

November/December 2021

## Key messages

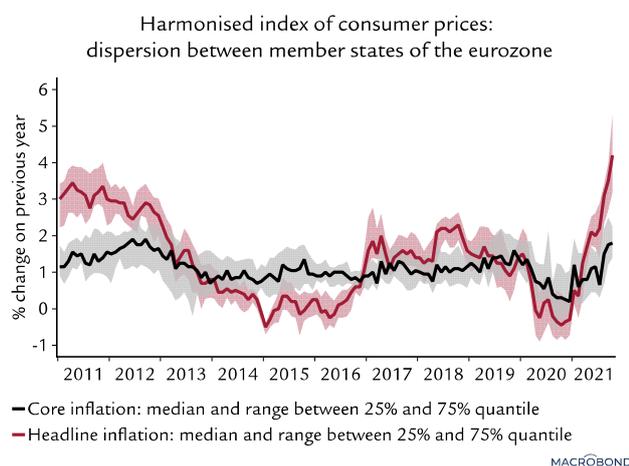
- USA: Deterioration of growth/inflation mix but no stagflation
- Eurozone: France and Italy grow strongly while Germany suffers from industrial supply bottlenecks
- Inflation: Energy as the main driver in Europe, rising wage pressure especially in the US and UK

## Comparison of forecasts

	2021 GDP growth		2022 GDP growth		2021 inflation		2022 inflation	
	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus
USA	5.4% ↓	5.7% ↓	3.3% ↓	4.1% ↓	4.4% ↑	4.4% ↑	3.1% ↑	3.4% ↑
Eurozone	5.2% ↑	5.1% ↑	3.7% ↑	4.4%	2.4% ↑	2.3% ↑	2.0% ↑	2.0% ↑
Germany	2.9% ↑	2.8% ↓	3.6%	4.4%	3.1% ↑	3.0% ↑	2.3% ↑	2.2% ↑
France	6.8% ↑	6.1%	3.6% ↑	3.8%	1.6%	1.7% ↑	1.8% ↑	1.6% ↑
UK	6.9% ↑	6.9% ↑	4.2% ↓	5.1% ↓	2.3% ↑	2.3% ↑	3.0% ↑	3.3% ↑
Switzerland	3.2%	3.4% ↓	2.7%	3.1% ↑	0.6%	0.5%	0.8%	0.6%
Japan	2.3% ↓	2.3%	2.1% ↑	3.0%	-0.3%	-0.2%	0.4%	0.5%
China	7.9% ↓	8.2% ↓	5.1% ↓	5.5% ↓	0.8% ↓	1.2%	2.0% ↓	2.1% ↓

Arrow indicates changes from previous month  
Source: Consensus Economics Inc. London, 11 October 2021

## Chart of the month



The energy price shock is affecting the eurozone to varying degrees, with headline inflation in October ranging from 1.4% in Malta to 8.2% in Lithuania and half the countries reporting rates between 3% and 5%. Core inflation, which excludes energy and food, also increased, but has only exceeded the 2% mark in a few countries that have so far published October data. With 2.8% core inflation, Germany is the most prominent example, triggering media attacks on the European central bank. However, interest rate hikes would be of little use against higher energy prices, and core inflation in Germany will fall again from January when certain base effects no longer apply.

## USA

### Comeback of stagflation?

#### GDP growth

Swiss Life Asset Managers	Consensus
2021: 5.5%	2021: 5.7%
2022: 3.4%	2022: 4.1%

According to the first GDP estimate for the third quarter, the US economy expanded by just 2.0% (annualised), a significant quarter-on-quarter slowdown and less than we and consensus expected. Combined with surprisingly high inflation rates, fears of stagflation arose among investors, a situation that is difficult to combat in monetary policy terms and was last experienced during the oil price shock of the 1970s. We consider the risk to be low. First of all, in contrast to the 1970s, the US is not currently faced with an external energy price shock, as the import dependency on crude oil has fallen dramatically and natural gas is exported in net terms. The balance between export and import prices (so-called terms of trade) has actually improved significantly in the last two years. Secondly, the high inflation has not eroded average purchasing power. Real incomes are higher than before the pandemic, and households have also accumulated considerable savings during the pandemic. The weakness in the third quarter was not attributable to private consumption – which grew dynamically – but rather to rising imports and low investment, especially in residential real estate. Rising imports are a good sign of domestic demand, and we already expect a return to moderate growth in the fourth quarter.

#### Inflation

Swiss Life Asset Managers	Consensus
2021: 4.4%	2021: 4.4%
2022: 3.1%	2022: 3.4%

While fears of stagflation are exaggerated, inflation concerns are thoroughly justified. Price momentum picked up again in October, especially for index heavyweight residential. In addition, corporate labour costs increased significantly in the third quarter. On the labour market, participation is still expected to pick up over the next few months, which should ease wage pressure to some extent.

## Eurozone

### Inflation at a multi-year high

#### GDP growth

Swiss Life Asset Managers	Consensus
2021: 5.2%	2021: 5.1%
2022: 3.7%	2022: 4.4%

We are slightly increasing our forecast for GDP growth in 2021 and 2022. The data available for the third quarter altogether paint a surprisingly positive picture of the state of the eurozone economy. Growth has recently been particularly robust in France and Italy, while in Germany it continues to be held back by global supply bottlenecks in industry. In Germany, however, gross domestic product in the first two quarters was revised up, which led to a net upward revision for the year as a whole. Data available so far for the final quarter of 2021 indicate a slight downturn in economic momentum due to supply bottlenecks in industry. Nevertheless, the purchasing managers' indices for manufacturing and services remain comfortably within the growth zone. Italy stands out in this regard, where the PMI actually rose slightly in October. Particularly in Italy, but also elsewhere, monetary and fiscal policy are developing a pronounced procyclical effect. The measures taken by the authorities to support the economy and the financial system have thus had the desired effect, as can also be seen not least in the figures for the labour market. The unemployment rate in the eurozone is now more than one percentage point below its September 2020 level.

#### Inflation

Swiss Life Asset Managers	Consensus
2021: 2.4%	2021: 2.3%
2022: 2.0%	2022: 2.0%

The parallel response of monetary and fiscal policy to the economic slump in the previous year is one of the reasons for the sharp rise in the inflation rate. However, half of the surge to 4.1% can still be explained by energy price developments. The energy transition comes with a price tag. While the inflation rate is likely to be significantly lower in 2022, we expect it to print 2% on average in 2022.

## Germany

### Start of second corona winter

#### GDP growth

Swiss Life Asset Managers	Consensus
2021: 2.9%	2021: 2.8%
2022: 3.6%	2022: 4.4%

Covid-19 case numbers recently rose faster than expected in Germany and reached the level of early November 2020. Hospitalisations and deaths are also on the rise but are still slightly below the November 2020 figures. The vaccination rate in Germany is now 66%. So far, the SPD has ruled out new restrictive measures and announced that it intends to end the state of emergency on 25 November. Instead, the focus is on third vaccination jabs, which are now recommended for older age groups and risk groups but also available to other groups of the population. So far, consumers have generally remained unconcerned, with improving consumer sentiment and stable mobility. However, volatile retail sales declined again in September. In addition, the Purchasing Managers' Index (PMI) for the services sector fell more sharply than expected in October. The PMI for manufacturing remained at a high level despite existing supply bottlenecks. However, the bottlenecks are set to continue to weigh on economic growth in the fourth quarter after having been responsible for disappointing growth of 1.8% in the third quarter. Notwithstanding this, the upward revisions for the first half of the year led to a slight increase in our 2021 growth forecast.

#### Inflation

Swiss Life Asset Managers	Consensus
2021: 3.1%	2021: 3.0%
2022: 2.3%	2022: 2.2%

Consumer price inflation again surprised on the upside in October, climbing to 4.5%. Such inflation rates were last seen when the Bundesbank was still at the helm. However, more than half of the increase is due to energy prices. We are raising our inflation forecast for both 2021 and 2022 but expect price momentum to normalise in the course of 2022. We therefore continue to expect the current surge to remain a temporary phenomenon.

## France

### Return to pre-crisis levels

#### GDP growth

Swiss Life Asset Managers	Consensus
2021: 6.8%	2021: 6.1%
2022: 3.5%	2022: 3.8%

With quarter-on-quarter GDP growth of 3.0%, the French economy outperformed the other eurozone heavyweights Germany, Italy and Spain in the third quarter and was the first country in this group to return to pre-crisis GDP levels. France benefits from a lower sector weighting in industrials compared to Germany. Supply bottlenecks also impact French manufacturing firms which have recently even been confronted with falling orders. The services sector, however, was buoyant, particularly those sectors hit hard by the pandemic, which exceeded all expectations. Gross value added in the hotel and restaurant industry grew by 43% in the third quarter, leaving 'only' a 9% gap to pre-crisis levels. Transportation also boomed, narrowing the pre-crisis level gap to 4%. Growth remains driven by massive fiscal stimulus. The central government deficit already reached the 2020 record level of EUR 178 billion in August 2021. However, as in many other developed countries, the screw will be tightened in 2022. The government is planning to cut spending by 3.5%, which in view of the high public spending ratio is set to put a significant brake on growth.

#### Inflation

Swiss Life Asset Managers	Consensus
2021: 1.6%	2021: 1.7%
2022: 1.8%	2022: 1.6%

The upward trend in gas prices, which is fuelling inflation in many parts of Europe and weighing on private consumption, is less of a problem in France. Gas only has a weighting of 1.1% in the basket for calculating inflation. More importantly, gas-fired power plants contribute only 6% to electricity generation, and as a net exporter France does not have to buy electricity from its neighbours at rising tariffs. This will help to keep inflation below 2% on an annual average in 2021 and 2022.

## UK Defying the shortage economy

### GDP growth

Swiss Life Asset Managers	Consensus
2021: 6.9%	2021: 6.9%
2022: 4.2%	2022: 5.1%

So far, the British economy seems to be defying the “shortage economy” in the form of empty shelves and supply bottlenecks, as well as the negative headlines about European relations. While the monthly GDP data available so far for the third quarter were not thrilling, they were solid enough for us to revise our cautious forecast for 2021 upwards. The biggest weakness remains the retail sector, which has been losing sales volumes month by month since the peak of sales in April 2021. Private consumption has shifted towards services, with, for example, hotels and restaurants surprisingly surpassing pre-crisis levels again in August. Activity has also almost completely normalised in the area of leisure and entertainment. Although consumer sentiment has recently declined, probably as a result of rising energy prices, service providers reported an acceleration of activity in October, contrary to the trend in continental Europe. However, we expect the economic upswing to lose momentum in 2022 – our GDP forecast remains more prudent than consensus. On the supply side, labour market bottlenecks could prevent the UK from exploiting its full growth potential, while on the demand side the upcoming interest rate hikes by the Bank of England could cause some drag.

### Inflation

Swiss Life Asset Managers	Consensus
2021: 2.3%	2021: 2.3%
2022: 3.0%	2022: 3.3%

Inflation fell slightly in September, from 3.2% to 3.1%, but is already expected to rebound in October due to the 12% higher price cap for electricity and gas. This regulatory intervention will keep energy prices artificially low over the winter months (wholesale prices have risen much more sharply). The cap is expected to be raised further at the next adjustment in April 2022. Combined with rising wages, annual average inflation is expected to be around 3% in 2022.

## Switzerland Flexible labour market

### GDP growth

Swiss Life Asset Managers	Consensus
2021: 3.2%	2021: 3.4%
2022: 2.7%	2022: 3.1%

A number of economic indicators are pointing to a further slowdown in growth momentum in the fourth quarter of 2021. Having said this, we do not expect that the fourth wave of the pandemic will lead to a renewed decline in gross domestic product in the current quarter or at the beginning of next year. Containment measures such as those that were necessary again at the beginning of the year now seem to be ruled out, even in the face of a renewed increase in the number of cases. On the demand side, consumer demand has been exceptionally robust and has also been driven by a rapid recovery in the labour market. We now expect the official unemployment rate to reach an annual average of 3.0% in 2021. We expect it to decline to 2.5% in 2022. According to our forecasts, the end-of-year rate at 2.4% will still print slightly above pre-crisis levels of 2.3%. The Swiss labour market has thus once again demonstrated its high flexibility, as among other things it has had to absorb three years of apprenticeship and university graduates over this period. However, the overall rate of unemployment including not only those registered as such but all job-seekers will likely not recover at the same rapid pace.

### Inflation

Swiss Life Asset Managers	Consensus
2021: 0.6%	2021: 0.5%
2022: 0.8%	2022: 0.6%

End-user prices for fossil fuels also rose further in Switzerland by the end of October. However, the weight of petroleum products (2.4%) is lower than in the consumer price statistics of the EU countries. In addition, the ongoing market opening in the Swiss retail sector and the strong franc are having a dampening effect on prices. Even the rapid labour market recovery is unlikely to bring any lasting inflation risks: expected wage growth in 2022 remains moderate at an average of 0.8%.

## Japan Continuity after the elections

### GDP growth

Swiss Life Asset Managers	Consensus
2021: 2.3%	2021: 2.3%
2022: 2.1%	2022: 3.0%

The general election of 31 October brought a surprisingly strong mandate for the incoming Prime Minister Fumio Kishida, whose Liberal Democratic Party (LDP) was able to defend an absolute majority in the House of Representatives. This will ensure continuity in economic policy, which has remained shaped by “Abenomics” even after the departure of Shinzo Abe. An ongoing expansive monetary policy and occasional fiscal packages are therefore to be expected, with Prime Minister Kishida already raising the prospect of such a package before the end of 2021: a relaunch of the “Go To Travel” program to stimulate tourism and even direct money transfers to the population are under consideration. Indeed, private consumption remains the weak link. In the second quarter of 2021, it was still 4.4% lower than in 2019 and according to initial indicators displayed little recovery in the third quarter. However, the vaccination progress and low case numbers led to an improvement in consumer sentiment and could trigger a recovery of consumption in the short term. In the medium term, however, higher wage growth remains the key to more consumption-driven growth. This is also Prime Minister Kishida’s declared goal, but there is a strong likelihood that he will miss it in the same way as Shinzo Abe. Despite reforms, appeals and incentives, Japan’s principle of “wage restraint versus job security” appears firmly anchored.

### Inflation

Swiss Life Asset Managers	Consensus
2021: -0.3%	2021: -0.2%
2022: 0.4%	2022: 0.5%

Consumer price inflation jumped above the 0% mark in September 2021 for the first time since August 2020, driven by energy and fresh food. Excluding these two volatile product groups, core inflation remained at -0.5%. We expect only a slight recovery of headline inflation to an average of 0.4% in 2021.

## China Growth disappointment

### GDP growth

Swiss Life Asset Managers	Consensus
2021: 7.9%	2021: 8.2%
2022: 5.1%	2022: 5.5%

China’s real economic growth slowed markedly from 7.9% annual growth in the second quarter to 4.9% in the third quarter. The driving factors were a mix of energy bottlenecks, a zero-tolerance policy towards new Covid-19 outbreaks and the frictions in the real estate market. Figures for September showed a slowdown of industrial production growth. While retail sales have recovered somewhat from the disappointing previous months, they remain well below the pre-crisis trend. Overall, GDP growth was lower than we expected. We are also projecting some of this cyclical weakness to the following quarters. For these two reasons, we have revised our GDP growth forecasts for 2021 and 2022 to 7.9% (from 8.3%) and 5.1% (from 5.4%). However, we still do not expect the upheavals in the real estate market to lead to an economic crisis. The Purchasing Managers’ Indices (PMI) for manufacturing recently sent out mixed signals. While at 49.2 the broader-based, official manufacturing PMI fell further below the 50-point growth threshold, the Caixin Manufacturing PMI rose from 50.0 to 50.6. According to both surveys, pressure on input prices remains high and supply bottlenecks are persisting. The foreign policy situation recently came to a head when US President Joe Biden stated that he would defend Taiwan in the event of a military attack by China.

### Inflation

Swiss Life Asset Managers	Consensus
2021: 0.8%	2021: 1.2%
2022: 2.0%	2022: 2.1%

As far as consumer price inflation is concerned, China remains the exception among the major economies. Inflation fell further to 0.7% in September. We carried out a further downward revision of our annual forecasts for 2021 and 2022. While producer price inflation climbed to 10.7%, we still expect only a very meagre pass-through to consumer prices. The central bank thus still has sufficient leeway to shape its monetary policy more expansively.

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