

Inflation: Here to stay?

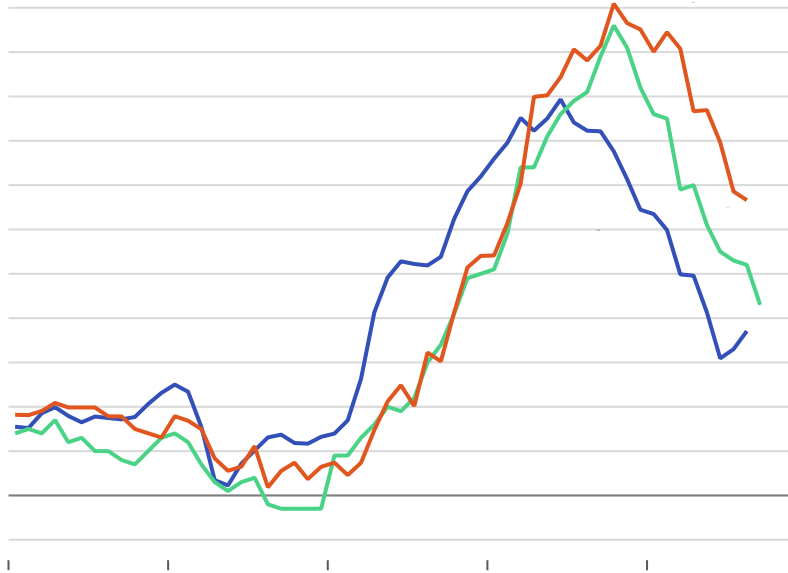
AAE Annual Meeting

06 October 2023
Michael Menhart
Chief Economist

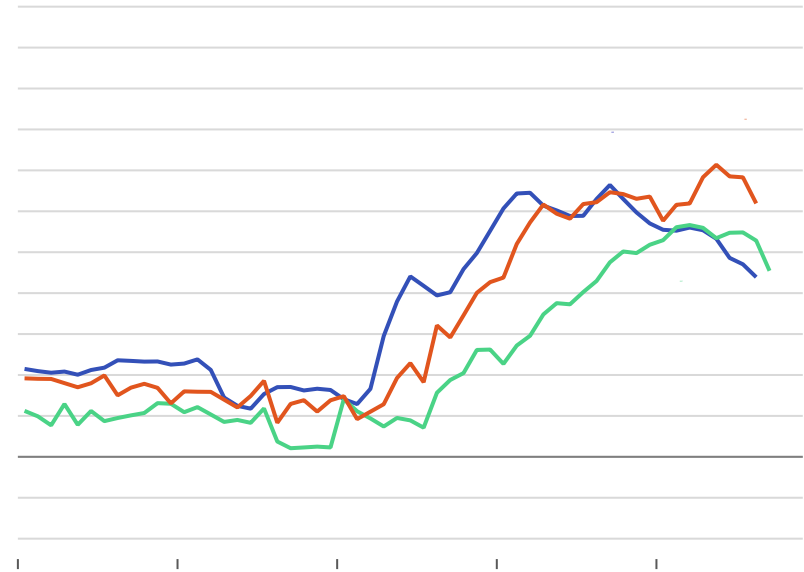
Munich RE 

Headline inflation has eased due to energy price (base) effects – but decline now faltering and core inflation trends remain concerning

Headline inflation
(CPI all items, y/y, in %)

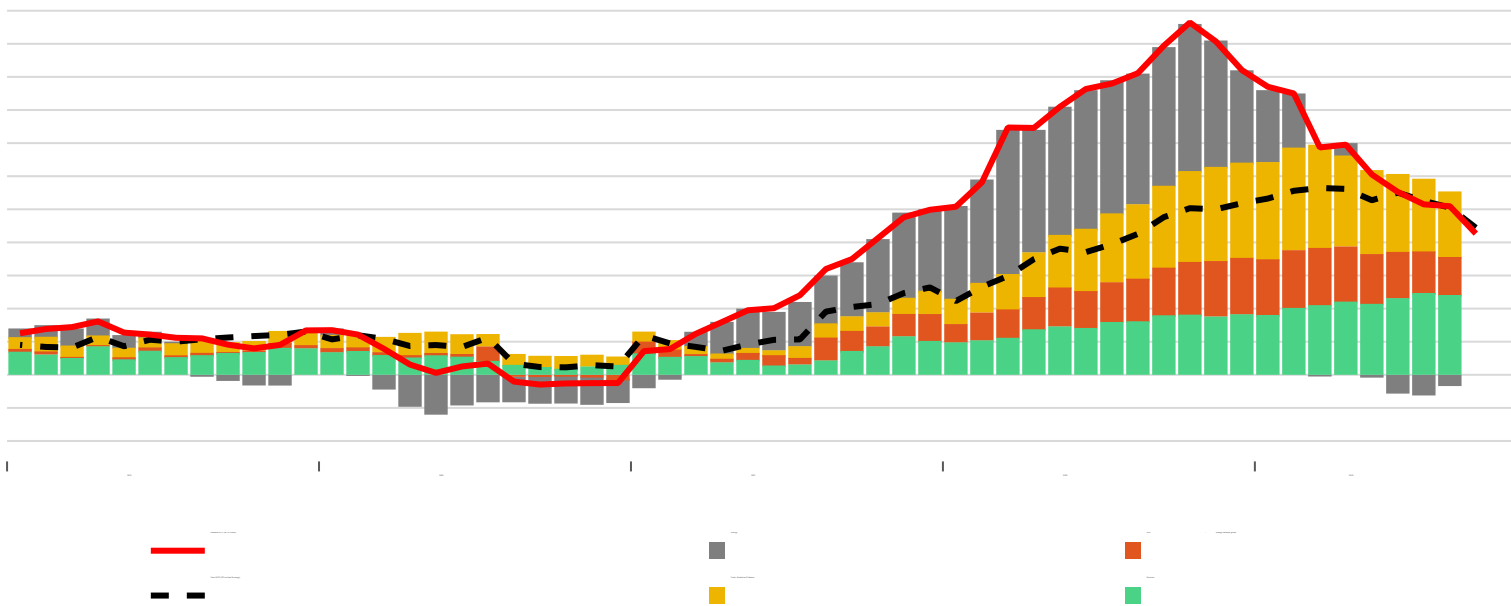


Core inflation
(CPI excluding food and energy, y/y, in %)



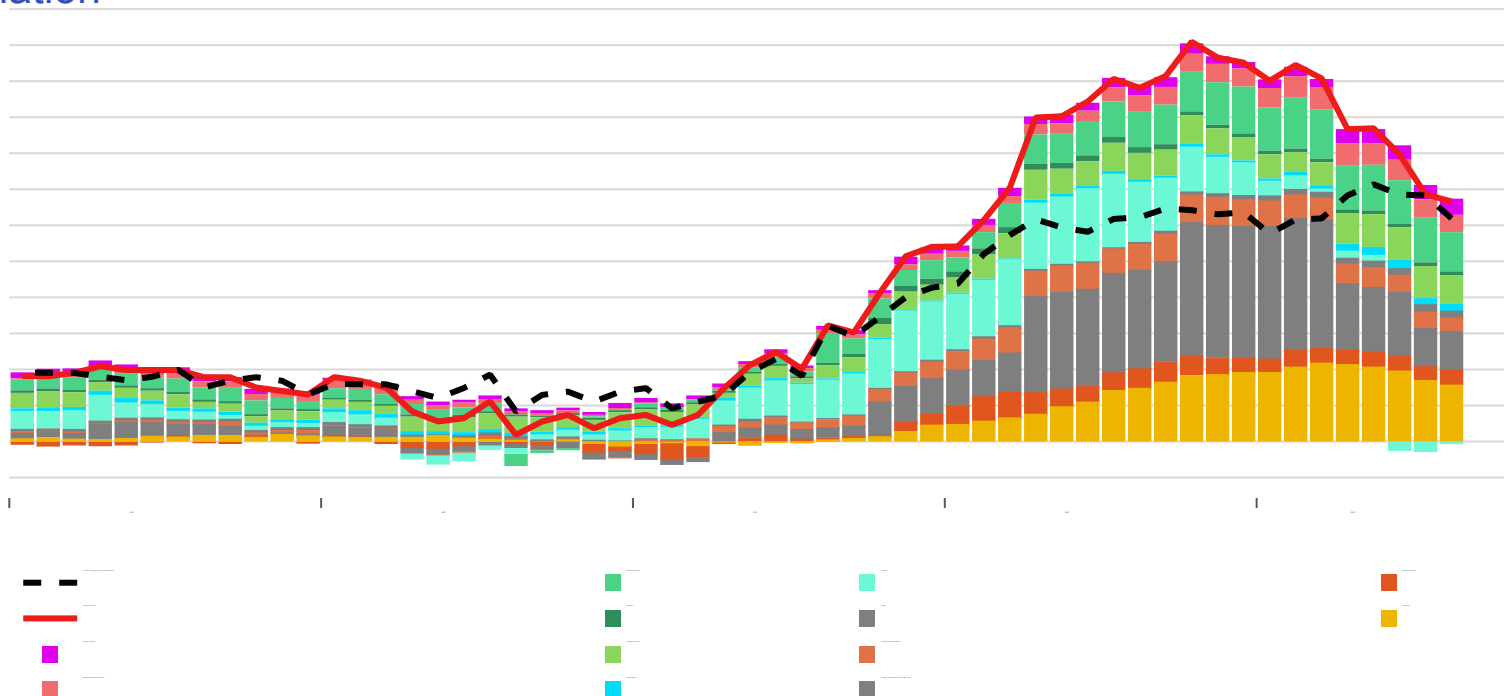
Euro area inflation still “broad”: driven by food, industrial goods and services price increases

Euro area: y/y inflation (in %) and contribution to inflation (in %-points); memo: core inflation

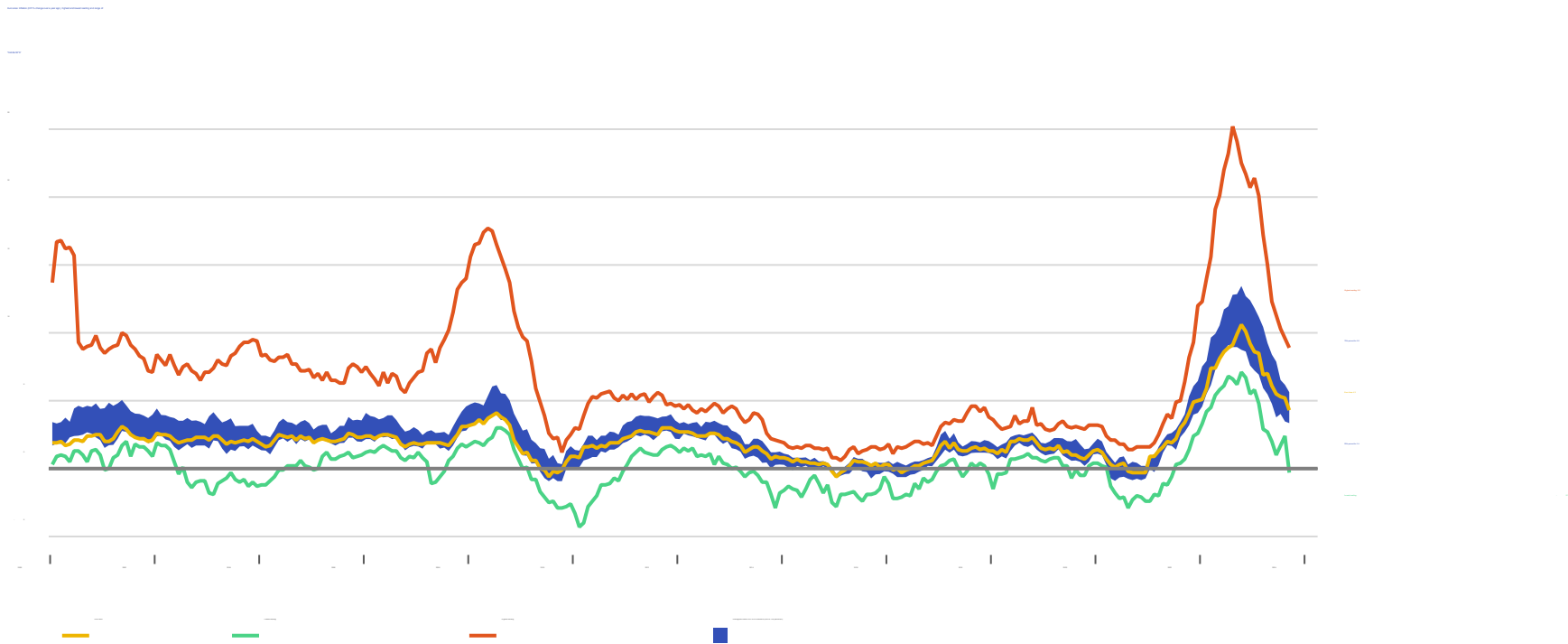


Core inflation in the UK higher than in Eurozone and quite stagnant for a longer period of time

United Kingdom: y/y inflation (in %) and contribution to inflation (in %-points); memo: core inflation

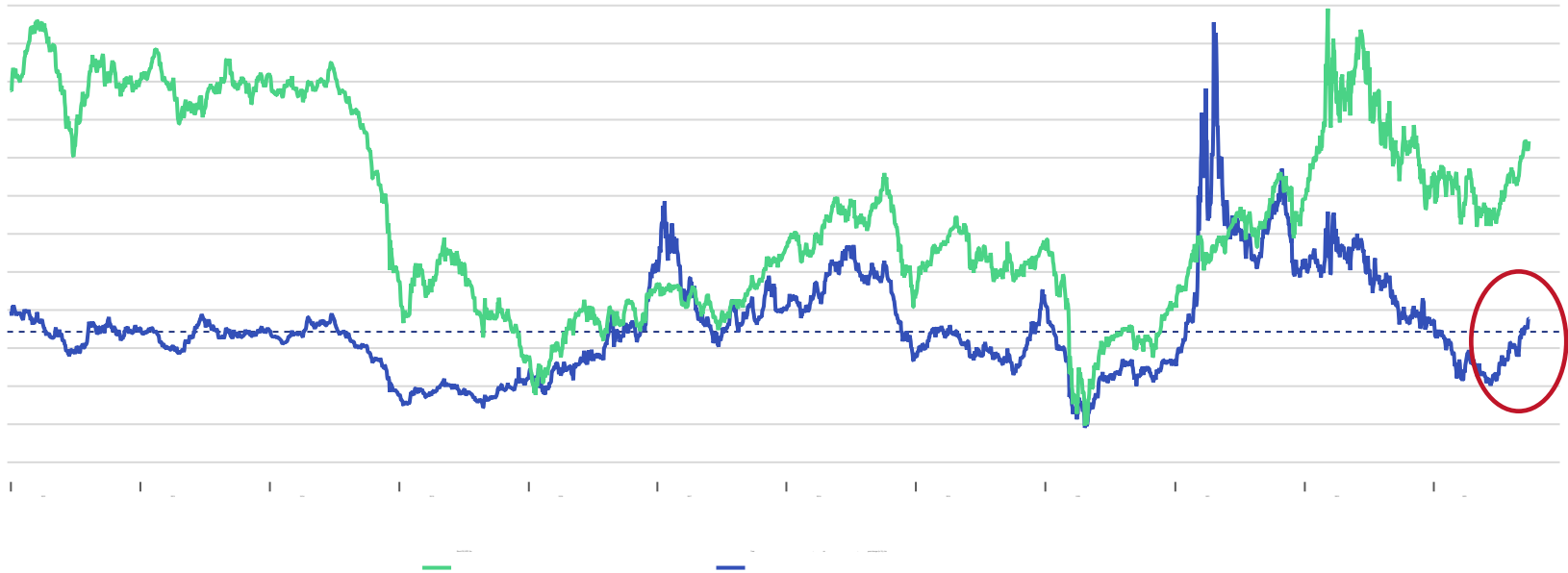


There is still a high range of national inflation rates among Eurozone members



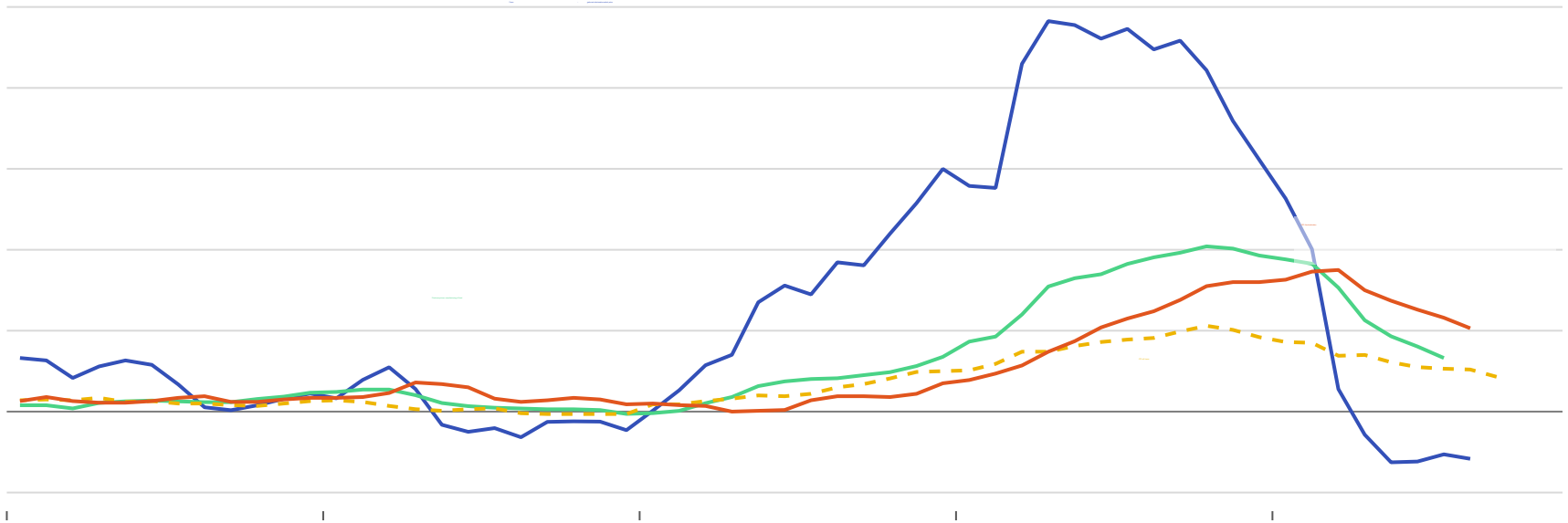
With the recent rise in oil prices, there is no disinflationary impulse from oil anymore – at least for now

Oil price (left-hand scale: USD/barrel, right-hand scale: y/y change in %)



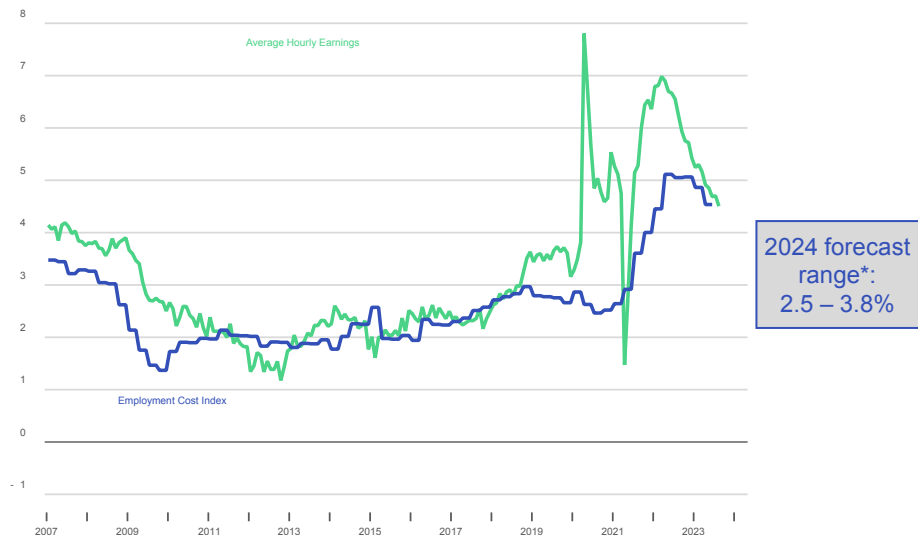
While food prices for consumers are expected to follow the decrease in wholesale food prices ...

Euro area: Farm-gate prices, food commodity prices, food manufacturer prices and consumer prices (y/y, in %)



... strong wage growth is likely to result in services price increases – wage growth rates in US softening, in EZ rising

US: Wage and employment cost inflation (y/y, in %)



Source: BLS (2023)

Eurozone: Wage and labour cost inflation (y/y, in %)

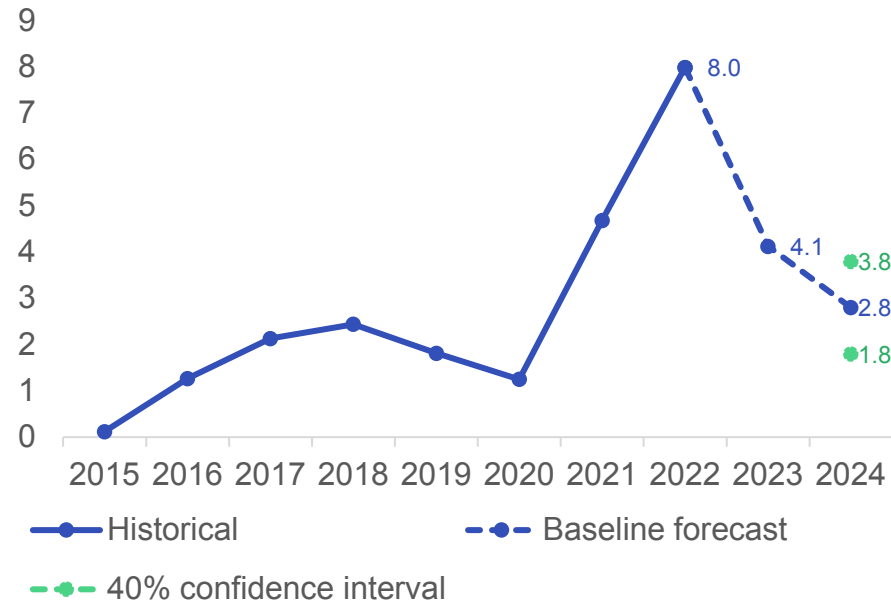


Source: ECB, Eurostat (2023 Q3)

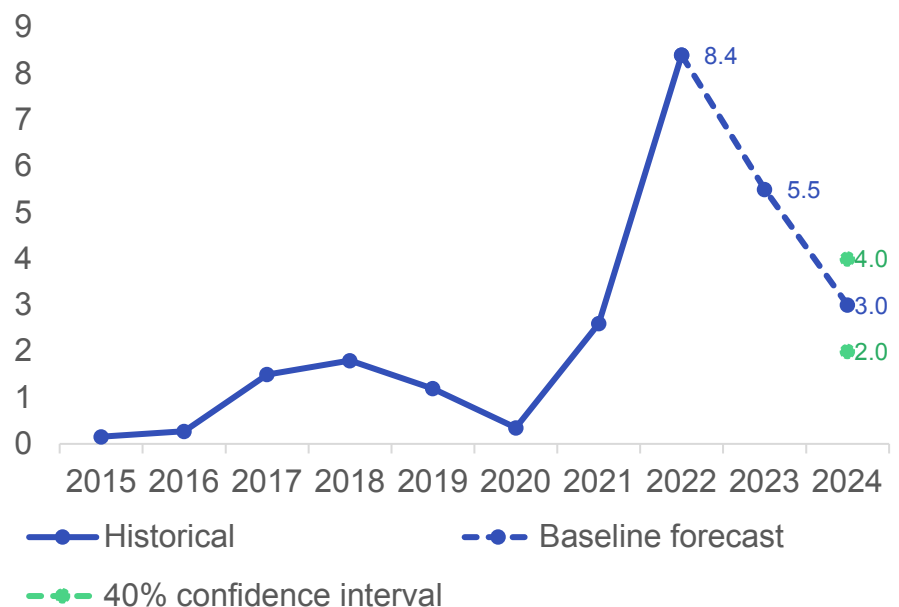
* Consensus forecasts, for euro area also ECB forecasts

Outlook 2024/2025 US and euro area: Inflation expected to ease but forecast uncertainty still high

US annual inflation (CPI change y/y in %):
baseline forecast and confidence intervals
based on historical forecast errors

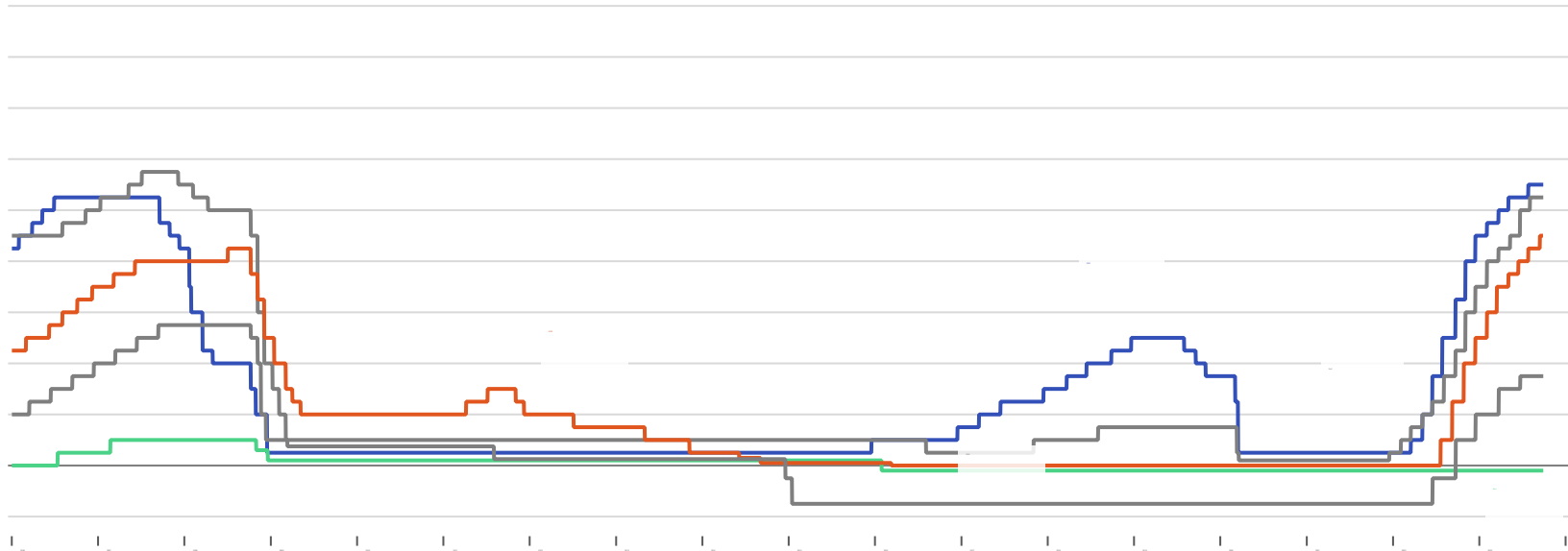


EZ annual inflation (CPI change y/y in %):
baseline forecast and confidence intervals
based on historical forecast errors



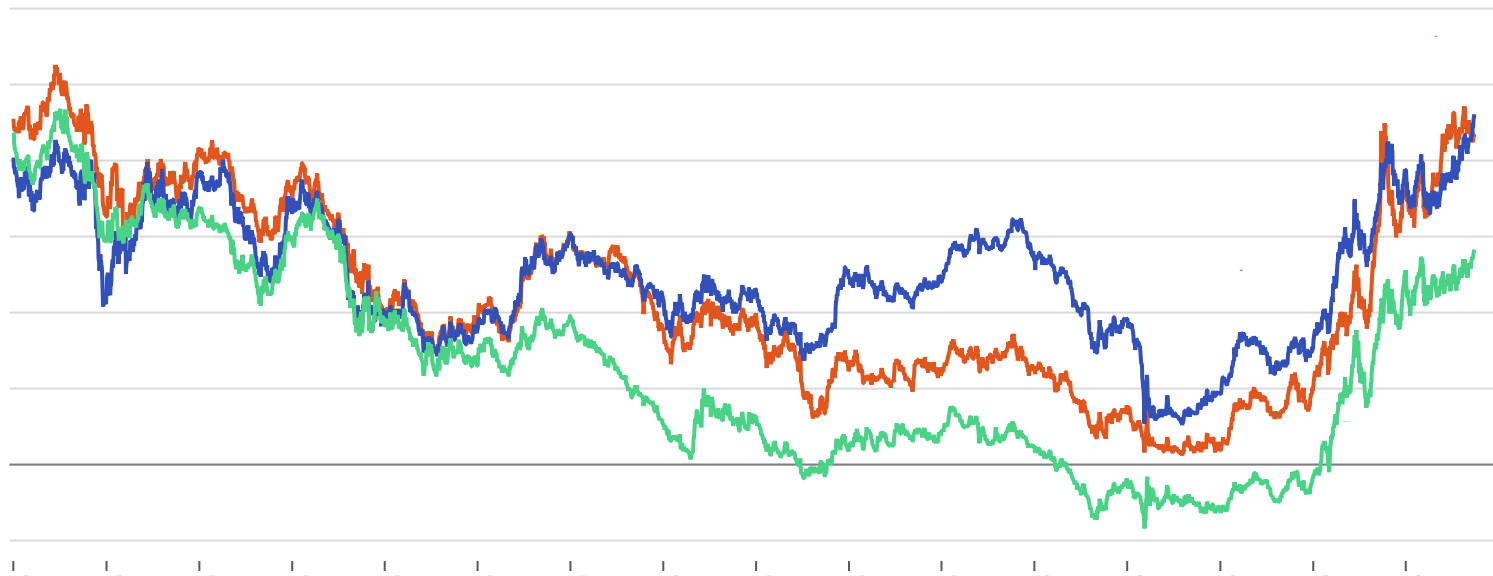
Monetary tightening in most advanced economies with different beginning and hawkishness

Central banks' key interest rates (in %)



Bond yields have increased sharply on the back of monetary tightening

10-year government bond yields (in %)



Consensus forecasts for end of Sept. '24:

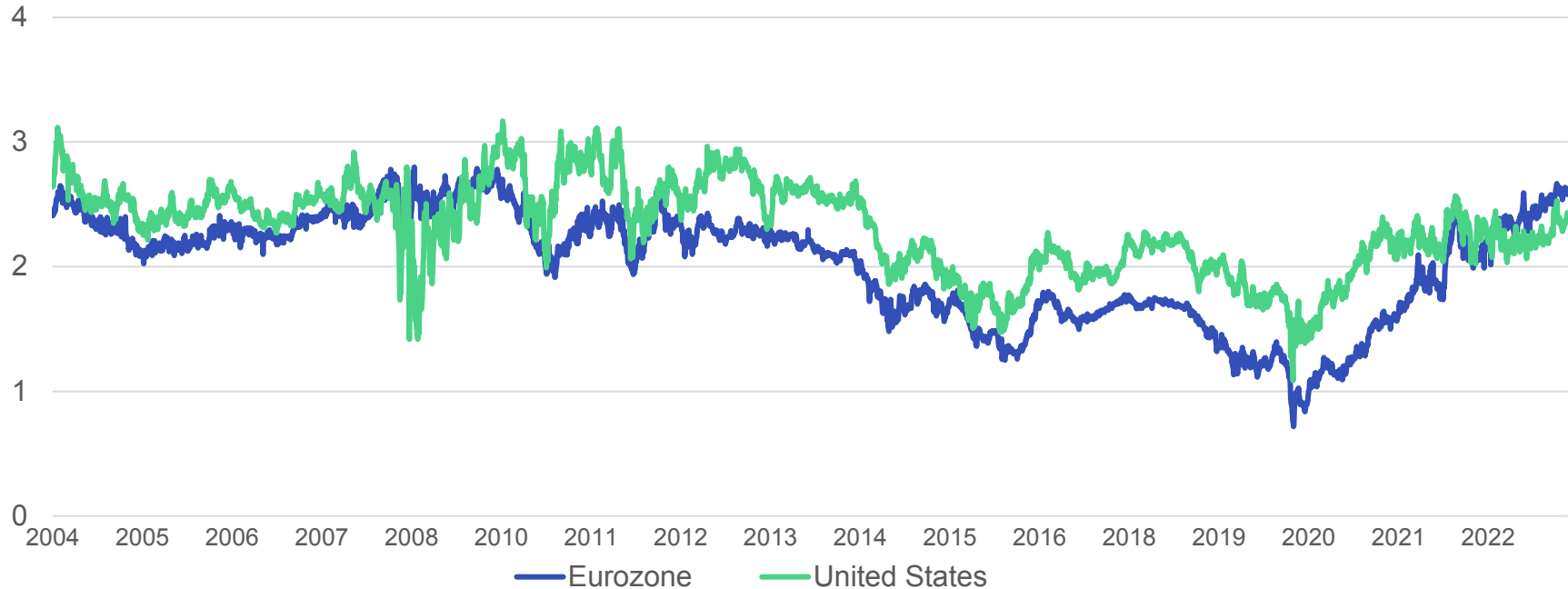
4.3

3.6

2.3

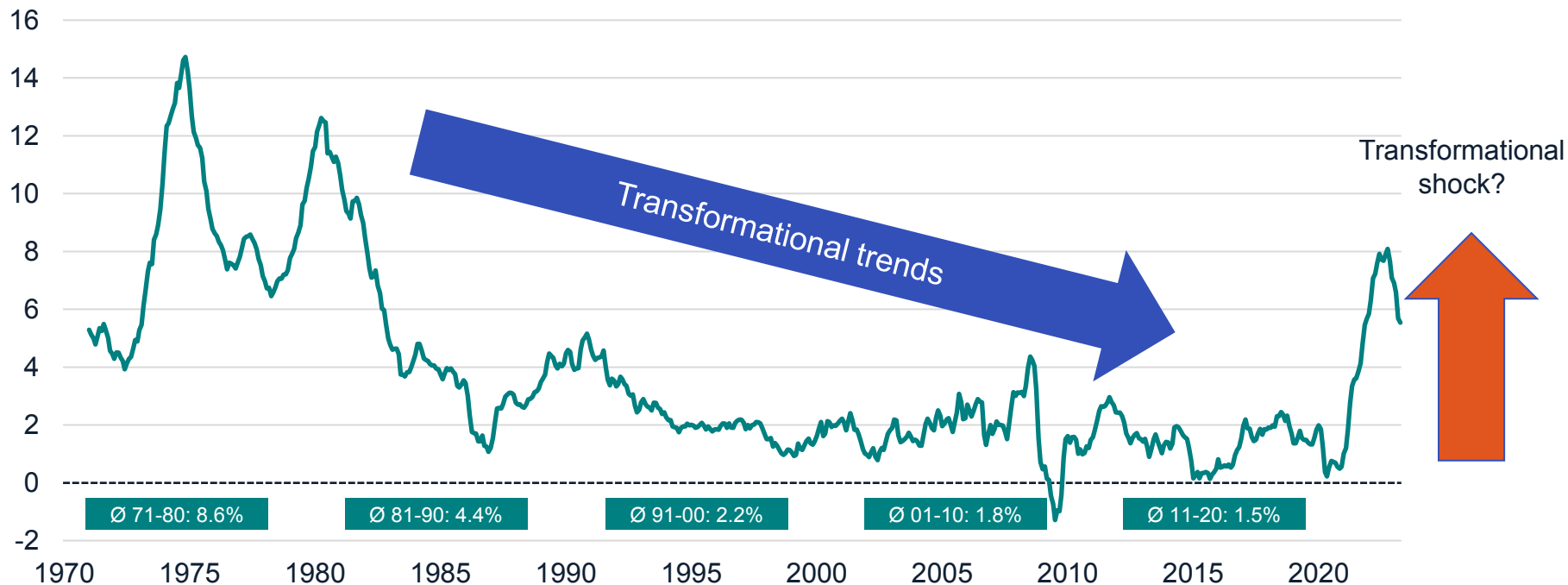
Inflation expectations for the US and the Eurozone have recently increased strongly

Market-based inflation expectations (5-year/5-year forward, in %)



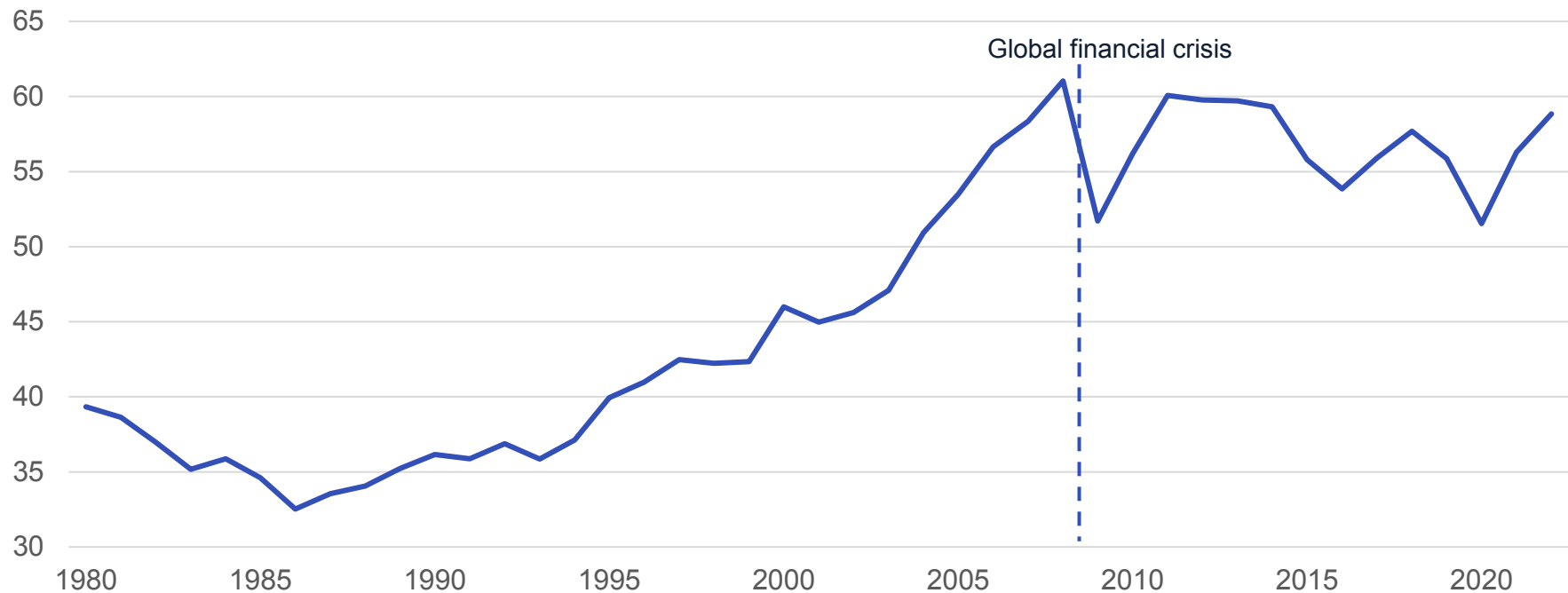
After four decades of lower inflation – will we see a high inflation environment?

Inflation, average of G7 economies (y/y CPI change, in %)



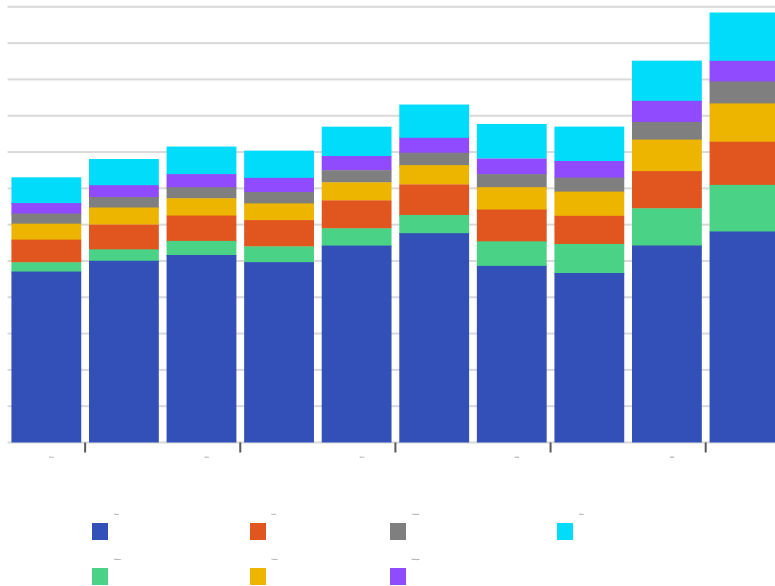
From “hyper globalisation” to “slowbalisation”

Global trade in goods and services (in % of global GDP)

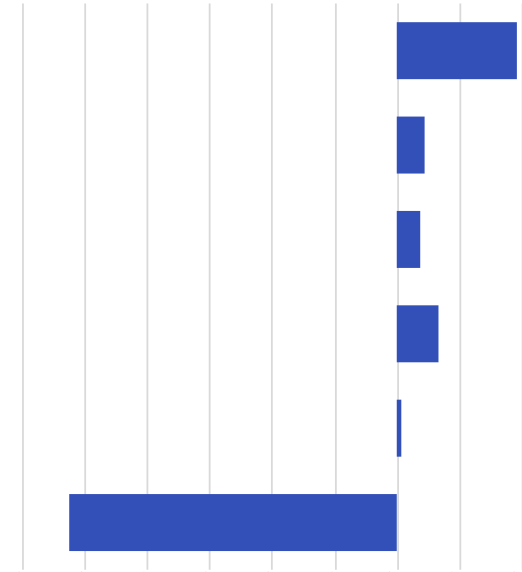


Trade diversion: US imports more from other Asian low-cost economies, Chinese import share has been reduced

US imports from selected Asian countries
(in tn USD)

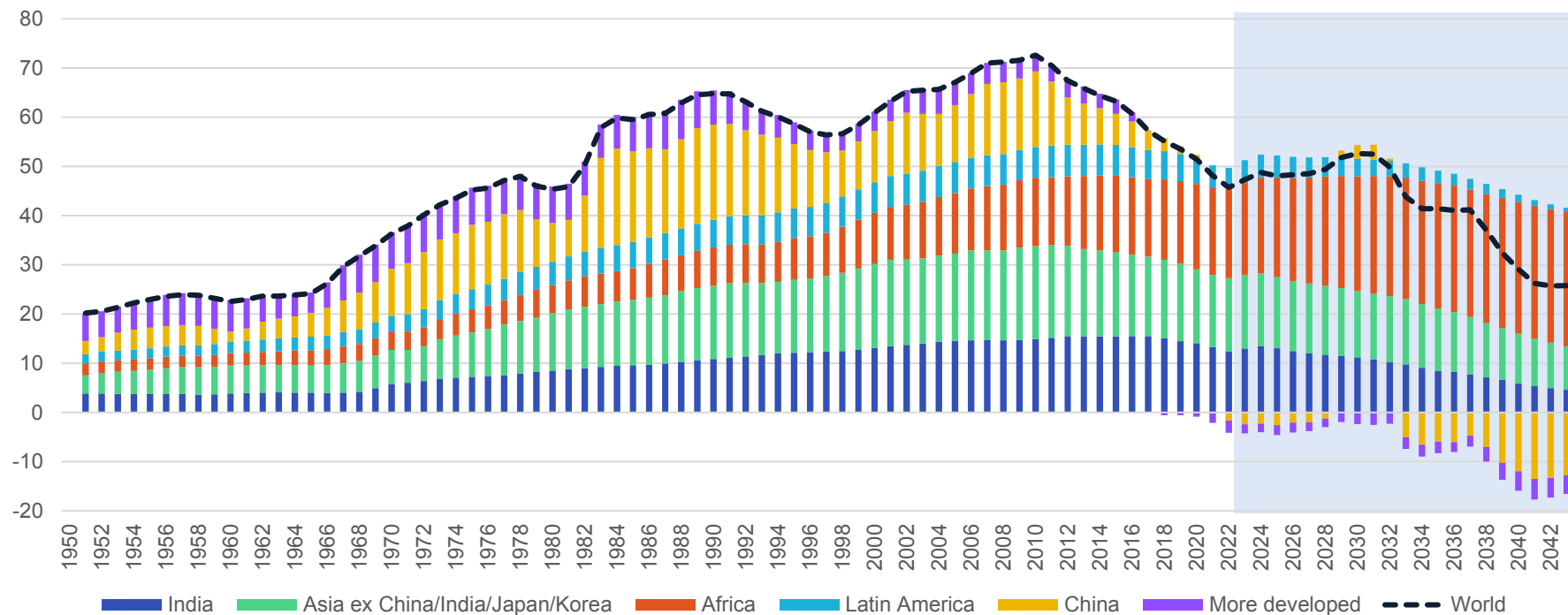


Change in share of US imports: 2022
compared to 2018 (in %-points)



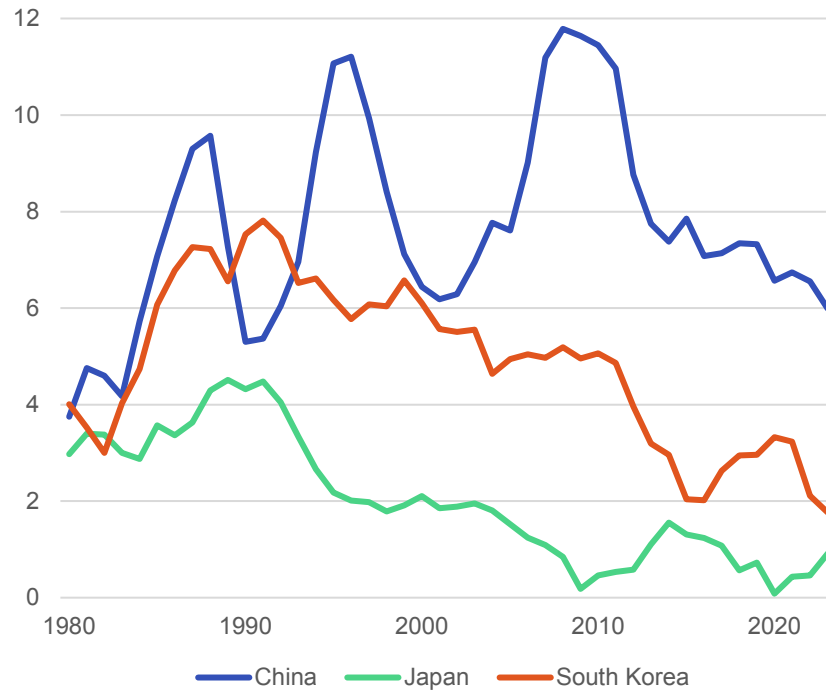
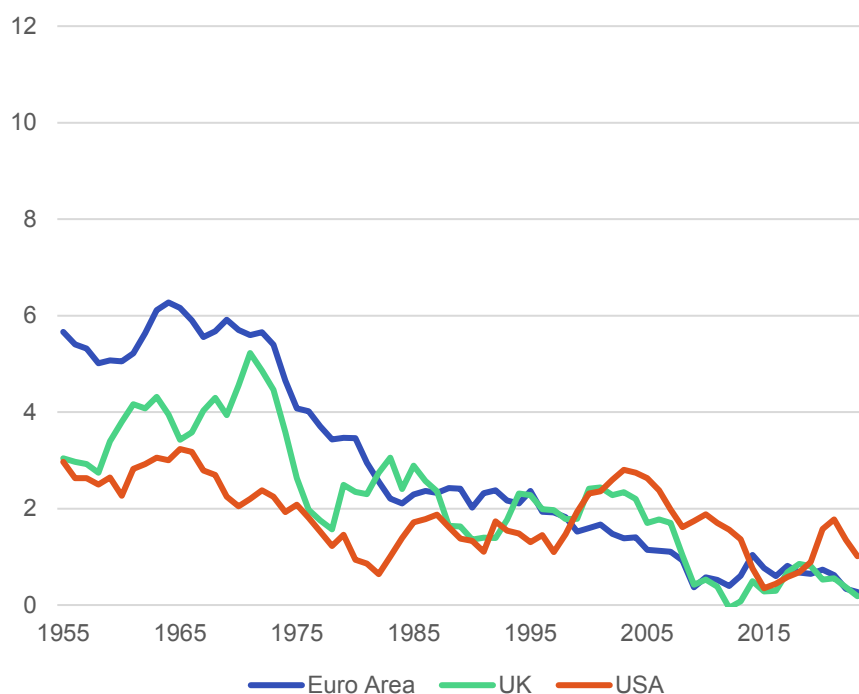
Demographic change will slow economic growth and exacerbate labor shortages – and could drive inflation up

Annual increase in working age population, in millions

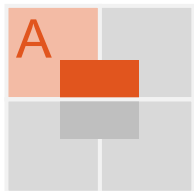


Productivity growth: Will technological progress counterbalance the drags from demographic change and deglobalization?

Labour productivity growth (5-year moving average, in %)

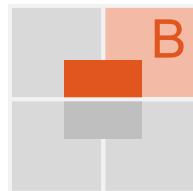


Major global trends are likely to shift inflation upwards over the medium term – how will central banks / economic policies react?



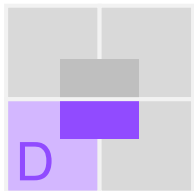
(De-)Globalisation

- Peak globalisation likely behind us
- Geopolitical factors favour regionalising supply chains
- Lower cost efficiency = **higher inflation**



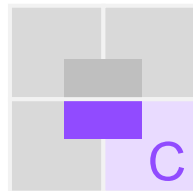
Decarbonisation

- CO2-neutral economies as target
- Climate policies, especially CO2 pricing, make fossil energy more expensive
- At least during transition phase **higher Inflation**



Demographics

- Effects of ageing on labour markets dependent on migration
- Temporarily higher wage growth
- Effects will also be driven by changing consumption patterns in ageing societies – **temporarily higher inflation**

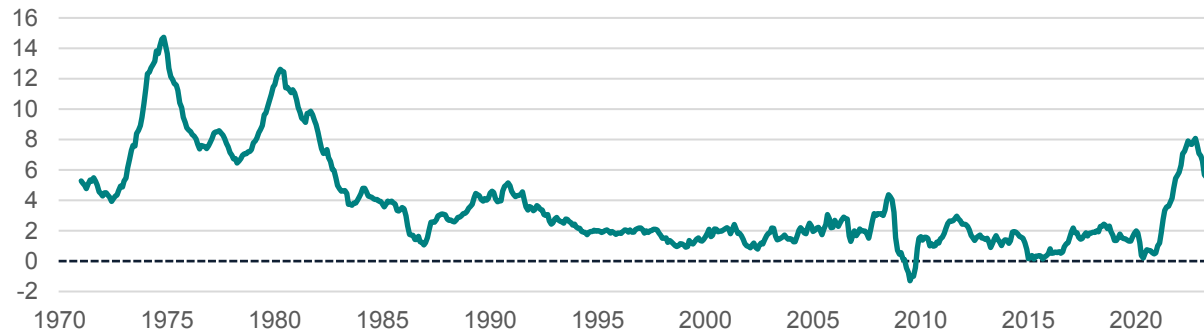


Digitalisation

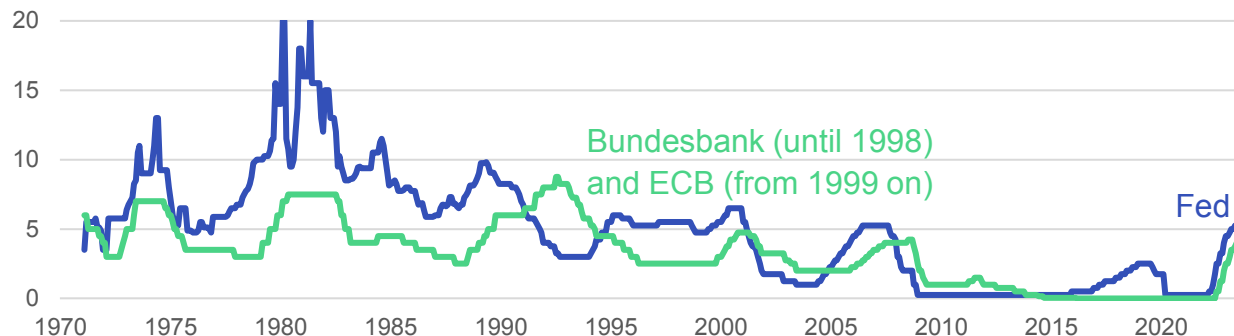
- Trend will continue (e.g. AI)
- Macroeconomic productivity effects dependent on specific technologies
- No upwards pressure on inflation, but (continued) **dampening effects**

However, at the end central banks hold the key to tame inflation

Inflation, average of G7 economies (y/y CPI change, in %)



Central bank policy rates, US and Germany/Eurozone (in %)



Interest rates in the Euro Zone will need to stay high “as long as necessary” to slow still-high inflation

Christine Lagarde, President of the European Central Bank (Frankfurt, August 2023)

Thank you for your attention!

Michael Menhart

MMenhart@munichre.com



Information contained in this material has been obtained from sources that Munich Re believes to be reliable. Munich Re does not guarantee its accuracy or completeness. Opinions expressed in this material are subject to change without notice. The foregoing has been prepared solely for informational purposes and should not be considered a recommendation or an offer to buy or sell any security or instrument in any particular trading strategy. The past performance of any market or security discussed in this material is no guarantee of future results and the value of investments may fall as well as rise.