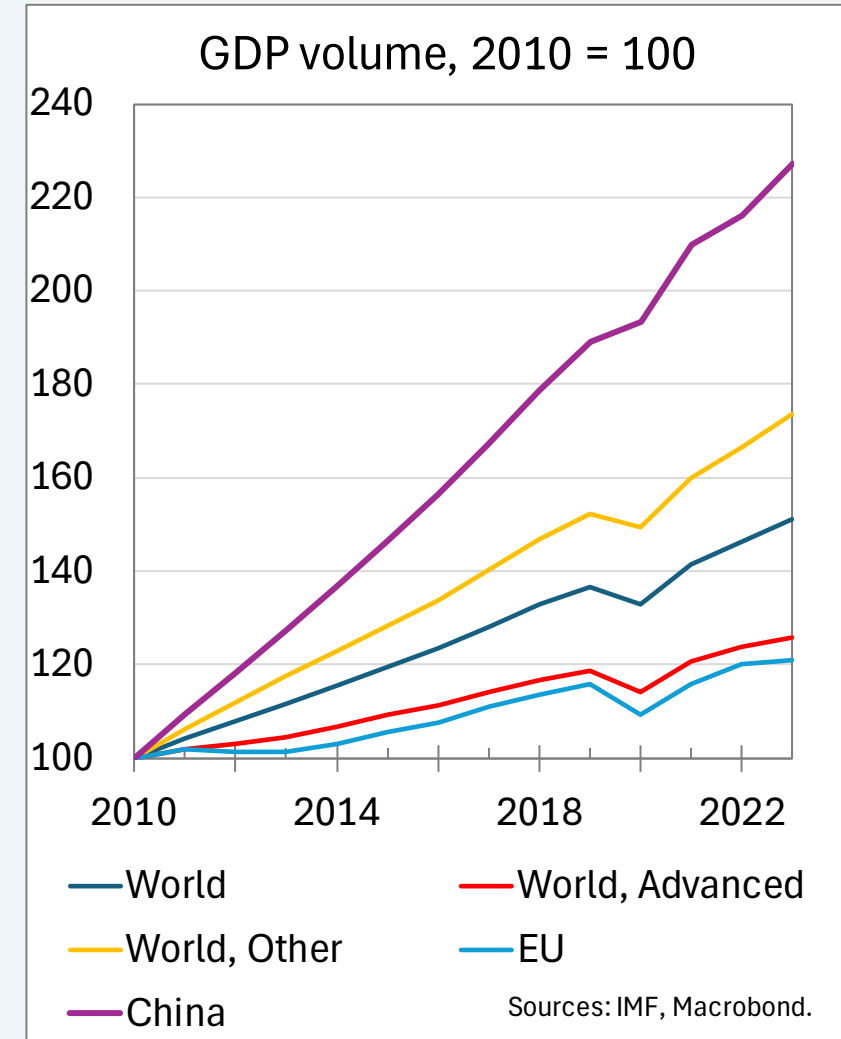# Global Economic Environment

AIECE meeting

Cologne

16.5.2024

Ville Kaitila

ETLA (Finland)

Mostly recovered from the shocks

- Global economy has witnessed many shocks during the past years.
  - Pandemic
  - Russia's invasion of Ukraine
  - GVC problems and very volatile commodity price developments
  - Inflation ➜ higher interest rates
  - Increased indebtedness ⎫
  - Geopolitical and geoeconomic tensions ⎭ We'll get back to these

- The economic shock has partly/mostly subsided but continues to drag on the world economy.

- Especially the broader geopolitical and geoeconomic tensions are likely to grow in the near future.

- In terms of growth, the EU was left behind in 2023.

GDP volume, 2010 = 100

—World   —World, Advanced
—World, Other   —EU
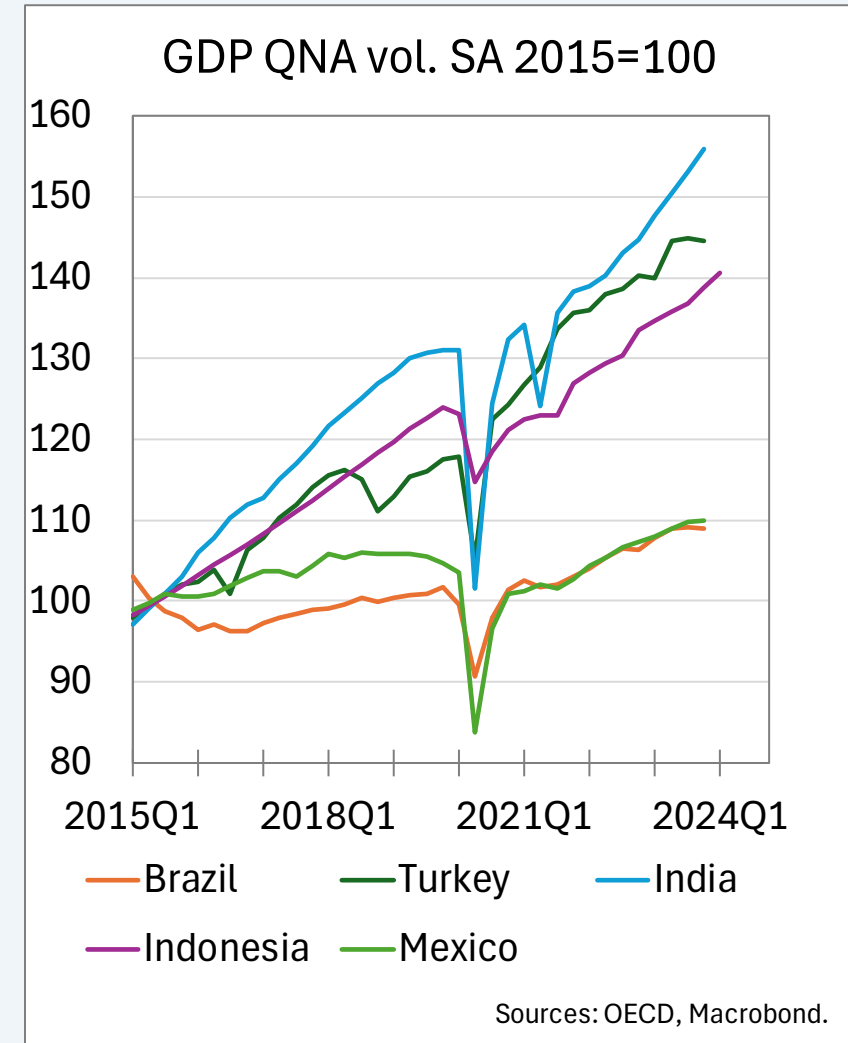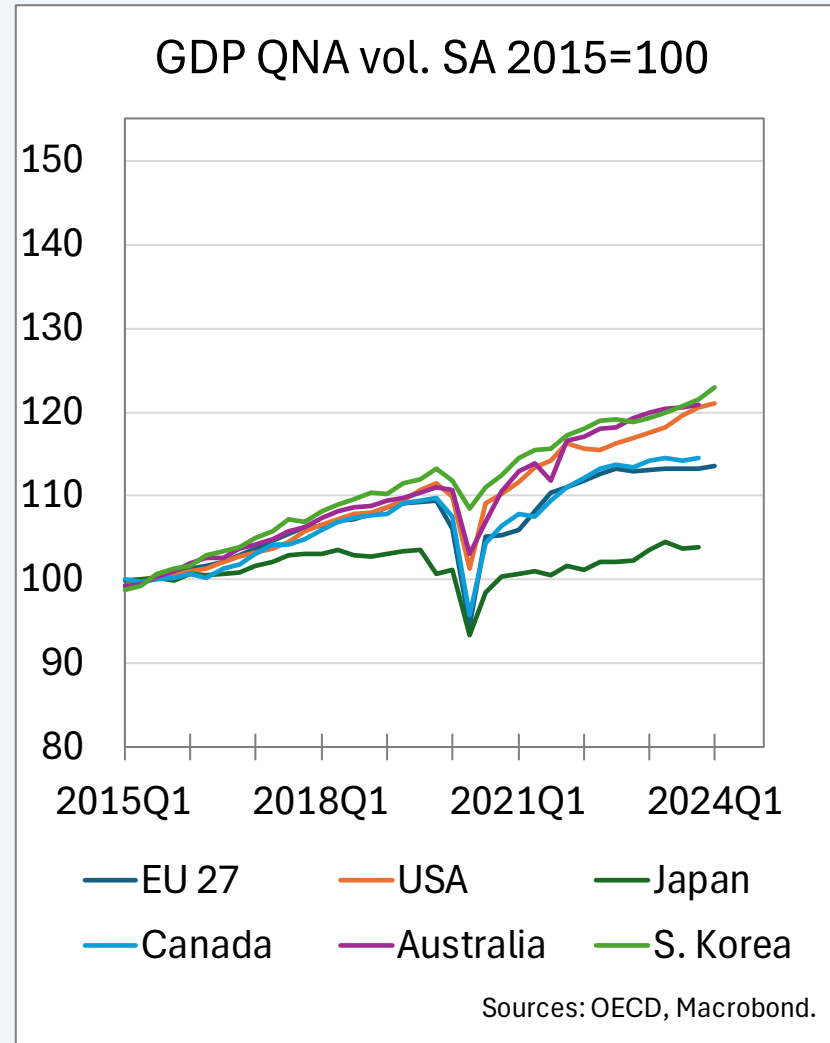—China   Sources: IMF, Macrobond.

- So far, stricter monetary policy has not led to hard landing(s).
- However, inflation is not yet done with. Also, the impact of higher interest rates may not yet have fully materialised.
- The timing of changes in monetary policy is important.
- Diminishing fiscal support while monetary policy is not yet loosened?
- Weak productivity development.
- Presidential elections in the US.

GDP volume change, %

Sources: IMF, Macrobond.

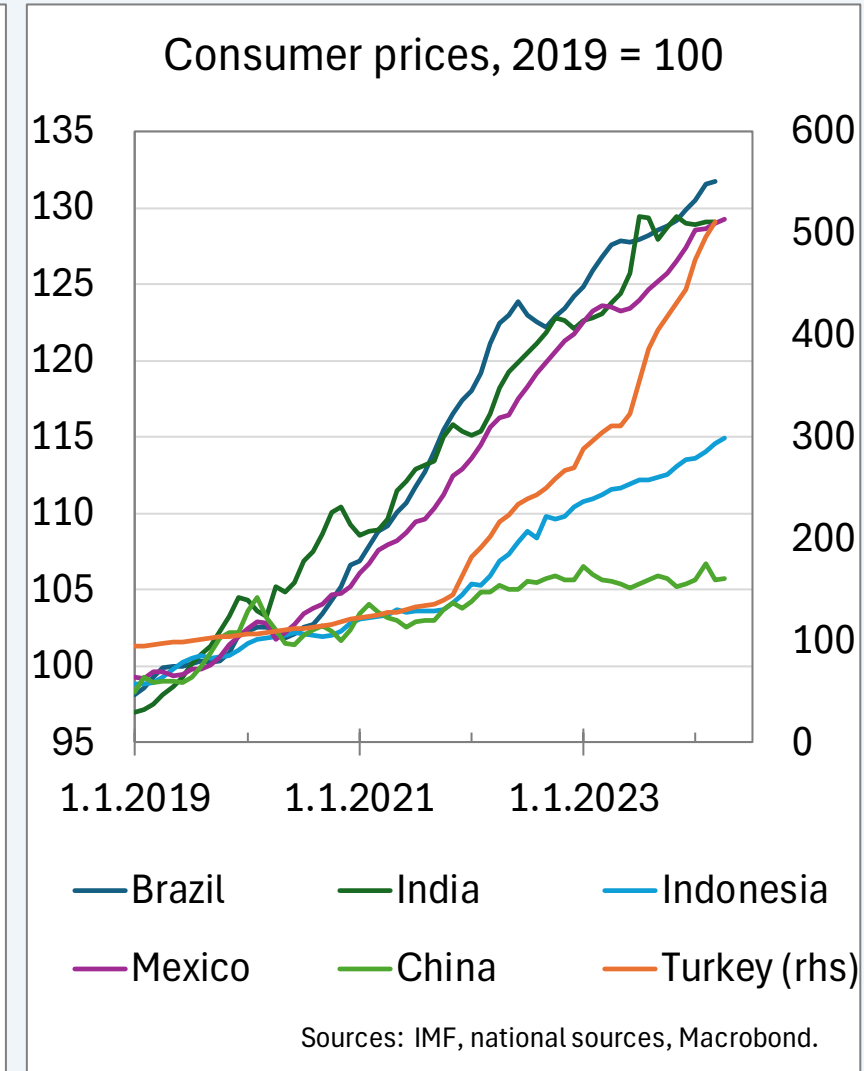World — World, Advanced — World, Other — EU — China
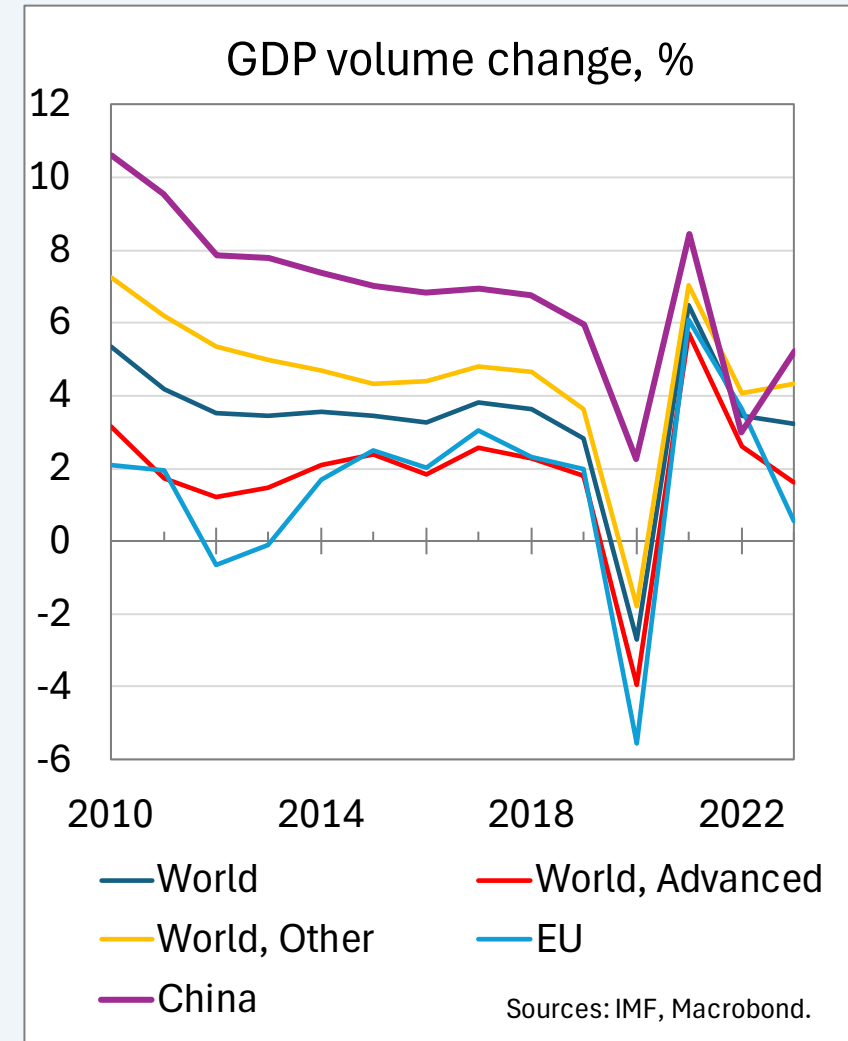
Quarterly GDP developments

- Quarterly GDP development has more or less recovered from the recent shocks.

- The EU is stagnant, dragged down by northern Europe, manufacturing, the war, and fallout from higher energy prices.

GDP QNA vol. SA 2015=100

Sources: OECD, Macrobond.

Legend: EU 27 — USA — Japan — Canada — Australia — S. Korea

GDP QNA vol. SA 2015=100

Sources: OECD, Macrobond.

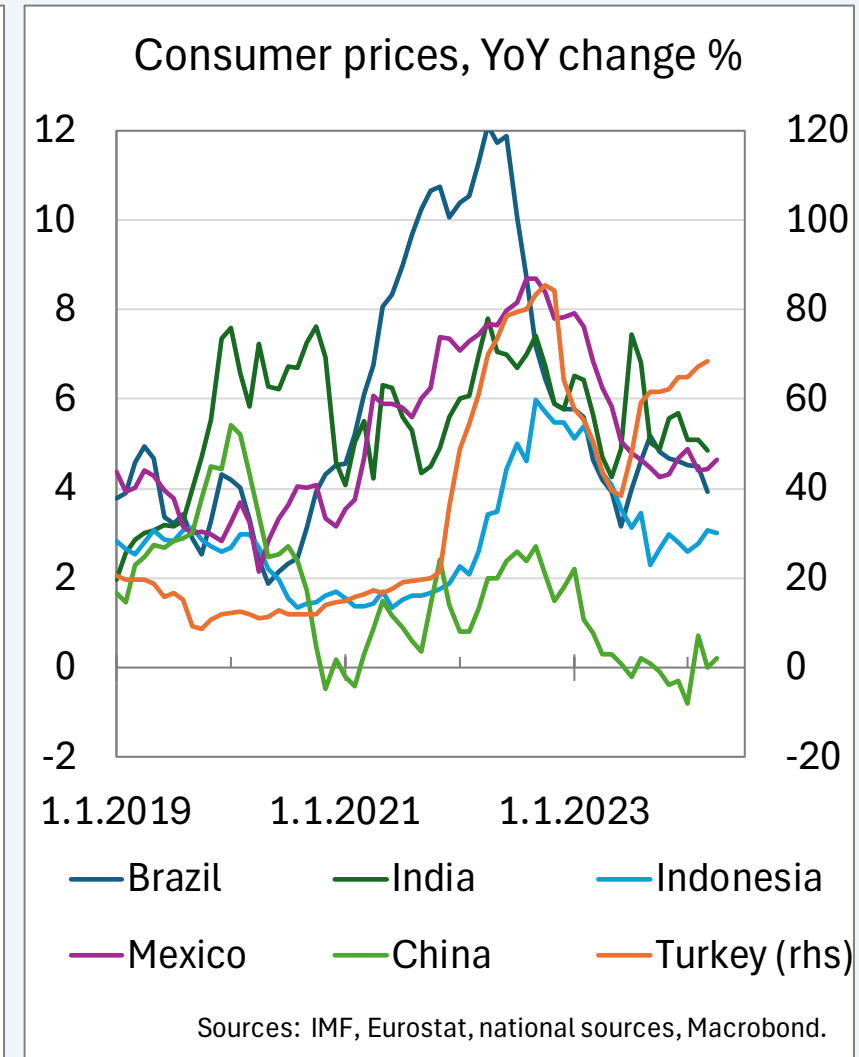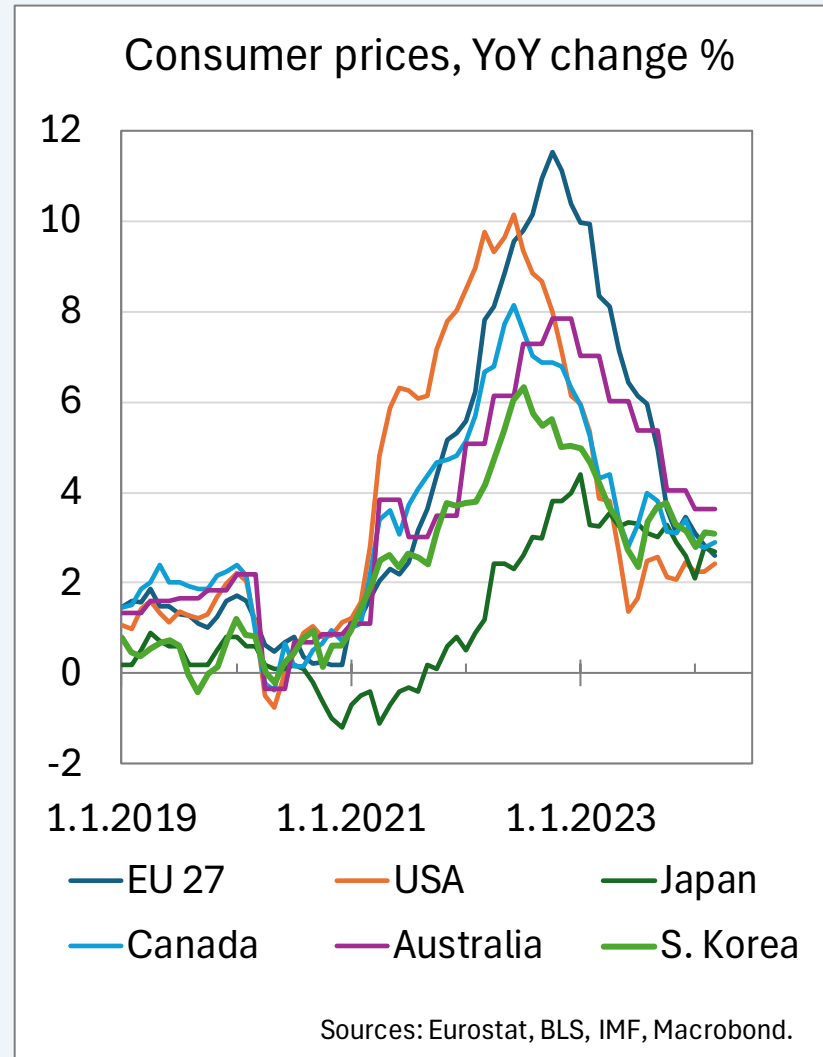Legend: Brazil — Turkey — India — Indonesia — Mexico

Consumer prices have risen to new levels

- Lower commodity prices, higher interest rates, less labour market pressures in many countries.

- Mostly, no wage-price spirals at least in developed economies.

- Japan and China more moderate development.

- Turkey (note rhs) is in a league of its own among these countries.

- Note: The indices may be defined somewhat differently in the countries.

Consumer prices, 2019 = 100

EU 27 · USA · Japan · Canada · Australia · S. Korea

Sources: Eurostat, BLS, IMF, Macrobond.

Consumer prices, 2019 = 100

Brazil · India · Indonesia · Mexico · China · Turkey (rhs)

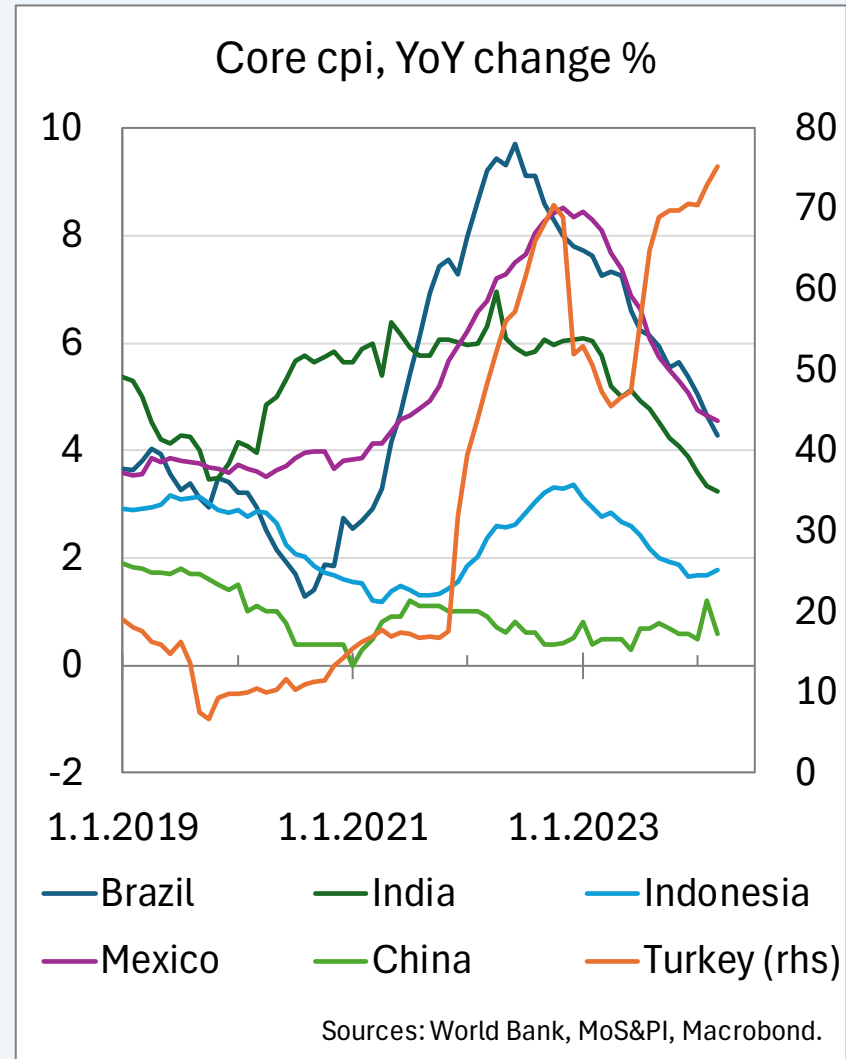Sources: IMF, national sources, Macrobond.
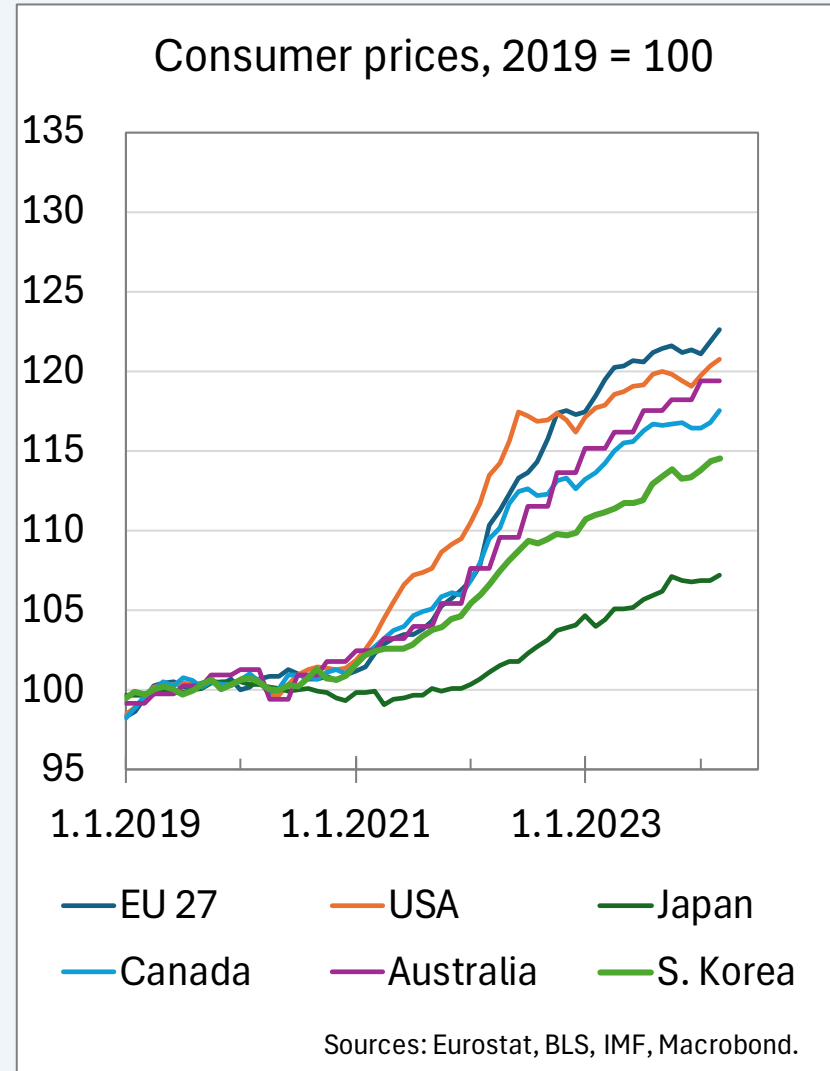
Inflation has moderated in many countries

- Inflation has crept up again in the US: earlier fiscal stimulus, strong private consumption, tight labour market.

- According to the IMF, the gap between actual and potential output levels in 2023 was +0.7% in the US, and -0.3% in the EA.

- China is back to zero inflation.

Consumer prices, YoY change %

EU 27 — USA — Japan — Canada — Australia — S. Korea

Sources: Eurostat, BLS, IMF, Macrobond.

Consumer prices, YoY change %

Brazil — India — Indonesia — Mexico — China — Turkey (rhs)

Sources: IMF, Eurostat, national sources, Macrobond.

Core inflation rates are expected to continue to decline

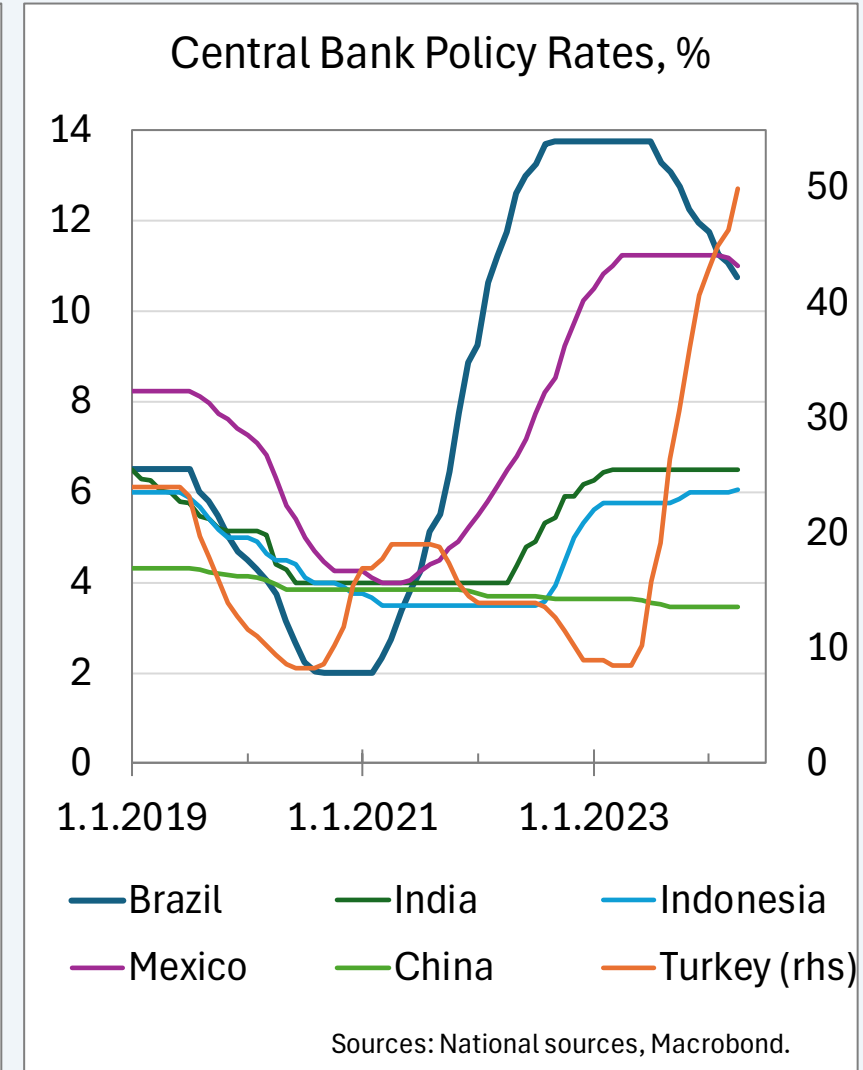Core cpi, YoY change %

Euro Area — USA — Japan — Canada — Australia — S. Korea

Sources: Eurostat, World Bank, Australian Bureau of Statistics, Macrobond.

Core cpi, YoY change %

Brazil — India — Indonesia — Mexico — China — Turkey (rhs)

Sources: World Bank, MoS&PI, Macrobond.
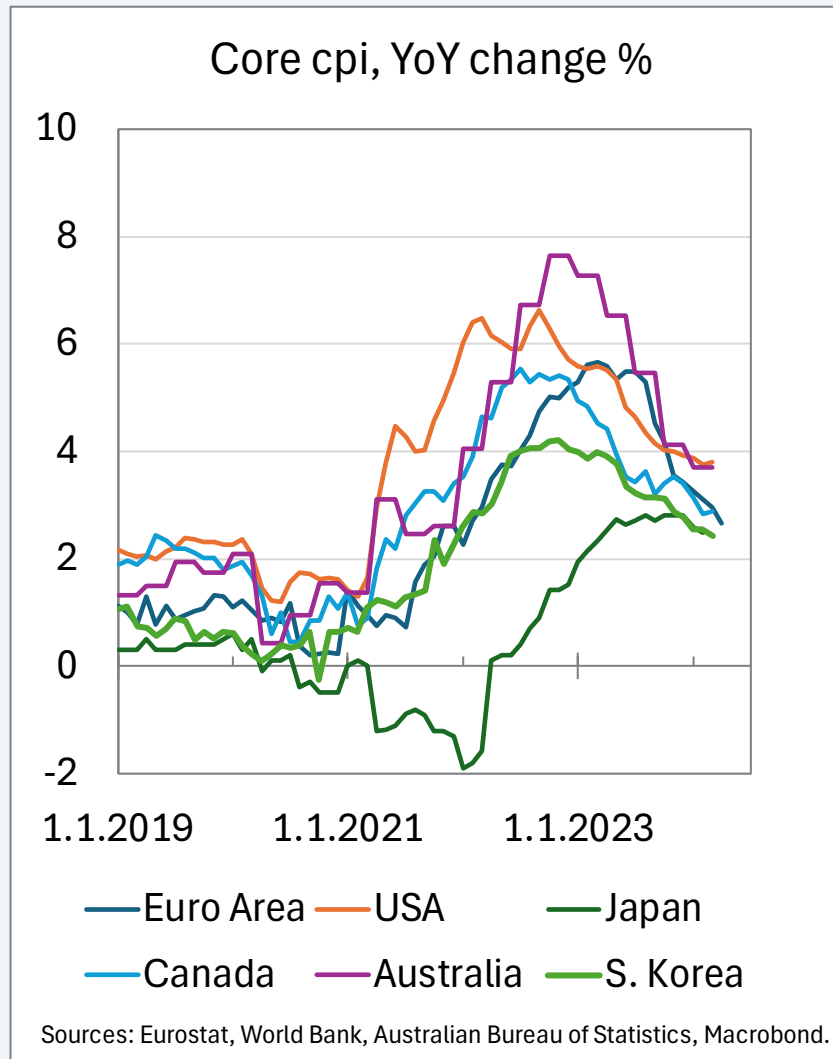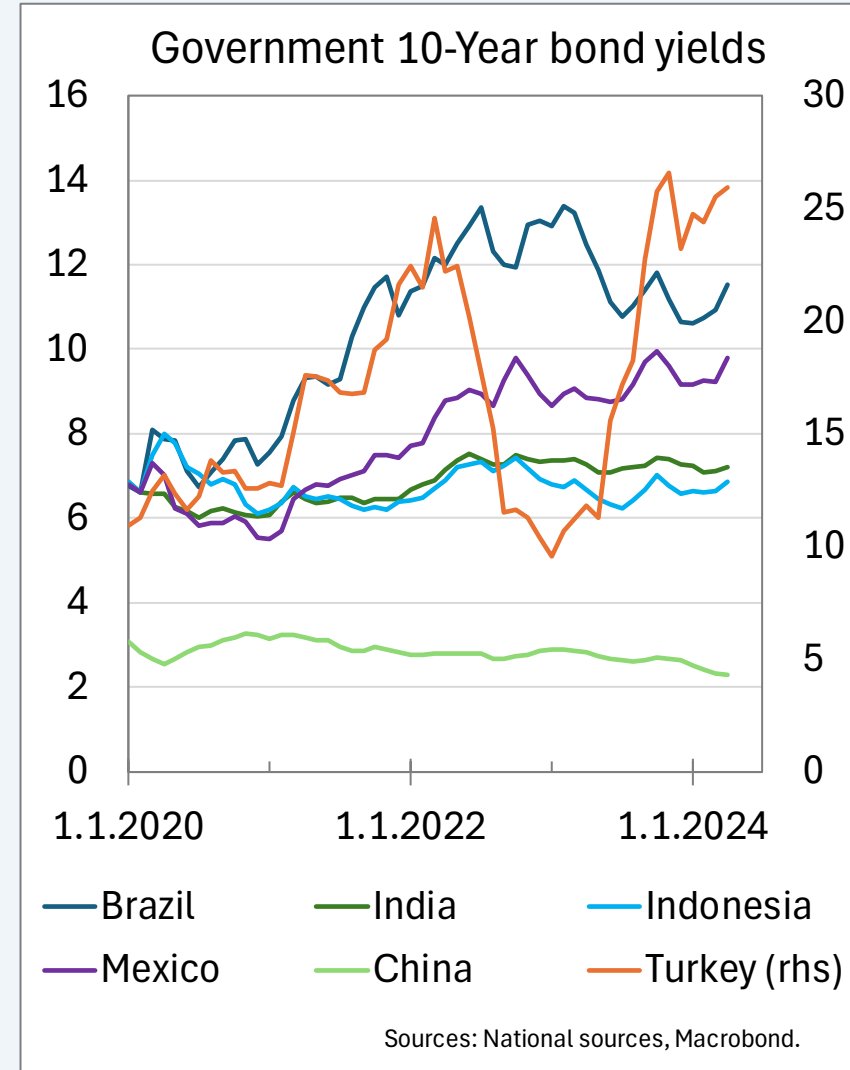
… and we are mostly waiting for interest rates to start a descent

- Nominal interest rates are relatively high, given expected inflation, and monetary policy is restrictive.

- Japan remains an exception.

- Households have been using their cumulated savings.

- Real interest rates have been rising.

- Tighter fiscal policy expected after expansion.

- Note: The policy rates shown in the graphs may be a bit different.

Central Bank Policy Rates, %

Euro Area — USA — Japan
Canada — Australia — S. Korea

Sources: National sources, Macrobond.

Central Bank Policy Rates, %

Brazil — India — Indonesia
Mexico — China — Turkey (rhs)

Sources: National sources, Macrobond.
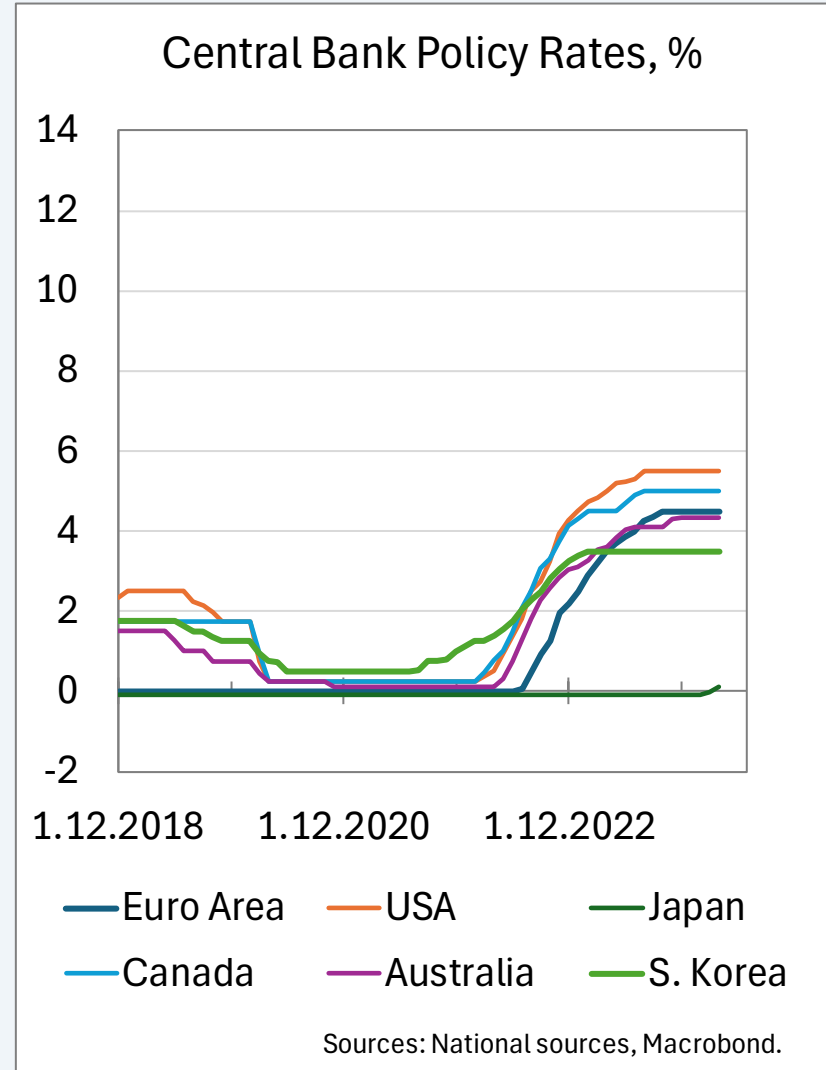
On the other hand, bond yields have risen again

Government 10-Year bond yields

Germany — USA — Japan — Canada — Australia — S. Korea

Sources: National sources, Macrobond.

Government 10-Year bond yields

Brazil — India — Indonesia — Mexico — China — Turkey (rhs)

Sources: National sources, Macrobond.
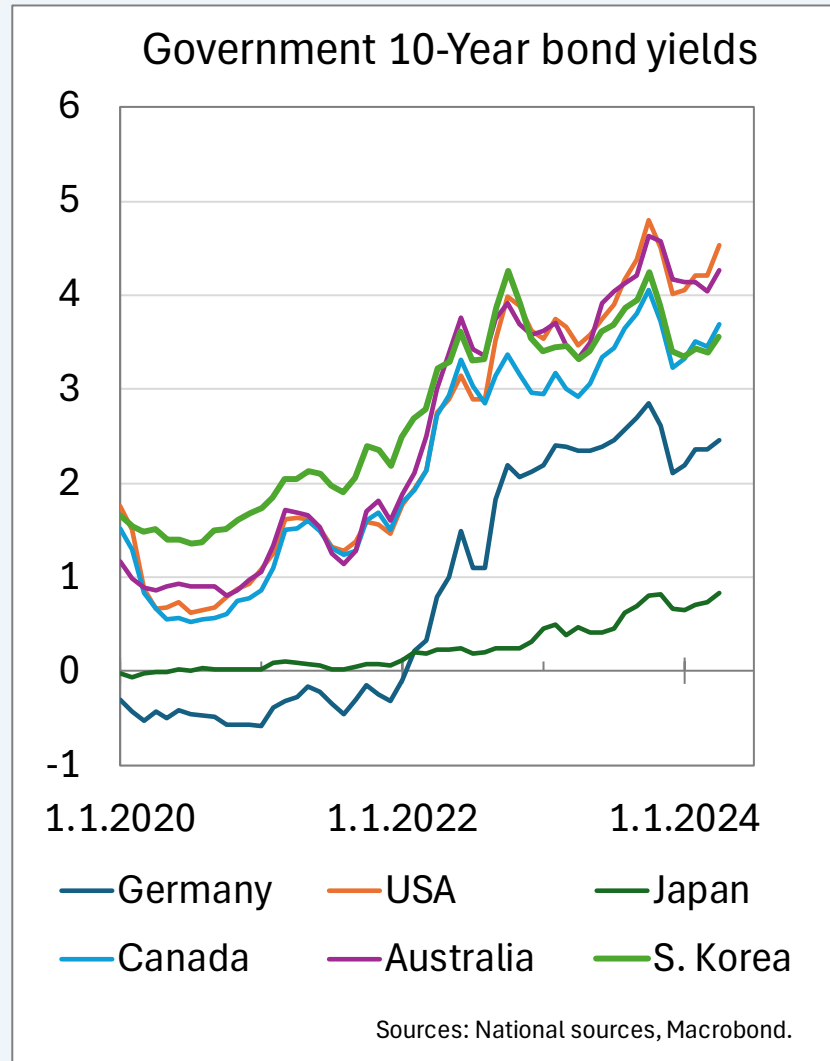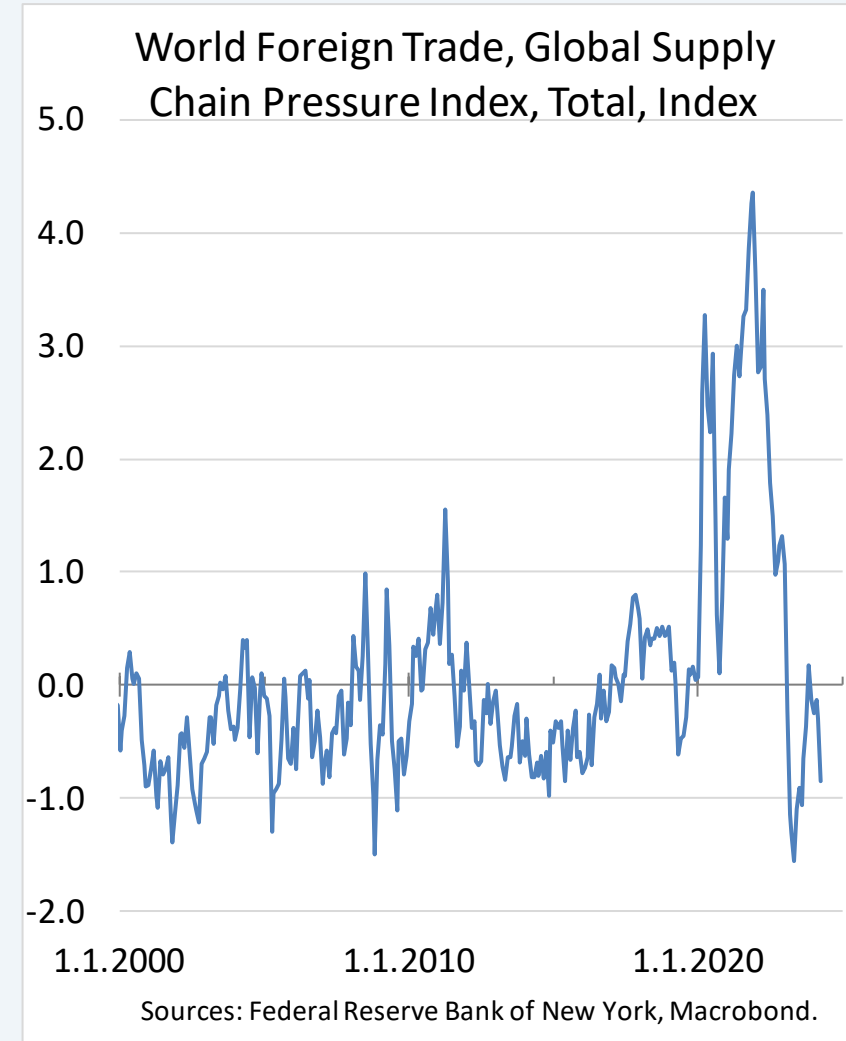
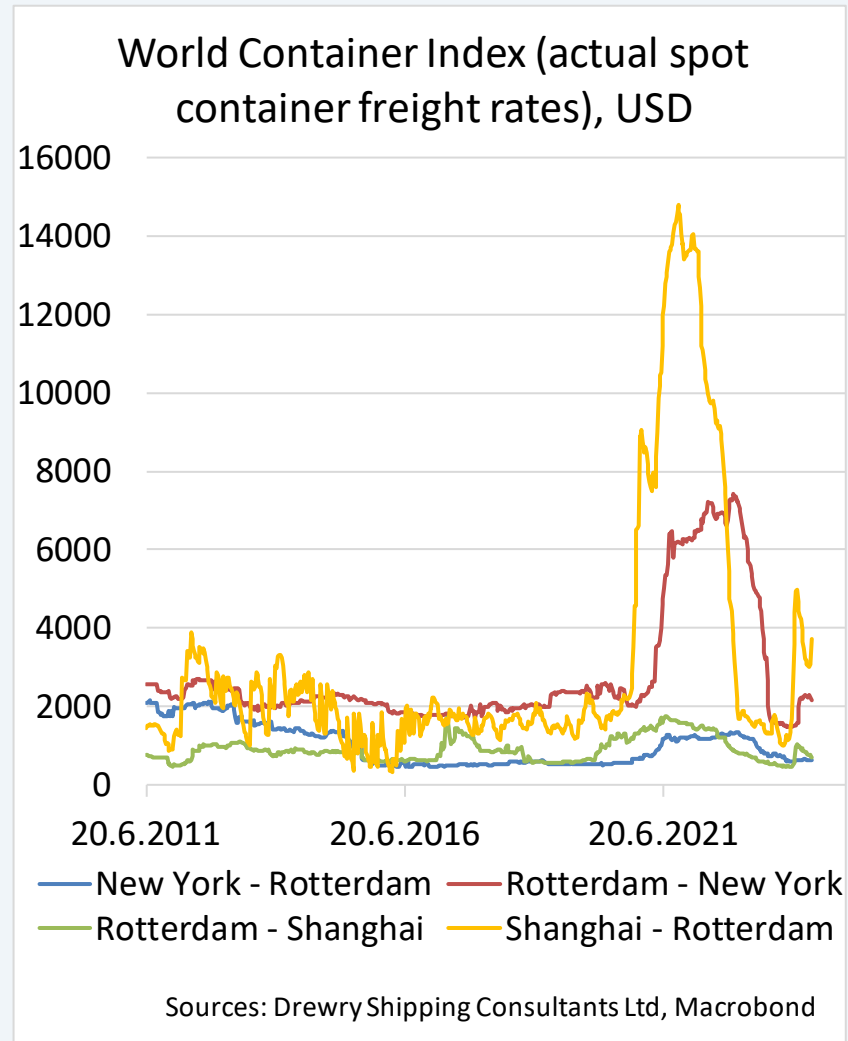# Real Effective Exchange Rates

- Japan's real effective exchange rate has depreciated a lot.

- Mexico's has appreciated.

Real Effective Exchange Rate
Index, 2020 = 100

Euro Area — USA — Japan — Canada — Australia — S. Korea

Sources: BIS, Macrobond.

Real Effective Exchange Rate
Index, 2020 = 100

Brazil — India — Indonesia — Mexico — China — Turkey

Sources: BIS, Macrobond.
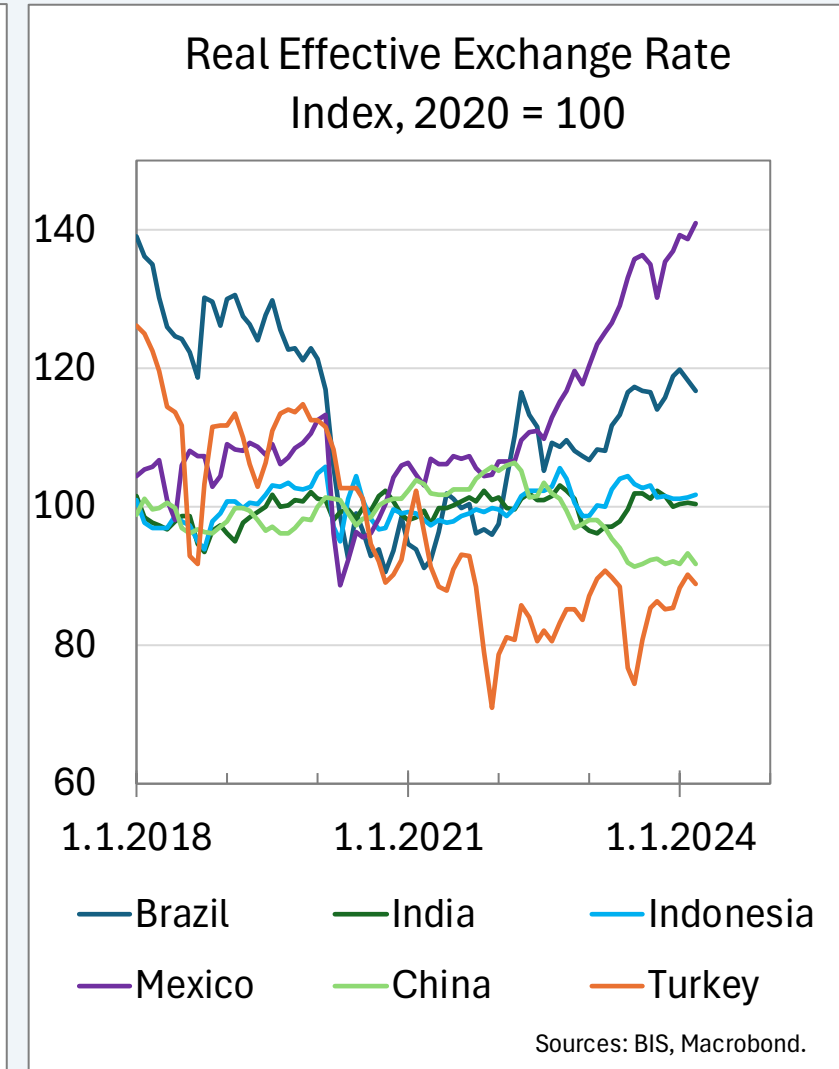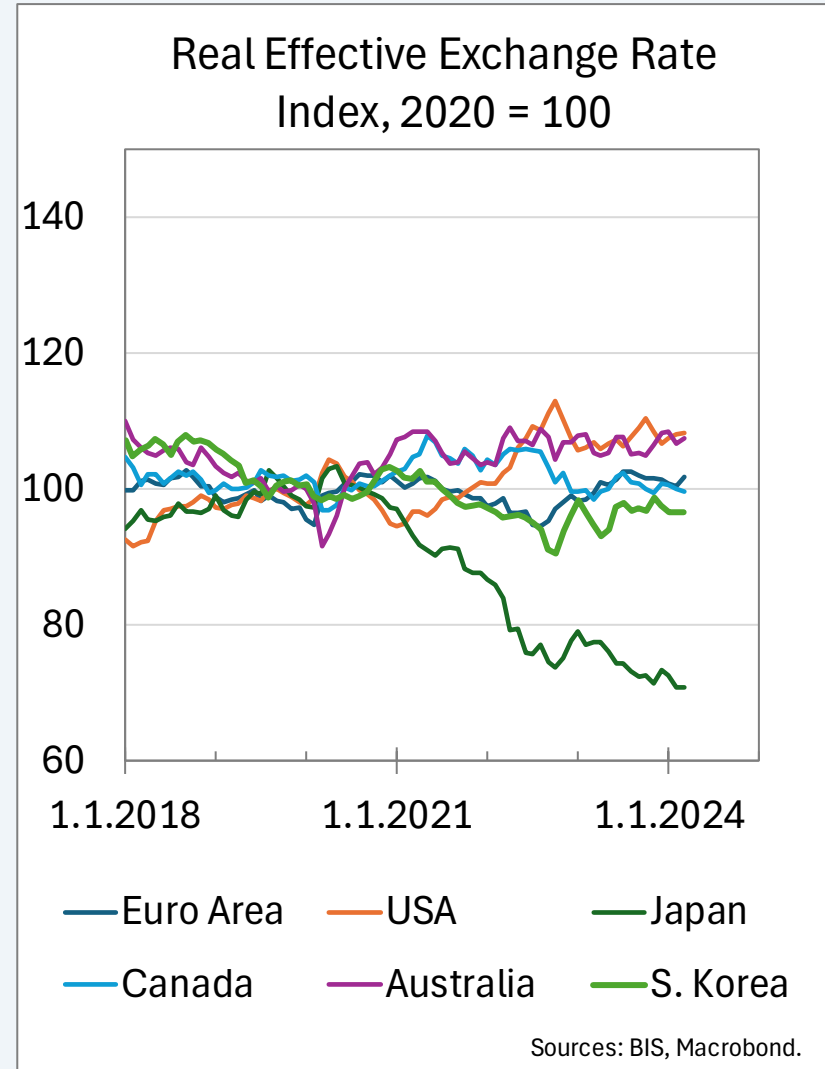
World trade has faced shocks

- The shocks have mainly passed.
- However, e.g. Maersk is still rerouting around the Cape of Good Hope.

World Container Index (actual spot container freight rates), USD

New York - Rotterdam — Rotterdam - New York
Rotterdam - Shanghai — Shanghai - Rotterdam

Sources: Drewry Shipping Consultants Ltd, Macrobond

World Foreign Trade, Global Supply Chain Pressure Index, Total, Index

Sources: Federal Reserve Bank of New York, Macrobond.

Purchasing managers' indices point toward a mild recovery

- EU manufacturing is a laggard.

- USA, China, and Japan are doing better.

- Better development in emerging economies.

Manufacturing PMI, SA

Legend: EU, USA, Japan, Canada, Australia, S. Korea

Sources: S&P Global, au Jibun Bank, Macrobond.

Manufacturing PMI, SA

Legend: Brazil, India, Indonesia, Mexico, China, Turkey

Sources: S&P Global, HSBC, Caixin, Istanbul Chamber of Industry, Macrobond.
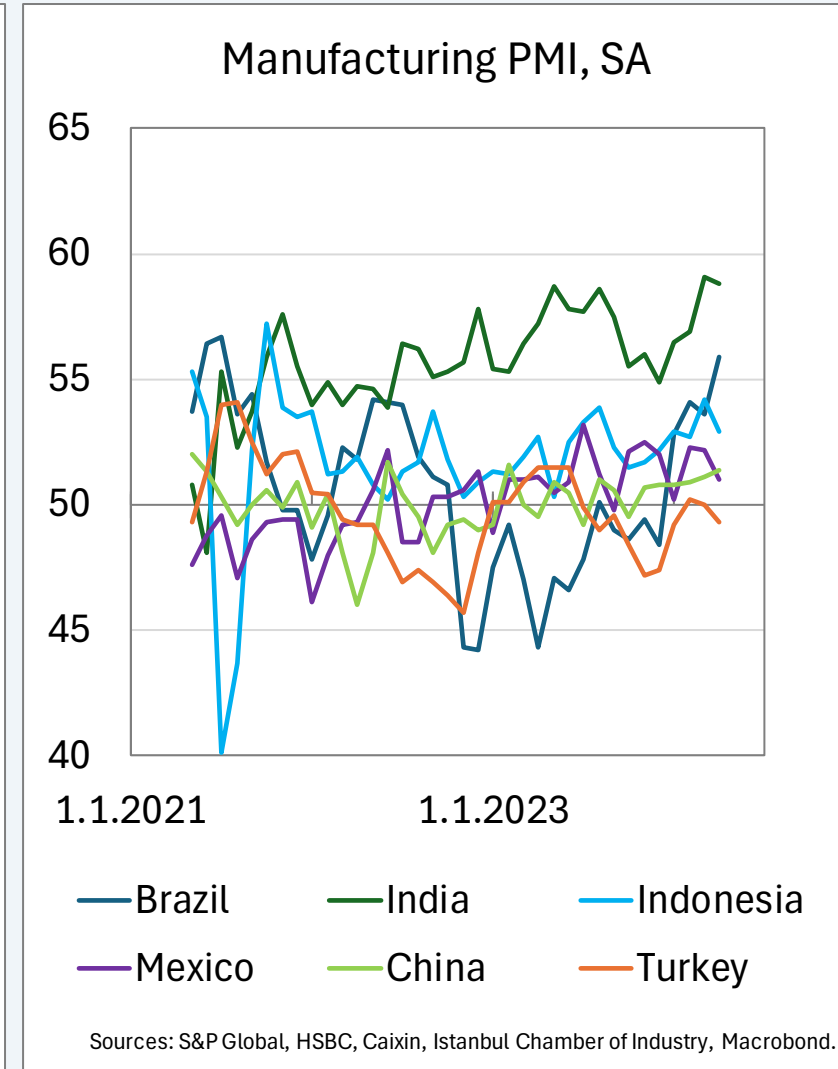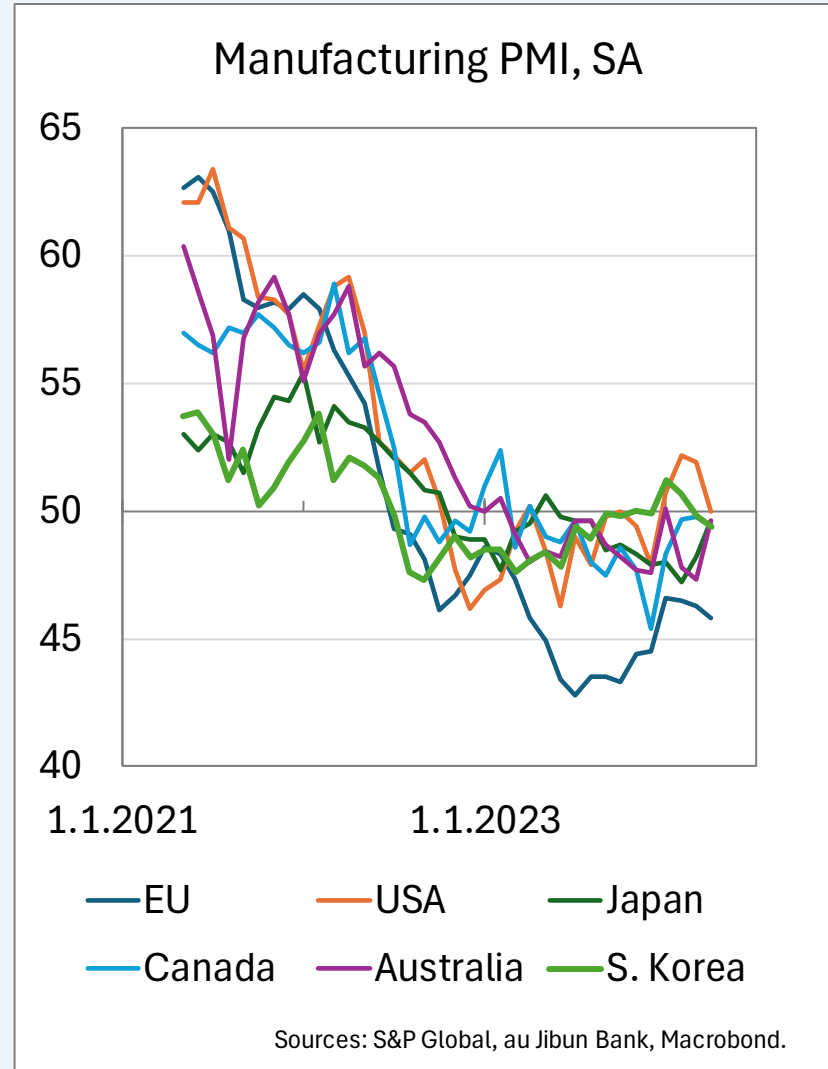
- Services are doing better than manufacturing in developed countries, also in the EU.

Services PMI, SA

EU — USA — Japan — Australia

Sources: S&P Global, au Jibun Bank, Macrobond.

Services PMI, SA

Brazil — India — China

Sources: S&P Global, HSBC, Caixin, Macrobond.
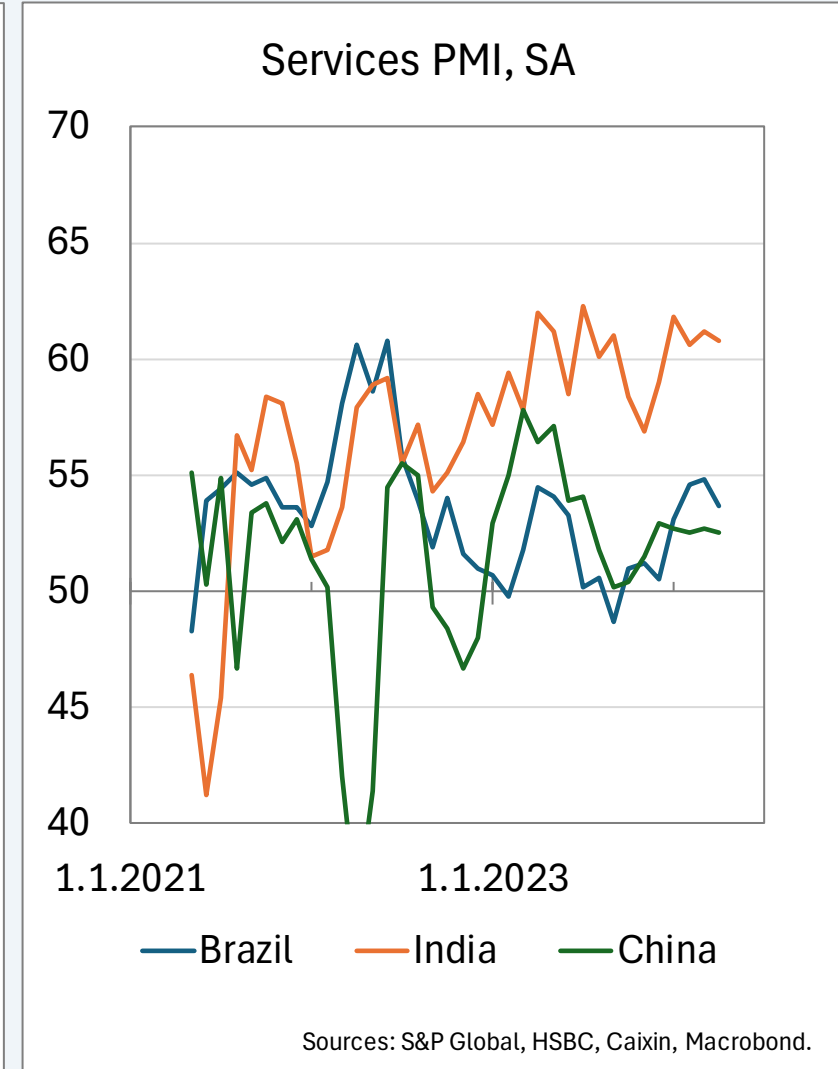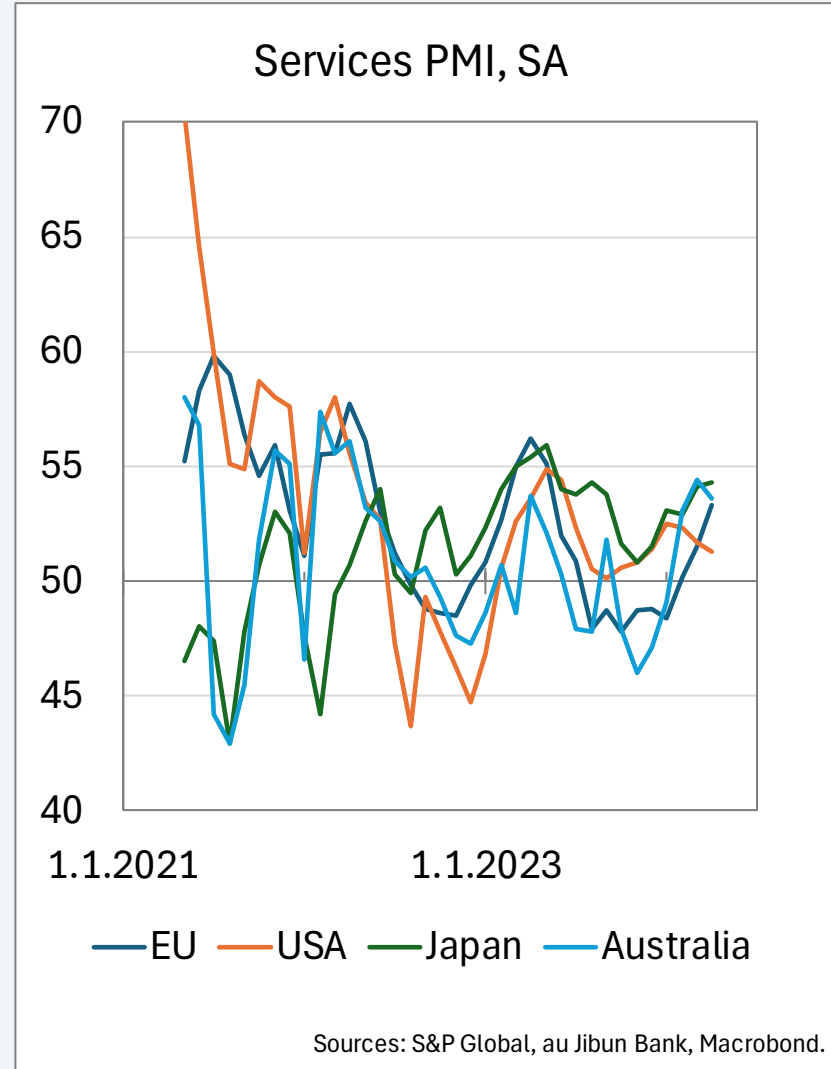
Will the US growth engine hold its strength?

- Private consumption has been strong, supported by good employment data and wage growth.

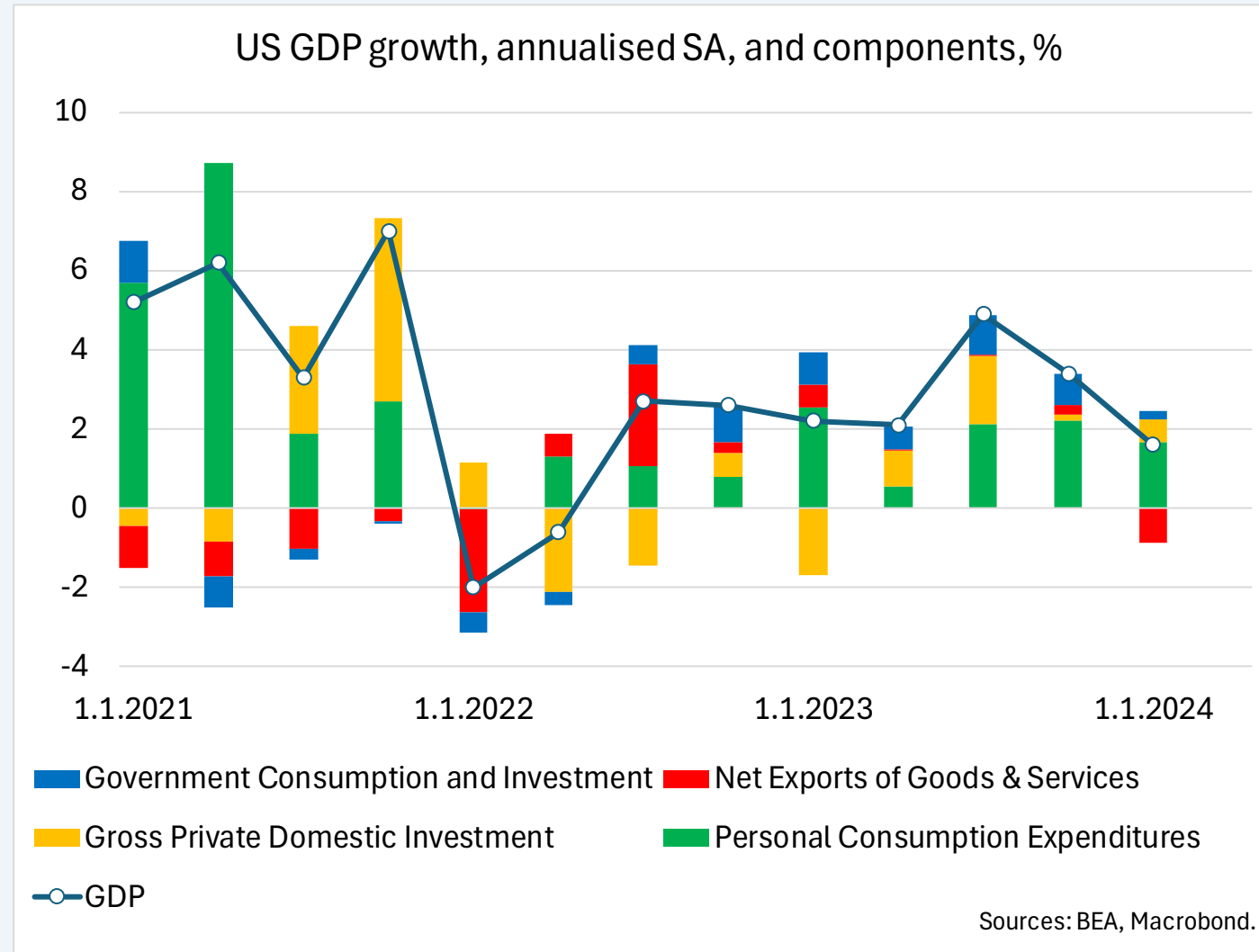- Government activity has also supported growth.

- Net energy exports have helped the economy.

- Fiscal policy is expected to have a negative impact on GDP growth. 2024 is an election year which is likely to boost expenditure.
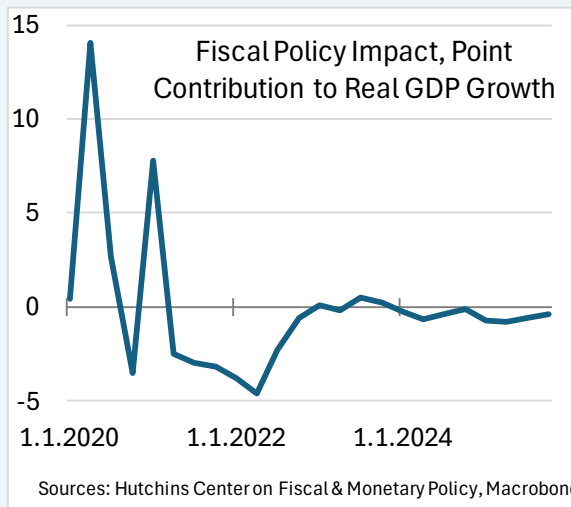
- New and much higher tariffs on imports from China, incl. electric vehicles (➔100%), EV batteries (25%), solar cells (50%), and steel and aluminium (25%).

Fiscal Policy Impact, Point Contribution to Real GDP Growth

Sources: Hutchins Center on Fiscal & Monetary Policy, Macrobond

US GDP growth, annualised SA, and components, %

Government Consumption and Investment
Net Exports of Goods & Services
Gross Private Domestic Investment
Personal Consumption Expenditures
GDP

Sources: BEA, Macrobond.

A closer look at US private consumption and investment

Personal consumption expenditures, Vol. yoy %

— Non-Durable Goods   — Durable Goods
— Services

Sources: BEA, Macrobond.

Gross private fixed investment, Vol. yoy %
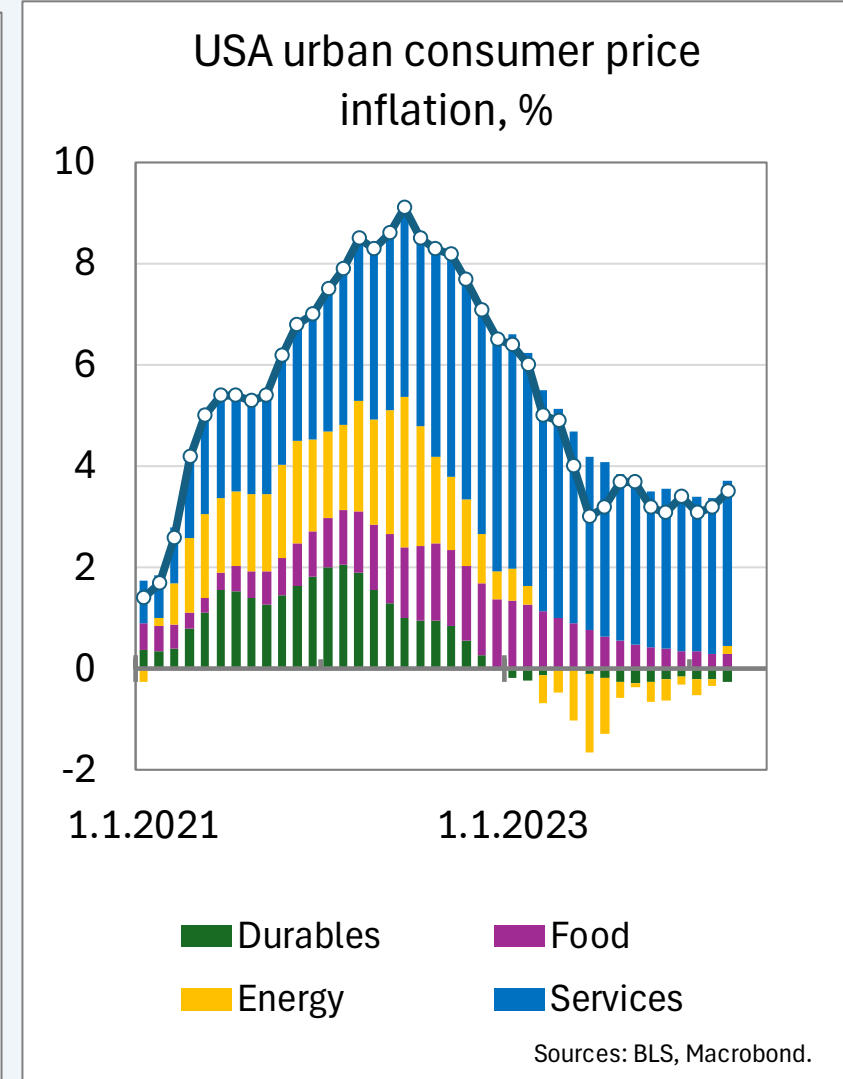
— Nonresidential, Structures
— Nonresidential, Equipment
— Nonresidential, Intellectual Property
— Residential

Sources: BEA, Macrobond.
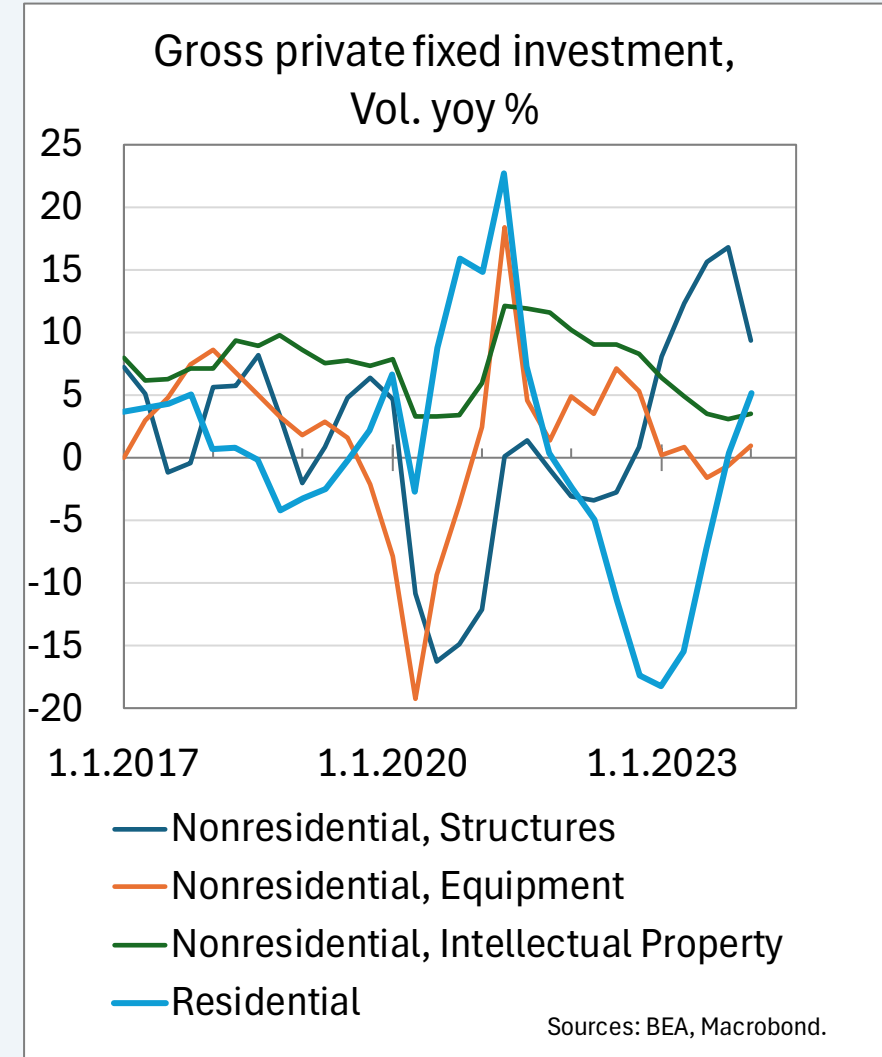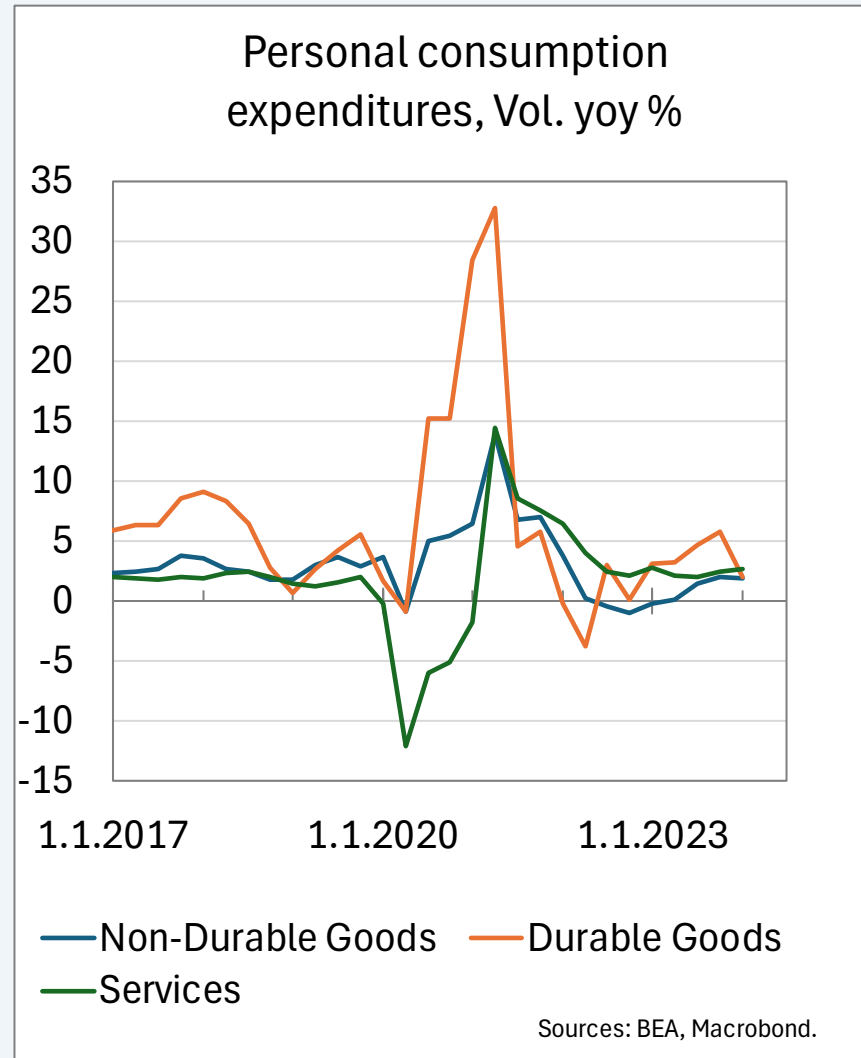
A closer look at US inflation

- Will the next Fed policy-rate move be downwards or upwards?

- The latest employment data were weak.

- Import tariffs will put pressure on prices.

Nominal weekly earnings

Employed Full Time, Wage & Salary Workers, Current Prices, SA, USD

Change yoy, % (rhs)

Sources: BLS, Macrobond.

USA urban consumer price inflation, %

All Items
Food
Energy
Durables
Nondurabl. less food
Services

Sources: BLS, Macrobond.

USA urban consumer price inflation, %

Durables
Energy
Food
Services

Sources: BLS, Macrobond.
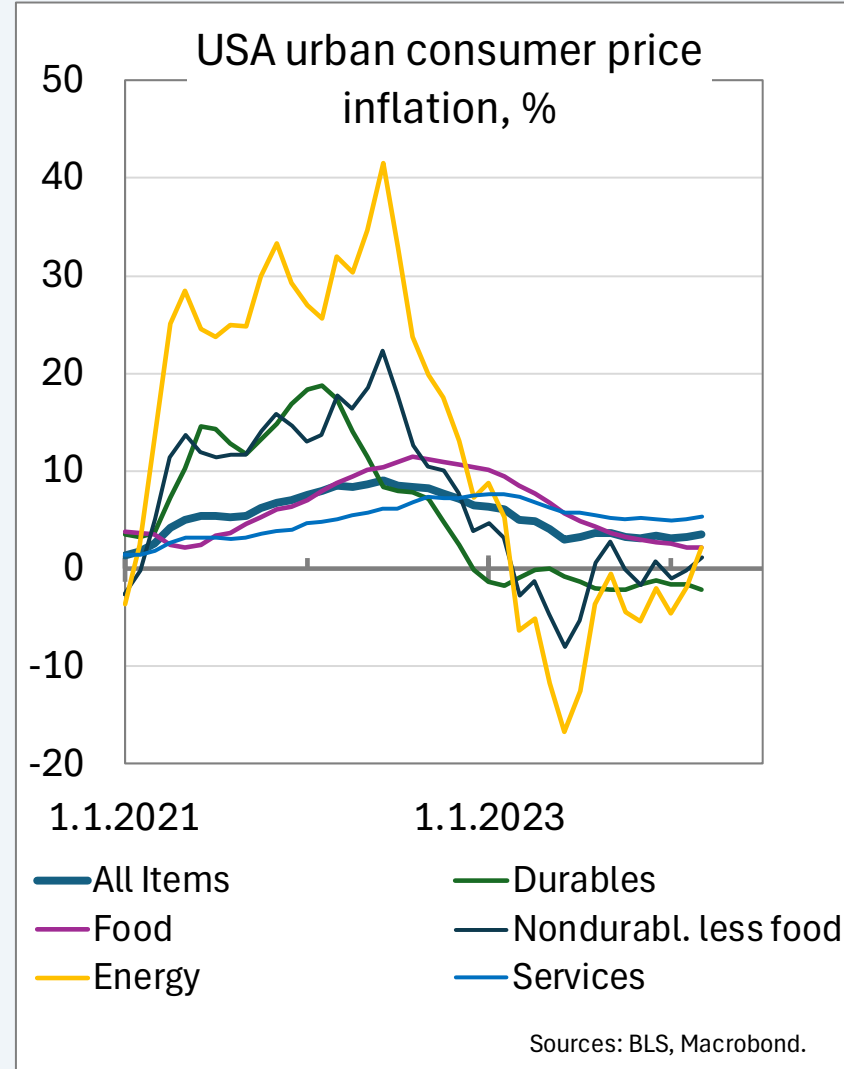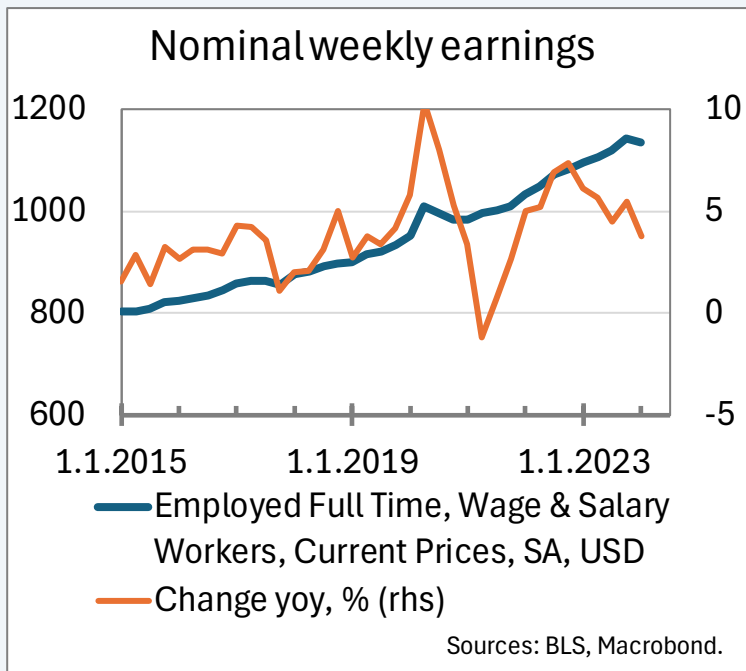
The favourite measure of the Fed: PCE

- CPI is higher than PCE.

Personal Consumption Expenditures inflation, %

Legend: Total Price Index, Goods, Services, Core rate

Sources: BEA, Macrobond.

Personal Consumption Expenditures inflation, %

Legend: Energy Goods & Services

Sources: BEA, Macrobond.

USA
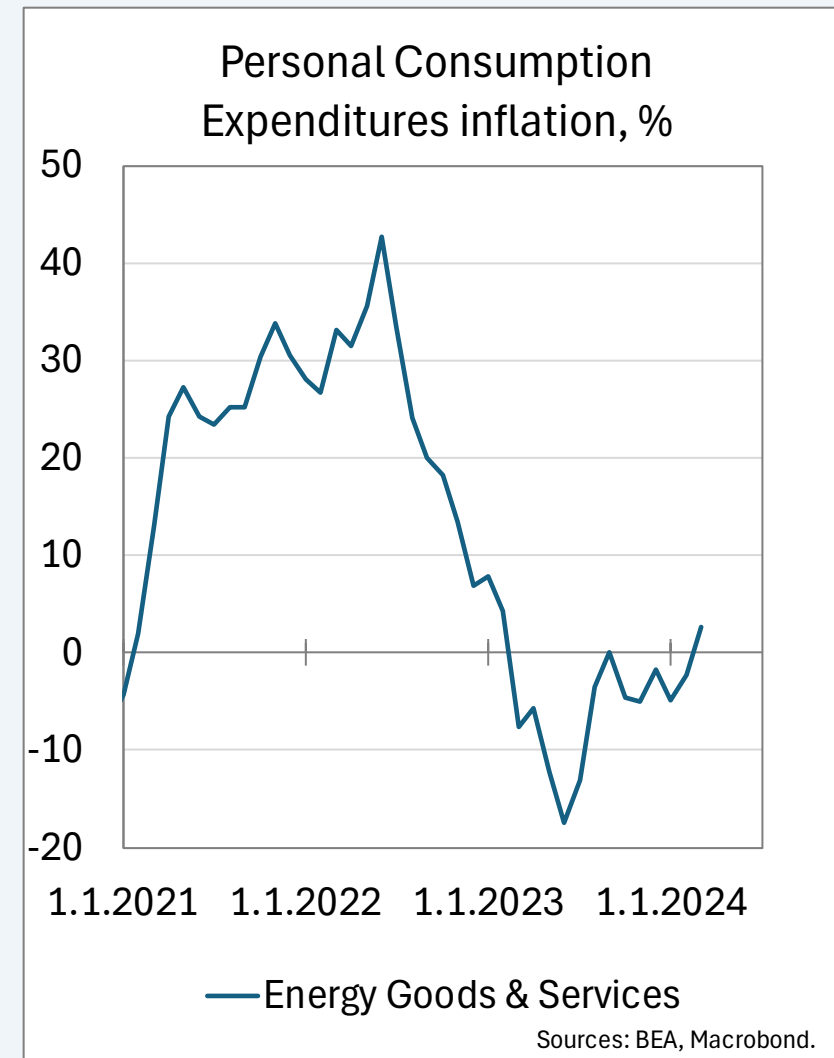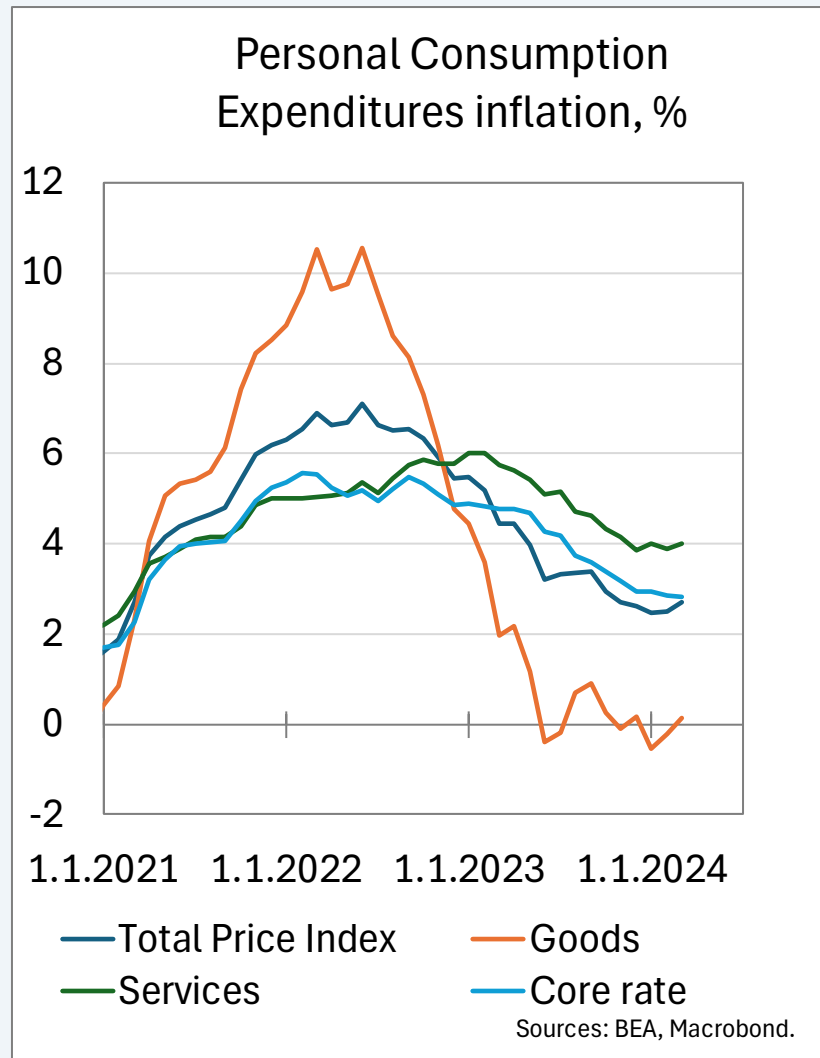
- A recession has been on the cards for quite some time already, but it has not materialized.

US recession probability 12 months ahead

—— Leading Indicators, New York Fed, Recession Probability (Treasury spreads)

Sources: NY Fed, Macrobond.

Some US economic indicators

—— Leading Indicators, Dallas Fed, Weekly Economic Index

—— St. Louis Fed, Real GDP Nowcast, Estimate, SA, AR

—— Price Pressures, St. Louis Fed (rhs)

Price pressure: probability that expected personal consumption expenditures price index (PCEPI) inflation rate (12-mo.) over the next 12 months will exceed 2.5 percent.
Sources: Dallas Fed, St. Louis Fed, Macrobond.

Japan

- Growth has been volatile but positive.

Japan quarterly GDP growth SA, and components, %

Legend: Private Consumption, Investment, Government Consumption, Inventories, Net Exports, GDP

Sources: Japanese Cabinet Office (CAO), Macrobond.
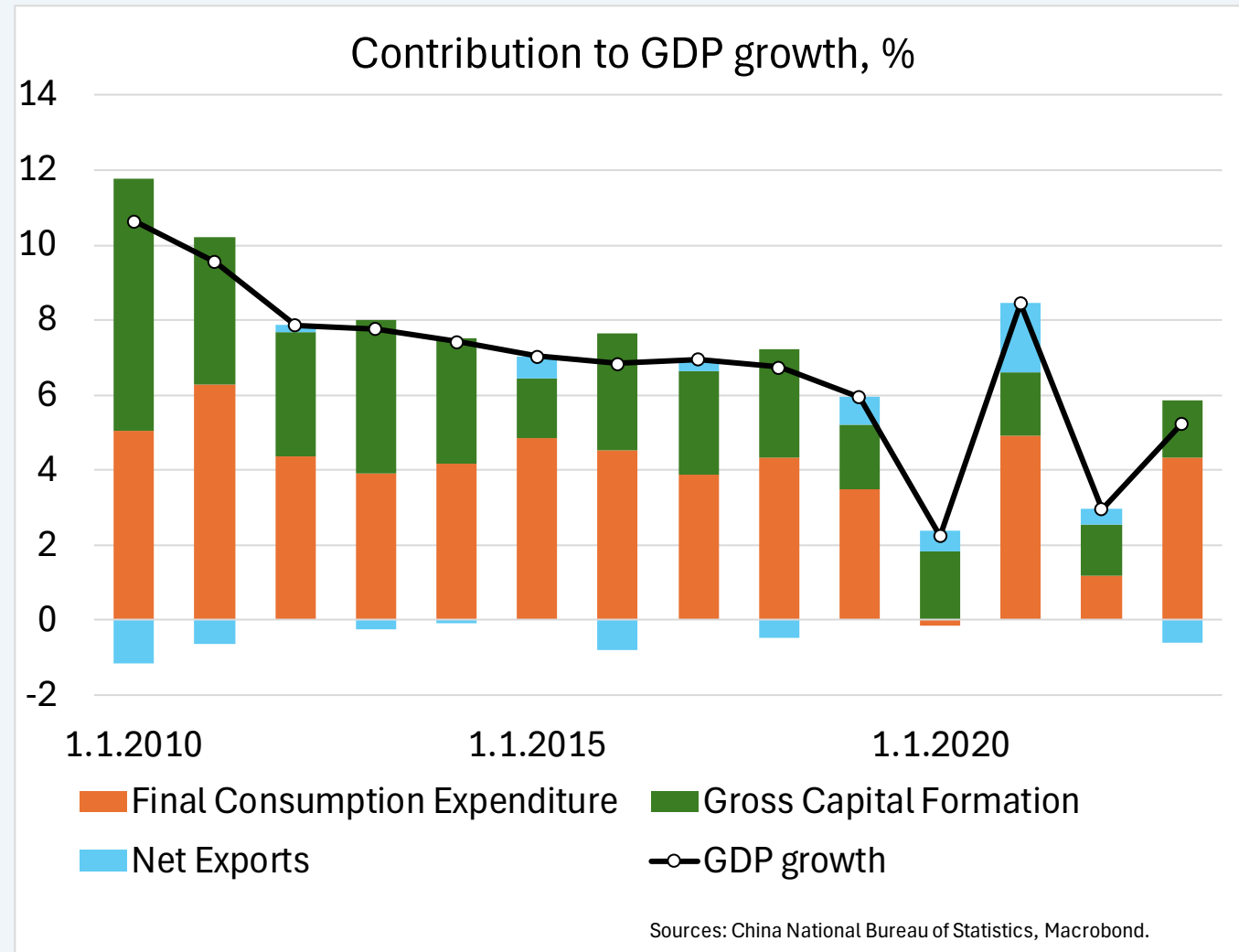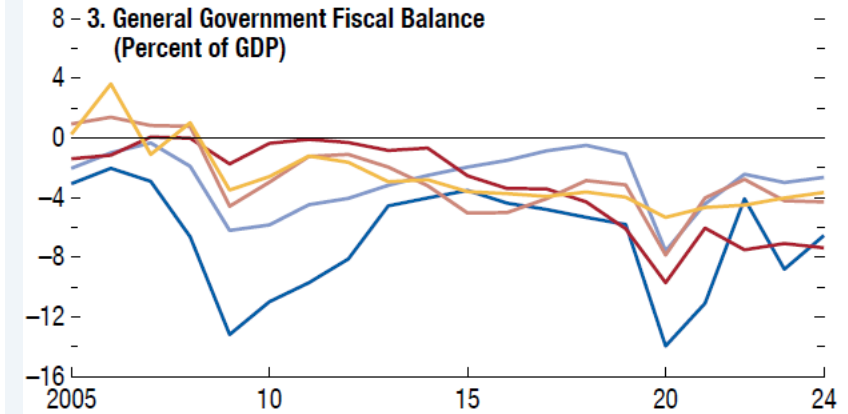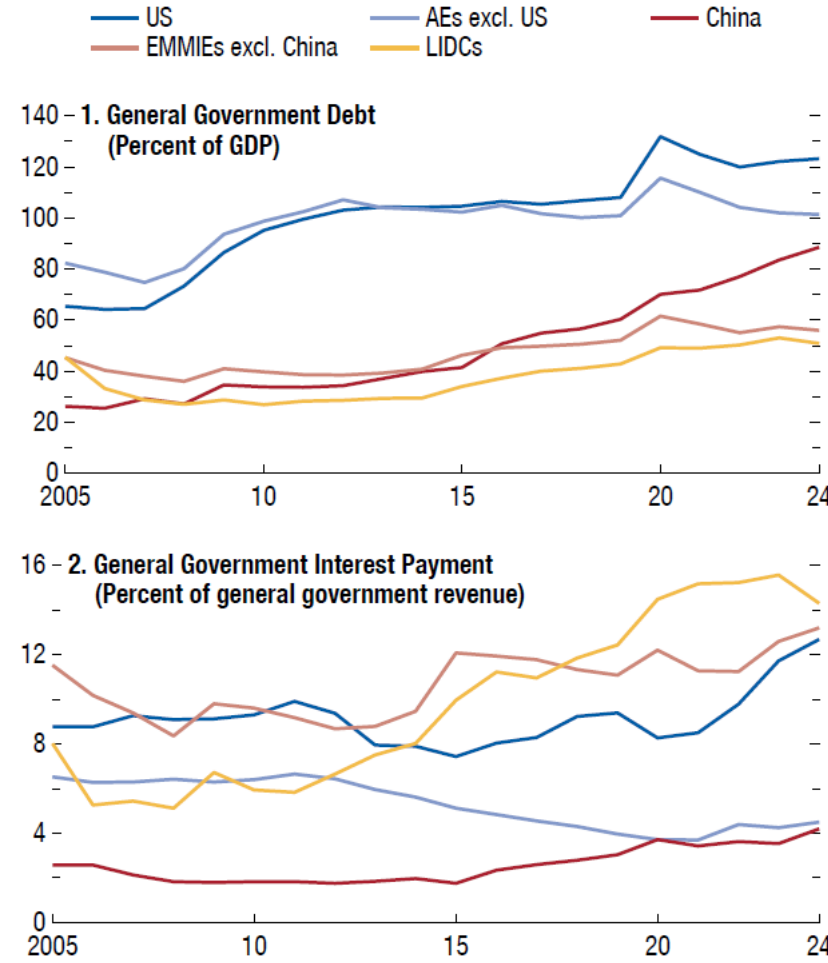
China

- The contribution of gross capital formation to GDP growth has decreased.

- Difficulties in the real estate sector continue. However, there is a rise in investment in infrastructure and manufacturing capacity.

- Government involvement is extensive.

- FDI inflows to China are down. Most of the inflows have come from Hong Kong. According to UNCTAD calculations, top ultimate investors in 2020 FDI stock were China (12%), HK (10%), the USA (10%), Japan (8%), and the UK (6%).

China's inbound foreign direct investment fell to lowest level in 30 years

Direct investment liabilities ($bn)

2023: $33bn

FINANCIAL TIMES   Source: State Administration of Foreign Exchange

Contribution to GDP growth, %

Final Consumption Expenditure   Gross Capital Formation
Net Exports   GDP growth

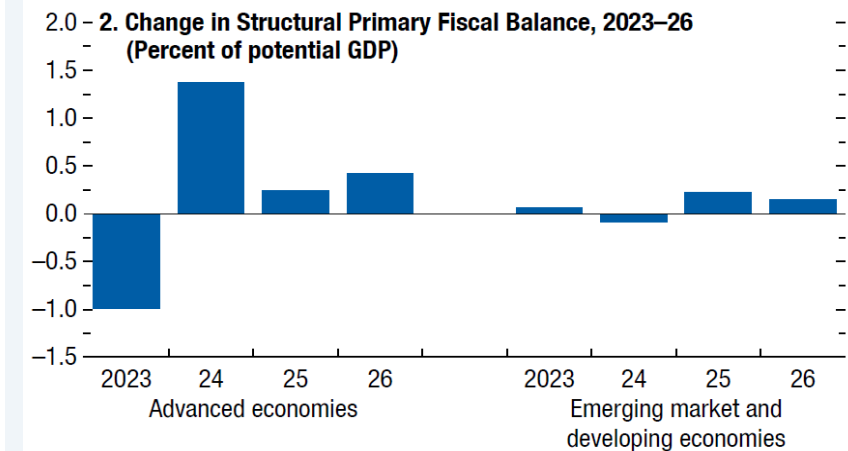Sources: China National Bureau of Statistics, Macrobond.

Government indebtedness

- China's public sector is ever more indebted with large deficits.

- Also the USA is running large deficits, and interest payments are a large share of public revenues.

- Euro area government debt is 89% of GDP, about the same as China's. Direction is different, however.

- The IMF expects advanced economies to tighten their fiscal stance especially this year.

Figure 1.12. Elevated Debt and Deficits

Legend: US, AEs excl. US, China, EMMIEs excl. China, LIDCs

1. General Government Debt (Percent of GDP)

2. General Government Interest Payment (Percent of general government revenue)

3. General Government Fiscal Balance (Percent of GDP)

Source: IMF staff calculations.
Note: AEs = advanced economies; EMMIEs = emerging market and middle-income economies; excl. = excluding; LIDCs = low-income developing countries.

2. Change in Structural Primary Fiscal Balance, 2023–26 (Percent of potential GDP)

Advanced economies · Emerging market and developing economies

Source: IMF staff calculations.
Note: In panel 2, the structural primary fiscal balance is the cyclically adjusted primary balance corrected for a broader range of noncyclical factors, such as changes in asset and commodity prices.

Geopolitical and geoeconomic tensions

- US – China relations. China's imperialistic aggression (Taiwan, South China Sea etc.)

- Russia's imperialistic aggression

- Middle East

- US presidential elections in November.

- EU parliament elections in June. Populist radical right.

- Geoeconomic fragmentation
  - West (especially the USA) vs. China & Co.
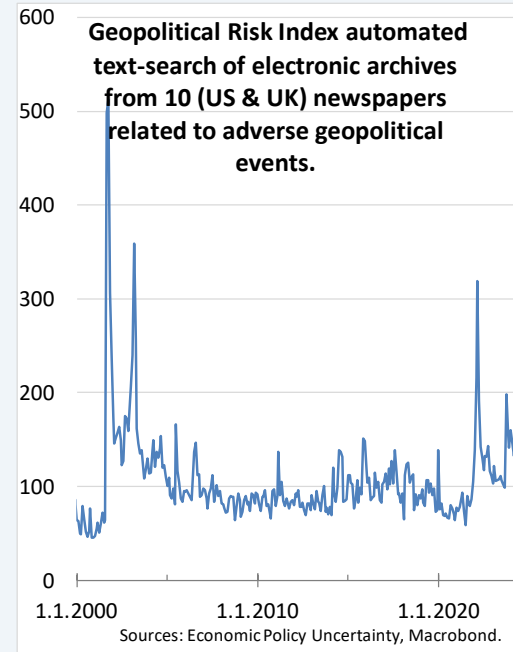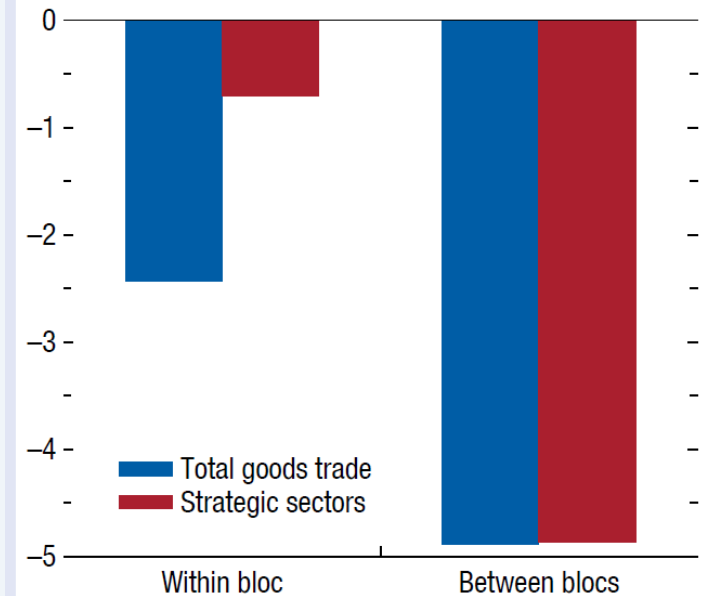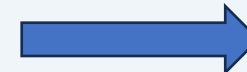 - Effect on trade, FDI, innovation, prices etc.

Geopolitical Risk Index automated text-search of electronic archives from 10 (US & UK) newspapers related to adverse geopolitical events.

Sources: Economic Policy Uncertainty, Macrobond.

Figure 1.1.1. Fragmentation Affecting Trade
(Percentage points; difference in trade growth before and after war)

Legend: Total goods trade / Strategic sectors
Within bloc / Between blocs

Sources: Trade Data Monitor; and IMF staff calculations.
Note: Bilateral quarterly growth rates are computed as the difference in log bilateral trade averaged using weights equal to the bilateral nominal trade. Strategic sectors include the following Harmonized System two-digit chapters: 28, 29, 30, 38, 84, 85, 87, 88, 90, and 93. Before the war is between 2017:Q1 and 2021:Q4. The bloc definition is based on a hypothetical bloc comprising Australia, Canada, Europe, New Zealand, and the US and a hypothetical bloc including China, Russia, and countries siding with Russia during the March 2, 2022, UN General Assembly vote on the war in Ukraine. Other countries are considered nonaligned.

28 Inorganic chemicals; organic or inorganic compounds of precious metals, of rare-earth metals, of radioactive elements or of isotopes
29 Organic chemicals
30 Pharmaceutical products
38 Miscellaneous chemical products
84 Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof
85 Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles
87 Vehicles other than railway or tramway rolling-stock, and parts and accessories thereof.
88 Aircraft, spacecraft, and parts thereof
90 Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof
93 Arms and ammunition; parts and accessories thereof

Large differences in growth forecasts for 2024

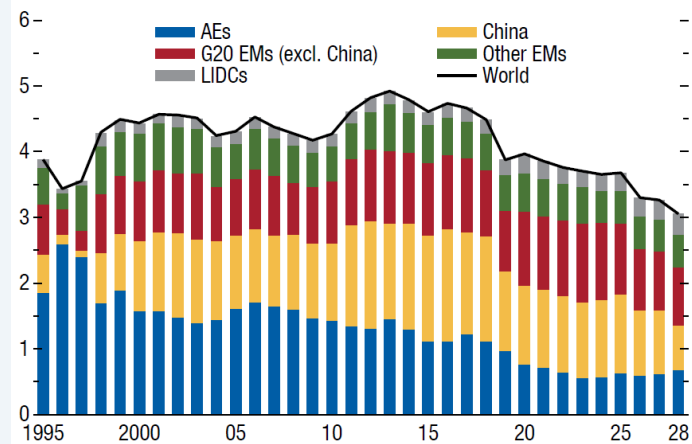
- A 2.5% GDP growth is often associated with recession in the world economy.

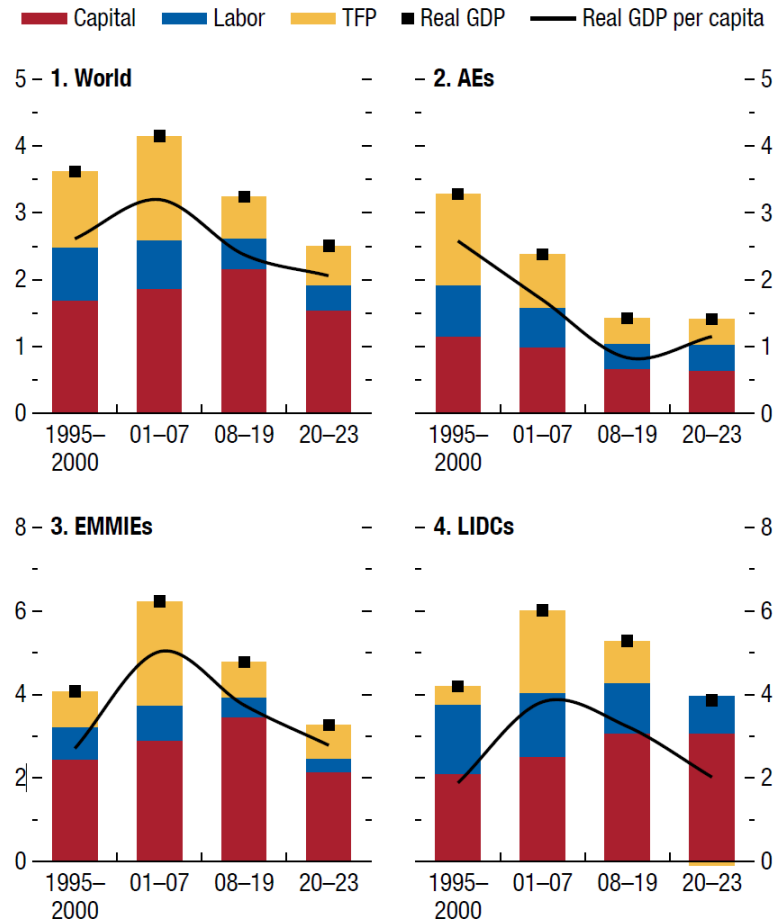- Optimistic? IMF forecasts.
- Slower growth in EMEs.

Figure 4.1. Five-Year-Ahead GDP Growth
(Percent)

Source: IMF staff calculations.
Note: The predicted variable is real GDP growth. The years on the horizontal axis refer to the year for which a forecast is made, using the April *World Economic Outlook* five years prior, such that, for example, the 2028 forecast is based on the April 2023 *World Economic Outlook*, and so on. AEs = advanced economies; EMs = emerging markets; excl. = excluding; G20 EMs = Argentina, Brazil, China, India, Indonesia, Mexico, Russia, Saudi Arabia, South Africa, and Türkiye; LIDCs = low-income developing countries.

	2023	2024E	2025E
World Bank (January)	2.6	2.4	2.7
OECD (February)	3.1	2.9	3.0
Fitch (March)		2.4	2.5
S&P Global (March)		2.6	2.6
IMF (April)	3.2	3.2	3.2
UNCTAD (April)		2.6	
Conference Board (April)		3.0	3.1

	2023	2024E	2025E
Advanced economies	1.6	1.7	1.8
- Euro Area	0.4	0.8	1.5
- USA	2.5	2.7	1.9
- Japan	1.9	0.9	1.0
EMDE	4.3	4.2	4.2
- China	5.2	4.6	4.1
- India	7.8	6.8	6.5

Overall growth slowdown (IMF data and analysis)

Figure 3.4. Contribution of Components of GDP Growth, 1995–2023
(Percent)

Legend: Capital | Labor | TFP | Real GDP | Real GDP per capita

1. World
2. AEs
3. EMMIEs
4. LIDCs

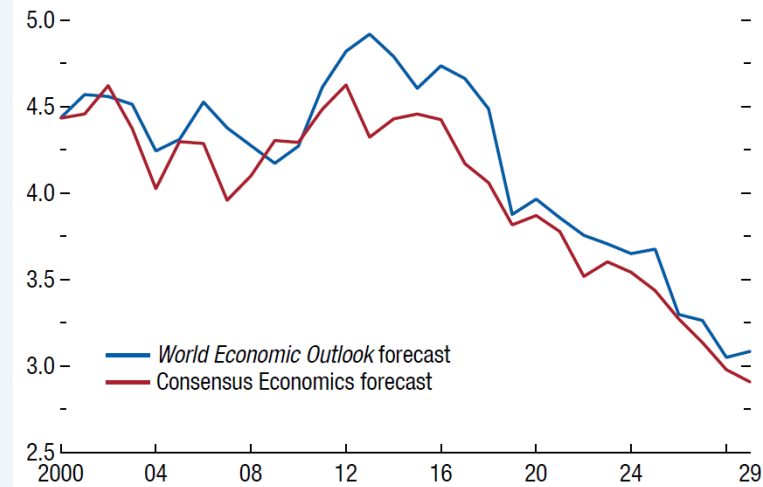(x-axis categories for each panel: 1995–2000, 01–07, 08–19, 20–23)

Sources: International Labour Organization; Penn World Table version 10.01; United Nations, World Population Prospects; and IMF staff calculations.
Note: Growth decomposition sample comprises 140 countries. Contributions of capital growth and labor growth reflect output share of respective factor inputs and their growth rates. AEs = advanced economies; EMMIEs = emerging market and middle-income economies; LIDCs = low-income developing countries; TFP = total factor productivity.

- Mostly slower TFP growth due to increased misallocation of capital and labour across firms within sectors because of economic frictions.
- Also decline in private investment and slower working-age population growth.
- IMF recommendations: structural reforms; increasing labour force participation; AI.

Figure 3.1. Five-Year-Ahead Real GDP Growth Projections, 2000–29
(World growth, percent)

— World Economic Outlook forecast
— Consensus Economics forecast

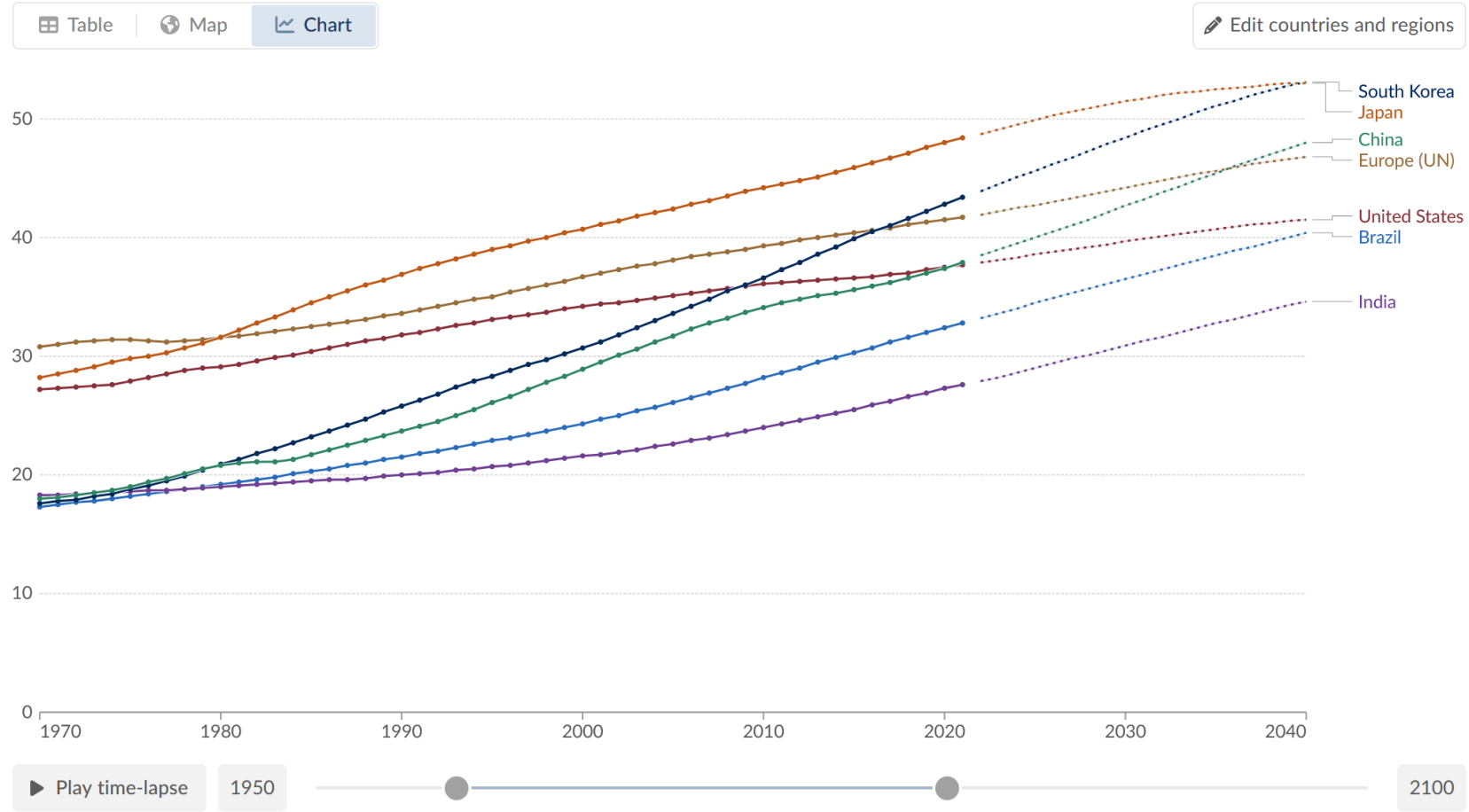(x-axis: 2000, 04, 08, 12, 16, 20, 24, 29; y-axis: 2.5 to 5.0)

Sources: Consensus Economics; and IMF staff calculations.
Note: *World Economic Outlook* (WEO) sample comprises 196 economies and Consensus Economics sample comprises 88 economies. Global real GDP growth projections are calculated using GDP in purchasing power parity in international dollar weights. The years on the horizontal axis refer to the year for which a forecast is made, using the April WEO from five years earlier. For example, the 2029 forecast is based on the April 2024 WEO, and so on. The red line depicts the mean of the Consensus Economics forecasts.

Getting older

Median age

The median age splits the population into two equal groups, with as many people older than it as people younger than it. Future projections are based on the UN medium-fertility scenario.

Our World in Data

| Table | Map | Chart |

Edit countries and regions

South Korea
Japan
China
Europe (UN)
United States
Brazil
India

▶ Play time-lapse   1950   2100

Data source: United Nations, World Population Prospects (2022) – Learn more about this data
OurWorldInData.org/age-structure | CC BY

Download   Share   Enter full-screen

ETLA

ETLA | Elinkeinoelämän tutkimuslaitos

From convergence to divergence

Figure 3.2.1. GDP Convergence between Countries, 2000–28
(Rate at which gap to frontier is closed, negative = convergence)

- 95 percent confidence interval
- Historical WEO projections
- With AI effects

Forecast
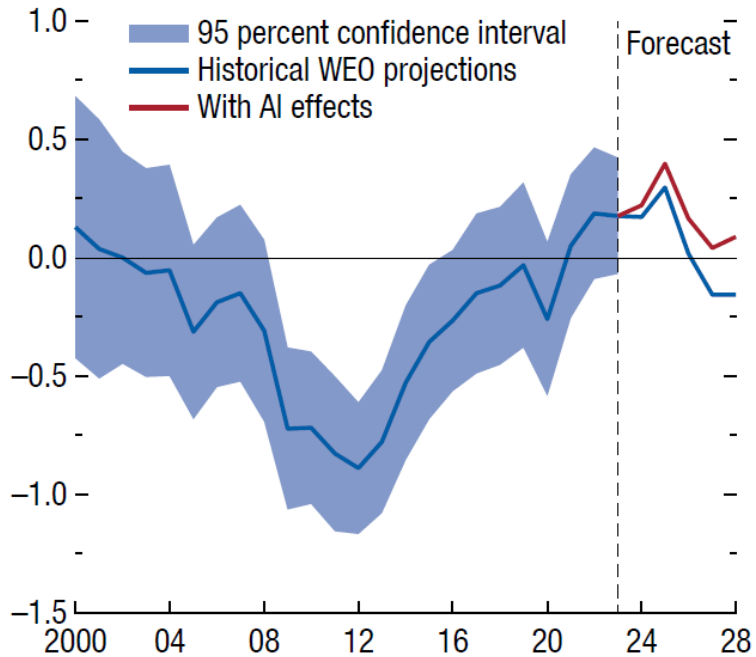
Source: IMF staff calculations.
Note: The convergence rate for year t corresponds to the β_t coefficient in the following regression: $\Delta\log(GDPpc_{it}) = \alpha_t + \beta_t\log(GDPpc_{it-5}) + \varepsilon_{it}$, in which $\Delta\log(GDPpc_{it})$ is average year-over-year GDP per capita growth in the five-year period between t and $t-5$ and $\log(GDPpc_{it-5})$ is GDP per capita at the beginning of the period. See Box 3.3 for effects of artificial intelligence (AI effects) on growth. AI = artificial intelligence; WEO = *World Economic Outlook*.

Figure 3.2.2. Global Inequality, 1995–2028
(Gini points, 0 = perfect equality; times)

- Gini
- Top 10/bottom 50 (right scale)

Forecast
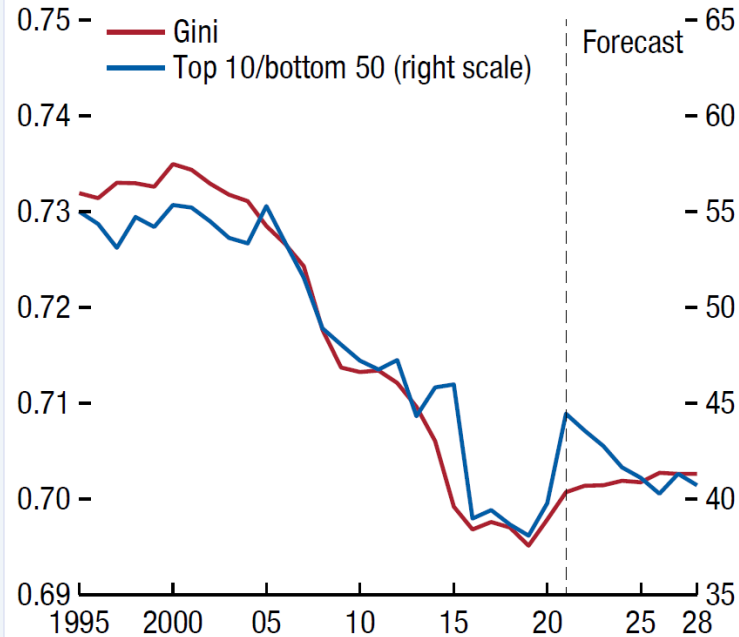
Sources: World Inequality Database; and IMF staff calculations.
Note: On the left scale, the Gini index calculates how the global income distribution deviates from a perfectly equal distribution. Income is measured before taxes. "Top 10/bottom 50" compares the average income of the top 10 and bottom 50 of the global income distribution. On the right scale, "times" refers to the number of times the average income of the top 10 of the income distribution is larger than the average income of the bottom 50 of the distribution. For example, a value of 40 on the right scale means the average income of the top 10 is 40 times larger than that of the bottom 50.

- GDP convergence between countries has turned into divergence (for now).

- Global pre-tax inequality has started to increase.

- Impact on migration etc.?