

Monthly Executive Briefing

Very high inflation in both the US and in the euro area

Very high inflation: Inflation is very high in both the US and in the euro area. In the US, CPI inflation is now 6.2% y/y, the highest level in more than 30 years. In the euro area, inflation rose to 4.9% y/y, which is the highest on record. Rising inflation is not only due to rising food and energy prices and US and the euro area core inflation rates are running at 4.6% y/y and 2.6% y/y, respectively. The concern is that inflation remains high, as wage growth is accelerating and inflation expectations are high, at least in the US.

Central bank divergence High inflation, while employment remains subdued compared to pre-covid levels, puts central banks in a difficult situation. Should they tighten monetary policy to get inflation back to around 2% or should they stay put in order to boost employment? We expect central banks to tighten monetary policy over the coming years but there will be large differences between countries and regions by how soon and how fast. We now expect the Fed to increase the tapering pace at the December meeting and to hike three times in 2022 (see *Fed Research: Say farewell to team transitory – tightening sooner and faster*, 30 November) while we still expect the first ECB rate hike is far away, as the ECB can better afford staying patient after so many years struggling with too low inflation and inflation pressure is less broad-based right now (also with lower wage growth compared to the US).

China: The overall picture in China is still one of weakness, but seemingly ‘peak stress’ in the property sector is now behind us, which, together with improving leading indicators (such as increasing credit growth), points to a bottom in early 2022. That said, we continue to expect more weakness in the short-term, as the headwind from the property sector will continue to linger.

Omicron and new COVID-19 outbreaks: As we warned last month, we are seeing new cases rising in most of the Northern Hemisphere. New cases are very high in Europe but are also rising in the US now. It is likely going to get worse before it gets better, but it also depends on how fast booster shots are rolled-out especially to elderly and people at higher risk. As we argued last month, consumption is likely to remain skewed towards much higher goods demand than normal. As supply may not normalise either (for instance because some people will remain reluctant to return to the labour force), it would prolong the bottlenecks, we are seeing in manufacturing and hence inflation may turn out to be more persistent. This would also put central banks in an even more difficult situation. Besides that the world was caught by surprise of the new omicron variant. At the time of writing, we do not know much about the new variant but fear is that it is better able to evade immunity. We will know more in two weeks’ time when we should get the first lab study results.

New global macro forecasts: This week, we published our new global macro forecasts for the US, the euro area, the UK, Japan and China, see *The Big Picture: Slower growth and rising inflation uncertainties*, 29 November. We expect COVID-19 outbreaks (and possible restrictions) to weigh on economic activity over the winter, especially in Europe. Economic activity should pick up in the spring, as COVID-related fears wane and supply chain problems ease. We expect inflation to moderate over the course of 2022 but to remain above 2% in the US. The biggest risk to our outlook is if inflation remains very elevated forcing an abrupt central bank response.

Key points

- Very high inflation in both the US and the euro area
- Central banks are about to tighten monetary policy but large differences across countries and regions
- Omicron and new COVID-19 outbreaks are creating uncertainties near-term
- We have published new global macro forecasts

Other readings

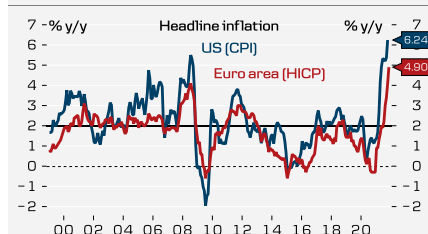
Fed Research: Say farewell to team transitory – tightening sooner and faster

The Big Picture: Slower growth and rising inflation uncertainties

COVID-19 Update: Watch out for the new B.1.1.529 variant

China Macro Monitor: ‘Peak stress’ is behind us

High inflation in both the US and in the euro area

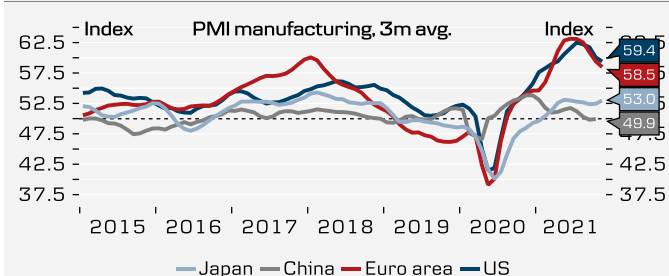


Sources: Eurostat, BLS, Macrobond Financial

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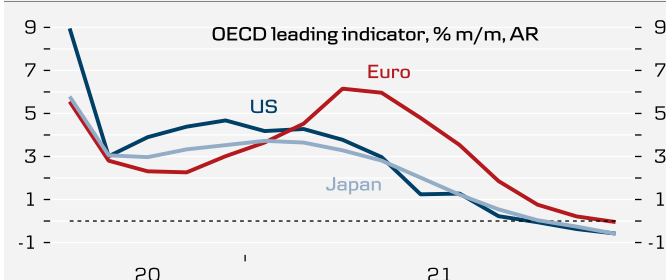
Macro charts overview

Global PMI manufacturing



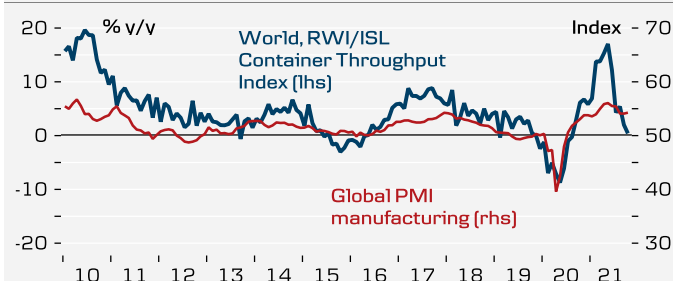
Source: Markit, Macrobond Financial

OECD leading indicator



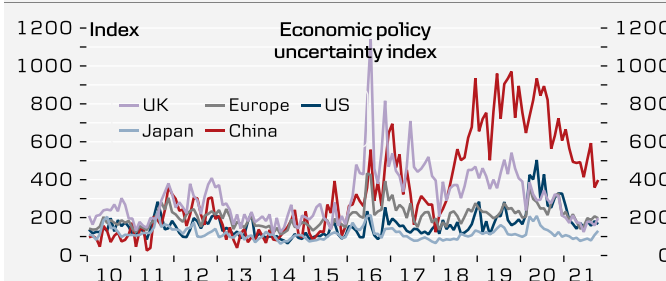
Source: OECD, Macrobond Financial

Global trade growth vs global PMI manufacturing



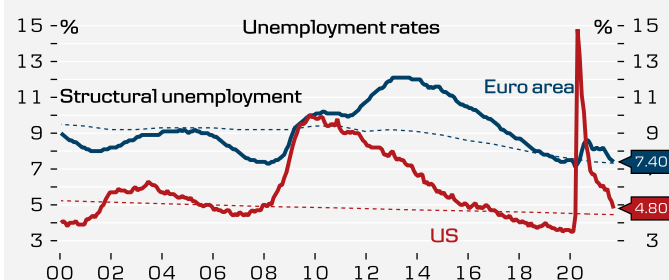
Source: Markit, RWI/ISL, Macrobond Financial

Economic policy uncertainty index



Source: Policy Uncertainty, Macrobond Financial

Unemployment rates



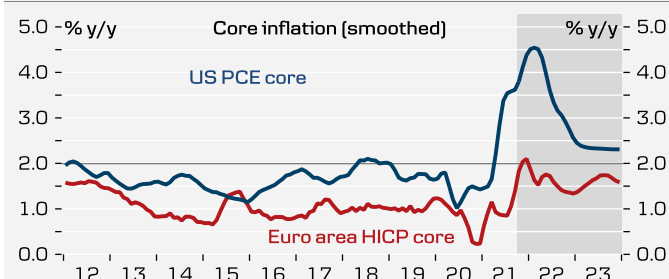
Source: BLS, Eurostat, Macrobond Financial

Wage growth



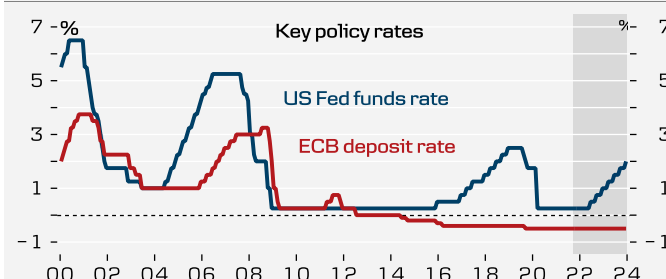
Source: BLS, ECB, Macrobond Financial

Inflation rates



Source: IHS Markit, Macrobond Financial, Danske Bank estimates

Policy rates



Source: ECB, Federal Reserve, Danske Bank estimates

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This research report has been prepared by Danske Bank A/S ('Danske Bank'). The author of this research report is Mikael Olai Milhøj, Chief Analyst.

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Expected updates

Monthly.

Date of first publication

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