The Forward View: Global October 2024

NAB Group Economics

Overview

- Stimulus measures announced by China, and expectations of more to come, have boosted the Chinese equity market and global commodity prices. Announcements to-date are, in our view, insufficient to get growth back on track. If the government fails to deliver on expectations of material stimulus, the gains in equity and commodity markets may unwind.

- The US economy continues to motor along but, in contrast, the Euro-zone economy looks to be going through another soft patch, in part due to the ongoing struggles of the German economy.

- Even as the US economy remains resilient, the Federal Reserve cut its policy rate last month by 50 bps. As with other major central banks that have cut rates, the substantial progress made in reducing inflation, well anchored inflation expectations and a better supply and demand balance (particularly in the labour market) means less restrictive interest rate settings are needed.

- While the Fed is expected to cut rates (and our central case is for 25bp cuts per meeting until rates return to neutral), stronger than expected employment and inflation data for September have tempered market expectations about how quickly this may occur and raised the possibility of the Fed pausing in the near term. This is a reminder that inflation remains high and that if it does not come down as expected, central banks will need to maintain restrictive policy settings in place for longer.

- Our global growth forecasts are unchanged this month. We see the global economy expanding by 3.1% in both 2024 and 2025, and then 3.2% in 2026, a subdued pace by historical standards.

- There remain a range of risks around this central outlook. As noted above, there is uncertainty over the pace with which central banks reduce rates. There remain a number of geopolitical tensions, including an expanding conflict in the Middle East which has recently led to an increase in oil prices. US elections could bring with them large changes in trade and, potentially, fiscal policies depending on results.

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Global growth forecasts

	2022	2023	2024	2025	2026
US	2.5	2.9	2.7	1.9	2.1
Euro-zone	3.4	0.5	0.6	1.0	1.5
Japan	1.5	1.7	-0.1	1.0	0.7
UK	4.8	0.3	0.9	0.9	1.2
Canada	3.8	1.2	1.1	1.4	1.8
China	3.0	5.2	4.7	4.6	4.4
India	6.5	7.7	6.6	6.2	6.4
Latin America	4.2	2.2	1.5	2.3	2.2
Other East Asia	4.2	3.2	3.9	3.8	3.9
Australia	3.9	2.0	1.0	1.8	2.3
NZ	2.4	0.7	-0.2	1.7	3.1
Global	**3.5**	**3.3**	**3.1**	**3.1**	**3.2**

Expectations of large-scale China fiscal stimulus driving markets but are yet to be delivered on

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

Financial and commodity markets: Chinese stimulus announcement triggers market surge

Financial markets initially responded positively to China's announced stimulus measures in September. Having trended lower in early September, equity markets climbed significantly across the rest of the month, with the MSCI US index rising to a record high at the end of September, other advanced economies to a record in early October and the EM index rising to its highest level since November 2021 – with the latter reflecting a surge in Chinese equity markets.

Similarly, commodity prices – as measured by the S&P GSCI – climbed rapidly, up almost 13% in early October from its early September lows, largely led by base metals. Iron ore, which is not included in the GSCI, rose close to US$110/t in early October, having fallen to almost US$90/t a month earlier. That said, the stimulus announced by the time of writing was unlikely to materially impact commodity demand, meaning these price increases were more akin to irrational exuberance than a signal of shifting market conditions.

Given this, asset prices that rose due to stronger sentiment regarding China could correct should fiscal stimulus fall short of expectations.

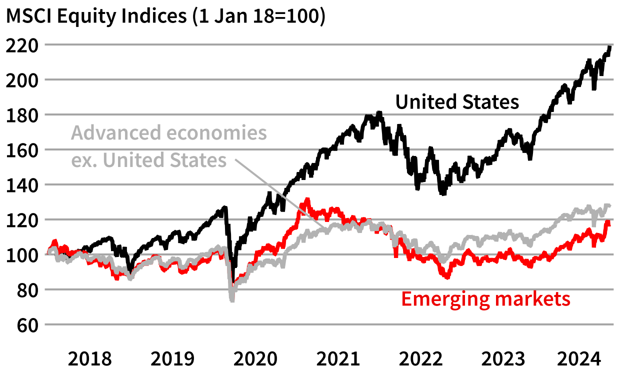
Oil prices have also climbed in excess of 10% over the past month – after having fallen to their lowest levels since late 2021 in early September. The intensified conflict in the Middle East, with Israel attacking southern Lebanon has raised concerns around disruptions to supply in the region, despite weak demand trends (with oil consumption growth in the first half the slowest since 2020).

There remains uncertainty around the timing and scale of cuts to major advanced economy (AE) central bank rates, despite the rate cutting cycle already being underway. Headline AE inflation edged lower in August – down to 2.4% yoy (compared with 2.6% yoy in July) – marginally below the range from 2.8% yoy to 2.5% yoy seen over the first seven months of the year.

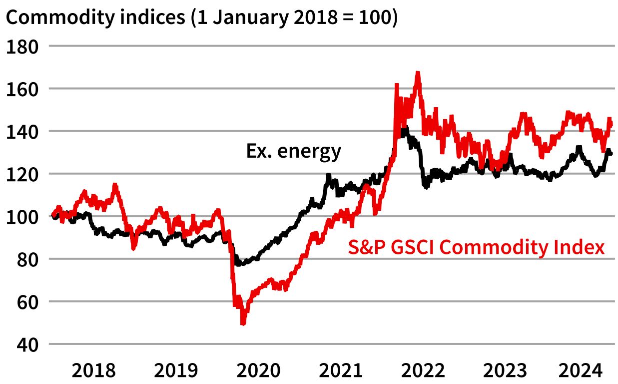
However, advanced economy core inflation remained stable in August – increasing by 2.7% yoy – with disinflationary progress essentially stalling in the past three months.

The persistence of AE inflation at above target rates has driven a cautious approach from most major central banks with respect to their policy rates. Following the Fed's 50 basis point cut in September, Fed Chair Jerome Powell indicated that the Fed was not "…in a hurry to cut rates quickly". There is typically a long lag between changes in policy rates and their full impact on the real economy. If persistently above target inflation results in delays to central bank cuts, this could negatively impact economic growth later in our outlook period (particularly in 2026).

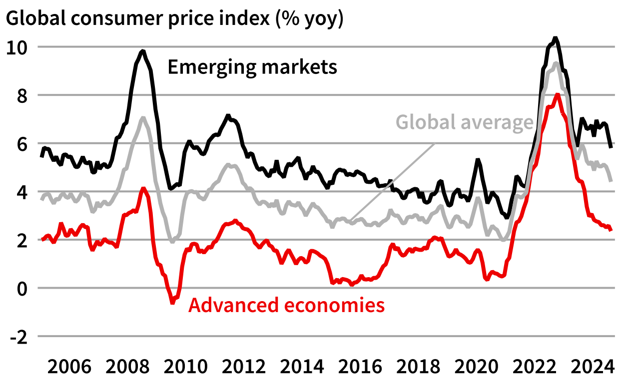
Global equities surged higher on China stimulus…



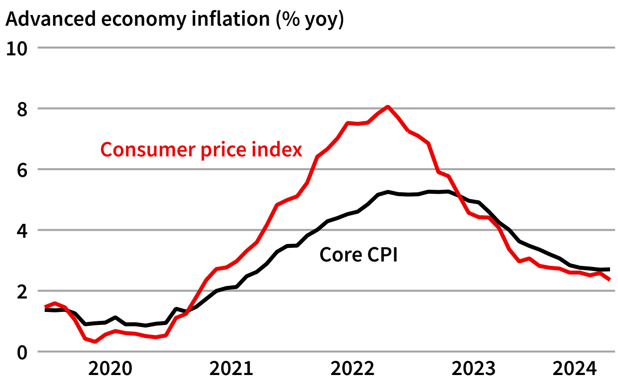
…along with commodity prices, led by metals



Advanced economy inflation edged down in August…



…but core inflation stalled over the past three months



Sources: Macrobond, NAB Group Economics

Advanced economies: US economy holding up while the Euro-zone wobbles and Japan reflates

This month we revised up our forecasts for the US economy. Incoming data point to stronger growth in Q3 (around 2.8% q/q annualised) and while upward revisions to estimated household income and corporate profits point to a better outlook for consumption and business investment. We still expect US GDP growth to slow from here. Consistent with this, business surveys for the US have improved this year, but are not particularly high by past standards. However, growth should remain at a decent level, with some gradual strengthening over the forecast period as the impact of the Fed's easing cycle – which commenced in September – comes through.

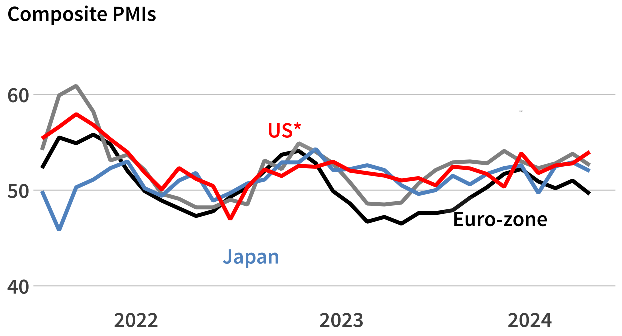
In contrast, business surveys raise concerns over the Euro-zone. The composite Euro-zone S&P Global PMI fell to a seven-month low in September. As inflation receded, the boost to household incomes was expected to lift consumption but consumers have remained cautious. While we think consumption growth will rise from here, we have revised down our near-term forecasts. The German economy has especially struggled. German GDP declined by 0.1% in Q2 and was unchanged over the year. Even as energy prices fell back from their Ukraine-Russia war spike, German industrial production has trended down and is almost 6% below its pre-COVID level, pointing to an ongoing drag from structural changes in German industry.

The UK and Japan composite PMIs also eased in September but remain in line with recent levels. UK growth was strong in the first half of the year. While August monthly GDP showed decent growth, this was offset by downward revisions to prior months and the stepdown in growth we had expected in H2 is underway. For Japan, after households experienced a large fall in real income over 2022-23, a recovery in H1 2024 led to strong consumption growth in Q2, contributing to a rebound in GDP after a weak start to the year.

From a monetary policy perspective, Japan has been the exception this year as the Bank of Japan (BoJ) has lifted rates while the other major AE central banks have cut them. For the latter, lower inflation, growth concerns (ex. US) and cooler labour markets – either reflected in rising unemployment rates or more normal levels of job vacancies – mean less restrictive policy settings are appropriate.

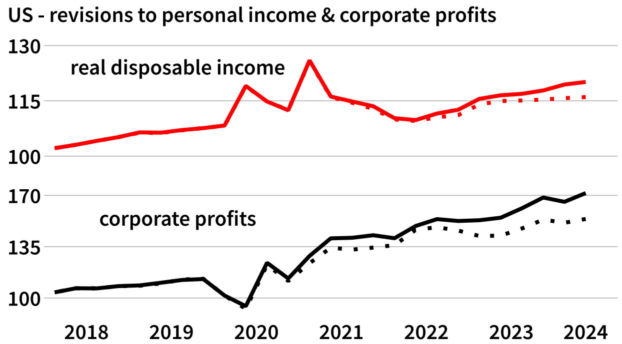
In contrast, up until March this year, the BoJ's policy rate was still negative (-0.1%) and now only stands at "around 0.25%". Given the lift in inflation, and inflation expectations, this means the real policy rate is negative. Pricing and wage setting behaviour does appear to have changed – wages growth and inflation (ex. periods of consumption tax increases) are at levels not seen since the early 1990s. While where inflation ultimately settles remains unclear, it is highly likely that it will be higher than in previous decades.

Worrying drift in Euro-zone business surveys continues



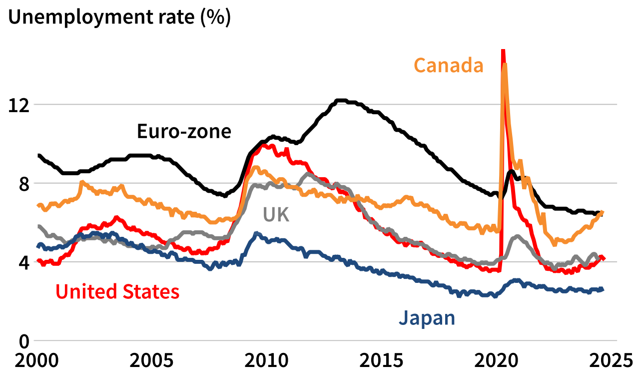
* Based on S&P Global and NAB weighted composite of US ISM PMIs

US data revisions point to an economy on firmer ground

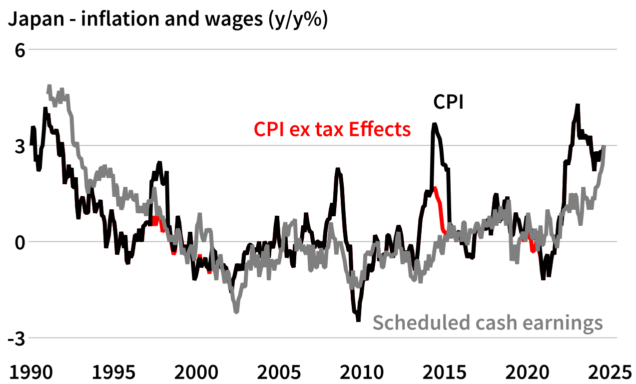


Solid lines - current estimates; dashed lines previous estimates

Labour market pressures have cooled



Japan – inflation and wages back to the 1990s



Sources: Macrobond, US BEA, NAB Group Economics

Emerging markets: China's stimulus has captured headlines, but so far it has underwhelmed

Business surveys provide some of the timeliest data on conditions in emerging markets. The EM composite PMI has trended lower since its recent peak in May – dipping down to 51.1 points in September (from 52.1 points in August).

Both the services and manufacturing measures were weaker in September. The EM services PMI dropped to 51.7 points (from 52.8 points previously) – driven primarily by weaker readings for both India and China (with the latter dropping to neutral levels). The EM manufacturing PMI fell into marginally negative territory at 49.8 points (from 50.8 points in August), with China the main contributor.

The key focus regarding emerging markets in recent weeks has been the stimulus package announced by Chinese authorities in September (along with expectations of further measures to come). This reflects the relatively weak performance of the Chinese economy in 2024 and a growing view by its government that intervention is necessary to bring growth back on track.

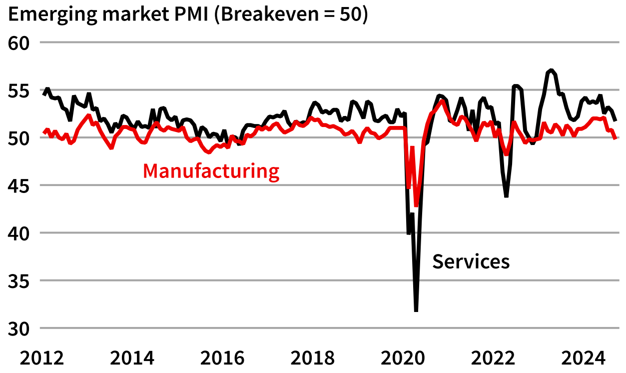
On the monetary side, the People's Bank of China (PBoC) announced a modest cut to its main policy rate (20 bps), steeper cuts to mortgage rates (50 bps), boosted liquidity to financial markets (in cutting the Reserve Requirement Ratio) and provided support for the property and equity markets. That said, loan demand from both households and businesses remains extremely weak and, on its own, we don't believe that these policy changes will be enough to reverse this trend.

A supporting fiscal package has also been anticipated, with a range of rumours in the past month regarding its contents. Last weekend's press conference from China's Finance Minister was underwhelming – with a focus on reducing risks in property, the banking sector and local governments, rather than providing support measures to boost consumption. More measures may be announced at the National People's Congress in late October.

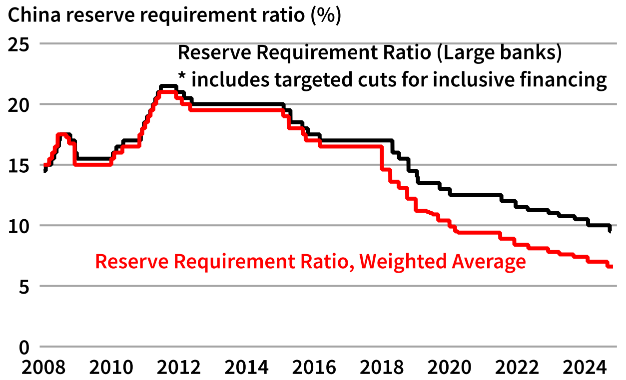
The fundamental issue facing Chinese authorities is a prolonged weakness in domestic demand, in part reflecting the fallout from the property bubble bursting, while the most policy measures since the start of the COVID-19 pandemic have been directed towards the supply side of the economy. This has increased existing imbalances, boosting industrial output that has contributed to the surge in China's export volumes.

Growth in China's export volumes has trended higher since mid-2023. According to CPB data, China's export volumes rose by 10.3% yoy in July, compared with an increase of just 0.8% yoy for the rest of the world. This has contributed to growing trade tensions between China and a broad range of countries, culminating in tariffs announced by the United States, the European Union and Canada among others.

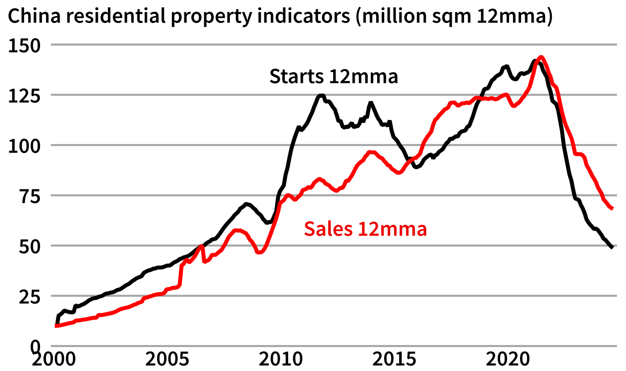
PMIs drift lower on weaker results in China



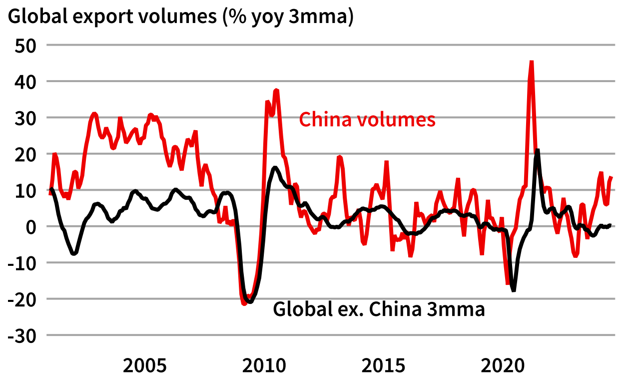
Monetary policy easing unlikely to be enough on its own



Property contributing to China's weak domestic demand



Imbalances have led to surging export volumes



Global forecasts and risks: near term growth subtrend; all eyes on China's policy decisions

Global economic growth edged lower in Q2, down to 3.2% yoy (compared with 3.3% in Q1 2024 and the recent cycle peak of 4.0% yoy in Q2 2023).

Growth trends diverged between advanced economies and emerging markets, with economic growth in the EM region down to 4.4% yoy (from 4.7% in Q1), with India, Russia and China slowing. In contrast, growth in advanced economies was slightly stronger, up by 1.5% yoy (from 1.3% yoy previously), with the United States and Eurozone the main drivers.

Despite the announced Chinese stimulus purportedly intended to assist in the country hitting its annual growth target of "around 5%", our forecasts for China remain unchanged for now. We see China's economy expanding by 4.7% in 2024 and 4.6% in 2025 – albeit meaningful fiscal stimulus (which we are yet to see) could add some upside risk, most likely to next year's forecast. It is not only the size of any program that matters but how and where funds are directed, with measures targeted at supporting demand needed to materially lift growth.

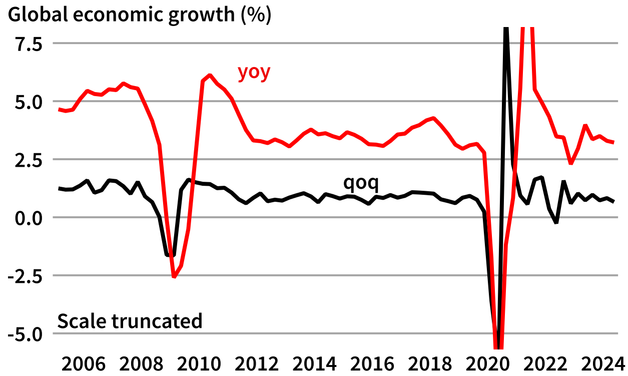
We have made some minor forecast changes to a few key economies – including a small upward revision to US growth in 2024 and 2025, while growth in the Eurozone has been revised slightly lower this year and next. Despite doubts around the accuracy of Russia's economic data, we have also revised up growth in 2024 and 2025 to reflect official reports. These changes are not large enough to alter our global forecasts. We see the global economy expanding by 3.1% in both 2024 and 2025, before moving marginally higher to 3.2% in 2026.

Geopolitical factors and policy decisions present risk to this outlook. Conflict in the Middle East has escalated in the past month, while the Russia-Ukraine war continues unabated, along with tensions between China and its neighbours in the South China Sea. These factors could disrupt commodity production and global trade.

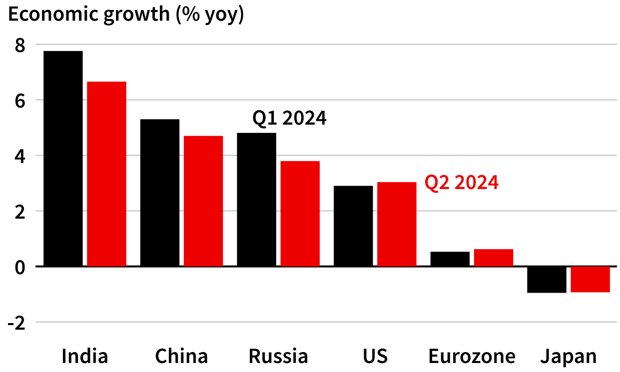
Global trade could also be impacted by growing protectionism, particularly with respect to China. While a broad range of countries have announced tariffs on Chinese goods, the list of countries could expand. November's US Presidential Election could have an even larger impact, with Republican candidate Donald Trump proposing a 10% across the board tariff on all goods entering the US, along with a 60% tariff on goods from China.

There also remains uncertainty around the timing of cuts to central bank policy rates – which will be dependent on progression towards inflation targets and labour market conditions in individual countries. Any delays to rate cuts could negatively impact economic growth towards the end of our outlook period.

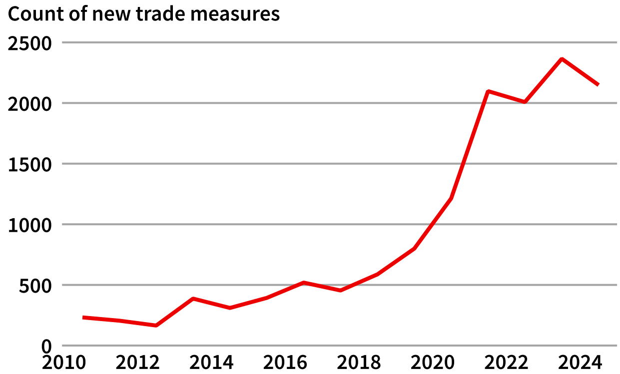
Global growth edged lower in Q2…



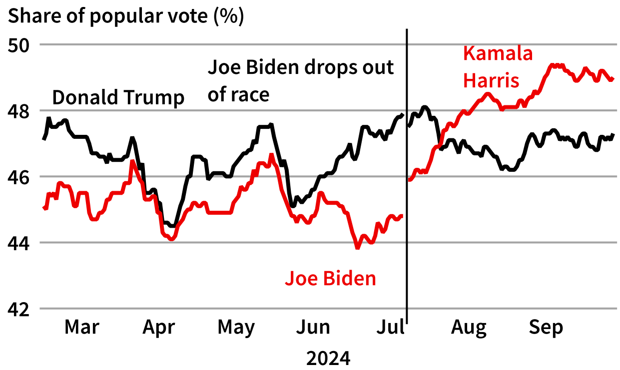
…led by slower growth among emerging markets



Global trade protectionism has risen in recent years



National polling for US Presidential Election



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