ABN·AMRO

Macro Weekly

A lot of noise

Group Economics

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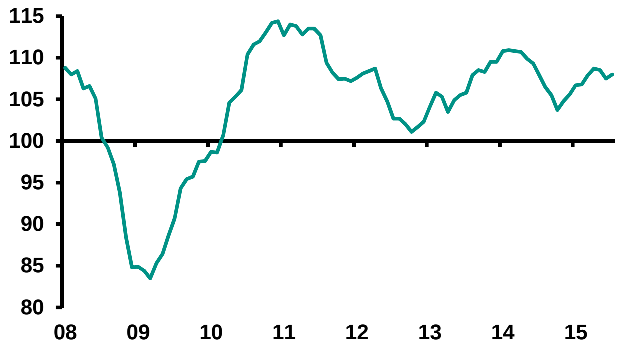
We are back from holidays. A lot has happened during the last couple of weeks and there is a broad spectrum of concerns, ranging from Greece to China and the strength of the global economy. Despite these concerns, I think the global economy is likely to strengthen in the period ahead. It is easy to worry about unexpected developments, but it is important to focus on what are the key drivers of the global economy.

The global cycle is set to strengthen

We have long held the view that the global economy is likely to gain speed in the second half of the year. That remains our view. Indeed, I think recent indicators are suggesting that we are right.

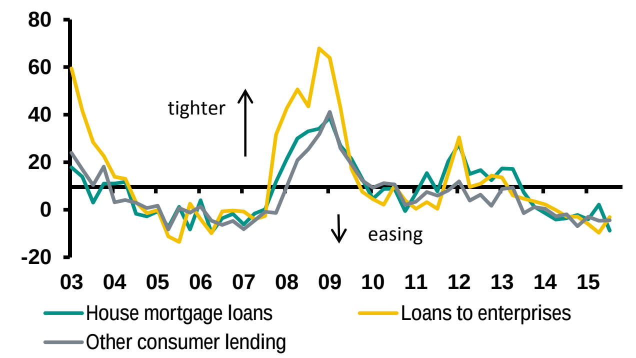
Germany: Ifo index



Source: Bloomberg

Recent confidence indicators in the eurozone are showing an improvement. And various variables are painting a consistent picture of an economy that is accelerating. The authoritative German Ifo index of business confidence rose unexpectedly in July after two consecutive monthly declines. The European Commission's index of Economic Sentiment, which combines business confidence in various sectors and consumer confidence rose to the highest level of the year, and in fact the highest level since 2011 in July. It has moved sideways since March. During my holidays the ECB's bank lending survey had shown a continued modest easing of lending criteria by commercial banks and the credit and money growth data for June were also encouraging.

Eurozone bank lending survey (ECB)



Source: Thomson Reuters Datastream

I cannot see what should disturb this positive pattern in the near term. The Greek saga does not appear to have had a noticeable negative impact, except for the Greek economy. The recent, renewed drop in oil prices will provide an additional, though small boost, offsetting any negative impact from borrowing costs which have risen somewhat since April.

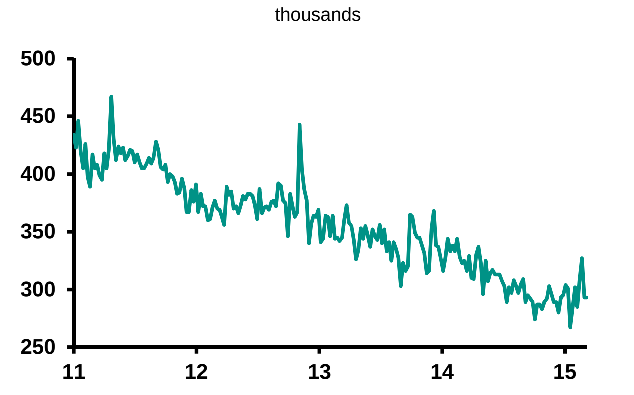
The stronger tone to the overall eurozone economy is having an impact on inflation. While headline inflation was unchanged in July at 0.2%, core inflation edged higher to 1.0%, up from 0.8%. While this is preliminary data, the stronger core inflation numbers appear to be broad based. I do not think that we are going to see a strong increase in inflation, I do believe that the recent trend underscores our assertion that deflation worries were overdone and that painful deflation does not tend to take hold in an economy where growth is accelerating.

US also likely to strengthen

US GDP growth amounted to 2.3% qoq annualised in Q2. That was a tad below expectations, but the number for Q1 was revised up from -0.2% to +0.6%. There has been a lot of debate about the accuracy of the US GDP data. A large majority of economists have argued that there is something wrong with the data as Q1 appears to be consistently the weakest quarter. The suggestion is that there is a problem with the seasonal adjustments carried out on the original data. The statisticians have now tried to address these issues, which contributed to the upward revision of the Q1 data. Nevertheless, over longer periods the data for the first quarter remains relatively weak.

It seems to me that we must acknowledge that GDP is simply difficult to measure. Indeed, it is getting ever more difficult to measure as services are by far the largest sector in the economy and electronics are playing an increasingly dominant role in the economy. While interpreting the trend in the economy we must, therefore, look at other data as well. The labour market is an important variable. And data on the labour market is much easier to obtain that on GDP. How difficult is it to count the number of jobless? It must therefore be more reliable. Recent trends are positive. Jobless claims continue to move lower. The last two weeks in particular jobless claims have undershot expectations.

US: initial jobless claims



Source: Bloomberg

There are concerns over productivity growth. Productivity growth has been very weak in the last couple of quarters. While I think productivity is hugely important, I would warn against reading too much into the data. As argued above, GDP is difficult to measure. If the official data is underestimating GDP growth, then productivity growth is also underestimated. The combination of robust data on the labour market and on corporate earnings suggests that the official data may well underestimate productivity.

China

Another area of concern is the Chinese slowdown and the decline in equity prices in China. I think this is hard to gauge. There is no doubt that Chinese growth has slowed. It is also likely it will continue to slow. The question is at what pace. Looking at the data, I am inclined to think that most Chinese data do not suggest that the economy is in a free fall. However, anecdotal evidence is not positive. Western companies are reporting weakening business conditions. We continue to believe that Chinese authorities have the means and the skills to prevent a hard landing of the economy. So we are not overly concerned.

The stock market is a focus point for commentators, in particular those who warn for problems ahead. We must see this in perspective. True, Chinese equities are some 30% down from their peak. However, the are also some 10-15% up since the beginning of the year and some 65-70 on a twelve month basis. In addition, the stock market in China does not have a strong bearing on the overall economy, nor is the correlation between Chinese stock prices and other equity markets around the world very high. I do not want to downplay the relevance of what is happening, but I am not too concerned about recent developments at this particular point.

The Greek saga is not over yet

While I was on holidays, Greece and its partners reach a deal. Well,... it was more like a deal to negotiate a new deal. This was welcome and it is progress, but it is too early to claim victory. Nobody seems particularly happy about the deal. Prime minister Tsipras has expressed his reservations and the IMF believes that Greek debt is unsustainable and is therefore not (yet) prepared to provide funds. Electoral support in Greece seems to be large, but many Syriza parliamentary representatives are against the conditions set for the deal. It is hard to see how this will move along smoothly.

It is to be hoped that negotiations do not fall apart again. What Greece needs more than ever now is economic growth. In my opinion there is too little emphasis on efforts to generate more growth. The various parties also seem to have very different views on how a achieve growth, but perhaps they can find some common ground. It is extremely sad to see that the Greek economy has fallen back into contraction after it had started to recover a little in the course of last year. Fingers crossed.

Main economic/financial forecasts

GDP growth (%)	2013	2014	2015e	2016e	3M interbank rate	23/07/2015	30/07/2015	+3M	+12M	2015e	2016e
United States	1.5	2.4	2.7	3.1	United States	0.30	0.30	0.7	1.5	0.9	2.4
Eurozone	-0.3	0.9	1.8	2.3	Eurozone	-0.02	-0.02	0.00	0.00	0.00	0.10
Japan	1.6	-0.1	1.1	1.2	Japan	0.17	0.17	0.2	0.2	0.2	0.2
United Kingdom	1.7	3.0	2.8	2.6	United Kingdom	0.58	0.58	0.6	1.5	1.0	2.0
China	7.7	7.4	7.0	7.0							
World	3.2	3.3	3.2	3.8							
Inflation (%)	**2013**	**2014**	**2015e**	**2016e**	**10Y interest rate**	**23/07/2015**	**30/07/2015**	**+3M**	**+12M**	**2015e**	**2016e**
United States	1.5	1.6	0.4	2.4	US Treasury	2.27	2.26	2.7	3.0	2.8	3.0
Eurozone	1.3	0.4	0.4	1.7	German Bund	0.74	0.66	0.8	1.6	0.9	1.8
Japan	0.3	2.8	0.8	1.4	Euro swap rate	1.05	1.00	1.1	1.9	1.2	2.0
United Kingdom	2.6	1.5	1.1	1.9	Japanese gov. bonds	0.42	0.42	0.6	1.0	0.7	1.0
China	2.6	2.0	1.5	2.0	UK gilts	2.01	1.97	1.7	2.5	2.0	2.7
World	4.3	3.9	3.9	3.9							
Key policy rate	**30/07/2015**	**+3M**	**2015e**	**2016e**	**Currencies**	**23/07/2015**	**30/07/2015**	**+3M**	**+12M**	**2015e**	**2016e**
Federal Reserve	0.25	0.50	0.75	2.25	EUR/USD	1.10	1.09	1.00	1.05	1.00	1.15
European Central Bank	0.05	0.05	0.05	0.05	USD/JPY	123.9	124.1	125	135	128	135
Bank of Japan	0.10	0.10	0.10	0.10	GBP/USD	1.55	1.56	1.47	1.50	1.49	1.51
Bank of England	0.50	0.50	0.75	1.75	EUR/GBP	0.71	0.70	0.68	0.70	0.67	0.76
People's Bank of China	4.85	4.60	4.60	4.60	USD/CNY	6.21	6.21	6.26	6.37	6.30	6.40

Source: Thomson Reuters Datastream, ABN AMRO Group Economics.

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