Issue 23.33
11 September 2023

ECOWEEK

“The decline in the working-age population raises the risk that, through various channels, inflation would increase. This creates a necessity of supply-side oriented policies to mitigate this risk.”

ECONOMIC RESEARCH

BNP PARIBAS

The bank for a changing world

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GLOBAL: POPULATION AGEING, WAGE GROWTH AND INFLATION

There is broad agreement amongst researchers that population ageing has a detrimental impact on economic growth through a reduction in the working-age population. There is less agreement on the impact on inflation, which amongst other things is influenced by age-dependent spending and savings behaviour. Wage developments will play a key role. A shrinking labour force could create structural labour market bottlenecks in certain sectors, trigger a 'war for talent' and force companies to pay higher wages and raise their selling prices. This would spill over to the rest of the economy. It shows the importance of supply-side oriented policies aiming to raise potential GDP growth, thus avoiding that the central bank would be forced to address the inflation challenge through tighter monetary policy, which would lower realised growth.

There is broad agreement amongst researchers that population ageing has a detrimental impact on economic growth. Recent research shows that in the US, between 1980 and 2010, it has reduced the growth rate in GDP per capita by 0.3 percentage points per year[1]. It is to be expected that this trend will continue. An ECB paper quotes research by the European Commission, which concludes that in the Eurozone, "*population ageing is expected to have a dampening impact on potential growth*[2]." The Commission assumes that the decline in the working-age population (chart 1) "*will not be significantly counterbalanced by migration and a further rise in the labour force participation rate*", but it expects that total factor productivity will be the main driver of potential growth over the medium term[3]. There is less agreement on the impact of ageing on inflation, which depends amongst other things on what happens to spending versus production, considering the differences in spending and savings behaviour between various age groups[4]. Wage developments may also be an important factor: a shrinking labour force could create structural labour market bottlenecks, trigger a 'war for talent', increase employees' negotiating power, and force companies to pay higher wages and raise their selling prices. This is one out of many channels whereby population ageing can, through the labour market, influence inflation (exhibit 1).

For a detailed analysis of these drivers, we can first assume that the total working-age population remains constant. People who retire are replaced by young people that enter the labour market, by migration, by people who decide to work longer, by an increase in the participation rate. Under such a scenario, there could still be a negative impact on inflation because older people receive a higher wage so if an older cohort is replaced with a younger one, the average wage level would decline.

EURO AREA: PROPORTION OF POPULATION AGED 15-64 YEAR-OLD

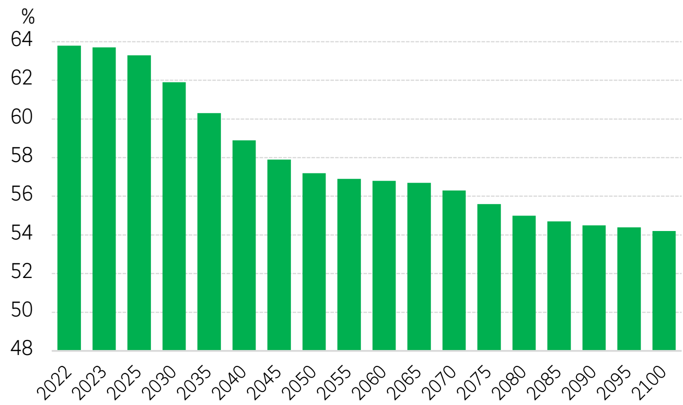


CHART 1 SOURCE: EUROPOP2023, EUROSTAT, BNP PARIBAS

This reduction in the cost base of companies could, through competitive pressure, cause a decline in selling prices. A potential increase in the productivity due to the changing age structure of the labour force, could also be disinflationary. On the other hand, wages increase faster for people early in their career, so this would limit the impact of the difference in wage levels[5]. Moreover, to the extent that older people work longer, the wage bill of companies would not decline.

1Source: Nicole Maestas, Kathleen J. Mullen, David Powell, *The Effect of Population Aging on Economic Growth, the Labor Force, and Productivity*, American Economic Journal: Macroeconomics, April 2023.
2Source: *The macroeconomic and fiscal impact of population ageing*, ECB Occasional Paper 296, June 2022.
3There is disagreement on the impact of an ageing workforce on productivity. The research mentioned in footnote 1 finds a negative effect in the US.
4 At the risk of oversimplifying, younger generations save in order to accumulate sufficient financial wealth by the time they retire whereas retired people have a low or even negative savings rate.
5Changes in the age structure of employment can therefore have substantial effects on wage growth. The main channel for such effects seems to be the different wage levels, given that the average hourly wage of an employee who is 60 or older is more than 50% higher than that of an employee under 30. The fact that wage growth tends to decrease with age works in the opposite direction. However, this effect tends to be more gradual and is therefore often less important – especially in times of large cyclical fluctuations in participation

The decline in the working-age population raises the risk that, through various channels, inflation would increase. This creates a necessity of supply-side oriented policies to mitigate this risk.

EDITORIAL

A more realistic assumption is that the working-age population declines, causing structural labour market bottlenecks in many if not most sectors. This would put upward pressure on wages as companies seek to poach staff from competitors or from other sectors where employees have similar skillsets. This way, upward wage pressure due to bottlenecks in one sector would spill over to other sectors, although the latter may not suffer from similar bottlenecks. A higher wage bill would force companies to increase their selling prices -if the competitive environment allows them to do so-, thereby creating another spillover channel to the rest of the economy. How about the possibility that in certain sectors, the opposite would occur, and that available labour would be in excess supply? Could this be a counterbalancing force in terms of inflation?

This is very unlikely due to the downward rigidity of nominal wages. Moreover, the question seems rather theoretical: anecdotal evidence shows that already today, shortages are widespread.

To conclude, the decline in the working-age population can, through various channels, put upward pressure on inflation. The fact that different channels exist increases the risk that this theoretical possibility becomes reality, hence the necessity of supply-side oriented policies to mitigate this risk: improving the matching of skills -those required by companies versus those offered by job seekers-, increasing the participation rate, providing incentives for working longer, a policy towards skilled migration, boosting productivity. This would not only raise potential growth but it would also avoid that the central bank would be forced to address the inflation challenge through tighter monetary policy, which would lower realised growth.

William De Vijlder

AGE AND WAGE GROWTH

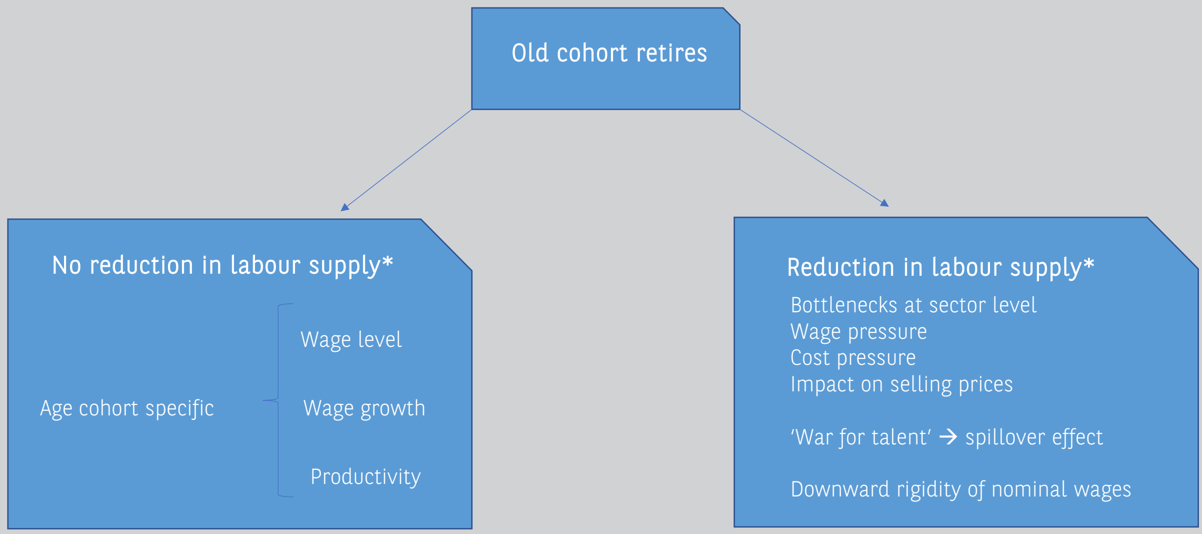


FIGURE 1

* Taking into account migration and change in labour force participation rate

SOURCE: BNP PARIBAS

MARKETS OVERVIEW

OVERVIEW

Week 1-9 23 to 8-9-23					
↘ CAC 40	7 297	▸	7 241	-0.8	%
↘ S&P 500	4 516	▸	4 457	-1.3	%
↗ Volatility (VIX)	13.1	▸	13.8	+0.8	pb
↗ Euribor 3M (%)	3.77	▸	3.80	+3.0	bp
↗ Libor $ 3M (%)	5.66	▸	5.67	+0.8	bp
↗ OAT 10y (%)	3.02	▸	3.10	+7.7	bp
↗ Bund 10y (%)	2.51	▸	2.57	+5.9	bp
↗ US Tr. 10y (%)	4.19	▸	4.26	+7.1	bp
↘ Euro vs dollar	1.08	▸	1.07	-0.9	%
↘ Gold (ounce, $)	1 939	▸	1 922	-0.9	%
↗ Oil (Brent, $)	88.6	▸	90.7	+2.3	%

MONEY & BOND MARKETS

Interest Rates		highest 23			lowest 23		
€ ECB	4.25	4.25	at	02/08	2.50	at	02/01
Eonia	-0.51	-0.51	at	02/01	-0.51	at	02/01
Euribor 3M	3.80	3.83	at	23/08	2.16	at	02/01
Euribor 12M	4.09	4.19	at	07/07	3.30	at	19/01
$ FED	5.50	5.50	at	27/07	4.50	at	02/01
Libor 3M	5.67	5.68	at	29/08	4.77	at	02/01
Libor 12M	6.04	6.04	at	30/06	4.70	at	20/03
£ BoE	5.25	5.25	at	03/08	3.50	at	02/01
Libor 3M	5.56	5.60	at	30/08	3.87	at	02/01
Libor 12M	0.81	0.81	at	02/01	0.81	at	02/01

At 8-9-23

Yield (%)		highest 23			lowest 23		
€ AVG 5-7y	2.64	2.64	at	02/01	2.64	at	02/01
Bund 2y	3.16	3.36	at	08/03	2.39	at	20/03
Bund 10y	2.57	2.75	at	02/03	1.98	at	18/01
OAT 10y	3.10	3.23	at	03/03	2.42	at	18/01
Corp. BBB	4.63	4.77	at	10/07	3.95	at	02/02
$ Treas. 2y	5.03	5.16	at	25/08	3.85	at	04/05
Treas. 10y	4.26	4.35	at	21/08	3.30	at	06/04
High Yield	8.68	9.16	at	20/03	7.94	at	02/02
£ gilt. 2y	4.79	5.51	at	06/07	3.15	at	02/02
gilt. 10y	4.42	4.74	at	17/08	3.00	at	02/02

At 8-9-23

EXCHANGE RATES

1€ =		highest 23			lowest 23			2023
USD	1.07	1.12	at	14/07	1.05	at	05/01	+0.4%
GBP	0.86	0.90	at	03/02	0.85	at	11/07	-3.3%
CHF	0.96	1.00	at	24/01	0.95	at	05/09	-3.2%
JPY	158.22	159.39	at	30/08	138.02	at	03/01	+12.4%
AUD	1.68	1.70	at	21/08	1.53	at	27/01	+6.5%
CNY	7.87	8.08	at	19/07	7.23	at	05/01	+6.1%
BRL	5.35	5.79	at	04/01	5.20	at	23/06	-5.1%
RUB	105.14	110.46	at	14/08	73.32	at	12/01	+35.0%
INR	88.88	92.37	at	14/07	86.58	at	08/03	+0.7%

At 8-9-23 *Change*

COMMODITIES

Spot price, $		highest 23			lowest 23			2023	2023(€)
Oil, Brent	90.7	90.7	at	08/09	71.9	at	12/06	+6.8%	+6.4%
Gold (ounce)	1 922	2 047	at	04/05	1 810	at	24/02	+5.9%	+5.4%
Metals, LMEX	3 664	4 404	at	26/01	3 564	at	24/05	-8.0%	-8.4%
Copper (ton)	8 229	9 331	at	23/01	7 852	at	24/05	-1.6%	-2.0%
wheat (ton)	192	2.9	at	13/02	190	at	01/09	-32.8%	-33.1%
Corn (ton)	181	2.7	at	13/02	161	at	21/08	-3.0%	-30.5%

At 8-9-23 *Change*

EQUITY INDICES

	Index	highest 23			lowest 23			2023
World								
MSCI World	2 949	3 064	at	31/07	2 595	at	05/01	+13.3%
North America								
S&P500	4 457	4 589	at	31/07	3 808	at	05/01	+16.1%
Europe								
EuroStoxx50	4 237	4 471	at	31/07	3 856	at	02/01	+11.7%
CAC 40	7 241	7 577	at	21/04	6 595	at	02/01	+1.2%
DAX 30	15 740	16 470	at	28/07	14 069	at	02/01	+13.0%
IBEX 35	9 365	9 695	at	27/07	8 370	at	02/01	+1.4%
FTSE100	7 478	8 014	at	20/02	7 257	at	07/07	+0.0%
Asia								
MSCI, loc.	1 225	1 246	at	01/08	1 065	at	04/01	+1.5%
Nikkei	32 607	33 753	at	03/07	25 717	at	04/01	+25.0%
Emerging								
MSCI Emerging ($)	974	1 052	at	26/01	941	at	16/03	+0.2%
China	59	75	at	27/01	57	at	21/08	-5.9%
India	835	835	at	20/07	703	at	16/03	+8.6%
Brazil	1 540	1 733	at	26/07	1 296	at	23/03	-0.2%

At 8-9-23 *Change*

PERFORMANCE BY SECTOR (Eurostoxx50 & S&P500)

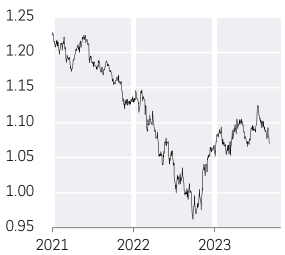
Year 2023 to 8-9, €	
+24.5%	Retail
+18.5%	Travel & leisure
+17.7%	Technology
+13.6%	Construction
+13.2%	Car
+12.7%	Media
+11.6%	Consumption Goods
+10.2%	Industry
+9.1%	Banks
+8.5%	Health
+7.0%	Index
+5.4%	Chemical
+3.0%	Utilities
+2.9%	Oil & Gas
+2.8%	Telecoms
+2.0%	Insurance
-3.7%	Food industry
-4.6%	Real Estate
-16.6%	Commodities

Year 2023 to 8-9, $	
+64.2%	Car
+47.3%	Technology
+24.8%	Retail
+22.7%	Travel & leisure
+21.8%	Construction
+15.6%	Index
+10.6%	Media
+9.8%	Financial services
+7.1%	Insurance
+6.3%	Industry
+3.9%	Oil & Gas
+3.7%	Chemical
+2.6%	Commodities
-0.2%	Household & Care
-3.4%	Health
-5.3%	Food industry
-11.6%	Banks
-11.7%	Utilities
-15.3%	Telecoms

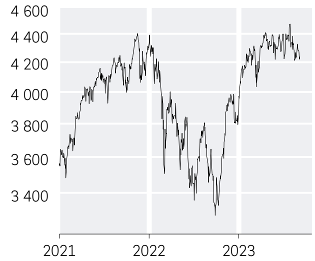
SOURCE: REFINITIV, BNP PARIBAS

MARKETS OVERVIEW

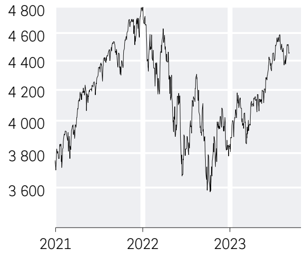
EURO-DOLLAR



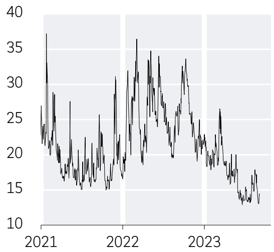
EUROSTOXX50



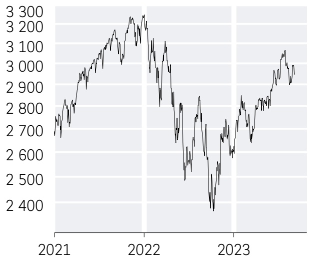
S&P500



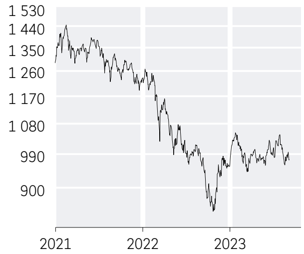
VOLATILITY (VIX, S&P500)



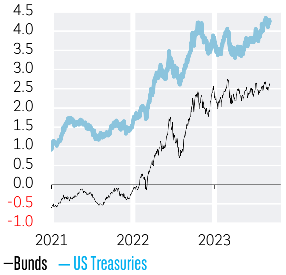
MSCI WORLD (USD)



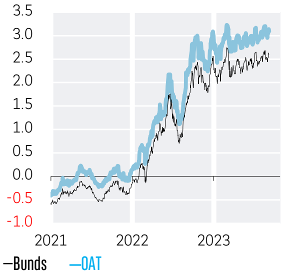
MSCI EMERGING (USD)



10Y BOND YIELD, TREASURIES VS BUND



10Y BOND YIELD

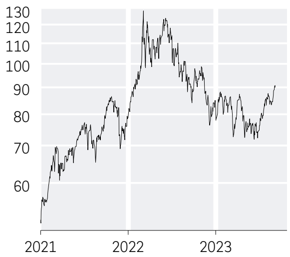


10Y BOND YIELD & SPREADS

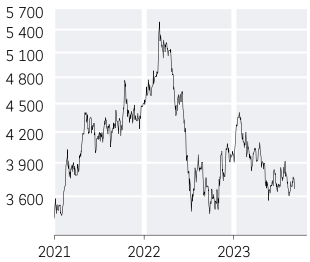
Year 2023 to 8-9

5.20%	Greece	262 bp
4.22%	Italy	164 bp
3.59%	Spain	101 bp
3.25%	Belgium	67 bp
3.24%	Portugal	66 bp
3.19%	Austria	61 bp
3.12%	Finland	54 bp
3.10%	France	52 bp
2.97%	Ireland	40 bp
2.94%	Netherlands	36 bp
2.57%	Germany	

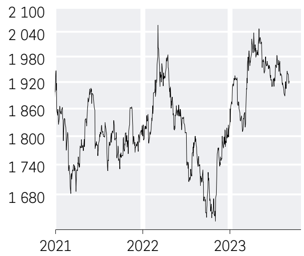
OIL (BRENT, USD)



METALS (LMEX, USD)



GOLD (OUNCE, USD)



SOURCE: REFINITIV, BNP PARIBAS

ECONOMIC PULSE

PMI SERVICES AND MANUFACTURING: THE GAP NARROWED CONSIDERABLY

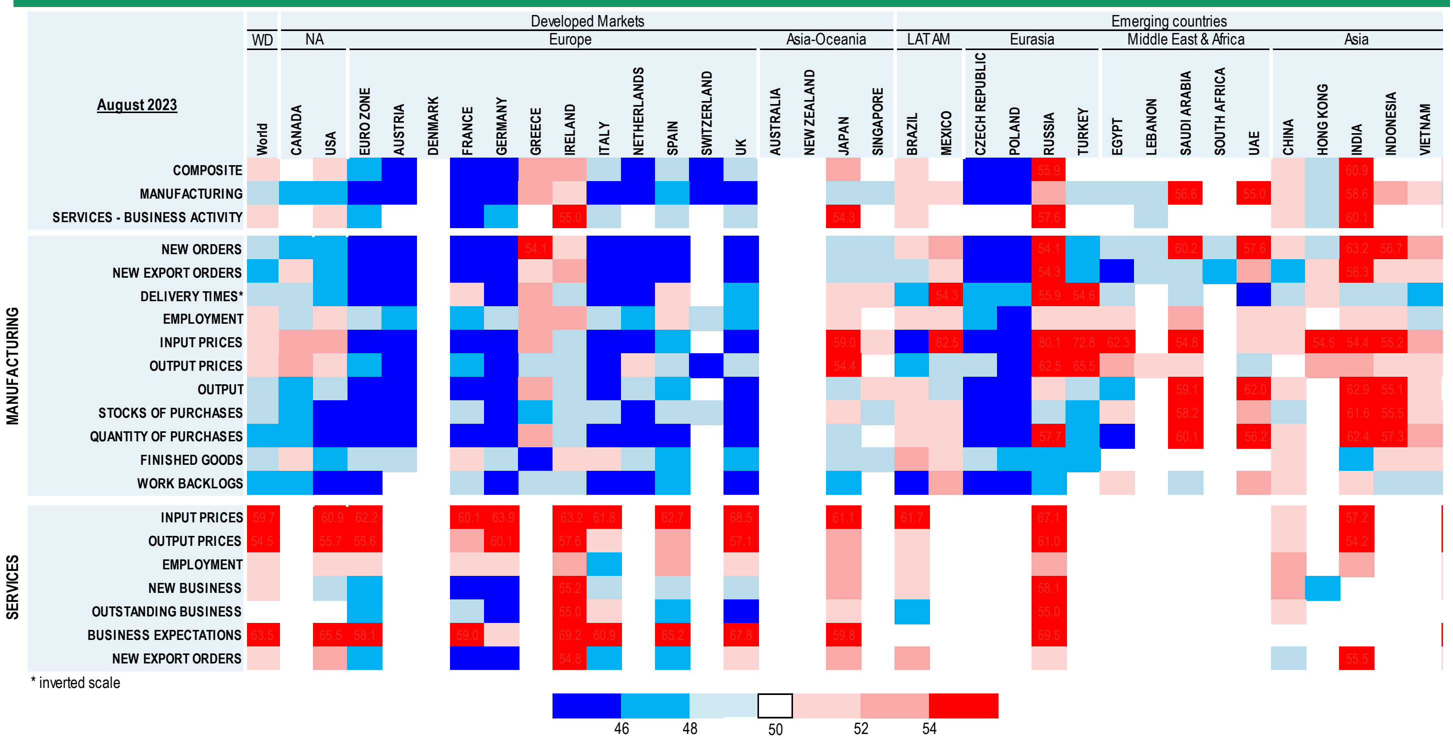
According to its final estimate, the S&P Global composite PMI index fell for the seventh month in a row in August, illustrating the loss of momentum in global growth in the middle of the 3rd quarter. The negative signal is reinforced by the level of the index, which reached just 50 (from 51.6 in July), the threshold between expansion and contraction. The good news of the modest increase in the manufacturing PMI (49 compared to 48.6 in July) – the first since May 2023 – is offset by the continued deterioration of the services PMI, for the seventh consecutive month (51.1 compared to 52.7 in July). The decoupling of the business climate between the two sectors is disappearing.

The deterioration in the services sector is widespread. Five of the six components covered by the survey fell: new business, new export orders, input prices, employment and output prices. Eleven of the 16 countries for which August data are available reported a decrease in the index compared to the previous month. This decline is marked in the euro area, driven down by Germany and Spain, to the point of sliding into contraction territory, for the first time since last December. The index also worsened in the United States, the United Kingdom and China. China's index is now at the lowest level since last December, when lockdown measures against Covid-19 were still in place.

The global manufacturing PMI index, while recovering slightly in August, remains in contraction territory for the twelfth month in a row, reflecting the difficult global economic conditions. In detail, the sub-indices of new orders, output, new export orders and quantity of purchases increased slightly but remained below 50. The employment sub-index rose (50.6 compared to 50.1 in July), but this good news is offset by the rise in input (51.1 compared to 49.3) and output prices (50.5 compared to 49.7), after three months of decline. The eurozone index rebounded, wiping out its July decline, but it remains well in contraction territory, almost 7 points below the 50-point mark. The manufacturing PMI also rose in the Asian countries covered by the survey. Conversely, the United States, Canada, and the United Kingdom saw their index fall due to a decline in new orders and output. In Japan, the index remained stable.

Tarik Rharrab

S&P GLOBAL PMI (AUGUST 2023)



SOURCE: S&P GLOBAL, BNP PARIBAS

ECONOMIC PULSE

S&P GLOBAL PMI (AUGUST VERSUS JULY)

			Developed Markets																		Emerging countries															
		WD	NA		Europe												Asia-Oceania				LAT AM		Eurasia				Middle East & Africa					Asia				
		World	CANADA	USA	EURO ZONE	AUSTRIA	DENMARK	FRANCE	GERMANY	GREECE	IRELAND	ITALY	NETHERLANDS	SPAIN	SWITZERLAND	UK	AUSTRALIA	NEW ZEALAND	JAPAN	SINGAPORE	BRAZIL	MEXICO	CZECH REPUBLIC	POLAND	RUSSIA	TURKEY	EGYPT	LEBANON	SAUDI ARABIA	SOUTH AFRICA	UAE	CHINA	HONG KONG	INDIA	INDONESIA	VIETNAM
	COMPOSITE	-1.0		-1.8	-1.9			-0.6	-3.9		2.6	-0.7		-3.1		-2.2			0.4		1.0				2.6							-0.2	0.0	-1.0		
	MANUFACTURING	0.4	-1.6	-1.1	0.8	1.8		0.9	0.3	-0.6	3.8	0.9	0.6	-1.3	1.4	-2.3			0.0	0.1	2.3	-2.0		-0.4	0.6	-0.9	0.0	-1.6	-1.1		-1.0	1.8	0.4	0.9	0.6	1.8
	SERVICES - BUSINESS ACTIVITY	-1.6		-1.8	-3.0			-1.1	-5.0		-1.7	-1.7		-3.5		-2.0			0.5		0.4				3.6			-1.6				-2.3	0.4	-2.2		
MANUFACTURING	NEW ORDERS	0.5	-1.5	-1.3	0.0	-0.4		-0.5	-0.2	-0.8	3.4	0.6	0.6	-4.7		-4.3			0.4	0.1	2.6	-1.9	1.1	-1.0	1.8	-2.1	-0.3	-1.5	-2.9	2.4	0.2	2.8	-0.6	1.6	1.7	2.7
	NEW EXPORT ORDERS	0.6	0.4	-1.8	1.1	-2.5		1.1	2.9	-0.4	4.3	-3.6	0.7	-0.1		-2.7			1.0	0.1	0.6	-2.4	4.1	2.3	7.0	-2.1	-1.2	-1.5	-11	-4.1	2.9	1.9	-1.0	0.4	0.5	4.9
	DELIVERY TIMES	-0.7	0.1	-1.7	-3.1	-3.1		-4.4	-4.1	-0.3	0.2	-2.0	-4.2	-1.5		-0.5			-0.8	-0.1	-1.0	2.6	-3.8	0.3	-1.3	0.7	0.6		-6.9		4.7	0.7	0.8	-0.4	0.3	-1.2
	EMPLOYMENT	0.5	-0.2	-1.6	0.2	0.5		-0.3	0.3	-1.4	2.1	-1.0	-1.4	1.0	-0.6	0.4			-0.9		1.6	-0.4	1.0	-0.2	-2.1	-0.8	0.8		1.3		0.1	2.8		-0.8	0.7	1.1
	INPUT PRICES	1.8	2.3	1.3	3.9	3.1		0.1	4.7	6.6	2.3	3.5	5.9	8.9		-1.8			1.4		6.7	3.3	4.6	2.4	4.1	-1.8	3.7		2.6		0.9	1.5	-0.6	0.7	-0.3	4.6
	OUTPUT PRICES	0.8	1.5	1.3	1.1	3.3		-0.4	0.7	-0.1	0.1	2.0	3.7	3.0	2.1	-0.5			-0.8		2.3	0.5	1.1	1.6	2.0	-3.1	1.7	-0.4	0.9		0.3		-0.5	-0.6	-0.1	5.3
	OUTPUT	0.5	-3.4	-1.7	0.8	3.9		1.9	-1.6	-0.6	7.7	2.1	0.6	-1.5		-3.1			0.0	0.2	3.1	-2.2	0.9	-0.4	-0.4	-0.7	-1.0		-6.9		-0.8	2.4		1.8	0.2	2.3
	STOCKS OF PURCHASES	-0.8	-2.9	-2.4	0.9	3.8		-0.3	0.6	-0.3	4.0	0.1	-0.7	1.1	-2.0	-3.3			-0.7	0.3	2.4	-4.0	1.4	0.3	3.7	1.8	1.7		1.2		-1.9	-1.0		0.8	-0.1	0.4
	QUANTITY OF PURCHASES	0.4		-0.1	0.5	3.5		-1.5	-0.1	-0.9	6.9	-0.3	1.8	-2.0		-2.8			0.3		2.6	-2.1	-0.2	-0.4	1.8	-2.8	-5.3		-2.0		1.9	1.7		1.0	0.7	4.3
	FINISHED GOODS	0.2	0.6	1.6	0.4	-3.0		2.9	-0.4	-1.4	1.1	0.8	4.0	-1.8		-1.7			-1.4	0.1	2.2	-0.2	1.2	-0.5	-1.1	0.8						0.1		-1.5	0.7	-0.6
	WORK BACKLOGS	0.1	-0.1	0.3	1.1			2.1	2.0	-4.2	-0.4	0.7	-0.3	1.2		-3.7			-0.5		-0.1	-2.9	-2.0	2.3	-0.7		0.8		-0.8		-3.2	0.4		-0.7	-1.1	1.4
SERVICES	INPUT PRICES	-0.5		-2.3	0.9			-0.4	0.9		-1.5	3.8		0.3		0.1			3.2		-2.1				7.1							-0.9		2.4		
	OUTPUT PRICES	-0.6		-0.9	-0.6			-1.3	0.0		1.3			-0.8		-2.3			0.0		-0.7				0.6							-0.4		0.6		
	EMPLOYMENT	-0.1		-0.6	-1.7			-1.8	-1.6		0.8	-2.4		-1.3		-1.2			2.8		0.5				4.1							-0.1		1.3		
	NEW BUSINESS	-1.0		-2.2	-1.5			-1.7	-0.6		-2.4	-2.2		-1.9		-1.5			1.7		0.5				4.7							-0.6	-4.9			
	OUTSTANDING BUSINESS				-1.1			-2.4	-1.7		0.8	2.4		-2.6		-2.8			0.8		-0.4				5.4							0.2				
	BUSINESS EXPECTATIONS	1.2		1.6	0.0			-1.3	2.0		0.2	-2.5		1.0		-0.1			0.9						6.6											
	NEW EXPORT ORDERS	-1.4		-2.1	-0.3			-0.1	2.0		-0.5	-2.5		-3.6		-0.7			-0.5		1.8				1.5							-1.8		1.0		

-3	-2	-1		0	1	2	3	

SOURCE: S&P GLOBAL, BNP PARIBAS

ECONOMIC SCENARIO

UNITED STATES

After a strong second half of 2022 (+0.7% q/q on average per quarter), US activity decelerated only slightly in the first half of 2023 (+0.5% q/q on average per quarter), thanks to the resilience of household consumption and the strength of nonresidential investment. The impact of the tighter monetary policy on lending standards is strong but it still limited on activity and employment growth. Q3 GDP growth is expected to be very positive again before a sharp slowdown in Q4 and to slide into recession in the first half of 2024. While the peak in inflation was reached in mid-2022, core disinflation remains gradual. Headline inflation should approach the 2% target in 2024. However, the slow pace of disinflation argues in favor of keeping monetary policy in restrictive territory, despite the expected start of the easing cycle in Q2 2024. This should limit the recovery in 2024.

CHINA

Economic growth, which was sluggish and unbalanced in 2022, started to accelerate in early 2023 following the end of the zero Covid policy. However, the post-Covid recovery has lost momentum very rapidly. Export momentum has stalled due to weak global demand and tensions with the US. Domestic demand remains held back by a significant loss in consumer and investor confidence. The crisis in the property sector is persisting, with the continued fall in sales, new defaults of developers and growing difficulties of certain financial institutions. The government and the central bank implement new policy stimulus measures, which yet remain of moderate magnitude. The weak financial situation of local governments should constrain public investment.

EUROZONE

After a slight contraction in GDP in Q4 2022, the euro area returned to slightly positive growth in the first half of 2023. According to the latest figures available, Q1 growth was again revised up (from -0.1% to 0.0% and now to +0.1% q/q), but Q2 growth was downwardly revised to +0.1% q/q, erasing the initially reported technical rebound of +0.3% q/q. The disparate performance between Member States further weakens the overall result. . France and Spain have been doing well, but Germany, Italy and the Netherlands are struggling. The negative effects of monetary tightening should intensify and further slow economic activity, which would stagnate in the second half of 2023, before starting a sluggish recovery. Although it is expected to decline throughout 2023, inflation would remain elevated, slightly exceeding 3% y/y at the end of this year. Illustrating the slowness of the disinflation process, it would still be significantly above the 2% target at the end of 2024 (2.5% y/y), forcing monetary policy to remain in restrictive territory.

FRANCE

French growth significantly surprised on the upside in Q2 2023, with activity accelerating more than expected (+0.5% q/q, after stagnation in Q1 and a modestly positive Q4 2022). While household consumption and investment remain depressed, this rebound has been supported by business investment and, above all, exports. A negative correction is likely in Q3. Inflation rebounded in August (5.7% y/y according to the harmonized measure), driven by energy prices, but which does not call into question its slow downward trajectory. Because of rising interest rates, household demand should remain subdued in 2023, weighing on our GDP growth forecast (0.7% in 2023, compared to 2.5% in 2022).

RATES AND EXCHANGE RATES

In the US, after having skipped the June meeting, the Federal Reserve proceeded, as expected, to a further 25bp rate hike in July. This increase would be the last in our view, but uncertainty remains given the still elevated core inflation and the resilience of activity and the labour market to date. In any case, these factors argue against a rate cut before the beginning of 2024. The residual uncertainty on the policy rate peak is reflected in long-term rates, which remained on an upward trend early September. However, as inflation falls further and the prospect of monetary easing in 2024 rises, long-term rates should resume their decline soon.

Unlike the Fed, the ECB did not pause in June but, like the Fed, it increased its key rates by 25bp in July (deposit rate at 3.75%, refinancing rate at 4.25%). We are of the view that this increase would mark the end of the ECB's tightening cycle, considering the effects of the monetary tightening already underway. But it is not yet certain that it will be the last, given the absence of a tangible fall at this stage of core inflation.

As part of its monetary tightening, the ECB also announced a complete halt, starting in July 2023, of its reinvestments under the APP. European long-term rates are trending up, moving in line with US rates, but in a more muted way. They are expected to ease gradually as the fall in core inflation should become more visible, dissipating uncertainty over the continuation of monetary tightening.

On 27 July, the Bank of Japan (BoJ) adjusted its yield curve control policy (YCC) by allowing a wider fluctuation in 10-year sovereign interest rates around the target of 0.5%Further adjustments to the YCC cannot be excluded, given that the country currently faces the fastest rate of inflation since the early 1990s. Nevertheless, the BoJ is unlikely to increase its policy rates this year, but a rise is expected in 2024.

We expect the dollar to weaken somewhat versus the euro. The dollar's valuation is expensive and next year the Federal Reserve should ease earlier and more than the ECB. We expect the yen to remain around current levels in the near term before strengthening versus the dollar based on the expected monetary divergence between the Fed and the BoJ in 2024.

GDP GROWTH AND INFLATION

	GDP Growth				Inflation			
%	2021	2022	2023 e	2024 e	2021	2022	2023 e	2024 e
United-States	5.9	2.1	2.1	0.3	4.7	8.0	4.0	2.1
Japan	2.2	1.0	2.0	1.0	-0.2	2.5	3.2	2.3
United-Kingdom	7.6	4.1	0.5	0.1	2.6	9.0	7.6	3.1
Euro Area	5.3	3.4	0.5	0.9	2.6	8.4	5.6	2.9
Germany	2.6	1.9	-0.3	0.3	3.2	8.6	6.2	3.0
France	6.8	2.5	0.7	0.5	2.1	5.9	5.7	2.7
Italy	7.0	3.8	0.9	1.1	1.9	8.7	6.0	2.0
Spain	5.5	5.5	2.2	1.5	3.0	8.3	3.6	3.2
China	8.4	3.0	5.1	4.5	0.9	2.0	0.5	2.0
India*	8.7	7.3	6.1	6.0	5.5	6.7	5.9	5.0
Brazil	5.0	2.9	3.1	1.8	8.3	9.3	4.7	4.2

Source : BNP Paribas (e: Estimates & forecasts)
Last update: 5 September 2023
* Fiscal year from 1st April of year n to March 31st of year n+1

INTEREST AND EXCHANGE RATES

Interest rates, % End of period		Q4 2023	Q1 2024	Q2 2024	Q3 2024	Q4 2024
US	Fed Funds (upper limit)	5.50	5.50	5.25	4.75	4.25
	T-Note 10y	4.20	4.05	3.95	3.90	3.90
Eurozone	deposit rate	3.75	3.75	3.75	3.50	3.25
	Bund 10y	2.60	2.45	2.40	2.30	2.35
	OAT 10y	3.17	2.99	2.93	2.85	2.92
	BTP 10y	4.50	4.25	4.10	4.10	4.25
	BONO 10y	3.70	3.45	3.35	3.30	3.40
UK	Base rate	5.50	5.50	5.00	4.50	4.00
	Gilts 10y	4.00	3.80	3.60	3.65	3.70
Japan	BoJ Rate	-0.10	-0.10	0.10	0.10	0.25
	JGB 10y	0.75	0.85	0.90	0.90	1.00

Exchange Rates End of period		Q4 2023	Q1 2024	Q2 2024	Q3 2024	Q4 2024
USD	EUR / USD	1.10	1.11	1.12	1.13	1.15
	USD / JPY	145	145	140	138	135
	GBP / USD	1.29	1.29	1.29	1.30	1.32
EUR	EUR / GBP	0.85	0.86	0.87	0.87	0.87
	EUR / JPY	160	161	157	156	155

Brent End of period		Q4 2023	Q1 2024	Q2 2024	Q3 2024	Q4 2024
Brent	USD/bbl	81	82	86	88	86

Sources: BNP Paribas (Market Economics, Interest Rate Strategy, FX Strategy, Commodities Desk Strategy)
Last update: 5 September 2023

FURTHER READING

Economic forecasting in a world without stylised facts	EcoTVWeek	8 September 2023
Inflation tracker of September 2023	EcoCharts	8 September 2023
The European Union's response to climate and industrial challenges	Chart of the Week	6 September 2023
From inflation to growth: the migration of uncertainty	EcoWeek	4 September 2023
Jackson Hole 2023: the fight against inflation is not over	EcoTV Week	1 September 2023
France: August's inflation figure reminds us that disinflation will remain gradual	EcoBrief	31 August 2023
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Eurozone: Inflation through the lens of business surveys. The case of services.	EcoWeek	24 July 2023
OECD: Economic pulse of June 2023	EcoPulse	24 July 2023
The Caribbean: Trouble in Paradise	EcoTVWeek	21 July 2023
United States: Money market funds reallocate their assets outside the ON RRP facility	Chart of the Week	19 July 2023
Eurozone: Inflation through the lens of business surveys - The case of industry	EcoWeek	18 July 2023
Is Chili a leader in energy transition?	EcoTVWeek	13 July 2023
Transport, France's main source of greenhouse gases emissions	Chart of the Week	12 July 2023
Eurozone: "have money, will travel"	EcoWeek	10 July 2023
Japan: After Price Inflation, Time for Wages?	EcoBrief	7 July 2023

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Internet: www.group.bnpparibas.com - **www.economic-research.bnpparibas.com**

Head of publication : Jean Lemierre / Chief editor: William De Vijlder

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