GLOBAL ECONOMIC OUTLOOK

CONTINUED DISINFLATION AND RATE CUTS TO SUPPORT GROWTH

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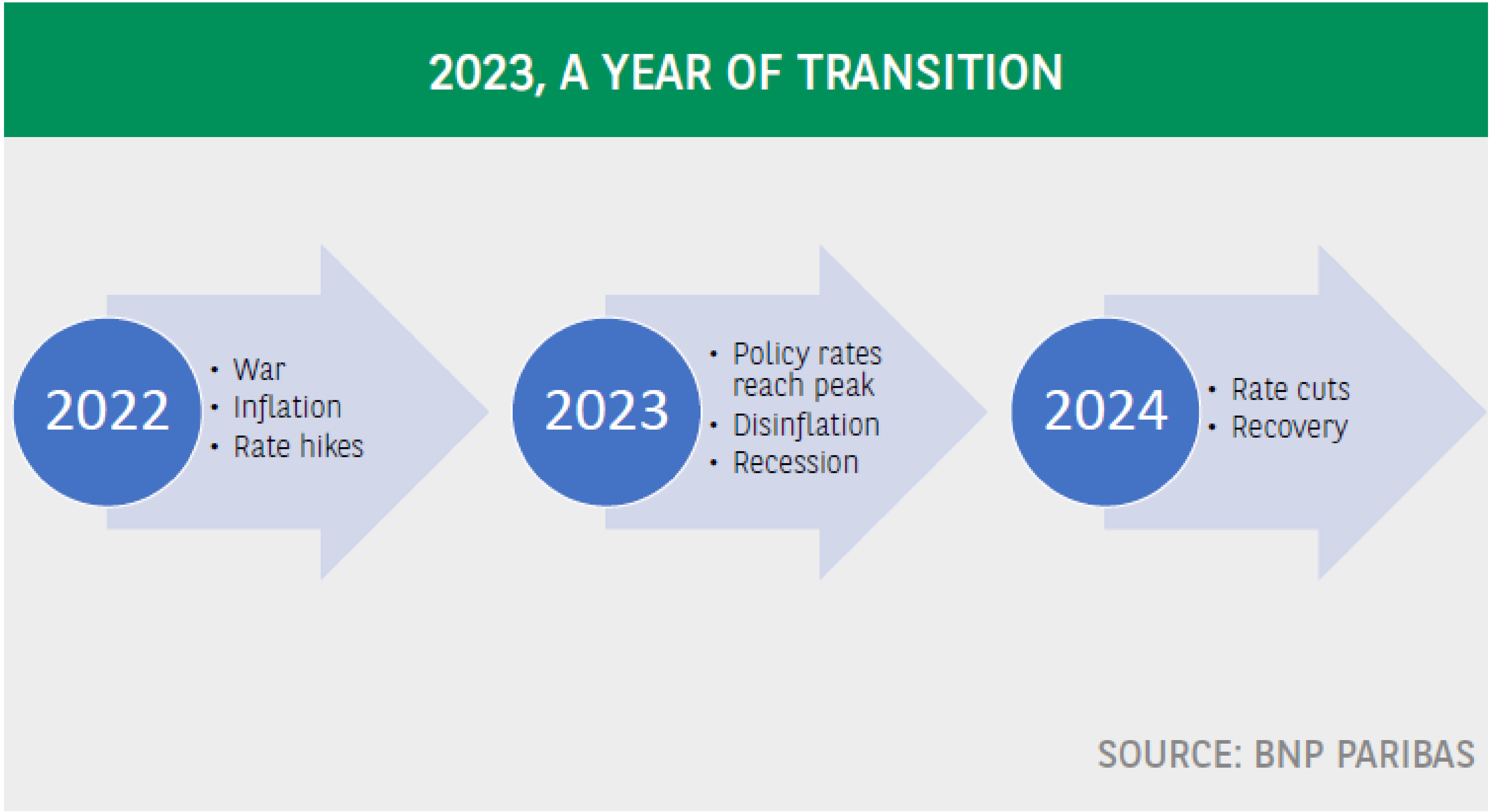
31 January 2024

BNP PARIBAS

The bank for a changing world

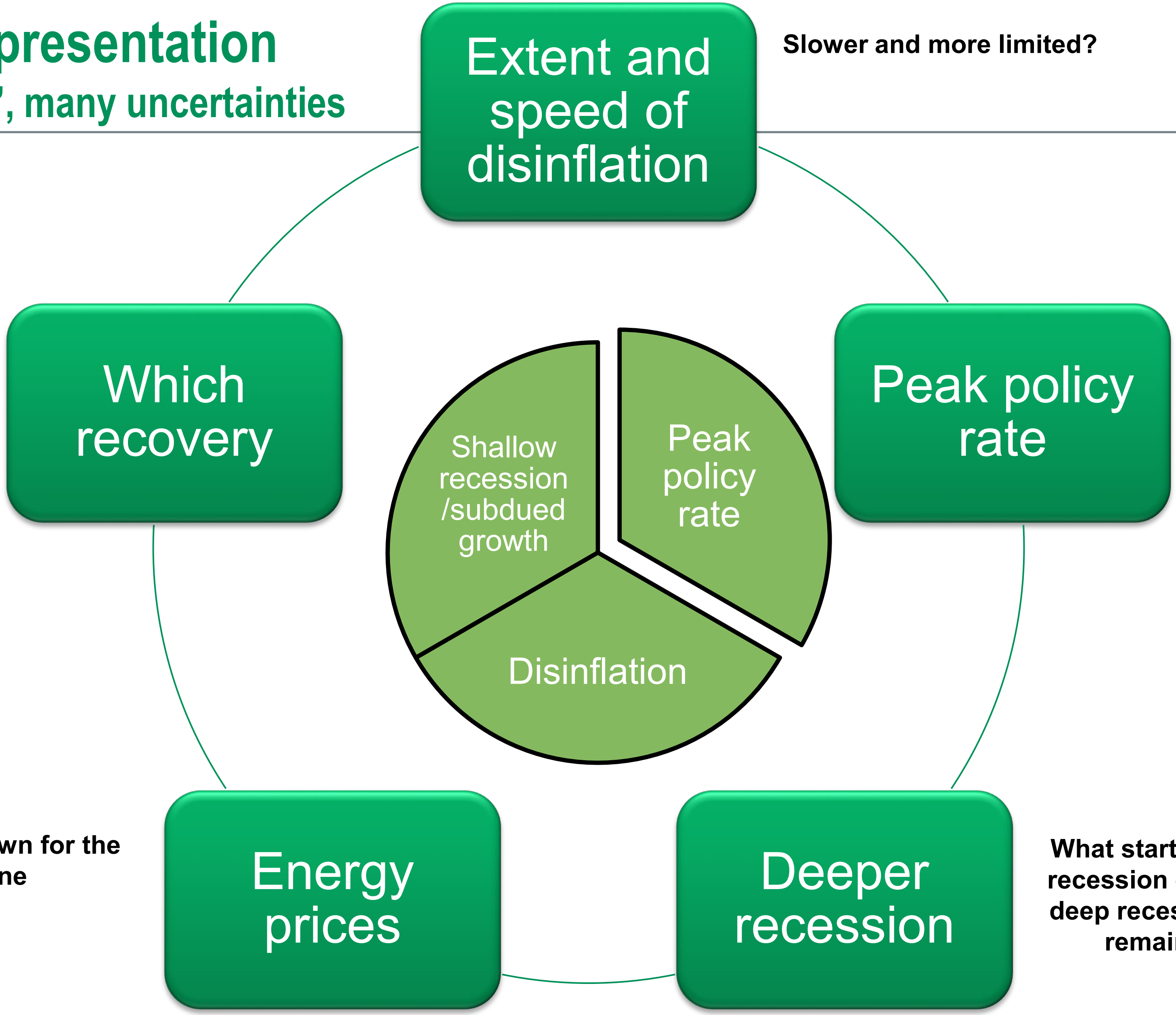
1 SUMMARY

From last year's presentation (1)



From last year's presentation

2023: three 'certainties', many uncertainties



Slower and more limited?

Higher?

Maintained for longer?

What started as a shallow recession could become a deep recession if inflation remains too high

The key unknown for the Eurozone

Does a slow recovery fuel fears about a relapse into a recession?

What does a recession without rate cuts imply for the subsequent recovery?

A helicopter view

2022 Concern
- Inflation up
- Rates up

2023 Worries
- Inflation down
- Rates up

2024 Relief
- Inflation down
- Rates down

IMF WEO update, 30 January 2024: a more positive message

Overview

The risks to global growth are broadly balanced and a soft landing is a possibility

Global growth is projected at 3.1 percent in 2024 and 3.2 percent in 2025, with the 2024 forecast 0.2 percentage point higher than that in the October 2023 World Economic Outlook (WEO) on account of greater-than-expected resilience in the United States and several large emerging market and developing economies, as well as fiscal support in China. The forecast for 2024–25 is, however, below the historical (2000–19) average of 3.8 percent, with elevated central bank policy rates to fight inflation, a withdrawal of fiscal support amid high debt weighing on economic activity, and low underlying productivity growth. Inflation is falling faster than expected in most regions, in the midst of unwinding supply-side issues and restrictive monetary policy. Global headline inflation is expected to fall to 5.8 percent in 2024 and to 4.4 percent in 2025, with the 2025 forecast revised down.

2024: two ‘certainties’…

‘Certainties’

- Inflation to decline further
- Policy rate cuts

… but several ‘known unknowns’

‘Known unknowns’

- Delayed impact of past rate hikes
- Reaction of demand to disinflation and rate cuts
- US soft landing

Could cause downward revision of inflation and growth outlook. This would imply an expectation of more and swifter rate cuts. Bond yields would decline.

Determines pace of recovery. We expect very gradual recovery.

Could cause quick reappareance of labour market bottlenecks thereby raising inflation expectations. This would imply an expectation of fewer and slower rate cuts. Bond yields would rise.

Summary

US business surveys correspond to a subdued level of activity in manufacturing whereas services continue to grow. Consumer sentiment has improved.

Eurozone business surveys have improved somewhat but do not yet reflect the start of a rebound.

US inflation has dropped but disinflation momentum has slowed recently.

.Eurozone inflation is down significantly. The decline of core inflation has gathered pace in recent months. There is a possibility that inflation would converge to the ECB target already in spring of this year.

We expect a sharp slowdown of the US economy in the first half of 2024 but no recession. Growth is expected to pick up gradually in the second half of 2024.

In the Eurozone, the ongoing decline in inflation and policy rate cuts should lead to a gradual improvement of quarterly growth as of the spring of this year

The decline of inflation will allow the Federal Reserve to start cutting rates this year. We expect the first cut in spring and cumulative cuts this year of 150 basis points.

Progress in terms of disinflation and its outlook should allow the ECB to start cutting rates in spring. We expect cumulative cuts this year of 125 basis points.

Summary

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Summary

We expect a sharp slowdown of the US economy in the first half of 2024 but no recession. Growth is expected to pick up gradually in the second half of 2024.

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FORECASTS

Forecasts: real GDP growth

Subdued growth

Sharp slowdown

	ANNUAL GROWTH (% y/y)			QUARTERLY GROWTH (% q/q)			
	2023	2024	2025	2024 Q1	2024 Q2	2024 Q3	2024 Q4
US	2.4	0.9	1.3	0.0	-0.3	0.2	0.3
Eurozone	0.5	0.6	1.6	0.1	0.3	0.4	0.4
Germany	-0.1	0.3	1.3	0.0	0.2	0.3	0.4
France	0.8	0.6	1.4	0.1	0.2	0.3	0.4
Italy	0.7	0.9	1.5	0.2	0.4	0.4	0.4
Spain	2.3	1.5	2.1	0.2	0.5	0.6	0.6
China	5.2	4.5	4.3	1.3	0.9	1.1	1.2
Japan	2.1	0.8	0.9	0.2	0.3	0.4	0.3
UK	0.3	-0.1	1.1	-0.1	0.0	0.1	0.2

Source: BNP Paribas Markets360

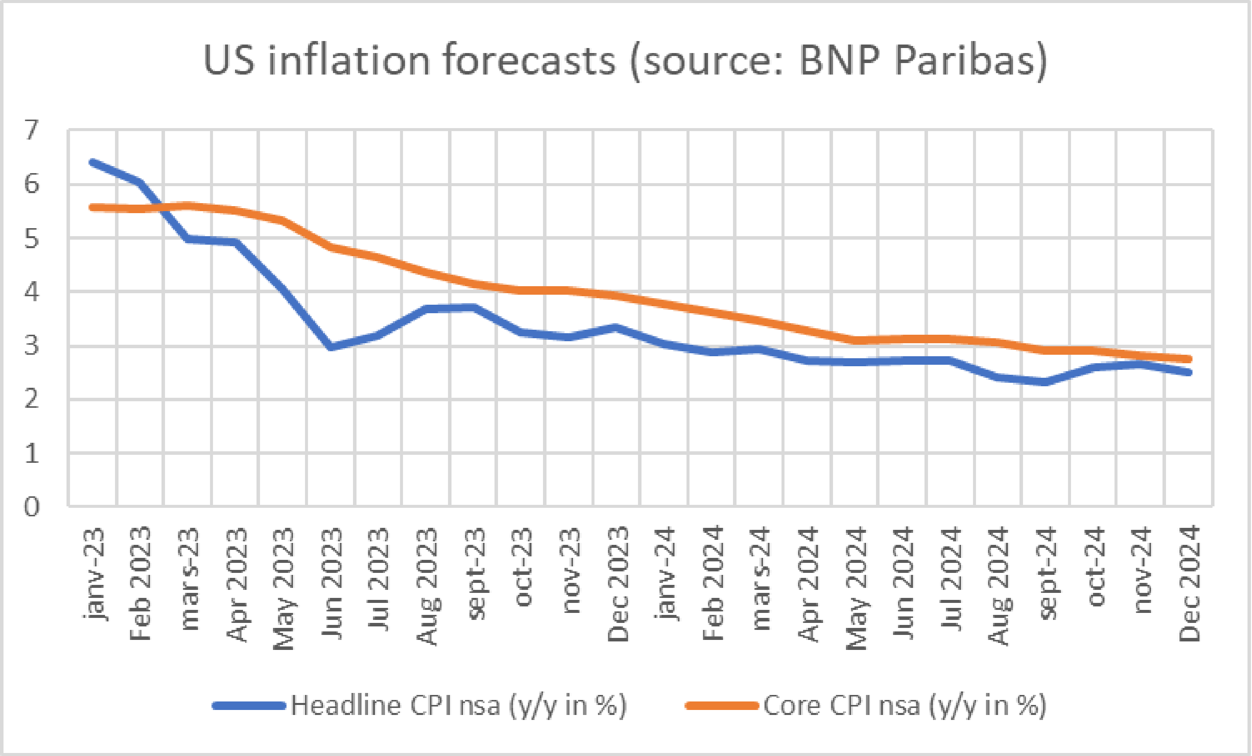
Forecasts: inflation

Disinflation paves the way for rate cuts

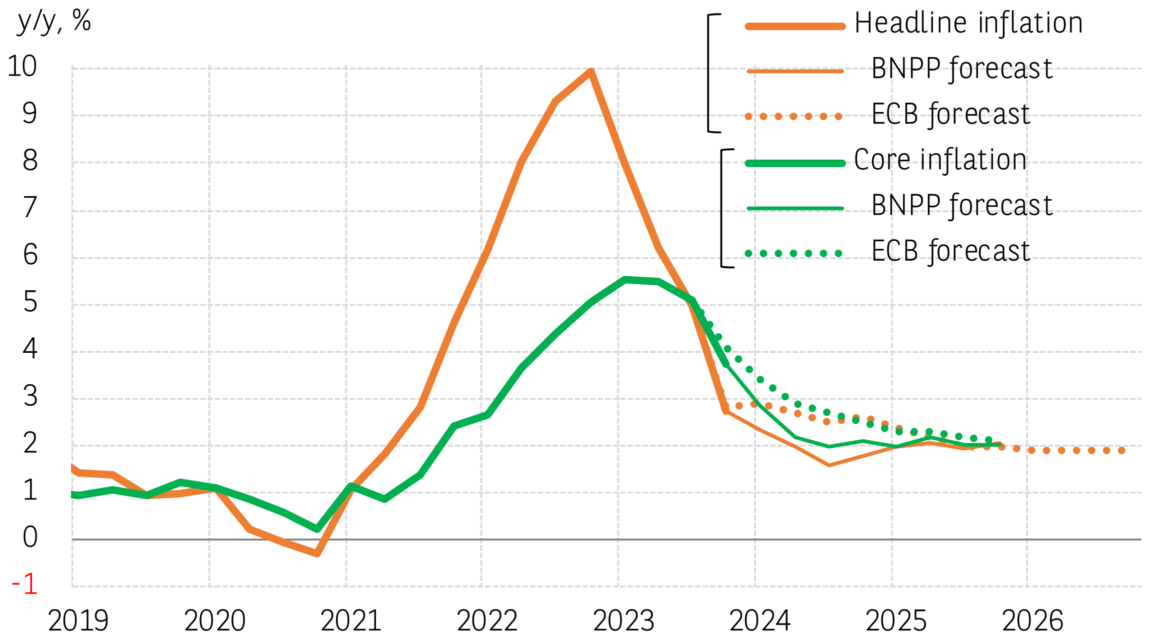
	ANNUAL RATE (% y/y)			QUARTERLY RATE (% y/y)							
	2023	2024	2025	2024 Q1	2024 Q2	2024 Q3	2024 Q4	2025 Q1	2025 Q2	2025 Q3	2025 Q4
US	4.1	2.7	2.3	3.0	2.7	2.5	2.6	-	-	-	-
Eurozone	5.4	1.9	2.0	2.3	2.0	1.6	1.8	2.0	2.1	2.0	2.1
Germany	6.1	2.3	2.1	2.7	2.2	2.0	2.1	2.0	2.1	2.0	2.1
France	5.7	2.3	1.8	2.9	2.2	2.1	1.9	1.9	1.8	1.7	1.8
Italy	6.1	1.9	1.9	1.6	1.9	2.0	2.1	2.0	1.9	1.7	1.8
Spain	3.4	2.0	2.0	2.6	2.4	1.3	1.6	1.9	2.0	1.9	1.9
China	0.4	1.5	1.7	1.3	1.5	1.5	1.8	-	-	-	-
Japan	3.2	2.3	1.9	2.6	2.4	2.1	1.9	1.8	1.9	2.0	2.0
UK	7.4	2.2	2.3	3.8	1.6	1.6	1.8	2.5	2.3	2.2	2.2

Source: BNP Paribas Markets360

BNP Paribas inflation forecasts



Inflation in the eurozone and forecasts



Source: Eurostat, ECB, BNP Paribas

Forecasts: interest rates

Policy rate cuts have already been anticipated to a large degree by bond markets. This limits the potential for a further decline in yields this year

Policy easing starts in spring 2024

	YEAR END			QUARTER END			
	2023	2024	2025	2024 Q1	2024 Q2	2024 Q3	2024 Q4
US	5.50	4.00	2.75	5.50	5.00	4.50	4.00
Eurozone	4.00	2.75	2.50	4.00	3.50	3.00	2.75
China	2.50	2.25	2.15	2.35	2.25	2.25	2.25
Japan	-0.10	0.25	0.75	0.10	0.10	0.25	0.25
UK	5.25	4.25	3.00	5.25	5.00	4.75	4.25

	Q1 2024	Q2 2024	Q3 2024	Q4 2024	Q4 2025
US					
2-year	4.20	3.80	3.55	3.35	3.10
10-year	4.15	4.00	3.95	3.95	4.00
30-year	4.40	4.30	4.25	4.25	4.30
Eurozone					
2-year	2.55	2.35	2.15	2.10	2.40
10-year	2.45	2.35	2.20	2.20	2.50
30-year	2.75	2.77	2.67	2.70	3.05
10y France-Germany spread (bp)	57	56	55	55	55
10y Italy-Germany spread (bp)	180	165	175	170	170
10y Spain-Germany spread (bp)	100	90	90	85	80
UK					
2-year	4.50	4.25	3.90	3.60	3.25
10-year	3.90	3.75	3.65	3.55	3.65
30-year	4.35	4.15	4.00	3.87	3.90
Japan					
2-year	0.20	0.40	0.60	0.65	0.65
10-year	0.95	1.20	1.35	1.35	1.35
30-year	1.85	2.05	2.10	2.05	2.05

Policy normalisation to start in Japan in spring. This might create global spillovers in bond and FX markets

3

CYCLICAL ENVIRONMENT

Purchasing managers' indices show services in better shape than manufacturing

S&P GLOBAL PMI, December 2023

Developed Markets

	December 2023	WD: World	NA: CANADA	NA: USA	Europe: EURO ZONE	Europe: AUSTRIA	Europe: DENMARK	Europe: FRANCE	Europe: GERMANY	Europe: GREECE	Europe: IRELAND	Europe: ITALY	Europe: NETHERLANDS	Europe: SPAIN	Europe: SWITZERLAND	Europe: UK	Asia-Oceania: AUSTRALIA	Asia-Oceania: NEW ZEALAND	Asia-Oceania: JAPAN	Asia-Oceania: SINGAPORE
	COMPOSITE	51.0		50.9	47.6			44.8	47.4		51.5	48.6		50.4		52.1			50.0	
	MANUFACTURING	49.0	45.4	47.9	44.4	42.0		42.1	43.3	51.3	48.9	45.3	44.8	46.2	43.0	46.2			47.9	
	SERVICES - BUSINESS ACTIVITY	51.6		51.4	48.8			45.7	49.3		53.2	49.8		51.5		53.4			51.5	
MANUFACTURING	NEW ORDERS	48.6	42.5	47.1	42.0	39.9		37.7	41.5	51.8	47.9	41.4	44.4	43.8		46.6			45.2	
MANUFACTURING	NEW EXPORT ORDERS	48.0	44.9	49.7	42.7	42.9		37.8	41.1	50.5	50.8	43.2	44.3	46.5		47.0			46.4	
MANUFACTURING	DELIVERY TIMES*	49.8	49.1	47.9	46.8	43.5		50.5	43.7	51.6	52.1	47.0	44.6	52.0		48.7			50.5	
MANUFACTURING	EMPLOYMENT	48.7	47.3	49.0	46.7	43.3		44.0	45.6	51.9	50.0	50.0	46.4	47.5	49.2	46.1			50.2	
MANUFACTURING	INPUT PRICES	52.4	54.1	55.3	43.1	42.4		47.5	38.0	53.7	52.6	45.3	40.7	45.6		47.5			59.8	
MANUFACTURING	OUTPUT PRICES	51.5	52.7	53.6	48.9	47.8		48.5	48.9	54.4	49.1	49.9	49.7	46.0	43.6	50.1			53.6	
MANUFACTURING	OUTPUT	49.5	45.4	48.1	44.4	41.4		40.7	43.8	53.3	49.4	45.4	44.7	46.3		45.5			46.8	
MANUFACTURING	STOCKS OF PURCHASES	48.2	45.1	47.6	43.0	45.0		42.1	42.3	48.4	44.0	45.0	43.7	41.4	46.8	43.5			50.4	
MANUFACTURING	QUANTITY OF PURCHASES	47.1	43.7	44.9	39.0	35.7		37.7	37.8	50.6	44.2	38.6	41.6	40.3		41.1			43.4	
MANUFACTURING	FINISHED GOODS	49.3	50.7	49.8	47.9	49.0		49.8	48.2	48.1	46.8	47.7	46.9	44.1		46.6			50.0	
MANUFACTURING	WORK BACKLOGS	46.5	43.8	44.8	41.6			42.9	37.9	44.7	50.3	44.7	44.5	42.3		39.5			45.2	
SERVICES	INPUT PRICES	57.6		57.7	61.6			59.5	64.8		62.6	57.4		63.5		64.5			57.0	
SERVICES	OUTPUT PRICES	54.2		55.0	55.6			53.5	58.7		56.5	52.3		56.8		58.6			52.9	
SERVICES	EMPLOYMENT	51.1		51.9	50.8			50.9	49.3		51.9	51.0		53.9		49.7			51.0	
SERVICES	NEW BUSINESS	51.7		52.0	47.1			44.0	46.8		52.3	48.1		51.8		52.8			51.9	
SERVICES	OUTSTANDING BUSINESS				47.5			45.1	48.0		51.5	47.7		49.9		48.5			50.6	
SERVICES	BUSINESS EXPECTATIONS	63.2		66.5	58.3			57.9	53.1		71.7	63.0		62.7		69.7			59.1	
SERVICES	NEW EXPORT ORDERS	49.3		49.3	46.0			46.6	43.6		53.4	48.0		46.0		50.5			49.5	

Emerging countries

	December 2023	LAT AM: BRAZIL	LAT AM: MEXICO	Eurasia: CZECH REPUBLIC	Eurasia: POLAND	Eurasia: RUSSIA	Eurasia: TURKEY	Middle East & Africa: EGYPT	Middle East & Africa: LEBANON	Middle East & Africa: SAUDI ARABIA	Middle East & Africa: SOUTH AFRICA	Middle East & Africa: UAE	Asia: CHINA	Asia: HONG KONG	Asia: INDIA	Asia: INDONESIA	Asia: VIETNAM
	COMPOSITE	50.0				55.7							52.6		58.5		
	MANUFACTURING	48.4	52.0	41.8	47.4	54.6	47.4	48.5	48.4	57.5		57.4	50.8		54.9	52.2	48.9
	SERVICES - BUSINESS ACTIVITY	50.5				56.2							52.9	51.3	59.0		
MANUFACTURING	NEW ORDERS	46.7	52.8	38.6	46.6	56.6	45.3	46.9	49.1	68.3	47.1	63.0	52.0	50.7	57.3	53.4	47.8
MANUFACTURING	NEW EXPORT ORDERS	44.1	49.7	39.4	47.5	48.1	48.0	48.5	49.1	53.9	48.0	50.3	49.5	49.9	53.2	50.2	49.8
MANUFACTURING	DELIVERY TIMES*	50.2	54.0	47.8	49.8	54.3	49.4	50.4		38.8		45.4	50.9	51.1	50.7	49.9	49.7
MANUFACTURING	EMPLOYMENT	52.1	48.7	43.5	47.3	54.3	50.1	51.0		51.2		51.4	48.1		50.2	50.5	49.9
MANUFACTURING	INPUT PRICES	54.5	64.8	46.1	49.6	65.6	58.9	60.4		54.5		51.5	50.5	53.3	51.1	58.2	55.5
MANUFACTURING	OUTPUT PRICES	49.1	51.1	48.9	47.8	58.9	56.8	52.0	50.7	52.9		48.2		52.8	52.1	52.0	50.2
MANUFACTURING	OUTPUT	48.4	51.6	41.5	47.4	54.4	46.8	46.7		61.0		63.9	52.3		57.4	53.5	48.9
MANUFACTURING	STOCKS OF PURCHASES	43.6	54.0	40.2	46.9	50.0	47.4	50.1		56.4		54.4	49.0		57.1	52.7	49.2
MANUFACTURING	QUANTITY OF PURCHASES	47.2	53.2	36.4	45.9	59.7	46.5	47.2		60.8		57.7	50.0		56.2	54.6	50.0
MANUFACTURING	FINISHED GOODS	46.6	50.7	47.5	51.7	48.0	47.5						50.4		47.1	49.8	50.0
MANUFACTURING	WORK BACKLOGS	43.8	50.9	44.1	46.4	49.1		50.2		48.2		50.7	49.4		50.8	50.1	50.6
SERVICES	INPUT PRICES	56.4				64.6							52.1		52.2		
SERVICES	OUTPUT PRICES	54.4				56.6							50.5		53.0		
SERVICES	EMPLOYMENT	50.1				54.8							50.4		50.7		
SERVICES	NEW BUSINESS	50.9				56.8							53.8	47.8			
SERVICES	OUTSTANDING BUSINESS	46.0				52.6							50.0				
SERVICES	BUSINESS EXPECTATIONS					69.6								51.3			
SERVICES	NEW EXPORT ORDERS	32.0				60.5							52.2	51.3	51.9		

* inverted scale

Colour scale: 46 | 48 | 50 | 52 | 54

Source: S&P Global, BNP Paribas

3.1 UNITED STATES

Summary: beating expectations

1. The possibility of a US recession triggered by monetary tightening is looking less and less likely given the resilience of an economy that continued to grow by 0.8% q/q in Q4 2023 and by 2.5% on average over the year as a whole.
2. Our central scenario is now that of a marked slowdown albeit without an economic recession in H1 2024.
3. The Federal Reserve can now look forward to a soft landing and consider rate cuts in 2024.
4. As the year progresses, political events will take centre stage.

US: Beige book shows positive growth expectations, a cooling labour market and declining pricing power

Overall Economic Activity

A majority of the twelve Federal Reserve Districts reported little or no change in economic activity since the prior Beige Book period. Of the four Districts that differed, three reported modest growth and one reported a moderate decline. Consumers delivered some seasonal relief over the holidays by meeting expectations in most Districts and by exceeding expectations in three Districts, including in New York, which noted strong holiday spending on apparel, toys, and sporting goods. In addition, seasonal demand lifted airfreight volume from ecommerce in Richmond and credit card lending in Philadelphia. Several Districts noted increased leisure travel, and a tourism contact described New York City as bustling. Contacts from nearly all Districts reported decreases in manufacturing activity. Districts continued to note that high interest rates were limiting auto sales and real estate deals; however, the prospect of falling interest rates was cited by numerous contacts in various sectors as a source of optimism. In contrast, concerns about the office market, weakening overall demand, and the 2024 political cycle were often cited as sources of economic uncertainty. Overall, most Districts indicated that expectations of their firms for future growth were positive, had improved, or both.

Labor Markets

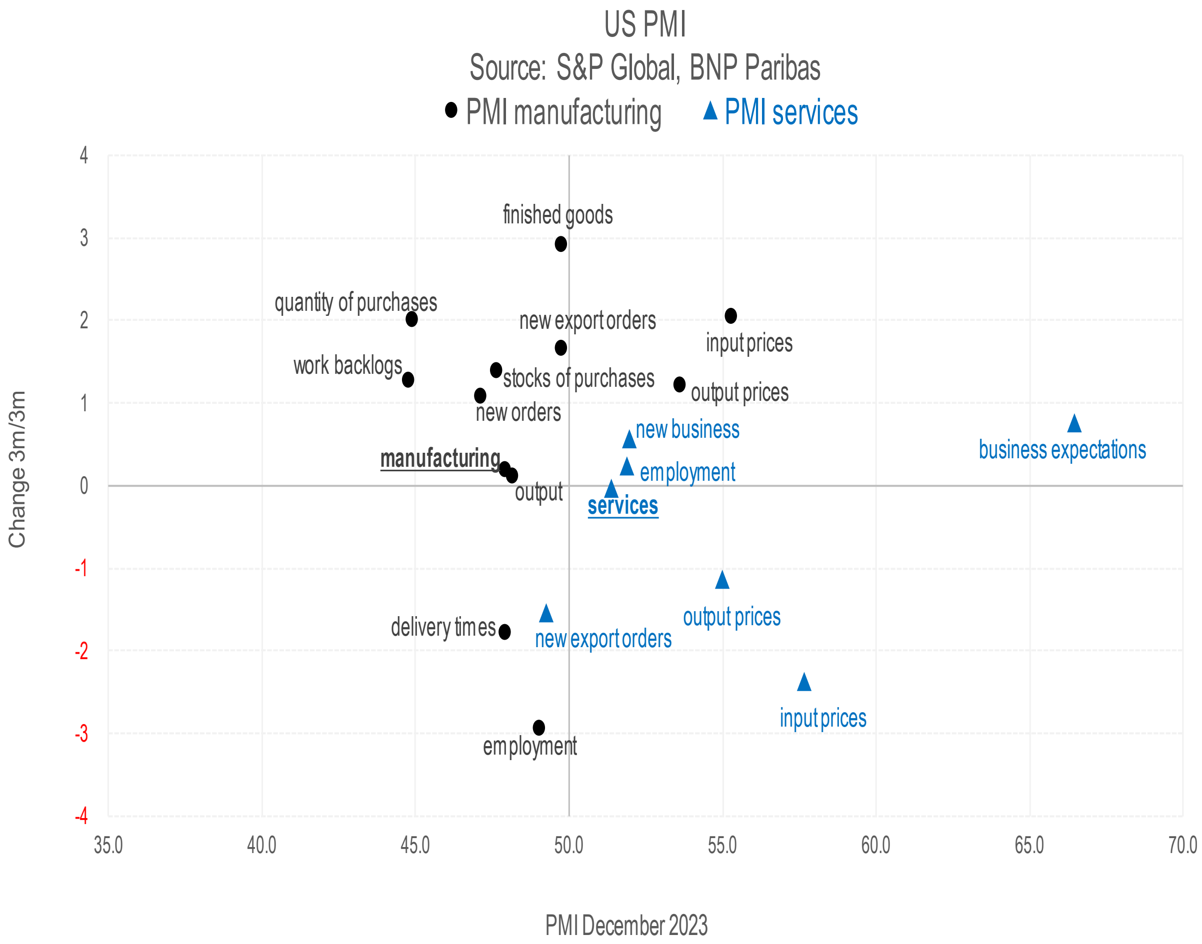
Seven Districts described little or no net change in overall employment levels, while the pace of job growth was described as modest to moderate in four Districts. Two Districts continued to note a tight labor market, and several described hiring challenges for firms seeking specialty skills, such as auto mechanics or experienced engineers in the Boston and San Francisco Districts, respectively. However, nearly all Districts cited one or more signs of a cooling labor market, such as larger applicant pools, lower turnover rates, more selective hiring by firms, and easing wage pressures. The pace of wage growth was characterized as moderate in Boston, Richmond, Chicago, and Dallas; as modest in New York and Philadelphia; and as slight in St. Louis. Firms from many Districts expected wage pressures to ease and wage growth to fall further over the next year.

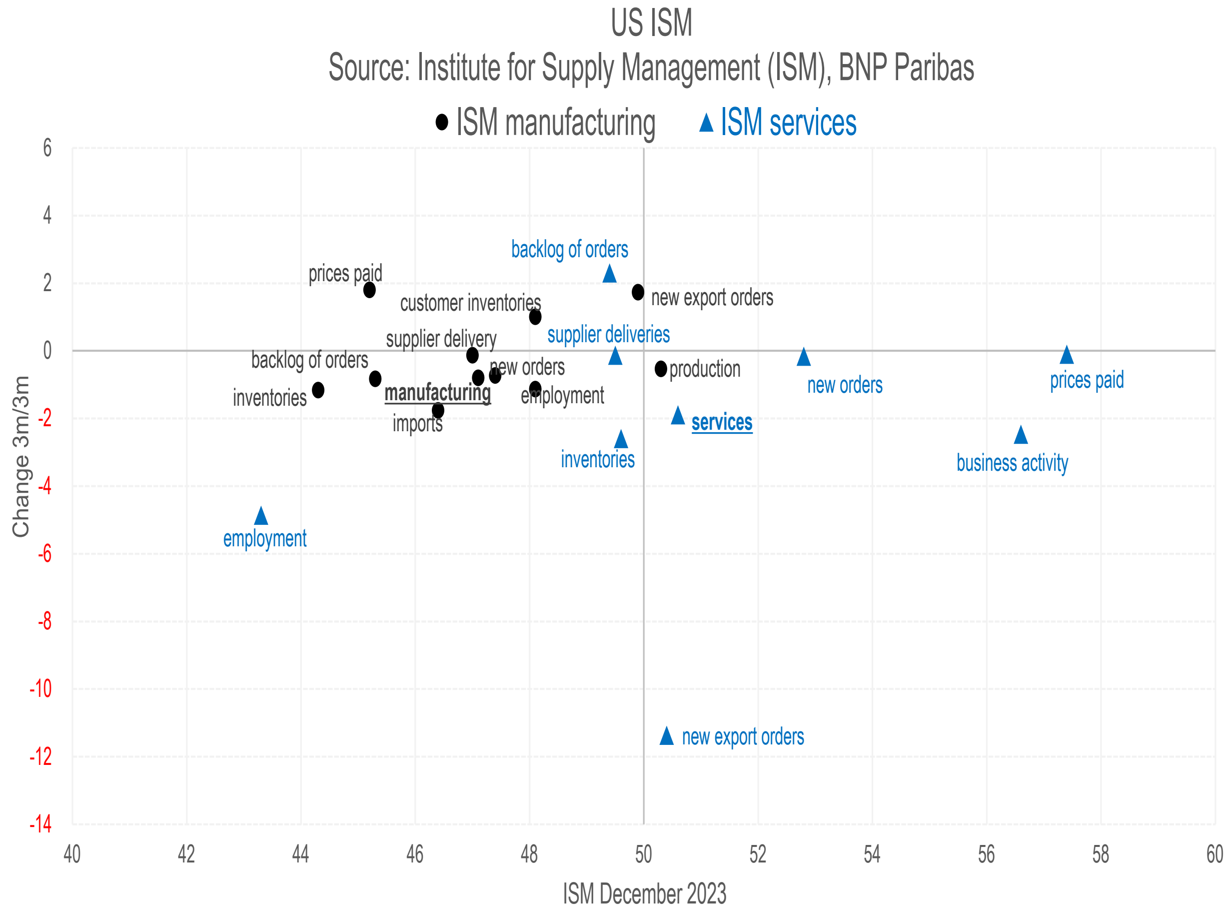
Prices

Six Districts noted that their contacts had reported slight or modest price increases, and two noted moderate increases. Five Districts also noted that overall price increases had subsided to some degree from the prior period, while three others indicated no significant shift in price pressures. Firms in most Districts cited examples of steady or falling input prices, especially in the manufacturing and construction sectors, and more discounting by auto dealers. Districts also noted that increased consumer price sensitivity had forced retailers to narrow their profit margins and to push back in turn on their suppliers' efforts to raise prices. Premium increases for property and casualty insurance and for health insurance continue to impact most firms. Three Districts noted that their firms were expecting price increases to ease further over the next year, while four Districts' firms anticipated little change.

Source: Federal Reserve

US: despite improved momentum, PMI and ISM levels still point to a contraction in manufacturing





Source: : S&P Global, Institute for Supply Management (ISM), BNP Paribas

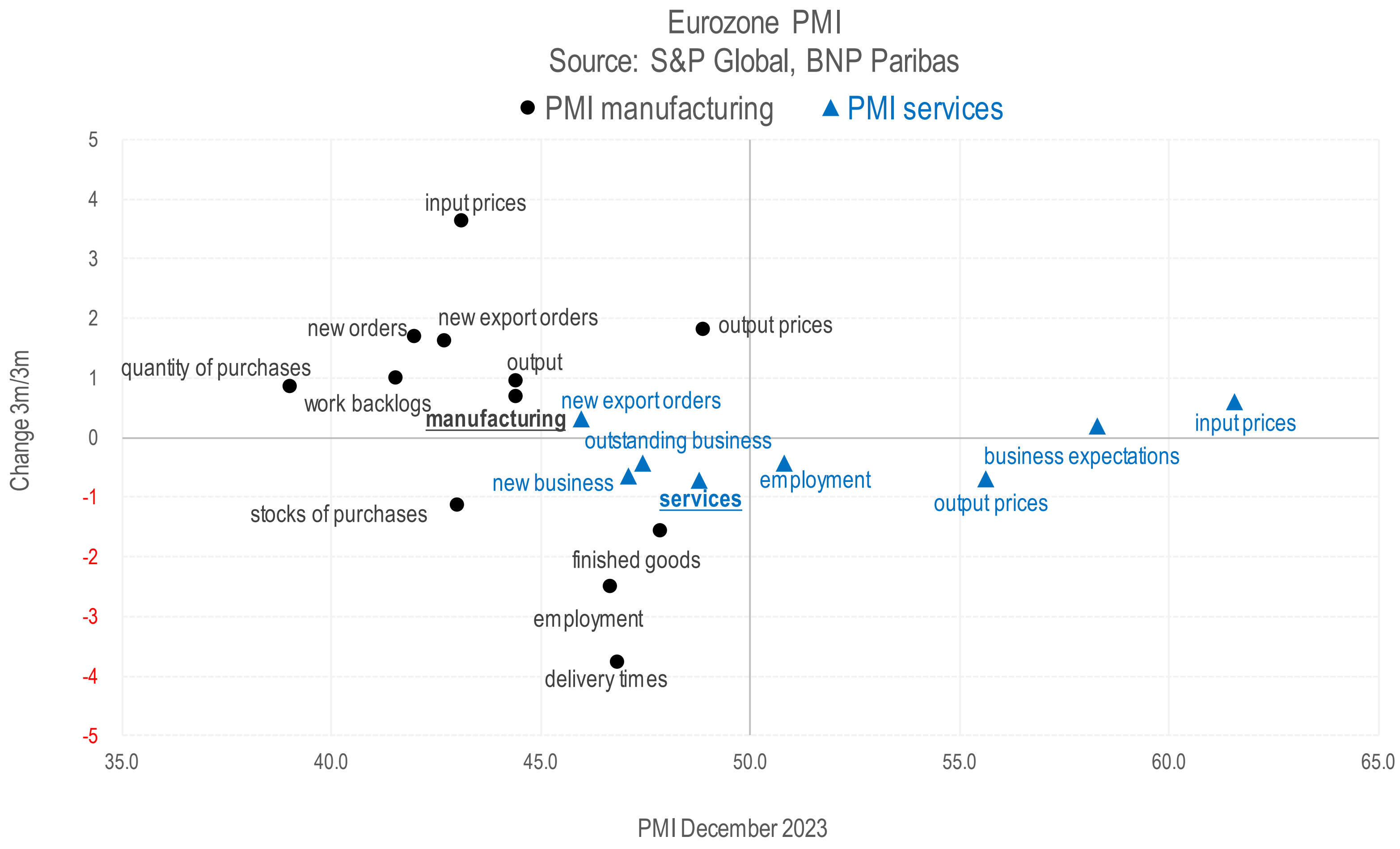
3.2

EUROZONE

Summary: ECB caution to continue despite decline of inflation

1. Euro zone activity is expected to pick up moderately in 2024, buoyed by the fall in inflation and the start of the cycle of policy rate cuts to key rates, which, according to our forecasts, will take place in April.
2. The labour market continues to surprise on the upside.
3. However, industrial production is falling sharply and remains highly exposed to escalating tensions in the Red Sea and the repercussions on shipping and supply chains.
4. 2024 will see a number of national parliamentary and presidential elections (Finland, Portugal, Belgium, Austria) and the European election (6 to 9 June). It seems likely that to some degree the political landscape in the region will be redrawn, causing shifts in the balance of power within the European Parliament.

Eurozone: manufacturing still in contraction territory but momentum has improved

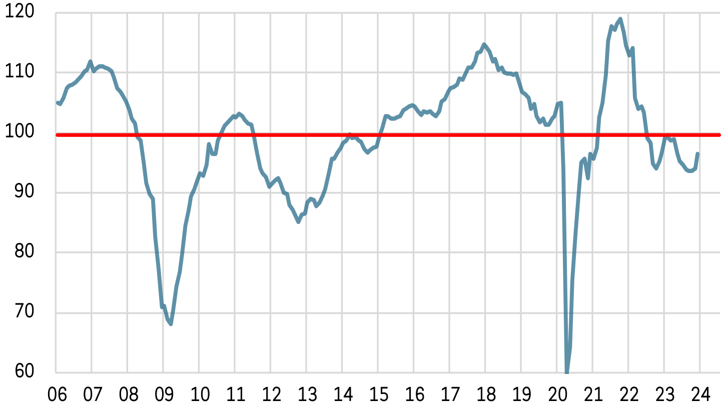


Source: S&P Global, BNP Paribas

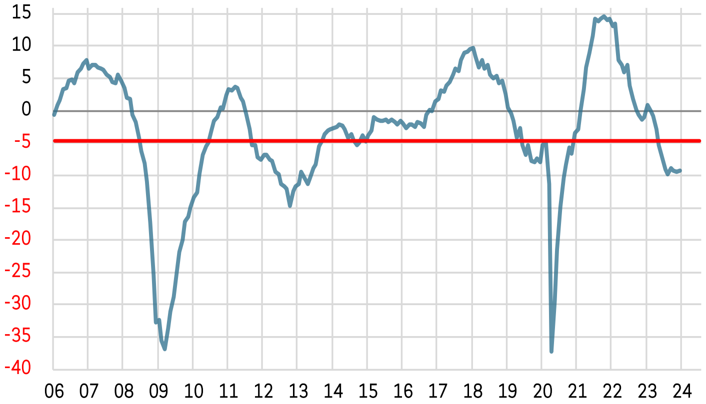
European Commission surveys show stabilisation

Eurozone: activity indicators

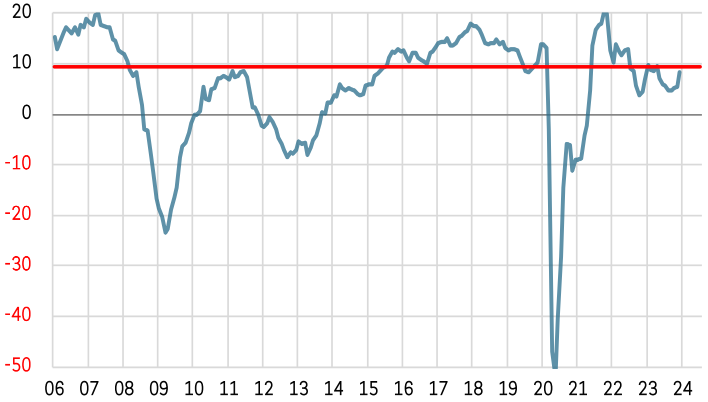
Economic Sentiment Index



Industrial confidence indicator

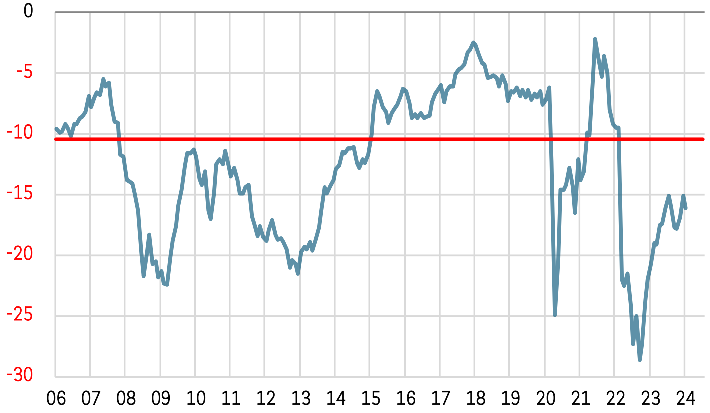


Services confidence indicator

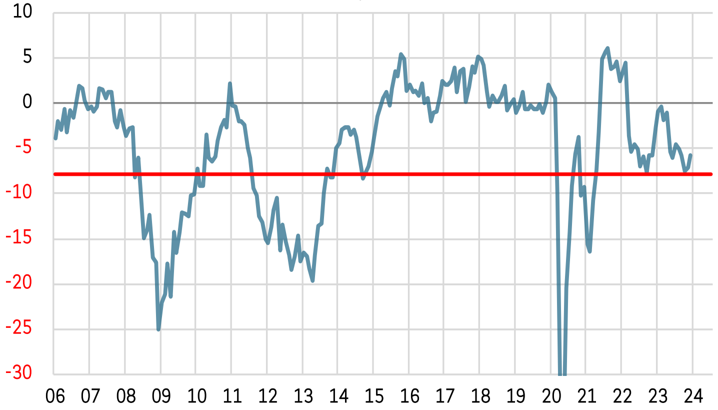


Construction confidence indicator

Consumer confidence indicator



Retail trade confidence indicator



line in red: historical average from 1985

Source: European Commission surveys, BNP Paribas

3.3 OTHER COUNTRIES

UK: flirting with recession

1. The UK economy is flirting with recession. The downturn in activity in the second half of 2023 is expected to continue until spring 2024 before an expected sluggish recovery, which nonetheless will be supported by the Bank of England (BoE) beginning its monetary easing cycle.
2. Despite an uptick in December 2023, inflation is continuing on its downward trajectory, which is clearly reflected in production prices and CBI surveys.
3. The turnaround in the labour market, which is still muted, is helping to reduce upward pressures on wages.
4. While this is good news for inflationary momentum, it is also reducing private consumption.
5. The BoE has little room for manoeuvre, with a first policy rate cut expected to occur in June 2024. However, monetary easing is expected to be slow, with a drop of just one1 percentage point (5.25% to 4.25%) anticipated in 2024.

Japan: A monetary shift is drawing near

1. Faced with a natural disaster and a political crisis, 2024 is off to a rocky start for Japan.
2. However, the economic impact of the earthquake that struck the country's west coast on 1st January 2024 is expected to be fairly limited due to the authorities' effective preparations and quick response in dealing with this type of event.
3. After an expected growth of +0.4% q/q in the fourth quarter of 2023, activity should slow in the first quarter of 2024, although it will remain positive at 0.2% q/q.
4. The fall in inflation and bond yields at the end of 2023 is providing some breathing room for the BoJ, which is expected to end its negative interest rate policy in March or April.
5. The road to monetary normalisation will be challenging for the BoJ, which, through its large-scale purchases of government bonds, has exacerbated the liquidity problems and volatility in the JGB market.

China: Still showing some weakness

- In Q4 2023, Chinese economic growth accelerated slightly to 5.2% year-on-year (y/y), compared to 4.9% in Q3. However, it lost momentum in quarter-on-quarter terms, standing at +1% q/q in Q4 vs. +1.5% in Q3.
- The Chinese economy continues to face a large number of vulnerabilities, which are likely to persist in the short term.
- The main causes for concern relate to domestic demand. In particular, the crisis in the property sector intensified further in late 2023.
- Weak demand and low confidence levels in the Chinese private sector have persisted. .
- In Q4 2023, deflationary pressures resulted from weak domestic demand, the fall in food prices, the correction in commodity prices and the decline in housing prices.
- The performance of the manufacturing export sector has strengthened, in contrast with the performances of domestically-oriented sectors.

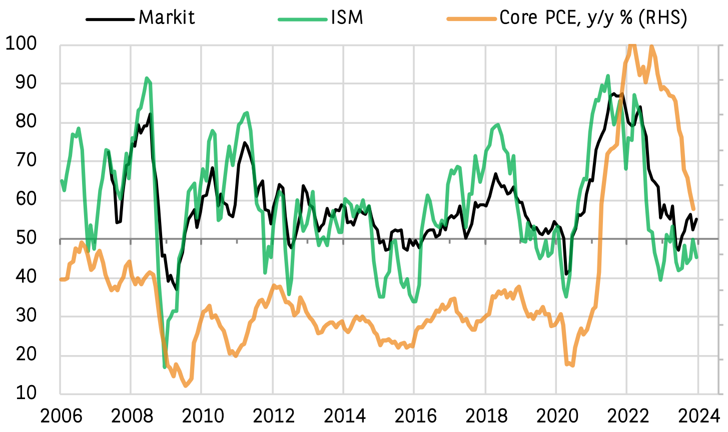
4

FINANCIAL MARKETS AND CENTRAL BANKS:

‘WE HEAR WHAT YOU SAY BUT WE’RE NOT LISTENING’

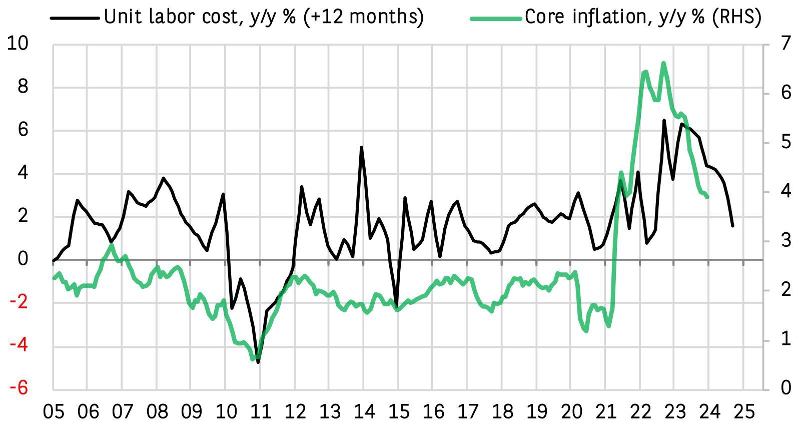
US disinflation continues

US: manufacturing input prices or prices paid



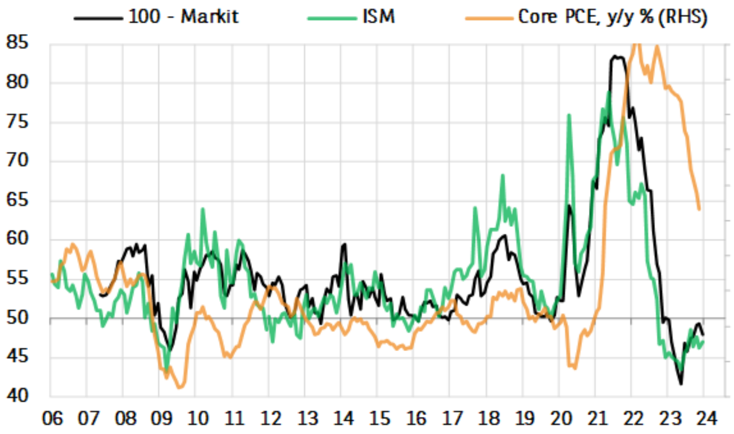
Source: S&P Global, ISM, BNP Paribas

Unit labor cost vs core inflation



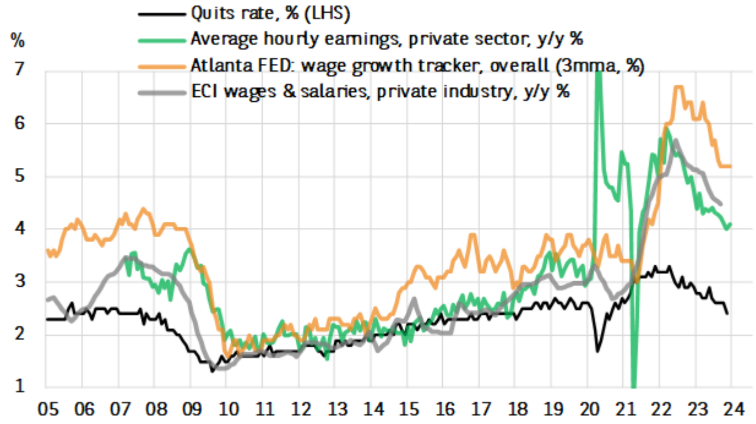
Source: BLS, BNP Paribas

US: manufacturing supplier's delivery times



Source: S&P Global, ISM, BNP Paribas

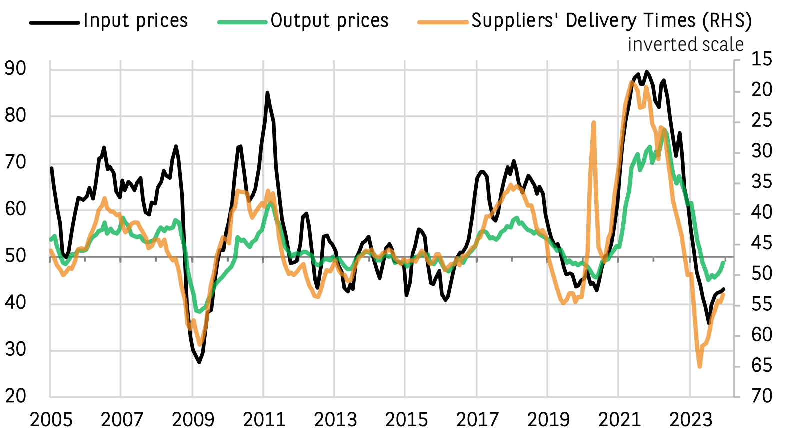
US wages indicators



Source: BLS, Atlanta FED, BNP Paribas

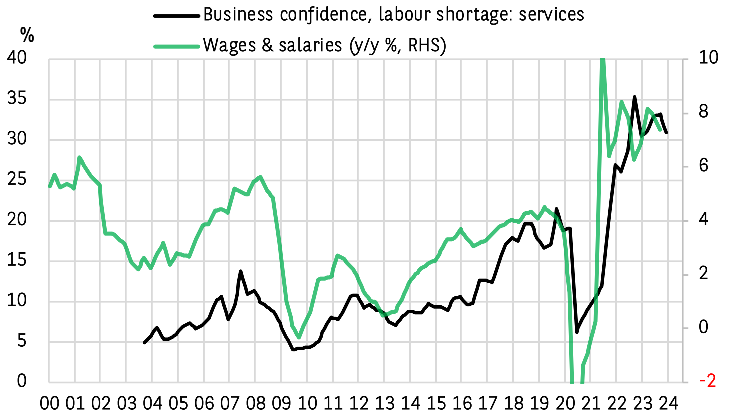
Eurozone disinflation (core HICP) has accelerated in recent months

Eurozone: PMI manufacturing components



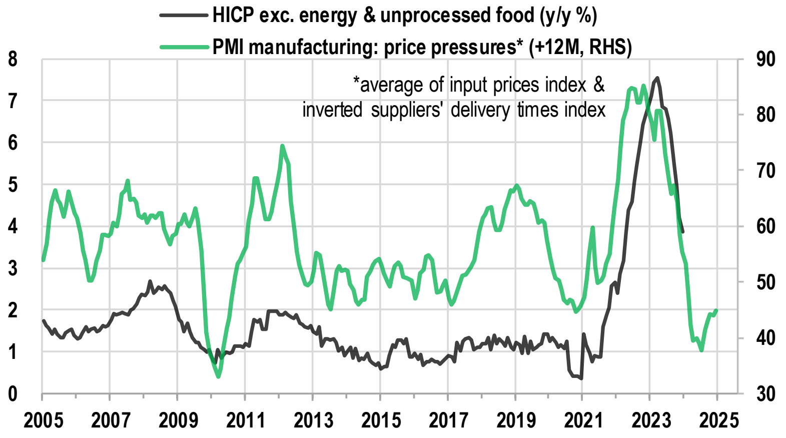
Source: S&P Global, BNP Paribas

Eurozone: labour shortage and wages



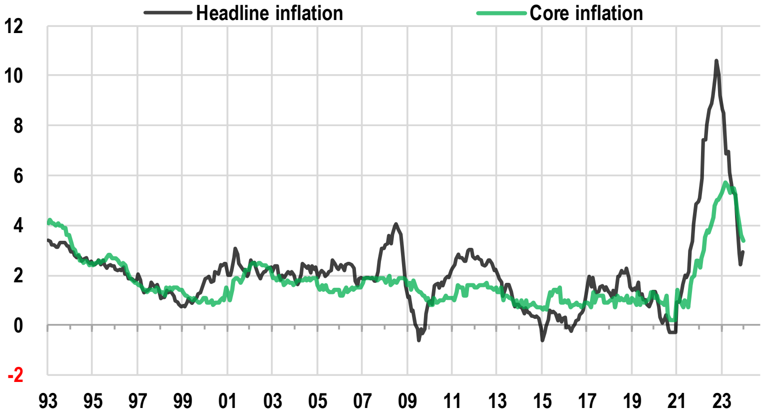
Source: European Commission surveys, Eurostat, BNP Paribas

Eurozone: PMI manufacturing components vs inflation



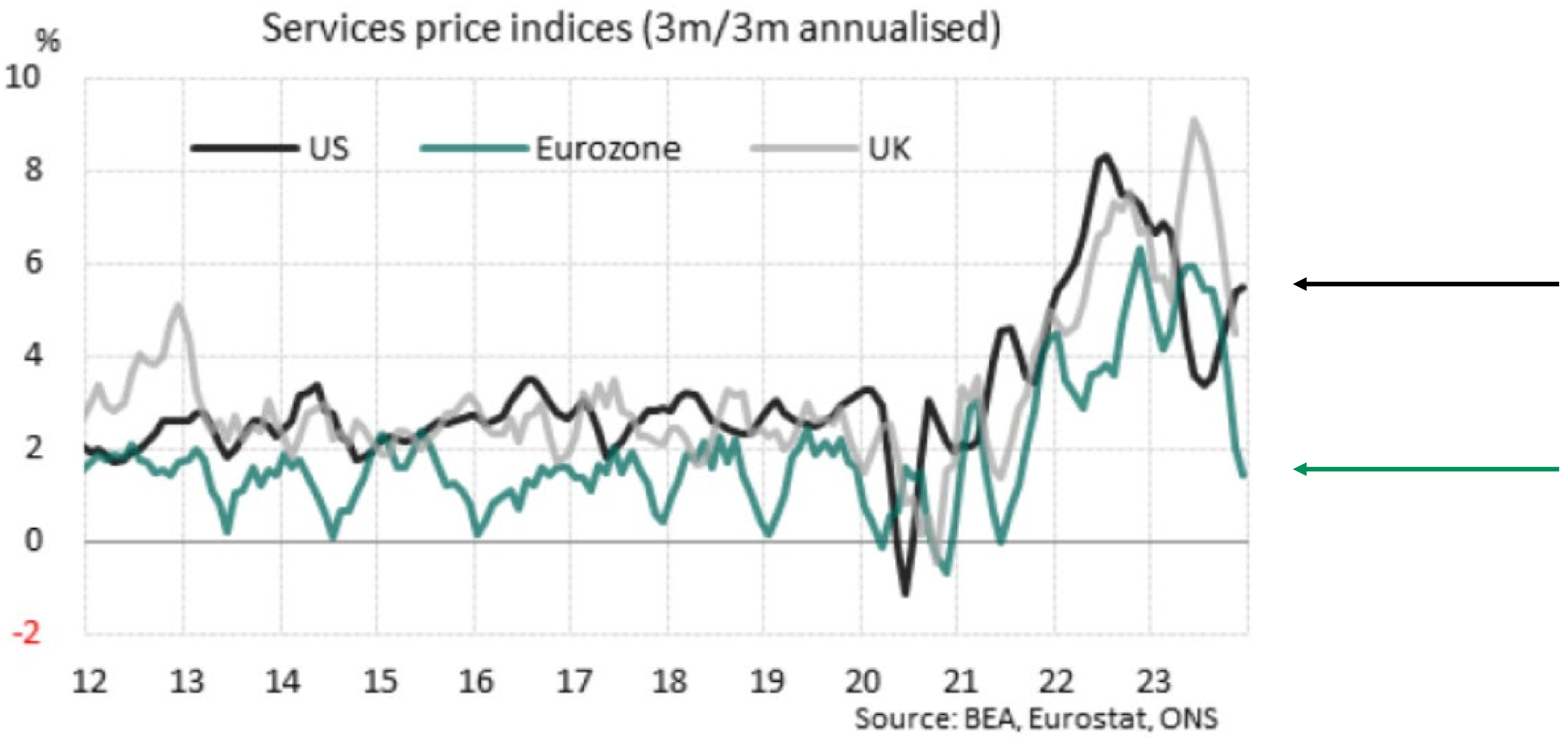
Source: S&P Global, Eurostat, BNP Paribas

Eurozone: core and headline inflation, %



Source: Eurostat, BNP Paribas

Services inflation has dropped in Eurozone but rebounded in US



Federal Reserve: rates will decline but cuts to be carefully calibrated and not rushed

inflation has been running close to 2 percent for the last 6 months. For a macroeconomist, this is almost as good as it gets.

But will it last? Time will tell whether inflation can be sustained on its recent path and allow us to conclude that we have achieved the FOMC's price-stability goal. Time will tell if this can happen while the labor market still performs above expectations. The data we have received the last few months is allowing the Committee to consider cutting the policy rate in 2024. However, concerns about the sustainability of these data trends requires changes in the path of policy to be carefully calibrated and not rushed. In

Source: Almost as Good as It Gets…But Will It Last?, Remarks by Christopher J. Waller, Member Board of Governors of the Federal Reserve System at The Brookings Institution, Washington, D.C., 16 January 2024.

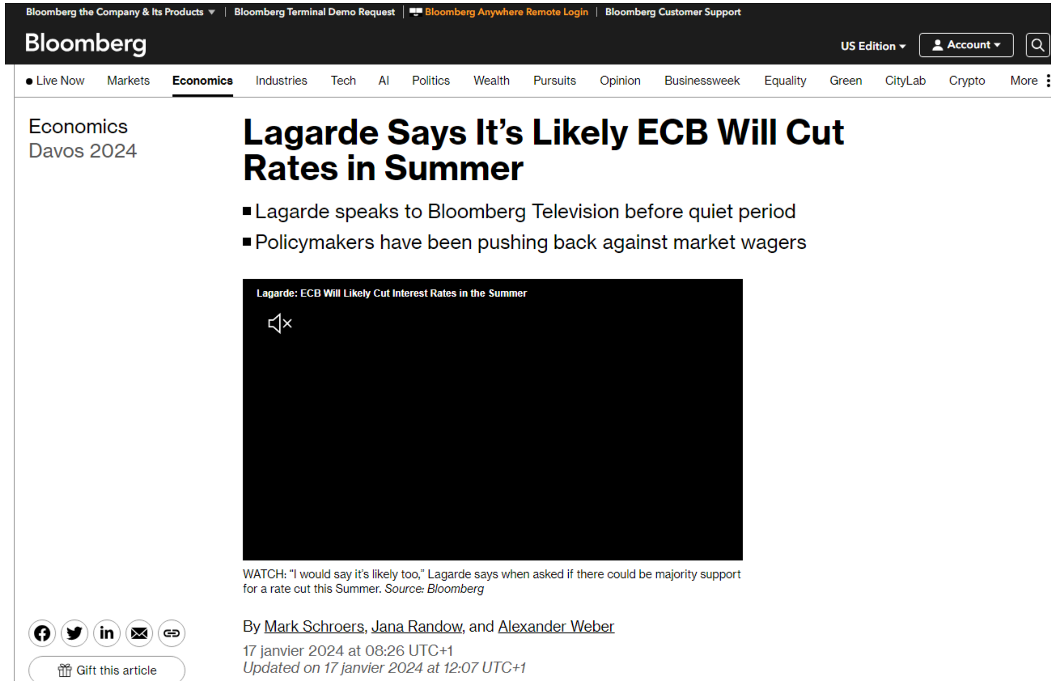
Percent

Variable	Median[1] 2023	2024	2025	2026	Longer run
Memo: Projected appropriate policy path					
Federal funds rate	5.4	4.6	3.6	2.9	2.5
September projection	5.6	5.1	3.9	2.9	2.5

The projections for the federal funds rate are the value of the midpoint of the projected appropriate target range for the federal funds rate or the projected appropriate target level for the federal funds rate at the end of the specified calendar year or over the longer run.

Source: Federal Reserve, Summary of Economic Projections, December 2023

ECB: first cut is likely in summer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Economics
Davos 2024

Lagarde Says It's Likely ECB Will Cut Rates in Summer

- Lagarde speaks to Bloomberg Television before quiet period
- Policymakers have been pushing back against market wagers

WATCH: "I would say it's likely too," Lagarde says when asked if there could be majority support for a rate cut this Summer. *Source: Bloomberg*

By Mark Schroers, Jana Randow, and Alexander Weber

17 janvier 2024 at 08:26 UTC+1
Updated on 17 janvier 2024 at 12:07 UTC+1

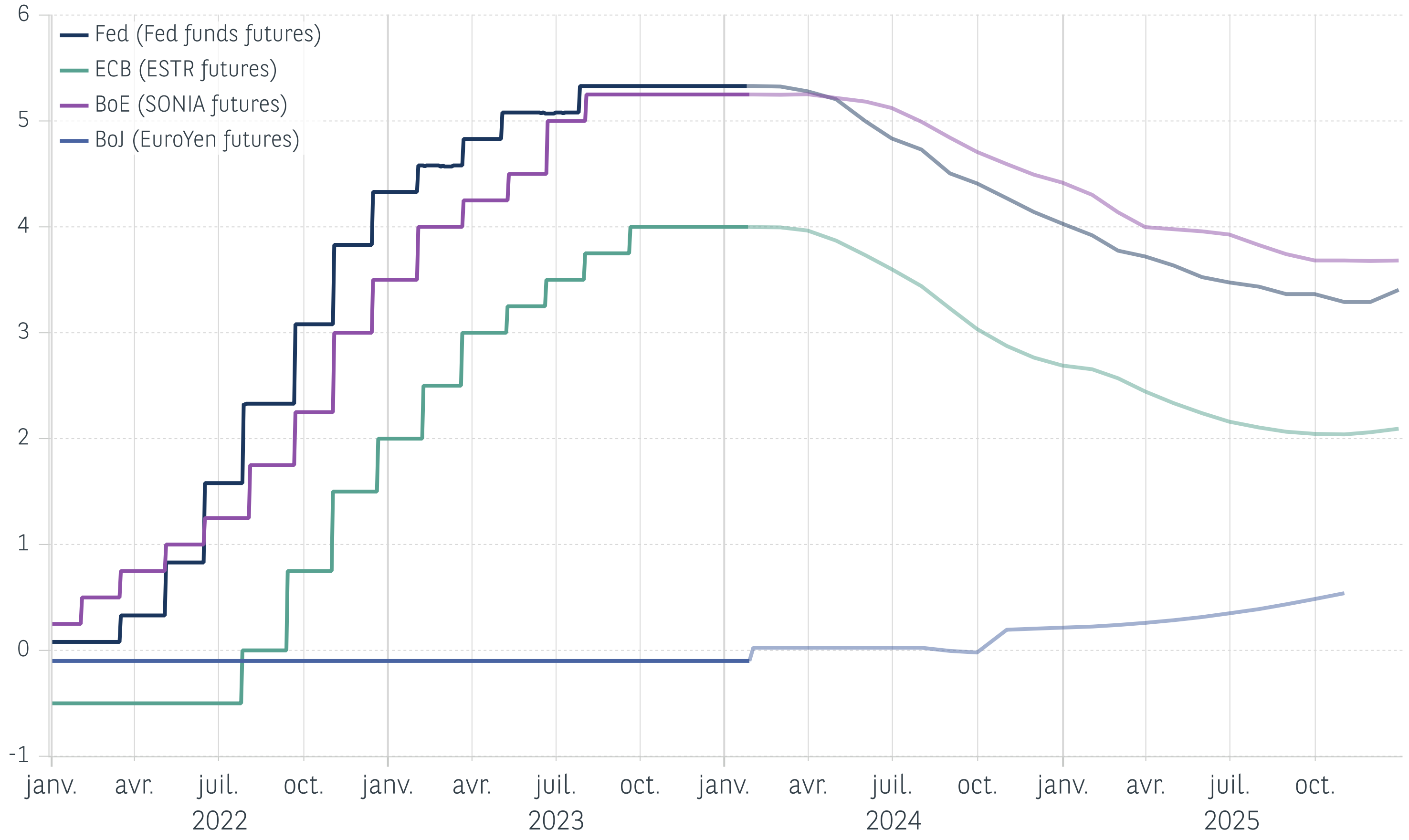
Gift this article

Source: Bloomberg

"On wage growth, I think whether you look at past wage numbers, whether you dissect that in compensation per employee, in negotiated wages, taking on or excluding the one-off payments, we are seeing a slight decline. So it's directionally good from our perspective. To your question about should it stabilise or should it decline, it's already declining. Clearly, our hope is that the wage increases – because we are still seeing an increase, whether you look at 5.2% or 3.4% depending on what measurement item you take – are sufficiently absorbed by the profit unit, as we are seeing happening at the moment.
It's also one of the reasons why we see growth coming up and the recovery beginning in the course of 2024; because of rising wages while inflation comes down, which will free up some purchasing power, which hopefully will stimulate consumption."

Source: Press conference, Christine Lagarde, President of the ECB, Luis de Guindos, Vice-President of the ECB, Frankfurt am Main, 25 January 2024

Markets price in earlier and more rate cuts



Source: Macrobond, BNP Paribas

Markets are 'rationally bullish'

The perspective from the central bank

1. Concern about avoiding premature easing, with the risk of having to change message or even being forced to hike rates after having cut them.
2. This would have a negative impact on their credibility.
3. Talking about possibility of early cuts could trigger a further easing of financial conditions (rising stock prices, falling interest rates for debt issued by companies). This could be counterproductive for monetary policy.
4. Faced with uncertainty about the extent and speed of disinflation, central banks have an interest in emphasising that they remain cautious, <u>especially since they still have the optionality to quickly alter the policy message if warranted.</u>

The perspective from financial markets

1. Competition amongst investors is pushing them to be 'rationally bullish't
2. Investors rely on more and earlier cuts in official rates than envisaged by the central banks.
3. Investors <u>want to avoid not being on the train when it leaves the station</u>, i.e. missing out on a rally when rates are being cut.

A difference in view between central banks and markets: does it matter?

1. Does this behaviour ("hearing but not listening") pose a risk to markets and the economy?
2. A likely consequence is increased volatility in fixed income markets, especially the short end of the curve, depending on messages from the central banks and the publication of economic data.
3. Monetary policy is closely linked to these data, but investor positioning is just as closely linked.
4. However, the impact of this volatility on the real sphere - economic activity and demand - should be very limited: for households and companies, trend is what matters, the fact that policy rates will fall, rather than their short-term fluctuations.

5

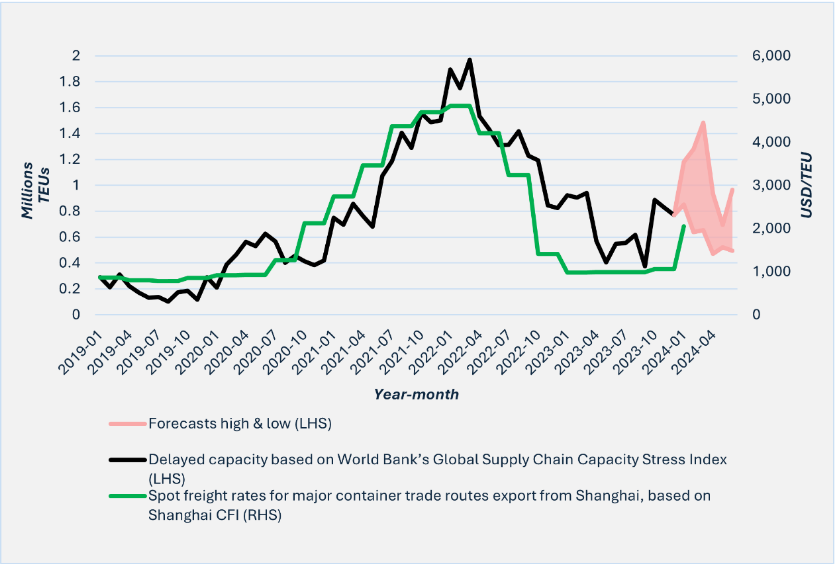
RISKS AND UNCERTAINTIES

Risks and uncertainties

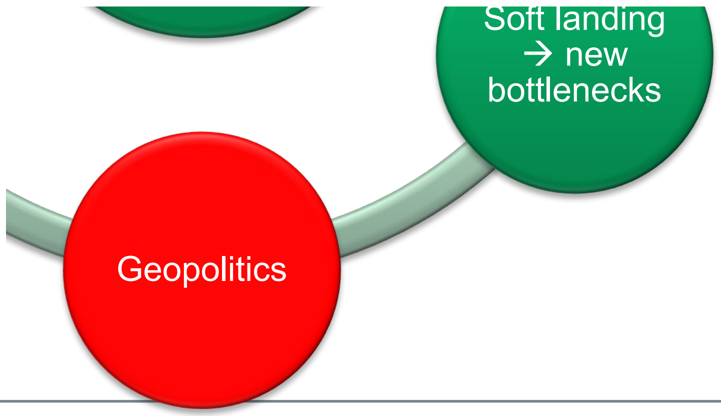
Risks and uncertainties

- Blockage of the Strait of Hormuz; **oil exported via the strait = +/- 18 mbd** +/- (+/-20% of oil traded worldwide), most impacted region would be Asia (destination of 80% of oil moving through Hormuz).
- **Available alternative capacity=3.8 mbd**
- **For the gas market, a blockage of Hormuz would stop Qatari exports of LNG, which account for 23% of global LNG trade. There is no alternative route**.

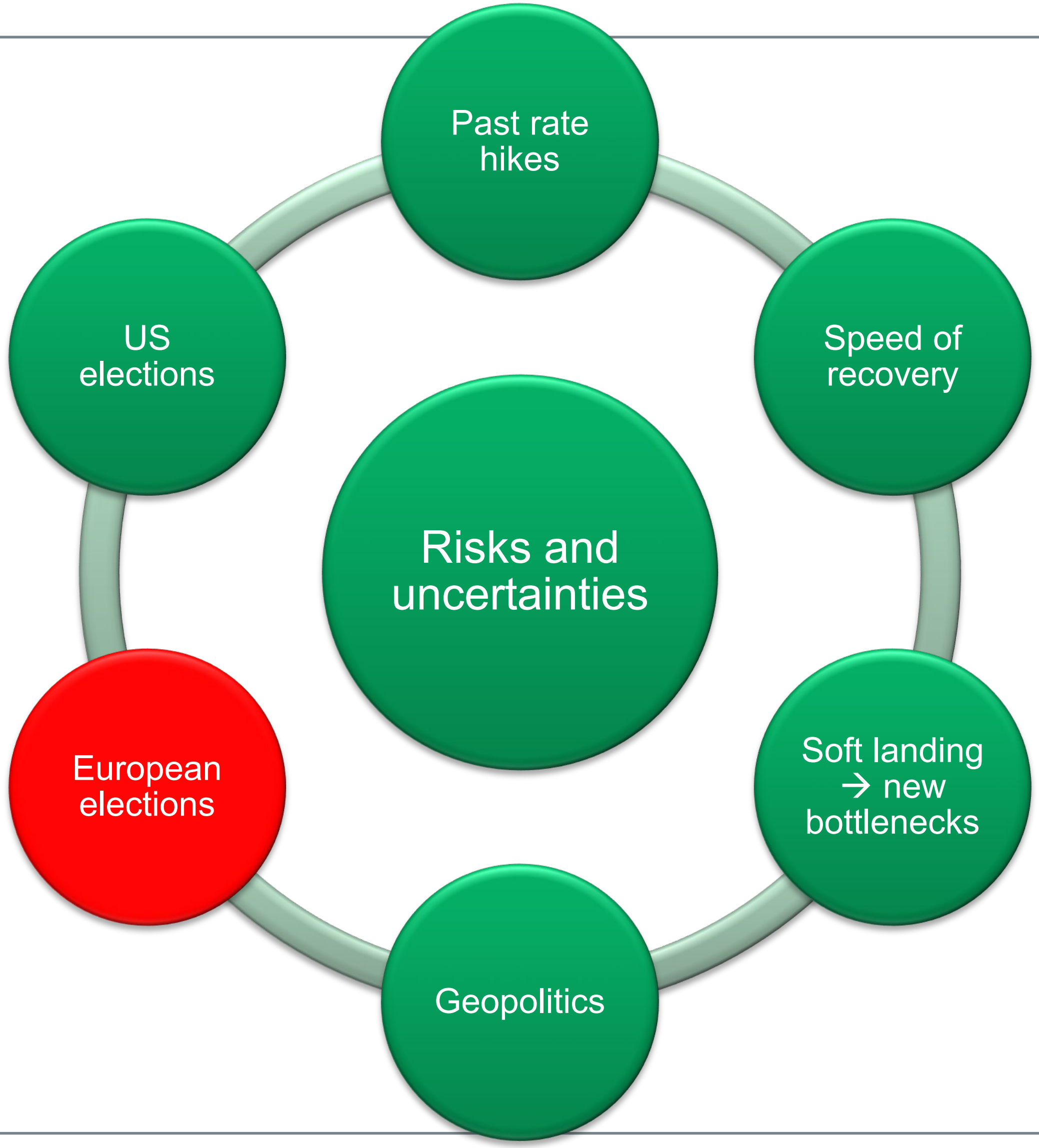
Figure 1: The World Bank's Global Supply Chain Stress Index jumped at the height of the COVID-19 supply-chain crisis and is forecast to rise again if Red Sea violence persists.



Source: WBG staff based on datasets provided by MarineTraffic and the Shanghai Export Containerized Freight Index (https://en.sse.net.cn/indices/scfinew.jsp).



Risks and uncertainties



Composition of and agenda of new European Commission

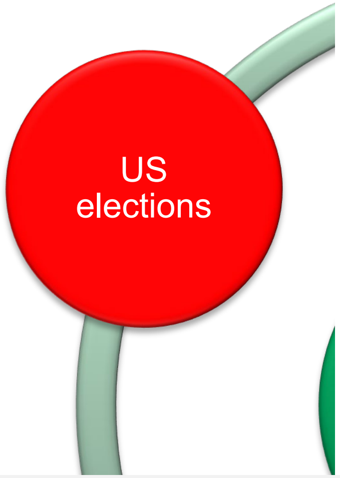
Composition of European Parliament

How easy or difficult will it be to agree, particularly under stress?

Risks and uncertainties

Polarisation comes with an economic cost

- **In case of a Trump victory, what happens to**
  - **Public finances**
  - **IRA**
  - **Climate-related policies**
  - **Import tariffs**
  - **Etc.**



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Help for the Heartland? The Employment and Electoral Effects of the Trump Tariffs in the United States

David Autor, Anne Beck, David Dorn & Gordon H. Hanson

WORKING PAPER 32082 DOI 10.3386/w32082 ISSUE DATE January 2024

"We study the economic and political consequences of the 2018-2019 trade war between the United States, China and other US trade partners at the detailed geographic level…**The trade-war has not to date provided economic help to the US heartland**…. **retaliatory tariffs had clear negative employment impacts,** primarily in agriculture; and these harms were only partly mitigated by compensatory US agricultural subsidies.
Consistent with expressive views of politics, **the tariff war appears nevertheless to have been a political success for the governing Republican party.** Residents of regions more exposed to import tariffs became less likely to identify as Democrats, more likely to vote to reelect Donald Trump in 2020, and more likely to elect Republicans to Congress. **Foreign retaliatory tariffs only modestly weakened that support.**"

6 APPENDIX

US: growth remained strong in Q4 2023

Table 2. Contributions to Percent Change in Real Gross Domestic Product

Line		2023	Seasonally adjusted at annual rates															
			2020				2021				2022				2023			
			Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	Percent change at annual rate:																	
1	**Gross domestic product**	**2,5**	**-5,3**	**-28,0**	**34,8**	**4,2**	**5,2**	**6,2**	**3,3**	**7,0**	**-2,0**	**-0,6**	**2,7**	**2,6**	**2,2**	**2,1**	**4,9**	**3,3**
	Percentage points at annual rates:																	
2	**Personal consumption expenditures**	**1,49**	**-4,34**	**-21,51**	**24,93**	**3,63**	**5,70**	**8,73**	**1,89**	**2,71**	**-0,03**	**1,32**	**1,05**	**0,79**	**2,54**	**0,55**	**2,11**	**1,91**
3	**Goods**	**0,47**	**-0,44**	**-1,59**	**10,23**	**0,71**	**3,52**	**3,24**	**-2,10**	**1,26**	**-0,30**	**-0,09**	**-0,18**	**-0,01**	**1,14**	**0,11**	**1,09**	**0,85**
4	Durable goods	0,34	-1,24	0,11	5,92	0,45	2,10	1,17	-2,26	0,89	0,12	-0,08	0,08	-0,08	1,07	-0,03	0,53	0,36
9	Nondurable goods	0,13	0,80	-1,70	4,31	0,26	1,42	2,08	0,16	0,38	-0,42	-0,01	-0,26	0,07	0,07	0,14	0,56	0,49
14	**Services**	**1,02**	**-3,90**	**-19,92**	**14,70**	**2,92**	**2,18**	**5,49**	**3,99**	**1,45**	**0,27**	**1,41**	**1,23**	**0,80**	**1,40**	**0,44**	**1,02**	**1,06**
26	**Gross private domestic investment**	**-0,21**	**-1,87**	**-9,29**	**13,52**	**2,36**	**-0,46**	**-0,84**	**2,71**	**4,63**	**1,16**	**-2,10**	**-1,45**	**0,62**	**-1,69**	**0,90**	**1,74**	**0,38**
27	**Fixed investment**	**0,09**	**-0,57**	**-5,28**	**5,04**	**2,55**	**1,63**	**1,05**	**-0,28**	**0,35**	**1,23**	**-0,05**	**-0,79**	**-0,99**	**0,53**	**0,90**	**0,46**	**0,31**
28	Nonresidential	0,58	-1,09	-4,12	2,69	1,35	1,18	1,27	-0,15	0,37	1,32	0,68	0,62	0,24	0,76	0,98	0,21	0,26
39	Residential	-0,49	0,52	-1,16	2,35	1,20	0,44	-0,22	-0,13	-0,02	-0,09	-0,73	-1,41	-1,23	-0,22	-0,09	0,26	0,04
40	**Change in private inventories**	**-0,31**	**-1,30**	**-4,01**	**8,48**	**-0,18**	**-2,08**	**-1,89**	**2,99**	**4,28**	**-0,07**	**-2,05**	**-0,66**	**1,61**	**-2,22**	**0,00**	**1,27**	**0,07**
43	**Net exports of goods and services**	**0,58**	**0,09**	**1,00**	**-2,58**	**-1,44**	**-1,04**	**-0,87**	**-1,03**	**-0,34**	**-2,59**	**0,56**	**2,58**	**0,26**	**0,58**	**0,04**	**0,03**	**0,43**
44	**Exports**	**0,32**	**-1,81**	**-8,78**	**5,06**	**2,31**	**0,06**	**0,20**	**0,16**	**2,42**	**-0,50**	**1,19**	**1,80**	**-0,41**	**0,76**	**-1,09**	**0,59**	**0,68**
47	**Imports**	**0,26**	**1,89**	**9,78**	**-7,65**	**-3,74**	**-1,10**	**-1,07**	**-1,19**	**-2,76**	**-2,08**	**-0,63**	**0,77**	**0,66**	**-0,18**	**1,13**	**-0,56**	**-0,25**
50	**Government consumption expenditures and gross investment**	**0,68**	**0,78**	**1,78**	**-1,03**	**-0,35**	**1,04**	**-0,80**	**-0,26**	**-0,04**	**-0,52**	**-0,34**	**0,49**	**0,90**	**0,82**	**0,57**	**0,99**	**0,56**

Source: U.S. Bureau of Economic Analysis

Eurozone: no recession in 2023 but mixed fortunes among Member States

- The eurozone narrowly escaped economic contraction in the last quarter of 2023, but the picture is mixed among countries. According to preliminary figures from Eurostat, real GDP in the euro area remained stable in Q4, following a slight decline of 0.1% q/q in Q3.
- Quarterly growth surprised to the upside in Spain (+0.6%), Italy (+0.2%), while the data for France (0.0%) and Germany (-0.3%) were in line with the consensus. The largest decline in the euro area came from Ireland (-0.7%) while Portugal's growth rose the most (+0.8%).
- Annual growth of 0.5% in the euro area for 2023 is in line with our forecast and gives a flat carry-over for 2024.
- As in 2022, Southern European countries were the main drivers to growth in the euro area in 2023. Conversely, a quarter of Member Countries saw their activity contract on an annual average in 2023: Germany, the Czech Republic, Austria, Latvia, and Ireland. Apart from Ireland – where the GDP data are volatile due to the activity of multinationals operating on the territory – the other four economies, which are relatively more industrialised than the rest of the Member States, have, among other things, suffered from the greater slowdown in demand in this sector.
- That said, Government expenditures remains an important driver of activity in several countries – rising 4.7% in France and 3.9% in Spain in 2023 – and masks some fragility in private domestic demand.
- The expected decline in inflation in the euro area in the first quarter of 2024 should allow activity to recover a little in Q1 (+0.1% according to our forecasts) before a more solid recovery in Q2 (+0.3% q/q) and a fortiori in the second half of the year, thanks to the start of the ECB's key rate cut.

Forecasts: emerging markets

BNP Paribas GDP growth forecasts Emerging Markets	ANNUAL GROWTH (% y/y)		
	2023	2024	2025
Latam			
Argentina	-2.0	-2.0	2.5
Brazil	3.1	1.8	1.8
Chile	-0.1	1.0	2.0
Colombia	1.1	1.0	2.5
Mexico	3.5	2.5	2.0
CEEMEA			
Czech Rep.	-0.4	1.6	2.9
Egypt	3.8	3.9	3.8
Hungary	-0.5	3.3	3.2
Poland	0.2	4.0	3.5
Romania	2.0	2.8	3.1
Saudi Arabia	-0.3	4.0	4.8
South Africa	0.6	1.1	1.9
Turkey	4.5	3.5	3.0
UAE	2.4	5.3	3.2
EM Asia			
India	7.5	7.0	6.5
Indonesia	4.9	4.8	5.3
Malaysia	4.4	3.9	4.2
South Korea	1.2	1.8	2.1
Thailand	2.3	3.7	4.5

BNP Paribas consumer price inflation forecasts Emerging Markets	ANNUAL RATE (% y/y)		
	2023	2024	2025
Latam			
Argentina	125.8	221.0	86.0
Brazil	4.6	3.6	3.9
Chile	7.7	4.0	3.0
Colombia	11.8	6.6	3.8
Mexico	5.6	4.3	3.9
CEEMEA			
Czech Rep.	10.9	3.2	2.5
Egypt	34.8	30.4	13.7
Hungary	17.8	4.8	3.6
Poland	11.5	6.0	4.0
Romania	10.6	5.5	4.0
Saudi Arabia	2.4	1.9	2.1
South Africa	5.8	4.7	4.3
Turkey	53.9	50.1	26.0
UAE	2.9	1.8	1.4
EM Asia			
India	5.8	5.7	4.5
Indonesia	3.5	2.7	2.5
Malaysia	2.5	2.8	2.4
South Korea	3.7	2.6	2.1
Thailand	1.4	2.4	2.0

BNP Paribas end-period policy rate forecasts (%) Emerging Markets	YEAR END		
	2023	2024	2025
Latam			
Argentina	143.00	75.00	60.00
Brazil	11.75	8.50	10.00
Chile	8.25	5.25	4.50
Colombia	13.00	8.50	5.75
Mexico	11.25	9.25	6.75
CEEMEA			
Czech Rep.	6.75	4.00	3.00
Egypt	21.25	28.25	23.25
Hungary	10.75	6.00	4.00
Poland	5.75	5.25	4.00
Romania	7.00	5.50	3.75
Saudi Arabia	5.75	4.25	3.75
South Africa	8.25	7.00	6.75
Turkey	42.50	30.0	20.0
UAE	5.15	3.65	3.15
EM Asia			
India	6.50	6.00	5.25
Indonesia	6.00	4.50	4.25
Malaysia	3.00	3.25	3.00
South Korea	3.50	2.75	2.50
Thailand	2.50	2.50	1.50

Source: BNP Paribas Markets360

Forecasts: exchange rates

BNP Paribas end-period FX forecasts

USD Bloc	Q1 2024	Q2 2024	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
EURUSD	1.10	1.12	1.14	1.15	1.16	1.17	1.18	1.18
USDJPY	145	141	138	135	133	132	131	130
USDCHF	0.89	0.88	0.88	0.87	0.86	0.85	0.85	0.85
GBPUSD	1.26	1.29	1.31	1.32	1.33	1.34	1.36	1.36
USDCAD	1.36	1.35	1.35	1.35	1.35	1.35	1.35	1.35
AUDUSD	0.66	0.67	0.69	0.70	0.70	0.70	0.70	0.70
NZDUSD	0.61	0.62	0.62	0.63	0.63	0.64	0.64	0.65
USDSEK	10.36	10.18	9.91	9.74	9.66	9.49	9.41	9.41
USDNOK	10.64	10.36	10.09	9.91	9.74	9.57	9.41	9.41

EUR Bloc	Q1 2024	Q2 2024	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
EURJPY	160	158	157	155	154	154	155	153
EURGBP	0.87	0.87	0.87	0.87	0.87	0.87	0.87	0.87
EURCHF	0.98	0.99	1.00	1.00	1.00	1.00	1.00	1.00
EURSEK	11.40	11.40	11.30	11.20	11.20	11.10	11.10	11.10
EURNOK	11.70	11.60	11.50	11.40	11.30	11.20	11.10	11.10
EURAUD	1.67	1.67	1.65	1.64	1.66	1.67	1.69	1.69
EURNZD	1.80	1.81	1.84	1.83	1.84	1.83	1.84	1.82
EURCAD	1.50	1.51	1.54	1.55	1.57	1.58	1.59	1.59

CEEMEA Bloc	Q1 2024	Q2 2024	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
USDPLN	3.95	3.84	3.73	3.70	3.71	3.68	3.64	3.64
EURCZK	24.80	25.40	25.70	26.00	26.00	26.00	26.00	26.00
EURHUF	385	390	395	400	405	410	415	420
USDZAR	19.00	19.00	18.75	18.50	18.25	18.00	18.00	18.00
EURRON	4.95	4.95	4.95	4.95	4.95	4.95	4.95	4.95
EURPLN	4.35	4.30	4.25	4.25	4.30	4.30	4.30	4.30
USDEGP	35.00	36.00	37.50	38.00	38.00	40.00	42.00	44.00
USDILS	3.80	3.75	3.70	3.60	3.60	3.55	3.55	3.50
USDCZK	22.55	22.68	22.54	22.61	22.41	22.22	22.03	22.03
USDHUF	350	348	346	348	349	350	352	356
USDRON	4.50	4.42	4.34	4.30	4.27	4.23	4.19	4.19

Asia Bloc	Q1 2024	Q2 2024	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
USDSGD	1.35	1.33	1.32	1.30	1.30	1.30	1.30	1.30
USDMYR	4.72	4.66	4.63	4.62	4.60	4.57	4.53	4.50
USDIDR	15,594	15,521	15,574	15,535	15,5	15,4	15,3	15,2
USDTHB	35.70	35.10	34.70	34.50	34.50	34.25	34.25	34.00
USDPHP	56.00	56.10	56.50	56.70	56.50	56.00	55.50	55.00
USDRMB	7.15	7.10	7.10	7.00	7.00	6.95	6.95	6.90
USDTWD	32.00	31.50	31.25	31.00	30.75	30.50	30.25	30.00
USDKRW	1,3	1,275	1,265	1,25	1,245	1,24	1,235	1,23
USDINR	83.40	83.90	84.50	84.60	84.00	83.60	83.30	83.00

Latam Bloc	Q1 2024	Q2 2024	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
USDBRL	4.90	4.80	4.70	4.60	4.55	4.50	4.50	4.50
USDCLP	880	870	865	860	855	850	850	845
USDMXN	17.80	17.80	17.70	17.60	17.50	17.50	17.40	17.40
USDCOP	4,1	4	3,95	3,95	3,9	3,9	3,9	3,9
USDPEN	3.75	3.75	3.70	3.65	3.65	3.60	3.60	3.60

Stronger euro versus USD on back of ECB cutting rates slighty less than Fed, market positioning and fair value analysis.

Stronger yen versus USD due to monetary policy divergence (rate cuts in US, less accommodative policy in Japan)

Source: BNP Paribas Markets360

Forecasts: commodity prices

BNP Paribas commodity price forecasts								
	Q1 2024	Q2 2024	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025	Q4 2025
ICE Brent 1m (USD/bbl)								
Quarter Average	**78**	**81**	**86**	**83**	**79**	**81**	**84**	**82**
NYMEX WTI 1m (USD/bbl)								
Quarter Average	**78**	**81**	**85**	**82**	**78**	**79**	**82**	**80**
Gold COMEX 1m (USD/oz)								
End Quarter	**2**	**2,05**	**2,1**	**2,02**	**2**	**1,96**	**1,92**	**1,89**
Quarter Average	**2,02**	**2,025**	**2,075**	**2,06**	**1,99**	**1,975**	**1,94**	**1,905**
Aluminium LME 3m (USD/t)								
End Quarter	**2,18**	**2,25**	**2,3**	**2,4**	**2,475**	**2,53**	**2,61**	**2,75**
Quarter Average	**2,19**	**2,215**	**2,275**	**2,35**	**2,435**	**2,505**	**2,57**	**2,68**
Copper LME 3m (USD/t)								
End Quarter	**8,3**	**8,4**	**8,45**	**8,6**	**8,8**	**8,91**	**9,1**	**9,4**
Quarter Average	**8,325**	**8,35**	**8,425**	**8,525**	**8,7**	**8,855**	**9,005**	**9,275**
Nickel LME 3m (USD/t)								
End Quarter	**17,3**	**17,2**	**16,9**	**16,6**	**16,5**	**16**	**15,825**	**16,1**
Quarter Average	**17,05**	**17,25**	**17,05**	**16,75**	**16,55**	**16,25**	**15,915**	**15,965**
EU TTF 1m (EUR/MWh)								
Quarter Average	**33**	**30**	**29**	**47**	**48**	**32**	**27**	**31**

Source: BNP Paribas Markets360

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