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Global Economic Outlook – June 2022

The Return of Tight Monetary Policy

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The Return of Tight Monetary Policy

"Inflation is not going to fix itself. The Fed and Bank of England don't seem to have much choice now but to take interest rates above neutral, whatever the consequences for growth."

Brian Coulton, Chief Economist, Fitch Ratings

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Inflation Pressures Unrelenting

Global inflation pressures continue to intensify, with increasingly adverse implications for the growth outlook. Recent Covid-19-related lockdowns in China are adding to global manufacturing supply-chain pressures. Energy and food supply disruptions from the Russia-Ukraine war are having a swifter impact on European inflation than expected. Inflation pressures are also building in the services sector, particularly in the US and UK, where tight labour markets are boosting nominal wage growth. Inflation forecasts have been revised up widely, particularly for Europe in 2H22.

World Growth Prospects Deteriorate

Fitch Ratings' has cut its world GDP growth forecast for 2022 by 0.6pp since the March 2022 Global Economic Outlook (GEO) to 2.9%. The biggest revision is to China where we now expect growth to fall to 3.7% this year, down from 4.8% in March. We have lowered our forecasts for growth in the US by 0.6pp to 2.9% and the eurozone by 0.4pp to 2.6%. We have cut world growth in 2023 by 0.1pp to 2.7%. The lockdown in Shanghai will cause China's GDP to fall in sequential quarterly terms in 2Q22 and with the 'dynamic-zero' Covid-19 policy still in place, we do not expect there to be a swift bounce back. Eurozone consumers will experience a greater drag on real incomes from inflation, and German industry is being affected by supply-chain disruptions and the China slowdown. The US economy has near-term momentum, with consumer spending supported by strong growth in jobs and nominal wages. But growth is set to slow from mid-2023 to barely positive rates in quarterly terms due to aggressive monetary tightening.

Fed Policy Stance Will Become Restrictive

Inflation challenges have become so pronounced that central banks are being forced to respond, abandoning prior forward guidance. The risk of inflation becoming embedded as wage-price dynamics develop and price expectations rise is pronounced. Labour markets are very tight in the US and UK, where wage inflation is high and rising as workers resist real wage cuts amidst high job turnover. We now expect the Fed to raise interest rates to 3.0% by 4Q22 and to 3.5% by 1Q23, i.e. above its estimates of the neutral rate and hence to a 'restrictive' stance. We also now expect the Bank of England (BOE) to raise rates to 2% by 4Q22 and 2.5% by 1Q23. The pace of wage growth has also risen in the eurozone, though only to 2.8%. With near-term inflation much higher, we now expect the ECB to raise rates by 100bp this year followed by 50bp in 2023. We forecast the ECB main refinancing rate at 1.5% by 2Q23, close to ECB estimates of the neutral range.

EU Gas Rationing Risk Remains

The risk of a sudden stop in all flows of Russian natural gas to Germany and Italy has been avoided for now, but it remains high while the conflict continues. Exposures are so high that we doubt the eurozone would avoid a recession in such a scenario.

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Global Forecast Summary

(%)	Annual Average 2017-2021	2021	2022F	2023F	2024F
GDP Growth					
US	1.9	5.7	2.9	1.5	1.3
Eurozone	1.0	5.4	2.6	2.1	2.1
China	6.0	8.1	3.7	5.3	5.0
Japan	-0.2	1.7	2.0	1.8	1.1
UK	0.7	7.4	3.8	1.1	1.6
Developed [a]	1.3	5.0	2.8	1.7	1.6
Emerging [b]	4.3	7.3	3.1	4.3	4.4
Emerging ex-China	2.4	5.9	2.5	3.0	3.7
World [c]	2.4	5.8	2.9	2.7	2.7
Inflation (end of period)					
US	2.5	7.0	6.5	2.8	2.7
Eurozone	1.5	5.0	5.3	1.4	1.7
China	2.0	1.5	2.7	2.3	2.4
Japan	0.3	0.8	2.3	1.0	0.8
UK	2.1	5.4	9.2	2.6	2.4
Interest Rates (end of period)					
US	1.22	0.25	3.00	3.50	3.50
Eurozone	0.00	0.00	1.00	1.50	1.50
China [d]	3.15	2.95	2.70	2.70	2.70
Japan	-0.10	-0.10	-0.10	-0.10	-0.10
UK	0.39	0.25	2.00	2.50	2.50
US 10-year yield	1.91	1.51	3.25	3.75	3.75
Exchange Rates and Oil					
Oil (USD/barrel)	60.9	70.6	105.0	85.0	65.0
USDJPY (end-period)	109.6	114.2	130.0	120.0	120.0
USDEUR (end-period)	0.87	0.88	0.95	0.95	0.95
GBPUSD (end-period)	1.31	1.34	1.25	1.25	1.25
USDCNY (end-period)	6.73	6.37	6.70	6.90	7.00

[a] US, Japan, France, Germany, Italy, Spain, UK, Canada, Australia and Switzerland
[b] Brazil, Russia, India, China, South Africa, Korea, Mexico, Indonesia, Poland and Turkey
[c] 'Fitch 20' countries weighted by nominal GDP in US dollars at market exchange rates (three-year average)
[d] One-year medium-term lending facility
Source: Fitch Ratings

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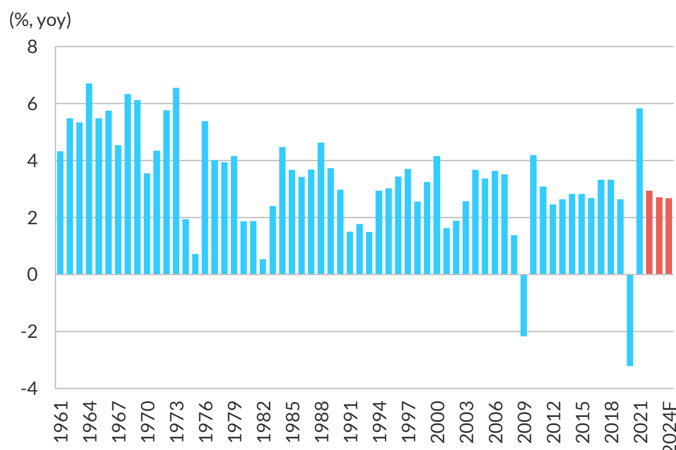
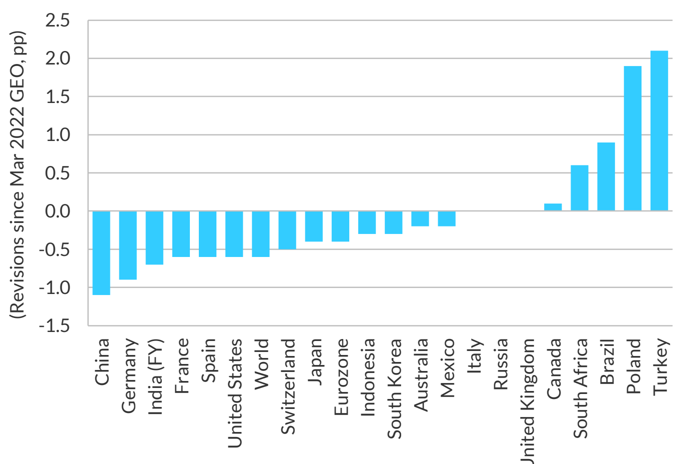
World GDP Growth



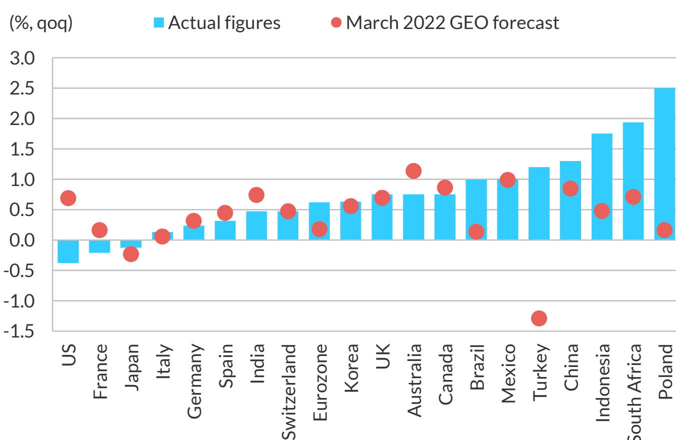
Source: Fitch Ratings, World Bank, Haver Analytics

Revisions to 2022 Annual GDP Forecasts



Source: Fitch Ratings

GDP 1Q22 Outturns vs Forecasts



Source: Fitch Ratings, national statistical offices, Haver Analytics

Forecast Highlights

We now forecast world GDP to grow by 2.9% in 2022, revised down from 3.5% in March. The revisions reflect weaker growth prospects in both China and in the major advanced economies and they are quite widespread, with 12 of the 20 countries covered in the GEO undergoing forecast downgrades.

We expect China to grow by just 3.7% this year after the severe lockdown in Shanghai in April and May. This forecast is 1.1pp lower than we expected in the March GEO and is also 0.6pp lower than the forecast update we issued in early May, reflecting the subsequent release of very weak April macroeconomic data. China's slowdown is being felt elsewhere in Asia and we have lowered our 2022 growth forecasts for Japan and Korea by 0.4pp and 0.3pp, respectively.

We have lowered US growth for 2022 to 2.9% from 3.5% in March, but this is primarily a reflection of an unexpected GDP decline in 1Q22. This arithmetically reduces the annual average, but the economy continues to show robust momentum as household incomes expand with employment and wage growth and reopening dynamics continue in parts of the services sector. We expect sequential quarterly GDP growth to be solid for the rest of 2022.

We have revised down eurozone 2022 growth to 2.6% from 3.0% in March. This is despite a surprisingly strong expansion of 0.6% qoq in 1Q22 – substantially above our March forecast of 0.2% – which partly reflected volatility in some smaller eurozone economies. The revision reflects the impact of higher inflation on real income growth, supply-chain disruptions and slower growth in China. The revised forecast would still be above eurozone long-term growth potential, reflecting ongoing reopening in the services sector – including the return of international tourism – and fiscal support from Next GenerationEU (NGEU) fund disbursements.

Germany has undergone the biggest 2022 forecast revision among the large eurozone economies at -0.9pp. This reflects its higher exposure to energy and supply-chain disruptions and to China. But we have cut France's forecast 0.6pp following a surprise fall in GDP in 1Q22. We have also lowered Spain's forecast by 0.6pp following a weaker-than-expected 1Q22 expansion and a jump in inflation. Italy's GDP forecast is unchanged at 2.7%.

Our 2022 growth forecast for emerging markets (EM) excluding China is unchanged at 2.5%. We have raised our expectations for Brazil, Turkey, South Africa and Poland following much stronger-than-expected 1Q22 growth. But this is offset by weaker growth in India, Indonesia and Mexico. We continue to see an 8% GDP decline in Russia this year: while domestic spending adjustment looks less abrupt, energy export volumes are falling faster than we had assumed.

We expect global growth to slow further to 2.7% in 2023. This is despite an anticipated recovery in China's growth rate to 5.3%, based on the assumption that lockdown and other restrictions become less severe next year. The world growth slowdown next year partly reflects the fading of post-pandemic reopening effects but, more significantly, the delayed impact of higher inflation and monetary policy tightening on demand and activity.

Specifically, we expect there to be a sharp slowdown in US growth from the middle of 2023 in response to anticipated rapid Fed rate

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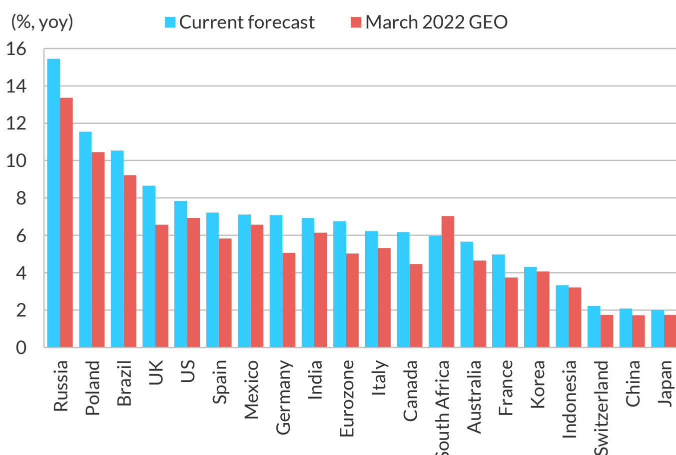

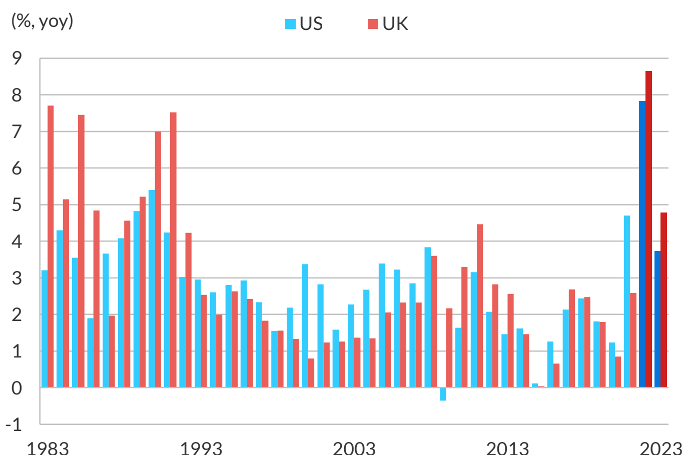

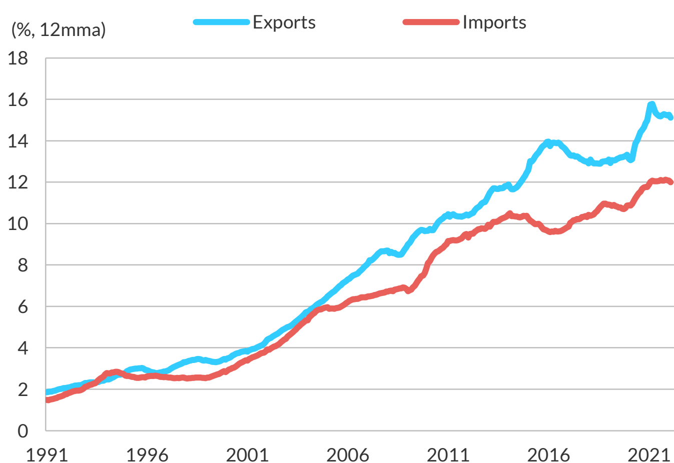

rises through the rest of this year. The housing market is already showing signs of responding to the rise in long-term interest rates and stepped-up monetary tightening will progressively take a toll on interest-rate-sensitive spending. We have lowered our 2023 annual US GDP forecast to 1.5% (from 1.6%) but this annual average figure obscures very weak quarterly growth forecasts of just 0.1% per quarter from 2Q23 through 4Q23. These very low rates would leave the US expansion perilously close to the risk of technical recession – i.e. two consecutive quarters of economic contraction. The pace of growth falls even further on an annual basis to 1.3% in 2024. Our forecasts for 2023 and 2024 are below consensus.

Our forecast of a sharp fall in UK growth – from 3.8% in 2022 to 1.1% in 2023 – also reflects the lagged effect of higher inflation and interest rates on demand. The UK is experiencing one of the largest inflation shocks among the advanced economies, but strong wage and employment growth, savings buffers accumulated through the pandemic and fiscal support for households will help to maintain positive consumer spending momentum in the near term. But with inflation now expected to stay close to double digits until the end of 2022 and the BOE set to raise rates to restrictive levels, we expect there to be a sharp slowdown in growth next year. In the eurozone, there will also be less monetary policy support to growth as the ECB moves rates back towards neutral.

We have again revised up our inflation forecasts for 2022 and 2023: we have increased our CPI inflation forecasts on average across the 20 countries in the GEO by around 1.3pp for both years (annual averages) since March and have raised our forecasts in all but one of the countries. Inflation forecast for the UK, Germany and the eurozone have seen larger increases in 2022. This partly reflects greater exposure to the rise in European natural gas prices, but the outlook for core inflation has also increased, particularly in the UK. We have also raised Turkey's 2022 annual average inflation rate by 8pp to 64%.

We now expect US CPI inflation to average 7.8% % in 2022 (revised up from 6.9% in the March GEO), 8.7% in the UK (from 6.6%) and 6.7% in the eurozone (5.0%). We expect that the rate of inflation will fall in 2023 as oil prices are assumed to decline to USD85 a barrel (from an annual average of USD105/barrel this year) and core goods prices stabilise as manufacturing supply chain pressures ease. However, we still expect US and UK inflation annual average CPI inflation rates to remain well above target in 2023 at 3.7% and 4.8%, respectively on average, while eurozone inflation is expected to average 2.2% next year, well above the pre-pandemic average of 1.7%. These annual average inflation forecasts for 2023 are higher than the end-year yoy forecasts shown in the tables, primarily reflecting the assumed monthly path for oil prices, which is highly uncertain.

We have made major upward revisions in this GEO to interest rate forecasts, with 18 of 20 countries predicted to have tighter monetary policy settings than we anticipated previously. Our end-2022 Fed Funds and ECB MRO rate forecasts have been increased by 100bp since the March GEO and our BOE forecasts has been lifted by 75bp. We have revised up out interest rate forecasts for end-2022 for Australia, Canada, India, Mexico and Poland by more than 100bp.

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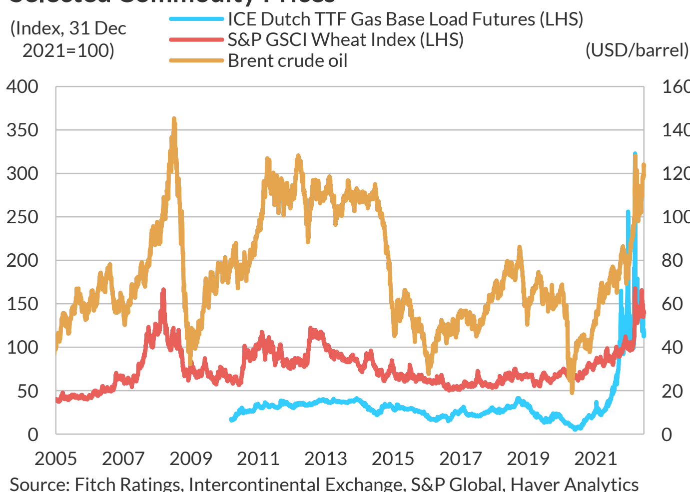
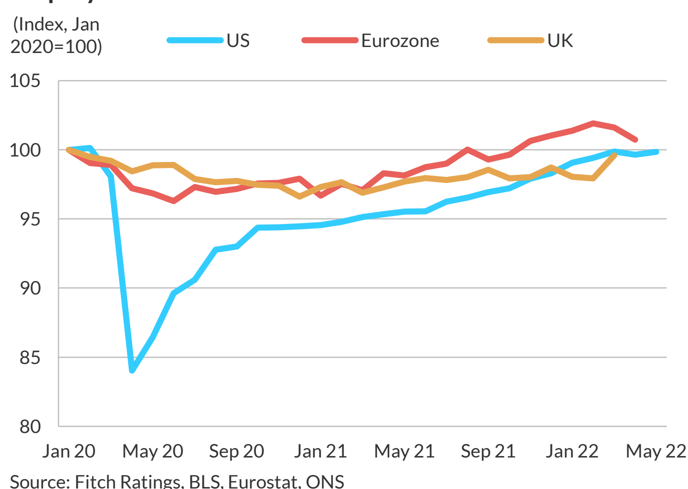
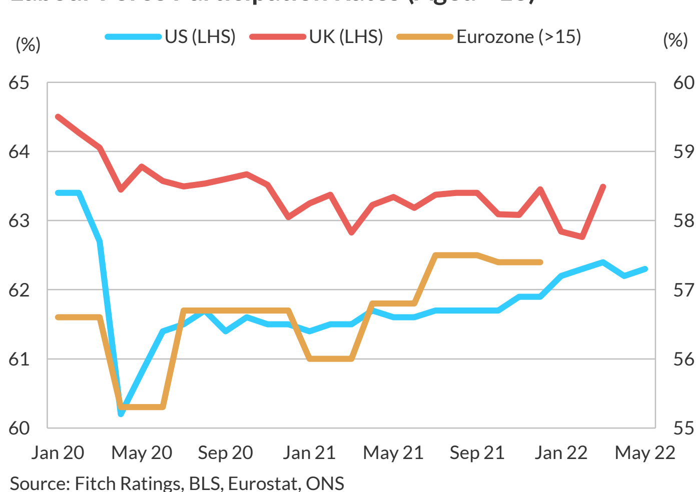


Source: Fitch Ratings, Intercontinental Exchange, S&P Global, Haver Analytics



Source: Fitch Ratings, BLS, Eurostat, ONS



Source: Fitch Ratings, BLS, Eurostat, ONS

We have also raised our end-2023 interest rate forecasts, but typically by a smaller margin. The forecast revisions incorporate more front-loading of rises in 2022, as well as higher terminal rates. We now expect the Fed, ECB and BOE to undertake roughly one- to two-year interest rate-raising cycles, compared to our earlier forecasts of much more protracted normalisation of interest rates. Nevertheless, we don't believe the Fed or BOE will be in a position to declare 'victory' in bringing core inflation back to target quickly and see rates remaining in restrictive territory through 2024.

Shanghai Shutdowns and the Supply Chain

The Shanghai shutdown is the main driver of our revision to China's growth forecast and will have major adverse consequences for global growth, but in the current inflationary environment, the impact on global manufacturing supply chains is a key focus. China is the world's largest goods exporter with gross merchandise exports of USD3,380 billion in 2021, accounting for 15% of global exports. China's huge net contribution to global goods supply is reflected in its USD697 billion trade surplus in 2021, the main counterpart to the USD1,082 billion trade deficit in the US.

These numbers underline the impact of any interruption to China's trade flows on global manufacturing supply chains. China's exports fell by more than 5% in April as Shanghai port throughput collapsed. The impact was swiftly seen elsewhere, including in Japan where automakers struggled to source component parts. While China's exports rebounded again in May, the risk of further lockdowns remains high while the dynamic-zero Covid-19 approach remains in place. These interruptions threaten to prolong and intensify upward pressures on core consumer goods prices.

There was little evidence that supply-chain pressures had started to ease significantly prior to the Shanghai lockdown, and the latest data suggest these bottlenecks may have deteriorated since March. Shipping freight costs have remained elevated in recent months, the ISM survey of US firms showed a lengthening of supplier delivery times in April – with little relief in May – and industry sources point to a further lengthening in semiconductor lead times in April. Meanwhile shipping freight times for US-China and Europe-China routes have remained very slow, at around 100 days. Our inflation forecasts continue to factor in an easing in goods bottlenecks over time as consumers switch spending towards services, fiscal support for consumers in the US fades and increased investment in challenged sectors starts to boost capacity. However, we now expect any major improvements to be delayed until late-2022.

Russia-Ukraine War Impact

After three months of the Russia-Ukraine war and related sanctions, the economic impact on the rest of the world is visible in supply-chain disruptions, falling consumer confidence, higher commodity prices and inflation. Germany's industrial production and orders fell sharply in March and there were reports of German autos manufacturers struggling to source parts previously imported from Ukraine. German industrial production increased in April but only marginally and interruptions to demand have dampened orders. Consumer confidence indicators have also fallen sharply in the largest eurozone countries in recent months and recent readings in Germany have been weaker than those at the nadir of the pandemic in 2Q20.

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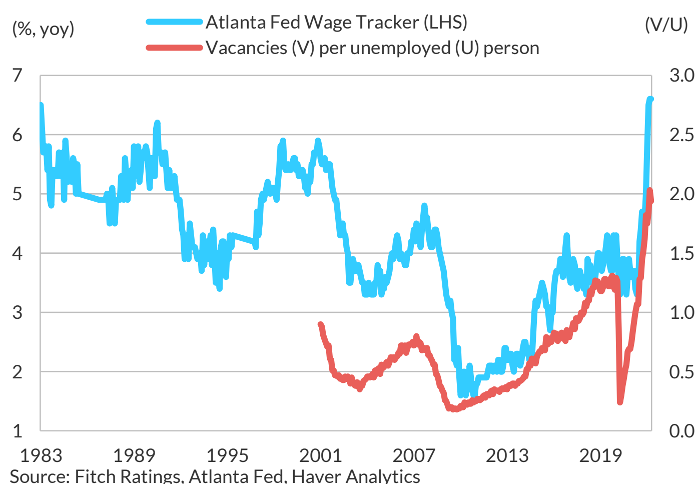
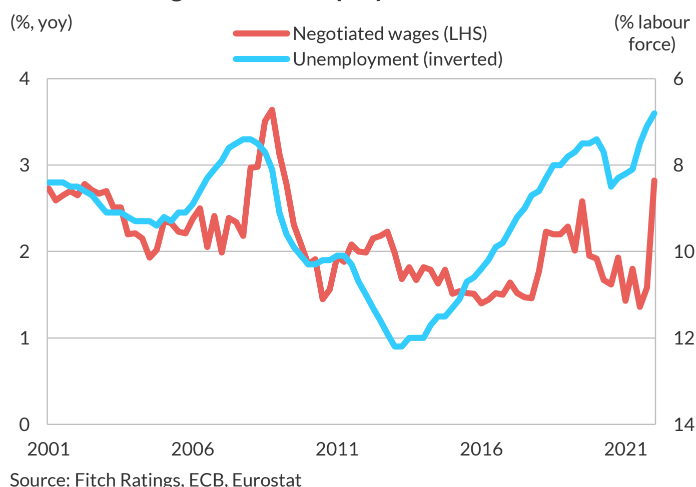
US Wage Growth and Vacancies/Unemployed



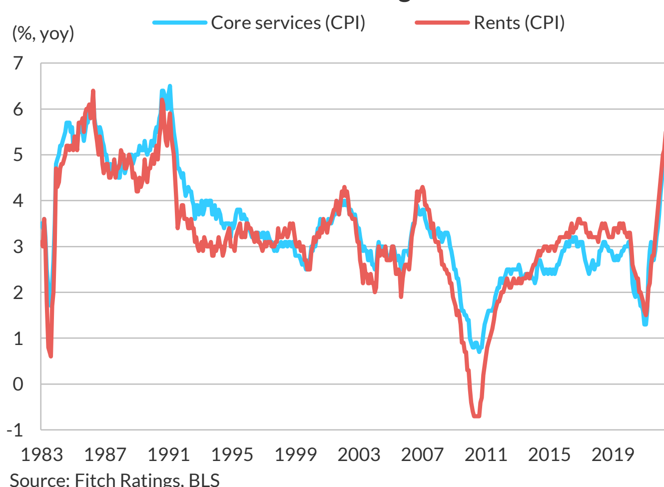
Source: Fitch Ratings, Atlanta Fed, Haver Analytics

Eurozone Wages and Unemployment



Source: Fitch Ratings, ECB, Eurostat

US Core Services CPI and Housing Rents



Source: Fitch Ratings, BLS

The most striking impact has been on commodity prices, inflation, and inflation expectations, commensurate with a potentially huge and lasting adverse supply shock. European wholesale gas prices had already risen sharply in early 2022 as fears of a Russian invasion increased, and they remain high. Russia's demand for payment in roubles for pipeline imports has raised fears of a sudden stop in gas supplies to Germany and Italy. Oil prices have also remained high, with Brent trading around USD120/barrel in recent days. Increasing numbers of buyers have been boycotting Russian imports. The EU recently announced a ban on seaborne Russian oil imports and while ultimately this may just lead to a redirection of global oil flows – with more Russian exports heading to Asia – infrastructure and other logistical constraints could cause a substantial loss of Russian supply. We have revised up our oil price assumptions by USD5/barrel for 2022 and 2023. Food prices have also been affected, with wheat prices 44% higher since December 2021 and the UN food price index up by 18%.

The impact on eurozone CPI inflation has been swifter than anticipated, with the food and energy components jumping recently and in combination accounting for more than 60% of headline CPI inflation in recent months. This rapid pass-through may be related to the sharp rise in near-term eurozone inflation expectations revealed in various surveys. This rise in expectations could also reflect the ongoing risk of a much more severe supply shock in the event of a sudden and total halt in Russian gas supplies to Europe. This risk has been avoided so far, but it remains elevated while the conflict continues. Gas rationing to industrial users would be likely in such a scenario and it would be hard, under such circumstances, to see the eurozone avoiding a recession in late-2022/early 2023 given the scale of exposures, particularly in Germany.

Tight Labour Markets and Wage Pressures

Labour markets have remained a bright spot as the recovery has been buffeted by shocks. Employment growth in the US and Europe has remained strong in 2022 and employment now slightly exceeds pre-pandemic (January 2020) levels in the eurozone and has almost fully recovered in the US. The US job recovery has been faster than we were expecting one year ago, taking around two years from pandemic lows rather than two and a half years. Unemployment rates have also fallen more quickly than expected and are now well below pre-pandemic rates in the eurozone and UK. Strong growth in job vacancies is further evidence of robust labour demand.

The recent resilience of employment growth partly reflects the ongoing re-opening of services sector activities after the easing of pandemic restrictions in early 2022. The leisure and transport (L&T) sectors most exposed to disruption from social distancing are typically labour-intensive and hence the recovery here is job-rich. L&T jobs in the US have grown by 3.5% year to date compared to a 1.8% expansion in private-sector jobs. With L&T employment still 2.4% below pre-pandemic levels, it looks like this dynamic has further to run. This is supported by the recent strength in PMI services balances in the US and Europe and the swift expansion in the L&T sector shown in UK monthly GDP data for March and April. The re-opening of international tourism is clearly boosting labour demand in Italy, Spain and France.

However, the employment recovery has been accompanied by rising and significant imbalances between labour demand and

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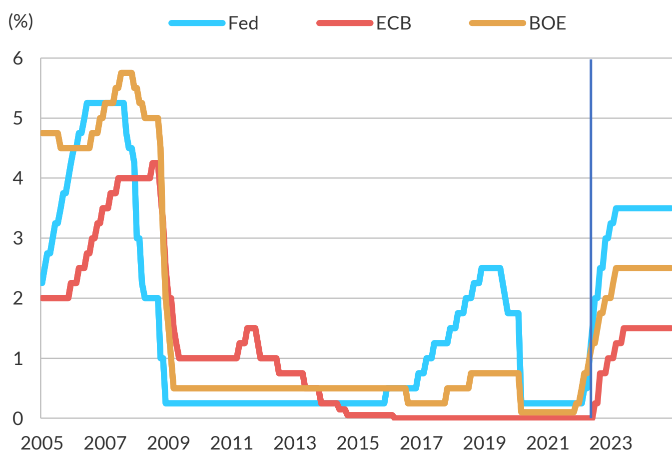
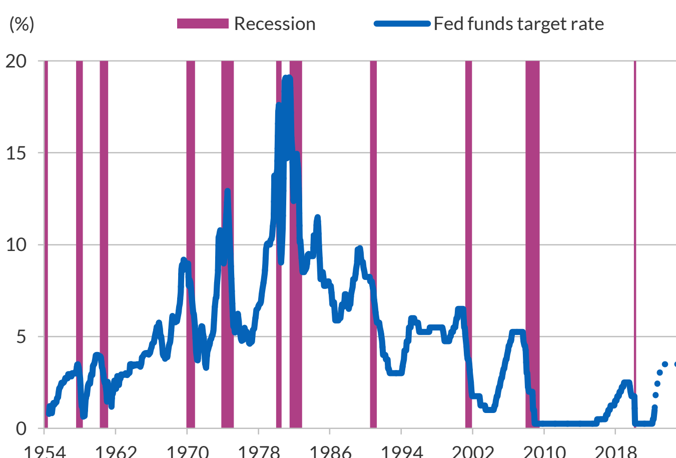
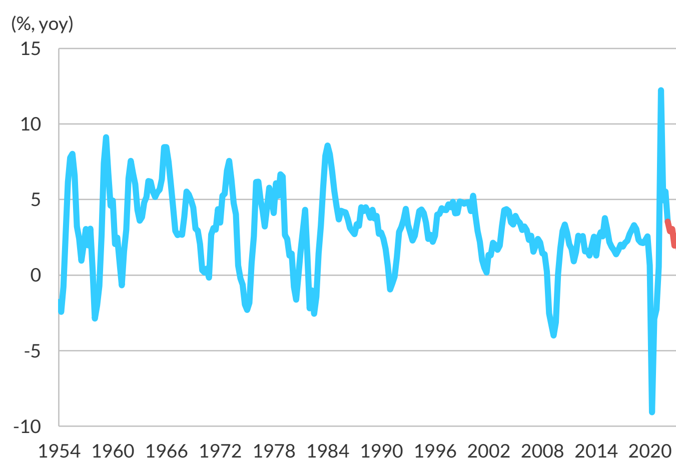


Source: Fitch Ratings, Fed, ECB, BoE, Haver Analytics



Source: Fitch Ratings, Fed, NBER, Haver Analytics



Source: Fitch Ratings, BEA, Haver Analytics

supply, particularly in the US and UK. This is evident in the fall in unemployment rates, a surge in the ratio of vacancies to unemployment, and business survey responses to questions about staff shortages and wage inflation. On the basis of long-term historical patterns, it has been surprising to see such clear evidence of widespread labour shortages when employment still remains slightly below pre-pandemic levels and employment-to-population ratios are still very depressed.

Various factors are behind this, including a sustained decline in labour-force participation rates in the US and UK, driven by older individuals. The US labour force has not grown since before the pandemic despite an expanding adult population, while the UK labour force is around 1% smaller than in January 2020. Another factor has been a sharp increase in job turnover, partly related to a rising share of workers voluntarily quitting their jobs. It may turn out that these trends prove to be temporary, pandemic-related shifts, but the surge in vacancies, accompanied by a very slow labour-supply response is putting upward pressure on wages. Job vacancies (openings) in the US have surged to 11 million and are now double the number of unemployed. Vacancies in the UK recently exceeded the number of unemployed, for the first time on record.

The leap in the vacancy-to-unemployment (V/U) ratio has been accompanied by a sharp rise in wage inflation in the US and UK to historical highs. The Atlanta Fed US wage tracker (weighted) jumped to 6.6% yoy in May, the highest since the data started in 1997; the seasonally adjusted Employment Cost Index rose by an annualised 5.8% qoq in 1Q22; and average hourly earnings rose by 5.4% yoy in the three months to May. In the UK, average earnings (including bonuses) grew by 7% yoy in the three months to March and by 9.9% yoy in March itself. These nominal wage growth numbers are well ahead of what might be viewed as a long-term sustainable level consistent with the 2% inflation target and real wages growing in line with trend labour productivity growth (which is around 1.5% in the US). Moreover, rising V/U ratios point to further wage acceleration. In the eurozone, wages have also grown alongside a sharp rise in vacancies and a fall in the unemployment rate. However, labour market imbalances look less intense – partly reflecting a full recovery in the labour force participation rates – and wage inflation is still quite low at under 3%.

Restrictive Monetary Policy to Return

High and rising nominal wage growth in the US and UK raises the prospect of the inflation shock becoming self-sustaining. In the current climate it is clear that firms are passing on higher costs for materials, energy and other inputs to consumers and they probably would do the same in response to a rise in labour costs. National accounts data suggest labour costs make up about 30% of total costs for US firms and the wage bill absorbs about two-thirds of value added, illustrating the potential for a wage-price spiral to start to develop. Rising services inflation in the US suggests inflation is becoming embedded. A sharp downturn in real consumer spending caused by a fall in real incomes could change the willingness of firms to pass on higher costs to consumers. But with robust job and wage growth, the near-term outlook for household real incomes and consumer spending still looks solid. Put another way, it does not look like the rise in inflation will 'automatically' deliver a slump in real consumption that would dampen inflationary pressures.

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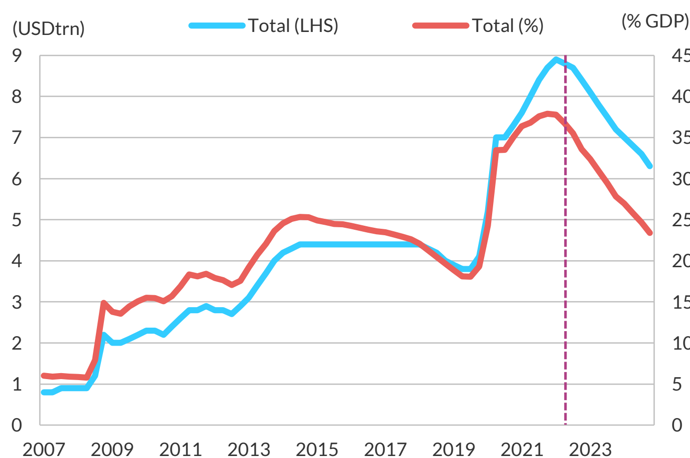
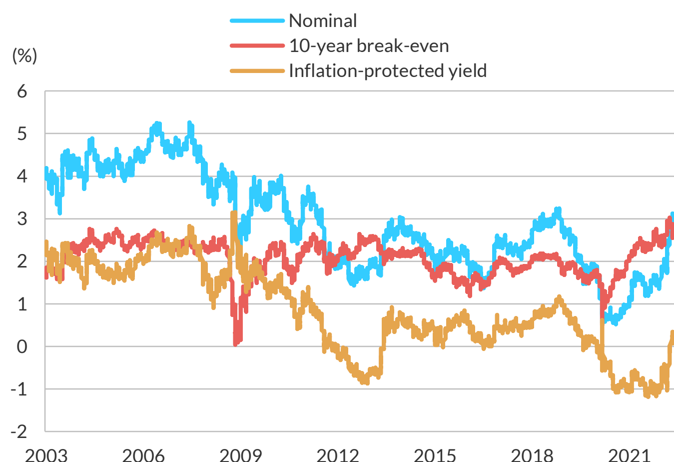
Fed Balance Sheet Outlook



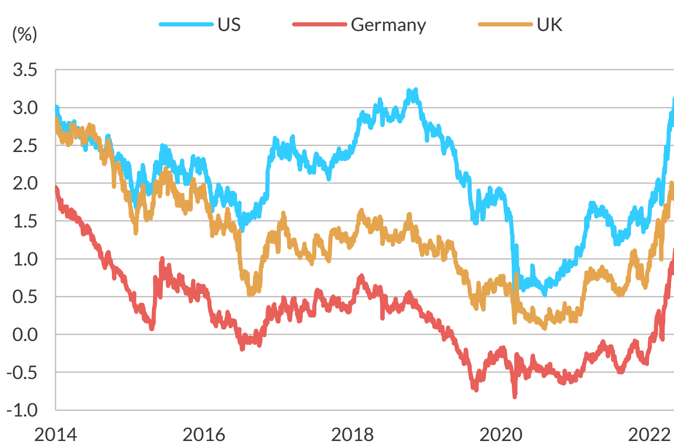
Source: Fitch Ratings, Fed

US 10Y Bond Yields



Source: Fitch Ratings, Federal Reserve Board, Haver Analytics

Global 10Y Government Bond Yields



Source: Fitch Ratings, Fed, Deutsche Bundesbank, TPI, Haver Analytics

Against this backdrop, the pressure is building for the Fed and BOE to raise interest rates quickly to levels that will actually start restricting domestic demand growth – i.e. to above the so-called 'neutral' rate which neither boosts nor constrains the economy. We now believe this is where the Fed is headed and expect 50bp increases at each of the next four meetings in June, July, September and November and then two more in 1Q23. This would take the Fed Funds rate to 3.5% by 1Q23, well above the long-run neutral rate of 2.4% indicated in the Fed's Summary of Economic Projections. In the UK, we now expect the BOE to raise rates to 2% by end-2022 and to 2.5% by 4Q23. Again, this would be above the estimates of the 'neutral' rate in the range of 1%-2% as quoted by BOE officials.

Core inflation and wage growth is significantly lower in the eurozone than in the US. But with inflation at record highs and core price pressures now adding to surging energy and food prices, the ECB has also announced plans to begin normalising key policy rates. Following the end of its Asset Purchase Programme and an expected 25bp hike to the MRO in July as choreographed, we expect the ECB to follow through with a stronger 50bp increase in September. Thereafter we expect rate rises to proceed more gradually given the eurozone's fragile growth outlook and lower core inflation. We anticipate another 25bp uplift in December, followed by two more in 1H23 to take the MRO to 1.5%. This would leave the deposit rate at the lower bound of the 1%-2% estimate of the neutral rate cited by some ECB officials. Since we expect energy prices to act as a drag on annual inflation in 2023, rates may not need to rise as far to exert the required downward pressure on prices.

Implications for Growth

It has been a long time since the world economy has had to live with restrictive US monetary policy settings. The Fed policy normalisation episode under Janet Yellen in 2017 and 2018 raised rates to only 2.5%, where they remained for only eight months before they were cut again. The last time US interest rates were above neutral was in 2006, although at 5%, they were much higher than we are expecting. The US economy currently looks a lot more resilient to rate rises than it was then, given the health of the banking sector, much lower household debt and debt service-to-income ratios, and stronger household financial balances buttressed by savings accumulated in the pandemic. The share of fixed-rate mortgage debt is also much higher now and it is very hard to argue there has been massive over-investment in housing.

Nevertheless, history provides some sobering lessons. Nearly all US recessions in the post-war period – as defined by the National Bureau of Economic Research – were predated by a sharp rise in the Fed Funds rate. Overall non-financial sector debt-to-GDP (including households, corporates and the government) is significantly higher today than in 2006. And an unknown factor this time is how quantitative tightening may influence financial markets, asset prices and risk appetite after years of easy liquidity. The Fed's balance sheet is expected to fall by nearly 15% of GDP by end-2024. This underscores the likelihood that US long-term bond yields will also rise further as policy rates adjust. The rise in US mortgage rates has already had an impact on housing demand. Global bond yields will also see upward pressure. The large rise in US dollar-denominated debt issued outside the US over the past decade could also increase the global impact of tight US monetary policy.

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United States

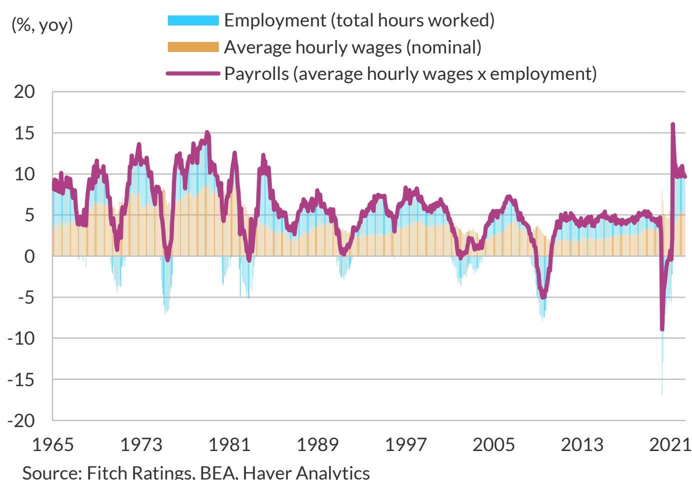
The US economy continues to expand robustly despite the steep rise in inflation. Strong employment and nominal wage growth are supporting the near-term outlook for consumption. We expect GDP to rise by 2.9% in 2022 – revised down by 0.6pp since the previous GEO on a weak 1Q22 outturn – but well above trend. However, unrelenting inflation pressures now look likely to force the Fed to raise interest rates to 3% by the end of this year and it is likely that growth will slow sharply from the middle of 2023 as a result.

GDP unexpectedly fell by 0.4% qoq (not annualised) in 1Q22 – compared to forecast growth of 0.7% in the March GEO – but this primarily reflected volatility in net trade and inventories related to global supply-chain disruptions. Consumer spending, PMI and employment data all point to GDP growth resuming at a robust pace in 2Q22. The rise in CPI inflation has hit consumer confidence, but rapid employment and nominal wage growth – both up by around 5% in yoy terms in April – are boosting aggregate household incomes. Business investment also has strong momentum and we expect sequential GDP growth to remain solid for the next six months.

However, inflationary pressures remain intense. Headline CPI inflation rose again to 8.6% yoy in May as services inflation continued to rise and food price inflation jumped to 10.1%, the highest rate since the early 1980s. While car prices stabilised in April, they rose again in May and the lockdown in China looks likely to impart renewed pressure on core goods prices in coming months. We have revised up our end-2022 CPI inflation forecast to 6.5% yoy (from 4.5% in the March GEO) and our 2022 and 2023 annual average inflation forecasts have been raised to 7.8% and 3.7%, respectively, (from 6.9% and 2.7% in the previous GEO).

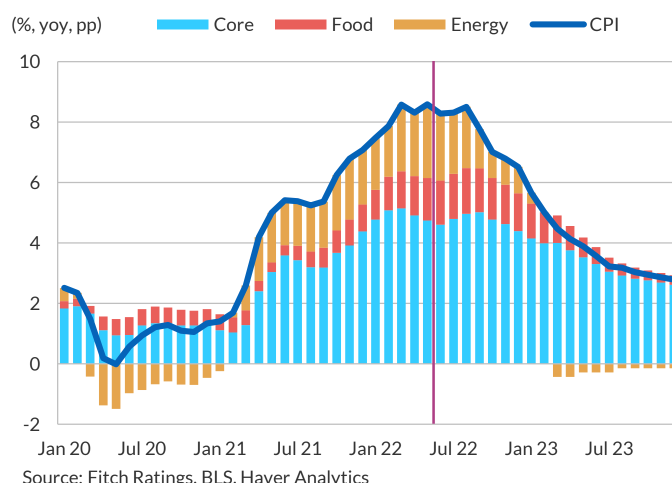
Tight labour market conditions are putting upward pressure on nominal wage inflation, which reached 6.6% yoy on the Atlanta Fed measure in May. The risk of wage-price dynamics gaining momentum is high. Against this backdrop we believe that the Fed will decide that interest rates need to be raised to restrictive levels – i.e. above their estimates of the 'neutral' rate – quickly. We now envisage the Fed raising rates by 50bp at each of the next four meetings, taking rates to 3% by year-end. We see a further 50bp of rises in 1Q23 and rates remaining at 3.5% through 2024.

US - Payroll Growth, Wages and Employment



Source: Fitch Ratings, BEA, Haver Analytics

US - CPI Inflation Contributions



Source: Fitch Ratings, BLS, Haver Analytics

United States - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	1.9	5.7	2.9	1.5	1.3
Consumer spending	2.3	7.9	3.6	1.9	1.5
Fixed investment	3.4	7.8	3.2	1.4	2.1
Net trade (contribution pp)	-0.6	-1.9	-1.3	-0.6	-0.6
CPI inflation (end-year)	2.5	7.0	6.5	2.8	2.7
Unemployment rate	5.1	5.4	3.6	3.7	4.1
Policy interest rate (end-year)	1.22	0.25	3.00	3.50	3.50
Exchange rate, USDEUR (end-year)	0.87	0.88	0.95	0.95	0.95

Source: Fitch Ratings

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Eurozone

The war in Ukraine and the slowdown in China will constrain the eurozone economy this year. Higher inflation, more intense supply-chain disruption, and ongoing uncertainty around the conflict means we have cut our 2022 economic growth forecast to 2.6% from 3.0% in March.

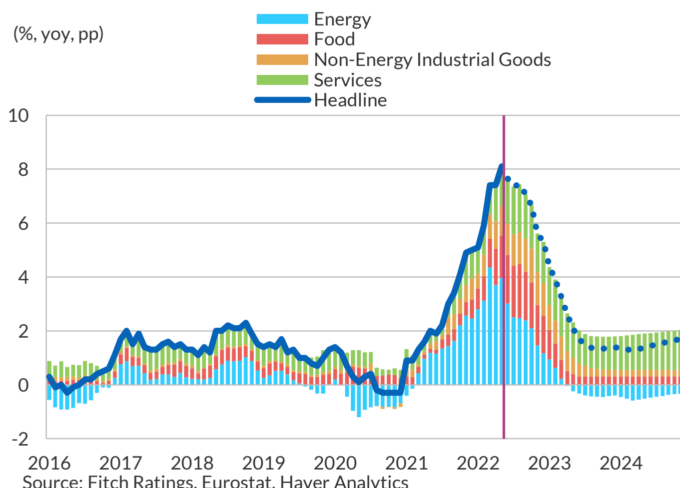
After inflation rose to a record high of 8.1% in May, we now expect it to end 2022 at 5.3%, up from our March GEO forecast of 3.4%. While higher energy and food prices, linked to the war in Ukraine, are driving up inflation, the pass-through of higher input costs to goods prices and the reopening of the services sector, combined with a pick-up in wages, is also expected to add to core price pressures. This will dampen consumer spending for the coming quarters, despite government efforts to limit impacts on the cost of living. Reflecting this, the European Commission's Consumer Confidence Indicator in May remained near its lowest since the first wave of the pandemic.

The outlook for industrial production also looks weak. The manufacturing PMI for May reached an 18-month low, with supply shortages, lengthy delivery times, and elevated producer costs intensified by the Ukraine war and China's lockdowns. Broader uncertainty about developments in the conflict, including on energy sanctions, is also limiting confidence. The expectations component of the Sentix economic index – an indicator of investor sentiment – rose slightly in June, but remained deeply negative. Strength in the services sector is helping eurozone economies to stay afloat. The reopening of the sector following Omicron variant restrictions in 1Q22 has released pent-up demand, with the services PMI in May still strong. Expectations for solid tourist inflows this year will also provide uplift. Strong employment should provide some support for households. With unemployment reaching record lows of 6.8%, further upward pressure on wages is also likely.

The ECB is also increasing efforts to normalise monetary policy. Following the June meeting, we expect the main refinancing operations (MRO) rate to rise by 100bp this year after quantitative easing ends in July, with a 50bp increase in September. In 2023, with falling energy prices expected to drag on headline inflation, we expect the ECB to be less aggressive in raising rates.

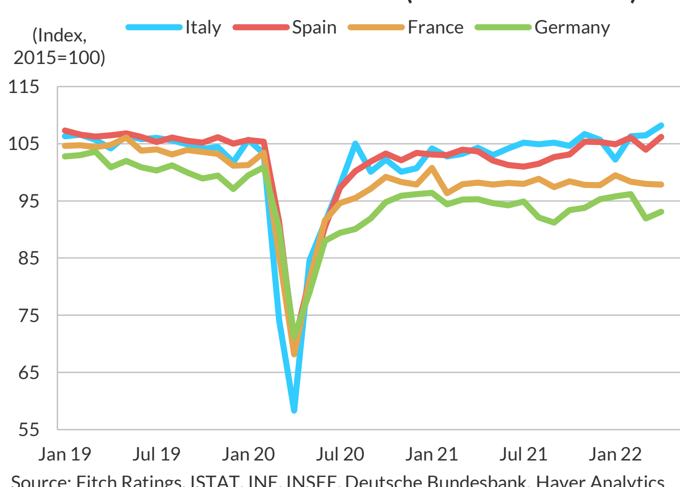
As inflation pressure eases and supply chains readjust, we expect pent-up industrial production and investment, alongside spending under the RRF, to drive growth of 2.1% next year.

Eurozone - Inflation



Source: Fitch Ratings, Eurostat, Haver Analytics

Eurozone - Industrial Production (excl. Construction)



Source: Fitch Ratings, ISTAT, INE, INSEE, Deutsche Bundesbank, Haver Analytics

Eurozone - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	1.0	5.4	2.6	2.1	2.1
Consumer spending	0.1	3.7	2.6	2.0	2.1
Fixed investment	2.2	4.1	2.8	2.7	2.2
Net trade (contribution pp)	0.1	1.3	-0.1	0.4	0.5
CPI inflation (end-year)	1.5	5.0	5.3	1.4	1.7
Unemployment rate	8.1	7.7	6.8	6.7	6.7
Policy interest rate (end-year)	0.00	0.00	1.00	1.50	1.50
Exchange rate, EURUSD (end-year)	1.15	1.13	1.05	1.05	1.05

Source: Fitch Ratings

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China

We have cut our forecast for 2022 growth to 3.7% to reflect the impact on activity of recent pandemic lockdown restrictions in Shanghai and elsewhere. Following very weak macroeconomic data for April we now anticipate a 1.5% qoq sequential decline in GDP in 2Q22 and only a fairly constrained rebound in 3Q22 as many restrictions will likely remain in place.

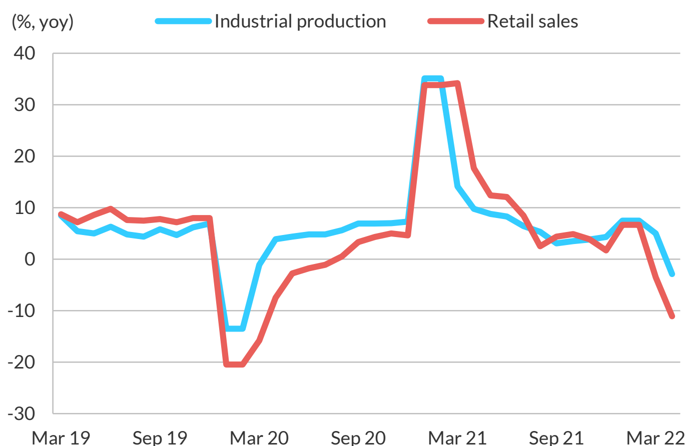
Shanghai was placed under severe lockdown in late-March. Stay-at-home orders, restrictions on movement and travel, and mass-testing regimes have hit consumption and manufacturing production hard. The city directly accounts for 4% of China's GDP and is one of the country's wealthiest urban centres but is also a key hub for domestic and international manufacturing trade.

The impact on the national economy – exacerbated by a tightening of restrictions in Beijing and elsewhere, though to a lesser extent – was seen in sharp outright yoy declines in industrial production and retail sales in April, a deepening of the housing slump and a slowdown in fixed asset investment and credit growth. While not as severe as the downturn in March 2020, these data strongly suggest that GDP will fall in 2Q22.

The Shanghai lockdown was eased on 1 June and national PMI indicators for May showed some slight improvements. But many restrictions in Shanghai and elsewhere are still in place, which will keep consumption subdued even if manufacturing activity resumes more quickly. There is also a high risk of new lockdowns being imposed if outbreaks return – the authorities remain fearful of the capacity of the healthcare system to cope with a surge in infections, partly reflecting incomplete vaccination coverage of the elderly and vulnerable population.

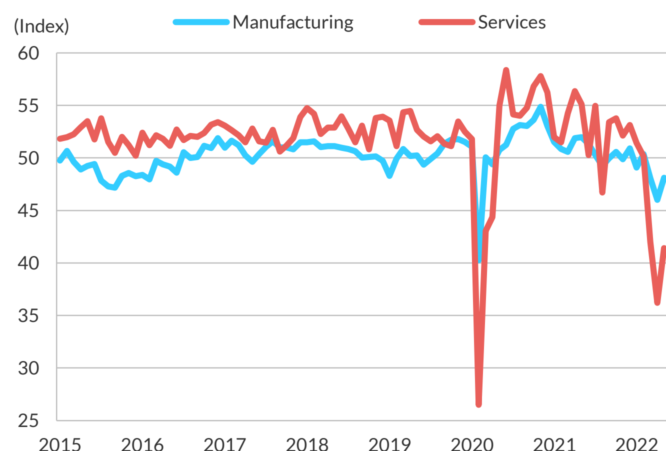
With the 'dynamic zero' approach to controlling the virus likely to remain in place well into 2023, the recovery in activity is likely to be restrained and subject to setbacks. Officials have increased pronouncements of policy support in recent weeks as concerns about the economy and job market have increased. The PBOC has cut mortgage rates and is encouraging banks to step up lending and there have been commitments to boost infrastructure spending. But easing measures announced look quite modest in scale and could struggle to gain much traction while social distancing remains prevalent. We see a more subdued recovery than in 2021, with growth at 5.3% next year.

China - Industrial Production and Retail Sales



Source: Fitch Ratings, NBS, CEIC

China - PMI Surveys



Source: Fitch Ratings, S&P Global, Caixin, Haver Analytics

China - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	6.0	8.1	3.7	5.3	5.0
Consumer spending	6.8	12.8	-2.7	5.4	5.1
Fixed investment	4.9	2.9	2.6	6.0	5.0
Net trade (contribution pp)	0.6	2.4	1.4	0.1	0.3
CPI inflation (end-year)	2.0	1.5	2.7	2.3	2.4
Policy interest rate (end-year)	3.15	2.95	2.70	2.70	2.70
Exchange rate, USDCNY (end-year)	6.73	6.37	6.70	6.90	7.00

Source: Fitch Ratings

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Japan

There is increasing evidence of a recovery in private domestic demand in 2Q22 but exports and industrial production are being hit by the lockdowns in China and associated supply-chain disruptions. We have revised down our 2022 GDP growth forecast to 2.0% from 2.4% from in the March GEO, with net trade now expected to be a drag on growth this year.

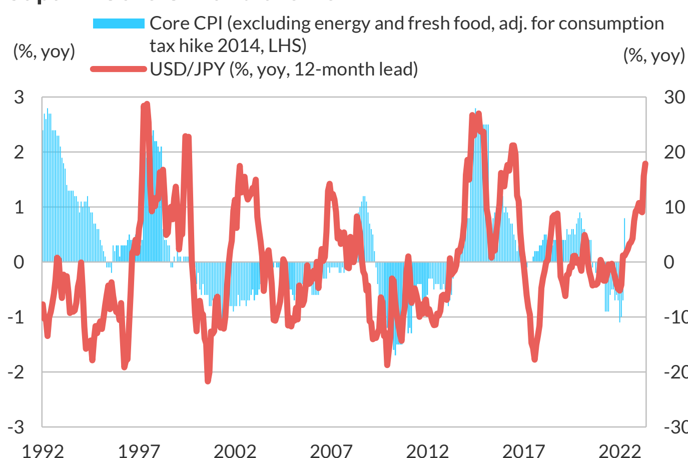
GDP declined by 0.1% in 1Q22, compared with -0.2% in the March GEO forecast. The fall reflected social distancing restrictions related to the Omicron Covid-19 variant and an accompanying slowdown in consumer spending. However, as restrictions have faded and mobility indicators have recovered there is increasing evidence of a pick-up in consumer spending and services activity in 2Q22. Services PMI balances moved back above 50 in April and May, retail and department store sales recovered in April and employment has also picked up. Indicators of business investment – including machinery orders - have also remained buoyant

However, the recovery is now suffering a renewed setback from the lockdown in China. Exports to China fell in annual terms in April and supply-chain disruptions were behind a decline in industrial production in April. The autos sector has been particularly badly affected by the Shanghai lockdown given its reliance on parts and component imports from China, with Toyota announcing large production cuts in June. We now expect exports to decline in 2Q22.

The yen has weakened sharply in the past three months in the face of rising US interest rates, trading around USD/JPY130 in recent weeks, its weakest for two decades. This is exacerbating upward pressure on inflation from higher imported energy prices and has prompted concerns from Finance Minister Shunichi Suzuki. Headline inflation reached 2.5% yoy in April, the highest rate since the late 1990s (excluding early 2014, when the consumption tax was increased) and core inflation jumped to 0.8%.

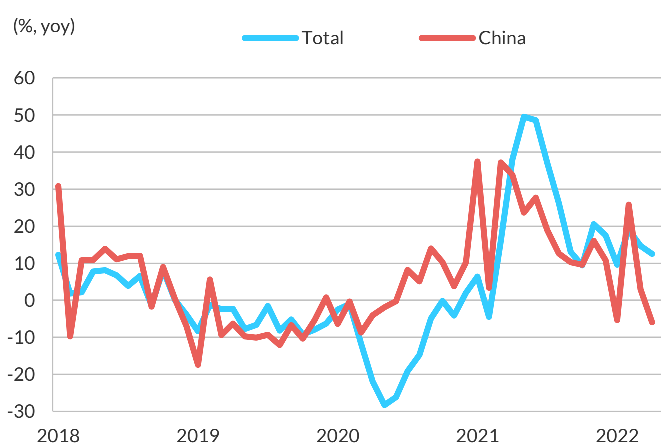
The Bank of Japan (BOJ) has shown little inclination to respond so far and indeed doubled down on its yield curve control (YCC) policy in April, pledging daily interventions to defend the 0.25% cap on 10-year Japanese government bond (JGB) yields. Nevertheless, with US 10-year yields expected to start rising again soon and inflation pressures growing, we think there is a chance that the BOJ could modestly recalibrate its YCC by raising 10YJGB yield cap by 10bp or so.

Japan - Core CPI and the Yen



Source: Fitch Ratings, Bank of Japan, MIC, Haver Analytics

Japan - Exports to World and China



Source: Fitch Ratings, Ministry of Finance, Japan Tariff Association, Haver Analytics

Japan - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	-0.2	1.7	2.0	1.8	1.1
Consumer spending	-0.6	1.3	4.1	2.2	1.2
Fixed investment	-0.6	-1.4	-2.3	2.1	2.1
Net trade (contribution pp)	0.1	1.1	-0.4	0.0	0.0
CPI inflation (end-year)	0.3	0.8	2.3	1.0	0.8
Unemployment rate	2.6	2.8	2.5	2.3	2.1
Policy interest rate (end-year)	-0.10	-0.10	-0.10	-0.10	-0.10
Exchange rate, USDJPY (end-year)	109.6	114.2	130.0	120.0	120.0

Source: Fitch Ratings

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United Kingdom

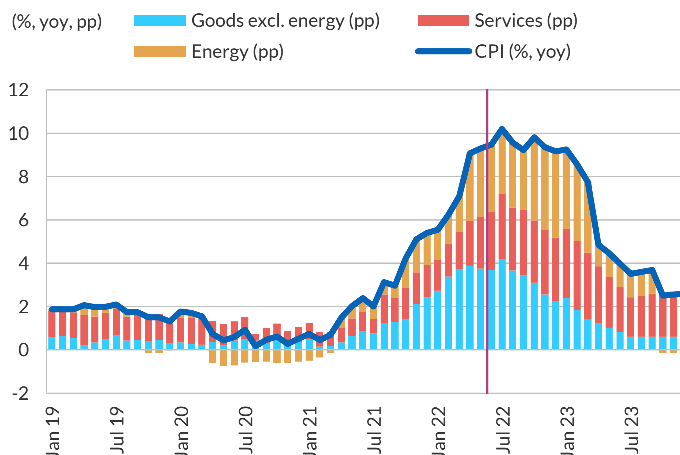
UK GDP expanded by 0.8% qoq in 1Q22, slightly faster than expected in the March GEO and helped by a rapid rebound in the leisure and transport sector after domestic Covid-19 restrictions were lifted in February. However, the outlook for growth has darkened following one of the sharpest increases in inflation among the advanced economies. We have revised down our 2023 growth forecast to 1.1% from 2.0% in the previous GEO to reflect a larger drag on real incomes from inflation, significantly faster-than-anticipated monetary tightening and slower growth in the eurozone.

Consumer confidence has fallen sharply in response to the jump in inflation to 9.0% in April, the highest rate since the early 1980s and boosted by an eye-watering 67% yoy increase in retail gas and electricity prices. Inflation will take a toll on real spending but the impact is likely to be more drawn out than many expect. Retail sales, consumer credit and credit and debit card transactions data point to GDP expanding further in 2Q22 and manufacturing and services PMI balances have remained above 50. Consumers have built up large savings buffers over the course of the pandemic and will now receive one-off fiscal transfers to help with the cost-of-living crisis. Re-opening momentum in the leisure and transport sector is ongoing. GDP declined in April but this largely reflected the wind down of the government's Covid-19 test and trace programme.

Moreover, household incomes are still being supported by strong job growth and accelerating wages. Labour demand continues to increase rapidly and while employment is still 280,000 below pre-virus levels, labour market conditions are very tight. The labour force is around 400,000 smaller than in January 2020 owing to a 1pp decline in the participation rate. Unemployment is now lower than before the pandemic and, for the first time, is less than the number of vacancies. This imbalance is pushing up wage growth, which reached nearly 10% yoy in April (these data are no longer significantly distorted by composition or furlough effects).

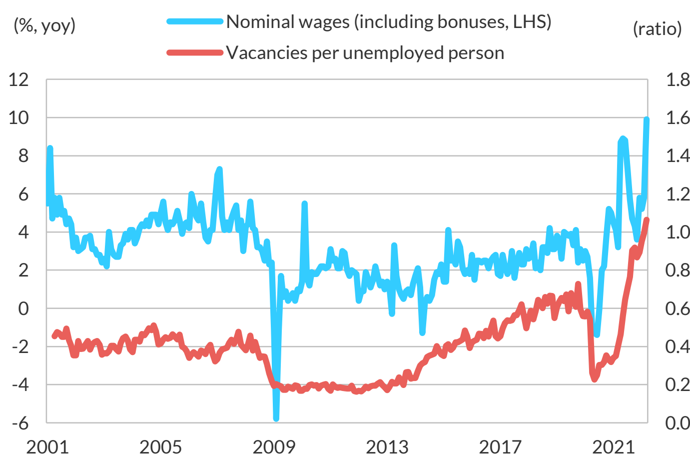
The BOE has raised interest rates four times since December 2021 but they remain very low at 1.0%. Inflation is likely to exceed 10% in coming months and remain very high through the rest of 2022, with a further 40% increase in electricity and gas prices expected in October. Wage-price dynamics are intensifying and we now expect the BOE to raise rates to 2% by end-2022 and to 2.5% by 1Q23.

UK - CPI Forecast



Source: Fitch Ratings, ONS, Haver Analytics

UK - Wages, Unemployment and Vacancies



Source: Fitch Ratings, ONS, Haver Analytics

United Kingdom - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	0.7	7.4	3.8	1.1	1.6
Consumer spending	0.2	6.2	4.6	1.4	2.0
Fixed investment	0.0	5.9	7.0	2.0	2.8
Net trade (contribution pp)	0.0	-1.5	-4.1	-0.5	-0.4
CPI inflation (end-year)	2.1	5.4	9.2	2.6	2.4
Unemployment rate	4.3	4.5	3.8	4.3	4.4
Policy interest rate (end-year)	0.39	0.25	2.00	2.50	2.50
Exchange rate, GBPUSD (end-year)	1.31	1.34	1.25	1.25	1.25

Source: Fitch Ratings

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Germany

We expect the recent lockdowns in China and the war in Ukraine to check Germany's economic recovery in 2022 through weaker trading conditions, more intense supply-chain disruption, and higher inflation. We now expect the economy to grow just 1.6% in 2022, down from 2.5% in the March GEO, which means it is now expected to reach its pre-pandemic level only in 1Q23.

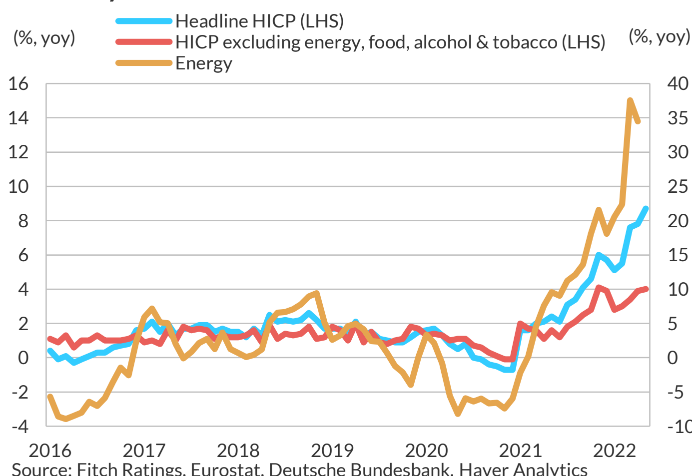
Germany's monthly industrial production, excluding energy and construction, fell 4.0% in March and barely recovered in April. Weaker manufacturing PMI readings and production expectations data since March suggest output will remain subdued, particularly as new export orders are hit by weaker growth in China and persistent component shortages. With Russian natural gas accounting for around 19% of Germany's total primary energy consumption, German industry also remains exposed to continued uncertainty in gas supply and prices as the conflict continues.

Stronger activity in the services sector as it bounces back from Covid-19 containment measures should provide some uplift for the economy. Germany's composite output PMI in May pointed to expanding business activity. A strong labour market should also buffer demand. Given the high demand for workers, we still expect the unemployment rate to gradually edge down over the forecast horizon. A 4.4% annual increase in Germany's hourly negotiated wages in 1Q22 also indicates that the tighter jobs market should provide uplift to pay packets, alongside planned minimum wage increases in late-2022.

Real household income will nonetheless be squeezed by higher inflation, which will keep consumer spending subdued this year. The European Commission's Consumer Confidence Indicator for Germany in May remained below lows reached during the first wave of the pandemic. Although energy and food prices have been higher than expected, raised input prices and disruption in the industrial sector is passing through to higher core inflation. We now expect the headline HICP to end 2022 at 5.6%, up 1.6pp on our previous forecast.

The closure of Russian pipelines, gas rationing, and higher energy prices, as part of escalations in the conflict, continue to pose a risk to growth. That said, as disruption from the conflict fades, and energy prices fall, we still expect stronger consumer spending and pent-up industrial activity and investment to support solid growth of around 2.3% in 2023, above our previous forecast for 2.1%.

Germany - Inflation



Source: Fitch Ratings, Eurostat, Deutsche Bundesbank, Haver Analytics

Germany - Confidence

Source: Fitch Ratings, European Commission, Haver Analytics

Germany - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	0.6	2.9	1.6	2.3	2.3
Consumer spending	-0.2	0.3	3.6	2.5	2.3
Fixed investment	1.4	1.1	2.0	3.6	3.1
Net trade (contribution pp)	-0.2	0.7	-1.9	-0.1	0.3
CPI inflation (end-year)	1.7	5.7	5.6	1.6	1.7
Unemployment rate	3.4	3.6	3.1	2.9	2.8
Policy interest rate (end-year)	0.00	0.00	1.00	1.50	1.50
Exchange rate, EURUSD (end-year)	1.15	1.13	1.05	1.05	1.05

Source: Fitch Ratings

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France

We have lowered our forecast for economic growth in France this year to 2.4%, from 3% in the March GEO. Quarterly economic growth in 1Q22 was weaker than expected at -0.2%, against our 0.2% forecast. France is not particularly reliant on Russia for energy or trade, but a higher inflation outlook, intensifying supply-chain disruption, and weaker activity across Europe due to the war in Ukraine is likely to restrain growth further this year and next.

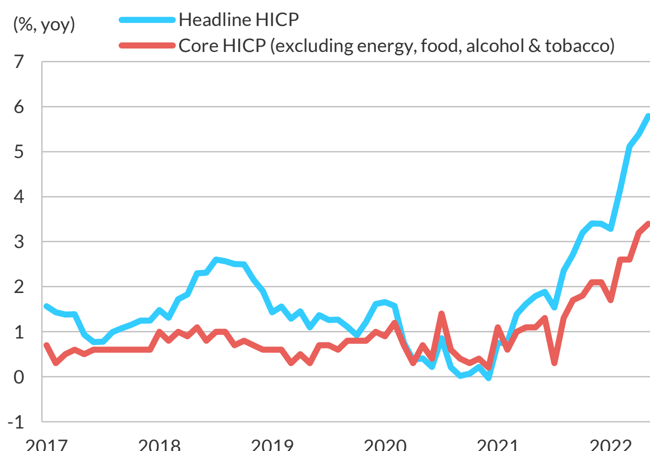
Quarterly household spending fell in 1Q22, and is likely to remain subdued in the coming quarters. INSEE's household confidence indicator dropped further below its long-term average in May, partly reflecting high price expectations and a weak assessment of conditions for major purchases. We now expect headline inflation at 4.2% by end-2022, up from 3%, given higher energy and food prices, alongside firmer core inflation.

The full inflationary impact of high energy costs will be limited by the government's electricity price caps, and given France's greater emphasis on nuclear power. Meanwhile, the easing of Covid-19 restrictions has supported a boost to demand, with services sector PMI in May still pointing to a strong expansion in 2Q22. Expectations for a solid tourist season should also support growth in 2H22.

Strength in the jobs market, and high savings, will provide a buffer for households too. Unemployment dropped to 7.3% in 1Q22, and we expect it to continue gradually edging down across the forecast horizon. With job vacancies and hiring plans remaining high, and the participation rate above pre-pandemic levels, wage growth is also likely to pick up this year.

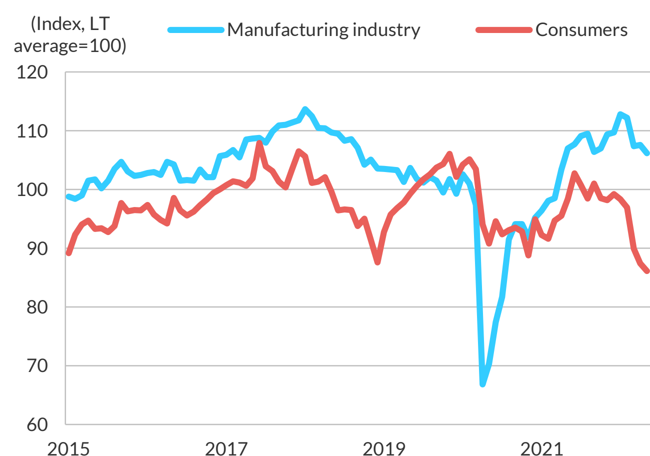
The outlook for industry is poorer. France's industrial production and INSEE's manufacturing climate indicator has slipped since the start of the year, as supply-chain disruption has intensified with the war in Ukraine and lockdowns in China. Manufacturing activity will remain sluggish. France's manufacturing PMI dropped to its lowest since October 2021 in May, amid the challenging export environment, ongoing component shortages, and elevated costs. Improved trading conditions, alongside easing inflation, should provide a fillip to household spending and firms' output and investment activity in 2023, and as such we expect growth of more than 2% in 2023.

France - Inflation



Source: Fitch Ratings, INSEE, Eurostat, Haver Analytics

France - Confidence



Source: Fitch Ratings, INSEE, Haver Analytics

France - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	1.0	6.8	2.4	2.1	1.9
Consumer spending	0.6	5.3	2.5	2.4	2.0
Fixed investment	3.1	11.5	1.9	2.8	2.0
Net trade (contribution pp)	-0.2	0.1	0.1	-0.1	0.1
CPI inflation (end-year)	1.4	3.4	4.2	1.5	1.7
Unemployment rate	8.6	7.9	7.4	7.3	7.2
Policy interest rate (end-year)	0.00	0.00	1.00	1.50	1.50
Exchange rate, EURUSD (end-year)	1.15	1.13	1.05	1.05	1.05

Source: Fitch Ratings

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Italy

We have maintained our 2022 GDP growth forecast for Italy at 2.7%. Quarterly economic growth in 1Q22 at 0.1% was in line with our expectations, while 4Q21 growth was revised upward slightly, which means the Italian economy is now back at pre-pandemic levels. Nonetheless, the effects of the war in Ukraine and its associated impact on inflation and supply chains will still significantly restrain growth this year.

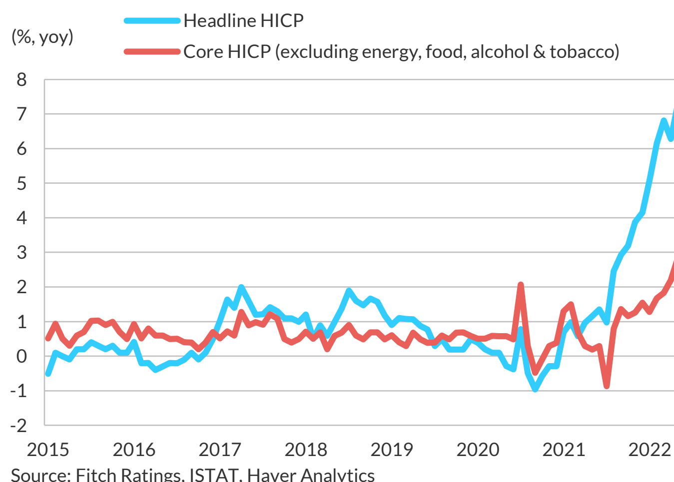
We expect consumer spending to support growth this year, but higher inflation coupled with still-subdued wage growth will dampen households' real spending power: ISTAT's consumer confidence indicator has fallen from highs in 2H21. We have also revised up our year-end inflation forecast by 1.7pp to 4.8% as the pass-through of higher input costs has increased core inflation pressures alongside elevated food and energy prices.

Disruption in the form of higher energy costs, supply-chain issues, and the suspension of some Russian activities due to sanctions and the war in Ukraine is likely to continue dampening Italian business activity for the months ahead. This was reflected in ISTAT's business confidence indicator for manufacturing and construction, which fell in May. With Russian gas accounting for around a fifth of Italy's total primary energy consumption, Italian industry also remains exposed to ongoing supply uncertainty and price shocks.

Resilience in the services sector should support positive growth in 2Q22. Services PMI rose in April and remained above 50 in May, following the reopening of the economy. The ongoing normalisation of travel should support strong tourist activity in 2H22. The strong labour market will also be a buffer. The European Commission's Employment Expectations indicator for Italy – a measure of firms' hiring plans – increased and remained above its historical average in May. With strong demand for workers, the jobless rate fell to 8.6% in 1Q22, and so we now expect the unemployment rate to average 8.5% this year, compared with 9.1% previously.

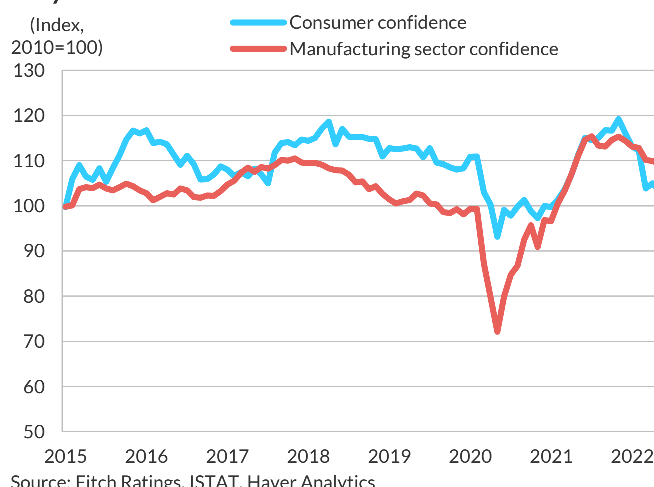
In 2023, we expect demand to be bolstered by a decline in inflation as energy prices fall, alongside strength in the jobs market and investment spending under the RRF. As such we expect solid economic growth of 1.9% in Italy next year.

Italy - Inflation



Source: Fitch Ratings, ISTAT, Haver Analytics

Italy - Confidence Indicators



Source: Fitch Ratings, ISTAT, Haver Analytics

Italy - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	0.1	6.6	2.7	1.9	1.9
Consumer spending	-0.5	5.2	2.2	2.2	2.1
Fixed investment	3.1	17.0	8.6	2.4	1.9
Net trade (contribution pp)	-0.1	0.0	-0.9	-0.1	0.2
CPI inflation (end-year)	1.0	4.2	4.8	1.1	1.3
Unemployment rate	10.1	9.5	8.5	8.2	7.9
Policy interest rate (end-year)	0.00	0.00	1.00	1.50	1.50
Exchange rate, EURUSD (end-year)	1.15	1.13	1.05	1.05	1.05

Source: Fitch Ratings

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Spain

We have revised down our forecast for the Spanish economy in 2022: we now expect GDP growth of 4.4%, compared with 5% previously. This means Spain's economy is now unlikely to reach its pre-pandemic level until 2Q23.

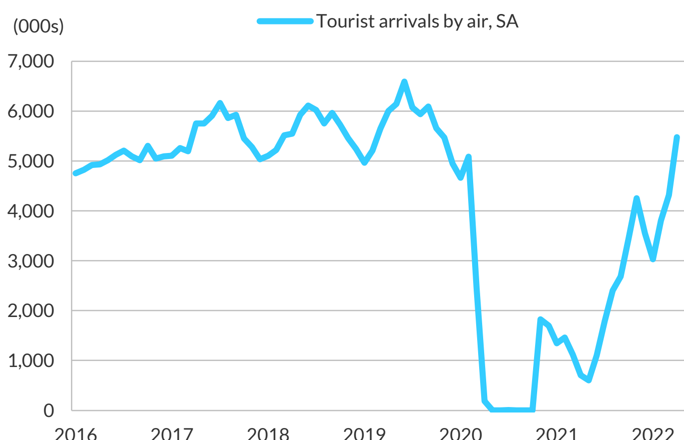
Quarterly private consumption spending fell sharply in 1Q22 as higher inflation hit households' real income. This weakness will continue throughout the year. The European Commission's Consumer Confidence indicator for Spain remained weak in April and May, partly reflecting households' downbeat assessment of forthcoming economic and financial conditions. We have raised our year-end forecast for inflation to 4.4%, from 2.9%, after annual inflation surged to 9.8% in March, and remained elevated at 8.5% in May. While the government's cap on gas prices should help to limit inflation, high food prices and core inflation pressure given elevated input prices and the reopening services sector, means inflation remains strong.

With fewer restrictions to global travel, Spain will benefit from a recovery in tourist activity this year, which should drive up quarterly economic growth and exports in 2H22. In 1Q22 total arrivals were already estimated at around 70% of levels in the same quarter in 2019. A sturdy labour market will support growth too. We expect the unemployment rate to continue edging down throughout the forecast horizon, given strong demand. The European Commission's Employment Expectations indicator for Spain – a measure of firms' hiring plans – remained above its long-term average, and increased, in May.

Although industrial production, excluding construction, rose in April and reversed a fall in March, high costs and import disruption emanating from the war in Ukraine are still likely to limit Spain's industrial activity in the months ahead. In 2Q22, manufacturing PMI readings have slowed relative to 1Q22 and the European Commission's Industrial Confidence indicator turned negative in April and remained weak in May, pointing to more subdued activity ahead given supply issues and stagnant order books. Delays in RRF spending in 2021 should help to support stronger public- and private-sector investment this year and next.

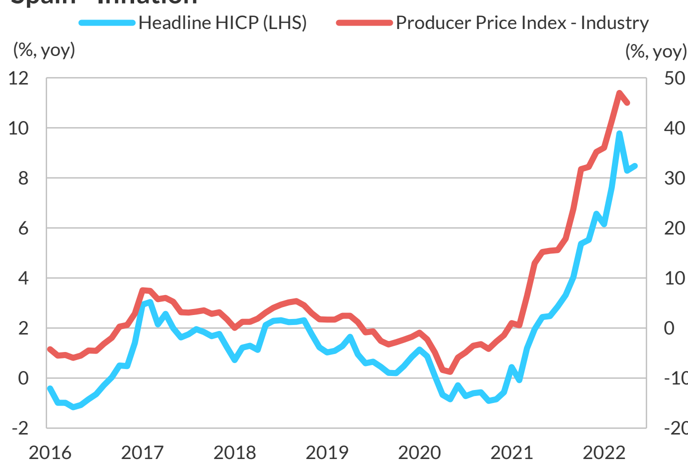
In 2023, we expect the inflation rate to fall significantly and supply disruptions to ease, which should support stronger consumption and production. We forecast solid growth of 3.4% in 2023, and similar in 2024.

Spain - Tourism



Source: Fitch Ratings, INE, Haver Analytics

Spain - Inflation



Source: Fitch Ratings, INE, Haver Analytics

Spain - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	0.3	5.1	4.4	3.4	3.3
Consumer spending	-0.3	4.6	0.0	4.0	3.3
Fixed investment	2.5	4.3	7.4	4.5	4.2
Net trade (contribution pp)	-0.4	0.4	2.5	-0.1	0.4
CPI inflation (end-year)	1.4	6.6	4.4	1.0	1.3
Unemployment rate	15.4	14.8	13.4	13.1	12.7
Policy interest rate (end-year)	0.00	0.00	1.00	1.50	1.50
Exchange rate, EURUSD (end-year)	1.15	1.13	1.05	1.05	1.05

Source: Fitch Ratings

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Switzerland

Switzerland's trade-driven economy will be more subdued in 2022 as weaker growth in the eurozone and China adds to existing supply-chain disruption and low investor confidence emanating from the war in Ukraine. As such, we have revised down our forecast for growth this year to 2.6%, from 3.1%.

The economy grew 0.5% qoq in 1Q22 in line with expectations, with the Omicron variant wave and restrictions weighing on the services sector. While cases have fallen and the economy has reopened, looking ahead, the KOF economic barometer – a leading indicator of economic activity – points to a weakening in growth conditions. It dropped in 1Q22, and fell below its long-term average in May.

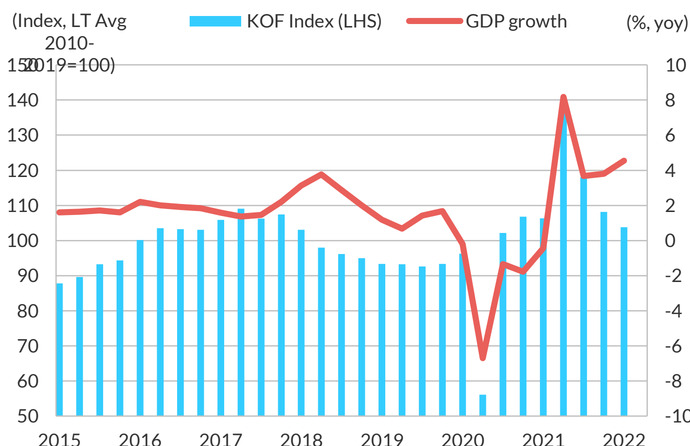
Global trade conditions have weakened since March, although the Swiss manufacturing sector has shown resilience. Manufacturing PMI fell in May, but it remained elevated at 60. Looking ahead, the expectations component of the Sentix economic index, a gauge of investor confidence, remained deep in negative territory in May and June. Industrial activity and exports are likely to weaken as subdued global growth hits output and supply chains.

Higher inflation will also weaken consumers' spending power this year, as reflected by the sharp drop in SECO's consumer sentiment index in April – its largest decline since the onset of the pandemic. The pick-up in inflation to 2.9% in May was driven by high energy costs, but also strengthening core inflation pressures. We now expect inflation to end the year at 1.7%, rather than 1%. The strong labour market will, however, provide some cushion. With the unemployment rate falling to 2.3% in 1Q22, we now expect the jobless rate to average 2.2% this year, down from 2.4%.

We expect the inflation rate to fall towards 1% in 2023 as energy price pressures ease. Nonetheless, we think the SNB will take the opportunity to begin raising interest rates in 2022 along with the ECB, also to avoid notable depreciation in the Swiss franc. We anticipate two 25bp increases this year, followed by two more in 2023 to take rates into positive territory.

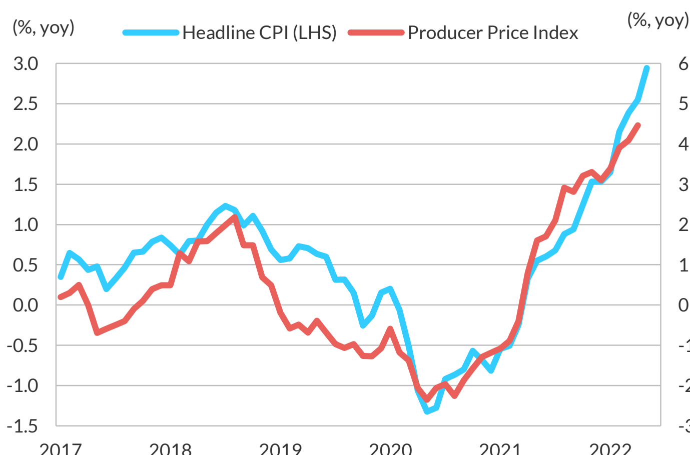
Lower inflation, an improvement in global trading conditions, and ongoing labour market strength should lead to decent growth of 1.9% in 2023. That is down 0.2pp on our previous forecast, following the weaker overall outlook for global growth next year.

Switzerland - KOF Index



Source: Fitch Ratings, KOF, SECO, Haver Analytics

Switzerland - Inflation



Source: Fitch Ratings, SFSO, Haver Analytics

Switzerland - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	1.4	3.7	2.6	1.9	1.7
Consumer spending	0.4	2.6	3.6	1.8	1.5
Fixed investment	1.4	3.4	0.9	1.8	1.5
Net trade (contribution pp)	1.2	4.1	-0.7	0.5	0.5
CPI inflation (end-year)	0.3	1.5	1.7	0.9	1.1
Unemployment rate	2.8	3.0	2.2	2.1	2.0
Policy interest rate (end-year)	-0.75	-0.75	-0.25	0.25	0.50
Exchange rate, USDCHF (end-year)	0.96	0.91	0.95	0.96	0.96

Source: Fitch Ratings

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Australia

We have cut our forecast for economic growth in Australia in 2022 to 4.0% from 4.2%. Quarterly growth in 1Q22 came in below expectations, at 0.8% against our 1.1% forecast, partly driven by high import activity. Meanwhile, the global growth outlook has weakened since the March GEO, and projections for inflation have increased.

Higher prices this year will restrain consumer spending power. In May, the Westpac-Melbourne Institute's consumer sentiment index dropped notably, partly reflecting households' anticipation for weaker economic conditions and falling real wages. Inflation in 1Q22 was above expectations, and we now project it to reach 5.5% by the end of 2022 – 1pp above our previous forecast. Surging energy and food prices linked to the conflict in Ukraine, alongside domestic capacity constraints and elevated input costs have been driving inflation higher.

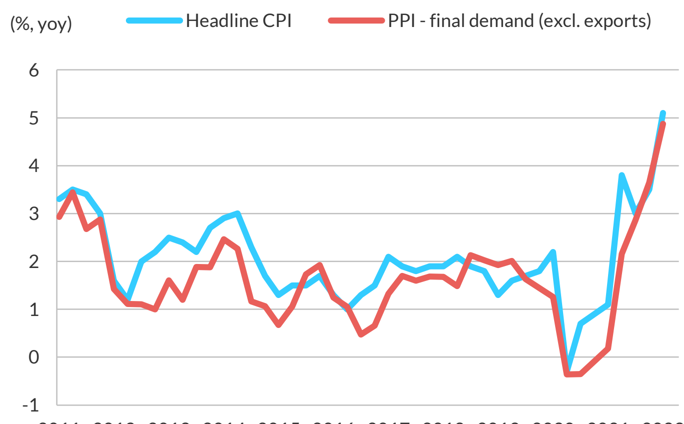
The resultant stronger interest rate outlook will also be a restraint to business and consumer activity in the coming years. The Reserve Bank of Australia (RBA) surprised in May and June with a total of 75bp in rate rises. Given mounting price pressures, we now expect the RBA to be more aggressive in raising rates. We anticipate increases of 100bp this year followed by a couple of increases next year to take rates to 2.5% by end-1H23.

Consumer spending will nonetheless be a key driver of growth this year. The Omicron variant led to patchy activity in 1Q22, but cases have now eased and household savings and the labour market remain supportive. The unemployment rate fell sharply to 4% in February, and we expect it to edge downward throughout the year, with job vacancies reaching a record high in 1Q22 and inward migration set to recover gradually as border restrictions ease.

While iron ore exports have been dampened by lockdowns and slower growth in China recently, elevated commodity prices amid global supply constraints are generally providing support for the Australian economy, with strong mining profits and solid demand for LNG. Services sector activity eased in May, but high levels of backlogged work also suggest an improvement in future output.

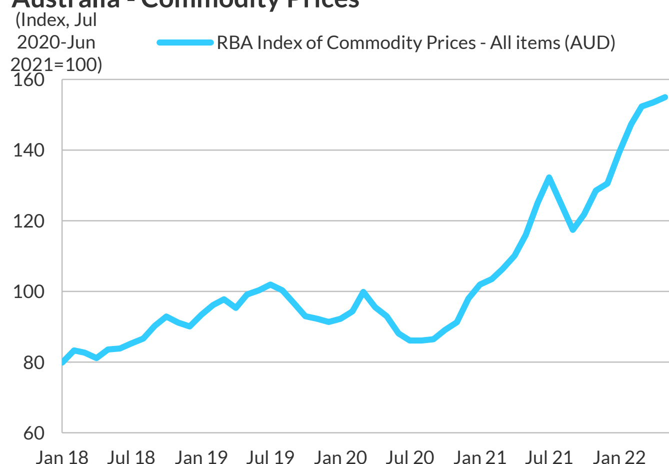
As global inflationary pressures and supply-chain frictions ease in 2023, we expect the growth outlook to improve slightly. We now forecast 2.5% growth next year, against our previous projection for 2.3%.

Australia - Inflation



Source: Fitch Ratings, ABS, Reserve Bank of Australia, Haver Analytics

Australia - Commodity Prices



Source: Fitch Ratings, Reserve Bank of Australia, Haver Analytics

Australia - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	2.0	4.8	4.0	2.5	2.0
Consumer spending	1.0	5.0	5.2	2.3	2.0
Fixed investment	2.0	9.6	2.1	2.7	2.5
Net trade (contribution pp)	-0.1	-1.6	-1.5	0.4	0.2
CPI inflation (end-year)	1.8	3.5	5.5	2.1	2.3
Unemployment rate	5.5	5.1	3.9	4.0	4.2
Policy interest rate (end-year)	0.92	0.10	1.85	2.50	2.50
Exchange rate, USDAUD (end-year)	1.37	1.38	1.40	1.40	1.40

Source: Fitch Ratings

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Canada

Since our March update, geopolitical shocks have increased demand for Canada's exports and the Bank of Canada (BOC) has raised interest rates more aggressively than expected. The BOC also started quantitative tightening in April, running down its medium- and long-term securities holdings as they mature.

We expect the first trend to lift Canada's 2022 economic growth to 3.8% (3.7% previously) as oil, gas, metals and cereal prices boost Canadian export returns. Domestic demand remains strong, driven by the firm recovery of business investment and by strong household consumption partly fuelled by accumulated household savings buffers. The labour market has tightened considerably year-to-date, with unemployment dropping to 5.2% in April 2022 from 8.0% in April 2021.

The slowdown in the housing market is likely to lead to weaker consumption growth. Nevertheless, we expect robust long-run demand from immigration inflows and tight current supply will sustain investment in the housing stock, despite the decline of sales/new listings in March and April.

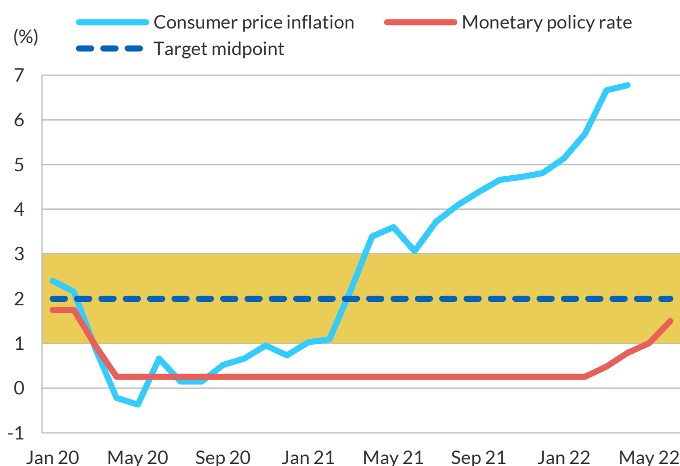
We have trimmed our 2023 economic growth forecast to 2.2% from 2.4%. As economic output normalises toward pre-pandemic levels, we expect the BOC's tighter monetary stance will increasingly weigh on consumption in 2023 when we assume most excess household savings will be exhausted.

The BOC has raised the policy rate 125bp in 2022 to 1.5% in June from 0.25% in January 2022. We expect that BOC will raise the overnight rate another 150bp to 3% by year-end and sustain the policy rate through 2023, as it seeks to lower demand and stabilise inflation expectations.

Supply-chain disruption, geopolitical shocks to fuel and food markets, and housing market strength have permeated both CPI and core inflation measures, raising concerns to the BOC of long-run expectations momentum. Headline 12-month inflation rose 6.8% yoy in April, following a steepening trend since August 2021.

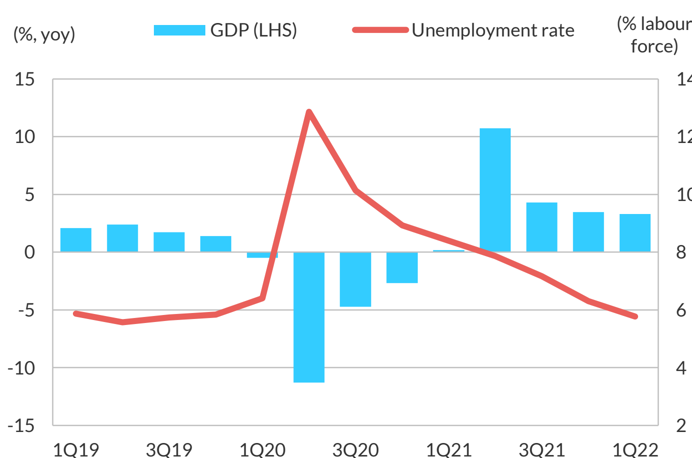
The federal and provincial governments have removed most pandemic-era stimulus, although aggregate general government deficit reduction will be slow as it falls to 4.1% of GDP in 2022, 3.1% in 2023, and 2.4% in 2024.

Canada - Inflation and Interest Rate



Source: Fitch Ratings, Bank of Canada, Statistics Canada, Haver Analytics

Canada - GDP and Unemployment



Source: Fitch Ratings, Statistics Canada, Haver Analytics

Canada - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	1.4	4.5	3.8	2.2	1.8
Consumer spending	1.3	4.9	2.8	1.1	2.2
Fixed investment	2.0	7.1	5.5	3.8	2.8
Net trade (contribution pp)	-0.4	-1.9	0.1	0.2	-0.6
CPI inflation (end-year)	2.0	4.8	5.0	3.0	2.0
Unemployment rate	7.0	7.4	5.3	5.5	5.5
Policy interest rate (end-year)	0.93	0.25	3.00	3.00	3.00
Exchange rate, USDCAD (end-year)	1.30	1.29	1.28	1.30	1.30

Source: Fitch Ratings

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Brazil

Fitch has increased Brazil's GDP growth forecast to 1.4% from 0.5% for 2022 on a better-than-expected 1Q22 GDP result. Brazil's economy grew by 1% qoq (1.7% yoy) in 1Q22, reflecting the continued reopening of the economy and fiscal support from an augmented social programme. Improved terms of trade and the recovering labour market, reflected in a declining unemployment rate and increasing participation rate, are supporting factors for near-term growth.

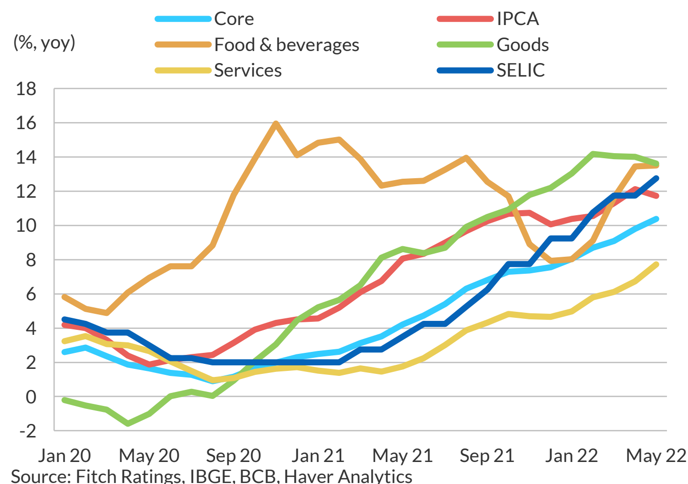
Nevertheless, slowing global demand (including China – a major trading partner of Brazil), high inflation, tightening domestic and external financing conditions and a polarising election cycle ahead will increasingly weigh on growth in 2H22. Fitch has also revised down its 2023 growth forecast to 1% as tighter domestic monetary policy will feed through the economy with a lag. The policy and reform stance of the next administration that takes office in January 2023 will be important for determining the growth outlook for 2023-2024.

Inflationary pressures have intensified in Brazil with IPCA inflation reaching 11.7% in May and core inflation reaching 9.3%. In light of the sustained price pressures, exacerbated by higher global prices amid supply-side disruptions, Fitch has revised up its inflation forecasts for 2022-2023. Inflation expectations have continued to move upwards and remain above the target for 2022 and 2023. The government has been cutting taxes to curb price pressures with additional such measures being discussed in congress, which, if passed could lower our forecasts.

The central bank BCB has tightened monetary policy significantly, with the benchmark Selic rate raised to 12.75% from a nadir of 2%. Fitch forecasts a modest increase in rates, although evolving external conditions and domestic price pressures could lead to rates to rise further and for longer.

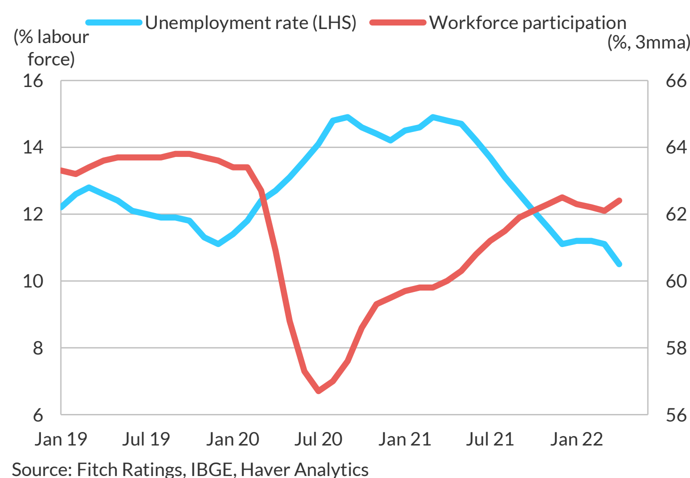
The Brazilian real has appreciated in recent months owing to higher domestic rates, low external imbalances and higher commodity prices (partly due to the war in Ukraine). However, the real has faced bouts of weakness too, especially as concerns over China slowdown and US Fed tightening have mounted. As such, renewed currency weakness cannot be ruled out.

Brazil - Inflation



Source: Fitch Ratings, IBGE, BCB, Haver Analytics

Brazil - Labour Market



Source: Fitch Ratings, IBGE, Haver Analytics

Brazil - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	1.0	4.6	1.4	1.0	2.1
Consumer spending	1.1	3.9	1.7	0.9	2.1
Fixed investment	4.7	17.3	-4.4	2.7	3.9
Net trade (contribution pp)	-0.2	-0.8	1.4	0.0	0.0
CPI inflation (end-year)	4.5	10.1	8.8	4.5	3.3
Policy interest rate (end-year)	6.01	9.25	13.50	9.25	7.50
Exchange rate, USDBRL (end-year)	4.27	5.58	5.10	5.10	5.10

Source: Fitch Ratings

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Russia

Judging by the recent improvement in financial market variables, the Russian economy appears to have shown a degree of resilience to the sanctions imposed by Western governments. After an initial surge in inflation, CPI has started to fall in recent weeks while the rouble has now strengthened to a level higher than before the start of the war after plummeting in late February. The 3.5% yoy expansion in 1Q22, which on quarterly seasonally adjusted basis translates to somewhere between +0.1 and -0.1% qoq, was also less severe than the -1.3% qoq decline we expected.

Russia still looks on course for a long, grinding decline in living standards, even without a full EU embargo on its oil exports. Numerous international businesses have stopped operating in Russia, a move that will result in huge disinvestments in the country. The May manufacturing PMI index reported that firms had already experienced a fall in output as new orders decline and uncertainty rises. Car sales plunged in May while imports also slumped (Russia currently is not publishing import data, but the collapse in exports to Russia by other countries is evident). Shortages of consumer goods as well as intermediate goods and companies' shrinking stocks are likely to worsen as supply-chain issues deteriorate in coming months. Commercial banks' requirements for borrowers and loan collateral have become much tougher.

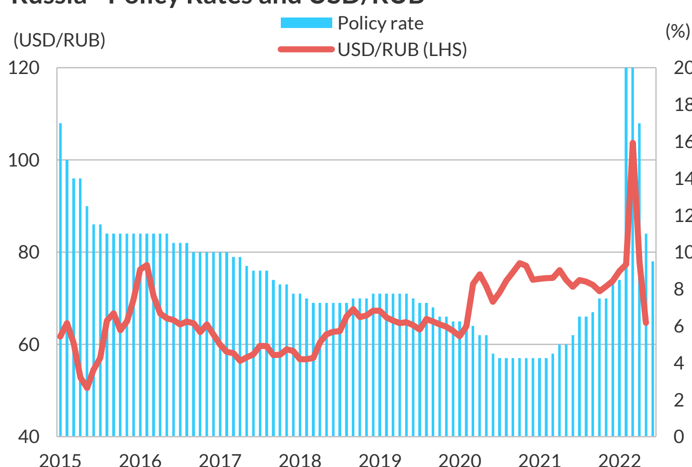
The initial plunge in the RUB/USD to around RUB130+ resulted in a surge in weekly inflation, prompting the CBR to raise rates by 1,000bp to 20% in February. The CBR also imposed capital controls including an 80% surrender requirement on exporters. The currency has also been supported by the continuing flow of energy exports, with the current account surging in the first four months of the year. The significant subsequent appreciation of the rouble to around RUB60+ has helped to suppress inflation and the CBR followed by cutting policy rates to 9.5% in June. It has eased some capital control measures to help counter the appreciation of the currency.

We continue to expect a GDP contraction of 8% this year though there remains a high degree of uncertainty. We have downgraded our GDP projection for next year to -1.5% (from -0.2%). The USDRUB is forecast at 85 at end 2023.

Russia - Foreign Brand Car Sales

Source: Fitch Ratings, Association of European Businesses, Haver Analytics

Russia - Policy Rates and USD/RUB



Source: Fitch Ratings, Central Bank of Russia, Haver Analytics

Russia - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	1.8	4.7	-8.0	-1.5	1.3
Consumer spending	2.8	9.5	-12.0	-3.5	0.3
Fixed investment	1.7	6.8	-5.3	-3.4	1.4
Net trade (contribution pp)	-0.6	-2.7	-2.8	0.0	0.2
CPI inflation (end-year)	4.2	8.4	16.0	12.0	10.0
Policy interest rate (end-year)	6.93	8.50	8.50	8.50	8.50
Exchange rate, USDRUB (end-year)	66.30	74.29	75.00	85.00	95.00

Source: Fitch Ratings

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India

GDP grew by 4.1% yoy in 1Q22 compared to our March forecast of 4.8%. We now expect the economy to grow by 7.8% this year (2022-2023), revised down from our previous forecast of 8.5%.

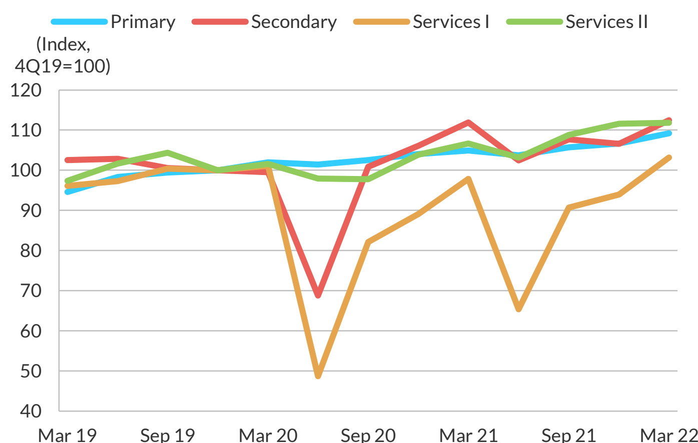
On a seasonally adjusted basis, 1Q22 GDP increased by 0.5% qoq, just below our March forecast of 0.7%, with government spending and investment more than offsetting weakness in exports. Consumer spending grew during the quarter, but slowed to a crawl given the impact of Omicron variant on economic activity. We expect 2Q22 growth to improve on a rebound in consumption as Covid-19 cases subsided towards end-March. We see consumer spending sustaining the economy in 2022 given the potential for catch-up, as an easing in restrictions allows for greater spending on sectors such as retail, hotels and transport. Sectors of the economy such as these ('Services I" in the chart) that require greater face-to-face contact continue to lag behind others.

Inflation has risen to an eight-year high and broadens across more CPI categories, posing a severe challenge to consumers. In the past three months, food inflation has increased by an average of 7.3% yoy while healthcare bills are rising at a similar pace. Pipeline pressures as measured by the wholesale price index (WPI) are also increasing. While the pass-through to CPI appeared contained until recently, WPI at close to 16% yoy could result in higher costs being passed on to consumers as demand for services increases.

With the inflation rate on the rise, the Reserve Bank of India (RBI) turned hawkish in April by introducing the new Standing Deposit Facility (SDR), which replaced the reverse repo rate to set a new, higher floor for the interest rate corridor. In May, in an unscheduled policy announcement, the RBI raised rates by 40bp to 4.4%, and subsequently to 4.9% in June. Given the deteriorating outlook for inflation, we now expect the RBI to lift rates further to 5.9% by December 2022 and to 6.15% by the end of 2023 (vs. previous forecast of 5%) and to be unchanged in 2024.

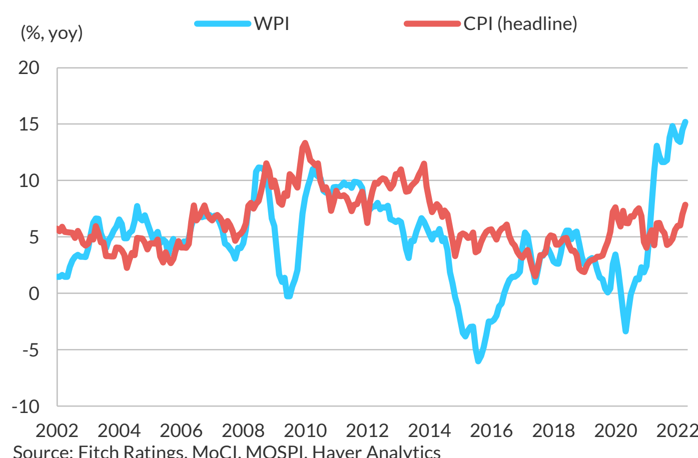
Higher borrowing costs are also likely to affect consumers although recent cuts to fuel excise duties and increased fertiliser subsidies will provide some small reprieve. India's economy also faces a worsening external environment, elevated commodity prices, persistent supply bottlenecks and tighter global monetary policy.

India - GDP by Industry



Source: Fitch Ratings, Haver Analytics

India - Selected Inflation Measures



Source: Fitch Ratings, MoCI, MOSPI, Haver Analytics

India - Forecast Summary

(%) FY starting April	Annual Avg. 2017-2021	FY21-22	FY22-23F	FY23-24F	FY24-25F
GDP	3.8	8.7	7.8	7.4	7.2
Consumer spending	4.1	7.9	9.2	6.0	5.9
Fixed investment	5.2	15.8	10.8	7.2	7.2
Net trade (contribution pp)	-0.9	-2.9	-2.1	0.7	0.6
CPI inflation (end-cal. year)	4.6	5.7	6.5	5.0	5.0
Policy interest rate (end-cal. year)	5.28	4.00	5.90	6.15	6.15
Exchange rate, USDINR (end-cal. year)	70.39	74.30	79.00	80.00	80.00

Source: Fitch Ratings

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Korea

GDP grew 0.6% qoq in 1Q22, in line with our March GEO forecast, with declines in investment and consumption offset by a strong contribution from net trade. The spread of the Omicron variant and the lockdown that followed at the start of 2022 greatly affected domestic demand. We expect the economy heading into 2Q22 to regain some momentum given the authorities' removal of all remaining Covid-19 restrictions and the downgrade of the coronavirus to a "class 2" disease, alongside treatable diseases, such as cholera and tuberculosis.

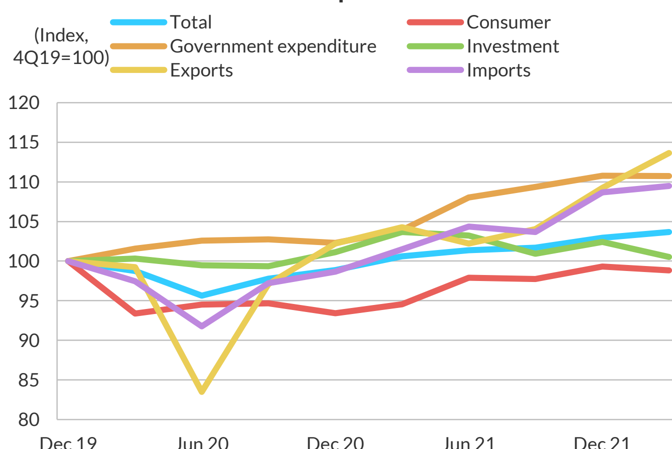
An improving Covid-19 situation and a further drop in precautionary savings should provide a near-term boost to consumption, which continues to be below pre-pandemic levels. However, high inflation continues to affect consumers' real purchasing power while higher policy rates are expected to increase debt servicing costs for highly indebted households. Household credit growth is also weakening as policy rates are tightened and tougher rules on lending are implemented to rein in growing household debt.

Slower global growth and Fitch's downward revision to China's growth are external challenges for the Korean economy. Strong export growth in 1Q22 was followed by a soft patch in April given China's disruption to trade caused by the lockdown in Shanghai. But export growth accelerated in May as an increase in shipments to Europe and the US more than offset disruptions to trade with China. Nevertheless, we expect Korea's exports cycle to remain dependent on China's economy in the coming months.

For 2022, we forecast GDP growth of 2.4% (down from previous forecast of 2.7%) with the war in Ukraine, tighter global monetary policy and further potential Covid-19 lockdowns in China as additional hurdles. We expect growth of 2.5% in 2023 (2.4% before).

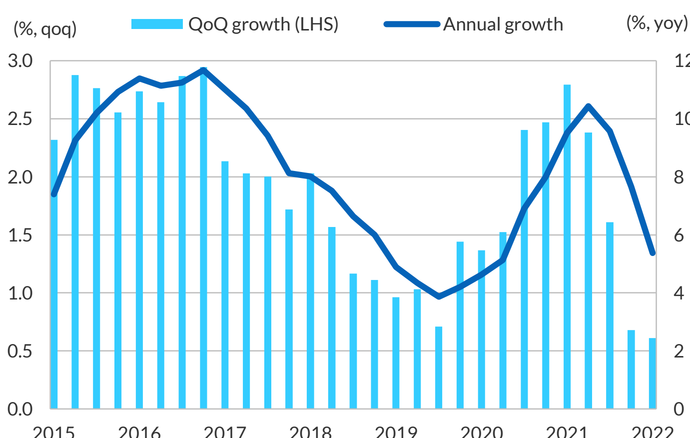
The rate of inflation continues to rise rapidly with producer prices climbing as energy and raw material prices push up manufacturing costs. Households' inflation expectations are also close to a decade high. The Bank of Korea has already lifted policy rates to 1.75% in May and we now see an extra 50bp by end-2022; we then expect rates to remain at 2.25% through 2023.

Korea - GDP Total and Components



Source: Fitch Ratings, Haver Analytics

Korea - Credit to Households



Source: Fitch Ratings, Haver Analytics

Korea - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	2.3	4.1	2.4	2.5	2.6
Consumer spending	1.4	3.7	2.3	2.9	3.1
Fixed investment	2.4	2.8	-1.8	1.9	1.4
Net trade (contribution pp)	0.2	0.9	1.6	0.4	0.6
CPI inflation (end-year)	1.4	3.7	4.2	1.5	1.6
Policy interest rate (end-year)	1.14	1.00	2.25	2.25	2.25
Exchange rate, USDKRW (end-year)	1,144	1,187	1,240	1,180	1,180

Source: Fitch Ratings

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Indonesia

The economy performed better than expected in 1Q22, growing by 5.0% yoy compared with our expectation of 4.0%. In seasonally adjusted quarterly terms, the economy grew by 1.8% qoq (March GEO 0.5% qoq) despite a sharp fall in government spending and an increase in imports, but supported by strong investment. But with slower growth in China and globally, we now expect the economy to grow 5.6% this year (versus 5.9% in our March GEO) with a modest pick-up to 5.8% in 2023. Interest rate increases, a moderation in commodity prices from historical highs over the forecast horizon and the government's aim to reduce the budget deficit could prove to be additional challenges to growth.

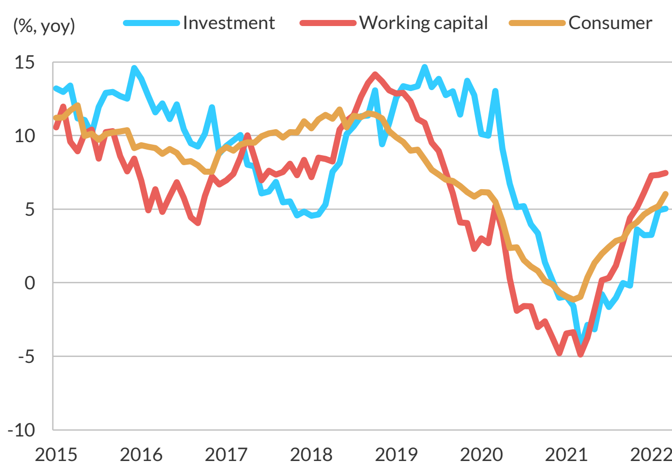
With Omicron variant cases dropping rapidly and restrictions eased, the economy is likely to benefit in the near term from the government's vaccination efforts. Increased protection from the vaccine should stimulate domestic demand with consumers helped by improving labour market dynamics. We expect higher commodity prices – which have boosted export revenues to record levels – as well as the recovery in credit growth to support the economic rebound.

Rising inflation could dent purchasing power, however; CPI reached 3.5% yoy in May, with further increases likely in the near term, though fuel subsidies are limiting the extent to which global energy prices are feeding into CPI. Inflation remains below Bank Indonesia's (BI) 4% upper end of the inflation band but we expect it to rise further this year.

BI has yet to raise rates, currently at 3.5%, and appears reluctant to tighten given its view of inflation as "manageable", which along with a fairly benign growth outlook "reduces the need to respond through interest rates". The central bank instead announced a quicker pace of planned reserve requirement ratio (RRR) increases – to 7.5% in July and 9.0% in September (peak of 6.5% before). Commercial bank lending to all economic sectors grew 6.4% yoy in April as consumers and corporates increased their borrowing, the latter to invest and raise working capital.

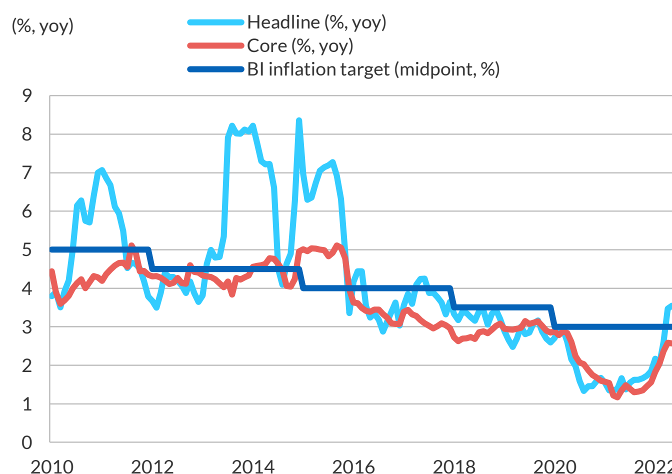
Monetary tightening will be conditioned on the path of core inflation and developments in the rupiah, according to BI. With core inflation unchanged in May and the currency only modestly weaker since the start of the year, this helps explain BI's inaction for now, although this could change as the Fed tightens policy further. We have lowered our policy rate forecast by 25bp this year and next to 4% and 5%, respectively

Indonesia - Bank Lending by Sector



Source: Fitch Ratings, Bank Indonesia, Haver Analytics

Indonesia - Inflation Measures



Source: Fitch Ratings, Badan Pusat Statistik, Bank Indonesia, Haver Analytics

Indonesia - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	3.4	3.7	5.6	5.8	5.8
Consumer spending	2.9	2.0	4.3	5.3	5.0
Fixed investment	3.2	3.8	6.4	5.7	5.7
Net trade (contribution pp)	0.6	1.0	0.4	0.9	0.9
CPI inflation (end-year)	2.7	1.9	3.9	3.0	3.0
Policy interest rate (end-year)	4.61	3.50	4.00	5.00	5.25
Exchange rate, USDIDR (end-year)	14,131	14,269	14,750	14,750	14,750

Source: Fitch Ratings

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Mexico

The economy showed improved momentum in 1Q22, following a rather weak performance in 2021. Monthly economic indicators have continued to improve in recent months. Consumption has recovered to above pre-pandemic levels due to labour market improvement, robust remittances and easing of lockdown measures, although services consumption lags behind. Private investment reached pre-pandemic levels but remains 13% below its most recent peak.

Fitch expects real GDP growth will slow to 1.8% in 2022 (compared with 2.0% in the March GEO) and 1.9% in 2023. Real GDP will not reach pre-pandemic levels until 2023, lagging behind regional peers. The limited fiscal impulse through the pandemic and an early reversal of the monetary policy easing has restrained the economic recovery as authorities prioritise macroeconomic stability.

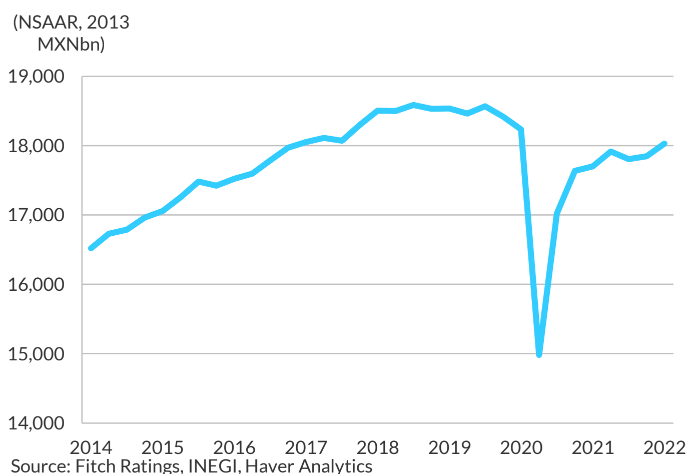
Growth prospects are further hindered by sluggish investment, a trend which is partly related to political noise and regulatory uncertainty. Most recently, the government's intention for higher state intervention in the energy sector has affected business confidence despite the dismissal by congress of the constitutional reform on the electricity sector.

Adverse global conditions are also affecting economic prospects, including higher energy prices and supply-chain disruptions. External demand from the US will remain supportive (including remittance receipts), but on a lesser scale than in 2021.

Inflation has accelerated to levels not seen since 2001 due to higher commodity prices, supply-chain disruption and pandemic-related demand shifts. Not only is headline inflation higher, but it is broadening as core inflation has also increased steadily, including non-food-related goods and services. The government has implemented several programmes to limit the social impact of inflation, including fiscal stimulus to prevent gasoline price increases and commitment with the private sector for price stability on 24 staple items. Stable gasoline prices have prevented inflation reaching even higher levels but we expect limited success from other government programmes.

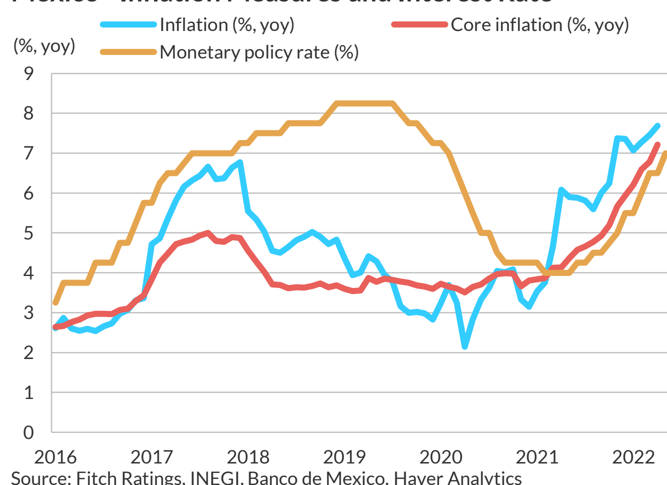
We project Mexico's central bank will continue its policy tightening given the persistence of high inflation and to avoid further contaminating inflation expectations. Policy rates are now likely to increase to 8.5% in 2022 (a 250bp increase through the year) and then by a further 50bp in 2023, taking rates well above our earlier forecasts of 7% and 7.5%, respectively

Mexico - Real GDP



Source: Fitch Ratings, INEGI, Haver Analytics

Mexico - Inflation Measures and Interest Rate



Source: Fitch Ratings, INEGI, Banco de Mexico, Haver Analytics

Mexico - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	0.2	4.8	1.8	1.9	1.9
Consumer spending	0.6	7.4	2.2	1.6	1.6
Fixed investment	-2.6	10.0	2.3	2.8	3.2
Net trade (contribution pp)	0.0	-2.2	1.3	0.2	0.1
CPI inflation (end-year)	4.7	7.4	5.3	4.2	3.5
Policy interest rate (end-year)	6.43	5.50	8.50	9.00	8.50
Exchange rate, USDMXN (end-year)	19.84	20.58	20.00	21.00	21.00

Source: Fitch Ratings

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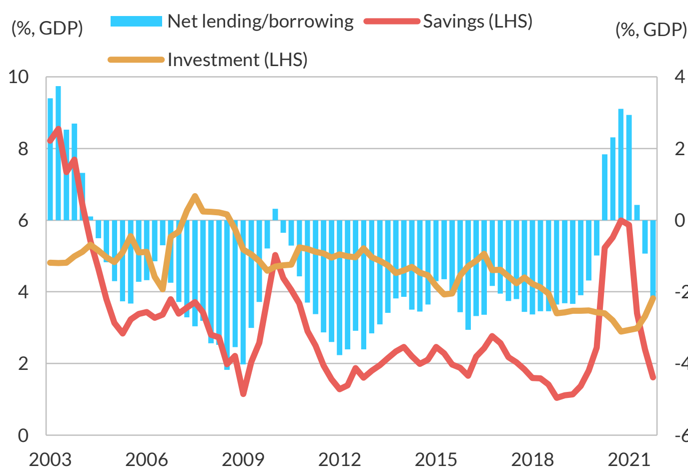
Poland

The Polish economy grew very strongly in 1Q21 despite an unfavourable backdrop of high inflation and war in neighbouring Ukraine. The 2.5% qoq jump in GDP (March GEO 0.2% qoq) was driven by an outsized increase in investment and a rebound in consumer spending. A higher starting point means that growth this year is likely to be 5.2% (3.3% before) despite the expected slowing of the economy in coming quarters. The impact on real incomes from accelerating inflation, tighter monetary policy, trade disruption, and rising economic uncertainty, among other factors, are likely to be responsible for this moderation. For 2023, we expect the economy to grow 3% (3.3% previously) and 2.3% in 2024.

Consumer sentiment remains supported by favourable labour market dynamics with strong demand for labour, resulting in the registered unemployment rate falling to 5.2% in April and wage growth rising at a strong annual rate of 12% in March from 8% a year ago. The large influx of Ukrainian refugees, totalling 3.5 million according to UN estimates, is also expected to boost consumption. There is some upside from faster absorption of Next GenerationEU (NGEU) funds – which were approved for Poland in early June, and which Fitch had already included in its forecasts.

Strong consumer expenditure, boosted by fiscal spending, high imported costs and a positive output gap are putting upward pressure on prices. Following cuts to indirect taxes (VAT, excise duty), the government is also planning a further reduction in direct taxes (personal income tax rate to be cut to 12% from 17%). It will be accompanied by higher fiscal spending on defence and refugees (education, healthcare, social protection). Second-round effects on inflation from rising wages are increasing pressure on the central bank to continue tightening policy. Moreover, the recent rise in costs of energy, materials, transport and labour is not yet fully reflected in consumer prices. We have raised our inflation forecast to 11% at end-2022 and 7.5% in late-2023. The government has offered additional aid to farmers and domestic businesses suffering in response to higher fertiliser and fuel costs. We now expect the National Bank of Poland to raise policy rates to 7.0% by end-2022 (March GEO forecast of 5%) and to 6.5% by end-2023 (5% before).

Poland - Households



Source: Fitch Ratings, ECB, CSO of Poland, Haver Analytics

Poland - Labour Market

Source: Fitch Ratings, CSO of Poland, Haver Analytics

Poland - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	3.7	6.0	5.2	3.0	2.3
Consumer spending	3.2	6.1	3.0	3.1	2.0
Fixed investment	3.7	3.9	11.6	4.5	4.0
Net trade (contribution pp)	0.1	-1.5	-3.2	-0.4	-0.1
CPI inflation (end-year)	2.9	8.7	11.0	7.5	4.0
Policy interest rate (end-year)	1.06	1.75	7.00	6.50	5.25
Exchange rate, USDPLN (end-year)	3.80	4.06	4.25	4.00	4.00

Source: Fitch Ratings

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Turkey

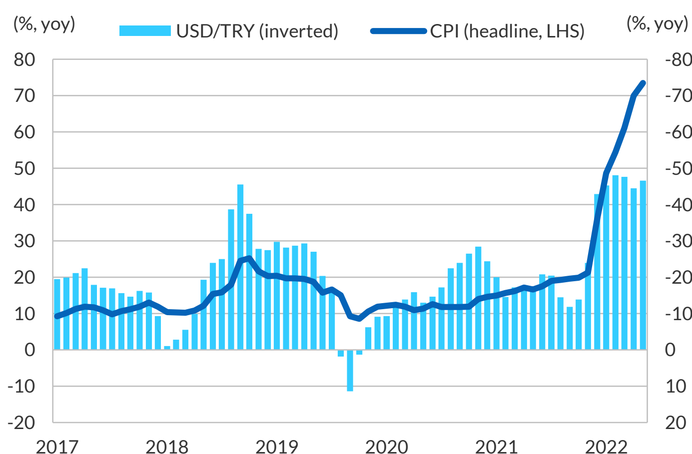
The economy performed much better than we expected in 1Q22, with activity increasing 1.2% qoq against an expectation of -1.3% qoq. Growth was helped by a boost from net trade as imports declined at a sharper pace than exports while investment provided additional support. Consumer spending declined as surging inflation – driven by the collapse in the lira and high commodity prices – dented households' purchasing power.

Since the previous GEO, headline inflation has risen by 20pp to 73.5% in May with strong pipeline pressures, as shown by the surge in producer prices to 132% yoy, likely to keep CPI inflation extremely high in coming months. Core inflation, which excludes more volatile items, such as energy, food and tobacco, is also reaching new heights with an annual jump to 56% yoy. Renewed weakness in the lira against the US dollar in early June will also add to adverse inflation dynamics. While inflation is forecast to peak this year and begin to ease, we still expect CPI inflation to end the year at around 60%.

Despite this rapidly deteriorating picture for inflation, the Central Bank of the Republic of Turkey (remains committed to keeping policy rates at 14%, and President Recep Tayyip Erdogan recently said that interest rate cuts could be forthcoming. Low interest rates and a weak currency form a key part of the government's new economic model, which aims to boost competitiveness and reduce the country's current account deficit. However, we expect that with inflation rising and the currency likely to weaken further, the central bank will raise policy rates, presumably after next year's general elections. We have pencilled in an increase to 19% by end-2023.

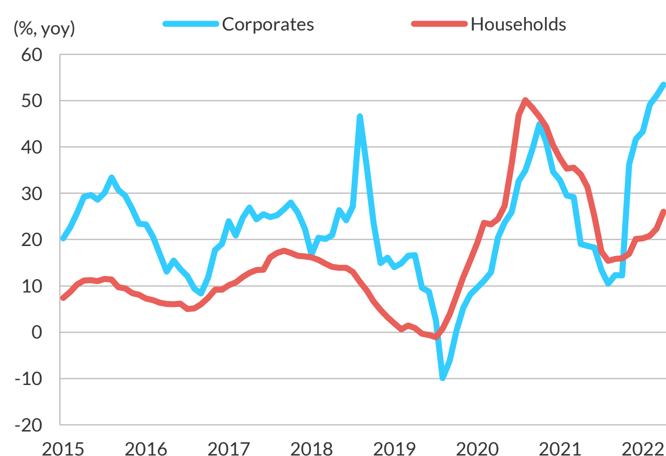
We are upgrading 2022 GDP growth to 4.5% from 2.4%, largely as a result of the strong economic performance in 1Q22, while also lowering 2023 to 3% from 3.2%. We expect economic activity for the remainder of 2022 to lose momentum given the expected deterioration in purchasing power (as inflation remains elevated), increased FX volatility, a less supportive global backdrop with tightening global central bank policies, lower growth in the EU (Turkey's main trading partner) and heightened geopolitical risks. Bank lending to households and corporates continues to recover after troughing in late-2021.

Turkey - Inflation and the Lira



Source: Fitch Ratings, Haver Analytics

Turkey - Total Lending to Corporates and Households



Source: Fitch Ratings, Haver Analytics

Turkey - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	4.8	11.0	4.5	3.0	2.9
Consumer spending	5.3	15.1	8.4	2.2	2.5
Fixed investment	1.8	6.4	1.9	3.7	2.9
Net trade (contribution pp)	1.1	4.9	1.1	0.1	0.0
CPI inflation (end-year)	14.9	36.1	60.0	55.0	50.0
Policy interest rate (end-year)	14.37	14.00	14.00	19.00	19.00
Exchange rate, USDTRY (end-year)	6.00	12.99	20.00	21.00	22.00

Source: Fitch Ratings

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South Africa

We have raised our 2022 economic growth forecast for South Africa to 2.3%, from 1.7% in the March GEO. The economy surpassed its pre-pandemic level in 1Q22 after quarterly growth came in above expectations at 1.9%, driven by strong investment and manufacturing activity. Despite this, further growth in 2022 will be dampened by the impact of the conflict in Ukraine, lockdowns in China, and persistent severe electricity shortages.

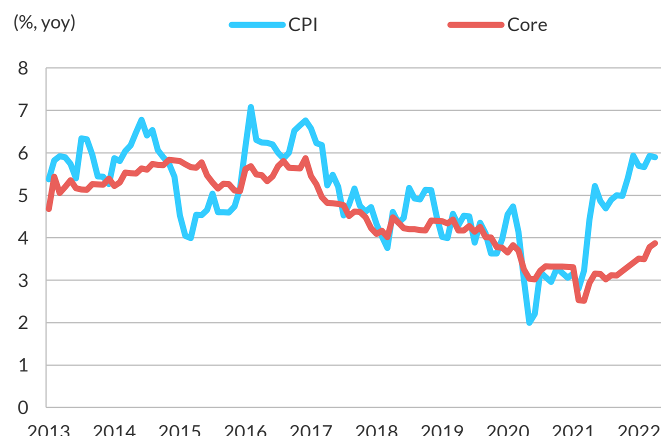
The outlook for industrial production in 2022 is weak. The ABSA/BER manufacturing PMI index fell sharply in April, reaching its lowest since July 2021, as activity was hit by the flooding in KwaZulu-Natal – the second largest province by GDP – along with ongoing power cuts. The PMI index picked up in May, but power cuts, high costs, and supply problems are likely to restrict output, alongside weaker growth in China and the eurozone. We expect the economy to contract in 2Q22 as a result.

High unemployment coupled with strong inflation will also limit consumer spending this year. The BER consumer confidence index fell in 1Q22, reflecting households' weaker assessment of the economic and financial outlook. Inflation remained elevated at 5.9% in April, driven by high global energy and food prices. We expect rising electricity and fuel prices to add to inflationary pressure. High input costs and supply-chain frictions are also raising producer prices, and shortages of skilled workers are likely to put upward pressure on wages, which will keep core inflation elevated throughout the forecast horizon. As such, we expect inflation to end 2022 above 6%, and have also raised our end-2023 forecast to 5.1% from 2.1%.

We now expect the South African Reserve Bank to be more aggressive in taming inflation. We anticipate a further 100bp in increases in 2022, to take rates to 5.75% by year-end, followed by 50bp in hikes early next year to take rates to 6.25%. The higher interest rate outlook will be another hurdle for household and business activity over the forecast horizon.

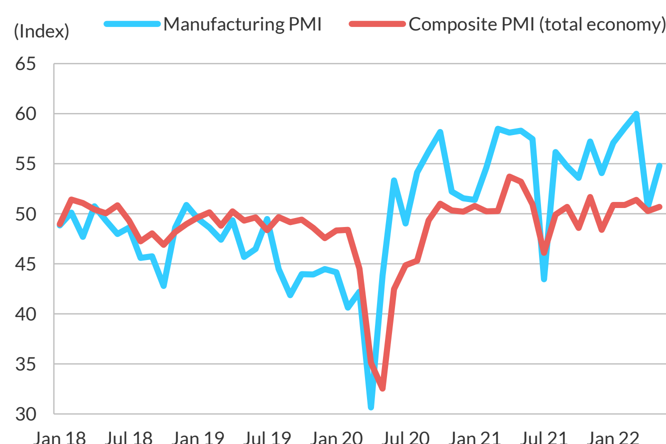
Given the weaker global growth outlook next year, alongside stronger inflation and higher rates in South Africa, we have also reduced our forecast for economic growth in 2023 to 2.0% from 2.5%.

South Africa - Inflation



Source: Fitch Ratings, Statistics South Africa, Haver Analytics

South Africa - PMI Balances



Source: Fitch Ratings, BER, S&P Global, Standard Bank, Haver Analytics

South Africa - Forecast Summary

(%)	Annual Avg. 2017-2021	2021	2022F	2023F	2024F
GDP	0.3	4.9	2.3	2.0	1.7
Consumer spending	1.1	5.6	2.9	1.9	1.6
Fixed investment	-4.0	0.2	4.2	2.4	2.6
Net trade (contribution pp)	0.0	0.1	-0.9	0.3	0.2
CPI inflation (end-year)	4.4	5.9	6.2	5.1	4.5
Policy interest rate (end-year)	5.57	3.75	5.75	6.25	6.25
Exchange rate, USDZAR (end-year)	14.45	15.91	16.10	16.60	16.80

Source: Fitch Ratings

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Appendix 1

Quarterly GDP QOQ

(%)	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23
US	1.5	1.6	0.6	1.7	-0.4	1.0	0.7	0.6	0.2	0.1
Eurozone	-0.1	2.2	2.3	0.2	0.6	0.0	0.2	0.1	0.6	0.8
China	0.5	1.2	0.7	1.5	1.3	-1.5	1.6	4.6	0.5	0.6
Japan	-0.4	0.6	-0.8	1.0	-0.1	1.3	1.2	0.4	0.2	0.2
UK	-1.2	5.6	0.9	1.3	0.8	0.3	0.2	0.0	0.4	0.4
Germany	-1.7	2.2	1.7	-0.3	0.2	0.0	0.4	0.5	0.6	0.7
France	0.2	1.0	3.2	0.4	-0.2	0.2	0.5	0.4	0.6	0.6
Italy	0.2	2.7	2.6	0.7	0.1	0.0	0.3	0.2	0.5	0.6
Spain	-0.5	1.1	2.6	2.2	0.3	0.2	0.8	0.7	0.9	0.9
Switzerland	-0.2	2.0	1.9	0.2	0.5	0.2	0.6	0.5	0.6	0.4
Australia	1.8	0.8	-1.8	3.6	0.8	0.7	1.0	0.9	0.6	0.4
Canada	1.1	-0.8	1.3	1.6	0.8	1.0	0.8	1.0	0.4	0.3
Brazil	1.1	-0.2	0.1	0.7	1.0	0.1	-0.2	0.1	0.3	0.4
Russia	1.8	1.4	0.1	1.5	0.1	-8.8	-6.7	1.3	1.2	1.7
India	1.6	-11.5	13.2	3.3	0.5	0.9	0.7	1.7	1.8	1.9
Korea	1.7	0.8	0.2	1.3	0.6	0.1	0.3	0.7	0.8	0.7
Mexico	0.4	1.2	-0.6	0.2	1.0	0.4	0.4	0.4	0.5	0.6
Indonesia	1.7	0.5	0.2	2.5	1.8	1.0	1.2	1.5	1.6	1.5
Turkey	2.2	1.7	2.8	1.5	1.2	0.5	-0.5	0.7	1.1	1.1
Poland	1.4	2.0	2.6	1.8	2.5	-0.7	0.0	0.3	1.3	1.1
South Africa	0.8	1.4	-1.8	1.4	1.9	-0.4	0.3	0.4	0.6	0.6
Developed [a]	0.6	1.7	0.8	1.3	-0.1	0.8	0.7	0.5	0.4	0.3
Emerging [b]	0.9	-0.2	1.9	1.6	1.1	-1.2	0.6	3.0	0.7	0.9
Emerging ex-China	1.5	-2.0	3.4	1.7	0.9	-0.9	-0.7	0.9	1.1	1.2
World [c]	0.7	1.0	1.2	1.4	0.4	0.0	0.7	1.5	0.5	0.5

[a] US, Japan, France, Germany, Italy, Spain, UK, Canada, Australia and Switzerland
[b] Brazil, Russia, India, China, South Africa, Korea, Mexico, Indonesia, Poland and Turkey
[c] 'Fitch 20' countries weighted by nominal GDP in US dollars at market exchange rates (three-year average)
Source: Fitch Ratings

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Appendix 2

Quarterly GDP YOY

(%)	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23
US	0.5	12.2	4.9	5.5	3.5	2.9	3.0	2.0	2.6	1.7
Eurozone	-0.9	14.7	4.0	4.7	5.4	3.2	1.1	0.9	1.0	1.8
China	18.3	7.9	4.9	4.0	4.8	2.0	3.0	6.1	5.2	7.5
Japan	-1.7	7.4	1.2	0.4	0.7	1.4	3.4	2.8	3.1	2.0
UK	-5.0	24.5	6.9	6.6	8.7	3.3	2.5	1.1	0.8	0.9
Germany	-2.8	10.3	2.9	1.8	3.8	1.5	0.3	1.1	1.4	2.2
France	1.8	19.2	3.0	4.9	4.5	3.6	0.9	0.8	1.6	2.1
Italy	0.0	17.5	4.0	6.4	6.2	3.4	1.0	0.5	0.9	1.6
Spain	-4.1	17.8	3.5	5.5	6.4	5.4	3.6	2.1	2.7	3.4
Switzerland	-0.4	8.2	3.9	3.6	4.4	2.7	1.4	1.8	1.9	2.1
Australia	1.4	9.7	4.1	4.4	3.3	3.2	6.2	3.4	3.2	2.8
Canada	0.2	11.7	3.8	3.2	2.9	4.7	4.2	3.5	3.1	2.5
Brazil	1.3	12.3	4.0	1.6	1.7	1.8	1.5	0.9	0.2	0.6
Russia	-0.3	10.5	4.0	5.0	3.5	-7.3	-13.6	-13.8	-12.8	-2.7
India	2.5	20.1	8.4	5.4	4.1	18.5	5.4	3.7	5.1	6.2
Korea	2.2	6.2	4.0	4.2	3.0	2.3	2.4	1.8	1.9	2.5
Mexico	-3.8	19.9	4.5	1.1	1.8	1.1	2.1	2.3	1.8	2.0
Indonesia	-0.7	7.1	3.5	5.0	5.0	5.5	6.5	5.5	5.3	5.8
Turkey	7.3	21.9	7.5	9.1	7.3	6.1	2.7	1.9	1.8	2.4
Poland	-0.6	11.3	5.5	7.6	8.5	6.3	3.6	2.1	0.8	2.7
South Africa	-2.4	19.5	3.0	1.7	3.0	1.0	3.2	2.3	1.0	2.0
Developed [a]	-0.5	13.0	4.1	4.5	3.8	2.9	2.7	1.9	2.3	1.9
Emerging [b]	10.6	10.7	5.1	4.2	4.3	3.4	2.1	3.6	3.2	5.4
Emerging ex-China	1.0	14.3	5.3	4.4	3.7	5.3	1.1	0.3	0.5	2.6
World [c]	3.7	12.1	4.5	4.4	4.0	3.1	2.5	2.5	2.7	3.2

[a] US, Japan, France, Germany, Italy, Spain, UK, Canada, Australia and Switzerland
[b] Brazil, Russia, India, China, South Africa, Korea, Mexico, Indonesia, Poland and Turkey
[c] 'Fitch 20' countries weighted by nominal GDP in US dollars at market exchange rates (three-year average)
Source: Fitch Ratings

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