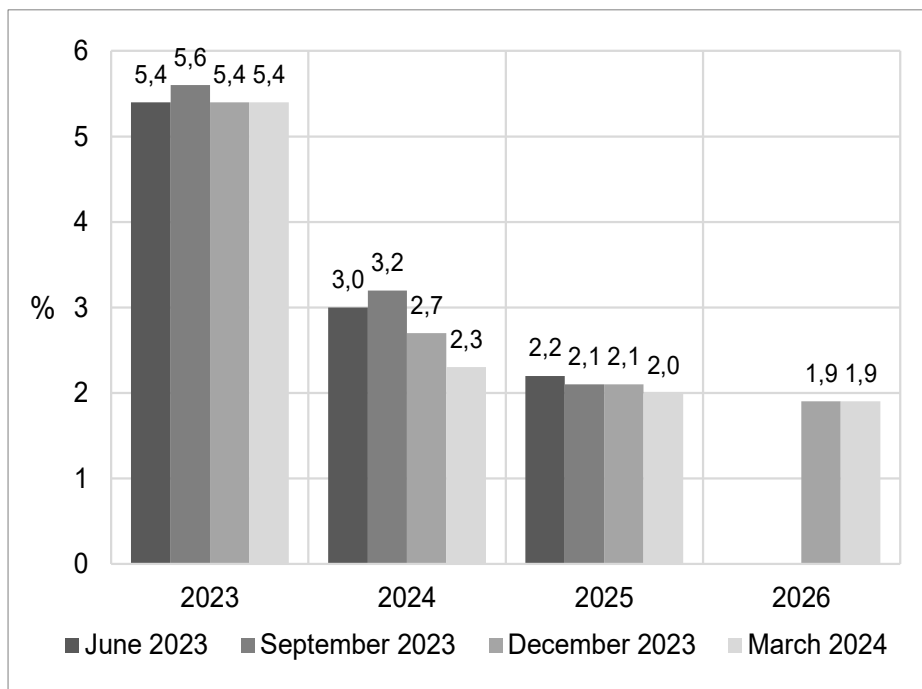
Source: ECB.

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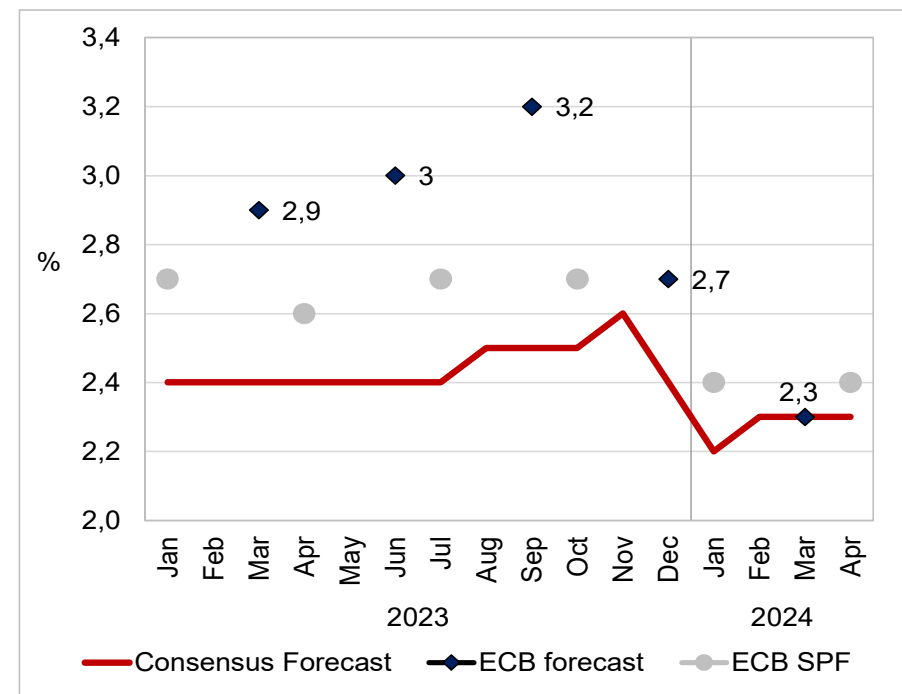
More benign short-term inflation outlook on the back of favourable recent developments

Inflation forecast for EA



Source: ECB.

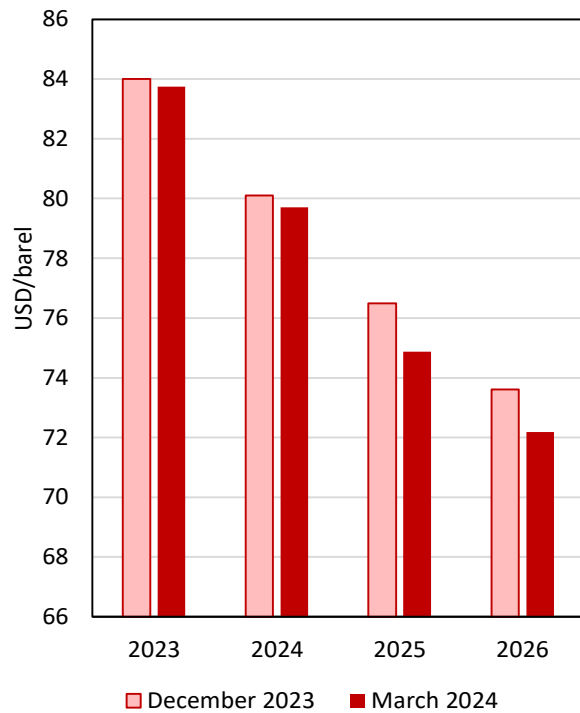
Inflation forecast for EA for 2024



Sources: CF; ECB.

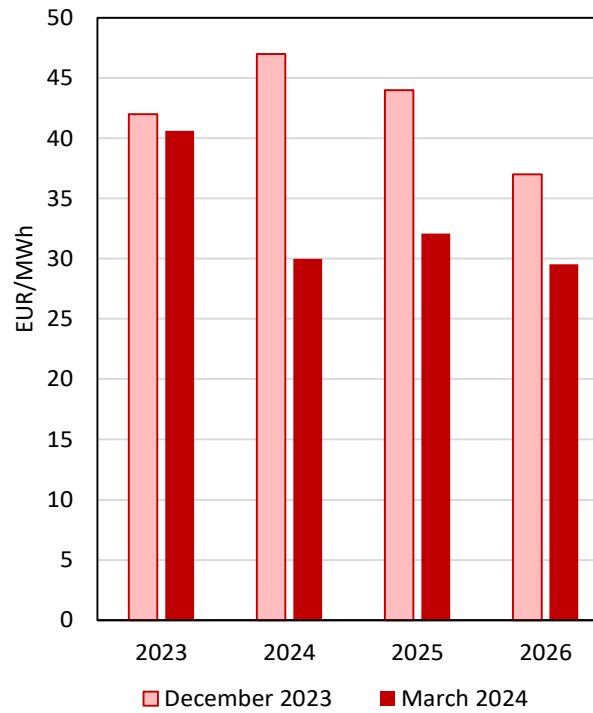
Commodity prices have supported the disinflation process

Oil prices



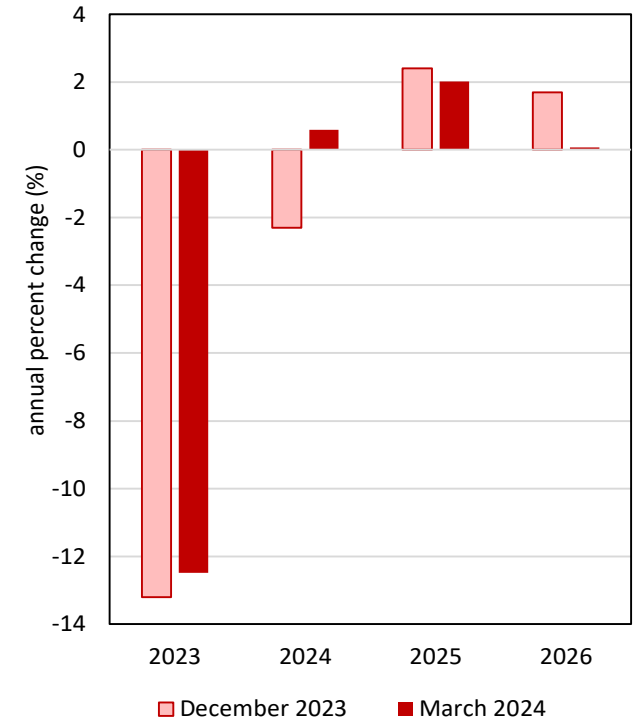
Source: ECB.

Natural gas prices



Source: ECB.

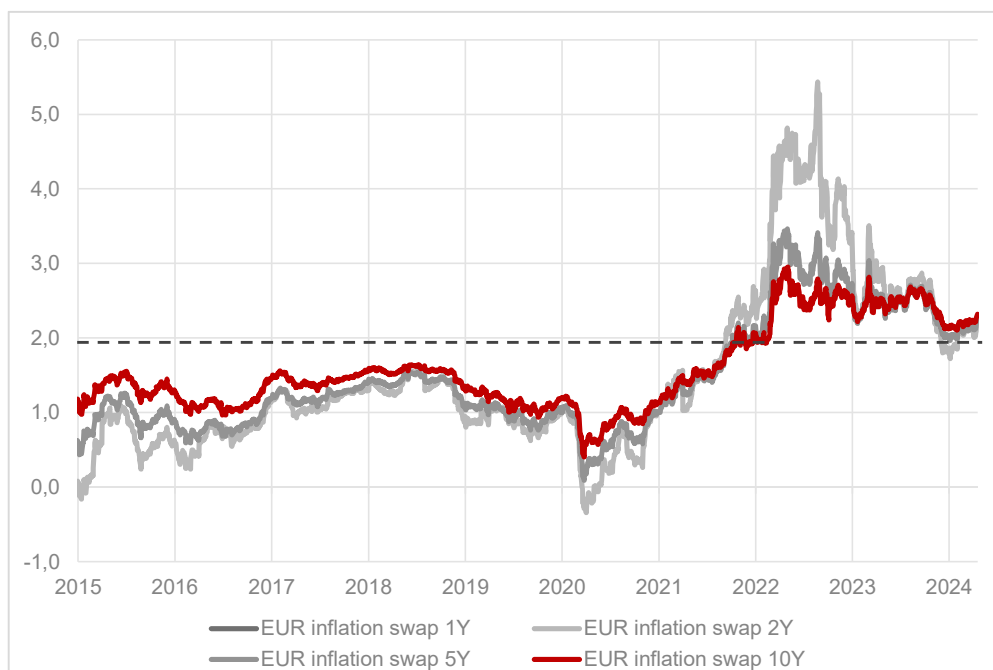
Non-energy commodity prices



Source: ECB.

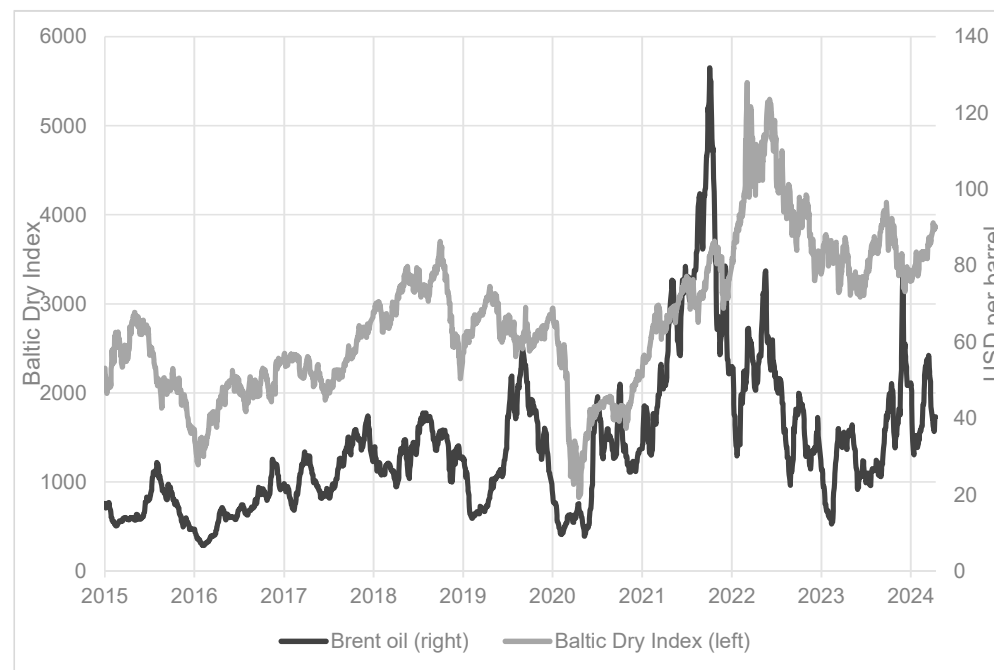
Inflation expectations have re-anchored despite rising geopolitical tensions

Inflation expectations converging towards 2%



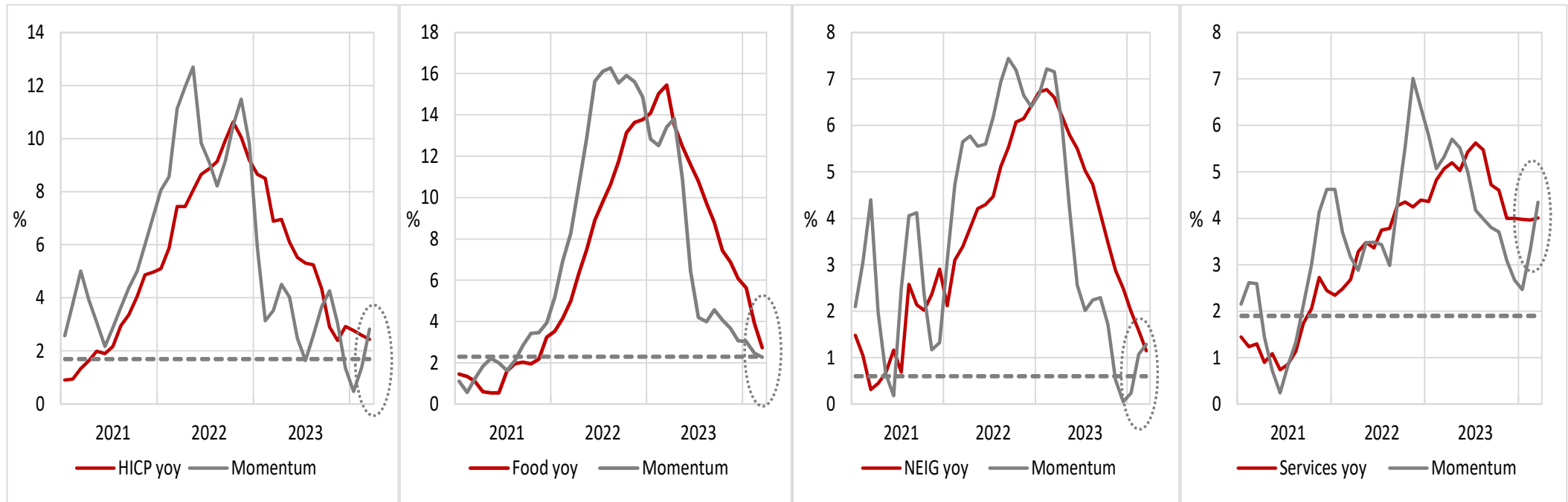
Source: Bloomberg.

Geopolitical risk rising again over the last year



Source: Bloomberg.

As inflation momentums gradually revert to long-term averages, services inflation remains elevated

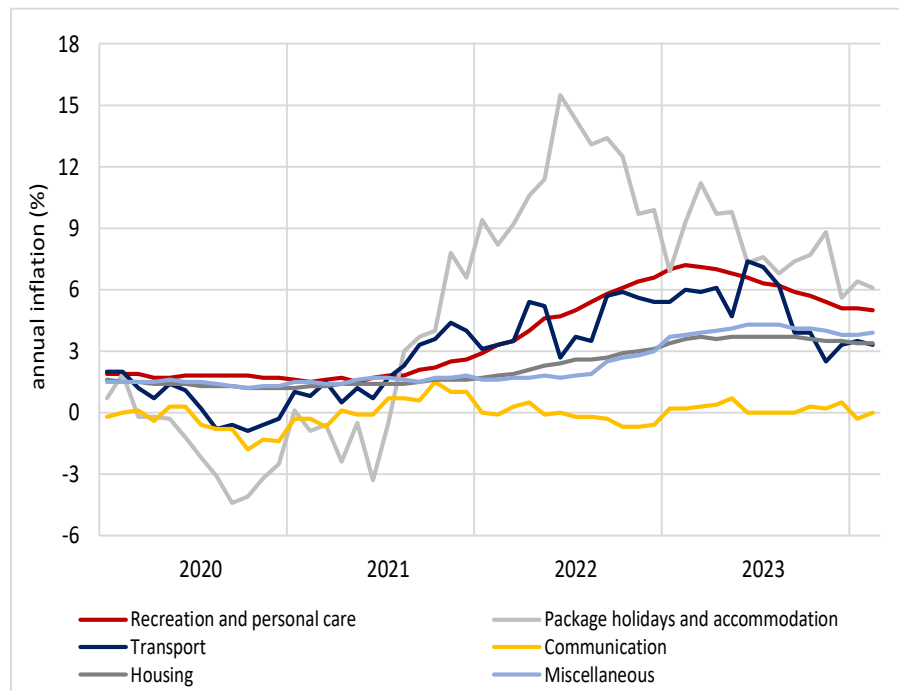


Notes: Momentum is defined as the quarterly rate of change on an annual level, calculated from the quarterly moving average of seasonally adjusted harmonised consumer price indices. The dotted line shows long-term average of momentum.

Sources: Eurostat; ECB; CNB calculations.

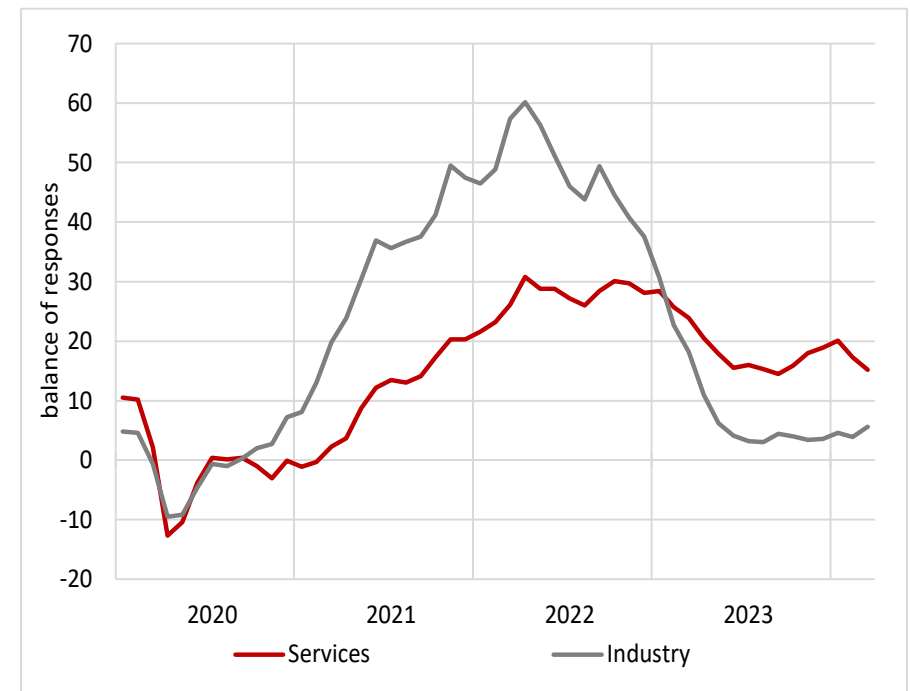
Price developments in the services sector, especially in the labour-intensive services, warrant careful monitoring

Services inflation, by components



Source: Eurostat.

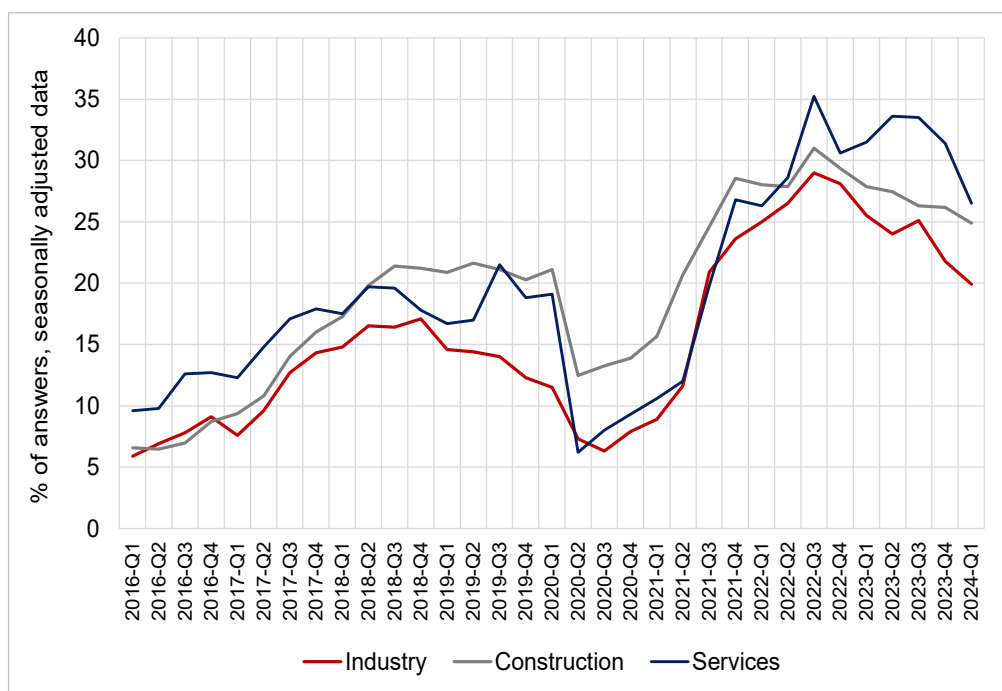
Businesses short-term inflation expectations



Note: Businesses inflation expectations refer to three months ahead.
Source: EC.

While unemployment remains low, there are signs of softening in the labour market ...

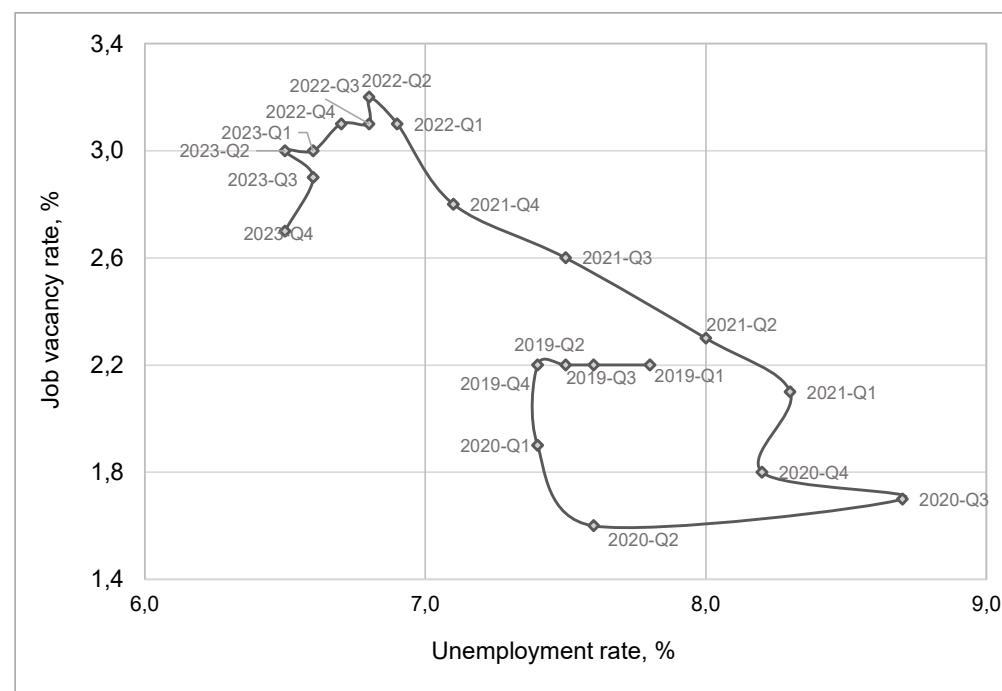
Labour as limiting factor in business activities



Note: The data refer to question: "What are currently the main limiting factors for your business?", from Business and consumer survey.

Source: EC.

Beveridge curve



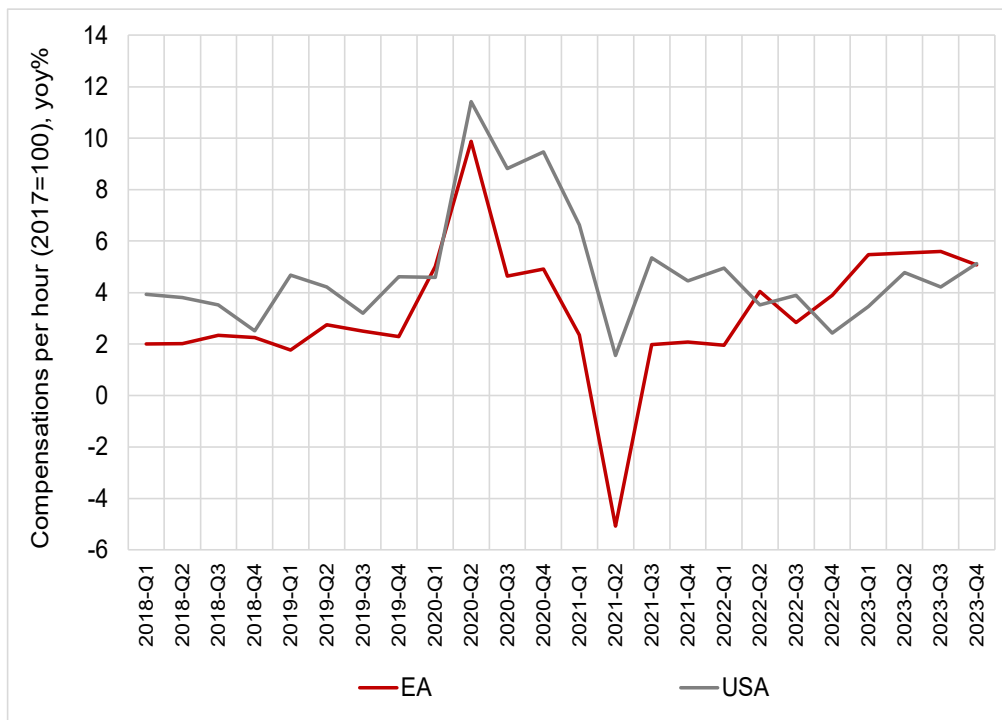
Source: Eurostat.

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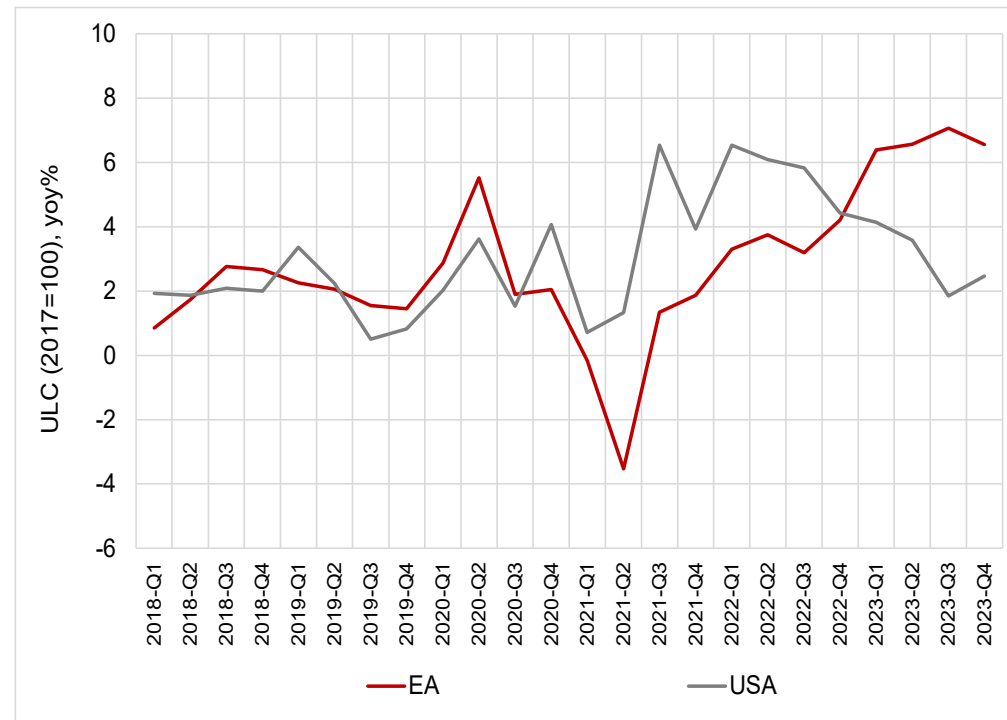
... but high wage growth and weak productivity are strengthening labour cost pressures

Compensation per hour in EA and USA



Note: Data for EA refer to B-N activities, and for USA to nonfarm business sector.
Sources: Eurostat; BLS.

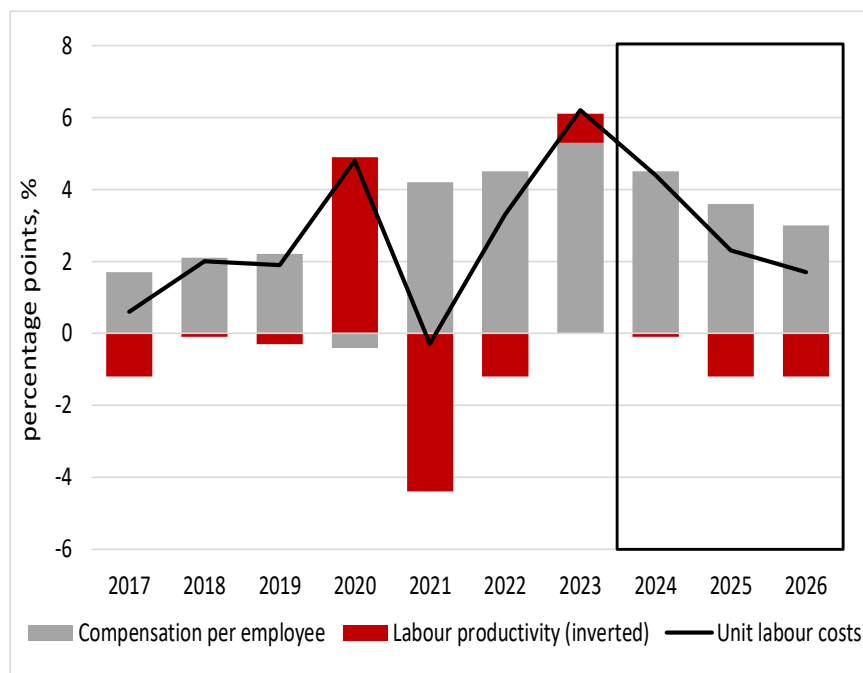
ULC in EA and USA



Note: Data for EA refer to B-N activities, and for USA to nonfarm business sector.
Sources: Eurostat; BLS.

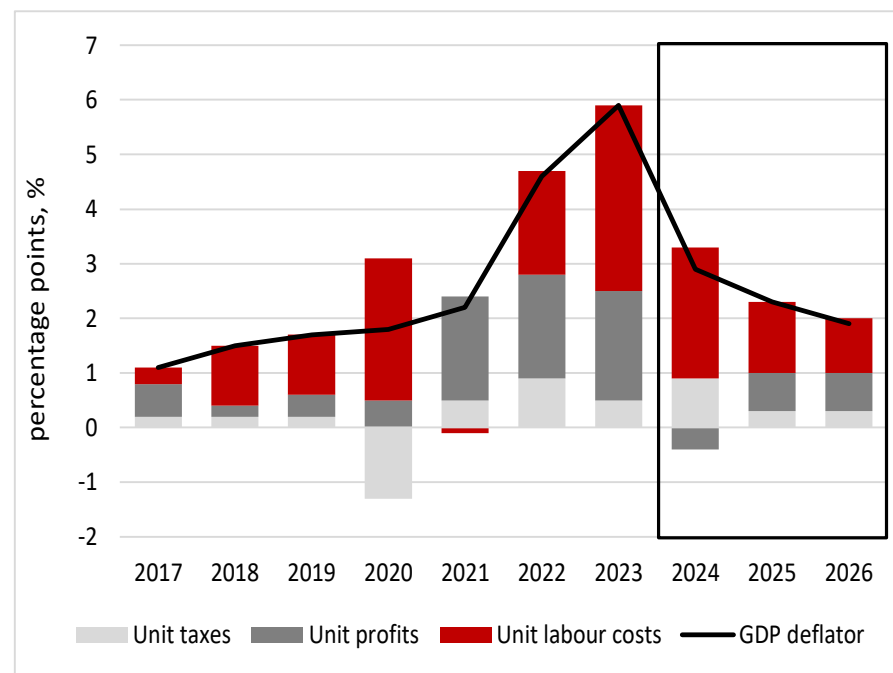
Productivity pick-up and restrained profit margins are expected to strengthen disinflation while wage pressures gradually moderate

Decomposition of unit labour costs



Source: ECB.

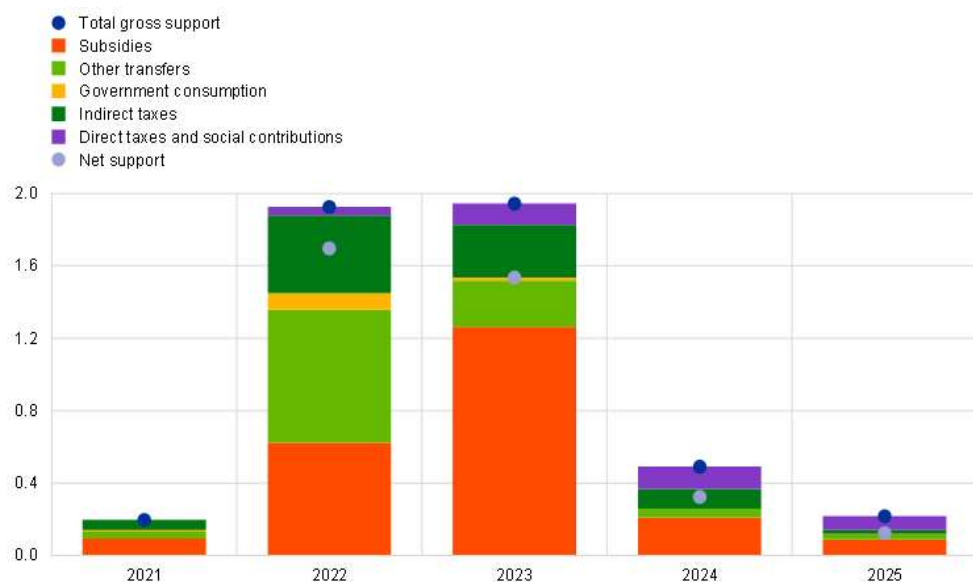
Decomposition of GDP deflator



Source: ECB.

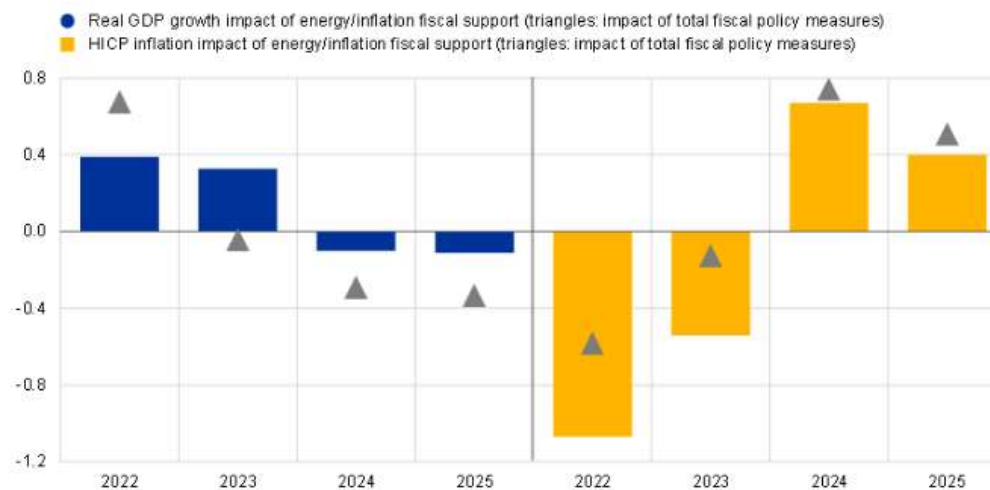
Expected unwinding of fiscal measures in 2024 could somewhat hinder disinflationary process

Euro area discretionary fiscal measures in response to high inflation (in % of GDP)



Source: ECB.

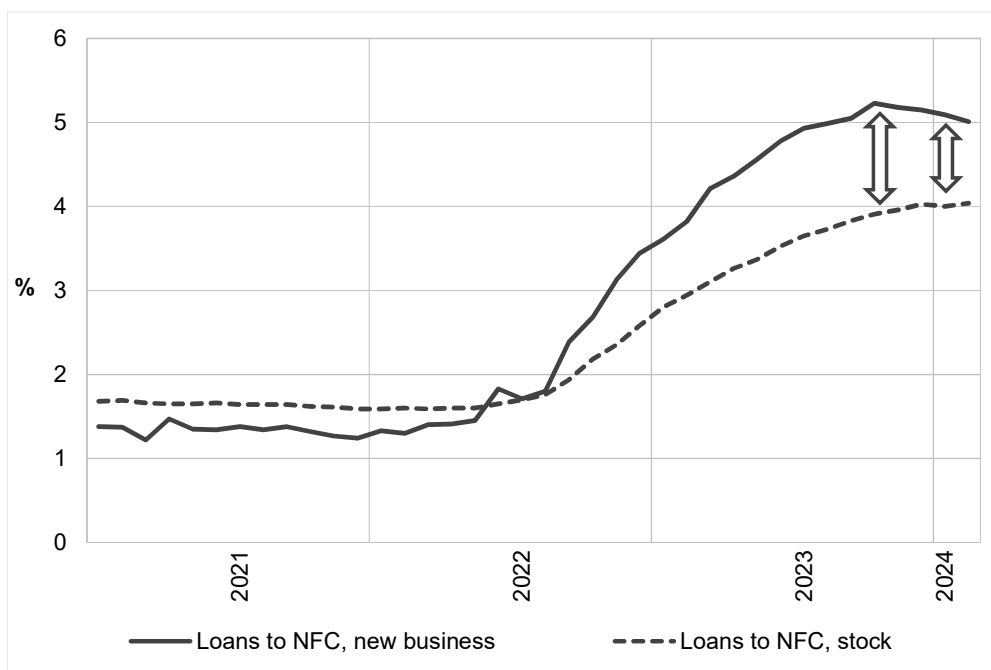
Macroeconomic effects of euro area discretionary fiscal policy measures (p.p.)



Source: ECB.

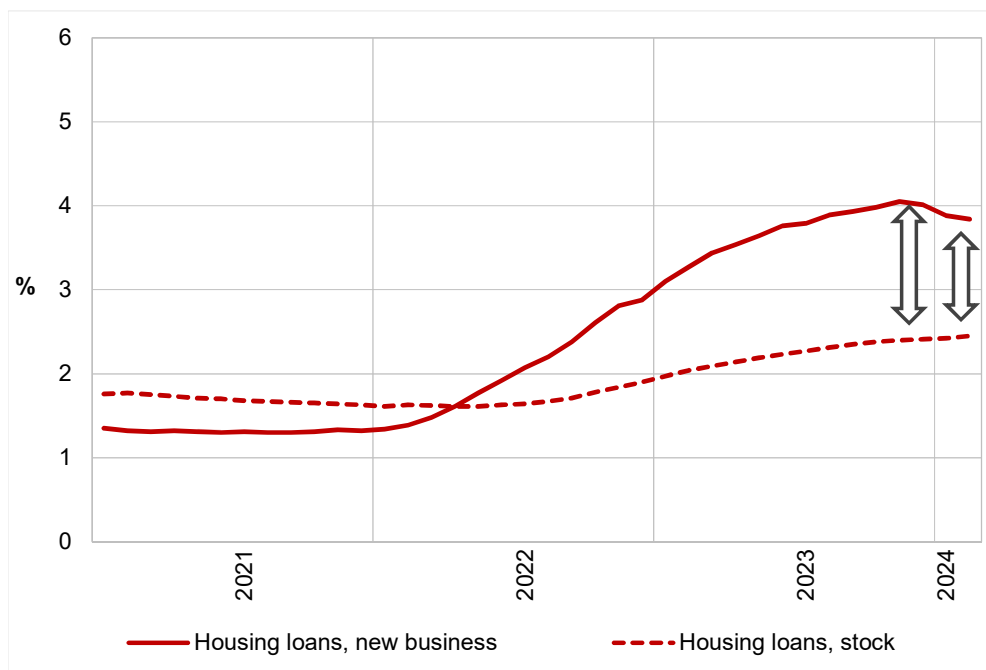
Monetary policy transmission is strong, near or even beyond peak effect on the real economy

Interest rates on loans to NFC`s in EA



Source: ECB.

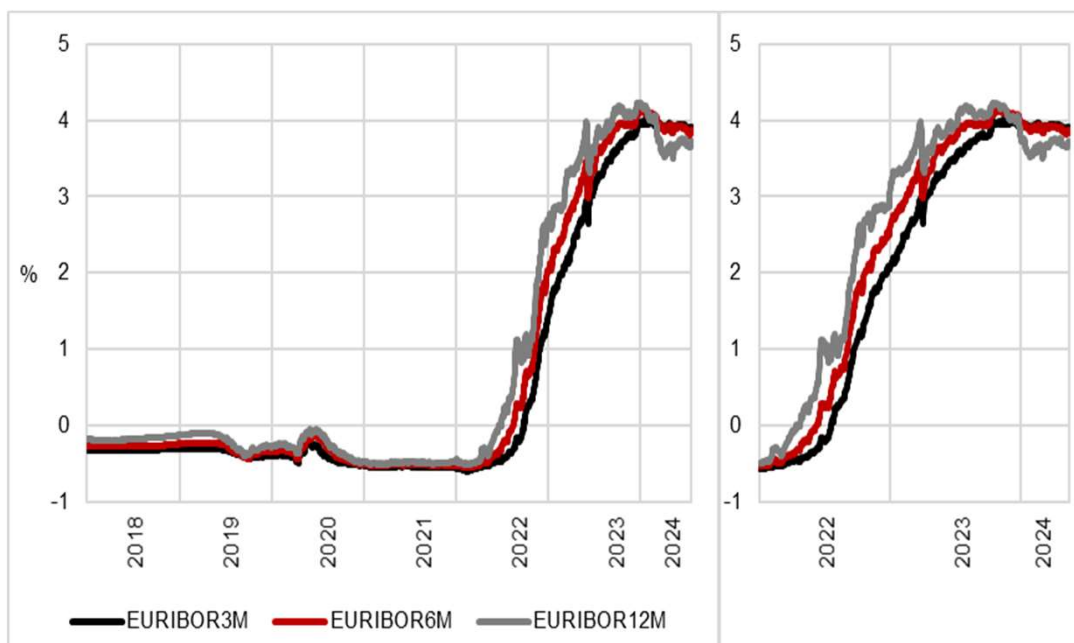
Interest rates on housing loans in EA



Source: ECB.

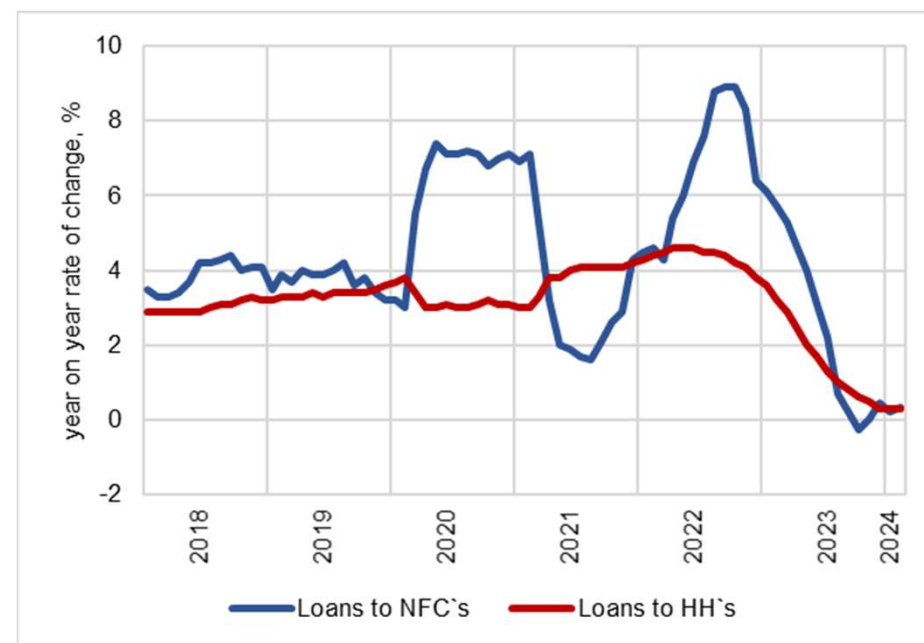
Euribor rates already transmitting expected cuts, while credit activity shows signs of stabilization

EURIBOR rates



Source: Bloomberg.

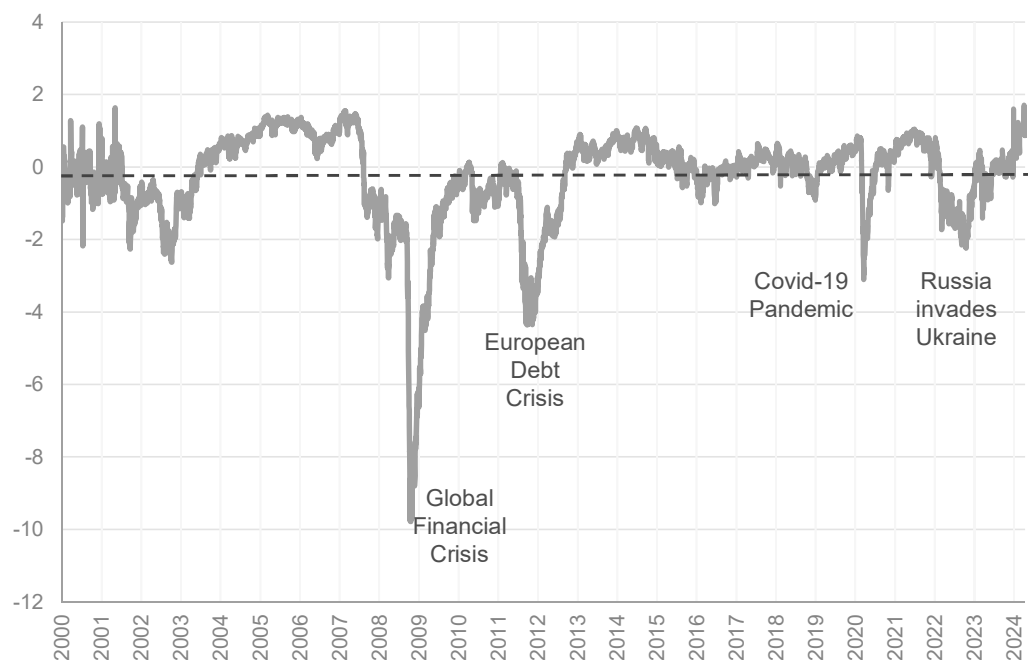
Loans to NFC's and HH's in euroarea, annual growth rates



Source: ECB.

EA financial conditions easing as equity prices surge, markets only now coming out from high volatility regime

EA Bloomberg market based financial conditions



Note: Positive value indicates accommodative financial conditions while negative value indicates tighter financial conditions. Index is a weighted average comprised from TED Spread, Euribor/OIS Spread, 10Y Bond Swap Spread, High Yield Europe Index, EuroStoxx Index, Dax Implied Volatility Index
Source: Bloomberg.

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Bund implied volatility 1 month 100% moneyness

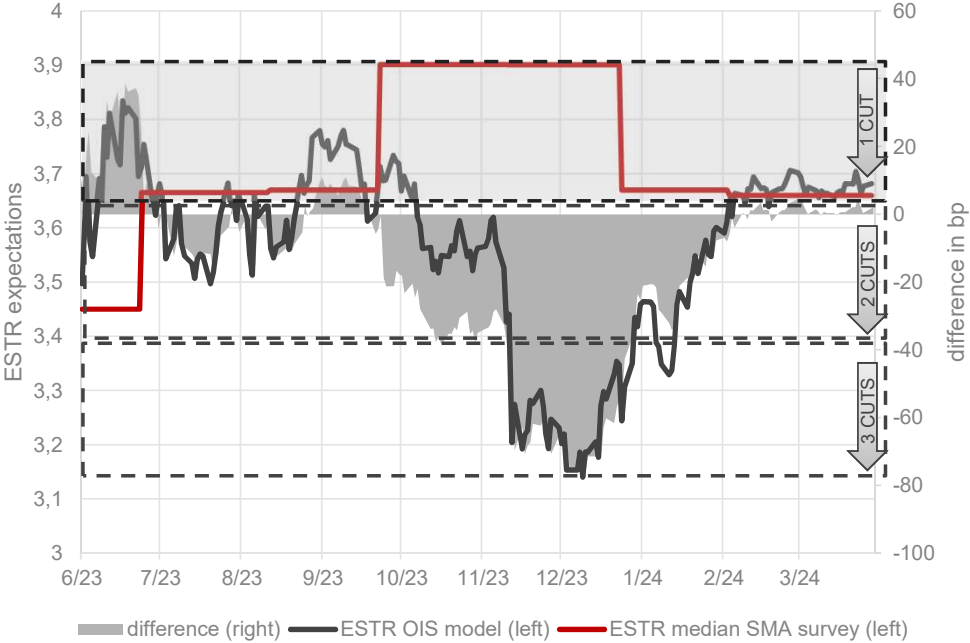


Note: The chart captures options' implied volatility on 1 month Bund futures. An implied volatility is the volatility implied by the market price of an option based on the Black-Scholes model and is different from realized volatility. 100% moneyness indicates that an option is At The Money.

Source: Bloomberg.

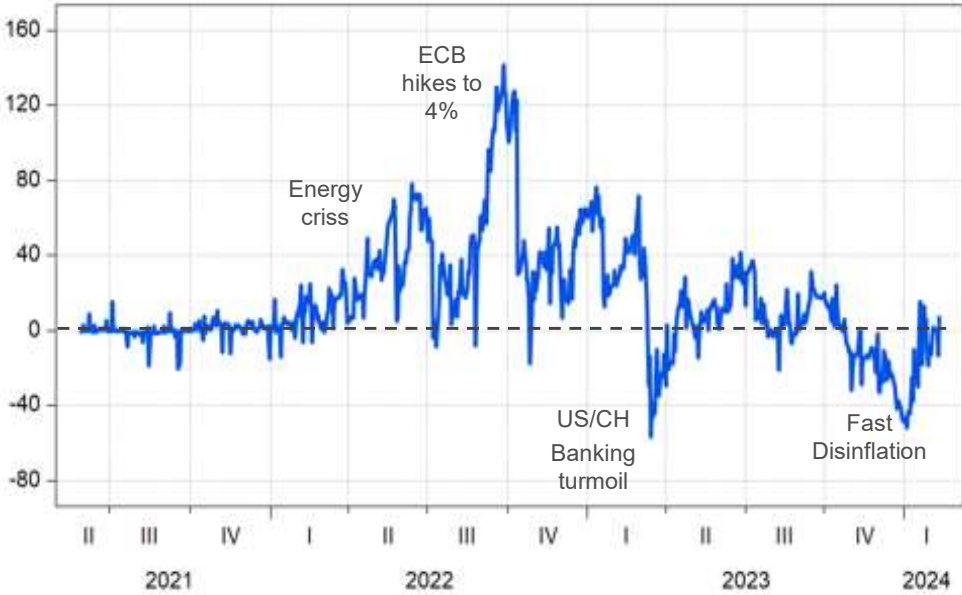
ECB's timing of a cut is data dependent, market pricing and economist's projections are converging

ESTR expectations for June 2024 SMA survey vs. Market pricing



Sources: Bloomberg, SMA survey.

ESTR expectations 6m ahead SMA survey vs. Market pricing



Note: SMA survey projections for ESTR 6m ahead are subtracted from market pricing
Sources: Bloomberg, SMA survey, CNB calculations.

ECB data dependent, not Fed dependent

Rate cuts expected by December 2024 Market pricing



Inflation market expectations diverging 5y5y Inflation Swap



Note: Rate expectations for ECB are based on OIS model and for Fed on Fed Fund Futures model
Source: Bloomberg.

Source: Bloomberg.



HNB

Summary

- While recovery keeps being delayed, euro-area economy has so far proved more resilient than initially feared.
- Headline inflation is coming down as expected, but underlying pressures are still present.
- Services inflation, especially labour-intensive services inflation, warrants careful monitoring as wage growth remains strong.
- Productivity pick-up and restrained profit margins are expected to strengthen disinflation, while wage pressures gradually moderate.
- Unwinding of fiscal measures in 2024 could somewhat hinder disinflationary process.
- Inflation expectations well anchored, financial conditions are already easing due to market expectations of interest rate cuts.
- Start, as well as pace, of easing will continue to be data dependent.



Thank you very much for your attention!