Group Economics | 18 August 2023

# Global Monthly

Macro Research Team abn.amro.group.economics@nl.abnamro.com Bill Diviney: +31 6 4778 4657

## A softer landing – but still a landing

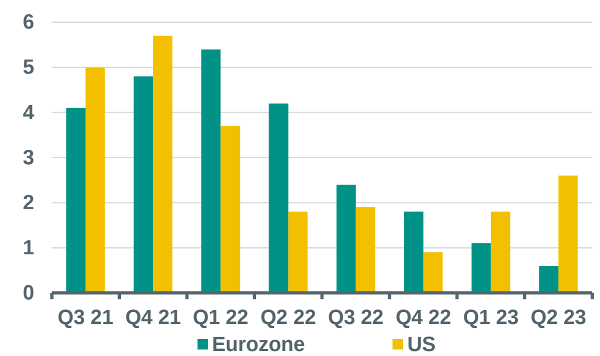
- **The major economies diverged in the first half of 2023, but overall, activity continued to expand, and inflation fell further back – albeit still well above central bank targets**
- **Unexpected strength in the US has led us to drop our call for recession. We still expect tight monetary policy to drive a US slowdown later this year, and to continue to weigh on the eurozone**
- **Even with rate cuts next year, tight monetary policy is likely to limit any post-slowdown rebound**
- ***Spotlight*: Will we face gas shortages in Europe next winter? We take stock of the energy crisis**
- **Regional updates: We expect prolonged weakness in the *eurozone* to eventually push inflation lower, while in *the Netherlands* we expect only modest growth following the technical recession in H1**
- **In the *US*, bank lending standards are not quite as tight as we thought, but will still drive a slowdown**
- ***China's* reopening rebound continues to fade, and headwinds have intensified**

**Global View: Even with a softer landing, tight monetary policy will still weigh heavily on growth**

Since our last Global Monthly before the summer break, the fortunes of the world's major economies have increasingly diverged. The US has exhibited unquestionable and unexpected strength; the eurozone has been weak, albeit not as weak as we thought; and China's post-pandemic recovery has disappointed. How have these divergent trends affected our growth outlook for the remainder of 2023 and into 2024? In terms of the main drivers, our growth outlook is mostly unchanged from June. We continue to expect the headwinds from tight monetary policy and dwindling excess savings to weigh on advanced economies over the coming quarters, while in China, we expect the government to limit the downside of the faltering recovery, but do not see a stimulus bazooka on the horizon. Still, the underlying strength evident in the US economy has led us to revise our recession call to one of a sharp slowdown, while we have made more backward-looking changes to our GDP forecasts for the eurozone and China. Looking beyond the near term expected weakness, we take our signal from where central bank policy is likely headed. Although continued disinflation means that interest rates have likely peaked in most advanced economies, we still expect tight monetary policy to exert a drag on growth for at least the coming year or so. As such, while growth should bottom out early next year, we do not expect a spectacular rebound to follow.

**Economic fortunes have increasingly diverged**

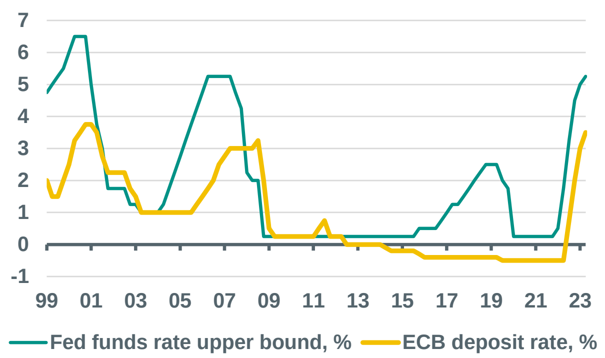
GDP growth, % y/y




Source: Bloomberg, ABN AMRO Group Economics

**Tight monetary policy to become a bigger drag**

Key policy rates, %




Source: Refinitiv, ABN AMRO Group Economics

## Taking stock of H1 2023: Divergent trends, but both growth and disinflation have continued

With Q2 data now in for most major economies, it is clear that despite the strong headwinds, the global economy continued to expand in the first half of 2023, and this was fortunately accompanied by a further decline in inflation. However, this big picture assessment masks major regional differences. The clear star performer has been the US: Q2 GDP growth not only surprised to the upside, with the economy expanding at an above-trend 2.4% annualised pace, but Q1 was also revised significantly higher, to 2% up from 1.3% in the third estimate. The strength was driven by continued resilience on the part of the US consumer, but a rebound in fixed business investment in the second quarter also came as a surprise given the weakness in global trade and manufacturing, and higher financing costs on the back of Fed rate hikes. While we continue to think this degree of strength is unsustainable in the current high rates environment, it nonetheless points to a degree of confidence and resilience in domestic demand that – combined with the continued decline in inflation – we now judge will help the US avoid a recession.

In the eurozone, in contrast, while the mild technical recession of Q4 22-Q1 23 was revised away in the latest GDP report, the details were hardly something to celebrate: domestic demand remained very weak, as consumer spending continues to be weighed by the aftermath of the energy crisis. Ominously, much of the strength was instead driven by falling imports, while export growth was flat over the same period. Finally, in China, the economy continued to normalise and expand following the end of the zero covid policy, but after a strong start of the year the recovery has been much weaker than expected, and the headwinds from the weak property sector and (at best) stagnating global trade and industry appear to be intensifying.

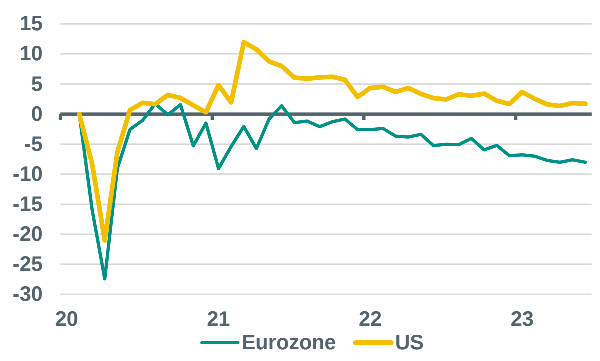
## Why haven't recessions materialised in (most) advanced economies?

With some important exceptions (including here in the Netherlands, as well as Germany), most advanced economies have managed to dodge the recessions that were widely predicted late last year – and in the case of the US, by a very wide margin. What went wrong? (Or right?)

We would highlight two important factors. First is the strength of household and business balance sheets, which appears to be cushioning against the impact of high interest rates for longer than we predicted. This is a much more dominant factor in the US, where stimulus during the pandemic was much more generous, and where the (unsustainably) low savings rate is enabling consumption of goods that is still above the pre-pandemic trend (durable goods consumption specifically is around 6pp above trend). In the eurozone, in contrast, goods consumption has fallen to well *below* trend in recent months, while the savings rate has picked up.

**US goods consumption continues to outperform…**

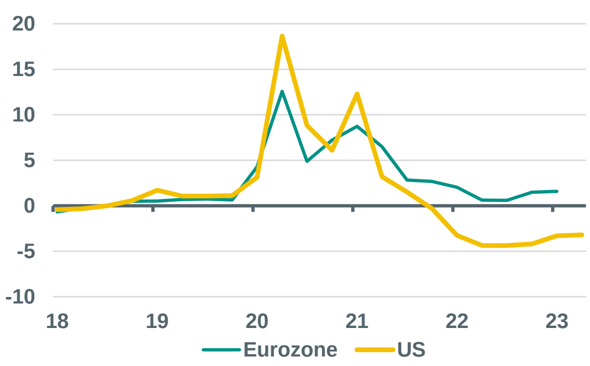
Real retail sales, % difference vs pre-pandemic trend




Source: Refinitiv, ABN AMRO Group Economics

**…driven by an unsustainably low savings rate**

Savings rate, % difference vs pre-pandemic average




Source: Refinitiv, ABN AMRO Group Economics

Something common to both regions, however, is a still relatively low level of bankruptcies – an after effect of the massive support governments provided to businesses during the pandemic. While bankruptcies have risen from the extraordinarily low levels of the recent past, so far they have only normalised rather than soared to recession-like levels.

The second important factor is what has come to be called the 'rolling recession': the idea that different sectors are going into recession at different points in time, but that these sectoral downturns are not sufficiently synchronised for the entire economy to be in a recession. This is arguably particularly evident in the eurozone, where goods consumption and manufacturing have been exceptionally weak, but this has been offset by the post-pandemic recovery in services. This narrative is also applicable to the US: the most interest rate sensitive part of the economy – housing investment – has contracted for eight consecutive quarters. But house building is now a much smaller part of the economy than it was before the global financial crisis, and so the impact of this decline on the broader economy is much smaller than it was back then.

## Forecast update: US recession dodged, but growth to weaken; eurozone to stay weak

The biggest change to our forecasts concerns the US. Our base case no longer foresees a mild recession, but instead a slowdown and a stagnation in output around the turn of the year. The headwinds facing the economy remain very much intact, both from tight monetary policy and the running down of excess savings. As such, we see a slowdown as a question of 'when' rather than 'if'. Even so, we also think the underlying strength of the economy means that it is likely to avoid a simultaneous and broadbased decline in output that would meet the recession definition. Our updated scenario now reflects this, while also keeping the expectation that the headwinds will eventually have a significant dampening impact on economic activity. Indeed, we judge such an outcome as necessary if inflation is to fall fully and sustainably back to the Fed's 2% target.

Previously, we expected the economy to contract over Q4-Q1 23, with a significant rebound in activity in the second half of 2024. We keep this profile broadly intact, but we have 'softened the edges' so to speak: the growth trough is now more shallow, but also the rebound is less pronounced. Net-net, this still means a significant upgrade to our annual average growth forecast for 2024, which goes to 0.9%, up 0.6pp from our most recent projection of 0.3%. Our forecast for 2023 also rises, to a large extent on the upward revision to Q1. See table below.

In the eurozone, we continue to expect a prolonged period of economic sluggishness, with GDP contracting moderately or being close to stagnant during the second half of this year and the first half of 2024. It is possible that volatility in GDP means this does not meet the technical recession definition of two consecutive quarterly contractions. However, the big picture is one of weak domestic demand that is increasingly seeing the effects of the sharp rise in interest rates over the past year. Indeed, activity and survey data published since the start of the summer indicates ongoing weakness ahead. Although GDP growth in 2023Q2 came in higher than expected (at 0.3% qoq) the expansion was largely due to exceptionally high growth rates in Ireland (+3.3%) and Lithuania (+2.8%). Excluding these two outliers, eurozone GDP would have expanded by only 0.1% in Q2. While we lack the full breakdown by expenditure for Q2, domestic demand contracted sharply in 2024Q4 and 2023Q1 (-0.6% and -0.7%, respectively), and our monthly activity tracker suggests domestic demand continued to contract in Q2. These are starkly different trends to those seen in the US, where domestic demand remains strong.

All told, following the upward revision to Q1 GDP growth (to 0.0% from -0.1%) and the upside surprise to Q2 growth, we now expect annual growth to increases to average 0.5% in 2023, up from our earlier estimate of 0.2%. Meanwhile the average for 2024 has edged lower to 0.7% from 0.8%, as we have lowered our forecasts for 2024H1 somewhat.

**Our GDP forecast changes (including Q1 23 revisions) for the US and the eurozone**

| | 2023 | | | | 2024 | | | | Annual average | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | 2023 | 2024 |
| US | 2.0 | 2.4 | 1.8 | 0.0 | 0.0 | 1.1 | 1.4 | 2.0 | 2.0 | 0.9 |
| *Old* | *1.3* | *1.9* | *-0.4* | *-1.3* | *-0.7* | *1.2* | *2.0* | *2.6* | *1.4* | *0.3* |
| Eurozone | 0.0 | 0.3 | -0.1 | -0.2 | 0.1 | 0.3 | 0.5 | 0.5 | 0.5 | 0.7 |
| *Old* | *-0.1* | *0.1* | *-0.2* | *-0.2* | *0.1* | *0.7* | *0.5* | *0.5* | *0.2* | *0.8* |

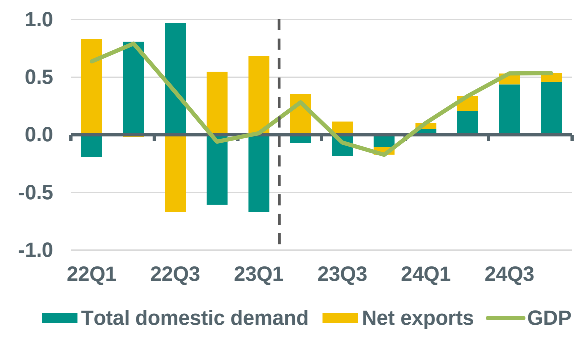
Note: Quarterly numbers are q/q saar for the US, q/q sa for the eurozone. Source: Refinitiv, ABN AMRO Group Economics

## Unemployment still expected to rise modestly in both the US and the eurozone

A key part of our updated forecasts – and critical to fixing the inflation problem – is that despite the growth upgrades, we still expect modest rises in unemployment in advanced economies over the coming quarters. In some countries, such as in Germany and the UK, the unemployment rate has already begun rising, and elsewhere labour market tightness has eased significantly. Even in the US, which has a particularly strong labour market, employment growth has come down markedly, and the job vacancy to unemployed ratio has fallen from a peak of 2.0 to 1.6 as of June, retracing a half of the rise seen since the pandemic (in 2019, the ratio averaged 1.2). With wage cost pressures elevated and demand expected to weaken (in the US) or to stay weak (eurozone), we expect this to trigger increased layoffs and reduced hiring. However, the starting point of extreme labour market tightness means that we are unlikely to see the kind of large scale layoffs we normally see in a downturn. While wage growth looks to have peaked, it remains elevated and above levels consistent with 2% inflation. A modest rise in unemployment should help to ease wage pressures, and in turn help to bring inflation fully back to 2% targets.

**EZ: Domestic demand contracted sharply over Q4-Q1**

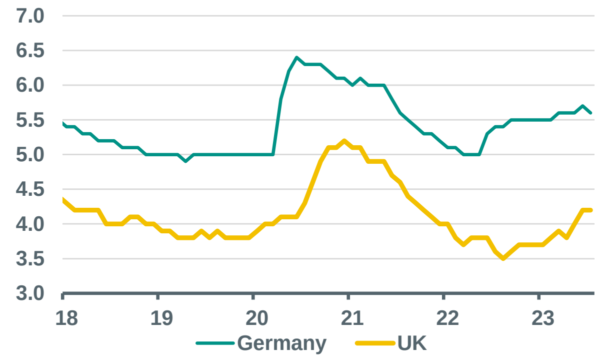
pp contribution to % q/q GDP growth




Source: Refinitiv, ABN AMRO Group Economics

**Unemployment is already rising in Germany and the UK**

Unemployment rate, %




Source: Bloomberg, ABN AMRO Group Economics

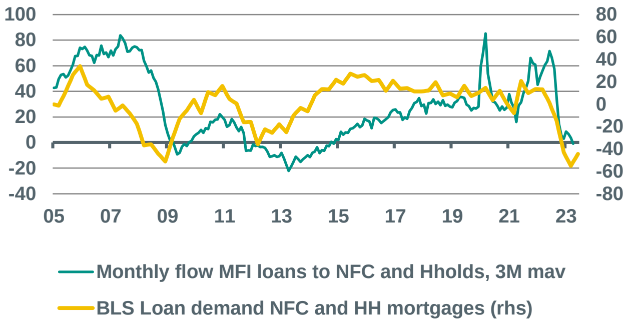
Regarding China, following disappointing Q2 and monthly activity data, we already cut our annual growth forecasts for 2023 and 2024 last month, to 5.2% (from 5.7%) and 4.8% (from 5.0%), respectively. The reopening rebound in services and consumption has faded since Q1, while headwinds from slowing external demand and property have intensified, and extreme weather in the summer has added to these headwinds. Further impacting confidence and sentiment is the scarring from previous stringent policies (Zero-Covid, regulatory crackdown). With the July data generally disappointing and signs of distress in the property sector ongoing, risks remain tilted to the downside, even though the PBoC continues with piecemeal monetary easing and the government is stepping up targeted support in line with our expectations.

## Why we still expect a sharp slowdown in the US, and continued weakness in the eurozone

With advanced economies proving to be resilient despite the surge in interest rates over the past year, it is reasonable to doubt whether high interest rates will have a dampening impact on activity going forward. However, monetary policy works famously with 'long and variable lags' – taking up to 4-5 quarters for the impact to be felt. What makes things even more complicated with this rate hike cycle is that there are reasons to expect lags could be shorter, as well as longer. Lags could be shorter, because financial markets move to price in rate hikes long before they happen – leading for instance to much higher mortgage rates even before central banks started raising interest rates. On the other hand, the lag for other parts of the economy could be longer, due first to the longer-term fixing of interest rates (eg. in many countries, the typical mortgage is fixed for a longer time period than in the past), but also due to the strength of household and business balance sheets, which has likely insulated many from the impact of rate rises so far. Indeed, on the latter point, as mentioned previously we think excess savings in the US especially have enabled the consumption binge to go on longer than we thought.

**EZ: Interest rate hikes are hitting loan growth**

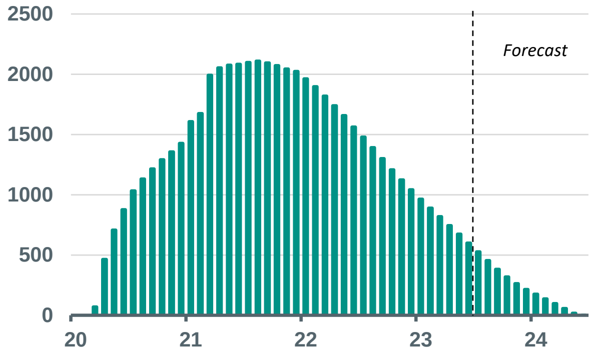
EUR bn balance: higher-lower




Source: Refinitiv, ABN AMRO Group Economics

**US: Falling excess savings to weigh on consumption**

Post-pandemic excess savings, USD bn




Source: Refinitiv, ABN AMRO Group Economics

However, we do see increasing signs of an impact from rate rises in the form of falling loan growth, and we expect that impact to intensify over the coming quarters. In the US, we estimate that excess savings are close to being exhausted (for lower income households that is likely already the case), and that this will drive a correction in goods consumption. Higher rates are also leading to a further tightening in bank lending standards, even if that tightening may not be as stark as suggested by the headline surveys (see US section). Finally, real interest rates have been depressed until relatively recently by elevated inflation. As inflation falls further, this will continue to push real rates higher, even without further rate rises by central banks. Indeed, this is one of the main reasons we expect the ECB and the Fed to start cutting rates in March next year.

## What are the prospects for recovery next year?

While we expect advanced economies to be weak over the coming quarters, we continue to expect a modest recovery in the second half of 2024. This is likely to be helped by modest interest rate cuts by central banks, as well as a recovery in real incomes as inflation falls back. Both of these naturally therefore hinge on the inflation outlook, which itself depends on labour market tightness continuing to ease. Without this, central banks will be unable to lower interest rates and tight monetary policy will continue to constrain economic growth.

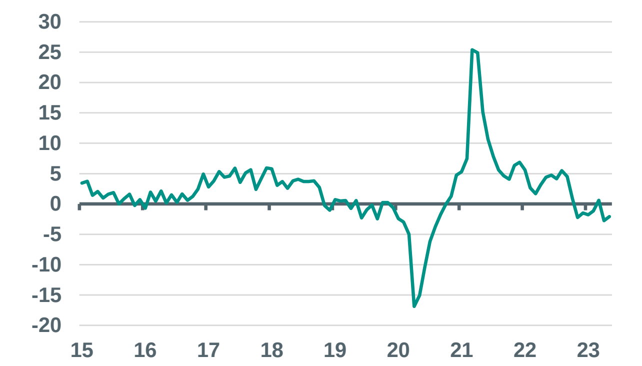
**Real rates could rise even without further rate hikes**

% US 2y yield minus 2y breakeven inflation rate


Source: Bloomberg, ABN AMRO Group Economics

**Global trade volumes in a year-long slump**

% y/y




Source: Refinitiv, ABN AMRO Group Economics

Even in our base case of continued falling inflation and modest rate cuts, monetary policy is likely to remain relatively restrictive even into 2025. We expect the fed funds rate to fall back to 3.50-3.75% by the end of 2024, and the ECB deposit rate to fall to 2.00% – still above estimated neutral rates for the US and the eurozone. Given this, we do not expect a sharp rebound in growth next year, but instead a return to near-trend rates of growth. This will also likely keep a lid on any recovery in global trade and industry, which has been in a downturn for almost a year now. In the near-term, we do expect a bottoming out in global manufacturing, but we do not foresee a strong recovery until sufficiently low inflation enables central banks to cut rates back to neutral levels – likely in 2025. (Bill Diviney, Aline Schuiling, Arjen van Dijkhuizen)

# Spotlight: Gas price higher, but not back to last year's peak

Moutaz Altaghlibi – Economist | moutaz.altaghibli@nl.abnamro.com
Philip Bokeloh – Senior Economist | philip.bokeloh@nl.abnamro.com

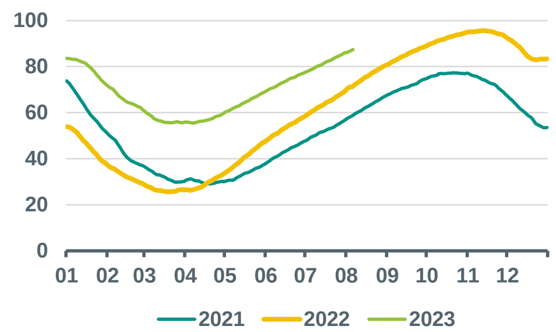
- **Bigger gas buffers limit the risk of shortages. The gap in gas supply left by Russia has been largely filled by other gas suppliers**
- **Share of renewables in power supply increasing fast, and energy consumption has fallen**
- **Our base case sees gas prices staying higher than before the energy crisis, but even in a negative scenario, we do not expect prices to return to levels we saw at the height of the crisis last summer**

### REPowerEU plan implemented successfully

The energy crisis triggered by the Russian invasion of Ukraine hit the European economy very hard last year. Surging gas prices following the halt of Russian supplies to the continent raised energy bills to unprecedented levels, pushing up inflation and curbing purchasing power. In this note we revaluate the situation for the upcoming winter. We think Europe has become less vulnerable to gas supply challenges than in early 2022 thanks to a series of measures. The REpowerEU plan is raising gas storage capacity, diversifying gas supplies with a bigger role for Liquified Natural Gas (LNG), and increasing the share of renewable power in the electricity mix along with supporting clean fuels such as hydrogen. Europe has made much progress on these fronts last year. The gap left by the decline in gas imported from Russia has been largely filled by other suppliers. Gas buffers are ample. So ample, that LNG tankers are sometimes turned away to Asia to serve customers there. Furthermore, the amount of energy generated from solar and wind has risen steadily, and gas consumption has fallen as energy is used much more efficiently.

**Gas storage levels in EU are rapidly increasing**

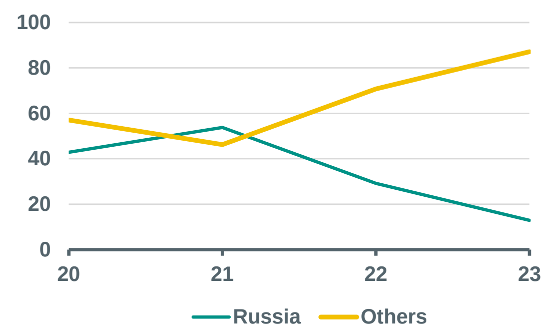
Percentage of storage capacity




Source: AGSI, ABN AMRO Group Economics

**EU has reduced its dependency on Russian gas**

Percentage of gas imports




Source: European Commission, ABN AMRO Group Economics

### Fears of a repeat of last year's price spikes are largely unwarranted

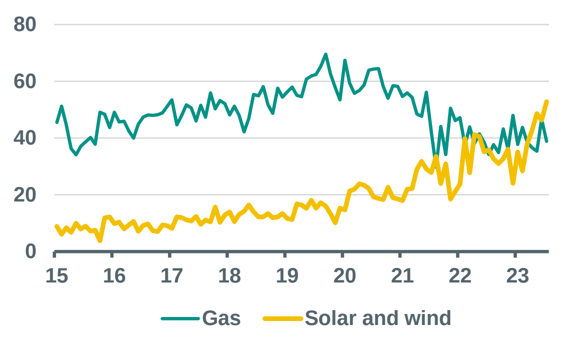
Despite the massive progress Europe has made, there is no guarantee that gas prices will remain low. After all, Russia is still responsible for an eighth of the European Union's imports. Should Moscow suddenly decide to turn off the gas tap, Europe will indeed have a problem. Europe was fortunate last year that gas demand in Asia was relatively low due to lockdown measures in China. With China's economy recovering, demand is rising again. Finally, gas demand last winter was as much as 7% lower than in the previous five years due to relatively mild temperatures. Assuming more normal winter temperatures, gas demand will be higher in the coming winter. By themselves, these concerns are justified. However, there are caveats to this as well. First, it is not in Russia's interest to further restrict exports as long as there is no gas pipeline to China, and given that northern Russian LNG ports are poorly accessible in winter. Second, the latest data from China do not suggest a strong rebound in the economy; on the contrary, the economy continues to languish (see our China story). Third, the hot summer did not cause a price shock this year, despite the increased demand for energy-intensive cooling associated with heat waves.

**There are also potential tailwinds for energy supply**

Last year's struggles with gas supplies came at a very unfortunate time. For a start, France's nuclear plants were operating at a low level as maintenance work was being carried out. Now that these are largely behind us, France's nuclear plants can once again supply more energy.[1] Another potential tailwind for energy supply comes from hydropower. The series of hot summers meant that water levels were low in Europe last year. As a result, hydropower generated a fifth less energy than usual. Periods of drought and heavy rainfall this summer show that climate change is also taking its toll this year. But, assuming weather conditions normalise somewhat, hydropower generation is likely to see a further recovery, which could partially offset any additional gas demand due to a colder winter. Finally, some countries have also resorted to a less desirable alternative from a climate perspective: coal. After the problems with gas supplies from Russia, some European countries decided to keep coal plants open longer than previously planned. This was a relatively simple measure, given the production capacity was already there. There are several reliable producers, so security of supply is guaranteed. And its price is relatively low. Still, it would be unwise to stick with this stopgap measure for long. It is bad for the environment and would damage the international credibility of Europe's climate ambitions. Other countries could point to this as justification for less ambitious climate goals than they would otherwise have.

**Renewables are replacing gas in the Netherlands**

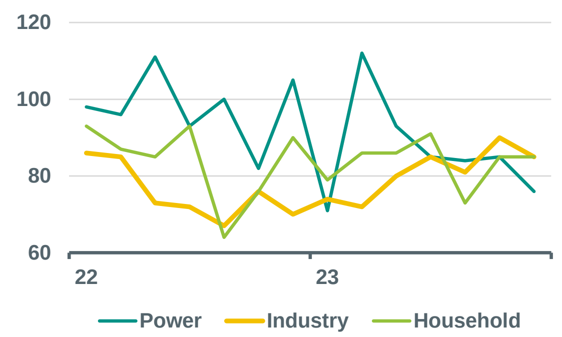
Percentage share in power generation




Source: Ember, ABN AMRO Group Economics

**All sectors in EU are cutting gas demand**

Natural Gas demand as percentage of 2019-2021 average




Source: Bruegel, ABN AMRO Group Economics

**Base case sees higher prices than pre-crisis, but no return to last year's peak – even in a negative scenario**

All things considered, we think gas prices will be higher next winter than in the years prior to the energy crisis. With Russia largely out of the supply picture, the gas market is tighter than before. Moreover, precautionary measures in the form of higher buffers also means additional costs and a higher average price level. We assume a TTF average year ahead price of 55 EUR/MWh for the second half of 2023 and 60 EUR/MWh for 2024. Furthermore, LNG has gained a larger share in the overall gas mix. This means that gas prices are more sensitive to global changes in supply and demand. Prices may therefore fluctuate more frequently than prior to the crisis, as we have seen in the past year when maintenance of gas plants in Norway and the US led to short-term price fluctuations. But on a global market the amplitude of price fluctuations will turn out smaller. In global markets there are more available supply alternatives, with more competition among suppliers and higher flexibility in adjusting production and access spare capacities. In a negative scenario where Russia halts all remaining exports to Europe, our estimates put the TTF year ahead average price at 110 EUR/MWh in 2023 and 150 EUR/MWh in 2024 (around 100-150% higher than in our base case). The higher level of gas prices will prop up inflation, albeit to a limited extent. As a rule of thumb a rise in gas prices of 10% raises total HICP inflation by around 0.1 percentage point. This would hit household purchasing power and put a brake on consumption growth. However, the burden of higher gas prices will be shared more evenly. While gas price ceilings and subsidies are about to expire, government support will probably be more focussed on low income households living in houses with a low energy label. Energy-intensive companies and sectors facing foreign competitors with access to cheaper energy sources will also suffer from higher gas prices, which could also lower economic growth somewhat.

[1] Traditionally, these plants run mostly on uranium from Niger. Since the military coup in Niamey, their supply is less assured. However, this need not cause immediate problems, as France has spread the risks in recent years by increasingly sourcing uranium from other countries.

# Eurozone: Economic weakness to continue for a while

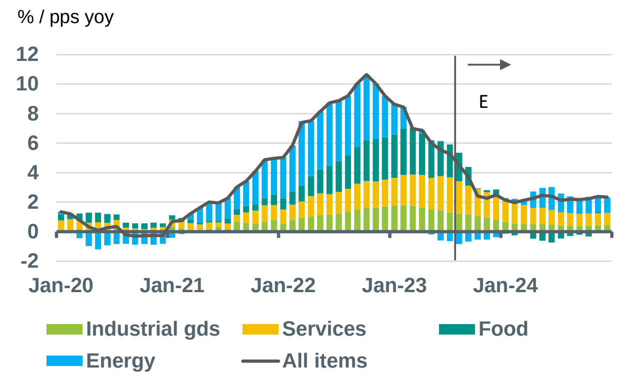
Aline Schuiling – Senior Economist | aline.schuiling@nl.abnamro.com

- **GDP was stronger than expected in 2023Q2, but the underlying picture remains one of ongoing economic sluggishness**
- **Core inflation has not yet convincingly declined, though it is only specific parts of services inflation that are still rising; the rest of the HICP components have already peaked and are slowing**
- **The ECB has probably ended its rate hike cycle. We expect rate cuts to start in March 2024**

Eurozone 2023Q2 GDP came in higher than expected at 0.3% qoq. Meanwhile, the Q1 result was revised higher, to 0.0%, up from -0.1%. This means that the eurozone was not in technical recession after all last winter, and GDP only contracted in one quarter (-0.1% qoq in 2024Q4). Despite the somewhat better than expected outcome for GDP in 2023H1, we still expect a considerable period of economic sluggishness, with GDP probably contracting moderately or being close to stagnant during H2 2023 and H1 2024 (see also the first chapter of our Global Monthly). Activity and survey data published since the start of the summer suggests further weakness to come. For instance, the manufacturing and the services PMIs each have persistently fallen over May-July, while business confidence also declined during these three months. We think that the unprecedented sharp interest rate hikes by the ECB since the middle of last year will continue to feed through to the economy in the coming quarters. Moreover, there are early signs that labour market conditions are turning and that the labour market has become less tight (eg. the vacancy rate has declined). Indeed, the ECB report of its main findings from contacts with non-financial companies mentions that 'many contacts continued to find recruitment challenging given shortages of various skills, but there were also a few signs of increasing slack in some parts of the labour market.'

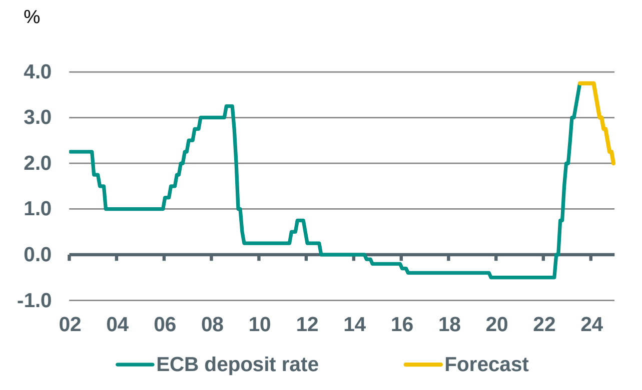
Headline inflation has continued to fall in recent months, but the core rate has stagnated, with declining goods price inflation offset by rising services inflation. Within services. an upward base effect in transport services was a major factor pushing total services inflation higher, while other parts of services inflation (e.g. communication services, personal care) have declined in recent months. Looking ahead, we expect disinflation to continue during the rest of this year. Core inflation will probably decline more slowly than headline inflation, but core inflation should also ease, as demand for goods and services will weaken and wage growth is expected to slow, which will also reduce the inflation rate of labour intensive services.

**Inflation and contribution from main components**




Source: Revinitiv, ABN AMRO Group Economics

**Rate cuts by the ECB to kick off in March 2024**




Source: Refinitiv, ABN AMRO Group Economics

The ECB raised the deposit rate by 25bp in July, as was widely expected, while also signalling that a pause in the rate hike cycle was likely. Our base line has remained that the peak in the deposit rate (3.75%) has now been reached and that there will be no further hikes. We have shifted our expectation of a pivot in the policy stance a few months forward and now expect a rate cut cycle to begin in March 2024, instead of our earlier forecast of December of this year (see also here). This largely reflects the resilience in services inflation and the labour market up until now. We expect a series of rate cuts will kick off in March 2024, and we continue to see the deposit rate at 2% by the end of next year.

# The Netherlands: Economy in a technical recession

Aggie van Huisseling – Economist | aggie.van.huisseling@nl.abnamro.com
Jan-Paul van de Kerke – Economist | jan-paul.van.de.kerke@nl.abnamro.com

- **The Dutch economy contracted by 0.3% qoq in Q2 and by 0.4% in Q1**
- **We expect yearly growth to slow down from 4.5% in 2022 to 0.5% in 2023, and to 1.1% in 2024**
- **Inflation is declining, but underlying price pressures remain firm**

The Dutch economy contracted by 0.3% qoq in Q2. As GDP had already contracted by 0.4% qoq in Q1, the Netherlands was in a technical recession during the first half of the year. Eurozone GDP expanded by 0.3% qoq in Q2, which means that the Dutch economy underperformed the eurozone aggregate. Still, in level terms, the Dutch economy has significantly outperformed the eurozone aggregate in the post-pandemic period (see graph below).

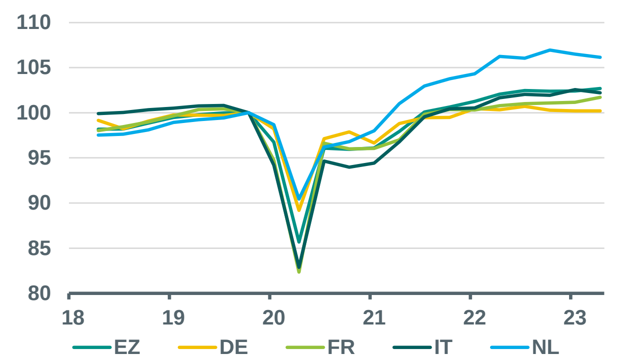
The contraction in Q2 was driven by the trade balance and private consumption. Weak external demand – particularly for (chemical) industrial goods – caused total exports to contract while imports grew. This resulted in a negative contribution from the trade balance to GDP. As the growth outlook for the eurozone remains subdued, the trend of weak demand for Dutch exports will most likely remain in place for the remainder of the year. Meanwhile, inflation has weighed on private consumption, causing it to contract by 0.2% qoq in Q1, with a much bigger fall of 1.6% in Q2. Although goods consumption contracted, services spending prevented a bigger drop in overall consumption. Some services sectors might still benefit from post-pandemic catch-up spending. We expect consumption to grow modestly over the rest of the year, as household spending is supported by a still exceptionally tight labour market, accelerating wage growth, and government support such as the energy allowance and the (energy) price ceiling.

Despite weak growth prospects and higher financing costs, fixed investment stood out, expanding by 1.3% qoq in Q2. The strength in investment was driven by infrastructure investment, transport and machinery, and sustainability related investment such as insulation, solar panels and heat pumps. Housing investment, by contrast, contracted on the back of the cooling housing market.

Despite the technical recession, the Dutch economy remains resilient; the labour market is still tight and bankruptcies – although increasing in recent months – are still below 2019 levels. Still, we expect growth to remain sluggish in the coming quarters. We have slightly adjusted our growth forecasts from 0.7% to 0.5% for 2023, and from 1% to 1.1% for 2024

**Strong post-pandemic recovery**

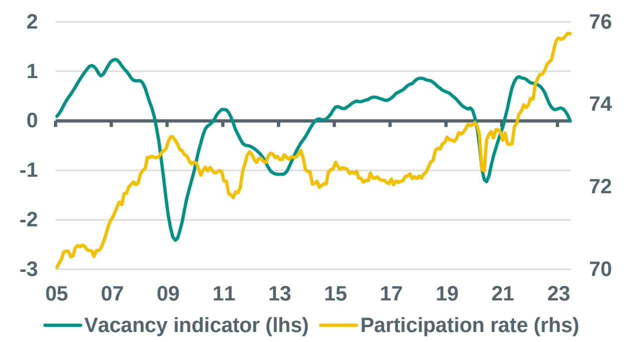
Index 2019 Q4 = 100




Source: Refinitiv, ABN AMRO Group Economics

**Tight labour market but weaker vacancy expectations**

%. Vacancy indicator 0 = neutral. +3% = positive, -3% = negative




Source: Refinitiv, ABN AMRO Group Economics

Inflation is on a downward trend. It fell to 5.3% in July, down from an annual average of 11.6% in 2022. Core inflation has remained more elevated and stood at 7.2% in July. Inflation is expected to come down further over the coming year and to average 4.8% in 2023, and 3.5% in 2024. As such, inflation is unlikely to return to 2% any time soon. Wage growth is likely to remain historically elevated, as workers seek to make up for past declines in real wages amid a very tight labour market (see graph). This is expected to last at least until the end of next year, putting upward pressure on labour-intensive services and goods. As the Dutch economy continues to have a positive output gap, the risk is that inflation remains well above the eurozone total for a considerable period. Some cooling of the economy, particularly domestic demand – as seen in the latest GDP figures – is therefore welcome.

# US: Still going strong

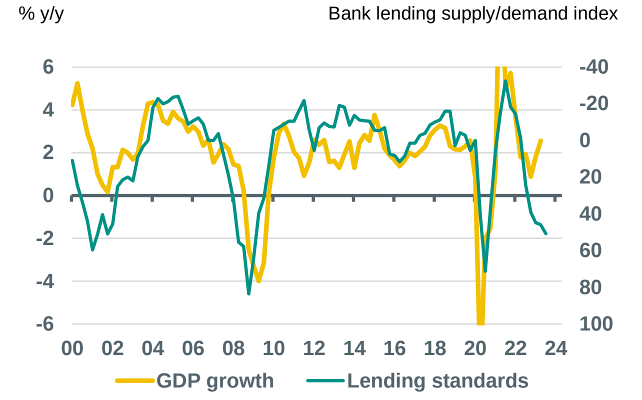
Bill Diviney – Senior Economist | bill.diviney@nl.abnamro.com

- **The US economy has exhibited remarkable resilience over the past half year. We no longer expect a recession, but still expect a slowdown, which eventually will bring inflation back to 2%**
- **The Fed's latest Senior Loan Officer Opinion Survey suggests bank lending standards may not be quite as tight as they seemed. This may help explain part of the recent resilience in the economy**
- **We continue to think interest rates have peaked, with rate cuts to start next March**

As we describe in this month's Global View, we have revised our call for a mild recession, and instead now look for a sharp slowdown and a stagnation in the economy later this year. In the meantime and moving into Q3, the economy has continued to perform well above expectations. In particular, nominal retail sales and industrial production surprised to the upside in July, rising 0.7% m/m and 1.0% m/m respectively. At the same time, payrolls growth cooled further, and housing investment indicators pointed to some renewed weakness; being the most interest rate sensitive part of the economy, housing may be feeling the effects of a rebound in mortgage rates. All told, though, the economy has started Q3 on a very solid footing, with the Atlanta Fed's GDPNow tracker for Q3 standing at an eye-popping 5.8% q/q saar; this will doubtless be revised significantly lower as more data for Q3 comes in (our forecast is for a more mundane 1.8% expansion), but it underlines the continued remarkable performance of the US economy. Against this backdrop, disinflation also continued in July, with both the headline and core CPI rising by a benign 0.2% m/m, and annual core inflation continuing to edge down. We expect falling wholesale used car prices to deliver another relatively benign core CPI reading for August, which should give the FOMC the confidence to keep policy on hold when it next meets in September.

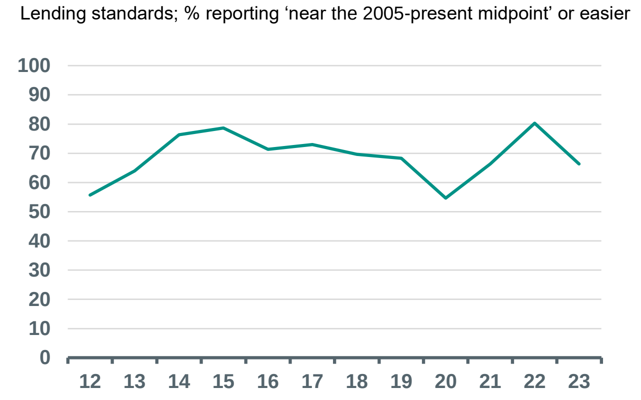
One of the key drivers of our mild recession call was that the Fed's Senior Loan Officer Opinion Survey (SLOOS) pointed to a major tightening in bank lending standards following the failure of some regional banks earlier this year. The July survey suggested a continued tightening of lending standards. However, another important aspect of the July survey was the special questions asking banks to report on the *level* of lending standards, not merely the *change* (as the headline results show). Because lending standards were highly accommodative in the post-pandemic period, even the sharp tightening in standards since then has left lending standards not all that tight after all (see chart below). The tightening in standards is weighing on credit growth, which will eventually hit economic activity, and this is a key reason we expect a sharp slowdown in the economy. However, we no longer think this will be enough to push the economy into a recession.

***Change* in lending standards suggests deep recession**




Source: Refinitiv, ABN AMRO Group Economics

**But the *level* of lending standards is not so tight**




Source: Federal Reserve, ABN AMRO Group Economics

What does this more benign macro outlook mean for the Fed? Had inflation stayed at the elevated readings of the turn of the year, we would have been minded to expect another round of rate rises and to simply delay the onset of recession. However, the fact that the recent resilience has been accompanied by further disinflation suggests that a significant slowdown will likely be sufficient to cool inflation – though it may take longer to fall back to 2% than we currently expect. We judge that falling inflation is still likely to trigger rate cuts starting next March. As Fed Chair Powell and NY Fed President Williams have repeatedly stated, falling inflation will continue to push real interest rates higher if the Fed does not cut rates next year. Rate cuts would therefore be aimed at keeping policy steady rather than providing stimulus to the economy.

# China: The outlook darkens

Arjen van Dijkhuizen – Senior Economist | arjen.van.dijkhuizen@nl.abnamro.com

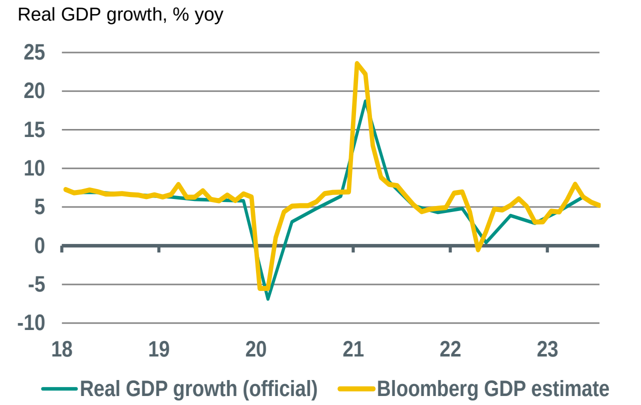
- **Reopening rebound fades, headwinds from slowing external demand and property have intensified**
- **We cut our annual growth forecasts for 2023 and 2024 last month; risks stay tilted to the downside**
- **PBoC continues with piecemeal monetary easing, further targeted support being rolled out**

The reopening rebound in services/consumption has faded, headwinds from slowing external demand and property have intensified, and extreme weather has added to the growth headwinds. Further impacting confidence and sentiment is the scarring from previous stringent policies (Zero-Covid, regulatory crackdown), as well as ongoing signs of distress in property. Given all of these headwinds, we already cut our growth forecasts last month for 2023/2024, to 5.2% (from 5.7%) and 4.8% (from 5.0%) respectively, following disappointing Q2 GDP and activity data (also see **here**).

### Macro data for July generally weaker than expected

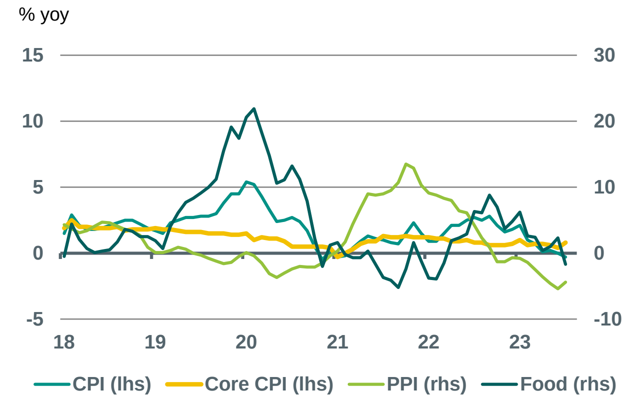
Monthly activity data for July continued to disappoint. Annual growth of industrial production, retail sales and fixed investment slowed further, and the unemployment rate edged up marginally to 5.3% (June: 5.2%). The PMIs still point to a divergence between weak manufacturing and stronger services, but the gap is narrowing (with services PMIs coming down). Annual growth of exports and imports has fallen deeper into contraction territory, confirming weakness in both external and domestic demand. Monthly lending volumes dropped sharply in July, following a stronger than expected seasonal uptick in June. Cooling housing sales and (delayed) mortgage prepayments are pushing down net mortgage lending. With consumer confidence still weak and ongoing signs of distress amongst developers (with spillovers to the financial sector), as illustrated by recent problems of large developer Country Garden Group, the property sector is not out of the woods yet. Residential housing sales slowed to 0.7% yoy in July (June: 3.7%), while property investment fell even deeper into contraction territory.

**Yoy growth up in Q2 on base effect; qoq growth was weak**




Source: Bloomberg

**Headline inflation turned negative, but core inflation picked up**




Source: ABN AMRO Group Economics, Refinitiv

### Headline inflation turned negative in July driven by food prices, but core inflation actually picked up

Headline CPI inflation came in at -0.3% yoy in July, the first negative number since February 2021. While this reflects weak domestic demand, food (particularly pork) and energy prices are key drivers as well. A strong base effect from a 26% jump in pork prices one year ago drove annual food price inflation into negative territory in July (-1.7% yoy). By contrast, core CPI rose to a six-month high of 0.8% yoy, although remaining relatively low. Meanwhile, producer price inflation (which correlates well with oil prices) seems to have bottomed out, with the annual decline easing to -4.4% yoy in July.

### PBoC continues with piecemeal easing, government rolls out more targeted support

In mid-August, the PBoC cut its 1-year medium-term lending rate by another 15bp to 2.50%, and the 7-day reverse repo rate by 10bp, to 1.80%. This was coupled with a large liquidity injection into the banking system, and with measures to support the yuan'. We expect piecemeal monetary easing (mini rate cuts, bank RRR cuts) to continue. Also, Beijing is taking more measures in an attempt to stabilise the property sector, restore confidence among consumers/firms/investors, and support demand. We still think they will refrain from rolling out a 'credit bazooka', partly because they want to keep leverage in check, particularly in the property sector, and given constraints regarding local government finances and shadow banking.

## Key views on a page

**The global economy continues to send mixed signals, with weakness in the eurozone contrasting with strength in the US, while China's post-covid rebound has disappointed. The global economy continues to expand, but the impact of monetary tightening is being increasingly felt, with manufacturing and housing already in a downturn. Tightening credit conditions are weighing on bank lending, which we expect to eventually hit other sectors of the economy. Headline inflation has continued to trend lower, but tight labour markets are keeping core inflation elevated. Central bank policy rates are peaking, but even with rate cuts starting in the first half of next year, we expect monetary policy to stay restrictive throughout 2024. This will keep a lid on any post-slowdown rebound.**

| Macro | Central Banks & Markets |
|---|---|
| **Eurozone** – Q2 GDP came in higher than expected at 0.3% qoq. Meanwhile, the Q1 result was revised higher, to 0.0%, up from -0.1%. This means that the eurozone was not in technical recession after all last winter. Despite the somewhat better than expected outcome for GDP in 2023H1, we still expect a considerable period of economic sluggishness, with GDP probably contracting moderately or being close to stagnant during H2 2023 and H1 2024. Core inflation has stagnated in recent months, but should decline during the second half of the year, also because wage growth is expected to slow down. | **ECB** – The ECB raised the deposit rate by 25bp in July, as was widely expected, while also signalling that a pause in the rate hike cycle was likely. Our base line has remained that the peak in the deposit rate (3.75%) has now been reached and that there will be no further hikes. We have shifted our expectation of a pivot in the policy stance a few months forward and now expect a rate cut cycle to begin in March 2024 instead of our earlier forecast of December of this year. We expect that a series of rate cuts will kick off in March 2024, and we continue to see the deposit rate at 2% by the end of next year. |
| **The Netherlands** – Dutch GDP contracted by 0.3% qoq in Q2. Following a 0.4% qoq contraction in Q1 this means that the Dutch economy was in a technical recession during the first half of the year. Dutch GDP is expected to grow by 0.5% in 2023 (revised downward from 0.7%). We expect growth to remain sluggish in the coming quarters on the back of high rates and lower external demand. The Dutch economy remains resilient; the labour market is still tight and bankruptcies – although increasing in recent months – are still below 2019 levels. We expect inflation (HICP) to average 4.8% in 2023 and 3.5% in 2024. | **Fed** – The FOMC raised rates by 25bp in July, and the Committee made clear that it is open to further tightening. We think July was the last hike of the cycle, and that benign core inflation readings will give the FOMC the confidence to keep policy on hold in September. We continue to expect the Fed to start cutting rates from next March. Even without a recession, falling inflation will push real rates higher, and Fed officials have signalled that this would be inconsistent with the FOMC's goals. Even with rate cuts starting next year, monetary policy is expected to remain restrictive throughout 2024 and even into 2025. |
| **UK** – Disinflation has resumed, providing some relief to the Bank of England, but upside inflation risks remain significant given that wage growth has continued to accelerate. Demand has also shown signs of rebounding, with GDP growth surprising to the upside in Q2. At the same time, unemployment has started rising, and we expect a softening in demand to dampen wage growth over time. The economy is expected to broadly stagnate over the coming year or so, weighed by tight monetary policy. | **Bank of England** – The MPC stepped back down to a 25bp hiking pace in August, following the surprise 50bp hike in June. We now expect one further 25bp hike in September, and for this to mark the end of the rate hike cycle. However, the BoE is in full data-dependent mode, and UK macro data has been erratic over the past few months. We do not expect rate cuts until next May, and there is a risk that rate cuts get delayed even further, if inflation proves to be more persistent. |
| **US** – We now expect a slowdown and stagnation rather than a mild recession. Growth was unexpectedly strong in Q2, and revised sharply higher for Q1. Meanwhile disinflation has continued, while wage growth has peaked. We now judge that a slowdown and a period of below trend growth will be sufficient to return inflation back to target. But there is significant uncertainty over where inflation will settle in the medium term given labour shortages and residual supply/demand imbalances in the economy. Inflation falling sustainably back to target hinges on a rise in unemployment over the coming year. | **Bond yields** – US economic resilience led to another bond sell-off, pushing yields to new highs as the market pushes out rate cuts, but on the front-end of the curve, we have seen a pullback in the pricing of additional rate hikes. Our central bank view implies that the short end of the curve will soon need to price in rate cuts for 2024 which will lead to a major drop in short-term rates. Both 10y Treasury and Bund yields are also expected to fall on the back to a flight to quality as economies weaken. However, the decline will be to a lesser extent than the short-end of the curve, leading both curves to bull-steepen by end 2023-34. |
| **China** – The reopening rebound in services/consumption has faded, headwinds from slowing external demand and property have intensified, and extreme weather adds to these headwinds. Further impacting confidence/sentiment is the scarring from previous stringent policies (Zero-Covid, regulatory crackdown), as well as ongoing signs of property distress. We already cut our growth forecasts for 2023/2024, to 5.2% (from 5.7%) and 4.8% (5.0%), respectively. Although piecemeal monetary easing and targeted support continues, as expected, risks remain tilted to the downside. | **FX** – We forecast a modest upside of the US dollar versus the euro for the following reasons. We expect rate cuts by the Fed and the ECB next year. Whereas most of the Fed rate cuts we foresee are anticipated by the market, our expected rate cuts for the ECB are not. If our views play out euro should weaken. Moreover, the speculative positions in the euro are extremely large. Our forecasts are 1.08 (end 2023) and 1.05 end 2024. |

## Main economic & financial market forecasts

| | GDP | | | | Inflation | | | | Policy rate | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2021 | 2022 | 2023 | 2024 | 2021 | 2022 | 2023 | 2024 | 2021 | 2022 | 2023 | 2024 |
| Eurozone | 5.4 | 3.4 | 0.5 | 0.7 | 2.6 | 8.4 | 5.2 | 2.2 | -0.50 | 2.00 | 3.75 | 2.00 |
| Netherlands | 6.2 | 4.4 | 0.5 | 1.1 | 2.8 | 11.6 | 4.8 | 3.5 | | | | |
| UK | 7.6 | 4.1 | 0.4 | 0.4 | 2.6 | 9.0 | 7.6 | 3.3 | 0.25 | 3.50 | 5.50 | 4.75 |
| US | 5.9 | 2.1 | 2.0 | 0.9 | 4.7 | 8.0 | 4.1 | 2.6 | 0.25 | 4.50 | 5.50 | 3.75 |
| China | 8.4 | 3.0 | 5.2 | 4.8 | 0.9 | 1.9 | 0.5 | 1.8 | 3.80 | 3.65 | 3.40 | 3.40 |

| | 2022 | 17/08/2023 | Q3 23 | 2023 | 2024 | Energy | 2022 | 17/08/2023 | Q3 23 | 2023 | 2024 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| US Treasury | 3.83 | 4.29 | 4.10 | 3.85 | 3.25 | | | | | | |
| German Bund | 2.57 | 2.70 | 2.55 | 2.40 | 1.90 | Brent - USD/bbl* | 85.91 | 84.12 | 85 | 85 | 95 |
| EUR/USD | 1.07 | 1.09 | 1.09 | 1.08 | 1.05 | WTI - USD/bbl* | 80.26 | 80.39 | 80 | 80 | 90 |
| USD/CNY | 6.99 | 7.29 | 7.20 | 7.00 | 6.60 | TTF Gas - EUR/MWh* | 88.63 | 54.73 | 50 | 55 | 60 |
| GBP/USD | 1.15 | 1.28 | 1.26 | 1.25 | 1.28 | | | | | | |

* Brent, WTI: active month contract; TTF: next calender year

| | 2022 | | | | 2023 | | | | 2024 | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **GDP (qoq)** | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Eurozone | 0.6 | 0.8 | 0.4 | -0.1 | 0.0 | 0.3 | -0.1 | -0.2 | 0.1 | 0.3 | 0.5 | 0.5 |
| Netherlands | 0.5 | 1.8 | -0.2 | 0.9 | -0.4 | -0.3 | 0.3 | 0.0 | 0.3 | 0.5 | 0.4 | 0.4 |
| US (saar) | -1.6 | -0.6 | 3.2 | 2.6 | 2.0 | 0.0 | 2.0 | 0.0 | 0.0 | 1.1 | 1.4 | 2.0 |
| UK | 0.2 | -0.1 | 0.1 | 0.0 | 0.3 | 0.4 | 0.3 | 0.5 | 0.5 | 0.6 | 0.6 | 0.6 |
| China (yoy) | 4.8 | 0.4 | 3.9 | 2.9 | 4.5 | 6.3 | 4.5 | 5.4 | 4.5 | 4.9 | 5.1 | 4.8 |
| **Inflation** | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Eurozone | 6.1 | 8.0 | 9.3 | 10.0 | 8.0 | 6.2 | 4.5 | 2.4 | 2.1 | 2.4 | 2.2 | 2.3 |
| Netherlands | 8.9 | 10.4 | 14.1 | 13.0 | 7.2 | 6.3 | 3.2 | 2.6 | 4.4 | 3.6 | 3.1 | 2.8 |
| US | 8.0 | 8.5 | 8.3 | 7.1 | 5.8 | 4.0 | 3.3 | 3.2 | 2.9 | 2.6 | 2.5 | 2.4 |
| UK | 6.2 | 9.2 | 10.0 | 10.8 | 10.2 | 8.4 | 6.8 | 5.0 | 4.5 | 2.8 | 2.9 | 3.0 |
| China | 1.1 | 2.2 | 2.7 | 1.8 | 1.3 | 0.1 | -0.1 | 0.5 | 1.0 | 1.6 | 2.3 | 2.0 |
| **Unemployment** | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Eurozone | 6.8 | 6.7 | 6.7 | 6.7 | 6.6 | 6.4 | 6.6 | 7.0 | 7.1 | 7.2 | 7.1 | 7.1 |
| Netherlands | 3.4 | 3.3 | 3.7 | 3.6 | 3.5 | 3.5 | 3.7 | 3.9 | 4.0 | 4.1 | 4.0 | 4.0 |
| US | 3.8 | 3.6 | 3.5 | 3.6 | 3.5 | 3.5 | 3.6 | 3.8 | 3.9 | 4.2 | 4.4 | 4.5 |
| UK | 3.8 | 3.7 | 3.6 | 3.7 | 3.8 | 4.2 | 4.4 | 4.6 | 4.8 | 4.8 | 4.7 | 4.6 |
| **Policy rate** | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Eurozone | -0.50 | -0.50 | 0.75 | 2.00 | 3.00 | 3.50 | 3.75 | 3.75 | 3.50 | 3.00 | 2.50 | 2.00 |
| US | 0.50 | 1.75 | 3.25 | 4.50 | 5.00 | 5.25 | 5.50 | 5.50 | 5.00 | 4.75 | 4.25 | 3.75 |
| UK | 0.75 | 1.25 | 2.25 | 3.50 | 4.08 | 4.66 | 5.50 | 5.50 | 5.50 | 5.25 | 5.00 | 4.75 |
| China | 3.70 | 3.70 | 3.65 | 3.65 | 3.65 | 3.55 | 3.40 | 3.40 | 3.40 | 3.40 | 3.40 | 3.40 |

Source: Refinitiv, Bloomberg, ABN AMRO Group Economics

## Macro Research Team


**Sandra Phlippen**, Chief Economist | sandra.phlippen@nl.abnamro.com

**Aggie van Huisseling**, Economist | aggie.van.huisseling@nl.abnamro.com

**Aline Schuiling**, Senior Economist | aline.schuiling@nl.abnamro.com

**Arjen van Dijkhuizen**, Senior Economist | arjen.van.dijkhuizen@nl.abnamro.com

**Bill Diviney**, Senior Economist | bill.diviney@nl.abnamro.com

**Jan-Paul van de Kerke**, Economist | jan-paul.van.de.kerke@nl.abnamro.com

**Nick Kounis**, Head of Financial Markets Research | nick.kounis@nl.abnamro.com


## FX & Rates Research


**Georgette Boele**, Senior FX & Precious Metals Strategist | georgette.boele@nl.abnamro.com

**Sonia Renoult**, Rates Strategist | Sonia.renoult@nl.abnamro.com