

Macroeconomic outlook 2022

In search of a new equilibrium

Hans Dewachter
Chief Economist, KBC Group NV
KBC Economics

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Five main messages

1

Unprecedented crisis and unusual recovery but no full reboot (yet)

2

Headwinds to the recovery persist but do not fully derail economic recovery

3

Inflation at record levels but eventually normalising as energy prices normalise and supply chain disruptions ease

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Central banks increasingly challenged by persistent inflation surprises face a 'pick-your-poison' moment

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Belgium recovered well from crisis but faces real challenges in the labour market

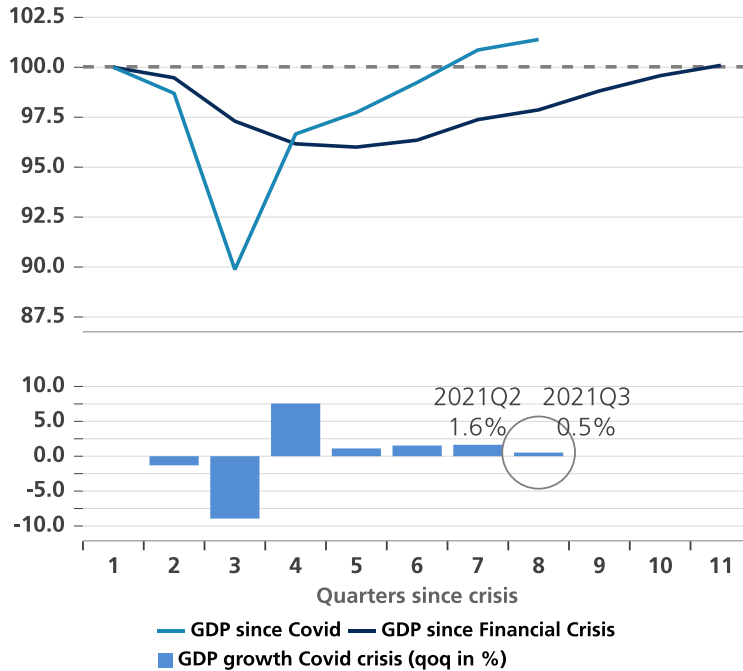
Unprecedented crisis and unusual recovery but no full reboot (yet)

"2021 became a turning point year as vaccination opened the door to recovery. But a full reboot of the economy is not yet in reach. Too many variables are still in search of a new equilibrium levels. Employment gaps remain as participation rates risk 'stalling' and economies 'exit' the crisis with substantially higher debt levels leaving them more vulnerable. Structural trends such as climate change add to the challenges ahead... "

Unprecedented crisis and unusual recovery but no full reboot (yet)

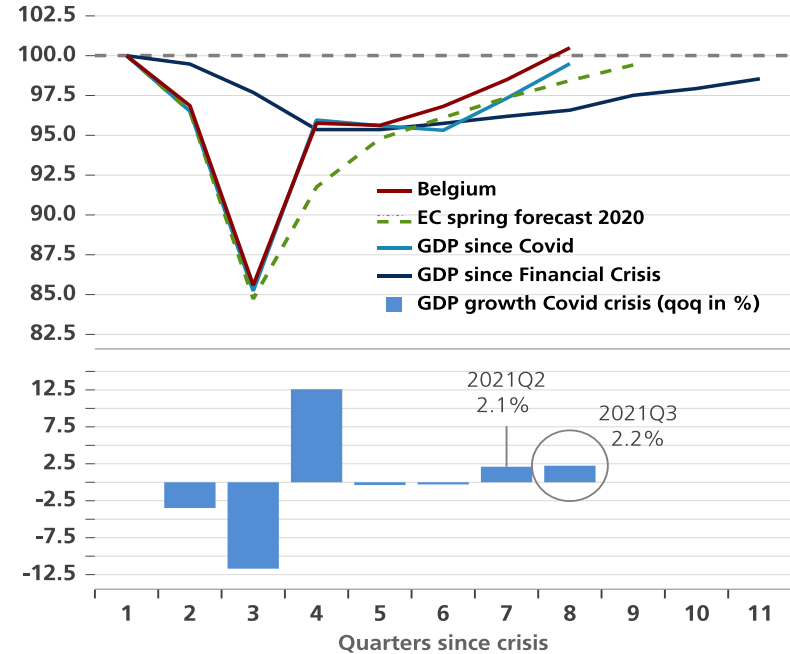
The economy recovered 'unusually' fast – a spring recovery

US gdp developments



Source: KBC Economics based on BEA

Euro area gdp developments

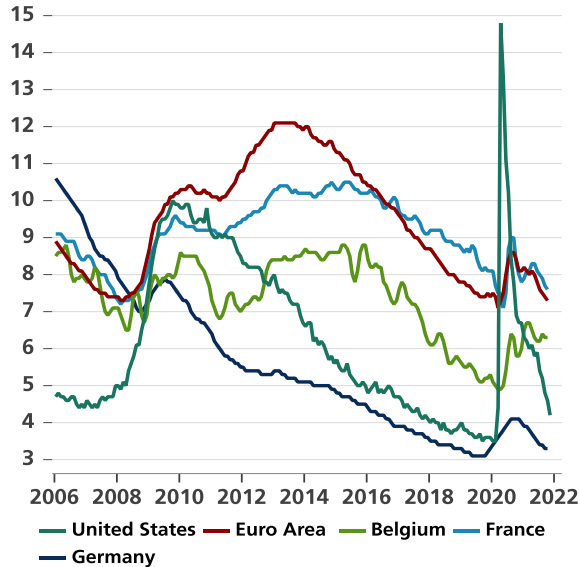


Source: KBC Economics based on Eurostat, NBB

Unprecedented crisis and unusual recovery but no full reboot (yet)

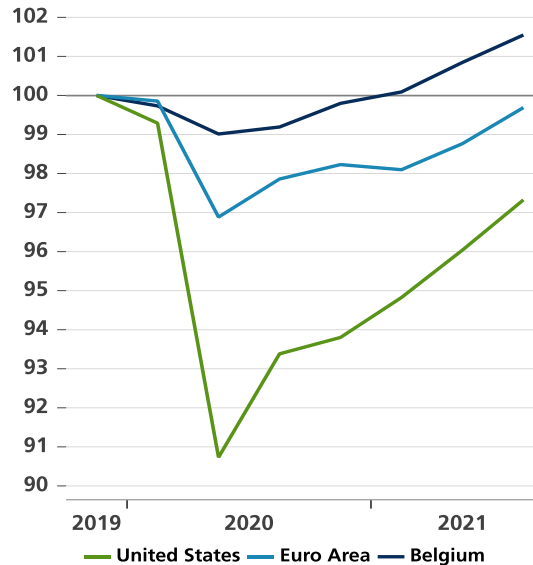
Labour markets are becoming tight as rebound in participation lags – missing labour?

Harmonized Unemployment Rates
% of active population



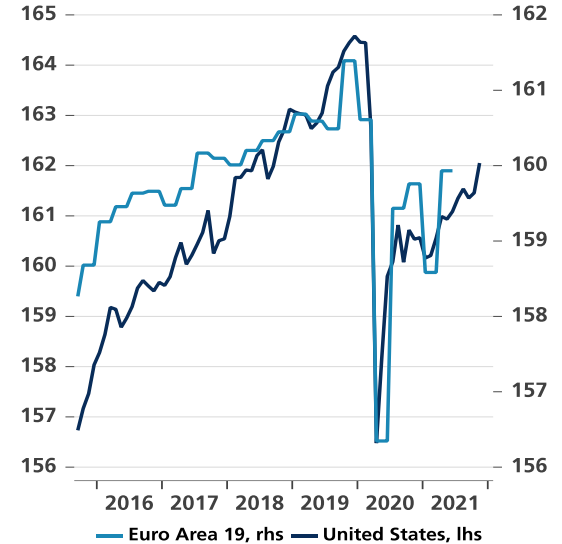
Source: KBC Economics based on Eurostat, BLS

Total domestic employment
(persons, Q4 2019 = 100)



Source: KBC Economics based on NBB, Eurostat, BLS

Labor force participation US and EA
persons in millions



Source: KBC Economics based on BLS, Eurostat

Headwinds to the recovery persist but do not fully derail economic recovery

"...Headwinds to the economic recovery have gained strength over 2021 and are likely to persist in 2022. The fourth Covid-wave crushed the dream of herd immunity at 70% while the Omicron underscores lingering mutations risks. In addition, the unbalanced recovery caused supply-demand imbalances and supply chain bullwhip effects causing severe labour and equipment shortages. The latter are likely to gradually resolve in the course of 2022 as the increased prices redirect and normalise demand. As supply chain disruptions dissolve and economies grow more virus resilience, we expect the economic recovery to pick up again, although globally at a lower pace..."

Macroeconomic outlook – slowly closing the output gap

Strong catch-up demand and fiscal support counter headwinds

KBC Economics forecasts 12/2021 (in %)

Real GDP growth	2019	2020	2021	2022	2023
Eurozone	1.6	-6.5	4.9	3.5	2.4
US	2.3	-3.4	5.6	3.7	2.3
China	6.0	2.3	8.2	5.1	5.0
Belgium	2.1	-5.7	6.0	2.5	1.8

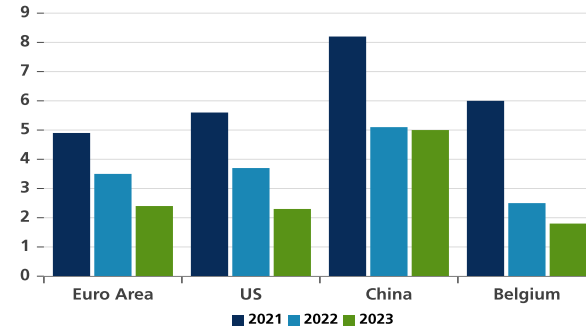
Source: KBC Economics

KBC Economics forecasts 12/2021 (in %)

CPI inflation	2019	2020	2021	2022	2023
Eurozone	1.2	0.2	2.6	2.3	1.9
US	1.8	1.2	4.6	3.0	2.2
China	2.9	2.5	0.9	2.3	2.2
Belgium	1.2	0.4	3.0	2.7	2.0

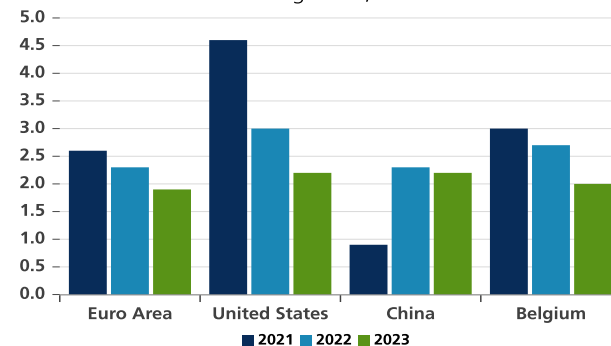
Source: KBC Economics

Economic growth: major economies
annual growth, in %



Source: KBC Economics

Headline inflation: major economies
annual growth, in %

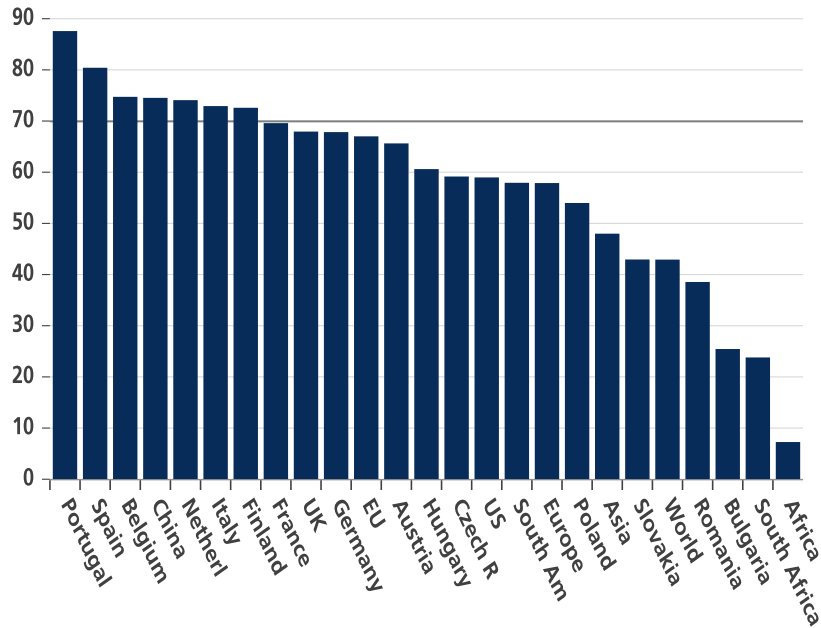


Source: KBC Economics

Headwinds persist but do not fully derail economic recovery

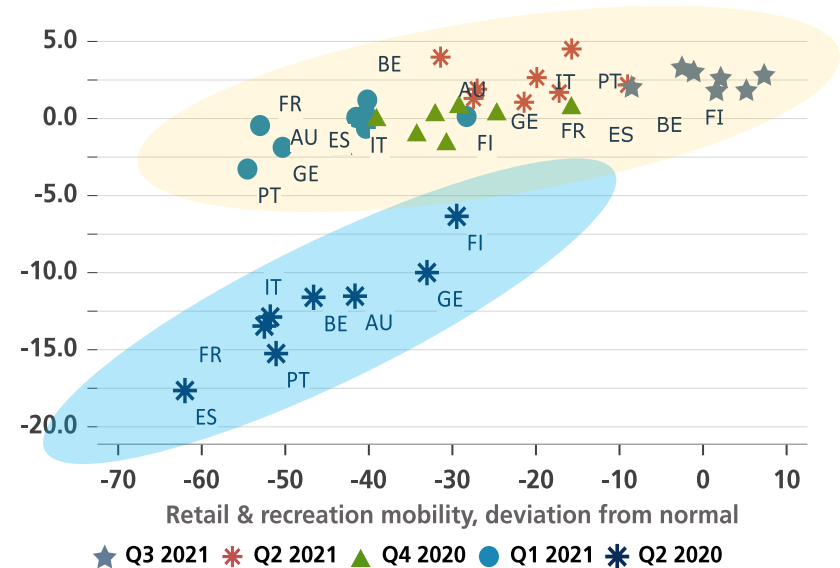
Dream of herd immunity shattered but economies are gaining resilience

Share of the Population Fully Vaccinated Against COVID-19



Source: KBC Economics based on Our World in Data

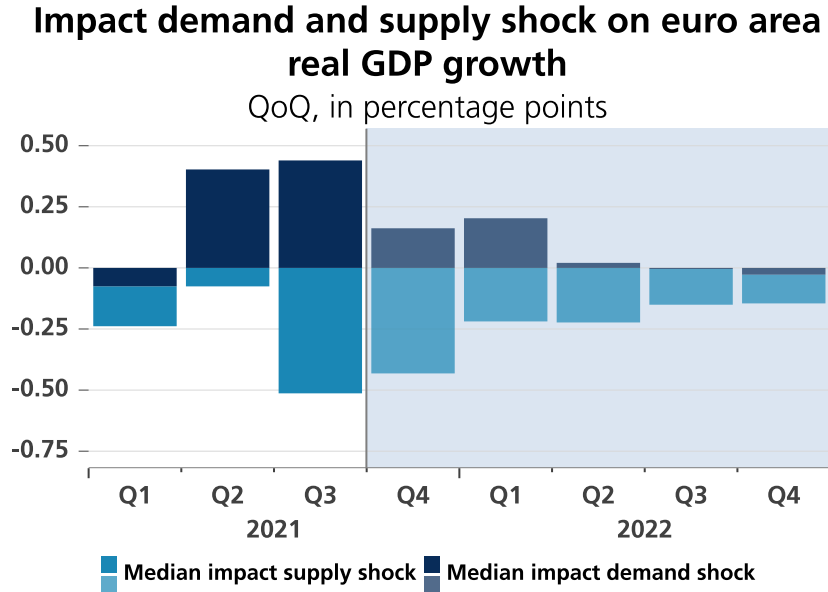
Relationship GDP growth and mobility restrictions



Source: KBC Economics based on Eurostat, Istat, CBS, NBB, INE, Google

Headwinds persist but do not fully derail economic recovery

Supply chains disruptions have significant negative impact on growth



Source: KBC Economics in-house BVAR model



Inflation at record levels but eventually peaking as energy prices normalise and supply chain disruptions ease

"...Persistent and strong upside inflation surprises keep inflation top-of-mind. Inflation dynamics have been pushed up by a number of (likely transitory) factors, including (oil price) base effects from the crisis, re-opening repricing and relative price adjustments due to biased demand and most recently the energy crisis. Current developments point to a carry-over of higher-for-longer inflation into 2022. But eventually inflation will decelerate as re-opening effects stabilise and energy prices normalize. It is unlikely to see similar extreme inflation impulses as in 2021, unless second round effects would gain strength and generalise. Also financial markets still see inflation decelerating..."

Macroeconomic outlook – slowly closing the output gap

Strong (biased) catch-up demand and fiscal support counter headwinds

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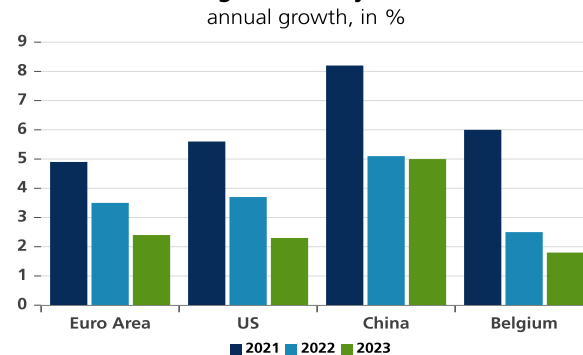
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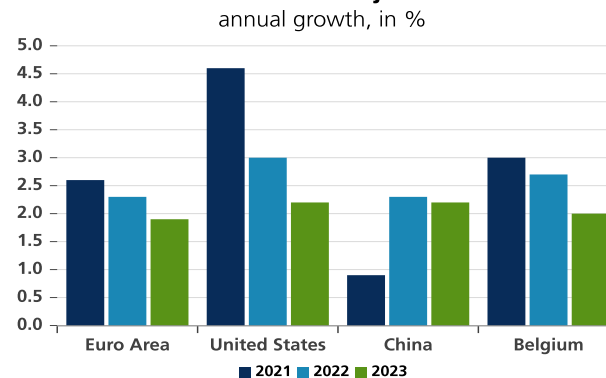
Source: KBC Economics 11

Economic growth: major economies



Source: KBC Economics

Headline inflation: major economies



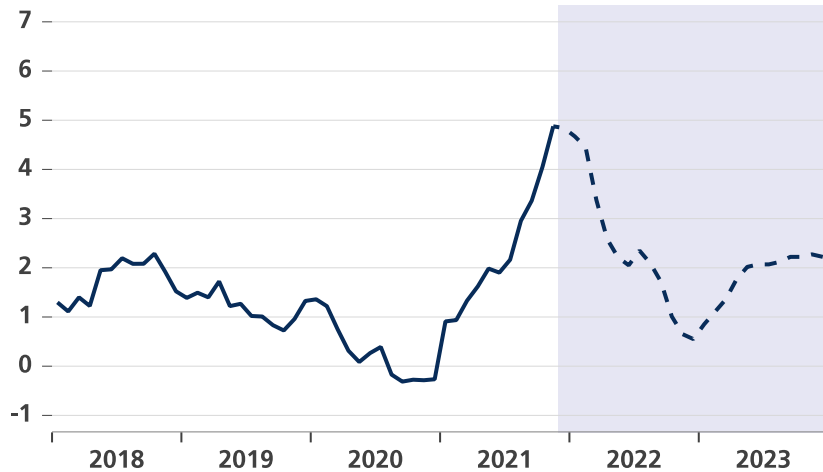
Source: KBC Economics

Inflation at record levels but slowly 'normalising'

Higher-than-expected inflation likely to persist for some time, but central bank targets still anchor inflation expectations

Euro area inflation normalising during 2022

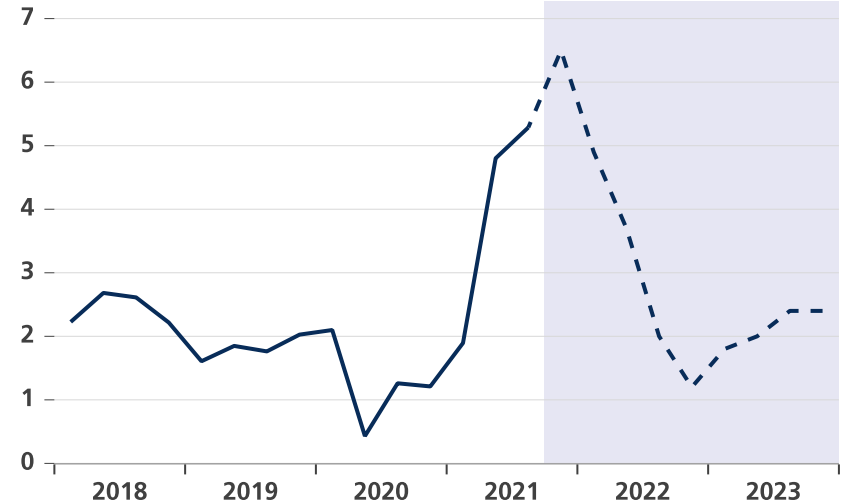
HICP headline inflation, annual change in %



Source: KBC Economics

US inflation is 'transitory' as well

headline inflation, quarterly frequency, annual change in %



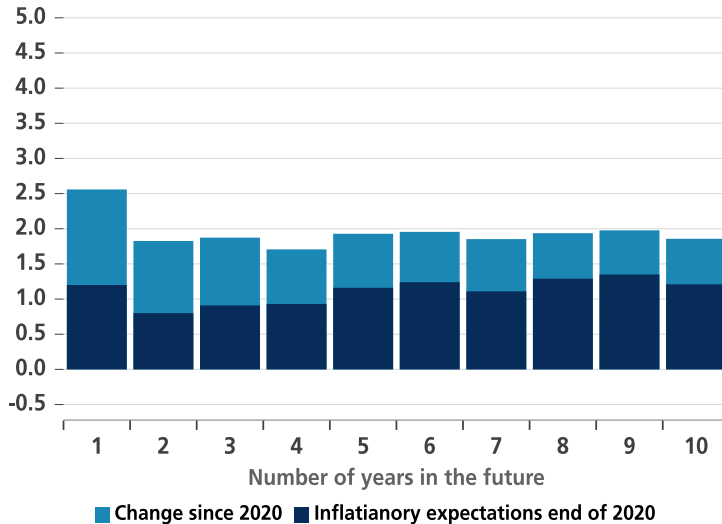
Source: KBC Economics

Inflation at record levels but slowly 'normalising'

Higher-than-expected inflation likely to persist for some time, but central bank targets still anchor markets' inflation expectations

Inflation-swap curve for EUR

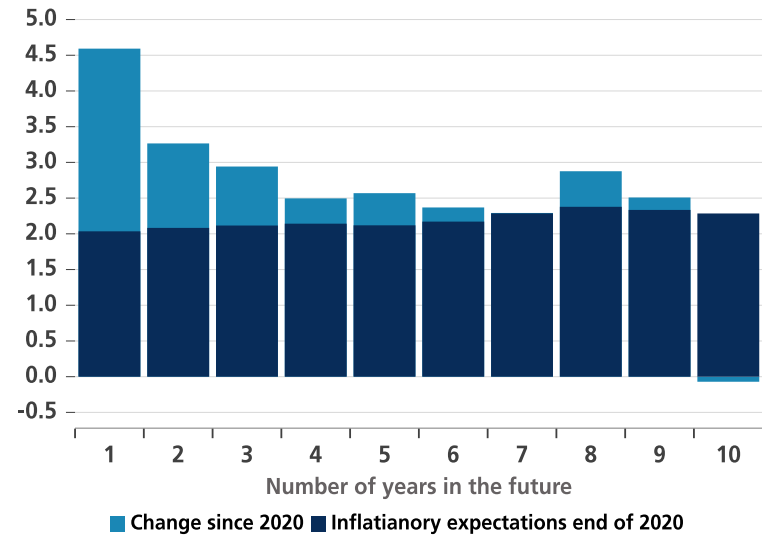
Forward (1Y) inflation, in %



Source: KBC Economics based on Refinitiv Datastream

Inflation swap curve for USD

Forward (1Y) inflation, in %

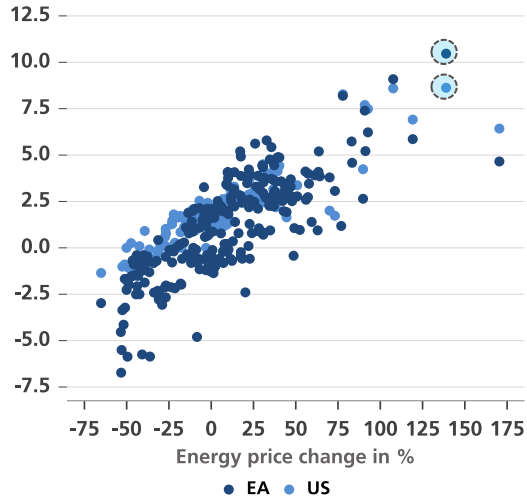


Source: KBC Economics based on Refinitiv Datastream

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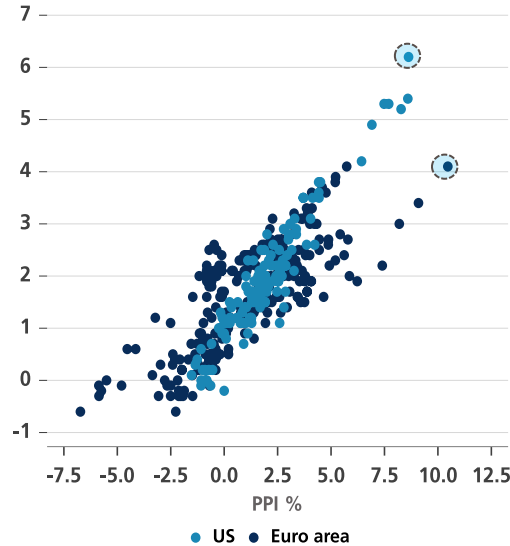
Cost-push effects and starting wage pressures in US

Energy inflation feeding into PPI: US and EA



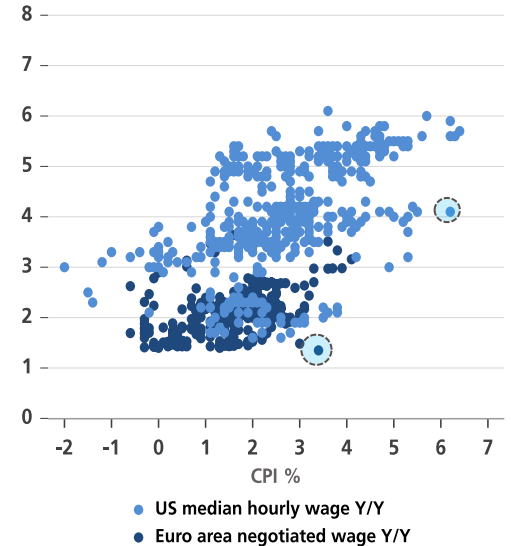
Source: KBC Economics based on StatCan, BLS, Eurostat, NBS, BOJ, Wor

PPI and CPI: US and EA



Source: KBC Economics based on StatCan, BLS, Eurostat, NBS, BOJ, Wor

CPI and wage inflation: US and EA



Source: KBC Economics based on StatCan, BLS, Eurostat, NBS, BOJ, Wor

Circles denote the latest observations for the US (light blue) and the EA (dark blue)

Central banks, increasingly challenged by persistent upside inflation surprises, face a 'pick-your-poison' moment

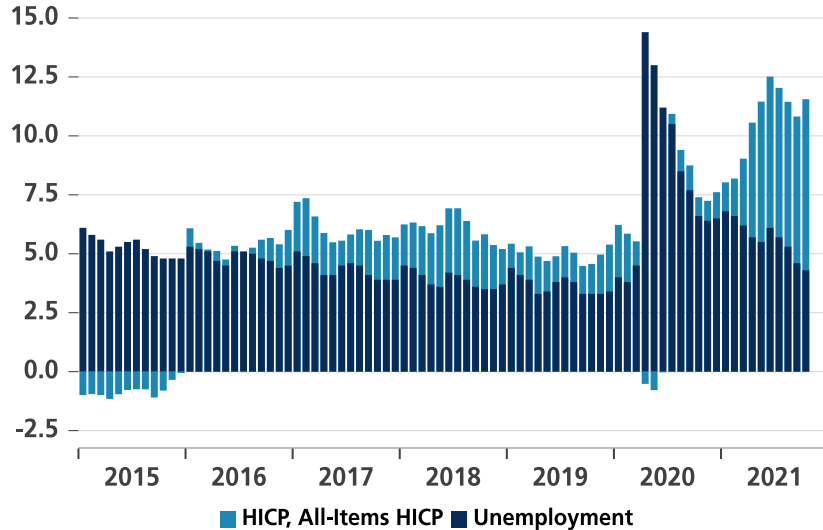
"...Persistent and strong upside inflation surprises keep inflation top-of-mind and put central banks increasingly before their pick-your-poison moment. An increasing number of central banks put (re-)anchoring inflation expectations top of the monetary policy agenda, as risks of second-round effects increase against the background of tightening labour markets. While monetary policy tightening is ineffective against supply chain disruptions, it can address excess demand and send a strong signal to financial markets regarding their determination to deal with inflation. The Fed seems determined – despite omicron – to reverse course and start tightening already in the first half of 2022, while the ECB maintains a wait-and-see attitude..."

Central banks increasingly challenged by persistent inflation

Central banks face a 'pick-your-poison' moment as economies climb the misery index ladder and real rates remain extremely accommodative

Misery index US

sum of inflation and unemployment rate, in %



Source: KBC Economics based on Eurostat, Japanese Statistics Bureau, Ministry of Internal Affairs

Real yield (10yrs) developments

approximations based on break-even inflation rates



Source: KBC Economics based on Macrobond, U.S. Department of Treasury

Central banks increasingly challenged by persistent inflation

Fed on an accelerated way to policy normalisation while ECB maintains focus on favourable financing conditions

KBC Economics forecasts - update 12/2021

	2020	2021	2022	2023
Fed	0.125	0.125	0.875	1.375
ECB (deposit rate)	-0.50	-0.50	-0.50	-0.25
US 10Y rate	0.93	1.60	2.60	2.70
Germany 10Y rate	-0.56	-0.20	0.60	0.80
EURUSD nominal exchange rate	1.23	1.14	1.21	1.26

Source: KBC Economics

Federal Reserve

Accelerated tapering opens door for policy rate hikes in 2022 (75 bps)

ECB

Ensuring favourable financing conditions remains a priority, PEPP expected to be wound down

USD

Stabilisation expected in the near term

Belgium recovered well from crisis but faces real challenges in the labour market

"... The Belgian economy performed quite strongly in 2021, partly due to the industry, which was somewhat less affected by supply constraints compared to those in the euro area. The again worsening climate regarding the pandemic will also affect economic activity in Belgium. Nevertheless, a "perfect storm" could be brewing in the Belgian labour market. Tight labour markets, staff drop-out due to Covid-disease and quarantine, and the decline of the working-age population is putting staff shortages at Belgian companies on edge. This could lead to upward real wage pressure ..."

Belgium recovered well and relatively fast from the COVID-crisis

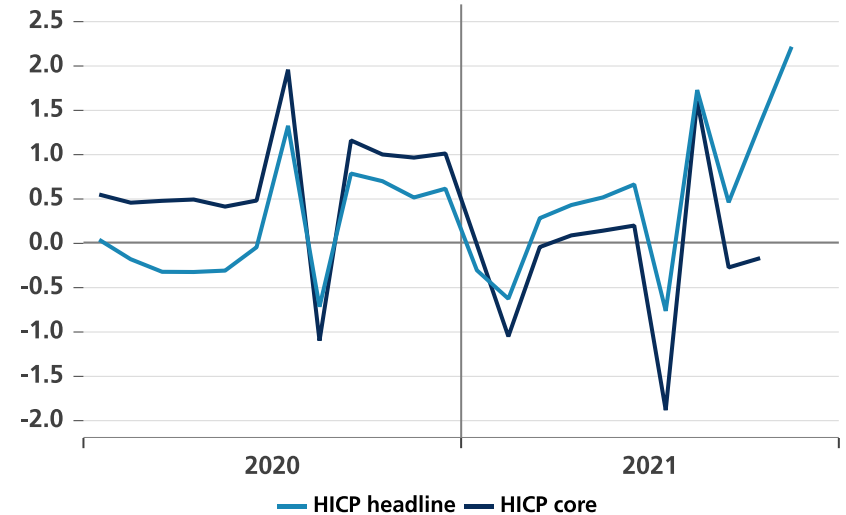
Manufacturing was less impacted by supply chain constraints

KBC Forecasts 12/2021 - Belgium

	2020	2021	2022	2023
Real GDP (average yearly change, in %)	-5.7	6.0	2.5	1.8
Inflation (average yearly change, harmonised CPI, in %)	0.4	3.0	2.7	2.0
Unemployment rate (Eurostat definition) (in % of the labour force, end of year)	6.0	6.2	6.0	5.7
Government budget balance (in % of GDP)	-9.1	-8.0	-5.3	-5.1
Gross public debt (in % of GDP)	112.8	112.9	113.3	114.8
Current account balance (in % of GDP)	0.9	0.4	-1.0	-0.5
House prices (Eurostat definition) (average yearly change in %, existing and new dwellings)	4.2	6.0	3.0	2.0

Source: KBC Economics

Inflation differential Belgium - Euro Area (in percentage points)

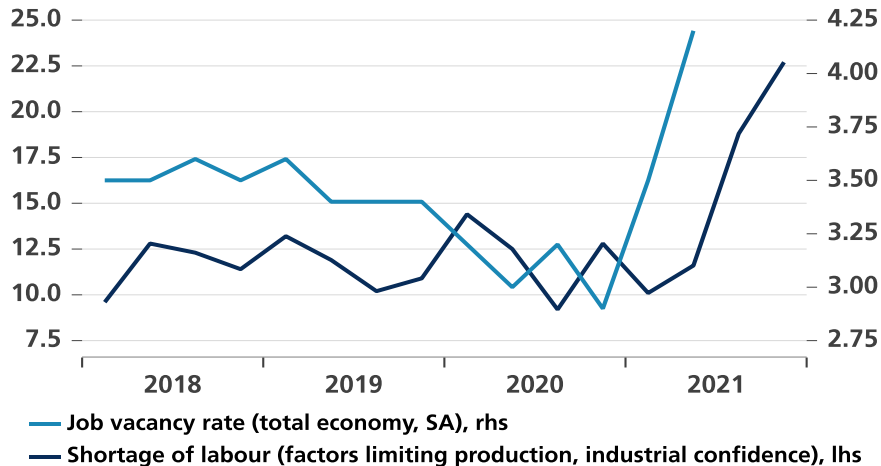


Source: KBC Economics based on Eurostat

But is a perfect storm is brewing on the Belgian labour market?

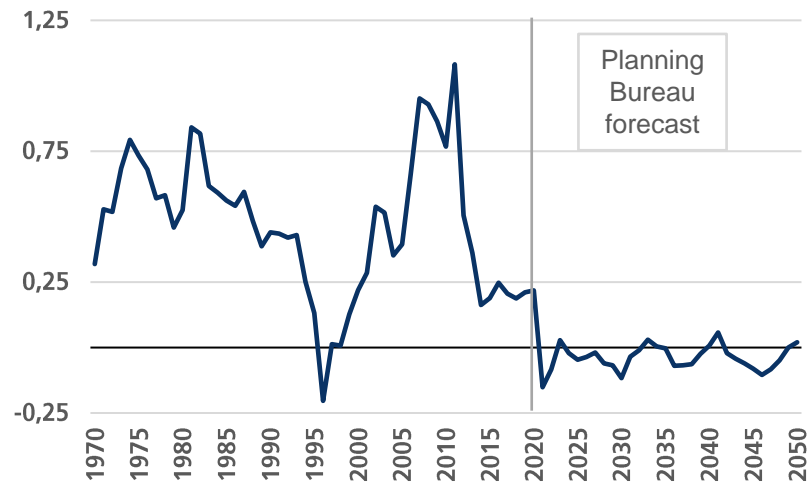
Labour market shortages worsen against background of high inflation, economic recovery and declining working-age population

Belgium - Factors limiting production (industrial confidence indicator)



Source: KBC Economics based on DG ECFIN, Eurostat

Belgium – Growth population at working age (people aged 20-64, yoy in %)



Source: KBC Economics based Federal Planning Bureau

Recap: main messages

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