



# Global Economic Outlook



September 2022

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# Introduction



2022 has arguably been one of the most challenging years the world has experienced in modern times. It's hard to downplay the scale of the geopolitical and economic uncertainty facing every one of us – from individual households to governments and business leaders.

We entered the year with a degree of cautious optimism as Covid restrictions were gradually eased, but what followed was a series of challenges that have tested the resilience of even the most robust, sustainable companies.

Economic modelling and forecasting is a notoriously challenging task, especially in a time of great uncertainty, but taking a step back and looking at the bigger picture is essential. KPMG's *Global Economic Outlook* brings together teams of experts from across the world. Our aim? To dig deeper into past trends, challenges and opportunities and explore how we believe the actions that are taken today may impact on economic output over the coming weeks, months and years.

The international outlook is patchy. Some countries, regions and territories achieved a strong post-pandemic rebound, for others – chronic political and economic challenges dampened hopes of regaining lost ground. It's a similar story across all areas of analysis – with different outlooks and outcomes in different areas. That said, there are several universally consistent themes and stories. The rapid return to economic activity after Covid created supply chain challenges which appear to be easing slightly but continue to drag down growth projections.

Combined with the devastating war in Ukraine, C-suites are grappling with shortages in everything from oil and gas to wheat and microchips. This has had a significant impact on both inflation and recessionary fears.

In my previous role with KPMG, I led the global organization's Energy & Natural Resources practice – supporting member firm clients in an industry that has become used to experiencing profound highs and lows. I now work with CEOs across all sectors as Global Head of Clients & Markets and much of what I witnessed in the energy world is applicable today across all businesses. KPMG's *Global Economic Outlook* is not an exact science, but in a time of great unease, I believe it is an invaluable asset, helping to map out some of the challenges and opportunities ahead and enable corporate leaders to plan for the future and prepare for an eventual return to sustainable, long-term growth.

**Regina Mayor**  
Global Head of Clients & Markets  
KPMG

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# The global outlook: High inflation takes its toll

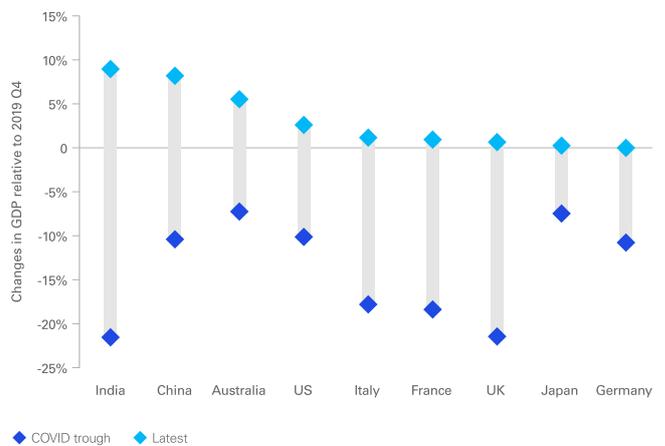


Clouds are once again gathering, marring the outlook for the global economy. As inflation accelerates, putting pressure on households’ finances and businesses’ margins, and causing central banks to tighten monetary policy aggressively, recession is once again on the horizon in many economies.

It was not long ago that the Covid-19 pandemic brought a big part of the economy to a halt, and while the recovery has been relatively swift once restrictions were lifted, its strength has varied across countries (Chart 1).

With all the new challenges so far this year, it is easy to forget that the virus has not yet disappeared. We could see a rise in infections over the colder months, including more disruptions to production in China due to the zero-Covid policy. The impact on labor supply and the health service is also likely to linger, causing a tighter labor market and additional burden on public finances in the medium term.

**Chart 1: The impact of the Covid-19 pandemic and the speed of recovery have been uneven**



Source: National statistics bodies, KPMG analysis.

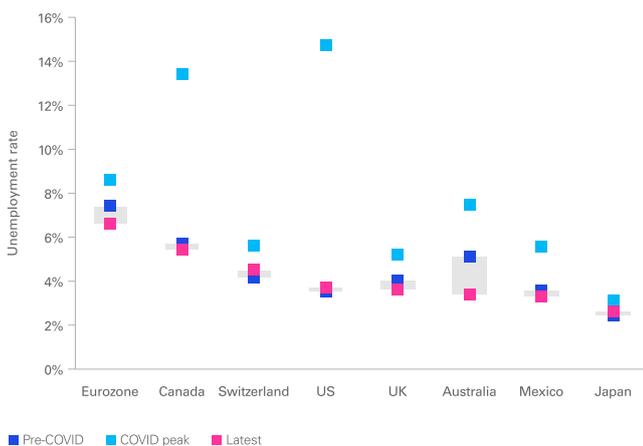
Pressures on global supply chains have eased since their peak late last year, despite the setbacks caused by the Russia-Ukraine war. However, they remain at historically high levels, contributing to the rise in costs experienced by many producers. While we expect the weakening in global economic activity to ease the pressure on supply chains in the short term, other factors could be working in the opposite direction.

With geopolitical tensions on the rise, more friction in supply chains could become the norm. And as labor costs rise in less developed economies and changes in production methods in some industries favor more localized presence, there may also be less impetus for companies to seek production sites further afield, causing globalization to be on the retreat. All this could see inflationary pressures remaining more elevated over the longer term.

Scarcity of workers has contributed to supply bottlenecks, as well as to more elevated inflationary pressures. As Covid-induced restrictions were lifted, demand for labor rose sharply. But the availability of workers fell in many countries, as some were affected by the pandemic while others chose to retire early. As a result, unemployment rates fell swiftly and have now reached pre-Covid levels or even below (Chart 2).

While a weakening economic environment is likely to see a fall in vacancies, the labor market could remain relatively tight over the next year<sup>1</sup>.

**Chart 2: Tight labor markets add to inflationary pressures**

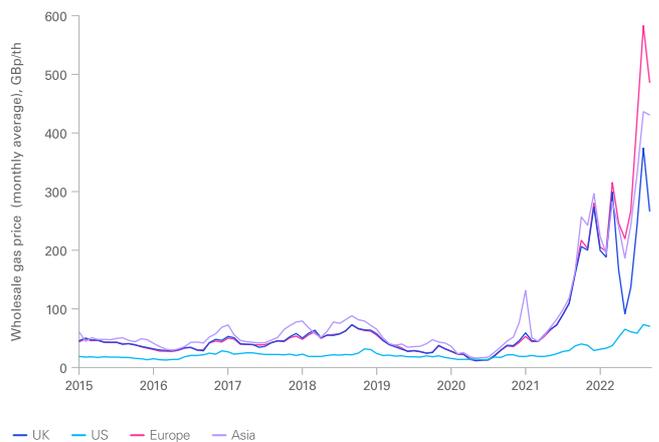


Source: OECD, KPMG analysis.

Although inflationary pressures were already present as economies reopened from Covid, the invasion of Ukraine by Russia added an extra strain, with a range of commodities exported by the region seeing their price rise significantly. More recently, some prices have moderated somewhat and supplies have adjusted while demand eased as the economy slows.

Energy prices have been at the centre of the inflationary surge, although oil prices have moderated lately, which contributed to a minor ease in annual inflation figures in many countries. Nevertheless, the price of gas remains heavily impacted by the conflict in Ukraine, with the rush to secure shipments of liquefied natural gas (LNG) for winter causing not just European but also Asian gas prices to spike recently (Chart 3). It is still uncertain whether sufficient gas supply will be forthcoming over the winter months. This could prove a significant blow to the short-term outlook of some European economies which are more reliant on Russian supply<sup>2</sup>.

**Chart 3: Gas prices are particularly high across most regions**



Source: Refinitiv Datastream, KPMG analysis.

1 See KPMG’s detailed forecasts for unemployment rates in the Appendix.  
 2 See our European country analysis for potential implications of lower gas supply in different economies.

The combination of supply chain bottlenecks, generous government spending, tight labor markets and a commodity shock triggered by the Russian invasion of Ukraine, have together caused inflation to shoot well above central banks’ target across many developed economies.

We expect inflation to moderate significantly from the middle of next year, as the energy shock is no longer reflected in the year-on-year inflation calculation. However, we could be entering an environment that is structurally more inflationary, as production costs – from materials to energy and labor – remain elevated.

Faced with inflation well above targets, an immediate concern for most central banks is that inflation expectations stay high, while their credibility in fighting inflation is lost. The need for fiscal support is likely to stoke more inflation in the medium term, placing fiscal policy actions at odds with the aims of central banks in meeting their mandates. In the cases where investors have been led to question the sustainability of public finances, such as the UK in late September 2022, depreciating currencies and rising borrowing costs have exposed vulnerabilities and increased the risk of contagion.

That is why central banks are likely to be more hawkish in their response to what could be a relatively short-lived burst in inflation, with markets pencilling in aggressive rate rises over the coming months (Chart 4).

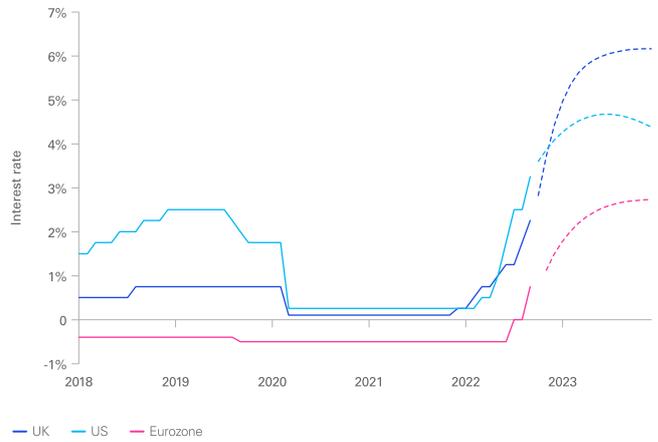
Moreover, if inflationary pressures are to become embedded, interest rates may stay at higher levels than what we saw in the past decade even after the current spike in inflation subsides. This would represent a significant shift in monetary policy in a relatively short space of time.

Rising costs are taking their toll on consumers, with a cost-of-living crisis putting a significant dent on households’ purchasing power. Consumer confidence has taken a big knock across most economies (Chart 5) and spending are following suit, causing overall economic growth to weaken.

Our overall forecast for the world economy is for GDP growth to moderate to 1.9% in 2023 after growth of 2.7% in 2022. Weaker growth could see inflation moderate to 4.7% in 2023 after averaging 7.6% in 2022, according to KPMG forecasts (Chart 6). But as economies around the world brace for another period of headwinds and slowdown in activity, the hope is that on this occasion the downturn will be relatively mild.

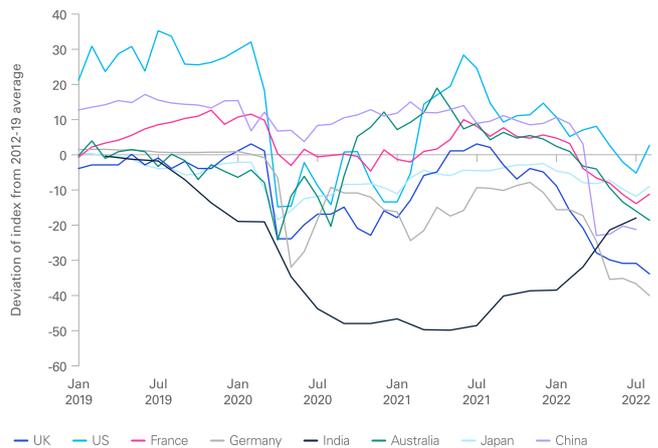
**Yael Selfin**  
Chief Economist, KPMG in the UK

**Chart 4: Central banks are expected to remain hawkish in the short term**



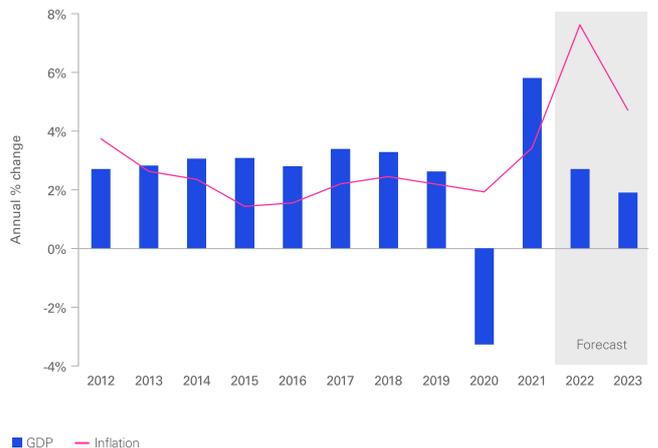
Source: BIS, FRED, Refinitiv Datastream, Bank of England, ECB, KPMG analysis.  
Note: Yield curves shown as of 26 September.

**Chart 5: Consumer confidence has fallen**



Source: GfK, The Conference Board, Cabinet Office of Japan, INSEE, Westpac-Melbourne Institute, China National Bureau of Statistics, Reserve Bank of India, KPMG analysis.

**Chart 6: World GDP growth and inflation projections**



Source: World Bank, KPMG projections.

# United States: Economy poised to stall

The Federal Reserve has committed to raise rates and hold them high for longer, to slowly bring inflation back to its 2% target. The goal is to prevent a more entrenched and persistent cycle of inflation from taking root with a mild but prolonged recession.

Economic growth is expected to slow below the economy’s potential rate of growth, employment is expected to stall and lose ground as we get into 2023. The unemployment rate is expected to cross 5% by year-end 2023 and 5.5% before inflation fully cools.

Fiscal stimulus is expected to remain limited as pandemic aid wanes and infrastructure projects take time to ramp up. Midterm elections will play a key role in determining whether the White House can deliver more on its promises to curb climate change and deal with social issues.

Overall economic growth hit a wall in 2022, after surging at its fastest pace since 1984 in 2021. Real GDP contracted for the first two quarters of the year; a phenomenon usually associated with a recession. The U.S. is not in a recession, yet. Payroll employment surged by 2.8 million jobs in the first six months of the year, twice the annual pace of the 2010s. Consumer spending slowed but did not collapse. That means that the losses we endured did not meet the depth and breadth of losses typically associated with a recession by the Business Cycle Dating Committee of the National Bureau of Economic Research (NBER), the official arbiter of business cycles.

That begs the question: Why do most Americans believe we were in a recession? Because the surge in inflation that they experienced eroded all they had gained in wages since the economy reopened and then some.

Rate hikes and the collapse in housing are expected to take a larger toll on consumer spending by the turn of the year. Home sales and construction activity have already cratered; housing prices will be the next shoe to drop. Housing is one of the single largest triggers to additional consumer spending; now, it is working in reverse.

Business investment is expected to contract after playing catch-up to supply chain delays over the summer. Spending on structures and equipment will be hardest hit. Spending on intellectual property, automation and cyber security is expected to remain buoyant.

**Table 1: KPMG forecasts for the U.S.**

	2021	2022	2023
GDP	5.7	1.5	-0.1
Inflation	4.7	8.2	3.8
Unemployment rate	5.4	3.7	4.3

Source: KPMG Economics, Bureau of Economic Analysis, Bureau of Labor Statistics.  
 Note: Forecasts are dated as of September 2, 2022. GDP and inflation are year-over-year % change. The unemployment rate is an annual average. Numbers are percentages.



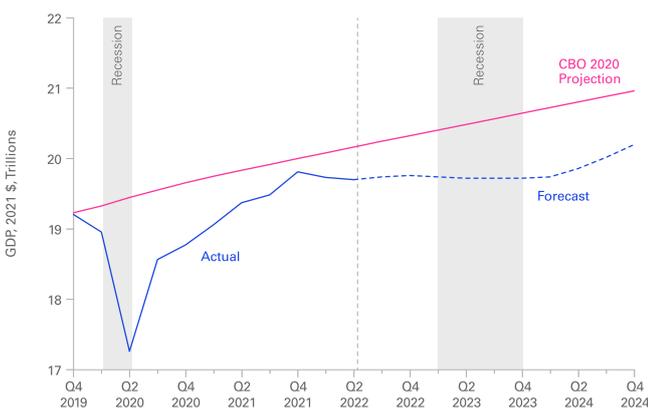
The pandemic aid that buoyed federal spending in 2020 and 2021 has come to an end, while much of the spending associated with the infrastructure bill and efforts to deal with climate change will take time to ramp up. The full effects of those latter shifts will not be felt until the mid-2020s.

State and local government coffers are in better shape. Tax revenues shot up with the surge in spending on goods and homes, while transfers from the federal government to deal with the pandemic have yet to be spent. Many of those windfalls were put into rainy-day funds to cushion budgets from future claims on revenues.

A portion is being used to temporarily suspend taxes on energy, food and school supplies. Those shifts and a surge in tax rebates is helping to blunt the blow of persistently high inflation and keep spending afloat. That makes for good politics but bad economics; tax rebates are poorly targeted and will boost demand at the same time the Federal Reserve is trying to curb demand and inflation.

A strong dollar and weaker growth abroad suggest that the trade deficit will reverse course and widen by year-end. A sharp slowdown in growth here is not expected to offset the drag of even deeper recessions abroad. Imports should continue to outpace exports and the trade deficit is expected to widen in 2023.

**Chart 7: U.S. growth stalls below trend**



Source: KPMG Economics, Bureau of Economic Analysis.

## Inflation slowly cools

A perfect storm of strong demand, supply chain disruptions and the war in Ukraine created the largest move up in inflation we have seen in more than four decades. A strong dollar, a drop in prices at the gas pump and some easing of supply chain disruptions have alleviated the upward pressure on some goods prices. Used vehicle prices are once again depreciating after soaring above the sticker price of new vehicles in 2021.

The jury is still out on how long energy prices can remain low. Much depends upon supply constraints, which remain substantial, and how far the Russian government is willing to go to weaponize its oil reserves. Investors pushed shale producers to curb their expansions and return more of their profits to the owners of capital in the shale industry, after the bath they took at the onset of the crisis. Neglect of energy infrastructure is another hurdle to increase production at home and abroad – refining capacity is particularly limited.

A larger issue is service sector inflation, which is more dependent upon the cost of labor. High wages, high turnover rates and a persistently high level of Covid infections, which is exacerbating staffing shortages, are boosting labor costs. Aging demographics and a surge in Long Covid cases are adding to labor shortages and will make those shortages more chronic as we get into the mid-2020s.

This is happening at the same time as the boost to productivity growth triggered by the pivot to working from home is evaporating; workers are using more of the time they saved by not commuting to engage in leisure activities.

The payoff to technological advances remains concentrated in a few large tech-savvy firms. It is not yet diffuse enough to raise the level of overall productivity growth and offset the shortfall in labor due to aging. A surge in retirements by the baby boom generation and early retirements is not being offset by younger workers entering the labor force. An additional two to four million workers are estimated to be suffering from Long Covid and are unable to work.

A surge in immigration could help alleviate those pressure but doesn't seem likely. The backlogs to immigration created by the pandemic are still substantial, while immigration reform remains on hold. Foreign students, who are dwindling in ranks, are looking for guarantees that they can continue to work in the U.S. once they relocate.



The largest near-term push on inflation is shelter costs. Changes in home values take at least a year to show up as a change in measures of home ownership costs; they were still accelerating through spring 2022. Rents, where demand has shifted in recent months, continue to skyrocket. Shelter costs are particularly problematic, as they account for nearly a third of the consumer price index and are still rising.

Acute labor shortages, a surge in more chronic and costly health conditions and the costs associated with treating Covid patients are putting upward pressure on medical costs. Rural hospitals are the most vulnerable. Consolidation is accelerating, which will further increase costs and limit access to care.

Last, but by no means least, inflation is inertial. Long periods of high inflation tend to distort the behaviors of households and firms. Workers demand wages be indexed to move up with measures of inflation, while firms start baking price hikes into their strategies to cover elevated costs. That phenomenon stoked the stagflation of the 1970s, a period the Fed wants to avoid, even if it means a rise in unemployment.

## The Fed commits to a recession

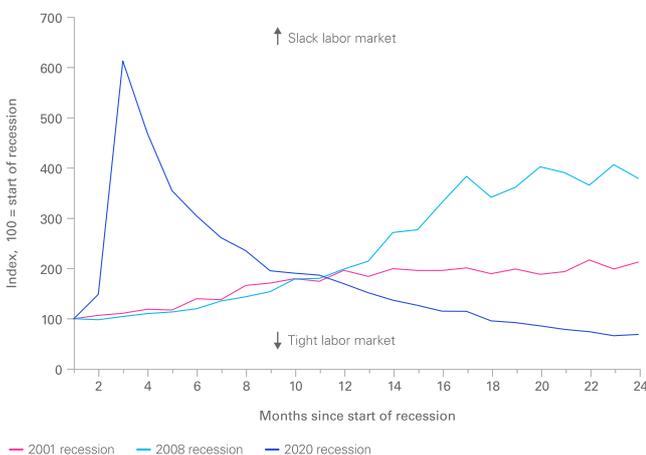
Federal Reserve Chairman Jay Powell laid to rest the fantasy of a soft landing in his annual speech for the Kansas City Federal Reserve Bank’s Jackson Hole, Wyoming Symposium held in August. Either the Fed runs the risk of stoking a more entrenched and corrosive cycle of inflation, which requires a deep and scarring recession to derail, or it triggers a mild but prolonged recession and smaller increase in the unemployment rate today. The latter represents the lesser of two evils.

The Fed can’t grow food or pump oil. It can reduce demand to better balance with what is becoming a more chronically undersupplied world; that is what it intends to do.

**Diane Swonk**  
Chief Economist, KPMG US

**Timothy Mahedy**  
Senior Economist, KPMG US

**Chart 8: U.S. unemployed persons per job opening**



Source: KPMG Economics, Bureau of Labor Statistics.

# Canada: On path for a mild, short-lived recession amid global uncertainty

The economic slowdown underway will likely continue in the next few months, responding to tighter monetary policy and slowing aggregate demand. While the labor market remains strong, and despite increased savings since 2020, household debt, especially for first-time home buyers, remains a risk to the outlook.

Inflation may have peaked but will remain elevated relative to target due to tight labor markets and uncertainty related to commodity prices. Avoiding a wage-fueled inflation remains a priority for global central banks while longer-term inflation expectations have remained stable.

Provincially, Ontario’s labor market keeps posting robust growth, Alberta is benefiting from strong demand for Canada’s energy products, and Québec and British Columbia are facing broad labor shortages.

## Mild, short-lived, recession may occur in early 2023

Covid variants have come and gone, and Canada’s GDP has recovered and stabilized above its pre-pandemic level. After rebounding 4.5% in 2021, GDP growth expectations for this year and next have been revised down in recent months. While another cycle from the ongoing pandemic could still disrupt Canada’s growth engine, restrictions for this coming winter are anticipated to remain lighter than they have been in recent years. Some analysts are now forecasting a short-lived recession for early 2023<sup>1</sup>.



**Table 2: KPMG forecasts for Canada**

	2021	2022	2023
GDP	4.5	3.4	1.3
Inflation	3.4	6.8	3.4
Unemployment rate	7.4	5.3	5.6

Source: Statistics Canada, KPMG analysis.

Note: Average % change on previous calendar year except for the unemployment rate, which is the average annual rate.

The main catalyst for these downgraded expectations has been the coordinated approach taken by global central banks to fight the current bout of inflation by slowing the demand side of the economy. In July, Canada’s overnight rate increased by 100 basis points (bps). The following hike of 75 bps on September 7th took the overnight rate to 3.25%, for a yearly tally of 300 bps so far – a pace of monetary tightening not seen since the mid-1990s following close to 15 years of accommodative monetary policy. Markets are pricing in another 50 bps hikes during the fall, as the Governing Council “judges that the policy interest rate will need to rise further”. It also stated that further changes in 2023 “will remain data-dependent”.

In a rising rate environment, governments, consumers, and businesses will find their debt more expensive to roll over. Canadian residential real estate prices have already started feeling the pinch of tighter monetary policy. While higher rates will cause the economy to gradually slow, most analysts expect Canada to eke out positive growth for 2023, albeit at a rate slightly below potential.

<sup>1</sup> See, for example: Desjardins, Economic and Financial Outlook (August 25, 2022); and RBC, Daily Economic Update (August 31, 2022).

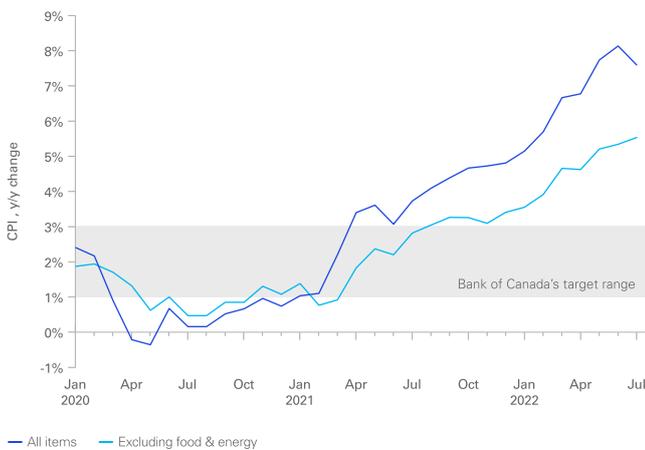
Here are some reasons to think Canada will achieve only a mild, short-lived, recession:

- Labor markets remain steady, which does not align with a deeper recession – the national unemployment rate is close to an all-time low and more than a million jobs remain unfilled;
- Households have accumulated excess savings during the first two years of the pandemic, somewhat counterbalancing elevated domestic debt-to-income ratios in some key housing markets;
- Canadian banks are well capitalized, which points to limited systemic downside risks;
- Canada’s energy sector, a key contributor to the country’s economic growth, continues to increase its exports in the face of higher commodity prices; and
- Different levels of governments are still enacting relatively loose fiscal policy.

## Inflation to remain elevated in the short run, winding down towards target over time

Inflation is expected to have peaked at an annual rate of 8.1% in June. While overall inflation decelerated to 7.6% in July, core inflation (excluding food and energy prices) still inched up to reach 5.5% (see Chart 9). With shelter costs expected to contribute more to inflation in the coming quarters, most forecasters expect inflation to remain above the BOC’s 1-3% target range into Q4 2023.

**Chart 9: Inflation has likely peaked in Canada**

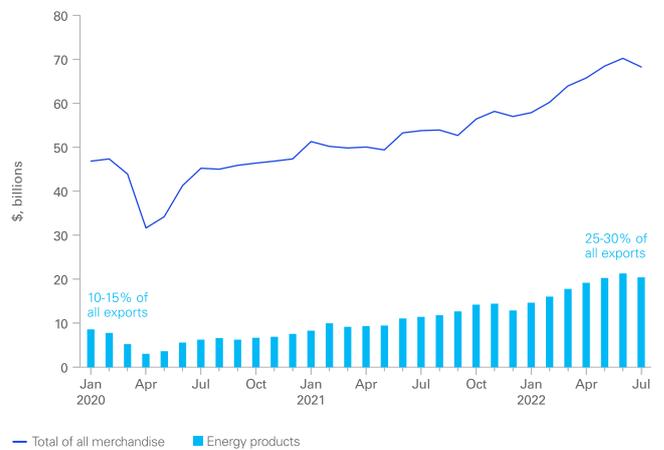


Source: Statistics Canada, KPMG analysis.

## Uncertainties and opportunities ahead

In the current high energy price environment, Canada’s energy exports remain strong, displaying month-on-month increases during the first six months of 2022, with a jump of 25% in Q2 over Q1. The energy sector, which now takes up a 30% share of all Canadian merchandise exports, is contributing significantly to Canada’s total merchandise trade growth (see Chart 10).

**Chart 10: Energy exports, a key contributor to Canada’s merchandise exports growth**



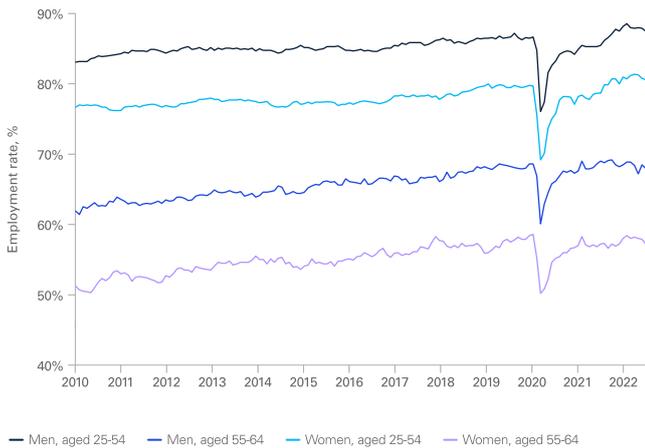
Source: Statistics Canada, KPMG analysis.

Strong demand for Canada’s energy products may enable more significant investments and growth opportunities in Canada’s energy sector. Western provinces, particularly Alberta, are already reaping the benefits with increased capital spending in the oil and gas sector. Yet, domestic oil and gas producers are also maintaining capital discipline as the investment to cash flow ratio remains in check.

Supply chains may continue to be put to the test as zero-Covid policies in key manufacturing countries may keep some key businesses on hold. This volatility may in turn have an outsized impact on exporters and importers as they deal with an unreliable flow of goods. Nevertheless, with recent suspensions in vaccine mandates for domestic travelers and a general easing of restrictions globally, restrictions for this coming winter are anticipated to remain lighter than they have been in recent years. Thus, the impact of Covid on economic activity is not expected to pick up significantly over the forecast horizon.

Tight labor markets will keep pressuring services inflation for some time. By mid-2022, there were more job openings in Canada than available workers. Employment rates quickly rebounded since the first wave of the pandemic and have reached historic highs for all age cohorts (see Chart 11). Job creation has however been muted since February.

**Chart 11: Very little slack in the Canadian labor market**



Source: Statistics Canada, KPMG analysis.

Some further gains on labor markets may occur as Canada implements a national daycare system akin to the one established in Québec in the late 1990s, which has contributed to the province showing one of the highest participation rates in the world among women of child-bearing age. However, the program’s contribution to alleviating the undersupply of workers can be expected to take time. A more ambitious immigration target, after two years of lower intakes due to the pandemic, is more likely to relieve stress in the short run.

## Economies facing elevated uncertainty for the near future

While only a mild recession is the base case scenario for the Canadian economy, there are risks to this forecast.

On the upside, a decline in supply chain bottlenecks may reverse some of the increase in prices we have seen in the past 18 months. Retailers are reporting elevated inventories, while intermediary goods accumulation in manufacturing facilities dissipated throughout 2022.

Excess savings from Canadians since 2020 are likely to prevent any economic slowdown from turning into a protracted recession. Retail sales have so far remained robust in the face of global uncertainty.

On the downside, Canada’s economy remains open to global economic trends and uncertainty. For one, European consumers may be forced to cut back on discretionary spending given the expected higher energy prices in the coming months, which may contribute to a further global economic slowdown. As the adage also goes, when the U.S. sneezes, Canada catches a cold – any pothole in the U.S. economy would also have implications for Canada’s growth path.

A higher inflation for a longer period of time may incentivize central banks to tighten monetary policy further. Combined with vulnerabilities coming from Canadian household debt levels, this may represent a downside risk to this outlook. As households may have to tighten their spending in the face of increasing interest rates, a correction in Canadian real estate prices may also lead to negative wealth effects that affect the economy at large.

Another key downside is that inflation expectations become entrenched at a higher level, which may trigger further monetary policy tightening. The prospect of a wage-price spiral remains a tail-end scenario, as various surveys point to relatively stable inflation expectations over a five-year horizon<sup>2</sup>.

All in all, central banks are committed to taming inflation – the benefits of a stable low-level of inflation having been made clear since the early 1990s. This may come at the cost of a mild recession.

### Sonny Scarfone

Manager, Economics & Strategy at KPMG in Canada

### Karicia Quiroz

Manager, Economics & Policy at KPMG in Canada

### Mathieu Laberge

Partner, Economics & Policy at KPMG in Canada

### Caroline Charest

Partner, Economics & Strategy at KPMG in Canada

<sup>2</sup> Canadian Survey of Consumer Expectations—Second Quarter of 2022.

# Brazil: Government balance creates risks

Consumption experienced growth in the first half, but momentum is slowing.

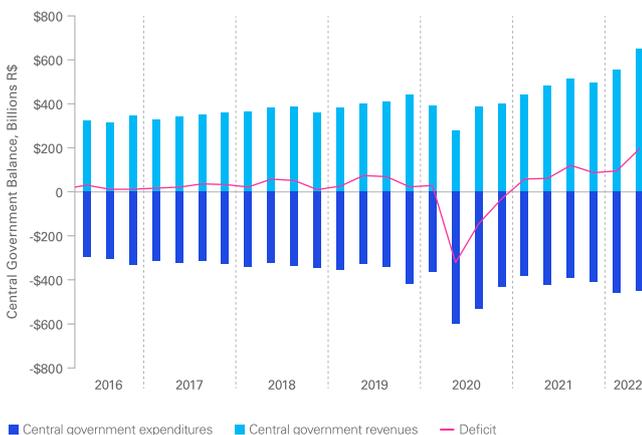
Central government is continuing stimulus while the central bank tries to tackle inflation.

The proposed budget poses a major risk to the government’s ability to counter slowing growth.

The Brazilian economy advanced 3.2% year-over-year in Q2, the sixth consecutive quarter of economic expansion, driven by household consumption and government expenditures. Trade and investment have both been a drag on economic growth, as exports dropped dramatically. Key to the outlook for Brazil is the fiscal balance – and whether it is sustainable post-2022. Looking forward, we expect growth to slow in 2023 as inflation continues to weigh on households while monetary policy remains contractionary.

Growth in government expenditures is painting over underlying weaknesses in the economy. Corporate tax revenues have surged, which improved the government’s balance sheet and allowed for continued fiscal stimulus at levels similar to the 2020 pandemic-era. This has boosted household spending even as high inflation erodes real incomes, and the central bank continues to tighten monetary policy to control inflation. Fiscal stimulus is likely to retreat in the next few quarters, which will reveal an economy that is facing the potential for a significant slowdown in economic activity in 2023.

**Chart 12: Brazil’s government expenditures far exceed pre-pandemic averages**



Source: KPMG Economics, Secretaria do Tesouro Nacional.

**Table 3: KPMG forecasts for Brazil**

	2021	2022	2023
GDP	4.8	1.9	0.8
Inflation	8.3	9.8	5.8
Unemployment rate	13.6	10.4	10.1

Source: KPMG Economics, Instituto Brasileiro de Geografia e Estatística.

Note: Forecasts are dated as of September 1, 2022. GDP and inflation are year-over-year % change. The unemployment rate is an annual average. Numbers are percentages.





Even though fiscal stimulus is likely to be withdrawn, the deficit is set to worsen on falling revenues. Falling revenues matter for Brazil's fiscal capacity – the government bases its target budget deficit on projected GDP growth. Brazil's congress approved a target deficit based on their own GDP projection for 2023 of 2.5% and much stronger government revenues, compared to market expectations of 0.8%. The budget leaves little room for Brazilian lawmakers to counteract slowing growth should a recession occur in 2023.

The persistence of inflationary pressures means that the central bank will be unable to provide monetary policy support as the economy slows. The Brazilian economy has been hit by its worst bout of inflation since 2004, forcing the central bank to increase the policy rate starting in March 2021. Despite Brazil's CPI inflation coming down to 8.7% in August amid falling crude oil prices, transport, and energy prices, the central bank will need to continue tightening policy to bring down inflation.

High inflation is beginning to erode household spending in Q3 despite a strong labor market. While consumption has been driving Brazil's recovery in 2021 and 2022, retail sales have been slowing over the summer. This trend indicates that consumers may be feeling the impacts of higher Selic rates from the Central Bank of Brazil. The unemployment rate decreased to its lowest level since 2015 and is falling, somewhat mitigating the impacts on high inflation on real incomes.

Brazil is heavily integrated in global trade, making net exports key to Brazil's outlook. Between 2011 to 2021, trade averaged 28% of GDP for Brazil, according to the World Bank. Brazil's exports have suffered from supply chain and infrastructure disruptions as well as poor harvests in agricultural industries. Higher oil and gas prices precipitated by the Russia-Ukraine war also weighed on exporters of non-petroleum products – Brazil imports more refined petroleum than it exports, and non-petroleum products constitute over 80% of export value. Brazil's exporters will also likely be facing a global slowdown in the coming quarters decreasing external demand. Meanwhile, imports from the U.S. and China have increased in recent quarters due to increasing domestic demand, creating a drag on overall net exports as a share of GDP. However, this trend may reverse as overall demand in Brazil slows.

Though GDP and unemployment have showed signs of improving in the first half of 2022, the economy is likely to begin slowing due to high interest rates and continuing inflation. Tighter credit conditions, a global slowdown, and worsening terms of trade are also likely to weigh on Brazil's already slowing net exports. Retreating fiscal stimulus in the coming quarters will reveal an economy that is facing a significant slowdown in 2023, with little room for maneuver from either the fiscal or monetary policy side.

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**Meagan Martin**  
Economist, KPMG US

# Mexico: Stable but surrounded by risks

Compared to other emerging markets, Mexico has been a laggard in economic growth. With or without a recession in late 2022 or early 2023, the long-term outlook for Mexico remains about 2%.

In case of a recession, Mexico has the fiscal space for a countercyclical policy response.

The central bank’s response to inflation has been strong, with rates expected to hit 9.5% by the end of 2022.

Growth in Mexico is expected to slow over the remainder of 2022, even though the first half of the year surprised to the upside. GDP is expected to come in at 1.7% year-on-year after rising by 5% in 2021. The level of economic activity is expected to be 2% below its pre-pandemic level by the end of this year. Public and private investment have been a drag on growth. The Mexican economy is currently 7% below the growth trajectory it was on before Covid hit. A slowing U.S. economy will further impact growth prospects in Mexico due to close trade relations.

Compared to other emerging markets, Mexico has been a laggard in economic growth. Prior to the pandemic, Mexico’s growth had been rising at a meager (compared to its Latin American counterparts) 2% per year. With or without a recession in late 2022 or early 2023, the long-term outlook for Mexico remains about 2%.

Consumer spending is over two-thirds of the economy and has been rising steadily since the pandemic slump in early 2020. With inflation at multi-decade highs, retail activity has been hit in recent months, but remains above pre-pandemic levels for now due to strong consumption and a return of tourism (which accounts for 15% of GDP).

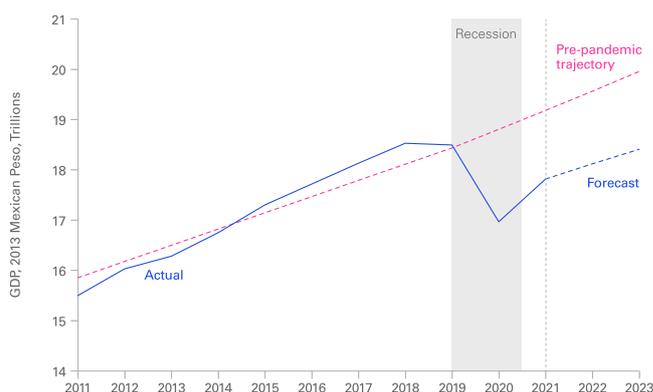
The unemployment rate hit 3.3% in July 2022 – a pre-pandemic low. Wage growth remains strong, while remittances hit a record high in 2022 and are expected to keep rising. Remittances are a crucial source of income for Mexican households, adding up to about 3.9% of GDP in 2020. The unemployment rate is expected to move up into next year and 2024 as the central bank continues its tightening cycle. By the end of 2022, the unemployment rate will likely hit 3.5%, with 2023 averaging 3.8%.

**Table 4: KPMG forecasts for Mexico**

	2021	2022	2023
GDP	5.0	1.7	1.5
Inflation	5.7	8.0	5.5
Unemployment rate	4.1	3.5	3.8

Source: KPMG Economics, National Institute of Statistics and Geography (INEGI).  
 Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate.

**Chart 13: Growth in Mexico remains below trend**



Source: KPMG Economics, INEGI/Haver Analytics.

Exports are expected to grow by 9.6% in 2022 and slow down to 4% in 2023. Strong demand from the U.S. consumer for cars, along with an uncoiling of supply chains, has helped this year. Mexico is an oil exporter and has benefitted from higher oil revenues in 2022 as prices skyrocketed. This has helped offset the 2% of GDP the government spent on fuel subsidies. Additionally, imports are expected to grow by 8% in 2022 and slow down to 3.7% in 2023.

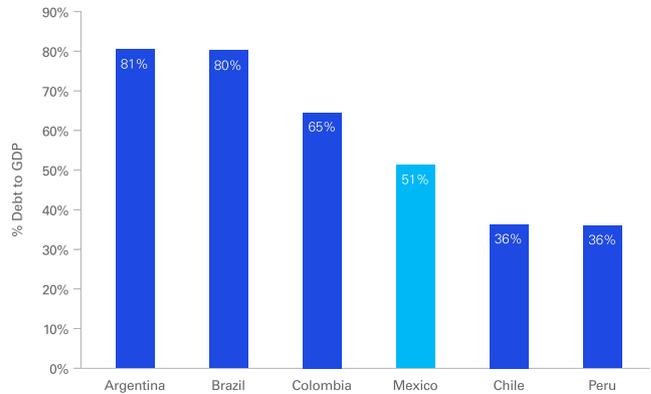
Pre-pandemic political reforms from the current government tightened the fiscal belt during a time when other governments were funneling funds to their troubled sectors. The silver lining is it allowed the country to keep its low investment grade debt rating. However, investment has been poor, as fiscal reforms have pushed out private investment.

Mexico’s public deficit will hit about 3.1% of GDP in 2022. A positive fiscal impulse has allowed Mexico’s government to provide fuel and energy subsidies to households in the first half of the year; the windfall received from rising oil prices has allowed the spending to net out. In case of a recession, Mexico has the fiscal space for a countercyclical policy response. However, Mexico did not enact as strong a response as its neighbors when the pandemic first hit, and therefore is unlikely to do so due to a global slowdown.

Inflation surged to 8.6% in the first half of August compared to a year ago. Much of that was caused by soaring food prices, as energy prices have come off their peak. Inflation is not expected to come down to the Banxico’s target of 3% (+/- 1 percentage point) until 2024 or later.



**Chart 14: Mexico has more fiscal space than most of its neighbors**



Source: KPMG Economics, Ministerio de Economía y Finanzas Públicas, Banco Central do Brasil, Banco Central de Chile, World Bank, Departamento Administrativo Nacional de Estadísticas, Bank of Mexico, Instituto Nacional de Estadística Geografía e Informática, International Monetary Fund/Haver Analytics.

The central bank’s response to inflation has been strong, with Banxico’s August meeting resulting in a 75 basis point hike to 8.5%. Rates are expected to hit 9.5% by the end of 2022. Mexico is at a different stage of the business cycle than the U.S.; a slowdown in world economic growth could be enough to help the central bank achieve its inflation target.

A recession is not in our base case but is the downside scenario, especially if the U.S. enters one at the end of the year. A recession in the U.S. would wipe out almost all growth for Mexico in 2023. About 80% of Mexico’s exports go to the U.S., therefore any drop in consumer or business activity in the U.S. will impact the Mexican economy and create a lasting damage to industrial production and private investment. A more severe global slowdown would pose even more downside risks for Mexico.

**Yelena Maleyev**  
Economist, KPMG US

# ASEAN: Global headwinds weighing on trade in the region

While the relaxing of Covid restrictions has benefited ASEAN economies, continued lockdowns in China and high commodity prices have been a dampener on growth.

Inflation rates are rising but remain low by global standards. Export revenues for commodity producers have been boosted by higher commodity prices.

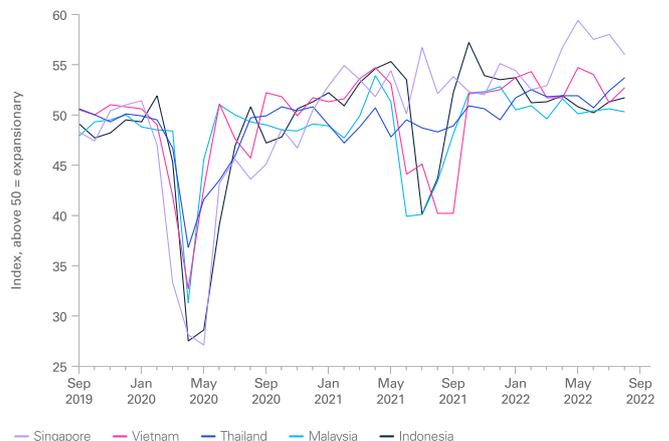
While interest rates in the region are generally being raised, the pace of tightening is slower than in some developed economies. The move into safe assets has resulted in currencies across the region losing value against the USD this year.



Covid restrictions have been unwound in many ASEAN countries this year allowing domestic activity to normalize. This has driven a strong rise in consumption, which has been particularly marked in Singapore (up 6.1% since the start of the year) and Malaysia (up 11.7%) – the rebound is consistent with both jurisdictions having some of the toughest lockdowns and ongoing restrictions in 2020 and 2021.

Solid consumption growth has been somewhat offset by difficult external conditions (a result of the lockdowns in China) and a mixed outturn for investment growth; rising inflation and borrowing costs have combined with concerns about the outlook to weigh on business’ capital expenditure plans. Overall, the pace of GDP growth in most ASEAN countries has broadly held steady this year, with the boost to household spending offset by drags elsewhere. But there have been some notable exceptions, with Malaysia recording a spectacular pace of GDP growth in the first half of the year.

Chart 15: Purchasing Managers’ Index, Asia



Source: KPMG Economics, IHS Markit, Macrobond.



### Tourism arrivals recovering slowly but surely

While tourism arrivals have started picking up, they remain well below pre-Covid levels. The recovery in Singapore appears to be one of the strongest in the region, with visitor arrivals reaching 50% of pre-pandemic levels in July. But given the ongoing lockdowns and border restrictions in China, a full recovery is unlikely in the near term. With tourism typically accounting for a significant share of GDP in Thailand, Vietnam, and Indonesia, the speed of the recovery in this sector will be a major driver of growth in the years ahead.

Chart 16: International arrivals, Asia



Source: KPMG Economics, Macrobond.

### Merchandise goods trade weighed down by lockdowns and global headwinds

More generally, lockdowns in China have disrupted trade throughout the region. A number of cities in China are currently in lockdown, which is creating ongoing disruption to supply chains as well as dampening China’s imports from across the Asia region. And the sharp slowdown in activity, particularly in the construction sector, has weighed on demand for key exports for most economies across the region. China’s importance as a source of demand means that all economies will continue to be impacted; growth in Korea’s exports (a bellwether for the region) moderated to 6.6% year-on-year in August.

Chart 17: Export growth, Asia



Source: KPMG Economics, Macrobond.

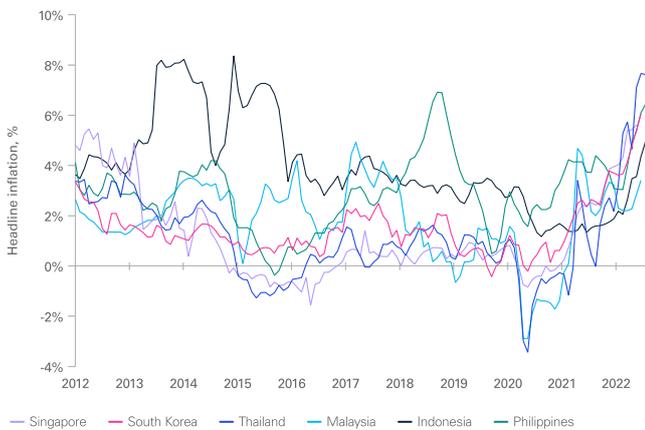
Looking ahead, conditions are set to remain challenging. If the authorities are able to ease restrictions and policy, a rebound in China’s economy will provide some welcome relief. But with growth momentum slowing and major advanced economies in Europe and North America leading the slowdown, any relief from an improved outlook for the region will be short-lived. Overall, export momentum is set to moderate over the next twelve months, as the full impact of interest rate rises and high inflation materializes in external demand for goods.

## Inflation rising to uncomfortable levels

As elsewhere, inflation is picking up across the region. But the rates are generally lower than in much of the rest of the world. Movements in global energy and food prices are flowing through and are being exacerbated by exchange rate depreciations. But relatively small amounts of fiscal stimulus through the pandemic and the lingering impact of restrictions means that domestic demand has not moved substantially beyond supply, resulting in limited domestic wage and price pressures. Overall, inflation rates are expected to peak at relatively low levels across the region.

The surge in commodity prices has also been a benefit to some Asian countries. In particular, Indonesia and Malaysia have seen significant rallies in their terms of trade this year as the price of crude and palm oil has skyrocketed. Those rallies have subsided in recent months, but strong commodity prices are clearly still benefiting commodity exports.

**Chart 18: Headline CPI inflation, Asia**



Source: KPMG Economics, Macrobond.

While the recent dip in oil prices may take some of the sting out of price hikes for consumers, we doubt that inflation has reached its peak for most of the region. We have therefore lifted our forecasts for inflation in 2022 and 2023 throughout the region.

## Policy tightening set to become a drag on growth

In the absence of widespread domestic pressures, the pace of interest rate rises has generally been slower than in other countries (albeit starting from a higher base in Indonesia and the Philippines). This outcome, coupled with a flight to safe assets (particularly the USD), has resulted in many currencies depreciating sharply this year; the Korean won has lost 19% and the Thai baht 13%. But in line with the positive shock to their terms of trade, commodity exporters have generally seen smaller movements, with the Indonesian rupiah depreciating by just 5% since January.

Fiscal tightening will add a further headwind to growth over the medium term, with the elevated levels of government spending through the pandemic now being unwound. In fact, in some countries such as Indonesia and Singapore, attention has started to shift towards fiscal consolidation, with the announcement of tax increases as initial signs of economic recovery emerge.

### Ben Udy

Economist & Senior Manager, KPMG in Australia

### Dr. Sarah Hunter

Senior Economist & Partner, KPMG in Australia

# China: Covid, property market and policy support

China will likely stick to its strict Covid containment policies in the near future. How the government balances the objectives of controlling the pandemic and maintaining economic growth is still the key issue to watch.

The property market has faced considerable headwinds since H2 2021 and the pressure continues to mount. The slowdown has had a large impact on investment, bank loans, and housing-related consumption.

The Chinese government has taken a series of fiscal and monetary policy measures to stimulate demand. We expect more measures to be announced to support growth.

China's GDP grew by 2.5% year-over-year (yoy) in H1 2022, below its 5.5% annual growth target set in March. The economy grew 0.4% in Q2. It was the second lowest quarterly growth, only higher than the first quarter of 2020 when the pandemic started (-6.9%). The slowdown in Q2 was mainly due to a resurgence of the Omicron variant of Covid between March to May, which caused lockdowns in some areas and logistic disruptions.

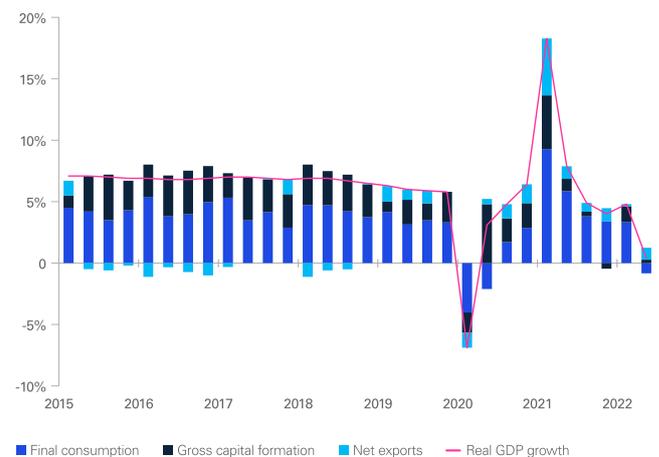
**Table 5: KPMG forecasts for China**

	2021	2022	2023
GDP	8.1	3.5	5.2
Inflation	0.9	2.5	2.3
Unemployment rate	5.1	5.4	5.1

Source: Wind, KPMG forecasts. Average % change on previous calendar year except for the unemployment rate, which is the average annual rate. Inflation measure used is the CPI, and the unemployment measure is the surveyed unemployment rate.



**Chart 19: Contributions to China's real GDP growth by sector**



Source: China's National Bureau of Statistics, Wind, KPMG analysis.



Economic activity showed a recovery in June as the Omicron outbreak came under control. However, summer travels led a resurgence of infections in some cities, and the daily new cases (including asymptomatic cases) increased to over 2,000 in mid-August from below 100 at the end of June. Growth in industrial production slowed and manufacturing purchasing manager index (PMI), a leading indicator, fell into contraction territory again in July. Meanwhile, the most severe heatwave in six decades hit many areas this summer, sending electricity usage up 6.3% in July – the fastest growth since last September. The drought also caused a shortage of hydropower production in some places, weighing on industrial production.

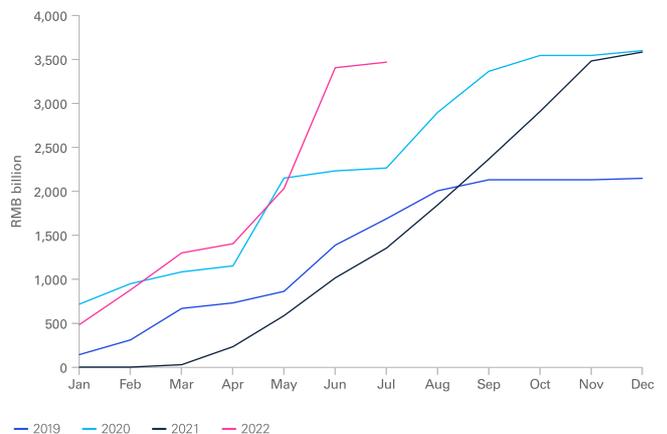
The recovery of consumption is still slow and is subject to the pandemic evolution. Growth of the retail sector rebounded to 3.1% in June from -11.1% in April, but it moderated again to 2.7% in July due to the recent resurgence. Besides the pandemic, household expectations for job security and income growth are important drivers to consumer spending. The government has taken various measures to keep the job market stable, and the urban surveyed unemployment rate dropped to 5.4% in July from 6.1% in April. We expect the unemployment rate to average at 5.4% in 2022. Income sentiment and consumer confidence will likely improve in H2, supporting a gradual recovery of consumption.

Meanwhile, the real estate market faces continued pressures. Liquidity is a key challenge for developers, especially those with high leverage ratios. Funding pressure has caused some developers to suspend construction of pre-sold houses, causing some homebuyers to threaten to stop making mortgage payments. We estimate the overall exposure of banks to the troubled projects is still relatively small, but possible contagion risks should be monitored. The government has taken actions to stabilize the market. On the demand side, many local governments have relaxed restrictions on property purchases, cut mortgage rates and lowered down-payment ratios. On the supply side, some cities are setting up relief funds to help developers with liquidity issues. The central bank also plans to provide targeted credit support to distressed developers to ensure delivery.

The government has maintained its overall real estate policy that ‘housing is for living in, not for speculation’. Although the property market is facing considerable headwinds, China’s increasing urbanization and households’ growing demand for quality homes should support the market in the long run.

Infrastructure investment has become the key driver to support economic growth. The government has speeded up the issuance of local government special bonds (LGSBs), a major funding source for infrastructure investment. By the end of July, the government had issued a total of RMB 3.47 trillion LGSBs, 95% of the annual quota. The pace of issuance was much faster than in previous years. Infrastructure projects such as water conservancy, transportation and urban renovation have seen fast growth. We expect infrastructure investment to remain strong in the second half of this year.

**Chart 20: Cumulative issuance of local government special bonds in recent years**



Source: Ministry of Finance, Wind, KPMG analysis.

Exports have remained resilient. Driven by strong external demand, China's exports were up 18% in July and increased 14.6% in the first seven months of the year. July's trade surplus hit a record high, exceeding USD 100 billion for the first time. The bilateral trade between China and ASEAN has further strengthened since the RCEP agreement took effect at the beginning of the year. With easing supply chain disruptions and production ramp-up, Southeast Asian countries are increasing their demand for intermediate goods from China. Exports of new energy products such as solar cells and lithium-ion batteries also saw strong momentum. Looking ahead, we expect exports' strong growth to moderate in H2, due to both high bases and slowing global growth.

We expect China's fiscal and monetary policy to remain supportive. After announcing a set of 33 supportive measures at the end of May, the government introduced another 19 measures in August to bolster growth. Utilizing the remaining balance accumulated from previous years, it announced a new RMB 500 billion quota in LGSBs to support local government spending. The new quota is expected to be fully issued by October. In addition, on top of the RMB 300 billion policy bank bond issuance announced in June, the government added another RMB 300 billion bond quota, which can be used as equity capital for key infrastructure projects.

On the monetary side, the central bank reduced the policy rate (medium-term lending facility, MLF) in August again, after cutting it in January. It also used special relending facilities to provide direct credit support to small and medium enterprises (SMEs), green investment and the transportation sector.

Inflation has remained low in China compared to many parts of the world, but it may see some upward pressure in H2. Food accounts for nearly 30% of China's consumer price inflation (CPI) and the cyclicity of pork prices is an important factor behind inflation fluctuations. Driven by recent increase of pork prices, CPI rose by 2.7% in July, up from 2.1% in May. In September, China released state pork reserves to ease pork prices. Excluding food and energy, core CPI remains muted as the consumption recovery stays weak. We expect overall inflationary pressure to remain in check in 2022. Meanwhile, producer price inflation (PPI) continued to moderate from a high base, slowing from 6.1% in June to 4.2% in July.

With the easing of Covid infections and relaxing of social distancing requirements, as well as the government's continued support measures, Hong Kong (SAR)'s economy showed a sequential improvement in Q2. Real GDP growth contracted at a moderate pace of 1.3%, narrowing from -3.9% in Q1. As Hong Kong has adopted a pegged exchange rate with the USD, the government raised its interest rate to 2.75% in lockstep with the U.S. Federal Reserve's rate hikes. Monetary tightening and a global economic slowdown may weigh on Hong Kong's recovery. Looking ahead, we expect Hong Kong's economic growth to continue to recover in H2, but challenges also remain.

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**Kevin Kang, PhD**  
Chief Economist, KPMG China

# Japan: Loose policy keeping the yen down, adding to inflation

Headwinds to households are mounting, exports weighed down by global environment.

Inflation has risen above the Bank of Japan’s target and has further to rise in the months ahead.

The Bank of Japan’s continuation with loose policy settings has caused the yen to depreciate to its lowest level in decades.

Japan has had a slow start to 2022 with GDP rising by less than 0.6% in the last six months. Activity has been supported by the continued relaxation of Covid restrictions, which has enabled a solid rebound in consumption. But momentum is expected to ease over the rest of 2022, as household budgets are squeezed by the step up in inflation. Lockdowns in China have put a significant drag on exports, and while conditions there are now improving, there are significant clouds hanging over other regions. Overall, we now expect Japan’s economy to grow by 1.6% this year, followed by 2.2% in 2023.

After rebounding through Q2, the latest activity data suggests that momentum in Japan’s economy is now easing. The services PMI, an indicator of growth momentum in the sector, fell into contractionary territory in August (49.2), suggesting that the inflationary headwinds facing households are flowing through to spending. But pent-up demand and excessive savings accrued during the pandemic are providing some immediate relief, with retail sales increasing by a robust 2.6% on the month in July.

Outside of domestic consumers, there is still scope for a further rebound in service activity through a continuing recovery in tourism inflows. Japan’s border restrictions have remained among the tightest in the world this year, with steps to re-open lagging behind most other countries. There was a further easing of the rules in September, with travellers outside of tour groups now allowed to enter as long as they have pre-booked their trip with an agent. Even so, the new daily cap of 50,000 for inbound arrivals is still around half of pre-virus arrivals so there is some way to go before the sector has fully recovered.

**Table 6: KPMG forecasts for Japan**

	2021	2022	2023
GDP	1.7	1.6	2.2
Inflation	-0.2	2.4	1.6
Unemployment rate	2.8	2.5	2.6

Source: Cabinet Office of Japan, KPMG analysis.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate.



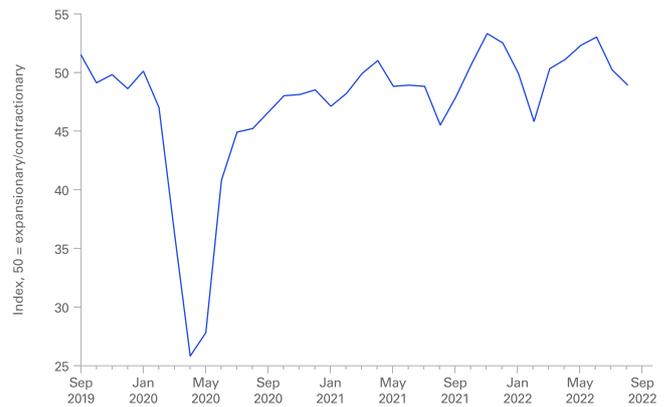


Japan’s manufacturing sector continues to face challenges, with the PMI reading falling to 51.5 in August. While this is still in expansionary territory, the key output and new orders sub-indices fell into contractionary territory. Global demand for Japan’s machinery and equipment capital goods is likely to ease as interest rate rises dampen investment momentum. And although exports to China have begun to rebound, in line with the re-opening of the economy, they are likely to remain subdued given the ongoing lockdowns and outlook for the domestic economy.

As in most other countries, headline inflation is set to remain elevated through the rest of 2022, as the impact of imported food and fuel price rises flow through. Indeed, Tokyo energy prices are up 29% from a year ago, the fastest pace of energy inflation since the 1980s. High energy prices have prompted the government to explore the restarting of some idle nuclear plants and the building of new plants. Food inflation is close to 5%, the highest rate in nearly a decade, and the strength in agricultural commodity prices and ongoing war in Ukraine means it is unlikely to moderate soon. The moves in global prices are also being reinforced by the depreciation of the yen, which is further increasing the local price of these essentials.

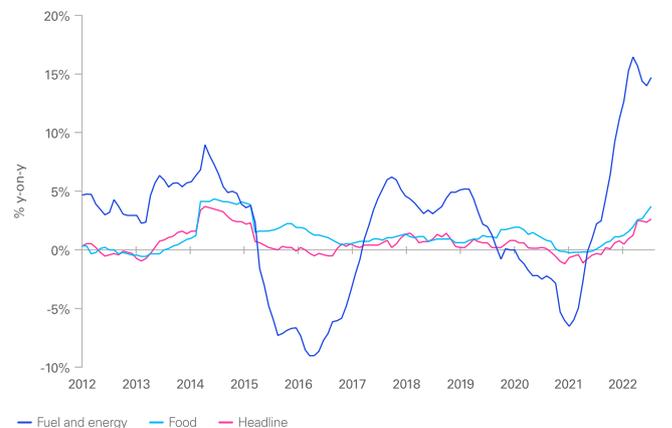
Unlike most other countries, wages growth in Japan has remained relatively subdued, at around 2% year-on-year, with the Spring Negotiation culminating in a subdued base pay increase. Given this, the risk of wage growth lifting markedly in response to inflationary pressures is very low, and this in turn is limiting domestically-generated price increases. Looking ahead, headline inflation is expected to moderate to 1.6% in 2023, as the impact of external price moves in 2022 drops out of the calculation.

**Chart 21: Purchasing Managers’ Index, Japan**



Source: KPMG Economics, IHS Markit, Macrobond.

**Chart 22: CPI inflation, Japan**



Source: KPMG Economics, Statistics Bureau of Japan Macrobond.

Given the lack of domestic inflationary pressures and the subdued economic outlook, the Bank of Japan (BoJ) is continuing to signal its commitment to ultra-loose monetary policy. Markets have repeatedly challenged the Bank’s yield curve control, but the BoJ has responded by lifting the pace of asset purchases to record levels, to maintain the 10-year bond yield close to 0%. This supports our view that the BoJ is unlikely to tighten policy settings any time soon.

The BoJ’s determination to keep policy settings loose has driven the yen to the weakest level since the 1990s, with the currency currently sitting around 140 yen per USD. And looking ahead, continued policy tightening in other countries may force the yen lower in the months ahead. The weak exchange rate is contributing to the recent strength in inflation; import prices are up by nearly 50% from a year ago. As the yen continues its descent this trend will continue and will be a driver of further increases in headline inflation in the near term.

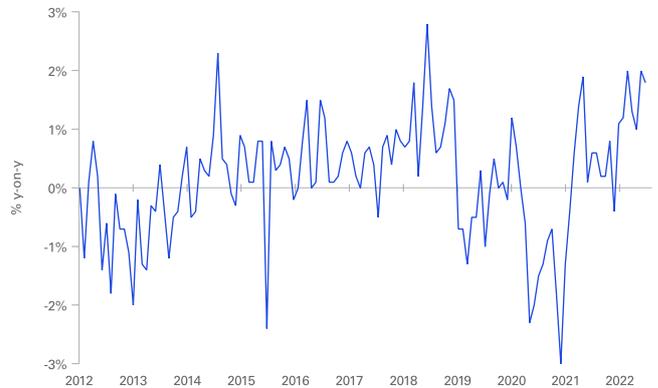
**Ben Udy**

Economist & Senior Manager, KPMG in Australia

**Dr. Sarah Hunter**

Senior Economist & Partner, KPMG in Australia

**Chart 23: Total cash earnings, Japan**



Source: KPMG Economics, Statistics Bureau of Japan Macrobond.

**Chart 24: Currencies vs US\$**



Source: KPMG Economics, Macrobond.

# India: Driving growth on the back of inflation control

India to remain among the fastest-growing economies globally.

Global geopolitical tensions expected to create uncertainty in the trajectory of inflation.

Investor-friendly policies such as the PLI schemes and their extension to newer sectors expected to help promote the manufacturing ecosystem in India.

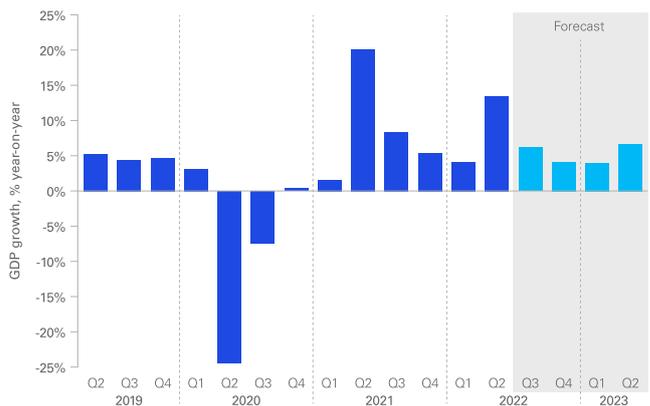
With the global economy suffering repeated shocks with surges in inflation, sluggish growth across countries, and monetary policy tightening, the ripples are also being felt in India, discernible from the high inflation. However, the country’s economy grew by 13.5% in Q1 of fiscal year 2022-23 backed by improvement in private consumption, largely on the back of the reopening of the services sector. As India celebrates 75 years of its independence, the country has emerged as the fifth largest economy in the world replacing the UK, in value terms. As India celebrates 75 years of its independence, the country has emerged as the fifth largest economy in the world replacing the UK, in value terms, and is expected to rank among the fastest growing globally, with the Reserve Bank of India (RBI) projecting a GDP growth of 7.2% for the fiscal year 2022-23.

**Table 7: KPMG forecasts for India**

	2021	2022	2023
GDP	8.7	7.2	6.3
Inflation	5.5	6.7	5.0
Unemployment rate	8.0	7.6	7.1

Source: Ministry of Statistics and Programme Implementation; CMIE, KPMG analysis.  
 Note: The years represent the April-March period; for instance, 2021 spans from April 2021 to March 2022. Real GDP numbers (at constant prices) for 2022 and 2023 and inflation rates for 2022 are advanced estimates by National Statistical Office (NSO) and the RBI’s survey of professional forecasters.

**Chart 25: India’s quarterly GDP growth**



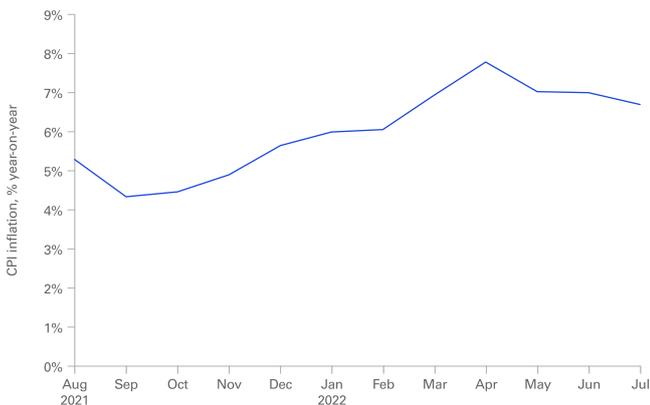
Source: Survey of Professional Forecasters, RBI and National Statistical Office.



An uptick in domestic economic activity is observable, with indicators of urban and rural demand such as automobile sales, consumer durables manufacture, and domestic air travel showing improvement. A positive movement in domestic demand is discernible from the robust import requirements for non-oil and non-gold commodities. Rising consumer optimism, improved corporate performance, and enhanced demand for contact-intensive services are expected to drive consumption.

Investments are also rising in the country, and factors such as a capex push by the government, improvement in capacity utilization and widening of bank credit will contribute to ramping up investment activity. In addition, Foreign Portfolio Investors poured over INR56,000 crore (~US\$7.1 billion) in August 2022 after nine months of continued outflows, indicating improved enthusiasm of foreign investors for the Indian equity market, which became the fifth largest recently in terms of market capitalization.

**Chart 26: India's Consumer Price Index**



Source: Ministry of Statistics and Programme Implementation.  
 Note: Inflation rate for July 2022 is provisional.

Unemployment rates, however, surged to a 12-month high of close to 8.3% in August 2022. Rural unemployment, which had been affected by factors such as erratic rainfall, is expected to decrease towards the end of the monsoon season, as agricultural job opportunities increase. However, concerns around the trajectory of urban unemployment are expected to persist in the immediate future.

Retail inflation, which was one of the highest in April 2022 (nearly 7.8%) due to the high prices of articles such as food and fuel, has witnessed a downward trend since May 2022. The government's reduction of excise duties on fuel in May, coupled with three interest rate hikes by RBI this year to 5.4% have helped moderate inflation. However, the central bank expects inflation to remain high in fiscal year 2022-23 at 6.7%, owing to effects of the global geopolitical headwinds. Furthermore, the appreciation of the U.S. dollar is a factor contributing to inflationary pressures.

The government's production-linked incentive (PLI) schemes are also promoting domestic manufacturing and job creation, with investment commitments of INR2.34 lakh crore (~US\$29.53 billion) as of April 2022. PLI schemes are also being considered for additional sectors such as furniture and toys, which will help bolster domestic manufacturing.

Over the coming years, India is expected to continue on its path of economic growth and become a US\$5 trillion economy by 2027. However, geopolitical uncertainties and tensions coupled with inflationary pressures and monetary tightening in economies like the U.S. and elsewhere are cautionary factors that could affect growth estimates.

**Preeti Sitaram**

Director, Government & Public Services, KPMG in India



# Australia: Mounting headwinds set to weigh on growth

The Australian economy has proven resilient to recent headwinds, achieving solid growth in H1 2022.

Rising inflation, a tight labor market and strong growth are forcing the RBA to hike rates aggressively.

As the full impact of the recent rate rises flows into the economy in the months ahead, growth and inflation are expected to moderate in 2023.

## Households resilient despite headwinds

Supply chain disruptions, elevated commodity prices, and rising interest rates are all weighing on economic activity to some extent. But households have thus far shaken off these pressures and are continuing to lead solid GDP growth. Helped by the release of pent-up demand from 2021’s Delta lockdown, consumption rose by 2.2% quarter-on-quarter in both Q1 and Q2, well above trend growth. The increase in spending is being led by a rebound in services, with households continuing to normalize their spending patterns.

Despite the lockdowns and real estate downturn in China, which are disrupting construction activity and demand for iron ore, strong demand for Australian energy exports has helped lift the trade balance to new highs. While some of that reflects elevated commodity prices, export volumes have increased too. Indeed, net trade (the difference between export and import volumes) made a 1 percentage point contribution to GDP growth in Q2.

Notwithstanding the robust growth in disposable income, which increased by 1% on the quarter in Q2, households have partly funded additional consumption in recent quarters by reducing their saving rate. The household saving rate is now 8.7%, still a little above its pre-Covid level, but at its lowest level in two years.

**Table 8: KPMG forecasts for Australia**

	2021	2022	2023
GDP	4.9	4.2	2.2
Inflation	2.9	6.3	5.2
Unemployment rate	5.1	3.8	4.4

Source: Australian Bureau of Statistics, KPMG analysis.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate.





## Businesses still signalling rising investment, government spending set to moderate

A rebound in business investment is likely in the near term, as the impact of the recent floods on building construction activity ease and firms continue to take advantage of tax incentives. The ongoing recovery in services exports, together with a recovery in inward migration, will also encourage firms to expand capacity. But overall, we expect momentum to moderate as the environment deteriorates. And after two years of outsized increases in government spending, we expect expenditure to fall back slightly, as emergency pandemic expenditure finally comes to an end.

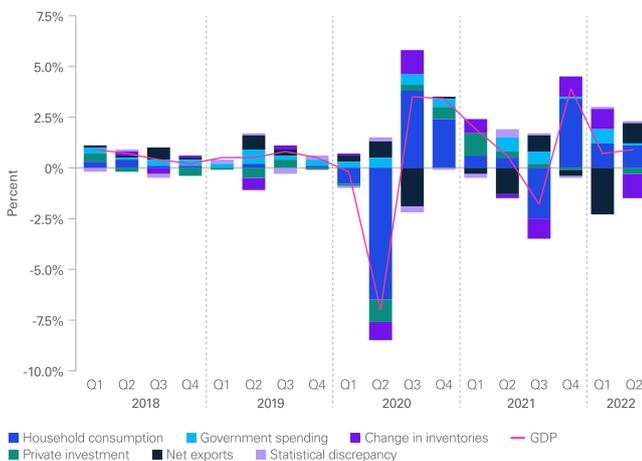
Overall, GDP growth momentum is expected to ease going through H2 2022, to a trough in mid-2023. But we still expect the economy to escape a recession, given its positive fundamentals.

## Inflationary pressure easing but still elevated

Oil prices have eased in recent months, but overall energy prices remain very high. The war in Ukraine has also put pressure on food prices globally and those pressures have been exacerbated in Australia due to the floods disrupting agricultural activity. In addition, escalating construction costs and rising housing rents are providing a significant boost to headline inflation. Taken together the headline inflation rate reached 6.1% in Q2, and trimmed mean inflation rose to 4.9%, the highest rate for each series since 1991.

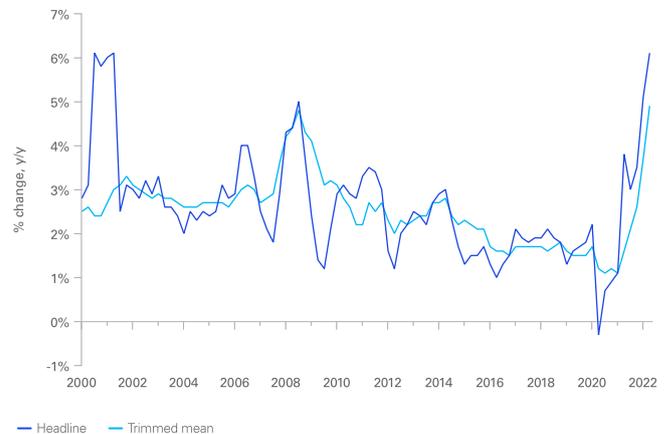
Businesses are reporting that purchase cost are continuing to surge, consistent with inflation increasing further in the near term. The ending of the Government’s fuel excise reduction is set to boost inflation to a peak of more than 7% in Q4. Thereafter, the modest easing in energy prices, the unwinding of flood impacts on food price, and softening demand momentum should see inflation moderate.

Chart 27: Quarterly GDP growth by component, Australia



Source: KPMG Economics, Australian Bureau of Statistics, Macrobond.

Chart 28: Australia’s CPI inflation



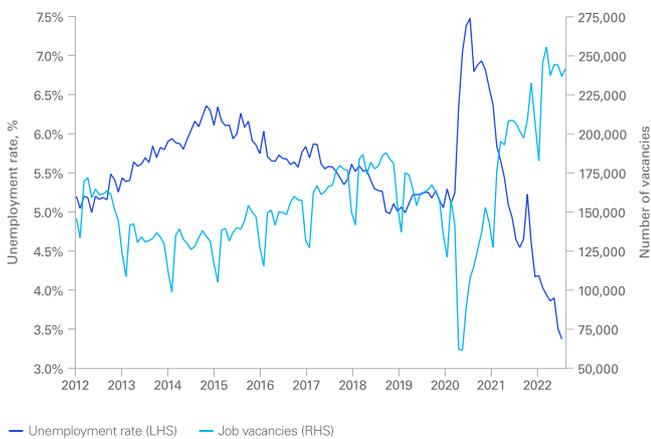
Source: KPMG Economics, Australian Bureau of Statistics, Macrobond.

## Labor market tightness stoking wage growth

The tightening in the labor market has continued in recent months. The participation rate remains close to its recent record high. But employment growth has been robust and there are now more job vacancies than unemployed people in Australia. Looking ahead, a slowdown in growth and a rebound in net migration should start to take some of the tightness out of the labor market. But given the huge backlog of job vacancies, the labor market is likely to remain very tight for some time to come.

The tight labor market is finally spurring wage growth. To be sure, the pace of wage inflation remains low compared to many advanced economies. Annual growth in the wage price index reached 2.6% in Q2, a little above its 2019 peak of 2.4%. But the historically large 5.2% increase in the minimum wage in Q3, further tightening in the labor market and continued rise in inflation mean that wage growth will likely accelerate in the months ahead.

**Chart 29: Job vacancies and the unemployment rate, Australia**



Source: KPMG Economics, ANZ, Australian Bureau of Statistics, Macrobond.

## RBA raising rates rapidly to cool domestic inflation pressures

The rapid rise in inflation and tight labor market has forced the RBA to accelerate its hiking cycle. The cash rate is now at 2.35% and Governor Lowe has indicated that further rate hikes will be needed in the months ahead. But we expect the pace of tightening to slow from here. By the end of this year we expect the cash rate to have reached 3.1%, with a further 0.25%pt hike possible in early 2023. Further significant hikes beyond this increase the risk that the Bank overshoots and tightens rates too aggressively. If that turns out to be the case, the RBA would probably need to reverse course and cut rates in late 2023 or early 2024.

**Ben Udy**

Economist & Senior Manager, KPMG in Australia

**Dr. Sarah Hunter**

Senior Economist & Partner, KPMG in Australia

# Germany: Europe’s biggest economy threatened by recession

Positive first half-year overshadowed by negative expectations.

High energy prices and gas shortage endangering economic growth.

New government package to fight high inflation.

The Russian invasion of Ukraine and its consequences continue to significantly affect the economic outlook for Germany. Real GDP grew by 0.1% in the second quarter of 2022, in comparison to Q1. Compared to Q2 of the previous year, the German economy grew by 1.7%. Real GDP has now reached pre-Covid levels. As governmental measures in response to the pandemic were lifted with the end of Q1, private consumption, for leisure and travelling, increased by 0.8% compared to the first three months of the year. Government consumption on the other hand increased by 2.3% in the second quarter with a focus on social services. In addition to that – and despite trade disruptions due to sanctions against Russian firms – German exports increased by 0.3% in the second quarter of the year.

The sentiment in the German business world, however, has cooled significantly. The ifo Business Climate Index fell to 88.5 points in August, reaching its lowest level since June 2020. Companies are expecting business prospects to become much more difficult in the coming months. They were also less satisfied with their current situation.

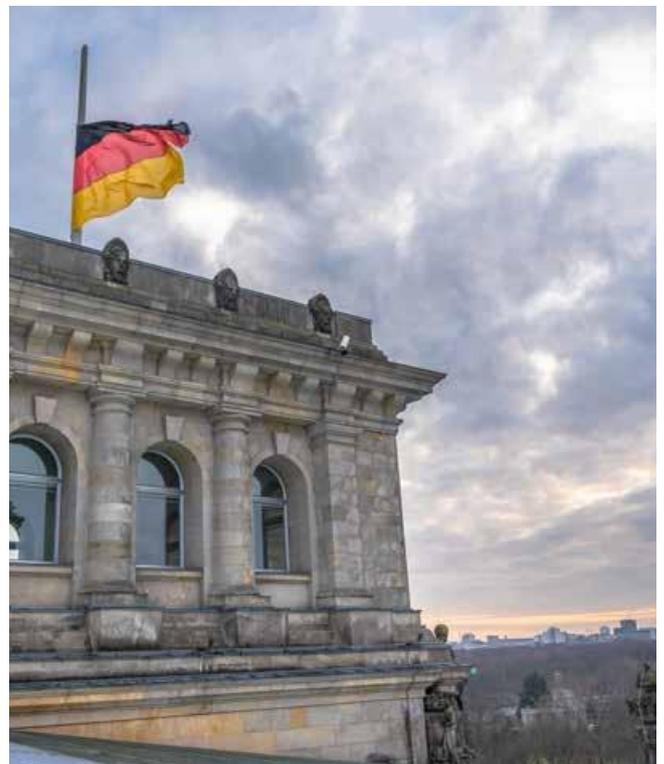
Higher energy prices and the threat of a gas shortage are weighing on the economy. In August, energy prices were 35.6% higher than in August 2021. In the same context, the electricity price for industry exceeded that for households for the first time. Until the beginning of the invasion in Ukraine, Germany obtained a significant share of its gas imports from Russia (55% in 2021). As a result of the country’s efforts to become less dependent on Russian gas, imports fell sharply in 2022. High demand for electricity, massive price jumps on the procurement markets, expensive production and uncertainty regarding gas imports will likely cause the price of energy to rise further in the coming months.

**Table 9: KPMG forecasts for Germany**

	2021	2022	2023
GDP	2.6	1.5	-0.5
Inflation	3.2	8.0	6.8
Unemployment rate	3.6	2.9	3.0

Source: Eurostat, KPMG forecasts.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Inflation measure used is the HICP.



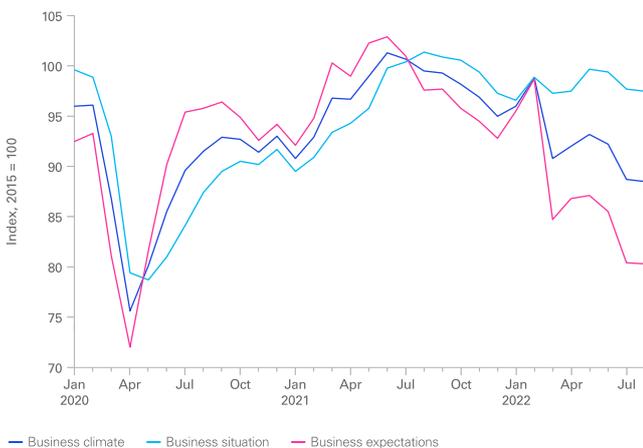
Accordingly, Germany experienced an inflation rate of 8.2% in Q2, while wages increased by only 2.9% compared to Q1. HICP inflation rate reached 8.8% in August 2022. The high inflation will slow the recently recovered private consumption, resulting in lower growth expectations. The German economy is crucially dependent on trade and exports. Exporting companies are suffering significantly from the overall global recession and decreasing demand from their most important trade partners. Developments in the main exports markets (China, the U.S., Western Europe) are not favorable for the German export industries.

**Chart 30: Headline and core HICP inflation in Germany**



Source: Eurostat.  
 Note: Core inflation excludes energy, food, alcohol and tobacco.

**Chart 31: ifo Business Climate Index for Germany**



Source: ifo Institute.

Supply chain disruptions, amplified by China’s zero-Covid strategy, are the main challenge for several industries, including key sectors such as the mechanical engineering as well as the automotive industry. These disruptions are expected to continue well into 2023. Because of material bottlenecks, more than one in two companies have already changed their procurement strategy for critical raw materials.

German fiscal policy in 2022 is influenced by benefits spending, such as transfers and tax reductions. Surprisingly, the government deficit was reduced to EUR13 billion in Q2, corresponding to 0.7% of GDP. This stems from a large increase of nearly 8% in tax income while expenditures, for example to support the labor market, increased by only 0.2%. These numbers, however, must be taken with a grain of salt, since corporate tax intake was inflated by higher nominal revenues and VAT-intake by an increase in prices. In comparison to the much higher deficit rate of 4.3% in the first half of 2021 though, the federal government has now some financial liberties to undertake measures aimed at increasing private consumption and counteracting the loss of purchasing power.

To ease the burden on households, the German government has signed off on a new EUR65 billion relief package. This third package is designed – in part – to support households struggling with the soaring cost of energy and other basic necessities. Measures include one-off payments to pensioners and students, higher child benefits and an electricity price cap for basic consumption.

In general, there is a need to adjust the economic forecasts for 2022 as well as for 2023 due to recent developments. After growing by 2.6% in 2021, we are expecting an increase of German real GDP by 1.5% for the year 2022 with a projected inflation rate of 8.0%. For 2023, we expect to see GDP growth of -0.5% and a lower inflation rate of 6.8%.

The future pandemic situation, however, could still be an important factor impacting economic growth for the next months in Germany. The German government has recently presented new measures aiming to reduce higher Covid-infections during the upcoming winter, leaving an option for each State (Bundesländer) to pass their own – possibly stricter – measures.

**Dr. Ventzislav Kartchev**  
 Head of Business Intelligence/Markets, KPMG Germany

# Austria: Strong energy headwinds – and fiscal support

Austrian recovery from Covid supported by ongoing strong fiscal support and private and corporate transfers.

Strong exposure to Russian gas imports has led to an increase in energy prices with risks to industry and consumption dynamics.

Elevated inflation with low, but positive, growth in 2023 as key forecast. Risks from a full stop in gas supply would trigger a recessionary environment.



Austria’s fiscal response to Covid was strong: 15.2% of GDP was spent as support measures in Austria, comparable to Germany (15.3%). This softened the downturn, especially cushioning losses in the services and tourism sector. Employment remained strong, with unemployment rate expected to fall to 4.6% in 2022. Austria’s 2021 upswing was robust (4.8%), led by strong industrial dynamics, despite the strong concentration of winter tourism and hospitality sectors in Austrian GDP.

Strong winter tourism dynamics contributed positively to 2022 GDP, with a particular boost to Q1. Nevertheless, tourism is still only at 64%, compared to 2019 levels. That said, Austria is currently exposed to simultaneous supply side shocks, exacerbated – if not entirely caused – by the war in Ukraine.

**Table 10: KPMG forecasts for Austria**

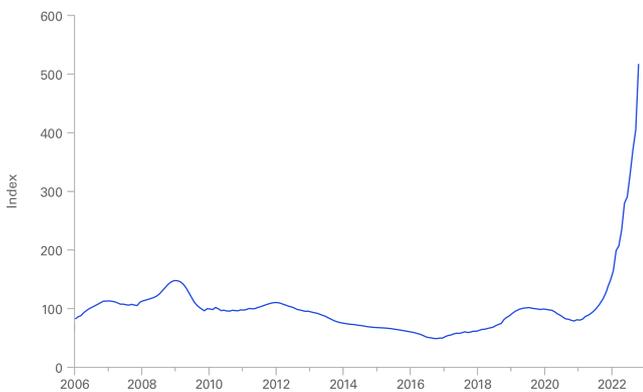
	2021	2022	2023
GDP	4.8	3.9	0.3
Inflation	2.8	8.5	5.8
Unemployment rate	6.2	4.6	4.6

Source: Eurostat, KPMG forecasts.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Inflation measure used is the HICP.

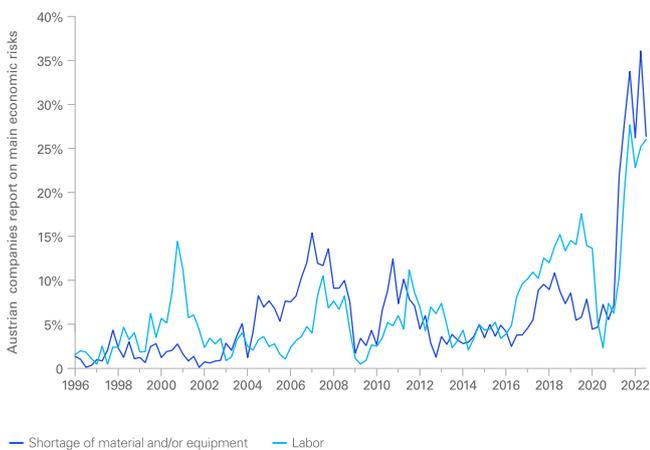
Gas and energy prices lead the current economic and political discussion, with reduced but still significant Austrian exposure to Russian gas exports (86%, compared to 49% for Germany, in 2021). The main risk, correlating strongly with gas prices, is electricity prices, which have risen dramatically (by over 400% compared to 2020 levels). This poses price risks for corporates and households, contributing significantly to inflation. Government measures to compensate for increasing energy prices are on the way, and will limit the fall in purchasing power, but at the cost of worsening the fiscal deficit, which has already been increased by strong Covid compensation (with government debt at 82.8% of GDP in 2021).

**Chart 32: Austrian Electricity Price Index**



Source: Austrian Energy Agency.

**Chart 33: Factors limiting production (industry), Austria**



Source: European Commission, KPMG analysis.

Supply chain disruptions, causing limitations to production and cost increases, are still persistent in many sectors. More than 40% of Austrian companies considered supply shortages as main economic risk in summer 2022.

Further risk stems from skill shortages across a range of economic sectors, tightened by Covid, but mainly driven by structural issues that have already been in place before the pandemic and the Ukraine war. More than 30% of Austrian service sector firms report non-availability of labor force as their main risk.

Driven by the supply side shock, Austrian inflation rate is expected to average 8.3% in 2022, while strong wage increases in autumn negotiations can be expected, reducing real income losses. Combined with strong fiscal response to both Covid and energy prices, prospects for households might turn out better than for other European peers, supporting consumption and therefore stabilizing GDP growth rates.

This comes at a cost of further deteriorating fiscal balance. Looking beyond the current crisis, consolidating measures and strategies for tackling structural issues are key for supporting future growth.

Based on these assumptions, we forecast the Austrian economy to grow by 3.9% in 2022, followed by a 0.3% growth in 2023, therefore not expecting an outright fall in 2023. Nevertheless, quarters with negative growth, especially in winter 2022/23, are not unlikely. Inflation will remain significantly above the ECB target, projected at 5.8% in 2023.

Major downside risk to the forecast is a full stop in gas delivery in autumn/winter, ending in a strong recession in 2023 and higher inflation rates than in the main scenario.

Over the medium term, annual growth is projected to recover to around 1.8%.

**Dr. Stefan Fink**  
Chief Economist, KPMG in Austria

# France: A costly shield from inflation

Robust growth in 2022 H1 conceals vulnerabilities facing households and businesses.

Inflation to peak at a lower level compared to its Eurozone peers thanks to the EUR72 billion tariff shield.

Unemployment is set to increase from current levels owing to a deterioration in the economic outlook.

After falling by 0.2% in 2022 Q1, the French economy registered solid growth of 0.5% in the second quarter of 2022. The composition of growth was broad-based, with household consumption, investment and net trade all contributing positively. The rebound was partly driven by a seasonal boost from tourism following the easing of Covid restrictions in March. GDP is now 0.9% above its pre-Covid level, although the majority of the increase (0.8 percentage points) can be accounted for by stronger government consumption.

Business and consumer surveys paint a gloomier picture for the near-term outlook. Consumer confidence is hovering close to its lowest levels since records began, while PMI surveys suggest subdued business confidence across all of the three main sector groups. While the shortage of labor and materials has reached its highest level for at least 30 years – limiting capacity – concerns around the outlook for demand are likely to weigh on production going forward.

We have revised down our forecast for GDP growth for this year and next. Despite robust performance so far this year, uncertainty around a weakening domestic demand, coupled with a deteriorating external environment, will likely see a significant slowdown in the latter part of this year and into 2023. We now expect GDP growth of 2.5% in 2022 and 0.6% in 2023.

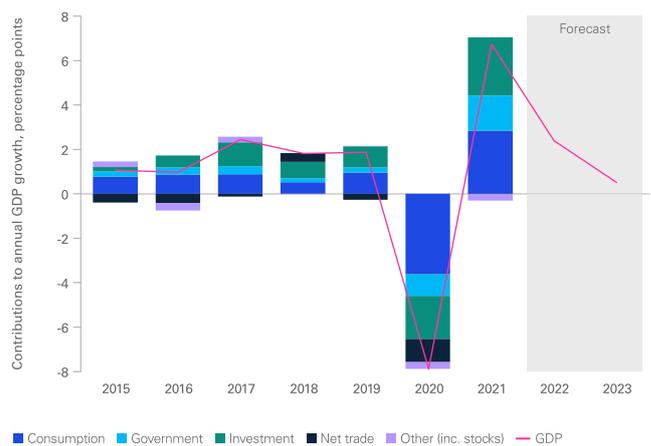
**Table 11: KPMG forecasts for France**

	2021	2022	2023
GDP	6.8	2.5	0.6
Inflation	2.1	5.9	3.9
Unemployment rate	7.9	7.5	7.7

Source: Eurostat, KPMG forecasts.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Inflation measure used is the HICP.

**Chart 34: Outlook for the French economy**



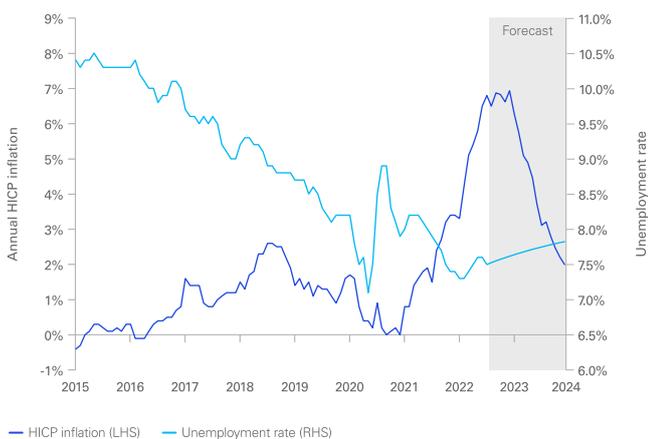
Source: Eurostat, KPMG analysis.



Annual HICP inflation eased to 6.6% in August, down from 6.8% in July but well above the 2.4% level recorded a year earlier. Although energy inflation slowed significantly in August, core inflation picked up to 4.1%. Nevertheless, France registered the lowest headline inflation in the EU. The main reasons for lower inflation in France have been due to a combination of its energy mix and the government’s measures to cap energy prices paid by households. Imports from Russia account for around 8.5% of gross available energy in France, which instead relies on its large nuclear fleet to generate power.

The French government has so far allocated a package of measures (“tariff shield”) worth EUR72 billion (2.9% of GDP) to protect consumers from rising energy costs<sup>1</sup>. These include a freeze of gas tariffs (worth EUR7.8 billion) and a cap on electricity price increases of 4% this year (worth EUR10.5 billion). These measures have been largely effective in keeping consumer prices in check: the National Institute of Statistics and Economic Studies (INSEE) found that the policy had prevented inflation from rising by 3.1 percentage points in the year to 2022 Q2. However, a recent announcement that the tariff shield would remain in place in 2023, costing EUR16 billion, would result in significant further pressure on the public finances.

**Chart 35: Outlook for French inflation and unemployment**



Source: Eurostat, KPMG analysis.

The French labor market remains tight. The unemployment rate fell to a low of 7.3% at the start of 2022, although the downward trend has reversed in recent months. Relative to pre-Covid levels, the participation rate has increased, in particular among females aged 20-24. This is potentially thanks to more widespread hybrid arrangements that allow greater flexibility. We expect the unemployment rate to gently increase as demand weakens, averaging 7.5% this year and 7.7% in 2023.

**Michal Stelmach**  
Senior Economist, KPMG in the UK

<sup>1</sup> Bruegel, *National policies to shield consumers from rising energy prices*, accessed 22 September 2022.

# Italy: Misty outlook amid mounting headwinds

A strong start to the year driven by a recovery in tourism turns to fears of a downturn as economic conditions deteriorate.

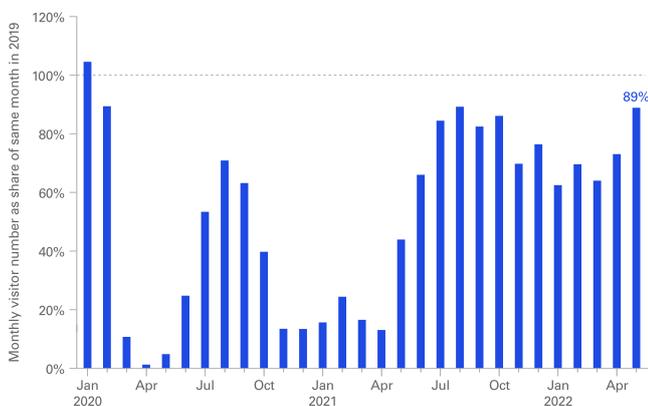
High inflation, driven by rising energy and food prices, is squeezing household budgets.

Stretched public finances, additional uncertainty regarding gas supplies, and political volatility pose significant downside risks to the outlook.

The resumption of travel following the relaxation of pandemic restrictions has helped support growth in the Italian economy during the first half of 2022. The overall number of visitors in May this year climbed to 89% of the levels seen in the same month of 2019, prior to the pandemic (see Chart 36). Meanwhile, GDP growth in the second quarter rose to 1.1%, following on from a weaker 0.1% in the first quarter of 2022.

However, surveys point to a deteriorating economic environment, signalling a slowdown in growth and a potential downturn on the horizon. In August, purchasing managers' indices across all three groupings of services, manufacturing and construction were showing readings of less than 50, pointing to a contraction. In addition, overall consumer confidence showed signs of weakness, with the ISTAT consumer confidence index falling to a post-pandemic low of 94.8 in July, before rising only modestly to 98.3 in August.

**Chart 36: Recovery in Italy's tourism has helped drive a stronger growth early in 2022**



Source: Istituto Nazionale di Statistica, KPMG analysis.

**Table 12: KPMG forecasts for Italy**

	2021	2022	2023
GDP	6.6	3.3	0.3
Inflation	1.9	8.1	4.9
Unemployment rate	9.5	8.2	8.5

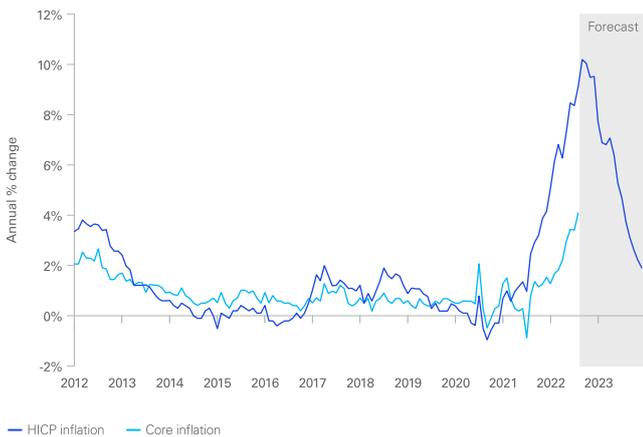
Source: Istituto Nazionale di Statistica, Eurostat, KPMG analysis.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Inflation measure used is HICP.



Inflation reached 9.1% in August, driven by a combination of rising energy and food prices, compared to 3.9% for core inflation, which excludes these components (see Chart 37). The ongoing turmoil in energy markets caused by uncertainties regarding Russian gas supplies is adding to pressure on household budgets and raising costs for businesses. Higher costs for businesses may in turn lead to further price rises which would continue to put upward pressure on inflation throughout the rest of this year. However, a recent fall in global food prices, which surged in the aftermath of Russia’s invasion of Ukraine, could see a modest relief to inflationary pressures later this year and during 2023. Overall inflation is expected to already be close to its peak, and to gradually fall back to 2% during the course of 2023.

**Chart 37: Italy’s inflation remains driven by energy and food components**



Source: Istituto Nazionale di Statistica, KPMG analysis.  
 Note: Core inflation represents HICP excluding energy, food, alcohol and tobacco.

Latest unemployment figures were at their lowest outside of the pandemic, at 7.9% in July of this year, which points to a degree of tightness in the labor market. However, an expected slowdown in growth could see the unemployment rate rise to 8.7% by the end of 2023.

The risk of a full interruption of Russian gas supplies could be particularly damaging to the Italian economy, which in 2020 relied on supplies from Russia for around 43% of total gas imports<sup>1</sup>. A full gas shut-off could necessitate measures such as gas rationing and price controls, and lead to as much as a 3.9 percentage point reduction in the level of GDP over 12 months<sup>2</sup>.

Tighter monetary policy by the ECB is especially challenging for the sustainability of Italy’s public sector finances. With overall government debt at over 150% of GDP in 2021, the second highest in the Eurozone, the cost of servicing the debt increases significantly as interest rates rise. Yields on Italian government bonds have risen from 1.3% to 3.3% during this year alone and are now more than three percentage points above the German yields, reflecting markets’ perceptions of a higher risk. Moreover, the victory of the centre right coalition led by Brothers of Italy could create additional uncertainties regarding the country’s relationship with the EU. A potentially slower pace of reforms could lead to tensions over the disbursement of the nearly EUR200 billion of EU funds allocated through the Covid recovery fund to Italy, which could generate additional headwinds for the Italian economy.

Despite the difficult domestic outlook, the Italian manufacturing sector remains an area of strength through its reliance on export markets. By the second quarter of this year, the real value of goods exports from Italy exceeded pre-pandemic levels by 9.7% and could help support overall GDP growth in our forecast as long as energy supplies are not curtailed.

**Dennis Tatarkov**  
 Senior Economist, KPMG in the UK

<sup>1</sup> Eurostat, <https://ec.europa.eu/eurostat/cache/infographs/energy/bloc-2c.html>  
<sup>2</sup> IMF; Gabriel Di Bella, Mark J Flanagan, Karim Foda, Svitlana Maslova, Alex Pienkowski, Martin Stuermer, Frederik G Toscani; *Natural Gas in Europe: The Potential Impact of Disruptions to Supply*; Working Paper No. 2022/145; July 2022

# The Netherlands: Inflationary squeeze weighs on economic growth

The Dutch economy to stagnate during the second half of 2022, as carry-over from 2021 loses momentum.

Private consumption expected to soften amid inflationary pressures.

Economic slowdown to be partially offset by expansionary fiscal policies.

The strong recovery of the Dutch economy after the pandemic continued in the first half of 2022, with an average annual growth of 5.9%. Higher household consumption of accommodation and food services as well as more investments in buildings and transport supported this. However, economic growth is expected to hit a speed bump in the second half of the year as the surge in inflation squeezes households' disposable income and businesses face headwinds from high input prices, higher interest rates, tax arrears and heightened economic and geopolitical uncertainty. Despite the labor market remaining tight with a low unemployment rate, consumer confidence recorded an all-time low in August for the fourth time this year. While producer confidence remained broadly unchanged, manufacturers' sentiment about future production and order book already showed signs of deterioration in August, according to the CBS (Statistics Netherlands).

As a result, we have lowered our GDP growth forecasts to 3% in 2022 and 1% in 2023. Even though the economy is expected to experience stagnation in the second half of 2022, annual growth remains robust in 2022 due to carry-over effects from the strong recovery from Covid in 2021. Risks to the outlook remain skewed to the downside. Persistent high energy and food prices and a worsening of the outlook of Netherland's main trading partners (Germany, Belgium, UK and France) would lead to lower consumption and investment levels.

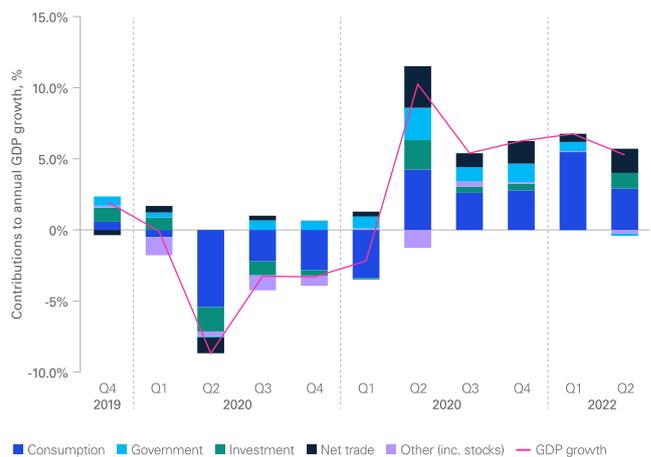
**Table 13: KPMG forecasts for the Netherlands**

	2021	2022	2023
GDP	4.9	3.0	1.0
Inflation	2.8	10.1	3.9
Unemployment rate	4.2	3.6	3.8

Source: Statistics Netherlands, Eurostat, KPMG forecasts.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Inflation rate measure is HICP.

**Chart 38: Economic growth by demand components, the Netherlands**



Source: Statistics Netherlands, KPMG analysis.

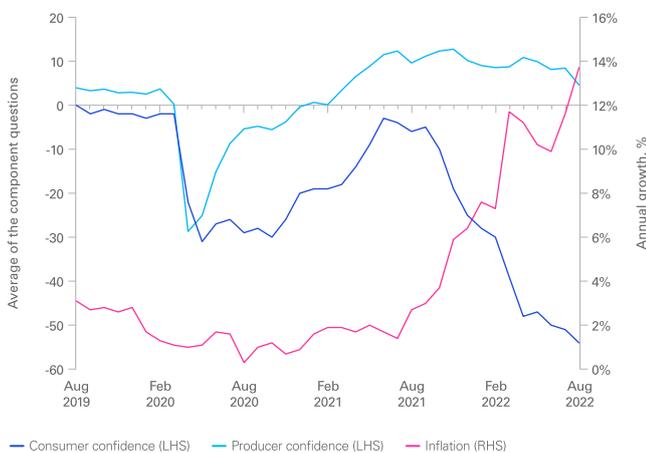


HICP inflation recorded double-digit annual figures in July (11.6%) and August (13.7%). Although this high headline inflation is mainly driven by sky-high energy prices, core inflation (HICP excluding energy and food) has also risen sharply due to higher input prices and wages. CBS reported that annual inflation on food, drink, and tobacco grew by over 10% in August. This led us to revise upwards our inflation forecasts to 10.1% in 2022 and 3.9% in 2023. The Dutch government activated an energy crisis plan in June to reduce reliance on Russian gas (around 15% of Dutch gas imports), which included buying LNG, cutting back gas consumption and removing the caps on coal plants during 2022-2024. At the time of writing, the Netherlands has hit the 80% EU target on gas storage, ahead of the target date of November 1 set by the EU. The government has announced that gas storage facilities will continue to be filled in order to create an additional buffer, absorbing potential setbacks. This strategy has gained greater importance after the shutdown of the Nord Stream 1 pipeline.

The spring update on the fiscal budget signaled a more expansionary stance, with policy measures such as a structural increase in defense spending (EUR2.2bn) to achieve 2% of GDP by 2024 in line with the NATO target, and linking the state pensions to changes in minimum wages (EUR2.4bn). The government has announced taxes on energy bills will be significantly reduced in 2023, an energy allowance will be paid to the most vulnerable households, and an increase of 10% in minimum wage in 2023. The fiscal deficit is not expected to increase significantly in 2022 due to the scaling back of Covid-19 testing and vaccination programs, and will increase slightly to 3% of GDP in 2023. However, there are medium and long-term risks associated to an increasing national debt-to-GDP ratio to be passed on to future generations.

**Diego Vilchez Neira**  
Senior Manager, KPMG in the Netherlands

**Chart 39: Dutch consumer confidence plummets as inflation accelerates**



Source: Statistics Netherlands, KPMG analysis.

# Ireland: Recent momentum, stumbles against headwinds

Ireland enjoying very strong economic growth, but some uncertainty remains as to strength and robustness.

Cost of living pressures eroding disposable incomes. Government well-positioned to help cushion impacts of price increases.

Bottlenecks and gaps in supply of infrastructure, housing, and utilities are hampering growth and competitiveness.

Ireland’s economy has been performing strongly for a number of years, and was one of a small number of countries to experience growth during the pandemic. As with most countries in Europe, Ireland is facing global downturn risks and a major cost of living challenge. Domestically, infrastructure bottlenecks are a further barrier to growth. These three core themes drive Ireland’s economic prospects for the remainder of 2022 and into 2023.

Global-domestic interdependencies have been key drivers of Ireland’s economic fortune over the past two decades. On the upside, the country’s skilled and open labor market, talent pipeline, and easy access to both the European and UK market, are all likely to contribute to growth over the coming years. Ireland’s strong industrial base in key sectors – in particular in Life Sciences and ICT – both owes and lends itself to multi-decade long investment by multi-nationals. Foreign direct investment (FDI) appetite remains strong post-pandemic and post-Brexit, and further investment can be expected in the medium-term, positioning Ireland well to take advantage of wider long-term trends in global economic growth.

On the downside, there are a number of clear and present headwinds. Firstly, Ireland’s close trading relationship with the EU, the UK, and the U.S. – each at risk of recession – creates risks of a downturn if lower demand in these three economies creates negative spill-over effects. To mitigate risks of contagion from key trading partners, Ireland’s export-focused economy has become increasingly diversified, but it is unlikely to be sufficient to fully insulate the country from such shocks.

**Table 14: KPMG forecasts for Ireland**

	2021	2022	2023
GDP	13.4	7.0	4.5
Inflation	2.5	7.5	4.0
Unemployment rate	6.2	4.5	4.5

Source: CBI, CSO, DOF, EC, ESRI, KPMG analysis.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Inflation measure used is the HICP.

Secondly, two economies are present – the multinational-driven economy and the domestic economy – and growth of the former consistently outpaces growth of the latter. At the same time, multi-nationals (MNCs) have been increasingly investing in regions outside Dublin, helping to improve the balance of economic growth across the country.





On the whole, risks to Ireland from the macro environment are clearly trending on the downside. However, any downturn is likely to be less severe than the previous global downturn in 2008-09, as resilience in Ireland's economy has increased.

Consistent with other European countries, cost of living and inflationary pressures are eroding disposable income in Ireland, while increases to already-high prices will reduce competitiveness. Indeed, inflation has begun to permeate all sectors of the economy, beyond its initial immediate impact on energy and primary materials. Prices in Ireland are estimated to have risen by 9.0% in the year to August, and the rising cost of fuel is continuing to drive up inflation. In the year to August, electricity was up 38%, gas up 56%, home heating oil up 72%, petrol up 24%, and diesel up 35% respectively.

Sentiment indices are increasingly highlighting the cautiousness amongst consumers and businesses about winter 2022/23 and beyond. Leading indicators and anecdotal evidence suggest a slowdown is already underway in consumers' spending and investment. By Q4, as heating usage increases along with energy unit pricing, consumers will also begin to feel the squeeze from rising interest rates.

These household-level headwinds mirror concerns amongst policymakers on a national level around costs and affordability. Government debt, repayment costs, and structural reforms have been keywords of successive budgetary packages over the last decade. On the upside, the public finances are currently in rude health: the tax take has never been higher and was 25% above expectations at end-August. As a result, the Government is running a surplus and had the capacity to both increase spending and to reduce taxes in its end-September budget. Many of the measures that have been introduced are one-off measures for 2022, aided by the bonanza exchequer returns. Social transfers through winter will be the cornerstone of the Government's response.

On a wider level, there is a broad agreement that Ireland's economy is being held back by a range of infrastructure bottlenecks. An under-supply of housing, coupled with high levels of inward migration is causing strain domestically, driving high rental and home ownership costs that are eating into workers' disposable incomes. Higher levels of investment in healthcare and education are needed to meet demographic and migration-linked pressures. There is also a need for a ramp-up in spending on low-carbon transport schemes and climate adaptation projects.

The Government's current fiscal position means that it has the requisite finances to make a dent in many of these bottlenecks through multi-year capital programmes. Should negative economic headwinds materialise, there are risks to the Government's ability to fund such projects. Recent Irish government research has found that income tax and corporation tax are highly concentrated around a narrow base of employees and a handful of big companies, creating a "potential vulnerability" at the heart of the Irish tax system. A global shock that affects the multinational and/or the higher end of the wage spectrum will negatively impact Ireland's tax yield.

On the whole, Ireland's economy is in a reasonably strong position in the face of multiple headwinds and downside risks. While cost of living increases are likely to outpace wage growth, Ireland has a good fiscal cushion with which to support low income and disadvantaged groups. At the same time, the breadth of uncertainty as to European and global growth is significant, and actual outturns will not be felt fully until early 2023.

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**Dr. Daragh Mc Greal**

Director, Strategic Economics, KPMG Ireland

# Switzerland: Resilient, but not immune to shocks

The Swiss economy exhibits robust growth, recovering from a lower Covid-induced output gap than its European peers.

Accommodative fiscal and monetary policies should further support growth, although some offset from the war in Ukraine should be expected.

Strength of Swiss Franc increased by a first-mover rate hike of SNB in June – no substantial risk to growth despite softening exports.

The Swiss economy is currently performing well, especially compared to its European peers. Cumulative GDP growth over 2020-2021 was 1.6% (Germany: -1.6%). This was due to agile, supportive policies and the general global upswing. Employment has already surpassed pre-crisis levels, with key factors including ongoing strong pandemic support and accommodative monetary policies. Especially strong export dynamics (watches, instruments, pharmaceuticals), combined with low levels of non-performing loans, have also supported growth.

The economy continued to grow by a robust 0.3% in both Q1 and Q2 2022. The value added to the service sector increased significantly as the Covid restrictions were lifted at the beginning of April. Within the service industry, accommodation and food services was the fastest-growing sub-sector with growth of 12.4% from the previous quarter.

In contrast to the positive growth impulses, exports of goods fell sharply by 11.5% in Q2, due to a significant contraction in transit trade.

A further slowdown in economic growth is expected, with overall 2022 growth rate still robust, but dampened by spillovers from the war in Ukraine. Although direct exposure to the war (exports to impacted markets, financial sector, investment) appears limited, indirect effects (higher energy and commodity prices, supply disruptions, and lower regional and global growth) could be substantial.

Fiscal and monetary policies remain supportive (despite a surprising Swiss National Bank (SNB) rate hike in June), and higher household savings during Covid should support private consumption as a stabilizer of growth. We expect GDP growth of 2.5% in 2022.

**Table 15: KPMG forecasts for Switzerland**

	2021	2022	2023
GDP	4.2	2.5	1.2
Inflation	0.5	2.9	1.8
Unemployment rate	5.1	4.3	4.2

Source: Eurostat, SECO, KPMG forecasts.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Inflation measure used is the HICP.



The war in Ukraine is also likely to continue to affect activity in 2023 with growth softening further, projected at 1.2%. Unemployment is expected to average 4.3% in 2022 (following 5.1% in 2021), and to remain stable in 2023 (4.2%), despite a reduction in Covid support. Inflation is expected to average 2.9% in 2022, before easing to 1.8% in 2023, which means substantially lower inflationary pressure compared to Switzerland’s peers.

With respect to monetary policy, the SNB surprised markets with a strong increase of its policy rate to -0.25% from -0.75%, leading to an even stronger CHF. In addition, as a consequence of increased skepticism over the success of ECB’s fight against inflation, the Swiss Franc has become even more attractive as a “safe” Euro substitute. This is creating a long-term effect, especially in an environment of high energy prices and therefore inflationary pressures. Consensus forecasts for EUR-CHF and USD-CHF are consequently both significantly below parity. A deepening of the Ukraine conflict and more severe impact on Europe could further support CHF demand.

Overall, risks remain skewed to the downside, and the forecast is subject to high uncertainty – with main risks related to a worsening of the war in Ukraine, in terms of scope and duration. This could lead to sharply higher commodity prices, supply disruptions, and even-lower regional and global growth, with risks to financial markets and adverse effects to exports from further deteriorating exchange rates.

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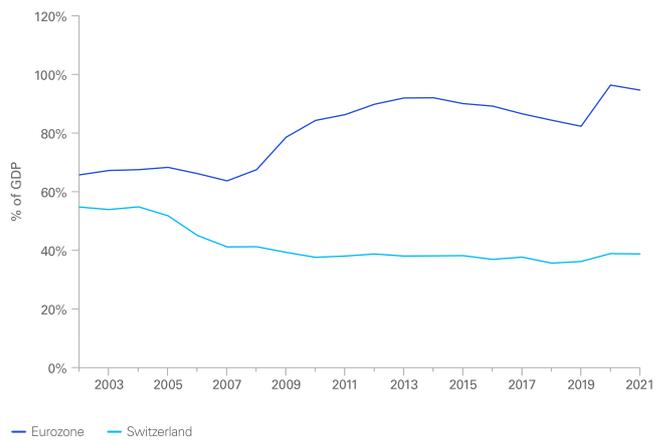
**Dr. Stefan Fink**  
Chief Economist, KPMG in Austria

**Chart 40: CHF exchange rates**



Source: Bloomberg.

**Chart 41: Debt-to-GDP ratio**



Source: Bloomberg.

# UK: Economy marred by stagflation

Inflation set to peak at 10.5% as government policies limit the impact of energy price rises on households' utility bills.

The economy is probably already in a mild recession, with growth expected to stay negative for the rest of this year.

A package of government support measures to households and businesses, and a reversal of major tax increases, are set to provide a large fiscal boost.

The UK outlook continues to be dominated by high levels of inflation, which first reached double digits in July 2022 at 10.1%, before easing to 9.9% in August. Supply chain disruptions, arising during the global recovery from the effects of the pandemic, caused the initial pick-up in inflation in 2021. More recently, the main driver of higher inflation has come from higher energy prices, particularly for natural gas, and elevated food prices, both linked to Russia's invasion of Ukraine.

European and UK gas markets have been extremely volatile throughout the past 12 months as the threat of and the eventual interruption of supplies from Russia has put upward pressure on prices. By August this year, UK domestic energy bills have already risen by 73.2% compared to a year ago. The UK Government's decision to cap domestic energy bills at £2,500 from October 2022 has limited further increases to 27%, avoiding the expected series of sharp rises that could have seen bills rise by another 235% by April 2023. We estimate that these measures will have reduced headline rate of inflation by around 5 percentage points next year (see Chart 42). This will help keep the peak of UK inflation at 10.5% in October this year before it is expected to fall throughout the following two years.

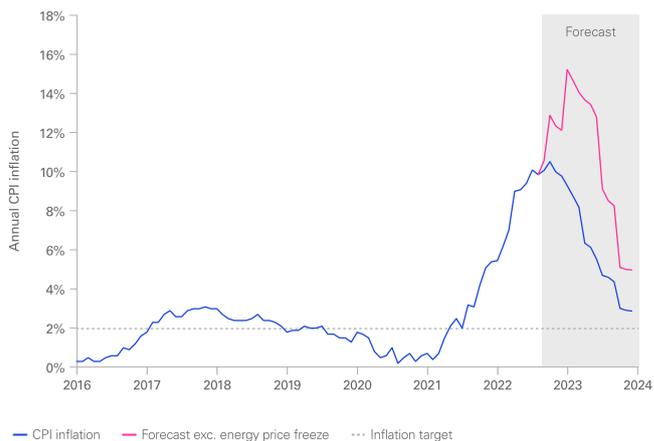
In contrast to natural gas, the prices of other commodities, such as oil, metals and food fell back from peaks reached in the aftermath of Russia's invasion in February. In August alone, the fall in global oil prices helped ease UK inflation to 9.9%, as the prices of automotive fuels fell by 6.8% between July and August. This, in addition to a fall in global food prices which took place between May and July this year, and which is yet to feed into UK consumer prices, should help in bringing inflation down towards the Bank of England's 2% target over the next 6 to 12 months.

Table 16: KPMG forecasts for the UK

	2021	2022	2023
GDP	7.4	3.2	-0.2
Inflation	2.6	8.9	5.6
Unemployment rate	4.5	3.7	4.3

Source: ONS, KPMG forecasts.  
 Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Inflation measure used is the CPI and the unemployment measure is LFS.

Chart 42: Outlook for UK inflation



Source: ONS, KPMG analysis.



The Bank of England has responded to the high levels of inflation by accelerating the pace of monetary policy tightening, and we expect Bank Rate to reach around 3.5% early in 2023. Monetary policy is expected to be more hawkish due to the need to counteract the inflationary impact of the Government’s energy support through this winter, as it has the potential to raise inflation in the medium term by shoring up household incomes and spending against more extreme energy price fluctuations.

The new Government announced a large package of fiscal loosening amounting to around £160 billion over the next two years, equivalent to 3.2% of GDP per annum. This included £45 billion of permanent tax cuts, funded by higher borrowing. Following this announcement, worries about the sustainability of UK public finances have led to a sharp increase in Gilt yields and a fall in the value of the pound.

**Chart 43: Market expectations for the peak in Bank Rate over the next 5 years**



Source: Bank of England, BIS, KPMG analysis.  
 Note: Latest data are for 26 September.

At the time of writing, sterling is down by 6.4% against the U.S. dollar since the start of September, while 5-year gilt yields are around 190 basis points higher. Financial markets now expect interest rates to reach around 6% next year (see Chart 43), although given the latest inflation outlook we find this scenario to be less likely.

The combination of high inflation, which erodes the real value of earnings, and rising interest rates, which raise the cost of debt, have created the conditions for an unprecedented squeeze on household incomes. In September, UK consumer confidence fell to a record low as the effect of the income squeeze was felt by households. This could signal a shift in demand towards more essential goods and services. In addition, a more cautious attitude to spending could lead some to maintain a higher level of savings buffer, which would further weaken consumption growth. We therefore expect overall consumption to grow by 3.7% this year and fall by 0.4% in 2023.

Investment is also expected to remain weak throughout the next 15 months due to weaker growth lowering investment returns, higher cost of borrowing due to tighter financial conditions, and the expected phasing out of the Government’s super deduction scheme on plant and machinery investment, which is due to end in March 2023. Offsetting this may be an increase in public sector investment, although details of specific policies remain unclear. Our latest estimates for investment point to growth of 5.8% in 2022, followed by a milder rise of 1.3% in 2023.

The UK economy is likely to already be in recession since the second quarter of this year, which we expect to last for three quarters. The slowdown in domestic demand has led to a weakening of growth momentum following the boost provided by a post-pandemic recovery early this year. The potential contraction in output among some of the UK’s main trading partners could see further slowdown in export growth this year. Nevertheless, compared to past downturns, the scale of the current downturn could be relatively mild, with the level of GDP falling by 1% between Q1 and Q4 of this year. And despite this, GDP growth is expected to reach 3.2% this year, greatly boosted by weaker GDP in 2021 due to pandemic-related restrictions. Further out, a picture of stop-start growth in 2023 could lead to a full year fall in GDP of 0.2% compared to 2022.

The UK labor market has continued to surprise to the upside this year. The unemployment rate has fallen from a Covid peak of 5.2% at the end of 2020 to 3.6% in the three months to July, its lowest level since 1974. Around three quarters of that fall were due to a rise in employment rate, as slowing population growth has not kept up with the pace of hiring against the backdrop of a tight labor market. In addition, a fall in participation rate – driven largely by an increase in the long-term sick – has inadvertently helped to keep unemployment low. We expect these factors to continue to depress labor supply over the medium term. As a result, we have revised down our forecast for unemployment to 3.7% in 2022.

We then expect the economic slowdown to gradually filter through to the labor market, with lower demand putting less pressure on employers to recruit new staff. Although the job vacancy rate is still around record highs, there are tentative signs that the market could soon begin to slacken. For example, leading indicators – including the KPMG/REC survey – suggest that staff availability has now returned to pre-Covid average, while a drop in average hours (typically seen as an indicator of labor utilization) suggests that weaker demand has so far led firms to use their staff less intensively. Our forecast for 2023 now sees the unemployment rate averaging 4.3%, slightly lower than during the Covid pandemic.

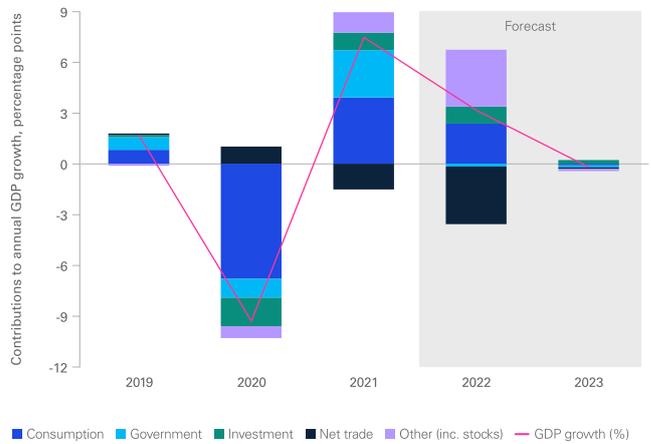
**Michal Stelmach**

Senior Economist, KPMG in the UK

**Dennis Tatarkov**

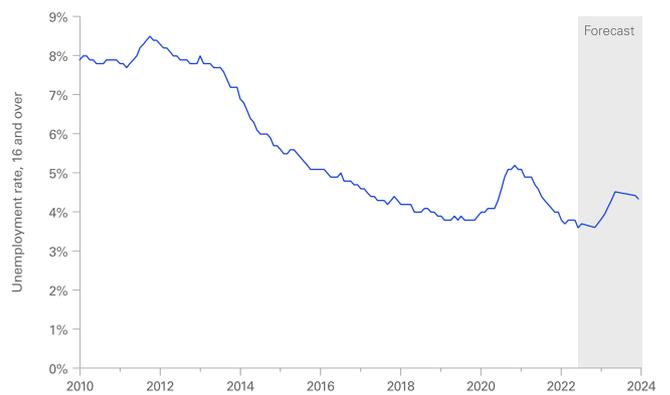
Senior Economist, KPMG in the UK

**Chart 44: Outlook for UK GDP**



Source: ONS, KPMG analysis.

**Chart 45: Outlook for UK unemployment**



Source: ONS, KPMG analysis.

# Central and Eastern Europe: Not a uniform story

Substantial, but varying energy exposure towards Russia leads to heterogenous shock impacts.

Higher GDP growth projections compared to Eurozone peers, but higher inflation rates leading to significant downside risks.

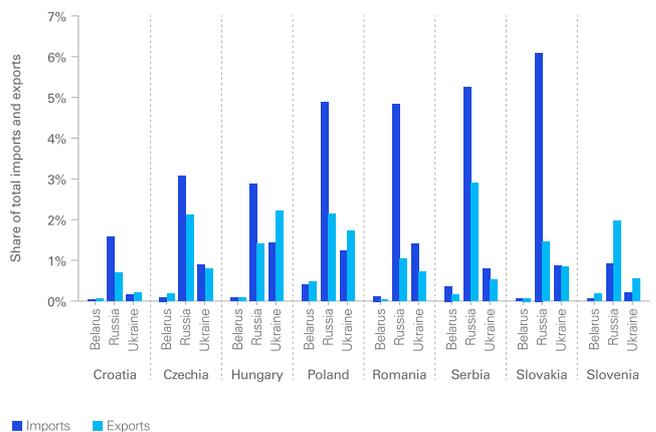
Strong interest rate increases as a response to elevated prices, with only Turkey lowering rates despite galloping inflation.

The central and eastern European countries are subjected to a significant shock from the ongoing war between Russia and Ukraine. Due to their economic interrelations and geographic proximity, CEE countries are specifically at risk from the decoupling of the Russian economy from the West. Nevertheless, despite ongoing sanctions against Russia and Belarus and therefore anticipated collateral damage for the CEE countries (CEE-11<sup>1</sup>, Georgia, Serbia and Turkey), positive growth is expected for the third and fourth quarter of the year, despite a substantial slowdown. Negative effects of the war, sanctions between the West and Russia amid unfolding energy challenges are expected to be dragged far into 2023 and pose a threat to the economic performance and growth of the region.<sup>2</sup> An at least technical recession in some CEE countries is therefore to be expected. Data released in the summer months confirm this scenario, with new challenges ahead. On the inflation side, the economic environment still does not assuage inflationary concerns with the indicators in CEE countries still reaching new highs even if peaks seem near. Energy prices remain a key concern ahead of the winter season while governments pursue anti-inflationary measures that seem increasingly likely to be prolonged or extended in scope.

Despite the war and ongoing sanctions, direct growth losses from trade are limited, as trade relationships between Russia, Ukraine and Belarus and the CEE-11 economies overall are not substantial. As Chart 46 shows, direct import as well as export links between CEE and Ukraine, Russia and Belarus are limited, compared to overall trade volumes (total imports from Russia amount to 1-6.1% and exports to 0.7-2.9%). It is trade links to other countries of the European Union that are essential for the region.



**Chart 46: Share of imports and exports in CEE by trading partner**



Source: UN Comtrade, World Bank, KPMG analysis.

1 CEE-11 countries: Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovenia, Slovakia.

2 Sovereign and Public Sector, Scope Ratings GmbH "Central and Eastern Europe MidYear Sovereign Outlook", July 2022 ([https://www.scopegroup.com/dam/jcr:129f4653-633a-41ab-b756-c4cdf2260787/Scope%20Ratings\\_2022%20Mid-Year%20CEE%20Sovereign%20Outlook.pdf](https://www.scopegroup.com/dam/jcr:129f4653-633a-41ab-b756-c4cdf2260787/Scope%20Ratings_2022%20Mid-Year%20CEE%20Sovereign%20Outlook.pdf))

However, indirect trade links could prove to be a challenging factor for the CEE region. Supply-chain and trade interruptions, either caused by sanctions against or by Russia itself, could potentially cause shortages of key inputs and create logistical bottlenecks. Exports of manufactured goods play a significant role in many CEE economies for which manufacturers themselves are dependent upon imported components.

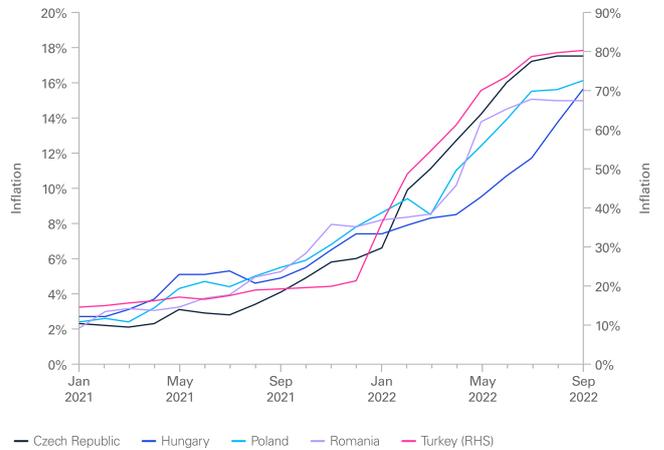
Furthermore, soaring prices of key commodities such as energy or metals have the potential to severely disrupt the economies of the CEE region. It leaves net energy importers such as Georgia, Ukraine, Turkey, Slovakia, Hungary and Serbia particularly exposed. Additionally, 90% of Turkey’s and Georgia’s wheat imports are from Russia and Ukraine. The prices, however, are expected to remain volatile and continue to increase, pushing up inflation and putting government finances and fiscal balance even further under pressure.<sup>3</sup>

Economic and price developments in Turkey are becoming increasingly worrying. Turkey’s inflation rate (> 80% on a year-on-year basis in August 2022), is at a 24-year high. Rising global commodity prices are jeopardizing Turkey’s economic policy, which has sought to combat high inflation with a current account surplus. Furthermore, there are indications that the government will be forced to restrict agricultural exports as Turkish farmers struggle with internationally rising commodity prices, supply chain problems and rising prices of fertilizers and fuels.

Developments are similar throughout the CEE Region. Rising commodity prices, booming demand and supply-side bottlenecks have contributed to a steady and significant increase in inflation. In August, inflation reached 16.1% in Poland, the Czech Republic reported 17.5% and Hungary 15.6%. This strong price momentum is expected to continue in the remaining months of 2022 due to high global energy and food prices and rising core inflation.

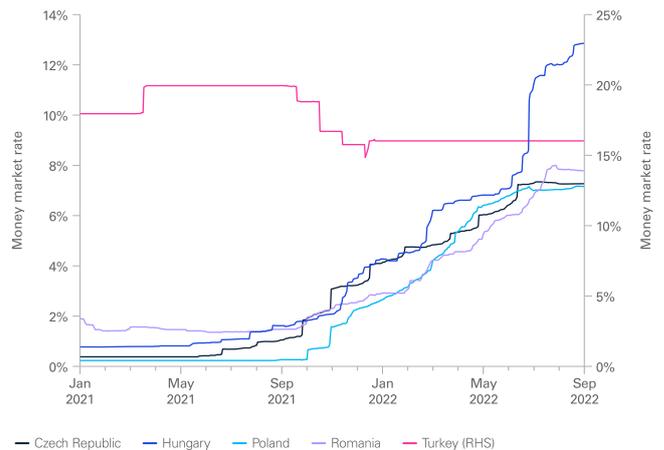
Inflation movements lead to significant increases in central bank rates, being reflected in elevated money market rates, with the strongest increase in Hungary. Despite galloping inflation in Turkey, money market rates came down, exacerbating exchange rate losses of the TRY (effective exchange rate index down by around 50% since end-2020), therefore creating additional inflationary pressure.

Chart 47: CEE Inflation rates, selected countries



Source: Bloomberg.

Chart 48: CEE selected money market rates



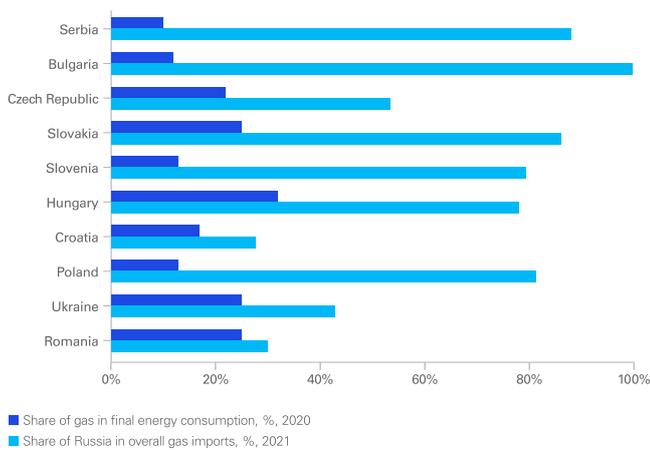
Source: Bloomberg.

3 Sovereign and Public Sector, Scope Ratings GmbH “Central and Eastern Europe MidYear Sovereign Outlook”, July 2022 ([https://www.scopegroup.com/dam/jcr:129f4653-633a-41ab-b756-c4cdf2260787/Scope%20Ratings\\_2022%20Mid-Year%20CEE%20Sovereign%20Outlook.pdf](https://www.scopegroup.com/dam/jcr:129f4653-633a-41ab-b756-c4cdf2260787/Scope%20Ratings_2022%20Mid-Year%20CEE%20Sovereign%20Outlook.pdf))



An important trigger for future development is the lingering problem of Russian gas dependency throughout the CEE. Even though the situation throughout central and eastern Europe proves to be heterogenous, the dependency on Russian gas is high for the majority of countries. Poland, Bulgaria, Slovakia, Slovenia and Hungary are particularly reliant, since more than 80% of gas consumption is sourced from Russia. A more prolonged interruption of gas deliveries could nullify any near-term economic growth, leading to a recessionary outlook and a significant increase of inflation rates.

**Chart 49: Gas dependency, CEE**



Source: Bruegel based on Entso-G and Eurostat.

Several central and eastern European countries are taking action in order to cut reliance on Russian gas or coal, including the Czech Republic. The energy company ČEZ and the Czech state have secured storage capacity in a liquefied natural gas (LNG) terminal in the Netherlands that enables reducing dependence on Russian gas by roughly one-third. Following the outbreak of the war, Poland banned the import of Russian coal, cutting off the main source of domestic coal supply with few substitutes available on the market. As a result, the price of coal skyrocketed from an average of just under PLN1,000 per tonne to more than PLN3,000 per tonne. This contributed to a GDP contraction of 2.3% in Q2 2022 from the previous quarter, raising the likelihood of a recession in 2022.

Set against that, Turkey as well as Hungary are refusing to agree and support the EU sanctions on Russia. Turkey is supplied with more than a third of its natural gas by Russia and at the end of August it came to the agreement of a partial rouble payment system for gas. Hungary, which is about 85% dependent on Russian gas, has lobbied hard to secure an exemption from EU sanctions on Russian crude oil imports and is the only EU member state to have categorically ruled out acting on a plan to cut gas consumption by 15% from August 2022 until March 2023.

**Dr. Stefan Fink**  
Chief Economist, KPMG in Austria

# South Africa: A growth recession as inflation rises

Economic growth back to pre-pandemic levels.

Inflation to peak in 2022 and then return to midpoint of South Africa’s inflation target range.

Current account surplus continues as global growth expectations moderate.

South Africa is returning to pre-Covid levels of economic growth and is currently facing the inflationary implications that arose as a direct consequence of the pandemic and the Russian invasion of Ukraine. Interest rates are rising and, as with the rest of the world, growth prospects are being reduced accordingly.

The South African policy rate has increased from a low of 3.5% in Q3 2021 to a current level of 5.5% and the consensus forecast is for a further increase of around 1 percentage point by the end of 2022. These increases would leave the policy rate at the level recorded prior to the onset of the pandemic and have led to a reduction in potential growth level attainable over the near-term.

Even though increasing interest rates have resulted in slowing growth prospects, the main contributor in this regard remains the insufficient and inconsistent supply of electricity from South Africa’s energy supplier Eskom, with over half of all business days in the second quarter of 2022 experiencing some degree of load shedding or electricity supply restriction. This barrier to growth has been recognized by the government, which in July announced the scrapping of license requirements for private power generators in a sweeping overhaul of the South African energy industry. However, given the lags associated with implementing large scale energy projects, it will take some time before the effects of these policy changes are realized.

South Africa is in a relatively unique position with many of its natural resource exports mirroring those of Russia<sup>1</sup> and consequently it has profited from the rise in commodity prices caused initially by both Covid and, latterly, the conflict in Ukraine. The result of the increase in commodity prices has been an improvement in South Africa’s terms of trade which has led to recent surpluses on its current account since 2020, only returning to deficit in the second quarter of 2022.

**Table 17: KPMG forecasts for South Africa**

	2021	2022	2023
GDP	4.9	1.8	1.5
Inflation	4.6	7.3	6.1
Unemployment rate	35.3	34.3	34.7

Source: Statistics South Africa, KPMG analysis.

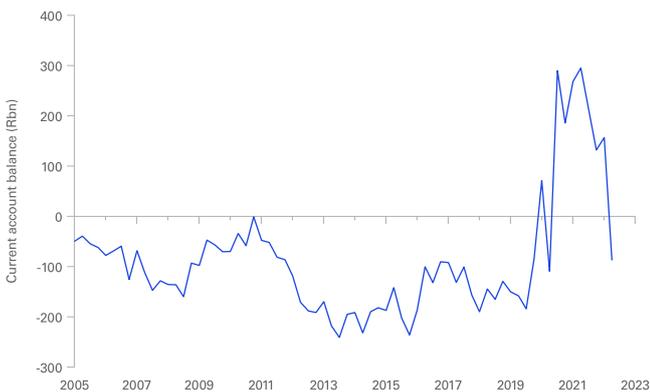


<sup>1</sup> These include palladium and other platinum group metals, gold, iron ore, coal as well as many other industrial metals.

GDP is set to grow by around 1.8% in 2022, led by contributions from the finance, real estate and business services sector, growth in personal services as well as mining, agriculture and trade, catering and accommodation. The projected growth in 2022 is noticeably lower than that achieved in 2021. It should however be understood that much of that growth was due to technical base effects following the sharp Covid-induced contraction experienced in 2020.

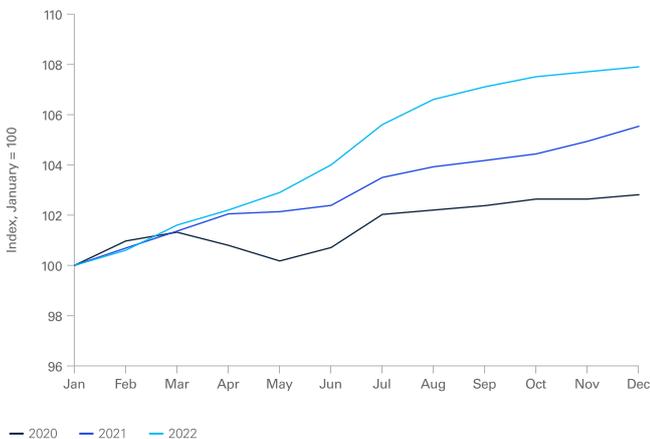
Growth in 2023 is expected to decline further to 1.5%, with higher interest rates and lower global growth reducing aggregate demand locally. In 2024, economic growth should return to the average pre-Covid level of around 1.7% as inflationary pressures abate and global growth rates improve.

**Chart 50: South Africa’s current account balance (Rbn)**



Source: Statistics South Africa, South African Reserve Bank, KPMG analysis.

**Chart 51: South Africa’s consumer price inflation (headline indexed 2020 - 2022)**



Source: Statistics South Africa, KPMG analysis.

Little tangible policy action has been taken to increase the lower investment and consumption spending caused by a reaction to a number of governance failures, including ongoing policy uncertainty, corruption, aging infrastructure and continued power shortages, the absence of growth-stimulating policy interventions and inadequate levels of service delivery. More will need to be done to lift the South African growth trajectory above its current long-term level.

The predicted rate of economic growth would not be sufficient to reduce the high unemployment rate, forecast at 34.3% for 2022. South Africa is set to remain in a paradoxical state of a growth recession, where slow growth is accompanied by rising unemployment unless some of the barriers to growth listed above are explicitly addressed.

Global inflationary pressure continues to weigh on the economy and remains largely cost-push in nature as aggregate demand still lags below its potential level. The main drivers of forecast consumer inflation remain energy prices, including both fuel and electricity prices, as well as food prices caused by ongoing supply chain disruptions following the pandemic and exacerbated by the conflict in Ukraine.

Although the global increase in commodity prices has slowed somewhat on the back of lower growth expectations, South Africa still faces elevated fuel and food production costs. Energy supply, and in particular electricity, remain an ongoing concern for South Africa whose energy regulator awarded the state-owned utility an above inflation 9.6% increase in energy prices from 1 April 2022.

The strength of the U.S. dollar, combined with lower global growth expectations, have eroded the positive balance on South Africa’s current account resulting from elevated commodity prices and led to an acceleration in inflation. Headline consumer inflation rate is expected to reach well above the upper boundary of the central bank’s inflation targeting range of 3% to 6%, at around 7.3% in 2022, before moving back towards the upper bound of 6% in 2023 and further to the midpoint of the targeting range in 2024.

**Frank Blackmore**  
Lead Economist, KPMG in South Africa

# Nigeria: Sustaining positive growth amid low oil production and rising inflation

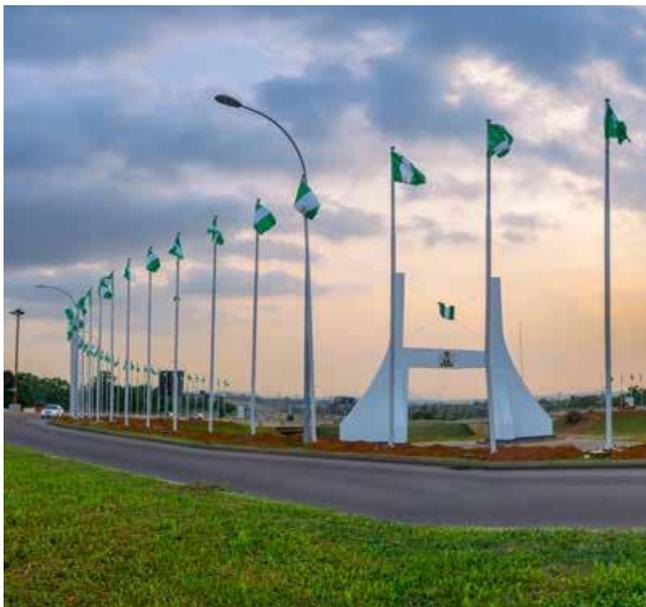
Nigeria’s economy is expected to continue on a positive trend, driven by growth in the non-oil sector.

The inflation rate is expected to remain in double digits in the short to medium term due to structural challenges and rising energy prices.

The unemployment rate is expected to remain heightened due to limited investment by firms and low manufacturing capacity.

Nigeria’s economy exceeded analysts’ expectations in 2021 as it grew by 3.4%. The Central Bank of Nigeria (CBN) had estimated a growth rate of 3.1%, while the IMF projected 2.6%. According to the National Bureau of Statistics (NBS), real Gross Domestic Product (GDP) grew by 3.1% in Q1 2022 and 3.5% in Q2 2022. The economy has thus grown for seven consecutive quarters, following its exit from recession in 2020. This consistent positive performance was driven largely by the continuous growth in the non-oil sector, particularly in the financial services, telecommunications and agriculture subsectors.

Year-on-year headline inflation rose to 19.6% in July 2022 from 18.6% in June 2022, according to the Central Bank of Nigeria data.

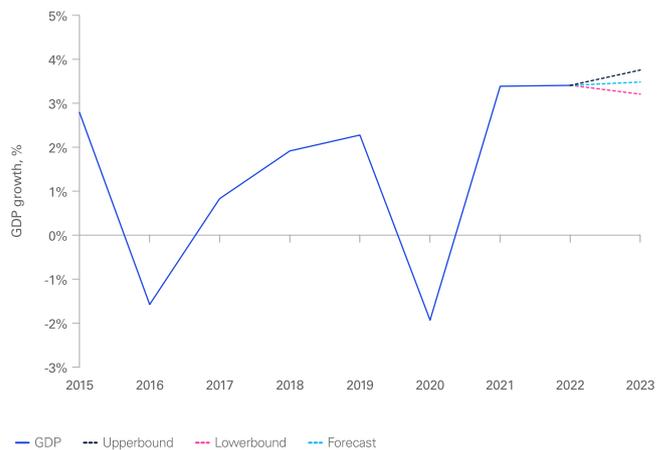


**Table 18: KPMG forecasts for Nigeria**

	2021	2022	2023
GDP	3.4	3.4	3.5
Inflation	15.6	16.1	13.1
Unemployment rate	34.2	38.3	42.7

Source: NBS, CBN, IMF and KPMG forecasts.

**Chart 52: Nigerian GDP annual growth**



Source: Nigeria Bureau of Statistics (NBS) (2015-2021), IMF (2022 and 2023), KPMG forecasts.



In July 2022, both the core and food components of inflation increased to 16.2% and 22.0% respectively, which drove the rise in headline inflation rates. The increasing inflation may further reduce households’ purchasing power and increase the cost of business operations.

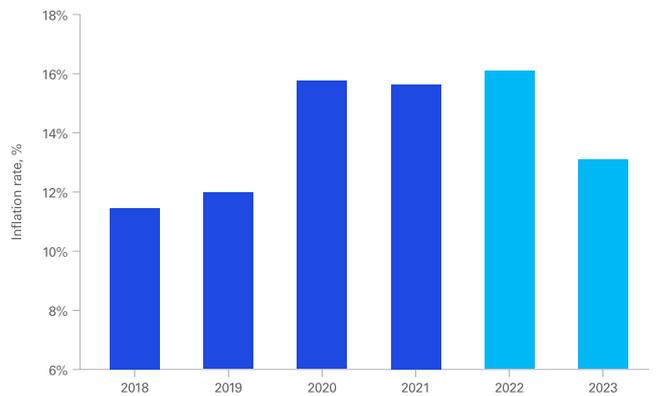
The unemployment rate in Nigeria stands high at 33% whilst under-employment stands at 22.8% based on data from the NBS. Youth unemployment has been historically high and currently stands at 42.5%. The burden of unemployment has been prevalent over the years due to limited investment by firms and low manufacturing capacity. The government is committed to reversing this trend and has recently launched the National Development Plan 2021 – 2025 aimed primarily at significant infrastructure investment, macro-economic stability, and a friendlier investing environment, to generate 21 million jobs.

Growth is expected to continue to be driven by non-oil sectors, fiscal expenditure by the government, CBN’s intervention programs to support the real sector and the efforts to prevent further increases in the inflation rate.

**Oluwole Adelokun**

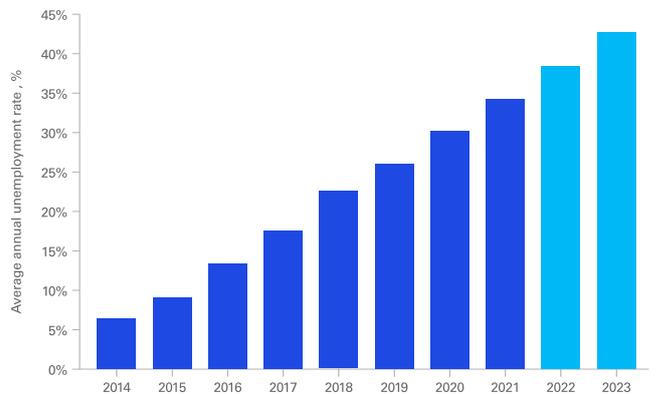
Associate Director, Strategy and Economics,  
KPMG in Nigeria

**Chart 53: Inflation rate, Nigeria**



Source: Central Bank of Nigeria (2018-2021), IMF (2022-2023).

**Chart 54: Average annual unemployment rate, Nigeria**



Source: Nigeria Bureau of Statistics (NBS); KPMG forecasts.

# Appendix: Summary of KPMG forecasts

	GDP			Inflation			Unemployment		
	2021	2022	2023	2021	2022	2023	2021	2022	2023
World	5.8	2.7	1.9	3.4	7.6	4.7	6.1	5.4	5.5
US	5.7	1.5	-0.1	4.7	8.2	3.8	5.4	3.7	4.3
Canada	4.5	3.4	1.3	3.4	6.8	3.4	7.4	5.3	5.6
Argentina	10.4	3.6	0.0	50.9	95.2	87.0	9.3	9.2	8.1
Brazil	4.8	1.9	0.8	8.3	9.8	5.8	13.6	10.4	10.1
Chile	11.7	2.0	-0.6	7.2	12.4	4.7	8.8	8.2	8.1
Mexico	5.0	1.7	1.5	5.7	8.0	5.5	4.1	3.5	3.8
Colombia	10.7	6.6	2.1	5.6	10.7	5.6	13.8	11.6	9.9
Peru	13.5	2.7	2.4	6.4	7.2	3.5	10.9	9.3	8.8
Germany	2.6	1.5	-0.5	3.2	8.0	6.8	3.6	2.9	3.0
Austria	4.8	3.9	0.3	2.8	8.5	5.8	6.2	4.6	4.6
France	6.8	2.5	0.6	2.1	5.9	3.9	7.9	7.5	7.7
Italy	6.6	3.3	0.3	1.9	8.1	4.9	9.5	8.2	8.5
Netherlands	4.9	3.0	1.0	2.8	10.1	3.9	4.2	3.6	3.8
Spain	5.1	4.1	1.8	3.0	9.3	4.9	14.8	12.8	13.0
Ireland	13.4	7.0	4.5	2.5	7.5	4.0	6.2	4.5	4.5
Eurozone	5.3	2.7	0.5	2.6	8.3	6.7	7.7	6.7	6.9
Norway	4.1	3.1	1.6	3.5	5.5	3.6	4.3	2.8	2.8
Sweden	5.1	2.4	0.8	2.2	7.4	4.8	8.8	7.4	7.4
Switzerland	4.2	2.5	1.2	0.5	2.9	1.8	5.1	4.3	4.2
UK	7.4	3.2	-0.2	2.6	8.9	5.6	4.5	3.7	4.3
Poland	5.9	4.1	1.4	5.1	13.8	10.9	3.4	2.9	2.9
Turkey	11.0	4.8	2.2	19.6	72.1	38.2	12.0	11.8	11.8
China	8.1	3.5	5.2	0.9	2.5	2.3	5.1	5.4	5.1
Japan	1.7	1.6	2.2	-0.2	2.4	1.6	2.8	2.5	2.6
Australia	4.9	4.2	2.2	2.9	6.3	5.2	5.1	3.8	4.4
India	8.7	7.2	6.3	5.5	6.7	5.0	8.0	7.6	7.1
Indonesia	3.7	5.7	4.7	1.6	4.4	4.0	6.4	5.7	5.9
Malaysia	3.2	8.6	4.8	2.5	3.6	3.1	4.6	3.9	3.9
Philippines	5.5	6.1	5.1	3.9	5.6	3.8	7.9	5.8	6.0
Singapore	7.6	3.5	3.5	2.3	5.9	2.9	2.7	2.1	2.3
South Korea	4.1	2.8	2.5	2.5	5.4	3.2	3.7	3.1	3.1
Saudi Arabia	3.2	8.0	3.6	3.1	2.6	2.3	6.6	6.0	6.0
Nigeria	3.4	3.4	3.5	15.6	16.1	13.1	34.2	38.3	42.7
South Africa	4.9	1.8	1.5	4.6	7.3	6.1	35.3	34.3	34.7

Source: National statistical agencies, KPMG analysis.

Note: Average % change on previous calendar year except for unemployment rate, which is average annual rate. Figures for India represent fiscal years 2021-22, 2022-23 and 2023-24. Consumer price inflation measured as % change Dec-on-Dec for Argentina, Chile, Colombia and Peru.

# Contacts

## United Kingdom

### **Yael Selfin**

**Chief Economist, KPMG in the UK**

yael.selfin@kpmg.co.uk

### **Dennis Tatarkov**

**Senior Economist, KPMG in the UK**

dennis.tatarkov@kpmg.co.uk

### **Michal Stelmach**

**Senior Economist, KPMG in the UK**

michal.stelmach@kpmg.co.uk

## United States

### **Diane Swonk**

**Chief Economist, KPMG US**

dswonk@kpmg.com

## Canada

### **Mathieu Laberge**

**Partner, Economics & Policy, KPMG in Canada**

mathieulaberge@kpmg.ca

## Australia

### **Dr. Sarah Hunter**

**Senior Economist & Partner, KPMG in Australia**

sarahhunter@kpmg.com.au

## China

### **Kevin Kang, PhD**

**Chief Economist, KPMG China**

k.kang@kpmg.com

## India

### **Preeti Sitaram**

**Director, Government & Public Services,**

**KPMG in India**

psitaram@kpmg.com

## Germany

### **Dr. Ventzislav Kartchev**

**Head of Business Intelligence/Markets,**

**KPMG Germany**

vkartchev@kpmg.com

## Austria

### **Dr. Stefan Fink**

**Chief Economist, KPMG in Austria**

stefanfink@kpmg.at

## The Netherlands

### **Diego Vilchez Neira**

**Senior Manager, KPMG in the Netherlands**

vilchezneira.diego@kpmg.nl

## Ireland

### **Dr. Daragh Mc Greal**

**Director, Strategic Economics, KPMG in Ireland**

daragh.mcgregal@kpmg.ie

## South Africa

### **Frank Blackmore**

**Lead Economist, KPMG in South Africa**

frank.blackmore@kpmg.co.za

## Nigeria

### **Oluwole Adelokun**

**Associate Director, Strategy and Economics,**

**KPMG in Nigeria**

oluwole.adelokun@ng.kpmg.com

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