1 November 2021

Monthly Executive Briefing

More pressure on central banks

Preliminary Q3 GDP data: We have received preliminary Q3 GDP growth estimates from the US and the euro area since our last update. Q3 GDP growth in the US was 2.0% q/q annualised (0.5% q/q), which was lower than expected and also weak since there was basically zero growth excluding inventories (which, however, pulled down GDP growth significantly in Q1 and Q2). US GDP is now 1.4% higher than in Q4 2019. US goods consumption has peaked but remains extremely high compared to normal, partly explaining why there are so many stories about bottlenecks in manufacturing globally. Growth in the euro area was much stronger (2.2%) but GDP remains 0.5% lower than in Q4 2019. Both US and euro area GDP remain below the pre-COVID trend path. We still believe the easy part of the recovery is now completed and it is not smooth sailing from here. One big question is whether the labour force rebounds back to pre-COVID levels or whether there are permanent damages affecting supply.

Still high inflation: Inflation remains high in the US and in the euro area. US CPI core inflation stayed above 4% in September while euro area HICP core inflation rose to 2.1% y/y in September. It is the first time euro area core inflation is above 2% since December 2002. Inflation in the US is expected to remain high well into 2022.

Central banks: The combination of seemingly slower growth, tight labour markets and high inflation (and higher inflation expectations) puts central banks in a difficult situation. The stagflation theme is definitely still alive. Investors expect central banks to tighten monetary policy earlier and faster than what they themselves are signalling right now. ECB President Lagarde attempted to push by market expectations but failed and investors are now pricing in a 20bp rate hike by October 2022. We, however, believe the ECB will keep rates unchanged for longer. See *ECB Review – Confirmed: Today's meeting was a prelude to December*, 28 October.

Challenging COVID-19 situation: We are approaching winter time in the Northern Hemisphere, which means COVID-19 has better conditions for spreading, as people start spending more time indoors (airborne transmission). We saw new cases skyrocketing both in the US and in Europe around this time last year and especially in Europe new cases have already started to move higher. The winter is probably going to be more challenging than what we thought 3-6 months ago, especially in countries with lower vaccine uptake. This also means the probability of tighter restrictions is rising. From an economic perspective, consumption is likely to remain skewed towards much higher goods demand than normal. As supply may not normalise either, 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. We discussed further in *COVID-19 Update: Brace yourself – winter is coming?*, 28 October.

Energy prices: Energy prices continued to increase in the beginning of October but the situation seems to be stabilising. European natural gas prices have started to decline after Russia's President Putin said Russia will start sending gas to Europe in early November although prices remain high. Electricity prices are also coming down. Oil prices are now USD85 per barrel but have moved sideways recently.

Key points

- Both US and euro area GDP remain below the pre-COVID trend path
- Inflation remains high
- Central banks are under pressure – markets are pricing in earlier and faster rate hikes
- Challenging COVID-19 winter ahead of us
- Energy prices seem to be stabilising

Other readings

ECB Review – Confirmed: Today's meeting was a prelude to December

COVID-19 Update: Brace yourself – winter is coming?

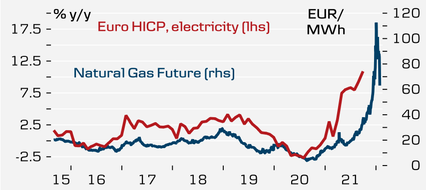
Fed Research – Preview: Tapering, yes, but how fast?

Top 5 charts on China's property crisis

Research Global: Power crunch supports metal prices despite fading demand

Research Global: Five reasons we see rising downside risks to growth

Natural gas prices have started to move lower again in Europe



Source: Eurostat, Bloomberg, Macrobond Financial

Note: Past or current performance is no guarantee of future performance.

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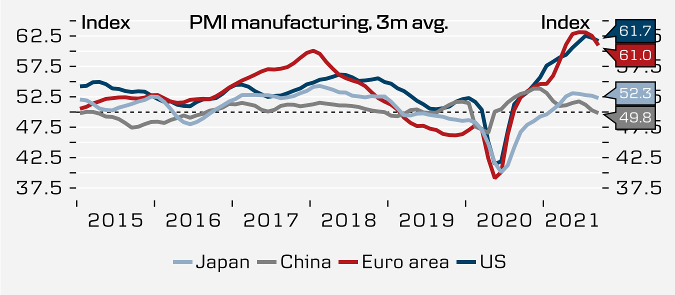
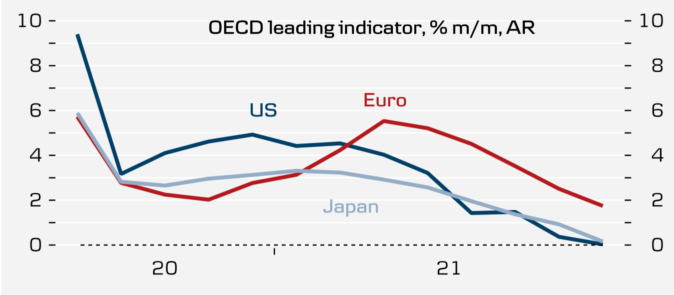
Macro charts overview

Global PMI manufacturing



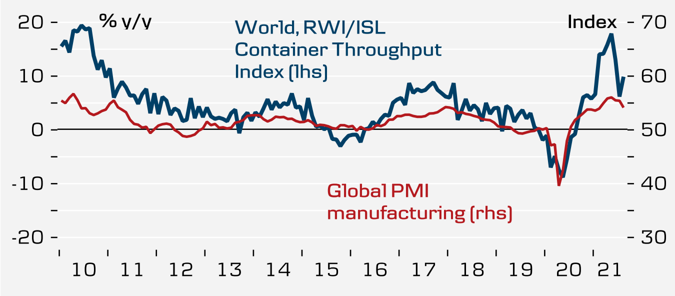
Source: Markit, Macrobond Financial

OECD leading indicator



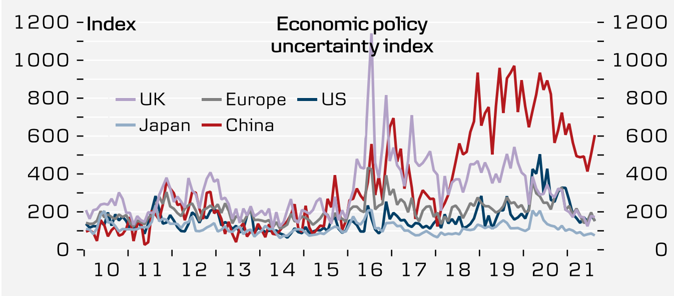
Source: OECD, Macrobond Financial

Global trade growth vs global PMI manufacturing



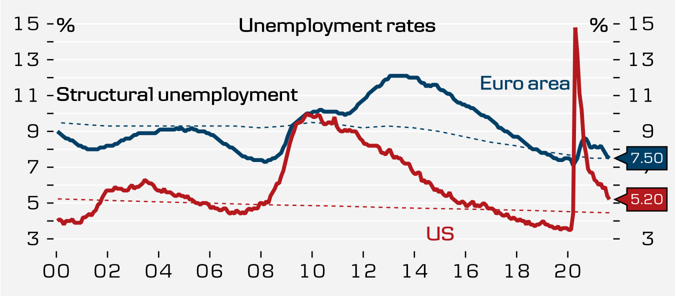
Source: Markit, RWI/ISL, Macrobond Financial

Economic policy uncertainty index



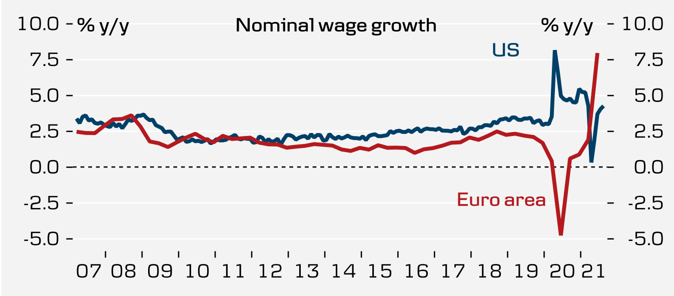
Source: Policy Uncertainty, Macrobond Financial

Unemployment rates



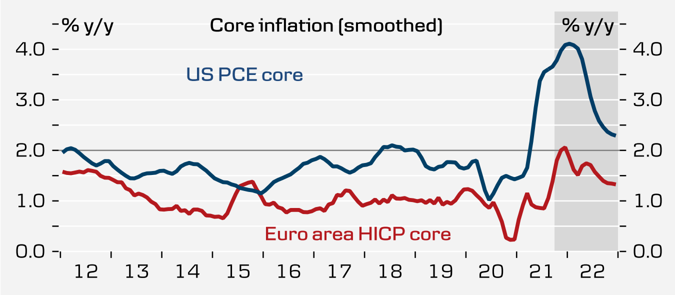
Source: BLS, Eurostat, Macrobond Financial

Wage growth



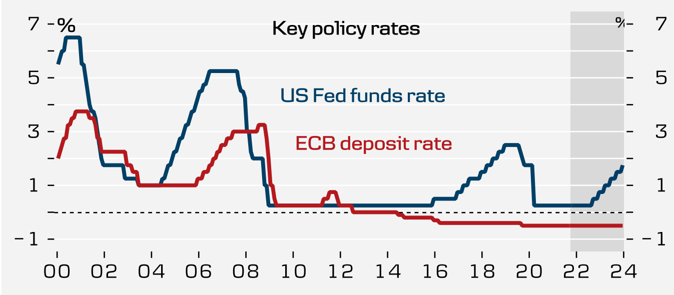
Source: BLS, ECB, Macrobond Financial

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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Monthly.

Date of first publication

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