

Global economy

Economic forecasts revised up

Consensus forecasts for developed world GDP growth in 2010 were revised up again in September, improving from the height of pessimism seen back in April and May. Upward revisions have reflected an economic upturn that has surprised almost all economists in terms of both the earlier than expected turning point and the strength of the rebound.

The Global PMI, for example, compiled by Markit for JPMorgan and based on PMI surveys covering both manufacturing and services, shows that global output growth has rebounded in a clear V-shape from the record low seen last November, rising in September at a pace last seen at the end of 2007.

However, although improving, forecasts for 2010 – especially for developed economies – remain lacklustre. The consensus forecast among economists polled by Reuters for Eurozone GDP growth in 2010, for example, has risen from 0.4% in the early summer to 1.0% in September. For the UK, the 2010 forecast has risen from 0.3% in May to 1.1% in September. Less marked revisions have been evident for Japan and the US. Japan is now expected to grow by 1.3% in September against a forecast of 0.9% in May, whereas the annualised rate of growth in the US at the end of 2010 is expected to now reach 2.7% against a

Chart 1: Global GDP

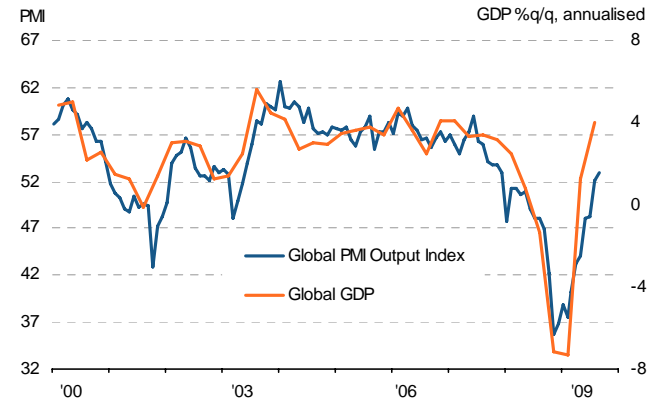
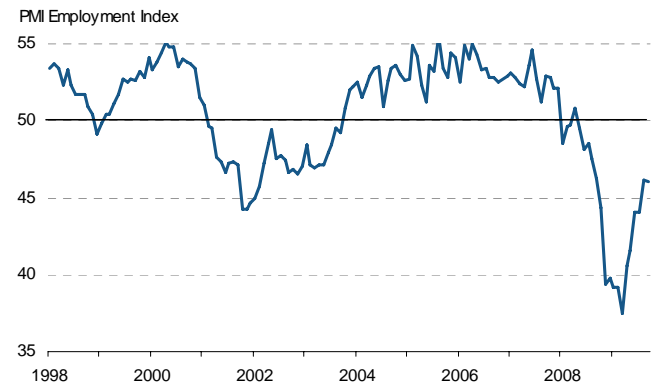


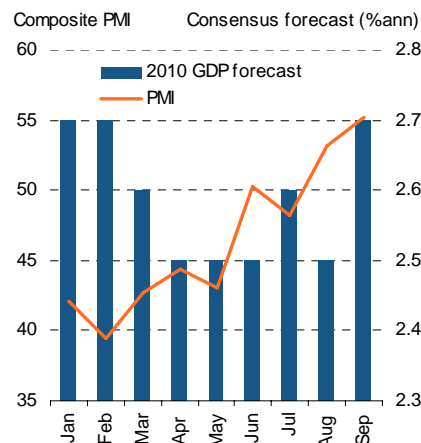
Chart 2: Global employment



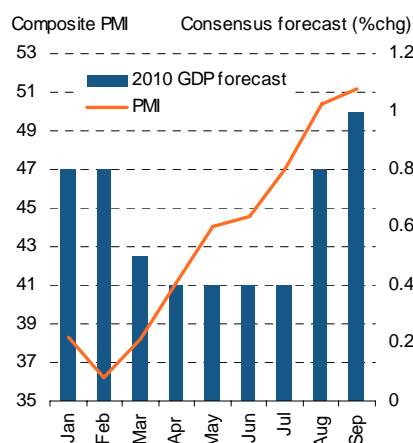
Sources: Markit, ISM, JPMorgan

Consensus forecasts for GDP growth in 2010 and Composite PMI Trends

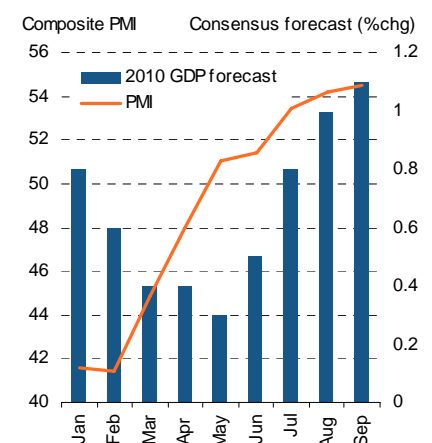
United States



Eurozone



United Kingdom



Sources: Markit, Thomson Reuters, ISM.

prediction of 2.5% in previous months.

There are many factors which explain why these forecasts are so low, including the following:

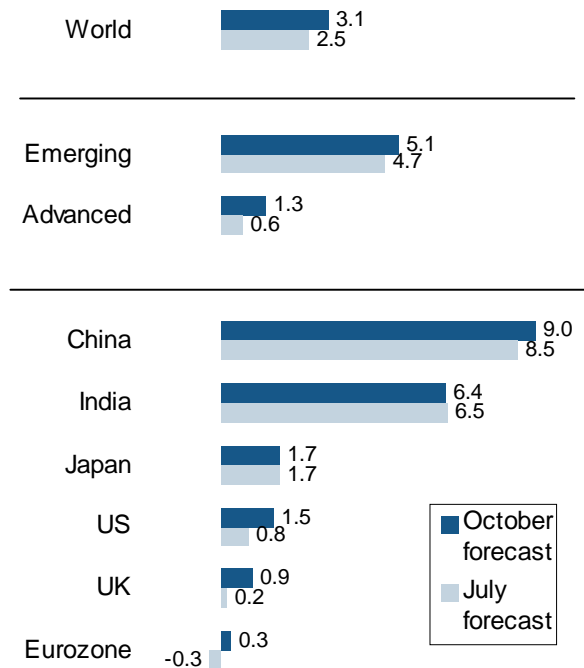
- companies and households are expected to continue to wind down debt levels incurred as a result of years of excess credit.
- stimulus measures are set to have a diminishing effect, especially as governments seek to balance their own books with higher taxes and spending cuts.
- the initial boost to growth generated by the restocking of warehouses will fade as we move into next year.
- employment continues to fall and, although the stabilisation of global labour markets by the end of 2009 remains a possibility according to PMI data (see the www.markit.com commentary section), unemployment *levels* look set to remain high, with jobless rates likely to reach double digits in the US and Eurozone. High unemployment means weak household expenditure growth, as well as a reduced tax-take and higher social security spending.

The stabilisation of labour markets in developed countries such as the US and euro nations is widely considered vital for a sustained global recovery. But the Global PMI Employment Index and US non-farm payrolls both disappointed in September. This is most likely a hiccup on the road to stabilisation by the year end, but it also represents a reminder that the recovery remains fragile and the path is likely to be bumpy. Interest rates are therefore generally expected to remain at historic lows in the US, UK and Eurozone until well into next year as a result.

It's a different story for emerging markets, however, which look set to enjoy stronger growth than developed nations in 2010. September saw the launch of the Emerging Markets Index, a PMI-based indicator produced by Markit for HSBC. The EMI summarised the outperformance of emerging market economic growth so far relative to developed countries.

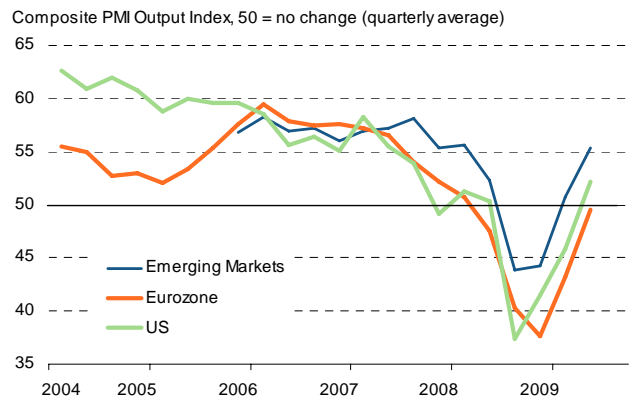
The latest – upwardly revised – GDP forecasts from the International Monetary Fund (IMF) reflect this outperformance. Advanced economies are only expected to grow by 1.3% next year, while emerging markets are set to expand by 5.1%. A 1.5% increase in US GDP contrasts with a 9.0% rise in China.

Chart 3: IMF 2010 GDP Forecasts



Source: International Monetary Fund.

Chart 4: All-Sector PMI Surveys: Output Index



The recent hiking of interest rates by the Reserve Bank of Australia, the first G20 country to hike, contrasts with the downbeat rhetoric from central banks such as the Bank of England, Federal Reserve and European Central Bank, and to a large extent reflects the country's close ties with Asian emerging markets. The hike serves to illustrate how economic trends between the developed and emerging markets are likely to diverge over the next year, with stronger growth and policy tightening in emerging markets (and those developed economies with especially close links to emerging markets) contrasting with low growth and loose policy in the developed world.

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