Perspectives
Economics

August 2022

Key messages

- Eurozone: Measures to address the gas crisis and ongoing uncertainty are likely to stall GDP growth
- US and UK: solid figures and record inflation are forcing central banks to put on the brakes
- China's real estate sector is worse than expected; infrastructure as a new growth driver

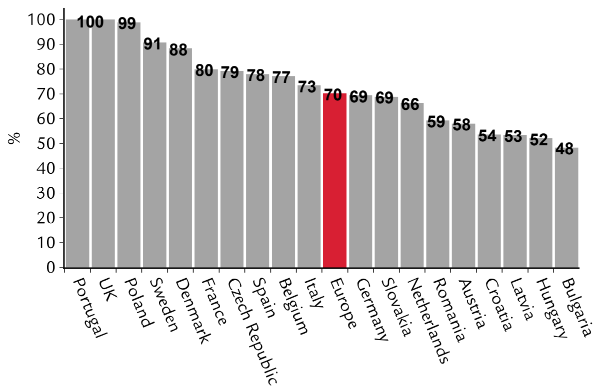
Comparison of forecasts

	2022 GDP growth		2023 GDP growth		2022 inflation		2023 inflation	
	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus
US	2.0% ↓	2.1% ↓	0.8% ↓	1.0% ↓	8.3%	7.9% ↑	3.8%	3.7% ↑
Eurozone	2.7% ↓	2.7% ↓	1.1% ↓	1.4% ↓	7.7% ↑	7.5% ↑	3.4% ↑	3.7% ↑
Germany	1.6% ↓	1.6% ↓	1.0% ↓	1.6% ↓	7.2% ↑	7.2% ↑	3.7% ↑	3.6% ↑
France	2.4% ↓	2.3% ↓	1.2% ↓	1.3% ↓	5.2% ↑	5.3% ↑	2.9% ↑	3.1% ↑
United Kingdom	3.5%	3.3% ↓	0.1% ↓	0.5% ↓	8.6% ↑	8.6% ↑	5.3% ↑	5.6% ↑
Switzerland	2.5%	2.5%	1.2%	1.5% ↓	2.6% ↑	2.6% ↑	1.5% ↑	1.4% ↑
Japan	1.3% ↓	1.6% ↓	1.6%	1.7% ↓	2.0%	2.0% ↑	1.2% ↑	1.3% ↑
China	3.5% ↓	4.2% ↓	5.3% ↑	5.4% ↑	2.3%	2.2%	2.0%	2.3%

Arrows indicate change from previous month
Source: Consensus Economics Inc. London, 11 July 2022

Chart of the month

Gas storage: Level in %



Source: Macrobond, GIE, Swiss Life Asset Managers

Everyone is currently talking about the filling levels of the gas storage tanks. But be careful with the interpretation: the UK has full gas storage facilities, but these are vanishingly small compared to consumption, while Austria's half-empty gas storage facilities cover half of the country's annual consumption. Throughout Europe, countries are on track to reach the 80% level required by the European Commission on 1 November. According to experts, this should be enough even in the event of a Russian gas supply stop this winter (with accompanying measures). In this worst-case scenario, however, the question of how to replenish the storage facilities for the winter of 2023/24 remains open – and has hardly been discussed so far.

US
Waiting for the recession

GDP growth	
Swiss Life Asset Managers	Consensus
2022: 2.0%	2022: 2.1%
2023: 0.8%	2023: 1.0%

Economists and financial markets are largely in agreement: the recession in the US is coming. The debate revolves mainly around the question of when it arrives and how harsh it is. We would reject the idea, sometimes expressed, that the US is already in recession. Figures from the labour market and industry are still too robust for that, and private consumption even increased slightly in real terms in the first half of the year. However, we are already seeing recessionary tendencies in the US housing market. The turnaround in interest rates was very quickly reflected in higher mortgage rates, and transactions in existing properties plummeted by 16% in the first half of the year. Interestingly, the positive trend in house prices continues unabated, as shown by the much-noticed Case-Shiller House Price Index (+8% H1) and the owner's equivalent rent in the consumer price index (+3% H1). The imputed rental value, which is based on a survey of homeowners, has recently gained momentum, arguing against an imminent recession (this component is typically very sensitive to recession fears). We still consider a mild recession next year to be the most likely scenario.

Inflation	
Swiss Life Asset Managers	Consensus
2022: 8.3%	2022: 7.9%
2023: 3.8%	2023: 3.7%

Inflation in the US remains stubborn. It rose from 8.6% to 9.1% in June, driven by higher energy prices. Core inflation fell less than expected (from 6.0% to 5.9%), and is continuing to show a broadening of inflationary pressure. Notable in June were significant price increases in rents (7.2% weighting in the basket) and in owner's equivalent rent of primary residence (23.5%). These components recorded the strongest monthly price jump since 1986 and 1990 respectively.

Eurozone
ECB comes out of the shadows

GDP growth	
Swiss Life Asset Managers	Consensus
2022: 2.7%	2022: 2.7%
2023: 1.1%	2023: 1.4%

Ten years after Mario Draghi's promise that the European Central Bank (ECB) would do everything it takes to ensure the continuation of the monetary union, he and the solidarity among eurozone member states are once again playing a key role in the European drama. The ECB has yielded to market pressure by announcing an interest rate hike of 50 basis points. At the same time, it launched a new tool to avoid, if necessary, the feared fragmentation of financial markets within the eurozone. Despite the ECB's concession, Mario Draghi had to give up his new role as Italy's prime minister and clear the way for new elections. According to investor surveys carried out by Sentix, the risk of Italy's exit from the euro is currently higher than at the height of the debt crisis in 2012. But Europe's solidarity is not only being strained in the context of monetary union. Recently, joint efforts have also been called for to achieve rapid independence on Russian natural gas. Both the short-term growth outlook and the inflation forecast for the Eurozone depend on the success of these efforts.

Inflation	
Swiss Life Asset Managers	Consensus
2022: 7.7%	2022: 7.5%
2023: 3.4%	2023: 3.7%

Our inflation forecasts for 2022 and 2023 were again revised upwards. This also applies to the consensus forecasts. We expect the inflation rate to rise further to 8.9% by September 2022. If we exclude the risk scenario of a collapse of energy supply next winter, a decline in inflation dynamics is to be assumed afterwards. In our base scenario, the inflation rate will fall back towards 2% by the end of 2023.

Germany
On the brink of recession

GDP growth	
Swiss Life Asset Managers	Consensus
2022: 1.6%	2022: 1.6%
2023: 1.0%	2023: 1.6%

Germany's economy is exposed to strong headwinds at the beginning of the second half of 2022. Stubborn inflation, concerns about energy supply next winter and rising finance charges are making a recession increasingly likely. According to the ifo institute, the magnitude of cancellations in the construction sector in June reached the level of the coronavirus crisis. These developments have a negative impact on consumer confidence: despite the persistently low unemployment rate, consumer sentiment remains at a record low since the survey began in 2005, according to GfK. Obviously, neither the subprime crisis, Europe's debt crisis or the pandemic worried German consumers anywhere near as much as the current geopolitical situation. The situation in Germany's industry is particularly depressed: According to preliminary data for the July Purchasing Managers' Index (PMI), order intake fell further. At the same time, a build-up of inventories suggests that industrial production is likely to decline in the coming months. The services sector PMI also fell below the 50-point growth threshold in July.

Inflation	
Swiss Life Asset Managers	Consensus
2022: 7.2%	2022: 7.2%
2023: 3.7%	2023: 3.6%

The above-mentioned business surveys suggest further easing of delivery bottlenecks and increasing inventories. On the eve of a possible recession, these are heralds of easing price pressures. The pace at which this becomes visible in consumer prices depends on short-term wage dynamics and, in particular, fossil fuel price developments. Germany's gas supply security over the coming winter thus remains the major unknown in the preparation of an inflation forecast.

France
Less bad than elsewhere

GDP growth	
Swiss Life Asset Managers	Consensus
2022: 2.4%	2022: 2.3%
2023: 1.2%	2023: 1.3%

In the light of current economic uncertainty across Europe, France seems to be in a relatively better position than its two neighbours, Italy and Germany. Compared to Italy, France's government is still able to act despite a lost majority in parliament. In contrast to Germany, French industry's lower dependence on Russian gas provides better protection for the country's manufacturing sector against the risk of energy rationing. Nevertheless, according to preliminary data, the Purchasing Managers' Index (PMI) for manufacturing in France fell below the growth threshold of 50 in July. The economy is supported by strong demand in the services sector. Usually, the current account balance of tourism is positive in the third quarter. In the year before the pandemic, the surplus amounted to around 1% of French gross domestic product. A recession may also become a potential scenario in France due to the rise in the cost of living and higher interest rates. In contrast to its neighbours, however, the French economy remains in a better position, especially since it will use all fiscal room to manoeuvre.

Inflation	
Swiss Life Asset Managers	Consensus
2022: 5.2%	2022: 5.3%
2023: 2.9%	2023: 3.1%

Among the four major participating countries in the monetary union, France stands out with its comparatively low inflation rate. For the time being, a large proportion of administratively fixed prices in the consumer price index are dampening inflationary pressure, as is the lower proportion of energy components. A further comparison also shows that France has suffered less from higher import prices than, for example, Germany. The latest announcement of further fuel price cuts in September and October should reduce inflation pressure noticeably.

United Kingdom
Better than expected

GDP growth	
Swiss Life Asset Managers	Consensus
2022: 3.5%	2022: 3.3%
2023: 0.1%	2023: 0.5%

The signs are bad: political turbulence, interest rate hikes, inflation and the aftermath of Brexit in the form of record traffic jams at the start of the holiday season. Nevertheless, the British economy seems to be defying the odds. Activity and survey data are not exactly rosy, but better than commonly expected. In contrast to the US and continental Europe, the Citi Economic Surprise Index, which compares incoming data with consensus expectations, improved markedly in July. Monthly GDP data for May showed solid growth, driven by manufacturing, construction and healthcare. In July, while Purchasing Managers' Indices (PMI) showed slowing momentum in manufacturing and services, most sub-indicators – with the exception of industrial orders – remained in growth territory and above Eurozone levels. Consequently, the UK is the only country apart from Switzerland that does not require a revision of our 2022 GDP forecast. We continue to anticipate a mild recession in 2023, a consequence of the tighter monetary policy and the weaker global economy. When it comes to gas supply in winter, the main problem is insufficient gas storage capacities. As a result, in addition to its own production and liquefied natural gas (LNG), the UK also depends on and is in competition with continental Europe for continuous pipeline gas flows from Norway.

Inflation	
Swiss Life Asset Managers	Consensus
2022: 8.6%	2022: 8.6%
2023: 5.3%	2023: 5.6%

Gas and electricity prices will remain key inflation drivers in 2022 and 2023. We expect the UK to have the highest average inflation rate among the main developed economies in 2023. Combined with persistently high core inflation (5.8% in June) and recently better-than-expected economic data, the Bank of England could accelerate the tightening course, which in turn increases the risk of recession in 2023.

Switzerland
Before a slowdown

GDP growth	
Swiss Life Asset Managers	Consensus
2022: 2.5%	2022: 2.5%
2023: 1.2%	2023: 1.5%

In contrast to neighbouring Europe, the Swiss economy remained in robust shape up to mid-year. The domestic economy remains supported by high employment and catch-up effects in the services sector. Foreign trade was also strong in the second quarter. Following a setback immediately after the Russian attack on Ukraine, the State Secretariat for Economic Affairs' (SECO) Weekly Economic Activity Indicator (WWA) rose throughout the second quarter. We continue to expect real gross domestic product to grow by 0.6% over the previous quarter. While our growth forecast for the current year does not deviate from the consensus forecast, we remain significantly more cautious with regard to the economic development in 2023. This is despite the fact that the consensus forecast underwent a slight downward revision for two consecutive months. The list of causes for the imminent cooling is long: higher interest rates are hampering construction activity and accelerating the trend towards increasing corporate bankruptcies. The increasing threat of recession in Germany and the US will be felt in the form of lower external demand. As elsewhere, the risk of an electricity shortage is weighing on the outlook over the next 12 months.

Inflation	
Swiss Life Asset Managers	Consensus
2022: 2.6%	2022: 2.6%
2023: 1.5%	2023: 1.4%

The strong franc is already having a dampening effect via a lower risk of imported inflation. In June, the annual rate of change in the producer and import price index remained at 6.9%. A quarter of the Swiss consumer price index consists of import prices, which also include energy products. Therefore, the effect of lower import prices on inflation may be significant. However, price increases in the services sector are still, in some cases substantial.

Japan
Abenomics lives on

GDP growth	
Swiss Life Asset Managers	Consensus
2022: 1.3%	2022: 1.6%
2023: 1.6%	2023: 1.7%

Shortly after the shocking death of former Japanese prime minister Shinzo Abe, his Liberal Democratic Party, along with its coalition partners, won a major victory in the parliamentary elections. Thus, the government of current Prime Minister Fumio Kishida seems secure for the time being. Although Kishida had criticized his predecessor's economic programme – known as Abenomics – as inadequate when he took office, the three cornerstones remain in his agenda: courageous monetary policy, flexible fiscal policy, and a growth strategy that encourages private investment. The Bank of Japan has so far faithfully followed the first principle by being the only major central bank to keep its monetary policy expansionary in July. It revised the economic growth forecast for the 2022 fiscal year from 2.9 to 2.4%, which is still a very optimistic scenario. At the same time, it emphasised the extremely high uncertainties for the Japanese economy, such as the currently record high Covid infection figures and the effects of the war in Ukraine. According to the July Purchasing Managers' Index, both industrial and services remain in growth territory, albeit with much slower momentum. New orders in the industry were below the 50 mark for the first time since September 2021, indicating contraction.

Inflation	
Swiss Life Asset Managers	Consensus
2022: 2.0%	2022: 2.0%
2023: 1.2%	2023: 1.3%

The Bank of Japan continues to view the rise in core inflation in June from 2.1% to 2.2% as temporary. In order to deviate from its expansionary monetary policy, sustained price pressure on wages must first become apparent. The real wage index is still below pandemic peaks and pre-pandemic values have not yet been breached in nominal terms (data available until May).

China
New growth drivers wanted

GDP growth	
Swiss Life Asset Managers	Consensus
2022: 3.5%	2022: 4.2%
2023: 5.3%	2023: 5.4%

China's economy grew significantly slower than expected in the second quarter, prompting us to lower our GDP forecast for 2022 from 4.3% previously to 3.5%. The real estate sector in particular produced some negative surprises. Both real estate investments and residential construction activity declined sharply. Sluggish construction activity has also triggered a wave of mortgage payment refusal as more and more presold housing projects fail to be completed. So far, the scale of the mortgage boycott represents only about 0.01% of total mortgages in China's banking sector. Nevertheless, an increasing number of unfinished housing projects would exacerbate the crisis of confidence and lead to even lower sales volumes. Therefore, the government is intervening and urging banks to increase lending for unfinished projects. In addition, the possibility of real estate buyers not having to service their mortgages on unfinished projects in the meantime is being considered. However, these measures are only intended to slow the downward trend of the sector and not to stimulate its growth. The days in which the real estate sector served as a growth engine for China's economy are numbered. Instead, the country is looking for alternative growth drivers by encouraging investment in infrastructure and manufacturing high-end products.

Inflation	
Swiss Life Asset Managers	Consensus
2022: 2.3%	2022: 2.2%
2023: 2.0%	2023: 2.3%

China's consumer prices rose by 2.5% year-on-year in June, leaving inflation at a moderate level. In particular, core inflation remains low and stood at 1.0% in June (May: 0.9%). This reflects subdued consumer demand due to the uncertain Covid situation and potential lockdowns.

Economic Research

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