



Entrapment

Financial crisis or stagflation?

From the nasty dilemma of stagflation...

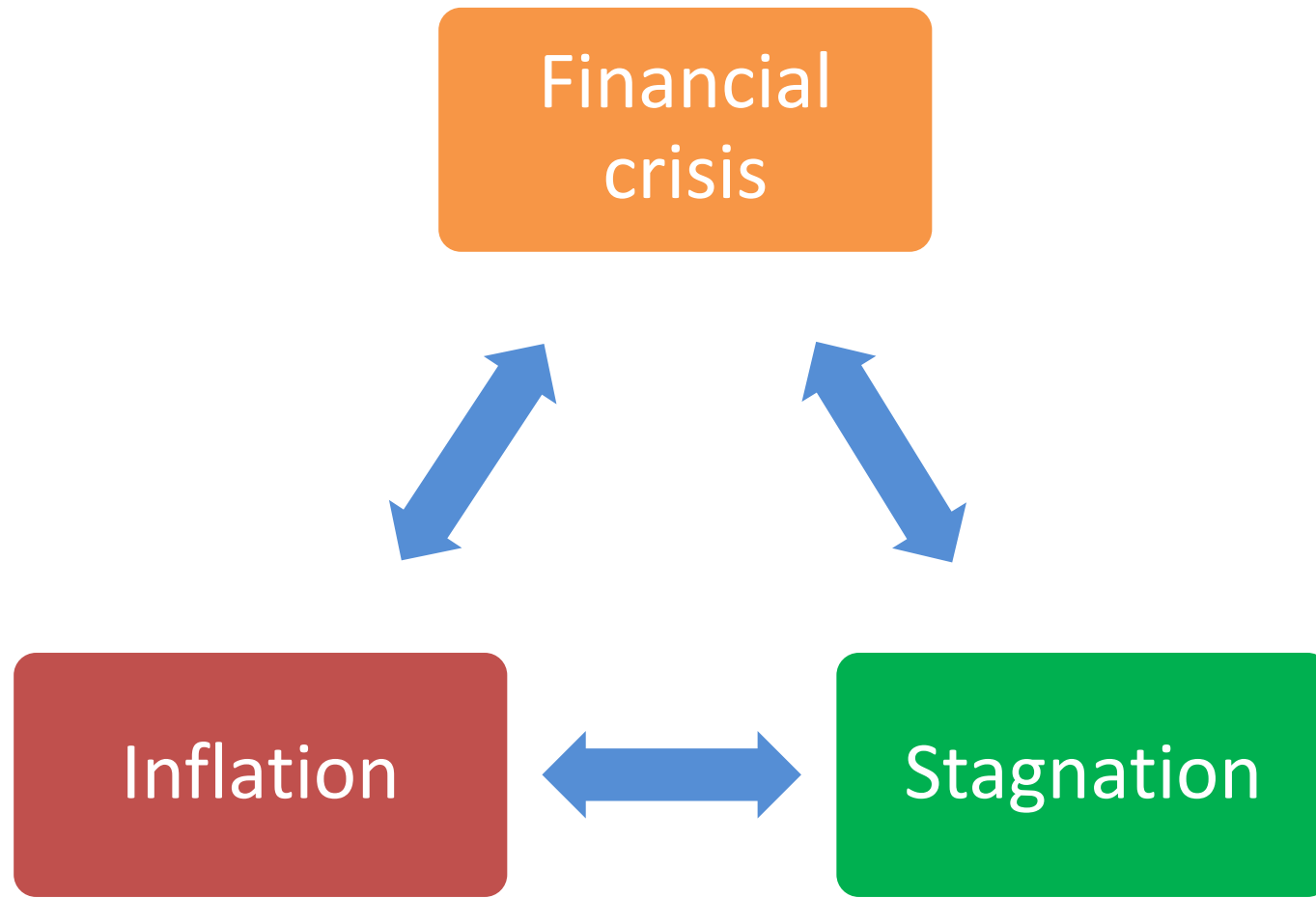
Stagnation



Inflation

Combating inflation with higher interest rates, creating a (too mild) recession and not doing enough, means ending up with stagflation

... to an even more nasty tri-lemma

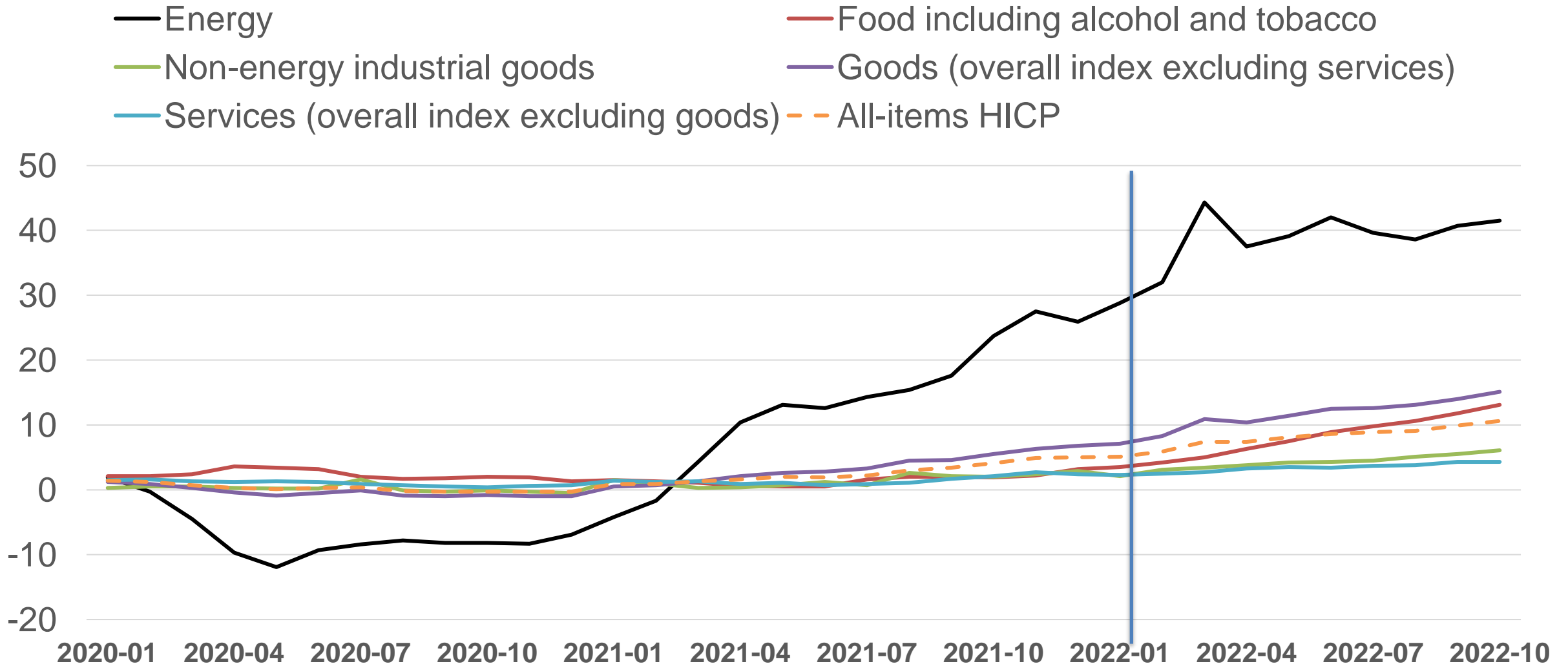




1. An energy crisis is not a pandemic



Inflation mainly driven by energy prices...



Eurostat

An energy crisis is not a pandemic



Inflation creates a totally different policy environment

= no massive bond buying schemes

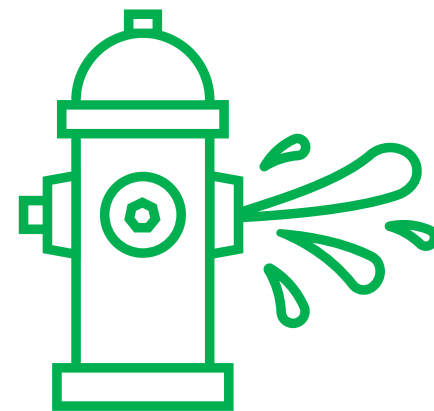
= no private debt moratoria

= fiscal prudence and consolidation

Unless a full blown banking crisis changes all that?

2. A welfare leak

Europe pays the price



Zoom 6m YTD 1y **5y** 10y All



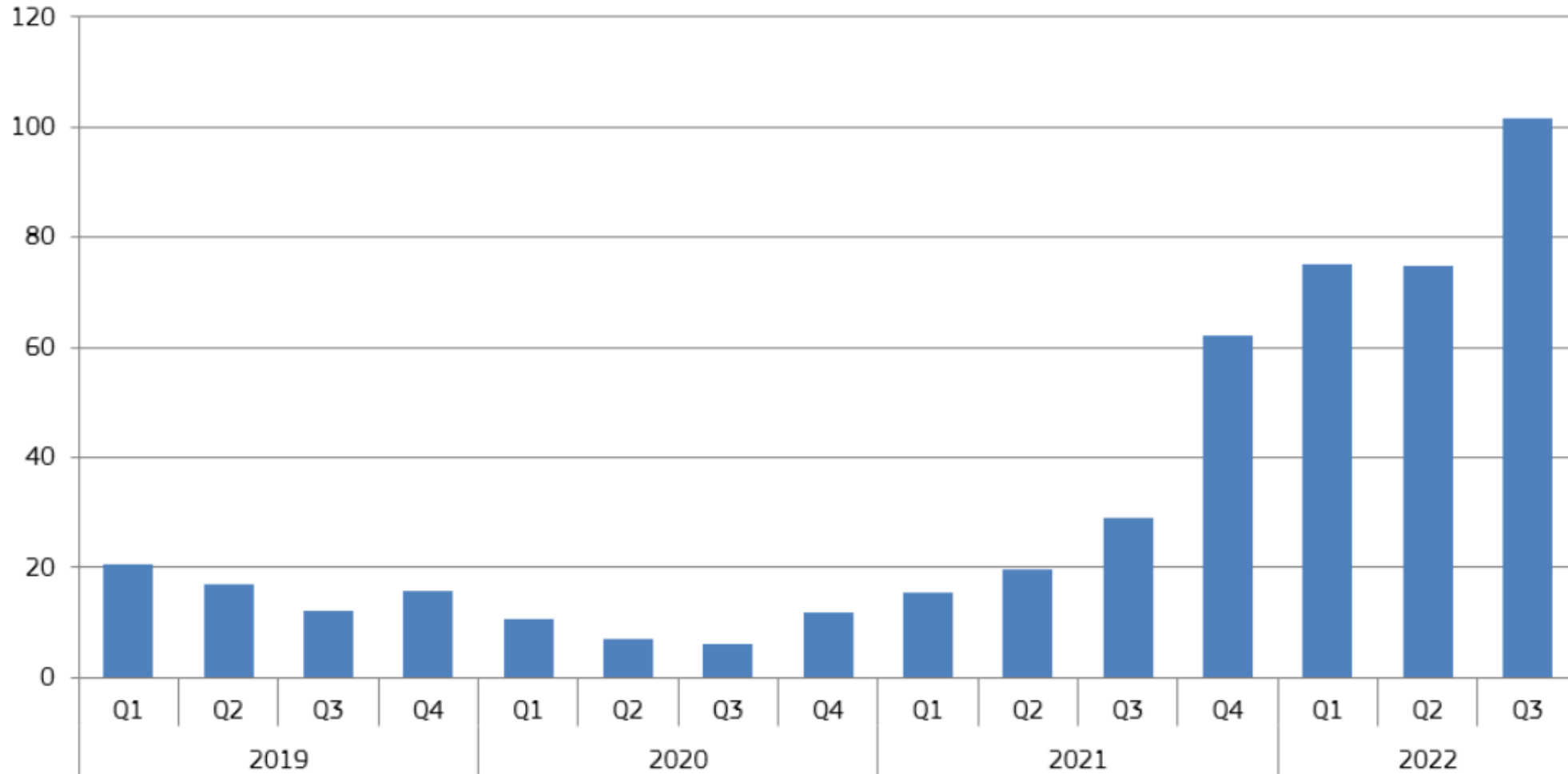
MacroMicro

美元/百萬英熱單位



- NYMEX-Henry Hub Natural Gas Futures Price
- CME-Dutch TTF Natural Gas (USD/MMBtu) (ICIS Heren) Front Month Futures Price
- CMEUK NBP NATURAL GAS (USD/MMBTU) (ICIS HEREN) Front Month Futures Price
- CME-LNG Japan/Korea Marker Platts Futures Price

Extra-EU gas import bill (bn euros)



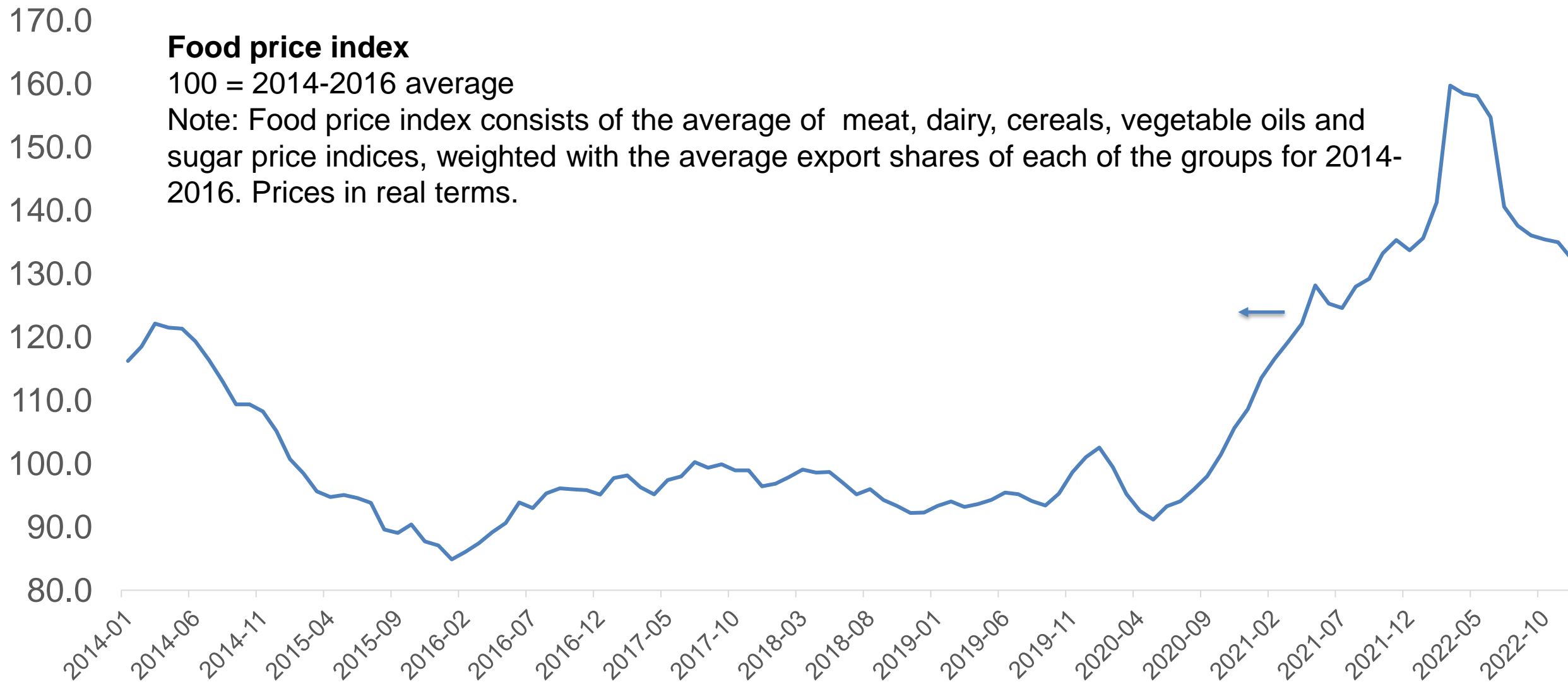
Source: ENTSO-G, Eurostat and own data calculations for the EU weighted average of import gas prices

Food crisis

Food price index

100 = 2014-2016 average

Note: Food price index consists of the average of meat, dairy, cereals, vegetable oils and sugar price indices, weighted with the average export shares of each of the groups for 2014-2016. Prices in real terms.



Bron: FAO (UNO)



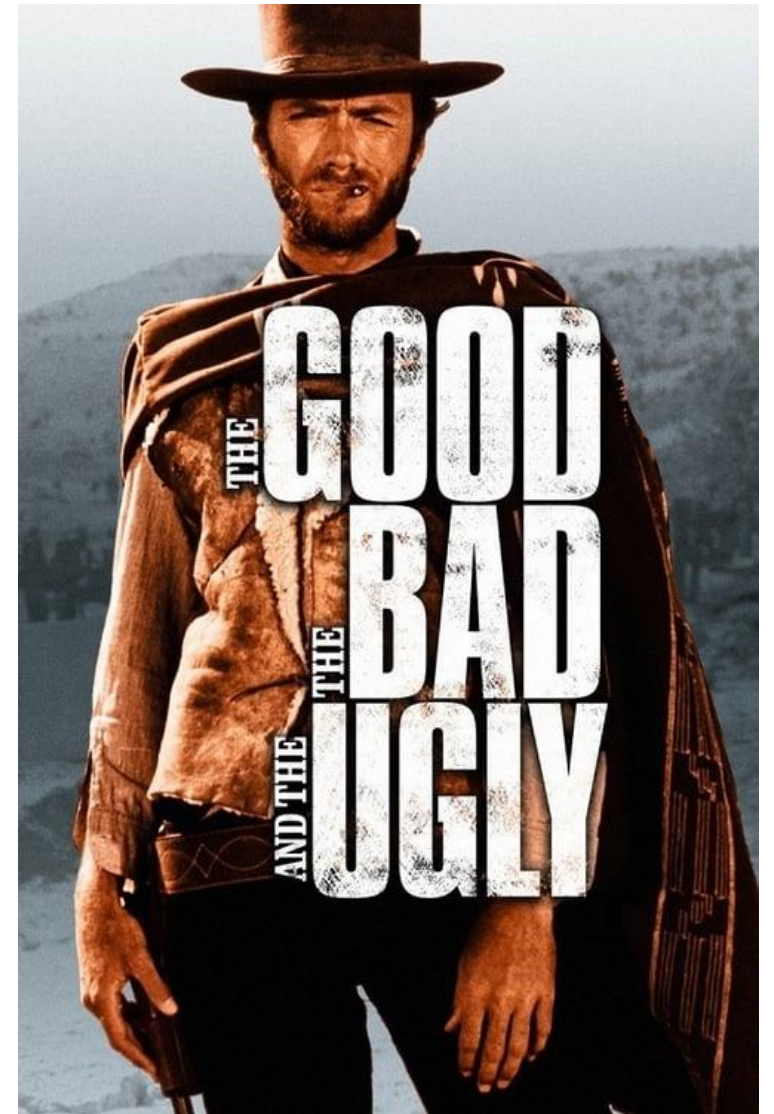
‘The dollar is our currency
and your problem’
John Connally, 1971

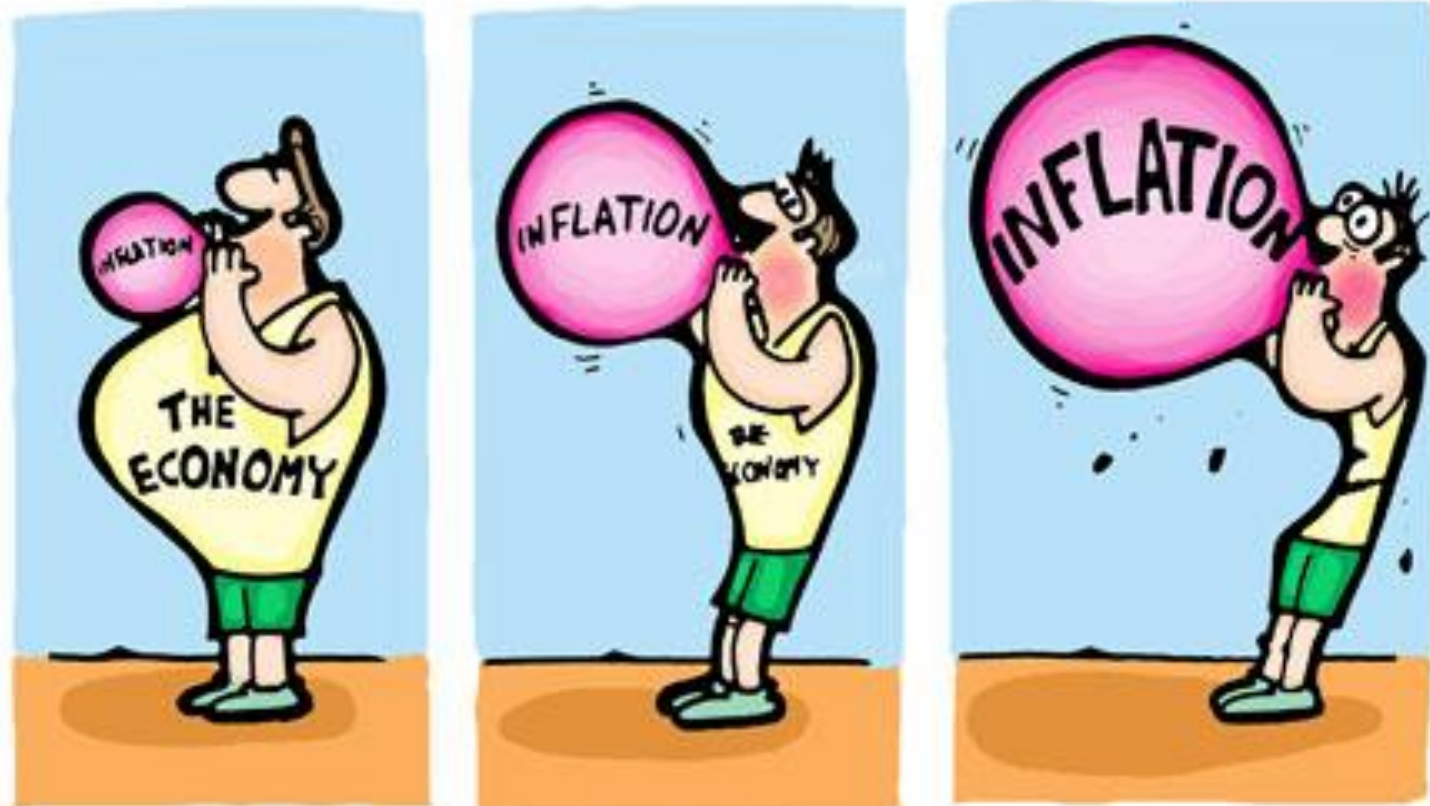


Back to the future?

Are we heading back to the 1970s?

3. The good, the bad and the ugly





2008-004 © INKCINCT Cartoons www.inkcinct.com.au

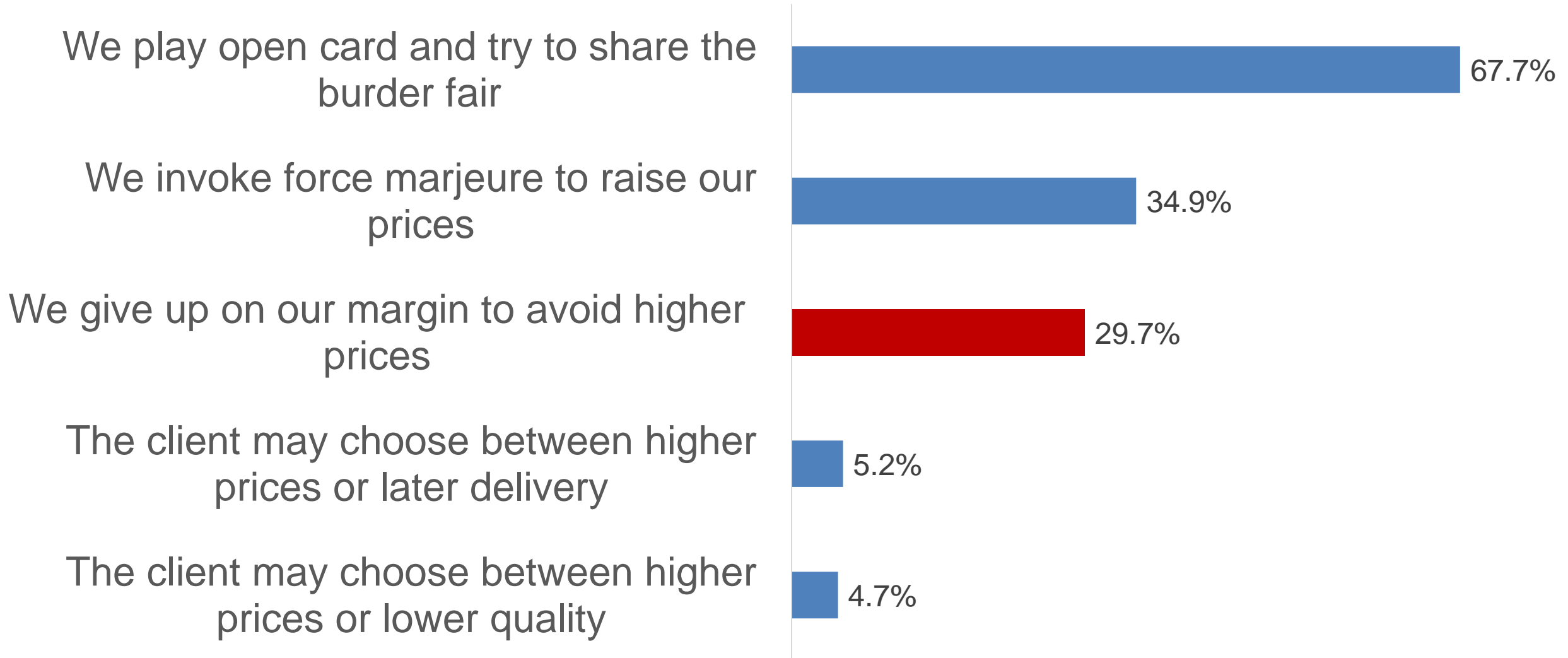
INKCINCT

Disruptions from inflation can lead to stagnation = stagflation

	Average 60's	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	Average 80's
Belgium	2,6	3,9	4,3	5,4	7,0	12,7	12,8	9,1	7,1	4,5	4,5	4,9
France	3,9	5,3	5,4	6,1	7,4	13,6	11,7	9,6	9,5	9,3	10,6	7,4
West-Germany	2,4	3,5	5,2	5,5	7,0	7,0	5,9	4,2	3,7	2,7	4,0	2,9
Japan	5,3	6,8	6,3	4,9	11,7	23,2	11,7	9,4	8,1	4,2	3,7	2,5
Netherlands	4,0	3,7	7,5	7,8	8,0	9,6	10,2	8,8	6,4	4,1	4,2	2,9
UK	3,5	6,4	9,4	7,1	9,2	16,0	24,2	16,6	15,8	8,3	13,4	7,2
US	2,3	5,8	4,3	3,3	6,2	11,1	9,1	5,7	6,5	7,6	11,3	5,6

Persistently high inflation creates transaction costs and distorts the price mechanism and finally the economy

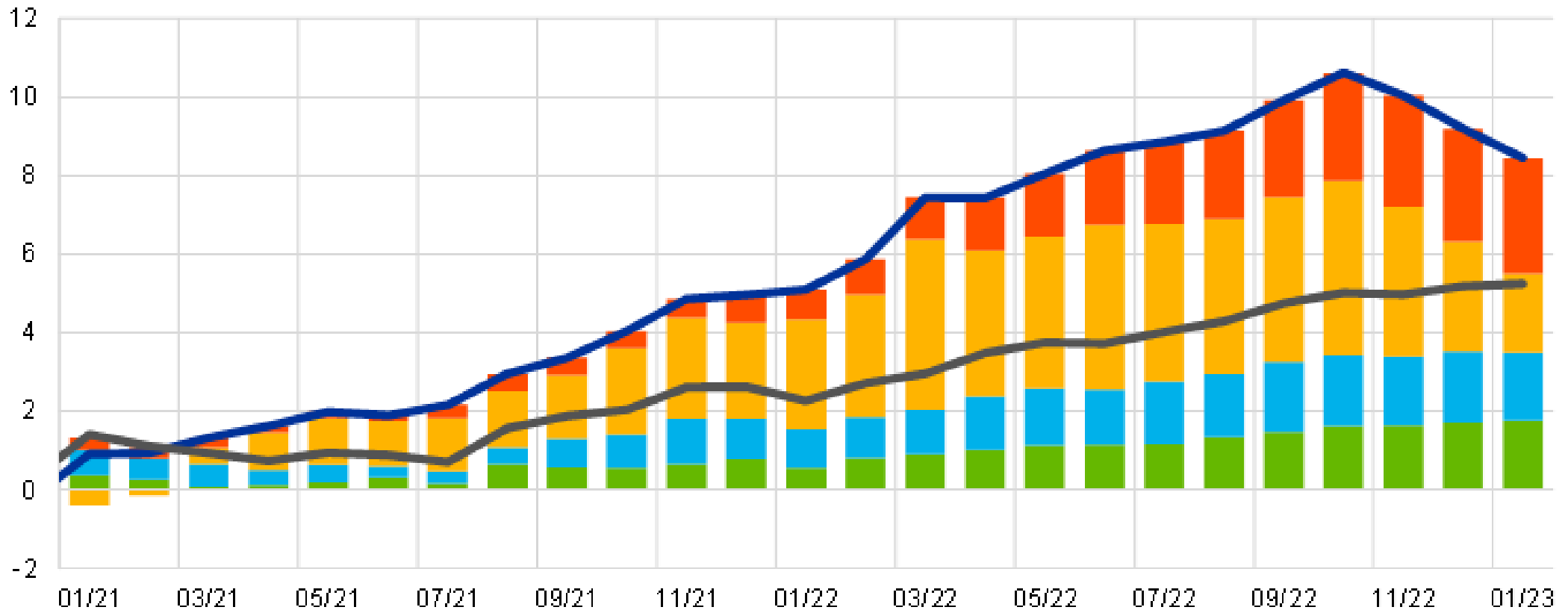
Do you negotiate with customers about higher costs and prices?



Source: Survey ETION/CRiON

...but does core inflation start to lead its own life?

- HICP inflation
- HICPX
- Energy
- Food
- NEIG
- Services



Bramhallz
NYDN

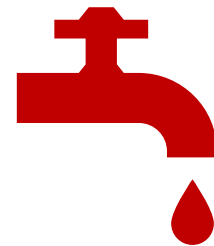
YOUR FUTURE
LOOKS PRETTY
MUCH LIKE
JIMMY CARTER'S

STAGFLATION



4. Turning off the money taps?

Not all taps are open



Percentage of companies that consider credit conditions as being tight

Q4 2022 = 35,7%



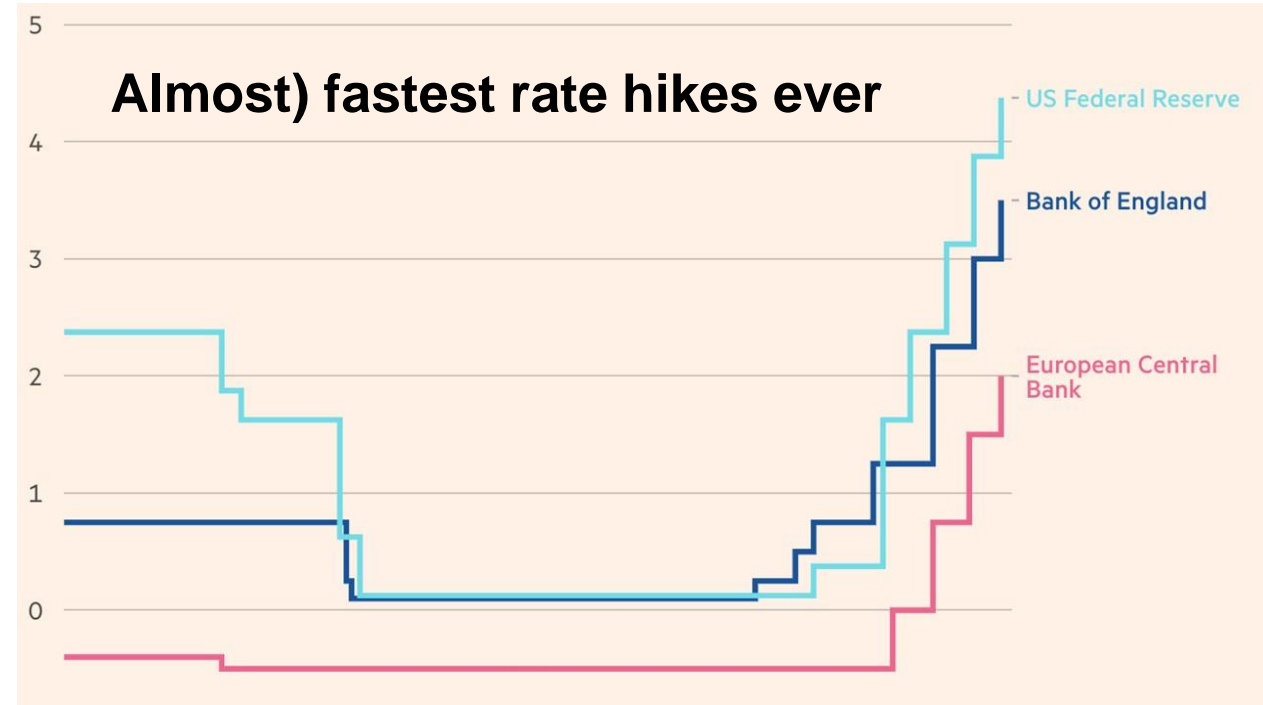
Industry:	30,2%
Services:	45,7%
Construction:	29,1%
Small:	35,8%
Medium:	33,7%
Large:	25,0%
XL:	27,7%

Bron: NBB

The return of gravity

- Interest rates are like gravity
- From zero to something
- Quantitative tightening

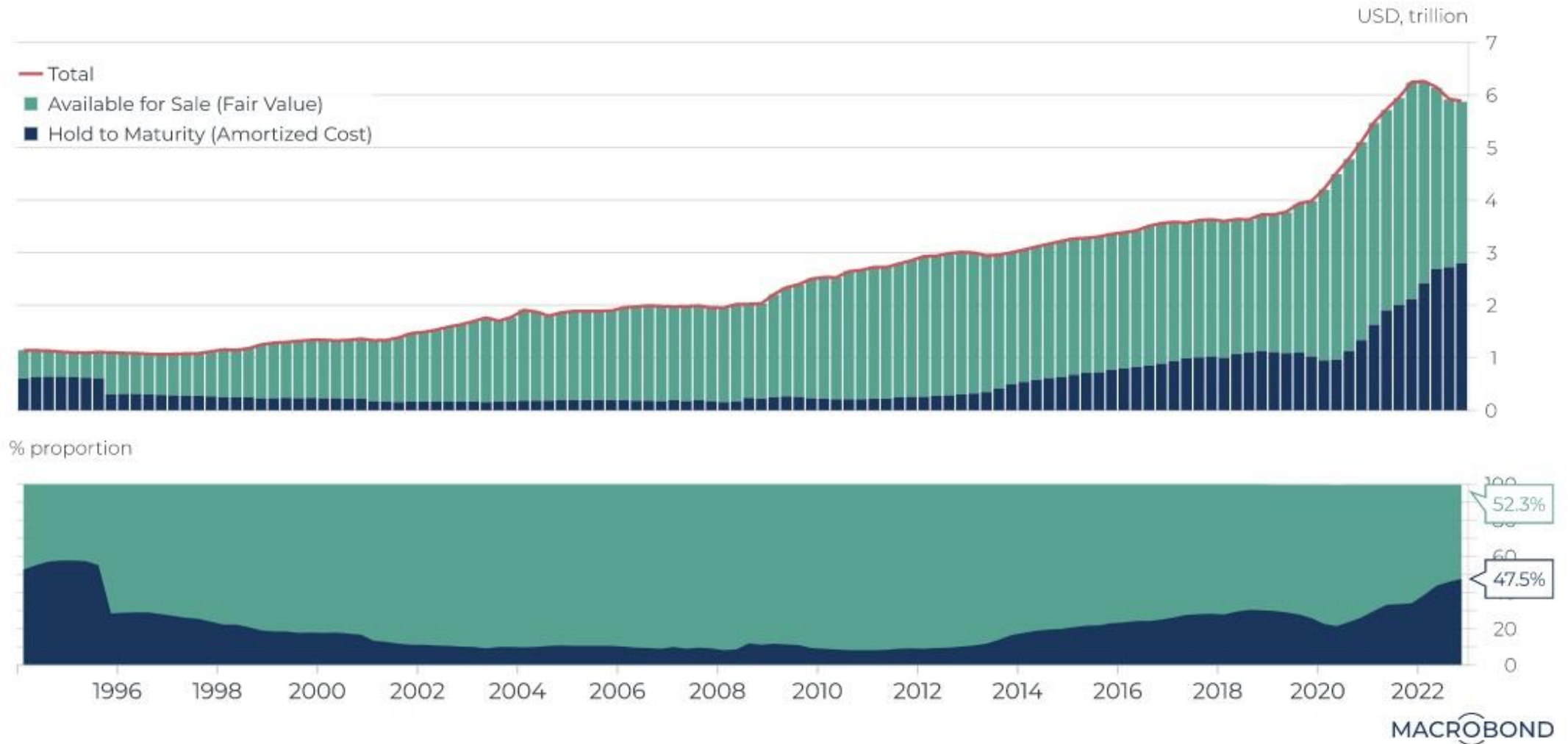
NASDAQ lost >20%



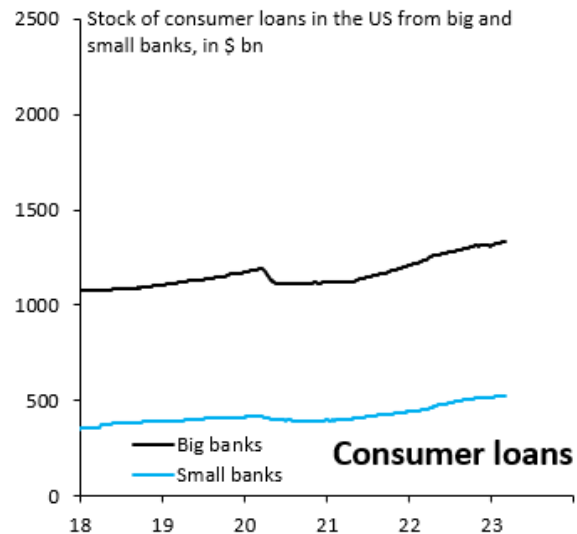
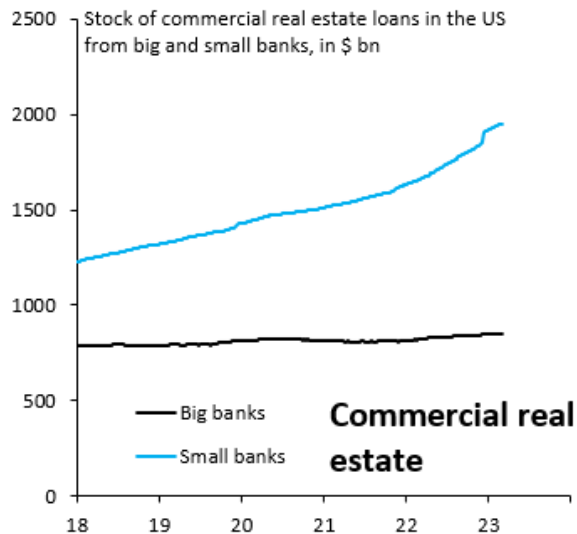
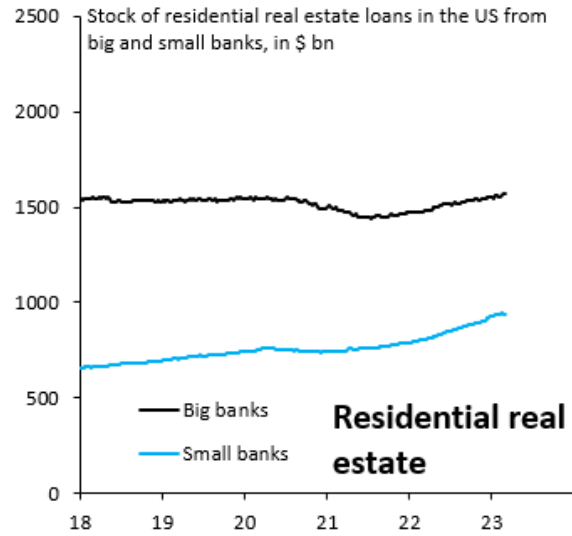
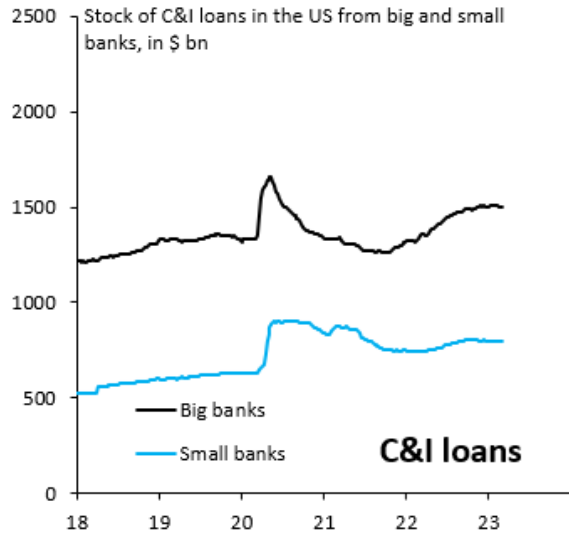
Hold to maturity not mature

US Commercial Banks & Saving Institutions: Securities held

Source: Federal Deposit Insurance Corporation

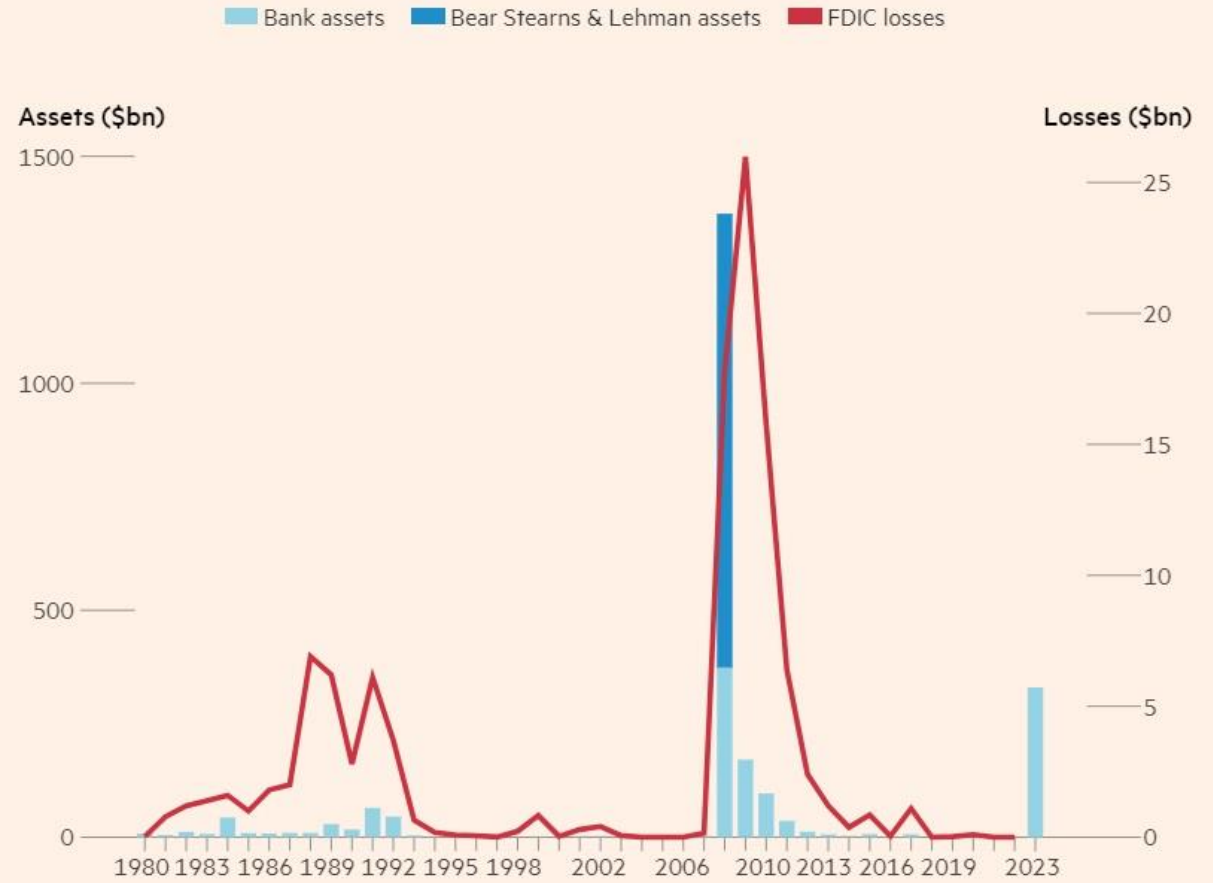


Concentration of risks



This is already a large banking crisis

US bank failures (\$bn), 1981-2023



FINANCIAL TIMES

Source: Oxford Economics, FDIC

There are several reasons to worry about the health of Europe's banks

Credit Suisse was the region's problem child but other institutions are not immune to the turmoil

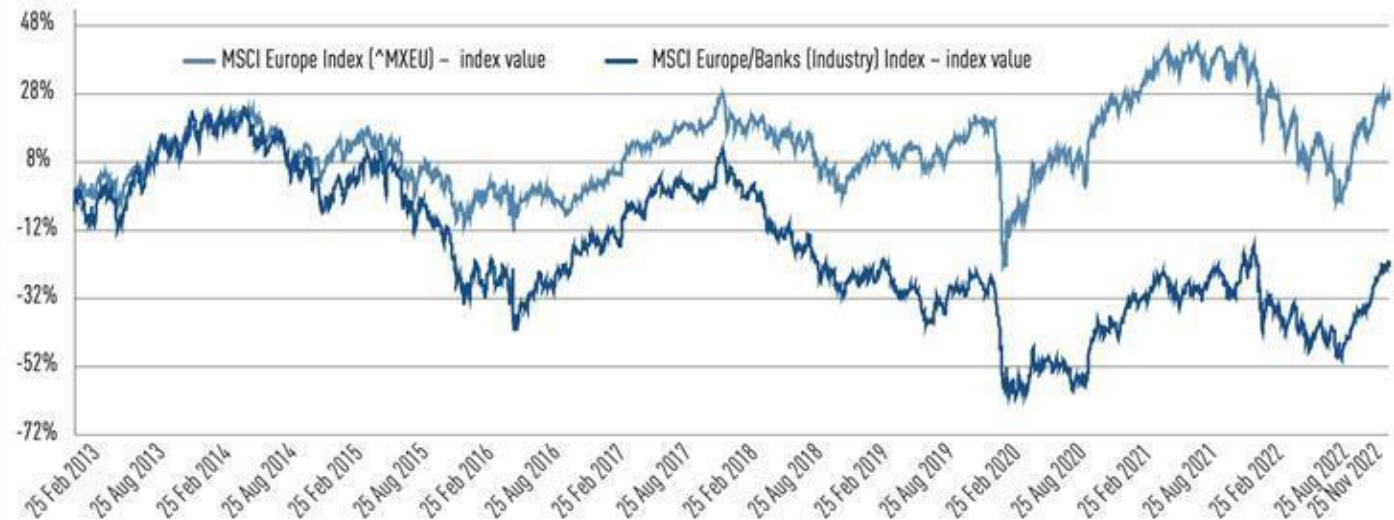
MARTIN ARNOLD [+ Add to myFT](#)



The headquarters of Credit Suisse, right, and UBS, left, at Paradeplatz in Zurich © Michael Buholzer/EPA-EFE/Shutterstock

- Eurozone banks are still not earning enough profit to cover their cost of capital
- Rising interest rates will hit the value of the banks' vast holdings of government bonds, mortgages and other debt

European banks have serially underperformed the broad market



Source: S&P Capital IQ

Global in life but national in death

Capital Outflows Show Loss of Confidence in Credit Suisse

Net new assets/net asset outflows reported by Credit Suisse*



* converted from CHF to USD at a rate of 1 CHF= 1.07988 USD

Source: Credit Suisse



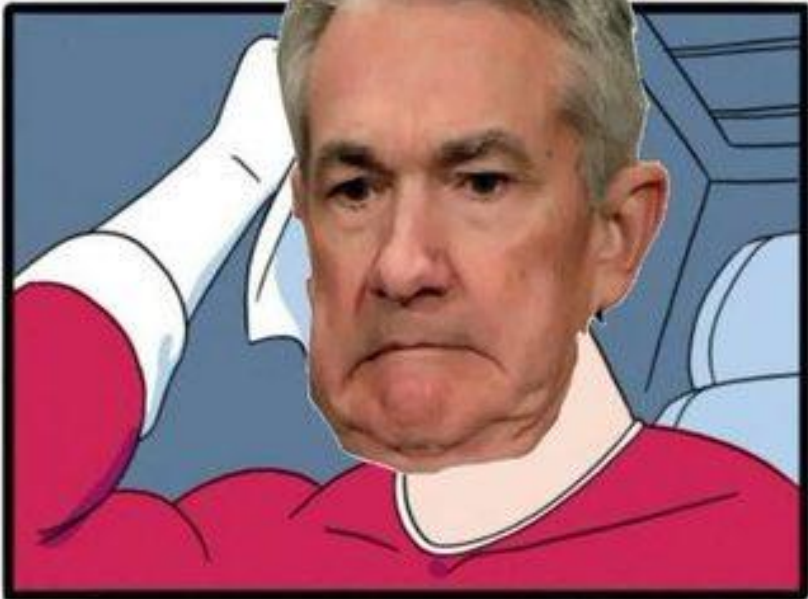
statista

Most banks are global in life but national in death (Mervyn King)

- \$54bn liquidity lifeline from the Swiss National Bank failed to stem the crisis
- Credit Suisse was sold for \$3.2bn to UBS

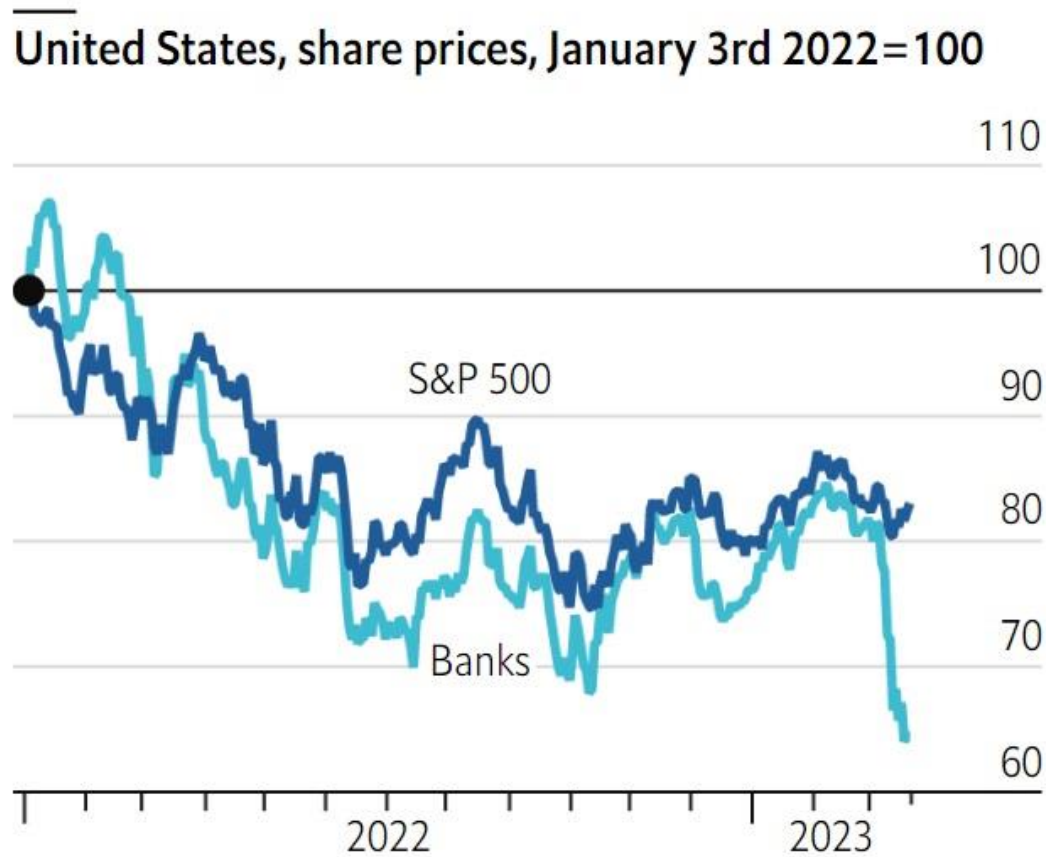
Swiss regulator demanded that AT1 debtholders lost out more than shareholders.

- European authorities restored calm by reassuring AT1 bondholders in eurozone and UK banks would not suffer the same fate.



Entrapment: Crisis or crisis?

This time is different



Source: Bloomberg

Course correction

United States, federal funds target rate, upper limit, %



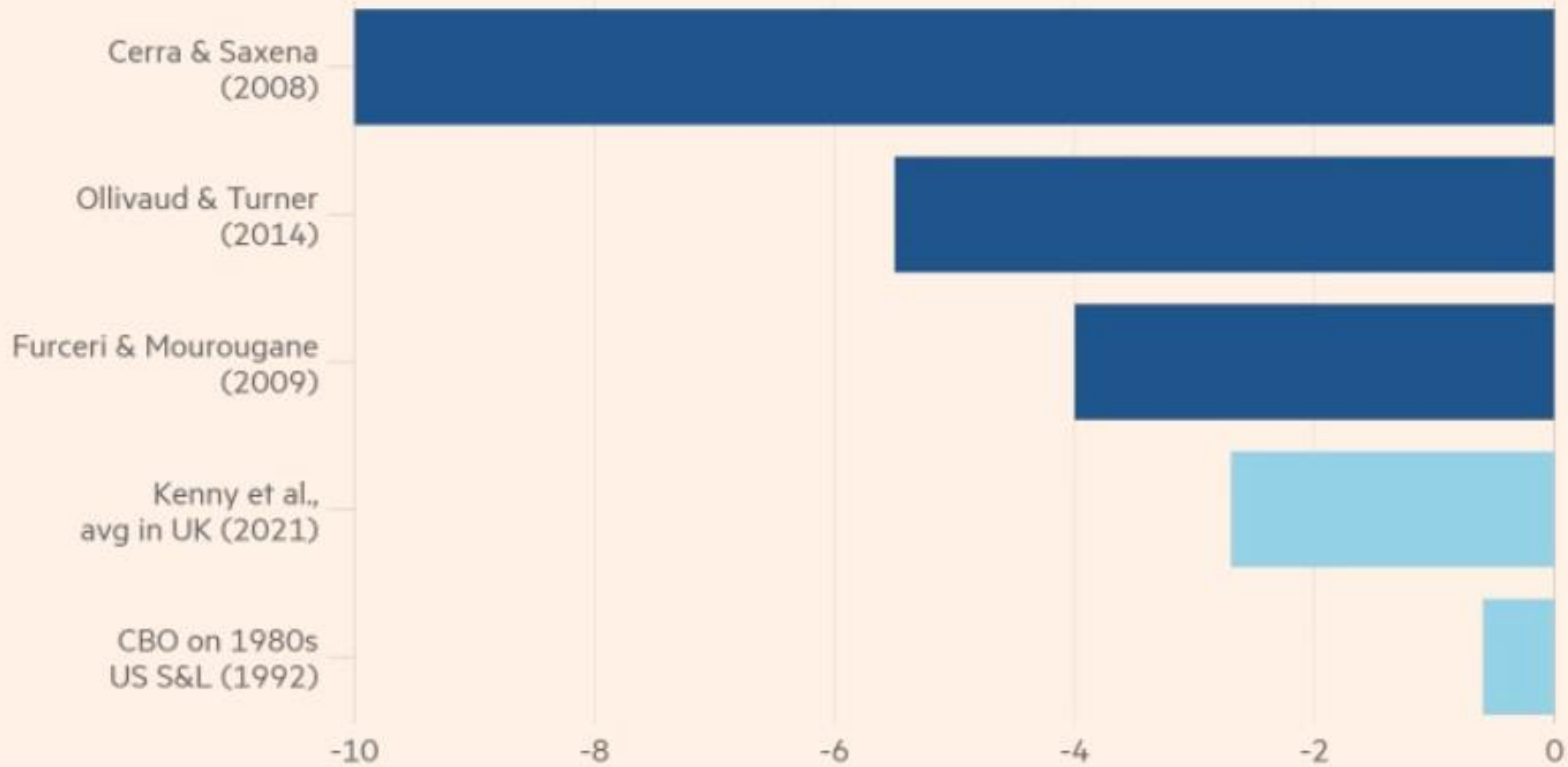
Source: Bloomberg

The Economist

Studies confirm the substantial costs of banking crises

Impact of crises on GDP (%)

■ Long-term ■ Short-term



Source: Oxford Economics
© FT

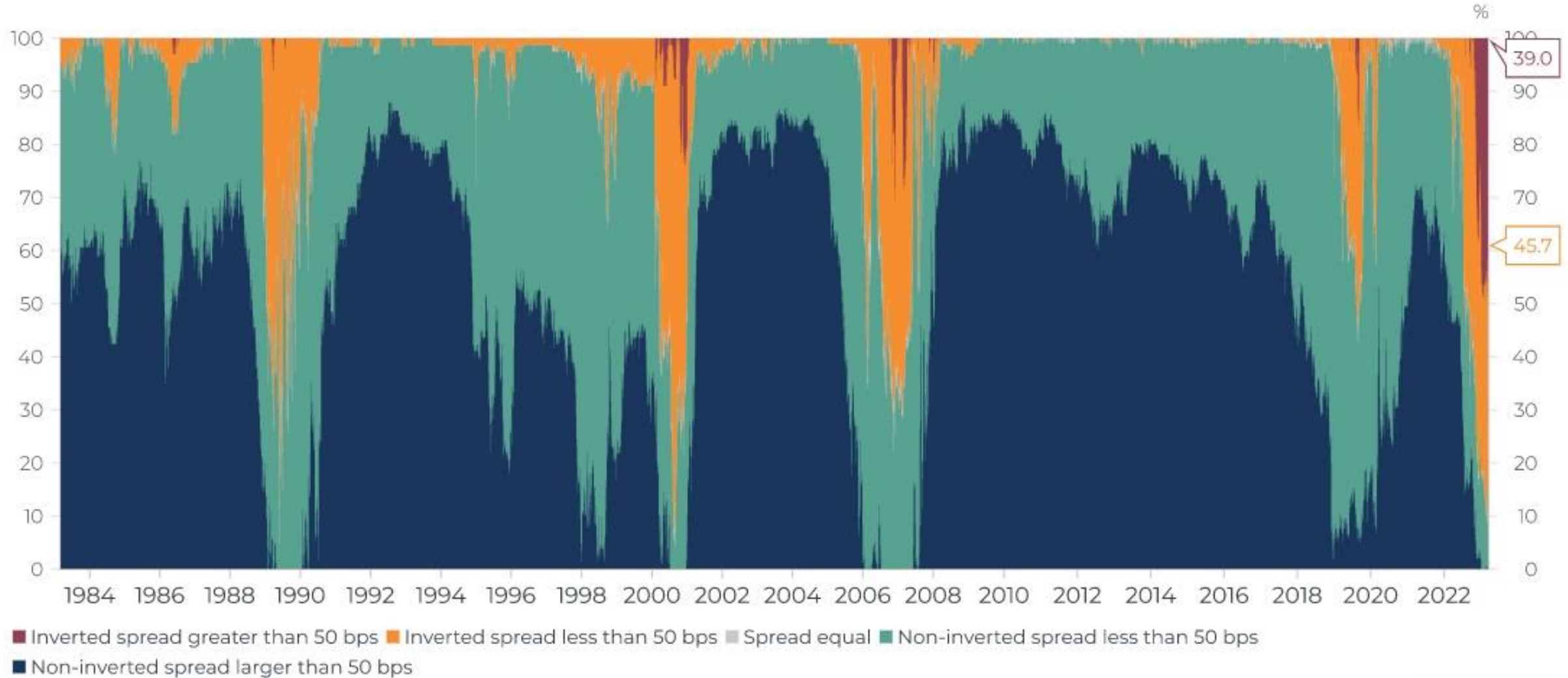
5. Do we need a recession?

Recession to rescue

Rising number of inverted yield curves signal recession

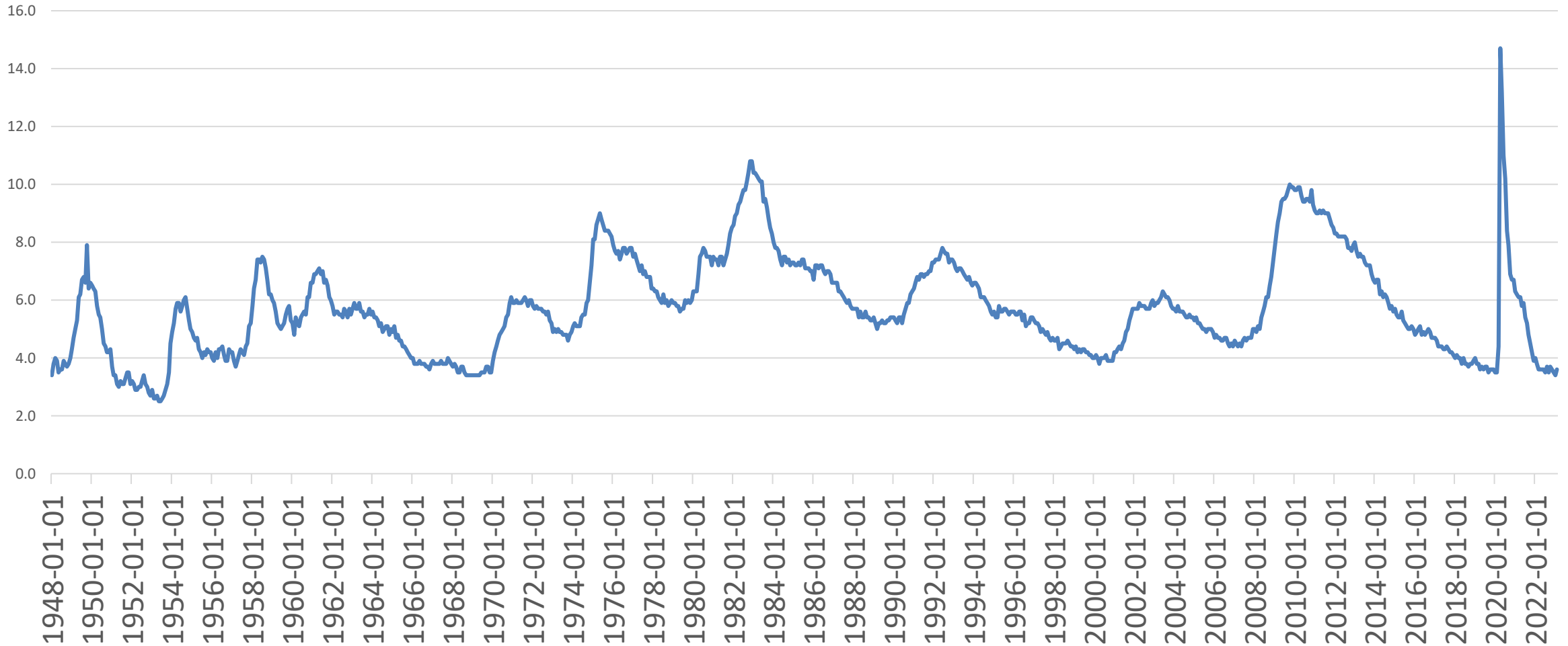
United States

Source: U.S. Department of Treasury, Macrobond Financial AB



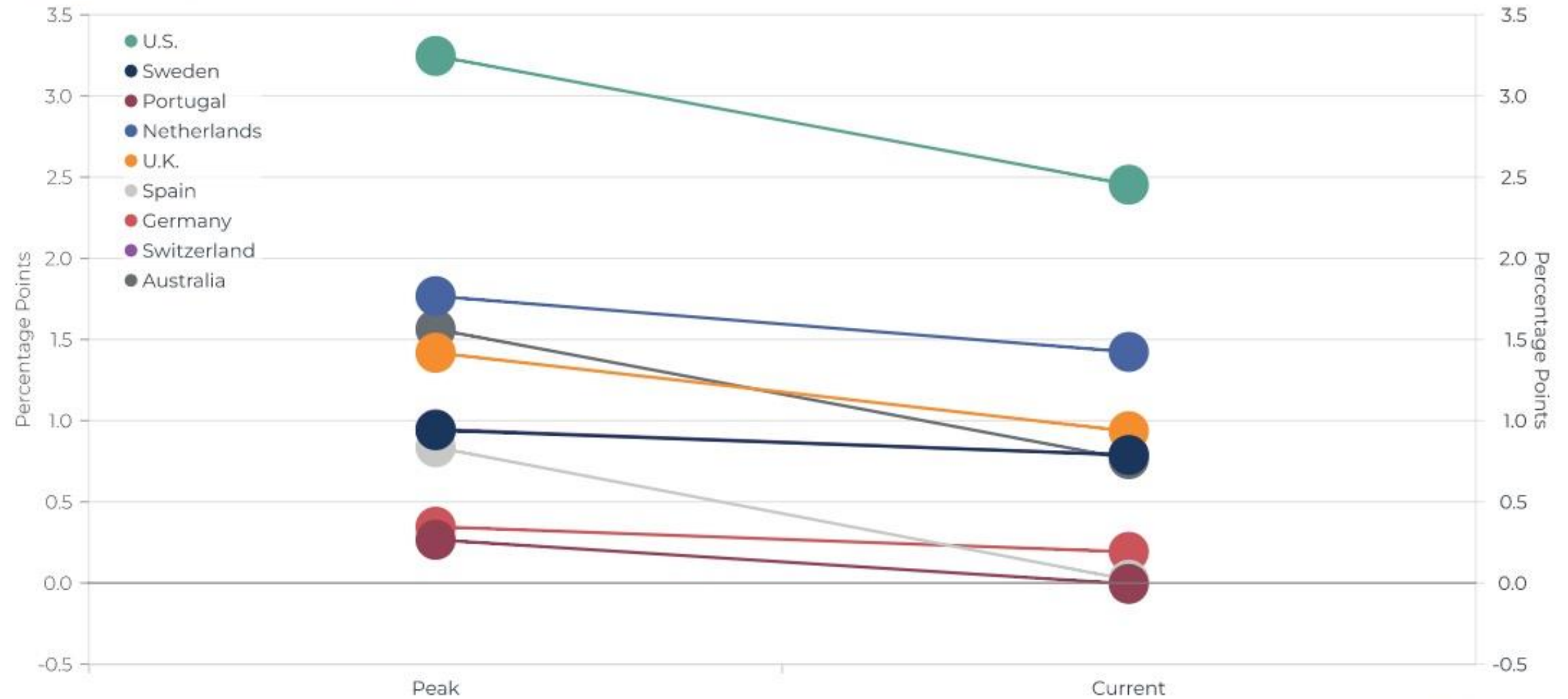
But US unemployment remains historically low

UNRATE



Job openings are still well above pre-pandemic levels in many large countries

Job openings rate as a share of the labour force, relative to December 2019

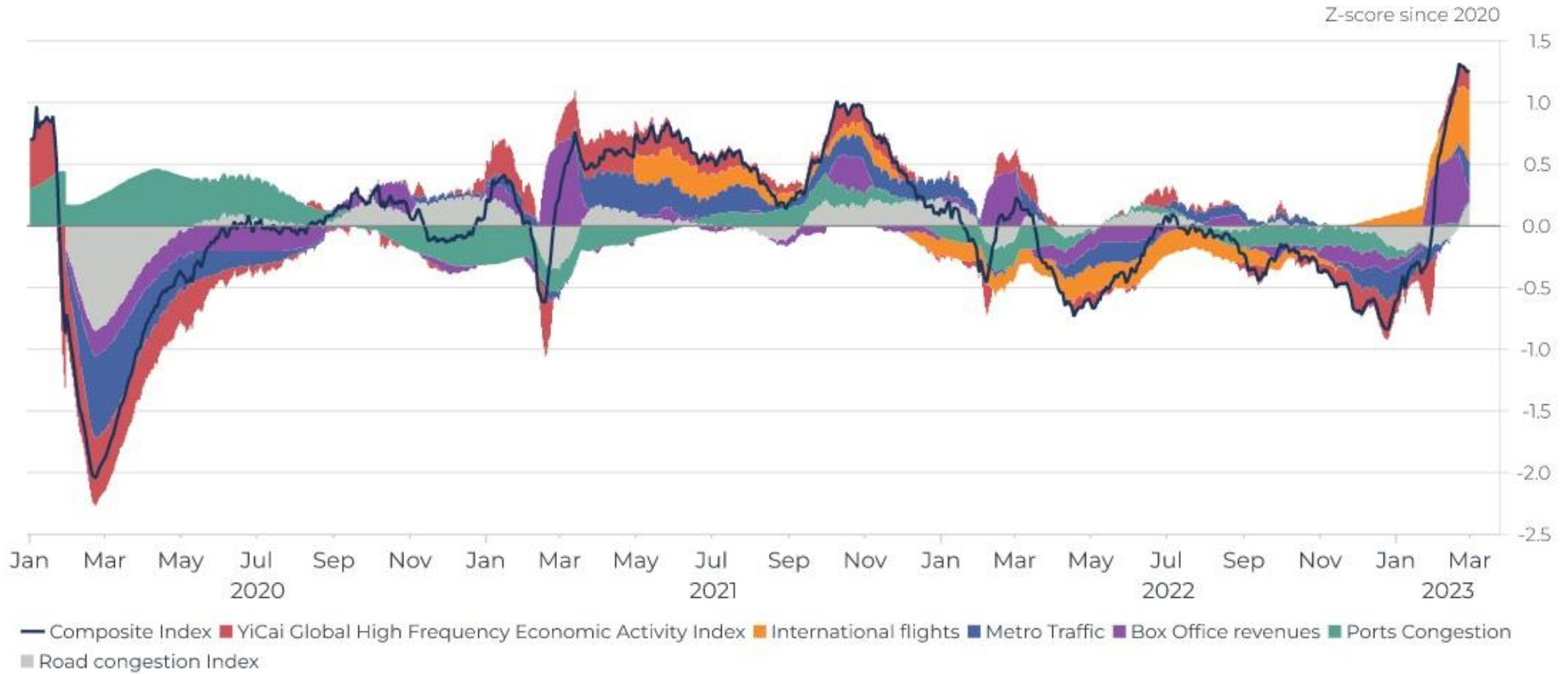


National Sources

MACROBOND

China: reopening composite index

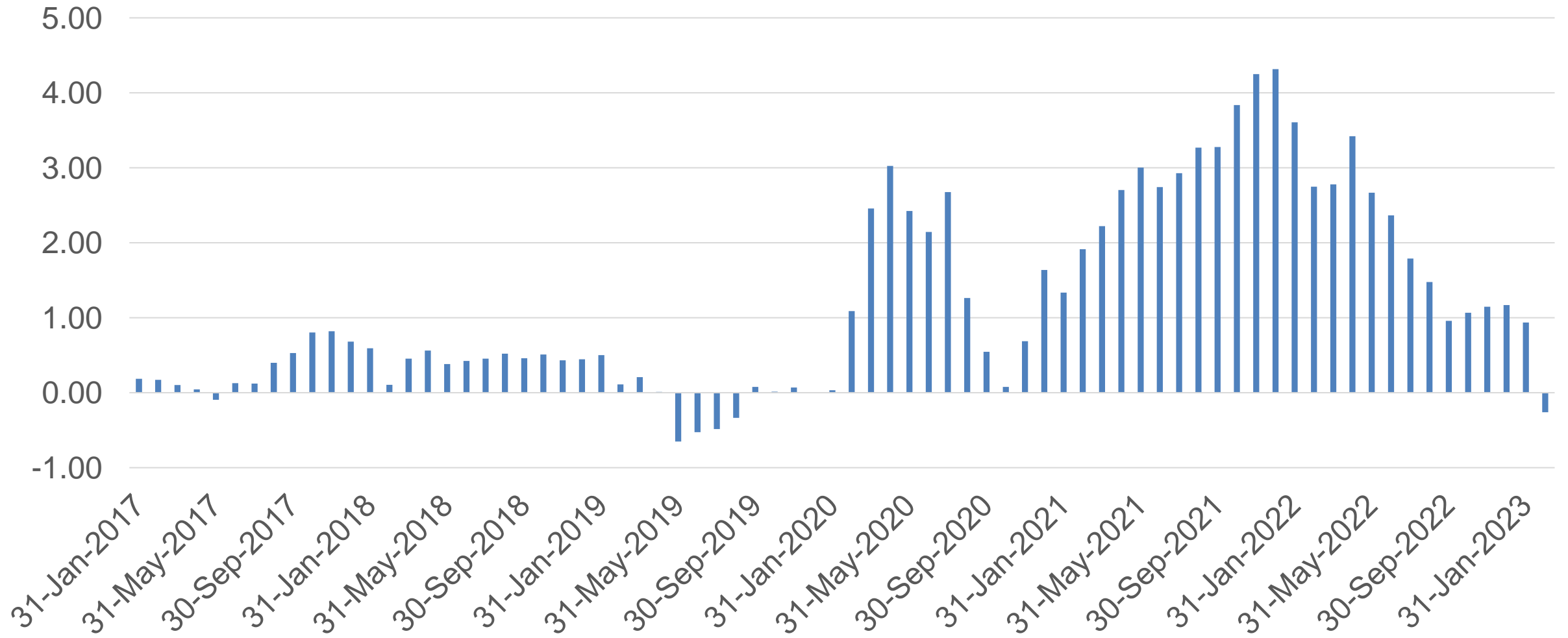
The composite index is built using various alternative daily datasets (roads & ports congestion, subway traffic, international flights, box office and economic activity index)



MACROBOND

etion

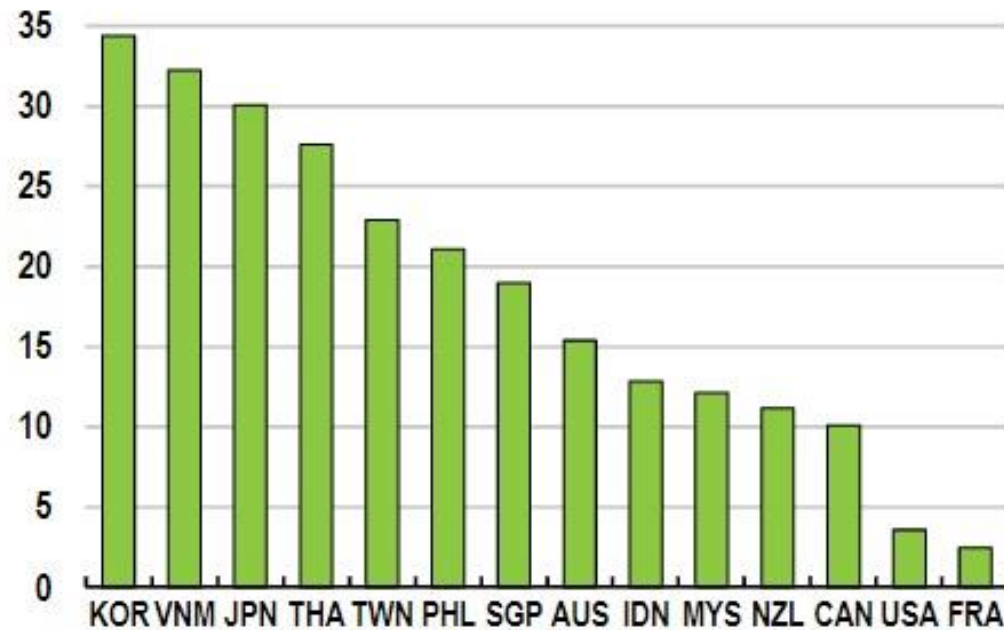
Supply chain stress easing



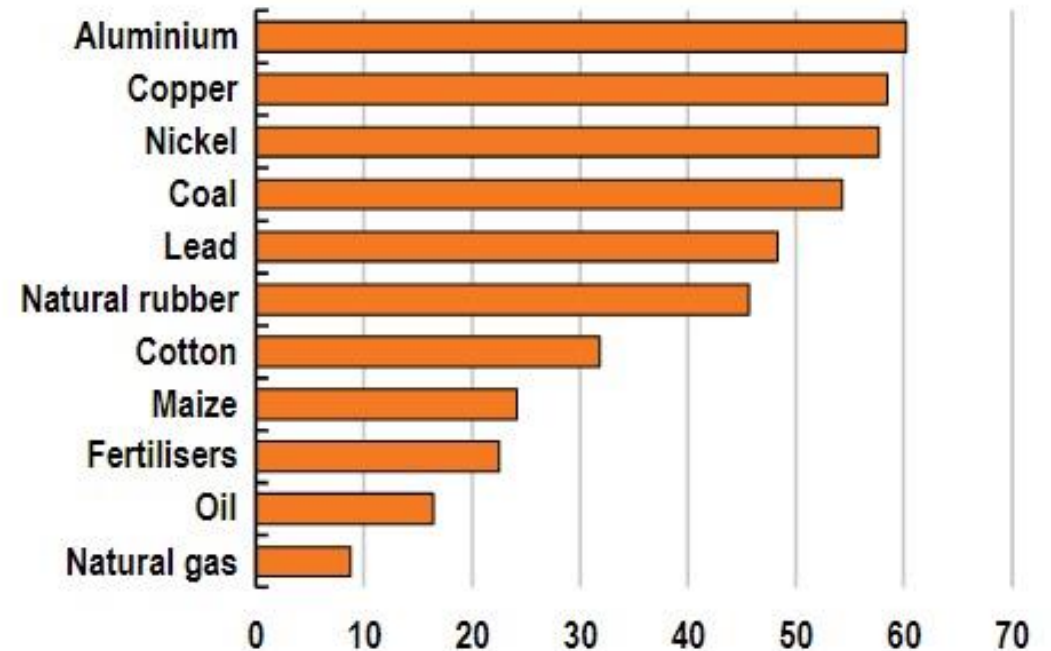
Federal Reserve Bank of New York

China reopening affects global demand

A. International visitor arrivals from China in 2019
% of total arrivals

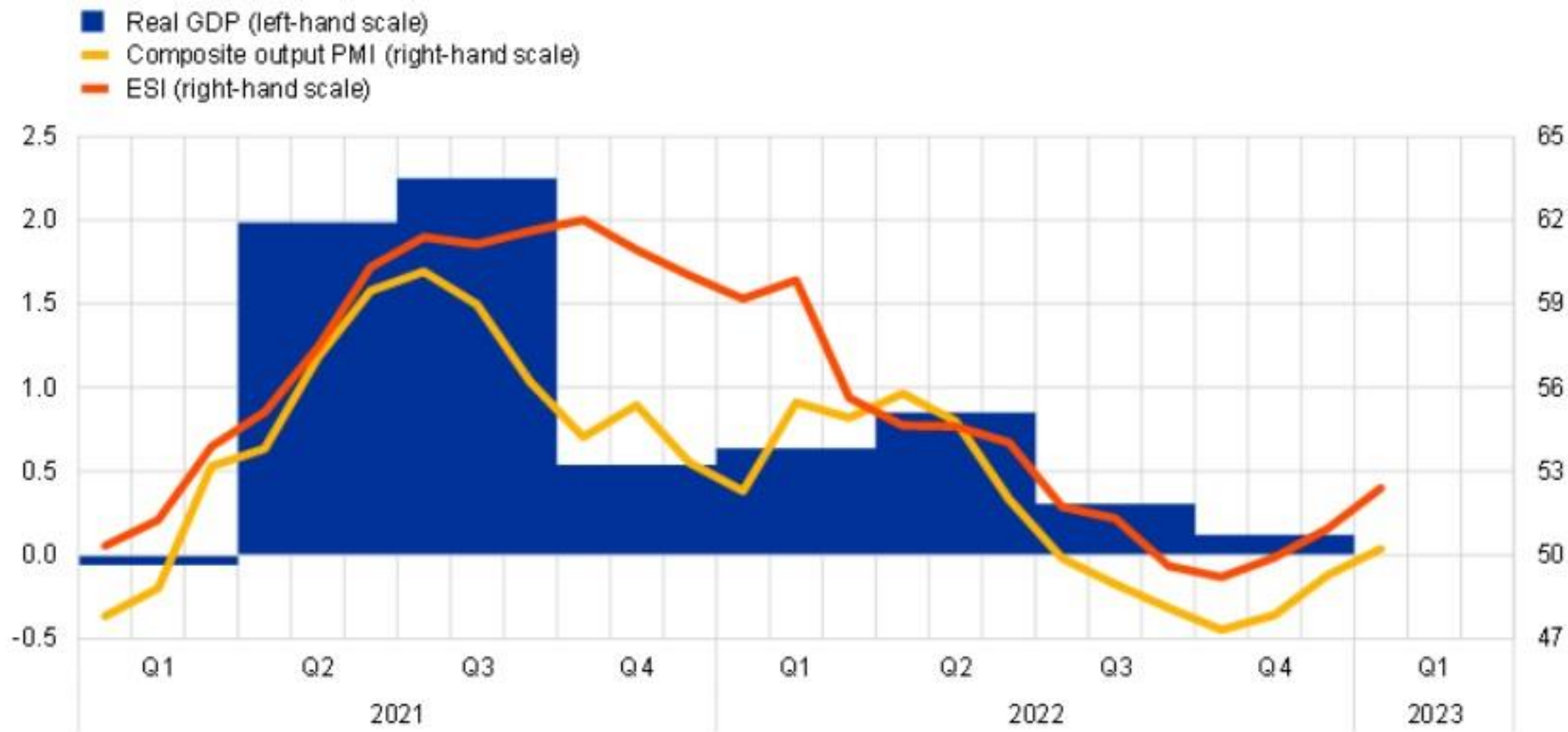


B. China's share of global commodity demand
%, 2021 or latest available



Note: Panel A: data for Australia are for the year to June 2019 and data for France are for 2018. Panel B: 2021 data for oil, natural gas, fertilisers, maize and cotton, and 2020 for all other commodities.

Source: OECD Interim Economic Outlook March 2020; International Energy Agency; OECD-FAO Agricultural Outlook database; World Bank; World Fertilizer Association; and OECD calculations.



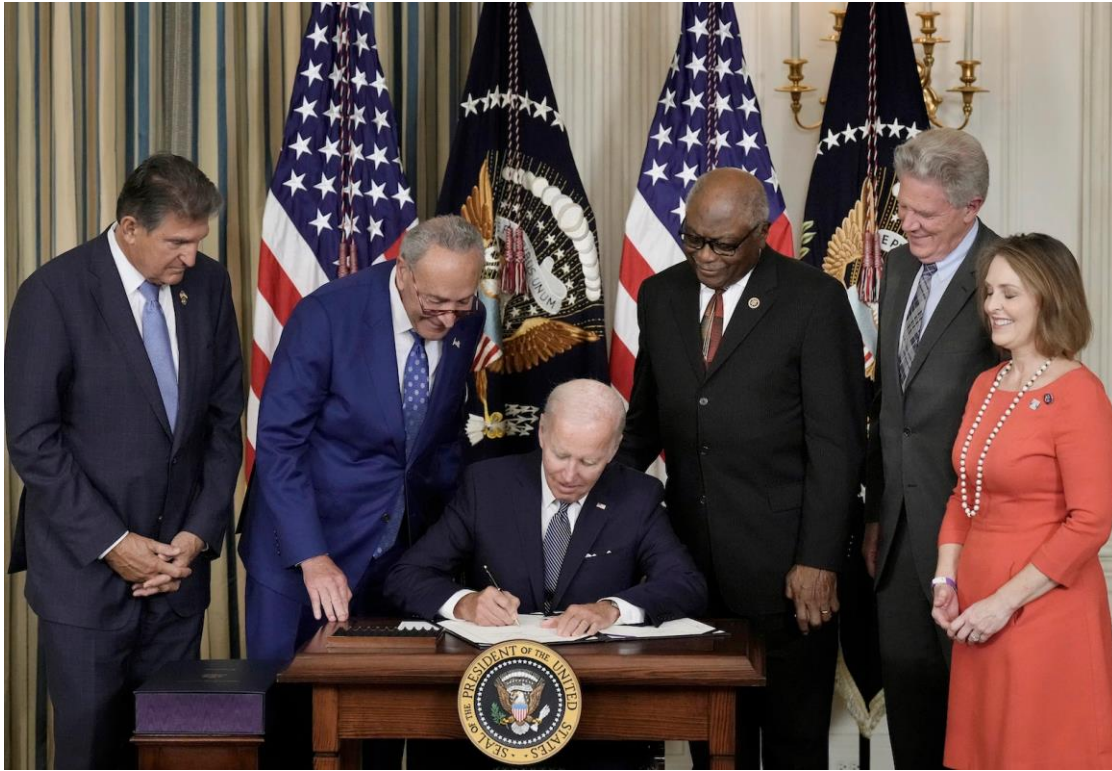
Sources: Eurostat, European Commission, S&P Global and ECB calculations.

	2020	2021	2022	2023e
Rich countries	-4.4	5.2	2.4	1.1
Eurozone	-6.1	5.7	3,5	0,8
Belgium	-5.7	6.2	3,1	0.1
Germany	-3.7	2.6	1.9	+0.3
France	-7.9	6.8	2.6	0.7
Netherlands	-3.9	4.9	4.5	0.8
Italy	-9.0	6.7	3.8	+0,6
UK	-9.3	7.4	4.0	-0.2
US	-4.4	5.2	2.1	1.5
Japan	-4.6	1.7	1.0	1.4
Developing countries	-1.9	6.6	3.7	3.7
World economy	-3.0	6.0	3.2	2.6

Bron: ETION, OECD, IMF, DeStatis, Planbureau

6. Europe needs to stand firm

In the long run strategic issues will matter more than a few percentage points of growth

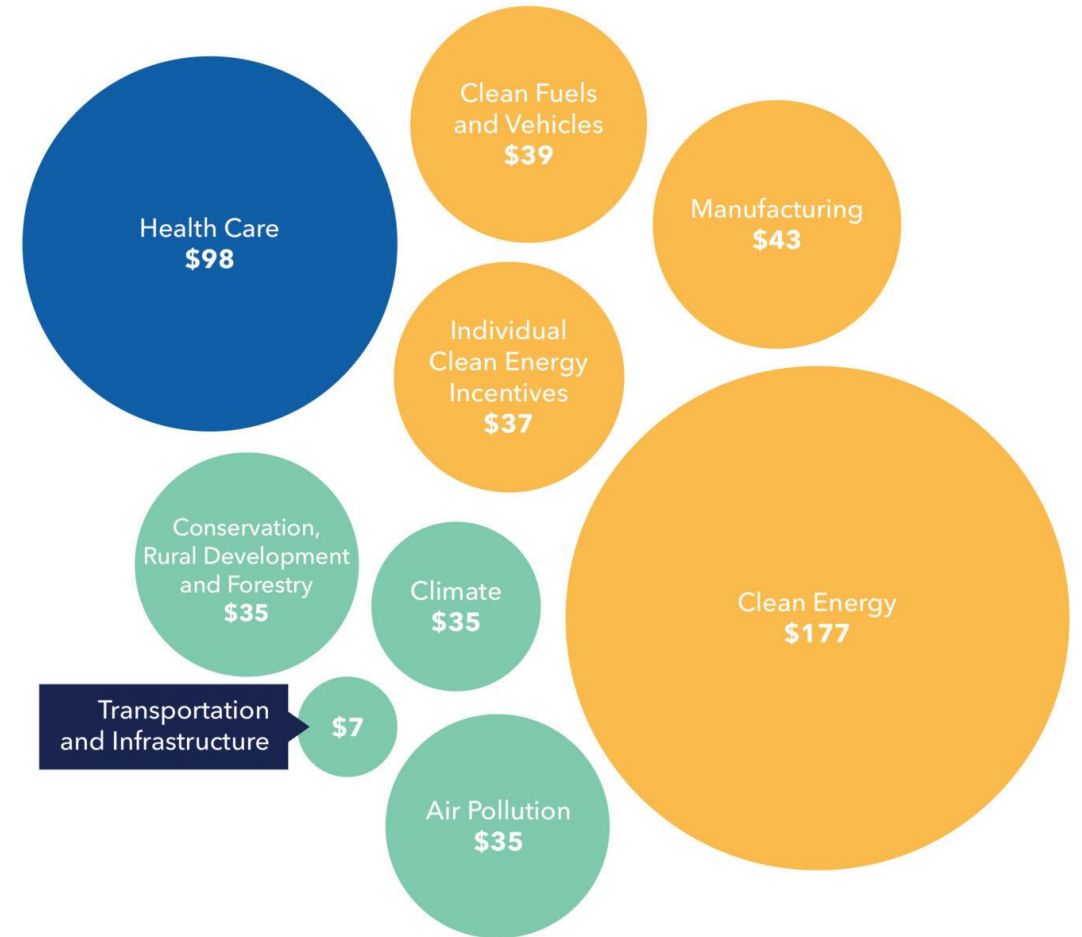


Inflation Reduction Act is dividing the EU

Spending and Tax Cuts

Figures in billions over 10 years from 2022-2031

● Health Care ● Energy ● Climate

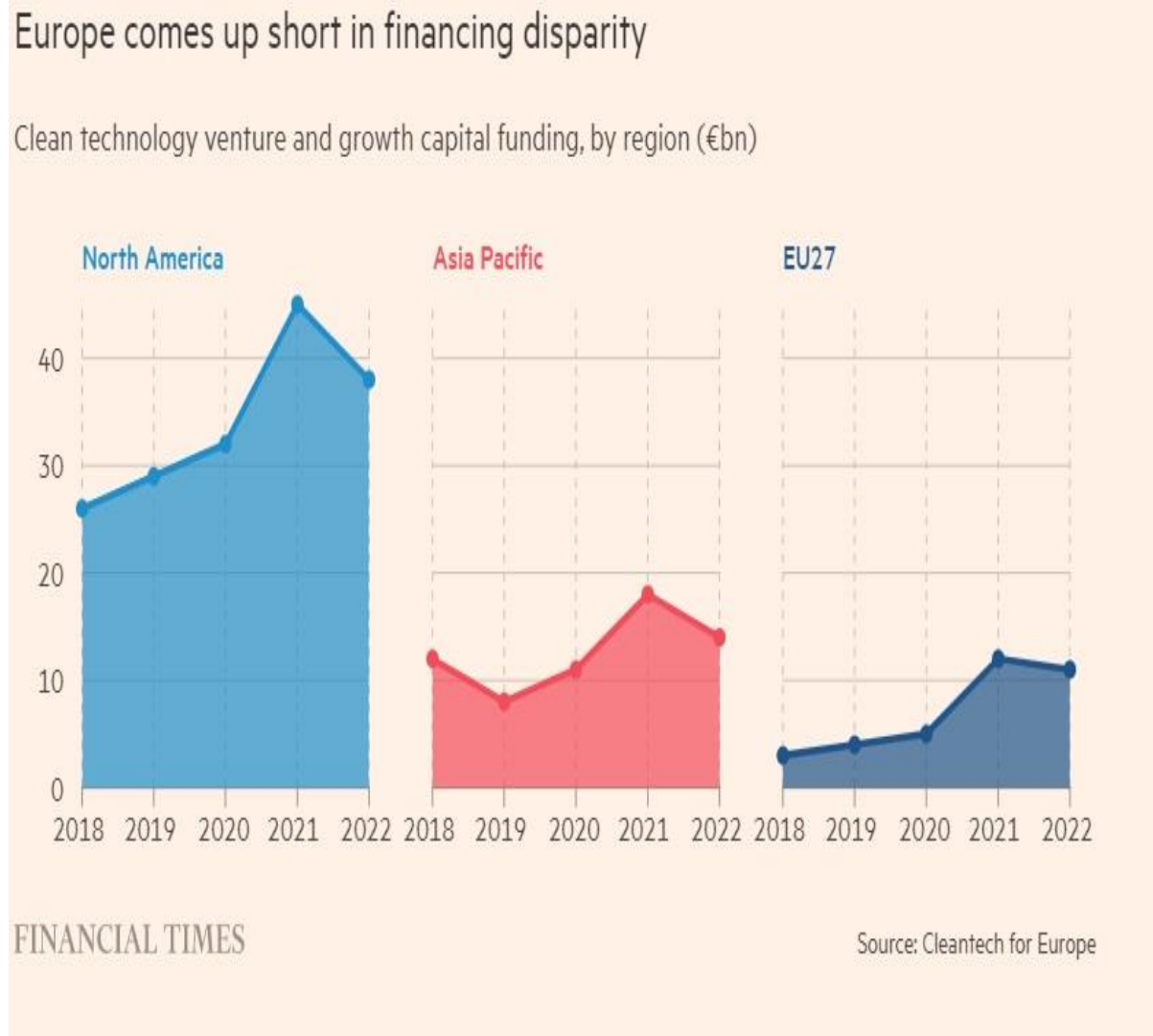


VW puts European battery plant on hold as it seeks €10bn from US

Europe's largest carmaker is 'waiting' for an EU response to Biden administration's subsidies

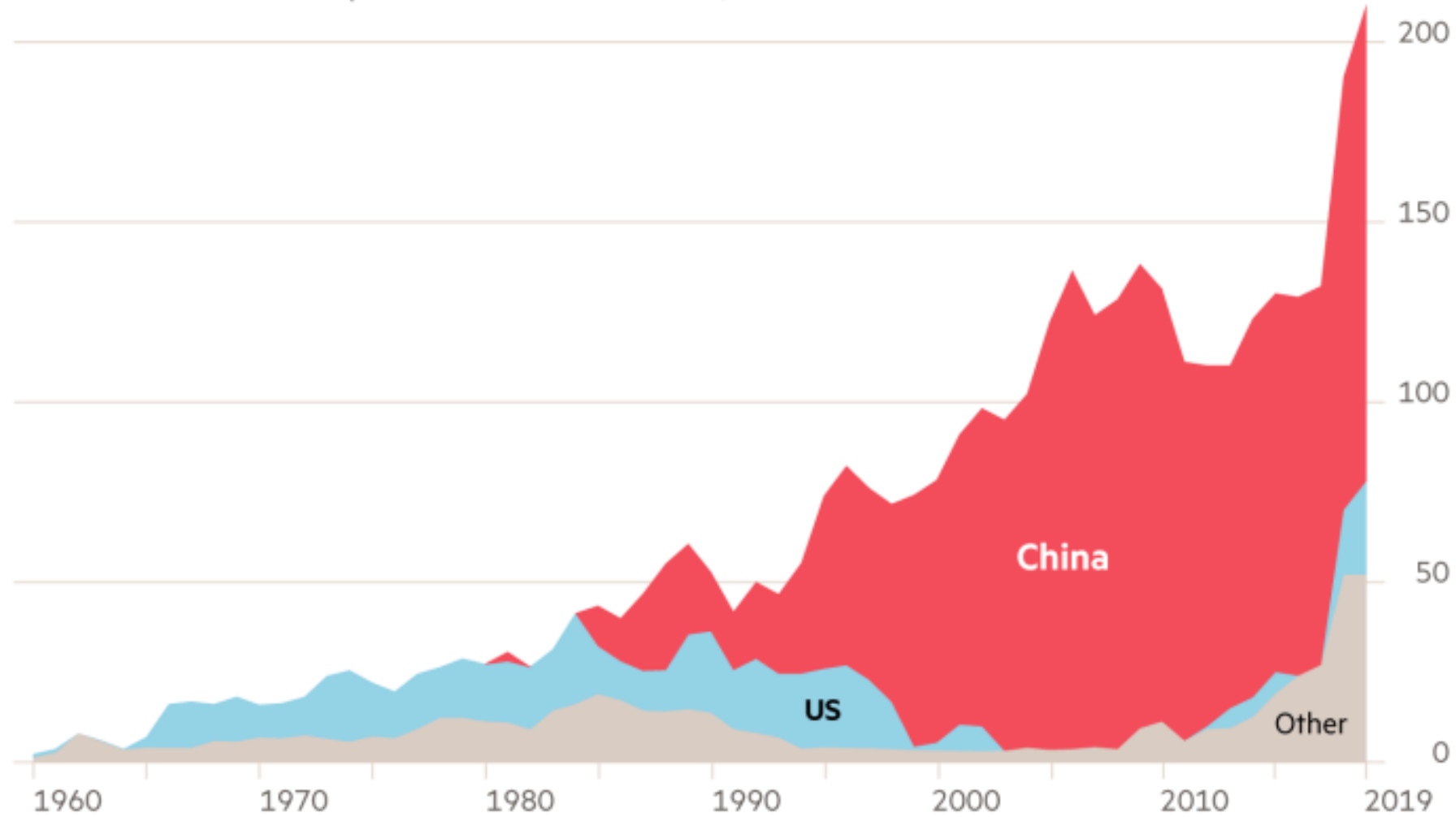


VW said no decisions had been made on the locations of its plants in North America or Europe and it was committed to its plan to build more cell factories in Europe © Jens Schlueter/AFP/Getty Images



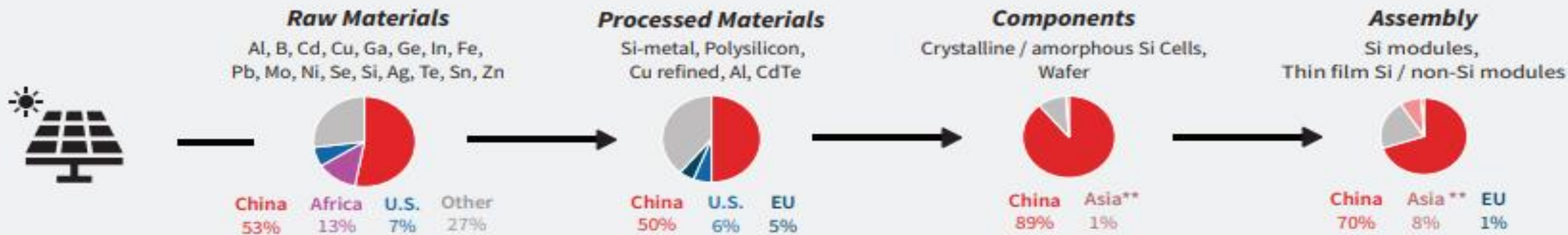
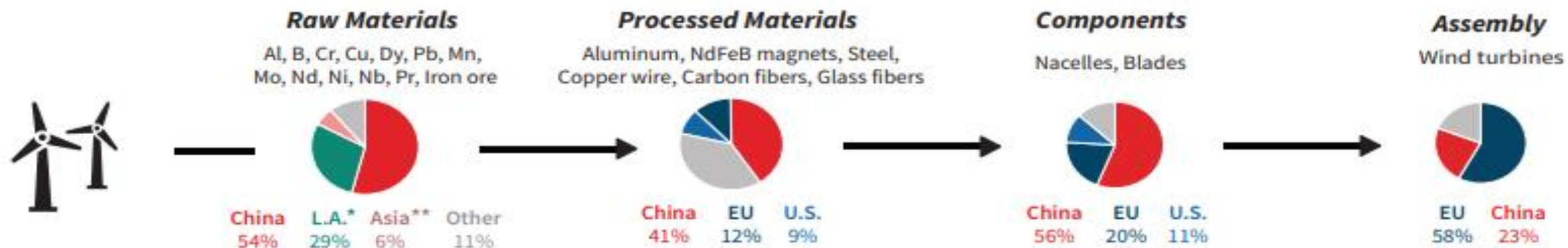
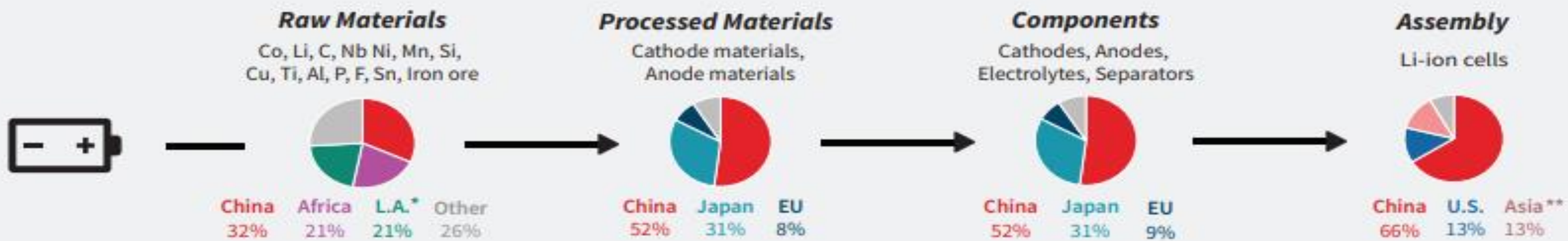
China dominates rare earths production

Rare-earths oxide mine production (metric tonnes, '000s)



Sources: US Bureau of Mines; US Geological Survey; 2011-2019 data comes from USGS annual Mineral Commodity Summaries

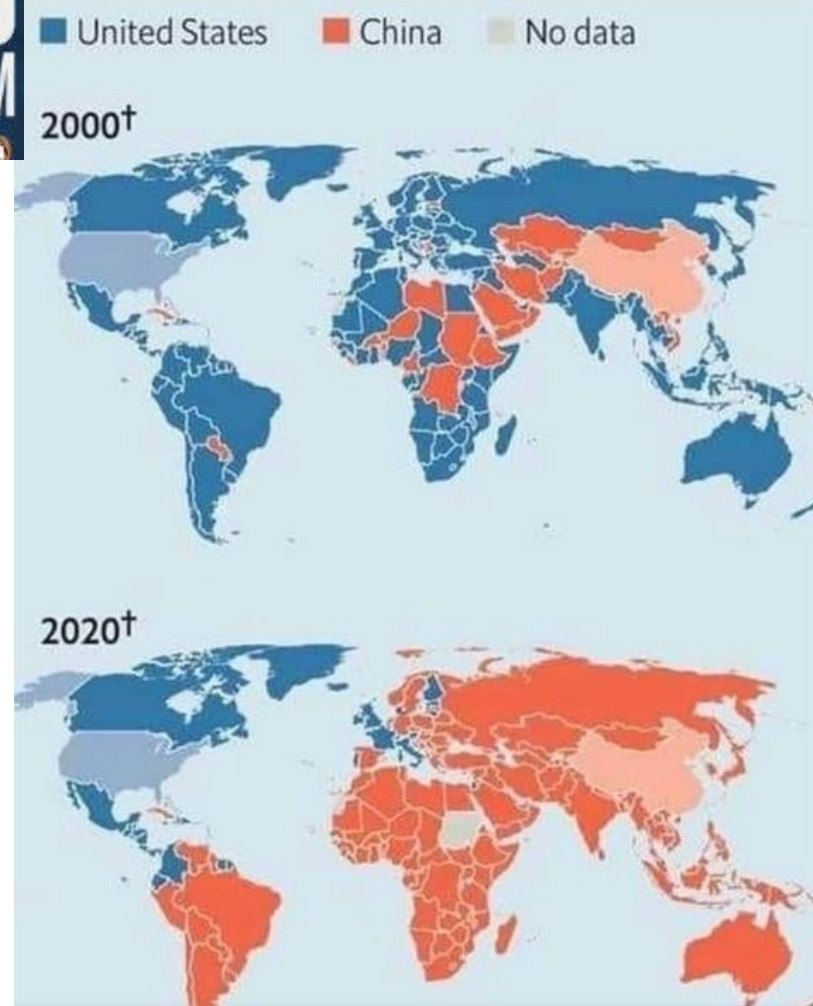
© FT



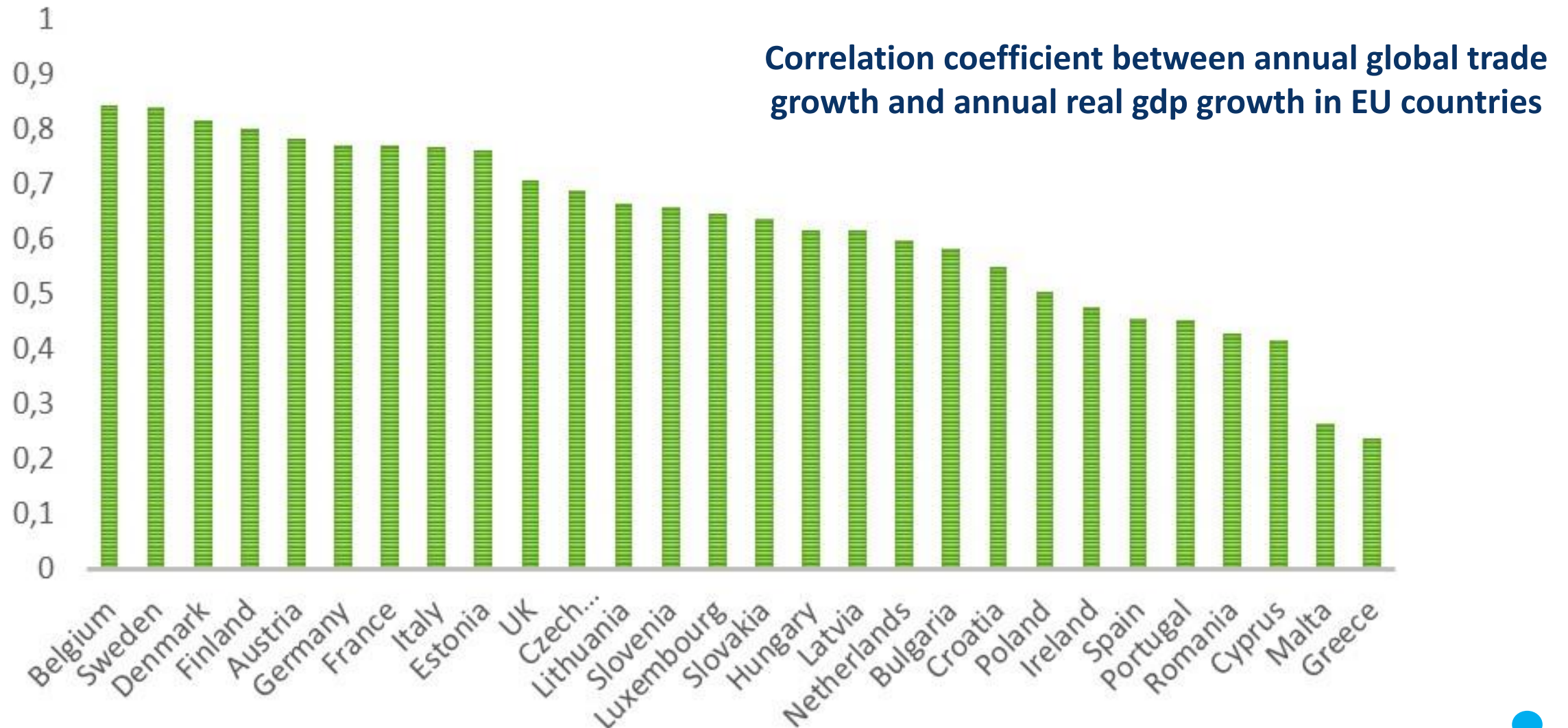
On the Chinese Table



Steven Johnson
**WHERE GOOD
IDEAS
COME FROM**
*The Seven Patterns
of Innovation*



Europe is vulnerable for trade wars





Giorgia Meloni claims victory in Italy's general election

Far-right leader Giorgia Meloni has claimed victory in Italy's election, and is on course to become the country's first female prime minister.

Italy first and making Italy great again?

The neverending story with a bad end?



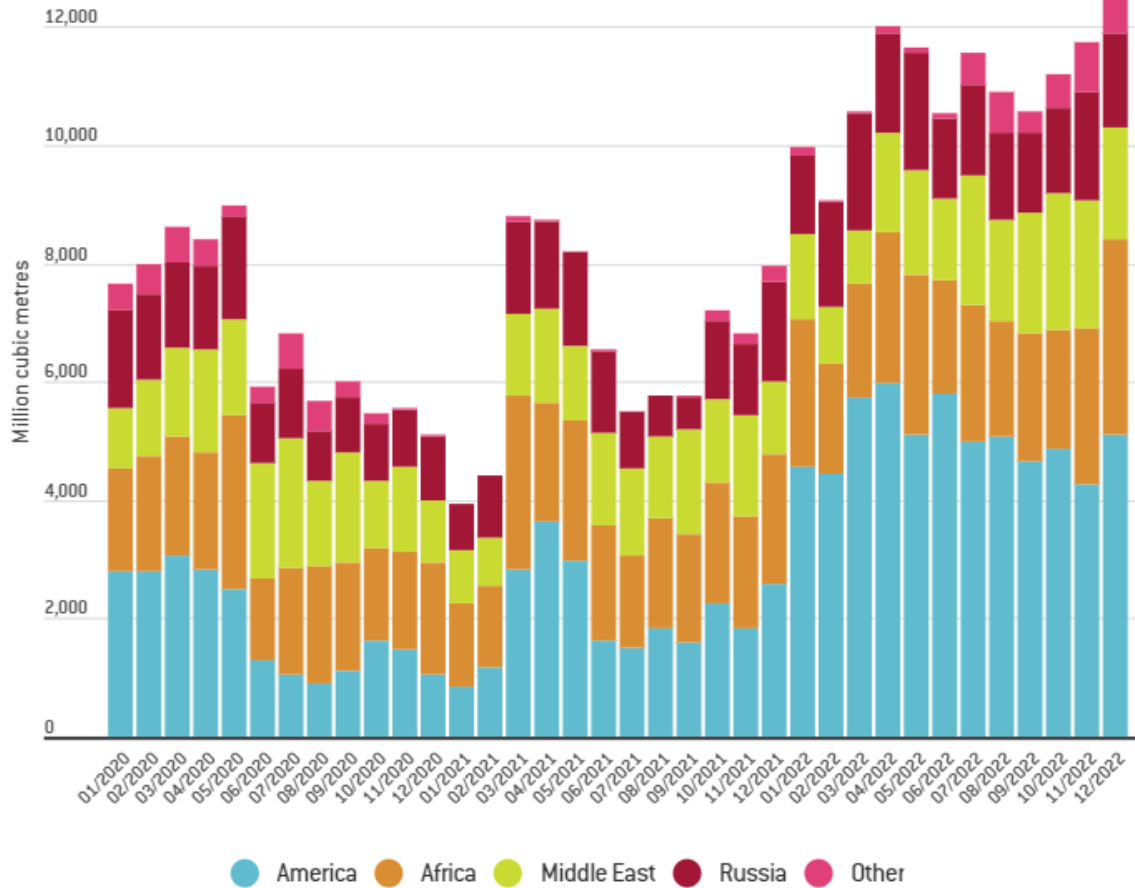
7. Light at the end of the tunnel?

And don't let it be a train

Towards a unified world gas market

EU27 LNG monthly imports by region of origin

Last updated: 03/01/2023 (update every month)

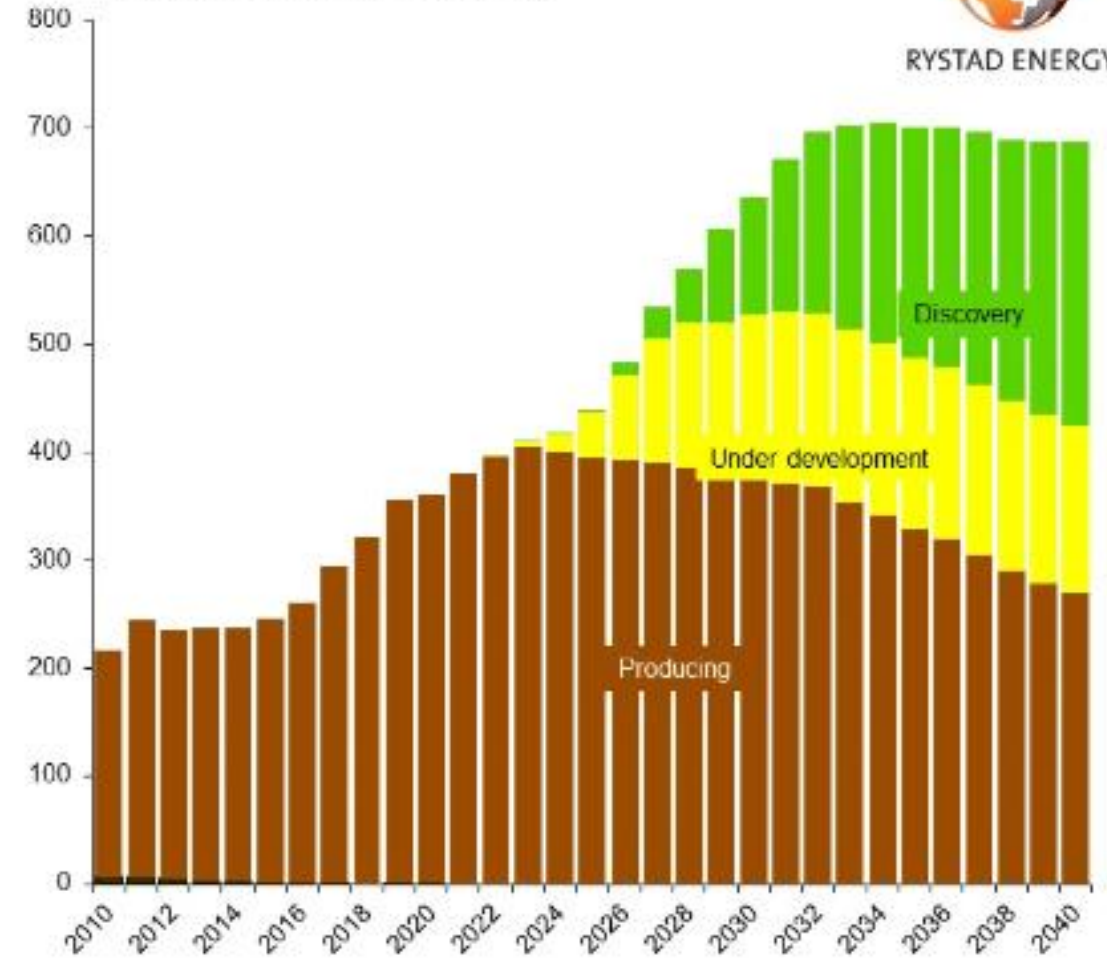


Global LNG production

Million tonnes per annum



RYSTAD ENERGY

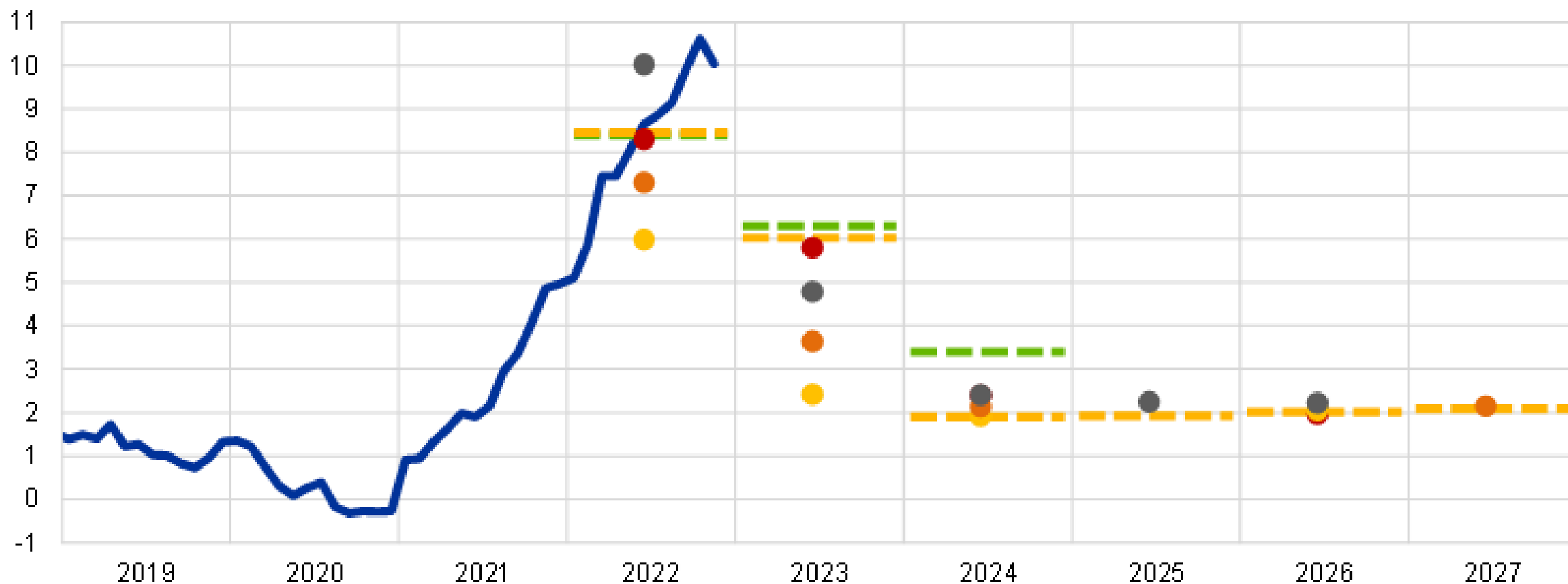


Source: Bruegel based on Bloomberg

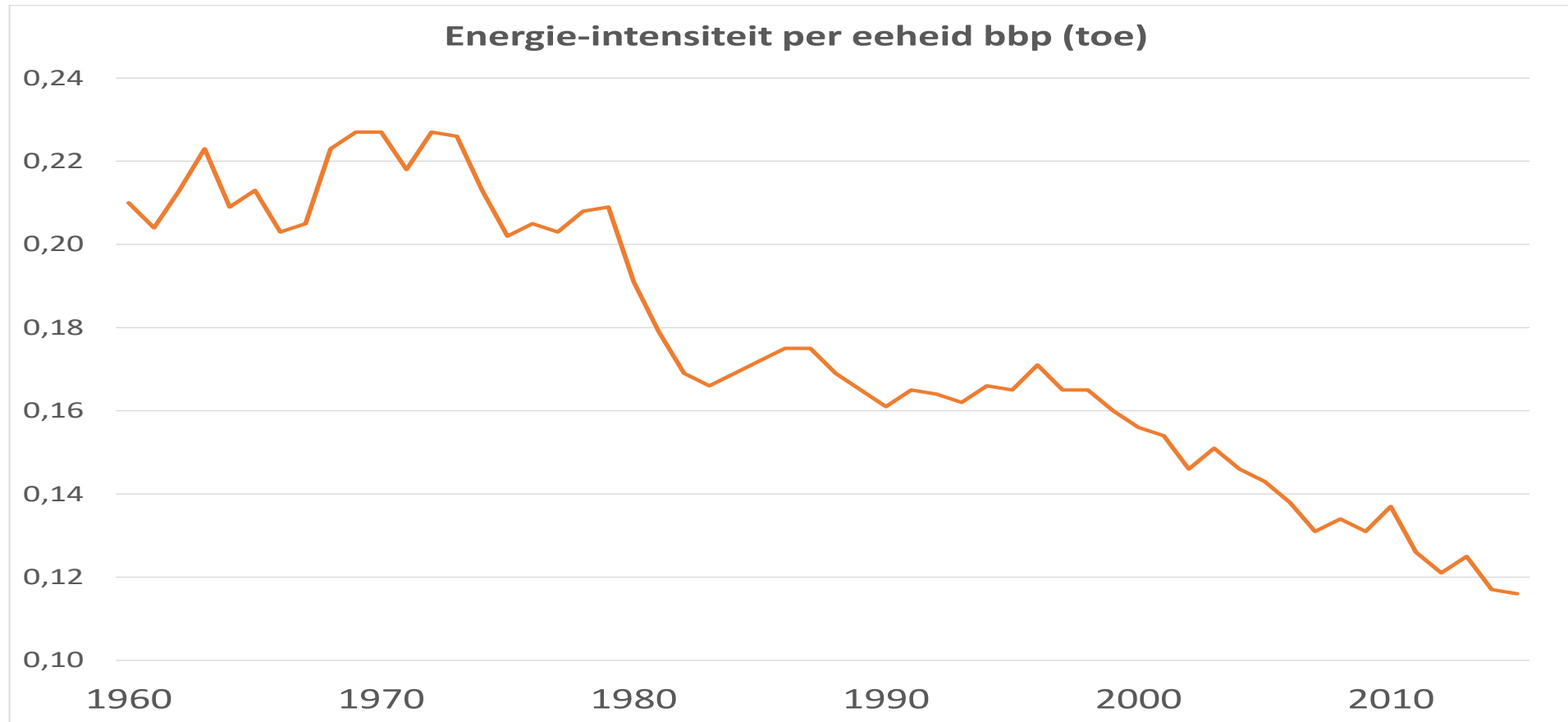
Eurozone inflation expectations

- HICP
- Eurosystem staff macroeconomic projections (December 2022)
- Consensus Economics – HICP
- Market-based indicators of inflation compensation (6 December 2022)

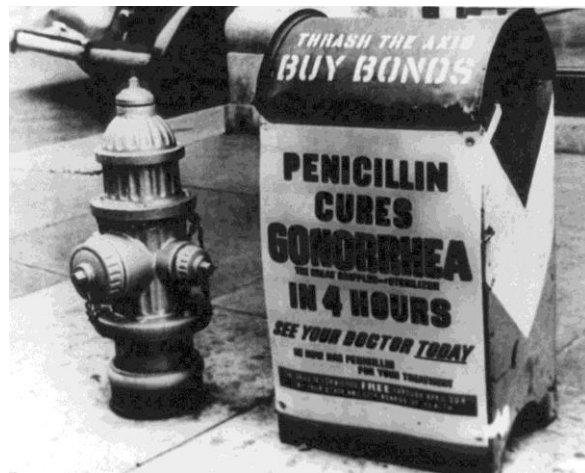
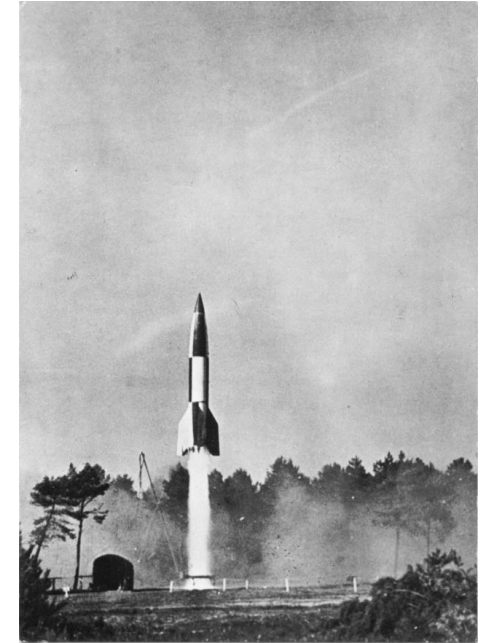
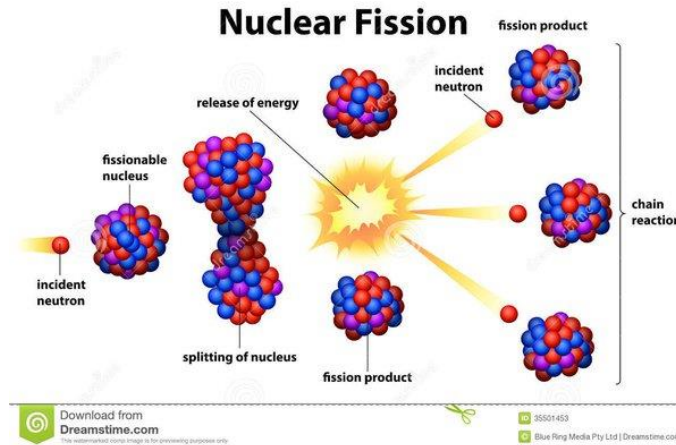
- SPF Q2 2022
- SPF Q3 2022
- SPF Q4 2022



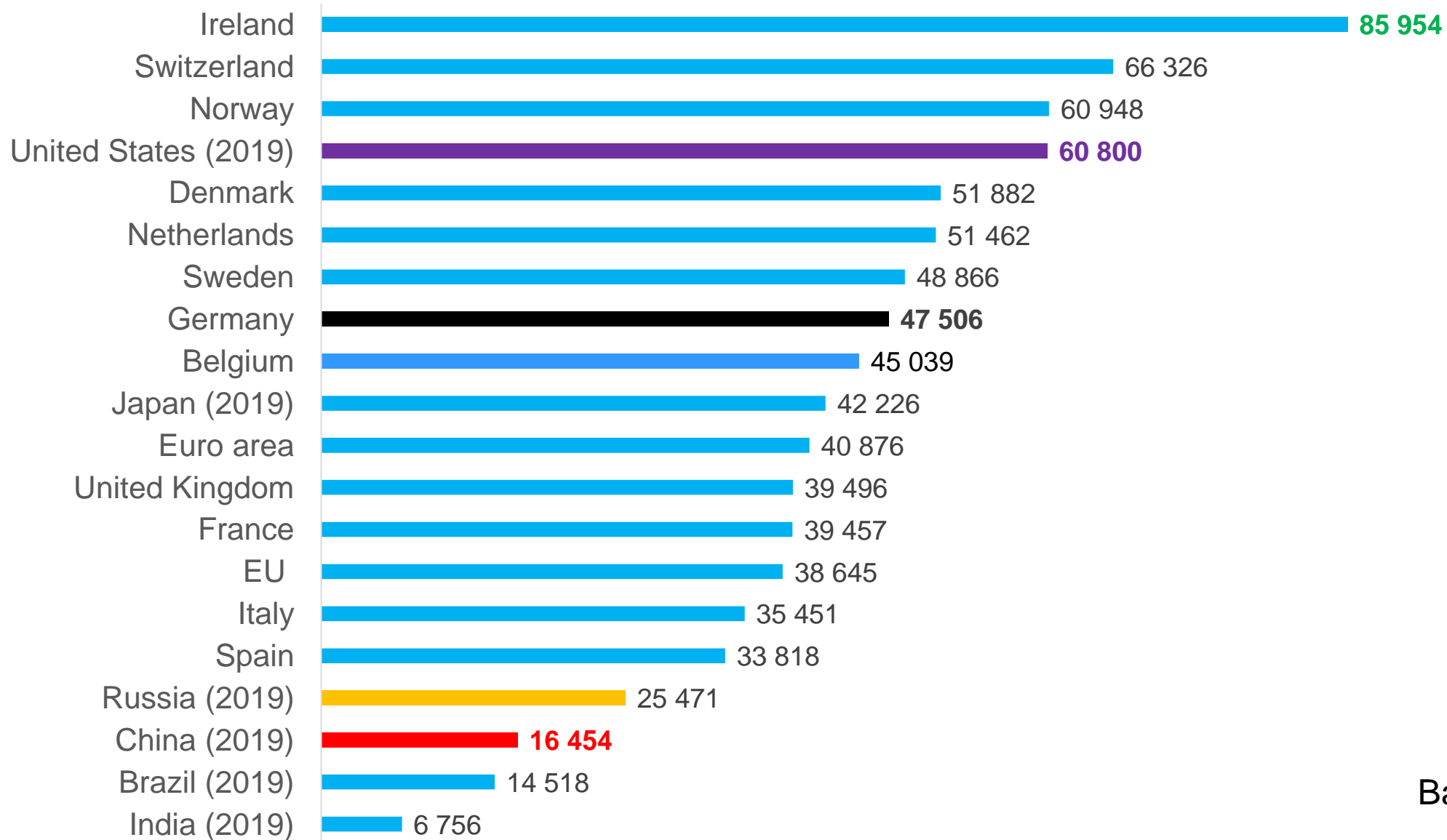
Energy-intensity to produce a unit of gdp



Wars accelerate innovation



GDP per capita (2020 dollars in constant ppp dollars of 2015)



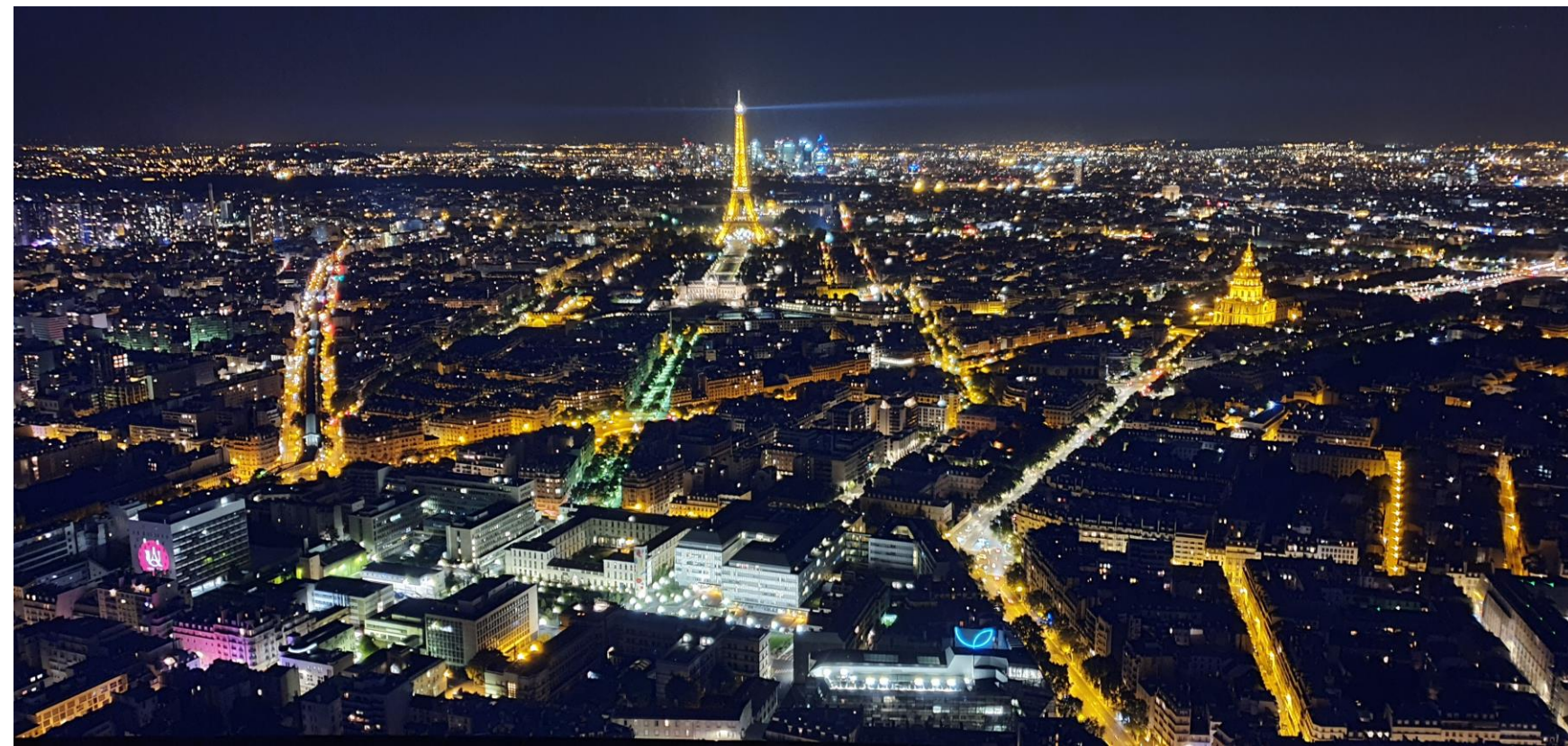
Based on OECD-data

It's the best of times, it's the worst of times

- Tri-lemma: only with a fast decline of inflation, it can be solved
- Economics is a game of relative prices
 - Higher energy prices (and carbon taxes) make sustainability cheaper
 - Higher gas prices make LNG look cheaper (unified gas market)
 - Higher labour costs make automation cheaper
 - Higher supply chain costs make just-in-case cheaper (decoupling, more inventories, local production...)
- It's the economy, stupid
 - You cannot win a war, only loose peace
 - But if you want to win piece, you need a strong economy

Solving the puzzle

- Not covid19 introduced a 'new normal' but the war in Ukraine marks a new era, literally a new iron curtain
- Are the 1970s and 1980s coming back ? Stagflation / greenflation
- The end of (further) globalisation in a polarised world (western values versus authoritarian; NATO versus former Soviet bloc)
- Just-in-case with severe supply chain disruptions
- Climate change will not wait but will the 'Green Deal' survive?
- Europe must stand firm and remember its historical lessons learned (Brexit, Green Deal, energy reliance, own defence system,...)



Geert Janssens

geert.janssens@etion.be

 @jrgeert

 YouTube **ETION**