



Liquidity letter

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ECB Forum in Sintra

Sintra, a city suitable for announcements

ECB toughens its words to fight inflation

- ▶ The ECB is still planning a rate hike, and Ms. Lagarde stuck to the central bank's plan by announcing a 25 bp increase in July, putting an end to speculation of a larger increase. The magnitude of the increase in September could be larger, unless the inflation outlook improves rapidly. The ECB will also end its purchases of securities under the APP program as of July 1st.
- ▶ *"Inflationary pressures are broadening and intensifying"* Ms. Lagarde added. Wage growth in the euro zone is expected to double to 4% this year, she said, adding that bottlenecks in production lines are likely to persist
- ▶ According to the ECB President, the era of very low inflation prior to the COVID-19 pandemic will not return and the ECB must act immediately as price inflation will likely remain above the 2% target for years to come - a dramatic change in tone from her previous comments which focused more on a commitment to raise rates only *"gradually"* -

Number of the week

5,8%

French inflation accelerates in June and reaches 5.8% over one year, compared to 5.2% in May



A paradigm shift

Central bankers are calling for the end of the low interest rate era.

The world's major central bankers have warned that the era of low interest rates and moderate inflation is over following the "massive geopolitical shock" caused by Russia's invasion of Ukraine and the coronavirus pandemic.

Speaking at the European Central Bank's annual conference, President Christine Lagarde, Federal Reserve Chairman Jerome Powell and Bank of England Governor Andrew Bailey called for quick action to curb inflation.

They warned that the fragmentation of the global economy into different competitive blocs could fracture supply chains, reduce productivity, increase costs and slow economic growth.

Inflation in France (year-on-year)



Source : INSEE



Towards a global recession?

According to the IMF, global growth is expected to fall to 3.6% in 2022 from 6.1% in 2021, well below the 4.1% forecast last January. This pace of growth is expected to persist until 2023-2024, in a context marked by the war in Ukraine, which is severely disrupting activity, investment and trade in the short term.

The war has caused prices to soar in a wide range of energy products.

Higher energy prices will reduce real incomes, increase production costs, tighten financial conditions and limit the impact of macroeconomic policies, particularly in energy-importing countries.

Thus, the risk of stagflation has increased in a context of a clear slowdown in global growth.

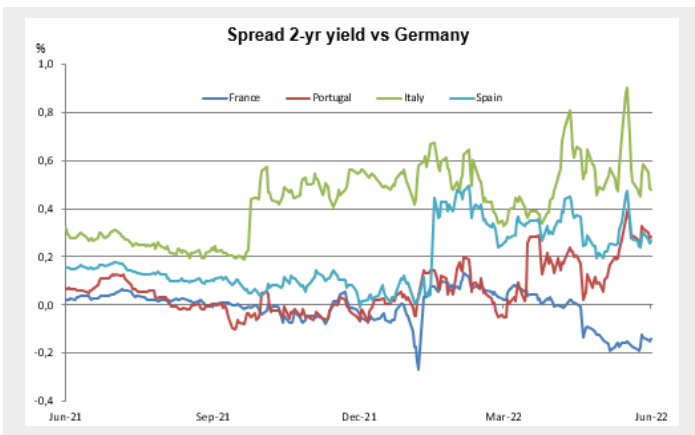


Inflation in the euro area is undesirably high and it is projected to stay that way for some time to come



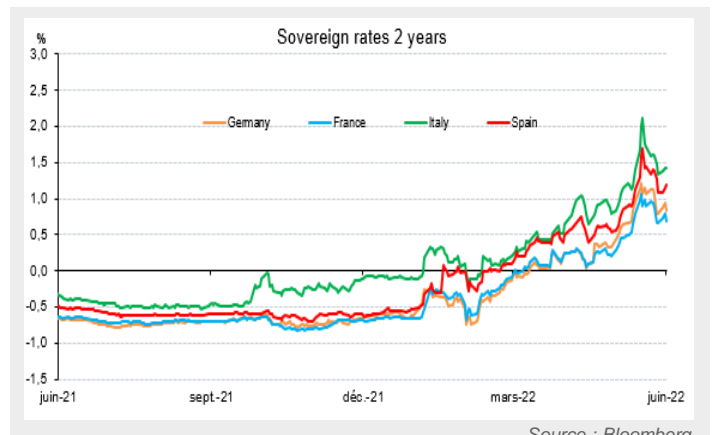
Christine Lagarde, President of the European Central Bank, June 28, 2022

Consequences on markets



2-year sovereign rates have continued to experience high volatility in recent days, but the "flight to quality" phenomenon in the bond markets has continued.

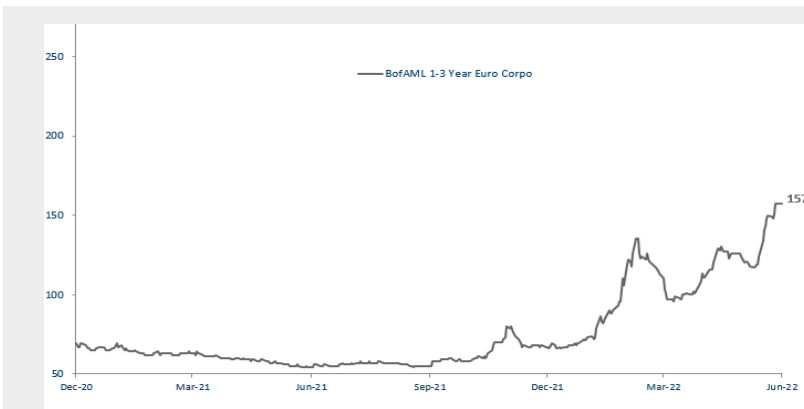
The German and Italian 2-year rates are respectively at 0.70% and 1.25%, down slightly from 0.79% and 1.37%



Source : Bloomberg

last week. However, they remain at high levels in anticipation of the ECB rate hike in July.

Spreads against Germany have stopped diverging and have slightly narrowed or stabilized (left graph)



Source : Bloomberg

In an uncertain environment, credit spreads have spread widely since May, with periods of calm.

The spread of the ICE BOFA Corporate 1-3 year index vs Govies is still high, and has stabilized at 157 bp for the last 4 days.



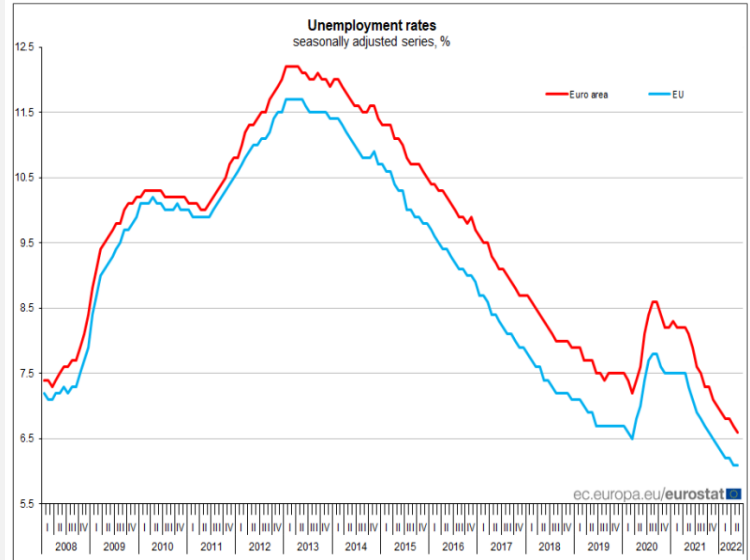
Euro zone: unemployment at its lowest

The unemployment rate in the Eurozone fell to 6.6%, a historic low in May (from 6.7% in April).

The Eurozone economy continues to rebound from the COVID-19 pandemic, however, runaway inflation exacerbated by Russia's invasion of Ukraine is expected to dampen this trend.

This is the lowest rate ever recorded since censuses began in 1998, just before the official launch of the euro in January 1999.

According to Eurostat, the number of unemployed people in the euro zone fell to 11.004 million from 11.085 million a month earlier.



Source : Eurostat

News



Sweden | The central bank raises its rate by 50 bp to 0.75%.

France | Household consumption up 0.7% in May

Agenda



5 July | Publication of the Eurozone PMI index

6 July | Publication of the US PMI index

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