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Global Outlook summer 2022

Belfius Strategic Research
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June 28th 2022

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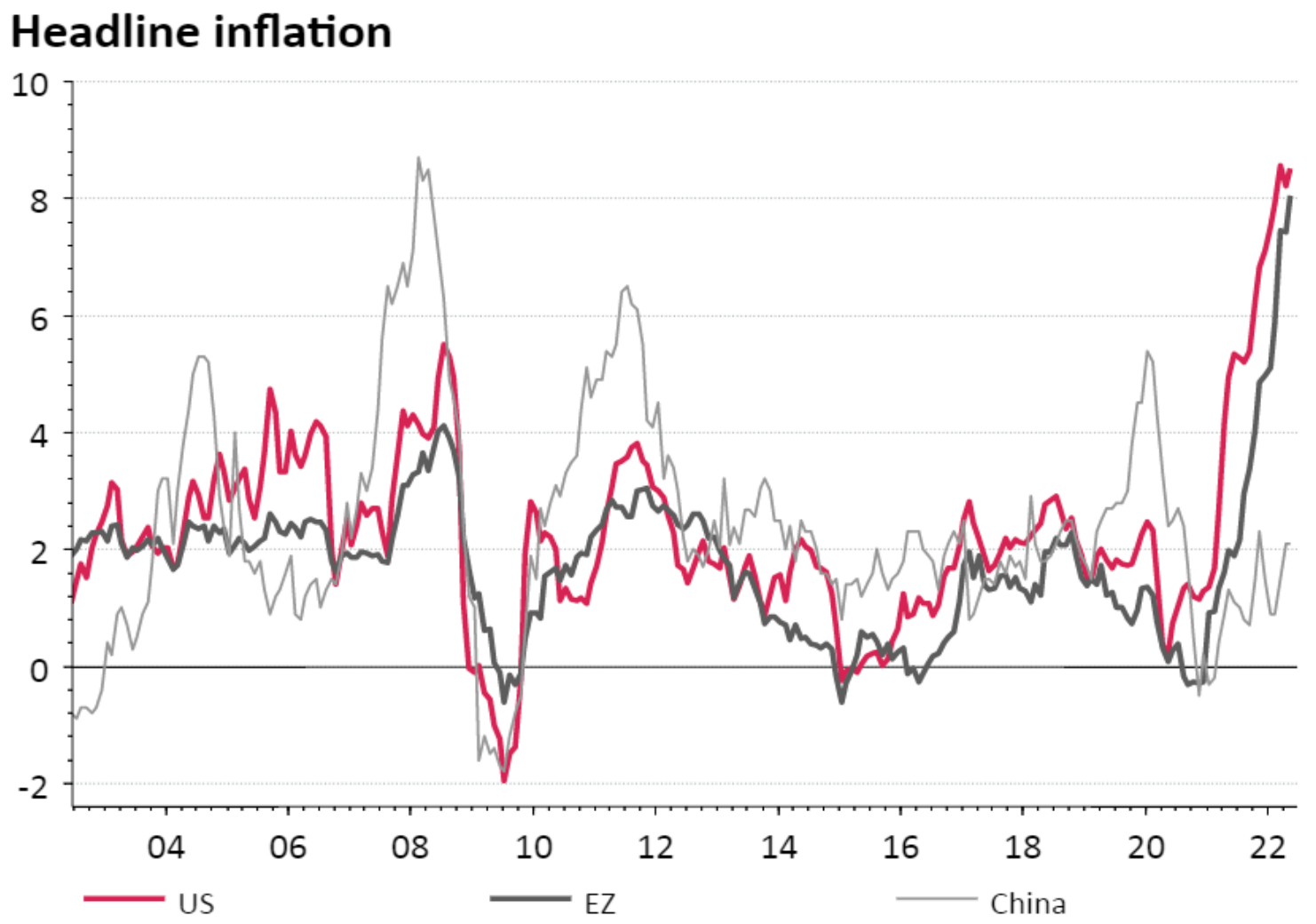
Inflation will stay high and lasts longer in DM.



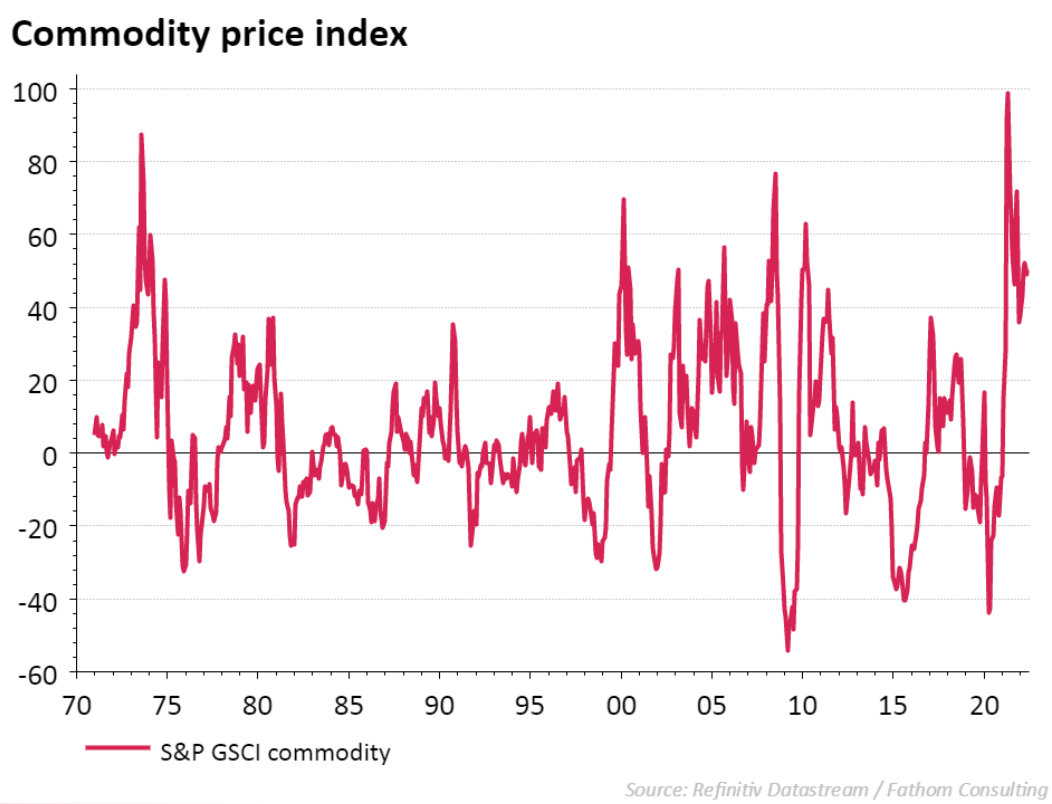
Source: Refinitiv Datastream / Fathom Consulting

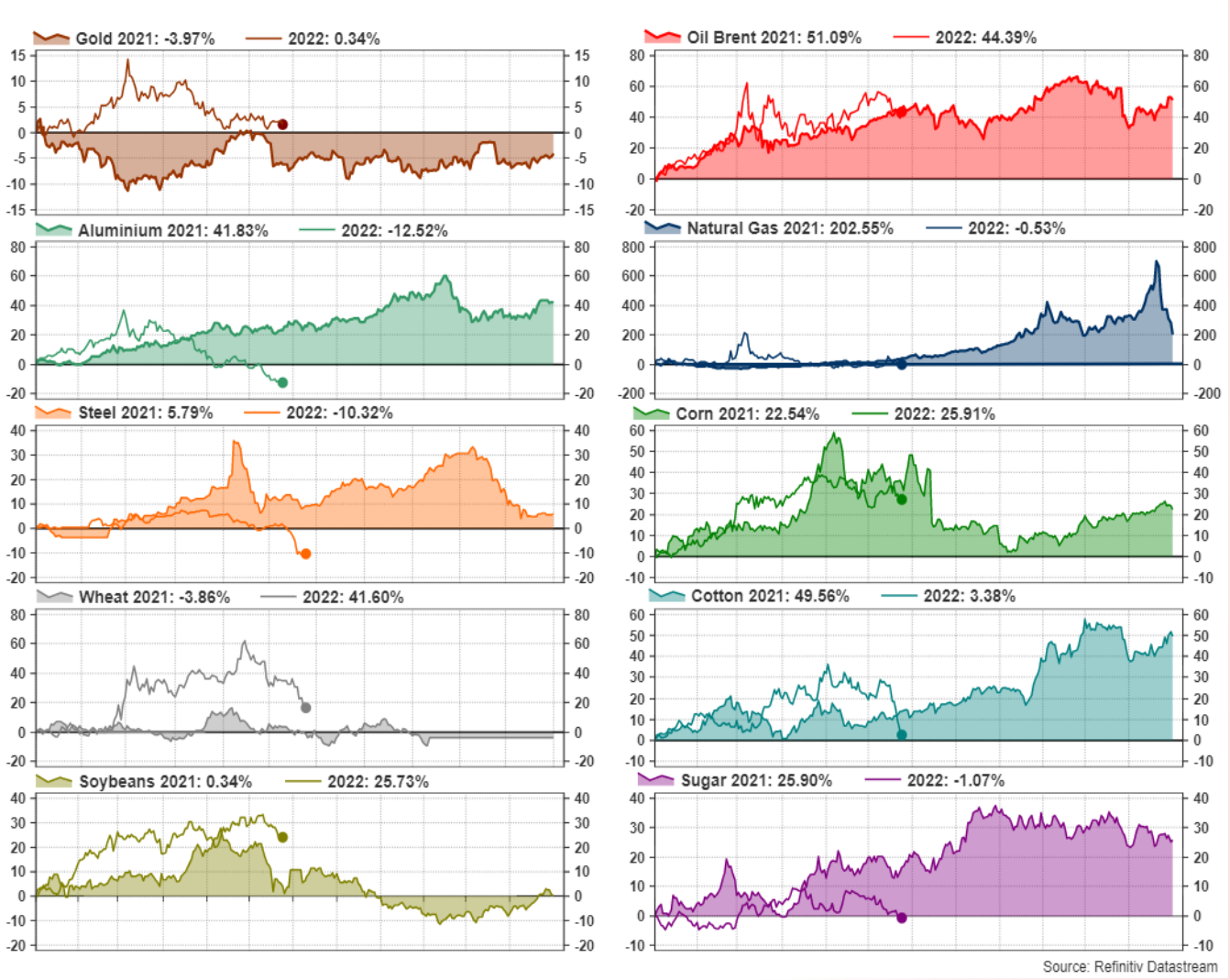
The combination of...

- high consumer demand for durable goods during lockdowns
- global supply chain problems
- soaring commodity prices
- reopening inflation (mainly services)
- labour market scarcity driving wages up in the US
- Russian invasion in Ukraine provokes uncertainty around energy supply and food supply

...fuels inflation. It will remain high for longer than previously thought and will also last longer.

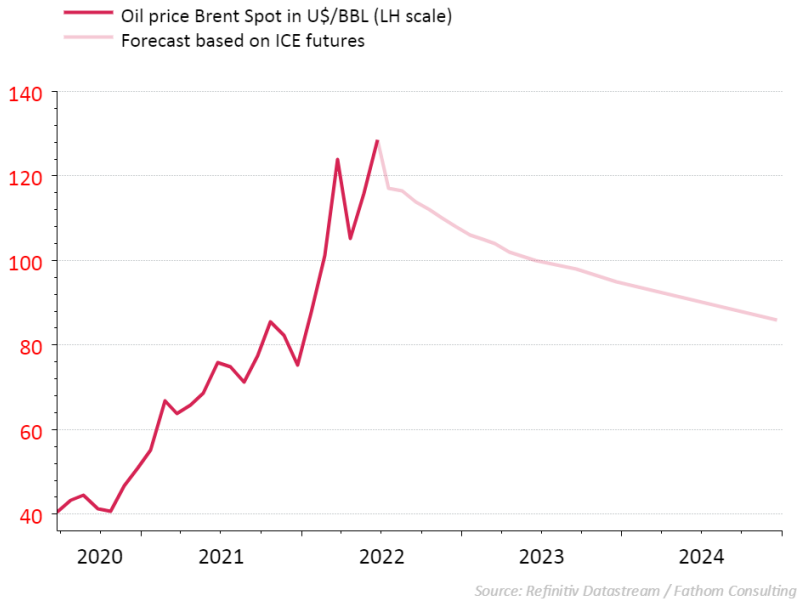
Largest commodity shock since the 1970s.





- Food inflation is expected to rise by 20% this year, before easing in 2023. Wheat prices are forecasted to rise +40% in 2022.
- Aluminium and steel prices are normalizing due to growth slowdown.

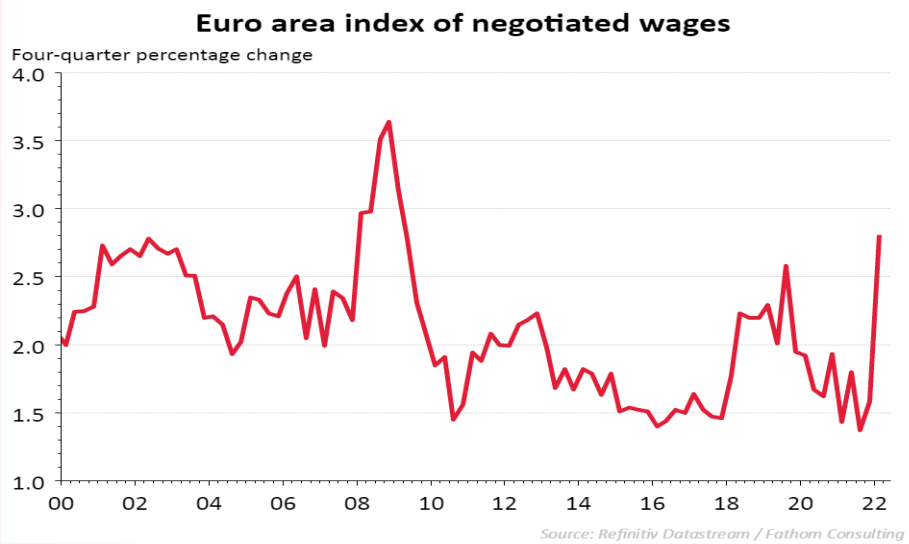
Energy prices expected to stay elevated.



- The price of Brent crude oil is projected to average $112 in 2022 , and $100 in 2023, before reaching a plateau at a higher average level than in 2020-2021.

- Average gas prices in Europe are projected to be more than double in 2022 compared with 2021.
- **Our projections assume that Russia will not cut of its gas exports completely. But a complete halt to Russian gas looks increasingly likely.**
- Industry rationing in Germany would mean reducing activity or shutting down completely, especially in energy intensive companies: chemicals, base metals… with knock-on effects in the supply chain.

Second/third-round effects are coming up in EZ.

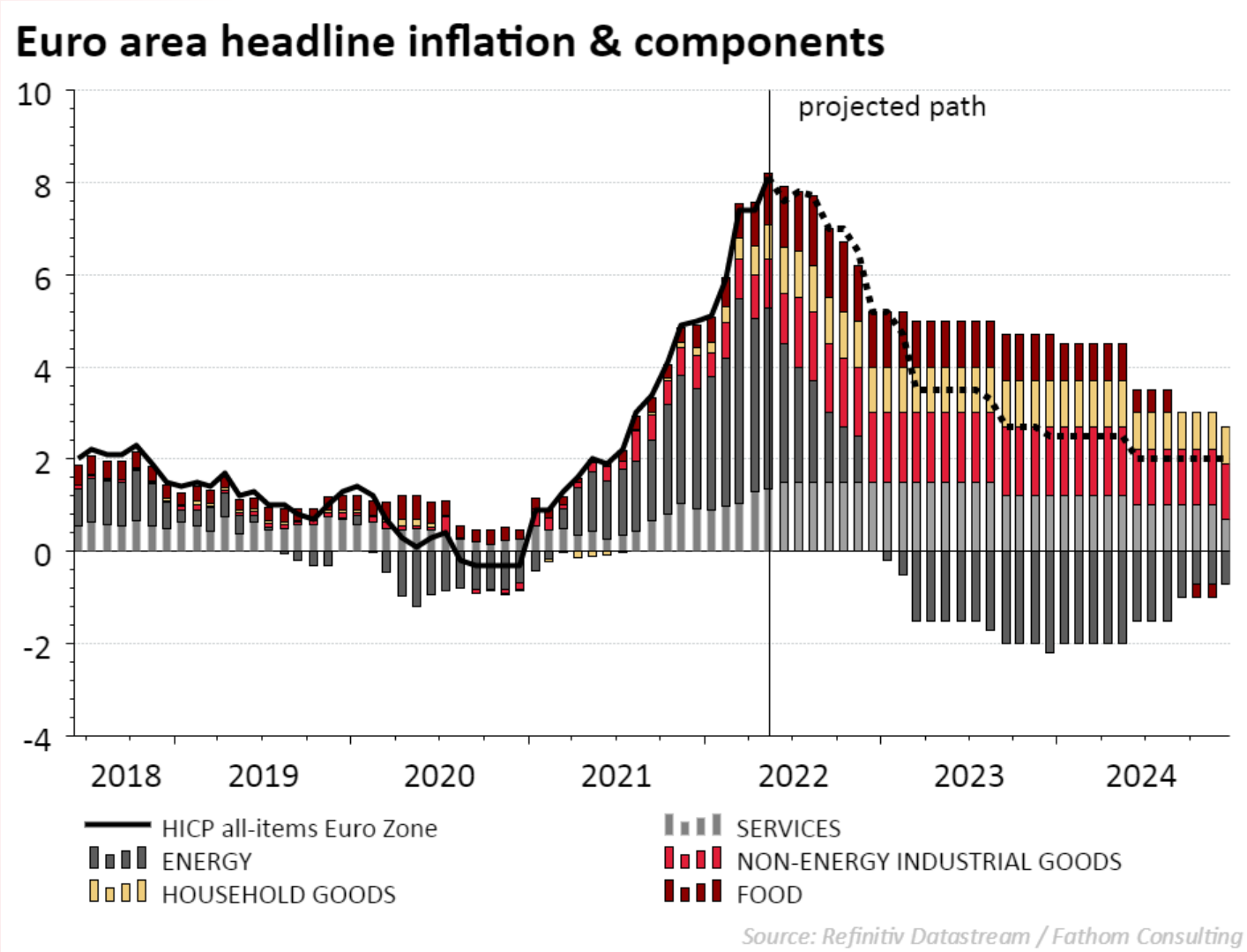


- Wage growth in Europe is expected to be supported by tight labor markets, increases in minimum wages and some effects of compensation for the high rates of inflation.
- In the eurozone, **compensation per employee is projected by the ECB to grow nominally by 4.2% in 2022 and 4.3% in 2023** before declining to 3.7% in 2024.
- These rates are well above the historical average since 1999 (2.2%) and also above the average rates observed before the great financial crisis (2.6%).

EU Business Survey May 2022

- Selling price expectations rose to a new all-time high in retail trade.
- In all other surveyed sectors, price expectations saw the first significant decrease since December (industry/construction) or August (services) of last year.

However… inflation is to come down next year.

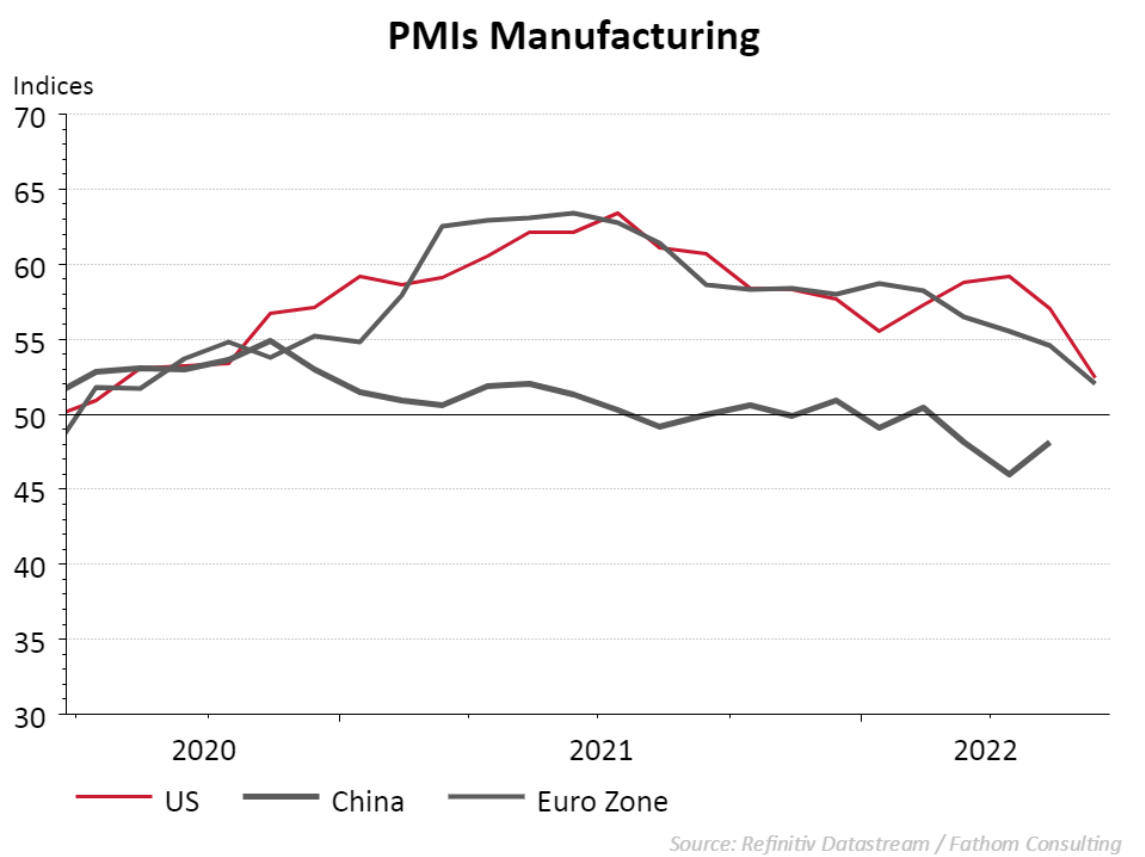


- Based on the energy futures, energy price inflation in the HICP basket should fall to zero in early 2023 and contribute negatively to overall inflation in 2023-2024.
- Food inflation is expected to pick up in the remainder of 2022 and is set to support overall inflation in 2023.
- **Core inflation is expected to average 3.9% in 2023 as wage growth accelerates and pushes up prices in services, industrial and consumer goods.**
- **Because of the anticipated negative contribution of energy prices, overall HICP inflation is projected to average 3,5% in 2023 and 2,2% in 2024.**

Our base case does not assume a recession, but downside risks are mounting.

Argument no. 1:

Manufacturing activity to keep growing in US and EZ.



Manufacturing business surveys in US and EU still point to growing activity.

Chinese manufacturing confidence still in negative territory but showing improvement after severe zero covid policy.

China and EM might take the lead in the recovery of H2 2022 thanks to fiscal and monetary measures.

China announced 33 measures intensifying efforts to boost economic growth : business, investment, consumption, food and energy security and supply chain stabilisation.

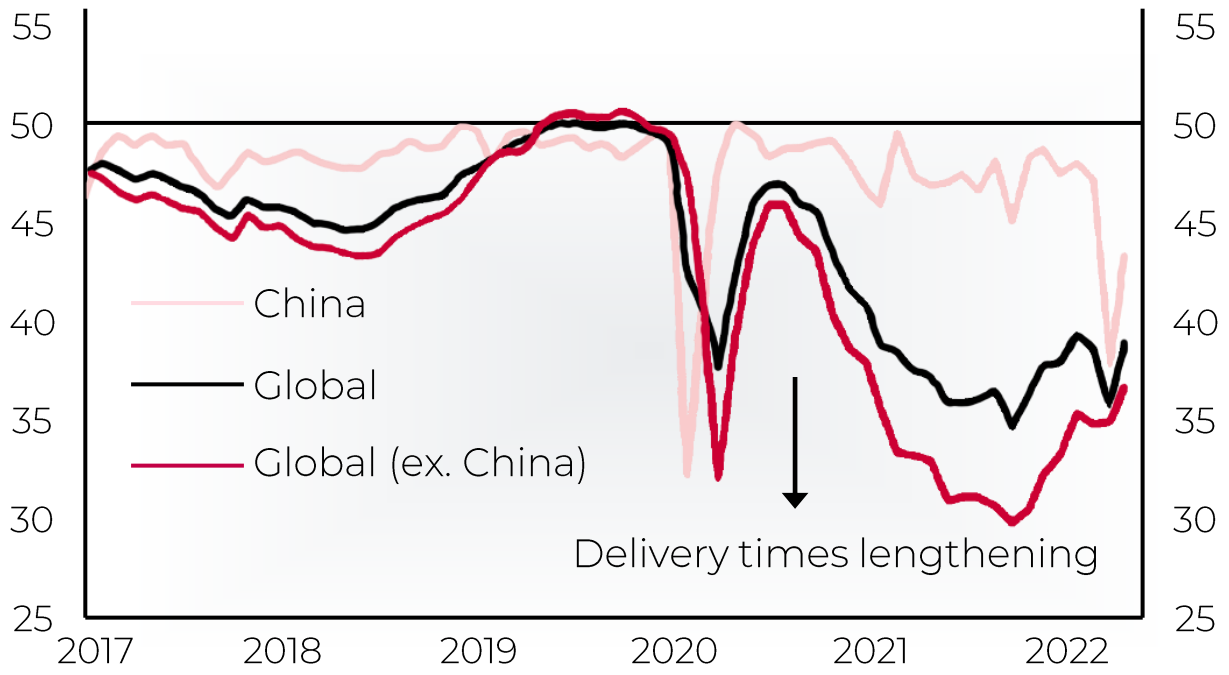
 Bron: Eikon Refinitiv

Our base case does not assume a recession, but downside risks are mounting.

Argument nr. 2:

Global manufacturing industry. PMI delivery times and stock of finished products.

Supply chain stress is easing.



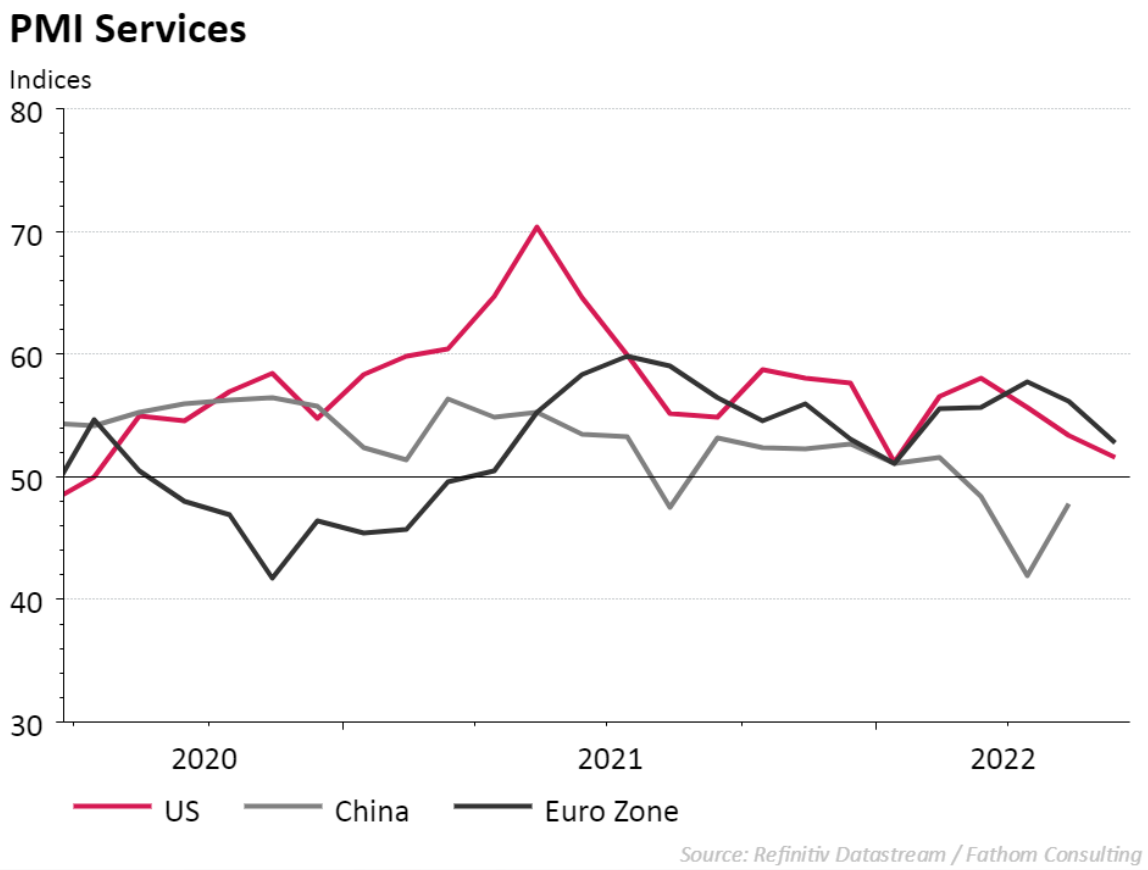
Shipping costs are falling but it is too early to celebrate this as congestion lingers.

Supply chain disruptions might hold on till the end of 2023.

 Bron: Capital Economics

Our base case does not assume a recession, but downside risks are mounting.

Argument nr. 3:
Service sectors prooving resilient in US and EZ, and improving in China.

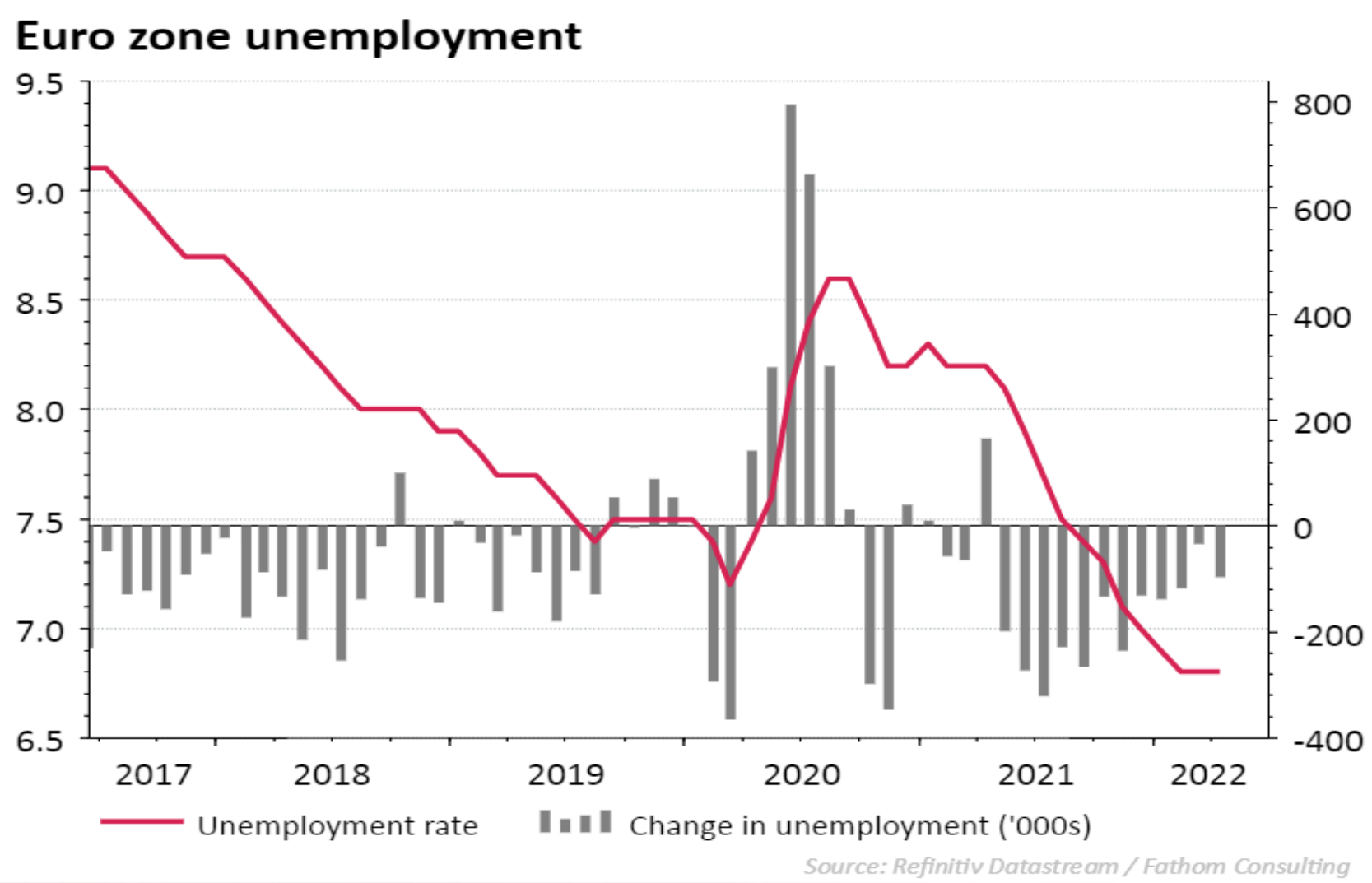


Business confidence in service sectors still point to expansion in the US and EZ.

China has suffered from harsh lockdowns, experiences higher unemployment, fewer new businesses and a weak domestic demand.

 Bron: Eikon Refinitiv

EZ: Tight labour market and higher participation rate should support consumption.



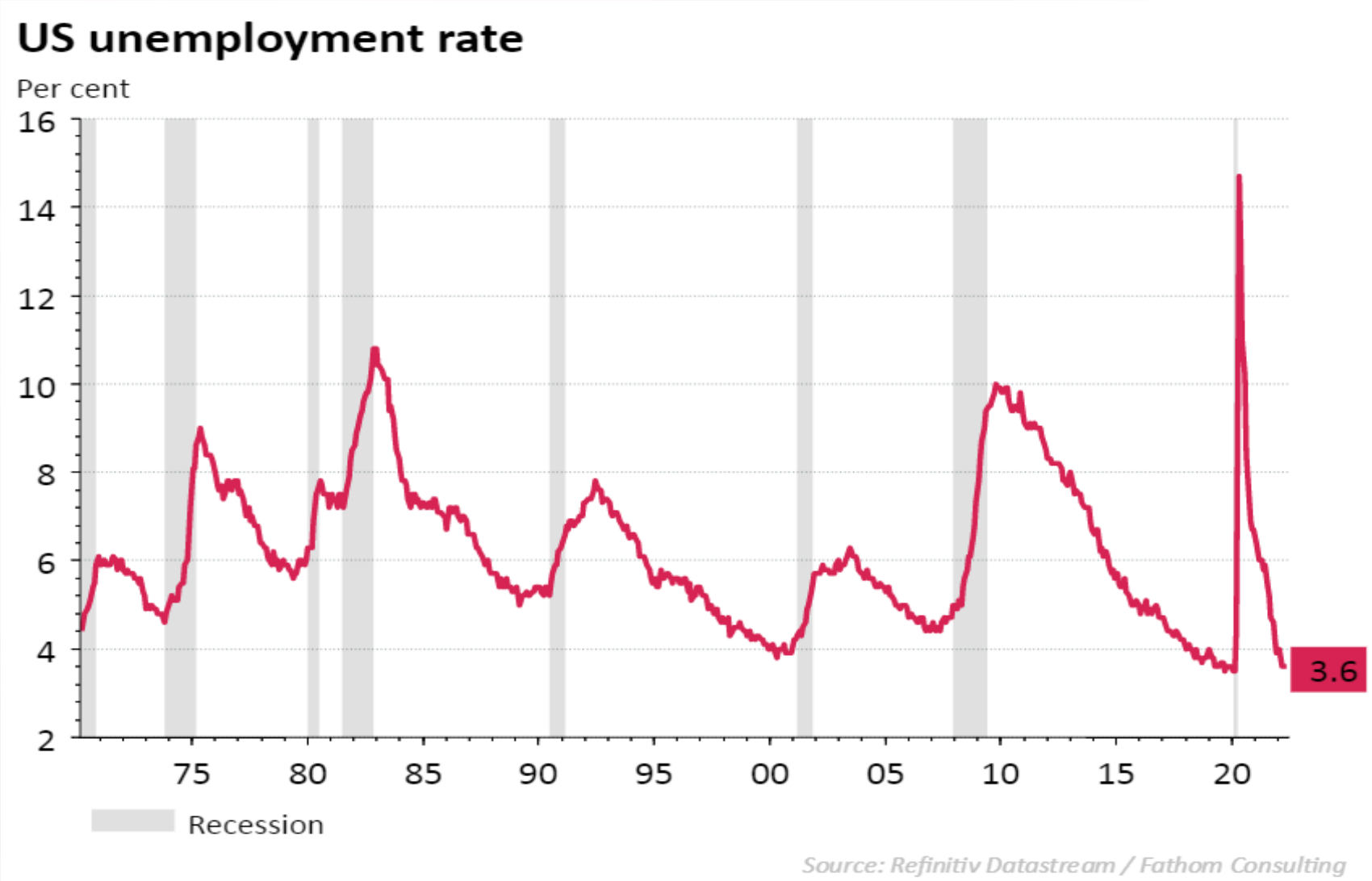
Although the excess savings accumulated during Covid are almost completely reduced in the meantime.

But: disposable income higher than pre-Covid because companies intend to continue hiring.

Demand for labour is stronger than pre-Covid due to higher public employment.

We expect unemployment to drop a bit more in years to come.

US: Labour market to be cooled down by monetary policy.



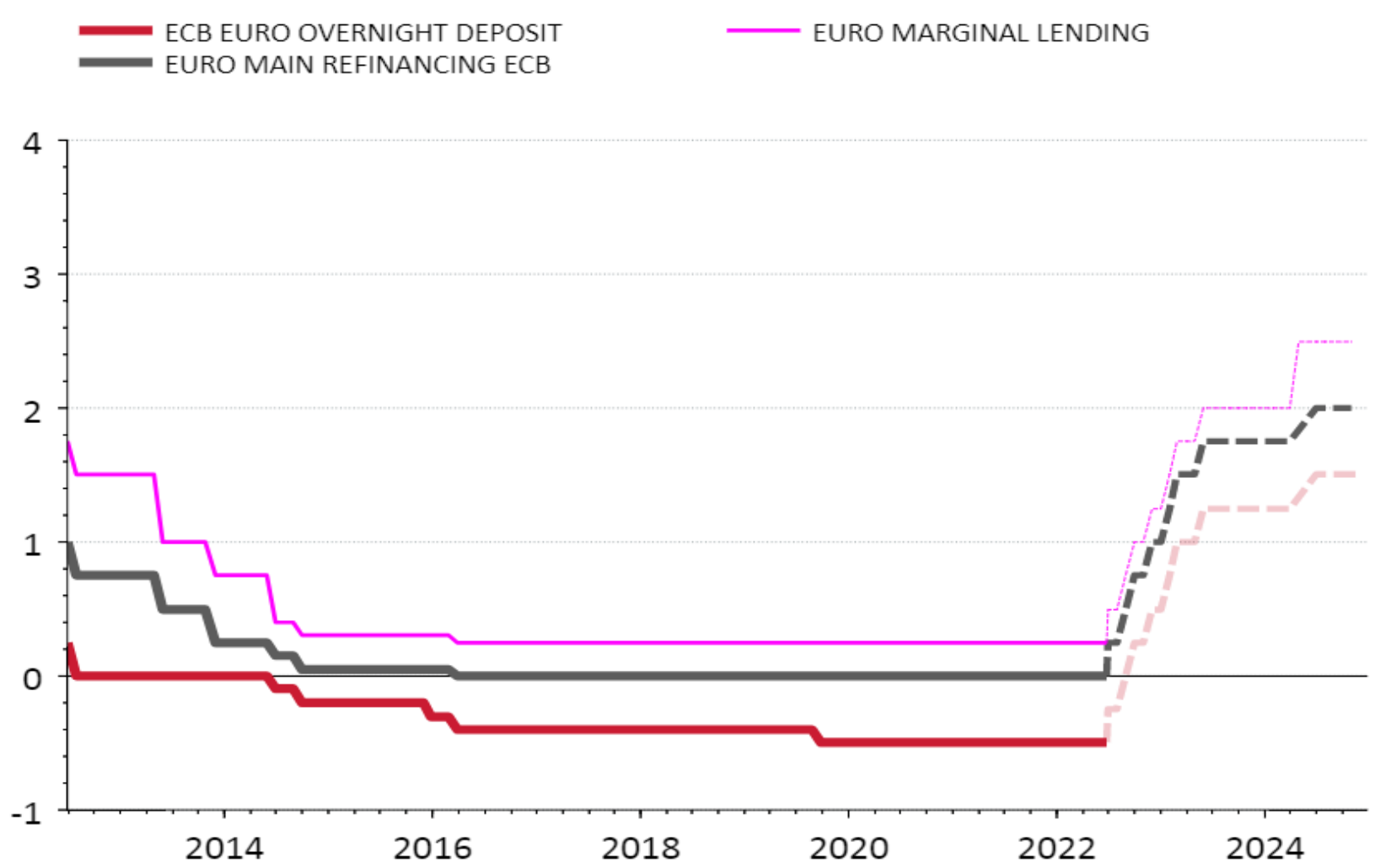
US companies prooved resilient with high profit margins.

But higher hourly labour costs are compressing margins.

Restrictive central bank policy and tightening financial conditions will weigh on consumer demand and are guiding to a higher unemployment rate later this year.

Ultimately this will lead to softer demand driven inflation.

ECB will start tightening in July.



Source: Refinitiv Datastream / Fathom Consulting (updated on 09/06/2022)

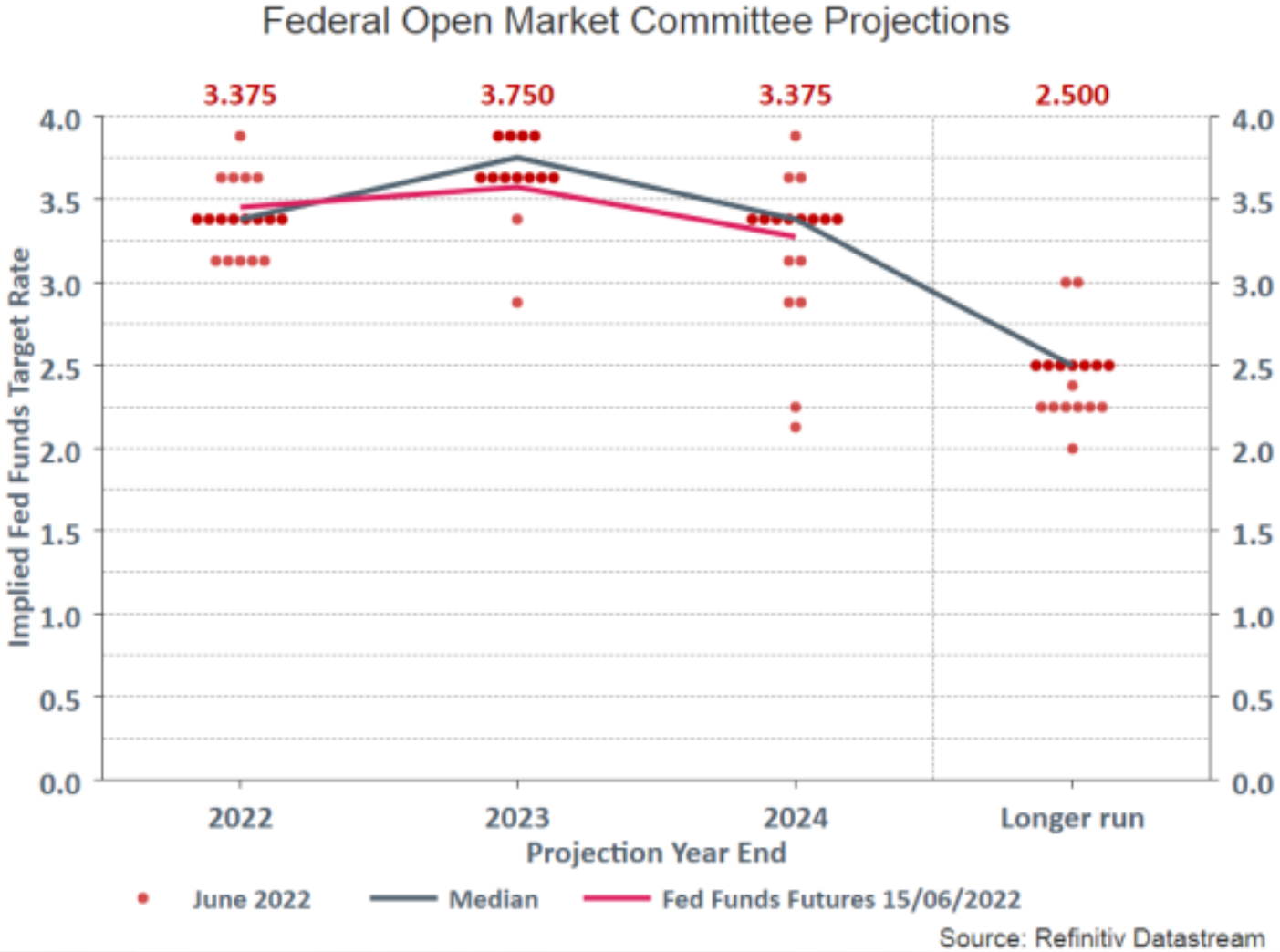
ECB will raise deposit rate by 25 bps in July and 25 or 50 bps in September.

The market discounts a bit less than 175 bps increase in rates by the end of the year.

The central bank experiences a heavy dilemma. On the one hand it wants to fight inflation, but this puts pressure on the spreads of peripheral countries like Italy.

Spread fighting tool to be installed after the end of net asset purchases.

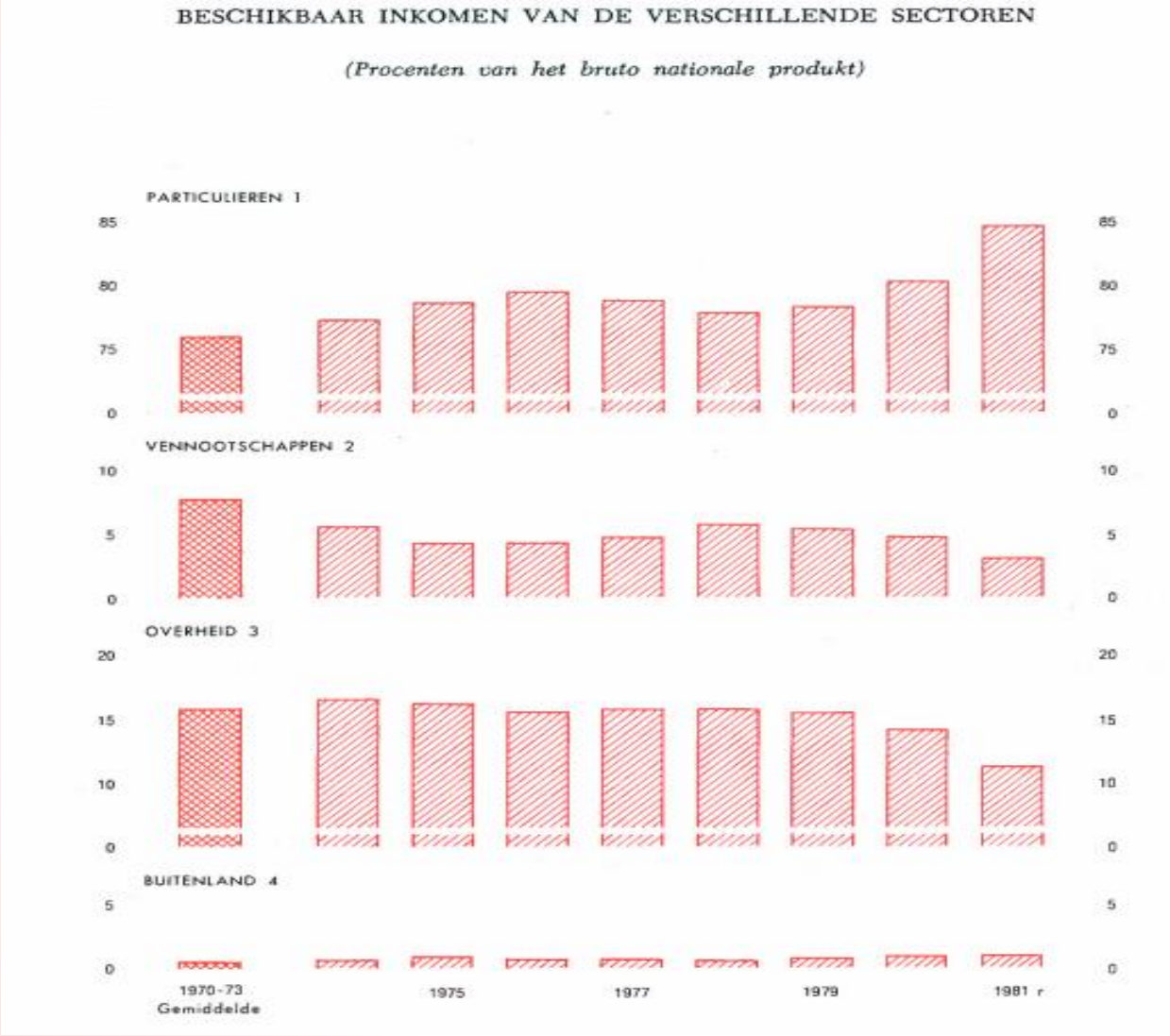
FED more decisive to tame inflation.



The median dot plot expects an additional 175 bpt rate hike by the end of the year

Risk: a brutal, faster-than-anticipated rate tightening might jeopardize a soft landing.

What about Belgium?
Employers, government AND consumers need to share the burden.



In the 70's Belgian companies experienced full blown wage indexation.

Consumers were protected, while companies disappeared and government payed the bill.

Automatic wage indexation needs to be monitored carefully.

Year report NBB 1981

Economic forecasts June 2022

	GDP projections (%yoy)			HICP projections (%yoy)		
	2021	2022	2023	2021	2022	2023
Belgium	6,1	2,2	1,6	3,2	8,3	3,6
Eurozone	5,4	2,8	1,8	2,6	7,3	3,3
UK	7,4	3,5	1,2	2,4	8,0	4,3
US	5,7	2,4	1,8	4,7	7,2	3,0
China	8,1	3,7	5,2	1,2	2,3	2,0

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