January Macro Brief

Special edition: 2024 outlook and top 10 macro trends

January 22, 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 **January 18, 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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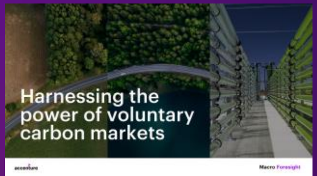

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Contents

Executive Summary

2024 promises to be year of transitions, new normals and reckonings with the consequences of accumulated imbalances

Executive Summary (1/2)

Global economic outlook for 2024

- **The key theme for the global economy in 2024 will be the transition from the post-pandemic normalization cycle to a new normal governed by changing structural realities.** Cyclical impulses that still have more room to run in 2024 include:
  - **Tailwinds:** (1) further disinflation for goods that were supply-constrained during the pandemic; (2) rebounding labor supply relieving labor market tightness; and (3) recovering real incomes supporting consumer spending, tempered by households' fatigue from still-high prices
  - **Headwinds:** (1) post-pandemic normalization of consumer spending turning from tailwind to headwind amidst fading pent-up services demand and dwindling excess savings; (2) residual lagged effects of past interest rate hikes; (3) ongoing slump in global manufacturing; and; (4) unwinding of pandemic and cost-of-living-related fiscal support measures
  - On balance, these cyclical winds are likely to be a drag on growth but supportive of disinflation
- **As the year progresses, the global economy will increasingly feel the pull of structural forces that dampen long-term growth prospects and drive renewed inflation pressure and volatility:**
  - **A global supply squeeze** on essential production inputs, including labor (due to demographic shifts), energy and commodities (particularly critical minerals), compounded by growing constraints on their access as geoeconomic fragmentation increases
  - **Higher long-term interest rates**, driven by the unwinding of decade-long central bank QE programs, rising term premia, and large public and private investment needs related to net zero transitions, technology adoption and supply chain resilience
  - **A new normal of geopolitical instability** that fuels increased supply, policy, and physical and cybersecurity uncertainty
  - **A global fiscal reckoning** as governments' post-pandemic debt and deficit overhangs force increased fiscal restraint and potential cutbacks to critical public investments (e.g., old-age related welfare programs, net zero transitions, military and resource security)
- **The net result is most likely to be a continued downshift in global growth and a further retreat in inflation to lower but still-elevated levels.** A persistence of above-target inflation due to structural cost pressures may constrain some central banks' ability to pivot to rate cuts to buttress slowing growth, leading to "higher-for-longer" scenarios and sustained financial pressures on firms and households
  - This remains a key reason why some economies (particularly in Europe) may still dip into or remain in mild recession, or struggle with more prolonged stagnation
- **Given the sheer number of cross currents at play, this transition from a cyclical to structural economic regime may prove bumpy and a source of ongoing volatility and downside risk.** A see-saw in economic momentum and sentiment is likely to be a key feature throughout 2024:
  - Already in January, inflation readings (for Dec 23) showing moderation in the pace of disinflation, coupled with growing anxiety about prolonged Red Sea shipping disruptions, have led markets to dial back expectations over the aggressiveness of interest rate cuts in 2024

Source: Accenture Strategy analysis

Companies must be prepared to navigate GenAI, the lagged effects of higher rates, and growing geopolitical risks in 2024

Executive Summary (2/2)

Regional perspectives

- **Growing geographic divergence is expected** as regions and countries come out of their normalization cycles at varying speeds and are impacted differently by structural headwinds depending on their economic and financial structures, trade links, and geopolitical alliances
- **The outlooks for major economies over the next 12 months therefore remain uncertain and best framed as probabilistic scenarios:**
  - The base case for the **US** is a "weakflation" scenario—a consumer-led downshift in growth and persistence of above-target inflation due to supply-side cost pressures, though the upside possibility of a soft landing has increased
  - In **continental Europe**, continued growth stagnation or mild recessions are most likely, with the more energy-intensive and manufacturing-led economies such as Germany at higher risk of weaker outcomes
  - The **UK's** dip into negative growth in late 2023 is most likely to give way to a tepid recovery in 2024, constrained by high rates and still-cautious consumers; an alternative scenario where the economy remains trapped in a cycle of rolling mild recessions is a risk
  - **China's** growth is expected to trend down towards a new, lower normal amidst structural challenges—e.g., property and financial market deleveraging, demographic headwinds—though more aggressive policy stimulus could prop up growth and delay this transition
  - Among advanced APAC economies, **Japan** is set for sluggish growth 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; **Australia** also faces a subdued growth outlook amidst ongoing lagged impacts of high rates and drag on exports from China's slowdown
  - In **emerging markets in Asia and Latin America**, the outlooks vary but are generally more favorable for the net commodity exporting economies (as geopolitical and climate risks keep commodity prices elevated), as well as those that have already embarked on rate cutting cycles; easing local currency pressures if Fed starts to loosen monetary policy should also help EMs more broadly

Considerations and priorities for companies

- **The focus for companies in 2024 should shift from last year's priority of preparing for a high risk of global recession, to planning how to adapt and operate in an emerging new normal** of growing geographic divergence, greater supply-side constraints, higher and more volatile inflation, tighter financial conditions, and elevated geopolitical uncertainty.
- **Key strategies companies can pursue to navigate this evolving global context include:**
  - Plan for divergent sales strength in geographic markets and across different consumer demographics
  - Maintain business plan agility and optionality in a context of still-high uncertainty, underpinned by strong scenario planning
  - Be opportunistic in strategic M&A
  - Invest in productivity, notably GenAI, to help overcome structurally-higher cost pressures
  - Build more resilience in supply chains and networks
  - Invest in strong risk management and government relations capabilities

Source: Accenture Strategy analysis

Companies remain uncertain over how long recent US economic resilience can persist, and increasingly anxious about geopolitical risks

Top of mind issues among clients

"How do we develop a multi-year strategy if higher interest rates persist?"

"The data says US economy is growing but our customer demand is down. What's driving the disconnect?"

"Has the US economy avoided a recession?"

"When will the resilience of the US consumer start to fade?"

"How could an escalation of conflict in the Middle East impact our business?"

"What are the top geopolitical risks we should be monitoring in 2024?"

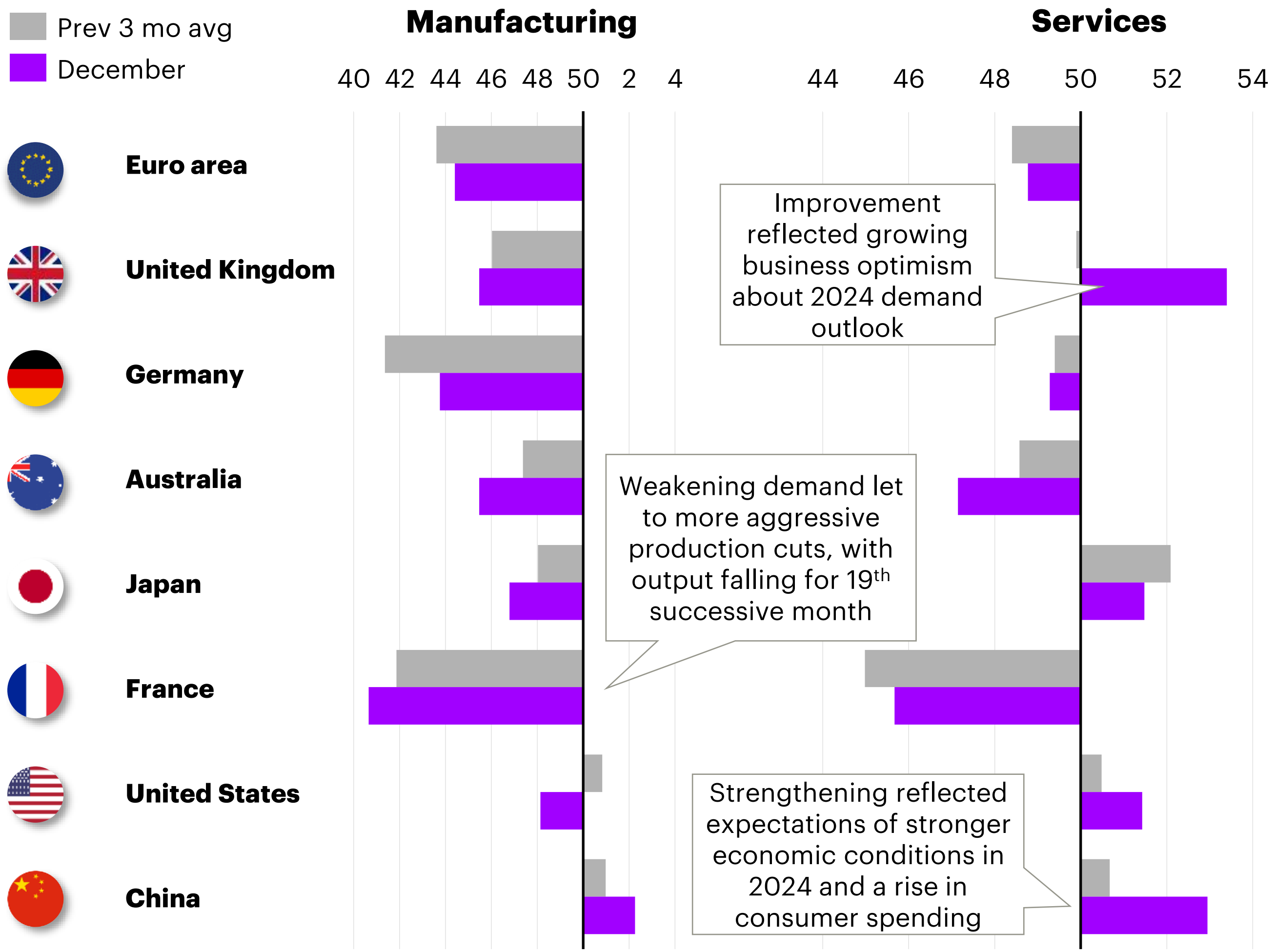
"When will M&A activity start to pick up? Where can we be opportunistic?"

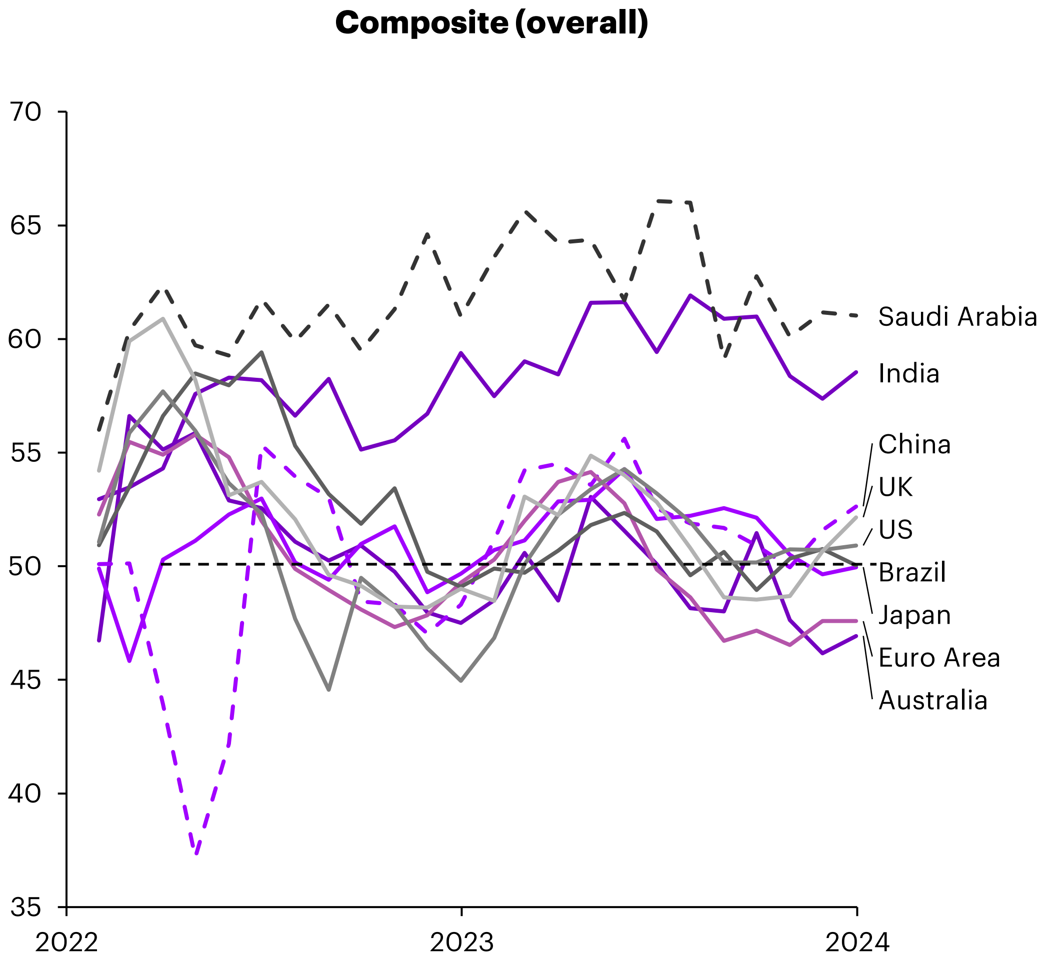
Source: Based on recent client conversations in December and January.

2024 Economic Outlook

Most major economies closed out 2023 with sluggish activity momentum, though there was some notable improvement in China and the UK and continued resilience in the US

PMI survey country snapshot



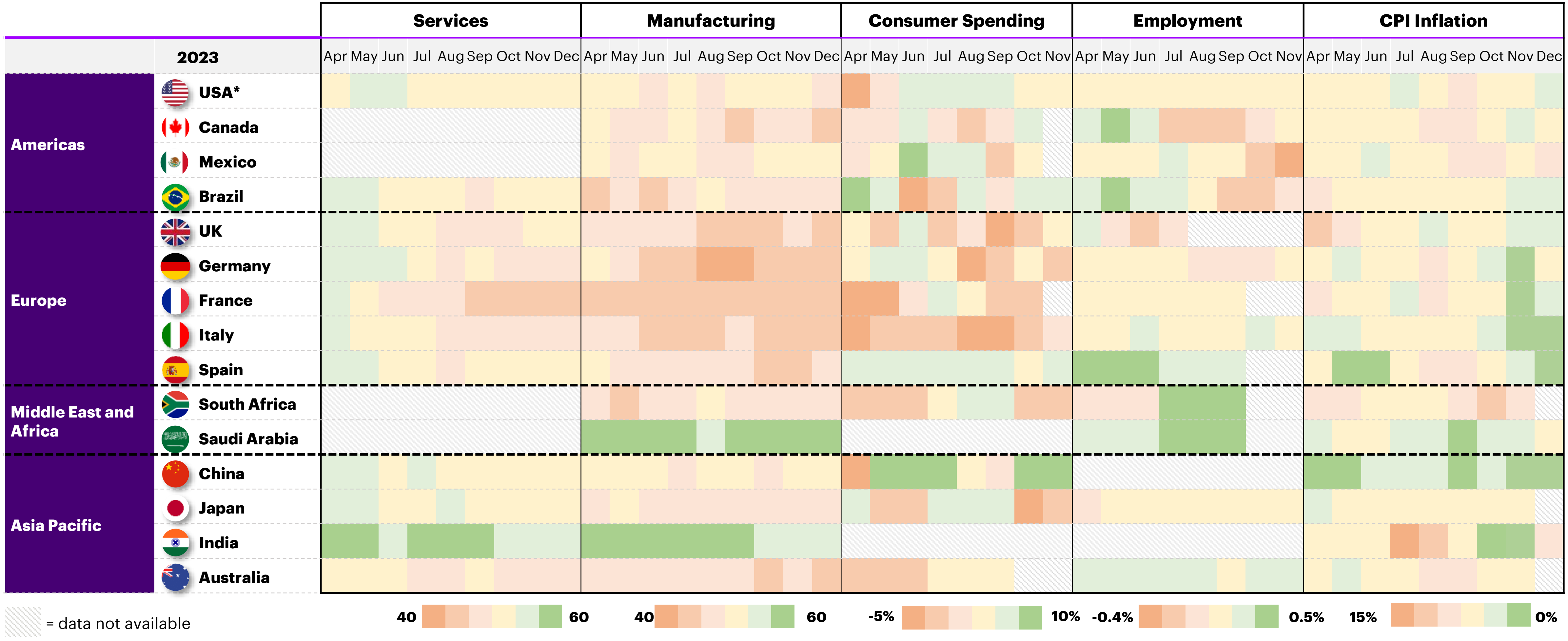


Note(s): A survey score above 50 indicates expansionary business activity and a score below indicates business activity contracted that month, most recent results may include preliminary flash figures
Source(s): S&P Global, Accenture Strategy analysis

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 JAN 18

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

Looking ahead, several cyclical impulses from prior years still have room to run in 2024 and, on balance, are expected to be a drag on growth but supportive of disinflation

Residual cyclical impulses affecting near-term outlook

NOT EXHAUSTIVE

Tailwinds

Goods price disinflation 	• Further price disinflation for goods that were particularly supply-constrained during the pandemic, such as autos and consumer electronics
Rebounding labor supply 	• Labor supply in US and Europe has been benefiting from rebounding immigration (incl. refugees) and people returning to labor force to offset their real income squeeze • Continuation of these trends should help further relieve labor market tightness
Recovering real income growth 	• Real incomes are again growing in many countries as inflation and continued labor market strength keeps wage growth solid • This should be a positive impulse for consumer spending, albeit tempered somewhat by households' cost fatigue (as price *levels* remain well-above pre-pandemic norms even as their rate of inflation slows)

Headwinds

Post-pandemic normalization of consumer spending 	• Final phase of this process will see the tailwind of pent-up services demand dissipate (as services rebounds are now fairly mature in most economies) and be overtaken by headwinds from – Remaining downward normalization of US consumer goods spend to pre-pandemic levels – Rise in household savings rates as excess savings buffers dwindle
Lagged effects of past rate hikes 	• Stronger residual impacts are expected in countries where there was less floating-rate debt and stronger household and corporate balance to help cushion the initial impacts of rising rates
Manufacturing slump 	• Global manufacturing momentum remains weak, reflecting in large part the global rebalancing of demand from goods to services spending rebalancing • The decline may start to bottom out in H1 given the sizeable destocking in 2023 and need for companies to recalibrate inventories
Unwinding of fiscal support 	• Most governments are now phasing out the last of their pandemic-time stimulus measures and cost-of-living relief-programs (e.g., energy subsidies) introduced during peak of recent inflation cycle

Source: Accenture Strategy analysis

As 2024 progresses, emerging structural forces will exert increasingly greater pull on the global economy, weighing on growth and renewing inflation pressures and volatility

Structural forces shaping the emerging “new normal”

NOT EXHAUSTIVE

	Forces	Description
	**Great supply squeeze**	• Tightening global supply of essential production inputs, including: – labor (due to declining and aging populations in many major economies) – energy (e.g. underinvestment in oil & gas) and critical minerals (limited extraction and refining capacity) – agricultural commodities (climate change and growing frequency of disruptive climate events) • Increasingly-constrained access to these inputs as geoeconomic fragmentation increases
	**Higher long-term interest rates**	• Even if central banks start to ease short-term rates, longer-term interest rates will nonetheless face structural upward pressures from (among other things): – Unwinding of decade-long central bank QE programs – Rising term premia amidst growing uncertainty about future growth, inflation and monetary policy – Growing large public and private investment needs related to net zero transitions, technology adoption and supply chain resilience
	**A new normal of geopolitical instability**	• Geopolitical warfare is increasingly becoming the norm rather than the exception – Key manifestations include armed confrontations, proxy conflicts, weaponization of resources and technologies, and economic statecraft such as sanctions and trade barriers • Major risks for 2024 include the spread of Israel-Hamas war to wider Middle East and prolongation of Russia-Ukraine conflict, which threaten renewed resource and supply chain disruptions
	**Fiscal reckoning**	• Public debt levels are at record highs in many countries after successive waves of pandemic-related spending and cost of living support to combat high inflation • These precarious fiscal positions are likely to: – Limit the scope for additional stimulus should economic conditions deteriorate further – Force more difficult public spending tradeoffs—e.g., balancing the need to finance strategic investments (net zero transition, resource security) with market pressures for fiscal consolidation

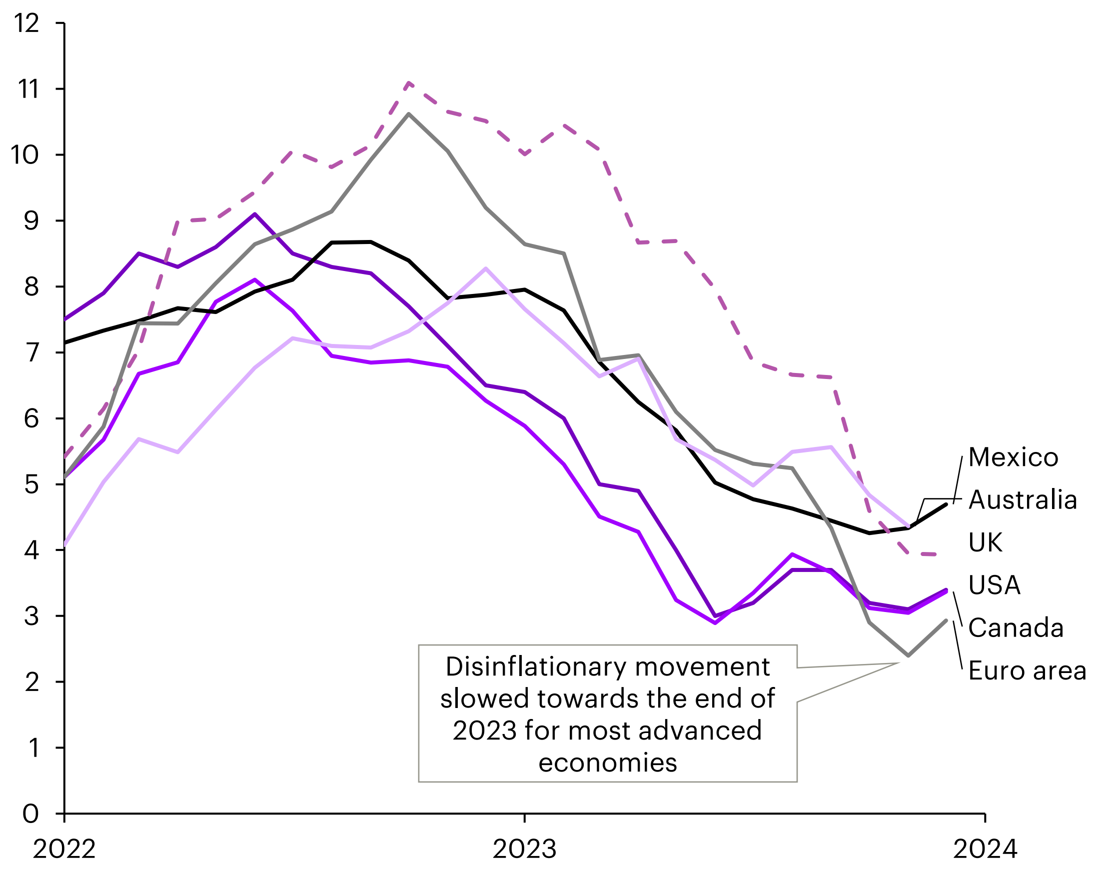
Source: Accenture Strategy analysis

Downside risks for 2024 are already emerging, with recent Red Sea shipping disruptions driving up freight costs and threatening to further slow disinflation momentum

Moderating disinflation and rising shipping costs

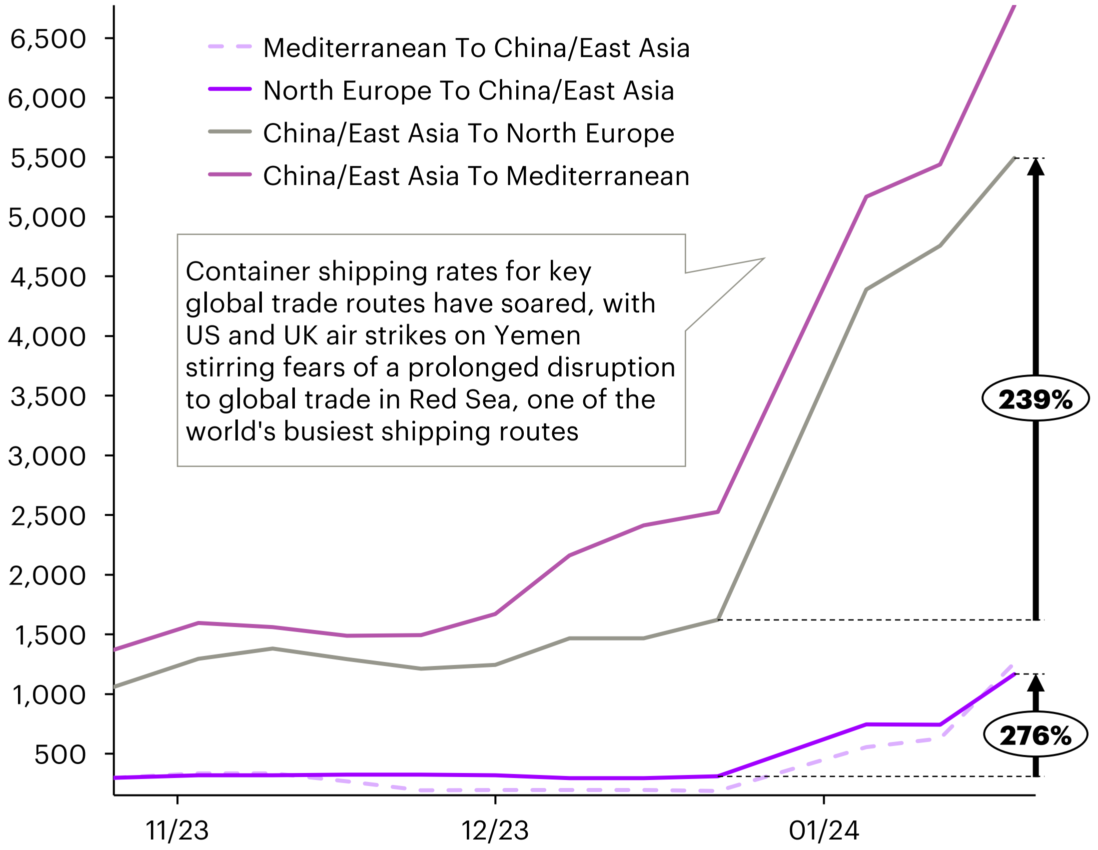
Disinflationary momentum has slowed

CPI Inflation - year-on-year % change



Impact of Red Sea attacks on freight shipping rates

Freight container pricing index (Nov'23 to Jan'24)



A significant growth downshift and above-target inflation due to structural cost pressures is base case for US economy, though upside possibility of a soft landing has increased

US near-term economic outlook and key scenarios

Economic scenario	Soft landing	Weakflation	Mild recession
Description	• Recent disinflation momentum brings inflation back to 2% target without significant further deterioration in consumer spending or labor market • Fed eases rates slightly to fine-tune its policy stance to lower inflation	• Loss of post-pandemic normalization impulse and lagged effects of past rate hikes drive growth to below-trend or near-zero pace (<1%) • Supply-side cost pressures keep inflation above target, at 3-4% • Fed maintains "higher-for-longer" policy stance	• A sharp drop-off in consumer spending accelerates labor market cooling and drags growth into mildly negative territory • Substantial Fed rate cuts, particularly if growth decline occurs alongside spike in financial sector stress
Key scenario drivers and assumptions	• Household and corporate financial buffers absorb residual impact from rate hikes • Continued recovery in labor supply	• Intensifying economic drag from past rate hikes • Recurring inflationary shocks from tight energy and commodity markets • Continued labor unrest and wage pressures	• Abrupt consumer spend downshift as excess savings depleted • Geopolitical conflict(s) trigger renewed supply chain disruptions • Credit stress episode
Corporate implications	• Stabilizing margins • Easing labor and financing costs	• Further margin erosion from cost pressures and weaker pricing power	• Rising bankruptcies denting B2B demand and household finances

Most likely (Weakflation)

What to watch for

- **Consumer spending inflection point:** A potential drop-off in consumer spending amidst depletion of households' excess savings, rising delinquency rates on consumer credit (especially subprime segments), and deteriorating housing affordability
- **Wage stickiness:** Robust ongoing employment growth, loss of momentum in recent labor supply recovery, and further organized labor unrest could keep wage pressures elevated even as inflation falls
- **Election cycle standoffs and disruptions:** A potential government shutdown in Q1 and policy uncertainty in run-up to November elections could disrupt economic activity and dent household and business confidence
- **Credit stress episodes and associated spillovers:** An acceleration of defaults in financially-stressed pockets of the economy—commercial real estate, consumer subprime credit card and auto loans, leveraged corporate loans—may spillover to broader corporate and household financing conditions

Source: Accenture Strategy analysis

Continued stagnation or mild recessions are most likely throughout Europe, with the more energy-intensive and manufacturing-led economies at higher risk of worse outcomes

Continental Europe near-term economic outlook and key scenarios

Economic scenario	Soft landing	Stagflation	Mild recession
Description	• Continued disinflation and rebounding consumption and investment lift economies out of recent stagnation • ECB, BoE and other central banks support recovery with rate cuts	• Continued growth stagnation that is more pronounced in energy- and manufacturing-intensive economies • Supply-side cost pressures hinder "last mile" of disinflation • Central banks maintain "higher-for-longer" policy stance	• Adverse cocktail of elevated inflation, weak external demand, and drag from past rate hikes keeps/drives growth negative • Substantial central bank rate cuts, particularly if growth decline occurs alongside spike in financial sector stress
Key scenario drivers and assumptions	• Households dipping more aggressively into their savings buffers • Reversal of recent manufacturing slump	• Continued precautionary household saving • Ongoing economic drag from past rate hikes • Persistence of elevated energy prices	• Ongoing weakness in Chinese demand for European exports • Geopolitical conflict(s) trigger renewed supply chain disruptions • Sovereign debt stress
Corporate implications	• Stabilizing growth and recovering investment • Easing financing costs	• Further margin erosion • Financial breaking point for many "zombie" firms	• Rising bankruptcies denting B2B demand and household finances

Most likely

What to watch for

- **Household savings behavior:** Unlike in US, European households have been reluctant to draw on their excess savings buffers, possibly in anticipation of further economic deterioration; continued precautionary saving would keep consumption muted
- **Residual hit from past rate hikes:** Due to greater use of variable-rate financing in Europe than in US, transmission of monetary tightening to economy has been quicker, but peak impact may still be ahead
- **Withdrawal of fiscal support**: How households respond to phasing out of energy subsidies and other residual pandemic-time fiscal support measures will be key to consumer spending outlook
- **Industrial policy implementation.** Failure to ratify or fund planned industrial policy initiatives could reinforce Europe's eroding industrial competitiveness and dampen prospective rebound in exports
- **Sovereign debt stress:** Uncertainty around upcoming elections and budget outcomes in high-debt countries (e.g., Italy, UK, France) could trigger spikes in sovereign borrowing costs

Source: Accenture Strategy analysis

A tepid growth recovery, constrained by high rates and still-cautious consumers, is most likely for UK, with downside risk that economy gets stuck in cycle of rolling mild recessions

UK near-term economic outlook and key scenarios

Economic scenario	Buoyant recovery	Sluggish recovery	Rolling mild recession
Description	• Economy emerges from its contraction in H2:23 and rebounds swiftly alongside continued disinflation • BOE supports recovery with gradual rate cuts	• Muted recovery to below-trend growth rate • Supply-side pressures drive ongoing labor market tightness and above-target inflation • BoE maintains "higher-for-longer" policy stance	• Reversal in recent disinflation momentum triggers further consumer retrenchment, preventing a durable growth recovery • Large BOE rate cuts
Key scenario drivers and assumptions	• Improving real incomes drive rebound in consumer confidence and spending • Contained wage-price spiral • Easing of housing affordability pressures amidst declining rates	• Real wage squeeze • Lowered Ofgem energy cap limits energy inflation pass- through to consumers • No cross-sectoral contagion • BOE rate cuts take longer than market expects	• Sharper consumer sentiment drop • Geopolitical conflict(s) trigger renewed supply chain disruptions • SMBs cut costs and hold-on to cash • BOE rate cuts unable to revive growth
Corporate implications	• Continued steady demand and recovering margins	• Weak consumer demand • Limited recovery in housing, retail spending • Persistent margin squeeze	• Stagnating top-line growth • Possible cash challenges to vulnerable firms
		Most likely	

What to watch for

- **Government fiscal policy:** In an election year, the government may provide tax relief but will have to walk a fine line as too much fiscal expansion will run counter to monetary tightening and risk re-igniting inflationary pressures
- **Trade impact:** UK's large dependence on imported energy and other geopolitically-sensitive commodities leave it at high risk of another bout of imported inflation; on the other hand, UK services industry is benefitting from recent strength in global services trade
- **Bank of England (BOE) policy:** BOE's hawkish stance relative to other European central banks and strong focus on keeping inflation expectations anchored may lead to rates remaining higher for longer
- **Consumer sentiment.** UK consumers have already cut back retail spend to lowest levels since COVID; a lowered energy cap kicking in and slowing inflation might provide more room for spending to rebound later in the year, but persistence of higher interest rates may continue to pressure household incomes (most mortgages in UK are short-term or floating-rate)

Source: Accenture Strategy analysis

Deceleration towards a new, lower structural growth rate is base case for China, though more aggressive policy stimulus could help stabilize growth

China near-term economic outlook and key scenarios

Economic scenario	Growth stabilization	Deceleration to new normal	Deflationary stagnation
Description	• Aggressive policy stimulus temporarily counteracts structural headwinds and keeps growth stable around 5% in near term	• Growth continues to trend down towards the slower (3-4%) potential rate associated with China's materializing structural challenges	• Significant downshift in growth reinforcing negative spiral of eroding consumer confidence, entrenched deflation, and financial and property sector spillovers to economy
Key scenario drivers and assumptions	• Improving consumer confidence • More aggressive fiscal stimulus and monetary policy loosening • Continued surge in "New Three" and auto exports	• Subdued consumer confidence and ongoing precautionary savings • Weak external demand keeping manufacturing spare capacity high • Cautious and measured policy stimulus • Slow burn of property sector retrenchment	• Falling consumer spending • Surge in real estate-related defaults • Significant deterioration of external demand (e.g., US recession) • Escalation of Western restrictions on trade with China
Corporate implications	• Rebound in goods and services spending • Easing financing costs	• Prolonged lower growth and investment • Margin erosion	• Potential contagion from property sector • Glut of export goods
		Most likely	

What to watch for

- **Property market spillovers:** Property sector challenges continue to unfold slowly but threaten to spill over into adjacent sectors, in addition to impacting general consumer confidence
- **Extent of policy stimulus:** China's government has been reluctant to deploy large-scale stimulus to contain debt risks, but may step up support if growth begins to slow sharply
- **"New Three" export strength:** China's exports of EVs, batteries, and solar cells have been surging the past 2 years, buoyed by government incentives for their production, which could help offset export weakness in traditional manufacturing goods
- **Local government financing stress:** Local governments are under increasing funding pressure from declining land sale revenues; this could force sharp spending cuts and hurt local economic growth
- **Consumer sentiment:** consumers remain cautious amid the property sector crisis and high youth unemployment, raising fears about deflation

Source: Accenture Strategy analysis

Japan's economy is expected to be sluggish in 2024 while India's resilience will be tested as global growth slows; Brazil's economy is likely to slow but rate cuts may provide cushion

Other key country outlooks

Region	Country	Base case outlook	What to watch for
Americas	Canada	• Tight financial conditions, weakening external demand and housing market distress are expected to keep growth muted in the near term	• Extent of consumer spending slowdown amidst high housing and debt service costs • The effectiveness of recent tax cuts in stimulating new homebuilding
	Brazil	• Slowdown in growth relative to 2023 due to normalization of agricultural output (which saw unusually-strong harvest season last year), though slowing inflation and recent interest rate cuts may limit extent of growth moderation	• Strength of agricultural harvest amidst shifting climate patterns • Ongoing uncertainty regarding planned tax reforms and overall fiscal trajectory
Asia Pacific	Japan	• After deteriorating significantly in H2 2023, 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 lingering inflation-wage growth gap narrows • How quickly the Bank of Japan loosens its yield curve control policy, especially if inflation remains sticky
	India	• Growth is expected to remain robust but moderate slightly amidst slowing external demand and rising oil prices	• Resilience in consumer spending • Signs of manufacturers or other companies shifting supply chains to India
	Australia	• 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 • The drag on Australian exports from China's economic slowdown

Source: Accenture Strategy analysis

Top 10 macro trends for companies

Consumer divergence, GenAI, geopolitical uncertainty, and financial and property market pressures are among the key macro trends impacting the business environment this year

Top 10 trends for 2024

	**1. Differentiation in consumer resilience and spending power grows**	• Growing differences in households' residual excess savings, real income growth, debt pressures and reliance on fiscal subsides lead to increasing divergence in spending among consumer segments
	**2. Lingering pay gaps relative to inflation keep labor bargaining power strong**	• Ongoing wage catchup dynamics are set to keep labor cost pressures elevated as workers seek compensation for past real income erosion
	**3. GenAI adoption picks up steam and begins to deliver productivity dividends**	• Expanding access to foundation models and parallel computing hardware democratizes AI application development, allowing companies to innovate on distinctive AI applications
	**4. Higher-for-longer rates start to bite harder and amplify financial stresses**	• Even if central banks start to ease short-term rates, structural drivers of higher long-term rates keep financial pressures on households and companies and drive further debt distress and bankruptcies
	**5. China de-risking momentum builds**	• Ongoing geopolitical tensions between China and the West and structural slowing of China's economy reinforce companies' tendencies and incentives to de-risk from China
	**6. Elections and geopolitical conflicts drive policy and business uncertainty**	• Uncertainties surrounding upcoming elections in major markets and the escalation or broadening of geopolitical conflicts continue to hamper business confidence, investment and planning
	**7. Stabilizing interest rate outlook supports gradual pickup in M&A**	• M&A transactions pick up steam—a combination of opportunities in take-private, carve-outs and add-on acquisitions—alongside continued thawing in IPO market
	**8. Property market struggles increasingly spill into broader economy**	• Deteriorating housing affordability and commercial real estate performance increasingly weigh on home and office-related spending, upstream sectors, and the financial health of exposed creditors
	**9. Global race for critical minerals and semiconductors heats up**	• Proliferating trade restrictions on geographically-concentrated critical minerals drive price volatility and create supply challenges for companies and their energy and digital transformation agendas
	**10. Industrial policy competition confronts fiscal sustainability challenges**	• Constrained fiscal space to execute existing or planned industrial policies (e.g., Germany, UK) further widens the industrial competitiveness gap between the US and Europe

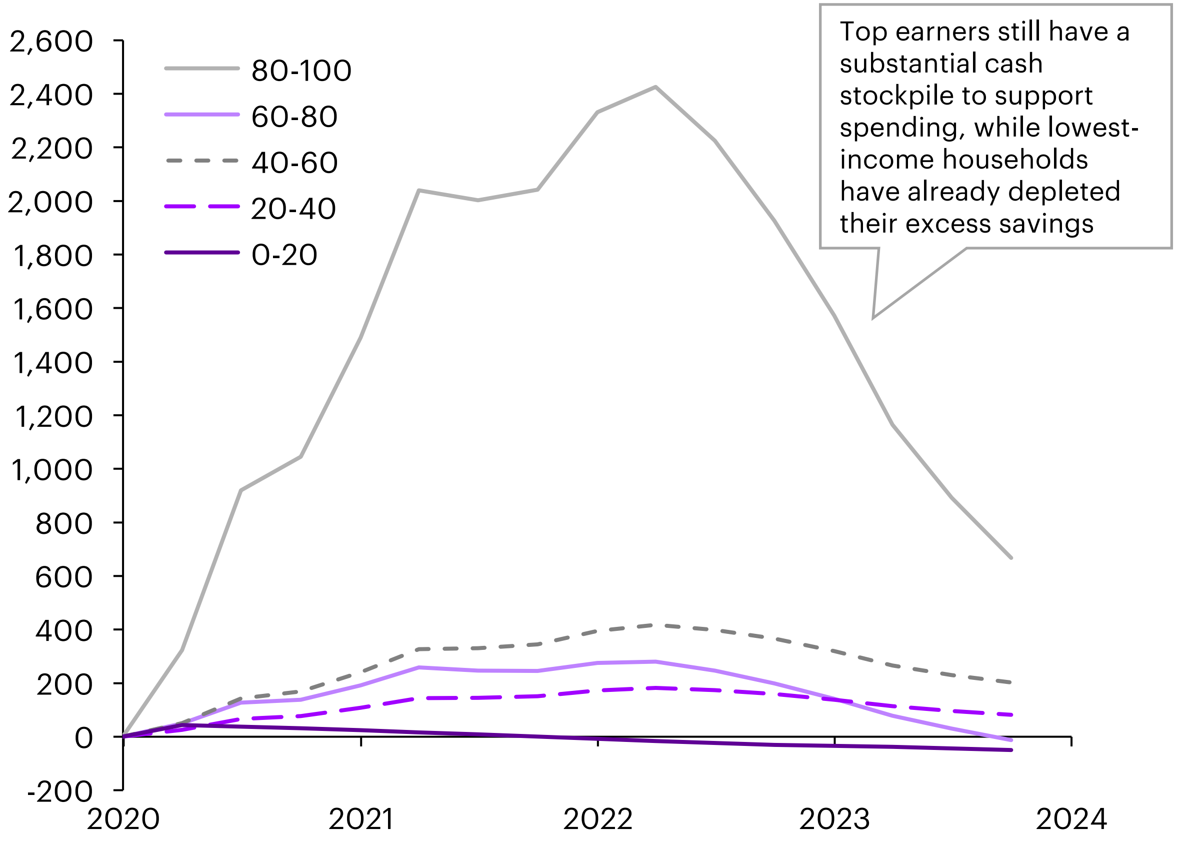
Source: Accenture Strategy analysis

Disparities in consumer health and spending resilience are set to widen further, with lower-income groups likely to face particular pressure to rein in spending

#1: Differentiation in consumer spending power grows

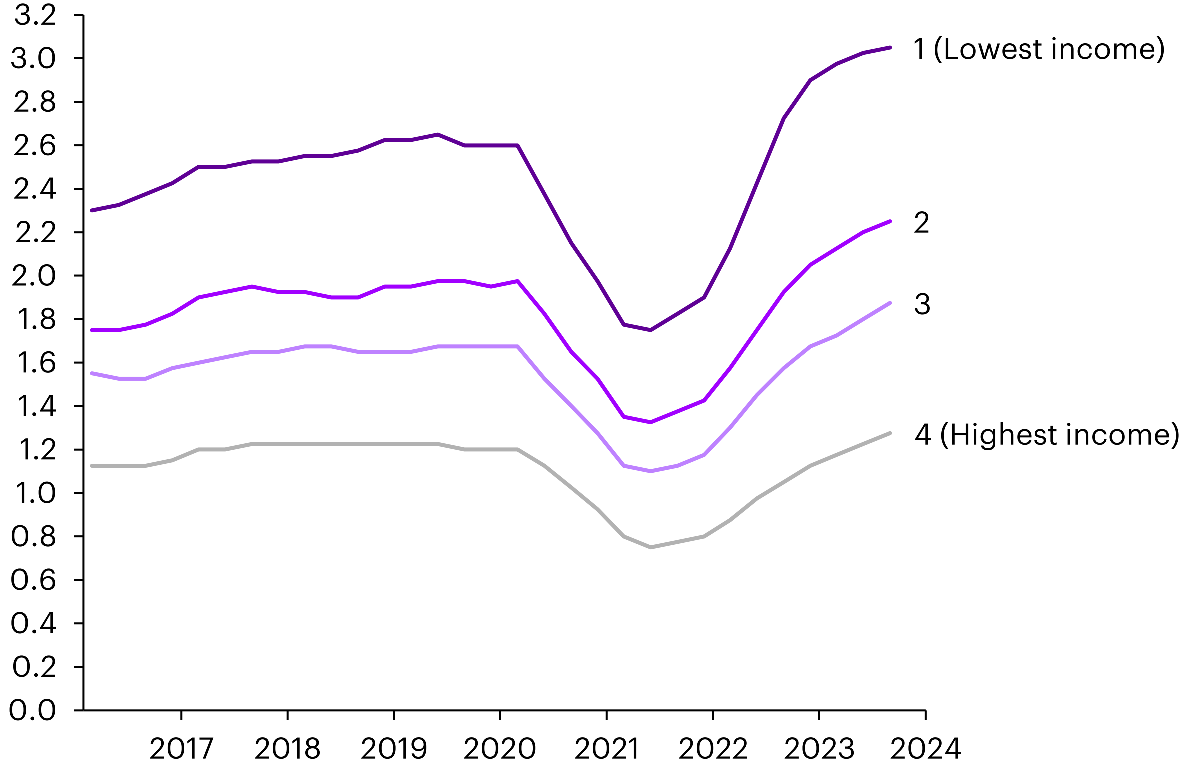
US household "excess" liquid savings by income quintile

USD billions



US credit card delinquency rate by income group[1]

Share of credit card borrowers who are newly delinquent (in percent, 4 month rolling average)



Note(s): (1) Credit card users are categorized into zip income quartiles by ranking zip code median income from lowest to highest and splitting zip codes into four equally sized groups by population

Source(s): New York Fed Consumer Credit Panel/Equifax; American Community Survey, Accenture Strategy estimates based on Federal Reserve data

Companies should be agile in adapting their marketing, pricing and channel strategies to the diverging spending power of different customer segments

#1: Business considerations

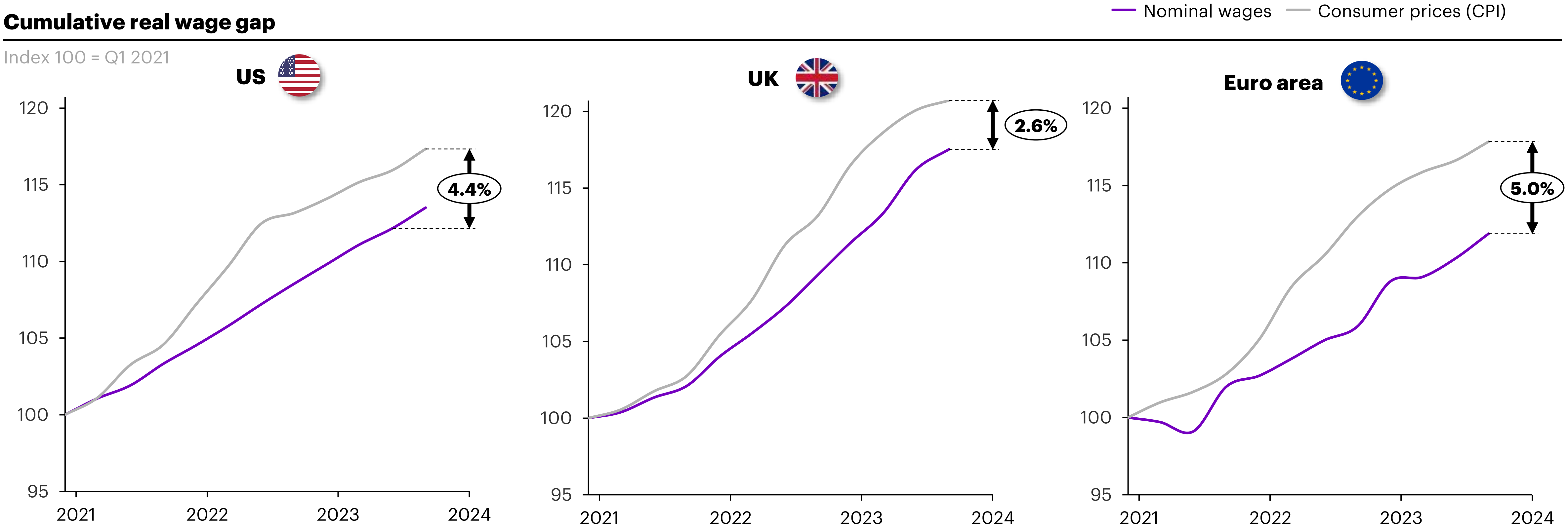
	Business considerations
Create a dynamic, data-driven pricing strategy	• Determine and employ different pricing strategy (e.g., discounts, price increases) for different product portfolio and customer segments to avoid cannibalizing revenues, e.g., applying across-the-board price cuts may risk revenue from some products that consumers would be willing to pay • Understand cost base of products can help businesses assess impact of future cost shifts and inform pricing strategy
Leverage targeted marketing and loyalty programs	• For customers under the most financial stress, businesses should consider elevating their loyalty programs to retain customers, e.g., – Expanding programs and offerings – Using tiered pricing features, e.g., Netflix and Disney+ introduced ad-supported subscription plans – Creating exclusivity for members, e.g., Zara members are given early access to savings • For top customers, utilize targeted marketing campaigns to increase spend; this can provide short-term growth opportunities
Explore ecommerce and mobile channels	• Price sensitive customers are likely to be more active in seeking online deals as – Online offers a better way to survey prices, i.e., Adobe survey indicated that e-commerce prices were 6% lower during 2023 holiday season – More options to fund their purchases, e.g., BNPL saw a 14% increase in 2023's holiday season
Stress-test P&L against different scenarios	• Stress-test financials and key operating metrics against a range of scenarios (including extreme outcomes) to understand business impacts • This can help businesses to identify any quick wins or longer-term investments that is required to protect margins

Source(s): Adobe Analytics, Accenture Strategy analysis

Real pay gaps accumulated over past two years are likely to sustain upward pressure on labor costs as workers seek to restore lost purchasing power

#2: Lingering wage catchup pressures

Cumulative real wage gap



Commentary

- Inflation has continuously outpaced wage growth since 2021, creating significant(and growing) deficit in real purchasing power
- Companies should prepare for ongoing labor cost pressures in 2024 amidst residual labor market tightness and as workers seek compensation for past real income erosion

Note: Nominal wages series for US is the employment cost index (ECI); for UK, private sector weekly average earnings; for Euro area, hourly labor costs.
Source(s): Haver Analytics, Accenture Strategy analysis

Companies should focus on improving business productivity to manage increasing labor costs pressures

#2: Business considerations

Scenario	Description	Wage inflation	Business considerations: People Functions	Business considerations: Strategic Planning
Continued labor cost pressures	• Workers continue to demand higher wages to protect their real purchasing power, particularly in highly unionized regions and sectors, e.g., – Auto and manufacturing – Media – Transportation	↑	• Communicate and manage employee salary expectations • Invest in productivity solutions, e.g., implement time management solutions to accurately track and manage employee hours; this enables greater visibility and can be used for salary negotiations	• Invest in automation where possible • Adopt flexible workforce strategy, e.g., – Consider contract workers and consultants to manage workload fluctuations – Outsource non-critical functions
Faster cooling labor market	• A faster-than-expected loosening of the labor market will, all else equal, tend to weaken worker bargaining power and wage pressures • This could result from: – A rapidly cooling economy – Further recovery in labor supply, e.g., stronger immigration	↓	• Revisit forecasts for hiring needs	• Align top-line considerations to personnel investments • Quickly identify core workforce needs (e.g., skills, size) that can manage a downturn but align with long-term business goals

Source: Accenture Strategy analysis

Expanding access to foundation models and parallel computing hardware will increasingly democratize AI application development, acceleration innovation possibilities

#3: Gen AI adoption picks up steam

ILLUSTRATIVE

Gen AI applications supported by maturing infrastructure

Growing focus

Application Software

Applications	End-user-facing B2B and B2C applications with proprietary or non-proprietary models	• Content Generation • Semantic Search • Agents

Model Infrastructure

Data Infrastructure	Storage, management and manipulation of data	databricks, Azure
Data	Core data to initially train and tune foundation model	IBM, appen, ORACLE
Models	ML model trained on core data	OpenAI, ANTHROP\C, MISTRAL AI_

Compute infrastructure

Cloud Platforms	Cloud infrastructure is essential for deploying generative AI	aws, CoreWeave
Hardware	Accelerator chips optimized for model training and inference workloads	NVIDIA, ASUS

Commentary

- Advances in foundation models' availability and parallel computing hardware are democratizing AI development
  - Small teams of specialized engineers have developed foundation models. For example, Mistral and X.AI built their models with core team of less than 20 people.
  - Competition among parallel computing suppliers like Nvidia, AMD and cloud providers with custom AI chips, is likely to drive down costs in the near term
  - Although supply shortages may persist in near-term, the overall direction is toward more affordable, available parallel computing for AI development
- As a result, developers can build differentiated applications on top of accessible foundations rather than focusing on foundational infra
- Growing prevalence of large multi-modal models and advancements in efficient edge inferencing also promise a new era of ambient intelligence

Sources: AMD, SemiAnalysis, Blackrock, Accenture Strategy analysis

To realize value and top-line growth, firms must move beyond Gen AI pilots to incorporate Gen AI into workflows, with a roadmap to embed and expose more capabilities

#3: Business considerations

	#1: Immediate to short term	#2: Medium term
Objective	• Accelerate Gen AI driven value realization across the organization	• Drive sustained competitive advantage including monetization of capabilities
What does good look like?	• Move beyond pilots to integrate off-the-shelf applications and plugins into business workflows • Gen AI COE beginning to drive scale. E.g., – Gen AI embedded in language and creative tasks across the business – Responsible AI practices embedded in the org • Roadmap for differentiated Gen AI supported offerings	• Core product leverages Gen AI to offer a superior customer experience (e.g., conversational reviews in native language) • Expose capabilities to offer differentiated offerings • Strong GTM to ensure focused monetization of offering
What is the impact?	• Select divisions begin to see productivity uplift (e.g., sales, corporate functions)	• Fundamentally different way-of-working • Significant uplift in productivity throughout the organization • New monetization opportunities open up

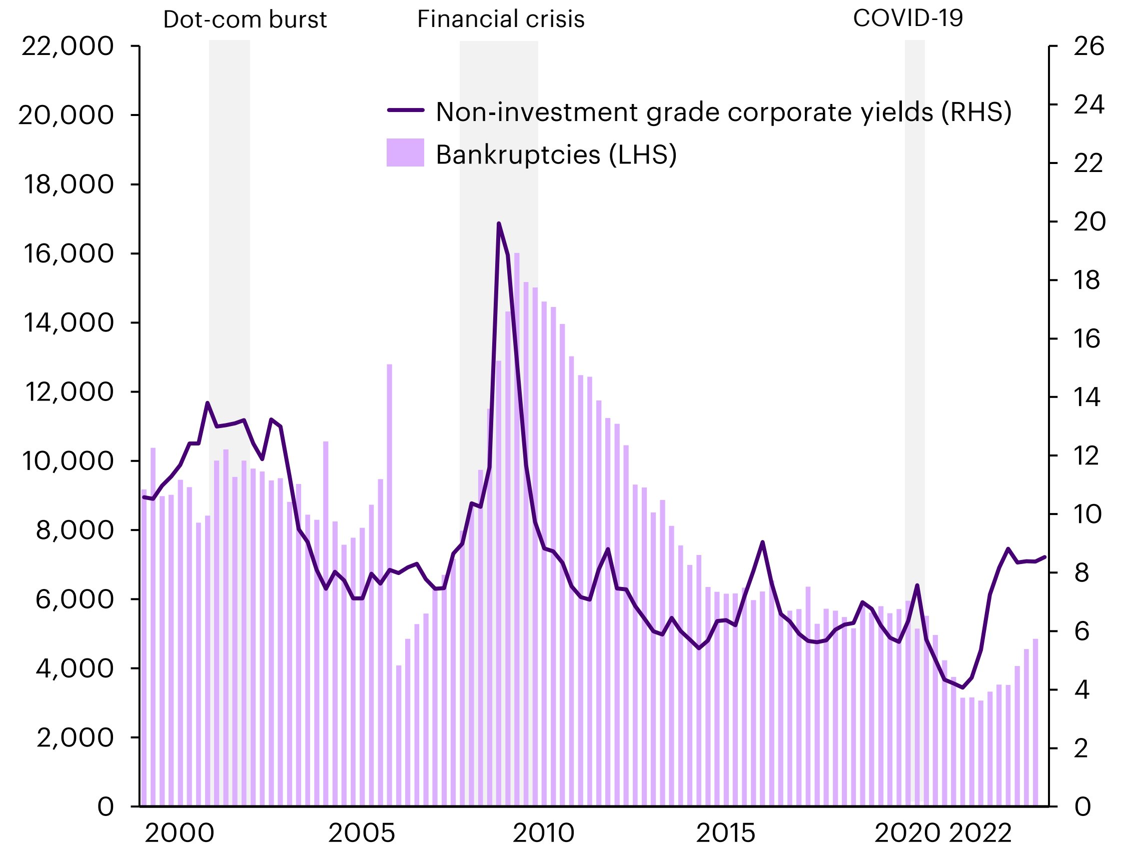
"Think of this as being middle of rebuilding an organisation shifting from being operational into one that is transformational."

Global CIO, Major Retail Group

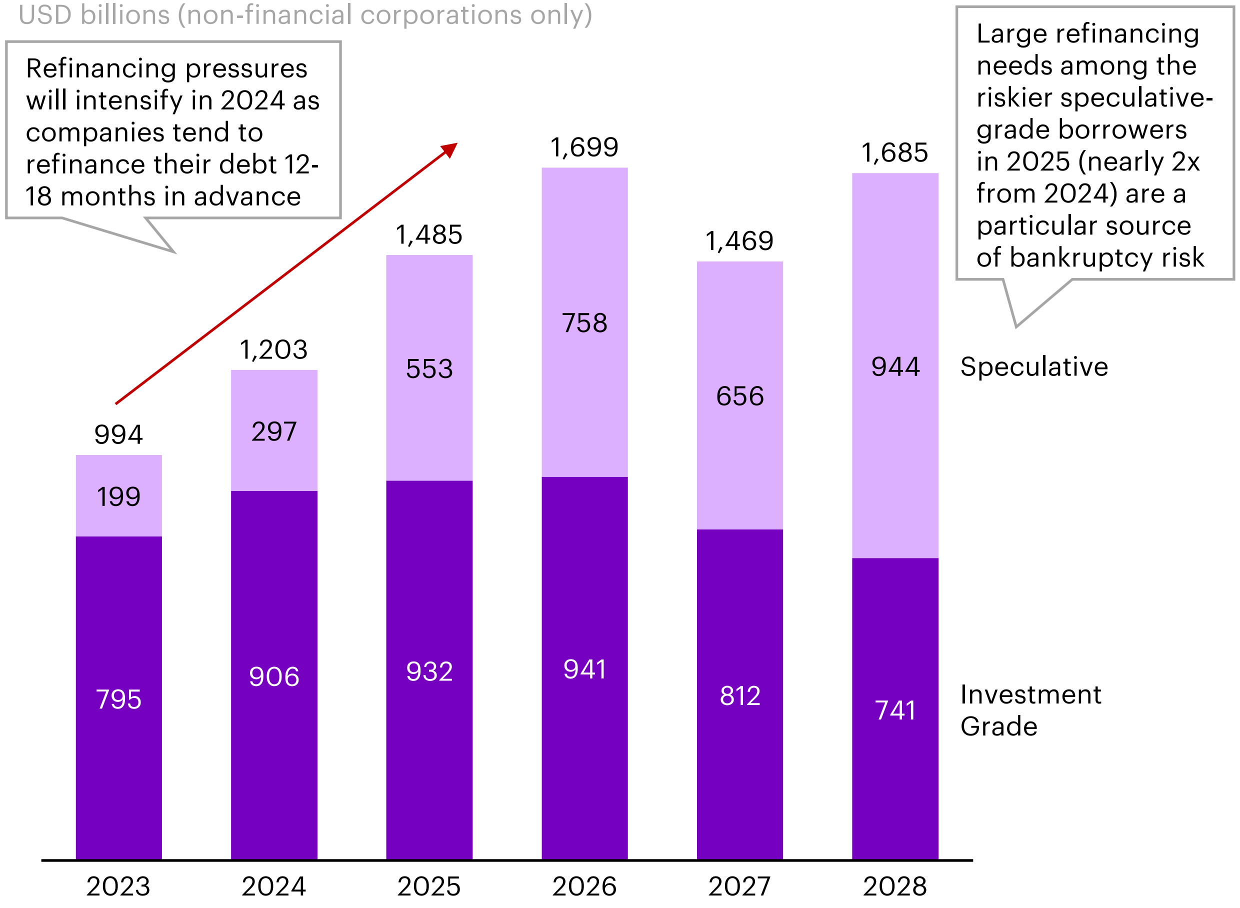
The significant likelihood of higher-for-longer rates is expected to amplify corporate bankruptcy pressures, particularly as debt refinancing needs grow in next 1-2 years

#4: Higher-for-longer rates amplify financial stresses

Corporate bankruptcy trends



Global corporate debt maturities



Note: Includes bonds, leveraged loans, and revolving credit facilities that are rated by S&P Global Ratings. Excludes debt instruments that do not have global scale ratings. Foreign currencies are converted to US dollars at the exchange rate on July 1, 2023. Data as of July 1 2023
Sources: S&P Global Ratings Credit Research & Insights, Accenture Strategy analysis

CFOs should focus on strengthening balance sheets and unlocking additional cash flow through stricter operational practices

#4: Business considerations

	Industries	Business considerations: Finance / CFO	Business considerations: Operations
Most exposed industries (industries with >USD 100 billion debt outstanding at lowest rating levels, "B-" and below)	• Healthcare • Communications, Media and Technology (incl. High Tech) • Consumer Goods	• Re-engineer balance sheet to improve financial position, e.g., debt-to-equity swaps • Work debt related metrics and covenant thresholds into scenario planning exercises • Consider divestment of non-core assets and unprofitable/underperforming businesses and assets	• Control expenses – Reduce overheads, staff incentives etc. – Streamline operations – Automate certain processes • Consider value- or risk-based deals with 3rd parties to reduce overall cost base • Improve cash flow management, e.g., – Negotiate longer vendor terms – Eliminate obsolete inventory – Optimize collection/receivables strategy, e.g., increase payment channels, automating payments etc. • Stringent portfolio management, with ability to quickly dial up/dial down 2024 change management investments • Improve and invest in tools used for forecasting and cash reporting
Industries with growing debt	• Materials • Retail • Financial Services • Auto	• Utilize short term financing, e.g., overdrafts to manage seasonal gaps in working capital and cash flows • Negotiate with creditors to restructure debt • Consolidate debt into one loan to reduce overall interest expense • Work debt related metrics into planning exercises, e.g., – Identify areas that can be converted into variable expenses that can be reduced if top line suffers • Sell non-core assets	

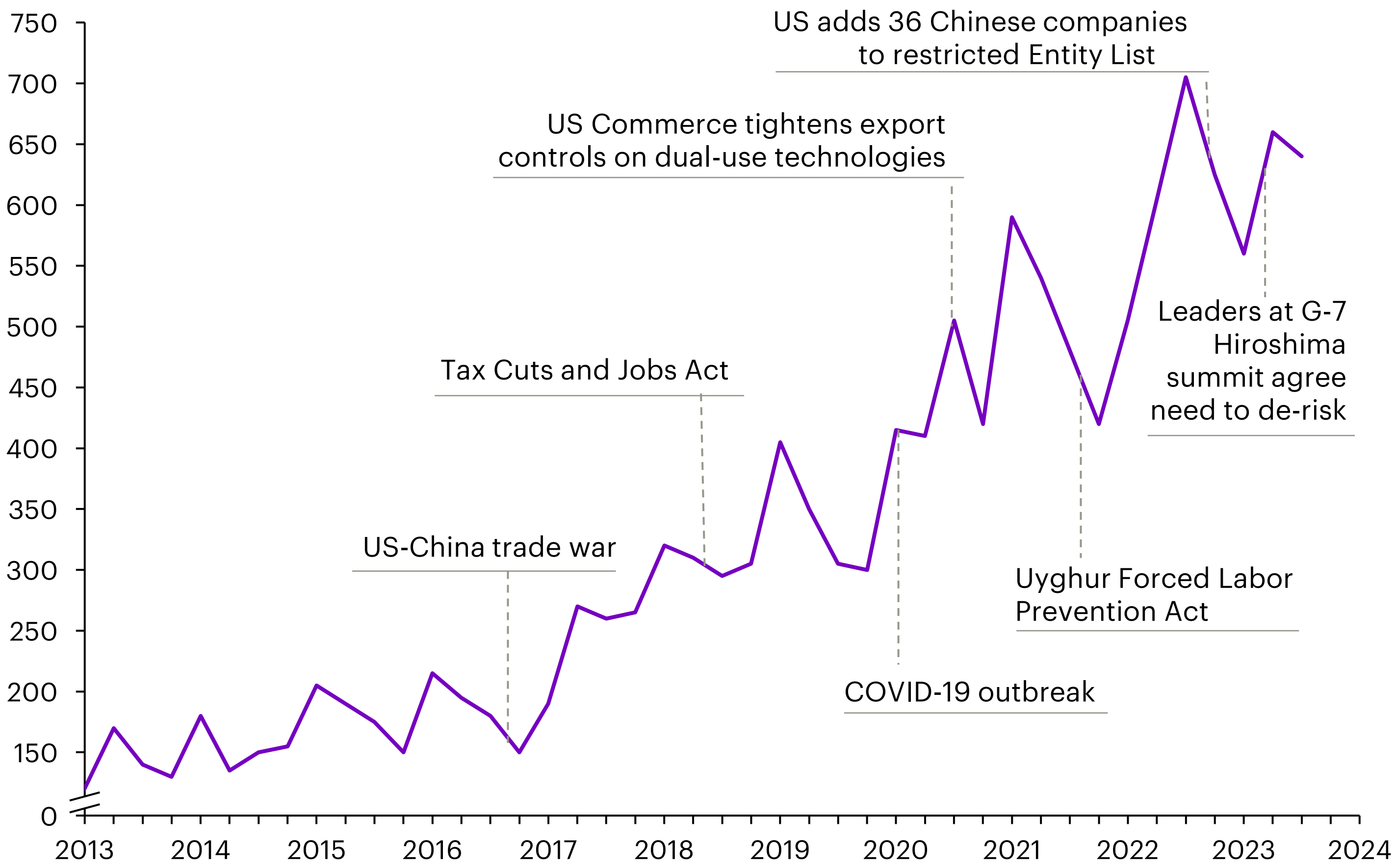
Sources: S&P Global Ratings, Accenture Strategy analysis

China de-risking involves diversifying supply chains and global portfolios, but it is also prompting companies to revisit their tech stacks, security and legal entities in China

#5: China de-risking

Mentions of "De-risk" or "Decouple" in company documents

Number of mentions on a quarterly basis



China de-risking drivers

- **Diversification of global supply chains**
  - Companies are hedging against new risks affecting supply from China, including risks stemming from tense China-US and China-EU relations
  - New trade wars and unsustainable wage growth in China could also lead to higher sourcing costs
- **Government incentives for local production**
  - Several countries, notably the US, the EU, India, and Southeast Asian countries, are incentivizing companies to re-shore or nearshore production away from China
  - Most common incentives include tax breaks, grants, land concessions, and import tariff exemptions
- **Technology and security concerns**
  - The growing complexity of complying with China's data regulations as well as restrictions on the use of Chinese or American technologies is leading to the fragmentation of tech stacks (i.e., China for China)
- **Weaker market growth in China**
  - China's lower growth is rooted in unresolved structural factors (e.g., aging population, growing stresses on the property sector, prompting companies to look for faster growth in other countries

Note: Company documents include filings and earning call transcripts
Sources: U.S. Commerce Department,Accenture Strategy, QZ/Sentieo

Companies should adapt to the changing nature of China's maturing economy and hedge against potential sources of political risk

#5: Business considerations

China trends	Business considerations
Weakening short-to-medium-term economic growth outlook	• Pursue differentiation through innovation, added features and improved quality over cheaper, lower-grade goods to avoid price wars with local players • Prioritize higher-margin segments to protect against higher price sensitivity
Ageing demographics	• Diversify market to other regions, especially those with a large and/or growing working age population, such as Southeast Asia and the Indian subcontinent • Shift product offerings to better target China's increasingly elderly population, e.g., user-friendly interfaces and ample user support resources
Increasing household incomes	• Increase focus on aspirational and premium brands • As labor costs in China rise, diversify supply chains toward more competitive labor markets, e.g., Southeast Asia, India and Mexico
Risk of territorial conflict	• Monitor possible developments which may increase tensions around China's contested territories • Build up inventories to protect against supply disruptions from China, and consider co-investing with suppliers to build capacity outside of China
Worsening trade and investment relations between the West and China	• Adapt your global sourcing strategy to reduce exposure to tariff measures between the West and China • Consider ringfencing your China business from a technology and legal standpoint
Overreliance on China for parts within a supply chain	• Ensure reliable supply of key production inputs by diversifying global supply chain with trusted partners, including tapping into incentives for local production to minimize de-risking costs

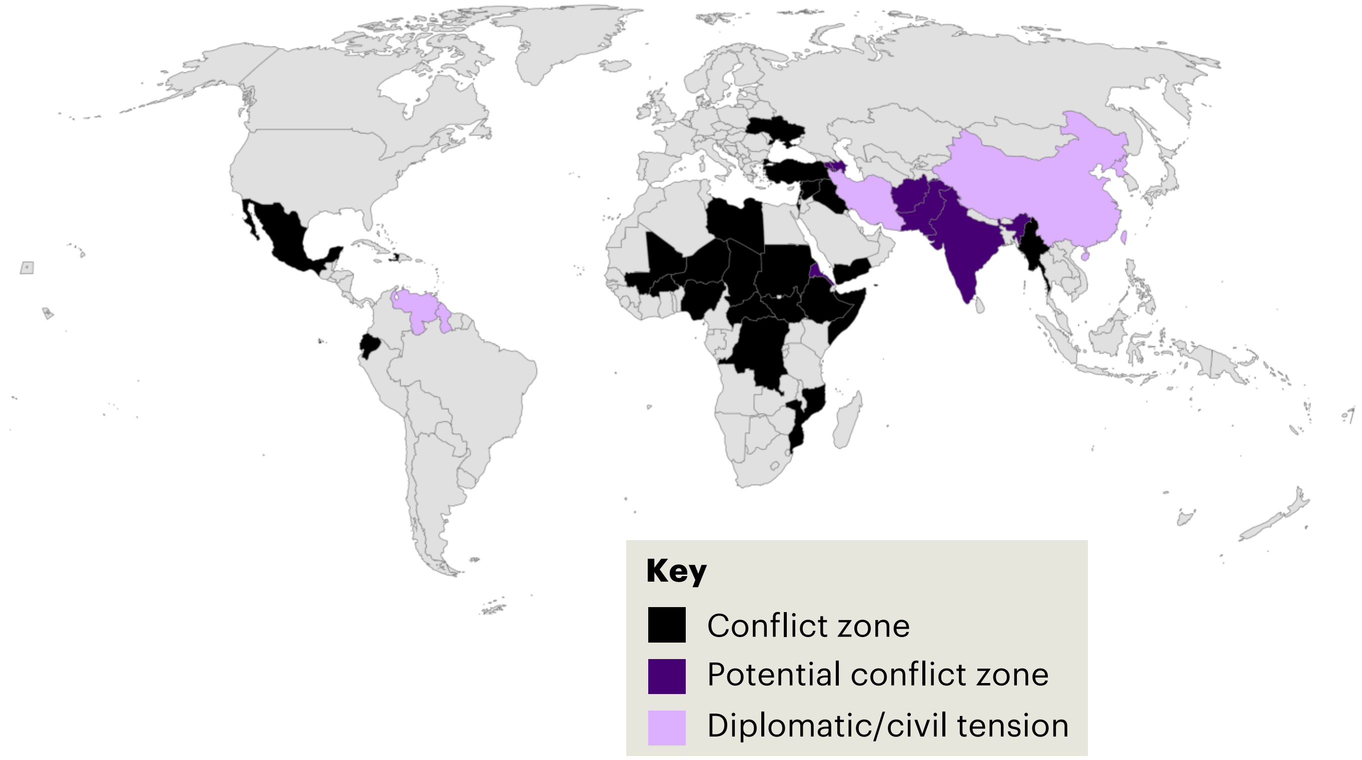
Sources: World Bank, Morgan Stanley

Against the backdrop of instability, many major geopolitical players will hold elections in 2024, fueling uncertainty about potential shifts in foreign and domestic policy agendas

#6: Elections and geopolitical conflicts

Current zones of military and diplomatic conflict

Ongoing wars, military conflicts, and diplomatic situations which may lead to conflict



Commentary

- **Regional Trends**
  - Major wars in Gaza and Ukraine will continue to test alignment within NATO, and between the US and its allies, especially around ongoing financial and military support and conflict resolution paths
  - A protracted conflict in the Red Sea and/or broader escalation of tensions in the Middle East can perpetuate shipping disruptions and keep energy prices elevated
  - Instability in Mexico and Venezuela and armed conflict in Ecuador may lead to further migration to the already-overwhelmed US southern border
- **Elections in 2024**
  - Over 70 countries are holding elections in 2024, representing roughly 55% of world's population and 60% of global GDP
  - The risk of resulting shifts in domestic and foreign policy shifts is significant and likely to be a major source of continued economic and market uncertainty

Sources: Council on Foreign Relations, Accenture Strategy

Companies should place greater focus on business continuity planning and government engagement to mitigate risk

#6: Business considerations

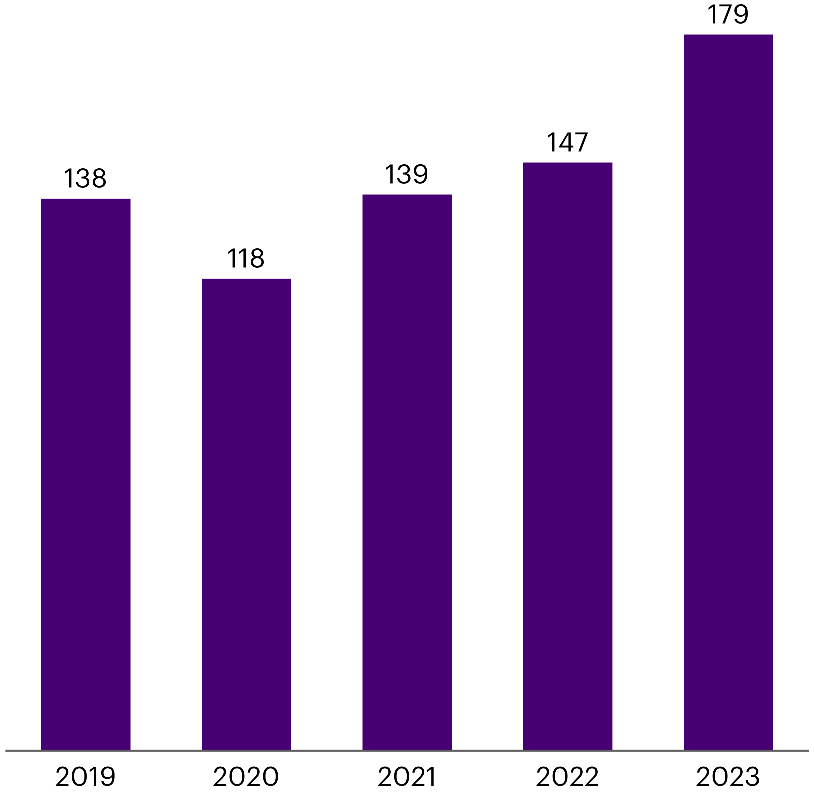
Trends	Business considerations
Escalating tensions in the Middle East	• Stockpile important supplies and equipment in case of delays in shipping • Include risk-sharing clauses in contracts with suppliers of critical raw materials to safeguard supply • Optimize supply chain efficiency by sourcing from nearby shipping centers, preferably minimizing ocean shipping between the Mediterranean and Indian oceans
Elections around the world	• Strengthen your government engagement function and find areas of alignment between your company's strategic priorities and those of different political platforms • Identify bipartisan issues and priorities, especially as it pertains to public investments and industrial policy, as these will inform growth opportunities that are less likely to be impacted by political transitions • Introduce greater flexibility in payment terms and conditions ahead of key elections to incentivize investments by risk-averse customers
Further outbreak of war and armed conflict	• Make supply chain resilience stress testing part of your risk management processes • Strengthen your investor relations and PR strategy as you deal with stakeholders with diverse and somewhat opposing views on particular conflicts

M&A transactions are likely to rebound—a combination of opportunities in take-private, carve-outs and add-on acquisitions—alongside continued thawing in IPO market

#7: Stabilizing interest rate outlook supports pickup in M&A

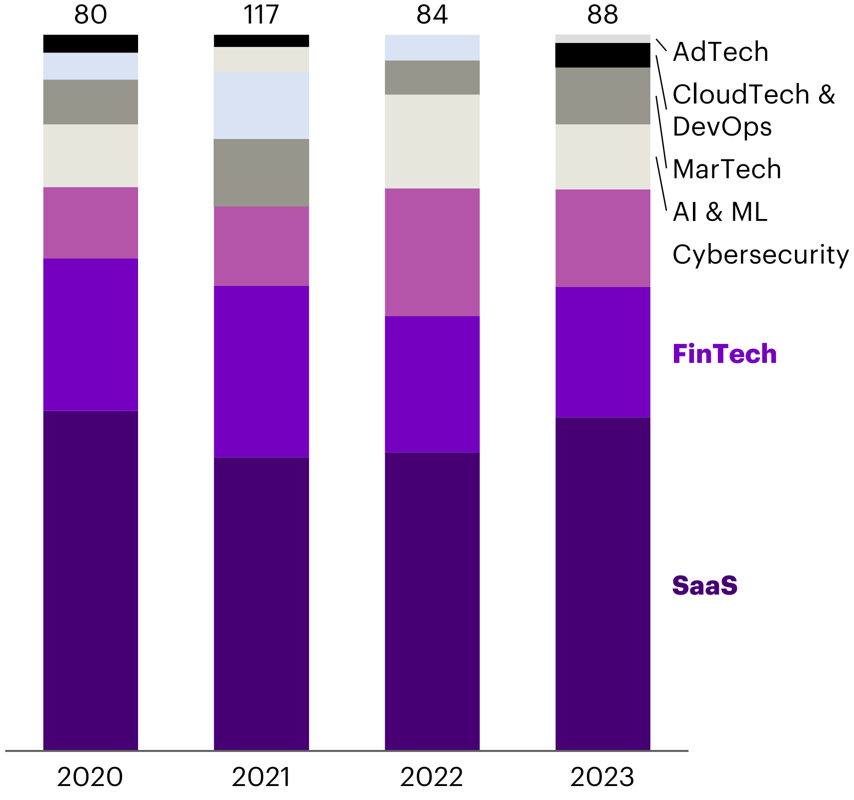
Take-private transactions in 2024 will likely continue to remain significant even if they don't hit 2023 levels

No. of take-private transactions



Carve-out opportunities have grown given declining revenue multiples and pressure to improve profitability

Global level of Tech corporate divestitures, no. of companies



Commentary

- Transactions expected to rebound include:
  - Take-private to transform and return assets to market at higher valuations
  - Add-on acquisitions given availability of attractive assets
  - Carve-out of non-core or underperforming business units from large companies
- Select VC firms are also experimenting with PE-type business models and might be more active in the space
- Separately, the stabilization (and even potential easing) of interest rates should support IPO market re-opening, though the bar to go public will likely be higher

Sources: Pitchbook, Refinitiv, Company Websites, Accenture Strategy analysis

Successful portfolio repositioning will require improving operational assets as well as navigating still-uncertain market conditions

#7: Business considerations

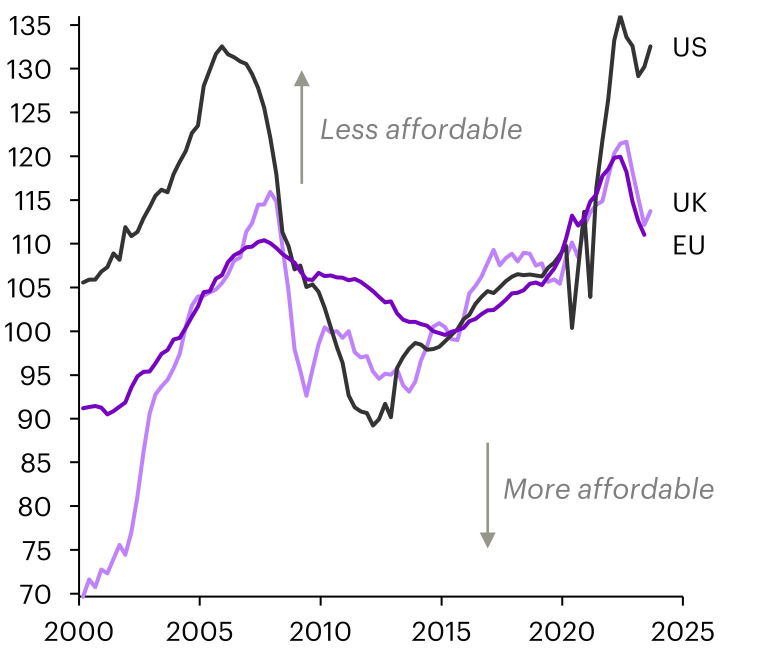
	Business considerations	Implications
Private Equity and financial investors	• Private equity and financial investors hold record funds ready to deploy • Expect an uptick in corporate divestitures and potentially, transformative take-privates • PEs need to be ready to capitalize on these opportunities, utilizing operational expertise to unlock hidden value in acquired assets while navigating increased competition for deals	• Develop rigorous criteria for identifying undervalued assets in corporate divestitures • Enhance operational capabilities to unlock synergy and improve acquired assets • Explore creative deal structures for take-privates with high transformative potential
Mature corporates	• Mature corporations have a chance to unlock value by streamlining operations and divesting non-core units • These divestitures can fuel strategic acquisitions in core segments or provide capital for long-term transformation • They must remain disciplined with valuations and ensure acquired assets align with strategic vision	• Optimize portfolio by carefully divesting non-core units • Use divestiture proceeds strategically for growth-oriented acquisitions in core segments • Consider take-privates as a potential lever for long-term transformation
Private pre-IPO companies	• Some thawing in the IPO market is underway, with more expected now that interest rates have likely peaked and may even start to come down gradually • Going forward, the bar for going public is likely to be higher, and successful founders and CEOs will need rock-solid business models to excite investors	• Scrutinize core economics and path to profitability • Retest PMF and TAM with rigor • Scale commercial engine and operating model (e.g., industrialize sales, marketing and support) • Install public-stage governance and oversight • Stress test strategy against market changes and take the long view on risks and opportunities

Housing affordability in US and Europe is near historical lows while losses from exposure to the struggling commercial real estate sector mount

#8: Property market struggles increasing weigh on broader economy

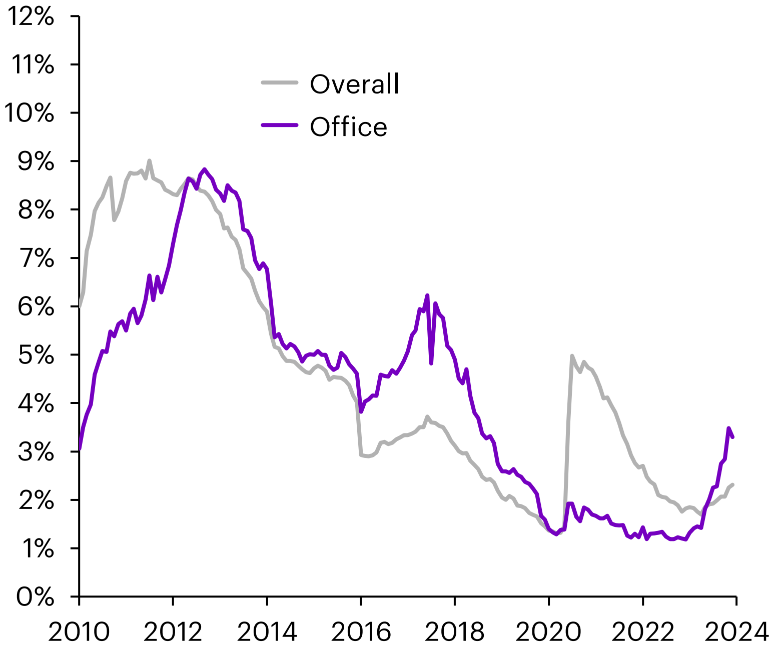
Housing affordability[1]

House price to income ratio, up to Q2 2023



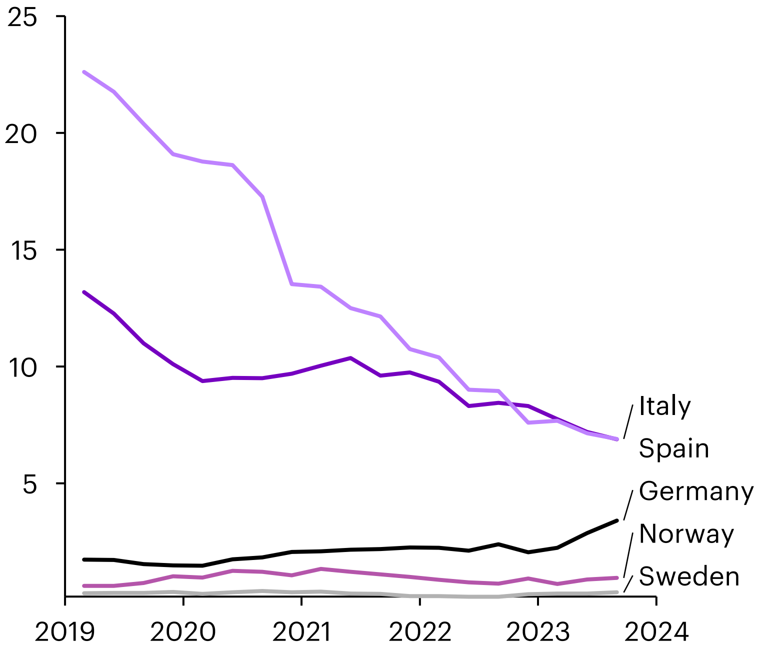
US CMBS delinquencies rates by property type

Percent



NPL rates on commercial mortgages in Europe

Percent of outstanding loans



Commentary

- House price-to-income ratios (one measure of housing affordability) in the US, UK and EU signal lowest affordability since peak of last housing boom in late 2000s
  - This will weigh on household income and crowd out available spending on other consumer discretionary, e,g., home improvement goods
- In parallel, default rates on commercial properties (particularly office buildings) are trending upwards—this increases risks to banks lending to commercial real estate and could lead to domino effects on the broader economy

Note(s): (1) Euro area data is only up to Q2 2023
Sources: OECD, Fitch Ratings, EBA Risk Dashboard, Accenture Strategy analysis

Navigating the CRE downturn involves both reducing CRE-related risks but also capitalizing on the opportunities generated from the dislocation

#8: Business considerations

	Business considerations
Actively manage existing bank and creditor relationship	• As credit conditions tightens, obtaining new funding will become increasingly challenging, particularly in capital intensive sector which requires refinancing, e.g., real estate, construction and CRE holding companies • Companies should continue to maintain a strong relationship with existing bank and creditor by proactively managing their exposures, e.g., – Track fundamentals, e.g., occupancy ratio and asset valuations closely – Negotiate covenants headroom to prevent defaults – Conduct business stress-test, and communicate outcome and mitigation strategy to creditors and investors
Opportunity to invest and diversify portfolio	• While there is opportunity to buy high quality distressed office properties at low valuations, investors should also consider diversifying their investments into other real estates that are driven by secular growth trends, e.g., – Demographic changes, e.g., senior and student housing – Technological innovation, e.g., data centers – E-commerce growth, e.g., warehouses
Conduct portfolio diligence and take necessary actions to preserve cash	• Investors and corporates are likely to see weakened balance sheets from increased provision for losses on CRE assets • There should be increased focus on identifying fundamental risks in their assets and portfolios, e.g., – Conduct rigorous analysis of capital structures and cashflows – Understand tenant mix, i.e., a concentration of SMB enterprises and industries represents a high risk – Evaluate asset environmental performance, e.g., tightening sustainability standards in Europe will add further pressure on asset valuations • This can help to devise mitigation strategies, e.g., equity injections, asset disposal etc.
Diversify top line into less cyclical sectors and control cost	• Companies exposed to consumers and housing-related expenses are likely to see a hit to short-term performance as low housing affordability and declining market valuation pose headwinds to big ticket purchases, e.g., – Consumers are likely to postpone renovation projects in a downturn (i.e., “wealth effect”), hampering demand for constructions and house furnishings • For these companies, controlling costs and diversifying top line would be key to maintain margins, e.g., – Construction companies can expand into publicly funded construction or infrastructure projects

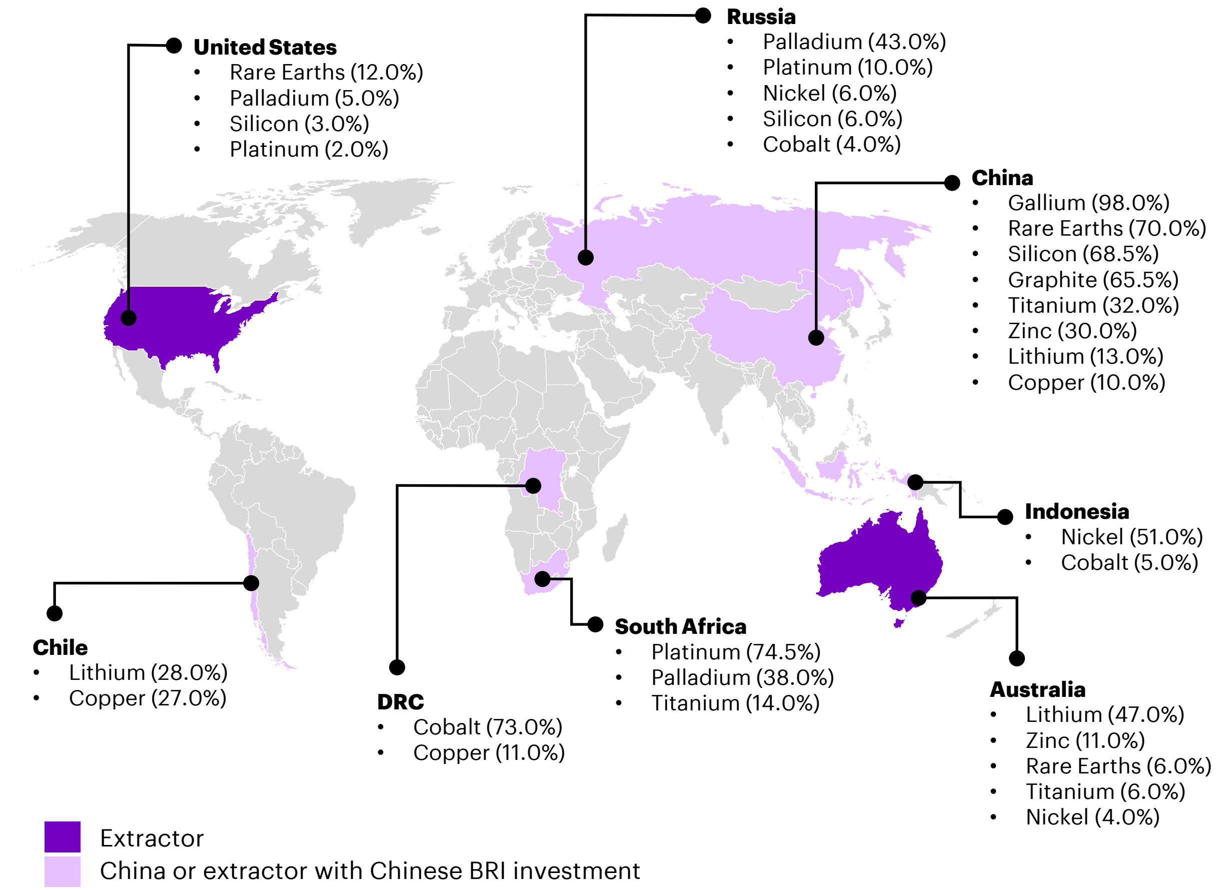
Source: Accenture Strategy analysis

Companies' energy transition and technology transformation ambitions depend heavily on on critical minerals, which are geographically concentrated, particularly in China

#9: Global race for critical minerals and semiconductors heats up

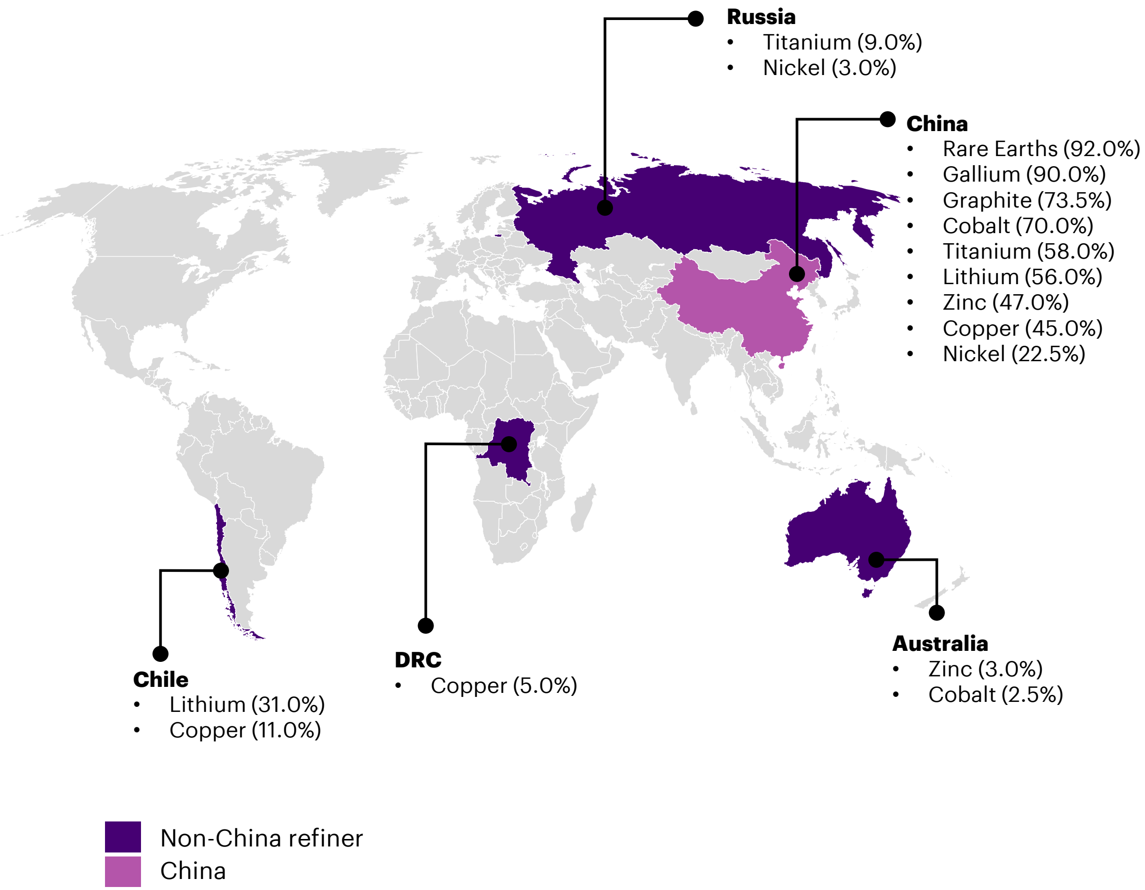
Largest mineral extractors by country

Percent global extraction, 2022



Largest mineral refiners by country

Percent global refinery, 2022



Source(s): UK Critical Minerals Intelligence Centre, Lazard, Green FDC, Accenture Strategy analysis

Critical mineral access is a geopolitical, not geological, issue; as tensions build further in 2024, companies should be prepared for access to be increasingly weaponized

#9: Business considerations

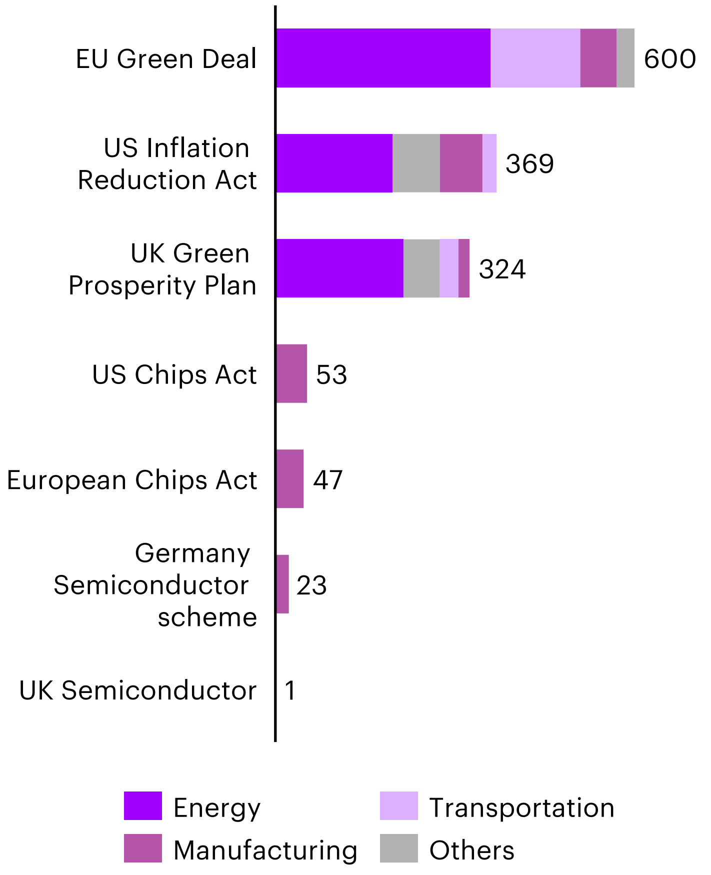
Trends	Business considerations
Mineral access concern ripples through industries	• Review net zero roadmaps, financial plans and strategic objectives based upon differing geopolitical scenarios • Identify key critical mineral dependencies and review potential interventions to build resilience
Potential weaponization of semiconductors	• Plan for potential restrictions on minerals related to semiconductors if US and China tensions escalate • Assess geographical concentration of semiconductor dependencies and identify potential for new supply, considering existing and upcoming semiconductor production subsidies and policies
A rise in export restrictions	• Ensure visibility across the entire supply chain to understand level of exposure • Secure mineral supply through sourcing and procurement initiatives, potentially considering direct investment or joint ventures in ecosystem partners (mining operations) • Build inventories, where possible, to increase potential reaction time • Lower demand for new minerals, where practical, by embracing circular economy practices, substituting materials or shifting portfolio choices
Western response to build critical mineral resilience	• Leverage subsidies that governments are providing to build resilience across the critical mineral supply chain • Prepare for continued geographic supply concentration of critical minerals in the near to medium term, due to the timelines associated with diversifying supply (e.g., 15+ years to open a new mine)
Responsible access to critical minerals	• Build transparency into the critical mineral supply chain, and understand the range of ESG implications associated with extracting and processing these minerals • Collaborate across the ecosystem to build responsible access

The growing use of industrial policy to address economic, security and environmental concerns is likely to increasingly pressure government finances

#10: Industrial policy competition confronts fiscal sustainability challenges

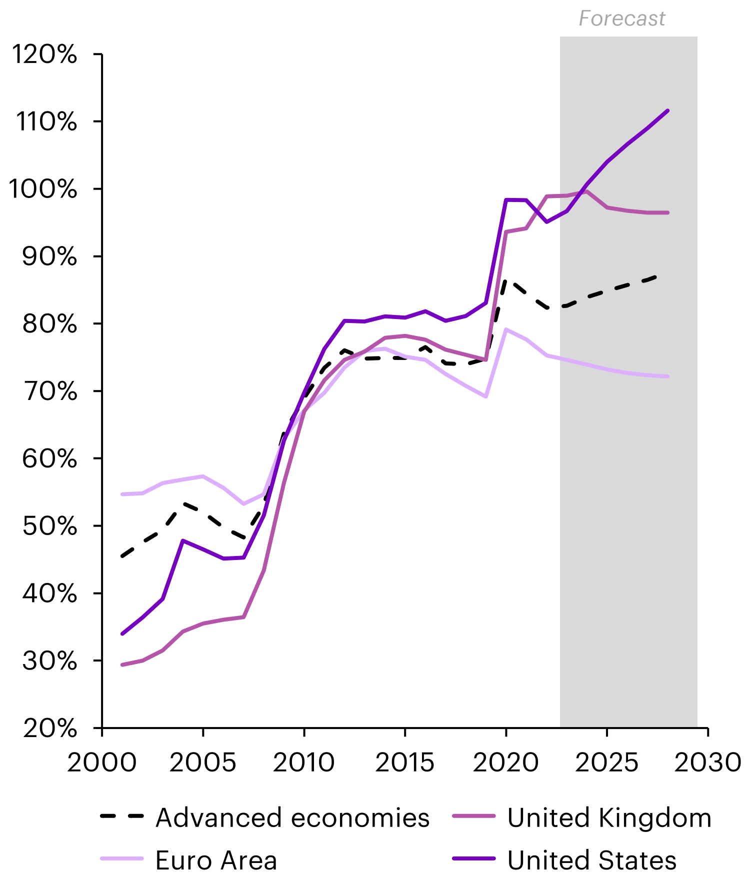
Government industrial policy commitments

Government spending commitment (in $ Bn)



Increasing net debt as a % of GDP

Net debt as a % of GDP for Advanced Economies



Commentary

- Governments globally are likely to ramp up industrial policies in an effort to accelerate energy transformation and secure critical minerals and semiconductor supplies
- Public spending in advanced economies has risen rapidly since the pandemic, pushing up public debt to decades-high levels
- In this context, the fiscal room to sustain or grow industrial policy initiatives is set to be increasingly squeezed,
- Recent budget crises and policy changes in 2023 are an early indication of this growing spending constriction
  - The **German** constitutional court's "debt brake" ruling triggered spending cuts to transport and energy and industrial subsidies in the 2024 budget
  - **EU** reformed its fiscal rule (Stability and Growth Pact) to give individual state greater discretion on debt and deficit plans
  - **US** Congress continues to struggle to agree on a full-year budget, or any longer-term plan to address a large and likely-unsustainable primary deficit
  - **UK** government announced in its Autumn Statement fiscal measures that imply a significant reduction in real public spending over next 2-3 years

Note: Advanced Economies include G7, Euro Area, Andorra, Israel, San Marino, Australia, Korea, Singapore, Czech Republic, Macao SAR, Sweden, Denmark, New Zealand, Switzerland, Hong Kong SAR, Norway, Iceland.
Sources: IMF, Accenture Strategy analysis

In assessing investment and location decisions, companies should factor in the growing risk that government incentives get dialed back over time due to fiscal pressures

#10: Business considerations

Trends	Business considerations
Location Strategy	• When making location strategies, corporations should focus on long-term fundamental demand outlook and work with upstream/downstream supply chain partners, instead of relying too heavily on government incentives/subsidies • From an operational perspective, have a plan to ensure long-term competitiveness after subsidies phase out or in case they don't fall through
Diverging Competitiveness	• US could gain more location advantage through further widening industrial competitiveness as rigid fiscal rules in Europe (both at EU and at country-level) put constraints on governments' credibility and capability to fully execute on planned industrial policies through expansionary budget • Companies could negotiate for higher non-policy incentives or consider other location benefits (e.g., access to skilled labor) in markets where industrial polices are less competitive in comparison to the US
Regionalization Focus	• From a decision-making perspective, get ready for more fragmentation and inconsistencies across regions given different country contexts and government policy constraints • Have a playbook to tailor strategies to fit specific market dynamics (including understanding specific policies)
Policy Priorities	• Understanding governments' strategic priorities will be key as governments under tighter budgetary constraints might need to prioritize spending: – i.e., continental Europe is more seriously confronted with an industrial structural transformation and energy security • Companies should invest in understanding government and political priorities for prospective industrial locations

Source: Accenture Strategy analysis

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Accenture Strategy's Macro Foresight capability is focused on helping companies and investors understand major macro shifts in the global economy and what they mean for corporate strategic planning, investment planning and enterprise-wide transformation – with the goal of helping clients distill complicated macro trends into simple, pragmatic recommendations which drive value.

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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