The Forward View: Global Feb 2024

Rate cuts expected in 2024 but inflation path remains uncertain

NAB Group Economics

Overview

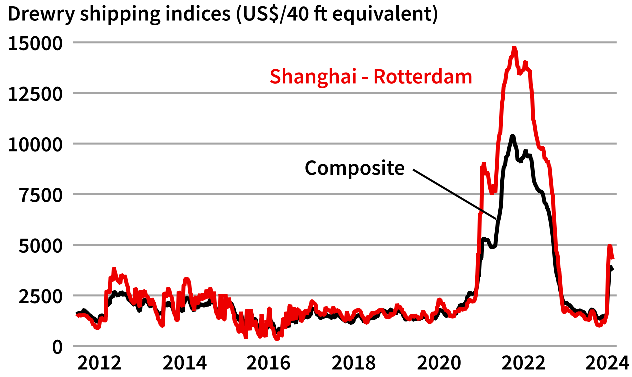
- While inflation has slowed considerably from its peaks (particularly in advanced economies (AEs)), disinflation stalled at the end of 2023. Disruptions to trade activity, due to attacks against shipping in the Red Sea, has introduced new uncertainty around the path of inflation this year.
- That said, with policy rates at restrictive levels, growth weak (or expected to slow in the case of the US) and significant progress in bringing inflation close to central bank targets, rate cuts by the major advanced economy central banks are expected in 2024 (ex. Japan).
- Growth in the United States has continued to outperform other advanced economies, with the Euro-zone, UK and Japan at, or near recession, at the end of 2023. Restrictive monetary policy and fiscal contraction is anticipated to drive subdued growth across AEs this year.
- Slower activity in AEs will constrain demand for emerging market produced goods. An uptick in Chinese export volumes in late 2023 saw EM exports edge higher, albeit this coincided with a steep fall in China's export prices.
- Overall, we expect the global economy to expand by 2.8% in 2024 (up from 2.7% previously), reflecting stronger than anticipated growth in the US providing a higher base for growth this year. Despite this revision, this would still be the weakest rate of growth since 2002 (excluding the extreme outliers of the Global Financial Crisis and the initial wave of COVID-19). We continue to anticipate a modest improvement in 2025, up to 3.0% – but for growth to remain below its long-term average (3.4% between 1980-2022).
- There remain a range of uncertainties. Should the pause in disinflation continue, this could delay policy rate cuts (impacting 2025 growth). Geopolitical tensions remain, including the Russia-Ukraine war, Middle East conflict and US-China tensions.

Table of Contents

Global growth forecasts

	2020	2021	2022	2023	2024	2025
US	-2.2	5.8	1.9	2.5	2.1	1.4
Euro-zone	-6.2	5.9	3.4	0.5	0.4	1.0
Japan	-4.2	2.6	1.5	1.9	0.1	0.5
UK	-10.4	8.7	4.3	0.1	0.0	0.7
Canada	-5.0	5.3	3.8	1.1	1.0	1.3
China	2.2	8.1	3.0	5.2	4.5	4.8
India	-6.0	8.9	6.7	7.0	5.8	6.2
Latin America	-7.0	7.4	4.1	2.3	1.4	1.9
Other East Asia	-2.8	4.5	4.2	3.2	3.4	3.9
Australia	-2.1	5.6	3.8	2.0	1.4	2.0
NZ	-1.4	5.5	2.4	0.7	-0.1	2.7
Global	**-2.8**	**6.3**	**3.4**	**3.2**	**2.8**	**3.0**

Disruptions to Red Sea shipping has seen freight rates jump to their highest levels since late 2022



Gerard Burg, Senior Economist | Antony Kelly, Senior Economist | Alan Oster, Chief Economist

Financial and commodity markets: Fresh supply disruptions threaten path of disinflation

The slowing in global inflation stalled at the end of 2023, with global consumer prices increasing by 5.3% yoy in December (having edged up from 5.2% yoy in November). Inflation has persisted at higher rates among emerging market economies – at 6.7% yoy in December – albeit there remain highly divergent trends between individual countries in this grouping.

In contrast, inflation trends have generally been broadly similar across most major advanced economies (with Japan being the notable exception). Consumer prices increased by 3.3% yoy in December (up from 3.1% yoy in November) but still the second lowest reading since July 2021 (when inflation was on its upwards path).

Attacks on shipping through the Red Sea have added some uncertainty around the path of inflation going forward. Avoiding this region adds around 10 days to a container vessel's journey between Europe and Asia. Shipping rates in late January surged to their highest levels since late 2022. An IMF study in 2022 suggested that a doubling of freight rates adds around 0.7% to global inflation – with the impacts lasting around 18 months – albeit impacts vary by country and are typically smaller in those having credible monetary policy (typically AEs).

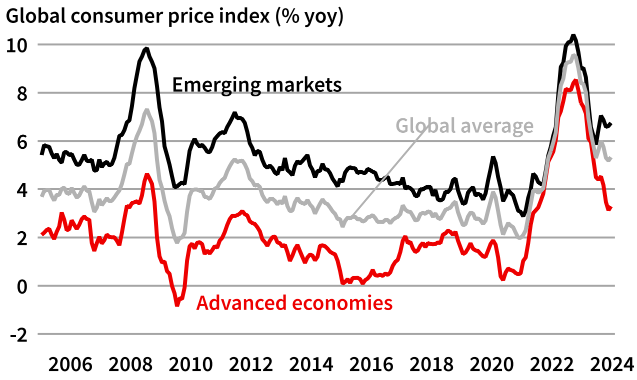
Inflation in advanced economies retreated significantly over H2 2023, bringing rates close to central bank targets. With policy rates at restrictive levels (ex. Japan) and growth sluggish (or, in the case of the US, expected to slow), rate cuts by the major advanced economy central banks are expected in 2024 (again ex. Japan). For the US we expect 125bps of rate cuts this year, while market pricing is around 90bps but has been volatile of late.

Global equity markets have rallied since late October, when expectations around policy rate cuts started to build. US markets have led the way, with the MSCI US index in mid-February up over 22% from its trough. Unlike various rallies in 2023, there were notable gains for equities outside the eight largest technology stocks (albeit these stocks still recorded the largest increase). In contrast, other advanced economy equity indices were around 13% higher and emerging markets around 12%.

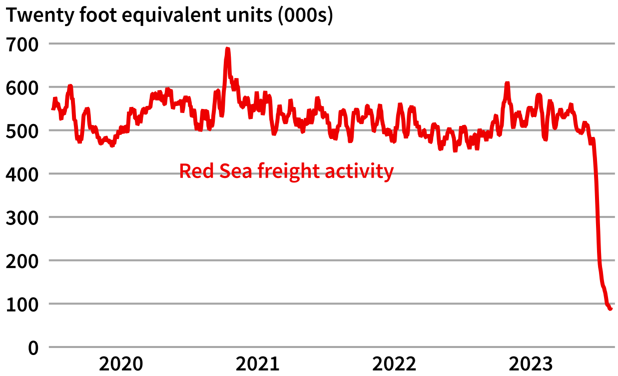
The smaller increase in equities in emerging markets reflects the sharp downturn in Chinese equity markets in early 2024. At the time of writing, authorities' efforts to stabilise these markets have had little success, however various studies suggest that income effects are more significant than wealth effects for China's consumption (limiting the impact on growth in 2024).

Commodity prices (S&P GSCI measure) have trended higher since early December, albeit this has been driven by energy commodities. Volatility in oil prices reflects the impact of weaker demand (due to slower global growth) as well as efforts by OPEC+ to restrict supply.

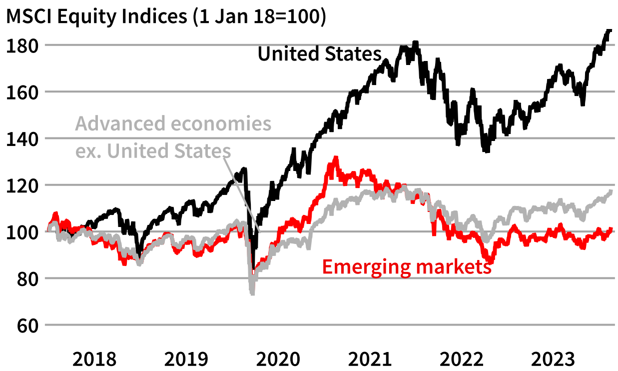
Disinflation stalled in December



Red Sea freight activity has plummeted



US equities surge to record highs



Chinese equities plunged in early 2024

Sources: Macrobond, NAB Group Economics

Advanced economies: US ended 2023 on a strong note; UK & Japan in 'technical' recessions

The US economy remains the clear outperformer, with the other major advanced economies (AEs) struggling. While US GDP growth slowed in Q4, at 0.8% it was another strong outcome. After declining in Q3, the Euro-zone saw meagre growth in Q4, while monthly indicators point to moderate growth in Canada but only sufficient to reverse the Q3 fall. In contrast, GDP in both the UK and Japan GDP fell the second quarter in a row.

Two consecutive quarters of negative growth is a popular recession measure. There has been a focus on the recession risk from the significant tightening in monetary policy since the start of 2022 so, while the weakness in the UK in 2023 was not unexpected, the shift in Japan has surprised given that monetary policy has not materially tightened and its economy grew strongly in H1 2023.

Households and businesses in Japan have cut back on consumption and investment respectively in each of the last three quarters. The weakness in consumption reflects falling real (inflation adjusted) income as wages have not kept up with inflation (while for the other major AEs real wages have turned positive). In contrast, there was a notable pick up in US real household income in 2023, supporting robust consumption growth.

The fall in business investment in Japan is harder to explain as corporate profits have been rising but may reflect the relative strength of the less capital intensive services sector while manufacturing has struggled.

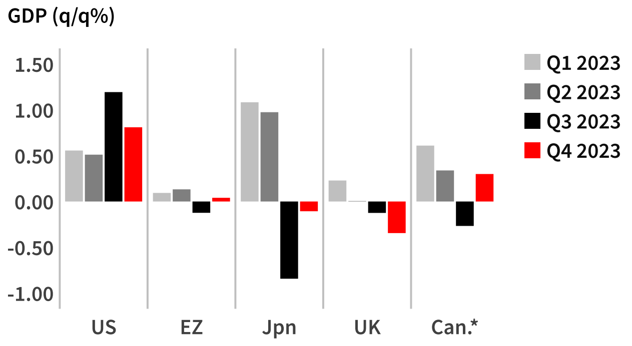
Both Western Europe and Japan, as net energy importers, endured a large negative shock to national income as a result of Russia's invasion of Ukraine. This partly unwound over 2023, but at the same time fiscal policy turned restrictive in these countries (a related development given the household and business energy support measures put in place by governments). This will continue into 2024 although we expect some further reductions in energy prices which should again provide some offset.

In contrast, US fiscal policy was supportive of growth in 2023 but this is set to turn around this year. This is one reason why we expect US growth to slow in 2024 both in absolute terms and relative to the other major AEs.

Business surveys suggest less of a gap between the AEs than does the GDP data. The UK PMI has picked up over recent months and its composite PMI is at a similar level to that of the US, with Japan close by. The Euro-zone remains weak with its PMI below the break-even level.

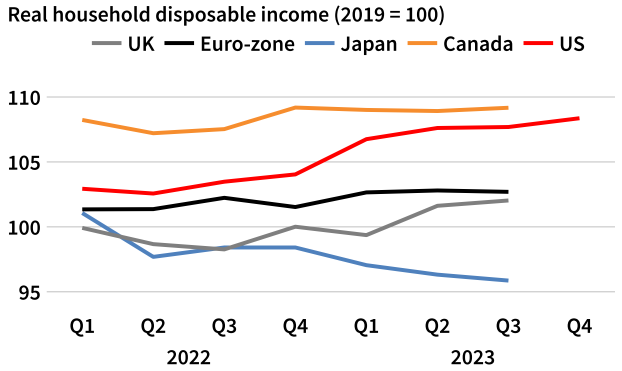
With monetary policy settings still restrictive and fiscal policy also a headwind, we expect only subdued major AE growth over 2024. While we expect central banks to ease policy this year (ex. Japan) – and this has already contributed to some improvement in financial conditions – the lagged impact of monetary policy means this is more of a factor for 2025.

US strong end to year, but weak elsewhere

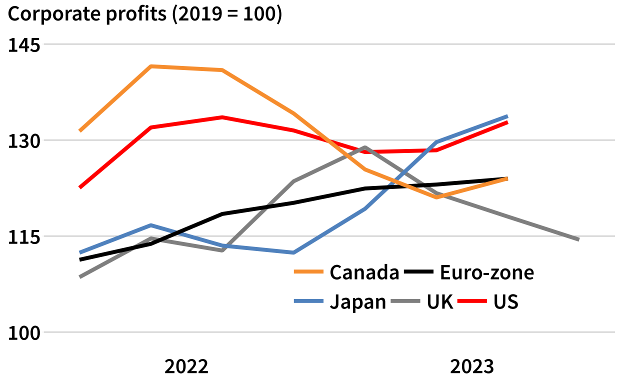


Source: Macrobond. NAB forecast for Canada in Q4

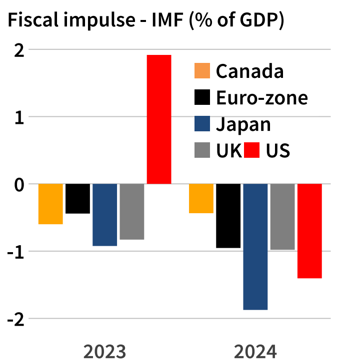
Outside UK/US h'hold real income flat or falling

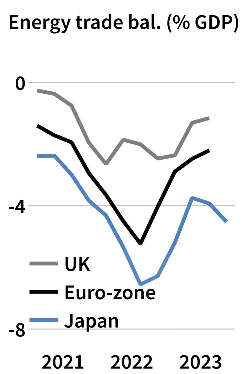


Profits off peaks in some AEs



It's not just interest rates that matter





Emerging markets: China's gains in export volumes secured by deep discounting

Emerging market business surveys provide some of the most timely indicators of activity. The EM composite PMI continued to edge higher in January – up to 53.5 points (from 53.0 points in December) – from its recent cycle low in October.

The key contributor to this uptick was the services sector, with the EM services PMI rising to 54.2 points (from 53.8 points in December). India was the key driver of the increase in January, which continues to record very strong positive readings, along with a small upturn in Brazil.

In contrast, the EM manufacturing PMI only edged higher in January, up to 51.1 points (from 50.9 points previously). Again, India and Brazil were the main contributors, with no change in China's reading and a dip in the Russian measure.

China narrowly exceeded its growth target in 2023 (growing by 5.2% versus the "around 5%" goal). Reports from the Economic Work Conference in December suggested this target would be unchanged in 2024, but there have been recent rumours that a cut to "around 4.5%" could be announced in March.

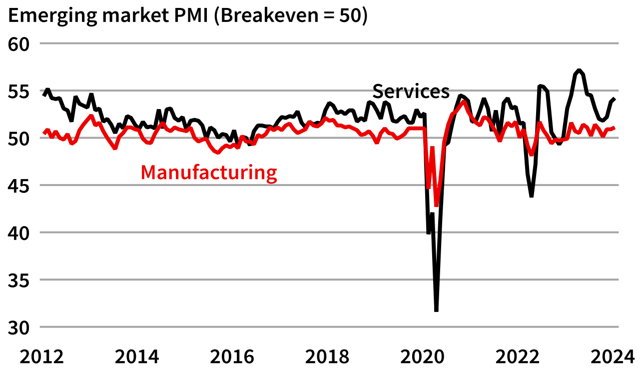
China's quarterly economic growth slowed in Q4 – down to 1.0% qoq (according to official seasonally adjusted data) from 1.5% qoq in Q3. There remain a number of headwinds to China's growth – most notably a range of constraints on consumption, along with the prolonged property downturn and subdued demand for lending – with the latter impacting efforts by authorities to stimulate the economy via monetary policy.

Emerging markets are generally more trade dependent than advanced economies (AEs). Slowing activity in AEs, reflecting the lagged impacts of monetary tightening along with stricter lending standards, will constrain demand for EM produced goods. That said, growth in EM export volumes edged up in the latter months of 2023 – up by 0.9% yoy (3mma) in November – compared with contractions across the middle of the year. This increase was driven by an uptick in exports from China, which rose by 5.7% yoy (3mma), while other EM exports fell by 1.9% yoy (3mma).

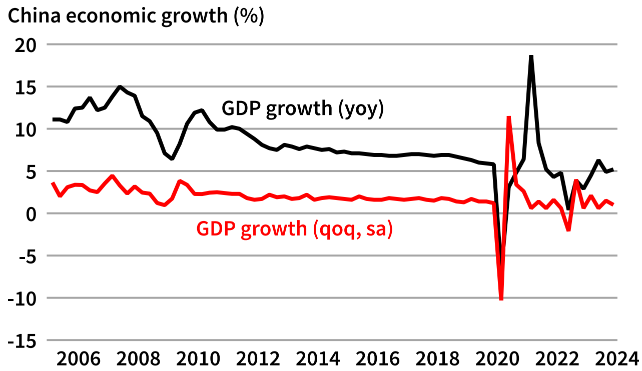
It is also worth noting that this increase in Chinese export volumes has coincided with a steep fall in export prices. China Customs data showed that export volumes rose by 13.3% yoy in December, while prices fell by 8.4% yoy (in local currency terms). The 9.7% yoy fall in export prices in October was the largest on record.

While US trade data suggests that Mexico overtook China as the largest source of imports in 2023, this does not reflect a decoupling in US-China trade. Mexico's imports of Chinese goods were also substantially higher, demonstrating a re-routing in trade activity, potentially to avoid still existing tariff measures.

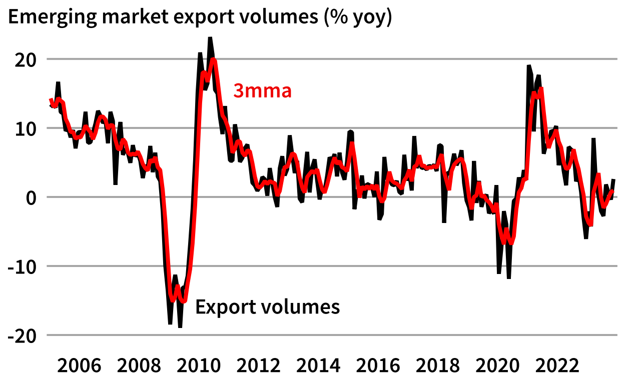
India the key driver of stronger EM PMIs



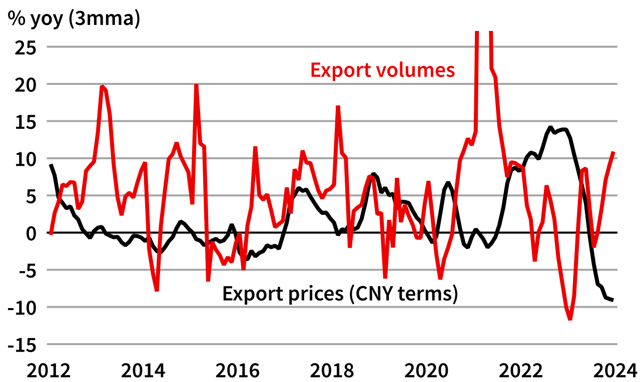
China's economy faces headwinds in 2024



EM export volumes edged up in late 2023…



…with volumes surging from China on price cuts



Global forecasts and risks: global surveys improve in early 2024, but we expect growth to slow

Preliminary data for global growth point to a slowing trend in Q4 2023. Growth for major advanced economies was essentially unchanged, albeit with disparity between countries. China's quarterly growth slowed in Q4, while East Asia eased. India and Russia are key uncertainties.

Global business surveys started 2024 on a stronger footing, with the JPMorgan global composite PMI moving up to 51.8 points in January (from 51.0 points in December). This up from the recent lows of 50.0 points in October 2023.

An uptick in the global manufacturing PMI was the key driver of this trend – moving from a negative 49.0 points in December to a neutral 50.0 points in January. A less negative outcome for advanced economy manufacturing – moving up to 48.9 points (from 47.0 points previously) was the main contributor to this result.

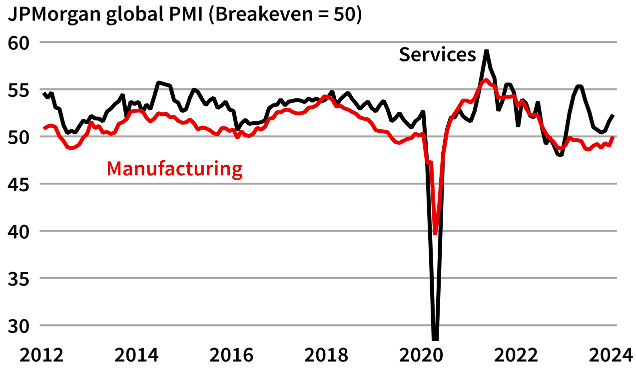
The increase in the global services PMI was comparatively muted – up to 52.3 points (from 51.6 points in December). Once again the advanced economies were the main contributor to the increase.

Our forecast for the global economy has been revised slightly higher this month. This reflects the stronger than anticipated growth in the United States in Q4 2023, providing a higher base for growth this year. Overall, we expect the global economy to expand by 2.8% in 2024. Despite this revision, this would still be the weakest rate of growth since 2002 (excluding the extreme outliers of the Global Financial Crisis and the initial wave of COVID-19). We continue to anticipate a modest improvement in 2025, up to 3.0% – but growth remaining below its long- term average (3.4% between 1980-2022).

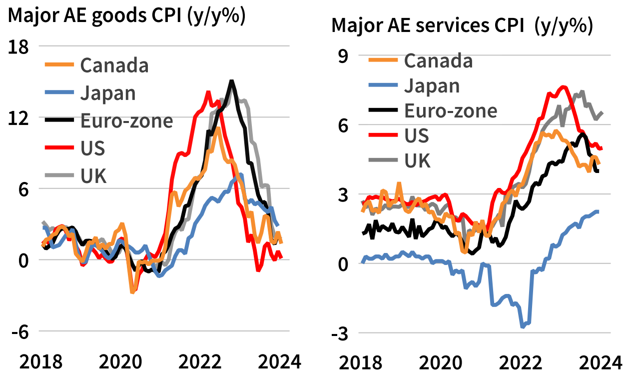
The path of inflation (particularly in advanced economies) remains a key uncertainty to the global outlook. While goods price inflation has been weaker – which could continue for a while – given steep declines in Chinese factory gate prices – services prices have remained sticky (albeit with variation across different countries). Should the pause in disinflation seen in late 2023 continue, this could delay the start of central bank policy rate cuts in 2024, impacting growth, particularly next year.

Geopolitical tensions could also disrupt economic activity during the next few years – with an intensification of these tensions in recent months. Russia's war against Ukraine is now approaching its second anniversary, with Russia threatening Poland and the Baltic states in recent months. Tensions in the Middle East have increased, with Houthi rebels in Yemen (reportedly supported by Iran) disrupting shipping through the Red Sea. Similarly, the relationship between China and the United States remains strained, with presumptive Republican nominee for President, Donald Trump, threatening an across-the-board 60% tariff on Chinese imports if he wins the election in November.

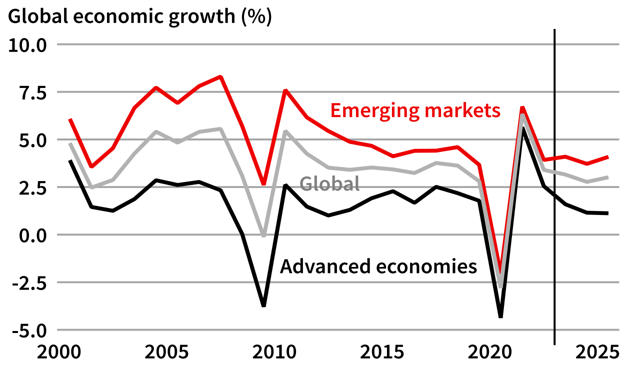
Advanced economies drove PMIs higher in January



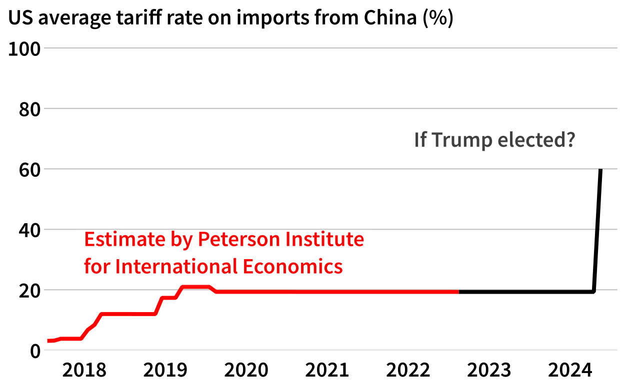
Service inflation sticky in a range of key economies



Global economy set to slow, led by AEs



Trump campaign statements point to risk of trade wars re-emerging if elected



Group Economics

Alan Oster
Group Chief Economist
+(61 0) 414 444 652

Jacqui Brand
Executive Assistant
+(61 0) 477 716 540

Dean Pearson
Head of Behavioural & Industry Economics
+(61 0) 457 517 342

Australian Economics and Commodities

Gareth Spence
Senior Economist
+(61 0) 422 081 046

Brody Viney
Senior Economist
+(61 0) 452 673 400

Behavioural & Industry Economics

Robert De Iure
Senior Economist – Behavioural & Industry Economics
+(61 0) 477 723 769

Brien McDonald
Senior Economist – Behavioural & Industry Economics
+(61 0) 455 052 520

International Economics

Tony Kelly
Senior Economist
+(61 0) 477 746 237

Gerard Burg
Senior Economist – International
+(61 0) 477 723 768

Global Markets Research

Skye Masters
Head of Research
Markets, Corporate & Institutional Banking
+(61 2) 9295 1196

Important notice