

# CHARTS OF THE WEEK

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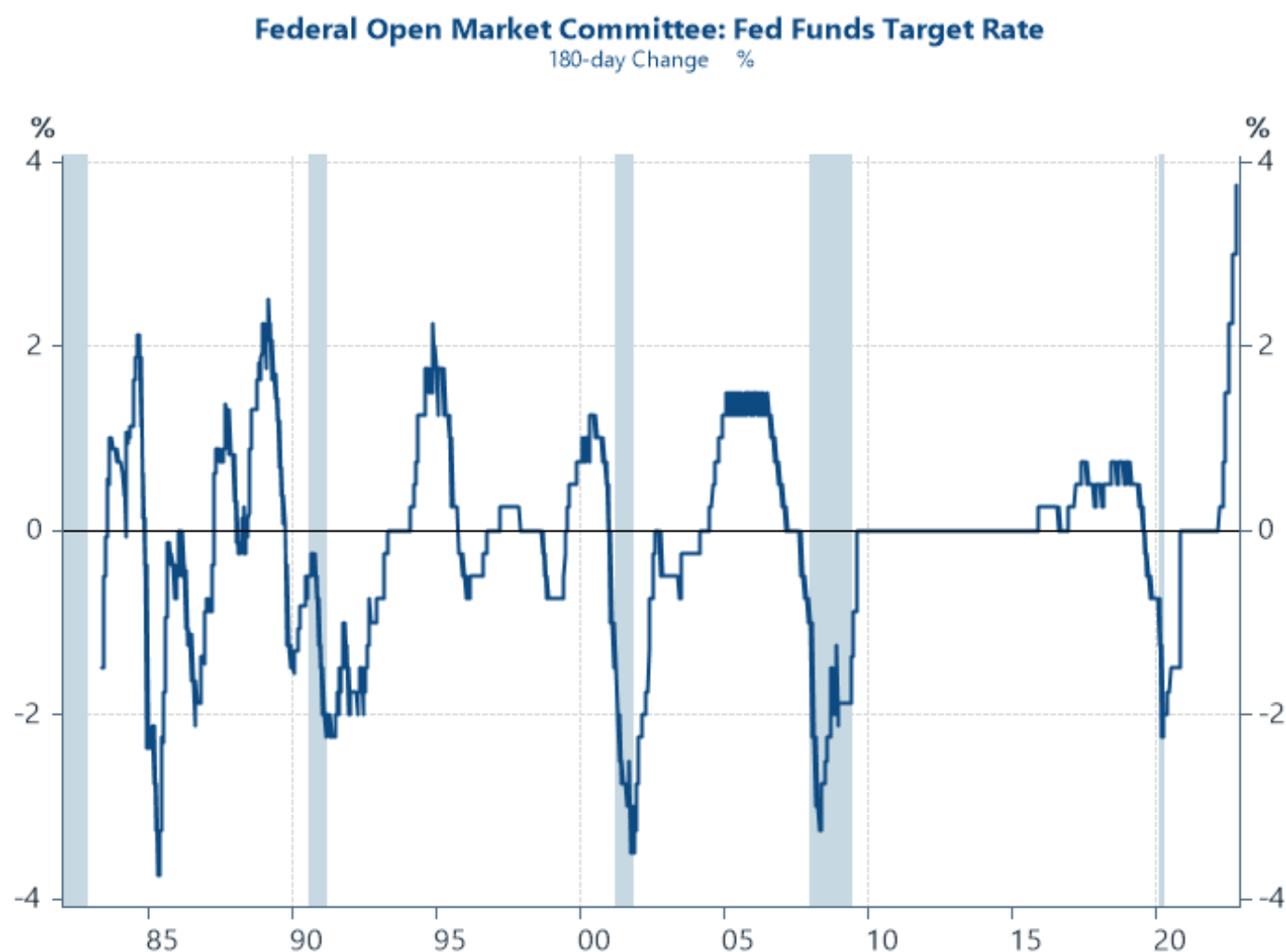
[ANDY CATES](#)

While the US Fed's decision to lift interest rates by 75bps this week was widely expected, subsequent comments from Chair Powell have led financial markets to anticipate more hawkish policy (than previously anticipated) in the period ahead. As our first three charts this week suggest, however, there has arguably already been a big change in the inflation-generating capacity of the world economy in recent months which is magnifying the risks of a policy error. An acute dilemma is certainly being confronted at present by Japan's and China's policymakers, albeit for different reasons, messages conveyed by our fourth and fifth charts this week. Finally in our sixth chart we home in on a new index that we have recently added to our ESG database that measures disaster risks arising from extreme natural events and the negative consequences of climate change.

## The Fed

When it comes to monetary policy, what really matters for economic conditions: interest rate levels or interest rate changes? We can't answer that question in the space we have available but suffice it to say that if changes in interest rates are important, then the US Fed has already enacted a meaningful tightening of monetary policy. The 6-month - or to be more precise, the 180-day change - in the Fed funds target rate is now 3.75 percentage points (see chart 1). That's the biggest 6-month shift for nearly 40 years. As the recession shading suggests in chart 1 below, that doesn't necessarily imply that a recession will follow based on past experience but the odds are not that good.

Chart 1: The Fed Funds Target Rate, 6 month change



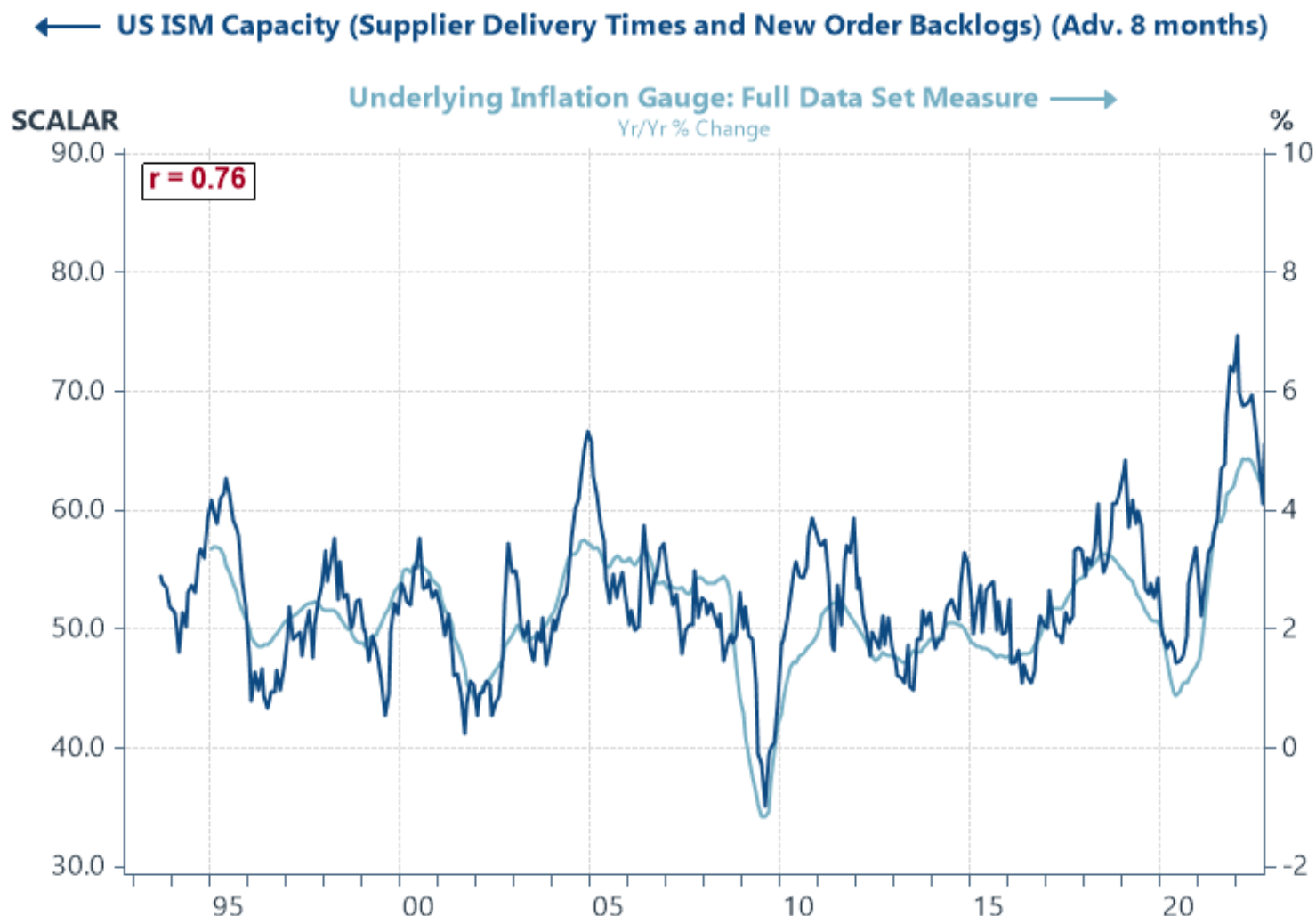
Source: Federal Reserve Board/Haver Analytics

## US manufacturing capacity and underlying inflation

The acute dilemma for the Fed (and other central banks) of course concerns still-high current inflation levels and still-tight labour markets. Encouragingly, some of the incoming data in recent weeks suggest US (and global) inflationary pressures are ebbing. For example, the Federal Reserve Bank of New York's underlying inflation gauge peaked in March and has fallen now for four consecutive months. The capacity utilisation gauges in this week's US ISM survey for October (e.g. supplier delivery times and new order

backlogs) have also moved back to more inflation-friendly levels. And that bodes well for that underlying inflation gauge in the period ahead, as evidenced in chart 2 below.

Chart 2: Capacity components of US ISM survey versus FRBNY's underlying inflation gauge

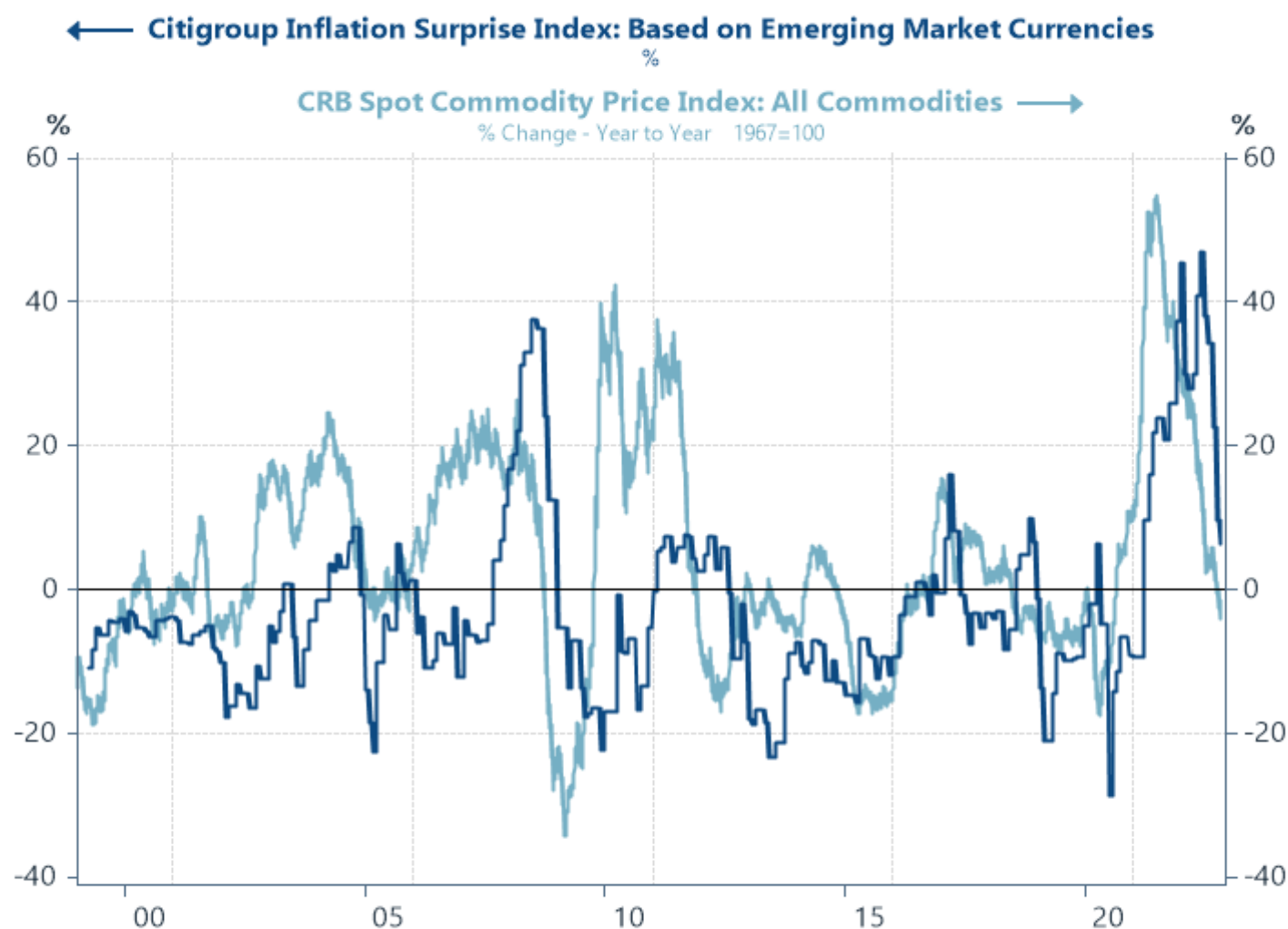


Source: Federal Reserve Bank of New York/Haver Analytics

## Commodity prices and EM inflation surprises

Ebbing demand and less acute supply-side disruption have also been driving many commodity prices lower. That should bode well for headline inflation outcomes in emerging economies which are more sensitive (than developed economies) to the price of food and energy (see chart 3 below).

Chart 3: Commodity price gyrations versus inflation surprises in emerging economies

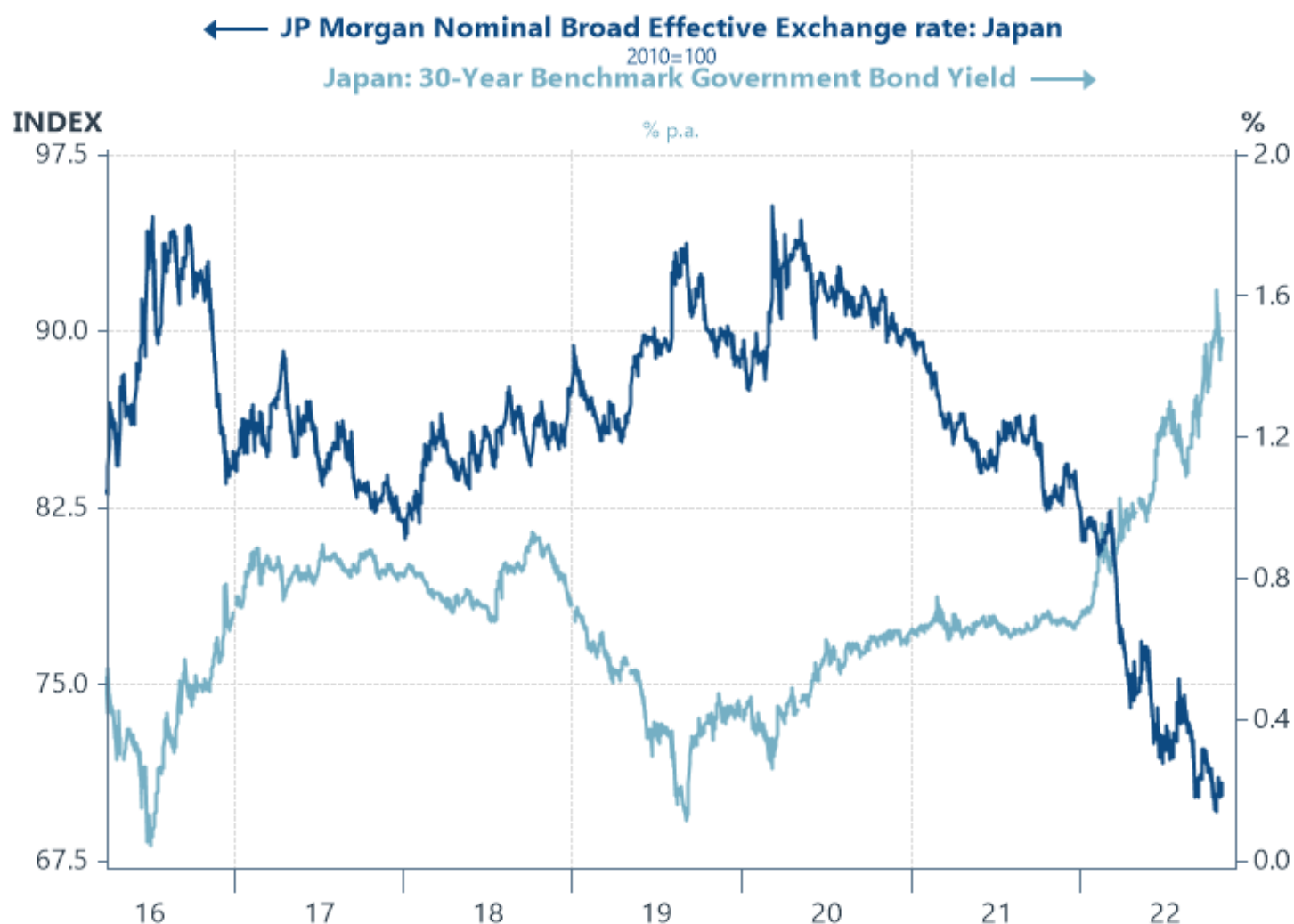


Sources: Citigroup, Commodity Research Bureau/Haver Analytics

## Japan's monetary policy conundrum

The 'tighter for longer mantra' that has applied to most major developed economies at present has not - until recently - applied to Japan. A sluggish recovery from the pandemic and lingering structural restraints have insulated the economy from the same inflation challenges that have bedevilled most major economies. However, while that has, until recently, left the BoJ with some latitude to keep policy rates in negative territory, the wide spread with US has caused the yen to weaken sharply and import prices to rise sharply. And this has heightened fears that monetary policy may now be too loose. Indeed, longer-term JGB yields have climbed sharply in recent weeks, forcing – via its yield-curve control policy – the BoJ to intervene.

Chart 4: Long-term JGB yields versus the nominal effective JPY exchange rate

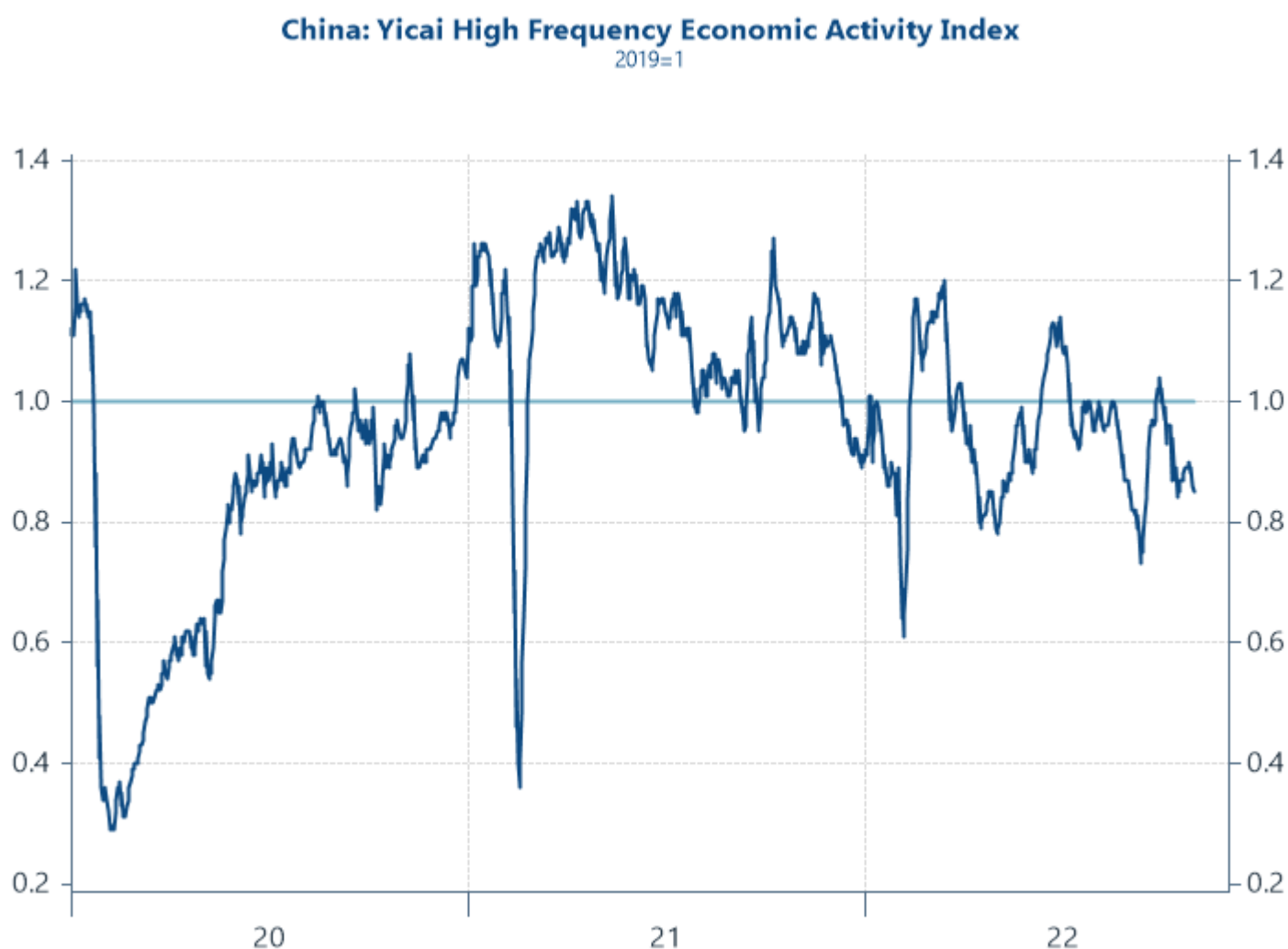


Sources: JP Morgan, Ministry of Finance Japan/Haver Analytics

## China's economic activity

China's economy continues to be constrained by its zero-COVID policy as well as by imbalances in its property sector. The latest Yicai high frequency economic activity index bears testimony to this underlying weakness. The index is constructed using daily high-frequency data in the fields of transportation, energy and the environment, consumption and trade, along with gauges of business and consumer confidence. The index is based to equal 1 in 2019 when economic activity was arguably closer to trend. But as chart 5 below suggests, it has languished below 1 for most of 2022 so far suggesting that growth has been below trend for much of this year.

Chart 5: The Yicai High Frequency Economic Activity Index

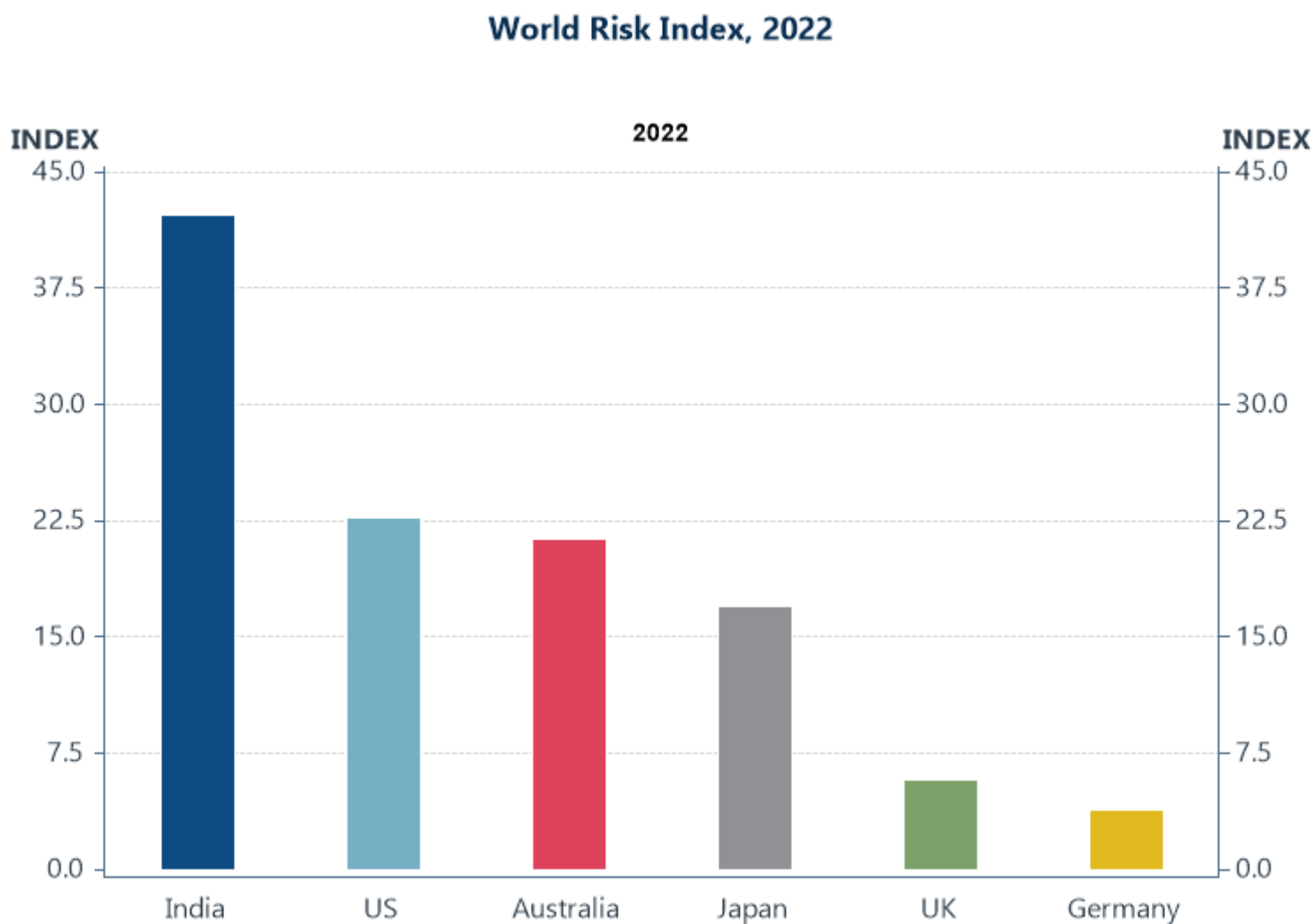


Source: Yicai Media Group/Haver Analytics

## Global risks

The Institute for International Law of Peace and Armed Conflict at Ruhr University Bochum has published an index that measures disaster risk arising from extreme natural events and the negative consequences of climate change as well as the vulnerability of society. The latest data for 2022 suggest that Germany and the UK have relatively low levels of risk compared with, say, the US and Australia. Several developing economies in Asia, including India, typically have higher risks (see chart 6 below).

Chart 6: World Risk Index in 2022 for selected economies



Source: Inst for Peace Preservation/Int Humanitarian Law/Haver Analytics

## ABOUT THE AUTHOR

Haver Analytics is pleased to bring Andrew Cates's commentaries on the state of the global economy to its clients.

Andy Cates has more than 25 years of experience forecasting the global economic outlook and in assessing the implications for policy settings and financial markets. He has held various senior positions in London in a number of Investment Banks including as Head of Developed Markets Economics at Nomura and as Chief Eurozone Economist at RBS. These followed a spell of 21 years as Senior International

Economist at UBS, 5 of which were spent in Singapore. Prior to his time in financial services Andy was a UK economist at HM Treasury in London holding positions in the domestic forecasting and macroeconomic modelling units.

He has a BA in Economics from the University of York and an MSc in Economics and Econometrics from the University of Southampton.

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For more information about these data, included data codes and DLXVG3 chart files, please email [sales@haver.com](mailto:sales@haver.com) and mention Charts of the Week.

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