AXA Investment Managers

28 September 2022

Investment Institute Macroeconomics

Monthly Investment Strategy

Summer passes, winter's coming

Key points

- An energy crunch appears to be materialising with Germany and CEE countries most affected.
- We forecast recession in the Eurozone, with a sharp contraction in coming quarters. The UK also looks set to experience recession, despite a fiscal package that has undermined confidence in UK markets.
- Chinese activity struggles on housing restructuring and COVID. We lower our 2022 growth outlook to 3%.
- US activity has been mixed, with falling gasoline providing short-term relief. Still there is overwhelming expectation of stagnation or outright contraction.
- The Fed continues to tighten policy aggressively. While most other central banks follow, the dollar continues to rise, threatening broader instability.
- Financial conditions have tightened. The rate outlook will ease only once tighter conditions visibly slow growth.

Global Macro Monthly

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Summer passes, winter's coming

Global Macro Monthly Summary September 2022

David Page
Head of Macro Research
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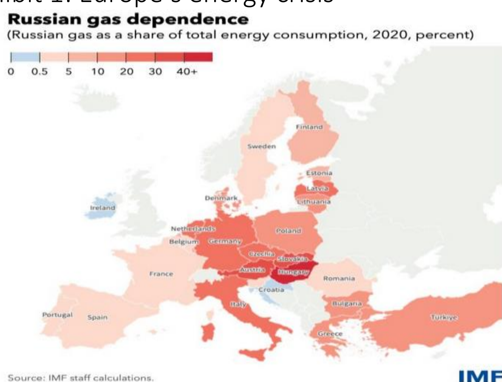
Outlook begins to darken

The prospect of an energy crunch has been ever-present since the Russian invasion of Ukraine. But as the nights draw in across the Northern Hemisphere, the economic realities this presents are coming into sharper relief. Europe faces the prospect not only of a gas-price-driven cost-of-living shock, but for some economies outright energy shortages and rationing. Our assessment suggests Germany, along with some of the more gas-dependent Central and Eastern European (CEE) economies (Exhibit 1), will have to restrict gas usage this winter – despite the fact that Germany has already reduced consumption by around 20%. This list could be longer, to include Italy if it cannot lower its consumption a further 2ppt to 10%; to include the UK in the event of a severe winter; and at the extreme France if its nuclear plants continue to struggle. This will depress output this winter, but restrictions will likely remain next year to prevent next winter facing the same challenges.

Exhibit 1: Europe's energy crisis



The energy shock is likely to lead to a Eurozone recession, led by the hobbled German industrial economy. We see a sharp contraction in Q4 2022 and Q1 2023, before modest growth resumes in the spring. We are also likely to see recession in the UK, despite a huge fiscal package unveiled by the latest Conservative government – its seventh economic policy reset in 12 years. UK stimulus has focused on energy relief, but medium-term tax breaks will take effect from the spring, after expected contraction this winter. Yet the unfunded package of fiscal easing has resulted in a sharp loss of confidence in sterling markets.

China continues to suffer from its housing restructuring, with the authorities ring-fencing the fallout while allowing a broader adjustment. It also faces an ongoing battle with COVID-19, even as the authorities experiment with less restrictive reactions. The focus is switching to next month's Party Congress, but we do not expect this to be a turning point for either of the above. We have lowered our growth outlook to 3% for this year and look critically at next.

Only the US is more mixed, with lower gasoline prices and a quick pass-through of easier supply conditions providing relief – albeit after two consecutive quarters of falling GDP. Yet even here the outlook is for slower growth. Some 80% of economists surveyed by Bloomberg expect zero or falling growth over the next two years, whether labelled recession or not – we forecast a mild recession. Ongoing pressure on real incomes, corporate margins and inventory threatens to slow growth further. But the Federal Reserve (Fed)'s unflinching resolve to restore price stability, focusing on backward-looking data while tightening using tools with long and variable lags commits the economy to "sub-trend" growth in the Fed's words – recession in ours.

The Fed is not alone in its hawkishness. The European Central Bank (ECB) and Bank of Canada both hiked rates by 75bps this month, the latter taking rates to the highs of its developed market peers. The Bank of England delivered only 50bps, but we think will move faster next meeting now it has full sight of the government's fiscal easing. Broader policy increases have not offset the relentless drive of the US dollar, now at 20-year highs against a basket of currencies. If currencies are weakening against the dollar where central banks are tightening, but not as quickly as the Fed, spare a thought for the yen. The Bank of Japan's consistent monetary easing has seen the yen hit 24-year lows, prompting intervention for the first time since 1998.

The combination has been brutal for financial conditions, with sovereign yields rising and risk assets – particularly equities – coming under greater pressure. Rate markets are reflecting the prospect of ever more aggressive central banks and relief is only likely once evidence emerges that conditions are loosening economic excess demand. The first signs of this might be on the cards in Canada, where employment has fallen for three months. The UK and even the US have also exhibited tentative signs of looser labour market conditions – but not enough to bank on yet. Nevertheless, if activity continues to slow into year-end, such signs should become more widespread. For now that is our forecast, but for central banks and markets to respond there will need to be much clearer evidence that this is becoming a reality.

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Global Macro Monthly – US

David Page
Head of Macro Research
Macro Research – Core Investments

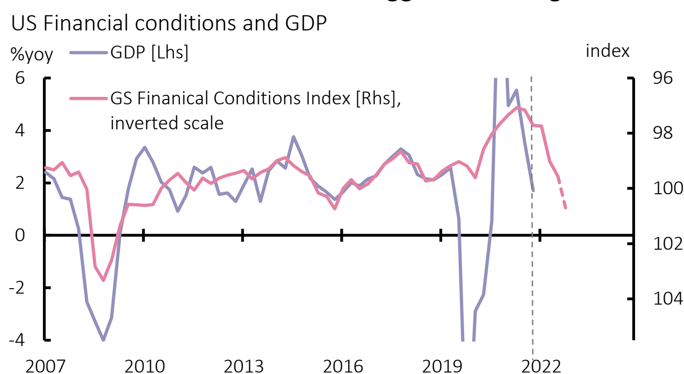
How quickly will economic slowdown temper policy?

The summer's news confirmed a much weaker US economy. Q2 GDP repeated Q1's surprise, falling by 0.6% annualised (Q1 was -1.6%). Two successive quarterly declines constitutes recession in most economies but the US National Bureau of Economic Research makes a broader assessment. While Q1 was hit by rising port activity and surging imports, Q2 reflected a sharp drop in inventories. However, final domestic sales were flat in Q2 – the weakest since the pandemic in 2020. The weak start has reduced the growth outlook for 2022 (Exhibit 2).

More recent evidence is mixed, leading the Federal Reserve (Fed) to describe recent indicators as suggesting "moderate growth" from "have slowed". Key surveys stabilised and consumer sentiment rose a little. This has coincided with a bounce in housing starts, labour supply, falling high-frequency jobless claims and a narrowing trade deficit. Falling gasoline prices and improving supply conditions have helped and we forecast this to support a 0.8% expansion in Q3, albeit mindful the Atlanta GDPNow tracker currently suggests a softer 0.3%. Longer term, a still-sharp squeeze on real incomes, pressure on corporate profits, tighter financial conditions and slowing inventory growth lead us to anticipate a GDP contraction by year-end and the start of a mild recession. We forecast growth of 1.4% in 2022 and -0.3% next year (consensus 1.6% and 0.9%).

Exhibit 2: Financial conditions suggest weaker growth

US Financial conditions and GDP



Source: Bureau of Economic Analysis, Goldman Sachs and AXA IM Research, 27 Sep-22

Despite this backdrop, the labour market remains resilient. Vacancies remain elevated, albeit having started to ease but unemployment remains low at 3.7%, although this also reflects reduced labour supply, despite a strong 0.5% monthly rise in August. Payrolls remain robust, rising by an average monthly 350k in Q2 and on track to deliver similar in Q3. This is anomalous with previous periods of weak growth. Other measures, including household and ADP surveys point to weaker growth. There is tentative evidence the labour market is starting to ease but overall conditions remain tight.

Annual CPI inflation fell to 8.3% in August, led by gasoline price falls but core inflation surprised, rising to 6.3%. On the month, core inflation rose by 0.6% following a more subdued 0.3% in July, with gains in clothing and other goods, combining with rising medical and education costs and supplementing persistently solid housing and shelter costs. August's core strength should not be repeated; we expect CPI to fall more visibly after September and forecast a slower decline than the consensus, in part reflecting an expectation that shelter and non-cycical services inflation will stay firm. We expect headline inflation to average 8.2% in 2022 and 5.2% in 2023 (consensus 8.0% and 3.7%). Importantly though, inflation expectations appear to be easing, with the Michigan University 5-10 year measure back to 2.8% and the Fed's consumer expectations survey falling further at 1,3 and 5-year tenors.

The Fed raised rates by an aggressive 0.75% to 3-3.25% in September. Its projections for year-end increased by 100 basis poinst (bps) from June, implying a 0.75% hike in November, 0.50% in December (to 4.50%) and another 0.25% next year to peak at 4.75%, before easing in 2024. The Fed requires signs of an easing labour market and "compelling evidence" of softer price pressures to ease the pace of tightening. But we expect these conditions to be met with the economy entering a mild recession by year-end; a more material slowdown than the "below trend growth" projected by the Fed. The Fed was evenly split (9 to 8) in September between rates at 4.25% and 4.50% by year-end and this should tip the balance in favour of 4.25%. If the economy is in recession by year-end we do not expect further tightening in 2023, although equally we see the Fed on hold for the year. That said, GDP has been erratic and the labour market and prices more resilient than expected. If this continues, the Fed will follow through with its projected hikes and more until job and price growth eases – albeit at the risk of a deeper downturn in activity.

Midterm elections loom. Incumbent parties tend to fare poorly at midterms and President Joe Biden's low approval ratings make him an unlikely exception. However, his ratings have risen over the last three months, while the Supreme Court Dobbs vs. Jackson ruling on abortion and former President Donald Trump's interventions in key Republican primaries appear to have shifted the odds for the Democrats retaining a Senate majority. We still expect them to lose the House, which will result in policy gridlock either way. But this will be important ahead of 2024's Presidential Election.

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Global Macro Monthly – Eurozone

François Cabau,
Senior Eurozone Economist
Macro Research – Core Investments

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Eurozone Economist
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Gas rationing leading to recession

We have moved our baseline outlook to a recession, projecting a cumulative 1.6% euro area GDP contraction between Q4 2022 and Q1 2023 – from a mild contraction in Q4. Necessary gas rationing during the winter at least in Germany and Italy is the main driver of the deeper retreat – with supply woes dominating the outlook despite soothing global supply chains.

Material gas consumption reduction, happening since the summer in Germany, implies the country is likely already in GDP contraction in Q3 (-0.4%qoq projected). September's flash PMIs suggest the euro area as a whole is flirting with economic contraction as early as Q3. PMIs suggest services can no longer offset manufacturing weakness and in fact has contracted for a second consecutive month.

Recovery from the winter is likely to be protracted. Countries will emerge with very low gas storage levels, requiring continued efforts (given no return of Russian supply expected) to replenish stocks ahead of the following winter. The policy mix is also likely to be much tighter than post-COVID-19, with inflation still high. Consistent with our revised 2023 GDP growth forecast at -0.5%, we project the level of euro area GDP to be lower than it is now at the end of our forecast horizon. Even accounting for a significant revision, at -1.2 percentage points (ppts), we continue to see risks skewed to the downside.

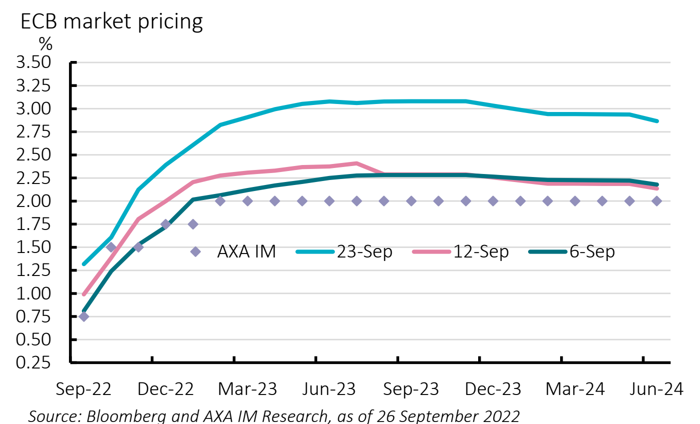
Inflation is also likely to stay high for longer. The Harmonised Index of Consumer Prices is likely to peak at 9.6%yoy in September – chiefly highlighting the impact of volatile components and we believe core will accelerate again to 4.7%yoy at the euro area level. Cost pressures – euro depreciation, energy costs and wages – remain material on non-energy industrial goods, despite supply bottlenecks easing. Looking ahead, we have revised up our 2023 inflation forecasts to 5.5% (from 4.4%) mostly due to energy components as energy contracts are renegotiated and government support not as wide ranging. We revise our core view up to 3.3% (+0.4ppts) boosted by wage increases and energy pass through effects.

ECB: Heading to upper-end of neutral

ECB interest rate increase frontloading looks set to continue. After an historic 125 basis point (bps) rate hike in just two meetings, we expect it to hike its deposit facility rate (DFR) by another +75bps to 1.5% in October, wary about inflation being "far too high above target" for too long, risking an unanchoring of inflation expectations, even as wage developments remain moderate. Given the latter and our expected material output drop, not in ECB's baseline, we forecast a more moderate +25bps in December and February bringing the DFR to 2%.

We see three main risks for rates rising further. First, at its September meeting, the ECB Governing Council argued explicitly in favour of "further dampening demand" while President Christine Lagarde[1] reiterated her mantra from Sintra that persistent supply shocks would be consistent higher rates not lower. Secondly, market expectations for the DFR have increased substantially, staying at around 3.0% from mid-2023 (Exhibit 3), reflecting US rate expectations. Despite this significant repricing, the euro reached a new 2022 low and these exchange rate concerns could also justify hiking rates faster higher, especially if mirrored in nominal effective terms. Third, there is the policy response from governments fuelling additional inflation pressures.

Exhibit 3: Market firmly pricing ECB in restrictive territory



Source: Bloomberg and AXA IM Research, as of 26 September 2022

Historical win for Italian centre-right

As expected, Brothers of Italy and the centre right coalition won Italy's general election. A better than expected score for Forza Italia versus Lega may limit BTP[2]-Bund spread widening pending the new government's formation – which should take about a month and its first steps. As seen in market price action since the election outcome, we think market complacency is unlikely to last into 2023, notably owing to medium fiscal sustainability concerns. Political (in)stability will remain a wild card.

[1] Lagarde, C., "Monetary policy in the euro area", ECB speech, 20 Sep-22

[2] *Buoni del Tesoro Poliennali*

Global Macro Monthly – UK

Modupe Adegbembo
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Macro Research – Core Investments

Pound sinks as investors fear Tory plan

Less than one month into its premiership and the Liz Truss government has appeared to push the UK towards a currency crisis. The pound fell to an all-time low of $1.035 to the US dollar in a continued sell-off following Chancellor Kwasi Kwarteng's first fiscal announcements. The Chancellor had outlined plans to drive the UK economy into a "new-era" and raise underlying trend growth to 2.5%. Markets were unconvinced by the large, unfunded fiscal easing, triggering a sell-off in UK assets following the announcement. Official estimates show the growth plan (excluding energy bills support) is expected to cost £160bn over the next five years (just under 6% of GDP) but this figure balloons when energy bills support is included which is expected to cost £60bn this financial year alone.

Most of the policy announcements were not a surprise, with Prime Minister Truss previously committing to cancelling the planned increase in corporation tax and reversing the recent increase in National Insurance. The government also brought forward to 2023 from 2024 a planned decrease in the basic rate of income tax and removed the additional higher rate of income tax. The government has faced considerable criticism over the regressive nature of these tax cuts during a cost of living crisis. Despite the scale of the plan, the government included no analysis of the impact on public finances. A full assessment from the Office of Budget Responsibility (OBR) is expected before year-end.

The Chancellor added to market pressure by stating there was "more to come". After a febrile few days, markets were factoring in a rise in the UK benchmark Bank Rate to 6% amid the uncertainty. There was also speculation the Bank of England (BoE) may be forced into an intermeeting hike. It is not obvious this would quell market fears, but we expect to see further communication from key policy makers, both at the BoE and in UK government, in the days to follow.

The additional fiscal stimulus jars with the BoE's aim of tempering demand to restore price stability – it will likely see it hike more. We now expect rates to reach 4% early next year compared to 3.50% prior. We expect the BoE to hike the bank rate by 75bps in November but a continued slide in the pound could see them do more. In addition, we now expect a 50bp hike in December and two 25bp hikes in February and March.

Global Macro Monthly – Canada

David Page
Head of Macro Research
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Growth starting to slow, BoC not much further to go

There are growing signs that tighter financial conditions are starting to take effect. The economy expanded briskly in the first half of 2022, rebounding from the end-year Omicron spread. Yet since May, growth has been lacklustre. Following a 2.5% decline in retail sales in July we see stagnant output, which should result in deceleration in Q3 GDP to 1.2% annualised. With our broader expectations for global deceleration, including a fall in key US GDP in Q4, we forecast Canada to slow to a standstill by year-end, leaving annual growth at 3.3% (from 3.5% in July), a view the market now shares. Growth should revive next year as inflation fades and investment rises, but we see this as a second-half story. For now, we expect 2023 GDP at 0.7%, below the consensus 1.1%.

Slower growth is beginning to impact the jobs market. Employment has contracted for three consecutive months and while falling labour supply kept unemployment low until July, a rebound in August saw unemployment rise to 5.4% from 4.9% – still historically low but easing. We expect only gradual labour supply recovery ahead, but weak economic activity will likely see jobs stagnate. We forecast unemployment rising gently to 5.7% by year-end, but to move higher towards 6.5% over 2023.

Inflation also appears to be easing. The headline Consumer Price Index (CPI) fell to 7.0% in August from 7.6%, largely driven by falling energy costs, but measures of core inflation also eased on the month. Inflation remains above the Bank of Canada's (BoC) target and could edge up again if energy tensions, particularly in the oil market, re-emerge before year-end. We lower our forecast for inflation this year to 6.8% (from 7.0%), modestly below consensus of 7.0%, but expect a slower decline next year at 4.3% vs 3.4%.

The BoC could thus be close to completing its rate hikes. This would be consistent with the aggressive 'front-loading' of hikes, leaving the bank rate among the highest of its peers. It also fits with September's guidance as the BoC said it was "assessing how much higher interest rates need to go", compared with three months ago, when it was "prepared to act more forcefully", preceding 175bps of tightening. We still expect the BoC to tighten further and expect a 50bp hike in October but the economic slowdown should make this the last. This would leave the Bank Rate at 3.75%, although we acknowledge the risk of a final 0.25% hike in December in line with the consensus view of a 4.00% peak.

Global Macro Monthly – China

Aidan Yao
Senior Economist (China)
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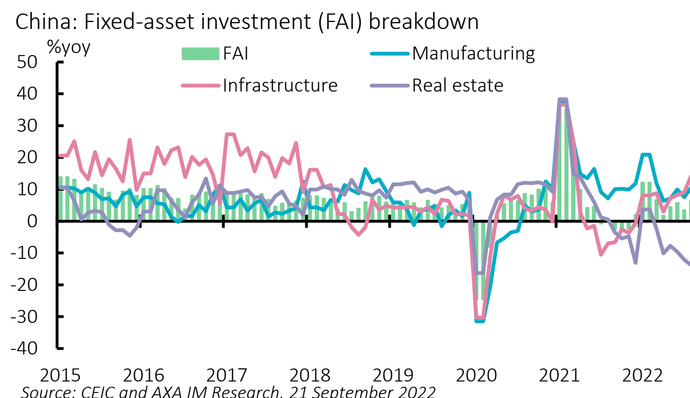
August data unexpectedly improves…

August data comfortably beat market expectations, suggesting parts of the economy gained, rather than lost, momentum after a weak start to Q3. Industrial production growth accelerated to 4.2%, the highest since March. Manufacturing output grew by 3.1%, improving from July. The biggest growth contributor was utility and power production, as power usage surged in response to an unusually hot summer. Auto production also maintained strong momentum thanks to buoyant car sales on the back of government subsidies.

Investment activity improved visibly. Infrastructure construction was again the bright spot, with growth accelerating to 14% from 9% (Exhibit 4). Even though local government bond sales have largely stalled since June, there seems to have been enough unused funds to support an acceleration of project approvals in the past two months. The momentum in the sector is likely to last well into the year end.

Exhibit 4: Investment picture improves outside real estate



Source: CEIC and AXA IM Research, 21 September 2022

Encouragingly, growth in manufacturing capital expenditure (capex) also quickened to a five-month high. It is not clear whether this reflects a genuine recovery of business confidence – which would be puzzling given ongoing fallout from COVID-19 and the real-estate turmoil – or a lagged response to previous export strength. If it's the latter, falling export growth recently will bode ill for the outlook.

The property market remained the single biggest drag on the economy. House sales continued to fall at a double-digit pace, even though year-on-year growth improved slightly from a low base. The government's push to restart unfinished projects may support construction somewhat from September. But in general, we expect the real estate adjustment to last, even though year-on-year growth may improve from last year's low base.

Retail sales were the biggest upside surprise. Headline growth nearly doubled from July's level to 5.4%, flattered by base effects. Goods sales growth strengthened to 5.1%, but the services sector did better despite the worsening COVID-19 situation. It is possible that Beijing's more lenient pandemic management provided the sector with more breathing room at the start of the current outbreak. However, with some big cities now under social and mobility restrictions, consumption may struggle to sustain this level of buoyancy in September.

… but not enough to prevent another growth cut

Overall, notwithstanding the positive August data, the most up-to-date developments seem to suggest the economy is not out of the woods. Fortunately, Beijing has started to react after a few months of policy hiatus. On the pandemic front, despite facing a more contagious outbreak than in April/May, the authorities have so far refrained from locking down highways and ports to prevent another Shanghai-style hit to the nation's supply chains. True, a few large cities are now under community restrictions, but most have avoided a blanket lockdown, with Chengdu – under the strictest controls – still permitting firms to operate on a closed-loop basis. Compared to Shanghai a few months ago, the current approach should help to mitigate, albeit not eliminate, the impact of the outbreak.

Beijing has also acted to manage the property market turmoil. Moves to speed up construction of unfinished projects and guarantee bonds issued by fundamentally-sound private developers are consistent with the authorities trying to ringfence the crisis and minimise spillovers. However, without a holistic plan to tackle deep-seated imbalances, these contagion-risk-management measures will prove insufficient to resolve the crisis within the sector. The market is pinning hopes on the Party Congress, and subsequent policy meetings, for signals of a comprehensive strategy to get the sector out of its predicament.

Finally, counter-cyclical policy easing has also restarted. Cutting deposit/lending rates and granting more bond issuance quotas to local governments to support infrastructure investment are moves in the right direction. But the steps are still too small to make a difference for an economy confronting stiffening headwinds. With the Fed hastening the pace of rate hikes, the CNY/USD crossing 7, and COVID-19 controls blunting policy easing effects, the odds of Beijing unleashing large stimulus in the coming months are low. We have therefore downgraded our Q3 and Q4 growth forecast, putting full year growth at 3%, down from 3.6%. The 2023 forecast of 5.2% is kept unchanged for now, as we await the upcoming political events to guide China's pandemic and economic policies for next year.

28 September 2022

Global Macro Monthly – Japan

Modupe Adegbembo
Junior Economist (G7),
Macro Research – Core Investments

Yen weakness sees FX intervention from Japan

Japan's accommodative stance on monetary policy continues to stand out against the global trend. The increasing divergence between Japanese monetary easing and tightening conditions in most other developed markets has seen the yen face continued pressure, with the currency declining by 20% against the dollar year to date. This slide and increased speculation on the yen has pushed Japan's Ministry of Finance (MoF) to intervene in foreign exchange (FX) markets to support the yen for the first time since 1998. Following the intervention, the yen rose from lows of ¥145.8 against the dollar, but the move is likely to provide only a temporary reprieve as divergence between the policy stance of the Bank of Japan (BoJ) and other central banks, such as the Federal Reserve, continues to grow.

At its September meeting, the BoJ reaffirmed its commitment to accommodative policy and kept all policy measures unchanged. There was some adjustment to its COVID-19 support package, with the BoJ taking the decision to phase out its support for business. Governor Haruhiko Kuroda reaffirmed his commitment to maintaining the current easing stance. He also said side-effects such as the weak yen were not due to the BoJ's negative interest rate policy alone and made clear that he did not intend the BoJ to follow the path of moving away from negative interest rates which has been taken by other central banks.

Japan has also faced the powerful Typhoon Nanmadol, the strongest typhoon to hit the country since 2000 and the fourth strongest on record. A total of nearly eight million people in about 3.7 million households were ordered to evacuate from areas in southern and western Japan and at present two people have been reported dead or missing. Despite the scale of damage and disruption caused, it appears to have caused less economic damage than previous typhoons.

The government is preparing a new economic stimulus with a package expected to be worth ¥15tn–30tn. However, reports suggest it is likely to be funded largely by rearranging existing budget commitments with the result that a second supplementary budget may have only a limited additional economic impact.

Global Macro Monthly – EM

Irina Topa-Serry,
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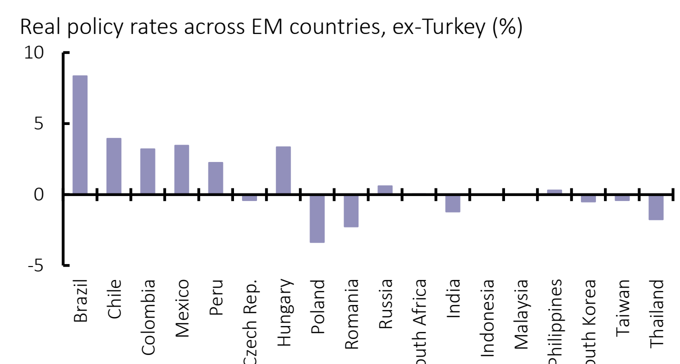
A 'cold' winter ahead

Europe is entering a difficult winter as the gas crisis intensified with the latest decision by Russia to shut off the Nord Stream 1 pipeline. Countries in Central and Eastern Europe, particularly reliant on Russian gas to varying degrees, are likely to experience a sharp output contraction in the coming winter quarters. Landlocked Hungary and the Czech Republic will be directly affected by gas shortages as well as second-round effects from weakening economic activity in Germany, their largest trading partner. We forecast a GDP growth contraction of four percentage points (ppt) cumulatively for Q4 2022 and Q1 2023 for both these countries. Poland, the biggest country in the region, imported around half of its natural gas supply and three-quarters of its oil from Russia in 2020, but its economy is less gas-intensive, with a greater reliance on coal. We expect Polish GDP to fall by 1.4ppt during the winter quarters. We now forecast GDP to contract by 2.4% in Hungary and by 1.8% in the Czech Republic next year, with growth at 0.9% in Poland.

Meanwhile, the combination of weak Chinese economic growth, higher US interest rates and a stronger dollar continues to weigh on emerging markets (EM) beyond Central Europe. Recession is looming for some big countries in Latin America, while Asia will still need to cope with a weaker China. Positive real policy rates could still offer some protection for capital flows and selected currencies (Exhibit 5), as some EM central banks have been hiking rates for quite some time, but that buffer will be eroded by the US Fed's future path of interest rates. Policy rates may have to stay higher for longer through EM which in turn could prove more painful for future growth.

Exhibit 5: Positive real interest rates buffer in EM

Real policy rates across EM countries, ex-Turkey (%)



Source: Bloomberg, Eikon DS, AXA IM Research, Sept. 2022 (using 2023 consensus inflation expectations)

Global Macro Monthly – Asia

Shirley Shen,
Economist (Emerging Asia)
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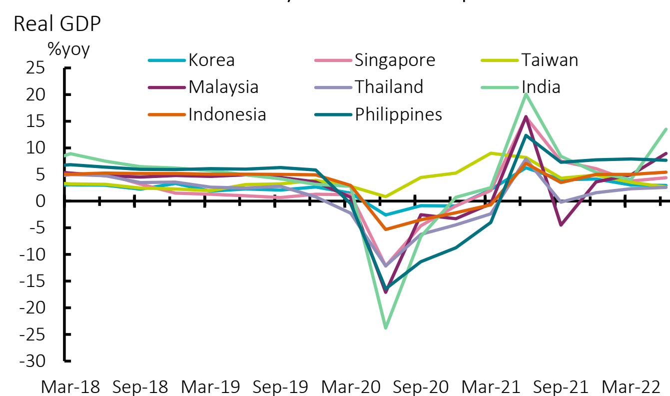
Growth anchor is shifting

Within Asia, growth seems to have generally recovered to pre-pandemic levels (Exhibit 6). However, despite some countries benefitting from an extended tech upcycle, weakening final demand from a global economic downturn has weighed on regional exports. In particular, export-dependent economies such as Korea and Taiwan have seen exports clearly weakening following last year's resilience. Meanwhile, the regional growth anchor appears to be shifting towards more domestic-oriented economies on strong domestic consumption/investment recoveries as well as the regional commodity exporters due to rising energy prices.

Exhibit 6: Growth mainly recovered to pre-COVID-19 level



Source: CEIC and AXA IM Macro Research, 21 September 2022

Headline inflation continues its uptrend. Since December 2021, Consumer Price Indices (CPI) across Asia have shown inflation accelerating by between 117 basis points (bps) in Malaysia and 570bps in Thailand. Local currency depreciation and the US Fed's aggressive monetary tightening served as catalysts for an even quicker policy normalisation in Asia. All central banks in the region have hiked by at least 25bps. Bank of Korea has been the most aggressive, hiking by 200bps, and at Jackson Hole, Governor Rhee Chang-yong indicated the bank was unlikely to halt its hikes before the Fed pauses. Central banks in Thailand, Indonesia and Malaysia have played down the need to closely follow the Fed, partly reflecting relatively benign core inflation.

Looking ahead, with persistent strength in the US dollar, we expect central banks in the region to intervene further with additional rate hikes through the remainder of the year, to smooth currency depreciation against the dollar and fend off inflationary pressure.

Global Macro Monthly – LatAm

Luis Lopez-Vivas,
Economist (Latin America),
Macro Research – Core Investments

Resilient growth across the region

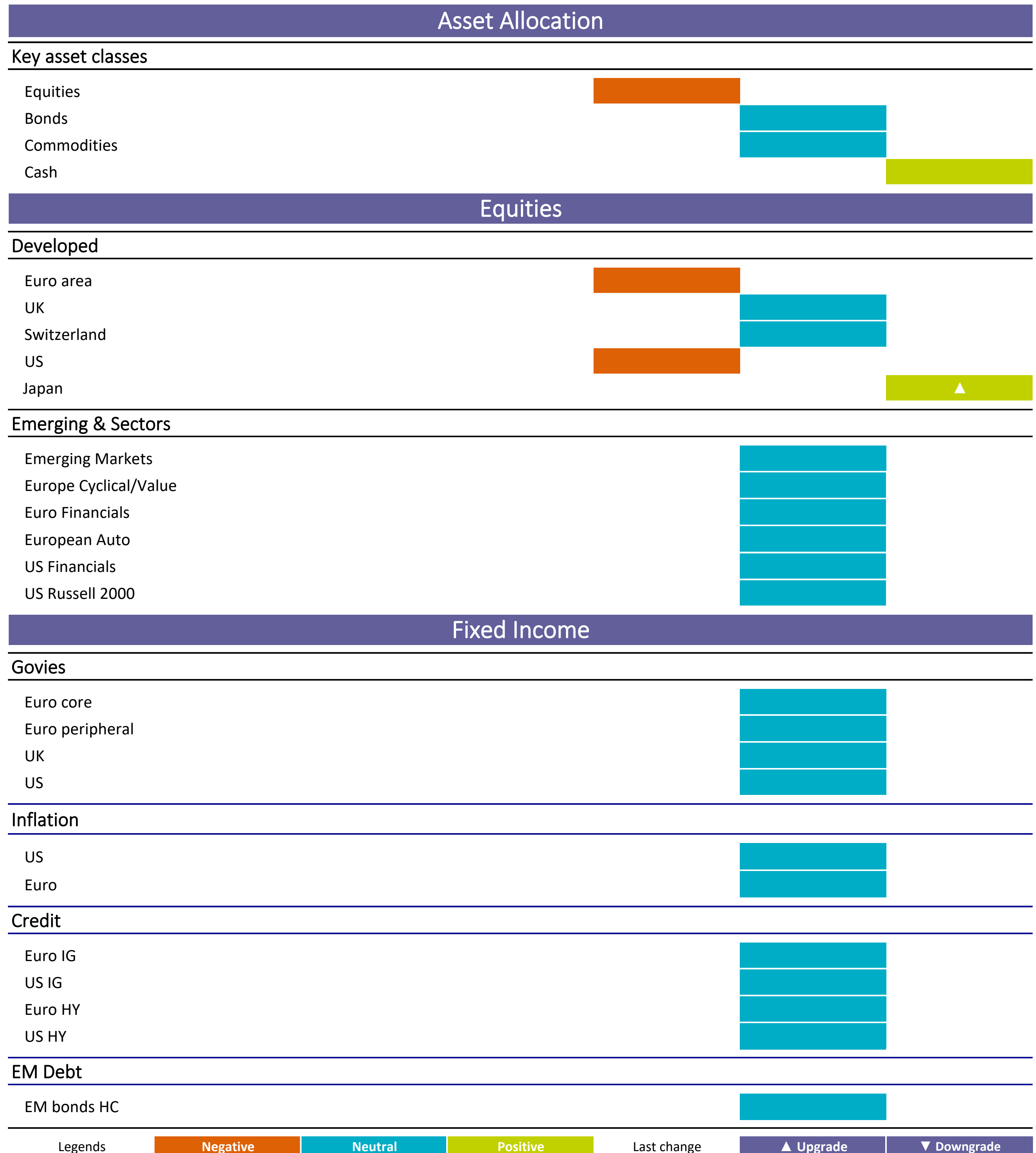
Economic growth in Latin America proved resilient in Q2 despite headwinds such as doggedly high inflation, a deep tightening cycle and the spectre of recession in developed markets. On a seasonally-adjusted quarter-on-quarter basis, GDP in the region accelerated to 1.1% (Q1: 0.9%). This better-than-expected performance was spearheaded by Colombia (+1.5%), Brazil (+1.2%) and Mexico (+0.9%). These economies continue to benefit from the ongoing commodity boom. Higher prices have not only fuelled exports but have also allowed governments to finance tax cuts and subsidies to protect consumers from rising energy costs. Likewise, elevated commodity prices along with moves by US companies to bring some production closer to home are providing an additional boost in the form of foreign direct investment inflows.

While also being large commodity exporters, the economies of Chile and Peru continue on a weak footing partly as the result of political turmoil. Chile fell into a technical recession as it contracted in Q2 for a second consecutive quarter (-0.01% quarter on quarter). The contraction came on the back of slowing consumption – inflation is at a 20-year high – and weaker fixed investment. Political uncertainty created by the referendum on the recently-rejected new constitutional draft had been weighing on investor sentiment since the process began. In Peru, quarterly economic growth was flat in Q2. Pedro Castillo's government is seen as weak and volatile, which is severely affecting business confidence and undermining investment. Social unrest has increased in the country, including blockades disrupting production in key copper mines.

On a more positive note, inflation has likely peaked in Peru – it decelerated for a second consecutive month in August. Annual inflation is also on a clear downward trend in Brazil, reaching 8.3% last month, the lowest since July 2021. These positive developments could allow the respective central banks to finally press pause on their hiking cycle after more than a year of relentless rate increases. In contrast, consumer prices keep rising in Chile, Colombia and Mexico which will likely force a tightening of monetary policy.

Moving into 2023, we expect growth in the region to significantly lose momentum as the global slowdown takes a toll on commodity prices in a context where inflation and policy rates will likely remain elevated in Latin America.

Recommended asset allocation



Asset Allocation	Negative	Neutral	Positive
Key asset classes			
Equities	■		
Bonds		■	
Commodities		■	
Cash			■
Equities			
Developed			
Euro area	■		
UK		■	
Switzerland		■	
US	■		
Japan			▲
Emerging & Sectors			
Emerging Markets		■	
Europe Cyclical/Value		■	
Euro Financials		■	
European Auto		■	
US Financials		■	
US Russell 2000		■	
Fixed Income			
Govies			
Euro core		■	
Euro peripheral		■	
UK		■	
US		■	
Inflation			
US		■	
Euro		■	
Credit			
Euro IG		■	
US IG		■	
Euro HY		■	
US HY		■	
EM Debt			
EM bonds HC		■	

Legends: Negative | Neutral | Positive — Last change: ▲ Upgrade | ▼ Downgrade

Source: AXA IM Macro Research – As of 28 September 2022

Macro forecast summary

Real GDP growth (%)	2021	2022*		2023*	
		AXA IM	*Consensus*	AXA IM	*Consensus*
World	6.1	3.1		2.4	
Advanced economies	5.1	2.2		0.1	
US	5.5	1.4	1.7	-0.4	0.7
Euro area	5.2	3.0	2.8	-0.5	0.9
Germany	2.6	1.3	1.5	-1.5	0.7
France	6.8	2.4	2.4	0.0	1.2
Italy	6.6	3.3	3.0	-0.6	1.1
Spain	5.1	4.7	4.3	0.6	2.3
Japan	1.7	1.5	1.4	1.7	1.6
UK	7.2	3.4	3.4	-0.2	0.1
Switzerland	3.5	2.3	2.5	0.6	1.2
Canada	4.4	3.3	3.5	0.7	1.5
Emerging economies	6.7	3.6		3.9	
Asia	7.0	4.4		5.1	
China	8.1	3.6	3.7	5.2	5.4
South Korea	4.1	2.3	2.6	2.0	1.9
Rest of EM Asia	6.1	5.6		5.2	
LatAm	6.8	2.8		2.0	
Brazil	4.6	1.5	1.8	1.0	0.8
Mexico	4.8	1.7	1.9	1.3	1.6
EM Europe	6.7	-0.7		-0.2	
Russia	4.7	-6.0		-3.5	
Poland	6.0	4.8	4.8	0.9	2.3
Turkey	11.5	5.6	3.7	1.5	2.3
Other EMs	5.4	4.2		3.7	

Source: Datastream, IMF and AXA IM Macro Research – As of 27 September 2022

CPI Inflation (%)	2021	2022*		2023*	
		AXA IM	*Consensus*	AXA IM	*Consensus*
Advanced economies	3.2	7.2		4.7	
US	4.7	8.2	8.1	5.2	3.8
Euro area	2.6	8.1	7.8	5.5	4.1
China	0.9	2.1	2.4	2.3	2.5
Japan	-0.2	2.3	2.0	1.3	1.4
UK	2.6	9.0	8.6	5.6	5.6
Switzerland	0.5	2.8	2.7	2.0	1.6
Canada	3.4	6.8	7.0	4.3	3.5

Source: Datastream, IMF and AXA IM Macro Research – As of 27 September 2022

These projections are not necessarily reliable indicators of future results

Investment Managers

28 September 2022

Forecast summary

Central bank policy						
		Meeting dates and expected changes (Rates in bp / QE in bn)				
		Current	Q3-22	Q4-22	Q1-23	Q2-23
United States - Fed	Dates	1.50-1.75	26-27 July 20-21 Sep	1-2 Nov 13-14 Dec	31-1 Jan/Feb 21-22 Mar	2-3 May 13-14 Jun
	Rates		+1.5 (3.00-3.25)	+1.0 (4.00-4.25)	unch (4.00-4.25)	unch (4.00-4.25)
Euro area - ECB	Dates	-0.50	21 July 8 Sep	27 Oct 15 Dec	2 Feb 16 Mar	4 May 15 Jun
	Rates		+1.5 (0.75)	+1.0 (1.75)	0.25 (2.00)	unch (2.00)
Japan - BoJ	Dates	-0.10	20-21 July 21-22 Sep	27-28 Oct 19-20 Dec	Jan Mar	May Jun
	Rates		unch (-0.10)	unch (-0.10)	unch (-0.10)	unch (-0.10)
UK - BoE	Dates	1.00	4 Aug 15 Sep	3 Nov 15 Dec	Feb Mar	May Jun
	Rates		+1.00 (2.25)	+1.25 (3.50)	+0.5 (4.00)	unch (2.50)

Source: AXA IM Macro Research - As of 27 September 2022

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28 September 2022

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