

Global Monthly

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Will labour shortages prove inflationary?

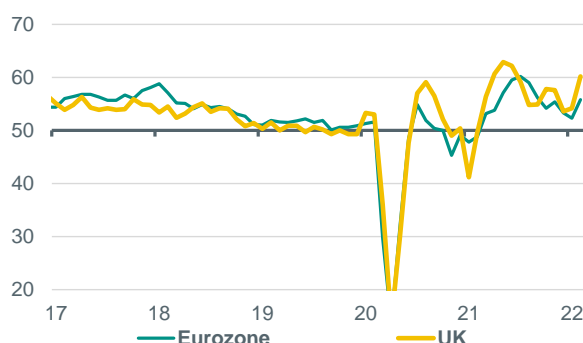
- ▶ Labour markets have tightened across the board, but with large differences in how much
- ▶ We take a deep dive into supply and demand-side developments, and find that the US is experiencing particularly extreme labour market tightness, with the UK and the Netherlands close behind
- ▶ For the eurozone in aggregate, labour market tightness is much less of a concern, keeping the prospects for a surge in wage growth low. However, the aggregate masks big country divergences
- ▶ **Regional updates:** We look at the implications of the ECB pivot for [the eurozone](#), while in [the Netherlands](#), the more shallow Omicron hit led us to make a significant growth forecast upgrade
- ▶ The [US](#) remains in the eye of the inflationary storm, with rebounding goods consumption not helping
- ▶ We expect growth momentum to recover in [China](#), helped by further piecemeal easing
- ▶ Finally, we launch [a new supply bottlenecks indicator](#), which suggests a modest easing recently

Global View: Job vacancy rates are surging – where have the workers gone?

Economies are rapidly rebounding from their Omicron-induced slump, which itself proved more shallow than feared. The eurozone composite flash PMI jumped 3.5 points to a 5 month high of 55.8 in February, while in the US, high frequency indicators from pandemic-sensitive restaurant dining and air travel sectors showed activity has already erased the Omicron losses of December and January. Indeed, the most pressing concern for policymakers continues to be inflation rather than the pace of recovery, and [we made further upgrades to our inflation projections across the regions](#), largely on persistent energy and goods inflation. We also brought forward the timing of ECB rate hikes, given the recent shift in communication from Governing Council members, although unlike in the US, we see a significant risk that growth and inflation undershoots in the eurozone end up derailing ECB rate hikes. Indeed, we have made downgrades to our eurozone growth projections on the back of tighter financial conditions and the hit to real incomes from inflation. Key to the medium term inflation outlook continues to be the labour market. With that in mind, this month's *Global View* tackles the seeming shortage of workers, what this means for wage growth, and whether we should worry about a wage-price spiral taking off.

PMIs suggest activity is rebounding in Europe...

Markit composite PMI (February 2022 = flash estimate)



Source: Refinitiv, ABN AMRO Group Economics

...as are pandemic-sensitive sectors in the US

%



Source: Bloomberg, ABN AMRO Group Economics

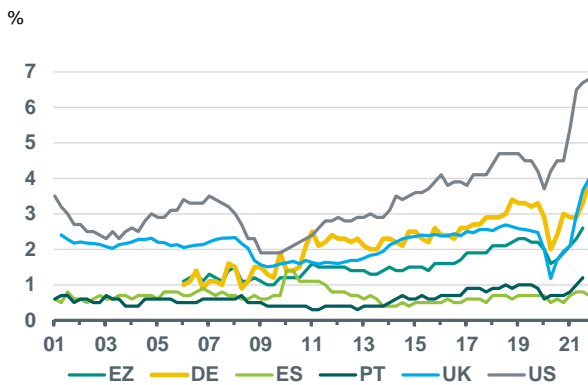
Where have the workers gone?

Will sufficient workers be willing and able to fill current and upcoming demand for labour? This is the key question to understand where inflation dynamics will go in the medium term, and what actions central banks are likely to take. In this monthly we therefore focus on these labour market dynamics, paying special attention to the US, the Eurozone, the UK and the Netherlands.

Tight, tighter, tightest

Labour markets are tight across the board, but there are large differences in just how tight. The eurozone aggregate shows that the vacancy rate has increased much less sharply than we have seen in the UK and the US. Within the eurozone, the variation in labour market tightness by country is large as well. In northern European countries like Germany and the Netherlands, vacancy rates are high and increasing rapidly, while in for example Spain and Portugal vacancy rates are low and increasing only gradually. Although the ECB considers eurozone aggregates for its policy decisions, divergence in macro- economic fundamentals within the eurozone remain a challenge.

Job vacancy rates

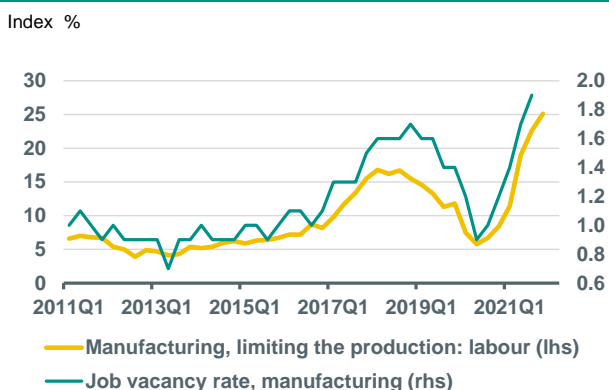


Source: Eurostat, BLS, ABN AMRO Group Economics

Potentially more 'hidden' vacancies in the pipeline

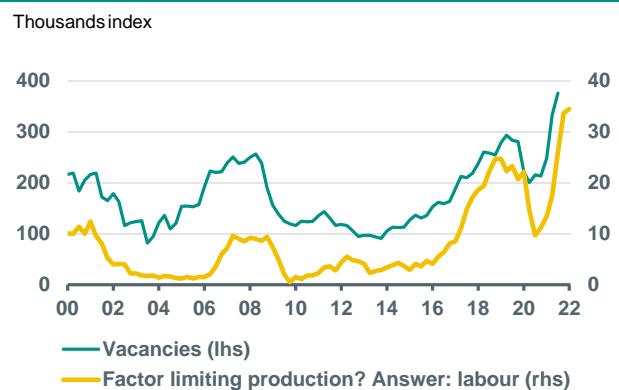
Particularly in extremely tight labour markets, employers may be discouraged to post their vacancies if no candidate is expected to apply. This can be considered hidden demand for labour that may come forward once more workers join the market. To get some sense of whether this is what is going on, we compare the survey results of employers claiming that labour shortage is limiting production to actual vacancies posted. In the Netherlands we see that the increase in the employers mentioning worker shortages is stronger than the increase in actual vacancies posted. This signals indeed that the 'discouraged employer effect' may be at play. While this discouragement creates a barrier to growth in labour demand at present, the 'hidden' vacancies are likely to be posted once employers perceive increased chances of finding candidates. In the eurozone manufacturing industry, we do not see any sign of a discouraged employer effect yet.

EZ Mfg: vacancy rate and labour shortages



Source: Eurostat, European Commission, ABN AMRO Group Economics

NL vacancies versus employers complaints



Source: CBS, ABN AMRO Group Economics

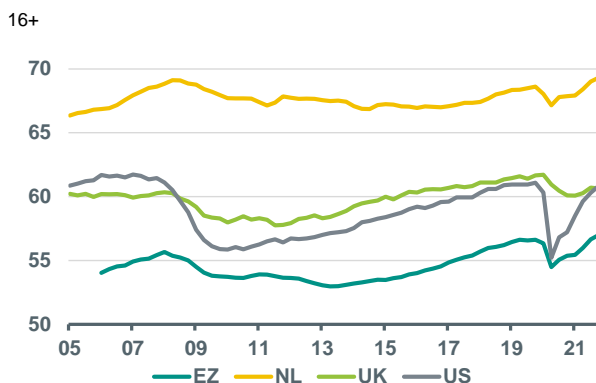
Are we above pre-pandemic demand?

Is labour demand already running above pre-pandemic levels, and if so, could it cause capacity constraints that prove inflationary? We have analysed this question from two angles: the total demand for labour (employment plus vacancies), and from employer surveys in manufacturing and services separately.

Only the Netherlands is above pre-pandemic levels

The pandemic led to a destruction of jobs that was visible in a drop in vacancies and rising unemployment. However, as economies were opening up in between lockdowns, new vacancies were posted and filled. The question is: did the creation of jobs make up for the destruction of jobs since the pandemic? Or, in other words, has the total demand for labour gone back to pre-pandemic levels?

Demand (employment + vacancies)



Source: CBS, ABN AMRO Group Economics

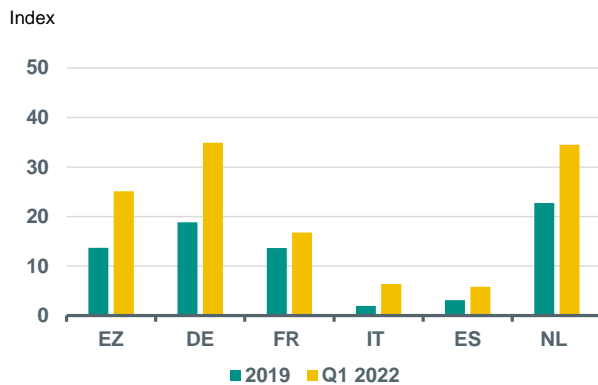
Despite the extremely tight labour market situation in the US – where wages have also risen to around 6% on a 3m/3m annualised basis, total demand for labour has still not gone back to pre-pandemic levels. This is not because vacancies haven't risen, but because more jobs were lost during the pandemic than new ones have been created. We will get back to this when looking at the supply side of the labour market.

In the UK – another extremely tight labour market – total labour demand is even further away from pre-pandemic levels. Here too, it seems that the massive vacancy rates increase has been more about restoring lost jobs from the pandemic than about creating additional labour demand. Still, total demand remains below pre-pandemic levels, indicating that there is still more room for recovery of previously lost jobs.

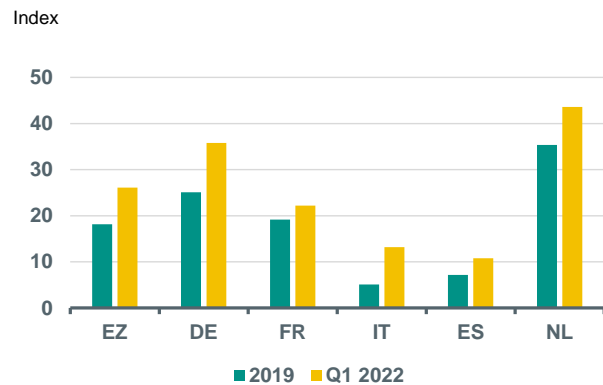
The Netherlands seems to be the exception to the rule: employment and vacancies have grown to above pre-pandemic levels. Total labour demand is now at 0.8 pp above pre-pandemic levels. This is largely due to the fact that fewer jobs disappeared during the pandemic. In the second quarter of 2020, the number of people employed declined only by 166,000 and has since more than recovered. In the meantime, 317,000 additional people have since joined the working population, and despite this, vacancy rates are still increasing.

Eurozone averages hide large differences

Employers' own assessment of whether shortages of staff constrain their productive capacity provides a more nuanced angle within the Eurozone. On aggregate, in both the industry and services sectors around 27 percent of employers consider shortage of staff the main limit to production. Again here, the Netherlands shows the most extreme situation, particularly in services, where 43 percent of employers indicate that labour shortages are their main capacity constraint. German employers also face severe capacity constraints from worker shortages, in both services and manufacturing. In Italy and Spain on the contrary, very few employers signals worker shortages as their main capacity constraint.

Industry - Factors limiting the production: labour

Source: European Commission, ABN AMRO Group Economics

Services - Factors limiting the production: labour

Source: European Commission, ABN AMRO Group Economics

Where are the workers?

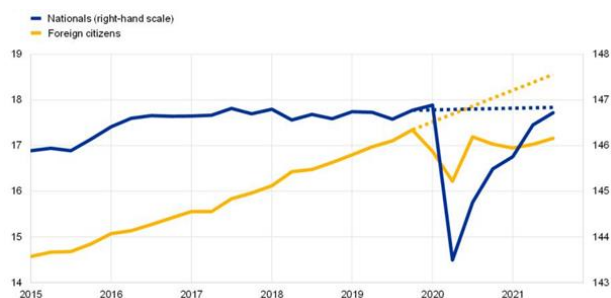
If total demand for work is not yet at the level before the pandemic in most countries, then it must be the supply of workers that creates tightness. Current labour supply data reveals striking differences across regions that help explain differences in wage pressures. The figure below plots the participation rates for different regions amongst people of 16 to 64 years old. On the one extreme, there is the US where millions of workers have voluntarily left the labour market, causing participation to drop in an unprecedented way. About half of the people who dropped out of the labour force went into early retirement, and are thus unlikely to return.

Eurozone participation back to level but below trend

The Eurozone experienced a double dip in participation that followed the two large lockdown periods, but current participation rates are back to pre-pandemic levels. That said, participation is still below the pre-pandemic trend. Another factor, spotted by recent [ECB research](#), that is currently limiting labour supply in the eurozone is migration. Since the pandemic fewer people have migrated to the eurozone, particularly from non-eurozone EU countries, and many European workers from abroad have returned to their home countries. This has had a (likely temporary) downward impact on labour supply of about 1.5 million workers.

EZ: National and immigrant workforce participation

Millions

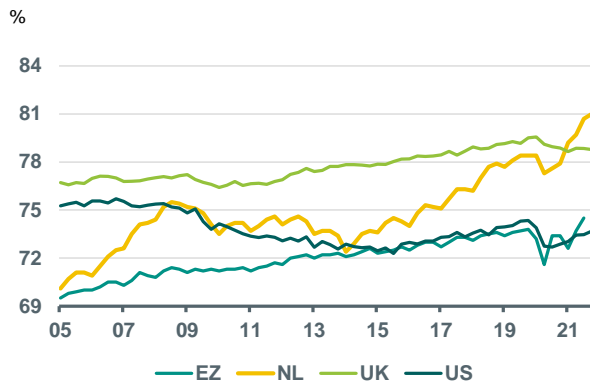


Source: Eurostat EU Labour Force Survey ; ECB Economic Bulletin

However, the labour supply picture in the Eurozone might still be blurred by the fact that wage subsidy schemes are keeping people in (possibly) ungainful employment, i.e. that these workers might be made redundant once subsidies come to an end. At its peak, take-up of wage subsidy schemes in Europe was as high as 16% of the labour force in 2020. With the current low level of unemployment in the euro area (7% in December) and the high percentage of employers seeing labour shortage as their main hampering production factor, the end of wage subsidies should provide some relief to the tight labour market. That said, it is highly uncertain how big the current take up still is. In Germany 2.7% of the workforce is still dependent on

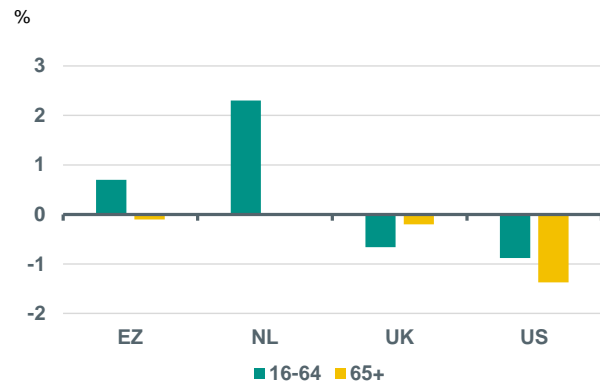
wage subsidies as of January 2022, while in France that figure was 2.2% as of December 2021. How many of these workers will re-enter the labour market and whether these workers match the vacancies posted is unknown. Depending on labour market rigidities per country, this frictional unemployment will eventually resolve as long as the job market remains tight.

Participation rate (16-64 yr)



Source: Labour Force Survey, CBS, BLS, ABN AMRO Group Economics

Net changes in participation since prepandemic



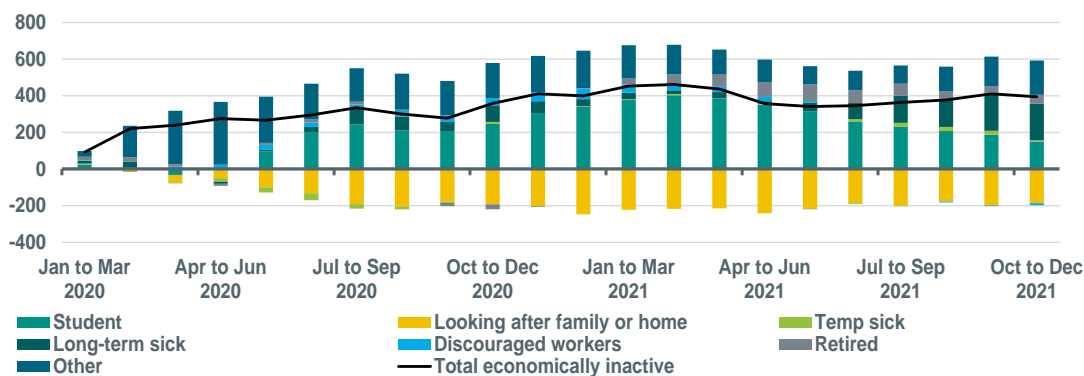
Source: Labour Force Survey, CBS, BLS, ABN AMRO Group Economics

Is long-covid reducing UK labour supply?

The UK shows a striking pattern of its own, where participation seems to be on a slow trend down since the pandemic. While one can explain differences between the eurozone and US patterns of participation from the fact the eurozone fiscal aid was directed at preserving jobs through wage subsidy schemes versus the US, where people were made redundant and then received government support via unemployment benefits, the UK had a similar wage subsidy scheme in place as the eurozone countries. A closer look at the motivation of people leaving the British labour force shows that at first, participation declined mainly due to people leaving the workforce to study. Currently, long lasting illness is has become the main reason for staying out of the labour market.

UK motivations to exit the workforce (aged 16-64 years)

Seasonally adjusted, cumulative change from Dec 19 to Feb 20, for each period up to Oct to Dec 21



Source Labour Force Survey, ABN AMRO Group Economics

The Netherlands: participation instead of wages

While demand for labour has increased massively, wages have hardly moved, with Dutch employers resorting to recruiting workers directly from education, from flexible jobs and from the pool of discouraged workers. Over the past year, the largest increases in worker participation rates are seen amongst the younger workers (15-34 years old) and workers with a non-western migrant background. Participation levels have also increased because a declining number of people have been leaving the workforce since the pandemic. It could be that the ability to work from home has incentivised people to stay on their job a little longer.

Whether there is more potential for increases in participation depends on the ability of about 1 million workers that are marginally attached to the workforce to make the switch to employment. Even in the Netherlands, labour supply still has some hidden reserves from the wage subsidy schemes that keep people on the payroll but out of work. In November and December 2022, about 4 percent of the workforce was receiving wage subsidies via their employer. These schemes are expected to end soon. Restaurants and bars have been the main receivers of support during the 5th and hopefully last wave of infections, and with the economy reopening, the worker shortage is also largest in this sector. This is a problem that may thus solve itself as subsidy schemes end.

Conclusion: Eurozone unlikely to see wage increases that prove inflationary

There is no doubt that labour markets are tight everywhere. In the US it is the most extreme, but the UK and the Netherlands are close followers. In the Eurozone in aggregate, it is a much less pressing issue at the moment.

As such, prospects for wage growth are the highest in US, but are also high in the UK. For the Netherlands, despite the labour market being as tight as the UK's, wage growth is less likely given that participation increases have helped to rapidly fill vacancies. Despite this additional participation, worker shortages are still a problem, and it remains to be seen how much further participation can increase before wages need to rise. We currently expect a modest 2.2% wage growth for 2022.

The US wage pressure stems from a negative supply shock that may not resolve soon, and this is creating sustained wage pressure even though labour demand has yet to return to pre-pandemic levels. If the January surge in retail sales (+3.8% m/m) does not correct in the coming months, this could generate additional wage pressures, with a serious risk of a wage-price spiral.

Only in the Netherlands has total demand for labour seemingly surpassed pre-pandemic levels. In fact, despite a jump in participation, there is still growing demand for labour, with vacancy rates continuing to rise. Looking ahead, given the expected increase in workers searching for jobs as wage subsidy schemes end, we expect wage pressures to remain modest in the coming year.

In the eurozone as a whole, vacancy rates have increased at a much more modest pace, showing that tightness is less of a problem at the aggregate level. On the supply side, the end of wage subsidy schemes will release new labour supply on to the job market just as in the Netherlands. The risk of mismatches is however hard to assess. The eurozone's labour market rigidities, both in geography and across sectors, may prove more inflationary than aggregate numbers suggest. But even if it does, we do not see a wage pressure in the eurozone aggregate that is anything like what we are seeing in the US. If wage growth accelerates significantly in say, NL and Germany but not elsewhere, this could create a dilemma for the ECB – but we are not there yet.

Eurozone: The consequences of the ECB's pivot

Aline Schuiling, Jolien van den Ende, Nick Kounis, Georgette Boele (aline.schuiling@nl.abnamro.com)

- ▶ **The ECB has made a hawkish pivot, signalling that it is gearing up to unwind net asset purchases and will start raising its policy rate before the end of this year**
- ▶ **Consequently, we have revised our forecasts for short term interest rates, government bond yields and the euro/dollar exchange rate upward, while lowering our growth forecasts somewhat**

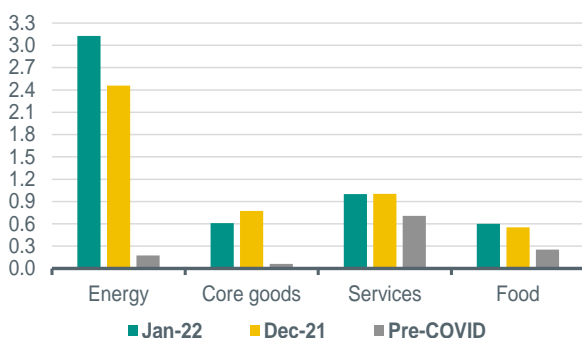
After the February Governing Council meeting, ECB President Lagarde sounded surprisingly hawkish. She signalled that the central bank will reduce policy accommodation this year. The central bank probably was spooked by the upward surprise in the inflation data for January (5.1%). Indeed, the core inflation rate did not decline as much as expected, which may have supported the view that underlying inflation was starting to firm. Moreover, the ECB seems to be becoming more confident that wage growth will rise this year. As a result of the ECB's pivot, we have changed our forecasts. We think that a tapering of the APP will be announced in March, with net purchases ending altogether in September. We have also pencilled in a 10bp deposit rate hike in December of this year and an additional one in March of next year. After that, we expect rate hikes to be aborted, or at least put on ice, with the deposit rate at -0.3% by the end of 2023. Having said that, there is a non-negligible probability that the window of opportunity for a rate hike might close before the end of the year, mainly because the inflation rate is expected to drop lower in the final months of the year, financial conditions will be tightening on the back of aggressive Fed rate hikes, and economic growth is expected to come in below current ECB expectations.

The changes in our ECB policy forecasts have led us to revise our estimates for short term interest rates, government bond yields and the euro/dollar exchange rate upward. The resulting tightening of financial conditions probably will not be strong enough to choke off the economic recovery, but it should reduce the pace of growth somewhat. Therefore, we expect GDP growth to slow down to the trend rate in the course of 2023, whereas we previously expected it to remain above the trend rate. Initially, we expect modest growth in 2022Q1 and a sharp rebound in 2022Q2-Q3 as Omicron related disturbances to services sector activity and global supply chain problems will hurt in the first months of this year, but will subsequently ease. A more normal cyclical growth pattern should take shape from the final quarter of this year onward.

With regard to inflation, we have sharply raised our forecasts for the first half of this year, mainly due to higher food and energy price inflation. Indeed, rises in energy commodity prices filter through into household energy prices with a significant delay, keeping energy price inflation elevated for a while. We expect some of the higher energy price inflation to filter through into some parts of core inflation, but this should be more than compensated by the downward impact of further normalisation of the inflation rate of holiday and entertainment related services. Sharp downward base effects in energy price inflation should push headline inflation well below the ECB's 2%-target in the final months of this year. Meanwhile, wage growth at the eurozone level is still subdued. It is expected to strengthen during this year and next, but the impact on underlying inflation should be buffered by rises in labour productivity.

Inflation still largely driven by energy

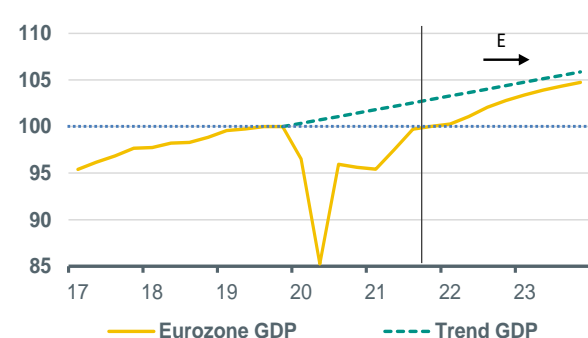
Contributions to HICP inflation, pps yoy



Source: Refinitiv, ABN AMRO Group Economics

An output gap remains

GDP, index 2019Q4 = 100



Source: Refinitiv, ABN AMRO Group Economics

The Netherlands: Limited lockdown impact lifts growth in 2022

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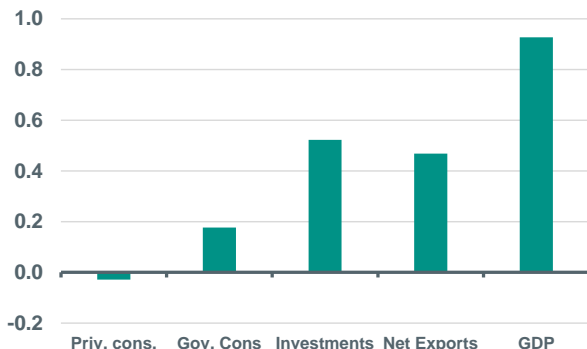
- ▶ **GDP growth in the fourth quarter surprised to the upside, with domestic demand driving growth**
- ▶ **We raised our 2022 growth forecast to 3.1% from 2.6%, due to carry over effects and limited lockdown impact**

Q4 GDP figures, released on 15 February, showed stronger growth than anticipated. We expected a modest contraction in GDP due to new Covid restrictions at the end of 2021, while the data showed that GDP expanded by 0.9% qoq (Eurozone: 0.3%). The main surprise was the relatively mild drop in private consumption (-0.1% qoq). Worries over the spread of the Omicron variant led the Dutch government to impose new restrictions in November and a lockdown in December. The Netherlands had, relative to European countries, among the strictest measures in place. Despite this, consumption was curbed to a lesser extent compared to previous lockdowns. Consumers showed flexibility by continuing to spend in sectors that faced restrictions (by going online) and, given the high vaccination rate, consumers continued buying goods and services in sectors that remained open. In contrast, in previous lockdowns consumers stayed at home much more.

Q4 growth was further driven by investment. Investment data has been less straightforward to interpret. Q4 investment (+2.6% qoq) increased significantly. This was long anticipated, as despite the rebound in sentiment, investment had been hampered throughout 2021 by the tight labour market and global supply bottlenecks. Government consumption also expanded in Q4, despite the fact that normally during lockdown periods regular healthcare is scaled down which suppresses government consumption. With the fourth quarter now published, 2021 growth came in at 4.8%, following the drop of 3.8% in 2020. Compared to the pre-pandemic level (measured by the fourth quarter of 2019) the level of GDP is now 2.7% higher.

Q4 domestic demand surprised to the upside

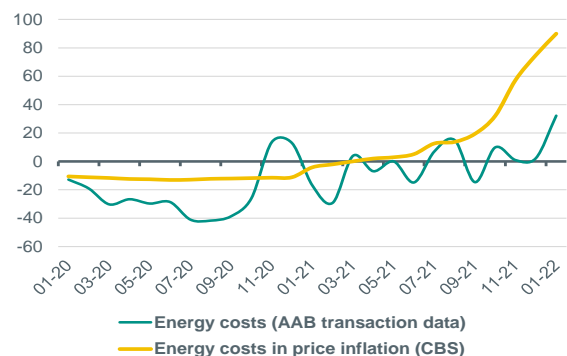
% contributions to fourth quarter GDP



Source: ABN AMRO, CBS

Exposure to energy lower than inflation suggests

Yoy, percentage change



Source: ABN AMRO, CBS

Looking ahead, the strong fourth quarter also carries over to growth in 2022. Given the recent announcement that the Dutch government will lift all restrictions on 25 February, we have revised our growth forecasts upwards, from 2.6% to 3.1%. Downside risks to growth stem mainly from abroad. Higher energy prices fed into inflation which spiked to 7.6% (HICP) in January. This could erode the purchasing power of consumers going forward. That said, the inflation figure assumes that every single month every household starts a new energy contract, whereas about half of the Dutch households have fixed term contracts. While energy prices surged 90% according to the inflation figure, AAB transaction data shows that household expenditure on utilities 'only' increased by 30% (see graph above). Therefore, the near-term effects on purchasing power will be less than can be inferred from the headline inflation figures. Other headwinds persist from both supply chain bottlenecks and the tight labour market. We expect investment growth to be backloaded in 2022 as supply chain bottlenecks ease of the course of 2022, which should be a tailwind for investment. Finally, as discussed in this month's *Global View*, no significant easing is expected on the labour supply front. Some relief is expected when the COVID-19 government support packages are phased out, but tightness is here to stay and will constrain growth for the foreseeable future.

US: In the eye of the inflationary storm

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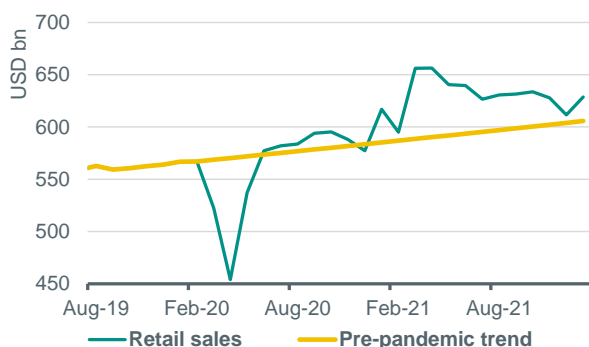
- ▶ **The supply side staged a strong recovery in January, but demand recovered even more**
- ▶ **Goods consumption is well above trend once again, defying the plunge in consumer sentiment**
- ▶ **The risk is that an inflationary mindset is now taking hold, requiring much steeper interest rate rises**

January activity data in the US was a mixed bag. On the positive side, supply is recovering strongly, with labour force participation and manufacturing registering very strong growth, suggesting that the price signal from higher (wage and goods) inflation is starting to have some easing effect on bottlenecks. On the other hand, the rebound in demand was even greater, with retail sales jumping sharply following their brief flirt with more normal levels of demand in December. Indeed, inflation remained stubbornly high in January, leading us to once again upgrade our forecasts, with 2022 inflation now expected to average 5%, up from 4.6% previously. We were somewhat less alarmed by the January print than market participants appeared to be, given that the bulk of the upside surprise was driven by goods and energy rather than services inflation. Still, the US economy remains in the eye of the inflationary storm, and given the continued acceleration in wage growth – and the possibility of a wage-price spiral taking off – the risk is still that things could get even worse before they get better.

The rebound in retail sales – which rose 3.8% m/m in January, following a downwardly revised -2.5% in December – was broad-based, and stood in stark contrast to the dramatic fall in Michigan consumer sentiment, to a new post-pandemic low of 61.7. With retail sales reported on a nominal basis (volume data comes with a lag), elevated inflation is flattering the figures somewhat. Even factoring this in, we estimate real sales are now around 3.8pp above the pre-pandemic trend, having been just 1pp above trend in December – dashing hopes that demand might just cool by itself. But if we really are back to square one, with goods consumption well above trend again, how do we square this with plunging consumer sentiment?

Retail sales back to well above trend

Real retail sales (January figure is our estimate)

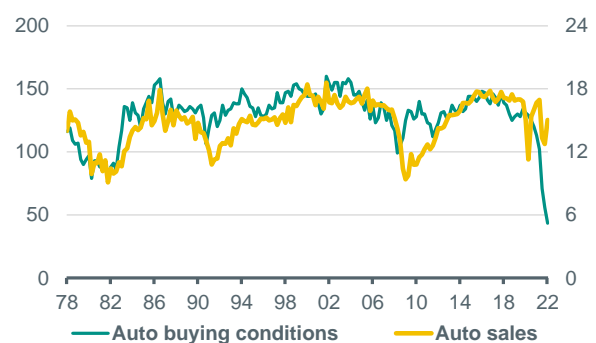


Source: Refinitiv, ABN AMRO Group Economics

Sentiment plunging to historic lows, but sales still high

Michigan consumer sentiment index

Auto sales, millions (annualised)



Source: Bloomberg, ABN AMRO Group Economics

Could an inflationary mindset be taking hold?

One explanation could be that the January rebound is temporary, driven by the Omicron-induced weakness in services, i.e. that there is a substitution element at play. If this is the case, sales are likely to quickly normalise now that the services recovery is back on track. Another – more worrying – explanation is that although consumers believe current buying conditions are bad, they may anticipate conditions getting even worse in future (perhaps on the expectation of higher prices), and so are front-loading their consumption. The latter would be an ominous sign for inflation coming back down of its own accord, as producers could feel emboldened to pass on higher pipeline costs, given continued strong demand even in the face of high inflation. Such a self-fulfilling inflationary dynamic would require a much more forceful policy response from the Fed to contain, implying a much steeper rise in interest rates than we currently have in our base case. While it remains to be seen which of these two scenarios will play out, given the upside risks to inflation also from the labour market, the risk continues to be that the Fed has to raise rates by more than our expectation of four rate hikes in 2022.

China: Dealing with Omicron and 'dynamic clearing'

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- ▶ Quarterly growth will drop in Q1 compared to Q4, but improving growth momentum is on the cards
- ▶ Omicron reduces gains from the shift in covid-19 policy from 'zero cases' to 'dynamic clearing'
- ▶ Falling inflationary pressures leaves room for further targeted easing including for real estate

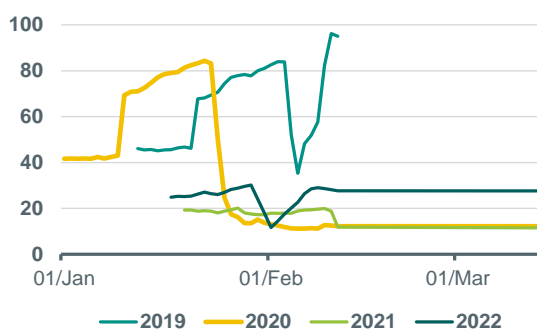
After a pick-up in Q4-2021, we expect quarterly growth to fall back in Q1, with drags from real estate and strict covid-19 policies remaining. That said, we expect qoq growth to pick-up in the course of this year and to be on average higher than last year. We think annual growth bottomed at 4.0% yoy in Q4-2021 and will accelerate towards around 5.5% yoy in the second half of this year. That would leave full-year growth for 2022 at 5.1%. China's official growth target for this year will be announced at the National People's Congress in early March. Our expectation of improving growth momentum in the course of this year is partly based on the assumption that the authorities will continue with targeted, piecemeal monetary and fiscal easing and a relaxation of macroprudential regulations, including for real estate.

Omicron reduces gains from the shift in covid-19 policy from 'zero cases' to 'dynamic clearing'

Due to the Chinese New Year (this year scheduled in early February) economic data from China are relatively scarce this month, with the monthly activity and foreign trade data for January/February combined being published in March. Still, from the data that are available we can conclude that the move in covid-19 policy from a centralised 'aim for zero cases' approach to decentralised 'dynamic clearing' (quickly contain local outbreaks) has been less supportive for consumer services than the authorities had hoped for. In 2021, the central government told people not to travel during the holiday break. This year, such decisions were delegated to local governments. However, due to the spread of Omicron – and the example of Xi'an – local governments became cautious. The result is that travel volume during the LNY break rose by over 30% compared to last year, but remained far below pre-pandemic levels. Tourism spending was actually lower compared to a year ago. All in all, we think that quarterly growth will fall back in Q1-22, after a pick-up in Q4-21, but will be higher than in Q1-21. The January PMIs also pointed in that direction, with the composite indices from both NBS and Caixin dropping significantly (see [here](#)).

Lunar New Year travel still far below pre-pandemic trend

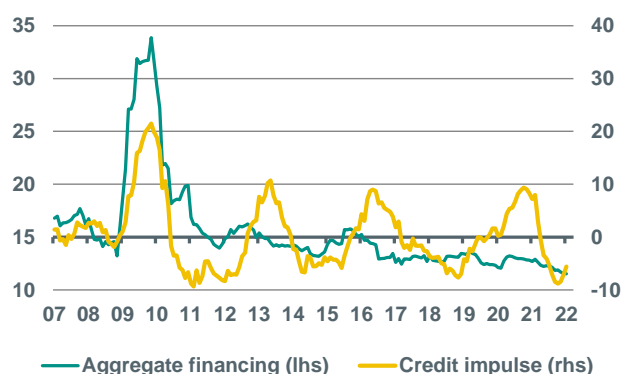
Daily number of travellers, millions



Source: CEIC (2022: forecasts from Chinese Ministry of Transport)

The turn in the credit cycle has further to run

% yoy



Source: Refinitiv, Bloomberg

Falling inflationary pressures leaves room for further targeted, piecemeal policy easing including for real estate

Our expectation that, going forward, growth momentum will improve compared to Q1 partly rests on the assumption of further targeted policy support. Pipeline inflation pressures are easing, although renewed commodity price rises could lead to hiccups (see for more background [here](#)). Consumer price inflation fell to below 1% yoy in January. We expect CPI inflation to bounce back in the course of this year, but to remain below the PBoC's 3% target. All of this leaves the authorities room to add some more piecemeal, targeted monetary and fiscal stimulus and a cautious relaxation of macroprudential regulation (including for real estate), to stabilize growth in a politically important year for the leadership. Moreover, while the credit cycle has already bottomed out and lending growth has begun to stabilize, some more easing seems warranted to realise a modest acceleration in lending growth and to contain the prevailing drags from real estate.

Spotlight: A global supply bottlenecks indicator

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- ▶ **Global supply bottlenecks in manufacturing and trade have been a key headwind in the recovery**
- ▶ **We created a comprehensive indicator measuring the severity and direction of these bottlenecks**
- ▶ **Some easing seen in late 2021, but Omicron could delay normalisation in supply-demand imbalances**

Widespread pandemic-related disturbances in global production and trade networks have proven an important headwind to the global 'post-pandemic' recovery. They also have added to inflationary pressures, although aside from in the US, the spike in energy prices has been the dominant driver of inflation. These bottlenecks stem from pandemic-related temporary closures of production and handling facilities, and from disturbances in global transport (eg closure of port terminals, port congestion, spike in freight tariffs). The supply issues are only in part a global phenomenon: the interconnectedness in global supply chains has created vulnerabilities for disruptions in the cross-border logistics of industrial supplies. They partly also reflect domestic developments (eg. country-specific covid-19 policies or supply shortages in labour markets).

Launching an indicator to measure global supply bottlenecks

To get a sense of the combined impact of these bottlenecks, we developed a comprehensive indicator measuring the severity and the direction thereof. Our indicator captures shortages in semiconductors (lead times), disturbances in global trade (container freight tariffs, Baltic Dry Index) and bottlenecks in manufacturing and electronics (global PMI manufacturing subindices for delivery times and backlogs). As supply bottlenecks have gone hand in hand with demand pressures (reflecting a pandemic-related shift in global demand from services to goods), we use the ratio between the global manufacturing PMI output sub-index versus orders (domestic and exports) as well – also see [here](#). Most variables used in the indicator have a global coverage; the only two exceptions being the PMI sub-index for delivery times and the output versus order ratio, for which we use the aggregates for developed economies (end-users in global supply chains). We think that this indicator helps provide a big picture overview of supply bottlenecks that are currently at play at the global level. The index does not include variables related to domestic issues such as congestion in specific ports, or labour supply. Nor does it capture variables related to the scarcity in commodity markets, which can be volatile and idiosyncratic in their drivers.

ABN AMRO – Global supply bottlenecks index

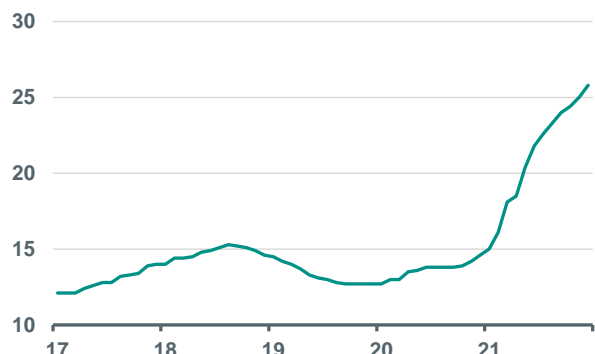
Weighted index, +6 = maximum bottlenecks



Source: ABN AMRO Group Economics, Bloomberg, Refinitiv

No signs of relief yet for semiconductors

Number of weeks



Source: Susquehanna Financial Group, Bloomberg

Some signs of easing seen in late 2021, but Omicron will likely delay a further easing of supply bottlenecks

Our indicator suggests that global supply bottlenecks started easing a little in late 2021, driven by output versus orders ratio (also see our analysis [here](#)) and the volatile Baltic Dry index. However, some variables such as the lead times for chips (determined by more factors than pandemic disturbances) are still at historic highs. We expect a further easing of supply-demand imbalances in the course of this year as we reach the end phase of the pandemic, with global demand for goods hit by inflation and rotating back to services. However, the spread of Omicron will likely delay this normalisation process. The gradual shift amongst globally operating firms from 'just in time' to 'just in case' will also have an impact over time, as firms diversify supply chains to ensure security of supply. This will likely lead to higher inventory levels in the longer run.

Key views on a page

The post-pandemic recovery is regaining momentum, with above trend growth to resume in the eurozone and the US following the Omicron-induced soft patch. However, uncertainty over the economic outlook remains the highest it has been since the start of the pandemic in early 2020. While economic growth has been strong, as economies have largely opened up, the supply-side has struggled to keep up with resurgent demand, with the consequence being inflation. This has brought forward the timing of interest rate rises in the US, with the Fed expected to begin raising rates in March. The ECB has meanwhile signalled a pivot to policy normalisation, and we now expect rates to start rising in December. Europe will also continue to feel the global spill-over effects of tighter US monetary policy over the coming year, pushing bond yields higher and ultimately dampening growth.

Macro	Central Banks & Markets
<p>Eurozone – The economy is going through a soft patch, with modest growth in 2021Q4-2022Q1. Supply side bottlenecks and record-high (energy price) inflation are restraining growth, even after the lifting of Omicron-related restrictions. Growth is expected to rebound sharply in 2022Q2-Q3, but should return to a more normal cyclical path thereafter. It should slow down toward the trend rate in the course of 2023. Inflation is likely to stay elevated in the first half of 2022 but should drop below the ECB target in the final months of the year. Wage growth at the eurozone level is still subdued. It is expected to strengthen during this year and the next, but the impact on underlying inflation should be buffered by rises in labour productivity.</p>	<p>ECB – After the February Governing Council meeting, ECB President Lagarde sounded surprisingly hawkish, signalling that the central bank will reduce policy accommodation this year. As a result of the ECB's pivot we now think that a tapering of the APP will be announced in March, with net purchases ending altogether in September. We expect APP to average EUR 30bn in Q2 and EUR 15bn in Q3. We have also pencilled in a 10bp deposit rate hike in December of this year and an additional one in March 2023. After that, we expect rate hikes to be aborted, or at least put on ice, with the deposit rate at -0.3% by the end of 2023. We think there is a non-negligible probability that the window of opportunity for a rate hike might close before the end of the year.</p>
<p>Netherlands – Q4 growth surprised to the upside. Instead of our expectation for a mild contraction, GDP expanded in Q4 by 0.9% qoq. Annual growth therefore came in at 4.8%. The strong Q4 reading carries over to 2022 growth. Together with the government's announcement to lift all restrictions, we have upgraded our growth forecasts for 2022 from 2.6% to 3.1%. This above trend growth however faces several constraints. Most notable are the notoriously tight labour market and supply bottlenecks. Inflation is expected to average at 3.7% in 2022, with upward price pressures from energy and supply bottlenecks gradually fading over the coming year.</p>	<p>Fed – Given persistently elevated inflation in the US, and upside risks to the outlook, we expect the Fed to begin hiking rates by 25bp in March. Thereafter, we expect three additional hikes this year and in 2023. This would take the target range of the fed funds rate back to the pre-pandemic level of 1.5-1.75% by mid-2023. The risk continues to be for an even steeper path of rate hikes. Shortly after lift-off, we expect the Fed to begin unwinding its balance sheet in late Q2, initially at a gradual pace, but eventually for this to run at \$60bn per month. There is a significant risk that the Fed reduces the balance sheet at a much faster pace, potentially using it as a tool in its fight against inflation.</p>
<p>US – Above trend growth is resuming after the Omicron soft patch of late 2021. However, elevated goods consumption and tightness in the labour market is continuing to put upward pressure on inflation. Wage growth has surged in recent months, raising the risk of a wage-price spiral taking off. While we expect above-trend growth to continue throughout 2022, growth is likely to slow to below-trend rates in 2023, on a combination of fading post-pandemic catch-up effects, weaker government spending following the failure of Biden's Build Back Better plan, and tighter monetary policy.</p>	<p>Bond yields – Given that we forecast the Fed funds rate to be at its eventual peak of around 2.50-2.75% by end 2025, we expect longer term yields will move higher in 2022, with the 10y US Treasury yield settling at around 2.6% at year-end. Once we move closer to the first rate hike, which we have pencilled in for March, we expect the US Treasury curve to bear flatten. Our new ECB forecasts have made us revise our forecasts for 10y Bund yields higher (to 0.5% at end-2022), although we do think that the market is already quite advanced in pricing in two 10bp rate hikes and the ending of APP. The rise in US yields will also put further upward pressure on their European counterparts.</p>
<p>China – We expect qoq growth to fall back in Q1, with drags from real estate and strict covid-19 policy remaining. Due to Omicron, the shift from 'zero cases' to 'dynamic clearing' has been less supportive for consumer services than was hoped for. We expect qoq growth to pick-up in the course of 2022. We think yoy growth bottomed at 4.0% yoy in Q4-21 and will accelerate to around 5.5% yoy in 2H-22. That would leave full-year growth for 2022 at 5.1%. Our expectation of improving momentum is partly based on the assumption that Beijing will continue with targeted, piecemeal monetary and fiscal easing and a relaxation of macroprudential regulations, including for real estate.</p>	<p>FX/EURUSD – Following the ECB meeting, we changed our ECB view. We now expect a modest rise in the deposit rate from the end of this year. We originally didn't have any hike in the deposit rate in our forecast horizon. Financial markets are pricing in more aggressive rate hikes for both the ECB and the Fed than we have. We think that if our view proves to be correct then that the euro still weakens versus the US dollar this year and next year. But it is likely that the overall size of the move is smaller than we originally had. Therefore, we have changed our forecasts in EUR/USD. Our new forecast for end 2022 is 1.07 (was 1.05) and for end 2023 1.05 (was 1.0).</p>

Main economic/financial forecasts									
GDP growth (% yoy)	2020	2021	2022e	2023e	Inflation (%)	2020	2021	2022e	2023e
United States	-3.4	5.7	3.8	2.3	United States	1.2	4.7	5.0	2.1
Eurozone	-6.5	5.2	3.4	2.5	Eurozone	0.2	2.6	3.6	1.4
Japan	-4.5	1.7	3.1	1.6	Japan	0.0	-0.2	1.0	0.7
United Kingdom	-9.4	7.5	5.2	2.1	United Kingdom	0.9	2.6	4.8	1.9
China	2.2	8.1	5.1	5.3	China	2.5	0.9	2.5	2.0
Netherlands	-3.8	4.8	3.1	1.9	Netherlands	1.1	2.8	3.6	2.2
Policy rate	18/02/2022	+3M	2022e	2023e	10Y interest rate	18/02/2022	+3M	2022e	2023e
Federal Reserve	0.25	0.75	1.25	2.00	US Treasury	1.93	2.00	2.60	2.60
European Central Bank	-0.50	-0.50	-0.40	-0.30	German Bund	0.21	0.30	0.50	0.50
Bank of Japan	-0.10	-0.10	-0.10	-0.10	Japanese gov. bonds	0.21	0.20	0.20	0.20
Bank of England	0.50	0.50	0.75	1.25	UK gilts	1.38	1.70	1.90	2.00
People's Bank of China	3.70	3.60	3.60	3.60					
Natural resources	18/02/2022	+3M	2022e	2023e	Currencies	18/02/2022	+3M	2022e	2023e
Brent - Oil USD/barrel	93.5	80	80	75	EUR/USD	1.13	1.10	1.07	1.05
WTI - Oil USD/barrel	91.1	77	77	72	USD/JPY	115.0	118	120	124
Henry Hub - Gas USD/mm	4.43	4.0	3.5	3.5	GBP/USD	1.36	1.31	1.26	1.25
TTF - Gas EUR/MWh*	51.6	40	35	25	EUR/GBP	0.83	0.84	0.85	0.84
Gold - USD/oz	1,898	1,700	1,500	1,300	USD/CNY	6.33	6.30	6.20	6.15

Source: Refinitiv, Bloomberg, ABN AMRO Group Economics

* Brent, WTI, Henry Hub: active month contract; TTF: next calendar year

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