Quarterly Macro Report – 4th Quarter 2024

The global economy remains resilient, but recession risks in the US and ongoing stagnation in China and Europe dampen growth prospects. In response, Western central banks have begun cutting interest rates, accepting the risk that inflation may stay above target levels.

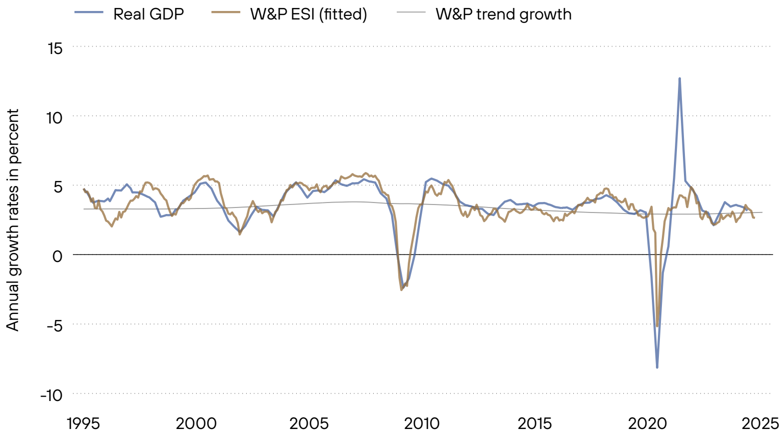
Despite restrictive monetary policies in many industrialized nations, the global economy remains stable, following its long-term growth trend. This stability is largely supported by strong growth in emerging markets such as India or Indonesia, as well as the ongoing resilience of the US economy. According to recent estimates from the Federal Reserve of Atlanta, the US economy is projected to have grown by 0.7% in the third quarter of this year.

Europe and China remain stagnant

However, this current robustness cannot entirely conceal the challenges in certain regions or the uncertainty surrounding future growth prospects. One area of concern is the sluggish performance of the European and Chinese economies, both of which are operating well below their capacity. The primary weakness in these regions stems from domestic demand, reflected in sluggish consumer spending and low levels of investment.

A quick recovery has become increasingly unlikely, raising concerns about whether the stabilization observed in the first half of the year can be sustained in the second half. In Europe, business sentiment has recently declined further, indicating a slowdown in activity in the coming months. Meanwhile, in China, residential construction starts have dropped 60% compared to 2019, and this downward momentum persists. Additionally, the real estate market has experienced further price drops, with new home prices in August 2024 down 5.3% compared to a year earlier. This ongoing pressure on Chinese households, whose primary form of savings is in real estate, is likely to delay any near-term recovery in domestic demand.

Fig. 1: Global economy stabilized by US and emerging markets



The global economy remains stable, maintaining its long-term growth trend. This is primarily driven by robust growth in emerging markets and the resilience of the US economy. However, certain regions, such as the Eurozone and China, show little to no growth momentum, clouding the broader outlook for the global economy.

Source: LSEG, Wellershoff & Partners

Substantial risk of a US recession

Another key concern for financial markets is the US economy, a major driver of global growth. Strong demand for imports has repeatedly provided support for other economies, even enabling above-trend growth in Switzerland during the second quarter. However, the US economy is showing signs of losing momentum. Economic indicators suggest a high probability of an impending recession. Capital market yields remain significantly below money market rates, and both domestic demand and business sentiment point to a contracting economy. Additionally, the labor market is showing early signs of weakness—a typical precursor to recessions. Unemployment in the US has increased from 3.7% to 4.2% this year, and job creation has slowed markedly.

> "The weak domestic economies in China and Europe leave them particularly vulnerable to a potential US recession, which could sever crucial impulses from foreign trade."

Loosening monetary policy

In response to these developments, Western central banks have begun loosening monetary policy. The Federal Reserve has taken a particularly aggressive stance, lowering interest rates by 50 basis points, with further cuts of up to 150 basis points anticipated by the end of next year. This shift underscores that supporting economic growth is becoming an increasingly central goal for many central banks.

However, the impact on inflation remains uncertain. While inflation rates have significantly decreased from their peaks in 2022, they remain high and continue to be far from central bank targets. Moreover, progress has slowed, and in some areas, it has stalled entirely, primarily due to persistent price increases in the labor-intensive services sector. For example, services inflation stands at 4.9% in the US, 4.1% in the Euro Area, and 5.6% in the UK. Given that wage growth continues to outpace inflation in most countries, this trend may persist for some time. In this context, central banks, which have already eased monetary policy significantly, are likely hoping that the weakening economic momentum will be sufficient to further lower inflation rates.

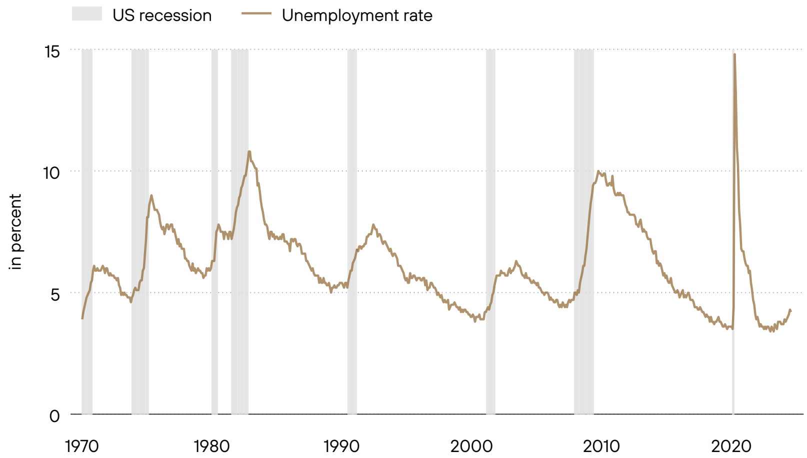
Table 1: Macroeconomic estimates (in %)

	GDP Growth			Inflation		Interest Rates	Money Growth M1
	Trend	2024*E*	2025*E*	2024*E*	2025*E*	Q4 2024	y/y 10/2024
USA	1.8	2.5	1.4	3.0	2.2	5.00	–0.8
Eurozone	1.1	0.6	1.2	2.7	2.4	3.50	–1.9
UK	1.7	0.6	1.5	2.8	2.4	5.00	–3.3
Switzerland	1.3	1.5	1.2	1.5	1.0	1.00	–6.3
Japan	1.1	0.5	1.0	2.5	1.5	0.25	2.2
China	4.5	4.3	4.5	0.6	1.5	4.35	-7.3
Brazil	1.4	1.8	1.8	4.0	3.2	10.75	10.7
India	5.0	6.3	5.5	4.5	4.2	6.50	7.4
Russia	1.0	2.0	1.0	6.2	4.5	19.00	3.2
World	3.0	2.8	3.1	4.4	3.6	–	–

Source: LSEG, Wellershoff & Partners

Fig. 2: Rising unemployment rate as a precursor to US recession

US recessions and unemployment rate

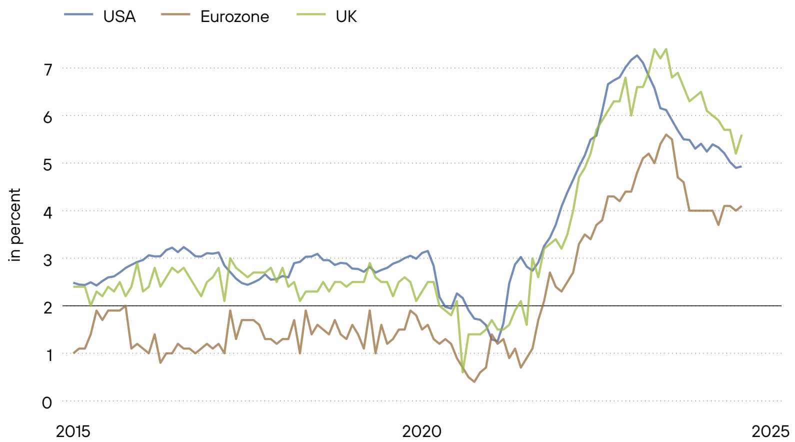


Source: U.S Bureau of Labor Statistics, Wellershoff & Partners

Since the beginning of the year, the unemployment rate in the US has increased from 3.7% to 4.2%, indicating a weakening labor market. Historically, significant rises in the unemployment rate have often coincided with recessions in the US, making this latest increase a cause for concern.

Fig. 3: Service prices as primary driver of inflation

Annual change of service price inflation

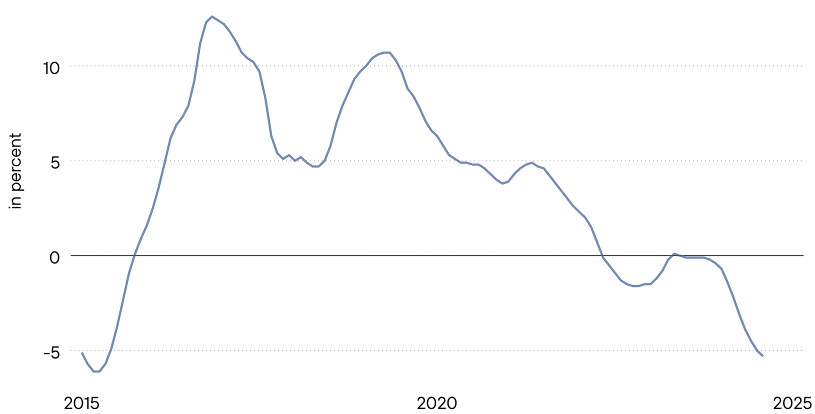


Source: LSEG, Wellershoff & Partners

Although inflation rates in most industrialized nations have decreased in recent months, they remain above central banks' targets, and the risks of a renewed increase are still elevated, particularly if monetary policy continues to ease. Notably, inflation in the services sector remains stubbornly high, recently registering at 4.9% in the US, 4.1% in the Eurozone, and 5.6% in the UK.

Fig. 4: China still suffering from real estate crisis

Annual change in newly build house prices in China



Source: LSEG, Wellershoff & Partners

The Chinese property market experienced another decline in prices over the past quarter, likely hindering economic recovery. For instance, in August, the prices of new houses were 5.3% lower than they were the previous year. This situation is particularly concerning, as Chinese households primarily invest their savings in real estate.

Capital Market

Amid monetary easing by major central banks, long-term interest rates declined over the past quarter. This can be attributed to market expectations of further rate cuts in the coming months and reflects growing concerns about slowing economic momentum, particularly in the US, where weaker economic data has heightened the risk of an impending recession.

In the last three months, interest rates on 10-year US Treasury bonds fell from 4.3% to approximately 3.8%, closely aligning with the Federal Reserve's (Fed) policy rate cut of 50 basis points, bringing it to 5% in mid-September. In contrast, long-term rates in the UK dropped by only 15 basis points despite a 0.25 percentage point cut by the Bank of England (BoE). Meanwhile, in the Euro Area, 10-year government bond yields declined by around 25 basis points over the same period, despite the European Central Bank (ECB) cutting rates by 50 basis points this year.

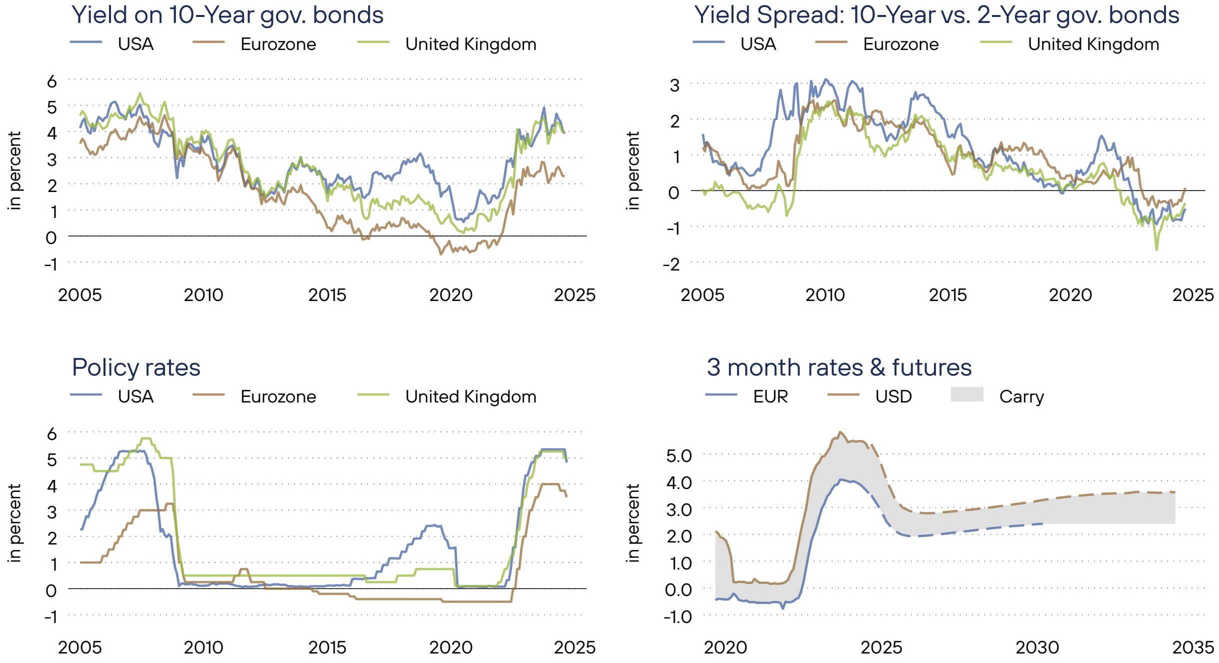
> "The uneven decline in long-term interest rates highlights the differing expectations regarding further rate cuts."

Differing expectations regarding rate cuts

The uneven decline in long-term interest rates highlights the differing expectations in capital markets regarding further rate cuts. In the U.S., the Fed has signaled the possibility of another rate cut by year-end, as weakening economic data and significantly lower inflation have raised fears of recession, further fueling market expectations of more aggressive monetary easing. Conversely, in the UK, a recent uptick in inflation is likely to delay further rate cuts by the BoE. In the Euro Area, where the economy continues to show limited growth, but core inflation remains sticky, market uncertainty surrounds the ECB's future actions.

In summary, yield curves remain inverted, indicating that long-term investments continue to offer lower returns than short-term ones, reinforcing a weak economic outlook. However, signals from the capital markets are mixed. Notably, yield premiums on corporate bonds, which typically reflect market risk sentiment, have shown no signs of recessionary concerns, remaining virtually unchanged throughout the quarter.

Fig. 5: Money market and capital market interest rates



Source: LSEG, Wellershoff & Partners

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Published by: Wellershoff & Partners Ltd., Zürich
Conception: Wellershoff & Partners Ltd., Zürich
Editorial Deadline: September 26, 2024