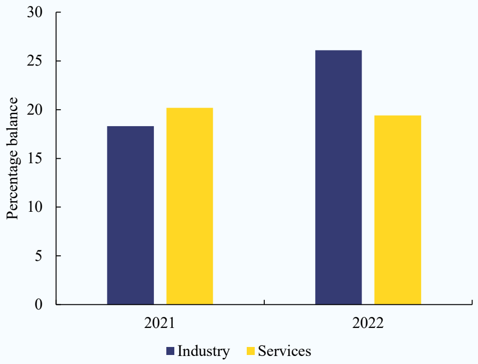
### *Box 1.3:* **Business managers are upbeat about investment this year**

While interim forecasts focus on aggregate GDP and do not project its demand components, the European Commission business surveys can provide useful indications on, inter alia, business investment plans in the first forecast year.

Twice a year – in spring and autumn – the Commission's survey for the manufacturing sector includes specific questions on investment. Since October/November 2021, similar questions have been included also in the services sector. In autumn, business managers are asked about investment realised/planned in the current year as well as plans for the following year. The survey also enquires about the purpose of investment (replacement, extension of production capacity, process streamlining, other) and the factors driving it (demand, profitability, technical factors, others). ([1])

*Graph 1:* **October/November 2021 investment survey results - EU**




In autumn 2021, the share of industry managers who assessed their investment to have increased in 2021 over the previous year was significantly higher than the share who reported it decreased, with the difference clearly exceeding its long-term average. This sharp increase is aligned with available National Account data on Gross Fixed Capital Formation (GFCF), which indicate for the EU without Ireland a 7.9% rebound during the first three quarters of 2021 compared with the same period of 2020. More broadly, over the period 2008 to 2021, the survey results correlate well with the GFCF data. In 2022, on balance, managers were expecting further expansion of their investment. A high positive balance in 2022 points to an increase in investment beyond what was projected in the Commission's autumn forecast. In services, managers estimated investment to have increased in 2021 compared to 2020, but the balance for 2022 was broadly even, suggesting stabilisation of investment on aggregate.

Upbeat investment plans for 2022 could be explained by the relatively high share of managers in industry who assessed their production capacity as insufficient to satisfy current order books and the expected change in demand in the coming months. The historically negative correlation between production capacity and investment is thereby confirmed for 2022. It must be noted, however, that at the time of the survey, risks related to a resurgence of the pandemic still appeared rather low, which may also explain the upbeat investment plans.

The increase in investment in 2021 and 2022 is broad-based across industrial groupings. In particular, the motor vehicle sector shows a strong rebound in the balance of managers' answers for 2022. This suggests a particularly strong investment growth in this sector this year, after an extremely negative final assessment of investment goods' producers in 2020 and only a mild recovery in 2021. An explanation could be the ongoing sweeping transformation of the sector from combustion engines to electric vehicles, which requires huge investment that was probably suspended in 2020/2021 due to the pandemic and the supply bottlenecks of raw materials (e.g. metal) and semi-conductors.

Also in the services sector the increase in investment in 2021 and 2022 is broad-based among sub-sectors. For 2022, the balance remains positive but decreases markedly among managers in 'real estate activities' and 'repair of computers and personal and household goods' branches.

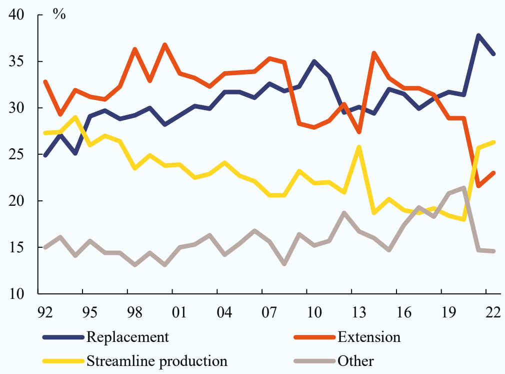
Graph 2 shows that investment in 2021 and 2022 mainly serves the purpose to streamline processes or replace worn-out plants or equipment.

([1]) For a full review of the results, see Technical paper 053, European Business Cycle indicators, 4th Quarter 2021 "Focus on investment activity and business sentiment across subsectors after COVID".

*(Continued on the next page)*

Box (continued)

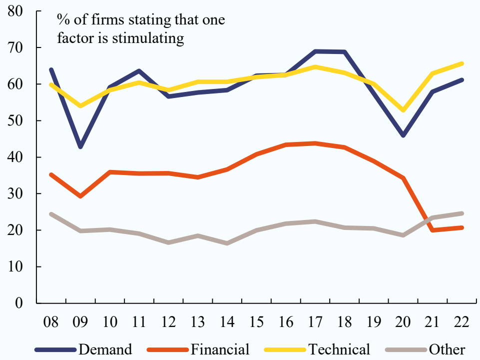
*Graph 2:* **EU – Industry survey - Structure of investment**




These trends suggest ongoing technological changes in equipment, including towards new green and digital technologies. Companies may also seize the opportunity – and are indeed often encouraged through specific policies - to replace outdated equipment with more efficient technologies.

Turning to the drivers of investment, the autumn Investment Survey points to the rebound in demand and technical factors as stimulating their investments in 2021 and 2022. This seems plausible in the light of the return of demand after COVID, as well as new investment needs related to the green and digital transition. These trends hold for both industry (See graph 3) and services. In particular for services, demand is considered to stimulate investment by more than 50% and 70% of managers in 2021 and 2022, respectively.

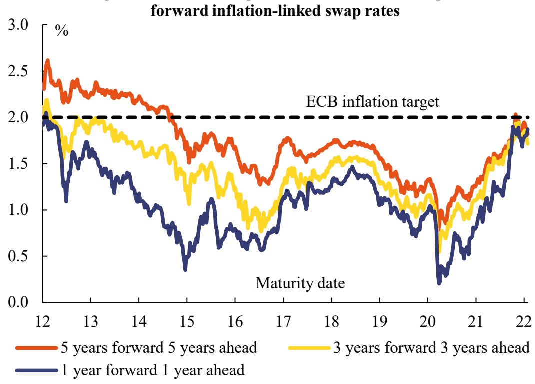
*Graph 3:* **EU – Industry survey – factors stimulating investment**




chain bottlenecks and energy prices is expected to lower inflation below 2% in 2023. This forecast sees a limited impact of higher prices on wages, as some residual labour market slack and continuous uncertainty related to the pandemic weaken claims for stronger wage growth. In addition, production bottlenecks and rising input costs weigh on companies' profit margins, further limiting room for wage hikes.

Market-implied inflation expectations remained at broadly similar levels to those around the cut-off date of the Autumn Forecast, with the widely followed 5-year forward 5-year ahead indicator standing at 1.9 at the end of January (see Graph 1.15). Meanwhile, selling price expectations reached record high levels in November, eased in December, to rise again in January across all surveyed business sectors (i.e. industry, services, retail trade and construction).

*Graph 1.15:* **Inflation expectations derived from implied forward inflation-linked swap rates**




*Source:* Bloomberg

## 1.7. RISKS TO THE OUTLOOK

Uncertainty in the economy increased in the winter months, according to the Commission's surveys, highlighting that risks surrounding the outlook remain high. However, the materialisation of some adverse risks since the Autumn Forecast leaves the balance of risks to the growth outlook broadly even. By contrast, the balance of risks to the inflation forecast remains skewed to the upside.