Perspectives
Economics

SwissLife
Asset Managers

July 2023

Key takeaways

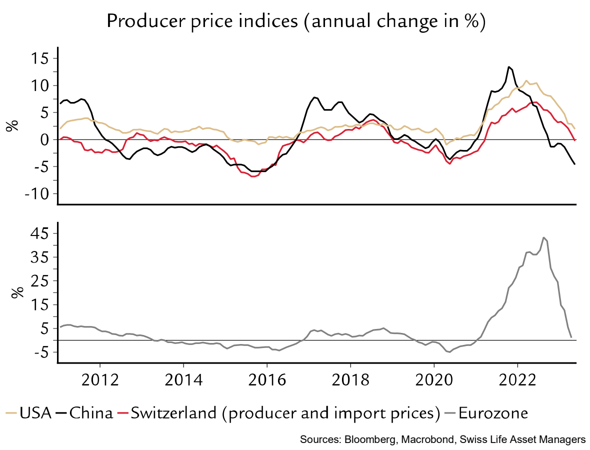
- USA: Signs of a positive turnaround in the housing market are hampering the work of the US Federal Reserve
- Eurozone: Industrial weakness is more pronounced, pressure on goods prices is likely to ease significantly
- China: Inflationary pressure remains low while the recovery continues to falter

Comparison of forecasts

	2023 GDP growth		2024 GDP growth		2023 inflation		2024 inflation	
	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus
USA	0.9%	1.3% ↑	0.6%	0.5% ↓	4.1% ↓	4.1% ↓	2.5%	2.6%
Eurozone	0.4% ↓	0.6% ↓	0.8%	0.9%	5.5%	5.4% ↓	2.4%	2.4%
Germany	-0.2%	-0.2% ↓	0.6%	1.1%	6.0%	6.0% ↓	2.3%	2.5% ↓
France	0.6%	0.6%	0.9%	0.9%	4.8%	5.3% ↓	2.1%	2.7% ↑
Italy	1.1%	1.0% ↑	0.6%	0.8% ↓	6.1%	6.1%	2.1%	2.5% ↑
Spain	1.8%	1.8% ↑	1.2%	1.5% ↓	3.9%	3.7% ↓	2.5%	2.9% ↑
UK	0.0%	0.1% ↑	0.4%	0.8%	7.4%	7.3% ↑	2.8%	3.2% ↑
Switzerland	0.7%	0.7%	1.5%	1.4%	2.1%	2.4% ↓	1.6%	1.4% ↓
Japan	1.2% ↑	1.1% ↑	0.7%	1.0% ↓	2.7%	2.8% ↑	1.2% ↑	1.5% ↑
China	5.8%	5.7% ↓	5.2%	4.9%	1.2% ↓	1.3% ↓	2.0% ↓	2.3% ↓

Arrows indicate change from previous month. Source: Consensus Economics Inc. London, 12 June 2023

Chart of the month



The supply chain shocks in the goods and transport sector have been overcome. New equilibrium prices have emerged on the commodity markets following the uncertainty in 2022. Price pressure at the producer level is easing accordingly. China is currently exporting disinflation again. In Switzerland, producer price developments are about four months ahead of consumer prices. A further fall in inflation at consumer level can therefore be expected. The extent of this decline remains dependent on the price-setting power of companies and the price development in the services sector.

USA
Unclear signals

GDP growth

Swiss Life Asset Managers	Consensus
2023: 0.9%	2023: 1.3%
2024: 0.6%	2024: 0.5%

The incoming economic data from the US are painting a mixed picture. On the one hand, industrial production is slowing down, thus confirming the negative global momentum in industry surveys. The S&P Purchasing Managers' Index for the US is again close to the December 2022 lows for the output and order intake components. On the other hand, both surveys and activity data paint a robust picture for the services sector, and the recovery in the housing market has continued from low levels. Sentiment among brokers improved according to the NAHB survey, construction starts for new houses soared in May and house prices picked up again somewhat after seven months of decline. Should it be confirmed that housing market actors have digested the interest rate shock of 2022 and are continuing to gain confidence, this would ironically send out a problematic signal for the US economy as it could trigger further interest rate hikes by the central bank, with an additional drag on corporate investment and the US commercial real estate market, which in contrast to residential real estate is facing high vacancies. We are sticking to our forecast of a mild recession in the US, although the timing (current assumption is for a slowdown already in the second half of 2023) is uncertain due to the contradictory data situation.

Inflation

Swiss Life Asset Managers	Consensus
2023: 4.1%	2023: 4.1%
2024: 2.5%	2024: 2.6%

Headline inflation in the US is continuing to fall in line with our expectations and stood at 4.0% in May. Energy and service prices (excluding housing) contributed slightly more to the reduction than we had expected, while inflation in the housing and consumer goods area turned out to be surprisingly persistent. Although core inflation is also falling, at 5.3% it remains at a level that makes it impossible to rule out further interest rate hikes.

Eurozone
Industrial weakness

GDP growth

Swiss Life Asset Managers	Consensus
2023: 0.4%	2023: 0.6%
2024: 0.8%	2024: 0.9%

Eurozone industrial production surprised on the upside in May. However, this was solely due to a volatile increase of 21% in Ireland. While industrial production in France and Germany increased slightly, it remained well below pre-pandemic levels and has largely moved sideways since the start of the year. While Italy and Spain's industrial sectors did better after the pandemic, they posted a sharp and surprising decline in April. Despite a significant easing in energy prices, even energy-intensive sectors in the Eurozone, such as chemicals and metals, were unable to increase their output substantially this year. Car production has also been flat since the beginning of the year, although production plans in Germany in particular are still clearly positive. It is increasingly likely in this sector that there will not only be no positive growth momentum from China following the reopening, but that competition will further exacerbate the structural problems in the European industrial sector: China's car exports reached new highs in April. The June purchasing managers' index confirms the industrial weakness in the Eurozone with a further decline in manufacturing and order intake and – for the first time since the pandemic – a decline in industrial employment.

Inflation

Swiss Life Asset Managers	Consensus
2023: 5.5%	2023: 5.4%
2024: 2.4%	2024: 2.4%

Now that supply bottlenecks have largely disappeared, slowing industrial demand is likely once again to become the main driver of goods prices. Producer prices in the Eurozone have been falling for four months and at 1% their annual inflation in April was unexpectedly below 2% for the first time since February 2021. Purchasing managers in industry have also been reporting falling purchasing and selling prices for the past four and two months respectively. In the services sector, however, price pressure remains high.

Germany
Labour shortage

GDP growth

Swiss Life Asset Managers	Consensus
2023: -0.2%	2023: -0.2%
2024: 0.6%	2024: 1.1%

Both survey and activity data for Germany were disappointing over the past month. April retail sales and industrial production increased less than expected, the purchasing managers' index (PMI) for manufacturing fell further below the 50 mark in June and the PMI for the services sector also fell short of expectations (at still high levels), with outstanding business declining for the first time since January. However, employment continues to rise and there are still significantly more companies than before the pandemic in both industry and services that are citing labour shortages as a factor hindering production. The shortage of labour will be an issue for the German economy for some time to come. The working population could shrink by 8% by 2035 and the Federal Employment Agency estimates that there will be a shortage of around 400 000 skilled workers each year. Labour market participation in Germany is relatively high at 70%, which limits the potential for growth here. This leaves only immigration, which was on a downward trend after 2015 prior to the sharp increase caused by the war in Ukraine. Against this backdrop, the Federal Government recently passed a new Immigration Act which is intended to make immigration easier for workers.

Inflation

Swiss Life Asset Managers	Consensus
2023: 6.0%	2023: 6.0%
2024: 2.3%	2024: 2.5%

Labour shortages will keep wage and therefore price pressure structurally high over the coming years, particularly in the services sector. From a cyclical perspective, however, goods prices are at least showing some signs of easing. Producer prices fell more than expected in May and according to the PMI industrial companies lowered their selling prices in June for the first time since 2020. We therefore anticipate a gradual decline in inflation to 2% towards the end of 2024, but not to the pre-pandemic rates averaging 1.2%.

France
Out of step

GDP growth

Swiss Life Asset Managers	Consensus
2023: 0.6%	2023: 0.6%
2024: 0.9%	2024: 0.9%

As the renowned Tour de France gets underway, the economy in France is somewhat out of step. The momentum from China anticipated at the start of the year is also proving less pronounced here. In addition, the continued tightening of monetary policy by the ECB is causing noticeable headwind for industry. The "order intake" component of the purchasing managers' index for manufacturing fell to its lowest level for 2023 in June, not a good sign for the second half of the year. In economic forecasting, it is practically impossible to predict the exact timing of a cyclical turning point even if the fundamental developments have been correctly analysed. Based on the partly high-frequency data series available today, it makes sense to position the timing of the economic slowdown in mid-May as since then, according to the online job advertisement platform Indeed, the volume of online job advertisements has declined across all sectors. Furthermore, the scores of the most highly regarded business surveys have deteriorated further in recent weeks. In addition to the continuing period of weakness in the manufacturing sector, the purchasing managers' index for the services sector now also fell below the 50-point growth threshold in June.

Inflation

Swiss Life Asset Managers	Consensus
2023: 4.8%	2023: 5.3%
2024: 2.1%	2024: 2.7%

The annual rate of change in producer prices is also declining in France. However, so far only data up to and including April are available. According to the above-mentioned survey of purchasing managers, the majority of companies surveyed in the manufacturing sector have since lowered their selling prices. In response to political pressure, large retailers have undertaken to pass on the lower purchase prices to customers. These observations explain our comparatively low inflation forecast.

Italy
Industrial sector under pressure

The Italian economy, which has been surprisingly dynamic since the pandemic, is gradually running out of growth drivers. Investments in the residential sector, a consequence of temporary incentives for energy-related renovations, have already passed their peak. Meanwhile, as in other countries, the industrial engine is stuttering. The downward trend in industrial production (seasonally adjusted) accelerated in April 2023, and according to the purchasing managers' indices the signs are continuing to point to contraction. The cyclical chemicals sector is particularly weak, while the pharmaceutical and transport equipment sectors (especially aviation) continue to perform well. The gap with the services sector has widened. The upward trend in retail sales remains unbroken and consumer sentiment surprised on the upside in June. Consumers are presumably viewing their personal financial situation more positively due to falling inflation, while job security was rated better again in the first quarter despite the slight rise in the unemployment rate.

Spain
Moderate wage cost pressure

Inflationary pressure in Spain eased further in May. Year-on-year headline inflation fell from 4.1% to 3.2%. In line with developments in the Eurozone as a whole, core inflation is falling somewhat more slowly and at 6.1% was twice as high as headline inflation in May. We expect this downward trend to have continued in June. The ECB raised its inflation forecast significantly in June, citing wage cost pressure as one of the main reasons. However, this is developing very heterogeneously within the monetary union. In Spain, while average wage costs per employee also increased in the first quarter, the trend should be more favourable in the medium term than in the Eurozone as a whole. In Spain, contractual wages are negotiated on the basis of headline inflation. In addition, a new three-year national collective bargaining agreement is entering into force as part of the recent labour market reform. These factors should help keep the pressure on wage costs relatively moderate.

Switzerland
Momentum continuing to fall

GDP growth	
Swiss Life Asset Managers	Consensus
2023: 0.7%	2023: 0.7%
2024: 1.5%	2024: 1.4%

Our assessment of an economic trend largely bereft of momentum was confirmed at the end of the second quarter. Business surveys are trending downwards on a broad front, with the purchasing managers' indices for manufacturing and more domestically oriented SMEs now below the 50-point growth threshold. However, the same survey of purchasing managers in the services sector continues to show growth. It is therefore above all private household consumption that is set to support growth over the summer months. However, even among Swiss consumers growth has its limits. Prospective increases in health insurance premiums and rents will reduce purchasing power over the coming quarters. Compared to previous years, domestic purchasing power can also be expected to flow to other European countries in the summer months, as the backlog demand for trips abroad still seems high. Rising construction and financing costs and sluggish approval procedures are also curbing momentum in the construction sector.

Inflation	
Swiss Life Asset Managers	Consensus
2023: 2.1%	2023: 2.4%
2024: 1.6%	2024: 1.4%

Our model predicts a temporary drop in the inflation rate below the 2% threshold for the second half of the year. This model is based on the producer and import price index as well as the development of service prices according to the purchasing managers' index. Towards the end of the year and at the beginning of 2024, inflation at consumer level will be influenced by one-off effects that the model does not take into account: in addition to rising existing rents for apartments, these include price increases for public transport and an increase in VAT. A renewed increase in electricity prices is also foreseeable for 2024.

UK
Stagflation?

GDP growth

Swiss Life Asset Managers	Consensus
2023: 0.0%	2023: 0.1%
2024: 0.4%	2024: 0.8%

Monthly GDP grew by 0.2% in April compared to the previous month and made up at least some of the March loss. The recovery was mainly driven by the services sector, which partially recovered from the impact of the bad weather in March. At the same time, industrial production and construction declined. However, this was the first negative monthly growth contribution since August 2022. Overall industrial production has recovered since last summer. This development contrasts with the purchasing managers' index for UK manufacturing, which has been consistently below the growth threshold of 50 over this period. As in the manufacturing sector, rising financing costs are holding back investment in the construction sector. The labour market remains more resilient than expected. Surprisingly, the unemployment rate fell again in April, while wage growth rose to 7.2%. This is the highest level in the post-pandemic period. The data contrast with the expectations of the Bank of England (BoE), which anticipated a slowdown in wage dynamics. The unexpected intensification of the labour market situation and high core inflation should serve to maintain pressure on the BoE to hike interest rates further. We now consider the risk of stagflation in the UK to be significant.

Inflation

Swiss Life Asset Managers	Consensus
2023: 7.4%	2023: 7.3%
2024: 2.8%	2024: 3.2%

Headline inflation remained consistently high in May at 8.7% year-on-year, but core inflation surprisingly continued to rise. While service prices were the main driver, food and consumer goods inflation also remained high. The BoE raised interest rates again in June and more than expected. The market is currently expecting further interest rate hikes up to 6% (from the current 5%), which we consider to be somewhat exaggerated.

China
Low price pressure

GDP growth

Swiss Life Asset Managers	Consensus
2023: 5.8%	2023: 5.7%
2024: 5.2%	2024: 4.9%

After economic data for April already came in significantly weaker than expected, May data also suggest that the recovery is already faltering again. Foreign trade figures for May again surprised significantly on the downside. Exports in particular plummeted sharply in May. Imports are also falling again. After industrial production in April was significantly lower than expected, May data were in line with expectations, but the latter were scaled down. In May, the official purchasing managers' index for the manufacturing sector remained below the growth threshold of 50 for the second month in succession. Private consumption remains robust. Retail sales continued to grow strongly. However, some base effects due to last year's lockdown measures are still playing a role here. The government has already reacted to these weak data. Surprisingly, China's central bank cut its key interest rate by 0.1 percentage points in mid-June. The low inflation is giving the central bank some room for manoeuvre. The weak data have also refuelled speculation about possible government stimulus packages. However, we currently consider the likelihood of a significant package, especially in the infrastructure or real estate area, to be low.

Inflation

Swiss Life Asset Managers	Consensus
2023: 1.2%	2023: 1.3%
2024: 2.0%	2024: 2.3%

While China's consumer price inflation rate increased marginally in May, it is still very low year-on-year at 0.2%. Producer prices remain clearly in deflationary territory at -4.6% year-on-year. The low price pressure also does not point to an overheating economy.

Economic Research

Marc Brütsch
Chief Economist
marc.bruetsch@swisslife-am.com
@MarcBruetsch

Damian Künzi
Head Macroeconomic Research
damian.kuenzi@swisslife-am.com
@kunzi_damian

Josipa Markovic
Economist Emerging Markets
josipa.markovic@swisslife-am.com

Rita Fleer
Economist Quantitative Analysis
rita.fleer@swisslife-am.com

Florence Hartmann
Economist Developed Markets
florence.hartmann@swisslife-am.com

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