February Macro Brief

Commercial real estate jitters

February 29, 2024

Accenture Strategy

Macro Foresight

About this document

The monthly brief is intended to inform executive teams, boards and investors on the state of the economy. It has been prepared based on data as of **February 26, 2024**.

Each brief includes a summary of global business-relevant macroeconomic developments, and a set of indicators that track the overall health of the economy, business activity and consumers.

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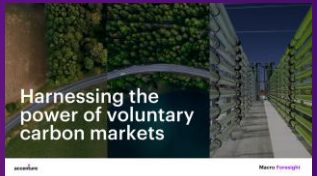

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Executive Summary

Global themes

- **The latest economic activity data signals a broad continuation of trends in recent months, including:**
  - Moderating but still-resilient business activity in the US (including a nascent revival in manufacturing), despite a drop in retail sales
  - Sluggishness throughout Europe, with further activity contraction in Germany and France, but some signs of a turnaround in the UK
  - Softening momentum in China, including ongoing deflation in consumer and producer prices
- **With recent disinflationary impulses from supply chain and energy price normalization now abating, inflation is showing some signs of re-acceleration in the US and Euro area.** This will weaken the Fed and ECB's conviction that inflation is on a steady and durable path back to target and likely delay the timing of potential rate cuts. Higher-for-longer interest rate scenarios therefore become more likely.
- **Concerns about economic spillovers from commercial real estate (CRE) distress came back into focus in February,** as several banks across the US, Europe and Japan reported larger-than-expected CRE losses and stress. For now, these appear to be flash points in an otherwise slow burn process where losses will be realized over a multi-year period without triggering major systemic credit events. But more acute fallout and contagion cannot be ruled out, particularly in scenarios where higher-for-longer rates exacerbate CRE valuation and refinancing pressures.

Regional highlights

Americas

- In the **US,** core inflation is re-accelerating, while CRE-related losses are expected to continue to disproportionately pressure smaller banks and companies
- **Brazil's** economy continues to defy expectations for a slowdown, though large fiscal deficits may hinder inflation stabilization

Europe, Middle East and Africa

- In **Germany,** rising NPLs on CRE loans, coupled with stranded CRE asset risks due to EU climate rules, continue to stress banks
- The **UK** economy is showing promising early signs of recovery from its recent recession
- **Saudi Arabia** enacted additional reforms to attract more foreign companies and talent

Asia-Pacific

- In **Japan,** exposures to US CRE appear concentrated in one major bank and not a systemic risk for the banking sector
- In **Indonesia**, the new President-elect has signaled broad continuity in economic policies, with some scaling up of raw material export bans

Key considerations and priorities for clients

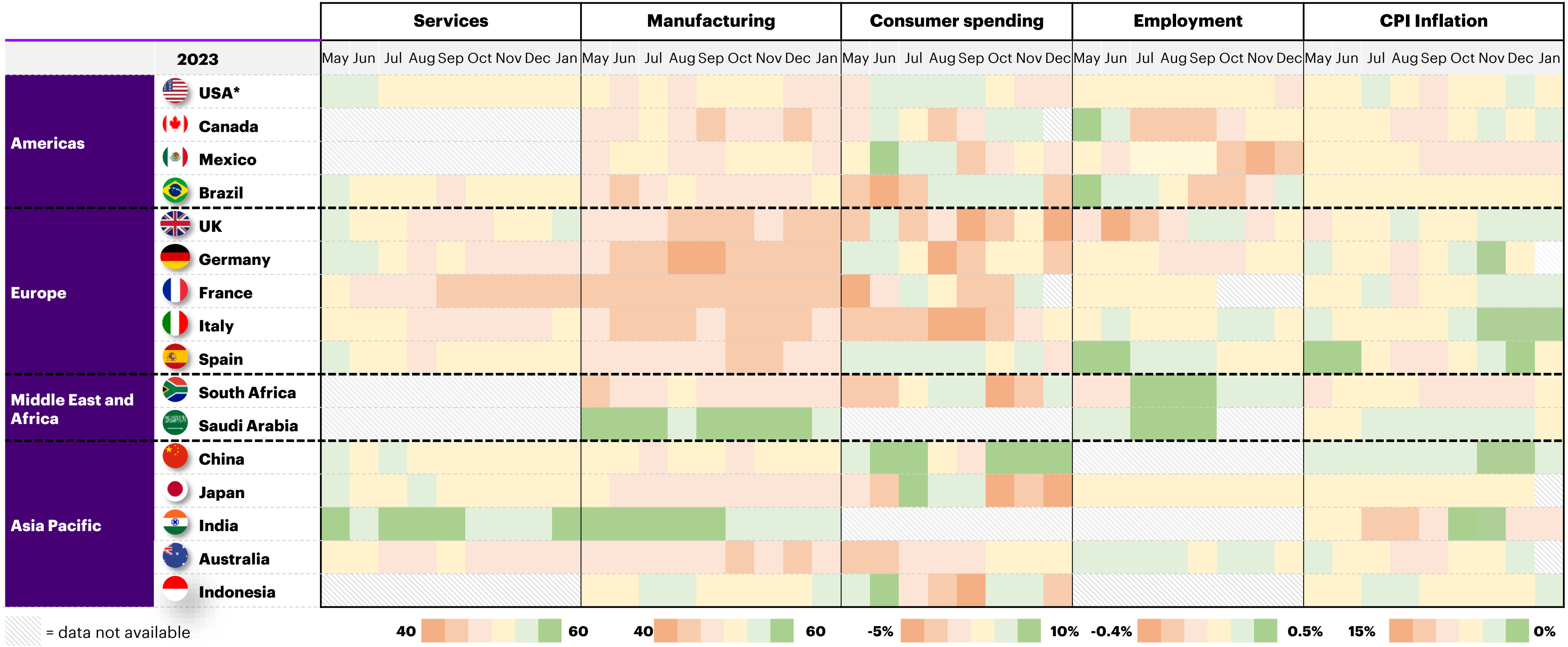
- **Companies must remain vigilant and prepared for the challenges associated with sticky inflation and higher-for-longer rate scenarios, including, among other things:** costlier debt refinancing, valuation pressures, and strong labor bargaining power and wage pressures.
- **Corporates should continue to proactively manage their CRE exposures but also be on the lookout for purchasing opportunities.**
  - For banks, the focus will be on provisioning for losses while also working with CRE owners to restructure debts and avoid defaults
  - Nonfinancial companies must: (1) be prepared for possibility of a credit crunch as balance sheets of CRE-exposed banks continue to come under pressure; and (2) capitalize on opportunities to buy high-quality but distressed office properties as prices downward correct

Source(s): Accenture Strategy analysis

The balance of recent data points to an ongoing slump in global manufacturing, moderating services momentum and further cooling of inflation and labor markets

AS OF FEB 26

Country economic momentum snapshot



Note(s): Services and Manufacturing metrics refer to PMI services activity and PMI manufacturing output as provided by S&P Global and may include preliminary “flash” figures, shading is based on most recent result. South Africa and Saudi Arabia manufacturing numbers refer to the whole economy. Consumer spending shading based on real retail sales growth 3MMA percent change except for Australia which is based on Q/Q % change. Employment growth is derived from employment figures as provided by government authorities. CPI uses harmonized figures for Euro Area countries.
Source(s): S&P Global, Haver Analytics, Accenture Strategy analysis

A consumer-led growth downshift alongside still-elevated inflation is base case for the US economy; continued stagnation or mild recessions are most likely throughout Europe

Latest economic outlooks: Americas and Europe

AS OF FEB 26

		Key recent datapoints	Base case outlook	What to watch for
Americas 	US	• Core inflation momentum re-accelerated in Jan • Labor market remained hot in January, adding 350k workers, with wage growth hovering at 5% • Retail sales fell 0.8% mom in Jan, an incipient sign of potential consumer weakening	• A "weakflation" scenario, characterized by consumer-led downshift in growth and persistence of above-target inflation due to supply-side cost pressures	• Further acceleration in core inflation delaying the timing of Fed's rate cuts • Consumer spending inflection, led by lower-income households • Intensifying credit crunch for small businesses from CRE stress on banks
	Canada	• January PMIs and other business surveys suggest ongoing contraction in both mfg. and services • Headline and core inflation eased further in Jan	• Tight financial conditions, weakening external demand and housing market distress are expected to keep growth muted in the near term	• Extent of consumer slowdown amidst high housing and debt service costs • The effectiveness of recent tax cuts in stimulating new homebuilding
	Brazil	• Monthly GDP tracker suggest resilient economic growth momentum at end of 2023 • Headline and core disinflation momentum both slowed in Jan	• Slowing growth relative to 2023 due to normalization of agricultural output, which saw unusually-strong harvest season last year	• Strength of agricultural harvest in 2024 amidst shifting climate patterns • Ongoing uncertainty regarding planned tax reforms and overall fiscal trajectory
Europe 	UK	• Economy ended in 2023 in a mild recession, with GDP falling 0.3% qoq in Q4 (after -0.1% in Q3) • Retail sales rebounded in strongly in Jan, and services growth has been surging since Nov	• A tepid growth recovery, constrained by high rates and still-cautious consumers, with downside risk that economy gets stuck in cycle of rolling mild recessions	• Durability of the recent consumer spending and services rebound • Extent of fiscal expansion (e.g. tax relief) in the context of an election year
	Germany	• Real GDP declined by 0.3% in Q4 2023 • Contraction in manufacturing intensified in Feb • Ifo business climate index rose in February mainly due to improving services sentiment	• Continued weakness in manufacturing, slowing export demand from China, high energy costs and restrictive fiscal rules are expected to keep growth stagnant in the coming quarters	• Failure to ratify or fund planned industrial policy initiatives could reinforce eroding industrial competitiveness and dampen prospective rebound in exports
	France	• GDP was stagnant in Q4 2023, with full-year growth of 0.9% driven mainly by net exports • Inflation further declined in Jan to 3.4%, lowest since Jan '22	• Ongoing muted growth as fiscal budget cuts and economic slowdowns in China and Germany counteract the positive to impulse to consumer spending from declining inflation and rebounding real wage growth	• Future implementation progress of fiscal consolidation measures and the industrial competitiveness investment plan in the face of the ruling minority government in the parliament

Source(s): Accenture Strategy analysis

China is expected to transition to slower growth path as it confronts structural challenges; Japan's economy is expected to be sluggish while India continues to thrive

Latest economic outlooks: Asia-Pacific

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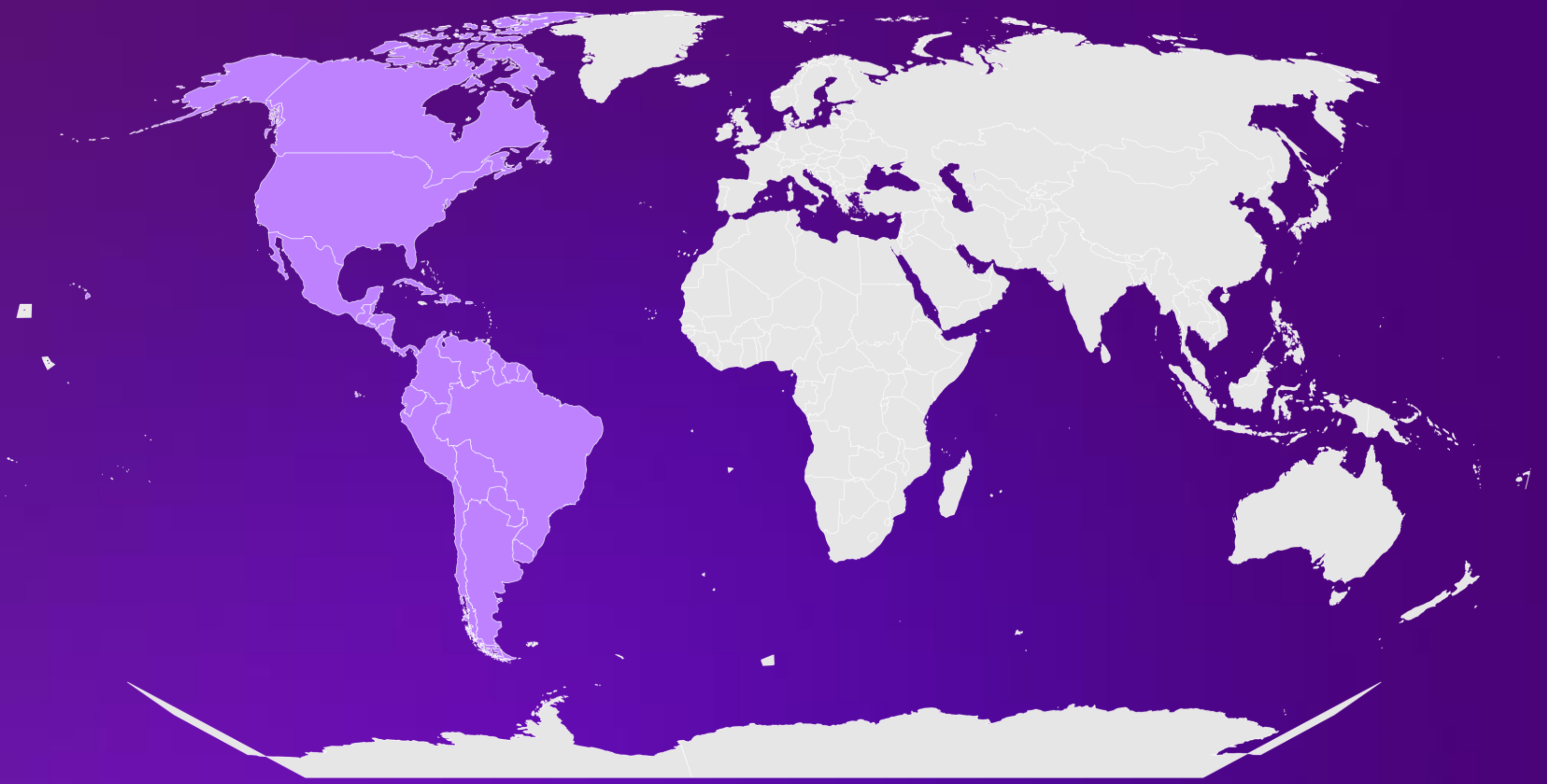
		Key recent datapoints	Base case outlook	What to watch for
Asia Pacific	China	• China's inbound foreign direct investment fell to lowest level in 30 years • Consumer prices fell by 0.8% yoy in January, marking the 4th straight month of declines • Expansion in manufacturing and services PMIs continued in January, marking limited rebound	• Subdued consumer confidence amid property sector challenges, soft external demand and limited policy stimulus in the near-term • Growth continues to trend down towards the slower (3-4%) potential rate associated with China's materializing structural challenges	• Extent of government policy support to prop up flagging growth and distressed property market • Export performance in targeted "New Three" sectors (EV, batteries, solar)
	Japan	• Real GDP contracted -0.1% qoq in Q4, as declines in both consumer spending and fixed investment offset a small rebound in exports, putting the economy in a technical recession • Nikkei 225 index surpassed its historical high in late-1980s after powerful rally	• GDP growth is expected to remain sluggish in 2024 as still-negative real income growth weighs on domestic demand and last year's strong export rebound (powered by pent-up auto and tourism demand and a weak yen) moderates	• Degree of moderation in tourism and auto export growth • Outcome of Shunto wage negotiations in the spring and extent to which inflation-wage growth gap narrows • How quickly the Bank of Japan loosens its yield curve control policy
	India	• Both manufacturing and services activity are expanding at a rapid pace • Inflation is still above the RBI's mid-point target range but has eased as the key component of food prices moderate	• Some moderation in growth momentum amidst slowing global demand, but still enough to maintain India's position as one of the fastest-growing major economies in 2024, continuing the trend from 2023 and 2022	• Resilience in domestic demand and strong growth in capital expenditure • Signs of manufacturers or other companies shifting supply chains to India
	Australia	• Judo Bank flash composite PMI moved into expansionary territory in February, driven by uptick in services demand • Consumer sentiment remains pessimistic, but improved substantially in February	• Growth is likely to remain subdued as cost-of-living pressures and high interest rates continue to weigh on domestic demand	• Impact of positive wealth effects from recent house prices increases on consumer spending • Ongoing drag on Australian exports from China's economic slowdown
	Indonesia	• Latest PMIs point to continued strength in manufacturing, as faster new order growth, coupled with better supply conditions, led to fastest pace of expansion in two years	• Growth is expected to remain robust in 2024 as inflation pressures ease slightly and consumer spending remains resilient • Headwinds remain from slowing external demand and persistently-elevated interest rates	• Potential economic policy shifts when new President-elect takes office • Continued measures to manage sluggish external commodities demand and inflation in food prices

Source(s): Accenture Strategy analysis

Spotlight developments

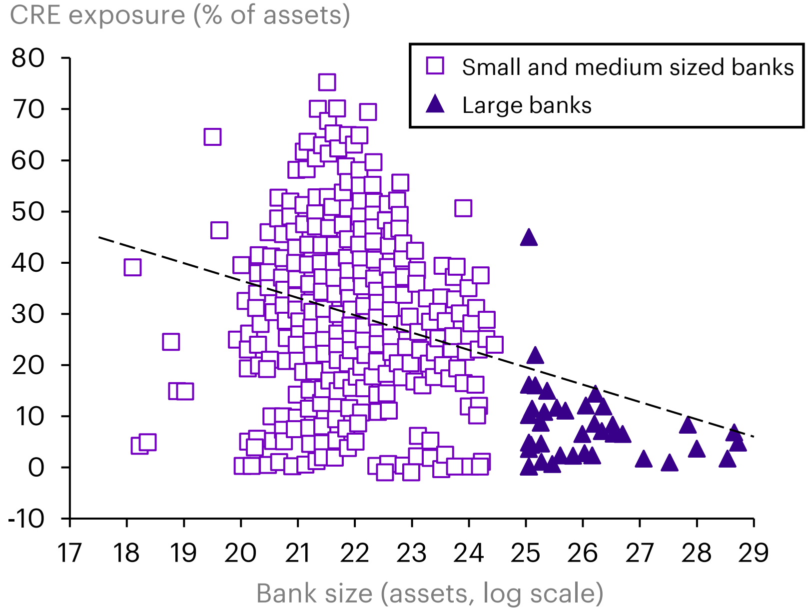
Americas



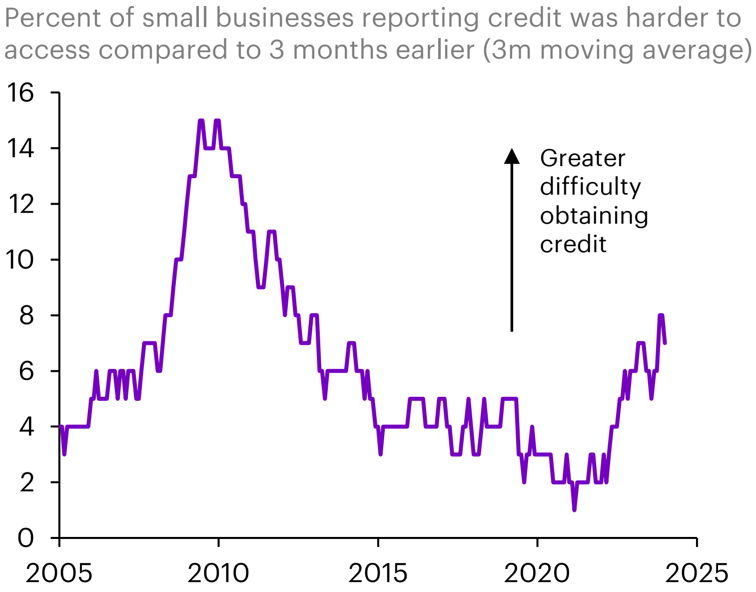
A slow burn of CRE losses in the US is expected to continue to disproportionately pressure smaller banks and companies, though broader financial contagion remains a risk

CRE-driven pressures on small businesses in US

Bank exposures to commercial real estate[1]



Small business access to credit



Implications for corporates

- Small and medium-sized companies relying on CRE-exposed regional banks are likely to face growing financing challenges and pressures to cutback on hiring and capex
- In turn, B2B companies with a significant small business customer base can expect some potential softening in demand
- Broader contagion could result from:
  - Disruptions in interbank funding markets due to opacity of counterparty exposures to troubled banks
  - Deleveraging among non-bank financial institutions with large CRE exposures
  - Urban "doom loops" where declining property values erode tax revenue and trigger cuts to public spending and outward population migration

Commentary

- Large CRE losses reported by New York Community Bancorp triggered a renewed selloff in shares of US regional banks in early February
- For the time being, most CRE distress remains confined to office buildings, but past real estate cycles suggest distress in one segment of the market can drag down property valuations more broadly
- Smaller US banks remain most at risk—some have as much as 75% of their assets tied to CRE via direct lending and holdings of CMBS
- Even a slow burn of CRE losses at current default rates can lead to significant profitability and capital pressures for these banks, forcing them to curtail lending to key customers such as small businesses, who are already facing growing difficulties securing credit

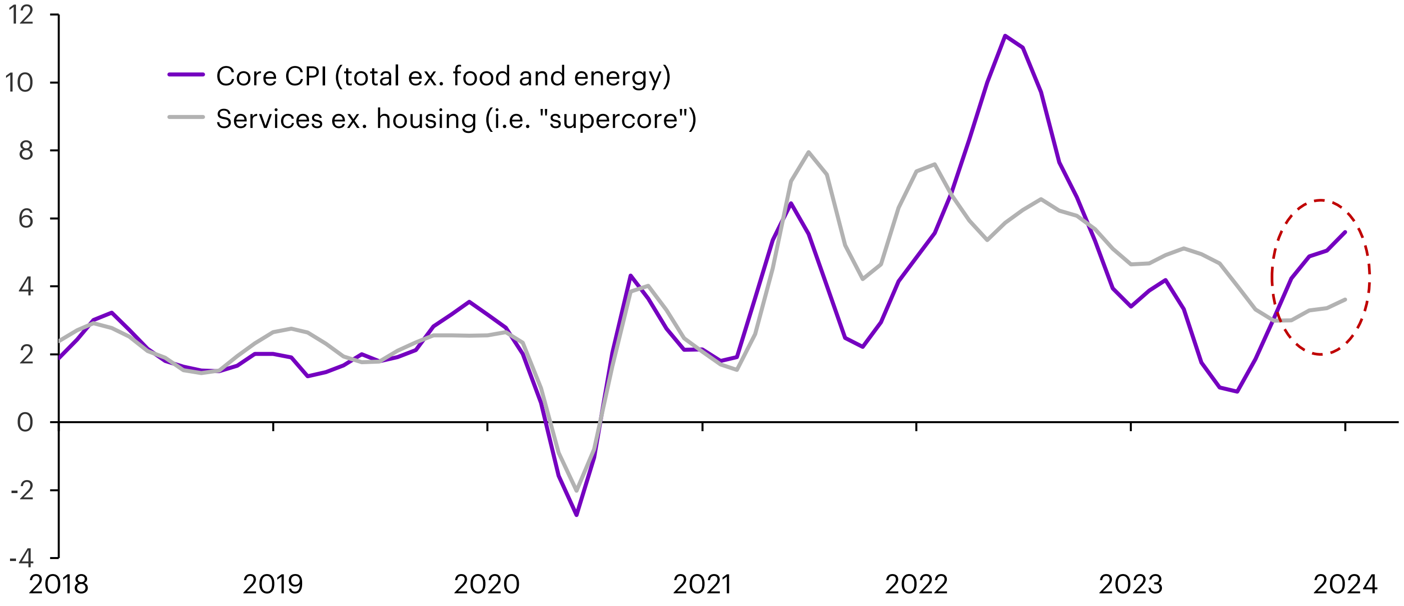
Note(s): 1/ Includes both direct (loans) and indirect CRE exposures (e.g. banks' holdings of commercial mortgage-backed securities)
Source(s): Federal Reserve Bank of St. Louis, National Federation of Independent Businesses, Accenture Strategy analysis

The recent re-acceleration in core US inflation, if sustained, raises the likelihood of higher-for-longer interest rate scenarios

Renewed core inflation pressures in the US

Short-term core CPI inflation momentum

3-month moving average % change, annualized



Implications for corporates

- Continued stickiness or acceleration in core inflation is likely to delay the timing of Fed rate cuts to the second half of the year, with a tail risk of no cuts at all in 2024 if economic activity remains resilient and the labor market does not cool further
- Companies should therefore prepare for the pressures associated with sticky inflation and higher-for-longer rate scenarios, including:
  - Costlier debt refinancing
  - Valuation pressures
  - Continued strong labor bargaining power and wage pressures

Commentary

- Short-term core inflation momentum (i.e. the 3-month moving avg. change) has been re-accelerating since Nov ‘23 and jumped up again January
- The “supercore” measure closely tracked by the Fed—services inflation ex. housing—was behind most of the increase and a cause for concern since:
  - Services are the set of prices most reflective of domestic demand and labor market conditions
  - Their stickiness suggests that, despite aggressive monetary tightening, underlying inflationary pressures are not sustainably abating, and that most recent disinflation can be attributed to external factors such as supply chain normalization and softening energy prices

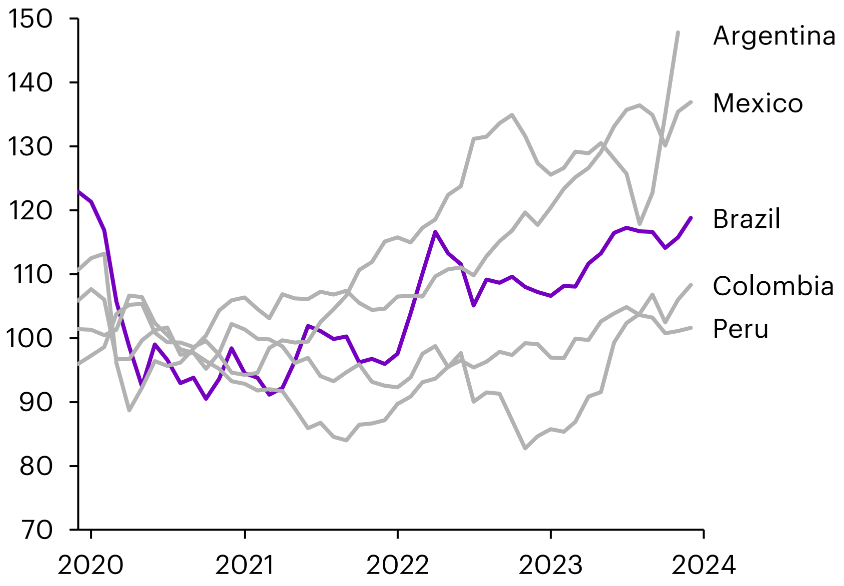
Source(s): Bureau of Labor Statistics, Accenture Strategy analysis.

Resilient economic activity is reinforcing Brazil's outperformance within LATAM, though a widening fiscal deficit may hinder inflation stabilization and longer-term growth prospects

Brazil's economic resilience

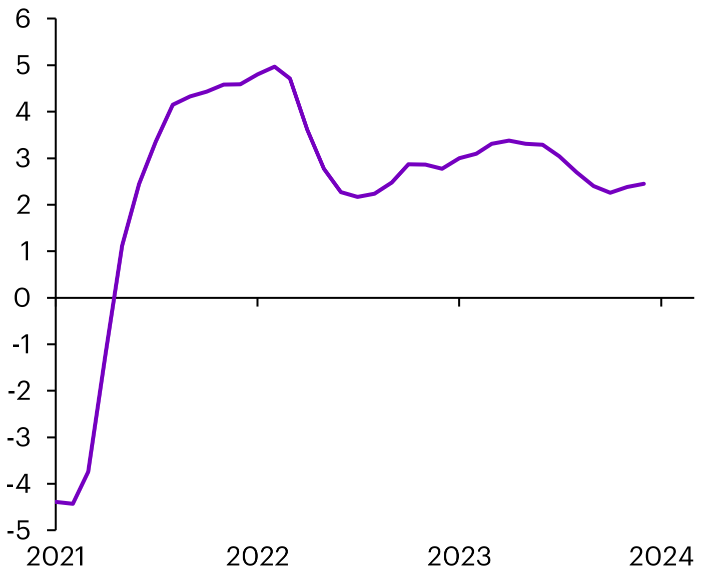
Real Broad Effective Exchange Rates (RBEER)[1]

Index 2020 = 100



Brazil Monthly Economic Activity Index (ICB-Br)[2]

% change in 12 months



Implications for corporates

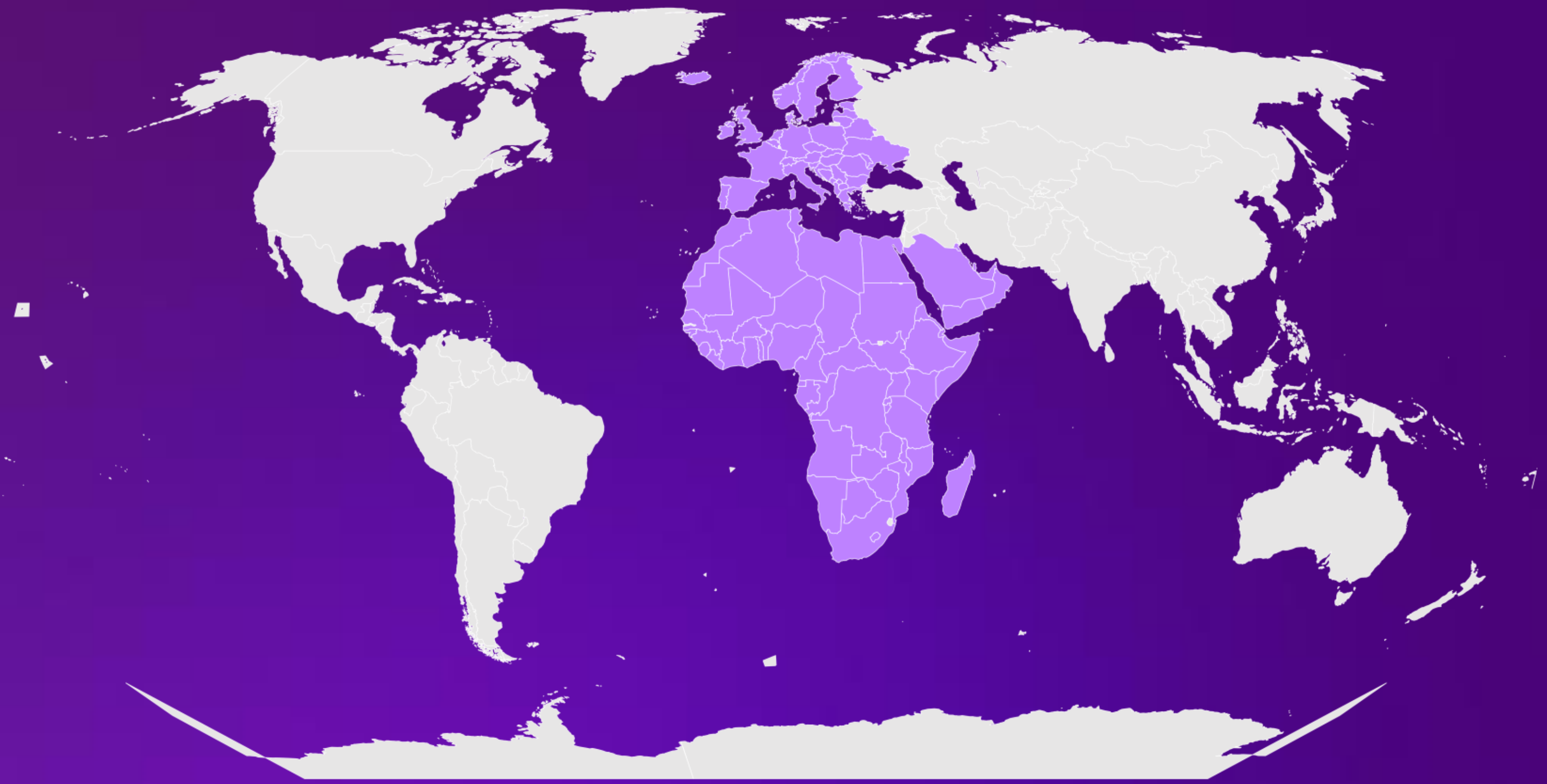
- Executives may find it easier to make the case for investments in Brazil relative to other more volatile markets in the region
- However, business plans will need to consider risk of higher-for-longer inflation and future tax increases, as Brazil's government tries to rein in fiscal deficit
- Key opportunities in Brazil in the short-term will be in exporting industries, as the BRL remains low relative to its pre-pandemic levels
- High-interest rates distressing leveraged companies' balance sheets should foster opportunistic M&A in Brazil, especially in sectors with room to continue to consolidate, such as healthcare, energy, agribusiness, retail and e-commerce

Commentary

- Brazil's economy has continued to outperform expectations, buoyed by still-strong consumption and particularly resilient export growth
- Inflationary pressures have not undermined Brazil's export competitiveness as much as in other countries (notably Argentina, and to a lesser extent Mexico) as the Brazilian real has failed to regain most of the ground lost to major currencies since 2020
- Against this positive backdrop, companies should continue to monitor the country's worsening fiscal situation, which is fueling inflationary pressures and might slow the pace of rate cuts by Brazil's Central Bank and force frontloading of fiscal austerity measures

Notes: (1) The Real Broad Effective Exchange Rate (RBEER) is a measure used to assess the value of a currency against a basket of other major currencies after adjusting for inflation; a rising RBEER indicates that inflation is outpacing currency depreciation, eroding a country's export competitiveness; (2): Banco Central do Brasil's Economic Activity Index (IBC-Br) is a monthly indicator of national economic activity that correlates strongly with GDP
Source(s): World Bank, Banco Central do Brasil, US Institute for Peace, Federal Reserve Bank of St Louis

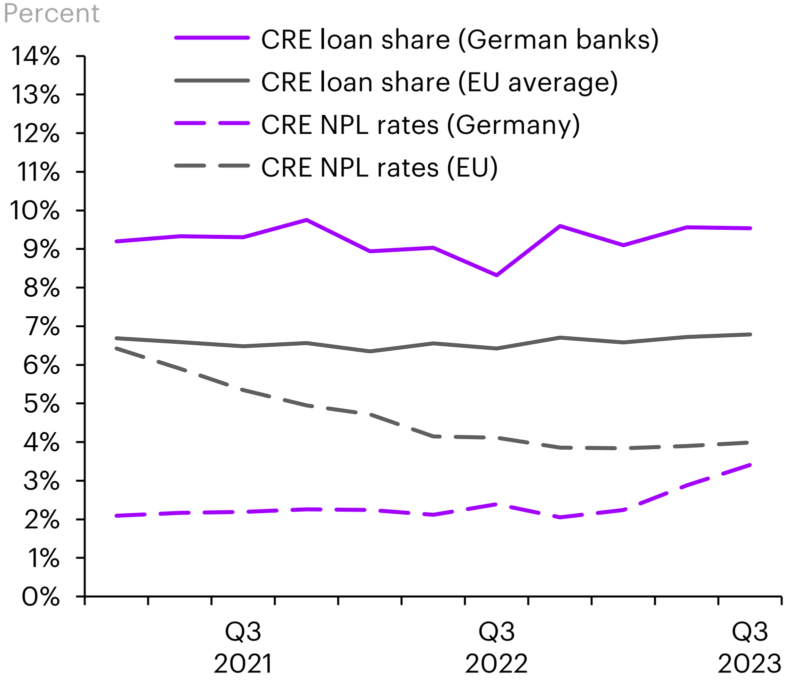
Europe, Middle East and Africa



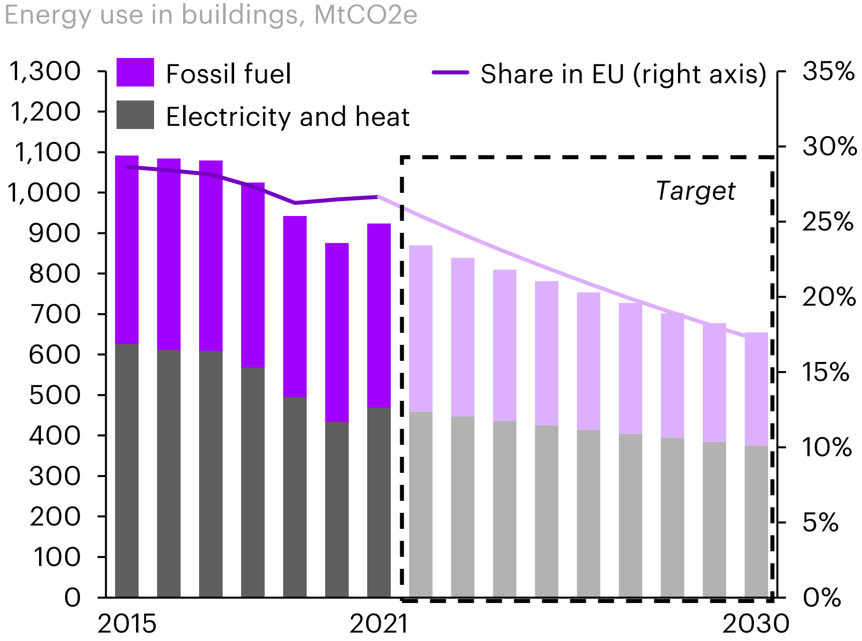
CRE-related losses are on the rise in Germany, and property portfolios also face valuation pressures and potential stranding as result of stricter EU climate regulations

CRE loans and climate-related pressures in Germany

Commercial real estate loans and NPL rates



Greenhouse gas emissions



Implications for corporates

- Though German banks' precautionary loan-loss provisions are fairly high, CRE's exposure to climate risks could lead to asset stranding and amplify losses and capital pressures
- Property owners face heavy CAPEX pressure to comply with decarbonization requirements, but could also capitalize on retrofitting distressed buildings to enhance energy efficiency and asset value

Commentary

- CRE exposures among German banks (as % of loan book) are 2.7 percentage points higher than the EU average, and the recent sharp increase in NPL rates on these CRE loan has raised concerns about vulnerability of German banking sector
- The EU's goal to reduce emissions in the building sector by at least 60% by 2030 (relative to 2015) suggests a need for approximately EUR 275 bn in additional investment in building renovation each year
- The combination of additional borrowing needs for these investments, coupled with downward pressure on CRE prices from stranded assets (i.e. buildings that cannot be cost-effectively retrofitted), threatens to exacerbate CRE losses and pressures on banks

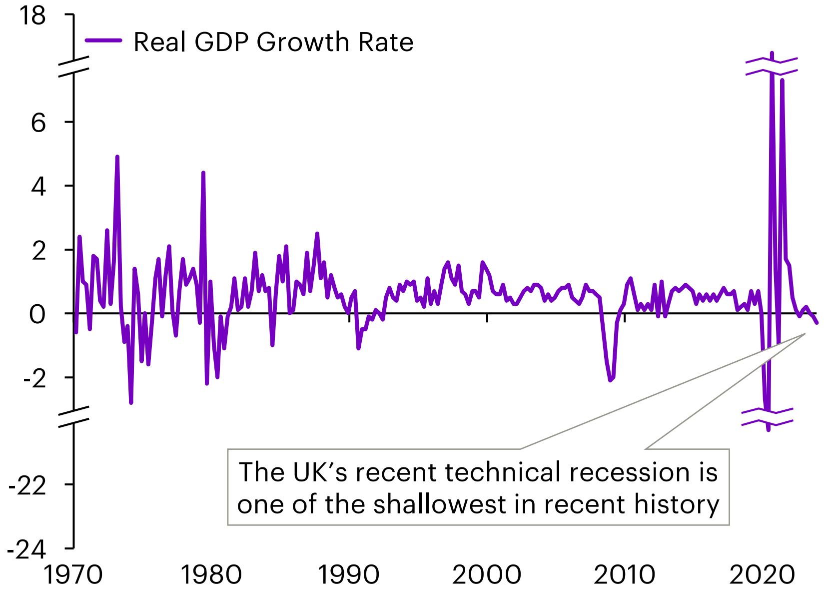
Source: European Banking Authority, Haver Analytics, Accenture Strategy analysis

The UK economy is showing early signs of recovery from its recent shallow recession

Recent UK economic growth momentum

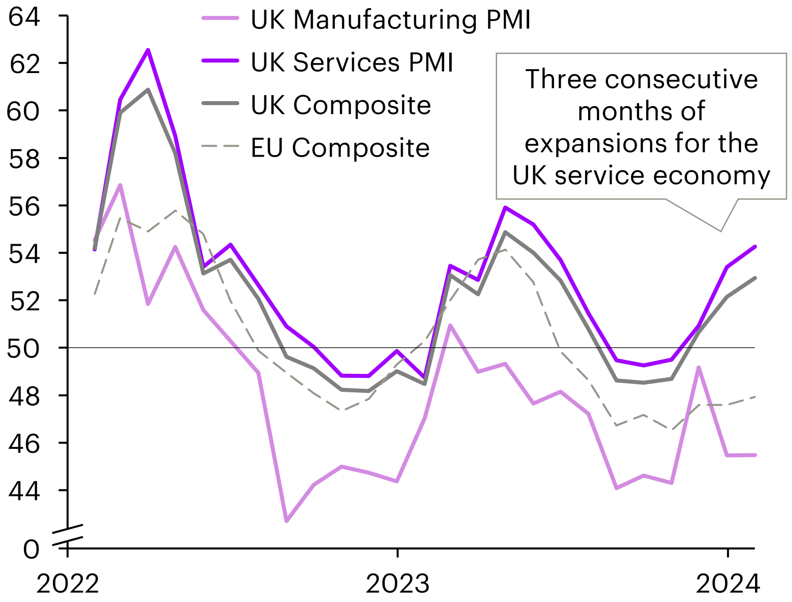
Shallowest recession in UK's history since 1970s

Quarter on quarter Real GDP growth rate (in %)



Faster rise in business activity

PMI Services, Manufacturing and Composite



Implications for corporates

- UK service sector companies are likely to benefit from rebounding demand, though a still-tight labor market could keep wage pressures high and dampen margins
- The recent rebound in consumer sentiment could help revive consumer spending, which has languished since mid-2023
- Manufacturing companies are likely to benefit from the recent fall in energy prices
- Bank of England could cut lending rates as early as May if inflation continues to cools, providing a stimulus to the economy

Commentary

- UK economy entered a mild recession in the second half of 2023, with real GDP contracting for two consecutive quarters (-0.1% in Q3 and -0.3% in Q4)
- However, recent PMI data suggests the economy may have already begun to turn the corner—services activity growth has been rebounding strongly since November, while the pace of manufacturing contraction has stabilized; retail sales also rebounded strongly in January
- Inflation has also come down markedly on the back of falling consumer energy prices (bringing headline CPI inflation down to 4% in January), but remains well above the 2% target and could make the Bank of England hesitant to cut rates too prematurely

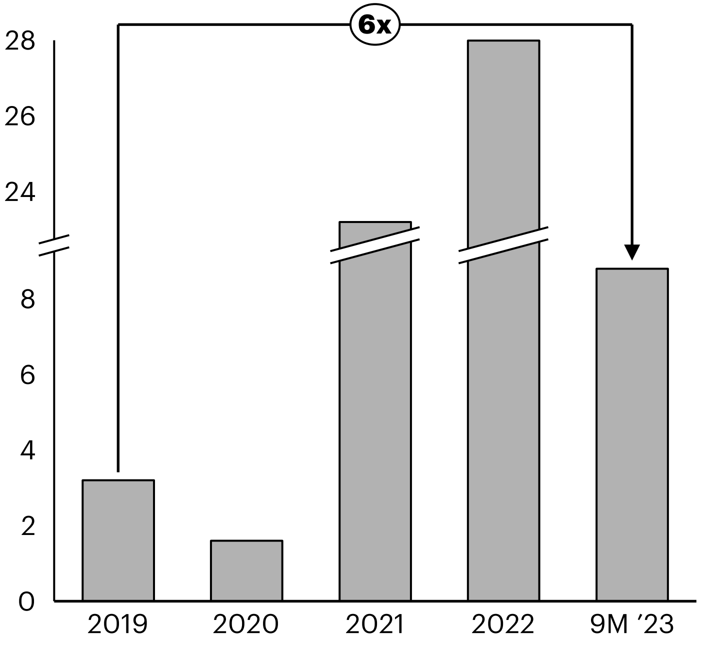
Source: Office of National Statistics UK, S&P Global PMI Data, Accenture Strategy analysis

Building on recent FDI momentum, Saudi Arabia continues to pursue reforms to attract more foreign companies and compete for global science and innovation talent

Saudi Arabia's FDI evolution and global economic competitiveness

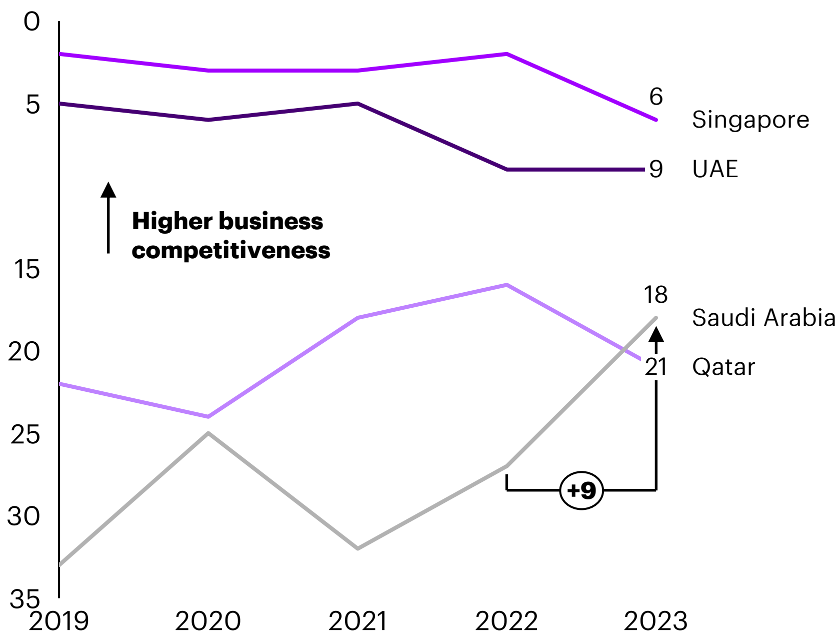
Net FDI inflows continues to surge…

Net FDI inflows (USD billion)



…as KSA's global competitiveness edges higher

Global rank, Business Legislation, World Competitiveness Index, 2023



Implications for corporates

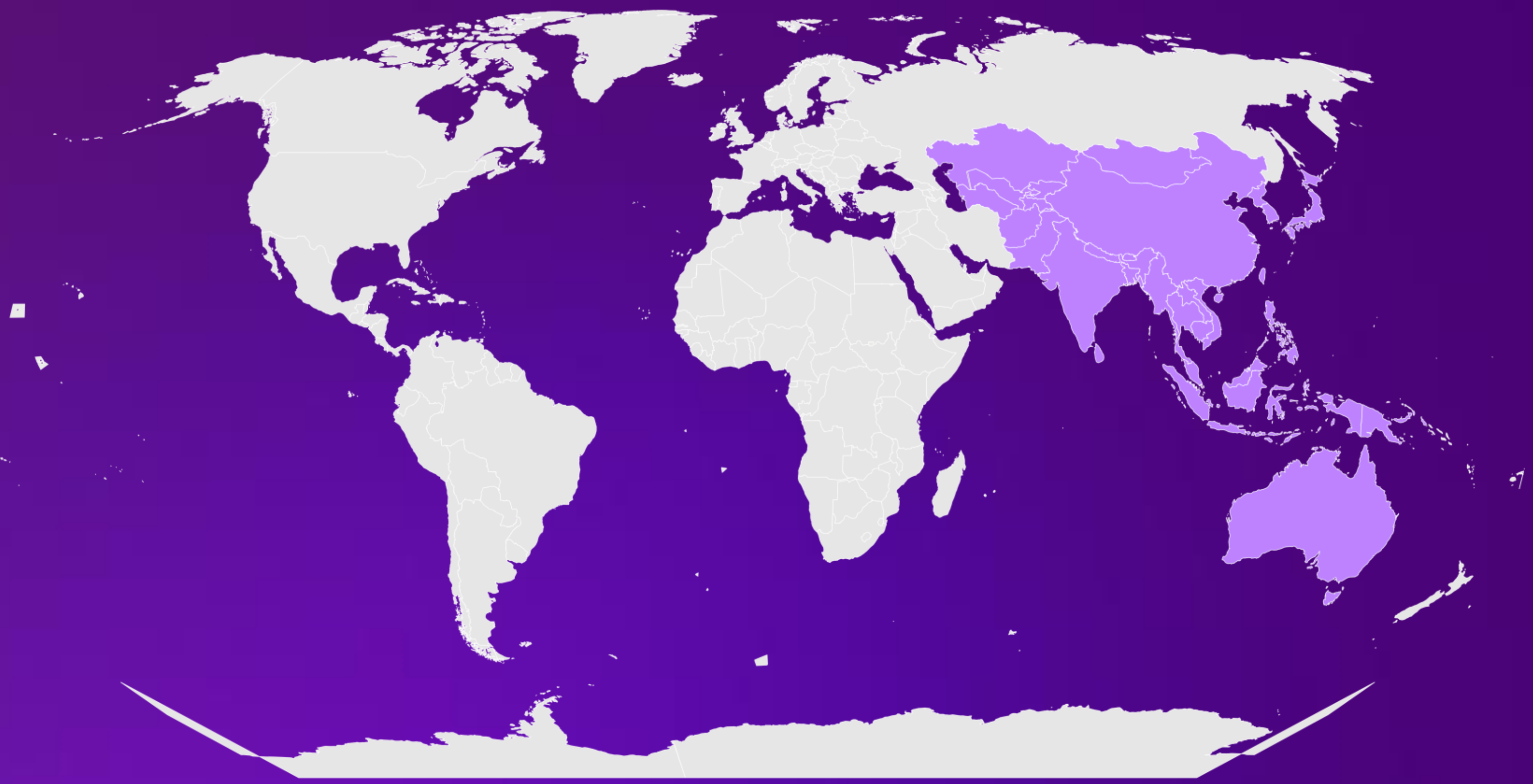
- A more conducive policy and regulatory framework for foreign investment is part of the Kingdom's ongoing strategy for economic diversification
- More efforts in this direction are expected to further attract foreign corporates seeking to relocate their regional headquarters or establish new R&D and high-tech centers
- As MNCs globally embark on enhancing their supply chain resiliency and energy supply security, KSA is growing in geostrategic importance

Commentary

- KSA's government continues to pursue reforms to attract more investments from foreign companies and compete for science and innovation talent:
  - Unveiled guidelines for MNCs seeking a 30-year corporate tax exemption if they establish their regional headquarters in KSA
  - Expanded expertise requirements to obtaining Special Talent Residency Visas, mainly to attract skilled workforce in sciences, tech and R&D
  - Modified age-limit for obtaining a Premium Residency Visa to foreigners under 21-years old and granted holders eligibility to apply for citizenship

Note(s): 1/ Business legislation is a sub-pillar of the IMD World Competitiveness Index' Government efficiency which assesses factors that play a role in determining a nation's competitiveness.
Source(s): The IMD World Competitiveness Center, General Authority for Statistics, Library of Congress, Accenture Strategy Analysis

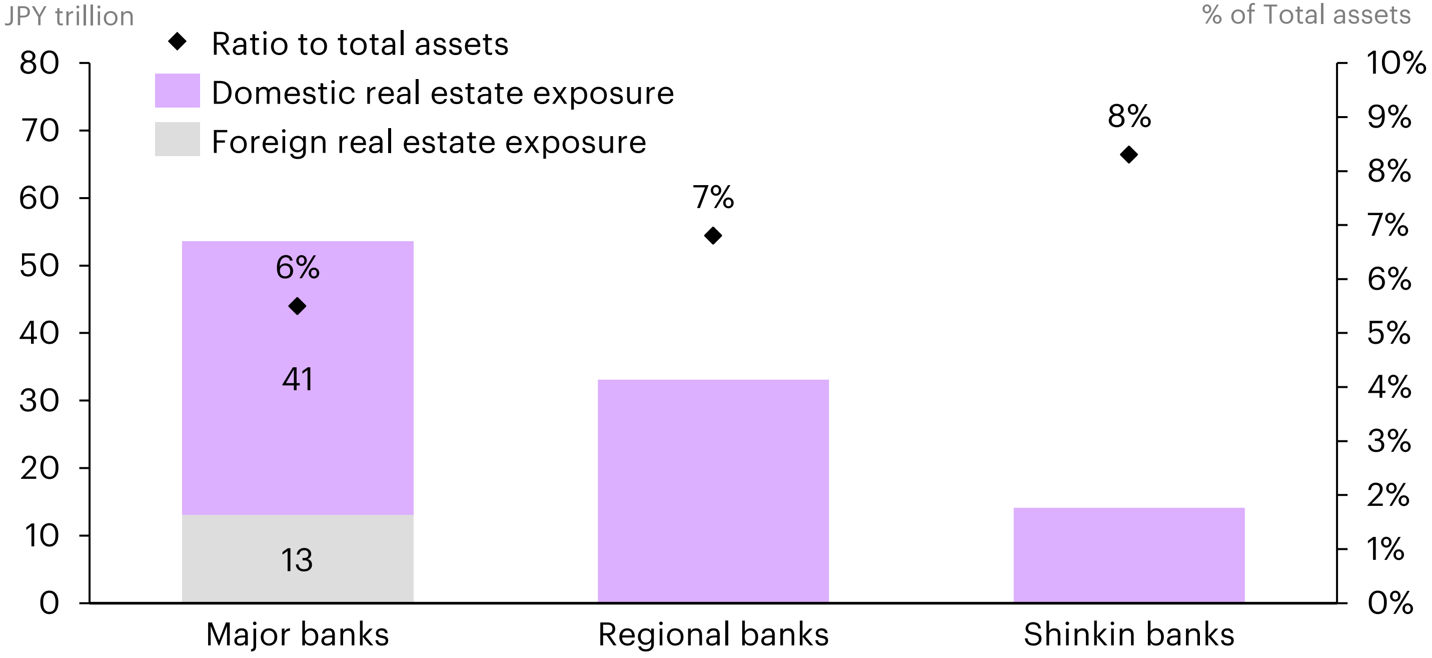
Asia Pacific



Despite concentrated US commercial real estate exposure in one major Japanese bank, broader vulnerabilities of Japan's banking sector to foreign CRE distress appear limited

Japanese banks' exposure to US commercial real estate

Real estate-related exposure of Japanese financial institutions



Implications for corporates

- Potential tightening of lending standards for foreign and domestic CRE loans is likely to impact Japanese construction / real estate and financial companies
  - Refinancing of CRE loans nearing maturity at higher rates could lead to additional stress for Japanese banks exposed to US interest rate, credit and FX risks
  - MNC's profit margins may be squeezed, especially those with larger US CRE exposure, as loss provision allocations increase
  - Construction and real estate development companies operating in Japan would face stricter regulations as banks have to manage risk
- Growing concerns over US CRE losses could lead to more stringent risk disclosures and capital provisions for financial lenders, leading to tighter financial conditions for companies operating in Japan

Commentary

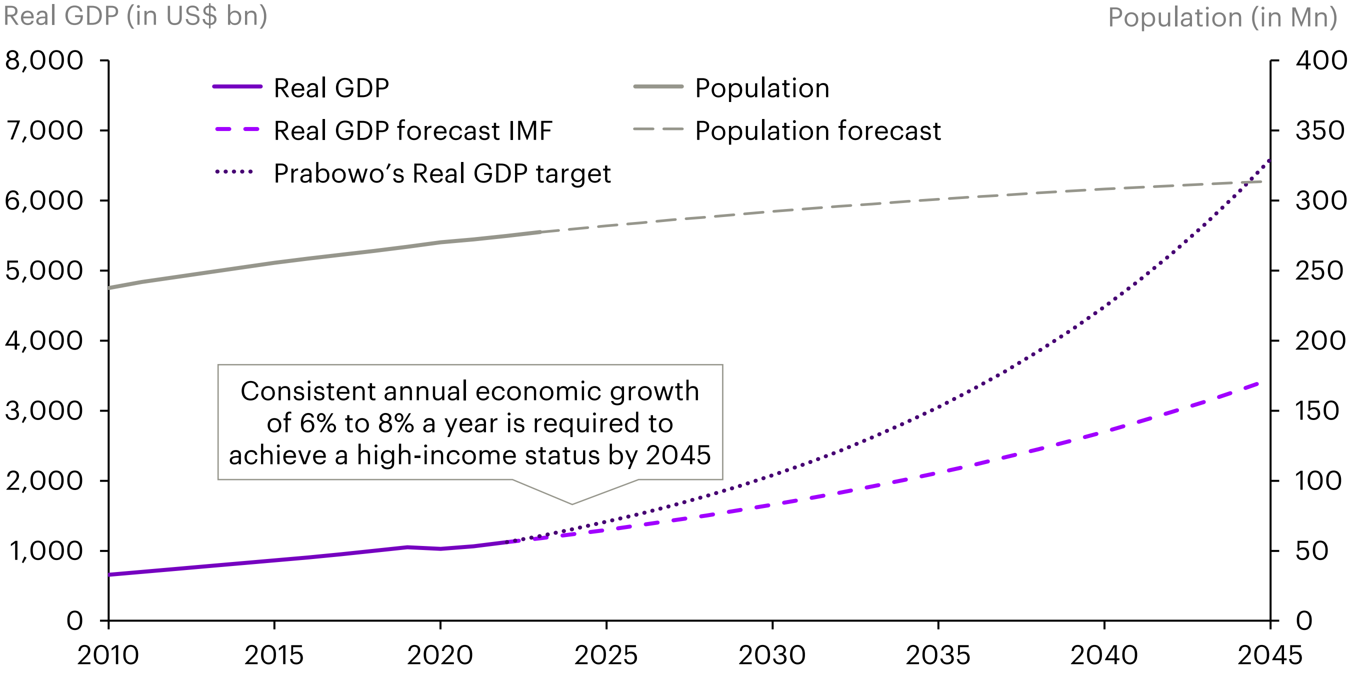
- Aozora Bank's exposure to US commercial real estate—the largest among major Japanese banks (USD 1.9bn as of Dec 2023, equivalent to 6.6% of its total loan book)—recently sparked some market concerns about potential contagion of US CRE distress to Japanese and APAC banks
- However, total exposure to foreign real estate among Japanese banks appears relatively small—roughly USD 19bn (2.8% out of all real estate-related loans), of which an estimated 80% is to US real estate—and confined to major banks with sound balance sheets; no regional or smaller banks are exposed
- As a result, Aozora concentrated exposure does not appear to be a canary in the coalmine for broader CRE-related banking system vulnerabilities in Japan; in fact, most of banks' CRE loan books are domestic and the Japanese CRE market has been strong with rising prices

Notes: 1) BOJ's definition of major banks includes 10 banks, one of which is Aozora Bank (2) Data as of end-March '23
Source: Aozora Company Financials, Bank of Japan Financial System Report (Oct'23), Financial Times, Accenture Strategy analysis

The result of Indonesia’s recent elections suggest there will be broad continuity in economic policies, including raw material export bans

Impact of Indonesia’s elections

Indonesia’s GDP growth and population forecasts



Implications for corporates

- Prabowo’s ambitious growth targets imply an expanding domestic market with a rising middle-class, presenting opportunities for corporates who can adapt to changing consumer preferences and sustainability
- Indonesia’s raw material export bans could result in:
  - opportunities for foreign companies to collaborate with Indonesian companies on mining and processing technology
  - short-term squeeze on profit margins for domestic miners and processors as they invest to compensate for limited domestic processing capacity
  - lower bargaining power for miners of raw materials where Indonesia does not hold a dominant market share (e.g. bauxite and copper)

Commentary

- President-elect Prabowo Subianto has pledged to prioritize government investments in manufacturing and infrastructure, and maintain an export ban on raw materials, with the goal of reducing the economy’s reliance on resource extraction and transforming Indonesia into an industrial powerhouse
- Despite Indonesia's 5% growth pre-pandemic, Prabowo's 8% growth target highlights the drive for advanced-economy status by 2045; this ambitious goal implies 6-8% annual growth and a near tripling of the economy’s size by 2045, potentially making Indonesia a top 5 global economy
- Prabowo has signaled his plans to broadly continue the economic policies of his predecessor (Joko Widodo), including USD 20 billion deal to phase out Indonesia’s large coal industry and plants, though in the near-term the economy will remain dependent on coal energy sources

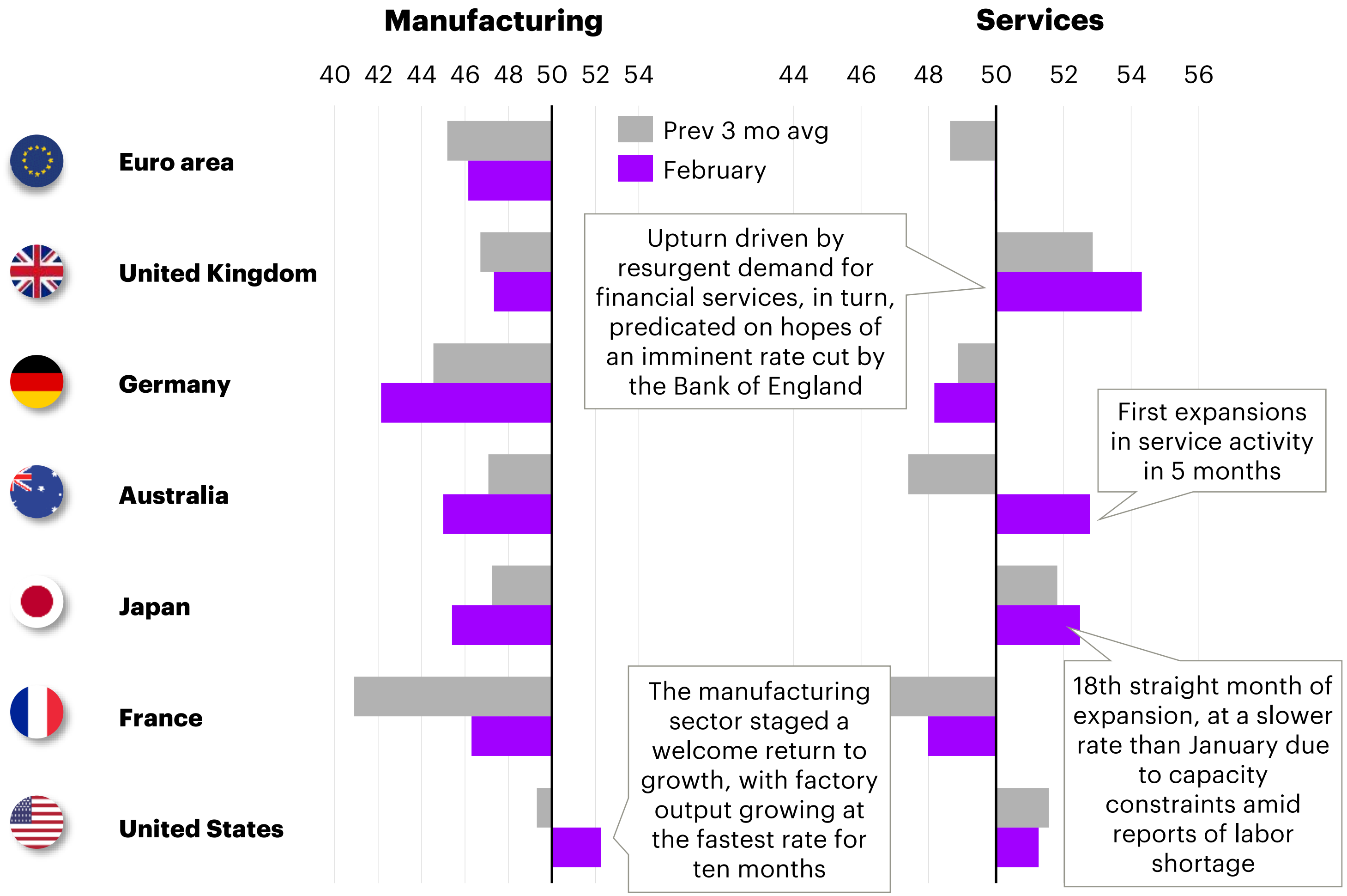
Source: IMF, UN, Accenture Strategy analysis

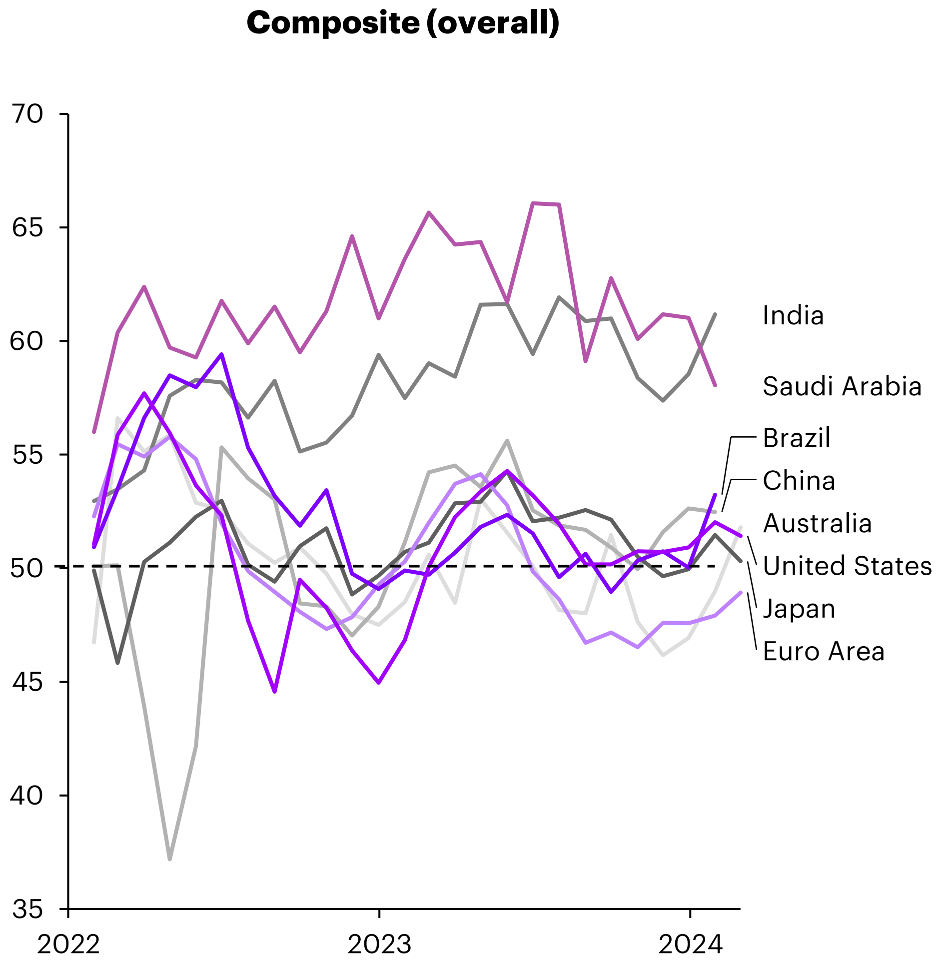
Economic indicator chart pack

Regional and industry activity

Manufacturing remains in contraction across most major economies but may be turning the corner in the US; services performance is mixed

Flash PMI survey country snapshot





Note(s): A survey score above 50 indicates expansionary business activity and a score below indicates business activity contracted that month, most recent results may include preliminary flash figures

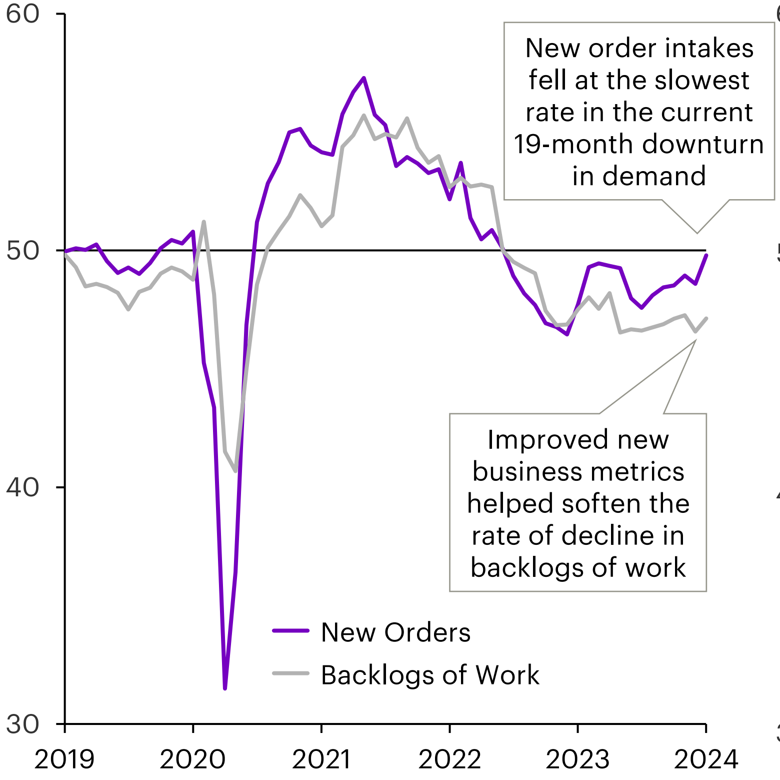
Source(s): S&P Global, Accenture Strategy analysis

Forward-looking manufacturing indicators such as rising new orders, slower inventory destocking and improving output expectations point to an improving outlook

Leading indicators of global manufacturing momentum

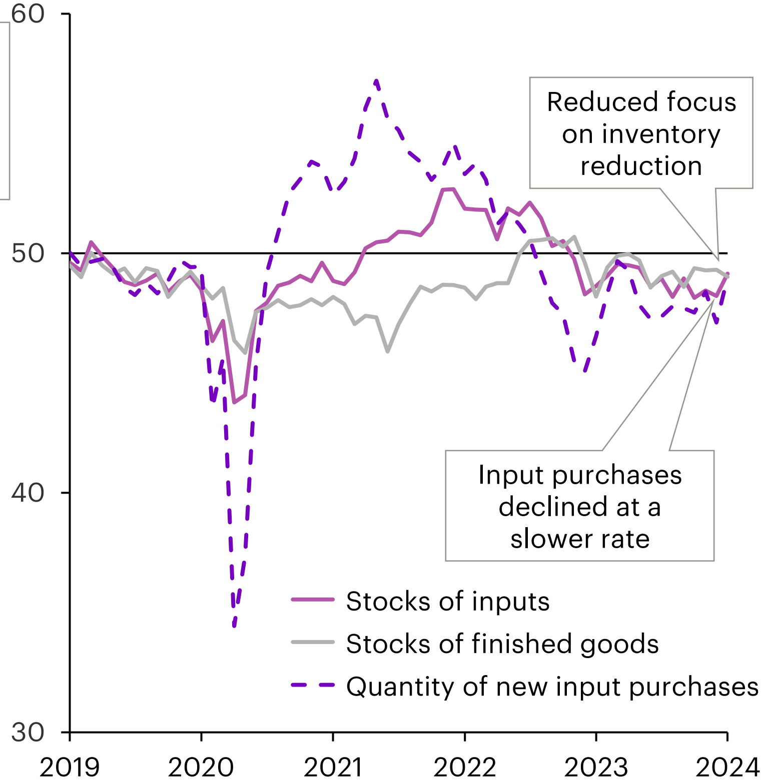
New order inflow fell at the slowest rate...

Diffusion indexes (SA, 50+=Expansion)



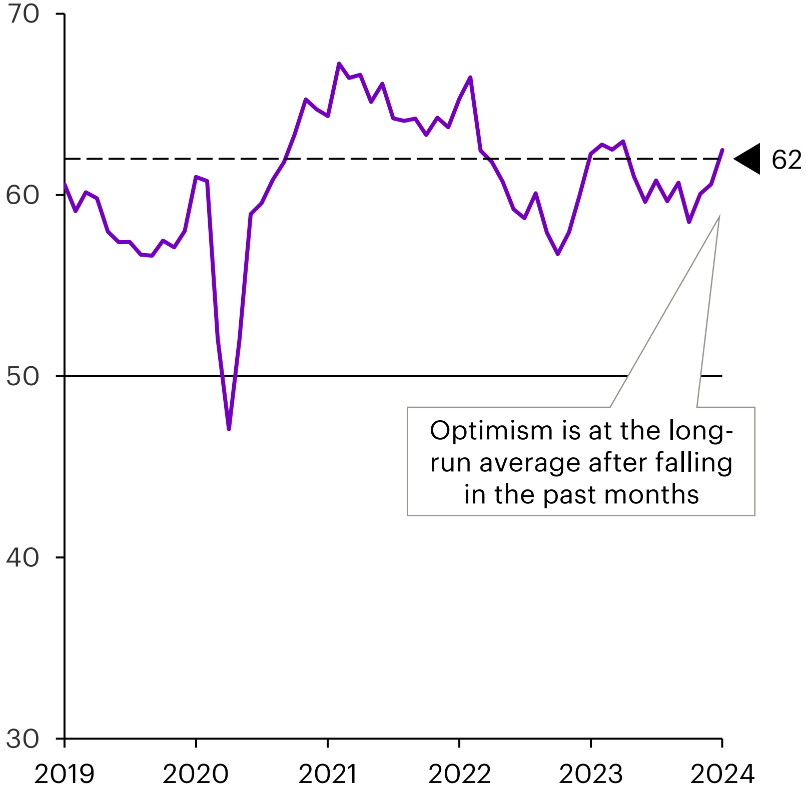
...with a reduced focus on stock reduction...

Diffusion indexes (SA, 50+=Expansion)



...highlighting optimism for the 12-m outlook

Manufacturing future output (NSA, 50+=Expansion)



Note(s):
1/ Data reflects global diffusion indexes, which are GDP-weighted averages in over 40 countries incl. US (21.6%), China (12.7%), Japan (7.7%), Germany (3.6%), UK (3.5%), and India (3.3%), among others. Annual weights are based on Gross Value Added (GVA) in the manufacturing sector in constant US$ from the World Bank. The select countries account for 98% of global manufacturing value added. 2/ Global manufacturing PMI indices are compiled by S&P Global from responses to monthly questionnaires sent to purchasing managers in survey panels totaling around 13,500 companies.

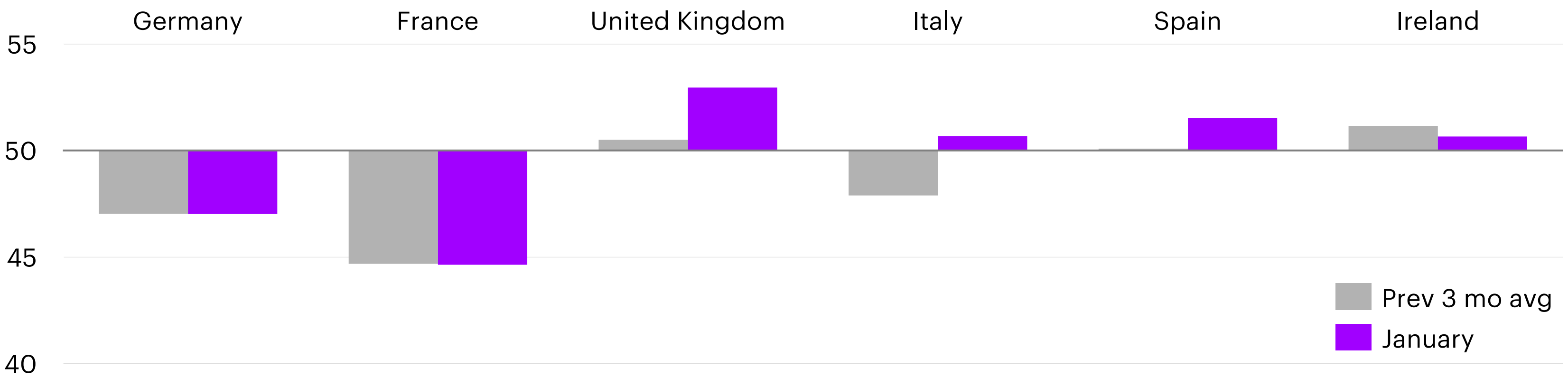
Source(s): Haver Analytics, S&P Global, Accenture Strategy analysis

Business activity improved in the UK, Italy, Spain and Ireland while the downturn continued in Germany and France

Regional performance: Europe

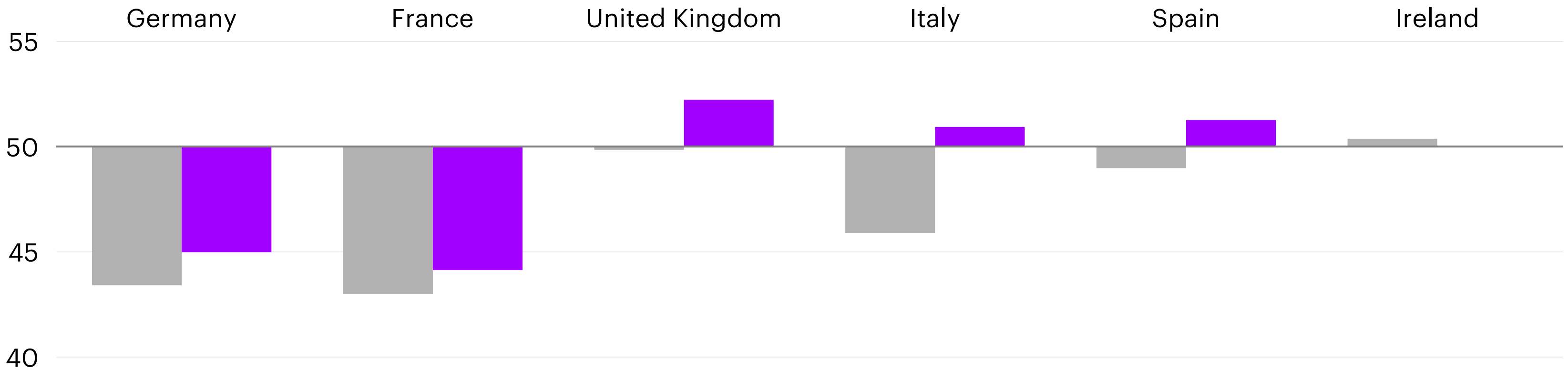
Output/activity

Jan '24 vs Previous 3 Month Average, Output/Activity PMI (>50=expansion)



New Orders

Jan '24 vs Previous 3 Month Average, New Orders PMI (>50=expansion)



Commentary

- New orders in November grew in the UK, Italy and Spain, while the downturn slowed for Germany and France in January (relative to the recent 3-month average)
- The service economy led the way in driving strong private sector output growth in the UK buoyed by stronger output growth projections and expectations of favorable economic conditions
- Expansion in the private sector in Spain was led by the growth of the service sector

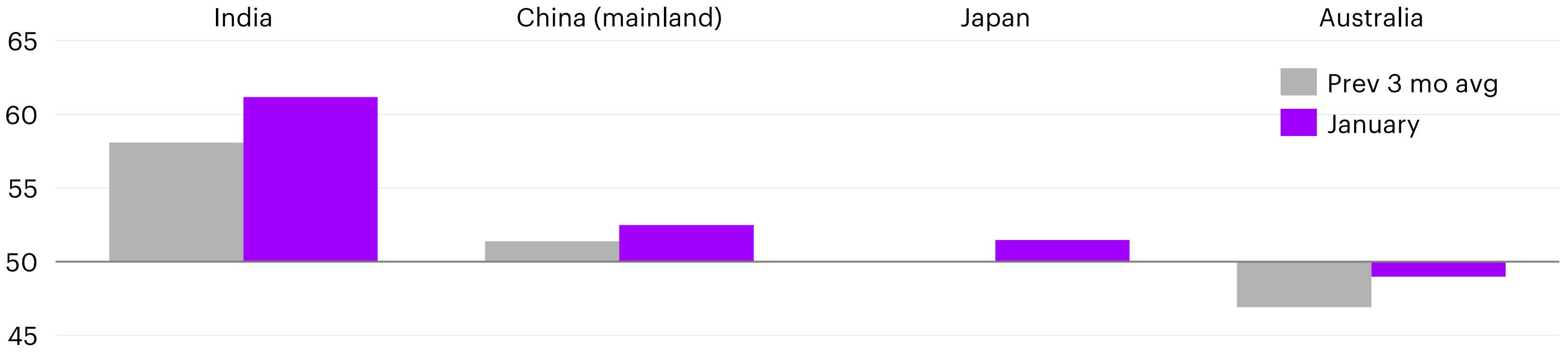
Source(s): S&P Global, Accenture Strategy analysis

India continues to show the strongest growth momentum within Asia-Pacific, while conditions deteriorated in Australia

Regional performance: Asia-Pacific

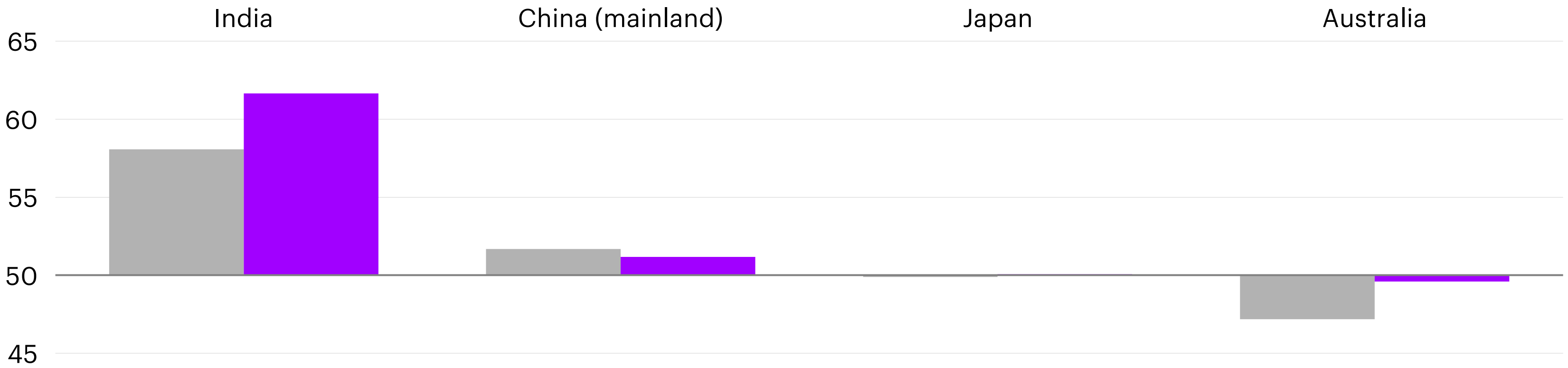
Country performance

Jan '24 vs Previous 3 Month Average, Output/Activity PMI (>50=expansion)



New Orders Index

Jan '24 vs Previous 3 Month Average, New Orders PMI (>50=expansion)



Commentary

- Indian private sector activity improved substantially in January, with both services and manufacturing growing on the back of demand strength and ongoing improvements in new business inflows
- In China, the service sector expanded at a softer pace while factory activity maintained growth momentum for the third month running
- In Australia, the composite index remained entrenched below the 50-threshold, pointing to deteriorating business activity; however, new orders and output fell less sharply in January

Source(s): S&P Global, Accenture Strategy analysis

Manufacturing sector saw expansion across most of Southeast Asia, with only Malaysia and Taiwan showing signs of contractions

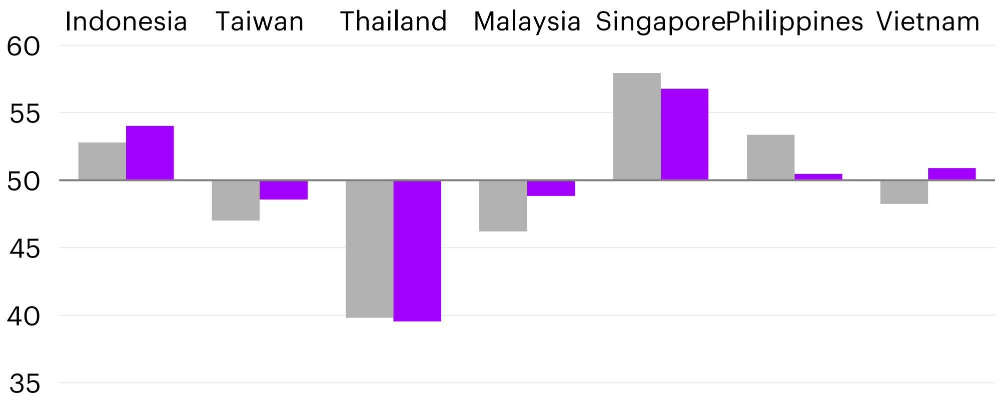
Regional performance: Southeast Asia

Manufacturing Performance

Jan '24 vs Previous 3 Month Average, Manufacturing Output

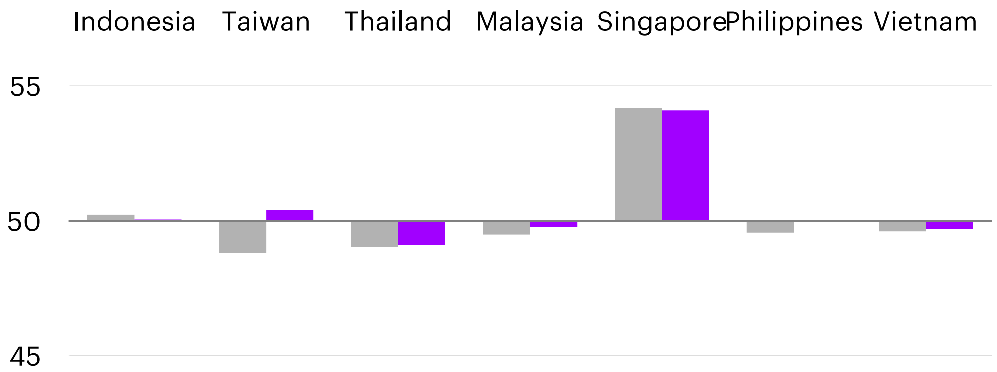
Manufacturing New Orders

Jan '24 vs Previous 3 Month Average, New Orders PMI



Manufacturing Employment

Jan '24 vs Previous 3 Month Average, Employment PMI



Commentary

- Faster new order growth, coupled with better supply conditions, led to production expanding at the fastest pace in two years in Indonesia
- The volume of incoming new orders for Thai manufactured goods fell for a seventh consecutive month at the start of 2024, reflective of softer economic conditions and reduced demand from clients
- The manufacturing sector in Vietnam climbed into expansion territory in January, with overall improvement in business conditions centered on renewed expansions in new orders and production

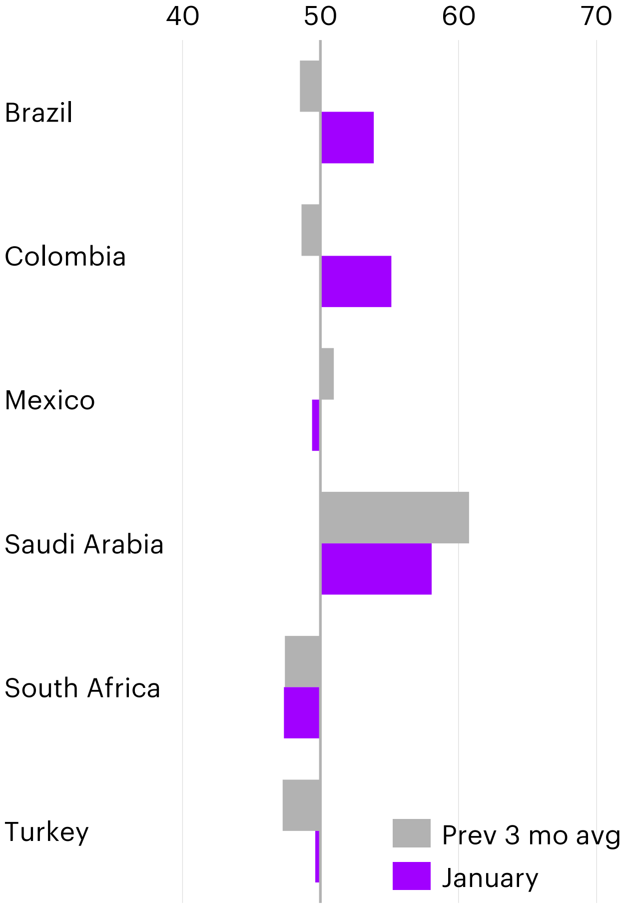
Note(s): Performance for Singapore covers the whole economy
Source(s): S&P Global, Accenture Strategy analysis

Saudi Arabia, Brazil and Columbia show signs of manufacturing expansion, while activity in South Africa and Turkey continues to deteriorate

Regional performance: Other emerging markets

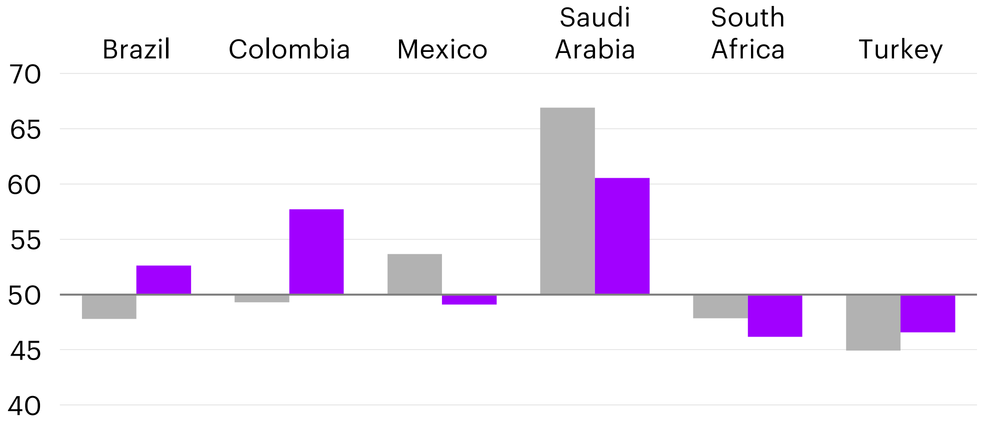
Manufacturing Performance

Jan '24 vs Previous 3 Month Average, Manufacturing PMI



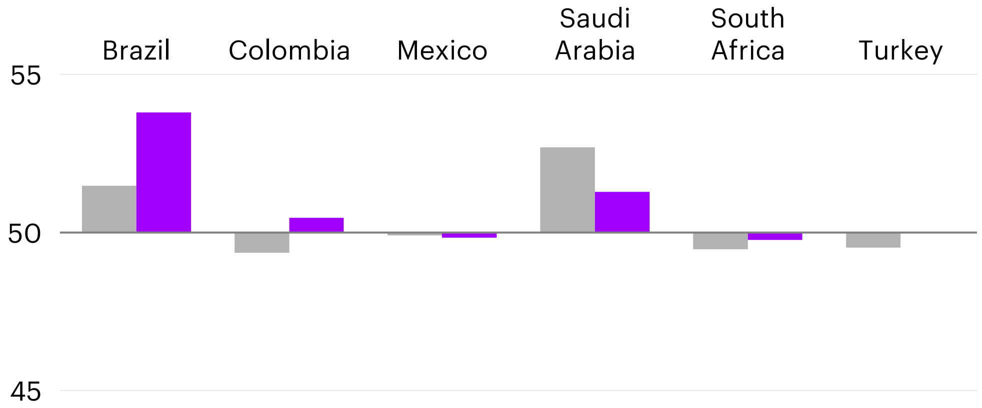
Manufacturing New Orders

Jan '24 vs Previous 3 Month Average, New Orders PMI



Manufacturing Employment

Jan '24 vs Previous 3 Month Average, Employment PMI



Commentary

- Brazilian manufacturing strengthened in January, with companies lifting production volumes to the greatest extent since mid-2022, spurred by a renewed increase in new work intake
- In Colombia, firms saw their order books expand at fastest pace since April 2011
  - Boosted production volumes and induced job creation led to one of the fastest increases in input purchasing on record
- Mexican firms' output slipped back into contraction territory amid downward pressure on new orders due to customer hesitancy to sign pending contracts, business closures, unfavorable weather, and demand weakness
- Business conditions across Saudi Arabia's non-oil private sector improved (slowest rate for two years in January), despite challenges stemming from rising costs and interest rates

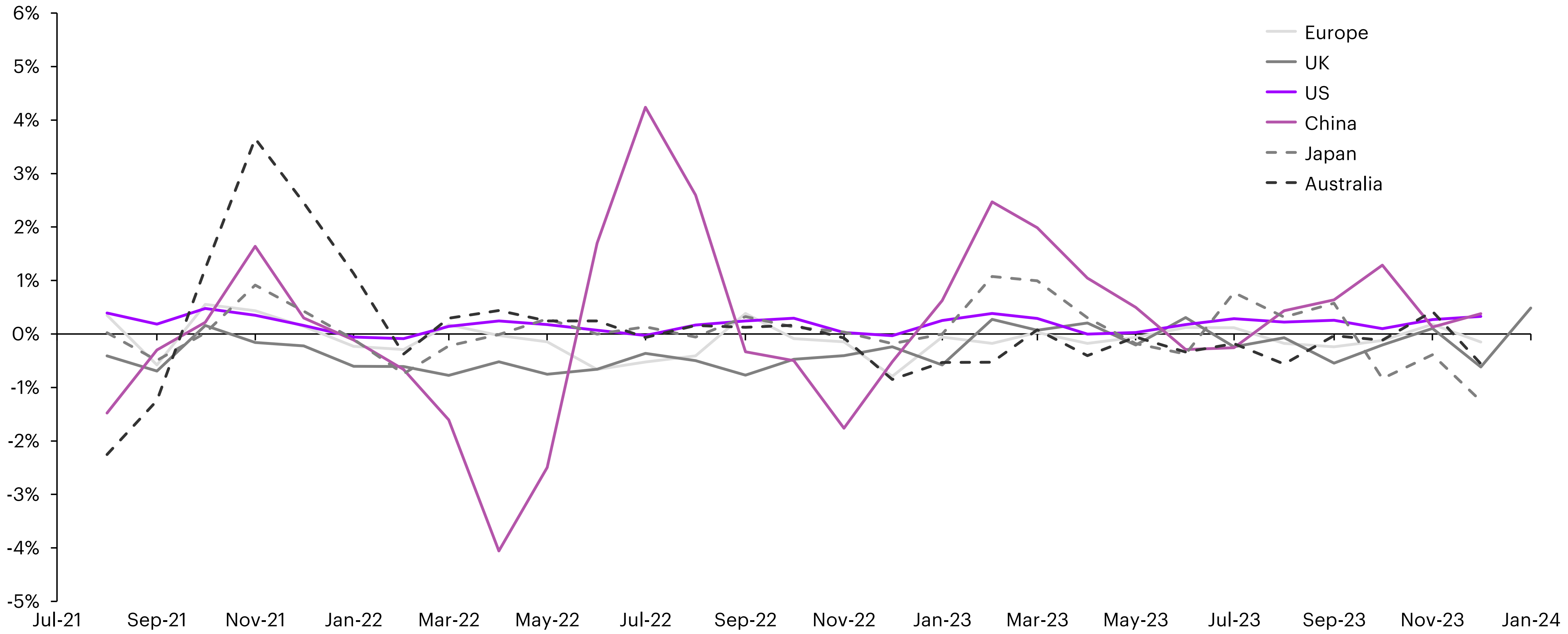
Note(s): South Africa and Saudi Arabia PMI is for the whole economy
Source(s): S&P Global, Accenture Strategy analysis

Consumer spending

Consumer spending continues to moderate in most major economies, though there is a nascent rebound in the UK

Consumer spending trends

Real (inflation-adjusted) consumer spending, 3 month moving avg. % change



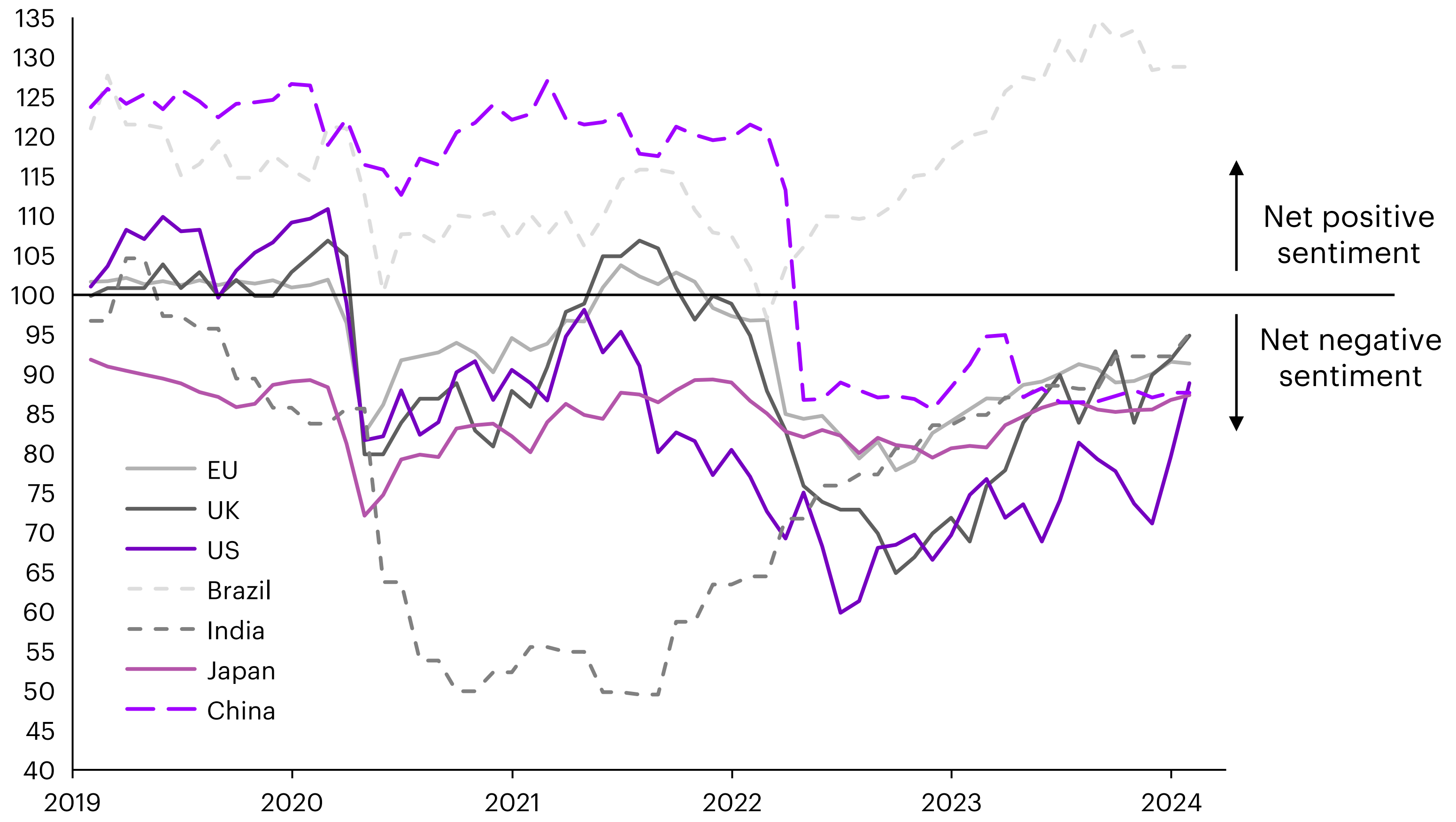
Note(s): Consumer spending series for US is personal consumption expenditures (PCE); for Euro Area, UK, Canada, Japan, Australia, and China series data is retail sales.
Source(s): BEA, BLS, Eurostat, ONS, Haver analytics, Accenture Strategy analysis

Consumer sentiment remains largely pessimistic globally but improved across most economies in January

Consumer sentiment

Indicators of overall consumer sentiment

Index



Commentary

- In the US, an increase in consumer confidence likely reflected slower inflation, anticipation of lower interest rates ahead, and still generally favorable employment conditions
- Despite the cost-of-living crisis still impacting many households across the UK, consumers appear to be encouraged by the positive news about falling inflation

Note(s): All series have been rebased from their original reported levels to a central point of 100. UK data from GfK Survey. US data from Michigan Survey
Source(s): EC Consumer Surveys, GfK Survey, University of Michigan Survey, Fecomercio, China National Bureau of Statistics, Reserve Bank of India, Japan Cabinet Office, WSJ

The rebound in UK consumer spending appears concentrated in goods; services spending is moderating as pent-up demand fades

Consumer spending trends by goods and services category

AS OF FEB 16

		US		UK		Germany		France	
		Prior 6 months	Latest monthly change	Prior 6 months	Latest monthly change	Prior 6 months	Latest monthly change	Prior 6 months	Latest monthly change
Goods	Groceries	0.8%	0.4%	-0.5%	3.4%	-0.8%	-0.7%	0.2%	0.2%
	Motor vehicles	-1.6%	1.6%	-8.2%	2.7%	0.5%	1.1%	6.4%	-0.9%
	Furniture	1.9%	0.6%	-2.2%	-3.2%	-4.8%	1.4%	-5.1%	0.8%
	Electronics	9.1%	3.3%	23.8%	0.7%	0.1%	-6.2%	4.1%	5.9%
	Footwear & apparel	1.3%	1.7%	-3.8%	-1.4%	-1.9%	-8.5%	-0.1%	1.0%
	Fuel	0.9%	2.1%	-0.6%	5.4%	-1.2%	2.1%	-3.5%	2.2%
Services	Transportation	1.4%	1.5%	-1.9%	-0.1%	0.8%	-0.4%	-0.9%	-0.7%
	Entertainment	1.4%	0.9%	1.8%	2.9%		n/a	3.2%	6.5%
	Dining out and hotels	2.5%	-0.3%	-1.0%	0.6%	-1.5%	-1.7%	1.9%	-1.1%
	Information services	3.0%	0.2%	-2.2%	0.4%	0.8%	2.4%	3.1%	-1.4%
	Telecom	2.8%	-0.1%	-3.3%	-0.8%	3.5%	4.9%	4.4%	-0.9%

Note(s): Spending figures are inflation-adjusted. Consumer spending series for US is personal consumption expenditures (PCE); for Euro Area and UK, series data is retail sales, motor vehicles sales/registrations, and services turnover. Some European services data may include B2B spending. Data presented is most recently available data for each geography and category.
Source(s): BEA, BLS, ONS, National Institute of Statistics and Economic Studies, Federal Statistical Office

Labor markets

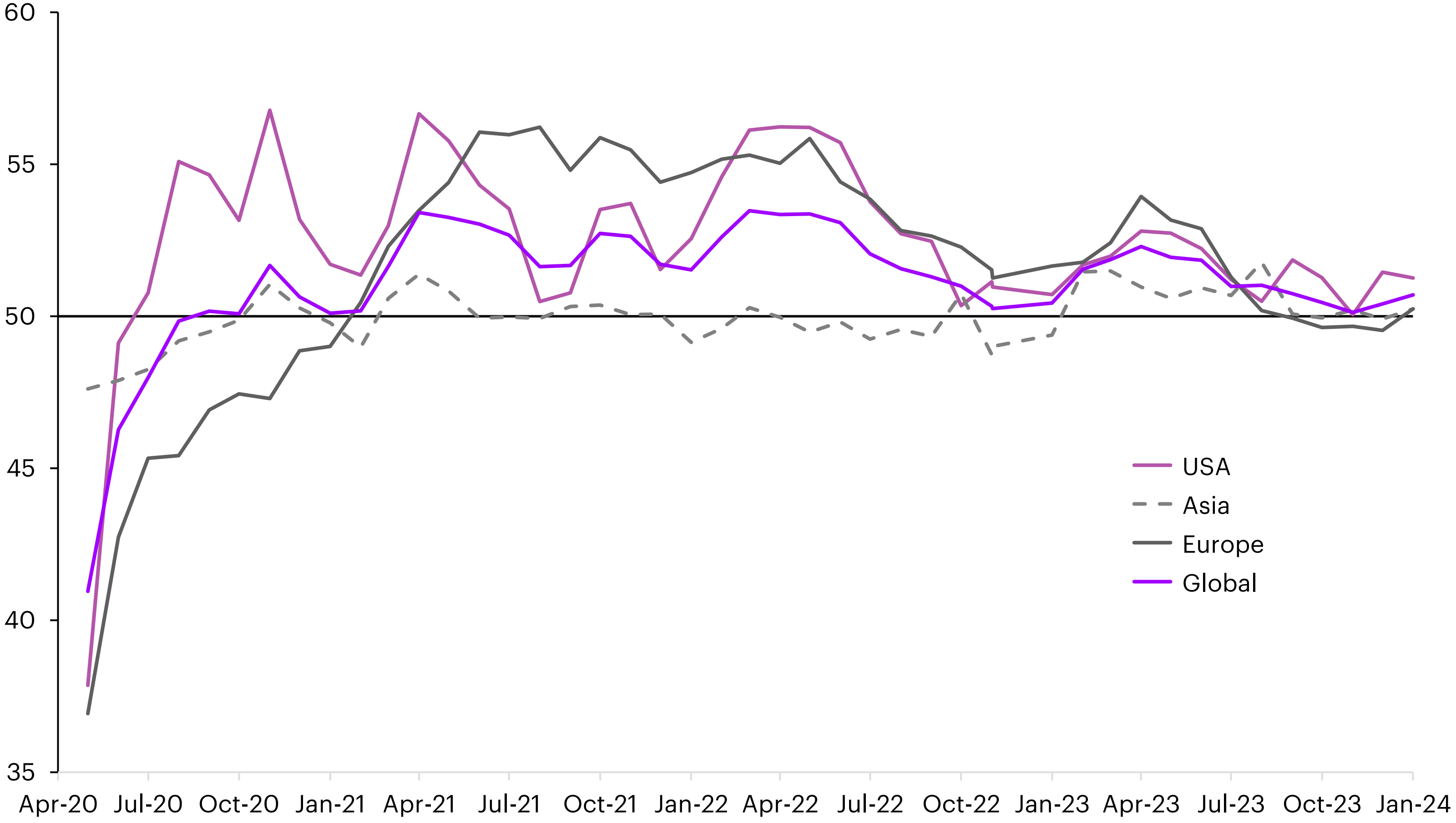
ok

Labor markets remain resilient as employment growth accelerated marginally in January

Employment growth

Aggregate PMI Employment Index

Index (>50=expanding employment)



Commentary

- In the US, employment growth decelerated in January after increasing in December
- Europe and the UK witnessed a marginal expansions in employment after contracting in December

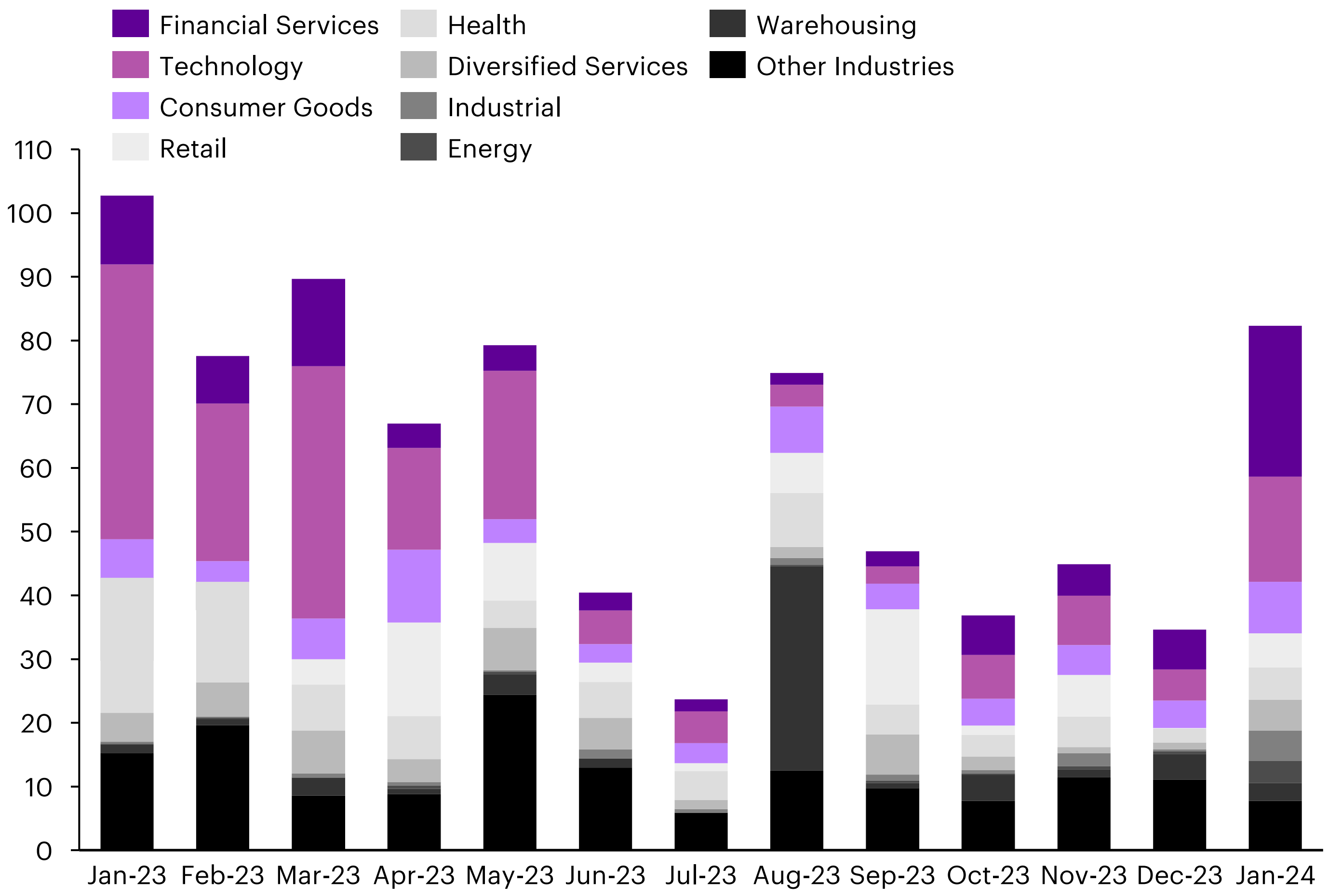
Source(s): S&P Global, BLS, Accenture Strategy analysis

US layoffs more than doubled in January, to the highest level in 10 months, as some employers in the technology and financial sectors launch restructuring efforts

US corporate layoff tracker

Announced layoffs by sector

Thousands (not seasonally adjusted)



Commentary

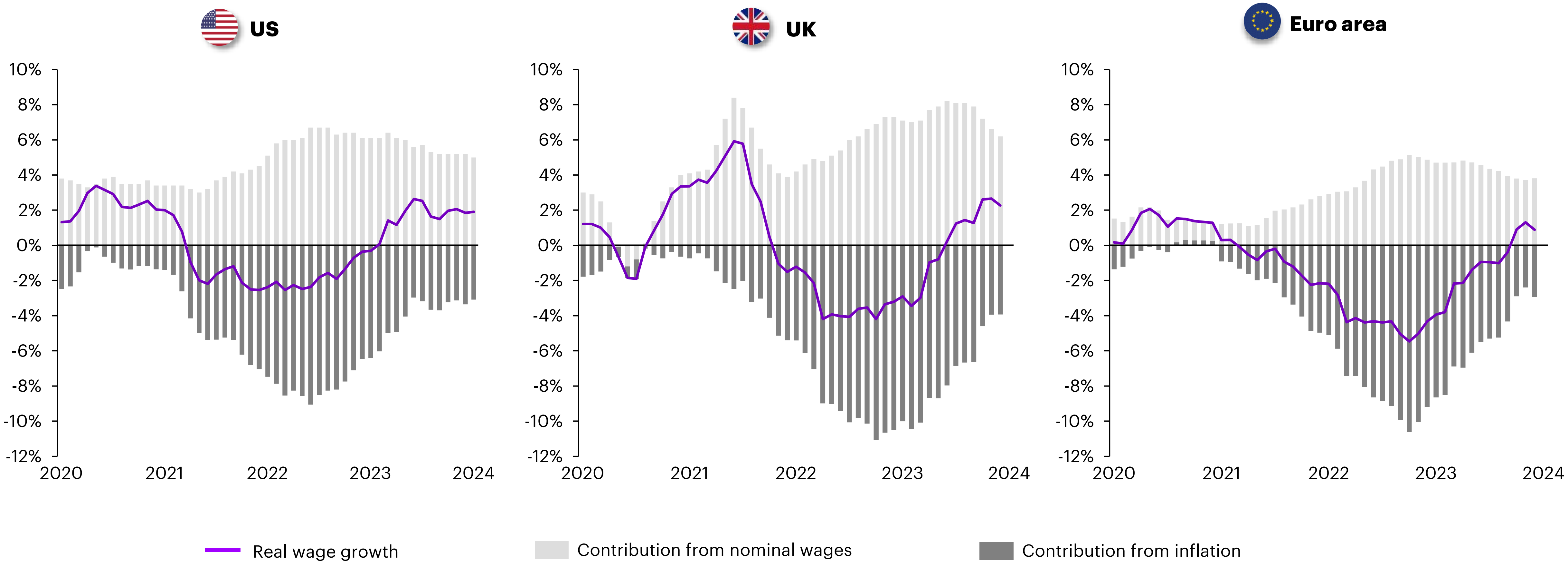
- The Financial sector led all industries in layoffs in January
  - PayPal Holdings Inc. announced a 9% cut of its workforce, citing a priority to "right-size" the company
- Technology companies announced the highest number of cuts in January since May 2023
- The layoffs appear driven by broader economic trends and a strategic shift towards increased automation and AI adoption in various sectors, though in most cases, companies point to cost-cutting as the main driver for layoffs

Source(s): Challenger Employment Report, Haver Analytics

Real wage growth is now in positive territory across the US, UK and Euro area amidst subsiding inflation

Wage growth developments

YoY % change in real wages and contributions to change (percentage points) from nominal wage growth and inflation

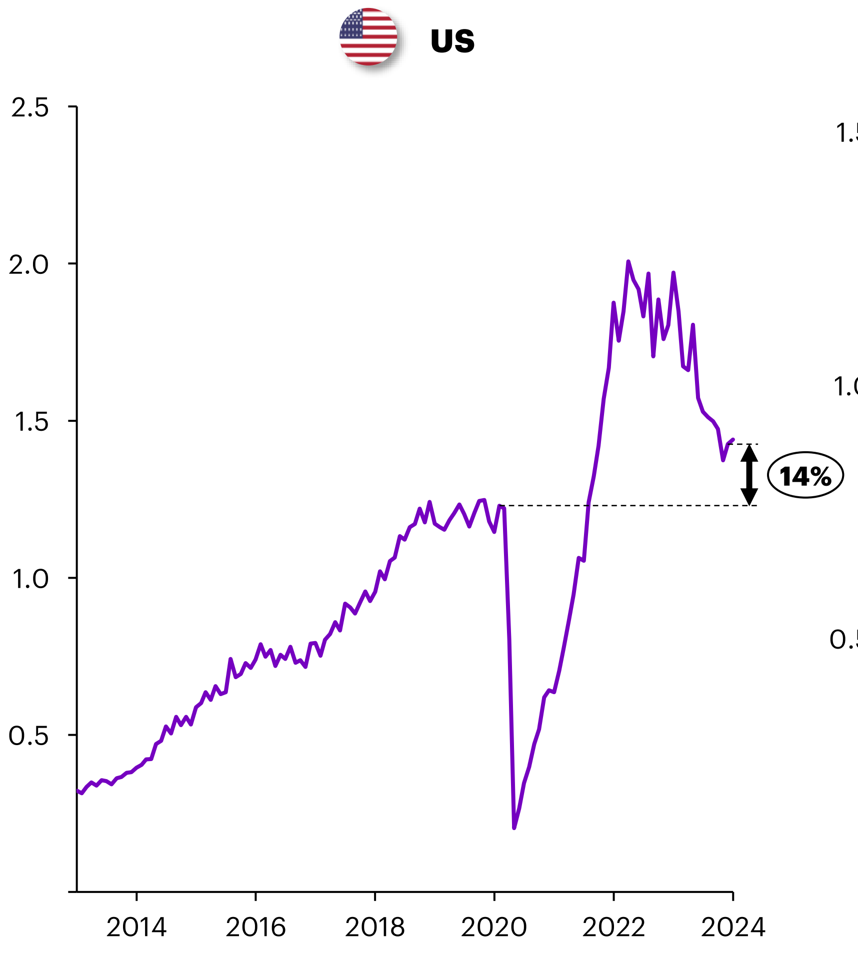


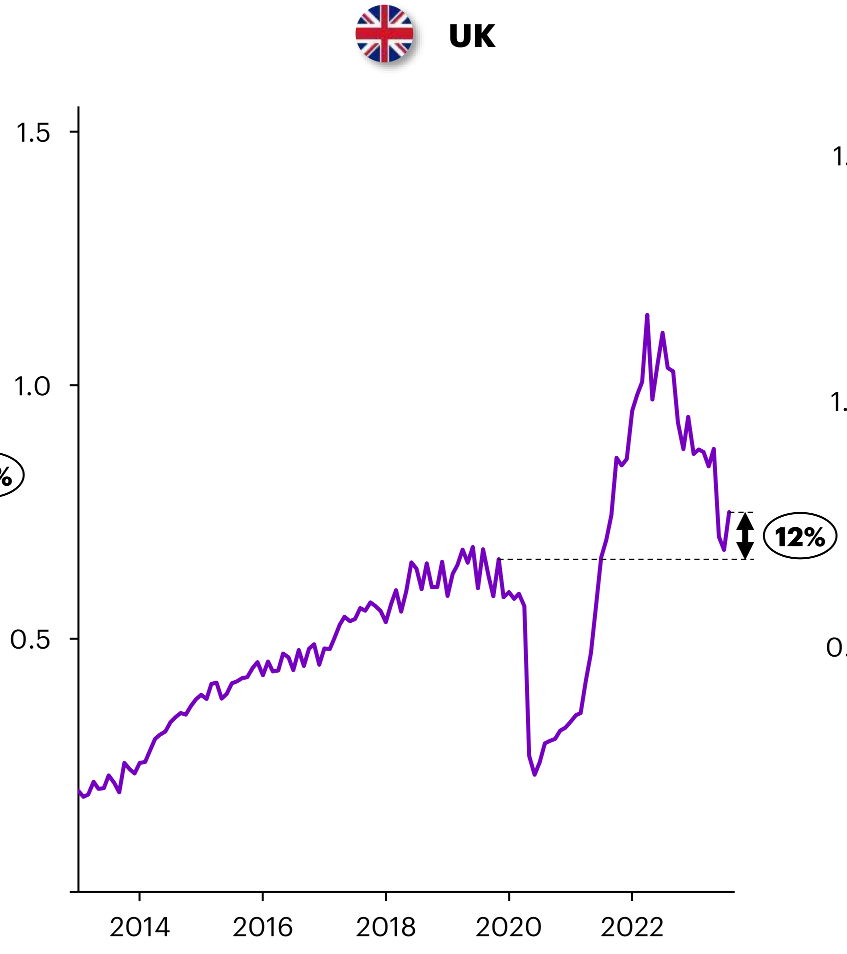
Source(s): BLS, ONS, Indeed, Accenture Strategy analysis

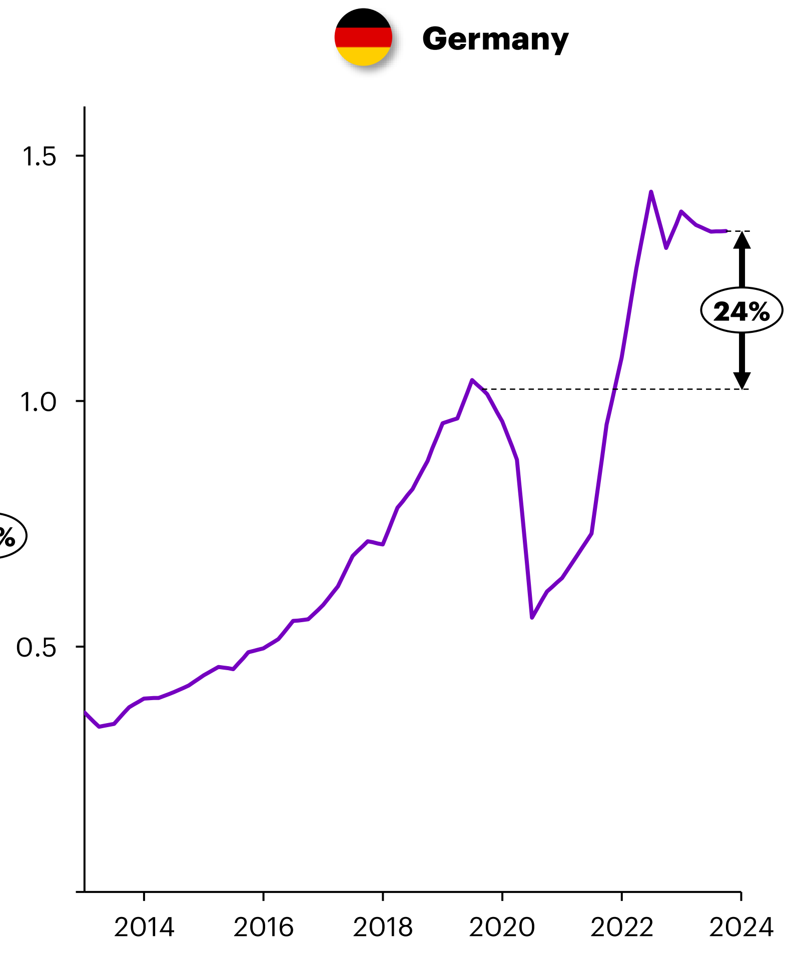
A difficult hiring environment (relative to pre-pandemic norms) persists across US and Europe, though labor market tightness has eased significantly in the US and UK

Labor market tightness

Job vacancies per unemployed person







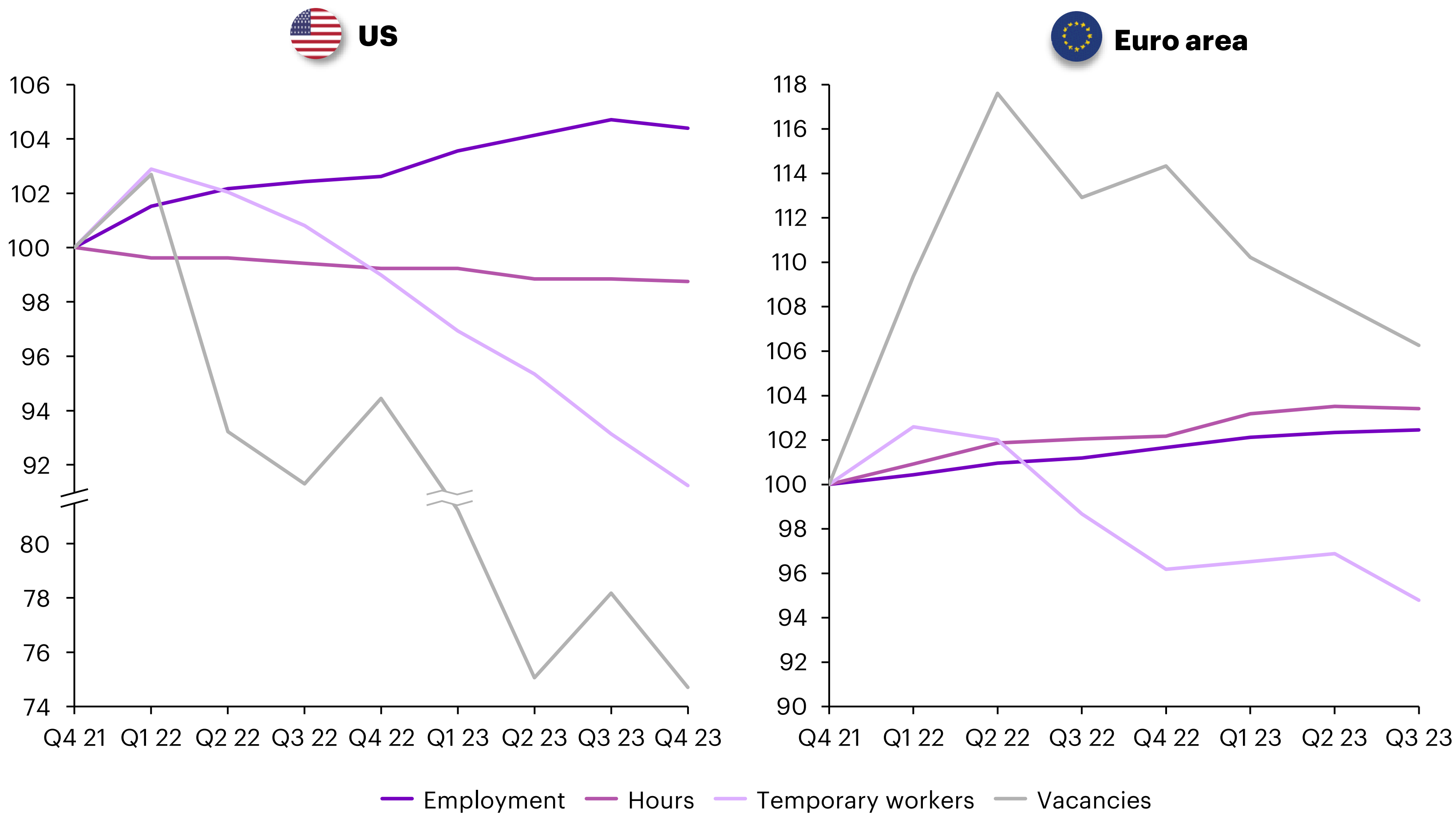
Source(s): BLS, ONS, Eurostat

In both US and Europe, worker hoarding remains prevalent and labor market adjustment is happening mainly through channels other than outright layoffs

Labor market indicators

Recent labor market movements

Index 100 = Q4 2021



Commentary

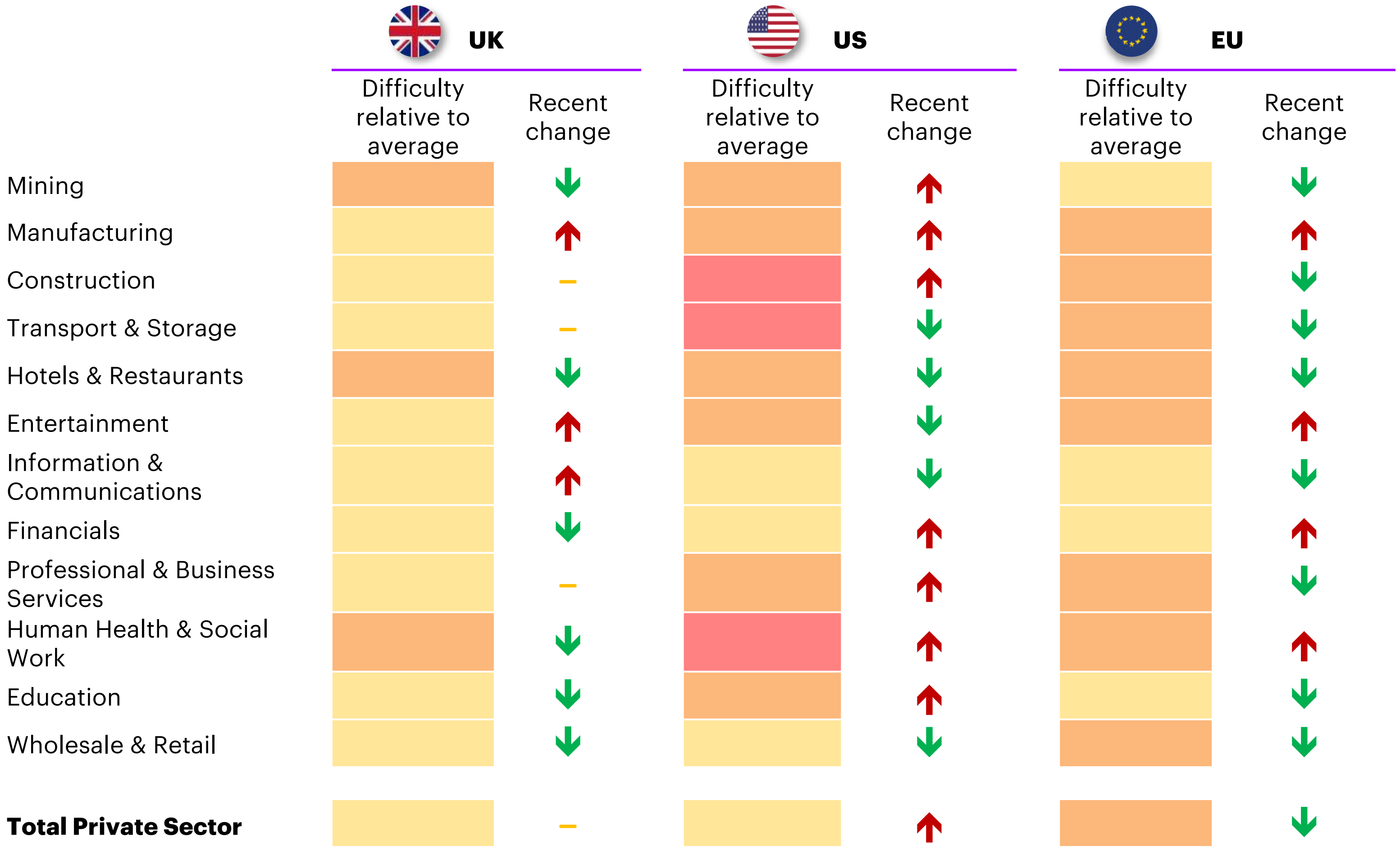
- While employment continues to remain high in the US, companies have been reducing hours and temporary workers to adjust to lower levels of demand
  - Job openings decreased slightly in Q4 2023, however, they increased in December after falling in the past two months
  - The number of people quitting their jobs was the lowest in nearly three years
- Just as labor markets in the Euro Area never quite reached the same levels of tightness witnessed in the US, they are slower to loosen in the current environment
  - Lower vacancies and increase in productive hours continue to be main channels of recent labor market adjustment

Source(s): Census Bureau, Bureau of Labor Statistics, Goldman Sachs Research, White House, Accenture Strategy analysis

Talent shortages remain most pronounced in the US while improving in the service sectors across UK and the EU

Relative difficulty of hiring by sector

Deviation in job vacancy rate from long-term average and recent trend (arrow)



Commentary

- Hiring difficulties are pronounced in the manufacturing and hotel and restaurant industries across the US, UK and EU
- While the difficulties have eased in the UK and EU, they are still pronounced in the US, particularly in construction and logistics

Difficulty finding labor (relative to long-term average)

More difficult — Less difficult

Note(s): Hiring difficulty in each sector is assessed by comparing average job vacancy rate in that sector over recent 3 months to its long-term pre-pandemic average (2012-2019). The recent trend (improving/worsening) is based on comparison of latest job vacancy rate to its average over the prior three months. UK and US analysis is based on monthly data, and EU on quarterly data.

Source(s): ONS, Eurostat, BLS, Haver Analytics, Accenture Strategy Analysis

Inflation

Disinflation momentum has slowed in the US and Europe; China continues to see outright deflation

CPI inflation rates and trends

Year over year change to CPI and point change from prior month

Country	YoY Inflation Rate	Change from previous month's rate (percentage points)
United States	3.1%	-0.3% ↓
United Kingdom	4.0%	0.1% ↑
Canada	3.4%	0.3% ↑
Germany	3.8%	1.5% ↑
France	3.5%	-0.7% ↓
Italy	0.9%	0.4% ↑
Spain	3.5%	0.1% ↑

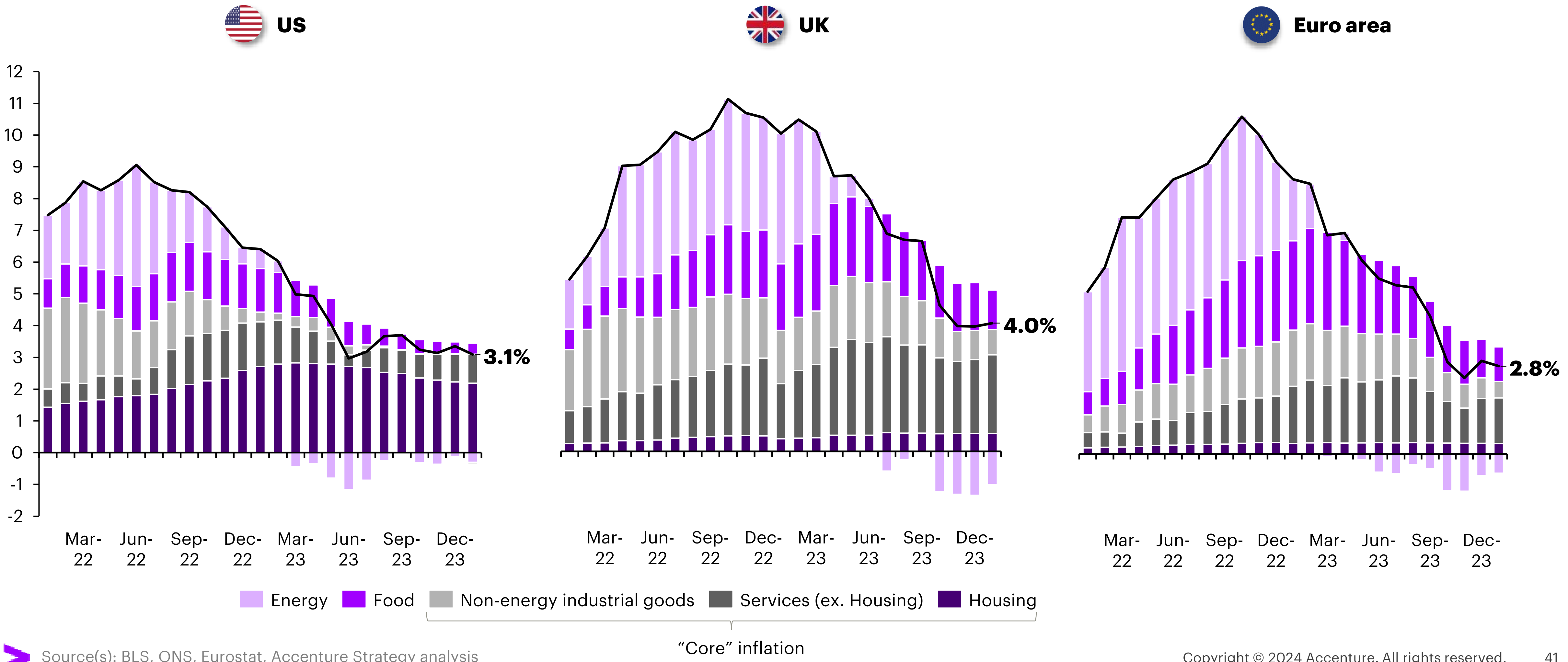
Country	YoY Inflation Rate	Change from previous month's rate (percentage points)
China	-0.8%	-0.5% ↓
Japan	2.6%	-0.2% ↓
Brazil	4.5%	-0.1% ↓
India	5.1%	-0.6% ↓
Singapore	3.7%	0.2% ↑
Korea	2.8%	-0.4% ↓

Source(s): BLS, ONS, Eurostat, Accenture Strategy analysis

Core inflation appears to be stabilizing at above-target levels in the US and Europe, reflecting ongoing stickiness in services prices

Drivers of recent CPI inflation

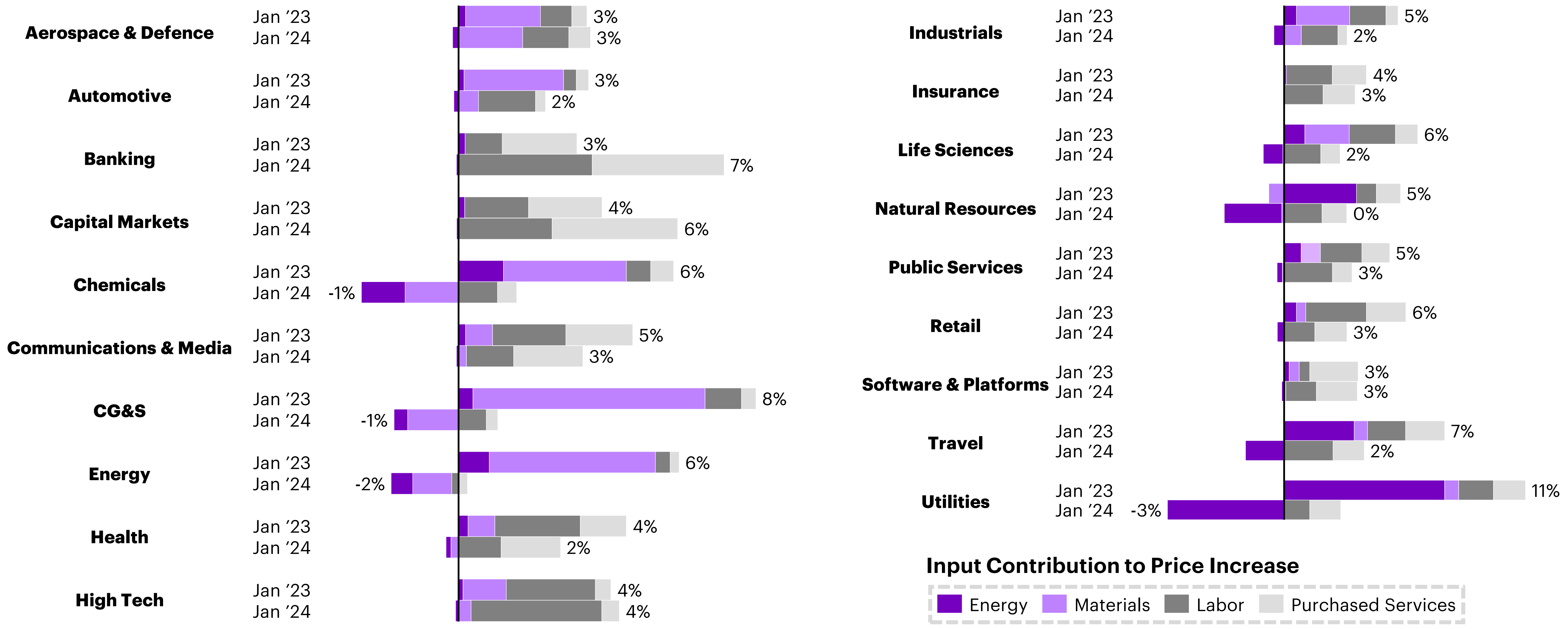
Year-on-year % change and % point contributions from major goods and services categories



Falling year-over-year materials and energy prices have reduced some of the input cost pressures across industries

Recent input cost inflation by industry

LTM year-over-year % change in input costs and contributions (percentage points) from key inputs, 2023

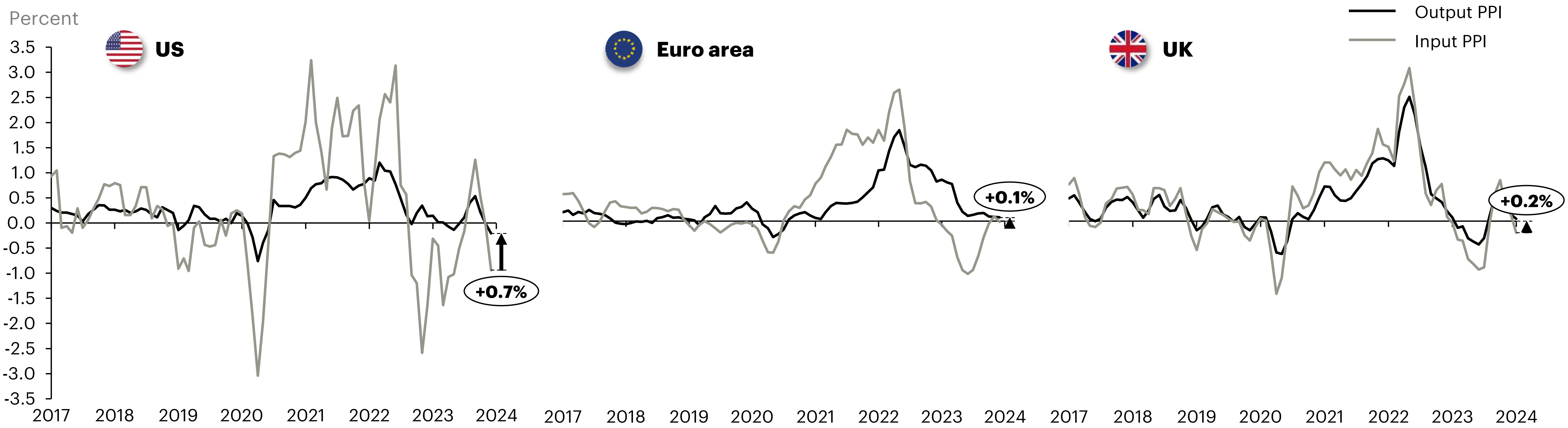


Note(s): Wage data as of Dec'23; Energy prices as of Jan '24 for Natural Gas, Nov'23 for Electricity and Jan'24 for Others; Materials and Purchased Services PPI price increases as of Jan'24.
Source(s): BLS, BEA, EIA, EPA, Accenture Strategy analysis

Companies in the US and Europe continue to be able to pass on their increase in input costs to customers

Company input cost pass-through trends

Producer price indices (PPI) for intermediate inputs and final outputs, 3 month moving average % change



Commentary

- The gap between cost increases for intermediate inputs (input PPI) and the change in producer selling prices for final goods (output PPI) is an approximate indicator of the extent to which producers have been absorbing their input costs increases
- In the US corporate margins have increased as input inflation pressures subsided

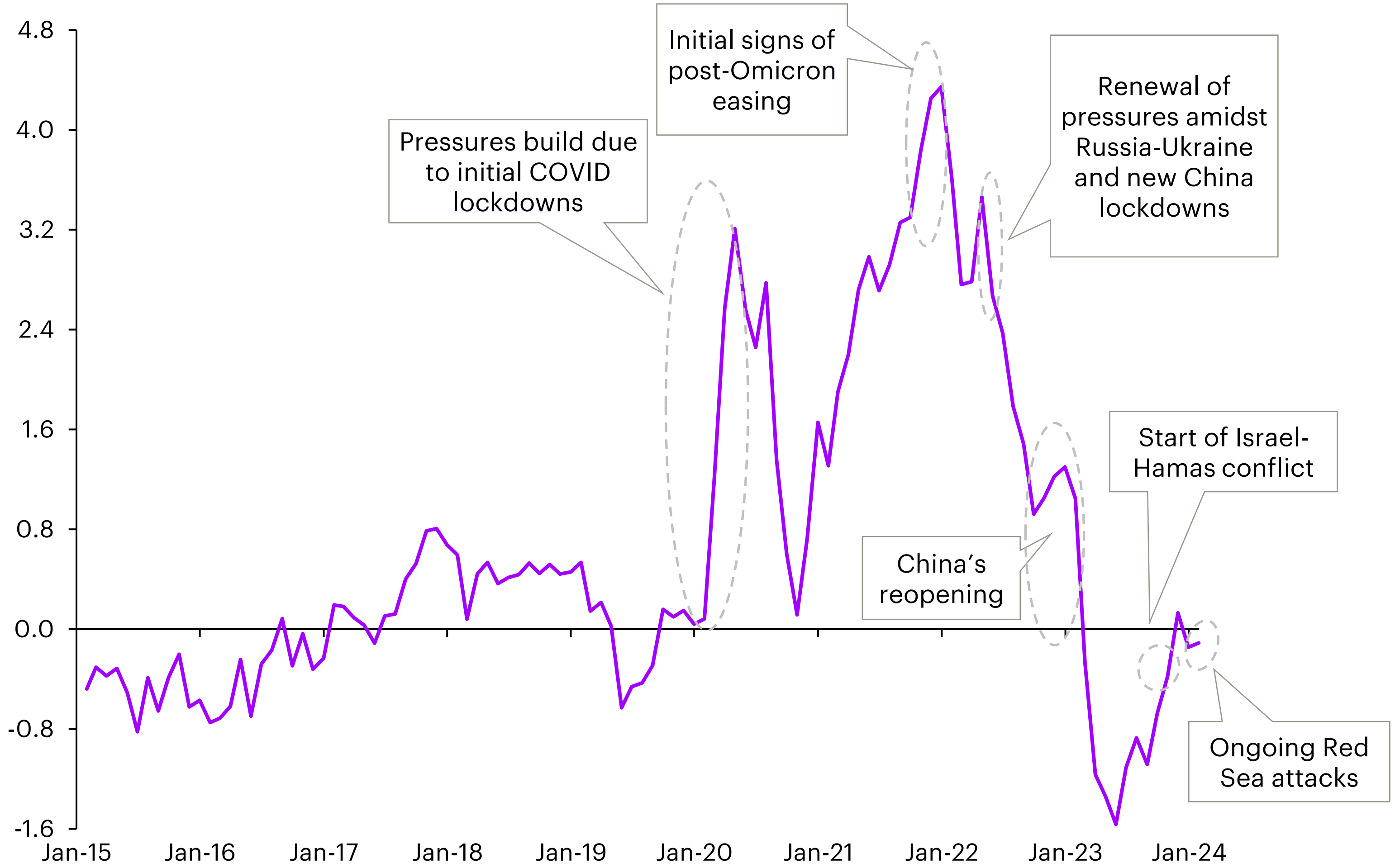
Note(s): 1) Figures in bold represent absolute percentage point difference between intermediate and final demand PPI YoY % values; higher positive values imply greater pass through to final producer selling prices, while larger negative values imply lower pass through. 2) US data is based on production flow classification for PPI, where Stage 2 intermediate inputs (shown in chart) feed into stage 3 production, stage 3 outputs serve as inputs to stage 4 production, and stage 4 provides inputs to final demand goods/services.
Source(s): BLS, ONS, Eurostat, Accenture Strategy analysis

Supply chains

Global supply chain pressures have now normalized to their pre-pandemic average

Global Supply Chain Pressure Index

Standard deviations from long-term average (=0)



Commentary

- Global supply chain pressures are settling near their long-run pre-pandemic average
- Going forward, risks are on the upside from the continued attacks by Houthi on the Red Sea passage, which could result in:
  - Increased shipping timelines with reduced access to the Suez Canal and re-routing through Cape of Good Hope
  - Spike in freight rates and insurance premiums

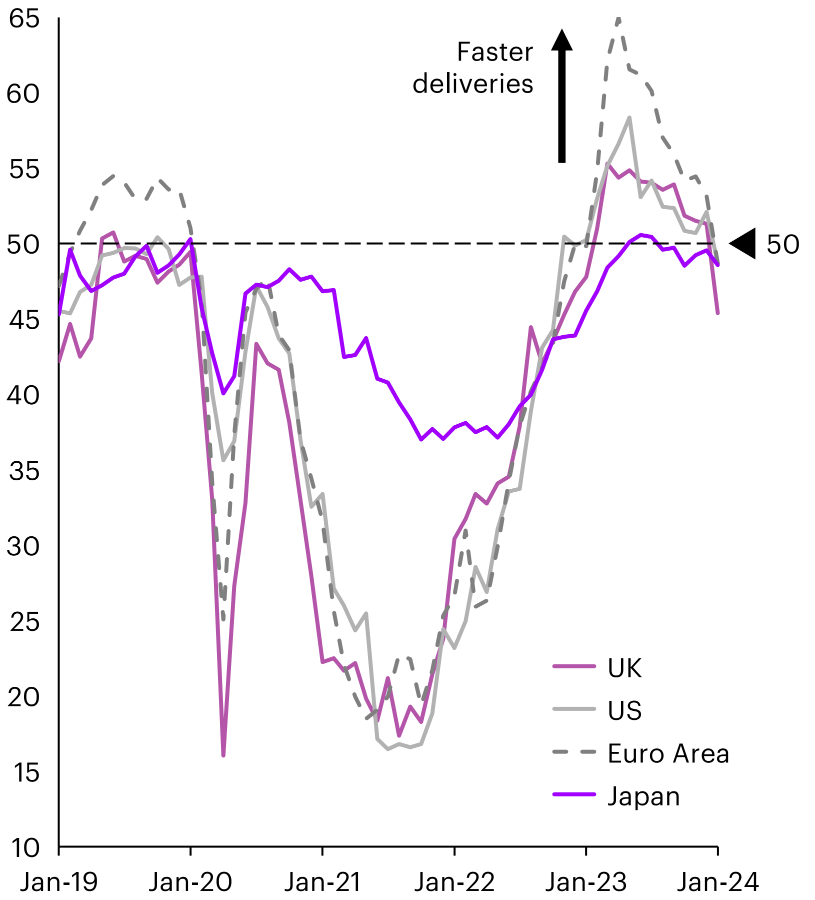
Source(s): Federal Reserve Bank of New York, Global Supply Chain Pressure Index, Accenture Strategy analysis

Global shipping delays due to the Red Sea crisis have lengthened suppliers' delivery times

Suppliers' delivery times and backlogs of work

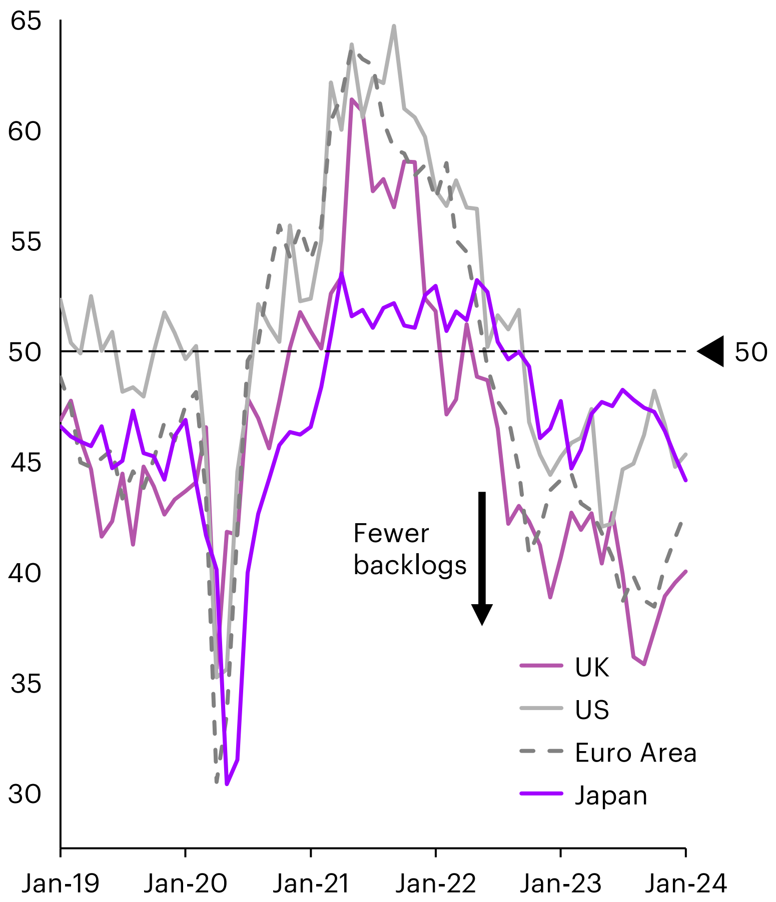
Suppliers' Delivery Times

Seasonally adjusted, 50+ = Increase



Manufacturing Backlogs of Work

Seasonally adjusted, 50+ = Increase



Commentary

- Supplier delays were overwhelmingly linked to longer international shipping times as vessels rerouted away from the Suez Canal in January, due to the Houthi attacks in the Red Sea
- The pace of work backlog clearance declined in Europe, which is especially exposed to the Red Sea shipping disruptions, but increased in Japan

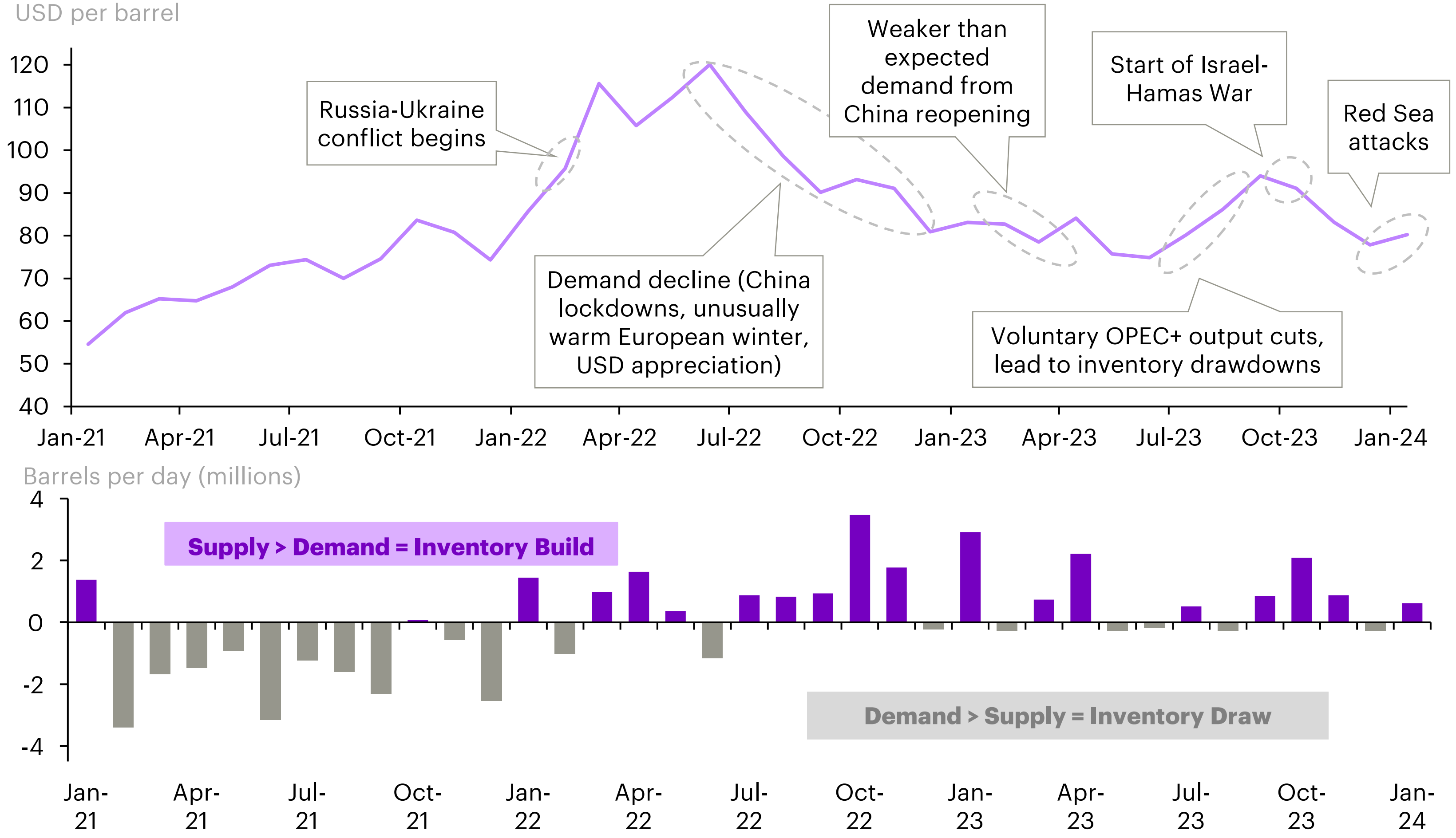
Source(s): CIPS/S&P Global, Haver Analytics, Thomson Reuters, Accenture Strategy analysis

Energy and commodities

Oil prices stabilized in February as supply shocks were offset by the slowdown in the global economy and weakening oil demand

Crude oil prices and inventories

Brent crude oil spot prices (upper panel) and global inventory changes (lower panel)



Drivers of energy prices in 2024

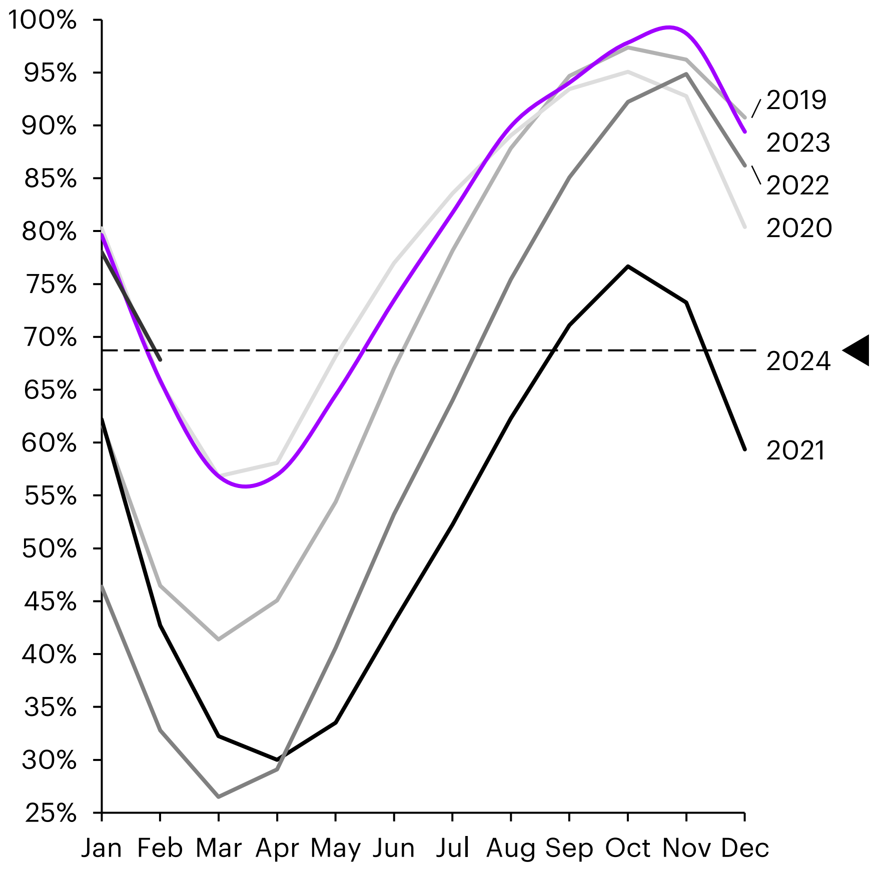
- Oil prices stabilized in February as global oil demand growth lost momentum towards the end of 2023 and the pace of expansion is set to decelerate further
- Going forward, upside and downside pressures to prices appear broadly balanced, with:
  - Oil supply shocks after an Arctic blast shut in production in North America and as OPEC+ deepened output cuts
  - Record output from the US, Brazil, Guyana, and Canada will help boost non-OPEC+ supply
  - Escalating geopolitical tensions in the Middle East could lead to further upward price pressure

Note(s): Monthly average of crude oil price UK Brent 38` API (USD per barrel)
Source(s): Energy Information Agency, World Bank, Bloomberg, Haver Analytics, Accenture Strategy Analysis

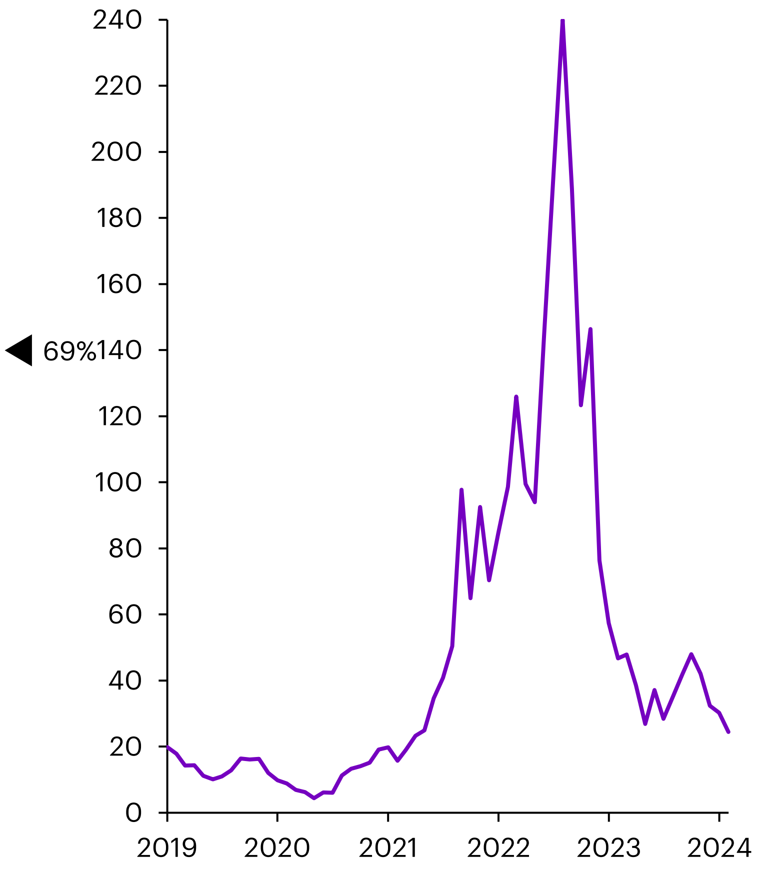
EU gas prices dipped again in early February and are facing less upward pressures amidst record storage levels and sluggish economic activity in Europe

EU natural gas reserves and prices

European gas reserves are relatively high at 97%...



with prices dipping amidst sluggish demand



Commentary

- Northwest Europe is roughly two-thirds of the way through the winter heating season, with a record volume of gas in storage for the time of year, which is putting downward pressure on gas prices
  - Storage facilities were still 67% full compared to a ten-year seasonal average of 49%
- Natural gas prices in Europe dipped again in early February, marking the 4th straight month of price fall, with chances of further contraction driven by
  - Further demand slowdown across the Euro area
  - Warmer-than-average temperatures across the Northern Hemisphere, leading to lower domestic demand
  - Strong performance of renewable energy sources and nuclear power generation

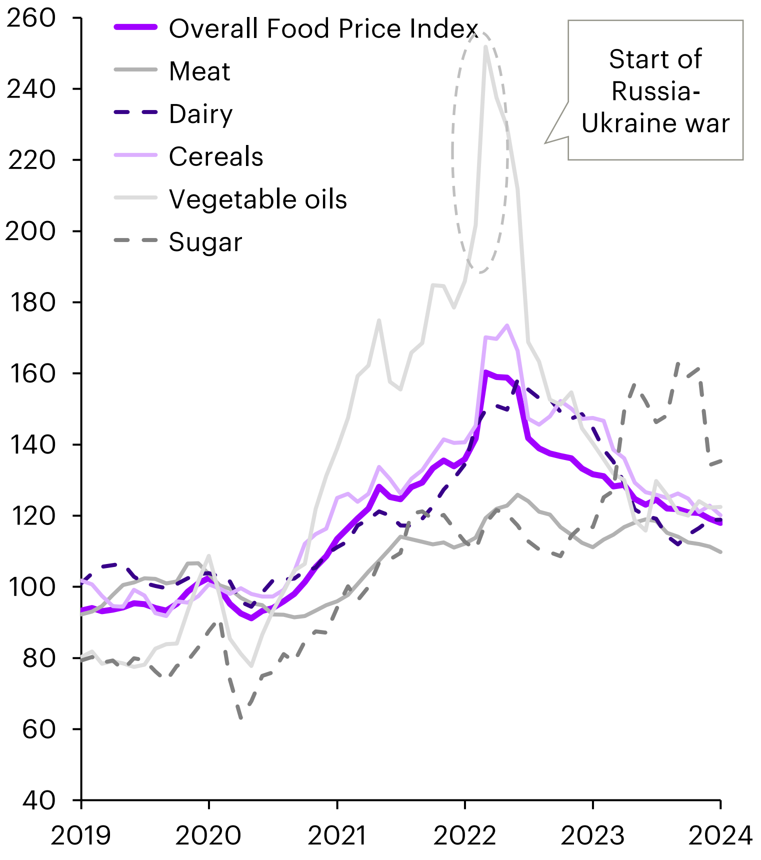
Note(s): Dutch TTF Natural Gas Futures front-month contract. TTF stands for Title Transfer Facility, which is a virtual trading hub for natural gas in Europe. TTF prices represent the average monthly price of natural gas traded at this hub and are considered a benchmark for natural gas prices in Europe.
Source(s): Gas Infrastructure Europe, Bloomberg, European Council, Reuters, Investing.com, Accenture Strategy analysis

Overall food and fertilizer prices fell marginally in January

Food and fertilizer prices

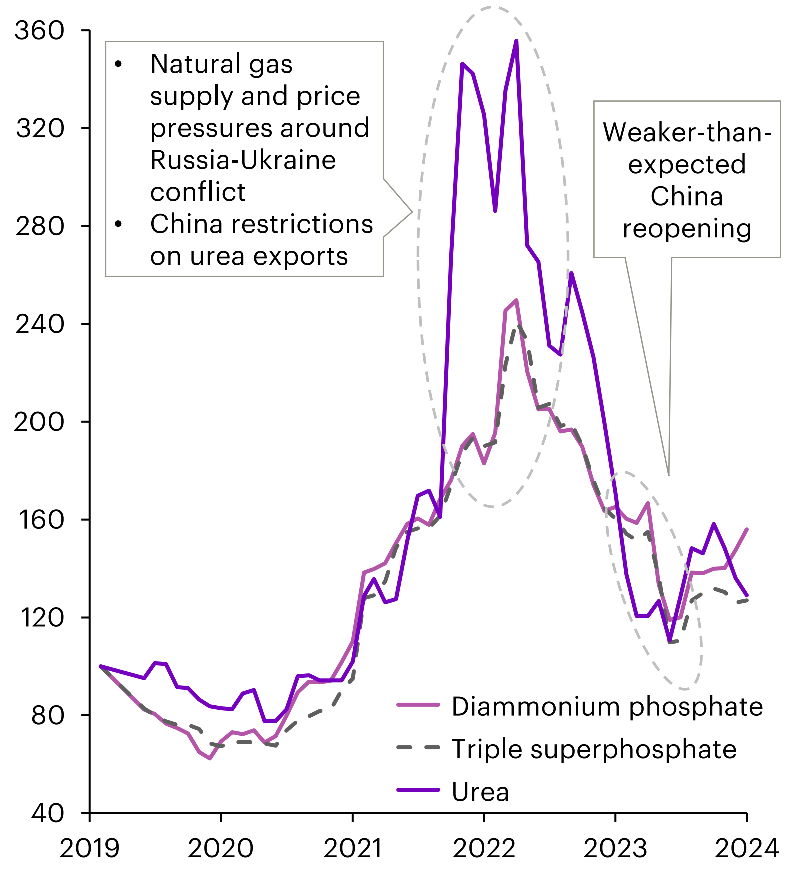
Food prices

Index, 2014-2016 = 100



Fertilizer prices

Index, Jan 2019 = 100



Commentary

- Overall food commodity prices fell further in January, as decreases in the price indices for cereals and meat more than offset an increase in the sugar price index, while those for dairy and vegetable oils registered only slight adjustments
- Sugar prices were up again after they fell significantly in December (to an 8-month low) driven by
  - concerns over the likely impact of below-average rains in Brazil on sugarcane crops to be harvested from April
  - slow start of the new season and unfavorable production prospects in Thailand and India (two major sugar producing countries)

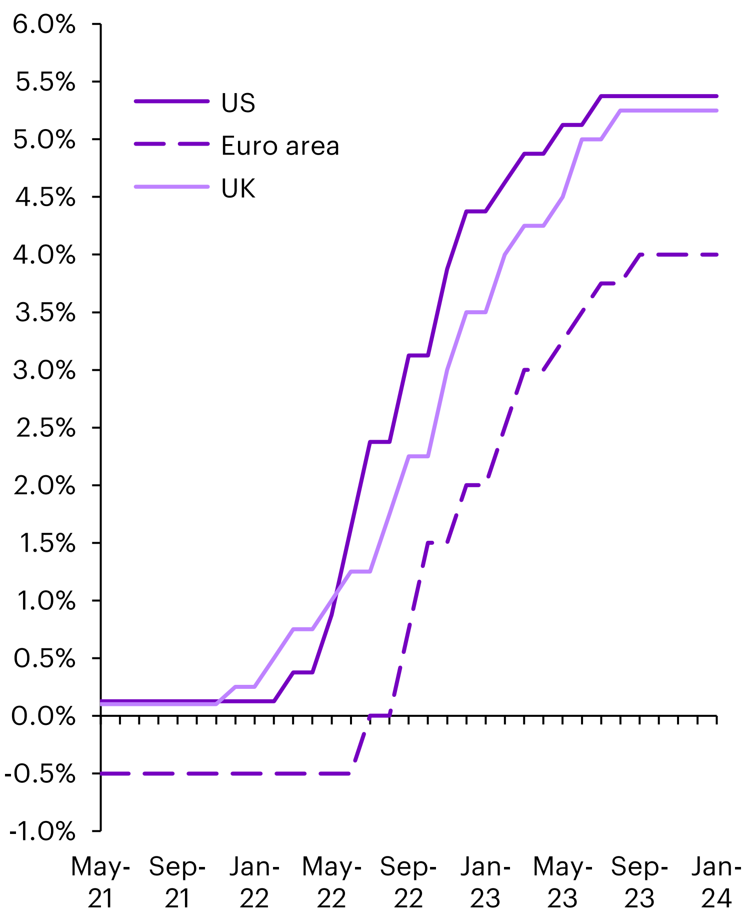
Note(s): (a) Food Price Index is a measure of the monthly change in international nominal prices of a basket of food commodities (b) Fertilizers include DAP (diammonium phosphate), TSP (triple superphosphate), and Urea.
Source(s): World Bank, UN FAO, USDA, Bloomberg, Accenture Strategy analysis

Financial markets

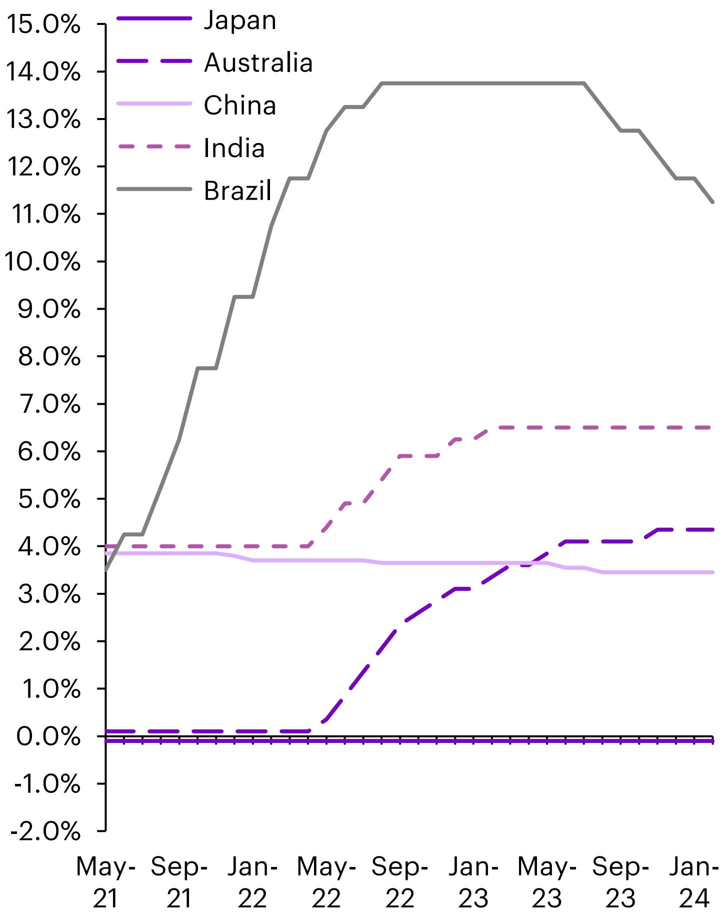
Most central banks are pausing to evaluate evolving conditions before initiating rate cuts

Monetary policy across major economies

US, UK and Euro area policy rates



Policy rates for other major economies



Commentary

- The Fed left rates unchanged in January, making it the 7th straight month without any rate change
- The ECB kept its key policy rates unchanged in January and reaffirmed its commitment to fighting inflation, though it has signaled rate cuts are in sight
- The Bank of England held its policy rate steady in January, keeping the rates high for getting the inflation to get back to 2% sustainability
- In its latest policy meeting on January 23, the Bank of Japan maintained its ultra-easy settings, pointing to "extremely high uncertainties"
- China's central bank cut its 5-year prime loan by 25bp to help relieve pressures on the ailing property sector, but kept its 1-year rate unchanged
- Brazil's central bank cut its benchmark rate by another 50bp in February on the back of continued disinflation progress

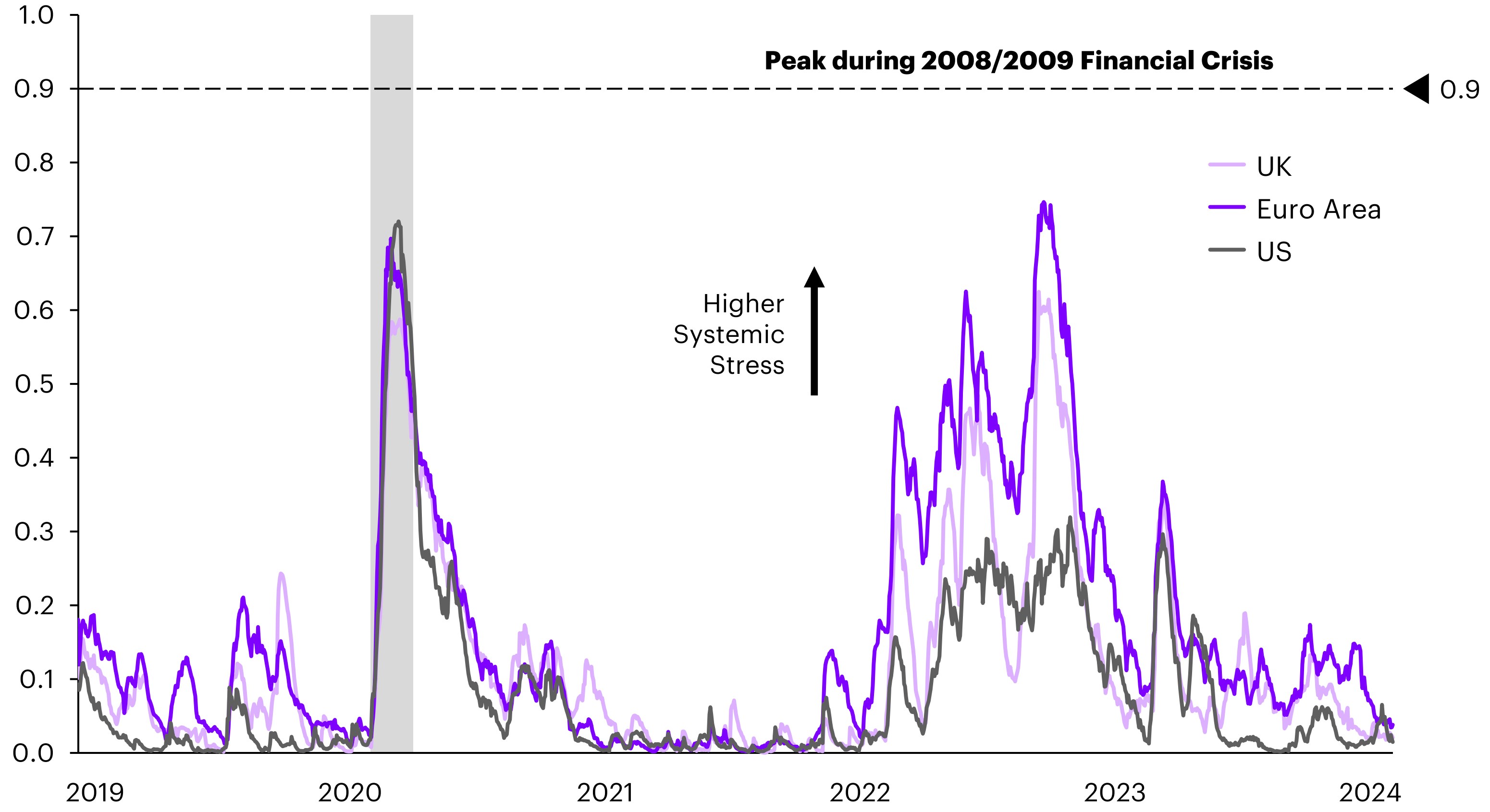
Source(s): Federal Reserve Bank, European Central Bank, Bank of England, Bank of Japan, Reserve Bank of India, Central Bank of Brazil, Reserve Bank of Australia, People's Bank of China, Accenture Strategy analysis

Systemic financial stress in major economies has generally remained subdued since peaking during the wave of bank failures in early 2023

Systemic financial stress indicators

Composite Indicator of Systemic Stress Index

(No Stress = 0, High Stress = 1)



Commentary

- Systemic stress levels in the US and Europe remain well below their most recent peak in March 2023
- Elevated financial pressures are likely to persist in 2024 amid
  - Ongoing interest rate uncertainty
  - Distress in certain sectors where banks have large exposure (e.g., commercial real estate)
  - Heightened geopolitical tensions

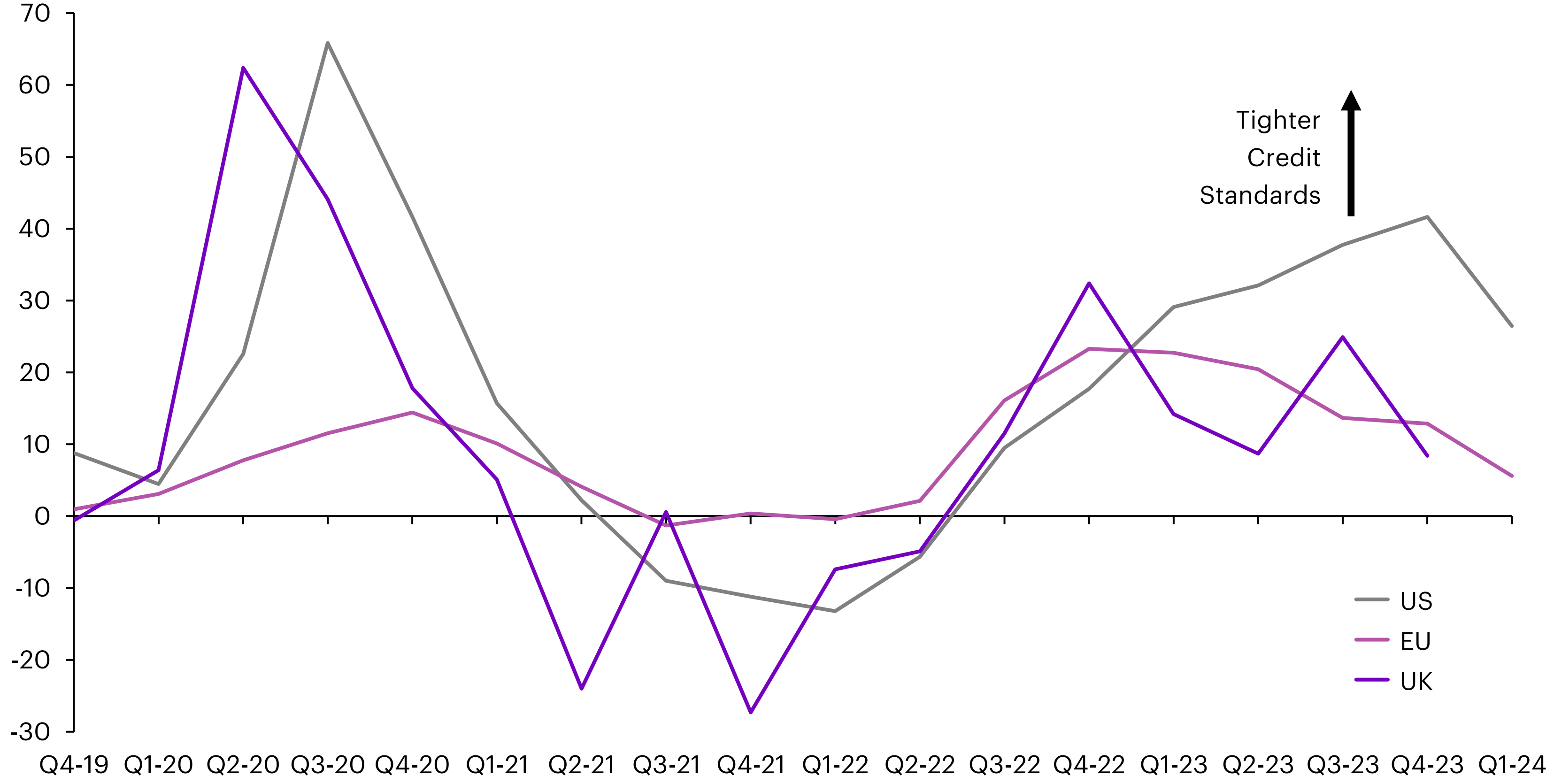
Note(s): (1) The composite indicator of systemic stress consists of market-based financial stress measures that namely covers the financial intermediaries sector, money markets, equity markets, bond markets and foreign exchange markets (2) Grey shading reflects U.S. recession
Source(s): Haver Analytics, European Central Bank, Accenture Strategy analysis

There continues to be net tightening of lending standards among banks in the US and Europe, with risks of a broader credit crunch if CRE distress intensifies

Restrictiveness of banks' lending standards

Banks are tightening their credit standards in tandem with monetary tightening

Index of weighted net change in credit standards (tightening standards > 0)



Note(s): The date of each datapoint refers to the quarter in which the bank lending survey was conducted but reports the assessment of credit conditions in the prior quarter. Lending standards for US and EU reflect a weighted index constructed using select survey questions to measure tightening or loosening standards to both households and enterprises. UK lending standards series based on inverted series of use of credit scoring

Source(s): Haver Analytics, EU Bank Lending Survey, BoE, Board of Governors of the Federal Reserve System, Accenture Strategy analysis

Commentary

- Monetary policy tightening since early 2022 has been leading banks to scale back lending and tighten their credit standards
- US banks continued to tighten credit standards in Q4 '23 for credit card loans and construction and land development loans, citing expected deterioration in collateral values, a less favorable economic outlook, an expected deterioration in credit quality
- In the EU, there was a moderate net further tightening in credit standards for loans to firms, with more tightening expected in the first quarter of 2024
  - Demand for loans by firms and households continued to decrease substantially, albeit less steeply than in the previous quarter
  - Bank lending conditions tightened more in real estate and construction than in other sectors

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The team has hubs in Europe, the United States, and Asia and its members have prior experience working for governments, investment banks, asset managers, multilateral institutions and large corporates to bring a global, multi-disciplinary perspective to problem-solving. Visit us at www.accenture.com/macroforesight.

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