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Economic Outlook and Credit Strategy

Speaker Name

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The global economic outlook in brief

- **Outlook 2024-25:** the most recent data have been better than expected, particularly in the Eurozone, where the cycle is likely past its worst; we expect a second half better than the first one and a rebound in 2025.
- **International trade flows** weak but **starting to recover**.
- **Inflation:** slightly declining around the 2% threshold, with some risks in the USA; **core inflation**, currently still above CB targets, will decrease gradually. **Key risks:** (1) supply-side shocks in energy markets related to escalation of conflicts; (2) stronger-than-expected ULC dynamics due to still tight labor markets; (3) accommodative fiscal policy in the US. More risks in the US than in the euro area.
- **The ECB is going to begin a phase of monetary policy easing in June.** The Fed is likely to postpone it to September/December.

GDP growth up to 2026

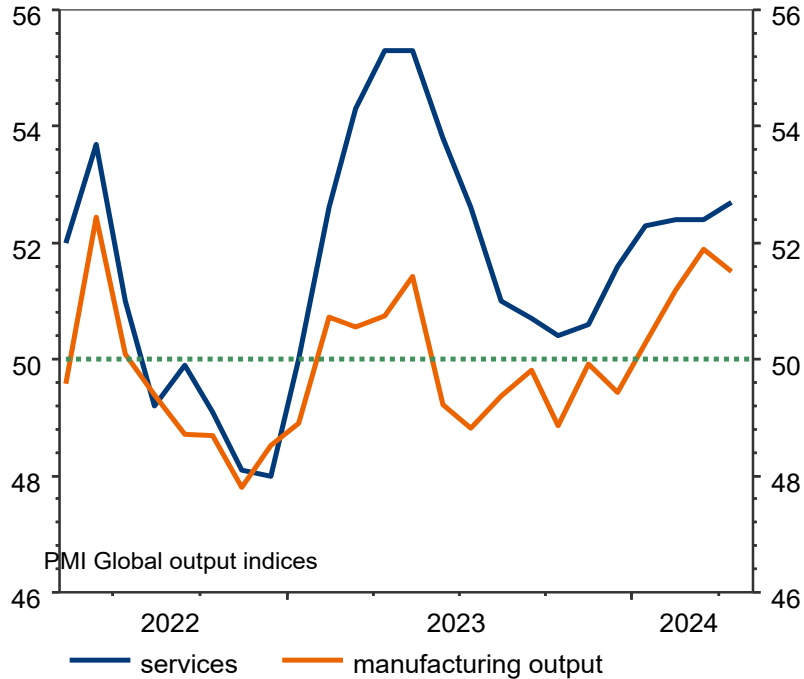
Full year GDP growth (constant prices)

	2022	2023	2024f	2025f	2026f
United States	1.9	2.5	2.3	1.8	2.1
Euro Area	3.5	0.5	0.6	1.3	1.4
Germany	1.9	0.0	0.2	1.1	1.4
France	2.5	0.9	0.9	1.4	1.4
Italy	4.1	1.0	0.7	1.2	1.0
Spain	5.8	2.5	2.1	1.8	1.7
OPEC	5.6	2.1	3.1	3.4	2.8
Eastern Europe	-4.4	3.8	2.1	2.0	1.8
Latin America	4.1	2.3	1.4	2.6	2.7
Japan	0.9	1.9	0.4	1.3	1.1
China	3.0	5.2	4.7	4.9	4.6
India	6.5	7.7	6.1	6.8	6.6
World	3.3	3.2	2.9	3.4	3.4

Note: PPP aggregate in constant dollars for OPEC, Eastern Europe, Latin America, World.
Change in GDP at constant prices in local currency in the other cases.
Source: Intesa Sanpaolo forecasts - Macroeconomic analysis

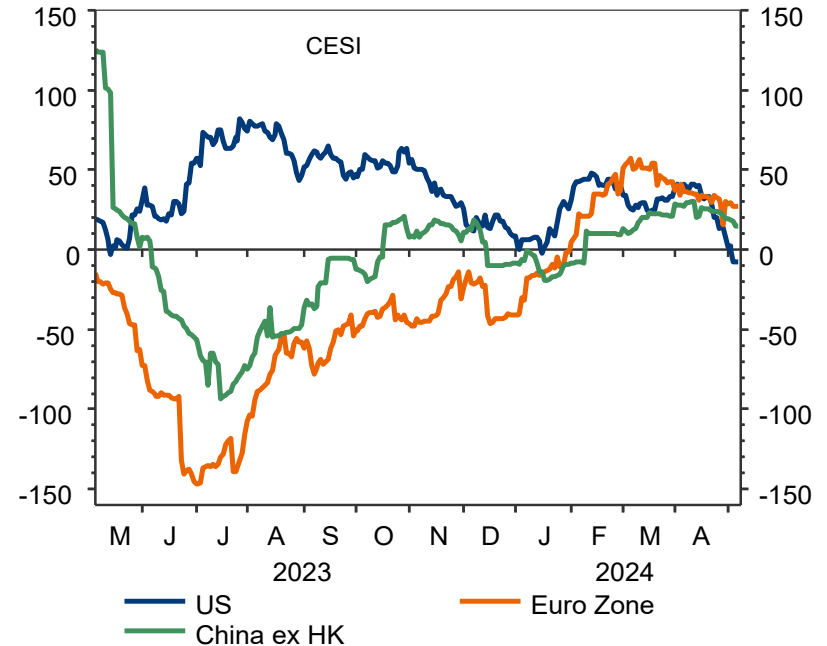
First signs of recovery in global economic activity

Global PMIs are improving



Source: S&P Global

Better than expected economic data, slowing down in the US more recently

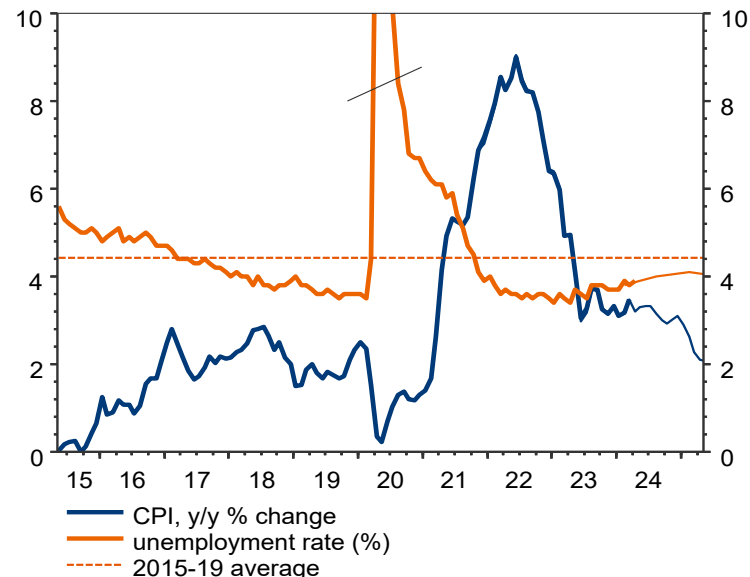
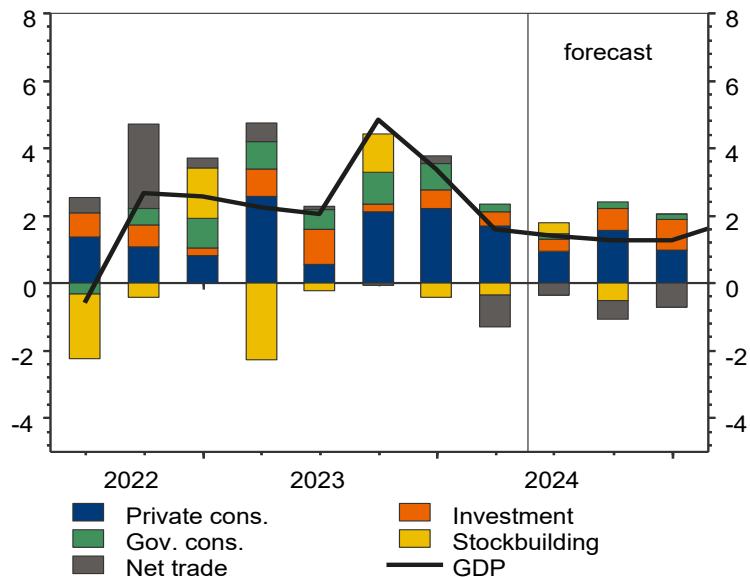


Source: LSEG Datastream

US 'soft landing', with a slight rise in unemployment

Mild slowdown in growth because of higher interest rate effects on domestic demand...

...with only a slight increase in the unemployment rate

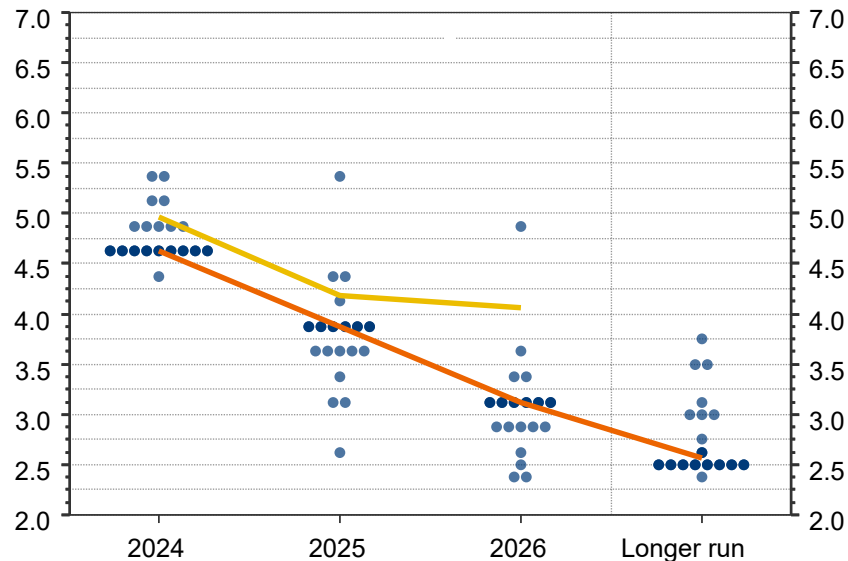


Source: BEA and Intesa Sanpaolo forecasts

Source: BLS and Intesa Sanpaolo forecasts

FOMC: no rush to cut rates

Dot plot at the March FOMC



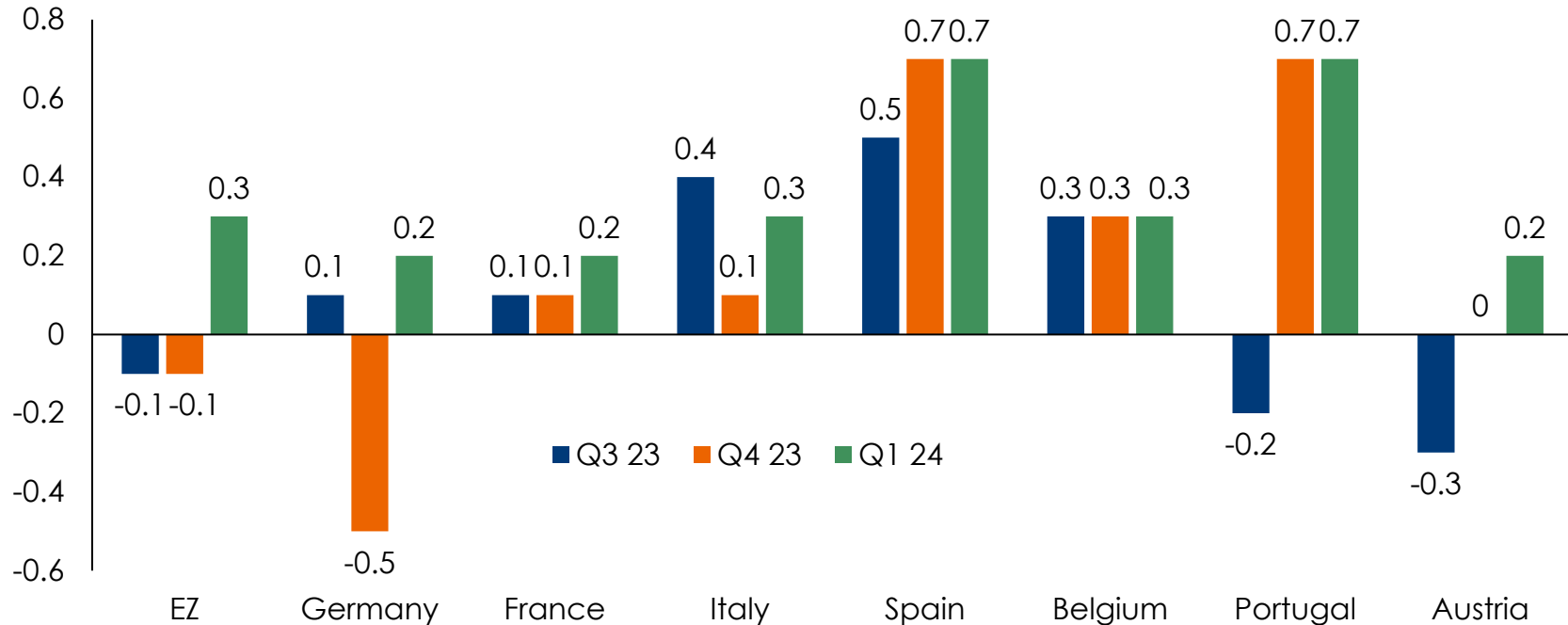
- FOMC participants' fed funds target, March 2024
- Median, March 2024
- Fed Funds Futures 5/7/2024

Source: Intesa Sanpaolo, Federal Reserve Board, Refinitiv-Datastream

- In May FOMC, **Powell did not mention plans to start cutting rates 'at some point this year'** as he did in the last two meetings.
- He also admitted that gaining greater confidence that inflation is moving sustainably toward 2% may take longer time than previously expected.
- We believe the new June projections will keep rate cuts on the table for this year.
- **We expect one/two cuts, in September and/or December.**

Eurozone: a stronger than expected Q1

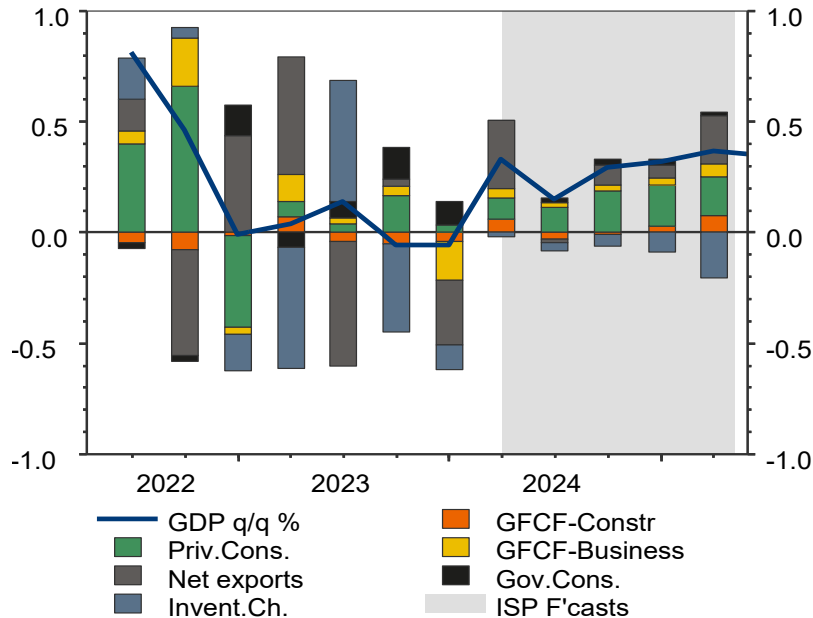
After a mild technical recession in H2 2023, the euro area economy resumed growing in Q1 2024 with positive cross-country prints (Real GDP % q/q)



Source: Intesa Sanpaolo, Eurostat

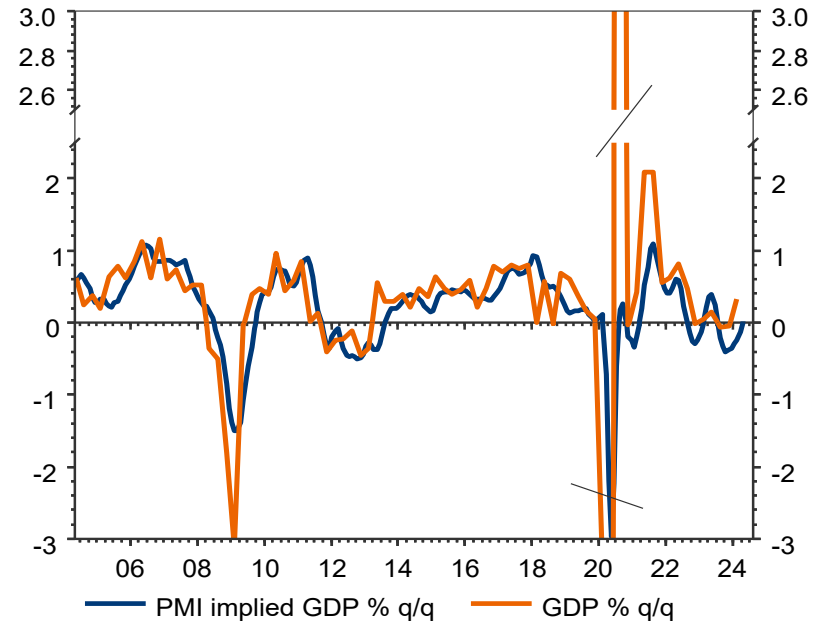
The cycle is likely over the worst of it

The surprise in Q1 could be due to a temporary payback of net exports and construction investment. A reacceleration expected in H2



Source: Intesa Sanpaolo forecasts, Eurostat

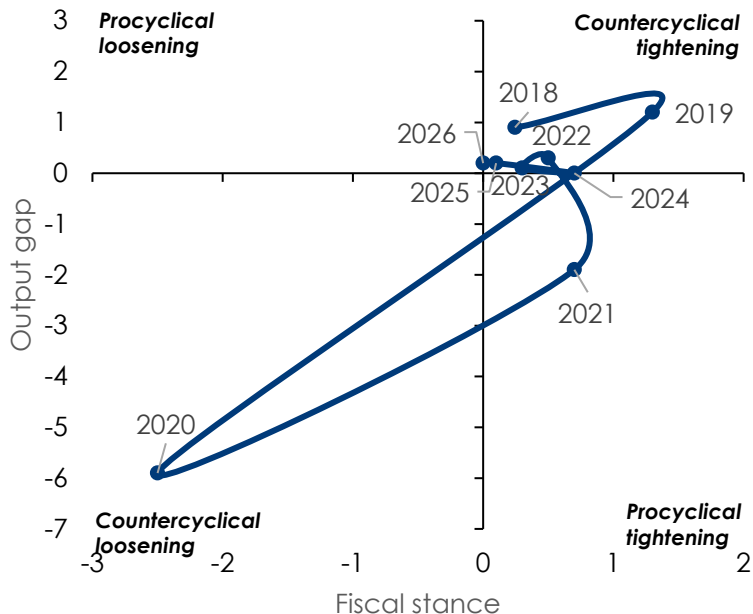
Confidence surveys suggest that the cycle is bottoming out and exiting the recession zone



Source: Intesa Sanpaolo, Eurostat, S&P Global

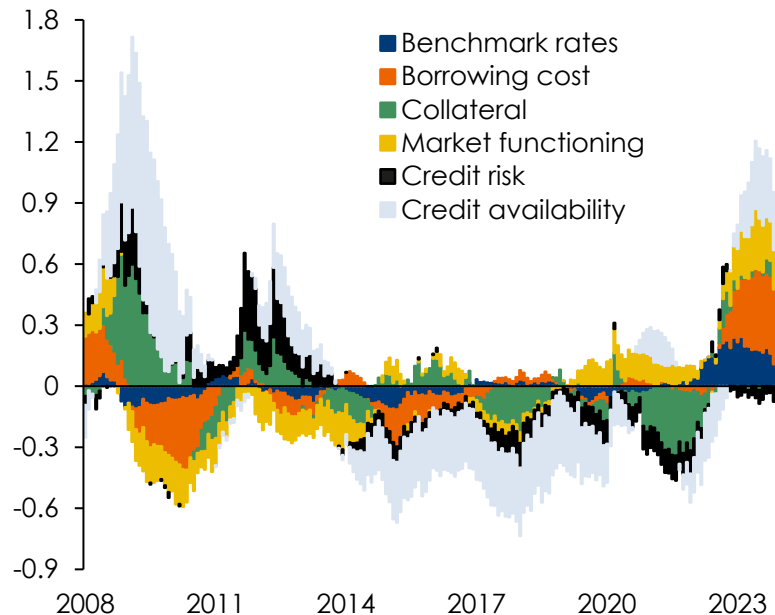
Slightly restrictive fiscal policy, tight financial conditions

After being loosened aggressively during the pandemic, fiscal policy will be tightened in the coming years



Note: fiscal stance measured as the change in the cyclically adjusted primary balance adjusted for expected NGEU grants. Source: Intesa Sanpaolo, ECB

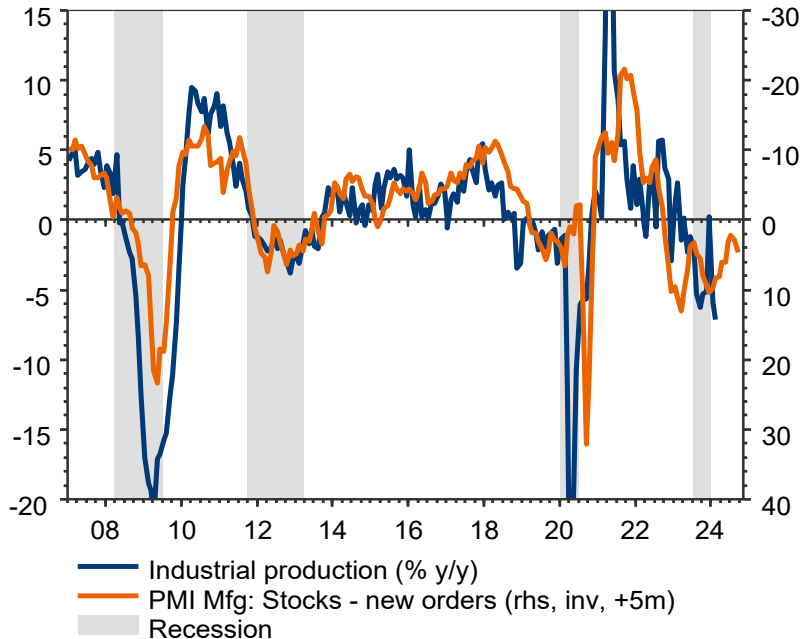
Our proprietary index shows that financial conditions are easing but still tight



Note: a positive figure implies a tightening of financial conditions. Source: Intesa Sanpaolo

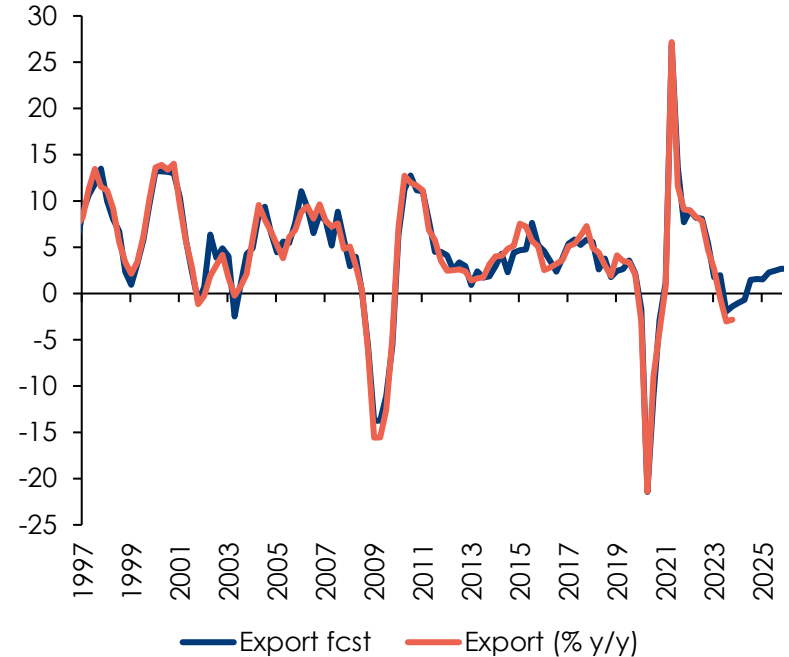
Manufacturing unlikely to reaccelerate anytime soon

The manufacturing still in negative territory, but the inventory cycle may provide some support to industrial production from mid-2024



Source: Intesa Sanpaolo, Eurostat, S&P Global

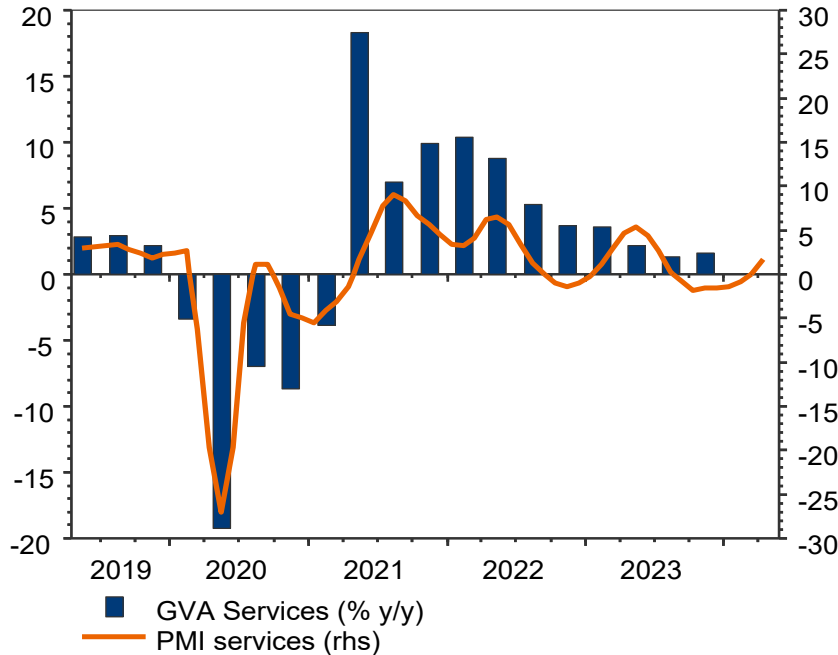
Export flows may have hit a low point but a material reacceleration is unlikely to materialise anytime soon



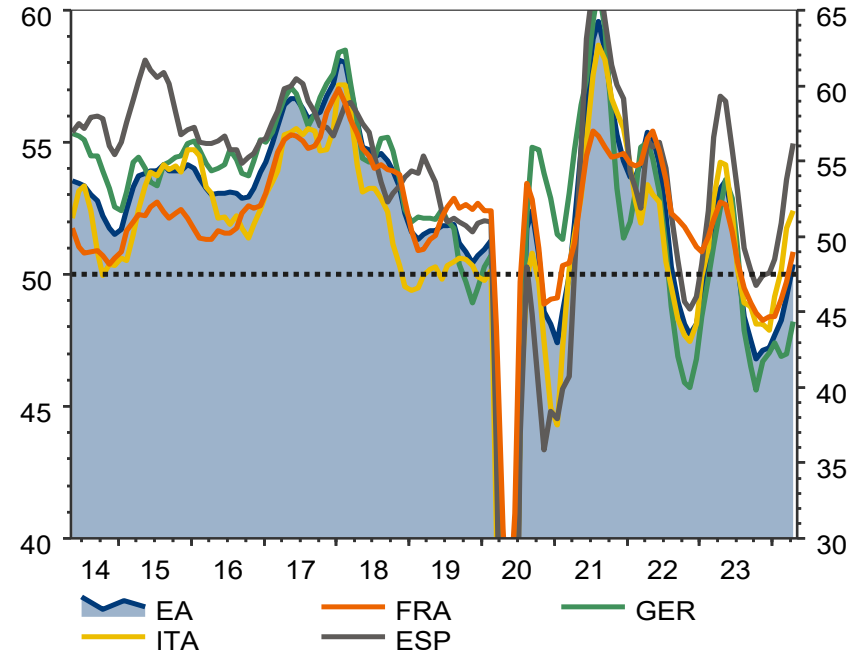
Source: Intesa Sanpaolo forecasts, Eurostat data

Services gaining momentum and driving the recovery

The service sector activity is improving ...



...driving the recovery of composite PMIs

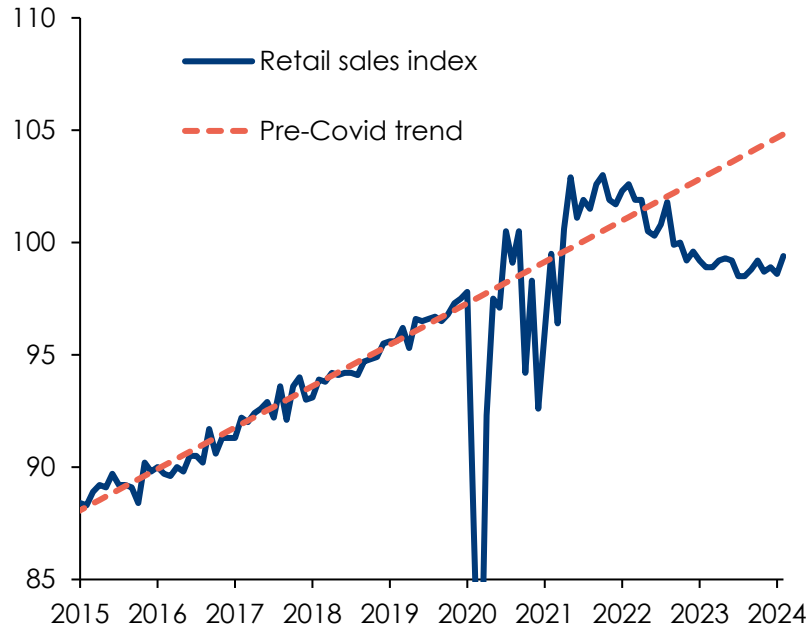


Note: 3-month moving averages.
Source: Intesa Sanpaolo, S&P Global

Source: Intesa Sanpaolo, Eurostat, S&P Global

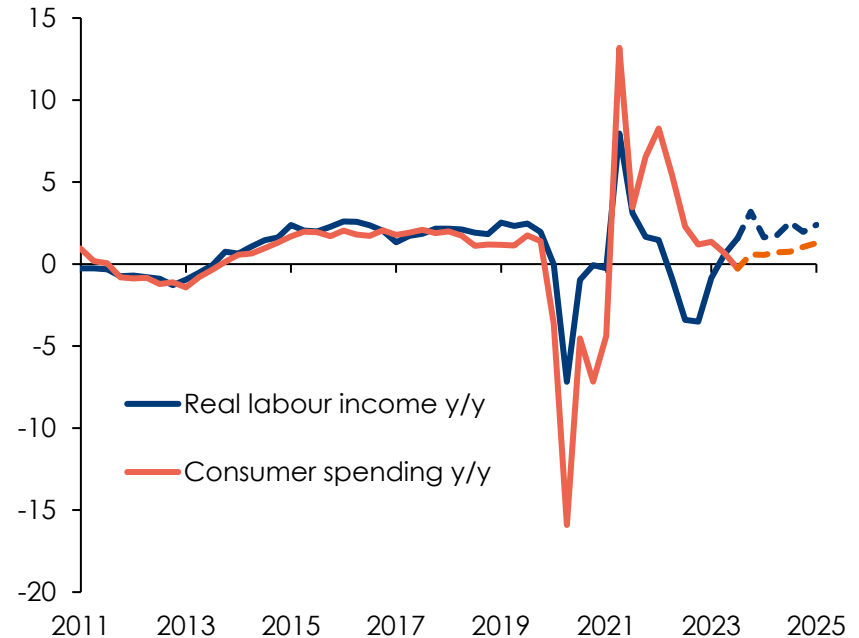
Easing inflationary pressures and a robust labor market will support domestic demand

Retail spending still below trend but has probably stabilised



Source: Intesa Sanpaolo, Eurostat

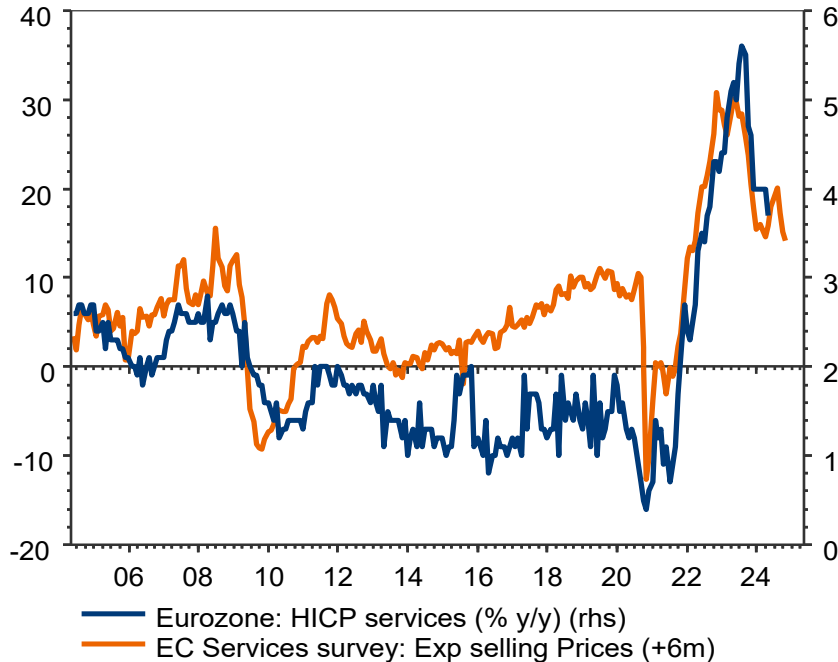
The recovery of purchasing power will underpin consumption growth



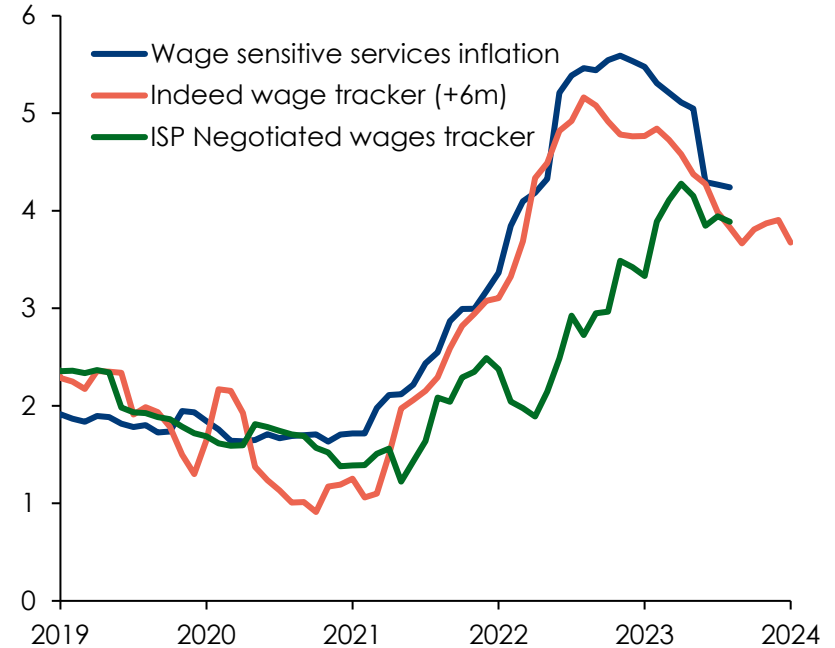
Source: Intesa Sanpaolo forecasts, Eurostat

Services inflation: sticky but not overheating

Price expectations in services still a high levels



Wage data: encouraging signs for labor intensive services inflation in the months ahead

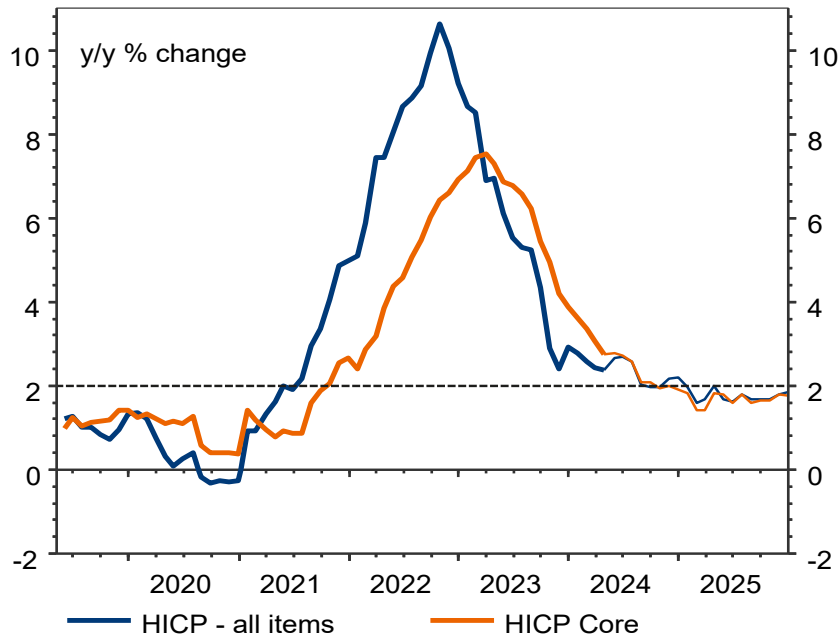


Source: Intesa Sanpaolo, Eurostat, EU Commission DG Ecofin

Source: Intesa Sanpaolo, ECB, Eurostat, Indeed

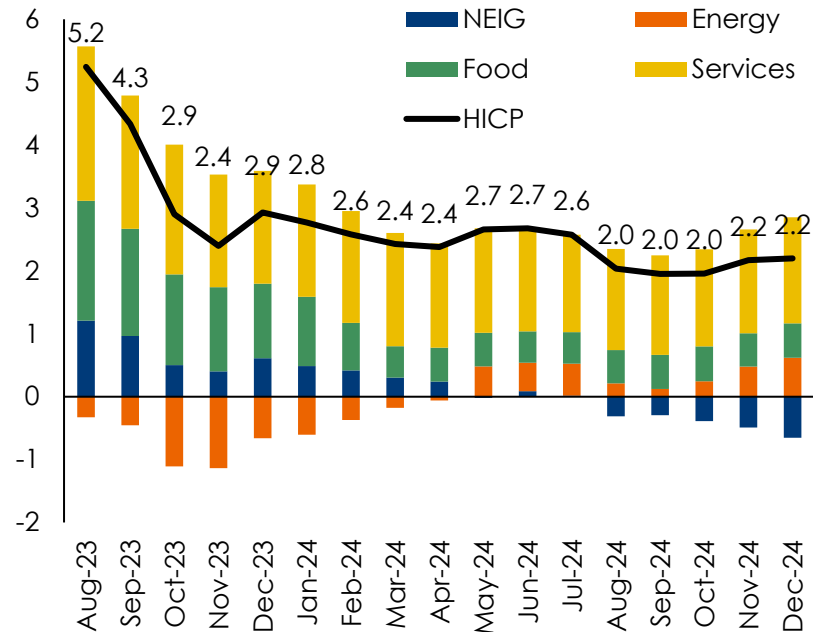
Inflation: the return to 2% is closer

Inflation expected to fall below 2% in 2025



Source: Intesa Sanpaolo forecasts, Eurostat data

Services: the main driver of inflation; energy back to positive territory

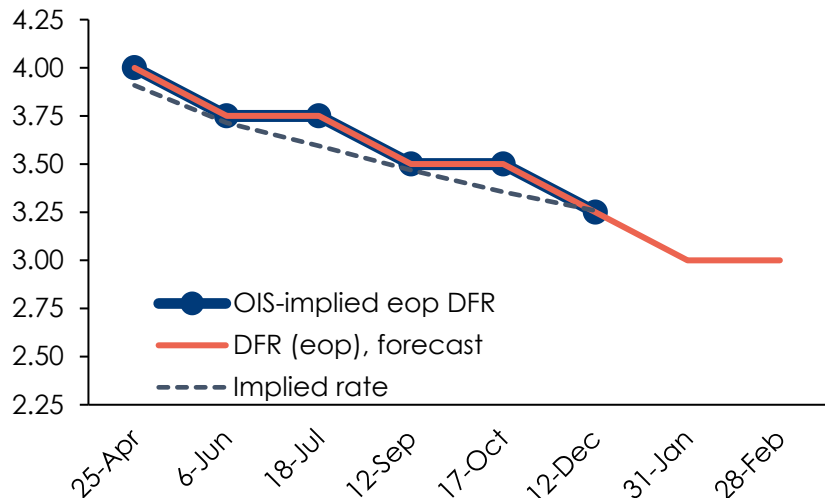


Source: Intesa Sanpaolo forecasts, Eurostat data

ECB: first cut expected on June 6th

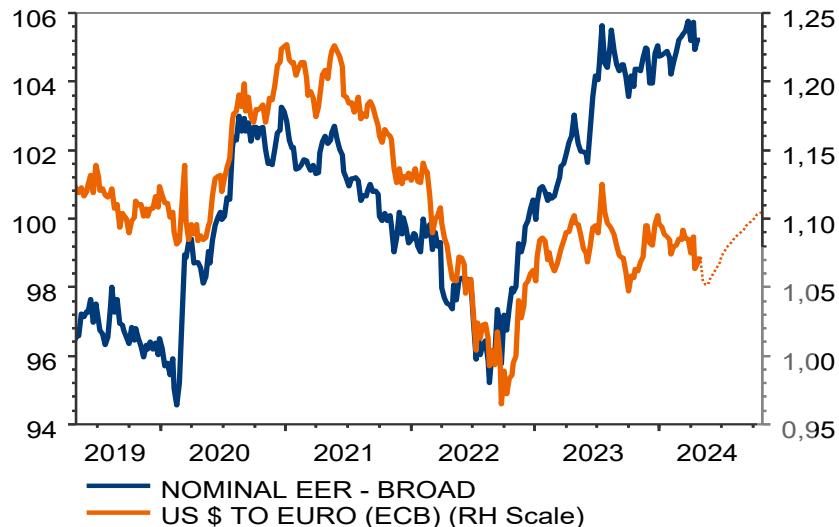
The cut cycle should start in June, boosted by a higher-than-expected drop in **inflation**, **wage moderation** and **low growth**. Two or three consecutive cuts before a pause, instead of single cuts interspersed with pauses (which is the central scenario).

Clear downgrading of the market's ECB cut expectations, now at 75bp by end 2024



Note: The implied DFR is estimated assuming an unchanged ESTR spread, rounding to the nearest 25 bp. Source: Intesa Sanpaolo, LSEG

Euro weak against dollar, but strengthening as effective average exchange rate

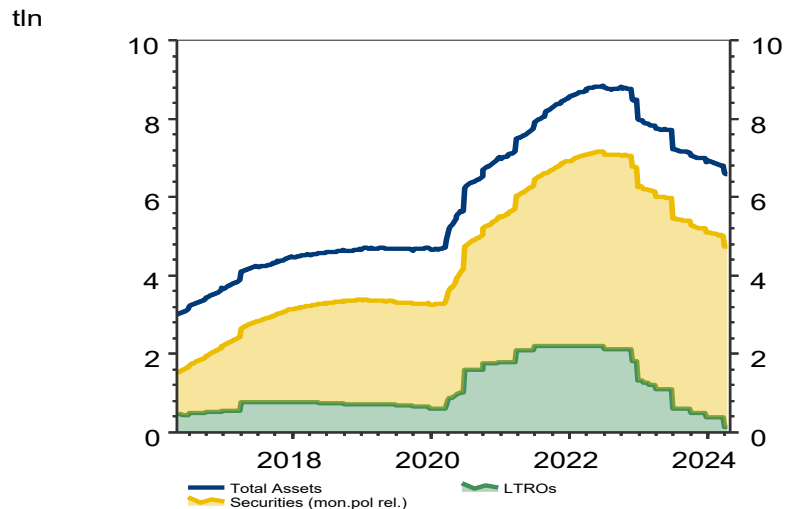


Source: LSEG Datastream, ECB and Intesa Sanpaolo forecasts.

Drainage of excess reserves will continue

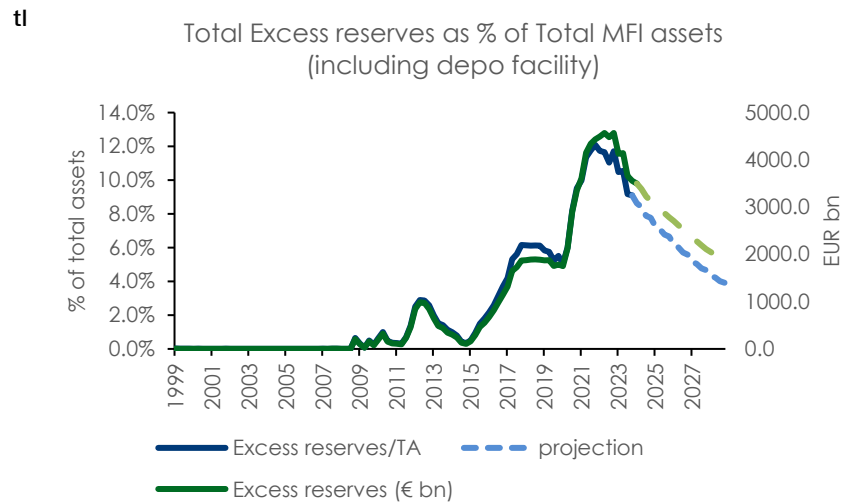
The ECB stopped reinvesting the APP portfolio from July 2023. The **QT will be extended to the PEPP portfolio from July 2024 (-7.5 billion per month)**. PEPP reinvestments will be completely eliminated from the end of 2024. The reduction of excess reserves has not yet translated into increased demand for the regular refinancing operations.

With the repayment of the TLTROs, the ECB's assets consist mainly of securities



Source: Intesa Sanpaolo elaborations on ECB data

The drainage of excess liquidity has so far proved to be fast and trouble-free



Source: ECB and Intesa Sanpaolo projections

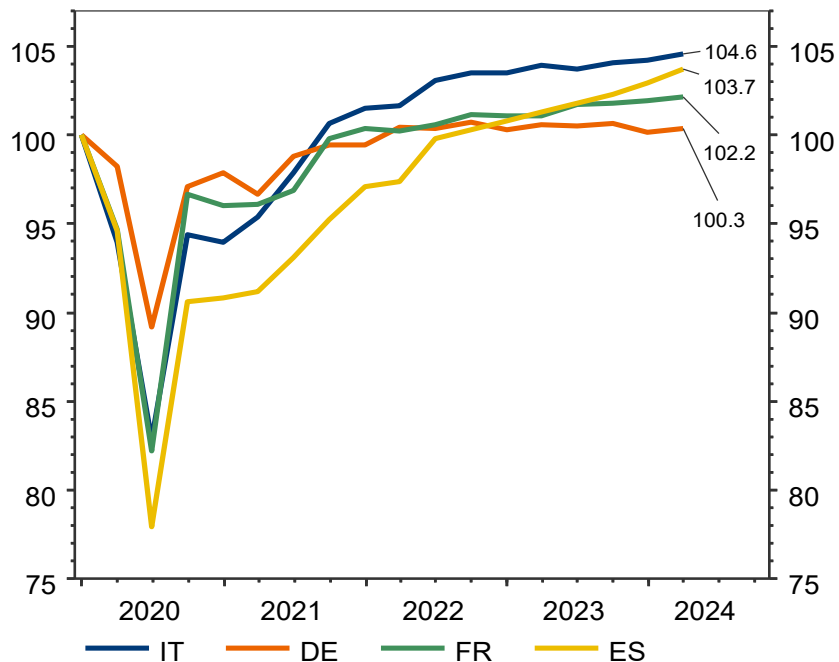
Eurozone: summary of forecasts

	2023	2024f	2025f	2023	2023	2023	2023	2024	2024	2024	2024	2025	2025
				1	2	3	4	1	2	3	4	1	2
GDP (constant prices, y/y)	0.5	0.6	1.3	1.3	0.6	0.1	0.1	0.4	0.4	0.7	1.1	1.1	1.3
- q/q change				0.0	0.1	-0.1	-0.1	0.3	0.2	0.3	0.3	0.4	0.3
Private consumption	0.6	0.8	1.3	0.1	0.1	0.3	0.1	0.2	0.2	0.4	0.4	0.3	0.3
Fixed investment	1.4	1.0	2.4	0.3	0.2	0.0	1.0	-0.2	0.3	0.2	0.7	0.8	0.6
Government consumption	0.8	1.0	0.4	-0.3	0.3	0.7	0.5	0.0	0.1	0.1	0.1	0.1	0.1
Export	-1.0	0.7	3.0	-0.5	-1.1	-1.2	0.0	0.9	0.3	0.6	0.5	0.9	0.9
Import	-1.4	0.8	2.0	-1.6	-0.1	-1.4	0.6	0.4	0.4	0.5	0.5	0.5	0.5
Stockbuilding (% contr. to GDP)	-0.4	-0.2	-0.6	-0.5	0.6	-0.4	-0.1	0.0	0.0	-0.1	-0.1	-0.2	-0.2
Current account (% of GDP)	1.5	1.8	2.2										
Deficit (% of GDP)	-3.6	-2.9	-2.4										
Debt (% of GDP)	88.6	89.7	89.5										
HICP (y/y)	5.4	2.4	1.8	8.0	6.2	5.0	2.7	2.6	2.6	2.2	2.1	1.8	1.8
Industrial production (y/y)	-2.2	-1.7	2.1	0.7	-0.8	-4.8	-3.9	-4.9	-2.2	-0.2	0.6	2.4	2.3
Unemployment (%)	6.6	6.6	6.4	6.6	6.5	6.6	6.5	6.5	6.6	6.6	6.6	6.5	6.4
3-month Euribor	3.43	3.68	2.61	2.63	3.36	3.78	3.96	3.92	3.82	3.63	3.33	2.87	2.51

Source: Intesa Sanpaolo forecasts

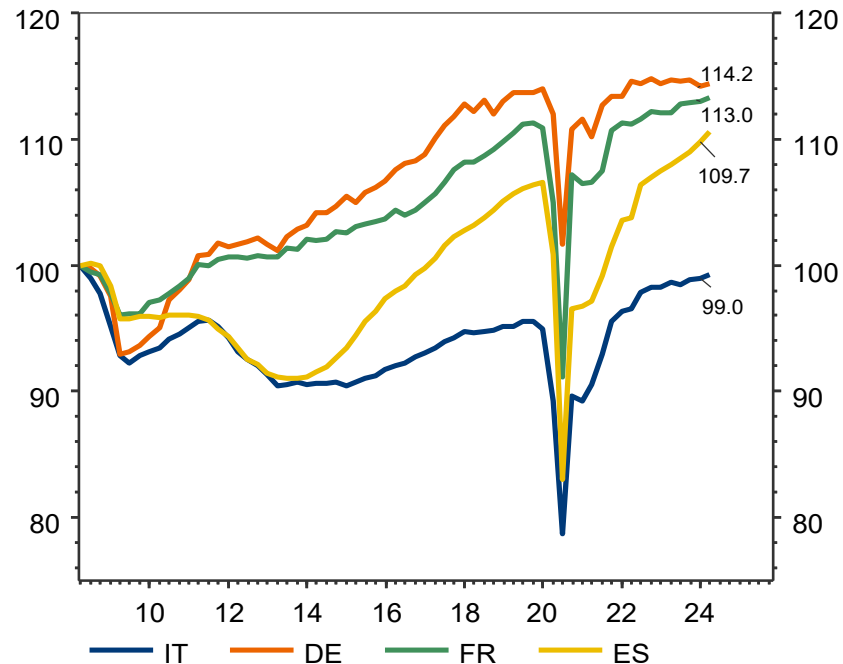
South Europe outperforming the North but further progress is needed to achieve convergence

GDP levels (2019 Q4 = 100)



Source: Intesa Sanpaolo, Eurostat

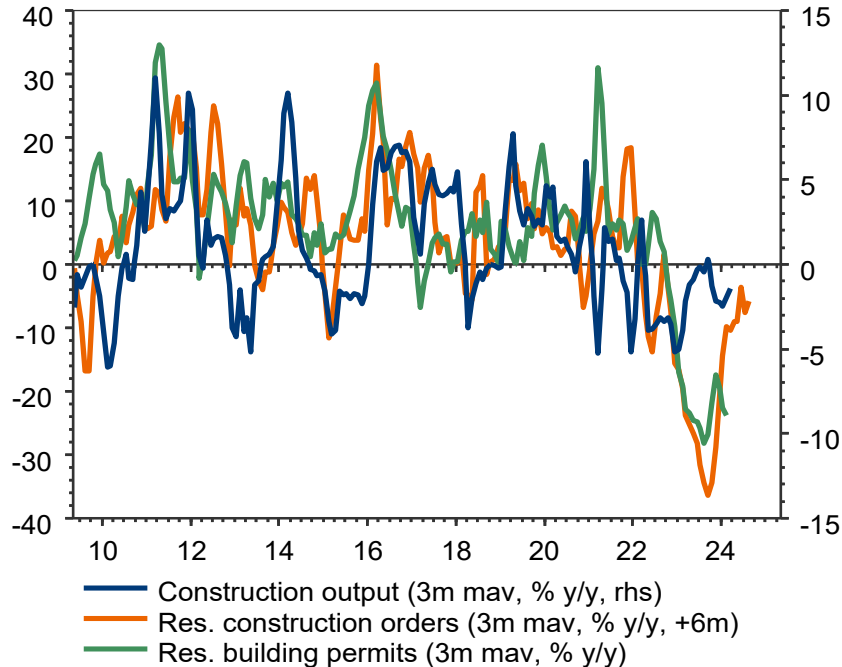
GDP levels (2008 Q1 = 100)



Source: Intesa Sanpaolo, Eurostat

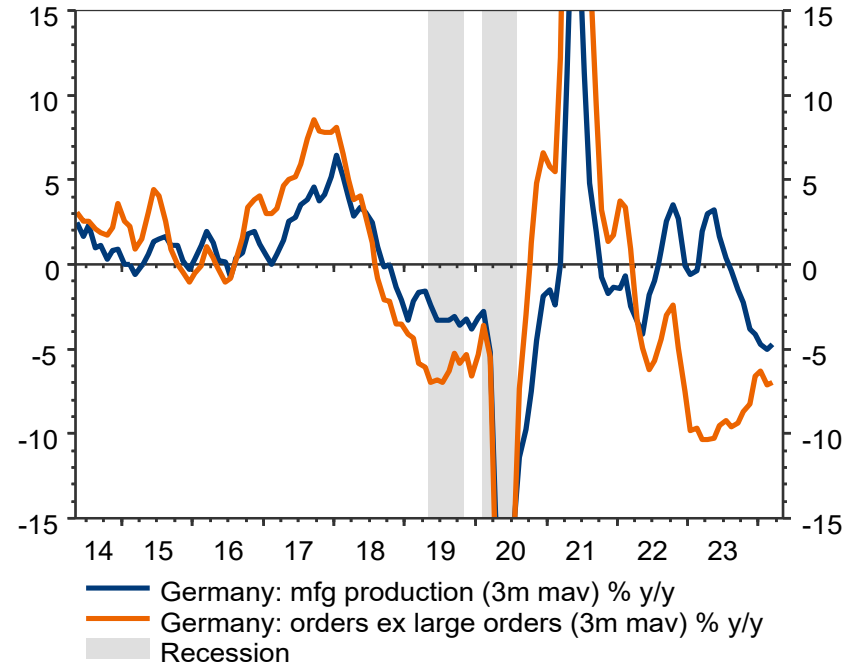
Germany: once again the sick man of Europe...

Mild weather conditions likely boosted construction in Q1, fundamentals remain weak



Source: Intesa Sanpaolo, Destatis, Deutsche Bundesbank

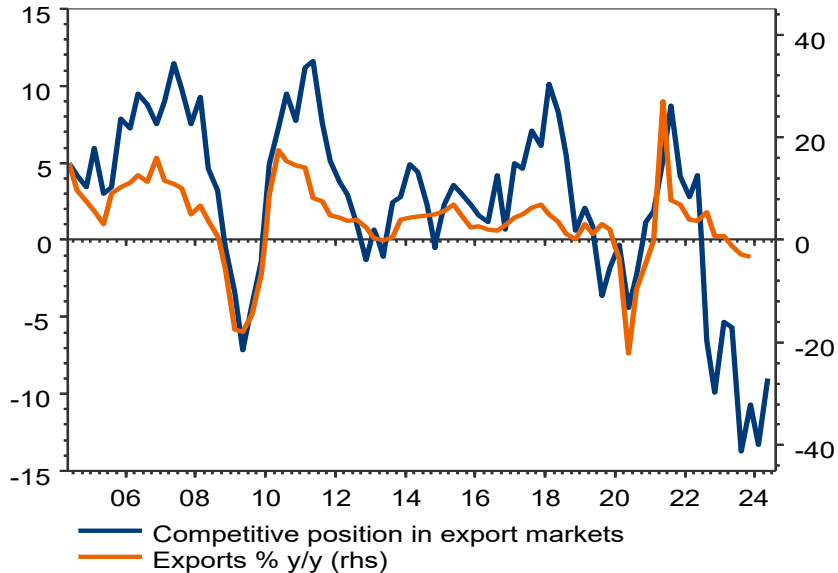
Factory orders on a downtrend, manufacturing reacceleration unlikely in the near term



Source: Intesa Sanpaolo, Destatis

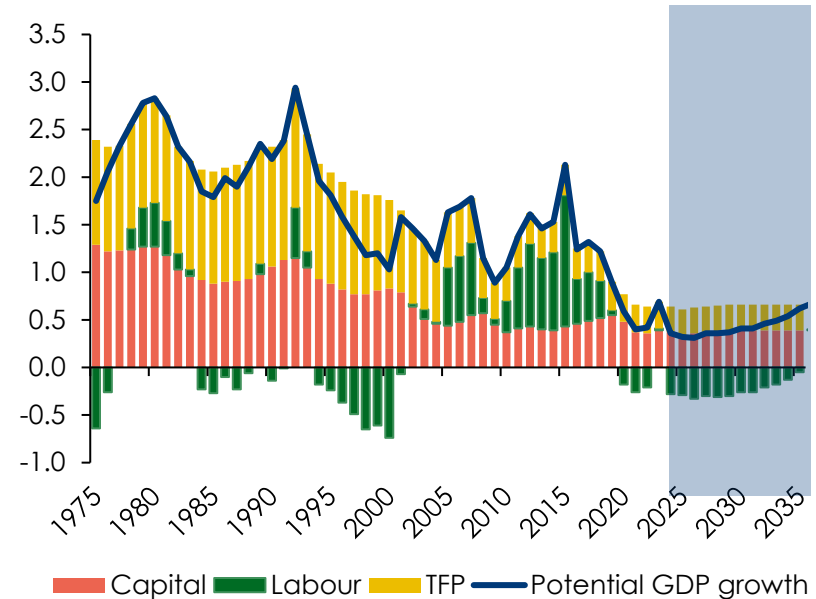
... facing structural challenges

Structural competitiveness issues may limit the recovery of German exports despite a more favourable cyclical backdrop



Source: Intesa Sanpaolo, Destatis, EU Commission DG Ecofin

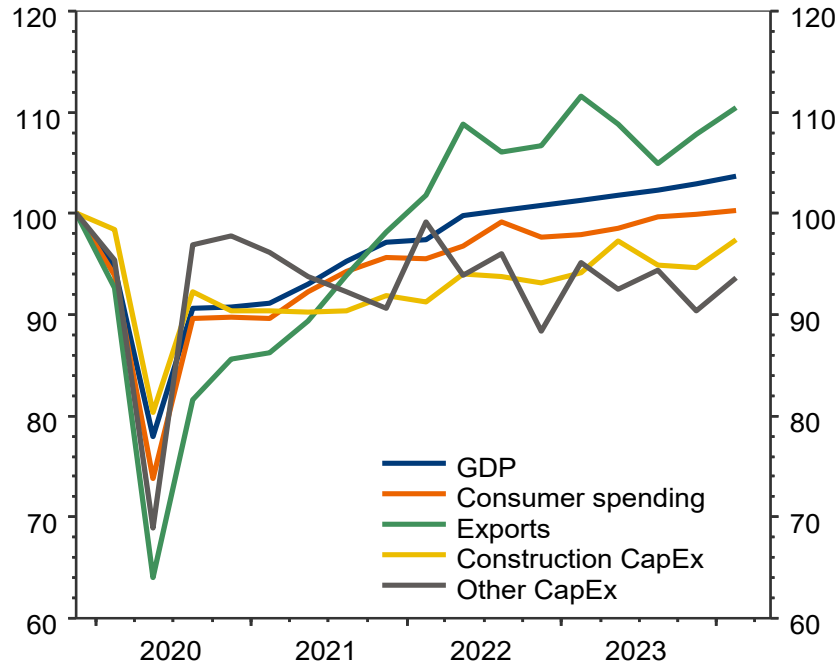
Potential GDP growth now stands at 0.4%, and, under favorable assumptions, will recover only moderately in coming years



Note: contributions to potential GDP growth. Source: Intesa Sanpaolo, German Council of Economic Experts

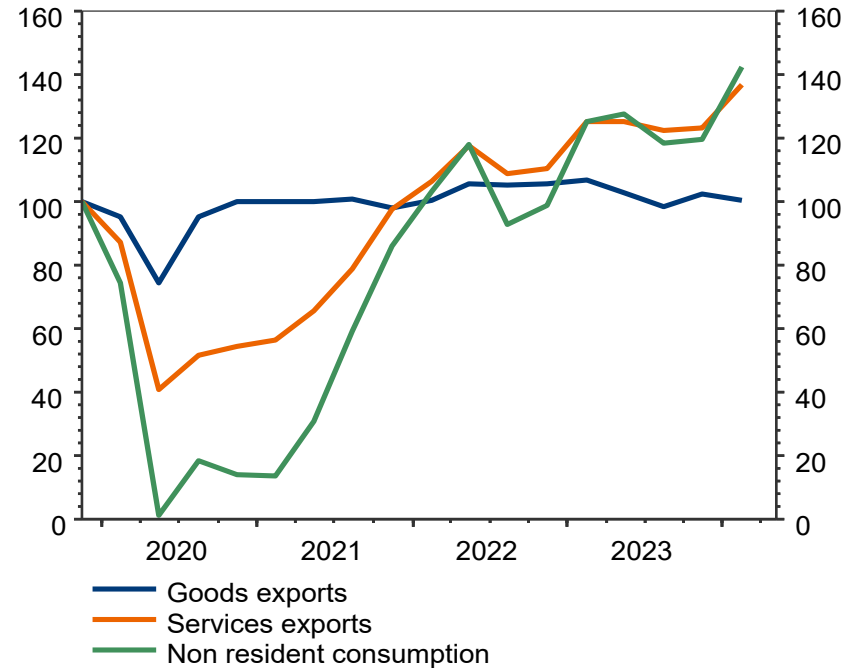
Spain: from laggard to leader

Real GDP by components
(2019 Q4 = 100)



Source: Intesa Sanpaolo, INE

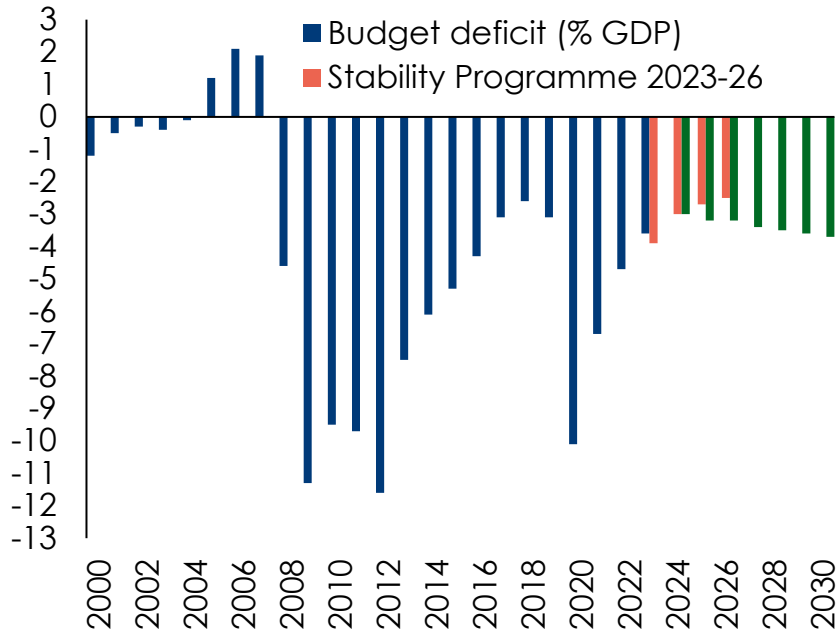
Tourism led the gains, exports of goods display less dynamism (2019 Q4 = 100)



Source: Intesa Sanpaolo, INE

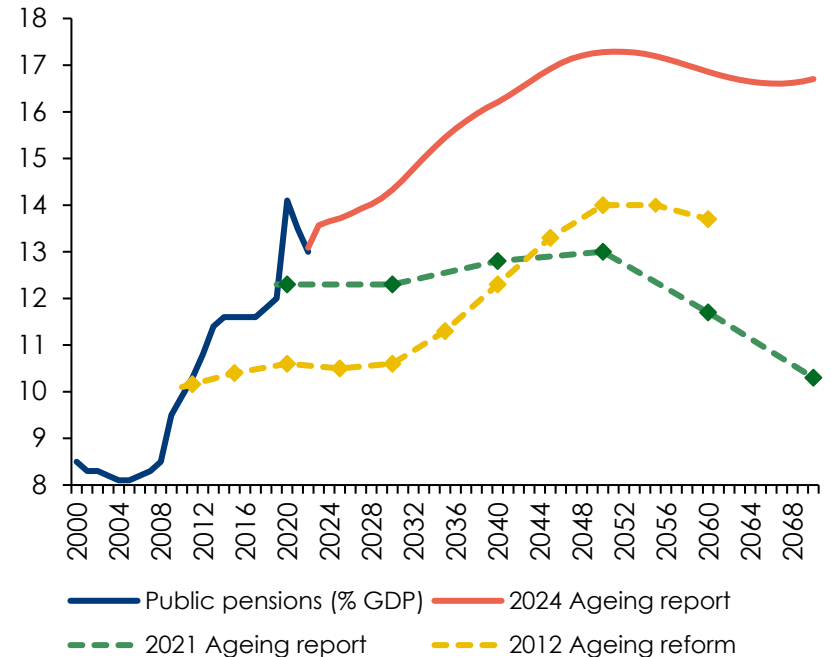
Political instability may delay fiscal consolidation

The 2023 budget will be rolled over in 2024, increasing the risk of fiscal policy inertia



Source: Intesa Sanpaolo, AIReF, Programa de Estabilidad 2023-26

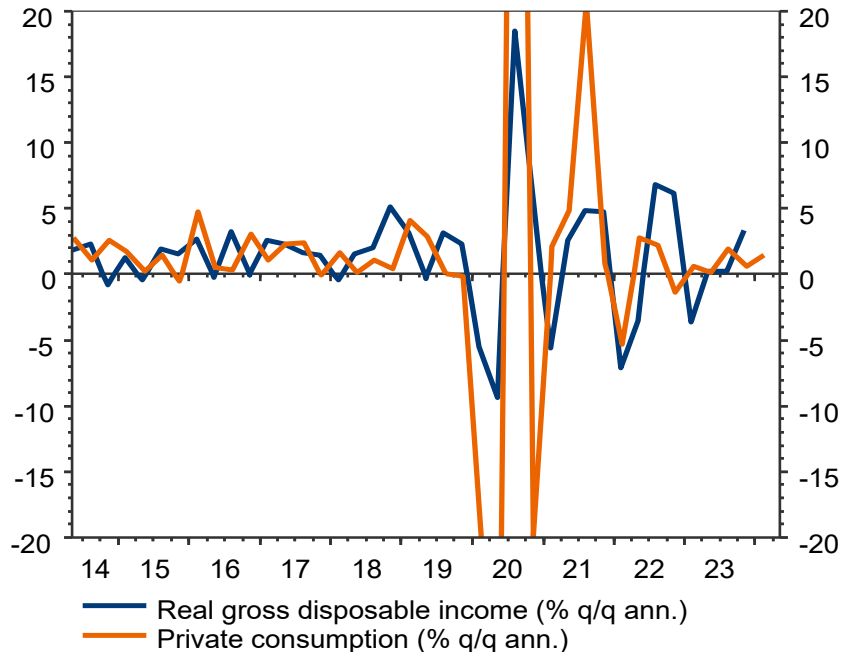
Pension spending will increase in the long-term as a result of a more generous reform



Note: for the Ageing reports 2012 and 2021 the available data points are marked, then interpolated to achieve the time series. Source: Intesa Sanpaolo, Eurostat, EU Commission

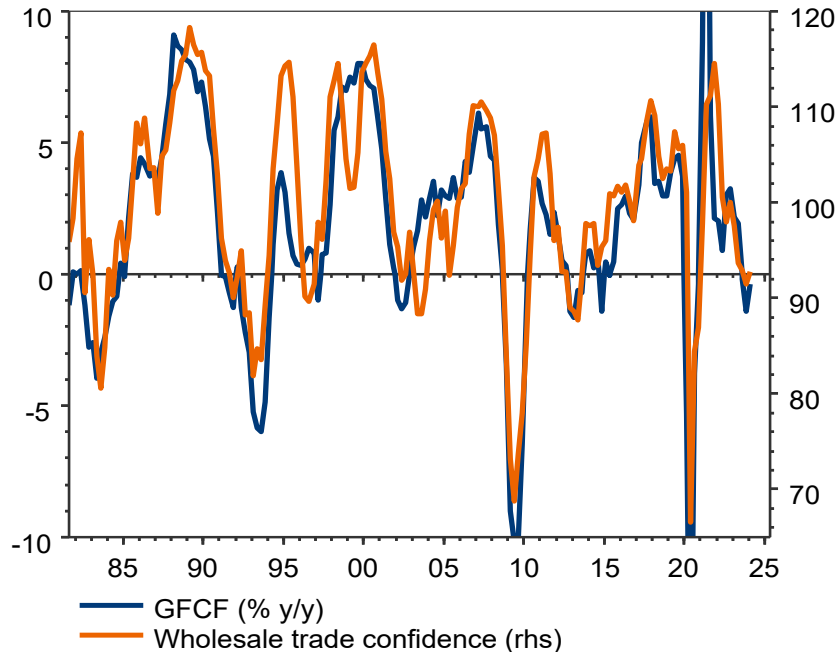
France: encouraging signs ahead

Disposable income is improving and will support spending in the months ahead



Source: Intesa Sanpaolo, INSEE

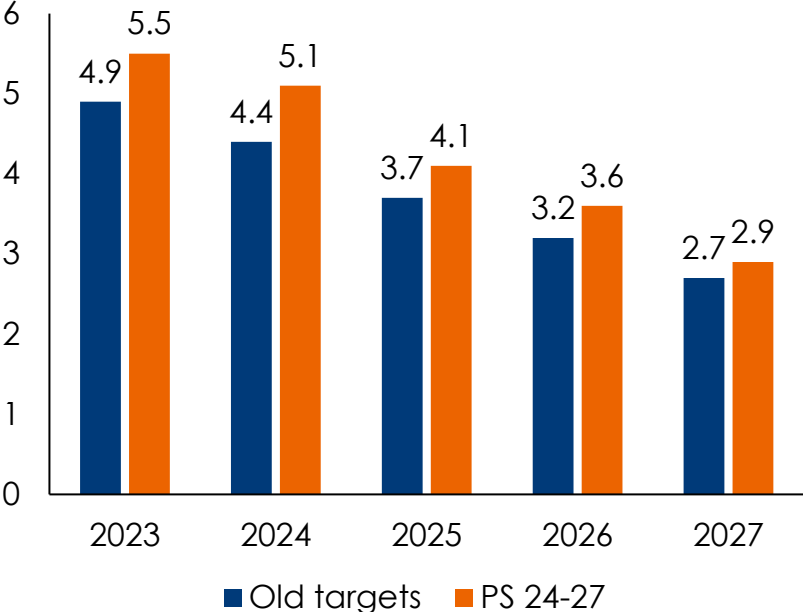
Investment at a turning point (but construction remains under pressure)



Source: Intesa Sanpaolo, INSEE

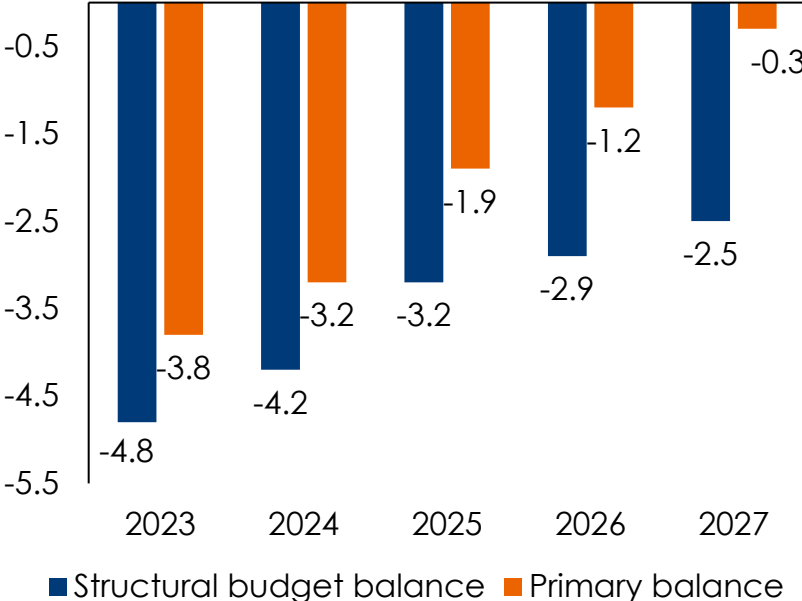
Worse than expected fiscal outcomes and highly ambitious targets

The Government missed its 2023 budget deficit forecasts and eased the targets for next years



Source: Intesa Sanpaolo, French Government

Targets remain optimistic and dependent on an ambitious spending review plan

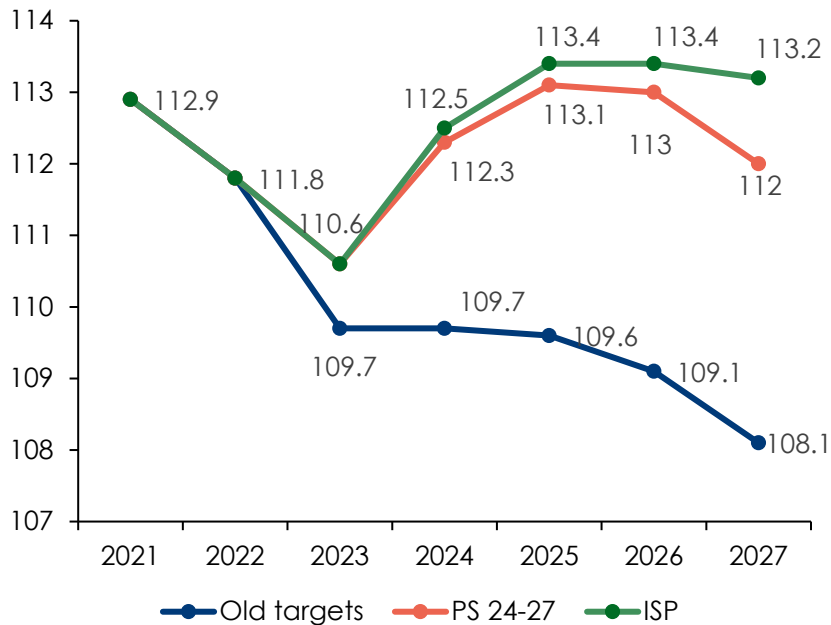


Source: Intesa Sanpaolo, Programme de Stabilité 2024-27

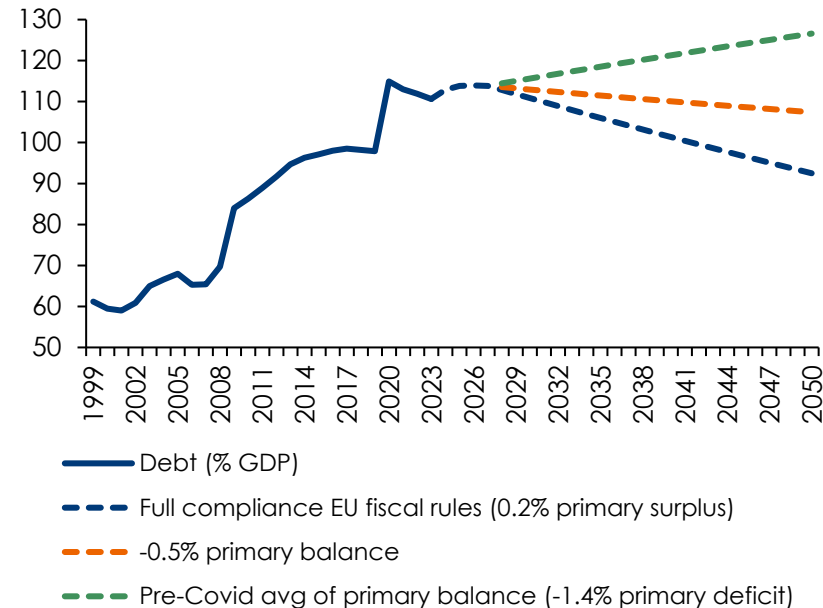


Rising risks to public finances

Public debt forecasts (% GDP)



In the long term a balanced primary budget may be required to achieve a debt downtrend and to be fully compliant with the new EU fiscal rules

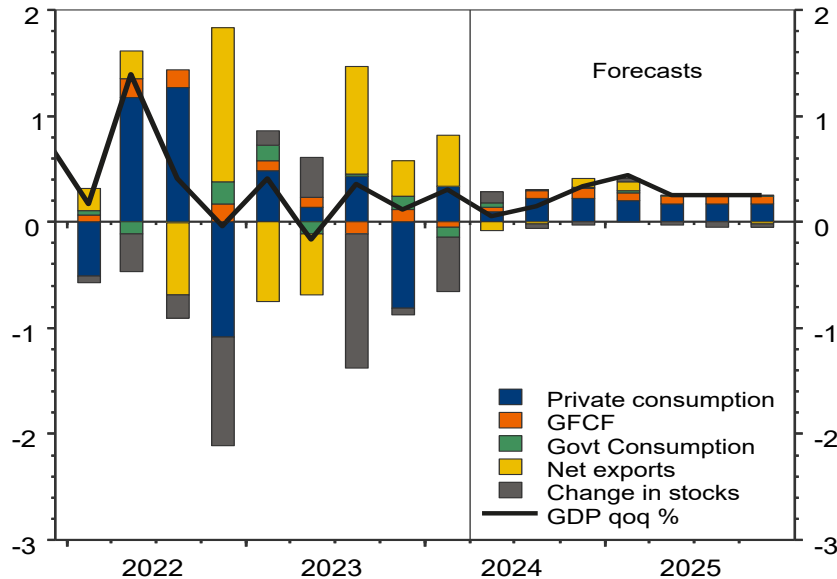


Source: Intesa Sanpaolo, French Government

Note: we assume nominal GDP growth to converge to 3.1% and the average cost of debt to 2.4%. Source: Intesa Sanpaolo simulations

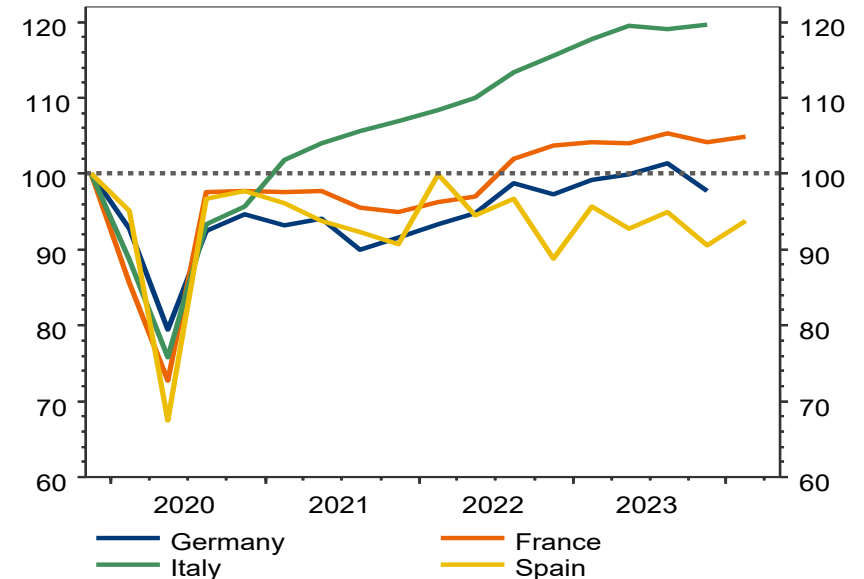
Italy: exports and investment in construction helped the economy stand out

GDP growth stronger than expected between late-23 and early-24, driven by net exports and construction investment



Source: Istat, Intesa Sanpaolo forecasts

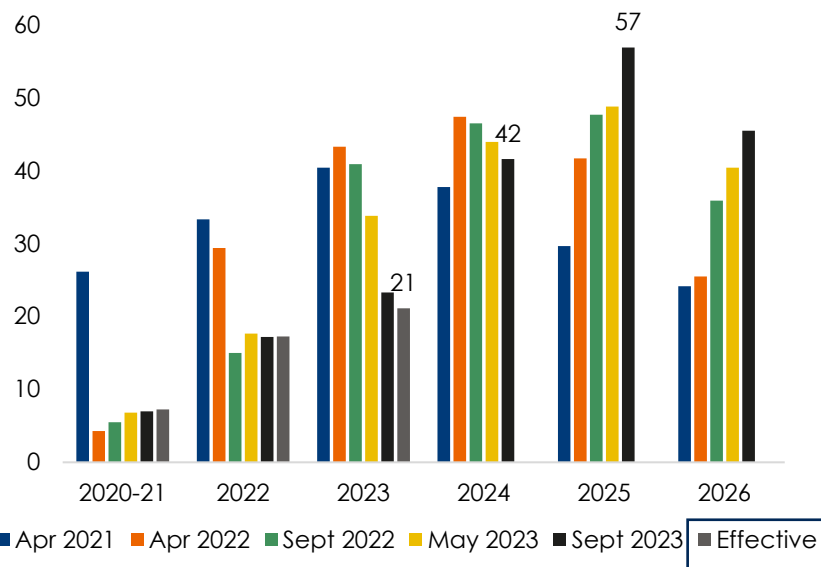
Investment growth (not only in construction) explained the post-pandemic outperformance



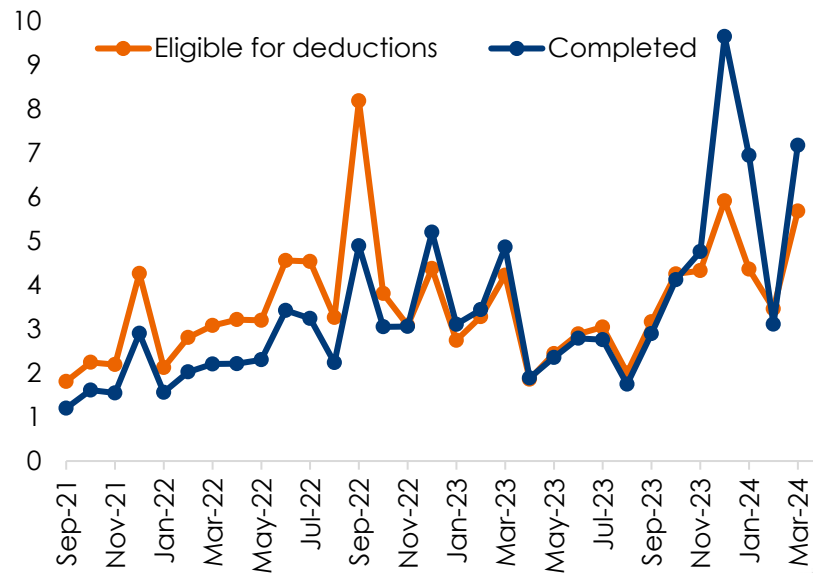
Note: gross fixed investments in machinery and equipment and weapons systems, Q4 2019=100.
Source: Intesa Sanpaolo, Eurostat

NGEU funds will provide additional support as the effects of construction bonuses fade

In 2023, actual expenditure financed by the NRRP amounted to EUR 21bn vs EUR 41bn expected by the Govt; a marked acceleration is needed



In Q1 2024, the flow of new investments eligible for Superbonus, and especially the completion of works, remained at a very high rate

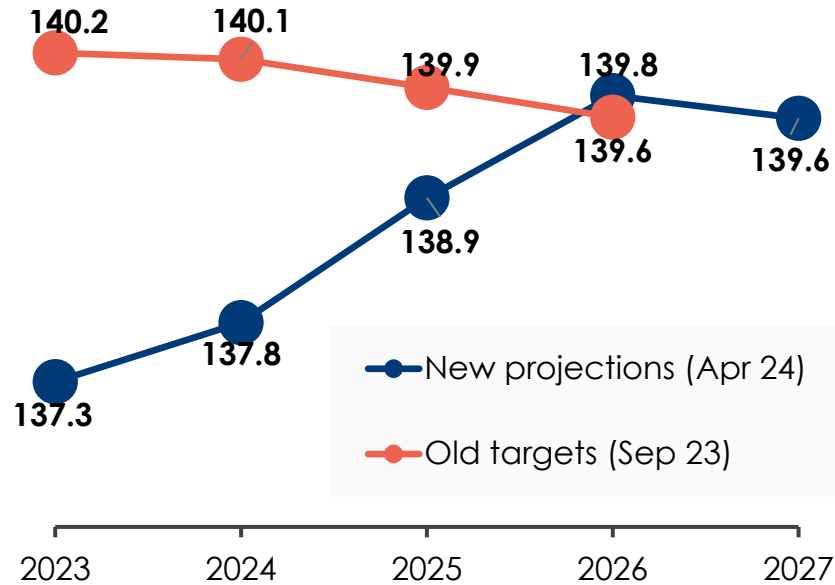


Source: Intesa Sanpaolo elaborations on Italian government estimates

Source: Intesa Sanpaolo, ENEA

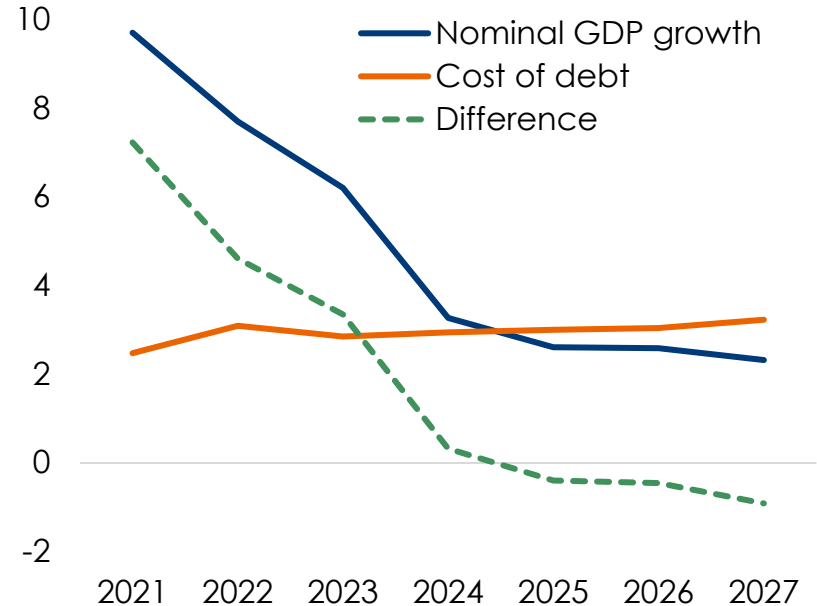
Debt to GDP ratio lower than expected, but it will rise again...

Debt (% of GDP): Govt scenarios



Source: Intesa Sanpaolo elaborations on Italian Government data

G-i is becoming less and less favourable

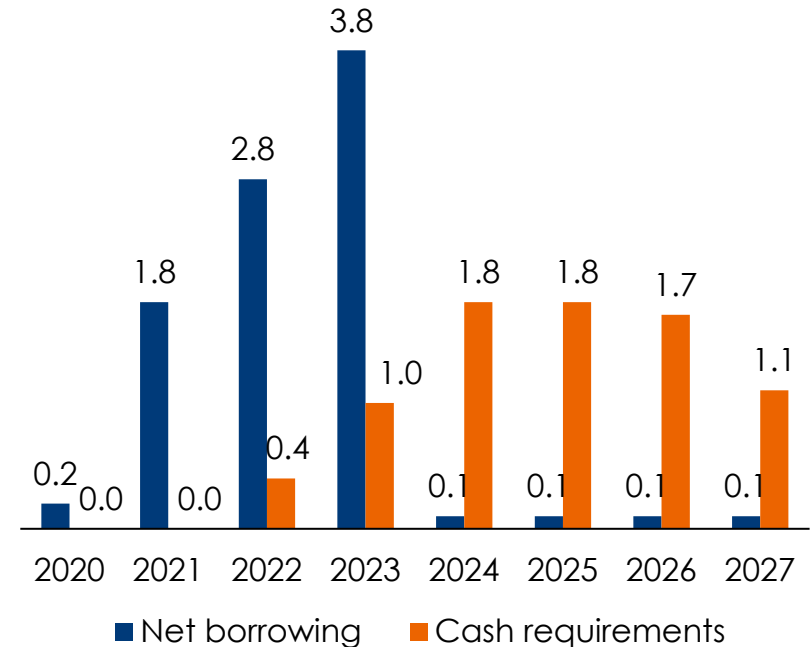
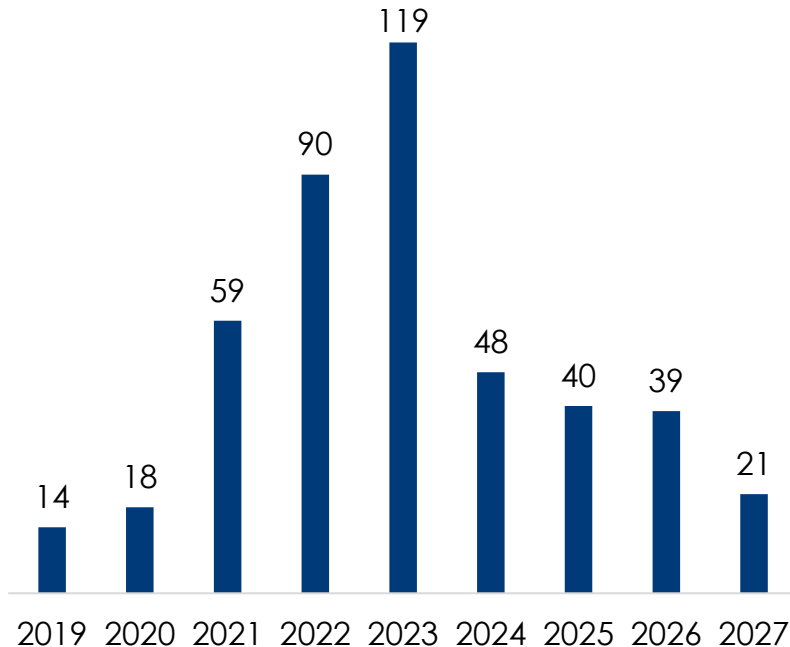


Source: Italian Government assumptions

...mainly due to the impact of building bonuses

Capital transfers (mainly due to building bonuses) hit a peak in 2023 and should gradually moderate...

...but the peak of the impact on cash borrowing requirements will be in 2024-26

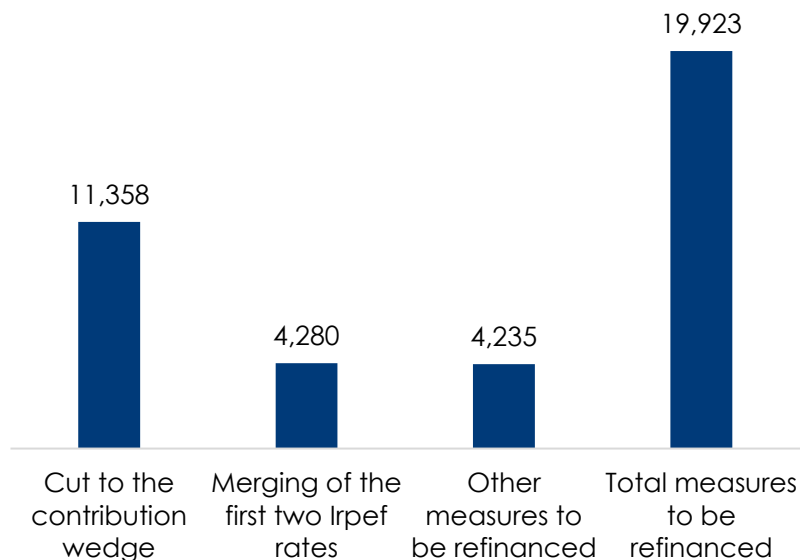


Note: EUR Bn. Source: Intesa Sanpaolo elaborations on Italian Government data

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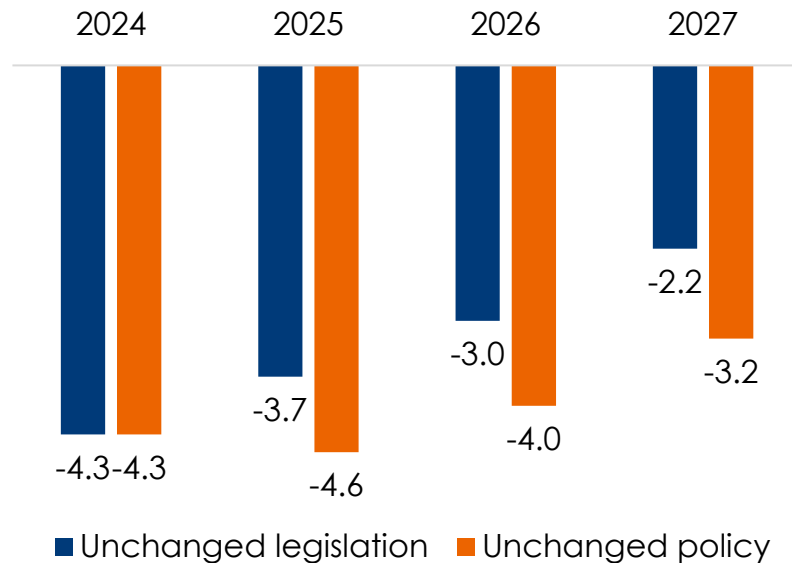
The main challenge will be to cover tax breaks expiring in 2025

The main challenge for the 2025 budget will be the need to refinance measures amounting to approximately 20 billion...



Note: millions of euro. Source: Intesa Sanpaolo elaborations on government data

...in the absence of which, in the Govt's estimates, net borrowing will rise next year, and remain elevated in 2026-27



Source: Italian Government

Important Information

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