

July 2021

## Key messages

- USA: COVID-19-sensitive components in the shopping cart boost inflation
- Eurozone: Further setbacks cannot be ruled out
- Switzerland: GDP already back to pre-crisis level

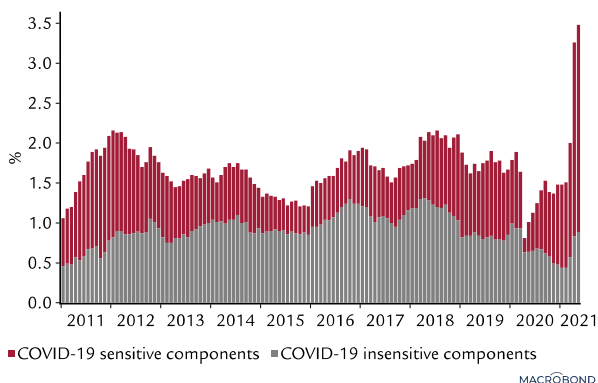
## Comparison of forecasts

	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	6.0% ↑	6.7% ↑	3.3%	4.1% ↑	3.5% ↑	3.5% ↑	2.4% ↑	2.6% ↑
Eurozone	4.4% ↑	4.4% ↑	3.3%	4.4% ↑	1.7% ↑	1.8% ↑	1.3%	1.4% ↑
Germany	3.2% ↓	3.3%	3.3% ↑	4.2% ↑	2.4%	2.5% ↑	1.3%	1.7% ↑
France	6.0% ↓	5.5%	3.1% ↑	3.9%	1.4%	1.4% ↑	1.3%	1.2% ↑
UK	6.1% ↑	6.6% ↑	4.3%	5.3% ↓	1.7% ↑	1.7% ↑	1.8% ↑	2.3% ↑
Switzerland	3.6%	3.5% ↑	2.5% ↑	2.9%	0.5%	0.4% ↑	0.7%	0.5%
Japan	2.5%	2.6% ↓	2.0%	2.8% ↑	0.0%	0.0%	0.4%	0.5%
China	8.2%	8.7%	5.4%	5.6%	1.3%	1.5%	2.3%	2.3% ↑

Arrows indicate change from previous month  
Source: Consensus Economics Inc. London, 14 June 2021

## Chart of the month

USA: contribution to PCE core inflation rate  
(source: San Francisco Fed)



A debate is still raging over whether the rise in inflation is only temporary or heralds a return to supposed by-gone times. The San Francisco branch of the US Federal Reserve System has calculated the price trend of goods and services in terms of their sensitivity to containment measures. It turns out that the contribution of the less-affected components to the core inflation rate is largely stable. Around three quarters of the current inflation rate can be attributed to COVID-19 sensitive components. There are many indications that the price increase is a one-off.

## USA Twin peaks

### GDP growth

Swiss Life Asset Managers	Consensus
2021: 6.0%	2021: 6.7%
2022: 3.3%	2022: 4.1%

The second quarter has ended and will likely mark a peak in two respects: firstly, the US economy's highest growth rates are behind us and secondly, the inflation cycle has passed its peak. The growth peak is being driven by major easing measures – no more restrictions apply in certain States – and substantial fiscal transfers to households. These factors will fade in the third quarter. The vaccination campaign is also losing momentum. Meanwhile, the US has fallen significantly behind European countries and major emerging economies such as China and India in terms of daily vaccinations even though it is still a long way from herd immunity. The challenge for the health authorities will therefore be in the third quarter to reach the 47% of the US population who are currently unvaccinated – otherwise there is a risk of another COVID-19 wave next winter. Despite the projected slowdown and our slightly more cautious growth forecast than consensus, the USA is still driving the global economy in the second half of the year. Politically, the focus in the coming months will be on the planned US infrastructure programme, where both the approach (bipartisan versus the Democrats alone) and the scope of the package are still completely open.

### Inflation

Swiss Life Asset Managers	Consensus
2021: 3.5%	2021: 3.5%
2022: 2.4%	2022: 2.6%

Inflation sprang another surprise in May, accelerating to 5.0%, the highest level since 2008. Once again, the increase was driven by used cars and pandemic-sensitive goods and services (see page 1). As a result, the inflation cycle is likely to have already peaked. We continue to expect a decline in June and a stabilisation from August at around 3.6% for headline inflation and 2.9% for core inflation.

## Eurozone EU money is now flowing

### GDP growth

Swiss Life Asset Managers	Consensus
2021: 4.4%	2021: 4.4%
2022: 3.3%	2022: 4.4%

As in the summer of 2020, containment measures in Europe will be eased, not least to safeguard the tourism season. The spread of the delta variant has to be kept in mind and weighed against the vaccination progress. A fourth wave in the autumn cannot be ruled out from today's perspective, but its short-term economic damage is likely to be less than during the winter of 2020/2021. In the next few days, the funds from the EU Recovery Fund will be released for the member states. On average in 2021 and 2022, these funds represent around 0.6% of the Eurozone's GDP. The effectiveness of fiscal policy instruments to combat a recession has to be assessed in terms of their timely implementation and the long-term effect on growth. Short-time work programmes, which were introduced in many places in the spring of 2020, can be implemented particularly quickly. By contrast, the Recovery Fund had at best one positive psychological effect in 2020: it helped to limit the risk premium on bonds of the southern member states, which were particularly hard hit by the pandemic. These monies are now having a pro-cyclical effect, which solidifies the economic upswing but also contributes to the risks of inflation.

### Inflation

Swiss Life Asset Managers	Consensus
2021: 1.7%	2021: 1.8%
2022: 1.3%	2022: 1.4%

Currently, 14 of the 19 euro member states have an inflation rate of 1.8% or higher. In the previous month there were seven countries for which this was true. It is therefore not surprising that the inflation risk has been the topic of intense debate in recent weeks. We assign only a 25% probability to the scenario of sustained higher inflation over the coming years. In our baseline scenario until 2024, we expect headline inflation to settle at around 1.5% for the Eurozone.

## Germany

### Optimistic service providers

#### GDP growth

Swiss Life Asset Managers	Consensus
2021: 3.2%	2021: 3.3%
2022: 3.3%	2022: 4.2%

Recently, there have been increasing signs of broader economic confidence in smaller companies and especially service providers. According to the ifo Institute, among the ten sectors with the most optimistic outlook for the next six months there is a strikingly large number that have suffered particularly badly from the containment measures. These include catering and accommodation as well as the entire passenger transport sector and travel agencies. According to the same source, the employment intentions of service providers also increased sharply. This development is the result of accelerated vaccination progress and rapidly falling incidence levels. Easing measures are now being implemented in rapid succession. These in turn are already having a positive impact on the dynamics of the domestic economy and consumer sentiment. According to GfK, the latter rose for the second consecutive time in June. The marked improvement in employment prospects and the prospect of wage increases should further boost sentiment in the second half of the year. Against this background, the German parliamentary elections in September will become the dominant topic. The latest election polls indicate that the traditionally fiscally conservative parties CDU, CSU and FDP have recently gained in popularity. Voter preference in tax matters will have fiscal implications beyond national borders.

#### Inflation

Swiss Life Asset Managers	Consensus
2021: 2.4%	2021: 2.5%
2022: 1.3%	2022: 1.7%

The annual rate of change in the Harmonised Index of Consumer Prices (HICP) will climb from the current 2.1% to 3.4% by November, before falling below 1.5% in the first quarter of 2022. While the Germans are tending to talk up the inflation risk in particularly drastic terms, it is precisely here that the temporary causes of its rise this year are particularly obvious.

## France

### The matter of the extra time

#### GDP growth

Swiss Life Asset Managers	Consensus
2021: 6.0%	2021: 5.5%
2022: 3.1%	2022: 3.9%

France is currently making its experiences with “extra time”. The hesitant easing of containment measures has been followed by a football defeat by its small neighbour, and politicians are suddenly uncertain whether Emmanuel Macron's presidency will be extended for a further five years next year. The resurgence of the traditional parties in regional elections makes for an exciting starting point for the election campaign. The comparatively widespread scepticism about vaccination in France may explain the slowdown in the pace of the vaccination campaign. Together with the spread of the delta variant, it poses a risk to the pick-up in the service sectors. However, the general economic mood at the beginning of the summer months is consistently encouraging: Business sentiment indicators continue to point to a strong upswing, which is increasingly also involving medium-sized companies. In the light of the elections, fiscal policy will continue to support the economic upswing in the coming months. In addition to his success in fighting the pandemic, President Macron will likely be judged by voters on his promise to bring the unemployment rate down to 7%. Despite a recession in 2020, this target remains within reach: At the end of the first quarter of 2021, the unemployment rate stood at 7.8%, down from 8.9% in the third quarter of 2020.

#### Inflation

Swiss Life Asset Managers	Consensus
2021: 1.4%	2021: 1.4%
2022: 1.3%	2022: 1.2%

The inflation rate has recently been 1.8%. The trend over the coming months will remain highly volatile. In July, a strong base effect will cause a one-off, sharp drop in the annual rates of change. However, easing measures in the services sector will lead to a rise in prices in the subsequent months.

## UK

### "Freedom Day" delayed

#### GDP growth

Swiss Life Asset Managers	Consensus
2021: 6.1%	2021: 6.6%
2022: 4.3%	2022: 5.3%

COVID-19 case numbers have soared since the end of May due to the rampant delta variant and are at their highest level since February. Prime Minister Johnson has therefore postponed "Freedom Day," the lifting of all restrictions in England, by four weeks to July 19, to give the vaccination campaign more time. Great Britain initially focused on providing as many people as possible with a first jab, but there is still some catching up to do with the second doses, with which protection against the delta variant should increase significantly. The delay in the opening plan is likely to have only a minor impact on the growth path. Although the Purchasing Managers' Index (PMI) for the services sector cooled slightly in June, it remains comfortably in growth territory. The monthly activity data also performed better than expected, which is why we upgraded the 2021 GDP forecast slightly. As expected, however, Brexit continues to put a brake on the UK economy. Export order intake is more sluggish than elsewhere in Europe according to the PMI survey, indicating continued uncertainty as regards trade relations. The precise implementation of the Northern Ireland Protocol remains a bone of contention and is a stubborn dispute which is currently holding back progress in other areas and, at worst, could lead to retaliatory measures such as tariffs.

#### Inflation

Swiss Life Asset Managers	Consensus
2021: 1.7%	2021: 1.7%
2022: 1.8%	2022: 2.3%

After a few quiet months, the UK also faced an inflation surprise. In May, headline inflation soared from 1.5% to 2.1%. The reopening of the economy seems to have had a stronger-than-expected impact on the prices of affected goods and services, such as catering. We have thus raised the inflation forecast for 2021 as a whole from 1.4% to 1.7%.

## Switzerland

### Back to pre-crisis level

#### GDP growth

Swiss Life Asset Managers	Consensus
2021: 3.6%	2021: 3.5%
2022: 2.5%	2022: 2.9%

By the end of the second quarter of 2021, we expect Switzerland's gross domestic product (GDP) to have returned to the Q4 2019 level. The newly developed weekly economic activity index of the State Secretariat for Economic Affairs (SECO) has been continuously higher since the end of May than it was before the lockdown in spring 2020. After a mild setback in the first quarter of 2021, during which real GDP contracted by 0.5% from the previous quarter, the pace picked up again with the rapidly implemented easing measures. Our own estimate of the contraction in GDP at the beginning of the year was very close to the official figure and did not result in a revision of the full-year forecast. Elsewhere, on the other hand, the need for adjustment seemed greater, as evidenced by the rise in the consensus forecast for 2021 from 3.3% previously to the current level of 3.5%. However, we are now more confident that the procyclical impetus from monetary and fiscal policy in the western economies will have a longer-lasting positive effect on Switzerland's export economy. As the vaccination drive has also accelerated significantly of late, we are raising the forecast for GDP growth in the coming year slightly. Even if the pandemic produces a fourth wave, we expect the economic damage to be lower again than in the period between October 2020 and March 2021.

#### Inflation

Swiss Life Asset Managers	Consensus
2021: 0.5%	2021: 0.4%
2022: 0.7%	2022: 0.5%

Representatives of the Swiss National Bank (SNB) recently made it clear that the rise in inflation rates will not lead to a change in the SNB's monetary policy. Instead, inflation in Switzerland is expected to remain reliably within the target range of 0% to 2% in the next few years. Following four deflationary phases since 2008, the SNB has thus achieved its objective of price stability.

## Japan Renewed mediocrity

### GDP growth

Swiss Life Asset Managers	Consensus
2021: 2.5%	2021: 2.6%
2022: 2.0%	2022: 2.8%

The Japanese economy seems once again caught in a kind of mediocrity. Sluggish vaccination progress, the ups and downs in COVID-19 case numbers and a moderately popular government that remains hesitant about the pandemic mean that nowhere else in the major developed world will the recovery of the economy in 2021 be as weak as in Japan. Admittedly, the contraction during the pandemic was also modest, but the latest economic data, ranging from retail sales to industrial production and the unemployment rate, have all been disappointing overall. Companies are not exactly radiating confidence either. While the Purchasing Managers' Indices (PMI) for manufacturing in most developed markets remained at historical highs in June, Japan's index remained barely in the growth zone after a significant contraction. Domestic demand seems to be particularly problematic at the moment, while orders from abroad have continued to improve. We expect economic momentum to pick up slightly in the second half of the year: The global upswing is progressing and will also drag Japan's export economy along, while some catch-up effects are to be expected in consumption. Nevertheless, our growth forecast remains on the cautious side for both 2021 and, in particular, for 2022 compared to the consensus estimate.

### Inflation

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

While the economic recovery is mediocre, the price trend in Japan is subterranean. Long-standing structural problems such as companies' low price-setting power, wage moderation and the general "deflationary mindset" of economic players mean that consumer price inflation remains at zero despite higher commodity and producer prices.

## China Few second-round effects

### GDP growth

Swiss Life Asset Managers	Consensus
2021: 8.2%	2021: 8.7%
2022: 5.4%	2022: 5.6%

China continues to pursue a zero-tolerance strategy in the event of local COVID-19 outbreaks. Recently, some clusters have appeared in the economically strong area of the Pearl River Delta, with corresponding sharp reactions from the authorities and effects on the production and shipment of export goods. In this respect, the recent acceleration of the vaccination campaign is encouraging. China is currently administering around 22 million doses a day, which is a world record in absolute terms and corresponds to 1.6% of the population. The effectiveness of the Chinese vaccine against the rampant delta variant remains questionable, as does the issue of whether the authorities will adopt a less drastic containment strategy with the increasing immunisation of the population. A change of course would certainly be good news for domestic consumption, which has been disappointing as of late, mainly due to cautious monetary and fiscal policy. Meanwhile, the export economy is benefiting from strong global demand for consumer goods, even if higher prices currently overstate Chinese foreign trade figures somewhat. Ironically, the easing of restrictions in the developed world, which should result in a shift in demand away from consumer goods towards services in the second half of the year, constitute a certain risk for China's export-driven recovery.

### Inflation

Swiss Life Asset Managers	Consensus
2021: 1.3%	2021: 1.5%
2022: 2.3%	2022: 2.3%

Producer prices continued to rise to 9.0% in May owing to higher commodity prices. As with the last uptrend in producer prices in 2016/17, we expect only minor second-round effects on consumer price inflation. The latter rose from 0.9% to 1.3% in May, mainly driven by a positive base effect, and is expected to climb to over 2% by the end of 2021.

## Economic Research



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



**Damian Künzi**  
**Economist Developed Markets**  
damian.kuenzi@swisslife.ch  
@kunzi\_damian



**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



**If you have any questions or if you would like to subscribe to this publication,**

please send an email to: [info@swisslife-am.com](mailto:info@swisslife-am.com).

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