MARKET BROKER

Sector Focus

Third Quarter Outlook

U.S. - The U.S. economy's momentum will probably prevent a recession in 2022. But as borrowing costs rise due to the Federal Reserve's aggressive monetary policy and the weight of exceptionally high prices, it is difficult to imagine the economy surviving 2023 undamaged. Now, we expect the U.S. economy to increase by 2.4 percent in 2022 and 1.6 percent in 2023. (compared with 2.4 percent and 2.0 percent , respectively, in May). The labor market is still tight and will stay there until the beginning of 2023, when it will start to rise as the effects of subsequent Fed rate increases become more pronounced. We now anticipate that the jobless rate will surpass 4.3 percent by the end of 2023 due to the economy's pressures getting worse as the Fed tightens its purse strings.

Given recent inflation developments, the Fed will now be much more aggressive: we see the policy rate rising from zero at the beginning of 2022 to 3% by year-end, reaching 3.50%-3.75% by mid-2023. The Fed will keep monetary policy tight until inflation decelerates and nears its target in the second quarter of 2024. Our lower GDP and inflation forecasts for 2023 and 2024 reflect this more aggressive stance.

Europe - We have lowered our GDP growth forecasts modestly for the eurozone economy. We now expect 2.6% growth this year and 1.9% next year (from 2.7% and 2.2% in our interim forecasts in May). Higher inflation drives our downward revision. We now expect consumer price inflation to reach 7% this year and 3.4% in 2023 (from 6.4% and 3% previously) on the back of higher energy and food prices resulting from geopolitical tensions. Lower international demand, particularly from China, is also expected to dampen growth. With pay increases falling short of covering increasing prices, consumers are beginning to feel the pinch on their purchasing power. Although less so than three months ago, we still anticipate sizable pandemic-related saving buffers and pent-up demand for services to keep consumption rising. This is because the instability in the financial markets is reducing net worth. The growth is clearly at risk from negative factors.

We anticipate that the ECB will increase all three policy rates by 25 basis points in July, and by another 25 basis points at least in September. We observe the ECB's policy rates peaking at neutral, in contrast to the U.S. Federal Reserve (around 1.5 percent).

Asia-Pacific - The prospects for the Asia-Pacific region are generally positive, notwithstanding war, increased inflation, and interest rates. The exception is China, where we anticipate that due to difficulties brought on by the COVID-19 lockdown, it will miss its growth goal. We further reduced our baseline 2022 growth prediction for China to 3.3% because to the slower-than-anticipated removal of COVID restrictions and the country's weak domestic demand recovery.

The post-COVID domestic recovery is largely still going strong outside of China. In particular, in countries with economies that are comparatively more driven by domestic demand, including India, Indonesia, and the Philippines, we anticipate strong economic growth in 2022–2023. However, the beginning of the normalization of monetary policy in many nations has been mostly influenced by growing inflation; all central banks in the region, with the exception of four, have begun to increase their policy rates. The avoidance of external pressure in the face of rising interest rates worldwide is the second major driver. Up to this point, capital outflows and currency devaluation in relation to the dollar have been controlled. But in order to stabilize inflation expectations and protect against external vulnerability, we anticipate that the majority of central banks will keep raising their policy rates.

Emerging Markets - Across the board, we increased our projection for consumer price inflation. Compared to our March forecasts, annual average inflation in a median EM will be 7.1 percent in 2022 and 4.1 percent in 2023, an increase of 1.2 and 0.6 percentage points, respectively. This higher inflation reflects the greater decline in consumer purchasing power and the resulting decline in real domestic demand for the rest of 2022 and 2023.

Even while we anticipate a return to lower inflation in the upcoming quarters, many EM central banks' target inflation level is still expected to be exceeded for some time. We now anticipate that, despite deteriorating economies, the pace of monetary policy tightening will step up across the majority of EMs. This is due to a combination of this and the U.S. Federal Reserve and other major central banks signaling a quicker policy tightening.

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