Perspectives
Economics

February 2021

Key messages

- As vaccination campaigns have started, 2021 sees the beginning of the end of the pandemic
- After China, the US and Switzerland are the next economies to reach pre-crisis levels
- Slack in the global economy limit upside inflation risks for the moment

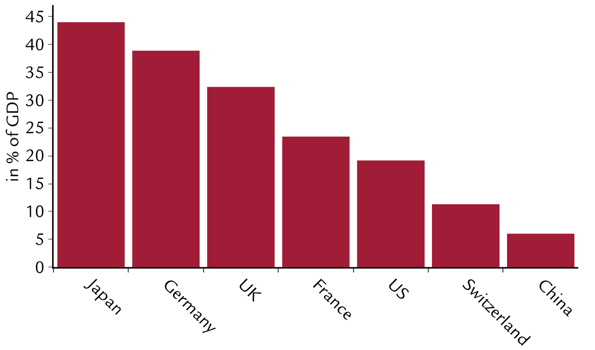
Comparison of forecasts

	2021 GDP growth		2022 GDP growth		2021 inflation rate		2022 inflation rate	
	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus
USA	4.8% ↑	4.4% ↑	3.2%	3.4%	2.2% ↑	2.1% ↑	2.2%	2.2%
Eurozone	4.6% ↑	4.4% ↓	2.4%	4.0%	1.0%	0.9%	1.5%	1.3%
Germany	3.7% ↑	3.7% ↓	2.4%	3.6%	1.7% ↑	1.5% ↑	1.6%	1.6%
France	6.8%	5.6% ↓	2.2%	3.8%	1.1%	0.8%	1.5%	1.1%
UK	5.1% ↓	4.3% ↓	4.1%	5.8%	1.5%	1.5% ↓	1.6%	2.0%
Switzerland	3.5% ↑	3.2% ↓	2.2%	2.9%	0.5%	0.3% ↑	0.7%	0.5%
Japan	2.6%	2.4% ↓	1.4%	2.2%	0.0%	-0.1% ↓	0.4%	0.5%
China	8.3% ↑	8.3%	5.2%	5.4%	1.4%	1.4%	2.1%	2.1%

Arrows indicate difference from previous month
Source: Consensus Economics Inc. London, 11 January 2021

Chart of the month

Total fiscal policy response in 2020 (spending, loans & guarantees)



▪ Discretionary fiscal response to COVID-19 pandemic (Source: IMF)

An unprecedented amount of money has been spent or put aside for fiscal policy measures to cope with the current crisis. In Switzerland, the fiscal stimulus in 2020 exceeds the amount spent during the great financial crisis in 2008 by a factor of 20, Germany's fiscal package is an estimated ten times larger this time. Lessons learned from Japan suggest that the announced amount of spending packages tends to exaggerate the actual money spent in hindsight. Yet, the size of the discretionary fiscal response to the COVID-19 pandemic remains gigantic. With monetary and fiscal policy working in the same direction, long-term inflation risks are now more significant than ever over the past 20 years.

USA
A wall of money

GDP growth	
Swiss Life Asset Managers	Consensus
2021: 4.8 %	2021: 4.4 %
2022: 3.2 %	2022: 3.4 %

As expected, US economic data ran into a soft patch at the end of 2020. In December, new restrictions led to the first monthly employment decline since April 2020, while fading fiscal support contributed to the third consecutive monthly decline in retail sales. We expect economic momentum to increase drastically at the start of 2021, primarily as a result of fiscal stimulus. The bi-partisan stimulus package that was hammered out at the end of December includes a stimulus check of USD 600 per person and extends enhanced unemployment benefits until mid-March. President Biden proposed another fiscal package worth USD 1.9 trn (8.8% of GDP) that includes another means-tested stimulus check of USD 1400 per person, an extension of enhanced unemployment benefits until September and, crucially, aids for state and local governments. Due to the super-tight majority in the Senate, most observers expect the final package to be closer to the USD 1.0 trn mark, with the stimulus check being the least disputed element. A survey by the New York Fed showed that households saved 36.4% of their first stimulus check, while another 34.5% was used to pay down debt. Respondents also stated that their propensity to save would increase with additional rounds of fiscal transfers. Hence, while these checks will certainly support private consumption in 2021, financial markets and households' balance sheets might actually be the biggest beneficiaries of that "wall of money".

Inflation	
Swiss Life Asset Managers	Consensus
2021: 2.2 %	2021: 2.1 %
2022: 2.2 %	2022: 2.2 %

During the pandemic, US core inflation has mainly been a function of economic dynamics. As such, core CPI also ran into a soft patch in the final quarter of 2020 on the back of sluggish demand. Headline inflation, however, surprised positively in December due to rising food and energy prices. We expect a normalisation of core inflation in 2021 as demand is set to recover swiftly, while headline inflation will additionally benefit from favourable base effects.

Eurozone
Inflation to make a comeback

GDP growth	
Swiss Life Asset Managers	Consensus
2021: 4.6 %	2021: 4.4 %
2022: 2.4 %	2022: 4.0 %

The start of vaccination campaigns in all member states suggests that we are progressing further towards the light at the end of the tunnel of the pandemic. Meanwhile, tightened containment measures to fight the combined dangers of a second wave and virus mutations mean that the setback in the economic recovery will be deeper and last longer than previously anticipated. Like the situation during the first lockdowns between February and May last year, services sectors across Europe suffer more from measures put in place, while manufacturers with a global client base benefit from intact supply chains. Accordingly, the Purchasing Managers Indices PMI suggest that manufacturing activity continued to expand at the start of the year, while service sectors contracted for the fifth consecutive month. Apart from the countries' individual sector composition and fiscal room to manoeuvre, the future handling of the pandemic and the success of the vaccination campaigns are key to determine the pace of the economic recovery going forward. Malta, Ireland and Spain saw a comparably fast start of their vaccination campaigns. Meanwhile the economic recovery is put at risk in countries like Austria, Greece and Slovakia where vaccination progress is slow and the level of containment measures high. A high frequency GDP tracker provided by Austria's central bank hints at a renewed sharp contraction since the start of the year.

Inflation	
Swiss Life Asset Managers	Consensus
2021: 1.0 %	2021: 0.9 %
2022: 1.5 %	2022: 1.3 %

Inflation is set to make a temporary comeback in 2021. Starting from a rate of -0.3% reported for December 2020, annual headline inflation is set to rise to 1.8% until October 2021. While inflation is heading towards the European Central Bank's target of "close to, but below 2%", we do not expect any monetary policy action to be undertaken. Most of the upside move is transitory, owing to base effects in energy prices or the removal of a temporary VAT tax rate cut in Germany.

Germany
One-off effects to lift inflation

GDP growth	
Swiss Life Asset Managers	Consensus
2021: 3.7 %	2021: 3.7 %
2022: 2.4 %	2022: 3.6 %

Germany's second lockdown did not cause a renewed fall in economic activity in the last quarter 2020. Incoming data led us to slightly lift our projection of fourth-quarter GDP growth prior to the preliminary release of official data on January 29. Industrial activity benefited strongly from firm demand out of Asia and the US. Yet, even more restrictive containment measures since the start of the year and the likely extension of the current lockdown warrant a downward revision of the forecast for the first quarter. According to the Oxford University COVID-19 Containment Policy Stringency Index, the German measures are among the most restrictive in Europe. Accordingly, domestic economic activity has slowed in January. Consumer confidence as well as the ifo Business Climate Indicator have registered a noteworthy drop as of late. Service sector activity is deteriorating according to preliminary data for the Purchasing Managers' Index. We now expect GDP to drop by 0.4% in the first quarter, before the economic recovery resumes. In our base case scenario, Germany's real GDP ends the year 2021 just slightly below its pre-crisis level. At the end of 2022, we project GDP to exceed the pre-crisis level by 1.5%. We expect major support from fiscal policy (see page 1): 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
2021: 1.7 %	2021: 1.5 %
2022: 1.6 %	2022: 1.6 %

Multiple one-off effects will lift Germany's consumer price index markedly in 2021. Higher global market prices for energy products, the new CO2 tax as well as the reversal of the temporary VAT tax rate all result in a jump in the headline inflation rate from -0.7% in December 2020 to 3.0% by the end of this year. While this increase is only temporary in our view, it is probably sufficient to attract media attention and trigger a renewed wave of unjustified inflation hysteria in the German public.

France
Vaccination starts only slowly

GDP growth	
Swiss Life Asset Managers	Consensus
2021: 6.8 %	2021: 5.6 %
2022: 2.2 %	2022: 3.8 %

In contrast to Germany, France has started to gradually ease containment measures since December. Business sentiment indicators improved consequently, again in contrast to latest developments in Germany. Accordingly, we expect GDP in France to resume its upward trend already during the quarter, after a renewed dip in the final quarter 2020. We expect the economy to grow by 1.8% in the first quarter and by 2.1% in the second quarter 2021. A return to pre-crisis GDP levels is unlikely before the second half 2022. While business sentiment in the French manufacturing industries is comparably solid, the lockdown continues to weigh on service sectors. France as a major European tourism destination should have a large self-interest in successful vaccination campaigns across Europe, allowing the re-opening for international travel by the second quarter 2021. Yet, the domestic vaccination campaign had a terribly slow start. According to numbers collected by Our World in Data, an Oxford University initiative, only 1.61 in 100 persons have received a first dose of the vaccines by the time we wrote this text. France thus lags most other Eurozone countries. Logistics may play a rule, but vaccination scepticism is far more common in France then elsewhere in Europe. It is thus encouraging that willingness to get the vaccine has increased markedly over the past weeks in reaction to positive news coming from Israel.

Inflation	
Swiss Life Asset Managers	Consensus
2021: 1.1 %	2021: 0.8 %
2022: 1.5 %	2022: 1.1 %

We assume headline inflation to have fallen to 0% in December 2020, marking a cyclical trough. Meanwhile, our inflation forecast remains above consensus for 2021 and 2022. Energy prices continued to rise at the beginning of the year. Depending on the timing of a renewed re-opening of the domestic economy, companies in the transport and accommodation sectors will be given back some price-setting power once pent-up demand for leisure and entertainment can break free again.

UK
Delayed recovery

GDP growth

Swiss Life Asset Managers	Consensus
2021: 5.1 %	2021: 4.3 %
2022: 4.1 %	2022: 5.8 %

After an endless stream of negative economic news, recent data releases for November and December 2020 at last brought some respite, suggesting that the economic damage from the second wave was less dramatic than we had expected. Especially encouraging was the fact that the manufacturing and construction sectors performed well despite the worsening medical situation. However, the emerging optimism was dialled back in the new year. New restrictions led to significant declines in mobility indicators, and the January composite Purchasing Managers' Index (PMI) dropped to the lowest level (40.6 points) since May 2020, way below the respective reading for the Eurozone (47.5) or the US (58.0). This was – unsurprisingly – mainly driven by the services sector, but the manufacturing sector also lost significant momentum. Adding to the woes of the British economy were disruptions caused by the shift to the post-Brexit trading regime. In the January PMI survey, manufacturers reported a significant increase in delivery times and input prices. Nevertheless, they stuck to their upbeat view for the rest of the year (the "future output" component kept hovering above the 70 points mark) as the border situation will likely improve. In combination with the swift progress of the vaccination campaign – the UK already administered 10 shots per 100 people at the time of writing – we expect the economy to rapidly recover after a GDP drop in the first quarter of 2021.

Inflation

Swiss Life Asset Managers	Consensus
2021: 1.5 %	2021: 1.5 %
2022: 1.6 %	2022: 2.0 %

After a year of inflation readings mostly below 1%, 2021 will likely bring a swift normalisation of inflation, especially when the economic recovery sets in in the second quarter. While lockdowns are a drag on services inflation in the first quarter, this might be mitigated by the unwinding of temporary VAT cuts, rising energy prices and higher costs on imported goods due to border disruptions.

Switzerland
"Long COVID" effects

GDP growth

Swiss Life Asset Managers	Consensus
2021: 3.5 %	2021: 3.2 %
2022: 2.2 %	2022: 2.9 %

Normally, we would have to wait until February 26 for the official release of fourth-quarter 2020 GDP data by the SECO, Switzerland's State Secretariat for Economic Affairs. These days, however, nothing in economic data analysis is normal anymore: SECO's newly introduced index of Weekly Economic Activity (WEA) already allows the conclusion that the economic impact of renewed containment measures in the final quarter 2020 and at the start of 2021 was far less dramatic than what we had witnessed between February and May 2020. In our base case scenario, economic activity is expected to gain momentum once containment measures are being eased again in March and thereafter. The gradual progress of the Swiss vaccination campaign should allow a reopening of affected services sectors during the second quarter. A favourable sector composition, comparably mild containment measures and export industries benefitting strongly from the fast recovery in Asia all ensure that Switzerland's GDP recovers more quickly to pre-crisis levels than its European neighbours. Yet, "Long COVID" effects will be felt by the Swiss economy too. Unemployment is set to rise to around 3.8% until April 2021. The sectors where most jobs are being lost remain accommodation, restaurants, travel agencies and entertainment. In these, corporate bankruptcies should start to become much more numerous in the months to come.

Inflation

Swiss Life Asset Managers	Consensus
2021: 0.5 %	2021: 0.3 %
2022: 0.7 %	2022: 0.5 %

Since February 2020, Switzerland has been stuck in the fourth deflationary period of the past 15 years. Rising energy prices will push annual consumer price inflation into positive territory again in the second quarter 2021. Improving global economic momentum and a likely increase in domestic services prices after the reopening of the economy are likely to push inflation to a temporary peak of around 1.0% at the end of the year.

Japan
Surge in cases and no vaccines

GDP growth	
Swiss Life Asset Managers	Consensus
2021: 2.6 %	2021: 2.4 %
2022: 1.4 %	2022: 2.2 %

The new year brought another state of emergency in various regions of Japan. While the pandemic rages far less dramatically than in Europe, infection rates and mortality in Japan are nevertheless now higher than in the first wave and among the highest in Asia. The government, worried about overcrowded hospitals, has again asked companies to reduce office presence and asked bars, restaurants, gyms etc. to cut opening hours. Sports events are still allowed at reduced capacities. Contrary to the first wave, non-essentials stores and schools were not asked to close. Even though these measures are recommendations rather than obligations, they already had a significant effect on individual mobility. According to data from Google, mobility in transit stations is 40% lower than normal, while mobility for retail and recreation purposes is 25% lower than normal. The Japanese economy, having been one of the least affected among developed markets in 2020, will thus likely report sluggish data – notably for private consumption – in the first quarter 2021. Meanwhile, survey data still suggests that manufacturing output should remain on its upward trajectory due to improving foreign demand. Due to the relatively favourable starting point, generally low potential growth and the painfully slow vaccination rollout (all vaccine approvals are still pending), we expect the economic recovery after the first quarter 2021 to be very modest compared to other developed economies.

Inflation	
Swiss Life Asset Managers	Consensus
2021: 0.0 %	2021: -0.1 %
2022: 0.4 %	2022: 0.5 %

In December 2020, Japanese headline inflation likely reached its trough at -1.2%. We expect a swift return to around 0% in the second quarter due to the energy price base effect. In 2021, price and especially wage pressure will likely remain low as the output gap is only gradually closing, with a projected average inflation rate of just 0%. 2022 might bring somewhat more positive price dynamics, but no inflation anywhere close to the Bank of Japan's 2% target.

China
Virus clouds Chinese New Year

GDP growth	
Swiss Life Asset Managers	Consensus
2021: 8.3 %	2021: 8.3 %
2022: 5.2 %	2022: 5.4 %

As the only major economy in the world, China surpassed pre-crisis levels in 2020. Full-year GDP expanded by 2.3%, beating our and consensus estimates. Buoyant exports of pandemic-related goods produced in China – such as medical equipment or computers – supported the strong performance. Moreover, industrial activity recovered swiftly after lockdown measures had been eased in the second quarter and ended the year 7.3% above pre-crisis levels. Strict virus containment measures and an efficient tracing strategy were successful in keeping the virus spread in check, allowing the economy to reopen swiftly, while policy stimulus boosted industrial and real estate activity. In 2021, China's economy should continue to expand, aided by solid external demand amid a global economic recovery. However, quarter-on-quarter growth rates will likely lose steam. Monetary and fiscal stimulus measures will moderate, as focus is shifting back towards financial stability concerns, especially in the highly indebted real estate sector. Moreover, the first quarter of 2021 will be challenging due to a recent upsurge in COVID-19 cases in northern China – just ahead of the Chinese New Year that will take place on 13 February. Consequently, Chinese policy makers are implementing measures to discourage travelling during the festivities, which will weigh on consumer confidence as well as on services activities such as transportation and leisure.

Inflation	
Swiss Life Asset Managers	Consensus
2021: 1.4 %	2021: 1.4 %
2022: 2.1 %	2022: 2.1 %

China's December consumer price index (CPI) moved back into inflationary territory at 0.2%, after having fallen into deflation in November (-0.5%). The higher reading was driven by a cold wave that pushed food prices higher. For the first quarter 2021 we expect, however, pork prices to bring headline CPI back to deflation again. Meanwhile, excluding food and energy prices, core CPI edged lower to 0.4%, from 0.5% previously.

Economic Research

Marc Brütsch
Chief Economist
marc.bruetsch@swisslife.ch
@MarcBruetsch

Damian Künzi
Economist Developed Markets
damian.kuenzi@swisslife.ch

Josipa Markovic
Economist Emerging Markets
josipa.markovic@swisslife.ch

Francesca Boucard
Economist Real Estate
francesca.boucard@swisslife.ch
@f_boucard

Rita Fleer
Economist Quantitative Analysis
rita.fleer@swisslife.ch

Consensus Economics
Forecast Accuracy Award Winner
Switzerland 2019

Consensus Economics
Forecast Accuracy Award Winner
Euro zone 2019

If you have any questions or if you would like to subscribe to this publication,
please send an email to: info@swisslife-am.com.
For more information visit our website at: www.swisslife-am.com