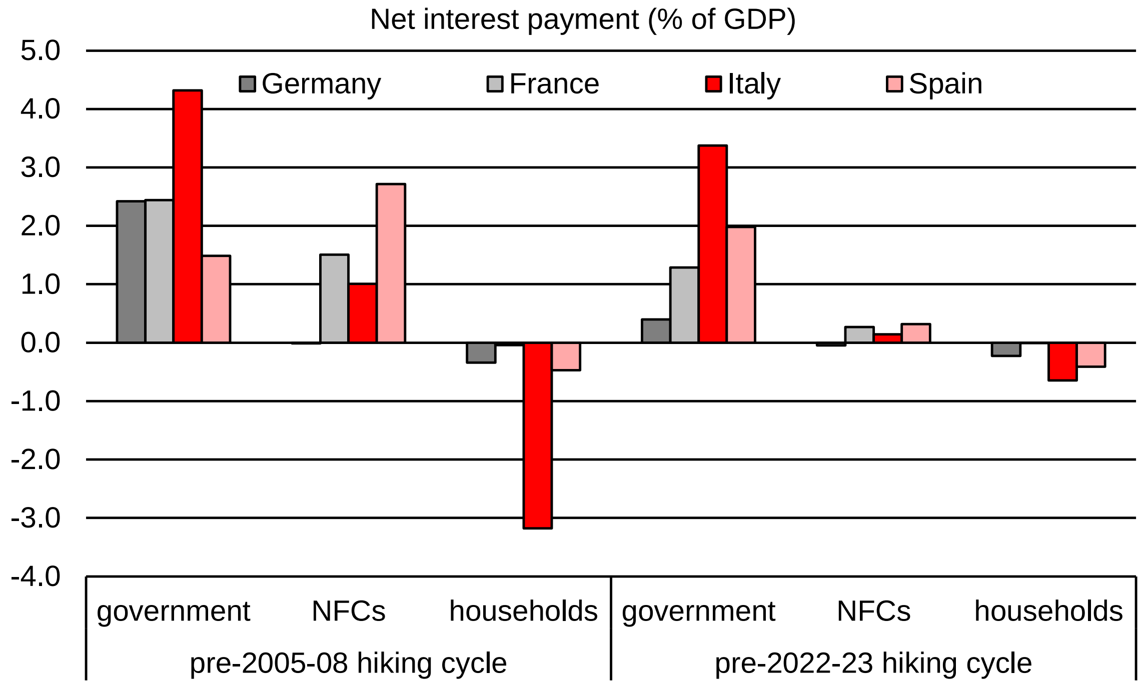
Eurozone: lower vulnerability to higher rates this time, but…



Source: Eurostat, UniCredit Research

- Our *Chart of the Week* compares net interest payments (defined as interest payments minus interest earnings) for the government, non-financial corporations (NFCs) and the household sector in the four largest eurozone countries, before both the ECB's current hiking cycle and that of 2005-2008. Net interest payment reflects both the level of interest rates and the stock of interest-bearing assets and liabilities[1]. For the sake of comparability, we express net payments as a percentage of GDP.
- The chart shows that, in general, eurozone countries are comparatively well positioned to face the current rate shock. In greater detail, net interest payments faced by governments is below that of 2005, thanks to a lower level of interest rates. Spain is the exception here, given that public debt as a share of GDP is now almost 120%, as opposed to 40-45% in 2005. The picture looks uniformly more favorable for the corporate sector, where net interest payments are much lower now than in 2005 (except in Germany, where there is little change). In the household sector, where interest-bearing assets typically exceed liabilities, the situation looks similar to that of 2005 with the exception of Italy. Here, reduced interest income reflects to a large extent the lower share of interest-bearing assets being held as Italian households' portfolios have increasingly moved towards (typically more risky) non-interest-bearing assets.
- While our chart suggests that rate hikes are likely to be manageable, we point out that cumulative monetary tightening this time around is very likely to end up being larger than that of 2005-2008, when the ECB increased its policy rate by a total of 225bp. Moreover, households are under huge pressure due to surging inflation and falling real income, which is especially affecting the most vulnerable part of the population. This will compound the impact on growth from higher rates.

Notes:

1. *We assume that the following financial instruments generate interest: deposits, debt securities and loans. In our analysis, we only consider households' direct holdings of interest-bearing assets, while we do not take into account holdings through investment funds, pension funds and life-insurance schemes.*

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This report was completed and first published on 11 November 2022 at 16:32.

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