

Global economic outlook amid rising risk of stagflation



Economic Research Department
August 2022

What's stagflation and what causes it

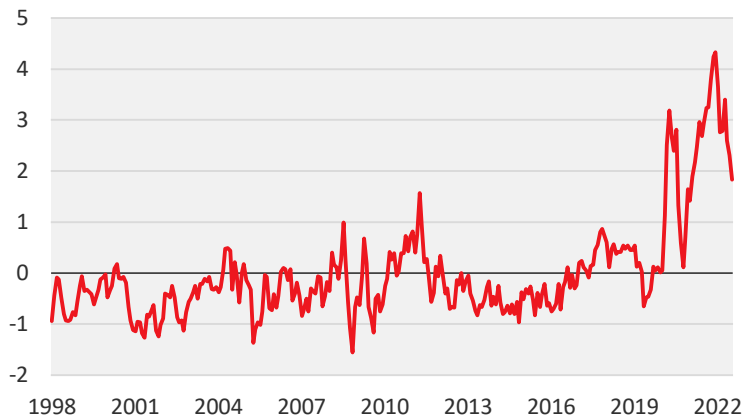
Stagflation is the simultaneous appearance in an economy of slow growth, high unemployment, and rising prices

- The 1970s experience of slow growth, high unemployment, and rising prices was the real example of stagflation
- Poor fiscal and monetary policy decisions, together with oil embargo were the main causes of stagflation in 1970s
- Current economic condition has many similarities (elevated inflation, slowing growth momentum and tightening monetary policy) to stagflation

Similar to the 1970s, supply shocks have driven prices higher

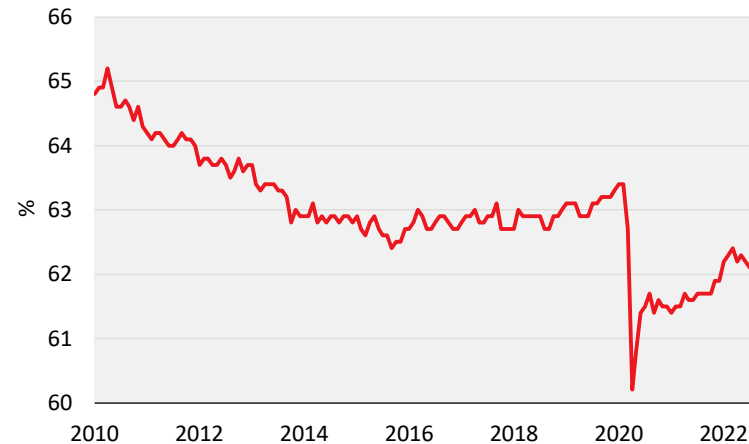
- Pandemic lockdown led to production shutdown and port congestion
- Pandemic sparked off a wave of great resignation
- Geopolitical tensions exacerbated energy and food supply issues as well as logistic arrangement

Global Supply Chain Pressure Index



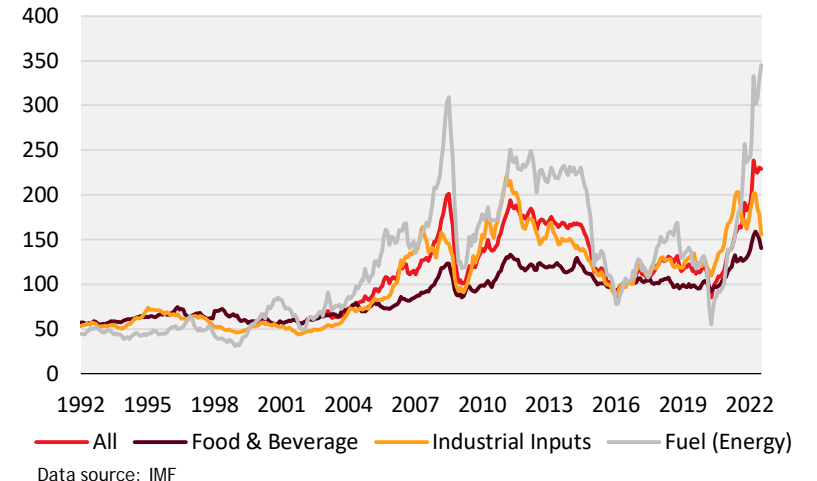
Source: Federal Reserve Bank of New York

US Labour Participation Rate



Source: Bloomberg

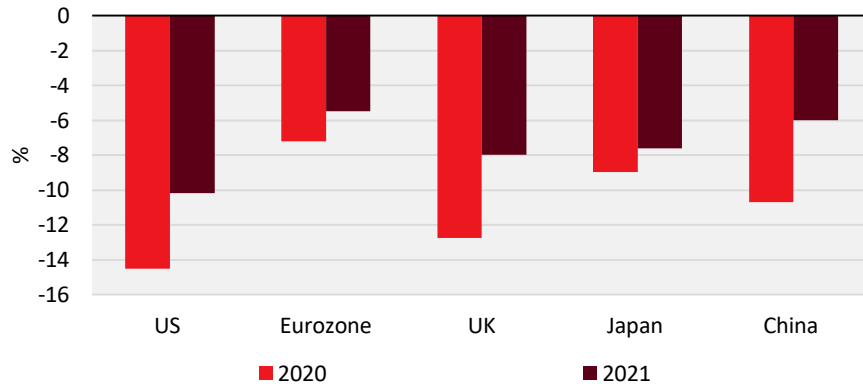
IMF Primary Commodity Prices (2016=100)



Data source: IMF

Excessive fiscal and monetary accommodation are another factor to blame

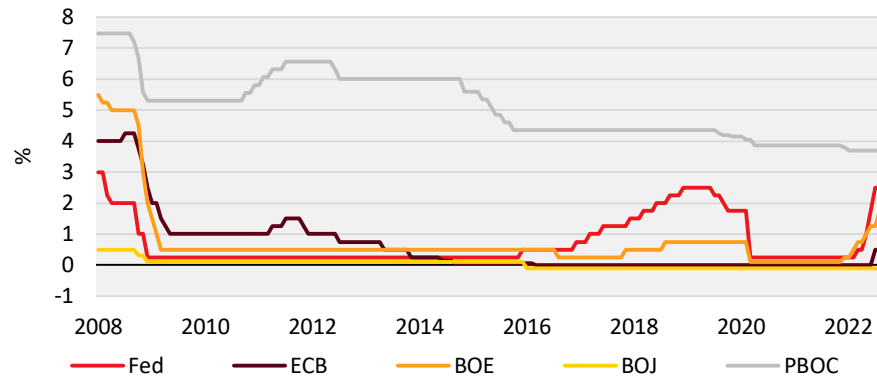
Budget Deficit (% of GDP)



Source: IMF

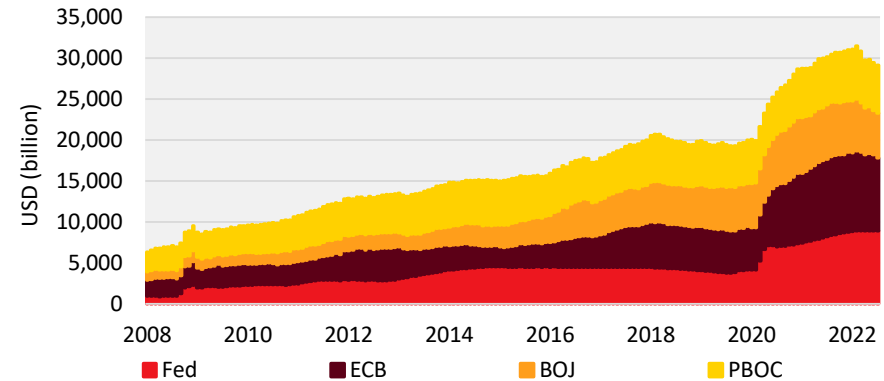
- Generous fiscal transfer was offered to stabilize the labour market
- Sharp reduction in policy rates and quantitative easing couldn't help pandemic disruption
- The central banks didn't rectify their monetary policy stance quick enough

Policy Rates



Source: Bloomberg

Balance Sheet (Asset Size)

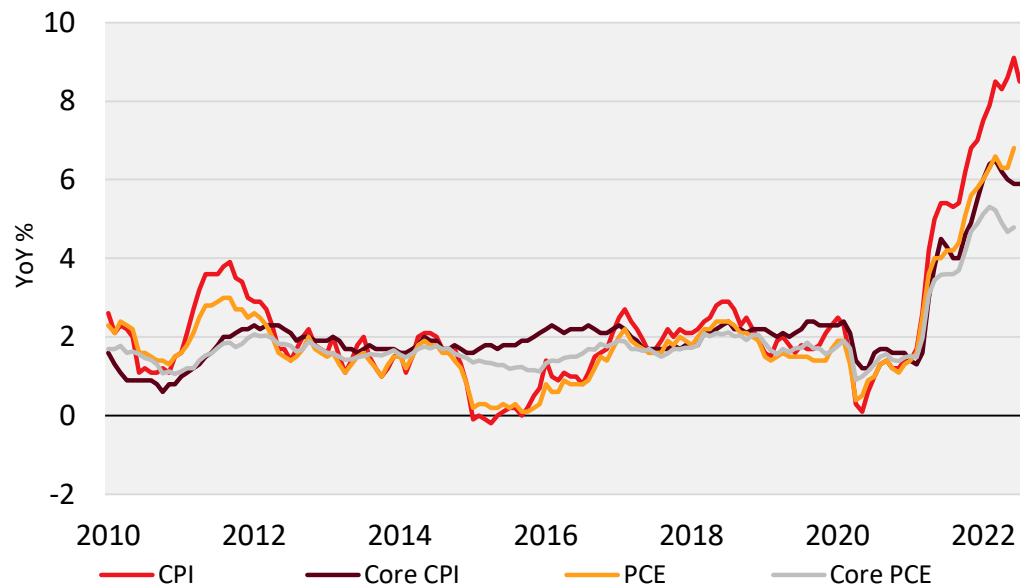


Source: Bloomberg

Inflationary pressure reaches multi-decade high

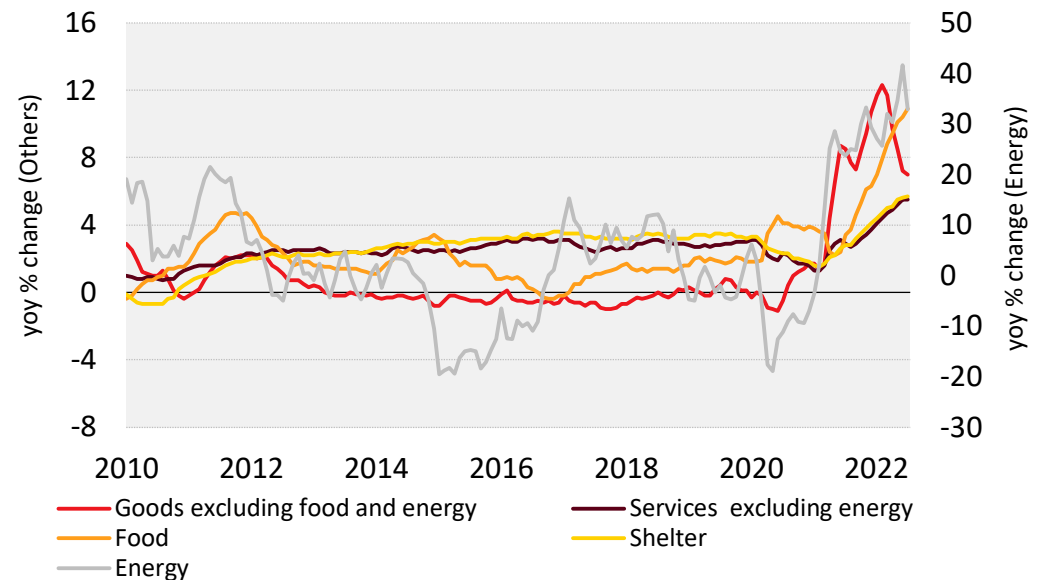
- Prolonged supply shocks, slow-to-adjust monetary accommodation and economic reopening resulted in broad-based increase in prices, including stickier services and shelter costs
- Unanchored inflation expectation is the last thing the global economy wants

US CPI & PCE Trend



Source: Bloomberg

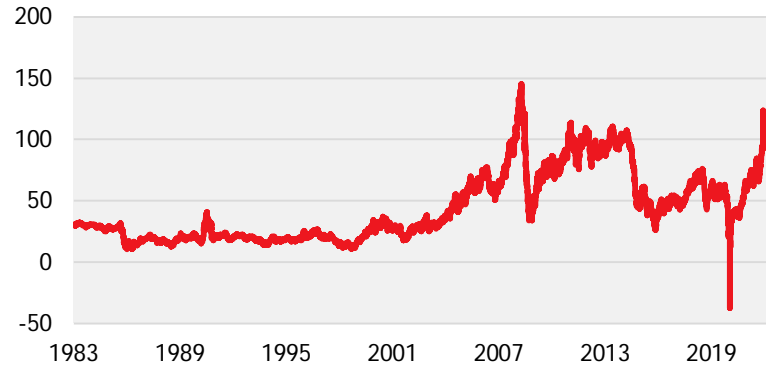
US CPI by Major Categories



Source: Bloomberg

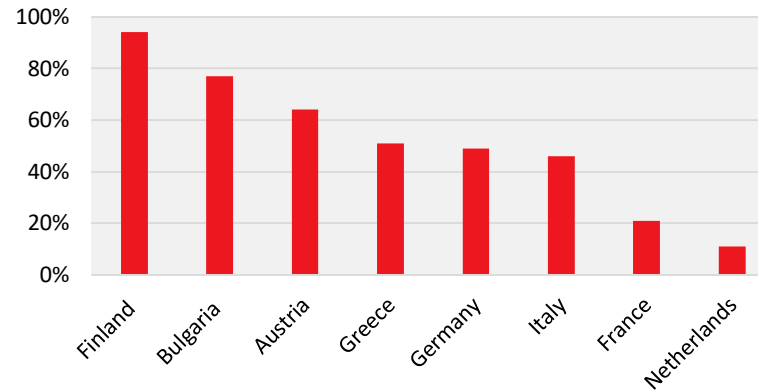
Supply-side pressure could potentially alleviate towards late 2022

WTI Crude Oil Futures Price (in USD, active contract)



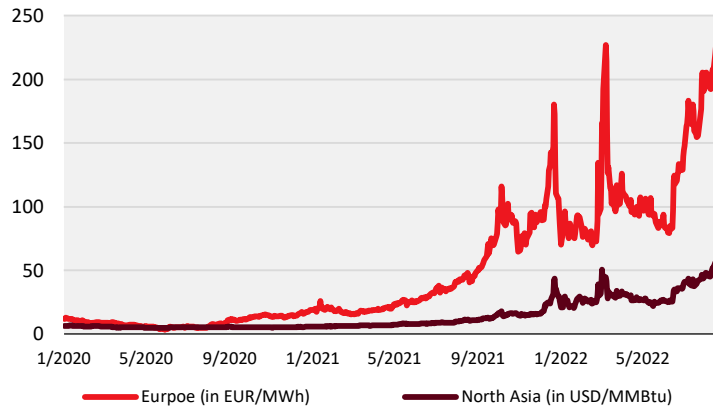
Source: Bloomberg

Dependence on Russian Natural Gas



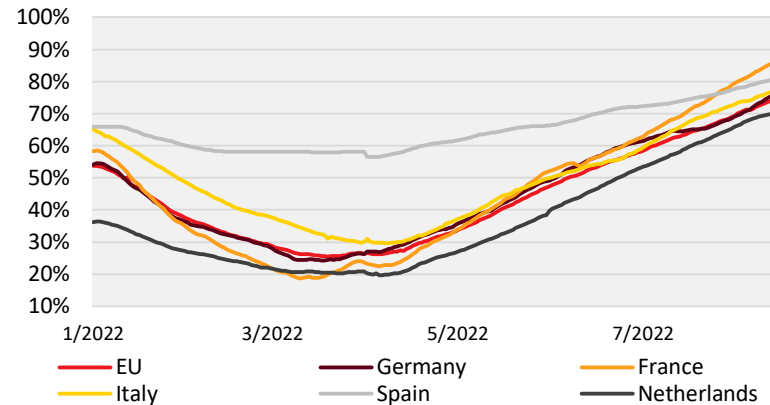
Source: European Union Agency for the Cooperation of Energy Regulators

Natural Gas Futures Price



Source: Bloomberg

Gas Storage (% of full)

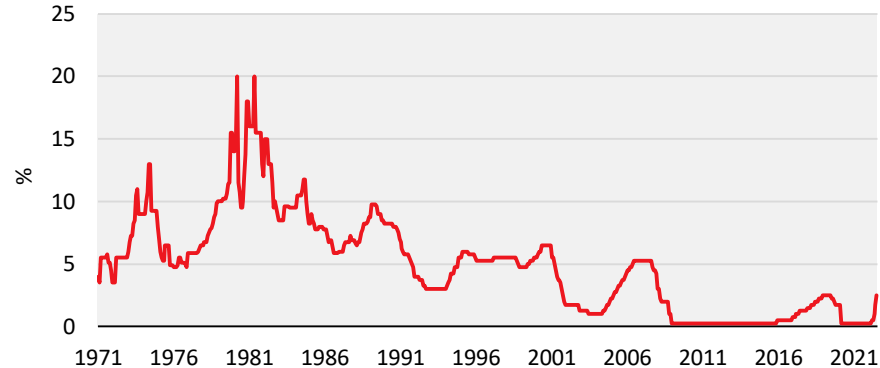


Source: Gas Infrastructure Europe

- The global economy (except Greater China) is on its way to normal functioning
- The world is adapting to new normal under Russia-related sanctions, energy and food supply disruption
- European natural gas remains one of the weakest links

Rapid interest rate hikes aim to control demand-side inflationary pressure

Fed Funds Rate Target (Upper Bound)



Source: Bloomberg

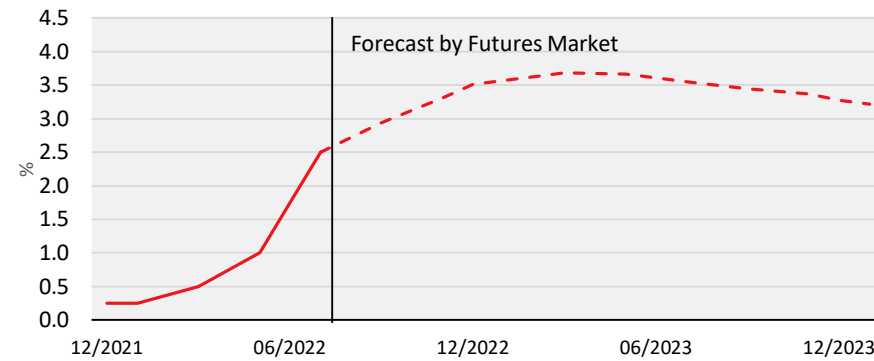
- After a period of inactions, central banks raised rates rapidly, but the rate level remains low compared to the 1970s and 1980s
- Inflation remains far higher than policy target. Markets might be too soon to price in rate cut next year

Major Central Banks' Rate Hike(s)

	Cumulative hike(s)	Duration
Federal Reserve	225 bps	6 months
European Central Bank	50 bps	2 months
Bank of England	165 bps	9 months
Bank of Canada	225 bps	6 months
Reserve Bank of Australia	175 bps	4 months
Reserve Bank of NZ	275 bps	11 months

Source: Bloomberg

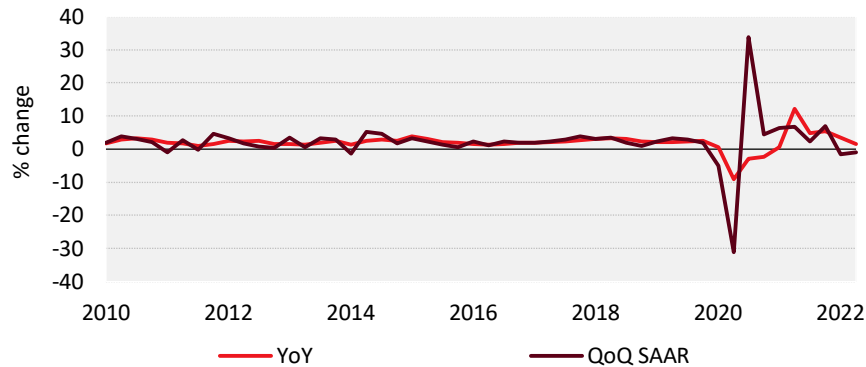
Fed Funds Rate



Source: Bloomberg

Growth slowdown unavoidable in advanced economies but employment markets remain robust

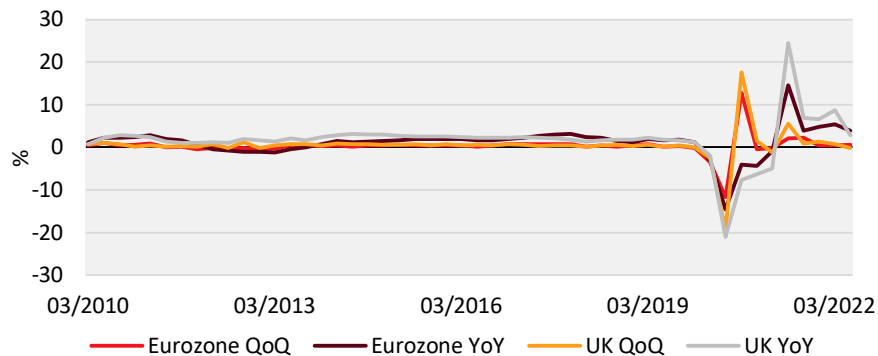
US GDP Growth



Source: Bloomberg

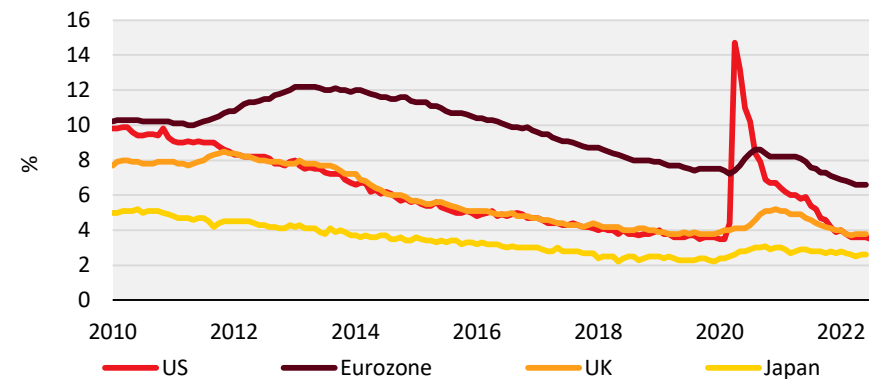
- According to IMF, no single major economy except Russia is forecasted to post negative growth
- The downward pressure could be offset by economic reopening, strong household financial position and robust employment markets, etc.
- The technical recession in the US is unlikely to be classified as a recession by NBER

Eurozone & UK Economic Growth



Source: Bloomberg

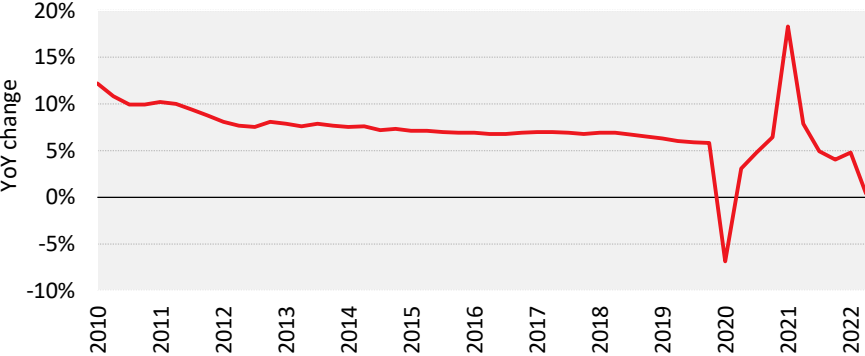
Unemployment Rate



Source: Bloomberg

Mainland economy bottomed in Q2

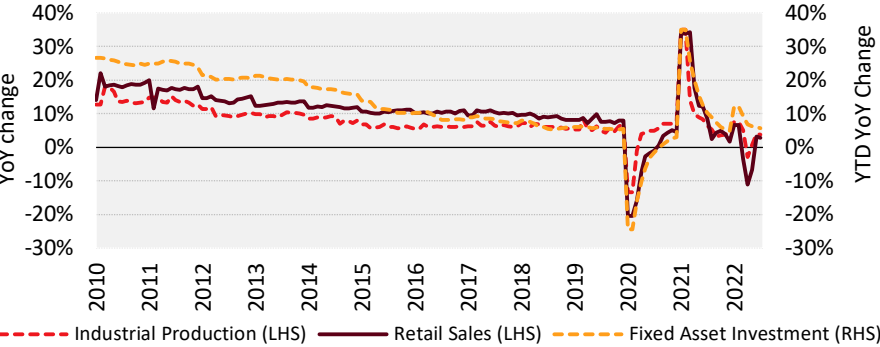
Mainland China GDP Growth



Source: National Bureau of Statistics of China

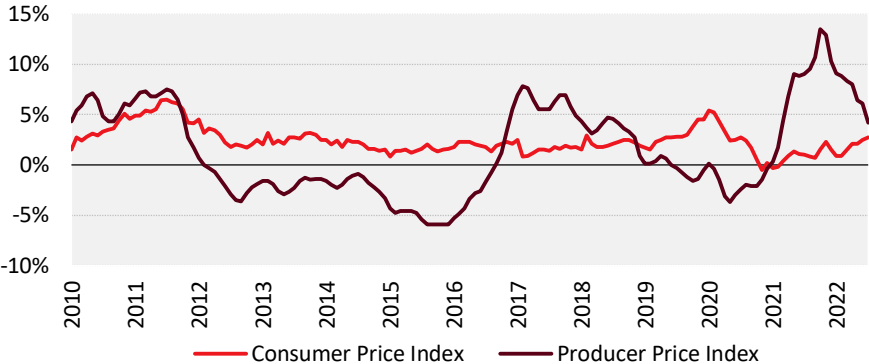
- Mainland economy likely bottomed out in Q2, amid stabilizing pandemic condition, and enhanced policy support
- The evolving regional outbreak and prolonged property market correction could partly offset the policy impact

Fixed Asset Investment, Retail Sales and Industrial Production



Source: National Bureau of Statistics of China

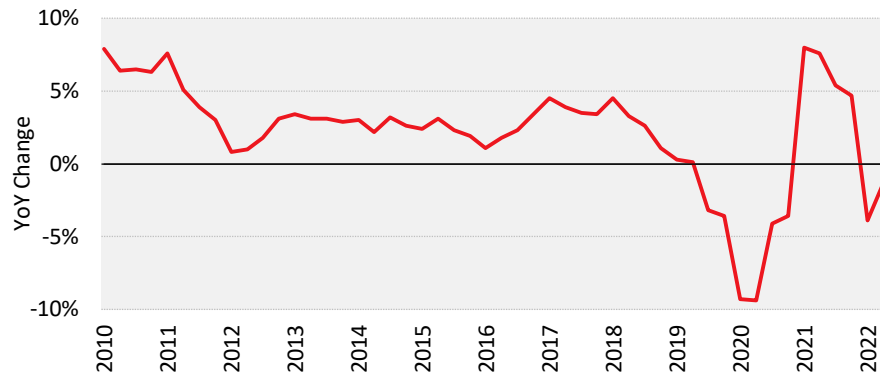
Mainland China Consumer and Producer Price Indices



Source: National Bureau of Statistics of China

Recovery in Hong Kong remains subdued, staying largely stagnant for 2022

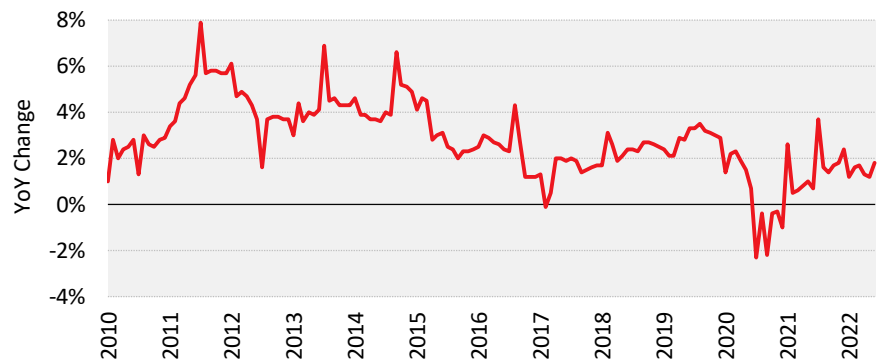
Hong Kong GDP Growth



Source: HK Census and Statistics Department

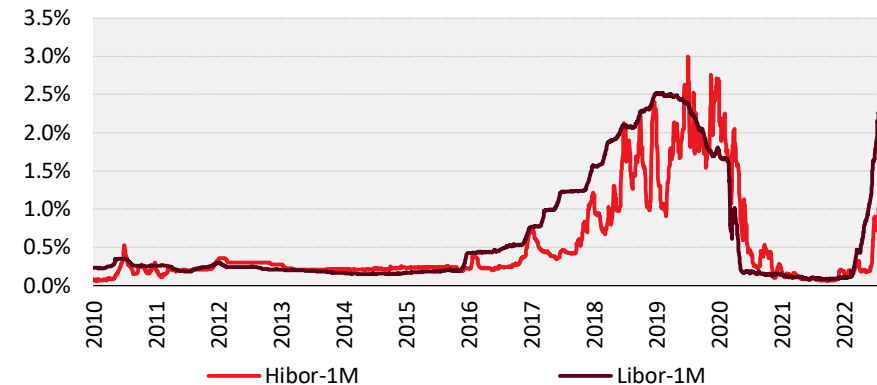
- Hong Kong avoided a technical recession, but its economy contracted 2.6% in 1H
- It takes time to fully return to normal, and the impact of consumption voucher likely to be short-lived
- Amid gloomier global economic outlook and tightening monetary policy stance, Hong Kong economy will stay stagnant in 2022

Hong Kong Consumer Price Index



Source: HK Census and Statistics Department

HK / US Interbank Rates



Source: Bloomberg

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