August 2021

Global Macro Views: Read the Footnote, Every Page

The Global Macro Forum

BNY MELLON | INVESTMENT MANAGEMENT

MELLON

World

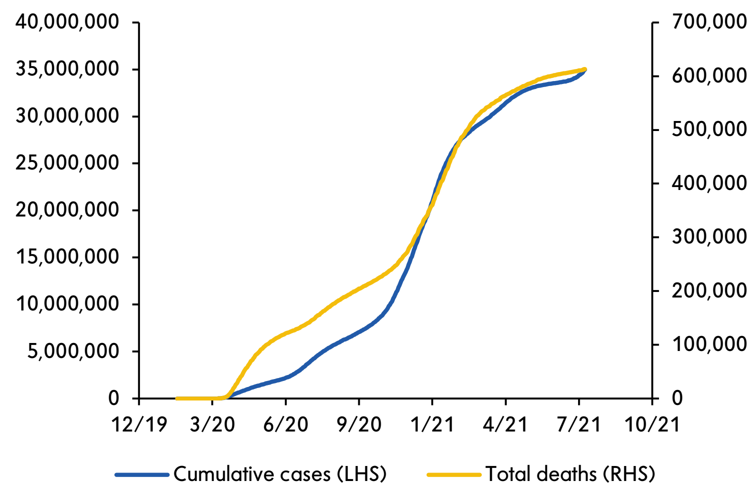
	2019	2020	2021	BoR	2022	BoR
Real GDP	2.60%	-3.70%	6.00%	–	3.60%	–
Inflation	2.60%	2.70%	3.30%	–	2.90%	–

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "^" represents a positive view, "v" represents a negative view and "—" indicates a neutral view.

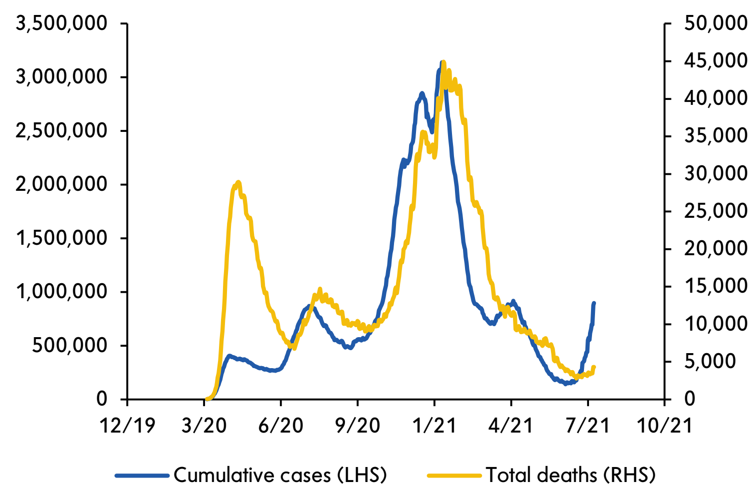
At some point, we will retire from being armchair epidemiologists, but not yet. The path of the global coronavirus pandemic continues to box about the economic outlook. However, vaccinations are proving to be a powerful counterpuncher. The herd to which the coronavirus can stalk is shrinking as the share of the population vaccinated or acquiring a natural immunity from having survived COVID rises.

Three problems intrude on the arithmetic of virus containment, which is why knocking out the virus is beyond reach. Not everyone has access to the vaccine. Not everyone with access chooses to be jabbed. And the more-infectious Delta variant of the coronavirus is the new opponent. Advanced economies have mostly gotten past the logistical hurdles that kept the first risk relevant. Vaccine hesitancy lingers around the globe, but governments and businesses are asserting themselves more to foster compliance. With healthcare resources available and greater experience in containment, the curve of confirmed COVID cases has flattened in Europe and the US. Most encouragingly, there is more white-space between new infections and mortalities.

United States
Cumulative Cases and Deaths
Number of people



14-day Change
number of people

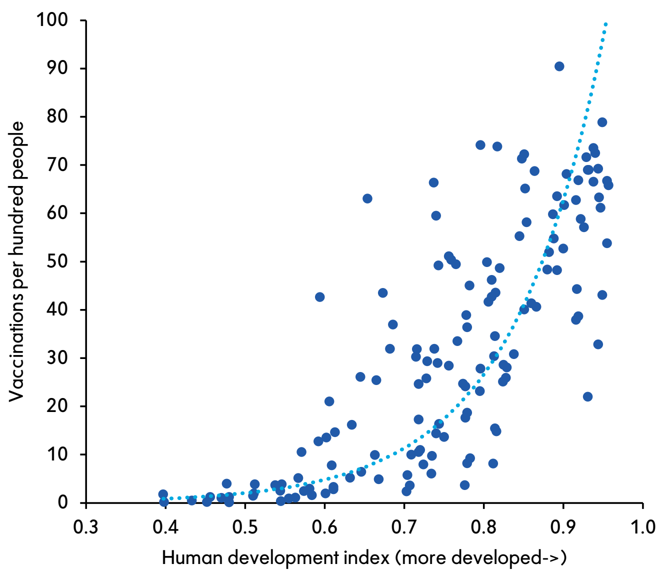


Source: Our World in Data, accessed 8/10/2021.

PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS.

Unfortunately, this is not uniformly shared, especially in Asia and South America, where vaccines are less available, and the Delta variant reaches more perniciously into their younger populations. Fundamentally, the pandemic is regressive, hitting poorer economies harder. Those places have fewer healthcare resources, their residents do not have a cushion of savings to ride out adverse times, and they rely more on the informal sector that requires physical presence to earn a living. This shows up as the sharply upward curve linking vaccination rates (on the vertical axis) and the degree of development (on the horizontal axis moving left to right from lowly to highly developed).

Vaccination Rate and Development
percent and index



People vaccinated at least once per hundred of the population

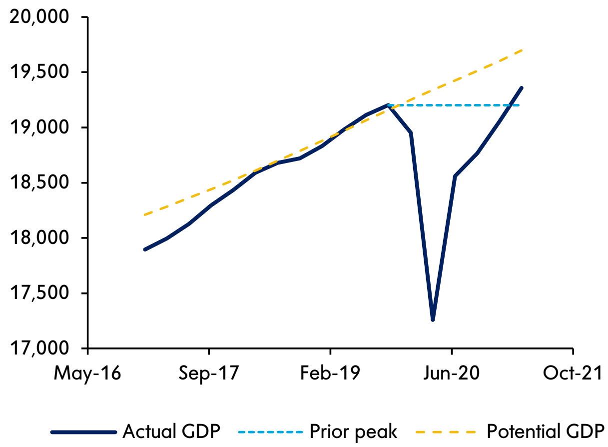
United States	57	Netherlands	69
Japan	39	Turkey	49
Germany	61	Switzerland	54
India	26	Poland	48
United Kingdom	69	Iran	9
France	62	Thailand	18
Italy	64	Sweden	63
Brazil	49	Belgium	69
Canada	72	Nigeria	
Russia	25	Austria	59
South Korea	38	Argentina	55
Spain	68	Norway	66
Mexico	36	Ireland	67
Indonesia	17	Israel	67

Source: Our World In Data, 8/1/2021.

The successful containment of the virus on the global stage requires the first portion of the curve to shift up to block the Delta variant (and worrisomely its mutating successors) from making further inroads into vulnerable herds. The unfortunate reality is that this is at least a year in the making, and, if achieved, the result will be a technical knockout in which the coronavirus remains with us but hemmed to the ropes of the ring potentially ready to re-engage. Until then, the best prospect is a split decision in which the world remains divided between haves and have-nots. In the interim, abstracting from the human toll in emerging economies, people in advanced economies will not feel at ease and global supply chains will be impaired.

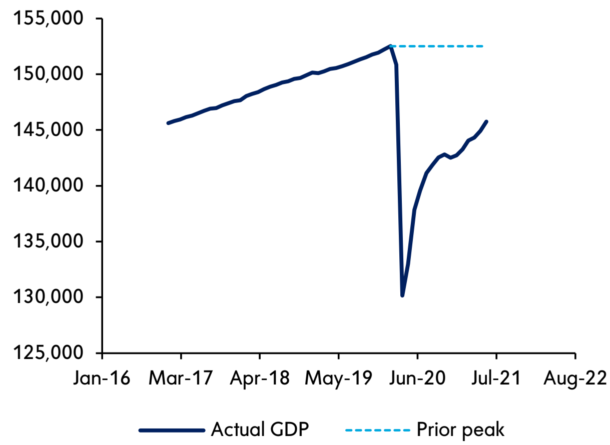
The result is a two-speed rebound, with advanced economies moving further ahead as lockdowns ease and fiscal stimulus is accommodated by central banks. The US is ahead of the pack, owing partly to progress with vaccinations and impatience with mitigation efforts and partly owing to unprecedented policy impetus. Indeed, real GDP in the second quarter reclaimed the output lost last year, although output remains below that of its trend expansion. Employment has been more sluggish to recover. After the early gains of workers returning to their previous places of employment, matching problems persist in the labor market for those seeking new jobs.

Real GDP
billions of dollars



Source: Bureau of Economic Analysis and Congressional Budget Office, accessed via FRED, 7/29/21.

Nonfarm payroll employment
thousands of workers



Source: Bureau of Labor Statistics, accessed via FRED, 7/29/21.

The latter matters most for the Federal Reserve (Fed), given the hurdle it set for itself in December that asset purchases will not slow until "substantial further progress" is made to achieving its goals of maximum employment and stable prices. The Fed is clearly treating the two goals hierarchically, determined to deal with employment first before addressing an overshoot of inflation.

Three factors bulk heavily in official thinking. First, they experimented last decade with running the labor market hot and liked the results of a 3½ percent total unemployment rate and a more equitable sharing of gains among underserved groups. Second, the trade-off between above-trend demand and inflation was decidedly and surprisingly favorable. Indeed, it was favorable enough for officials to switch from outlook-based to outcome-based policy setting. After all, if inflation did not rise as predicted by their models, then waiting for it to happen rather than merely be forecasted seems to them the prudent bet. That is, in casting economic fundamentals aside, Fed officials reject the admonition at the bottom of all our published notes that past performance is not necessarily indicative of future results. Third, they have taken to heart that their policy tools are asymmetric. Providing needed policy stimulus when the interest rate instrument is already at its zero lower bound is much more problematic than raising interest rates later if inflation should emerge.

Investors have fallen into the same mindset as Fed officials, with three lessons taking firm hold of public sentiment.

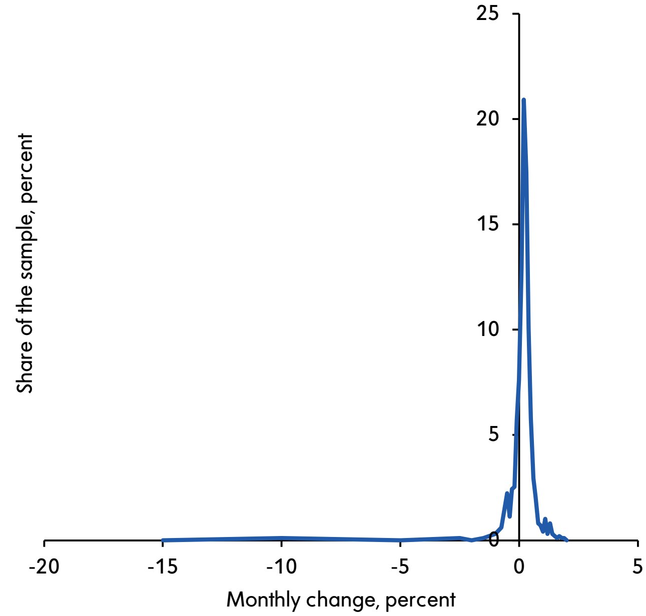
First, economic outcomes are a mixture of two distinct cases. In the benign one, the global economy fitfully makes progress toward herd immunity and those nations further along that journey perform well. In the malign case, the virus mutates to become more infectious, lengthening the trip to herd immunity and leaving containment efforts pressing down on the marketplace. This explains why news of the rise of the Delta variant set back confidence on a few occasions of late.

This property is evident in the US data over the longer haul. The chart on the right plots the distribution of monthly payroll employment growth (not annualized) for the past 82 years. Outcomes are tightly clustered around one- to three-tenths percent, which produced secular expansion of the economy. There are some modest declines, which produced recessions. And there is a far-left tail of large adverse supply shocks, small in probability weight but large in economic devastation. Economic life mixes mostly benign results and rate disasters. However, rare disasters remind investors that safe-haven Treasury yields do not need much of a term premium (perhaps even a negative one because they appreciate in value in the thin air of the left tail) and that corporate debt and equities require fattened compensation for risk. No firmer lesson has been drilled into us in the past eighteen months than bad things can happen to good people, which is why the probability of the malign case of truly adverse supply shocks is elevated and changeable to news about the virus.

Second, expectations about the fiscal policy response have ratcheted higher, especially in the US. The right hand chart plots estimates from the International Monetary Fund (IMF) of the US cyclically adjusted budget balance (or structural balance) relative to potential GDP. The structural balance controls for the effects of swings in economic activity on revenue and spending to reveal the discretionary element of policy as the remainder. Doubling-down is evident in that the discretionary worsening of the general government budget balance in downturns is twice what it was in the prior one. Fiscal authorities intend to pave any hole dug by rare disasters.

Nonfarm employment, 1939 to 2021

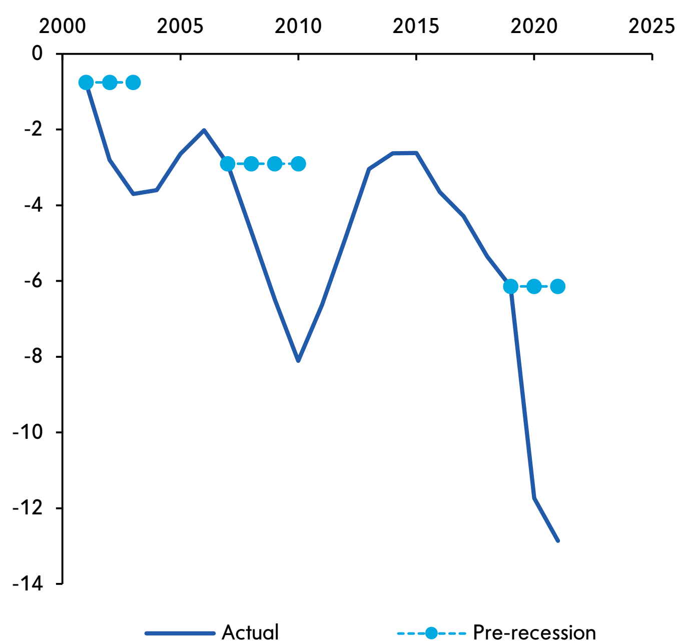
share of the sample, percent



Source: Bureau of Labor Statistics, accessed via FRED, 8/1/21.

Structural budget balance

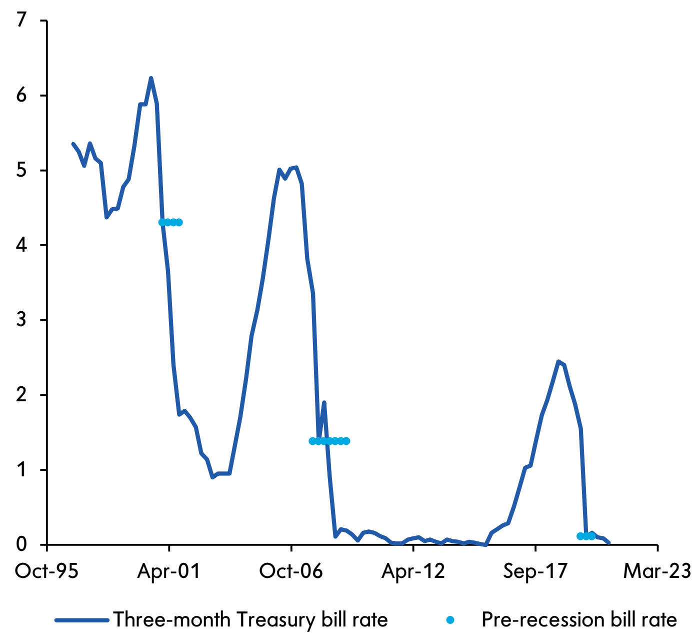
relative to potential GDP, percent



Source: International Monetary Fund, World Economic Outlook (April 2021).

Third, fiscal impetus has been fully accommodated by the Fed in the past three cycles. An indicator of the stance of monetary policy, the three-month Treasury bill rate plotted to the right, is slashed in economic downturns and stays low for a considerable time thereafter.

Three-month Treasury bill rate
percent



Source: Federal Reserve and the NBER, accessed via FRED, 7/30/21.

This increasingly full-throated fiscal response, reliably abetted by the central bank, teaches that recessions will be shorter, and rebounds will be more vigorous over time. Indeed, the results are evident in that after-tax corporate profits (on a national-income-and-product-account basis and plotted relative to nominal gross domestic income at bottom) vault above their prerecession levels each episode. The net effect has been to keep equity prices on an upward tear, risk spreads narrow, and longer-term Treasury yields low. While this has not been a bad bet based on the past three business cycles, please reread the warning at the bottom of the page.

After-tax corporate profits relative to nominal GDI
percent

Source: Bureau of Economic Analysis and the NBER, accessed via FRED, 7/30/21.

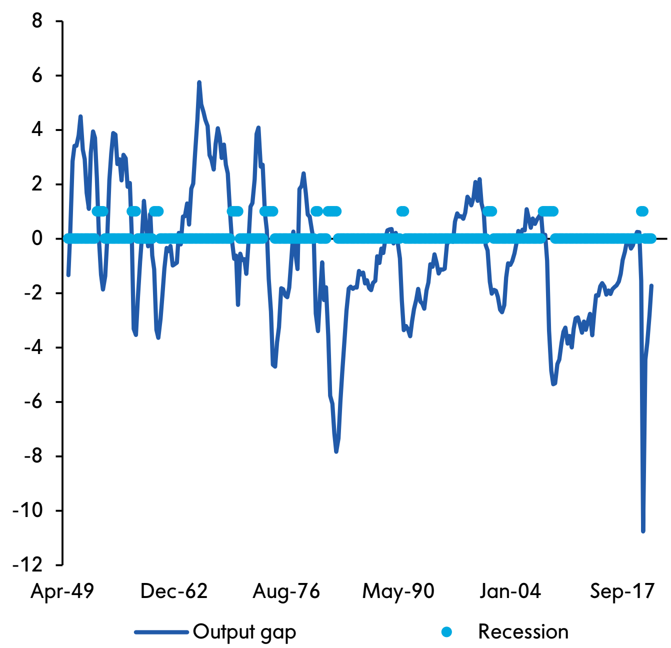
This is outcome-based investing, based on the same logic as current Fed thinking. A twice-as-vigorous policy response to any future malign event brings the benign case sooner into view, without apparently an upsurge in inflation. A lower discount rate and higher profits combine to improve equity prices, pushing the distance to default further toward the horizon. True, the principle has worked for both the Fed and investors for the past two decades. We harbor the suspicion (perhaps inculcated by the admonition at the bottom of every page we have written) that two decades do not demonstrate a trend and that doubling-down is not a strategy to follow in policymaking or at a casino.

Inflation has, in fact, emerged more dramatically and persistently than Fed officials expected. For now, the institution holds the view that the uptick is narrow and will be transitory. (Notice the irony here that their embrace of outcome-based policymaking is situational. The *outcome* of above-goal inflation does not currently trigger a response because their *outlook* is that it will be transitory.)

Supply-chain disruptions, rising commodity prices, and accelerating wages are all putting upward pressure on prices, making it increasingly difficult for the Fed to dismiss high realized inflation as transitory. Should aggregate demand growth continue to be rapid and supply-chain constraints linger, the risk of embedding the recent increase in inflation expectations will rise. This is especially so given that some of the more rapid price increases are in categories with notable persistence (owners-equivalent rents) and salient to households (energy and food away from home).[1]

We think that the Fed is on the wrong side of history and inflation will linger longer and higher above their goals of 2 percent than they assert. But, the Fed will wait for a convincing demonstration of this before responding. The place to watch, in the meantime, is expectations of inflation and actual wages. If they do move persistently higher, a longer-term relationship will reassert itself in the next few years. As in the chart to the right, one of the best predictors of cyclical downturns (the dots denoting quarters when the US is in recession) is the current state of resource utilization (plotted along the vertical axis as actual real GDP relative to its potential level). When resources are stretched, as they will be starting next year, the Fed struggles to catch up by raising the policy rate in real terms and economic performance suffers. Medium-term policymaking and investing should look forward to that outlook, not backward to outcomes.

GDP relative to potential GDP
percent



Source: Bureau of Economic Analysis, Congressional Budget Office, and the NBER, accessed via FRED, 8/1/21.

This dynamic recurs around the globe. The economic outlook for European growth continues to brighten, and we expect the European economy to narrow the growth gap between it and the rest of the developed world in the second half of the year. While the rebound to date has lagged peers, the belated delivery of fiscal stimulus and coronavirus vaccines should drive growth meaningfully higher in the coming months. With a great deal of slack left in the labor market, the European Central Bank (ECB) will endeavor to keep yields low, the Eurodollar exchange rate weak, and spreads tight as the Fed moves toward tapering its asset purchases next year.

In contrast to the relatively synchronous rebound evidenced in developed markets, the outlook for economic activity and the stances of monetary policy in Emerging Markets vary widely. Strong Chinese, US, and now, European growth should provide a supportive global demand environment, but domestic conditions vary greatly. In China, administrative tightening has slowed the growth of credit as authorities work to stabilize growth at slightly above trend. As a rule, the markets of North Asia are on sound macro-economic footing with well anchored inflation expectations and are positioned to benefit from strong US and European demand. Eastern Europe faces a similar outlook as tight trade ties with the Eurozone and established inflation-targeting frameworks will help them avoid being forced into pro-cyclical monetary policy firming.

Other Emerging Markets, primary those of South Asia and Latin America, have been forced to hike rates as currency depreciation drove realized and expected inflation higher. Looking forward, we expect further policy differentiation between emerging markets as countries with established inflation targeting frameworks outperform those without. Credit quality and elevated government debt levels is a potential medium-term issue as the appetite for "post-crisis" fiscal consolidation is low.

Japan

	2019	2020	2021	BoR	2022	BoR
Real GDP	0.8%	-4.8%	3.0%	–	2.5%	–
Inflation	0.8%	-0.2%	0.0%	–	0.5%	–

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "⮝" represents a positive view, "⮟" represents a negative view and "—" indicates a neutral view.

Japan's manufacturing and export sector are poised to be the key drivers of its economy in 2021. However, recent supply-side disruptions, notably the chip shortage exacerbated by a factory fire in March, has acted as a drag on the recovery, particularly in the auto sector. Despite these setbacks, the recent Tanka business survey was solid and demand appears to be well supported. While the recovery may be choppy and challenged by supply-side issues, it is at least headed in the right direction.

Another state of emergency acted as a drag on Japan's consumption recovery in the second quarter. That said, the vaccine rollout is accelerating, on course for 50% of the population to be vaccinated by mid-September. Signs of an upturn in consumer sentiment will likely boost spending from late June. The Tokyo Olympics will be an important event for the political fortunes of Prime Minister Suga, who is on thin ice with his electorate.

Inflationary pressures are very subdued and we forecast no headline inflation in 2021. Core inflation should very gradually lift in 2022, but still remain far off the Bank of Japan's (BoJ) 2 percent inflation target. The BoJ will remain highly accommodative. It's recent policy review left yield curve control and quantitative easing (QE) programs largely unchanged and in place, while providing some operational tweaks.

Australia

	2019	2020	2021	BoR	2022	BoR
Real GDP	1.6%	-2.4%	5.2%	⮝	3.3%	–
Inflation	1.5%	0.9%	2.1%	⮝	1.9%	⮝

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "⮝" represents a positive view, "⮟" represents a negative view and "—" indicates a neutral view.

Global activity and prices have moved higher since we last met and so have our forecasts for the economies of Australia and New Zealand. In Australia, the labor market is adding jobs at an exceptional clip, far outpacing both private sector and policymaker forecasts. While underlying inflation has yet to meaningfully accelerate, the pace at which labor market slack is being absorbed has begun to create wage pressures within the Australian economy. While a recent outbreak of the Delta variant participated a new round of lockdowns, we think this downside risk will subside over the medium-term once enough of the population has been vaccinated. In recent meetings, the Reserve Bank of Australia (RBA) maintained monetary policy accommodation and forward guidance. However, policy is becoming incrementally less dovish. At its July meeting, the RBA did not extend its 3-year yield target; therefore, as time passes, the maturity of the yield target will naturally decline. The bond purchase program was extended but at a slightly tapered purchasing pace and with more frequent reviews than the previous announcements of 5- to 6-month envelopes of bond purchases. We believe that conditions to tighten monetary policy will be met by 2023, resulting in the RBA raising its policy rate ahead of the current timeline.

In New Zealand, cost pressures are building and inflation is close to achieving the central bank's target. A recent business survey indicated growing business optimism, labor shortages, and cost pressures. The Reserve Bank of New Zealand (RBNZ) has pulled forward its timed exit from policy accommodation to next year. We anticipate RBNZ tightening to commence in the first half of 2022.

Emerging Markets

Asia

China

	2019	2020	2021	BoR	2022	BoR
Real GDP	6.1%	2.3%	8.4%	⌄	5.4%	–
Inflation	2.9%	2.4%	1.6%	–	2.1%	⌄

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "⌃" represents a positive view, "⌄" represents a negative view and "—" indicates a neutral view.

We maintain our 8.4% annual growth forecast for this year alongside 1.6% annual consumer price inflation, but downside risks are coming into view which call for a prolonged hold (and a neutral bias) in macro policies.

After standing out as the only major economy with any growth in 2020, China's macro exceptionalism is past its prime. On a sequential basis, after a sharp rebound in late 2020 and earlier this year, China's growth rate is now tracking a (slower) 5% to 5.5% seasonally adjusted annual rate. This is because policy induced headwinds to growth are intensifying and COVID infections continue to flare up sporadically with herd immunity not in sight until year-end. Moreover, external demand could be peaking—especially as rapidly recovering developed markets (DMs) pivot toward services and away from China's COVID-related exports of medical supplies and electronics.

Chinese policymakers have used the post-pandemic growth rebound to refocus on medium-term risks. They continue to crack down on shadow-banking, whilst initiating new restrictions on real-estate lending and also reining in the fin-tech sector and curtailing local government borrowing. Tightening regulations in these areas emanate from the authorities' eagerness to rein in financial risks, stabilize contingent fiscal liabilities, dismantle (private) monopolies in the tech sector and lower the credit intensity of medium-term growth. As a result, the credit impulse has contracted even before services activity and the consumption side of China's economy have normalized and managed to catch up to the production side of GDP.

What's more, household income growth remains slower than its pre-pandemic rate as profit-margins and labor-incomes remain squeezed. Due, in part, to more restrained fiscal transfers to and social spending on households in China than most DMs and many advanced EMs. Another contributing factor is the resurgence of COVID-19 infections, including more contagious variants, in several parts of the country. Although these breakouts have been well contained, by extensive testing, targeted lockdowns and an acceleration of vaccinations, it has weighed on several domestic sectors ranging from box-office sales, to catering and internal travel and tourism.

The waning cyclical momentum is increasingly evidenced from easing PMIs, a slowing trend in fixed asset investment, as well as in monetary aggregates. Non-food inflation remains subdued and the unusually low pass-through of elevated commodity and upstream price pressure to retail price indices highlights a combination of weak downstream demand, or heightened manufacturing competition, and pricing power erosion.

In view of the sequential loss of macro momentum, we expect the People's Bank to adhere to its "no sharp shifts in policies" through early 2022, and maintain ample onshore liquidity. Moreover, the likelihood is rising of bringing forward some central- and local-government spending to provide a near-term impulse to the economy. The pace of vaccinations could also be sped up to incorporate booster-doses and counter any short-comings on the way to timely herd immunity ahead of the scheduled Winter Olympics in February 2022.

Other issues that could impact market sentiment and macro outcomes are China's increasingly discordant relationship with the US and many other advanced economies. The Biden Administration's coalition-building approach and bi-partisan support for a strategic pushback against China has begun fraying cross-border manufacturing foreign direct investment (FDI) and technology linkages, and it has sharpened tensions across a host of geo-political issues. For now, barring a few exceptions and entities, they do not pose a major risk to trade or capital raising and the increasing shift of global finance into onshore Chinese markets.

South Korea

	2019	2020	2021	BoR	2022	BoR
Real GDP	1.9%	-1.0%	4.0%	⮝	3.0%	⮟
Inflation	0.5%	0.5%	2.0%	⮝	1.5%	–

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "⮝" represents a positive view, "⮟" represents a negative view and "—" indicates a neutral view.

In our view, Korea's economy is poised to grow by an above trend rate in this year and the next. The Bank of Korea (BOK) will be the first central bank in Asia to kick off policy normalization. We have nudged up our growth and inflation forecasts for 2021 and 2022, and we now expect at least two 25 basis point rate hikes to take the policy rate to 1.00% by the end of 2022. The main driver of Korea's improved macro outlook is its burgeoning exports, led by semiconductors and electronics. The spike in semiconductor prices, resulting from global shortages, has tilted the terms of trade in favor of Korean chipmakers. The government's elevated spending and reasonably well managed lockdowns have put a floor beneath easing in private consumption. The pace of vaccinations is picking up and herd immunity is expected by the end of this year. Looking ahead, we expect pent-up consumption demand and savings to come to the fore as the economy progressively opens up. Increased fiscal spending in the coming two quarters, ahead of national elections in the first quarter of 2022, will provide an additional potential impetus to growth. Ongoing reflation will underpin the BOK's exit from highly accommodative policies. This would also accord with the central bank's well known concern about financial stability emanating from rising property prices and household debt. All that said, policy rate hikes by the central bank will be gradual and well telegraphed. This is because, outside of the semi-conductor sector, macro conditions are still fragile and any rapid or abrupt rate hikes would be damaging, in particular, for increasingly leveraged household balance sheets.

India

	2019	2020	2021	BoR	2022	BoR
Real GDP	5.1%	-7.0%	9.0%	–	6.5%	⌄
Inflation	3.3%	6.5%	5.9%	^	5.6%	^

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "^" represents a positive view, "⌄" represents a negative view and "—" indicates a neutral view.

India's growth outlook is stabilizing around 9% this year, as the second round of COVID-19 infections is abating and lockdowns are steadily easing. However, the inflation outlook is worsening and risks are tilted higher this year and the next. Even with a sharp curtailment of activity this past April-May, as the Delta variant flared-up, the pass-through of elevated upstream prices has been much more rapid to the retail level. Aside from high commodity and import price pressure, this highlights the drawbacks of hiking excise taxes on fuel and petroleum products and the slow re-imbursement of general sales tax (GST) refunds due unto to small- and medium-size enterprises, whose distressed margins may have intensified the price pass-through. Looking ahead, as the economy gradually normalizes, the main risk is that rapidly shrinking output gaps and negative real short-term rates un-anchor inflation expectations. Our base case is that a pullback in yearly increases in commodity and oil prices will help. But even then, inflation in India is poised to hover at the upper end of the Reserve Bank of India's (RBI) 2 percent to 6 percent inflation target range and may necessitate a much larger hike in rates by the RBI than has been priced in.

Latin America

Economic activity has been more resilient to mobility restrictions in 2021 than during the previous year. Households and companies have adapted slightly better to lockdowns, and the anticipated slowdown was less severe. Also, against our own expectations, several countries like Chile, Colombia and Peru extended fiscal stimulus at least until the end of the year. Higher commodity prices and wage remittances further supported the economic rebound. Therefore, we increased our GDP growth forecast for the whole region to 6.0% from 4.3% previously.

We continue to think that economic recovery in the region will take several years and, excluding Chile and likely Brazil, most countries will not return to pre-pandemic levels before 2023 due to fiscal constraints, low investment-to-GDP, and still weak labor markets.

Inflation is currently the top concern, and it will likely keep policymakers vigilant. Capacity constraints in several services and an unexpected rise in the demand for durable goods have joined higher food and energy price pressures. In many cases, inflation will likely be above targets for a considerable period of time.

Idiosyncratic political risk has intensified amid severe socioeconomic damages generated by the pandemic. The Andean region has been volatile and the most recent political events in Chile, Colombia and Peru suggest an increasing risk to sound macro policies. The agenda in the second half of the year remains crowded with electoral processes in Argentina and Chile, along with social protests in Colombia.

Brazil

	2019	2020	2021	BoR	2022	BoR
Real GDP	1.0%	-4.1%	5.1%	-	2.3%	⮝
Inflation	3.7%	3.2%	7.0%	⮝	4.5%	⮝

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "⮝" represents a positive view, "⮟" represents a negative view and "—" indicates a neutral view.

The Brazilian economy had a much better performance in the first quarter despite mobility restrictions. Brazilians have adapted better to lockdowns and the economy expanded 1.2% on a sequential basis. The extension of the emergency aid, still loose monetary conditions, and higher terms of trade are boosting the economy. GDP growth likely slowed in the second quarter, but we see growth accelerating in the second half of the year, supported by a faster government vaccine rollout. We expect Brazil to grow 5.1% in 2021. Inflation pressures have intensified and been more persistent than previously anticipated. Inflation is well above the 3.75 percent target, driven by food, energy, currency depreciation and, most recently, some services. Headline inflation rebounded from 1.9 percent year-over-year in August to 8.1 percent in May and will likely peak in the third quarter at 8.5 percent. We expect inflation to remain above the central bank's target, at least during the next 12 months. The central bank has turned more hawkish and started a tightening cycle directed at reducing monetary stimulus by the end of 2021. The central bank has hiked its policy rate by 225bps to 4.25%, and we see another 225bps to 6.5% by year end.

On the fiscal side, the acceleration of infections in the first half of the year led the Bolsonaro Administration to extend the fiscal stimulus up to the third quarter. This extra-spending has been excluded from the spending cap for the second consecutive year. However, fiscal balance results have surprised on the positive side as the mix of higher-than-expected growth and inflation boosted government revenues, and efforts to contain the wage bill and pensions reduced the primary deficit to 5.0% from 9.0% in the first half of the year. The structural reforms agenda is gradually gaining traction. External accounts in Brazil continue to improve, supported by favorable terms of trade. Brazil's current account deficit dropped to 0.5 percent of GDP in the twelve months to May 2021 from 2.8 percent at the end of 2019. We expect the current account deficit to end at 0.6 percent of GDP in 2021.

Mexico

	2019	2020	2021	BoR	2022	BoR
Real GDP	-0.1%	-8.2%	5.5%	⮝	2.5%	-
Inflation	3.6%	3.4%	5.0%	⮝	3.5%	-

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "⮝" represents a positive view, "⮟" represents a negative view and "—" indicates a neutral view.

Growth in Mexico surprised to the upside, fueled by net exports, remittances and the reopening economy. We recently increased our GDP forecast for 2021 to 5.5 percent from 4.0 percent. Inflation pressures have been more persistent due to higher energy prices, food, durable goods and, most recently, core services that were affected by capacity constraints. Headline Inflation has accelerated to 6.0 percent and core has been persistently above 4.0 percent. We expect inflation to gradually fall to 5.5 percent at the end of the year. We revise average inflation in 2021 to 5.2 percent from 3.9 percent before. The Central Bank of Mexico (Banxico) increased its policy rate by 25bps in June to 4.25 percent and further rate hikes will be data dependent.

We expect a current account surplus of 1.0 percent of GDP in 2021, down from a 2.4 percent deficit in 2020. Net exports and remittances helped improve the current account during the pandemic and have offset capital outflows from the government debt market.

Fiscal austerity will continue in 2021, and we see a reduction of the fiscal deficit to 2.7 percent of GDP in 2021 from 3.9 percent in 2020. We project debt-to-GDP ratio to stabilize at 53 percent in 2021 after jumping 8 points between 2019 and 2020.

Developed Markets

United States

	2019	2020	2021	BoR	2022	BoR
Real GDP	2.3%	-3.1%	6.5%	–	2.9%	–
Inflation	1.8%	1.1%	4.5%	⮝	3.5%	⮝

Western Europe

Euro Area

	2019	2020	2021	BoR	2022	BoR
Real GDP	1.1%	-9.0%	5.0%	⮟	3.0%	⮟
Inflation	1.2%	0.4%	2.0%	–	1.6%	–

United Kingdom

	2019	2020	2021	BoR	2022	BoR
Real GDP	1.2%	-10.0%	6.2%	⮟	3.0%	⮟
Inflation	1.9%	0.8%	1.4%	–	1.6%	–

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "⮝" represents a positive view, "⮟" represents a negative view and "—" indicates a neutral view.

Russia, Turkey, South Africa, CEEMEA

Russia

	2019	2020	2021	BoR	2022	BoR
Real GDP	1.2%	-4.0%	3.0%	⮟	1.5%	⮟
Inflation	4.2%	3.5%	3.5%	–	3.3%	–

Turkey

	2019	2020	2021	BoR	2022	BoR
Real GDP	0.5%	0.0%	3.5%	⮟	4.0%	⮟
Inflation	15.0%	12.0%	11.0%	–	11.0%	–

South Africa

	2019	2020	2021	BoR	2022	BoR
Real GDP	0.4%	-7.0%	3.0%	⮟	1.5%	⮟
Inflation	4.1%	3.5%	3.5%	–	3.5%	–

Poland

	2019	2020	2021	BoR	2022	BoR
Real GDP	4.2%	-3.5%	4.5%	⮟	4.0%	⮟
Inflation	2.2%	3.0%	2.2%	–	2.5%	–

Source: Firm analysis as of July 6, 2021. 2021 and 2022 are forecasts. BoR (Balance of Risks): Indicates bias relative to our forecasts as new information becomes available. "⮝" represents a positive view, "⮟" represents a negative view and "—" indicates a neutral view.

The Global Macro Forum

Alejandro Martinez Cruz
Vice President, Emerging Market Economist

Alejandro is an emerging market economist with a particular focus on Latin American countries. He provides macro views, insights and trade recommendations based on his analysis of economic, statistical and socioeconomic data, which inform the investment decisions of the Emerging Market Debt team.

Prior to joining the firm, Alejandro held several senior roles at HSBC, including a Mexico rates and foreign exchange analyst, senior LatAm strategist and the Head of Latin American Fixed Income Research. In the latter role he led fixed income research efforts for Argentina, Brazil, Chile, Colombia, Mexico, Peru, Ecuador, Dominican Republic and Costa Rica. Previously, he was an economist for Citigroup, and a currency and local rates market analyst at the Bank of Mexico. Alejandro has been in the investment industry since 1998.

Alejandro earned a degree in economics from Instituto Tecnológico y de Estudios Superiores de Monterrey and a masters in economics from the University of Rochester.

Aninda Sankar Mitra
Vice President, Senior Sovereign Analyst

Aninda is senior sovereign analyst of BNY Mellon Investment Management Singapore Pte. Ltd and provides non-discretionary research or discretionary investment management services to the firm as a subadvisor. He is responsible for Asia ex-Japan sovereign debt research. Aninda joined in March 2014 from Fitch Ratings Credit Wire Service where he served as senior director Asia Pacific. Aninda was previously Head of Southeast Asia Economics at ANZ Bank and Senior Sovereign Analyst at Moody's in Singapore and New York.

Aninda holds a MA Economics from University of North Carolina and a BS Economics (Magna Cum Laude) from Bridgewater College. Aninda has over 22 years of experience as a sovereign analyst and economist focused on Asia.

Vincent Reinhart
Managing Director, Chief Economist & Macro Strategist

Vincent is Mellon's Chief Economist and Macro Strategist. In this role, he is responsible for developing views on the global economy and making relative value recommendations across global bond markets, currencies and sectors.

Previously, Vincent served as the Chief US Economist and a managing director at Morgan Stanley. For the prior four years, he was a resident scholar at the American Enterprise Institute (AEI). Vincent also worked in several roles at the Federal Reserve over 24 years, including Director of the Division of Monetary Affairs and Secretary and Economist of the Federal Open Market Committee (FOMC). His responsibilities at the Federal Reserve included directing research and analysis of monetary policy strategies and the conduct of policy through open market operations, discount window lending and reserve requirements. Prior to these roles, he was the principal liaison with the domestic desk at the Federal Reserve Bank of New York and was responsible for preparing a document outlining policy alternatives for each FOMC meeting. He was Deputy Director in the Division of International Finance and Associate Economist of the FOMC and spent five years at the Federal Reserve Bank of New York in both the domestic and international research departments.

His academic publications primarily concern the conduct of policy and issues related to the monetary transmission mechanism as well as an analysis of alternative auction techniques and Treasury debt management. After an undergraduate training at Fordham University, he received graduate degrees in economics at Columbia University.

Nicholas Tocchio
Sovereign Analyst

Nick is a sovereign analyst contributing to interest rate and currency strategy for global portfolios. He is responsible for fundamental credit and market analysis for Australia, Canada and New Zealand. Nick joined the firm in 2013 and holds a BA in Economics from Hamilton College. He has been in the investment industry since 2013.

Endnotes

[1]To be clear, Fed officials are correct that base effects and bottlenecks currently adding to inflation are transitory. However, because we think that they will be larger and last longer than the Fed expects, they will become more permanently embedded into inflation expectations.

Disclosure

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