January 2024

2024 Global Economic Outlook

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OVERVIEW

In 2023, the global economy showed surprising resilience in the face of significant policy restriction. The US Federal Reserve (Fed) firmed monetary policy at its most rapid pace in decades, raising the federal funds rate by 5¼ percentage points and reducing its balance sheet by more than $1 trillion since March 2022. Despite this, the US economy expanded steadily, as robust consumer activity fueled above-trend growth and the labor market remained tight.

In 2024, growth momentum is expected to taper off as monetary policy restraint gains more pronounced traction. The Fed's mission remains incomplete, as inflation persists above the 2% target and is not anticipated to return to that level until 2026, according to its December Summary of Economic Projections.

Global Backdrop

The progress in lowering inflation in 2023 owed importantly to the adjustment of commodities and goods prices, which pulled consumer price inflation toward 3% from 6% at the start of the year. However, reaching the 2% mark depends on addressing sticky and inertial services prices. This "last mile" of reducing inflation will probably be more challenging than officials expect, prolonging the disinflation process and requiring the Fed to maintain tighter policies to manage aggregate demand. We think market participants could face serial disappointment given the premature expectation of a Fed pivot toward easing in the early part of 2024. In the wake of December's Federal Open Market Committee (FOMC) meeting, we put more weight on the scenario that developed-market central banks could declare victory too early—easing policies before they are certain they reached inflation targets. In a less likely scenario, the Fed may be on track to achieve its "soft landing," returning inflation to 2% without a noticeable slowdown in growth.

Politics will likely be at the top of investors' minds in 2024. The upcoming US presidential election in November and various national elections worldwide, including key ones in Taiwan, India, Mexico, Indonesia, the United Kingdom and Europe, matter for the global macroeconomy.

Outside the United States, we believe the economies of other developed markets are in for slow growth or outright decline. The euro area faces a potential mild recession. The European Central Bank's policy tightening, coupled with weakness in global goods demand, particularly affecting Germany, is contributing to this economic softening. Although most central banks have signaled an end to tightening, the Bank of Japan will likely be swimming against the tide, raising its policy rate and exiting its negative-rate regime early in the year.

In our view, global growth will increasingly depend on emerging markets (EM) like India and China. The former's economy is experiencing a boom that has momentum. The latter will be more reliant on policy to drive expansion amid ongoing private-sector weakness and a difficult demographics transition. The global economic landscape is becoming riskier due to geopolitical tensions, which add to uncertainty and volatility.

As the world economy stands at a crossroads, key questions for the year ahead include whether a soft landing will allow the Fed to pivot early or if a prolonged "last mile" of inflation will keep policies tighter for an extended period, potentially leading to a harsher downturn. The consequences of global elections, particularly in the United States, and the impact of geopolitical crosswinds are crucial factors to monitor in 2024. Here are four themes shaping the outlook:

1. Economic growth is expected to slow as the effects of monetary policy take hold, coupled with the depletion of savings buffers.

2. The challenging "last mile" in reducing inflation may prolong tighter Fed policies and limit the scope for easing.

3. High real yields and escalating debt burdens constrain governments seeking to stimulate their economies.

4. Consequential elections and a tense geopolitical atmosphere add to turbulence.

United States

In our outlook, the US economy retains growth momentum in the first part of 2024 and then slows as the effects of monetary policy take hold, coupled with the depletion of savings. At December's FOMC meeting, Fed Chair Powell signaled that the firming cycle is over. Calling a peak to the policy-rate cycle gives markets a one-way bet given that the next move is down. Why the pivot? The Fed apparently believes aggregate supply will continue to fill in to meet strong demand and, accordingly, are unworried about the "last mile" in reducing inflation to goal. If this turns out to be the case, we feel it will be a historical outlier that is at odds with the typical sluggish adjustment of the prices of many services and the need for the market to correct many relative price distortions feeding public angst about the economy.

If it turns out the "last mile" of inflation is hard, as we believe, then either market participants will be serially disappointed as the Fed doesn't get the opportunity to lower the nominal rate because inflation doesn't fall as much as hoped or inflation stalls out north of its goal because the Fed lowers the nominal rate anyway. Our forecast is for the former—that disappointment is in store as the initial rate cut is put off until September given the stubbornness of inflation. If inflation and price pressures continue to fall faster than expected, an easing cycle may begin in the Spring, sooner than our base case.

Monetary policy acts with a lag and the cumulative force of one-and-a-half years of Fed firming will restrain activity in 2024. However, we think this is less likely to take as dramatic a turn as in March 2023, when regional bank balance sheets were under stress and the failure of Silicon Valley Bank led to a sharp decline in bank stocks. The regulatory interventions this prompted, including the creation of the Bank Term Funding Program (BTFP) and expanded deposit guarantees, should limit contagion going forward. Spending and jobs growth in housing-tied sectors is slowing. Commercial real estate faces the cyclical headwind of high interest rates and the secular one of reduced demand for office space in light of the shift toward work from home. These risks will be important to monitor in a tighter-for-longer scenario. A highly anticipated US election in November will likely add to turbulence as the year progresses.

Fiscal Discipline in US Could Continue to Deteriorate

There are 471 seats up for election in November 2024 (president, vice president, 34 senators and 435 representatives). The two major parties have drifted significantly apart in their philosophies, and who controls the executive and legislative branches will matter for a wide range of economic, social and domestic policies, as well as the direction of the judiciary over time. The next president will probably begin their term with a poorly performing economy—the "long and variable" lags of monetary policy restraint are likely to have firm traction by 2025 to the chagrin of the occupant of the White House. Any ambition for fiscal expansion will be tempered by the tepid reception of investors to additional debt given the already large stock of government debt outstanding. Neither political party is likely to achieve a decisive majority on Capitol Hill and each is riven by factions. We foresee that the legislative process will continue to lurch from deadline to deadline with threats of shutdowns and debt-ceiling standoffs. Partisan differences will not go away and likely express themselves in legislative dysfunction, both the failure to address longer-term problems and an inability to run the government smoothly from day to day. Investors will likely be reminded by ratings agencies that the path of US government debt is unsustainable and that no effective process governs it. While the US dollar is quite unlikely to be dislodged as the safe-haven currency, the pedestal it rests upon will likely continue to erode.

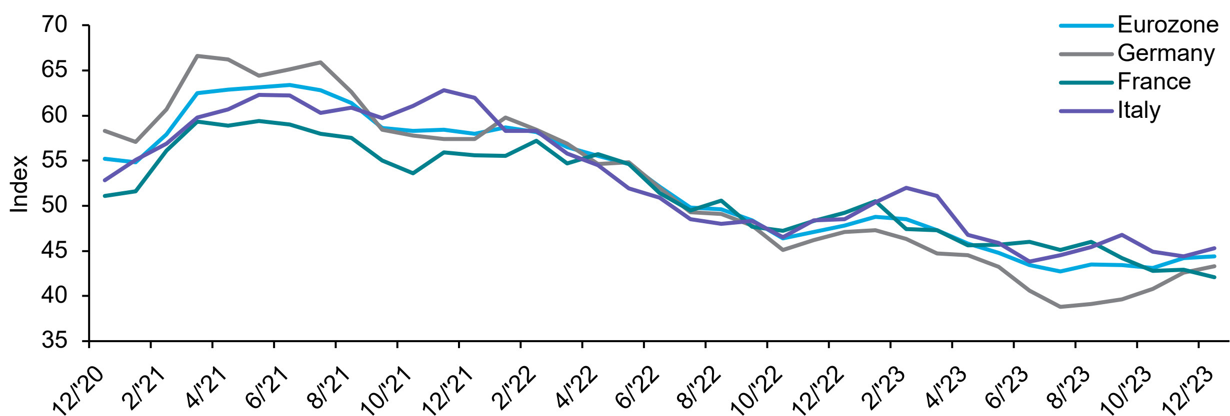
Euro Area

The euro area economy struggled in 2023, as monetary policy firming lowered aggregate demand by restraining credit growth and investment. In addition, softness in global goods markets weighed on Northern Europe's manufacturing base. The war in Ukraine further complicates matters, in part by disrupting energy markets. This economic stagnation will likely carry through 2024, with the potential of a mild recession.

Signs show inflation continues to normalize and national consumer price indexes depict an ongoing disinflation process in Europe. The European Central Bank has reached its terminal rate after 450 basis points of cumulative tightening since July 2022. We think the next policy move will be a rate cut sometime in the middle of 2024 as growth remains weak and inflation continues its trend lower.

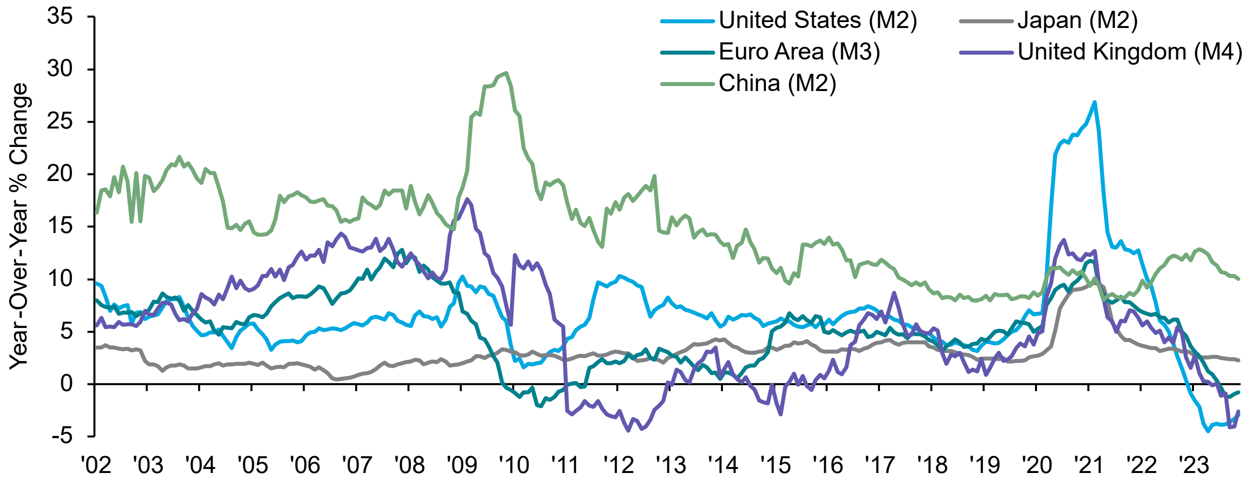
Euro Area: Manufacturing PMIs

>50 indicates expansion; <50 indicates contraction



Source: Bloomberg as of January 4, 2024. Note: A Purchasing Managers' Index (PMI) is an economic indicator comprised of monthly reports and surveys from private sector manufacturing firms. It consists of a diffusion index that summarizes whether market conditions are expanding, staying the same, or contracting as viewed by purchasing managers.

Major Economies - Broad Money Growth

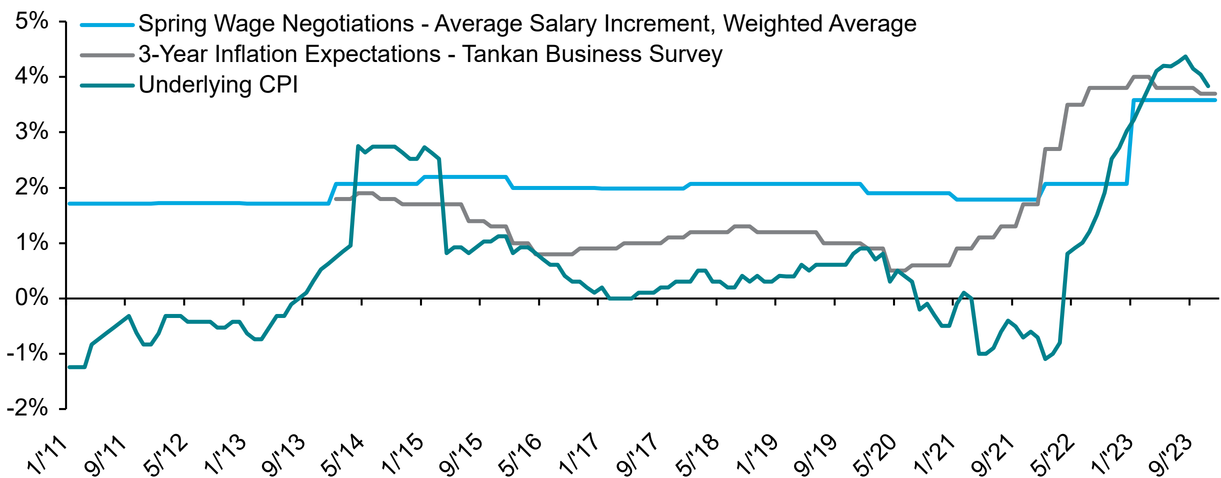


Source: US Federal Reserve, Bank of Japan, European Central Bank, Bank of England, People's Bank of China as of January 4, 2024.

Japan

Japan—a beneficiary of rising global prices—has experienced a sustained upswing in underlying inflation after decades of fighting deflation. Underlying inflation above 2% has momentum and signs point to positive wage growth in the Spring "shunto"—the annual wage negotiations between enterprise unions and the employers in Japan. Japanese firms appear more comfortable passing on higher costs to prices, creating potential for a virtuous cycle of domestic inflation. Supported by evidence that underlying inflation can run sustainably at 2%, we think the Bank of Japan will begin lifting its policy rate from negative territory in early 2024, kicking off a gradual tightening cycle. This removes an anchor for global yields.

Inflation Pressures Are Rising In Japan



Source: Bank of Japan, Japanese Trade Union Confederation (RENGO), and Japanese Statistics Bureau as of January 5, 2024.

PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS.

China

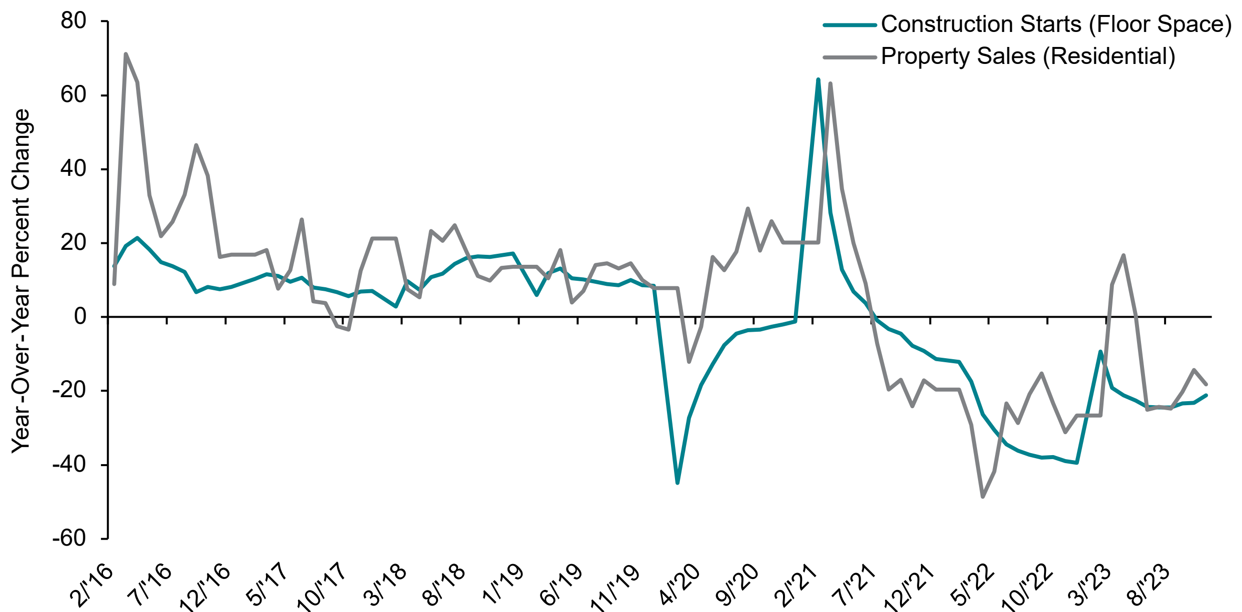
China's economy, once a robust growth engine for the world, has experienced a notable shift lower in recent years. The ongoing real estate crisis, which originated in 2021, weighed heavily on the domestic economy in 2023. Economic indicators hit a low point around the middle of 2023 but stabilized as policymakers implemented stimulus measures.

Looking ahead to 2024, the growth trajectory depends on the thrust of Beijing's fiscal policy. The private sector lacks a clear catalyst, with lingering effects from the zero-COVID policy restraining consumer activity and youth unemployment remaining high. While monetary policy has already been relaxed considerably, more onus now falls on fiscal spending to stabilize growth.

Beijing has taken a measured and incremental approach to fiscal stimulus. The expectation is for Beijing to maintain a 5% real growth target for 2024 to bolster confidence. A consistent infusion of fiscal expansion, coupled with ongoing monetary accommodation, is poised to stabilize growth. However, it is important to temper expectations, as China is unlikely to replicate the unstoppable industrial growth seen in the last decade. Various headwinds, including constraints in the property, export and technology sectors, have taken precedence in shaping the economic outlook.

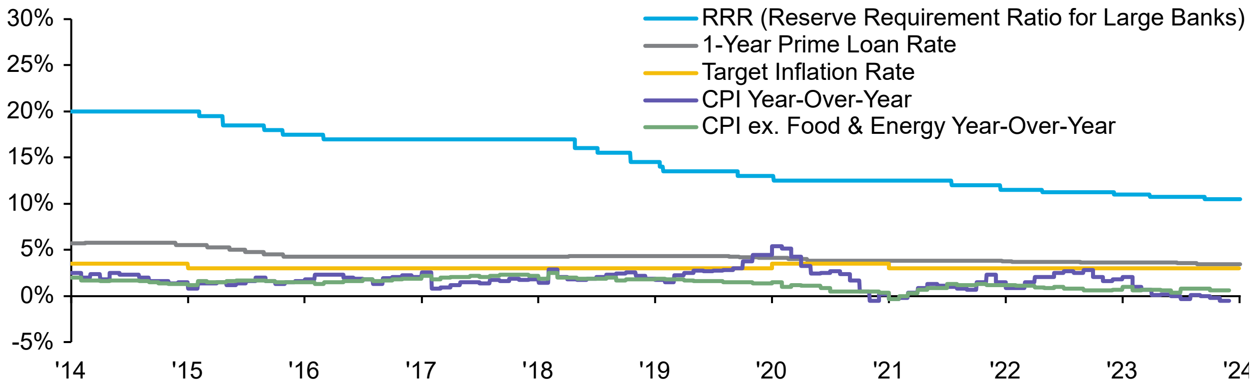
Chinese inflation remains benign, with a 12-month inflation rate contracting by -0.5% in November. Core inflation saw a modest rise of 0.6%, enabling the People's Bank of China to ease policy rates in 2023. Expectations point to further monetary easing in 2024, although the People's Bank of China faces a delicate balancing act between rate cuts and safeguarding banks' net interest margins, stabilizing the currency and curbing capital outflows. With the conventional policy space narrowing after years of cuts, the People's Bank of China confronts increasing limitations.

China - Property Market



Source: Bloomberg as of January 4, 2024.

China - Policy Rates and Inflation



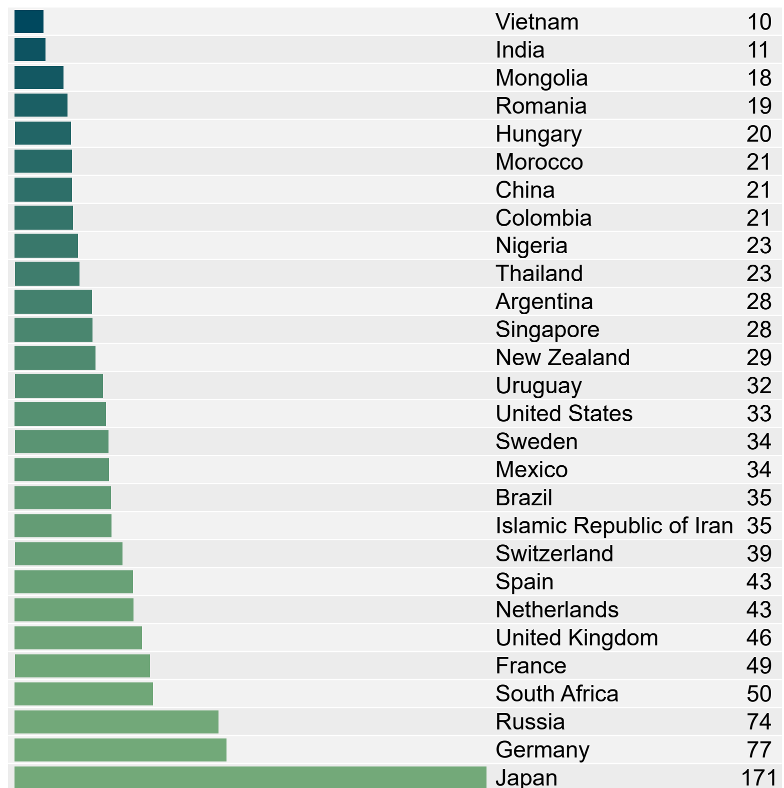
Source: Bloomberg as of January 4, 2024.

India

India's booming economy expanded at a brisk pace of 6.6% in 2023 and that momentum will likely carry into this year, moderating only slightly. The government's strong push for public investment and a pick-up in private capital expenditure support productivity. The International Monetary Fund's longer-term trend forecasts for the Indian economy suggest it will double in terms of real gross domestic product by the end of this decade, becoming the third largest economy by size after the United States and China. Inflation remains moderate, with food price pressures easing and core inflation under control around 4.5%. Inflation could moderate further, allowing the central bank to ease later in the year. There is an important election in the Spring, with Prime Minister Modi seeking another term.

Years to Double GDP

Estimate



Source: IMF as of January 5, 2024. Note on calculation: Years to double real GDP is determined by the Rule of 70. This determines the number of years it takes for a variable to double by dividing the number 70 by the growth rate. For the growth rate, we use the IMF's long-term annual real GDP projection.

Emerging Markets

EM central bank easing should broaden in 2024. Several major Latin American central banks, such as Brazil and Chile, have already begun easing rates after containing inflation with aggressive and early tightening. Central and Eastern European economies should lower rates in 2024 as well, with the added complication of the nearby War in Ukraine.

In Asia, the inflation cycles have been different. With fewer domestic inflation pressures, central banks throughout Asia have not needed to tighten as much. EM Asian central banks will remain on hold a little longer than the rest of EM and lower rates more slowly.

Turkey and Argentina are more idiosyncratic, with forceful policy responses being implemented in both economies to grapple with hyperinflation. This year will be an important phase, with inflation needing to decline quickly.

Vincent Reinhart
Chief Economist & Macro Strategist

Vincent is the firm's Chief Economist and Macro Strategist. In this role, he is responsible for developing views on the global economy and making relative value recommendations across global bond markets, currencies and sectors.

Previously, Vincent served as the Chief US Economist and a managing director at Morgan Stanley. For the prior four years, he was a resident scholar at the American Enterprise Institute (AEI). Vincent also spent 24 years at the Federal Reserve, holding several roles including Director of the Division of Monetary Affairs and Secretary and Economist of the Federal Open Market Committee (FOMC). His responsibilities at the Federal Reserve included directing research and analysis of monetary policy strategies and the conduct of policy through open market operations, discount window lending and reserve requirements. Prior to these roles, he was the principal liaison with the domestic desk at the Federal Reserve Bank of New York and was responsible for preparing a document outlining policy alternatives for each FOMC meeting. He was Deputy Director in the Division of International Finance and Associate Economist of the FOMC and spent five years at the Federal Reserve Bank of New York in both the domestic and international research departments.

His academic publications primarily concern the conduct of policy and issues related to the monetary transmission mechanism as well as an analysis of alternative auction techniques and Treasury debt management. After an undergraduate training at Fordham University, he received graduate degrees in economics at Columbia University.

Nicholas Tocchio
VP, Global Economist

Nick is a global economist who helps develop the firm’s views on global macroeconomics. Previously, Nick contributed to global fixed income investment strategy at Standish Mellon Asset Management, a BNY Mellon company.

Nick holds a BA in Economics from Hamilton College and has been in the investment industry since 2013.

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