

January 2021

Key messages

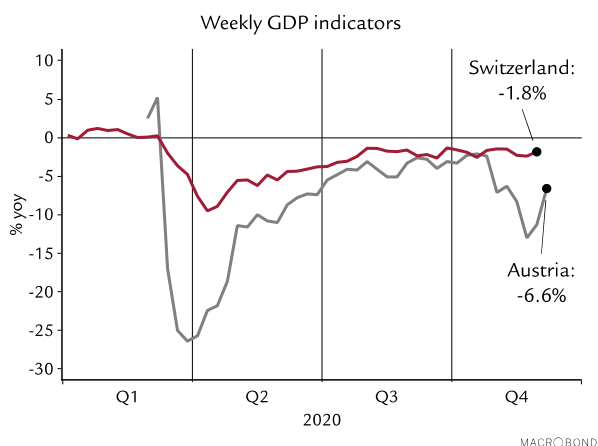
- Renewed lockdowns cause less economic damage as global supply chains remain intact
- Return of price-setting power in European services industries expected
- Switzerland's GDP to recover back to pre-crisis levels in the third quarter 2021

Comparison of forecasts

	2020 GDP growth		2021 GDP growth		2020 inflation rate		2021 inflation rate								
	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus							
USA	-3.6%	-3.6%	↑	3.7%	↑	4.0%	↑	1.2%	1.2%	1.9%	2.0%				
Eurozone	-7.1%	↓	-7.3%	4.5%	↑	4.7%	0.3%	0.3%	1.0%	0.9%					
Germany	-5.3%	↑	-5.4%	↑	3.5%	↑	3.9%	↑	0.4%	↓	0.5%	1.4%	↓	1.4%	↓
France	-8.7%	-9.3%	↑	6.8%	↑	5.9%	0.5%	0.5%	1.1%	0.8%					
UK	-10.8%	↓	-11.1%	↓	5.5%	↑	5.3%	↑	0.9%	↑	0.9%	1.5%	1.6%	↑	
Switzerland	-3.1%	↑	-3.7%	↑	3.2%	↑	3.3%	↓	-0.7%	-0.7%	0.5%	0.2%			
Japan	-5.1%	↓	-5.3%	↑	2.6%	2.6%	↑	0.0%	↓	0.0%	0.0%	0.0%			
China	2.0%	2.1%	↑	8.2%	8.0%	↑	2.5%	↓	2.7%	1.4%	↓	1.7%	↓		

Arrows indicate difference from previous month
Source: Consensus Economics Inc. London, 10 December 2020

Chart of the month



While health authorities are struggling with COVID-19 contact tracing, the economists' "contact tracing" with the real economy is improving as more high frequency data becomes available. The most recent innovation is the State Secretariat for Economic Affairs' (SECO) weekly GDP indicator for Switzerland, which is moving sideways in the fourth quarter. Hence, regional containment measures have slowed but not materially thrown back economic activity, in line with our forecasts. In Austria, where a nationwide lockdown was imposed, the annual GDP growth rate temporarily dropped by around 9 percentage points, indicating a significant, albeit less damaging impact of the second COVID-19 wave on the real economy.

USA

Housing market boom

GDP growth

Swiss Life Asset Managers	Consensus
2020: -3.6 %	2020: -3.6 %
2021: 3.7 %	2021: 4.0 %

COVID-19 infections and deaths are reaching new highs in the US as the second wave has moved towards the more populous coastal regions, notably California. In this state, stay home orders are now in place for most counties. Nevertheless, we expect the renewed wave of restrictions to be far less damaging for the economy than in spring, as businesses are better prepared, supply chains remain intact and the duration of restrictions is more predictable. In October, retail sales and industrial production continued to improve, while housing market transactions reached the highest level since 2005, fuelled by historically low mortgage rates. According to survey indicators, economic conditions remained favourable in November: the composite Purchasing Managers' Indices (PMI) moved to the highest level since March 2015 (58.6 points), while the NAHB survey among home builders even reached record highs. Given the resurgence of the pandemic, these levels are probably not sustainable, and we expect slower economic growth over the winter months. In fact, the disappointing November labour market report might have already been a harbinger of what is in store for the "Corona winter". Political uncertainty is, however, likely to subside further once there is clarity on the Senate seat distribution after the Georgia runoff elections (5 January) and once the new president is inaugurated on 20 January.

Inflation

Swiss Life Asset Managers	Consensus
2020: 1.2 %	2020: 1.2 %
2021: 1.9 %	2021: 2.0 %

Due to negative energy base effects, headline inflation will likely end the year 2020 with a modest 1.0% print. Inflation is, however, set to rebound in the second quarter 2021 as these base effects swing to the positive side. We expect core inflation to move higher in the course of 2021, as the output gap should be reduced significantly once vaccines are available. The recent massive increase in narrow money supply (M1) is adding to potential inflationary pressure in 2021.

Eurozone

Service price inflation in 2021

GDP growth

Swiss Life Asset Managers	Consensus
2020: -7.1 %	2020: -7.3 %
2021: 4.5 %	2021: 4.7 %

Europe is back in lockdown as the region is hit by a severe second wave of the pandemic. Ireland and France responded more quickly to the renewed worsening of the situation, but re-openings of their economies are unlikely to be announced before mid-January. A broad series of newly available high frequency indicators suggest that the economic damage of current containment measures is substantially smaller than in spring (see page 1 for the case of Austria). Nevertheless, based on the information of such timely indicators, we lower our estimate for the final quarter 2020, for which we now assume a GDP contraction by 1.6%. This also results in a slightly lower projection for the full year 2020. Compared to the first wave, there are three major differences to the economic environment now: First, global supply chains remain intact, helping European manufacturers to benefit from recovering demand in Asia and the Americas. Second, monetary policy support and large fiscal stimulus have successfully dampened fears of a credit crisis in the wake of the recession. Finally, the corporate sector is now seeing light at the end of the tunnel, as widespread vaccination of the population over the next twelve months has become a likely scenario. We thus expect economic activity to quickly recover from the current dip and project a return to positive quarterly GDP growth in the first quarter 2021.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.3 %	2020: 0.3 %
2021: 1.0 %	2021: 0.9 %

Inflation data are set to stay volatile throughout 2021. One-off impacts on prices from new taxes to support Europe's climate policies and the removal of earlier VAT tax cuts in Germany by January will result in rising inflation at the start of the year. A likely return to more normal circumstances is an additional reason to expect service sector prices to rise. Consumers are likely to accept higher prices for leisure and transport services, for which pent-up demand is significant.

Germany

Fiscal policy “all-in”

GDP growth

Swiss Life Asset Managers	Consensus
2020: -5.3 %	2020: -5.4 %
2021: 3.5 %	2021: 3.9 %

Our assessment that a renewed lockdown will have a comparably less dramatic impact on economic dynamics is particularly true for Germany. With demand from overseas continuing to rise in the last quarter 2020 and global supply chains remaining intact, manufacturers are far less affected by containment measures compared to spring. Factory orders rose strongly at the start of the quarter and the manufacturing Purchasing Managers' Index (PMI) remained in expansion territory even though large parts of Europe went into renewed lockdowns. Until the first week of December, a truck mileage index showed record-high volumes of goods shipped on German highways for that period of the year. This observation is in sharp contrast with the collapse of transport activity between February and April. The German government's fast and comprehensive fiscal response to the pandemic was one of the most noteworthy European policy events in 2020. The consensus to abandon the black zero and the debt brake – previously sacrosanct budget principles – is still valid during the current economic slowdown, as the country finds itself in a renewed lockdown over the festive season. As the COVID-19 vaccination program is now starting in continental Europe, the ruling coalition has the incentive to maintain its generous fiscal policy stance at all costs until the general election for the Bundestag in September 2021.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.4 %	2020: 0.5 %
2021: 1.4 %	2021: 1.4 %

The new CO2 tax and the reversal of the temporary VAT tax rate cut are expected to result in higher inflation prints going forward. Anecdotal evidence from the tourism industry suggests that holiday package prices are likely to rise sharply in the months ahead. In our base case, we expect annual inflation to exceed 2% in the last quarter 2021.

France

A better managed second wave

GDP growth

Swiss Life Asset Managers	Consensus
2020: -8.7 %	2020: -9.3 %
2021: 6.8 %	2021: 5.9 %

In contrast to its major peers in the Eurozone, France seems to have managed the second wave of the pandemic more decisively so far. The peak of daily new infections was reached in the first half of November and a gradual reopening of the economy in January seems within reach. The economic damage of renewed containment measures is less severe than in spring. Most importantly, manufacturers were able to maintain production as supply chains remained intact. The manufacturing Purchasing Managers' Index continued to hover around the critical 50-points mark throughout the last quarter 2020. We expect GDP to have contracted by 2.6% in the fourth quarter, which is far less than the contraction by 5.9% in the first and by 13.8% in the second quarter of the year. In the short-term, the timing of the service sector reopening will determine the recovery pace. In the medium term, however, the vaccination progress remains the single most important issue to watch. International surveys reveal that there are comparably more vaccine sceptics in France than elsewhere in Europe. A new IMF study shows that social unrest typically increases in the years following a pandemic. In Europe, France is an obvious candidate where such a development might unfold, with protests from the Gilets Jaunes movement likely resurfacing once the country starts to prepare for the presidential election in 2022.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.5 %	2020: 0.5 %
2021: 1.1 %	2021: 0.8 %

Inflation is likely to fall to 0% in December, marking a cyclical trough. We stick to our above-consensus inflation forecast for 2021 as energy prices started to move up lately. Furthermore, companies in the transport and accommodation sectors will be given back some price-setting power when pent-up demand for leisure and entertainment can break free again.

UK

Vaccination to the rescue

GDP growth

Swiss Life Asset Managers	Consensus
2020: -10.8 %	2020: -11.1 %
2021: 5.5 %	2021: 5.3 %

Contrary to the spring wave of COVID-19 infections, the UK reacted early this time, using a strategy of automatic restrictions once certain criteria are met in a region. This approach seems to have worked well, as mortality rates have remained below the EU average. It also means that renewed economic damage is likely in December, as Greater London and other parts of the South are moving again into the most restrictive tier. As the starting point in October was already very low (monthly GDP stood at 92% of its February level), the UK will likely end 2020 as the hardest-hit economy in the developed world, apart maybe from Spain. The approaching end of the Brexit transition period has added to the damage, illustrated by the disappointing recovery of financial services, a sector which performed well in other economies. The services sector, which is a net exporter in the UK, will not be fully covered by the trade agreement that is still in discussion at the time of writing, and many financial activities for EU clients have thus already been shifted to the Continent. On the positive side, the new year will bring clarity on future trade relations, which could unlock investment plans. Also, the UK seems best placed to achieve early herd immunity. Vaccinations have already started, public acceptance of vaccines seems to be generally high and the order book for the three most advanced vaccines amounts to 145 million doses in 2021, which covers more than the entire population.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.9 %	2020: 0.9 %
2021: 1.5 %	2021: 1.6 %

In line with our expectations, headline inflation increased from 0.5% to 0.7% in October. We expect inflation to move somewhat lower until year-end as many service businesses are closed due to the pandemic. The normalisation of activity should lift inflation again in 2021, but the end of the Brexit transition period implies significant uncertainty for the near-term inflation outlook.

Switzerland

Pre-crisis level reached in 2021

GDP growth

Swiss Life Asset Managers	Consensus
2020: -3.1 %	2020: -3.7 %
2021: 3.2 %	2021: 3.3 %

As can be seen on page one, the State Secretariat for Economic Affairs' (SECO) innovative weekly GDP indicator for Switzerland was moving sideways in the fourth quarter until calendar week 49. Although we expect more stringent containment measures to dampen economic dynamics somewhat in the coming weeks, GDP is unlikely to drop by more than 0.5% in the fourth quarter from the previous quarter, as global supply chains remain intact. In the third quarter, the Swiss GDP recovered more strongly than anticipated by the majority of economists. Hence, full-year 2020 GDP forecasts underwent a substantial upward revision last month, and our earlier assessment that Switzerland's economy is getting away from the crisis with a black eye is confirmed by incoming data. SECO stated on December 15 that they expect GDP to contract by 3.3% in 2020 and to grow by 3.2% in 2021 and 3.3% in 2022. In the increasingly likely scenario that vaccination will start in earnest in the first quarter 2021, Switzerland is on track to see its GDP returning to pre-crisis levels already in the third quarter 2021. Nevertheless, high frequency data like the number of jobseekers on online platforms suggest that long-term effects are only about to emerge. We expect the unemployment rate to rise to around 4% in the first half 2021. Also, the number of corporate bankruptcies has started to trend upwards since October, a trend which is expected to continue in the quarters to come.

Inflation

Swiss Life Asset Managers	Consensus
2020: -0.7 %	2020: -0.7 %
2021: 0.5 %	2021: 0.2 %

During almost half of the past ten years, Switzerland was stuck in deflation, i.e. annual changes of the consumer price index in negative territory. We expect the current deflation to continue until March 2021. In November, prices again fell more than what we had expected. We refrain from lowering the forecast for inflation as energy prices have started to rise in the final quarter 2020. Retail heating oil prices are up by 10% so far in December from the previous month.

Japan Sentiment improves

GDP growth

Swiss Life Asset Managers	Consensus
2020: -5.1 %	2020: -5.3 %
2021: 2.6 %	2021: 2.6 %

Asia currently seems to be a world of its own. Even though the pandemic gives a seasonal comeback in Japan and South Korea currently, incidence is at a level Europe last saw back in late July/early August. Other nations in East Asia are even less affected according to official figures. In the wake of the rapid recovery in China, sentiment among Japanese companies has improved significantly. The fourth-quarter Tankan, Japan's most important business survey, significantly beat market expectations, showing better sentiment among both manufacturers and service providers, independent of the company size. The auto industry showed by far the largest recovery in business conditions among sectors, implying that auto production, which had recovered from 50% of pre-crisis levels in May to 96% in September, might soon reach full capacity again. Also promising is the turnaround of the employment and capacity utilisation sub-component of the Tankan survey, which mirrors the slight uptick in the job-to-applicant ratio in October. Hence, the unemployment rate, at 3.1% in October, might have already reached its cyclical peak. On the negative side, investment plans for the current fiscal year have been reduced further, also reflected in a slight moderation of sentiment in the construction sector. Given still easy financial conditions and a relatively strong financial position of corporates, a revival of a positive investment cycle in 2021 is likely.

Inflation

Swiss Life Asset Managers	Consensus
2020: 0.0 %	2020: 0.0 %
2021: 0.0 %	2021: 0.0 %

Japan is experiencing a period of deflation that will last until March 2021, according to our forecasts. The main reasons are a stronger yen, a pandemic-related decline in wages and low energy prices. As in most other economies, the base effect on energy will turn from negative to positive in the second quarter 2021 and lead to slightly positive inflation readings again. On average, however, both 2020 and 2021 are likely to see zero inflation.

China Back to deleveraging

GDP growth

Swiss Life Asset Managers	Consensus
2020: 2.0 %	2020: 2.1 %
2021: 8.2 %	2021: 8.0 %

China's economy surpassed its pre-crisis level by more than three percent in the third quarter 2020, and economic indicators for the fourth quarter point to an ongoing economic expansion. Factories reopened swiftly after the lockdown implemented in February, while restrictions on individual mobility were relaxed only gradually. Hence, industrial production recovered earlier and stronger compared to consumption. Nevertheless, November retail sales grew by 5% compared to a year ago, showing that consumers are swiftly catching up. China's successful containment of the pandemic throughout 2020 has been key for the country's strong economic performance. Heading into 2021, the country will, however, have to prove that it is able to manage the contagion risk during the Chinese New Year festivities that will take place in February, when hundreds of millions of people leave their cities to meet their families in the more rural parts of the country. Moreover, since China's economy has recovered strongly from the pandemic-induced crisis, fiscal and monetary stimulus measures will be gradually phased out in order to slow down the credit acceleration and to refocus on reducing the country's debt pile. The deleveraging effort will likely lead to an increase in default rates, particularly among non-profitable state-owned companies, and authorities will have to be vigilant to find the right balance between necessary defaults and prevention of systemic risks.

Inflation

Swiss Life Asset Managers	Consensus
2020: 2.5 %	2020: 2.7 %
2021: 1.4 %	2021: 1.7 %

For the first time in 11 years, China's headline CPI fell into deflation in November (-0.5%). The main driver were pork prices that declined by 12.5% compared to a year ago. We expect inflation readings to remain in deflationary territory throughout the first quarter 2021, dragged down by decelerating food prices. Nevertheless, the weak readings are unlikely to urge the PBoC, China's central bank, to cut interest rates as inflation is expected to recover over the course of 2021.

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