

ECB preview

First interest rate cuts are most likely in summer now

- Inflation falls, but slower than expected; manufacturing keeps struggling, services show signs of recovery
- No policy changes are expected this week, all eyes will be on the revisions of macroeconomic projections

There were no significant changes in economic developments since the last Governing Council meeting, although economic surprise index was slightly positive. Euro area manufacturing PMI remained unchanged and below 50, indicating that industry remains weak. Services PMI, however, has recovered somewhat, while construction PMI – not unexpectedly – sank to the lowest level in years. Real estate sector is the weakest link in most European economies, but despite much lower number of transactions and falling prices so far it had limited negative spillovers into other sectors.

No monetary policy changes are expected during the next week's Governing Council meeting, while the most important information will be new ECB staff macroeconomic projections. Currently the ECB expects inflation to average 2.7% and GDP to grow by 0.8% this year. It is likely that both inflation and GDP growth will be revised downward by a couple decimal points, but not be enough to signal first rate cuts as soon as April. Market currently assigns less than 20% probability of interest rate cut in April (down from almost certainty at the end of last year). For the ECB to start cutting rates this spring we would need to see a lot more economic and financial stress, which is not the base case scenario.

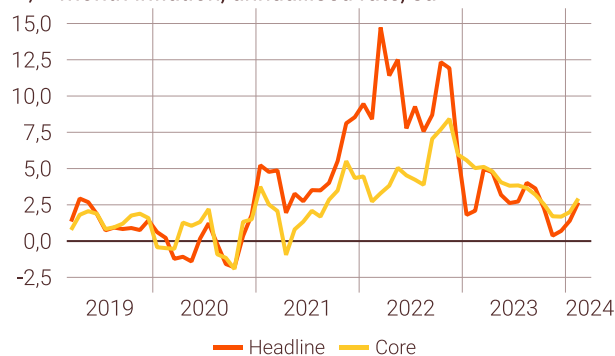
Thus, we revise our forecast and now expect that the ECB will start cutting rates in June. Nevertheless, we still think that rapid disinflation and economic weakness will continue, thus ECB will continue cutting rates in every meeting starting June, leaving deposit rate at 2.75% at the end of 2024.

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Tepid inflation momentum

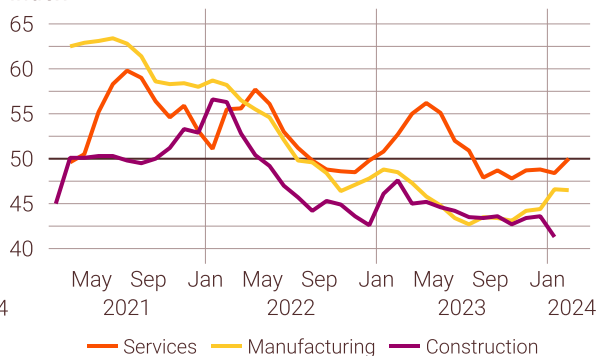
%, 3-month inflation, annualised rate, sa



Källor: Swedbank Analys & Macrobond

Divergence in euro area PMIs

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Sources: Swedbank Research & Macrobond

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