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Special: H2 – How can the energy-transition bet pay off?

Analysts: Thomas Wybierek // Pascal Seidel

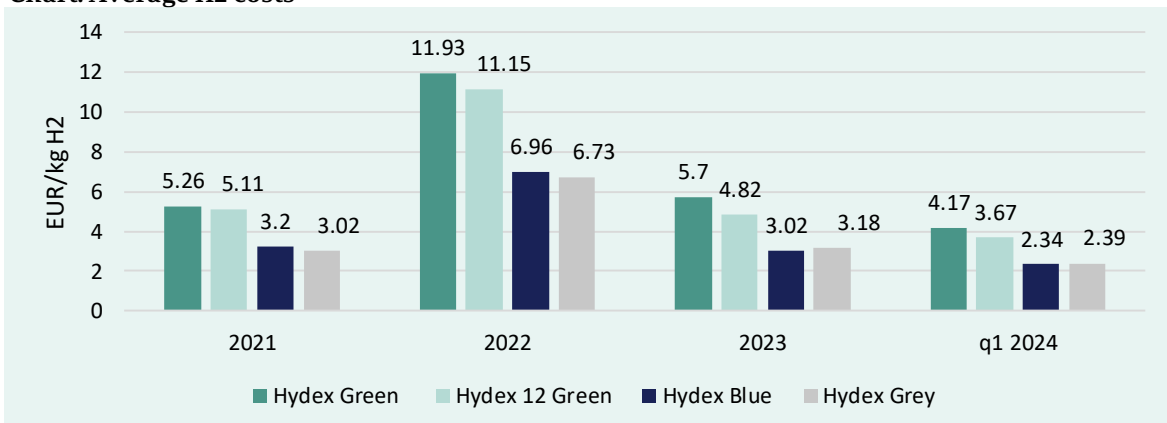
Hydrogen seen as miracle cure for the energy transition thanks to the absence of carbon atoms

Solutions for the transformation and energy transition all centre around hydrogen (H₂). In contrast to the fossil energy sources used to date, namely coal, oil and gas, H₂ has a matchless advantage: the absence of carbon atoms. The inclusion of H₂, with its high energy content, in each and every decarbonization strategy is therefore entirely justified. Unfortunately, the fact that there are chemical and physical differences between the energy carriers is often overlooked in the discussion. Put in layman's terms, the combustion of H₂ or the use of its energy content initially results merely in the formation of a compound comprised of H₂ and oxygen, in other words water. However, the production, i.e. the splitting of molecular compounds containing the element H, likewise requires energy. Although a kind of circular economy is thus created, there also energy deficits involved. This is repeatedly criticized, for example in the discussion on future forms of mobility, in which the physical limits of battery-electric drives are often overlooked.

Availability, manufacture and costs

The rapid substitution of oil and its derivatives (liquid) and coal (solid) can generally only be accomplished with difficulty. However, the fact that natural gas and H₂ share the same physical state means that this is most likely where best to start with the transition in mind. That said, differences in their respective atoms mean that the substances are not interchangeable on a 1-to-1 basis. H₂ is lighter than air, and its atoms smaller, which is why it can diffuse through many materials, and there is also the fact that H₂ can store less energy per cubic meter than natural gas. This is important insofar as only volume is discussed, which is usually the case when it comes to pipeline transport. H₂ has far higher energy density by weight than natural gas (approx. 3 to 4 times as much). Where pipelines are not an option, H₂ can be transported by railway wagon or ship (tanker), with liquefaction or compression of the hydrogen possible for this purpose. Conveyance of H₂ over longer distances by sea (intercontinental transport) requires conversion or a chemical bonding, for which carriers such as ammonia or LOHC (liquid organic H₂ carrier) are used. However, the conversion processes require energy once more. While H₂ is not toxic, carriers (such as ammonia) are. The core problem with H₂, however, lies in sufficient availability. Approximately 95 million metric tons of H₂ were produced worldwide in 2022. In 2030, estimates assume a demand of around 125 million metric tons, of which about 30 percent could be produced "green". In addition, there is the fact that the supply infrastructure is as yet insufficient and not fully developed. All in all, deficits are also reflected in the cost per unit of H₂.

Chart: Average H₂ costs



Sources: E-Bridge, NORD/LB Research

Since 2021, for example, E-Bridge Consulting has published the Hydrex cost index, which compares the various H₂ production processes on the basis of their marginal costs (without account being taken of capital costs). The volatilities associated with green electricity are of particularly negative significance in this context. Accordingly, a further comparative indicator was created in the form of the "Hydrex 12 Green" spot index, which describes the marginal production costs of an electrolyser (system that uses electricity to split water into hydrogen and oxygen) during the 12 most favourable hours of the day on average. It should be noted that these are marginal production costs only, and neither include capital costs nor transportation and distribution costs in Germany.

"Green" the wrong colour? Only in the short or medium term!

False colours are not only known to cigar smokers (second choice cigars) or card players (non-trump). This issue is also increasingly playing a role in the development of the hydrogen economy as part of the transformation. Hydrogen is initially classified by colour according to the original energy source used in its production. The generally used rainbow pattern usually includes nine shades of black/brown (hard coal/lignite) and grey (natural gas) and, with steadily decreasing climate-damaging emissions, the colour ultimately changes to green. Ideally, water is split into hydrogen (H₂) and oxygen (O₂) via electrolysis using electricity generated from renewable energy sources. However, what doesn't seem difficult at first glance proves less easy in the actual implementation. On the one hand, the decarbonization of entire industrial sectors requires enormous amounts of H₂ but, on the other, the general need for clean electricity from renewable energies is growing at the same time. Accordingly, the electricity is fed into the grid and is only available – if at all – to a limited extent for conversion into molecular hydrogen. This reopens the classic "pass-the-blame" game. If H₂ is not readily available, the transition to using it will either not happen at all or will be delayed, but without demand there will be no investment in the development and expansion of hydrogen production either.

H₂ bet only likely to pay off with the help of CCS technology

In order not to jeopardize the necessary ramp-up of the hydrogen economy, the existing capacities should be utilized and the use of "red" H₂ (nuclear energy as power source) and "blue" H₂ should no longer be demonized. The "blue" hydrogen is obtained from natural gas, but most of the CO₂ produced in the process (90%) is captured and not released into the atmosphere but instead injected into the seabed in the North Sea, for example. The corresponding technology (Carbon Capture & Storage) is already successfully in use in Norway. The only hurdle would lie in the transport of that CO₂ from industrial sites (steel sector) from within the country. The considerations in this context tend towards a pipeline. The Wilhelmshaven location, which is set for implementation as an energy hub, is the current favourite as CO₂ collection hub. This is the only way to successfully realize this key component of the transformation, especially given that the availability of the desired "green" hydrogen is not expected to be adequate in the foreseeable future. In 2023, it was estimated that just 0.3 percent of hydrogen production could be declared "green". In order not to waste valuable time on the transformation path, blue hydrogen must therefore be used as a bridge technology until sufficient quantities of green H₂ are readily available and can be utilized. At this point, however, it should be noted that CCS costs have tended upwards in the last 2 years. This development makes blue hydrogen a little more expensive again and, according to E-Bridge, will lead to an adjustment of the Hydrex in the coming weeks. Since the hydrogen core network as well as subsidies for the steel industry (one of the most important energy consumers) are in place, it is crucial to ensure supplies as quickly as possible in order to remain globally competitive in the steel sector and to be potentially able to export newly acquired expertise in mechanical and plant engineering at a later time. The H₂ colour model ought to be set aside for the time being, especially since statements from industry indicate that premiums on "green" products are rarely achievable.

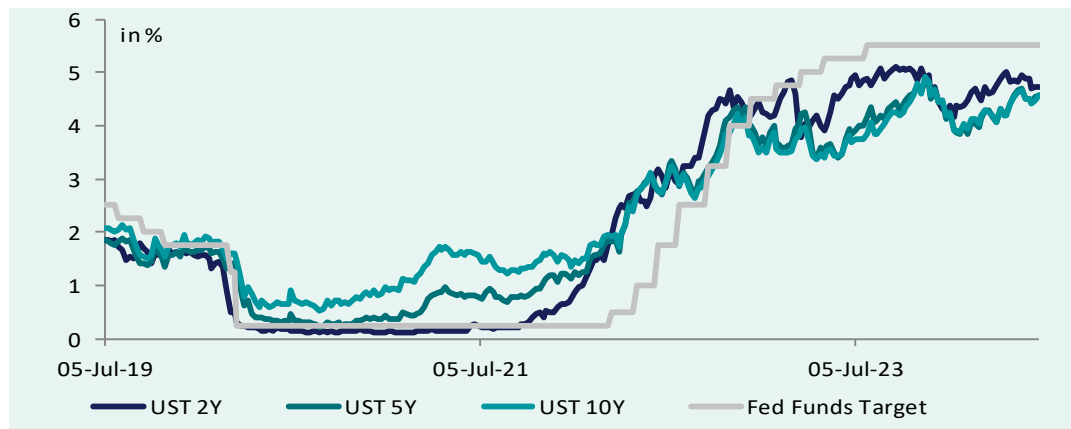
USA: Second half of the year to see the Fed able to take action

Analysts: Tobias Basse // Constantin Lüer

Relatively weak retail sales figures of late

As mainstay of the North American economy to date, the US consumer quite clearly remains in the focus of the international financial markets. Preliminary data indicate that retail sales grew by just 0.1 percent mom in May as month under review. Indeed, excluding automobile sales makes for a change rate of just -0.1 per cent mom. These figures can – especially when considering the data revisions carried out by the statisticians – at any rate only be described as a surprise on the downside. However, after the preceding month's marked phase of weakness, the control group of retail sales – which is of core relevance for the GDP survey – grew quite markedly by an impressive 0.4 percent mom, but this increase must probably be interpreted primarily as a countermovement. Though private household consumption thus remains a key supporting factor for economic expansion in the USA, there are limits to how much it can continue to help drive growth. Inflation concerns are undeniably of great importance in this context, so the rising wage levels at the moment cannot spark any real consumption appetite. While Q2/2024 can be expected to see quarter-on-quarter GDP growth able to pick up again, we are not reckoning with a really exceptional improvement, however.

Chart: Interest rates in the USA



Sources: Macrobond, NORD/LB Macro Research

High interest rates continue to weigh on the real estate market

The monthly FHFA House Price Index once again disappointed many market participants. An uptick of 0.2 percent mom was published for April, in addition to which the change rate of the time series reported for the previous month was revised marginally downwards to 0.0 percent mom. The Case Shiller HPIs for 20 metropolitan regions gave a more positive showing, with an increase of 0.38 percent mom. The high interest rates, however, continue to weigh on the mood in the US construction industry. This was reflected by the widely followed NAHB index's slump to just 43 points in June. Indeed, the "Prospective Buyers Traffic" subcomponent deteriorated significantly, with the time series now registering a level of just 28 points. It is evident from this current development that the demand side is to be seen as a major problem. The combination of persistently high house prices and significantly higher interest rates are clearly making the financing of property more difficult.

Second half of the year to see the Fed able to take action

US consumer prices rose by 3.3 percent yoy in May as month under review, so it looks as if the slight disinflationary tendencies in the USA are persisting. Given this environment, interest rate cuts are

gradually becoming an option again for the Fed's monetary policymakers. Indeed, against this background we are maintaining our view that the US central bank will actually implement two "small" downward rate adjustments in the course of the second six months of 2024. Though the concerns over growing inflation expectations of private households will likely retain relatively high relevance in the FOMC for the time being, the developments on the US price front ought to then permit corresponding adjustments from Q3/2024 onwards to what has in the meantime become a pretty restrictive monetary policy. A very close eye also needs to be kept on the figures from the United States labour market in this context. Although no truly lasting deterioration is to be expected there – the effects of the personnel shortage in the recent past are still making themselves felt – increasingly clear indications of a certain downturn should be expected to gradually emerge. Given the Federal Reserve's targets, a development of this nature would also have significance for the FOMC's further monetary policy. Moreover, the slowly burgeoning concerns about the rising interest burden on the state will likely provide the rationale for a lower Fed funds target rate. The central bankers in Washington will at any rate be looking to only very cautiously adapt their monetary strategy to the changed macroeconomic environment in North America.

Fundamental forecasts, USA

	2023	2024	2025
GDP	2.5	2.3	1.7
Private consumption	2.2	2.1	1.6
Govt. consumption	2.7	2.5	1.0
Fixed investment	2.0	2.5	2.6
Exports	2.6	1.9	2.5
Imports	-1.7	2.5	2.2
Inflation	4.1	3.1	2.3
Unemployment rate ¹	3.6	3.9	4.2
Budget balance ²	-6.5	-5.9	-6.1
Current acct. balance ²	-3.3	-3.1	-3.0

Change vs previous year as percentage; ¹ as percentage of the labour force; ² as percentage of GDP

Sources: Feri, NORD/LB Macro Research

Quarterly forecasts, USA

	III/23	IV/23	I/24	II/24	III/24
GDP qoq ann.	7.0	3.4	1.4	2.0	1.2
GDP yoy	2.9	3.1	2.9	1.7	1.2
Inflation yoy	3.5	3.2	3.2	3.3	3.1

Change as percentage

Sources: Feri, NORD/LB Macro Research

Interest and exchange rates, USA

	27.06.	3M	6M	12M
Fed funds target rate	5.50	5.25	5.00	4.50
3M rate	5.33	5.00	4.70	4.30
10Y Treasuries	4.29	4.00	3.70	3.60
Spread 10Y Bund	184	170	150	130
EUR in USD	1.07	1.07	1.09	1.09

Sources: Bloomberg, NORD/LB Macro Research

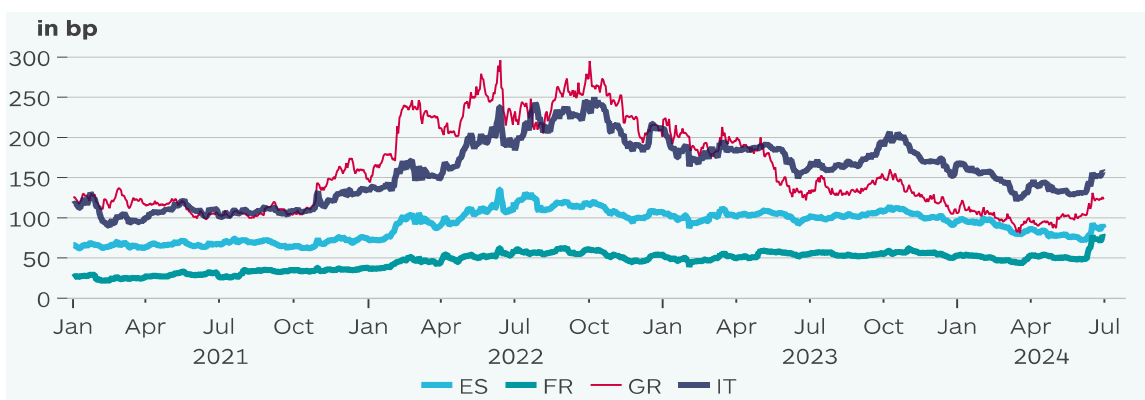
Euroland: ECB initiates cautious interest rate turnaround

Analysts: Christian Lips, Chief economist // Valentin Jansen

Economic sentiment remains subdued

Economic sentiment in the eurozone remains subdued. Though continuing to signal moderate growth, the purchasing managers' indices surprised on the downside in June with an unexpected setback. The Industry PMI registered a particularly clear decline to a level of 45.6 points and thus well inside the contraction zone. The EU Commission's monthly economic survey paints a similar picture, with a rebound in industrial confidence and a merely sluggish upward movement in consumer confidence. The Economic Sentiment Indicator remains largely unchanged at 95.9 points, well below the long-term average. For the time being, therefore, there is no acceleration in growth to be expected, for which reason we are maintaining our forecast of 2024 as a whole closing with real year-on-year GDP growth of just 0.7 percent – in which respect we are somewhat more cautious than the ECB in its latest projections.

Chart: Political uncertainty in the wake of the EU elections drives spreads to Bunds (10Y)



Sources: Macrobond, NORD/LB Macro Research

European elections: Macron's high-stakes gamble ill received in the markets

The European elections saw right-wing parties up their share of the vote, a trend particularly marked in some member countries such as France. Emmanuel Macron responded to the resounding electoral success of Marine Le Pen (Rassemblement National, RN) by deciding to go on the offensive, thereupon dissolving the National Assembly and calling a snap election. However, this move now threatens to backfire, as Macron's camp merely figured in third place in surveys polled in late June. An absolute majority for the RN is indeed unlikely but, with a hung parliament and a phase of cohabitation, the uncertainty about the future political direction would remain elevated. Against this background, Macron's high-stakes gamble is not going down well in the financial markets. The prospect of an election victory for the Rassemblement National and growing concerns about the future direction of fiscal policy have led to a significant widening of the spreads of French OATs to German Bunds (10Y). In the wake of increased political uncertainty there are also slight contagion effects to be seen in the euro area (see chart). The ECB has not been put on alert yet, but Ms Lagarde says that a close eye is being kept on it.

ECB: Much to be said for a cautious rate-cut path after the interest rate turnaround in June

As had been expected, the ECB initiated the "moderation of the degree of monetary policy restriction" phase at the last regular Council meeting and lowered all three key rates by 25 basis points. Anything other than a rate cut in June would have come as a surprise, with a whole lot of explosive power for the markets. Particular attention was paid to the central bank's updated projections. A certain surprise

came with the raising of the inflation forecast for 2025, with the achievement of the 2-percent stability target thus postponed back to the second half of that year. With the current inflation projections, the ECB is thus reversing a good part of the unexpectedly downward adjustment from March. In principle, the narrative – return to the 2-percent target in the course of 2025 – has remained unchanged since September last year. In light of the persistent upward movement in prices in the euro area, especially in services, and an improving economy, the Governing Council is still not looking to give guidance on the future interest rate path. However, key interest rates are expected to remain restrictive overall for some time to come, even if the pressure on the brake pedal is set to be slowly eased. Ms Lagarde's comments at the press conference on the ECB Governing Council's interest rate decision, which was adopted with just one dissenting vote, align well with this. In our view, the slightly lower inflation figures expected in late summer, together with a growing certainty that the euro area will return to price stability in the foreseeable future, open the door for a further rate cut. For precautionary reasons, however, this is not to be expected until September, and a rate cut is practically off the table for July. We have been stressing for some time that the meetings with updated projections will likely be given priority when it comes to further rate adjustments, which suggests an interest rate path of 25 basis points per quarter. With this pace of adjustment in mind, we expect a further key-rate cut by the same amount in December as well. In an interview in late June, ECB Governing Council member Olli Rehn – a central banker who, based on experience, cannot be classified as a hawk nor as a dove – described as reasonable forecasts that provide for a cut of 25 basis points per quarter and assume a terminal rate of up to 2.25 percent for 2025. This is quite close to our rate forecast, to which we are sticking.

Fundamental forecasts, Euroland

	2023	2024	2025
GDP	0.6	0.7	1.4
Private consumption	0.6	1.1	1.6
Govt. consumption	1.0	1.2	0.7
Fixed investment	1.5	-0.3	2.6
Net exports ¹	0.3	0.6	-0.1
Inflation	5.4	2.5	2.1
Unemployment rate ²	6.6	6.4	6.3
Budget balance ³	-3.6	-2.8	-2.6
Current account balance ³	1.7	2.1	1.7

Change vs previous year as percentage, ¹ as contribution to GDP growth; ² as percentage of the labour force; ³ as percentage of GDP

Sources: Feri, NORD/LB Macro Research

Quarterly forecasts, Euroland

	III/23	IV/23	I/24	II/24	III/24
GDP sa qoq	0.0	-0.1	0.3	0.3	0.3
GDP sa yoy	0.2	0.2	0.4	0.5	0.8
Inflation yoy	5.0	2.7	2.6	2.5	2.3

Change as percentage

Sources: Feri, NORD/LB Macro Research

Interest rates, Euroland

	27.06.	3M	6M	12M
Repo rate ECB	4.25	3.65	3.40	2.90
3M rate	3.70	3.50	3.30	2.80
10Y Bund	2.45	2.30	2.20	2.30

Sources: Bloomberg, NORD/LB Macro Research

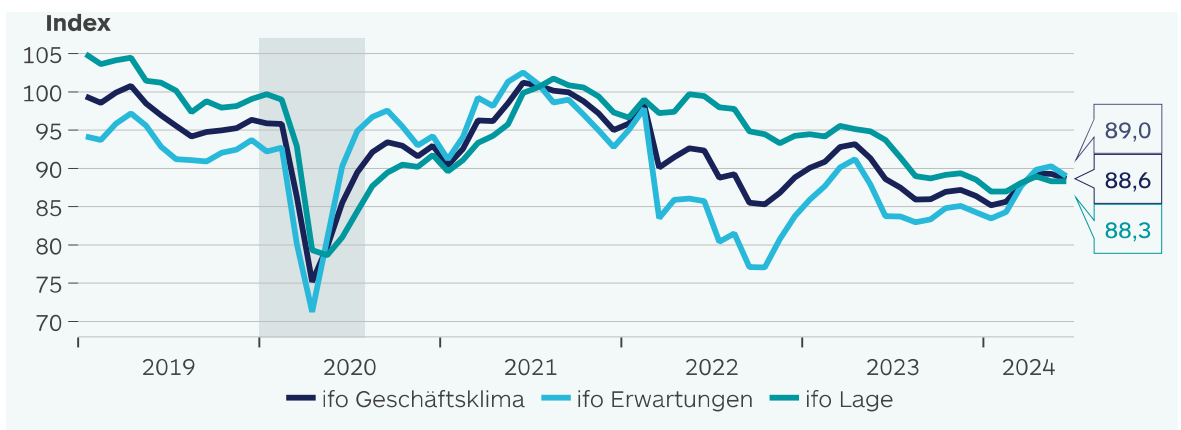
Germany: Sentiment dampener in June – EM tournament without sustained growth effect

Analysts: Christian Lips, Chief Economist // Christian Reuter

Industry with continued headwinds, export economy under pressure

Germany's economy has started into Q2 on a rather sluggish note so far. Preliminary data from the Federal Statistical Office indicate that manufacturing output contracted by 0.1 percent mom in real terms, adjusted for seasonal and calendar effects. This is partly put into perspective by atypical seasonal patterns in the construction industry, where the mild weather in winter made it possible to bring work forward. In the meantime, however, there is a lack of follow-up orders, as reflected, for example, in April's year-on-year decline of 17.0 percent in the number of issued residential building permits. Things have not gone smoothly of late in terms of foreign trade either. Exports to non-EU third countries, accounting for a good half of Germany's foreign trade, fell in May by 6.4 percent mom in real terms, adjusted for seasonal and calendar effects, down 2.3 percent yoy. On the other hand, exports to the USA, Germany's largest trading partner, rose sharply, by 4.1 percent yoy. However, this is not enough to compensate for the declines in exports to the country's second and third largest foreign markets, namely China (-14.0 percent yoy) and Britain (-1.7 percent yoy). This indicates an overall contraction in export volume, as exports to the EU are not expected to make up for this shortfall. The disillusionment in many industrial companies about the recovery now becoming more distant is now having an impact on the labour market as well, with the unemployment rate soaring to 6.0 percent in June. The economic upturn will likely bypass the labour market this time since many companies have "hoarded" workers in light of the shortage of skilled labour and need no added manpower right now.

Chart: ifo business climate disappoints in June – ray of hope for the services sector



Sources: Macrobond, ifo, NORD/LB Macro Research

ifo and PMIs: Sentiment dampener in June on hopes for growth

Overall, the leading indicators painted a mixed picture in June. While the surveys among financial market experts (ZEW, sentix) had still sent slightly positive signals, sentiment among German companies suffered an unexpected setback in June. The purchasing managers' indices surprised clearly on the downside: the Industry PMI registered a particularly marked deterioration, with its Services part also slight down in June. Contrary to expectations the ifo Business Climate Index likewise dropped, to a level of 88.6 points. In particular business expectations slumped, while companies remained dissatisfied with the current business situation, with the level of 88.3 points unchanged mom. The effect of the ECB's initial interest rate cut appears to have largely faded. What particularly stands out in the ifo sur-

vey at the sectoral level is the significant setback for the trade sector, though in the manufacturing sector, too, the mood clouded significantly in June. Contrary to the indication from the purchasing managers, however, the sentiment among service providers brightened noticeably and, with the balance at 4.2 points, hit its highest level since May 2023. Overall, the ifo survey for June as month under review was disappointing. While this has barely impacted the mood on the stock markets, the latest signs of weakness from the leading indicators are a clear dampener for the economic outlook, however. In particular the weakness in industry is slowing the German economy, and proves how fragile the economic bounceback still is. With the threat of fresh tariff disputes and ongoing geopolitical tensions, the underlying conditions for the strongly export-oriented German industrial sector remain difficult. While some institutions have revised their forecasts slightly upwards, we are maintaining our cautious growth forecast of 0.2 percent for Germany for 2024.

No sustained growth effect from the EM tournament to be expected

The extent of the European Football Championship's contribution to the sentiment upturn in the services sector is difficult to estimate. The overall picture of all leading indicators in June shows no positive effect from Euro 2024 for its host country in the sense of any sustainable increase in overall economic activity. Expectations in this direction are exaggerated anyway. Empirically and especially for large countries, no systematic positive effects for GDP growth or private consumption can be identified from major (soccer) events. However, there can be significant shifts during the year, especially in individual economic sectors – for instance due to the short-term increase in travel activity. And, according to the ifo Institute, there was more positive feedback from the hospitality industry in June. However, it is to be feared that this is a one-off effect and that with the end of the tournament the effect might even reverse again. Even if no one here in Germany would have anything against it: That the equation "Summer fairytale 2.0 + good performance of the national team = economic upturn" can become reality this year is thus highly questionable. The sporting path to winning the title is admittedly difficult in itself, but is at any rate manageable – for which we keep our fingers crossed!

Fundamental forecasts, Germany

	2023	2024	2025
GDP	-0.2	0.2	1.1
Private consumption	-0.7	0.8	1.8
Govt. consumption	-1.0	1.0	1.2
Fixed investment	-0.7	-1.0	2.4
Exports	-0.7	1.8	3.8
Imports	-2.4	1.0	5.2
Net exports ¹	0.8	0.4	-0.4
Inflation ²	6.0	2.6	2.3
Unemployment rate ³	5.7	6.0	5.9
Budget balance ⁴	-2.5	-1.7	-1.0
Current account balance ⁴	6.1	7.5	6.7

Change vs previous year as percentage, ¹as contribution to GDP growth; ²HICP; ³as percentage of the civil labour force (Federal Employment Office definition); ⁴as percentage of GDP

Sources: Feri, NORD/LB Macro Research

Quarterly forecasts, Germany

	III/23	IV/23	I/24	II/24	III/24
GDP sa qoq	0.1	-0.5	0.2	0.2	0.3
GDP nsa yoy	-0.5	-0.4	-0.9	0.6	0.6
Inflation yoy	5.7	3.0	2.7	2.6	2.2

Change as percentage

Sources: Feri, NORD/LB Macro Research

Switzerland: Return to neutral monetary policy

Analyst: Christian Reuter

Domestic demand still the dominant driving force – external economic stimuli awaited

In its summer forecast for GDP, Switzerland's State Secretariat for Economic Affairs (SECO) is somewhat more optimistic than in the spring, for 2024 raising the growth expectations for the Swiss economy by 0.1 percentage points to 1.2 percent yoy. On the other hand, the SECO experts expect the companies to remain reluctant to invest for the time being in light of the existing underutilization. They also expect rather dampening effects from foreign trade for now, as economic activity in the USA and China is slowing and the euro area is only very sluggishly picking up momentum. They do expect, however, that the Swiss franc's somewhat weaker exchange rate will support the export economy, and thus industrial output, in the medium term. The KOF Economic Barometer is giving the green light here, having advanced by 0.5 points to a level of 102.5 in June. Together with the significant upward revision in the previous month, this clearly paints the picture of a continued moderate upturn. For the time being, however, it looks as though growth will continue to be based on domestic economic factors such as the service sectors and consumption in the second half of 2024 as well. The SECO experts expect a slight acceleration of the Swiss economy in the coming year, and saw no reason to adjust their growth forecast from the spring. They also expect additional stimuli, in particular from foreign trade, and to see an end to the phase of weakness in investment. Accordingly, the risks to the Swiss economy are mainly to be seen abroad at present.

Second rate cut in a row – return to neutral monetary policy

The trend in inflation paved the way for the SNB. Inflation remained unchanged at 1.4 percent yoy in May. The core rate, too, remained unchanged, at 1.2 percent yoy, and thus slightly lower than economists had anticipated. As expected, the Swiss National Bank lowered its key interest rate by 25bp to 1.25 percent in June. When making its decision, the SNB also took account of the exchange rate of the Swiss franc, which had appreciated by up to 4 percent at its peak since late May. The central bank is certainly looking to avoid importing deflation, as it would be difficult to combat due to the low interest rate level in Switzerland. In making this second rate cut, the SNB is abandoning its restrictive stance and initiating a phase of economically neutral monetary policy. The focus will now likely increasingly shift towards external economic developments. The political uncertainties in Europe and the European monetary union play a major role here, making the franc attractive as a safe haven. Immediately after the interest rate decision, the Swiss franc lost 0.5 percent against the euro. The still quite weak state of economic activity at home and abroad, together with inflation in the target range provide a rationale for a further rate cut in September, especially as the ECB is expected to cut rates. The appointment of new SNB President Martin Schlegel, an insider, reflects the central bank's wish for continuity.

Fundamental forecasts*, Switzerland

	2023	2024	2025
GDP	1.2	1.3	1.8
Inflation (CPI)	2.1	1.2	1.0
Unemployment rate ¹	2.0	2.3	2.3
Budget balance ²	0.3	0.3	0.2
Current account bal. ²	7.0	7.5	7.5

Interest and exchange rates, Switzerland

	27.06.	3M	6M	12M
SNB policy rate	1.25	1.00	1.00	1.00
3M rate	1.19	0.90	0.90	0.90
10Y	0.56	0.60	0.70	0.90
Spread 10Y Bund	-189	-170	-150	-140
EUR in CHF	0.96	0.96	0.97	0.97

* Change vs previous year as percentage; ¹ as percentage of the labour force, ² as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

Japan: Central bank in Tokyo also pinning hopes on the Fed

Analyst: Tobias Basse

Ongoing pressure on the yen

The Japanese currency remains under enormous pressure, with the psychologically important mark of 160.00 JPY per USD now in focus. This development is evidently making for fears in the forex market that the US central bank might not be making any further rate cuts in 2024. The weak yen remains a double-edged sword for the Japanese economy. On the one hand, the Japanese currency's depreciation tendencies quite clearly deliver positive stimuli for the domestic export industry, as reflected in the fact that exports grew significantly in May by an impressive 13.5 percent yoy. On the other hand, rising import prices are increasingly threatening to weigh more lastingly on household consumption. This problem is seen especially by the policymakers in the Japanese Ministry of Finance. Basically, therefore, hardly anything has changed of late. Against this background, the Bank of Japan is now likely under considerable pressure to take action, and there can be no doubt that further interest rate hikes meanwhile are on the agenda of the central bankers in Tokyo.

Caution called for

As expected, the Bank of Japan had no intention of announcing any adjustments to its interest rate policy, meaning that the key rates remain within the range of 0.00 to 0.10 percent for the time being. That said, the current inflation data from the Land of the Rising Sun have now probably dispelled any remaining deflation concerns among the central bankers in Tokyo; indeed, consumer prices rose by 2.8 percent yoy in May. Though distorting special effects also play a major role in explaining this movement, the BoJ can nevertheless already start considering raising its key rates in the very near term. A rate hike in July has now become highly likely, with recent comments by central bank governor Kazuo Ueda also pointing in this direction! However, the Bank of Japan will be looking to remain cautious in the upcoming adjustments to its monetary policy. This probably likewise applies to the foreseeable quantitative tightening measures!

Central bankers in Tokyo also pinning hopes on the Fed

It goes without saying that slightly higher key rates in Tokyo could help the yen a bit. However, a clear trend reversal, which would then also make for a "real" abatement of the Japanese currency's current phase of weakness, would probably require a great deal more boldness on the part of the central bankers in the Land of the Rising Sun – which is something the BoJ officials are unlikely to summon up. A diffuse fear of deflation appears to be firmly anchored in the minds of many central bankers in Tokyo. It looks as if the Bank of Japan is also hoping for near-term rate cuts by the Fed, which would then help provide much more sustainable support for the yen!

Fundamental forecasts*, Japan

	2023	2024	2025
GDP	1.9	0.2	1.3
Inflation	3.3	2.4	1.8
Unemployment rate ¹	2.6	2.5	2.4
Budget balance ²	-5.2	-4.2	-3.6
Current account bal. ²	3.6	3.7	3.5

* Change vs previous year as percentage;

¹ as percentage of the labour force; ² as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

Interest and exchange rates, Japan

	27.06.	3M	6M	12M
Key rate	0.10	0.20	0.20	0.25
3M rate	0.31	0.25	0.30	0.35
10Y	0.66	1.00	1.10	1.20
Spread 10Y Bund	205	-130	-110	-110
EUR in JPY	172	168	165	157
USD in JPY	161	157	151	144

China: Economic environment remains inconsistent

Analyst: Valentin Jansen

Caixin Manufacturing PMI unexpected hits a two-year high

With the official Manufacturing PMI having unexpectedly dropped back below the growth threshold in May, the results of the Caixin Manufacturing PMI were a particular focus of attention. Against this background, observers found themselves wondering if they were seeing things as this index unexpectedly hit a two-year high of 51.7 points, outpacing expectations. Overall, the Caixin Manufacturing PMI has been signalling expansive tendencies in key segments of China's industry for seven months, with levels just above the 50-point mark – a trend also attributable to the index's composition, especially among SMEs in southern China. A closer look at the details reveals positive developments: growth in both domestic and foreign demand continued upwards, prompting the companies to scale up production and purchasing activities. This is also backed up by the latest foreign trade data, according to which exports were above consensus estimates in May, at 7.6 percent yoy. By contrast, the import side again gave a disappointing showing, dropping back to a small yoy plus of just 1.8 percent and thus delivering an ongoingly weak picture of domestic consumption. May's inflation data point in this direction too, according to which the CPI remained lacklustre at 0.3 percent yoy. Month-on-month comparison makes the frailty in the consumer price trend even more evident, with the minor plus in April (0.1 percent mom) "cancelled out" in the latest data by contraction in the same amount.

Beijing's reform endeavours and foreign trade relations remain clearly in focus

Tedious and rather sectoral economic progress mean that the focus in China's stock markets remains first and foremost on the developments around Beijing's reform endeavours and foreign trade relations. New levels of escalation in punitive tariffs on imports of electric vehicles into the EU, for example are particularly weighing on sentiment in the stock markets. While initial rapprochements between Brussels and Beijing provide grounds for hope, new import duties are now also looming from the Canadian side, however. Difficult as it is to rescue from its ongoing predicament, the real estate sector has triggered a series of government support programs in recent weeks, though their effect will likely take quite some time to kick in.

PBOC to trade government bonds on the secondary market for the first time in two decades

After a two-decade hiatus, the PBOC is once again planning to trade government bonds on the secondary market in order to gain more control in the tense liquidity environment. On the other hand, the leeway for easing key interest rates will likely remain limited until the Fed follows in the wake of the European Central Bank and also begins to moderate its restrictive monetary policy. The ECB's initial rate cut in early June undoubtedly made for somewhat more flexibility; historically, interest rate adjustments by the PBOC have typically been in the amount of '-15 basis points'.

Fundamental forecasts*, China

	2023	2024	2025
GDP	5.2	4.8	4.5
Inflation	0.3	0.7	1.5
Unemployment rate ¹	5.2	5.2	5.1
Budget balance ²	-4.6	-4.8	-4.8
Current account bal. ²	1.4	1.3	1.2

* Change vs previous year as percentage;

¹ as percentage of the labour force; ² as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

Interest and exchange rates, China

	27.06.	3M	6M	12M
Deposit rate	1.50	1.50	1.50	1.50
3M SHIBOR	1.92	2.00	2.00	2.00
10Y	2.21	2.30	2.30	2.30
Spread 10Y Bund	-24	0	10	0
EUR in CNY	7.78	7.76	7.85	7.83
USD in CNY	7.27	7.25	7.20	7.18

Britain: On the verge of a policy shift?

Analyst: Constantin Lüer

The lights are at green

20 June saw the MPC meet to discuss its further interest rate strategy, opting to leave the Bank Rate unchanged at 5.25 percent for the time being. This date was interesting in that the latest findings on inflation developments for May were released just one day before, with the news that the inflation target of 2.0 percent had been achieved. Though having identified a relaxation in consumer price trends, the Bank of England nonetheless expects inflation to rise again (slightly) and therefore prefers to wait before taking further action. The reason behind this strategy lies in the temporarily lower energy prices in mid-2023, which are "artificially" dragging down the current annual rate and quite possibly making the present situation somewhat misleading.

Monetary policy shift likely in Q3

Seeing as the in some cases low monthly rates from the previous year are no longer considered in the calculation and the current data indicate the likelihood of an inflation rate of over 2.0 percent yoy in the short term, the MPC is accordingly maintaining a cautious stance. Various central bankers have also repeatedly emphasized the primacy of price stability. Nonetheless, we consider an initial rate cut in the August or September meeting as likely. The upside risks in terms of consumer prices are more or less stable. There is a rather flattening dynamic to be seen, for example in the various sub-sectors of the services industry, if still at a fairly high level. Indeed, "goods and commodities" as second key sub-component actually registered zero growth.

An election thriller in the offing

The discussions on key interest rates are not the main subject of media coverage right now, however. The UK's voters are set to go the polls on 4 July to elect a new House of Commons – with the strong likelihood of a shift in power. Besides smaller parties, the main political events of the day revolve around the conservative Tories, who have been in power for over 14 years, with their leading candidate and incumbent Prime Minister Rishi Sunak, and the Labour Party headed by Sir Keir Starmer. An unknown variable for the coming parliamentary term will likely be the right-wing populist "Reform UK" party – with opinion poll ratings of 17 percent putting it just behind the Tories. Nigel Farage, a driving force behind Brexit, positioned himself virtually at the last minute as the party's top candidate, which indeed increased its popularity. However, Labour is well ahead of the Tories and Reform UK in the opinion polls with 41 percent, and will likely win the most seats in the House of Commons. Indeed, given the UK's first-past-the-post electoral system, forecasts indicate the likelihood of even more seats for Labour than signalled by the already positive polls. The elections are at any rate not likely to make for any greater economic frictions.

Fundamental forecasts*, Britain

	2023	2024	2025
GDP	0.1	0.2	1.8
Inflation (CPI)	7.3	2.9	2.2
Unemployment rate ¹	4.0	4.4	4.5
Budget balance ²	-5.0	-3.6	-3.1
Current account bal. ²	-3.3	-2.7	-2.8

* Change vs previous year as percentage

¹ as percentage of the labour force as per ILO concept,

² as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

Interest and exchange rates, Britain

	27.06.	3M	6M	12M
Repo rate	5.25	5.00	4.75	4.25
3M rate	5.13	4.78	4.55	4.03
10Y	4.13	3.80	3.68	3.50
Spread 10Y Bund	168	150	148	120
EUR in GBP	0.85	0.86	0.86	0.86
GBP in USD	1.26	1.24	1.27	1.27

Quelle: Feri, Bloomberg, NORD/LB Macro Research

Australia: Economy at a crossroads?

Analyst: Constantin Lüer

Reserve Bank of Australia with undefined strategy

At its monetary policy meeting in early June the RBA held the cash rate unchanged at 4.35 percent as generally expected, the main reason being the persistently high yoy and qoq inflation rates of 3.6 and 1.0 percent respectively in Q1/2024. Price stability is defined a little further and more flexibly Down Under than at the ECB or the Fed, for example, and is put at between 2-3 percent yoy. Another special aspect is that the official data are only reported on a quarterly basis. However, there are various inflation estimators, such as the Melbourne Institute Inflation Gauge, which indicates a rate of 0.3 percent mom for May. The three preceding months had consistently registered lower rates, against which background the RBA understandably prefers to wait and see how the inflation situation develops before making any adjustments to its key rate. Indeed, the Australian central bankers are deliberately leaving it unclear whether the interest rate might actually develop downwards or even upwards.

A host of concerns keep the RBA on alert

The growing momentum in inflation of late as well as the ongoing upward risks are making for some degree of unease among the central bankers. A further source of concern for the monetary policymakers lies in the state of overall economic activity itself. With GDP growth of 0.1 percent qoq in Q1/2024, Australia's economy made an extremely weak start to the year and merely continued last year's "losing streak". These two issues – inflation and the smouldering risk of a tangible recession – are, as she herself says, also the ones preoccupying the RBA's current governor and chair Michelle Bullock. While central banks are supposed to protect economies from overheating, the fact is that in this case the strategy already appears to be too restrictive. Nevertheless, RBA officials are not even ruling out the possibility of key-rate hikes at the moment.

Positive stimuli from China

There is also some good news, however. The easing of the tensions in trade relations between Australia and China is progressing steadily, and previously imposed trade restrictions are being increasingly lifted. This is particularly good news for Australia, as around a third of all its exports go to the Middle Kingdom. Rich in raw materials, Australia supplies China with coal, for example, but agricultural products such as wine, cereals and beef from Down Under are also in demand. The lifting of punitive tariffs has therefore stimulated export activity. In return, Australia has withdrawn existing complaints to the World Trade Organization regarding punitive tariffs imposed by China. Li Qiang's recent visit to Australia is likely symbolic of the improving relationship between the two states – this was the first official visit by a Chinese prime minister in seven years.

Fundamental forecasts*, Australia

	2023	2024	2025
GDP	2.0	1.2	2.2
Inflation	5.6	3.5	2.8
Unemployment rate ¹	3.7	4.2	4.5
Budget balance ²	-0.8	-0.6	-0.8
Current account bal. ²	0.3	0.5	0.1

*Change versus previous year as percentage;

¹ as percentage of the labour force; ² as percentage of GDP

Sources: Feri, Bloomberg, NORD/LB Macro Research

Interest and exchange rates, Australia

	27.06.	3M	6M	12M
Cash target rate	4.35	4.35	4.20	4.00
3M rate	4.46	4.40	4.25	3.85
10Y	4.00	4.20	4.10	3.90
Spread 10Y Bund	155	190	190	160
EUR in AUD	1.61	1.62	1.60	1.57
USD in AUD	0.66	0.66	0.67	0.68

Portfolio strategies

Yield curve, Euroland

Yields and forecasts (Bunds/Swap)

	Yields (in %)	NORD/LB forecasts for the horizons		
	27.06.2024	3M	6M	12M
3M	3.70	3.50	3.30	2.80
1Y	3.21	2.90	2.60	2.20
2Y	2.81	2.50	2.30	2.00
3Y	2.58	2.37	2.17	2.00
4Y	2.50	2.30	2.10	2.04
5Y	2.44	2.30	2.10	2.10
6Y	2.43	2.30	2.13	2.15
7Y	2.42	2.30	2.15	2.19
8Y	2.36	2.30	2.17	2.23
9Y	2.41	2.30	2.19	2.27
10Y	2.45	2.30	2.20	2.30
2Y (Swap)	3.19	2.85	2.65	2.40
5Y (Swap)	2.85	2.65	2.45	2.50
10Y (Swap)	2.80	2.65	2.55	2.70

Sources: Bloomberg, NORD/LB Macro Research

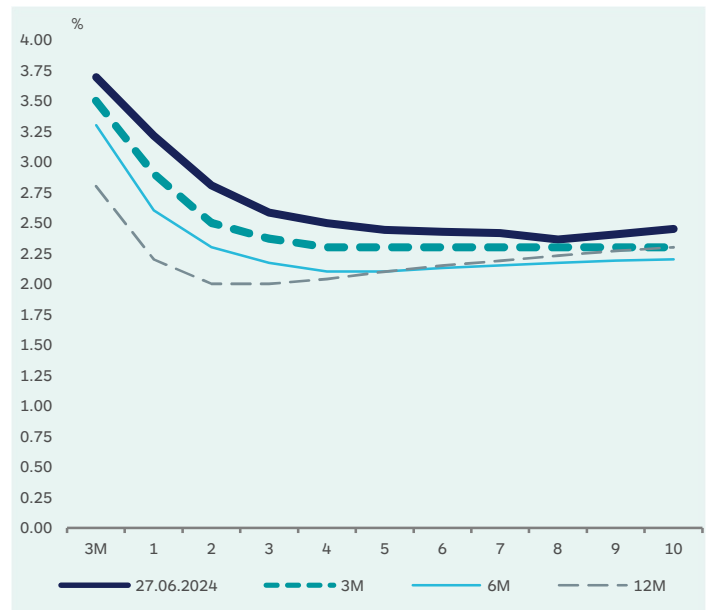
Forecasts and total returns

	Total returns (in %) for horizons...		
	3M	6M	12M
3M	0.93	1.81	3.43
1Y	1.02	1.90	3.21
2Y	1.06	1.94	3.41
3Y	1.13	0.81	3.76
4Y	1.28	2.48	3.97
5Y	1.27	2.71	4.03
6Y	1.31	2.85	4.03
7Y	1.36	2.92	3.99
8Y	1.07	2.69	3.58
9Y	1.46	3.01	3.81
10Y	1.90	3.44	4.01

Sources: Bloomberg, NORD/LB Macro Research

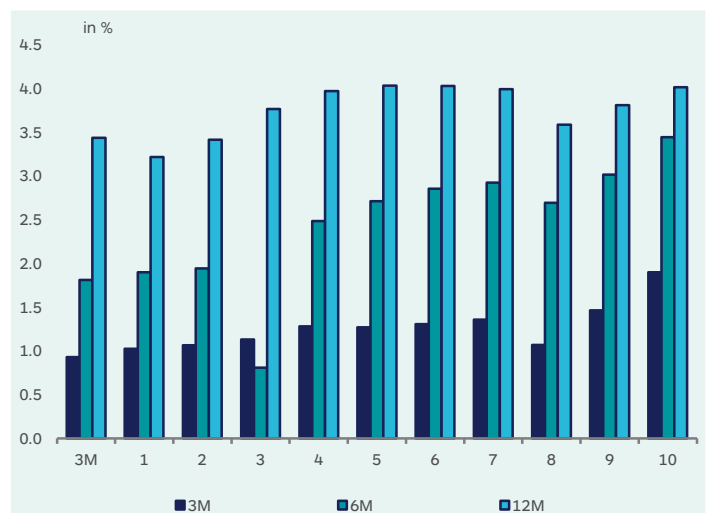
A total return is the absolute profit from an investment in the time period under consideration, with account being taken of the pro-rata yields plus the price gains or losses to be anticipated on the basis of the forecast yield curve change.

Yield curve forecasts (Bunds)



Sources: Bloomberg, NORD/LB Macro Research

Expected total returns



Sources: Bloomberg, NORD/LB Macro Research

Portfolio strategies

International yield curve: 3-month & 12-month horizons

3-month horizon

Expected total returns (as percentage) in euro					
	EUR	USD	GBP	JPY	CHF
1Y	1.0	1.2	-0.5	2.5	0.4
2Y	1.1	0.6	-1.3	2.7	0.3
3Y	1.1	0.6	-1.8	2.4	0.2
4Y	1.3	0.4	-1.5	2.4	0.2
5Y	1.3	0.0	-2.1	2.6	0.2
6Y	1.3	0.9	-2.4	2.2	0.0
7Y	1.4	-0.6	-1.7	2.5	-0.2
8Y	1.1	-0.6	-1.3	2.5	0.0
9Y	1.5	-0.4	-0.2	2.7	-0.1
10Y	1.9	-0.2	1.2	3.3	-0.2

Sources: Bloomberg, NORD/LB Macro Research

Expected total returns (as percentage) in national currencies				
	USD	GBP	JPY	CHF
1Y	1.2	1.1	0.0	0.2
2Y	0.6	0.2	0.0	0.0
3Y	0.6	-0.3	0.0	0.0
4Y	0.3	0.1	-0.1	0.0
5Y	-0.1	-0.5	0.2	0.0
6Y	0.8	-0.8	-0.2	-0.2
7Y	-0.6	-0.2	0.0	-0.4
8Y	-0.7	0.3	0.1	-0.2
9Y	-0.5	1.4	0.2	-0.3
10Y	-0.3	2.8	0.9	-0.4

Sources: Bloomberg, NORD/LB Macro Research

12-month horizon

Expected total returns (as percentage) in euro					
	EUR	USD	GBP	JPY	CHF
1Y	3.2	2.9	3.1	9.8	0.0
2Y	3.4	2.2	2.9	10.1	-0.2
3Y	3.8	2.2	2.8	9.9	-0.4
4Y	4.0	2.4	3.2	10.0	-0.4
5Y	4.0	2.7	3.0	10.3	-0.5
6Y	4.0	4.3	3.1	9.9	-0.7
7Y	4.0	3.3	4.1	10.1	-1.2
8Y	3.6	3.5	4.6	9.9	-1.8
9Y	3.8	3.8	5.7	9.9	-2.2
10Y	4.0	4.0	6.6	10.3	-3.4

Sources: Bloomberg, NORD/LB Macro Research

Expected total returns (as percentage) in national currencies				
	USD	GBP	JPY	CHF
1Y	4.8	4.6	0.2	0.9
2Y	4.1	4.4	0.4	0.6
3Y	4.1	4.4	0.3	0.4
4Y	4.3	4.8	0.3	0.4
5Y	4.6	4.6	0.7	0.3
6Y	6.2	4.7	0.3	0.1
7Y	5.2	5.7	0.4	-0.4
8Y	5.4	6.2	0.3	-1.0
9Y	5.7	7.4	0.3	-1.4
10Y	5.9	8.3	0.6	-2.6

Sources: Bloomberg, NORD/LB Macro Research

A total return is the absolute profit from an investment in the time period under consideration, with account being taken of the pro-rata yields plus the price gains or losses to be anticipated on the basis of the forecast yield curve and exchange rate change.

Portfolio strategies

Stock market strategy; 3-month, 6-month & 12-month horizon

Levels and performance

Index	Level		Status		Performance	
	as at				since	
	27.06.2024	Prev. month	Start of year	Prev. month	Start of year	
DAX	18,210.55	18,497.94	16,751.64	-1.55%	8.71%	
MDAX	25,373.89	26,716.80	27,137.30	-5.03%	-6.50%	
EuroSTOXX50	4,902.60	4,983.67	4,521.44	-1.63%	8.43%	
STOXX50	4,498.87	4,488.56	4,093.37	0.23%	9.91%	
STOXX600	512.59	518.17	478.99	-1.08%	7.01%	
Dow Jones	39,164.06	38,686.32	37,689.54	1.14%	3.82%	
S&P 500	5,482.87	5,277.51	4,769.83	3.80%	14.84%	
Nikkei	39,341.54	38,487.90	33,464.17	2.22%	17.56%	

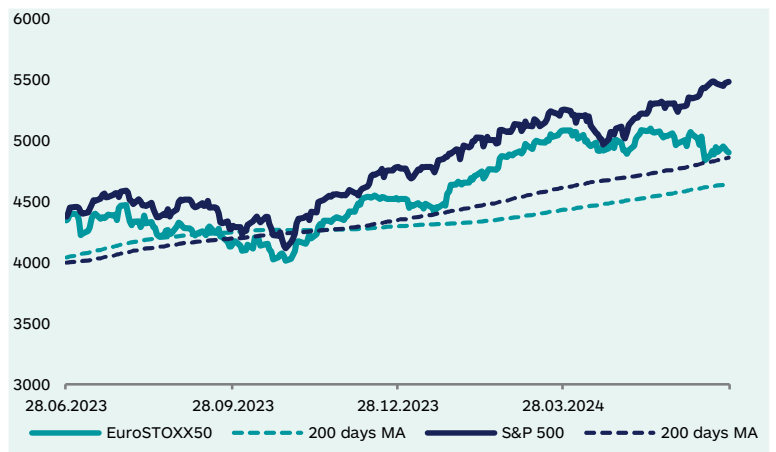
Sources: Bloomberg, NORD/LB Macro Research

Index forecasts

Index	NORD/LB forecast for the horizons ...		
	3M	6M	12M
	DAX	17,500	18,500
MDAX	25,500	26,700	27,400
EuroSTOXX50	4,700	4,950	5,100
STOXX50	4,350	4,400	4,450
STOXX600	500	510	550
Dow Jones	38,500	38,500	39,000
S&P 500	5,100	5,100	5,200
Nikkei	38,000	39,500	38,500

Sources: Bloomberg, NORD/LB Macro Research

EuroSTOXX50 and S&P500



Sources: Bloomberg, NORD/LB Macro Research

Date of going to press for data, forecasts and texts was **Friday 28 June 2024**.

The next English issue of Economic Adviser will be appearing on **2 September 2024**.

Overview of forecasts

Fundamental forecasts

in %	GDP growth			Rate of inflation			Unemployment rate ¹			Budgetary balance ²		
	2023	2024	2025	2023	2024	2025	2023	2024	2025	2023	2024	2025
USA	2.5	2.3	1.7	4.1	3.1	2.3	3.6	3.9	4.2	-6.5	-5.9	-6.1
Euroland	0.6	0.7	1.4	5.4	2.5	2.1	6.6	6.4	6.3	-3.6	-2.8	-2.6
Germany	-0.2	0.2	1.1	6.0	2.6	2.3	5.7	6.0	5.9	-2.5	-1.7	-1.0
Japan	1.9	0.2	1.3	3.3	2.4	1.8	2.6	2.5	2.4	-5.2	-4.2	-3.6
Britain	0.1	0.2	1.8	7.3	2.9	2.2	4.0	4.4	4.5	-5.0	-3.6	-3.1
Switzerland	1.2	1.3	1.8	2.1	1.2	1.0	2.0	2.3	2.3	0.3	0.3	0.2
China	5.2	4.8	4.5	0.3	0.7	1.5	5.5	5.2	5.1	-4.6	-4.8	-4.8

Change vs previous year as percentage; ¹ as percentage of the labour force (Germany: as per Federal Employment Office definition); ² as percentage of GDP

Sources: Feri, NORD/LB Macro Research

Key interest rates

In %	27.06.24	3M	6M	12M
USD	5.50	5.25	5.00	4.50
EUR	4.25	3.65	3.40	2.90
JPY	0.10	0.20	0.20	0.25
GBP	5.25	5.00	4.75	4.25
CHF	1.25	1.00	1.00	1.00
CNY	1.50	1.50	1.50	1.50

Sources: Bloomberg, NORD/LB Macro Research

Exchange rates

EUR in...	27.06.24	3M	6M	12M
USD	1.07	1.07	1.09	1.09
JPY	172	168	165	157
GBP	0.85	0.86	0.86	0.86
CHF	0.96	0.96	0.97	0.97
CNY	7.78	7.76	7.85	7.83

Interest rates (government bonds)

	3M rates				Yields 2Y				Yields 5Y				Yields 10Y			
	27.06.	3M	6M	12M	27.06.	3M	6M	12M	27.06.	3M	6M	12M	27.06.	3M	6M	12M
USD	5.33	5.00	4.70	4.30	4.71	4.30	4.00	3.90	4.30	4.10	3.90	3.60	4.29	4.00	3.70	3.60
EUR	3.70	3.50	3.30	2.80	2.81	2.50	2.30	2.00	2.44	2.30	2.10	2.10	2.45	2.30	2.20	2.30
JPY	0.31	0.25	0.30	0.35	0.06	0.30	0.35	0.37	0.26	0.60	0.65	0.67	0.66	1.00	1.10	1.20
GBP	5.13	4.78	4.55	4.03	4.24	4.68	4.46	3.98	4.01	4.35	4.08	3.81	4.13	3.80	3.68	3.50
CHF	1.19	0.90	0.90	0.90	0.76	0.75	0.70	0.80	0.64	0.65	0.70	0.70	0.56	0.60	0.70	0.90

Sources: Bloomberg, NORD/LB Macro Research

Spreads (bp)

	3M EURIBOR				2Y Bund				5Y Bund				10Y Bund			
	27.06.	3M	6M	12M	27.06.	3M	6M	12M	27.06.	3M	6M	12M	27.06.	3M	6M	12M
USD	164	150	140	150	191	180	170	190	186	180	180	150	184	170	150	130
JPY	-339	-325	-300	-245	-275	-220	-195	-163	-218	-170	-145	-143	-179	-130	-110	-110
GBP	143	128	125	123	143	218	216	198	157	205	198	171	168	150	148	120
CHF	-251	-260	-240	-190	-205	-175	-160	-120	-181	-165	-140	-140	-189	-170	-150	-140

Sources: Bloomberg, NORD/LB Macro Research

Annex



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Origination Corporates
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+49 511 9818-9650

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Financials
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Corporate Customers
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