Macro scenario - Global

December 7, 2023

High inflation and strong activity delay easing in the US

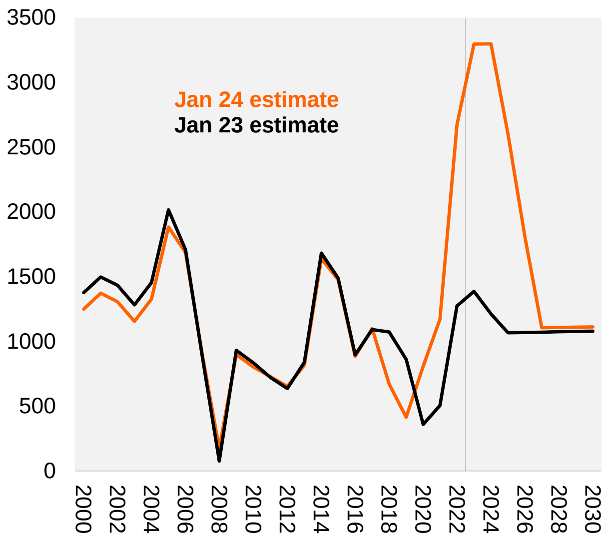
- U.S.: We have shifted our expectation for the start of interest rate cuts from June to December this year and continue to see 3 cuts in 2025. Strong activity, together with more persistent inflation should lead the Fed to wait longer and gather more data, in order to have enough confidence to begin interest rate cuts.
- Europe: We continue to expect the start of interest rate cuts in June amid weak activity and moderating inflation. We forecast that the benchmark rate will fall from 4.0% currently to 2.75% by YE24 and 2.0% in 2025.
- China: Improved activity in 1Q24, though amid lingering uncertainties. We keep our GDP growth estimates at 4.7% in 2024 and 4.5% in 2025.
- Global: Other DMs are decoupling from the Fed and signaling that rate cuts will start soon.
- LatAm: the plot thickens.

U.S.: interest rate cuts only by December

Growth and employment should remain robust in 1H24. We forecast 2.5% GDP growth in 1Q24 – still strong and driven by household spending (2.3% qoq/saar).

One of the reasons behind the resilience in activity is the surge in immigration in recent years, which lifts potential GDP via faster workforce growth. The increase in immigration became more evident after a review by the Congressional Budget Office (CBO), which now estimates that 3 million new immigrants are coming to the U.S. every year (see graph), mostly unauthorized individuals (~2 million), resulting in a labor-induced supply shock to the economy. We estimate that increased immigration boosts potential GDP by 0.5 percentage point to 2.5%-3.0%.

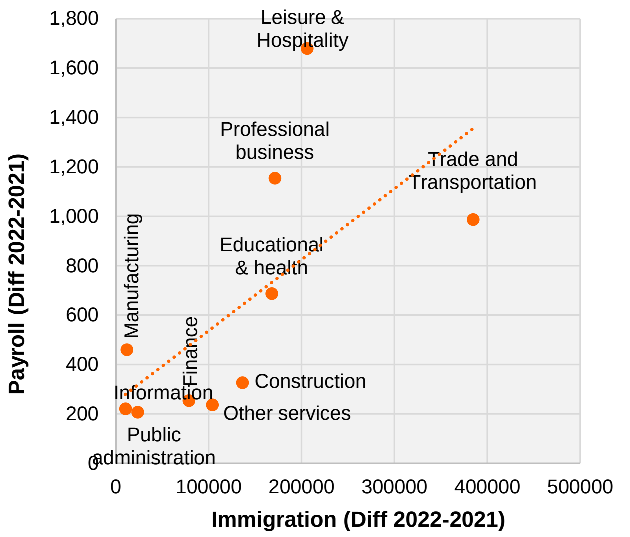
Immigration estimations revised up



Source: CBO, Itaú

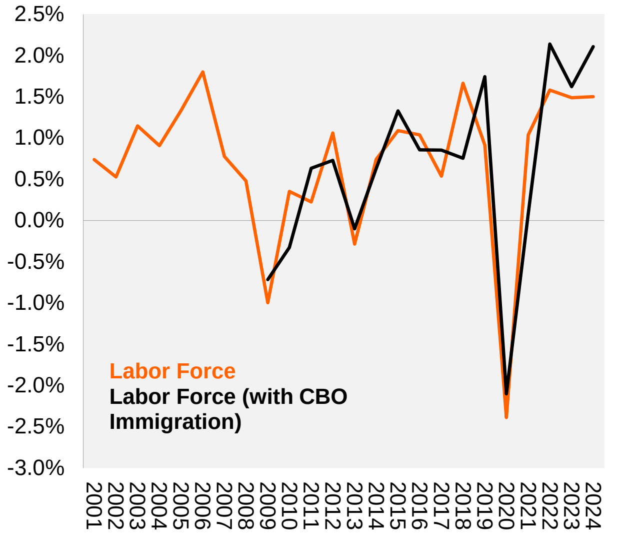
This immigration shock fuels employment gains, which are more evident in industries that absorb more immigrants (see graph). Therefore, we also expect sustained brisk growth in payrolls – above 200k per month – throughout the first half. Our estimate for the neutral payroll (consistent with constant unemployment) was 250k last year and should be around 210k this year, so that the unemployment rate will remain flat in 2024.

Immigration & Payroll are correlated



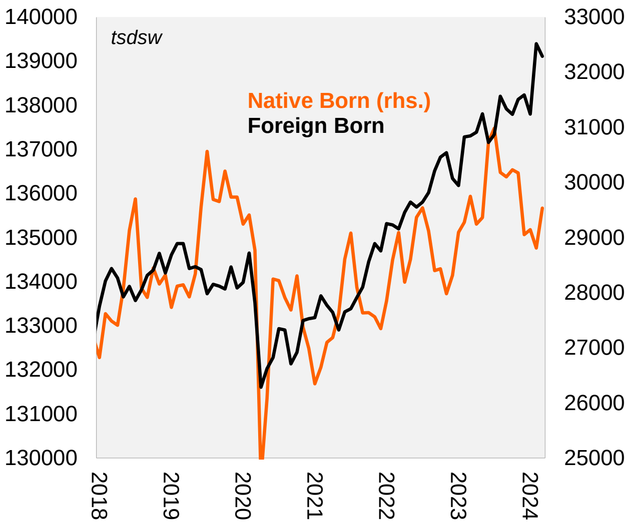
Source: Haver, CBO, Itaú

Labor force is increasing



Source: Haver, Itaú

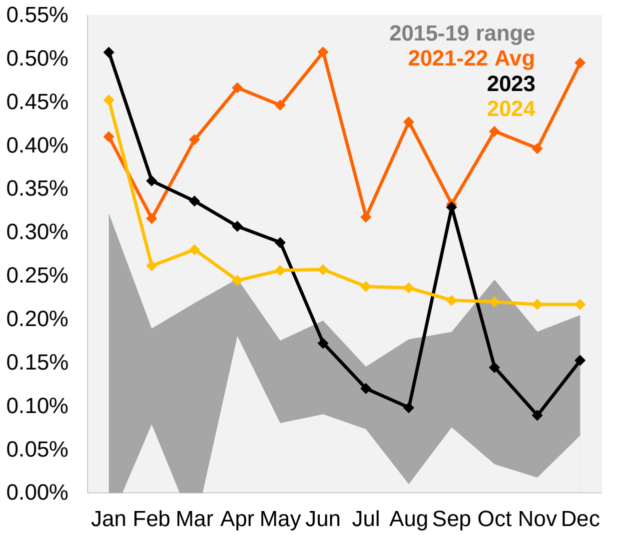
Foreign born labor force rising



Source: Haver, Itaú

Meanwhile, despite favorable supply-side developments, inflation surprised to the upside for the third consecutive month in March. High inflation persistence, at levels above the target, reduces the authorities' confidence that the spike seen in the first two months was a bump in the road in the disinflation trajectory aimed by the Fed. We still expect a slowdown in the Core PCE deflator in the coming months, but with resilient activity, wages still under pressure, amid recent upward surprises, we consider that the trajectory may be even more erratic.

Core PCE pace



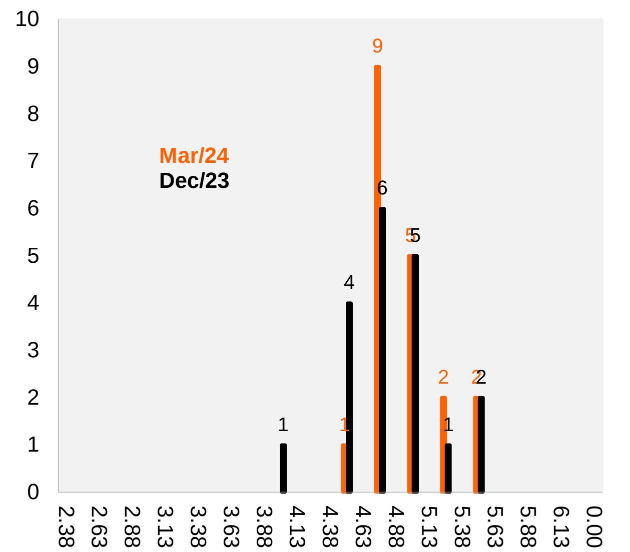
Source: Haver, Itaú

With resilient activity and more persistent inflation, the Fed will need more time to regain confidence in disinflation, which should delay the beginning of interest rate cuts.

We have shifted our expectation for the start of cuts from June to December, maintaining 3 cuts next year. At the March meeting, Federal Open Market Committee members signaled a median expectation of three rate cuts for the year, though with an asymmetrical distribution in the direction of fewer cuts. This division after a new inflation surprise should be enough for most members to dismiss the chance of interest rate cuts in the first half of the year, especially amidst a scenario of strong growth and employment, that is expected to continue. We forecast a terminal rate of 4.25-4.50%, to be reached in September 2025.

We also revised our estimate for the 10-year Treasury rate to 4.35% (from 4.0%) this year and 4.0% (from 3.75%) next year.

The Fed expects three cuts this year, but the asymmetry is for less

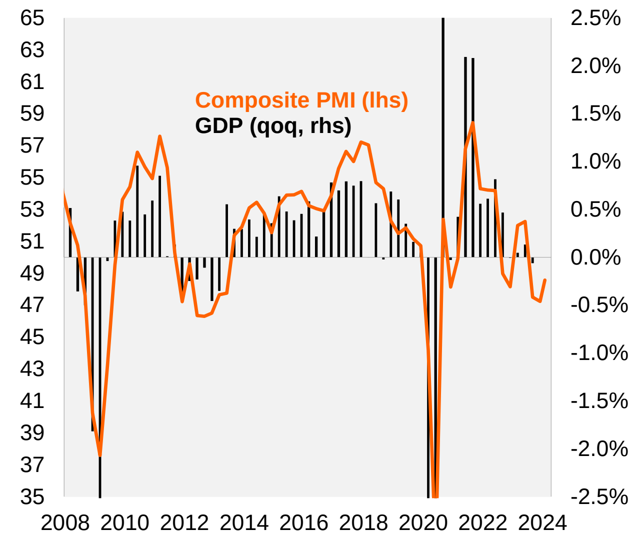


Source: Fed, Itaú

Europe: Rate cuts to start in June amid weak activity and moderating inflation

Indicators point to activity stabilization at a low level. PMI surveys showed improvement in 1Q24 driven by services, while advances in manufacturing remained modest. PMIs indicate a stable GDP in early 2024 – a still slow pace – but leaving negative territory. We anticipate 0.5% growth in the year, averaging 0.2% per quarter.

EZ PMI: consistent with flat GDP in 1Q24



Source: Haver, Itaú

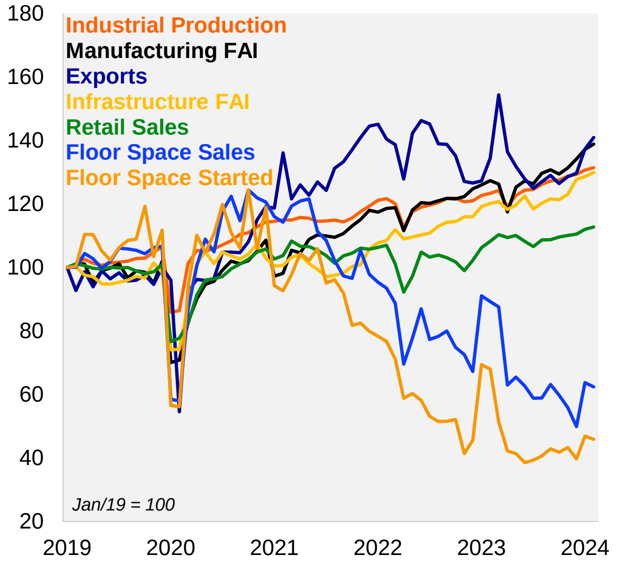
We see continuing moderation in inflation, allowing interest rate cuts from June onward. In March, core inflation receded to 0.24% mom/sa from 0.38% in February. Going forward, core inflation should go back to around 0.2% per month, with moderating services inflation (amid weak activity) and goods inflation at a low level. In this context, the first interest rate cut should happen at the June meeting, reaching 2.75% by YE24 and 2.0% in 2025.

The ECB's sharper cycle of cuts than the Fed's, in a context of weak activity, should lead to a weaker Euro going forward. We expect the Euro to reach 1.05 against the dollar in 2024 and 2025, compared to 1.08 previously.

China: Improved activity in 1Q24 amid lingering uncertainties

Improved activity in 1Q24... Figures for January and February showed that manufacturing and infrastructure remained robust. During this period, industrial production expanded 7.0% yoy (December 2023: 6.8%), while investment in infrastructure climbed 9% (close to the 10.7% pace seen at the end of 2023). Furthermore, PMI surveys continue to indicate a strong industrial performance in March, running at 50.8 (February 2024: 49.1). On the other hand, retail sales remained flat and real estate numbers are quite weak, with construction and sales plummeting 25% and 30% yoy, respectively.

Manufacturing and infrastructure offset weakness in real estate



Source: Haver, Itaú

... amid lingering uncertainties. The growth model implemented by China in recent years – encouraging domestic infrastructure and manufacturing to compensate for the slowdown in real estate – has had significant impacts on the global economy, but there are doubts as to how long it will be sustained. Firstly, China has excess production capacity in multiple industries (such as electric cars, batteries, solar panels), creating negative pressure on global prices of manufactured items. Secondly, a more challenging global geopolitical environment will likely trigger protectionist responses from other countries, curbing Chinese exports. Finally, there is a limit to how much a strong performance by manufacturing and domestic infrastructure can offset the weakness in the real estate industry. Daily home sales improved somewhat in March, but more evidence of stabilization in the sector is needed. (See Macrovision: China: a dual track economy)

In this context, our growth forecasts remain at 4.7% in 2024 and 4.5% in 2025.

Other DMs decouple from the Fed and signal that rate cuts soon; BoJ moves in the opposite direction and leaves negative rates behind

Monetary policies in developed countries became evidently more divergent in March, despite the Fed's caution regarding the start of its easing cycle.

On the one hand, the central banks of Switzerland, Australia and the UK were more dovish in their decisions. The Swiss National Bank was the first in the DM group to trim interest rates, surprising the market. The Reserve Bank of Australia removed the upward bias from its communication. The Bank of England conveyed a dovish message, with one vote for a rate reduction in the latest meeting and the Governor signaling that cuts are possible going forward.

On the other hand, the Bank of Japan left negative interest rates behind, reaching a range between 0.0% and 0.1%. However, without the prospect of more hiking, we see the yen at a weaker level of JPY/USD at 150 this year and 145 next year (135 previously for both years) and, consequently together with our Euro revision, our DXY projection was revised to 105.5 and 105.1, respectively.

LatAm: the plot thickens

Déja vu. Since our last monthly review, the main development has (again) been a further delay in the Fed's market-implied pricing on the beginning of the easing cycle, triggered by a string of stronger-than-expected data in the U.S. Our call for fewer Fed rate cuts this year, an even stronger dollar, and greater inflationary risks from oil spot prices, amid elevated geopolitical uncertainty, contribute to more caution in the ongoing easing cycles in the region.

A more gradual projected easing path. Central banks throughout the region eased as we had forecasted since our last review, with Mexico beginning the easing cycle at a 25-bp pace, taking the policy rate to 11.00%. While further declines in core inflation and a softer start in activity this year support the continuation of the easing cycle in May, we changed our call for a pause. Our end of year policy rate forecast now stands at 9.75% (previously at 9.5%) and 7.75% (previously at 7.5%) for yearend 2025.

In Brazil, the BCB delivered the unanimously expected 50-bp cut to 10.75%, yet shortened its guidance amidst more uncertainty, signaling that it envisages one last 50-bps move in its next meeting (removing the plural from previous statements) followed by 25-bps cuts starting in June. We revised our 2024 yearend rate up to 9.75% (9.25% previously).

In Chile, the BCCh unanimously delivered the expected 75-bp cut, taking the policy rate down to 6.5%, taking the total cuts in the cycle to 475-bps, with the guidance suggesting further cuts but removing the explicit reference to reaching the 4% neutral during 2H24 from the January guidance, which was then reaffirmed the IPoM's corridor. The decision and changes to the corridor were essentially in line with our rate path forecasts, in which we envisaged a sequential step down in the pace of cuts after the January 100-bps decision; we revised our yearend policy rate call up to 5.25% (from 4.75%).

In Colombia, the Board finally accelerated the pace to 50-bps, taking the policy rate to 12.25%, as we had anticipated. Even though the divided decision had members again voting for larger cuts, we expect BanRep to continue easing by 50-bps in the near term yet revised our 2024 yearend call to 8.75% (from 8.25%). In Peru, we revised our 2024 yearend call to 5.75% (up from 5.25%).

It's not over 'til it's over. Weaker currency paths, and idiosyncratic factors, led us to revise our 2024 yearend inflation calls up in Chile (+60-bps to 4.2%), and Colombia (+40-bps to 5.2%). We also revised our inflation forecast for both 2024 and 2025 in Brazil to 3.7% and 3.6% respectively (+10 bps in each year). We maintained our yearend CPI calls for Mexico (4.2%) and our above-consensus yearend inflation call in Peru (2.8%).

In Argentina, so far, so good. The stabilization program marches on, yielding a faster-than-expected improvement across nominal data and an unprecedented fiscal consolidation, contributing to a recovery of Argentinean assets. Monthly inflation decelerated, helped by the appreciation of the currency, while the fiscal balance swung positive in the first two months of the year. We now envisage a primary fiscal surplus of 0.5% of GDP in 2024 (from 0% of GDP in our previous scenario), as we still expect the economy to contract by 3% in 2024, with downside risks considering the whopping fiscal consolidation, and the decline in real wages. We still foresee inflation falling to 180% by year-end 2024, with upside risks, down from 211.4% in 2023. We also revised our nominal exchange rate down to ARS 1,500/USD by YE24 (from ARS 1,695 in our previous scenario), assuming a softer acceleration of the crawling peg policy starting in 2Q24, and we reduced our monetary policy rate forecast to 70% by year-end, from 80% previously. The macro-outlook is still fragile, with the population's still-high confidence in the administration to be tested by the effects of the stagflationary scenario in the coming months.

Global | Forecasts and Data

	2018	2019	2020	2021	2022	2023	2024F		2025F	
							Current	Previous	Current	Previous
GDP Growth										
World GDP growth - %	3.6	2.8	-2.8	6.3	3.5	3.1	**3.1**	3.1	**3.3**	3.3
USA - %	3.0	2.5	-2.2	5.8	1.9	2.5	**2.5**	2.5	**2.0**	2.0
Euro Area - %	1.8	1.6	-6.2	5.9	3.4	0.5	**0.5**	0.5	**0.9**	0.9
China - %	6.7	6.0	2.3	8.1	3.0	5.2	**4.7**	4.7	**4.5**	4.5
Interest rates and currencies										
Fed Funds - %, eop	2.27	1.55	0.09	0.08	4.4	5.3	**5.1**	4.6	**4.4**	3.9
U.S. 10 Year Treasury - %, eop	2.83	2.00	0.93	1.47	3.88	3.88	**4.35**	4.00	**4.00**	3.75
USD/EUR - eop	1.15	1.12	1.22	1.13	1.07	1.10	**1.05**	1.08	**1.05**	1.08
CNY/USD - eop	6.9	7.0	6.5	6.4	6.9	7.1	**7.2**	7.2	**7.2**	7.2
DXY Index* - eop	96.2	96.4	89.9	95.7	103.5	101.3	**105.5**	102.2	**105.1**	101.7

Source: IMF, Bloomberg and Itaú

* The DXY is a leading benchmark for the international value of the U.S. dollar, measuring its performance against a basket of currencies that includes the euro, yen, pound, Canadian dollar, Swiss franc and Swedish krona.

Compared scenario

World

	2023	2024		2025	
		Current	Previous	Current	Previous
GDP (%)	3.1	**3.1**	3.1	**3.3**	3.3

Latin America and Caribbean

	2023	2024		2025	
		Current	Previous	Current	Previous
GDP (%)	2.2	**2.0**	1.8	**2.3**	2.4

Brazil

	2023	2024		2025	
		Current	Previous	Current	Previous
GDP (%)	2.9	**2.3**	2.0	**1.8**	2.0
BRL / USD (eop)	4.86	**5.00**	4.90	**5.20**	5.10
Monetary Policy Rate (eop,%)	11.75	**9.75**	9.25	**9.75**	9.25
IPCA (%)	4.6	**3.7**	3.6	**3.6**	3.5

Mexico

	2023	2024		2025	
		Current	Previous	Current	Previous
GDP (%)	3.2	**2.8**	2.8	**1.8**	1.8
MXN / USD (eop)	16.97	**17.9**	18.2	**18.9**	19.3
Monetary Policy Rate (eop,%)	11.25	**9.75**	9.50	**7.75**	7.50
CPI (%)	4.7	**4.2**	4.2	**3.7**	3.7

Argentina

	2023	2024		2025	
		Current	Previous	Current	Previous
GDP (%)	-1.6	**-3.0**	-3.0	**2.5**	2.5
ARS / USD (eop)	809	**1500**	1695	**2350**	2650
Reference rate (eop,%)	100.0	**70.0**	80.0	**60.0**	60.0
CPI (%)	211.4	**180.0**	180.0	**60.0**	60.0

Chile

	2023	2024		2025	
		Current	Previous	Current	Previous
GDP (%)	0.2	**2.4**	1.7	**2.0**	2.2
CLP / USD (eop)	879	**920**	890	**850**	830
Monetary Policy Rate (eop,%)	8.25	**5.25**	4.75	**4.5**	4.50
CPI (%)	3.9	**4.1**	3.5	**3.1**	3.0

Colombia

	2023	2024		2025	
		Current	Previous	Current	Previous
GDP (%)	0.6	**1.0**	1.0	**2.6**	2.9
COP / USD (eop)	3855	**4000**	3880	**4000**	3890
Monetary Policy Rate (eop,%)	13.00	**8.75**	8.25	**6.00**	5.25
CPI (%)	9.3	**5.2**	4.8	**3.0**	3.0

Peru

	2023	2024		2025	
		Current	Previous	Current	Previous
GDP (%)	-0.6	**2.5**	2.5	**3.0**	3.0
PEN / USD (eop)	3.70	**3.75**	3.75	**3.77**	3.77
Monetary Policy Rate (eop,%)	6.75	**5.75**	5.25	**4.25**	4.25
CPI (%)	3.2	**2.8**	2.8	**2.5**	2.5

Source: Itau

Commodities

	2019	2020	2021	2022	2023	2024		2025	
						Current	*Previous*	*Current*	*Previous*
Brent Oil	64	50	75	82	77	**80**	80	**75**	75
Iron Ore	90	153	116	110	135	**110**	110	**90**	90
Copper	7788	7788	9525	8402	8489	**8500**	8500	**8600**	8600
Corn	383	437	592	656	480	**400**	400	**380**	380
Soy	912	1207	1290	1474	1311	**1100**	1100	**950**	950
Wheat	540	604	790	757	669	**610**	610	**600**	600
Sugar	13	15	19	20	22	**23**	23	**20**	20
Coffee	130	123	235	166	188	**170**	170	**150**	150

Source: BBG, Itaú

Macro Research – Itaú

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