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Written by Andy Cates

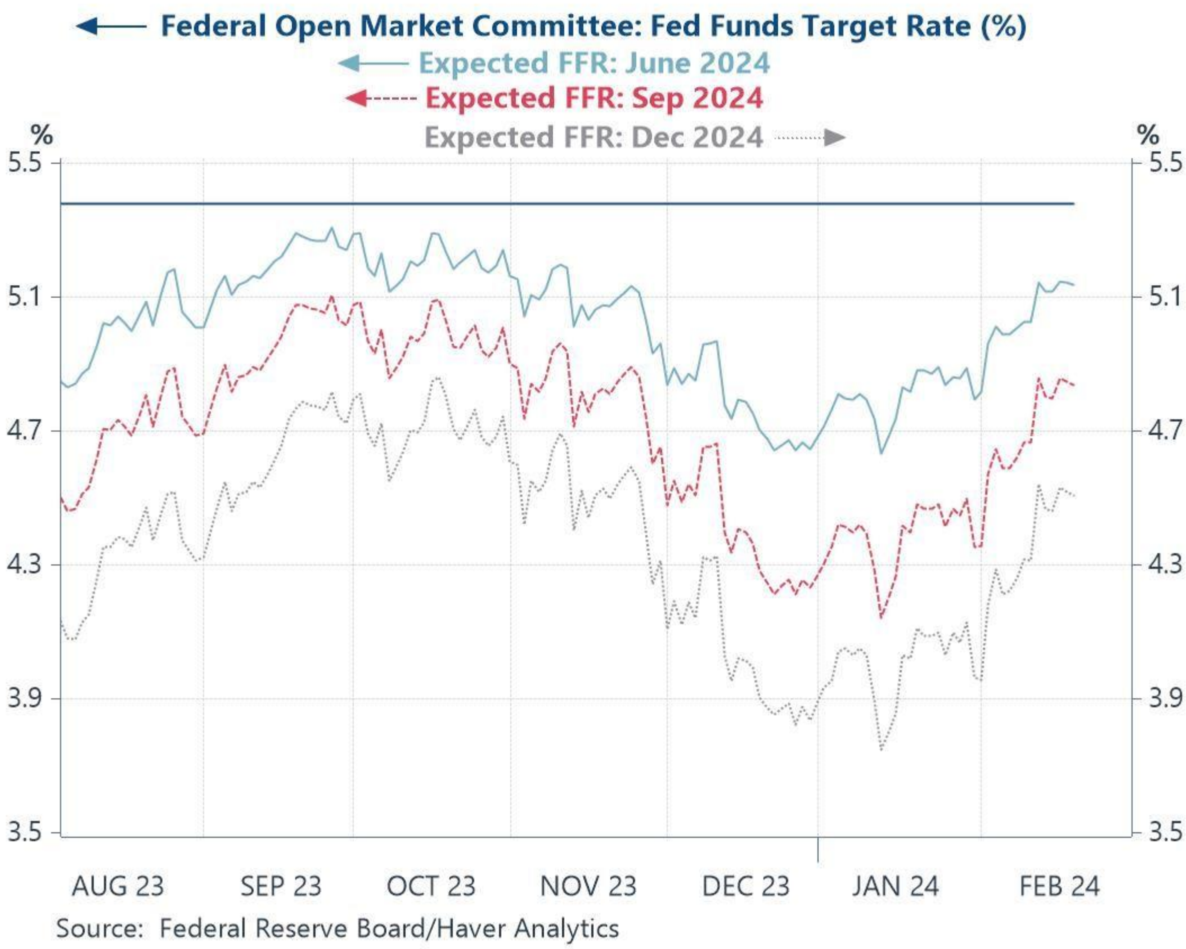
Navigating cyclical and structural headwinds

A quiet economic calendar coupled with holidays in North America and much of Asia have left markets struggling for direction in recent days. This week’s US FOMC minutes revealed concerns among some members about reducing policy rates too soon. And in our charts this week, we first examine the shift in investors' expectations for those policy rates that has unfolded in the early weeks of this year (chart 1). Surprisingly strong US inflation data is one reason why a tighter-for-longer campaign is now under more serious consideration. Seasonal data variability at this time of year, along with recent fluctuations in energy prices (see chart 2), are undoubtedly being weighed by policymakers at present. But so too is evidence suggesting that labour markets have been tight and that wage pressures in the US and Europe have, hitherto, been too strong. Still, as our next two exhibits illustrate, more inflation-friendly labour market data have emerged in recent days (see charts 3 and 4). Against this backdrop, equity markets in most major economies have remained resilient, partly thanks to optimism about new technology (e.g. AI). This optimism may have been further bolstered by this week's trade data from South Korea, which highlighted a resurgence in its semiconductor trade (see chart 5). Lastly, we turn our attention in our final exhibit of the week to the global economy's social progress and the worrisome findings released by analysts from the Social Progress Imperative last week (chart 6).

Market expectations of Fed policy

Fed Funds futures contracts suggest that investors have become considerably less optimistic about the prospects for looser US monetary policy in the year ahead. At the start of January, those contracts suggested the US central bank might reduce the Fed funds rates by nearly 75 basis points by the end of June, by more than 100 basis points by the end of September and by around 150 basis points by the end of the year. Fast forward to today and investors are now assuming only around 25 basis points of interest rate cuts by June, a little more than 50 basis points by September and only around 85 basis points by the end of the year.

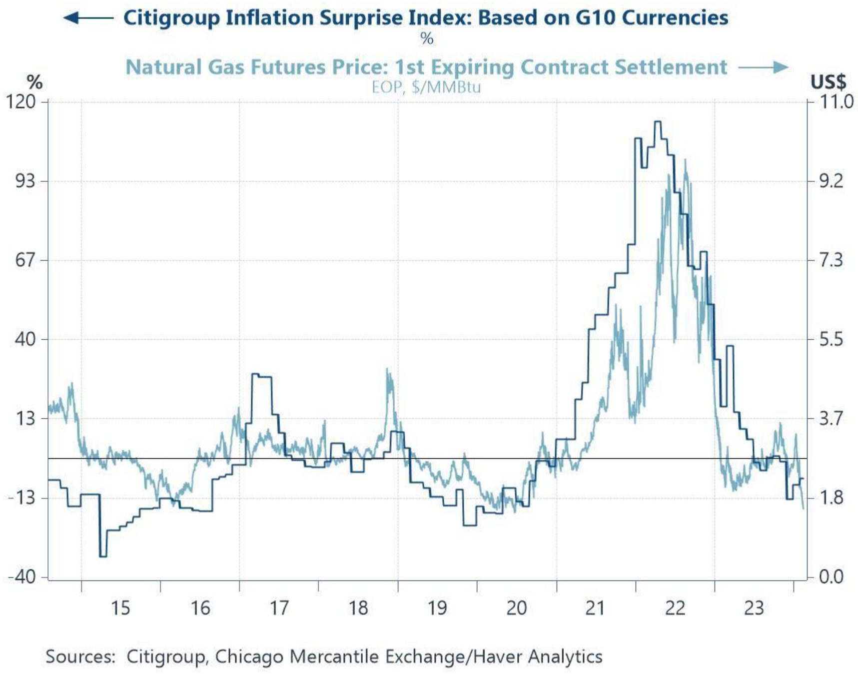
Chart 1: Implied pricing of the Fed's interest rate policy from futures contracts



Inflation surprises and energy prices

Positive inflation surprises coupled with stronger-than-expected growth data have been a principal driver of firming interest rate expectations in the US. Whether those positive surprises persist, however, remains to be seen. On the inflation front, for example, data surprises can often be traced to energy price swings, as evidenced by chart 2 below. And notwithstanding geopolitical turbulence, global energy prices, and natural gas prices in particular, have remained well behaved over the past few weeks.

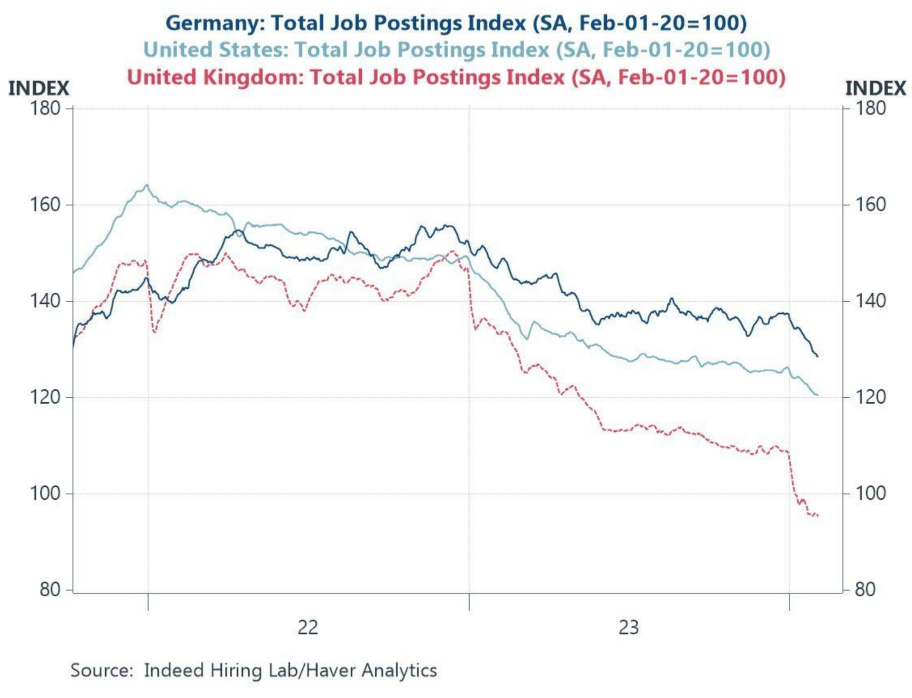
Chart 2: Citigroup's G10 inflation surprise index versus natural gas prices



Labour market activity in the US and Europe

A more pressing concern for central banks in their efforts to manage inflation is, of course, the persistent tightness of labour markets. Across most major economies, recent months have seen strong employment growth, low unemployment rates, and elevated wage inflation. However, evidence from high-frequency indicators, such as job postings, suggests that labour market activity might be starting to slow. Notably, job listings from the employment search firm Indeed have significantly declined in the US, Germany, and especially in the UK since the beginning of the year (see chart 3).

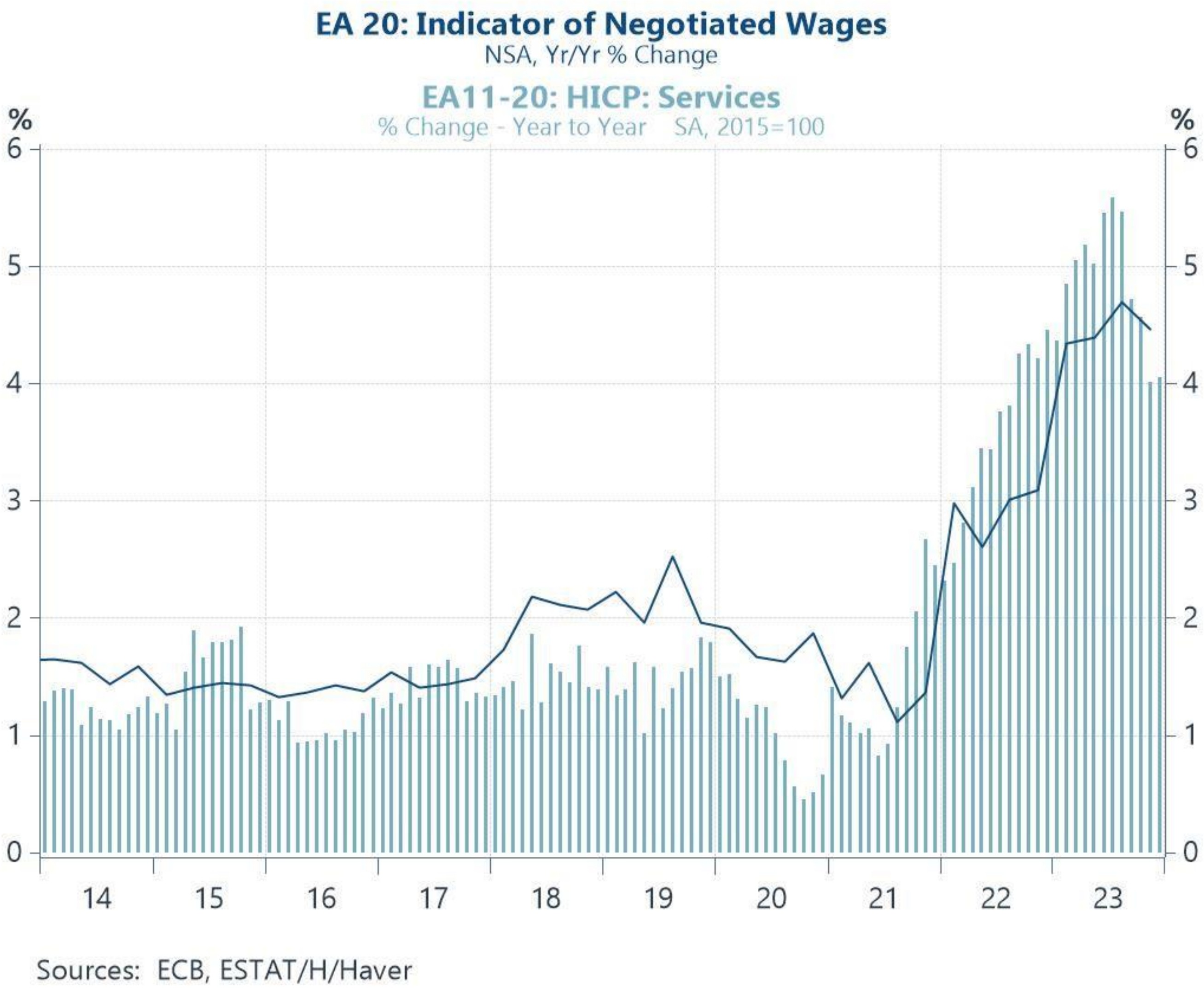
Chart 3: Job postings in the US, Germany and the UK



Wage inflation in the euro area

Another more inflation-friendly data point that emerged from the euro area this week concerned negotiated wage growth. These data specifically slowed to 4.5% y/y in Q4 from 4.7% in Q3 2023 (see chart 4) This is good news for those members of the ECB Governing Council that are concerned about firming wage pressures and its links with service sector inflation. However, at 4.5% y/y, aggregate wage inflation is arguably still too high to be consistent with the ECB's 2% medium-term inflation target.

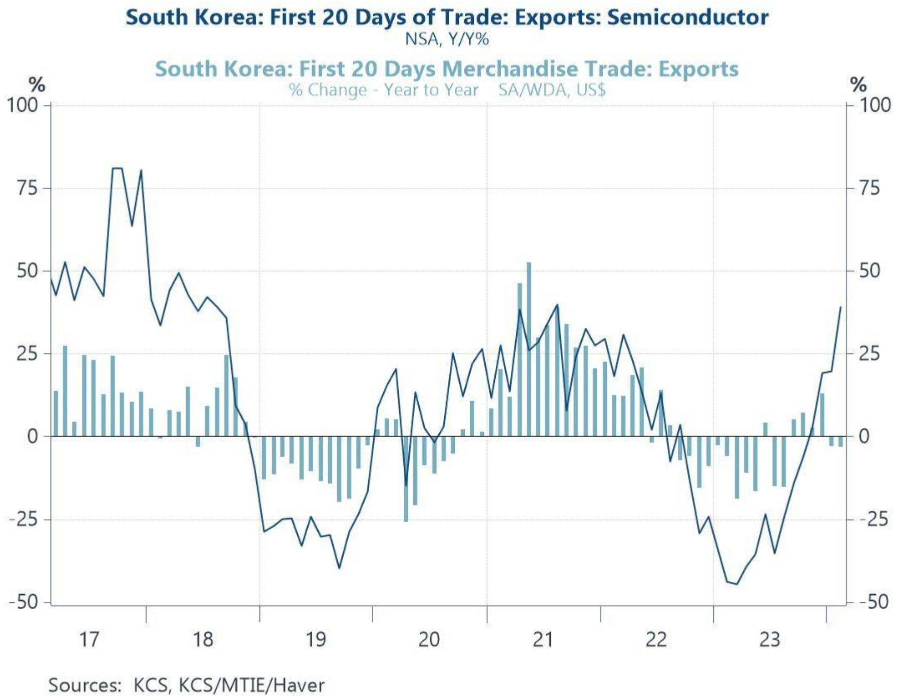
Chart 4: Euro area: Negotiated wage growth versus service sector CPI inflation



Semiconductor trade in South Korea

Other noteworthy data points emerged from South Korea this week and evidence in particular suggesting that semiconductor trade has been perking up. Exports of semiconductors specifically climbed by around 39% y/y in the first 20 days of February, up from 19% y/y in January. That being said aggregate export growth was far more restrained and in fact down by around 3% y/y in the first 20 days of February (and on a working-day adjusted basis).

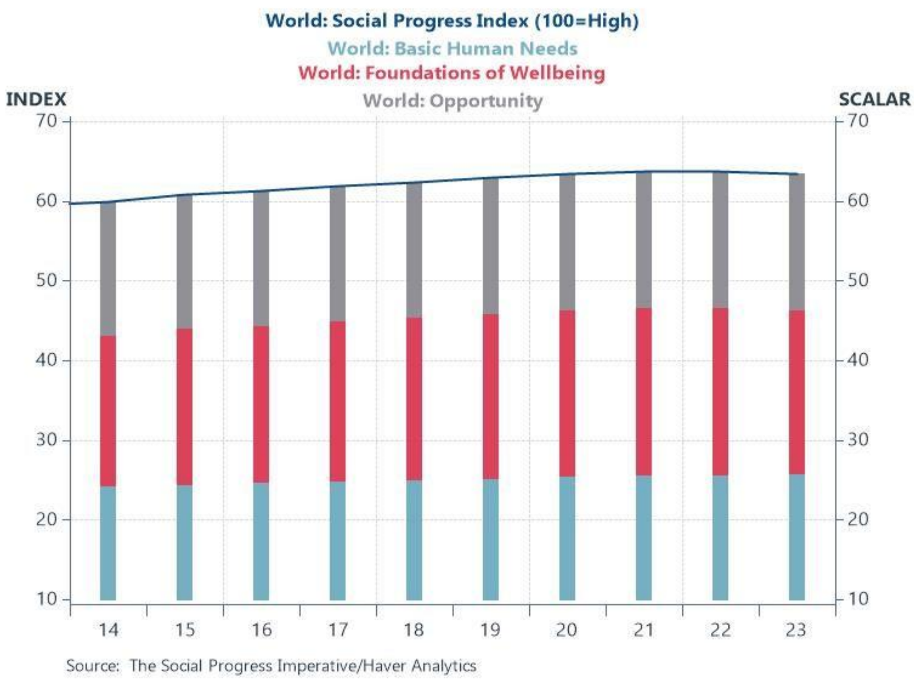
Chart 5: South Korea exports of semiconductors versus total exports



Social progress

In our final chart this week we focus on an index of Social Progress, designed by the Social Progress Imperative. The 2023 update reveals a concerning trend: a global decline in the index for the first time in a decade, signalling a worldwide recession in social progress. This decline could be largely traced to setbacks in Health, Rights, Voice, and Information & Communications. Out of the countries assessed, 61 experienced a notable decrease in their social progress scores in 2023, while 77 showed no improvement. Remarkably, only 32 countries demonstrated any substantial positive progress.

Chart 6: The Social Progress Index and its underlying components



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.

Data featured in this commentary:

Chart 1: Implied pricing of the Fed's interest rate policy from futures contracts
FFEDTAR@DAILY
BFFM24S@FFUTURES
BFFU24S@FFUTURES
BFFZ24S@FFUTURES

Chart 2: Citigroup's G10 inflation surprise index versus natural gas prices
V110CIS@INTDAILY
PZGASF1@DAILY

Chart 3: Job postings in the US, Germany and the UK
J134PI@INTDAILY
J111PI@INTDAILY
J112PI@INTDAILY

Chart 4: Euro area: Negotiated wage growth versus service sector CPI inflation
L025NWQ@EUDATA

Chart 5: South Korea exports of semiconductors versus total exports
N542XTVR@EMERGEPR
W542IX20@EMERGEPR

Chart 6: The Social Progress Index and its underlying components
S001SPI@ESG
S001SPIB@ESG
S001SPIW@ESG
S001SPIO@ESG