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Key Global Macroeconomic Themes For 2022

December 2021

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Key Global Macro Themes For 2022

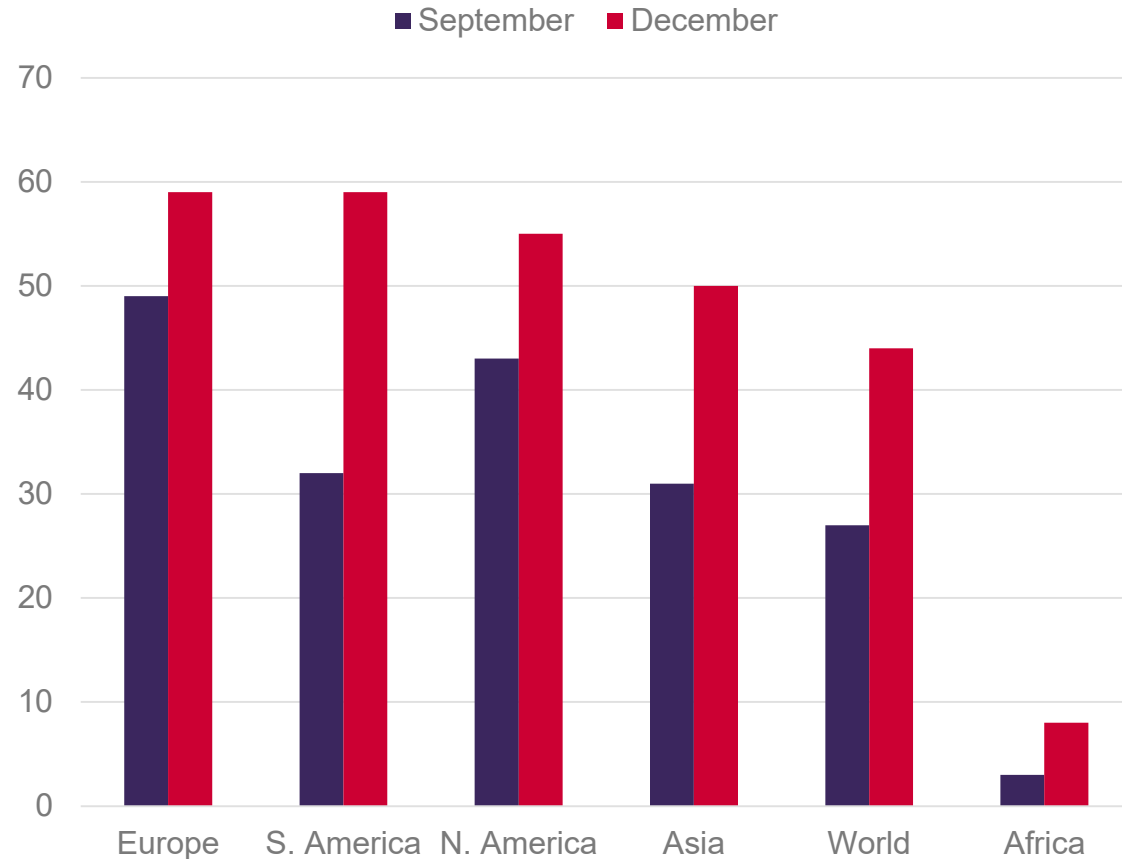
Theme	View	Theme	View
1	Almost Full Economic Normalisation & Covid-19 Policy Pivot	6	A Tough Landscape For EM Policymakers
2	Another Year Of Above-Trend Growth, But A Cyclical Slowdown Nonetheless	7	Financial Markets Not A One-Way Bet In 2022
3	Tourism Will See An Uneven Recovery	8	Rising Polarisation & Divergent Reform Momentum
4	Inflation Will Peak As Rebalancing Occurs	9	Old Opportunities And Risks In Geopolitics
5	Developed Markets Will Start To Tighten Policy, But Not As Much As Rate Markets Suggest	10	Risks Will Remain Top Of Mind

Source: Fitch Solutions

Theme 1: Almost Full Economic Normalisation & Covid-19 Policy Pivot

Rising Vaccinations And Antiviral Treatments Are Positive

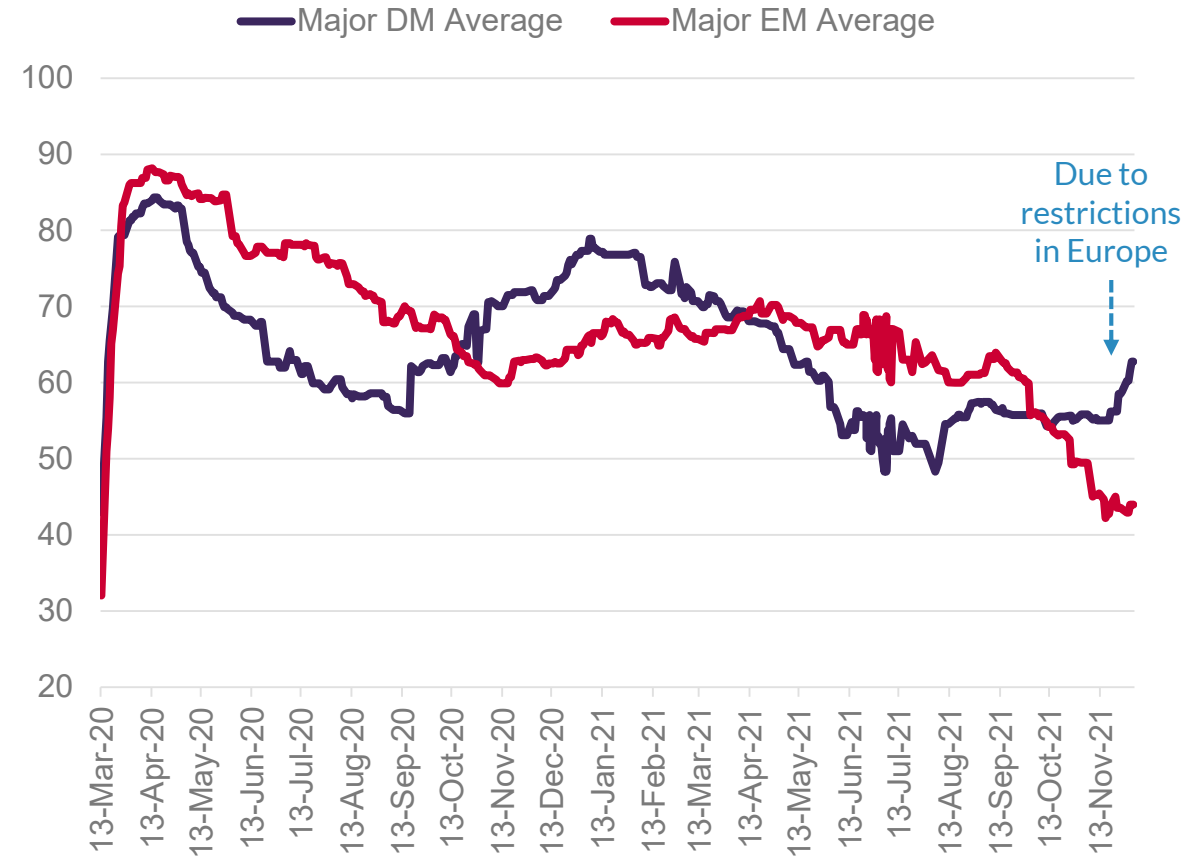
Persons Fully Vaccinated, per 100 people



Source: Our World in Data, Fitch Solutions

Despite Seasonal Rise, Restrictions Will Head Lower

Stringency Index

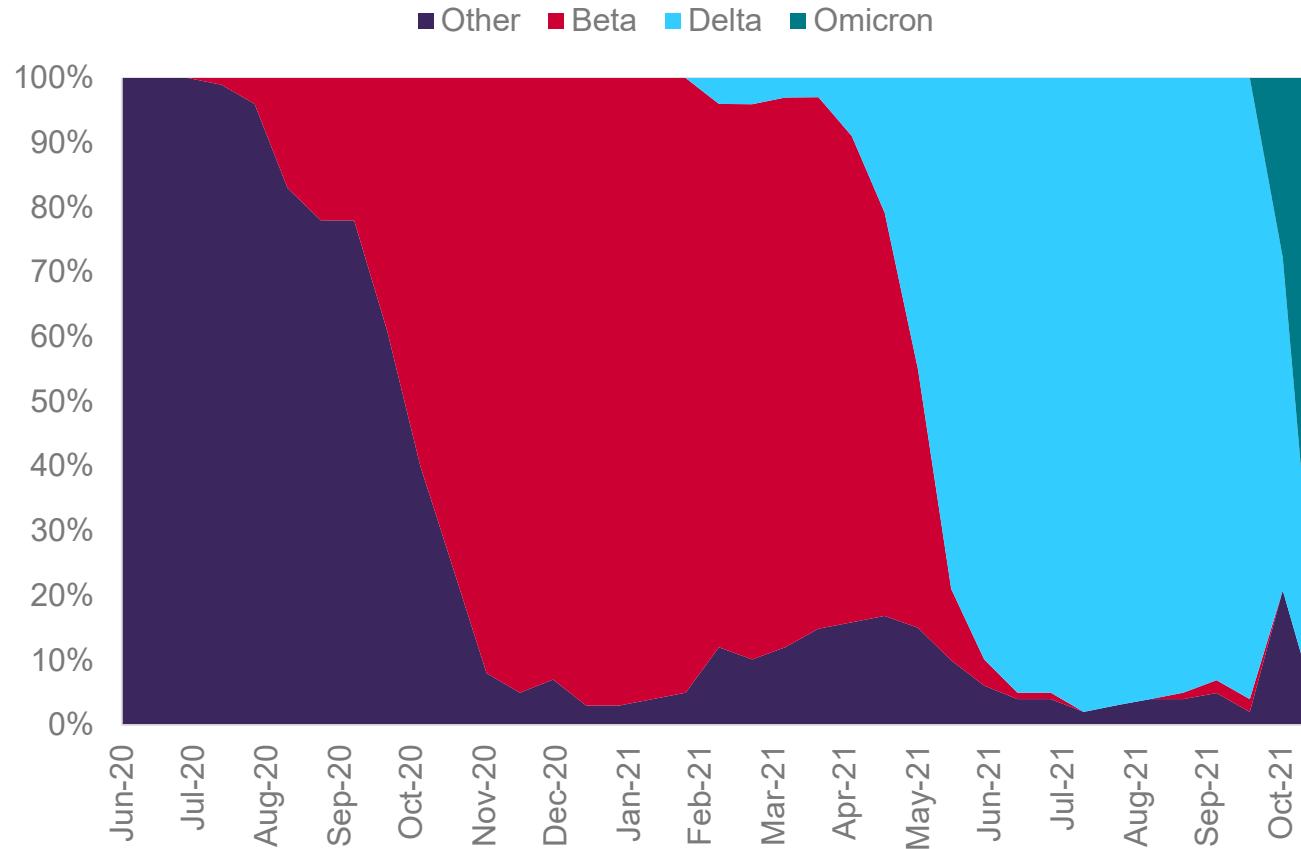


Source: University of Oxford, Bloomberg, Fitch Solutions

Omicron Poses A Risk To This View And Global Growth

The Rise Of Omicron Could Change Everything

South Africa – Cases By Variant



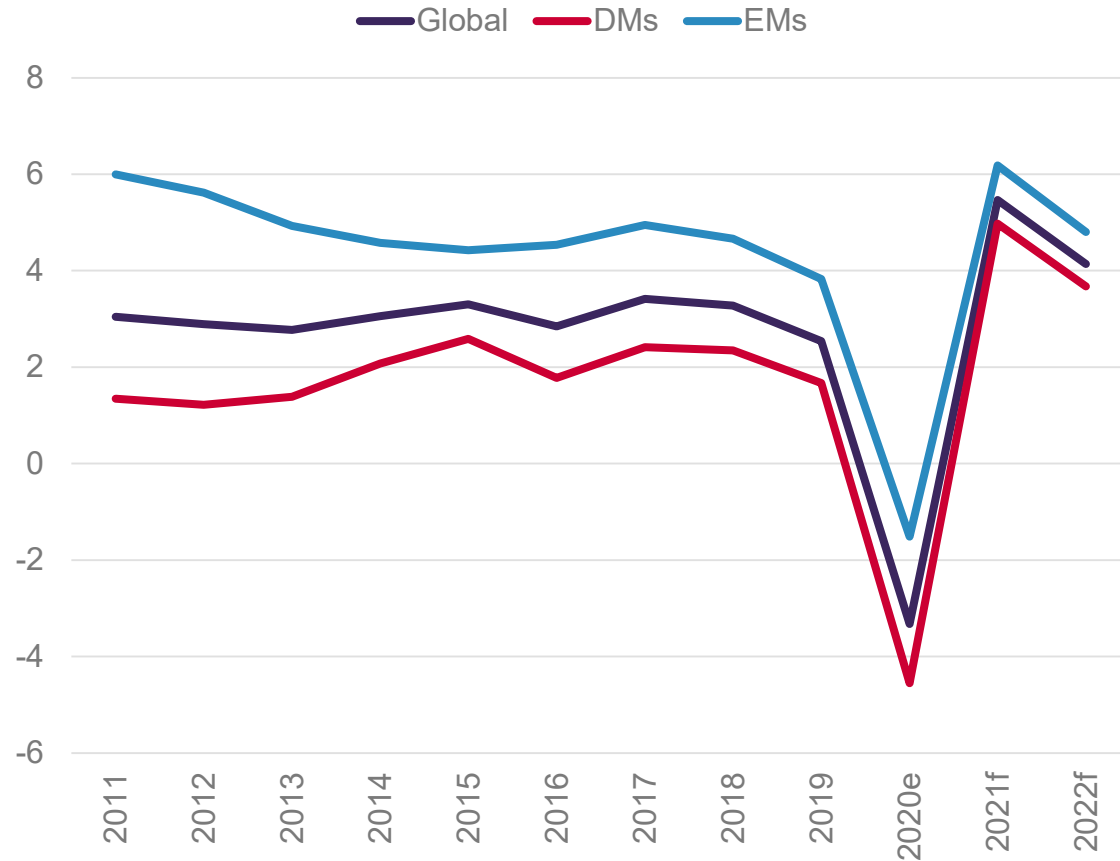
Source: GISAID, Fitch Solutions

- The Omicron variant poses significant risks given that it is likely much more transmissible than the Delta variant and is becoming dominant.
- Already it accounts for 88% of all infections in South Africa and 14% in the US.
- Scientists do not yet know whether the symptoms are more severe than the Delta variant and whether vaccines remain effective against it.
- If symptoms are more severe and vaccine efficacy drops, this could lead to new lockdowns as many countries have already implemented travel restrictions. This would have a large and negative impact on global growth.
- However, if symptoms are less severe and the vaccines remain effective, this is good news as Omicron will overtake Delta as the most prevalent variant.

Theme 2: Above-Trend Growth, But A Cyclical Slowdown Nonetheless

Global Growth To Ease From Abnormally High Levels

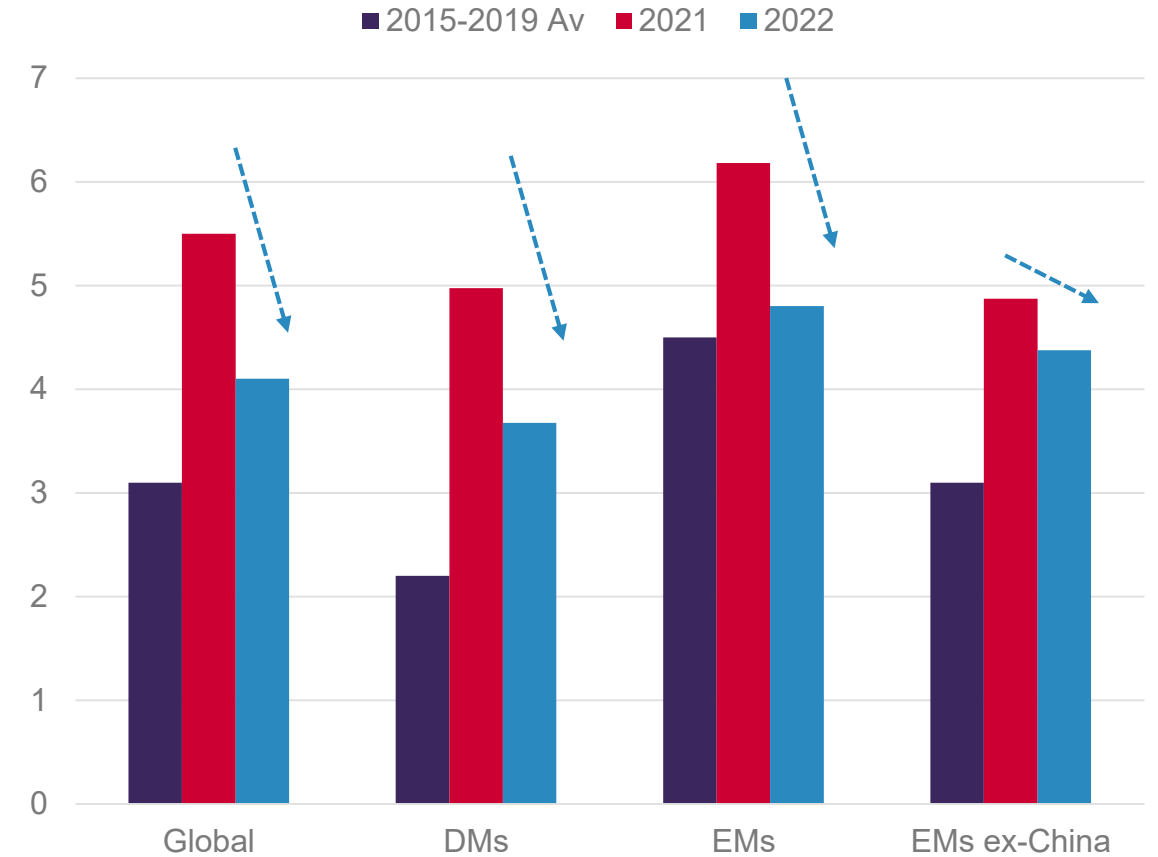
Real GDP Growth, %



e/f = estimate/forecast. Source: Fitch Solutions

EMs Holding Up Against China's Slowdown

Real GDP Growth, %



Source: Fitch Solutions

Slowdown Will Be Broad, But Regional Differences Exist

Slowdown In Growth, But Certain Economies Buck The Trend

Real GDP Growth, %

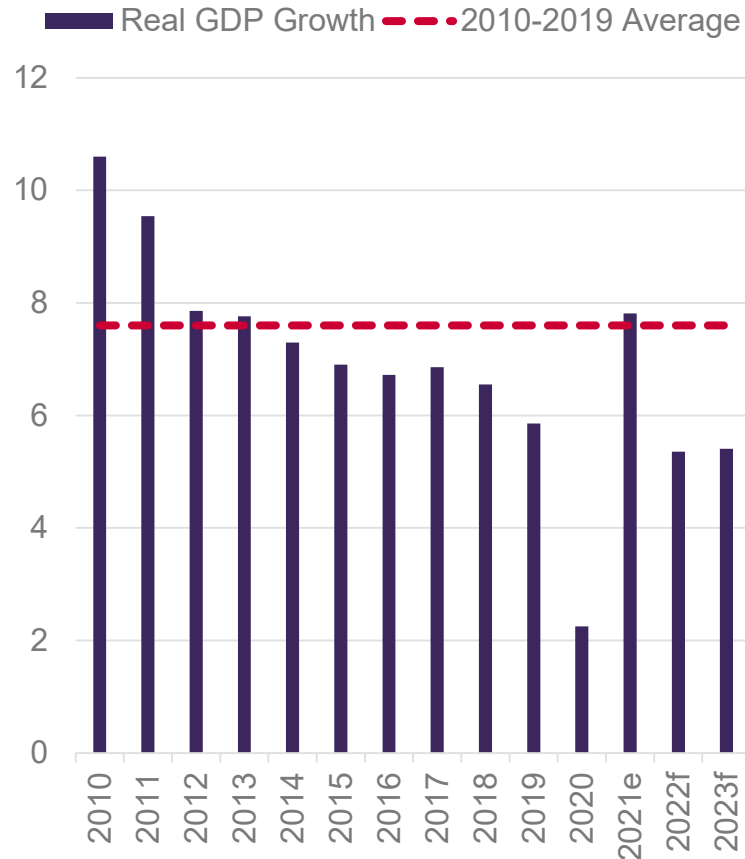


f = Fitch Solutions forecast. Source: Fitch Solutions

But China's Economy Will Face A Cyclical And Structural Slowdown

China To See A New Growth Trend

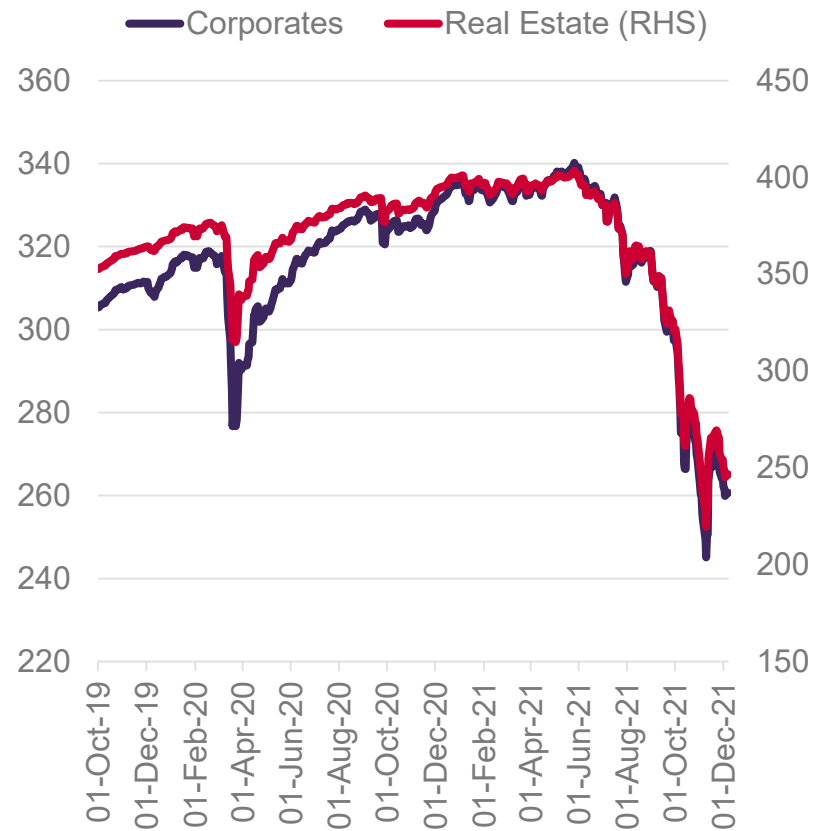
Real GDP Growth, %



Source: Fitch Solutions

High Yield Market In China Still Stressed

Markit iBoxx USD Asia ex-Japan China High Yield Indices



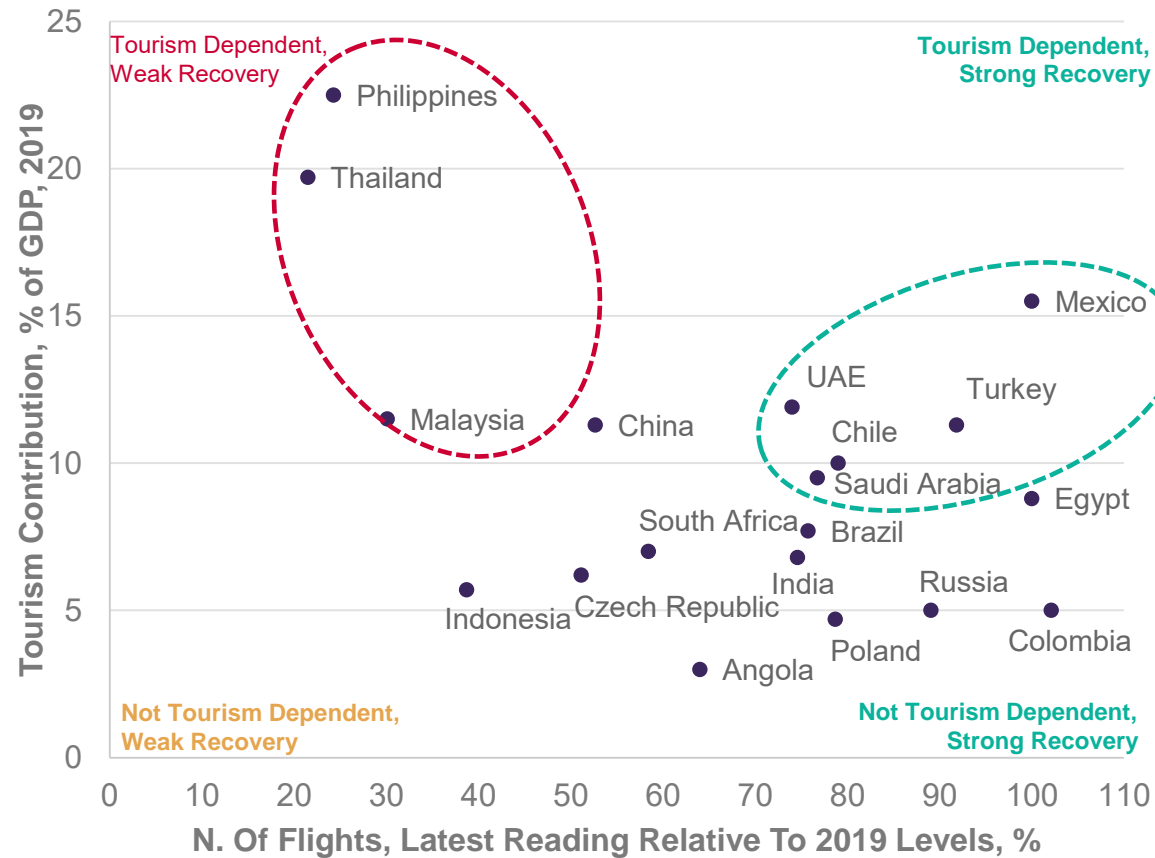
Source: Bloomberg, Fitch Solutions

- From a cyclical perspective, high base effects, the regulatory crackdown, a zero-Covid policy and property sector risks will weigh heavily on growth in 2022.
- The property sector is of particular concern given ongoing cashflow issues with major developers as well as still-elevated credit stress in the high yield segment.
- From a structural perspective, worsening demographics, higher debt loads, lower growth targets and macroprudential policies aimed at reining in financial risks will see growth slow over the coming year.

Theme 3: Tourism Will See An Uneven Recovery

Asian Economies Lagging Behind, Mexico Doing Best

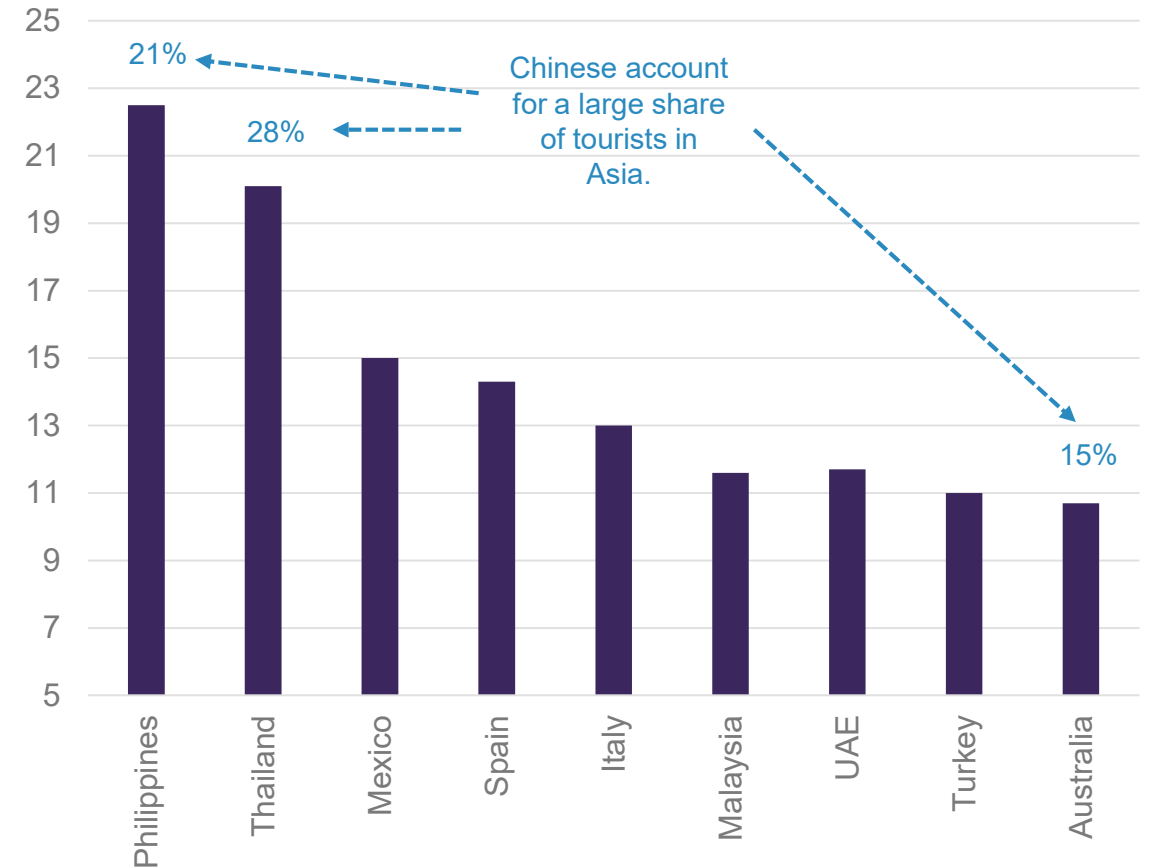
Tourism Contribution To GDP vs Recovery In Number of Flights, %*



*As of Mid November. Source: Fitch Solutions

Those Dependent On Tourism & China Will Recover Slowly

Tourism Contribution To GDP, & Chinese Tourists Share Of Total, % (2019)

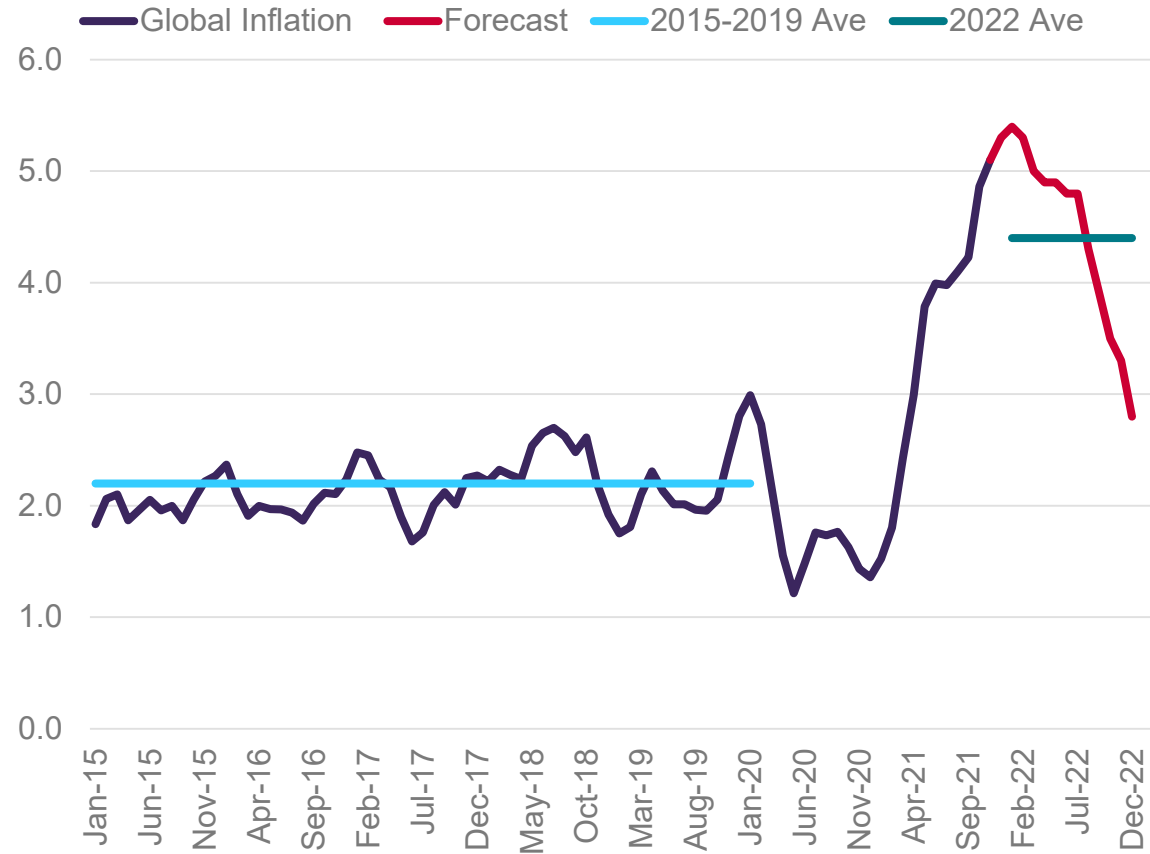


Source: WTTC, Fitch Solutions

Theme 4: Inflation Will Peak As Rebalancing Occurs

Global Inflation Will Slowly Peak

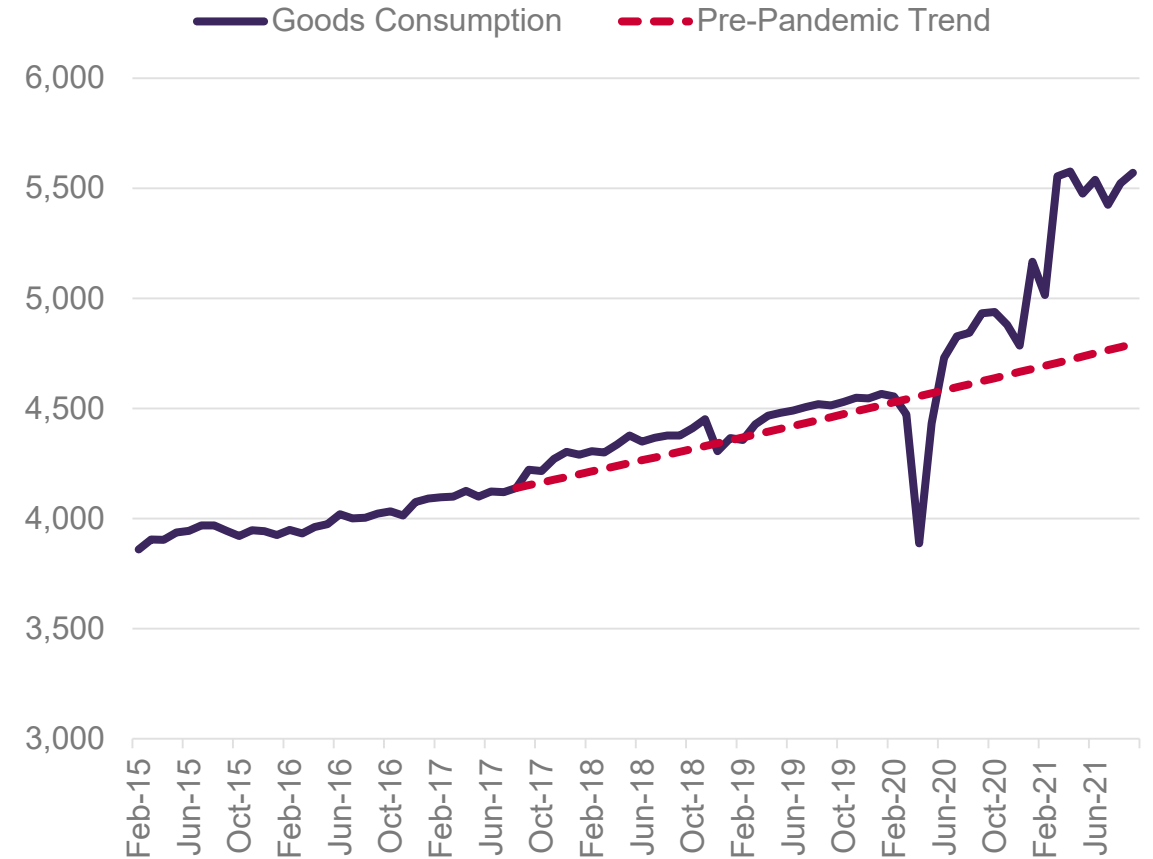
Global Inflation, %



Source: Bloomberg, Fitch Solutions

Goods Demand Well Above Trend, But Should Normalise

US PCE Goods Consumption USDbn & Trend

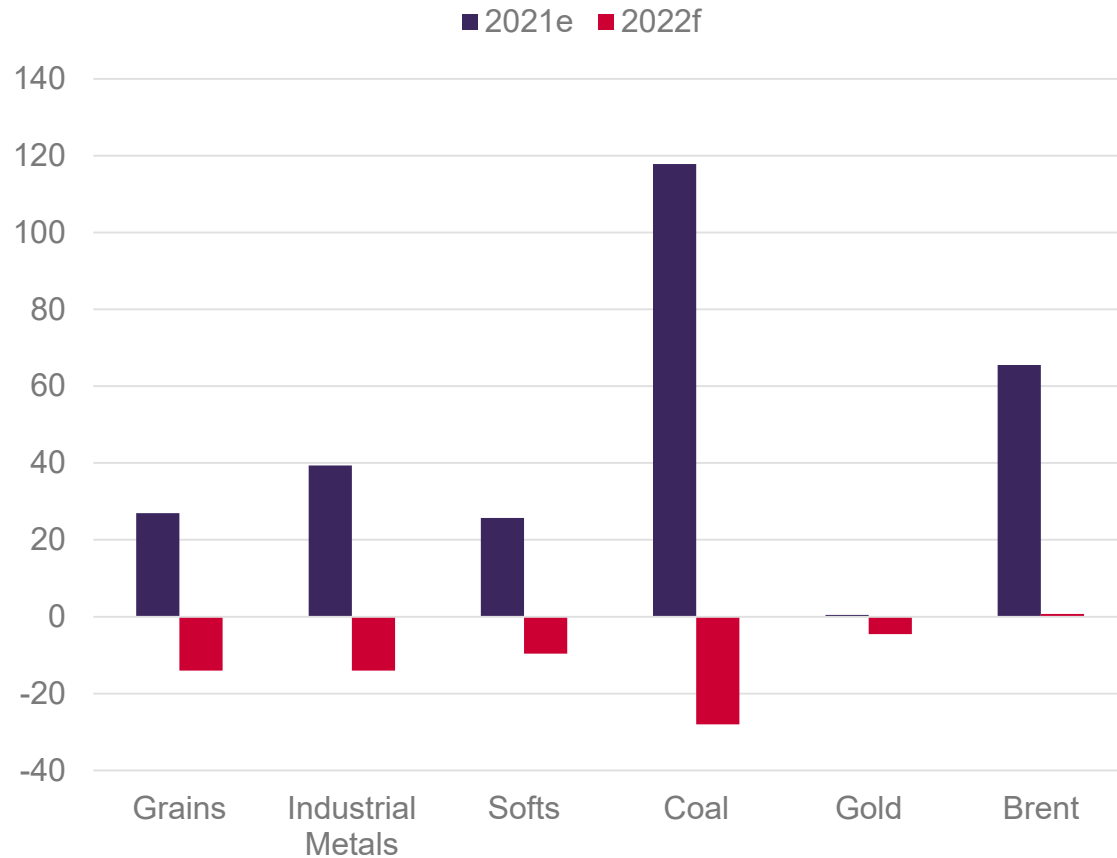


Source: Bloomberg, Fitch Solutions

Base Effects, Lower Commodity Prices And Seasonality Should Help

After A Surge In 2021, Commodity Prices Will Ease

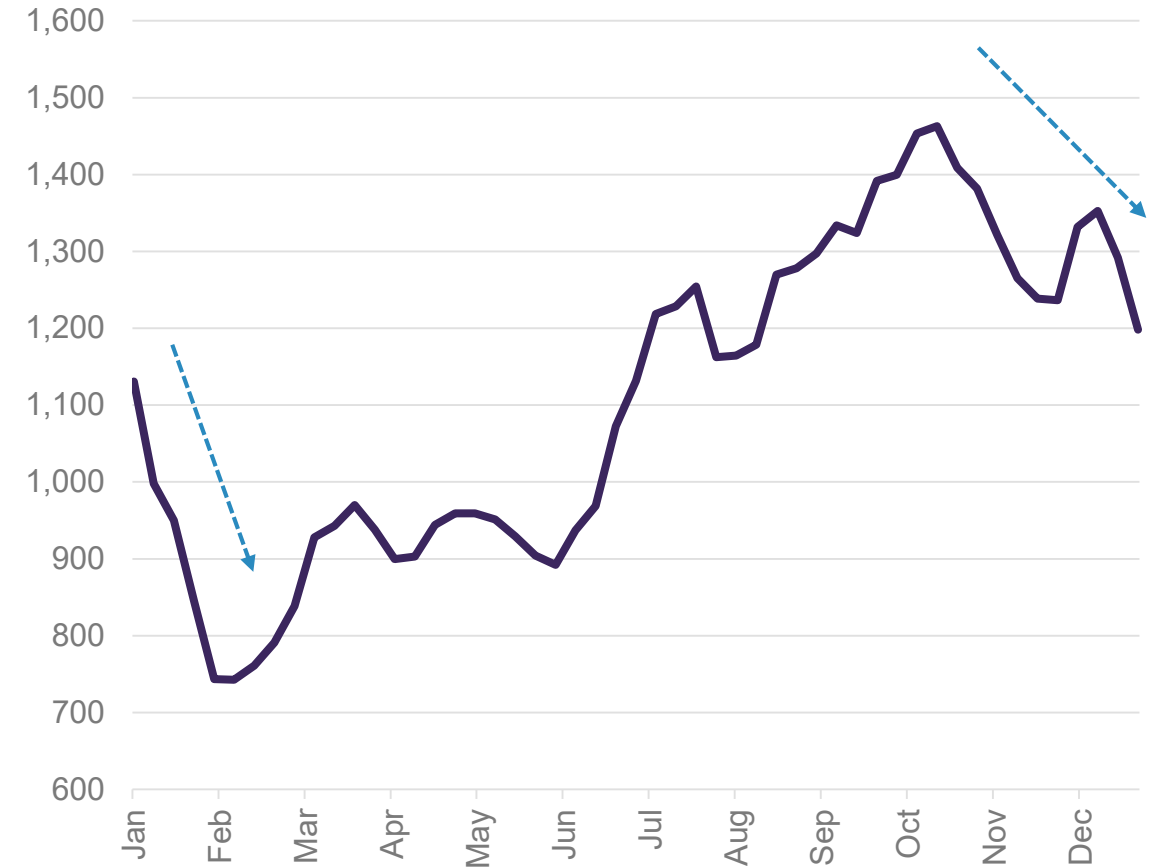
Change In Commodity Prices, %



e/f = estimate/forecast. Source: Fitch Solutions

Shipping Rates Show Seasonal Weakness After Holidays

Baltic Dry Index Trend Over Calendar Year (2010-2021 average)

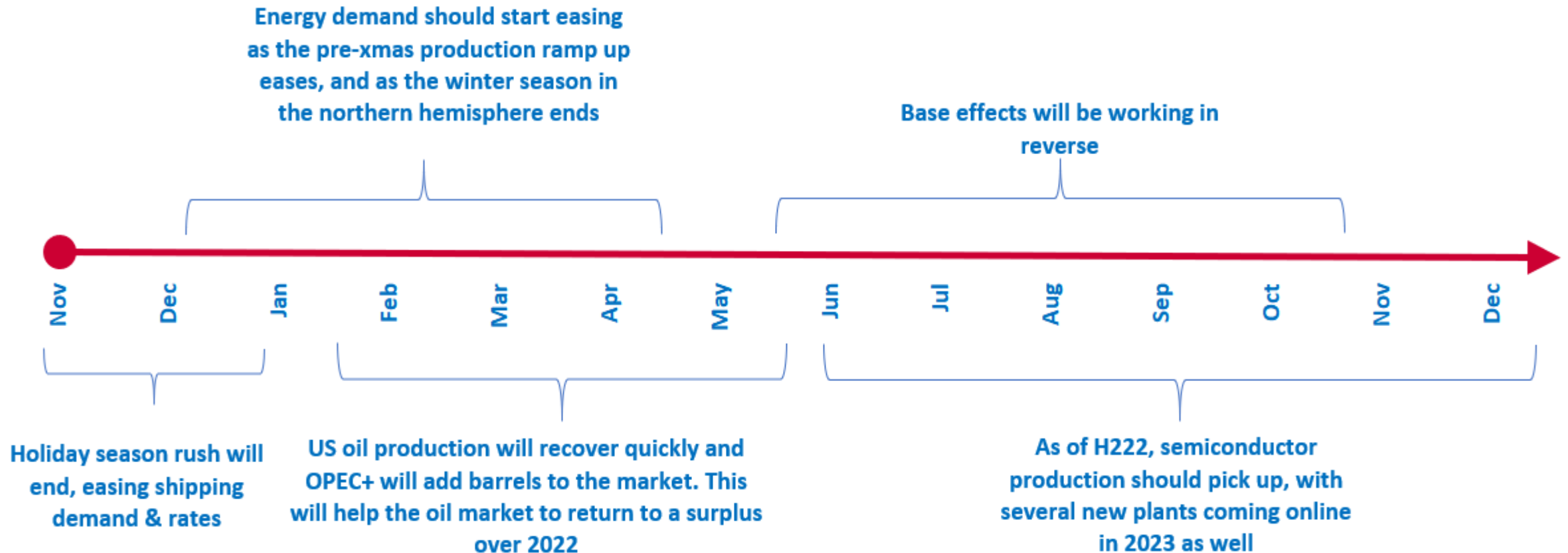


Source: Bloomberg, Fitch Solutions

Various Factors Point To Slowing Inflation

Inflation Should Start Easing Over The Coming Quarters

Factors That Will Help Inflation To Ease

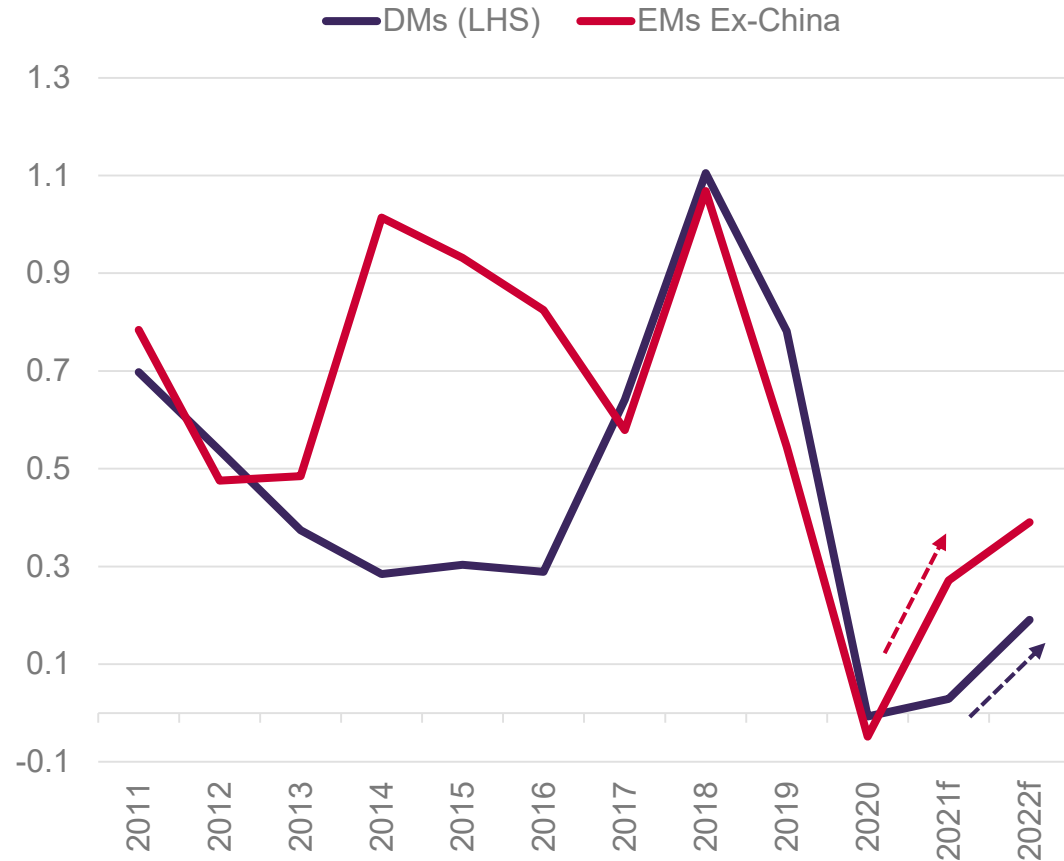


Source: Fitch Solutions

Theme 5: DMs Will Tighten Policy, But Less Than Rate Markets Suggest

EMs Raised Interest Rates First, DMs To Follow

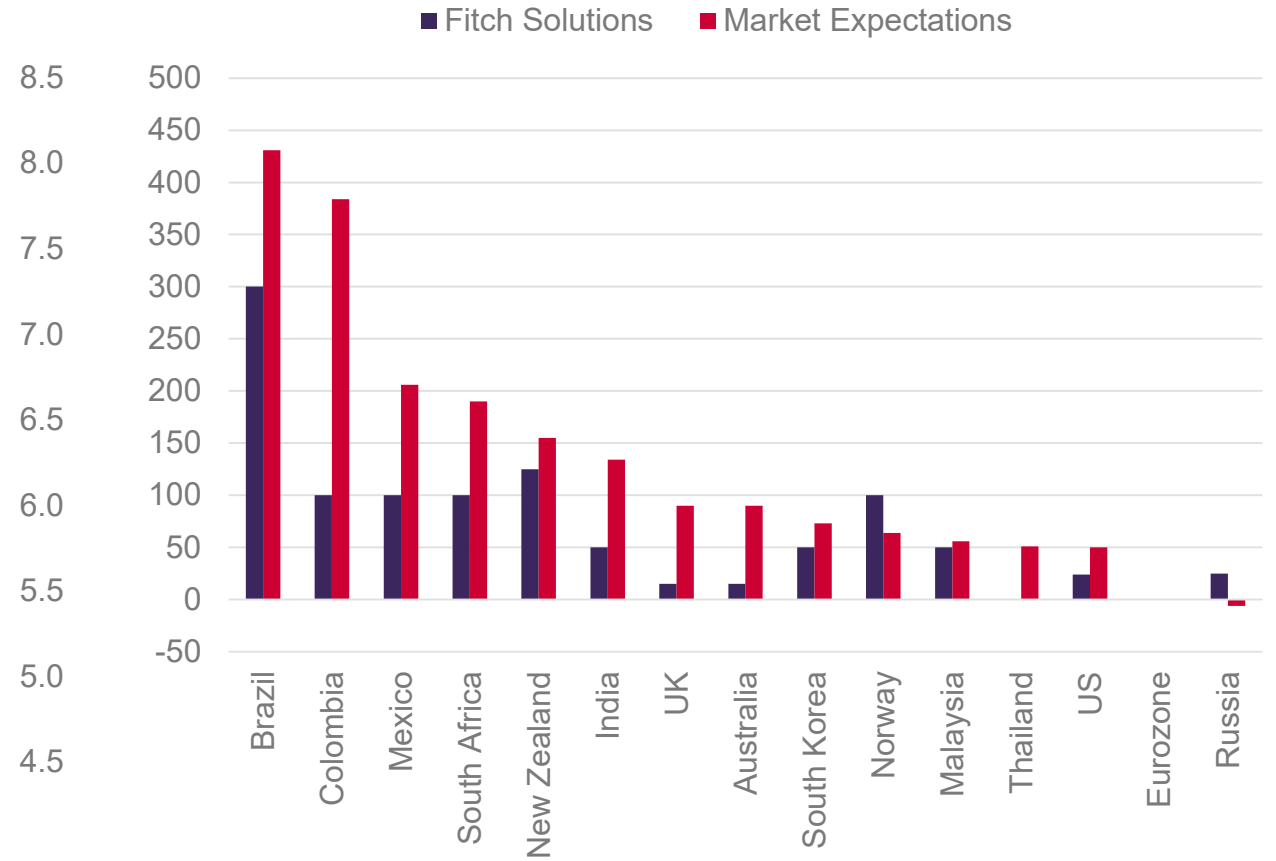
Policy Interest Rate, %



Note: Weighted average. f = forecast. Source: Fitch Solutions

Markets Seem Too Hawkish

Change In Interest Rates, bps

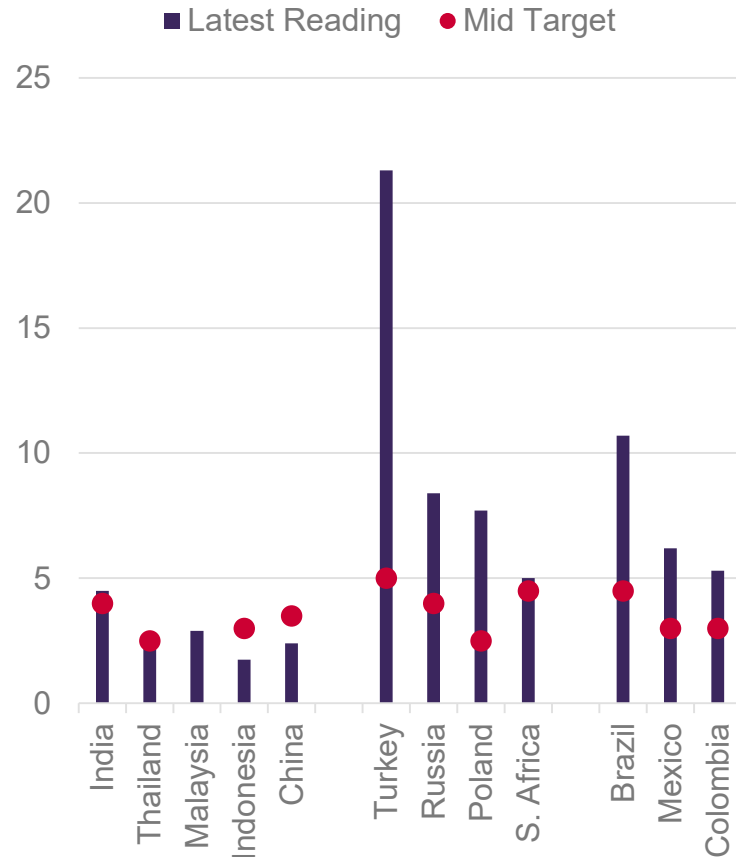


Source: Bloomberg, Fitch Solutions

Theme 6: A Tough Landscape For EM Policymakers

Inflation Is Well Above Target In EMs

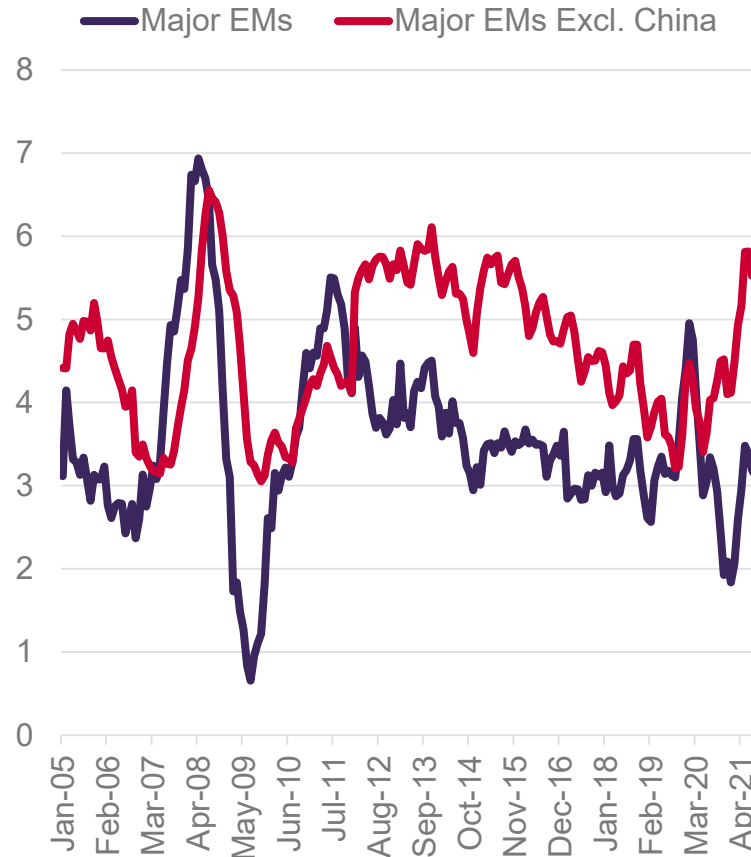
Inflation vs Mid-Point Target, %



Source: Bloomberg, Fitch Solutions

Excluding China, Inflation Is Elevated

Inflation, %



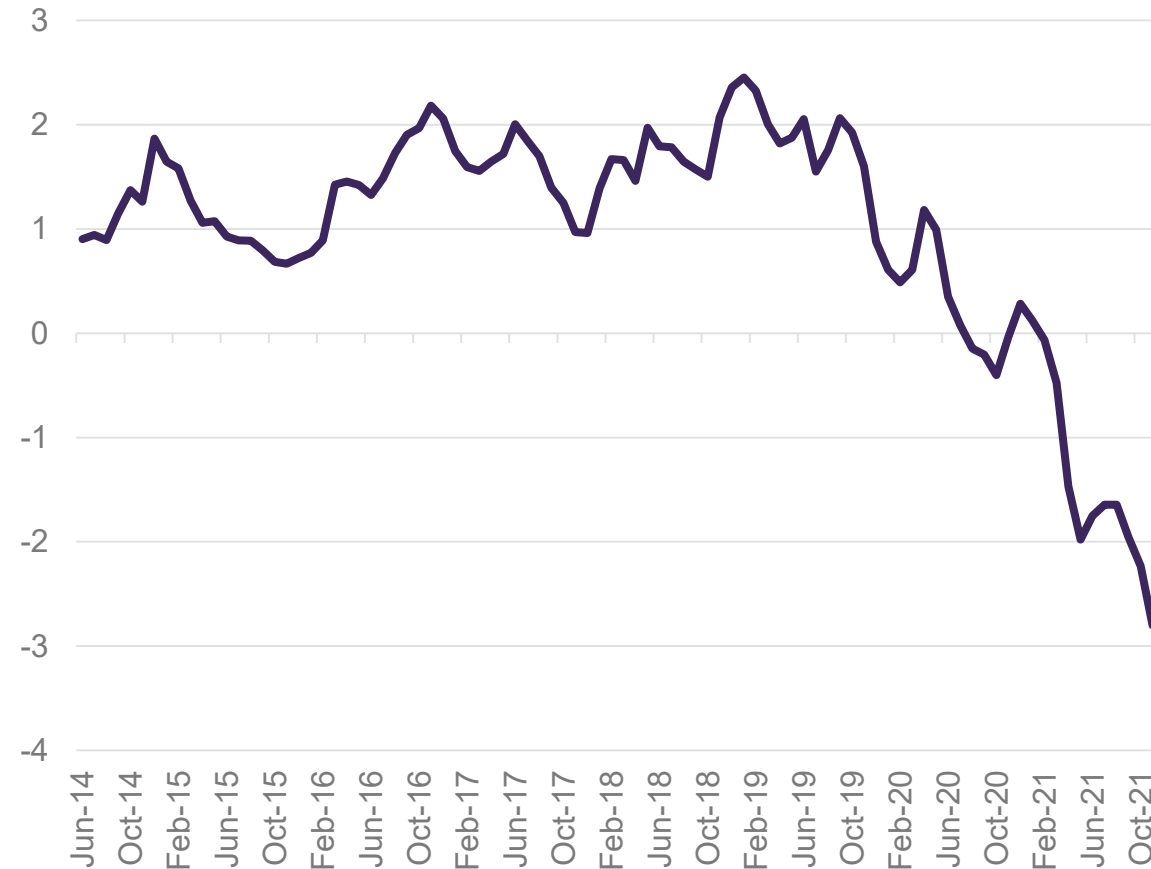
Source: Bloomberg, Fitch Solutions

- Emerging Markets will face several challenges over the coming months, which may weigh on investor appetite.
- Higher inflation will force central banks to maintain tight monetary policy, even at time when growth is slowing.
- Lower commodity prices will also weigh on growth.
- Rising interest rates by the Federal Reserve could lead to currency volatility for EMs.
- Pandemic fatigue and rising inflation could impact the result of several upcoming elections, which could result in a rise in political risk.

Low Carry Appeal For EMs, Slowing Output

With Inflation Running Hot, Real Rates Remain Negative

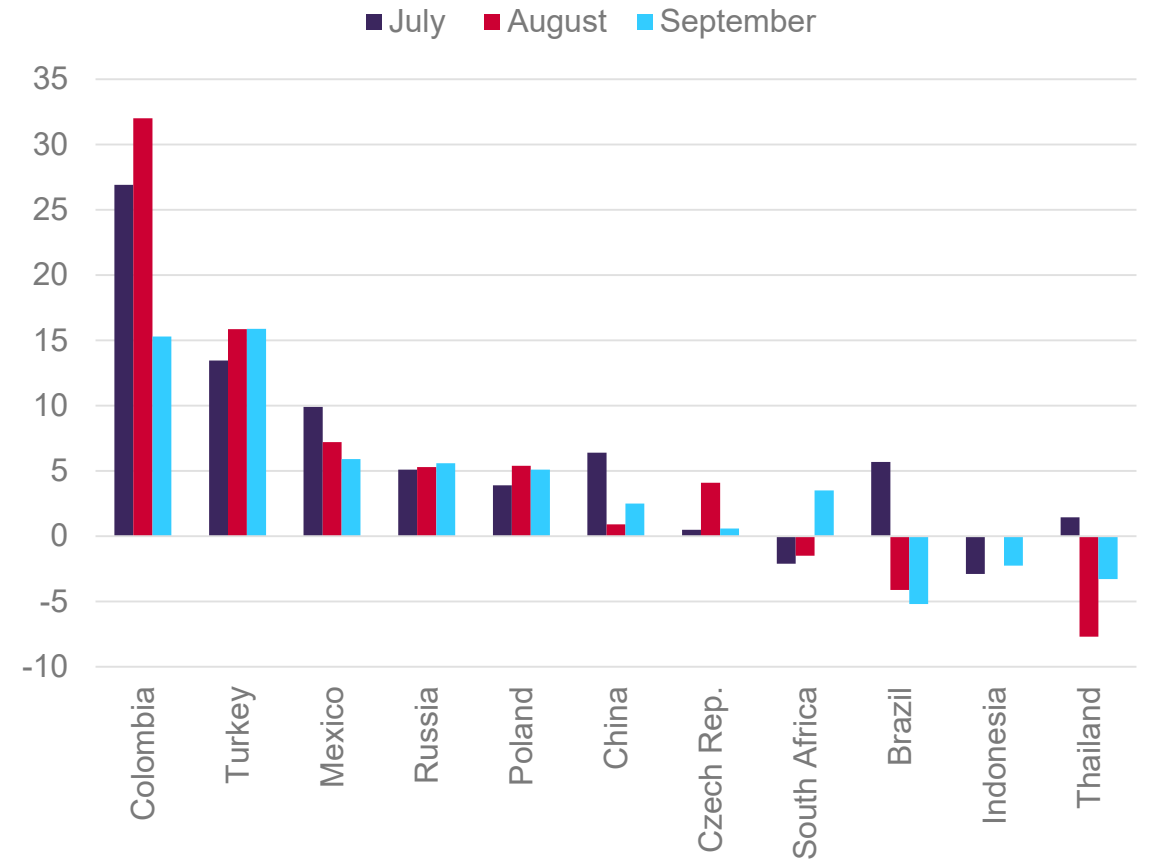
Major EMs Unweighted Average Real Interest Rate, %



Source: Bloomberg, Fitch Solutions

Activity Slowing Slightly In EMs Already

Retail Sales Volumes, % y-o-y

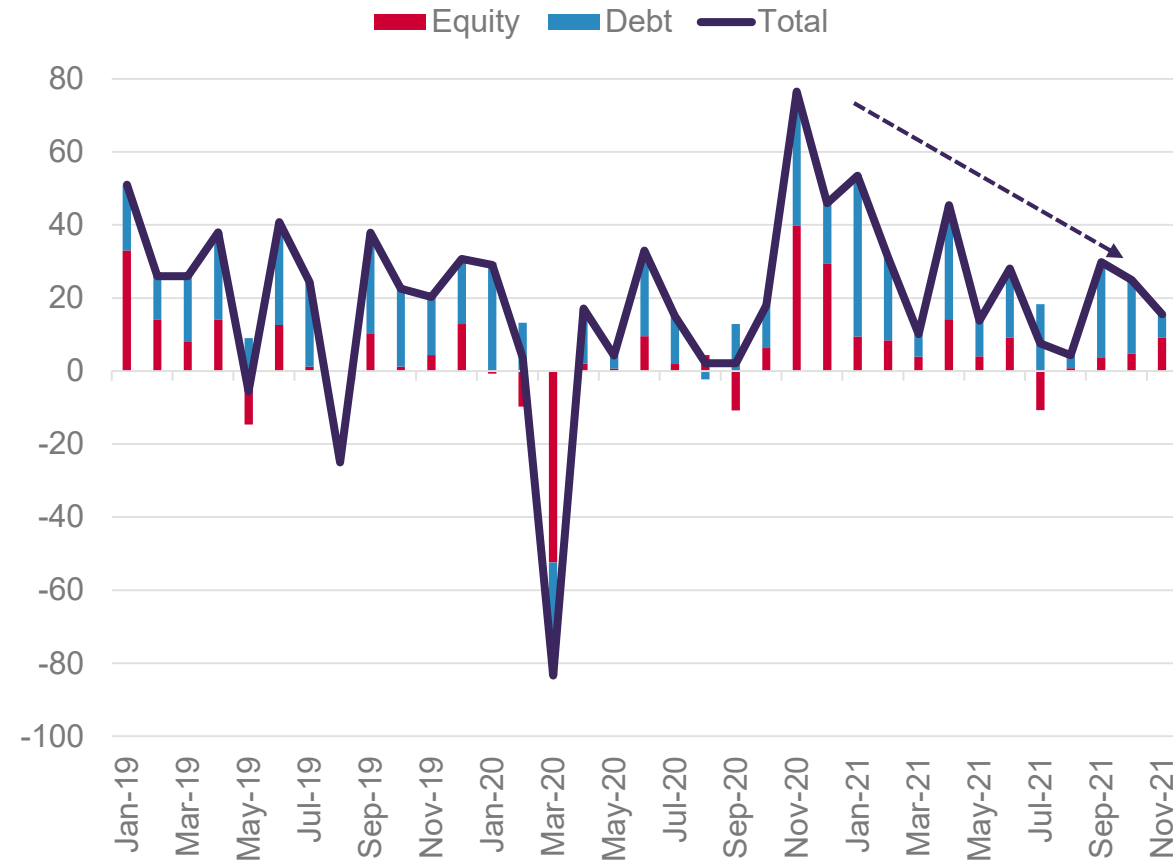


Source: Bloomberg, Fitch Solutions

Foreign Investment Into EMs Has Been On A Declining Path

Foreign Investors Seem Less Keen On EMs

Equity & Debt Flows To EMs, USDbn



Source: IIF, Fitch Solutions

Investors Shying Away From EM Bonds?

Market Cap Of JP Morgan EM Local Government Bond ETF, % y-o-y

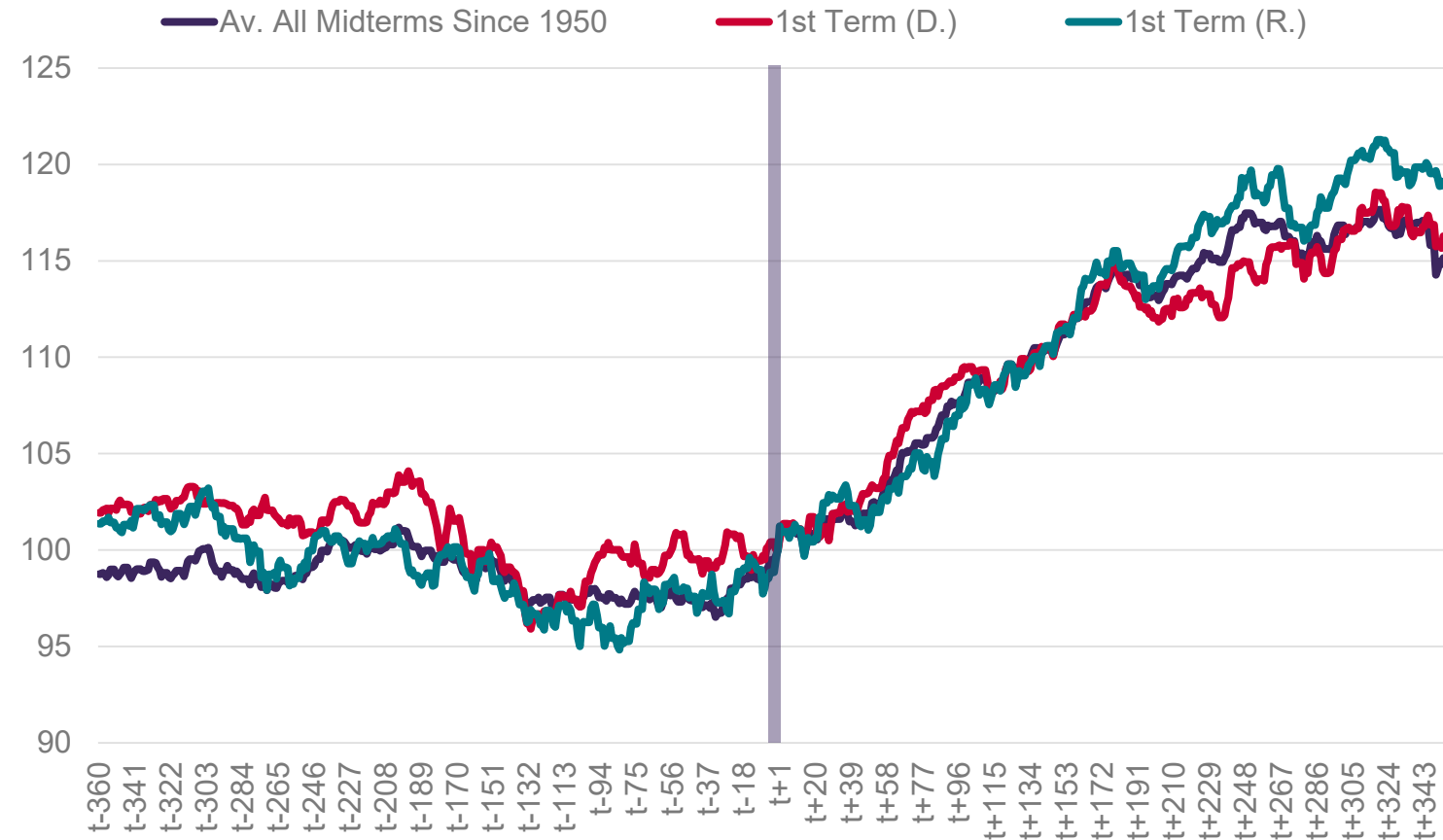


Source: Bloomberg, Fitch Solutions

Theme 7: Financial Markets Not A One-Way Bet In 2022

Equity Market Volatility Rises Ahead Of The Midterms

US – Historical Performance Of The S&P 500 360 Days Before & After Midterms, %*



D. = Democrat, R. = Republican president. *Midterm = 100. Source: Bloomberg, Fitch Solutions

- Financial markets will face a greater set of challenges as the economic cycle matures and new risks emerge.
- These include much higher uncertainty regarding the trajectory of monetary policy, rich valuations, slowing economic and earnings growth, as well as political risk emanating from the US midterm elections in November 2022.
- US equity markets were notably less volatile in 2021 than in recent years, so even a return to the pre-crisis level of volatility could come as a bit of a shock.
- We also expect the US dollar to remain on the front foot and for commodity prices to ease, which could weigh on emerging market currencies.

Theme 8: Rising Polarisation And Divergent Reform Momentum

Key Elections To Watch In 2022

Date	Country	Expected Outcome
Jan-22	Portugal	Incumbent victory
Mar-22	South Korea	Too close to call
April and June 2022	France	Weakened incumbent victory
Apr-22	Hungary	Weakened incumbent victory
May-22	Colombia	Opposition victory
May-22	Philippines	Victory of an 'illiberal populist' candidate.
May-22	Australia	Weakened incumbent victory
Aug-22	Kenya	Too close to call
Oct-22	Brazil	Opposition victory
Dec-22	US mid-terms	Loss of Democratic Party majority

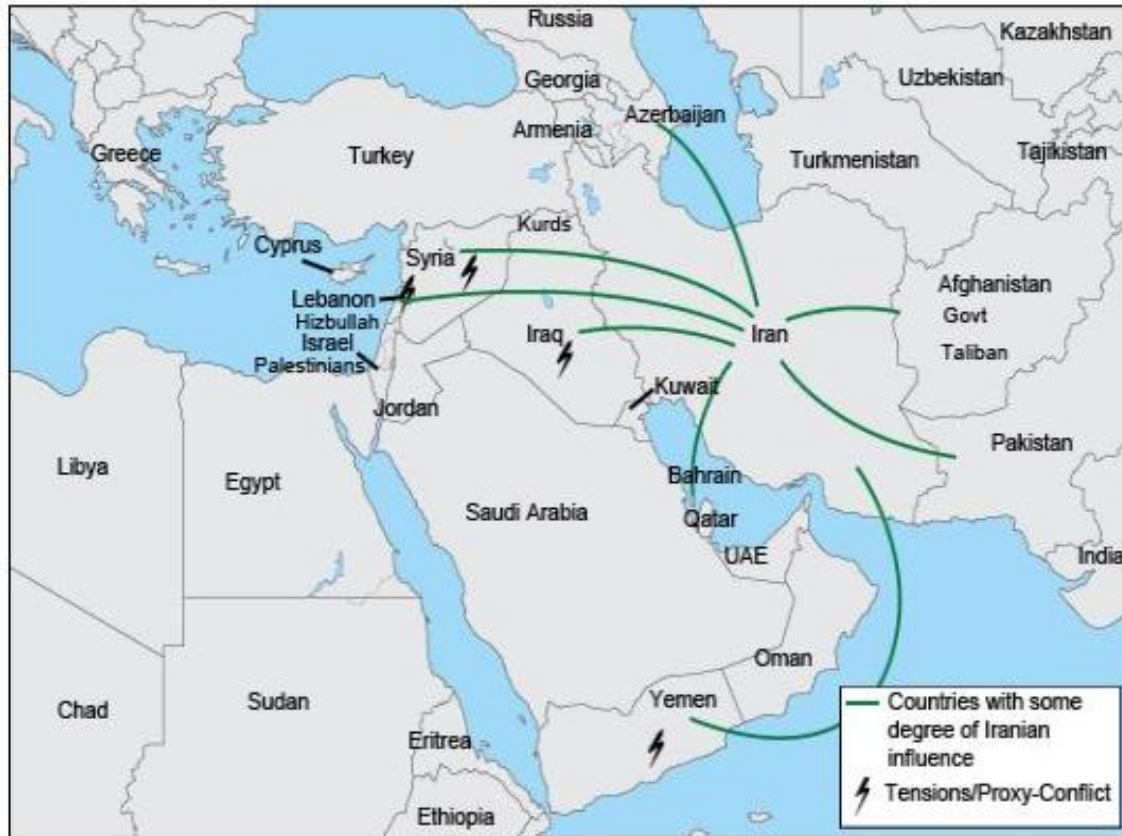
Source: Fitch Solutions

- In 2022, several elections will take place in a polarised political environment due to uneven economic recoveries and wealth inequality.
- This could strengthen anti-establishment sentiment in many markets, boosting support for new and/or fringe parties.
- Most incumbents will either lose or, at best, manage narrow victories. Leaders in EMs will face particularly difficult elections, with early polling showing strong support for leftist challengers in countries such as Colombia and Brazil.
- Lingering popular discontent and various upcoming contentious elections mean reform momentum across EMs will slow, particularly in Sub-Saharan Africa and Latin America.
- We also expect that several major DMs will face severe policy gridlock, particularly the US.

Theme 9: Old Opportunities And Risks In Geopolitics

Iran Deal Could Help Reduce Regional Tensions

Map Of MENA



Source: Fitch Solutions

Geopolitical Rivalry Will Remain In Play

Indo-Pacific Region – Geopolitical Alignments



Source: Fitch Solutions

Theme 10: Risks Will Remain Top Of Mind

Various Risks Remain In Play

Key Risks To Watch Out For



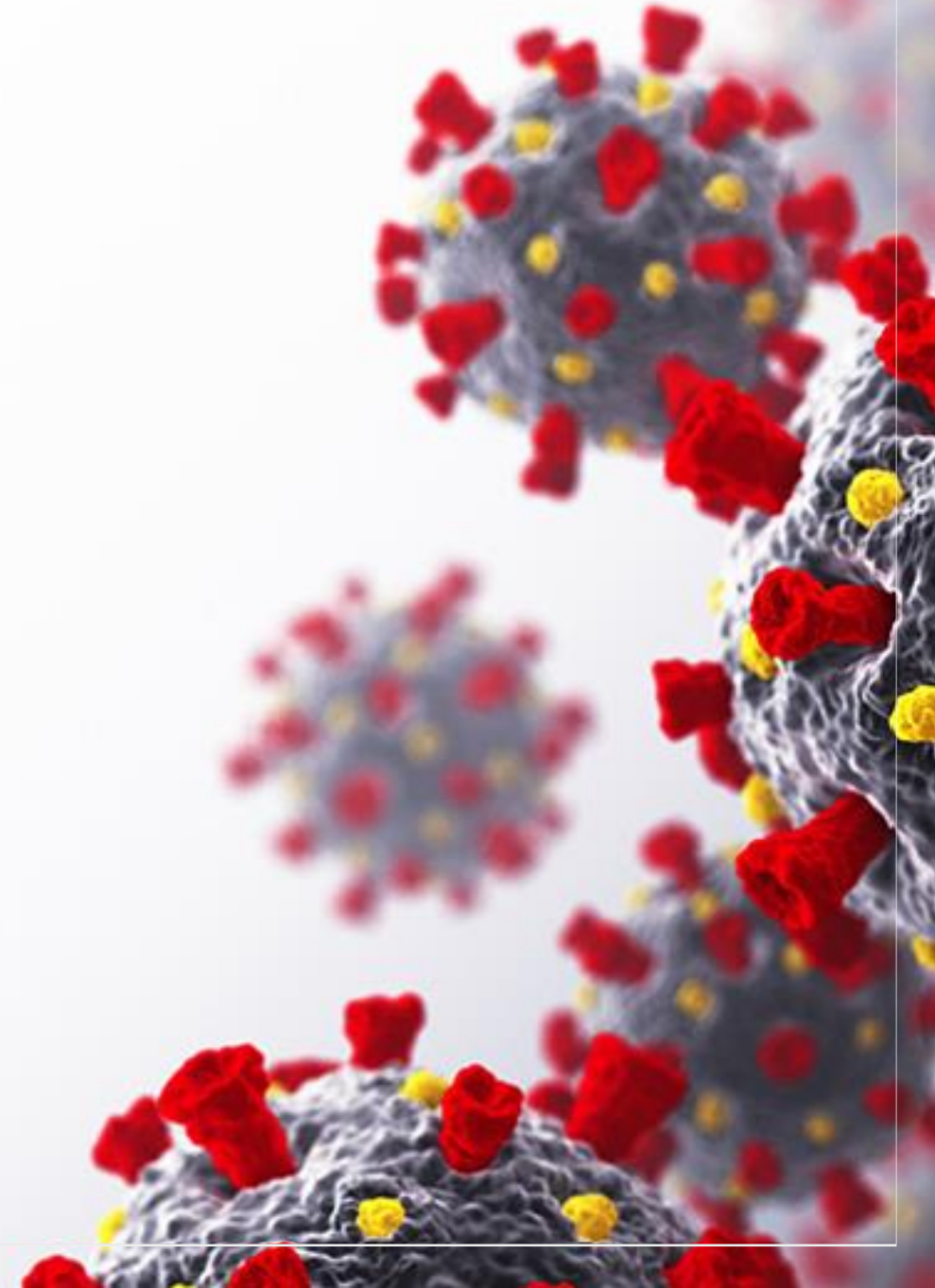
Source: Fitch Solutions

- **First**, credit stress from the property sector in China could spread to the wider economy and result in a sharper economic slowdown than we are currently anticipating. Combined with the potential for more Covid-19 outbreaks, the sector could even prompt a 'hard landing'.
- **Second**, there is a risk that, rather than easing as we expect, price pressures could remain strong for the duration of 2022. This could prompt a more aggressive tightening cycle, resulting in a significant re-pricing of markets, causing volatility and depressing growth as investors and consumers retrench, particularly for EMs.
- **Third**, we should not discount the risk of new Covid-19 variants, particularly as large sections of the global population remain unvaccinated.
- **Fourth**, geopolitical missteps between Russia and Ukraine, the US-Iran and US-China could result in a rise in tensions and greater risk aversion.

Connected Thinking in Challenging Times

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