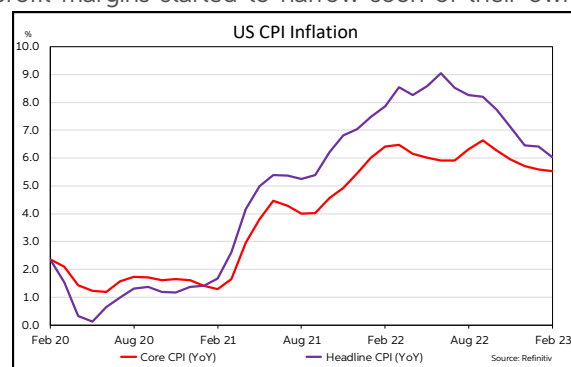


Margin Call

- **March has seen a welcome sharp fall in headline inflation in the Eurozone.** This is likely to be repeated elsewhere as the sharp jump in energy prices following the Russian invasion of Ukraine early last year starts to drop out of annual rates. The Eurozone HICP rate fell to 6.9% in March from 8.5% in February and is now well below the peak level of 10.6% hit last October. Meanwhile, the Irish rate fell from 8.1% to 7.0% in March. US inflation is already well on its way down, with the headline CPI rate declining to 6% in February from a peak of 9.1% last summer. Further big falls in headline inflation rates are store in the coming months. This, though, is the end on the good news story on inflation. When you exclude energy, inflation remains high and sticky. The monthly rise in the Eurozone HICP excluding energy was 1.3% in March, while the annual rate continued to accelerate, reaching 7.9%. Core inflation remains sticky in the US and elsewhere too.
- **Wholesale energy prices have been in marked decline since last summer and are now below the levels that prevailed ahead of the Russian invasion of Ukraine.** So why has a temporary, albeit very large, spike in energy prices generated a persistent inflation problem? Wage growth picked up in response to the surge in inflation, but is still lagging well behind the rise in consumer prices, and is already starting to moderate in economies like the US and UK. Instead, it would appear that a widening of profit margins is the principal factor behind the sharp rise in underlying inflation. The US has seen a surge in corporate profit margins in the last two years to levels that are well above historical norms, according to official data.
- **A recent excellent paper from the ECB (*How tit-for-tat inflation can make everyone poorer*) clearly demonstrates that soaring profit margins are mainly responsible for the marked pick-up in domestic inflation** in the Eurozone over the past year. It shows that profit margins rose at a much faster pace than unit labour costs during 2022, right across the whole economy. It was most pronounced in the agriculture sector, which has resulted in extremely high levels of food price inflation which is now running at 15.5%. However, it was also evident in manufacturing, construction, energy, utilities and personal services. As a result, while increasing profit margins contributed about one third to the broadest measure of inflation in the economy, the GDP deflator, on average since 1999, they accounted for two-thirds in 2022.
- **How have firms being able to do this?** The first reason the ECB concludes is that demand has outpaced supply in many sectors post the pandemic, with pent-up demand unleashed at a time of major disruptions to supply chains and capacity constraints in economies. This allowed firms to expand their profit margins without fear of losing market share. Secondly, rising inputs costs made it easier for firms to mask increasing their profit margins, and pass both on to customers in higher prices. Workers will demand higher wages if this behaviour persists, with the ECB noting the risk of a wage-price spiral developing. This can be expected to be met with a stronger policy response from monetary authorities that would see demand weaken significantly and force margin compression on firms. Thus, it would be better all-round if profit margins started to narrow soon of their own accord, allowing core inflation to fall back.
- **This week, the main release of note will be US CPI inflation data for March.** As mentioned previously, the headline CPI rate has been in marked decline for a number of months, falling to 6% in February, down from 6.4% in January. Meantime, core-CPI has been declining more slowly, edging back to 5.5% in February. The consensus is for the headline rate to ease to 5.2% in March, but the core rate is projected to rise to 5.6%. Elsewhere, a 0.1% increase in retail sales is pencilled in for March. The control group measure, a key core-retail sales indicator, is expected to rise by 0.6%, having increased throughout Q1 so far. Meanwhile, industrial production is expected to have flat-lined again in March. In terms of more timely data, the April reading of the University of Michigan consumer sentiment index is due. On the monetary policy front, the latest Fed FOMC meeting minutes will garner close attention, as investors look for further details regarding the Fed's view on recent turbulence in the US banking sector, and the future path of interest rate hikes.
- **Similarly, the ECB monetary policy meeting account for March will also be of keen interest this week.** The ECB hiked interest rates by 50bps for the second consecutive meeting last time out, and indicated that further monetary policy tightening will be required, if the economy performs in-line with the central bank's macro forecasts. Retail sales and industrial production will also feature in the Eurozone, like in the US. A further modest increase in both indicators is envisaged for February, though there is upside risk to industrial production, following strong German figures for the month.
- **In the UK, the monthly reading of GDP for February is due.** UK data have generally printed ahead of expectations so far in 2023. The BoE has become more positive on the outlook as a result of this, and the significant drop in wholesale energy prices in recent months. A further improvement in output, with GDP rising by 0.2% in the month is forecast in February.



	Interest Rate Forecasts			
	Current	End Q2	End Q3	End Q4
		2023	2023	2023
Fed Funds	4.875	5.125	5.125	4.625
ECB Deposit	3.00	3.50	3.50	3.50
BoE Repo	4.25	4.50	4.50	4.50
BoJ OCR	-0.10	-0.10	-0.10	-0.10
Current Rates Reuters, Forecasts AIB's ERU				

	Exchange Rate Forecasts (Mid-Point of Range)			
	Current	End Q2	End Q3	End Q4
		2023	2023	2023
EUR/USD	1.0920	1.09	1.11	1.13
EUR/GBP	0.8782	0.88	0.88	0.88
EUR/JPY	143.88	140	139	138
GBP/USD	1.2433	1.24	1.26	1.28
USD/JPY	131.77	128	125	122
Current Rates Reuters, Forecasts AIB's ERU				

Date	UK & Irish Time		Release	Previous	Forecast
This Week:	ECB Speakers: BoE Speakers: Bailey (Wed); Pill (Thu); Tenreyro (Thu) Fed Speakers: Williams (Mon); Goolsbee, Harker, Kashkari (Tue); Barkin (Wed) IMF World Economic Outlook (Mon)				
Mon 10th	IRL/ Most EU-20/ UK		Easter Monday (Market Holiday)		
	JPN:	09:30	Economy Watchers Poll (March)	52.0	50.4
Tue 11th	CHINA:	02:30	PPI (March)	(-1.4%)	(-1.7%)
	CHINA:	02:30	CPI (March)	-0.5% (+1.0%)	+0.1% (+0.1%)
	EU-20:	09:30	Sentix Index (April)	-11.1	
	EU-20:	10:00	Retail Sales (February)	+0.3% (-2.3%)	+0.1% (+1.6%)
	US:	11:00	NFIB Business Optimism (March)	90.90	
Wed 12th	US:	13:30	CPI Inflation (March)	+0.4% (+6.0%)	+0.3% (+5.2%)
			- Core	+0.5% (+5.5%)	+0.4% (+5.6%)
	US:	19:00	Fed FOMC Meeting Minutes (21-22nd March)		
Thu 13th	CHINA:	04:00	Trade Balance (March)	+\$116.9bn	+\$91.7bn
			- Exports	(-6.8%)	(+3.1%)
	GER:	07:00	Final HICP Inflation (March)	+1.1% (+7.8%)	+1.1% (+7.8%)
	UK:	07:00	GDP (February)	+0.3% (+0.0%)	+0.2%
			- 3m/3m	+0.0%	+0.0%
	UK:	07:00	Industrial Output (February)	-0.3% (-4.3%)	+0.2% (-3.7%)
			- Manufacturing Output	-0.4% (-5.2%)	+0.3% (-4.7%)
	UK:	07:00	Goods Trade Balance (February)	-£17.9bn	-£18.7bn
	ITA:	09:00	Industrial Output (February)	-0.7% (+1.4%)	-0.2% (-0.2%)
	EU-20:	10:00	Industrial Production (February)	+0.7% (+0.9%)	+0.1% (-0.4%)
	EU-20:	11:30	ECB Monetary Policy Account (15-16th March)		
	IRL:	11:00	CPI Inflation (March)	+1.6% (+8.5%)	+1.0% (+7.5%)
			- Final HICP Inflation	+1.5% (+8.1%)	+0.9% (+7.0%)
	US:	13:30	Initial Jobless Claims (w/e 3rd April)	+228,000	
	US:	13:30	PPI Final Demand (March)	-0.1% (+4.6%)	+0.0% (+3.0%)
			- Ex-Food & Energy	+0.0% (+4.4%)	+0.3% (+4.4%)
Fri 14th	FRA:	07:45	Final HICP (March)	+0.9% (+6.6%)	
	SPA:	08:00	Final HICP (March)	+1.1% (+3.1%)	
	IRL:	11:00	Residential Property Price Index (February)	-0.6% (+6.1%)	+0.0% (+5.5%)
	US:	13:30	Retail Sales (March)	-0.4% (+5.4%)	+0.1% (+%)
			- Ex-Autos	-0.1%	+0.2%
			- Control Group	+0.5%	+0.6%
	US:	13:30	Industrial Production (March)	+0.0% (-0.3%)	+0.0% (-0.5%)
			- Manufacturing Output	+0.1%	
			- Capacity Utilisation	78.0%	78.3%
	US:	15:00	Preliminary Michigan Consumer Sentiment (Apr)	62.0	

◆ Month-on-month changes (year-on-year shown in brackets)

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