



Economic Situation and Strategy

15 September 2023

ECB: All birds fly high

Do you know the game "All birds fly high" from your childhood? All the players sit at a table and drum with their fingertips on the tabletop. When the game leader calls out "All the birds are flying high", all the players raise their hands in the air with their arms outstretched. Then the game leader calls out another animal, e.g. "All horses fly high"! The players now have to think quickly whether the animal can fly. If it cannot, they must not put their hands in the air. If someone does put their hands up by mistake, they are eliminated from the game. A fun game in which you have to think and react as fast as lightning.

Now, it is not known whether the vote on today's ECB interest rate decision also took place in this way and whether Ms Lagarde acted as the game leader. But we can imagine that there was an intense discussion between the "hawks", who voted for a further tightening of monetary policy, and the "doves", who did not want to raise interest rates any further. In the end, the former retained the upper hand, so that in the vote either all or at least a large majority in the Governing Council voted in favour of an interest rate hike. Whether dove or hawk, both are birds after all.

The new growth and inflation projections of the ECB economists are likely to have been decisive for this decision. Above all, the increase in the inflation forecast for the coming year from the previous 3.0 to 3.2 per cent is likely to have paved the way for an even more restrictive monetary policy. We consider this assessment surprising, not to say questionable, for two reasons: First, it assumes a relatively significant decline in price pressures for the

rest of 2023, which is the only way the forecast of 5.6 per cent at the end of the year can still be achieved. After eight months, the increase is 6.6 per cent, so that an inflation rate of only 3.5 per cent is expected for the remaining four months; this is sportive. In contrast, we consider the forecast for 2024 to be significantly too high; our own estimate is 2.7 per cent. The reasons for this lie in the expected development of US inflation, which we discuss in more detail below. Conversely, the growth forecasts of 0.7 per cent for 2023 (previously 0.9 per cent) and 1.0 per cent for 2024 (previously 1.5 per cent) seem too optimistic to us, not least because of the dampening effect of restrictive monetary policy. We therefore only expect growth rates of 0.5 and 0.9 per cent.

In this respect, we assume that this was the last interest rate step in this cycle. This is also how we interpret Ms Lagarde's statements at the press conference. At the next ECB meeting on 26 October she should therefore rather shout "All penguins fly high" during the vote. Because even though penguins are birds, they cannot fly. Therefore, all hands should remain down.

US inflation: Mission almost accomplished

The latest US inflation data for the month of August caused confusion: while the headline inflation rate rose from 3.2 to 3.7 percent, the core inflation rate, which excludes energy and food prices, fell from 4.7 to 4.3 percent. The different direction of the two rates is due to the development of energy prices. For example, the sharp rise in the price of oil from around 70 US dollars in June to almost 90 US dollars recently led to higher prices for fuel and transport services. Higher petrol prices alone were responsible for more than half of the monthly price

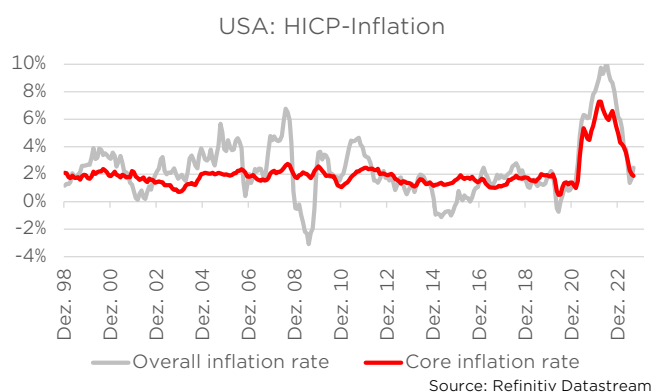
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increase. As in the previous months, the second largest price driver was the imputed rents of flat owners. However, price pressures have eased considerably for most components of the basket of goods. Foodstuffs were still 4.3 per cent more expensive in August than twelve months ago; in January their annual rate of change had still been over ten per cent. The price increase for new cars halved in the same period from six to three per cent, the same applies to restaurant visits.

Nevertheless, both headline and core inflation rates are still well above the Federal Reserve's target of two per cent. Therefore, the Fed will not declare inflation defeated at the moment. However, if one digs a little deeper into the price statistics, one comes across findings that allow the conclusion that the degree to which the target has been reached is much higher than it appears at first glance. US inflation is strongly influenced by the shelter component, which in August was more than seven per cent higher than a year earlier. Housing costs account for a good 34 percent of the total basket of goods and just under 45 percent of core inflation. The CPI housing inflation index is designed to measure changes in consumer spending on the entire stock of housing services. Therefore, the index includes both the rents of households that have just moved and are paying the current asking rent and the rents of households that have not moved and are therefore paying a different rent. However, ongoing changes in asking rents are gradually incorporated into the rent index as households move or landlords update their leases. Therefore, house and rent price indices can provide information on the future development of housing inflation. Based on this assumption, housing inflation is expected to weaken significantly in the coming months.

But what does the price development look like without the ominous component "residential real estate"? Overall US inflation excluding housing was 1.8 per cent in August, the core inflation rate excluding shelter, also known

as "super-core inflation", was 2.3 per cent. It is hard to believe, but these figures correspond roughly to the picture that emerges when US inflation is calculated on the basis of the HICP, the hard-core consumer price index used here in the Eurozone. This is because imputed rents, for example, play no role at all in this index. The overall inflation rate calculated by the US Bureau of Labor Statistics was 2.5 per cent in August (after 1.7 and 1.4 per cent in the two previous months), the core inflation rate was 1.9 per cent (after 2.0 and 2.3 per cent in July and June).



The US Federal Reserve is likely to take a generally favourable view of the inflation trend and interpret that its significant interest rate hikes of the past 18 months are increasingly having the desired effect. We therefore assume that key interest rates will not be raised further in the coming week. We also no longer expect a rate hike for the last two FOMC decisions this year on 7 November and 18 December, while market expectations are currently still around 40 percent.

Our conclusion: Both in the euro area and in the US, the cycle of interest rate hikes is over. Moreover, with regard to inflation, the Fed will announce "mission accomplished" sooner than the ECB.

Carsten Klude

Market data

Stock markets	As of	Change versus				
	15.09.2023 14:39	07.09.2023 -1 week	11.08.2023 -1 month	13.06.2023 -3 months	13.09.2022 -1 year	30.12.2022 YTD
Dow Jones	34907	1,2%	-1,1%	2,0%	12,2%	5,3%
S&P 500	4557	2,4%	2,1%	4,3%	15,9%	18,7%
Nasdaq	13926	1,3%	2,1%	2,6%	19,7%	33,1%
DAX	15945	1,4%	0,7%	-1,8%	20,9%	14,5%
MDAX	27471	1,1%	-2,2%	0,0%	8,5%	9,4%
TecDAX	3129	0,6%	0,0%	-3,7%	6,3%	7,1%
EuroStoxx 50	4315	2,2%	-0,1%	-0,8%	20,3%	13,7%
Stoxx 50	4041	2,4%	1,7%	1,2%	13,7%	10,7%
SMI (Swiss Market Index)	11217	2,0%	1,2%	-1,0%	3,0%	4,5%
Nikkei 225	33533	1,6%	3,3%	1,6%	17,2%	28,5%
Brasilien BOVESPA	119392	2,9%	1,1%	2,3%	7,8%	8,8%
Russland RTS	1024	1,0%	2,4%	-0,6%	-20,2%	5,6%
Indien BSE 30	67839	2,4%	3,9%	7,4%	12,0%	11,5%
China CSI 300	3709	-1,3%	-4,5%	-4,0%	-9,8%	-4,2%
MSCI Welt	2983	1,2%	0,3%	1,8%	13,9%	14,6%
MSCI Emerging Markets	982	0,9%	-1,6%	-3,1%	0,2%	2,7%
Bond markets						
Bund-Future	131,23	7	-24	-242	-1216	-170
Bobl-Future	116,32	107	93	-2	-554	57
Schatz-Future	105,03	22	4	-29	-274	-39
3 Monats Euribor	3,87	22	21	72	287	198
3M Euribor Future, Dec 2023	4,00	11	9	22	148	39
3 Monats \$ Libor	5,67	0	4	12	238	90
Fed Funds Future, Dec 2023	5,44	-1	3	27	158	80
10 year US Treasuries	4,33	7	16	51	91	50
10 year Bunds	2,66	7	7	23	93	10
10 year JGB	0,72	7	14	30	47	31
10 year Swiss Government	1,05	1	-3	9	-2	-55
US Treas 10Y Performance	576,38	0,1%	-0,3%	-2,5%	-3,3%	-0,6%
Bund 10Y Performance	533,72	-0,3%	-0,1%	-1,0%	-5,0%	1,6%
REX Performance Index	431,08	-0,2%	-0,5%	-1,0%	-4,0%	-0,3%
IBOXX AA, €	3,84	3	9	19	97	25
IBOXX BBB, €	4,68	1	12	14	67	-2
ML US High Yield	8,63	-4	9	4	18	-35
Convertible Bonds, Exane 25	6620	0,0%	0,0%	0,0%	0,5%	0,0%
Commodities						
MG Base Metal Index	383,72	0,5%	1,1%	-0,8%	-3,6%	-8,3%
Crude oil Brent	93,86	4,3%	8,1%	26,3%	0,6%	10,5%
Gold	1915,90	-0,1%	-0,1%	-1,8%	12,4%	5,5%
Silver	22,89	-5,5%	1,0%	-3,7%	17,7%	-3,6%
Aluminium	2177,25	1,2%	2,5%	-0,8%	-5,3%	-7,3%
Copper	8397,50	1,1%	1,7%	-0,6%	5,0%	0,4%
Iron ore	120,56	2,7%	14,4%	7,2%	18,9%	8,3%
Freight rates Baltic Dry Index	1340	17,4%	18,7%	24,8%	-4,8%	-11,6%
Currencies						
EUR/ USD	1,0645	-0,6%	-3,3%	-1,4%	4,6%	-0,2%
EUR/ GBP	0,8588	0,1%	-0,5%	0,2%	-1,0%	-3,2%
EUR/ JPY	157,45	-0,2%	-1,0%	4,5%	9,0%	11,9%
EUR/ CHF	0,9551	-0,1%	-0,7%	-2,4%	-1,2%	-3,0%
USD/ CNY	7,2764	-0,8%	0,5%	1,6%	4,4%	5,4%
USD/ JPY	147,47	0,1%	1,7%	5,2%	2,0%	12,5%
USD/ GBP	0,81	0,7%	2,6%	1,7%	-6,8%	-2,9%

Source: Refinitiv Datastream

Carsten Klude
+49 40 3282-2572
cklude@mmwarburg.com

Dr. Rebekka Haller
+49 40 3282-2452
rhaller@mmwarburg.com

Martin Hasse
+49 40 3282-2411
mhasse@mmwarburg.com

Dr. Christian Jasperneite
+49 40 3282-2439
cjasperneite@mmwarburg.com

Simon Landt
+49 40 3282-2401
mlandt@mmwarburg.com

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