

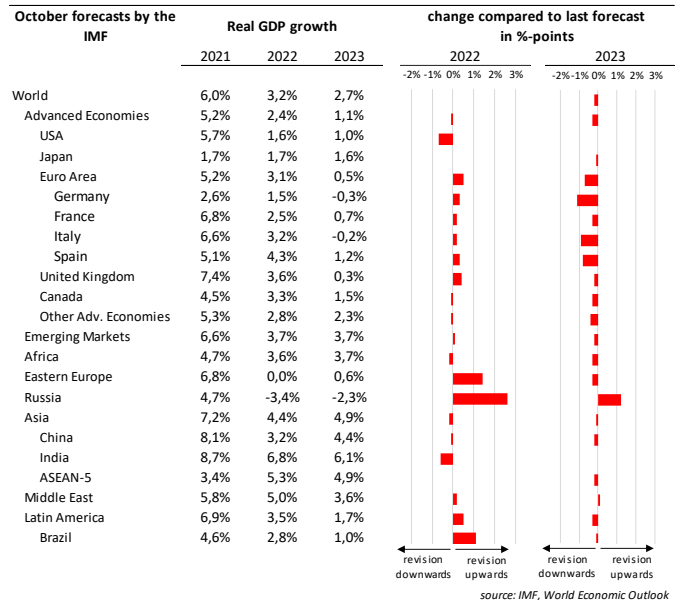


ECONOMIC SITUATION AND STRATEGY

14 October 2022

Are we in for a long recession?

The spectre of stagflation - i.e. a phase of stagnating economic growth and simultaneously high rates of price increases - buzzed around in the first half of the year and caused great concern among economists. In the meantime, not only has stagflation occurred, but the outlook for the overall economic situation has deteriorated further. Against the background of the latest economic figures, economists' warning lights are still on. In Germany, the inflation rate was ten percent in September and the real gross domestic product grew by only 0.1 percent in the second quarter of 2022 compared to the first. However, leading indicators such as the ifo business climate index, consumer confidence, high production costs or falling incoming orders speak a clear language and point to an economic slump in Germany. The situation in the Eurozone looks somewhat less problematic: Although prices also rose by ten percent recently, real gross domestic product - driven by strong catch-up effects in the tourism industry - grew by 0.8 percent. However, there are already signs of an economic downturn in the coming quarters. And in the USA, too, the course is set for a recession: The inflation rate is declining only slowly and in September was 8.2 percent, far above the target of two percent, and real GDP already shrank in the first half of the year. This means that the question is no longer whether the economic areas of the USA and the Eurozone are drifting into recession, but rather how long the economic slump will last and what measures can be taken to quickly return the economy to its old growth path.



In order to estimate the development of the real gross domestic product in the coming months, it is worth taking a look at the current forecast of the International Monetary Fund (IMF). As in the last three publications, the IMF has revised its global GDP forecasts downwards. In view of the largely very poor leading indicators, however, the downward adjustments are not surprising and, in our view, are still partly too optimistic. The IMF confirms its global GDP forecast of 3.2 percent for this year, but lowers it by 0.2 percentage points to 2.7 percent for next year. The risks to the outlook are on the downside, and the list of potential disruptive fires is long: a further escalation in the war between Russia and Ukraine, increasing geopo-

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litical fragmentation that hinders global trade and international cooperation, persistently high inflation rates, more difficult refinancing conditions especially for poorer economies, and the risk of a sovereign debt crisis or an escalation of the crisis in the Chinese real estate sector. If these risks materialise, GDP growth of just two percent in 2023 is conceivable - well below the historical average of 3.6 percent (1970 to 2021).

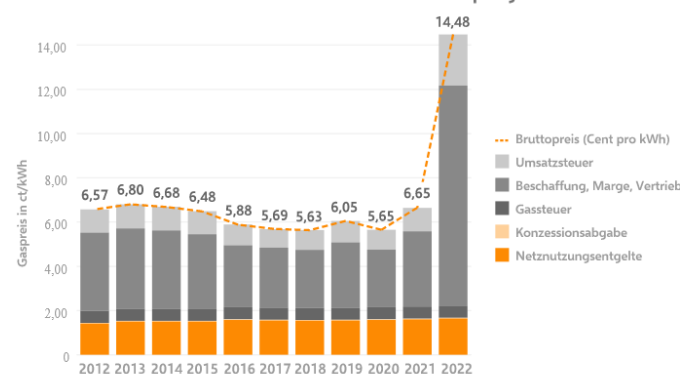
A look at the individual regions paints a gloomy outlook for 2023. The IMF has revised its GDP forecast downwards for almost all countries. Only India, the USA, the Middle East and Russia are exceptions. While the forecasts for the first three economies have been confirmed for the coming year, the IMF has adjusted its outlook for Russia for 2022 and 2023 significantly upwards. The reasons for the revision are the stronger than expected resilience of crude oil exports and strong domestic demand with stronger fiscal and monetary policy support. In contrast to the significant upward revision for Russia's GDP forecast, the revision for Germany is particularly negative. Compared to the July publication, the IMF has lowered its forecast by 1.1 percentage points to -0.3 percent for 2023. In our view, the growth expectations for the coming year still appear too optimistic, as the industry-intensive and export-oriented German economy is disproportionately affected by the extreme rise in production costs and a global economic slowdown. We therefore expect a decline in real gross domestic product of 1.4 percent next year.

However, things do not have to turn out quite so badly: If the price dynamics weaken and if energy costs in particular stabilise or even decline, this would be a clear sign of easing with regard to the real purchasing power of private households and for German industrial production. To what extent the gas price brake presented at the beginning of the week will provide a remedy and actually curb energy costs is difficult to assess at this point in time. In detail, the expert commission "Gas and Heat" envisages a two-step relief procedure: In a first step and as a financial bridge until the regular introduction of the gas price brake, the state will take over the monthly instalment payment in December for private gas and district heating customers. The basis for calculating the down payment is the consumption in September 2022. The rebate is taxable as a pecuniary advantage, whereby lower income groups benefit more due to an expected high tax allowance or due to the lower tax rate relative to higher income groups. In a second step, gas prices are to be capped for the period from March 2023 to at least April 2024. The

gas price for a basic quota corresponding to 80 percent of the annual consumption determined in September 2022 is to be fixed at twelve cents per kilowatt hour. Consumption above the basic quota will then be billed at the agreed energy price. Why did the expert commission choose 80 percent as the limit? It has to do with the fact that a 20 percent saving in gas consumption is probably necessary to prevent a gas shortage. To promote the competitiveness of German companies, the expert commission also envisages a gas price cap for industrial customers: The gas price is to be fixed at seven cents per kilowatt hour for a quota amounting to 70 percent of consumption in 2021.

Durchschnittliche Gaspreise

Haushalte mit einem Ø-Verbrauch von 20.000 kWh pro Jahr



Quelle: verivox.de

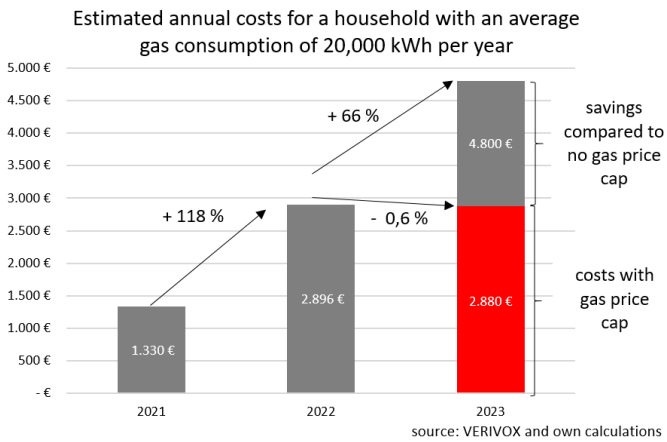
source: <https://www.verivox.de/gas/gaspreise/>; 13.10.2022

verivox

What does this mean for a private household? Of course, the savings vary depending on the amount consumed and the agreed energy price, but we have calculated the proposed relief package for a household with an annual gas consumption of 20,000 kilowatt hours. According to the comparison portal VERIVOX, the gas price in 2021 averaged 6.65 cents per kilowatt hour, resulting in annual costs of €1,330 (€110.84 per month). With an increase in the gas price to an average of 14.48 cents per kilowatt hour in the current year, the consumption costs in 2022 will increase by around 118 percent to 2,896€ per year (monthly 241.33€). Thus, in December 2022, our household will save an estimated €241.33 before taxes through the first stage of the relief package. If we assume the current gas price of around 24 cents per kilowatt hour for the following year, the annual costs would rise to €4,800 without the gas price cap (€400 per month) - this corresponds to a further increase of 66 percent compared to 2022. However, if we take the planned gas price cap into account in our calculation, the annual gas costs would even fall slightly to €2,880 (€240 per month). If our household maintains its gas consumption of 20,000 kilowatt hours, it would save €1,920 in 2023 due to the gas

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price cap. If the household managed to reduce its gas consumption by twenty per cent, the annual costs could be further reduced to 1,920€ (160€ per month).



It is difficult for us to make a final assessment of the proposed gas price brake, as the exact savings effects are difficult to quantify and depend very much on personal gas savings and the future gas price. Certainly, the expert commission's proposal leaves room for criticism, for example why the second stage will not come into force until March 2023, but one should give it credit that it was faced with an extremely ambitious goal. On the one hand, the package of measures is intended to generate noticeable financial relief in order to preserve the purchasing power

of consumers and social peace, and on the other hand to maintain savings incentives in order to avoid a gas shortage in Germany. A further constraint was that the measures could be implemented quickly and pragmatically. Against this background, the proposal for a gas price brake is a promising starting point that needs to be further refined in the coming weeks. For example, it should be considered how consumers who have already saved a lot of gas in the past and who benefit relatively less from the price cap can be relieved further. However, achieving complete social justice quickly reaches the limits of feasibility.

Overall, the proposed gas price brake, like the €9 ticket and the fuel rebate, should temporarily dampen the upward momentum of the inflation rate in Germany and reduce the risk of inflation getting out of hand. Even if the course is set for a recession in the coming months, there is reasonable hope that the economy will pick up quickly. In this context, further price dynamics are crucial: Should they decline in the coming months, the pressure on the central banks will be reduced and the interest rate adjustment path flattened. This would reduce the headwind for the economy and the stock and bond markets could recover.

Market data

Stock marketes	As of	Change versus				
	14.10.2022 09:17	07.10.2022 -1 week	13.09.2022 -1 month	13.07.2022 -3 months	13.10.2021 -1 year	31.12.2021 YTD
Dow Jones	30039	2,5%	-3,4%	-2,4%	-12,6%	-17,3%
S&P 500	3669	0,8%	-6,7%	-3,5%	-15,9%	-23,0%
Nasdaq	10649	0,0%	-8,5%	-5,3%	-26,9%	-31,9%
DAX	12356	0,7%	-6,3%	-3,1%	-19,0%	-22,2%
MDAX	22226	-1,4%	-12,2%	-12,9%	-34,2%	-36,7%
TecDAX	2694	-1,3%	-8,5%	-7,9%	-26,2%	-31,3%
EuroStoxx 50	3406	0,9%	-5,0%	-1,4%	-16,6%	-20,8%
Stoxx 50	3389	0,3%	-4,6%	-2,5%	-4,6%	-11,2%
SMI (Swiss Market Index)	10228	-0,8%	-6,1%	-6,2%	-13,4%	-20,6%
Nikkei 225	27091	-0,1%	-5,3%	2,3%	-3,7%	-5,9%
Brasilien BOVESPA	114300	-1,8%	3,2%	16,8%	0,7%	9,0%
Russland RTS	970	-3,5%	-24,5%	-13,4%	-47,7%	-39,2%
Indien BSE 30	58342	0,3%	-3,7%	9,0%	-3,9%	0,2%
China CSI 300	3842	1,0%	-6,5%	-11,1%	-22,2%	-22,2%
MSCI Welt	2412	-0,2%	-7,9%	-5,2%	-20,6%	-25,4%
MSCI Emerging Markets	855	-4,8%	-12,8%	-11,9%	-32,2%	-30,6%
Bond markets						
Bund- Future	136,22	-145	-717	-1640	-3272	-3515
Bobl-Future	119,80	56	-206	-598	-1470	-1344
Schatz-Future	107,10	16	-67	-254	-507	-494
3 Monats Euribor	1,36	71	145	194	191	195
3M Euribor Future, Dec 2017	2,29	6	13	0	283	3
3 Monats \$ Libor	4,01	10	72	150	389	380
Fed Funds Future, Dec 2017	4,22	11	22	0	415	3
10 year US Treasuries	3,91	3	49	101	237	242
10 year Bunds	2,19	-1	46	110	231	237
10 year JGB	0,25	1	0	5	17	18
10 year Swiss Government	1,25	-13	18	55	136	139
US Treas 10Y Performance	571,56	-0,5%	-4,1%	-7,5%	-17,3%	-18,2%
Bund 10Y Performance	534,80	-0,9%	-4,8%	-9,6%	-18,9%	-19,3%
REX Performance Index	435,30	-0,7%	-3,1%	-6,0%	-11,1%	-11,3%
US mortgage rate	0,00	0	0	0	0	0
IBOXX AA, €	3,67	16	79	141	327	319
IBOXX BBB, €	5,03	24	102	155	424	416
ML US High Yield	9,63	34	118	101	485	473
Convertible Bonds, Exane 25	6219	0,0%	-5,6%	-1,2%	-24,0%	-24,1%
Commodities						
MG Base Metal Index	377,47	-0,4%	-5,2%	1,5%	-18,4%	-18,2%
Crude oil Brent	94,92	-3,1%	1,7%	-5,0%	13,9%	21,1%
Gold	1667,16	-2,1%	-2,2%	-4,5%	-7,0%	-8,5%
Silver	18,90	-6,7%	-2,8%	-1,9%	-18,5%	-18,8%
Aluminium	2359,15	2,5%	2,6%	0,6%	-22,7%	-15,9%
Copper	7665,50	2,1%	-4,1%	4,9%	-21,5%	-21,3%
Iron ore	95,40	-0,2%	-5,9%	-14,1%	-22,0%	-15,2%
Freight rates Baltic Dry Index	1818	-7,3%	29,1%	-9,2%	-65,1%	-18,0%
Currencies						
EUR/ USD	0,9769	-0,3%	-4,0%	-3,0%	-15,5%	-13,7%
EUR/ GBP	0,8653	-1,6%	-0,3%	2,3%	1,9%	3,1%
EUR/ JPY	144,12	1,6%	-0,3%	4,4%	9,8%	10,5%
EUR/ CHF	0,9745	0,5%	0,8%	-0,9%	-9,1%	-5,7%
USD/ CNY	7,1785	0,8%	3,0%	6,8%	11,7%	12,9%
USD/ JPY	147,23	1,3%	1,8%	7,1%	30,0%	27,9%
USD/ GBP	0,89	-1,3%	2,3%	5,9%	20,8%	20,0%

Source: Refinitiv Datastream

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