

Week Ahead

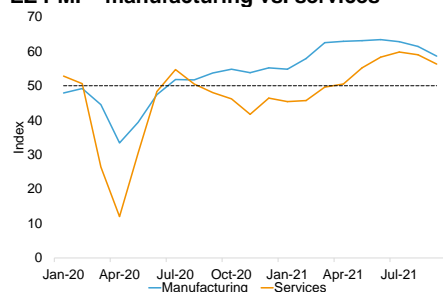
Focus: EZ PMI, Upswing and Inflation

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EZ PMI – manufacturing vs. services



Source: Market data provider, Erste Group Research

German Electricity price vs. CO₂-price



Source: Refinitiv, Erste Group Research

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Note: Past performance is not necessarily indicative of future results

EZ – will sentiment recover in October?

Next week, the first flash estimate of the October PMI data will be published for the Eurozone, Germany and France. In September, sentiment in manufacturing and among service providers weakened unexpectedly sharply. Supply problems and weakening demand weighed on manufacturing sentiment.

Now that the problems in global supply chains have worsened in some areas since September, we do not expect purchasing managers' sentiment to ease in October. The automotive sector in particular is currently suffering from the global shortage of semiconductors. In Germany, automotive production in July and August was already well below the previous year's level as a result. However, there have been first positive news in Asia in the last few days that give hope for an easing of the situation. For example, Intel will be able to increase its semiconductor production in Vietnam to 100% again soon after regional corona measures have been lifted.

In addition, the dramatic rise in energy prices is weighing on the costs of many industrial companies. Some energy-intensive sectors (e.g. fertilizer manufacturers) have already had to cut production in recent weeks. The rapid rise in energy prices has several causes. Among other things, the long winter in 2020/21 emptied gas storage facilities in Europe to long-term lows. In Asia, too, demand for natural gas has risen sharply as a result of the previous long winter. Unfavourable weather conditions, which had a negative impact on the energy yield of renewable energy sources, as well as climate policy measures exerted additional upward pressure on energy prices.

We currently consider the situation on European as well as global energy markets to be the biggest risk to the Eurozone's growth outlook in 4Q21 and 1Q22. Following a verbal intervention by Russia's President Putin, the situation on the markets has eased somewhat, but European gas and electricity prices are still far above historical averages. This is likely to have a dampening effect on private consumption in the coming months, as sharply rising energy costs will reduce households' available funds for other consumer goods and services. A recent report on the planned expansion of coal production in China initially calmed the Asian markets somewhat, after a number of industrial companies in China had to curb or completely halt production due to energy shortages. This also increases the risk of further aggravation of the problems in global supply chains.

The lopsided upswing

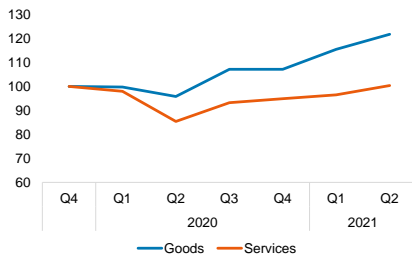
The most important question currently being discussed in the markets is the further development of inflation. In addition to reports of very high

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14. October 2021

US real consumption expenditures by category, Index Q4 2019 = 100



Source: US Bureau of Economic Analysis, Erste Group Research

inflation rates, ever new reports of supply bottlenecks are fuelling uncertainty. The prices of energy, raw materials, transport services have risen massively globally in 2021 and in the USA moreover for some product categories. The rapid ramp-up of the US economy was a major factor. But the underlying cause is more accurately a lopsided recovery. Not only did the US economy emerge very quickly, but there was also a major shift in demand from services to goods, which was amplified through huge public stimulus packages. While real consumer spending on services in Q2 2021 was just 0.3% above the pre-crisis level in real terms, spending on goods rose by almost 22% in the same period. As a share of GDP, spending on services fell by 2 percentage points, while the share of spending on goods rose by 3.4 percentage points. This was accompanied by a massive increase in US imports, which in turn increased demand for freight capacity and raw materials, thus driving up prices globally. Strong demand for housing in the US added to this pressure. The situation in the Eurozone is similar in that demand for goods also recovered faster than for services. The difference, however, lies in the level. Spending on goods has more or less only reached the pre-crisis level, while spending on services is still far below. All in all, however, it was a lopsided upswing here, too.

Overall, it is therefore more accurate to speak of excess demand than of supply bottlenecks. Looking at the consequences it doesn't make much difference, but the cause is easier to identify. The reasons for the shift in demand to goods were manifold and were reinforced by the large stimulus packages in the US. However, the lack of availability of services and continued caution on the part of consumers was certainly decisive. These factors should subside and with them the imbalances in demand. This should ease supply-side bottlenecks, although it could take a few more months, as the start of the Christmas season will keep demand for goods high for the time being. Returning to the inflation outlook, the covid-related shift in demand should be temporary and so should the price pressures triggered by it. With the normalisation of the demand structure, price pressures for goods are thus expected to decline significantly next year. Together with declining special effects and a higher basis of comparison for some products, this suggests a significant decline in inflation rates next year.

Economic calendar

Ctry	Date	Time	Release	Period	Consens	Prior
Eurozone						
FR	22-Oct	9:15	PMI Index	Oct P		55.0 Index
DE	22-Oct	9:30	PMI Index	Oct P		
EA	22-Oct	10:00	PMI Index	Oct P		
USA						
	15-Oct	14:30	Retail Sales mom	Sep		

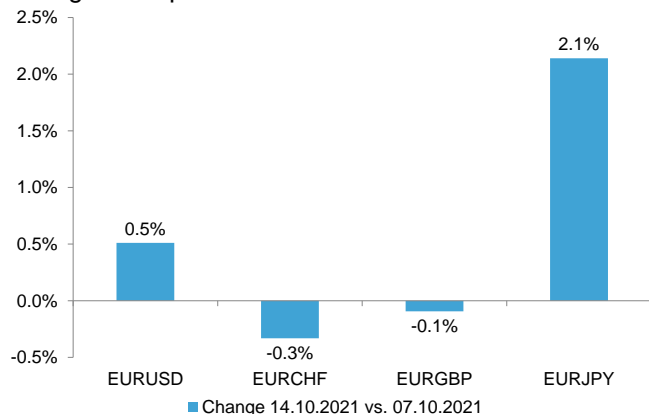
Central bank events

	Date	Time	Event
ECB	11-Oct	14:30	Philip Lane, speech, IIF Annual Membership Meeting
	12-Oct	14:30	Philip Lane, fireside chat: <i>Economic Outlook</i> , SUERF/EIB/Columbia/Société Générale Conference
Fed	13-Oct	18:00	FOMC minutes meeting of September 21-22

Source: Market Data Provider, ECB, Federal Reserve, Erste Group Research

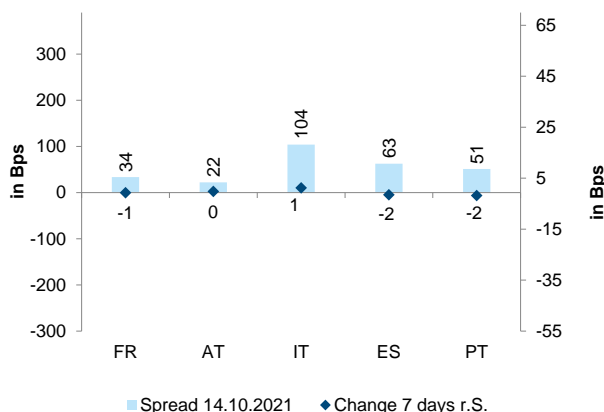
Forex and government bond markets

Exchange rates EUR: USD, CHF, GBP and JPY
 Changes compared to last week



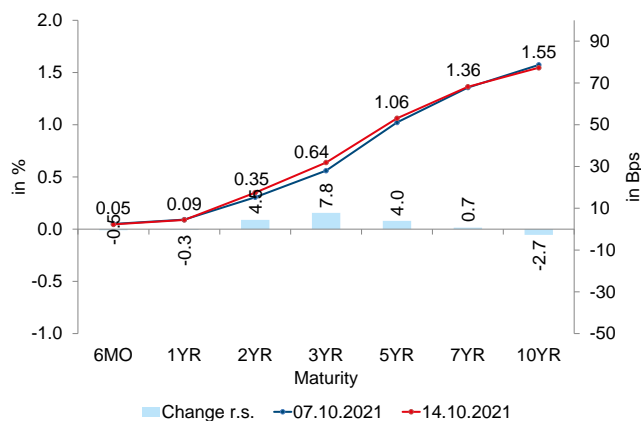
Source: Market Data Provider, Erste Group Research

Eurozone spreads vs. Germany
 10Y government bonds



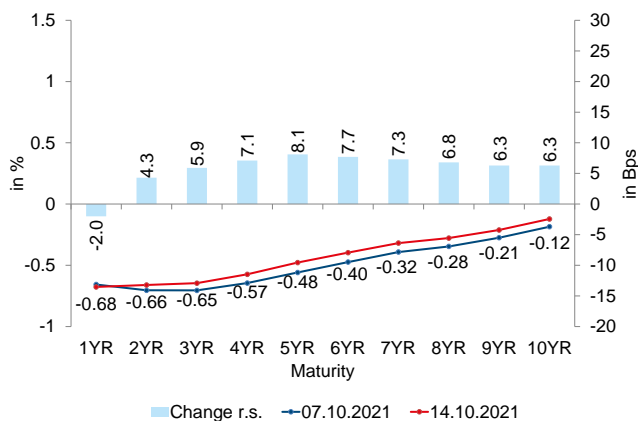
Source: Market Data Provider, Erste Group Research

US Treasuries yield curve
 Changes compared to last week



Source: Market Data Provider, Erste Group Research

DE Bund yield curve
 Changes compared to last week



Source: Market Data Provider, Erste Group Research

Forecasts¹

GDP	2019	2020	2021	2022
Eurozone	1.3	-6.5	5.0	4.2
US	2.3	-3.5	5.9	3.3

Inflation	2019	2020	2021	2022
Eurozone	1.2	0.3	2.2	1.8
US	1.8	1.2	4.2 ↑	2.7 ↑

Interest rates	current	Dec.21	Mar.22	Jun.22	Sep.22
ECB MRR	0.00	0.00	0.00	0.00	0.00
3M Euribor	-0.55	-0.54	-0.54	-0.54	-0.54
Germany Govt. 10Y	-0.12	-0.20	-0.10	0.00	0.10
Swap 10Y	0.26	0.10	0.20	0.30	0.40

Interest rates	current	Dec.21	Mar.22	Jun.22	Sep.22
Fed Funds Target Rate*	0.08	0.13	0.13	0.13	0.13
3M Libor	0.13	0.15	0.15	0.15	0.15
US Govt. 10Y	1.54	1.50	1.60	1.80	1.80
EURUSD	1.16	1.18	1.18	1.18	1.18

*Mid of target range

In case of changes to our forecasts compared to the previous issue, arrows show the direction of the change.

Source: Market Data Provider, Erste Group Research

¹ Note: In accordance with regulations, we are obliged to issue the following statement:
Forecasts are not a reliable indicator of future performance.

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