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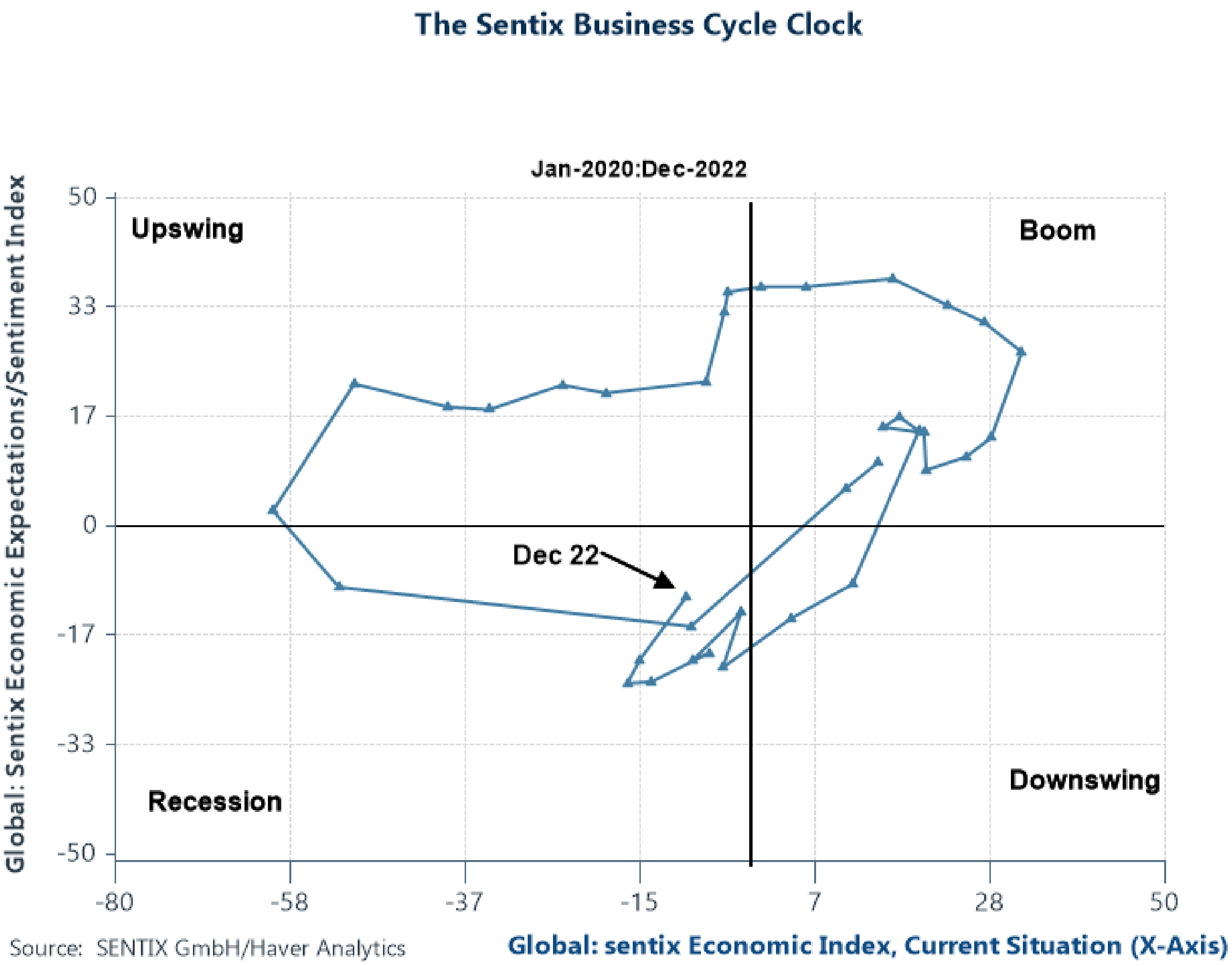
Financial markets have remained on inflation alert and on recession watch in recent weeks and our charts this week should offer some fresh perspective on both themes. Specifically, we look at the recession signals from the December sentix survey (chart 1); at how ebbing capacity pressures in the latest ISM survey are signalling good news for US inflation (chart 2); and at the good news on the inflation front that's already being conveyed by the global dataflow (chart 3). Otherwise the negative impact on the US housing market from the Fed's tightening campaign is placed in some context (in chart 4). Euro area financial balances are then also put into some context relative to the recession threat facing the region (in chart 5). Finally, the spotlight has recently turned to China as its policymakers start to relax their previously-rigid COVID restrictions. Heading into this news, however, the evidence this week on the trade front was quite grim (chart 6).

The global business cycle

This week's sentix surveys of investor expectations continued to convey a high probability of a global recession outcome in the period ahead. This is illustrated by our business cycle clock in chart 1 below showing the current situation component from the global aggregation of this sentix survey plotted against the expectations component. When (as now) both components are in negative territory a recession is implied. Encouragingly, however, the latest survey also signalled a less severe recession outcome compared to the November survey.

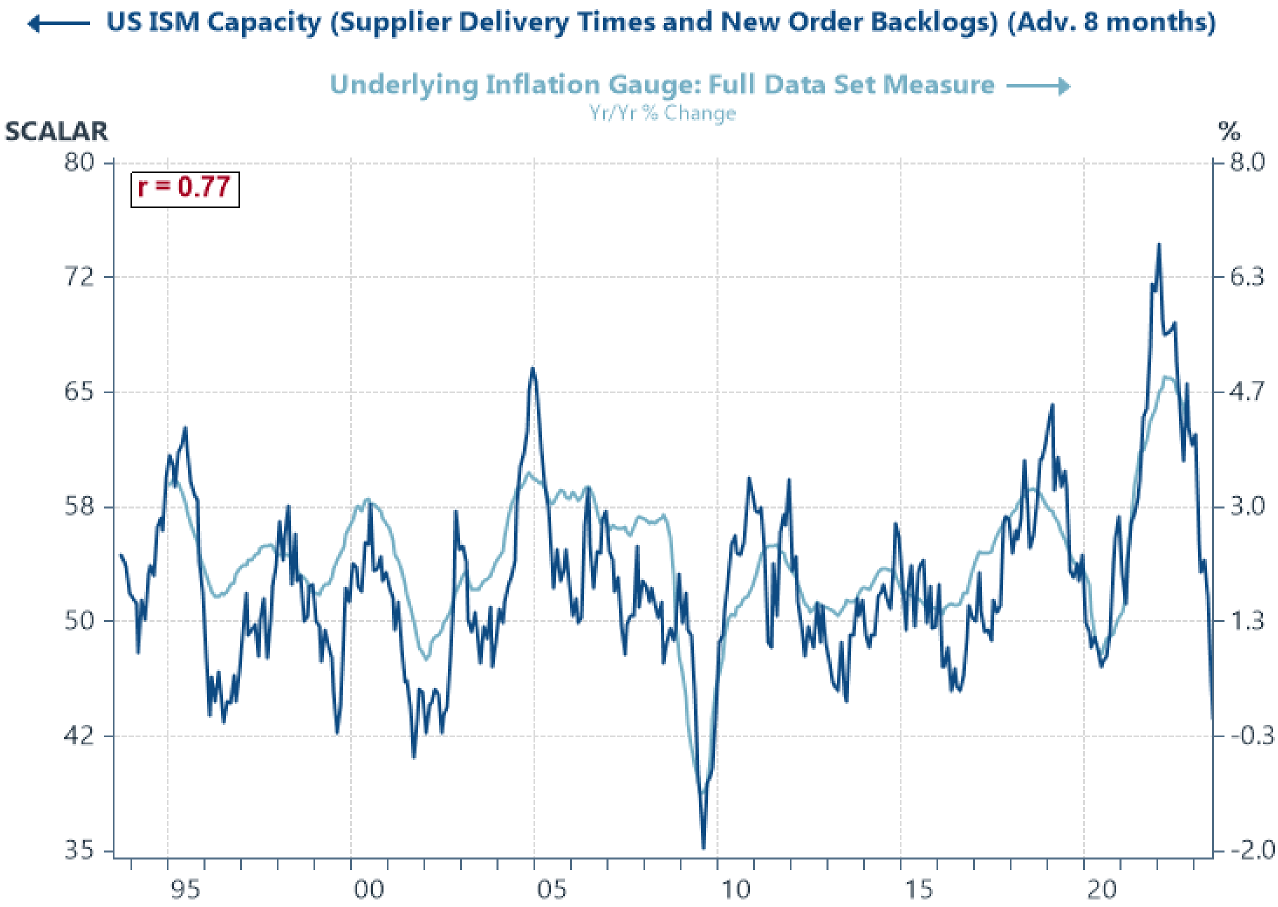
Chart 1: The sentix business cycle clock



US capacity pressures

One reason for that recent relative improvement in this survey might be related to inflation. Financial markets have certainly priced in a more benign inflation outlook in the US in recent weeks. In truth the data can be cut both ways on this issue at present but ebbing energy prices and improving supply-side fundamentals are clearly sending some inflation-friendly signals at present. The capacity signals in the latest US ISM survey and how these square with underlying inflationary pressures offer some evidence for this (chart 2).

Chart 2: US ISM capacity pressures and the New York Fed's underlying inflation gauge

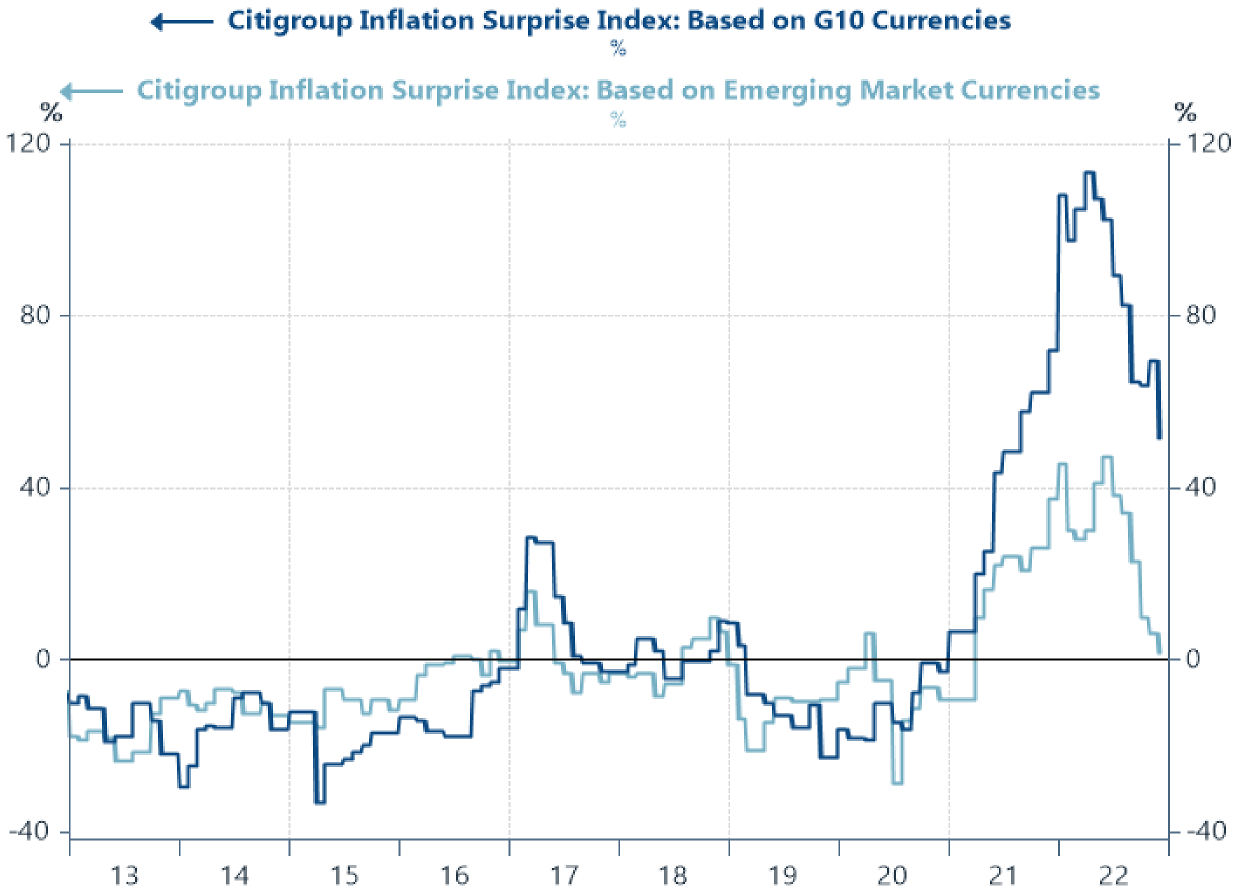


Source: Federal Reserve Bank of New York/Haver Analytics

Global inflation surprises

Incoming data from other major developed and developing economies have also offered a more sanguine picture of the global inflation scene. Citigroup's inflation surprise indicators, for example, suggest a trend toward fewer positive data surprises (relative to consensus forecasts) and more negative surprises has taken hold in the past few weeks.

Chart 3: Citigroup's inflation surprise index for developed and developing economies

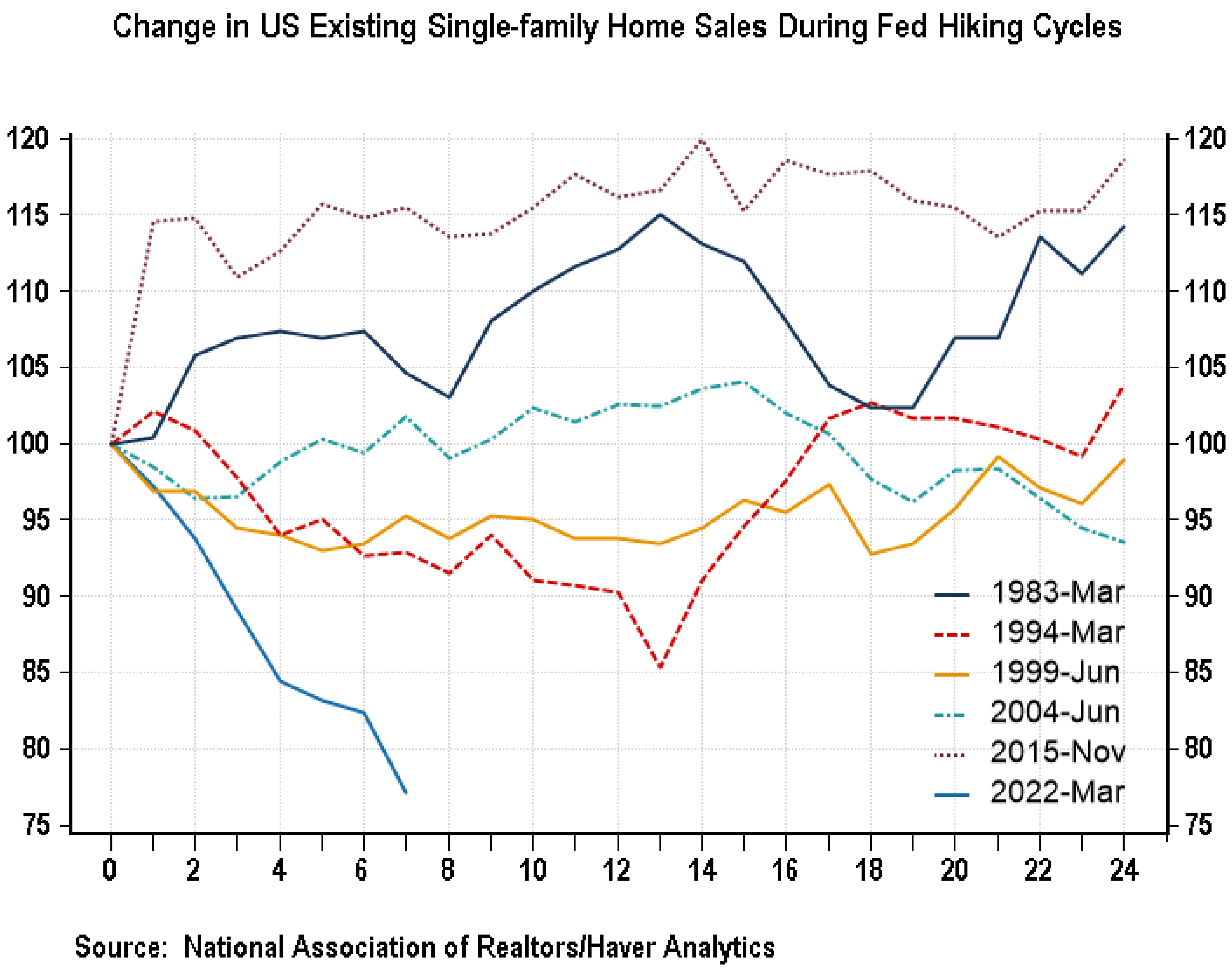


Source: Citigroup/Haver Analytics

The US housing market

The impact of the Fed's recent tightening campaign on the US housing market has been severe. That's the message from chart 4 below which shows the evolution of existing home sales from March to October 2022 relative to the change in sales that has unfolded during previous Fed tightening cycles over the past 40 years.

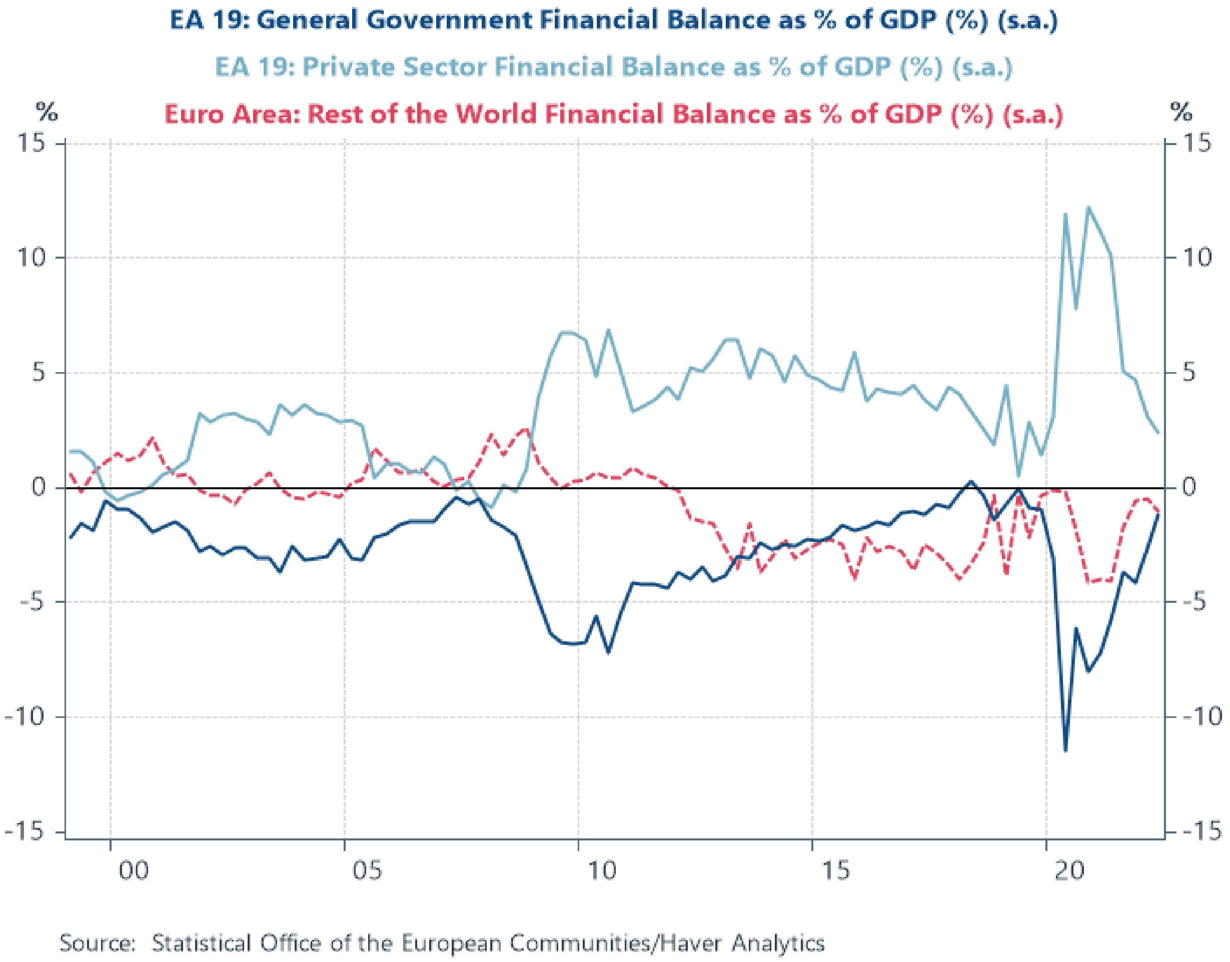
Chart 4: The evolution of US existing home sales during Fed tightening cycles



Savings balances in the euro area

Geopolitical turbulence and – until recently – high energy prices alongside the ECB's campaign to tighten monetary policy are good reasons to expect further economic instability in the euro area in the months ahead. The severity of a recession outcome will partly hinge, however, on underlying savings imbalances. On that score though the euro area – as a whole – is in reasonably good shape. Small financial savings deficits in both the government accounts and the overseas accounts are being financed at present by a reasonably healthy private sector savings surplus, albeit a much reduced one relative to the COVID shocks of 2020 and 2021. This suggests there could be some leeway for orderly balance sheet adjustments that could cushion the region as whole from a severe recession outcome in the period ahead.

Chart 5: Sectoral financial balances in the Euro area



Note: Haver has recently begun to store data for the key sectoral financial balances of the world's major economies in our G10 database.

China's trade with other major economic blocs

Finally, this week's dataflow for China's trade painted a weakening picture, underscoring - ahead of the measures that have just been taken to reopen the economy - the heavy impact that prior COVID restrictions were having on the economy. China's aggregate exports fell by 8.7% y/y in November while imports fell by 10.6%. Exports to the US were especially weak compared with the EU and the ASEAN nations (see chart 6 below).

Chart 6: China's exports to the US, EU and ASEAN

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

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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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