The Forward View: Global July 2024

NAB Group Economics

Overview

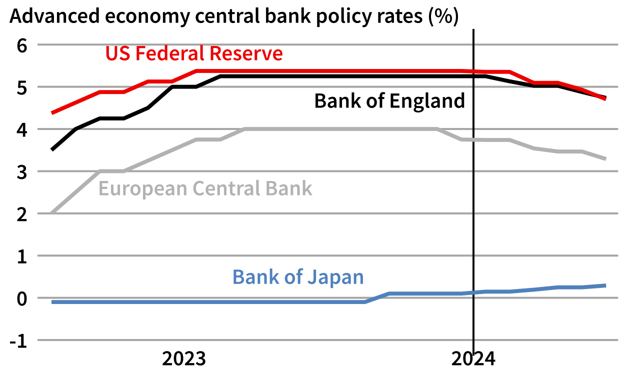
- Global inflation remains elevated and, edged higher in May to 5.1% yoy, with recent upward pressure coming from emerging markets. Advanced economy inflation has remained comparatively stable in 2024 and was 2.6% yoy in May, slightly down from 2.7% yoy through Q1.
- Recognising the reduction in inflation from its peak that has already occurred, cooling labour markets and that monetary policy is clearly restrictive, the major AE central banks (outside of the Bank of Japan) have started easing rates or are expected to do so soon. Low inflation readings in the US in May and June, as well as a cooling labour market, are laying the foundation for the Fed to start easing in September.
- The major advanced economies appear to have generally experienced moderate growth in Q2, except the UK which again appears to have grown rapidly. In the US, we are expecting growth in Q2 to be similar to that in Q1; still reasonable but well down from the robust pace of H2 2023.
- There were contrasting election results in the UK and France, with a clear winner in the former but a coalition government will need to be formed in France. The new UK government is promising supply side reforms but in both cases government action will be constrained by needed budget repair.
- Emerging market business surveys weakened considerably in June, but from a high level. China's economy grew by 4.7% yoy in Q2 – down from 5.3% yoy in Q1, with weak domestic demand an ongoing headwind; while a surge in export volumes has supported growth it is unlikely to be sustainable.
- Our global forecasts are unchanged and we continue to expect soft global growth of only 3.0 to 3.1% between 2024 and 2026. There remain a range of risks around the outlook, including the extent and speed of central bank easing, as well as geo-political tensions (Ukraine/Russia, Middle-East, South China Sea). Trade protectionism continues to ramp up and could take a further turn for the worse if, as is now expected, Donald Trump is elected as President in November.

Table of Contents

Global growth forecasts

	2022	2023	2024	2025	2026
US	1.9	2.5	2.2	1.4	1.8
Euro-zone	3.5	0.6	0.8	1.2	1.4
Japan	1.5	1.8	-0.2	0.7	0.7
UK	4.3	0.1	1.1	0.9	1.2
Canada	3.8	1.2	0.8	1.3	1.8
China	3.0	5.2	4.7	4.6	4.4
India	6.4	7.7	6.6	6.2	6.4
Latin America	4.2	2.2	1.3	2.1	2.1
Other East Asia	4.2	3.1	3.8	3.7	3.9
Australia	3.9	2.0	1.0	2.1	2.1
NZ	2.4	0.6	0.2	2.5	3.1
Global	**3.5**	**3.2**	**3.0**	**3.0**	**3.1**

Central banks moving to ease (ex Japan) – markets now expect start of Fed easing cycle to be in September



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Financial and commodity markets: monetary easing still waiting on inflation to subside

Recent months have seen global measures of inflation persist at comparatively high levels. In May, global inflation edged higher to 5.1% yoy, having lost momentum following the decline to 4.8% yoy in January. Recent upward pressure has come from emerging markets, particularly surging price growth in Turkey (75% yoy in May) and parts of Africa (including Nigeria, Angola, Egypt and Ghana).

In contrast, advanced economy inflation has remained comparatively stable in 2024 – remaining at 2.6% yoy in May, following on from 2.7% yoy in each month of Q1. In most of these economies, growth in goods prices has been relatively subdued, while services prices have continued to climb at a faster pace.

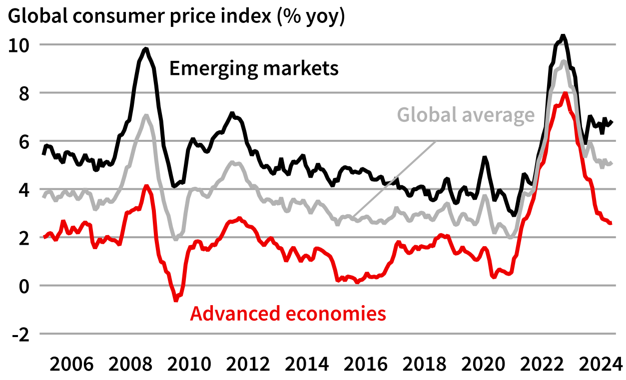
The lack of clear direction with respect to inflation means that there remains uncertainty around monetary policy in major economies although, outside of Japan, the bias is to ease policy. Both the Bank of Canada and European Central Bank cut policy rates in June and further cuts are expected, although the timing maybe be sensitive to incoming data, with inflation in both Canada and the Euro-zone ticking up recently. Low inflation readings in the US in May and June, as well as a better balanced labour market, are laying the foundation for the Fed to start easing in September – this is now fully priced by markets – barring material upside surprises in upcoming inflation reports.

The French legislative elections saw considerable support for populist candidates on the right and left, both of which have plans that would increase the deficit. This would further pressure the government's balance sheet – the budget deficit was already 5.5% of GDP in 2023, compared with the EU ceiling of 3%. In response, the 10-year bond spread for French and German government bonds rose to its highest level since the end of the European sovereign debt crisis in 2012. The lack of an outright majority, and the need for a coalition to be assembled to form a new government, suggests that policy inertia and political instability lie ahead.

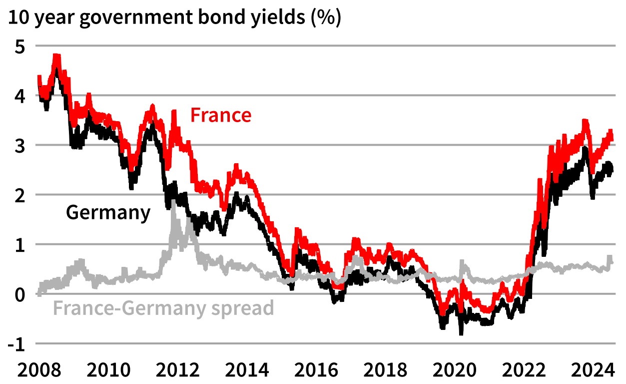
Global equity markets have continued to trend higher – with MSCI indices broadly moving up from late-October 2023. Both US markets and other advanced economies rose to fresh record highs in mid-July, while emerging market indices rose to their highest levels since February 2022.

Trends in commodity markets remain highly mixed. Base metal prices, which surged in May due to speculative inflows into futures markets, retreated in June. In contrast, energy prices in the S&P GSCI rose considerably – led by a US$10/barrel increase in crude oil prices over the month, in part reflecting fears of further Middle East conflict, this time in Lebanon.

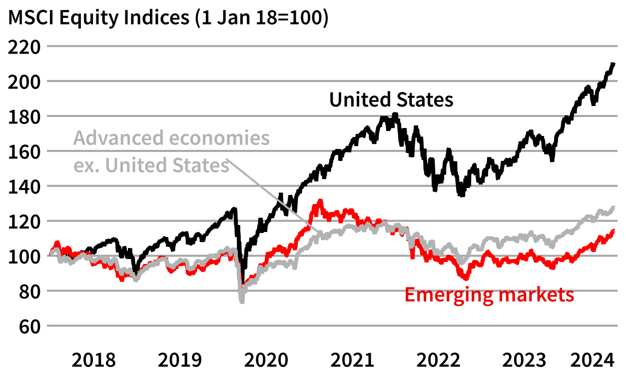
AE inflation has remained relatively stable in 2024



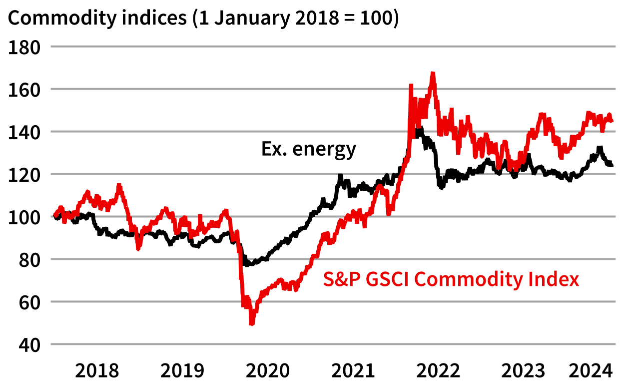
France's bond spread higher on budget concerns



Global equities have continued to trend higher



Higher energy prices but base metals pulled back in June



Advanced economies: UK leading the way on growth…for now

We expect that the major advanced economies generally experienced moderate growth in Q2, except the UK which again appears to have grown rapidly.

Business survey readings for the major advanced economies (AEs) gave up ground in June. While the Q2 average in the Euro-zone was clearly higher than in Q1, the recent loss of momentum is consistent with our view that growth was likely to be moderate this year. In part this reflects a negative fiscal policy impulse, highlighted by seven European economies, including France and Italy, being placed into 'excessive deficit procedures' which will limit their budget headroom.

The UK grew more quickly than the other major AEs in Q1 and is on track to do so again in Q2. Monthly GDP in May increased by 0.4% and on a three-month basis was up 0.8%. Even with no growth in June, GDP would be up 0.6% in Q2, which has led us to revise up our UK forecast. Growth at this pace does not look sustainable; while household incomes are seeing a boost from easing inflation, interest rates remain high and fiscal policy is likely to remain a headwind, as the new government is committed to following the same fiscal rules as its predecessor. Supply-side reforms, e.g. for housing, may help but will take time to bear fruit.

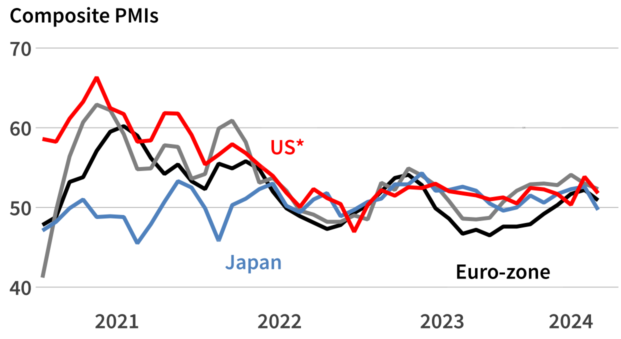
The fall in the Japanese composite PMI in June raises further doubts about its economy, which contracted in two out of the last three quarters (to Q1). However, partial data available to May for household consumption and industrial production look solid – underpinning our forecast that growth resumed in Q2 – but machinery orders are down and the auto testing scandal is impacting car production.

In the US, we are expecting growth in Q2 to be similar to that in Q1 (around 0.4% q/q); still reasonable but well down from the robust pace of H2 2023. Household consumption is growing moderately, but many other partial indicators (for housing, trade and business investment) have been soft over recent months.

While US growth over the last year has been robust, the unemployment rate is creeping upwards, while Canada has seen a notable lift in unemployment as jobs growth has not matched very strong population growth. In contrast, the Euro-zone, with softer growth, has seen unemployment fall. However, taking into account other labour market indicators, such as job vacancies, labour market pressures have eased across the majors.

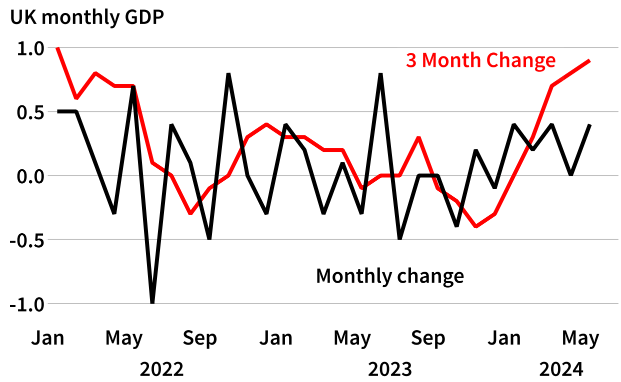
We expect growth to remain modest this year, but to strengthen modestly over 2025 and 2026. This partly reflects the expected easing in monetary policy (which has already begun in the Euro-zone and Canada). A key uncertainty is the direction of the US fiscal and trade policy which won't become clearer until the results of the elections in November are known.

Business surveys eased in June

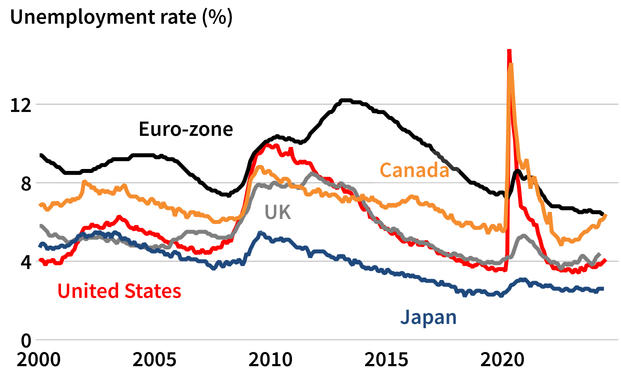


* Based on S&P Global and NAB weighted composite of US ISM PMIs

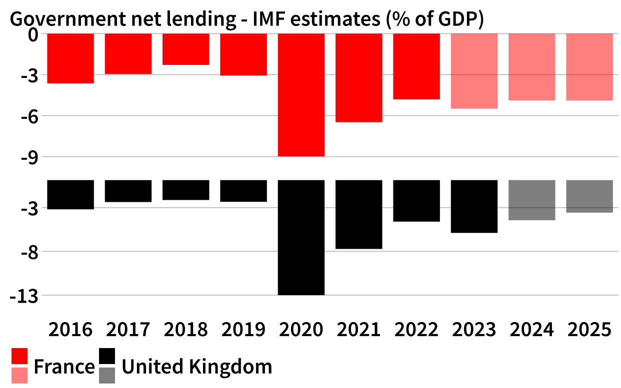
Business surveys eased in June UK GDP acceleration continued into May



Labour market pressures easing



Elections – new governments, same fiscal constraints



Emerging markets: China's economy slowed in Q2, despite help from exports that raised tensions

Emerging market business surveys weakened considerably in June. The EM composite PMI dropped to 53.3 points (down from 54.4 points in May). It is worth noting that the level in May was among the highest recorded in the past decade.

The key driver of this decline was the services sector – with the EM services PMI dropping back to 52.6 points (from 54.5 points previously). Key to this downturn was China, when its services PMI dropped to its lowest level since October 2023, while Russia's services PMI drifted further into negative territory (having been strongly positive in January). Part of the drop in China's measure was attributed to domestic tourism activity – boosted by holidays in early May that were absent in June.

In contrast, the EM manufacturing PMI edged marginally higher in June – up to 52.1 points (from 52.0 points between March and May). India was the main driver of this increase, with modest gains in China and Russia offset by a decline in Indonesia.

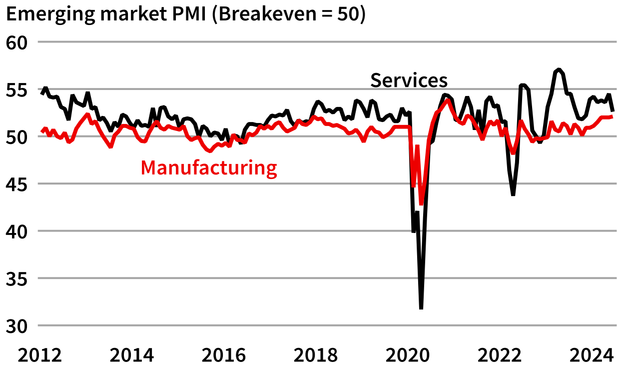
China's economy grew by 4.7% yoy in Q2 – down from 5.3% yoy in Q1. There was a larger slowdown in China's services sector than its manufacturing & construction industry – with weak domestic demand negatively impacting the former, while the surge in export volumes has helped to underpin the latter.

A lack of policy support for households during the COVID-19 pandemic, combined with the prolonged downturn in the property sector and an ageing population (that encourages saving to support retirement) has constrained consumption. Real retail sales rose by 1.8% yoy in June – its weakest outcome since China abandoned its zero-COVID policies in December 2022.

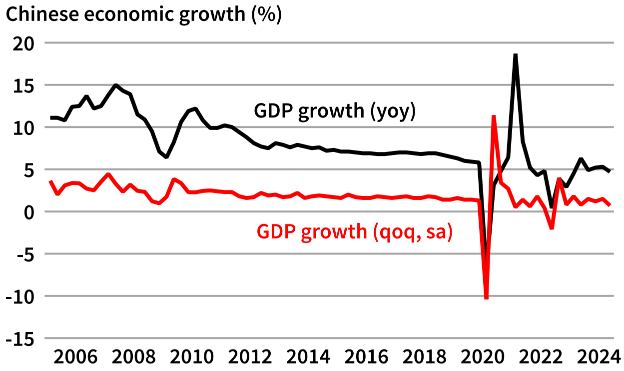
Trade has been a key source of China's growth in recent quarters, with export volumes expanding since the middle of 2023, allowing growth in industrial output despite weak domestic demand. Volumes rose by 6.1% yoy (on a three month moving average basis) in April – down from double digit growth in the January and February. In contrast, export volumes from the rest of the world rose by just 0.6% yoy (3mma).

This led to growing trade tensions with a broad range of countries – with high profile tariffs on electric vehicles announced in the United States and European Union. Concerns that these policy measures could make Chinese exporters to pivot to South East Asia resulted in Indonesia announcing its own tariffs on Chinese goods in late June. These measures were focussed on comparatively lower value added products, such as textiles, clothing and footwear, along with ceramics and cosmetics. Indonesian authorities believe increasing Chinese exports in these sectors will harm micro, small and medium sized domestic producers.

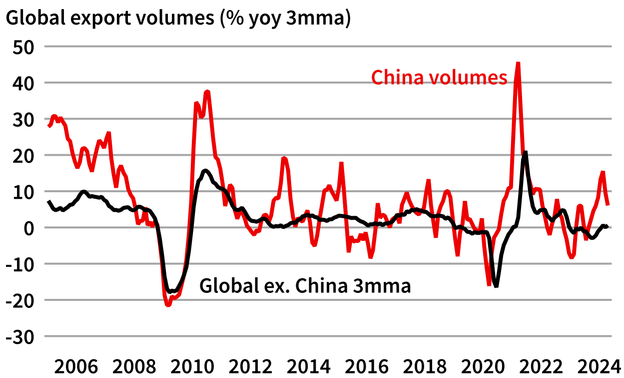
Weaker China services drives PMI lower in June



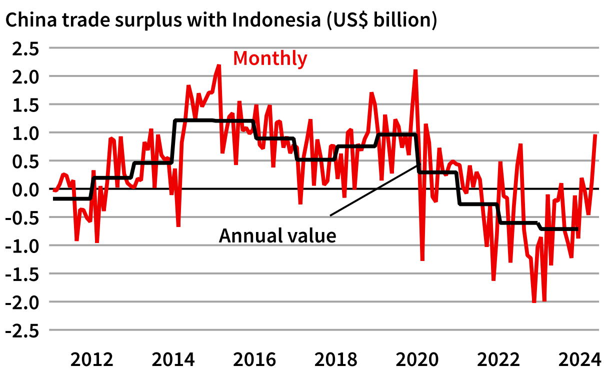
Weak domestic demand saw China's growth slow in Q2



China's exports have outpaced the rest of the world



Shift in China-Indonesia trade balance in early 2024



Global forecasts and risks: growing trade and political risks around a subdued global outlook

Global business surveys were somewhat softer in June, with the JPMorgan global composite PMI down to 52.9 points (from a twelve-month high of 53.7 points in May).

The downturn in the composite measure was driven by the global services PMI, which eased to 53.1 points (from 54.0 points previously). There was a larger decline recorded in EMs than advanced economies in June.

In comparison, the global manufacturing PMI edged down to 50.9 points in June (from 51.0 points previously). Trends between country groups differed, with the EM manufacturing PMI slightly stronger and the AE measure slightly weaker.

We have made some minor revisions to our forecasts this month – most notably for China, the United Kingdom and Canada in 2025 – albeit these changes largely cancel each other out. As a result, our global forecasts remain unchanged – we expect growth of 3.0% in both 2024 and 2025 before improving slightly to 3.1% in 2026. This outlook sees growth remaining below the long term average (of 3.4% between 1980 and 2022).

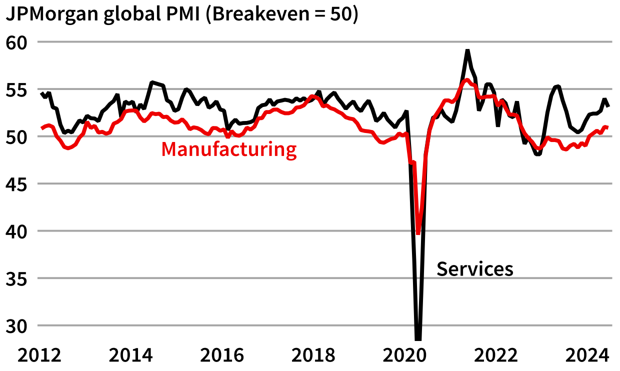
There remain a broad range of factors that present uncertainty around our economic outlook. Recent months have seen a range of countries – from the United States, the European Union-27 and more recently Indonesia – announce tariffs to counter the surge in China's exports. There is a risk that additional countries – including other emerging markets in South East Asia – may seek to join the current wave of protectionism, unless China begins to address its industrial capacity issues and trade balance.

Similarly, the path of inflation – and the resulting monetary policy decisions by major central banks – remains unclear. The persistence of AE inflation at above target levels, having remained essentially stable across the first five months of 2024. This has the potential to delay policy rate cuts (including in the Euro-zone and Canada that have already commenced the rate cutting cycle), which could negatively impact global economic growth in 2025 and 2026.

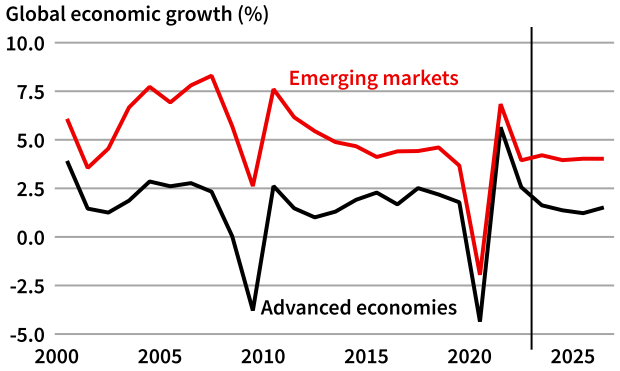
The outlook for US economic, foreign and trade policy has become even more uncertain in recent weeks, particularly following the Presidential debate. President Joe Biden's poor performance in the debate, and decline in the polls, triggered calls for his replacement as the Democratic candidate ahead of the November election.

There also remain a broad range of geopolitical tensions across various parts of the world. The Russia-Ukraine war continues to negatively impact the supply of energy and agricultural commodities. Oil markets could face further disruption if conflict between Israel and Hezbollah commences in Lebanon. Finally, tensions in the South China Sea between China and its neighbours have continued.

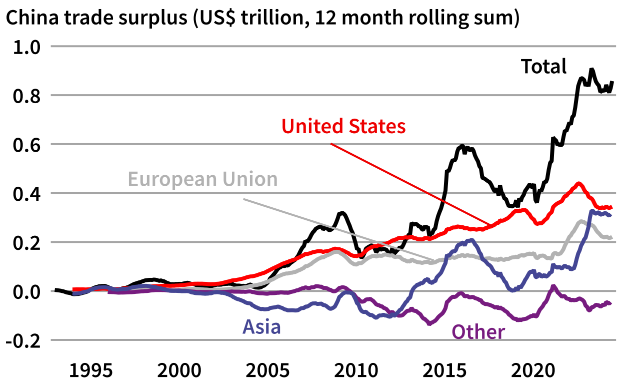
Services drove a softer global PMI in June



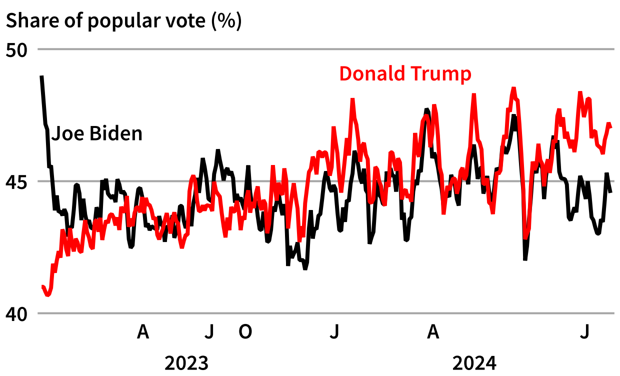
Subdued economic growth through to 2026



Tariffs a response to China's increased trade imbalance



Polling for US presidential election



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