MACROECONOMIC PROJECTIONS

ECONOMIC BRIEF 28.092022

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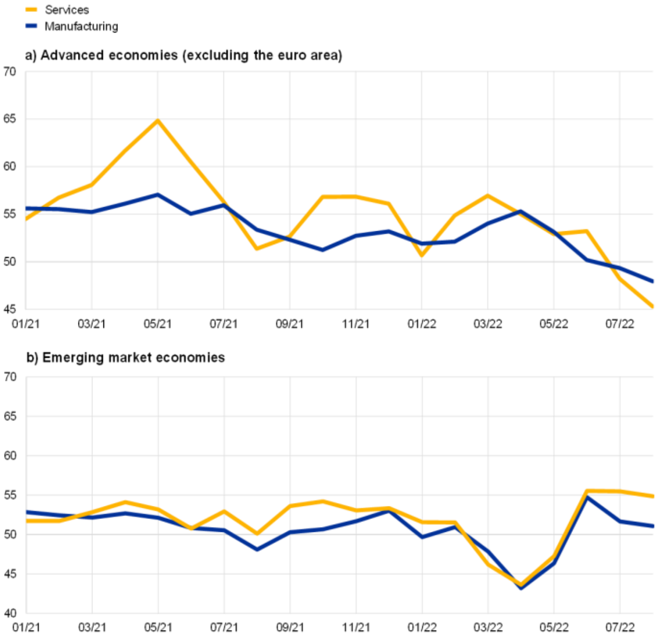
1. ECB Macroeconomic Projections

High inflation, tighter financial conditions and lingering supply bottlenecks are taking their toll as global economic activity is slowing down. According to the September 2022 ECB staff macroeconomic projections, the global growth outlook is subdued, with global real GDP – excluding the euro area – projected to grow by 2.9% in 2022, 3.0% in 2023 and 3.4% in 2024. This outlook is weaker than that described in the June 2022 Eurosystem staff macroeconomic projections and implies that the global economy is expected to grow at a rate slightly below its long-term average this year and next, as economic activity slows across advanced and emerging market economies. A weaker demand outlook and improved supply have helped to alleviate supply chain pressures, though these are still present. The outlook for global trade and euro area foreign demand has also deteriorated compared with the June projections. Global price pressures remain broad-based and elevated amid commodity price spikes, lingering supply constraints, still relatively robust demand and tight labour markets. These pressures are, however, expected to decline as commodity markets stabilise and growth weakens. In an environment of high uncertainty, the balance of risks around the baseline projections is tilted to the downside for global growth and to the upside for global price pressures.

PMI output by sector and economy type



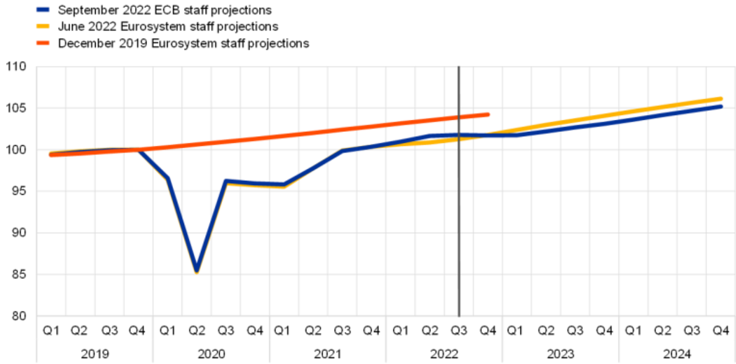
On 8 September 2022 the Governing Council decided to raise the three key ECB interest rates by 75 basis points. This major step frontloads the transition from the prevailing highly accommodative level of policy rates towards levels that will ensure the timely return of inflation to the Governing Council's 2% medium-term target. Based on the Governing Council's updated assessment, over the next several meetings it expects to raise interest rates further to dampen demand and guard against the risk of a persistent upward shift in inflation expectations.[1]

[1] Economic Bulletin Issue 6, 2022 (europa.eu)

2. Euro Area Economic Growth

Beyond the near term, euro area economic growth is expected to gradually pick up after the headwinds weighing on activity during the winter of 2022/23 dissipate. The uncertainty surrounding this outlook remains large. The September 2022 ECB staff macroeconomic projections foresee annual real GDP growth at 3.1% in 2022, 0.9% in 2023 and 1.9% in 2024. Compared with the June 2022 Eurosystem staff macroeconomic projections, the growth outlook was revised upwards for 2022 and downwards for 2023 and 2024. Quarterly year-on-year real GDP growth is projected to be 1.4% in the fourth quarter of 2022, 1.4% in the fourth quarter of 2023 and 2% in fourth quarter of 2024. This shows that the projected average real GDP growth rate for 2022 is strongly influenced by positive carry-over effects from the dynamic first half of the year, while the projected average real GDP growth rate for 2023 is strongly influenced by the expected slowdown in the second half of 2022.[2]

Euro area real GDP (including projections)



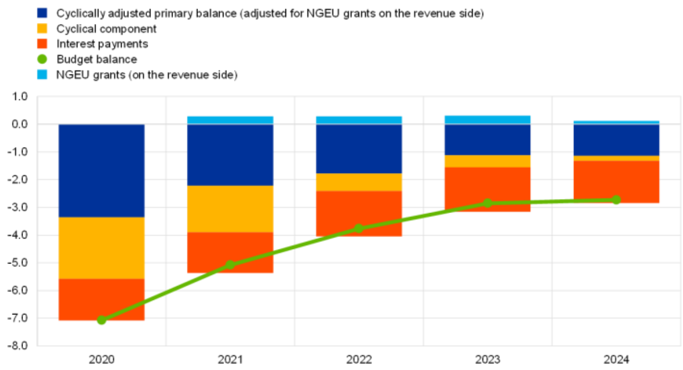
3. Fiscal Developments

According to the September 2022 ECB staff macroeconomic projections, the euro area budget balance is projected to improve steadily in the period up to 2024, although by somewhat less than foreseen in the June projections. However, the fiscal projections continue to be surrounded by high levels of uncertainty, mainly related to the war in Ukraine and developments in energy markets that could lead governments to adopt additional fiscal stimulus measures. Recently, such fiscal support measures have been largely aimed at countering the rising cost of living for consumers, in particular for energy. Moreover, the financing of new defence capacities and support for refugees from Russia's war in Ukraine have also played a role. Nevertheless, the euro area government budget deficit is expected to continue to fall – from 5.1% of GDP in 2021 to 3.8% in 2022 and then to 2.7% by the end of the forecast horizon. Following the strong fiscal loosening in response to the coronavirus (COVID-19) crisis in 2020, the fiscal stance tightened last year and is projected to continue to tighten somewhat, in particular in 2023, and to be neutral in 2024. In a context of heightened uncertainty and downside risks to the economic outlook owing to the war in Ukraine, as well as energy price increases and

[2] Economic Bulletin Issue 6, 2022 (europa.eu)

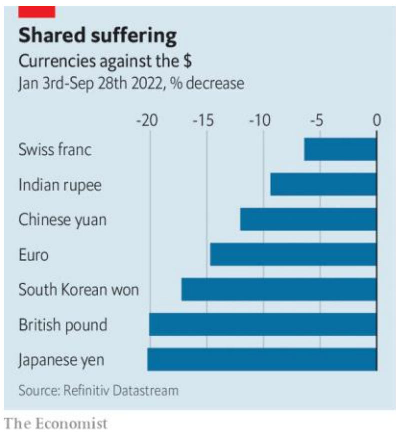
continued supply chain disturbances, on 23 May 2022 the European Commission recommended extending the general escape clause of the Stability and Growth Pact (SGP) to the end of 2023. This would allow fiscal policies to adjust to changing circumstances if necessary. At the same time, with fiscal imbalances still exceeding their pre-pandemic levels and inflation exceptionally high, fiscal policy needs to be increasingly selective and targeted in order to avoid adding to medium-term inflationary pressures, while ensuring fiscal sustainability over the medium term.[3]

Budget balance and its components



4. Currency Movements

Higher rates in America have turbocharged the dollar. The dxy, an index of the greenback against half a dozen major currencies, has risen by nearly 18% this year, and is now at its highest in more than two decades. The flip side of dollar strength has been drama elsewhere. In Britain sterling took a breathtaking dive, aided by the government's decision to unveil the country's largest tax cuts since the 1970s. Short-term interest rates rose just as spectacularly. Meanwhile, the euro reached its lowest point against the greenback in two decades on September 26th. Expectations of rate rises by the European Central Bank, as it fights the resulting increase in imported inflation, sent bond yields in the euro area rising, too. In heavily indebted Italy yields on ten-year sovereign bonds are not far off a worrying 5%.



Jolting currency movements have led to a spate of interventions. In Japan, where the central bank is fighting an increasingly lonely battle to keep interest rates low, the government intervened to prop up the yen for the first time since the Asian financial crisis in 1998; China's central bank is requiring banks to post reserves when selling foreign-exchange derivatives contracts, making it harder to bet against the yuan. [4]

[3] Economic Bulletin Issue 6, 2022 (europa.eu)
[4] Financial markets are in chaos. What next for the real economy? | The Economist

5. North Macedonia

The European Bank for Reconstruction and Development (EBRD) said it expects North Macedonia's gross domestic product (GDP) to increase by 2.7% in 2022, revising downwards its projection for 3% growth made in May. In 2023, North Macedonia's GDP is forecast to grow by 2.3%, the EBRD said in the September edition of its Regional Economic Prospects report. In the May issue of the report, the EBRD projected economic growth of 3% for North Macedonia in 2023.

The revisions since May are driven mostly by the reduced gas supplies from Russia and rising inflation on a global level, which are expected to slow economic growth in 2023 in the regions where EBRD works, the bank said.

The EBRD now forecasts economic growth of 3.2% in 2022 and 3% in 2023 for the Western Balkans region. However, projections are subject to major downside risk should Russia’s war on Ukraine escalate or the volume of its gas exports decline even more, the EBRD noted.[5]

[5] EBRD cuts N. Macedonia's 2022, 2023 GDP growth projections (seenews.com)