

## **Barometer Q3 2021: Supply chain and inflation headwinds hamper the global recovery**

**Bucharest, October 26, 2021** – More than 18 months after the global recession triggered by the COVID-19 pandemic started, the economic recovery continues. This trend owes much to progress in the vaccine rollout over the summer, particularly in advanced economies. In turn, this is spurring a rebound in consumption of high-contact services. The situation remains heterogeneous in emerging economies: this rebound is benefitting export-oriented countries, while service-dependent economies continue lagging.

Despite the positive outlook, signs that the global recovery is losing momentum are accumulating. Pandemic outbreaks in critical links of the supply chain have resulted in supply disruptions, feeding price pressures. These disruptions are starting to affect manufacturers' production and sales across the globe. Headwinds represented by supply concerns, labour shortages, and inflation, alongside the lingering threat of COVID-19, add to the list of risks and uncertainties.

In light of the continued recovery, Coface upgraded its risk assessments for 26 countries, including Germany, France, Italy, Spain, Switzerland and Belgium. Strong exports of manufactured goods to advanced markets are prompting upgrades for export-oriented economies in Central and Eastern Europe (Poland, Hungary, Czechia), in Asia (South Korea, Singapore, Hong Kong) and in Turkey. After downgrading 78 country risk assessments last year, these upgrades are in addition to the 16 already implemented in the 1<sup>st</sup> half of 2020. They are accompanied by 30 sectoral assessment upgrades.

### **Progress with the vaccination still supports the recovery**

Global economic trends highlighted in our latest barometer have been largely confirmed in the third quarter. Progress with the vaccination in Western Europe and North America helped to avoid new waves of strict mobility restrictions, and is fuelling optimism that a repetition of last year's lockdowns will be avoided. However the threat of COVID has not disappeared: lower vaccination rates in emerging markets – particularly in low-income countries – still pose the risk of the emergence of variants resistant to currently available vaccines.

The global manufacturing sector has recovered fast since mid-2020, prompted by increased spending on consumer goods. Because of robust households' demand, strong trade flows continue to be a key support for economic growth, notably in Asia-Pacific. Demand for electronics and commodities are indeed benefiting several markets in the region, such as South Korea and Taiwan. The economy of several key commodity exporters (Russia, Ukraine, South Africa, Chile, Algeria, etc.) are also supported by higher prices. In CEE, the region's competitive exports and the wide integration in European supply chains are also supportive of export growth.

In terms of sectoral trends, the easing and lifting of restrictions in countries where vaccination rates are the highest is contributing to a shift of household spending towards high-contact services such as retail, hospitality and recreation. The recovery of the tourism sector remains more challenging.

### **Supply chain issues and inflation hamper the recovery momentum**

Nevertheless, headwinds are accumulating, particularly on the supply-side of the economy. High level of savings in high-income countries prompted a rapid recovery in consumer spending. At the

same time, pandemic disruptions created breaks in the supply chain that are hampering business activity. Competition for commodities and input goods is strong, hindering industrial production at the global level and, in some instances, having an impact on sales. This is notably true for the shortage of semiconductors, which is impacting a wide-array of industries from the automotive to information and communication technologies sectors both in advanced and emerging economies.

Commodity prices, input costs and freight rates have surged since the summer of 2020. Many commodities broke record levels. This has been notably the case with energy – particularly as European and Asian gas prices soared – metals, lumber and food prices. Widespread price increases for commodities and inputs has also translated into increasing consumer prices. The harmonized inflation rate in the Eurozone reached 3.4% in September, the highest level in 13 years. This echoes a rise in inflation observed in most parts of the globe, most notably in the US, where the inflation rate has also been hovering a 13-year high of 5.4% in the last 4 months to September. A peak in inflation is expected soon in advanced economies, but risks are tilted to the upside.

The inflation conundrum could be complicated by reports of labour shortages, as businesses offer higher compensations to fill job vacancies. An increase in labour costs could mean more persistent inflationary pressures. Faced with this risk, some central banks – including the US Federal Reserve and the UK Bank of England - have already signalled that the end of ultra-accommodating monetary policies is approaching. In Europe, while the ECB is closely monitoring the inflation dynamic with concern, tightening remains a more distant prospect. In emerging economies, several central banks had to hike their benchmark policy rates in recent months, due to concerns over rising inflation.

The fiscal side of the equation will remain supportive in advanced economies. In Western Europe, while many national governments will continue to support their economy further until the end of the year, the EU recovery fund (worth EUR 750 billion) will slowly be paid out. In the US, the next steps of the fiscal response are still uncertain, as key parts of President Joe Biden's economic agenda are still being debated in Congress.

### **The Chinese economy is experiencing some turbulence**

Also of importance for the global economy, China's economy showed signs of a slowdown heading into the 2<sup>nd</sup> half of 2021. In the third quarter, GDP was up 4.9% from a year ago, the slowest pace since the third quarter of 2020. On a quarterly basis, activity merely expanded (+0.2%). We forecast China's economy to grow by 7.5% this year, expecting GDP growth to remain low in the last quarter.

Several factors are behind the deceleration in Chinese economic activity: policy tightening in credit growth, softening domestic consumption, and energy rationing for industries. Another factor is related to China's "Dual carbon" goals, leading to the imposition of policies constraining steel production, as the sector accounts for around 15% of the country's carbon emissions. As a result, the volume of monthly steel output has been falling from nearly 100 million tonnes in May to 83.2 million in August, with further steel output cuts are expected in 2021.

Considering the role of China in international trade and in regional supply chains, an economic slowdown would pose significant downside risks to Asian economic activity, but also in other emerging markets in Latin America, Middle East and Africa.



P R E S S R E L E A S E

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