Fundación MAPFRE

2022 ECONOMIC AND INDUSTRY OUTLOOK: SECOND QUARTER PERSPECTIVES

MAPFRE Economics

2022 Economic and Industry Outlook: Second Quarter Perspectives

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Executive summary

2022 Economic and Industry Outlook: Second Quarter Perspectives

Economic outlook

Following the progress made in controlling the COVID-19 pandemic, at the beginning of 2022 the global economy was showing, albeit moderately, positive growth rates. The environment observed at the beginning of the year was characterized by a number of constraints to global economic recovery, including the new Omicron variant of the coronavirus, which, thanks to the experience accumulated in previous waves and the effectiveness of vaccines and treatments, marked a new phase in the pandemic of living with a more endemic and normalized disease. Other key factors were the high and persistent inflation rates, and supply chains which, while continuing to weigh down the imbalance between supply and demand, showed some improvement.

However, the outlook for global growth has been significantly impacted by the conflict between Russia and Ukraine, which has caused it to markedly deteriorate. Global commodity prices have increased mainly in energy, oil derivatives and food, raising the risk of economic disruption, albeit with some divergence by region. This will entail greater risks to production capacity and growth while increasing the risk of inflation.

The Eurozone, due to its proximity to the conflict, its need to deal with refugee flows, and its high energy dependence on Russia, among other factors, will suffer a greater economic impact. In this context, the economic growth estimate for the Eurozone has been lowered to 2.9% in 2022 (from 3.9% previously), maintaining 2.7% for 2023, with the inflation forecast rising to 5.5% in the year's last quarter.

Meanwhile, the U.S. economy, despite its energy self-sufficiency and limited trade link with Russia, is not immune to the downward revision of activity levels, given its broader interconnectedness with the global economy, dependence on still fragile supply chains and more generalized inflationary pressures, among others. As a result, the GDP growth forecasts are 3.2% and 1.7% for 2022 and 2023, down from 4.0% and 2.5% in our previous report, with an average inflation estimate for the last quarter of 2022 of 6.9%.

The emerging markets are facing a more fragmented impact, which will be positive for economies that export raw materials such as oil, metals, certain foods, etc., and negative for emerging economies that are mainly manufacturing-based, which must contend with high production prices.

Thus, in the baseline scenario considered in this report, the forecast for global GDP growth would be 3.6% in 2022 and 2023, and inflation (average for the last quarter of the year) would stand at 6.8% and 4.1% for 2022 and 2023, respectively. In contrast, a situation closer to stagflation is observed in our stressed scenario (of a more pessimistic nature), where overall economic growth of 3.2% and 2.6% is forecast for 2022 and 2023, respectively, with an inflation forecast (average of the last quarter of the year) of 7.8% and 4.3% for each of those years. Finally, we present a shock scenario (lower probability and higher impact) in this report, in which the GDP growth forecast would be 0.8% and 0.5% for 2022 and 2023, and average inflation in the last quarter of the year would be 9.0% and 6.2%, respectively.

Industry outlook

The conflict in Ukraine and the sanctions against Russia have complicated the outlook for the global insurance markets, which are facing a slowdown in economic growth, higher and more persistent inflation than expected, and an environment of great uncertainty and heightened volatility in the financial markets. Thus, some of the main problems generated by the process of economic reopening after the worst phases of the pandemic have been aggravated by the war instead of being corrected.

All of these factors are darkening the outlook for business development and profitability in the insurance industry in 2022, in an environment where inflation is eroding business margins and household purchasing power, which makes it difficult to pass on rising claims costs to insurance prices. Disruptions in supply chains continue to affect certain lines of business, such as auto insurance, where this economic phenomenon is weighing down new vehicle registrations. In addition, volatility and corrections in both the bond market and the main equity indexes may negatively affect the balance sheet and solvency position of insurance companies that have not adequately managed these risks.

But on the positive side, business volume in some lines of business, such as health and life protection insurance, continue to benefit from increased sensitivity to sickness and death risk as a result of the pandemic and the war, especially in markets where public health systems are weaker or remain saturated. Other important business segments, such as property, commercial and industrial multirisk, continue to show their characteristic resilience to such situations.

On the other hand, the persistence of higher-than-expected inflation is leading to monetary policy tightening in most markets, both developed and emerging, which will favor the development of Life insurance linked to savings and traditional annuities. However, the negative real interest rates that persist in many markets, coupled with higher and longer-lasting inflation than anticipated, may erode household saving capacity, reducing demand for these kinds of products.

As for the outlook for Life insurance in which the policyholder assumes the investment risk, the downturns and high volatility of the securities markets create a more complex environment for their marketing. Insurance companies will therefore be forced to adapt their products to a new context in which risk-free interest rates and risk premiums on fixed income are rising due to greater economic uncertainty and the withdrawal of monetary stimuli by central banks, with spreads more aligned to the credit risk of the issues. The Life investment business is therefore facing a more complex scenario in which the sovereign and corporate bond market will undoubtedly play a bigger role.

1. Economic outlook

1.1 The world economic outlook

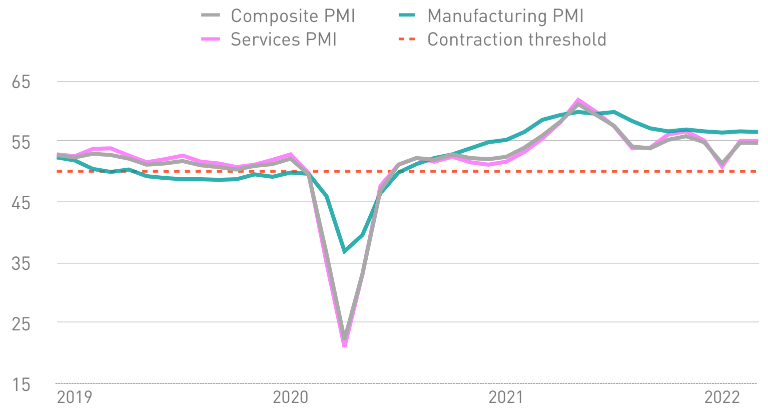
1.1.1 Renewed uncertainty in a tense geopolitical context

The outlook at the beginning of 2022

The beginning of 2022 was marked by a continuation of the global economic recovery (see Charts 1.1.1-a and 1.1.1-b), with positive growth rates that—while consolidating the previous recovery trend after the progress made in controlling the COVID-19 pandemic in both developed and emerging countries (see Charts 1.1.1-c and 1.1.1-d)—showed clear signs of moderation. At that time, recovery was impacted by factors such as: (i) the potential recirculation of the virus (through the Omicron variant) and the return of social distancing measures, (ii) supply chains which, while showing some signs of improvement, continued to weigh down the imbalance between supply and demand, and (iii) higher and persistent inflation rates that were beginning to negatively impact real incomes.

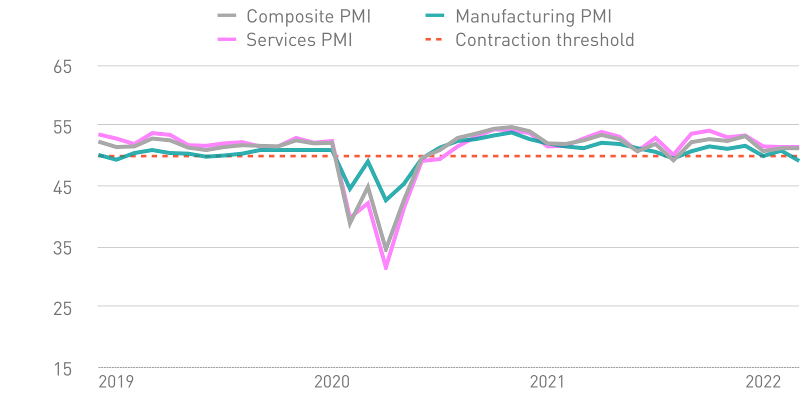
Throughout the first quarter, the epidemiological conditions proved to be relatively benign for economic activity due to the experience gained in previous pandemic waves, the effectiveness of vaccines and treatments, and the short-term, high-intensity behavior of infections. This situation gives cause for optimism, signaling that the pandemic may have entered a new phase of living with a more endemic and normalized disease. With regard to the supply shock and bottlenecks, these have maintained the pre-existing asymmetries, with certain signs of improvement and decongestion in certain branches of manufacturing and transport, although they are still far from normal. Finally, the price constraint continued the trend of upward pressures, with a broader and more

Chart 1.1.1-a
Developed markets: PMI performance



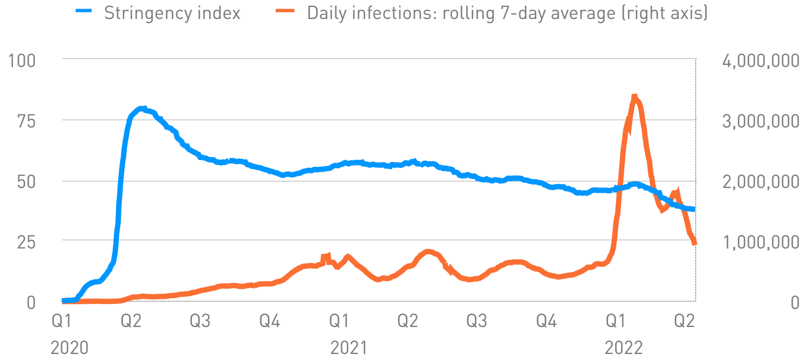
Source: MAPFRE Economics (based on Bloomberg data)

Chart 1.1.1-b
Emerging markets: PMI performance



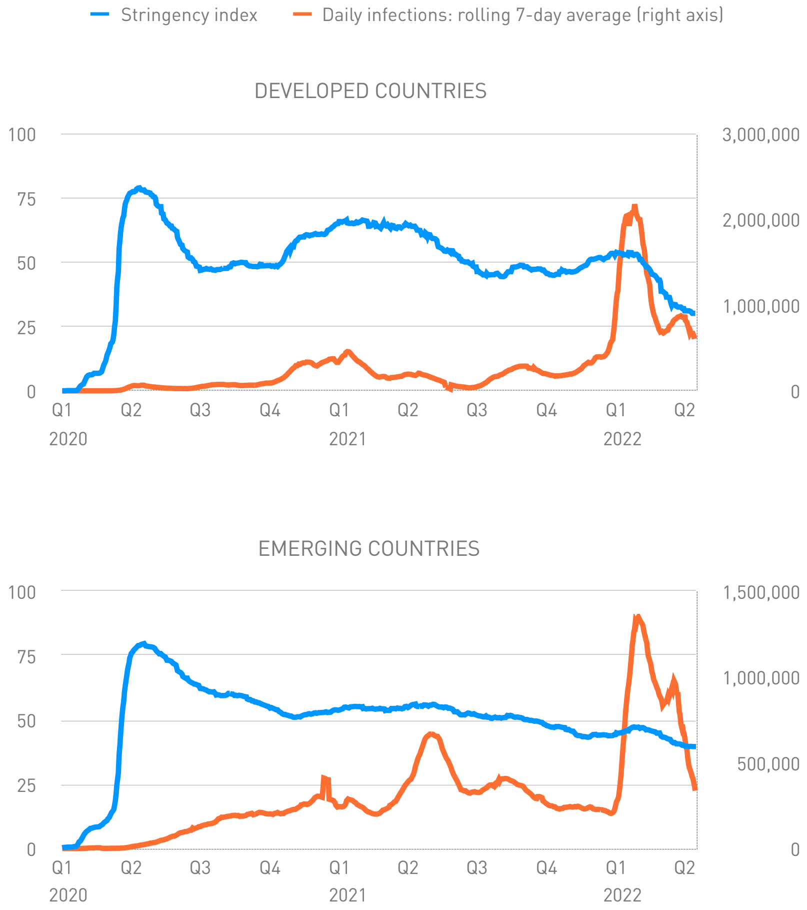
Source: MAPFRE Economics (based on Bloomberg data)

Chart 1.1.1-c
Global: daily COVID-19 infections vs. stringency index



Source: MAPFRE Economics (based on data from the Coronavirus Government Response Tracker, University of Oxford)

Chart 1.1.1-d
Developed and emerging: daily COVID-19 infections vs. stringency index



Source: MAPFRE Economics (based on data from the Coronavirus Government Response Tracker, University of Oxford) persistent product base that serves as a justification to address the shift towards tighter monetary and fiscal policies.

The geopolitical constraint

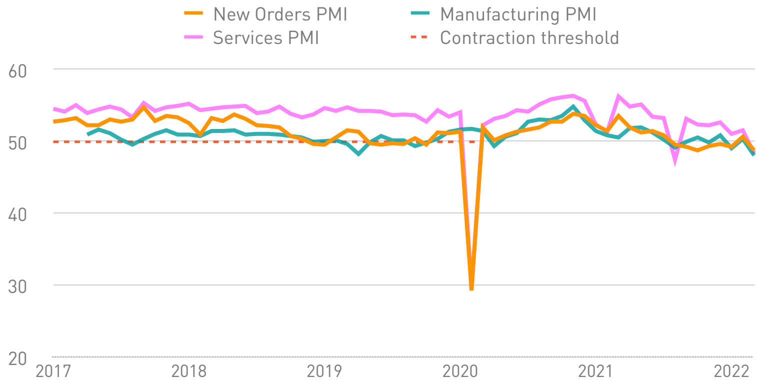
However, the first quarter of the year saw the arrival of a new constraint on economic activity levels: the onset of Russia's invasion of Ukraine. With this new geopolitical constraint, which has deepened the supply shock, the outlook for growth forecasts points to a notable deterioration in global economic activity and an increase in price pressures, albeit with divergences by region. The forecasts would thus shift towards a baseline scenario of downward global activity and upward inflation (3.6% growth and 6.8% average inflation in the last quarter, respectively, in 2022, versus 4.8% and 3.8% previously); a stressed scenario of broader risk, approaching stagflation, with an additional four-tenths cut to GDP and rising inflationary dynamics (3.2% and 7.8% by 2022, in each case); and ultimately, although still an unlikely possibility, a shock scenario that includes the risk of recession with GDP growth and inflation forecasts in 2022 of 0.8% and 9.0%, respectively (see Tables A-1 and A-2 in the Appendix of this report).

The Eurozone is expected to suffer the greatest impact in this regard, with expected growth of 2.9% in 2022 and rising inflation (5.2% on average and 3.8% in the fourth quarter). Among the conditioning factors for this downward revision are its proximity to the conflict, its need for cohesion mechanisms to deal with refugee flows, its close trade relations with the region and, more immediately and palpably, its high energy dependence (still unlinked to the SWIFT sanctions imposed on Russia). With this, the second round of price pressures would be more immediate, the direct impact on business margins more pronounced, especially for those highly dependent on gas flows, and their channeling to the final consumer would also be greater. This would increase the risk of second-round effects on prices, anchored in higher expectations in the longer term.

As for the United States (with a GDP growth forecast of 3.2% for 2022 compared to 4.0% previously), its energy self-sufficiency, limited trade link with Russia, and strong labor market have made consumption more resilient than expected, although it is clearly deteriorating in real terms. Nevertheless, the U.S. economy is not immune to downward revisions, given its broader interconnectedness to the global economy, its dependence on still fragile supply chains, more widespread inflationary pressures, and monetary policy tightening in terms of interest rates, which will soon include the first balance sheet reduction.

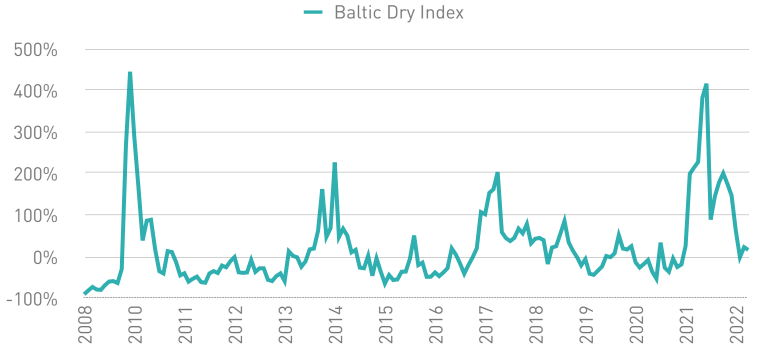
Finally, although their ties are not as close or dependent, emerging markets face a more fragmented impact: positive for economies that export raw materials like oil and derivatives, metals, and certain foodstuffs, among others, and negative for emerging economies with intensive manufacturing activity, whose production capacity is impacted by these high prices. In particular, countries like China (with a new economic growth forecast of 4.8% for 2022, versus the previous 5.0%) and certain industry-intensive satellite states in Asia are additionally facing the risk of direct sanctions that may intensify the problem and a political environment of zero tolerance for the pandemic. This is causing new lockdowns in cities like Shanghai, Changchun, Jilin, Shenzhen, and Langfang, aggravating the bottlenecks originating in Asia that, given their global relevance, would exacerbate the supply shock and, with it, the risk of stagflation (see Chart 1.1.1-e).

Chart 1.1.1-e
China: PMI performance



Source: MAPFRE Economics (based on Bloomberg data)

Chart 1.1.1-f
Global: global trade (average transport cost index)
(year-on-year variation)



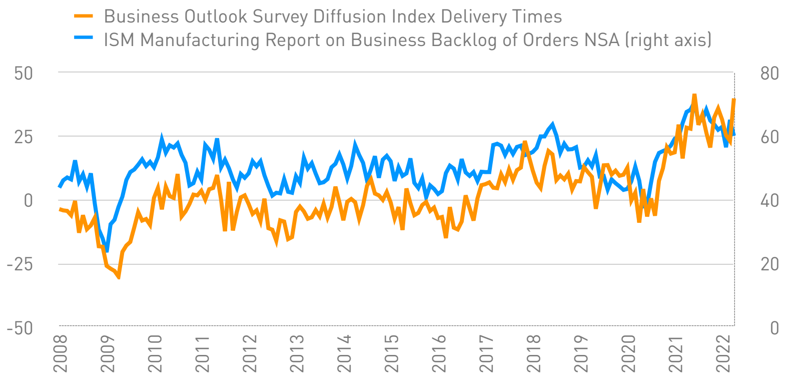
Source: MAPFRE Economics (with Bloomberg, IIF, Haver data)

Transmission channels for the geopolitical constraint

The conflict between Russia and Ukraine, which began with the Russian invasion on February 24 (see Box 1.1.1-a), has had an immediate impact on global commodity prices, intensifying the historical upturn that commodities had been experiencing previously, mainly in the energy, oil derivatives and food sectors, and generally raising the risk of economic disruption, although with certain divergences by region. Generally speaking, this new geopolitical constraint implies greater risks to production capacity and raises the risk of inflation (see Charts 1.1.1-f to 1.1.1-k).

On the other hand, this geopolitical event served as a catalyst for intense risk aversion, with widespread corrections in equity markets, an extension of the movement to credit spreads, and bonds and hard currencies serving

Chart 1.1.1-g
Global: Lead time and backlog trends



Source: MAPFRE Economics (with Bloomberg, IIF, Haver data)

Box 1.1.1-a
The conflict in Ukraine: geopolitical context and long-term vision

The world, and especially Europe, is confronting strategic challenges with medium-term and long-term consequences that could be very significant. It has become clear that Russia's invasion of Ukraine goes beyond the tragedy now occurring in that country, bringing up unresolved conflicts rooted in the turmoil of the last quarter of the 20th century. Russia was never in agreement with the borders that resulted from the collapse of the Soviet Union, and China always wanted more than just a position as a massive exporter of low-value goods. Subsequently, Russia always maintained hopes for recovery of territories such as the Republika Srpska, Transnistria, Donbas, Georgia, and a few others, waiting for the time when borders could be redrawn. Meanwhile, China managed to strengthen its ties with the West through the World Trade Organization (WTO), without having to address questions of ethics, and with the unspoken aim of recovering what it had lost during its *Century of Humiliation*, including Taiwan.

The dissidence toward the European model at the end of the 2010s, spurred by Brexit, by a society with growing inequalities that was also facing the impact of COVID-19, by certain acquired vulnerabilities (debt, sales, and energy), by the strained relationships among the various architects of the post-war model, and by a changing of the guard in Eurozone leadership (Juncker, Draghi, Merkel, Von der Leyen, Borrell, Lagarde), seems to have created the ideal time for a sort of shared pushback by China and Russia as circumstantial partners. This apparent state of accord is emerging as an alliance to take advantage of persisting weaknesses in the West, along with some shared interests existing among a growing group of hardline leaders in the East. Although some of the facts at hand seem to support the idea that their time has effectively come, there are others suggesting that, in the end, any sort of shared destiny will remain elusive.

Because of its invasion of Ukraine, Russia is facing official and unofficial sanctions from the rest of the world. These are having a real impact on Russia's economy, but it is still managing to fund its war and keep its economy reasonably stable, thanks to the scheme of requiring payment for natural gas in rubles, essentially structured by Gazprombank, the Central Bank, the Eurozone, and China. Europe's dependence on Russia for energy is Putin's best tool for deterrence, while Europe's commercial dependence on China is the best way for that country to keep things calm when the situation starts to become frenetic. This allows China to avoid the effects of Russia's economic struggles, although it has less ability to tolerate a state of stagflation in Europe. Ultimately, both Russia and China are still managing to keep the effects of the world situation under control.

Russia was expecting to deal with a divided West, and this has not been the case. The "strategic challenge" (as Merkel called it) represented by China after the COVID-19 pandemic, and now the war in Ukraine, has put the West on guard, which materialized at the most recent security meeting in Munich. The North Atlantic Treaty Organization (NATO) and those responsible for foreign security and diplomacy have all adopted positions not seen (in either case) since the times of Javier Solana. This is now being laid out in Europe's strategic and defensive roadmap in the form of the Strategic Compass (published a few months ago) and the foundations for a European Defense Force. This is also taking place in a context of clear mutualization of European efforts, as reflected in NextGenEU, emerging financing plans, an increased focus on defense, and renewed discussions about a European treasury. In other words, regardless of what those in Russia and China may have privately expected, the problems arising during the last five years have generated a stronger trans-Atlantic alliance and a

Box 1.1.1-a (continued)
The conflict in Ukraine: geopolitical context and long-term vision

European Union with more clearly established priorities and a sense of common purpose.

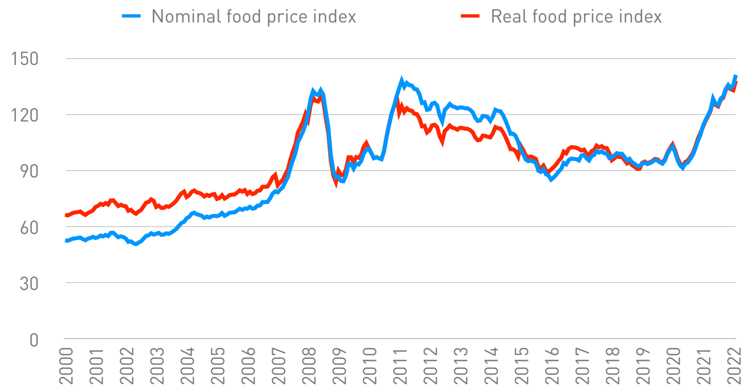
Another potential miscalculation by Putin that will take its toll as the weariness sets in is that of regional alliances. Russia had two natural partners in its bellicose ambitions: Turkey and China. Both are partnerships based more on need than on a shared worldview, and Russia has its own roadmap that takes precedence over all other interests, especially since its ultimate aim is to prevail. On the one hand, Turkey represents NATO's second largest military force, with its links to Russia arising equally from its energy and tourism interests. Therefore, it needs to balance its interests and ties with Russia to stabilize its currency and current account without entering a deep recession before 2023, when the Turkish general elections will be held. Although he might lose the next election, Erdogan will seek to go down in history for something other than plunging Turkey into a deep recession and undoing ties with its natural European partner. On the other hand, there is China, which is trying to remain on the fence in terms of politics, failing to condemn Putin for his invasion but avoiding any statements that would be seen as encouraging him. The reason for this, as explained above, is that China needs Europe, and it does not want to further solidify any views that it stands in opposition to the values Europe publicly defends.

Although the future of the conflict in Ukraine remains to be seen, in the worst-case scenario it will continue to drag on, because Russia is encountering local resistance much stronger than it expected, in a global context of interests and alliances that is more complex than it may have assumed.

as a safe haven to a certain extent. While the initial shock was highly intense, as reflected by the VIX, as news flow normalized and economic sanctions became more detailed, the reduced uncertainty has resulted in a more stable situation in recent weeks. However, it is not free of the risk of further events of similar impact, exacerbated by less benign financial conditions (see Charts 1.1.1-l and 1.1.1-m).

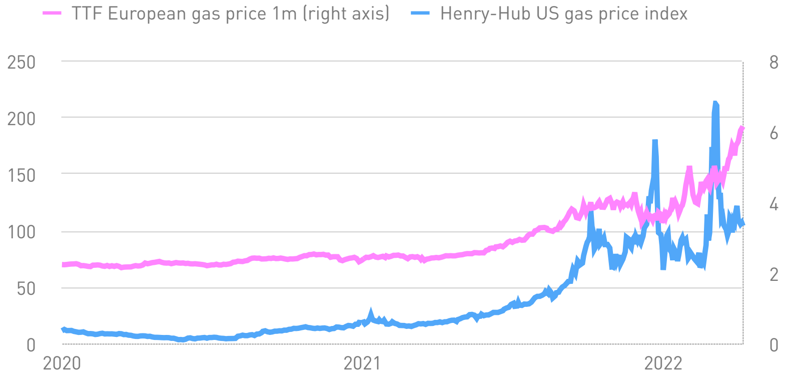
This shock has come at a time when economic policies were already beginning to pivot from the broadly accommodative environment that became widespread during the pandemic toward further tightening, still in its early stages in developed markets and at a far more advanced stage in most emerging markets (see Boxes 1.1.1-b, 1.1.1-c, and 1.1.1-d). Similarly, although with some lag with respect to the channel of basic input and energy prices, a deterioration is expected to begin affecting business margins and, secondly, to be passed on to end consumers in an additional attempt at cost pass-through, resulting in a second round of higher prices, less intense base effects and higher and longer-lasting inflation expectations. Faced with such dynamics, and given the risk of leading to the potential destruction of demand, economic policymakers must respond to a delicate situation. On the one hand, there is the need to

Chart 1.1.1-h
Global: food price index



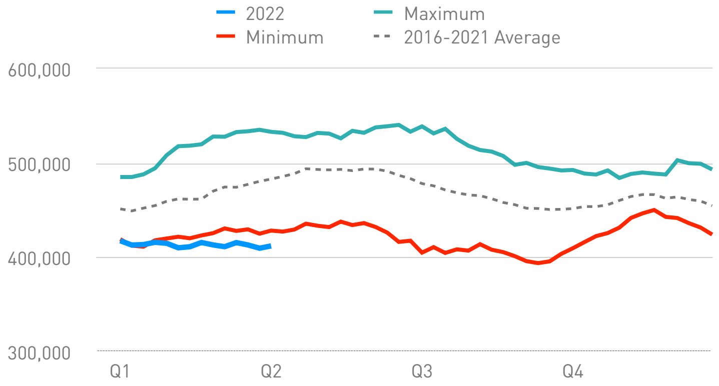
Source: MAPFRE Economics (with FAO data)

Chart 1.1.1-i
Global: gas price trends



Source: MAPFRE Economics (with Bloomberg, IIF, Haver data)

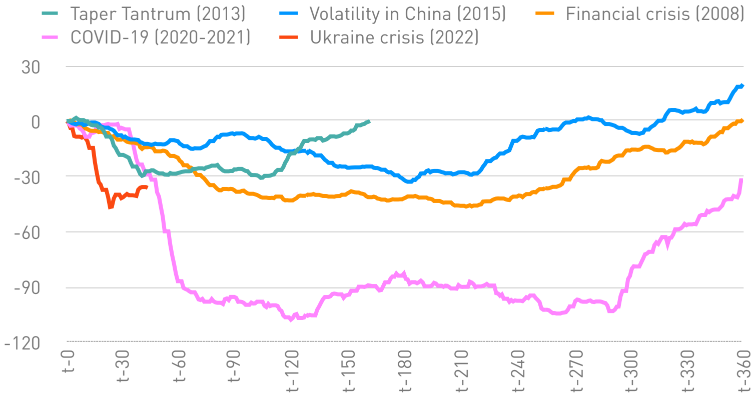
Chart 1.1.1-j
Global: crude oil inventories compared to historical levels



Source: MAPFRE Economics (with Bloomberg, IIF, Haver data)

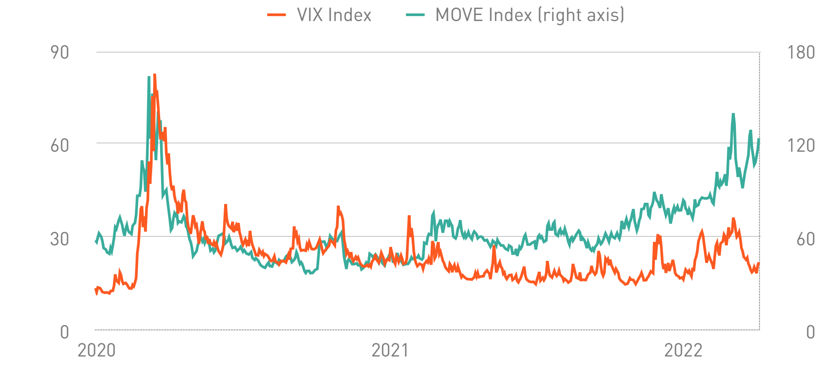
Chart 1.1.1-k
Emerging markets: portfolio investment flows

(billions of U.S. dollars)



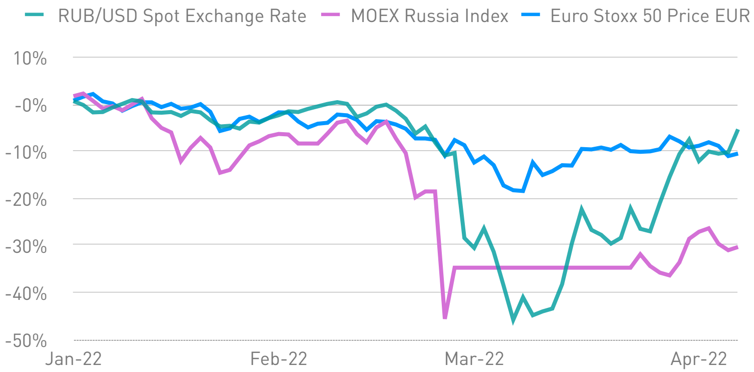
Source: MAPFRE Economics (based on IIF data)

Chart 1.1.1-l
Global: volatility trends



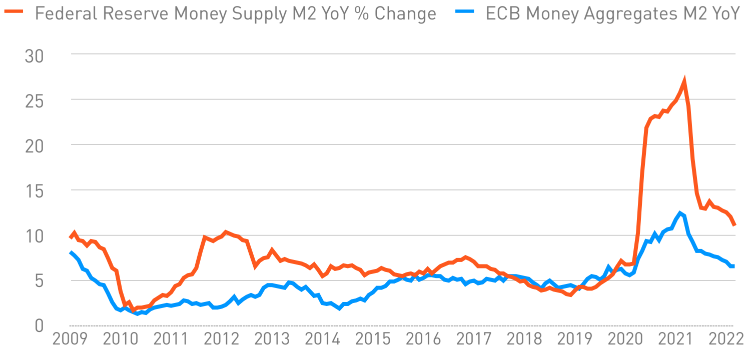
Source: MAPFRE Economics (based on Bloomberg data)

Chart 1.1.1-m
Europe and Russia: changes in stock market indexes and exchange rates



Source: MAPFRE Economics (based on Bloomberg data)

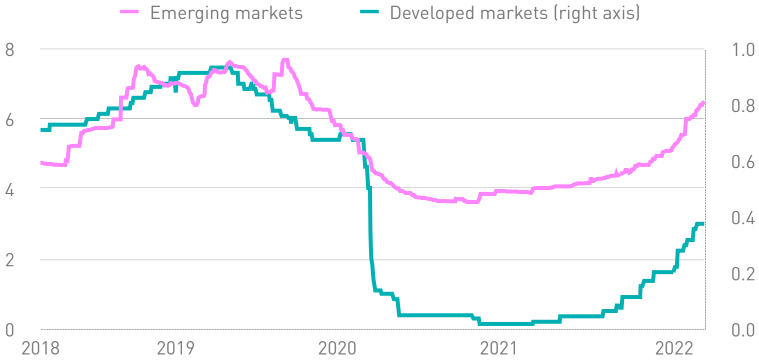
Chart 1.1.1-n
United States and Eurozone: monetary aggregates trends (M2)



Source: MAPFRE Economics (with Haver data)

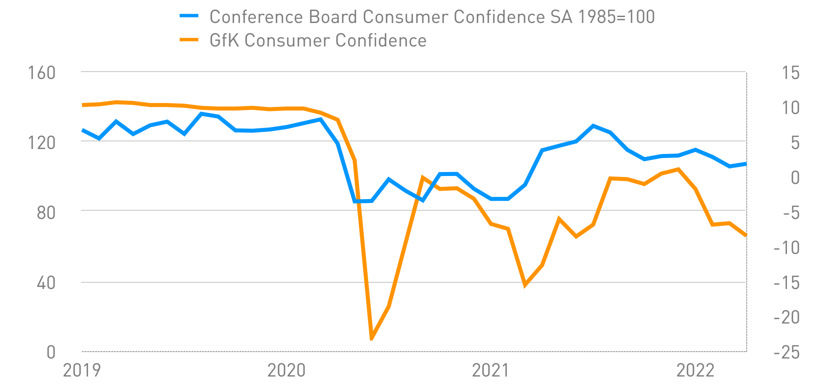
Chart 1.1.1-o
Developed and emerging markets: official interest rates

(average, %)



Source: MAPFRE Economics (based on BIS data)

Chart 1.1.1-p
Global: consumer confidence



Source: MAPFRE Economics (with Haver data)

recover fiscal and monetary margins and to combat historically high inflation rates with more orthodox policies; and on the other hand, the need to delay the process and resume fiscal dampening in view of the current scenario of deteriorating activity and implications for prices. So much so that a pause in normalization or additional fiscal expansions could exacerbate the problem, as was the case with the initial bottlenecks, which were triggered against a backdrop of fiscally and monetarily stimulated demand (see Charts 1.1.1-n to 1.1.1-p).

The central outlook

At this juncture, the dynamics of global economic activity are being affected by this new geopolitical constraint, which presents the possibility of unknown actions and rapid escalation, a difficult challenge with the potential to lead to systemic risk events that deteriorate the forecast scenario through other channels. While the *baseline scenario* has a broad base of probabilities, in line with what we have indicated in previous reports[1], and the *stressed scenario* (alternative) presents a stress situation derived from it, we have also analyzed an additional scenario centered on the possibility of a broader conflict and dynamics that, despite being among the tail risks, would have sufficient potential to lead to a global recession in 2023 (*shock scenario*).

Baseline scenario

For the purposes of this report, in the *baseline scenario*, at least for now, the pandemic is expected to have a minimum impact, considering that we have reached robust herd immunity, selective and low-impact restrictions are being maintained, and the transition from the pandemic to the endemic phase is underway, aimed at not damaging economic activity. On the geopolitical side, there will be a moderate impact on economic growth under the assumption of a time-limited conflict, sanctions consistent with those already in place lasting beyond 2022 (sanctions on Russia will not disappear even with a ceasefire), and a direct effect on trade. This will in turn affect the prices of energy and non-energy commodities, reducing economic performance as prices rise sharply.

In this *baseline scenario*, oil and gas prices will remain above 100 USD/b throughout 2022 (vs. 85 USD/b in our previous report) before settling in the vicinity of 90USD/b at the start of 2023 and following a long-term converging path from 2024 onwards that would maintain potential prices above the pre-conflict period. For gas and the broader commodities aggregate, the normalization path is expected to be similar, not without underlying volatility, but with longer-term potential of recovering their previous trend from 2024 onwards.

Box 1.1.1-b
Monetary policy update: European Central Bank

European Central Bank

At its meeting on March 10, the European Central Bank (ECB) announced that interest rates would remain unchanged (0% for main refinancing operations and -0.5% for the deposit facility). Regarding the Pandemic Emergency Purchase Programme (PEPP), the ECB has confirmed that it will end net purchases at the end of March. However, maturity reinvestment will be maintained until at least the end of 2024. As for the Asset Purchase Programme (APP), the Governing Council reviewed the purchase plan for the coming months. Monthly net purchases under the APP will amount to €40 billion in April, €30 billion in May, and €20 billion in June. The calibration of net purchases for the third quarter will be data-dependent and reflect its evolving assessment of the outlook (see Chart A).

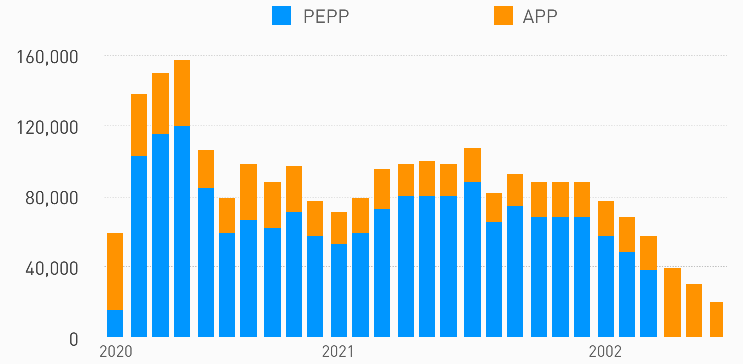
As for targeted longer-term refinancing operations (TLTROs), they remain on schedule in their third series, with completion scheduled for June, ensuring that their maturity does not hinder the smooth transmission of monetary policy. Finally, in view of "the highly uncertain environment caused by the Russian invasion of Ukraine," the ECB decided to extend the Eurosystem repo facility for central banks (EUREP) until January 15, 2023.

On the macroeconomic front, the ECB presented new projections that incorporate recent geopolitical developments, with a downward revision in terms of GDP to 3.7% in 2022 and 2.8% in 2023 (vs. 4.2% and 2.9% previously), and a significant upward revision in expected inflation to 5.1% in 2022 and 2.1% in 2023 (vs. previous forecasts of 3.2% and 1.8%, respectively).

Energy shock

Russia's military intervention in Ukraine, begun on February 24, has caused a shock in the markets in general, but especially in the energy sector (Brent, +54%; natural gas, +98%), agricultural products (corn, +30%; wheat,

Chart A.
ECB: PEPP and APP monthly purchases



Source: MAPFRE Economics (with Haver data)

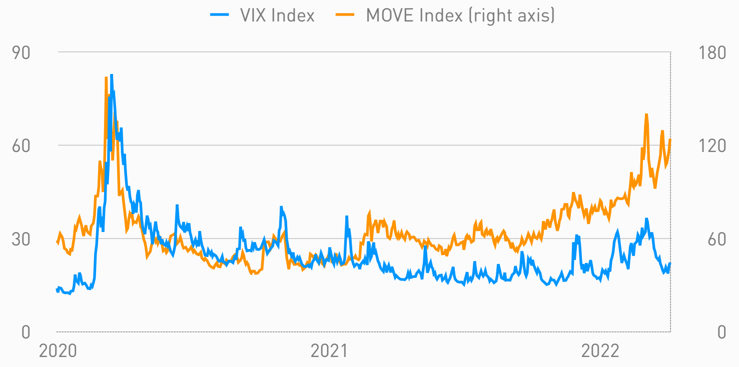
Box 1.1.1-b (continued)
Monetary policy update: European Central Bank

+60%; soybeans, +32%), metals (gold, +13%; nickel, +140%; steel, +14%; palladium, +60%), currencies, stock exchanges, and fixed income markets, introducing high volatility to the market (see Chart B).

Starting from an inflation outlook that was not good before the conflict in Ukraine, and now with the disruption in the oil and at least part of the natural gas supply, oil and natural gas prices have gained new momentum in world markets as supply has been reduced. Many countries are again trying to rebalance their energy sources. This pressure on demand is being passed on to prices to benefit producing countries. In this context, and given the small production increase agreed to by Saudi Arabia (400 million bbl/day), Western countries are in a position to lift sanctions on Iran and Venezuela to be able to replace the suppression of Russian oil.

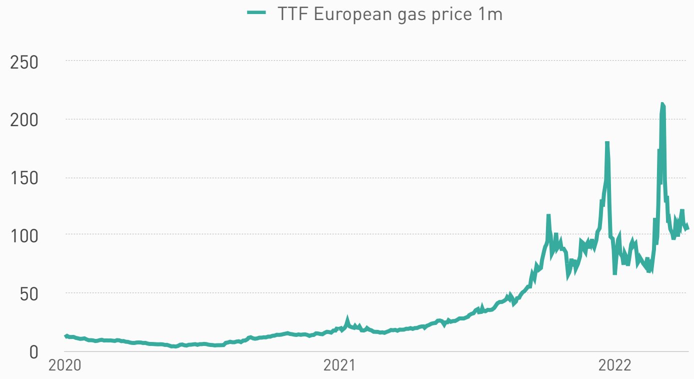
The gas situation is more serious, since the quantities coming from Russia are very significant. Replacing Russian gas with liquefied gas from other destinations is not easy, since the regasification terminals have not been built. Hence, Russia's threat to completely cut off supplies could put

Chart B.
Stock and bond volatility



Source: MAPFRE Economics (based on Bloomberg data)

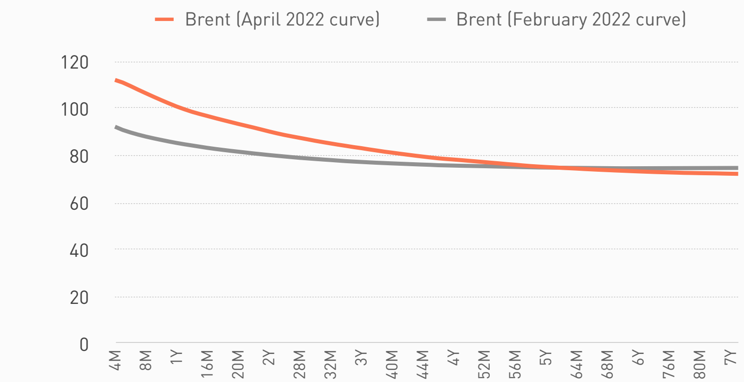
Chart C.
Gas price trends



Source: MAPFRE Economics (based on Bloomberg data)

Box 1.1.1-b (continued)
Monetary policy update: European Central Bank

Chart D.
Changes in oil prices.



Source: MAPFRE Economics (based on Bloomberg data)

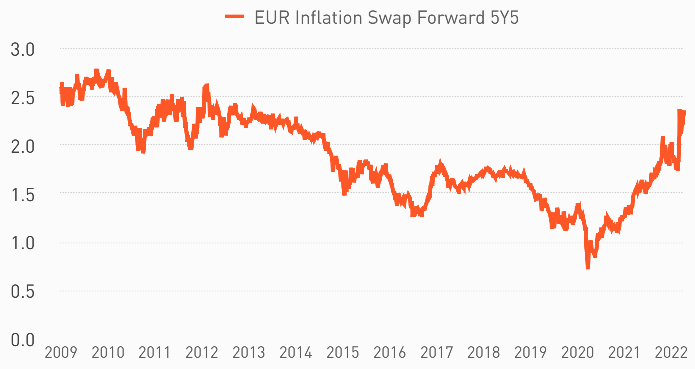
European countries in a real bind because of its impact on prices (see Charts C and D).

Assessment

Following the last ECB meeting, the scenario of declining economic activity and rising prices hinders not only its timetable but also the very imperative of price stability in an environment where the gap between production and consumption is widening. This is taking place under a dynamic of higher and more immediate inflationary pressures already reflected in the inflation outlook (see Chart E).

While the ECB's inflation scenario of 5% is plausible, it could be underestimated due to several factors: (i) the errors in previous forecasts (with some inclination to moderate expectations), (ii) the implications of the continued escalation of the Russia-Ukraine conflict (only weeks ago, it was thought that implementing sanctions would be the culmination of tensions,

Chart E.
Eurozone: inflation expectations



Source: MAPFRE Economics (based on Bloomberg data)

Box 1.1.1-b (continued)
Monetary policy update: European Central Bank

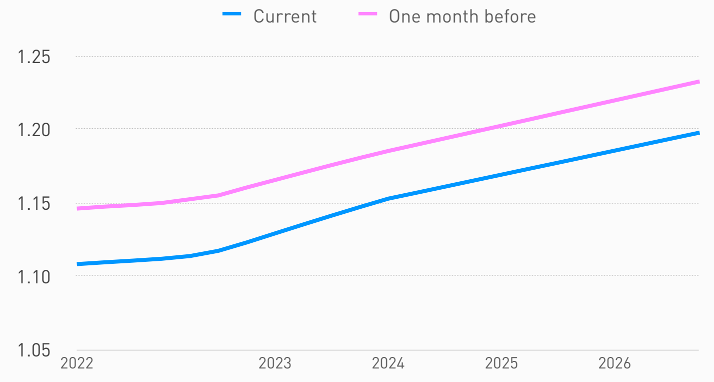
while the second round of sanctions has now been activated without assessing the effects of the first round), and (iii) a rise in prices that is already spilling over to other components (housing, transportation, and food, among others), so that the expected base effect may no longer be so favorable.

In this sense, in addition to the economic slowdown that was already expected before the conflict, the ongoing supply shock cannot be ignored, and it shifts the forecast towards a risk of "stagflation." This would see a second round of latent price pressures trickle down from basic inputs to business margins (still disrupted, as indicated by high producer prices), especially in those with high energy dependence (wholesale electricity price in Spain +95%, after +189% in 2021) and whose channeling to the final consumer would consolidate the second-round effects.

Thus, in the short term, as inflation moves markedly higher and away from the target, the monetary policy line would lead towards tighter financial conditions under the umbrella of a still-lax fiscal policy. Although the starting point would continue to be accommodative, such conditions would synchronize with global monetary tightening, albeit at the risk of continuing to weaken the euro against the dollar (see Chart F).

In the medium and long term (as happened with "the Trichet moment") the possibility of placing both the balance sheet and interest rates in neutral territory throughout the current normalization cycle, in an environment of increasing economic and fiscal fragility for EU member countries, could lead to a fiscal dominance event that would very possibly end the current proposed roadmap.

Chart F.
Eurozone: EUR/USD Futures (CME)



Source: MAPFRE Economics (based on Bloomberg data)

Source: MAPFRE Economics

Box 1.1.1-c
Monetary policy update: Federal Reserve

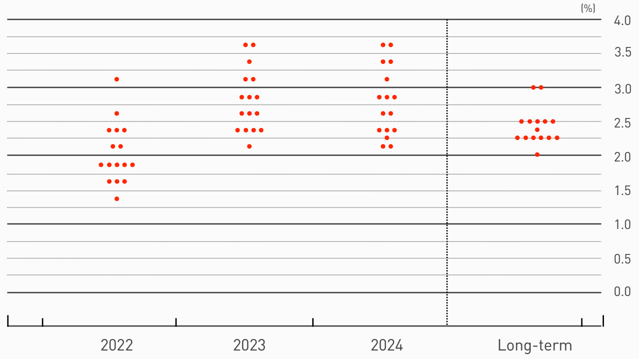
Federal Reserve

The U.S. Federal Reserve, at its March meeting, kicked off the monetary normalization cycle by raising benchmark interest rates by 25 basis points, bringing the range to 0.25%-0.50%. As for their projections, via the dot plot from the Federal Open Market Committee (FOMC), they moved towards a more accelerated pace with six additional rate hikes in 2022 (versus the three announced in December), between three and four additional hikes in 2023 and a slight cut in the longer term (see Chart A). Regarding balance sheet tools, although the Fed is maintaining the planned course of introducing adjustments in asset holdings once the interest rate adjustment process has begun, the details remain incomplete and will be defined in the coming meetings.

On the macroeconomic front, the Federal Reserve's estimates featured a downward outlook for economic activity, with GDP expanding by 2.8% in 2022 and 2.2% in 2023 (vs. 4.0% and 2.2% previously), while the inflation outlook was revised upward, with PCE expected at 4.3% and 2.7% in 2022 and 2023, respectively (vs. 2.6% and 2.3% previously), and core inflation in line with more persistent pressures.

As for the Fed's narrative, it was marked by the ongoing uncertainty surrounding the conflict in Ukraine and its still-uncertain effects on activity and prices. Nonetheless, the risks they are weighing offer less of a tilt on growth and a greater predisposition to control the effects on historically high inflation figures. While certain bottleneck indicators showed recent signs of moderation leading to inventory restocking and relief in producer costs, the effects of an additional endogenous shock, initially in commodity hikes and passed through to manufacturing not yet recovered, compelled the U.S. central bank to a faster pace of tightening to bring monetary policy closer to neutral territory (see Chart B).

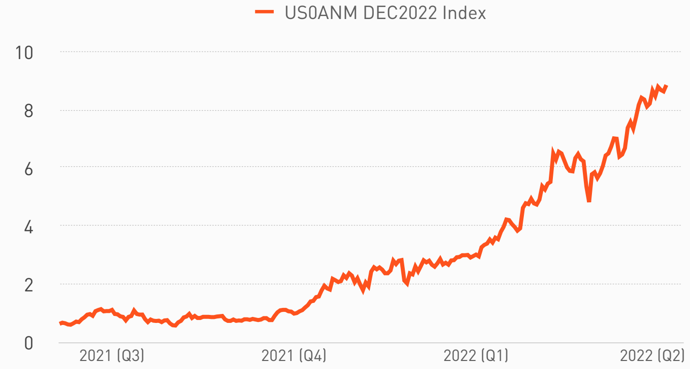
Chart A.
United States: Federal Reserve dot plot



Source: MAPFRE Economics (based on Bloomberg data)

Box 1.1.1-c (continued)
Monetary policy update: Federal Reserve

Chart B.
United States: interest rate hikes expected in 2022

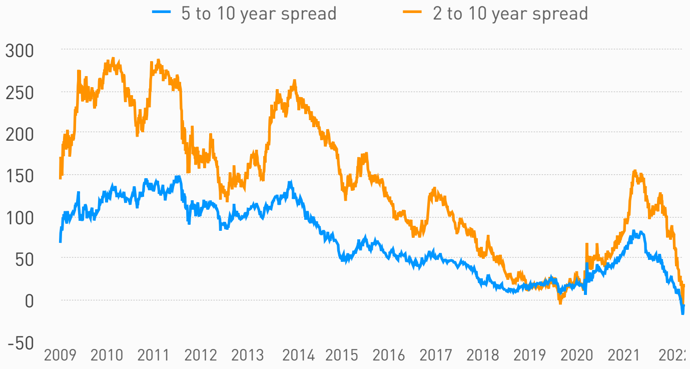


Source: MAPFRE Economics (based on Bloomberg data)

Assessment

As mentioned in previous analyses, the FOMC's priorities have followed the timeline of supporting its decisions from an accommodative approach, in the interest of closing the output gap and employment recovery at the expense of elevated inflation, toward a tightening stance more focused on the price stability mandate as it systematically permeated the inflation outlook. However, in the wake of the current geopolitical crisis, it has been forced to accelerate its change in stance in the face of second-round supply shocks, which, while having a more limited impact than in Europe, given the country's greater energy independence, have caused some economic contagion. In this regard, tighter monetary policy is to be expected as input shocks are transmitted to remaining supply-side rigidities (highlighting the potential for additional manufacturing deterioration from China due to its epidemiological situation and tightening policy).

Chart C.
United States: flattening of interest rate curves



Source: MAPFRE Economics (based on Bloomberg data)

Box 1.1.1-c (continued)
Monetary policy update: Federal Reserve

In the short term, these adjustments are expected to progress towards monetary neutrality, which could lead to additional volatility amplified by geopolitical news flow and some permissiveness to adverse macroeconomic data while preserving the optionality to reverse the process in case of an unfavorable scenario and broader implications. The supply-demand mismatch is expected to take on a more consistent structure in the longer term, normalizing current inflation figures and allowing the neutral interest rate to consolidate in its low band (2.5%). In this way, the Fed would be able to align inflation that, while above target, would follow the declining path with a complete tightening cycle that would give the institution some room to maneuver in terms of interest rates and balance sheet size. However, the risk of causing a recession increases and could be the trigger for a reversal of the process (see Chart C).

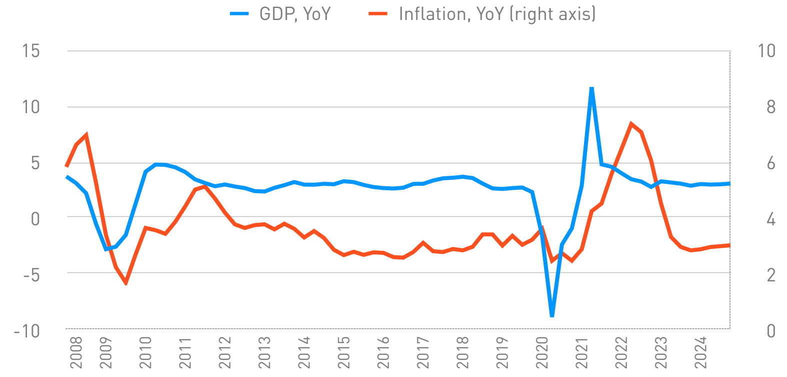
Source: MAPFRE Economics

In terms of inflation and the central banks' reaction function, the rise in prices will become more persistent throughout 2022, giving way in early 2023 to a gradual reversal toward the central banks' long-term target culminating in 2024. In this scenario, developed central banks maintain the current pace of raising interest rates toward the neutral rate in 2022 and 2023, in convergence with an inflation dynamic that is running out of momentum (see Chart 1.1.1-q). Thus, in the *baseline scenario*, the forecast for global GDP growth would be 3.6% in 2022 and 2023, while the inflation forecast (average of the last quarter of the year) would be 6.8% and 4.1% in each of those years (see Table 1.1.1).

Stressed scenario

By contrast, an alternative scenario is considered of a more pessimistic nature (*stressed scenario*), which is defined by two main milestones: (i) a conflict extending beyond 2022, but that does not foresee the confrontation of more international actors (NATO and/or China), and (ii) the risk of

Chart 1.1.1-q
Baseline scenario: GDP and inflation



Source: MAPFRE Economics

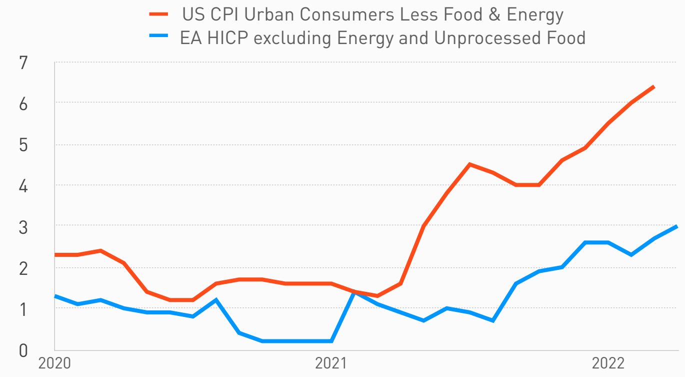
Box 1.1.1-d
The United States and the Eurozone: economic policy asymmetries in the new global context

Two years after the start of the COVID-19 pandemic, the world is now facing a new negative external shock caused by the Russian Army's invasion of Ukraine. After the uneven pace of recovery in the different economies, determined by the effectiveness of national policies to address new coronavirus variants and high levels of public deficit and inflation, the Russia-Ukraine conflict has increased inflationary pressures (high commodity prices, especially for Russian gas and oil and Ukrainian grain, as well as trade distortions in other markets due to sanctions against Russia and other indirect effects). Amid these circumstances, the global economy is slowing down, and the financial markets are experiencing greater volatility (reflected in higher financing costs).

In this regard, although the United States and the European Union are facing the same global scenario, their economic policy formulas are different, as they respond to the specific contexts of each economy. On the one hand, the pace of recovery in the first quarter of 2022 is significantly different: the United States is recovering faster than the average in Europe, where no two countries are alike, not even powers such as Germany and Italy. Meanwhile, even features that may seem similar, such as the high inflation throughout 2021, have taken different paths in the two regions (see Chart A): U.S. inflation was mainly linked to demand factors, given the remarkably high direct payments by the government to the population compared to the OECD average, while the predominant factor in Europe has clearly been supply-driven as a result of the energy crisis.

These differences in economic policy are also determined by exposure to geopolitical risks. One clear example is Europe's greater energy dependence on Russian oil and gas (especially Central and Eastern Europe) compared to the United States, which is also a net energy exporter. As a result, Europe and the United States have different nuances to address in their fiscal and monetary policy choices.

Chart A.
U.S. and Eurozone: inflation without energy and food



Source: MAPFRE Economics (with Haver data)

Box 1.1.1-d (continued)
The United States and the Eurozone: economic policy asymmetries in the new global context

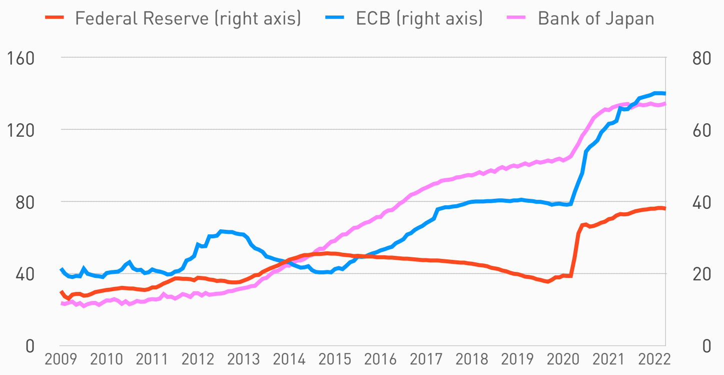
Monetary policy

The European Central Bank (ECB) and the Federal Reserve share a flexible inflation target of around 2%. To meet this objective, the ECB takes a medium-term approach that gives it short-term flexibility, while the Federal Reserve, in addition to controlling inflation, aims to ensure maximum employment and moderate long-term interest rates. The Fed thus has greater flexibility since, in addition to looking after the interests of a single nation (which means less bureaucratic red tape), it needs to respond faster in the short term.

In this context, and in response to the pandemic, both the ECB and the Federal Reserve had to revise their monetary policy strategies (changes published in July 2021 and August 2020, respectively) and generate new control instruments, such as asset purchase programs and forward guidance strategy. This has allowed them to go beyond the conventional stimulus based on lowering interest rates, which were at the effective lower bound (ECB rates were already close to 0% before the pandemic and the Fed lowered its rates to that level in March 2020). The COVID-19 crisis has modified these central banks' current ability to meet their targets after being exposed to a high level of fiscal debt to address it, highlighting the structural deficits accumulated by the Eurozone, which are well above those observed in the U.S. economy.

Now, with the start of the Russian invasion of Ukraine, inflationary pressures are on the rise, leading to a normalization of the measures adopted in response to the pandemic. The ECB has tapered the asset purchases scheduled for this year, while the Federal Reserve has accelerated its bond selling program; both are measures that seek to reduce the central banks' balance sheet to cool inflation (see Chart B). Given this objective, the ECB has adopted a more cautious tone in its forward guidance, planning interest rate hikes that will depend on the short-term economic and geopolitical context, which is quite uncertain, after ending its asset purchases. Meanwhile, the Federal Reserve already raised rates to 0.25% in March and has made it clear that it will continue to do so at its upcoming monetary policy meetings (they should stand at at least 1.25% by the end of 2022).

Chart B.
Selected economies: central bank balance sheet (% GDP)



Source: MAPFRE Economics (with Haver data)

Box 1.1.1-d (continued)
The United States and the Eurozone: economic policy asymmetries in the new global context

At any rate, the confidence of the different economic agents in the central banks' ability to control inflation will be essential, and the fact that it has been held below target for a prolonged period—not to mention fears of another "Trichet moment" (where the ECB raised interest rates and worsened the 2008 crisis)—raise the expectations toward higher inflation.

In this sense, joint European action is taking on renewed importance, where the strengthening of pan-European institutions is a key factor in diversifying the asymmetric risks faced as a result of external shocks. In this framework, tax harmonization is needed to ensure that initiatives, such as the issuing of pan-European bonds to finance the NGEU, find support and can thus become a relevant step in the creation of a secure European asset to help as a monetary control mechanism.

Política fiscal

In comparison with the United States, where the flexibility and speed of the processes for the adoption of economic policy measures in general is remarkable, in Europe these require reaching a broad consensus in an area where the interests of each country are usually in opposition. For example, the United States has already tightened its fiscal policy after forgoing Build Back Better and exhausting the stimulus check mechanism, whereas Europe's implementation of NGEU tranches could result in their use to deal with the current problem.

On the other hand, fiscal policy is affected by the size of the public sector, which is clearly larger in the Eurozone. In this sense, it is clear that fiscal policy in the Eurozone (focused on supporting household and corporate income throughout the pandemic) absorbed the impact of the COVID-19 crisis through its more favorable social welfare systems. These were reinforced through financing schemes for the labor flexibility of companies, tax exemptions, extension of moratoriums, public guarantee programs for granting loans, and supranational programs such as the aforementioned NGEU, whose funds are used to provide loans and/or subsidies to EU member states. The United States carried out similar measures but also opted for programs involving direct transfers to citizens. This formula, repeated under both the Trump and Biden administrations, has generated a larger fiscal deficit due to the size of these programs. In this regard, the United States is already managing plans to increase individual, corporate and additional taxes on large fortunes in order to meet the needs of the fiscal coffers, while in Europe the fiscal imbalance is being addressed by limiting spending after the end of aid programs and exemptions.

As on past occasions, fiscal policy's current dynamics point to it resuming its functions as a mechanism to absorb the energy shock with fewer implications for monetary policy, albeit in a more restrained way, since this implies greater pressure in the future (more debt, deficit, and structurally vulnerable in terms of potential) with less monetary backing. In turn, and as regards a loss of purchasing power given supply-side inflation, while there has been a need to distribute efforts to avoid a price-wage spiral and thus maintain a certain level of competitiveness, with commodities as strong as they are, the strength of the currency used in these exchanges is decisive as it could be another way of losing purchasing power more broadly.

Box 1.1.1-d (continued)
The United States and the Eurozone: economic policy asymmetries in the new global context

Assessment

In a context of global monetary tightening, if Europe allows itself to lag behind other central banks, the euro's purchasing power may erode, which is already being seen in the West (1.10 with negative remuneration against the USD or GBP and with growing remuneration prospects as support). This is also being widely observed in the emerging economies (which were early in the process), and perhaps more notably in China (which is far from joining the global monetary tightening process due to its internal situation)

and Japan (at the end of March, the central bank reemphasized its ultra-loose stance as 10-year JGB yields soared towards the top of its yield curve control target band).

Source: MAPFRE Economics

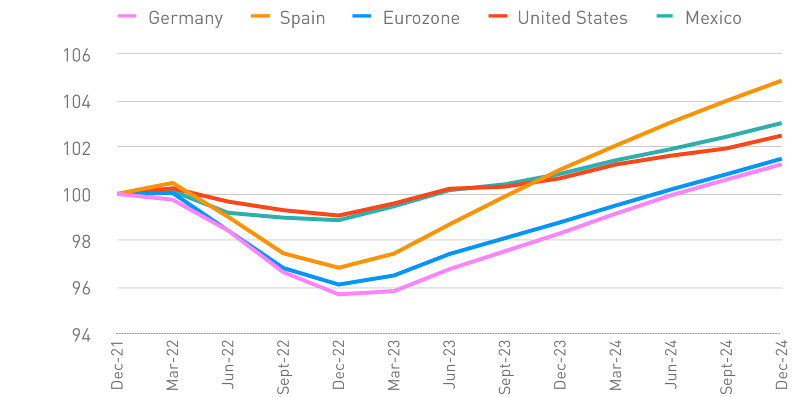
further sanctions that would include specific measures on gas and oil on the Western side (new sanctions or embargoes), or supply cuts on the Russian front side. Compared to the more limited scenario proposed above, the impact on activity in this *stressed scenario* is more unfavorable, with latent stagflationary implications. These would mainly affect Europe, which would see several quarters of negative growth rates, an impact on the markets that have not discounted them, with the current risk aversion returning to levels similar to those of the day of the invasion, a generalized deterioration in consumer confidence and the deterioration of agents' balance sheets (see Chart 1.1.1-r). According to the above, in the *stressed scenario*, we anticipate global economic growth of 3.2% and 2.6% in 2022 and 2023, respectively, with an inflation forecast (average of the last quarter) of 7.8% and 4.3% in each of these years.

Table 1.1.1
Global economy: growth and inflation forecasts under various scenarios of analysis

	GDP growth (YoY)		Inflation (average last quarter)	
	2022(f)	2023(f)	2022(f)	2023(f)
Baseline scenario	3.6%	3.6%	6.8%	4.1%
Stressed scenario	3.2%	2.6%	7.8%	4.3%
Shock scenario	0.8%	0.5%	9.0%	6.2%

Source: MAPFRE Economics

Chart 1.1.1-r
Stressed scenario: Real GDP in selected economies



Source: MAPFRE Economics

Under this second scenario, oil and gas prices will not stabilize until after 2024, with oil prices above 110 USD/b throughout 2022 and above 90 USD/b in 2023. The implications for consumption would entail a further decline in disposable income, deteriorating the pre-existing savings positions since the pandemic and thus agents' balance sheets. In the case of commodities in the aggregate, a later normalization would be impacted, with producer margins under some level of stress and a latent inability to pass through prices across the board.

Consequently, in the *stressed scenario*, inflation rates respond to the hike in a more prolonged manner throughout 2023, eroding consumption in the face of a deeper loss of purchasing power for disposable incomes in real terms and primarily sapping the activity of sectors with less price-fixing capacity.

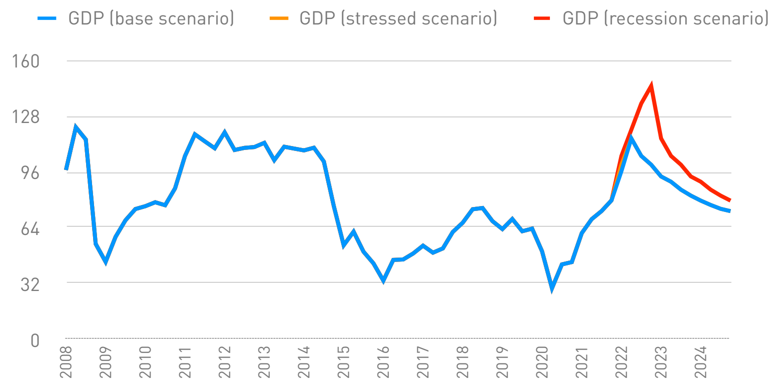
On the economic policy side, the fiscal response would foreseeably become expansionary to cushion the shock, albeit more selectively, deteriorating public accounts as monetary policy moves into a more precipitous normalization. Access to financing in the markets would therefore be affected via higher interest rates, which, despite this, would not turn into a fiscal dominance event like the one in 2012, although it would show increased, more selective spreads that respond to tacit vulnerabilities.

Shock scenario

Finally, there is the *shock scenario* (lower probability and higher impact), which could be caused by one or more of the following factors: (i) an aggravated conflict in which NATO joins the military dynamic, (ii) increased involvement in the conflict by China and other international actors leading to a global trade shock, (iii) a severe disruption of supply chains (COVID-19 shock) combined with an exponentially growing commodity crisis suppressing demand via prices (food crisis and Arab Spring), or (iv) a spillover into the financial channel (Asian Dragon crisis) with a reversal of global flows triggering a recession in late 2022 or early 2023.

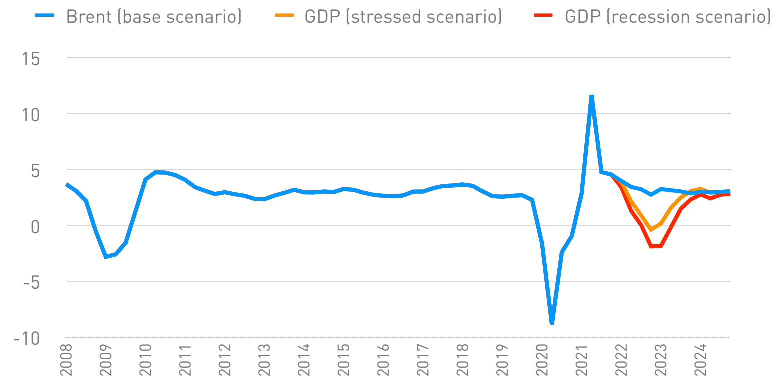
Under this *shock scenario*, oil prices are set at USD 150/b in 2022, USD 100/b in 2023 and above USD 80/b in the long term, in the face of the inability to offset Russian production by players such as Saudi Arabia, Iran, and Venezuela (see Chart 1.1.1-s). Additionally, economic activity is abruptly impacted, triggering a recession with high inflation rates and a growing perception of deterioration in real terms, with GDP growth forecast at just 0.8% and 0.5% in 2022 and 2023, and average inflation in the last quarter of 9.0% and 6.2% in each of those years. The effect on markets is severe, with the negative impact of risk assets reaching two standard deviations, risk aversion in terms of the VIX reaching COVID-

Chart 1.1.1-s
Shock scenario: oil price (Brent spot)



Source: MAPFRE Economics

Chart 1.1.1-t
Shock scenario: GDP (YoY)



Source: MAPFRE Economics

Lehman levels and fiscal dominance reigning in bond markets. As a consequence of this concatenation of events, central banks and governments take a reactive stance, resuming the accommodative policies of balance sheet expansion and the return of interest rates to the Zero Lower Bound (see Chart 1.1.1-t).

1.1.2 Risk assessment

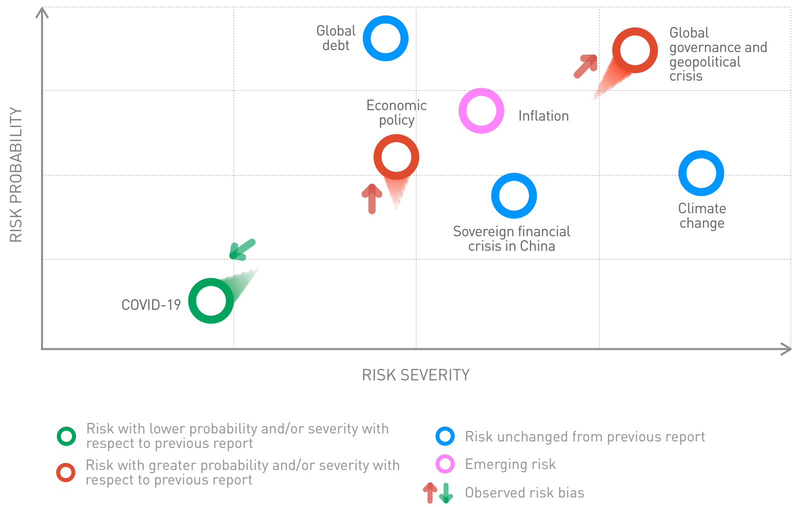
There are several additional potential triggers illustrated schematically on the risk map, which could result in an event similar to a recessionary shock. Chart 1.1.2 illustrates the updated risk map for the global economy as we look ahead to the second quarter.

Global governance and geopolitical crisis

The global governance issues have deteriorated and are centrally driven by the eruption of the conflict in Ukraine during the first quarter of the year. The Russian invasion has generated tension and impacts not only in the military field and in the correlation of global forces (see Box 1.1.1-a), but also in economic terms. These include the escalation of the historical spike in inputs in the field of energy, oil derivatives and food; the growing risk of economic disruption; a temporary increase in risk aversion that has created an environment of greater uncertainty in the financial markets; an accelerated change in monetary policy bias and, overall, greater risks to the pace of recovery of global production capacity and to inflationary pressure control.

On the other hand, global governance is also facing a number of unique situations at this juncture. In the United States, mid-term elections are looming, with President Biden's approval ratings deteriorating amid the erosion of consumer income due to inflation and new signs of polarization that could portend the return of Donald Trump or a similar candidate. In Latin America, meanwhile, fragmentation and polarization are adding to

Chart 1.1.2
Short-term risk balance: vulnerabilities and global risks



Source: MAPFRE Economics

the wounds left by the COVID-19 pandemic. Although some economies enjoy favorable flows from higher-priced commodity exports, the pass-through effect of inflation is eroding most of the income gains. In addition, elections in Brazil and Colombia point to new protagonists in Latin American mob rule.

In North Africa, the inflation of unprocessed products, especially foodstuffs in the form of grain and similar, is driving up the price of bread and food in that region of the world, which is totally dependent on grain from Ukraine and Russia. It should be noted that the Arab Spring of a decade ago took place right in the middle of a food inflationary phase.

Additionally, the European Union is seeing its challenges increasing. Viktor Orbán won by a large majority in Hungary, the division of powers continues to erode in Poland, the German coalition is facing its first problems, and the elections in France have shown how close populism is to the current establishment. Likewise, the pressures on prices have led to multiple forms of protest and supply collapses that run the risk of generating a new yellow vest movement. Finally, the complex situation facing Europeanism, coupled with the invasion of Ukraine, forecasts a severe toll for the Eurozone through energy, trust and trade channels.

Global debt

After reaching a new global all-time high in the first half of 2021 (at the highest level since World War II), the second half of 2021 saw a slight decrease in debt-to-GDP, registering 351% ($303 trillion) thanks to economic activity that remains expansionary on the back of higher inflation rates. In developed markets, this ratio performed better over the year, declining by 12.3 percentage points. Leading the deleveraging were financial and non-financial corporations, followed by the public sector and, to a lesser extent, households. In contrast, emerging markets accumulated more than 80% of the new debt burden, albeit at a slower pace and in a context of higher interest rates in the face of premature monetary tightening.

It should be noted that the momentum of the post-pandemic economic recovery, a moderation in budget deficits, and the additional impact of high inflation rates reducing the real value of debt have helped to ease the accumulated burden. However, as inflation-side pressures become more persistent and monetary policy shifts, financing through negative real interest rates could be diluted, accompanied by less robust economic growth. With this, future fiscal policy faces a process of consolidation in the face of constrained financing via higher interest rates, in a geopolitical context in which economic frictions would be less well supported than during the pandemic to cushion the impact on growth. Accordingly, the ability to coordinate selective fiscal policies is anticipated as a key aspect in maintaining some balance between current high stocks that limit potential, rising debt interest rates and declining economic activity. Thus, the risk of further fiscal expansions could exacerbate the inflationary process, provoking a more aggressive monetary response that triggers selective stress situations. Similarly, and despite a restrictive path, the gradual increase in interest rates may have asymmetric impacts in certain segments with lower credit ratings, as well as in countries with accumulated vulnerabilities and high external financing in foreign currency.

Economic policy

With the acceptance of more persistent inflation rates and the second-round effect from commodity prices as a result of the geopolitical conflict, the risk of wages not keeping up, and thus to the long-term inflation outlook, has pushed monetary tightening into a more precipitous phase than initially anticipated. While the core scenario remains one of gradual planning, correctly transmitted to the markets and with limited impact on activity, there is an increased risk of erratic action by the main central banks as they attempt to achieve neutral policies somewhat further from consensus and without sufficient time to assess the impact not only on prices, but also on economic growth. In this sense, the risk could be exacerbated by fiscal policy becoming decoupled from monetary policy, given the potential propensity to dampen the current shock with newly expansionary fiscal policies, the feedback of a more rapidly accelerating inflation, and the risk of an unanticipated impact (both on the economic performance side and on the financial markets side) amid perceptions of an oversized tightening cycle that would support the reversal of the process.

Sovereign financial crisis in China

Uncertainty in China remains as restrictions under the zero-tolerance COVID-19 policy spread across more regions of the country, exacerbating the risk of economic slowdown (the latest PMI data, from March, shows a contraction in industry and services) while exposing further difficulties on the consumption side, additional supply shocks and heightening fears about the real estate sector. In this sense, the central bank continues to provide the economy with looser financial conditions, reinforcing countercyclical regulations and stimulating the export channel with the intention of providing the country with some macroeconomic stability. However, despite these attempts to shore up the economy, the crisis in the real estate sector continues to create problems. While Evergrande's restructuring process continues, new developers are facing the slowdown in the sector, highlighting the downgrading of the third largest developer (Sunac) and stating that the signs about the sector are still worrying.

In addition to these doubts, there is the ambiguous geopolitical positioning around the Russia-Ukraine conflict, whose tail risk could trigger international sanctions that resume the uncertainty generated during the Trump-era trade war, expanding the problems in global supply chains. All in all, and despite efforts to address financial vulnerabilities, shore up fragile growth, and resolve structural problems, the risk of triggering a debt crisis with systemic potential for sovereign-financial spread remains real.

Climate change

The most recent progress in addressing the climate crisis through a broad policy framework of international awareness following COP-26 at the end of 2021 has been overshadowed by Russia's invasion of Ukraine, highlighting broad global energy security issues. The disruption in energy and other commodity supplies poses an additional challenge to the energy transition trajectory worldwide, with particular relevance to the case of the European Union and its Green New Deal plans, due to the pronounced direct impact of the conflict, high current energy dependence and the potential for wider sanctions. While this crisis may generate additional impetus for investment, lay the foundations for a more robust project, and accelerate development plans on a broader scale, in the short term, managing current risks may require investment policies based on antagonistic positions, reactivating energy plans and temporary carbon-intensive increases. This process requires focusing on safeguarding more immediate interests, to be offset by doubling efforts for energy transition in the medium and long term.

COVID-19

According to the latest epidemiological report from the World Health Organization (WHO), the number of new cases and deaths from COVID-19 has been decreasing since the end of March 2022. During the week of April 11-17, 2022, the number of new COVID-19 cases decreased by 24% compared to the previous week while deaths fell by 12% (see Charts 1.1.1-c and 1.1.1-d). The Omicron variant, which is currently classified as a variant of concern, is the most widely circulating in the world, especially the BA-2 sublineage, which has a higher transmission rate than BA-1. However, the global circulation of all Omicron variants is declining, although WHO will maintain close surveillance of the BA.2 sublineage and has asked countries not to let their guard down. Recombinant variant XE, resulting from the combination of the BA.1 and BA.2 sublineages, is being tracked by WHO as part of the Omicron variant, and early estimates suggest a 10% transmission advantage compared to BA.2, although further confirmation is needed.

The presence of coronavirus will continue for many years to come, and a number of governments have already considered a gradual return to "normalcy," while continuing to pay attention to new variants and outbreaks. In general, this means that epidemiological risk is no longer the main determinant of activity levels, as was the case during the last two years. In the past few months, progress has been made in practically eliminating all the restrictions[2] established by many governments to control the spread of the virus, including using face masks indoors. Countries such as Singapore, Vietnam, Australia, and New Zealand, which in the past maintained a strategy of maximum COVID-19 control and suppression, abandoned it at the end of 2021, removing part of the restrictions and increasing their vaccination efforts. In contrast, China and its financial center Hong Kong continue to apply the COVID Zero tactic, even though the strict measures imposed come at a high economic cost. The Institute for Health Metrics and Evaluation (IHME) believes that the chances of containing the spread of omicron in China are very limited and projects that in the long term it will have a significant increase in infections and deaths, with a peak towards the end of May[3].

Regarding the need for and potential benefit of a second booster dose of vaccination (fourth dose), there are differing responses from regulators. However, most experts agree in recommending the need for a fourth dose in the population at risk of severe illness, hospitalization, and death. In

Europe, available studies and epidemiological data are being reviewed to provide a common position for European Union and European Economic Area countries on this issue, and some of them have already recommended a fourth dose for different vulnerable population groups. In the United States, the Food and Drug Administration (FDA) has authorized a fourth dose for persons over 50 years of age and certain immunocompromised persons. In addition, several countries in the Asia-Pacific region are also preparing for the administration of the fourth dose, pending in some cases the determination of the eligible population.

Experts' opinion on the future prospects of the pandemic is affected by the appearance of new variants, their virulence and transmissibility, and the effectiveness of vaccines and antivirals against them. Some predict that COVID-19 will become a seasonal, predominantly winter disease, where the most vulnerable people will need to receive booster vaccinations. Some pharmaceutical companies are already developing variant-specific vaccines that could target whatever strain is circulating when the booster is needed, while others advocate shifting the focus from vaccination to production and distribution of antivirals to mitigate the impact of COVID-19.

Inflation

From a contextual point of view, the current implications for inflation risk are based on a predominantly supply-side inflation, with special mention of the direct impact of the Russia-Ukraine conflict through the energy component and other inputs that feed back into the initial bottleneck problem, produced by the measures implemented to control the health effects of the COVID-19 pandemic. Thus, the potential risk is, firstly, the possibility of triggering second-round effects on wages in the short and medium term, which would exacerbate the current inflation problem by placing it above the central banks' target for a prolonged period of time and, ultimately, the risk of persistence leading to de-anchoring and an upward revision of long-term inflation expectations.

Consequently, the central banks' reaction function reinforces these dynamics, leading first to the need for orthodox policies towards monetary neutrality and then, less anticipated than expected, into the restrictive realm. In this scenario, while the neutral rate is likely to converge with inflation rates in a downward direction in 2022–2023, should monetary policy measures prove insufficient to moderate demand-side inflation expectations, or should the supply-side shock become more persistent, this would lead to an even more aggressive tightening, penalizing consumption and economic activity to avoid shifts in inflation towards structurally higher levels.

1.2 Forecasts and risk assessment in selected economies

1.2.1 United States

Solid activity indicators,
but with strong inflationary pressures.

Inflation remains high (8.5% March), including core inflation (6.5%), with robust demand and a strong labor market (unemployment at 3.6% in March). All of this, along with supply chain problems coming from 2021, has led to an imbalance between supply and demand that puts pressure on prices. The San Francisco Federal Reserve is already questioning whether the stimulus, not only monetary but also fiscal, was excessive.

U.S. economic policy will have to decide how to make a soft landing. Inflation slows down the economy in that it reduces purchasing power. Monetary policy will have to become more restrictive to deal with it, which will be a further factor in the slowdown in economic activity. Thus, the Federal Reserve will now have to carefully weigh the pace of interest rate hikes. In this regard, at its March meeting, it announced a rate hike of 0.25 basis points (bps) to 0.25%-0.50% and indicated that, at a forthcoming meeting, without specifying whether it would be the next one, it would begin to reduce the balance sheet. For now, its strategy has been to clearly communicate that there will be a series of interest rate hikes, which should number nine or 10 of 0.25 bps in 2022 (to end the year at around 2.5%) and with no foreseeable changes for 2023.

- Inflation continues to exert pressure, reaching 8.5% in March, with core inflation at 6.5%.
- The Federal Reserve raised interest rates in March by 0.25 bps to 0.25-0.50%.
- The labor market is strong; only consumer confidence reveals some skepticism for the coming months.
- The conflict in Ukraine may aggravate supply problems, including agricultural fertilizers.

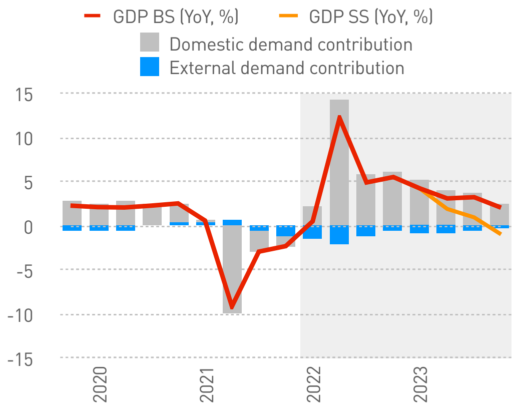
Accordingly, a slowdown in economic activity is inevitable due to inflation and energy costs in particular, as well as the still unresolved supply chain problem and the tightening of monetary policy. There is significant uncertainty in this context regarding prices, the labor market, and how consumption and investment will react. In this sense, we estimate that consumption will still perform reasonably well, due to the strength of the labor market and accumulated savings, while investment will slow down and exports will be reactivated, especially in energy and military equipment.

At the indicator level, the purchasing managers' indexes (PMIs) for April remain positive, which is consistent with the strong demand, with the composite and manufacturing index at 59.7 and the services index at 54.7. In the labor market, job creation continues and unemployment is at a record low of 3.6% in March. The Conference Board consumer confidence indicator is unchanged at 107.2, but the University of Michigan's worsened to 64.1. Thus, our new growth estimate is now 3.2% and 1.7% for 2022 and 2023, downgraded from 4.0% and 2.5% in our previous report (see Table 1.2.1 and Charts 1.2.1-a and 1.2.1-b).

As mentioned above, March inflation rebounded to 8.5% and core to 6.5%, with food +8.8%, energy +32%, motor fuels +48%, and natural gas +22%. The main risk now is how to bring down inflation without sending the economy into a recession. We are therefore in a highly dynamic scenario in which the government and the Federal Reserve will have to adjust the course of the economy without making drastic moves, while carefully analyzing the macroeconomic data, and particularly the behavior of the labor market in response to inflation, as it comes out.

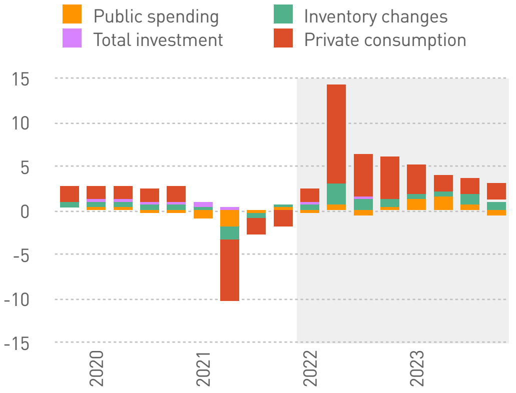
On November 8, congressional elections will be held. The Democrats will try to avoid an economic crisis at all costs, which would give Congress to the Republicans. Historically, the state of the economy and household finances are very significant factors influencing the outcome of elections. The Biden administration is considering releasing strategic oil reserves in an attempt to reduce domestic energy prices. However, the conflict in Ukraine may exacerbate supply problems, including disruptions in the agricultural fertilizer market. The best news that could come would be a ceasefire in Ukraine, assuming a status quo at the geopolitical level that would imply, among other issues, that the United States accepts the reality of a multipolar world where different world powers must coexist.

Chart 1.2.1-a
United States: GDP breakdown and forecasts



Source: MAPFRE Economics (based on Federal Reserve data)

Chart 1.2.1-b
United States: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on Federal Reserve data)

Table 1.2.1
United States: main macroeconomic aggregates

						Base (EB)		Estresado (EE)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	2.3	2.9	2.3	-3.4	5.7	3.2	1.7	1.5	0.6
Domestic demand contribution	2.5	3.3	2.5	-3.3	7.0	3.9	1.4	2.0	0.2
External demand contribution	-0.2	-0.3	-0.2	-0.1	-1.3	-0.7	0.3	-0.4	0.4
Private consumption contribution	1.7	2.0	1.5	-2.6	5.6	2.3	1.1	0.9	0.7
Total investment contribution	0.8	0.9	0.7	-0.3	1.3	0.9	0.4	0.5	-0.2
Public spending contribution	0.0	0.2	0.3	0.3	0.1	0.0	0.2	0.0	0.2
Private consumption (% YoY)	2.4	2.9	2.2	-3.8	7.9	3.3	1.6	1.3	1.0
Public spending (% YoY)	0.0	1.2	2.0	2.0	1.1	-0.1	1.1	-0.1	1.1
Total investment (% YoY)	3.8	4.4	3.1	-1.5	6.1	3.9	2.0	2.3	-1.1
Exports (% YoY)	4.1	2.8	-0.1	-13.6	4.6	6.2	6.4	4.7	4.9
Imports (% YoY)	4.4	4.1	1.1	-8.9	14.0	6.7	1.9	4.4	0.3
Unemployment rate (%, last quarter)	4.2	3.8	3.6	6.8	4.2	3.4	3.7	4.0	4.1
Inflation (% YoY, last quarter)	2.1	1.9	2.3	1.4	7.0	6.9	3.0	7.3	3.8
Fiscal balance (% of GDP)	-4.2	-6.1	-6.3	-15.3	-11.9	-5.9	-6.0	-6.5	-6.9
Primary fiscal balance (% of GDP)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Trade balance (% of GDP)	-4.2	-4.3	-4.1	-4.3	-4.8	-5.2	-4.8	-5.2	-4.7
Current account balance (% of GDP)	-1.9	-2.1	-2.2	-2.9	-3.6	-4.1	-3.5	-4.0	-3.3
Official interest rate (end of period)	1.50	2.50	1.75	0.25	0.25	2.50	2.50	2.75	3.00
3-month interest rate (end of period)	1.69	2.81	1.91	0.24	0.21	1.95	2.57	2.28	3.20
10-year interest rate (end of period)	2.40	2.69	1.92	0.93	1.52	3.00	3.32	3.50	4.00
Exchange rate vs. U.S. dollar (end of period)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Exchange rate vs. euro (end of period)	1.20	1.15	1.12	1.23	1.13	1.13	1.16	1.11	1.12
Private lending (% YoY, average)	6.9	4.6	5.3	6.2	15.6	8.2	-0.7	7.7	-0.9
Household lending (% YoY, average)	3.4	3.5	3.0	3.4	6.5	8.0	6.8	8.0	7.0
P.S. non-financial lending (% YoY, average)	6.1	9.1	6.6	8.7	2.1	7.3	4.8	7.4	4.8
P.S. financial lending (% YoY, average)	2.9	2.2	2.2	5.6	4.2	2.3	1.3	2.4	1.4
Savings rate (% pers. disp. income, avg.)	7.3	7.6	7.6	16.4	12.1	6.0	6.3	6.8	6.8

Source: MAPFRE Economics (based on Federal Reserve data)
Forecast end date: April 28, 2022

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1.2.2 Eurozone

Higher inflation, lower growth.

The context for the Eurozone economy has changed substantially. The invasion of Ukraine has added stress to energy prices and to inflation that had started to rise in January 2021. At the time, it was just the imbalance between demand (encouraged with aid) and supply (constrained by confinements and other supply chain problems). Then gas price tensions began to mount in the face of Germany's non-approval of the Nordstream 2 pipeline, paid for by Russia, on the eve of the German elections in September. In fact, in order to press for a decision, Russia began to put pressure on gas prices. From there, and in the absence of alternatives to supply gas in the energy production mix, came the tension in electricity prices. Electricity has risen in a year by 34% (February), gas by 41.4%, motor fuels by 42.7%, and heating energy by 23.4%. The problem is rooted in producer costs (PPI), which have risen by 31.4% in one year. For a while, producers themselves have absorbed the impact, but the blow is now expected to be passed on to end-consumer prices.

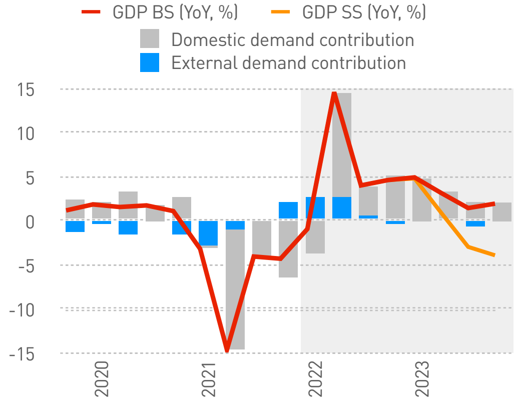
Overall inflation in the Eurozone reached 7.4% in March, with core inflation rising to 2.9%. With the Ukrainian conflict and sanctions in place, it is difficult to foresee energy costs going down; they are only expected to come down if a peace agreement is reached. There are doubts that, even with peace, the West will be in a position to restore the previous situation. The confirmation that Germany and other European countries are looking for energy alternatives points to a new energy framework rather than a situation of replenishment of previous sources of supply. It is also important to note that there is significant price tension and even a reduction in the supply of fertilizers, which will result in higher prices for agricultural products. However, if at least energy stabilizes due to the base effect, inflation will decrease.

As for indicators, the purchasing managers' index (PMI) in the Eurozone had mixed performance, with the composite index at 55.8 points, manufacturing at 55.3, and services at 57.7. The European Commission's Economic Sentiment Indicator also worsened to 108.5; consumer sentiment declined to -18.7, manufacturing fell to 10.4, and services rose to 14.4.

All in all, inflation is expected to be higher and more persistent than in the pre-Ukraine invasion scenario. However, the forecast has become more complicated due to volatility in energy prices. The rise in prices will not be accompanied by wage growth to the same extent, so the squeeze on consumer purchasing power will affect growth. In this context, we have lowered our estimate for Eurozone economic growth to 2.9% in 2022 (from 3.9% previously), and maintained 2.7% for 2023 (see Table 1.2.2 and Charts 1.2.2-a and 1.2.2-b).

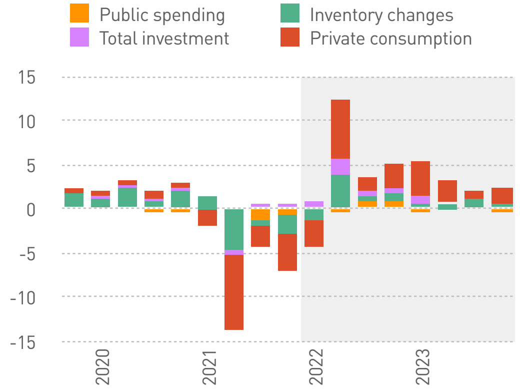
- **An inflationary upward cycle has been unleashed; getting it back on track will be difficult, especially because of high producer prices. It is expected to moderate somewhat due to the base effect.**
- **Energy is an issue to be resolved, but it will not be easy or quick. There will not be a return to the status quo, but alternatives will be sought.**
- **The ECB already pivoted toward ending the purchase program, but it is taking its time before raising interest rates.**
- **The 2022 GDP growth forecast has been lowered to 2.9% from the previous 3.9%.**

Chart 1.2.2-a
Eurozone: GDP breakdown and forecasts



Source: MAPFRE Economics (based on ECB data)

Chart 1.2.2-b
Eurozone: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on ECB data)

Table 1.2.2
Eurozone: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	2.8	1.8	1.6	-6.5	5.3	2.9	2.7	-0.3	-0.2
Domestic demand contribution	2.3	1.7	2.4	-6.1	3.9	3.0	2.8	-0.3	-0.3
External demand contribution	0.5	0.1	-0.9	-0.4	1.4	-0.1	-0.1	0.0	0.2
Private consumption contribution	1.0	0.8	0.7	-4.2	1.8	2.3	1.9	0.5	0.8
Total investment contribution	0.9	0.6	1.5	-1.6	0.9	0.6	0.8	-0.5	-0.8
Public spending contribution	0.2	0.2	0.4	0.2	0.8	0.2	0.2	0.2	0.2
Private consumption (% YoY)	1.9	1.4	1.4	-8.0	3.5	4.4	3.6	1.0	1.4
Public spending (% YoY)	1.1	1.0	1.8	1.1	3.8	1.0	0.8	1.0	0.8
Total investment (% YoY)	4.2	3.1	6.8	-7.3	4.3	3.0	3.8	-2.5	-3.7
Exports (% YoY)	6.0	3.6	2.7	-9.4	10.9	4.3	3.4	1.8	0.6
Imports (% YoY)	5.5	3.7	4.8	-9.2	8.6	4.9	3.8	2.1	0.3
Unemployment rate (%, last quarter)	8.8	8.0	7.5	8.3	7.1	7.5	7.4	8.9	9.1
Inflation (% YoY, last quarter)	1.4	1.9	1.0	-0.3	4.6	5.5	3.0	6.0	3.5
Fiscal balance (% of GDP)	-0.9	-0.4	-0.6	-7.2	-5.4	-4.0	-2.8	-5.4	-5.6
Primary fiscal balance (% of GDP)	1.0	1.4	1.0	-5.7	-3.9	-2.6	-1.5	-3.9	-4.1
Trade balance (% of GDP)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current account balance (% of GDP)	3.2	3.1	2.4	1.9	2.5	1.1	1.3	0.1	0.2
Official interest rate (end of period)	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.00
3-month interest rate (end of period)	-0.33	-0.31	-0.38	-0.55	-0.57	-0.42	0.16	-0.24	-0.26
10-year interest rate (end of period)	1.13	1.17	0.32	-0.19	0.32	1.20	1.85	1.90	3.00
Exchange rate vs. U.S. dollar (end of period)	1.20	1.15	1.12	1.23	1.13	1.13	1.16	1.11	1.12
Exchange rate vs. euro (end of period)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Private lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Household lending (% YoY, average)	2.3	2.4	3.4	2.9	3.5	3.1	5.3	2.4	3.3
P.S. non-financial lending (% YoY, average)	1.2	1.9	2.0	2.5	3.0	3.6	3.5	1.8	1.0
P.S. financial lending (% YoY, average)	1.5	-0.5	1.4	-2.5	-0.2	0.7	2.8	0.6	3.1
Savings rate (% pers. disp. income, avg.)	12.3	12.5	13.0	19.5	17.8	13.3	12.2	14.3	12.8

Source: MAPFRE Economics (based on ECB data)
Forecast end date: April 28, 2022

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At its March meeting, the European Central Bank (ECB) decided to accelerate the tapering of the conventional asset purchase program (APP) from April to June and indicated that subsequent months would be decided on the basis of emerging data. It also indicated that interest rate hikes would start "some time after" the end of the APP and would be gradual. The Governing Council is prepared to maintain a monetary policy that supports the recovery, as implied by the "non-hikes" when other central banks are raising interest rates. However, the ECB could come under pressure from inflation and inflation expectations in the markets.

The risk for the economy of the Eurozone is mainly the upturn in inflation, which will reduce disposable income for consumers, and margins for companies, making them more cautious in their investment decisions, which will take its toll on the growth of the economy. The resolution of the energy problem will be key in the coming months, and even years. While inflation will only moderate due to the baseline effect, the vicious cycle of climbing prices has begun, and getting inflationary dynamics back on track will be a difficult task.

1.2.3 Spain

Concerns are centered on energy costs.

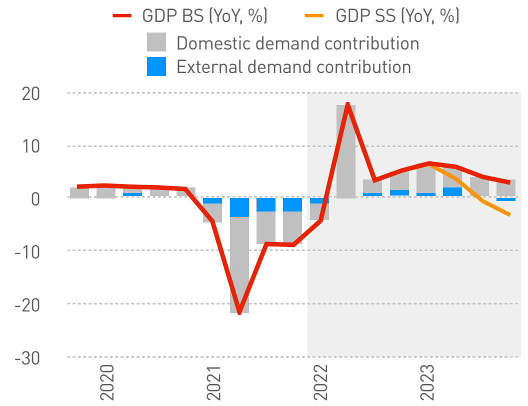
Spain's economy grew at a good pace in the second half of 2021, rising 2.6% QoQ and 2.9% QoQ in the third and fourth quarters, respectively. However, the picture has changed with rising energy and food costs, bringing headline inflation to 9.8%. Growth is now expected to fall in the first two quarters (by around 0.6% QoQ), because real household disposable income is decreasing as a result of rising prices.

With respect to circumstantial indicators, the purchasing managers' index (PMI) was down in March, with the composite index at 53.1 points, manufacturing at 54.2, and services at 53.4. February retail sales slowed to 0.9% YoY from 4.0% previously (seasonally adjusted). Consumer confidence, meanwhile, came in at -9 in February, with the components relating to the future economic situation at -0.4. Industrial production fell 0.1% MoM (+1.7% YoY) in January, with further contractions expected in the remaining months of the quarter due to factory shutdowns caused by high energy costs. In this context, we have revised the growth outlook for the Spanish economy for 2022 to 4.2%, from 5.5% in our previous report, and to 3.0% for 2023, from 4.3% previously (see Table 1.2.3 and Charts 1.2.3-a and 1.2.3-b).

- **The increase in energy costs has been passed on to the other CPI categories.**
- **In food it is evident, since the price of fertilizers will exacerbate it.**
- **Likewise, this situation has generated shutdowns in freight transport and fishing and serious problems in agriculture and livestock farming.**
- **The government has activated relief measures, but only after these shutdowns.**

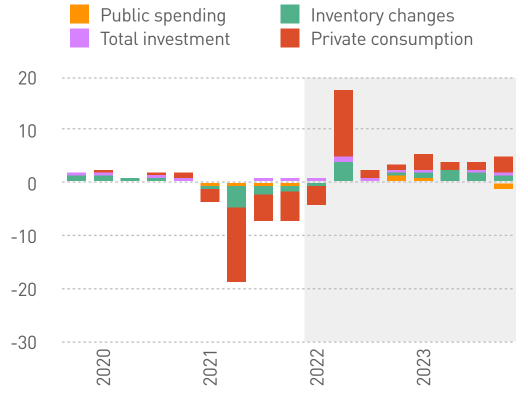
The Spanish government has activated support to alleviate the economic impact of the war in Ukraine, through aid and loans to companies, discounts on fuel, tax reductions on electricity bills and aid to agriculture and fishing. Most of the aid arrived only at the end of March, after a 15-day truckers' strike, farmers' demonstrations, and with the fishing fleet unable to fish.

Chart 1.2.3-a
Spain: GDP breakdown and forecasts



Source: MAPFRE Economics (based on INE data)

Chart 1.2.3-b
Spain: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on INE data)

Table 1.2.3
Spain: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	3.0	2.3	2.1	-10.8	5.0	4.2	3.0	-0.5	-0.3
Domestic demand contribution	3.2	2.9	1.6	-8.8	4.6	3.5	3.1	0.2	-0.1
External demand contribution	-0.2	-0.7	0.5	-2.1	0.4	0.7	0.1	-0.7	-0.2
Private consumption contribution	1.8	1.0	0.6	-6.8	2.6	2.0	1.9	0.2	0.4
Total investment contribution	1.3	1.2	0.9	-1.9	0.8	1.1	1.0	0.0	-0.5
Public spending contribution	0.2	0.4	0.4	0.7	0.6	0.3	0.2	0.1	0.1
Private consumption (% YoY)	3.0	1.7	1.0	-12.0	4.6	3.6	3.5	0.6	2.2
Public spending (% YoY)	1.0	2.3	2.0	3.3	3.0	1.6	1.0	1.6	1.0
Total investment (% YoY)	6.8	6.3	4.5	-9.5	4.1	7.3	6.3	1.0	-2.5
Exports (% YoY)	5.5	1.7	2.5	-20.2	13.4	7.9	4.1	5.7	1.7
Imports (% YoY)	6.8	3.9	1.2	-15.2	12.8	6.5	5.0	2.7	-0.9
Unemployment rate (%, last quarter)	16.6	14.5	13.8	16.1	13.3	14.2	13.9	16.8	16.4
Inflation (% YoY, last quarter)	1.1	1.2	0.8	-0.5	6.6	5.5	2.1	7.0	2.6
Fiscal balance (% of GDP)	-3.0	-2.5	-2.9	-11.0	-7.0	-5.5	-4.1	-7.2	-6.9
Primary fiscal balance (% of GDP)	-0.5	-0.1	-0.6	-8.8	-4.9	-3.6	-2.3	-5.2	-4.9
Trade balance (% of GDP)	-1.9	-2.4	-2.2	-0.8	-1.5	-4.1	-4.2	-5.5	-5.1
Current account balance (% of GDP)	2.8	1.9	2.1	0.8	0.7	0.6	1.4	-0.5	0.9
Official interest rate (end of period)	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.00
3-month interest rate (end of period)	-0.33	-0.31	-0.38	-0.55	-0.57	-0.42	0.16	-0.24	-0.26
10-year interest rate (end of period)	1.57	1.42	0.47	0.06	0.60	2.20	2.80	2.85	3.53
Exchange rate vs. U.S. dollar (end of period)	1.20	1.15	1.12	1.23	1.13	1.13	1.16	1.11	1.12
Exchange rate vs. euro (end of period)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Private lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Household lending (% YoY, average)	-1.4	-0.3	-0.2	-0.9	0.0	2.0	3.7	1.3	1.5
P.S. non-financial lending (% YoY, average)	-1.1	-2.0	-0.8	1.8	3.1	2.9	3.0	-3.6	-6.8
P.S. financial lending (% YoY, average)	-5.9	3.8	-6.5	1.6	0.2	-3.2	3.6	-3.2	4.3
Savings rate (% pers. disp. income, avg.)	5.8	5.6	8.3	15.2	11.3	7.6	6.0	8.4	6.7

Source: MAPFRE Economics (based on INE data)
Forecast end date: April 28, 2022

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In a special meeting to address the energy issue, the EU approved a proposal by Spain and Portugal to consider the Iberian Peninsula an "energy island" due to its poor energy connection with the rest of Europe. Spain has experienced one of the highest electricity price increases in Europe. They have therefore been authorized by Brussels to cap prices in the wholesale electricity market. The argument is that in the formula for calculating the European pool, gas has a much higher weight than in the Spanish production mix. This results in high margins for the electricity companies that use other production technologies, known as "windfall profits."

Inflation stood at 9.8% YoY in March (+3.0% MoM), highlighting the cost of housing, housing supplies and transport. Core inflation rose to 3.4%, which shows that energy and raw material costs are already affecting the other items. Food price increases are evident (6.8% in March) and high fertilizer prices will aggravate them. The price increase in production is surprisingly high (+40.7% in February) due to electricity and gas costs, causing the interruption of production in many factories. The government has called for wage moderation, raised pensions by only 2.5%, and is trying to limit price increases (rental housing 2%) to limit inflation.

The risks for Spain's economy are mainly the energy cost and a possible extension of inflation to all categories. The energy problem does not have a quick solution, and the intervention in the price, although unconventional, would allow it to adjust to the reality of the mix of Spanish production. Caution should be exercised, because failure to arrive at a coherent price could discourage investment, just when it is needed most. The Ukrainian conflict has generated price increases in energy and fertilizers, which have affected many agricultural products, even in countries that were not direct importers, as prices have risen in international markets (wheat, corn, sunflower oil, etc.). Additionally, tourist inflows should continue to recover as concerns about the pandemic subside, so good news is expected on that front. Finally, in a more structural and medium-term perspective, the effective use of European Union funds is essential to generating dynamism in the Spanish economy.

1.2.4 Germany

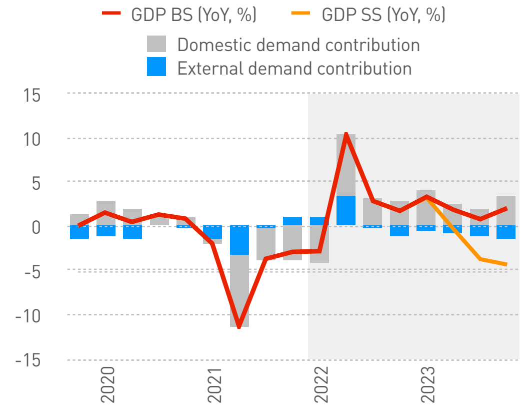
Expectations are trending downward significantly.

German GDP in the last quarter of 2021 contracted quarter-on-quarter (-0.35% QoQ) as a result of the constraints generated by the Omicron variant. The start of 2022 looked stable until the conflict in Ukraine broke out. Now there could even be a small contraction in the first quarter of 2022 due to high energy prices and supply chain problems that will tend to worsen instead of improving.

Business IFO expectations visibly worsened in March to 85.1 from 99.2, and the assessment of the current situation also declined to 97.0 from 98.6 previously. ZEW expectations dropped dramatically to -39.3 from +54.3. GfK consumer confidence has been worsening for four months, moving into negative territory (-8.1 in March), while in November it was in positive territory. Additionally, the PMIs (purchasing managers' indexes) fell again in April, with the composite index at 54.5, the services index at 57.9 and the manufacturing index at 54.1 points.

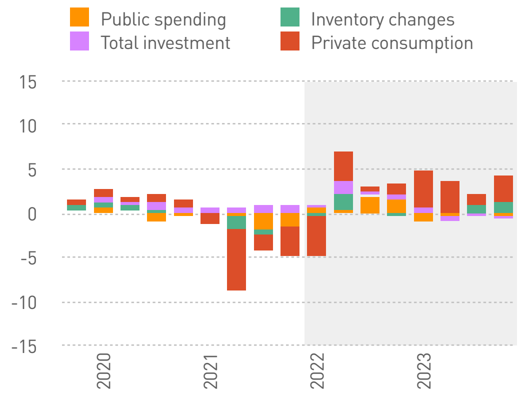
A negative perception of the future by companies will make investment decisions more cautious, which will affect GDP. In this context, we have again downgraded our growth estimates for the German economy, although we believe it will avoid recession in 2022 unless there is an energy supply cut from Russia, as it will be difficult for Germany to fully replace Russian gas supplies (>50% of its purchases). Thus, our GDP

Chart 1.2.4-a
Germany: GDP breakdown and forecasts



Source: MAPFRE Economics (based on DESTATIS data)

Chart 1.2.4-b
Germany: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on DESTATIS data)

Table 1.2.4
Germany: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	3.0	1.1	1.1	-4.9	2.9	2.0	3.1	-1.3	-0.5
Domestic demand contribution	2.7	1.6	1.8	-4.0	2.1	3.0	3.9	-0.5	-0.2
External demand contribution	0.3	-0.5	-0.7	-0.9	0.7	-1.0	-0.8	-0.8	-0.3
Private consumption contribution	0.9	0.7	0.9	-3.2	0.1	3.1	2.7	1.3	1.2
Total investment contribution	0.7	0.7	0.4	-0.6	0.3	0.6	1.1	-0.6	-0.8
Public spending contribution	0.3	0.2	0.6	0.8	0.7	-0.2	0.2	-0.2	0.2
Private consumption (% YoY)	1.7	1.4	1.6	-6.1	0.1	5.9	5.0	2.4	2.3
Public spending (% YoY)	1.7	1.0	3.0	3.5	3.1	-0.9	0.8	-0.9	0.8
Total investment (% YoY)	3.3	3.5	1.9	-3.0	1.3	2.7	5.2	-2.8	-4.0
Exports (% YoY)	5.6	2.5	1.1	-10.1	9.8	3.7	2.9	1.1	0.0
Imports (% YoY)	5.7	4.0	2.9	-9.2	9.1	6.3	4.8	3.2	0.8
Unemployment rate (%, last quarter)	5.5	5.1	5.0	6.2	5.3	5.2	5.1	6.9	7.3
Inflation (% YoY, last quarter)	1.4	1.6	1.5	-0.3	5.3	5.5	2.6	7.5	3.0
Fiscal balance (% of GDP)	1.3	1.9	1.5	-4.3	-3.7	-2.5	-1.3	-4.0	-4.7
Primary fiscal balance (% of GDP)	2.3	2.8	2.3	-3.7	-3.1	-1.9	-0.7	-3.4	-4.1
Trade balance (% of GDP)	7.8	6.8	6.3	5.6	5.1	2.5	2.4	1.4	0.8
Current account balance (% of GDP)	7.8	7.9	7.6	6.8	7.0	3.7	3.5	2.8	2.3
Official interest rate (end of period)	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.00
3-month interest rate (end of period)	-0.33	-0.31	-0.38	-0.55	-0.57	-0.42	0.16	-0.24	-0.26
10-year interest rate (end of period)	0.43	0.25	-0.19	-0.58	-0.18	1.00	1.60	1.40	1.80
Exchange rate vs. U.S. dollar (end of period)	1.20	1.15	1.12	1.23	1.13	1.13	1.16	1.11	1.12
Exchange rate vs. euro (end of period)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Private lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Household lending (% YoY, average)	3.2	2.3	4.7	4.3	3.8	1.7	10.4	0.7	7.4
P.S. non-financial lending (% YoY, average)	3.9	9.4	4.4	3.5	2.8	3.6	3.3	3.4	2.2
P.S. financial lending (% YoY, average)	-1.6	0.4	10.3	9.5	11.0	6.6	5.1	6.7	5.6
Savings rate (% pers. disp. income, avg.)	10.6	11.3	10.7	16.2	15.1	9.7	9.1	10.8	9.6

Source: MAPFRE Economics (based on DESTATIS data)
Forecast end date: April 28, 2022

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- The German economy is moving away from recession, but expectations are falling.
- Business confidence has declined significantly in March, which will affect consumption and investment decisions.
- Consumer confidence has also declined, exacerbated by the invasion of Ukraine and the lockdowns at the end of 2021.
- Risks are elevated at the level of energy prices and supply and due to the aggravation of problems in supply chains.

growth estimate for 2022 now stands at 2.0%, down from 3.9% in our previous report (see Table 1.2.4 and Charts 1.2.4-a and 1.2.4-b).

Meanwhile, March inflation stood at 7.3%, and the non-energy index at 3.6%. By categories, (in February) we observed: food (+5.1%), household energy (+20.8%) and fuels (+40%), with an impact on transport in general (+11%) and restaurants and hotels (+5.1%).

The risks of economic disruption are high. Germany is heavily dependent on energy imports from Russia, especially natural gas. In this regard, it has already announced that it will eventually reduce its dependence, but in the short term it is unable to fully replace this source. This poses a major risk, whether it is pressured to enforce sanctions against Russia or whether Russia decides unilaterally to cut off gas supplies. An economy as industrialized as Germany's could go into recession if there is energy rationing to industry. Tension with Russia, instead of decreasing, seems to be increasing. Problems in the supply chain will now tend to worsen, especially certain minerals and metals on which industry relies. Supply problems now also extend to some agricultural products, such as wheat and sunflower oil. The problem lies not only in the supply from the countries in conflict, but other countries, as a precaution or out of economic interest, are reserving their own production of these products.

1.2.5 Italy

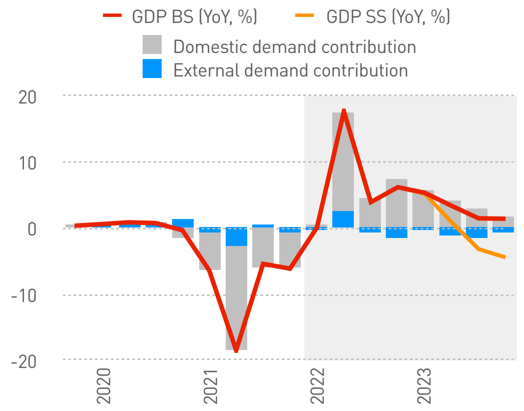
Sharp economic slowdown due to high energy costs.

A sharp slowdown is expected for Italy's economy, which has already begun to be observed in the last two quarters. This is due to the significant rise in energy costs, with gas, electricity and oil prices reaching their highest levels in many years. Electricity is up 82% and gas 64% in one year (February). The producer price index for January is up 41.8% YoY, with the energy category doubling in one year (+118%). With producer prices so high, it is going to be impossible to contain consumer prices for long.

By Q4 2021, Italy was starting to enter a slowdown as energy costs were rising, with a decline compared with the previous two quarters. In the first quarter of 2022 the situation has worsened, so that a contraction in activity is expected compared to the previous quarter (-0.5%), although year-on-year it will remain positive (+5%). In view of the circumstances and without an easy solution for energy costs, a slowdown in activity is to be expected in a country where energy consumption is key for industry.

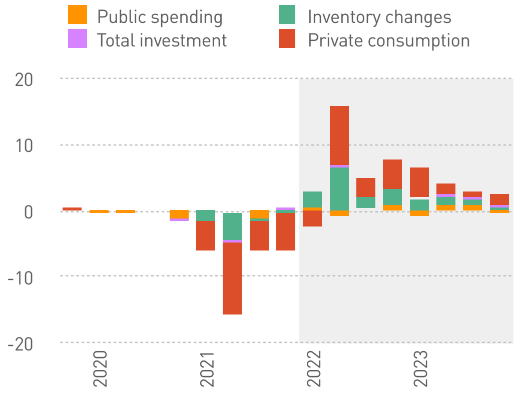
Purchasing managers' indexes (PMIs) worsened in March, with the composite index at 52.1, the manufacturing index at 55.8, and the services index at 52.1 points. Industrial production rose 3.3% YoY (+4.0 MoM) amid persistent supply chain problems. Car sales were 22.6% below the previous year's level (February). Meanwhile, consumer confidence (108) and manufacturing (111) declined slightly in February. In this context, we have lowered the growth outlook for 2022 by 1.5 percentage points to 2.9% from 4.4% previously, and for 2023 by 1.2 percentage points to 2.2% from 2.5% in our previous report (see Table 1.2.5 and Charts 1.2.5-a and 1.2.5-b).

Chart 1.2.5-a
Italy: GDP breakdown and forecasts



Source: MAPFRE Economics (based on ISTAT data)

Chart 1.2.5-b
Italy: domestic demand breakdown and forecasts



Fuente: MAPFRE Economics (con datos de ISTAT)

Table 1.2.5
Italy: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	1.7	0.8	0.5	-9.1	6.6	2.9	2.2	-0.4	-0.5
Domestic demand contribution	1.7	1.1	-0.2	-8.3	6.7	3.7	2.2	0.4	-0.6
External demand contribution	0.0	-0.3	0.7	-0.8	-0.1	-0.9	0.0	-0.9	0.1
Private consumption contribution	0.9	0.6	0.1	-6.3	3.0	2.2	1.9	0.2	0.6
Total investment contribution	0.6	0.5	0.2	-1.7	3.4	1.2	0.5	-0.1	-0.9
Public spending contribution	0.0	0.0	-0.1	0.1	0.2	0.3	0.1	0.3	0.1
Private consumption (% YoY)	1.5	1.0	0.2	-10.6	5.2	3.7	3.2	0.3	1.0
Public spending (% YoY)	-0.1	0.1	-0.5	0.5	1.0	1.6	0.6	1.6	0.6
Total investment (% YoY)	3.4	2.9	1.2	-9.2	17.0	5.7	2.3	-0.5	-4.9
Exports (% YoY)	6.0	1.7	1.8	-14.2	13.4	4.0	4.0	0.7	0.1
Imports (% YoY)	6.5	2.9	-0.5	-12.7	14.6	7.0	4.1	3.6	-0.1
Unemployment rate (%, last quarter)	11.0	10.6	9.8	9.8	9.3	9.4	9.1	10.4	10.5
Inflation (% YoY, last quarter)	0.9	1.1	0.5	-0.2	3.9	6.0	2.0	8.4	3.0
Fiscal balance (% of GDP)	-2.4	-2.2	-1.5	-9.6	-7.2	-5.0	-4.1	-6.4	-6.9
Primary fiscal balance (% of GDP)	1.4	1.4	1.9	-6.1	-3.7	-1.5	-0.7	-2.9	-3.3
Trade balance (% of GDP)	3.1	2.6	3.4	4.1	3.4	0.6	1.3	-0.5	-0.5
Current account balance (% of GDP)	2.6	2.6	3.3	3.7	3.3	1.0	1.1	-0.1	-0.6
Official interest rate (end of period)	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.00
3-month interest rate (end of period)	-0.33	-0.31	-0.38	-0.55	-0.57	-0.42	0.16	-0.24	-0.26
10-year interest rate (end of period)	2.00	2.77	1.43	0.52	1.19	2.64	3.51	3.20	4.48
Exchange rate vs. U.S. dollar (end of period)	1.20	1.15	1.12	1.23	1.13	1.13	1.16	1.11	1.12
Exchange rate vs. euro (end of period)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Private lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Household lending (% YoY, average)	1.2	1.8	2.2	1.2	3.0	4.2	4.7	3.4	2.5
P.S. non-financial lending (% YoY, average)	-3.0	-0.5	-0.7	2.8	0.0	0.9	3.0	-5.5	-4.8
P.S. financial lending (% YoY, average)	-13.2	25.1	-5.8	-10.9	22.1	-1.0	-1.6	-3.2	-2.5
Savings rate (% pers. disp. income, avg.)	9.7	9.6	9.5	17.0	14.0	9.4	8.4	10.3	8.8

Source: MAPFRE Economics (based on ISTAT data)
Forecast end date: April 28, 2022

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On the other hand, inflation in March was 6.7%. Fuels (+37%), electricity (+82%), and transportation services (+12.1%) contributed to this rise. Of particular concern is the rise in producer prices (+41.4% in February), as these increases are expected to be passed on to final products. To mitigate the effects of rising energy costs, Mario Draghi's government has established aid of €3.5 billion for individuals and €3.5 billion for companies. This is possible because at the fiscal level revenues are also performing favorably due to the effect of inflation. Italy is planning to use NGEU funds in 2022 equivalent to 1.1% of GDP in subsidies and 1.2% of GDP in loans. To receive the next tranche of €24 billion, Italy has to meet 45 milestones as presented in its Recovery and Resilience plan.

- **Like the other Eurozone countries, Italy is concerned about inflation, especially in terms of energy.**
- **Producer prices are soaring, and it is only a matter of time before they are passed on to consumers.**
- **For now, the central scenario is only a slowdown, but uncertainty persists; a recession is not yet our central scenario.**
- **As long as EU funds are available and reforms continue, Italy will continue to be supported by European institutions.**
- **Rising bond yields are one aspect to watch.**

At the risk level, now that President Sergio Mattarella has been reelected and Draghi remains as Prime Minister, the political risk in Italy has been substantially reduced. Now the risks are mainly inflation and a downturn in economic activity. A recession is possible, although it is not yet our central scenario. Rising bond yields, together with the approaching end of the ECB's purchase program, may represent an extra charge in interest expenses for the public coffers, which would leave less room for fiscal maneuver. The specter of deteriorating solvency is always there, but as long as Italy continues to make progress with reforms, it will have the support of the ECB and the European Union.

1.2.6 United Kingdom

Bracing for impact:
real incomes suffer with inflation.

Inflation is the most worrying issue at the moment for the UK. After years of monetary expansion and persistently low interest rates, a pandemic that forced demand stimulus policies (while restricting supply during successive lockdowns), a cost overrun when implementing green energy transition policies (increasing their effects on inflation measurement, with an added impact on electricity and oil production capacity), this succession of events would reach its culmination with the invasion of Ukraine. The successive sanctions would lead to the withdrawal of two major producing countries from the raw materials and agricultural market. In addition to all this, there was the recent political process of the United Kingdom's withdrawal from the European Union (Brexit).

These new economic conditions have dealt a severe blow to the economy, especially the domestic economy. Rising prices will cause households to lose purchasing power, negatively impacting the largest component of GDP: private consumption. For 2022, estimates of the impact of these new factors (0.5 percentage points) will be offset, on the one hand, by the expectations of a strong first quarter and, on the other, the savings that consumers were able to accumulate over the months of lockdown. Looking ahead to 2023, when these constraining factors disappear, the scenario will be more adverse, with inflation impacting more forcefully with a greater gap.

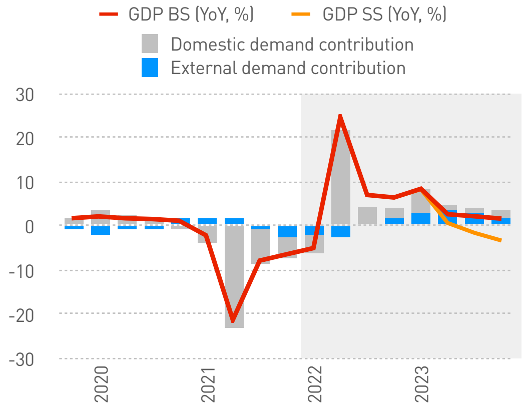
The problems seen in the supply chains, which caused bottlenecks in production, will be lengthened mainly by the pandemic outbreak being experienced in China. In February, retail sales grew positively (+7.0%), but with a base effect (-3.7% in February 2021) mainly motivated by the atypical scenario marked by the pandemic in February 2020. Vehicle registrations have grown by +15% YoY, but still remain below the trend observed in the pre-pandemic scenario. As for consumer confidence (GFK), it continued to worsen in March (-26). Elsewhere, the purchasing managers' indexes (PMIs) for April worsened with the composite at 57.6, manufacturing at 55.3 and services at 58.3 points. Against this backdrop, we have lowered our growth estimate for 2022 by 0.7 percentage points from 4.4% to 3.7%, and by 1.2 percentage points for 2023, from 2.8% to 1.6%. The economic slowdown will be felt mainly in private consumption (-0.7 pp, to +4.7%) and exports (-2.7 pp to +5.3%) due to the greater impact of the slowdown in the external sector (see Table 1.2.6 and Charts 1.2.6-a and 1.2.6-b).

- Headline inflation in March came in at 7.0%, with core at 5.7% and is expected to continue rising for at least two more months.
- A slowdown in private consumption seems to be inevitable.
- High energy prices have no quick fix as long as the conflict in Ukraine persists.
- The Bank of England raised interest rates by 25 bps to 0.75% and will continue to raise rates in May.

Meanwhile, inflation soared to 7.0% for March, with an upward trend also for core inflation, reaching 5.7%, accentuated mainly by the rise in energy (+23.1%) and vehicles (mainly second-hand) (+30.6%), but also food (+5.1%), clothing (+8.9%) and hotels and restaurants (+5.0%). The Bank of England, at its meeting in March, raised interest rates by 25 bps to 0.75%. Based on the assessment of the economic situation, the committee felt that a further modest tightening of monetary policy might be appropriate in the coming months, but there are two-way risks to this view, and the decision will be made depending on the evolution of the medium-term inflation outlook. The outlook for inflation was already high before the Ukraine invasion and has now worsened.

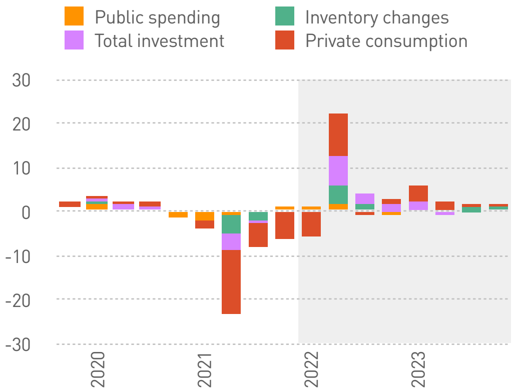
The risks to the UK economy have clearly worsened, especially as there may be a slowdown in private consumption. It all depends on the performance of wages and whether households are willing to make use of their accumulated savings. In the event that they choose to reduce their consumption, we could be approaching recession. If energy prices do not stop rising, inflation could continue to rise for a couple of months or even longer, which would mean that the effect of inflation will have already been transmitted to all products. The Bank of England should continue to raise interest rates, but these should be implemented gradually, as a precipitous rise could make the situation even worse. There are still expectations of a reduction in energy and commodity prices, but this outcome will depend on what happens with the war.

Chart 1.2.6-a
United Kingdom: GDP breakdown and forecasts



Source: MAPFRE Economics (based on data from the Office for National Statistics)

Chart 1.2.6-b
United Kingdom: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on data from the Office for National Statistics)

Table 1.2.6
United Kingdom: main macroeconomic aggregates

	2017	2018	2019	2020	2021(e)	Baseline (BS)		Stressed (SS)	
						2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	2.1	1.7	1.7	-9.4	7.5	3.7	1.6	0.9	-1.0
Domestic demand contribution	1.9	0.9	1.9	-9.8	8.2	4.7	0.8	1.7	-2.3
External demand contribution	0.3	0.8	-0.2	0.4	-0.7	-1.1	0.9	-0.8	1.3
Private consumption contribution	1.0	1.3	0.8	-6.4	3.7	2.8	0.3	0.8	-1.5
Total investment contribution	0.6	0.0	0.1	-1.7	0.9	1.2	0.6	0.3	-0.5
Public spending contribution	0.1	0.1	0.8	-1.1	3.0	0.3	0.3	0.3	0.3
Private consumption (% YoY)	1.6	2.1	1.2	-10.5	6.1	4.6	0.6	1.3	-2.5
Public spending (% YoY)	0.6	0.4	4.2	-5.4	14.5	1.4	1.2	1.4	1.2
Total investment (% YoY)	3.3	-0.1	0.5	-9.4	5.3	6.7	3.5	1.8	-2.7
Exports (% YoY)	5.7	2.8	3.4	-13.9	-1.1	5.3	5.8	3.8	4.5
Imports (% YoY)	2.9	3.1	2.9	-15.9	3.0	8.5	2.3	6.1	-0.7
Unemployment rate (%, last quarter)	4.4	4.0	3.8	5.2	4.1	3.8	3.8	4.6	5.6
Inflation (% YoY, last quarter)	2.7	2.0	1.3	0.8	4.8	6.8	3.3	9.5	4.5
Fiscal balance (% of GDP)	-2.4	-2.2	-2.3	-13.0	-8.8	-5.0	-2.7	-5.6	-4.8
Primary fiscal balance (% of GDP)	0.4	0.4	0.0	-11.0	-6.1	-0.1	0.6	-0.6	-1.3
Trade balance (% of GDP)	-6.7	-6.5	-6.1	-6.1	-6.7	-7.8	-6.7	-8.6	-7.6
Current account balance (% of GDP)	-3.6	-3.9	-2.7	-2.7	-2.9	-4.6	-3.3	-5.2	-3.9
Official interest rate (end of period)	0.50	0.75	0.75	0.10	0.25	1.00	1.25	0.87	1.38
3-month interest rate (end of period)	0.52	0.91	0.79	0.03	0.26	1.33	1.70	1.17	1.71
10-year interest rate (end of period)	1.19	1.27	0.83	0.20	0.97	2.00	2.55	2.37	3.33
Exchange rate vs. U.S. dollar (end of period)	1.35	1.28	1.32	1.36	1.35	1.35	1.39	1.34	1.39
Exchange rate vs. euro (end of period)	1.13	1.11	1.18	1.11	1.19	1.19	1.19	1.19	1.20
Private lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Household lending (% YoY, average)	4.0	3.1	2.1	2.9	3.5	4.7	6.3	4.6	5.5
P.S. non-financial lending (% YoY, average)	9.4	2.7	1.6	5.6	-1.3	1.5	2.1	1.4	1.5
P.S. financial lending (% YoY, average)	8.5	5.5	2.2	9.0	-5.6	6.1	4.6	6.3	5.1
Savings rate (% pers. disp. income, avg.)	4.8	4.8	4.6	13.8	11.0	5.8	7.1	6.7	7.7

Source: MAPFRE Economics (based on data from the Office for National Statistics)
Forecast end date: April 28, 2022

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1.2.7 Japan

The economy will grow less due to rising raw material costs.

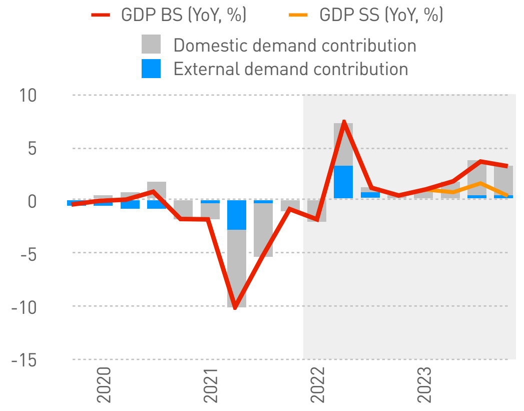
The global slowdown naturally affects the Japanese economy due to its island status, especially because of the rising prices of raw materials, metals, and energy. Purchasing managers' indexes (PMIs) remained weak in March, with the composite at 50.9, manufacturing at 53.4 and services at 50.5 points. Several indexes and surveys based on expectations decreased, as seen in those reflecting consumer confidence (35), the Leading Indicators CI (103.6), and the survey of observers of the economy (Outlook:43). Car sales are down 18% compared to February of the previous year, and vehicle production has fallen 5%. Industrial production grew 0.2% in February. On the other hand, retail sales decreased 0.4% in the month (+6.0% in February year-on-year). Meanwhile, the tertiary sector continues to expect a recovery led by a strong rebound in domestic demand once the isolation measures are lifted (March 21). In this regard, the government is expected to continue easing the distancing restrictions over the coming months. Investment is also expected to grow (+2.1%) after two years of consecutive declines. The Japanese economy is thus expected to grow by 2.8% in 2022 (8/10 less than forecast in our previous report), with domestic consumption moderating (+2.3%) and exports being the main driver of this growth (+6.4%), especially due to trade with other Asian countries (see Table 1.2.7 and Charts 1.2.7-a and 1.2.7-b).

Additionally, inflation was around 1.2% in March, with core inflation at around -0.7%. It should be noted that, for the time being, inflation has been mainly confined to producer prices (+9.3%). Contributing to this effect is the slowdown in wages, which are growing at around 0.9%, causing producers to eventually have to pass on the increase in their costs. As for the main components of the consumer basket, fuels rose by 33%, electricity by 20%, gas by 16.5% and food by 2.8%. The Bank of Japan decided at its December meeting to maintain negative interest rates at -0.10% and to continue with quantitative and qualitative monetary easing (QQE) with yield curve control in order to achieve its 2% price stability target and maintain this target in a stable manner. On the other hand, the monetary base will continue to be expanded until the year-on-year rate of increase in the observed CPI (all items except fresh food) exceeds 2% and is able to remain above the target in a stable manner.

- **Economic growth in 2022 is forecast at 2.4%, down eight-tenths of a percentage point from our previous report.**
- **The outlook on the industrial sector is now less positive due to the rising cost of raw materials, energy, and prolonged supply chain problems.**
- **Auto sales are lower than in 2021 (-18%), along with production (-5%).**
- **Likewise, consumer sentiment is decreasing.**

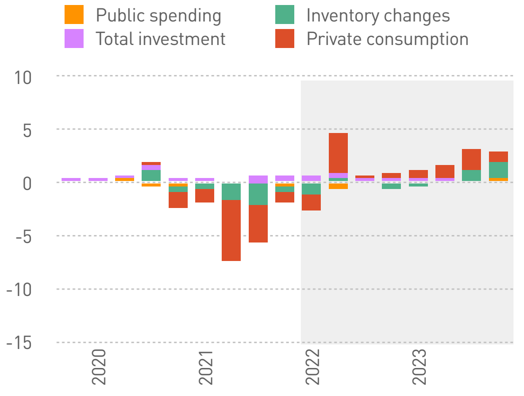
The main risk for the Japanese economy comes from a possible slowdown in exports resulting from the deterioration of external conditions and a slump in domestic consumption due to a decrease in the purchasing power of wages. Even if consumer inflation is low, higher producer inflation could lead to higher inflation later on. The Bank of Japan will seek to bring inflation closer to 2%. Thus, measures to tighten international and domestic financial conditions could put additional weight on investment.

Chart 1.2.7-a
Japan: GDP breakdown and forecasts



Source: MAPFRE Economics (based on Statistics Bureau data)

Chart 1.2.7-b
Japan: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on Statistics Bureau data)

Table 1.2.7
Japan: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021 (e)	2022 (f)	2023 (f)	2022 (f)	2023 (f)
GDP (% YoY)	1.7	0.6	-0.2	-4.5	1.7	2.4	2.0	0.9	1.4
Domestic demand contribution	1.2	0.5	0.2	-3.8	0.7	2.1	1.8	0.6	1.3
External demand contribution	0.5	0.0	-0.5	-0.8	1.0	0.3	0.2	0.3	0.1
Private consumption contribution	0.6	0.1	-0.3	-2.8	0.7	1.2	0.7	0.3	0.5
Total investment contribution	0.4	0.1	0.2	-1.2	-0.3	0.5	1.2	0.1	0.7
Public spending contribution	0.0	0.2	0.4	0.5	0.5	0.2	-0.1	0.2	-0.1
Private consumption (% YoY)	1.1	0.2	-0.5	-5.2	1.3	2.1	1.2	0.5	0.9
Public spending (% YoY)	0.1	1.0	1.9	2.3	2.1	0.9	-0.4	0.9	-0.4
Total investment (% YoY)	1.7	0.3	1.0	-4.7	-1.4	2.1	3.0	0.3	3.0
Exports (% YoY)	6.6	3.8	-1.4	-11.9	11.8	5.9	4.7	4.1	3.0
Imports (% YoY)	3.3	3.8	1.1	-7.2	5.2	4.3	3.9	2.5	2.8
Unemployment rate (%, last quarter)	2.7	2.4	2.3	3.0	2.7	2.6	2.4	2.8	2.7
Inflation (% YoY, last quarter)	0.6	0.9	0.5	-0.9	0.5	2.0	0.9	3.0	1.1
Fiscal balance (% of GDP)	-3.1	-2.5	-2.9	-9.5	-8.5	-6.6	-4.8	-7.1	-5.9
Primary fiscal balance (% of GDP)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Trade balance (% of GDP)	0.9	0.2	0.0	0.6	0.3	-1.0	-0.1	-1.1	-0.4
Current account balance (% of GDP)	4.2	3.5	3.4	2.9	2.9	1.8	2.9	1.6	2.6
Official interest rate (end of period)	-0.06	-0.06	-0.07	-0.03	-0.02	-0.05	-0.09	0.00	0.07
3-month interest rate (end of period)	0.07	0.07	0.07	0.08	0.07	0.07	0.03	0.12	0.19
10-year interest rate (end of period)	0.05	0.01	-0.02	0.04	0.09	0.24	0.30	0.35	0.44
Exchange rate vs. U.S. dollar (end of period)	112.90	110.83	109.12	103.54	115.00	113.96	109.91	115.05	110.59
Exchange rate vs. euro (end of period)	135.40	126.90	122.59	127.05	130.25	128.87	128.03	130.19	128.48
Private lending (% YoY, average)	4.2	2.5	1.7	5.3	2.9	1.6	0.9	1.2	0.0
Household lending (% YoY, average)	2.2	2.5	2.3	2.4	2.2	0.8	0.7	0.6	0.3
P.S. non-financial lending (% YoY, average)	2.4	2.3	3.4	8.1	3.6	-0.7	-1.0	-0.8	-1.1
P.S. financial lending (% YoY, average)	8.0	6.3	2.9	17.0	7.1	-5.0	-6.0	-5.0	-6.0
Savings rate (% pers. disp. income, avg.)	1.6	1.7	2.7	10.6	6.7	3.0	2.4	3.7	2.1

Source: MAPFRE Economics (based on Statistics Bureau data)
Forecast end date: April 28, 2022

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1.2.8 Turkey

Soaring inflation and negative real interest rates weigh on the currency.

The conflict in Ukraine is adding to the difficulties for the Turkish economy. Rising commodity costs are putting further pressure on inflation, in turn impacting the Turkish lira. Inflation reached 61.1% in March, and the lira has again lost value since the Russian invasion. The government continues to focus on strengthening exports, production, and employment. However, the rising cost of raw materials will cause the current account deficit to widen in the coming months. Turkey imports 35% of its gas from Russia. Although Turkey has condemned the invasion of Ukraine, its willingness to act is limited by its intense economic relationship with Russia.

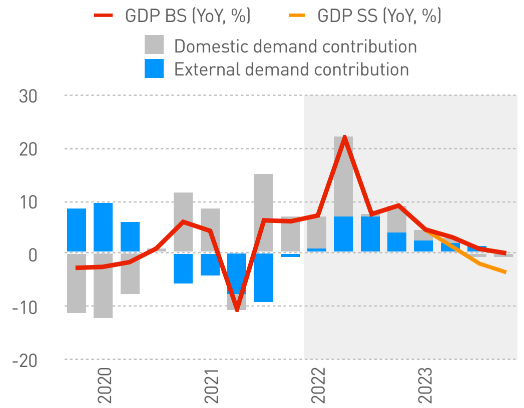
In 2022, 8.5 million tourists were expected from the two warring countries; now, this number will be substantially lower. The Turkish government hopes to be able to compensate for its reduced trade relations with Russia and Ukraine with increased economic relations with Middle Eastern countries, which have relatively high purchasing power. Thus, the government is now focused on dealing with the effects of the conflict and fighting inflation. Its goal is to get inflation levels back below 10% before the June 2023 elections, provided that commodity prices moderate again. In addition, the creation of guaranteed lira deposits is expected to contribute to exchange rate stability.

The manufacturing purchasing managers' index (PMI) declined 1 point to 49.4 in March, and the economic sentiment survey worsened to 98.2. The survey of expected retail sales for the next three months improved (+7.0% YoY). Thus, in 2022, GDP is expected to grow by 2.0%, down 8/10 from our previous estimate. Investment will be the main loser due to uncertainties regarding the stability of the currency and the economy's high exposure to external debt in dollars. Exports should perform better (+10%), boosted by the currency depreciation, while private consumption (+5%) will be the other catalyst (see Table 1.2.8 and Charts 1.2.8-a and 1.2.8-b).

- **Inflation accelerated in March to 61.1% and took hold as core inflation also rose to 48%.**
- **The central bank held interest rates at the last three meetings at 14.0%, implying negative real rates (-47%).**
- **The Turkish lira lost -10% in Q1 2022 (to 14.7 TRY/USD).**
- **The commitment to low interest rates and depreciated currency represents a strategy of decoupling from other economies, but it involves a high level of risk.**

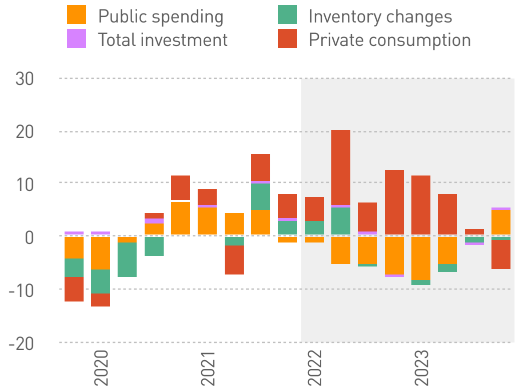
Inflation, meanwhile, reached 61.1% YoY in March, with core inflation at 48.4%, and it may soar even higher due to currency depreciation before starting to ease, at which point commodities will start to moderate. By components (in February), inflation is high in every aggregate, with food (64.4%), housing (+23.8%), electricity (49.7%), transport (75.7%), and accommodation and restaurants (55.2%) standing out in particular. The Turkish Central Bank has kept interest rates (1-week Repo) stable at 14.00% at its last three meetings. However, real interest rates are in strongly negative parameters (-47%). The central bank expects that, with this strategy, and with the lira deposit guarantee mechanism, the economy will manage to intensify the use of the lira, hoping to maintain this strategy until indicators point to a permanent decline in inflation and the 5% target is reached in the medium term. According to the monetary policy committee's statement, "the stability of the general price level will promote macroeconomic stability and financial stability through the fall in the country's risk premium, reversing the trend towards the use of the dollar, the increase in foreign exchange reserves, and the lasting decrease in

Chart 1.2.8-a
Turkey: GDP breakdown and forecasts



Source: MAPFRE Economics (based on TURKSTAT data)

Chart 1.2.8-b
Turkey: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on TURKSTAT data)

Table 1.2.8
Turkey: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	7.5	3.0	0.9	1.8	11.0	2.0	2.5	-0.2	0.4
Domestic demand contribution	7.2	-0.6	-1.4	7.5	5.9	0.5	2.1	-1.6	-0.2
External demand contribution	0.3	3.5	2.3	-5.7	5.1	1.5	0.4	1.5	0.6
Private consumption contribution	3.5	0.3	0.9	1.9	9.3	3.2	-0.9	1.6	-2.2
Total investment contribution	2.4	-0.1	-3.1	1.9	1.6	-1.1	0.3	-1.7	-0.7
Public spending contribution	0.7	0.9	0.6	0.3	0.3	0.2	0.3	0.2	0.3
Private consumption (% YoY)	5.9	0.6	1.5	3.2	15.1	5.0	-1.5	2.6	-3.6
Public spending (% YoY)	5.0	6.5	4.1	2.2	2.1	1.1	2.0	1.1	2.0
Total investment (% YoY)	8.3	-0.2	-12.4	7.2	6.4	-4.7	1.5	-7.2	-2.9
Exports (% YoY)	12.4	8.8	4.6	-14.8	24.9	10.7	3.8	8.4	1.4
Imports (% YoY)	10.6	-6.2	-5.4	7.6	2.0	5.1	2.8	2.7	-1.3
Unemployment rate (%, last quarter)	10.3	12.3	13.3	12.9	11.0	11.5	10.6	12.1	11.6
Inflation (% YoY, last quarter)	11.9	20.3	11.8	14.6	36.1	52.9	16.2	59.7	17.4
Fiscal balance (% of GDP)	-1.6	-1.9	-2.9	-3.5	-2.7	-1.9	-1.5	-1.8	-1.6
Primary fiscal balance (% of GDP)	0.2	0.0	-0.6	-0.8	-0.2	0.5	0.7	0.6	0.6
Trade balance (% of GDP)	-6.8	-5.2	-2.2	-5.3	-3.6	-5.7	-4.9	-7.5	-7.3
Current account balance (% of GDP)	-4.8	-2.8	0.7	-5.0	-1.8	-3.8	-2.5	-5.4	-4.6
Official interest rate (end of period)	12.75	24.06	11.43	17.03	14.00	14.00	14.25	14.49	12.87
3-month interest rate (end of period)	14.61	24.07	10.76	17.53	15.63	15.39	13.68	15.44	12.51
10-year interest rate (end of period)	11.72	16.53	11.95	12.51	22.99	22.07	17.09	22.62	17.30
Exchange rate vs. U.S. dollar (end of period)	3.79	5.29	5.95	7.44	13.32	14.90	15.45	15.68	15.66
Exchange rate vs. euro (end of period)	4.55	6.06	6.68	9.11	15.23	16.85	17.99	17.75	18.19
Private lending (% YoY, average)	20.9	20.2	8.4	30.1	23.9	28.8	13.2	28.9	12.1
Household lending (% YoY, average)	17.5	9.8	3.3	41.8	20.3	6.1	10.8	5.9	10.6
P.S. non-financial lending (% YoY, average)	21.8	18.2	5.5	29.0	23.2	14.6	15.8	12.3	10.4
P.S. financial lending (% YoY, average)	27.2	25.1	18.3	21.2	30.9	59.8	20.4	57.3	18.4
Savings rate (% pers. disp. income, avg.)	32.3	32.0	30.4	21.0	23.0	15.5	11.9	15.1	9.7

Source: MAPFRE Economics (based on TURKSTAT data)
Forecast end date: April 28, 2022

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financing costs. This would create a viable basis for investment, production and employment to continue to grow in a healthy and sustainable manner."

Risks to the Turkish economy increased again with the Ukrainian conflict. Rising commodity costs will add further pressure on inflation. The real interest rates (strongly negative) do not help the currency or, subsequently, foreign investment. The strategy is unorthodox and seems to be to try to decouple financially from the external sector, following a kind of "autarky"; a high-risk strategy with a logic that dates from a time when economies were not so interconnected. The strategy may stimulate domestic activity, but everything that is imported will become inaccessible. The risk of default on dollar debt increases, except for companies with natural hedging (those that export in dollars).

1.2.9 Mexico

Inflation adds difficulties to growth.

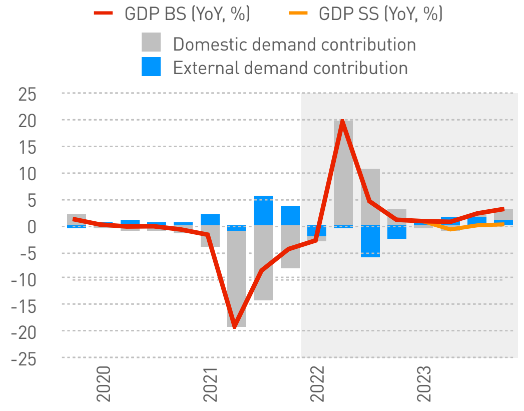
The conflict in Ukraine (which has added to the supply shocks caused by the pandemic) will impact Mexico through various channels, such as higher prices for fertilizers (ammonium nitrate), gas, oil, plastics and some essential metals in vehicle manufacturing. As for gas, the government has decided to apply measures to cap its price, but these are not sufficient to prevent its rise from being transmitted to other products. As for oil, although Mexico is a producer, its total balance of oil products is negative (since it imports refined products). Thus, the inflationary context and the difficulties in the supply of some essential raw materials will reduce the potential growth for this year.

In terms of activity indicators, the manufacturing PMI for March came in at 49.2, up from 48.0 in February. However, confidence in industry decreased slightly to 52.2 in March. While industrial production performed well (+4.2% YoY), automobile manufacturing is still 20% below pre-pandemic levels, as are levels of gross fixed investment in the economy. In this context, we lowered our GDP estimate by one percentage point for 2022 to 1.6% due to the decrease in consumption and investment (1.8% and 3.1%, respectively), while exports are expected to improve (+8.5%), provided that supply chain problems do not recur (see Table 1.2.9 and Charts 1.2.9-a and 1.2.9-b).

In addition, inflation for March stood at 7.45%, with core inflation at 6.78%. The rise in prices is particularly driven by the upward growth in agricultural products (16.2%) and beef (16.8%), while electricity and gas have grown to a lesser extent. Energy, in general, has moderated due to the government's price controls, which caused it to increase by only 4.7% overall. The Bank of Mexico, at its March meeting, approved an increase in official rates by another 50 bps to 6.50% and is expected to continue raising rates in 2022. The central bank considers this path for interest rates necessary to converge inflation to the 3% target for 2023. In this regard, we expect subsequent rate hikes to be above inflation, and could go even higher if inflation fails to stabilize, or if the Fed's interest rate hikes need to be paced to avoid significant exchange rate effects.

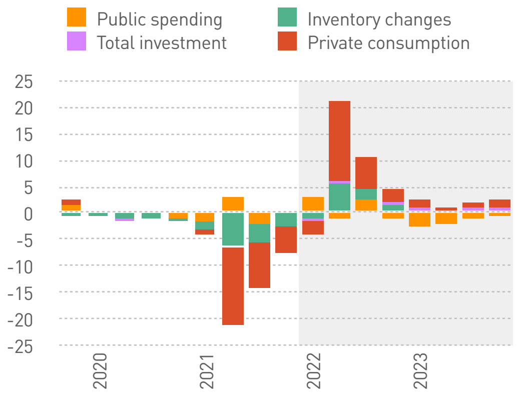
- **Expected growth for 2022 has decreased by one percentage point to 1.6%.**
- **Rising commodity prices will put pressure on agricultural and industrial product prices.**
- **Inflation reached 7.45% in March, with core inflation also high at 6.78%.**
- **Interest rates are rising, but lagging behind inflation.**

Chart 1.2.9-a
Mexico: GDP breakdown and forecasts



Source: MAPFRE Economics (based on INEGI data)

Chart 1.2.9-b
Mexico: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on INEGI data)

Table 1.2.9
Mexico: main macroeconomic aggregates

	2017	2018	2019	2020	2021(e)	Baseline (BS)		Stressed (SS)	
						2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	2.3	2.2	-0.2	-8.4	5.0	1.6	1.9	0.1	1.4
Domestic demand contribution	3.3	2.4	-1.0	-10.6	7.8	0.3	1.7	-1.5	1.2
External demand contribution	-0.9	-0.2	0.8	2.3	-2.8	1.3	0.2	1.6	0.2
Private consumption contribution	2.3	1.7	0.2	-7.0	4.9	0.5	1.5	-0.2	1.3
Total investment contribution	-0.2	0.2	-0.9	-3.1	1.9	0.6	0.4	0.1	0.1
Public spending contribution	0.1	0.3	-0.2	0.0	0.2	0.3	0.3	0.3	0.2
Private consumption (% YoY)	3.4	2.6	0.4	-10.7	7.3	1.8	2.9	-0.2	2.2
Public spending (% YoY)	0.7	2.9	-1.8	0.1	1.4	2.1	2.3	2.1	2.3
Total investment (% YoY)	-1.1	0.8	-4.7	-17.9	10.6	3.1	2.4	0.6	1.0
Exports (% YoY)	4.1	5.9	1.5	-7.2	6.4	8.0	4.9	6.2	3.1
Imports (% YoY)	6.8	6.4	-0.7	-14.2	14.4	5.2	4.1	2.0	2.2
Unemployment rate (%, last quarter)	3.3	3.3	3.4	4.6	3.7	3.9	3.9	4.3	4.6
Inflation (% YoY, last quarter)	6.8	4.8	2.8	3.2	7.4	6.5	4.4	6.8	5.0
Fiscal balance (% of GDP)	-1.1	-2.0	-1.7	-2.8	-3.0	-2.9	-2.5	-3.3	-2.9
Primary fiscal balance (% of GDP)	1.4	0.6	1.1	0.1	-0.3	-0.4	0.1	-0.6	-0.3
Trade balance (% of GDP)	-0.9	-1.1	0.4	3.1	-0.9	-0.7	-0.6	-0.8	-0.7
Current account balance (% of GDP)	-1.7	-2.0	-0.3	2.4	-0.4	-0.4	-0.3	-0.6	-0.5
Official interest rate (end of period)	7.25	8.25	7.25	4.25	5.50	8.00	8.00	8.05	7.75
3-month interest rate (end of period)	7.66	8.63	7.45	4.47	5.86	8.25	8.28	8.30	8.00
10-year interest rate (end of period)	7.66	8.70	6.84	5.23	7.57	8.90	8.42	9.32	8.72
Exchange rate vs. U.S. dollar (end of period)	19.67	19.65	18.93	19.88	20.50	21.29	21.73	21.94	21.98
Exchange rate vs. euro (end of period)	23.59	22.50	21.26	24.40	23.22	24.08	25.31	24.83	25.54
Private lending (% YoY, average)	12.1	10.4	8.9	5.2	0.0	7.6	7.7	6.3	7.8
Household lending (% YoY, average)	9.9	8.4	6.2	1.6	4.4	6.4	6.0	6.2	5.4
P.S. non-financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. financial lending (% YoY, average)	1.7	-0.8	6.2	3.7	18.7	14.0	11.8	12.7	12.1
Savings rate (% pers. disp. income, avg.)	10.7	12.3	16.4	22.2	23.4	20.5	18.7	21.0	18.6

Source: MAPFRE Economics (based on INEGI data)
Forecast end date: April 28, 2022

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The risks to the Mexican economy are now focused on rising commodity and energy prices, the supply of agricultural (fertilizers) and industrial (metals, plastics) products, and their impact on inflation. Supply chain difficulties could be revived by the disruption caused by surging energy costs. Rising interest rates, although below inflation for now, are already tightening financial conditions, and this could also have an impact on potential growth, which is already affected by weak consumption and, in particular, private investment.

1.2.10 Brazil

Inflation and rising interest rates moderate economic growth.

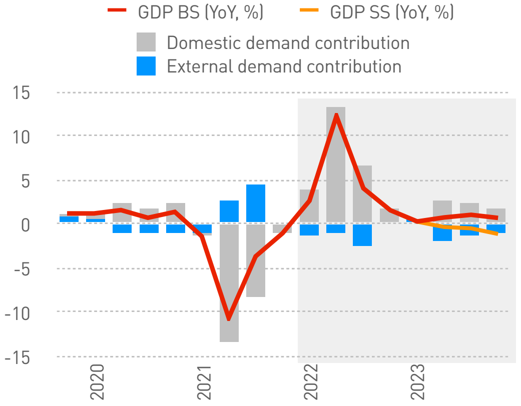
The Brazilian economy will suffer a significant slowdown in 2022 to +0.7% YoY from +5.0% in 2021. Both private consumption (+2.6%) and investment (-4.1%) will experience decelerations. The performance of exports (+1.0%) is generating the most doubts, because while commodity prices are soaring, the shortage and problems affecting fertilizers in the international market could affect agricultural exports. Private consumption is trending downward due to inflation and problems in global supply chains, mainly impacting automobile production. Vehicle registrations have fallen 23% (February) and are at half of 2019 levels.

Purchasing managers' indexes (PMIs) improved in February, although the manufacturing index showed negative values (49.6), the composite stood at 53.5 and the services index at 54.7 points. The Brazilian stock market is up 11% for the year (38% in euros), mainly thanks to the mining company Vale, the oil company Petrobras, and the banks. In this context, we have marginally raised our forecast for Brazilian GDP growth by two-tenths to 0.7% for 2022 (see Table 1.2.10 and Charts 1.2.10-a and 1.2.10-b). Although growth remains limited, influenced by the tailwind for commodity prices, the overall context remains negative, with high energy costs and inflation, which have not yet stabilized and will reduce household electricity consumption.

Inflation, meanwhile, stood at 11.3% (general HICP) in March, with energy prices up 29% YoY, electricity +29%, gas cylinders +30%, automotive fuels +28%, and transport in general +17%. The central bank (BCB) decided at its March 16 meeting to approve the increase of SELIC interest rates by 100 bps to 11.75%, considering it necessary to combat the secondary impacts of the current commodity price shock, which are being reflected with a certain lag in other prices. The central bank has an inflation forecast of 7.1% for 2022 and 3.4% for 2023. According to COPOM's statement, in this scenario interest rates would rise to 12.75% in 2022 and then fall to 8.75% by the end of 2023. The committee understands that this decision reflects the uncertainty sur-

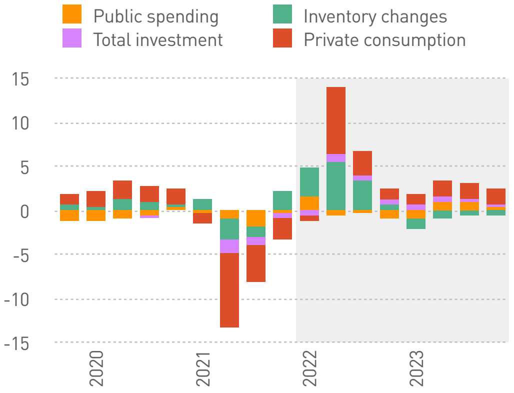
- **Inflation reached 11.3% in March, with pressure on food, energy, and transportation.**
- **The central bank raised interest rates to 11.75% and another 100 bps hike is expected at the next meeting.**
- **Industrial activity, particularly in the automotive industry, is still affected by the parts shortage and high energy prices.**
- **The stock market is up 11% so far this year (+38% in euros).**
- **Presidential elections are in October, with Lula da Silva leading the polls.**

Chart 1.2.10-a
Brazil: GDP breakdown and forecasts



Source: MAPFRE Economics (based on data from the Brazilian Institute of Geography and Statistics (IBGE))

Chart 1.2.10-b
Brazil: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on data from the Brazilian Institute of Geography and Statistics (IBGE))

Table 1.2.10
Brazil: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021 (e)	2022 (f)	2023 (f)	2022 (f)	2023 (f)
GDP (% YoY)	1.6	1.7	1.2	-4.2	5.0	0.7	1.2	-0.4	0.9
Domestic demand contribution	2.0	2.4	1.8	-5.6	6.3	1.7	1.5	0.4	1.2
External demand contribution	-0.4	-0.7	-0.6	1.4	-1.3	-1.0	-0.3	-0.9	-0.3
Private consumption contribution	1.5	1.7	1.8	-4.0	2.7	1.8	1.8	0.9	1.6
Total investment contribution	-0.4	0.9	0.7	-0.1	3.5	-0.8	0.1	-1.1	-0.1
Public spending contribution	-0.1	0.1	-0.1	-0.8	0.3	0.4	0.1	0.4	0.1
Private consumption (% YoY)	2.2	2.4	2.6	-5.7	3.9	2.6	2.6	1.3	2.3
Public spending (% YoY)	-0.7	0.8	-0.5	-4.5	2.0	2.4	0.4	2.4	0.4
Total investment (% YoY)	-2.6	5.2	4.0	-0.5	17.3	-4.1	0.5	-5.8	-0.3
Exports (% YoY)	5.2	3.4	-2.5	-2.2	6.3	1.0	5.1	-0.3	3.8
Imports (% YoY)	7.2	7.2	1.4	-10.2	12.9	6.3	5.6	4.5	4.5
Unemployment rate (%, last quarter)	11.9	11.7	11.1	14.2	11.1	11.1	10.5	11.6	11.6
Inflation (% YoY, last quarter)	2.9	3.7	4.3	4.5	10.1	7.6	4.5	8.2	4.9
Fiscal balance (% of GDP)	-7.8	-7.0	-5.8	-13.6	-4.4	-8.8	-7.7	-9.1	-8.4
Primary fiscal balance (% of GDP)	-1.7	-1.5	-0.8	-9.4	0.7	-1.0	-0.8	-1.2	-1.5
Trade balance (% of GDP)	2.8	2.3	1.4	2.2	2.3	1.7	1.7	2.0	2.1
Current account balance (% of GDP)	-1.1	-2.7	-3.5	-1.7	-1.7	-2.6	-2.9	-2.4	-2.7
Official interest rate (end of period)	7.00	6.50	4.50	2.00	9.25	13.50	9.50	13.94	10.37
3-month interest rate (end of period)	6.90	6.40	4.40	1.90	9.15	13.35	9.52	13.84	10.27
10-year interest rate (end of period)	10.21	9.24	6.81	6.98	10.31	12.53	12.10	13.59	13.00
Exchange rate vs. U.S. dollar (end of period)	3.31	3.87	4.03	5.20	5.58	5.55	5.69	5.70	5.70
Exchange rate vs. euro (end of period)	3.97	4.44	4.53	6.38	6.32	6.27	6.62	6.45	6.63
Private lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Household lending (% YoY, average)	4.7	7.0	10.8	10.1	17.7	13.0	9.4	12.9	9.0
P.S. non-financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Savings rate (% pers. disp. income, avg.)	17.4	16.4	15.8	19.0	22.3	19.0	18.5	19.5	18.1

Source: MAPFRE Economics (based on data from the Brazilian Institute of Geography and Statistics (IBGE))
Forecast end date: April 28, 2022

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rounding its scenarios, and it makes a balance of risks with an even larger variance for prospective inflation than usual. Without prejudice to its fundamental objective of ensuring price stability, this decision also implies smoothing fluctuations in the level of economic activity and promoting full employment. The central bank also believes that, in view of its projections and the risk of a de-anchoring of longer-term expectations, it is appropriate for the monetary tightening cycle to move significantly further into even more contractionary territory. Thus, for the next meeting, the committee expects another tightening of the same magnitude.

Currently the most important risk for the Brazilian economy is inflation and that expectations will be anchored at higher levels. Hence the central bank's swift reaction in raising interest rates. This has been positive for investment and for the currency, which has strengthened in the last three months to BRL 5.1/USD. The cost of inflation and higher interest rates means a slowdown in the economy. Some structural reforms (public administration, tax and privatizations) are still expected, but there is little hope that these can move forward at this time. In October there are presidential elections, and the surveys point to a return of Lula da Silva, who is ahead in the polls.

1.2.11 Argentina

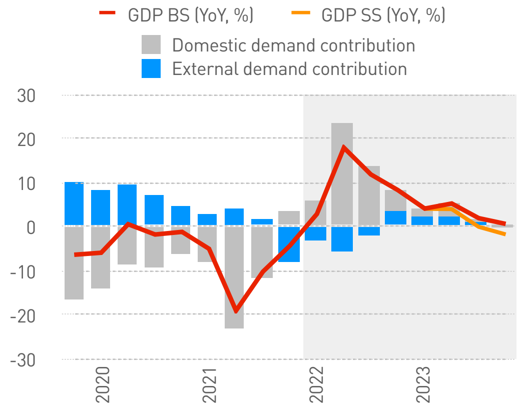
The need to moderate inflation, stabilize the exchange rate and move ahead with structural reforms.

At the end of March, the IMF approved a new US$44 billion aid package for Argentina's economy. It is a 30-month program with an immediate disbursement of US$9.6 billion. The program sets out pragmatic and realistic objectives, along with credible policies to strengthen stability and begin to address the economy's deep-seated problems. The program also seeks to improve public finances and begin to reduce the high and persistent inflation through a multi-pronged strategy, including an end to monetary financing of the fiscal deficit and improvements in the monetary and exchange rate policy framework. A strong political and social consensus will be necessary to implement the reform agenda, which is essential to address long-term structural problems. In this regard, growth-compatible fiscal consolidation (e.g., spending cuts), positive real interest rates and a competitive exchange rate will be required to attract demand for pesos and improve reserve coverage. These conditions should eventually relax existing exchange controls.

At the outlook level, after the recovery observed in 2021, in 2022 the Argentine economy will return to more moderate growth levels, especially with the international context of high energy prices and a domestic inflationary context. The leading indicator (from TDT University) rose to 134 (+6.3%), but consumer confidence declined to 36.9 and showed a decreasing trend over the last 3 years. Thus, we expect growth of 3.0% in 2022 and 0.8% in 2023 (see Table 1.2.11 and Charts 1.2.11-a and 1.2.11-b).

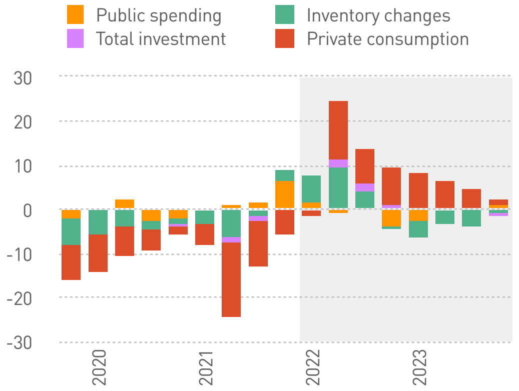
Meanwhile, inflation in March stood at 55.1% YoY, having accelerated again with respect to February (52.3%); on a monthly basis, this means 6.7% MoM. By items and on a monthly basis: food (7.2%), transport (5.5%), hotels and restaurants (5.4%), clothing (10.9%), electricity and gas (7.7%) due to regulated prices. The underlying rate was 57.3% year-on-year (6.4% month-on-month). The global supply shock led to price increases in all raw materials and other key products in the production chain. Wheat, corn, and soybeans, but also oil, gas and fertilizers are some of the examples of increases in raw material and input prices that directly and indirectly affect prices in Argentina.

Chart 1.2.11-a
Argentina: GDP breakdown and forecasts



Source: MAPFRE Economics (based on INDEC data)

Chart 1.2.11-b
Argentina: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on INDEC data)

Table 1.2.11
Argentina: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	2.8	-2.6	-2.0	-9.9	10.2	3.0	0.8	1.6	0.0
Domestic demand contribution	6.6	-4.0	-8.8	-10.2	12.1	1.6	0.9	0.0	0.0
External demand contribution	-3.8	1.4	6.8	0.3	-2.0	1.5	-0.1	1.6	0.0
Private consumption contribution	3.1	-1.7	-5.1	-9.3	7.2	5.1	1.1	3.9	0.5
Total investment contribution	2.8	-1.2	-2.7	-2.2	5.3	-2.3	0.2	-2.6	-0.1
Public spending contribution	0.4	-0.3	-0.2	-0.5	1.0	0.0	0.1	0.0	0.1
Private consumption (% YoY)	4.2	-2.2	-7.3	-13.8	10.7	7.3	1.5	5.5	0.7
Public spending (% YoY)	2.6	-1.9	-1.2	-3.3	6.9	0.1	0.6	0.1	0.6
Total investment (% YoY)	13.4	-5.7	-15.9	-12.9	27.4	-14.2	1.4	-16.3	-0.3
Exports (% YoY)	2.6	0.6	9.1	-17.3	9.3	3.1	2.0	1.7	0.6
Imports (% YoY)	15.6	-4.5	-19.0	-17.9	17.1	-3.3	2.2	-5.3	0.7
Unemployment rate (%, last quarter)	7.2	9.1	8.9	11.0	9.3	8.1	7.6	8.6	8.3
Inflation (% YoY, last quarter)	23.3	47.4	52.2	36.4	51.4	52.2	37.9	54.4	39.5
Fiscal balance (% of GDP)	-5.9	-4.9	-3.8	-8.3	-3.6	-3.7	-2.5	-3.9	-2.9
Primary fiscal balance (% of GDP)	-3.8	-2.3	-0.4	-6.4	-2.1	-2.3	-0.8	-2.5	-1.2
Trade balance (% of GDP)	-0.8	-0.1	4.0	3.8	3.8	3.9	3.7	4.0	4.1
Current account balance (% of GDP)	-4.8	-4.9	-0.8	0.9	1.4	1.4	0.7	1.4	0.8
Official interest rate (end of period)	28.75	59.25	55.00	38.00	38.00	30.00	27.50	30.83	27.38
3-month interest rate (end of period)	27.44	56.76	45.13	29.55	31.49	33.58	27.02	33.04	27.13
10-year interest rate (end of period)	5.91	10.86	19.36	14.61	18.40	16.99	14.15	17.24	14.75
Exchange rate vs. U.S. dollar (end of period)	18.65	37.70	59.89	84.15	102.72	160.00	214.58	167.88	216.27
Exchange rate vs. euro (end of period)	22.37	43.17	67.28	103.26	116.34	180.93	249.95	190.10	251.30
Private lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Household lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. non-financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Savings rate (% pers. disp. income, avg.)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

Source: MAPFRE Economics (based on INDEC data)
Forecast end date: April 28, 2022

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- The IMF has approved a new US$44 billion aid package for Argentina; a 30-month program with immediate disbursement of US$9.6 billion.
- Commitment to reforms, fiscal consolidation and end of deficit monetary financing.
- The Argentine peso ended the quarter at 111 ARS/USD, with an 8% depreciation.
- The economic growth forecast for 2022 is 3.0%.

The Central Bank of Argentina (BCRA), at its meeting of March 22, decided to increase the interest rate of the 28-day term LELIQ (reference rate) by 2 percentage points, from 42.5% to 44.5% per annum. In its Objectives and Plans for 2022, the BCRA reported that it was beginning to leave behind the period of exceptional policies generated by the pandemic and resumed the objectives set forth in January 2020. In that sense, interest rate hikes took place in January, February, and again in March to establish a policy interest rate trajectory to tend towards positive real rates and to preserve monetary and exchange rate stability.

The risks for the Argentine economy are varied. On the one hand, the price shock that will continue to keep inflation high and make it difficult to stabilize the exchange rate and, on the other hand, the political difficulties to carry out the reforms agreed upon in the IMF package. Despite this, progress is expected, especially on fiscal consolidation, otherwise credibility with the IMF would be severely damaged.

1.2.12 China

The resurgence of COVID-19 aggravates the economic slowdown already underway.

The latest economic activity indicators, up to February, show positive trends in retail sales and investment. However, other indicators reflect less favorable performance, such as real estate sales (-19.3%), and there are indications among large real estate companies of drops of 43% in this same period. The market is showing some discomfort with the discrepancy between certain data, namely those that point to everything going well (industrial production, investment, and retail sales) and those that paint a different picture (upturn in unemployment, real estate sales and prices, falling wages and low inflation, except in fuels). In addition, in March, the rebound of COVID-19 cases led to new lockdowns in some regions with significant weight in terms of GDP, such as Shenzhen (see Chart 1.2.12-c). Thus, economic activity is expected to slow down in March and April.

With respect to indicators that forecast behavior in the coming months, the purchasing managers' indexes (PMIs) for March receded and are below the contraction threshold (<50), following a downward trend for a year now, with the composite at 43.9, manufacturing at 48.1 and services at 42.0 points. January–March retail sales (cumulative) are down 3.5%, while retail surveys remain positive and industrial production is up 5.0% year-to-date (March).

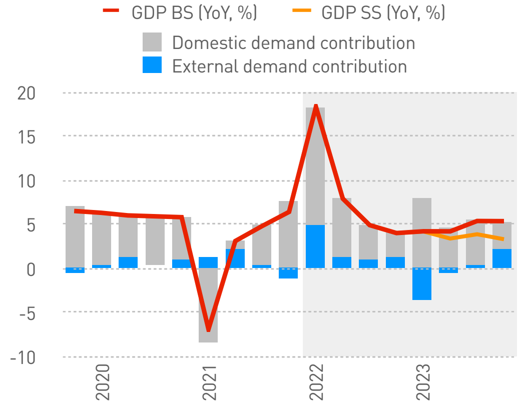
In this context, we have lowered the growth estimate for 2022 to 4.8% (from 5.0% in our previous report), especially due to the new lockdowns imposed in March and the consequent disruption of normal production and consumption activities. Even so, consumption is expected to grow 4.7% and public consumption 8.1%. Investment (+4.8%) is low compared to pre-COVID-19 levels, a situation likely related to the crisis in the construction sector. Exports (+4.1%) should be at a normal level, but this outlook may change in the face of pressure from the United States to join the sanctions against Russia (see Table 1.2.12 and Charts 1.2.12-a and 1.2.12-b).

- Economic growth in China is slowing due to problems in the real estate sector and will now be aggravated by the imposition of new lockdowns due to pandemic flare-ups.
- Inflation, which remains subdued, will allow monetary policy to turn toward an accommodative tone. However, this is also a symptom of slackening consumer demand.
- Regulators continue paying attention to systemic risks in the real estate sector.

Inflation, meanwhile, came in at 1.5% in March, stable with respect to January, an "anomaly" in these times and an indirect sign that there is not so much pressure on demand. The exception is precisely fuels, up 23.4%, including gas, electricity, and domestic fuels (+3.6% YoY). Food receded (-3.9%) and core inflation was 1.1%. The central bank has kept the 1-year marginal lending facility rate and 7-day rates unchanged at 2.85% and 2.10%, respectively, and injected RMB 100 billion of long-term liquidity. This contrasts with market expectations of interest rate cuts. The resurgence of COVID-19 cases implies further downward pressures for activity growth and the real estate sector, in particular, land sales and the number of housing projects begun deteriorated further despite marginal easing measures at the local level. Due to this worsening activity, we believe that the next steps will be monetary policy easing with a 10 bps cut in the interest rate and a 50 bps cut in the required reserve ratio (RRR) in the coming months, as well as a more expansionary fiscal policy.

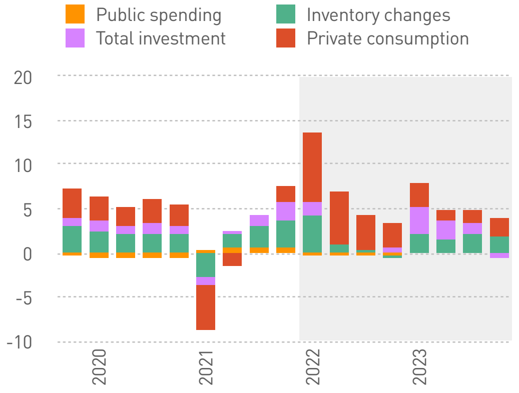
In terms of risks to the Chinese economy, the worsening property market remains, with a significant number of developers struggling with liquidity difficulties. As mentioned above, sales fell by 19%, with the decline reaching 43% in a group of larger developers. In the same vein, the resurgence of COVID-19 has led several provinces to impose lockdowns. Similarly, the problem in Ukraine may affect China, both through U.S. pressure on sanctions and through difficulties in exporting and importing certain products. China's exposure to Russian bonds may also bring setbacks in the event that Russia defaults. On the positive side, inflation remains low and will allow the central bank to take measures to support the economy. At the same time, there are tailwinds for the currency, as Saudi Arabia is considering accepting yuan for oil purchases. If this materializes, it would be a blow to the dollar. The U.S. freeze on Russia's central bank reserves has made many countries think about whether their reserves are safe in American hands in the event of any discrepancy in positions.

Chart 1.2.12-a
China: GDP breakdown and forecasts



Source: MAPFRE Economics (based on BoPRC data)

Chart 1.2.12-b
China: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on BoPRC data)

Table 1.2.12
China: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	6.9	6.7	6.0	2.2	8.1	4.8	5.3	3.7	4.8
Domestic demand contribution	6.7	7.4	5.2	1.6	6.1	5.1	5.0	4.0	4.5
External demand contribution	0.2	-0.6	0.7	0.7	2.0	-0.3	0.3	-0.4	0.3
Private consumption contribution	3.7	3.2	2.5	-0.9	5.2	1.9	3.2	1.4	3.0
Total investment contribution	2.6	3.1	2.2	1.3	1.1	1.9	1.9	1.4	1.6
Public spending contribution	0.3	1.2	1.1	0.8	0.3	1.4	0.1	1.4	0.1
Private consumption (% YoY)	9.4	8.1	6.3	-2.4	12.9	4.7	7.8	3.4	7.3
Public spending (% YoY)	2.0	7.1	6.6	4.6	2.1	8.1	0.5	8.1	0.5
Total investment (% YoY)	6.2	7.3	5.1	3.1	2.6	4.8	4.7	3.5	3.9
Exports (% YoY)	6.7	4.4	2.3	2.0	17.9	4.1	3.1	2.1	1.5
Imports (% YoY)	7.8	6.5	-0.7	-2.2	6.5	4.4	9.1	2.6	7.1
Unemployment rate (%, last quarter)	2.9	2.9	3.1	3.5	3.4	3.5	3.2	3.7	3.5
Inflation (% YoY, last quarter)	1.8	2.2	4.3	0.1	1.8	3.0	2.4	3.8	3.7
Fiscal balance (% of GDP)	-4.8	-4.7	-5.6	-8.6	-5.2	-7.1	-6.0	-7.4	-6.4
Primary fiscal balance (% of GDP)	-1.8	-1.5	-2.2	-4.7	-1.5	-3.7	-2.8	-4.0	-3.1
Trade balance (% of GDP)	3.9	2.7	2.8	3.5	3.1	2.4	2.6	2.3	2.8
Current account balance (% of GDP)	1.5	0.2	0.7	1.9	1.8	1.1	0.7	1.0	0.9
Official interest rate (end of period)	3.25	3.30	3.25	2.95	3.00	2.75	3.00	2.87	3.11
3-month interest rate (end of period)	5.53	3.70	3.20	3.03	2.73	2.37	2.63	2.50	2.80
10-year interest rate (end of period)	3.88	3.23	3.14	3.14	2.78	3.12	3.76	3.29	3.98
Exchange rate vs. U.S. dollar (end of period)	6.51	6.88	6.99	6.52	6.35	6.42	6.38	6.43	6.41
Exchange rate vs. euro (end of period)	7.80	7.87	7.85	8.00	7.19	7.25	7.44	7.27	7.44
Private lending (% YoY, average)	13.1	12.9	13.1	13.1	12.3	11.9	10.2	11.6	9.9
Household lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. non-financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Savings rate (% pers. disp. income, avg.)	29.5	28.8	29.0	33.0	30.3	30.1	28.4	30.6	28.3

Source: MAPFRE Economics (based on BoPRC data)
Forecast end date: April 28, 2022

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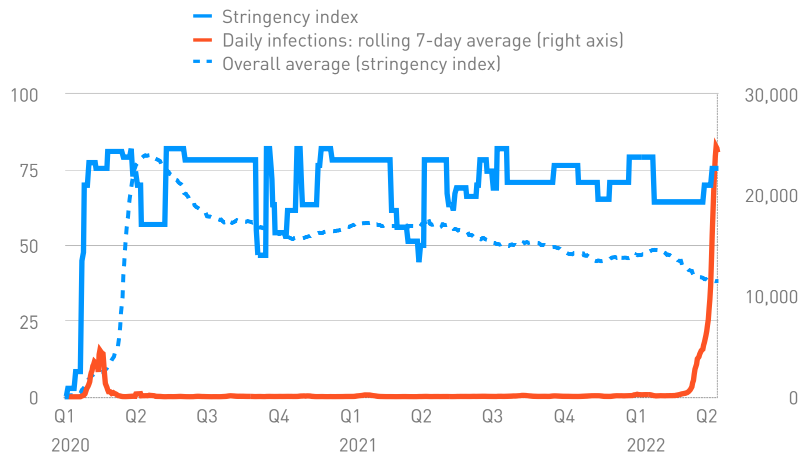
Chart 1.2.12-c
China: daily COVID-19 infections and stringency index



Source: MAPFRE Economics (based on data from the Coronavirus Government Response Tracker, University of Oxford)

1.2.13 Indonesia

The commodity cycle favors the return to the growth trajectory.

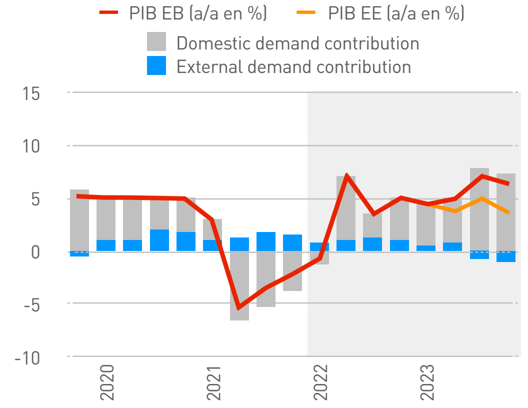
Indonesian GDP rose 5.0% YoY in the last quarter of 2021, driven by average growth of 3.7% YoY. The strength has been mainly in exports (+24% YoY full year), with imports growing 23.3%, while consumption rose 2%, investment 3.8% and government consumption 4.2%. Exports benefited and continue to do so in 2022, thanks to the upward price flow of the country's main export, palm oil, resulting in a highly positive trade balance (since 2020) of $36.2 billion (in February). This is due to the rise in prices of exported products (16% on average in 2021), among which are the aforementioned palm oil, coal and, to a lesser extent, gas. This strength in the trade balance should continue in the coming quarters, in view of the evolution of prices of all commodities, including agricultural and all mining, and will continue to be a driver for 2022 GDP. This surplus is very positive for the currency stability that has been verified throughout 2021, with moderate inflation also contributing to this.

In terms of outlook surveys, the manufacturing PMI rose to 53.8 in March (from 50.2 in February). Meanwhile, household surveys and consumer confidence indicators point to a continuation of the recovery. Retail sales in February were up 14.5% year-on-year. Against this backdrop, we estimate Indonesian GDP growth of 5.7% in 2022 and 5.6% in 2023, thanks to favorable conditions for exports (see Table 1.2.13 and Charts 1.2.13-a and 1.2.13-b).

Inflation, meanwhile, stood at 2.6% in March, with core inflation at 2.4%, a level well below what is being verified in other parts of the world. So it seems that, for now, Indonesia is sheltered from rising energy, commodity costs and supply chain disruptions. The reason is that Indonesia is a net exporter. Producer prices have risen by only 3%, while in Europe there are countries where they are up 30%. At its

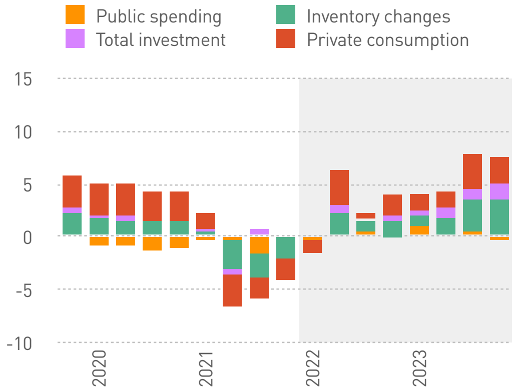
- **In 2022, export-driven growth of 5.7% is expected.**
- **High prices for palm oil, coal and other raw materials favor international terms of trade.**
- **Inflation is benign (2.6% YoY in March) in the context of what is happening in the rest of the world.**
- **The central bank has decided to maintain interest rates to continue supporting the economic recovery.**

Chart 1.2.13-a
Indonesia: GDP breakdown and forecasts



Source: MAPFRE Economics (based on BPS data)

Chart 1.2.13-b
Indonesia: domestic demand breakdown and forecasts



Source: MAPFRE Economics (based on BPS data)

Table 1.2.13
Indonesia: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	5.1	5.2	5.0	-2.1	3.7	5.7	5.6	4.2	4.7
Domestic demand contribution	4.8	6.2	3.6	-3.4	2.7	5.9	7.1	4.4	6.2
External demand contribution	0.3	-1.1	1.4	1.4	1.0	-0.2	-1.5	-0.2	-1.5
Private consumption contribution	2.8	2.8	2.9	-1.5	1.1	2.2	3.5	1.4	3.2
Total investment contribution	2.0	2.2	1.5	-1.6	1.2	2.4	3.3	1.7	2.5
Public spending contribution	0.2	0.4	0.3	0.2	0.3	1.0	0.3	1.0	0.4
Private consumption (% YoY)	5.0	5.1	5.2	-2.7	2.0	4.2	6.4	2.6	5.9
Public spending (% YoY)	2.1	4.8	3.3	2.0	4.2	11.4	4.1	11.4	4.1
Total investment (% YoY)	6.2	6.7	4.5	-5.0	3.8	7.3	9.7	5.2	7.6
Exports (% YoY)	8.9	6.5	-0.5	-8.1	24.0	5.1	-2.5	3.3	-4.0
Imports (% YoY)	8.1	12.1	-7.1	-16.7	23.3	7.1	4.1	4.9	2.4
Unemployment rate (%, last quarter)	5.3	5.1	5.1	6.7	6.1	5.8	5.4	6.2	6.2
Inflation (% YoY, last quarter)	3.5	3.3	2.7	1.6	1.8	4.6	3.0	6.3	3.9
Fiscal balance (% of GDP)	-2.6	-1.7	-2.2	-6.2	-4.6	-4.5	-3.9	-4.7	-4.2
Primary fiscal balance (% of GDP)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Trade balance (% of GDP)	1.9	0.0	0.3	2.7	3.7	4.4	2.5	4.4	2.4
Current account balance (% of GDP)	-1.6	-2.9	-2.7	-0.4	0.3	0.5	-0.9	0.5	-1.0
Official interest rate (end of period)	4.25	6.00	5.00	3.75	3.50	4.25	4.75	5.07	5.30
3-month interest rate (end of period)	5.48	7.70	5.51	4.06	3.75	4.68	5.68	5.53	6.08
10-year interest rate (end of period)	6.31	7.98	7.10	6.10	6.38	7.27	7.47	7.83	7.95
Exchange rate vs. U.S. dollar (end of period)	13,484	14,380	13,883	14,050	14,253	14,189	13,759	14,463	13,926
Exchange rate vs. euro (end of period)	16,171	16,465	15,596	17,241	16,143	16,045	16,027	16,369	16,178
Private lending (% YoY, average)	8.2	10.8	8.8	1.4	0.9	8.7	12.3	9.5	12.6
Household lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. non-financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. financial lending (% YoY, average)	15.1	5.6	-3.0	-6.0	-12.0	29.8	23.8	29.5	23.9
Savings rate (% pers. disp. income, avg.)	23.6	24.0	22.8	21.4	25.7	25.2	24.0	25.6	23.2

Source: MAPFRE Economics (based on BPS data)
Forecast end date: April 28, 2022

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March meeting, the Central Bank of Indonesia maintained interest rates at 3.50%. The decision is consistent with the need to maintain exchange rate stability and control inflation (the central bank's inflation target stands at 3%, +/- 1%), along with efforts to revive economic growth despite the accumulation of external pressures, particularly geopolitical tensions between Russia and Ukraine. Bank Indonesia has also continued to optimize its policy mix strategy to maintain stability and support economic recovery.

Thanks to the trade surplus, the current account balance also moved into positive territory in Q4 2021 (+0.28% of GDP, final). The existence of high external financing may pose a risk, especially if the Federal Reserve raises interest rates faster than Bank Indonesia. On the other hand, the currency has stable performance thanks to the positive trade balance that offsets the negative effect of outward investment flows.

1.2.14 Philippines

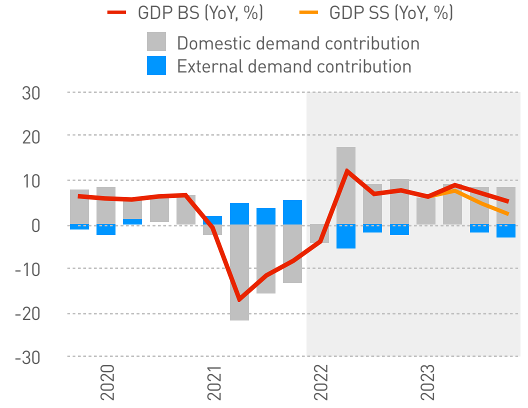
Economic recovery will continue after a strong 2021.

The Philippine economy grew by 7.7% YoY in the fourth quarter of 2021 and by 5.5% in the full year thanks to the end of the pandemic restrictions, which were very tight in the first half of last year. In addition, private consumption also grew by 7.5% YoY and public consumption by 7.4% YoY. The recovery in investment has also lost some steam (+12.6% in the last quarter of 2021). The manufacturing PMI improved to 53.2 in March from 52.8 in February. In addition, the central bank's surveys for the next quarter by sector all point to a continuation of the recovery: industry, construction, trade and services. Consumption should grow by 6.8% and investment by 13%, while exports are expected to grow by 8.8% and imports by 9.5%. Thus, we have adjusted the GDP growth forecast for 2022 to 6.8% and that for 2023 to 5.7% (see Table 1.2.14, and Charts 1.2.14-a and 1.2.14-b).

- **The recovery of the Philippine economy will continue despite headwinds from inflation and currency depreciation.**
- **The central bank is holding interest rates stable to continue supporting recovery while tolerating some depreciation of its currency.**
- **Foreign investment may decline due to uncertainty, but domestic investment will remain strong.**

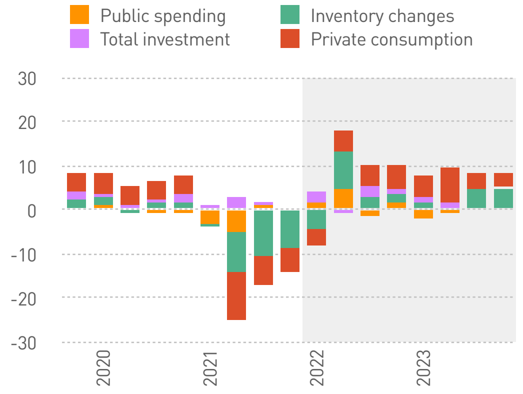
Inflation stood at 4.0% in March, with high increases in transportation (10.3%), electricity, gas and fuels (17.4%). Thus, inflation reached the upper band of the 2-4% target range of the Central Bank of the Philippines (BSP). In its February meeting, the BSP kept interest rates unchanged at 2.00% (Overnight Repo). In addition, it is expected to maintain an

Chart 1.2.14-a
Philippines: GDP breakdown and forecasts



Source: MAPFRE Economics (based on PSA data)

Chart 1.2.14-b
Philippines: domestic demand breakdown breakdown and forecasts



Source: MAPFRE Economics (based on PSA data)

Table 1.2.14
Philippines: main macroeconomic aggregates

						Baseline (BS)		Stressed (SS)	
	2017	2018	2019	2020	2021(e)	2022(f)	2023(f)	2022(f)	2023(f)
GDP (% YoY)	6.9	6.3	6.1	-9.6	5.6	6.8	5.7	5.1	5.0
Domestic demand contribution	7.9	8.8	6.3	-13.2	8.1	8.0	8.0	6.0	7.4
External demand contribution	-0.9	-2.4	-0.2	3.6	-2.5	-1.2	-2.3	-0.9	-2.4
Private consumption contribution	4.3	4.2	4.2	-5.8	3.1	5.0	4.0	3.4	3.7
Total investment contribution	2.7	3.5	1.0	-5.9	2.1	3.0	2.9	2.5	2.6
Public spending contribution	0.7	1.6	1.1	1.6	1.1	0.7	0.2	0.7	0.2
Private consumption (% YoY)	6.0	5.8	5.9	-7.9	4.2	6.8	5.5	4.8	5.1
Public spending (% YoY)	6.5	13.4	9.1	10.5	7.0	4.7	1.5	4.7	1.5
Total investment (% YoY)	10.6	12.9	3.9	-27.5	9.6	12.7	11.6	10.7	10.4
Exports (% YoY)	17.4	11.8	2.6	-16.3	7.8	8.8	10.6	7.1	9.1
Imports (% YoY)	15.1	14.6	2.3	-21.6	12.9	9.5	13.4	7.6	12.6
Unemployment rate (%, last quarter)	5.0	5.1	4.6	8.7	6.8	6.3	5.9	6.4	6.0
Inflation (% YoY, last quarter)	3.0	6.1	1.4	2.9	3.6	5.9	2.6	7.5	3.2
Fiscal balance (% of GDP)	-2.1	-3.1	-3.4	-7.6	-8.6	-8.4	-7.1	-8.9	-7.8
Primary fiscal balance (% of GDP)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Trade balance (% of GDP)	-12.2	-14.7	-13.1	-9.3	-13.4	-17.8	-16.0	-18.3	-17.0
Current account balance (% of GDP)	-0.7	-2.6	-0.8	3.1	-1.2	-5.2	-3.9	-5.6	-4.7
Official interest rate (end of period)	3.00	4.75	4.00	2.00	2.00	2.50	3.25	3.74	4.18
3-month interest rate (end of period)	3.22	5.03	3.97	2.00	1.81	2.67	3.37	3.80	4.26
10-year interest rate (end of period)	5.70	7.05	4.44	2.97	4.72	5.80	5.88	6.52	6.63
Exchange rate vs. U.S. dollar (end of period)	49.92	52.72	50.74	48.04	50.27	51.43	49.07	52.23	49.46
Exchange rate vs. euro (end of period)	59.87	60.37	57.01	58.94	56.93	58.16	57.16	59.11	57.46
Private lending (% YoY, average)	17.6	16.8	9.5	4.0	0.9	6.8	8.0	7.5	8.2
Household lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. non-financial lending (% YoY, average)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
P.S. financial lending (% YoY, average)	9.4	10.3	6.9	-8.0	8.1	8.8	12.2	7.9	12.2
Savings rate (% pers. disp. income, avg.)	7.1	6.4	5.0	5.6	3.5	4.1	5.9	4.7	5.3

Source: MAPFRE Economics (based on PSA data)
Forecast end date: April 28, 2022

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accommodative policy to ensure the sustainability of the recovery. The central bank noted that economic growth appears to be gaining traction on improved mobility and sentiment due to the relaxation of quarantine protocols. However, given the ongoing recovery, the BSP's priority remains to maintain support for the domestic economy. Thus, the central bank's stance on monetary policy is to continue to support the recovery and thus maintain rates, which carries some risk to currency stability. With such a move, however, it aims to avoid a premature exit from pandemic response measures to avoid long-term economic damage. The current policy is also supported by a manageable inflation outlook.

The main risks heading into 2022 for the Philippine economy come from inflation, energy prices, and freight transport costs. The May 2022 presidential election also introduces uncertainty and may mainly affect foreign direct investment.

2. Industry Outlook

2.1 The economic environment and its impact on insurance demand

2.1.1 Global markets

The beginning of the Russian invasion of Ukraine in February 2022 has complicated the outlook for global economic activity and, consequently, the performance of insurance markets worldwide, which are facing an environment of higher uncertainty, a slowdown in economic growth beyond what was expected before the conflict started, and greater inflationary pressures. Some of the main problems generated by the post-pandemic economic reopening process, instead of being corrected, have been aggravated by the war and the sanctions imposed on Russia for the invasion. The downward revision of the global economic growth estimate to 3.6% (6.1% in 2021), rising inflation forecasts and increased uncertainty due to the conflict (coupled with a pandemic that is still causing distortions in some economies) are darkening the outlook for business growth and profitability in the insurance industry in 2022. The picture remains mixed, however. While some economies risk falling into a situation of economic stagnation with high inflation rates, which would be a particularly damaging scenario for all sectors of the economy, others, in which the labor market remains strong, have better prospects despite inflationary pressures and the complex economic and geopolitical outlook.

The war in Ukraine and the sanctions against Russia have put pressure on energy and commodity prices, which have risen sharply, leading to higher and more persistent inflation than expected. This has been fueled by supply bottlenecks after the reopening of the economy (which were starting to improve, but have worsened again following the invasion) and the extensive fiscal and monetary aid packages implemented to combat the situation caused by the pandemic. This situation casts a shadow on the outlook for the insurance industry, whose profitability may be negatively affected by the erosion of business margins due to inflation, increasing the pressure on insurance prices at a time when the inflationary process will reduce household purchasing power and make it more difficult to transfer the cost increase to prices. In terms of Non-Life business volume in this environment (see Box 2.1.1), auto insurance will remain impacted by the fall in new vehicle registrations (still far below pre-crisis levels), which is being amplified by the supply bottlenecks due to the shortage of semiconductors and metals such as aluminum, of which Russia is one of the main producers. These disruptions in supply chains continue to weigh down new vehicle registrations, negatively impacting the Auto insurance business. On the positive side, in terms of business volume, some lines of business, such as health and Life protection insurance, may benefit from increased sensitivity to the risk of illness and death as a result of the pandemic and war, especially in countries where public health systems are weaker. Other important business segments, such as home multirisk and industrial, also tend to be resilient in these situations.

Box 2.1.1
Updated forecasts for growth in Non-Life premiums: an assessment of the effect of the crisis in Ukraine

The new economic environment

In the wake of Russia's invasion of Ukraine, the trade, financial and confidence disruption this has entailed, and the sanctions imposed by the West, the global economic outlook has visibly deteriorated. The recovery of pre-pandemic levels of economic activity, delayed at the end of 2021 by the emergence of the Omicron variant, has been again postponed for a large number of countries as a result of the geopolitical crisis. At the same time, the global economic context is becoming more complex, due mainly to an exhaustion of fiscal policy coupled with the deterioration in production caused by the continued disruptions in the value chain. The situation is being aggravated by the acceleration of two kinds of inflation (one determined mainly by demand, as in the United States, and another driven by supply factors linked to energy, gas and electricity provision and cost problems, as in Europe) that determines different paths for economic activity and monetary policy. This context is also marked by a return to uncertainty and risk aversion, which, on the one hand, is increasing savings rates and, on the other, reducing consumption while tightening financial conditions globally.

Broadly speaking, for the selected markets we are concerned with in this analysis, the deterioration in the outlook compared to the previous global economic outlook is palpable, but not catastrophic (see Table A). For the time being, under our baseline scenario, we still believe that a de-escalation of geopolitical tensions is possible over the next two months, although the risks lie on the downside.

Table A.
Change in average expectations 2022-2023
(basis points over January 2022 forecasts;
exchange rate in % appreciation/depreciation)

	Growth	Inflation	Official interest rate	Curved slope	Exchange rates	Non-Life premiums
United States	-80	190	100	-69	-4%	-5
Eurozone	-50	160	13	6	4%	-30
China	-20	15	-13	5	1%	-13
Spain	-50	135	13	8	4%	-10
Brazil	-25	65	260	-103	-10%	-12
Mexico	-50	95	200	-169	-1%	-50
Turkey	-40	1,300	100	300	8%	-230

Source: MAPFRE Economics

In this new economic context, we generally expect a slowdown in growth compared to the previous baseline scenario, which will be more pronounced among developed countries that are especially exposed to trade with Eurasia, such as Europe, or financially sensitive to tighter conditions, such as the United States. On the other hand, countries exporting raw materials and commercially outside the scope of the

Box 2.1.1 (continued)
Updated forecasts for growth in Non-Life premiums: an assessment of the effect of the crisis in Ukraine

Chart A
United States: forecasts before and after the outbreak of the conflict in Ukraine
(YoY, %)

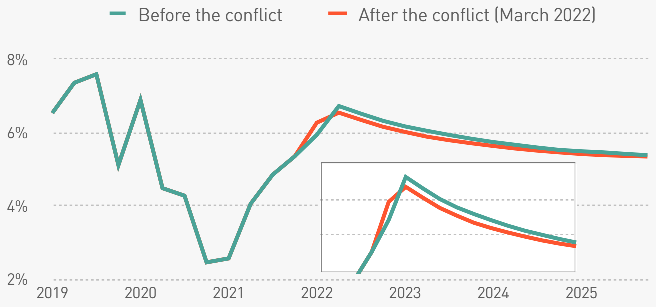


Chart B
Eurozone: forecasts before and after the outbreak of the conflict in Ukraine
(YoY, %)

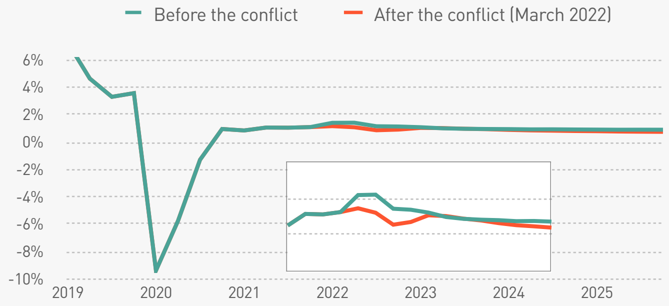


Chart C
Spain: forecasts before and after the outbreak of the conflict in Ukraine
(YoY, %)

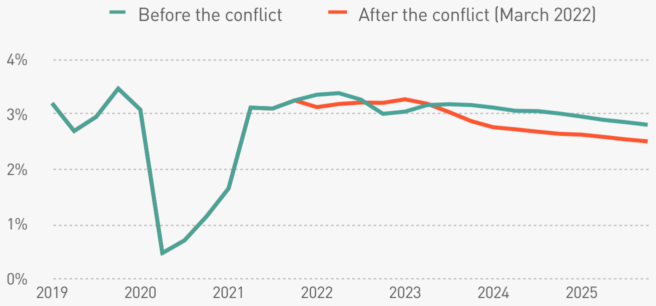
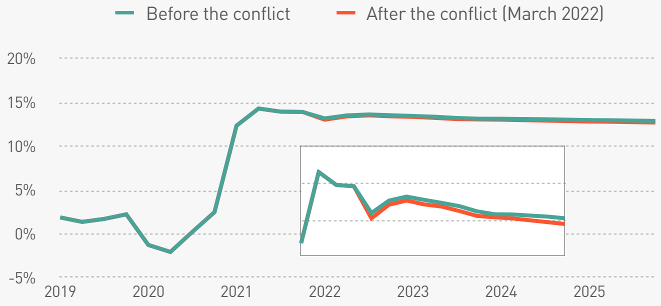


Chart D
Brazil: forecasts before and after the outbreak of the conflict in Ukraine
(YoY, %)



Box 2.1.1 (continued)
Updated forecasts for growth in Non-Life premiums: an assessment of the effect of the crisis in Ukraine

Chart E
Mexico: forecasts before and after the outbreak of the conflict in Ukraine
(YoY, %)

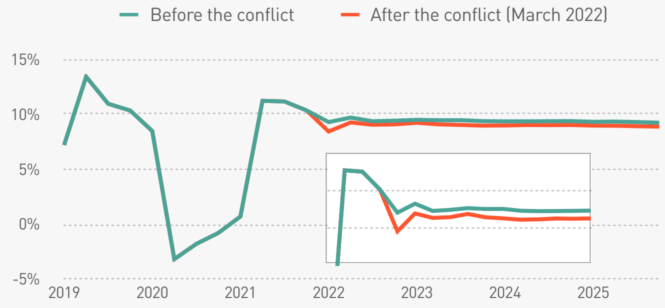
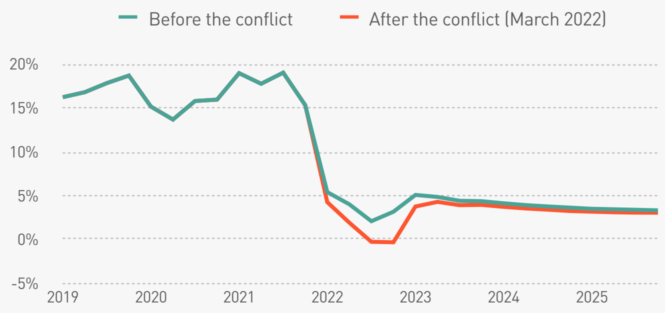


Chart F
Turkey: forecasts before and after the outbreak of the conflict in Ukraine
(YoY, %)



Source: MAPFRE Economics

sanctions seem to have less exposure in terms of activity, as is the case of Latin America and Asia.

On the inflation side, the asymmetries are also palpable, since the advanced economies have almost 150 basis points of higher inflation expected on average in 2022-2023, while other less exposed economies do not face such a challenge. Divergences in activity and inflation, especially between the United States and the Eurozone, or between developed and emerging markets, will give rise to differentiated monetary biases, with the countries in Latin American exhausting the path of interest rate hikes, the United States maintaining it, but with less intensity (lower expected hikes), and the Eurozone considering a hike at the end of 2023.

Changes in inflation, activity and monetary bias will lead to changes in the expected slope of the interest rate curve and, albeit with different intensities, this points in almost all countries to a loss of slope, anticipating growing fears in activity and in some cases investment (inverse slope).

Box 2.1.1 (continued)
Updated forecasts for growth in Non-Life premiums:
an assessment of the effect of the crisis in Ukraine

Adjustment to premium forecasts in the Non-Life segment

The last column of Table A shows how, as a result of the expected deterioration in economic activity, prices and financial conditions (currency depreciation and flattening of the curve), premium growth forecasts in the Non-Life segment of the insurance market are also deteriorating. On average, we expect Non-Life premium growth in 2022 and 2023 to be 40 basis points lower than we anticipated a year ago, with greater declines in markets that are strongly sensitive to the economic cycle (such as emerging markets) and smaller declines in more developed countries, even though the expected deterioration in activity is greater in the latter.

In our baseline scenario, no substantial changes are foreseen in the structure of insurance demand or supply, with the potential growth of the different markets we analyzed remaining intact and their monetary rules unchanged. Nor is an inflationary spiral or a stagflationary process expected to occur. Therefore, in the markets we analyzed, the conflict in Ukraine is expected to have transitory effects on insurance demand (as explained above) without altering their long-term growth. Thus, Non-Life premiums will return to their long-term growth path as of 2024, as shown in Charts A to F.

Source: MAPFRE Economics

On the other hand, the persistence of higher-than-expected inflation is leading to a tightening of monetary policy in most markets, both developed and emerging (with some exceptions, such as China), which will favor the development of Life insurance linked to traditional savings and annuities. However, situations of negative real interest rates persist, coupled with higher and lasting inflation, which may erode the saving capacity of households and reduce the demand for this type of product. As for the outlook for Life insurance policies in which the policyholder assumes the investment risk, the downturns and high volatility of the stock markets are making them difficult to market. Insurance companies will thus be forced to adapt these products to a new environment in which risk-free interest rates and risk premiums on fixed income are rising due to the withdrawal of monetary stimuli. Hence, the Life investment business faces a more complex scenario in which the sovereign and corporate bond market is playing a bigger role.

It is also noteworthy that asset valuations were at high levels, being driven, in the case of fixed income, by interest rate cuts and net bond purchase programs implemented by central banks to combat the economic repercussions of the pandemic. In terms of equities, many indexes surged to record highs, helped by the high liquidity and lack of returns in fixed income. The announcement of the withdrawal of monetary stimulus by the Federal Reserve and other central banks, coupled with the geopolitical situation caused by the invasion of Ukraine, has increased volatility and corrections in both the bond market and the main equity indexes. This situation may negatively affect the balance sheets and solvency positions of insurance companies that have not adequately managed these risks.

2.1.2 Eurozone

Economic growth forecasts for the Eurozone have been lowered by one percentage point from the previous estimate, pointing to 2.9% growth in 2022 versus 5.3% in 2021 (-6.5% in 2020) in an environment of great uncertainty as a result of the war in Ukraine and the sanctions against Russia for the invasion. Europe is the region most impacted by the conflict due to both its strong trade links and its energy dependence on Russia. Thus, the environment continues to be one of recovery and economic growth, but a significant slowdown is anticipated compared to the previous year, which complicates the outlook for the insurance sector. In addition, the rise in inflation due to the economic reopening after the worst phases of the pandemic has been aggravated by soaring energy, food and commodity prices as a result of the war. These factors may erode the profits of insurance companies, putting pressure on insurance prices.

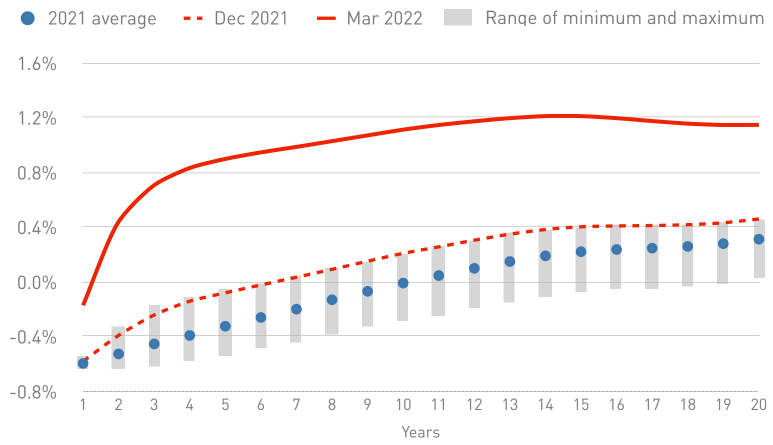
Disruptions in supply chains (which were beginning to improve) have worsened again and will continue to affect the automotive sector, due particularly to the shortage of chips needed for production together with other raw materials of which Russia is a major producer. This is weighing down new vehicle registrations and having a negative impact on the auto insurance business, and there is great uncertainty as to how long this situation may last.

On the other hand, the strong upturn and the persistence of inflation (7.4% in March) are leading to a change in the ultra-accommodative monetary policy of the European Central Bank (ECB), which is reducing its net asset purchase programs at a more accelerated pace than expected. Thus, the increase in net purchases of sovereign and corporate bonds is expected to end between July and September, with interest rate hikes starting "some time after" the end of the net purchase program. They would in any case be gradual, depending on the data that emerges.

In this regard, at its April meeting, the ECB decided to hold short-term interest rates at current levels (0% for main refinancing operations and -0.5% for the deposit facility). However, in the risk-free yield curves produced by the European Insurance and Pension Authority (EIOPA)[4] illustrated in Chart 2.1.2, another sharp increase in market risk-free interest rates can be seen in all tranches. These reach substantially higher levels than the maximums registered in 2021, with positive interest rates as of maturities over one year (when they remained in negative territory up to six years at the end of 2021). However, despite the new upturn, risk-free interest rates remain at relatively low levels (significantly below inflation), which, although improving, continues to paint a complex picture for the traditional Life savings and annuity business of insurance companies, which are facing a situation of negative real interest rates.

On the other hand, the Euro Stoxx 50 index—and in general, the main stock markets worldwide—have seen increased volatility due to the greater uncertainty generated by the war in Ukraine and the sanctions against Russia, together with the central banks' messages on the withdrawal of monetary stimulus measures. As a whole, these factors complicate the outlook for Life insurance products in which the policyholder assumes the investment risk. Such products will have to be adapted for an environment

Chart 2.1.2
Eurozone: risk-free yield curve
(%)



Source: MAPFRE Economics (based on EIOPA data)

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marked by greater volatility in equities, with fixed income offering higher interest rates and risk premiums more in line with the credit risk of the issues, once the central banks start to withdraw their net asset purchase programs.

2.1.3 Germany

Among the large Eurozone economies, Germany is the most exposed to the consequences of the war in Ukraine and the sanctions against Russia. Its economic growth forecast for 2022 has therefore been substantially downgraded, by around two percentage points, to 2.0%, compared to 2.9% growth in 2021 (-4.9% in 2020). As noted above, the war in Ukraine has again exacerbated the problems due to the sharp spike in energy prices and disruptions in supply chains. In any case, private consumption will continue to be the driver of German economic growth, followed to a lesser extent by investment, which creates an environment that is still favorable for the insurance sector, albeit with a higher level of uncertainty that has deteriorated confidence indicators.

On the other hand, German sovereign bond yields continue to experience a significant upward trend, and in April showed positive levels in all maturities over one year (when in the previous quarter they were negative in maturities up to 10 years). The upturn in inflation and the ECB's messages concerning the withdrawal of monetary stimulus and possible interest rate hikes at the end of the year are clearly reflected in the rise in German sovereign bond yields. While interest rate levels remain depressed, they are at least moving out of negative territory and the yield curve is sloping positively. This represents a slight improvement in the still-difficult environment for traditional life savings and annuity business given the low nominal interest rate levels, leading to a negative real interest situation. The German DAX, on the other hand, is showing continued volatility, which has increased as a result of the invasion of Ukraine, complicating the outlook for Life insurance products in which the policyholder assumes the investment risk. However, the upturn in fixed-income interest rates may help companies to market the type of products that offer some protection against the loss of purchasing power in the face of rising inflation, adapted to the risk profile of policyholders.

2.1.4 Italy

As is the case for the Eurozone as a whole, economic growth expectations for Italy have been lowered (by 1.5 percentage points) due to the war in Ukraine and the sanctions against Russia for the invasion. The forecast for the Italian economy in 2022 therefore points to GDP growth of 2.9%, a significant slowdown compared to its 2021 growth of 6.6% (-9.1% in 2020). The strong performance of private consumption and investment (with the help of European recovery funds) will be weighed down by the external sector as a result of the high energy prices and supply chain disruptions that the war in Ukraine has exacerbated. The outlook for the insurance sector in this market is therefore complicated, in an environment of higher inflation that is eroding household disposable income and business margins, which may negatively affect business volume and profitability while putting pressure on insurance prices.

Meanwhile, the ECB's change in monetary policy stance due to the upturn in inflation in the Eurozone (more persistent than expected) and, in particular, the end of net purchases of sovereign and corporate bonds scheduled for the third quarter of the year, continues to cause a spike in the risk premium and the term premium of Italian sovereign debt. This trend is in line with inflation (6.5% in March), although the level of nominal interest rates remains below inflation, leading to a situation of negative real interest rates that complicates the sale of traditional Life savings and annuity products. Furthermore, the equity markets are increasingly volatile, with a strong correction in the FTSE MIB underway since the beginning of the year that has worsened as a result of the invasion of Ukraine, although it seems to be improving. In any case, the outlook is complicated for Life insurance products in which the policyholder assumes investment risk, which have gained importance in the Italian market in recent years in the face of the sustained environment of low interest rates and, in recent months, as an alternative to hedge against the upturn in inflation.

2.1.5 Spain

The Spanish economy is also being affected by the war in Ukraine and the sanctions against Russia, although to a lesser extent than other large Eurozone economies. In any case, this situation has led to a substantial revision of economic growth expectations for 2022, lowering the forecast by 1.3 percentage points to 4.2% compared to 5.0% in 2021 (-10.8% in 2020). This means the Spanish economy will experience a slight slowdown in growth, postponing the return to its pre-pandemic level until 2023. The pandemic is trending favorably, having a positive impact on key sectors for the Spanish economy such as tourism, but the increase in energy and food prices has led to a sharp rise in inflation. Private consumption and investment (with the help of European funds) continue to recover, but they are losing momentum due to the elevated uncertainty, loss of household purchasing power, and drop in business margins as a result of inflation. This may hamper business growth in the insurance market and erode its profitability, increasing pressure on insurance pricing processes. Likewise, the supply shortage continues to slow down production levels in the automotive sector, weighing down exports and new vehicle registrations, a situation that has also worsened as a result of the invasion of Ukraine. The auto insurance business will therefore continue to suffer from this situation, and uncertainty has risen as to its possible recovery in the coming months.

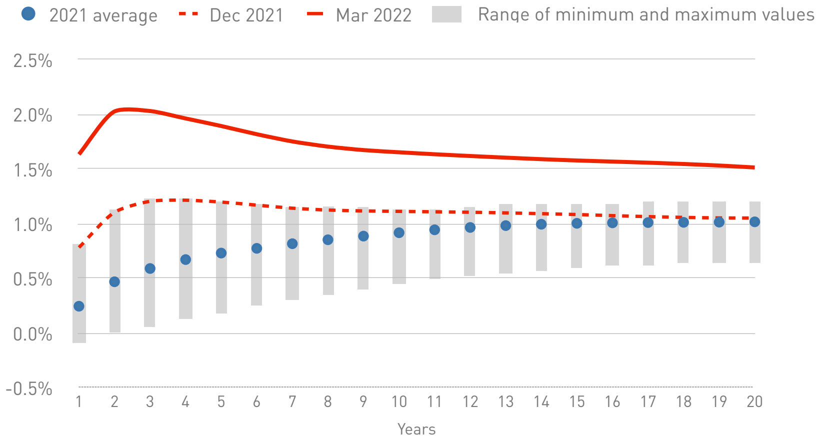
The savings-linked Life insurance business, on the other hand, will continue to be affected by the low interest rate environment. However, the situation is beginning to improve slightly as a result of the change in the ECB's monetary policy stance towards the end of the monetary easing process, with the end of the increase in net purchases of sovereign and corporate bonds planned for the third quarter and expectations of an interest rate hike at the end of the year (depending on the evolution of inflation). This is raising the market interest rate curve of the Spanish sovereign bond, which has moved out of negative territory in all maturities longer than one year and is beginning to offer a positive term premium. However, the nominal interest rates remain at levels lower than inflation, creating an environment of real negative interest rates, so the forecast is that insurance premiums for life insurance and traditional annuities are still far from pre-pandemic levels. Equity, which had been an alternative to hedge against the low interest rate environment and the upturn in inflation, has suffered a spike in volatility as a result of the war in Ukraine, complicating the outlook for the growth of Life insurance products in which the policyholder assumes the investment risk. However, the upturn in fixed income interest rates may drive sales of these types of products, which offer some protection against the loss of purchasing power in the face of rising inflation. Adapted to the risk profile of policyholders, they are positioned to take advantage of the rise in risk-free interest rates and risk premiums that are more in line with the credit risk of the issues, once the net purchase programs for sovereign and corporate bonds scheduled for the third quarter of the year are completed.

2.1.6 United Kingdom

Economic growth expectations for the United Kingdom in 2022 have also been lowered, being reduced by 0.7 percentage points to 3.7%, compared to 7.5% growth in 2021 (-9.4% in 2020). However, such growth remains significant and will enable it to exceed the pre-crisis level this year, driven by consumption and (to a lesser extent) private investment, which is being weighed down by the external sector due to high energy prices and supply chain shortages, problems that the war in Ukraine and the sanctions against Russia have exacerbated. The economic growth forecast for this year will continue to support the insurance market, although the upturn in inflation and the resulting erosion of household disposable income and corporate margins may end up negatively affecting business volume and profitability, putting pressure on insurance prices.

With regard to traditional Life savings and annuities, the Bank of England continued to tighten monetary policy and increased interest rates twice by 25 basis points in February and March, to 0.75%, as a result of the upturn in inflation (7% in March). The risk-free yield curves produced by EIOPA at the end of March (see Chart 2.1.6) show a significant rise in all sections of the curve, which is notably above the maximum levels reached in the previous year. A first section in the short maturities (up to two years) shows a markedly positive slope, and a second section shows an inversion of the yield curve in the middle and long sections, with a negative slope. Thus, uncertainty about inflation and the future direction of monetary policy continues to produce distortions in the yield curve. Despite being able to offer a positive term premium on maturities up to two years, the interest rate environment remains difficult for the marketing of traditional

Chart 2.1.6
United Kingdom: risk-free yield curve
(%)



Source: MAPFRE Economics (based on EIOPA data)

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Life savings and annuity products due to the low nominal interest rates, which are below inflation, generating an environment of negative real interest rates. On the other hand, the FTSE 100 continues to show high volatility, suffering a sharp contraction with the outbreak of the war before correcting and returning to close to its historical highs, which complicates the marketing of Life insurance products in which the policyholder assumes the investment risk, which are deeply rooted in this market.

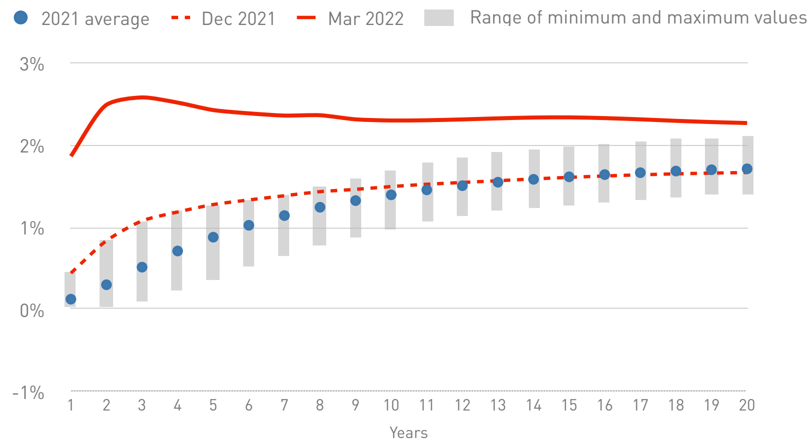
2.1.7 United States

GDP growth expectations in the United States have been lowered by 0.8 percentage points to 3.2% in 2022 as a result of the war in Ukraine and the sanctions against Russia. These circumstances are aggravating the problem of high inflation already present in this economy due to the increase in energy prices and supply bottlenecks in an economy with a saturated labor market and abundant liquidity in the system. The U.S. economy therefore continues to grow, painting a favorable picture for the insurance industry. This is the case despite expectations of an economic slowdown compared to the significant growth of 5.7% in 2021 (-3.4% in 2020), amid the further tightening of the ultra-loose monetary policy that the Federal Reserve has been applying and cutbacks in fiscal stimuli. The upturn in inflation and upward pressure on salaries may have a negative impact on the short-term profitability of the insurance industry due to the resulting increase in costs, which puts pressure on insurance rate-setting processes.

The Life business will benefit from interest rate hikes in an environment of economic growth. However, expectations of further rate hikes may delay the decision to purchase traditional Life savings and annuity products as they materialize. Meanwhile, the equity markets have also been impacted with increased volatility and rotations in portfolio composition in the new interest rate scenario, which may complicate the sale of Life insurance products in which the policyholder assumes investment risk, very common in this market.

The latest forward guidance from the Federal Reserve on a further tightening of monetary policy in the face of rising inflation was reflected in the most recent yield curves produced by EIOPA in December (see Chart 2.1.7), which show a sharp rise in market risk-free interest rates in all sections of the curve, significantly above the maximum levels reached in the previous year. Two sections of the curve can be clearly distinguished: a first section in the maturities up to three years with a steep positive slope, but also an inversion of the yield curve at the end of March 2022 in the middle and long sections (above three years), where it had a negative slope.

Chart 2.1.7
United States: risk-free yield curve
(%)



Source: MAPFRE Economics (based on EIOPA data)

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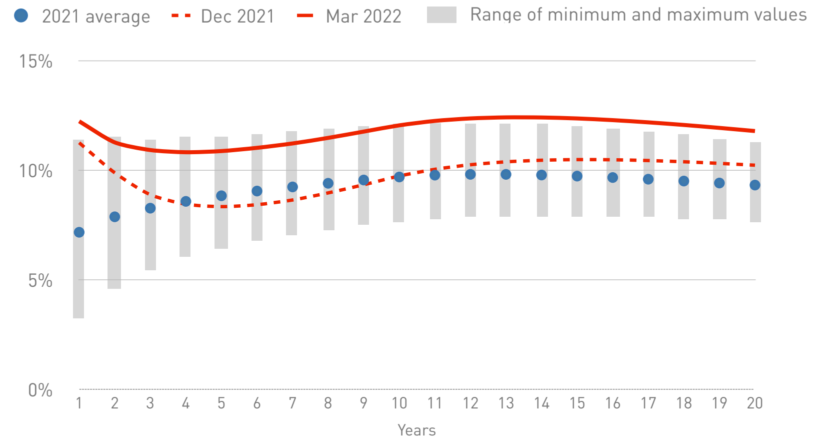
Despite being able to offer a positive term premium on products with maturities up to three years, the interest rate environment continues to be complicated for the marketing of savings products due to the low nominal interest rates, which remain below inflation, generating an environment of negative real interest rates. Meanwhile, equity markets continue to show signs of exhaustion (after reaching record highs in recent years) due to the economic slowdown, the end of fiscal aid and the increase in interest rates, which increases the cost of financing for companies. These increases in market interest rates affect both the risk-free component and the risk premium component (due to the end of the increased net purchase programs for sovereign and mortgage-backed corporate bonds), having a negative impact on the valuation of bond portfolios, but they have better prospects for 2022, as they can offer higher yields. These factors continue complicating the outlook for the Life insurance business in which the policyholder assumes the investment risk, and companies will have to adapt their products to a new interest rate environment in fixed income and greater volatility and lower profitability in equities, depending on the risk profile of the policyholders.

2.1.8 Brazil

In 2022, the Brazilian economy is expected to suffer a significant slowdown as a result of the tightening of monetary policy to control inflation, which is well above the central bank's target. However, expectations have improved slightly, with the real GDP growth forecast at 0.7% compared to the strong recovery in 2021, when real GDP grew by 5.0%, surpassing the pre-pandemic level (-4.2% in 2020). Economic reactivation and the rise in

Chart 2.1.8
Brazil: risk-free yield curve
(%)



Source: MAPFRE Economics (based on EIOPA data)

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energy prices caused a strong rebound in inflation, which is not yet under control (11.3% in March), forcing the central bank to tighten its monetary policy with new interest rate hikes, reversing the expansionary measures adopted to combat the economic effects of the pandemic. These measures are having a positive effect on exchange rates, which may provide somerelief from the negative impact of inflation on the profitability of insurance companies.

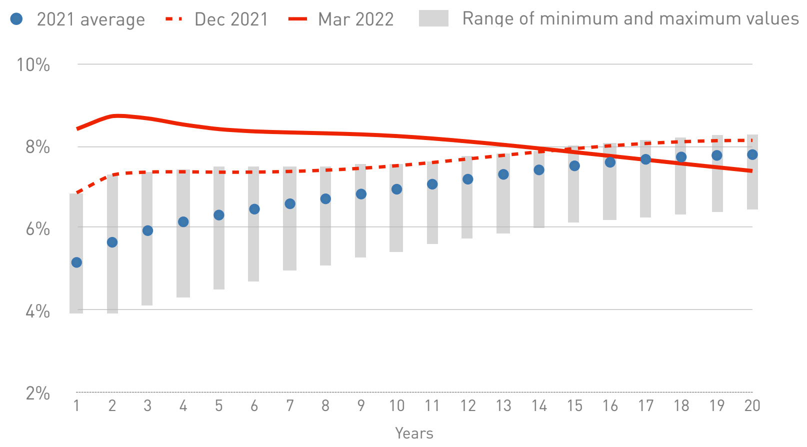
The deceleration of the economy in 2022 could hamper the growth of Non-Life insurance, which experienced a marked rebound in 2021. Problems in global supply chains continue to affect automobile production and new vehicle registrations, which are still far from pre-pandemic levels, a situation that will continue to weigh on the auto insurance business. Meanwhile, the interest rate environment following the latest rate hikes remains very favorable for the Life savings and annuities business as an instrument to protect household savings against rising inflation (coupled with increased risk sensitivity as a result of the pandemic, which may favor Life insurance as protection against the risk of death). Products with medium and long-term interest rate guarantees may be favored by the expectation that interest rates are near peak levels and could go down once inflation starts to ease. The Bank of Brazil, as a part of its monetary policy tightening process, raised interest rates again in 2022 to 11.75% (after applying five rate hikes in 2021, from 2%), and an additional increase could be applied in April 2022 before they stabilize. The risk-free yield curve produced by EIOPA (see Chart 2.1.8) is beginning to flatten, presenting a slight negative slope in its first tranches, but significantly less than in the previous quarter.

2.1.9 Mexico

For the Mexican economy, the GDP growth estimates for 2022 have been lowered to 1.6%, compared to 5.0% in 2021 (-8.4% in 2020), in a context of progressive monetary policy tightening to address rebounding inflation. These circumstances have been aggravated by additional pressure on energy and food prices arising from the conflict in Ukraine, stagnant consumption and persistently weak gross fixed investment. This implies a significant slowdown in the economy, generating a less favorable outlook for insurance business compared to 2021 in terms of business and profitability (due to the upturn in inflation). However, the economic growth and the increased risk sensitivity of households and companies as a result of the pandemic may continue to stimulate demand, especially in lines of business such as health and Life protection insurance.

On the other hand, rising inflation (7.45% in March) has led the Bank of Mexico to raise the official interest rate to 6.5% in March (from 5.5% in December), the second rate hike of 2022 (after five previous hikes in 2021). The EIOPA curves (see Chart 2.1.9) show a rise in market risk-free interest rates in the short and medium tranches in a curve that presents a negative slope in practically all of its tranches, except for the shortest (maturities up to two years), where it still offers a positive term premium. This interest rate environment remains favorable for the development of the Life savings On the other hand, rising inflation (7.45% in March) has led the Bank of Mexico to raise the official interest rate to 6.5% in March (from 5.5% in December), the second rate hike of 2022 (after five previous hikes in 2021). The EIOPA curves (see Chart 2.1.9) show a rise in market risk-free interest rates in the short and medium tranches in a curve that presents a negative slope in practically all of its tranches, except for the shortest (maturities up to two years), where it still offers a positive term premium. This interest rate environment remains favorable for the development of the Life savings and annuities business due to the high level of short-term interest rates and the need to protect savings against high inflation. Nevertheless, the economic slowdown and erosion of household purchasing power due to the sharp increase in prices may reduce savings capacity, which complicates the outlook for this line of business.

Chart 2.1.9
Mexico: risk-free yield curve
(%)



Source: MAPFRE Economics (based on EIOPA data)

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2.1.10 Argentina

For 2022, growth estimates for the Argentine economy have been revised slightly upward to 3.0%, compared to 10.2% in 2021 (-9.9% in 2020). This is moderate growth compared to 2021, when the Argentine economy recovered to pre-crisis levels, with private consumption being the main driver of growth. Inflation has rebounded again to 55.1% in March, contributed to by the increase in energy prices as a result of the war in Ukraine and the sanctions against Russia, with the currency continuing on its depreciation path, negatively affecting the profitability of insurance companies. The high inflation environment and the need to implement a series of reforms agreed on with the International Monetary Fund (IMF) may weigh on the economy and the insurance industry, although the moderate economic growth environment remains favorable for its performance.

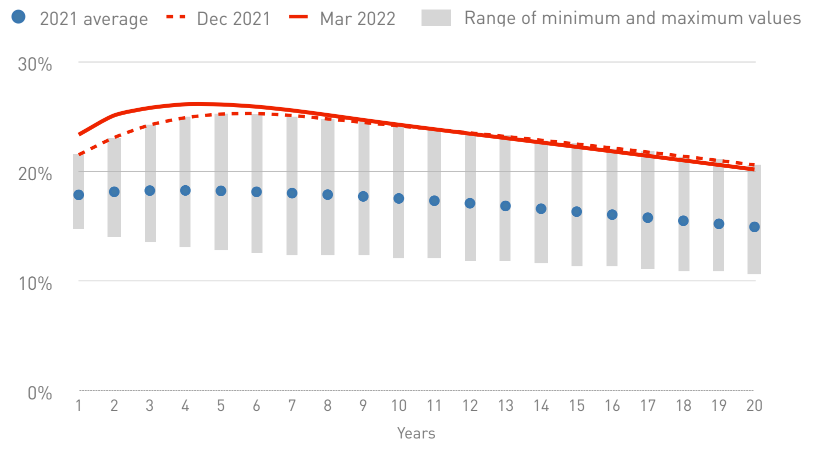
On the other hand, the central bank has tightened its monetary policy by raising the benchmark interest rate twice in March and April to 47% (from 40% at the beginning of the year), which is still below inflation in an environment of negative interest rates. This is a difficult context for the marketing of Life savings insurance products, which cannot offer sufficient interest rates to offset the loss of purchasing power due to high inflation, as financial assets with sufficient returns to support this type of product are not available on the market. However, the expected economic growth will continue to be favorable for the development of life insurance business.

2.1.11 Turkey

In the case of the Turkish economy, real GDP growth expectations for 2022 have been lowered to 2.0%, compared to 11.0% in 2021 (1.8% in 2020). This represents a sharp slowdown compared to the exceptional performance of the economy in the previous year, in an environment of high inflation that has been aggravated by the war in Ukraine and the sanctions imposed on Russia for the invasion. Inflation continues to rise, eroding household disposable income and corporate margins, hindering both business and profitability in the insurance industry. At its last meeting, the Turkish central bank decided to maintain its policy of not raising interest rates, deepening a situation of negative real interest rates and sharp exchange rate depreciations, which are fueling inflation due to higher import prices. All these factors are having negative repercussions on the business and profitability of the insurance industry, as inflation is driving up claims and operating costs, which cannot be compensated by companies' financial margins, putting pressure on insurance prices.

At its aforementioned April meeting, the Turkish central bank maintained the official interest rate at 14% despite the rise in inflation (which reached 61.1% in March). However, the EIOPA curves (see Chart 2.1.11) show a further rise in market risk-free interest rates, with a curve presenting a positive slope in its short and medium tranches before inverting in maturities above four years. This continues to produce a complex interest rate scenario for the sale of Life savings insurance products, on account of the uncertainty regarding short-term rates and a term premium that may be offered for longer-term products that is far from offsetting the loss ofpurchasing power caused by high inflation, which means that real interest rates are widely negative. Nonetheless, the outlook is a bit more favorable for the Life protection business due to the greater sensitivity to the risk of death generated by the pandemic and the war in an economy that, despite losing momentum, continues showing growth.

Chart 2.1.11
Turkey: risk-free yield curve
(%)



Source: MAPFRE Economics (based on EIOPA data)

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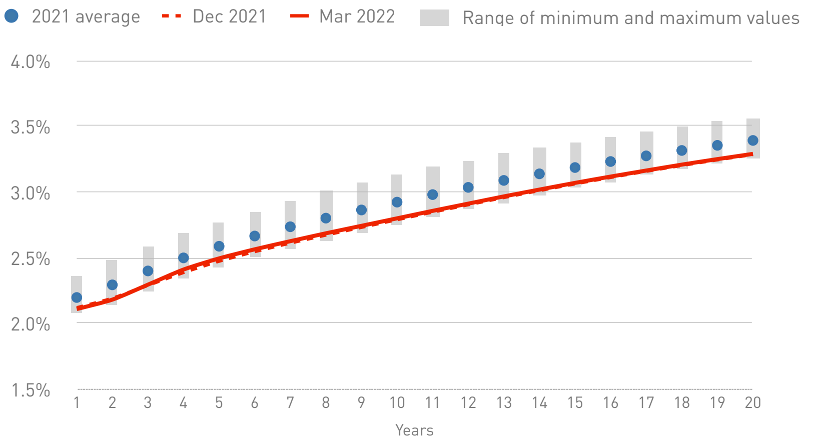
2.1.12 China

Economic growth expectations in 2022 for the Chinese economy have been slightly lowered (-0.2 percentage points), anticipating GDP growth of around 4.8%, down from 8.1% in 2021 (2.2% in 2020). This slowdown in the pace of growth is being influenced by the problems in the real estate market and the management of the pandemic, with the latest outbreaks leading to new lockdowns, coupled with the increase in energy prices as a result of the war in Ukraine and the sanctions against Russia. In any case, this level of economic growth remains significant and is supported by strong domestic demand. The anticipated economic growth in 2022, despite the slowdown, continues to create a favorable environment for the insurance industry, helped by the low level of insurance penetration in the economy and the monetary and fiscal stimulus policies being implemented by the Chinese government.

Chart 2.1.12
China: risk-free yield curve
(%)



Source: MAPFRE Economics (based on EIOPA data)

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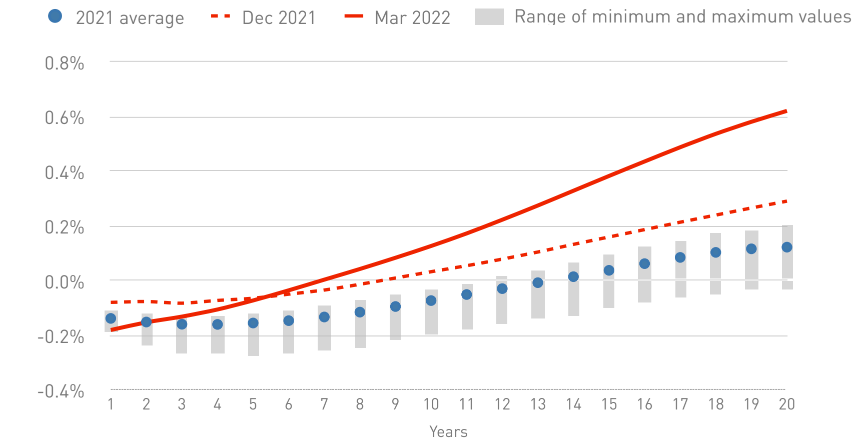
As for the interest rate environment, the pickup in inflation in China as a result of higher energy prices has been moderate, and the central bank has reaffirmed its intention to continue to pursue an accommodative monetary policy. The EIOPA curves (see Chart 2.1.12) show that risk-free interest rates have barely moved on a curve that remains positively sloped. This stable interest rate environment with positive term premiums is favorable for the Life savings and annuities insurance business, as it can offer higher medium- and long-term guaranteed rates than short-term rates. Meanwhile, the increased sensitivity to the risk of death due to the pandemic and the economic growth predicted for this year could also boost the Life protection business.

2.1.13 Japan

For Japan, estimates for economic growth in 2022 have been revised downward by 0.8 percentage points to 2.4% compared to 1.7% in 2021 (-4.5% in 2020). Despite the downward revision, this represents an acceleration in Japan's economic growth after a worse-than-expected 2021 due to supply chain problems and high energy prices, which will continue to have negative impacts due to the conflict in Ukraine. As a result, the country's GDP will not return to its pre-pandemic level this year. Private consumption will be the main driver of the acceleration in economic growth, followed to a lesser extent by investment, which will maintain a favorable environment for the insurance industry.

Chart 2.1.13
Japan: risk-free yield curve
(%)



Source: MAPFRE Economics (based on EIOPA data)

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For its part, the Bank of Japan has decided not to alter its ultra-accommodative monetary policy in an environment in which inflation has picked up slightly, but is still below its 2% target. On the EIOPA curves (see Chart 2.1.13), we observe that the risk-free interest rate curve has steepened, with negative values for maturities up to six years (compared to eight years in the previous quarter). This increase in the positive slope makes it possible to offer a higher term premium, favoring the marketing of Life savings and annuity products. Although interest rate levels remain low, the rebound in medium and long-term rates (notably higher than usual) is beginning to stimulate the growth of these lines of business. On the other hand, the interest rates of U.S. Treasury bonds (used by Japanese Life insurers as an alternative investment to boost the return on their portfolios) continue to rise, helping to restore some of the appeal of these investments to lever up returns.

2.1.14 Philippines

In the Philippines, economic expectations for 2022 have been revised upward, anticipating an acceleration in GDP growth to 6.8% compared to 5.6% in 2021 (-9.6% in 2020); it will thus exceed its level prior to the pandemic (which hit the country hard) this year. This robust economic growth, driven primarily by private consumption and investment, will favor the insurance business, which also stands to benefit from the low penetration of insurance in the country's economy. However, the spike in inflation and the currency depreciation being experienced may negatively affect insurers' short-term profitability by increasing the cost of claims and putting pressure on the price of insurance.

As regards Life insurance, the Central Bank of the Philippines is keeping the benchmark interest rate for monetary policy at 2% despite the upturn in inflation (4% in March). The return on the 10-year sovereign bond was slightly above 6% as of March 31, with the interest rate curve becoming steeper with a greater term premium, bolstering the sale of savings Life and traditional annuities products, as it is possible to guarantee higher medium and long-term rates than is the case in the short term.

2.1.15 Reinsurance

Global economic losses from natural and man-made catastrophes are estimated at $280 billion in 2021, up from $217 billion in 2020[5]. It should be noted that, of these losses, $270 billion were attributable to natural catastrophes. In addition to the devastating earthquake in Haiti, there were more than 50 severe floods worldwide, as well as tropical cyclones, extreme cold and heat events and severe convective storms. Total insured losses were $119 billion, the fourth-highest amount for a single year on record, of which natural catastrophes caused $111 billion, also the fourth-highest annual figure on record. The top loss of 2021 was Hurricane Ida in the United States, which in August lashed the southern United States with Category 4 winds before continuing on to the Northeast, where it unleashed heavy rains that caused heavy flooding in and around New York City. Swiss Re has estimated total insured losses from Ida at $30-32 billion.

The increase in insured damage has maintained a long-term trend (based on 10-year moving averages) of 5-7% annual growth, where recurring secondary peril events, such as severe convective storms, flooding and wildfires, have become increasingly important. In 2021, secondary risks accounted for 73% of all insured losses from natural catastrophes, confirming their growing contribution in global economic and insured losses. In this regard, the major events were winter storm Uri in the United States ($15 billion in insured losses) and the devastating floods in west-central Europe in July, which resulted in record insured losses of around $13 billion. However, there is a large flooding protection gap worldwide. Over the past 20 years, insurance has only covered 7% of total economic losses from flooding in emerging markets and 31% in advanced economies.

For 2022, it is to be expected that natural catastrophes (by definition both volatile in frequency and severity), regardless of their behavior during the year, will continue to fuel the growing trend in the cost borne by insurance and reinsurance for these catastrophes in the medium term. The insurance industry must work to better understand these events in order to be able to price them correctly and thus contribute to sustainable insurance for the benefit of the society that suffers from them.

2.2 Regulatory and supervisory trends

Report on risks and vulnerabilities in the EU financial system

On April 13, the Joint Committee of the European Supervisory Authorities (EBA, ESMA and EIOPA) released its report on risks and vulnerabilities in the EU financial system for March 2022[6]. The report highlights that Russia's invasion of Ukraine has aggravated the outlook for growth and inflation and brought heightened market volatility.

The EU economy was on track for a strong recovery from the crisis caused by the COVID-19 pandemic and the financial sector largely proved resilient. However, the recovery appears to have been hindered by new waves and variants of the virus, concerns regarding inflation risk, rising commodity prices and heightened geopolitical risks. Additional vulnerabilities and risks for the financial system have built up over time. Financial markets remain vulnerable to changes in market sentiment, particularly if financial conditions tighten unexpectedly due to inflation pressures. In the real estate sector, persistent price increases and higher borrowing by households have increased risks. At the same time, the financial sector is increasingly exposed to environmental risks and risks stemming from digitalization.

In light of the risks and uncertainties, the Committee advises national competent authorities, financial institutions and market participants to take the following policy actions:

1) Financial institutions should be prepared for further potential negative implications stemming from geopolitical tensions and ensure compliance with the sanctions regimes put in place both at the EU and at global levels.

2) Financial institutions and supervisors should prepare for a possible deterioration of asset quality in the financial sector.

3) The impact of further increases in yields and sudden reversals in risk premia on financial institutions and investors should be closely monitored.

4) Retail investors are of particular concern, and supervisors should monitor risks to retail investors seeing that their participation in financial markets has increased substantially in recent years.

5) Financial institutions should incorporate additional environmental, social and governance considerations into their business strategies and governance structures. In this regard, on March 24, 2022, the three supervisors updated their joint statement recommending that national authorities and market participants use the interim period until January 1, 2023, to prepare for the implementation of the new European Commission Delegated Regulation on the provision of sustainability-related information and taxonomy[7].

6) Considering the elevated level and frequency of cyber incidents, financial institutions should strengthen their cyber resilience and prepare for a potential increase in cyberattacks.

Tables: macroeconomic forecast scenarios

Table A-1
Baseline and Stressed Scenarios: Gross Domestic Product
(annual growth, %)

	Baseline Scenario (BS)						Stressed Scenario (SS)					
	2018	2019	2020	2021(e)	2022(f)	2023(f)	2018	2019	2020	2021(e)	2022(f)	2023(f)
United States	2.9	2.3	-3.4	5.7	3.2	1.7	2.9	2.3	-3.4	5.7	1.5	0.6
Eurozone	1.8	1.6	-6.5	5.3	2.9	2.7	1.8	1.6	-6.5	5.3	-0.3	-0.2
Germany	1.1	1.1	-4.9	2.9	2.0	3.1	1.1	1.1	-4.9	2.9	-1.3	-0.5
France	1.8	1.8	-8.0	6.3	3.2	2.2	1.8	1.8	-8.0	6.3	-1.0	-0.5
Italy	0.8	0.5	-9.1	6.6	2.9	2.2	0.8	0.5	-9.1	6.6	-0.4	-0.5
Spain	2.3	2.1	-10.8	5.0	4.2	3.0	2.3	2.1	-10.8	5.0	-0.5	-0.3
United Kingdom	1.7	1.7	-9.4	7.5	3.7	1.6	1.7	1.7	-9.4	7.5	0.9	-1.0
Japan	0.6	-0.2	-4.5	1.7	2.4	2.0	0.6	-0.2	-4.5	1.7	0.9	1.4
Emerging markets	4.5	3.7	-2.1	6.3	4.2	4.2	4.5	3.7	-2.1	6.3	2.5	3.5
Latin America[1]	1.2	0.2	-7.0	6.3	2.0	2.1	1.2	0.2	-7.0	6.3	1.0	1.1
Mexico	2.2	-0.2	-8.4	5.0	1.6	1.9	2.2	-0.2	-8.4	5.0	0.1	1.4
Brazil	1.7	1.2	-4.2	5.0	0.7	1.2	1.7	1.2	-4.2	5.0	-0.4	0.9
Argentina	-2.6	-2.0	-9.9	10.2	3.0	0.8	-2.6	-2.0	-9.9	10.2	1.6	0.0
Emerging markets, Europe[2]	3.4	2.5	-2.0	6.0	-1.4	1.9	3.4	2.5	-2.0	6.0	-2.0	1.0
Turkey	3.0	0.9	1.8	11.0	2.0	2.5	3.0	0.9	1.8	11.0	-0.2	0.4
Asia-Pacific[3]	6.4	5.4	-0.9	7.1	4.8	4.6	6.4	5.4	-0.9	7.1	3.5	3.3
China	6.7	6.0	2.2	8.1	4.8	5.3	6.7	6.0	2.2	8.1	3.7	4.8
Indonesia	5.2	5.0	-2.1	3.7	5.7	5.6	5.2	5.0	-2.1	3.7	4.2	4.7
Philippines	6.3	6.1	-9.6	5.6	6.8	5.7	6.3	6.1	-9.6	5.6	5.1	5.0
Global	3.6	2.9	-3.1	6.1	3.6	3.6	3.6	2.9	-3.1	6.1	3.2	2.6

Source: MAPFRE Economics

[1] Argentina, Brazil, Chile, Colombia, Mexico and Peru; [2] Russia, Turkey, Commonwealth of Independent States (CIS) and Central Europe; [3] Association of Southeast Asian Nations (ASEAN)
Forecast end date: April 28, 2022

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Table A-2
Baseline and stressed scenarios: inflation

(end of period, %)

	Baseline Scenario (BS)						Stressed Scenario (SS)					
	2018	2019	2020	2021(e)	2022(f)	2023(f)	2018	2019	2020	2021(e)	2022(f)	2023(f)
United States	1.9	2.3	1.4	7.0	6.9	3.0	1.9	2.3	1.4	7.0	7.3	3.8
Eurozone	1.9	1.0	-0.3	4.6	5.5	3.0	1.9	1.0	-0.3	4.6	6.0	3.5
Germany	1.6	1.5	-0.3	5.3	5.5	2.6	1.6	1.5	-0.3	5.3	7.5	3.0
France	2.1	1.3	0.5	2.0	1.6	1.7	2.1	1.3	0.5	2.0	2.1	2.8
Italy	1.1	0.5	-0.2	3.9	6.0	2.0	1.1	0.5	-0.2	3.9	8.4	3.0
Spain	1.2	0.8	-0.5	6.6	5.5	2.1	1.2	0.8	-0.5	6.6	7.0	2.6
United Kingdom	2.0	1.3	0.8	4.8	6.8	3.3	2.0	1.3	0.8	4.8	9.5	4.5
Japan	0.9	0.5	-0.9	0.5	2.0	0.9	0.9	0.5	-0.9	0.5	3.0	1.1
Emerging markets	4.9	5.1	5.1	5.5	4.9	4.3	4.9	5.1	5.1	5.5	5.3	4.4
Latin America[1]	6.6	7.7	6.4	9.3	7.8	6.0	6.6	7.7	6.4	9.3	9.0	7.0
Mexico	4.8	2.8	3.2	7.4	6.5	4.4	4.8	2.8	3.2	7.4	6.8	5.0
Brazil	3.7	4.3	4.5	10.1	7.6	4.5	3.7	4.3	4.5	10.1	8.2	4.9
Argentina	47.4	52.2	36.4	51.4	52.2	37.9	47.4	52.2	36.4	51.4	54.4	39.5
Emerging markets, Europe[2]	6.4	6.6	5.4	8.4	7.1	6.2	6.4	6.6	5.4	8.4	7.5	6.6
Turkey	20.3	11.8	14.6	36.1	52.9	16.2	20.3	11.8	14.6	36.1	59.7	17.4
Asia-Pacific[3]	2.7	3.3	3.1	2.3	2.7	2.7	2.7	3.3	3.1	2.3	3.0	3.0
China	2.2	4.3	0.1	1.8	3.0	2.4	2.2	4.3	0.1	1.8	3.8	3.7
Indonesia	3.3	2.7	1.6	1.8	4.6	3.0	3.3	2.7	1.6	1.8	6.3	3.9
Philippines	6.1	1.4	2.9	3.6	5.9	2.6	6.1	1.4	2.9	3.6	7.5	3.2
Global	3.6	3.8	2.8	6.4	6.8	4.1	3.6	3.8	2.8	6.4	7.8	4.3

Source: MAPFRE Economics

[1] Argentina, Brazil, Chile, Colombia, Mexico and Peru; [2] Russia, Turkey, Commonwealth of Independent States (CIS) and Central Europe; [3] Association of Southeast Asian Nations (ASEAN)
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Table A-3
Baseline and stressed scenarios: 10-year government bond yield
(end of period, %)

	Baseline Scenario (BS)						Stressed Scenario (SS)					
	2018	2019	2020	2021(e)	2022(f)	2023(f)	2018	2019	2020	2021(e)	2022(f)	2023(f)
United States	2.69	1.92	0.93	1.52	3.00	3.32	2.69	1.92	0.93	1.52	3.50	4.00
Eurozone	1.17	0.32	-0.19	0.32	1.20	1.85	1.17	0.32	-0.19	0.32	1.90	3.00

Source: MAPFRE Economics
Forecast end date: April 28, 2022

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Table A-4
Baseline and stressed scenarios: exchange rates
(end of period, %)

	Baseline Scenario (BS)						Stressed Scenario (SS)					
	2018	2019	2020	2021(e)	2022(f)	2023(f)	2018	2019	2020	2021(e)	2022(f)	2023(f)
USD-EUR	0.87	0.89	0.81	0.88	0.88	0.86	0.87	0.89	0.81	0.88	0.90	0.89
EUR-USD	1.15	1.12	1.23	1.13	1.13	1.16	1.15	1.12	1.23	1.13	1.11	1.12
GBP-USD	1.28	1.32	1.36	1.35	1.35	1.39	1.28	1.32	1.36	1.35	1.34	1.39
USD-JPY	110.83	109.12	103.54	115.00	113.96	109.91	110.83	109.12	103.54	115.00	115.05	110.59
USD-CNY	6.88	6.99	6.52	6.35	6.42	6.38	6.88	6.99	6.52	6.35	6.43	6.41

Source: MAPFRE Economics
Forecast end date: April 28, 2022

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Table A-5
Baseline and stressed scenarios: official benchmark interest rate
(end of period, %)

	Baseline Scenario (BS)						Stressed Scenario (SS)					
	2018	2019	2020	2021(e)	2022(f)	2023(f)	2018	2019	2020	2021(e)	2022(f)	2023(f)
United States	2.50	1.75	0.25	0.25	2.50	2.50	2.50	1.75	0.25	0.25	2.75	3.00
Eurozone	0.00	0.00	0.00	0.00	0.00	0.25	0.00	0.00	0.00	0.00	0.25	0.00
China	3.30	3.25	2.95	3.00	2.75	3.00	3.30	3.25	2.95	3.00	2.62	3.08

Source: MAPFRE Economics
Forecast end date: April 28, 2022

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4/ Chart 2.1.2 shows the minimum, average, and maximum levels reached in 2021, along with the level of the latest curves published by EIOPA for December 2021 and March 2022. In this case, as in the other insurance markets analyzed, these curves can be viewed for other months and currencies on the interactive graph. See:
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