Liquidity letter

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Who will cut rates first?

US inflation delays Fed rate cuts

ECB ready to cut rates if inflation falls further

- **US** The latest US inflation data do not allow the Fed to justify the start of an interest rate cut. The solidity of the economy has meant that in recent months, anticipation of the start of a rate cut has been postponed on numerous occasions. The core inflation data due next week should not give any different signals.
- **US Govies** US government bond yields hit new highs since the start of the year - with the two-year yield briefly exceeding 5% and reaching its highest level since November - following Jerome Powell's statements.
- **Eurozone** According to Christine Lagarde, the ECB would be prepared to cut interest rates if inflation continued to fall. With the disinflation process well advanced, it is likely that the ECB will precede the Fed in easing monetary policy measures.
- **UK** The gradual slowdown in inflation continued in the UK. The annual consumer price index fell in March for the second consecutive month, from 3.4% to 3.2%, which was higher than analysts' expectations (3.1), but reached its lowest level since September 2021.

Statements by Fed Chairman **Jerome Powell** have pushed Treasury yields, already on the rise, to their highest level since November. According to the CME Group's Fed Watch tool, the odds of an interest rate cut in June following his comments, the latest retail sales data and inflation are 16.4%, compared with 56.1% a week ago.

Number of the week

3,2%

This is the rate of inflation in the UK at the end of March. Down from 3.4% in February

Jerome Powell

FED Chairman **Jerome Powell** has said that the US economy, while otherwise solid, has not seen inflation return to the central bank's target, making it even more unlikely that interest rates will be cut in the near future.

"The latest data shows solid growth and continued strength in the labour market, but also a lack of progress towards returning to our 2% inflation target.

They have clearly not given us any greater confidence and, on the contrary, indicate that it will probably take longer than expected to reach this stage.
That said, we believe that the policy is well positioned to deal with the risks we face.

We can maintain the current level of rates for as long as necessary".

Christine Lagarde: "Ready to lower rates

ECB President **Christine Lagarde** has stated that the governors are "observing a disinflation process" which is currently in line with expectations and should bring consumer price growth back to a sustainable 2% by mid-2025.

"If we do not have a major shock in the evolution of the situation, we are heading towards a time when we will have to moderate the restrictive monetary policy that we have put in place".

This should happen "within a reasonably short period of time", said Ms Lagarde, without giving any further details.

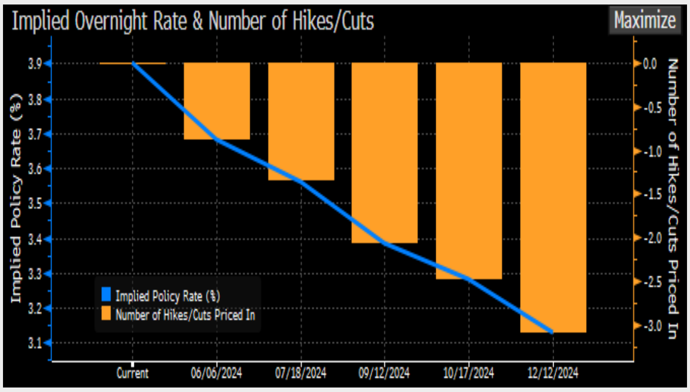
These remarks come just five days after the ECB reinforced the possibility of an interest rate cut in June, due to falling inflation.

This would be the first drop since the authorities raised borrowing costs to combat runaway prices and, given that the US economy is still in full swing, it is likely to precede any such move by the Fed.

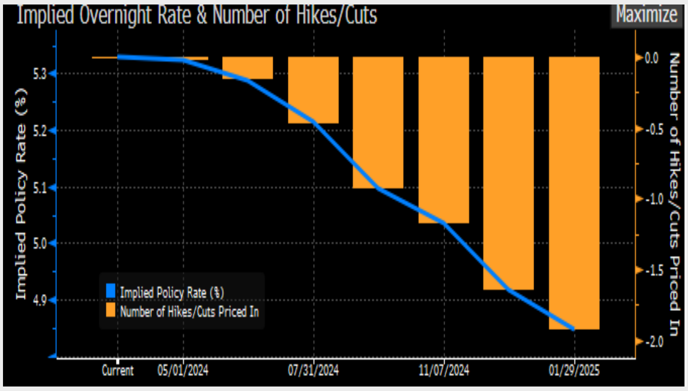
On the other hand, growth in the eurozone, which comprises 20 countries, has been virtually at a standstill for over a year, which has made it possible to control the surge in prices that followed Russia's invasion of Ukraine.

> *If there are no major shocks in the evolution of the situation, we are heading for a time when we will have to moderate the restrictive monetary policy we have put in place*
>
> *Christine Lagarde, President ECB*

ECB



FED



Source: Bloomberg 17/04/24

With a week to go before the **ECB**'s final monetary policy meeting, the chances of seeing the first interest rate cut at the next meeting on 6 June remain stable.

The probability is now around 87%. According to experts, the ECB should approve three 25bp rate cuts between now and the end of the year. In line with this forecast, the €STR index should stand at 3.12% in December 2024. More generally, the pace of rate cuts has slowed compared with the forecasts made at the start of the year, when more than 5 cuts were expected before the end of the year.

As for the **Fed**, Jerome Powell's recent statements and the latest data published on the rise in US inflation mean that expectations of a first rate cut at the central bank's June meeting are now virtually nil.

The first rate cut is now scheduled for September 2024, and a total of two are expected between now and January 2025. The current scenario is very different from the forecasts made at the beginning of the year, when up to seven rate cuts were expected.

Y. Stournaras - ECB: time to diverge from the FED

Yannis Stournaras, ECB

According to Governing Council member **Yannis Stournaras**, the ECB should not be afraid to depart from the Fed's "overly cautious" stance on interest rates.

Speaking in Frankfurt after the ECB gave its clearest signal yet that it will begin to end its unprecedented series of rate hikes in June, the Greek official reaffirmed that four rate cuts were possible this year, although investors had reduced their bets on such measures on a global scale.

"It's time to diverge. The situations in the eurozone and the US are completely different. In the US, demand is much stronger, mainly because of the impetus provided by the budget.

This is not the case in Europe. Inflation in the eurozone has been driven mainly by supply, not by demand or wages".

Slow descent of inflation in the UK

Inflation in the UK fell to **3.2%** in March, according to the Office for National Statistics.

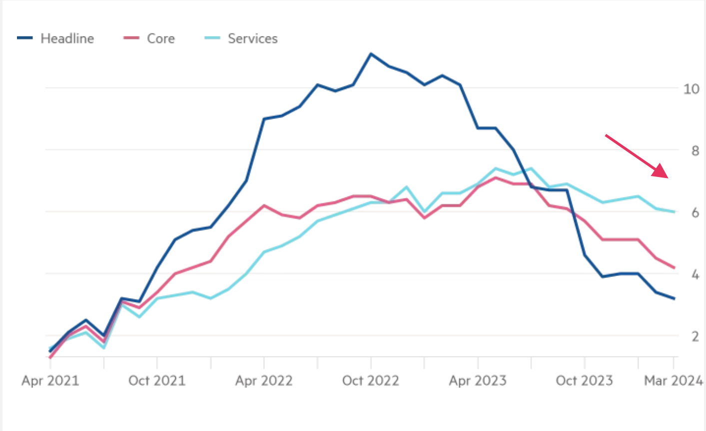
This figure is slightly higher than the 3.1% forecast by economists polled by Reuters, but down on February's 3.4%.

Food prices were the main drag on the nominal rate, said the ONS, while fuel pushed it up.
Core inflation, which excludes energy, food, alcohol and tobacco, came in at 4.2%, against a forecast of 4.1%.

Bank of England Governor **Andrew Bailey** said he saw "clear evidence" that interest rates were falling from their peak of 11.1% in October 2022.

According to the central bank, inflation should briefly fall to its 2% target in the spring before rising slightly. According to analysts, the BOE will cut interest rates twice in 2024 from the current rate of 5.25%, starting in late summer.

Inflation in the United Kingdom



"Our judgement on interest rates is this: how far do we have to go now to have confidence in the disinflation process? "

Andrew Bailey, Governor Bank of England

News

- **US** retail sales up more than expected in March (+1.1% vs. 0.4% expected)
- **China** | Annual GDP at T1 rose to 5.3% from 5.2% over the previous period.
It was expected to be 4.8%.

Agenda

- **26 April** I Decision by the Bank of Japan on interest rates
- **26 April** I Publication of inflation rate Core PCE in the US at the end of March

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