MACRO OUTLOOK

Safe moderation

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In the US, the cautionary approach introduced into our projected growth baseline has not yet been quantitatively incorporated into our forecast, but evidence of weakening consumer spending momentum is accumulating. As a result, we are revising our GDP growth outlook downwards for Q2 and anticipate downside risks for H2.

In the EA, our baseline remains unchanged anticipating that strengthening real incomes, monetary policy easing, and gradual improvement in foreign demand will marginally accelerate the underlying economic pace. However, recent unusual supply and demand trends suggest there is some downside risk to our outlook.

In China, our expectation is for the economy to continue expanding at a rate near its potential, which aligns with the Communist Party's strategic and geopolitical objectives. On the one hand, it fulfils the broader strategic and geopolitical ambitions of the Asian giant; while at the same time, it reflects a more realistic assessment of China's moderated growth potential.

For the third month running, inflation has been on the soft side in the US. Although technical factors or corrective measures likely exaggerated the monthly decline and may partially bounce back in July, we think incoming data remains consistent with our baseline that underlying disinflation continues.

In the EA, core inflation pressures remained persistent, particularly in services. However, our outlook of gradual disinflation remains unchanged, as the resilience in services reflects temporary idiosyncratic effects that we anticipate will diminish as we move into the second half of the year.

In China, June's inflation figures were lower than expected, largely because the seasonal rise in food supply exceeded expectations. Despite this, our baseline projection is broadly unchanged. We remain of the view that China is in a prolonged phase of low inflation as a result of structural reforms by policymakers. Nonetheless, as supply-demand imbalances partially ease in H2, we anticipate that price pressures will build up very gradually.

In line with our macro baseline, we maintain our prediction that the Fed and the ECB will cut rates twice this year, in September and December. In China, the ongoing balancing act between the economy's natural rebound and policymakers' interventionist measures is expected to continue in the near future. The PBoC is likely to maintain its cautious stance as the July Politburo meeting approaches.

GROWTH

US – Under pressure

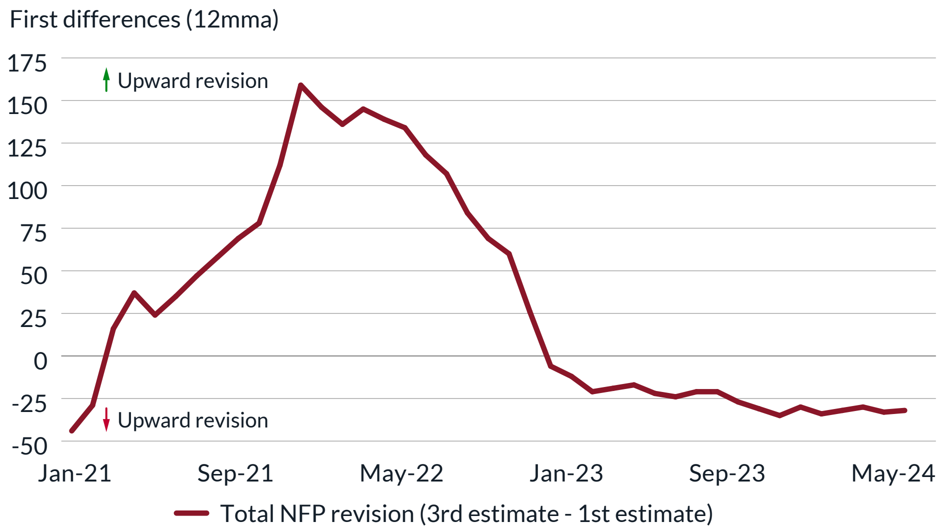
In the US, the cautionary approach introduced into our projected growth baseline has not yet been quantitatively incorporated into our forecast, but evidence of weakening consumer spending momentum is accumulating. As a result, we are revising our GDP growth outlook downwards for Q2 and anticipate downside risks for H2.

Recent data indicates that consumer spending prospects are declining. This is evidenced by the below facts:

1. Services activity lost direction. The ISM services index fell back into recessionary zone in June for the second time in the past three months. Weaknesses were widespread, affecting key subcomponents such as business activity, employment, and new orders. Although some recovery is likely in July, the increased volatility casts a shadow over the outlook for domestic demand.
2. The labour market is at a crossroads. On the one hand, JOLTS data for May suggests the current level of job openings is consistent with a balanced market. However, with key sub-indices such as quits rate, separation rate, hire rate, and openings/unemployed ratio being close to or below pre-pandemic levels, any further declines from these levels will become more alarming. On the other hand, the June non-farm payroll report highlighted two issues. Firstly, the data does not seem particularly reliable, with job creation being repeatedly overestimated and more than 111k jobs initially reported being retracted over time since April. Secondly, the private sector is losing momentum in job creation, including in the manufacturing and services sectors. Over the past two months, non-cyclical and government jobs have seen sustaining job creation. (**Figure 1**)

FIGURE 1

Labor demand is back to pre-COVID norm. Any further declines become alarming

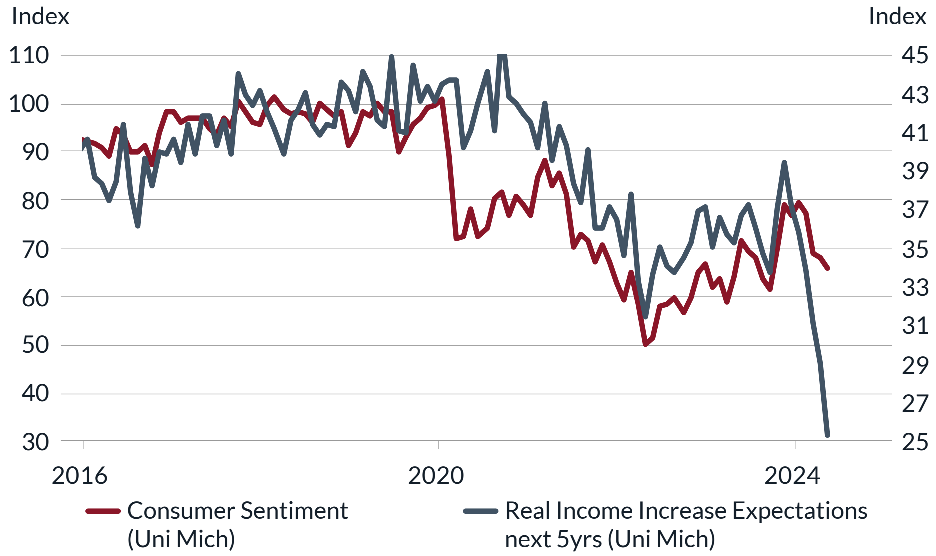


Source: Haver Analytics, ANIMA Research

3. Consumer confidence keeps declining. (**Figure 2**)

FIGURE 2

Consumer prospects continue to weaken



Source: Haver Analytics, ANIMA Research

4. Spending momentum is losing steam across the board. In May, the monthly growth rate of spending for services has dropped to its lowest level since August 2023.

ANIMA baseline. Against this backdrop, we revise down our GDP growth forecast for Q2 to 1.8% q/q SAAR (from 2.1% prior). For Q3-24 we expect 1.4% q/q SAAR (unchanged from previous baseline) and 1.4% q/q SAAR for Q4-24 (unchanged from previous baseline) – consistent with an annual growth rate of 2.3% (from 2.4% prior). (**Table 1**)

EA – Cautiously optimistic

Incoming data for Q2 indicates that growth prospects have slightly cooled following a surprisingly robust Q1. Our baseline remains unchanged anticipating that strengthening real incomes, monetary policy easing, and gradual improvement in foreign demand will marginally accelerate the underlying economic pace. However, recent unusual supply and demand trends suggest there is some downside risk to our outlook.

Challenges persist on the supply side. The composite PMI for June was 1.2 points lower than in May, reflecting a significant 3.2pt drop in manufacturing output. Industrial production in Germany underperformed expectations in May, with widespread contraction across sectors, except for non-durable consumer goods and energy production.

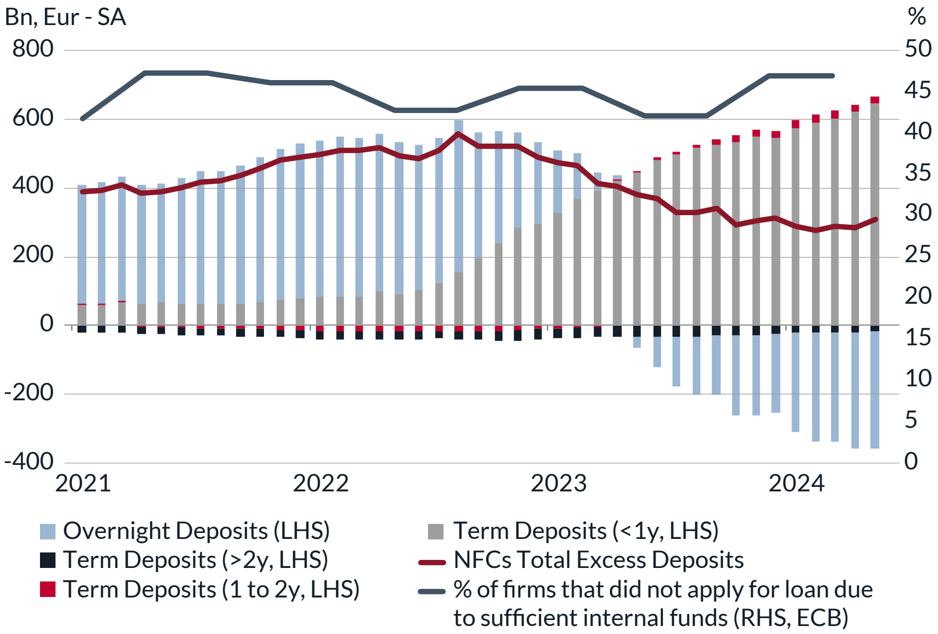
Demand is looking stronger. Retail sales marginally increased in May, and April's figures were revised upwards. Furthermore, monthly consumer spending in France bounced back sharply in May. Overall, spending has shown a modest growth trend in recent months. This is encouraging, as recovering consumer spending is a fundamental driver of our growth outlook.

We expect household demand to remain in the driving seat. The combination of robust wage increases, lower inflation rates, and steady employment growth should contribute to support consumer confidence. Moreover, a buoyant tourism season is expected to boost service sector spending, particularly in peripheral countries.

The labor market continues to show resilience. Employment growth in Q1-24 remained stable for the third consecutive quarter, while in April the unemployment rate decreased to a historic record low of 6.4%. More up to date qualitative indicators consistently suggest sustained net hiring in the service sector with particular strength observed in peripheral economies. Additionally, concerns among households regarding unemployment have eased somewhat. (**Figure 3**)

FIGURE 3

Corporates' balance sheets remain healthy



Source: Haver Analytics, ANIMA Research

Looking ahead, we continue to anticipate a slight acceleration in the underlying pace of the economy. Several favorable factors, such as easing financial conditions and inflation, along with low unemployment, are expected to revive the manufacturing sector and sustain consumer spending. Furthermore, the slowdown caused by the reduced quantity of inventories is anticipated to diminish. Survey data suggests a moderate restocking trend in the coming quarters.

ANIMA's baseline incorporates recent Q2 data revealing a weaker manufacturing sector than anticipated alongside stable consumption. As a result, we are slightly revising down our growth outlook. We now expect growth of 0.2% quarter on quarter for Q2-24 (revised from 0.3% previously), 0.3% quarter on quarter for Q3-24 (revised from 0.4% previously), and 0.4% quarter on quarter for Q4-24 (unchanged from earlier estimates), leading to an annual growth rate of 0.7% (compared to 0.8% previously). (**Table 2**)

China's momentum is expected to reach its lowest point in Q2

Our expectation is for the Chinese economy to continue expanding at a rate near its potential, approximately 5%, which aligns with the Communist Party's strategic and geopolitical objectives. On the one hand, it fulfils the broader strategic and geopolitical ambitions of the Asian giant; while at the same time, it reflects a more realistic assessment of China's moderated growth potential compared to the period from 1980 to 2010.

Q2 is anticipated to reach its lowest annual growth. Therefore, we foresee a slowdown during the second quarter due to weakening supply and demand conditions, as evidenced by a consistent flow of data indicating a temporary reduction in economic momentum.

Following a rise in Q1 and a weakening in Q2, we foresee domestic demand stabilising in the latter half of the year. Confidence indexes have shown a broad moderation in economic momentum within the manufacturing, services, and construction sectors, yet they remain at expansionary levels. At the same time, we expect foreign trade to continue to exceed expectations: exports were stronger than anticipated in the first half of the year, supported by positive trends in exports to G3 countries (U.S., Eurozone, Japan) and a favourable base effect, while imports slowed due to lower inflows of key commodities. Overall, foreign trade is expected to maintain stable momentum in the months ahead.

The housing market remains unchanged: we remain convinced that stabilising the sector will require time. The latest housing policy easing package from May, introduced a fresh 300-billion-yuan refinancing facility to support the purchase of unsold houses for conversion into social housing. Though this is a move in the right direction, it will take time to meaningfully reduce housing inventory and raise house prices, which have been declining since mid-2021. Therefore, we maintain a cautious outlook.

ANIMA baseline. Overall, our baseline scenario remains unchanged: China's economy is projected to expand at a quarterly rate of approximately 5%, maintaining its growth potential throughout 2024. We foresee GDP growth developing as follows: 4.8% q/q in Q2, 5.2% q/q in Q3, and 5.2% q/q in Q4, resulting in an annual growth rate of 5.0%. (**Table 1**)

INFLATION

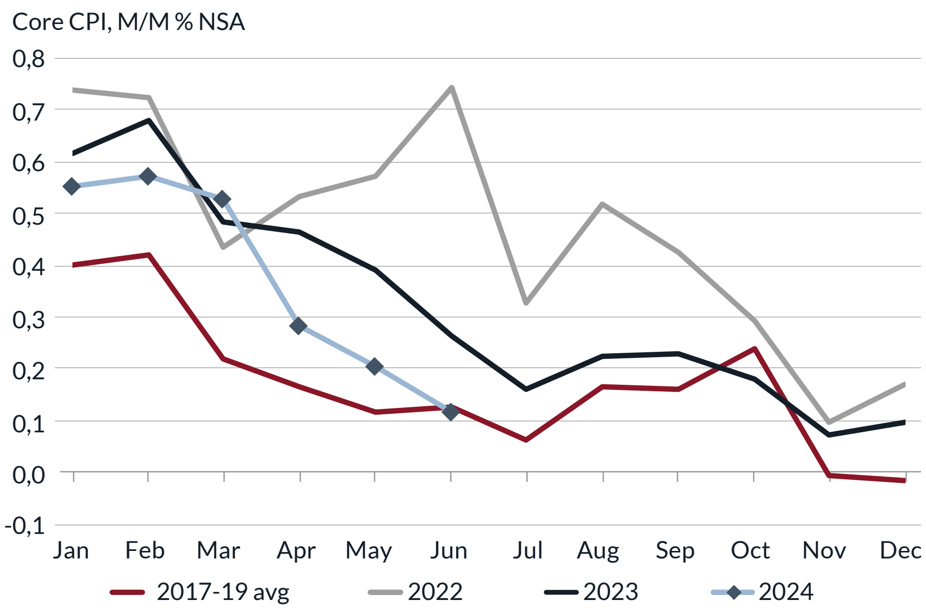
US – CPI is trying to catch a tiger by its tail

For the third month running, CPI inflation has been on the soft side. Although technical factors or corrective measures 1) likely exaggerated the monthly decline and 2) could partially bounce back in July, we think incoming data remains consistent with our baseline that underlying disinflation continues.

For the third consecutive month, CPI inflation was subdued. In June, headline momentum turned negative (-0.1) for the first time since July 2022, while core momentum was 0.1%, 0.1pp short of the consensus forecast and 0.2pp lower than in May. Core-level weakness was widespread as outlined below:

1. Core goods experienced a -0.1% m/m decline. Excluding the decrease in used car prices (-1.5% m/m), core goods prices were broadly flat, in line with the pre-COVID norm. We forecast core goods price momentum to stay around the pre-COVID average in the coming months, as suggested by forward-looking indicators like manufacturing PPI, core goods import prices and used cars prices. (**Figure 4**)

FIGURE 4
Inflation's underlying momentum heading in the right direction

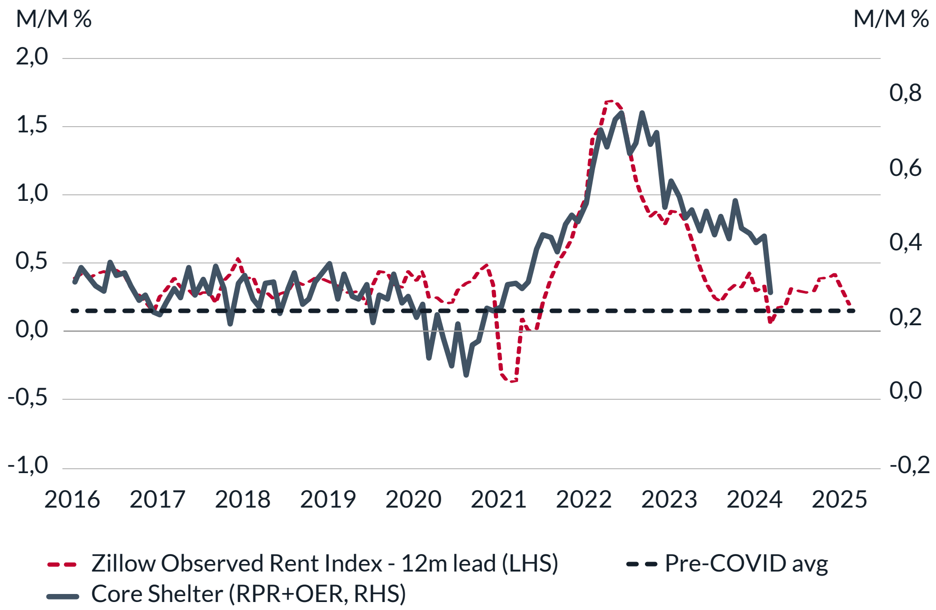


Source: Haver Analytics, ANIMA Research

2. Shelter prices dropped 0.2pp to 0.2%. The decrease was distributed across the main components. Core shelter (RPR+OER) reverted to the pre-COVID norm (0.26% and 0.28% m/m); lodging away from home decreased by -2.0%. Despite the monthly decline being exaggerated by volatile components (hotels) and a correction of the abnormal rise in OER in the NY district in May, the data indicates that core shelter prices could ease further, in line with market data indications. (**Figure 5**)

FIGURE 5

Shelter prices: more easing ahead



Source: Haver Analytics, ANIMA Research

3. "Supercore" prices showed no change in momentum for the second consecutive period. This is despite motor vehicle insurance partially recovering (+0.9%) from the sharp decline seen in May (-0.11%). Several items sensitive to macroeconomic conditions and reopening, such as lodging away, airfares, and food away from home, showed easing trends, with some falling well below pre-COVID levels.

ANIMA baseline. For Q3-24 we expect 2.8/3.2% y/y (vs 2.9/3.4% prior), for Q4-24 we project 2.8/3.1% y/y (vs 2.9/3.3% prior) - consistent with an annual rate for 2024 at 3.0/3.4% (vs 3.1/3.5%). (**Table 2**)

EA – Core slowdown remains gradual and steady

In June, core inflation pressures remained persistent, particularly in services. However, our outlook of gradual disinflation remains unchanged, as the resilience in services reflects temporary idiosyncratic effects that we anticipate will diminish as we move into the second half of the year.

Positive headline. June inflation meets expectations led by declines in energy and food prices. Looking forward, recent oil price hikes may introduce volatility in energy inflation, while upstream price indicators for food suggest continued easing.

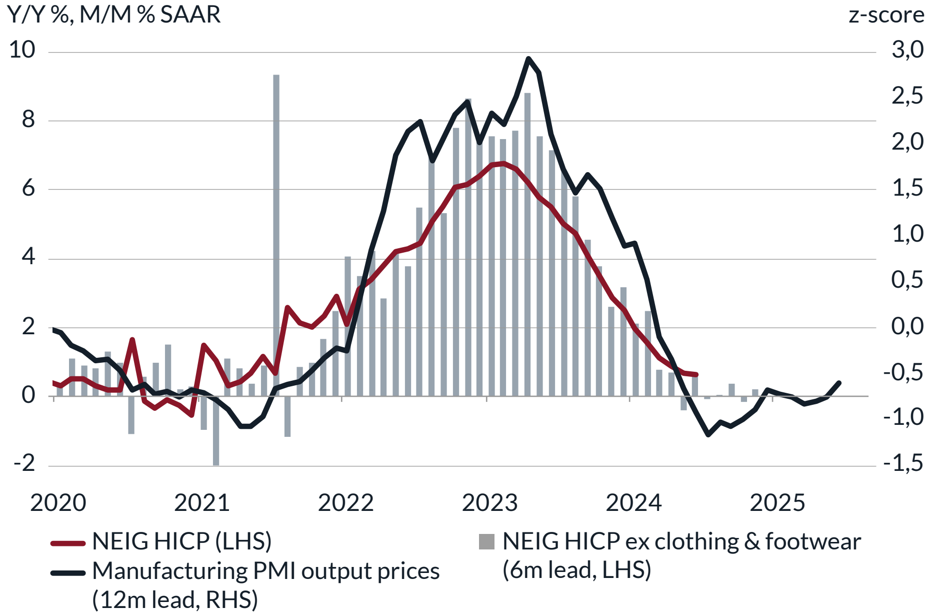
Core inflation showed no change in June, highlighting persistent underlying pressures.

Nevertheless, **our core baseline remains unchanged**, supported by the following reasons:

1. **The tailwind for core goods (NEIG) is diminishing, without any signs of upward pressure.** In June, core goods inflation remained relatively stable. Tradable goods had benefited from the pass-through effects of earlier improvements in supply chains and energy prices. This trend has resulted in NEIG prices decreasing from a peak of 6.7% y/y in Q1-23 to 0.7% y/y in June 2024. We anticipate these favorable conditions to dissipate throughout the summer, supported by stabilizing indicators such as manufacturing output prices and supplier delivery times. Consequently, our expectation is for core goods inflation to persist at current low levels in H2-24. (**Figure 6**)

FIGURE 6

Core goods tailwinds fade



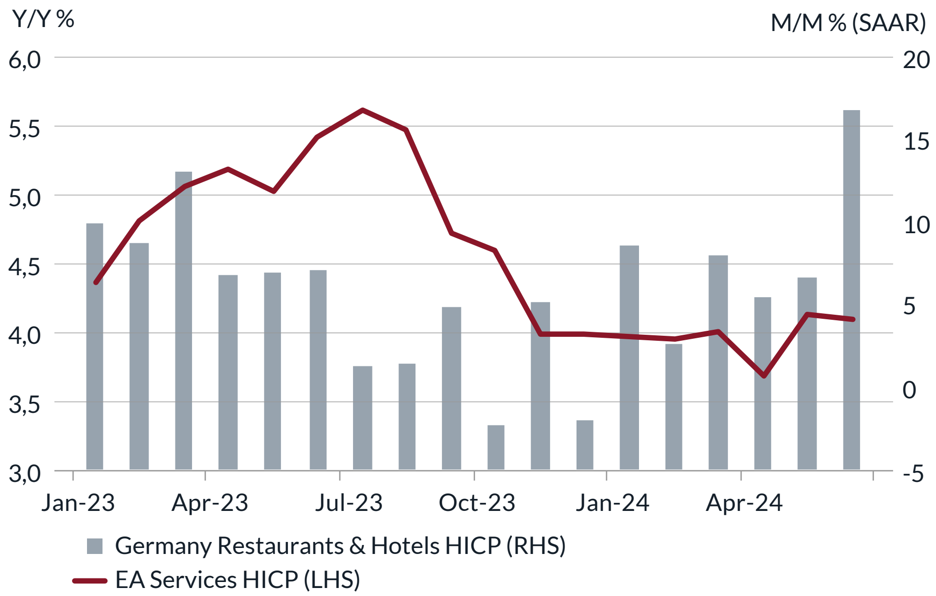
Source: Haver Analytics, ANIMA Research

2. **Services inflation on steroids.** In June, services inflation remained stable at 4.1% y/y, the same as in May. However, we attribute June's persistent services inflation to idiosyncratic effects. More volatile items like airfares, as well as components linked to the Euro 2024 Championship in Germany (such as restaurants, hotels, and domestic package holidays), were significant contributors. Similarly, the upcoming Olympic Games in France in July might cause further volatility. (**Figure 7**)

Overall, the downward trend remains. Beyond June, we expect a continued, albeit modest, fall in core prices. We forecast another 0.1pp decline in core inflation in July (to 2.8%), which should then continue to ease, reaching 2.5% y/y by the end of the year. The reduction in services pressures is likely to be more sustained than in goods, albeit at a slower rate. We foresee a gradual decline in services inflation throughout the year, aided by slower wage growth. Furthermore, services inflation has been impacted by the passthrough of past energy cost reductions, which we expect to continue. Indeed, recent supply-side soft data on price pressures (PMIs/EC) is consistent with cooling inflation in services, suggesting a gradual slowdown ahead.

FIGURE 7

Temporary/idiosyncratic effects keep supporting services inflation



Source: Haver Analytics, ANIMA Research

The wages-profits-productivity nexus is loosening. The latest data shows that profit margins are normalizing and absorbing higher unit labor costs. Additionally, leading indicators on wage dynamics indicate a slowdown in the coming quarters.

ANIMA baseline. We revised our headline profile slightly upwards due to the recent rise in oil prices, while the core remains largely unchanged. More specifically, we project headline/core HICP at 2.4/2.7% in Q3-24 (previously 2.3/2.7%) and 2.3/2.5% y/y in Q4-24 (previously 2.2/2.5%) - consistent with an annual growth rate for 2024 of 2.4/2.8% (compared to 2.5%/2.8% in ECB projections). (**Table 2**)

China – Balancing out

June's inflation figures were lower than expected, largely because the seasonal rise in food supply exceeded expectations. Despite this, our baseline projection is broadly unchanged. We remain of the view that China is in a prolonged phase of low inflation as a result of structural reforms by policymakers. Nonetheless, as supply-demand imbalances partially ease in H2, we anticipate that price pressures will build up very gradually.

Inflation unexpectedly dipped in June. The headline inflation rate dropped more than forecasted to 0.2% year-on-year from 0.3% year-on-year, thanks to weak food prices resulting from an increase in supply. At the same time, core inflation stayed the same as service prices remained flat.

Inflation averaged 0.1% y/y in H1 due to weak momentum. Consumer prices remained flat in the first quarter; however, inflation picked up pace sequentially in the second quarter. This emerging inflationary trend is primarily driven by the turnaround in the Pork Cycle, with pricing hitting its lowest point at the end of 2023.

We foresee food prices continuing to rise at least through the end of the summer, sustaining the overall level of headline inflation.

Core inflation was flat in the first half of the year. Core prices stayed nearly unchanged at around 0.7%, the same level seen since mid-2023 due to weak service inflation dynamics after the late-2023 surge.

On the other hand, producer prices also continued to slowly reflate through H1. We remain confident that the deflationary conditions China has been experiencing since January 2023 are gradually fading. However, significant supply-demand imbalances will continue to put a strain on consumer prices in 2024.

Prices will rise, but the recovery will be modest. We believe China is experiencing a prolonged period of low inflation due to structural changes implemented by policymakers. In the second half of the year, as the supply-demand imbalance begins to diminish, we anticipate price pressures to gradually increase, although inflation will stay well below the central bank's 3% target for 2024.

ANIMA baseline. Against this backdrop, we have modestly revised our baseline downward: we now predict headline inflation will evolve as follows: 0.3% quarter-on-quarter in Q2, 0.6% quarter-on-quarter in Q3 (down from 0.7% year-on-year) and 1.0% quarter-on-quarter in Q4 (down from 1.1% quarter-on-quarter). (**Table 2**)

TABLE 1 AND 2

ANIMA's growth and core inflation baseline

Growth	US Q/Q %, SAAR	EA Q/Q %	China Y/Y %
Q4 23	3,2%	0,0%	5,2%
2023	**2,5%**	**0,5%**	**5,2%**
Q1 24	1,4% ↑	0,3%	5,3%
Q2 24	1,8% ↓	0,2% ↓	4,7%
Q3 24	1,4%	0,3% ↓	5,2%
Q4 24	1,4%	0,4%	5,2%
2024	**2,3%**	**0,7%** ↓	**5,1%**

Core Inflation	US CPI Y/Y %	US PCE Y/Y %	EA Y/Y %	China Y/Y %
Q4 23	4,0%	3,2%	3,7%	-0,3%
2023	**4,8%**	**4,1%**	**4,9%**	**0,2%**
Q1 24	3,8%	2,9%	3,1%	0,0%
Q2 24	3,4% ↓	2,7%	2,8% ↑	0,3%
Q3 24	3,2% ↓	2,6%	2,7%	0,7%
Q4 24	3,1% ↓	2,6%	2,5%	1,2%
2024	**3,4%** ↓	**2,7%**	**2,8%** ↑	0,6%

Source: Haver Analytics, ANIMA Research

MONETARY POLICY

Fed – Nearing the target

In line with our macroeconomic forecast indicating that inflation, including the ongoing "supercore" momentum, will keep slowing down, we maintain our prediction that the Fed will cut rates twice this year, in September and December.

Taking a cautious approach, we foresee the Fed will maintain its current cautious stance at the upcoming July meeting.

Risk management considerations will dominate. We believe the FOMC still vividly remembers the unexpected rise in inflation witnessed in Q1. Therefore, additional evidence indicating a deceleration in private consumption and "supercore" inflation is likely necessary before making any decisions.

And yet it moves. Nevertheless, as the macroeconomic outlook aligns more closely with reduced pressures for aggressive monetary policy, we anticipate the Fed will highlight a more balanced view of dual risks.

Our baseline is unchanged. Consistent with our macro-economic outlook that inflation, including "supercore" momentum will continue to ease, we maintain our expectation that the Fed will cut rates twice this year, in September and December. We expect the Fed to indicate its intention to act at the upcoming Jackson Hole Symposium (24-26 Aug).

ECB – Viewing the glass half empty

Our expectation remains that the ECB will decrease policy rates by 25 basis points at both the September and December meetings.

Our baseline remains unchanged. We continue to expect the ECB to cut policy rates by 25bp at the September and December meetings.

Risks surrounding our forecasts are finely balanced. On the downside, incoming data suggests that Q2 GDP growth is likely to be weaker (0.2% Q/Q) than the ECB's forecasts (0.4%). On the upside, core inflation continues to move sideways, supported by services inflation, while the labour market remains robust.

"No Fed! No party!". Against this backdrop, and with the Fed continuing to refrain from reducing policy rates, we believe the ECB will adopt a wait-and-see approach in July, consistent with its cautious messaging at the Sintra forum.

Waiting for a sign. Nevertheless, in line with our forecast that the Fed will signal the possibility of the first rate cut at the upcoming Jackson Hole Symposium (24-26 Aug), we anticipate the ECB to make another move in September (12 September), even though the Fed won't have started easing yet, as their FOMC meeting is scheduled a week later (18 September).

PBOC – Watching from the sidelines

In China, the ongoing balancing act between the economy's natural rebound and policymakers' interventionist measures is expected to continue in the near future. The PBoC is likely to maintain its cautious stance as the July Politburo meeting approaches.

Policymakers' attention remains on the housing sector. In Q2, policymakers approved new measures aimed at gradually reducing the stock of unsold properties held by developers. Despite this, the journey towards real estate recovery continues to be challenging without substantial interventions. This aligns with our longstanding expectation that authorities will continue with their incremental approach to bolstering economic momentum this year.

Our PBoC outlook remains unchanged. We project monetary policy will stay neutral this year, affirming our expectation that the central bank will reduce the reserve requirement ratio by 50 basis points and the benchmark monetary rate by 10 basis points by the close of the year. Risks persist in favouring a more aggressive tightening of stimulus once the Fed initiates its expansionary cycle.

In July, the Politburo is expected to prioritise long-term opportunities over short-term concerns, particularly those linked to the housing sector. At the upcoming Politburo meeting, we anticipate Xi Jinping's attention will pivot towards enduring priorities like technological advancement and securing global economic leadership, which will become China's strategic focal points with significant investments planned from 2025 onwards.