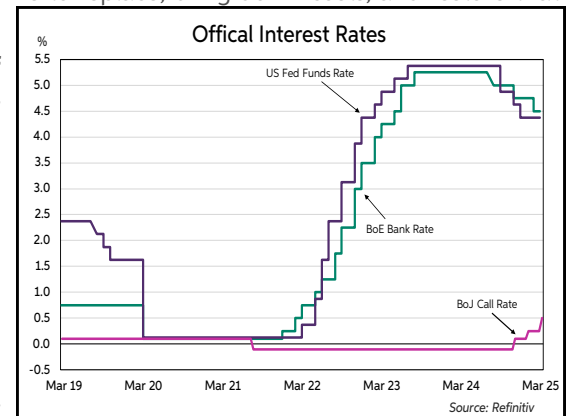


Can Germany deploy its fiscal bazooka?

- With markets now priced in for the impending “fiscal bazooka” from the EU’s joint defence spending initiative and Germany’s infrastructure and defence proposals, the coming week will be pivotal in realising these ambitious plans.** In Germany, a recall of the old parliament has seen a tense debate ahead of the final votes next week on the fundamental reforms to the “debt brake”. With the Greens having the balance of votes to meet the two-thirds majority needed to push through the reforms. The outgoing government party had been holding out to secure a greater share of climate-related spending or even pushing the €500bn infrastructure fund to the next parliament. This raised the risk that the plan would fall as the centrist parties will not hold a two-thirds majority in the new parliament. However, media reports today (Friday 14th March), suggest the Greens will relent and vote through the reforms next week.
- Overall, these developments raise the question of how much of a boost the EU will receive from these policies.** While NATO-aligned countries have been targeting a rise in defence spending to at least 2% of GDP, the domestic defence industries in Europe are concentrated amongst a small number of firms. Indeed, on an output basis, the defence sector in the EU generated €159bn in turnover, or just 0.9% of GDP in 2023, albeit up 29% since 2021. This raises the question of whether a boost in public spending on defence, necessary as it is, will lead to a meaningful increase in GDP. In the short run, this higher spending may leak to imports from the US and other regions with larger defence industries, negating somewhat the boost to EU GDP.
- This brings the debate back to the infrastructure plan in Germany and more broadly in Europe.** With Germany running large trade and current account surpluses over many years, the refrain since the post-GFC period has been for the EU’s largest economy to do more to boost its own domestic output, inducing higher demand for exports from its European peers and thus creating a rising tide of growth across the bloc. On paper the €500bn plan could be a game changer, if spent wisely on growth-enhancing projects. For example, Germany’s manufacturing sector has lost competitiveness versus Chinese exports due to higher energy and input costs. Reducing the reliance on foreign energy imports would be a start, but Germany has been steadily mothballing domestic nuclear power over the past decade, and this will take time to replace, bring down costs, and restore that lost competitiveness.
- As we discussed recently, the EU’s new competitiveness plan (on the back of the Draghi Report) could be as vital to boost long-run growth as the fiscal spending planned at German and EU level.** These many piecemeal, and politically difficult, reforms could in time be a greater catalyst to the private sector by boosting trade within the bloc, completing the capital markets union, and underpinning a recovery in moribund productivity. For now, attention instead remains firmly fixed on the big bazooka.
- Meantime, the monetary policy spotlight this week will be on the US Fed, the Bank of England and the Bank of Japan.** The Fed left rates on hold in January, with officials advocating for a gradual pace of easing this year. Thus, the FOMC is widely expected to leave policy unchanged on Wednesday. However, the Fed’s updated Summary of Economic Projections will garner significant attention, especially the interest rate dotplot. The median projection in December was for just two 25bps rate cuts this year, although the market is currently pricing in closer to three cuts. Remarks from Chair Powell on the economy will also be in focus. **Meantime, it is anticipated that the BoE will decide not to alter rates this week,** despite the MPC voting 7:2 in favour of a 25bps cut in February, with the two dissenters wanting a 50bps reduction. **Similarly, the BoJ is expected to stand pat.** However, pressure is building on the BoJ to hike rates again, as inflation is likely to overshoot its forecast, and given Rengo, Japan’s largest labour union, agreed a 5.5% wage increase for this year, its highest rise in over 30 years.
- On the data front, a busy schedule in the US includes updates on retail sales and industrial production.** Having trended higher throughout the last four months of 2024, retail sales fell sharply by 0.9% in January, amid a broad-based decline in spending. Furthermore, the control group measure (a key core-sales indicator) contracted by 0.8% in the month. However, both metrics are forecast to recover somewhat in February, rising by 0.6% m/m and 0.3% m/m, respectively. Meanwhile, industrial production increased by 0.5% in January, supported by a surge in utilities output due to cold weather and a bounce in Aerospace manufacturing. A 0.3% increase is pencilled in for February.
- In the UK, the unemployment rate is projected to remain at 4.4% in January, while average earnings are set to remain elevated, at +5.9% y/y.** A modest deterioration in UK consumer confidence is expected in March also. In contrast, a slight improvement in Eurozone consumer confidence is anticipated this month.



	Interest Rate Forecasts			
	Current	End Q1	End Q2	End Q3
		2025	2025	2025
Fed Funds	4.375	4.375	4.375	4.125
ECB Deposit	2.50	2.50	2.25	2.00
BoE Repo	4.50	4.50	4.25	4.00
BoJ OCR	0.50	0.50	0.75	0.75

Current Rates Reuters, Forecasts AIB's ERU

	Exchange Rate Forecasts (Mid-Point of Range)			
	Current	End Q1	End Q2	End Q3
		2025	2025	2025
EUR/USD	Retrieving...	1.03	1.04	1.05
EUR/GBP	Retrieving...	0.83	0.83	0.84
EUR/JPY	Retrieving...	155	157	157
GBP/USD	Retrieving...	1.25	1.26	1.26
USD/JPY	Retrieving...	150	150	149

Current Rates Reuters, Forecasts AIB's ERU

Date	UK & Irish Time	Release	Previous	Forecast
This Week:	ECB Speakers:	de Guindos (Wed); Lane (Thu)		
	BoE Speakers:			
	Fed Speakers:	Williams (Fri)		
Mon 17th	IRE:	St. Patrick's Day (Public Holiday)		
	ITA: 09:00	Final HICP Inflation (February)	+0.1% (+1.7%)	+0.1% (+1.7%)
	US: 12:30	Retail Sales (February)	-0.9% (+4.2%)	+0.6% (+4.0%)
		- Ex-Autos	-0.4%	+0.4%
		- Control Group	-0.8%	+0.3%
	US: 14:00	NAHB Homebuilder Sentiment (March)	42.0	43.0
Tue 18th	EU-20: 10:00	Total Trade Balance (March)	+€14.6bn	
		- EuroStat Trade (January)	+€15.5bn	
	GER: 10:00	ZEW Economic Sentiment (March)	26.0	45.0
	US: 12:30	Building Permits (February)	+1.47m / -0.6%	+1.45m / -1.6%
		- Housing Starts	+1.37m / -9.8%	+1.38m / +0.7%
	US: 13:15	Industrial Production (February)	+0.5% (+2.0%)	+0.3% (+1.1%)
		- Manufacturing Output (February)	-0.1%	
		- Capacity Utilisation	77.8%	77.8%
	JPN: 23:50	Machinery Orders (January)	-1.2% (+4.3%)	-0.5% (+6.9%)
	JPN: 23:50	Trade Balance (February)	-¥2,758bn	+¥722.8bn
		- Exports	(+7.2%)	(+12.1%)
Wed 19th	EU-20: 10:00	Final HICP Inflation (February)	+0.2% (+2.4%)	+0.2% (+2.4%)
		- Ex-Food & Energy	+0.5% (+2.6%)	+0.5% (+2.6%)
		- Ex-Food, Energy, Alcohol & Tobacco	+0.6% (+2.6%)	+0.6% (+2.6%)
	EU-20: 10:00	Labour Costs (Q4)	(+4.6%)	
		- Wages	(+4.4%)	
	IRE: 11:00	Residential Property Price Index (January)	+0.5% (+8.7%)	+0.4% (+8.4%)
	US: 18:00	Fed FOMC Policy Announcement		
		- Fed Funds Target Range	4.25-4.50%	4.25-4.50%
	US: 18:30	Fed FOMC Post-Meeting Press Conference		
	JPN:	BoJ Monetary Policy Announcement		
		- BoJ Call Rate	0.50%	0.50%
Thu 20th	UK: 07:00	ILO Unemployment Rate (January)	4.4%	4.4%
	UK: 07:00	Employment Change (January)	+107,000	
	UK: 07:00	Average Earnings (January)	(+6.0%)	(+5.9%)
		- Ex-Bonus	(+5.9%)	(+5.9%)
	UK: 07:00	Claimant Count (February)	+22,000	
	UK: 11:00	CBI Trends - Orders	-28.0	
	UK: 12:00	BoE MPC Policy Announcement		
		- Bank Rate	4.50%	4.50%
	US: 12:30	Initial Jobless Claims (w/e 10th March)	+220,000	+225,000
	US: 12:30	Philly Fed Business Index (March)	18.1	12.0
	US: 14:00	Existing Home Sales (February)	+4.08m / -4.9%	+3.93M / -3.7
	JPN: 23:30	CPI Inflation (February)	+0.5% (+4.0%)	
		- Core CPI	(+3.2%)	(+2.9%)
Fri 21st	UK: 00:01	Gfk Consumer Confidence (March)	-20.0	-21.0
	FRA: 07:45	INSEE Business Climate (March)	96.0	96.0
	EU-20: 15:00	Flash Consumer Confidence (March)	-13.6	-13.0

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