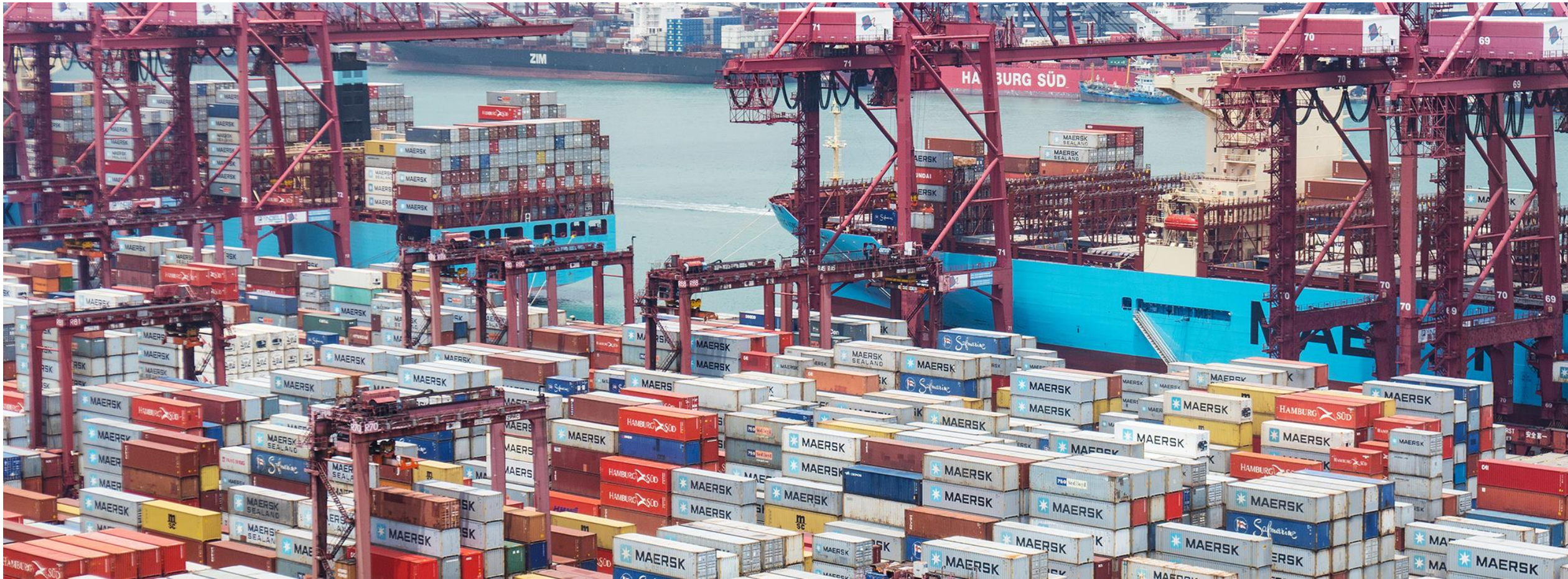
Global Economic and Financial Outlook

Zürcher Kantonalbank

CEE-Swiss Impulse Sessions | Chamber of Commerce Switzerland – Central Europe (SEC)

Dr. Martin Weder | Chief Economist and Head of Economic Research | April 16, 2024



Economic and Financial Outlook

Economic Outlook: Recession in most advanced economies averted – but growth will likely remain low

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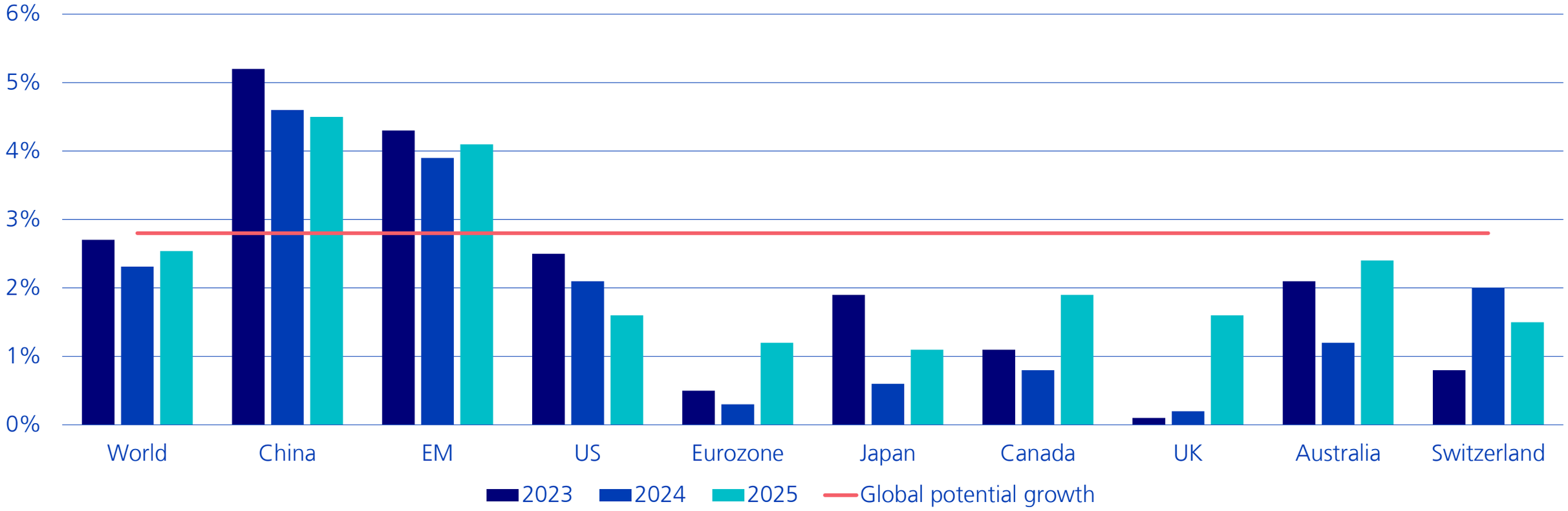
Annual real GDP growth in percent

Realised and projected economic growth rates

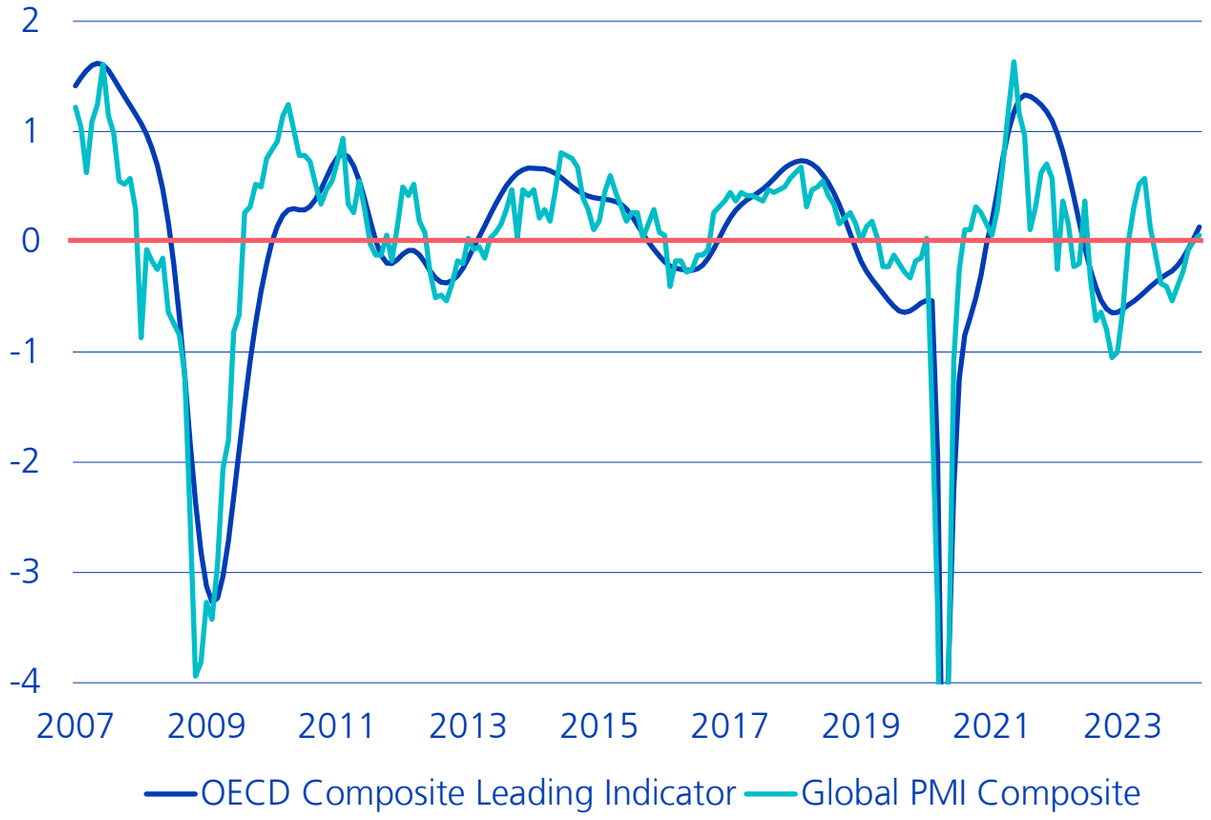


Sources: Zürcher Kantonalbank, Refinitiv

Economic Outlook: Global leading indicators continue to brighten – economic data better than expected

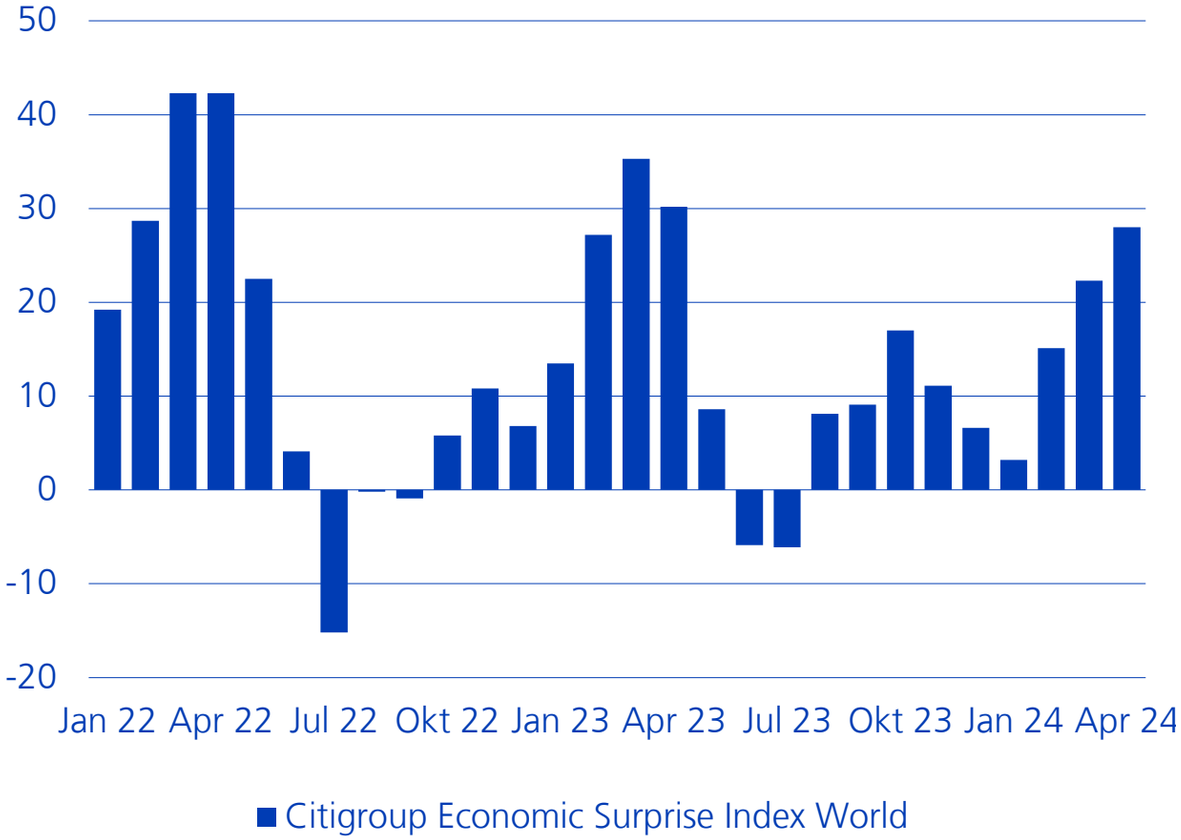
Leading economic indicators are rising

Standardised values (z-scores)



Economic data continue to surprise on the positive side

Citigroup Global Economic Surprise Index



Sources: Zürcher Kantonalbank, Refinitiv

Central and Eastern Europe: Economic Sentiment is improving, but remains below its long-term average

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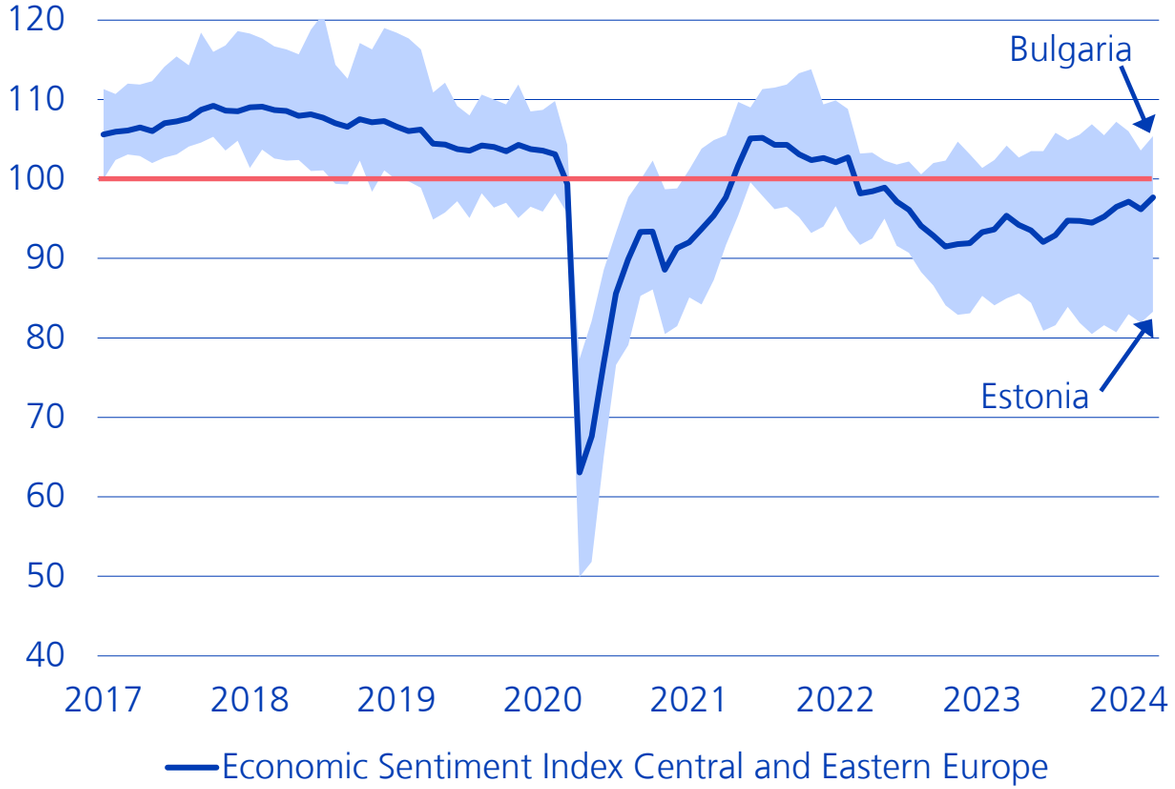
Slow recovery after reaching trough in late 2022

Economic Sentiment Indicator (long-run average = 100)



Economic Sentiment is a good proxy for growth

Monthly indicator based on surveys

- Composite indicator produced by European Commission
- Objective is to track GDP growth in EU member states
- ESI is a weighted average of five sectors:
  - Industry (40%)
  - Services (30%)
  - Consumers (20%)
  - Retail (5%)
  - Construction (5%)
- Scaled to a long-term mean of 100
- Values above 100 indicate above-average growth

Sources: Zürcher Kantonalbank, Refinitiv

Central and Eastern Europe:
Positive and rising growth rates expected in 2024 and 2025

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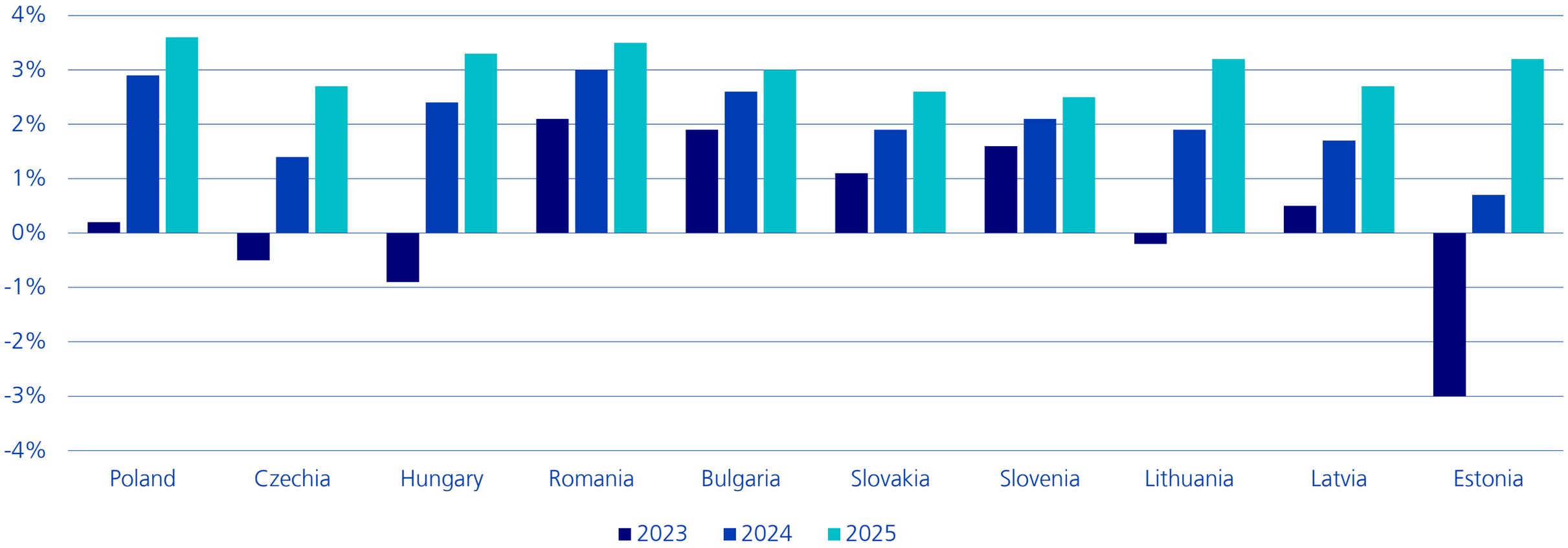
Annual real GDP growth in percent



Sources: Zürcher Kantonalbank, Bloomberg

Inflation: Despite ongoing downward trend, annual rates mostly remain above their respective targets

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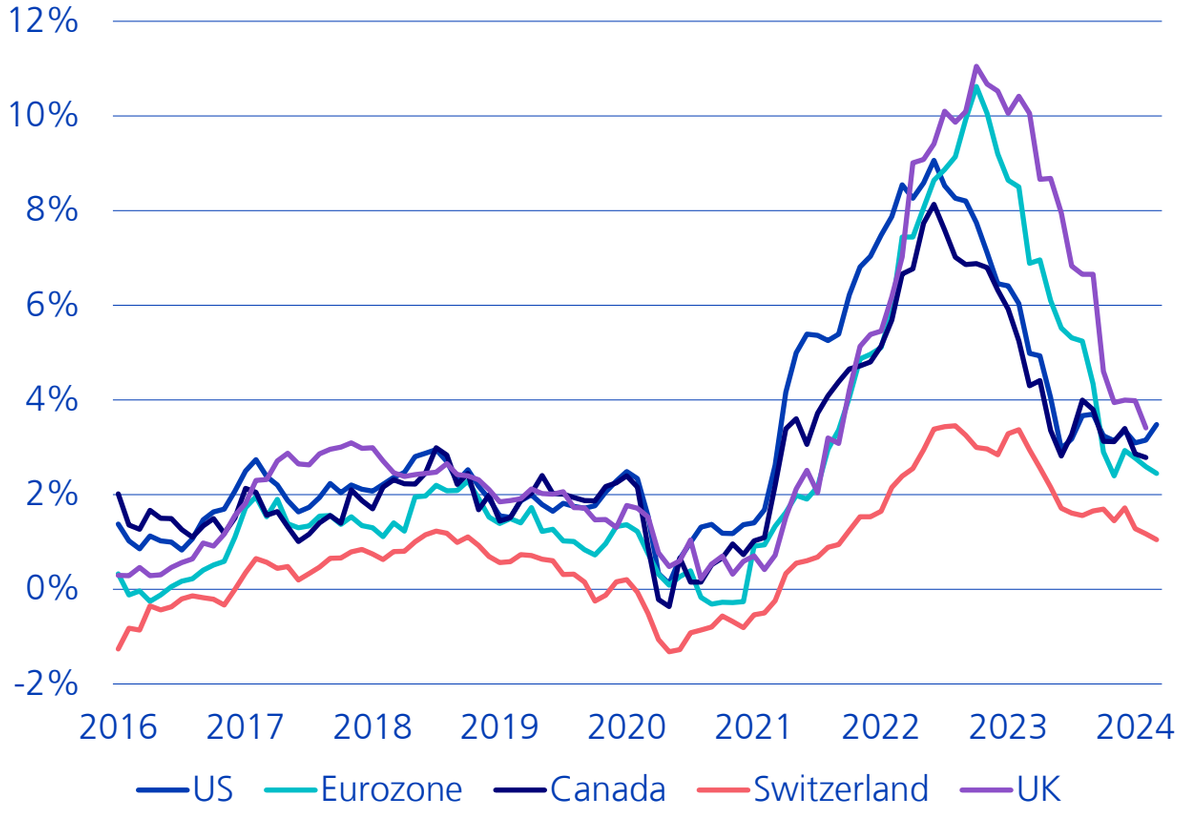
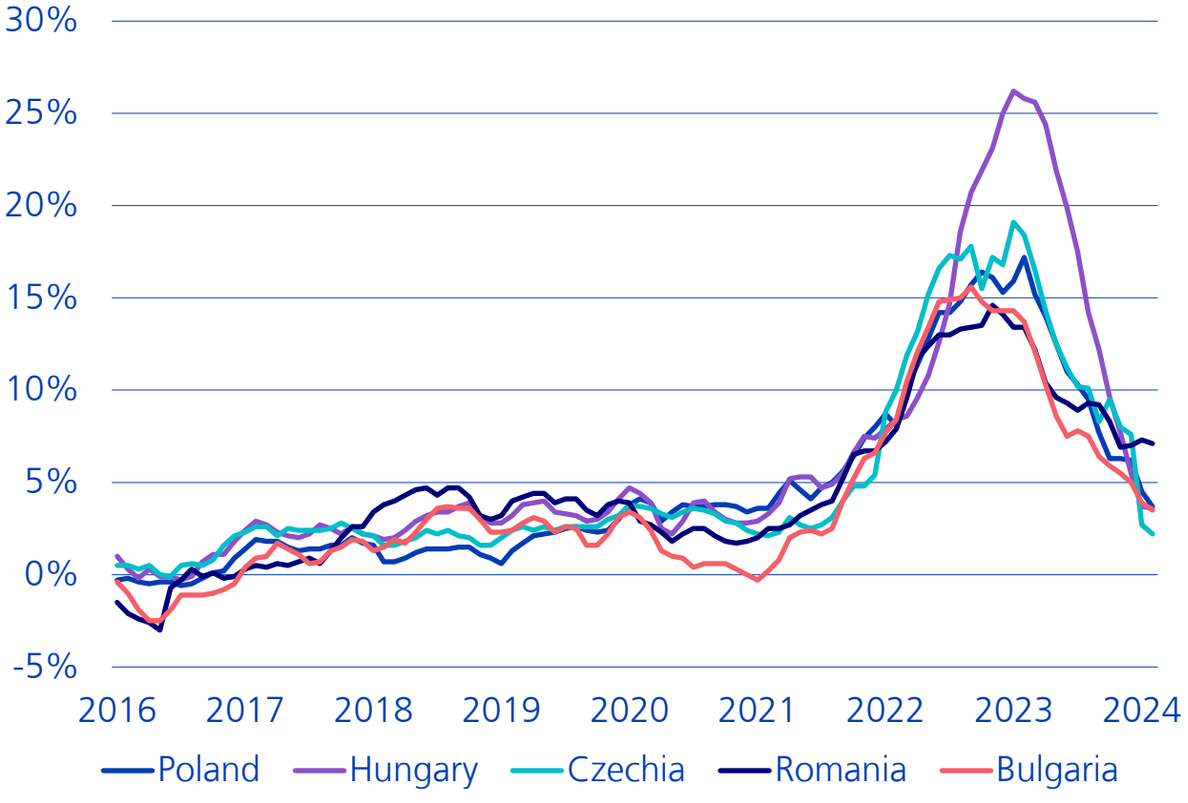
Inflation in the US is rising again

Headline inflation rates in percent



CEE: Downward trend continues outside of Romania

Headline inflation rates in percent



Sources: Zürcher Kantonalbank, Refinitiv

Inflation: And now for the hardest part...

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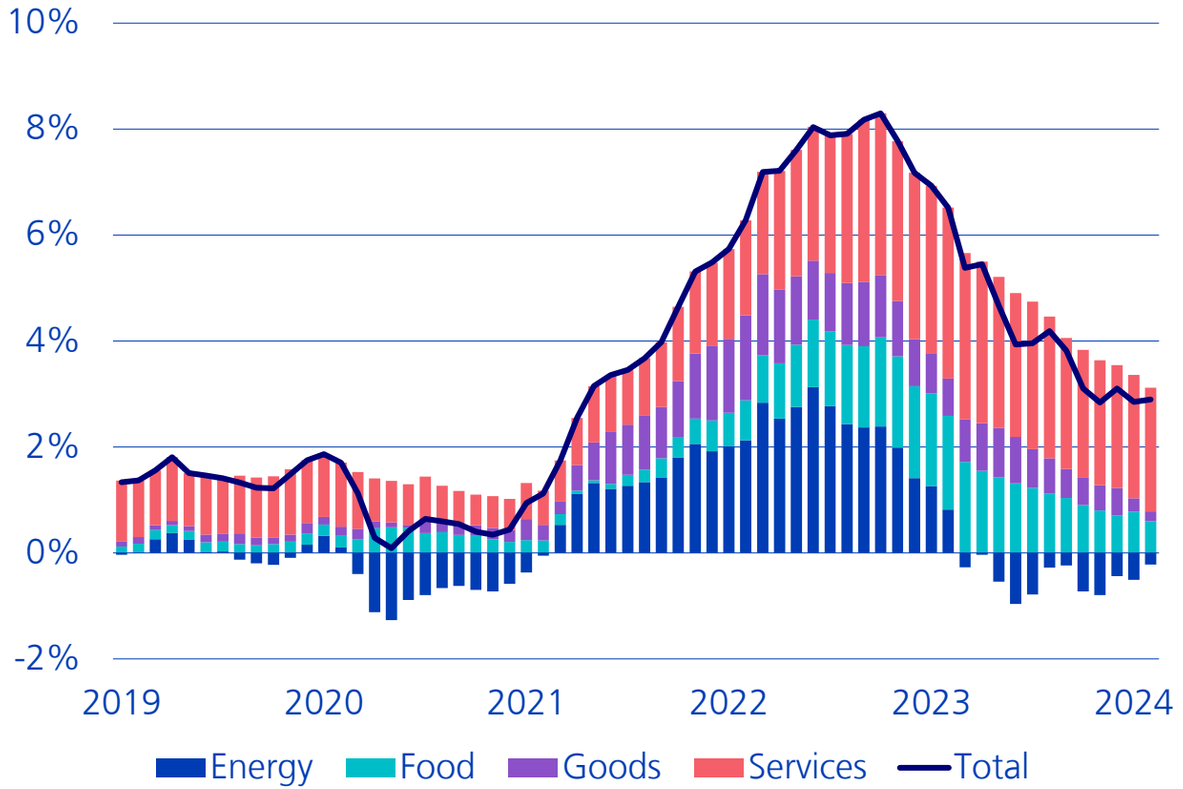
Services inflation turns out to be sticky

Contribution to inflation in advanced economies



What's driving inflation today?

Inflation has changed its character over time

- Energy and food prices are normalising
- Supply bottlenecks have mostly disappeared
- Services now account for more than 80% of inflation:
  - Wages are still rising strongly in most countries
  - Shelter costs and rents are an important driver
  - Health care
  - Leisure and hospitality
  - Transport and travel

Central and Eastern Europe:
Inflation will fall further and reach «average levels» in 2024/25

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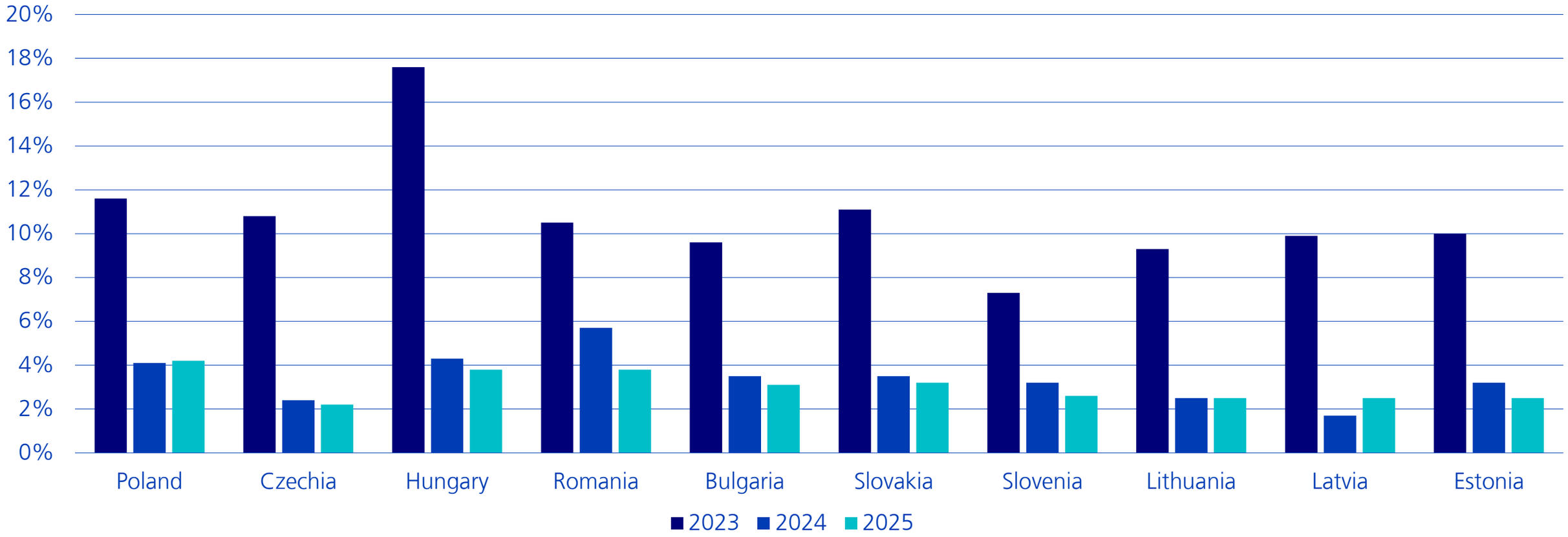
Annual average inflation in percent



Sources: Zürcher Kantonalbank, Bloomberg

Monetary policy:
Waiting for rate cuts by the biggest central banks

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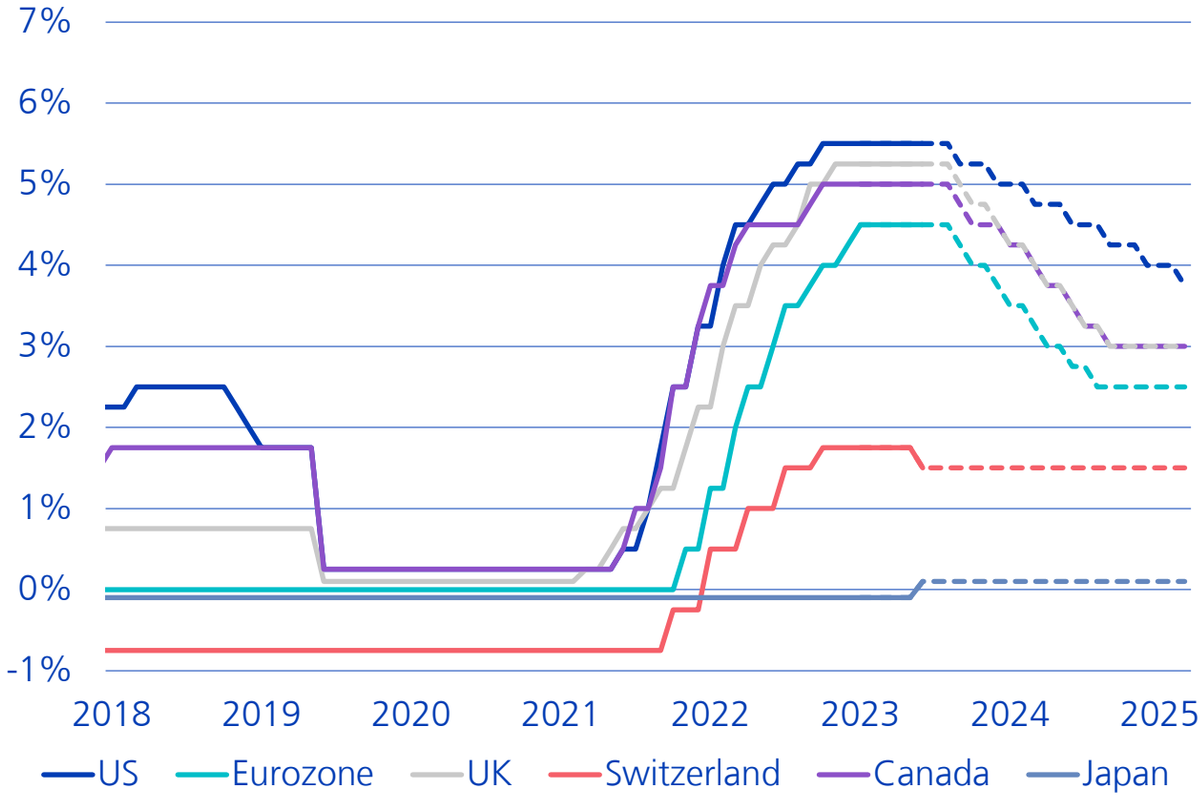
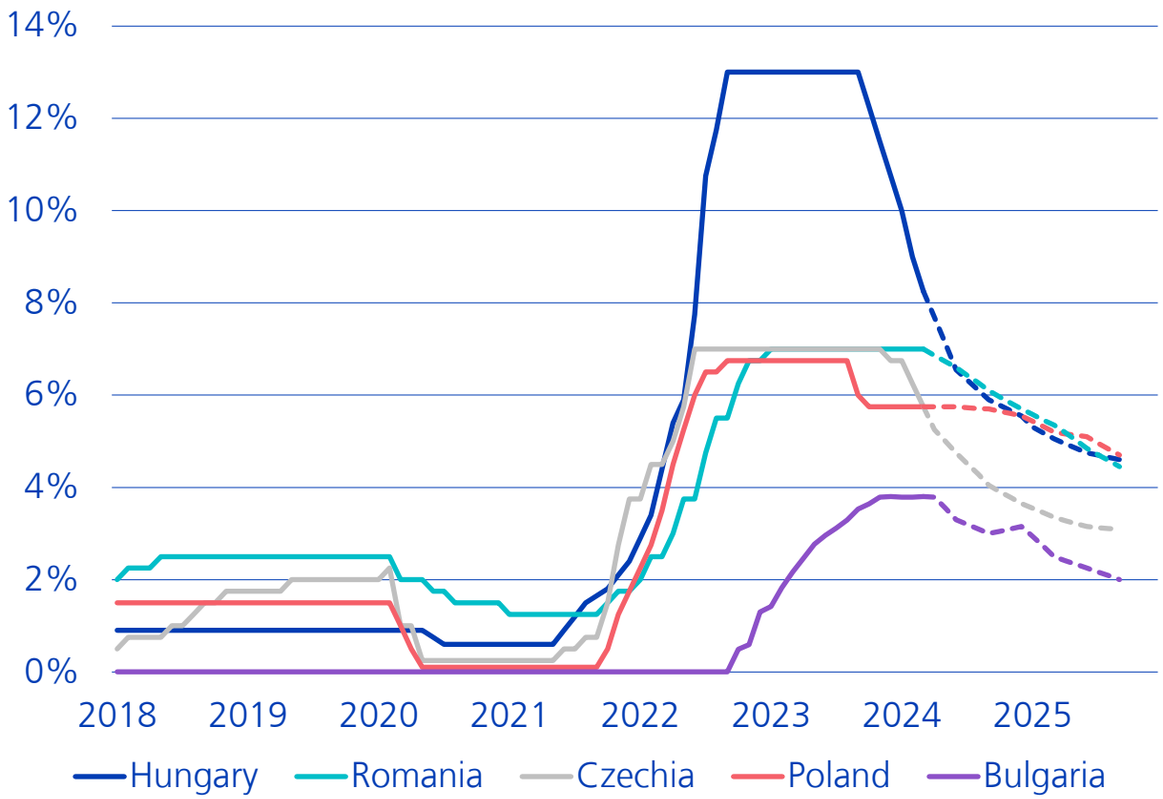
SNB surprised markets by cutting rates in March 2024

Key interest rates in percent



CEE: Rate cuts are already well on their way

Key interest rates in percent



Sources: Zürcher Kantonalbank, Bloomberg, Refinitiv

Financial Markets: A touch of «goldilocks» in equity markets collides with highly volatile bond markets

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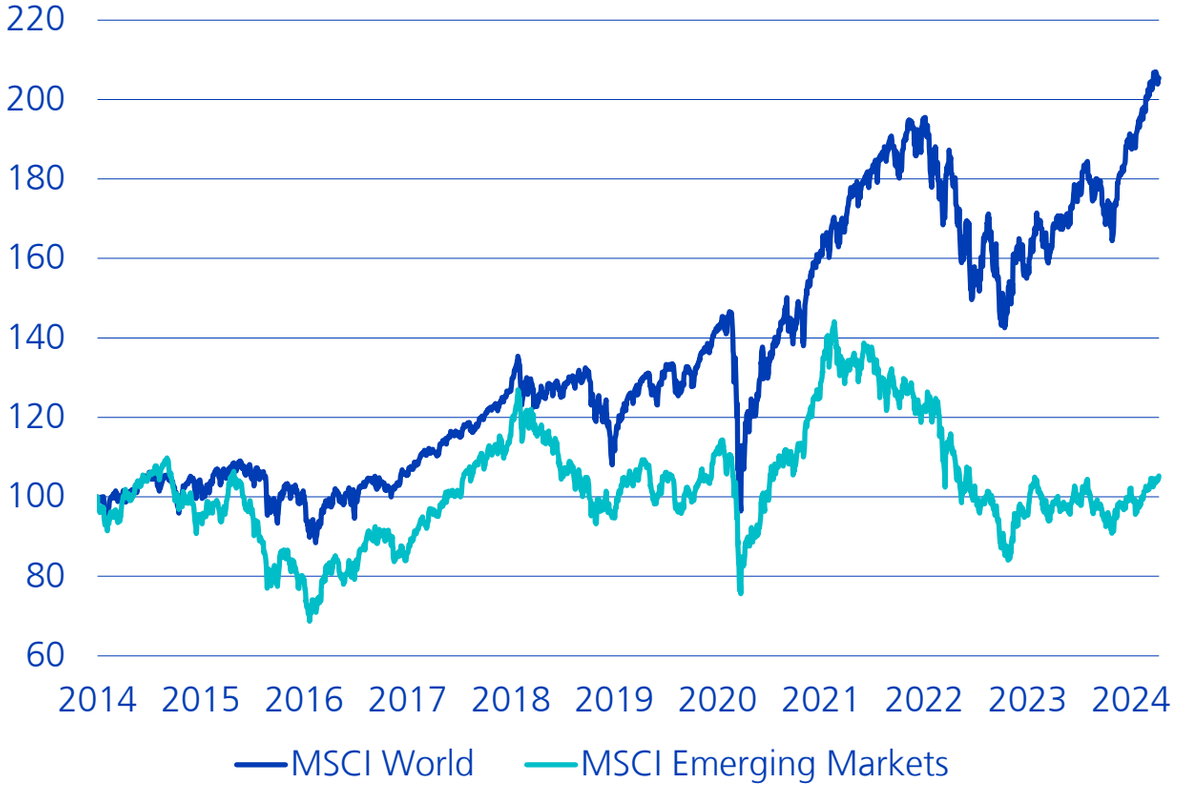
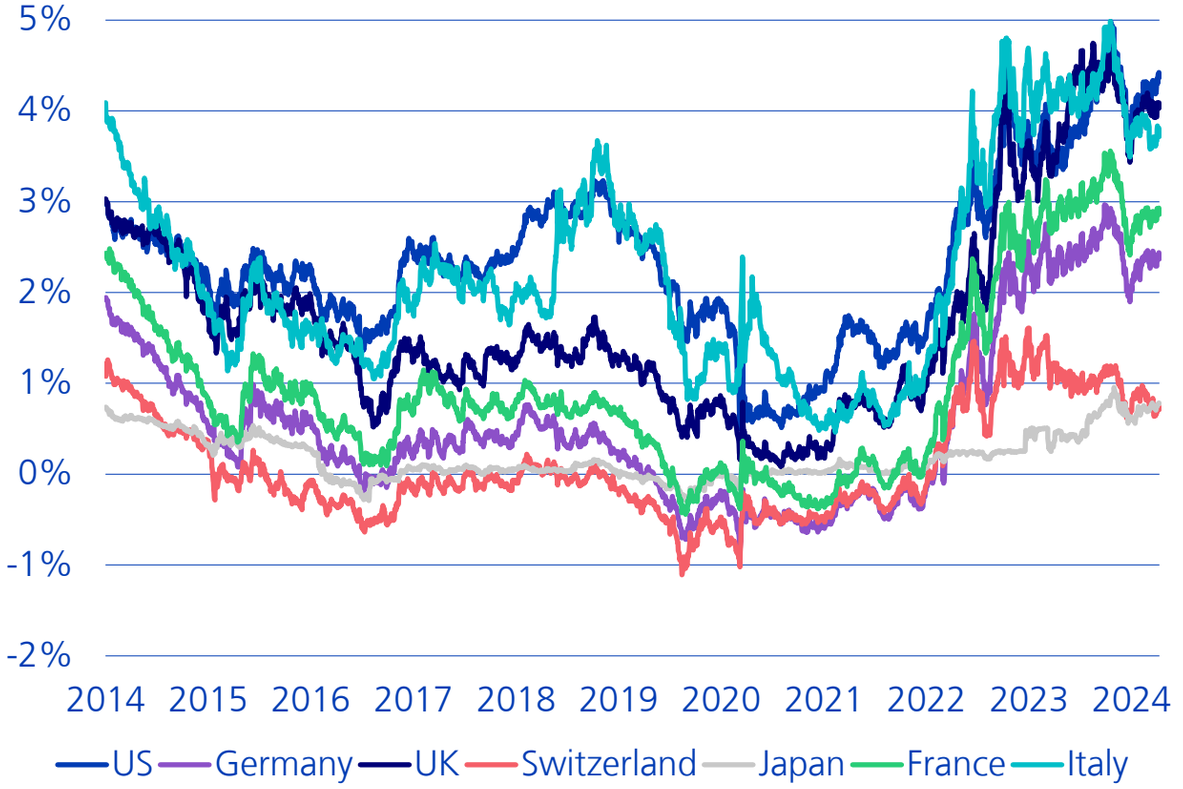
Equity markets have reached new all-time highs

Equity indices (start of 2014 = 100)



Long-term yields remain elevated

10-year government bond yields in percent



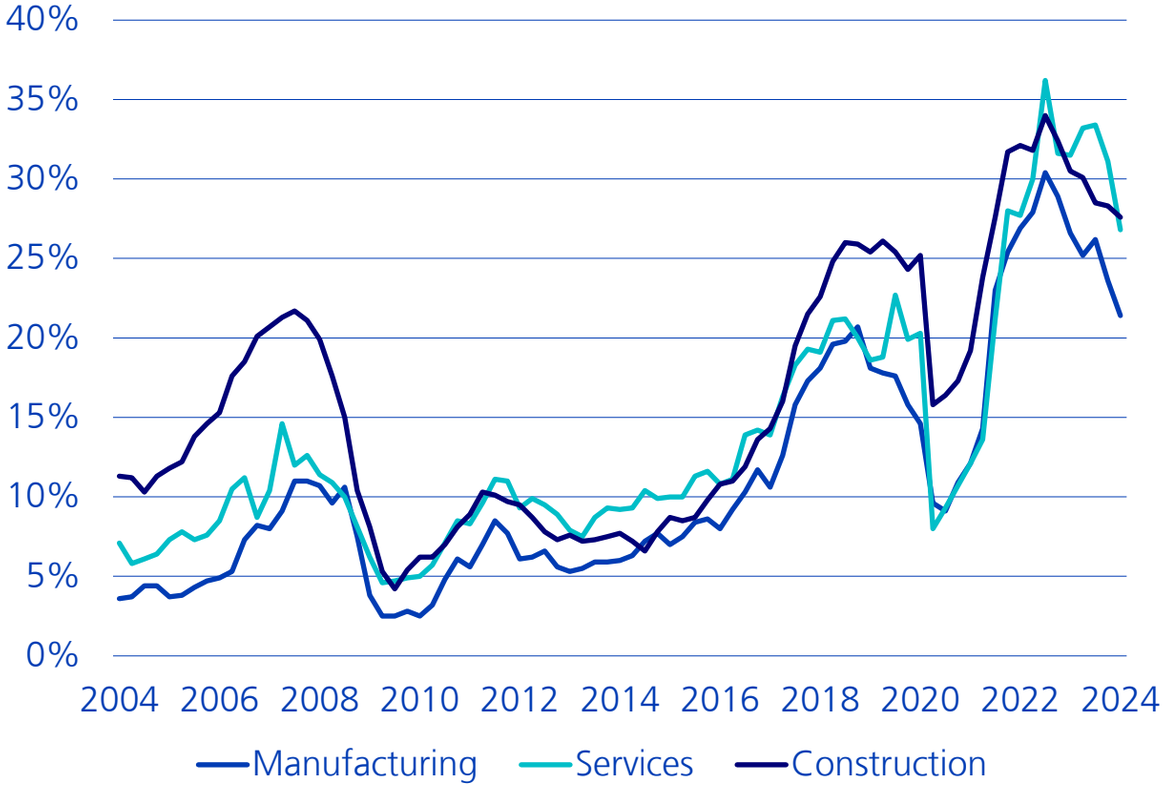
Sources: Zürcher Kantonalbank, Refinitiv

Demographics

Labour market: Shortage of skilled workers remains a big concern despite cyclical slowdown

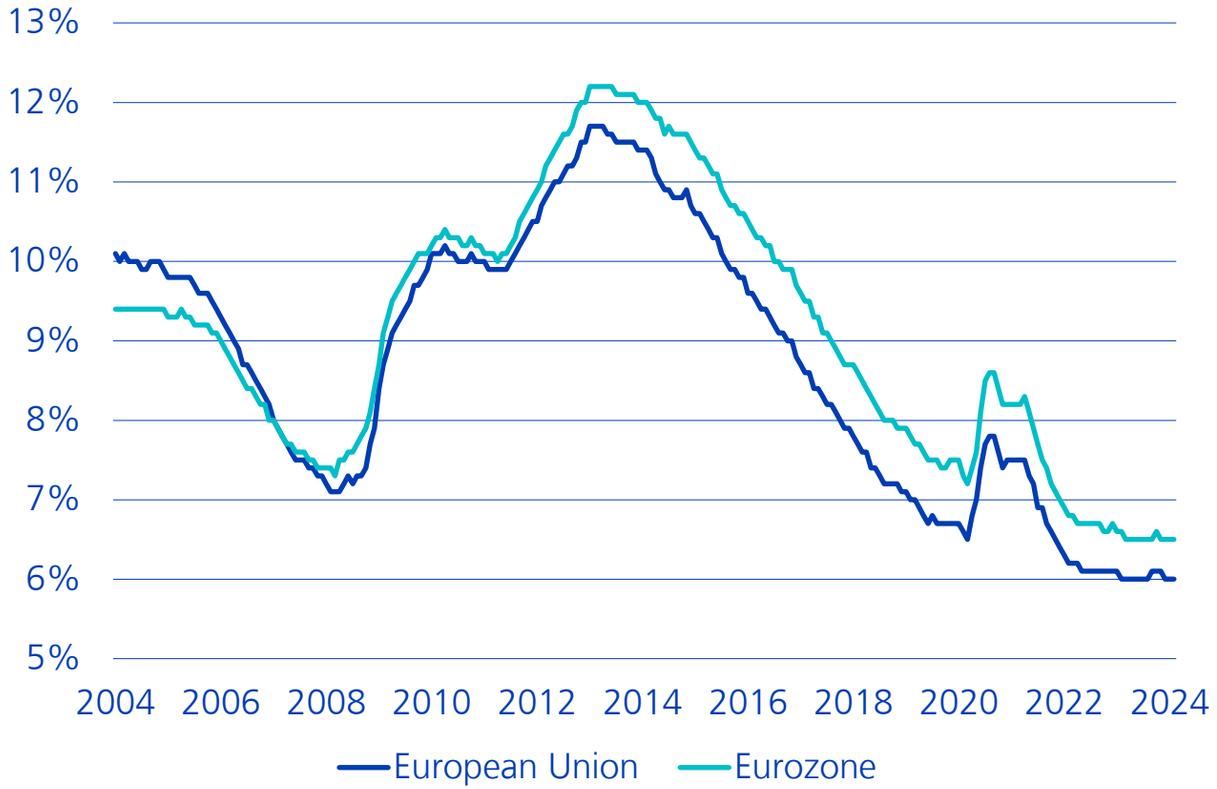
Structural rise interrupted by cyclical fluctuations

Share of firms that cite labour as factor limiting production



Unemployment is currently at an all-time low

Seasonally adjusted unemployment rates in percent



Sources: Zürcher Kantonalbank, Refinitiv

Labour market: It's going to get worse – working-age population is declining almost everywhere

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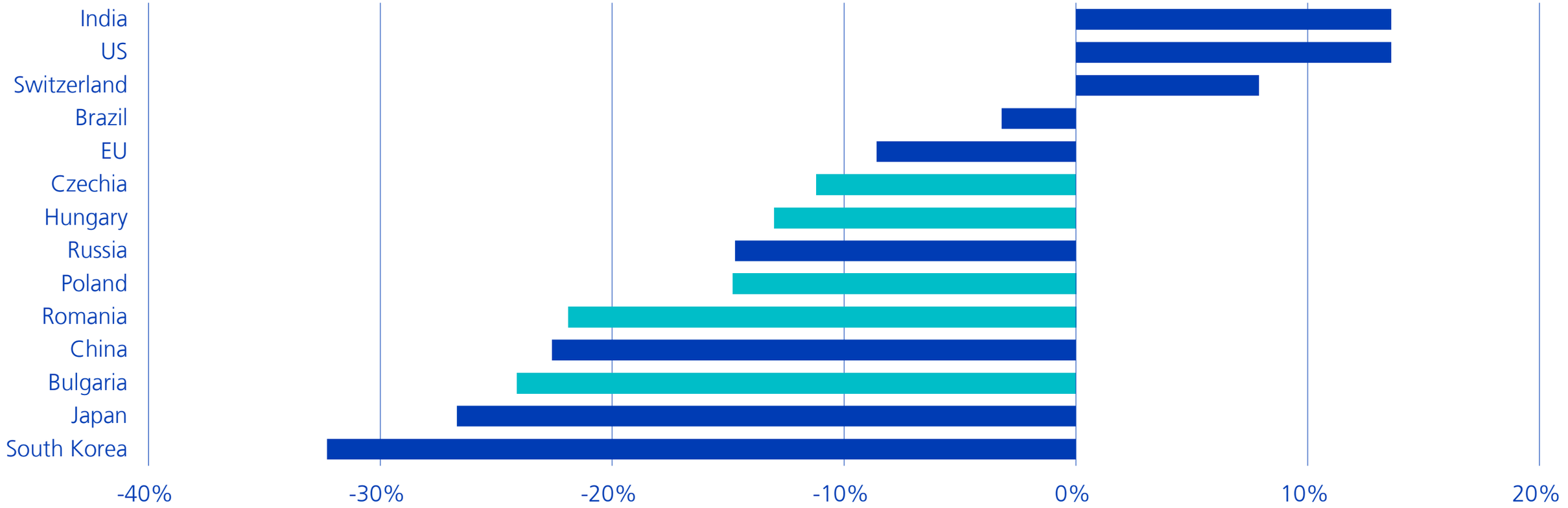
The situation is even worse in East Asia

Change in working-age population (age 15 to 64) from today to 2050 in percent



Sources: Zürcher Kantonalbank, Oxford Economics, Refinitiv

Labour market: Wage growth in Central and Eastern Europe is significantly higher than in the West – and will remain so

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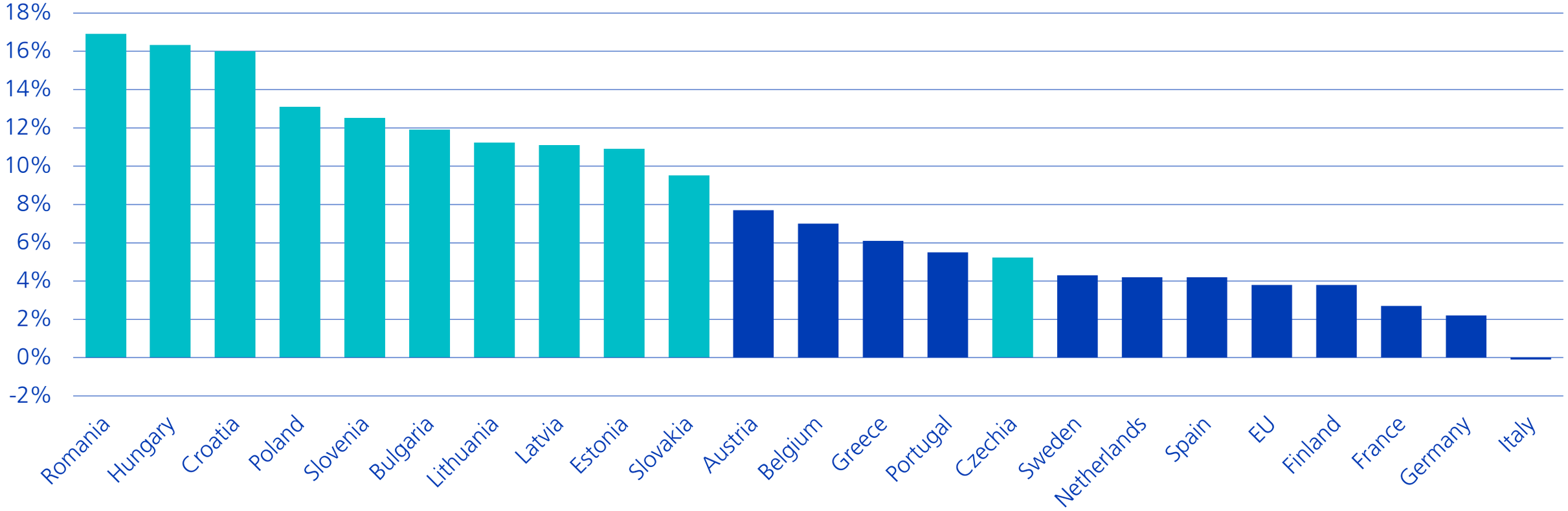
Wages in many Central and Eastern Europe are still rising at double-digit rates

Nominal hourly labour costs of whole economy (annual change in percent, end of 2023)



Sources: Zürcher Kantonalbank, Eurostat

Geopolitics and the fracturing of the world economy

Deglobalisation: Not yet a reality, but harmful trade interventions are increasingly having an impact

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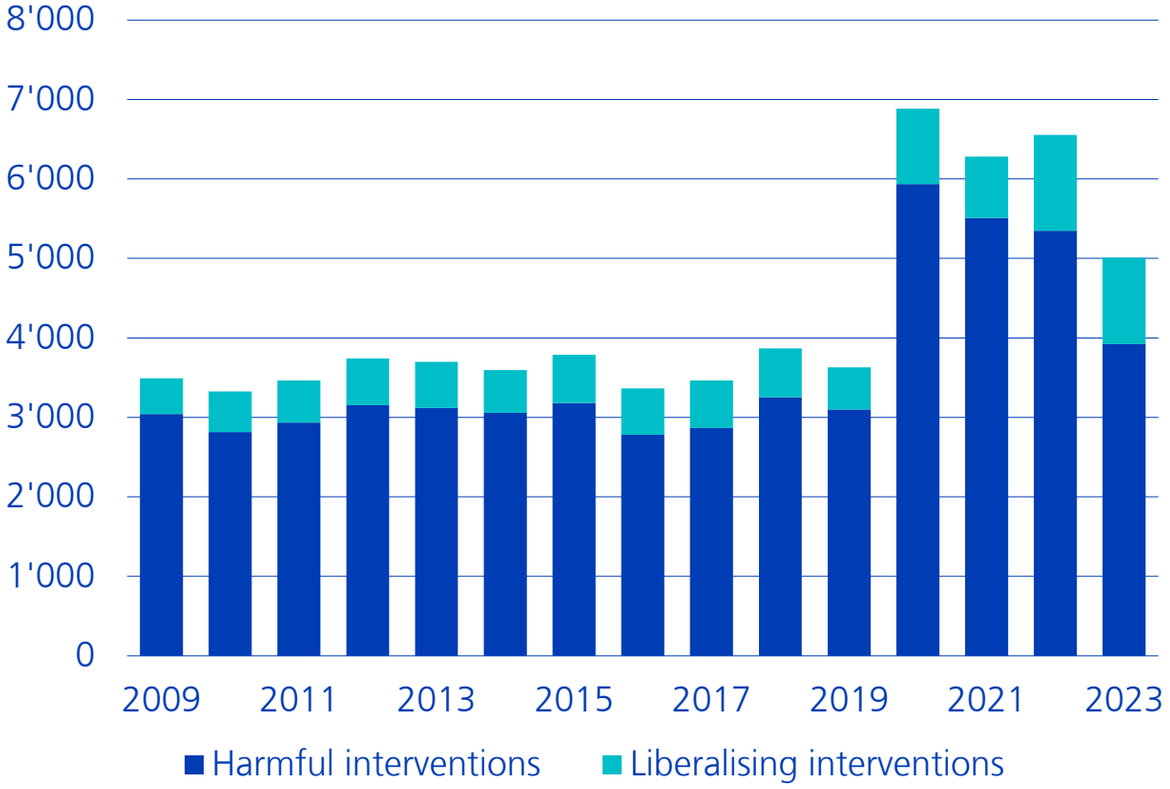
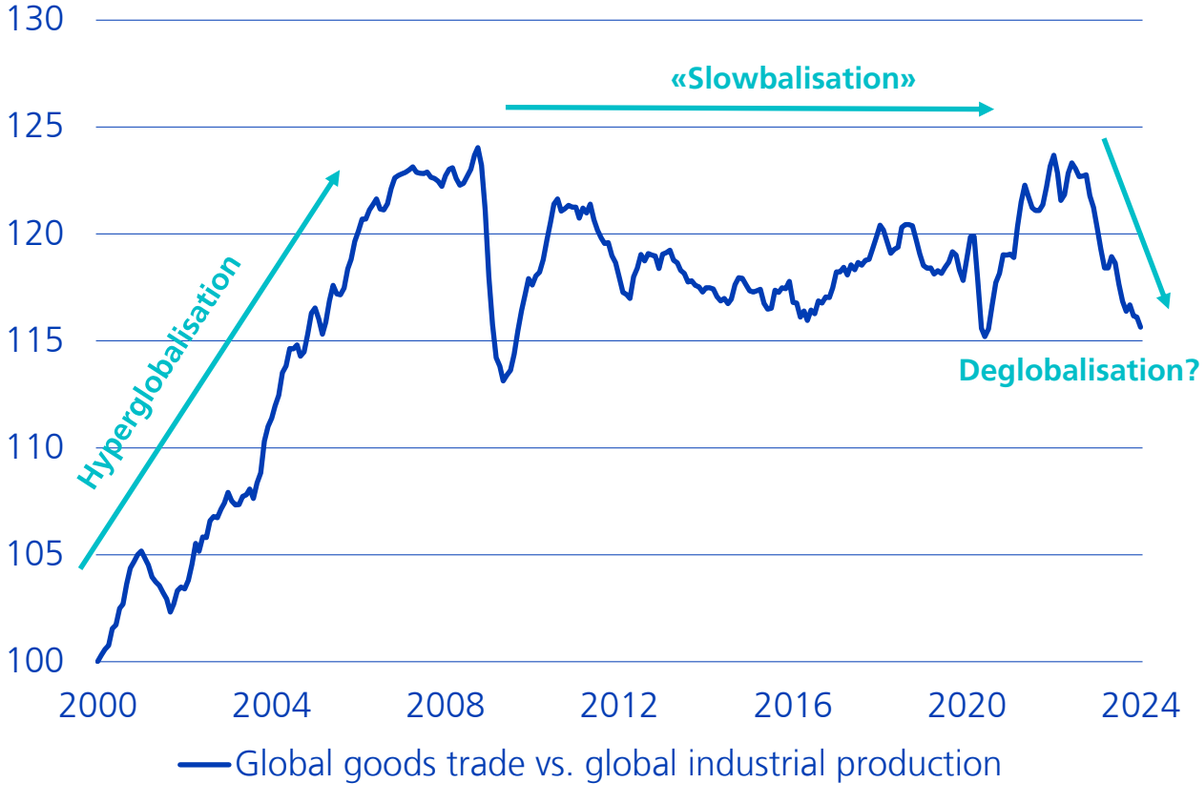
Harmful trade interventions have risen sharply in recent years

Number of global interventions per year



Trade is no longer growing more rapidly than production

Goods trade relative to industrial production (index, early 2000 = 100)



Sources: Zürcher Kantonalbank, Global Trade Alert, Refinitiv

The global economy is fracturing into China- and US-aligned blocs

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US & Allies	Leans US	Unaligned	Leans China	China & Allies
Poland	Hungary		Kazakhstan	Russia
Romania	Cyprus		Uzbekistan	Belarus
Czechia	Georgia		Serbia	Tajikistan
Ukraine	Moldova		Azerbaijan	Kyrgyzstan
Slovakia			Armenia	
Bulgaria				
Croatia				
Lithuania				
Slovenia				
Latvia				
Estonia				
Bosnia and Herzegovina				
Albania				
North Macedonia				
Kosovo				
Montenegro				

Sources: Zürcher Kantonalbank, Capital Economics

The shape of a divided world: «De-risking» instead of «De-coupling» is the right strategy for Europe

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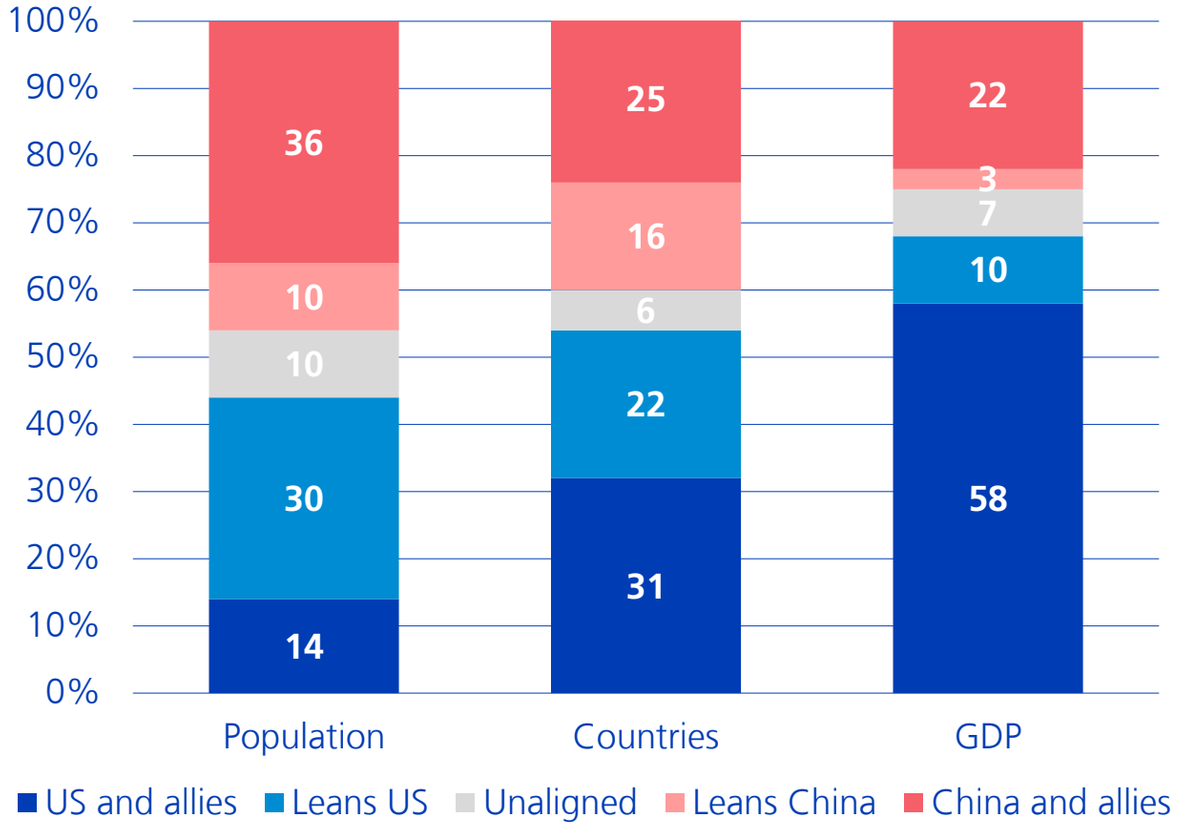
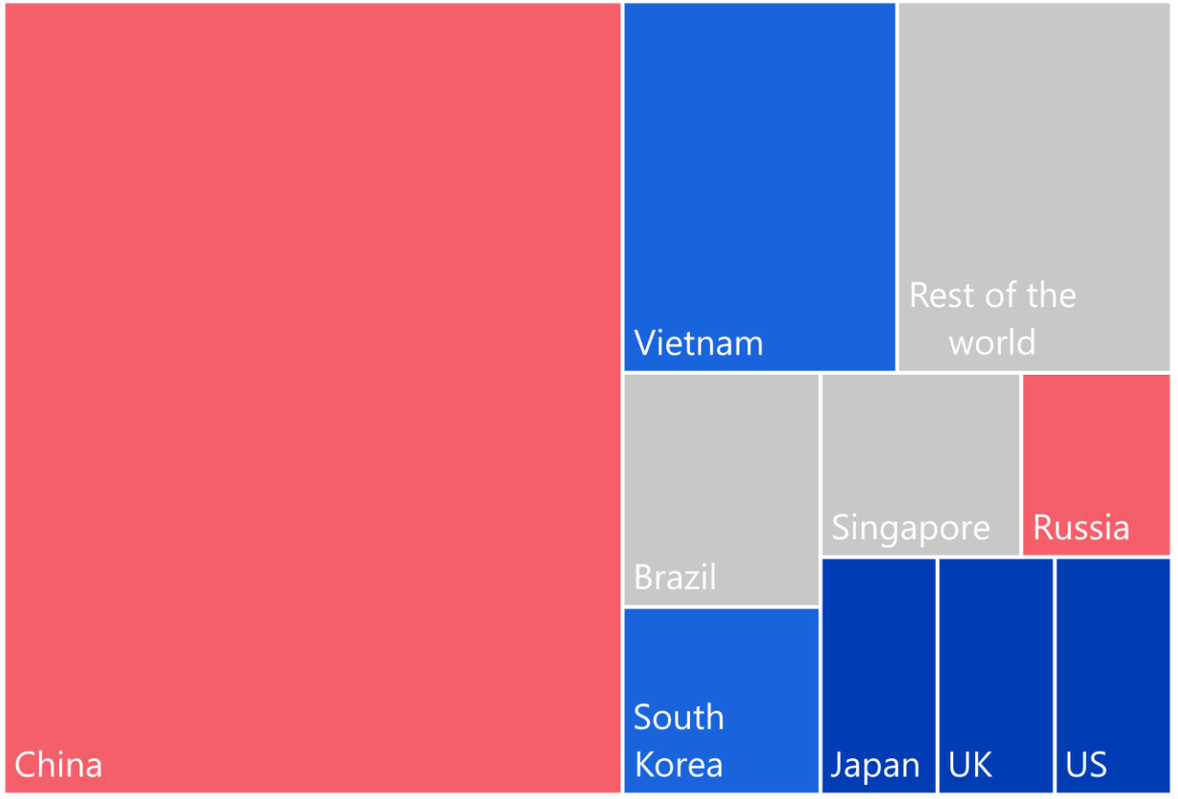
The two blocs are of similar size in terms of population

But the US bloc is far larger in terms of economic power



More than half of critical products in the EU are from China

Source of EU imports of critical products



Sources: Zürcher Kantonalbank, Capital Economics, European Commission

Energy transition: Balancing energy security, equity and sustainability is challenging, but possible

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Rank	Country	ETI score
(1)	Sweden	78.5
(2)	Denmark	76.1
(3)	Norway	73.7
(4)	Finland	72.8
(5)	Switzerland	72.4
(6)	Iceland	70.6
(7)	France	70.6
(8)	Austria	69.3
(9)	Netherlands	68.8
(10)	Estonia	68.2
(11)	Germany	67.5
(12)	United States	66.3
(13)	United Kingdom	66.2
(14)	Brazil	65.9
(16)	Spain	65.0
(17)	China	64.9

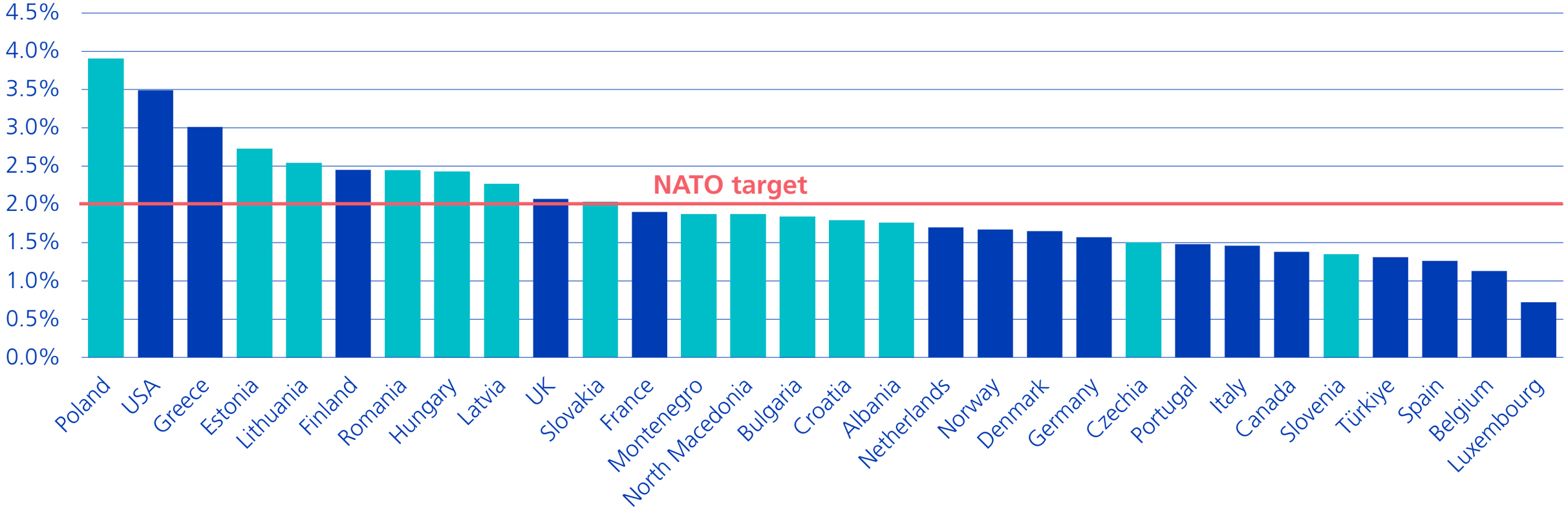
Rank	Country	ETI score
(18)	Hungary	64.3
(19)	Canada	64.2
(21)	Albania	63.7
(24)	Australia	63.6
(26)	Latvia	63.4
(27)	Japan	63.3
(29)	Slovenia	62.6
(33)	Croatia	62.0
(36)	Lithuania	61.2
(38)	Italy	60.6
(40)	Poland	59.7
(42)	Belgium	59.2
(44)	Slovakia	58.8
(45)	Czechia	58.6
(48)	Bulgaria	57.2
(49)	Romania	56.8

Sources: Zürcher Kantonalbank, Accenture, World Economic Forum

Defense: Central and Eastern Europe as a role model for the West

Most Central and Eastern Europe countries have done their homework

Defense expenditure as a share of GDP



Sources: Zürcher Kantonalbank, NATO

Defense: NATO Europe on course to meet 2% target in 2024

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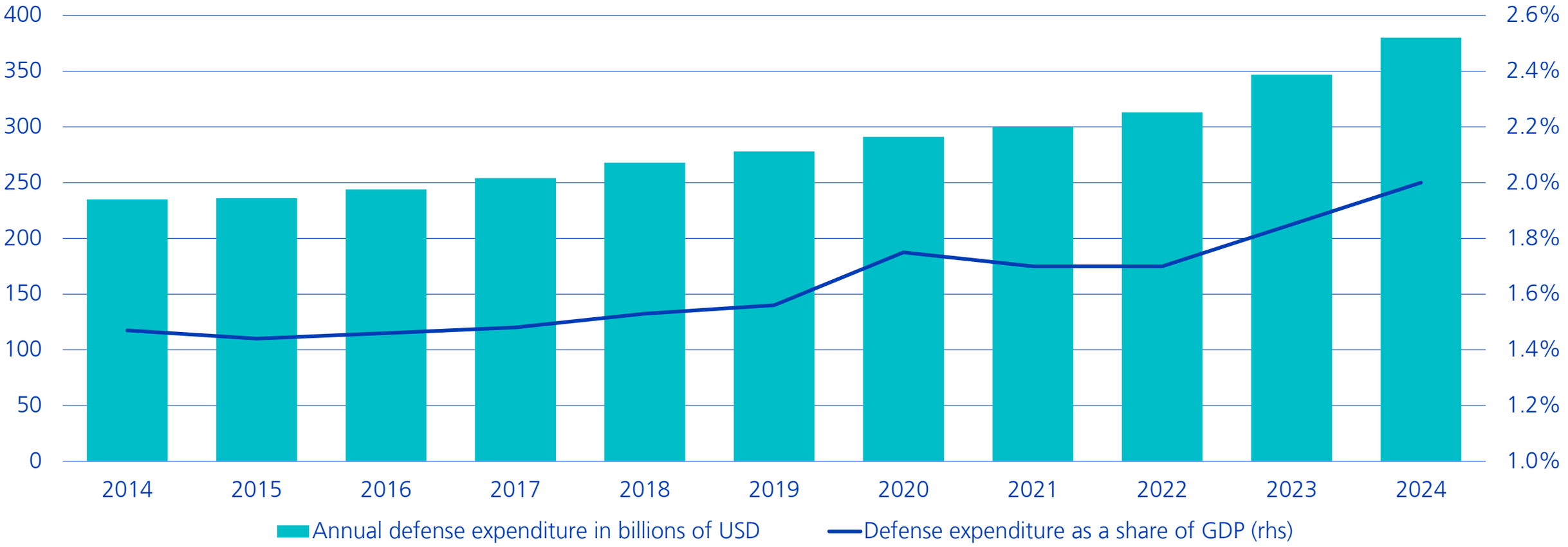
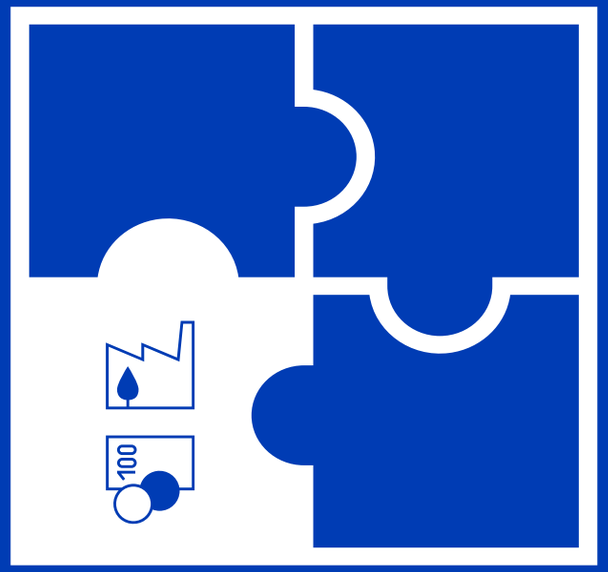
Defense expenditure is expected to rise sharply again this year

Defense expenditure of NATO Europe as a share of GDP



Sources: Zürcher Kantonalbank, NATO

Opportunities for investment



«NextGenerationEU»: 800 billion EUR of public investment are a unique opportunity for Europe

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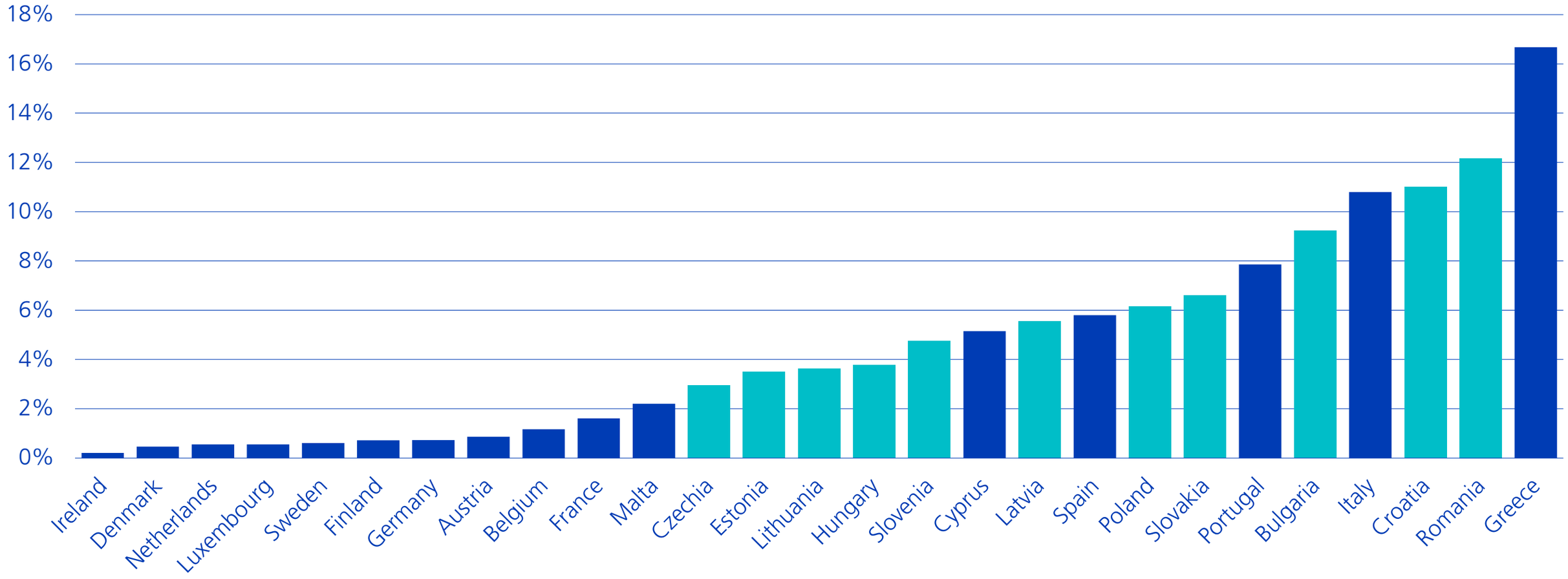
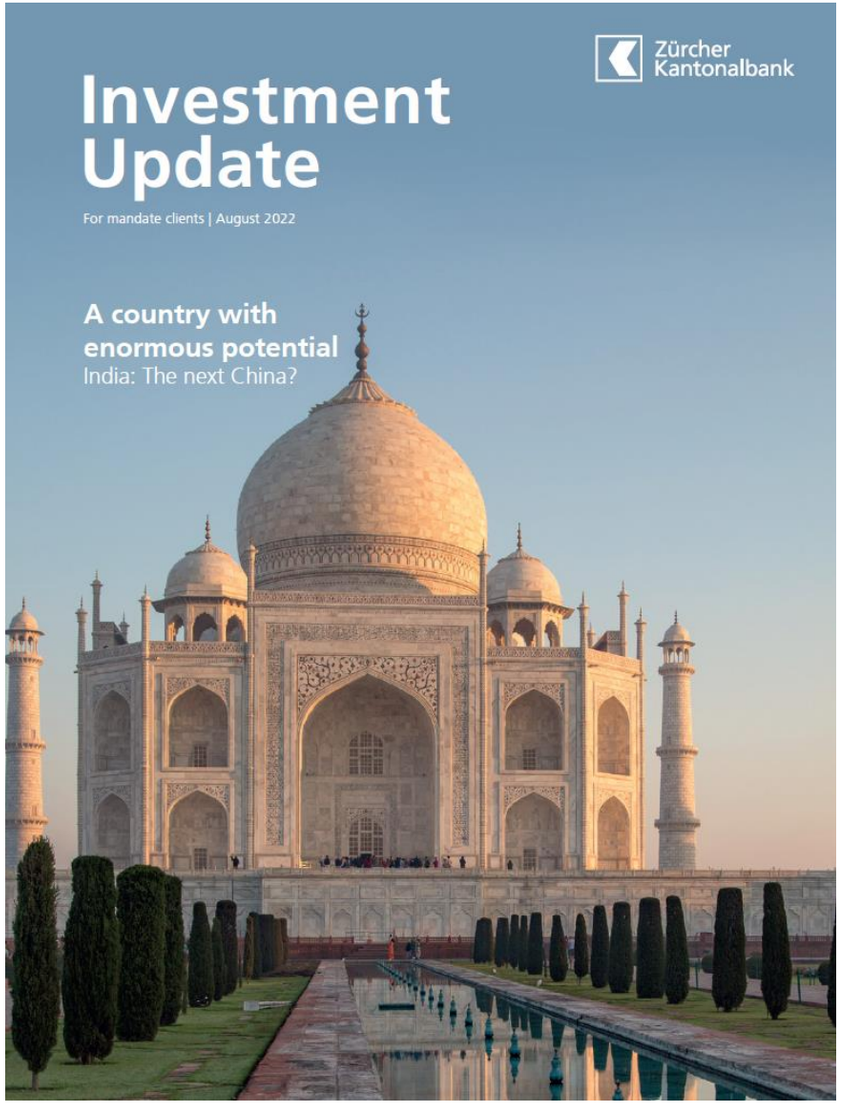
CEE countries benefit greatly from the EU recovery fund

EU Recovery Fund: Allocated funds as a percentage of GDP

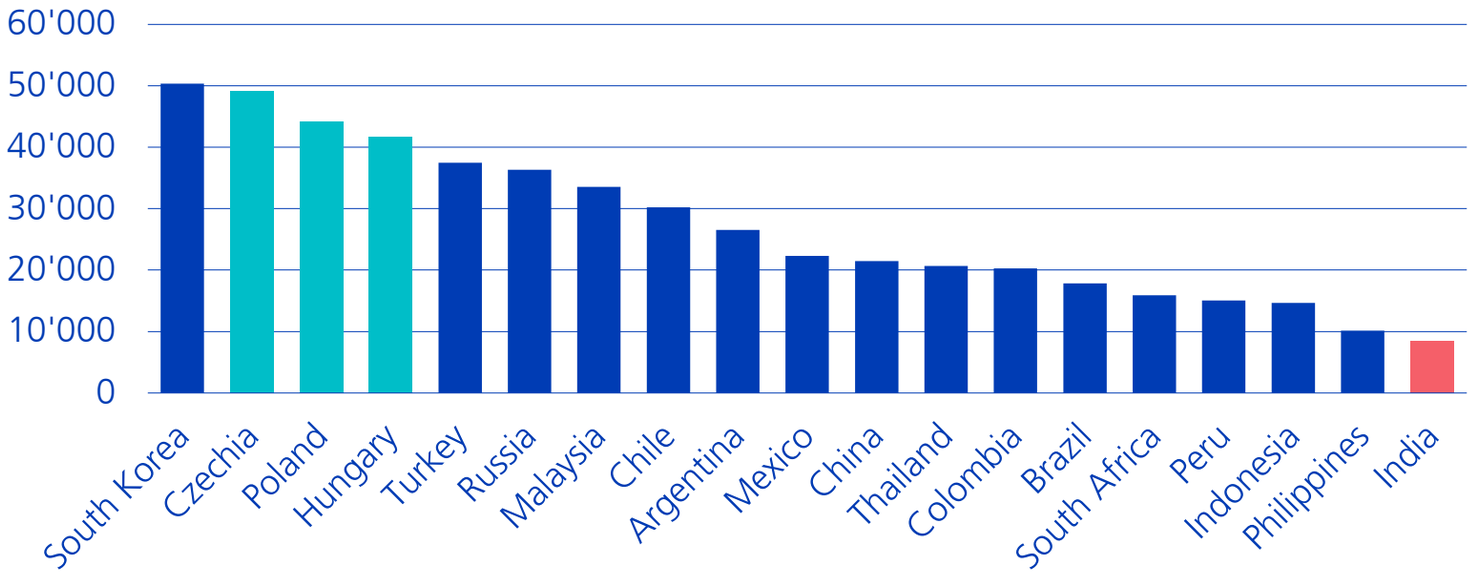


Sources: Zürcher Kantonalbank, European Commission

Is India the next China? The world's most populous country still has enormous upside potential



GDP per capita in USD (at PPP)



Key obstacles

- Lack of industrial know-how
- Excessive bureaucracy
- Heavily fragmented corporate landscape
- Inadequate infrastructure
- Land scarcity

Sources: Zürcher Kantonalbank, Refinitiv

Portfolio Investment: Emerging Markets constitute only a small share of equity and bond portfolios

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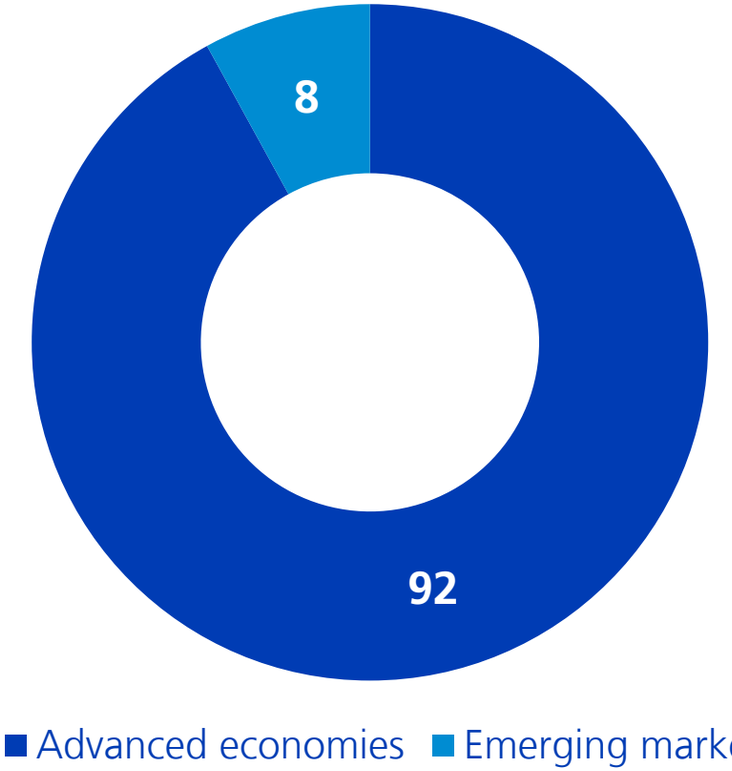
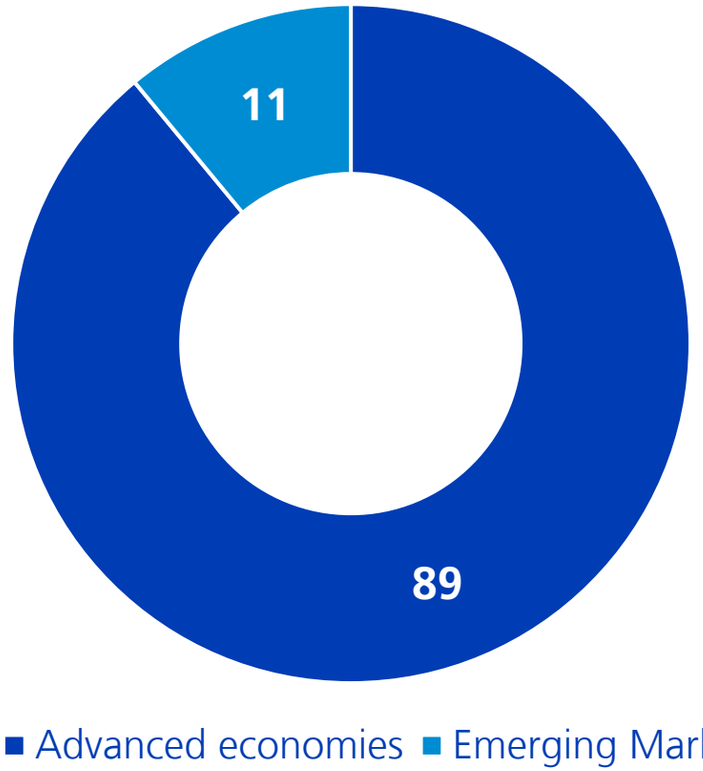
Equity investments are dominated by advanced economies



Bonds: Emerging Markets only play a small role



Sources: Zürcher Kantonalbank, MSCI, Refinitiv

Conclusion

Key take-aways: Central and Eastern Europe economies are well equipped to navigate cyclical and structural challenges

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Outlook	**Economic growth likely to remain low as interest rates stay elevated** **Inflation will continue to decline, but at a much slower pace**
Demographics	**Shortage of skilled workers will persist** **Education and innovation will become even more important**
Geopolitics	**Global economy is increasingly fractured – which will drive up prices** **CEE countries have made great progress in terms of energy transition**
Investment	**CEE countries are attractive for both real and financial investment**

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