# EUROZONE
# 2023-2024 SCENARIO

## STAGNATION BETWEEN TWO POWERFUL FORCES

October 2023

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WORKING EVERY DAY IN YOUR INTEREST AND FOR SOCIETY

GROUP ECONOMIC RESEARCH

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# SUMMARY

## STAGNATION BETWEEN TWO POWERFUL FORCES

The soft-landing narrative continues to be fuelled by a resilient labour market, despite the slowdown in economic activity, and by the healthy economic and financial situation of private agents. The eurozone is no exception to the favourable trend in supply. But the eurozone economy is slowing more than others, raising more pressing questions as to the end of the abnormal cycle of expansion. **While activity is now 2.6% higher than before the health crisis, the annual pace of quarterly GDP growth has dipped sharply, from 4.2% in Q2 2022 to 0.5% in Q3 2023.**

***Between the peak in monetary transmission and the slowdown in inflation***

The slowdown is almost equally attributable to the terms-of-trade shock resulting from the rise in commodity prices in 2022 and the earlier and more significant than expected impact of the rise in interest rates. The nature of the landing will depend on the interplay between two opposing and powerful forces: the implementation of the most extensive and rapid monetary restriction that the zone has experienced and the strengthening of the disinflationary momentum expected from Q4 2023. In our scenario, monetary policy transmission peaks in 2023 and **growth comes out at zero in H2 2023, putting the lid on any increase in the annual average growth rate relative to its modest 0.5% at the end of June. The return to a positive growth rate (0.9% annual average in 2024) will be based on gains in purchasing power stemming from disinflation (with inflation declining from 5.6% in 2023 to 3.1% in 2024)** and the lag in adapting wages to past inflation.

***More harmonious shock responses***

The economic situation in **the eurozone is difficult to read owing to the growing divergence of trends in the constituent economies.** The German economy weakened further in the summer, particularly in manufacturing, impacted by the slowdown in major export markets (China and the United States) and, more structurally, by the loss of competitiveness stemming from higher energy costs.

In our scenario, the Germany economy will contract in the third and fourth quarters of 2023. In contrast, peripheral countries have thus far proved more resilient, underpinned by strong performances in tourism and NextGenerationEU investments. With the exception of Italy, hindered by a weak manufacturing sector, the growth rates of these economies are expected to outperform the eurozone average.

***Public finances: moderate pro-cyclicality***

After the extremely expansionary policies of recent years, pressures for a substantial adjustment in public finances are mounting. **In our scenario the impetus will be slightly negative in 2023, less damaging than suggested by the stability programmes announced in the spring, owing to the implementation of counter-cyclical measures and compensation for higher oil prices. Most of the adjustment is therefore postponed to 2024.**

# SUMMARY

## STAGNATION BETWEEN TWO POWERFUL FORCES

| Forecasts | Quarterly rate (QoQ, %) | | | | | | | | | | | | Annual rate (YoY, %) | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| EMU | 2022 | | | | 2023 | | | | 2024 | | | | 2021 | 2022 | 2023 | 2024 |
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | | | | |
| **GDP** | **0,7** | **0,8** | **0,3** | **0,0** | **0,0** | **0,2** | **0,0** | **0,0** | **0,3** | **0,4** | **0,4** | **0,4** | **5,9** | **3,4** | **0,5** | **0,9** |
| **Households consumption** | 0,0 | 0,9 | 1,0 | -0,7 | 0,1 | 0,0 | 0,3 | 0,2 | 0,3 | 0,4 | 0,4 | 0,4 | 4,4 | 4,2 | 0,5 | 1,2 |
| **Public consumption** | 0,5 | -0,2 | -0,1 | 0,5 | -0,6 | 0,4 | 0,2 | 0,3 | 0,2 | 0,2 | 0,2 | 0,2 | 4,2 | 1,6 | 0,1 | 0,9 |
| **Total GFCF** | -0,5 | 0,5 | 1,2 | -0,3 | 0,4 | 0,1 | 0,1 | 0,1 | 0,3 | 0,4 | 0,4 | 0,5 | 3,7 | 2,8 | 1,1 | 1,0 |
| **G&S exports** | 1,6 | 2,0 | 1,0 | -0,2 | 0,0 | -0,9 | -0,6 | -0,2 | 0,3 | 0,7 | 0,7 | 0,7 | 11,3 | 7,3 | -0,2 | 0,8 |
| **G&S imports** | 0,1 | 1,9 | 2,1 | -1,1 | -1,1 | -0,2 | -0,2 | 0,1 | 0,2 | 0,6 | 0,7 | 0,7 | 9,1 | 7,9 | -0,6 | 1,1 |
| **Inventory changes (% of GDP)** | 0,7 | 0,9 | 1,0 | 0,9 | 0,4 | 0,8 | 0,8 | 0,8 | 0,7 | 0,7 | 0,7 | 0,8 | 0,6 | 0,9 | 0,7 | 0,7 |
| ***Contributions to GDP growth*** | | | | | | | | | | | | | | | | |
| **Domestic demand excluding inve** | 0,0 | 0,5 | 0,7 | -0,3 | 0,0 | 0,1 | 0,2 | 0,2 | 0,2 | 0,3 | 0,4 | 0,4 | 4,0 | 3,1 | 0,5 | 1,0 |
| **Inventories** | -0,1 | 0,1 | 0,1 | -0,1 | -0,5 | 0,5 | 0,0 | 0,0 | -0,1 | 0,0 | 0,0 | 0,0 | 0,5 | 0,3 | -0,2 | 0,0 |
| **Net exports** | 0,8 | 0,1 | -0,5 | 0,4 | 0,5 | -0,4 | -0,2 | -0,1 | 0,1 | 0,1 | 0,1 | 0,1 | 1,4 | 0,0 | 0,2 | -0,1 |
| **Unemployment** | 6,8 | 6,7 | 6,7 | 6,7 | 6,6 | 6,5 | 6,7 | 6,8 | 6,8 | 6,9 | 6,8 | 6,9 | 7,7 | 6,7 | 6,6 | 6,9 |
| **Consumer prices** | 6,1 | 8,0 | 9,3 | 10,0 | 8,0 | 6,2 | 5,0 | 3,3 | 3,3 | 3,3 | 3,1 | 2,9 | 2,6 | 8,4 | 5,6 | 3,1 |
| **Unemployment** | 6,8 | 6,7 | 6,7 | 6,7 | 6,6 | 6,5 | 6,7 | 6,8 | 6,8 | 6,9 | 6,8 | 6,9 | 7,7 | 6,7 | 6,6 | 6,9 |

# SUMMARY

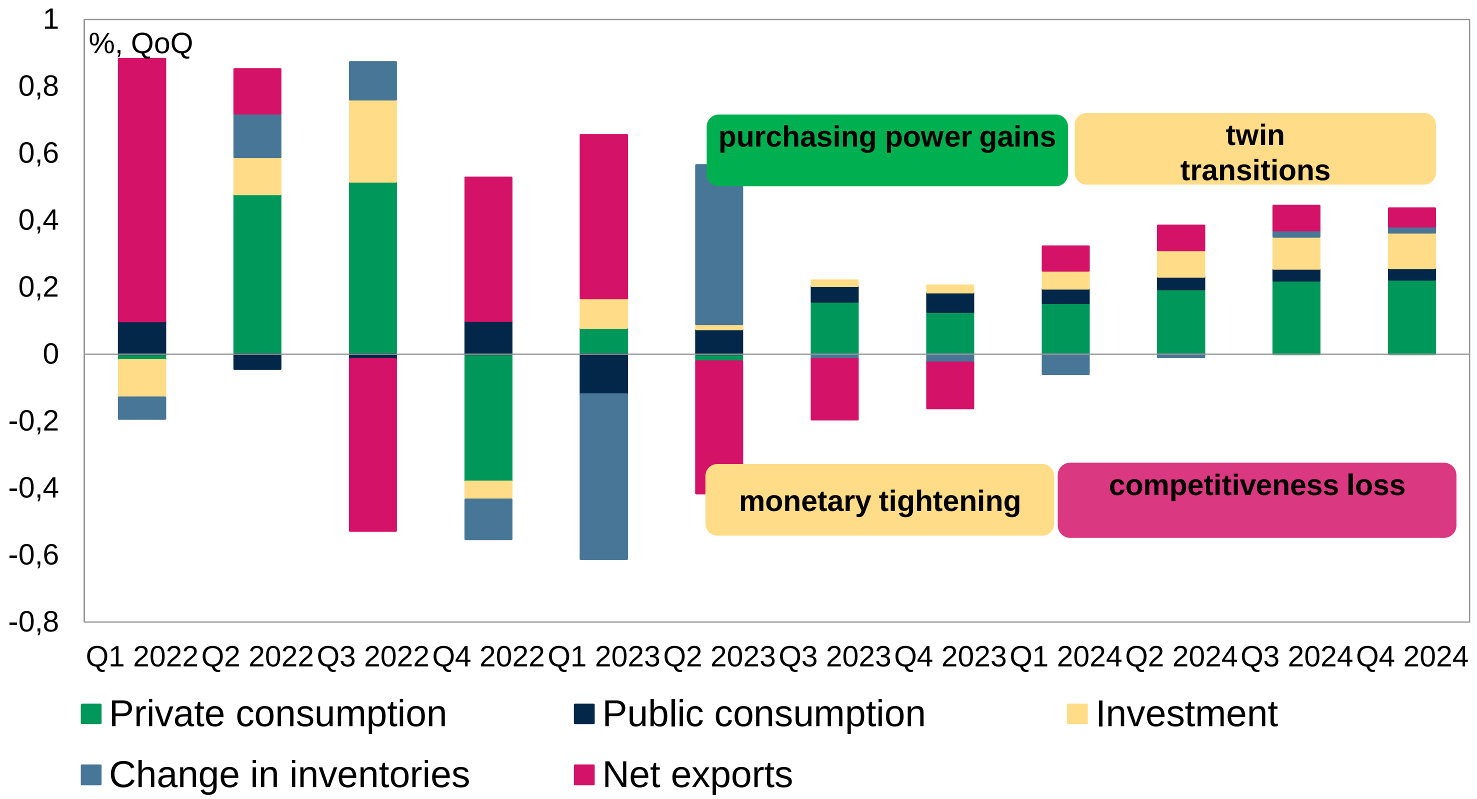
## STAGNATION BETWEEN TWO POWERFUL FORCES

| Forecasts | Quarterly rate (QoQ, %) | | | | | | | | | | | | Annual rate (YoY, %) | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Eurozone | 2022 | | | | 2023 | | | | 2024 | | | | 2021 | 2022 | 2023 | 2024 |
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | | | | |
| **Eurozone** | **0,7** | **0,8** | **0,3** | **0,0** | **0,0** | **0,2** | **0,0** | **0,0** | **0,3** | **0,4** | **0,4** | **0,4** | **5,9** | **3,4** | **0,5** | **0,9** |
| **Germany** | 1,0 | -0,1 | 0,4 | -0,4 | -0,1 | 0,0 | -0,2 | -0,2 | 0,2 | 0,3 | 0,5 | 0,5 | 3,1 | 1,9 | -0,4 | 0,5 |
| **France** | -0,1 | 0,4 | 0,3 | 0,1 | 0,0 | 0,5 | 0,1 | 0,2 | 0,2 | 0,3 | 0,4 | 0,4 | 6,4 | 2,5 | 0,9 | 1,0 |
| **Italy** | 0,1 | 1,4 | 0,3 | -0,2 | 0,6 | -0,4 | 0,1 | 0,1 | 0,0 | 0,4 | 0,5 | 0,5 | 8,3 | 3,9 | 0,7 | 0,6 |
| **Spain** | 0,3 | 2,5 | 0,5 | 0,5 | 0,6 | 0,4 | 0,3 | 0,3 | 0,5 | 0,6 | 0,4 | 0,3 | 6,4 | 5,8 | 2,4 | 1,7 |
| **Netherlands** | 0,5 | 1,8 | -0,2 | 0,9 | -0,4 | -0,2 | 0,0 | 0,1 | 0,2 | 0,3 | 0,3 | 0,4 | 6,2 | 4,4 | 0,4 | 0,7 |
| **Belgium** | 0,1 | 0,7 | 0,3 | 0,2 | 0,4 | 0,3 | 0,1 | 0,1 | 0,2 | 0,3 | 0,4 | 0,4 | 6,9 | 3,0 | 1,2 | 1,0 |
| **Ireland** | 6,8 | 2,2 | 2,4 | -0,9 | -2,6 | 0,5 | -0,2 | -0,5 | 1,7 | 1,1 | 1,1 | 1,1 | 14,8 | 9,5 | -1,5 | 3,1 |
| **Portugal** | 2,3 | 0,1 | 0,5 | 0,5 | 1,5 | 0,0 | -0,2 | 0,2 | 0,4 | 0,7 | 0,7 | 0,4 | 5,7 | 6,8 | 2,1 | 1,5 |
| **Greece** | 2,7 | 0,5 | 0,3 | 1,2 | 0,0 | 1,3 | 0,2 | 0,3 | 0,5 | 0,6 | 0,4 | 0,4 | 8,1 | 5,9 | 2,3 | 1,9 |
| **Finland** | -0,1 | 0,7 | -0,4 | -0,6 | 0,3 | 0,6 | 0,1 | 0,2 | 0,3 | 0,2 | 0,3 | 0,3 | 3,2 | 1,6 | 0,4 | 1,0 |
| **Luxembourg** | 0,0 | -0,2 | 0,0 | -2,1 | 0,6 | -0,1 | 0,4 | 0,4 | 0,6 | 0,6 | 0,6 | 0,6 | 7,2 | 1,4 | -0,9 | 1,9 |
| **Austria** | 0,7 | 2,0 | -0,4 | 0,0 | 0,1 | -0,8 | 0,0 | 0,1 | 0,2 | 0,4 | 0,4 | 0,5 | 4,4 | 4,8 | -0,2 | 0,7 |
| **Slovenia** | 0,0 | 0,5 | -0,5 | 0,7 | 0,2 | 1,1 | 0,1 | 0,4 | 0,6 | 0,7 | 0,7 | 0,7 | 8,4 | 2,9 | 1,6 | 2,3 |
| **Malta** | 0,8 | 2,2 | 0,6 | 1,6 | 0,6 | 1,1 | 0,3 | 0,6 | 0,5 | 0,5 | 0,6 | 0,4 | 12,2 | 6,9 | 3,7 | 2,1 |

# STAGNATION BETWEEN TWO POWERFUL FORCES

## BETWEEN THE PEAK IN MONETARY TRANSMISSION AND THE SLOWDOWN IN INFLATION

Growth contributions and supporting/detracting factors




*Sources: Eurostat, Crédit Agricole S.A./ECO.*

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# RECENT DEVELOPMENTS AND SHORT-TERM SCENARIOS

## INDUSTRY SLUGGISH ON CYCLICAL AND STRUCTURAL FACTORS

The eurozone has not been spared by the weakness of the global manufacturing cycle. Economic activity slowed sharply in all sectors in Q2 2023 but industry was already showing a year-on-year decline (-0.7%). **However, performances across the manufacturing sector are highly contrasted due to disruptions in value chains, post-pandemic adjustments in the composition of demand, and changes in relative prices. Business activity in energy-intensive sectors has declined continuously in the last 12 months**, while automotive-related sectors have benefited from the return to normal in semiconductor supply and still high order backlogs. Conversely, durable goods producers, as well as the upstream and downstream construction sectors, are suffering the full brunt of past increases in inflation and interest rates. Construction growth remains positive year-on-year but is slowing. While services generally maintained positive growth over one year (1.6%), retail, hotels and transport shifted from double-digit growth rates to quasi-stagnation.

Adjustments to the composition of demand are still afoot, making it harder to pinpoint a clear trend in industrial activity. But in one clearly foreseeable development, backlogs will gradually dry up and orders will decline relative to stocks of finished products. And with manufacturers having built up extensive stocks in the spring, industrial production will in all likelihood decrease. The slowdown is expected to intensify in the third quarter.

***No demand impetus in Q2 2023***

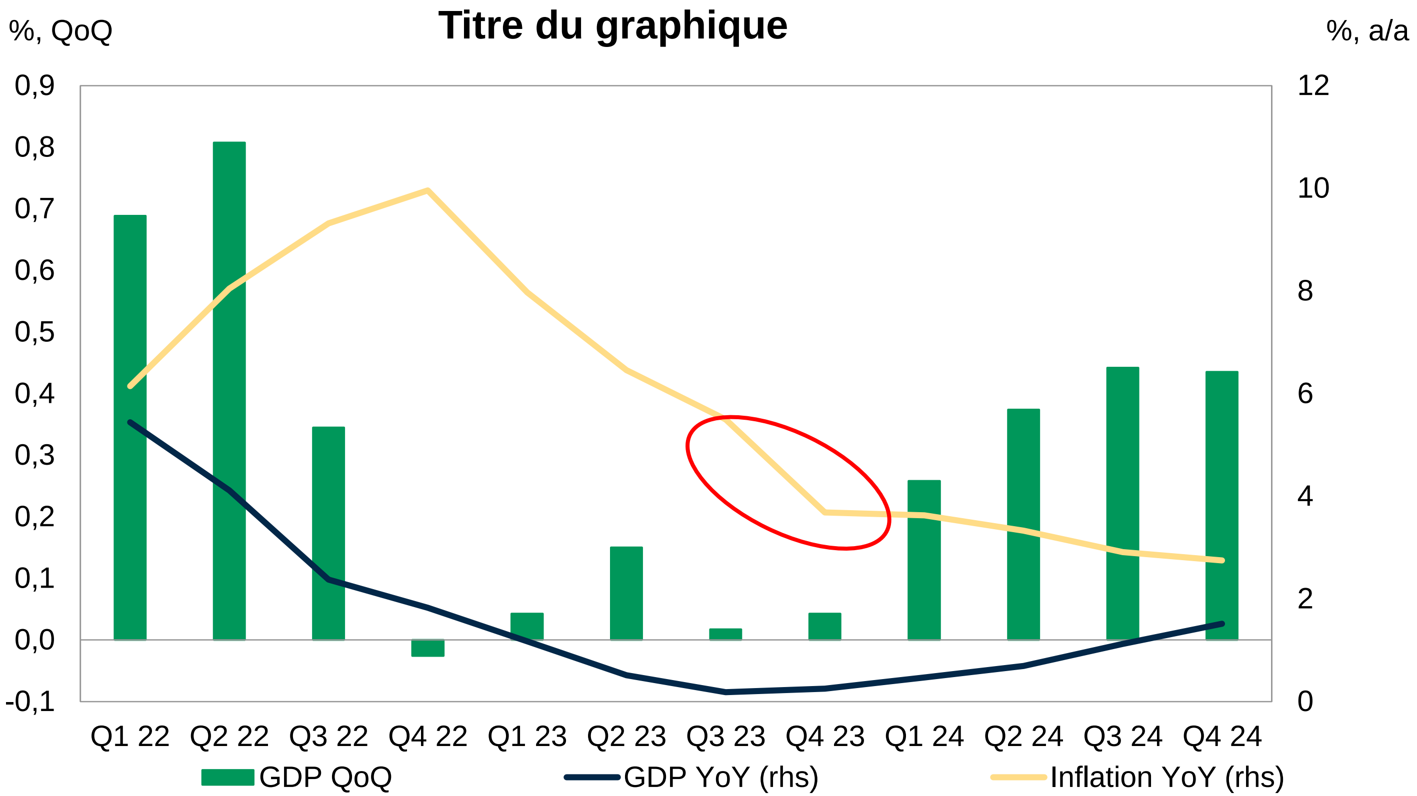
**GDP growth in Q2 2023 was only a little less sluggish than in the first, coming out at 0.2% in the former after 0% in the latter. Growth was saved solely by the strong, and likely involuntary, building of inventories (+0.5 contribution points), offsetting the negative contribution of foreign trade (-0.4 points), with domestic demand having generated zero impetus for three quarters** (+0.1 points in the second quarter). Growth in household consumption was interrupted by a sharp decline at the end of 2022 and has failed to pick up since, though it has not dipped since the beginning of 2023. After decreasing in late 2022, investment was lacklustre at best in the first two quarters of 2023 (+0.3% over the quarter). Housing investment has already fallen by 2.6% year on year, while investment in non-residential construction continues to grow but at a slower pace. Investment in machinery and equipment is adversely affected by weak demand for durable goods and investment goods. On the brighter side, investment in transport goods, after the disastrous year of 2021, continues to show a positive pace of growth, albeit slower than before.

The slowdown in global demand is clearly evident in exports of goods and services, which have been declining since the end of 2022. While the sharper contraction in imports, after the peak linked to the emergency gas supplies in the summer of 2022, enabled a positive contribution from trade until the first quarter of 2023, the normalisation of the import penetration rate is now revealing the weakness of foreign sales and its negative impact on growth.

# RECENT DEVELOPMENTS AND SHORT-TERM SCENARIOS

## DISINFLATION AND MONETARY TRANSMISSION SET THE TEMPO

### GDP: sharp slowdown, then modest rebound

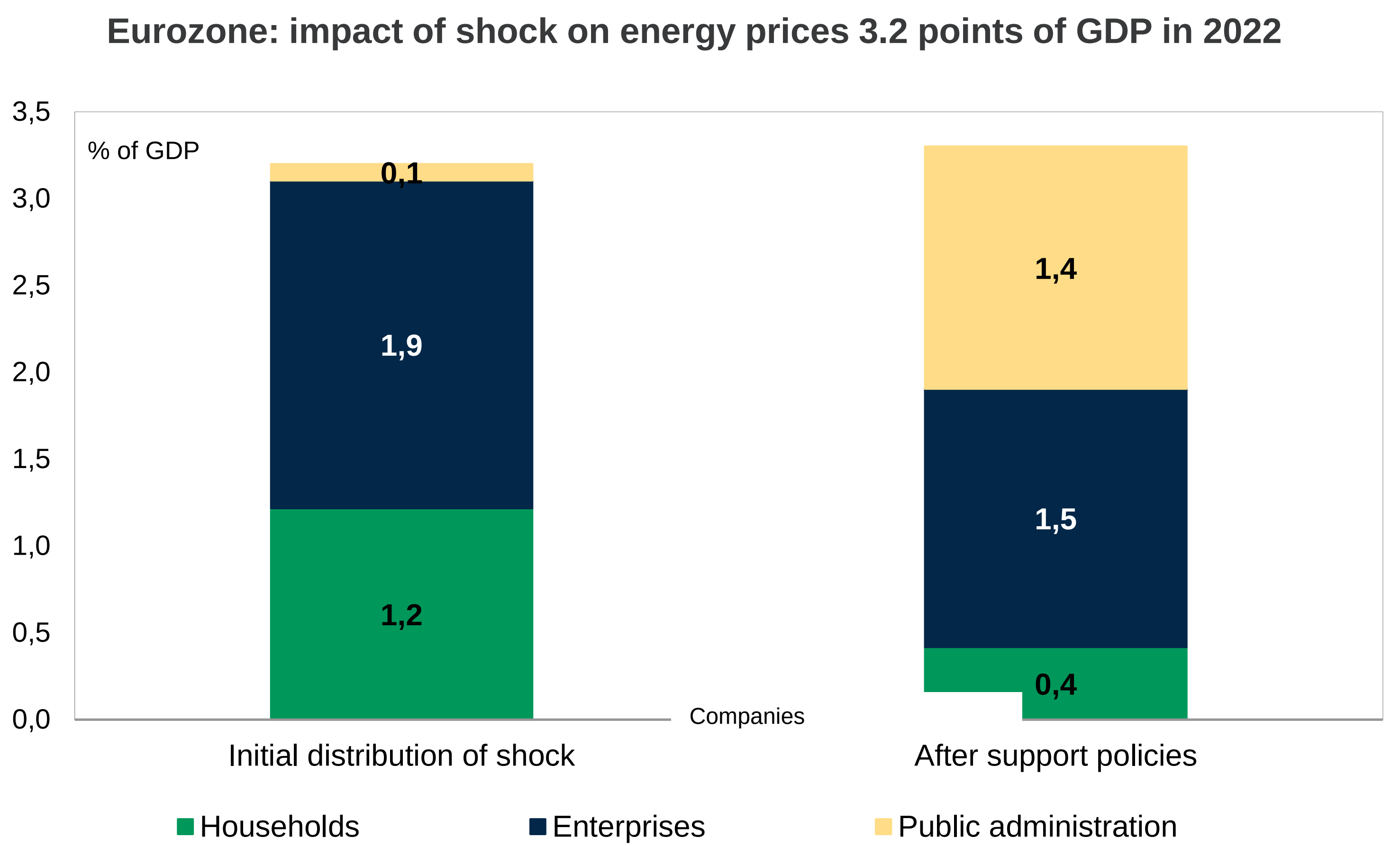



Source : Crédit Agricole S.A.

*Sources: Eurostat, Crédit Agricole S.A./ECO.*

# A CRISIS OF COMPETITIVENESS

## IMMEDIATE AND SUBSTANTIAL BUT AMORTISED




*Sources: Eurostat, Crédit Agricole S.A./ECO.*

# MORE HARMONIOUS RESPONSE

## TO SUPPLY SHOCKS

**Mapping of risks related to the crisis in competitiveness and the slowdown in the manufacturing cycle**

| | Manufacturing as a share of GDP | Share of energy-intensive industrial sectors | Electricity prices for companies (€ per kWh) | Share of exports in GDP | Trade exposure to China | Trade exposure to USA | Trade exposure to Germany |
|---|---|---|---|---|---|---|---|
| Germany | 20.3 | 5.1 | 0.26 | 18.2 | 6.4 | 10 | |
| France | 10.9 | 3 | 0.15 | 9.9 | 4.3 | 7.4 | 13.7 |
| Italy | 15.8 | 3.3 | 0.39 | 15.6 | 3.2 | 10.5 | 12.2 |
| Spain | 12.7 | 3.1 | 0.28 | 10.6 | 2 | 4.8 | 10.1 |
| Netherlands | 12.6 | 3.3 | 0.21 | 27.2 | 2.2 | 4.3 | 26.2 |
| Belgium | 13.6 | 6.4 | 0.28 | 32.8 | 1.4 | 5.8 | 20.9 |
| Portugal | 14.5 | 3.1 | 0.18 | 9.4 | 0.8 | 6.2 | 11 |
| Greece | 9.9 | 3.3 | 0.24 | 10.9 | 0.8 | 3.8 | 6.5 |
| Finland | 18 | 3.5 | 0.17 | 12.7 | 5 | 9.6 | 11 |
| Austria | 17.2 | 5 | 0.24 | 13.6 | 2.5 | 6.7 | 29.4 |

*Sources: Eurostat, Crédit Agricole S.A./ECO.*

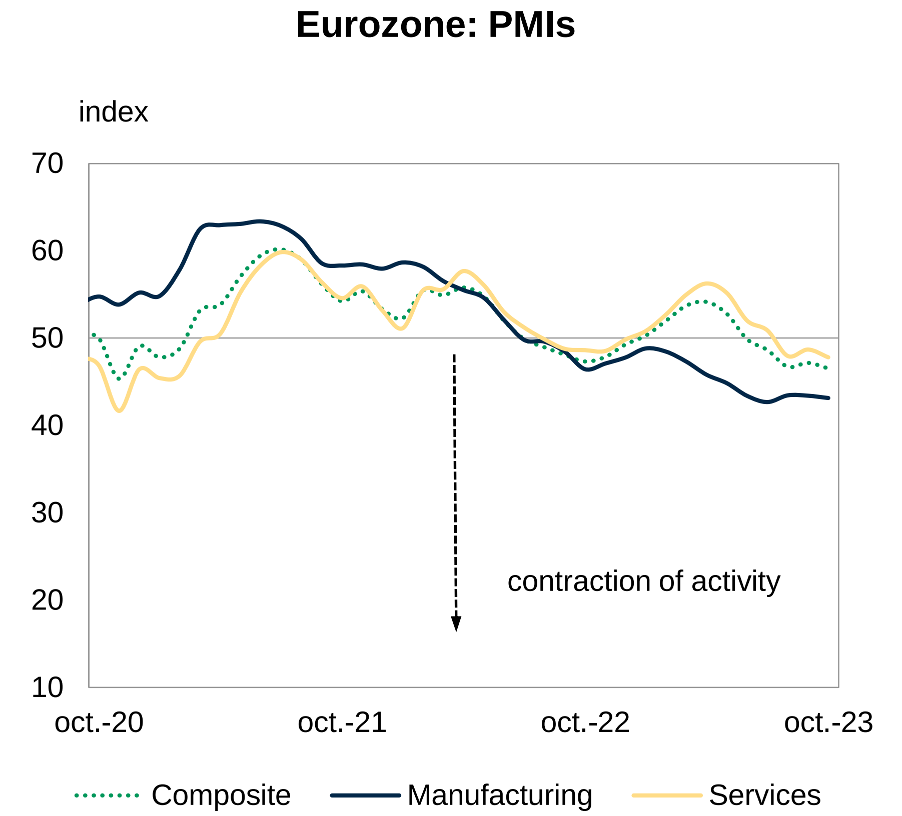
# RECENT DEVELOPMENTS AND SHORT-TERM SCENARIOS

## ECONOMIC SLOWDOWN INTENSIFIES AT THE BEGINNING OF THE THIRD QUARTER

**The slowdown in activity is expected to intensify in the third quarter.**

**Surveys point to a sharper deterioration in manufacturing activity and the end of the expansion in the services sector.** At 46.5 points in October (after 47.2 in September), the composite PMI for the eurozone declined for the fifth month in a row to reach a three-year low. Excluding the pandemic period, this is the sharpest decline in activity in the last decade. But the trend needs to be read against the brisk initial pace resulting from the post-pandemic reopening. The decline in new orders is accelerating sharply, continuing to reduce order backlogs. Despite these trends, confidence improved slightly with an increase in the production outlook.

In the manufacturing sector, the index deteriorated further in October (to 43 points after 43.4), decreasing for the seventh consecutive month. **Orders are once again declining sharply, but so are inventories of finished goods, leading to a recovery in the order-to-inventory ratio for the first time since March. Purchases of inputs have also decreased, and with the decrease in orders exceeding the decrease in production, backlogs continue to narrow, limiting future production.** Purchasing managers are still expecting manufacturing production to increase, but the momentum is slowing. The contraction in hiring under way for the past four months is accentuating. In the services sector, the index (at 47.8 points after 48.7) showed a third consecutive month of contraction in activity in October and an acceleration in the contraction. Despite the deterioration in new business, future activity is reported to be growing more strongly. Job creations are still positive but less vigorous.




*Sources: S&P Global, Crédit Agricole S.A.*

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# THE NATURE OF THE LANDING WILL HINGE ON THE INTERPLAY BETWEEN TWO FACTORS: MONETARY TIGHTENING AND DISINFLATION

***A modest recovery underpinned by consumption***

**With a growth overhang of 0.5% in Q2 2023 and weak demand from the rest of the world, our scenario is based on a modest recovery in domestic demand. While failing to offset past losses in purchasing power, the increase in purchasing power linked to disinflation at the end of the year could nevertheless lend a boost to household disposable income in real terms.**

**The growth rate in labour supply and employment in the eurozone remained positive but slowed somewhat in the second quarter.** Working hours are still on the rise overall, except in the industrial and construction sectors, which have already started to reduce working hours. Job creations, still positive in Q2 (+0.2% after 1.6% in Q1 2023) and a further increase in wages per worker (0.7% over the quarter) continued to fuel **growth in nominal household disposable income (1.3%).**

**Though the pace of this growth is weakening (after 2.5% in Q1 2023), it remains higher than that of prices.** The private consumption deflator rose by just 0.9% in Q2, less than in Q1 (+1.3%), leading to **a second quarter of gains in real disposable income (+0.4% in Q2 2023 after +1.1% in Q1 2023). These gains in purchasing power did not translate into more consumption but were transferred entirely to savings.** After increasing by 1.2 points in Q1, the savings rate increased by another 0.3 points to 14.8%. The savings rate has recovered since Q4 2022 and once again exceeded its pre-pandemic average after the decline in summer 2022. **Rather than dipping into the excess savings built up since COVID-19, households continue to increase them.** While the excess savings are not evenly distributed among households (the two highest quintiles of income distribution claiming the lion's share), and while they have been invested in part in illiquid assets, they still have the potential to cushion the negative effects of monetary tightening on private consumption.

Growth in nominal disposable income has picked up since the end of 2021 on an increasingly positive contribution from remuneration, despite an increasingly smaller contribution from net property income due to the increase in the share of interest expenses, up 1.5 points over the past year. Real disposable income, after falling continuously between summer 2021 and summer 2022, is now benefiting from this momentum, as well as from disinflation.

**We expect unemployment to rise slightly as job creations slow and labour force dynamics to remain strong. Employment will therefore continue to support household income. The increase in wages per worker, up 5.5% year-on-year in Q2 2023, can no longer be fuelled by labour market tensions, which are now on the decline. But wage momentum will remain strong in 2024, at close to 4%, well above the inflation rate.** Wage negotiations at the end of the year, particularly in Germany, are still pointing to substantial wage growth at the turn of the year. Wages are expected to outpace inflation at the end of the year and in 2024, ensuring a positive contribution to real income growth. These factors underpin our scenario of a moderate acceleration in household consumption in 2024.

# THE LOGIC BEHIND THE SCENARIO

## THE NATURE OF THE LANDING WILL HINGE ON THE INTERPLAY BETWEEN TWO FACTORS: MONETARY TIGHTENING AND DISINFLATION

*Wealth effects*

Housing plays an important role in the transmission of monetary policy, particularly in the current tightening cycle, which follows several years of substantial growth in house prices and credit in some eurozone countries. **Negative wealth effects, mainly through rising interest expenses, serving to crowd out consumption are modest in the eurozone. While the share of homeowners with a loan and the household debt ratio have increased in some countries, the share of variable-rate loans has decreased, making households less vulnerable to rising interest rates.** These indicators do not give rise to fears of a significant reduction in resources available for consumption. The countries having experienced the greatest increases in debt are also those where disposable income has risen sharply in recent years and where the savings rate is highest. These factors point to a possible amortisation of the increase in the cost of servicing the debt on consumption. The latter is expected to grow 1.1% in 2024, after 0.4% in 2023. Moreover, these indicators have converged over the past decade between countries and the eurozone presents fewer asymmetric risks linked to the weakness of household balance sheets, particularly from “systemic” countries. In addition, variable-rate loans are being renegotiated in the most exposed countries.

*Investment is picking up with contrasting dynamics*

**With the expected erosion of profitability and the rising costs linked to the gradual transmission of monetary policy, investment is unlikely to pick up significantly.** The deterioration in productivity since the end of 2022 continued in the second quarter of 2023 (-1.4% yoy). The increase in unit labour costs, driven by the ever-faster growth in wages per worker (5.5% yoy), will no longer be able to be passed on to selling prices in a disinflationary environment.

This **gradual loss of pricing power has already been demonstrated by industry and services surveys.** This reduces the risk of second-round effects driven by margins. **However, investment in infrastructure and in the dual transition continues to be financed by NextGeneration EU funds and, in strategic sectors, by state aid.** In addition, investment in transport goods will continued to be bolstered by the renewal of company car fleets. **These factors offset the sharp decline in housing investment. Investment is expected to grow extremely modestly (1.1% in 2023 and 2024).**

# THE LOGIC BEHIND THE SCENARIO

## DEMAND SLUGGISH BUT POISED TO RECOVER

***Monetary tightening already visibly impacting activity***

Demand and activity are already being affected in the housing sector, and the volume of business spending is adapting to interest rates well above the equilibrium level. The transmission of monetary tightening is being felt strongly both on volumes and rates, particularly through banking. And part of the transmission still lies ahead, set to play out between now and mid-2024.

***Net credit demand down***

Monetary supply in the eurozone fell once again in September year-on-year (-1.2% after -1.3% for M3) resulting in a sharp decrease in the still positive contribution of credit to the private sector (with a smaller year-on-year increase of 0.2% after 0.6%). **The slowdown in (adjusted) loans to non-financial companies (NFCs) was more pronounced (from 0.7% yoy to 0.2%) than that of loans to households (from 1% yoy to 0.8%).** This is especially true when comparing the former to their post-financial crisis growth peak of 8.9% in September-October 2022. For household loans, the slowdown came a little earlier and started from a lower growth rate (the post-financial crisis peak being 4.6% in April-June 2022). But the slowdown in home loans was equally emphatic, with growth of just 0.2% year-on-year in September.

**According to the ECB's BLS survey, the decline in demand for credit was significant and stronger than expected in Q3 2023, both from NFCs and households**. For households, this applied to home loans and consumer credit. For companies, the decline resulted primarily from the decrease in investment and M&A activity, while the need for circulating capital and inventories generated stable demand for credit. Banks expect net demand from businesses and households to decline further in Q4 2023, albeit at a slower pace. But the weakening of credit flows is not informed solely by the decline in demand.

***Credit supply decline to last***

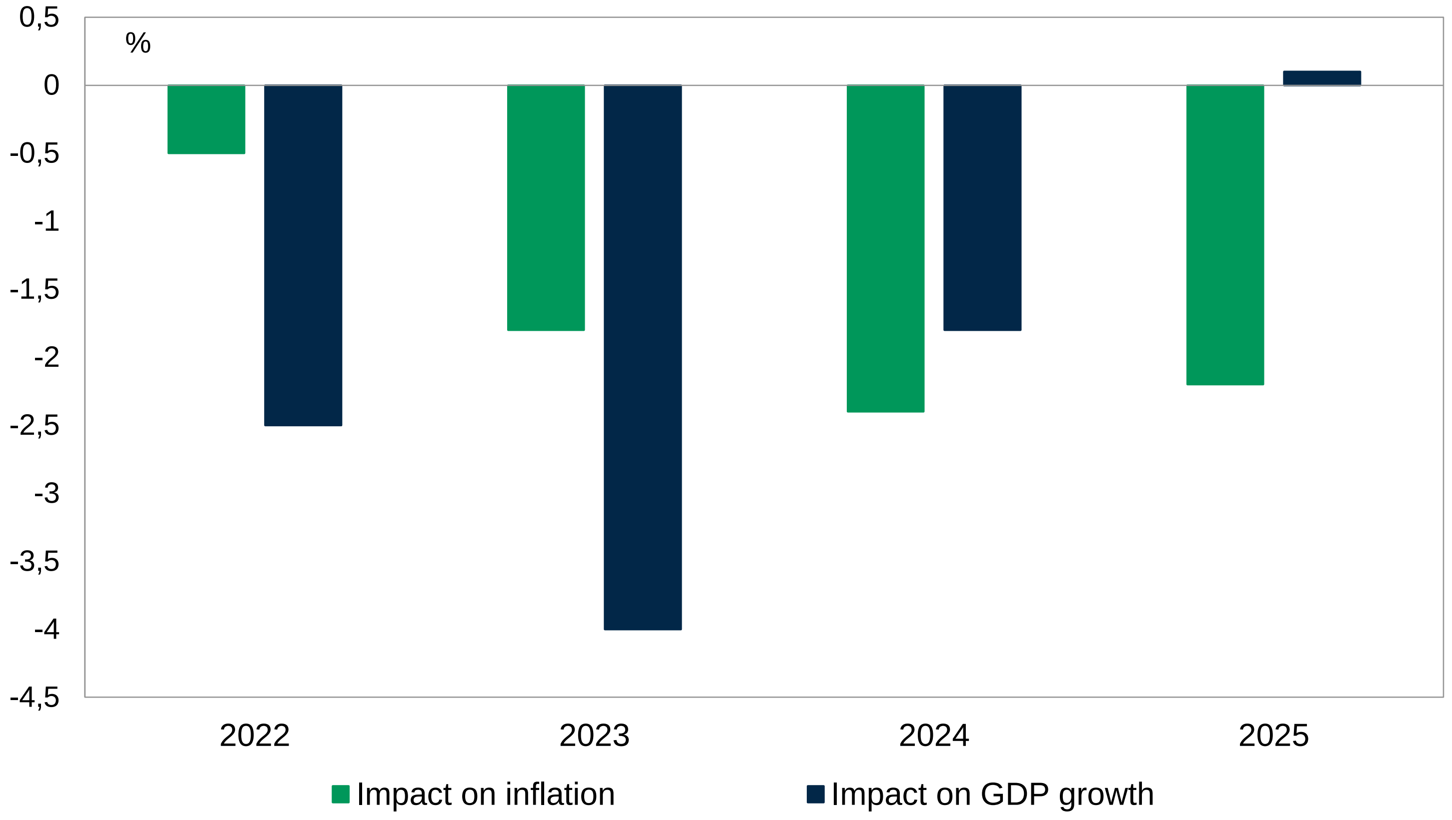
**Supply is also shrinking, with the number of rejected loan requests exceeding their historical average. Credit terms and conditions also tightened sharply in the third quarter, particularly for home loans, but also, and significantly, for NFCs.** The pace of tightening has eased slightly but remains above its average since Q2 2022.

For Q4 2023, banks are expecting continued tightening at a more moderate pace for NFCs, at the same pace for home loans and at a higher pace for consumer credit. **Bank financing is considered as harder to access and the higher risk borne by the private sector justifies a further tightening of credit supply in the coming quarters.**

# MONETARY TIGHTENING

## TRANSMISSION TO ACTIVITY: PEAK IN 2023

**The impact of monetary tightening has yet to be fully felt**




*Sources: ECB, Crédit Agricole S.A./ECO.*

# RESPONSE TO MONETARY TIGHTENING

## MORE HARMONIOUS THAN BEFORE

**Mapping of risks related to the channel of negative wealth effects on consumption**

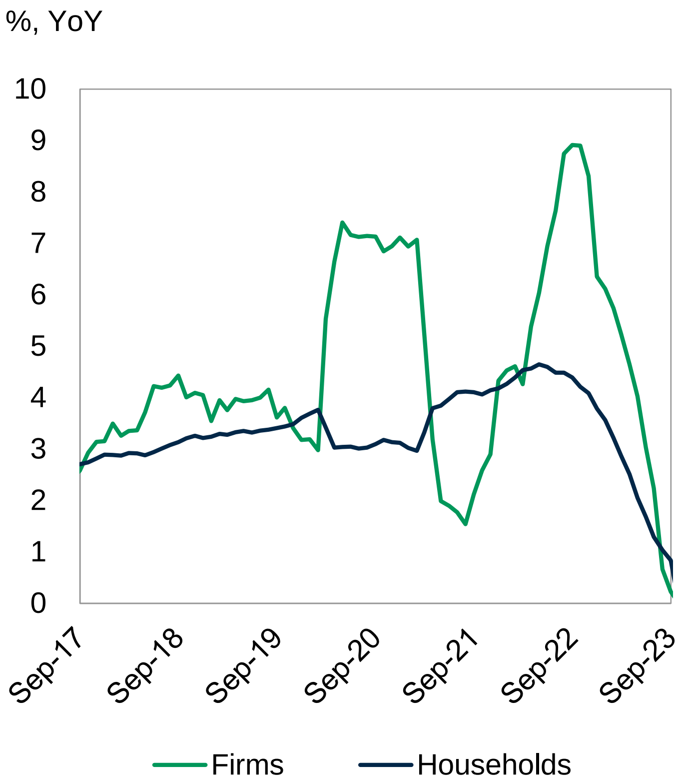
| | Share of owners with a loan | Share of variable-rate loans (new loans) | Household debt (% of GDP) | Change in outstanding loans (adjusted) since 2017 | Change in housing prices since 2014 |
|---|---|---|---|---|---|
| Germany | 18.2 | 11.6 | 57.4 | 42.5 | 70.6 |
| France | 23.1 | 0.8 | 75.2 | 42.8 | 30 |
| Italy | 10.8 | 40.0 | 48.0 | -16.9 | 2.8 |
| Spain | 26.4 | 23.7 | 63.1 | -9.8 | 47 |
| Netherlands | 48.8 | 14.3 | 104.2 | 3.5 | 93 |
| Belgium | 33.2 | 7.8 | 63.8 | 38.6 | 36.4 |
| Ireland | 28.7 | 10.8 | 32.6 | 15.5 | 82.8 |
| Portugal | 32 | 76.5 | 79.8 | -1.2 | 96 |
| Greece | 9.2 | 44.4 | 60.8 | -26.0 | |
| Finland | 30.5 | 95.5 | 81.5 | 35.2 | 11.7 |
| Austria | 18.9 | 39.6 | 53.1 | 44.4 | 79.1 |

*Sources: Eurostat, ECB, EMF-Hypostat, Crédit Agricole S.A./ECO.*

# MONETARY TIGHTENING

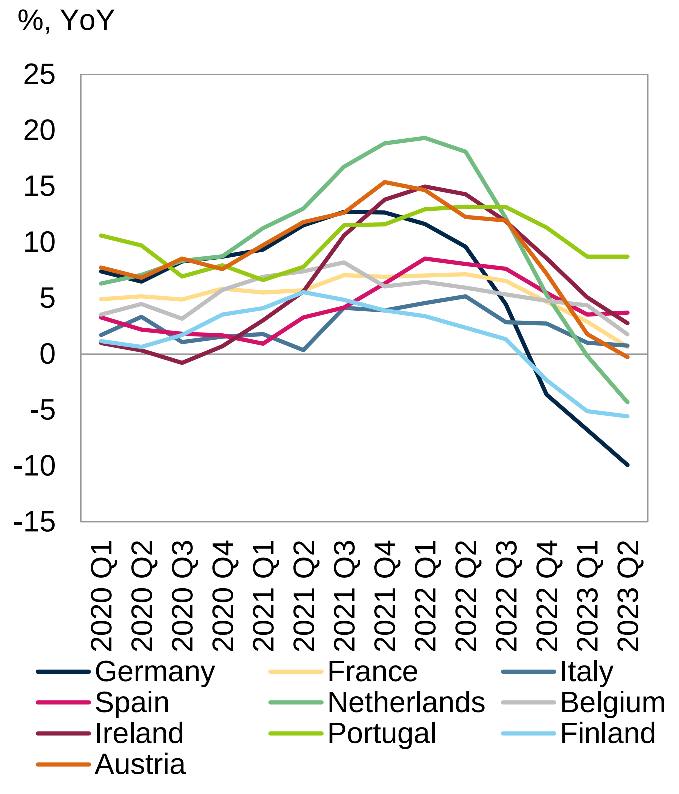
## INITIAL IMPACT ON ACTIVITY ALREADY VISIBLE

### Change in outstanding adjusted bank loans




*Sources: ECB, Crédit Agricole S.A./ECO.*

### Property market correction

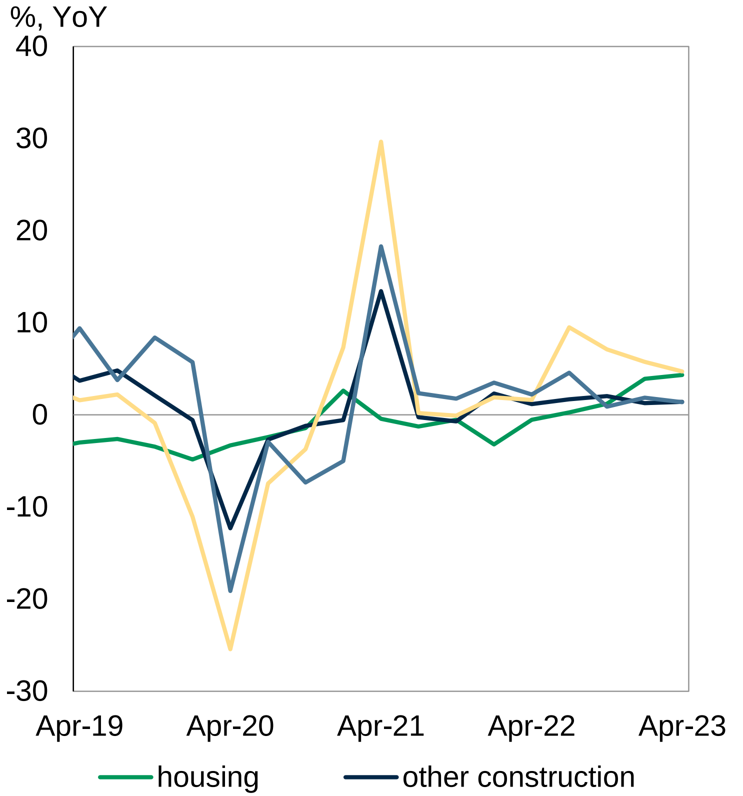



*Sources: Eurostat, Crédit Agricole S.A./ECO.*

# MONETARY TIGHTENING

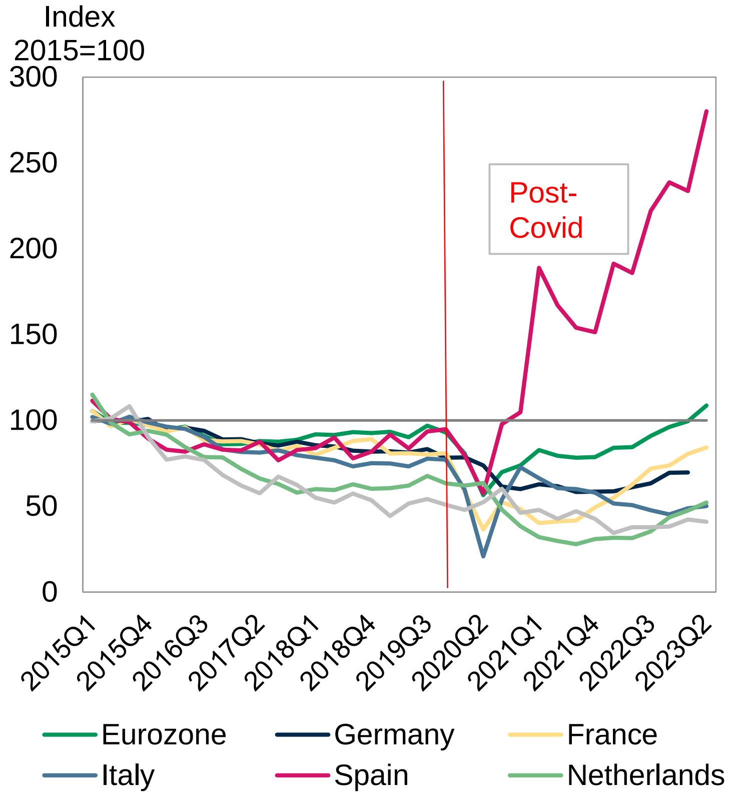
## INITIAL IMPACT ON ACTIVITY ALREADY VISIBLE

### Investment: the first victim




*Sources: Eurostat, Crédit Agricole S.A./ECO.*

### Business failures: slow recovery

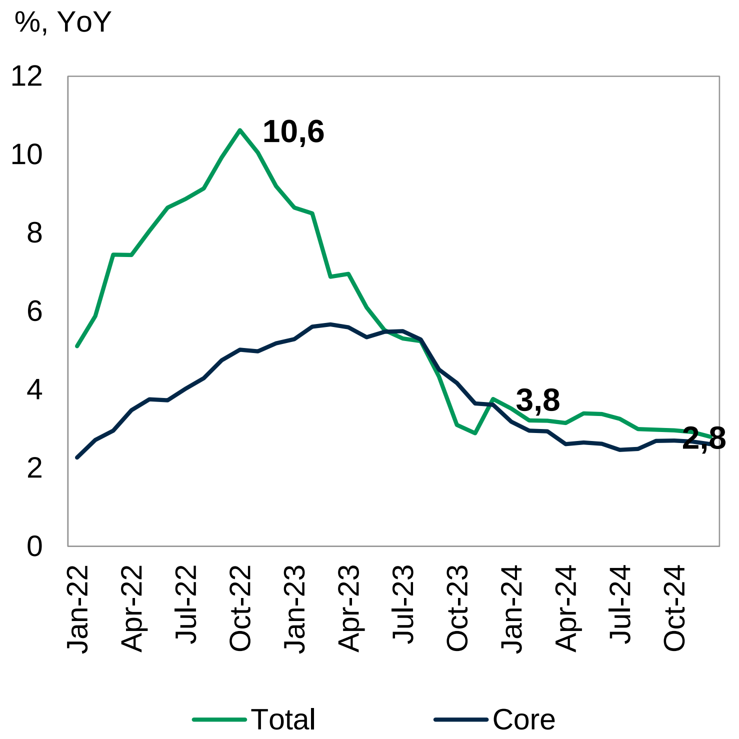



*Sources: Eurostat, Crédit Agricole S.A./ECO.*

# INFLATION DECLINE

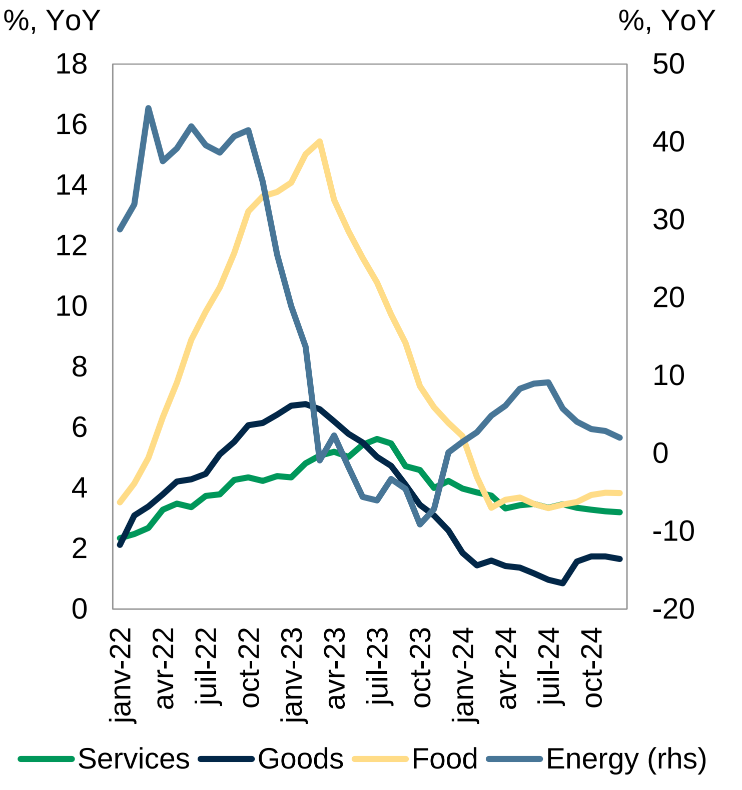
## LARGELY MECHANICAL

**Inflation falls sharply but remains above the 2% target**




*Sources: Eurostat, CACIB, Crédit Agricole S.A./ECO.*

**Upstream pressures lift, end of dissemination**

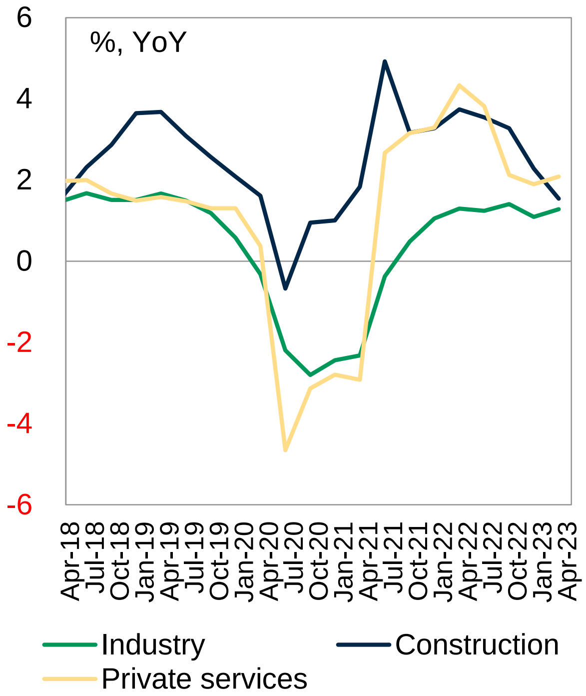



*Sources: Eurostat, CACIB, Crédit Agricole S.A./ECO.*

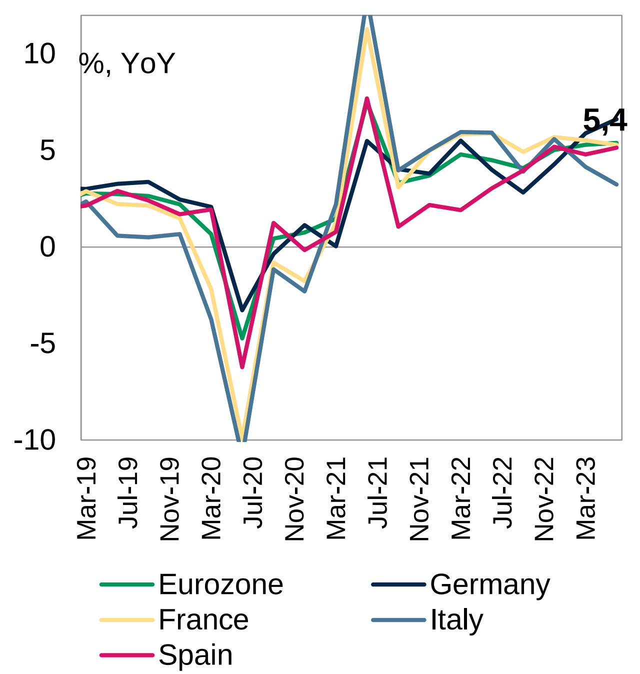
# PURCHASING POWER RECOVERY

## SUPPORTED BY EMPLOYMENT AND WAGES

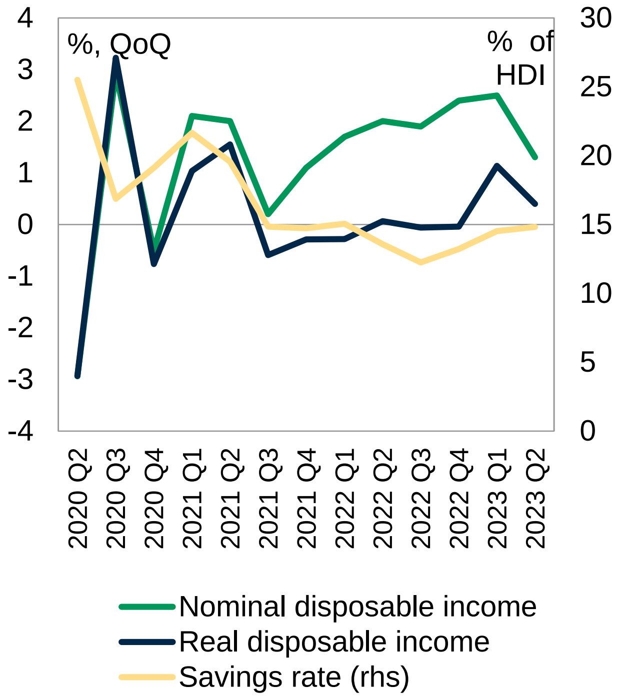
### Job creation: faster than activity




### Salary per worker: delayed adjustment to past inflation




### Purchasing power gains saved




*Sources: Eurostat, Crédit Agricole S.A./ECO.*

# THE LOGIC BEHIND THE SCENARIO

## ECB: FROM GUIDING EXPECTATIONS TO OBSERVING DATA

***Don't be fooled by the closeness of the destination***

Despite the power of monetary policy transmission and its visible impact on inflation, the ECB's message **at its last meeting on 26 October** is that we should not be fooled by the closeness of the destination, because the last mile is always the toughest to travel. Consequently, at the ECB's most recent meeting, at which it **maintained key interest rates at 4.5% for the refinancing rate and 4% for the deposit rate,** the Governing Council **discussed neither a date for an initial rate cut nor the extent of this possible cut.** The focus for now is not on guiding expectations but on observing data. The ECB will continue to gather evidence of a sustained and widespread decline in inflation.

***Taking no risks on second-round effects***

The central bank's key concern is to rule out any risk of second-round effects. **The ECB sees the wage rises of 2023 as the natural catch-up of inflation in 2022 and is now seeking to ensure that this process ends in 2024, with a slowdown in wage growth consistent with the disinflationary process under way.** For the time being, **the data from the latest wage negotiations in June 2023 (with negotiated wages increasing 4.3% yoy in Q2) for the following 12 months do not clearly herald a turning point in wage growth**. However, the Indeed leading indicator for posted jobs points to a sharp deceleration in wage growth for these jobs since the spring. The ECB is also seeking to gauge how much wage increases will be absorbed by profits without being fully passed on to prices. The response of companies will naturally depend on demand, already negatively affected by monetary policy. The ability of companies to pay higher wages already appears to be diminished, with an initial drop in the margin rate in Q2 2023 in the eurozone and a smaller contribution from margins to the growth of the GDP deflator. **But the ECB will have to wait for the initial results of collective bargaining in spring 2024 before it can be reassured about the stability of inflation expectations around its target.**

***Keeping an eye on expectations***

**Expectations remain largely informed by the Q4 Survey of Professional Forecasters (SPF) and the September Survey of Monetary Analysts (SMA), which show that the median of long-term expectations is stable at 2%.** Market expectations extracted by inflation compensation instruments have shown a rise in 5-year expectations in 5 years above 2.5% since July, owing primarily to an increase in the risk premium rather than an increase in expectations. More recently, the deteriorating growth outlook has served to bring these expectations down to 2.5%. The ECB is keeping a close eye on the latest August results of its consumer survey, which for the second month in a row showed an upwards revision of the median forecast for 2026, now at 2.5%. This rise in inflation expectations, albeit with a one-year horizon, was also demonstrated by European Commission consumer surveys in September, but not by the consumer surveys of retail and services companies. While the October PMIs point to a slight acceleration in input prices in services, the increase in sales prices continues to slow with a tightening of margins, while in industry price indices are contracting across the board.

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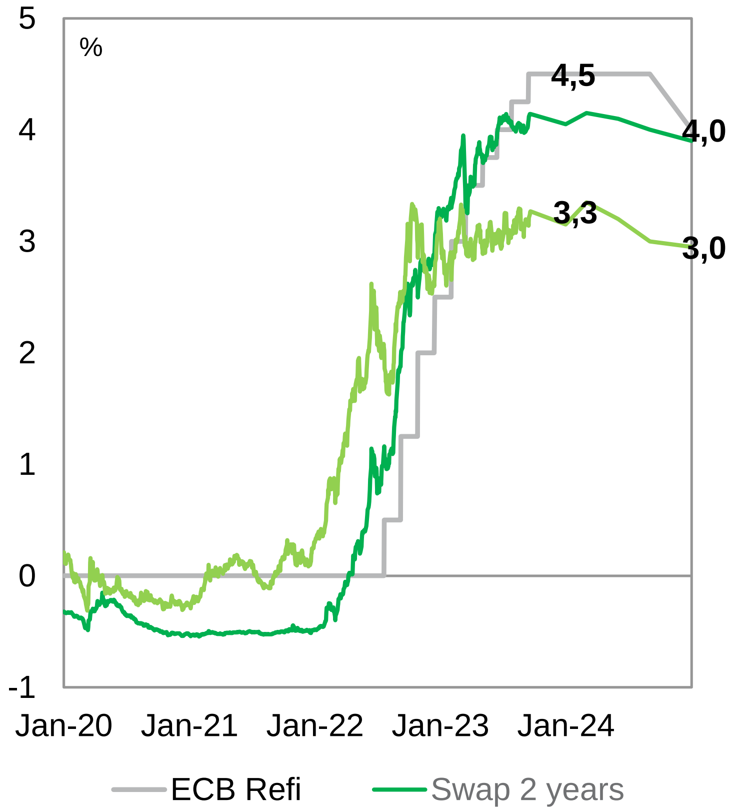


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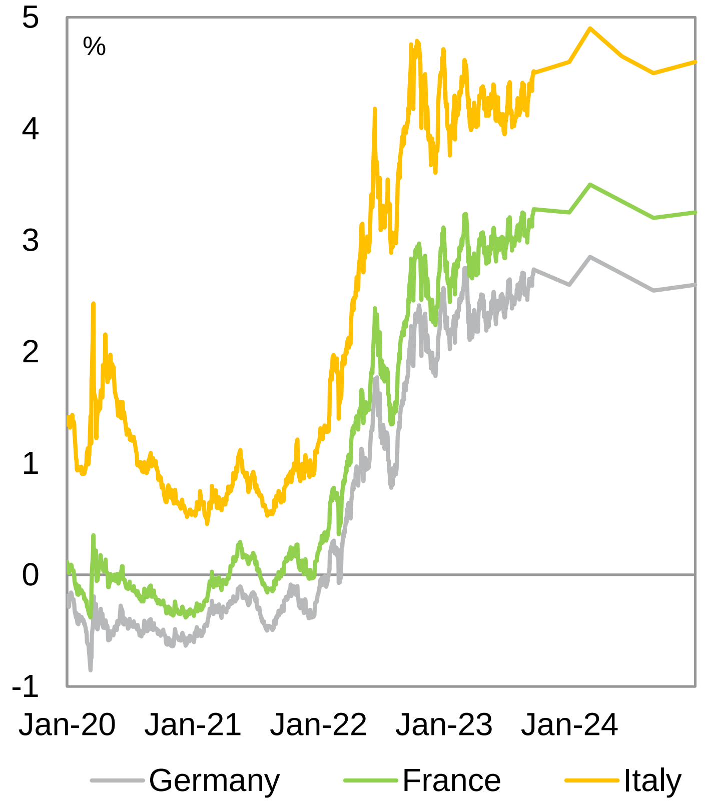


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